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Aritzia, Inc. (ATZ.CA)

Q3 2021 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Thank you for standing by. This is the conference operator. Welcome to Aritzia's Third Quarter 2021 Earnings Call. As a reminder, all participants are in listen-only mode, and the conference is being recorded. After the presentation, there will be an opportunity to ask questions. [Operator Instructions]

I would now like to turn the conference over to Helen Kelly, Vice President of Investor Relations. Please go ahead.

Helen Kelly

Vice President-Investor Relations, Aritzia, Inc.

Thank you, Anastasia, and thank you, all, for joining Aritzia's third quarter 2021 earnings conference call. On the call today, I'm joined by Brian Hill, our Founder, Chief Executive Officer, and Chairman; Jennifer Wong, our President, Chief Operating Officer; and Todd Ingledew, our Chief Financial Officer.

Following management's discussion, we'll host a question-and-answer period open to analysts and investors. Please note that remarks on this conference call may include our expectations, future plans and intentions that may constitute forward-looking statements. The uncertain and dynamic nature of COVID-19 and its ongoing impact could continue to materially alter our performance. We would refer you to our most recently filed Management Discussion & Analysis, and Annual Information Form, which include a summary of the material assumptions, as well as certain material risks and factors that could affect our future performance and our ability to deliver on these forward-looking statements. Our earnings release, the related financial statements, and MD&A, as well as the Investor Presentation are available on SEDAR, as well as the Investor Relations section of our website at aritzia.com.

I will now turn the call over to Brian.

Brian Hill

Founder, Chief Executive Officer & Chairman, Aritzia, Inc.

Thank you, Helen, and thank you, everyone, for joining us this afternoon. 2020 has been a year unlike any other we have experienced in our 37-year history at Aritzia. As a team, I am proud of what we have accomplished so far despite the many challenges along the way. Looking beyond this pandemic, we're well-positioned for meaningful growth, capitalizing on the unprecedented opportunities ahead.

While we believe our results during fiscal 2021 have been impressive given the circumstances, what's far more important, however, is what they signal about Aritzia's post-pandemic. Throughout this year, we progressively adjusted and adapted through that pandemic's vast challenges.

Notwithstanding restrictions as a result of the virus' impact, we continue to grow our revenue, are in a much stronger financial position, and have accelerated our strategic investments in infrastructure across people, processes, and technology.

Our four growth levers: digital innovation of eCommerce retail and Omni channel capabilities; secondly, geographic expansion across the United States; third, development throughout all our product divisions; and four, brand awareness in both the United States and internationally, drove our growth pre-pandemic, has ensured our success mid-pandemic, and will fuel our growth post-pandemic.

We will emerge from COVID-19 poised to elevate our much loved everyday luxury experience consisting of our engaging service provided by our outstanding boutique and Concierge teams, our beautiful and expanding multidimensional product, our aspirational environments throughout our eCommerce and retail channels, and our captivating communications shared by world-class marketing campaigns.

Together with Jennifer and Todd, I am pleased to report our Q3 results. In the third quarter of fiscal 2021, in the midst of this pandemic, we grew our revenue, we delivered meaningful EBITDA, and we strengthened our balance sheet. Todd will discuss the details shortly.

At the start of the quarter, 93 of our 97 boutiques were open. However, we ended the quarter with 83 of our now 101 boutiques opened. We had to close 18 boutiques in the heart of Toronto for the last week of the quarter. Unfortunately, these boutiques were closed during our busiest week of the year.

For health and safety reasons, capacity restrictions, and in anticipation of further boutique closures, we made the decision to pull forward the start of our Black Friday event to the week prior, stretching out demand in our boutiques. In hindsight, this was a fortuitous decision as we shortly thereafter received 48 hours' notice of the boutique closures in Toronto. In spite of these closures, our decision to pull forward our Black Friday start resulted in a record event performance.

For all our boutique employees impacted by these temporary closures, we have once again continued to ensure they have income continuity. This has proven invaluable in our ability to quickly reopen once the restrictions lift and continues to build loyalty within our team. I remain thankful for the commitment of our people during these times of uncertainty.

Notwithstanding the impact that these closures had on our business, our open boutiques, despite severe restrictions, performed beyond our expectations, on average at 81% of last year's productivity, an increase from the 70% productivity of Q2. Regional variation in performance endures depending on both the impact of COVID and the severity government restrictions by geography and environment.

Operating as our most effective yet profitable marketing tool, we continue to expand our boutique network thoughtfully with fastidious location selectivity, exceptional business terms, and with downside safeguards in place. During the quarter, we successfully opened five new boutiques comprised of four Aritzia boutiques and most excitingly our first Super World boutique in Soho, New York, in the iconic former flagship Dean & DeLuca space. In addition, we expanded two of our existing boutiques, increasing our footprint in these highly successful locations.

Appreciating the everyday luxury experience they've come to love and expect from us, our clients continue to enjoy our existing and new boutiques while also showing a growing affinity to shop with us online. Client enthusiasm for our eCommerce channel sustained its accelerated momentum in third quarter with revenue up 78.5% despite most of our boutiques being open.

Ongoing investments online continue throughout the quarter as Jennifer will speak to shortly. The ability to deliver new features and functions on our digital platforms allows us to thoughtfully expand our online capabilities, replicating the same everyday luxury experience our clients enjoy in our boutiques.

Our boutiques and eCommerce channel complement one another and our clients have a growing affinity to flexibly shop with us whenever, wherever. Our Omni channel clients spend three times more than both our retail exclusive and our eCommerce exclusive clients. Due to this, we will continue to build open boutiques and invest in our eCommerce channel, deepening our clients' loyalty.

Across our boutiques and online, our fall/winter assortment is arguably the best product season we've had ever at Aritzia. We have multiple programs across categories driving our businesses, resonating with our clients' evolving lifestyle. With a stronger than expected season and a purposefully conservative initial buy, we experienced sell-outs across all our key programs.

To capitalize on the demand, we did our best to mitigate these product shortages. However, with global transportation compromised due to the pandemic, we are somewhat inhibited in our ability to do so. Our wide assortment, coupled with our product strategy of testing and reacting to highly productive programs, has always served us well and will continue to do so into the future.

In marketing, we continue to produce captivating campaigns including our well-received holiday gift [indiscernible] (00:08:54), which reflected and embrace our clients' current stay-at-home lifestyle. This is mirrored in our product catalog where we continue to feature models at home with great efficiencies gained as we learn and adjust with each new season. Not only is this unique approach grounded in our prioritization of health and safety, it resonates with our clients' reality.

During the quarter, we also introduced our With Love brand campaign rooted in celebrating fearless individuality and our diverse Aritzia community, a reflection of our ongoing investment in diversity and inclusion. In short, I am proud of our entire team's achievements as we close another challenging yet successful quarter.

I will now turn the call over to Jennifer to give you an update on some of the key areas of our operations. However, before I do, I would like to congratulate Jennifer on the November cover story in The Global and Mail Report on Business where she was duly recognized as one of Canada's best executives.

Jennifer Wong

President, Chief Operating Officer, Corporate Secretary & Director, Aritzia, Inc.

Thanks, Brian, for the very kind introduction, and good afternoon, everyone. I trust you had a peaceful holiday season with your families and a chance to reflect and take a moment as we step into the new year.

Looking back, we knew this holiday would be far from normal due to the pressured conditions imposed by COVID-19. Yet, I continue to be proud of what our team has achieved through tremendous adaptability, focus and resilience. We successfully executed another strong holiday season while making considerable progress to advance our long-term strategies. And we achieved all of this while continuing to uphold our industry-leading health and safety standards and ensuring our people whose jobs were affected by mandated COVID measures had income continuity.

I want to touch on three areas of focus within operations this quarter: first, the efficient and effective management of our distribution center and Concierge teams to support our peak holiday period; second, the continued investment in digital capabilities to elevate our Omni channel offering. And finally, the fulfillment of our responsibility as a corporate citizen by giving back to the communities where we live and work.

We began prepping for our peak holiday period at mid-fall with the hiring and training of nearly 800 seasonal associates across our distribution centers and expanded our Concierge team with the addition of almost 180 permanent and seasonal staff and redeploying 100 retail style advisers from temporarily closed boutiques. By all standards, it was an historic Black Friday for Aritzia. We achieved record-breaking performance on several fronts. On Black Friday alone we recorded nearly 1 million visits on aritzia.com, and over the entire event, our distribution centers picked, packed, and shipped more than 1 million units, forging new all-time records at two of our DCs while our Concierge team facilitated more than 120,000 client interactions over e-mail, chat, and phone.

And in particular, I'm proud of the manner in which our DC and logistics operations pivoted in response to industry-wide carrier delays. Above and beyond our efficient daily operation, our teams acted with swift operational dexterity, making real-time adjustments to mitigate these carrier delays.

Our Omni channel experience was another point of pride in the quarter and our boutiques warmly welcomed our clients with exceptional service. Our eCommerce team seamlessly mirrored that experience online with enriched functionalities while our Concierge team engaged our clients with quality care across both channels.

Our Concierge function was established in 2012 with the start-up of our eCommerce website. It has grown over the years alongside aritzia.com, including the migration to a new case management system under the SAP platform and a new integrated and vastly expanded phone system early this year.

We also hired a seasoned Vice President of Concierge just in time to lead through an exceptionally busy holiday period, talk about hitting the ground running. And while our team has done a phenomenal job to-date, we are further investing to take every aspect of this growing operation to the next level. We will evolve and integrate our people, processes, and technology in this critical area to support our accelerated eCommerce growth and elevate our Omni channel offering to delight our customers.

During the quarter, we continued to invest in our digital capabilities to enrich our multi-channel client relationship. We made enhancements to site navigation and invested in personalization. This included the opportunity for clients to customize their Super Puff and an AI tool for size and fit, which has already been used by hundreds of thousands of clients. In addition, we introduced free shipping and free returns to support our continued US expansion. And as I mentioned on the last call, we launched our Afterpay partnership in November.

While the concept of buy now, pay later is relatively new in Canada, this payment option [ph] shared (00:14:48) eCommerce transactions is growing globally particularly amongst Gen Z and millennials. With limited marketing to-date, we've already seen higher average order values, and Afterpay is proving to be an attractive choice for our clients to transact with us. Our investment in our digital selling tool, the Clientele App, is also continuing to drive higher average order values and conversion. We remain excited about the app's potential and expect to roll it out across all of our boutiques in the coming months.

And finally, we're planning additional Omni capabilities to integrate our boutiques with our eCommerce channel. As a result of the recent reclosure of our boutiques in Ontario and Québec, we introduced a new Call & Collect service whereby our clients may purchase online through our concierge and pickup curbside at a closed boutique.

And starting in fiscal 2022, we will introduce functionalities such as store inventory visibility; buy online, ship from store; and buy online, pick up in store. These initiatives allow our clients to shop precisely where, when, and how they prefer while driving sales and conversion as we optimize inventory across our network.

And with the impact of COVID-19 reducing many companies' ability to give during the holiday season, we were grateful to be able to sustain our corporate giving program. With the support of our people and our loyal clientele, we continued to give back to our communities where we live and work.

Through our Aritzia Community giving program, we donated holiday backpacks filled with comfort essentials to youths experiencing homelessness in Vancouver's Downtown Eastside and partnered with local agencies to gift 1,000 Super Puffs to women and girls in need across Canada.

And lastly, with COVID numbers escalating in many parts of Canada as the year drew to a close, we extended our Aritzia Community Care Program to even more people on the virus's front line. In 2020, we gifted a total of 110,000 clothing packages to healthcare heroes with our heartfelt appreciation.

And despite the massive disruptive nature of COVID-19 this past year, we continue to successfully navigate the uncertainty with agility. We redoubled our focus on managing through the virus resurgence and it's been tremendously rewarding to see all that we've accomplished. While we could not have imagined this kind of strain pre-pandemic, it's made us all that much wiser and stronger. As Brian noted earlier, our performance under the wake of COVID is a compelling indicator of just what we can and will do once it's over.

I'll now turn the call over to Todd to discuss our financial results.

Todd Ingledew

Chief Financial Officer, Aritzia, Inc.

Thanks, Jennifer, and good afternoon, everyone. We're extremely pleased to have delivered positive revenue growth in the third quarter. The sustained strength in our eCommerce channel and the higher than expected demand in our reopened boutiques demonstrated our clients' enthusiasm for our Fall/Winter product. Our revenue growth contributed to meaningful cash flow generation, leaving us in a solid cash position at the end of the quarter.

In the third quarter, we generated net revenue of CAD 278 million, up 4.1% from CAD 267 million last year. As Brian noted earlier, we are pleased with the sustained momentum in our eCommerce channel, which delivered 78.5% revenue growth year-over-year, driven by meaningful increases in both traffic and conversion.

We have reopened all of our boutiques by September 9 at the start of the third quarter. Despite severe capacity restrictions and reduced operating hours, open boutiques in the quarter trended on average at 81% of last year's sales productivity levels, up from an average of 70% in the second quarter. We ended the quarter with a record Black Friday event despite the resurgence of COVID-19 and the mandated reclosure of 18 boutiques in Ontario just five days before Black Friday.

Gross profit in the third quarter was CAD 126 million and our gross profit margin was 45.3%, up 60 basis points from 44.7% last year. The improvement in gross profit margin is largely the result of higher than expected rent abatements and lower product costs. These benefits were partially offset by the deleverage from reduced retail revenue and higher warehousing and distribution center costs that were driven by the growth in our eCommerce business.

SG&A expenses were CAD 75 million, up CAD 11 million at 26.8% of net revenue compared to 24% last year. The increase is driven by CAD 5 million for health and safety protocols related to COVID-19 as well as continued investment in world-class talent across key areas of the business.

Adjusted EBITDA was CAD 55 million for the third quarter compared to CAD 58 million last year. Despite the ongoing impacts of COVID-19, we generated free cash flow of CAD 68 million in the quarter, reflecting our strong revenue performance as was prudent inventory expense and working capital management. We ended the quarter with a cash balance of CAD 174 million and access to the CAD 100 million under our revolving credit facility which was repaid in full during the quarter.

Inventory at the end of the third quarter was CAD 138 million, up 12.3% from the end of the third quarter last year. The increase year-over-year reflects higher inventory in transit associated with reorders of highly productive styles to meet demand in the fourth quarter. Due to the strength of our performance in the third quarter, we have less seasonal sale inventory compared to last year. Therefore, we are well-positioned with clean inventory as we head into the end of the fall/winter season and the launch of spring. Overall, the third quarter was indicative of the strength and resilience of our business.

Given the uncertainty in the operating environment, we will not be providing specific guidance for the fourth quarter. Instead, I will share some recent trends in our business performance. Driven by our product offering which is resonating with our clients' evolving lifestyle and our effective marketing strategies, our eCommerce channel has sustained its strong momentum. Productivity levels quarter-to-date in our open boutiques are trending similarly with those we saw in the third quarter. However, the severe capacity restrictions and evolving nature of COVID-19 makes it difficult to know if this trend will continue.

Combining these factors with the mandated closure of 39 boutiques in Ontario and Québec, we expect significant pressure on our retail performance. While the closures are expected to extend through the end of the fourth quarter, we believe our eCommerce business is well-positioned to moderate the impact of these measures.

Turning to gross profit, we expect continued higher warehousing and distribution center costs from growth in our eCommerce channel and we have not factored in any benefit from further rent abatements. We also expect to

incur higher air freight costs as we chase demand of highly productive styles, all putting pressure on gross profit year-over-year in the fourth quarter.

Further, fourth quarter SG&A expenses are expected to see a similar year-over-year increase as compared to the third quarter. The increases are driven by our ongoing operating expenses of approximately CAD 5 million per quarter related to our health and safety protocols as well as continued investment in talent. These increases will be slightly offset by some variable cost savings from boutique closures. In addition to these puts and takes, we expect deleverage from reduced retail revenue in the fourth quarter will impact gross profit margin and SG&A as a percentage of net revenue.

Our strong financial position with CAD 274 million of liquidity in place at the end of the third quarter enables us to weather further uncertainty while continuing to take advantage of unparalleled opportunities and strategically invest in critical infrastructure across our business. Despite near-term headwinds, our business model continues to prove resilient throughout the pandemic. Momentum behind our eCommerce channel remains strong and we are optimistic of recovery is in sight. As we look ahead, we remain confident that we are well-positioned to capitalize on the opportunities to deliver profitable growth and create long-term value.

With that, I'll now turn it back to Brian.

Brian Hill

Founder, Chief Executive Officer & Chairman, Aritzia, Inc.

Thanks, Todd. As Todd mentioned, the resurgence of COVID-19 has led to the temporary reclosure of 39 boutiques across Ontario and Québec during the fourth quarter thus far. We are working closely with our landlords for further rent abatements in light of the current closures, recognizing this is a difficult time for both parties. We're thankful for their ongoing support and their partnership.

There's no playbook for managing through a global pandemic and the last few months have proven yet again the virus's unpredictability. Effectively managing the ever-changing impacts of COVID-19 remains our number one priority as we continue to progress with the many exciting opportunities ahead.

With our eCommerce business significantly expanding its footprint, this is not only a meaningful sales contributor. It drives significant in-boutique traffic and, in turn, our boutiques drive traffic online. As we expand our product offering and Omni channel capabilities, the seamless relationship between our online business and our boutiques is essential to our growth. They work together to service our clients whenever and wherever.

To capitalize on this multi-channel client relationship, in addition to continued digital investments online and in our boutiques, we're developing an even broader suite of Omni channel capabilities and further investing in our concierge services. Together, these contribute to an elevated Everyday Luxury experience.

We're also continuing to open new boutiques across North America in increasingly available premier locations, capitalizing on the extraordinary financial terms being presented. By the end of the fiscal year, we will have opened a second Super World boutique in Los Angeles and opening in a new market, Honolulu.

And for fiscal 2022, we already have a healthy pipeline of new boutique openings with additional opportunities under consideration. We will continue to expand our product lines from new categories such as intimates and swim to extended depth including sizes, colors, and length; and breadth, more new styles, building on our highly productive programs, all of this contributing to our five-year plan to double our current style count.

And, as always, we will invest in infrastructure. With the unique availability of world-class talent, we will continue to grow our high performance team at all levels, evolve our processes for even greater efficiency, and expand our technology suite as required as Jennifer shared.

Now that we have reached the end of our previous five-year plan, we are building a refreshed plan which we hope to share with you in the foreseeable future. This understandably is a fluid process given the current uncertainty. We are confident, however, that fundamentally, our strategic growth levers, as previously discussed, are on point and we have the foundation in place to capitalize on a potential post-pandemic.

Close, I would like to thank our people and our clients. Our results over the past several months are testimony to the talent of our world-class team and our clients' enduring loyalty. I'm also very grateful that through the enormous effort of our Aritzia Community health and safety team, our people, our clients to date there continues to be no confirmed community spread of COVID-19 virus within any of Aritzia's workplaces.

Finally, I would like to thank our investors and everyone on the call. Your patience, support, and commitment to Aritzia through this uncertain period are deeply appreciated. I look forward to continuing to share our exciting story with you.

Helen?

QUESTION AND ANSWER SECTION

Operator: We will now begin the question-and-answer session. [Operator Instructions] The first question comes from Mark Altschwager with Baird. Please go ahead.

Mark R. Altschwager

Analyst, Robert W. Baird & Co., Inc.

Q

Good afternoon and really nice performance through this challenging time. To start out, I was wondering if you could just give us a bit more detail on the revenue trends you're seeing quarter-to-date. Were you able to sustain positive revenue growth through the holiday period? Sounds like response to the products has been great. I'm just trying to get a better sense of the ability to offset those reclosures with the digital business through December.

Brian Hill

Founder, Chief Executive Officer & Chairman, Aritzia, Inc.

A

Yeah. Thanks for that question. It's devastating that, unfortunately, they timed the closures where the highest volumes were going to occur and I don't think that's an accident, unfortunately, the same way. There's a lot of places got shut down in new year. So, for us, they did it. We had a bunch of stores. 18, I believe, Todd...

Todd Ingledew

Chief Financial Officer, Aritzia, Inc.

A

Yeah.

Brian Hill

Founder, Chief Executive Officer & Chairman, Aritzia, Inc.

A

...closed just before our busiest week, Black Friday. And then they closed another – all the rest of Ontario and the rest of Québec just in time for December 25. That was an early Christmas present for us, December 25, just in time for Boxing Day and Boxing Week. So, Ontario is our biggest market and Québec is a very solid market for us as well and so we're going to feel that. I'll let Todd get into specifics, hand it over to him but it hurts. I mean we have a great eCommerce channel but we're an Omni channel retailer and we think that's our competitive edge. And we think our customers like shopping in all channels, as I suggested. So the minute we shut down one of our main channels and our best markets, we feel that that's for sure. Todd?

Todd Ingledew

Chief Financial Officer, Aritzia, Inc.

A

Yeah. Mark, obviously we had, as Brian was just saying, the 39 boutiques closed right as we started our holiday sale season. And those closures are expected to continue through the end of the quarter but we do – we have seen that the productivity levels in our open stores is that trend is continuing as it did in the third quarter, so right around 80%. And then our eCommerce channel has also continued with the strong momentum into the fourth quarter.

So, we're pleased with that and we do expect that again, the eCommerce channel will be able to moderate the impact of the boutique closures and frankly, the severe restrictions that were under in our open boutiques.

Brian Hill

Founder, Chief Executive Officer & Chairman, Aritzia, Inc.

A

And what's encouraging, though, is how our boutiques bounced back when they did open after the initial closure back in the spring and how they bounce back and how they grew even with the severe restrictions. As Todd mentioned, I mean we're at 81%. Some of our stores have 25% capacity limitations on them. So a lot of them do and they all have – almost all of them have capacity limitations and that, coupled with reluctance of a lot of customers to go out and leave their house and lockdown orders in different places and discouragement from the leadership, governments and political politicians for people to go out.

So against all that in that backdrop, it's given us even more confidence that after these stores reopen and with hopefully this pandemic getting behind us with the vaccinations, that we will actually come – business will see some pretty meaningful growth almost immediately with our eCommerce channel as we mentioned not going back to former levels, but staying close to where it has been.

So, we're pretty darn excited. We're kind of looking past this period and because of – and partially because there's nothing we can do about it but – and we don't really have a choice, but we're looking past this period. I'm super excited about what we see in front of us.

Mark R. Altschwager

Analyst, Robert W. Baird & Co., Inc.

Q

That's really helpful. And I guess along those lines, Brian, maybe could you speak to some of the biggest learnings you had from this massive acceleration in the digital business this year? How does that impact the strategy moving forward in terms of stores versus digital and how you're looking to invest in areas like digital marketing?

Brian Hill

Founder, Chief Executive Officer & Chairman, Aritzia, Inc.

A

Well, I think that we got a lot of the learnings in the spring because once again, when all our stores closed, we didn't really have a choice. So that was – we started the learning and the biggest one and which has fueled all our product initiatives is the fact that when we're online, we don't have limitations for the breadth of our product and the types of product mix. And that's why we're out pursuing these initiatives, which where we think coupled with the world-class talent that's out there is enabling us to do so.

I mean even if we wanted to do it three years ago, I'm not sure that talent is available. They were all at other places but with a lot of the industry struggling, a lot of retailers either bankrupt or on the verge of bankruptcy, we've managed to bring in talent and understand and be able to expand our product base. So that's probably the biggest one is the fact that our eCommerce channel doesn't have the walls and those restrictions that our retail has.

On the other hand, what is so encouraging for us is how good our retail has been. I mean to think that with all these restrictions, all the health orders in place, all the capacity limitations in place, that our business and our stores are performing at 81% of their capacity – of last year is just shocking to us. If you [ph] listed (00:34:55) to me a year ago that we're going to have capacity limitations at 15% or 25% and 50% in different places and we're going to have a pandemic which is going to – keeping people in and everything else and then with all the hassles of health and safety precautions and everything else that we'd be at 81%, we'll just be like, no, not a chance.

So it's made us recognize that our customers, and particularly our good customers, as we mentioned, would spend 3 times the amount of money of our single channel customers. Our dual channel customers and multi-channel customers spend so much more money that they want – our best clients want that ability to shop in all our channels and will continue to do so.

So I think initially with the pandemic, it was a big aha with eCommerce. However, as this continued, it's been more of a big aha back with retail saying, hey, it's not going anywhere. And certainly for Aritzia, it's not going anywhere and that, coupled with the opportunities that we've seen out there with real estate and just – even just the locations that are available to us, that perfect storm is – we think, is going to lay us a foundation for the next decade-plus.

Mark R. Altschwager

Analyst, Robert W. Baird & Co., Inc.

Q

That's great. Thanks for taking my questions and best of luck this year.

Operator: The next question comes from Irene Nattel with RBC Capital Markets. Please go ahead.

Irene Nattel

Analyst, RBC Capital Markets

Q

Thanks and good afternoon, and really congratulations on a heroic performance this quarter. Wondering – just thinking about – you talked a little bit, Brian, about some [indiscernible] (00:36:44) that the changes that you're seeing in productivity or the learnings for online. But in terms of how the boutiques operate and how the two of them integrate and how the concierge – the sort of the increased concierge is performing, how does that make you think about the business on a post-pandemic basis and maybe any changes or sort of shifting that you'll do?

Brian Hill

Founder, Chief Executive Officer & Chairman, Aritzia, Inc.

A

Thanks, Irene. I think first and foremost, what our clients want is that Everyday Luxury experience and that's not going to change. And that's shown not to change pre-pandemic, during the pandemic, and we think post-pandemic. We think our product offering and the value of our offering and customer service levels and the product and everything else that we do in environments they shop in, they still want to be.

I mean I think when we opened our Super World store, there's not a lot of exciting things happening in the world when opening and things like that and positivity around. So now, when we do do it and we do do some of these things and we've offered incredible new product because we did such a great job of – I'm not tooting our own horn so much but we did such a great job of cleaning out our spring and summer merchandise that we entered fall with a massive position of strength with a brand-new collection and no lingering effects of the spring and summer collection that the customers respond to that.

So people are still going to wear clothes. People are still going to want exciting new product. People are going to still want innovation and things and so they're still going to do that. And then as on a multi-channel perspective, they're going to want to have all this flexibility; a buy online, pickup in store and see store visibility and all the different things that Jennifer and her team are working on as far as ensuring that we continue to be flexible and allow customers to enjoy this rich experience anywhere.

So ironically, I'm not sure some people's habits will certainly change and change forever but I'm not sure people will change. And I'm not sure people will change how they go about and what excites them and what they want to do and what thrills them. And so I don't think people will change. I think their habits will change and we've already seen how they're going to change. So we think we're extremely well-positioned here to continue to prosper post-COVID.

Irene Nattel

Analyst, RBC Capital Markets

Q

That's great. Thank you. And, yes, what will thrill us will be to get out of the house finally. So as you're preparing for the spring and summer, and then particularly with what is likely [indiscernible] (00:39:34) some reopening, how are you positioning the mix, order levels, et cetera, given all this uncertainty around timing?

Brian Hill

Founder, Chief Executive Officer & Chairman, Aritzia, Inc.

A

It's interesting. I mean we've been fortunate to have our eCommerce be so strong so that the dichotomy of our sales between all our stores and our eCommerce channel functioning and just the eCommerce channel functioning and operating when the store is closed, the dichotomy of that sales revenue isn't that great that we can't sort of go in with a more conservative buy, assuming everything's going to be up and running, which will also be perfect amount of inventory for whatever reason things are limited.

So we're making sure from a product perspective that we're well-positioned, we're able to chase. As I mentioned, we had a little bit harder time chasing our product this season and it was not primarily the factories and the mills. It was the transportation and the clogs in transportation, that we had challenge in our air freights. There isn't as many airplanes flying, so the ones that were were full and so even those were taking longer. There wasn't as many ships going across the ocean so they were taking longer and everything was taking longer.

So it didn't give us the opportunity to respond. We went in with a conservative buy, which I do 1,000 times over because who knew what was going to happen and then we had such a great response. We tried to scramble as we normally do to repeat and as we test and repeat. And we tried to facilitate these orders but it was actually the transportation which was – end up being more of a challenge than not. And prices and everything else from that

transportation were [ph] in some of the cases (00:41:22) 5 and 10 times what they normally were, depending on where it was coming from and the timing of it.

So we're going to continue to buy. From a fashion perspective, it's a good question. If people change how they're shopping for clothing and you'll stay-at-home kind of wardrobe is where it's at. If you read some of the fashion magazines, people though suggest they've had it with this home – stay-at-home product mix and they want something a little bit – certainly women want something a little bit more fashionable and perhaps even sexier and everything else [indiscernible] (00:41:59).

So it will be interesting to see what happens. We're ready for it, though, and we're going to embrace it and we think what's going to happen after is going to play right into our sweet spot of what we do at Aritzia.

Operator: The next question comes from Stephen MacLeod with BMO Capital Markets. Please go ahead.

Stephen MacLeod

Analyst, BMO Capital Markets Corp. (Canada)

Q

Thank you. Good afternoon and congrats on a great solid performance. Just had a couple questions. Lots of great color so far, so thank you. I just wanted to turn a little bit on the closed stores, right? I think in your prepared remarks, you mentioned or maybe it was Todd, I can't remember. But you mentioned something about curbside pickup and buy online, pickup in store. Are those new offerings for Aritzia? I was also under the impression that you didn't have curbside pickup previously.

Brian Hill

Founder, Chief Executive Officer & Chairman, Aritzia, Inc.

A

Yeah. We didn't have it previously. I mean this is just efforts we're making here. It's not meaningful enough to our business at this point in time and I think partially because our eCommerce channel is so good and that our distribution center, I can't remember the KPIs, but we're getting an order before noon today and I think it's getting shipped out or prepared and packed and everything before the end of the day. Is that right?

Jennifer Wong

President, Chief Operating Officer, Corporate Secretary & Director, Aritzia, Inc.

A

Pickup. I think cutoff, it's for 5:00.

Brian Hill

Founder, Chief Executive Officer & Chairman, Aritzia, Inc.

A

Cutoff is when?

Jennifer Wong

President, Chief Operating Officer, Corporate Secretary & Director, Aritzia, Inc.

A

For 5:00, the end of the day when the trailer comes.

Brian Hill

Founder, Chief Executive Officer & Chairman, Aritzia, Inc.

A

Yeah. And so our eCommerce – I think curbside pickup is certainly meaningful to some. It hasn't been as meaningful to us. We are offering it. We think some of the buy online, pickup in the store and some of these other opportunities that we're going to be working on early in the year are going to be more meaningful. But I think Jen

just shared that. It's not particularly meaningful to our business at this point in time and I think it's just generally because it's Ontario and Québec only where our stores are closed.

And the customers still like coming into our stores that are open. There's no question about that and our eCommerce is so effective at turning in. If you're in Toronto and you order something before noon today, you could potentially get it by tomorrow morning. And so we just found that our eCommerce channel is so efficient that people just prefer that meaningfully over curbside pickup and things.

Stephen MacLeod

Analyst, BMO Capital Markets Corp. (Canada)

Q

Right. Okay. No, I see that. That's great. Thank you. And I was just curious if you could give a little bit of color around rent abatements in the quarter to be able to quantify sort of what that number was.

Brian Hill

Founder, Chief Executive Officer & Chairman, Aritzia, Inc.

A

Go on.

Todd Ingledew

Chief Financial Officer, Aritzia, Inc.

A

Yeah. The rent abatements, they were approximately 330 basis points of benefit in the quarter.

Stephen MacLeod

Analyst, BMO Capital Markets Corp. (Canada)

Q

Okay. That's helpful. And then I just had – just wanted to get a little bit of color around, Jennifer, you mentioned the Clientele App. And it sounded like there was something that was being rolled out. Just wondering if you can give an update on where you are in terms of that [ph] because of (00:45:12) specific investment.

Jennifer Wong

President, Chief Operating Officer, Corporate Secretary & Director, Aritzia, Inc.

A

Yeah. I've been talking about that app for a few quarters now and I just wanted to give an update that we are still rolling it out in respectively phase two. I think and maybe it was the last quarter, the quarter before, I mentioned that we had piloted it with only 25 style advisors. I believe we're up to closer to 500 to 1,000 style advisors where we're working our way towards close to 200,000 style advisors. And certainly, with the stores closing and reclosing, it's been a really valuable tool for us to continue to connect with the customer and still [ph] service her (00:45:49).

So I just wanted to remind everyone that that's still a really important aspect of our Omni channel offering and that we continue to roll it out. And our goal is to be able to roll it out to all the boutiques eventually.

Stephen MacLeod

Analyst, BMO Capital Markets Corp. (Canada)

Q

Right. Okay, that sounds great. And then maybe just finally, Todd, I missed some of your commentary around the gross margin outlook and you had highlighted some of the puts and takes. And I was just wondering if you could just quickly gloss over that.

Todd Ingledew

Chief Financial Officer, Aritzia, Inc.

A

Sure. So maybe I'll start. Brian has alluded to it but we did start the quarter in a very healthy inventory position and had lower seasonal sale products. So that we do expect that that will drive lower markdowns and improve – like continue to improve product cost margins in the fourth quarter. So there is a positive there showing the underlying health of the business but we do expect to continue to have higher warehousing and distribution center costs from our growth in our eCommerce volume and additional air freight from the chasing of demand of our highly productive styles from the last few months. And then obviously the closure of the 39 boutiques in Ontario and Quebec that will generate some deleverage. But I think putting it all together net-net, we are expecting to see slightly more pressure on gross profit in Q4 and then removing the rent abatements.

So when you look at it as a whole, we will see more pressure than we did with all the puts and takes in the third quarter. But again, that's before taking off the rent abatements. And then we're not anticipating at this point the same level of rent abatements that we got in the third quarter.

Stephen MacLeod

Analyst, BMO Capital Markets Corp. (Canada)

Q

Okay. That's great color. Okay. That's great. Thank you. That's it for me.

Operator: The next question comes from Derek Dley with Canaccord Genuity. Please go ahead.

Derek Dley

Analyst, Canaccord Genuity Corp.

Q

Yeah. Hi there. Just a couple of quick ones for me. So just in terms of your commentary on store openings next year just given the really favorable lease rates you guys are seeing, can you sort of help us quantify what you expect? Should we expect a similar number of store openings in 2022 as we saw on 2021?

Brian Hill

Founder, Chief Executive Officer & Chairman, Aritzia, Inc.

A

That's an interesting question. So the fact that we've actually in this year of the pandemic have – will have by the end of the year, I believe, have seven new stores and three repositionings, probably it has more to during deals pre-COVID. I know the first three, four months of this year we didn't do a ton of deals. They did a couple because we signed off on a couple because we couldn't resist because the deals were so good. So we've been sort of a little bit more bullish on the back half of the year as far as signing deals. I don't know where we are.

Once again, we're not going to rush things as well and take secondary locations or do deals that we don't feel comfortable with from a financial perspective nor deals that we're not getting proper protection on language, which has been a bit of a challenge with an ongoing pandemic or a further additional pandemic. We want to make sure we have language protecting, covering us there that we're at least, if nothing else, sharing the burden of the situation in the future.

That said, I mean, if we thought previous, there was not many people out looking for new locations. Now there's even less. So we're one of the few people out there and we're opening as many stores as we can. I haven't had a real estate update since early November. We've talked on some things, but a full scale one. So we hope to have one in the next week or two weeks to find out what the team has been working on.

And I think we've approved a few deals so far, but there's a bunch that are approvable. So, we'll see how that shakes out and one ends up coming to fruition or not and we'll go from there and we'll let you know we'll have probably better handle on the next – our next update.

Derek Dley

Analyst, Canaccord Genuity Corp.

Q

Okay. No. No. That's helpful. And then just thinking about the holiday selling season that you guys just went through a number of other retailers kind of pointed to how much more of an extended selling season started earlier probably ended earlier as well compared to past years. Did you guys see something similar?

Brian Hill

Founder, Chief Executive Officer & Chairman, Aritzia, Inc.

A

Are you talking about off-priced portion of that season?

Derek Dley

Analyst, Canaccord Genuity Corp.

Q

Yeah. I guess I'm talking about the sales portion of the holiday season. And I guess just incremental – when the incremental demand came in a little bit.

Brian Hill

Founder, Chief Executive Officer & Chairman, Aritzia, Inc.

A

Yeah. So as I mentioned in my commentary that we broke early this year. We're anticipating the governments were mulling over, shutting things down in Toronto and Peel, and also for health and safety reasons. We want to spread it out a little bit. So we started it a week earlier than we had up in the past. It's not something we want to continue to do in the future, but we thought based on the environment that was out there, we thought we'd do that and so we did that.

We haven't really ended things any sooner although we did go back to full price and all our products that we were carrying over a week sooner than we typically do. We're cognizant of the off-price activity we've had in the last 12 months. Obviously when the virus hit, we went off-price, couple weeks after the stores closed down, online we had our regular spring-summer sale. It probably extended a little longer than we normally do because we did have a lot of inventory and we wanted to start the new season fresh. We've now started the fall promotional period about a week sooner.

So we are cognizant of how much off-pricing we've been doing and we want to get back and think we can get back to our normal process and off-pricing calendar sort of from hereon in. And so we have been off-priced a little bit more. Because of that, we saw the uptake little sooner, but from a sales perspective from timing. And then, of course, closing of 39 boutiques before Boxing Week in Canada, which is a big deal, that hurt a little bit. But we hope to be off-price next year and we think the sales channels and the sales periods will start reflecting very similarly than they have in the past.

Derek Dley

Analyst, Canaccord Genuity Corp.

Q

Okay. Terrific. Thank you.

Operator: The next question comes from Meaghen Annett with TD Securities. Please go ahead.

Meaghen Annett

Analyst, TD Securities, Inc.

Q

Thank you. Good afternoon. Could you talk a bit more about how traffic patterns at the peaks trended through the quarter? And at what level did you see store productivity peak?

Todd Ingledew

Chief Financial Officer, Aritzia, Inc.

A

[indiscernible] (00:53:52) and then store productivity peaking, when did it peak?

Brian Hill

Founder, Chief Executive Officer & Chairman, Aritzia, Inc.

A

Well, typically we used to have our store productivity in our store traffic everything we used to peak around Boxing Week and the week before Christmas and the week after Christmas. So the last two weeks of December. With the advent in Canada and – but the US was almost so, we kind of used to refer to it, not too long ago as a single hump camel versus a two-hump camel. In the US, we have the two-hump camel because we had Christmas last two weeks rush. And then we also had the Black Friday event.

And then in Canada when we introduced the Black Friday event, we got with Canada now. And so we do see this two-hump, which we actually think works a little bit better because it doesn't burn all our teams out right at a time when they want to be spending time with friends and family and things like that too. So we've seen this two-hump camel per se with our sales. And so from a peaking perspective, that hasn't changed. It's kind of the same. Now are you referring to stores and productivity based on COVID or are you talking about activity based on COVID or are you talking about selling periods in general and what has been changed this year?

Meaghen Annett

Analyst, TD Securities, Inc.

Q

So it's more so a question as to where store productivity was when we saw cases really come down and perhaps people returning back to stores to get out of the house and whatnot during that period. Did we see productivity get back up to 100% at any point in time?

Brian Hill

Founder, Chief Executive Officer & Chairman, Aritzia, Inc.

A

Do I see it getting back up to 100%? I don't think it will get back up to 100% because I just think, as I say, people haven't changed but their habits have. And I think a lot more people will be shopping online going forward. So I suspect that we won't see the same numbers we have although I don't see this catastrophic collapse either and we've shown that even during COVID with 81% productivity in our store. So we think after COVID it could get up close to 100%. And I'd love to see it 100% and our eCommerce channels stay with its same growth that it's been on since COVID. But realistically I don't really see it going back to 100.

I don't know if it's going to be at 80% or 70%. But I agree there was a little bit after the stores have been closed for so long, there's a little excitement to get back out in the stores. On the other hand, COVID was still around and still persisting, and people were still getting out.

So I don't know where we're going to net out at this point in time. We've run models at 70% up to 90%. We haven't been bullish in running them at 100%, and we haven't, we don't see any reason why they'd be below 70% at this point in time. But that's where we kind of predicted it'd be probably be 70% to 90%. And the average there is 80%, which is very close to where we were prior to our stores closing down.

Meaghen Annett

Analyst, TD Securities, Inc.

Q

Okay. That's great color. Thank you. And then wondering if you can give any details on the progress being made maybe more so internally with respect to product expansion? Is there anything to note that maybe the consumer isn't seeing yet? Can you talk specifically about any new categories you might be introducing in the near term?

Brian Hill

Founder, Chief Executive Officer & Chairman, Aritzia, Inc.

A

Well, the near term, we're not introducing any new categories this fiscal year, which is six weeks left in this fiscal year per se. We hope to be introducing one of our new categories in Q4 just in time for Q4 just before Q4 next year. And the other one is late Q4, early Q1 next year, our two main issues being swim and intimates. We've already seen – we've already been adding colors and length, and we hope to have that in full-blown by this spring and our spring launch. We're going to have more colors and more lengths in our stores. And we've already introduced more sizing last year or so this year than we're in now.

So we see some of those. And then as far as some of the other categories we're expanding, just expanding styles and existing lines and things like that, we're already doing some of those, but not all of those. So if you look at the chart and we think we're going to double our breadth of product within five years and we're kind of arguably a year in and we're probably 20% of the way to that new goal, and we hope to be another 20%, maybe even slightly ahead. We've been very successful in putting the teams and the infrastructure together and we are right on our calendars of what we put in place as far as these introductions. So we're pretty optimistic that we'll be able to achieve all our aspirations on the product side here.

Meaghen Annett

Analyst, TD Securities, Inc.

Q

That's great. Thank you.

Operator: [Operator Instructions] The next question comes from Mark Petrie with CIBC. Please go ahead.

Mark Petrie

Q

Yeah. Good afternoon. I just wanted to follow up on a couple things. First just with regards to your sort of purchasing and planning for spring/summer, would you say you're similarly conservatively positioned as you were heading into fall/winter? Or have you been able to adjust just given sort of the strong sustained demand you've seen particularly in eCommerce even amidst the lockdowns?

Brian Hill

Founder, Chief Executive Officer & Chairman, Aritzia, Inc.

A

I would say we're probably a little less conservative for spring/summer than we were for fall/winter. We were bullish in some of our areas of our business for fall/winter and conservative and others. And now we're probably a little less conservative. We're still working through our eCommerce and we still need to be conservative, not only because of the virus, but the composition of our eCommerce and retail sales. Our buys on eCommerce look different than our buys in retail. As I mentioned earlier our retail we have four-wall limitations as far as the breadth of product we can supply, and online, we don't. And so we're still sort of a little reticent in committing too much one way or the other because the buys look slightly different between the two channels.

So understanding that and then also understanding COVID, but we're certainly not conservative when it comes to thinking from a fashion perspective and where we think fashion is going and what consumer and our customer clients' outlook will be and what kind of product they're buying.

Ironically, fashion and trends and things, although people have had to stay at home, colors and styles and shapes and fits and things, they've been evolving as we've gone along because people are still being posting on Instagram and people are still – there's still new things happening in the world. They just probably reflect a different reality from a styling perspective than they would have if the pandemic hadn't hit, but that certainly hasn't stopped. And ground to a halt, there's still as much innovation and desire for different new fresh styles and things as there ever was.

Mark Petrie

Q

Okay. Thanks. And how does your success sort of just in developing the online experience affect how you think about international growth opportunities? I think the last time you talked about it, it's understandably fallen down the pecking order of priorities just given the magnitude of the opportunity in the US. But I'm just curious how you're thinking about international today. And can you accelerate brand building without stores or do you need that physical presence in order to launch that more materially?

Brian Hill

Founder, Chief Executive Officer & Chairman, Aritzia, Inc.

A

Yeah. I mean, I think the world has proven and eCommerce-only players have proven that they don't need stores to do that. That said, we're believing that if you actually accompany things with stores, it actually has a better experience and a faster uptick. We're picking off as much of the low-hanging fruit on our international eCommerce opportunity now, we've already identified all the low-hanging fruit. I would say we're probably 20% of the way through it. We had a discussion prior to the holiday season that we just weren't – still it wasn't growing to the rate we think that we wanted nor the rate we think it should have been growing.

So we've identified we had a full audit of what we were doing and not doing and doing well and not doing well. And we've put some of those measures in place. But we think over the next three, four months, we're going to put all those measures of the low-hanging fruit in place, at which point in time then comes a little bit more of the work out if we need to continue to expand, we're going to need to be doing certain things.

So we're going to have to make shipping, low-hanging fruit, things like making shipping and duties and things like that easier, making currencies easier and things like that, a little bit higher-hanging fruit and heavier lifting is creating localized websites with content and changing product mixes and things for different markets and things like that.

So we think there's a meaningful opportunity with the low-hanging fruit and we'll see where that nets out and then we'll decide along with everything else we do and plan. What makes the most sense as far as a little bit more of the workout out stuff, high-hanging fruit that we're going to need to chase and put a bit more effort into it and whether things get in that pecking order of other initiatives are not. Low-hanging fruit, we're just going to do. That other stuff is a little bit different.

Mark Petrie

Q

Understood. Appreciate all the comments today and all the best.

Brian Hill

Founder, Chief Executive Officer & Chairman, Aritzia, Inc.

Okay.

A

Todd Ingledew

Chief Financial Officer, Aritzia, Inc.

Thanks, Mark.

A

Brian Hill

Founder, Chief Executive Officer & Chairman, Aritzia, Inc.

Thank you.

A

Jennifer Wong

President, Chief Operating Officer, Corporate Secretary & Director, Aritzia, Inc.

Thank you.

A

Operator: This concludes the question-and-answer session. I would like to turn the conference back over to Helen Kelly for any closing remarks.

Helen Kelly

Vice President-Investor Relations, Aritzia, Inc.

Thank you, Anastasia, and thanks again to everyone for joining us this afternoon. We will be available after the call to answer any questions you may have. As usual, please take care, and we look forward to speaking with you again very soon. Thank you.

Operator: This concludes today's conference call. You may disconnect your lines. Thank you for participating and have a pleasant day.

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