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Sleep Number Corp. (SNBR)

Q1 2021 Earnings Call

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Analyst, KeyBanc Capital Markets, Inc.

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MANAGEMENT DISCUSSION SECTION

Operator: Welcome to Sleep Number's Q1 2021 Earnings Conference Call. All lines have been placed in a listen-only mode until the question-and-answer session. Today's call is being recorded. If anyone has any objections, you may disconnect at this time.

I would like to introduce Dave Schwantes, Vice President of Finance and Investor Relations. Thank you. You may begin.

Dave Schwantes

Vice President-Finance, Investor Relations & Decision Support, Sleep Number Corp.

Good afternoon and welcome to the Sleep Number Corporation first quarter 2021 earnings conference call. Thank you for joining us. I am Dave Schwantes, Vice President of Finance and Investor Relations. With me today are Shelly Ibach, our President and CEO; and David Callen, our Chief Financial Officer.

This telephone conference is being recorded and will be available on our website at sleepnumber.com. Please refer to the details in our news release to access the replay. Please also refer to our news release for a reconciliation of certain non-GAAP financial measures and supplemental financial information included in the news release or that may be discussed on this call.

The primary purpose of this call is to discuss the results of the fiscal period just ended. However, our commentary and responses to your questions may include certain forward-looking statements. These forward-looking statements are subject to a number of risks and uncertainties outlined in our earnings news release and discussed in some detail in our Annual Report on Form 10-K and other periodic filings with the SEC. The

company's actual future results may vary materially. We also want to refer you to our recently updated investor presentation, which can be accessed on our website at sleepnumber.com.

I will now turn the call over to Shelly for her comments.

Shelly Radue Ibach

President, Chief Executive Officer & Director, Sleep Number Corp.

Good afternoon and welcome to our first quarter earnings call. My SleepIQ score was 88 last night. Through continuous innovation across our enterprise, Sleep Number is winning consumers' hearts, minds, and share of wallet. We are improving lives through better quality sleep, while delivering exceptional value for all stakeholders.

First quarter demand was more than 30% higher than prior year, which reflects broader and deeper brand relevance as we build on the accelerated shift in consumer trends towards prioritization of their health, faster adoption of digital products and services, and increased preference for brands with an authentic purpose. We see these trends continuing to benefit performance during the balance of this year and beyond.

Our strategic investments and leadership in sleep science are propelling the advancement of 360 smart bed features that improve sleep health and drive customer engagement. And Sleep Number's culture of individuality and wellbeing provides the foundation for our mission-driven team, who passionately innovate with agile learning and exceptional execution.

Our first quarter performance was driven by a significant acceleration in both consumer demand and profitability. We are raising 2021 EPS guidance to at least \$6.50, compared to reported EPS of \$4.90 in 2020 and \$2.70 in 2019.

Net sales increased 20% to \$568 million, with demand growth accelerating from previous quarters to more than 30% year-over-year and over 40% on a two-year basis. Greater than \$50 million of smart bed deliveries shifted out of the first quarter due to temporary foam supply constraints. Operating income grew 45% to \$76 million. EBITDA grew 39% to \$97 million, and EPS increased 85% to \$2.51.

We also had record return on invested capital of 27.6%, up 850 basis points from prior year, as we continue to realize compelling value from disciplined capital deployment. To support our expanding business, we have increased our credit revolver to \$600 million.

Our purpose, to improve the health and wellbeing of society through higher quality sleep, is resonating with consumers through our brand positioning. With sleep science-based innovation, brand accelerators and our digital ecosystem, we continue to build momentum. Our strong first quarter demand growth represents a sequential acceleration from each of the past two quarters on a one, two, and three-year basis.

By leveraging extensive research and insights from more than 9 billion hours of sleep data, we constantly advance the smart bed experience to help individuals improve their quality sleep. Early last month, we introduced the new Performance and Classic Series 360 smart beds, with a digitally-led marketing campaign. Each ad is deepening customer engagement with the Sleep Number 360 smart beds by connecting the health and wellness benefits of proven quality sleep.

With the knowledge from our proprietary sleep data, we recently introduced My Daytime Alertness feature. This new capability provides advanced real-time insights that pair a sleeper's personal data with self-reported information and sleep science to deliver individualized recommendations for how to improve sleep.

In addition, the SleepIQ update includes simplified navigation for customers to access other wellness features, such as circadian rhythm insights, nighttime Heart Rate Variability, and monthly HealthIQ wellness reports. These sleep experience advancements, including relevant personalized health metrics, are driving increased customer engagement, brand advocacy, and referrals.

Lifelong relationships remain an important source of ongoing efficient growth through referral and repeat sales, which represent about half of our demand. In addition, our digital ecosystem is enabling Sleep Number to efficiently acquire new customers. We are optimizing digital content, which is tailored by audience and platform, in real time for efficiency and scale.

Results include highly qualified digital traffic growth of over 40% in the quarter and record levels of conversion. Since transitioning to all smart beds nearly three years ago, we have driven average demand growth of 14%. Sleep Number's agile go-to-market strategy and exclusive direct-to-consumer distribution model also remain strong drivers of sustainable growth. Our sell-from-anywhere model directly aligns with how customers want to shop: in-store, online, or by phone, delivering a seamless value-added experience across all touch points.

Average sales per store for the first quarter grew 9% to nearly \$3.2 million on a trailing 12-month basis. One-third of Sleep Number stores now average more than \$3 million, and 16 stores exceeded \$6 million in sales, with 1 store over \$8 million. Online sales also remained strong, growing 116% in the quarter to nearly 14% of total sales, compared to approximately 8% last year.

We are benefiting from the cumulative impact of Sleep Number's strategic initiatives within our mission-driven culture. Like most businesses, we continue to navigate supply chain cost and availability pressures related to the ongoing global impact of the COVID-19 pandemic. Our unique business model and high sales growth and gross margin rates give us great flexibility as we manage for total operating margin. We have taken \$20 million of pricing for 2021 and will adjust offers to drive favorable total margin through discounts, financing mix, and attach.

Our vertical structure affords optimized solutions as we remain focused on demand, business leverage, and capital efficiency. Raising 2021 guidance reflects the strength of our first quarter performance and underscores the value inherent in the convergence of our growing sleep innovation leadership, pioneering 360 smart beds, digital ecosystem, and lifelong customer relationships.

More sleep data leads to better consumer insights and advancement of sleep health innovation. Broadening relevance drives accelerating demand and increases customer acquisition, retention and referrals, resulting in higher revenues and profit margins. Growing scale improves operational efficiency and effectiveness across our core infrastructure, which is increasing profitability and cash generation as we expand our smart sleep ecosystem.

The remarkable strength of our highly engaged solution-orientated team and vertically integrated business model demonstrates compounding benefits. Thank you Sleep Number team for your ongoing courage, resourcefulness, and passion to innovate for an exceptional customer experience, and thank you for continuing to champion a kinder, more just society for all. As our performance indicates, we have built a compelling, synergistic strategy with increasing consumer relevance. The outcome supports our commitment to create and sustain superior shareholder value.

Now, David will provide additional financial details on first quarter performance and outlook for 2021.

David R. Callen

Executive Vice President & Chief Financial Officer, Sleep Number Corp.

Thank you, Shelly. I'd like to add my thanks to our Sleep Number teams and business partners. We are incredibly proud of your tenacity and creativity to navigate the challenges of this pandemic. You continue to find ways every day to improve the lives of Sleep Number customers with proven quality sleep. Since our earnings call two months ago, we have further advanced our digital capabilities, business processes, and performance drivers.

We introduced daytime alertness insights, completed the introduction of the new Sleep Number 360 smart beds, opened two additional assembly distribution centers, and improved more than 200,000 lives. We evolved our digital marketing and consumer engagement tools and applied selling from anywhere retail capabilities when snow and ice disrupted much of the country. We protected service levels for customers by leaning into resilient supplier partnerships and efficiently expanded our revolving credit facility to \$600 million through robust banking relationships.

These are examples of how Sleep Number teams continuously strengthen the business, leading to greater than expected performance this year and beyond. Q1 demand drove the highest quarterly sales orders in company history, more than 30% over the prior year and more than 40% greater than two years ago. This accelerated demand combined with the temporary foam chemical supply constraints, resulted in more than \$50 million in deliveries shifting out of the first quarter. However, foam production is now expected to normalize by the end of Q2.

We continue to be pleased with the higher than expected demand growth as consumers embrace proven quality sleep from Sleep Number. The strength and acceleration of performance has led us to raise our 2021 EPS guidance to at least \$6.50. Net sales of \$568 million were 20% greater than the prior year, marking the third consecutive first quarter with double digit net sales growth. Average revenue per unit grew 3% this quarter which is especially noteworthy given units grew 17% and online business made up nearly 14% of total net sales. Generating growth from both ARU and units over time is a unique strength of this business.

In the first quarter, we continue to advance customers online experience while adding 11 new and relocated stores. We are targeting approximately 650 stores by year-end and expect sales growth from new stores to be additive in the back half of 2021 and beyond.

Interestingly, many of the financial metrics for Q1 were very similar to Q4 of 2020, though Q1 was one week shorter. We remain committed to delivering at least 300 basis points of operating profit leverage in 2021 versus 2019. Recall that this two year comparison is most relevant as it eliminates the noise from comparisons to 2020 which were affected by COVID and the extra fiscal week.

I'll also provide one year insights for certain metrics to help with modeling. Our Q1 net operating profit rate of 13.4% levered 570 basis points over the first quarter of 2019 on 33% two year net sales growth. R&D spending on exciting new innovations drove a 58% two year increase but resulted in just 30 basis points of deleverage over that period. This was more than offset by 50 basis points of G&A leverage plus sales and marketing initiatives that drove 440 basis points of leverage over two years.

Q1 gross margin expanded 110 basis points in two years to a healthy 62.6%, while gross profit dollars expanded 36% to a quarterly record of \$356 million. It is worth noting that the Q1 gross margin rate was pressured versus 2020 by reinstated incentive comp, commodity and labor inflation, and constrained efficiencies from shipping more than \$50 million in deliveries out of the quarter. Despite these pressures, the operating synergies of our

vertical business model contributed to record quarterly operating profits of \$76 million, 45% higher than the prior year.

In just two years, we have grown Q1 operating income 134% on 33% net sales growth. Our first quarter record EPS of \$2.51 was 85% higher than 2020 and more than three times the \$0.80 of earnings in Q1 of 2019. Clearly, using all performance levers is creating superior shareholder value.

We continue to prioritize investment in those performance levers, both through capital spend and directly through the P&L. During Q1, we generated cash from operations of more than \$112 million, 31% higher than the prior year and 64% higher versus Q1 of 2019, even while spending more to support our near and long-term growth drivers.

We also invested \$12 million in capital projects and \$167 million in Sleep Number stock during Q1. The renewed \$600 million board authorization for future investments in Sleep Number shares underscores the tremendous value we see in our stock.

We continue to target leverage of 2.5 to 3 times EBITDAR, ending Q1 with leverage of 2.3 times EBITDAR. Executing this unique sleep science and digitally-enabled strategy is driving exceptional performance. The increased 2021 EPS guidance of at least \$6.50 reflects the strong start we had in the first quarter and the confidence in the performance the balance of the year. This implies one year growth of at least 40% over record 2020 EPS excluding the 53rd week last year and more than 140% since 2019.

A reminder of a few other assumptions regarding the increased EPS outlook, consistent with the context provided last call include: We expect to employ the benefits of our vertical structure to deliver more than 300 basis points of operating profit margin expansion versus 2019. This is based on two-year net sales growth of at least 30%, which is above the high end of the range provided just two months ago.

This two-year operating margin expansion is expected while leaning into near- and long-term growth drivers, especially in R&D which is expected to be approximately \$65 million in 2021, compared to \$35 million in 2019. We now expect approximately \$25 million of pressures on gross margin for the balance of the year for higher than expected commodity, labor, and logistics costs. We expect to offset these pressures with approximately \$20 million of surgical pricing actions and efficiency gains, particularly in sales and marketing.

We expect to grow top and bottom lines each quarter in 2021 versus 2019 with more of the growth coming in the first half of the year. With the guidance increase, we now expect to generate record cash from operations of approximately \$300 million in 2021. We are thrilled with the progression of the business and the performance of our teams. Our commitment to the pursuit of breakthrough performance is delivering superior and sustained value for Sleep Number stakeholders.

Gabriel, at this point, please open the line for clarifying questions.

QUESTION AND ANSWER SECTION

Operator: Absolutely. [Operator Instructions] The first question will come from the line of Peter Keith of Piper Sandler. Please go ahead.

Peter Jacob Keith

Analyst, Piper Sandler & Co.

Q

Hi. Good afternoon everyone and congrats on the continued success. Maybe just quickly follow on the comments around pricing. I had a – I did have a question there. So the \$20 million that you're taking strategically, does that more than offset the input cost inflation that you're seeing?

And secondarily, couldn't you go up more than \$20 million? I guess mathematically that just looks like a 1% price increase. Historically, you've taken 2% price increases. And certainly your broader industry peers have taken substantially more. So if you could maybe dig into the pricing dynamic a little bit more.

Shelly Radue Ibach

President, Chief Executive Officer & Director, Sleep Number Corp.

A

Sure, Peter. Thank you for the question. We took this pricing in early March. And, of course, we continue to learn more every week regarding commodity pressures. And we took the pricing on selected SKUs. And as you stated and we covered, it's worth about \$20 million. Our unique model, Peter, gives us a range of options as we manage for total operating margin in our business.

And clearly, we have additional – we certainly have additional pricing actions available to us. And we can be quite fluid between our selling process, discounts, financing and attach. That gives us the ability to trade up the line based on our adjustments or make short-term, real-time adjustments in discounting and financing. We love our competitive positioning right now. And we have such a strong value equation compared to anyone across the board and love the units and the acquisition we're driving.

We have a lot of year in front of us. And while the \$20 million with the newer information on commodity costs gets us close, but not quite all the way, we have so many levers to be able to pull that are yet in front of us. And again, we're going to focus on total operating margin. You can see the strong progress we've already made here in the first quarter and that certainly led us to raising our guidance to at least \$6.50 for the full year.

Peter Jacob Keith

Analyst, Piper Sandler & Co.

Q

Okay. That's helpful. The second question I wanted to ask and I'm not trying to sound naïve, but it's a question that we're getting a lot from investors is, what's changed with Sleep Number? Clearly, there is some demand as a result of maybe COVID and the stay-at-home dynamics, but at the same time your growth has been quite spectacular.

We could argue you're growing much faster than the overall industry and you're seeing very nice flow-through in your model. So just big picture, what do you think is driving this elevated demand and do you think there's some sustainability to this even as the vaccinations increase and people start spending on things outside the home?

Shelly Radue Ibach

President, Chief Executive Officer & Director, Sleep Number Corp.

A

This is an important question, Peter, and we're super excited. This goes back to when we fully transitioned to 360 smart beds nearly three years ago with now an average demand over that span of time of 14% and that's all since we transitioned to the smart beds. Along with that, we also brought our digital marketing buying capability in-house and we've been perfecting and advancing that.

And if you think about algorithms and the precision that comes with them, more sleep data leads to better insights and advancement of innovations that are relevant for the consumer. And at the same time, this additional data and knowledge that we have on the marketing side also leads to more efficient and effective targeting and qualified digital traffic which is converting at a higher level.

So these two combined are driving both the demand and then, of course, with the scale that's also driving the stronger flow-through. And then I have to highlight our big unlock during COVID, once the COVID pandemic hit last year around selling from anywhere. We pivoted to a new model that is very unique to our vertical model and that was a big unlock for us in the selling and marketing expense line which we said last year at over 300 basis points of leverage and that we are going to hang on to that as we moved into this year and we're certainly demonstrating that we have and that we intend to and see greater and greater efficiency.

So, is it sustainable? Absolutely. And this is the innovation strategy that we set out to deliver back in 2012, at the beginning of this transformation of the company. And here we are, and I would say it's early days. This is a great opportunity to join Sleep Number and get behind us as we are early on our path of sleep innovation leadership leading to connected health.

Peter Jacob Keith

Analyst, Piper Sandler & Co.

Q

Okay. That's a great summary. Thanks so much and good luck.

David R. Callen

Executive Vice President & Chief Financial Officer, Sleep Number Corp.

A

Thanks, Peter.

Operator: And your next question will come from Brad Thomas with KeyBanc Capital. Please go ahead.

Bradley Thomas

Analyst, KeyBanc Capital Markets, Inc.

Q

Hi. Good afternoon everyone. I'll add my congratulations on a nice start to the year here. My first question was just going to be about your updated full year guidance. I think you beat consensus here in 1Q by \$0.68. There's \$50 million of sales that you think will happen in 2Q that could have happened in 1Q. And you're raising the full year by \$0.50. Just to connect the dots, are there any other moving pieces as we think about the balance of the year, or are you all just being conservative with flowing through the strong 1Q? Thanks.

David R. Callen

Executive Vice President & Chief Financial Officer, Sleep Number Corp.

A

Yeah. Hey, thanks, Brad. As like every year, there are a lot of moving parts and we're pretty early in the year. We just gave guidance two months ago and we've raised our guidance for the year by \$0.50. We are very confident in

the trajectory of the business. But we're managing both some tailwinds, we talked about the demand side being at the high end of our expectations, actually above our high end of our expectations.

And we're balancing those against some of the headwinds that we're facing with new commodity costs that we've highlighted, and we're taking all of that into account as we think about the full year. And we are – couldn't be more thrilled about the performance of our teams and the business and the way consumers are reacting to the superior sleep that they get through Sleep Number's products.

We are also very happy with – a big shout-out to our supply chain teams. I mean, it's been really challenging to navigate through the supply chain's challenges globally, not just ours. But this is happening across businesses everywhere, and our teams have done a phenomenal job working with our partnerships, with our suppliers, and making sure that we get more than our fair share of supply and make sure that we're serving our customers.

So, all-in, we did get a bit more tax benefit in Q1 than what we had expected. That's built into the full-year thinking as well. It impacted full year by about a dime compared to prior year. So, all-in, we're going to use all of our levers to deliver superior financial performance, at least \$6.50 of EPS which is, as I said, more than 140% of just two years ago in 2019 when we were running clean in 2019.

Shelly Radue Ibach

President, Chief Executive Officer & Director, Sleep Number Corp.

A

Brad, I'll add on for the demand side. We continue to see momentum in demand here in Q2. It's obviously early, but I think it's important to underscore that, and we're excited about what is yet to come, thus the raise to \$6.50 here early in the year. And also, we recognize that people are out more and they're spending more and that bodes well for us. It's working great. And we are excited about what that will mean for us for the remainder of the year.

Bradley Thomas

Analyst, KeyBanc Capital Markets, Inc.

Q

That's very helpful. And then the 2Q estimate is going to be a tough one, I think, for all of us to get our arms around given you had stores close to not open last year. If we look at having grown 30% versus about two years ago and then layering on another \$50 million of orders that could come in, you can get a revenue number over \$500 million for 2Q. Obviously it's a pretty big growth rate here. Can you help us get any more sense of how to think about modeling that second quarter?

David R. Callen

Executive Vice President & Chief Financial Officer, Sleep Number Corp.

A

Brad, you are thinking about it the right way. We talked about this year in our original guidance two months ago that for the full year about 4 to 5 points of our growth was going to be because of the strong ending backlogs that we were servicing here in the first half.

We've always said that we expected more of our growth to come in the first half of the year. But we do expect growth top and bottom line every quarter versus 2019 here in 2021. So directionally, you're thinking about it the right way. We expect to have a pretty big quarter in second quarter.

Bradley Thomas

Analyst, KeyBanc Capital Markets, Inc.

Q

Thanks so much.

David R. Callen

Executive Vice President & Chief Financial Officer, Sleep Number Corp.

A

Thank you.

Operator: Your next question will come from Bobby Griffin of Raymond James. Please go ahead.

Bobby Griffin

Analyst, Raymond James & Associates, Inc.

Q

Congrats on a great first quarter. David, maybe to follow up on the backlog question first and I got a longer-term strategic question for you. First on the backlog, that 45 points of growth call it like \$80 million to \$90 million round number coming in, then you add on the \$50 million or so that you have shifting. If the materials are there, could you really take that backlog back down to like a normalized level [indiscernible] (33:40)? Or even if the materials are there, there's capacity issues that you have to stretch out over a couple of quarters?

David R. Callen

Executive Vice President & Chief Financial Officer, Sleep Number Corp.

A

Yeah. Hey, Bobby, you're breaking up a little bit. I'm pretty sure I heard your question, so I'll do my best. But if I...

Bobby Griffin

Analyst, Raymond James & Associates, Inc.

Q

[indiscernible] (33:56).

David R. Callen

Executive Vice President & Chief Financial Officer, Sleep Number Corp.

A

No, no. I'm good. I think you're asking about whether the backlog impact for the year was about \$80 million to \$90 million. That's directionally right. And then thinking about when that would be serviced in terms of how that would benefit our first half of the year or this year. We do expect a more normalized type of backlog but our growth has been exceptional.

And so we are having higher backlog than we've ever had. And that's just going to be the state of the union we expect during the course of the year. That's all baked into our thinking of how we're going to deliver more than \$6.50 of EPS here in this year and plan to do even better than that in years beyond.

Bobby Griffin

Analyst, Raymond James & Associates, Inc.

Q

Yeah. I guess, that was part of it. I guess the second part of it was, if you take the \$90 million and you add on the \$50 million, you probably had a [ph] \$140 million (34:50). Do you have enough like – if all the materials and the foam and everything that's there and available for you to get which is a big if, I understand that. But is there enough capacity that you can get all that to flow through in one quarter, or is it just naturally going to have to bleed over a couple of quarters just because it's such [Technical Difficulty] (35:05) relative to the capacity of the business, I guess, is a better way to ask that question.

David R. Callen

Executive Vice President & Chief Financial Officer, Sleep Number Corp.

A

Yeah. Well, Bobby, some of that backlog was serviced clearly in the first quarter, and what we're saying is that relative to where we expected to be, we carried \$50 million of deliveries...

Bobby Griffin

Analyst, Raymond James & Associates, Inc.

Okay.

Q

David R. Callen

Executive Vice President & Chief Financial Officer, Sleep Number Corp.

...out of Q1. So that's really how to think about it.

A

Bobby Griffin

Analyst, Raymond James & Associates, Inc.

[ph] That is helpful (35:32). That's helpful. And then secondly, I think the long-term target of gross margin is 52% to 54% (sic) [62% to 64%] last quarter in the slide deck. [indiscernible] (35:40) some of the drivers...

Q

David R. Callen

Executive Vice President & Chief Financial Officer, Sleep Number Corp.

Okay, Bobby, I think we lost you. I can answer the question though that – where I think you were headed. Gabriel, we're still on the line, is that correct?

A

Operator: We still are.

David R. Callen

Executive Vice President & Chief Financial Officer, Sleep Number Corp.

I assume we just lost Bobby. Okay. So I'll go ahead and answer his question about gross margin. In our long-term slide in our Investor Relations materials, we say 62% to 64% gross margin rate. Look, we've said this many times over the course of history that we're not going to corner ourselves by trying to chase gross margin rate. We're going to use all of the levers of our business model to pursue sustainable and superior shareholder value creation. And that's through the full bottom line, that's through the full P&L.

A

Shelly highlighted that we've got a lot of levers to use, not just pricing, to get after covering our commodity cost pressures that we're absorbing here in 2021. We're going to use them all. And that's a great thing with this business model that we will certainly have – we have a lot of levers at our disposal to deliver superior shareholder value. We expect to use them all here in 2021. We're not guiding to a gross margin rate. We're telling you that we are committed to delivering more than 300 basis points of net operating profit expansion versus 2019.

Shelly Radue Ibach

President, Chief Executive Officer & Director, Sleep Number Corp.

And we're also certainly not shying away from our very strong gross margin rate, and it will continue to be an important source.

A

David R. Callen

Executive Vice President & Chief Financial Officer, Sleep Number Corp.

So, Gabriel, with that, let's – I don't know if Bobby got back on the line. We can check if he's there, or we can move on to the next question.

A

Operator: Not quite yet. So we can move on to next question from Atul Maheswari of UBS. Please go ahead.

Atul Maheswari

Analyst, UBS Securities LLC

Q

Good evening. Thanks a lot for taking my question. So versus your guidance two months back, you're taking up the revenue estimate by quite a bit, but you're keeping the margin expectations the same. So I guess, what has changed that would cause operating leverage to be limited on faster sales growth? I understand the input cost pressures but you are taking up pricing in response to that. So why should there be not more leverage on faster sales growth?

David R. Callen

Executive Vice President & Chief Financial Officer, Sleep Number Corp.

A

Oh, Atul, we're certainly going to drive that. The idea of being this early in the year and taking up our guidance for the year by \$0.50 is a pretty significant move. We're saying at least \$6.50. We think we've got levers to drive stronger performance than that, but we think that that's the right place to land, all things considered. We talked about managing a full year and managing all of the puts and takes that happen during the course of a year.

There's a ton of year left. We're thrilled with where we are. We're thrilled with demand. We're thrilled with how the company is performing. But, yeah, we have some uncertainties about where the commodity cost pressures might go. We also are thinking about potentially changing consumer behaviors, we don't know. But we know that we can operate well in any environment, and that's what gives us confidence about the numbers and the color that we provided for the guidance today.

Atul Maheswari

Analyst, UBS Securities LLC

Q

Understood. Thanks.

Shelly Radue Ibach

President, Chief Executive Officer & Director, Sleep Number Corp.

A

And Atul, the at least \$6.50 of EPS reflects at least a 30% growth on a two-year basis for the full year, and a 300 basis points of operating margin leverage.

David R. Callen

Executive Vice President & Chief Financial Officer, Sleep Number Corp.

A

It's – sorry, the \$6.50 is...

Atul Maheswari

Analyst, UBS Securities LLC

Q

Okay.

David R. Callen

Executive Vice President & Chief Financial Officer, Sleep Number Corp.

A

All right.

Atul Maheswari

Analyst, UBS Securities LLC

Q

Yeah. So I guess, as a follow-up, if we roll back the clock 12 months to your first quarter 2020 results, I think back then you mentioned that April 2020 was down like about 50% or so. So are you able to provide a quarter-to-date comp for this current month, April 2021?

David R. Callen

Executive Vice President & Chief Financial Officer, Sleep Number Corp.

A

Sorry, could you repeat that question?

Atul Maheswari

Analyst, UBS Securities LLC

Q

So I think in the month of April of 2020, I think your comps were down 50%, obviously due to the store closures. So are you able to provide a quarter-to-date number for this month?

David R. Callen

Executive Vice President & Chief Financial Officer, Sleep Number Corp.

A

Well, we don't provide a lot of insights on interim basis, because it's – a couple weeks don't make up a month or a quarter. But we have said that the strong growth that we saw in the first quarter has continued here so far in the second quarter. And that is even on a two-year basis or a three-year basis even. So even if – that's why we provided those reference points so that you can take out the impact of COVID and the closed stores last year. Reflecting back on your previous comment, I just want to clarify that the two-year growth in EPS at, at least, \$6.50 is at least 140% increase over 2019, \$2.70.

Atul Maheswari

Analyst, UBS Securities LLC

Q

Got it. Thank you and good luck with the rest of the year.

David R. Callen

Executive Vice President & Chief Financial Officer, Sleep Number Corp.

A

Okay. Thanks a lot.

Operator: Your next question will come from Curtis Nagle with Bank of America. Please go ahead.

Curtis Nagle

Analyst, Bank of America Merrill Lynch

Q

Good evening. Thanks very much. Just a couple of clarifying questions, one, just on the comment about growth in every quarter, for 4Q, did that include the impact of lapping the extra week?

David R. Callen

Executive Vice President & Chief Financial Officer, Sleep Number Corp.

A

That comment is about 2021 versus 2019, not 2021 versus 2020.

Curtis Nagle

Analyst, Bank of America Merrill Lynch

Q

I see. Okay.

David R. Callen

Executive Vice President & Chief Financial Officer, Sleep Number Corp.

A

And so because there are so many changing dynamics in 2020, it makes it very unusual. And it is – I really encourage you to look at your models versus 2019, use the color that we've provided today, and use it and go from there.

Curtis Nagle

Analyst, Bank of America Merrill Lynch

Q

Okay. Certainly fair. And then just clarifying on the price increase, you said tactical, not exactly sure where you're taking it. Just like sort of [indiscernible] (42:26) looking at the MSRPs in your beds, and I know you usually don't sell the MSRP, but looking at that, it doesn't look like it's changed in the past. I don't know, maybe since 2018, so if you can just be a little more specific about where those tactical price increases are coming from.

David R. Callen

Executive Vice President & Chief Financial Officer, Sleep Number Corp.

A

Well, we were very tactic – very laser-focused on certain bed sizes and certain models, and you may not see that in those prices that you're looking at.

Curtis Nagle

Analyst, Bank of America Merrill Lynch

Q

Okay. I'll follow up later. Thanks very much. Appreciate it.

David R. Callen

Executive Vice President & Chief Financial Officer, Sleep Number Corp.

A

Okay. You bet.

Operator: And your last question will come from Seth Basham of Wedbush. Please go ahead.

Seth Basham

Analyst, Wedbush Securities, Inc.

Q

Thanks a lot, and good afternoon. My first question is just thinking about the backlog, again just to make sure I'm clear, so \$50 million carried out of Q1, where do you expect the backlog to be out of Q2?

David R. Callen

Executive Vice President & Chief Financial Officer, Sleep Number Corp.

A

A more normal level. And the \$50 million isn't a reflection of our backlog. It's a reflection of where we thought we would be versus where we landed. Just want to make sure that we were clear on that, right?

Seth Basham

Analyst, Wedbush Securities, Inc.

Q

Okay.

Shelly Radue Ibach

President, Chief Executive Officer & Director, Sleep Number Corp.

About two weeks of delivery.

A

Seth Basham

Analyst, Wedbush Securities, Inc.

Got it. So you don't expect any excess backlog or deliveries that are outstanding coming out of the second quarter?

Q

David R. Callen

Executive Vice President & Chief Financial Officer, Sleep Number Corp.

Yeah. Directionally, we believe that our backlog will be more normalized. And we are experiencing pretty phenomenal demand, and that can always affect the timing of when deliveries are made. But that's how we're thinking about it. In terms of the supply chain challenges that caused a hiccup in making deliveries here in first quarter, we don't – we expect those to be resolved here in the second.

A

Seth Basham

Analyst, Wedbush Securities, Inc.

Got it. So when you think about the vertically integrated model that you are – so you have – you definitely do not have foam production, or you'd come into these challenges. Are there other areas with providers of yours or suppliers of yours that you've encountered challenges?

Q

David R. Callen

Executive Vice President & Chief Financial Officer, Sleep Number Corp.

So, look, this challenge isn't even the result of the [ph] foamers (44:44). It's not their problem. It's the challenge with the chemical producers. And you saw that's been a trifecta of bad luck for those producers. And they are coming back online, and their production capacity is very strong. And we expect here in the second quarter that that's all stabilized. We've already seen some improvement in our delivery windows and our levels of service. And our first available date is about 17 days right now, and that compares to normally even around 14 days. So we're not that far off right now where we normally would be.

A

So in terms of just our broader supply chain, we have great relationships with our suppliers. We, I think, have a very flexible supply chain. We've been strategic about which parts of the business we have included in our vertical model. But these are folks that specialize in different areas, and it makes sense for them to be in the business they're in enough to be in ours. But we work really closely together, and we have multiple factories across the country and around the globe. So, we feel good about our supply chain. It's not easy given the environment, but our teams are managing it every day.

Seth Basham

Analyst, Wedbush Securities, Inc.

Got it. Okay. And the other area of questions that I'd like to address is sales and marketing. And first on advertising, could you give any more data as to what your advertising leverage in the quarter year-over-year to help us understand some of the moving pieces?

Q

Shelly Radue Ibach

President, Chief Executive Officer & Director, Sleep Number Corp.

A

Yeah, we levered in – on specific media lines, Seth. We did lever on our 20% net sales and obviously substantially more when you look at the demand. This is an area we're going to continue to lean into with our strong value proposition. We're really excited about the unit growth and the ARU growth in the quarter, and an area of ongoing efficiency and effectiveness for us.

Seth Basham

Analyst, Wedbush Securities, Inc.

Q

Maybe asked in a different way, Shelly, did your media spending leverage more than the rest of sales and marketing?

Shelly Radue Ibach

President, Chief Executive Officer & Director, Sleep Number Corp.

A

Total sales and marketing was higher. Media leverage was a piece of it.

Seth Basham

Analyst, Wedbush Securities, Inc.

Q

Yeah. I'm just trying to get some color as to the key drivers there between media and your leverage on your labor force, but I guess we'll leave it at that.

David R. Callen

Executive Vice President & Chief Financial Officer, Sleep Number Corp.

A

Well, we've touched on this a little bit before, Seth, in the sense that we've – the digital capabilities that we've put in place during the pandemic have served us extremely well. We've got a number of different tools that we're now using, including workforce management throughout our sales for retail operations. That is proving to be extremely productive. And we'll continue to – that's part of how we are delivering the robust net operating profit margin expansion. And we look to – we're excited about where we are and where we're headed.

Shelly Radue Ibach

President, Chief Executive Officer & Director, Sleep Number Corp.

A

And the higher demand.

David R. Callen

Executive Vice President & Chief Financial Officer, Sleep Number Corp.

A

It all starts with demand with this model. No doubt.

Shelly Radue Ibach

President, Chief Executive Officer & Director, Sleep Number Corp.

A

[ph] The big source (48:05).

Seth Basham

Analyst, Wedbush Securities, Inc.

Q

Understood. Thank you very much. Appreciate it and best of luck.

David R. Callen

Executive Vice President & Chief Financial Officer, Sleep Number Corp.

A

Thanks very much, Seth.

Shelly Radue Ibach

President, Chief Executive Officer & Director, Sleep Number Corp.

A

Thank you.

Operator: And we have no further questions at this time. I'll now turn the call back over to the presenters for closing remarks.

Dave Schwantes

Vice President-Finance, Investor Relations & Decision Support, Sleep Number Corp.

Thank you for joining us today. We look forward to discussing our second quarter 2021 performance with you in July. Sleep well and dream big.

Operator: This concludes today's conference call. Thank you for joining. You may now disconnect.

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