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Shoe Carnival, Inc.

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Earnings Call

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Call Participants

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Presentation

Operator

Good morning, and welcome to Shoe Carnival's Fourth Quarter 2025 Earnings 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. Today's call will reference forward-looking non-GAAP measures, including expenses related to CEO transition costs. These forward-looking metrics have not been reconciled to GAAP as all forward-looking expenses associated with the CEO transition are not known at this time.

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

Clifton E. Sifford

Interim President & CEO and Vice Chairman

Good morning, everyone, and thank you for joining us today. With me are Kerry Jackson, our Chief Financial Officer; and Tanya Gordon, our Chief Merchandising Officer.

I want to address directly the leadership change since our last earnings call. Mark Worden departed from his role as President and CEO on February 24. On behalf of the Board and the entire organization, I want to acknowledge Mark's contribution to this company throughout his tenure and wish him well. The Board appointed me Interim President and CEO and a search for a permanent successor is underway.

Some of you know my history here well. I served as President and CEO from 2012 to 2021 and have remained on the Board as Vice Chairman since then. I know this business, I know our people, and I know what it takes to execute in family footwear retail. My focus is straightforward: lead with clarity, execute with discipline and ground every strategic decision we communicate today and what our operational data supports.

Let me turn to the results and a path forward.

Fiscal 2025 demonstrated this organization's fundamental operational discipline. Full year EPS of \$1.90 exceeded consensus. Gross profit margin exceeded 35% for the fifth consecutive year. We ended the year debt-free for the 21st consecutive year with over \$130 million in cash and securities. These outcomes reflect the work of 5,000 employees executing through a challenging consumer environment.

The fourth quarter came in above consensus at \$0.33 per diluted share. Holiday was intensely competitive, and we chose not to chase unprofitable sales volume. That discipline preserved margins and protected the balance sheet as we moved into fiscal 2026.

Shoe Station's full year results continue to validate the model. Shoe Station net sales grew 2.7% for the year, outperforming the family footwear industry for the third consecutive year, while Shoe Carnival sales declined. The Shoe Carnival banner still represents roughly 65% of total volume. The performance gap between our two banners is real, but we will be working diligently to improve Shoe Carnival's performance and lessen the gap between the two banners.

I also want to note Shoe Station's e-commerce performance, which has been particularly strong. Online sales are demonstrating broad consumer resonance with Shoe Station brand and assortments well beyond the physical store footprint of the converted locations. That is an important signal as we think about the opportunity ahead.

I want to be direct about where the rebanner program stands and while we are adjusting the pace.

Fiscal 2025 was the first large-scale deployment of this program. We completed 101 rebanners, a significant step beyond the initial 10-store test conducted in fiscal 2024. When we evaluated the performance of those 101 stores, particularly the second half results, we observed meaningful variability in in-store sales performance across the converted locations. Some stores are performing very well. Others have not yet achieved the results we expect from the model. As the number of stores increased, the e-commerce channel, as I noted, performed strongly across the board.

That variability tells us we have more work to do before continuing conversions at the pace we had planned.

Specifically, we are focused on better understanding which consumer demographics respond most favorably to the Shoe Station format in store, which marketing approaches are most effective at driving sustained traffic to newly converted locations and how we can further refine product assortments in rebanner stores to improve in-store conversion and productivity.

We are not stepping back from our rebanner strategy. We are being disciplined about its pace and targeting. We plan to rebanner approximately 21 stores before Back-to-School 2026, while that evaluation is completed.

The Board's conviction in Shoe Station as a company's long-term growth vehicle is unchanged. The proposed corporate name change to Shoe Station Group, Inc. remains on the agenda for shareholder consideration at our annual meeting on June 10, 2026. At the same time, we recognize that Shoe Carnival banner continues to serve an important customer base in a meaningful number of locations, and we will continue to manage both banners with discipline and intent.

We expect to provide updates on the longer-term rebanner trajectory as this work progresses and as we gain greater clarity on where the model delivers the strongest and most consistent returns.

Kerry will walk you through the detailed financial guidance. Let me set the context.

Fiscal 2026 has three operational priorities: reducing inventory, completing targeted rebanners and controlling costs. On the inventory, we entered fiscal 2026 with close to \$440 million in merchandise inventory, up 14% from the prior year end. This increase is primarily opportunistic pre-tariff buys that supported our strong margins in fiscal 2025. In fiscal 2026, we will work that inventory down through disciplined selling and targeted promotional activity. That process will create near-term gross margin pressure, but it is necessary and it is the right thing to do.

On rebanners, we plan to convert 21 stores before Back-to-School 2026, focusing on locations where we have high confidence in the underlying consumer and store level economics. We are using our customer analytics to more precisely tailor assortments by location, aligning product with both the customer who has historically shopped the store and the customer we intend to attract with more premium brand mix. This targeted approach reinforces Shoe Station as our primary store growth banner while supporting comparable store sales improvement across both Shoe Station and Shoe Carnival as we move through the second half of the year.

On costs, our SG&A expenses are expected to decrease approximately \$12 million to \$14 million compared to fiscal 2025, reflecting reduced banner activity and continued operational cost discipline throughout the organization.

On the product side, I want to highlight a significant brand launch heading into the first quarter. We launched the Jordan brand from Nike, and it is currently available in over 60% of our stores with a full fleet roll out expected by mid-April. Jordan resonates across both banners, but we believe it will be particularly effective in our legacy Shoe Carnival stores, which serve a more urban consumer whose lifestyle and brand preferences align closely with Jordan's identity. We believe Jordan has the potential to reach approximately 5% of our enterprise-level athletic sales. We do not expect all of that volume to be incremental as some displacement of existing athletic assortment is anticipated. But the brand addition is a meaningful positive and important signal of the strength of our vendor relationships.

The financial results is EPS guidance of \$1.40 to \$1.60 compared to \$1.90 in fiscal 2025. That step down is real, is explainable and is almost entirely a gross margin story, driven by the timing of our price and cost changes related to tariffs. Kerry will explain that dynamic in more detail.

I also want to note that our fiscal 2026 guidance excludes CEO transition costs, which will be disclosed separately and reported as incurred.

Earlier this month, the Board approved an increase in our quarterly cash dividend to \$0.17 per share. This marks the 12th consecutive year we have increased the dividend, representing a compounded annual growth rate of approximately 15.5% over that period. The dividend is payable April 20, 2026, to shareholders of record as of April 6, 2026. The company has now paid a dividend for 56 consecutive quarters. That record reflects a consistent commitment to returning capital to shareholders from a position of financial strength.

In closing, I want to stress that the fundamentals of this business are sound. We have a debt-free balance sheet, substantial cash reserves, a proven store format with the Shoe Carnival banner and a proven growth vehicle with the Shoe Station banner that is winning where it has been appropriately deployed. The near-term earnings pressure is real. It is understood, and we have a clear plan to manage through it.

The decisions we are making in fiscal 2026 on inventory reduction, on the pace and focus of rebanners, and on cost discipline are deliberate and they are grounded in what our data tells us about our long-term returns. These actions are designed to position this company for meaningful improvement in fiscal 2027 and beyond.

Kerry?

W. Kerry Jackson
Executive VP & CFO

Thank you, Cliff. Good morning, everyone. I will cover the fourth quarter and full year financial results, balance sheet and cash flow, rebanner strategy financial impacts, and our fiscal 2026 guidance. The guidance reflects meaningful context to interpret accurately and will provide that context in some detail.

Net sales in the fourth quarter were \$254.1 million, a decline of 3.4% versus \$262.9 million in the fourth quarter of fiscal 2024. Comparable store sales declined 3.5%.

By banner, Shoe Station net sales were approximately flat with a low single-digit comparable store sales decline. Shoe Carnival net sales declined 4.5% with a mid-single-digit comparable store sales decline. Rogan's now fully integrated into the Shoe Station's operating structure, generated \$15.5 million in net sales with product margin expansion exceeding 500 basis points as we completed the transition to the Shoe Station assortment in those stores.

Gross profit margin was 34.9% in the fourth quarter, approximately flat compared to 34.9% in the fourth quarter of fiscal 2024. Merchandise margin expanded 30 basis points, reflecting continued pricing discipline. This improvement was offset by 30 basis points of deleverage in buying, distribution and occupancy costs on lower overall sales volume. The holiday selling environment was highly competitive, and we made deliberate pricing adjustments to maintain competitiveness through December without sacrificing the quarter.

SG&A was \$77.8 million or 30.6% of net sales compared to \$77.6 million and 29.6% in the prior year period. The year-over-year increase as a percentage of sales reflects deleverage of the lower revenue and approximately \$2.7 million of rebanner-related investment, partially offset by lower variable selling costs.

Net income was \$9.1 million or \$0.33 per diluted share, exceeding consensus expectations. For context, this compares to \$14.7 million or \$0.53 per diluted share in the prior year quarter. The prior year fourth quarter contained certain tax credits and other benefits associated with the Rogan's acquisition that totaled \$0.19 per share and did not recur in fiscal 2025. Our Q4 2025 earnings contained approximately \$0.08 per share of rebanner investment and otherwise increased \$0.07 per share before the impacts of these prior year Rogan's benefits and current year rebanner investment.

For the full fiscal year, net sales were \$1.135 billion, a decline of 5.6%. The full year comparable store sales decline was also 5.6%, with Shoe Carnival's mid-single-digit decline, partially offset by Shoe Station's low single-digit growth.

Shoe Station's net sales were \$236.7 million, representing 21% of total net sales. Shoe Station grew organically 2.7% versus fiscal 2024, outperforming the family footwear industry and exceeding Shoe Carnival's performance by 10.4 percentage points for the full year.

Full year gross profit margin was 36.6%, an increase of 100 basis points versus fiscal 2024's 35.6% and the fifth consecutive year gross margin has exceeded 35%. Merchandise margin for the full year expanded approximately 180 basis points compared to fiscal 2024.

I want to spend a moment on that merchandise margin expansion because it is an essential context for understanding our fiscal 2026 guidance.

In early Q2 of fiscal 2025, the company made a deliberate decision to raise retail prices in anticipation of tariff-driven cost increases. At the time of that price increase, tariff-affected product had not yet entered our cost stream. Our average unit costs were still based on pre-tariff inventory. The result was a period during which we were selling at higher prices before our cost increase, generating a temporary but meaningful benefit to merchandise margin. This dynamic contributed significantly to the 180 basis point merchandise margin expansion and the full year 100 basis point gross margin improvement.

This decision was appropriate given the information available and the tariff environment at the time. It materially supported fiscal 2025 results. However, it creates a challenging comparison of fiscal 2026 when tariff costs arrive in our cost of sales while our ability to raise prices further is constrained by competitive dynamics. This timing mismatch is the primary driver of gross margin compression in our fiscal 2026 guidance.

Full year SG&A was \$348.4 million or 30.7% of net sales versus \$337.6 million and 28.0% in fiscal 2024. The 2.7 percentage point increase as a share of sales reflects approximately 2.0 points of rebanner investment and the balance from deleveraging on lower revenue.

Full year operating income was \$66.8 million or 5.9% of net sales. Net income was \$52.3 million or \$1.90 per diluted share compared to \$1.87 consensus estimate, a modest but meaningful beat.

The full year rebanner P&L investment reduced operating income by approximately \$24.1 million or \$0.66 per diluted share.

Our balance sheet remains a genuine competitive advantage. We ended fiscal 2025 with \$130.7 million in cash, cash equivalents and marketable securities, an increase of approximately 6% from the end of fiscal 2024. We had no debt outstanding, the 21st consecutive year we have ended the fiscal year debt-free, \$100 million of available revolving credit and \$50 million remaining under our share repurchase authorization.

Operating cash flow for fiscal 2025 was \$71.3 million. Capital expenditures were \$44.7 million, primarily rebanner related.

Merchandise inventories ended fiscal 2025 at \$439.6 million, up 14% compared to \$385.6 million at the end of fiscal 2024. As Cliff noted, this elevation was intentional. We made opportunistic pre-tariff buys of seasonal merchandise and in-demand product in advance of expected cost increases. Those purchases directly supported merchandise margin expansion in fiscal 2025 and are expected to partially offset higher tariff affected costs as that inventory is sold in fiscal 2026.

Working the inventory position down in fiscal 2026 is an operational priority. That process will involve targeted promotional activity on merchandise that is not of the ongoing assortment and other excess merchandise, which will create a near-term pressure on merchandise margins. That pressure is accounted for in our guidance.

As Cliff described, we will complete approximately 21 store rebanners in the first half of fiscal 2026 compared to the 71 stores previously communicated. The financial implications are incorporated in our guidance.

Total rebanner P&L investment for fiscal 2026 is expected to be in the range of \$10 million to \$15 million compared to the \$25 million to \$30 million previously communicated. The reduction reflects the lower number of rebanner conversions planned, partially offset by the continuation of customer acquisition and marketing costs for stores converted in fiscal 2025 that are still ramping up.

Rebanner capital expenditures for fiscal 2026 are expected to be in the range of \$5 million to \$7 million compared to the \$25 million to \$35 million previously guided, consistent with the revised rebanner plan.

Regarding inventory reduction, notwithstanding the reduced number of store conversions in fiscal 2026, the company remains committed to reducing merchandise inventory by \$50 million to \$65 million during the fiscal year. We will achieve that reduction primarily through the sale of opportunistic pre-tariff and in-demand products purchased in fiscal 2025 and increased promotional activity as we work through excess inventory with the majority of that promotional selling concentrated in the first half of fiscal 2026. As inventory normalizes, promotional intensity is expected to moderate in the second half of the year, which supports the improvement in gross margin trends we expect from the first half to the second half.

The inventory reduction is expected to significantly increase our operating cash flow in fiscal 2026 compared to fiscal 2025. Coupled with the now expected lower capital expenditures, this provides increased flexibility to fund growth investments from cash reserves.

I want to frame the fiscal 2026 guidance carefully because the year-over-year comparison requires more context than typical guidance discussion.

Our fiscal 2026 guidance excludes CEO transition costs, which will be reported separately as incurred.

Net sales are expected to be down 1% to up 1% versus fiscal 2025. Comparable store sales are expected to decline in the first half as the fleet composition remains similar to the latter part of fiscal 2025. As 21 stores complete conversion before Back-to-School and Shoe Station's e-commerce and store momentum continues, we expect comparable store trends to improve in the second half. The full year comparable store sales results is expected to show improvement versus the 5.6% decline in fiscal 2025.

Gross profit margin is expected to be approximately 34%, a decline of approximately 260 basis points compared to fiscal 2025. Let me walk through the three components of that compression directly.

First, tariff-driven cost increases. As pre-tariff inventory is sold and replaced with higher cost tariff-affected goods, average unit cost increase. This is the cost side of the equation.

Second, the nonrecurrence of the fiscal 2025 price increase benefit. As I described in the full year results section, we raised prices in early Q2 fiscal 2025 before the cost increased. That benefit, higher prices, lower costs does not repeat in fiscal 2026. In fact, our retail pricing may be moderated, not increased, given the competitive environment our customers are shopping in.

Third, promotional inventory reduction activity. Working through the excess merchandise requires promotional selling, which compresses merchandise margin in the near term.

I want to offer an important frame for these factors in aggregate. Our fiscal 2026 gross profit guidance reflects a decline of approximately 260 basis points from fiscal 2025. The compression we are reporting versus fiscal 2025 is primarily the unwinding of a timing benefit that was always temporary, plus modest net headwinds from tariffs and promotional activity. In fiscal 2027, we expect to return to a more historically typical gross margin of better than 35%.

On expenses, SG&A costs are expected to decrease approximately \$12 million to \$14 million versus fiscal 2025. The decline is primarily due to lower banner costs from the reduced conversion plan and ongoing operational discipline across the organization.

Pulling it together, net sales down 1% to up 1%, gross margin of approximately 34% and expenses down \$12 million to \$14 million produces expected operating income in the range of approximately \$47 million to \$55 million. After interest income and taxes at an expected rate of approximately 26%, we expect EPS in the range of \$1.40 to \$1.60, excluding CEO transition costs compared to \$1.90 in fiscal 2025.

From a quarterly cadence perspective, the first half will carry more of the gross margin pressure as we sell through elevated inventory and execute rebanner conversions. The second half benefits from improved comparable store sales trends as newly converted Shoe Stations locations ramp, the stabilization of inventory levels and moderation of promotional activity. We will provide more specific quarterly perspective when we report Q1 fiscal 2026 results in late May.

The fiscal 2026 guidance reflects an honest and fully supported assessment of the gross margin environment, the work required to normalize inventory and the more measured pace of the rebanner program. The expense reductions are real and operational. The balance sheet is strong and expected to grow stronger with normalizing inventory. Shoe Station continues to grow in both its stores and e-commerce channels.

The EPS step down from \$1.90 to the \$1.40 to \$1.60 range is significant, but it has clear and explicable cause. The multi-year gross margin context I provided demonstrates that Fiscal 2026 represents a return toward historical norms, not a structural deterioration of this business.

I will now open the call for questions.

Question and Answer

Operator

Your first question comes from Mitch Kummetz with Seaport Research.

Mitchel John Kummetz
Seaport Research Partners

Cliff, welcome back. I've got a few. Let me start with -- you guys talked about some variability of the Shoe Station in-store performance. Could you just explain what's going on there? Is that a function of the demographics, household income, assortment, lack of awareness of the concept in certain markets? Can you just help us understand why you're seeing that variability across stores?

Clifton E. Sifford
Interim President & CEO and Vice Chairman

Mitch, it's good to be back. Good to hear from you. The best way for me to answer that is a little bit of everything you mentioned. We rebannered stores in Shoe Carnival locations and where Shoe Carnival customers shop, where Shoe Carnival co-tenancy is. And we may have raised the assortment level a little too high for that consumer. So we need to go back and it's part of what we're doing now.

We're just digging into each one of those stores to understand the customer that's there to understand the demographics within the range of the store so that we can make the corrections from a product standpoint and get the comps to perform once again. The first few stores that we opened up were in great locations that serve a customer with a higher income level, higher demographics.

And then we started converting Shoe Carnival stores. And I believe that we converted them too quickly before we did the -- too quickly before we did the research on the individual stores. So I think it's a fixable problem.

It's something that we're working very hard on. I believe that my goal is that by back-to-school, we have the assortments adjusted in those stores so that we can enjoy a better second half.

Mitchel John Kummetz
Seaport Research Partners

And then just as a follow-up on the rebannered. I think you said you're at 144 Shoe Station stores now. Is it reasonable to think that maybe some of those need to be converted back to Shoe Carnival stores? And when you think about the business longer term, under the prior CEO, there was talk about Shoe Station eventually being essentially the entire fleet. Kind of where you guys sit today, are you rethinking that? And is the go-forward strategy maybe that there's reason to have two banners instead of just Shoe Station down the road?

Clifton E. Sifford
Interim President & CEO and Vice Chairman

So let me take your first question first. No, we're not absolutely not going to rebanner a Shoe Station store back to a Shoe Carnival store. We are going to adjust the product mix in those stores, especially where the demographics demand that so that we can get the customer that was shopping in those stores to shop in the Shoe Station stores. As far as the second question, we absolutely will -- I hate to put an absolute to it, but our goal at this point is to operate two banners.

We think that the diversity of our customers, especially as we enter into the Midwest and North-midwest and South, we should operate those stores as Shoe Carnival stores. And Shoe Station will then be operated in the appropriate areas where the demographics call for the kind of product mix that we want Shoe Station to carry.

Mitchel John Kummetz

Seaport Research Partners

And is it too early at this point to say kind of what that might look like long term operating two banners? I mean, is there an opportunity to have two national chains under the company? Or how do you think about that?

Clifton E. Sifford

Interim President & CEO and Vice Chairman

We're still in the process of studying that. We -- I'm not prepared today to give you that answer. But I hope by the next call that we can flesh that out a little further for you so that you understand what the growth aspirations are for each one of those banners. I do think the growth opportunity for Shoe Station is still strong. I just think we need to look at market areas that have, as I said before, higher income demographics and the consumer that's looking for the brands that we carry in the premium brands that we carry in Shoe Station.

Mitchel John Kummetz

Seaport Research Partners

Okay. And then last one for me. Kerry, as far as the guidance goes, and I do appreciate the additional color. It sounds like -- and it sounds like you're actually going to give more color on the next call. But from what you said, I think both from a sales and then especially from a margin -- gross margin standpoint, it looks like more pressure in the first half than the back half. Is there anything more explicitly you can say about the first quarter in terms of comp, in terms of margins and earnings?

W. Kerry Jackson

Executive VP & CFO

We're not going to give any details on the per quarter. But I'll give you some -- but you're right about the margin 2026 and the guidance is really a margin story. And it gets back to in Q2 of last year, we made a conscious decision to raise our pricing prior to the tariff costs entering our inventory. And what we saw was an elevated merchandise margin beginning in Q2.

In fact, the merch margin in Q2 was almost up 400 basis points, whereas in Q1 of '25, it was up about 50 basis points. So the compare is very difficult and the hardest compare is Q2, and that's where we're seeing the most pressure we're going to see is in the first quarter. So we're helping understand that those temporary increases, we knew going into it that the cost was going to catch up to us on the tariff side of it, but it'd be mainly in 2026.

And that 180 basis point merchandise margin increase that we had in '25, we're saying we're going to give that back. And then -- you add that some additional pressure due to reducing inventories, et cetera, and that accounts for the full 260 basis points of margin pressure we've built into our guidance.

Operator

Your next question comes from Sam Poser with Williams Trading.

Samuel Marc Poser

Williams Trading, LLC, Research Division

I guess welcome back, Cliff, and welcome back Kerry, and it's good to have...

I heard Carl coming back next week. Is that...

Clifton E. Sifford

Interim President & CEO and Vice Chairman

Carl only comes back to have lunch.

Samuel Marc Poser

Williams Trading, LLC, Research Division

I guess, well, I hope he has a good lunch.

Anyway, the... Question -- I want to follow up on -- I want to get some idea. You're down 260 -- you're saying down 260 for the year. Could you give us some help as to -- is the first half of the year going to be down 350 and then the second half, the balance in the second half. Can you just direct us on the gross margin so we can at least be in some kind of ballpark?

W. Kerry Jackson

Executive VP & CFO

Well, I would tell you to look at, particularly in the first half, the increase that we had in our merch margin, and I just gave you the numbers on that. We're expecting that to fully reverse in our '26 because that was gained artificially. And then the additional pressure of the markdowns and the tariff costs coming into our inventory, which obviously we're seeing today, that's going to put -- that's the pressure we're talking about.

Samuel Marc Poser

Williams Trading, LLC, Research Division

So I get that.

I mean, I guess -- so in Q2, you had 390 basis points of merchandise margin increase last year and then you delevered your BD&O. I assume you're expecting BD&O deleverage on top of that big increase. So I mean, we could be looking at Q2 in the down what 450, 500 point range for gross margin. Is that -- am I thinking about that right?

W. Kerry Jackson

Executive VP & CFO

Well, directionally, yes. And like I said, we're not giving quarterly. On an annual basis, BD&O is relatively flat from a leverage standpoint in our guidance. The tier effect on an annual basis is really coming out of the merch margin for the aforementioned issues that we talked about.

Samuel Marc Poser

Williams Trading, LLC, Research Division

And on the merch margin, I would think that the biggest pressures on the merch margin from a tariff perspective would be Q2 and Q3. And then Q1 has some pressure there, but more pressure on markdowns.

W. Kerry Jackson

Executive VP & CFO

Well, keep in mind, the biggest pressure in the year is the temporary increases we took in 2025. That's the biggest part of the whole thing. And that was -- the tariff costs were not dramatic in our inventory in 2025. That pressure we're going to see flow through into 2026. So the 180 basis point improvement that we saw in 2025 was really the pricing that we increased starting in Q2 that we just can't repeat in 2026.

In fact, we'll see pricing pressure likely because of the economic environment. We can't continue to increase prices, and we're going to probably have to reduce some of those prices to reflect the market.

Samuel Marc Poser

Williams Trading, LLC, Research Division

I mean I think that's exactly what I said. I mean, forget about the pricing, you took the prices last year and you benefited from that big in Q2 and Q3. Q1, you hadn't taken the prices yet and you hadn't taken

the prices yet in Q1. So you're getting the benefit from the price in Q1, but that's going to be offset by promotional activity. And then in Q2 and Q3, you have the flow-through of the tariffs and you're lapping those price increases that you took. So Q2 and Q3 from a tariff/price increase comparison should be the worst, but then you'll sell more full price goods in Q3, which is the offset. But in Q1, you would -- so I mean, Q1 and Q3 look like they'd probably be similar from a year-over-year basis for different reasons as far as the change.

W. Kerry Jackson

Executive VP & CFO

Well, Q1 in '26 won't be as hit -- won't have as much margin pressure because we still have the pre-tariff inventory that we're going to be -- that we've talked about all year. That's the purpose of carrying the higher level of inventory for most of the year is the benefit, and we'll see that benefit in Q1. So even though -- so the comparisons margins were only -- merch margins were only up 50 basis points in Q1 last year.

We're going to -- so we're -- and we'll have the benefit of selling pre-tariff goods inventory. So in Q2, we'll have less of a benefit of that -- we also have a very difficult compare where our merch margins were up almost 400 basis points. That's why we're saying Q2 is the most difficult margin compare for the year, and it will be the most decline on a year-over-year basis.

Samuel Marc Poser

Williams Trading, LLC, Research Division

All right. And then let's move on to Shoe Station. The -- you mentioned that -- could you -- you mentioned the comp was for the quarter -- for the year, it was up low singles. And for the quarter, it was down low singles. Can -- but you've said that your e-commerce -- like how do the stores do versus e-commerce? I mean, like it sounds like the stores are lagging e-commerce. So that 1,000 basis point difference for the year in the comp, how much of that was driven through by the e-commerce versus the stores versus compared to Shoe Carnival?

Clifton E. Sifford

Interim President & CEO and Vice Chairman

Sam, e-commerce business at Shoe Station was incredibly strong across markets, this is one of the reasons we're still convinced that Shoe Station is the banner that is going to continue to grow as the e-commerce business was phenomenal across market areas where we didn't even have Shoe Station stores. So really pleased with that. However, you are correct that the rebanner stores are not performing the way we expected them to perform.

In fact, the rebanner stores were down high single digits and the legacy stores down mid-singles. And that's the -- and that is the reason we've decided to put a hold on any additional stores until we can determine exactly what's going on in the brick-and-mortar stores and get that corrected. And that's our #1 priority. We're working hard to -- with all the data that we have. And as you know, we have a lot of data. And we're going to figure the problem out and get those stores turned around.

Samuel Marc Poser

Williams Trading, LLC, Research Division

And then lastly, in the -- this goes back to the margin and everything else.

You converted how much of the gross -- within the promotional activity, I mean, how much of how many of these converted stores of the 101 stores you converted last year, do you really believe were opened putting their best foot forward, so to speak, with the mix that you intended?

I'm not saying it was the right mix versus having too much carryover just to get the conversion done, but you had too much of the old Shoe Carnival assortment in the store. And now you have to clear that out to really find out what really could have been. I mean, because in what I -- I haven't been to a Shoe Station store, but from what I hear, there's -- it looked like, yes, you brought in HOKA and other -- some of the other good stuff, but it was lost in the sea of leftovers from the old Shoe Carnival stores.

And that may have hurt the comps.

Clifton E. Sifford

Interim President & CEO and Vice Chairman

Yes. I don't -- that did not happen, Sam. What we did, as I understand it and we've got a room full of people here.

And if I say something wrong, they correct me. But we cleaned the Shoe Carnival inventory out of the converted stores, sent them to the Shoe Carnival stores so that we could open up the rebannered stores with clean, what we consider to be clean Shoe station type merchandise. And so I don't know where you heard that from. I think -- I don't know who's visited the store and saw old inventory, but that is the way we converted the stores. And it worked in the first few stores, but it did not work as well as we anticipated as we continue to open up stores.

And I think the issue with that primarily is that we took Shoe Carnival locations with Shoe Carnival co-tenancy, and we opened up Shoe Station stores and maybe we elevated the product higher than the consumer was ready for. And that's what we're studying today to make sure that we're right on that, and we'll make those corrections. But that's why I think the Shoe Station stores are not performing to the plan that we had.

I just was handed a note if whoever you were speaking to was speaking of Rogan's, that we didn't make a lot of inventory adjustments in Rogan's because their customer base was completely different. It was a work shoe-based, blue-collar based retailer.

Operator

Your next question comes from Jim Chartier with Monness, Crespi & Hardt.

James Andrew Chartier

Monness, Crespi, Hardt & Co., Inc., Research Division

So as we just talked about your Shoe Station comps turned negative in fourth quarter. The expectation was that Shoe Station will be the dominant banner and those stores will be comping positive and that will lead to an overall comp in the second half of '26. So in light of the sales slowing at Shoe Station and turning negative in fourth quarter, what gives you the confidence that sales turn positive in the back half of this year?

Clifton E. Sifford

Interim President & CEO and Vice Chairman

Well, Jim, thank you for the question. What we're doing is we're going through each individual store and their assortment what's working, what's not working. One of the things we did at Shoe Carnival, and you followed us for a while, so you know we built assortments based on the consumer or a customer that was shopping each store. And so the assortment was slightly different based on the customer.

We did not, in my opinion, do that very well for Shoe Station. So the merchants are going in, we have all the demos. We have all the Shoe Perks data that we're looking at on who's buying the product. And we are making those adjustments. from an assortment standpoint in our stores. And we think that we can get those adjustments, as you know, it takes -- you can't decide today to make adjustments in product and get the product in tomorrow, it takes about 6 months.

So we believe that those adjustments will be in place by back-to-school, and that should, based on all the information we have through our Shoe Perks program and the demographics of each individual store, we should start seeing an improvement in the second half of the year.

James Andrew Chartier*Monness, Crespi, Hardt & Co., Inc., Research Division*

Okay. Was there a conversion problem then? Was traffic okay and then the consumer walked in the store and just didn't see what she wanted and then said that conversion was softer?

Clifton E. Sifford*Interim President & CEO and Vice Chairman*

The conversion rate was actually flat. And I think the reason for that is that in the beginning, when the customer came in, that was previously a Shoe Carnival customer and saw the elevated product, that customer just did not come back a second time. And I believe that's why as we work through those stores and they became more and more mature throughout the year, we saw a decline in purchases. Jim, one other thing I'd like to add to that. We also saw a decline in the average unit per transaction.

So that just tells us that they were coming in and they were only purchasing one pair. Some of that could have to do with the economy and some of that could have to do with the fact that maybe we were not promotional enough in those stores to get them to buy that second pair.

James Andrew Chartier*Monness, Crespi, Hardt & Co., Inc., Research Division*

Okay. And then Kerry, just trying to understand what next year, FY '27 should look like, right? So you're going to have a negative impact this year from selling pre-tariff inventory at post-tariff prices, but that should be normalized this year. And then you've got -- I guess, what is the impact from the discounting and promotions you're going to have to run to work down inventories levels this year?

And then in terms of like rebanner investments for next year in '27, is it going to be similar to '26 at this point, do you think? And then how should we think about the synergy benefits that you expected from operating primarily as a single banner? Is that no longer in the cards?

W. Kerry Jackson*Executive VP & CFO*

Jim, those are great questions, but that is part of the evaluation Cliff was talking about that we are doing right now and looking back and letting the data tell us exactly what needs to happen, unsure how many stores will we rebannered from the standpoint of in the Shoe Station because we really need to take a tighter look and understand what hasn't -- the stores that haven't met our expectations, what are the causes behind that and then extrapolate those causes into future Shoe Carnival stores and understand the opportunity we have.

We no longer believe that 90% of our stores will be rebannered to Shoe Station because as Cliff says, it looks like the demographics don't always support the Shoe Station banner. Now that's what will be over the next several quarters as we get through that data analysis, be able to give you better guidance on how that will work. What we were trying to say in '27 and talk about the margin that we think 2026 is a transition period to give back those artificial gains, the -- I should say the temporary gain we had in 2025 back in our margin and we will be -- have a little compression because of some clearance, tariff goods. But we think 2027 from a margin perspective, at this stage, we don't see any reason that we wouldn't be back to more historical gross profit margins in the 35%. So we're trying to give some comfort from the standpoint that '26 is a transition year, then we get back to normal.

Now on the Shoe Station, whether they're rebanners or new store growth, those are the type of things we're going to be talking about in the next several quarters.

James Andrew Chartier*Monness, Crespi, Hardt & Co., Inc., Research Division*

Okay. And then just there's been a lot of talk about tax refunds being bigger this year. Just curious if you're seeing anything in the business related to tax refunds.

Clifton E. Sifford

Interim President & CEO and Vice Chairman

Well, between the tax refunds, the war and the economy rising prices, it's difficult to say our business is trending the way it's trending because of tax refunds. There's just a lot going on with the economy today.

Operator

Your next question is a follow-up from Mitch Kummetz with Seaport Research.

Mitchel John Kummetz

Seaport Research Partners

Yes. I was just hoping to clarify something. In terms of your comp guide for 2026, Kerry, I think in your prepared remarks, you said that it should be better than the minus 5.6%. But could you be a little bit more specific in terms of kind of what comp you're looking for? And then also, I believe you've explicitly said that it would be negative in the first half, but then improvement in the second half. I think there's sort of an assumption that it turns positive in the second half. I don't know if that's actually accurate or not. So can you just help me out on those 2 items.

W. Kerry Jackson

Executive VP & CFO

We here again, we'll be more qualitative than quantitative on this. But -- so we're primarily comp right now. So we stated our total sales will be -- our guide is minus 1% to up 1%. Comp is directionally very similar to that. And yes, we expect to have a better second half from a sales perspective than the first half. And that's as explicit -- so that's a definite improvement over what we did in '25.

Operator

There are no further questions at this time. I'll now turn the call back over to Mr. Sifford for any closing remarks.

Clifton E. Sifford

Interim President & CEO and Vice Chairman

Thank you for joining us today. I am thrilled to be back and for the opportunity to work with this talented team. I look forward to speaking to you all again in May. Thank you again.

Operator

This concludes today's conference call. Thank you for participating. You may now disconnect.

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