FY25 Q2 Earnings Release Conference Call Transcript

December 19, 2024

[OPERATOR]

Good afternoon, everyone. Welcome to NIKE, Inc.'s Fiscal 2025 Second Quarter Conference Call. For those who want to reference today's press release, you'll find it at investors.nike.com.

Leading today's call is Paul Trussell, VP of Corporate Finance and Treasurer. Now I would like to turn the call over to Mr. Paul Trussell. Please go ahead, sir.

[PAUL TRUSSELL]

Thank you, operator. Hello, everyone, and thank you for joining us today to discuss NIKE, Inc.'s fiscal 2025 second quarter results. Joining us on today's call will be NIKE, Inc.'s President and CEO, Elliott Hill; and our CFO, Matt Friend.

Before we begin, let me remind you that participants on this call will make forward-looking statements based on current expectations, and those statements are subject to certain risks and uncertainties that could cause actual results to differ materially. These risks and uncertainties are detailed in NIKE's reports filed with the SEC. In addition, participants may discuss non-GAAP financial measures and nonpublic financial and statistical information.

Please refer to NIKE's earnings press release or NIKE's website, investors.nike.com for comparable GAAP measures and quantitative reconciliations. All growth comparisons on the call today are presented on a year-over-year basis and are currency neutral unless otherwise noted.

We will start with prepared remarks and then open up for questions. We would like to allow as many of you to ask questions as possible in our allotted time, so we would appreciate you limiting your initial question to one. Thanks for your cooperation on this.

I'll now turn the call over to NIKE, Inc. President and CEO, Elliott Hill.

[ELLIOTT HILL]

Thank you, Paul. Hello, everyone, and happy holidays. In my first call, I want to start by saying how energized I am to be back at NIKE, working alongside my teammates. I look forward to the journey that lies ahead for all of us.

When I retired in 2020 after 32 years, I continued to stay in touch with many of my teammates and cheered them on from the sidelines. Why? Because I have an irrational love for this company. I know NIKE inside and out, take pride in what the brand stands for and want to see the company succeed. And in a moment where our team, brand and business are being challenged, my singular focus is to help get us back on track to get back to winning.

Today, I'm going to share what I've seen and heard in my first 2 months. I will then outline some of the immediate moves we're making to reposition the business. I'll tell you this. We, the entire NIKE team, feels a sense of urgency here.

My full leadership team and I went on the road the past few weeks to meet our teammates, partners and consumers to get a first-hand view of our brand and business. We went to L.A., New York, Amsterdam, London, Paris, Shanghai, Beijing. Together, we walked the high streets and shopping malls of those cities to see how consumers are experiencing our brand at retail. I met with key wholesale partners in each geography, all of which I already know and have developed deep relationships with over the years. I met with the commissioners of the NFL, NBA and WNBA, MLB and NWSL, the heads of the top NCAA conferences and teams like PSG and past and present athletes like MJ and Ronaldo to Sabrina, Asia and Erling. I visited our distribution centers in Memphis and Laakdal and had calls with our top 5 manufacturing partners to understand the evolution of our supply chain as we've grown the business.

It was important to me that I spent my first 60 days personally collecting these deep and direct insights. Across the board, our partners are energized. The people I talked with are rooting for a strong NIKE, because when NIKE is at its best, we bring excitement. We invite consumers into the world of sport and sport culture. And when we do that, we help grow the overall marketplace. That's good for consumers, that's good for our partners, and that's good for NIKE.

The consistent feedback we've heard is pretty simple: Let's see more of NIKE being NIKE, and that starts with leveraging all the advantages that make us great. Three of the world's most iconic brands, a dominant roster of athletes, teams and leagues, unmatched patented innovation, a deep catalog of products at every price point, teams positioned to serve consumers across 190 countries, a full integrated marketplace across multiple channels, strong, long-standing relationships with leading suppliers and manufacturing partners and most importantly, passionate, highly talented and committed teammates.

Lately, we haven't been maximizing these strengths. From everything I heard and observed, there are clear themes about the recent state of our business and where we need to go. I'll start with a high-level observation. We lost our obsession with sport. Moving forward, we will lead with sport and put the athlete at the center of every decision. The sharpness in each sport is what differentiates our brand and our business and fuels our culture.

Another observation is that the reliance on a handful of sportswear silhouette is not who we are. We will get back to leveraging deep athlete insights to accelerate innovation, design, product creation and storytelling. Sport is what authenticates our brand.

I also see that we've shifted investments away from creating demand for our brand to capturing the brand demand through performance marketing for our digital business. We will reinvest in our brands to create stories that inspire and emotionally connect with our consumers during important sports moments and critical product launches.

When visiting our teams around the world, it was clear. centralization has impacted the resources we have in key countries and key cities. We will rebalance resourcing and empowering our teams on the ground to win with the everyday athletes and influencers.

My last observation. Prioritizing NIKE Digital revenue has impacted the health of our marketplaces. We will build back an integrated marketplace across NIKE Direct and wholesale, our marketplace will be consumer-led. Putting our best product and presentation in the path of the consumer wherever they choose to shop.

And ultimately, with sport as our North Star, we will reenergize our culture and identity. We believe we have one of the strongest mission statements of any one and that is to bring inspiration and innovation to every athlete in the world. To me, inviting 8 billion athletes into sport is a pretty powerful purpose.

One question I know you want to ask me is if we have the talent at NIKE? And are they motivated? The short answer to both is yes. I've grown more and more confident, as I've traveled around the world and saw our teams engaging with each other, with our consumers and with our partners. It's also been great to see how much expertise we've added since I've been away in spaces like supply chain, product creation, technology, materials, sports science, you name it. Our talent is world-class. Everywhere I've been, the teams are inspired and ready to go. I feel the optimism. We will win, and we will do it as a team.

What our teams right now need right now is clear direction and focus. We built this company on the guiding principles of world class management of product, brand and marketplace. We create innovative and coveted products, tell emotional inspiring stories through our brand and execute in a way that grows the entire marketplace, digital and physical, wholesale and NIKE Direct.

My leadership team and I have already identified key near-term actions in each area, and we've got to move fast. First, in product. We're getting sharper on specific sports. We're shifting into sport-led teams segmented by men's, women's and kids, and we call each of them fields of play, and it is a segment to grow approach. Throughout our history, we've utilized inflection points to further segment our businesses to unlock the next wave of growth. We will do this by empowering more nimble cross-functional teams to obsess in the needs of sports-specific athletes by gender, the approach enables the team to identify new opportunities, fuel innovation and drive incremental growth by sport and by gender.

Breadth and depth and how we orchestrate our complete product portfolio have always been strengths of NIKE. We will return to the discipline of franchise management that I was a part of for so many years. We've already started managing the inventory in our marketplaces and will move faster to return to a pull market for our largest classic footwear franchises. At the same time, the team has been planting the seeds of the next franchises that will fuel growth. In the quarter, some of our most sought-after products are franchises that are distinctly NIKE, the Pegasus 41, NIKE Shox and the Kobe lineup. And we're building anticipation for what's ahead, unveiling the Vomero 18 and Pegasus Premium to passionate runners at the running event in my hometown a few weeks ago.

There's still work to do in rounding out the portfolio, but I'm really encouraged by the innovation coming from our fields of play in the next several seasons, especially in the high-volume areas like running, training, sportswear, and core product and the Jordan Brand lineup.

Turning to the NIKE Brand. There are moments when we need to create impact that's felt around the world, and day-to-day work that connects emotionally with local communities. We will deliver bold, creative marketing that leverages our athletes in sport moments, and drive the ground game authentically in neighborhoods. To do that, we're going to be much more intentional about investing to move the brand forward.

We're already moving in that direction. The marketing team delivered moments this quarter that got us back to owning the conversation in Sport. From the Liberty's first WNBA championship to the Dodgers World Series win to Saquon Barkley's reverse hurdle, to city takeovers at the Berlin, Shanghai, New York City and Chicago marathons.

We're also going to continue to be aggressive in sports marketing. In just the last 60 days, we've announced the re-signing of the NBA and the WNBA, the Brazil Football Confederation, FC Barcelona and last week, the NFL. We drive growth through sports most iconic partners. Their athletes are the creative fuel for our brand. They power our innovation agenda, our brand voice and our revenue.

Inspiring the consumer includes being part of the active communities who run, train and compete locally, it's about showing up and building relationships every day with athletes and influencers. My visits to the geos the past few weeks only reinforced my conviction that we need to get back to empowering our teams in key countries and key cities.

I know for my years of working in our geographies, they're the ones creating emotional consumer connections in their neighborhood. They're the ones identifying the insights that inform our offense. We will resource our key country and key city teams to create stronger consumer connections, build relationships with athletes, influencers and partners and unlock incremental growth for our brand and business.

We're optimistic about the actions that are already underway in product and brand, but we're still in the early innings of elevating the marketplace, both in NIKE Direct and with our wholesale partners. What I've seen is traffic in NIKE Direct, digital and physical, have softened because we lack newness in product and we're not delivering inspiring stories. The result is we become far too promotional. We've moved to a push model.

Entering the year, our digital platforms were delivering roughly a 50-50 split of full price to promotional sales. The level of markdowns not only impacts our brand, but it also disrupts the overall marketplace and the profitability of our partners. We will return NIKE Direct, digital and physical, to premium destinations that lead the sports industry, that'll elevate the consumer experience and be the ultimate representation of the NIKE brand. It's where we'll offer our most complete assortments, tell deep product stories, and share our passion for sports.

Being premium also means full price. We'll focus promotions during traditional retail moments, not at the consistent levels we are today. And we will leverage NIKE value stores to profitably move through any excess inventory. The final action we prioritize is building back and earning the trust of our key wholesale partners. Some partners and channels feel we've turned our back on them, and we stopped engaging consistently. I've connected with many of them directly. Ed and Lauren at Dick's; Régis and Mike at JD Sports; Marriott, Foot Locker, Heinrich at the Deichmann Group; Michael at Sports Direct; Mr. Yu with Topsports; Mr. Yu and Mr. Wang from Pou Sheng; and Juan Carlos at Innova Sport. They're all encouraged by our commitment to delivering new innovative products, telling emotional and inspiring stories and elevating NIKE Direct. Their confidence is building in our product pipeline, and they welcome the closer collaboration as we invest more in their business.

We know our sales teams will have to earn every open-to-buy dollar, but we're investing to make sure our partners feel supported. We'll give them access to our best products and the breadth and depth they need, educate their teams on the latest NIKE innovation and provide them with the marketing support, both in-store and out-of-home. We'll do more than just sell in our products. We'll actively support mutually profitable sell-through. Simply put, we will win when our partners win.

Before I hand it off to Matt, I just want to say it's been an incredibly rewarding first 2 months. It feels great to be back with my NIKE teammates. This isn't going to be easy, but we're ready for the challenge. After spending so much time with my team in the past few weeks, I'm confident we are all aligned and focused on the areas that will make the most immediate impact.

I'll list the near-term priority actions again: ignite our culture through a focus on obsessing sport and getting back to winning; accelerate a complete product portfolio driven by athlete insights through sport-led fields of play; increase investment in our brand to deliver big, bold marketing statements; invest in and empower our teams in key countries, in key cities to win the ground game; elevate the marketplace through a more premium NIKE Direct and an unwavering commitment to our wholesale partners.

Some of these actions are already underway and some need to move faster, and I will continue to evaluate and assess what is needed. I recognize that some of these actions will have a negative impact on our near-term results. But we're taking a long-term view here. We're making the decisions that are best for the health of our brand and business, decisions that will drive shareholder value. I strongly believe NIKE's path to sustainable, profitable growth will be through sport.

And with that, I'll turn it over to Matt to cover some of the specific quarter results and our financial outlook before we take some questions.

[MATT FRIEND]

Thank you, Elliott, and hello to everyone on the call. To start, our Q2 financial performance largely met our expectations as we continue to make progress repositioning our business. Today, I will focus my remarks on our recent performance and outlook. First, I will start by reviewing our Q2 financial results. Then I will go deeper into our performance in the quarter, including marketplace trends, portfolio highlights and operating segments. And last, I will review our near-term outlook, including strategic actions introduced by Elliott to accelerate our pace in stabilizing the business and reigniting brand momentum.

This quarter, revenues were down 8% on a reported basis and down 9% on a currency-neutral basis, reflecting ongoing headwinds from our franchise management actions. We continue to drive the biggest reductions to our classic footwear franchises on NIKE Direct, which was down 14%, with NIKE Digital declining 21% and NIKE stores declining 2%. Wholesale was down 4%.

Gross margins declined 100 basis points to 43.6% on a reported basis due to higher markdowns on NIKE Direct, wholesale discounts to liquidate inventory and channel mix headwinds, partially offset by lower product costs and strategic pricing actions. SG&A was down 3% on a reported basis. While we increased investment in areas such as sports marketing, this was more than offset by lower wage-related expenses and timing shifts and other demand creation expenses. Earnings per share was $0.78.

Now let me go deeper into the quarter's performance. Q2 marketplace trends largely reflected the challenges that Elliott outlined, with traffic and retail sales across the marketplace falling below our expectations, especially in September and October. In November, we saw momentum build with digital and physical traffic inflecting positive, especially around the quarter's biggest consumer moments. In North America, Black Friday week was our largest demand week ever on NIKE Digital with sales up double digits. In Greater China, our 11/11 performance exceeded plan.

However, on NIKE Digital, our off-price mix was up high single digits versus the prior year, with performance marketing increasing over the same period. As Elliott said, NIKE Digital has become a platform where we have been capturing demand and competing with our wholesale partners rather than creating and growing demand for our brands. This is why we must elevate the consumer experience, grow organic traffic and drive full demand.

Next, inventory was flat versus the prior year. as elevated supply in North America and Greater China was offset by declines in EMEA and APLA. Footwear inventory declined, while apparel and accessories inventory increased to support marketplace growth. On a year-over-year basis, these trends were partly driven by timing-related factors. That said, inventory levels are higher than we would like, especially given recent sales trends on NIKE Direct.

Partner-owned inventory declined versus the prior year. We took some steps this quarter, and we plan to accelerate inventory actions in our second half to drive a return to a healthy marketplace. In particular, we are moving aggressively to reduce aged inventory, adjust supply with demand on NIKE Digital and ensure we have marketplace capacity for our newest product assortments.

Turning to our portfolio. This quarter showed progress in key areas, especially as our teams get back on the offense and support with consumers. Overall, our sport performance fields of play grew year-over-year, offset by a double-digit decline in sportswear. In training, men's was up high teens; women's, up high single digits; and kids, up high single digits. In Global Football, men's grew low single digits and kids grew high teens. In basketball, women's grew strong double digits and kids grew low teens. And in running, men's was flat, and women's, up low to mid-single digits.

In addition, we took another step forward shifting our product portfolio by reducing the proportion of our business driven by our classic footwear franchises. For Q2, these franchises again decelerated faster than the overall business and at a rate greater than the first quarter. As I said last call, we expect the impact of these shifts to continue for the next few quarters.

With that, let me turn to our operating segments. In North America, Q2 revenue was down 8%. NIKE Direct declined 15%, with NIKE Digital down 22% and NIKE stores down 3%. Wholesale declined 1%. EBIT declined 10% on a reported basis.

Highlights in the quarter included growth in kids with strong momentum in apparel and performance footwear. Men's and women's training drove strong growth. And in basketball, Ja grew double digits, Kobe became the market's largest signature franchise, with demand far exceeding available supply. And Sabrina 2 made a statement as the NBA's second most worn sneaker this season, behind only the Kobe 6.

Throughout Q2, we positioned NIKE as the branded athletes around key sports moments. Our Winning Isn't Comfortable running campaign won Ad Age's Best Ad of 2024, as our ground game-built momentum at the Chicago and New York marathons. As the NFL season got underway, our Kobe release drove our largest cleat shock drop in NIKE history. And when the New York Liberty clinched the WNBA championship and my L.A. Dodgers won the World Series, our brand storytelling owns the moment.

In EMEA, Q2 revenue declined 10%. NIKE Direct declined 20%, with NIKE Digital down 32% and NIKE stores up 3%. Wholesale declined 4% and EBIT declined 10% on a reported basis. We continue to build momentum in sport performance led by strong growth in men's and kids Global Football; men's and women's running return to growth, and all 3 of our top performance franchises in EMEA, Mercurial, Pegasus and Phantom grew double digits. In sportswear, we are seeing momentum from newer franchises, including shocks, Vomero 5, LD-1000 and P-6000.

In addition, we moved first in EMEA to reposition NIKE Digital as a premium platform. This quarter, full price realization improved with a strong double-digit decline in off-price sales. While we are seeing near-term traffic impact as we reduce promotional activity in paid media, we believe these shifts will elevate the total marketplace over time.

In Greater China, Q2 revenue declined 11%. NIKE Direct declined 7%, with NIKE Digital down 4% and NIKE stores down 8%. Wholesale was down 15%. EBIT declined 27% on a reported basis.

In Q2, we experienced another quarter of retail traffic declines in a difficult macro environment. This quarter also required higher markdown activity to drive sell-through and inventory velocity, which negatively affected gross margins. In a competitive environment, NIKE's focus is on serving consumers with product innovation and brand inspiration and fueling the growth of sport in China. This quarter, Ja 2 launched with strong sell-through. Pegasus 41 top sales in women's running and new ACG apparel releases created social buzz. We also continue to see strong full price demand with lower markdowns and higher margins for our locally designed Express Lane products.

This fall, more than 250,000 runners joined us for the Shanghai marathon. In addition, we hosted marathoner, Eliud Kipchoge, for community events, school visits and a run along the Great Wall to inspire the next generation of runners in China. While near- term conditions are challenging, sport continues to grow in China, and we are addressing our current headwinds to reignite brand momentum and a healthy pull marketplace. In APLA, Q2 revenue was down 2%. NIKE Direct declined 4%, with NIKE Digital down 8% and NIKE stores up 2%. Wholesale declined 1%. EBIT declined 12% on a reported basis.

Earlier on, we read consumer trends in Korea and Japan and moved quickly to diversify our sportswear footwear portfolio. Our mix of classic footwear franchises in APLA is below our global business, and new styles are resonating with consumers. Our look of running franchises are up triple digits, and new releases like City and Air Max Muse drove positive consumer response. In addition, we drove strong growth in men's and women's training and kids Global Football as men's and women's running return to growth in the geography.

Now let me turn to our financial outlook. As I said last quarter, we intend to continue providing quarterly guidance during this period of transition. Let me start first by providing some additional color and context. Elliott has now outlined certain strategic actions to reposition our business and reenergize NIKE brand momentum through sport. Some of these actions have been in motion, and we are accelerating the pace. Others are new. More specifically, we are shifting NIKE Digital to a full-price model and reducing the percentage of our business driven by promotional activity. We are also reducing investment in performance marketing, which will reduce paid traffic. This will require short-term liquidation of excess inventory through less profitable channels.

We are creating capacity in the marketplace to sell in seasonal newness and innovation for fall and holiday '25. This requires additional investment in marketplace returns, higher wholesale discounts to liquidate excess inventory and to win back shelf space as well as higher promotions to accelerate volume through our NIKE factory stores.

We are targeting a significant reduction in weeks of supply of our classic footwear franchises over the next few seasons, with time lines varying by franchise, channel, market and geography. As a result, summer order books will be down versus the prior year.

We are increasing brand marketing activity to support key product launches and upcoming sports moments. Investment in sports marketing is also increasing with our recent long-term partnership extensions. And we are investing to rebuild our key city offense, our sport by consumer field of play and our commercial teams to serve our retail partners.

We believe the strategic actions that Elliott has outlined are the right moves for NIKE to create better balance in our business and to reignite growth with our wholesale partners in an integrated marketplace. But over the near term, the net effect of these actions will result in lower revenue, additional gross margin pressure and higher demand creation expenses, with a greater headwind to the fourth quarter compared to the third quarter.

Turning to our third quarter outlook. We expect Q3 revenues to be down low double digits. This reflects initial steps on the actions outlined above as well as worsening foreign exchange headwinds, partially offset by a timing benefit from Cyber Week shifting into our third quarter. We expect Q3 gross margins to be down approximately 300 to 350 basis points, including restructuring charges during the same period in the prior year. This reflects the actions described earlier to clean and to reset the marketplace.

We expect Q3 SG&A dollars to be slightly down year-over-year, including restructuring charges in the prior year. We will continue to tightly manage expenses while we strategically increase investment, as mentioned earlier. We expect other income and expense, including net interest income, to be $30 million to $40 million for Q3.

With that, let me turn it back over to Elliott.

[ELLIOTT HILL]

Thanks, Matt. Before taking questions, I wanted to share some additional thoughts. Matt and I have made it clear that we're repositioning the business to get back to driving a pull market for NIKE. Over the coming quarters, we'll provide more details of our plans, and I commit to being transparent on our progress. We'll also share more specifics about the marketplace moves, stories and products that give us optimism.

But I want you to know my bigger purpose for being here. I rejoined NIKE to take our consumers, our amazing athletes and this great company to someplace new. I want to be a part of a team that celebrates the biggest sports moments in unexpected ways, supports record-breaking athletes, creates innovation that people couldn't even imagine, builds new markets for sport from the ground up, and most of all, a team that changes people's lives, a team that helps athletes at all levels all around the world to reach their full potential. It's an ambitious vision, but one that I truly believe only NIKE can deliver.

Thank you, and let's open it up for questions.

[OPERATOR]

The first question comes from Bob Drbul, Guggenheim.

[BOB DRUBUL]

Elliott, welcome back. Congratulations and best of luck.

[ELLIOTT HILL]

Thank you, Bob. I appreciate it. It's good to be back.

[BOB DRUBUL]

I guess, I appreciate all the commentary. The one question I'd love for you to elaborate a bit more on is the relationships and the reception by your retail partners, especially around earning back the shelf space that you've given up as a company over the last few years.

[ELLIOTT HILL]

Yes. Thank you, Bob. Here's what I'd say. We are absolutely committed to getting back to leading and growing a consumer-led marketplace. And I think there are a couple of keywords there, obviously, key being consumer-led. The bottom line is there are consumers that want to shop NIKE Direct, there are consumers that want to shop wholesale, and there are consumers that want to shop digital and physical, and we have to show up with the best representation of the NIKE brand wherever that is. And we will do exactly that.

In terms of our key wholesale partners, I've got a long history there, as you know, Bob, and I have deep relationships with all of them. I listed a number of them. And so we have work to do. And I would say, especially in the specialty channels, Bob, running and football specialty, we're committed to investing in there. We've already started to invest in those areas. We've started to engage with our wholesale partners, bringing them out here for what we call key account planning meetings or bringing them out to have product engagement meetings for fall '25, and the response has been very positive.

If I had to sort of frame, it up for you, they want us to get back to being NIKE, and they want us to have the unrelenting flow of innovative products that we bring across all sports and against all price points and they want us to get back to being to delivering bold brand statements that help drive traffic. Because when it's all said and done, they want and need from us is to drive mutually profitable growth for them and for us, and that's exactly what we're going to get back to. And we will the only way we're going to get back open to buying shelf space is to do the things that we've already laid out, pave up the marketplace, bring innovative coveted product every single quarter, bring the brand heat that drives traffic and drive sell-through. They're open, they're receptive, and we're excited and looking forward to getting back in business with them.

[BOB DRUBUL]

Great. And I guess one of the other meetings, I think you said you had was with the NCAA. Just curious if you think this is the year for the Ducks, are they going to win the college football playoff?

[ELLIOTT HILL]

Bob, that's a trick question. My guess is I might have the founder on this call, I don't know. But I think where I sit today in the role I sit; I better say I better go with the NIKE team. And by the way, with the number of NIKE teams we have in the playoffs, I like my chances. I'd like a few more of those calls or questions.

[OPERATOR]

We'll take the next question from Michael Binetti, Evercore.

[MICHAEL BINETTI]

Elliott, welcome back, it's great to hear your voice. Elliott, did you think you gave us some commentary around how you're planning the near-term investments in the business. And Matt, you made some allusions to some of those investments continuing into the fall. As you look at your first 60 days and think about the path to getting this brand back to growth longer term that it deserves, what do you think are some of the most important things about how you phase the cost in bringing investments back into the business along the way and the pace of those investments along the way as you look to, I guess, returning to growth as we look past fiscal '25.

[ELLIOTT HILL]

Thank you, Michael. We touched on, in our prepared remarks, what we saw out in the market as we travelled around. And first and foremost, we've got to get back to putting sport at the center of everything that we do. Our product management, we're starting to clean up what we have out in the marketplace. We're starting to shift dollars from performance marketing to brand marketing. We will invest our fields of play because that's where we drive our product innovation, our newness, our distinction, and we will also invest in the brand. And then finally, which is demand creation, both from sports marketing and then just big, bold brand marketing efforts.

And then we touched on what we call our ground game in key countries, in key cities. We'll speak later today with our teammates. But I think the easiest way to think about it, we can't do all of them everywhere. So, we're going to focus in on 5 sports to start with, running, basketball, training, football and sportswear. And while we have 10 key countries and 12 key cities, we're going to focus our efforts on 3 key countries and 5 key cities. So, we're really going to narrow down, and we'll pace and phase as we go throughout the next 18, 24 months or so. So, I'm excited about the actions we're taking and the clarity we have about where we need to invest.

[MATT FRIEND]

And Michael, what I would add to that is you've seen us for a couple of quarters now tightly managing expenses as we have been prioritizing our investments in the brand and demand creation. The long-term sport partnerships, these assets like the NFL, the NBA, the WNBA, Brazil. These are long-term partnerships deep into the next decade. And I think that's a great example for you of our commitment to sport and to invest behind sport, not only now but for the long term. And so over the next couple of quarters, you will see our demand creation investment continue to go up. That's going to be a combination of sports marketing and our investment behind the brand. This quarter, our SG&A was down 3%, but our demand creation was up 1%, and we expect demand creation to continue to lead our SG&A growth over the next few quarters.

The other thing I would just add is when I think of investment, I'm thinking up and down the P&L, and we are making meaningful investments beginning in the third quarter to clean up the marketplace. That means liquidating inventory. That means our sales return reserves in order to be able to clear aged inventory, so we can create space to sell in our new assortments and the innovation that we're excited about in fall and holiday '25. And it also means planning for markdowns in our factory stores. And so that's reflected in the guidance that we provided for Q3. And we do expect that to continue for the near term until we can get ourselves back to a balanced and repositioned business to drive growth looking forward.

[OPERATOR]

From Bank of America, Lorraine Hutchinson has the next question.

[LORRAINE HUTCHINSON]

You're accelerating a lot of the work around lifestyle in fiscal '25. But how much incremental pressure do you expect on 2026 sales? And based on your analysis of the pipeline, when will newness gain sufficient scale to offset that pressure?

[ELLIOTT HILL]

Thanks, Lorraine. Again, as we look at where we are today, we touched on it for a number of times already and the concentration that we have in a few key franchise styles and one of the core competencies that we have in NIKE's franchise management, and it's foundational to this company and what we will as we already talked about, we're taking actions to reduce the amount of inventory in the marketplace, which then it opens up shelf space, open-to-buy for a new innovative product. And I am excited about the product that is coming.

We are we have 3 brands that we can drive from NIKE, Jordan and Converse. From performance to sportswear with over 10 different sports, men's, women's kids, footwear, apparel, equipment, accessories and up and down price points. And I've seen now the product that's coming from our fields of play. I was able to sit through a fall '25 a few of the presentations with our key retailers, and they're excited about the product that's coming, and it will be led with running, training and sportswear. And again, I think the small cross-functional teams are doing a really nice job of now starting to flow innovative product into the marketplace. And that's the quickest way to return to health.

[MATT FRIEND]

Lorraine, we took another step forward this quarter and those 3 franchises decelerated at a rate that was faster than the overall business for the second straight quarter, and the rate this quarter was greater than we drove in the first quarter. And so, as I mentioned last quarter, that has had a disproportionate effect on the NIKE Digital business results because of the concentration of those franchises on digital.

And so, what we had highlighted was that these actions would result in a mid-single-digit headwind on our financials for the balance of this year. And with Elliott being 60 days in and looking at the current plans and where he wants to take our product portfolio, we have accelerated those actions. And so, I expect the impact to be bigger for the balance of this year. And getting very sharp and specific on reducing the weeks of supply over the next few seasons to ensure that across the entire marketplace, these franchises are back at a healthy full price level.

I made a comment in my prepared remarks that summer '25 is down slightly versus the prior year, and that reflects this accelerated level of actions that Elliott outlined. I'd note that even with these actions, we almost offset it by the contribution of newness and innovation. And so even that is as a signal for me, gives me confidence that the work we started over a year ago to build the pipeline is taking root with our partners.

[OPERATOR]

Adrienne Yih from Barclays has the next question.

[ADRIENNE YIH]

I apologize if my phone is crackly, sorry about that. I appreciate the notion of margins before sales. And so, when we look at kind of what you're doing, you're accelerating sort of the reset actions. When you get to the fall of next year, do you have the proven innovation at scale to replace what you are liquidating now? And then, Matt, is there a reset inventory provision that's happening right now in the gross margin. And kind of to wrap that all up, it would very much seem that you are going for those margins before sales. So, when we think about FY '26, I think it would be rightfully the right thought to think that sales would be down again if you're going for margins, as you say, healthy bedrock margins before you drive the top-line growth.

[ELLIOTT HILL]

Hey, Matt, how about if I take the first part of it. I'll hit product and okay, so we outlined the idea of fields of play and taken each of our sports and further segmenting them by men's, women's, kids and putting tight small teams against each one of those segments of business. That, fortunately, has already started. That started over 12 months ago. And because of that, we're starting to see those teams deliver the innovation. They're taking the insights from the consumers that they serve in each of those fields of play. And we're starting to see the product come through the marketplace and started in spring and summer.

As it relates to fall, as you referenced, great confidence around running, especially on the footwear side of our business, Structure, Peg, Vomero, 3 different price points, a lineup that includes a really strong trail lineup, and we have a leading business in racing, both flats and spikes. Our training, of course, is led with Metcon and continues to be a strength of ours in training, along with our apparel that's coming along with that. We have some new concepts around comfort, style and performance.

Basketball is another one that excites me, and it's maybe the best example of this fields of play working. Let me start with men's and our portfolio. You have Jordan with Tatum and Luka coming, and then the NIKE brand, of course, the LeBron, Kobe, Ja, Booker and a new GT series. So, I'm really excited about the basketball lineup. What is really fun for me to see coming back new to see us running this gender offense, we've launched women's basketball program, which I didn't think we'd ever do. Sabrina, Matt already touched on it, #2 shoe in the NBA. And then we have Asia and Caitlin coming back from behind -- and behind that. Sportswear, a new lineup around look at court, look at basketball, look at football, including the Field General. So, net-net is the product's coming, and we're gaining confidence with each season.

[MATT FRIEND]

Yes. And from a financial implication perspective, Adrienne, I guess, a couple of thoughts. First, as I said, a number of these actions we had underway, and Elliott has provided a perspective that we accelerate them. And some of these actions are new actions, like moving more aggressively to reposition NIKE Direct and NIKE Digital, in particular, as a premium channel. And so with him being 60 days in, we are continuing to take time to understand the impact of those actions. But we remain committed to being transparent and provide guidance on a 90-day basis.

As it relates to kind of what's in the third quarter outlook and how quickly are we moving, with revenues being down low double digits and our margins being down 300 to 350 basis points, we are certainly accelerating some of these actions. But some of these actions are going to take time to carry all the way through. And so, our focus is on getting back to a healthy marketplace and getting back to a full-price business, both in our partners and importantly, in NIKE Direct, because we believe that will elevate the entire marketplace and create a foundation for growth.

We're very focused on our inventory because we know that a healthy inventory is absolutely critical for us in order to be able to present the right assortment for consumers and to give our new innovation and our new seasonal product the best presentation across the entire marketplace. And so that's what's been reflected in our third quarter financials.

And I'll just reiterate a point I made in my prepared remarks, which is I said that we expect a greater headwind in the fourth quarter as compared to the third. And that's because the timing of implementing these actions are different across different geographies and different time lines. You heard me talk about the product portfolio rebalancing, being ahead of ahead in APLA for our repositioning the digital business, being ahead in Europe. And so, as we look ahead, from what we can see to-date through the fourth quarter, we expect the headwinds to be larger in the fourth quarter than the third quarter guide that we've provided.

[OPERATOR]

The next question is from Jay Sole from UBS.

[JAY SOLE]

Terrific. Elliott, you mentioned in your prepared remarks that you're willing to take some actions in the near term that will hurt in order to do what's best for the brand and the company over the long term. The history of NIKE is that the companies always try to balance short-term earnings with sort of long-term investment. The question is how far are you going to take the actions in the short term to really put the business on that sustainable path you're talking about to drive in other words, how long are you willing to sort of take the actions in terms of resetting the marketplace, making investments in key cities, rebuilding brand marketing? Is there a limit? And is there a sort of a balance here you're thinking to strike? Or you want to go 100%, just do the right thing, whatever it costs to put the company back on the path to winning? Sorry, that's a long question, but hopefully that make sense.

[ELLIOTT HILL]

That's right. No worries. So, here's I'd love for all of you to think about it. I want you to know we're acting with a sense of urgency. And you've heard Matt talk about the different moves that we're making around inventory, et cetera. And I think the biggest takeaway, hopefully, is that we're putting sport back at the center of everything that we're doing. Our products at offense, we are going to lead with sport. And we'll do that through our sport field to play. We've got the cross-functional teams. And you can see now already the investments that we've made there, and we'll continue to make there are starting to pay dividends as we roll it through spring and summer of '25, end of fall and holiday '25.

From a marketing perspective, we will continue to invest in big, bold brand ideas. We touched on some of the activities that have already taken place and some of the excuse me, marketing campaigns, the Winning Isn't Comfortable ad won an award at Ad Age for 2024, Ad of the Year.

So, feeling good about where we're heading. We've made investments in sports marketing, and we've continued to do that. And then, of course, through the marketplace. And investing in the marketplace is doing the things that we've already talked about, pulling inventory out, return to vendor, but it's also investing in new products, marketing, in-store presentation, both at a strategic account level that covers an entire country and then down to the city level, which includes specialty accounts, which we are making some investments in. Running specialty started in North America.

So, I think it's going to take time, but I am confident that we are making the right moves and the right shifts to drive this brand, this business forward.

[MATT FRIEND]

Jay, the way, I think, about the implications on our financials in the near term, I break these actions down between 2 buckets. I would say there are near-term headwinds that we will endure as a result of the repositioning of our channel mix and our product portfolio. And those will create headwinds and are creating headwinds right now. But we expect that as we recalibrate the portfolio of both our channels, meaning NIKE Direct and wholesale or our product, that those headwinds will end.

And then we have transitory headwinds, which are the actions that we're taking to clean up the marketplace in inventory as well as some of the supply chain deleverage that we're experiencing as our sales decline, which we would expect to recapture as our business returns to growth. And so, I think that hopefully, that's a helpful way to think about what we're looking at here. And we're definitely focused on both of those dimensions and confident that these actions will reposition NIKE and also provide opportunity for us once we've completed what we've set forward to do.

[OPERATOR]

Next up is Matthew Boss, JPMorgan.

[MATT BOSS]

Great. Elliott, so maybe could you help rank the fields of play opportunities you see by category? And then just on the long-term view, what's a reasonable timeline to realign inventory to pull market? And then after, for the product pipeline and the marketing investments to return to sustainable profitable growth?

[ELLIOTT HILL]

Yes. So let me hit the fields of play, and we have a number of fields of play, and we have a sharp focus on 5. And we see those as our biggest opportunities from running to basketball to football, that's Global Football or soccer, training and sportswear. And we will break each one of those fields of play down by men's, women's and kids. And what we're most excited about is, not only the product innovation that's coming out of there, but the merchandising opportunities that we have.

So, for example, there are moments when we need to show up as a running brand, footwear, apparel, accessories, men's, women's, kids, and there are moments when we need to show up as a women's brand. And this offense allows us to do both of those and will unlock incremental growth for both our brand and our business moving forward. So, in terms of the fields of play, those are our sharp focus in the near term. And we are learning and growing this offense and would be able to apply it to more sports in the future, and we're excited about it.

[OPERATOR]

The next question is Jon Komp, Baird.

[JON KOMP]

I want to follow up on the ultimate sort of margin recapture potential, if you will. I'm just curious, Elliott, as you look at some of the moves in the past few years that the brand is focused on, where the products are being sold, more in the digital channel, specifically. And today, if you look at the organizational structure throughout supply chain and distribution, are there sort of unique opportunities to become more efficient? Or is it purely going to be getting back to growth to scale some of the investments from the past few years?

[ELLIOTT HILL]

Here's what I'd say. No question, growth, certainly, will help. And I believe the moves and the confidence, that the moves that we're making will help set us up to for long-term sustainable and profitable growth, the product, the marketing, the clean marketplace. One of the moves that I did make is that one of the first leadership moves I made, I had Venky, who's now our Chief Supply Chain Officer reporting directly to me, he looks everything from factory, transportation, all the way through to logistics to the consumer. And it certainly will be I've only been here 60 days, but it'll certainly be a focus as we move forward as an opportunity for margin expansion.

[MATT FRIEND]

And Jon, if you look over history, we've consistently been a double-digit margin company. And when I think of the actions that we're taking in the marketplace today, there are a number of opportunities as we look forward. Specifically, we talked several years ago about the profitability of selling a product through the digital channel. But that math is relying upon it being a full-price sale. And to take the point that Elliott made around the business being 50% full price and 50% off price today, the profitability of the channel has significantly been challenged over the past several quarters.

And so, in addition to cleaning up the inventory, there's certainly a margin rate benefit opportunity within NIKE Direct to run, albeit a smaller but a healthier and more profitable business. And that includes opportunities our teams are working on to continue to drive the cost of fulfillment down as well as being less reliant upon paid media and performance marketing in order to be able to drive the top line. But leveraging the investments that we're making in our brand to drive organic top of funnel traffic to us and to our partners.

[OPERATOR]

Next up is Brooke Roach from Goldman Sachs.

[BROOKE ROACH]

Elliott, I was hoping you could speak to any specific actions that you'll be taking either in the North America or Greater China geographies as you look to accelerate some of these actions over the course of the next 12 months.

[ELLIOTT HILL]

Yes. So, I'll take North America first. We have a new leader, Tom Petty, leading North America. Has a deep, long history with NIKE and a lot of experience. He's led North

America before, and I can tell you that he and his team are being aggressive in all of the actions that we've outlined in terms of cleaning up the marketplace, building back the relationships with our wholesale partners, investing in the brand, elevating NIKE Direct and they'll start moving there in spring, so in January.

And so resetting NIKE Direct, leveraging the relationships, investing in RSG, which is running specialty. We've invested in Beacons' on-the-ground game, invested in the brand. We touched on a bunch of that Liberty, Dodgers wins. And so, the shift is going to take time, but I'm really confident in Tom and his team's ability to execute across product brand marketplace and to get North America back to growth.

In terms of China, hey, we are all we continue to be excited about China long term. There's 1.3 billion consumers and our biggest opportunity is to invite those consumers into the world of sport and the lifestyle of sport and to grow the overall marketplace. And when we do that, I like our chances of growing. We were just in China, and there's no question. It's also a promotional marketplace. The competitors have both international and local increased. And it's a place that I've spent a tremendous amount of time. I've been in China market since 2002 and had some deep experiences in China in 2006, '08, getting ready for the '08/'08 Olympics and led a reset plan in China, and a growth plan there. But in the end, I have confidence in the teammates to help get this business back to growth.

It will start as it always does, with product innovation, and we are investing with China in product innovation, not only the product from the globe, but we have a local what we call Geo Express Lane. It's a local product creation team on the ground, creating product for China. We also have a sports research lab. We call it the NSRL, NIKE Sports Research Lab, that is doing, of China, research, in terms of gait, foot form, et cetera. So, we're making product of China for China and then big brand bold statements, Matt touched on some of them, Shanghai Marathon, et cetera.

And then, I think, our biggest, biggest after-product becomes the marketplace. We have got to reset bigger bolder consumer-led NIKE concepts that represent the full expression of the NIKE brand, have the service and the experience that we expect that'll drive the performance and the productivity of those doors. And the good news is, just I was over there and I met with Topsports and with Pou Sheng, our 2 biggest partners, and they're ready to go.

So long-winded answer, but I think it all comes back to what we were talking to in both of these geographies. It comes down to product management. It comes down to brand management and it comes back to marketplace management.

[OPERATOR]

Now we'll hear from Ike Boruchow, Wells Fargo.

[IKE BORUCHOW]

Elliott, great to hear from you. Actually 2 questions, I think, for Matt. Just a follow-up on the guide. When you talked about the expense guide for the third quarter, I just want to make sure I understand. Is that relative to the $4.2 billion in expenses of last year so in other words, the restructuring charges some of those took out. So just trying to understand the growth of slightly is or down slightly is relative to what dollar number?

And then just a follow-up to that is when you talked about greater headwinds relative to 3Q. I think that was in the sentence of talking about revenue, gross margin and demand gen spend. Was the comment meant to absolutely all 3 of those line items? Or was it really meant for revenue or gross margin or something more specific?

[MATT FRIEND]

Yes. Ike, on your first question, the SG&A guide is related to the full amount, including the restructuring charge in the prior year. As it relates to your second question, the answer is yes. As I mentioned, these actions are happening on different time lines across different regions. And based on what we can see today, we think the net impact of these actions across revenue, margin and demand creation will be larger in the fourth quarter than they are in the third quarter. So, the year-over-year impact is -- another way to take it is the year-over-year impact, when you compare to the prior year, will be more significant in the fourth quarter.

[OPERATOR]

And everyone, that does conclude the question-and-answer session as well as today's conference. We would like to thank you all for your participation today. You may now disconnect.

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