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# Conference Call Transcript

## BRBY.L - H1 2010/2011 Burberry Group plc Trading Update Conference Call

### Event Date/Time: Apr 19, 2011 / 08:00AM GMT





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**John Guy**
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**Rogerio Fujimori**
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**Thomas Chauvet**
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**Louise Singlehurst**
*Morgan Stanley - Analyst*

**Vicki Lee**
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## PRESENTATION

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**Operator**

Good day, and welcome to the Burberry second half trading update conference call. Today's conference is being recorded. At this time, I would like to turn the conference over to your host today, to Miss. Stacey Cartwright, EVP, Chief Financial Officer. Please go ahead, madam.

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**Stacey Cartwright** - ***Burberry Group Plc - EVP and CFO***

Good morning, everybody. Welcome to Burberry's second half trading update call. With me this morning, I've got Fay Dodds, our Investor Relations Director. As usual, I'm going to provide a brief summary of our performance, and then we're going to be happy to take your questions.

So before I start, let me just comment on three of our markets; first of all Japan, where we continue to monitor the situation closely. Our first priority remains to support our staff, all of whom we're pleased to confirm are safe, and our team on the ground in Japan is staying very close to our partners there.

As background, remember there are two main channels for our business in Japan. The first is the non-apparel joint venture, where we directly operate two stores and 14 concessions, and here, the revenue from these accounts for less than 2% of group retail wholesale revenue.

The more important contribution is licensing, where Japan accounts for about two-thirds of the total group licensing revenue. Of this, two-thirds is apparel, the license with Sanyo Shokai and Mitsui, which runs to 2015; and one-third is non-apparel, where we have a number of different licenses on short-term contracts. Note that the apparel and non-apparel agreements have contractual minimum royalty payments, and as you will have seen from the statement this morning, our current assumption is that we will continue to receive these payments as originally planned.

Secondly, as regards China, following the acquisition of the former franchisees operation September last year, the business transferred from Wholesale to Retail. This impacts our second half numbers, and will also, of course, impact the first half of the new financial year until we anniversary the acquisition.

And finally, all my comments this morning will exclude the discontinued Spanish business. We have in the last quarter completed the transformation from selling the local domestic collection in Spain to now selling the full global collection, which is available in our main line stores and a number of limited number of wholesale accounts and retail concessions. And this business has now been fully integrated within our European regional team, and will report going forward as part of Europe. So of course, once we complete the announcement of our '10/'11 results in May, we'll no longer be disclosing Spain as a separate market.

So now turning to the numbers. We had a strong finish to the year leading to total underlying revenue growth in the second half of 30%. Within this, Retail sales increased by 42%, new space contributed 10%, China contributed 19% with the faster growth in the fourth quarter due to the final acquired stores transferring across, the benefit from the 10 stores we've opened during the year, and early wins from improving retail disciplines driving productivity gains.

Comp store sales growth in the acquired stores was around 30% for the half, obviously, not yet included in the Burberry comp number. And then comp store sales for the rest of the Group grew by 13%, with double-digit mainline growth in all regions for the half. Asia Pacific was consistently strong in both quarters, whilst Europe and the Americas did slow, although still delivered high single-digit mainline growth in the fourth quarter, up against the shift in Easter and the non-anniversarying of certain prior year promotional activities.

In Wholesale, revenue, excluding China, increased by 29%, again ahead of guidance, and this outperformance was thanks to our improved supply chain, logistics and systems capabilities, which meant we were able to respond to higher than anticipated in season orders, whilst also improving shipping, which led to higher overall fulfillment rates than in our planning assumptions. And finally, licensing, where underlying revenue declined by 5% in line with guidance.

In the second half, we've also made further progress on our five strategic themes. So under the first, leverage the franchise; in Retail, we're delighted with the performance of Prorsum and London, which although lower gross margin in percentage terms, demonstrates the progress we're making in elevating the brand through product innovation as well as marketing and digital initiatives.

In the fourth quarter, we began the rollout of our new global digital commerce platform, and we continued to introduce retail theatre technology to our stores.

Under the second of our themes, non-apparel growth, this is now 40% of sales, and highlights that the half in Retail included scarves, where there's been much product innovation, men's large leather goods and shoes.

Under the third theme, retail led growth, we've opened a net seven mainline stores around the world from Shenzhen to Sao Paulo; from New York to Milan. In under-penetrated markets, we continue to use the franchise model to enter new markets such as Israel, Egypt and Armenia, and we've agreed, subject to regulatory approval, to move five stores in Saudi Arabia from a franchise operation to a joint venture, in line with our strategy of taking greater control over the brand.

And then finally, under operational excellence, we could not have delivered the sales we have today, especially in replenishment, without the continuing improvements the team are making in supply chain, planning and systems.

And so in summary for the financial year just ended, we're looking for adjusted profit before tax to be around the top end of the range of market expectations, with our understanding of that range being GBP279 million to GBP300 million. As usual, we'll go through the full P&L details at our prelims in May once the year-end process has been completed.

We've also this morning released our normal guidance for the new financial year, including a 12% to 13% increase in average selling space in the year. In addition, the 50 acquired stores in China will add around a further 12% to space in the first half. We've got further strong growth in Wholesale; up by a mid-teens percentage excluding China, led by Americas, travel retail and emerging markets; and a mid-single digit increase in underlying licensing revenue, with the step-up in the Japanese apparel license minimums being offset by certain planned non-apparel terminations, and then double-digit growth expected from the global licenses of eyewear, watches and fragrances.

As Angela said in her quote this morning, the luxury industry as a whole does face some macro challenges; some since we last spoke in January, such as the consequences of the recent events in Japan, the political unrest in the Middle East and North Africa; and some ongoing such as raw material price increases, which will place pressure on gross margin, and tough comparatives as we anniversary some big comp sales growth numbers.

We've also talked in January about our what we call pay as you go approach. We're seeing operating leverage in our core business, and we're choosing to re-invest some of this either to grow the business or to cleanup legacy issues, while at the same time delivering steady progress in the Retail Wholesale operating margin.

In '11/'12, this reinvestment will include upgrading the quality of our real estate in flagship markets such as London, building our presence in new markets such as Latin America and India; and again, we'll talk to you about these in more detail in May.

Against this background we do, however, remain confident that our strategies will enable us to continue to outperform in the new financial year.

So with that, we'd now be pleased to take your questions.

## QUESTION AND ANSWER

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**Operator**

(Operator Instructions). Erwan Rambourg, HSBC.

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**Erwan Rambourg** *- HSBC - Analyst*

I had three questions, please; firstly on Japan. I understand you're securing the flows from your partner there, but can you tell us what you've seen following the catastrophe, both in terms of what your partner is seeing, but also in terms of what you're seeing in terms of the non-apparel business?

Second question is on China. You've seen 30% comps, which presumably means you haven't seen a lot of teething issues. Can you tell us how this 30% is built and how have you made progress versus the way China was dealt with previously? Is it mostly in terms of traffic generation; in terms of conversion; in terms of ASPs? What have you brought in the limited period of time?

And then thirdly, a point of detail on some of the tests you've put through in terms of Burberry Brit standalone stores; and also, I remember you had this idea of potentially expanding Japanese labels to places like Hong Kong or other areas in the South East Asia region. Can you give us an update on that, please?

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**Stacey Cartwright** *- Burberry Group Plc - EVP and CFO*

Okay right. Well, there's quite a lot in there Erwam, I'll go back to Japan first of all. I don't think there's anything different to call out in terms of what trading we've seen versus what you'll have heard from any of the other luxury players in the marketplace. Clearly, in the immediate aftermath of the devastation there, sales dropped very significantly and there's been some claw-back of that. And obviously, I'm just talking about our non-apparel operations there. We run 14 shop-in-shops and two standalone stores. But I don't think there's much more to say on that.

In terms of China and the 30% comps, clearly, there's underlying growth in the market, but we do believe we are significantly outperforming. And what's clearly helped to drive the growth, apart from clearly the reaction to the brand and all of the digital innovative marketing initiatives and the product innovation that's gone into that marketplace, it's also been about more discipline when it comes to inventory management in so far as we're making sure that replenishment product is reaching those stores. We're not running with as tight levels of inventory as our franchise partners was previously and, therefore, we're not walking sales as potentially was being done previously.

I will say we're only at the start of the improvements that we looked to place on the operations in the China market. We won't have SAP rolled out there, for example, until the autumn. Clearly, it takes a while to convert over, and we only acquired the business last autumn. And then as we said previously, you don't just flick a switch and turn on SAP; there's a good year or so of getting to learn the system and then anniversarying and using the comparative data to help to drive the business further. So we see good upside to come as we roll SAP into the marketplace.

And then, we'll also rolling out the Burberry sales and service training program into the stores as well, and that's only at the very early stages. And clearly, improving productivity, as we have done in the other markets through the sales and service sales training program, remains a lever to pull there.

In terms of the Brit tests, they are just that, other than there's the sort of -- almost a sort of pilot store in 444 Madison Avenue as a means of demonstrating to wholesale partners what the Burberry Brit concept should look like.

Apart from that, which did open over a year ago, all of the other stores that we've opened have been opened less than a year, we've got half a dozen in the US now, very much focusing on what we call our flagship cluster strategy. So for example, you've got three in New York; we've just opened one in Milan relatively recently; and, of course, we've opened up one in Covent Garden only last Thursday.

So that's a great opportunity. It's the largest of the Brit stores, and a great opportunity for you closer to home to go and see the Burberry Brit concept.

But they are only test stores at the moment. We're very pleased with how they're landing, but looking to refine the merchandising product assortment and before we decide what else to do with them.

And then I think the final question was around the Japanese labels. I think you're referring to the Blue and Black Label product. And again, just a pilot in terms of opening up two pilot stores in Hong Kong, the first of those outside of the Japanese marketplace, just to see how that lands.

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**Erwan Rambourg** - ***HSBC - Analyst***

Okay, just a quick follow-up, and thank you on Japan; I understand there's probably very poor visibility, but can you give us an idea of the type of run rate you've had since the stores have reopened, basically?

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**Fay Dodds** - ***Burberry Group Plc - Director of IR***

Erwan, if you look at our non-apparel joint venture, it's significantly less than 2% of our Retail Wholesale revenue, so I don't really think it's particularly relevant.

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**Erwan Rambourg** - ***HSBC - Analyst***

Or what your partner has seen maybe?

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**Fay Dodds** - ***Burberry Group Plc - Director of IR***

And again, I don't think we're going to comment, not on their trading. The best thing to do is look at the Japanese department store numbers as they come out, because that's historically been a pretty good guide to the way that our part of the market is trading now.

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**Erwan Rambourg** - ***HSBC - Analyst***

Okay, thank you very much. Thanks a lot.

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**Stacey Cartwright** - ***Burberry Group Plc - EVP and CFO***

Thanks, Erwan.

**Operator**

Katharine Wynne, Investec.

**Katharine Wynne** - ***Investec Bank (UK) Plc - Analyst***

I just wanted to ask about stock levels and working capital trends. Perhaps you can give us an idea of where you ended up year on year in terms of stock and what the working capital move broadly is looking like for the year just ended.

**Stacey Cartwright** - ***Burberry Group Plc - EVP and CFO***

Okay, now clearly, this only a trading update and we do like to keep something back for May when we do the full P&L account and balance sheet, but directionally, no change from what we said on inventory back in January that inventory would grow by a greater percentage in the sales because, clearly, you've got the acquired inventory with the acquisition of China stores.

You've then got what we talked about earlier, which is actually putting appropriate levels of inventory into the China stores so that we're not walking customers the way that potentially we were doing before. And then the third element is actually investing more in replenishment inventory than we have done previously. And that's what's helped to fuel both the like-for-like sales growth, plus this significant outperformance on Wholesale in the second half.

So, yes, inventory levels will be higher. We'll give you the details of that when we come back in May. And then in terms of the rest of working capital trends, very happy with the way that we've managed debtors, creditors, etc., so you'll see the output of that when we announce in May.

**Katharine Wynne** - ***Investec Bank (UK) Plc - Analyst***

Thank you.

**Stacey Cartwright** - ***Burberry Group Plc - EVP and CFO***

Thanks, Katharine.

**Operator**

Warwick Okines, Deutsche Bank Research.

**Warwick Okines** - ***Deutsche Bank Research - Analyst***

Just a question on the cost base, please, for the year ahead. You gave a couple of examples of investing in the future. I was just wondering if you could talk about whether there would be any costs of legacy cleanup in the P&L for the year ahead. And also, just what sort of underlying inflation rates we should be assuming for the year ahead.

Thank you.

**Stacey Cartwright** - ***Burberry Group Plc - EVP and CFO***

We've talked previously about what we call the pay as you go approach, which is where, yes, we do still have legacy cleanup, and we do still have investments to be made. And one of the examples there that we've hinted in the release today is the fact that as we upgrade our store presence in some of our flagship markets, there is the transitional impact of essentially turning off profitable stores whilst you're redeveloping or putting in place temporary operations to bridge you into the new flagship presence in the market.

But we're managing that internally in such a way as to still deliver across the year as a whole Retail Wholesale margin progression. So we talk about steady improvements there, and we manage the cost base accordingly, and we manage the gross margin expansion accordingly.

So I'm not going to talk more specifically than that at this stage, but that is the underlying premise is that we will fund what we need to fund from the underlying leverage and improvements that we make across the core business.

**Warwick Okines** *- Deutsche Bank Research - Analyst*

Okay, thank you. And just in terms of inflation rate for the underlying business, can you give us any steer on that?

**Stacey Cartwright** *- Burberry Group Plc - EVP and CFO*

Well, again, it's different by different areas. So, clearly, when it comes to wage inflation, the nature of our business with some of the creatives and the innovation that's going on in the business we have to pay accordingly. There is a war on talent out in the marketplace, so it's not as straightforward as saying, well, it's low single-digit wage inflation.

In certain markets, you're facing higher pressures when it comes to rent increases. And then when it comes to cost of sales and raw material price increases, again, what we've had historically is our supply chain team able to deliver bottom line benefits to gross margin. A lot of their efforts now are turned more to mitigating the impact of raw material price increases and ensuring that we're not being hit by that.

**Warwick Okines** *- Deutsche Bank Research - Analyst*

Great, thanks very much.

**Operator**

John Guy, RBS.

**John Guy** *- RBS - Analyst*

Just a couple of questions from me on -- first of all on the ASPs. I know you flagged that you'd seen average selling prices increase. Just wondering what the increase was during the fourth quarter over the third quarter; if you could --

**Stacey Cartwright** *- Burberry Group Plc - EVP and CFO*

Yes, fair to say that ASPs was the biggest contributor to our like-for-like sales growth, so I don't think we talked specifically about the numbers. But it was the biggest contributor, and that is not down to us raising prices per se, that's about the mix shift. We talked about the move towards Prorsum in London; we talked about greater emphasis on outerwear; and where we are moving prices, we tend to do it in a way that is from a consumer's point of view, they see the price value tradeoff so that we're adding -- whether it's leather trim to a handbag, or whatever, there's some element of innovation or embellishment that enables you to go to the next price point.

**John Guy** *- RBS - Analyst*

Okay, great. And with regards to space allocation from -- or to apparel versus non-apparel on some of the new stores that you're opening, is it fair to say that if you were looking at a broad split between the two that 60% is now, or at least 60% is now being driven towards the non-apparel over apparel? Is that a far assumption to make, do you think?

**Stacey Cartwright** *- Burberry Group Plc - EVP and CFO*

It depends on the store, to be honest, and the different markets that we're in. It is store by store, because it's also if you've got a two-storey new store coming on board, it may well be that you're going to allow most of the ground floor to be non-apparel. It really depends on the configuration of the store. Clearly, you start with the premise of where's the non-apparel going to go, but it's not quite as scientific as it's 60/40.

**John Guy** *- RBS - Analyst*

Okay, so if you were looking at a split store over a store on one floor, are you able to give us an indication of where those percentages are?

**Stacey Cartwright** *- Burberry Group Plc - EVP and CFO*

Well, again, it depends on the marketplace. It's not pushed out in that way from corporate. You're taking note of the local intelligence in terms of what the right product mix will be for that particular market; you're talking note of what the rest of the flagship assortment looks like in that marketplace; whether this is something that -- we've got a big flagship already in that market so, therefore, maybe you want to emphasize this product category over that product category. You've got consideration as to what the other big wholesale accounts in the area look like. So again, it's what's right for the marketplace.

**John Guy** *- RBS - Analyst*

Okay, great. And just finally on your comments around raw material pressure. I wouldn't imagine -- I obviously appreciate that raw material prices are going up, but relative to where the mix is moving, surely that's more than offsetting some of the raw material pressures that the market in general is seeing.

**Stacey Cartwright** *- Burberry Group Plc - EVP and CFO*

Well, remember, in terms of the mix shift, that's actually depressing or putting pressure on gross margin, because -- just because you're moving up into higher price points, doesn't mean that you're delivering higher gross margin. Perversely, Prorsum is the halo of the brand, it's incredibly important and it's profitable, but it's the lowest gross margin. So the more you turn up the pyramid, actually, the more pressure you're putting on gross margin; so that tradeoff doesn't quite work.

**Fay Dodds** *- Burberry Group Plc - Director of IR*

And you'll remember also that we said that the differential between non-apparel and apparel is much smaller for us than other luxury peers, because our gross margin on some of our apparel lines, like outerwear, is relatively high.

**John Guy** *- RBS - Analyst*

That's great. Thanks very much indeed.

**Stacey Cartwright** *- Burberry Group Plc - EVP and CFO*

Okay. Thanks, John.

**Operator**

Fraser Ramzan, Nomura.

**Fraser Ramzan** *- Nomura - Analyst*

Just one on operating costs. I was thinking about the second half performance. Certainly, relative to what I was looking for, there was about a GBP50 million additional sales benefit, so that was great, but profit-wise, there was only about a GBP15 million drop-through from that. And I think my question really is, as you drive replenishment, what does that to your variable cost? Presumably, to get back in stock, there's an impact on variable costs within the business and, therefore, we should presumably looking forward expect limited downward progress in the cost of sales ratio.

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**Stacey Cartwright** - ***Burberry Group Plc - EVP and CFO***

Okay, first thing just to pick up on, your numbers there are exactly that, Fraser; they're your numbers in terms of GBP50 million trading through to GBP15 million. From our numbers, we had a much higher flow-through. We didn't have a GBP50 million uplift on revenue. So that's the first thing to say. Replenishment is a very strong positive contributor to overall margin expansion. So again, it's one of the mitigants as we look at the various pressures on gross margin as we move into the new year, whether it's the higher mix on Prorsum London, whether it's raw material price pressures. Actually, the more we do on replenishment, the more good news that is in terms of offsetting some of those core pressures.

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**Fraser Ramzan** - ***Nomura - Analyst***

Okay. But you do have, clearly, some upward variable costs related to strong sales performance as a business?

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**Stacey Cartwright** - ***Burberry Group Plc - EVP and CFO***

Yes, but those are -- you've got the variable costs in terms of credit card commissions, turnover rents, things like that; not [that] significant otherwise.

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**Fraser Ramzan** - ***Nomura - Analyst***

Okay, great. Thank you very much.

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**Stacey Cartwright** - ***Burberry Group Plc - EVP and CFO***

Okay. Thanks, Fraser.

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**Operator**

Rogerio Fujimori, Credit Suisse.

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**Rogerio Fujimori** - ***Credit Suisse - Analyst***

I have two questions on China. I think first you flagged last year you'd be working on product assortment, increasing menswear, children's wear, etc., so would it be correct to assume most of these changes will be done in fiscal '12?

That's my first question.

Second one is on your GBP20 million incremental profit guidance for next year. It's primarily the pickup for Retail margin, right? So is it correct to assume your base plan is to have the upside from improving stock productivity to be reinvested into the business? So if you could give an update on your thinking after six months ownership that would be great.

Then the third question is just some color on how traffic levels in mainland China compare to your 13 stores in Hong Kong.

Thank you.

**Stacey Cartwright** - ***Burberry Group Plc - EVP and CFO***

Okay, well, first of all, just to pick up on directionally drive to increase menswear and children's wear in China, that remains part of the strategy. It's not a case of it will be completed in '11/'12; that's part of the ongoing strategies.

I'm not sure I got the second question. I don't -- Fay, did you?

**Fay Dodds** - ***Burberry Group Plc - Director of IR***

I think, Rogerio, was the question about whether there's any upside to the GBP20 million guidance we gave?

**Rogerio Fujimori** - ***Credit Suisse - Analyst***

Yes, given your -- basically, the trend you have seen in terms of improving stock productivity and replenishment in this first six months.

**Fay Dodds** - ***Burberry Group Plc - Director of IR***

Yes. Clearly, we have made strides arguably faster than you might have expected, so the base line is stronger in China. So, yes, the potential to add a little bit more than the GBP20 million than we said for the first full year.

And I think the last question was around traffic levels versus Hong Kong. Well, I will tell you the Hong Kong stores remain the most productive that we have in the world. So China's still got a little bit of catching up to do.

**Rogerio Fujimori** - ***Credit Suisse - Analyst***

Thank you very much.

**Operator**

Thomas Chauvet, Citigroup.

**Thomas Chauvet** - ***Citigroup - Analyst***

Stacey, I saw your comment to Reuters earlier that Retail sales in Europe continue to be strong, I guess driven by tourists, but not wholesale sales. What's happening there, and which wholesale markets in particular are you referring to?

That's my first question.

Secondly, can you perhaps help us model Spain? What was the absolute turnover of the global collection in the second half? How many doors are you present now? How much contribution going forward do you expect from Wholesale and Retail? I understand it will be mostly Wholesale.

And finally, what's currently the average differential roughly in retail price between China, Hong Kong, US and Continental Europe? And in China, how does the product mix compares with the rest of the Group between apparel and non-apparel for FY'11?

**Stacey Cartwright** - ***Burberry Group Plc - EVP and CFO***

Okay, well, there's quite a lot in there, so I'll start off and let Fay see if she remembered what the last questions were.

I think the first one was on European Wholesale, what's happening there. This is simply what we flagged in terms of the legacy cleanup in the European market in terms of the number of small accounts that we've traditionally sold to across Europe in some of the secondary tertiary, I would say cities, but in some cases just towns, where to be honest, we haven't got the right brand image in terms of the right adjacencies; we haven't got the right scale, and we've been continually working with many, many of these smaller accounts to either get them to the appropriate level, or to agree that we won't be selling them going forward.

So that remains part of the strategy, and you see that coming through into the numbers when we talk about Retail continuing to perform very nicely in Europe.

When you see the total numbers for Europe, you have to bear in mind that there is this cleanup on a lot of the legacy wholesale accounts that continues to go on.

The Spain global collection, to be honest, it's small millions of pounds, Thomas. That's why we're not even going to talk about Spain going forward. We don't talk about what the French or the German individual sales numbers are, and Spain is essentially no bigger than those markets going forward. We've limited the distribution now to less than 100 wholesale accounts, and we're in --

**Fay Dodds** *- Burberry Group Plc - Director of IR*

With 20 concessions across the mainland, of course.

**Stacey Cartwright** *- Burberry Group Plc - EVP and CFO*

Yes, exactly; 20 odd Corte Ingles doors, and that's it. So it's a small market for us now appropriate with the scale of luxury in that market; so none of our peers operate on a larger scale than we do either.

Then I think the next question was around retail price differences across the different markets. Because you have freight and duties and taxes, etc., typically, you see China at about 140 to UK being at 100. Hong Kong tends to be 120-130; and I can't remember what other market -- yes, the US tends to be a little higher than the UK. That is entirely consistent with the global luxury peers.

It's partially driven out of -- as I said, the pricing architecture is driven out of the fact that you do have different taxes and operating costs in the different regions, and that's how historically that's all been built up. And we keep a careful eye on what our luxury peers are doing and make sure that our pricing architecture is consistent across the board.

**Thomas Chauvet** *- Citigroup - Analyst*

Okay.

**Fay Dodds** *- Burberry Group Plc - Director of IR*

Yes, I think the final question was on China product mix, and there's a very, very slight -- non-apparel is very slightly at a higher degree of sales, but nothing really to write home about.

**Thomas Chauvet** *- Citigroup - Analyst*

Okay, thank you. Thank you very much.

**Operator**

Louise Singlehurst, Morgan Stanley.

**Louise Singlehurst** *- Morgan Stanley - Analyst*

Just a couple of quick ones on Wholesale. Given, obviously, a much stronger beat than what we thought in Wholesale for the period, can you just talk about the attitude and the tone of the wholesalers?

And when you talk a lot more about the in-season reorders, how fast are you actually accepting orders and time to delivery now, and compare that versus where you were 12 months or 24 months ago?

Thanks.

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**Stacey Cartwright** *- Burberry Group Plc - EVP and CFO*

Okay. Well, attitude and tone of the Wholesale customers have been very positive. I think we continue to outperform and, therefore, Burberry is a very successful brand for them to be carrying, if I'm just going to generic about it.

In terms of time to delivery, we -- now that we have replenishment product in the DCs, we can turn this round 24 hours/48 hours and get the product out to the consumer. We might have been able to deliver in that timescale previously, but chances are we wouldn't have actually have had the product. So it's less about the processing time out of the DC, it's about the fact that it wasn't there in the DC to start with.

So I think we've got a lot stronger in the way in which we're managing the core replenishment offering and flowing that product into the DC to make sure that it's there and can be pulled on for Wholesale and Retail alike.

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**Louise Singlehurst** *- Morgan Stanley - Analyst*

Great, and just as a quick follow-up, color by geography. Obviously, Germany stands out as a bit of a surprise, being one of your key strengths in the quarter. Any other color for Europe particularly?

Thank you.

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**Stacey Cartwright** *- Burberry Group Plc - EVP and CFO*

I don't think so. The other markets in Europe seem to be doing fine as well; probably stronger Northern Europe than Southern Europe. So traditionally, we called out Italy as one of the stronger markets. That's probably the laggard now in Europe. But that's the beauty of the global brand and the way in which we run the regions is that there's always one or two markets that are picking up the mantle if other ones go a little softer, just because they've got strong comps that they're up against.

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**Fay Dodds** *- Burberry Group Plc - Director of IR*

And I think, Louise, as Stacey said her script, the fourth quarter is quite difficult to read, because we're not anniversarying the promotional activity that we did in January, and then Easter's gone missing as well, which is important to the US and Europe.

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**Louise Singlehurst** *- Morgan Stanley - Analyst*

Very clear, thank you.

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**Operator**

(Operator Instructions). John Guy, RBS.

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**John Guy** *- RBS - Analyst*

Just a quick follow-up on SAP and the back-end side of the business. You said a while ago that you were roughly around about 6 out of 10, and I was just wondering, obviously, with China rolling forward and SAP going in in autumn, where you think you'll be by the end of the first half of next year. Will you be closer to an 8 out of 10, or were you sort of trundling along at a percentage point a year.

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**Stacey Cartwright** - ***Burberry Group Plc - EVP and CFO***

Yes, you need to separate the two aspects. One is the actual operational roll-out of SAP, which we are -- essentially, we were pretty much through until we then acquired China. So you've got China and some of the emerging markets still to go there; and then, essentially, we're almost 100% of the way through. But that's not the same as then leveraging the benefits out of it.

As I've said many times before, you have to have the system in, you have to anniversary it for a year, you have to get everybody learning how to use it properly, and then you start to see the benefits come through.

So we talked about being 6 out of 10 from an actual operational point of view, rather than an actually rolling out the system's point of view. And I think we continue to make progress. I don't think it's as easy as saying, well, I'm going to be 7 out of 10 by this stage, or 8 out of 10 by that date; we continue to make nice, steady progress. And everything we've delivered in this second half pays testament to the fact that the systems and the operational improvements mean that we can respond when demand is there and our Wholesale sales, instead of being high teens being 29% growth, is testament to that.

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**John Guy** - ***RBS - Analyst***

And, Stacey, do you think that that was reflected in your comment then when you were at 6 out of 10, or is this a direct result of an improvement from that 6 out of 10.

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**Stacey Cartwright** - ***Burberry Group Plc - EVP and CFO***

I think it's all part of the journey that we're on. Maybe we say we're now 7 out of 10, I don't know; but we're somewhere in the range between the two.

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**John Guy** - ***RBS - Analyst***

Okay, so 6.5 then. (Laughter).

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**Stacey Cartwright** - ***Burberry Group Plc - EVP and CFO***

Not that this is scientific, John; but, yes.

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**John Guy** - ***RBS - Analyst***

Thanks very much.

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**Operator**

Vicki Lee, Barclays Capital.

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**Vicki Lee** - ***Barclays Capital - Analyst***

Couple of questions on China, again. Just in terms of space growth, you've given the guidance of around 50 new stores over the medium term. Just again, as we get a little bit deeper into that market, how are you feeling around that potential in terms of the space opportunity, and particularly around the square footage that those new stores would have, compared with the existing 50?

And then just secondly on the phasing of the costs and how we think about that there; obviously, I'm expecting a sharp increase in China in terms of that investment piece in the next year or so, but just how to think around that investment piece over the medium term; and over and above particularly what's going to have to be associated with store increases.

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**Stacey Cartwright** *- Burberry Group Plc - EVP and CFO*

Okay, so China, space. Just to reiterate that we haven't moved off the fact that we talk about 100 stores in China in the medium term. If the stores that we acquired were on average about 2,000 square feet, it's fair to say that these will probably be heading towards more like twice that sort of size on average as we move through the portfolio. But of course, within that, you've got a range of smaller stores plus the big flagship Beijing store, for example, that we had the big store opening for just last week. But, yes, they will be larger stores than those that we've traditionally -- or that we've acquired historically.

I'm not sure I followed the second question, so I'm going to throw that one to Fay. (Laughter).

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**Fay Dodds** *- Burberry Group Plc - Director of IR*

Oh, thank you very much. I think in terms of the phasing, of course, every year, we'll give you guidance on how many stores we're looking to open as a total and how many of those are in China. And I don't think there's anything we would call out particularly that as we move to opening in China I don't think it particularly impacts our costs over and above what you'd see elsewhere around the world.

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**Vicki Lee** *- Barclays Capital - Analyst*

Okay, thank you very much.

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**Operator**

Fraser Ramzan, Nomura.

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**Fraser Ramzan** *- Nomura - Analyst*

I just wanted to come back to you on the space contribution from the new stores ex China in the second half. Obviously, those stores were very productive. Is there anything in particular to highlight there; any reasons why we might continue to expect those kinds of levels of productivity going forward on new space?

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**Stacey Cartwright** *- Burberry Group Plc - EVP and CFO*

No, we always talk about how there isn't a direct correlation between the sales growth and the space growth; it's directional. So 10% space growth may contribute 8% sales, or 11% or 12% sales, but it will be in that sort of range.

Clearly, as you open more stores in higher productivity markets like Asia, I would say you're more likely to be at the top end of that range than the bottom end. But I don't think you can take the second half as something you can then extrapolate forward, because we're expanding stores across all the geographical markets, as we said.

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**Fraser Ramzan** *- Nomura - Analyst*

And generically speaking, from the trials you've done so far, are the Brit stores very productive?

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**Stacey Cartwright** *- Burberry Group Plc - EVP and CFO*

They're not more productive than the more conventional stores in that local marketplace; so they're very nice and they're contributing in line with what we're seeing from all of the other stores.

**Fraser Ramzan** *- Nomura - Analyst*

Okay, that's great. Thanks very much.

**Stacey Cartwright** *- Burberry Group Plc - EVP and CFO*

Right; thanks, Fraser.

**Operator**

Warwick Okines, Deutsche Bank.

**Warwick Okines** *- Deutsche Bank Research - Analyst*

I just wanted to ask the traditional question on the balance sheet actually, because it's not been asked yet. Stacey, what market conditions or balance sheet metrics would you need to see in order to reinitiate your share buyback program, or indeed raise your payout ratio from 40%?

**Stacey Cartwright** *- Burberry Group Plc - EVP and CFO*

Yes, it's a good question, Warwick. I think no change from our previous position that this is something that the Board keeps under regular review. I think the Board is quite happy with the 40% dividend payout ratio. We think that's entirely appropriate. It provides the right balance then for what we can reinvest back into the business, and you've seen us increasing the level of capital expenditure in the last year or so, and we'll continue to do that in terms of organic investment.

In terms of whether it's appropriate to embark on any share buyback program, that's really a matter for the Board; and when we've got something to say on that, we will.

**Warwick Okines** *- Deutsche Bank Research - Analyst*

Okay, thanks very much.

**Operator**

As there are no further questions on today's queue, that will now conclude today's question and answer session. I'd now like to turn the call back over to your host today, to Miss Stacey Cartwright, for any additional or closing remarks.

**Stacey Cartwright** *- Burberry Group Plc - EVP and CFO*

So in conclusion, Burberry had a strong finish to the year. We're looking forward with confidence to the new financial year, albeit mindful of the global macro challenges that the luxury industry faces.

We thank you very much for your attention. We're looking forward to speaking with you again on May 26, which is when we publish our preliminary results.

Thanks very much.