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The Children's Place, Inc. (PLCE)

Q4 2018 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Ladies and gentlemen, thank you for standing by and welcome to The Children's Place Fourth Quarter and Fiscal Year 2018 Earnings Conference Call. This call is being recorded. If you object to our recording of this call, please disconnect at this time. All participants have been placed in a listen-only mode and the floor will be open for your questions following the presentation.

[Operator Instructions]

It is now my pleasure to turn the floor over to Anthony Attardo, Director of Investor Relations, to begin.

Anthony Attardo
Director, Investor Relations, The Children's Place, Inc.

Good morning and welcome to The Children's Place conference call. On the call today are Jane Elfers, President and Chief Executive Officer, and Mike Scarpa, Chief Operating Officer and Chief Financial Officer. The Children's Place issued press releases yesterday morning and copies of the releases and presentation materials for today's call have been posted on the Investor Relations section of the company's website. After the speakers' remarks, there will be a question-and-answer session. [Operator Instructions]

Before we begin, I would like to remind participants that any forward-looking statements made today are subject to the Safe Harbor statement found in this morning's press release as well as in the company's SEC filings, including the Risk Factors section of the company's Annual Report on Form 10-K for its most recent fiscal year.

These forward-looking statements involve risk and uncertainties that could cause actual results to differ materially. The company undertakes no obligation to publicly release any revisions to these forward-looking statements to reflect events or circumstances after the date hereof. After the prepared remarks, we will open the call up to your questions. We ask that each of you limit yourself to one question, so that everyone will have an opportunity.

And with that, I'd like to turn the call over to Jane Elfers.

Jane T. Elfers

President, Chief Executive Officer & Director, The Children's Place, Inc.

Thank you, Anthony, and good morning, everybody. 2018 was the foundational year of our three-year plan with accelerated digital investments laying the groundwork for operating leverage in the out years. After we provided our original guidance in March, significant strategic competitive opportunities arose that led to the decision to sacrifice margin in the near term in order to strengthen our long-term position.

We shared with you our strategy to compete aggressively against key competitors with a focus on long-term market share gains. We believe that the recent bankruptcy announcements and accelerated store closings once again provide validation that our forward-looking strategy was on the mark. Although the results from 2018 will extend the timeline to achieve our objectives initially targeted for 2020, the strategic steps we took in 2018 increase our brands' longer-term potential earnings and facilitates the path to get there.

Now, let's discuss the recently announced agreement to purchase the IP assets of Gymboree and Crazy 8. Our winning bid at the auction for the Gymboree Assets provides us with another catalyst for transformative growth for The Children's Place and value creation for our shareholders. Acquiring the Gymboree Assets will give us the opportunity to exercise greater control over our ability to capture a larger portion of the estimated $600 million of market share left behind by the total liquidation of Gymboree and Crazy 8.

We believe this acquisition will provide us with a path to revitalize the Gymboree brand across channels, including e-commerce, TCP stores, wholesale and international. The Gymboree customer base is intensely loyal to the brand. They are passionate about the highly curated, elevated head-to-toe product that is Gymboree's core DNA and she has made it known how much she misses that legacy Gymboree product due to the recent merchandising changes.

As we discussed on our second quarter conference call, after seeing the new Gymboree product that was introduced in July of 2018 and reading the customers' reaction to that product on social media, we designed and produced a limited assortment of highly curated, elevated head-to-toe toddler product to address this void. This new product will be available on our website and in over 200 of our stores beginning in May 2019.

We recently posted some images of this new product on our Facebook page and the customer feedback has been very encouraging. This product will initially carry The Children's Place label, but our plan is to rebrand it to the Gymboree label starting in early 2020. We believe that the acquisition of the Gymboree brand and its legacy strength in the toddler sizes will provide us with a unique opportunity to expand our market share in this important size range.

The ownership of the Gymboree brand and IP will reinforce and expand the market opportunity, as it will allow us to tap further into the DNA of this product and attract new customers to The Children's Place in a number of channels of distribution. The brand will provide us permission to operate in segments of the market that were previously unaddressable at TCP.

As a reminder, we accelerated approximately $30 million of our planned $50 million of incremental digital transformation spend into 2018 with a heightened focus on building our digital personalization capabilities in 2019 and beyond. The Gymboree Mom, like The Children's Place Mom, is digitally savvy and shows a preference for omni-channel shopping experiences and we are now better prepared to bring these customers into our digital ecosystem.

Our work in connection with the acquisition process provided us with a detailed analysis of Gymboree's real estate portfolio and presented us with additional insights on how to maximize the productivity and profitability of our existing locations in colocated centers and a clear view into potential new centers that may offer upside potential.

We have already identified sites to be addressed and have started to execute on a real estate plan, which will add incremental sales and profits to our accretion forecast over time. As we execute upon the Gymboree market opportunity, we anticipate the acquisition will be accretive to our earnings beginning in 2020, following low-teens percentage dilution in 2019 as we make incremental investments to support the strategic opportunities for the brand across various channels.

Moving on to Q4, in 2018, we recognized that our closest specialty competitor was distressed and with our stores overlapping nearly 70% of their approximately 800 remaining locations, we were presented with unique market share opportunity.

Accordingly, we made the strategic decision to sacrifice short-term margin to strengthen our long-term position. Gymboree's recent bankruptcy announcement validates that our strategy was on the mark. When we last updated investors in early December, we discussed a solid start to the holiday season in November following a very strong October, which in retrospect may have pulled forward some weather-driven demand from December.

Despite the solid start, we felt it was prudent at that time to discuss the high likelihood of further distress for TCP and the potential for unprecedented near-term competitive pressure as presenting a meaningful risk to profitability. At that time, our near-term visibility was clouded by a lack of clarity on the scope and timing of the competitive closings, which added significant complexity to forecasting the fourth quarter.

After the holiday, news of Gymboree's intention to completely liquidate its Gymboree and Crazy 8 brands intensified. This provided us with the additional insight needed to determine how to best position ourselves into 2019.

Based on this new information, we took strategic action in the fourth quarter to significantly accelerate the liquidation of our seasonal carryover inventory in response to Gymboree's plan to liquidate all of its stores in a compressed Q1 timeframe.

We have never experienced a total liquidation of a direct competitor of this size in proximity. So, we are in uncharted territory. However, we believe that our ability to liquidate our seasonal inventory in the normal timeframe of February and early March would be severely compromised by the potentially significant traffic pullback in Q1 caused by the compressed Gymboree liquidation event, delayed tax refunds, the potential for unseasonable weather and a later Easter.

Taking all these factors into consideration, we made the decision that liquidating carryover inventories into stronger seasonal traffic during the post-Christmas period and prior to the full-blown Gymboree liquidation in Q1.

Although this accelerated liquidation adversely impacted our fourth quarter EPS, it allowed us to minimize the adverse margin impact that we would have otherwise experienced had we attempted and potentially failed to liquidate our seasonal carryover product in Q1 during the Gymboree liquidation. This accelerated liquidation strategy enabled us to exit the quarter with over 50% less seasonal carryover inventory versus last year, with total inventories down 6.5% versus our guidance range of flat to up low-single digits.

Our lean inventory position allows us to focus on moving through our spring seasonal product in what we anticipate will be a highly volatile first half of 2019. We are anticipating that the first half of 2019 will be a highly disruptive period for us as the number of overlapping Gymboree stores and compressed time period within which they are liquidating, together with a very late Easter and the potential for pull-forward of demand from Q2 into the Q1 liquidation event, creates unprecedented challenges.

It's important to highlight that The Children's Place is influenced by the Gymboree and Crazy 8 liquidations meaningfully more than others because of the significant overlap between our two businesses. We currently estimate that we have store overlap with 61% of the approximately 534 Gymboree brand locations that will close and 80% of the approximately 264 Crazy 8 locations.

Neither TCP nor Gymboree compete heavily in newborn with only modest mid-single-digit exposure to the category. We both do the lion's share of our business in toddler, big kids, footwear and accessories. And as a result, we have much greater exposure to the disruptive impact of the Gymboree closures, but we are also much better positioned to capture the market share benefit beyond the closings.

We see 2019 as a tale of two halves. Near term, we expect to be negatively impacted in the first half of 2019. We currently estimate an adverse impact from Gymboree's liquidation event in the first half. Our expectation is that their Q1 liquidation sales will draw demand forward from Q2 putting further pressure on a quarter where we are up against a 13.2% comp from last year.

We anticipate seeing the benefits from the Gymboree liquidation beginning in the back half of 2019. We also expect added market share benefit from record supply release in the children's apparel segment as other distressed retailers continue to close doors.

Moving on to additional market share opportunities, we don't think of the recent bankruptcies as isolated events that will shift to the rear-view mirror. Rather, we consider these events to be part of a longer term and significant shift in the competitive children's landscape. We see market share gains as an annuity that is anticipated to live long beyond any single troubled competitor.

As we indicated on our Q3 call, we estimate the market share opportunity from a collective group of ill-positioned retailers is meaningfully larger than any single player like in Gymboree or Sears. We anticipate this group of capital-constrained, poorly-positioned and/or over-stored retailers will continue to be forced to consolidate and shutter doors and if we continue to successfully execute on our long-term strategy, the current market presents The Children's Place with significant and ongoing market share opportunities.

Moving on to AUC, you've heard us frequently discuss our AUC or product cost advantage. We project that our AUC will be down in 2019 while others will be raising their prices. Our strategic focus on AUC provides us with another competitive advantage that allows The Children's Place to outperform in all economic environments. We believe our AUC profile allows us the opportunity to offer the millennial consumers a quality product at great value versus our competitors. This AUC advantage allows for greater margin and cash stability in more difficult economic or competitive climate.

The relative strength allows us to invest as others are harvesting, which enhances the share gain opportunity, provides us with relatively stronger returns in cash flows and the cycle repeats. Competing with a relatively lower AUR also allows us to gain share in difficult economic periods. This was evident in prior recession periods when Children's Place comped positive low-single digits as other retailers posted low-single digit declines.

In good economic times such as the last several years, we posted some of the strongest comp gains in the specialty retail sector. As we continue to execute our decade-long sourcing strategy of country migration and vendor consolidation, our product costs are anticipated to continue to mix lower, which reinforces our AUC advantage.

Moving on to digital transformation, let's review our progress on our digital transformation initiatives in Q4 and share with you what we are working on for Q1 and beyond. Our digital business continued to lead in Q4 as we delivered over 20% growth on a comparable week basis in the quarter and continued to provide our millennial mom with a stronger omni-channel offering. E-comm penetration increased 500 basis points to 28% of net sales in Q4 versus 23% a year ago.

Our outsized digital growth is fueling our loyalty and private label credit card programs, which are key to our digital transformation. The significant momentum we're seeing in our digital business in 2018 gives us continued confidence in achieving a mid-30s digital penetration by 2020.

We believe that our competitive advantage is starting with our time-tested strategic management of our business, our best-in-class product, our lower AUC profile, less competitive supply and the tapering off of incremental digital investments combined with an improved digital strategy and an optimized door footprint provide us with the tools necessary to take advantage of the looming market share opportunities in 2019 and beyond.

We understand the power of our peer-leading ROIC and the cash flow opportunities it provides us to enhance shareholder return, including the recent ability to acquire the Gymboree Assets when the opportunity presented itself.

Now, I'll turn it over to Mike.

Michael Scarpa

Chief Operating Officer & Chief Financial Officer, The Children's Place, Inc.

Thank you, Jane, and good morning, everyone. Following a discussion on the agreement to acquire the Gymboree Assets, I will provide an update on our fourth quarter financials and our outlook for 2019.

First, let's discuss the transaction. We are excited about the Gymboree transaction and the opportunity this provides us to drive accelerated growth and value creation. As detailed in the press release, we have agreed to acquire, as part of an auction held in connection with Gymboree's bankruptcy proceedings, the Gymboree and Crazy 8 intellectual property and related assets for $76 million in cash. The acquisition is being funded by cash on hand and borrowings under our revolving credit facility. The acquisition will not disrupt our share repurchased (sic) [repurchase] or dividend plans.

I'd like to provide some additional context regarding the financial implications of the deal. The acquisition of the Gymboree and Crazy 8 IP and databases will provide us with the opportunity to more than double our previously targeted market share opportunity by leveraging TCP's digital and physical infrastructure. We anticipate the incremental sales will flow through at attractive incremental margins and drive earnings accretion and cash generation beginning in 2020.

The acquisition of the Gymboree Assets will also enhance the flexibility we have with our fleet optimization program. As Jane previously mentioned, the acquisition process provided us with a detailed analysis of Gymboree's real estate portfolio. The analysis presented us with additional insights on how to maximize the productivity and profitability of our existing locations in co-located centers and gave us a clear view into potential new centers that may offer upside potential.

We are already leveraging our deep relationship with the mall landlords and executing a plan, which allows us to pursue an additional 25 TCP locations over the next 24 months to take advantage of the void left in those markets where Gymboree has closed.

It's important to stress that we are not adding net square footage to our corporate store base. We remain a net closer of stores. This is purely optimization of our fleet to achieve higher returns. The acquisition will provide us opportunities across various channels, including e-commerce, TCP stores, wholesale and international.

It is anticipated that the acquisition will be accretive to adjusted earnings per share beginning in 2020, following a low-teens percentage dilution in 2019 as the company makes incremental investments to support the strategic opportunities provided by the Gymboree Assets and funds the acquisition.

I'll now provide an update on Q4 results and discuss our forward outlook. In the fourth quarter, we generated adjusted EPS of $1.10 versus $2.52 last year. Our adjusted EPS versus last year was adversely impacted by four main factors. One, our strategic decision to accelerate the liquidation of seasonal carryover inventory ahead of Gymboree's first quarter liquidation event resulted in an adverse impact of $0.79 per diluted share. Two, store traffic declines and lower conversion rates in the weeks leading into Christmas resulted in an adverse impact of $0.30 per diluted share.

Three, higher fulfillment costs as a result of higher freight expense associated with our unplanned ship from store activity, along with higher distribution center wages paid as a result of labor shortages, resulted in an adverse impact of $0.25 per diluted share. And four, an adverse impact of approximately $37 million in sales resulting from the calendar shift related to the 53rd week in the fourth quarter of 2017 resulted in an adverse impact of $0.12 per diluted share.

Details for the fourth quarter are as follows. Net sales were $531 million versus last year's $570 million, down $39 million or 6.9%. Last year's additional week in the fourth quarter accounted for an additional $37 million in sales. The new revenue recognition rules accounted for approximately $6 million in sales. We recorded a slight decline in comp retail sales of negative 0.6%. U.S. store comps were a negative 8.2% in the quarter, with traffic down 3%.

Traffic was meaningfully lower in the weeks leading up to Christmas, down 11%. Transactions and conversions were also down as a result of inventory imbalances from our unplanned ship from store activities.

In Canada, where traffic was relatively flat throughout the quarter, comps were relatively flat. Our e-commerce business performed well, with sales up 20% on a comparable week basis.

Gross margin; adjusted gross margins declined 550 basis points to 31.5% of sales from 37% in Q4 of 2017 from the combination of the decision to accelerate the liquidation of seasonal carryover inventory ahead of Gymboree's first quarter liquidation and weaker-than-expected sales in the weeks leading up to Christmas.

Our inventory clearance strategy resulted in approximately 290 basis points of margin pressure in the fourth quarter, but will help us limit our inventory exposure and minimize the adverse margin impact that we would have otherwise experienced had we attempted to liquidate the product in Q1. Gross margins were also adversely impacted by the increased penetration of our e-commerce business and the deleverage of fixed expenses resulting from a modest decline in comparable retail sales.

As discussed in our third quarter call, our fourth quarter distribution cost adversely impacted margins by $5 million, or approximately 90 basis points, and revenue recognition had a $6 million impact on margin in the quarter.

Adjusted SG&A; adjusted SG&A was $128 million versus $134 million last year and deleveraged 60 basis points to 24.2% of sales. This was the result of fixed cost deleverage based on lower-than-expected comps and $6 million related to the reclassification of certain items due to the new revenue recognition rules, offset by lower incentive compensation expenses.

Adjusted depreciation and amortization was approximately $17 million in the quarter. Adjusted operating income for Q4 2018 was $22 million or 4.1% of sales versus $57 million or 10% of sales in Q4 2017, down 590 basis points, predominantly due to lower gross margins as previously discussed. Our adjusted tax rate in the quarter was 15.4% versus 20.7% last year.

Moving on to the balance sheet, our cash and short-term investments at the end of the year were $69 million as compared to $260 million last year, reflecting the impact of $190 million in cash repatriated in 2018, which was utilized to fund our accelerated share repurchase program and working capital. We ended the year with $49 million outstanding on our revolver compared to $21 million last year.

Our inventory was down 6.5% at the end of the year, which was significantly lower than our flat to up low-single-digit guidance as a result of our strategic decision to accelerate the liquidation of our seasonal carryover inventory ahead of the Gymboree Q1 liquidation event.

Our seasonal carryover inventory is down over 50% versus Q4 of 2017 as we strategically positioned ourselves to move through our spring seasonal inventory in the first half of 2019. We are anticipating to exit Q1 with inventories flat to last year.

Moving on to cash flow, we generated $140 million in operating cash flow in 2018 despite meaningful margin and incremental digital transformation investments being made in the business throughout the year.

Capital expenditures in the quarter were $16 million and $71 million for the year. Even with our focus on market share gains and our significant investment in our digital transformation strategy, ROIC remained strong at nearly 30% as of fiscal year-end, which we believe places us firmly at or near the top of our retail peer group.

Now, let me take you through our updated outlook for 2019. Outlook for 2019, the company expects sales for fiscal 2019 to be in the range of $1.89 billion to $1.1915 billion (sic) [$1.915 billion] on comparable retail sales between flat to negative 1%.

We project e-commerce penetration will grow from approximately 28% to over 30% of net sales. Adjusted operating margin is expected to be in the range of 6.3% to 6.8% of sales as compared to 6.6% in adjusted operating margins in 2018. We anticipate fiscal 2019 adjusted net income per diluted share to be in the range of $5.25 to $5.75 as compared to adjusted net income per diluted share of $6.75 in 2018.

We anticipate approximately $30 million of adverse sales and $30 million of adverse gross margin impact as a result of the Gymboree liquidation, which will adversely impact EPS by $1.50. We note that 2019 includes a higher adjusted tax rate of approximately 25%, which will reduce earnings by approximately $1.15 versus 2018 with approximately $1 of that amount resulting from an adverse impact on share-based compensation deductibility due to our current share price.

Our agreement to acquire the Gymboree and Crazy 8 IP and related assets will adversely impact adjusted net income per diluted share by approximately $0.75 as we make incremental investments to support the strategic opportunities for the brands and fund the acquisition. As part of our fleet optimization program, we anticipate closing between 40 to 45 locations.

We plan to utilize a third-party logistics provider to assist with fulfillment of holiday 2019 e-commerce demand, which should help minimize the disruption we experience this year. We expect to generate strong cash flow from operations in 2019, which will fund our capital return program and capital expenditures. We expect capital expenditures to be in the range of $70 million to $80 million. We ended the year with approximately $238 million remaining on our share repurchase authorization.

Q1 2019 outlook, as discussed, Q1 2019 is anticipated to be a highly disruptive quarter for The Children's Place as the Gymboree liquidation event and a later Easter creates unprecedented challenges. As a result, the company anticipates an adjusted net loss per diluted share in the range of a loss of $0.70 to a loss of $0.40 as compared to adjusted net income per diluted share of $1.87 in Q1 of 2018.

The Gymboree liquidation will have $1.15 to $1.40 adverse impact on adjusted EPS. In addition, adjusted EPS will be adversely impacted by approximately $0.92 due to a higher tax rate resulting from the impact of share-based compensation tax deductibility due to our current share price.

Finally, the acquisition of the Gymboree and Crazy 8 IP and related assets will also adversely impact adjusted earnings per share by approximately $0.15 to $0.20. The company expects sales for fiscal Q1 to be in the range of $385 million to $395 million based on comparable retail sales between negative 10% to negative 12%.

Quarter-to-date, traffic and comps are running down double-digits, pressured by Gymboree's liquidation event and delayed and lowered tax refunds versus last year. Although it's difficult to assess the impact of a possible pull-forward of Q2 demand into the Q1 Gymboree liquidation event, we currently estimate that a pull-forward should reasonably occur. And as a result, we anticipate Q2 comps to decline, albeit, at a more moderate rate than the Q1 decline.

Outlook for 2020, 2018 presented us with significant long-term market share opportunities, which we aggressively pursued. As a result, the timeline to achieve $12 in adjusted EPS by 2020 will be extended. Although the path to achieve our initial 2020 objectives is longer, the strategic steps we took in 2018 likely smooth the path to get there.

I will now turn it back to Jane for closing remarks.

Jane T. Elfers

President, Chief Executive Officer & Director, The Children's Place, Inc.

Thanks, Mike. As 2018 concludes, we're reminded of the durability of our business model and the strength of our long-standing strategic growth plans. We're reminded that our model withstands intense competitive pressures as others in this space cannot. We're reminded how we've remained firmly on offense as others struggled to make the investments necessary to compete in a rapidly evolving omni-channel world.

2018 was a transformational year for our company and for those that choose to look beyond the near-term, there are now even more reasons to be excited about the years ahead. I'd like to close the call by highlighting a few of them.

Our product is superior and resonates with millennial moms through what has been a very difficult period for kids' retail. Births have been down every year since 2008, with 2017 seen births at their lowest level in 30 years, yet we've managed to grow market share and post comps in the mid-single digits over the last few years.

We've discussed the investments we've made in digital personalization and the benefits we anticipate to derive from those investments. The bulk of the heavy lifting from the digital transformation is behind us and we are excited about the opportunities that lay ahead.

In 2019, we anticipate seeing the benefits take hold from the digital personalization investments that we've made to-date. We've shared our outlook for a decline in AUC in 2019. This allows us a meaningful and unique competitive advantage to help drive profitability. And in addition, we expect to drive margin benefits through market share gains, our fleet optimization strategy and ongoing expense management.

Our cash return story, which is built upon a strong balance sheet that has returned over $1 billion to investors since its inception, is anticipated to be another meaningful driver in 2019. We have a time-tested management team that has proven itself over the long term in a difficult space as we continue to deliver for our shareholders.

And lastly, the announcement of our acquisition of Gymboree's assets is the latest chapter in a very compelling story and we couldn't be more excited about our future.

At this point, we'll open the call to your questions.

QUESTION AND ANSWER SECTION

Operator: [Operator Instructions] Our first question comes from the line of Dana Telsey of Telsey Advisory Group.

Dana Lauren Telsey
Analyst, Telsey Advisory Group LLC

Q

Good morning, everyone. As you think about the path to accretion from Gymboree in 2020, any guidepost that we should be watching for? And then, is there anything structural that you look at different towards accomplishing that 12% operating margin over time? Thank you.

Michael Scarpa
Chief Operating Officer & Chief Financial Officer, The Children's Place, Inc.

A

So, Dana, as I said in my prepared remarks, 2018 presented a significant opportunity for additional long-term market share and we definitely took advantage of that. As a result, we expect our timeline to achieve our 2020 goals of $12.00 EPS and 12% operating margin will be extended. While we're seeing rising costs associated with freight and labor, the majority of the fundamentals that we had modeled within those ranges remain in place, and we think that the acquisition of Gymboree actually enhances the opportunities.

Again, just based on the disruption that took place in 2018 and the resulting impact, we just see these timelines being extended. We don't see anything structurally that's impacting that.

Operator: Your next question comes from the line of Adrienne Yih of Wolfe Research.

Adrienne Yih
Analyst, Wolfe Research LLC

Q

So, good morning. So, congrats on the acquisition of those assets, your single biggest competitor, I think it really does set the groundwork for material market share recapture. So, I want to stay on that theme, Jane. And if you can help us with this notion of the $600 million, how much of that is actually going to be in Gymboree opportunity?

And then, the manner in which you're doing it, it sounds like you're not going to keep the stores, so we're not going to worry so much about sort of store deleverage. Are you bringing that Gymboree brand in-house and, therefore, it becomes marginal transactions through your own fixed-cost infrastructure and is that the portion that's leading to that accretion in 2020?

And then, for Mike, also staying on the same theme, when you get to that mid-30% 2020 digital penetration, what does the TCP store base look like? And I just want to confirm that you will not have standalone Gymboree stores. You'll have an online presence of Gymboree and then you'll have the Gymboree brand within the TCP infrastructure? Thanks very much.

Jane T. Elfers
President, Chief Executive Officer & Director, The Children's Place, Inc.

A

Sure. Thanks, Adrienne. When you look at the opportunity, Gymboree was only a few years ago over $1 billion brand. Most recently through January full-year 2018, their sales were approximately $650 million. Of that $650 million, $460 million of it was Gymboree and the balance was Crazy 8.

When you think about what we're planning to do, we're focused on the Gymboree brand. As you mentioned, we are not planning to open any freestanding Gymboree stores. We think that this is a multi-channel play. We see number one opportunity online on e-commerce. And so, we will be working on developing a Gymboree website.

We are looking to brand this product in early 2020 and we're looking to have some component of the Gymboree product in a subset of our stores. As we mentioned on the call, we had gone ahead and developed some toddler product to address the void that we saw in July when Gymboree re-branded. That product is coming in soon.

It's under the TCP label, obviously, not the Gymboree label. That product is toddler-only and that will give us an opportunity to really work through the product and make sure that the quality, the look, the styling is how we want it. And then, as we said, we will brand it with the Gymboree label in early 2020.

As far as international opportunities, we'll be looking at those with Gymboree franchise partners and with our franchise partners. And then, certainly, wholesale is a discussion we're having internally.

Michael Scarpa
Chief Operating Officer & Chief Financial Officer, The Children's Place, Inc.

A

So, from a overall fleet perspective, we still are having basically 1,000 lease events over the next three years, which continues to provide us with great flexibility. We've closed 42 locations in 2018 and 211 toward our goal of 300 by the end of 2020. We sit today with 972 stores. We plan on closing 40 to 45 in 2019; an additional, call it, 45 in 2020 to get us to that 300 goal.

I did mention that the acquisition process provided us with what we think is good opportunities to potentially open some additional stores. We have a shortlist of 40 stores that we are investigating and think that we'll be opening about 25 stores over the next two years. There'll be TCP stores, but we think that there is a great opportunity to take advantage of the void in the market where Gymboree is closed. So, basically we're thinking, by 2020, we will end up with roughly 900 stores in the fleet.

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

Susan Anderson
Analyst, B. Riley FBR, Inc.

Q

Good morning and thank you for taking my question and thanks for all the details. Very helpful. I guess just a follow-up on Adrienne's question, I was curious if you have any thoughts around how big you think the Gymboree business could be and then also as a lot of your competitors probably go after that market share, I guess how do you combat maybe any additional promotional pressure if any of one them decide to get promotional to gain that share? Thanks.

Jane T. Elfers
President, Chief Executive Officer & Director, The Children's Place, Inc.

A

Thanks. I think it's for us to label their concerns. There are not a lot of labels left in children's specialty retailing. Over the past several years, we have seen so many of them go out of business, not being able to compete. To be in this business, there is not a lot of loyalty for the customer. And so, you really need to be able to compete on scale and not a lot of people can do that. So, when you look at the fact that we've now acquired two of the most recognizable names in kids' specialty, I think that puts us in a different position than the competition.

As far as the Crazy 8 label is concerned, Crazy 8 was developed by Gymboree to compete against Children's Place and it was important to us to retire that label, so that, that would not be resurrected as a competitor.

As far as Gymboree is concerned, we said there was $460 million of volume out there. There is only – the Gymboree and Crazy 8, as of 2018, as we said, had gotten down to combined $650 million. Of that $650 million, there was only $230 million in total toddler plus baby out there for the opportunity and most of that is mall-based. So, we are really the last specialty competitor left in the mall at those price points.

So, I think that you can pretty much assume that a lot of that share is going to come to us and now obviously owning the IP and being able to brand Gymboree within the mall and online, I think that that's a major opportunity. So, I really don't see a competitor coming out and certainly a mall-based competitor, because I don't know who that would be fighting for that share. So, we feel pretty comfortable with the acquisition.

Operator: Your next question comes from the line of Jim Chartier of Monness, Crespi, Hardt.

James Andrew Chartier
Analyst, Monness, Crespi, Hardt & Co., Inc.

Q

Hi. Good morning.

Jane T. Elfers
President, Chief Executive Officer & Director, The Children's Place, Inc.

A

Hi.

James Andrew Chartier
Analyst, Monness, Crespi, Hardt & Co., Inc.

Q

It sounds like, from a category perspective with Gymboree [ph] shrink to toddler, (43:57) it's a good fit. Just curious on a few other areas. How did Gymboree's e-commerce capabilities compare to yours and what percentage of sales did Gymboree get from e-commerce? What the private label credit card penetration might have been?

And then, you highlighted your AUC advantage. How do you expect the Gymboree price value equation to benefit from your sourcing expertise? Thanks.

Jane T. Elfers
President, Chief Executive Officer & Director, The Children's Place, Inc.

A

Thank you. The Gymboree e-commerce business, I think, was around $100 million as of 2018. At its heyday, it was $150 million. So, I can't really speak to the details of it, but I would think that it was not nearly growing at the percentages that a lot of other retailers were growing over the last few years on e-comm. So, I'm not sure they were able to make the investments.

We've certainly made a lot of investments around digital, particularly in 2018. So, we feel confident that we are in a much better position to be able to bring those customers into our digital ecosystem now that we have their customer list and I think that based on what we've done and all the work we've done on our website, we should be in a good position when we launch in 2020 to be able to add a tab on our website, to be able to really reach out and communicate in a good efficient way with that Gymboree customer base.

As far as AUC is concerned, sourcing is the strength of ours. Our Head of Sourcing has already been in conversations as far as how we are going to pull that together from an AUC perspective. Obviously, the Gymboree AUC is a higher AUC, which is the same as the product that we're bringing in that we mentioned it's coming – that toddler product is coming in May. We put a picture of it in our investor deck. Those AUCs will be higher, I would say anywhere between 20% and 30% higher, as well the AURs.

And so, that's really what that customer wants. There is a very different aesthetic, if you will, to the Gymboree brand than there is in any other brand. And I had mentioned earlier that being in this business for as long as I've been in the kids business, there really isn't a lot of loyalty and you really have to work for the loyalty.

And we've been very successful in growing market share, we've been very successful with our Mom, but the Gymboree Mom and the Gymboree customer is quite unique in her passion for that product. And there really isn't anything like the Gymboree product out in the marketplace and the DNA of that product is something that was built over a lot of years and that customer really misses that product.

So, we think our ability to recreate and revitalize Gymboree will not only give us a new avenue for growth, but it will also help us within our stores, particularly when Gymboree is over penetrated in the toddler areas and we are not, help us bring a younger customer into our store and really help us maximize that toddler opportunity.

As far as the private label credit card, we don't really have any information on that. We will work to bring the Gymboree customer into our own loyalty programs and our own loyalty private label credit card programs. I can't give you information on what that meant to them.

Operator: Our next question comes from the line of Paul Lejuez of Citi.

Paul Lejuez
Analyst, Citigroup Global Markets, Inc.

Q

Hey, guys. Thanks. You guys have had to compete against Gymboree closings in the past. I understand this time, it is different in terms of the number of store closings, but in many ways, it's still center-by-center, store-by-store. So, I'm curious what's different this time in terms of how your stores are behaving relative to what you've seen historically? Thanks.

Jane T. Elfers
President, Chief Executive Officer & Director, The Children's Place, Inc.

A

I think it's really the compressed time period is the best answer we could give you. Like we said, we were in uncharted territory. We've obviously never come against something like this. You're talking 800 stores where we compete in over 70% of the locations. So, you're looking at almost 600 doors where basically across the street from us, we've got a competitor with a lot of the same type of classification liquidating in a 90-day period and what is now a 60-day period.

We have also got the competitive pressures of the later Easter. We've got the competitive pressures of what happened in February, with significantly delayed tax refunds and we've also got the pressure of the web. So, when you look on their website, the Crazy 8 website is now closed as of last week, but the Gymboree website is significantly promotional and I assume will continue to be.

They're still receding goods into their stores. We're obviously watching them very closely and we're still seeing them recede goods in there as well as spring goods. So, it is a very compressed, very unusual time for us. As we said, we think it will be disruptive, but we are very much looking forward to the back half of the year when we feel that we're going to have a lot of tailwinds.

Operator: Our final question will come from the line of Marni Shapiro of The Retail Tracker.

Marni Shapiro
Managing Partner, The Retail Tracker

Q

Hey, guys. I'm looking forward to see what you guys do with Gymboree. I agree with you, I think there is an opportunity to bring the brand back. There has been a lot of talk about Gymboree. There is another competitor in the market that's also gone out in the segment that's smaller, but one that's been growing for you, which is Payless. So, at the same time, could you talk a little bit about that opportunity as well or is that just so secondary to you? And then, everything else, I'll follow-up with offline.

Jane T. Elfers
President, Chief Executive Officer & Director, The Children's Place, Inc.

A

Sure. I don't think it's secondary. They do about 35% of their business in kids and I think it's really what have we spoke about on the conference call in my prepared remarks when I said it's not just about Gymboree and Crazy 8 closings, there are so many competitors out there and we see this as years to come as an annuity. And Payless is just another example of a company who closed I think over 2,000 doors. We've been going after the footwear business for years and we think that that's an opportunity for us as well.

Operator: Thank you for joining us today. If you have further questions, please call investor relations at 201-453-6693. You may now disconnect your lines and have a wonderful day.