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Signet Jewelers

Signet Jewelers FY27 Q2 Earnings

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Signet Jewelers; Chief Executive Officer & Director
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PRESENTATION:

Operator^ Hello, everyone. Thank you for joining us. And welcome to the Signet Jewelers Fiscal Year 2027 Quarter two Earnings. (Operator Instructions) I will now hand the conference over to Rob Ballew, Senior Vice President in Investor Relations and Capital Markets. Please go ahead.

Rob Ballew
Signet Jewelers; Senior Vice President, Investor Relations & Capital Markets

Good morning. Thank you for joining us for today's earnings conference call. During today's discussion, we will make certain forward-looking statements. Any statements that are not historical facts are subject to a number of risks and uncertainties. Actual results may differ materially. We urge you to read the risk factors, cautionary language and other disclosures in our annual report on Form 10-K, quarterly reports on Form 10-Q and current reports on Form 8-K.

Except as required by law, we undertake no obligation to revise or publicly update forward-looking statements in light of new information or future events. During the call we will discuss certain non-GAAP financial measures. For further discussion of the non-GAAP financial measures as well as the reconciliation of the non-GAAP financial measures to the most directly comparable GAAP measures, investors should review the news release we posted on our website at ir.signetjewelers.com. With that, I'll turn the call over to JK.

J.K. Symancyk
Signet Jewelers; Chief Executive Officer & Director

Thanks, Rob. And good morning, everyone. I'd like to start today by thanking our Signet team. Your commitment and execution of Grow Brand Love is inspiring. We're building something great, so thank you for being a part of it. There are three key takeaways I'd like to leave you with today.

First, we delivered another solid quarter with positive comps, now five of the last six quarters with positive comps each month of the quarter and drove more than 35% adjusted EPS growth.

Second, we are accelerating our key brand initiatives including merchandise refreshes, enhancements to both the online and in-store customer experience and a more modern, emotionally engaging marketing approach as we look to drive a positive comp over the holiday. Third, we have growing confidence in our ability to deliver this year, and we're raising guidance for the second time.

We had a solid quarter with comps up over 2%, reflecting high single-digit comp growth at price points over $2,000 including a strong Mother's Day. Timepieces continued to deliver strong category comp growth, up almost double digit to last year.

We delivered low single-digit comp growth in Bridal led by a stronger sales performance. Fashion saw a 1% comp decline, reflecting decreases in comps at Banter and lower price points in general, largely metal pieces with nice sales growth at middle to high price points. Beyond top line, we continue to navigate tariffs.

This quarter reflects diligent and ongoing work from our team led by Stacee Johnson-Williams, who continued to minimize the impact of ongoing tariffs and pursue any and all available refund of direct tariffs previously paid. They are also actively working with our valued vendor partners to pursue recovery of any applicable indirect IEEPA tariffs and continue to build on further supply chain opportunities.

The speed and agility of our team in their efforts here is a direct reflection of our improved operating model. Looking forward to the second half, we have several initiatives working to differentiate Signet's brands. This week, we're introducing an important evolution of Kay, one of the most recognized jewelry brands in the U.S.

We're building on Kay's strong foundation with Love All In, a new campaign that brings a fresh expression of love to the Kay experience from our imagery and language to how and where consumers engage with the brand. The goal of Love All In is to move Kay from an idealized expression of love to something much more real and authentic while also expanding the occasions and relationships we can celebrate with them.

As we mentioned on the last call we have redesigned the websites for Jared, Kay and Zales. We have launched both Kay and Jared and early results are promising. We expect Zales to launch later this month. I'd encourage you to visit the Jared and Kay sites now. You'll immediately notice better imagery and product presentation that includes more realistic on-model photography to help customers buy with confidence.

A simpler navigation structure helps customers get to the right product faster alongside curated experiences that work to connect inspiration directly to product. In short, it's a more modern, intuitive and inspiring shopping experience. This creates a foundation for digital growth by including deeper personalization, agentic discovery and greater omnichannel connectivity.

I'd like to take a moment to thank our digital and technology teams. You delivered ahead of schedule while serving customers without disruption, and you've positioned us well for an important Q4 ahead. Alongside those efforts, we continue to transform our marketing playbook while driving efficiency and spend.

For example, we reduced marketing spend this quarter while driving positive comps and increased social media impressions including unpaid impressions with the strongest increase in efficiency at our three largest brands.

We also saw those three brands, Kay, Zales and Jared increase their customer consideration in the second quarter. Proof points like these give us confidence that stronger storytelling drives better brand engagement. We believe the combination of our marketing playbook and refreshed websites can continue expanding reach and engagement to drive conversion through digital experiences that reinforce brand distinction rather than relying solely on paid traffic.

Importantly, ahead of holiday, we've invested in opportunities within our assortment and across price points. We know the consumer is always focused on value across income brackets, and we will leverage the full strength of our portfolio to drive differentiation and serve customers.

This means both narrowing and deepening of top performers as well as fortifying trends and fast following successes. We believe we are well positioned to deliver compelling value throughout the holiday season and have provided more flexibility within our strategic vendor base to react quickly to trends. Turning to my final takeaway today.

We have growing confidence in our ability to deliver this year as we raised guidance for the second time. We are driving consistent results with momentum and focus. We're taking deliberate actions to strengthen our brands, deepen customer engagement and create long-term shareholder value.

Before I hand things over to Joan, I'd like to formally welcome our new Zales and Blue Nile Presidents. Jamie Cygielman, our new President for Zales and Banter, was most recently with Mattel, serving as Global Head of Dolls which included leading the American Girl and Barbie lines. Jamie brings 30 years of experience building and transforming long-standing, well-known brands. Pam Cloud, our new Blue Nile President, joins us with more than 30 years of luxury retail experience including more than 25 years with Tiffany & Company.

A merchant at her core, Pam understands the power of signature and proprietary collections as key to driving brand affinity. With Jamie and Pam rounding out our brand leadership team, we believe we now have the right leaders aligned to the right strategy and the momentum to bring Grow Brand Love to life at scale. I'm excited for what this team will accomplish as we continue shaping the future of Signet. Summarizing my key takeaways today.

First, we delivered another solid quarter with positive comps, now five of the last six quarters, with positive comps each month of the quarter and drove more than 35% adjusted EPS growth.

Second, we are accelerating our key brand initiatives including merchandise refreshes, enhancements to both the online and in-store customer experience and a more modern, emotionally engaging marketing approach as we look to drive a positive comp over the holiday. Last, we have growing confidence in our ability to deliver this year, and we're raising guidance for the second time. With that, I'd like to turn it over to Joan.

Joan Hilson
Signet Jewelers; Chief Financial & Operating Officer

Thanks, JK. And good morning, everyone. We are pleased to announce that we have proactively signed an early renewal with our primary consumer credit partner, Bread Financial, after a competitive bidding process fueled by the strength of the portfolio. The renewal includes a new profit-sharing agreement that we estimate will generate over $1 billion to Signet in incremental non-comp revenue and operating income over its life.

This includes roughly $80 million of cash expected to be received in the third quarter in conjunction with the signing of our agreement which will be recognized ratably over the term. We estimate an operating benefit over the next 36 months between $200 million and $250 million.

And thereafter, the amount should increase through the term of the agreement. We expect between $30 million to $40 million of non-comp revenue and gross margin benefit this year, partially offset by higher incentive compensation. Importantly, there is no loss sharing within the agreement. This is incremental to our current profitability and is still expected to provide significant benefit to Signet even across recessionary scenarios.

In addition to the direct financial benefits, the agreement will also bring a number of customer enhancements over the next 12 to 18 months. These will focus on continued tech investments, robust analytics to enable data-driven marketing as well as an improved customer experience and credit capabilities to support customer needs including cross-shopping among Signet brands.

Additionally, we plan to offer credit from Bread Financial to Blue Nile customers for the first time ahead of this holiday season. With this announcement, I'd like to thank our financial services team which is led by Lisa Walker and also Vince Ciccolini for their work which brings tremendous value to shareholders and our customers. Turning to progress on Blue Nile.

We are doubling down on what makes Blue Nile differentiated within the Signet portfolio. Blue Nile has served as a diamond education resource since 1999, and we believe serves as one of the first touch points for consumers on their shopping journey. Building on this foundation, we'll be announcing a new luxury partnership in the coming weeks, reinforcing the rarity and enduring value of natural diamonds while continuing to provide customers with exceptional choice across diamonds and other gemstones.

Additionally, we will be transitioning more of the Blue Nile showrooms to full-service stores with an increased availability of on-hand assortment, particularly in the new collections. While not included in our comp sales, the brand delivered 10% sales growth this quarter.

Now turning to the quarter. Revenue was $1.5 billion with comp growth of 2.2%, reflective of AUR growth of 6% with growth across channels and among categories including Bridal, Timepieces and Services. Adjusted gross margin was roughly $600 million for the quarter, with rate up 70 basis points.

Merchandise margin increased 20 basis points, reflecting a core performance in line with expectations and an additional $13 million of refunds of tariffs previously paid above our expectation. This offset a significant increase in gold costs and a higher effective tariff rate.

SG&A expense decreased $12 million to last year, driving a 60 basis point rate improvement from operating model changes and continued spend discipline. Adjusted operating income increased 25% to $107 million, driving 140 basis points of rate expansion. Adjusted diluted EPS increased 36%, reflecting operating income growth, higher interest income and a lower diluted share count.

Now turning to the balance sheet. Inventory ended the quarter at $2 billion, down 1% to last year, even including the impact of gold costs. Cash ended the quarter at roughly $525 million, up nearly $250 million to this time last year. Free cash flow year-to-date improved by more than $10 million to last year, driven by inventory and vendor payable management, improving by one week, partially offset by incentive comp payout this year as well as higher cash taxes. Turning to share repurchases and capital allocation.

With the new credit deal, core performance and our outlook, we are stepping up the pace of share repurchases while remaining committed to a strong balance sheet. To this end, this morning, we announced a nearly $400 million increase to our share repurchase authorization and a $125 million ASR that we intend to initiate this month. Net, we will have $575 million of authorization remaining and repurchased roughly $325 million year-to-date after the completion of the ASR. Combined with dividends, we'll have returned 12% of our recent market cap in the first nine months of this year alone.

With last year's free cash flow as a baseline and adding the benefits of the new credit deal, our shares trade at a pro forma yield of nearly 20%. Accordingly, we believe Signet shares remain undervalued and that share repurchases and attractive organic investments remain the best uses of capital to create value for our shareholders. The incremental cash from the new credit deal will only increase our ability to invest in both of those. To recap, we delivered another quarter with positive comps and margin expansion, leading to 36% adjusted EPS growth.

We strengthened our balance sheet, signed a credit agreement adding meaningful value and are significantly stepping up our return of capital to shareholders while ultimately increasing our adjusted EPS guidance by over 10%.

Turning to guidance, we are raising our guidance for the year to reflect first half performance, a modest increase in expectations in the back half of the year, the improved economics from the credit renewal, refund of tariffs previously paid and additional share repurchases. For the full year, we now expect the same-store sales range to be flat to up 2.5%, increasing the low-end guide 75 basis points. This reflects AUR and unit trends in the back half similar to those in the first at the midpoint.

We now expect adjusted operating income between $535 million and $605 million, up nearly 10% or $50 million at the midpoint. This range includes the benefit from the new credit agreement and $30 million of refunds on tariffs previously paid, inclusive of the $15 million realized in Q2, primarily direct refunds.

Of note, the refund represents less than half of the net headwind from incremental tariffs in the current year. With respect to indirect refunds, we're assuming no material amount in the current year. However, timing of refunds of indirect tariffs paid is still fluid. At this time we expect indirect refunds to benefit fiscal '28 at a similar level or somewhat higher level than direct refunds this year.

We are also actively working to accelerate holiday receipts in advance of any potential sanctions on countries that import Russian energy. As a result of these changes, we now expect GMM expansion for the full year, driven by the back half. Turning to SG&A.

We expect to show leverage in SG&A for the entirety of the year across the range with modest deleverage in the second half of the year. The deleverage in the back half reflects $17 million to $25 million higher incentive comp expense as a result of the increase in our guidance and the expected cash from the new credit agreement.

In addition to the above, we are also increasing fiscal '27 adjusted EPS guide to include additional share repurchases as well. In aggregate, our guidance range is increasing by over 10%. Finally, for the year, we continue to expect $150 million to $180 million in capital expenditures.

For the third quarter, our smallest quarter of the year, we expect a same-store sales range of down 1% to up 2% with adjusted operating income between $31 million and $48 million. This quarter, we expect $7 million to $9 million of benefit from refund of tariffs previously paid.

We expect benefit in the quarter from the new credit deal beginning in September in the range of $12 million to $16 million. We expect 40% to 50% of the incremental incentive comp expense noted a moment ago to flow into the third quarter, causing modest SG&A deleverage. Before we turn to Q&A, I'd like to thank our team for their continued commitment and the execution of our Grow Brand Love strategy. Operator, now let's go to questions.

QUESTION & ANSWER:

Operator^ (Operator Instructions) Your first question comes from the line of Randy Konik with the office of Jefferies. Your line is now open please go ahead.

Randy Konik
Jefferies; Analyst

Yes thanks a lot and thzanks for taking my question. I guess, first, JK, when you think about your conviction and confidence for the back half of the year, what in your strategy or the recent strategies you've taken on and then execution improvement on the team and in different areas of that are giving you that confidence and conviction to kind of do well in that and continue this momentum into the back half of 2026.

J.K. Symancyk
Signet Jewelers; Chief Executive Officer & Director

Yes. Randy, thanks for the question. I think you answered part of the question the way you asked it, honestly. It starts with consistent performance within the business. The fact that I felt like it's important that we've established credibility and accountability to do what we say we're going to do. And that's a track record this team has built and that mantra of performing while we transform the business is an important part of what gives me that confidence.

I think the second, this is a busy quarter, and it's evidence that we're doing a lot of things to really make the business better, both in the short term and the long term. And whether that's what we talked about with website redesign, some of the improvements in the core business, the credit deal, the underlying SKU and inventory reduction that we're seeing across the business despite some of the external factors that might make those moves more challenging.

The improvements we're seeing across merchandise programming, the relaunch of Kay's brand platform, all of the strength of holiday plans that we know are coming, that all gives me confidence. And I think, in particular, coming against a backdrop that has really tested those strategies and the way that our team has navigated that change is the other thing that really helps me have much more faith in our ability to affect our will on the outcome.

And I think that's probably the third leg of the stool. It's -- we've got the right team in place. And I don't think you accomplish all these things if you don't have the right talent deployed against the right strategy. And when I look at that and I think about some of the things we talked about that are clearly adding value to the business in this quarter really does position us to strike that balance between improving short-term results, but also gives us the fuel to invest in these things that we believe are going to create long-term value for both customers and ultimately, shareholders.

Randy Konik
Jefferies; Analyst

Super helpful. And I guess for Joan, one thing that we keep kind of telling people is to buy the math, and that means look at the cash flows that Signet generates and not just the overall cash flow, but the free cash flow at that.

So maybe kind of give us a reminder on what you think is base level of free cash flow from an ongoing standpoint to give us some perspective on how you think about the CapEx needs of the business. You gave us a little math there before. And then maybe talk about, I guess, a couple of quarters ago, you gave us a change in philosophy on in terms of financial capacity, I think you said -- you went like (inaudible) financial ability.

That's down $1.5 billion, meaning you're more aggressive with the balance sheet that's cash but also cash flow. Just kind of give a perspective on how we should be thinking about that you already kind of put together the ASR (technical difficulty) giving aggressive purchasing productivity going off this innovation, just give us more discussion on this.

Joan Hilson
Signet Jewelers; Chief Financial & Operating Officer

Well thank you for the question, Randy. I would say that the last part of the question, I think we were able to get the intent of the question. You were breaking up a bit. But to start off, the baseline, yes, what I would share with the -- on the call here is that we are continuing to drive inventory discipline. one is you saw that we were down 1% in overall inventory even with gold cost.

JK mentioned inventory and SKU rationalization to really improve the health of our inventory. And so that's a lever we continue to pull. Spend discipline is another lever that we continue to pull. And then the vendor payables, I noted in my prepared remarks that we have improved the days payable outstanding by one week which is a meaningful change in our business.

So applaud the teams for working with our vendors to really drive that improvement for us. And so we continue to drive free cash flow in a similar fashion while improving inventory and our vendor terms and agreements that we have. So continued positivity there.

As we look at our principles on capital allocation, we see a floor of liquidity of $1.5 billion. And we consider anything above that, and we can target that at the end of the year, but we consider anything above that to be excess cash on the -- within our cash opportunities. And number 1, organic investment.

JK talked about them. We are investing in the website redesign. That is going well. So we'll continue to identify opportunities such as that to continue our organic investments including our fleet. We talked about $150 million to $180 million of capital investments.

That's in our guidance. So that's, we think, an important use of capital. And beyond that, returning excess cash to shareholders is a very high priority for us. We talked about on the call that if you just use the baseline of FY '26, it's a pro forma 20% yield. And we believe that we have an attractive value within our stock and continue to prioritize the share buybacks.

We also noted that we increased the authorization of our share buyback program. And on the completion of our ASR of $125 million, we'll have $575 million remaining. So believe that we have a good capital allocation plan and priorities and look forward to continuing to drive that forward.

Operator^ Your next question comes from the line of Paul Lejuez with Citi.

Paul Lejuez
Citi; Analyst

Curious if you could talk -- I think you said you changed something in the back half of your guidance slightly. Just curious if you could talk about what that was. Any comments about third quarter to date? And then on the credit agreement, I think you mentioned, Joan, the $200 million to $250 million in profit over the next 36 months.

Can you just go into a little bit more detail on how that flows? I think you said $1 billion overall over the life of the agreement. So can you just talk about the difference between the next 36 months and then what happens beyond?

Joan Hilson
Signet Jewelers; Chief Financial & Operating Officer

Sure. So if we first address the guidance question and the back half. We raised the midpoint of our same-store sales guidance for the full year, 37.5 basis points. So -- and that's based on the year-to-date performance and slightly higher expectations for the second half. And we raised the low end by 75 basis points. So high end stayed the same, raised the low end 75 bps based on performance.

We increased our adjusted EPS guide by 10% for the year, reflecting the year-to-date performance as well as the new credit agreement, the refund of tariffs previously paid and then the additional share repurchases. So basically, two-thirds of that raise came from the newer items that I just mentioned and a third came from the core performance. We're pleased with the performance in margin on the core business.

We were at expectations in -- for the core performance in the first half of the year and through the back half flat to slightly up. So continuing to manage the merchandise margin well. The team has done a good job, as JK noted in his remarks. And then we expect modest SG&A leverage for the year including the increase in incentive comp. So -- and that's a $17 million to $25 million higher SG&A cost to us.

So feel that with the management of merchandise margin, the management of spend discipline and really harvesting the benefits of our operating model shift, we've been able to really post up and raise our guidance for the year. And so we're very pleased with that. With respect to the third quarter to date, as you know we do not comment on like intra-quarter performance as part of our practice.

But what we can say is that we're currently well within the guidance range provided for the third quarter. And then with respect to the Bread deal, we are very much pleased with the partnership with the Bread Financial team.

And what I was sharing is that the economic benefit over the term of the agreement is greater than $1 billion through 2035. And importantly, that includes consideration for any sort of recessionary activity, and that's important to note that there's no loss sharing within this agreement. So we feel confident in terms of the benefit that we've provided over the $1 billion over the term of the agreement.

It's a quarterly profit sharing which is recorded as revenue and incremental operating income. And it is -- when you think about the $200 million to $250 million, that's over 36 months. And what that reflects is just a profit sharing on the performance of the portfolio as well as there are other elements of benefit to Signet economically within that range.

So we'll believe that it's a strong agreement and that importantly to note that the profit sharing ratios increase over time. So the better the performance of the portfolio, we continue to generate economic benefit to Signet and the shareholders.

Operator^ Your next question comes from the line of Jeff Lick with Stephens Inc.

Jeffrey Lick
Stephen Inc; Analyst

Congrats on some great results. Joan, just to kind of build on what Paul's question was, maybe just thinking it in a different way. If you just kind of straight line and said, okay, 10 years, $1 billion, so it's $100 million a year, would the right way to be thinking about it is, all else equal, assuming that none of us move about this agreement which we didn't until right now that whatever you thought SIG was going to make, you're now basically just at $100 million of EBITDA on top of that.

Joan Hilson
Signet Jewelers; Chief Financial & Operating Officer

Yes. What I said in my prepared remarks, Jeff, it's incremental to Signet.

Jeffrey Lick
Stephen Inc; Analyst

Okay. Great. That's very helpful. And then JK, one for you. Just curious an update. Obviously you talked a lot over the last year about the challenges that you have in 4Q last year. You've divided the 4Q into three different shopping occasions effectively or segments and the inability to have the $150 to $250 price points. Just an update there as you head into that important season. How confident are you on where things stand being improved over last year?

J.K. Symancyk
Signet Jewelers; Chief Executive Officer & Director

Yes. I appreciate the question, Jeff. I'm feeling good as we go into Q4. And I think it's an equal part of addressing those things that we learned about the consumer, but I think we're better positioned as we go into this year, not only to meet them where they are, and that's a combination of we talked about in marketing, website redesign which I think was a limiting factor for us as we look at some of these last couple of years and that earlier season in November, especially.

But we -- with -- last year, we were obviously chasing tariffs and dealing with pretty volatile inventory environment and not just tariff, gold, all those sorts of things. I think our team did a great job of managing all of that to the tune of not creating a headwind.

But it certainly makes merchandise assortment changes a little more challenging. And I think having a much more stable playing field in front of us and the agility that we picked up we've been much more intentional going into the quarter around how we leverage all price points across all brands to really put ourselves in a better position to take advantage of the power of the portfolio. And I think that plus getting some progress behind us in terms of brand distinction, it really puts us in a position to show up with a much stronger footprint as we go into Q4 this year.

Jeffrey Lick
Stephen Inc; Analyst

And then just a quick housekeeping one for Joan. Joan, I think in your prepared remarks, you made reference to the new tariff rate being higher than the old tariff rate. Did I hear that wrong? Or could you just -- obviously there's a new tariff rate that will be in place that replaces the IEEPA tariffs. Is that in your guys' case, effectively higher? Or did I hear that wrong?

Joan Hilson
Signet Jewelers; Chief Financial & Operating Officer

It's not effectively higher. It's just the way that our inventory turns over time and the impact of the tariff on the turn as it flows through cost of goods. So it's really something that we've been able to manage. What I also did say is that the tariff -- the refund of tariffs previously paid did not fully offset the impact of tariffs in the year.

So that's also something that the team was able to hurdle, Jeff, and work through it with just working with the vendors with some price increases as well as just overall managing the assortment mix to gain the benefits that we've been able to do within the merchandise margin.

Jeffrey Lick
Stephen Inc; Analyst

But the tariff impact is really more just a timing issue for tariffs that you probably paid six to nine months ago that just show up in cost being sold down?

Joan Hilson
Signet Jewelers; Chief Financial & Operating Officer

Yes. Sounds accurate. Thanks for the clarification.

Operator^ Your next question comes from the line of Rick Patel with Raymond James.

Rick Patel
Raymond James; Analyst

Congrats on all the progress and strong execution. Can you talk about the trajectory of AUR? I think it was 6% in the quarter. It's a modest acceleration versus the prior quarter. What drove that? Was it pricing or sales mix? And how do we think about the durability of AUR growth for the back half?

J.K. Symancyk
Signet Jewelers; Chief Executive Officer & Director

Yes. Thanks for the question, Rick. I mean I think the AUR is really influenced probably more by mix than anything across our business. Part of that, I mean we talked about strength across the core brands. That one of our brands that isn't seeing that at the same rate is Banter.

That drives a healthy amount of unit performance for our business. And when that is not seeing the unit growth, and I mean it is seeing some AUR expansion just because of what's going on with gold, but it changes what mix looks like within our business. So there's a little bit of AUR inflation as a function of mix, but it is also reflective of our ability to move higher in price point within our brands.

We're intentional around the opportunity we see at higher price points, particularly in natural diamond, both fashion and bridal, where we see some share -- potential share gain opportunities and I think some assortment balance opportunities across our portfolio. So I do feel like for the near term, AUR is going to be a little bit bigger part of the story. But we also -- we ultimately look for balance between the two and think modest unit growth and a little bit stronger AUR expansion is the right mix for our business for the longer term.

Rick Patel
Raymond James; Analyst

And how do we think about the impact of gold prices from here? Prices are below the peak in January, but higher than where they were mid-summer. So does that impact -- how does that impact the gross margin line as we think about the back half? And is there anything to call out for early fiscal '28 as those costs make their way through the system?

J.K. Symancyk
Signet Jewelers; Chief Executive Officer & Director

No. I mean this is not a new phenomenon, Rick. The question is a good one, but it's something we've been dealing with for a while. And so the answer is pretty similar. I think we've thought about from a design and mix standpoint, how do we engineer the right product at the right price points for customers and deliver the right value proposition.

There's no question any time we've seen gold price increases pass through to the consumer at an industry level, not just Signet, we see some resistance on units and a little bit of pullback, particularly at kind of lower kind of value price point and gold weights. But we're also sitting in a position where that is not our biggest input cost.

Our biggest input cost is actually diamonds. And so we are fortunate that we sit in a market where on both sides, natural as well as lab-grown, there's opportunity there. Their ability to balance that across the fulsomeness of our portfolio from a finished jewelry standpoint really does position us. So our guide reflects all of that.

It has, and our team has really been navigating this environment now for -- if you talk about those five of the last six quarters, that has been true in all of those quarters on some level. So we're well positioned to be able to navigate that.

Operator^ Your next question comes from the line of Ike Boruchow with Wells Fargo.

Ike Boruchow
Wells Fargo; Analyst

Joan, thanks for all the help on the credit agreement and the benefits. Just at a super simplistic level, is the benefit expected to, over the next three years, effectively take EBIT up 50% outside of any organic benefits to the business?

Or would you expect some of those dollars to be reinvested or a good portion of those dollars to be reinvested into the business somehow? I'm just asking because it's a meaningful impact to your EBIT. And so I'm just kind of curious how we should think about the models building over the next three years because of it?

Joan Hilson

Signet Jewelers; Chief Financial & Operating Officer

So it's a great question. And as we navigate through to next year, we will evaluate what reinvestment is required along with continued spend discipline management and other actions that we would take to continue to drive margin expansion for the business. But we would expect to see a majority of flow-through to an economic benefit. But remember, as we -- as I have mentioned that the rate of sharing increases over time. So it's not something that you should think about on a straight-line basis.

Ike Boruchow

Wells Fargo; Analyst

Right. I guess if you have multiyear line of sight in that capacity, it's somewhat similar to Randy's question. Like do you look at your stock and consider -- obviously you're being aggressive on the buyback with your cash, but do you consider adding leverage to take advantage of that scenario given it seems like there's a lot of profit growth that the market doesn't seem to be giving you credit for at this point?

Joan Hilson

Signet Jewelers; Chief Financial & Operating Officer

At this stage, we're not considering adding leverage for that. But what we are considering is as we look at our capital allocation priorities, we believe that the deal that was on the table enables us to truly evaluate and prioritize investment as well as return of cash to shareholders in a different light than we've been able to do in the past. And so we are also feeling very strongly about the core performance of our business.

So with those two thoughts in mind, we believe that we have flexibility on where we can invest in our business to actually work the short term and invest in the long term to continue sustained improvement in our operating performance.

Ike Boruchow

Wells Fargo; Analyst

Got it. And sorry, the last one, Joan or JK. Just on the gross margin line, so ex the refund, gross margins are still down. I think last time we heard from you, you expected them to be flat and then up in the fourth quarter.

Can you just confirm if that's still the plan? And just kind of -- I'm sorry if you gave it earlier, Joan, but maybe just the building blocks of the gross margins. What are the good guys and bad guys in the second quarter that still caused a like-for-like decline year-over-year?

Joan Hilson
Signet Jewelers; Chief Financial & Operating Officer

Yes. So the second quarter actually came in at our expectations. And so from a core perspective, and we expected the margins to -- merchandise margins to be down. And so what we cite there is just continued pressure from tariff and gold costs and really trying to drive through the inventory turn. And as we got into the back half of the year with the price increases, as well as the assortment opportunities that JK mentioned, we've been able to look at flat to slightly up in the back half of the year in terms of merchandise margin.

And just to add on to that, our promo, our conversion rate is consistent in our view of guidance. So it's really about really understanding the core components of the product, really optimizing in that regard while delivering product that the customer still sees the value in. And so that's really how we've been managing margin go forward. So flat to slightly up in the back half.

Operator^ Your next question comes from the line of Lorraine Hutchinson with Bank of America.

Lorraine Hutchinson
Bank of America; Analyst

Could you talk a little bit about the performance of fashion ex Banter and then the role that lab-grown is playing in that fashion performance?

J.K. Symancyk
Signet Jewelers; Chief Executive Officer & Director

Yes. Sure. We continue -- I think one of the things that is important to note in our breakdown, fashion is pretty much everything. It's not bridal. So on the whole, I would describe it as flattish ex Banter with the same comments we outlined in the call as driving more growth on the high end and the middle end and then anything that is sort of in the lower end exposed has been where there's softness. That really is all tied to metal.

And as we've seen -- as we move forward, we have confidence in both plans of what we've got in the pipeline in terms of new receipts, new programs for the holidays as well as how we're seeing the customer adjust to the new normals with gold that we feel strong about that performance. Within fashion, I mentioned higher price point is an opportunity.

We've seen strength there. Natural diamond, we continue to see as an opportunity. Lab-grown diamond fashion still coming off of a low base, obviously because so much of fashion has been without stone in our business, but is driving growth for us. And then even though we don't carve it out, Timepieces is really a source of strength across the business that has kind of flirted around the double-digit growth line for a couple of years now. So I feel good about fashion.

I think as we go into the back half of the year, also more optimistic around some of the plans we have with men's which has driven growth, color which I think is an opportunity in our assortment today that we address moving forward. So looking to build on that momentum and really extend it across all price points.

Operator^ Your next question comes from the line of Mauricio Serna with UBS.

Mauricio Serna
UBS; Analyst

I guess just maybe you alluded a little bit to the back half of the year, specifically for Q4, what's the implied comp in your guidance at the low versus the high end? And maybe you also talked a little bit about the promotions. Maybe could you elaborate a little bit more about what you saw in promotions this quarter on a year-over-year basis? And what are your expectations for the holiday season?

J.K. Symancyk
Signet Jewelers; Chief Executive Officer & Director

Yes. Let me take promo first. I mean I think Joan hit it importantly. We've maintained some really good discipline there and have really been -- I've been proud of the team's ability to manage that. I think we found ourselves in a position this last year Q4, where given the start, we were a little more promotional going into it.

I think we are much more confident of not only our base plan and the way we're attacking those kind of three parts of the season, how we're leveraging the strength of the portfolio. I think we're more coordinated across our efforts going into the holiday this year. But we also have better contingency plans in place. And so I think you'll see that discipline hold.

I do believe, just given the state of the consumer that value is going to be a big story, value being sort of the right quality at the right price and really delivering on it, not necessarily meaning that in terms of high end or low end, but really how do you set up the consumer to be motivated by value. And I think we are much more mindful of that.

It's reflected in our guide. So when we talk about being well positioned for that and also going back to previous questions about margin, our expectation that we'll be able to hold and strengthen our margin performance as we go into it is something that is fully contemplated in that guidance. So we're -- that's what we're seeing.

We're not seeing any sort of elevated or crazy promotional response from others in the industry right now. And so I think we've got the right kind of measured approach to make sure we've got the right value proposition to win during the quarter and also still deliver on the improvements that we're talking about.

Joan Hilson

Signet Jewelers; Chief Financial & Operating Officer

Mauricio, to your question on the implied guide, the top line range is implied at minus 2% to plus 3%. And it's an increase of approximately 25 basis points on the low end and 60 basis points on the high end, reflecting current performance -- and then I would just articulate here that the -- at the midpoint, we see ample opportunity in the fourth quarter for benefit for us. And where our two- and three-year stacks are -- if you look -- if you do the math, it's down low single digit on a two-year and flattish on a three-year. So I believe that there's ample opportunity in our -- in that quarter for us to really bring home a nice performance.

Mauricio Serna

UBS; Analyst

Got it. Very helpful. And then just one quick follow-up on the new credit agreement. I guess, can you just give like a high level, what drives these benefits that you're going to get? What changed versus the previous credit agreement? And just to confirm that, that would still imply that you don't have -- you're not going to carry the credit in your balance sheet, right? I would assume that kind of continues to be the case.

Joan Hilson

Signet Jewelers; Chief Financial & Operating Officer

Thank you for the question. Yes. It is not us. The credit portfolio will not be carried on our balance sheet. It is owned by the third-party credit provider. The change in the agreement is at the highest level is the profit sharing agreement which we did not have in our previous agreement.

We're very pleased to be able to bring that through a competitive bidding process, and it was really on the strength of the portfolio that we have today, and it's something that our partners see as beneficial to both of us. And so the profit sharing is something that we feel we'll both benefit from, but also the key point in that, Mauricio, is that there is no loss sharing.

So if -- for example, if there was net a loss in the portfolio that would not impact -- we would not share in a loss. And in fact, there are other revenue-generating opportunities with the agreement which are all factored into the view that we gave of over $1 billion in benefit over the term of the agreement.

So we believe it's a very strong agreement for both parties and one that will really serve our customers well because we'll be able to continue to bring financial services offerings to them that enable cross-shopping, and we're launching the Blue Nile credit card for the first time ahead of holiday. We're really pleased with being able to do that in such a quick fashion. So overall, it was a very favorable outcome, we believe, for both of us.

Operator^ Your next question comes from the line of John Keypour with Goldman Sachs.

Jonathan Keypour
Goldman Sachs; Analyst

Just a quick one on the credit agreement. I was just wondering if you mentioned that the economics improved, right, the sharing ratios increased over time. I'm just curious if there are like provisos or anything you have to accomplish for that to happen or if it just naturally scales as part of the deal?

Joan Hilson
Signet Jewelers; Chief Financial & Operating Officer

That is part of the arrangement that we have in our agreement. There's no threshold.

Jonathan Keypour
Goldman Sachs; Analyst

Okay. And then a follow-up just on unit growth. You mentioned you called out in the press release that higher ticket items did very well high single-digit growth. But you flagged in the past that the sub $250 or the sub $150, like the cheaper it gets, the harder it gets to sell. I'm just wondering what you saw at that end of the ladder. And my understanding is that the lower-priced items are actually quite high margin. So how does that factor into the margin expectations for the second half of the year?

J.K. Symancyk
Signet Jewelers; Chief Executive Officer & Director

Yes. No. I appreciate the question. I mean the simple answer is it's all contemplated in the guide. We saw performance in Q2 consistent with what we expected. I'll remind you that a disproportionate amount of our unit performance happens within Banter and our core brands happens online.

It is outsized relative to what its contribution to revenue is. And so I won't go through all of those numbers. People are probably tired of hearing me talk about price points and doing that math. But we have actually taken actions as it relates to new receipts in the holidays that we believe fortify those positions. We're seeing -- we've tested a lot through Q2 and into Q3 that really informs that confidence.

And those receipts, as we've talked about on these calls before all happen to flow through in really September. And so it was consistent performance with what we had seen and consistent to what we had guided to. And I would say one important distinction, I know there was a lot in the script, so I'll reiterate this just in case anybody missed it.

While we've got confidence in the plans that we have in place to improve it, we also haven't dimensionalized big changes in performance by price point as we look at the guide for the back half of the year. We think it -- so that guide reflects the consistency we talked about.

On your question around margin, yes, I mean it's we've seen margin rate expansion modestly in the back half of the year. The guide contemplates that. And we've been able to manage mix. I think the reality is the percents obviously change and look a little more attractive on some of the lower price point goods. But the contribution of the flow-through on the higher price point is still really good and accretive for our business.

And so where so much of our business happens is in that mid-tier, and we've seen really good stability there. And so no real callouts other than what we've talked about before. We continue to see an opportunity for some rate expansion in the back half of the year. As Joan put it, we saw improvement to the trend and saw that margin fall exactly where we thought it would for Q2 once you strip out tariff refunds. So I feel good about where we're positioned going into the next -- this back half.

Operator^ Your next question comes from the line of James Sanderson with Northcoast Research.

James Sanderson
Northcoast Research; Analyst

Congratulations for a great quarter. Just wanted to go back to outlook for the rest of the year. You mentioned e-commerce platform improvements at Jared's and at Kay's. Wondering if you can take those learnings and help us understand how that might be a benefit to Zales going forward and if those benefits are part of your guidance already?

J.K. Symancyk
Signet Jewelers; Chief Executive Officer & Director

Sure, Jim. And I'll clarify one thing you said just to make sure everybody is on the same page. It's not a platform change. It's user experience redesign. So the only reason I think that's important is obviously the more you invest with the back end, the more you introduce potential challenges. That's not what we've done with our websites. Back end is functional. Company has invested a lot over the last several years to make the backend sound.

So when you think about that end working, we're good. Where we've fallen short really was in our -- what does the customer see and how do we connect with the customer in a way that they shop most today. And so we've redesigned that front-end experience for our three largest brands, Kay, Zales, Jared. We have launched live already, Jared and Kay. And what we said in the call is early results are promising.

I think we didn't give specific numbers because I think it takes more than two or three weeks for us to start reporting on something like that. But we've come out of the gate strong. We're seeing better engagement from customers. We're seeing average order value increases. We're seeing engagement with our product display pages higher. And all of those things bode well as you move into a critical time period for our -- for that to be a bigger part of our business.

Importantly, too, we did all this, no negative impact. This was -- our team did a tremendous job of managing all of this on the back end, running in parallel and flipping a switch in a time period where it frankly was seamless. And so I really appreciate the work that went into it.

We will launch Zales later this month. That gives us plenty of time to do two things really. One, to really rebuild natural search algorithms and all the things that happen when you start to change content. But two, it also gives us an opportunity to learn where customers are engaging the most and how to best leverage those improvements in a way that we can play offense.

And when it's all said and done, I mean it may sound soft, but better imagery, realistic on-model presentation that really does help a customer imagine style and trend differently and how it might fit them, much simpler navigation, sort of a shoppable editorial and the ability to navigate the site and shop in a more modern, intuitive and frankly, more inspiring content.

Part of that redesign is not just the wire frames of the page, but it's updated content, all new photography, imagery, introduction of live video, better engagement that really does help whether you're in the discovery phase for something that you know you want or you're shopping for the -- you're just looking for a thing and you're trying to be inspired. And so really like what we're seeing from customers so far and think that it obviously is going to help us as we go through the back half of the year.

James Sanderson
Northcoast Research; Analyst

All right. I had one quick follow-up question on the credit agreement. Given the magnitude of the agreement, how does this improve the flow-through profitability you expect out of the business over the next several years?

Joan Hilson
Signet Jewelers; Chief Financial & Operating Officer

We would expect -- what I mentioned, Jim, earlier, is that we view it as incremental to Signet and that it gives us the opportunity to consider some reinvestment and really bring a better experience to customers with the hope of continuing to grow the credit portfolio with our partner and again, include a greater profit sharing for the company. So we see it as a plus an incremental benefit, and it also provides flexibility for investment.

James Sanderson
Northcoast Research; Analyst

So would you expect that to slightly improve that outlook or that target going forward? Is that the right way to look at it?

Joan Hilson
Signet Jewelers; Chief Financial & Operating Officer

We would expect, yes, our outlook for our operating margin to improve.

Operator^ There are no further questions at this time. I will now turn the call back to JK Symancyk, Chief Executive Officer, for closing remarks.

J.K. Symancyk
Signet Jewelers; Chief Executive Officer & Director

Thank you, and thanks everyone, for joining our call today, and thanks once again to our team. We look forward to discussing further detail on our holiday plans and our Grow Brand Love progress in December. Until then, good-bye for now. Thanks.

Operator^ This concludes today's call. Thank you for attending. You may now disconnect.