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VF Corp. (VFC)

Q1 2023 Earnings Call

CORPORATE PARTICIPANTS

Allegra Perry

Vice President-Investor Relations, VF Corp.

Matt Puckett

Chief Financial Officer & Executive Vice President, VF Corp.

Steven E. Rendle

Chairman, President and Chief Executive Officer, VF Corp.

OTHER PARTICIPANTS

Laurent Vasilescu

Analyst, BNP Paribas Exane

Michael Binetti

Analyst, Credit Suisse Securities (USA) LLC

Mackenzie Boydston

Analyst, BTIG LLC

Brooke Roach

Analyst, Goldman Sachs & Co. LLC

Matthew R. Boss

Analyst, JPMorgan Securities LLC

Ike Boruchow

Analyst, Wells Fargo Securities LLC

Robert Drbul

Analyst, Guggenheim Securities LLC

MANAGEMENT DISCUSSION SECTION

Operator: Greetings. Welcome to the VF Corporation First Quarter Fiscal 2023 Conference Call. At this time, all participants are in a listen-only mode. A question-and-answer session will follow the formal presentation. [Operator Instructions] Please note, this conference is being recorded.

I will now turn the conference over to your host, Allegra Perry, Vice President of Investor Relations. Thank you. You may begin.

Allegra Perry

Vice President-Investor Relations, VF Corp.

Good afternoon, and welcome to VF Corporation's first quarter fiscal 2023 conference call. Participants on today's call will make forward-looking statements. These statements are based on current expectations and are subject to uncertainties that could cause actual results to differ materially. These uncertainties are detailed in documents filed regularly with the SEC.

Unless otherwise noted, amounts referred to on today's call will be on an adjusted constant dollar basis, which we've defined in the press release that was issued this afternoon and which we use as lead numbers in our discussion because we believe they more accurately represent the true operational performance and underlying results of our business.

You may also hear us refer to reported amounts, which are in accordance with US GAAP. Reconciliations of GAAP measures to adjusted amounts can be found in the supplemental financial tables included in the press

release, which identify and quantify all excluded items and provide management's view of why this information is useful to investors.

On June 28, 2021, the company completed the sale of its Occupational Workwear business. Accordingly, the company has reported the operating results and cash flows of this business in discontinued operations for all periods through the date of the sale. Unless otherwise noted, results on today's call are based on continuing operations.

Joining me on the call will be VF's Chairman, President and Chief Executive Officer, Steve Rendle; and EVP and Chief Financial Officer, Matt Puckett. This quarter's earnings presentation has been designed as a visual aid to our prepared remarks. You have the option to follow along via the slide window in the webcast portal. The presentation is also available to download on our website.

Following our prepared remarks, we'll open the call for questions. I'll now hand over to Steve.

Steven E. Rendle

Chairman, President and Chief Executive Officer, VF Corp.

Good afternoon, everyone, and thank you for joining our first quarter fiscal 2023 earnings call. I'll take you through an operational update of our business, which will be followed by a review of our financial performance by our CFO, Matt Puckett.

I want to start by addressing the evolution of the macro environment since we last met in mid-May. Excluding China, consumer health is generally good across our markets, although I won't be the first person to point out that sentiment has softened, leading to changing behavior amongst consumers, who are being forced to be more choiceful and cautious in their spending in the near term.

From our point of view, we see this being largely confined to the value end of the marketplace, where VF has very little exposure. To date, we've seen limited impact on the mid- to higher-end consumer, where the majority of our brands are positioned in terms of demographic and distribution. We have a strong and resilient family of brands that are well positioned within their respective segments. And across the VF portfolio, we have a greater number of high-performing brands today than ever before.

Our TAMs are healthy and maintain good momentum, and we remain underpenetrated in certain areas, with the opportunity to gain further share in growing markets. We are continuing to invest in our brands, enabling the creation of innovative products and capabilities to drive enhanced consumer engagement and loyalty across all touch points. We're working closely with our retail partners to drive sell-through and ensure our family of brands remains at the forefront of consumers' minds.

Through our well-established strategic platforms and capabilities, we are mitigating headwinds faced across the marketplace and the persistent impact of COVID in China while reinforcing our competitive advantages. Amidst this backdrop, we delivered a healthy top line performance in Q1, achieving revenue of \$2.3 billion, up 7% on a constant dollar basis, ahead of our initial expectations.

And in fact, excluding China, the business grew low double-digits. Our Big 4 brands grew 6% in aggregate, led by The North Face and Timberland. The remainder of the portfolio grew 16%. And lastly, before I go into more details on the brands, I'd like to highlight that we remain committed to returning cash to shareholders with our dividend, which amounted to \$194 million in the quarter.

I'll start with Vans. I'd like to take a minute to update you on the work underway, then go into the details of the brand's performance. Behind the scenes, our teams are diligently working to address the key headwinds we've identified. First, on China, which was largely in line with our cautious expectations, reflecting macro challenges and COVID disruption. Driving energy and engagement, Vans opened its first owned Taiwan store in June, along with a brand mobile app.

We launched a new collaboration with Brain Dead, which sold out completely in the first hour. Our 618 shopping event was expanded onto the [ph] Douyin and Douluo (5:20) platforms and rose by mid-single digits versus last year. Finally, we partnered with Tencent on 58 virtual products for Phase 1 of our Metaverse activation and in four days, achieved 43 million impressions. We remain confident of the long-term growth opportunity Vans has in China.

Second, we're seeing early signs of positive response from customers on our ongoing efforts to rebuild our core Classic strategy and energy around our 5 icons. The Classic Since Forever campaign is showing improved ROI in the first two months with over 25 million views globally. Phase 2 of the campaign launched with support from Anderson Paak, Vans' music influencer including live appearances in London stores and a live performance at our House of Vans venue. The first signature product drops on our US online platform sold out in 24 hours.

Brand heat has begun to show some bright spots. We saw nearly 8% growth in Vans family members versus Q4, reaching nearly 24 million members globally, which represents a 41% increase versus last year. We also generated strong sell-through of Sailor Moon and Stranger Things collaborations, including exclusive online customs pre-releases.

Our Stranger Things collaboration was the second biggest customs launch since Harry Potter, and the in-line product will launch in early September. We hosted prelaunch events for our new Pinnacle business unit at Paris Fashion Week with top-tier accounts, including a sell-in event and a Twitch live stream of the Brain Dead launch. The Joe Freshgoods Pinnacle collabs sold through quickly with three times average sales price in resale market. The second drop is coming in holiday.

Finally, in our Americas DTC business, we're working through a set of agile actions to capture and optimize traffic and drive higher conversion, such as front-of-store merchandising updates and quick floor set changes. We're seeing a positive initial response across key product styles. We continue to monitor our customer satisfaction levels where we are scoring above the peer set.

Vans Q1 sales declined by 4%. Excluding China, global sales were up 4%. As mentioned, a number of targeted actions are being implemented at Vans under the leadership of Kevin Bailey. While our financial performance is not yet where we'd like it to be, we are encouraged by the work underway to reignite momentum. The brand is healthy, which is clearly evident when we launch truly innovative product as indicated with the recent global collaborations, all of which resonated with our consumers and generated high rates of sell-through.

We continue to see strong growth in our Vans Family membership where members have higher frequency and rates of spend. Overall, we're encouraged with the early progress being made with actions underway and confident in the brand's long-term prospects to reignite growth.

The North Face had another outstanding quarter, with sales up 37%, representing broad-based growth across regions and channels. Growth during the quarter was fueled by our 365 product initiatives with warm weather apparel and accessories as well as rainwear generating strong performances.

Collaborations continue to drive brand heat, including the members only Earth Day inspired collaboration, which drove high digital sell-throughs in the US and EMEA. Our return-to-travel lines also performed well, including bags and luggage, and we saw early positive performance for our Packs business for back-to-school. Our marketing campaigns are clearly resonating with our consumers.

Starting with our Full Circle Everest Expedition, which promoted access to the outdoors with over 5 billion impressions. Our Pride campaign was well received and allowed us to broaden our reach and welcome new consumers to the brand. And The North Face ranked number one in presale revenue for the outdoor category during the all-important 618 China shopping holiday.

We continue to see growth in our XPLR PASS loyalty program as we celebrated its one-year anniversary with over 900,000 sign-ups translating to 50% growth year-over-year.

Finally, we are thrilled to have welcome Nicole Otto as our new brand President during the quarter, following a successful transition period. She brings with her a deep understanding of the consumer engagement strategies and a wealth of industry experience. As a proven innovator and future-focused leader, she steps in at an opportune time with strong product pipelines positioning the team to further drive our strategies.

The positive inflection at Timberland continued in Q1 with another quarter of double-digit sales growth, up 14%, driven by strong performances in EMEA and Asia Pacific. We're sharpening our consumer focus and accelerating a launch culture to attract new consumers to the Timberland brand and is paying off as we see success stories from the elevation of our iconic boat shoes globally with Generation Boat to the creation of a footwear design and innovation experience inside Fortnite.

Our commitment to product innovation and craftsmanship continues to serve us well. Our Q1 growth was driven by men's footwear, led by outdoor across lifestyle hike, trekkers and seasonal executions like trail-ready sandals.

Apparel was also strong, especially lightweight outerwear and logo tees with apparel as a whole accounting for 20% of quarterly sales. We continue to drive eco-innovation with a focus on circularity and building a greener future. On Earth Day, we introduced the Timberloop Trekker, our first footwear product that can be disassembled and recycled at the end of its journey.

We also expanded our Timberloop Take-Back program from the US to include the UK, France, Italy and Germany. In PRO, we saw excitement around our first collaboration with Samuel Adams with a limited-edition work boot selling out in one week. Initiatives like these are key to connecting new and existing consumers from work to weekend. Across the board, we're excited about the trajectory of the Timberland brand and its opportunities for future growth.

Finally, on Dickies. Global brand sales were down 13% reflecting softer trends in the Americas value end consumer and a more conservative inventory posture of our largest customer in the US. It's worth noting that excluding sales from this customer, revenue in the Americas and globally were up mid-single digits in Q1.

In APAC, Dickies was impacted in China by lockdowns, but saw positive growth across other markets in the region. Our rest European business has seen continued strong performance with regional sales up 30%, driven by work lifestyle products.

We kicked off our 100-year anniversary campaign Made in Dickies, which drove higher traffic to and average order value on our e-comm sites in the US and EMEA. We are generating solid growth globally across icons, women's and work lifestyle, while Workwear has been soft, reflecting a larger exposure to the value end.

Exciting collaborations, such as with Supreme and New York Sunshine are generating momentum and energy, while enabling Dickies to broaden its distribution into Tier zero accounts. The underlying performance of Dickies remains positive. Outside the top four brands, the balance of the portfolio generated revenue growth of 16%.

Starting with Supreme. The brand was broadly flat in the quarter and largely in line with our plan. Our European stores performed well and benefited from the openings in Berlin and Milan in the prior year, where there continues to be a high level of energy and excitement for the brand. As we indicated in May, we are excited to be resuming enhancement and expansion of the store network in coming months.

We've also returned to conducting in-person consumer engagement with recent events in Milan, New York and Paris which have received a positive response. We continue to be pleased with the performance of our outdoor emerging brands, which collectively grew 15%, driven by Altra, which was up 34%, maintaining its number one position in trail and capturing new consumers as it leverages its new products on the road.

We continue to focus on product innovation and development and recently entered the space of speed shoes with the launch of the Vanish Carbon Shoe. We're seeing an improving performance of our Packs business with stronger demand across the bag and travel category and our brands in the Americas and EMEA during the first quarter. Revenue was up more than 30% versus last year, a little ahead of schedule, driven by healthy order books, higher reorder rates and anticipation of back-to-school shipments where the season is off to a good start.

Now, let me take a minute to update you on the progress we're making on our purpose-led sustainability initiatives. As part of our road map to meet our science-based targets, VF has invested across a number of key regenerative materials. Through a collaboration between Vans, The North Face and Timberland, we invested in the first regenerative rubber pilot in the world in Thailand with TerraGenesis International. We continue to partner with New Zealand Merino to create the first regenerative wool platform in the world in collaboration with SmartWool and Icebreaker.

These projects help deepen the understanding of these benefits to support farmers regenerative journey, who'd been creating a captive supply of raw materials for use in our products. We continue to receive recognition for our efforts in transparency, with Timberland and The North Face tie for second place and Vans taking third place on the Fashion Transparency Index.

Finally, we remain committed to advancing our efforts on diversity and inclusion with the first all-black Mt. Everest climb sponsored by the VF Foundation, The North Face and SmartWool.

In summary, we delivered a solid top line performance in Q1, ahead of our initial expectations, amidst the softer consumer environment. And importantly, we're maintaining our operating outlook for fiscal 2023. This is a testament to the resiliency of our purpose-built family of brands, which is focused on the outdoor, streetwear and active spaces that benefit from favorable consumer tailwinds.

I remain impressed by and proud of our teams whose passion, perseverance and execution continue to drive our success. Looking forward, while uncertainty persists across geographies and marketplaces, from ongoing macroeconomic headwinds, we are confident in our strategies. We remain focused on the things that we can control, and we'll continue our strategic investments to ensure long-term sustainable and profit growth.

With that, I'll hand over to Matt and take you through the financials. Matt?

Matt Puckett

Chief Financial Officer & Executive Vice President, VF Corp.

Thanks, Steve, and good afternoon, everyone. As Steve mentioned, we delivered a top line performance in the quarter that was better than our initial expectations and was achieved amidst the softening consumer environment. Revenue was up 7% in constant dollar terms and up low double-digits, excluding China. Including the negative FX translational impact of nearly \$100 million, sales were up by 3% on a reported basis.

Our EPS was \$0.09, down 68% on a reported dollar basis and down 59% in constant dollars, largely in line with our expectations. However, we incurred about \$0.05 of noncontrollable impacts relative to our plans, primarily driven by FX. Before I unpack the P&L, let me talk about the operating environment across our primary geographies.

Globally, today, we are open for business from a COVID standpoint across the value chain. Although we are still feeling the effects of isolated impacts from COVID-related lockdowns in China during Q1. Revenue in the Americas was up 7%. Our performance has overall been resilient, considering the softer macro backdrop and subdued traffic levels in our DTC network. While the Outdoor segment has been the key driver, Vans also generated growth with regional revenue up 3% for the brand.

The consumer remains solid at the higher end but the value end has been more impacted, and we've seen certain retailers begin to take a more cautious approach to open to buy generally. However, we continue to see the strength of our brands position us to take advantage of opportunities in the marketplace as they arise. In the quarter, EMEA was our strongest performing region with revenue up 24%. All markets were up, driven by Italy and France. This was achieved despite softer consumer confidence, which continues to impact traffic levels.

All brands recorded growth with particularly strong performance is generated by The North Face, Timberland, Packs, SmartWool and Dickies. Importantly, both direct-to-consumer and wholesale grew by double digits.

APAC was down 15% with Q1 being a tale of two stories. First, China. We experienced meaningful impacts from rolling lockdowns across the quarter, with overall sales down 37% on the Mainland, in line with our expectations. Consumer spending post lockdown has been soft to date as expected. It is worth noting that the Outdoor segment continues to grow strongly, with The North Face generating double-digit growth in the market during Q1. Overall, the business has seen a progressive improvement throughout each month of the quarter.

Second, in the rest of Asia, our business is recovering nicely with high-teens growth being seen across markets. Turning now to gross margin. Where we were adversely impacted by a number of factors in the quarter. Our adjusted gross margin was down 260 basis points, largely in line with our plan, excluding transactional currency impacts.

As anticipated, this was driven primarily by mix, particularly reflecting the evolution of channels and brands, which together impacted margins by 160 basis points and higher freight costs, which were partially offset by price increases. We maintain a relatively low level of promotional activity, which remains in line with last year.

Let me take a moment and update you on the supply chain environment. This is a competitive advantage for VF, and we continue to use our scale and diversification to mitigate headwinds. Relative to the last time we updated you, we're starting to see the level of supply chain disruption ease albeit nowhere near the pre-pandemic normal.

In terms of sourcing, our supply base is fully operational as we step into Q2, and we continue to work to move production closer to consumption where it makes sense for us to do so. The eight weeks of lockdown in China during the quarter will take some time to flow through the system and overcome, but we are well placed to recover from this relatively quickly.

In terms of logistics, we're seeing improved transit times across the water, reflecting a slight ease in congestion and shortened dwell times in port. This is leading to overall better predictability and reliability. From a cost standpoint, there is some abatement in spot rates, both ocean and air, albeit these remain high relative to historic levels. I'd like to thank our supply chain teams for their continued hard work, perseverance and performance in this disruptive environment.

Moving on to inventory. There are a couple of things to unpack here relative to the headline number. First, we've implemented a supply chain financing program with the majority of our finished goods suppliers. In connection with the rollout of this program, we began taking ownership of inventory from these suppliers at the point of shipment in Q1, different from the past when we generally took ownership at the destination point.

This results in VF owning the inventory an additional month or so. Although we are taking ownership of the inventory sooner, there is no impact on cash flow since the point at which payment is due to the supplier did not change. Accordingly, the increase in inventory is offset by an increase in accounts payable, which was up 91% in the quarter. Now that the supply chain financing program has been established effective on purchase orders issued from September 1, VF will be increasing payment terms with the majority of its finished goods suppliers.

This change will improve VF's overall cash flow, while at the same time benefiting the supplier base. This impact is contemplated in our operating cash flow outlook. Second, the on-hand inventory, excluding in-transit, rose by about 50% as planned. On a two-year organic basis, excluding in-transit, which is a better comparison considering last year's unusually low levels, inventories were up 26%. This planned increase reflects anticipated deliveries to support on-time shipping of complete assortments. We feel good about our inventory levels, although we are closely monitoring our own and channel inventories in light of the softer consumer environment and ensuring we maintain a controlled promotional strategy.

And finally, adjusted operating margin was down by 340 basis points, largely in line with our plan, reflecting the lower gross margins and the targeted investments we continue to make in our strategic priorities. Our strategic investments increased by 7% in the quarter, primarily reflecting initiatives in the digital and technology space. On a constant dollar basis, SG&A was up 8% in our smallest quarter of the year, broadly in line with our revenue growth, reflecting our continued focus on managing the P&L and maintaining cost discipline. We'll continue with a very thoughtful and purposeful approach to managing costs across the business.

Turning to our fiscal 2023 outlook. I'm pleased to confirm that we're maintaining our currency adjusted fiscal 2023 outlook while revising our earnings outlook on a reported dollar basis to reflect ongoing negative impacts from foreign currency fluctuations.

We expect total revenue to be up at least 7% in constant dollars, unchanged from our prior outlook. We now expect adjusted earnings per share of \$3.05 to \$3.15 implying 4% to 7% growth versus the prior year on a constant dollar basis. This reflects the significant strengthening of the US dollar across most major global currencies and contemplates current FX rates through the balance of the fiscal year.

As a result of and to account for this currency impact, we now expect gross and operating margins to be up slightly versus last year. Our operating profit guidance implies growth of about 10% on a constant dollar basis.

Finally, I'd like to give you a short update on the Timberland tax case. A judge ruling issued on July 14 formalized the decision and started the appeals clock. We expect to make the deposit during our third quarter of this fiscal year.

We remain confident in our strategy and in the strength of our family of brands that benefit from favorable consumer tailwinds in our TAMs to drive sustainable and profitable growth despite a softening consumer environment and continued elevated uncertainty.

To round out my remarks, I'd just like to add that I'm proud of the great work of our teams that has enabled VF to continue to deliver against our strategy. With that, we'll now open the line and take your questions.

QUESTION AND ANSWER SECTION

Operator: Thank you. [Operator Instructions] Our first question comes from the line of Laurent Vasilescu with BNP Paribas. Please proceed with your question.

Laurent Vasilescu

Analyst, BNP Paribas Exane

Q

Good afternoon. Thanks for taking my question. Steve, I wanted to follow up on your prepared remarks and ask about the general health of the consumer to what you're seeing from a macro and market standpoint. We've seen a number of retailers and brands actually preannounce, which typically don't preannounce, most notably a German brand just two days ago. With North Face up 37% likely outperforming this year, how – can we glean anything on the state of the sporting goods channel versus other channels?

Steven E. Rendle

Chairman, President and Chief Executive Officer, VF Corp.

A

Yeah, Laurent. Appreciate you – this is an interesting question. It's one we spend quite a bit of time on looking at not only our own data, but broader market data. And as I said, the consumer health from our vantage point is generally good across all markets. China certainly lagging as the impact of the lockdowns has had an impact. But sentiment is softening, and there's a lot of data out there that would support that. And certainly, consumer behavior is changing. Consumers are becoming more choiceful as household expenses are up and in some cases, up significantly.

As we look at it and as we reflect it over our business, we see it primarily in that value end consumer. And that's the part of the market as you know, over the last five years, we've done quite a bit of work to mitigate our exposure, and we really only have one brand, and it's just a small percent of their total revenue. So where we see for our market and in our consumer, there's limited impact on that mid- to higher end consumer.

And I think where you're going, the macro trends of Outdoor, certainly health and wellness for us continue to support solid sell-through and where we're positioned with our own stores and our own digital and our key accounts, we continue to see good sell-through. We're very attentive to the right product in the right environment at the right time to the best of our ability with the current supply chain, but really managing closely to ensure we've got the products that are selling and where they're not, moving quickly to place the right products in place.

So I can speak for us, Laurent. We're well positioned. The energy you see in The North Face, the energy we see at Timberland in our emerging brands, specifically Altra, SmartWool, continue to give us a lot of confidence. The work we've done, the strategies in place, but most importantly, with the people we have working across these brands continue to keep us well positioned.

Laurent Vasilescu

Analyst, BNP Paribas Exane

Q

Very helpful. And then, Steve, last quarter, you talked about Vans sequential improvement over the quarters. How do we still think about that? And then with regards to – there were some channel dynamics between DTC and wholesale for Vans, overall, how do we think about that? And then, Matt, just a quick question. Just modeling question. I think last quarter, you talked about \$0.23 of unfavorable nonoperating impacts, three items. With the \$0.25 adjustment this quarter, was that just largely FX? Or were there other factors to consider? Thank you.

Steven E. Rendle

Chairman, President and Chief Executive Officer, VF Corp.

A

So to the first part of your question, let me first say and I think it's important. We're not meeting our expectations in Vans. And while we're not, we're still confident. We've got the right leader. You heard from Kevin in our last meeting, the strategies that are in place, but most importantly, the actions that he's driving across the business, absolutely are showing benefit and giving us confidence that we're on the right track.

From a quarter standpoint, and I guess to your sequential question, Q1, we missed really based on our lower DTC traffic and comping a strong year last year. There was slightly lower revenue in China than planned. But on the positive side, our European business continues to do well and was above expectation.

So as we think sequentially, our focus on our own DTC, where we can control that narrative where we can really drive that experience. We think about the Classics campaign that we have in place, while also staying mindful of the progression side of the product offer. We've seen continued double-digit growth with Altra. Our Sk8-Hi continues to grow at a double-digit rate. We see sequential improvement as we go across the year.

And I guess, what gives us confidence in that is where we drop new products with new innovation and new innovative partners to the comments in our remarks around Stranger Things, the Sailor Moon collab and Brain Dead, we're seeing good sell-through. There is risk in this business. I don't want to at all say that there's not. But we have a really good understanding of where it is and mitigating actions in place to make sure that we continue to move against that long-term strategy because there's every evidence in our side that this is a strong brand. It has enjoyed significant growth in the past, and it remains very relevant. And there's tremendous number of consumers still coming in engaging and joining our loyalty program, just kind of reinforces the confidence that we have and the trajectory we know we have in the future.

Matt Puckett

Chief Financial Officer & Executive Vice President, VF Corp.

A

Yeah. I'll add one point on Vans in terms of the sequentiality. Certainly, we've performed a little below our expectations in the quarter, but we're not significantly off our plans. The brand did grow 4% ex China in the quarter against, actually, what's probably the toughest compare of the year from a quarterly perspective. So for everything Steve said as well as kind of just looking at the numbers from a compare standpoint and obviously expecting the China business to improve sequentially through the year as well, we remain confident in how we see the brand positioned for the year.

I love you asked the question on nonoperating impacts, Laurent, you got the details there. You're spot on. Let me try to answer this and not confuse because it's easy to get confused, I believe. The \$0.23 we talked about before, which we gave you all those pieces, the currency component of that was translation only when we laid that out. That \$0.23 has now become kind of \$0.39, okay?

And most things are unchanged. Currency translation is kind of \$0.16, \$0.17 worse which is a piece of the \$0.25 reduction and the rest is transaction, currency transaction that's flowing through our P&L and primarily through our gross margin. So that's how to think about, kind of two-thirds translation, one-third transaction of that \$0.25 reduction. And if you throw that translation against what we were talking about previously, which I think is appropriate, you kind of get right at \$0.40 impact now year-over-year from a nonoperating point of view.

Laurent Vasilescu

Analyst, BNP Paribas Exane

Q

Very helpful. Thank you very much. I'm looking forward to September.

Steven E. Rendle

Chairman, President and Chief Executive Officer, VF Corp.

A

Thank you, Laurent.

Matt Puckett

Chief Financial Officer & Executive Vice President, VF Corp.

A

Yeah. Thanks, Laurent. See you soon.

Operator: Our next question comes from the line of Camilo Lyon with BTIG. Please proceed with your question.

Mackenzie Boydston

Analyst, BTIG LLC

Q

Great. Hi. This is Mackenzie Boydston on for Camilo. Thanks for taking our questions. My first question is just on China. Just curious, given the choppiness in that market, can you just talk about your opportunity there and how you're planning to manage inventory just given kind of the choppiness there? Thanks.

Matt Puckett

Chief Financial Officer & Executive Vice President, VF Corp.

A

Yeah. Let me start with that, and maybe Steve will want to talk about kind of the growth opportunity. Clearly, we think long term, it remains a clear opportunity for growth. We are navigating short-term challenges. We guided the business to be down about 35% in the first quarter, and we kind of largely fell in line with that at down 37%.

If you look across the rest of the region, we actually saw really, really good growth. Importantly, the outdoor brands maintain momentum aided by the kind of market tailwinds. But it really coupled with consistent performance and execution of our brand teams there, particularly in The North Face.

So I think we're navigating that in a way that we anticipated. A lot of what we saw occur in Q1 in terms of the results was us taking swift and aggressive actions with our retail partners to pull back on inventory levels and get our weeks of supply down, which is really what's happened.

We do expect sequential improvement in the market moving forward, but we'll still be negative in Q2 is our expectation kind of mid-teens, probably the way that mid-teens to 20% is kind of the way to think about that. And then returning to some level of growth as we move into the back half of the year.

Steven E. Rendle

Chairman, President and Chief Executive Officer, VF Corp.

A

And maybe to just kind of finish that out. We continue to see long-term opportunity in China and remain very committed to the Chinese market and the Chinese consumer. There's significant distribution opportunity and significant brand awareness opportunities. And I think what's interesting, when you look at the consumer trends within the Chinese market, our portfolio is extremely well suited for long-term growth, and you certainly see that in The North Face business.

We've established a structure in Shanghai, developing our local teams, strengthening that local knowledge, but most importantly, really connecting closely to serving the health and well-being of the Chinese consumer. And we think that will serve us extremely well on the long term.

Mackenzie Boydston

Analyst, BTIG LLC

Q

That's Great. Thanks for that. And then I think you kind of touched on this in the prepared remarks, but just some more color on discussions that you're having with your wholesale partners for fall and holiday. So are you seeing any more incremental caution, any cancellations and just maybe where the biggest cancellation risk might be from a timing perspective would be helpful?

Matt Puckett

Chief Financial Officer & Executive Vice President, VF Corp.

A

Yeah. I'll take that one. I guess one thing important to recognize, I think, and really important for us is we've purposely pivoted our portfolio really away from those channels which generally more challenged and more susceptible to higher levels of promotional activity and maybe more exposed to some of the impacts from an inflationary standpoint on that lower end consumer.

With that, we've got a higher penetration of both direct-to-consumer and international, which are less promotional. Specifically with the retail partners, which are our key strategic partners, both in the US and in Europe, we generate high margins with our brands, and we remain a partner of choice for those retailers. We've got strong brands. We've got great kind of connectedness to those businesses, a lot of transparency and frequent dialogue.

And ultimately, that allows us, I think, to work very closely together on issues and how we see that evolving over time. As it relates to cancellations, at this stage, our business model, we have – we always have cancellations. And it's something that's contemplated. But when we look at where we are today, our sell-through remains good. Our sales-to-stock ratios are well balanced and really the overall inventory is healthy.

So while we're watching this very closely, and we certainly will see some cancellations, we feel kind of balanced in terms of how we're viewing that. And certainly, all of that is contemplated in our outlook.

Mackenzie Boydston

Analyst, BTIG LLC

Q

Great. Thanks so much. Best of luck for the rest of the year.

Steven E. Rendle

Chairman, President and Chief Executive Officer, VF Corp.

A

Thank you.

Operator: Our next question comes from the line of Matthew Boss with JPMorgan. Please proceed with your question.

Matthew R. Boss

Analyst, JPMorgan Securities LLC

Q

Great. Thanks. So Steve, could you speak to the energy that you cited at North Face? And anything driving the sequential moderation that I think is embedded in the low-double-digit guide for the year? And then just at the overall portfolio level, you held your top line guide, but any underlying changes by brand maybe relative to 90 days ago that you'd cite in the top line outlook overall?

Steven E. Rendle

Chairman, President and Chief Executive Officer, VF Corp.

A

Yeah. So I'll take the first half. And on The North Face, in the last call, Steve, I think, did a great job really breaking down the broad-based strength across regions, channels and product categories. And that continued, Matthew, as we went into Q1 here. TNF is so well positioned in that outdoor marketplace where there is a good tailwind. And just the sheer authenticity of the brand and its relevance, both on Mountain and off Mountain is helping the brands stay very much in front of its core consumers.

I think where you see the real energy is in the product and marketing and what the teams are driving there from a real innovation and newness standpoint. You've heard us talk a lot about the 365-day initiative that came through really quite significantly here in Q1 with our warm weather products as well as rainwear selling extremely well. And as we've come in here towards back-to-school, we're starting to see backpacks pick up also our travel product.

But I think it's the marketing that's really driving this, and we carried that momentum out of the fall. This Full Circle Everest Expedition that we mentioned in our prepared remarks, this is the first all-black expedition to Mt. Everest and really drives hard against this outdoor industry opportunity of building a stronger, more inclusive community and also the Pride Campaign opening up to a broader set of consumers and inviting them also to be part of that outdoor community. This is continuing to strengthen the brand, leveraging that authenticity and setting it up really well for the balance of the year.

Matt Puckett

Chief Financial Officer & Executive Vice President, VF Corp.

A

And Matt, relative to kind of the guide. And we've consistently shown now across multiple quarters last year this quarter, this purpose-built family of brands is performing well, it's able to deliver on our commitments at the VF level. In fact, in Q1, we actually did a little bit better than our initial expectations, with that revenue growth of 7%. Actually, the top four brands combined grew 6%, and importantly, the rest of the portfolio grew 16%, contributing in an accretive way to VF results.

To answer your question about TNF and then kind of more probably the rest of the portfolio, we did not change any underlying outlook. But as we contemplate the puts and takes and Steve referenced a little, I mean, we probably do see a little more risk to Vans, but potentially, certainly some offsets to The North Face. But in our

view, it's really early in the year. And to change anything, doesn't – we don't feel compelled to do so based on our kind of how we view the overall business and how we view each of the brands, by the way.

Clearly, TNF had a strong quarter. The indicators kind of are flashing green at the moment. But remember, it's a small quarter. It's small for VF and it's even smaller for The North Face. We are – we did benefit from some wholesale shipment timing differences, which were planned, so that wasn't a surprise. We had some shipments that came end of the quarter from last year.

And then importantly, we're shipping this year closer to on time, not perfectly on time by any stretch, but definitely in a better way in terms of shipping out. And so kind of more normal shipping patterns through the quarter helped us as well. But certainly, we feel good about where The North Face is and have a lot of confidence in the trajectory of the business overall.

Matthew R. Boss

Analyst, JPMorgan Securities LLC



That's great color. And then, Matt, maybe just on the gross margin outlook. So was foreign exchange, was that the entire driver of the full year revision or any change to the promotional forecast embedded within gross margin? And just anything to think about in terms of the cadence, if we're thinking of gross margin in the second quarter, maybe relative to the back half of the year?

Matt Puckett

Chief Financial Officer & Executive Vice President, VF Corp.



Yeah. Absolutely. So the gross margin change, which we were up 50% before, up slightly. So you could kind of call that maybe around a 40 basis point change, something to that effect, largely driven by currency FX, but also have modeled in assuming a slightly more promotional environment across the business. And I think the other thing to recognize there is we've got lots of levers in gross margin. There is a little bit of favorability in terms of our outlook relative to the use of air freight as we move through the balance of the year.

So a couple of puts and takes there. But we have, I think, importantly, assume a modestly higher promotional environment as we move through the year implied in the guide. As it relates to the evolution, we certainly expect a sequential improvement in gross margin throughout the year. There's a few factors that really I think drive that. First, mix won't be the same negative as it was in Q1 based on China, and kind of how we see the mix evolving across channels and brands through the balance of the year.

So there'll be still some negative impact, I think, in Q2. But as we move through the balance of the year, that will start to right size and that will change. The cost compares from a freight standpoint will not be as impactful. Q1 is far and away the toughest compare from a freight, both in terms of rates last year in Q1, the rates had not moved as aggressively as they did beyond that. And then from an airfreight standpoint, as we move through the year, that's going to be a favorable kind of tailwind to us from a comparative standpoint.

And then I think important to note, we did see kind of pricing benefits in Q1, which were meaningful that actually will increase as we move through the year just based on the kind of the timing of some of those price increases and when they hit the market, in particular, for The North Face and Timberland, those brands that are more heavily weighted towards the fall and winter. Gross margin will still be negative in Q2. I think it's worth knowing that.

Matthew R. Boss

Analyst, JPMorgan Securities LLC

That's helpful. Best of luck.

Q

Steven E. Rendle

Chairman, President and Chief Executive Officer, VF Corp.

Yeah. Thank you, Matt.

A

Matt Puckett

Chief Financial Officer & Executive Vice President, VF Corp.

Thanks, Matt.

A

Operator: Our next question comes from the line of Bob Drbul with Guggenheim Securities. Please proceed with your question.

Robert Drbul

Analyst, Guggenheim Securities LLC

Hi. Good afternoon. Just a couple of questions from me. First, when you – the business is very strong in Europe – so I think if you can talk about the state of the consumer in the US, what are your assumptions around what you expect out of Europe over the next few quarters? And then the second question is more on some of the volatility that you're seeing in your DTC business, can you just talk about the assumptions around that piece of the business, how you're planning it? Almost curious around inventory that you have around that? And I have a follow-up with some inventory questions as well.

Q

Matt Puckett

Chief Financial Officer & Executive Vice President, VF Corp.

Okay. Bob, I'll start with maybe the Europe part and let Steve come in here on DTC a little bit. But clearly, Europe continues to be a terrific performing market for us. And it's been – kind of been and remains the fastest growing region. I think strong momentum, the integrated marketplace strategy that across brands there that's being applied really consistently and the execution of that, I think just continues to deliver great results. We're not going to grow 24% across the year necessarily again quarter-by-quarter, it's certainly worth knowing that.

A

But we're really confident in what we're seeing because it's broad-based across markets, and it's broad-based across brands. I mean every brand grew in the region in the quarter, and we said that more often than not of late. We saw double-digit growth across both direct-to-consumer and wholesale. And we just got a lot of confidence in what we're doing, the strategies and really how the teams are bringing those strategies to life from a marketplace management standpoint in the region.

Steven E. Rendle

Chairman, President and Chief Executive Officer, VF Corp.

And then, Bob, on the DTC question. There's obviously one of those – one of the key strategic pillars in the evolution of VF and certainly our brand portfolio. It remains a very important part of our long-term algorithm for sure. And I guess just to take a step back, the one thing that I think you can see that we've done is in our two largest DTC businesses, North Face, Vans. Both of our leaders come with exceptional background, both from a brick-and-mortar and digital standpoint.

A

And the benefits of VF and our portfolio model and the sharing across our teams as we work on our Vans business, as Nicole comes in and gets set into North Face business. Her ability to share, test, learn and quickly scale the ideas that drive consumer engagement, you think about consumer acquisition from an omni standpoint, not just brick-and-mortar, but how we think about inclusively stores to online, we're really – we've got the right leaders in the right place to help us really continue to elevate our understanding and their ability to engage consumers and pull them across our lease line, be it that digital or virtual or physical and look to convert them.

Robert Drbul

Analyst, Guggenheim Securities LLC

Q

Great. And if I could just follow up on the inventory. So I think it was the organic inventory that you have. There's a lot of moving pieces to the inventory generally. But when you look closely at the inventory, in terms of by brand or by region, you said you're comfortable with it, but can you just maybe put some numbers around if there are any other pockets that you're concerned about with the absolute number around where that inventory level sits today?

Matt Puckett

Chief Financial Officer & Executive Vice President, VF Corp.

A

Yeah. Sure, Bob. Happy to try to help you get there. Yeah. Overall, we feel good about where we are, certainly, as we said, I think if we look across the different business units, yeah, there's areas where we're probably a little bit elevated. We were that way in China. We're kind of coming into a better position in China with the actions that we've taken in the quarter and have kind of planned moving forward. So I think we feel pretty good about where we are there and quickly getting into a kind of better place and a healthy place.

Certainly, the Dickies business is a brand where we're a little bit elevated at this stage, given kind of how abruptly we've seen that business kind of change in the US market with that lower end consumer. And we referenced in the prepared remarks kind of a softening of sell-out, but also some inventory actions, right? So some pretty aggressive actions in terms of thinking about kind of model stocks and in-stock ratios and kind of lowering the expectations in that regard, which kind of pushes some inventory back up pretty quickly.

And so we'll work our way through that. The good news is that's all core inventory, right? So we're a little bit elevated at this point in the Dickies brand. But not something we're not capable of managing through. And I think the important thing is now that the inventories at retail are quickly in the right place with key partners. If we see improving sell-out, that will generate incremental volume very quickly as well, just as we saw it kind of move the other direction. So that's I think one thing.

And then certainly, across the rest of the brands. Vans is a little high in a few places, if I'm honest, but again, not something that's unmanageable and again, driven by core products. The North Face and Timberland are relatively well positioned. I think The North Face is, in some cases, still kind of missing some key things that we'd like to have. And we're working really hard to continue to drive back into a better overall stock position from a North Face standpoint. But hopefully, that gives you a little more color.

Robert Drbul

Analyst, Guggenheim Securities LLC

Q

Yeah. Definitely. Thank you.

Matt Puckett

Chief Financial Officer & Executive Vice President, VF Corp.

A

Thank you, Bob.

Operator: Our next question comes from the line of Michael Binetti with Credit Suisse. Please proceed with your question.

Michael Binetti

Analyst, Credit Suisse Securities (USA) LLC

Q

Hey, guys. Thanks for taking all the questions here. Maybe just following up on an earlier question, a little help orienting the model as we connect to 2Q here. How to think about growth for North Face in 2Q and Vans in 2Q? I guess, both in total and in China for Vans. I'm just curious to Matt's comments earlier on how you're thinking about the total company improvement in China going to mid-teens to 20% in the second quarter? I'd love to zero in on the brands a little bit there and North Face, too, as we get into seasonally more important?

And then I guess just bigger picture. Can you help us understand when we look at revenues relative to 2019, I know Europe's got a lot going on right now that's positive for the broader retail market, but Vans looks like it's up about 20% in Europe versus Americas down 9%. And I'm just trying to understand the difference in the consumer response to the brand in those two markets? And what you see that's different from the consumer and how they're reacting to Vans in the US from Europe?

Matt Puckett

Chief Financial Officer & Executive Vice President, VF Corp.

A

Thanks, Michael. I'll take the question here on the guide or on the outlook for Q2 and how to think about that a little bit by brand, try to shape that for you a bit. I think certainly, The North Face, the outlook would not imply in a large quarter like Q2, we're going to see the kind of growth that we saw in Q1. So you'll see some deceleration there, but we'll still see solid growth in The North Face is our expectation, really across quarters as we look across the year.

Certainly, Vans will see some sequential improvement is our expectation in Q2 into Q3 and then on to Q4. That's really driven by improvement in China. In China's case in Q2, it's kind of less negative. So that 15% to 20% is kind of a down 15% to 20%, I think you got that, but down 15% to 20% in China for VF. We haven't talked about it by brand. But you will see some sequential improvement in Vans driven by kind of the China implications as well as kind of modest improvements in the other parts of the business.

Steven E. Rendle

Chairman, President and Chief Executive Officer, VF Corp.

A

So on the Vans revenue compare between EMEA and here in the US, maybe the – I think the way I'd go at that, Michael, is let's talk about Europe specifically and what we've seen over there. And you were just with us. I think you saw the strength of our European platform. The coordinated way that we go to market. So those key account relationships are really quite critical.

And we look at those both from a physical environment, but also those key digital retailers where we've been able to leverage the scale of VF to drive those season-to-season initiatives, putting ourselves in a place to really get in front of the consumers with the right product.

I would tell you the integrated marketplace strategy that's used in Europe is really quite strong and a real deep understanding of that specialty consumer, the more lifestyle and some of those more sport-inspired parts of the distribution and really thinking through where we're placing the products and driving icons on a kind of consistent, season-to-season basis.

Our growth historically has come in those key markets of the UK and Germany. As we come into this year, we're starting to see really nice growth in France and Italy. And I think you kind of combine that you put together multiple quarters of very strong growth, contrasted here in the US where we have such a high concentration of owned stores, where we have seen the traffic compression as we continue to work to bring that back.

And to be honest with you, I think our integrated marketplace learnings from Europe are now coming here to the United States. Kevin will leverage those along with his team, and I think you'll start to see us really merchandise appropriately or differently to give consumers different views of the brand and a stronger use of our assortment to drive the revenue here in North America, taking those learnings, and that's one of the key benefits of our VF model, being able to look at those powerful strategic platforms internationally and share those learnings openly and take those learnings quickly and move them into positive results.

Michael Binetti

Analyst, Credit Suisse Securities (USA) LLC



Thanks a lot for all the detail.

Operator: Our next question comes from the line of Brooke Roach with Goldman Sachs. Please proceed with your question.

Brooke Roach

Analyst, Goldman Sachs & Co. LLC



Good afternoon. And thank you so much for taking our question. A lot of ground has been covered. But I wanted to follow up on the comments that you had made about VF's Vans owned stores in the Americas. Can you quantify the store productivity of the Vans America brick-and-mortar fleet that you're seeing now versus pre-COVID levels? Perhaps what levels of improvement is baked into the guide for second half and the implications for fixed cost leverage and margin that you anticipate as you continue to roll out those additional brand campaigns? Thank you.

Matt Puckett

Chief Financial Officer & Executive Vice President, VF Corp.



Hi, Brooke. I'll take that. Overall, today, we're kind of 85% to 90% productivity from where we were pre-COVID. And we've seen that kind of sequentially improved, but it didn't so much in Q1. That's been a kind of quarter-to-quarter improvement, but in this quarter, which is obviously a smaller quarter from a store revenue standpoint, we didn't see the kind of improvement, and that was really, I think, tied to kind of traffic compares, which we ended up being different than our expectation.

As we move across the balance of the year, what we expect is kind of by the end of the year to be right at 100% productivity from where we were pre-pandemic. So that's kind of where we are and what our modeling would assume.

Clearly, you're right, there are some implications there on the P&L today in terms of kind of absorbing the fixed costs associated with that store fleet. That said, it's a really highly profitable set of stores that we have, even operating at kind of a 90% productivity level. Super profitable. We generate a lot of four-wall profit and overall, a lot of earnings at the EBIT line for the brand. But there is some overhang there that continues as those productivity levels are a little bit below where they had been historically, which were obviously extremely high.

Brooke Roach

Analyst, Goldman Sachs & Co. LLC

Q

Great. That's very helpful. If I could just ask one follow-up. Can you provide an update on your pricing actions? Are you seeing any pushback from partners or from the consumer from some of the early pricing that you've taken? And have there been any changes to your pricing plans for the next few seasons?

Matt Puckett

Chief Financial Officer & Executive Vice President, VF Corp.

A

Yeah. By and large, no. I mean, we're right on track. We – our average price increase on carryover product was somewhere between 3% and 4% in the quarter, which is exactly what we expected it to be. I think one thing that's kind of a proof point there is Vans. In our stores, in the quarter, our AUR was up 10%. And by the way, our gross margins in our stores and online and then collectively at the channel level across brands were higher than they were last year and certainly in line where they have been historically.

So the prices themselves, and that's a clear example in Vans, but everywhere where we see it, we've not seen a meaningful impact from a pricing standpoint beyond what we would have expected. So we feel pretty good, we're going to see that impact that 3% to 4% I mentioned will grow a little bit as we move into the back half of the year as some of the brands that were kind of lower impact in the first half or really in particular, the first quarter related to spring product will start to weigh in there a little bit more.

Brooke Roach

Analyst, Goldman Sachs & Co. LLC

Q

Thank you so much. I'll pass it on.

Matt Puckett

Chief Financial Officer & Executive Vice President, VF Corp.

A

Thank you, Brooke.

Steven E. Rendle

Chairman, President and Chief Executive Officer, VF Corp.

A

Thank you.

Operator: Our final question comes from the line of Ike Boruchow with Wells Fargo. Please proceed with your question.

Ike Boruchow

Analyst, Wells Fargo Securities LLC

Q

Hey, guys. Thank you. Matt, just a couple of follow-ups. Just on the inventory. Thanks for all the color. Can you kind of help us think about how to – what you're expecting three months from now when you guys report Q2 on the balance sheet? And then I think to Matt's question, the gross margin, I appreciate another decline in 2Q. Can you kind of give us the magnitude of decline that you're expecting? And then the last one is to Matt's question, you – I think you said a little bit of an elevated promo outlook versus three months ago. Is that broad-based? Or is that specific to Vans or to any geographies or anything like that? Thank you.

Matt Puckett

Chief Financial Officer & Executive Vice President, VF Corp.

A

Yeah. So there's a lot there. Let me make sure that I get it all. The inventory position three months from now, well, I'm not going to give you a number, but we will be kind of at where we plan to be, which is going to be probably better positioned than we were two years ago. So I expect that it'll continue to see an increase versus the two-year compare.

Clearly, we're going to have, for a period of time, this impact of the in-transit inventory, which is kind of a new thing. But as we look forward and we look at kind of our days of supply, and by the way, our days we ended Q1, we're kind of in line with our expectations. We feel good about where we are.

And I think what we're focused on right now is making sure that we've got the right inventory to support what continues to be a strong sort of growth outlook across our brands as we look through the balance of the year. We're going to manage very carefully in terms of the – as we think about the environment that we're operating in for sure, but we feel good about where we're positioned there.

As it relates to gross margins in Q2, I would expect they'll be down about a point.

Ike Boruchow

Analyst, Wells Fargo Securities LLC

Q

Great. Thank you.

Matt Puckett

Chief Financial Officer & Executive Vice President, VF Corp.

A

Thanks, Ike.

Operator: Thank you. Ladies and gentlemen, we have reached to the end of the question-and-answer session. I will now turn the call back over to Steve Rendle for closing remarks.

Steven E. Rendle

Chairman, President and Chief Executive Officer, VF Corp.

Thank you, everybody, for your questions today. I'd love to leave you with three takeaways.

As you heard, we're delivering against our revenue targets. We've reaffirmed our outlook for the year, and we're generating healthy profit margins despite what is a softer consumer environment. It is a direct reflection of the resiliency and strength of the family of brands and certainly the hard-working, passionate teams that we have across our business.

Second, we're going to remain focused on those things that we can control and absolutely be thoughtful about our investment, the approach to supporting our growth and how we think about the long-term view of our portfolio. And I think then lastly, we're confident about where VF is positioned to generate that long-term sustainable growth. Our portfolio carried momentum in. It continues to show that momentum and we're really excited to have host you here in Denver on September 28 and get you up to speed on how we look at the years here to come. So thank you for your time, and we look forward to seeing you here shortly.

Operator: This concludes today's conference, and you may disconnect your lines at this time. Thank you for your participation, and have a wonderful day.

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