

Crown Crafts, Inc.

Fiscal 2022 Second Quarter Conference Call

Wednesday, November 10, 2021, 02:00 P.M.  
Eastern

**CORPORATE PARTICIPANTS**

**Randall Chestnut** – *Chairman and Chief Executive Officer*

**Olivia Elliott** – *President and Chief Operating Officer*

**Craig Demarest** – *Vice President and Chief Financial Officer*

## PRESENTATION

### Operator

Ladies and gentlemen, thank you for joining today's Crown Crafts, Inc. Investor Conference Call. The call will begin momentarily. Once again, we do thank you for attending. The call will begin in about 60 seconds. If anyone should need assistance while you are waiting, please press star (\*) zero (0) to signal an operator. Thank you.

Hello, ladies and gentlemen, and welcome to the Crown Crafts, Inc. Investor Conference Call. Your host for today's call is Mr. Randall Chestnut, Chairman and Chief Executive Officer. Joining Mr. Chestnut on the call will be Ms. Olivia Elliott, President and Chief Operating Officer, and Mr. Craig Demarest, Vice President and Chief Financial Officer.

At this time, all participants are in a listen-only mode. Later, we will conduct a question-and-answer session and instructions will follow at that time. Any reproduction of this call in whole or in part is not permitted without prior written authorization from Crown Crafts, Inc. As a reminder, today's conference call is being recorded today, November 10, 2021.

At this time, I would like to turn the conference call over to Mr. Craig Demarest, who will begin the conference. Please go ahead.

### Craig Demarest

Thank you, Jamie. Welcome to the Crown Crafts Investor Conference Call for the second quarter of fiscal year 2022. With me today are Randall Chestnut, the Company's Chief Executive Officer, and Olivia Elliott, the Company's President and Chief Operating Officer.

A telephone replay of this call will be available one hour after the end of the call through 4:00 p.m. Central Standard Time on February 8, 2022. Also, a web replay of this call will be available for 90 days and can be accessed by visiting our website at [www.crowncrafts.com](http://www.crowncrafts.com).

Before we begin, I'd like to remind listeners of the cautionary language regarding forward-looking statements contained in the press release. That same language applies to comments made in today's conference call.

I will now turn the call over to Randall.

### Randall Chestnut

Thank you, Craig. Good afternoon to everyone, and thanks for joining us for our second quarter fiscal 2022 conference call. We're happy with the results of the quarter. However, we did confront several notable challenges during the quarter.

In the early part of August, we implemented a new warehouse management system, which is intended to streamline our warehouse operations in Compton, California. However, it took almost two weeks to get the system up to speed, and during this two-week period of time, we were void of shipments almost entirely.

At the end of August, Southeast Louisiana was impacted by Hurricane Ida, and our offices here in Gonzales, Louisiana, were significantly impacted by the storm. The roof of the building was destroyed, and water leaked into the building, requiring us to close the office for several weeks and have employees work from home, which in itself was a challenge as they were experiencing power and internet outages to most of their homes at the same time that we were closed.

Along with many other U.S. companies, we're also experiencing delays and extra costs associated with the importation of goods from Asia. Fortunately, we have a contract with the freight forwarder that has somewhat protected us with slightly better rates than other importers are getting. We're passing along increases to our customers wherever we possibly can to offset these charges.

Labor has also been very tight. We've experienced higher turnover rates in our warehouse operation in Compton during the past few months. We're working with our employees and human resources to hire and retain a quality workforce, but that in itself has been somewhat problematic.

Turning to the balance sheet and dividends. Our Board of Directors today declared a special dividend of the Company's Series A common stock of \$0.35 per share along with a quarterly cash dividend of \$0.08 per share. Both of these dividends will be paid on December 31, 2021, to shareholders of record as of the close of business on December 10, 2021.

After the payment of these dividends, we will have distributed \$52.9 million back to the shareholders since we began paying dividends again in 2010. That warrants repeating itself. Since 2010, we will have distributed back to the shareholders almost \$53 million.

The normal dividend that we usually pay of \$0.08 per share per quarter, or \$0.32 annually, equates to a 4.3% annualized yield based on yesterday's close price. We're very pleased with the financial strength of the Company that allows us to pay these dividends.

Now I'll turn it over to Olivia and Craig to discuss the quarter in more details and then at the end, we'll take questions from anyone who may have questions on the line. Thank you.

### **Olivia Elliott**

Thank you, Randall, and good afternoon, everybody. I'm going to touch on the second quarter results at a very high level and then I'll turn the call over to Craig, and he's going to go into more detail.

Second quarter net sales were \$20.2 million compared with \$21.7 million last year, but if you include Carousel Designs, which ceased operations in May of 2021, from both quarters, second quarter sales for both years would have been \$20.2 million.

Net sales for the first six months of fiscal year 2022 were \$38.9 million compared with \$37.9 million last year and once again if you exclude Carousel from both years, net sales for the current year-to-date period would have been \$38.3 million compared with \$34.9 million last year, which represents an increase of 9.8% for NoJo and Sassy.

We continue to see a shift in sales due to consumers starting to shop in Brick-and-mortar locations again, but internet-based sales still represent more than 25% of our sales. We've also continued to see higher international sales this year, with those sales representing almost 5% of year-to-date sales.

Second quarter net income was \$2.4 million compared with \$2.5 million last year. When you exclude the impact of Carousel from both quarters, net income would have been \$2.4 million for both quarters, or \$0.24 per diluted share this year compared with \$0.23 last year. Net income for the first six months of fiscal year 2022 was \$5.1 million compared with \$3.7 million last year.

When you exclude the impact of the forgiveness of the Paycheck Protection Program loan from the current year and Carousel from both years, net income for the six months period of the current year would have been \$3.9 million or \$0.38 per diluted share, compared with \$3.6 million or \$0.36 per diluted share last year.

As Randall mentioned, we continued to feel the impact of rising freight costs, which impacted our gross margin this quarter. On the balance sheet side, we finished the quarter with \$1.9 million in cash and no debt. So overall, this was a very good quarter for us.

I'm now going to turn it over to Craig for more details.

### **Craig Demarest**

Thanks, Olivia. I'm going to give financial highlights. For a more detailed analysis, please refer to the Company's Form 10-Q filed with the SEC this morning.

As Olivia mentioned, net sales were \$20.2 million for the second quarter of fiscal 2022 compared with \$21.7 million for the second quarter of the prior year, a decrease of \$1.4 million or 6.6%. Sales of bedding, blankets and accessories decreased by \$1.9 million, which included a decrease of \$1.5 million due to the closure of Carousel Designs in the first quarter of this year. This decrease was partially offset by an increase of \$502,000 in sales of bibs, toys and disposables.

Net sales were \$38.9 million for the first six months of fiscal 2022 compared with \$37.9 million for the same period of the prior year, an increase of \$1.1 million or 2.8%. The increase in sales is primarily due to \$3.1 million higher sales of bibs, toys and disposables, partially offset by lower sales of bedding and blankets, including a decrease of \$2.3 million due to the closure of Carousel. The increases in sales during the comparable six-month period are due to a strong new modular set and higher replenishment orders at a major retailer.

Gross profit decreased by \$1 million and decreased by 32.8% of net sales in the prior year quarter, to 30% of net sales in the current year quarter. The decrease in gross profit includes the effect of the closure of Carousel, which recognized a gross profit of \$629,000 in the prior year quarter. Gross profit decreased by \$1.4 million and decreased from 32% of net sales for the prior year six-month period, to 27.5% of net sales for the same period in the current year.

The closure of Carousel resulted in a \$1.9 million decrease in gross profit, which in the current year six-month period included the sale of inventory below cost and the recognition of charges of \$334,000 associated with the settlement with the supplier of a commitment to purchase fabric and \$265,000 associated with the liquidation of Carousel's remaining inventory upon the closure of the business. The Company's gross profit has also been adversely impacted in both three- and six-month periods of the current year by continuing increases in the cost of ocean-going freight.

Marketing and administrative expenses decreased by \$638,000 and decreased from 17.6% of net sales in the prior year quarter to 15.6% of net sales in the current year quarter. Marketing and administrative expenses decreased by \$652,000 and decreased from 19% of net sales for the prior year six-month period to 16.8% of net sales for the same period in the current year. The decrease in amounts for the current year period includes lower charges incurred by Carousel of \$547,000 for the three-month period and \$807,000 for the six-month period.

Other items in the six-month period ended September 26, 2021, include a \$1.985 million gain from the forgiveness of the PPP loan. The current year-to-date provision for income taxes is based upon an estimated annual effective tax rate from continuing operations of 19.6% compared

with 24.2% in the prior year. The current year-to-date provision includes no tax expense from the gain on extinguishment of debt, which will be permitted to be excluded from taxable income, the effect of which is expected to lower the effective tax rate for fiscal year 2022 by approximately 4%.

During the current and prior year six-month period, the Company recorded discrete reserves for unrecognized tax liabilities as well as entries associated with excess tax benefits or shortfalls arising from the vesting of non-vested stock and the exercise of stock options. The effective tax rate from continuing operations, combined with the effect of the discrete income tax items, resulted in an overall provision for income taxes of 19.2% for the current year-to-date period and 24.9% for the prior year.

Net income for the second quarter of fiscal 2022 was \$2.4 million or \$0.24 per diluted share compared to net income of \$2.5 million or \$0.24 per diluted share for the second quarter of fiscal 2021. Net income for the first six months of fiscal 2022 was \$5.1 million or \$0.50 per diluted share compared to net income of \$3.7 million or \$0.36 per diluted share for the same period in fiscal 2021.

I will now turn the call back over to Randall.

**Randall Chestnut**

Craig, Olivia, thank you very much. Jamie, if you come back on, we'll open it up to anyone who may ask questions that's on the call.

**QUESTIONS AND ANSWERS**

**Operator**

Ladies and gentlemen, at this time, if you would like to ask a question, you may press star (\*), then one (1) using a touchtone telephone. To withdraw your question, you may press star (\*) and two (2). If you are using a speakerphone, we do ask that you please pick up your handset before pressing the numbers to ensure the best sound quality. Once again, that is star (\*) and then one (1) to join the question queue.

Our first question today comes from Linda Bolton Weiser from D.A. Davidson. Please go ahead with your question.

**Linda Bolton Weiser**

Yes, hi, how are you? I'm sorry to hear about all the issues with the hurricane impact.

**Randall Chestnut**

Hey, Linda. How are you?

**Olivia Elliott**

Hey, Linda. We are good. How are you?

**Linda Bolton Weiser**

Good, good. So, do you have your building now fixed in terms of the damage? Has it been repaired from the hurricanes?

**Randall Chestnut**

Not entirely. As I said earlier, Linda, the hurricane ripped the roof literally off the building and with all the shortages of material and labor, all the landlord has been able to do has put a temporary roof back on the building and it still has a leak in one part, but fortunately it's not over an area that affects us very much, so we've got everybody back to work, but we still don't have a permanent roof back on the building. It's been a challenge.

**Linda Bolton Weiser**

Right. So, in terms of -- I got on a little late, so I heard you describing the warehouse issue. Is that completely resolved now? And are you -- is your shipping back to a normalized level now?

**Randall Chestnut**

It is. It's resolved. It -- we had planned, Linda, to take a little over a week to take an inventory to put the system in and convert it. We had a slight hiccup or two, which you always do and it took a little over that. It took almost two weeks, and we literally were void of shipments for almost two weeks in the month of August. Then two weeks later, the hurricane came. So we had a great month. Yes, the system is in. It's operating, it's doing well and it's a good system. It just took a little bit longer than we had planned to get it in and get it all working properly.

**Linda Bolton Weiser**

Right. Is there any way to quantify the sales loss in the quarter from that issue?

**Randall Chestnut**

Linda, that's very difficult to do because a lot of it comes back in the next month in September and so it's difficult to quantify. I mean we did lose some business because we know that some retailers just canceled orders and didn't reorder.

**Linda Bolton-Weiser**

Okay and in terms of your pricing initiatives to try to recover some of your cost inflation, how are competitors reacting? I mean do you think there's any risk of losing some shelf space, or are competitors pretty much doing the same thing with pricing?

**Randall Chestnut**

Well, I mean we have to -- we have to run our own business, Linda, and that's what we do. We run our own business. We make our own decisions, and we do what's right for the Company and for the shareholders and we're going to do that. We may lose a little bit of business, but we're in hopes that it will be very minor, and -- but we've got to pass it on. The cost -- an article came out this morning and said that inflation was at a 25-year high for the month of October, the highest since 2000 -- since 1990, I'm sorry. So, we're facing inflation like we've never seen before. We have to pass it on.

**Linda Bolton Weiser**

Yes, of course. So, in terms of getting your product in from Asia, are you able to get containers, or are you literally having problems getting access to container shipping? So, what exactly are you experiencing? Is it that you're getting the containers, but everything is just delayed, or can you give a little more color on that?

**Randall Chestnut**

We're a little bit fortunate, Linda. We have a contract with a major steamboat shipper that we have in effect, that they have their own terminal in the Long Beach area where they bring the containers into and they break containers and ship it. So, we've been a little bit fortunate. I'm not going to say that we haven't had backup and that we've had goods floating around the Pacific

Ocean trying to get into the Long Beach port. We've had a number of them, but -- and we've also because a lot of our products, particularly the toy products that come from Southern China, and this particular shipper doesn't handle Southern China. So instead of risking the extra cost coming out of Southern China in and around the Hong Kong area, we're actually trucking goods from the Hong Kong area, Guangzhou, et cetera. We're trucking goods up to Shanghai, so we can use this particular shipper to ship out of the Shanghai area, which we're having to pay that cost to get it the inland freight in China, but it's worth it because we get on a -- we ship with a reliable shipper that we can count on that will get the goods on the boat and get it to us, and it also helps protect our rates.

So, we're doing a lot of different things, but net-net-net, it is costing more and it is for everybody. We're not the only one in that boat.

**Linda Bolton Weiser**

Right, okay. So, in terms of the cost inflation, would you say that in general like things are getting worse? Or were kind of stabilizing, and then you see kind of that some things are stopping going up in terms of cost inflation?

**Randall Chestnut**

Linda, that would be a forward-looking statement and we try very hard, as you well know, not to make forward-looking statements because they're hard to live up to later, but it's been difficult, let's put it that way, and we're fighting it every day.

**Linda Bolton Weiser**

Okay.

**Randall Chestnut**

Candidly, we think we're doing probably better than a hell of a lot of people were doing, because of some of the moves we've made and some of the decisions we made.

**Linda Bolton Weiser**

Right, okay and then can you just comment maybe on the demand side of it in terms of your like POS movement at retail? Is demand still fairly strong for your products and things are moving off the shelf pretty quickly? Is that the case? Or how would you characterize demand?

**Olivia Elliott**

Demand is very strong. So, our POS is very stable, and what's on the shelf is moving.

**Linda Bolton-Weiser**

Okay.

**Randall Chestnut**

We monitor POS on a weekly basis, Linda, with all of our major retailers. Not everyone because some of them don't have it, but it's 90% of our major -- 90% of our business, we get the reports weekly and see the POS for the week before.

**Linda Bolton Weiser**

Okay. That sounds good. Well, I think that's all I had for now, but thank you for answering my questions and good luck with everything.

**Olivia Elliott**

Thank you, Linda.

**Randall Chestnut**

Thank you, Linda. Appreciate it. Thank you. Have a good day.

**Linda Bolton Weiser**

You too.

**Operator**

Once again, if you would like to ask a question, please press star (\*) and one (1).

Our next question comes from Ralph Marash from First Manhattan Company. Please go ahead with your question.

**Randall Chestnut**

Hey Ralph. He butchered your last name, but other than that, how are you? Ralph?

**Ralph Marash**

There we go. If I take myself off mute, that will help too.

**Randall Chestnut**

That would help.

**Olivia Elliott**

It probably would.

**Ralph Marash**

Hi. So, I'm glad that much of the hurricane -- many of the hurricane issues are behind you, and I hope that the rest of them get straightened out really soon. Just two financial questions. The first is that inventory seemed kind of high at the end of the quarter.

**Randall Chestnut**

Actually, I'll take that one. They are up, but that's a pretty damn good thing right now. With all the stuff floating around the Pacific Ocean, at least we got goods and so yes, they are a little bit high and part of that was we had bulked up because we knew we were going to be down for a couple of weeks, and we wanted to be sure we got everything in because we weren't bringing containers in, nor were we shipping during that two-week period, so inventories are a little bit high, but it's not a -- it's not problematic.

**Ralph Marash**

That's very good. Thank you and the second question is that advertising question...

**Randall Chestnut**

Yes, the other part of that is that we bought these goods at lower prices than we would have to buy them today.

**Ralph Marash**

Thanks. That's helpful on all counts. The second question was that advertising spending seemed much lower this quarter.

**Olivia Elliott**

That's a direct result of Carousel. It was a direct consumer. So direct consumer is highly driven by advertising.

**Ralph Marash**

Great. Thanks very much.

**Olivia Elliott**

Thank you, Ralph.

**Randall Chestnut**

Thank you, Ralph.

**Operator**

Ladies and gentlemen, that is our final question today. I'd like to turn the floor back over to the management team for any closing remarks.

**CONCLUSION**

**Randall Chestnut**

Okay, Jamie. Thank you very much and thanks to everyone who is on the call today. I repeat, we're extremely proud of the results of this quarter. Management has done an outstanding job of working through all the challenges and posted good results for the quarter.

I'd like to thank everyone for their continued support and interest in the Company and a special thanks for our employees, suppliers and all of our customers. We look forward to talking with you again in mid-February when we release the third quarter earnings.

With that, we'll conclude our conference call for today. Again, thank you for attending.

**Operator**

Ladies and gentlemen, that does conclude today's presentation. We do thank you for joining. You may now disconnect your lines.