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Earnings Call

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Call Participants

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Mitchel John Kummetz

Seaport Research Partners

Samuel Marc Poser

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Presentation

Operator

Good morning, and welcome to Shoe Carnival's Second Quarter 2025 Conference Call. Today's conference call is being recorded and is also being broadcast via webcast. Any reproduction or rebroadcast of any portion of this call is expressly prohibited.

Management's remarks today may contain forward-looking statements that involve a number of risk factors. These risk factors could cause the company's actual results to be materially different from those projected in such statements. Forward-looking statements should also be considered in conjunction with the discussion of risk factors included in the company's SEC filings and today's earnings press release.

Investors are cautioned not to place undue reliance on these forward-looking statements, which speak only as of today's date. The company disclaims any obligation to update any of the risk factors or to publicly announce any revisions to the forward-looking statements discussed on today's conference call or contained in today's press release to reflect future events or developments.

I will now turn the conference over to Mr. Mark Worden, President and CEO of Shoe Carnival, for opening remarks. Mr. Worden, you may begin.

Mark J. Worden

President, CEO & Director

Good morning, everyone, and thank you for joining us today for Shoe Carnival's Second Quarter 2025 Earnings Conference Call. Joining me on today's call are Patrick Edwards, Chief Financial Officer; and Tanya Gordon, Chief Merchandising Officer.

Our second quarter results demonstrate meaningful progress on our corporate strategy. We beat earnings consensus by over 20% and expanded gross margins 270 basis points to 38.8%, our strongest Q2 margin in years.

Our rebanner strategy is exceeding targets. EPS declined year-over-year from our planned rebanner investments, as expected, but margins expanded faster than planned, driving our strong earnings beat for the quarter.

Since our last call, we've completed our back-to-school season, the period that defines our year. Fiscal August represents less than 8% of our days, but drives approximately 25% of our annual profits.

As we moved into back-to-school in August, we achieved a significant milestone. The company returned to positive comparable sales growth for this must-win period. Shoe Station grew sales high single digits and expanded margins. Shoe Carnival delivered positive children's category comp sales growth and margin growth. Rogan's expanded both comparable sales and margins. Every banner stepped up when it mattered most.

Let me walk through what drove these results and why it matters for our future. Three strategic decisions shaped our quarter in back-to-school success. First, we prioritized margin dollars over pursuing lower-quality, lower-profit sales. Second, we invested in inventory depth to improve availability for back-to-school. Third, we continued investing in our rebanner program despite market uncertainty.

These choices are paying off. Q2 gross margins reached 38.8%. That 270 basis point expansion came from disciplined pricing, improved mix and better inventory availability, not from deep discounting.

The rebanner strategy contribution was significant. Shoe Station outperformed Shoe Carnival by over 10% on merchandise sales during Q2 and back-to-school. Beyond top line sales gains, we're seeing a shift in demographics from Carnival's sub-\$30,000 household towards Shoe Station's over \$50,000 range. This evolution and customer mix is driving improved economics across the portfolio and reducing the corporation's exposure to economic downturns.

These new Shoe Station households shop differently. They purchase premium brands and build higher-priced baskets. The result, product margins expanded 280 basis points at Shoe Station in Q2 plus fiscal August versus the prior year.

Carnival and Rogan both expanded margins, too. But the new customer buying higher-priced premium brands at Shoe Station is the big strategic win to highlight. All of this delivered \$0.70 in EPS, beating expectations and giving us the confidence to raise our annual profit guidance range today.

Turning to back-to-school. August was our first real test of Shoe Station at scale, and we passed convincingly. We ran one campaign idea across 3 banners with ruthless simplicity. We have the brands families want at prices that make sense, heavy digital, strategic social, surgical television in rebanner markets.

The fiscal August numbers were strong. Shoe Station grew comparable sales high single digits overall, driven by the children's category growing sales high singles with margin expansion and the adult athletics category growing sales in the low 20s, also with margin growth. Notably, Shoe Carnival delivered positive children's comp sales and margin growth for fiscal August back-to-school also, despite a challenging environment to the lower-income customer.

Each banner contributed differently during back-to-school. Station attracted new higher-income shoppers. Carnival competed effectively without sacrificing economics. Rogan started its rebanner efforts toward Shoe Station and migration toward the more accretive pricing strategy. Based on encouraging sales growth results during the Rogan's rebanner start, we extended the campaign into fall.

Now let me review the latest details on our rebanner rollout progress because this is where our strategy becomes reality.

We acquired Shoe Station's 21 stores at the end of 2021. We entered fiscal 2025 with double the store count since the acquisition with 42 Shoe Station stores, approximately 10% of our fleet. Through relentless execution, we're now at 87 Shoe Station stores, approximately 20% of the company. By the end of fiscal 2025, we'll operate 145 Shoe Station stores, approximately 1/3 of our entire fleet.

By back-to-school 2026, we'll surpass 215 stores, 51% of the current fleet at Shoe Station. That's the tipping point where growth begins to overtake decline, and we become a different company.

The performance gap is developing as we anticipated. Shoe Station rebanners sales are up 8% year-to-date through August, while Carnival comps declined high singles. The Shoe Station rebanners are generating product margins 270 basis points above prior year through August year-to-date. Importantly, we are growing sales with a more affluent target we aim to attract to Shoe Station, with sales now growing in the core demographic of over \$50,000 household income.

Shoe Station's back-to-school taught us valuable lessons. We won in athletics. We expanded margins across categories. We sharply grew our children's category penetration. But despite the growth achieved, we left sales on the table in the children's category- too conservative on depth, not prominent enough in key store areas. Valuable insights captured, now we know how to grow the children's category even higher next back-to-school.

Rogan's continues to exceed expectations. August sales and product margin growth surpassed the metrics we set. Our response was decisive. Finish the rebanner process at all Rogan's locations to Shoe Station this year. The Station model works, the economics are proven. Wisconsin becomes our next Shoe Station stronghold to expand from.

Let me address to Carnival directly as transparency here is important. Carnival Q2 comps declined high single digits, though we saw sequential improvement from Q1 and sharp improvement at quarter end as back-to-school began. August showed further progress, delivering low single-digit declines, with growth in children's categories and solid athletic performance. The sub-\$30,000 income consumer faces ongoing pressure.

While we could pursue more aggressive promotions to drive traffic, we believe maintaining margin discipline is the right long-term decision versus propping up this customer segment, we are strategically shifting away from. We're managing the Carnival banner as a cash generator during our transition to Shoe Station.

Over each upcoming quarter, Carnival's percentage of our portfolio declines systematically. By back-to-school 2026, it will represent less than 49% of our company. This deliberate shift reduces our exposure to a more volatile consumer segment while we diversify our customer base by building our premium banner.

Our financial position gives us advantages many competitors do not have. As of fiscal August end, cash and securities are up double digits year-over-year at nearly \$150 million, debt is zero. While others navigate covenants and credit lines, we invest from strength. We are investing approximately \$25 million this year in our rebanner strategy with an expected 2- to 3-year ROI payback, a strong payback model and currently our highest profit return for our cash flow.

We continue to evaluate acquisitions in a disciplined fashion. Our aim is to elevate our customer demographics, expand into new markets and do so at a fair valuation.

As announced after the Q1 call, I asked Kerry Jackson to return to my executive leadership team. Kerry's 35 years with the company and over 25 years as our CFO is a great asset to have back at my side. I'm excited about this extra horsepower supporting our strategic growth initiatives.

On inventory, yes, we're heavy. This is strategy reflecting the macroeconomic volatility, not accident. Our intentional inventory investment delivered sharply improved in-stock rates on key items during back-to-school versus last year. When demand spiked in August, we captured it and drove comp sales growth with accretive margins. That availability at a lower cost basis was a key element that drove our margin expansion and our Q2 earnings beat.

We expect to normalize inventory levels in 2026, with completion timing dependent on tariffs and supply chain clarity. But understand this, with our balance sheet and our margin profile, carrying extra inventory that's selling profitably is a luxury problem. We'd rather have it and sell it than miss the sale entirely.

Looking forward, our confidence is building on multiple fronts. Our rebanner strategy is delivering strong sales and margin growth. Gross profit margins are robust and on pace to exceed our high side guidance, given current trends. We tightened sales guidance to reflect Station's and Rogan's growth and Carnival's reality. Overall, we raised our annual EPS guidance range to reflect the Q2 profit beat and fiscal August comp growth results.

Importantly, we can see the inflection point approaching. When Station hits 51% of our fleet next year, the math flips. Station growth begins to overtake Carnival decline, median income customers overtake deep discount shoppers as our core.

I'll now turn the call over to Patrick to walk through the detailed financials and updated outlook. Patrick?

Patrick C. Edwards

Senior VP, CFO, Secretary & Treasurer

Thank you, Mark. Good morning, everyone. Let me provide additional detail on our second quarter and back-to-school financial performance and our updated fiscal 2025 outlook.

Starting with our Q2 and August sales results, second quarter net sales were \$306.4 million compared to \$332.7 million in the prior year. The 7.9% change reflects our strategic focus on higher-margin business as we transform our customer mix and banner portfolio.

Our 7.5% comparable store sales decline includes approximately 100 basis points of impact from the 20 rebanners we completed this quarter. The divergent performance by banner in the quarter reinforces our rebanner strategy. Shoe Station sales grew 1.6% with essentially flat comparable store sales. Through August year-to-date, Station rebanner comps are now up high single digits.

In Q2, Shoe Carnival sales declined 10.1%, as we maintained pricing discipline despite pressure on the low-income consumer. Shoe Carnival's high single-digit comp decline in the quarter was the main driver of our overall comparable store sales decrease. Rogan's delivered approximately \$20 million in net sales, in line with our integration plans.

Let me now provide some additional color on our performance by major footwear category during August, our highest stake month of the year. Total company comparable growth was achieved with mid-singles growth in children's and low singles growth in athletics. Shoe Station far outperformed the total company, achieving high singles growth in children's and low 20s growth in men's and women's athletics.

Total company men's and women's nonathletics declined low singles, reflecting the strong athletic cycle we are in, with Station also in the low singles, outperforming Carnival.

Now moving on to gross profit. Our gross profit margin of 38.8% represents a 270 basis point expansion versus last year. Let me break this down. Merchandise margins improved 390 basis points, driven by three factors: disciplined pricing strategy across all banners, favorable mix shift as Shoe Station grows and strategic inventory investments that improved in-stock rates. This more than offset 120 basis points of deleverage in buying, distribution and occupancy costs.

SG&A expenses were \$93.6 million or 30.6% of sales compared to 27.1% last year. Approximately 200 basis points of this increase relates to our rebanner investments, with the remainder due to deleverage, partially offset by disciplined cost management.

Our effective tax rate in the quarter was 25.9% versus 26.3% last year. Net income was \$19.2 million or \$0.70 per diluted share compared to \$22.6 million or \$0.82 last year. Our Q2 2025 earnings with \$0.21 of rebanner investments and otherwise exceeded the prior year by \$0.09.

Turning to our balance sheet and cash flow. We ended the quarter with \$91.9 million in cash and marketable securities, up from \$84.5 million last year. Following our strong August performance, cash and securities exceeded \$148 million, up over 10% versus prior year, and we continue to operate debt-free.

Inventory at quarter end was \$449 million, up 5% versus last year. This strategic investment delivered the product availability that drove our margin expansion and positive comps during back-to-school. Year-to-date, capital expenditures totaled \$24.4 million, with approximately \$20 million funding our 44 rebanner conversions.

Let me provide more detail on our rebanner economics. The \$0.21 second quarter EPS impact includes store closure costs, 4 to 6 weeks of lost sales during conversion, additional depreciation, customer acquisition costs and grand opening expenses. Year-to-date, we've absorbed \$0.36 of EPS impact. We now expect approximately \$0.70 for the full year or about \$25 million in operating income impact. Given the margin increases and high single-digit comp lifts we are achieving, these investments are a compelling use of our resources.

Now turning to our updated fiscal 2025 outlook. Based on our second quarter outperformance and positive August momentum, we are raising several key metrics. Net sales guidance is now \$1.12 billion to \$1.15 billion, tightened from our previous range. This implies significant sequential improvement in the back half, with comparable store sales improving from down high single digits in Q2 to down low single digits in the back half of the year.

This improvement reflects a growing Shoe Station mix and strong event period performance, including August positive comparable sales. We're raising the EPS guidance range from \$1.70 to \$2.10, increasing the low end by \$0.10. This reflects our Q2 beat and confidence in sustained margin expansion. The wide EPS range reflects macro uncertainty and expected traffic volatility outside key selling periods.

Gross profit margin guidance increases 150 basis points to 36.5% to 37.5%, reflecting the structural margin improvement from rebanners and disciplined pricing. SG&A is expected to be \$355 million to \$360 million, including the increased rebanner investment. Capital expenditures are expected to be \$45 million to \$55 million, with \$30 million to \$35 million for rebanners. For the third quarter specifically, we expect net sales of \$290 million to \$300 million and EPS of \$0.50 to \$0.55.

In closing, we are successfully evolving our business mix toward higher-margin categories and customers. Our rebanner investments are generating strong returns, and our balance sheet provides the flexibility to execute our rebanner strategy while remaining opportunistic on acquisitions.

I'll now turn it back over to Mark for closing remarks.

Mark J. Worden

President, CEO & Director

Before opening for Q&A, let me briefly summarize where we are. We delivered \$0.70 EPS in Q2, beating expectations by over 20%, with gross margins at 38.8%, our highest Q2 margin in years. That 270 basis point expansion came from strategic choices that are working. We increased our annual EPS guidance range today, reflecting the Q2 beat and fiscal August results.

Fiscal August delivered something significant. We achieved positive comparable sales growth during back-to-school, our highest stakes period. Shoe Station grew sales high single digits, carnival delivered positive children comps, Rogan grew sales and margins while being rebannered. Every banner contributed when it mattered most.

Our rebanner strategy is working. Station outperformed Carnival merchandise sales by over 10% in Q2 and fiscal August. Product margin resulting from our rebanner strategy expanded nearly 300 basis points. We'll operate 145 Shoe Station stores by year-end, on track for majority Shoe Station by next back-to-school.

We set out to build a company that serves median-income families with better brands and better experiences. The company is no longer a concept. It's operating, it's growing, and it's delivering. With that, Patrick, Tanya, and I would be happy to take your questions. Operator, please open the line for Q&A.

Question and Answer

Operator

[Operator Instructions] Your first question comes from the line of Mitch Kummetz with Seaport Research Partners.

Mitchel John Kummetz
Seaport Research Partners

Going to be a handful. First of all, Mark, I'm curious on the second quarter. Your sales came a little below plan, but obviously, your gross margins were well ahead of plan. You talked about prioritizing margin dollars.

I'm just curious, is there something about the quarter that was a bit unexpected? Or did you kind of change your priorities in the quarter in order to kind of achieve the results that you did that were a bit different than what you kind of laid out 3 months ago?

Mark J. Worden
President, CEO & Director

Mitch, thanks for the question. I think the opportunistic buys and additional inventory that the team brought in performed better than we expected. We captured success at a lower cost basis and strength at a higher-margin run first.

Second, the Shoe Station performance continues to accelerate. And as that grows towards a higher percent of our mix, that's helping us drive our margins higher than we expected.

And third, we continue to see competitors do irrational things related to pricing, and we believe that's not the strategy for us. We've stayed true while others were doing very aggressive profit dilutive activities before back-to-school. We stayed true and steady to our focus of where we're going to be, ready to deliver growth when the customer is ready to shop profitably during back-to-school.

And it delivered, with comparable growth coming in Q3 right away as soon as back-to-school started. It was an exciting period of time.

Mitchel John Kummetz
Seaport Research Partners

And then, Patrick, on the third quarter, you gave us guidance in terms of sales and earnings. Is there anything more you can say in terms of kind of what your comp expectations are for the quarter and then also margins gross versus SG&A?

Patrick C. Edwards
Senior VP, CFO, Secretary & Treasurer

Mitch, thanks for the question. Yes, there's a little bit more detail that we can provide on our third quarter results.

First, our -- on our sales, the \$290 million to \$300 million range that we've given is down 2 to down 5. So midpoint somewhere in the 3% range, similar to our annual guide in the back half of the year. We don't have any meaningful difference in stores, so our comp would be very similar to our total sales on that front.

With respect to margin, we earned 36% in the quarter last year. We would expect a number that is 100 to 150 basis points above that in Q3 this year. So targeting a number of like 37% to 37.5% would be the thought process. SG&A, I think the best way to think about that is a pure number that is \$95 million. So consistent with what we spent in Q2, which was about \$94 million.

Mitchel John Kummetz

Seaport Research Partners

That's very helpful. And then just as a follow-up to that. I mean, it sounds like August is off to a very good -- or 3Q is off to a very good start, given August. Can you just maybe talk through kind of your expectations for the balance of the quarter in order to get to sales down 2 to 5?

Patrick C. Edwards

Senior VP, CFO, Secretary & Treasurer

Sure. That would -- that's a pretty easy take to make for us. The low end of our range at \$290 million would assume comparable sales and total sales declines in the high singles, consistent with what we've seen in the first half of the year. And then at the low side of it, we see a number that is more flat. But the midpoint is this 3% sort of decline, which is a meaningful improvement from where we've been in the first half of the year.

Mitchel John Kummetz

Seaport Research Partners

And then, Mark, you made a comment in your prepared remarks that you're managing Shoe Carnival as a cash generator. Can you just elaborate on that?

Mark J. Worden

President, CEO & Director

Yes. I think that comes back to our margin integrity and not chasing traffic gains at any cost for that sub-\$30,000 household. We're seeing the competitive set go after that low-income strap household with very aggressive pricing activity that's eroding margins and delivering different outcomes than we just put up, let's say, our 270 basis point growth in Q2. That was discipline.

We think that's the right thing as we're strategically moving away from that sub-\$30,000 households. Instead of propping that up, chasing unprofitable low-quality sales now, we decided, and we'll continue to decide with Shoe Carnival, not to prop up that segment.

So we will expect to see in our guidance, that lower-income customer choosing to shop elsewhere and that median-income household shopper, \$50,000 and up, choosing to shop at us. It's profitable, it's where we're heading, and it's a strategic path.

With that, Shoe Carnival throws off very strong cash characteristics and as we shared, cash up sharply as we sit here today, positioning us to fund fully our growth initiatives, to fund fully this transition to Shoe Station, the median customer and to be ready for further strategic initiatives as they arise.

Mitchel John Kummetz

Seaport Research Partners

And then maybe last for me. You mentioned that once Shoe Station gets to -- like 51% of your store base kind of the model lifts, that would happen kind of midway through next year. Does that mean that the impact of the rebanner is kind of net neutral to next year's earnings because whatever drag that you see in the first half gets offset by a tailwind in the back half? How should we think about that? I know you're not giving next year guidance yet, but if you could just kind of walk us through that intuitively.

Mark J. Worden

President, CEO & Director

I can give you broad strokes. As you said, we're not ready to provide the full financial thought on it. But you've got it right. We believe when we hit 51% of our fleet is operating a Shoe Station, next back-to-school, we start seeing sustained comp positive versus a sporadic, which we're delivering now in key event periods.

So we think about it in our early planning that the back half of next year is where we start showing a comp positive for the total corporation, for the Q3, Q4 period. Shoe Carnival will still represent a significant percent, and we still expect that will be a headwind from that lower-income customer.

So we're not anticipating high or mid-single digit comp in the back half of the year. But rather, it turns an inflection point to low singles, just barely comp. But that's something to build on as we continue to transition.

Financially, we're not really ready to share broader thoughts on that beyond that comp directional concept. And the rebannered fact of a significant amount in the guide would be rebannered in Q1 and Q2. And those financial implications, we'll provide more guidance as we get further along this year.

Operator

Your next question comes from the line of Sam Poser with Williams Trading.

Samuel Marc Poser

Williams Trading, LLC, Research Division

A couple of mine. I'd like to talk to you about the inventory levels and the gross margin guidance and get some color on maybe where inventories are at the end of August. And just looking at the 3Q guidance and the gross margin guidance there, it looks like you'll sell \$60 million, \$70 million of cost of goods in August, give or take, you have \$449 million of inventory on hand.

How do you keep the gross margin guidance as high as it is with all this inventory? Doesn't the rubber have to hit the road sometime?

Tanya E. Gordon

Executive VP & Chief Merchandising Officer

It's Tanya. Just expand on your question in terms of inventory at the end of August, to answer your question, it's really in line with where we ended Q2, up mid-singles. And we strategically went after inventory to build for back-to-school, which helped us deliver that comp growth in the month of August.

We also worked through and bought opportunistic buys, which we're carrying in that inventory. So that number that you see in terms of inventory is opportunistic buys that will carry until we get to spring 2026. So that's just carrying through and then the balance where we built -- so we built in sandals and opportunistic buys for 2026.

And then the other place that we're carrying additional inventory is in the athletic business, specifically in kids athletic because we built that for back-to-school, which again helped us deliver that comp growth in the month of August. And those are all in key items, high-margining styles that will carry all the way through the season.

So we recognize we have more inventory than we would like to, but we strategically did that for better margin opportunities and growth as we work through third quarter into the balance of the year.

And then on the margin side of the equation, Mark spoke to that. But again, we continue to see better margins based on the opportunistic buys that we've done, our disciplined pricing, which we will strategically be disciplined through the balance of the year; and the key item position that we have this year and the better key item position that we're in this year than we've ever been.

Samuel Marc Poser

Williams Trading, LLC, Research Division

Just a follow-up. So we know a hard number. The inventory was \$449 million. That's a hard number that can tell us what's happening. Is that -- what is the number -- I mean, I don't know, since we don't know what the mid-single-digit increase year-over-year means, is -- what -- I mean, what is the number? Is it higher or lower than \$449 million? Is it -- since you had that strong August, is that now at 420? Because it's really what the number is, not what the increase is. It's looking forward, not looking backwards.

Mark J. Worden

President, CEO & Director

Sam, it's Mark. We're not going to give interim inventory right this second, books aren't closed for all of that. We're sharing -- sales are closed for fiscal August, and we're really delighted to be able to give the full back-to-school growth and margins closed. We're really delighted to be able to share that and the category information.

Here's the message on inventory. We have too much, as I said in my speech. And as Tanya said, we have it in places we feel good about delivering strong margins as we work through the fall season, the spring season and the key items.

Next year, once we have complete clarity or better clarity on the supply chain and tariffs, we will be working through and normalizing inventory levels. But we do not see that margin erosion becoming relevant in this fiscal year, and we do not see that product being margin deteriorating next year. It's a good product.

Samuel Marc Poser

Williams Trading, LLC, Research Division

Okay. And then just a little question. Are you guys going to see Jordan product for Spring '26? And with the Shoe Carnival business comping down high singles, could we assume that their brands such as Birkenstock and Skechers and others that were probably significantly better or possibly up, and it was a lot of the real low-end, moderate nonbranded products that really drove the comp down because the -- even the lower-income customers want those sort of high-in-demand brand?

Mark J. Worden

President, CEO & Director

Yes, I'm going to grab that, Sam. We're not going to share with our competitors what new products are coming in. I have great confidence. We have outstanding exciting brands that will be on our sales floor in early 2026, but I'm not going to share what those are with our competitive set to think about that.

On the second part of that question, our higher ticket items, best brands in the world, whether that's a footbed or an athletic in performance, performing outstanding. We've seen those drive the results, we're seeing those lead to capturing the higher-income customer, to delivering sales growth, to delivering margin growth.

Without a doubt it's tight focus on the best brands in select segments and not private label. It's been a winning recipe for us being a retailer and not a manufacturer, and we're seeing that play out incredibly well at this point of time. While others navigate their covenants and manufacturing, we just stay focused on buying the world's best brands and delivering margin growth.

Samuel Marc Poser

Williams Trading, LLC, Research Division

And then lastly, how are you seeing -- like how are the brands in general taking price? What are you seeing from price increases going into the balance of this year and going into next year due to the tariff impact from your wholesale partners?

Tanya E. Gordon

Executive VP & Chief Merchandising Officer

Sam, just recently, it had been a little quiet because we're on a pause, a 90-day pause with China right now. So China at 30%. But when they came back with the Vietnam with the additional 10, so it was 10 on top of 10, we're starting to get some more increases there. So as we move into spring, we're looking at price increases between 5% and 7% in total based on what we've gotten back thus far.

Operator

[Operator Instructions] There are no further questions at this time. I would now like to turn it back over to Mark Worden for closing remarks.

Mark J. Worden

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President, CEO & Director

Thank you all for joining us for our second quarter call. We're excited about the progress we're seeing with our growth strategy and look forward to discussing it in greater depth with you at our Q3 call later this year.

Operator

That concludes today's conference call. You may disconnect.

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