GAP INC.

Gap Inc. Fourth Quarter Fiscal 2024 Conference Call Prepared Remarks
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Whitney Notaro – Head of Investor Relations, Gap Inc.

Good afternoon, everyone. Welcome to Gap Inc.'s Fourth Quarter Fiscal 2024 Earnings Conference Call. Before we begin, I'd like to remind you that the information made available on this conference call contains forward-looking statements that are subject to risks that could cause our actual results to be materially different.

For information on factors that could cause our actual results to differ materially from any forward-looking statements, please refer to the cautionary statements contained in our latest earnings release, the risk factors described in the company's Annual Report on Form 10-K filed with the Securities and Exchange Commission on March 19, 2024, and any subsequent filings with the Securities and Exchange Commission, all of which are available on gapinc.com.

These forward-looking statements are based on information as of today, March 6th, 2025 and we assume no obligation to publicly update or revise our forward-looking statements.

Our latest earnings release and the accompanying materials available on gapinc.com also include descriptions and reconciliations of any financial measures not consistent with Generally Accepted Accounting Principles.

Joining me on the call today are Chief Executive Officer Richard Dickson and Chief Financial Officer Katrina O'Connell.

With that, I'll turn the call over to Richard…

Richard Dickson – Chief Executive Officer, Gap Inc.

Good afternoon and thank you for joining us today.

I'm excited to share with you our strong fourth quarter results, which rounded out an exceptional year for Gap Inc. We continued to perform while we transform, delivering another quarter that exceeded financial expectations and underscored the meaningful progress we're driving across our strategic priorities.

Operational and financial rigor is the fabric of how we work and has delivered solid metrics that Katrina and I will discuss during this call. This discipline has enabled us to execute effectively against our brand reinvigoration playbook and at the same time strengthen our platform by building and sharpening our operational capabilities with highlights on supply chain and technology. And we continued to energize our culture, empower our global team, and attract great new talent.

I want to begin by taking a moment to thank our global team for their partnership and collaboration this past year. Their relentless dedication to our transformation has been instrumental in driving the progress we've made.

Let me share some highlights on the progress we achieved in 2024:

- Gap Inc. delivered positive comps in all four quarters, with all four of our brands comping flat to positive for the year demonstrating consistency and strength across the portfolio.
- Gap Inc. gained market share for the 8th consecutive quarter, reflecting that our brands are resonating with consumers.
- We achieved one of the highest gross margins in the last 20 years, a clear result of our focus on financial and operational rigor.
- We increased operating income by more than $500M and operating margin by 330 basis points vs. last year's adjusted rate, while we continue to drive efficiencies in our cost structure.
- And we delivered a full year EPS of $2.20, the highest since 2018, demonstrating our earnings power as we drive toward becoming a high performing company that generates sustainable, profitable growth.

Looking ahead, we have more work to do but we are building on a much stronger foundation. 2025 represents an exciting step in our ongoing transformation, as we begin to transition our focus from fixing the fundamentals to continuous improvement through innovation and pave the way for momentum in the years ahead.

Since this is our year-end call, our remarks today will be a little longer than usual as we have a lot to cover. I'll begin by providing an update on our fourth quarter performance and progress in the context of our strategic priorities. Then, Katrina will walk you through our detailed financial results and share our outlook before we open the call for questions.

Let's start with our first strategic priority, financial and operational rigor…

Gap Inc. comparable sales were up 3% in the quarter with:

- Comps at Old Navy, our largest brand, also up 3%. This is the brand's 8th consecutive quarter of market share gains reinforcing its leadership position as the #1 specialty apparel brand and retailer in the U.S.
- Gap comps accelerated to 7%, the 5th consecutive quarter of positive comps, and the brand delivered its 7th consecutive quarter of market share gains.
- Banana Republic comps were up 4% and gained share as a result of our focus on reestablishing this premium brand in our portfolio.
- Athleta had a more challenging quarter, with comps down 2% while maintaining market share with more work to do as we continue to reset the brand.

We delivered SG&A in-line with our expectations and expanded operating margin 120 basis points versus last year. EPS was $0.54, up 10% versus the fourth quarter of last year. We ended the year with strong cash balances of approximately $2.6 billion and generated $1 billion in free cash flow in fiscal 2024.
Brand Reinvigoration

Turning to our next strategic priority, we remain focused on driving relevance and revenue by executing on our brand reinvigoration playbook. Each brand is at a different point in the process, and I am encouraged by the improvements we've driven across the portfolio.

Let's start with Old Navy…

In 2024, Old Navy delivered one of the highest annual net sales in the brand's history and was the #1 specialty apparel brand and retailer in the U.S. We've been connecting our customers with products they want through compelling storytelling and executing with clarity in pricing and in-store navigation. The brand is gaining more relevance as demonstrated by our digital dialogue, notably our strong social and influencer engagement. As a result, we finished the year strong with a 3% comp in the quarter and the 8th consecutive quarter of market share gains.

Our strategic pursuit in both denim and active this year led to a consistent drum beat of innovation and newness across these key categories. We have been putting insights into action with product innovation, leveraging our scale and expertise, and executing with excellence – and the results are showing up on the scoreboard.

Old Navy leaned into denim with an expanded offering, a dynamic in-store and online experience, supported by a fall campaign expressing our evolving brand identity work. In the fourth quarter, we increased share in denim, driven by our on-trend assortment in wide and loose fits as well as barrel.

On our third quarter earnings call, we spoke about the exciting opportunity we see for Old Navy to become the destination for the family as the value player in the active category. During the year, the brand grew to be the #5 player in the category and the only brand among the top 5 to gain share. And we are not stopping there. In the fourth quarter, Dynamic Fleece and Powersoft were great examples of innovation that drove Old Navy's strength in the active category and we are bringing more innovation, style and value in 2025 with our recently launched StudioSmooth collection. This new fabrication brings exceptional comfort and value to consumers and marks another step forward in our expansion within the active category.

Old Navy's merchandising narratives and style are presenting better, and our in-store and online communication has improved with more clarity around pricing and more compelling marketing promoting great value. This evolution of the customer experience has resulted in higher NPS scores for both stores and online. With the foundational elements we've established, we are a stronger Old Navy than we were a year ago and are positioned well for 2025. In the year ahead, Old Navy will be focused on ongoing innovation in key categories, driving big ideas with storytelling while mobilizing an enhanced customer experience.

Recognizing the work achieved and the metrics delivered shows the powerful position Old Navy holds in our portfolio and in our industry, and we continue to believe there is significant growth potential ahead for the brand.

Now, let's turn to Gap…

Gap is back in the cultural conversation. This brand was built on strong product narratives with brilliant marketing, expressed through big ideas, and over the past year, each of these were reignited. The team has been executing the brand reinvigoration playbook with excellence and it's showing up in the results. Gap's comp accelerated to 7% in the quarter, marking the 5th consecutive quarter of positive comps and the highest quarterly comp in 3 years. In the fourth quarter, the brand also achieved the 7th consecutive quarter of share gains as the brand continued to resonate with consumers.

This strong performance was fueled by innovation, product newness and compelling marketing with a social-first approach. The momentum in women's continued in the fourth quarter, men's also performed well and we began to see improvement in kids and baby. Our focus on big ideas resonated with strength in key categories like fleece, denim and sweaters, driven by the performance of Cashsoft, our innovative fabric, all of which were amplified by our Give Your Gift holiday campaign.

The brand campaigns and collaborations are attracting a new generation to Gap while reinforcing the brand to those who have loved us for years. In 2024, we expanded our customer base and saw increased engagement with the brand as a result of our trend-right product and culturally relevant messaging. And we're building on that momentum in 2025 with our latest fashiontainment moment released last week featuring Parker Posey, dancing to METTE's "Mama's Eyes" -- a celebration of the confidence that comes from feeling comfortable in your clothes and in your own skin, which is resonating and bridging the generation gap all over again.

Our legacy inspires us to pursue the significant potential this brand has, and with consistent execution of our playbook, we are excited about the brand's growth potential in the years ahead.

Now moving on to Banana Republic...

There's been a lot of progress at Banana Republic as we continue to focus on re-establishing the brand to thrive in the premium lifestyle space. The brand successfully implemented fundamental fixes throughout the year – leaning into classics, more precise assortments, focusing on fit and rebuilding trust – and we're beginning to see signs of stabilization with the early results showing up in the fourth quarter. Comps were up 4% with market share gains.

Women's drove the acceleration at the brand with better fundamentals across pricing, product and design which translated incredibly well, most notably for holiday occasion dressing. The brand continued to build on the strength in the men's division and leaned into classics with a stronger cashmere point of view, which resonated with consumers.

The work the Banana Republic team has done to improve women's and strategically redeploy marketing to more culturally relevant storytelling is starting to deliver results. I am confident Banana Republic is positioned well for continued progress in 2025 and beyond.

Shifting to Athleta...

In 2024, Athleta stabilized revenue, delivering a flat comp and improvements across several key metrics. The brand re-entered the cultural wellness and sports conversation through major activations that engaged key brand partners like Simone Biles and Katie Ledecky on the world stage in Paris, and most recently Lexie Hull and Kate Martin. In addition, we meaningfully increased the number of new and reactivated customers. I'm encouraged by Athleta's ability to maintain its rank as the #3 brand in the Women's active category this year and the only brand in the top 3 to gain share.

Despite this progress, the year was not without challenges and volatility. This was reflected in the fourth quarter when the brand delivered a negative 2% comp, missing our expectations. Despite a strong start to the holiday season, Athleta struggled to keep up its core loyal customers engagement during the peak holiday shopping moments. In 2025, we will be strengthening our product and ensuring newness to excite our core customer base while continuing to inspire new customers.

Athleta has made progress in a number of areas this past year, however we are still in the process of resetting the brand which in the near term may result in choppy quarterly performance. We have more work to do to implement our reinvigoration playbook and realize the brand's full potential. Our ambitions for Athleta remain high.

Moving to our third strategic priority, strengthening the platform…

Today, Gap Inc.'s platform creates significant value with the benefit of scale across our global supply chain supporting a fleet of more than 3,500 stores, a technology platform that enables one of the largest e-comm businesses in the U.S. as well as an active customer file of over 55 million.

I was impressed with the resilience and agility of our supply chain as we successfully navigated a number of disruptions during the year. This will serve us well as we continue to navigate a highly dynamic environment, top of mind being tariffs, which Katrina will address in her remarks.

In 2024, we began to cultivate a digital-first organization and mindset, building and sharpening our operating capabilities to improve effectiveness and efficiency, and in turn, drive increased cost leverage and demand creation. Sven Gerjets, our Chief Technology Officer who joined us last summer, began pursuing plans to leverage technology to enable both our business performance and our transformation. This included standing up an Office of AI, focused on driving AI innovation across our strategic priorities over time - with early use cases primarily related to employee enablement. In 2025, we will be developing AI monetization opportunities relative to the consumer experience, product to market, as well as organizational productivity. Now having organized the various ways we can use AI to enable value creation, we're prepared to mobilize against this framework with intention.

Our financial and operational rigor is allowing us to find efficiencies and cost savings that we plan to reallocate to invest in new platform capabilities to support the ongoing success of our brands. As our focus shifts toward continuous improvement in 2025, we will be optimizing-for-growth by cutting low value projects to fuel high-value opportunities. We see significant organic growth potential through smart and targeted investments in areas like design, consumer insights and store operations that deepen the execution of our playbook and seed new avenues for future growth.

Reflecting on our fourth priority, I'm proud of how our teams have stepped out of their comfort zones to embrace new ways of working. Getting comfortable with the uncomfortable creates resilience and the resilience of this organization is showing up as we continue to perform while we transform. A great strategy can only go so far without a culture that is united and mobilized behind it and the energy of our people is impressive, and it's fueling creativity and driving executional excellence.

Transformations of this scale take time and we've been deliberate about taking a phased approach. In 2024, we were focused on fixing the fundamentals and made significant progress. As we look ahead, we are beginning to focus on continuous improvement through innovation to pave the way for momentum in the years ahead. We are stronger today and have consistently proven our ability to navigate a highly dynamic macro environment while delivering results. Gap Inc. has a powerful portfolio of brands that matter, and we're proving that they can matter more.

Our playbook is working and showing up in comp growth and share gains and we are well positioned for organic growth over time. We continue to unlock efficiencies in the business and deploy savings into high potential growth opportunities. Our financial and operational rigor is driving operating margin expansion and generating significant cash flow, allowing us to invest in the business while returning cash to shareholders through dividends and share repurchases.

I'm pleased with what we've been accomplishing so far, but our aspirations are high, and we have more work to do. We remain focused on controlling the controllables and successfully executing our strategic priorities, continuing to be market share winners in any environment.

I'll now turn the call to Katrina for a closer look at our financials…

Katrina O'Connell – Chief Financial Officer, Gap Inc.

Thank you, Richard, and thanks everyone for joining us this afternoon.

Our strong finish to the year, reinforces the power of our portfolio of iconic American brands that shape culture and our confidence that our transformation is taking hold. The meaningful progress we've made on our strategic priorities is showing up in the results, with a return to topline sales growth for the year, resulting in share gains, and all brands showing signs of reinvigoration. The discipline we've developed has enabled significant margin expansion and earnings growth, and our rigor in expense and inventory management drove substantial operating and free cash flow generation, resulting in a strong balance sheet. The reinvigoration of our brands, combined with our financial and operational rigor, is enabling us to perform while we transform, consistently delivering on our commitments as we continue to strengthen our performance.

Some key highlights from fiscal 2024 include the following:

- It's exciting to see the brand reinvigoration driving results with Gap Inc. comparable sales up 3% and all four of our brands comping flat to positive for the year, which is notable as we execute on our reinvigoration playbook.
- This was Gap Inc.'s 2nd consecutive year of market share gains driven by wins across our brand portfolio.
- Gross Margin in fiscal 2024 expanded 250 basis points versus last year. This progress reflects both the increased relevance of our product and brands and our disciplined inventory management.
- We tightly managed SG&A dollars below the prior year and in-line with our beginning of year outlook. With our focus on expense management and financial rigor, we realized efficiencies in our cost structure that more than offset variable costs from higher sales as well as wage inflation.
- This resulted in operating income of $1.1 billion, growing 83% compared to last year's adjusted operating income, and an operating margin of 7.4% for fiscal 2024, a 330-basis point improvement versus last year's adjusted operating margin.

- And we achieved over 50% growth in full year earnings per share to $2.20.
- We ended the year with $2.6 billion of cash, cash equivalents and short-term investments on the balance sheet, net cash from operating activities of $1.5 billion, and generated $1 billion in free cash flow.
- And we returned approximately $300 million in cash to shareholders through dividends and share repurchases.
- This strong performance gives us confidence in the 2025 outlook we provided today which reflects continued sales growth, with gross margin expansion and SG&A leverage resulting in another year of operating income growth.

Turning to our detailed results for the fourth quarter:

Net sales of $4.15 billion decreased 3% year over year, inclusive of the 7-percentage point negative impact related to the loss of the 53rd week.

Net sales for the quarter were negatively impacted by the weekly shift related to the 53rd week dynamic, as well as the loss of the extra week. For that reason, I'll be referencing comparable sales by brand as we believe it's more indicative of each brand's underlying performance.

Gap Inc. comparable sales were up 3% in the quarter.

By Brand…

Starting with Old Navy, comparable sales were up 3%. The brand continued to win in key categories, like active and denim, with innovation and newness driving strength and market share gains.

Turning to Gap brand, comparable sales meaningfully accelerated, up 7%. Gap has been reignited and is executing the brand reinvigoration playbook with excellence driving relevance and revenue.

Banana Republic comparable sales were up 4%. The brand saw notable improvement in its women's business during the quarter and continues to build on its strength in men's.

Athleta comparable sales were down 2%. While the brand maintained market share in the fourth quarter, it did not meet our expectations, and the team will be taking away important learnings and insights for 2025 as we continue to reset the brand.

Gross margin of 38.9% was flat year over year as merchandise margin expanded 20 basis points and ROD deleveraged 20 basis points in the quarter.

SG&A was $1.35 billion in the quarter, $105 million below last year and in-line with our outlook as we demonstrated continued rigor in expense management. SG&A as a percentage of net sales was 32.6%, leveraging 130 basis points versus last year primarily due to the timing of incentive compensation accruals as well as lower advertising costs in the quarter.

Fourth quarter operating margin of 6.2% improved 120 basis points compared to last year's operating margin.

Earnings per share in the quarter were $0.54, up 10% versus last year's earnings per share of $0.49.

Now, turning to full year fiscal 2024 results.

Net sales of $15.1 billion increased 1% year-over-year, up about 2% on a 52-week basis, at the high end of the guidance range we provided.

Gross margin of 41.3% expanded 250 basis points versus last year, ahead of our expectations. Merchandise margin expanded 210 basis points. ROD leveraged 40 basis points primarily due to higher sales in the year.

SG&A was $5.1 billion, $100 million below last year and in-line with our outlook. As a percentage of net sales, SG&A was 33.9%, leveraging 110 basis points versus last year's reported rate and 80 basis points versus last year's adjusted rate.

Fiscal 2024 operating income was $1.1 billion, growing 83% compared to the prior year's adjusted operating income of $606 million, and ahead of our guidance of mid-to-high 60% growth. Operating margin expanded 330 basis points versus last year's adjusted rate to 7.4%, our highest annual operating margin since 2018.

Earnings per share for the year were $2.20, up 64% versus last year's reported EPS of $1.34 and up 54% versus last year's adjusted EPS of $1.43. This demonstrates the value creation we've begun to unlock in this early stage of our transformation and indicates the earnings power of Gap Inc. as we continue to perform while we transform.

Now turning to the balance sheet and cash flow.

We maintained disciplined inventory management, ending the year with levels up 3.6% year-over-year. The increase was primarily due to the timing of in-transit inventory as we navigated macro-economic conditions. Excluding the higher in-transit, we maintained our inventory principle, managing a healthy stock to sales ratio, with inventory lagging sales growth and were able to finish the year with what we believe is the right inventory composition going into fiscal 2025. With the rigor and discipline that is now core to how we operate, we expect our 2025 inventory to continue to align with this principle.

We ended the year with cash, cash equivalents and short-term investments of $2.6 billion, an increase of 38% from last year. Full year net cash from operating activities was $1.5 billion. Free cash flow of $1 billion for the year demonstrates the rigor we have put into managing the business.

Capital expenditures for the year were $447 million.

During the year, we returned $225 million to shareholders in the form of dividends, representing annual dividends of $0.60 per share.

And during the fourth quarter we repurchased 3 million shares for approximately $75 million.

With a strong balance sheet, we and the Board consistently evaluate capital allocation as we strive to maximize shareholder value. Our balanced capital allocation framework is as follows:

- Our number one priority is to invest organically in the business through capital expenditures to the degree we believe we can drive strong returns. Capital expenditures in 2025 are expected to be about $600 million for the year, up 34% as we utilize our strong balance sheet to invest in the organic opportunities for value creation that we see in our business.
- Second, we believe in paying an attractive dividend as a key component of shareholder return. Our goal is to increase the dividend as net income grows and we evaluate both the payout ratio as well as the yield. In line with that principle, on Feb. 25th our Board authorized a 10% increase to our first quarter fiscal year 2025 dividend per share.
- Third, our principle regarding repurchasing shares is to offset dilution over time. Our fourth quarter share repurchase of $75 million marked our first repurchase since 2022, reflecting our confidence in the business and our future. As a reminder, we have approximately $400 million remaining under our current share repurchase authorization.

Our strong balance sheet gives us the foundation to focus on capital allocation with the goal of enhancing long-term shareholder value.

This has been an incredible year in which our four strategic priorities have resulted in a return to profitable sales growth. I want to thank our teams for their commitment and tremendous contributions that fueled these strong results. With our momentum and the clear opportunities to drive continuous improvement across the business, we are confident in our ability to strengthen our performance in the year ahead.

Now, turning to our outlook for fiscal 2025...

We've been operating in a highly dynamic backdrop for the last few years, and we're expecting the same for fiscal 2025. As a result, we've taken a balanced view with our guidance and remain focused on controlling the controllables. Specific to tariffs, in fiscal 2024, we sourced less than 10% of our product from China, and less than 1% of our product from Canada and Mexico combined. Our fiscal 2025 outlook is informed by what we know today regarding tariff policy and includes any expected margin impact, albeit small, from current actions related to those countries.

Starting with full year 2025 revenue, we expect net sales for the year to grow approximately 1% to 2% year-over-year, including an estimated 30 basis point unfavorable impact from foreign currency due to a stronger U.S. dollar. Our outlook assumes ongoing strength at Old Navy and Gap, stabilizing performance at Banana Republic and a longer recovery timeline at Athleta. An important note regarding the quarterly cadence for the year, in the second quarter we will be lapping the 2-percentage point benefit we saw last year from the incremental revenue related to our credit card agreement which we do not expect to recur this year.

Moving to gross margin…

We are proud of the significant gross margin gains we achieved in 2024 as we returned to historically high levels. Our goal in 2025 is to sustain these gains and build upon them through continued rigor and executional excellence. With that, we expect gross margins to expand slightly for the year, with roughly equal amounts coming from ROD leverage and merchandise margin.

Turning to SG&A…

We are driving continuous improvement in the cost structure of the company as we rigorously drive savings in our core operations through efficiency and effectiveness. Our outlook reflects approximately $150 million in cost savings and efficiencies through better operations. A portion of which will be reinvested for future growth with the balance offsetting continued inflation. With this in mind, we expect SG&A to leverage slightly for the full year.

Considering our expectations for approximately 1-2% net sales growth combined with slight gross margin expansion and SG&A leverage, we see a clear path towards delivering 8% to 10% operating income growth in fiscal 2025. This growth rate includes an estimated 2-percentage point unfavorable impact from foreign currency due to a stronger U.S. dollar.

We expect net interest income to be approximately $15 million for the year, with a quarterly cadence that reflects seasonality similar to fiscal 2024.

We are planning for a 2025 tax rate of approximately 26%.

We are expecting approximately 35 net store closures during the year, with the majority of closures at Banana Republic.

Now, let me share some color on our outlook for the first quarter of fiscal 2025.

We expect net sales in Q1 to be flat to up slightly year-over-year. This includes an estimated 50-basis point headwind related to foreign currency due to a stronger U.S. dollar and contemplates our quarter-to-date performance. While the cold start to February was somewhat unfavorable, we are pleased with what we've seen as the weather has normalized.

As it relates to first quarter gross margin, we expect gross margins to expand slightly compared to last year's gross margin of 41.2%.

And we are planning for SG&A to leverage slightly versus last year in the first quarter.

As I reflect on the year, I am proud of the significant progress we've made across our strategic priorities. The reinvigoration of our brands is driving sales growth and consecutive market share gains, which, when combined with our rigor, is delivering meaningfully improved financial performance. We look forward to building on the success of 2024 in the year ahead as we drive toward becoming a high performing company that generates sustainable, profitable growth, and delivers long-term value for our shareholders.

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