

# DLTH Earnings Call Transcript

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**Quarter: 2**

Operator: Good day, and welcome to the Duluth Holdings Inc. Second Quarter 2025 Conference Call. All participants will be in a listen-only mode. After today's presentation, there will be an opportunity to ask questions. Please note this event is being recorded. I would now like to turn the conference over to Mr. Chris Steffes with Duluth Investor Relations. Please go ahead, sir.

Chris Steffes: Thank you, and welcome to today's call to discuss Duluth Trading's second quarter financial results. Our earnings release, which was issued this morning, is available on our Investor Relations website at [ir.duluthtrading.com](http://ir.duluthtrading.com) under News Releases. I'm here today with Stephanie L. Pugliese, President and Chief Executive Officer, and Heena K. Agrawal, Senior Vice President and Chief Financial Officer. On today's call, management will provide prepared remarks and then open the call for questions. Before we begin, I would like to remind you that the comments on today's call will include forward-looking statements, which can be identified by the use of words such as estimate, anticipate, expect, and similar phrases. Forward-looking statements by their nature involve estimates, projections, goals, forecasts, and assumptions and are subject to risks and uncertainties that could cause actual results or outcomes to differ materially from those expressed in the forward-looking statements. Such risks and uncertainties include, but are not limited to, those that are described in our most recent annual report on Form 10-Ks and other SEC filings as applicable. These forward-looking statements speak only as of the date of this conference call and should not be relied upon as predictions of future events. And with that, I will turn the call over to Stephanie.

Stephanie L. Pugliese: Good morning, everyone, and thank you for joining us today. We are encouraged by our second quarter results demonstrating positive momentum in our initial turnaround efforts. Our team has worked tirelessly and made improvements across several critical areas of the business. This includes promotional reset, cost control, tariff mitigation, and a disciplined approach to inventory management. Our strategic and operational efforts have begun to yield tangible benefits, leading to an enhanced gross margin, reduced expenses, and lower inventory levels, which played out in our Q2 results. As we reduced the depth of promotional activity, we anticipated that our top-line revenue would contract year over year. Yet despite a sales decline of 7% versus last year, we delivered gross margin improvement and SG&A leverage, which drove a \$1.5 million increase in adjusted EBITDA, reaching \$12 million or 9% of sales. We concluded the quarter with a strong liquidity of \$73 million reduction in inventory compared to last year, meeting our expectations of sequential inventory improvement each quarter. Let me elaborate further on each of the areas of improvement. Starting with an update on the resetting of our promotional cadence, we have reduced the depth of our promotions to strategically elevate full-price sales, increase our average unit retails, and drive improved profitability. We are intentionally shifting our focus towards higher quality sales. At the same time, we know that we are operating in a dynamic environment. We will continue to test, read, and react to pricing initiatives throughout the second half of the year to meet customers' needs and manage higher profitability. As mentioned last quarter, we also quickly began to right-size the cost structure and alleviate pressure from tariffs. I am pleased to report that we are on track to realize \$10 million in cost savings in fiscal 2025. While structure, we have also continued to invest time and energy to improve processes that optimize productivity now and in the future. Our ongoing commitment to inventory management and enterprise planning has led to enhancements in our operational and planning processes. This

end-to-end cross-functional initiative has resulted in the 12% reduction in Q2 ending inventory that I mentioned earlier, primarily due to our emphasis on rightsizing inventory receipts. We expect that these efforts combined with SKU and style count reductions in future seasons will lead to better use of cash, stronger inventory turns, and improved margins. Now let me provide an update on our approach to mitigating tariffs, focusing on short-term actions that do not compromise the long-term integrity of our products. In addition to working closely with our manufacturing base and finding areas of SG&A; to offset margin impact, in fall 2025, we have selected targeted products for retail increases. We did this while recognizing the need for a balance of styles that are lower priced and continue to be a great value for our customers, all with our uncompromising eye on maintaining quality. And while we are reducing deeper discounted promotions, we have implemented buy more and save discounts on some of our key programs like underwear and long tail tees. We believe that this will maintain our quality standards, help to offset the increase in cost of goods, and still allow our customers to realize the value that we offer. Now let's move on to our performance in the second quarter starting with some of our product highlights. Duluth men's bottoms drove higher profitability as we pulled back on promotional depth delivering more than a 10% increase in AUR. As we continue to expand the offering in men's tops, new items like the barbecue shirt in standard fit, Breeze Shooter untucked, and Drummond Slub Cotton shirts resonated with our customers. Our Mother's Day print collection in women's was our most successful print launch ever with our heirloom bibs complemented by matching garden accessories. New product lines such as Artisan Hemp, a durable yet breathable hemp and organic cotton blend, and Featherlite Chick Knit shirts were well received and speak to the commitment we have to comfort, durability, and functionality in all that we do. And lastly, AKHG grew by more than 10% in both men's and women's driven by better in-stock position in key items like stonerun pants. We also saw positive responses to new Wonderwear performance shorts, Tundra, and the After Sweat collection. Now turning to our marketing efforts for the quarter, we saw success with a full funnel approach highlighted by our Q2 Father's Day campaign. We focused on both awareness and consideration with this campaign and our Good Morning America Gifts for Dads feature drove better awareness than our similar spot during last year's peak season. Finally, this quarter, we launched the Big Damn Van, a mobile retail experience enabling Duluth to be more visible at events throughout the country, including store openings. Moving on to our retail portfolio, our store sales grew 5% year on year. This success was driven by improved traffic trends combined with increased conversion rates and higher average order values. Store marketing efforts were successful in generating awareness and driving traffic through tactics like geo-targeted ads and connected TV. We closed one underperforming store this quarter and have renewed leases on two stores that are meeting our higher profit hurdle rates. Further, we are excited to open our first new store since 2021 in Kansas City, Kansas, and Maple Grove, Minnesota. These are priority markets for us and we are thrilled to see these stores come to life and join our improving retail portfolio in the coming weeks. And speaking of fall, we have begun the process of tightening our assortment and have reduced our SKU count compared to the prior year with a more focused collection. Our business is built on a foundation of core products, strengthened by innovative new solutions designed to solve customers' problems. We are revitalizing our product and marketing strategies to reflect the true essence of our brand. For example, this month, we are relaunching core men's and women's denim that is built for greater durability and comfort along with adding new products like the Seawool collection, which is naturally thermo-regulating, wicks away moisture, and controls odor. These products provide the kind of functional apparel our customers depend on as the seasons change. We know that the second half of the year is our most important for customer engagement, revenues, and profitability. As we lead up to our peak season, our focus remains on continuing the turnaround efforts and leading with a sense of urgency. Through rigorous preparation and alignment of all functions in the business, including marketing and promotional productivity, inventory positioning, and customer communication, our goal is to not only meet but exceed our customers' expectations during this critical period. In closing, we are pleased with our Q2 performance and the progress we have made so far on the first phase of our turnaround efforts and I am committed to building on this momentum. In the near term, our focus remains on simplifying the business, managing costs, mitigating the ongoing impacts of tariffs, and most importantly delivering on our promise to customers with excellence. Looking ahead, we acknowledge the significant work that is to

come in the second half of this year and in our turnaround plan. We will continue to leverage our foundational work in product sourcing, optimizing our fulfillment center network, and rationalizing our store portfolio. In addition, we are refocusing our marketing efforts and product assortment to celebrate the self-reliant spirit of our customers. Moving on to 2026, we are reducing our SKUs and refining our assortment. This focused approach will enable us to emphasize the core products that distinguish the Duluth brand. I am confident that in the long term focusing on Duluth Trading's core strengths, customer engagement with our brand, solution-based products, and product innovation and excellent customer service in our omnichannel environment will create shareholder value and ultimately restore the company to profitable growth and success. Now I'll hand it over to Hina to discuss our financial results for the second quarter and our outlook for fiscal year 2025.

Heena K. Agrawal: Thanks, Stephanie, and good morning. Echoing Stephanie's comments, we are pleased with our Q2 results, which represent an important step forward in our turnaround efforts. As stated on our last two calls, our primary focus this year is to reset our promotional cadence to restore price integrity, improve inventory management, and strengthen operational execution. In April, as new tariffs were announced, we responded proactively with mitigation actions. In addition, we initiated cost reduction efforts and implemented steps to manage cash flow and liquidity during this period of macroeconomic uncertainty. I am proud of the team's unwavering commitment to the goals we established at the start of this year and their agility in developing solutions to mitigate macro headwinds. Now to provide an update on our second quarter results and progress in these areas. Today, we reported second quarter 2025 net sales of \$131.7 million, down 7% with gross margin expansion of 240 basis points versus last year to 54.7% and SG&A; leverage driven by cost reductions. Our reported EPS is \$0.04 and adjusted EPS is \$0.03 favorable to last year by \$0.05. Adjustments to EPS include restructuring charges of \$700,000 net of tax and tax valuation allowance of negative \$900,000. Adjusted EBITDA for the quarter increased by \$1.5 million versus last year to \$12 million or 9.1% of sales. Starting with the top line, as we reset our promotional depth to drive greater profitability, our Q2 net sales declined 7% versus last year and declined 9.8%, excluding the wholesale shipment shift from Q1 to Q2 this year. Direct channel sales, excluding wholesale, saw an 18% decrease, primarily due to a decline in web traffic resulting from the promotional reset, partially offset by a higher average order value. Mobile sales penetration continued to improve, increasing by 100 basis points. Retail store sales increased 5.3%, driven by improved traffic trends from targeted marketing efforts, increased conversion rates, and an optimized inventory allocation strategy leading to improved in-stock levels. In addition, store profitability improved as we reduced promotional depth, driving higher average unit retail and average order values. Duluth men's sales declined by 8% and women's declined by 11.3% as we reset promotions, while AKHG grew by 11.4% with double-digit growth across both men's and women's driven by improved inventory availability. Effective inventory management led to improved in-stock rates and profitability improved across channels and businesses with shallower promotions. Gross profit margin rate for the quarter was 54.7%, expanding by 240 basis points compared to last year, driven by an 8% increase in average unit retail and a greater proportion of full-price sales as we reset promotions. Gross margin continues to improve due to two factors: a rebalancing of promotions to restore price integrity by reducing the depth of discounts and the flow through of lower product costs resulting from our direct-to-factory sourcing initiative. The impact of tariffs on Q2 margin was negligible and will be felt more strongly in the second half of the year. To offset the impact of tariff costs, we began implementing our targeted price increases at the July in addition to vendor negotiations and inventory receipt management. SG&A; spend was \$68.8 million, which is \$5.2 million or 7.1% lower than last year. SG&A; as a percentage of sales improved by 10 basis points to 52.2% compared to last year. Advertising came in at 8.9% of sales, deleveraging by 60 basis points. The improved SG&A; leverage was driven by reduced outbound shipping costs and lower fixed overhead expenses, including personnel and depreciation. As Stephanie mentioned, we are on track to deliver \$10 million in cost reductions this year as we rightsize our expense structure. Inventory at the end of the quarter was \$148.1 million, a decrease of \$20.7 million or 12% compared to the prior year. In addition, store in-stock levels increased by 200 basis points year over year. These improvements were driven by enhanced processes like enterprise planning, which optimized inventory receipts and inventory positioning to drive greater availability. We have made progress in managing receipts with year-round inventory

levels currently 6% lower than last year, a healthy level to support appropriate depth in our core products. As Stephanie mentioned, we have also reduced SKUs and inventory levels for the upcoming fall/winter season. At the end of the quarter, our inventory mix included 78% in current products and 22% in clearance goods compared to 11% in clearance last year, primarily due to slower than expected sell-throughs of our spring/summer merchandise. To address this, we activated the Big Dan clearance event, reducing our clearance inventory to 16% of the total as of the September. For spring/summer 2026, we've adopted a more sustainable approach, reducing our SKU count by over 20%, creating a more focused and relevant assortment to ultimately drive higher sell-throughs. Our capital expenditures for the first half were \$9.7 million compared to \$8 million in the prior year, with the increase in spend primarily driven by our two new stores set to open this month. We ended the quarter with net liquidity of \$73.3 million and net debt of \$26.7 million. Our cash and cash equivalents were \$5.7 million with borrowing on our credit facility at \$32.5 million. As we actively managed our inventory levels, we cut our borrowing in half versus prior quarter. As communicated last quarter, we anticipate that our peak borrowings for the year are behind us. Now turning to our outlook for fiscal year 2025. We are maintaining our fiscal year 2025 financial guidance. The adjusted EBITDA range of \$20 million to \$25 million considers several factors. First, mitigating the impact of tariffs with price action, vendor negotiations, and management of the timing of inventory receipts next, reducing expenses to protect against top-line headwinds from dialing back discount levels and to align our overall expense structure with the current scale of our business. Lastly, further integrating our planning processes and financial discipline to drive a higher return on our investments in inventory and assets like the fulfillment center network and store portfolio. Further elaborating on tariffs, we now anticipate an impact to the current year of approximately \$15 million based on the last announced rates by country. The average tariff rate based on country of origin and timing of receipts is approximately 12% this fiscal. The impact of tariff costs in the first half of the year was negligible and will primarily hit the second half. We have offset the majority of these additional costs by strategically increasing prices in select categories. These price increases implemented in late July and early August are currently meeting sales expectations in terms of elasticity. In addition, we have partnered with our vendors to share in the cost impact and continue to actively manage the timing of inventory receipts. Speaking of SG&A, we've implemented over \$10 million in cost reductions this year, while maintaining our investment in marketing as a percent of sales. We are strategically optimizing our organizational expenses in line with the current size of our business, effectively managing the revenue impact of our pricing and promotional adjustments, mitigating tariff impacts, and balancing the short and long-term needs of the business. Regarding our balance sheet and capital expenditures. First, we continue to project inventory levels to normalize in the second half of the year due to a rebalancing of sales and inventory receipts. We expect year-end inventory to decrease by double digits compared to the prior year. This reduction and rightsizing of receipts ensures that we are past our peak borrowing levels. Second, we are maintaining our capital expenditure plan at approximately \$17 million for the year. This includes funding for the two new stores opening this month along with Manhattan Omni fulfillment software and regular maintenance. Finally, our asset-based lending facility continues to enable higher flexibility in maintaining liquidity and access to cash. To summarize, we are encouraged by the strides we are making in restoring price integrity, improving inventory management, and strengthening operational execution. These initiatives will allow us to fully leverage the benefits of our strategic and structural initiatives over time. We are taking holistic actions to counteract the impact of tariffs, making decisive moves to optimize our expense structure and under Stephanie's leadership, focusing on our product assortment and brand marketing investments. With that, we will now open the call for questions.

Operator: Thank you. And the first question will come from Jonathan Komp with Baird. Please go ahead.

Jonathan Komp: Yeah. Hi. Good morning. Thank you. Stephanie, I want to follow-up. If you could maybe share more on some of the specific metrics that you're looking at, and the team is looking at as you decide the appropriate level of pullback in your promotional activity. And then as you look forward into the key selling periods in fall and surrounding holiday, just any thoughts on your confidence level of being able to maintain more discipline on the promotional side given some of the results you saw here in the quarter?

Stephanie L. Pugliese: Sure. So let me start with the question around the key metrics that we're looking at. Gross margin dollars are the primary measure that we are looking at because we know Jonathan that obviously that drives all of the dollars then below that line on the P&L.; Through the discipline that we've been able to very quickly enact in the business around SG&A; leverage, it's given us the ability to continue what we started in the first quarter around the promotional pullback knowing that there will be a contraction of sales. But ultimately the profitability is our first and foremost objective for this year to get us to that the EBITDA that we just reinforced on the bottom line for the year. In terms of as we look forward and the confidence that we have in the fourth quarter, as we said in the first quarter actually and reiterated today, we are seeing success in the pullback of the depth of promotion. We are still in terms of the frequency of promotion, we're still pretty consistent to where we've been in the past. So the ultimate gross margin dollars that we're generating are due to the pullback in-depth. And that's the plan that we have as we go forward for the balance of this quarter and then into the fourth quarter. And the fact that we've seen the success so far this year in the first two quarters is what gives us a lot of confidence there.

Jonathan Komp: Yes. That's encouraging to hear. Maybe a question then on gross margin. Just given some of the dynamics with the tariff impacts ramping up, but obviously some benefits from the activity you just mentioned and then the pricing that you're putting into place. Just any further color on the ability to continue the gross margin rate expansion and especially the fourth quarter? I know looks like quite an easy comparison, but just any more color on the back half gross margin rate expectation?

Heena K. Agrawal: Yes, Jonathan, this is Heena. I'll take that question. So we implemented price increases in two ways starting July 25 and August 8. And what we are seeing so far is, it is meeting our sales expectations from a price and unit elasticity standpoint. So we are going to continue to mitigate the impact of tariffs on the from our pricing activities. We've also had vendor negotiations to fulfill some of the cost increases, and then we are managing the timing of our receipts. In addition to that, the SG&A; cost reductions are definitely helping from an overall P&L; standpoint. So we feel very good about the second half and our ability to meet our gross margin requirements. There will be some differentiation between Q3 and Q4. We'll see a bigger ramp up in Q4 versus in Q3 where these tariff impacts are just beginning to take hold.

Jonathan Komp: Okay, great. Two other questions for me. Just on the SG&A;, the cost savings that you're targeting, the \$10 million to be achieved in fiscal 2025, any further color just how much you achieved in the second quarter and how the savings will ramp here looking forward?

Heena K. Agrawal: Yes. I mean, what we can say is the \$10 million is primarily coming from two areas. One is headcount that we had announced on June 4, and then the other is controllable expenses like consulting, travel, and also some depreciation and amortization. So we started seeing the benefits of that in Q2. I would say we are about a third of the way there already. So we feel very good about the \$10 million for the rest of the year for the entire year.

Jonathan Komp: Okay. And then last question for me. Just stepping back bigger picture, as you think about reestablishing appropriate margin targets for the business, just I'm curious what you'd need to see in order to be able to share more detail on an appropriate levels of margin for the business or longer-term expectations around the profitable sales base you need to get back to more reasonable annual profitability levels?

Stephanie L. Pugliese: So, I'll take that one Jonathan. I think the primary thing for the balance of this year is the two things really are the manageable expenses as Heena just talked about a moment ago and the resetting of price integrity. And part of that resetting of price integrity is certainly the promotional cadence that we just talked about. But the other part is the inventory management. And within inventory management, SKU and style productivity. So the balance of this year as we know, we are still in the process of rightsizing that inventory. As we move forward into 2026, as we talked about in the last quarter's call, we are planning and actually executing to a 20% decrease in SKU and style count. So as we get to that point where our assortment is rationalized, our expense plan if you will is rationalized that's where we will have the ability to really create a strong margin profile for the business. So, at this point our focus is executing really well the balance of the year both in all of the things we just talked about around the margin profile and also obviously operationally, and for our customers. And then as

we move forward to 2026 that's where we start to really start implementing those key KPIs around SKU productivity, around promotional cadence, and around inventory management that will lead to a stronger margin profile long term.

Jonathan Komp: Okay, great. That's very clear. Thanks again for taking all the questions.

Stephanie L. Pugliese: Sure. Absolutely. Thanks.

Operator: This will conclude our question and answer session as well as our conference call for today. Thank you for your participation. You may now disconnect.