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Q2 2019 TheRealReal Inc Earnings Call

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PRESENTATION

Operator

Good day, ladies and gentlemen, and welcome to The RealReal Second Quarter 2019 Earnings Conference Call. (Operator Instructions) As a reminder, today's program may be recorded.

And now I'd like to introduce your host for today's program, Mr. Paul Bieber, Head of Investor Relations. Please go ahead, sir.

Paul Bieber

Thank you. Good afternoon, and welcome to The RealReal's Earnings Call for the Quarter Ended June 30, 2019. I'm Paul Bieber, Head of Investor Relations at The RealReal. Joining me today to discuss The RealReal's results are founder and CEO, Julie Wainwright; and Chief Financial Officer, Matt Gustke. Julie will provide an update on our business, including progress on a few key initiatives, and then Matt will review our Q2 financial results and financial outlook. This conference call will be available via webcast on our Investor Relations website at investor.therealreal.com.

I'd like to take this opportunity to remind you that during this call, we will be making forward-looking statements, including statements relating to the expected performance of our business, future financial results, strategy, long-term growth and overall future prospects. These statements are subject to known and unknown risks and uncertainties that could cause actual results to differ materially from those projected or implied during this call, in particular, those described in our risk factors included in our financial perspectives for our initial public offering filed with the SEC on June 27, 2019, and the risk factors included in our Form 10-Q that will be filed on or before August 14, 2019. You should not rely on our forward-looking statements as predictions of future events. All forward-looking statements that we make on this call are based on assumptions and beliefs as of today, and we undertake no obligation to update them except as required by applicable law.

Our discussion today will include non-GAAP financial measures. These non-GAAP measures should be considered in addition to and not as a substitute for or in isolation from our GAAP results. A reconciliation of GAAP to non-GAAP results may be found in our earnings release and supplemental materials, which is furnished with our Form 8-K filed today with the SEC and may also be found on our Investor Relations website.

I would now like to turn the call over to The RealReal's Founder and CEO, Julie Wainwright. Julie?

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

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Thanks, Paul. Good afternoon, and thank you for joining us on our first earnings call as a public company. For those new to The RealReal, we are excited to introduce you to our business. For everyone on the call, we are thrilled to share our progress with you and provide you with details on our second quarter financial performance.

Before we proceed, I'd like to take this opportunity to thank our consignors, our buyers and our employees for their help making The RealReal into the world's largest online marketplace for consigned luxury goods. I'd also like to thank our new public market investors as well as our private investors for placing their trust and capital in us.

We are very pleased with our IPO progress and investors' enthusiasm with our market. While our IPO was a major milestone, we believe we are in the very early stages of capitalizing on a massive TAM, which I will discuss in more detail shortly.

First, some quick Q2 financial highlights. We generated GMV of $228.5 million, a 40% year-on-year increase and revenue of $71 million, a 51% year-on-year increase. We are particularly happy about this growth, given that we achieved it while driving significant marketing leverage. Matt will provide more color on our quarterly financial performance later in this call.

Since many of you are new to our story, I'd like to start with a brief overview of what makes us unique, and then talk about a few key initiatives in the second quarter. The RealReal's mission is to empower consignors and buyers to extend the life cycle of luxury goods in a way that honors the luxury brand. We are truly revolutionizing luxury resale by unlocking supply, instilling trust and continuously investing in our technology platform.

Our marketplace provides access to authenticated goods across multiple large categories, including women's and men's fashion, fine jewelry and watches, home, art and kids. Through continuous investment in our technology platform, logistics infrastructure, customer service and people, we attract and cultivate a loyal and engaged consignor and buyer base.

Trust and service are the cornerstones of our marketplace. For our consignors, we make consignment easy and perk to us by providing them with an end-to-end solution, from advising them on the products to consign to in-home pickup, shipping to our warehouse, authentication, copywriting, pricing, photography and pick, pack and ship. Our scale and global reach and the data we leverage from millions of transactions at our marketplace allow us to quickly sell and to optimize pricing for our consignors.

On the other side of the market, buyers trust us because we have a rigorous authentication process. We employ more than 100 gemologists, horologists and authentication experts, who authenticate each item we sell. Buyers are also attracted to our marketplace because the products are exclusive to us and are offered at a compelling price.

Our marketplace benefits from the traditional network effect. The more consignors we aggregate, the more products we get, which then in turn attracts more buyers. However, unique to our model is the flywheel effect. In addition to more buyers attracting more consignors and vice versa, our consignors become buyers and our buyers become consignors. This increases the stickiness and velocity in the marketplace and dramatically enhances the economics of our business by driving down acquisition costs.

Now moving to our TAM. Each year, consumers purchase hundreds of billions of dollars of personal luxury goods. These goods accumulate in their home over time and create an amazing market opportunity for us. Frost & Sullivan estimates the total value in the U.S. alone of luxury goods potentially available for resale is approximately $198 billion. Considering that consumers keep luxury products for on average 5.3 years, this implies the luxury resale market replenishes with $37 billion in additional product each year. With $711 million in GMV in 2018, we are only scratching the surface in terms of the opportunity and believe we have significant runway to grow our marketplace over the coming years.

I'd now like to discuss the progress on a few of our key initiatives in Q2, including the opening of Perth Amboy facility, automation and our retail strategy. First, we launched operations at our 500,000 square foot Perth Amboy, New Jersey facility in the second quarter. We signed the lease on Perth Amboy in the fourth quarter of last year. So we were thrilled to finally begin shipping from there. We are committed to New Jersey and have already hired more than 200 employees in Perth Amboy through June 30. We expect to hire another 200 people in Perth Amboy by the end of the year to scale our operation. Importantly, Perth Amboy doubles our capacity. Our first nontest order from Perth was shipped on April 24 to a buyer and a guest in Georgia. The order value was $493.56, a little trivia for you.

Next, let's discuss automation, which goes hand-in-hand with our ability to scale efficiently. The first step in automating our inbound operations begin in pricing. In the first quarter, we automated approximately 35% of our unit volume. We exited Q2 automating the pricing of 52% of unit volume, and we are on pace to automate 60% to 65% in the third quarter. Importantly, pricing automation has resulted in more consistent pricing and incremental dollars per item. And we have begun automating other parts of our inbound operations, including copywriting and photo retouching. These efforts will support improvements in inbound operation, unit costs and importantly, significantly increase the scalability of our operations.

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Finally, I'd like to discuss our retail strategy. We opened our first store in SoHo in November of 2017, followed by West Hollywood in July of 2018. In May of this year, we opened a small footprint store in New York on the Upper East Side that has 1,800 square feet of selling space and 5,700 total square feet of space. Our retail stores redefine the luxury consignment shopping experience and offer buyers a highly curated selection of products that are refreshed daily. Importantly, all the products in the stores are also available online. We are completely omni-channel. We love our stores as they drive supply in GMV, have high AOVs, low return rates, drive brand awareness and create a halo effect in the local market.

As we highlighted in our S-1, our SoHo store generated approximately $2,500 per square foot of supply and $2,500 per square foot of GMV in 2018. The strong performance has continued in 2019. The West Hollywood store performed very similarly to the SoHo store, and the Upper East Side is also performing well, but it's only been open for a few months. We are excited by the momentum of our retail stores, and we plan to opportunistically expand our retail footprint over the coming years. We will be strategic and judicious with our store rollout strategy. We plan to launch approximately 2 stores per year, focusing on the East and West Coast. If you haven't visited a store yet, we really encourage you to do so.

Now with that, I'll turn the call over to Matt for the second quarter financial results.

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

Thanks, Julie, and good afternoon, everyone. I'd like to echo Julie's comments that we're excited to discuss our results in our first public quarter and to share our outlook for the business.

As Julie mentioned, we generated revenue of $71 million in Q2, a 51% year-on-year increase and GMV of $228.5 million, a 40% year-on-year increase. Before we discuss the details of the P&L, I'd like to start by reiterating how we manage the business financially, and from there, translate that into our results and outlook.

First, we're very proud of our leadership position in authenticated luxury consignment. And as our growth in customer satisfaction have demonstrated, we are addressing a massive opportunity. We are still in the very early stages of capitalizing on this opportunity and are confident that there is much more growth in front of us than behind us. Our primary focus remains on unlocking supply through our unique supply acquisition model that removes practically all of the friction for consignors as well as delivering a superior proposition for buyers. We will continue to invest aggressively in growth through marketing investments, growing our sales team, adding expert authenticators and expanding our operations capacity.

Secondly, as we have always done, we will balance these investments with improving unit economics and operating leverage. We benefit from scale to leverage fixed cost and to drive unit level efficiencies, so our investments in growth are consistent with driving toward profitability. Additionally, we will continue to optimize our spending to drive leverage across all parts of the business.

Third, we will focus on increasing gross profit per order through our average order value, take rate and cost of sales as these increases amplify the leverage of our operating expenses.

So let's discuss the results for Q2, after which I'll provide an outlook for Q3 and the full year. We monitor and measure our business performance using key operating metrics, including active buyers and GMV among others. We believe these metrics are key indicators of our growth and the overall health of our marketplace. I'll spend a bit of time on each one of these metrics before diving into the financials.

Trailing 12-month active buyers in Q2 were 492,000, up 40% year-over-year. Buyer retention trends continue to be very strong. GMV from repeat buyers was 83.1% of total GMV in Q2. We believe GMV is the primary measure of scale and growth of our marketplace. In the second quarter, we generated $228.5 million in GMV, an increase of 40% year-over-year. Trailing 12-month GMV per active buyer was up 1% year-over-year to more than $1,700.

Q2 orders were approximately 505,000, up 40% year-over-year and AOV remained strong at $453. For the first 6 months of 2019, our AOV increased by $2 year-over-year. Q2 AOV reflected earlier-than-expected promotional activity by retailers, which resulted in lower average prices per item sold on a year-over-year basis. This was offset in Q2 by an increase in items per order. And so far in Q3, the impact of the retail promotional environment on resale prices is consistent with prior years, and we anticipate our AOV to increase year-over-year in the third quarter.

At a category level, all of our top level categories experienced growth in excess of 25% year-over-year. Women's and jewelry remain the 2 largest categories and grew essentially in line with the overall business growth. Men's was the fastest-growing category in Q2 with strength in sneakers and street wear. Our Los Angeles store also aided in men's category growth. Returns and cancellations of approximately 27.9% were down 100 basis points year-over-year, driven primarily by a lower cancellation rate.

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Q2 consignment take rate was 36.6%, an increase of 110 basis points year-over-year. This increase was driven by take rate changes in February of this year when we lowered our take rate for certain high-value products and offset that with an increased take rate for items below $145. Notably, we have continued to see strong growth in low-priced supply since we implemented these changes. And as a result of these changes, we expect year-over-year take rate increases in the third and fourth quarters and a modest year-over-year increase in full year 2020 as we anniversary the changes. We also note that take rates can vary from quarter-to-quarter based on the mix of products sold as well as which consignors had item sales. In a steady state, we expect take rates to be highest in the second and third quarters of the year and to decrease in Q4 with a higher mix of high-priced products.

Now moving on to the P&L. Total revenue in Q2 was $71 million, an increase of 51% year-over-year. Revenue growth outpaced GMV by 11 percentage points, primarily due to higher take rates and accelerated 200 basis points as compared to Q1's year-over-year growth.

Q2 consignment and service revenue was $60.7 million, up 44% year-over-year. Consignment and services revenue includes approximately $4.1 million of revenue from shipping fees and our subscription program called First Look. Direct revenue was $10.3 million, up 114% year-over-year. As a reminder, we generate direct revenue when we accept returns from buyers after we have already paid the consignor. In such instances, we recognize the gross proceeds as revenue when the goods subsequently resell.

Q2 gross profit was $46.1 million, an increase of 50% year-over-year. Gross profit per order increased by 7% year-over-year to more than $91. Our consignment gross margin was 71.7%, up 90 basis points year-over-year, driven by a higher take rate. Our direct gross margin was 24.7%, up 500 basis points year-over-year, driven by higher direct product margins. Direct gross margin is lower than consignment gross margin because direct revenue is recognized on a gross basis with corresponding cost of sales. We expect direct gross margins in the high teens going forward, but there could be variability on a quarterly basis.

Moving on to operating expenses. Please note that I will speak about OpEx on a non-GAAP basis, excluding equity-based compensation and related taxes. For a reconciliation to GAAP, please refer to our earnings release. Marketing expense was $11.6 million in Q2, an increase of 26% year-over-year. Marketing as a percentage of revenue was 16.4% compared to 19.7% in the same period a year ago. Importantly, we demonstrated 330 basis points of marketing leverage while delivering 40% GMV growth and 51% revenue growth in Q2.

There are several factors driving our marketing leverage, including: one, buyer retention, 83.1% of GMV came from repeat buyers in Q2; two, network effects within our marketplace, including our flywheel, where buyers become consignors and consignors become buyers; three, optimizing our media mix towards television, TV advertising comprised 52% of our media mix in Q2; and finally, conversion to buyers from our long tail of members.

We expect marketing leverage to continue in the second half of the year, but generally will vary from quarter-to-quarter based on the timing of our advertising spend.

Operations and technology expense, which includes costs relating to our stores, local consignment offices, fulfillment centers, merchandising, engineering and product management was $33.8 million in Q2, an increase of 49% year-over-year. Operations and technology as a percent of revenue was 47.7% compared to 48.4% in the same period a year ago. The improvement was driven by productivity increases in our inbound operations, which more than offset new expenses for our Los Angeles and Madison Avenue stores and our new fulfillment center in Perth Amboy, New Jersey. Our Perth Amboy facility, which opened in May, doubles our fulfillment capacity and currently operates at very low utilization rates. We expect operations and technology leverage to continue in the second half of the year, driven by automation in our inbound operations and the year-over-year anniversary of our L.A. store opening.

Selling, general and administrative or SG&A expense was $24.6 million, up 76% year-over-year. SG&A as a percentage of revenue increased to 34.7% compared to 29.8% in the same period a year ago, driven primarily by investments in administrative function headcount in advance of our IPO as well as other IPO-related spend.

Our adjusted EBITDA loss for Q2 was $20.9 million or 29.4% of revenue.

At the end of the second quarter, cash, cash equivalents and short-term investments totaled $66.7 million. In late June, we raised approximately $321 million in net proceeds from our IPO. The proceeds are not reflected in our Q2 balance sheet as we received the cash in July. Inclusive of IPO proceeds, our pro forma cash balance was $387.6 million at the end of Q2. As a result, our existing business is fully funded.

Before we move into guidance, I'd like to spend some time on path to profitability. Going forward, we expect margin expansion to come from several areas, including top line leverage resulting in higher gross profit per order, variable operating expense efficiencies in all areas of the business and leverage of fixed costs.

More specifically, we expect gross profit per order to increase from improvements in take rate, modest increases in AOV and improved shipping rates over time. We expect variable costs per order to decrease due to marketing efficiencies from sustainable buyer retention and improving buyer acquisition costs and automation and process improvement in our inbound and fulfillment operations.

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We expect fixed cost leverage to be driven by G&A, marketing and technology headcount and rent expense. Fixed cost leverage will be modest in the near term as we continue to invest in our operations, technology and public company expenses, but over time will increase. We expect gross profit, variable expense efficiencies and fixed expense leverage to each contribute approximately 1/3 of our total EBITDA margin expansion toward our long-term target margin.

Now moving on to guidance. We expect Q3 GMV of $233 million to $239 million, representing an annual growth rate of 36% to 40%. We expect our Q3 EBITDA margin loss percent in the range of 28% to 30%. For the full year, we expect GMV of $974 million to $988 million, representing an annual growth rate of 37% to 39%. We expect our 2019 EBITDA margin loss percent in the range of 24% to 25%.

And a few final notes for those building models. Our guidance assumes normal seasonal trends for AOV with a decline quarter-over-quarter in the third quarter before increasing in the fourth quarter. We expect take rates to increase year-over-year in both Q3 and Q4. Our pro forma share count post-IPO was 85.3 million.

In closing, we're pleased to report strong Q2 results and are encouraged by the momentum in our business. We will continue to focus on driving strong top line growth while also delivering margin improvements as we drive toward profitability.

With that, we will open the line for questions. Operator?

QUESTION AND ANSWER

Operator

(Operator Instructions) Our first question comes from the line of Michael Binetti from Credit Suisse.

Our next question comes from the line of Justin Post from Bank of America Merrill Lynch.

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

I guess, one for Julie and one for Matt. And congrats for getting through the IPO process. Julie, just -- I guess, first on supply. Wondering how the sell-through rates were in the quarter, how do you feel about those? And then secondly, what are the key initiatives? I know supply is so important in the second half. Maybe you give us some update on luxury manager headcount and other key initiatives you have in the second half.

And then, Matt, on your guidance, I appreciate the GMV guidance. Any other things we should be aware of that could affect the revenues besides take rates, such as the mix to direct revenue or returns or any other nuances to revenue in the second half?

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

Well, that's a lot, Justin. It's Julie, obviously. So first of all, I don't -- and I'm going to be careful about what we give out and what we don't give out. But our sell-through rates were healthy. As you know, we do control the pricing of the product and we can vary the rates based on trends we see in the marketplace. So -- I mean, we can vary the price. So we had a healthy sell-through rate. Nothing extraordinary or different than what we've seen in the past in Q2.

And then in terms of what we're doing for supply going forward, I think it's worth noting that at least in L.A. and New York, our supply is -- it has a component -- not a significant component, but a component coming from the retail stores, and we did open a small footprint for our Madison that's also contributing healthily to our supply mix. But our supply initiatives are as they've been in the past. We get most of our products, the majority of our products from (inaudible) and home visits, followed by people who send in the products from inside sales. Now we're going to have to put stores as a supply in aggregate as our third source. And then lastly, we do work with some vendors, and that's a pretty small, less than 5% of our total business, for ad hoc product and opportunistic opportunities from that channel. So we actually are really in great shape going into the second half of the year. Certainly, hiring LMs is important to us. We tend to hire ahead of the curve and bring them up to speed. I'm not going to give you the exact number, but we're on track. We feel really good about the second half.

One other reminder for those who maybe are new to our numbers, 80% of our supply historically has come from repeat consignors. Again, we haven't seen any change in the second quarter to indicate that, that won't happen going forward in the second half of the year. So we're pretty excited about our prospects for the balance of the year.

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

Okay. And I'll take the second question. So first of all, thanks for the question. So we guide to GMV because we believe it to be the single best measure of the health and scale of our marketplace. Within that, of course, are some other trends that you have to use to derive to get to revenue, take rate chiefly among them. We have talked about our expectations there.

Other items that can affect revenue, to your point, include our return rate and the proportion of our sales that are from the direct business. Our return rate, we've seen essentially stable year-over-year with a modest decrease in Q2. Typically, we see a slight year-over-year decrease in the third quarter of the year, given the mix of products and pretty much stabilization in the fourth quarter. So that's how I think about that piece. And then direct revenue, as you might recall, was higher as a percentage of the total in Q1 than it was in Q2, reflecting the buildup of the inventory from our holiday return period. So I would expect to see direct sales as a percent of total sales decreased modestly in the third quarter quarter-over-quarter and then a bit more so of a decrease in the fourth quarter as that inventory's basically run through and our seasonal trends quarter-over-quarter are strongest.

Operator

Our next question comes from the line of Michael Binetti from Credit Suisse.

Michael Charles Binetti *- CrÃ©dit Suisse AG, Research Division - Research Analyst*

Congrats on a great start here. And sorry, we had a little technical difficulty there before. Let me ask you, Matt, on the AOV in the quarter. We got muted out for a minute there. You may have said it, I apologize if you did. But -- I think it was down a little bit year-over-year. But I think if I feel my way through the metrics you guys give, that was a pretty big spike in the buyers in the quarter. And I think that -- I think new buyers typically come in at a little bit of a lower AOV. Was that an explaining factor on AOV in the quarter? And does that play into the comments you made for how we think about the back half of the year on AOV?

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

Potentially. So let me just go through -- so AOV was flat year-over-year in the quarter at $453. That reflected average item price decreases across essentially all categories that we trace back to some pretty -- earlier than expected. But as many on the call know, relatively aggressive promotional activity in the retail environment that happened earlier this year than it has in past years and had a depressive effect on resale prices through the quarter. That was offset by an increase in the number of items per order. To your point, when we see prices go down, we tend to see an inverse correlation in new customer growth. So new customer growth tends to be strongest in periods where prices are lowest. Beyond that, I think we saw in the quarter and quarter-to-date in the third quarter, very strong trends surrounding and post the IPO in terms of leading indicator metrics for both supply and demand, whether it's traffic growth or membership growth or new consignors, new buyers. Very encouraged by the trends we saw in the quarter and subsequent to it.

Michael Charles Binetti *- CrÃ©dit Suisse AG, Research Division - Research Analyst*

Okay. One other just small modeling question, a little more on maybe on the direct gross margin, why that was up so much in the quarter? I know you gave us some thoughts on how to think about it for the rest of the year. I'm curious if there's any fundamental change that you saw in the quarter that might have caused what looked like an unusual number. But on -- maybe on a more fund basis, this maybe a jump ball between Matt and Julie, but that was some very rapid improvement in the pricing automation line that you called out, Julie. Can you walk us through maybe some of the initiatives there? And then where we'll see that manifest itself? Is that -- on the P&L, is that number keeps moving up for the year?

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

Sure. So look, pricing is just one component of what we do. It is one that we actually have -- we can get top line leverage far and consistency. So when we automate pricing, we tend to have slightly higher prices. And it's better for the consignor and it's better for us, obviously.

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So look, pricing, we think -- by the end of the year, we're going to be over 60% of products being auto priced, but we have other initiatives underway. And I think I mentioned some of those, so let's reiterate some of them. We have automatic copywriting. We have automatic -- while we're working on some things in the gemology area, but there are things that we're working on to further -- it's actually the copywriting and we're seeking process to streamline it. Over time, this will appear in the operations part of the P&L. This year, the impact will be a little hard to really understand the true impact because it's being layered on layer. And -- but I would say, next year, you'll start seeing a nice impact.

We're also testing and have had really good results with automating retouching. The retouching component, which is about $1.10, just to break it out specifically for you. If we send it out -- most of it's sent offshore, that we can eventually get to 80% of it automated, but we're running some really good tests now. Quite a bit of it's been automated. We get 2 benefits from that. Certainly, long-term lower costs in our operations units, but it also speeds up time to get on the site. Sending products offsite for retouching, which is mostly color balancing and cropping can add up to 3 days of incremental time, so we're going to get 2 benefits as we roll that out. But again, we're in early stages. As you can appreciate, we test everything before we roll it out in a larger way to make sure that both the sell-through rate is unchanged or enhanced and customer services, also calls go down not up. So we make slow but steady changes, and we're very judicious before we roll it out in a mass way.

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

Yes. Just to add to that briefly. So those improvements as well as several process improvements within operations allowed us to demonstrate leverage in the ops and tech line despite significant investments in technology, in our warehouse infrastructure and so forth. So that's going to be kind of representative of how we think about it generally going forward, balancing investment with leverage overall.

And to your question about direct margins, there's no particularly special story about what happened in the second quarter. It's a bit random. The number is relatively small in the grand context of things. It's about $10 million in actual sales. I think what happened essentially in the second quarter, like with the rest of the business, we had lower price points being sold. And the lower price points correlate with a higher take rate, so to speak. In the case of direct sales, that's a product margin equivalent. So it's just a bit of randomness within the business. We think, over time, that should stabilize in the high teens. You could see a breakout quarter that's in the mid-20s. You can see one that's kind of in the mid-teens. But generally speaking, it's going to bounce around, but we think direct sales as a percent of the total business should be steady to decreasing over time. It's not something that we are certainly actively trying to increase.

Michael Charles Binetti - ***CrÃ©dit Suisse AG, Research Division - Research Analyst***

Okay. Congrats, again.

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

Thanks.

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***

Congrats on the IPO and a great first quarter out of the gate. I guess, first, I know you spoke a little bit about promotion. I know though that a lot of your categories and products are probably not impacted by promos. Could you maybe ice a little bit more where you saw the biggest impact and ready to make pricing adjustments?

And then second, as it relates to marketing expense, obviously, nice leverage there. As we think about the medium term, how should we think about marketing expense leverage? And what other opportunities you have to take that cost down?

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

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So I'm going to start, and then -- this is obviously, Julie, and then Matt will kick in. So we've -- the promotional impact of discounting, mostly from department stores, is not new to us. They did start earlier this year. But as Matt indicated, we've already seen recovery fairly fast. And where it impacts us the most is in the apparel category and specifically women's apparel category. Some products do not actually have a big impact, and those tend to be fine jewelry and watches and some of the street wear. So we have seen this before. It was earlier. I know other people have indicated they thought it was deeper. We actually felt it was earlier, but not deeper. And as we said, we did recover. And it is something we balance all the time. We balance the tension between full price, discounted things and resell. So we're in pretty good shape going forward. I would say if department stores get desperate in September, October, we might have some of that tension. Again, that'll be offset by high seasonality. So this is one of the beauties in our diverse product line. This is one of the beauties of having product diversity because we don't see it in fine jewelry watches, men's and street wear and even women's handbags. So we feel pretty good about where we're going, and we're doing really well so far in Q3 again.

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

Okay. Yes. So I think that pretty much covers the promotional question. So I'll speak a little bit about marketing leverage. So one of the beauties of marketplaces in general is that once they get to a certain level of scale, you can sort of count on network effects to support growth. We certainly have that in abundance, amplified by what we call the flywheel effect of buyers becoming consignors and specifically, consignors becoming buyers in the equation of buyer acquisition costs and that continues. So the proportion of our consignors who are becoming buyers has been consistent. That conversion has been consistent.

At the same time, our ongoing media mix bias towards television continues to generate very healthy returns for us, not only in terms of generating high numbers of new customer growth, but doing so at a very low cost relative to our other paid channels and with very productive users who happen to also align with the existing demographics of our buyer base. So growth in the right areas at the right cost. We see quite a lot of runway ahead of us there.

On top of that, nearly half of our new buyers in any given period are actually converting out of our -- the member base that we have accumulated prior to that period. So right now, actually, our membership base is growing. I won't say exponentially, but it's growing very quickly. It could be to some degree around an IPO halo effect around the business. But that -- as that base builds, that will just kind of create a pull for us to convert for many quarters to come. So those effects together, we would expect to see continuing driving marketing leverage. That said, we're going to be -- 2 things. One, expect quarter-to-quarter variability in our marketing spend, just based on the timing of when we choose to spend more heavily and less heavily based on the ROIs that we anticipate. And we may be opportunistic and elect to invest more aggressively to accelerate or to just underscore both supply and demand growth. But I think you can anticipate embedded in our guidance is no real significant change in terms of leaning in, in the near term, but rather continuing to see rather healthy growth rates of year-over-year marketing leverage.

Operator

Our next question comes from the line of Scott Devitt from Stifel.

Scott William Devitt *- Stifel, Nicolaus & Company, Incorporated, Research Division - MD*

One for Julie, one for Matt. First, Julie, you talked a bit about the promotional activity in the quarter and impact on the business. And interestingly, the business still grew very nicely despite that in terms of lower prices being offset by more items per order and more buyers. And so just taking a step back and kind of understanding that promotional activity, department store closures and things like that are going to be an ongoing industry dynamic going into the future. And just how you think about that in terms of the way it impacts the business, if at all, if the positive, negative or a total nonevent?

And then secondly, for Matt, square footage, I think you're up to roughly 1 million square feet now. If you could talk a little bit about capacity utilization, where you think you're optimized and when you'll think you'll need the next facility in the future?

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

Okay. Let's go back to promotional activity. So again, I want to underscore that this is not a new phenomenon for us. And because -- there's 2 factors going on with our business. We want to get the absolute highest price for the consignor but also for us, but we also want to sell-through items. Some items are more vulnerable to a tension between department score -- department store discounting and those tend to be actually contemporary and mid-tier luxury brands, which are the ones that get discounted most heavily during this time. And so there is a tension between what price we can charge versus the discounted new price. That's something that we're always pushing up and testing the limits.

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Actually, though we saw a promotional effect, and it did happen earlier, the truth is we're actually discounting less on quarter-on-quarter than we have in previous times, and that's because we've gotten more sophisticated in the way we do it. Again, this is where diversity of products serves us. So going forward, we feel like we've got enough flexibility in our business model and discipline around our pricing and our -- and the way we actually view pricing versus sell-through to do an accurate prediction of what's going to happen. Now certainly, extraordinary things can happen, but we have been there before. I think 2013 and '14 were particularly bad. And we maneuvered, and we've gotten more sophisticated and our product line has gotten more diverse since then. So we feel pretty confident about our ability to ride out the storms that are in front of us, especially when it comes to -- and again, it's primarily department card discounting of women's apparel.

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

Yes. Nothing to add to that. So I'll take the other question around just our general capacity within our e-commerce centers. So as you correctly noted, so we added about 0.5 million square feet in May, that doubled our capacity. So if you think about it differently, it means that first $500,000 got us to about $700 million of GMV, which is what we achieved in 2018. So you should expect that the next DC will give us about that much growth capacity. So I won't be overly precise about that, but think about it plus or minus 2 years of growth, after which we'll need probably another one of about the same size.

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

And just underscore -- one other thing on that. And of course, we'll have to bring it on before we need it. Otherwise, it makes very unhappy employees. So -- and it usually takes us 4 to 6 months to ready a warehouse to make it condition ready, so we can conduct business.

Operator

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

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

Congrats on the quarter. A couple of questions. First, if you can just talk maybe about customer demographics and how you see that evolving? And also maybe just some traction with some of the -- based on the newer verticals, including men's, home and other.

And then maybe for Matt, just on the services revenue, how we should think about that going forward? And kind of what the trends in First Look subscribers?

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

So on the demographics, we are -- this year, we had a changeover point where millennials and younger became the single largest group of buyers and consignors. That's still getting stronger. I mean, part of that's just the millennials are also getting older and they are getting richer. So the consignor base is shifting along with the buyer base. So -- and part of it's our media mix. So that trend is continuing, and I would expect it to continue. And also, we did change our media mix and television along -- well, any television along with OTT has really helped.

So the other thing you should know is that by increasing our -- well, sorry, let me back up. Our base has also gotten more male and that's gone up slowly, but that's also driven by more male consignors, and we certainly have seen that growth pretty substantially this year. It's our fastest growing. It's still fairly small as a percent of our total category, but it is the fastest growing. So when you -- this is no surprise. You have the more male consignors, you have are the more people consigning men's street wear in particular or men's clothing, the more men you're going to get on your site. And we've seen that rise fairly steadily. We're pretty excited about that. But I think it's really key to say that we do still appeal to a really broad demo. I do want to reiterate this. There is an idea that -- we've heard people say everyone's rich. In fact, 50% of our buyer and consignor base have an income under $50,000, so we're attracting a younger, more vibrant group. And certainly, 50% are above it. So we still have a broad demo. I don't know if that answered, but -- sorry, Paul Bieber just said it was $100,000. Sorry, 50% are above $100,000 and 50% are below $100,000.

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

Got it. That's great.

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

And did you ask about new categories? New categories...

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

Yes. The new categories. I think you commented about men. And then just on the services revenue outlook.

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

Well, men's is -- it is the fastest growing. We're not giving out the exact breakdown. We did it in the S-1, but it actually continues to grow. Growth's a little slower. But in terms of the overall mix, it's getting more important for us. Home and art is fairly steady. So it's growing the rate of the business, but not beyond that. And certainly, men's is growing faster.

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

Yes. And for those of you who are less familiar. So our men's business is a relatively small proportion of the total single-digit percent of our GMV, growing significantly faster than the overall business. Certainly, the trend towards street wear and sneakers has helped our business quite a bit as well as the rollout of retail stores, particularly our store in Los Angeles that has helped actually dramatically change the growth rate of our male consignor and buyer base in the overall category.

And I think you also had a question about other revenue. I'm afraid there's not much more to get into there. The lion's share of the other portion of revenue is shipping fees that we charge to buyers, and that's going to be relatively consistent per order going forward. First Look, for those of you who don't know, is a program that we have that allows buyers primarily -- the primary benefit is earlier access to products that are newly launched to the site 24 hours before they are available to the general public. It's a very small source of revenue, but an important benefit to our customers who very much crave what is newest and hottest. And a nontrivial amount of our business is sold of the items that are [reposted] to the site within the first 24 hours.

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 2 follow-ups on the store strategy broadly. Now that you're getting some real experience with what these stores do to both drive the flywheel and more specifically drive supply, how do you think about investing against the store strategy, going faster, moving along at sort of a steady pace that we've talked about in the past? How might what you see in that strategy play out over the next 6 to 12 months, change or more from maybe some of the investment strategy you think?

And as you see more of these stores pop up, are there secondary benefits where, from a branding perspective and a marketing perspective, there could be incremental layers of efficiency in the model because the store gives you a more physical presence and drives more awareness and drives more supply into the store? And therefore, maybe you have to -- you don't have to run as fast on the treadmill on the marketing side to drive the same level of flywheel effect? So I would love you to go a little bit deeper on both those topics.

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

Sure. I'm going to start, and then I'll kick it over to Matt. We actually don't have any change right now. And our plan -- our goal is to rollout 2, maybe 3 stores a year, but most likely 2 stores per year. We're waiting for the right location, the right build-out cost, the right rent, so we can actually roll them out efficiently.

We do not need the stores for growth, but they are a good brand reinforcer and they've proven to be also a good source of GMV as we've said before. We only have one store that's been around for now -- I mean, L.A. is just about ready to lap itself and it just did. And then the SoHo store has been open 18 months. So it really wouldn't be judicious of us to continue to rollout multiple stores.

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I will call out that we're still testing a little bit. The store in Madison is a much smaller footprint store. And we want to understand that impact, so we can put that in our mix for potential either the second store in a market or smaller markets. But you can expect a store to rollout in the first quarter of next year. And again, we're going to do it. We're going to take it slowly. We're in no hurry here. And we're just starting to understand the impact of awareness. The other thing I want to call out. You talked about marketing efficiencies. We're getting great marketing efficiencies independent of the stores. And so we wouldn't need the stores to achieve our economic model on a increasingly marketing-efficient business.

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

Yes. Just to add to that on the pace of investment stores. To Julie's point, our stores are so new as a portfolio that they -- we just really need more time just to get more experience, more data and watch the cohorts of consignors and buyers who roll through the store as well as the halo effect in the markets in which the stores operate before we were to do anything different. So certainly, not next year would we deviate from the plan of approximately 2 new stores. If the existing stores and those new ones continued to perform like they do or even improved their performance, we'd reevaluate at some point down the road, but we'd do so only in the context of our overall drive toward profitability. We wouldn't use a retail store expansion to deviate material from that.

Second -- on the question on marketing, yes, absolutely right. The stores are great drivers of awareness and support our overall marketing efficiency. So over time, that -- it absolutely does take some pressure off of continued increases in efficiencies in our overall marketing investment. So you can think of it as sort of a portfolio of assets that is driving awareness and ultimately, acquisition and retention of the base of consignors and buyers.

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

We have time for one more question.

Operator

Our final question then comes from the line of Oliver Chen from Cowen and Company.

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

Regarding take rate, what are your thoughts on the dynamics there in terms of the long-term benefits, whether that be mix or like-for-like? And also, I would love your thoughts on agility that you have and the levers that you can pull if the environment and competitors discount more than you expected. What happens like in terms of your response and what you can do within your control?

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

Go ahead.

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

So I'll start on take rates. So I haven't no time for a dissertation on our take rate philosophy. But in general, the core of our commission structure to consignors is a tiered structure, whereby the more that a consignor sells, the higher rate that they earn. And that's a very important driver of consignor retention and loyalty within our ecosystem. On top of that, we've layered a number of exceptions on both the high end and low end simplistically. So a lot of certain higher-priced products like watches and handbags and sneakers will get a commission incentive, so we'll take a lower take rate on that. But the prices are so much higher that the actual net to us in terms of revenue and gross profit on that transaction is still very healthy. We've subsidized that and offset that -- more than offset that with increases in take rate on the low end of the spectrum. So currently, we have a 60% take rate on items under $145.

So that's how we think about the blend. And we're always thinking about the best ways to optimize both sides and the totality of the system, so that we can balance supply and making sure that we're getting the appropriate mix of products across categories and price points, and we'll continue to do that over time. And at the moment, we are

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competitive across every category and every price point. So we are able to do that and being multi-category has a lot of benefits, one of which is the ability to react to a competitive environment on things like pricing and take rates in the context of our broader strategy.

And then on the question of agility and what can we do, well, the good news is our costs are not fixed on products. So the beauty of a marketplace model is that we're going to get the same percentage of the transaction in our revenue regardless of the price. So we have, to some extent, a partial hedge against that environment. But to the extent that we see a sustained heavy promotional environment, I don't know that it can get, frankly, much more sustained and significant than what we've seen over the past year. So I think we've been through that. And what we've learned, to Julie's point, is being diverse across categories is our best weapon. The depth of promotional activity tends to be really focused on women's apparel, which is our single largest subcategory, but pretty much everything else has a lot of insulation around pricing, whether that's handbags or jewelry or watches or men's products. So the more that we diversify our product mix, less susceptible we are to those pressures.

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

And then one last thing on the -- on what's going on with take rates on the category by category level. Look, people -- the easiest way for any competitor to get into a market is to offer a greater -- give the consignor more money. The issue then becomes can you sell-through that item or will you end up paying them out? So their cost structure is going to be inverted, which, again, especially if you're focused on a single category, our breadth across categories does give us incredible flexibility. And our incentives for a consignor to stick with us, meaning the more you make, the more you get to stay at that level the next year also helps keeps consignor repeat rates as high as they are.

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

That's very helpful. Just a quick follow-up on the unit -- the per unit dynamics. Does that interplay with fulfillment and handling costs in terms of how that fluctuates and just needing to touch more items through your system or not so much?

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

If I'm following your question, it's around the number of items in an order increasing and does that have an impact on other costs? Is that the question?

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

Yes. Because sometimes, in companies as the number of units increases and their AURs go down, there's more logistical costs than you previously expected in handling.

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

So first of all, kudos to you for getting one extra question. And we said it's the last one. And secondly, yes, there is obviously a cost. However, we have so many -- so much work on our operations by process optimization and then automation in key areas, it is actually -- we're able to balance that at this time and we feel really good about us showing more leverage in that area than deleveraging in that area.

All right, guys. I think that's it. Do I get to make my closing? Thank you very much to all for joining us on this call. We're excited about our results in Q2. We're looking forward to talking to you again to report Q3 results. The other thing I want to thank, of course, the employees, which work very hard at The RealReal and our consignors and buyers. So with that, I think we're closing out the call.

Operator

Thank you. And thank you, ladies and gentlemen, for your participation in today's conference. This does conclude the program. You may now disconnect. Good day.

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