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J.Jill, Inc. (JILL)

Q2 2022 Earnings Call

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CORPORATE PARTICIPANTS

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Mark Webb
Executive Vice President & Chief Financial and Operating Officer, J.Jill, Inc.

OTHER PARTICIPANTS

Dana Lauren Telsey
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Daniel James Lupo
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MANAGEMENT DISCUSSION SECTION

Operator: Good morning. My name is Rex, and I will be your conference operator today. At this time, I would like to welcome everyone to the J.Jill Second Quarter 2022 Earnings Conference Call. On today's call are Claire Spofford, President and Chief Executive Officer; and Mark Webb, Executive Vice President, Chief Financial Officer and Chief Operating Officer. All lines have been placed on mute to prevent any background noise. After the speakers' remarks, there will be a question-and-answer session. [Operator Instructions]

Before we begin, I need to remind you that certain comments made during these remarks may constitute forward-looking statements and are made pursuant to and within the meaning of the Safe Harbor provisions of the Private Securities Litigation Reform Act of 1995, as amended. Such forward-looking statements are subject to both known and unknown risks and uncertainties that could cause actual results to differ materially from such statements. Those risks and uncertainties are described in the press release and J.Jill's SEC filings. The forward-looking statements made on this recording are as of September 1, 2022 and J.Jill does not undertake any obligation to update these forward-looking statements.

Finally, J.Jill may refer to certain adjusted or non-GAAP financial measures during these remarks. A reconciliation schedule showing the GAAP versus non-GAAP financial measures is available in the press release issued September 1, 2022. If you do not have a copy of today's press release, you may obtain one by visiting the Investor Relations page of the website at jjill.com.

I will now turn the call over to Claire.

Claire Spofford
President, Chief Executive Officer & Director, J.Jill, Inc.

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Thank you, operator, and hello, everyone. Thank you for your interest in J.Jill. For today's call, I'll review highlights of our second quarter performance and provide an update on our strategy before turning the call over to Mark to review our financial performance and outlook in more detail.

Our second quarter results reflect the team's continued execution of our business strategy, focused on regularly flowing newness, driving full-price sales and expense management, while operating in a volatile consumer environment. This strong execution helped to drive a record quarter of adjusted EBITDA of $35.6 million for Q2, led by gross margin expansion of 150 basis points on top of last year's difficult comparison and supported by year-over-year sales growth of approximately 1%.

In line with Q1, woven tops and dresses continued to be stand-out categories, demonstrating our customers' appetite for newness and novelty. Our core franchises like linen, across tops, bottoms and dresses, continued to perform well as well.

Now, I'm going to talk about what we're seeing and hearing from our customers. Last quarter, we mentioned that while our customer is not impervious to economic pressures, including inflation, she tends to be more resilient than the average consumer. In particular, we saw a strong start to the quarter over Mother's Day and heard from our store associates that she was generally stocking up early for her seasonal wardrobe and shopping for a summer packed with events and travel.

We did see a slowing in purchasing in the latter part of the quarter, as our customer had shopped earlier for the season and headed out on vacation. But we remained committed to full-price selling, resulting in strong margin performance for the quarter. As the weather turns and we continue to flow newness, we're staying close to her and our field organization on her behaviors and shopping intent. And we feel confident, based on what we've heard, that she's coming back to refresh her fall wardrobe.

Now, I want to provide an update on the way we are using our stronger foundation as a platform for the long-term profitable growth of the company. As we move into Q3 and beyond, we are beginning to invest meaningfully in brand awareness and the growth and value of our customer base. This investment will support our growth agenda as we move into the latter part of this year and into 2023.

Recently, you may have heard our announcement around the Welcome Everybody campaign and our Size Inclusivity initiative. Before I go deeper into the modernization of our brand and value proposition with Welcome Everybody, I want to outline the approach we've taken to launch this initiative.

We remain committed to the execution of our operating model, and our new inclusive sizing efforts are being managed with the same focused approach. We've offered extended sizes for a long time online and, to some extent, in our stores, but we haven't done a sufficient job of building awareness and supporting this offering, providing a real opportunity for us to reach new customers and to do a better job of serving the customers we have.

As we prepared for this rollout, we focused on perfecting our fit, improving her experience when shopping for extended sizing, and clearly communicating our robust range of size options.

Now, I will go into more detail about the brand campaign. As I mentioned on the last earnings call, we conducted a thorough customer insight plan, including primary research with thousands of existing and prospective customers, as well as information gathered from our field associates. Our due diligence informed every aspect of

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the Welcome Everybody campaign and Size Inclusivity, revealing several real opportunities to excite our current customers and to introduce new customers to our brand.

These include: merging the Missy and Women's collections to provide a size-integrated shopping destination for customers in stores; bringing 2X into our stores where we know there's an appetite for it, while continuing to carry sizes extra small for 4X online; continuing to offer deep range of the products in Petite and Tall to support growth and the consumer need within these categories; and to reintroduce our brand and compelling value proposition and products to her through the Welcome Everybody campaign.

Reintroducing our brand also create an opportunity for us to respond to one of our most salient needs, the importance of seeing women she could relate to, and women who look like her in our marketing, and to celebrating individuality in our presentations and messagings. We continue to build on the success we've seen in social channels like Facebook Live and Instagram, by featuring a diverse cast of influencers across a range of sizes and body types, who are helping us spread the word around our brand and the Welcome Everybody ethos.

As I talked about earlier, fit was among one of the most important aspects of the Size Inclusivity initiative. The design team conducted extensive fit sessions to closely evaluate the fit on all different body types and perfect the fit within our extended size runs. This extensive fit testing allowed us to interpret each style and bring it to life for the full range of customers.

We want every woman to be able to find her desired fit and products that are uniquely relevant to her with the confidence that J.Jill has what she is looking for in beautiful styles and fabrications.

As we look to the remainder of the year, we continue to take a conservative outlook with respect to the consumer landscape, but expect to leverage the operating disciplines and our stronger foundation to continue to execute on our objectives and strategies.

Now, I am going to turn it over to Mark, who'll go into detail about our financial performance.

Mark Webb

Executive Vice President & Chief Financial and Operating Officer, J.Jill, Inc.

Thank you, Claire, and good morning, everyone. We were pleased with the overall performance of our second quarter, despite the volatile consumer environment Claire discussed and the difficult comparison to last year. Our continued focus on driving profitability delivered strong gross margin, adjusted EBITDA and cash flow on sales growth of approximately 1%.

Total company sales for the quarter were $160 million, up 0.7% versus Q2 2021. Total company comp sales grew 0.8%, driven by the stores channel. Store sales for Q2 were up 2% versus Q2 2021, driven by higher average unit retails through strategic price increases and reduced promotions.

Direct sales, as a percentage of total sales, were 46% in the quarter. Direct sales were down 0.7% compared to second quarter last year, which was the first quarter that meaningfully reflected the new operating model, focused on driving fewer markdowns and more full-price sales through this channel.

Looking at the rest of the P&L. Reflecting our continued focus on driving profitability, gross profit was $112 million, up $3 million compared to Q2 2021. Q2 gross margin was 70.1%, up 150 basis points over Q2 2021, as the impact of strategic price increases and reduced promotions more than offset product cost inflation and approximately 140 basis points of incremental freight charges compared to Q2 2021.

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SG&A expenses were $84 million, compared to $86 million last year, as increases in selling costs from store operating hours and shipping and strategic investments in marketing were offset by savings in occupancy costs, depreciation and amortization and management incentive. SG&A, as a percentage of sales, leveraged 130 basis points compared to the prior year.

Adjusted EBITDA was $36 million or 22.2% of sales for the second quarter 2022, compared to $33 million or 20.5% of sales in Q2 2021. Please refer to today's press release for a reconciliation of adjusted EBITDA.

Turning to cash flow. Our results continue to demonstrate the strong cash generation of the business. We generated $28 million of cash from operations in the second quarter and $35 million in cash from operations year-to-date, resulting in end of second quarter cash of $62 million, with zero borrowings against the ABL. We paid down the remaining amount on our stub term loan during the second quarter, bringing funded debt on the balance sheet to $206 million.

As noted in our press release today, we are continuing to explore options to refinance our remaining outstanding term loan credit facilities with the objective to decrease the total size of the facilities and extend our debt maturities.

We ended the quarter with inventory levels up 12% compared to the end of second quarter 2021. This increase is driven by elevated levels of goods in transit, with on-hand cost and units down in the low to mid-teens. The increase in in-transit goods is primarily driven by the strategic decision to ship fall product one to two weeks early this year to help improve on-time deliveries and minimize the use of more expensive airfreight in light of continuing supply chain disruption. We remain very comfortable with overall inventory levels in the business and the mix of that inventory at full-price and markdown as we enter the third quarter.

Capital expenditures in the quarter were approximately $1.4 million and were primarily related to capital maintenance projects, investments in brand modernization and growth initiatives, and the kickoff of the new POS project. Capital spend will ramp in the back half as we progress with the POS project and plan for store investments later in the year.

With regard to store count, we closed 2 stores in the quarter, ending with 247 stores.

With respect to our future outlook for fiscal 2022, the third quarter represents a difficult comparison given the strong full-price-driven recovery experienced in the quarter last year. As such, we are projecting for the third quarter of fiscal 2022 sales to be flat to down 3% versus Q3 2021 and adjusted EBITDA to be between $21 million and $23 million. Included in this outlook is an expectation that gross margin is relatively flat to last year and SG&A dollars will increase as we make strategic investments, particularly in marketing, to support the near- and long-term growth initiatives Claire outlined in her remarks.

For full year, we are reaffirming our prior outlook for the following metrics. Annual sales. We expect annual sales to grow modestly compared to prior year, with back half performance weighted to the fourth quarter as we anniversary the impact of Omicron last year. And adjusted EBITDA, we expect annual adjusted EBITDA dollars to be up compared to 2021, with growth outpacing the expected modest increase in annual sales.

The expected growth in adjusted EBITDA is driven by gains in sales and margin, partially offset by expected pressure from expense inflation and investments we are making in talent, store operations and marketing.

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With respect to gross margin, we now expect gross margin to be up slightly compared to 2021. Regarding store count, we now plan to close net 10 to 14 stores in fiscal 2022, including the opening of up to 2 new stores late in the fourth quarter. And finally, we now expect capital expenditures of about $15 million for the year.

Thank you. And I will now hand it back to the operator for questions.

QUESTION AND ANSWER SECTION

Operator: [Operator Instructions] We'll pause for just a moment to compile the Q&A roster. Your first question comes from the line of Dana Telsey. Your line is open.

Dana Lauren Telsey

Analyst, Telsey Advisory Group LLC

Q

Good morning. Nice to see the progress on the results. Claire, as you talk about the customer and slowing down in the second half of the quarter, what did you see there? Was it traffic? Was it transactions? And with the Welcome Everybody campaign, what's been the response to that? Anything in category by region or online versus in stores?

And then, Mark, on the refinancing, what's your expectation of the timing of refinancing and what it could mean? And then, just lastly, with the full-price environment that you're seeing, the newness that you're offering, anything on particular categories and where the price increases are or where you're seeing the greatest acceptance of the product newness? Thank you.

Claire Spofford

President, Chief Executive Officer & Director, J.Jill, Inc.

A

Thanks, Dana. With regard to the customer, we did see a slowdown in traffic in the latter half of the quarter. And again, I think what we heard from our store teams was she had shopped early. We definitely saw a super strong start to the quarter, beginning with Mother's Day, which is a big holiday for us. And we heard that she had sort of shopped early and she had a very busy summer plan. She was getting out and about. She was traveling, going on vacation. And we think that that had an impact on traffic in the latter half of the quarter. But we continue to field our tracker quarterly. And she has absolutely said that she intends to come back and purchase for the fall. And so, we're excited to see that happen as we move into the fall season.

Around the campaign, we've really just launched a few weeks ago. So it's very early. I will tell you that we've gotten very positive feedback from consumers online, on social, lots of comments about, oh, we didn't know you carried extended sizes, great to see the price parity, really pleased, love this campaign kind of thing. And the store teams are very excited. They've been doing outreach to customers, and we are excited to see that momentum grow as we get into the quarter.

From a category standpoint, and then I'll let Mark circle back on your second question, we continue to see kind of the same trends, Dana. We see real strength at full-price. We are not seeing price resistance in the novelties and newness, categories like dresses, woven tops, things that she's buying for travel or for going out. We saw real strength in Wearever in this quarter as well, which she wears to work and for travel.

So very little price resistance there, and those categories continue to be some of the areas where we took prices up. So continued story there that we saw in Q1 as well.

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Mark Webb
Executive Vice President & Chief Financial and Operating Officer, J.Jill, Inc.
A

And Dana, just regarding the refi, thanks for the question. Look, we just continue to be very excited about the recovery in the business. And as we've stated before, we really are taking an opportunistic approach and there really isn't the urgency or the need to refinance. It's a desire to refinance for the reasons that we stated in our remarks.

What we've been doing is getting prepared to do so. And when the markets are ready and the terms are in line with what we're looking for, I think we stand ready to go. But no further indication of timing than that.

Dana Lauren Telsey
Analyst, Telsey Advisory Group LLC
Q

And then, just it looks like there was a slight change in the net new stores. Anything on the store environment and what you're seeing there and your outlook for openings and closings?

Mark Webb
Executive Vice President & Chief Financial and Operating Officer, J.Jill, Inc.
A

Yeah. We still believe in the opportunity for store growth that's out there. We've said before that we will make sure that we are negotiating the right terms for our business to do so. Still a lot of opportunity out there. I think what you're seeing with respect to the slight revision down in the expected store account opening for this year is just some of the lead times with getting build-outs, as well as the fact that we're going to take the time necessary to negotiate the right deal for the best location.

Dana Lauren Telsey
Analyst, Telsey Advisory Group LLC
Q

Thank you.

Mark Webb
Executive Vice President & Chief Financial and Operating Officer, J.Jill, Inc.
A

You bet.

Operator: Your next question comes from the line of Daniel Lupo. Your line is open.

Daniel James Lupo
Analyst, Norris, Perne & French LLP
Q

Hey. Thanks for taking the question and very nice quarter. If I kind of look at the quarter and the strong kind of cash flow in the quarter, could you maybe comment a little bit more outside of kind of profit margins what really drove that? How does your working capital position expand today and how do you kind of think about that for the rest of the year?

Mark Webb
Executive Vice President & Chief Financial and Operating Officer, J.Jill, Inc.
A

At this point, Daniel, you see on the inventory piece, which is always the largest working capital impact for us, we are investing in inventory. We're taking earlier deliveries where we can to ensure on-time delivery. But, really, the

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cash from ops is from ops, and it's full-price driven and it's the power of full-price margin-driven business model that generates the cash in the business.

Daniel James Lupo
Analyst, Norris, Perne & French LLP

Q

Got it. And just to kind of follow up on the refinancing question. I guess, maybe it was talked about maybe last quarter about being opportunistic. So, I guess, have you had conversations at least from the last quarter conference call to this quarter conference call, and maybe kind of what's been some of the feedback that you've been receiving?

And then also just kind of in the prepared remarks, you made comments about lowering the overall quantum of debt. So given where maybe the loan is trading or quoted in the secondary market, have you thought about maybe repurchasing at a discount in the secondary?

Mark Webb
Executive Vice President & Chief Financial and Operating Officer, J.Jill, Inc.

A

We have – Daniel, it's a good question. We have – there are certain covenants and restrictions against that that limit our ability to do so. But what we've said and what we've been doing is getting ourselves ready. And as you know, in these situations, the market has to be conducive. The market's been pretty tough through the summer. We are hopeful that it is improving and will continue to improve. And we're extremely confident in our position as a company to enter that market when the market's ready.

So, that's kind of the approach that we're taking. It is opportunistic at this point. The objective to address the quantum is a qualitative statement, I guess, at this point that we feel really good about the overall debt levels and where we stand and we have term. It's more about getting more term and being opportunistic and just improving the balance sheet in that way. So that's our objective. We feel like the momentum of the business supports it and the work that we've been doing is really, at this point, to get ready.

Daniel James Lupo
Analyst, Norris, Perne & French LLP

Q

Got it. No, that's helpful. That's all I had for today. So, thank you for your time.

Mark Webb
Executive Vice President & Chief Financial and Operating Officer, J.Jill, Inc.

A

Thanks, Daniel.

Operator: There are no further questions at this time. This concludes today's conference call. You may now disconnect.

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