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REAL.OQ - Q3 2020 RealReal Inc Earnings Call

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PRESENTATION

Operator

Ladies and gentlemen, thank you for standing by, and welcome to the RealReal Third Quarter 2020 Earnings Results Conference Call.

(Operator Instructions)

I would now like to turn the call over to Paul Bieber. Sir, you may begin.

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

Thank you, Corey. Good afternoon, and welcome to the RealReal's Earnings Call for the Quarter ended September 30, 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.

Hopefully, you had a chance to read our press release and stockholder letter that we distributed earlier today, both of which are available on our Investor Relations website.

Before we begin, I'd like to remind you that we will be making 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, subsequent quarterly reports on Form 10-Q and in our earnings release from earlier today.

In addition, our presentation will include certain non-GAAP financial measures for which we have provided reconciliations to the most comparable GAAP measures in our earnings press release. 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*

Thanks, Paul, and welcome to our Q3 earnings call, everyone. When we provided our last update in August, we were seeing encouraging signs of recovery. In July, our supply has returned to growth, and GMV was on the cusp of growth. Improving trends in our LA and New York City markets, led by the influx of supply into our reopened luxury consignment offices, known as LCOs and retail stores and an increase in request for white glove service overall contributed to our improving GMV and our GMV quarter growth.

Consequently, we started reinvesting in marketing sales, hiring and expanding our retail footprint with the launch of TRR in Chicago. We are learning how to work safely in a COVID environment and feel comfortable making these investments for current and future growth. In fact, we're beginning to show results. The 17% quarter-over-quarter improvement in Q3 GMV underscores our improving fundamentals.

And so far in Q4, retail and LCO supply increased 48% year-on-year in October, compared with down 20% year-on-year in Q3 and down 81% year-over-year in Q2. This retail recovery amplifies our overall supply recovery and gives us optimism that a return to positive year-on-year GMV growth could happen over the balance of Q4.

While uncertainty remains, we are laser-focused on making operational changes and strategic investments that will position us to emerge from COVID, a stronger, more agile company and set us up for long-term sustainable growth going forward. Once again, we'd like to thank all of our employees for their dedication to continuing to move the company forward during these unprecedented times. And with that, I'll turn it over to questions.

QUESTIONS AND ANSWERS

Operator

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

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

I guess a couple of questions here. Obviously, vaccine news. When you look out 9 months to 12 months, what could be different for your supply acquisition? And you think that could really get a lot easier for you next year? And do you think as people go virtual on curve side, you could really see some savings now that you have more experience with that?

And then second, the marketing spend picked up and the new buyers were, I think, $5 million in the quarter. How do you feel about the efficiency of that marketing spend? And do you think it will get more efficient as we move forward?

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

I'll start, and then I'll turn it over to Matt. So post-COVID, here's what we -- you don't really know what it's going to look like, but we have a pretty good indication that virtual is here to stay. And we're pretty early in the phases of using that as a tactic. So it's hard to predict great efficiencies, but it's a really good way for our LMs to work and for our gemologists, some of our gemologists to work and our watch experts also. So that will definitely be in the mix going forward.

Stores are going to be in the mix. Since we've reopened the store, we're seeing, as we noted and our LCOs, influx the product, people are really comfortable dropping off product and that's starting again too in October, a record number. We're also going to test, took a mini store LCO concept, similar to the one in our Madison store in New York City, very small footprint, 2,000 to 3,000 square feet with about 400 to 500 SKUs max in the front and then luxury consignment offices in the back.

We're going to be running that test in the next 120 to 150 days, we should have 3 of them with our one opening next week in Palo Alto. So that we believe will be part of the mix because Madison, as a neighborhood store, a small footprint neighborhood store with a luxury consignment office has really come back quickly. We also believe vendor is going to be a more important part of our mix and maybe a greater percentage. We've always used vendor strategically to offset or to go after certain product lines.

We believe for the next year to at least 18 months, we're going to have even better quality vendor products, and we're already seeing some of that mix change now. So vendor won't be a huge percent, but it will be a more prominent part of our business, maybe 15% of the GMV, it may be as high as 20%. So we will see -- continue to see products mix shifts, too, as noted in other businesses, apparel and footwear have been down for us, while fine jewelry, handbags and men's have done really well along with home and art.

So all of those things, we expect to more normalize as people get out and about and go into offices again. So we expect all of our categories to start growing again and healthy numbers.

I'm going to make one comment about the marketing efficiency and then turn it over to Matt. Look, we are really great at driving down our cost of acquisition, but now wasn't the time to really pull back on putting money into the marketplace because what we're doing is not just generating demand, but future consignors. So while our marketing efficiency isn't what it was prior to COVID, we do expect it to return to a nice number and then a declining number over time. It just makes sense because we still have an amazing flywheel effect where our buyers become consignors and our consignors become buyers. But with that, I'll turn it over to Matt for more color.

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

Yes. Thanks. Thanks, Julie. Thanks for the question, Justin. So a couple of ways to think about marketing efficiency. And I think it's -- there's a little bit of danger in getting too focused on the very short term. So if you would go back, like the second quarter, for example, where our marketing investment was as close to 0 as we've ever been and the marketing efficiency in that period was off the chart, right? And so naturally, there's some sort of correlation between spend and efficiency.

We saw signs of recovery in as early as early May, at which point, we began to progressively reinvest. So we have continued to progressively reinvest as we continued to see signs of recovery in both supply and GMV. And most recently, with retail starting to come back, we're feeling that it's the right decision for us to make. It's going to take time as the typical path for people to turning into buyers as they first become members and then they either become a buyer or they become a consignor. So the investments that we're making for today are helping us today, but they're going to help us next month, next quarter and beyond. So we are laser-focused on setting ourselves up to come out of the year in a strong trajectory and set ourselves up for a strong post-COVID world.

Operator

Your next question comes from the line of Oliver Chen from Cowen.

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

Regarding the regions, you've seen improvement in supply in New York and LA, but New York looks like it's improved faster than LA, which is less negative. Could you help us understand how those markets are manifesting and any differences or similarities between them? Also, the inbound operation unit costs ahead look like an opportunity for automation. So what would you generally highlight for efficiencies that you're seeing ahead as we look forward to that as well?

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

Oliver, I'll start again, it's nice to hear your voice, and turn it over to Matt. New York, the schools are back. So just to be blunt, the schools are open and people came back faster into the urban area. So -- and when our -- we reopened SoHo and then we opened Madison. The stores became vibrant. The LCOs got busy quickly. So New York, while still not performing as phenomenally as well as it did last year, beginning of this year, it seems like last year, it is coming back faster.

So that's what we think is the prime reason. It's just people are back and engaged in New York and New York area. So that -- I mean, there isn't -- I don't know, Matt, if you have another theory because every other number shows that just we can tell you when people start coming back. And when Hamptons started shutting down, our business started ticking up in August.

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

Yes. I've seen the same basic thing. The only other thing to add to that is we do have an extra store and an extra consignment office in New York. So we have a little bit more of a retail presence there. So that certainly contributed at the very tail end of the quarter and certainly into October. But we're obviously encouraged by the trends in both the markets, but recognize there's still a very long way to go to where we were.

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

And then...

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

The second question...

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

Yes. Second question.

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

Yes, on inbound automation efficiencies. So we're progressing very nicely even during COVID. We basically got into our stated goal of 75% automation in the big 3 projects that we've talked about repeatedly by the end of the third quarter. We think there's some more incremental room for us to go to automate a little bit more. But the gains that are going to come from that are not so much by further automation. It's driving increasing volume through the system because there's a tremendous amount of leverage that comes from a steady amount of a lot of supply that helps us leverage the people that we have, and there are certain aspects of the costs that are fixed. So getting back to growth is when we're really going to start to see even more benefit than we have recently.

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

Okay. And finally, on the order account, Q3 orders being down 5% and your average order value being up. Would you expect a similar dynamic? Like how does that interplay with the supply units and/or the changes you're witnessing in mix?

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

Yes. So I'll start that one. So underneath AOV is our selling prices and items per transaction. Selling prices have remained elevated throughout COVID really. And that's really on the back of a mix shift toward more handbags, jewelry and, to some extent, men's products. So that we'd expect to see continuing into the fourth quarter. But that other part of units per transaction that's more tightly correlated with the abundance of supply, the total available supply in the marketplace was still down a fair amount throughout the third quarter. So as our supply builds back up, that's where we'd expect to see that start to come back up and get our AOV overall back to where was it pre-COVID.

Operator

Your next question comes from the line of Michael Binetti.

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

So I just want to ask a quick one on the short term here. I want to understand how you're getting back to flat GMV with positive November, December? We're starting off at, I think, negative 5 in October. And obviously, we're seeing the headlines of COVID spiking again. But I'm sure you're more prepared than you were last time you saw these spikes. But I would assume that, that would -- that could hurt supply again until there's a vaccine available, which obviously we got nice news on today. But maybe walk us through how you're building through the quarter getting back to positive, please?

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

I'll answer a little bit, and then I'll turn it over to Matt. We don't really -- look, COVID is out there. It's not going away. But I would say our consignors and our sales team has learned how to live with it and pick up product safely. Store drop-offs really are changing the dynamics in key markets for us right now, even though we only have a few stores open. But not just stores, LCO drop-offs also.

So we're not as worried about a big shutdown like we had before, where we couldn't operate at all. I think going -- certainly, COVID is rampant, but it's more under control in the urban areas than it was before. So we feel like we will be able to -- we've already seen some improvement in supply. We're going to be able to continue to grow supply and we are -- as we said, we're also testing another -- the mini store LCO in -- like the one on Madison, that's going to open in Palo Alto. So we feel pretty good about where we are -- what we've seen, I mean, the number we gave out on the LCO plus retail store drop off, up 48% year-on-year in October. I think it bodes well as we move into the winter.

So that's why we feel good. And we do think -- expect to see seasonality in gift giving during the holidays time. So it's still uncertain times. We don't want to sound overly optimistic, but we have enough early indicators that we feel good.

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

Yes. Not to slice this too finely, but I think just to add another level. So what we saw throughout Q3 was relatively steady improvements in supply. And then GMV sort of followed. We had a little bit of a lapping thing in the middle of the quarter. But coming into October, things were a little -- that recovery kind of stalled out for a couple of weeks, but then really started to pick up momentum in the back end of October. Retail was a big driver of that and by retail, that's inclusive of the LCOs.

General recovery amplified by retail in the tail end of October. And that supply -- as you know, Michael, that supply is not going to hit the site for 2 to 3 or maybe even 4 weeks from the end of October, and it's going to benefit us as we kind of get deeper into the holiday season.

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

Okay. It's a fine tooth question, Matt, but on the -- if we take out the supply coming in through retail and LCO, it looks like the the other area -- that's only 18%, I think you said of the supply in the shareholder letter. It means the rest of the channel would be over 80%. And it looks like that would be -- that supply coming in through other channels is probably up high-single digits in the third quarter. It seems like it leaves quite a bit of room for that to decelerate in the fourth quarter, still get to your double-digit growth target. Is that -- are you seeing similar trends in other areas? Or is that conservatism would be a fair answer, I'm just curious what you're seeing in the other areas?

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

No. That's not -- certainly not how we're thinking about it. So I won't answer all those parts because there's a little bit apples and oranges, the supply value versus supply units. But here's what I'd characterize it. We are calling it like we see it. I think there's enough uncertainty in the world so we don't want to add to that uncertainty by unnecessarily providing conservatism on top of our guidance. I don't think that serves anyone well.

So we are being as transparent as we can possibly be given all of the uncertainty around us and telling you exactly what we think is going to happen. So that's -- we're confident that we can see a return to growth over the balance of the quarter. And the entire organization is laser-focused on getting us there, not just to deliver this quarter but -- we're certainly not thinking exclusively about the short term. We are very focused on setting ourselves up to exit the year with strong momentum. So that when COVID is behind us, then we can really be a significant part of the bounce-back story.

Operator

Our next question comes from the line of Eric Sheridan from UBS.

Eric James Sheridan - *UBS Investment Bank, Research Division - MD and Equity Research Internet Analyst*

Maybe I'd come back to newer sales reps that are joining the organization now, how does that compare to some of the efficiency ramps?

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

Oh, we lost him.

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

We lost Eric. Is he still with us? Operator, are you still there?

Operator

Yes, sir, you're still in the call. He -- his line -- and I'm showing his line still connected and open, at least on our end.

Eric James Sheridan - *UBS Investment Bank, Research Division - MD and Equity Research Internet Analyst*

Can you guys hear me okay?

Operator

Now, you are back.

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

Yes, back.

Eric James Sheridan - *UBS Investment Bank, Research Division - MD and Equity Research Internet Analyst*

Okay. Sorry about that. I was curious about sales reps joining the organization now, what you're seeing from an efficiency standpoint and a productivity ramp versus before pre-COVID period, how that might compare? And then I apologize if I missed it earlier in the call, but anything on COVID-related expenses of a permanent nature versus transient nature whenever that happens, then we're on the other side of this thing, how to think about the impacts on the cost structure from those 2 variables?

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

So I would say we're still learning how to ramp our team and train our team, and we've had some wins, and we've had some opportunities for improvement. So it is more challenging in COVID times. We used to -- people used to shadow each other. So I would say that it's been uneven, some really big wins, but it's been uneven. So we have work to do in our training of bringing on new people.

Efficiencies virtual still a new tool. We're learning how to work with that. That's more I think a long-term situation, we've only been doing virtual now for a few months. So that -- we do expect efficiencies over time. But right now, we're more worried about getting in as much product as possible and taking advantage of some interesting trends that we've seen. Most notably, again, a lot of people are dropping off at the LCOs and the store. So we're capitalizing on that and moving forward.

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

Yes. A couple of other things amplifying that. So it always takes our new salespeople a few months to ramp.

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

That's right.

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

That's been kind of the natural trajectory since the beginning of the company. But we've amplified that because of how intensely the change from one quarter to the next in terms of the number of salespeople. In the second quarter, we weren't hiring anybody. In fact, we had to let a number of salespeople go.

So from that low point to where we're heading in Q4, the sheer number of new people is higher than really any period that I can remember as a percentage of the base. So there's a short-term productivity hit. But I think as we kind of get into next year, that should normalize.

And the second question with respect to COVID expenses. From memory, I think we're looking at about $6 million of COVID-specific expenses for 2020 and that's going to continue on, realistically, at least until next summer at about $2 million to $2.5 million a quarter, after which we think it should sort of trail off. Hopefully, by this time next year, COVID is in the past and COVID expenses are as well.

Operator

Your next question comes from the line of Ike Boruchow from Wells Fargo.

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

Matt, I kind of wanted to dig into the direct business, just to make sure I understand what's going on today, the last couple of quarters, the thoughts for Q4 and just high level into next year, how to think about it. I mean the penetration has obviously gone up. I think you've explained what's going on. The gross margins have been down by a decent amount year-over-year. Trying to understand how to think about that into the fourth quarter? And then how do you see this kind of normalizing into next year? Is this going to take some time until things start to improve. Just anything as we look out on the profitability and the drivers of what's going on there would be helpful.

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

Sure. So for those of you who aren't as familiar, so we have a component of our revenue that is booked on a gross basis. That's direct sales. And that's really anything that originates from product that is on our balance sheet as inventory. Most of that product historically has come from kind of late customer returns that we've accepted back and has yielded about 6% to 7% of our total GMV coming from that channel.

It's been a touch higher over the course of this year and that's largely due to having a relative lack of supplies we've had to sell harder into the inventory that we had on hand. So that's a temporary phenomenon. And as we build back supply that component of direct should normalize out.

Now we are starting to ramp, though it's very small, still a buy upfront program that we use selectively with both individual consignors and some of our business or vendor sellers where we offer to buy products upfront. That yields a slightly better margin for us at the end of the day, but we're highly selective in the products that we offer that to. So that has a small impact now and expect it to be a relatively small impact going forward.

That said, given the nature of that business, where the costs are essentially fixed upfront and the GMV that comes from that is subject to a little bit of ASP pressure. That's where you kind of get that margin variability. But it's a small part of our overall mix of GMV and doesn't really have any material impact by the time you get down to what really matters, which is our gross profit per order. So going forward, I think you're going to see percentage margin variability anywhere from the low teens to just, call it, 20%, but it doesn't really have a weighted average material impact on gross margin.

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

And is there anything on the inventory on the balance sheet today, Matt, that makes you uncomfortable? Are you pretty clean with your inventory right now?

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

Yes, yes, yes. I mean, our inventory at the end of the quarter, I think it's still sub $20 million. So yes, it's still a very small inventory balance in the grand scheme of things, and we're not looking at that and thinking about any significant inventory risk.

Operator

Our next question comes from the line of Edward Yruma from KeyBanc Capital Markets.

Edward James Yruma - *KeyBanc Capital Markets Inc., Research Division - MD & Senior Research Analyst*

I guess, first, Matt, just a quick modeling question. You said somewhere in the shareholder letter that you expect units shipped to approach double digit and yet GMV is expected to be flat. So I just wanted to square those 2 comments.

And then, I guess, second -- and you pointed out some mix issues, favorable mix but ultimately resulting in a lower take rate, I think, 190 bps decrease year-over-year. Do you expect this mix to kind of hold in the short to medium term? And there have been some publicized large competitors that are seemingly incentivizing some of these categories. Are you seeing downward pressure on some of these hot items, like sneakers and watches?

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

Okay. I will start with the supply demand. And maybe you want to talk about some of the category terms we're seeing, Julie. So what we laid out in the shareholder letter with supply outpacing demand, that's entirely consistent with what we anticipated and what we, in fact, knew needed to happen coming out of the year. The reality is we were in a supply imbalance, a deficit in available supply versus where we were a year ago. So in order to get the marketplace back in true balance so that we can -- supply and demand can grow in lockstep going forward. we first needed to get back to kind of even water level. So that is the simple math. So if we're growing supply in the high-single digits over the balance of the year that will enable us to kind of get back to seeing positive growth in the GMV side.

And then I'll start on the category piece. You're right. Higher selling price products have an inverse correlation with take rate, handbags, jewelry, watches, et cetera. In the very short term, I think that mix stays because that's -- COVID or not that is the typical holiday mix. So particularly as we get into the peak of the holiday season, I would expect to see elevated levels of those product categories, more or less consistent with what we saw in Q3, frankly, maybe a little bit higher but then as we get into next year, we are seeing interesting signs of recovery across categories. So it's not like no one's buying women's ready-to-wear, that is coming back nicely as well. Particularly as we get closer to the end of COVID, I think we'll start to see our product mix drift back to what its historical level was.

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

And when you're talking about increased competition, we have such a large TAM. We really don't feel especially when peer-to-peer marketplaces start going down to maybe no-commission or aggressive commission. That's a way for them to compete. It's not really the self-posting world, really isn't our consignor base. And so we don't see that as any competition for product at all. So yes, I mean, I think that's probably the fairest way to say, but we do participate in a very large TAM. And for us, it's just getting that -- just getting the product back in again, but it's coming in nicely for us.

So...

Operator

Your next question comes from the line of Aaron Kessler from Raymond James.

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

A couple of questions. Maybe first just on the supply acquisition. Can you give me a rough sense for where that sits today by mix and maybe potentially how you see that changing longer term? Should we expect some of these mini stores to replace some of the historical kind of white glove service as well? And how are you thinking about maybe the cutoff for white glove, is could be by price? Or how are you looking at deciding kind of when you send out a sales person to a person's home going forward?

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

Mix -- look, the mix hasn't changed that much. I mean we've been pushing certain categories because we go into high seasonality. So we've always sell a lot of handbags, fine jewelry and watches. So if you go to our site and you see any kind of promotion, it's just our normal prep for high seasonality.

On the mini stores, I think, first, it's probably a good moment to take a step back. When we saw -- before COVID, we saw a shift where people were dropping off things at the LCOs and the stores when we got up to about 18% of supply value coming into those channels. So we changed the shift with the type of people that work in those stores and our LMs did not facilitate that transaction with our consignor. So we've -- we changed that. I would assume that if these mini stores work, then we will have a different mix, we have more of associates, more sales associates and consignor associates working to assist the consignors in those stores, and they are -- they can be set up a more efficient model for us. I don't know if that answered the entire question.

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

Most of it. So then the other question is what -- how we're thinking about the traditional white glove in-home service going forward?

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

Well, we've always kind of cut off. We've always had -- we have -- we sort of work the way the consignor works. But we -- our average -- and this really has been fascinating to watch even with virtual appointments and curbside pickup. We've always gotten about 2.5x more value by going to someone's home than if they send it into us. And that's just the nature of having a close relationship with the consignor and qualifying them before we go into the home. So we've always had that, and I don't expect that to change at all.

What may change is the mix in the market, especially if these mini stores start working and maybe hiring more people in a regional market, it would shift to a different type of sales associate in the store.

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

So that's clear, I mean, the virtual style of appointment is not just a COVID phenomenon. It's here to stay, and it works very well for certain people. But the exact mix of in-home versus virtual going forward, we don't know. We're certainly going to let our consignors largely lead us there because at the end of the day, we're providing a service, and we want to make sure that our consignors are as satisfied as they can be.

Interestingly, very recently, we've been starting to see an uptick in the interest for in-home appointments again. So I think that's kind of another sign to us that people are kind of settling in to trying to think about the post-COVID life.

Operator

Your next question comes from the line of Rick Patel from Needham & Company.

Rakesh Babarbhai Patel - *Needham & Company, LLC, Research Division - Senior Analyst*

I had a question on the vendor programs. But I believe you mentioned this could reach 15% to 20% of the business. Does this happen over the next year? Or do you see this as a long-term target? And second, can you provide some additional color on the areas of investments that would be needed to support growth here? I'm just curious how it affects the margin trajectory as we think about the coming quarters?

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

It's really more of a long-term, it's probably more of an 18-month plan to get the vendor at that level. We've already started staffing and changing our staff to have category expertise and bringing in more senior people in that category. We've not quite changed the entire team, we're more strengthening the team, but it's getting there. But it's more within the next 12 to 18 months we'd expect that shift to happen.

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

Yes. And so part of getting there is staffing up and creating category expertise and focus. Technology is another key portion of the strategy. But we need to build out certain technology that can support selling multiple quantities of a similar item. And that itself -- that's a multi-quarter journey to get that launched and really streamlined.

And in terms of the impact on margins, what's true -- but it's hard to say because we don't know exactly what the vendor product is going to be. But if it's similar to how it has been historically, it tends to be significantly higher than average value in terms of selling price per product. Now of course, it means the take rate is lower, but when you translate that down to the actual number of dollars of GMV and gross profit dollars per unit, it tends to be significantly higher than average. So it should be additive to our contribution margin over time.

Rakesh Babarbhai Patel - *Needham & Company, LLC, Research Division - Senior Analyst*

And can you talk about the competitive backdrop as well with holiday promotions starting earlier this year? Are you seeing any impact on your business in terms of average selling price or perhaps gross margin as you need to price competitively?

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

Yes. I'll start that. No, it's a simple answer. I mean, our average selling price was up 9% in the quarter, continues to be up year-over-year. So we're not seeing any particular impact that's connected to the retail environment. Part of that is given the mix of products that we have right now, which is skewed more toward handbags, jewelry, watches, which just inherently have much less promotional pressure potential. So that's the good news. Bad news, right, so as the supply starts to come back, it's going to be coming back and demand is going to be coming back even more so in women's ready-to-wear, but that will be a nice problem for us to have going forward.

Operator

Your next question comes from the line of Susan Anderson from B. Riley.

Alec Edward Legg - *B. Riley Securities, Inc., Research Division - Associate*

It's Alec Legg on for Susan. Just to go back on those mini store formats, are you able to provide any details on the type of locations you've targeted? Are they more city centers or suburbs? And then have you looked into mall locations by chance?

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

Yes. So again, we -- the best test example we have is our Madison store in New York City, which is a very neighborhooding store. Certainly, it's still very urban, but it's very neighborhoody. So we're looking at neighborhoods around key markets.

So our first store that we're going to test this outside of New York City is in Palo Alto. But we're looking at San Jose. We're looking outside the main center, but still important centers and both California and New York still very popular states, Texas. We'll see how it goes. Again, we're going to open 3 and see how that works.

We have looked at malls, we continue to look at malls. They are -- they still don't look like they're the answer for us for many different reasons, including they're still fairly aggressive in their cost structure where they want a percent of sales. When there's a lot of really nice retail space everywhere now in the 2,000- to 3,000-square foot space in neighborhoods that we think are going to be better for us financially and perhaps better for us then we'll find out in terms of customer adoption.

Alec Edward Legg - *B. Riley Securities, Inc., Research Division - Associate*

Okay. Very helpful. And then on the new Chicago store, congratulations on that. Are you able to provide how that performed relative to the other 4 locations? And I guess, just the general reception of that store?

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

All right. So yes, I am so glad you asked that question. I happened to be there on the opening weekend. It was the best opening weekend we've ever had for a store, and it was boarded up as most stores still were as a precaution going into the election. I'm happy to say it continues to do very well. The boards are coming off this week. We're just thrilled. It's a great location on Michigan Avenue, our single biggest store under one roof. I think LA has similar square feet, but it's 2 different stores. You have to go outside to get into the other one. So it looks like it's off to a very, very good start.

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

And operator, I think we'll take our last question.

Operator

Your last question comes from the line of Simeon Siegel from BMO Capital Markets.

Simeon Avram Siegel - *BMO Capital Markets Equity Research - Analyst*

Matt, just touching back on your supply demand comment, the high single-digit delta between supply and demand, is that a normal lag you'd expect to run or is that a catch-up? And then any way to quantify how much of the ASP increase was mix versus like-for-like?

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

Sure. Yes, it is entirely a catch-up. Our available supply in the marketplace was down approximately 10% year-over-year throughout the duration of the third quarter. So this really allows us to kind of get back to a normalized state. Now it's not always the case that supply and demand go in lockstep in a given month or even quarter. There are periods of supply build and supply sell-through. But in a normalized state, we have to just kind of play catch-up so that we can, on an annual basis, at least, kind of get back into balance going forward. And then the -- remind me of the second question.

Simeon Avram Siegel - *BMO Capital Markets Equity Research - Analyst*

You can quantify mix versus...

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

Yes. It's mix. It's all mix. It's all mix towards handbags, watches, jewelry and a smaller degree men's, which are slightly higher than average. Like-for-like is...

Simeon Avram Siegel - *BMO Capital Markets Equity Research - Analyst*

Great. And do you have a view on which of these product category mix are pandemic focused versus what might be -- excuse me, longer-lasting trends?

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

I think it's all. To be honest, I think it's all pandemic focused because apparel is slowly coming back, but apparel and fine jewelry and watches are growing, men's is growing. Apparel is still down, although it's significantly better than it was during Q2.

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

Yes. The one exception to that is men's...

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

Oh, in shoes -- wait, shoes are also down. So shoes are more down than apparel. So I think that's somewhat entertaining on a pure level. We expect those categories to return to a more normal rate when people go back to work and get go more and go out more often versus occasions.

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

Right, with the exception that our men's business is still significantly under penetrated relative to the rest of the business. So we would expect to see that continue to grow at higher rates over the next few years than the overall business.

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

And it's growing now. Yes.

Well, that concludes our Q3. The next time we'll be talking to you, it will be on the other side of the holidays. So I want to wish you all a happy and safe holidays, and I appreciate your time today. Thank you very much.

Operator

Ladies and gentlemen, this does conclude today's conference call. Thank you for your participation. You may now disconnect.
