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GCO - Q1 2021 Genesco Inc Earnings Call

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CORPORATE PARTICIPANTS

David Slater *Genesco Inc. - VP of Financial Planning & Analysis and IR*

Melvin G. Tucker *Genesco Inc. - Senior VP of Finance & CFO*

Mimi Eckel Vaughn *Genesco Inc. - CEO, President & Director*

CONFERENCE CALL PARTICIPANTS

Janine M. Stichter *Jefferies LLC, Research Division - Equity Analyst*

Jonathan Robert Komp *Robert W. Baird & Co. Incorporated, Research Division - Senior Research Analyst*

Mitchel John Kummetz *Pivotal Research Group LLC - Senior Analyst of Footwear, Apparel Vendors and Retailers*

Samuel Marc Poser *Susquehanna Financial Group, LLLP, Research Division - Senior Analyst*

Steven Louis Marotta *CL King & Associates, Inc., Research Division - MD & Director of Research*

PRESENTATION

Operator

Good day, everyone, and welcome to the Genesco First Quarter Fiscal 2021 Conference Call. Just as a reminder, today's call is being recorded. I would now like to turn the call over to Dave Slater, Vice President of FP&A and Investor Relations. Please go ahead, sir.

David Slater - *Genesco Inc. - VP of Financial Planning & Analysis and IR*

Thank you, Savannah, and good morning, everyone, and thank you for joining us this morning to discuss our first quarter fiscal 2021 results. With me on the call today are Mimi Vaughn, our President and Chief Executive Officer; and Mel Tucker, our Chief Financial Officer.

Participants on the call expect to make forward-looking statements. These statements reflect the participants' expectations as of today, but actual results could be different. Genesco refers you to this morning's earning release and the company's SEC filings, including the most recent 10-K filing, for some of the factors that could cause differences from expectations reflected in the forward-looking statements made during the call today.

Participants also expect to refer to certain adjusted financial measures during the call. All non-GAAP financial measures referred to in the prepared remarks are reconciled to their GAAP counterparts in the attachments to this morning's press release and in the schedules available on the company's home page under Investor Relations in the quarterly earnings section.

I want to remind everyone we have posted a presentation summarizing our results that is accessible on our website. Now I'd like to turn it over to Mimi.

Mimi Eckel Vaughn - *Genesco Inc. - CEO, President & Director*

Thank you, Dave. Good morning, everyone, and thank you for joining us today. We hope each of you and your families are doing well and staying healthy. Much has changed in the world since we last spoke a few months ago as the COVID-19 pandemic has challenged Genesco and others in so many ways. And as we strive to protect our people, our customers and our businesses.

Before we begin, I'd like to thank the Genesco team for the incredible tenacity and resilience you have demonstrated during these extraordinary times. Throughout the crisis, our people have been resourceful and effective, working to best navigate our business through this pandemic.

Our company began fiscal '21 with positive momentum, following 11 consecutive quarters of comp sales growth. Thanks to the work we did last year, creating a footwear focused company and building on the turnaround and profitability that began in fiscal '19, we entered the pandemic in a position of strength.

Each of our businesses has a strong strategic position, grounded in a deep and constantly evolving understanding of the customer it serves. The strength of our concepts and the competitive advantages we've built into leadership positions over time were evident, as our customers actively sought to engage with us online, while our stores were closed and as they have enthusiastically returned to our physical locations as we have reopened our stores.

Going back to where we left off at our fourth quarter call, the impact from COVID-19, at the time, was limited to some softness in-store traffic, primarily in tourist destinations in both the U.K. and North America and in airport stores. The situation changed quickly as the number of reported cases rapidly increased, resulting in the President declaring a national emergency in many states requiring nonessential businesses to close and individuals to shelter at home.

To safeguard the health of our employees and customers and with their well-being foremost in our minds, we made the decision to temporarily close all North American stores beginning on March 18 and all U.K. locations beginning on March 23. We also closed our headquarters buildings in Nashville, Montreal and Scotland and began working remotely at that time. With our principal source of revenue interrupted, we quickly went to work and took dramatic and swift actions to drive e-commerce, our remaining source of revenue and to preserve liquidity and financial flexibility.

We've more than doubled our e-com business over the last 5 years, thanks to a variety of investments. We've had a real focus on mobile. We've made our website experiences better for navigation and checkout and we've invested in distribution center expansions with dedicated e-commerce fulfillment among many other investments. We've been able to capitalize on these investments, driving significant gains in our digital business during the pandemic.

In mid-March, we began executing specific actions to further drive e-com sales and enhance communications with our customers while stores were closed. We increased online advertising spend above the increase we already planned, investing in marketing channels that have historically had higher conversion rates. In addition, we strategically revised our social and other digital campaigns to reflect comfort, creativity and at home messaging, while intentionally featuring lifestyle supporting social distancing. User-generated content, positive messaging and creative campaigns, reflecting quarantines resonated especially well with our teen and used customers.

So we did experience a brief slowdown in digital sales from mid-to-late March as consumers stocked up on food and other necessities to weather a prolonged home confinement, trends picked back up in early April and continue to accelerate week over week, resulting in triple-digit e-commerce gains for the month and at almost 65% comp gain for the quarter. Close to 90% of Journeys e-com traffic came in over mobile with a 65% conversion increase. Schuh's advanced digital capabilities benefited it greatly as well as there have been days when e-com sales alone have been higher than last year's stores plus e-com sales combined. What's most exciting is the number of new visitors to our sites, representing nearly 50% of traffic in Q1.

Not only are we attracting new customers and expanding our online shopper base, but we are also converting traditional in-store customers to digital buyers. In May, e-commerce sales increased considerably above April substantial levels, and we posted a 300-plus percent comp increase even as our stores were reopening. April delivered all-time records for e-com shipments. And in May, we broke those records again. Our ability to process these volumes was made possible by the hard work of our DC teams and the investments we've made in enhancing our fulfillment capabilities.

As pleased as we've been with e-com, the loss of store sales presented a tremendous economic challenge for our business. As such, the next area of significant focus was inventory. Knowing our stores would be closed for several weeks, our highly skilled and experienced merchant and product teams quickly turned to reducing any seasonal product they could, given a shorter spring/summer selling season, pushing out orders for core product that would be needed later and canceling select fall/winter merchandise orders that we anticipated wouldn't be needed. This was a very complicated undertaking, and our genuine thanks goes out to our teams and our fantastic vendor and factory partners who have not only extended us additional payment terms, but also, as they always have over the years, work collaboratively and productively with us to adjust inventory levels to the reduced demand.

As a result, inventory at the end of Q1 was up only 6% on a significant reduction in sales from store closures, and we have reduced receipts by several hundred million dollars going forward. The increase at quarter's end was largely at Journeys, representing fresh products that should sell-through as stores reopen.

Our attention turned also to managing expenses, tightening capital and controlling cash outflows. We made the decision to reduce our workforce by 90% across our stores, corporate offices and distribution and call centers largely through extensive furloughs. We chose furloughs to give employees the confidence they were still employed by us and to facilitate a faster ramp-up when stores reopened.

In addition, we implemented salary reductions for me, our executive team and select employees, while our Board volunteered to forego their cash compensation during this difficult period. As a result of these and other decisive and some difficult actions across our P&L, we reduced expenses by 20% during the quarter.

At the same time, we've had productive conversations with our landlord partners regarding rent relief while stores were closed, along with discussions about rent structures as stores reopen, given our need for more flexibility due to the significant uncertainty ahead. Finally, we cut capital spending by more than 50% for the coming year. We're moving forward with planned inventory -- planned investments in digital and omnichannel strategic projects such as (inaudible) and distribution center upgrades, which are vital to further building our capabilities, but we've halted other spending mostly associated with new real estate projects.

While we started the crisis in a positive cash position to ensure we had adequate liquidity, we borrowed a little over $200 million from our existing credit facilities and recently secured additional availability, which Mel will discuss. We managed cash burn very well and at quarter's end, had $239 million of cash, including these borrowings, thanks to the extensive efforts I've described across the company and our treatment of payables and rent.

Overall, we remain confident we're taking the necessary steps and working actively to maintain the cash position needed to navigate this pandemic. On May 1, we shifted our focus, and we're excited to quickly begin reopening stores and welcoming customers back to serve them in our physical locations. We're operating at reduced hours, adhering to CDC and other government and health authority guidelines, where state and local officials have allowed malls to operate.

As of today, we have opened more than 900 Journeys stores and more than 80 J&M stores, close to 1,000 stores in total. More than 70% of our stores are now open in North America and 2/3 of our fleet is open in total. The health and well-being of our employees and customers remains our absolute priority and our special task force teams have worked tirelessly to ensure the appropriate safety procedures and equipment are in place for our stores and headquarters. All stores are operating under enhanced measures, including Requiring our employees to wear masks; providing hand sanitizer in multiple locations throughout the store; implementing enhanced cleaning and sanitation protocols; reconfiguring sales floors to promote physical distancing; and modifying employee and customer interactions to limit contact.

We will continue to reopen stores in a phased approach and where we believe we can work carefully under our enhanced measures to ensure the safety and the health of our people and customers. With the visibility we currently have, we're anticipating reopening close to 85% of our stores on both sides of the Atlantic by the end of June and almost all stores by the end of July. For the Journeys stores we've reopened, not surprisingly, we've experienced lower traffic, double-digit decreases compared to last year. Journeys, however, has been able to more than offset this headwind through significantly higher conversion and higher transaction size, comping nicely positive to last year so far in the stores that are open.

Women's and kids sales have been especially robust, and we've seen families shopping together to satisfy pent-up demand. All in all, we're very encouraged by Journeys' store performance post reopening. We've always known the Journeys' customer enjoys the store experience and the exceptional service they receive in person, and it's been tremendous to see the strength of the Journeys brand draw shoppers back in. To have opened as many stores as quickly as Journeys' has done, is a real testament to its operational abilities and sales have benefited from this first-mover advantage.

Conversion at the reopen Johnston & Murphy stores has also been much higher, but traffic has been slow, substantially slower than we've seen at Journeys. While traffic and sales have been improving each week, we believe the return to pre-virus levels will take some time, as the J&M customer has remained largely on the sidelines due to the economic uncertainty brought on by the pandemic.

Reopen store sales have been running at less than half of last year's level so far. And while J&M, historically, enjoys a larger penetration of e-commerce sales, the gains during the quarantine have not been as pronounced as we've seen in our teen and used businesses. As was the case prior to the pandemic, casual footwear and apparel continued to drive J&M sales, as working from home and sheltering in place has temporarily reduced the need for dressier product.

With respect to Schuh, it's too early for a read since only a few stores have been open for a few days. The U.K. has been slower to open than the U.S. and is opening with a greater number of restrictions. June 15 is a key date when England allows stores to reopen, and we expect to have over 2/3 of our fleet up and running then. With best-in-class e-commerce capabilities, Schuh has been the most successful of our businesses, capturing some of the lost store sales over the past 2 plus months, albeit through heavy promotional activity to match the U.K. competition. Like Journeys, women's and kids sales have been most brisk.

So it's important to note that we believe sales in May, typically a low volume month for us, are benefiting from a number of special factors, including pent-up demand, less competition, while many stores remain closed, more free time as consumers are home during the week with kids out of school, and consumer pending -- spending power, which has been bolstered by stimulus money and enhanced unemployment benefits. We've also opened in areas least affected by the virus, so we will see where sales normalize once all stores are open.

Regardless of the near-term volatility we may experience in the coming months, we remain confident in the strategic positioning of our businesses for the longer term. We aspire to create and curate leading footwear brands and to be the destination for our consumer favorite fashion footwear. Both Journeys and Schuh as houses of brands have demonstrated their vast consumer appeal during this crisis. J&M, along with Levi's and our other Licensed Brands, have unique and rich histories and their longer-term success lies with the loyal customer bases they've built up over the years. There will be opportunities that arise out of this chaos and the retail consolidation that is following and our businesses are very well positioned to capitalize on them.

I began and would like to end my remarks today, thanking our extraordinary team of people for their diligent efforts and perseverance, especially those who've been on the front lines in our stores and distribution centers. Tons of great adversity like these highlight our greatest asset, our talented, experienced and highly committed people who adapted quickly and with ingenuity and creativity are meeting the many challenges we face. This has made all the difference for our company and has been inspiring to see unfold. Genesco team, I'm so proud of all that you've accomplished.

At the same time, we've made a real effort to take care of our community through activities like Journeys' involvement in the Tennessee Emergency Management Agencies COVID-19 response, J&M's donation of thousands of masks to the local community resource center; the Schuh Trust's GBP 3 million donation to the National Emergencies Trust; and the National Health Services charities and License brands shoe donation to local schools, health care workers and Soles4Souls. Our thanks also to our partners around the world who have extended great support to us.

And finally, during this time of pain and anguish in our country, all of us at Genesco stand with those fighting for the causes of equality and racial justice, and we call on us all to help heal the decisiveness and to make progress in our communities. And with that, I'll turn the call over to Mel to give more insight into our performance and our financials.

Melvin G. Tucker - *Genesco Inc. - Senior VP of Finance & CFO*

Thanks, Mimi. We are certainly in unprecedented times. But I also couldn't be more proud of how the Genesco team members are conducting themselves in this very challenging environment. Little did we know during our prior earnings call on March 12, what lie ahead of us. Fortunately, Genesco entered the COVID-19 global pandemic in a position of financial strength with $81 million in cash at the start of the year and no North American borrowings.

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During the first quarter, we used $45 million to fund operating losses and for working capital purposes and spent $7 million on capital projects. We borrowed $208 million, leaving us with $239 million in cash on hand at quarter end, benefiting from our treatment of payables and rent. To accomplish this, we strengthened our financial position by drawing upon existing lines of credit in the U.S. and U.K., extending payment terms and managing inventory by reducing future receipts by over $300 million at cost. We carefully scrutinize all operating expenses, eliminating all nonessential spend. Planned capital expenditures for this year were reduced by approximately $35 million with our expected spend now roughly at $30 million. We actively modeled multiple potential scenarios surrounding the length of store closures as well as various levels of sales performance once our stores reopened.

Further, we evaluated our cash burn rate under each scenario, given the uncertainty surrounding the reopening and recovery of the economy to ensure we had ample liquidity. In order to further reinforce our balance sheet this month, we amended our ABL lending agreement, increasing the facility from $275 million to up to $350 million of borrowing capacity. With these improvements to our capital structure, we are even better positioned to navigate these turbulent times, and we do have options for additional liquidity should we need it.

Turning to the results from the first quarter. Given that stores were closed for the back half of the quarter, including the lead up to the Easter holiday, net sales were down 44%. This precipitous drop in revenue led to an adjusted loss from continuing operations of $51.4 million or $3.65 per share compared to adjusted earnings of $5.9 million last year or $0.33 per share in what is typically a lower volume quarter.

Q1 consolidated revenue was $279 million compared to $496 million last year, driven by store closures, lower wholesale revenue, lower foreign currency exchange rates, all set partially by digital comp growth of 64%. We did not provide overall store comp results in Q1, as our comp policy removes any stores that are closed for 7 consecutive days, and therefore, we feel that overall sales is a more meaningful metric.

By division, overall sales were down 48% at Journeys, 39% at Schuh and 48% at J&M. While Licensed Brands, overall sales were up 21% due to the Togast acquisition. Moving to margin. In total, consolidated gross margin decreased 640 basis points to 43%. Higher shipping and warehouse expense, driven by large increases in e-commerce accounted for 260 basis points of this decrease and affected all of our businesses. Schuh's gross margin, which was down 1,230 basis points was impacted the most due to a significant e-com business and a higher proportion of cell product, given the heavily promotional environment in the U K. J&M's gross margin also decreased due to increased markdown activity and was down 320 basis points. Journeys' wasn't very promotional, but gross margins decreased 400 basis points due to higher e-com expense plus an increase in inventory reserves.

Adjusted SG&A expense came in at $190 million, a 20% reduction in dollars compared to last year because of the proactive steps we took at the onset of the pandemic. A significant amount of savings resulted from the reduction in store selling salaries and wages in our corporate areas from the furloughs and salary reductions. Compensation expense also benefited from employee retention credits related to the Cares Act in the U.S. as well as government relief provided in the U.K. and Canada.

Rent expense was lower in Q1, driven in part by property tax relief in the U.K. and the true-up of excess rents not likely to be incurred in fiscal '21. Bull contract rent is included in our expenses per accounting requirements as we continue to negotiate with our landlords. For the quarter, there was no bonus expense compared to a meaningful amount due to a strong Q1 last year. To add all this up, the first quarter's adjusted operating loss was $69.5 million versus operating income of $8.4 million last year. We fully impaired Schuh's goodwill related to the acquisition and partially impaired other trade names during the first quarter. These noncash charges are included in GAAP earnings, but removed from non-GAAP results. Our adjusted non-GAAP tax rate for the first quarter was 27%.

Turning to the balance sheet. Overall, Q1 inventory was $392 million, a 6% increase or $24 million over last year on quarterly sales that were down 44%. Journeys' inventory growth is the primary driver of the increase, up 14%. We see very little risk here as most of this inventory is core product. At Schuh, on a constant currency basis, inventory was down 11%. J&M's inventory was down 8%. At the end of May , overall inventory was down 10% to last year, thanks to the demand we've experienced since our stores reopened in May's strong e-commerce results.

Due to the continued uncertainty, we are not providing guidance, but we'll provide some thoughts on Q2 given our view at this time. Based upon the assumption that the opening schedule unfolds, as Mimi described and that schools begin to open as usual in August, we expect that overall sales in Q2 should be higher than Q1.

Our e-commerce business is off to a good start in May. But as more stores reopen, we would expect this strong performance to moderate. In Q2, we expect gross margin rates to be lower than Q1, with continued prior from higher shipping and warehouse expense from the higher e-commerce sales, a heavier promotional environment and potential additional inventory reserves.

SG&A dollars in Q2 will be closer to the Q1 levels than the levels in Q2 last year, but could vary depending upon our reopening cadence and store volumes. We expect to benefit from the same savings actions we did in Q1, but with some higher costs due to higher variable expense from operating stores. We anticipate burning a good deal more cash in Q2 as the payables with extended terms come to -- come due, which will bring down our cash balance.

Our wholesale customers have been -- begun paying their pass to invoices, which should add somewhat to cash, and we look forward to the remaining outstanding accounts catching up. We are planning inventory conservatively, but we will adjust accordingly as visibility increases. The annual tax rate is expected to be approximately 28%.

In conclusion, I would like to thank our teams for their quick response and diligent efforts put forth in managing inventory, capital and SG&A, which has enabled us to maximize our liquidity as we successfully navigate these most challenging times. As we all endure this trying stretch together, we would like to wish everyone's safety and good health. This concludes our prepared remarks. At this time, I would like to turn the call back over to the operator for questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) And we will take our first question from Steve Marotta with CL King & Associates.

Steven Louis Marotta - *CL King & Associates, Inc., Research Division - MD & Director of Research*

I have two questions. The first is, can you talk a little bit about the e-commerce activity in markets that have been reopened. And clearly, there's a balance of your stores that haven't reopened yet, and I assume that e-commerce is strong in those. But how is the e-commerce activity, specifically in markets that have been reopened, say, in the second or third week?

Mimi Eckel Vaughn - *Genesco Inc. - CEO, President & Director*

Great. Steve, good to talk to you. Hope you are doing well. We were really satisfied with the way that our e-comm performed over the course of the first quarter. At the end of March, consumers were shopping only the stock up for the quarantine. But in April, our digital sales began to pick up pretty robustly. They grew stronger each week of April and just exploded at the end of the month. There definitely was the impact of stimulus money on our e-comm sales. That was the only channel that was available for our consumers largely to purchase in, but that really robust activity carried into May. Recent bank account analysis says that the consumer spent half of their stimulus money in the first 10 days after getting it. It reminds us a lot of just tax money and tax refund money. It's a real jolt into the overall economy. And so it's definitely a combination of stimulus and less ability to shop in stores that drove the high e-comm volumes, but we took advantage of this. And look, we were able to process that volume, thanks to some of the investments that we've made and our DC staff's running and keeping the operations going. That stimulus money, because of its impact in May as we've reopened stores, the rising tide lifted both sales in stores and online. And so it's a little bit too early to tell definitively how e-commerce will settle out. We do expect that it's going to moderate from our plus hundreds of percent level, but the consumer really like the experience that they had shopping online. We converted a lot of consumers to shopping online, both who shopped in our stores before and we got a lot of new customers. And so I think that, that will bode well for higher levels of e-commerce going forward. We've been running at about a 20% level of growth, and that stepped up from our historical levels of 15%. And I imagine that going forward, it will be even stronger than that.

Steven Louis Marotta - *CL King & Associates, Inc., Research Division - MD & Director of Research*

That's helpful. And one of the impediments to converting the Journeys customers, as I recall in the past, has been the fact that there is a fairly large percentage that purchase in cash in the store. Can you remind us what that percentage was last year? Or what percentage of sales within Journeys stores were cash? And how you think that this endemic may affect that going forward? And then how you can convert some of those customers online?

Mimi Eckel Vaughn - *Genesco Inc. - CEO, President & Director*

Yes. So you are right that you think about that team customer and you think about the way that they interact with us. A lot of times, they will be working in a part-time job, where they will get money from mom and dad or from their relatives and bring cash into the stores to buy their shoes. And we have seen in the past, about 30% of our overall sales being done in cash. And certainly, that wasn't an option during the time that our stores were closed. But interestingly, our team customers figured it out, whether they relied on debit card usage. We have enhanced the overall payment options that our customers can use online, whether it be PayPal, whether it be other ways to be able to pay in multiple segments. We adopted Klarna in the U.K. We adopted an Afterpay as the companies that we're using, even for Johnston & Murphy. And so there are more options for shopping online for the consumer. And we expect that, going forward, that the consumer may be more interested in things like contactless payments, which we have the ability to transact with in our stores. And payment is going to be just a really important place for -- focus for us, both online and in stores. And we have enhanced and will continue to enhance our options, so that the customer can interact with us however they like.

Operator

And we will take our next question from Janine Stichter from Jefferies.

Janine M. Stichter - *Jefferies LLC, Research Division - Equity Analyst*

I just wanted to ask a little about inventory in the channel. It sounds like Journeys wasn't too promotional in the first quarter, but you're expecting that to heat up a bit in 2Q. Can you talk a little bit about what you're seeing just in terms of the inventory that's out there, competitors and how you think this might impact the promotional environment?

Mimi Eckel Vaughn - *Genesco Inc. - CEO, President & Director*

Sure. Janine, good to talk to you. So interestingly, every one of our businesses had a different promotional posture during the pandemic. Journeys has started out being somewhat promotional online, but that was really just to match competitor discounting in the market. And I think that, that was a bit of a knee-jerk reaction that, out of the gate, a lot of people and brands who sell product that Journeys sell went to some pretty significant discounting early on. But that also came off pretty quickly and for the balance of the quarter. And then also in our store opened up, we haven't been especially promotional. And I think that the consumer certainly has an appetite for sale product. We've seen some of that. We have seen that there is a little bit more economic sensitivity than there has been in the past, clearly, because of everything that's happened. But we're not anticipating needing to promote extensively within Journeys in order to clear merchandise. I think you may have heard what Mel said is that our inventory, actually in May, since our stores have opened up so robustly and online continues to be strong, was down 10%. So we don't expect that we're going to have to promote in order to clear through our inventory.

There has been a difference between perhaps footwear and apparel. I think the consumer's appetite for footwear has been stronger. It's an easier purchase. I think that perhaps some consumers are still just a little bit more cautious trying on apparel, but we'll see. And I think that others who've reported on the footwear front have reported some pretty nice sales. So as long as sales move briskly and inventory doesn't become a backlog in the channel, we're going to respond to whatever we need to do to make sure that our inventory is rightsized. And we'll think creatively about hitting the right sets of price points to satisfy the consumer appetite for better value and better sales.

Janine M. Stichter - *Jefferies LLC, Research Division - Equity Analyst*

Okay. Great. And then just as you go through your negotiations with your landlords, any changes in how you're thinking about the long-term size of the fleet, just kind of given what you're seeing with the migration online?

Mimi Eckel Vaughn - *Genesco Inc. - CEO, President & Director*

Yes. So I think you've got two questions in there. One is just negotiations with landlords and then overall size of the fleet. So we spent a significant amount of effort during the last few months with our landlord partners. It's been a key initiative since rent is the biggest expense item on our P&L outside of the cost of goods. We pay more rent per square foot because we believe we need to be in the right locations. It's more than selling salaries. And to define the rent discussions, the way we've been thinking about rent is that we are paying rent for traffic in shopping centers that will drive and generate sales. And the pandemic brought about two problems: One is that stores were closed, and there was no way to generate sales. And then secondly, stores that are opening are opening on different schedules, and there's a large variation in terms of how they're performing. Some are performing really well. Our average is good, but some are performing well below average. And that points to the need for rent relief while stores are closed and also variable rent helps to share the risk and the uncertainty of how stores are going to perform, going forward. We've made some progress, mostly with smaller landlords. Some of the larger ones have just been waiting to understand the reopening better.

In terms of how we think about the fleet. Going into the pandemic, I think we've shared with you before that we perform well across A, B and C locations. And in fact, our C locations are more profitable on a 4-wall percentage basis than our A locations. Interestingly, our B and C locations have actually performed more strongly since they have reopened. All have been good, but B and C shoppers, I think, have fewer options. And so they have been flocking back into malls. So to say specifically how are we thinking about our fleet, we have been shrinking square footage over the last few years. I think that, that will continue. And the number of stores that we have opened will be very highly dependent on the rent structures and the rent deals that we have in place. One of the really positive effects of store reopening as we've seen huge productivity in our overall labor model, and we have been able to with reduced store hours. And also with how much higher conversion we have seen that we've gotten a lot of productivity out of our store force and using things like workforce management and traffic counting has allowed us to manage that really allowed our operations team to do a great job of managing that ramp back up. And so selling salaries has been been okay as far as the economics go, but it really is rent that is the highlight and that will dictate the number of stores that we will keep open.

Operator

Our next question will come from Mitch Kummetz with Pivotal Research.

Mitchel John Kummetz - *Pivotal Research Group LLC - Senior Analyst of Footwear, Apparel Vendors and Retailers*

Let me just start on Q2 to date. Is there any way you could quantify the performance like the first 5 weeks of the quarter, either in terms of kind of a sales number or an overall comp number?

Mimi Eckel Vaughn - *Genesco Inc. - CEO, President & Director*

Yes. So look, Mitch, I think that that's -- it's early days, right? We've just expanded a whole lot of effort around opening up of our stores. Let me give you a little bit more color. So Journeys we've got about 80% of our fleet open right now. Traffic has been down a lot. I'd say it's running down in the close to 20% range. I think that's better than some of the numbers that I've seen on the mall on average that younger customer has just had a lot of appetite to come back into the mall. We've seen much higher conversion and higher transaction size. We've seen family shopping together, as I said, more multiple purchases. And we've seen, as we said, positive comps and nicely positive, I mean, even in the double-digit range. Stores tend to open up really strongly, and I think that's the measure of pent-up demand, and then they'll trend over time to a more normalized levels. Some of the other things that we've seen or we've seen a change in just overall traffic patterns, weekends are usually really good for us. We've actually seen strong traffic on weekdays. Weekends were the ones that have the power hours, but now we're seeing power hours during the week in the afternoons. People are coming to shop from 12 to 5 or 12 to 6. We're also seeing some of our smaller markets perform well. There have been some strong states. Interestingly, California and the Midwest to the South have been strong. Places like Ohio and Illinois, Indiana, Tennessee, have been strong. The weaker states have been highly tourist destinations like Hawaii. Florida has been weak. Places like Orlando have been weak. Places like Miami have been weak. Texas has been flattish so far. So every day, every week, we're absorbing where we are, and we're pleased with the Journeys' performing in particular. We've talked about Johnston & Murphy being a bit more slow to ramp up. I think the major difference has been the quantum of traffic and and Johnston Murphy is seeing a lot less traffic than journeys has been seeing conversion is strong. But that customer's mind is elsewhere right now. It's on pandemic. It's on the economy. It's on taking care of their family. And they're working at home. So we've seen some pretty big differences in J&M and the reopening. But like the last -- like the Great Recession, J&M had 9 fantastic years on a run after absorbing the impact of the Great Recession. And we're sure that, that business will build strongly over time and get back to historical levels.

Mitchel John Kummetz - *Pivotal Research Group LLC - Senior Analyst of Footwear, Apparel Vendors and Retailers*

Okay. And then Mel, on Q2, I just want to hit on a couple of the things that you mentioned. So I think you said sales higher than Q1. And I'm wondering why that would be? I think in the past, Q2, Q1, sales-wise looked pretty similar. So is that really a function of more stores open for more days in Q2 than Q1? Or is there something else that play there? And then you kind of spoke to gross margin and SG&A, and I'm trying to understand whether or not in the second quarter, you expect EBIT to be higher or lower than Q1?

Melvin G. Tucker - *Genesco Inc. - Senior VP of Finance & CFO*

So with the Q2 sales, we expect them to be high, and I think that's really more a function of store count. If you look at the first quarter, we were closed pretty much half the quarter, made up for some of that with e-comm. And if you look at where we are right now, roughly 2/3 of the stores are opened with more stores opening, and we should be close to fully opened by the end of July. So as we continue to open stores and they're opening nicely, as Mimi mentioned, with the Journeys stores comping up positive and e-commerce continuing to comp positive, we set a unit volume record in the month of April only to exceed that in the month of May. So that's more a function of just the timing of when our stores are opening and the fact that we're going to have more store open days. And then the stores are opening very strong at Journeys.

Mimi Eckel Vaughn - *Genesco Inc. - CEO, President & Director*

I'd just to add one thing to that before Mel just talked about gross margin and SG&A. The way to think about it, Mitch, is that I think that some of the demand, we would have otherwise gotten in April. The end of March and April actually got pulled forward into the months of May and June. And we expect that, that spring shopping, that typically would have happened earlier, is going to -- it's still going to happen -- it's just going to happen in the second quarter as opposed to the first quarter. And then just to talk a bit about gross margin and SG&A?

Melvin G. Tucker - *Genesco Inc. - Senior VP of Finance & CFO*

Yes. So on the margin line, we do expect margin will be a little lower in Q2 than it was in Q1. And really, this is a function of the fact that our e-comm penetration is exceptionally high right now. Shipping and warehouse expenses run along with that. The variable cost structure in e-comm is going to drive more cost in that regard, and it flows through the margin line. Also in the U.K., it's been very promotional. And we expect that it has continued for much of the quarter, and we expect that will continue. And then the last thing is I think there's going to be some pressure regarding inventory reserves, and it's just math in terms of if you look at how we value our inventory, it looks at weeks of supply and when the stores close, some of those numbers have come up. So we think there might be a few reserves that we might have to take in the second quarter. But at the end of the day, it's going to be a little lower than what it was in the first quarter. As it relates to SG&A dollars, we think that we're probably going to be in line with Q1, but we're probably going to be below Q2 dollars. And this is really just a function of us continuing to save on the things that we've saved previously. The biggest savings was in our selling salaries. We continue to save on the rent line with the U.K. property tax credits that we're receiving for government relief. And we're also going to save on percentage rent as well. So those lines will provide significant benefit. But at the end of the day, until the stores return to full volume, we're still going to be running below last year's level in terms of SG&A cost.

Mimi Eckel Vaughn - *Genesco Inc. - CEO, President & Director*

Yes. It's pretty dynamic, though. I think that, as you've heard, we've opened more stores and part of the ability to save expenses during the first quarter was a result of just having our stores completely closed. So it's really a dynamic relationship between how many stores we have opened and operating and what our expense structure is. We're working hard to -- in light of the loss sales through the course of the year to manage expenses really carefully, and we'll continue to do that through the course of the year.

Operator

(Operator Instructions) We will take our next question from Sam Poser with Susquehanna.

Samuel Marc Poser - *Susquehanna Financial Group, LLLP, Research Division - Senior Analyst*

I guess the first question I have is what -- you haven't talk about this, but could you give us some idea of what percent how big the e-commerce business is right now? What percent of your sales it was in the first quarter by brand or by (inaudible) or in total, so we can have some idea just to help us modeling and get some idea of at least some piece of the action we can review more carefully?

Mimi Eckel Vaughn - *Genesco Inc. - CEO, President & Director*

Yes, Sam, I hope you're doing well, too. The way to think about e-commerce and how big the business is that just the 64% comp in the first quarter. I think that looking at it, as we traditionally have, as a percentage of overall sales, probably isn't the right way to look at it these days just because so many stores were closed. The volumes were pretty astonishing in the -- in May. We talked about being up 300%. And I think that we're going to sustain some of that level of increased volume. But again, there's no question that stimulus money helped to propel those sales. And so last year, we were tracking to have e-commerce to be about 15% of our overall retail sales this year. I think, again, those proportions might not be meaningful. But I think that we will -- certainly, last year, we were growing our e-comm business at 20% in the first quarter. We grew at 64%. So I think the right way of thinking about that is is somewhere between that 20% and 64% is where we're going to end up being for the year.

Samuel Marc Poser - *Susquehanna Financial Group, LLLP, Research Division - Senior Analyst*

So I understand that. But I guess my question is, last year, was e-commerce 15% of sales last year? Or in Q1, how much...

Melvin G. Tucker - *Genesco Inc. - Senior VP of Finance & CFO*

It was about 13.

Mimi Eckel Vaughn - *Genesco Inc. - CEO, President & Director*

It was about 13% last year. We got a lot of variation across the quarters because there's a lot higher penetration in the fourth quarter. And we anticipated that we would hit about 15% this year. And look, if sales were normalized, we grow at more than a 20% rate, which is what we were growing at prior to the pandemic. So store sales are going to be down a lot, Sam, so the denominator is going to be less. And I think what's important is just to think about how much growth we're going to get out of e-com in terms of dollars.

Samuel Marc Poser - *Susquehanna Financial Group, LLLP, Research Division - Senior Analyst*

That's what I'm trying to figure out. So could you tell us by quarter of last year, what percent e-commerce was or what the e-commerce sales in dollars were by quarter last year? So we can at least have something to work with that because the stores have been closed.

Mimi Eckel Vaughn - *Genesco Inc. - CEO, President & Director*

Sure. So in terms of by quarter for last year, we'll have to give you the specific numbers. I think altogether, the -- as we said, e-comm was about 13% last year. E-comm is 50% higher in the fourth quarter, so I think you can back into the numbers for the first 3 quarters.

Operator

And we will take our next question from Jonathan Komp with Robert Baird.

Jonathan Robert Komp - *Robert W. Baird & Co. Incorporated, Research Division - Senior Research Analyst*

Maybe just one follow-up to the last question. I mean if e-commerce, I know you said it was planned originally to be 15% of sales this year. If it were to go something much higher, 20%, 25% plus, can you maybe just talk about the margin implications of VAT and thinking about getting back towards 4% or 5% operating margin over time, how the e-commerce mix is going to impact that?

Mimi Eckel Vaughn - *Genesco Inc. - CEO, President & Director*

Sure. That's a great question, Jon, because e-comm definitely has a different set of economics than our stores do. And I think I'd start by saying that our digital business is profitable. We have typically run our e-com channel to be profitable. And I think that, that is a result of traditionally not overspending on marketing just for this sense of driving sales. We also utilize other practices to ensure profitability like threshold for free shipping. E-comm is a more profitable channel than stores based on the way that we do our allocation. And so we actually leverage the investment we've been making over a wider base of sale. If we go to 20% to 25% of sales, we will grow e-comm . And we saw that in the first quarter. We actually saw that as we looked at the financials from May as well that e-comm is adding positively and profitably. So it isn't the case that for every e-comm sale we make that we hurt profitability. The challenge for that is that we also need sales in stores because of the heavily fixed expense base. Our expense base in stores is about 70% fixed. And so it's -- if all we did was grow e-comm a lot more and held store sales constant, we would become more profitable. But with the loss of store sales, that's really what ends up impacting the overall P&L.

Jonathan Robert Komp - *Robert W. Baird & Co. Incorporated, Research Division - Senior Research Analyst*

Okay. That's helpful. Maybe just one follow-up to that, Mimi. As kind of get past the period now where there is maybe a lot of natural traffic moving towards online. Do you have any view on the competition and the cost to drive the online traffic, what might happen?

Mimi Eckel Vaughn - *Genesco Inc. - CEO, President & Director*

Yes. Well, your point -- good point. Your question is a good question because we were seeing that the cost of certainly new customer acquisition and even paid search was going up pretty significantly. And part of what we saw during the pandemic is that while we increased our ad spending, that return on the ad spending was very strong. And I think that with more people interested in shopping online then you're spending dollars, even if you were spending the same amount would become more effective because there's more opportunity to be able to drive sales. Look, I think that, as in anything else, that things tend to normalize. I think that some customers will convert permanently to shopping e-comm. I think that we've probably accelerated the trends that we were seeing by 2 to 3 years. And so I think that what we'll end up normalizing is that paid search costs will end up normalizing to the new levels. I would hope we'll continue to see some of the increases in productivity, at least for the time being.

Jonathan Robert Komp - *Robert W. Baird & Co. Incorporated, Research Division - Senior Research Analyst*

Okay. That's really helpful. Just last one for me. On J&M, could you just maybe remind us how much today you'd say is more casual styles versus more traditional? And just how you see kind of the current trends with consumers being at home playing out for that brand and what you're doing?

Mimi Eckel Vaughn - *Genesco Inc. - CEO, President & Director*

Sure. I think that you know that J&M has traditionally been known as a dress resource. But over the last 10 years, we have done a -- the J&M team has done a tremendous job of not on;ly proliferating the footwear styles into more casual product, but also selling a lot of apparel and accessories. And what we have seen most recently is that the dress shoe business has been declining and that's because consumers have really liked some of the hybrid products that we have put out there with the athletic bottoms, but more dressy uppers. And so the growth that we have seen have been around casual and dress casual truck footwear is proportionately a lot less than our casual -- and dress casual today. If you look at our overall assortment, casual footwear is, by far, have the largest penetration in the first quarter, followed by dress casual and then dress footwear after that. And so our penetration of dress footwear is just a percentage has come down over time. And so we have less exposure to the dress category than we had in the past. In terms of consumers being at home and how is that going to play out for fashion, I mean, we definitely have seen that it's comfortable to be at home that we've seen some nice responses online to certainly anything related to comfort. We have a tremendous assortment of shirts. You're having to drop up your top and not necessarily bottom, so we have a tremendous assortment of shirts in our spring line, both conversational prints. Our knits have performed really well. And so that has been -- what has been driving our business for now. A lot of folks are sitting at home in their slippers, or no shoes at all. And -- but over time, again, we expect that as people get back to work, as people get back to a more normal lifestyle that the J&M customers potentially will shift back into into purchasing footwear. And I expect that, again, as in everything else that these trends that we've been seeing will accelerate. So I anticipate that after the pandemic that our casual assortment will skew even more in the casual direction.

Operator

And our next question will be a follow-up from Mitch Kummetz with Pivotal Research.

Mitchel John Kummetz - *Pivotal Research Group LLC - Senior Analyst of Footwear, Apparel Vendors and Retailers*

I've got a couple of follow-ups. So first off, I just want to drill down on the inventory a little bit. I was hoping maybe you could speak to -- I don't know if you can give like a percentage of what you're holding that's seasonal, specifically sandals. Do you see any excess within kind of that business? I know Mimi you said that kind of maybe what didn't sell in Q1, we'll sell in Q2. But I'm wondering if there's any concern about sandals and how are you thinking about any excess there in terms of liquidating it versus maybe carrying it over, if it doesn't sell? And then also on the inventory, how are you guys thinking about kind of the seasonal side of your business for the back half? Are you concerned about a potential second wave? And maybe potentially getting caught with some excess boots. And so you're maybe planning that side of the business conservatively versus things that are more sort of core basic. So just that on the inventory, then I had another one.

Mimi Eckel Vaughn - *Genesco Inc. - CEO, President & Director*

Okay. Great. So to speak to the percentage of inventory that is seasonal. I think about it more as the seasonal product in the spring and the summer is more the icing on the cake. We sell a lot of core product during the course of the spring and the summer, a lot of athletic product. I mean, our kids live in athletic shoes year-round. And so that's a big part of the assortment. Having said that, Journeys' had a really nice sandal package, and sandals have been driving sales. The customer is really taken with some branded stand offs and that seasonal assortment that during fit together was just really terrific of some fashion product. And so we are not worried about liquidating our sandal inventory and stores are opening up. That's some of what we're seeing as far as sales being risk around sandals. As far as seasonal inventory for the back half of the year, that's -- we sell boots in the back half. And so whether you want to call to seasonal or not, I think we think of this as a fashion. We will -- we continue to sell athletic year round. So we'll continue to carry some of our athletic assortment well into the back part of the year.

And on boots, clearly, I think that we're going to learn a lot more. Our merchant teams have been able to adjust really phenomenally to the differences in demand. They took down received pretty quickly when we thought demand would be less, and they're in the process of ramping it back up to prepare for back-to-school as we've opened more strongly than we thought. So we will -- we've placed our boot purchases, and we will adjust those purchases as we get more visibility over the course of the next few weeks and months. And I think we'll learn a lot more, and we'll have a lot more insight. We anticipate that there will be more inventory available in the channel. We've gotten access to product both in Journeys and in Schuh that we wouldn't, otherwise, get because people haven't taken their full allocation. And so we think that we'll have a lot of good flexibility to be able to do what we need to do in response to holiday into Christmas buying.

Operator

And that will conclude today's question-and-answer session. I would like to turn the call back to Mimi Vaughn for any additional or closing remarks.

Mimi Eckel Vaughn - *Genesco Inc. - CEO, President & Director*

Thank you for joining us today. We hope everybody stays healthy and safe and look forward to talking to you again in a few months, if not before.

Operator

And this concludes today's conference. Thank you for your participation, and you may now disconnect.
