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Market Intelligence

Nautilus, Inc. NYSE:NLS

FQ2 2023 Earnings Call Transcripts

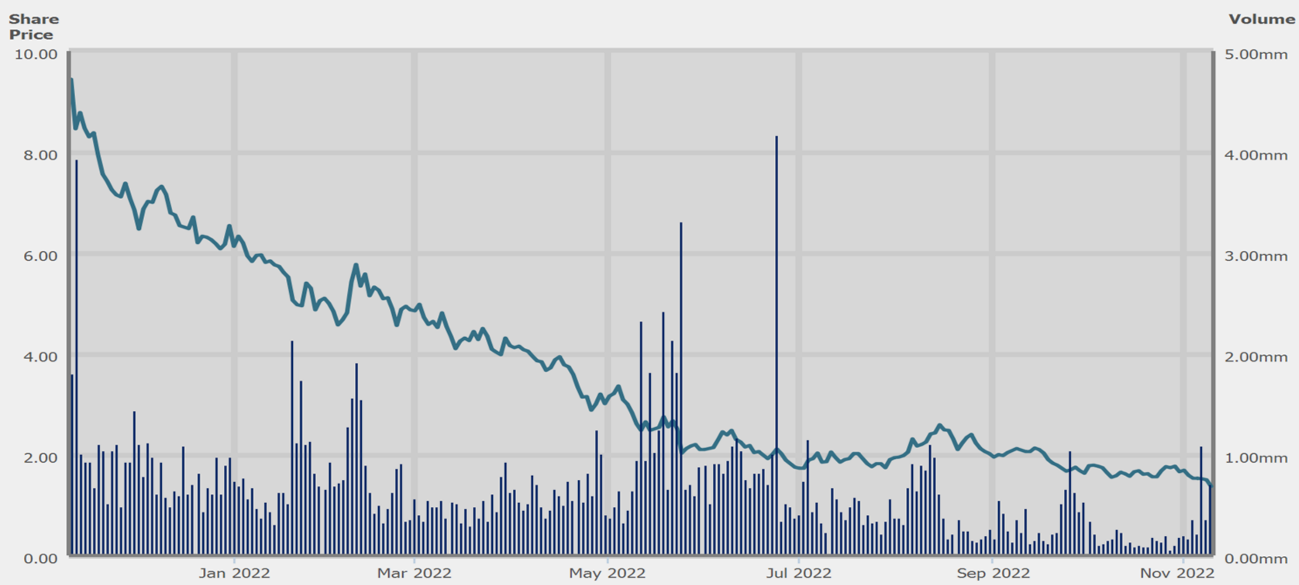
Wednesday, November 09, 2022 9:30 PM GMT

S&P Global Market Intelligence Estimates

	-FQ2 2023-			-FQ3 2023-	-FY 2023-	-FY 2024-
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	CONSENSUS
EPS Normalized	(0.52)	(0.40)	NM	(0.11)	(2.37)	(0.63)
Revenue (mm)	69.38	65.46	▼ (5.65 %)	142.81	395.82	430.11

Currency: USD
Consensus as of Nov-01-2022 9:51 PM GMT

Stock Price [USD] vs. Volume [mm] with earnings surprise annotations



- EPS NORMALIZED -

	CONSENSUS	ACTUAL	SURPRISE
FQ3 2022	(0.49)	(0.42)	NM
FQ4 2022	(0.58)	(0.56)	NM
FQ1 2023	(0.71)	(1.06)	NM
FQ2 2023	(0.52)	(0.40)	NM

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Call Participants

EXECUTIVES

Aina E. Konold
Chief Financial Officer

James Barr
CEO & Director

ANALYSTS

John-Paul Wollam
ROTH Capital Partners, LLC, Research Division

Mark Eric Smith
Lake Street Capital Markets, LLC, Research Division

Michael Arlington Swartz
Truist Securities, Inc., Research Division

ATTENDEES

John Mills
ICR, LLC

Presentation

Operator

Good day and welcome to the Nautilus Inc. Second Quarter 2023 Earnings Results Conference Call. [Operator Instructions] After today's presentation, there will be an opportunity to ask questions. [Operator Instructions] Please note, today's event is being recorded.

I would now like to turn the conference over to John Mills with ICR, please go ahead sir.

John Mills
ICR, LLC

Thank you. Good afternoon, everyone. Welcome to Nautilus' fiscal 2023 second quarter ended September 30th conference call. Participants on the call today from Nautilus are Jim Barr, Chief Executive Officer; and Aina Konold, Chief Financial Officer. Please note this call is being webcast and will be available for replay for the next 14 days. We will be happy to take your questions at the conclusion of our prepared remarks. Our earnings press release was issued today at approximately 1:05 PM pacific Time and may be downloaded from our website at nautilusinc.com on the Investors page.

The earnings release includes a reconciliation of the non-GAAP financial measures mentioned in today's call to the most directly comparable GAAP measures. Please note, we'll be comparing results versus last year fiscal 2022 and versus fiscal 2020, as we believe comparing to the last pre-pandemic period, it's helpful in demonstrating our growth and progress. For today's call, we have a presentation that management will refer to during their prepared remarks. On slide 2 is our full Safe-Harbor statement, which we ask everyone to read. You can access the presentation now by going to the Investors page on our website and clicking on Events and Webcast.

I'd like to remind everyone that during this conference call, Nautilus management will make certain forward-looking statements. These forward-looking statements are based on the beliefs of management and information currently available to us as of today. Such forward-looking statements are not guarantees of future performance and therefore one should not place undue reliance on them. Our actual results may be affected by known and unknown risk, trends, uncertainties and factors that are beyond our control and ability to predict. For additional information concerning these factors, please refer to the Safe-Harbor statement and to our SEC filings which can be found in the Investor Relations section of our website.

And with that, it is my pleasure to turn the call over to Nautilus' CEO, Mr. Jim Barr.

James Barr
CEO & Director

Thank you, John and thank you all for joining us. I'd like you to takeaway 3 things from today's call. One, the profound and enduring shift in consumer fitness habits post pandemic toward at-home workouts continues to enhance the long-term opportunity for our country -- company. Two, Nautilus operating model is a strategic advantage to weather short-term top line challenges, our asset-light manufacturing diversified product portfolio, omnichannel distribution and variable cost structure that enables tight management of margin, operating expenses and inventory levels is a model built to flex with a variation of market conditions.

Third, we continue to enhance and scale our differentiated digital offering JRNY to better serve our customers and capture long-term revenue and profit. As proof points for this, this quarter, despite the challenged top line, we grew JRNY members and managed down our inventory on plan, significantly improved our gross margins and reduced our operating expenses, delivering a significant beat to analysts' adjusted EBITDA consensus. This resulted in cutting our quarterly loss in half sequentially, trending towards our goal to breakeven in the back half of the year.

At-home fitness like many other consumer focused industries is undergoing short-term macroeconomic challenges, but the long-term profitable growth opportunity for our company remains intact. Our research shows that consumers and particularly our recently defined high-value target segments are sticking with home workouts, even as they tighten their belts and watch their budgets.

Consumers long-term habits have shifted and solidified in the past 2-plus years in favor of home fitness. Over 60% of US adults recently surveyed say they consistently worked out at-home, up from 43% who reported the same at the beginning of 2020. In our target segments, this trend is even more profound with nearly 90% working out at-home. This is a long-term seismic shift and Nautilus is well positioned to take advantage of this opportunity.

To whether the macro and retail challenges, we are staying grounded in our noble mission and unwavering in our dedication to build a healthier world one person at a time. We also remain steadfast in our strategy to provide consumers a broad variety of superior products at a wide range of price points via our omnichannel distribution models. And we continue to enhance the portfolio with our differentiated JRNY connected fitness offering. These advantages of a broad assortment of products and omnichannel distribution allowed us to offset areas of weakness in the quarter.

Moving now to the second quarter financial results. Even in this tough environment, we saw solid end consumer demand for our products and for our JRNY digital offering. We delivered net sales of $65 million in the second quarter, with the Direct channel up 51% compared to 2020 and the retail channel up 11% compared to 2020. While we saw a moderate level of retail sell-through, the widely publicized over inventoried and conservative position of retailers across many categories and their continued focus on lowering these inventories resulted in new sales for the quarter.

We added 40,000 members in a seasonally soft quarter and passed the key threshold of 400,000 JRNY members, an increase of over 116% compared to the same period last year. Growth in our Direct channel was driven by our strength portfolio as cardio particularly IC bikes lagged, reinforcing of our strategic advantages, having a broad portfolio offering both high-quality strength and cardio modalities as one channel or modality is soft, we can push the other.

Further, 51% growth in our Direct channel versus the same period in 2020 supports our belief that post pandemic exercise habits favoring home fitness are here to stay. Retail channel growth was up 11% compared to the same pre pandemic order in fiscal 2020 excluding Octane, yet retailers remained cautious about inventory levels across many categories including home fitness.

We are tracking and assisting in the destocking of existing retail inventories as they sell-through and while we are seeing reorders from some retailers, others still have additional stock to sell before being comfortable in placing significant reorders. Given these conditions, when we saw softened reorders in retail, we pivoted with a focus on our Direct channel for this past quarter. Driven by key actions we took earlier this year to lower supply chain costs, we improved gross margins by 480 basis points sequentially from the first quarter and we expect continued improvement in the back half of the year and into fiscal 2024.

While top line grew about 19% sequentially, we reduced our adjusted operating expenses by 19%, showcasing our operating leverage and variable cost structure. As a result, adjusted EBITDA loss for the quarter totaled $10 million, cutting the loss from the first quarter in half, delivering a significant beat to analysts' consensus. We are demonstrating real improvement in adjusted EBITDA performance and expect continued improvement during the back half of the year.

Lastly, we remain comfortable with our liquidity position given flexible nature of our cost structure and the fact that we're entering the seasonally stronger second half of the year which we expect will deliver strong improvement in our adjusted EBITDA compared to the first half. Aina will provide more detail later in the call along with diving deeper into quarterly results.

Now I would like to discuss the other elements of our unique operating model. As noted before, our model is designed for agility with significant variability. Some examples of the variable parts of our business are as follows. An asset-light model and with outsourced manufacturing, utilizing contractors for sprints and surges in software development, continuing to rationalize our product portfolio and focusing on fast moving top sellers. SKU rationalization under North Star has resulted in over 80% of the volume in the quarter concentrated on top 25 products.

Our approach to marketing and embracing digital media allows us to be nimble and shift marketing investments as needed. In the quarter, we focused advertising spend on transactional media to drive traffic with the best chance of converting to sales. We also made the decision to shift marketing investment from the second quarter to our peak season in the third quarter and in January when more consumers are expected to shop and purchase in the category.

And last, we continuously regulate non-media operating expenses looking for efficiencies and savings. An additional focus of our business model and an important pillar of North Star is our supply chain becoming a strategic advantage. We have made great progress here and are reaping the benefits with the gross margin sequentially improving by 480 basis points this quarter and we expect even greater improvement in the back half of the fiscal year based on the following.

We closed our Portland DC at the end of October and have successfully transferred inventory to our Columbus and Southern California DCs, both strategically placed to optimize their expedited deliveries. We renegotiated inbound freight rates, as well as contract manufacturing cost for our top products. Once we sell-through these inventories, we will start to see the flow-through of manufacturing in freight savings possibly later this fiscal year.

Let me now move on to providing an update on JRNY. As I said earlier, we are pleased to report that we added 40,000 members in our seasonally soft second quarter and are now at 400,000 total JRNY members, a 116% improvement year-over-year. Let me highlight the important accomplishments that led to this growth.

80% of our units sold are JRNY enabled now. JRNY is now offered across the cardio portfolio including treadmills, bikes and our proprietary Max Trainer, as well as available with Bring Your Own Device for our number one selling SelectTech Dumbbells. We have enhanced several important aspects of the JRNY platform including usage analytics to help better understand what our members use and enjoy among our industry-leading variety of ways to workout.

We've also added an enhanced member communication platform that permits us to more easily convey new features and benefits and coach and encourage members between workouts. We continue to enhance our instructor-led content library and added new Explore the World immersive experience routes to give consumers nearly 400 places to visit while working out. We are doubling down on our differentiated adaptive workouts that are unique to each individual member and expect to offer more features over the coming quarters. We continue working to integrate JRNY with motion tracking with our leading 552 and 1090 Dumbbells and are on track to start a broad beta test in the third quarter.

Finally, we are excited to add per typical early life cycles of subscription products, we are beginning to convert the very first of the 12 month membership trials that bundle with JRNY enabled cardio products. As more trial memberships come up for renewal and this data becomes more meaningful and useful, we will share information on conversion and churn, for now churn is embedded in the member numbers.

These advancements have us well-positioned to grow our base and engagement of JRNY members. We continue to expect to end the fiscal year with more than 1.5 million JRNY members. And in addition to the digital capabilities in JRNY, what do we have coming up for fitness season? Well, new products of course. This week, we introduced the Schwinn 190 upright and the Schwinn 290 recumbent bikes, both bikes are connectable to JRNY and feature terrain control technology, plus modern design elements and functionality suitable for all fitness levels.

We also recently launched a new value priced treadmill the Bowflex BXT8J, which we believe is an important -- which we believe is important this holiday as consumer shop with value in mind. This treadmill pairs with the users' phone or tablet and offers our differentiated adaptive workouts Explore the World routes, JRNY radio and hundreds of trainer led workouts through the JRNY app. It is available for online purchase at select retailers including Amazon, Best Buy, DICK'S Sporting Goods and Nebraska Furniture Mart.

I would like to close with a few other important points. Due to the current economic environment and the conservative position of our retail partners, we are lowering our previous revenue expectations for the back-half of 2023. Even with these lower expectations, we expect strong improvement in our top and bottom line results for the back-half of 2023 due to third and fourth quarter seasonality, increased advertising spend to drive more demand, new products and leveraging the advantages of our operating model. Aina will provide more details on guidance and liquidity in a few moments.

Over the last 2-plus years, we have made tangible lasting changes to our business where we leverage the shift in consumer fitness trends and set our company up for long-term growth. While we have temporarily slowed some elements of our North Star investment as we responsibly balance long-term ambitions with short-term objectives, we remain steadfast on our path to Nautilus digital transformation.

Given the dynamic market environment and a tremendous long-term growth potential in this sector, as previously announced, our Board of Directors launched a comprehensive review of strategic alternatives to identify partner opportunities to accelerate the company's strategic transformation and enhance shareholder value. We have engaged Evercore, a global investment bank advisor to assist in this effort. At this time, we have no additional information to share regarding the process of timeline.

I will now turn it over to Aina who will give us more detail on the second quarter results and the guidance for the full-year.

Aina E. Konold
Chief Financial Officer

Thank you, Jim and good afternoon everyone. Today, I'll be speaking to total company results for Q2 fiscal year '23 and will provide guidance for the full-year. Please go to our website to view our press release and the slides accompanying this presentation for more information on Q2 and year-to-date results and for additional information on our segments. Given the unique nature of last year's results, we'll also be comparing this year's revenue to fiscal year 2020 to gauge our growth and overall company improvements when compared to more normalized pre pandemic results.

Turning to Slide 11, total Company P&L for the quarter for the comparisons primarily to last year. Net sales for the second quarter were $65 million, down 53% versus last year and up 24% versus the same quarter in fiscal year '20, excluding Octane. Our Direct segment grew 51% versus the same quarter in fiscal year '20, while the retail segment grew 11%. Gross profit was $11 million and gross margins were 18% down 13 points from LY but up sequentially, nearly 5 points from last quarter. I'll now go through the drivers of the gross margin decline from last year.

4 points due to increased discounting as we were still benefiting from pandemic tailwinds last year, 4 points due to the deleveraging logistics fixed costs, given the decline in sales, 2 points to the last year's release of a special warranty reserve. 2 points due to inventory adjustments related to continued progress in phasing out Nautilus branded inventory, 3 points related to increased JRNY investments. These declines were partially offset by approximately 2 point of supply chain cost improvements like lower inbound freight and more favorable FX rates with the dollar strengthening against the RMB. If we exclude the impact of the inventory adjustments and last year's release of a special warranty reserve, Q2 gross margins would have been 22%.

Turning now to adjusted operating expenses. The next few lines of the P&L have been adjusted to exclude acquisition and other cost related to the purchase of VAY in last year's legal settlement. Please see our press release for a reconciliation to GAAP. Adjusted operating expenses were $25 million, down 35% versus last year. The primary driver of the decrease was lower advertising, which was $3 million this year versus $12 million last year.

Adjusted operating expenses excluding advertising were $22 million, down 15% versus last year, even with continued investments in JRNY. We controlled variable expenses across all functions to ensure that they remain in line with lower sales. Adjusted operating loss was $14 million and adjusted EBITDA loss was $10 million.

I'd now like to walk through a waterfall chart on Slide 13 that shows how we went from an adjusted EBITDA loss of nearly $20 million in Q1 to only $10 million in Q2. Q2 sales were up $11 million or about 20% versus Q1. We brought down inventory levels per our plan and we expanded our margin sequentially by nearly 5 points, delivering $5 million more in gross profit on $11 million more sales. Much of this is due to the great progress we've made to transform our supply chain into a strategic advantage.

Another North Star priority was shifting more of our advertising spend to digital media, which gives us flexibility to adjust marketing investments as needed. We reduced marketing dollars in Q2, a seasonally low revenue quarter and shifted them to the fitness season. This quarter's ad spend was primarily in transactional media to drive traffic with the best chance of conversion, because we have an asset-light, semi-variable operating model, we have the ability and flexibility to ramp down expenses in line with sales. Q2 OpEx excluding advertising was down $2 million versus Q1. As a result, we delivered nearly $10 million more in EBITDA, cutting our loss in half from nearly $20 million down to $10 million.

Let me now turn to Slide 14 for first half results with comparisons primarily to Last year. Net sales were $120 million, down 63% versus last year and up 17% versus the same period in fiscal year '20, excluding Octane. Gross profit was $18 million and gross margins were 15%, down 15 points versus last year. The key drivers of the gross margin decline were 7 points due to increased discounting, 6 points related to deleveraging logistics fixed cost, 2 points due to the Q2 inventory adjustment, 3 points due to increased JRNY investments. These declines were partially offset by 3 points of supply chain cost improvements.

Turning to adjusted operating expenses on the next slide. As a reminder, please see our press release for a reconciliation to GAAP. Adjusted OpEx was $56 million, down 27% versus last year. Selling and marketing expenses were down 48% or $21 million, driven by lower ad spend, which was $9 million this first half versus $24 million last year. Adjusted operating expenses excluding advertising were $47 million, down 10% versus last year, inclusive of continued investments in JRNY. Adjusted operating loss was $37 million and adjusted EBITDA loss was $29 million.

Turning now to the balance sheet as of September 30th. Cash was $7 million per our plan, quarter ending inventory was $99 million, down 39% versus last year and down 11% versus year-end. At 9/30, about 11% of our inventory was in transit and continues to be concentrated in our best-selling SKUs with over a 1/4 of our inventory cost in SelectTech weights. AR was $34 million and trade payables were $37 million, both down from year-end. Debt was $47 million, we had $22 million available for borrowing, bringing our liquidity at the end of September to $29 million. We remain comfortable with our liquidity as we are entering our seasonally higher volume back half. Higher revenue, combined with our expectations of sequentially higher gross margins and continued cost discipline will result in improved liquidity in the back half.

I'll now turn to guidance for the rest of the year. We are lowering full year revenue guidance to between USD 315 million and USD 365 million, which translates to second half revenue of between USD 195 million and USD 245 million. Given the adjustment to our full year revenue expectations, we are now guiding to full year adjusted EBITDA loss of between minus $30 million to minus $40 million, which implies a second half adjusted EBITDA of breakeven to a loss of $10 million. The presentation contains a waterfall chart on Slide 18 that demonstrates our path to second half breakeven adjusted EBITDA compared to first half adjusted EBITDA loss.

Similar to Q2, the most impactful improvement will come from higher revenue, supported by higher gross margins. We now expect gross margins in the second half to be between 24% and 27%, an improvement of 9 points to 12 points versus first half gross margins. The margin improvement is driven by lower logistics cost as we've closed the Portland DC and gotten out of the storage locations to be rented to house our excess inventories. Better FX as the dollar continues to strengthen versus the RMB and lower product costs as we've sold through older inventory and are getting more benefit from the newer inventory that reflects lower factory and inbound freight costs.

We expect to invest in more advertising versus the first half and expect variable costs to grow in line with sales, partially offset by continued cost discipline in other areas. Our objective is breakeven adjusted EBITDA in the second half and we believe that we have enough levers given our asset-light, semi-variable operating model to adjust for a variety of sales outcomes. Lastly, we continue to expect JRNY members to cross the 0.5 million mark at year end '23.

With that, I'll turn it over to Jim.

James Barr
CEO & Director

Thank you, Aina. It is my hope that one takeaway from our earnings call today is that Nautilus is positioned for top and bottom line improvement for the remainder of this year and over the long-term, despite the challenging macro and retail environment. There is long-term opportunity due to an enduring and profound shift of consumer behavior towards at-home workouts. Our company is well positioned to meet these needs with our strong portfolio of product offerings and expanded on-channel go-to-market model and a differentiated digital platform.

As seen this past quarter, the Nautilus operating model allows us to lean into one channel when the other is pressured and a broad product portfolio provides balance when one category such as cardio or one modality, for example bikes may be lagging. Our operating model is a strategic advantage relative to competitors who have lagged behind in adjusting their businesses in light of macroeconomic challenges and we and are just beginning to adjust theirs in key ways to more closely emulate ours, asset-light manufacturing, a broadening product portfolio, expanding omnichannel distribution and a more variable and agile cost structure.

We are making steady progress on the execution of our strategy and have already begun to see the fruits of our labor. Despite the challenged top line, we grew JRNY members and managed down our inventory on plan, significantly improved our gross margins and reduced our operating expenses. This resulted in cutting our quarterly loss in half sequentially and trending towards our goal to breakeven in the back half of the year.

Under our North Star strategy, we have streamlined our portfolio and divested the noncore parts of our business. We've hired the right leadership with a measured approach to recruiting talent in line with growth, double down on our investment in digital and strengthened our supply chain and we did it all while riding a historic wave of demand and navigating unprecedented operational challenges. Our liquidity, the strength of our brands and our operating model all provide reasons to believe in the success of this company.
To end, I want to thank our employees and partners for focusing on what they can control, balancing long-term opportunity with near-term pressures and for their tenacity, resilience, creative problem solving and tireless support of our mission. And now I'd like to turn it over for questions. Operator?

Question and Answer

Operator

[Operator Instructions] Today's first question comes from Michael Swartz with Truist.

Michael Arlington Swartz
Truist Securities, Inc., Research Division

I understand you took down guidance for the full year. It sounds like most of that is related to the retail business. So I guess with the new number you're guiding to here, I mean, how much comfort do you have? And I guess, how much visibility do you have into that -- into the second half of the year, given everything -- I think everyone is hearing about retail, a reduction of inventory?

James Barr
CEO & Director

Well, first, as I mentioned, I'll start and Aina will tag on. First, we are getting some reorders. It varies retailer-to-retailer. It depends on where their stock position is and really their level of comfort. As I mentioned in my remarks, there's a risk aversion we haven't seen in recent years in retail and that's not just our category that you'll see -- you'll see a lot of that going on. We continue to monitor the retail sell through and the retail levels and they are coming down and they are headed in the right direction. So we think we'll see that.

I think it's important to point out that we continue to see and I mentioned it in my remarks, I call this end consumer demand. In other words, people are still buying our products. So you're seeing that in Direct, the 51% versus the same period pre-pandemic. So that tells us that, that there as well. We know the long-term is there as well. So it's just a matter of working through the inventory and the timing of that and we continue to monitor that. And we don't just sit on the sidelines either, we have ways to help our retailers -- their problems are our problems. So we do help them, try to sell through what they have. We coordinate with our own channel to make sure we're not undercutting each other with prices, bidding on the same keywords, et cetera. So we'll just continue to monitor that situation going forward, but we're optimistic. We know this is a temporary problem, right? This is not permanent problem. We've expanded our doors in retail, they're there for a reason. We're just a little clogged in this -- in the retail channel for the short term. Anything you would add?

Aina E. Konold
Chief Financial Officer

I just would agree that a lot of the downward guidance is driven by retail. We're really pleased with how Direct has been doing and we're pleased with how they did in Q2.

Michael Arlington Swartz
Truist Securities, Inc., Research Division

Okay. Great. That was my next question. Just in terms of the clarification, I mean, did you take down or lower your expectations for Direct? Or is that kind of similar to what you had expected before?

Aina E. Konold
Chief Financial Officer

It's about similar, most of the decline is in retail.

Michael Arlington Swartz
Truist Securities, Inc., Research Division

Okay. Perfect. And then maybe I think last quarter, maybe the last 2 quarters, you kind of pointed to slowing promotion or maybe normalized promotion or something approaching normal maybe over the

-- relative to the COVID period. I guess as we sit here today in early November, how would you classify promotion right now?

James Barr
CEO & Director

Yes, I'll start, I mean it's a fairly promotional environment out there, right? I mean I think everybody is seeing the same thing. I've never seen Black Friday deals start so early. We know consumers have limited discretionary income and we're hitting it early and hard. And we're doing the same thing. That said, we've got lots of things going the other way that we mentioned in terms of margin and advertising spend to support that. What would you add on to that?

Aina E. Konold
Chief Financial Officer

I would add on that, if you compare how we're thinking about this back half versus last year back half, last year back half, we were really over inventoried. So we wanted to use promotional lever to clear that inventory. This year, we want to be competitive, but we don't have an inventory kind of hangover that we need to push through. So we can be more -- we can be more selective in how we choose to be competitive. So I'm really -- I'm happy with our inventory position and I think we can be competitive and still deliver the margin expansion we're looking for in the back half.

Operator

And our next question today comes from Mark Smith at Lake Street Capital Markets.

Mark Eric Smith
Lake Street Capital Markets, LLC, Research Division

You just hit on one of my questions, but that was just retail and total channel inventory, just kind of what you're seeing. And then along with that, just promotional environment, especially as we think about just entering this key selling season?

Aina E. Konold
Chief Financial Officer

So when you ask about inventory, you're thinking about our inventory or the retailer inventory?

Mark Eric Smith
Lake Street Capital Markets, LLC, Research Division

I would love to hear kind of both and maybe the retail inventory of your product, total kind of retail inventory of all competitors as well and then your inventory.

Aina E. Konold
Chief Financial Officer

Yes, so I'll start with our inventory, the one that's showing up on our balance sheet. I'm really proud of how well the team has managed. I mean we were not pleased with how high it got last year and it's been a pretty strong cross-functional effort to make sure that we glided it down and still meet our objectives on top line and margin expansion. So really, really pleased with that. And as Jim said, we're watching -- we have a way of monitoring our inventory at the retailers and it's moving in the right direction as well.

The thing that's tricky and you asked that question and you're right, how are they doing with all their other things they're stocking, not just in fitness, but also in other categories. So what we're seeing is, even if they're selling through our product and maybe they're getting close to lower or more appropriate levels, they may still choose to be more cautious and just wait till the rest of their inventory appropriately glides down before they reorder more like normal patterns. So we have a backlog in retail. We had a backlog last quarter. They're reordering things that have stocked out, but I think it will take a while for them to probably digest all the inventory they have across all other categories outside of fitness.

Mark Eric Smith
Lake Street Capital Markets, LLC, Research Division

Okay. And then the other question for me is, we like the cuts to the operating expenses and it sounds like some of that was very strategic just in this quarter. But can you just speak broadly to the sustainability of these cuts? And then how you balance not cutting too deeply?

Aina E. Konold
Chief Financial Officer

That's a great question and one that we think about all the time and kind of Jim referred to it in his remarks about, it's a balancing act, right? We need to make sure that we can meet our near-term objectives without cutting off our future. So what I want to just remind everybody is when we were growing and the pandemic was at its height and sales were doubling quickly, we chose intentionally not to hire as many full-time equivalents that were our employees. We expanded our capabilities really reaching out to outside contractors, outside resources, so that when the demand went down, as we predicted, we knew there'd be a dip after the high then we could more easily shed some of these excess costs. And then as we're -- as that kind of brings in closer and we need to start looking maybe more closely to some things that are more fixed rather than variable, we're going to make sure that we really balance and make sure that we don't cut off our opportunity to take advantage of the recovery when it comes.

I don't know, Jim, if you'd want to add anything to that?

James Barr
CEO & Director

No, I think this is a rough number, I'm not sure if we said it before, but as we doubled sales, we only increased our headcount 20% and that was intentional. And some people thought we should go faster, but we just thought it was a measured way to do that. And so that's what we've done and we think we're in a pretty good position. We've done things like others have done in freezing hiring, for example, that's the first thing. And we did that early in the summer. We've continued that. So anytime someone wants to hire someone including a backfill, it requires my personal approval and that has slowed things down.

And like Aina said, look, both of us came here to really grow this company and make it into something fantastic and it's tough to pull back on some of these things when we want to go faster. So that is what she said, it's a balancing act. And we try -- when we do make cuts and we do hold the line in certain cost areas, it's really kind of with the principle of when this turns back around, we are managing a dip, that's what we're doing, no one thinks this is permanent. The reasons for it are not permanent, we're managing this dip. And on the other side of the dip, we want to be able to capture the full velocity of growth coming out of the dip. We know that's the position we're in and we try to balance those things responsibly every day.

Mark Eric Smith
Lake Street Capital Markets, LLC, Research Division

Perfect. Maybe I'll sneak in one last accounting one. I think you do closed the Portland DC during this next quarter, is that right? Is that October?

Aina E. Konold
Chief Financial Officer

Yes, we closed it in October at least expiration.

Mark Eric Smith
Lake Street Capital Markets, LLC, Research Division

Okay. So there's no lease expense or any onetime things that we should look for in this next quarter?

Aina E. Konold
Chief Financial Officer

No, because we just closed it at lease expiration, I mean there's a little bit of moving costs, but very minor...

Mark Eric Smith
Lake Street Capital Markets, LLC, Research Division

Okay.

Aina E. Konold
Chief Financial Officer

Like transferring the inventory -- it's very minor.

Operator

[Operator Instructions] Today's next question comes from JP Wollam with ROTH Capital Partners.

John-Paul Wollam
ROTH Capital Partners, LLC, Research Division

If I can maybe step back for a minute, maybe one will focus kind of more internally and then the other kind of more external environmental. But if we start internally and I understand no one can control the macro. As you said, Jim, you're managing a dip right now. If you could just kind of maybe walk through when the team meets internally, what are kind of the couple 2 to 3 things that are really top of mind that are priorities that you want everyone kind of really drilling down to come out the other side of this best positioned?

James Barr
CEO & Director

Yes, sure. No, that's a great question. I think first and foremost, focusing on our long-term opportunity, right? We are managing a dip, but we're all here. We all chose Nautilus because we wanted to build something great. And we saw in the pandemic that the opportunity we came here for expanded significantly in a permanent way. So a lot of our discussion is how to make sure that we're on track for capturing that.

A big part of that, of course, is JRNY and making sure that -- because we see where the puck is going. I mean it's digital and equipment together reinforcing one another. Over time and it's already happening now, people buy equipment because of the digital experience and the digital experience makes the equipment better every day. So it's this type of thing. I'd say another thing is our consumer. Pillar one of our strategy is to be consumer obsessed. And so the data and insight that are coming out and trying to read both timing but the long-term needs of consumers and bake that into our product design and things like that is top of mind.

And then, of course, the short-term weighs in here, right? We -- as Aina said, we want to make sure that we're in a position after the dip that we are moving forward as quickly as possible. So when we are given choices, some things are hard choices, some are easy. One JRNY invest -- I mean, I'm sorry, on North Star investment we've taken down is our brand advertising. We spent a fair amount of money last year on brand advertising and moved our brand to a more modern place, Bowflex brand that is and we were excited about that. And we want to keep doing it. But we just don't have the wherewithal to do it when we're managing the dip. Does that mean we won't do it again? No, I think when we have the resources to do it, we'll do it.

But I'm already really seeing the fact that we invested last year in brands. And then when we take our advertising down to the lowest transactional level, I remember for this past quarter, we continue to generate sales at an amazing ROI, why? Because we actually had invested in that previously. So we continue to balance that short and long-term as we go forward in the business. Anything you would add that I didn't come?

Aina E. Konold

Chief Financial Officer

No, I think it's that balancing act. Don't lose sight of the long-term, but do what we need to do to manage through this dip.

John-Paul Wollam
ROTH Capital Partners, LLC, Research Division

Okay. Great. And then maybe from the kind of external perspective, as we head into the seasonally strong quarters and Aina I know we're maybe a couple of months in already. But maybe if you could just talk about what you are looking forward to most kind of given the broader environment, maybe that's marketing dollars going a little further than they used to, people tightening wallets and maybe trading down out of expensive gym memberships. Anything that you can kind of point to that you're looking forward to and gives you confidence in the next couple of quarters?

James Barr
CEO & Director

Yes, I mean it's some of the things I've already said. And then I talked about the new products that are value priced. I think those are ready that came out -- even though 2 of them are bikes and bikes are down, they're different bikes. They're like, for example, the recumbent is a category we pretty much own. So we think our products are well timed, the new products that we've done. We didn't go hog wild on it like we did a couple of years ago when we're getting started in JRNY, we just have the 3 that I talked about.

And then really one of our key advantages that's really fueled our growth over the last few years has been total cost of ownership relative to the competition. So we look at SKU-by-SKU comparisons of what our equipment costs versus others cost and then build in the cost of the subscription, what you get for that subscription. And we had even before the pandemic hit, when bikes were super hot, we introduced a couple of bikes that were half the price of Peloton, for example, and those did extremely well. We continue to have that cost advantage across our portfolio. And then when you add in the cost of our subscription and the digital experience, which is becoming so important to people these days, that just enhances our total cost of ownership.

So those are some of the things we feel really uplifted about. And really, honestly, with people just focusing and I said in my remarks, I'm so proud of our people for focusing in on what you control. There are times during business cycles, there's some stuff you don't control. We don't control the macro, are we concerned about it? Sure. We don't control retailer inventories, but it's temporary, right? We know this is on the other side because we see the demand for our products today. We see the demand for our products in the future. So compartmentalizing that keeping your spirits up and working through the dip, that's what responsible operators do. It may not -- it may mean you have to slow down your ambition in the short-term, but our long-term is intact and that's what keeps us going.

Operator

And ladies and gentlemen, this concludes our question-and-answer session. I'd like to turn the conference back over to the management team for any final remarks.

James Barr
CEO & Director

Thank you, everyone on the call today for your continued support of Nautilus. We look forward to talking to you again in our third quarter fiscal year 2023 earnings call in February. Have a great rest of the day, onwards and upwards.

Operator
Thank you, sir. This concludes today's conference call. We thank you all for attending today's presentation. You may now disconnect your lines and have a wonderful evening.