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Arhaus Inc.

Third Quarter 2021 Earnings Conference Call

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CORPORATE PARTICIPANTS

John Reed, *Co-Founder, Chairman and Chief Executive Officer*

Jen Porter, *Chief Marketing Officer*

Dawn Phillipson, *Chief Financial Officer*

Wendy Watson, *Senior Vice President, Investor Relations*

CONFERENCE CALL PARTICIPANTS

Curtis Nagle, *Bank of America*

Jonathan Matuszewski, *Jefferies*

Peter Keith, *Piper Sandler*

Simeon Gutman, *Morgan Stanley*

Adrienne Yih, *Barclays*

Peter Benedict, *Robert W. Baird*

Cristina Fernandez, *Telsey Advisory Group*

Steve Forbes, *Guggenheim Securities*

PRESENTATION

Operator

Good morning, and welcome to the Arhaus Third Quarter 2021 Earnings Conference Call.

At this time, all participants are in a listen-only mode. A question-and-answer session will follow the formal remarks.

Please note that this call is being recorded and the reproduction of any part of this call is not permitted without written authorization from the Company.

I would now like to turn this call over to your host, Ms. Wendy Watson, Senior Vice President of Investor Relations. Thank you, ma'am. You may begin your presentation.

Wendy Watson

Good morning, and thank you for joining Arhaus' inaugural earnings call.

On with me today are John Reed, Co-Founder, Chairman and Chief Executive Officer, Jen Porter, Chief Marketing Officer, and Dawn Phillipson, Chief Financial Officer.

John will begin with a company overview and operational details, Jen will discuss the status of marketing initiatives across our omni-channel footprint, and Dawn will cover our third quarter performance and outlook. After their formal remarks, we will open the call to questions. For Q&A, please limit to one question and one follow-up. If you have additional questions, you may return to the queue.

We issued our earnings press release and our 10-Q for the quarter ended September 30, 2021 before market open today. These documents, along with supplementary slides, will be made available on our Investor Relations website at ir.arhaus.com. A replay of the call will also be available on our website within 24 hours.

As a reminder, remarks today concerning future expectations, events, objectives, strategies, trends or results constitute forward-looking statements. Actual results or events may differ materially due to a number of risks and uncertainties. For a summary of these risk factors, and additional information, please refer to this morning's press release and the cautionary statements and risk factors contained in the Company's third quarter 10-Q, as such factors may be updated from time to time in its other filings with the SEC. The forward-looking statements are made as of today's date and, except as may be required by law, the Company undertakes no obligation to update or revise these statements.

We will also refer to certain non-GAAP financial measures and this morning's press release includes the relevant non-GAAP reconciliations.

I will now turn the call over to John.

John Reed

Good morning, everyone, and thank you for taking the time to join our Third Quarter 2021 Earnings Call, our first as a publicly traded company following our IPO in early November.

This is an exciting milestone for our Company, and I want to thank the more than 1,400 Arhaus team members for working together to get us to this point. You truly are the best in the business and I am proud to be part of such a dedicated team who cares for one another, our clients, and what we do.

We had a record third quarter performance, with net revenue in both our retail and eCommerce channels up 69% and comparable growth up over 61%, compared to the third quarter last year. Dawn Phillipson, our CFO, will cover our third quarter performance and the outlook for the remainder of the year in more detail later in the call, but we are extremely pleased with the trends in our business.

Because this is our inaugural earnings call, I will take a few minutes to introduce Arhaus, describe what makes our brand so special, and explain why I am so excited about the growth going forward.

I founded the Company 35 years ago, with the simple mission that furniture should be responsibly sourced, lovingly made and built to last. In order to fulfill our mission, we built a unique model that differentiates us in the marketplace in four key areas and offers multiple strategies for growth. We believe we are in a position to nearly double the size of our business over the next few years and drive profitable long-term growth for years to come.

Our first key differentiator is our product. All of our products are designed in-house and sourced directly from leading artisan vendors around the world. By sourcing our own exclusive products, we control the design, we control the incredible quality, the supply chain and our costs. Through our vertically integrated design and sourcing model, we offer a globally curated assortment of handcrafted products that represent our “livable luxury” aesthetic.

The second key differentiator is our showrooms. From our very first showroom in Cleveland, Ohio, we have always believed that retail is theater and our showrooms should showcase our products in a way that is both inspirational and aspirational. When clients walk into our showrooms, we want them to envision that it could be an extension of their own home. We put as much detail and attention into our showrooms as we do in our products, and expanding our showroom base represents a tremendous whitespace growth opportunity and significantly builds our brand awareness.

In the third quarter, we opened two new showrooms, a traditional showroom in Salem, New Hampshire and a Design Studio in Burlingame, California. We also relocated our showroom in McLean, Virginia to Tyson’s Galleria and converted this showroom into the new format. We ended the third quarter with 77 showrooms across 28 states. We expect to end the year at 79 showrooms. In the U.S. alone, we believe we can grow to as many as 165 total showrooms, and our target is to add five to seven new showrooms per year for the foreseeable future.

Within our showrooms, we are also growing our In-Home Designer program that offers clients the complimentary service of having a designer personally come to their home. At the end of the third quarter, we had 65 in-home designers in 54 showrooms, and the average order value when a client purchases through one of our in-home designers is three times greater than the standard order. We intend to have at least one in-home designer per showroom, with some locations accommodating more than one.

The third differentiator is our omni-channel experience. Jen will cover our omni-channel initiatives in detail later in the call, but we take the same inspirational approach to showcasing our products online and in our catalogs as we do in our showrooms. Our omni-channel approach serves to further increase our brand awareness and represents another lever of our growth. We only recently began investing in our digital capabilities, and with eCommerce comprising approximately 18% of net revenue today, we see a significant runway to grow our eCommerce sales as we enhance our omni-channel capabilities.

The fourth key differentiator is our client-first mentality. This core value runs through our business. Everything we do, from the way we design our products, build our showrooms, hire, train and retain associates, and invest for growth, is with our clients in mind. I invite you to visit one of our showrooms and experience our client-first mentality and our incredible design consultants firsthand.

With our tremendous opportunity to continue growing and scaling our business, we are closely focused on the current supply chain dynamics and making investments to expand our distribution capabilities.

On the inbound side of the supply chain, we are working closely with our vendor partners to fulfill orders and ramp up production. Our vendors have been incredibly resilient through the strong demand environment, increasing their capacity, growing with us and further deepening our relationships. At the same time, we are also expanding our vendor base and bringing in more new products.

In upholstery, we expect to see improvements in lead times with the opening of our new upholstery manufacturing and distribution facility in North Carolina. This facility will double our in-house upholstery manufacturing capabilities.

On the outbound side of the supply chain, we are increasing our capacity and expanding our footprint. We have begun a 230,000 square foot expansion of our Ohio distribution and corporate office facility, as well as expanding our offices in North Carolina, which will add 310,000 square feet of distribution capacity, in addition to 187,000 square feet of upholstery manufacturing.

In the second half of 2022, we are planning to add a third distribution facility in the western United States, where we have significant growth opportunities. Along with our ongoing efforts on the inbound side, the increase in our outbound capacity will further allow us to get products to our clients more quickly and more efficiently, reducing backlogs and shortening lead times.

In summary, we feel very good about the trends in our business and the investments we are making to drive long-term growth. At a time when consumers are spending more and more time in their home, investing in their homes and looking for more functional spaces, we think we are very well positioned to continue to gain market share. The premium home furnishings market in the United States represents a $60 billion opportunity. Today, our market share is less than 1% of this large and rapidly growing market, and we have multiple avenues, and a long runway, to pursue sustainable growth.

I could not be more excited about the future of Arhaus. We know our products are unique in the marketplace. We have built an incredible team and incredible infrastructure to grow and to scale the business.

Now, I'll pass the call over to Jen Porter to review the omni-channel and digital initiatives.

Jen Porter

Thank you, John, and good morning, everyone.

One of Arhaus' biggest opportunities to increase our market share is to grow our brand awareness. We are in the enviable position of introducing a meticulously crafted and proven heritage brand, grown mostly organically over the past 35 years, to a highly fragmented and, arguably, underserved market.

In 2019, we began significantly increasing our investment in digital initiatives and brand marketing overall. We developed a test-and-learn strategy that balances a brand awareness approach with high return on advertising spend, or ROAS, driven targeted campaigns. Our focus is on profitable and meaningful long-term growth of the brand. We have a proven ability to drive brand awareness by opening more showrooms, and we see continued opportunity by further enhancing and expanding our omni-channel, marketing and technology capabilities.

For the third quarter, we are excited to report healthy client growth over Q3 last year in terms of both existing client numbers and value, as well as new client acquisition numbers and value.

Our approach to clients is omni-channel. Our direct mail channel continues to perform incredibly well for us, with our Fall Catalog hitting homes at the end of August. We mailed this catalog to our largest circulation ever, while achieving a higher ROAS than last year. We are particularly excited to see direct mail continue to perform not only with our existing client base, but also as a significant driver of traffic to our website and new clients to the brand. Early results for our Holiday Catalog, which hit homes in the beginning of November, are looking very promising, as well.

Q3 saw us increasing our media advertising and partnerships, participating in both House Beautiful's Whole Home and Architectural Digest's Iconic Home campaigns, along with continuing to develop and expand upon our influencer program on social media. In September, we reached 1 million followers on Instagram.

On the eCommerce front, we saw strong eCommerce growth, driven by owned, earned and paid marketing efforts. We continue to believe that eCommerce not only drives direct eCommerce revenue, but also serves as a gateway to the brand and a discovery tool for our product. We are thrilled to be launching our new website this month, which will immediately step-up our online user experience, allowing us to better showcase our brand and share product knowledge with our online clients. The site will also bolster our product merchandising capabilities, as well as position us for further optimization throughout 2022, and beyond. Along with other digital initiatives launched this year, such as our 3D room planner, digital catalogs and virtual showroom tour, we believe we have tremendous opportunity to continue to deepen our client relationships and grow our eCommerce business.

We look forward to sharing more information about our omni-channel development and growth in future quarters once our new site is up and running.

For now, I'll pass over to Dawn Phillipson.

Dawn Phillipson

Thank you, Jen, and good morning, everyone.

As John mentioned, we are pleased with our third quarter results and the underlying trends in our business. Demand and net revenue were very strong in the quarter. We're working hard to address the supply chain challenges to deliver product in a timely manner to our clients, and we are investing for growth, as you heard from John and Jen.

As a reminder, because our IPO was in early November, we were a private company in the third quarter with minimal tax obligations.

For the third quarter, net revenue increased 68.7% to $203 million. The growth was driven by increased demand for our products, as well as elements of our supply chain beginning to catch up with client demand. We're pleased to announce comparable growth was 61.3% in the quarter.

Demand remained strong in the quarter, as well, with demand comparable growth of 28.3% on a one-year basis and 72% on a two-year stacked basis. Given the substantial demand comp growth that we began to see in the third quarter of 2020, and the corresponding increase in our backlog, we've been focused on reducing delivery times from the peak levels experienced earlier this year. Accordingly, we expected comp growth to outpace demand comp growth in the quarter, and our results were in line with those expectations.

Gross margin increased 87.6% to $85 million in the quarter, driven by our higher net revenue, partially offset by the related increase in product and transportation costs, as well as higher credit card fees related to demand. Gross margin as a percent of net revenue increased 420 basis points to 41.7%, the improvement reflecting our ability to leverage our fixed costs over higher net revenue.

SG&A expenses increased 66.2% to $68 million, primarily from investments to support the growth of our business in corporate and warehouse expenses, higher demand-driven showroom compensation expense, increased marketing investment, and one-time costs related to the IPO. As a percentage of net revenue, SG&A expenses declined 50 basis points to 33.5%.

Interest expense in the quarter was approximately $1 million.

Net income of $14 million in the third quarter of 2021 was up significantly, compared to approximately $1 million the third quarter last year, and Adjusted EBITDA increased over three times to $31 million, from $10 million in the third quarter of 2020.

Year to date through September 30, net income increased to $31 million and Adjusted EBITDA increased to over $90 million, compared to $14 million and $41 million, respectively, in the first nine months of 2020.

Turning to the balance sheet, as of September 30, cash and cash equivalents were $149 million and the Company had no long-term debt.

Net merchandise inventory was $171 million as of September 30, a 58% increase from December 31, 2020, as we built inventories in response to our strong ongoing client demand. As I mentioned earlier, while we are focused on reducing our backlog and our comp growth is now outpacing our demand comp growth, demand remains very strong and we are increasing our inventory levels accordingly.

For the nine-month period ended September 30, 2021, net cash provided by operating activities was $143 million. Post-IPO, the Company remains in a net cash position.

For the nine-month period ended September 30, capital expenditures were nearly $30 million and landlord contributions were $11 million. As a result, company-funded capital expenditures were approximately $18 million for the nine-month period.

Regarding cap ex and investment in new showrooms, this is a good time to point out our strong unit economic model and return on investment from new showrooms. We target an average investment in a new showroom of approximately $1.4 million, with the landlord contributing the balance of the total $3 million to $4 million cost. We expect new showrooms to be profitable within the first year of opening, and by year three, they have an average net revenue of $6 million, with a 27% contribution margin.

As I mentioned, we completed our initial public offering after the third quarter. We used the proceeds from the IPO to pay the $64 million exit fee due under our former term loan that we terminated in December 2020. We allocated the remainder of the IPO proceeds for general corporate purposes, including the replenishment of working capital after the payment of a pre-IPO distribution to Arhaus LLC unitholders.

Regarding our full year 2021 and implied fourth quarter outlook, please refer to this morning's press release.

Underlying our outlook, particularly for net income, is continued expectation that higher freight costs will pressure gross margin in the fourth quarter, as higher cost inventory is delivered. As a reminder, in the fourth quarter, we will also incur a $15 million derivative expense related to our former credit facility, $15 million in one-time IPO and reorganization costs, and we will begin to incur public company costs of approximately $3 million per quarter, all impacting SG&A expenses. These items are fully factored into our outlook for the full year and implied fourth quarter guidance.

Note, that going forward, we plan to issue annual guidance, which will be updated quarterly.

That concludes our prepared remarks, thank you for your attention, and we would now like to open the call up for questions.

Operator

At this time, we'll be conducting a question-and-answer session. One moment while we poll for questions.

Our first question comes from the line of Curtis Nagle with Bank of America. You may proceed with your question.

Curtis Nagle

Good morning, and thanks very much. Yes, I guess the first one—one of your competitors, obviously, reported last night. I think there were some questions around whether they had seen any change in behavior in terms of, I don't know, where people are shopping and what channels, or perhaps more demand due to Omnicron, I think they said not really, but just curious if you guys had any comments on that, and then I'll have just a quick follow-up.

Dawn Phillipson

We continue to see demand strong in both channels. eCommerce continues to perform really well, as it has throughout COVID, but showroom traffic has picked up, as well. We aren't seeing meaningful trends differentiating in kind of the third quarter or fourth quarter to date based on the new variant.

Curtis Nagle

Okay, fair enough, and still very early, so that makes sense, and then just, forgive me if I've missed this, but in terms of when we're thinking backlog peak, is it fair to assume kind of mid next year, or how is that looking right now, and how has that maybe changed in terms of your expectation, say, from, I don't know, three months ago?

Dawn Phillipson

Yes, our expectation for the backlog is consistent with how we were thinking about it a few months ago. We continue to see really strong demand, as we noted in the press release, and based on that strong demand and continuing freight constraints, we do expect that that backlog to remain elevated and we will work through it throughout 2022. We're not seeing significant increases in cancellation rates, so clients continue to be willing to wait for the merchandise and the product. So, we feel confident in our strategy. We do continue to be opportunistic and bring in product as quickly as possible and in a financially prudent manner, so we think our strategy is working, and we'll continue to closely monitor cancellation rates, but to date we feel good about how we're handling it.

John Reed

Curtis, just to add, answer that, we do expect the backlog to continue. However, the amount of wait time the clients have continues to get a little bit tighter; in other words, they don't have to wait quite as long as they did six months ago. That's really the key that we're looking at, is we may not be 100% in-stock, but you don't have to wait X amount of time, which, as Dawn just mentioned, we're seeing—you know, clients are used to that. They've been trained around the world to wait now for two years for things, almost. So, they're willing to wait, they know it. It's product that they're investing in their home, not throwaway product, so it will be there long term for them.

Curtis Nagle

Right, and just to clarify, you guys are not seeing an increase in cancellations; is that correct?

Dawn Phillipson

That's correct, Curtis. Those remain lower than pre-COVID rates.

Curtis Nagle

Perfect. Okay, thank you, appreciate it.

Dawn Phillipson

Okay.

Operator

Our next question comes from the line of Jonathan Matuszewski with Jefferies. You may proceed with your question.

Jonathan Matuszewski

Great. Good morning, John, Dawn and Jen. Congrats on the strong quarter.

John Reed

Thank you.

Jonathan Matuszewski

I have two questions. The first one is on just promotionality. I think a key question in retail these days is how sustainable the pullback in promotional posture is once COVID fades. So, maybe just kind of take a chance to kind of share Management's confidence in being able to see success with more full-priced selling in a future backdrop where there may not be a pandemic and there may not be long lead times. So, just maybe talk to that dynamic. Thanks.

Jen Porter

Hi, Jonathan, this is Jen Porter. Yes, we feel very confident in our current approach. We actually started pulling back on promotional activity back in 2019, so pre-COVID, and we were seeing really strong responses to it at that time. It really allows us, as a brand, to focus more on the quality of our product, the stories of our artisans, the uniqueness of what we are offering to our clients, and we see really strong responses to that. Our clients are looking for that quality esthetic and they're willing to pay for it. So, we have continued to pull back on promotions throughout the COVID time period. We do still run promotions from time to time, particularly over three-day weekends. But, we think that pullback can continue going into 2022.

Jonathan Matuszewski

Great, that's helpful, Jen. Then, I guess, Dawn, just a follow-up question on freight costs. I'm curious how those are trending in October and November against maybe initial expectations you had for 4Q. I'm not looking for specific guidance for next year, but just directionally, do you think freight costs as a percentage of inventory should still be higher versus the recent trend, or do you think it's kind of practical that maybe that ratio could be more flattish, or even down, next year? Thanks.

Dawn Phillipson

Sure. We continue to be opportunistic and really thoughtful in our approach to inbound product, between bringing in product at the spot rate and the contracted rate. We don't have any material changes to the forecast with regards to freight increases. I think we were appropriately conservative with how we thought about those for next year. We are seeing a little bit of favorability in the fourth quarter relative to what we had provided a few months ago. But, that being said, the freight industry continues to be volatile. Until we have a very clear line of sight into any favorability that would be ongoing, we're going to kind of hold steady with how we're thinking about 2022. So, the gross margin rate for the fourth quarter, I would expect somewhere in the kind of 38% to 39%, so slightly better than where we were anticipating a few months ago.

John Reed

Jonathan, just to add to that, keep in mind, you may or may not know, but over half of our product is purchased here in the United States, so we have not seen significant increases in freight costs, like the containers are, and that's, we think, a competitive advantage of ours.

Jonathan Matuszewski

That's helpful, thanks for the color, and best of luck for the rest of the quarter.

John Reed

Thank you.

Operator

Our next question comes from the line of Peter Keith with Piper Sandler. You may proceed with your question.

Peter Keith

Thanks. Good morning, everyone, and congrats on the first quarter out of the gate here. I wanted to ask about the new North Carolina facility with the upholstery production and DC capabilities, could you give us the timing on when you expect that's going to open, and, then, are you seeing any potential delays just as it would relate to hiring or buildout?

John Reed

Sure, I can take that, Peter. The building is built. We're actually getting permits, hopefully, this week or next week. We fully intend to be in there before the year's out, putting product in there and getting going. As far as the team goes, they are almost hired. It's been a great response. It's a great building to work out of. We give great benefits, and so forth. So, we're pretty well almost fully staffed. We're excited to go. We moved a few people down from Cleveland to help manage it, and so forth, they've been down there for a month or so, and we're ready to go. We're just waiting on one inspector, which we hope we'll hear from very soon.

Peter Keith

Great, okay, that's exciting, and maybe a separate question, I'll direct it to Dawn, on the model. So, a really nice increase in the outlook for Q4 versus what you were looking for earlier, and we're looking at, I guess, if our math is right, you know, kind of midpoint, raising revenue by about $14 million and raising EBITDA by about $6 million, so it's a really healthy mid-40s contribution margin, if our math is right. Is there anything unique about Q4 that allows you to get that type of margin, or is that something we could see in later quarters, as well?

Dawn Phillipson

We're continuing to work through the backlog. Our strategy to bring product in at some of those higher spot rates, you're seeing some of that on the top line flow through. We also have worked really diligently in the warehouse and with our third-party providers to expand the capacity flowing out of our existing headquarters building. So, we're really pleased with where we expect the fourth quarter to come in and hopeful that we'll be able to continue that cadence.

Peter Keith

Okay, sounds great. Well, good luck with the holiday season.

John Reed

Thank you.

Operator

Our next question comes from the line of Simeon Gutman with Morgan Stanley. You may proceed with your question.

Simeon Gutman

Hey, good morning, everyone. My first question is on sales. Can you talk about how you characterize the underlying momentum of the business? Do you feel like it's accelerating, do you think it's holding? It looks like the top end of your sales guide implies a modest acceleration, and like we calculate this geometric back. But, curious if you think is that fair, or do you think things are getting sequentially stronger?

Dawn Phillipson

Hi, Simeon. You know, while we don't provide guidance on demand, we haven't seen any meaningful change in demand trends in the fourth quarter on a two-year stacked basis. We are facing larger year-over-year comparisons in the fourth quarter, so we're looking at it on a two-year stacked basis.

I will note that, similar to what we anticipated and saw in the third quarter, we would expect comp sales growth to outpace the demand comp growth as we continue to work through the supply chain constraints and deliver against a backlog of orders, but demand continues to be healthy and we're pleased with what we're seeing in our client base.

Simeon Gutman

Okay, thanks, and then my follow-up is on Adjusted EBITDA. In the fourth quarter, despite the revision higher, it still looks like it will be down year-over-year, and we know why, investments and maybe some freight pressure. Can you talk about the drivers between those two, when we sort of lap them both, and then whether there's anything different in timing as far as the investments go, whether they're shorter in duration, longer in duration, and when we might see EBITDA flip? I'm not trying to get quarterly guidance for next year, but just, conceptually, when we see EBITDA growth year-over-year.

Dawn Phillipson

As we think about the investments we're making in the business, in the fourth quarter, we're going to see the expenses and the investment in North Carolina and some IT initiatives come into play in the P&L, and as we think about next year and onboarding a western distribution center that is larger in size than North Carolina, it will take time to start to see some leverage on those. We don't expect to come out of the gate on both of those facilities with everything running smoothly at 100%, so we have thoughtfully forecasted a ramp-up out of those facilities. I think you can kind of think about the timing of those as a scale of both.

Then, as we think about freight costs, I mentioned earlier we are forecasting those to remain elevated through next year. Until we have line of sight into those clearly coming down consistently, it's just prudent for us to expect those to remain elevated.

Simeon Gutman

Okay, thanks. Happy Holidays and good luck in the fourth quarter.

John Reed

Thank you.

Dawn Phillipson

Thank you.

Operator

Our next question comes from the line of Adrienne Yih with Barclays. You may proceed with your question.

Adrienne Yih

Yes, good morning, and congrats again on your first quarter out of the box, very successful. John, I was wondering—or Dawn—can you discuss the price increases that you took kind of early fall? I believe it was in the high-single-digit range. When did you take them, what was the customer reaction? Clearly, it doesn't seem like any noticeable impact on demand. What's the opportunity for 2022 further increases?

Then, Dawn, if you can talk about what is the assumption for spot versus contract in your fourth quarter guidance, what does it look like for Q1, and does Q1 have any more or similar pressure on freight and inventory deliveries? Thank you.

John Reed

Sure, I can start with that. Yes, we did take price increases. We have not seen much demand falling off, if any. The clients seem to be fine, sales teams adjusted to it, and it seems like it's good to go. As far as the future goes, your guess is as good as mine. Prices are going up all over the place. We think things have stabilized quite a bit from the beginning of this year, where lumber prices were two or three or four times higher and then they came back down. At least things don't seem to be as volatile as they were. We're hopeful, as I'm sure everybody in the world is, that inflation will get under check here. But, if we do get price increases, we intend to pass them along, raise prices, and really protect our margin.

Dawn Phillipson

Hi, Adrienne. With regards to the spot versus contract rate, it varies by origin, and it really is contingent on what's going on at each individual port. What I'll say is that the fourth quarter is relatively consistent with how we approached it and the rates that we—or the percentages between spot and contract that we deployed in the third quarter. We are forecasting those to continue throughout 2022, but it's really just contingent upon container availability and what's happening at each individual port, which, as you know, is not just subject to Arhaus shipping. So, that's how we forecast it. We think we're appropriately conservative in '22.

Andrean Yi

Okay, thank you very much. Best of luck for holiday.

John Reed

Thank you very much.

Operator

Our next question comes from the line of Peter Benedict with Baird. You may proceed with your question.

Peter Benedict

Great. Hey, good morning, everybody. I guess my first question, maybe for Jen, just on the new web platform that's going to be launching here later this month, just curious, can you expand on maybe two things: one, as a customer, what are we going to see, maybe, that's most noticeable or most different; and then what is it really going to allow you to do, I guess, next year that you have not been able to do in the past, or with data analytics, or just what would you kind of call out as the biggest deliverables there? That's my first question.

Jen Porter

Yes, hi, Peter. Yes, we're really excited about the new site launching. We're in final testing mode right now, so coming very quickly. I think the biggest thing that we're really excited about for the immediate impact is just the huge step-up in sort of customer user experience, so really focusing in on that immersive creative, content and imagery and storytelling, and really working to bring the Arhaus brand to life on that digital channel.

I think one of the most amazing things about the Arhaus story is this brand has been getting—being built for 35 years, and our showrooms, we know what happens when clients are in there, and we've had a good site experience, but we're really excited for clients to be able to really deep-dive into the brand, into the product, get that sort of "wow" factor when they see imagery, and then get into the details of the story, and then also making the shopping and the purchase journey easier and more seamless, and ultimately less stressful for clients. So, we're excited about things like navigation and merchandising capabilities, to really help that client journey as they're starting to explore the product, get the information that they need, find other products that they might like, and really be able to do that in their homes and then be able to connect that to their in-showroom experience, or do the entire thing digitally online.

Looking forward to next year, I think, with the replatform, really excited about the increased analytics capabilities and back-end functionality. So, you know, over time, really being able to lean more into AI, product discovery, content personalization, and the like, analytics will really allow us to understand how clients are engaging with the platform, so we can constantly test and improve conversion optimization and opportunity, and really just getting to know our clients better, and then probably—I know you only asked for next year, but I think the other really key thing for us to it really just improves our speed to market for new innovation, as well.

So, we really see this as a great step-up and that's going to be the immediate impact on our eCommerce business, but it's really setting us up for success in the future to stay at the head of enhancements that we can make to that online part of our business.

Peter Benedict

All right, that's great content, thank you, and I guess, maybe somewhat related, certainly, over to brand awareness, and just curious, some of the strategies around that. I know opening the showrooms on their own drives some brand awareness, but maybe talk about your plans from a marketing perspective, where you're allocating your spend over the next year or two, and just how your brand awareness sets up right now nationally and maybe if there's any pockets regionally that are particularly strong or underdeveloped. Just any context around that and your kind of plans for driving brand awareness would be helpful. Thank you.

Jen Porter

Definitely. Yes, I mean, I think you nailed a big one. Our showrooms are just such an incredible new client acquisition vehicle for us, they introduce the brand to new pockets and markets around the country, and so we've been seeing incredible success with that. We've been opening new showrooms, we have additional new showrooms planned for next year, and we're excited to continue to support that. We are very purposeful about the marketing support we put around those showrooms. It's great knowing that we have this key tool in those markets. We can really amplify our efforts of digital marketing, catalogs, social media in those pockets, as well, to amplify those effects.

I think, overall, though, as we're thinking about brand awareness, we really look at it as an omni-channel opportunity and holistically across the marketing mix. Within our direct mail program, we are very focused on our prospecting audience and have really been working over the last few years to increase our prospecting circulation and getting these incredible introductions to the brand into the homes of clients, and we've been really excited by the results we've been seeing this year, and looking to continue that next year.

Digital marketing and more broad-based marketing is also a great opportunity to support what we're seeing, but I think there are also—we touched a little bit on the call about some of our partnerships and media efforts. We really haven't done much about brand before. Arhaus really grew relatively organically for 35 years, and so we're just at the beginning of investing in those areas, and really looking to continuously try new things and test and optimize upon what works.

Then, social media and influencers, I noted that we hit a million followers on Instagram in Q3, and we just see so much runway and potential in those areas, both in our own channels, but also partnering with influencers and partners, just to spread that message to a wider audience.

So, we have a lot of levers to pull, and I think we're really excited just to continue playing and pushing into those and seeing what works the best.

Peter Benedict

That's great. Thanks so much and good luck.

John Reed

Thank you.

Jen Porter

Thank you.

Operator

Our next question comes from the line of Cristina Fernandez with Telsey Advisory Group. You may proceed with your question.

Cristina Fernandez

Good morning, and congratulations on your first report here. I wanted to ask, also, on supply chain, but specifically on Vietnam, what are you seeing there through your partners as far as production, and perhaps any color you can share on your exposure and the ramp-up in manufacturing out of that country?

John Reed

Yes, Vietnam has probably been one of the sore subjects over in Asia. They were basically shut down for quite a while, they are up and running now, and we believe that our shipments will be pretty much on time going forward here.

One thing to note is Vietnam is a very small part of our business, I think we only have two or three vendors there, so it hasn't impacted us much at all. We had pretty good inventory stock, so we're not seeing a decrease in sales in just Vietnamese products. Whereas, I'm sure if we had a lot more eggs in the Vietnam basket, it would be a whole different story.

Cristina Fernandez

Thank you, and then my second question is on stores. Perhaps you can talk about your store pipeline for next year, I guess any locations that you're particularly excited about, and anything to note, underperformance you're seeing out of your Design Centers, you know, the smaller format stores. I noticed a few, but any color there would be helpful. Thank you.

John Reed

Sure. Yes, we're constantly working on new stores. I think the guidance has been we're going to open five to seven. We feel confident we'll be in that range. We're not giving out locations at this point. As far as Design Studios, we've only had one open the whole year, very happy to see the results of that one. We've had another one open for a few months and another one open a few weeks. The newer ones also have started right out of the gate pretty strong on demand sales. Of course, to turn those into actual sales usually takes a little bit, just for the backlog, and so forth. We do have two more Design Studios being opened before the year is out, so we'll have five in total by January 1, and after that we're very excited to really tweak them, merchandise them, remerchandise them if we need to, learn a lot into 2022, and then from there we'll see if we can really grow that business, as well as the regular stores.

Cristina Fernandez

Thank you.

John Reed

You're welcome.

Operator

Our next question comes from the line of Steve Forbes with Guggenheim Securities. You may proceed with your question.

Steve Forbes

Good morning. Just maybe for Jen, I'm curious if you could discuss any client demographic or client engagement differences that you are seeing within the new customer base relative to the existing base. I think you mentioned something like better marks here about new customer growth. So, just curious what you're seeing, anything notable to call out.

Jen Porter

We've been really excited by our new customer growth over the last sort of year-and-a-half, and we continue to see that, so that is really exciting. It's really too early to have a full picture as to how those clients are behaving relative to clients who joined the business earlier, but, really, the initial result is that they're spending more than new clients were before COVID, but we're seeing that trend in our existing client base, as well, and currently their behavior, their repeat behavior seems like it's very similar. So, we're going to be continuing to monitor it and pay very close attention to it, but, overall, it's looking like they're coming in and being really great clients to our brand.

Steve Forbes

Then, maybe just a quick follow-up on the in-home designer initiative. Can you update us on the percentage of demand generated from that group, your hiring plans for the next couple of years, and whether the average order value generated from those designers has changed at all relative to what was discussed during the IPO process?

Dawn Phillipson

Sure. Hey, Steve. The AOV, we said earlier, a few months, is over three times that of a non-in-home designer-assisted sale, and we continue to be consistent with that. When we think about their penetration, we are seeing increases in that program, relative to where we were at last year, so we're really pleased with how that program is continuing to perform. We will continue to expand that program. By the end of this year, we'll have several more in place, and then next year we'll continue to ensure that our existing store fleet has the appropriate staffing levels, and all new showrooms will also have this program deployed, as well. So, we're really confident and we're excited about this program, and it seems to be working really well for us.

Steve Forbes

Thank you. Best of luck.

Dawn Phillipson

Thank you, Steve.

John Reed

Thank you very much.

Operator

Ladies and gentlemen, we have reached the end of today's question-and-answer session. I would like to turn this call back over to Ms. Wendy Watson for closing remarks.

Wendy Watson

Thank you, everybody, and we will look forward to talking to you again next quarter.

John Reed

Happy Holidays, everyone, and thank you for your time.

Operator

Thank you, everyone, for your participation in our call and interest in Arhaus. We look forward to speaking to you next quarter.