06-Dec-2022

Signet Jewelers Ltd. (SIG)

Q3 2023 Earnings Call

Copyright © 2001-2022 FactSet CallStreet, LLC

CORPORATE PARTICIPANTS

Vincent J. Sinisi
Senioir Vice President-Investor Relations, Signet Jewelers Ltd.

Virginia C. Drosos
Chief Executive Officer & Director, Signet Jewelers Ltd.

Joan Holstein Hilson
Chief Financial & Strategy Officer, Signet Jewelers Ltd.

OTHER PARTICIPANTS

Mauricio Serna
Analyst, UBS Securities LLC

Lorraine Hutchinson
Analyst, BofA Securities, Inc.

James Jon Sanderson
Analyst, Northcoast Research Partners LLC

Will Gaertner
Analyst, Wells Fargo Securities LLC

Paul Lejuez
Analyst, Citigroup Global Markets, Inc.

MANAGEMENT DISCUSSION SECTION

Operator: Hello everyone and welcome to the Signet Jewelers Fiscal 2023 Third Quarter Earnings Call. My name is Emily and I'll be coordinating your call today. At the end of the presentation you'll have the opportunity to ask a question [Operator Instructions] I will now hand the call over to our host, Vinnie Sinisi, Senior Vice President of Investor Relations. Please go ahead.

Vincent J. Sinisi

Senioir Vice President-Investor Relations, Signet Jewelers Ltd.

Good morning and welcome to our third quarter earnings conference call. On the call today are Signet's CEO, Gina Drosos, and Chief Financial and Strategy Officer, Joan Hilson. During today's presentation, we will make certain forward-looking statements. Any statements that are not historical facts are subject to a number of risk and uncertainties, and actual results may differ materially. We urge you to read the risk factors, cautionary language, and other disclosure 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'll discuss certain non-GAAP financial measures. For further discussion of the non-GAAP financial measures as well as reconciliations 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 www.signetjewelers.com/investors. With that, I'll turn the call over to Gina.

Virginia C. Drosos

Chief Executive Officer & Director, Signet Jewelers Ltd.

Copyright © 2001-2022 FactSet CallStreet, LLC

Thank you, Vinnie, and thanks to all of you for joining us today. I want to begin by thanking the entire Signet team for a standout quarter in a challenging retail environment. Their passion for rising to every challenge and opportunity is inspiring. I'm particularly pleased that our Signet team was recognized this quarter by Fortune as one of the Top 20 Best Workplaces in Retail. This is a great reflection of the purpose, pride, and excellence our team members bring to our customers every day. I'm proud to lead this exceptional team.

There's one core message that I want you to take away from today's call; Signet is uniquely positioned to deliver consistent market share growth and value creation given our number one and growing leadership position in jewelry, an industry that tends to grow steadily from year-to-year and is more resilient to economic cycles than other parts of retail. We've established our strong position in this attractive industry over the past five years by making significant strategic pivots that are now creating a virtuous flywheel effect when compounding advantages that are accelerating positive momentum and growth.

First, we've created a differentiated portfolio of banners that appeals to a broad, diverse, and growing mix of customers. Second, we've established a Connected Commerce presence that is resetting customer expectations for the experience they want to have with shopping for, buying, and owning fine jewelry. Third, we've built a flexible operating model that gives us multiple levers to pull so we can deliver our commitments even when faced with challenging economic or market conditions. And fourth, we're executing a disciplined capital allocation strategy that is delivering meaningful value creation. It's focused first on expanding market share, growing the top line, and consistently delivering double-digit annual operating margin.

Since the beginning of our transformation in fiscal 2019, we've invested nearly $700 million in capital and over $900 million in acquisitions, far beyond any company in the industry. On the strength of these investments, we've accelerated growth and returned more than $1.3 billion to shareholders through share repurchases and dividends. We saw the benefits of this flywheel effect again in the third quarter; we beat expectations and are now raising full year guidance inclusive of Blue Nile. Revenue was nearly $1.6 billion, up 2.9% versus year-ago and up 33% compared to pre-pandemic levels. We generated non-GAAP operating income of $58 million, a strong result in a quarter that saw one-time COVID and supply chain-induced benefits last year but consistently lost money prior. In fact, Q3 fiscal 2020 suffered operating losses of nearly $30 million.

And we delivered non-GAAP operating margin ahead of expectations for the quarter. This improvement was largely driven by the positive impacts of services, the health of our inventory and strategic assortment choices including tiering-up, value engineering and balanced pricing. We achieved this despite Blue Nile losses which we anticipated and more than covered without impacting our core businesses or distracting us from disciplined execution.

Now even in a challenging environment, we're heading into holiday with multiple points of strength. First, we're well stocked with significant newness and great value at all price points; and most importantly, we're not overstocked like much of retail. In fact, our inventory was down 2% in the quarter excluding acquisitions; and with clearance at the lowest levels in recent history, it's healthier than it's been since our transformation began roughly five years ago. We've tiered-up our assortment and nearly 30% of our assortment is new for holiday. Since Q3 fiscal 2020, our inventory is down 17% excluding acquisitions, with sell down and clearance penetration down 13 points.

In addition to being well stocked, we're well staffed. A key driver of our staffing strength is retention. At KAY's for example, staff turnover is 17% lower than it was last year. This ensures we have more experienced consultants on the floor, an important factor because consultants with at least 2 years of experience in our stores sell two times more than consultants who've been with us for 6 months or less. And we're able to optimize labor costs by

Copyright © 2001-2022 FactSet CallStreet, LLC

adjusting staffing plans dynamically in response to changing retail traffic. Using our proprietary store level data we can flex to optimize coverage by hour when and where we need it without being under- or over-staffed. As a result, our sales per labor hour are up more than 70% versus fiscal 2020.

We're still facing macroeconomic headwinds and consumers' behaviors can be somewhat volatile, but we're prepared for this. Our flexible operating model is designed to sustain our financial commitments even in the face of these challenges. We're ready for strong holiday execution. Now I'd like to provide prospective on where we're headed longer-term and why Signet is so well-positioned to deliver consistent market share growth and value creation year-over-year. My confidence in our long-term growth is grounded in both the attractiveness of the jewelry industry itself and in Signet's strong leadership position within the industry.

Jewelry is different from the rest of retail, for example, cyclical industries like apparel are more sensitive to economic volatility, carry inventory with a relatively low residual value. And sell products that consumers see as more discretionary. Conversely, customers placed a higher value on jewelry. They see jewelry purchases as less discretionary because they're tied to special occasions and people in their lives and jewelry retains its value or appreciates over time. In addition, jewelry doesn't go out of style from season-to-season. This makes jewelry more resilient, and as a result, more attractive than many other retail industries. It's an industry well designed for sustainable long-term growth.

And Signet has an advantageous position in this attractive industry. Jewelry rewards the flywheel effect I described which is a point of difference for Signet. Inventory is a good example. Over the past five years, we have transformed the way we plan, manage and optimize inventory. We operate today with a disciplined, tightly integrated approach. First, we leverage our vendor relationships and purchasing scale to ensure quality and availability while managing cash and protecting margins. Second, we consumer test our assortments, with the most advanced AI and data analytics capability in the industry. We believe our proprietary product concept testing capability is improving our new product success rate, enabling us to bring bigger ideas to market with greater confidence and speed.

Third, we provide unrivaled inventory depth and transparency to both customers and our jewelry consultants. Customers can work with our virtual and in-store consultants to find, see and purchase individual pieces across our multi-banner ecosystem. And finally, we provide a full range of flexible fulfillment options including buy-online pickup in-store, ship-to-store, curbside pickup, same-day delivery, and now more than 25,000 secure consumer access points. After launching the program just two years ago, customers are opting for a flexible fulfillment option in over 38% of online orders. These capabilities not only benefit our customers, but also minimize stranded inventory across our fleet.

Taken together, this holistic approach to inventory design, management and delivery is a significant competitive advantage. And it has driven significant inventory productivity gains with our core turns of 1.5 times now nearly twice what they were when we began our transformation. I'd like to turn now to progress we've made in the quarter on our four Where to Play focus areas. Let's start with winning in big businesses. A good illustration is how we are growing market share, and winning in bridal. It's the most important segment in fine jewelry. Not only because of its high relative value, but also because bridal is the point of market entry for jewelry lifetime value.

It's the emotional and financial moments when long-term relationships are established between couples and with their jewelry consultant, 35% of new customers during Q3 made their first purchase at Signet through bridal. And over the past 3 years, roughly a third of bridal engagement customers have returned for subsequent non-engagement purchases, wedding bands, fashion jewelry, statement pieces and gifts. This is a more than 40% higher repurchase rate versus non-bridal customers, an average transaction value of their second purchase has

Copyright © 2001-2022 FactSet CallStreet, LLC

increased, up 23% compared to 3 years ago. We've also continued to widen our customer funnel with Diamonds Direct and Blue Nile, two very strategic acquisitions that focus in bridal and have brought younger, more affluent and more diverse customers to our business.

The good news is that over time bridal is not cyclical. Engagements, weddings and anniversaries happen consistently, year-in and year-out. COVID is presenting what is the first meaningful blip in engagement ring purchases in the past four decades. Calendar year 2021 represented a 40-year peak in engagements which is being somewhat offset in 2022 and 2023. Both expected to be down low double-digits. We anticipated this blip in consumer dynamics and positioned ourselves to increase our share of bridal and lean into fashion and gifting. As engagements return to more normalized levels we will be especially well-positioned given that maximizing lifetime value is an ongoing priority for us and a playbook that we are running across our entire business.

Accelerating services is our second strategic focus area. As we've said, we see services as a $1 billion business over time and we're continuing to make steady progress towards that goal. The success of our loyalty program Vault Rewards, is a good example. We already have 1 million Vault Rewards members in just the first year of the program. Our program is especially powerful because we're the only jewelry retailer that can offer this type of holistic loyalty approach across multiple banners and versus other specialty retail we provide high value given the very nature of what we sell, particularly for the engagement and bridal experience.

Jared was the first to roll this out in the first half of fiscal 2023 and now has more than 30% of sales coming from its loyalty members. KAY and Zales followed with rollouts during the third quarter and are already seeing more than 25% of sales coming from loyalty members. In addition, loyalty members are spending 40% more per repeat purchase than non-loyalty customers on average. And they are making second purchases 25% faster.

In repair, we simplified our offerings with bundles that combine typical repair services. This improves both the customer and the employee experience by simplifying the offer and the operation. Earlier this year, bundles represented about 15% of our repair business. Today, 65% of paid repairs are part of a bundle. This is encouraging because bundles drive margin through AUR, which was up 18% versus a year ago. With this success, we have further opportunity for growth. Our research indicates that only 40% of people who shop in malls even know that our banners do repairs. We see upside potential and have doubled our marketing spend on services versus a year ago which is helping drive growth and customer awareness.

Our third Where to Play strategy is to expand Accessible Luxury and value. Accessible Luxury continues to grow in importance. This top-end of our market now represents approximately 30% of our business, up nearly 10 percentage points versus the pre-pandemic period. The shift toward higher price products is being driven by a combination of factors. Our data-based ability to attract higher income customers, the appeal of our high value assortment and the ability to trade customers up the value chain and our price architecture. We've also added Diamonds Direct and Blue Nile, both of which have a strong presence in Accessible Luxury contributing to the increase. These factors are working. We're seeing spending at higher price points in all our categories, engagement, anniversary and wedding bands and fashion.

Overall, North America average transaction value increased 8% compared to last year and is up 27% versus pre-pandemic. We're equally committed to serve customers at the value-end of the market. This is the cohort that is most impacted by economic pressures and we want to ensure we are providing them with superior value as part of our portfolio strategy. To do this, we continue to innovate within our assortment to cut costs customers don't see or care about and to provide a breadth of financing options for every budget.

Copyright © 2001-2022 FactSet CallStreet, LLC

Leading in digital is our fourth strategy. We're now delivering a digital data-driven Connected Commerce experience that is unrivaled in jewelry. One of the biggest differences in Signet today versus five years ago is the mix of customers we serve. We've added 22.5 million new customers since fiscal 2019. As a result, our customer base is significantly stronger today than it was five years ago; it's younger, more multicultural, more affluent, more digitally savvy, and more demanding in terms of total customer experience. No other jewelry company is as well positioned as Signet to meet these expectations.

In recognition of this shift, we're continuing to enhance our digital capabilities and offerings. We introduced two-way SMS just over a year ago for example, and it now represents 14% of our digital support contacts year-to-date. In Q3 alone, 23% of all contacts were through our SMS channel. This matters; after texting with a jewelry expert, conversion is more than 15 times higher than a typical e-commerce purchase. Interestingly, 60% of these purchases are made online and 40% are made in store. We also know that Net Promoter Scores are typically 15 points higher when a customer shops with one of our virtual consultants.

We've enabled social selling by equipping our jewelry consultants to curate personalized digital style guides and use them as a way to reach out to customers with clienteling support, driving both digital sales and store traffic. Customers can browse and buy directly from the style guides that connect directly via chat, SMS or social platforms. We also know that virtual appointments booked online have more than doubled since last year and sales attributed to virtual JCs have grown 150%. Customers who engage in a virtual appointment convert 12 times more than those who don't and AOV is nearly three times more.

We're also adding enhancements specifically focused on mobile conversion because 87% of our website traffic is now coming from mobile devices. We see digital as much more than a standalone e-commerce capability. The power of digital is the ability it gives us to create a seamless Connected Commerce capability that no one in jewelry can match.

The final point I want to underscore is the strength of our financial position which enables so much of the progress we're making. Disciplined cost management and our flexible operating model allow us to invest strategically in our core business and in acquisitions to expand market share, maintain appropriate levels of leverage, and return cash to shareholders through repurchases and dividends, with a goal of becoming a dividend growth company. So to recap, jewelry is an attractive industry and we're in an advantageous position within this industry. It's analogous to being the best house in a great neighborhood. And given our compounding advantages, we're growing share and investing in growth well ahead of the industry which positions us for sustainable value creation.

As important as our financial health is, it's only part of our story. As I said at the outset, the most important part of our success and of my confidence in our future is our culture of innovation and agility powered by rigorous executional discipline. Our team continues to rise to every challenge and to go after every opportunity to serve our customers, grow our business, and lead our industry. We've built many advantages that set us apart in the jewelry industry and in retail, but none is as important as the caliber of our people and the culture in which they're thriving.

On that note, I'll turn it over to Joan.

Joan Holstein Hilson

Chief Financial & Strategy Officer, Signet Jewelers Ltd.

Thanks, Gina, and good morning everyone. Our key message is that Signet is uniquely positioned among retailers to deliver consistent returns. We're doing this by growing market share, expanding margin, and optimizing our balance sheet, all of which [ph] leads to (00:22:15) long-term value creation. We are committed to delivering double-digit annual operating margin which we're able to do with our flexible operating structure even

Copyright © 2001-2022 FactSet CallStreet, LLC

when the top line environment is challenging, and we are continuing to take advantage of our balance sheet strength to consistently invest in our growth while returning cash to shareholders.

Before turning to the quarter, I'd like to share some additional perspective on our recent acquisition of Blue Nile. This acquisition is a great example of our ability to be agile as market share growth opportunities emerge. Our balance sheet strength and our ability to generate cash enables us to step in at the right time for the right assets at the right price. We've now been working with the Blue Nile team for just over 90 days. We see significant opportunities to maximize value by bringing together Blue Nile and James Allen, our two digitally native banner.

This combination is driving higher synergies than we anticipated at the time of the acquisition. We also see top line and margin opportunity by leveraging assortment, price architecture, data analytics and the integration of our merchandising capabilities. Importantly, Blue Nile enables us to grow our share in bridal with a slightly higher price mix and a demographic that is different and additive to the top of our customer funnel. With all of this in mind, we are reaffirming our full-year non-GAAP operating margin as 10.8%. Even with the diluted impact of Blue Nile, which is offset by a greater line of sight into the efficiencies we see in our core business.

Now turning to the quarter, we exceeded the high-end of our revenue guidance excluding Blue Nile despite a more than $20 million drag on the top line from the sharp decline of the pound and the Canadian dollar. On the bottom line, we exceeded the high end of guidance even with the impact of Blue Nile, which operated at a loss during the quarter. We delivered profitability during a historically challenging quarter and despite negative high single-digit comp. In the two years prior to the pandemic, we had losses in Q3. We've reset that trend. Our results are a meaningful shift from pre-pandemic levels and reflect the impact of our always on marketing, rigorous cost discipline and even earlier preparation for holiday.

For the quarter, we delivered total sales of $1.6 billion, up 2.9% year-over-year. On a constant currency basis we were up 4.2%. Same-store sales were down 7.6%, which was attributable to consumer behavior shift and macroeconomic pressure. Roughly, half of the comp decline was attributable to lower price points including Banter, which was down roughly 30%.

We saw our strongest performance at higher price points. Our average transaction value in North America was up 8% in Q3, which reflects our mix shift to higher price points as we broadened our reach into Accessible Luxury with more targeted customer acquisitions, tiered-up assortment and price architecture. We also raised prices selectively as needed in response to inflationary pressures by working closely with our vendors to ensure we can deliver the best pricing and value in the industry.

Our fleet reflects our transition to higher price points as well. Sales this quarter were up 33% compared to Q3 of FY 2020 with roughly 450 fewer stores, which translate into a 45% increase in sales per square foot versus the pre-pandemic period. This is the result of a much stronger footprint we've established over the past few years. We have decreased our exposure to C malls by almost 20 points and we've increased all small stores to almost 40% of our fleet.

Turning now to services. North America revenue in Q3 increased roughly 8% on a year-over-year basis and nearly 16% versus FY 2020. This growth was driven by increased awareness of our services offerings and the success of service bundle. As we continue to improve attachments on warranty and repair, we're seeing both the meaningful margin contribution and an increase in return visits. Even better, services margin is over 20% higher than merchandise margin.

Copyright © 2001-2022 FactSet CallStreet, LLC

Non-GAAP gross margin in Q3 was 35.2% of sales down 220 basis points on a year-over-year basis. This reflects the expected impact of Diamonds Direct and Blue Nile, both of which carry a lower relative margin due to their higher bridal mix. Merchandise margin in our organic banners improved versus last year. This is a direct result of our disciplined inventory management, flexible fulfillment capabilities, and a higher-margin services partially offset by the deleverage of store fixed cost.

Non-GAAP SG&A in Q3 was roughly $500 million or 31.4% of sales. Deleverage of 80 basis points compared to last year was 215 basis points better than Q3 FY 2020. This was primarily driven by strategic investments in IT and digital and our flexible operating model enabled us to partially minimize the impact of a negative high-single digit comp on labor and other variable costs under our control.

Non-GAAP operating income was $58 million or 3.7% of sales. We continue to demonstrate the positive impact of the structural changes in our business. Our Q3 non-GAAP operating margin is more than 600 basis points higher than it was during the third quarter of FY 2020 when we had an operating loss of 2.5%.

Now let's turn to the balance sheet. We ended the quarter with approximately $330 million in cash and equivalents on hand. Since the end of Q2, we've returned cash to shareholders, through December 2 of $52 million in share repurchases or nearly 1 million shares along with common dividends of $18 million and we completed the cash purchase of Blue Nile. Further, our leverage ratio on a trailing 12-month basis currently stands at approximately two times EBITDAR, well below our previously stated goals of below 2.75 times and down 50% from Q3 of FY 2020.

Our capital investments are also an important differentiator. As an example, since we began our transformation we have spent more than $300 million in strategic, digital, and technology investments. A significant part of a $700 million of capital that we've invested in total. We have also invested in banner differentiations with a continued expansion of Foundry and the freshness of our fleet. Looking forward we expect capital investments this year of up to $215 million, down from our previous expectations reflecting the impact of external supply chain constraints.

We continue to buy back shares and have $570 million remaining in our authorization as of December 2. This reflects our belief that Signet's stock is significantly undervalued. The resilience of the jewelry industry and the disciplined execution of our strategies give us confidence that the market will soon recognize our unique ability in the jewelry industry to generate consistent shareholder returns.

I'll close with our financial guidance for fiscal 2023 which reflects current business trends and the inclusion of Blue Nile. Black Friday weekend was encouraging and met our expectations with our biggest Cyber Monday in our history. We are seeing shifts in consumer purchasing patterns that indicate many consumers are waiting until later in the season to complete their shopping. We anticipate the strength in our assortment newness will persist. Customers will continue to purchase at higher price points and our holiday readiness will enable us to be there for customers with the products, fulfillment options, and value based facts.

At the same time we know that the economic pressures and concerns will continue to exist. Foreign currency is expected to remain a headwind and our digitally native brands are likely to continue seeing the consumer shift back to the stores through holiday. We're approaching Q4 with a healthy balance of confidence and conservatism, confidence driven by our over-performance in Q3, the inclusion of Blue Nile, our readiness for holiday, and the strength of our operating model, and an appropriate level of conservatism that reflects consumer and macroeconomic variables beyond our control.

Copyright © 2001-2022 FactSet CallStreet, LLC

Keeping this in mind and reflecting current business trends, we are raising fourth quarter revenue guidance in the range of $2.59 billion to $2.66 billion partially offset by the expected headwind related to the sharp decline of the British pound and Canadian dollar. We expect non-GAAP operating income guidance for the quarter in the range of $363 million to $404 million. Our guidance does not include a worsening of macroeconomic factors. Compared to last year, Q4 guidance includes merchandise margin expansion reflecting strength in our assortment architecture and inventory health. In addition, we continue to leverage efficient labor and advertising models along with the flexibility to support further Q4 promotion.

We are raising fiscal 2023 diluted EPS guidance to $11.40 to $12 per share including the Q3 beat and the impact of share repurchases through December 2. Quarter-after-quarter I continue to be inspired not only by our team's dedication to customers, but also by their strong sense of accountability to shareholders. They are both agile and disciplined which shows up time and again in our results no matter the environment we're in.

With that, we're happy to take your questions.

QUESTION AND ANSWER SECTION

Operator: Thank you. We will now begin the question-and-answer session. [Operator Instructions] Our first question today comes from the line of Mauricio Serna with UBS. Please go ahead Mauricio. Your line is open.

Mauricio Serna
Analyst, UBS Securities LLC

Q

Hi. Sorry, can you hear me? I think it got cut off for a second. Hello?

Vincent J. Sinisi
Senioir Vice President-Investor Relations, Signet Jewelers Ltd.

A

Mauricio? Yeah, good morning. We can hear you.

Mauricio Serna
Analyst, UBS Securities LLC

Q

Perfect. Good morning, everyone. Great. Thanks for taking my questions.

Vincent J. Sinisi
Senioir Vice President-Investor Relations, Signet Jewelers Ltd.

A

Good morning.

Mauricio Serna
Analyst, UBS Securities LLC

Q

I guess I wanted to ask if you could provide a little bit more context on how do you get to the fourth quarter sales guidance. Maybe you could break it down. Like, what does that imply for same-store sales growth and then like roughly the contribution from Blue Nile and Diamonds Direct? And also, maybe on the fourth quarter gross margin, I recall last year there was an impact on inventory and inventory adjustment on 4Q 2021, so I just was wondering if you could provide like what was that impact that we should keep in mind for as we model the 4Q gross margin. Thank you.

Copyright © 2001-2022 FactSet CallStreet, LLC

Virginia C. Drosos
Chief Executive Officer & Director, Signet Jewelers Ltd.

A

Hi, Mauricio. Let me give just some big-picture context and then Joan will jump in on some of the more specific details that you just asked about. I think first, let's start with the Q3 beat. It was broad-based. On the top line, we beat both on the core and on our pure-play banner, inclusive of James Allen and Blue Nile. And what I think is important is that this punctuates that Signet is not a COVID story. We're successfully executing on a multiyear turnaround of this company which also led to outperformance on the bottom line in the sense that our core outperformed sufficiently to more than cover the anticipated Blue Nile losses.

On the guidance, we're I think appropriately encouraged by the trends that we saw Black Friday weekends. Our omni traffic was up strong double digits, we saw strong AOV margin in line with expectations. But probably the most encouraging sign was Cyber Monday where we had record visits to our sites low double digits and purchases in the strong single digits, so I think customers are beginning to shop. We think this holiday will come in later than usual. Customers at every income tier are looking for value and so they're waiting a bit later to shop, but it's encouraging to see so much online traffic because we know that we see that first before we see purchases happening online and in store because people in the jewelry category tend to browse first before they buy, so I think that's the positive side.

Obviously, we're still very mindful of the macroeconomic environment that we're in. Customers especially in the value tier are the most challenged, and so our expectations are that we continue to drive purchase at higher price points in the Accessible Luxury tier more so than value.

Joan Holstein Hilson
Chief Financial & Strategy Officer, Signet Jewelers Ltd.

A

And then to respond to the guidance question, Mauricio. Our top line guidance for sales implies a 1 to 2-point change in the comp for our core businesses, and that largely relates to the impact of foreign currency exchange and to Gina's point the impact on the lower price point performance in our business. And then basically, as we think about the gross margin for Q4, remember we had some inventory charges so there's a few puts and takes. We had inventory charges related to one-time accounting adjustments that we're not anniversarying this year as well as the positive impact of our services business as well as other benefits that we're seeing come through related to our inventory and the cleanliness of our inventory in terms of scrap and other inventory-related charges, so really a good margin story.

On top of that, I would say our merchandise margin mix itself is improving and it's really structured around the higher price point assortment, value engineering our product to support our lower value price point customers. And really the overall health of the inventory, the impact of clearance sales is far less negative than it had been in the past. And to Gina's point, over the Black Friday weekend, even while promotions were occurring within our business, we had a margin performance that met our expectations so we're very pleased with the overall view.

Operator: Our next question comes from Lorraine Hutchinson with Bank of America. Please go ahead, Lorraine.

Lorraine Hutchinson
Analyst, BofA Securities, Inc.

Q

Thank you. Good morning. Can you provide some further details on Blue Nile? Maybe what you're projecting for sales over the next several years? And then also, is it loss-making in the fourth quarter? Was that folded into the 4Q operating income guidance?

Copyright © 2001-2022 FactSet CallStreet, LLC

Joan Holstein Hilson
Chief Financial & Strategy Officer, Signet Jewelers Ltd.

A

So, with respect to Blue Nile and the guidance, we folded our view of Blue Nile and t incurred a loss in the third quarter. We folded in its view – our view of that for the fourth quarter which impacted the slight loss and as well as when you think about Blue Nile, we think of it in combination, Lorraine. So, it's a combination of our digitally made banners and as we are addressing synergies, we're seeing greater synergies than we had at the time of acquisition.

We see opportunity at the top line as we reset assortments, integrating our merchandise capabilities. We see opportunity in margin expansion, merch margin expansion as well as the back office synergies through SG&A. So all of that thinking is included within our guidance for the year and as we progress for this year, we'll come back to you on our view for in the later years but we see it all in the positive.

Lorraine Hutchinson
Analyst, BofA Securities, Inc.

Q

Thanks, and then just one follow-up Joan, would you be able to quantify the inventory reserve that you'll be going up against in the fourth quarter this year?

Joan Holstein Hilson
Chief Financial & Strategy Officer, Signet Jewelers Ltd.

A

We haven't quantified that, Lorraine, it was a reasonably large reserve that we don't need to anniversary this year all about given the health of our business and I'll just remind you that we're also – the implied guidance is the negative comp on the top line when you're thinking about this cost leverage.

Operator: Our next question comes from Jim Sanderson with Northcoast Research. Please go ahead, Jim.

James Jon Sanderson
Analyst, Northcoast Research Partners LLC

Q

Good morning, thanks for the question and congratulations on a great quarter. I wanted to dig into the commentary you provided about your long-term outlook, you're talking about engagement and bridal. If bridal is about 40% of your sales mix and you're expecting some softness post-COVID, should we start to look at maybe mid-to-high single-digit sales declines related to that segment in 2023 calendar year? Is that the right way to kind of look at that category?

Virginia C. Drosos
Chief Executive Officer & Director, Signet Jewelers Ltd.

A

Yeah, I think what I was trying to provide was some perspective on the stability actually of bridal over time. It's a very consistent part of the jewelry business, I mean year in, year out you'll have engagements, weddings, anniversaries, and if you look back pre-COVID it was very, very steady. So about 2% growth of engagements and weddings year-in, year out.

COVID has caused a bit of a blip in the sense that last year we saw an uptick in engagements. This current year that we're in, we've seen a downtick in engagements but it's the peak ever or a peak in the last four years anyway of weddings. So, we shifted, we saw that coming and we've shifted and we've really been working to own the wedding.

Copyright © 2001-2022 FactSet CallStreet, LLC

So, two wedding band purchases, earrings for the bridesmaids, watch for the groom, gifts for the mother of the bride, that kind of thing as an offset to the slight downtick that we see in engagements. Next year we expect to see a slight downtick again in engagements, but then it normalizes, it all actually grows to get back to normal the year after and we think normalizes ongoing after that. So it's really the first meaningful, I would call it a temporary blip that we have seen in how engagement and weddings have been working, but the great news is that with our consumer insight work we've predicted that and came around that, so that we're really working on lifetime value.

Our loyalty program and I gave a lot of stats in the call has been a fantastic addition in that context, because we're seeing most people come into the loyalty business through engagement. We're contacting previous engagement customers to bring them into the loyalty programs and then we're working lifetime value with them. So I think the fact is that there will be less engagements next year, Signet would expect to grow share within the engagement category and we expect also to grow our fashion and gifting business as we surround the wedding.

James Jon Sanderson
Analyst, Northcoast Research Partners LLC

Q

Okay, so a little bit of offset to maybe some slight tick down in the segment related to just the timing of the impact of COVID, is that the message I want to take away?

Virginia C. Drosos
Chief Executive Officer & Director, Signet Jewelers Ltd.

A

Yeah, it is really just a demographic fact but what we do is leverage all the different aspects of our business to understand those and then offset that as we put together our business plans for the year ahead.

James Jon Sanderson
Analyst, Northcoast Research Partners LLC

Q

Understood, thank you.

Operator: The next question today comes from Will Gaertner with Wells Fargo. Please go ahead well.

Will Gaertner
Analyst, Wells Fargo Securities LLC

Q

Hey, guys, thanks for taking my question.

Vincent J. Sinisi
Senioir Vice President-Investor Relations, Signet Jewelers Ltd.

A

Good morning.

Will Gaertner
Analyst, Wells Fargo Securities LLC

Q

Look, I understand you're not to be guiding here but maybe can you just give us some color on the puts and takes as gross margin, operating margin into next year, how to think about Blue Nile and Diamonds Direct, how their impact on the business from a gross margin and then operating margin perspective?

Virginia C. Drosos
Chief Executive Officer & Director, Signet Jewelers Ltd.

A

Copyright © 2001-2022 FactSet CallStreet, LLC

So, Blue Nile carries a profile similar to Diamonds Direct and James Allen because it's largely – it's predominantly in the bridal business which carries a relative lower margin, Will. So as you think about Blue Nile and its merchandise contact that will affect its merchandise margin rate. When we think about integrating that with James Allen, we believe that we can continue to expand the operating margin as we influence the assortment architecture of Blue Nile.

So the other point that I really make is that as we continue to grow our services business which kind of attached to all of our businesses, all of our banners that also carries a higher gross margin profile I mentioned in my prepared remarks that is 20% higher than other merchandise margin categories. So that's a positive. The other – we have sourcing opportunities that we continue to explore in the call, we – gives us room to be positioned to be flexible with our promotional strategy into Q4 and as well as into the next year. So, that's really the gross margin story.

As we think about Blue Nile go forward we said in the past that it would be accretive as early as Q3 of next year and as we look at it, we're really viewing it as a combined banner with James Allen. So if you look in our 10-Q, you'll see digitally native banners. What we're really presenting to you is that this is a combined entity that really drives and two partial banners that play off to each other attracting different customers with Blue Nile being slightly higher and slightly younger and more affluent which really opens up the top of the funnel, but brings with it a different margin profile.

So, overall, really positive about Blue Nile, its impact on our business, our ability to manage its performance within the guidance that we've provided for this year. And as I said earlier, we will come back to you on our fourth quarter call with respect to looking into next year.

Operator: [Operator Instructions] Our next question comes from Paul Lejuez with Citi. Paul, your line is open.

Paul Lejuez
Analyst, Citigroup Global Markets, Inc.

Q

Hey, thanks, two questions, one I think you mentioned encouraging results of a Black Friday weekend that met expectations but you also said that you're seeing signs that the consumer was waiting for later in the season to complete their shopping. So, just kind of curious how to square those two things and then curious if you could talk a little about a bit more about transition versus ticket, in which categories you're seeing higher AURs versus where you might be seeing some pressure, thanks.

Virginia C. Drosos
Chief Executive Officer & Director, Signet Jewelers Ltd.

A

Sure, so I'll take the Black Friday and later in the season. So, both of those things are true. We saw encouraging results of a Black Friday. As I mentioned, we saw omni-traffic up double digits. So, a lot of people in stores, but a lot of people online, and we saw our online revenue up mid-single digits. So, that was great that we see people buying at the time, but a lot of people we see browsing.

And they'll be waiting we think until later in the season making sure they get the very best value that they can. We're well-positioned for that. We're positioned with I think very strong merchandise offers, great newness, non-comps in digital, experience, marketing, all of those things to drive closure of those customers. But the beginning of our holiday season, especially with our highest ever Cyber Monday was encouraging.

Copyright © 2001-2022 FactSet CallStreet, LLC

Joan Holstein Hilson

Chief Financial & Strategy Officer, Signet Jewelers Ltd.

A

And as we think about the sales equation Paul, it's – our conversions were relatively flattish. We mentioned we have a higher average transaction value but on a lower traffic our transactions were down.

Operator: That's all the questions we have time for today. So, I'll now turn the call back to management for any concluding remarks.

Virginia C. Drosos

Chief Executive Officer & Director, Signet Jewelers Ltd.

Well, thanks everyone. The point that I want to ensure that Joan and I have made this morning is that Signet is uniquely positioned to deliver consistent market share growth and value creations given our strong and growing leadership in jewelry, an attractive industry that tends to grow steadily from year-to-year and is more resilient to economic cycles than other retail industries.

We've established our leadership position by strategically creating a virtuous flywheel effect that is building positive momentum and growth that no other company in our industry is achieving. We're raising the year, integrating Blue Nile ahead of plan, continuing to deliver annual double-digit operating margins, and maintaining the flexibility that comes with a strong healthy balance sheet. We're ready for holiday and confident we can deliver the long-term growth to which we're committed. Thank you very much and happy holidays.

Operator: Thank you everyone for joining us today. This concludes our call and you may now disconnect your lines.

Disclaimer
The information herein is based on sources we believe to be reliable but is not guaranteed by us and does not purport to be a complete or error-free statement or summary of the available data. As such, we do not warrant, endorse or guarantee the completeness, accuracy, integrity, or timeliness of the information. You must evaluate, and bear all risks associated with, the use of any information provided hereunder, including any reliance on the accuracy, completeness, safety or usefulness of such information. This information is not intended to be used as the primary basis of investment decisions. It should not be construed as advice designed to meet the particular investment needs of any investor. This report is published solely for information purposes, and is not to be construed as financial or other advice or as an offer to sell or the solicitation of an offer to buy any security in any state where such an offer or solicitation would be illegal. Any information expressed herein on this date is subject to change without notice. Any opinions or assertions contained in this information do not represent the opinions or beliefs of FactSet CallStreet, LLC. FactSet CallStreet, LLC, or one or more of its employees, including the writer of this report, may have a position in any of the securities discussed herein.

THE INFORMATION PROVIDED TO YOU HEREUNDER IS PROVIDED "AS IS," AND TO THE MAXIMUM EXTENT PERMITTED BY APPLICABLE LAW, FactSet CallStreet, LLC AND ITS LICENSORS, BUSINESS ASSOCIATES AND SUPPLIERS DISCLAIM ALL WARRANTIES WITH RESPECT TO THE SAME, EXPRESS, IMPLIED AND STATUTORY, INCLUDING WITHOUT LIMITATION ANY IMPLIED WARRANTIES OF MERCHANTABILITY, FITNESS FOR A PARTICULAR PURPOSE, ACCURACY, COMPLETENESS, AND NON-INFRINGEMENT. TO THE MAXIMUM EXTENT PERMITTED BY APPLICABLE LAW, NEITHER FACTSET CALLSTREET, LLC NOR ITS OFFICERS, MEMBERS, DIRECTORS, PARTNERS, AFFILIATES, BUSINESS ASSOCIATES, LICENSORS OR SUPPLIERS WILL BE LIABLE FOR ANY INDIRECT, INCIDENTAL, SPECIAL, CONSEQUENTIAL OR PUNITIVE DAMAGES, INCLUDING WITHOUT LIMITATION DAMAGES FOR LOST PROFITS OR REVENUES, GOODWILL, WORK STOPPAGE, SECURITY BREACHES, VIRUSES, COMPUTER FAILURE OR MALFUNCTION, USE, DATA OR OTHER INTANGIBLE LOSSES OR COMMERCIAL DAMAGES, EVEN IF ANY OF SUCH PARTIES IS ADVISED OF THE POSSIBILITY OF SUCH LOSSES, ARISING UNDER OR IN CONNECTION WITH THE INFORMATION PROVIDED HEREIN OR ANY OTHER SUBJECT MATTER HEREOF.

The contents and appearance of this report are Copyrighted FactSet CallStreet, LLC 2022 CallStreet and FactSet CallStreet, LLC are trademarks and service marks of FactSet CallStreet, LLC. All other trademarks mentioned are trademarks of their respective companies. All rights reserved.