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Q3 2023 Allbirds Inc Earnings Call

EVENT DATE/TIME: NOVEMBER 08, 2023 / 10:00PM GMT

CORPORATE PARTICIPANTS

Christine Greany *The Blueshirt Group, LLC - IR*
Joey Zwillinger *Allbirds, Inc. - CEO*
Annie Mitchell *Allbirds, Inc. - CFO*

CONFERENCE CALL PARTICIPANTS

Bob Drbul *Guggenheim Securities LLC - Analyst*
Alex Straton *Morgan Stanley & Co LLC - Analyst*
Janine Stichter *BTIG, LLC - Analyst*
Cristina Fernández *Telsey Advisory Group - Analyst*
Mark Altschwager *Robert W. Baird & Co. - Analyst*
Tom Nikic *Wedbush Securities Inc. - Analyst*
Krista Zuber *TD Cowen Inc. - Analyst*

PRESENTATION

Operator

Good afternoon, everyone, and welcome to the Allbirds third-quarter 2023 earnings call. (Operator Instructions) This conference call is being recorded and may not be reproduced in whole or in part without written permission from the company. Now I'll turn it over to Christine Greany from The Blueshirt Group. Please go ahead.

Christine Greany ***The Blueshirt Group, LLC - IR***

Good afternoon, everyone, and thank you for joining us. With me on the call today are Joey Zwillinger, CEO; and Annie Mitchell, Chief Financial Officer.

Before we start, I'd like to remind you 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, Q4 guidance targets, impact, and duration of external headwinds, simplification initiatives, strategic transformation plan, and related planned efforts, go to market strategy plan to transition to a distributor model, and certain international markets, anticipated distributor model arrangements, expected profitability, cost savings targets, gross margin estimates, product plans and expectations, third-party partnership strategy, marketing 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 June 30, 2023, 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 adjusts 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 Joey to begin the formal remarks.

Joey Zwillinger ***Allbirds, Inc. - CEO***

Thanks, Christine. Good afternoon, everyone, and welcome. We delivered Q3 results in line with the expectations we provided in August as well as another quarter of solid progress under our strategic transformation plan. Our flock is executing well across the board, which we believe is setting up Allbirds to achieve sustainable and profitable growth, and in doing so create durable shareholder value.

During the third quarter we achieved another set of material proof points that are driving the business forward and positioning the company to hit our 2025 targets with positive full-year adjusted EBITDA and positive cash flow.

First, we made significant progress against cleaning up inventory, ending the quarter with just under $80 million of inventory on the balance sheet that represents a sequential decline of 14% from Q2 and a year-over-year decline of 37%.

This is notable given the cautious consumer spending environment and makes us confident that we can effectively clean up the marketplace to enable us to focus on our fresh and innovative new product as we entered 2024 with plans to drive resonance with the consumer through a better product mix and key upgrades to our core franchises.

Another critical metric we use to measure our progress during this transformational year is cash. We closed Q3 with $132 million, reflecting minimal operating cash use of $5 million in the quarter, which was required to meet our seasonal working capital needs leading up to holiday.

Next, we captured savings from our strategic sourcing efforts, keeping us on track to achieve the upper end of our cost of goods sold, savings targets of approximately $20 million to $25 million versus 2022 on a volume-neutral basis. We also continue to drive towards our $15 million to $20 million G&A savings targets with notable progress made via our international transitions.

While working down inventory, we also kept things fresh for our consumer with the launch of our updated Courier and the Vista Racer. These two models are really the final chapter of product that we had developed pre-transformation. We decided to keep these in the line but buy them tight and for only a limited timeframe to drive freshness in a period where we knew our primary intent would be to work down inventory.

The Wool Runner 2 that dropped last week is more aligned with the focus for the next generation of product from Allbirds. This fresh take on our original icon features new innovations and upgrades, including improved comfort, a more durable upper and a streamlined aesthetic. And the launch is supported by a marketing campaign aimed at connecting with our core consumers in a far more resonant way.

We're thrilled with the step change this represents, and it validates the strategy we have for product, given that after just a few days of selling, the Wool Runner 2 is our highest sales velocity launch of the year. We look forward to bringing more innovation like this to the market in 2024.

As we approach another holiday selling season with consumers exercising caution around spending, we're prepared for an early and highly promotional holiday period industry-wide and prioritize getting inventory to a healthy position in early 2024 with an elevated pace of unit sales through 2023.

We intend to remain competitive on price with reduced marketing spend. In fact, Q4 will mark our fourth consecutive quarter of moderated marketing spend, which is expected to be down more than 15% for the full year in '23 versus 2022.

Outside of marquee selling events such as Black Friday, Cyber Monday, our promotions and markdowns generally focus on non-core styles and those we expect to sunset or replace with next-generation versions.

This approach has helped us maintain full price brand integrity. And we expect to increase full price selling when we bring new and more innovative product offerings to market next year. Indeed, we're looking forward to a number of activities in 2024 across product and marketing that we expect will generate momentum with our consumer.

Zooming out and taking a look at the shape of the transformation, 2023 has been a year of diagnosing and fixing, most notably our cost structure, inventory position, and go-to-market model by region, while also recalibrating our assortment to drive more resonance with our core consumer in '24 and beyond. Having done this heavy lifting, we believe we'll enter 2024 with a strengthened foundation and a right-sized cost structure.

This will enable us to allocate resources and effort towards driving growth from our most profitable products and through our most profitable channels and regions, setting us up to improve our bottom line year over year. The actions we're taking now give us confidence that even in a challenging environment, we can achieve our goal of positive adjusted EBITDA and positive cash flow in 2025.

Now, I'll walk through some updates on the four pillars of our transformation plan, starting with product and brand. In Q4, we're continuing to flow in updated and refreshed core assortments. As I noted earlier, the Wool Runner 2, a fresh take on the biggest icon in the history of our brand just launched last week. And we'll soon introduce a capsule for her that reflects our new gender differentiated approach and shows how our refocused consumer insights work translates into great product.

In 2024 we're looking forward to launching more innovative assortments with an emphasis on our core franchises, along with key upgrades to those silhouettes, like we did with the Wool Runner 2. As we embarked on our transformation efforts, we knew that product development cycles would limit our ability to drive substantial newness in 2023. So while we are eager to bring these upgrades to the line in Q4, this is really just a taste of what's to come in 2024 and beyond.

As I touched on earlier, throughout this year we've deliberately pulled back on marketing spend and remained focused on being as efficient as possible while we transition and clean up our inventory. Our new influencer program is beginning to build with a material portion of our marketing mix. And we're pleased with the early outcomes to drive awareness and consideration, particularly with women.

We believe our upcoming holiday campaign will resonate well, and we expect the newness, color assortment, and promotional cadence to deliver results within the guided range for the quarter, enabling us to finish our transitional year with both marketing spend and inventory reducing at a greater rate than sales.

Turning to our second pillar, optimizing the US distribution and store profitability. When we developed our transformation plan, this pillar was focused on optimizing our US stores and slowing the pace of openings. We've completed all of the 2023 store openings under the previously committed leases and have no further openings planned.

We've since widened the aperture to optimize our US distribution more broadly with a continuing focus on improving store profitability. Q3 in-store traffic remained challenging for the retail industry broadly. And we experienced this as well. Given the consumer headwinds affecting the landscape, we expect this to persist in Q4 and have reflected that in our guidance. Our work in stores across merchandising and marketing, staff training, and labor scheduling are beginning to show improvements in store operations. But there is still work to do here.

In the digital ecosystem, as we seek to optimize our US distribution, we'll be launching on a leading digital marketplace in the coming weeks. We expect this platform to drive an incremental, profitable revenue stream, and we'll share additional details at launch.

Looking at wholesale. This remains a key channel for our future and one that provides us with the opportunity to profitably raise brand awareness, while also providing a unique view into what our consumers truly crave. Informed by these insights, we're collaborating closely with our partners to ensure that we're appropriately represented until we have an assortment that we believe will best resonate with consumers.

And we expect lower sales from this channel in the second half of this year and into the first half of 2024. We intend to utilize a pull versus a push strategy focusing on sell-through to ensure we're showing up in the right way before expanding door count. As we bring our new assortments to market through 2024, we anticipate re-accelerating growth in this channel in the second half and are speaking with new potential partners to selectively broaden the number of accounts.

Now, on to our third pillar, transitioning our direct go-to-market strategy towards a distributor model in international markets. This is the most complex activity within our transformation plan and we believe has the potential to move the needle on profitability quickly. We're incredibly pleased with the progress we've made on this front and expect to have additional news soon.

During the third quarter, we finalized the previously-announced agreements with third-party distributors in Canada and South Korea, and those regions are now transitioned, including personnel, stores, and inventory. Additionally, we recently signed LOIs for two additional important regions with distributors in both Japan and Australia, New Zealand.

We're thrilled to be partnering with high-quality organizations that have extensive brand building and distribution capabilities in their respective regions. The transitions are expected to occur by mid-year 2024. Three quarters into this strategy, we're pleased to have four regions with clear transition pathways towards a profitable and scalable structure.

We anticipate selectively opening up distribution in new regions, beginning in the second half of 2024, to further capitalize on this distribution model, which similar to wholesale, requires no capital investment from us. We expect that this opportunity will not only deliver additional profit to us, but also drive volume expansion to support additional manufacturing cost savings through SKU productivity. At the same time, we believe the distributor model will drive increased brand awareness internationally and provide greater access to both new and existing customers.

As a reminder, initially, the move from direct model to a distributor model will result in a decline in revenue for the impacted regions. But we expect strong flow-through to the bottom line, making this higher-quality revenue. Annie will provide more color around the economic model shortly.

Moving to our fourth and final pillar, improving overall gross margins and managing operating expenses. We are firmly on track to achieve our stated goals to capture $20 million to $25 million of COGS savings and $15 million to $20 million of SG&A savings by 2025, as compared to our run rate at the end of 2022.

We continue to ramp up shipments from our new manufacturer in Vietnam during Q3 and expect the transition to fully take shape by year-end, with P&L benefits beginning in 2024. We now expect that our work in this area will allow us to deliver the high end of the expected cost of goods savings range by 2025.

Additionally, as we continue to work through inventory, bring new products to market and reduce the depth of promotions, we believe this will allow us to move the consumer back towards the full price model, improving gross margin.

Entering the final stretch of the year, we're pleased with the progress under each of the four pillars and remain confident that our transformation plan is positioning us to improve capital efficiency and drive profitability.

We are fortunate to have an experienced team who has embraced a highly disciplined operational approach. This enabled us to take decisive action in 2023 to lay the groundwork for improved year-over-year profitability in 2024 with a path to our first expected calendar year of positive adjusted EBITDA and cash flow in 2025.

We've significantly improved our inventory position, heading into the important holiday selling season. We have excitement building for 2024 product launches. We are well on our way to transforming our international business. And we have institutionalized rigor across the organization.

Our path is clear. And after approaching the end of year one of this transformation, we're acting with discipline to drive long-term growth via products, regions, and channels that have the greatest potential to deliver elevated levels of profit. We appreciate the support of our analysts and shareholders and believe the progress we're making will compound into strong shareholder returns in the future.

Now, over to Annie to walk through specifics on the quarter and commentary on the shape of the remainder of this year.

Annie Mitchell *Allbirds, Inc. - CFO*

Thanks, Joey. We're pleased to report another quarter of operating and financial progress. Q3 results came in within our expected range on the top line, exceeded expectations we provided on the bottom line. And for the third quarter in a row, we delivered solid improvement across our key metrics of inventory, cash, and costs.

Third quarter revenue of $57.2 million declined 21% versus a year ago and largely reflects our strategic actions to clear through legacy inventory, as well as planned declines in wholesale revenue to ensure we are set up to drive high sell-through with our fresh and updated assortment in 2024.

Gross margin came in at 43.5% that compares to 44.8% a year ago and primarily reflects higher promotional activity as we continue to work down non-core styles and colors, leading up to our new product introductions planned for 2024.

Before we get to next year, we're focused on ensuring that we engage and delight the consumer this holiday season, which means increased promotional activity versus a year ago. Simply put, as you heard from Joey, we intend to be competitive on price. As a result, we anticipate that fourth quarter gross margin will be below 40%.

Turning now to expenses. We brought down SG&A, excluding depreciation and stock-based compensation by $1.8 million or 5% versus a year ago. This came in better than we expected and can be traced to our careful cost control, most notably the ongoing tightening of discretionary expenses. As we talked about last quarter, we continue to expect that Q4 SG&A dollars will be up both on a sequential and a year-over-year basis.

Marketing expenses reflect a planned decline of $2.5 million or 19.6% compared to Q3 2022. Looking at Q4 marketing spend, we continue to expect a modest uptick from Q3 levels as we support the Wool Runner 2 launch and the holiday sales push.

In Q3, we incurred $1.2 million in restructuring charges associated with our strategic transformation, an increase of $0.5 million compared to Q3 2022. Taken together, our top-line results and careful cost control drove a better than expected adjusted EBITDA loss of $19 million in Q3.

Moving to the balance sheet and cash flow. I'm pleased to report another quarter of solid progress against two of our key benchmarks. First, I'll talk about inventory. We ended the quarter with inventory levels down 37% versus a year ago and down 32% from year-end.

The improvement reflects more selective and disciplined buys and our commitment to achieve a healthier composition and clean position by year-end. Indeed, we expect to end the year with inventory levels of approximately $70 million, reflecting a year-over-year decline of approximately 40%.

Now let's look at cash. At the close of Q3, we had $132 million of cash on the balance sheet. Our aggressive actions to bring down inventory levels and reduce operating expenses allowed us to narrow our operating cash use versus a year ago.

Through the third quarter, operating cash use was just $5 million compared to $18 million a year ago. We also delivered significant improvement for the year-to-date period, with operating cash use narrowing to $25 million versus $82 million. We anticipate that operating cash usage will increase slightly in Q4 compared to Q3 levels.

Before turning to guidance, I'd like to share some data points to help you understand the financial implications from our transition to third-party distributors in international markets. Starting at a high level, prior to the transition to a distributor model, Allbirds had a presence in the following six international regions, representing approximately 26% of total revenue for the nine-month period ending September 30. Australia and New Zealand combined, Canada, China, Europe, including both the EU and UK, Japan, and South Korea.

During the third quarter, we completed the previously announced transition of our Canadian and South Korean businesses to local distributors in those countries. This encompasses Allbirds' e-commerce, bricks and mortar, and wholesale businesses across both regions. The transaction was recorded in Q3 as a non-operating loss on the sale of business totaling $2.3 million and is excluded from adjusted EBITDA in the quarter.

Next, after quarter-end we signed LOIs with the distributors in two additional regions: Japan and Australia, New Zealand. Those transitions are expected to be completed mid-year in 2024, as noted in our press release today. The New Zealand agreement is contingent upon the employee consultation process, which is standard in that country.

For added perspective, Canada and South Korea combined represented approximately 4% of total company revenue year to date in 2023. And Japan and Australia, New Zealand combined represented approximately 8% of total company revenues year to date in 2023, so very good progress on this strategic pillar three quarters into the transformation, with four regions and approximately 12% of the overall business in transition to a simpler model that we believe is better positioned to grow.

Now we'll turn to some additional data points that underscore the benefits of the distributor model. First, we'll be selling products directly to the distributors at a lower price versus our prior direct sale to the consumer at full retail. While this will result in initial impact to revenue, we anticipate that the expertise and local knowledge of our distributors will help drive brand visibility and growth over the coming years.

Next, under this model of selling directly to distributors, gross margin will naturally be below both DTC and typical wholesale margins. Because this model requires lower operating expense, we anticipate strong flow-through from gross profit to the bottom line. As each region transitions, we expect them to be immediately profitable.

Turning now to Q4 guidance, our expectations assume a few key factors. One, we're prepared for a cautious consumer and a highly promotional environment this holiday season. We know the consumer will be looking for great products at great price points. And we have a targeted promotional plan to ensure we are competitive throughout the quarter.

Second, it's important to note that this promotional stance will impact both sales and gross profit.

Third, the outlook we're providing today also reflects a full quarter of revenue under the new pricing model for Canada and South Korea. This results in a $2.5 million negative impact to revenue in Q4.

For the fourth quarter, revenue is expected to be in the range of $66 million to $72 million, representing year-over-year comparisons of negative 22% to negative 15%. Adjusted EBITDA loss is expected to be in the range of negative $26 million to negative $23 million.

Given the progress we're making within all of our strategic pillars, especially the international piece of the transformation, we expect to return to full-year guidance in 2024 on our call in March. We also anticipate that we'll be positioned to provide increased granularity around top line expectations and the related impact of the international transition to help you most effectively model the business going forward. Now I'll ask the operator to open the call for Q&A.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Bob Drbul, Guggenheim.

Bob Drbul ***Guggenheim Securities LLC - Analyst***

Hi, good afternoon. I guess, just two quick questions for me. And the first one is just, on the inventory side, can you just expand more in terms of the quality of the inventory, the newness of the inventory? And then, I think the second piece is just love to hear a little bit more about the product changes in women's and overall what you guys are planning as you think through some of the newness heading into next year. Thanks.

Annie Mitchell ***Allbirds, Inc. - CFO***

Hi, Bob, thanks for your question on inventory. It's definitely part of -- I'm most excited about in terms of our progress. So I really appreciate you asking about it. We're absolutely pleased with the progress that we've made, cleaning the marketplace and moving our inventory composition toward core products. That's really been the effort this year in 2023 to make sure that we end the year with the right composition.

Year to date, inventories are down 32%. And we expect to end the year down about 40% year over year. With that, we do -- by doing all the heavy lifting already this year, we expect to exit the year well-positioned to bring in fresh and updated product for 2024. And I know that Joey is excited to talk a little bit about that.

Joey Zwillinger ***Allbirds, Inc. - CEO***

Yeah. Thanks, Bob. So I think the Wool Runner 2 is probably a great example to start with. I would say, at the high level, we're looking at moving to a franchise offense, and this is what we've been speaking about all year.

The core franchises have an opportunity if we embellish them correctly and merchandise effectively to really create a lot of brand equity around the silhouette and drive a lot of growth with our existing consumer. And I think will resonate just much more strongly with a broader base, given that some of these icons are what we became famous for.

So first and foremost, it's a focus on core. And I think Wool Runner 2 being the highest sales volume launch that we've done this year and even some months prior than that is a really good example of taking that icon and slightly updating it to make sure we deliver amazing quality, durability, and communicate the value of what we're doing with the brand personality that we did through some of the marketing work, it's going to work better.

And that's what we saw in this launch, being the best one so far. So that's one of the core insights. And I think in that we'll be trimming out some of the lower productivity SKUs as we focus the effort on our core franchises.

And then as you alluded to in your question, one of the other key insights that we found is that within our target demographic, our target consumer, we do have higher awareness with women than we do with men. And the consideration, on the other hand, is flipped there where our consideration is a bit lower with women.

And so what we do understand is that the brand is beloved by both genders. But in particular, there is stronger resonance currently as you track from have you heard about us to are you going to buy the product with men.

So that's the work that we're doing in terms of sharpening up the product offering both on a color and trim perspective, which you'll see a little bit of in this quarter, but also in terms of extending some of those core franchises to be a little bit more feminine to resonate more strongly with her. So that's overall, the two key aspects I'd draw you to. I'd say, materially, we're going to start in Q2 next year and continue throughout the rest of 2024, and of course, beyond that too.

Bob Drbul ***Guggenheim Securities LLC - Analyst***

Thank you. Good luck.

Operator

Alex Straton, Morgan Stanley.

Alex Straton ***Morgan Stanley & Co LLC - Analyst***

Great, thanks for taking my question. Hi, Joey, Annie, good to speak to you again. I have one quick high level question and then a more specific guidance question for Annie. So maybe, Joey, the first one for you, the strategic transformation plan has been underway for a few quarters now. Where do you think you've made the most progress or already seeing results?

And then maybe on the other end, what has proven more challenging than you thought when you started this journey? Then for Annie, just you have a wide revenue guidance range into the fourth quarter. Can you just walk us through what that accounts for on the low end and the high end? Thanks a lot.

Joey Zwillinger ***Allbirds, Inc. - CEO***

Alex, thanks. Okay, so let's do it in order. I'd say, I'll zoom back and just put it in perspective on how I would characterize what we've done in the last few quarters here as we entered this transformation to help answer that question. So I'd say at the top level, this year is one where we've fundamentally altered the cost structure in such a way that we can be profitable at a much smaller top-line level.

And we've talked a lot about the work that we've done on cost of goods and some of the G&A streamlining and the go-to-market in international regions. That has not been a trivial amount of work. And execution has been excellent on those elements.

And so while you don't get to see that benefit in the P&L necessarily as we burn through the inventory that we currently have on the balance sheet. That is probably the most important element of what we've accomplished this year. Along the way, we started the year with, I would call it, an unhealthy level of inventory and an unhealthy mix of inventory, and we've gotten ourselves on track to really fix that.

So we expect to end the year and enter 2024 in a really healthy position as it comes to inventory. And that's going to allow us to then inflect our gross margin in such a way that we can take the benefits of all those cost savings that we've done throughout the year and also win the customer and the consumer back to a full price selling model by lightning the markdown intensity and driving the new innovation from the recalibrated product assortment that we introduced in the marketplace at full price.

And so that gives us a great focus in 2024 to drive fairly significant gross margin expansion, particularly in the direct channel. And that I would say, just like zooming out is the big thing and I'd say, and the thing we're probably most proud of that we can sit here and hammer down today.

Of course, when we think about the look forward, it's product. We haven't yet brought all of this fresh and new innovative product that we have on the road map to market. So the proof points aren't quite there yet. But I'll say we are off to a really good start with what we've shown for the Wool Runner 2.

And I think it's a really good testament to the type of changes and updates we're going to be bringing to market. And the results speak for themselves as far as we're seeing internally and sharing with you today. So pretty encouraged by that, albeit that's the one that just has the longest lead time, given the product development lifecycles for making footwear. So that's the one that we're still plugging away at and really can't give you as many proof points as we can on the cost side.

Annie Mitchell ***Allbirds, Inc. - CFO***

When we're looking at our top line for Q4 and the guidance given, specifically the range, and it primarily reflects the macro-driven pressures that's affecting traffic and sales industry-wide. Adding on top of that, of course, is a continuation of our transformation work, which of course, is progressing extremely well and setting us up to engage with the consumer in fresh, new, and innovative ways in 2024.

Combined with that is, of course, we're planning for a highly promotional environment this holiday season. We know that consumer is going to be looking for a great product at a great price point. And we want to ensure that we're going to be competitive throughout the quarter.

Alex Straton ***Morgan Stanley & Co LLC - Analyst***

Great, thanks a lot. Good luck, guys.

Joey Zwillinger ***Allbirds, Inc. - CEO***

Thanks, Alex.

Annie Mitchell ***Allbirds, Inc. - CFO***

Thanks Alex.

Operator

Janine Stichter, BTIG.

Janine Stichter ***BTIG, LLC - Analyst***

Hi, everyone, good afternoon. I want to dig in a little bit more into as you think about the optimal channels of distribution for the brand. First off, on the wholesale side, it sounds like you're considering re-ramping that business in the back half of next year. So I'd just be curious to understand the types of potential new partners that you're looking at, what you think that brings you both from a new customer acquisition and a brand awareness standpoint.

And then on the retail business, I'd just love your thoughts on if you're exploring any potential store closures and just what the profitability of the fleet looks like right now, if there's any major variances in performance that should be called out. Thank you.

Joey Zwillinger ***Allbirds, Inc. - CEO***

Okay. Thanks, Janine. I will tackle the first part of that. And maybe on the retail side, Annie can jump in. So I mean, when you ask the question about optimal, I think it's a good way to frame it. What we've always envisioned is that we want to be a very effective omnichannel retailer. And we are a brand first. We want to delight consumers where they want to shop the best.

And one of the examples that we gave today is an impending launch on a digital ecosystem or digital marketplace in the US, just as an example of making sure that when we have product that we can segment to the right channels, that we're going to deliver that and make sure we capture opportunity to meet consumers where they want to be met.

So what does that look like if you fast forward way down the line? I think it's a little hard to say exact percentages, but there's a very material portion of our business that should be in wholesale. And we think about that as a very profitable and brand-building exercise for us where it lifts awareness, and frankly, you can trade some of the gross margin between direct and wholesale for some of that marketing that you otherwise would spend to drive awareness.

So that's very important for us, and anticipate building that, as we noted, particularly starting in 2H '24. But we expect that to grow much more significantly.

And in terms of the different channels, there's a whole sequence that we'd like to undergo in order to build an effective marketplace, working with some smaller accounts that drive perhaps leading indicator of trend for consumers onto other premium segments of the wholesale marketplace like we have in department stores and outdoor and sporting goods.

And I think in some of those channels, there's other non-competitive accounts that we're talking to and are pretty excited about the opportunity to work with. So we'll give you more detail as we get into 2024 and give you a picture for what we expect for the year, but that's generally how we're thinking about it.

Janine Stichter ***BTIG, LLC - Analyst***

Really helpful. Thank you.

Annie Mitchell ***Allbirds, Inc. - CFO***

Janine, when it comes to retail, we've paused opening new retail doors this year. We're done with all the doors that we're going to open. We don't currently have any closures planned at this time. But we will continually analyze and evaluate our retail fleet's performance and options.

As Joey mentioned, our focus is to drive growth by focusing on our most profitable products, channels, and regions. And for retail, that profitability comes from us executing on the initiatives that we've already started to put in place.

And also let's go back to why do we have stores to begin with? We do have a retail footprint because we operate in an ecosystem for our consumer. And these stores are the best expression of our brand to that consumer. It helps us to grow awareness, and as well, as we combine with our distribution around wholesale. We expect that the stores will enjoy more traffic and offer more compelling assortment as consumers start to know and understand and love our brand.

Janine Stichter ***BTIG, LLC - Analyst***

Perfect. Thanks so much.

Operator

Cristina Fernández, TAG.

Cristina Fernández ***Telsey Advisory Group - Analyst***

Thank you for taking my questions. I wanted to ask first on international. It seems like the business took a step down in the quarter. It might just be the function of the year-over-year comparison. But wanted to see if you can talk about what demand trends are you seeing in some of your major international markets and what is the level of promotional activity you're seeing there? Is it similar to the US or is it better? Thanks.

Annie Mitchell ***Allbirds, Inc. - CFO***

Great. Thanks for your question. And to clarify within Q3 because we transitioned both Canada and South Korea in the month of September, the transition of those from the direct model to the distributor was worth $750,000 on the top line. Said in another way, if we'd continue to operate them, our sales for the quarter would have been higher by $750,000.

When we look at the overall trends across the regions, we're seeing that Asia is performing year over year in Q3 slightly better than some of the other geographies. This is largely tied to worldwide macro events, and it really differs by geography. But I would say that China and Japan were definitely some of our better performing overall international geographies.

Joey Zwillinger ***Allbirds, Inc. - CEO***

And the promotional intensity is reasonably consistent across regions. There's a little plus or minus here or there, but generally pretty consistent. And I would say that as we have some of these conversations with distributor partners, what we're finding is that the brand is positioned incredibly strongly and these partners are pretty eager to invest capital behind the brand. And I'm quite optimistic and excited about what they can bring to the business.

Cristina Fernández ***Telsey Advisory Group - Analyst***

Thank you. And then the second question I had is related to some of the pricing actions you took on the core franchises, the original models, for Tree Runner and Wool Runner. What reception did you see to those price decreases? And is the strategy to keep those in the lineup? Or will you sunset those styles as Wool Runner 2 and Tree Runner 2 to get -- I guess to get further along?

Joey Zwillinger ***Allbirds, Inc. - CEO***

Yeah. Thanks for the question. Just in general on pricing, what we're working towards sometime in 2024 is going to be some very clear and distinct price tiers, ranging for the bulk of the business between $98 and $138 per pair in the footwear business.

And sharpening those price points is really something we'd like to do, driven from the insights that we've seen and the data that we have in terms of where we drive the most volume from our business, particularly when positioned in that active life territory, not promoting heavily technical running-oriented gear that might push you above that $140 threshold.

So that's where we expect to sit. And I would say that the most important element of those pricing changes was that it is in the lead up to the launch of the Wool Runner 2. We wanted to make sure there was space between those two models and segment them.

Similar thing is going to -- we'll do when we introduce new capsules for the Tree Runner in that Tree Runner 2 orientation, so same kind of thinking. And as those new generations grow the business, we would expect that at some point, we would sunset the original models, albeit in some cases we might not do it immediately.

Cristina Fernández ***Telsey Advisory Group - Analyst***

Thanks.

Operator

Mark Altschwager, Baird.

Mark Altschwager ***Robert W. Baird & Co. - Analyst***

Good afternoon, thanks for taking my questions. First off, maybe just a modeling question for Annie. Just with respect to the Q4 revenue guidance, can you give us a breakdown with what you expect for US versus international? I know there were some comments in the prepared remarks on the distributor changes, but if you could maybe simplify it for us a little bit, that would be helpful.

Annie Mitchell ***Allbirds, Inc. - CFO***

Yes. And to be clear, are you looking for year-over-year growth?

Mark Altschwager ***Robert W. Baird & Co. - Analyst***

Correct.

Annie Mitchell ***Allbirds, Inc. - CFO***

Yeah. We anticipate that both the US and our international business, for the ones that we continue to operate directly, will be roughly in line with each other, so no major differentiation between the two growth rates. When we look at the impact from the exit of Canada and Korea in terms of a direct model, that is worth three points on the top line.

So our guidance of down 22 to down 15, within there is three points from moving Canada and South Korea from the direct model to the distributor model. But in terms of the overall trend, both the US and international are moving in the same direction.

Mark Altschwager ***Robert W. Baird & Co. - Analyst***

That's really helpful. Thank you. And then, switching gears, was hoping if you could give us some additional context on what you're planning from a promotional standpoint over holiday. I guess, you've done a great job cleaning up the inventory, at least it looks that way on the balance sheet.

So I mean, are these promotions meant to still clean up some older product? Or is this more about staying top of mind during this transition period? And I guess, do you worry that the promotional plans might curb the ability to return to full price selling as the new product starts to roll in, in 2024? Thank you.

Janine Stichter ***BTIG, LLC - Analyst***

Yeah. It's a good question, Mark. So I think you shouldn't see anything too wild from us over the promotional cadence here. I think we're trying to line up. What we're seeing in the market is that people are starting to promote pretty early, maybe even earlier than what we saw last year from when the start of this cadence comes in industry wide.

And we found if you're not competitive in that moment, then you're leaving opportunity on the table. And it's really our objective to get to a really healthy place by the start of next year. We still have a little bit of work to do, as Annie guided you all, to trying to end the year around 40% down year over year in terms of inventory on the balance sheet.

So it's still a little bit of work to do there. And that includes a pretty big event, as you well know, Black Friday, Cyber Monday, and around that, we'll do some other select discounting. And that will be to trim the tail of any remaining styles or colors that we don't expect to support in the future, and maybe over some of the big events, offering a broader assortment that includes some of our core styles. So I do think the way we've handled this, this year has allowed us to maintain that full price brand integrity.

Predominantly, our promotional opportunities for consumers have been around styles that we no longer intend to support, and particularly on a colorway basis. Even in styles that we support, there are colors that move really slow, we don't expect to bring back.

And so that's a helpful aspect to how we've managed the promotional cadence. I feel like we've been fairly surgical, despite the fact that we've had to increase the depth of promotion as well as to some degree, their frequency.

And as we get into next year, that's going to be a helpful foundation for us to win people back. The approach that we're taking is essentially based on two factors. One is that we'll have a much better assortment and new innovation coming to market. That's generally the best way to get a consumer back to full price.

And then secondarily, we left some room this year by going fairly deep on our markdowns to work through the inventory that we can lighten the discount intensity. And so, we may have the same frequency, but the depth will be much shallower.

And that's going to give us an opportunity to build some brand momentum, as well as inflect on gross margin in a fairly material way when you compound that with the cost savings we got from manufacturing changes.

Mark Altschwager ***Robert W. Baird & Co. - Analyst***

It's really helpful. Thank you, and best of luck.

Joey Zwillinger ***Allbirds, Inc. - CEO***

Thanks, Mark.

Operator

Tom Nikic, Wedbush Securities.

Tom Nikic ***Wedbush Securities Inc. - Analyst***

Hey, everybody, thanks for taking my question. Obviously, there's been a big pullback in marketing this year, given the transition of the product assortment. But how should we think about the need to reinvest in marketing, I guess, in 2024 and beyond when you have the new products that you're developing in place and using marketing to reignite the top line?

Joey Zwillinger ***Allbirds, Inc. - CEO***

Thanks, Tom. There so when we have the fresh product assortment coming, and particularly if we're using promotion less as a lever, price as less of a lever, we're going to want to spend on marketing and invest behind strength.

What we want to do is focus that on the core franchises, so that we continue to build a lot of equity around those core models, and that's the work we're embarking on. So that is one element that we'll look at in 2024 and beyond.

I would say that another key factor for you to consider is the model still over the coming years will be intended to drive leverage on our marketing as a percent of sales. And a large part of that is about the channel mix in the business.

So as we shift to international from direct distributors, that's a much more significant leverage because we don't support those markets with marketing dollars anymore, and similarly, on the wholesale side, just has a much smaller marketing spend as a percent of the overall sales. So that's one aspect of driving leverage in the long term.

And then, finally, I'll just say that our brand has tremendous amounts of affinity with our core consumer. And people do really love the brand. We've seen that in all the work we do consistently with consumers, mirrored by the NPS scores we collect and the fact that we found consistently that people have a very high degree of desire to come back and consider buying again from us.

So given that it creates this opportunity, where we do have opportunities to work with either people or brands that we can partner with in the future, and some of those opportunities, it's hard to sometimes predict how well they come off, but some of them can be really catalytic.

And given that we have such a differentiated offering to the marketplace and a differentiated message, we get to go in the doors with some pretty compelling opportunities and rest assured that we're working on those very regularly.

Tom Nikic ***Wedbush Securities Inc. - Analyst***

Thanks very much, [and best of luck to you].

Operator

Krista Zuber, TD Cowen.

Krista Zuber ***TD Cowen Inc. - Analyst***

Hi, thanks for taking our question. This is Krista on for John Kernan. Two questions, first, just a modeling question on the distributor economics. Just a clarification on the transition impact to revenues. I think you're guiding to -- I think it's $2.5 million impact to revenues in Q4 for Canada and South Korea.

Should that be the run rate we use for the next few quarters until we anniversary the transition? And should we expect the Australia, New Zealand, and Japan revenue impact to be roughly double than that since their representation of revenue is somewhat higher? And I have one follow-up. Thanks.

Annie Mitchell ***Allbirds, Inc. - CFO***

Great. Thank you for the question, really appreciate it. The impact for Canada and Korea in Q4 is very much related to it being the first full quarter that they are on the distributor model. So no, we would not expect that to be the overall runway going forward. We do, as we get into 2024, plan on giving additional color and guidance for the full year related to how this is going to overall impact the business.

When we think about the way that we're going to sell into these distributors, pricing will vary based on the exact quantity and mix. But directionally, a good way to think about the revenue per unit is that we're going to sell in with a gross margin that's naturally below both DTC and typical wholesale margins.

And we do anticipate very strong flow-through to the bottom line based on the low operating expenses in this model. And therefore, we expect to generate contribution margins north of 20% with this new international model.

Krista Zuber ***TD Cowen Inc. - Analyst***

Okay, great. Thanks. And then just one philosophical question on the margin profile long term. Just would love to get your thoughts on how you see the long-term gross margin and adjusted EBITDA margin potential within the construct of the execution of this transformation plan. Thank you.

Joey Zwillinger ***Allbirds, Inc. - CEO***

Yeah. We're not going to want to go into too many long-term details when we're in the throes of this. I can tell you, we still target a gross margin in our direct business in the US of targeting 60% gross margin, and a lot of the work we've done so far is tracking towards that.

So that's an important element there. And you can see gross margin naturally transition across the channels, albeit at different levels. But the cost savings that we're generating this year are certainly applicable across channel.

So that's the most I'd probably say at this point. And we'll think about how to get back to you all in terms of what we expect for next year, what we expect for 2025, and give you a longer-term picture as we get into 2024 and beyond.

Krista Zuber ***TD Cowen Inc. - Analyst***

Great. Thanks. Best of luck.

Operator

This concludes the question-and-answer session. I would now like to turn it back to management.

Joey Zwillinger ***Allbirds, Inc. - CEO***

Thanks, everyone. I'll just close with a few comments. I should just say, our team is laser focused on profitability and driving high-quality sales, even if it does mean sacrificing growth at times. And while we do that, we do intend to seek growth opportunities across products and channels that drive elevated levels of profit.

And the incremental progress we're making is building on an already strong brand foundation. And we expect it to compound into strong shareholder returns in the future.

So thanks for your continued interest in Allbirds as we move through quarter after quarter through this transformation and do the great work we're doing. And we look forward to wrapping up the year with you and looking out to '24 in a few months. Thanks.

Operator

Thank you for your participation in today's conference. This does conclude the program. You may now disconnect.