Allbirds
Q2 2024 Earnings Call Prepared Remarks
Wednesday, August 7, 2024
2:00 p.m. PT

Christine Greany, Investor Relations:

Good afternoon, everyone and thank you for joining us. With me on the call today are Joe Vernachio, CEO, and Annie Mitchell, CFO.

Before we start, I'd like to remind you that we will make certain statements today that are forward-looking within the meaning of the federal securities laws, including statements about our financial outlook, including cash flow and adjusted EBITDA expectations, 2024 full year and Q3 guidance targets, impact and duration of external headwinds, strategic transformation plan and related planned efforts, go-to-market strategy, transitions to a distributor model in certain international markets, anticipated distributor model arrangements, expected profitability, cost savings targets, gross margin estimates, product plan timelines and expectations, marketing strategy and investment, product and brand strategy, and other matters referenced in our earnings release issued today.

These forward-looking statements involve a number of risks and uncertainties that could cause actual results to differ materially. Please also note that these forward-looking statements reflect our opinions only as of the date of this call, and we undertake no obligation to revise any statements to reflect changes that occur after this call. Please refer to our SEC filings, including our Quarterly Report on Form 10-Q for the quarter ended March 31, 2024, for a more detailed description of the risk factors that may affect our results.

Also, during this call, we will discuss non-GAAP financial measures that adjust our GAAP results to eliminate the impact of certain items. These non-GAAP items should be used in addition to and not as a substitute for any GAAP results. You will find additional information regarding these non-GAAP financial measures, and a reconciliation of these non-GAAP measures to their most directly comparable GAAP measures to the extent reasonably available, in today's earnings release.

Now, I'll turn the call over to Joe to begin the formal remarks.

Joe Vernachio, CEO:

Hello everyone and thanks for joining us today.

We are pleased to report another quarter of strong execution and performance in line with our expectations. Our Q2 results reflect continuing progress both operationally and financially as we set the business on a path to return to top line growth in 2025.

We are on a trajectory to reignite our product and brand. Before we talk about this next chapter, let's take a look at what we've accomplished over the past 18 months. Since the announcement of our strategic transformation plan, we have reset the business, establishing the foundation for the next phase of Allbirds' journey. Importantly, we have demonstrated our ability to formulate a plan, and then execute and deliver on that plan. I'd like to provide a quick recap of our actions since March of 2023.

- Starting with retail stores. We have closed 14 underperforming US locations to bias toward a smaller physical footprint that better serves our footwear product strategy and advances our goal to build a profitable retail fleet.
- Next is International. We have successfully transitioned to a distributor model in the five targeted regions where we were previously selling direct. We also opened four new regions, where we had an opportunity to partner with leading distributors and leverage our strong brand affinity. We believe this distributor model positions us to achieve profitable and scalable growth internationally.
- Looking at cost of goods. Our shift to a new factory along with material optimization is enabling us to capture significant COGS savings, driving longer term gross margin expansion.
- We're also generating OpEx savings. We have rebuilt the wireframe of the Company and we're operating with greater overall efficiency. We believe this positions us to drive long-term profitability as we scale.
- And turning to our balance sheet, we cut our inventory by more than half and drove improvement in working capital in 2023 versus prior year. We entered 2024 in a very healthy position and we're carefully managing inventory going forward.

Against that backdrop, we are now prioritizing three main focus areas: Making Great Product, Telling Compelling Stories, and Providing Customers with an Engaging Shopping Experience.

Creating great product is paramount to our long-term success. Getting the product engine ignited has been among my highest priorities since taking over the product reins last November. After bringing in a new Chief Design Officer in December, we built a roadmap to evolve our go-forward product and Brand strategy.

The first critical step was to edit the line to more closely reflect our evolving strategy. As a result, we have limited the number of recent product introductions to just a few launches - all of which have performed well thus far and demonstrate that our customers are asking for newness from Allbirds. The Wool Runner 2, Tree Runner Go and Canvas Piper have all met with positive consumer response. Next up is the launch of our Tree Glider in just a few weeks.

We then set out to inject newness as quickly as possible. Using our existing tooling, we swiftly introduced new colors and materials into the product line, which is allowing us to infuse freshness into our offerings for the second half of 2024 and the first half of 2025. You'll first see this reflected in the fall when we plan to introduce corduroy as well as more rugged versions of our water resistant collection.

Looking ahead to our Fall '25 and Spring '26 collections, we are creating these product lines from the ground up, with an elevated design and product architecture that emphasizes Allbirds' lifestyle brand positioning. We are in the intensive phase of designing and developing a robust line of products that will begin to launch in the second half of next year. We are very motivated by the progress we are seeing with each sample that arrives from our development center. We have more than 10 new product launches planned across these two seasons. The collections will not only enhance our product range but also reinforce our dedication to quality, comfort, style, and sustainability.

In preparation for our new product launches in mid-2025, we will be telling compelling marketing stories by utilizing a new brand narrative called “Allbirds by Nature”. This narrative celebrates the duality of the word "nature," connecting our design philosophy inspired by the natural world while also encouraging people to embrace their innate and unique human nature.

Allbirds by Nature will enable us to inspire and engage with consumers on a wide range of topics, from product benefits to universal human experiences. For example, "Breathable by Nature" will highlight our use of natural and recycled materials and knit constructions that offer exceptional breathability. "Comfortable by Nature" will showcase the comfort of our shoes while also encouraging people to feel comfortable in their own skin.

To amplify this narrative, we are prioritizing increased marketing investments starting in the second half of the year, with a phased ramp-up planned to continue throughout 2025. More on this from Annie shortly. Our efforts will be centered around driving awareness through an upper funnel strategy that tells the Allbirds brand and product story in a fresh, engaging, and consistent manner. Specifically, our initiatives are designed to convey our brand message and product attributes through the lenses of rational, emotional, and cultural connections. By incorporating these elements, we can create a richer, more engaging narrative that resonates with the values and aspirations of the Allbirds consumer.

As we bring fresh, updated product to the market and amplify our marketing, Providing Customers with an Engaging Shopping Experience is our other key priority. We are enhancing the in-store consumer journey, starting with an improved assortment presentation, wayfinding, and floor displays. In 2025, we plan to take further steps to enhance the consumer experience by making both our stores and website easier and more enjoyable to shop. You will hear much more about this in the quarters to come.

As we embark on the next phase of our journey, our track record of execution over the past 18 months gives us confidence in our ability to advance our three main focus areas of Making Great Product, Telling Compelling Stories and Providing Customers with an Engaging Shopping Experience. We have bolstered the organization with key hires and internal promotions, creating a team that is coalesced around a clear path forward. We're continuing to operate with urgency and remain committed to building shareholder value over the long-term. We appreciate your support and look forward to keeping you updated on our progress.

Now I'll turn the call over to Annie to discuss the financials.

Annie Mitchell, CFO:

Thanks Joe, and good afternoon everyone. We are pleased to deliver another quarter of performance within or exceeding our expectations, reflecting consistent execution by our teams. Net revenue came in within our guidance range and adjusted EBITDA exceeded the expectations we outlined last quarter. Notably, we delivered another quarter of gross margin expansion, and a 25% year over year improvement in adjusted EBITDA.

Q2 revenue totaled $52 million. The results are primarily attributable to lower unit sales partially offset by higher ASPs within our Direct business. The return to full price selling is a critical component of our long term strategy, however, it is creating a near-term headwind to sales. Additionally, revenue was impacted by our international distributor transitions and planned retail store closures.

While the transition to a distributor model and the closure of retail doors are reducing our topline and the associated gross profit dollars, these actions are done with intention, as they support our cost management and efficiency efforts, and are offset by savings in marketing and SG&A, which I will discuss in a moment.

Second quarter gross margin improved to 50.5%, up 360 basis points sequentially and 770 basis points versus the prior year. The year-over-year expansion is attributable to the continued benefit from a healthier inventory position, lower freight costs, and lower promotional activity in the direct business, as well as COGS savings captured from our factory shift and materials innovation. Year over year improvement in gross margin is expected to continue in the second half of 2024, although not at the same magnitude that we've seen year to date. We continue to expect Q3 and Q4 gross margin to be in the mid-40s, reflecting the combination of retail store closures, transitions to international distributors and planned promotional activity around the holidays.

Looking at SG&A, our teams did great work controlling costs in the quarter. SG&A dollars, excluding stock-based compensation and depreciation and amortization, totaled $28 million, down 22% versus the prior year. The decrease can primarily be traced to lower personnel expenses and occupancy costs. This was partially offset by costs associated with our retail store closures, as planned. During the quarter, we closed 10 US stores, followed by 1 additional closure subsequent to quarter-end. This brings us to 14 stores year-to-date, putting us at the high end of our plan to close 10-15 US stores in 2024, and we continue to evaluate opportunities to optimize our retail fleet. In connection with these store closures, plus one internationally, we incurred one-time cash charges of $3 million in Q2.

Q2 marketing spend totaled $12 million, down 6% year over year. As Joe mentioned, in the second half of 2024, we plan to increase our marketing investment to begin driving awareness through top of funnel spend in the lead up to our 2025 product introductions. While total marketing dollars are expected to be down on a year over year basis in Q3 and Q4, we anticipate that our US spend will be up. Recall that under our new distributor model, in-region marketing costs effectively go to zero following the transitions. With five regions now transitioned to distributors, the year-over-year savings are expected to more than offset the investments we're planning to make in our remaining direct markets…the US, UK and EU.

Now, turning to the balance sheet and cash flow. The company is in strong financial condition with a solid balance sheet. Inventories at the end of Q2 remained healthy, totaling $54 million dollars. That's down 42% year over year and down 7% from the end of 2023.

We closed the second quarter with $87 million of cash and cash equivalents and no outstanding borrowings under our $50 million revolver. Operating cash use was $16 million. That's down sequentially from Q1, reflecting our seasonal working capital cadence, and up versus the prior year when inventory was a material source of cash due to our clean up efforts throughout 2023.

Our three focus areas of Making Great Product, Telling Compelling Stories, and Providing Customers with an Engaging Shopping Experience, combined with other strategic actions we are taking this year, are positioning the business to return to top line growth in 2025 and set us up to deliver profitability in future years.

A foundational step in our plan to restore growth is the return to full price selling. We are committed to this model following a promotional 2023 and pleased to see the benefits begin to manifest - which is reflected in our year-to-date gross margin expansion.

Looking at other key initiatives, as I just noted, we've taken swift action related to our US retail fleet. And on the international front, we continue to partner with distributors in new regions, with Benelux and Scandinavia signed this quarter. We have transitioned the majority of our existing regions to a distributor model. During the second quarter, we completed transitions in Japan and Australasia, and last week, we announced the transition of China, an important region for our brand. We're pleased to be working with leading distributors who have both regional and industry expertise to help us extend our brand reach and position us to achieve profitable and scalable growth internationally.

Moving to guidance…we are reiterating our full year sales outlook, and based on performance year to date, we are increasing our gross margin range by 100 basis points and bringing up the bottom end of our Adjusted EBITDA range by $3 million.

Full year net revenue is expected to be in the range of $190 to $210 million dollars. The full year impact from our retail store closures and international transitions is now expected to be in the range of $25 to $30 million versus our prior expectation of $32 to $37 million. Let me unpack that for you.

- The impact from retail is higher than anticipated due to the speed at which we've been able to exit leases.

- The impact from international transitions is lower than expected due to the timing of this year's transitions, combined with slightly higher initial orders from our distributors.

By geographical market, full year 2024 US net revenue is expected to be in the range of $150 to $165 million dollars and includes approximately $10 to $12 million of impact resulting from our US store closures. Full year international net revenue is expected to be between $40 and $45 million and includes approximately $15 to $18 million of impact resulting from our transition to a distributor model in certain international markets.

Gross margin is now expected to be in the range of 43 to 46 percent, up from prior guidance of 42 to 45 percent. Key drivers include reduced promotional intensity compared to 2023, lower inbound and outbound freight and initial savings from our factory shift to Vietnam and materials innovation.

Full year Adjusted EBITDA loss is now expected to be in the range of $75 to $63 million which compares to prior guidance for a loss of $78 to $63 million. While there are a number of dynamics at play on the top line, we've remained focused on improving the bottom line and you can see the results of that this year.

Turning now to Q3 guidance, third quarter net revenue is expected to be between $40 and $43 million dollars. This comprises US revenue in the range of $33 to $35 million and international revenue in the range of $7 to $8 million.

Q3 adjusted EBITDA loss is expected to be between $19 and $16 million.

We're pleased with our first half performance and proud of the way our teams are executing as we enter the next phase of our journey.

With that, I'll ask the operator to open the call to questions.