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SBH.N - Q2 2023 Sally Beauty Holdings Inc Earnings Call

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PRESENTATION

Operator

Good morning, everyone, and welcome to the Sally Beauty Holdings conference call to discuss the company's fiscal 2023 second quarter results. listen-only mode. After management's prepared remarks, there will be in-state. Now I would like to turn the call over to Jeff Harkins, Vice President of Investor Relations and Treasurer for Sally Beauty Holdings.

Jeff Harkins - *Sally Beauty Holdings, Inc. - VP of IR & Strategic Planning*

Thank you. Good morning, everyone, and thank you for joining us. With me on the call today are Denise Paulonis, President and Chief Executive Officer; and Marlo Cormier, Chief Financial Officer. Before we begin, I would like to remind everyone that management's remarks on this call may contain forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995.

Actual results may differ materially from those indicated by these forward-looking statements as a result of various important factors, including those discussed in the Risk Factors section of our most recent annual report on Form 10-K and other filings with the SEC. Any forward-looking statements made on this call represent our views only as of today, and we undertake no obligation to update them. The company has provided a detailed explanation and reconciliations of its adjusting items and non-GAAP financial measures in its earnings press release and on its website. Now I'd like to turn the call over to Denise to begin the formal remarks.

Denise A. Paulonis - *Sally Beauty Holdings, Inc. - President, CEO & Director*

Thank you, Jeff, and good morning, everyone. We're pleased to report another solid quarter in fiscal Q2 with notable strength in our Sally division, which delivered comp sales growth of 9.1%. On a consolidated basis, net sales increased 1% to $919 million and comparable sales grew 5.7%, with e-commerce sales up 9% year-over-year on a constant currency basis. Solid gross margin performance and prudent cost control enabled us to deliver adjusted EBITDA of $105 million.

The results reflect strong execution by our team and demonstrate that our strategies are working in what continues to be a dynamic macro environment. In the quarter, comparable transactions at Sally were up low single digits, with average ticket up mid-single digits driven by higher average unit retail prices and flat units per transaction. On the BSG side, comparable store transactions were down slightly with average ticket up low single digits, driven by higher average unit retail prices, partially offset by lower units per transaction. The color and care categories remained strong at Sally, up 6% and 2%, respectively, on a total sales basis, which includes the impact of store closures. Color continues to see strong momentum with great coverage up 14%.

Turning now to BSG. Color was up 4% on a total sales basis and nails, skincare and cosmetics performed well in the quarter. Care was down 2%, reflecting Sally's continuing to buy closer to need and the lapping of some new product launches last year. Of note, in both segments, we have made great progress on inventory. Our in-stock levels are the best we have seen since 2019 with lower total weeks on hand, enabled by our investments in planning and allocation and supply chain technologies.

Taking a bit broader look at the Sally consumer, we saw customer purchasing behavior hold steady in January and February as compared to Q1, with some softening in transactions and ticket at the end of March that continued in April. We're closely monitoring this trend and focused on actions around newness and value that inspire our customers to shop. Additionally, cost control remains a priority.

Halfway through the year, we're particularly pleased to be on track with our fiscal 2023 priorities and delivering financial results consistent with the goals we laid out last November when we shared our vision for the Sally Beauty Holdings of the future. We believe the execution of our 3 strategic initiatives is unlocking our future growth potential as we enhance customer centricity, fuel innovation and increase operating efficiency. Today, I'll provide a few highlights on each one.

Let's start with customer centricity. In Q2, we had 17 million active loyalty members at Sally U.S. and Canada, comprising 78% of sales. And our rewards credit card at BSG represented 9% of sales for the quarter. We pride ourselves on serving as a trusted resource for our DIY customers and professional stylists and they continue to award us with high NPS scores and high engagement with our brands in store, on our website and across multiple social media outlets. At BSG, we're seeing strong stylist engagement with our salon H2 platform, which has now surpassed 1,000 new digital storefronts in the first territory we're piloting.

During these initial months, we're working closely with our stylists to ensure they have the resources they need to utilize this is a powerful selling tool to grow their businesses. We're excited about the potential for this platform, which advances our goal to build a services ecosystem that empowers our solid community to operate more value-added and profitable businesses. Turning now to our Sally business. Our virtual color expert program continues to perform well with great customer response and feedback.

When customers utilize this service, we see average ticket trend higher by about 40%, driven by color and color accessories. Additionally, NPS scores are 16 points higher than our already strong baseline. Virtual color expert is currently in 75 stores. As we look to scale the initiative, we remain on track to roll out this to our e-commerce platform in the second half of the year.

Moving on to our new Studio by Sally concept. We are on track with the initial store rollout and opened our first pilot location in Dallas at the end of fiscal Q2. The store looks fantastic and we're thrilled to be bringing this experiential retail concept to market. With Studio by Sally, we're essentially updating and modernizing our proven sally formula, making it more interactive and engaging for our customers. We are ideally positioned to do this by leveraging our DIY authority and utilizing our core competencies across color and care, education and digital.

Customer response in the initial weeks has been positive, and we have 5 additional locations slated to open this fiscal year. Moving on to our second strategic initiative, owned for brand penetration and product innovation. At BSG, after a few years during which vendors were focused on overcoming pandemic-related supply chain issues, we are starting to see the innovation pipeline pick up in the pro channel. We are bringing newness to our stylists in color and care, including new bonding products from 2 of our marquee vendor partners, including Wella Ultimate Repair and Paul Mitchell Bond Rx, both of which recently launched. Additionally, we expanded our distribution with ColorView to approximately half of our stores and partnered with Danger Jones for the exclusive U.S. launch of their new Vivid color line in all BSG locations.

Danger Jones is a highly creative and edgy direct-to-consumer brand, recently brought to market by the makers of Pulp Riot, which has an incredibly strong following. This is a more intense color line. It's considered highly artistic and has the potential to bring a new customer to BSG. This is a great example of our authority in color and ability to stay at the forefront of the category. Lastly, BHG's biggest launch in fiscal '23 will be in the third quarter when we introduced Amica, a fun clean vegan haircare brand, which will be carried in the majority of our U.S. stores.

At Sally, we're continuing to bring newness to our customers, focusing on both vendor innovation and owned brands. In the second half of the year, we're excited about several new brand launches from our vendor partners across key categories like hair color, hair care and textured hair. On the owned brand side, we completed the full launch of our new bond bar line in the second quarter, which is performing well and bringing in new customers who have not shopped at Sally previously. On brand sales penetration for the Sally segment was 34% of sales in the second quarter, up compared to the prior year.

Turning now to our third strategic initiative, capturing efficiencies and optimizing our capabilities. Our store optimization program is enabling us to improve productivity and profitability while delivering a convenient omnichannel experience to our customers. In the initial months following our recent store closures, sales transfer has been strong and was a contributor to our 9% comp sales growth at Sally this quarter.

From a supply chain perspective, we've continued to increase efficiency as macro-driven disruptions have begun to recede. As a result, I am pleased to note that we are approaching the second half of fiscal 2023 with healthy inventory, and as I mentioned earlier, strong in the stock level. Lastly, our Fuel for Growth initiative is ongoing and remains an important component of how we think about the future and deliver on our profitability targets. As an example, we are currently testing a new shipment frequency to our stores that we believe will reduce our transportation costs and drive better labor productivity in both our stores and DCs while maintaining healthy in-stock levels.

In the current environment, we remain focused on driving forward our long-term growth agenda while managing expenses. We're staying close to our customers, providing them with engaging experiences and leveraging our authority in color and care to bring newness in services and assortment to both our DIY customers and professional stylist communities. We're confident that our competitive advantages and strategies will drive sustainable growth and value for our shareholders in the coming years. Now I'll turn the call over to Marlo to discuss the financials.

Marlo M. Cormier - *Sally Beauty Holdings, Inc. - Senior VP & CFO*

Thank you, Denise, and good morning, everyone. Our second quarter results reflect another solid quarter of progress and execution across our 3 strategic initiatives. Second quarter net sales increased 1% to $919 million on 378 fewer stores and 80 basis points of unfavorable foreign currency impact. Comparable sales grew a healthy 5.7% with Sally's delivering 9.1% growth in BSG returning to positive comps. Digital performance remained strong with global e-commerce sales up 9% on a constant currency basis to $87 million and representing 10% of total net sales.

We maintained strong adjusted gross margins, which came in at 50.7%. Increased product margin at Sally Beauty driven by pricing leverage and higher owned brand penetration was more than offset by lower margin at BSG due to a channel mix shift between stores and our expanded Regis business as well as a shift in some distribution center costs from SG&A expense into gross margin. Turning now to operating expense. Adjusted SG&A totaled $390 million. That's up $12 million versus a year ago, in line with our expectations and reflect higher labor, accrued bonus and advertising costs, partly offset by savings from our previously announced distribution center consolidation and store optimization plan.

It's early days, but we're pleased to see our wage investments begin to bear fruit in the form of improved retention and stronger conversion in store. Additionally, we are on track to achieve expected expense savings of approximately $50 million this year from our distribution center consolidation and store optimization plan, which will serve as a partial offset to macro-driven wage pressure.

We expect to capture the majority of those savings across the second quarter through the fourth quarter at approximately $15 million each quarter with a small portion that occurred in the first quarter. Looking forward to the third quarter, we expect SG&A on a dollar basis to be up low single digits to the prior year, driven primarily by increased labor costs and higher accrued bonus expense. Ongoing cost control, combined with our strong gross margin performance drove solid bottom line performance.

Adjusted operating margin came in at 8.3%, adjusted EBITDA margin was 11.5%, and adjusted diluted earnings per share was $0.41. Looking at segment results. Sally Beauty's strong 9.1% comparable sales increase reflects strong sales recapture from recently closed stores, contributing just under half of the increase as well as the comparison to a challenging second quarter last year, which included the impact from Omicron supply chain challenges and the onset of inflationary pressures, particularly at Sally U.S. and Canada.

Segment net sales increased 1% despite 356 fewer stores in operations versus a year ago and 90 basis points of unfavorable foreign currency impact. At constant currency, Sally e-commerce sales increased 7% to $34 million, representing 6.4% of segment net sales for the quarter. Notably, we're seeing that our Klarna buy now, pay later payment option is driving higher average order value and bringing a new and younger customer to Sally.

For the Global Sally segment, color was up 6%, driven by great coverage and care increased 2%. At Sal U.S. and Canada, color increased by 8%, while care was down 1%, including the impact of store closures. Gross margin at Sally expanded 100 basis points to 59.8%. There are 2 key drivers here. First, product margins remained strong, driven primarily by pricing leverage and higher owned brand penetration. Second, there was a favorable true-up of the noncash inventory write-down we took in the fourth quarter of last year related to the distribution center consolidation and store optimization plan. Strong sales and gross margin performance drove 200 basis points of segment operating margin expansion, which came in at 17.4%.

Moving to the BSG segment. We saw second quarter trends that were consistent with our first quarter comparable sales growth of 1.3% compares to a disruptive quarter last year that was impacted by supply chain challenges in Omicron. Net sales increased 1% on 22 fewer stores in operation versus a year ago and 50 basis points of unfavorable foreign currency impact. On a constant currency basis, BSG e-commerce sales increased 11% to $53 million or 13.7% of segment net sales for the quarter.

The color category remained strong and was up 4%, while care declined 2% at BSG on a total sales basis. As our stylists continue to purchase closer to need and we lap some new product launches from last year. The mail category was particularly strong, up 17%, reflecting strong response to our resets in the latter part of last year. Gross margin at BSG decreased 160 basis points to 38.9%, primarily driven by lower product margins due to the sales channel mix shift between stores and our expanded regions partnership as well as a shift in some distribution center costs from SG&A into gross margin.

Segment operating margin came in at 9.6%. Moving to the balance sheet and cash flow. We ended the quarter with $62 million of cash and cash equivalents and $34 million outstanding under our asset-based revolving line of credit. Our net debt leverage ratio stood at 2.2x. During the quarter, we were able to further strengthen the balance sheet by taking advantage of a narrow opening in the market to refinance our $406 million term loan. Most notably, the loan has an extended maturity date and is covenant light, substantially mirroring the covenants under our [5 and 5/8%]senior notes due 2025. Under the new agreement, which matures in February 2030, the term loan has an aggregate principal amount of $400 million and bears interest at a floating rate equal to 1 month term so for, plus a spread of 250 basis points.

The term loan was priced with an original issue discount of 99 in the quarter and includes mandatory quarterly amortization payment of 25% of the original loan amount. Subsequent to the end of our second quarter, we entered into a 3-year interest rate swap agreement on April 28, which swaps a notional amount of $200 million of the new term loan from the floating term interest rate to a fixed rate of 3.705%.

Looking at inventory. We are particularly pleased with the substantial progress we've made across composition and in stock levels. The combination of our improved capabilities and receding supply chain disruptions have enabled us to return to a healthy overall position. Quarter end inventories came in slightly above $1 billion versus $963 million a year ago. That's up 6% and primarily reflects higher vendor pricing, improved in-stock levels as well as the timing of receipts. We expect our inventory to finish this year just below $1 billion.

Second quarter cash flow from operations was $25 million and capital expenditures totaled $17 million. For the full year, we continue to expect to return to free cash flow generation in the range of $175 million to $200 million, providing us with the financial flexibility to invest in our strategic initiatives to drive long-term growth.

Turning now to guidance. I'll start with some comments on cadence. Given the challenging macro conditions we're lapping in the second quarter, we expect that this would be our highest comp performance of the year. Looking at the second half of fiscal 2023, we expect third quarter comparable sales to be in the low single digits and remain on track to achieve our full year guidance as follows. Comparable sales are expected to increase by low single digits compared to the prior year, driven by growth in key categories, sales transfer from store closures related to our store optimization efforts, our expanded Regents distribution and new strategic initiatives.

Net sales are expected to decline by low single digits compared to the prior year, reflecting the unfavorable impact of store closures from the company's store optimization efforts, net of expected sales recapture rates and the anticipated unfavorable impact from foreign exchange headwinds. At the end of fiscal 2023, store count is expected to be down 6% to 7% compared to the end of fiscal 2022 due to our store optimization plan and a small number of new store openings.

Gross margin is expected to remain above 50% and adjusted operating margin is expected to be in the range of 8.5% to 9.5%. We -- this reflects increased investments in store labor, partially offset by an expected benefit to operating earnings of approximately $10 million related to our distribution center consolidation and store optimization plan. We appreciate your time this morning. Now I'll ask the operator to open the call for Q&A.

QUESTIONS AND ANSWERS

Operator

Thank you. (Operator Instructions) One moment, please, for our first question. That will come from the line of Oliver Chen with PD Cowen.

Oliver Chen - *TD Cowen, Research Division - MD & Senior Equity Research Analyst*

The Sally comp was really impressive. It looks like recapture is really working. What are you seeing with recapture? And what should we think about happening ahead with recapture? Also, as everybody thinks about consumers and inflation, what are your thoughts in terms of how that's playing out and your solid performance? And also, is it interplaying with traffic, traffic can sometimes be fairly volatile.

Denise A. Paulonis - *Sally Beauty Holdings, Inc. - President, CEO & Director*

Oliver, thanks for the questions. I'll start off and Marlo will jump in as needed here. Overall, the Sally comp, we were really pleased with what we delivered in the quarter. And sales recapture is going in line with plan, which was about a 40% target that we communicated. So pleased to see that shift come over. That shift is particularly strong in the color side of the business, and we do anticipate that, that will continue as expected through the remainder of the year.

About half of that comp increase that we reflected in the quarter was from the recapture. As you'll remember, other factors, including owned brands and newness in the business, combined with Q2 last year being particularly challenged with both supply chain and Omicron impact really made up the difference there. So pleased with what we're seeing in Sally. We do realize that Q2 was the strongest quarter because of what we were lapping last year. Overall, though, more broadly, inflation and traffic and what we're seeing.

We came into the year knowing that there was going to be a really dynamic environment with the consumer, and that's really what we built into our targets as we came through the year. playing out largely as we expected, quarterly cadence in line with what we expected, traffic and general market trends in line with what we expected. So excited that as we're coming through the first half of the year, we're averaging out to about a 3.3% comp with a little over 9% operating margin, which is squarely what we set out to do. And as we're looking at Q3 right now, see comps around low single digits, so right on track to deliver our year. We're closely watching the consumer and understanding any behavior changes that are there. But right now, I think we have the right mix of value and newness to continue to get that customer to enjoy our shopping experience at both Sally and BSG.

Oliver Chen - *TD Cowen, Research Division - MD & Senior Equity Research Analyst*

And inventories have made nice progress. I know you've really put some prudent efforts there. Looking ahead, what are the major catalysts or initiatives we should focus on for inventory? And how is that manifesting by Sally relative to BSG in terms of the progress you're making?

Denise A. Paulonis - *Sally Beauty Holdings, Inc. - President, CEO & Director*

Yes. On the inventory front, overall, as I mentioned on the call, there's a good play that we have with the technology that we put in behind planning and allocation as well as supply chain in terms of technologies. And so we're able to get much more sharp about the amount of inventory we need in stores and in our distribution centers to be flowing that product successfully. And we've really seen great response from our vendor partners and their ability to deliver against the expectations we have. So we feel really good about that. And Marlo, do you want to comment a bit on where we're going to head for the rest of the year?

Marlo M. Cormier - *Sally Beauty Holdings, Inc. - Senior VP & CFO*

Yes. So in terms of how we see the rest of the year playing out, as Denise mentioned, we are in a really improved state where we want to be with our inventory position at just over $1 billion as we progress through the year. We see that coming down just a bit. But as we finished, we're expecting just under $1 billion.

Operator

We'll go next to the line of Korinne Wolfmeyer with Piper Sandler.

Korinne N. Wolfmeyer - *Piper Sandler & Co., Research Division - VP & Senior Research Analyst*

I'd first like to touch on just the guidance. I mean, obviously, you've put up a good quarter now, but you did talk about maybe some softness in March and maybe the early parts of April. And is that really the reasoning for not raising guidance and leaving it unchanged? And can you just kind of expand on those trends you were seeing here in the early parts of April.

Marlo M. Cormier - *Sally Beauty Holdings, Inc. - Senior VP & CFO*

Thanks for the question. I'll reiterate that the cadence in the quarters of the year are playing out largely as we expected coming into the year. So the shape of the curve from Q1 to Q2 with comp sales in line with what we had anticipated with Q2 lapping some challenging times last year. In the back half, as we said, low single-digit comps, really reflecting what we had anticipated for the year.

When you comment on the consumer, I'll say that on the BSG side, stylist behavior remains very consistent with what we've seen in the last few quarters. They are buying closer to need, being a bit more frugal, no substantial changes there at all. We called out in our prepared remarks on the Sally side that we did see a really consistent January and February, but with a slight bit of pressure against both traffic and basket as we were at the end of the quarter and then coming into April.

Nothing outsized, and that's what I want to reinforce, but we did see a little bit of a shift of a little bit more frugality coming in there. That's reflected in the low single-digit comp outlook that we have for Q3. But as I said before, the focus that we have on the Sally side with newness with our own brands with a focus in nail and some other areas where we can add items to the basket still feel really good about where we're headed for the full year.

Korinne N. Wolfmeyer - *Piper Sandler & Co., Research Division - VP & Senior Research Analyst*

Great. And then maybe can we just...

Marlo M. Cormier - *Sally Beauty Holdings, Inc. - Senior VP & CFO*

Sorry, go ahead.

Korinne N. Wolfmeyer - *Piper Sandler & Co., Research Division - VP & Senior Research Analyst*

One more in and a little bit on the BSG side of the business. Can you just comment how much Regis contributed this quarter? And then in terms of the end consumer in the professional channel, is that still holding up and it's really just the stylists that are shifting their spending patterns and kind of like how much they're spending out of time, but that end consumer is still healthy. Can you just comment on that?

Denise A. Paulonis - *Sally Beauty Holdings, Inc. - President, CEO & Director*

Yes. In reverse order, I'll start a little bit with BSG side and the stylist and the consumer for that stylist. In general, what we're hearing from stylist is a continuation of the trends before that they will have some clients who might not get as many add-on services or might stretch their time between color treatments, just in an effort to save a little bit of money here and there. We continue to see that. When you think about the products that we sell through to our stylists, a very large proportion of that actually goes down the drain in the salon.

It is used by the pros and then a small amount of the business is that retail direct to consumer. I think our stylists are very focused on retailing that product is it's a good add-on profitability and then a way for them to know their clients will keep that great look that they have leaving a salon when they use those products. And the piece we're most encouraged about on our side is with our platform offering that we have and that we're piloting in a couple of markets or a couple of states today, the ability for that stylist to have another way to retail product as well.

So no real change in trend there at all. And I think your second question had been about trends in BSG and what we were seeing with Regis. We came into the year expecting that our Regis business would double throughout the year. We remain largely on track for that. So that would have been consistent in our second quarter as well. That's in Q4 is when we turned that on last year.

Operator

We'll go next to line Ashley Helgans with Jefferies.

Ashley Elizabeth Helgans - *Jefferies LLC, Research Division - Equity Analyst*

First, just any thoughts around the current promotional environment? And then any trends by product category, color, hair care that you see emerging.

Denise A. Paulonis - *Sally Beauty Holdings, Inc. - President, CEO & Director*

Sure. Promotional environment remains very consistent with what we've seen for the last few quarters. Overall, our promotion investment is directionally in line with what we had seen earlier in the year as well. We are seeing good vendor support. Our vendors would like to see units continue to move. And as we have good offerings where that elasticity is there and available, our vendors are really supporting us in those efforts. And so we appreciate that and continue to watch the broader dynamic as well. In terms of category trends, I think a lot of continuation from what we've seen before.

On the BSG side, lots of focus on the care portion of the business and what will be best for someone's customer. So at the end of the day, what's the treatment that they need, what's the help that they need in that business. Really excited to see new bonding products come out from both Wella and John Paul Mitchell that we think are going to resonate very well with our stylist base. We are also very excited on the BSG side about Danger Jones, a vivid color line that's getting great response, very trendy in terms of even the packaging of what's come out, and we're excited to see where that goes. And then for us, distribution around ColorView and Amica really round out the portfolio for what our consumers are looking for. So in general, we're still seeing a lot of focus on express color.

But more broadly very excited that the newness that's coming through the BSG channel and from our vendor partners really steps up this quarter as they've now kind of fully lapped supply chain and other pandemic-related challenges. And on the Sally side, great interest in our own brands, great interest in hair repair products there. gray coverage remains extremely strong, up 14% in the quarter. That doesn't mean this is -- were challenged. It just meant they held a little more steady while gray coverage really grew. And then we're seeing some fun add-ons. You think about the Taylor Swift and the trends behind that. People are getting into things like [Cartincil]. Not a huge business, but things that reflect kind of the current environment of what's trending out there in the marketplace.

Operator

We'll go next to the line of Olivia Tong.

Olivia Tong Cheang - *Raymond James & Associates, Inc., Research Division - MD & Research Analyst*

I wanted to ask you about the delta between your comp performance in SBS and BSG because it sounds like the magnitude of store closures is a big factor. And obviously, that's more -- significantly more pronounced at the Sally side than on the BSG side. But can you talk about what else drove that differentiation between performance and SBS versus BSG?

Denise A. Paulonis - *Sally Beauty Holdings, Inc. - President, CEO & Director*

Yes. So yes, I think the key comp out there in terms of the magnitude of the comp being a strong 9%, and then BSG returned as a strong -- or to the positive comp at the low single digits. As you mentioned, over half or about half that at the SBS level of that comp is being driven by store optimization. And then underneath that, we've got strong performance, especially in our color category on the Sally side.

On the BSG side. And then thinking about it in terms of year-over-year performance, we've got a really big comparison that we're trying to lap from Omicron last year, that was a big drag as well as just the inflationary pressures that we're starting to appear in some supply chain challenges. That was on the Sally side. And we had that as well on the BSG side, but not to the same degree that we have seen on the Sally side.

Olivia Tong Cheang - *Raymond James & Associates, Inc., Research Division - MD & Research Analyst*

And then there's 17 million active loyalty members now over 3/4 of sales. Could you talk a little bit about the profile of your loyalty members relative to the non-loyalty members, average basket, frequency of purchase versus the average -- and we talked a little bit about this at our conference, but the sales to nonmembers, are they new people? Or can you talk about what efforts are being made -- what efforts are being made to convert more of them into loyalty members?

Denise A. Paulonis - *Sally Beauty Holdings, Inc. - President, CEO & Director*

Let me try with that one. I'll start in reverse order. When we think about loyalty and non-loyalty, our nonloyalty members are likely folks to -- they could be new. They might be shopping for the first time or so and don't yet see the benefit of signing up for the loyalty program. They could also be members who just choose to want to remain not identified that come through in the transactions. The differential between nonloyalty and loyalty, we do definitely see with our loyalty members more frequent transactions, higher basket, typically higher cross-category penetration in terms of what they're putting into their basket.

And the group that we're really focused on within our loyalty program, while we love them all, the top tier of our customers within our loyalty platform are really are heavy shoppers. They typically have a color-oriented basket. They will come in 2 or 3x more frequently than the average customer. And we really see that reflected in both basket size as well as the total spend per year with that frequency being up. So we continue to do things that will incent them to come in terms of how we talk to them about the program. And we also have offering that our Sally customers can also participate and get a credit card if they would choose to do so.

We see that penetration much lower on the Sally side than we see with the 9% penetration on the BSG side. But it is another opportunity, particularly for Pros who might be shopping in Sally as well to have that advantage. And then things we keep doing to enhance the customer experience and give them more ways to pay.

We recently launched Klarna on our e-commerce site. And the buy now pay later opportunity is bringing in new customers to us, and it's actually increasing basket as well. So it's a great potential for people to participate more in the electrical categories where things are a bit more expensive, and they might want a more simple payment process that they could go through. So we continue to innovate on other ways that would bring new customers into the mix as well.

Operator

We'll go next to the line of Simeon Gutman with Morgan Stanley.

Michael Efram Kessler - *Morgan Stanley, Research Division - Research Associate*

This is Michael Kessler on for Simeon. Just a question on the expense structure. You talked about savings from DC store closures. It sounds like labor level staffing, advertising is all kind of normalizing or getting there. Can you just talk about the -- where we are on that normalization path or steady-state path? And does that mean, I guess, going forward, how to think about a comp leverage point for the business?

Denise A. Paulonis - *Sally Beauty Holdings, Inc. - President, CEO & Director*

Yes. On the SG&A side, so we did talk about how to think about Q3, right, from a dollar basis, it is a step up from Q2 as well as last year. So compared last year. It is a low single-digit increase year-over-year, and that's driven by the wage inflation and the bonus accrual. Thinking about it in terms of kind of run rate and how we look at it going forward from Q2. There is a bit more of a step-up from wages, just given the timing of merit. But at that point, you would expect a stabilization of the wage pressure.

Operator

Anything further Mr. Gutman?

Michael Efram Kessler - *Morgan Stanley, Research Division - Research Associate*

All good.

Operator

And I'll now turn it over to Denise for some closing remarks.

Denise A. Paulonis - *Sally Beauty Holdings, Inc. - President, CEO & Director*

Thank you, and I appreciate everyone joining us this morning. We continue to be very excited about the path that Sally Beauty Holdings is on and look forward to providing additional updates in the future. And as a final note, as always, thank you to all of our associates across the world for all you do every day to help serve our customers.

Operator

Thank you. And as a reminder, today's conference was recorded for replay. Please refer to the company's press release for that replay information. That does conclude our conference for today. Thank you for your participation and for using AT&T bond Conferencing. You may now disconnect.