

PrivateCompanyReport




3Q Ended October 29, 2022

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Key Personnel

Rob Brooks CEO

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Analyst's Insight

Analyst : Jim Rice

Saks OFF 5TH (SO5) sales growth slowed to just under 7% in 3Q22, the first fully comparable period following the e-commerce spin-off from its brick-and-mortar (O5) business in June 2021. Excluding \$3 million of shipping revenue, retail sales grew a more modest 4.3% as the economic headwinds began to hit affluent customers and cause a pullback in luxury-goods sales, which heretofore had been more resilient. With growth slowed, operating losses grew and were also impacted by investments in marketing, customer experience and acquisitions. EBITDA was negative \$24 million for 3Q22 and negative \$57 million for YTD22. SO5 is the off-price format of the luxury Saks banner and may be somewhat insulated to the downturn, although not immune. Accordingly, and like its sister company Saks.com (Saks), the Company is slowing its growth investments and increasing its focus on profitability by curbing expenses and taking a more targeted approach to customer acquisitions. Also similar to Saks, the Company laid off an unspecified number of workers in early 2023 as it made "changes to streamline its organizational structure" and prepare for slower growth going forward. The Company plans to cut capex in FY23 and delay the opening of a new distribution center (management said it doesn't need the capacity given the slower growth).

Free cash flow was negative \$101 million in the YTD period, reflecting the operating losses and increased working-capital investments, including higher inventory levels. As a result, the Company went from a net-cash position at FYE21 to a net-debt position of \$23 million at the end of 3Q. While there is not enough data to calculate a credit score, we estimate it is in the E range. Accordingly, we are closely monitoring cash flow and liquidity. As of 3Q ended October 29, 2022, liquidity totaled about \$82 million (down from \$120 million at the end of 2Q) and included \$6 million in cash and \$76 million available under its \$125 million revolver, which had \$10 million in borrowings outstanding (limited by borrowing base restrictions). For 4Q22 heading into 1Q23, we expect top-line and margin pressures to have continued as the sector looked to clear out excess inventory levels. A more conservative approach to capital allocation and expense management should help preserve the already modest liquidity. However, SO5 is a Company that needs to deliver growth to leverage its high overhead and more modest gross profits, including the higher cost of order fulfillment. Accordingly, if growth, margins, profits and cash flow do not improve heading into 2H23, the Company may be forced to raise additional capital, including the possible sale of equity capital. Amidst all of this, in March there was a management shakeup as Rob Brooks replaced Paige Thomas as CEO. Previously, Brooks was the president of O5 retail stores (details below).

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 CreditRating:

 N.A.

A1
A2
B1
B2
C1
C2
D1
D2
E1
E2
F1
F2
DIP

What's Happening

Company Background

In March 2020, Hudson's Bay Company (HBC) completed transactions that resulted in it becoming HBC L.P., a private, limited partnership holding company, which wholly owns and operates Hudson's Bay with 83 stores in Canada and 40 Saks Fifth Avenue (SFA) stores mostly in the U.S., in addition to 86 U.S. and 14 Canada Saks OFF Fifth stores (O5, and together known as HBCx). HBC L.P. also owns controlling stakes – 75% and 80%, respectively – in Saks and the Saks OFF Fifth (SO5) e-commerce businesses. Additionally, the Company owns, entirely or with joint venture partners, approximately 40 million square feet of primarily real-estate properties (HBC P&I, which is included in HBCx). In April 2022, HBC L.P. acquired, for \$36 million, a 52.7% controlling stake in Convene Global Holdings LLC (a hybrid meeting and workspace provider) and a pledge to enter into leases, subleases and operating contracts.

Each of the Company's operating subsidiaries – HBCx, Saks and SO5 – should be considered separate credit risks.

Executive Changes

In March 2023, Paige Thomas stepped down as CEO of SO5 to pursue new opportunities outside the Company. Rob Brooks has been promoted from president of the O5 stores to CEO of SO5. Also, SVP Jennifer Drake, head of the O5 stores, has been promoted to president of O5. Thomas had joined SO5 in 2020 as president, and in 2021, she led the transaction to establish SO5 as a stand-alone digital business and was then named CEO.

Brooks has been with HBC for more than seven years. He served as chief customer officer at O5 before becoming president. HBC credited him with leading customer-centric initiatives, profit-improvement strategies and operational advancements for efficiencies.

In February 2023, Julie Mares was appointed SVP of e-commerce. Mares had previously led e-commerce and omnichannel at Untuckit.

E-Commerce Spin-off

In March 2021 and June 2021, respectively, the Company's parent announced that the Saks and SO5 e-commerce businesses would commence operations as stand-alone companies. In March 2021, Insight Partners made a \$500 million minority equity investment in Saks, valuing the business at \$2 billion, for a 25% stake. On June 21, 2021, Insight Partners acquired a 16% stake in SO5 for \$150 million. In March 2022, Insight purchased an additional 4% interest for \$50 million, valuing the business at \$1.25 billion. The Company received \$100 million of the investment and agreed to pay an affiliate fee to the brick-and-mortar retail business, HBCx. Affiliate fees for YTD22 were \$12 million, compared to \$5 million in YTD21.

Rent the Runway Partnership

In August 2022, the Company announced a partnership with Rent the Runway to offer more than 60 exclusive, previously-owned luxury brands. The partnership is structured so that SO5 will take ownership of the goods, which will only be available online and not in stores.

Credit Facility

SO5 maintains a \$125 million ABL credit facility, which matures August 6, 2026. As of October 29, 2022, there was \$10 million in direct borrowings, resulting in the availability of \$76 million, net of borrowing base restrictions. Interest on borrowings under the ABL accrues at LIBOR plus 1.25% to 1.50%. As of the same date, the Company was in compliance with all covenants. The Company also has a \$20 million term loan, due August 6, 2026. The term loan accrues interest at the LIBOR rate (with a floor of 1%) plus 5.50% to 5.75%.

Financial Snapshot

(U.S. Dollar in Millions)

	3 Months Ended			9 Months Ended		
	10/29/22	10/30/21	% Change	10/29/22	10/30/21	% Change
Operating Performance						
Sales	\$ 124.0	\$ 119.0	4.2%	\$ 395.0	\$ 165.0	139.4%
Comp Store Sales (% Change)	5.8%	39.7%		18.3%	42.0%	
Gross Margin	37.9%	38.7%	-0.8%	37.0%	40.6%	-3.6%
EBITDA ⁽¹⁾	\$ (24.0)	\$ (3.0)	-700.0%	\$ (57.0)	\$ 0.0	N.M.
EBITDA Margin	(19.4%)	(2.5%)	-16.9%	(14.4%)	0.0%	N.M.
Op. Income (Loss) ⁽¹⁾	\$ (26.0)	\$ (6.0)	-333.3%	\$ (64.0)	\$ (3.0)	<-1,000%
Int. Exp (Income)	\$ 1.0	\$ 1.0	0.0%	\$ 2.0	\$ 1.0	100.0%
Net Income (Loss)	\$ (26.0)	\$ (8.0)	-225.0%	\$ (69.0)	\$ (6.0)	<-1,000%
Working Capital & Liquidity Indicators						
Cash and Equivalents	\$ 6.0	N/A	-	\$ 6.0	N/A	-
Inventory	\$ 148.0	N/A	-	\$ 148.0	N/A	-
Inventory turnover (annualized)	1.2	N/A	-	1.2	N/A	-
Working Capital	\$ 34.0	N/A	-	\$ 34.0	N/A	-
Current ratio	1.3	N/A	-	1.3	N/A	-
Debt & Leverage Ratios						
Total Debt	\$ 29.0	N/A	-	\$ 29.0	N/A	-
Net Debt (Net Cash)	\$ 23.0	N/A	-	\$ 23.0	N/A	-
Stockholder's equity	\$ 212.0	N/A	-	\$ 212.0	N/A	-
Tangible net worth	\$ 212.0	N/A	-	\$ 212.0	N/A	-
Total debt to equity ratio	0.1	N/A	-	0.1	N/A	-

(1) Excludes transaction, restructuring and other one-time costs of \$2 million during the FY21 periods, and non-cash equity compensation of \$2 million during YTD22.

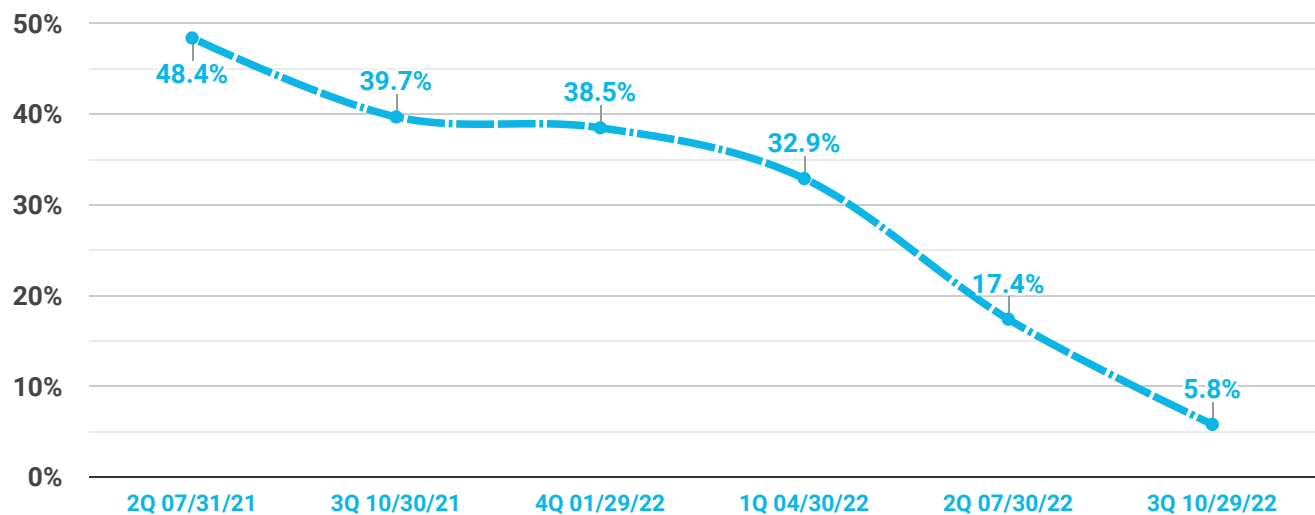
Free Cash Flow Analysis

(U.S. Dollar in Millions)

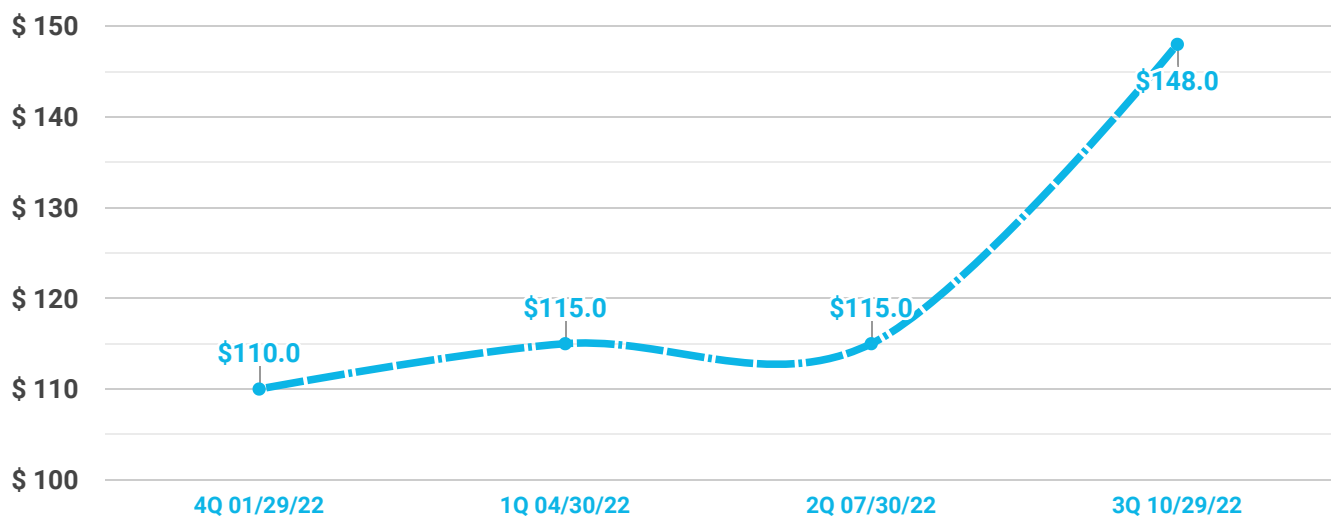
	3Q 10/29/22	2Q 07/30/22	FYE 01/29/22	3Q 10/30/21
Cash From Operations	\$ (87.0)	\$ (46.0)	\$ (9.0)	\$ 15.0
Cash From Investing	(14.0)	(8.0)	(9.0)	(2.0)
Cash From Financing	54.0	44.0	(1.0)	59.0
Net Change in Cash	(47.0)	(10.0)	(19.0)	72.0
Cash From Operations	(87.0)	(46.0)	(9.0)	15.0
+ Interest Expense (Income)	2.0	1.0	0.0	1.0
Capital Expenditures	14.0	8.0	9.0	2.0
Free Cash Flow Before Interest Expense	(99.0)	(53.0)	(18.0)	14.0
Free Cash Flow / Interest Expense	(49.5)	(53.0)	No Int. Expense	14.0
Free Cash Flow After Interest Expense	(101.0)	(54.0)	(18.0)	13.0
Debt Service				
Total Debt	\$ 29.0	\$ 20.0	\$ 25.0	N/A
Revolver Available	76.0	77.0	64.0	N/A
Cash & Cash Equivalents	6.0	43.0	53.0	N/A
Total Liquidity	\$ 82.0	\$ 120.0	\$ 117.0	N/A

Performance Charts (U.S. Dollars in Millions unless otherwise noted)

Comparable Store Sales Quarterly



Inventories





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