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CORPORATE PARTICIPANTS

Julie Wainwright *The RealReal, Inc. - Founder, President, CEO & Chairperson*

Matthew Gustke *The RealReal, Inc. - CFO & Treasurer*

Paul Judd Bieber *The RealReal, Inc. - Head of IR*

CONFERENCE CALL PARTICIPANTS

Aaron Michael Kessler *Raymond James & Associates, Inc., Research Division - Senior Internet Analyst*

Aatish Shah *BMO Capital Markets Equity Research - Senior Associate*

Abigail Zvejnieks *KeyBanc Capital Markets Inc., Research Division - Associate*

Irwin Bernard Boruchow *Wells Fargo Securities, LLC, Research Division - MD and Senior Specialty Retail Analyst*

Justin Post *BofA Merrill Lynch, Research Division - MD*

Michael Charles Binetti *Crédit Suisse AG, Research Division - Research Analyst*

Oliver Chen *Cowen and Company, LLC, Research Division - MD & Senior Equity Research Analyst*

Susan Kay Anderson *B. Riley FBR, Inc., Research Division - Analyst*

PRESENTATION

Operator

Ladies and gentlemen, thank you for standing by, and welcome to The RealReal First Quarter 2020 Financial Results Conference Call. (Operator Instructions) I'd now like to hand the conference over to your speaker today, Paul Bieber. Thank you. Please go ahead.

Paul Judd Bieber - *The RealReal, Inc. - Head of IR*

Thank you. Good afternoon, and welcome to The RealReal's earnings call for the quarter ended March 31, 2020. I'm Paul Bieber, Head of Investor Relations at The RealReal. Joining me today to discuss our results are Founder and CEO, Julie Wainwright; and Chief Financial Officer, Matt Gustke. Each of us is conducting the call from our homes, so we apologize for any technical difficulties.

Hopefully, you've had a chance to read our shareholder letter that we published earlier today, along with our press release. Before we begin, I'd like to remind you that management will make forward-looking statements during the course of this call. These forward-looking statements involve known and unknown risks and uncertainties, and our actual results could differ materially. You can find more information about these risks, uncertainties and other factors that could affect our operating results in our most recent periodic report on Form 10-K and in our earnings release from earlier today.

In addition, our presentation will include non-GAAP financial measures, and we have provided reconciliations to the most comparable GAAP measures in our earnings press release, which is available on our Investor Relations website.

With that, I'll hand the call over to Julie for introductory remarks, and then we'll go straight to Q&A. Julie?

Julie Wainwright - *The RealReal, Inc. - Founder, President, CEO & Chairperson*

So I want to say hello to everyone, and thank you for joining the call. I would be remiss if I didn't start the call with a major thank you to all the employees of The RealReal. This has been, as I'm sure everyone is saying, an unprecedented time for the employees, for our customers, for our consignors, for every person we deal with, all of the small businesses and large businesses, as our business partners. It has been a time where our strengths have triumphed over fear or hard decisions have been made where there's been tremendous innovation and tremendous angst through that innovation. But one thing is very clear. The team at The RealReal is an excellent team. It's one of the best teams I've ever worked with in my 40-year career. I'm proud to be part of this company. And we are not only going to persevere. We know we're going to end up on top.

Again, a big thank you to everyone The RealReal touches, from The RealReal employees to our consignors, our buyers and everyone we do business with.

Now that's all I'm going to do to start the business. This is a crazy time. So we are going to hear the words, fluid, et cetera, from us a lot because it is a fluid time.

With that, operator, we're ready to take some questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) And your first question comes from the line of Justin Post from Bank of America.

Justin Post - *BofA Merrill Lynch, Research Division - MD*

Great. I know it's a tough time for everyone. First question, can you help us understand how much of the downturn in sales is supply-related versus demand-related and maybe you could talk about the percent of items that sell through today versus pre COVID, just the sell-through rates? And then secondly, could you talk a little bit about the current capacity of the warehouses today? And how are you thinking about California's Phase 2 plan? And how do you see Brisbane maybe potentially opening up?

Julie Wainwright - *The RealReal, Inc. - Founder, President, CEO & Chairperson*

All right. So this is Julie. I'll take -- I'll start with most of it. So as we've said many, many times, we're a supply-driven business. Our demand did fall off for about 10 days, but it came roaring back. So our demand is clearly there, and it's at pre-COVID levels. So we're excited about that. Our biggest challenge, first in [March] and the first 2 weeks in April was actually getting supply in, in our biggest states, in our biggest regions and then, secondarily, processing that. We do have warehouse op centers in Brisbane, California and Secaucus and Perth Amboy. California is a little different. Phase 2 here, while it is a directional notion from our governor, does not mean every local town nor local county has to follow Phase 2. So it leaves more -- leaves us with more uncertainty.

However, having said that, we were told late this weekend that we could now bring back half of our staff, 200 people, in shifts of 100 per shift to work in Brisbane. And we're very excited about that. We started unfurloughing people and then rerouting product back to the Brisbane area. So again, that's -- prior to COVID, we had 460 people. So now we're going to be able to run a shift of 100 times 2 every day. We're very excited about that. And we think it's going to enhance our ability to process things very quickly. And more importantly, we started curbside pickups in many, many states in April and initiated a fleet of vans. That actually will expand as the states open up. So we feel good about where we are. Things are picking up. Things are opening up now, again, I'm going to use that word, but it's still fluid. So -- but we are excited about what we're seeing in the measures, constraints opening.

Matthew Gustke - *The RealReal, Inc. - CFO & Treasurer*

Yes. Let me just pick up on the call around -- on the question around sort of sell-through rates. I think Julie alluded to the fact that demand has held up quite well or has bounced back quite well after the initial post-COVID shock. So we continue to see traffic being up year-over-year despite our marketing spend being down 2/3 or more. And the result of that is that our sell-through rates, we measure them over multiple periods of time, 4 days being the first marker, 4-day sell-through has held -- has bounced back remarkably well and is now at post-COVID levels, just really underscoring the point that as new product comes to the site, it's going to sell.

Operator

For your next question, from the line of Oliver Chen from Cowen.

Oliver Chen - *Cowen and Company, LLC, Research Division - MD & Senior Equity Research Analyst*

Regarding the last 2 weeks of April, that was encouraging with GMV improving modestly. Could you speak to why that may be happening? And also, it was also encouraging what you mentioned on Net Promoter Scores in April. Would love your thoughts on that. And then the virtual consignment, you've quickly and agilely pivoted to that. What do you think that means in terms of step changes in the way customers interact and unit economics as well?

Julie Wainwright - *The RealReal, Inc. - Founder, President, CEO & Chairperson*

So Oliver, let's just get through a couple of things. So the recent April, the end of April picked up, it's because we rolled out virtual, and we also rolled out a fleet of vans for curbside pickup. So our demand had -- the people coming to the site had a lot more product to get into. So this is really a new initiative for us (technical difficulty) our life for a while, and we're hoping in the near term, meaning in the next few weeks, we'll also have curbside drop-off in our retail locations. So we're really, really excited about that. But really, the pickup in demand was due to this -- the whole company innovate -- now in terms of unit economics and where that goes, it's too early to tell. I think we're still going to have a blended rate. People love the face-to-face meetings, but we are getting a lot of units per when we do the virtual appointment. So it looks very encouraging now. But again, it's early days. We don't even have a full month of data in from that.

Oliver Chen - *Cowen and Company, LLC, Research Division - MD & Senior Equity Research Analyst*

Okay. And our last question, Julie, is about as you look at context for the industry and the things we're seeing with frankly bankruptcies and promotions and other people have to unlock inventory, what are your thoughts for how you'll be prepared for that kind of -- that promotional environment and how your business model will be flexible?

Julie Wainwright - *The RealReal, Inc. - Founder, President, CEO & Chairperson*

So in the past, we've seen price compression when people deeply promote. We are not seeing that now at all. So again, that may change, but we're not seeing price compression. And what we mean by price compression is we have to lower our prices in response to department stores, in particular, lowering their prices. So we aren't seeing that. Any of our discounting is due to just older inventory selling because the newer inventory is slower to go on the site.

Operator

For your next question, from the line of Michael Binetti from Credit Suisse.

Michael Charles Binetti - *Crédit Suisse AG, Research Division - Research Analyst*

I just want to square a couple of things. I think you said in mid-April with the pre-release that you were seeing traffic about flat year-over-year despite marketing down significantly. Today, you're saying traffic up slightly year-over-year, but marketing is down 66%, 2/3. But given what we've heard in broader retail about e-commerce accelerating significantly with other online retailers pointing to trends now back pre-corona levels. I guess do you feel like you've left any business on the table by restricting advertising this much, Julie?

Paul Judd Bieber - *The RealReal, Inc. - Head of IR*

Operator, I think we may have lost Julie. Can we just hold on for a minute?

Operator

Okay. But I still see her line here.

(technical difficulty)

Matthew Gustke - *The RealReal, Inc. - CFO & Treasurer*

Okay. So I'm trying to now remember the question that we're going through. Marketing spend and are we leaving things on the table. So in abstract, yes -- go ahead, Julie.

Julie Wainwright - *The RealReal, Inc. - Founder, President, CEO & Chairperson*

Yes. I mean we are leaving -- here's what we waited for our marketing. We weren't going to be running marketing against quasi-empty shelves. So now that everything is loosening up, we will be revising our marketing budget and be adding more money back in to drive our normal business. So again, the worst thing we could have done is spend a lot of money when the product was harder to get in. But again, things are starting to loosen up. So everything is fluid, everything is changing, and we will be revising our marketing budget up.

Operator

For our next question, from the line of Ed Yruma from KeyBanc Capital.

Abigail Zvejnieks - *KeyBanc Capital Markets Inc., Research Division - Associate*

This is Abbie on the line on behalf of Ed. We just wanted to know when do you think you'll see the effects, you said half the employees are going back to the Brisbane center. Do you think that will immediately increase supply? Or what do you think like the time line is in regards to this quarter?

Julie Wainwright - *The RealReal, Inc. - Founder, President, CEO & Chairperson*

Abbie, this is Julie, obviously -- hey, Abbie, look, we're going to -- that's about processing the product coming in. So there's 2 components. One, our ability to do curbside pickups increases across the U.S. We're going to be there, and that's starting. It already started in May. So we believe it's going to pick up even more in some key regions like the Western states and also the Northeast corridor. So we're excited about that. And the good news is when we get the products in, we can then process them. We do -- process them. We do have a backlog now, and we expect that backlog to diminish in the next few weeks with Brisbane opening up. So like I said, right now, it feels not like we're getting back to normal, but things are loosening up, and it looks more promising than it has in the last few weeks.

Operator

For our next question, from the line of Michael Binetti from Credit Suisse.

Michael Charles Binetti - *Crédit Suisse AG, Research Division - Research Analyst*

So I just wanted to make sure -- I just wanted to calibrate a few comments earlier. I think, Julie, you also said that demand came back quickly after 10 days. We've heard that in other places in retail as well. I think you said it's back to pre-corona levels or maybe where you were trending at on a daily basis in February. But I think the commentary you gave on forward guidance paints a little bit more of a ramp back to year-over-year levels in fourth quarter. Can you help me try to calibrate a couple of those comments, please?

Julie Wainwright - *The RealReal, Inc. - Founder, President, CEO & Chairperson*

Sure. They certainly sound conflicting, and I'll invite Matt to jump in here, too. The way we measure our demand is our sell-through without price reduction in a 4-day period. So -- but we clearly need more product in. So our overall GMV is still down. But of the products we have, it is selling at -- without a price reduction at a very fast clip. So our focus is really about getting more supply in, and supply is limiting our growth, not consumers wishing to buy on our site. Matt, do you want to give more color on the math?

Matthew Gustke - *The RealReal, Inc. - CFO & Treasurer*

Yes. Yes, that's mostly what I was going to say. I guess I'll just add that traffic is another way to think about interest or demand. Traffic is up modestly year-over-year, which is really similar to what we were immediately post super-COVID shock. So in the second week of March or, I guess, the third week of March, so up modestly right now on much lower marketing spend.

Michael Charles Binetti - *Crédit Suisse AG, Research Division - Research Analyst*

Okay. And then I wanted to ask about your comment that some of the virtual appointments, you're seeing good yields there, good conversion rates. Is there any kind of metrics you can tell? I mean if we have to think about that as being a bigger part of the business going forward, it might be good to hear a little bit more about some of the metrics you're seeing. And I know, Julie, you're dealing with a fairly limited time frame of data, but would love to hear a little bit more about that.

Julie Wainwright - *The RealReal, Inc. - Founder, President, CEO & Chairperson*

It's so -- sure. It's so limited. It's so scary. Let me just give you a couple of data points. So we've done 10,000 virtual appointments, and that's great. So we're sort of excited about that. We're doing something new today, actually it's launching, which is giving consignors the ability to self-schedule, which we also think will be pretty exciting. Right now, it's in beta form, but it will be rolled out very shortly. We were worried when we started doing the curbside pickups with the virtual appointments that we wouldn't get a lot of unit. In fact, we're getting pretty much the same equivalent unit as if we were coming to your house. And I think it's because, again, we removed friction. It's a combination of a virtual appointment with a curbside pickup with the van is great. What we don't -- but we only have 10 vans running. And so that's really not a lot. We're immediately expanding those to 15, and we'll add them on a necessary basis. So I don't -- we're testing a lot of different things, but it looks promising. It doesn't look like a one-to-one replacement for our LMs visiting. But in some areas, it may end up being that. So let's -- we'll have a lot more information by the time we get through the end of June, and then we can really give strong guidance on that, including what the economics are looking like.

Operator

And for our next question, from the line of Aaron Kessler from Raymond James.

Aaron Michael Kessler - *Raymond James & Associates, Inc., Research Division - Senior Internet Analyst*

I worried I may have missed a question, but I don't think I did. On the -- you mentioned the business vendors opportunity, I think, interest up 10x. How should we think about the longer-term opportunity there? Do you think this changes that? Or is it just more of a near-term phenomenon? And then do you think that resets a little bit lower as we get past this? And then just how has demand changed maybe among existing buyers versus new buyers?

Julie Wainwright - *The RealReal, Inc. - Founder, President, CEO & Chairperson*

Hey, Matt, do you want to take that? Go ahead.

Matthew Gustke - *The RealReal, Inc. - CFO & Treasurer*

Sure. Okay. So our vendor business has historically been small, and we've used it to kind of fill in products strategically in key categories, typically higher-value categories. You correctly state that interest in -- for new vendors, and vendors -- by vendors, we just mean businesses of any form. This could be a boutique. It could be a store. It could be a brand. It could be any form of reseller. Interest from new vendors is up 10x versus pre-COVID levels. But we're going to continue with our pre-existing strategy that we're only going to bring in product that we know we can sell. High-value, high-demand, coveted products. So historically, we're running about 5% of our GMV coming from the vendor business. That will tick up a few percentage points in the near term. And frankly, it's anybody's guess how long that goes. But I would say, so long as there are difficulties in the retail environment, I would expect to see an elevated level of vendor business. But we're not going to compromise our standards for quality and value going forward. So we'd expect it to not likely to exceed 10% of our GMV anytime soon. And then remind me of your second question.

Aaron Michael Kessler - *Raymond James & Associates, Inc., Research Division - Senior Internet Analyst*

Yes. Second question is just maybe how demand has changed maybe among maybe existing buyers and new buyers. And maybe additionally, just on the supply front, are you seeing with kind of shelter-at-home that people are kind of cleaning up their closets more and looking to sell more once they're able to or once some of these restrictions are lifted?

Matthew Gustke - *The RealReal, Inc. - CFO & Treasurer*

Yes. I guess I'll take the first one on new and repeat buyers. It's going to be a broken record, Aaron, where supply is really driving all of these trends. New buyers and repeat buyers are both kind of impacted by a more limited selection available on the site. I'd say those trends are -- they're tracking more or less in parallel. And as supply rebounds, we'd expect to see both an increase in new buyer growth and an increase in repeat buyer purchase volume. And it's interesting -- I don't think we have much more to add to the question around supply and if there's sort of pent-up demand for it. We're seeing certainly that there's strong interest in consignment. And again, our constraint has just been our ability to handle that volume, either doing pickups or through any one of our other means. So we'd anticipate as restrictions are loosened primarily in Brisbane here in California that we will start resuming not typical, but increased marketing activities, which we'd expect to start generating more interest in consignment, consignment leads, which we're well positioned to convert and start increasing supply trajectories.

Operator

For our next question, from the line of Ike Boruchow from Wells Fargo.

Irwin Bernard Boruchow - *Wells Fargo Securities, LLC, Research Division - MD and Senior Specialty Retail Analyst*

Hope everyone and your families are safe and doing well. I think this question might be for Matt. I know there's no specific guidance, but you talked about a normalization potentially by June and gradual improvement from there. So I guess my questions would be, are there any puts and takes or details you can give that kind of go behind the assumptions that you're kind of making for the rebuild of GMV?

And then 2 quick ones on what you say in the shareholder letter. You talked about the growth rates gradually improving. But then you made a comment about Q3. What I want to understand is are you saying that the Q3 growth rate could be worse than Q2? Or are you just saying that the growth is not going to be linear in the sense that like the growth rate improves meaningfully much more for Q4 versus Q3?

Matthew Gustke - *The RealReal, Inc. - CFO & Treasurer*

Sure. I'll take both of those. So yes, we'll go back to the -- I think, Julie's introductory comment that things are very fluid. We don't know more than any of you do about what's going to happen as states begin to reopen and therefore, restrictions on our business loosen beyond what we know today. We just made the point to lay out the set of assumptions that we're using to offer as much of an outlook as we can, given the information that we have. So that is based on the assumption that we do see a progressive opening of the economy beginning in June. And therefore, our business trends would start to follow that, and our growth rates would start increasing from that basis.

By Q3, what we mean -- so Q3 of 2019 was essentially our IPO quarter, where we had a significant acceleration in the business. It came back down to more normal levels in the fourth quarter of 2019. So what we mean specifically is that the improvement in growth rates as we go quarter-to-quarter is not likely to be linear, not that necessarily that we expect the year-over-year growth rate in Q3 to be lower than in Q2.

Irwin Bernard Boruchow - *Wells Fargo Securities, LLC, Research Division - MD and Senior Specialty Retail Analyst*

Got it. And then, Matt, just when you say potentially exit the quarter in Q4 2019 levels, I just wanted to clarify, do you mean the quarter itself could be comparable to the Q4 of '19 or that you're -- by the time you're exiting the quarter? Sorry to get too granular.

Matthew Gustke - *The RealReal, Inc. - CFO & Treasurer*

Yes. Well, it's overly precise from what -- for what we're able to foresee. We can't accurately predict what's going to happen for Q2, no less in the months of Q4. I think the spirit of that is just to say that we think that by the end of the peak holiday season, think of it as kind of November, December, that we -- our internal models and our resource builds and the staffing that we are planning for in our e-commerce centers and our sales team would support growth that's approaching 2019 levels in peak holiday season.

Operator

For our next question, from the line of Susan Anderson from B. Riley FBR.

Susan Kay Anderson - *B. Riley FBR, Inc., Research Division - Analyst*

I had a quick question on the $70 million in cost saves. Is that meant to just be in this -- or how is that supposed to be spread out over the year? Then also, can you talk a little bit about where the savings are coming from?

Matthew Gustke - *The RealReal, Inc. - CFO & Treasurer*

Sure. So $70 million, just to be clear, is the intent of the expense reductions that we've made that would impact this fiscal year. The cuts were broad-based. The largest was marketing. So think of approximately $20 million, $25 million of that $70 million was intended to be marketing. And the rest of it is, broadly speaking, headcount-related including things like hiring freezes, layoffs, unfortunately and furloughs that made up the bulk of the rest of it.

In terms of the sequencing of the cuts. We took action pretty early, which is serving us well. The cuts began toward the end of March. And of course, we're paying people into the early part of April. So we will have a pretty good, lower run rate in the second quarter that's more or less tracking the -- our expected GMV profile and then building kind of back up from there as we get to the rest of the year.

Susan Kay Anderson - *B. Riley FBR, Inc., Research Division - Analyst*

Great. That's helpful. And then just on the technology front, it looks like you're still investing there, I think, as planned. But I guess have you cut any of the investments slated for this year on the tax front to make the operations more efficient.

Julie Wainwright - *The RealReal, Inc. - Founder, President, CEO & Chairperson*

This is -- we did put a hold on some hires in tech, but that was the least -- there were 2 areas that were the least touched, tech and then also our sales team. So the sales relationship with our consignors, new and repeat, is really important. So both of those were left mostly intact. I would say that the tech team had to shuffle their priorities. We weren't doing virtual consignments prior to the COVID situation. So it's -- they're really more focused -- their focus changed, and they have -- they were least affected, but they also were affected.

Matthew Gustke - *The RealReal, Inc. - CFO & Treasurer*

Yes. And I would add to that, that the pre-existing priorities are largely untouched, right? So we've talked a lot about focusing on operations efficiencies and automation. And we continue to make good progress there. We made progress in the first quarter and expect to see continuing progress throughout the year, such that the 3 key areas that are impacted by automation to include copywriting, photo retouching and pricing could all approach 75% of unit volume.

Operator

(Operator Instructions) Your next question comes from the line of Simeon Siegel from BMO Capital.

Aatish Shah - *BMO Capital Markets Equity Research - Senior Associate*

This is Aatish on for Simeon. In terms of new buyer acquisition, does the current environment change the go-forward strategy when things normalize? Meaning, are there any learnings from the media mix and SEO optimization?

Julie Wainwright - *The RealReal, Inc. - Founder, President, CEO & Chairperson*

Well, let me tell you that whatever we learned, we're not resting our -- we're not assuming it's going to be that interesting or applicable going forward. Everything we do is test and learn. Now having said that, a while ago, we went into OTT more aggressively than digital. And during this time, with shelter-in-place, it's really served us well. But I mean that doesn't mean that we're going to continue that strategy going forward. But even when we cut budgets, we kept a very small budget running on such properties like Hulu, which has done very, very well. SEO, we always continue to work in the background, and that's actually been driving our costs down. Our cost of acquisition is so low that pre-COVID, that we really -- we're in good shape in any case. We've really got some great performance marketing people on our team that know how to drive efficiencies and effectiveness at the same time.

Operator

(Operator Instructions)

Matthew Gustke - *The RealReal, Inc. - CFO & Treasurer*

Okay. Great.

Julie Wainwright - *The RealReal, Inc. - Founder, President, CEO & Chairperson*

Listen, I want to thank you. I do want to -- I think I was cut off with Oliver's question on retail, and it's going to be carnage out there. We aren't dependent on retail. I think that's going to be our gain during this period of time. And it does make me sad to think the retailers that are primarily a retail company are going to have such a hard time. But we're in a unique position to get stronger due to that. It's not a position I necessarily want to be in, but it's an opportunistic position for us to go from strength to strength.

So I want to thank you all for your time. Hopefully, we can do this again without technical errors. The next time, we might even be in a real office instead of working out in our various homes. I hope you're all staying healthy. And please remember, we're open for consignment, virtual -- you can do self-scheduling and virtual appointments. We'd love to work with you. Thanks so much.

Operator

Ladies and gentlemen, this concludes today's conference call. Thank you all for participating. You may now disconnect.
