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PRESENTATION

Angela Ahrendts - *Burberry Group plc - CEO*

Good Morning. Welcome to Burberry's results presentation for the six months to September 30, 2012. Today, Stacey and I will review key developments in the first half.

And then, with Matt McEvoy, our Senior Vice President of Strategy and New Business Development, we'll talk about our new division, fragrance and beauty. As we directly operate this business, it will enable us to capitalize on exciting opportunities we have in these underpenetrated categories, and how we plan to accelerate this growth significantly over time.

But let me, first, turn to our first-half achievements. In challenging markets, revenue grew by 6%; adjusted PBT grew 7%.

We saw operating leverage in retail/wholesale, with revenue up 7% and adjusted operating profit up 11%, driven by higher quality sales, and tight expense control.

Cash generation was strong, and we increased the interim dividend by 14%.

Our five key strategies remain as relevant today as ever. The portfolio is balanced by channel, region, product, and a team focused on consistent execution.

Despite a slowdown in traffic during the first half, we are staying in our lane; continuing to invest in high growth flagship in emerging markets, and high potential product categories.

We're evolving our capabilities, front and back of house, to drive greater efficiency, while correcting legacy issues.

And brand momentum remains strong. We were the fastest-growing luxury brand in this year's inter-brand survey of the top 100 global brand value.

We continue to gain recognition for our digital innovation, be it Altagamma or L2, who last month again named Burberry as the fashion brand with the highest digital IQ.

We continue to connect customers globally with the brand with rich compelling content across all of our platforms; from burberry.com to social media, where Burberry remains the leading luxury brand on Twitter, Chinese social media, and Facebook with now over 14 million fans.

Turning to revenue, in common with many of our peers, we're being impacted by the well-documented slowdown in the luxury sector, which for us is broad-based across regions and product divisions.

Total revenue for the half increased by 6% at reported FX, and 8% at constant FX. Both wholesale and licensing were consistent with our previous guidance, and we delivered 10% underlying retail growth against record prior year comparatives. This marks the 14th consecutive six-month period of double-digit retail growth.

And in retail, comparable store sales in the half increased by 3%, with 6% growth in Q1 and 1% in Q2. Footfall was the primary driver of this deceleration, but was offset by an increased average transaction value, so higher quality sales growth.

In the first half, there were some modest like for like price increases, in line with previous seasons, and always benchmarked against our peers. And the mix continued to drive average selling prices, with Prorsum and London up 5 percentage points.

Brit, which only a few years ago was about 75% of our revenue, is now more balanced in the portfolio at about 55% of mainline apparel retail sales in the first half. It is more dependent on key items, such as jersey and denim, so the business naturally performs more in line with footfall.

A key highlight of the first half was the opening of 121 Regent Street here in London. With 27,000 square feet of selling space, it is our largest brand environment in the world, and the most digitally advanced.

Customers can experience every facet of our brand through immersive, multi-media content, exactly as they do online. Walking through the doors is like walking into Burberry World, our website. We call Regent Street Burberry World Live because it blurs the lines between physical and digital.

And we're delighted with its early performance. To drive global reach, awareness and footfall, there are over 350 editorials covering the opening, the design, the aesthetics, and the technology.

Regent Street, it's an iconic beacon for our great brand, and it aligns our physical presence here in London, our home market, with burberry.com; our global digital brand perception.

Having recently retested all store projects against our 25% IRR hurdle, our capital expenditure plans for the full year will remain unchanged at GBP180 million to GBP200 million. About half of the spend is directed to flagship markets, with high demographic, local populations, and a strong influx from global tourism.

The pipeline in the second half is as strong as ever, with openings in Chicago this week; Shanghai; and the first ever menswear standalone store, which opened last month in Knightsbridge, here in London.

Turning to wholesale, where revenue increased by 5% underlying, as guided, wholesale is often a lagging indicator, and our customers worldwide are taking a more cautious view for the second half of the year. But our focus remains on the quality of sales.

During the year, we are continuing to correct legacy businesses in this channel, whether it's our positioning in the US, or small European specialty accounts, or rationalizing opening price point products in core accessories and outerwear.

And we're seeing good growth in targeted areas, including US department stores, where we added another 10 dedicated shop-in-shops during the half; Asia Travel Retail, where we're working dynamically with key partners to respond to the changing tourist footfall and spending patterns; and emerging markets, which was helped by five new franchise store openings in the half.

Finally, licensing, where underlying revenue was down 5%, this is consistent with our full-year guidance.

We continued to rationalize non-apparel licenses in Japan, at the cost of about GBP3 million in the first half, and we're celebrating our preparation for the transition to the global collection when the apparel license there expires in June 2015. And we expect to start to share our thoughts with you on Japan from early 2014.

Our global product licenses delivered solid growth, helped by inventory build ahead of the launch of the Britain Watch in early October. This launch illustrates again how we align all of our resources to create maximum impact for the brand and the business.

The Britain is our first collection of high end watches celebrating our craftsmanship and design values. Global press days resulted in a great reception for the collection, while launch events in the US, UK, and Asia drove reach and awareness across all media touch points.

The launch was supported by innovative digital experiences on both Burberry.com, and on mobile, including personalization of user's local time; location; weather; and a scale to scale interactive 3D model that offered customers a try-before-you-buy option.

Initial sales are very strong, and the consumers responding to the iconic design and our luxury positioning, specifically in Asia, which represents half of The Britain's sales since launch. This compares to about one-third of all watch sales historically.

Our business also remains very balanced by region, as you can see from this slide. Within Asia Pacific, which is our largest region, the performance of Hong Kong was relatively robust, if somewhat uneven during the first half. New stores in Russell Street and Pacific Place further elevate our brand presence in this high productivity flagship market.

Christopher and I were just in Hong Kong last week, where we shared the excitement of the launch event and met with key partners; real estate developers; our highly talented team; and our new fragrance distributors.

Mainland China delivered mid-teen underlying sales growth in the first half, albeit slowing in the second quarter.

The footfall data we have in China is somewhat limited, but internal consensus is the traffic was lower, affecting all product divisions, but offset again by more purchases at higher transaction values.

We continue to strategically invest in Mainland China, evolving the store portfolio and improving our retail disciplines, as we believe reports stating that this is still one of the high potential markets over the long term. This stimulates demand for luxury goods at home, China is forecasted to become the second largest luxury market behind the US by 2017; and abroad, as outbound travelers from China are forecasted to increase from 70 million in 2011 to over 100 million in 2015.

Turning to Europe, which represents -- which is 33% of our revenue, the retail performance was mixed during the half. Northern Europe, i.e., France and Germany, outperformed; and Southern Europe, mainly Italy, underperformed. The UK, which is nearly 40% of our Europe retail, slowed during the second quarter, reflecting, in part, the Olympic disruption.

The Americas grew by 5%, with wholesale outperforming retail. With about 80% of our retail sales to domestic customers, comp growth in the half was broadly unchanged against strong prior year comparatives there.

Real estate expansion in the Americas is focused in Brazil and Mexico. And in the US, we have a magnificent new flagship on Michigan Avenue, in Chicago. It just reopened last week and, based on everything I've seen today, the timing was perfect.

Finally, in the Rest of World we saw 14% growth, balanced between retail and wholesale.

Our business is also well balanced by product division, as you can see from the slide here. Our merchants also build very balanced assortment by label, within categories such as outerwear, by diversifying lengths and fits; and by price point, always focusing on price value; and constantly introducing new fashion styles, while retiring slower trending replenishment styles.

So the shape of the business remains consistent with accessories as our largest product division at 39% of revenue, underpinned by large leather goods, with outwear at around half of apparel, and replenishment styles around half of mainline revenue.

Our growth initiatives are working, be it men's tailoring, which more than doubled in the half in retail, and men's accessories, which are up over 40%.

We continue to execute our monthly floor sets more efficiently, and today sees the launch of our festive offer across all digital and physical channels worldwide.

With less predictable traffic, we've been intensely focused on preparing for the all-important festive season. We've been fast-tracking key best selling styles; obsessing over visual merchandising on and off line; creating a new gifting experience on Burberry.com; and optimizing our marketing capabilities to drive awareness and conversion across all mediums.

Before I hand over to Stacey, let me show you a short video that highlights the key achievements of the team in the first half.

(video playing)

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

Good morning, everyone. I'm going to review the first-half profit and cash performance with you, before then briefly covering some of the financials around fragrance and beauty.

In the first half, against challenging markets, revenue grew 6%; adjusted profit before tax grew 7%; and cash position strengthened, even after nearly GBP90 million of capital investment; and we've increased the interim dividend by 14%, as we continue to rebalance the pay out between halves.

Adjusted operating profit increased by 7%, including a small translation benefit.

We delivered operating leverage in retail/wholesale with revenue up 7%, and adjusted operating profit up 11%; leading to a 60 basis point improvement in operating margin to 15.5%.

We'd originally guided first-half margins being lower than last year, but the sales slowdown experienced during the second quarter, offset by better quality of sales in that period, and tight expense control, all contributed to the margin improvement.

Our goal for the full year, albeit ahead of the all-important third quarter, remains to deliver a modest improvement in operating margin, just as we have done in each of the last three years.

Our retail/wholesale gross margin increased by 250 basis points to reach 69.2%; in line with the second half of last year. We benefited from modest price increases in all regions, FX gains on sourcing, along with a small assist from the continued mix shift to retail.

Operating expenses increased by 11%, or GBP44 million. There was a GBP15 million saving from lower accruals for performance-related payments.

So of the gross increase of GBP59 million, around half was related to new retail space, which increased by 12% in the period, with the strong pipeline of larger format store openings this year we had higher pre-opening costs than normal; and about one-third of the increase was general inflation across the business; with the balance being investment in areas such as customer resources, creative media at the front end, and IT infrastructure and logistics at the back of house.

In light of slowing demand in the luxury sector, we're also tightly controlling spend in areas such as headcount, travel, and other expenses, strictly prioritizing discretionary business projects, and while marketing has been held at a steady percentage of sales in the first half.

We will continue to dynamically manage both gross margin and operating expenses to drive the further modest improvement in full-year retail/wholesale operating margin.

Turning now to licensing, with revenue down 5% underlying and expenses held at GBP7.9 million, operating profit was GBP44.7 million; that's an 85% margin.

And now to the income statement. The net finance charge was GBP0.2 million. Here, facility fees offset the low interest rate received on our net cash balances. For the full year, we're expecting a similar number.

The exceptional charge of GBP61.5 million is really two main items; firstly, a charge of GBP73.8 million relating to fragrance and beauty, which I will come onto explain later; and a credit of GBP11.7 million relating to the China put option liability valuation, compared to a charge of GBP2.9 million last year.

Certain assumptions used in the valuation have changed to reflect lower growth expectations for the Chinese luxury goods sector. Note that this is, of course, non-cash.

Finally, the effective rate of tax for the year is estimated at 25%, which is the rate applied to the adjusted PBT in the first half, and compares to 26.5% last year.

Cash generation remains strong, with net cash at September 30, of GBP237 million; that's up 36% compared to a year ago.

Depreciation was GBP49 million, and remains on track for the full year at around GBP110 million.

The seasonal working capital outflow was GBP96 million, and that's a slight improvement on last year.

Payables decreased, partly because of lower performance incentive accruals, while the inventory outflow more than halved.

Our inventory is in great shape, despite the second quarter slowdown in retail sales. At GBP353 million on the balance sheet, inventory grew by just 4% compared to September last year. That's less than half the rate of retail sales growth, and well below the 12% space growth.

Facilitated by the investment in planning and IT, we procured significantly less for the season, specifically to drive better working capital efficiency. And, as well as less inventory, the quality was much improved, with a significantly less aged inventory, and a higher proportion held in replenishment and current season styles.

From the GBP138 million operating cash flow, we invested GBP89 million in our stores and infrastructure. As Angela said, having re-tested new store projects against our 25% IRR hurdle, with potentially lower sales projections, capital expenditure remains at GBP180 million to GBP200 million for the year.

Tax paid was broadly unchanged at GBP47 million.

Dividends grew by GBP10 million to GBP79 million, while the ESOP trust purchases total GBP28 million, and our cash position remains healthy.

The Board does continue to regularly review the balance sheet strategy of the Group, and remains of the view that a prudent balance sheet remains appropriate in this challenging external environment, and gives us flexibility to invest in growth initiatives over time.

The slide in your packs summarizes our current guidance, but I would just like to reiterate that our financial position is strong. Our goal for the full year remains to deliver a modest improvement in retail/wholesale operating margin, balancing expense control against investing for growth.

Before I hand over to Angela and Matt to discuss the strategic rationale and opportunities in fragrance and beauty, let me comment, first, on the financial aspects of the transaction.

As you know, the license with Interparfums ran until December 31, 2017. But under the terms of the agreement, Burberry was entitled to exit on December 31, 2012, at a cost of EUR181 million. We have exercised that option, and will pay Interparfums that sum on that date.

We've extended the license relationship for a three-month transition period up to March 31, 2013, and we'll begin operating the beauty division on our own account, therefore, from April 1, next year.

So, clearly, we're very excited about the opportunities that this new beauty division offers us over the long term. It will be a very important new growth platform.

However, under accounting rules, as we've technically terminated a license relationship, the transaction is treated very differently to an acquisition. We're required to expense the full EUR181 million, or GBP142 million, through the income statement by December 31, 2017, when the original license expired.

Applying the accounting rules means that half of the payment, that's GBP71 million, is recorded as an intangible asset, which will be amortized on a straight line basis from the period April 1, next year until December 31, 2017; resulting in an expected annual charge of GBP15 million. And this charge will be treated as an exceptional item, and of course is non-cash. Whilst the balance has been expensed in the first half as an exceptional item, along with GBP2.5 million of related costs, giving a total first-half charge of GBP74 million.

When concluding how much to capitalize, accounting rules require us to estimate only the incremental income earned by the Group from the fragrance and beauty business over that period, from April 1, next year to December 31, 2017. In this calculation, no account is taken of any halo of integration benefits to our existing core business from having the business in-house from April next year, or the financial benefits beyond 2017, both of which, we believe, are significant.

Looking at the near-term financial impact, let me provide you with some building blocks for your models. As we don't start operating until April 1, next year, the effect on adjusted PBT will be immaterial in the current financial year.

The only impact will be the exceptional items being, firstly, the GBP74 million charge in the first half that I've just described; plus the setup costs in the second half that we expect to total between GBP5 million and GBP10 million. This is largely in respect of recruitment, new headcount to run the new beauty division, and certain marketing costs that will no longer be borne by Interparfums.

Looking forward, the financial year to March 31, 2014, will be a transition year for this business, reflecting Interparfums' selloff period, which will reduce Burberry's first-half revenue '13/'14, as well as reducing off-price or inappropriate distribution upfront/ rather than creating another legacy issue.

At this stage, we're expecting to recognize approximately GBP140 million of wholesale revenue for '13/'14, contributing to around GBP25 million of retail/wholesale operating profit, which will weighted towards the second half.

Licensing revenue will be reduced by approximately GBP25 million in the year in respect of the fragrance contribution.

The overall impact on adjusted PBT and earnings will be broadly neutral for '13/'14, as there's only minimal financing income foregone. But beyond this transition year, the transaction will, of course, add to adjusted earnings.

We anticipate that the business will require normalized net working capital of around GBP50 million in the first full year.

We're at the start of an exciting journey, and we will share more as we integrate.

Now let me turn over to Angela, who will outline the rationale and the opportunity.

Angela Ahrendts - *Burberry Group plc - CEO*

At the results presentation in May, we discussed our record of execution against our five core strategies. Under leverage the franchise, we highlighted the opportunity to unlock the potential in our licensed businesses, and in particular fragrance and beauty. We can now look forward to directly operating this business from April 1, next year, adding a new growth platform to the Company.

I'll briefly discuss the opportunity, and then Matt will outline the strategy. But, first, a little background.

The structure of the agreement with Interparfums provided Burberry with a one-time opportunity to exit the existing license early and bring fragrance and beauty in-house. Otherwise, we would have had to wait until 2018.

Interparfums has been a great partner for the last 20 years but, as you know, Burberry's evolved over the past few years and we're looking forward to the future.

We view fragrance and beauty in the context of our leading global brand stature, and that frames our objectives for this business. Given its current size and potential, we believe that now is the appropriate time to undertake the transition, and we're extremely excited about it.

Integration offers a number of benefits. First, fragrance is the most widely encountered projection of the brand. It's Burberry's opening price point, sold through over 20,000 points of sale worldwide. Fragrance also represents around one-third of our global brand media spend. Integration provides the absolute ability to direct and leverage this expansive brand platform across all consumer touch points.

In marketing terms, direct operation will facilitate a single integrated global program. Whether a particular ad features fragrance or ready-to-wear, it projects the Burberry brand. The ability to manage the fragrance spend as part of a cohesive media budget will assist in optimizing our brand presence in every market. The combined spend with integration also add scale advantages in media placement and cost.

Integration of fragrance and beauty further enables us to capitalize on the synergistic relationship with fashion in both product and marketing, and to better align these categories with our brand architecture.

In terms of distribution, we'll now work directly with the distributors to align our retail profile and point of sale presence, both physical and digital, with the brand fragrance and beauty, with the brand.

Fragrance and beauty are among the most visible categories on the selling floors, and we can now approach most major retailers with one unified brand statement.

Last year's Burberry Body launch, hopefully, illustrates a few of these principles in practice. As we said at the time, the launch was an outstanding opportunity to connect our expanded global audience with the modern Burberry brand.

Body imagery, which included the iconic trench coat, was projected across multiple channels, including outdoor, TV, print, in-store, through an extensive global marketing campaign.

Fragrance and beauty lend themselves particularly well to social media and other digital activity, which formed a key part of the Body program.

Body featured in the runway show, and was the basis of a ready-to-wear and accessory capsule collection for all stores.

In brief, Body supported the full brand by extending its reach to a new audience; showcasing digital innovation, and product integration.

For those who followed Burberry over the years, you'll recognize that this transaction is in line with our strategy of enhancing brand control, whether integrating geographies, such as China, or products, like men's tailoring.

Integration elevates a business to true core activity of the Company. It takes on an ownership mindset, allowing us to capture its full potential.

Now to the scale of the potential for fragrance and beauty. Fragrance and beauty is amongst the largest categories in luxury. According to Bain and Altagamma, the perfume and cosmetic segment represents 20% of the luxury market; the fourth largest segment after apparel, accessories, and hard luxury.

This market is anticipated to experience relatively stable expansion with mid single-digit growth in the medium term, and the higher end beauty category within that amongst the fastest growing. Historically, perfume and cosmetics has been less cyclical than the rest of luxury.

Looking at fragrance first, Burberry's underpenetrated, particularly as you consider our brand size on a relative basis. This slide compares the size of the Burberry brand to that of selected peers, whom, you might guess, are Dior; Channel; Armani; and Dolce & Gabbana.

Despite Burberry's position as among the largest luxury apparel and accessory brands, we are among the smallest in fragrance. And although relatively small, growth has been slow, with fragrance growing at one-third of the rate of the rest of the Group the last five years.

While we don't underestimate the highly competitive nature of this category, given the brand's broad appeal, women, men's, all generations, all geographies, there is clear opportunity for us to rescale the fragrance business.

And in beauty, we're just starting. It's positioned among the luxury beauty brand. We began a test two years ago. From there, we've continued to refine our proposition and slowly expanded the retail footprint to approximately 90 doors today. We lost a little momentum during the uncertainty over the license's future, and we're looking forward to intensifying our beauty effort.

Given our fashion credentials, appeal to the millennial luxury customer, and the strong early response to product, we see outstanding opportunity here. We expect beauty to form a core of this new platform.

I'll now introduce Matt, to outline our strategies for this new business.

Matt McEvoy - *Burberry Group plc - Senior VP, Strategy & New Business Development*

Morning. With the integration upon us, I'll provide a high level view of our product strategies for accelerating growth, and the plan for in-house operation.

In terms of product, we plan to continue to execute the strategy put in place over the last two years; a strategy consistent with that of the rest of our business.

Historically, Burberry has been a somewhat disparate fragrance portfolio. We've tended to launch a line and move to the next, with each introduction cannibalizing its predecessors. The launch of Body represented a shift in strategy. We looked to establish Body as a core pillar; a franchise that will remain a cornerstone of the portfolio. We're doing this with an ongoing program of Body line extension and limited edition projects.

The outstanding launch of Body parfum last September moved Burberry fragrances into the top 10 in the US, which is the largest fragrance market in the world. That was for the first time.

From there, you've seen the introduction of the EDT in July, and the current launch of Rose Gold limited edition; and that's to mark the one year anniversary, also in time for holiday.

In March, we're looking forward to launching Tender; a lighter, fresher interpretation of the scent, targeting high growth markets in Asia.

Through this strategy of building core franchises or pillars, we'll drive consistent sales growth and financial returns. We'll also position and segment the fragrance offering consistent with our brand pyramid; Body, in the more refined luxury zone; Brit, the most casual contemporary offering in the range.

We'll both rationalize the existing portfolio and add lines, continuing to shape the pyramid over time, developing the cohesion found in our ready-to-wear categories.

Beauty, as Angela mentioned, is moving from its test phase. Now that we've established a base, the plan is increase the pace of seasonal product introductions, similar to that of our monthly fashion themes, in keeping with the rhythm of this category, while continuing to strengthen the base.

An intensified marketing effort goes hand in hand with this. We'll begin to expand the number of doors, while remaining selective about the right space. All of this is basic stuff; some areas have not received the appropriate attention over the last year.

Operationally, we'll use the same structure as Interparfums does today. Burberry has always provided the creative product conception and design, all the marketing imagery; no change here. Interparfums has performed the product development, sourcing, operationally marketing, and sold to the distributors. Manufacturing, logistics, and sales to retailers are all outsourced.

Broadly, the plan is to step into Interparfums' shoes. We'll continue to work with the existing supplier base; we'll outsource logistics to specialist operators; and largely sell through the existing distributor network. As part of the Body launch last year, we started working more closely with this critical group, educating them on the branding and objectives. Previously, we'd only had limited contact with the distributors.

And this model's familiar to us. We manage and outsource manufacturing base, and often work with third party logistic agents. In some ways, operationally, fragrance is less complex than our core business; dramatically fewer SKUs in the product introductions, a smaller supplier base. That's not to suggest that the category does not have complications of its own, which we will have to master.

Which takes me to the transition agreement. Over the past 10 years, we've integrated a number of businesses; China, Menswear, as Angela mentioned. Each of these had its challenges. In the case of fragrance and beauty, although intimately involved with the business, we've not sourced the category, or worked closely with the customer base.

With the primary objective of continuity, we developed a transition plan with Interparfums. This involves a three-month extension of the license, taking it March 31; ensures continuity and development of existing projects; and includes transferring know-how to Burberry with the progressive transition of projects and processes over the next five months.

The work of integration is well underway. With the distributors, in September we hosted the largest dealers at the Runway Show, and a seminar on our future fragrance and beauty plans.

Our team was in Cannes two weeks ago at the annual gathering of the fragrance and beauty trade; meeting with distributors, in parallel with Interparfums, planning the marketing program for 2013.

Our sourcing and logistics teams are working with Interparfums and the supplier base to ensure continuity of product flow; the IT team is adapting our systems to incorporate this new product division; and HR is filling the people gaps. It's all happening. We plan to be operational by April 1.

Beauty, as we are calling it, has become the fifth product division. It will operate similarly to the other divisions, where a core group of category specialists leverages the functional expertise, like marketing and supply chain, the infrastructure, IT and financial systems, and regional organizations to deliver product to the consumer. In anticipation of this, we've recently hired category specific expertise.

Our new chief supply chain officer started in September. He has over 20 years experience in fast-moving consumer goods, primarily with Nestle.

A new head of fragrance and beauty product design and development to work with Christopher; she previously head of make-up at a leading French beauty house.

And to lead marketing for the category, our new head of partner marketing joined from P&G, with over 10 years experience in prestige fragrance.

So, that's our operating strategy in brief. Let me introduce Angela -- bring back Angela, something like that.

Angela Ahrendts - *Burberry Group plc - CEO*

Thanks, Matt. So, I hope we've conveyed a little of our enthusiasm for this new growth platform. It is the most visible expression of the brand, with excellent prospects to drive future financial performance.

In fragrance and beauty, Burberry has a product for the full range of the brand's fans. And we intend to capitalize on this amazing opportunity.

So, in summary, we are staying the course, investing in flagship and emerging markets, focusing on innovation and high growth product categories, driving productivity, while improving efficiencies, and always continuing to correct legacy issues, to deliver operating leverage, while illustrating our pay-as-you-go approach.

The team has never been more united or committed to consistent execution, regardless of the external environment, and we look forward to new opportunities in fragrance and beauty.

So, thank you very much. Stacey and I'll now take your questions.

QUESTIONS AND ANSWERS

Luca Solca - *Exane BNP Paribas - Analyst*

Luca Solca, Exane BNP Paribas. I have three questions, if I may. Could you give us a little bit more detail about retail productivity, and what you're experiencing in terms of growth, in terms of sales per square meter? And if you could give us also some clarity on the new format you're experimenting.

On brand development, it's very clear that Burberry is becoming stronger and stronger, as you've highlighted. I wonder if there are any gaps that you notice in the quality of brand perception between markets where you have legacy distribution, like China, and other markets that you've been managing for longer, directly.

And third, I understand how you're going to be having significantly better control of marketing as far as beauty is concerned, but I wonder about possible disadvantages that you may have in operations because of scale, inferiority against larger players, like L'Oreal and P&G. And I wonder whether you have considered joining forces with leading players, like them. And what is the rationale behind going alone?

Angela Ahrendts - *Burberry Group plc - CEO*

Okay, so that was actually four questions. And let's go back to front, because you may have to repeat one or two of the first ones.

Starting with fragrance and beauty, it's kind of like Matt said; there is -- in the PD and in the sourcing area, it is something we've never done before. Interparfums did outsource that. They had a little leverage because they had multiple brands. So we are absolutely in conversation to potentially outsource certain pieces, specifically PD insourcing, technical insourcing, with a larger player, to your point, to optimize the scale, etc.

So, we are building it. We're also looking at outsourcing opportunities. We have five months to figure it out. We're one month into the transition.

What was the third one?

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

There was one on retail productivity, which if I pick up. You can do the math in terms of our 1.2 million square foot and work out that in a full year we've been trading at about GBP1,000 per square foot.

It's a very different picture across the different geographies. So whilst we will exceed that, on average, particularly in the European and the Asian regions, we perform under that in the US market. I don't think that's any different in terms of the direction versus our peers. It's the nature of those markets.

We've had a lot of focus and activity over the course of the last few years, as you know, driving sales and service productivity within the stores. That work continues. And we know that there's still somewhat of a gap to close versus many of our peers, and we remain very focused on delivering that.

And, somewhere in the middle, there was another question about China, I think.

Luca Solca - *Exane BNP Paribas - Analyst*

What about the new format?

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

In term of the new formats, there's probably nothing to call out. When you say new formats, clearly, we have the Brit stores. They're largely -- we've got the Brit test stores largely in the US, a couple in Europe; nothing to call out in terms of differing levels of productivity.

We did mention that we had our first menswear-only store opened in Knightsbridge. But it's really too early to say anything on that as it was literally, what, a week or so ago.

China, I can't quite remember what the question was. In terms of the legacy? I think you talked about legacy --?

Luca Solca - *Exane BNP Paribas - Analyst*

The question was about the quality of the brand perception in China because of the legacy, which you have to deal with.

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

And in terms of the legacy, just to remind you, we acquired about 100,000 square feet. But very small in terms of the individual footprint, so 50 stores, about 2,000 square feet each.

I think as we called out in the release, as we start to open new stores, we really are opening them up in the larger format, appropriate for the individual marketplaces. So, for example, in Shanghai we've got three fantastic stores coming in the course of the next year, an average of about 9,000 square feet each. So it's a transitional journey in that marketplace.

Angela Ahrendts - *Burberry Group plc - CEO*

And it's transitional in the market, but then understand that nearly 20 million people go to Hong Kong. So we're up to 20 stores in Hong Kong, that's why the Pacific Place flagship that we literally just opened a few weeks ago. Macau, we've got a great footprint.

When they finally travel internationally, they go to Paris first. We've got new flagships that have opened there. Then they come to London, to Regent Street. So it's why I mentioned the editorial in Regent Street, because the pickup on Chinese social media was huge.

So it's not just in the market; the biggest opportunity is catering to the Chinese consumer, wherever they are. We do have Mandarin-speaking associates in every flagship store in the world today, and, to me, that impacts the perception in the home market, even more so than locally.

John Guy - *Berenberg Bank - Analyst*

John Guy, Berenberg. Three questions, please, but we can do it on a one-by-one basis, if you like. First one is with regards to the relationship between the retail/wholesale margin and the OpEx as a percentage of sales.

A great first half performance on margin; smashed the expectations in terms of margin in spite of, probably, a little bit more incremental markdown in the first half of the year. But the OpEx as a percentage of sales, up 190 basis points to close to 54%. Fashion and leather goods' peers run at 42.5%, and I can think of at least two other players that are sub-40%.

So am I being really cynical in thinking that you're just waiting until you have to terminate that Japanese license and knocking it down by, should be, 800 to 900 basis points? Or in order to smooth the EBIT delta? Or what's actually going on? Why is this still so high? That's my first question.

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

Shall I pick that one up, first of all? I know it's your favorite question, John. We always talk about managing the bottom line, retail/wholesale operating margin. In the same way as we don't talk about where the OpEx number might go in due course, we're not going to talk about where the growth margin might go to in due course.

We run a model internally, literally on a week by week basis, with Angela and myself dynamically managing the investment in the business to ensure that we deliver the operating margin leverage.

There are things that we could do, whether it's legacy cleanup, stopping some of the investment for the future, whether it's in technology, whether it's in new markets, that would immediately get that OpEx number down. But the whole point is that we're doing what's right for the brand in the longer term, and we're building the retail/wholesale operating margin on a steady basis. And we talk about having the leverage and the levers to pull to continue to do that, and that's what we will continue to do.

John Guy - *Berenberg Bank - Analyst*

It's still too high, Stacey. Anyway, okay, so second question around fashion and beauty. Very strong opportunity in terms of margin, and I think, looking at Interparfums' Burberry related revenue it was, in euros, about EUR230-odd million. I appreciate they get a little bit more kickback from some royalties and JV partners.

So the GBP140 million that you've guided to looks relatively conservative, and close to an 18% operating margin. Once you start to roll out on fashion and beauty, we should conceivably see that margin grow. Do you think that that's fair?

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

Yes, I do think that's fair. And it's probably worth just explaining a little bit about the background behind our GBP140 million estimate for the '13/'14 year.

You're absolutely right that when you look at Interparfums' numbers they go further through the value chain. They have certain JVs on the distribution side, which means they capture more of the end value.

We're talking about wholesale revenue only within the GBP140 million, and two aspects within that. First of all, we know that the first few months of '13/'14 will be adversely impacted for us by the fact that Interparfums will have been running down their inventory levels up to the point that they hand the business back over to us, come March 31. So we are not expecting there to be as much demand in those early months because the distributors, bluntly, will already have enough inventory. So the GBP140 million is a sort of part year revenue number.

What we've also done is to take a view on what might be inappropriate distribution that historically has been embarked upon. And in the same way, as you know, we've been in legacy cleanup on our core business, our view has been to get in from the off here and to build the business for what's appropriate going forward, without building another legacy for us to clean up in the future. So that's why we've been, hopefully, reasonably conservative with that estimate.

John Guy - *Berenberg Bank - Analyst*

And on the margin opportunity just -- ?

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

And on the margin opportunity, if you do the math, obviously, the GBP140 million represents not quite a full year's revenue, never mind the growth that you put on thereafter, and yet we'll be carrying pretty much the full-year cost base from April 1. Therefore, yes, there is opportunity to build that margin up further.

John Guy - *Berenberg Bank - Analyst*

Okay, thanks. And my final question, just on Burberry Britain watches. Gucci tried this and it ended up diluting their brand by introducing a relatively low end watch. I appreciate that this is a partnership with Fossil, but why are you moving into an area where, to be honest, I don't think you have the heritage; you don't have the craftsmanship; you don't have the after-sales experience. I'm just wondering, I think fashion and beauty is a great opportunity, but I don't understand why you're moving into this market.

Angela Ahrendts - *Burberry Group plc - CEO*

Do understand, we've played in that market for over eight years, so what we're doing is we're elevating this product. We have, historically, played in the under $500 watch category. That is one of the things we say correcting legacy issues.

We are repositioning the watch business. The new watches, on average, are fivefold the retail price of the old watch. They're not just check driven. There's an iconic expression that Christopher has designed; he has personally designed these watches with Fossil's creative director. So no different than Body in fragrance. The new Britain will be the pillar, will be the trenchcoat of our watch business.

So it's never going to be our core, but we are absolutely -- look at Chanel's J12, look at all of our peers; we are absolutely owed a nice, solid piece of business in this category.

John Guy - *Berenberg Bank - Analyst*

Thanks very much.

Fraser Ramzan - *Nomura International Plc - Analyst*

Fraser Ramzan, Nomura. Two questions. First one is on operating cost. Thanks for the detailed breakdown on cost you gave in the first-half release.

Looking at that comment on general inflation, that looks like 5% general inflation running through the business at the moment. And I'm just wondering, a, what you might be doing to get that number down in the second half because, not accruing the bonus, there's a limit to how long one can go on with that kind of activity; and, secondly, what the outlook might be on general inflation for next year, as you think ahead. That's the first question.

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

Okay, Fraser, you're absolutely right; a number of about 5% in terms of general inflation. Clearly, a large part of the cost base is driven by, first of all, the property costs running at the retail stores. And that tends to go either in line with turnover, because it's turnover-based rents, so, yes, it's inflation but it's linked to turnover; or there are step changes in some of the fixed rents from time to time, depending upon -- so you're always subject to the vagaries of what the specific leases say. But a large chunk of it is turnover related.

The second big cost across the business, of course, is payroll. And you can expect that we will manage the payroll very conservatively and responsibly, depending upon what happens to the top line, as we move forward; not only into the second half, but also into the outer years.

So you've got, if you like, those levers; as well as, as you called out, there's obviously the performance-related element of it, which is made up not just of bonuses; but also the outlook in terms of share scheme vesting, which is dependent upon longer term metrics around profit growth, typically over a three-year period.

Fraser Ramzan - *Nomura International Plc - Analyst*

So is it fair to say that 5% is kind of backward looking? You've had fixed rent reviews, you perhaps gave a payroll review at the beginning of the year, but, as we move forward, that should come down.

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

Yes. It's part of how we dynamically manage the business. I'm not going to say it's going to be x% next year; that's all part of where we are with the budgeting process right now for '13/'14.

Fraser Ramzan - *Nomura International Plc - Analyst*

Okay. And then a second one, inventory. Great inventory position at the half year. I guess you planned it down; you indicated six months ago that, that was where you were going, you weren't buying for the outlets. It kind of sounds a bit churlish, but to what extent did you get lucky there?

You didn't buy for the outlets, trade pulled back, you delivered the margin; fantastic. How flexible have you been able to be since you saw the pullback in trading? Because I think that's the ongoing story. Not buying for the outlets, that presumably continues for the second half, but then what about 2013?

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

I would say, I've got Donald sitting on the front row, the idea that we just got lucky on inventory management I think will not land well with him, or his team.

I think this is the culmination of the investment that we've made in the planning function, in the systems over the course of the last few years, which has meant that we've got much greater visibility now and we're able to impact the whole procurement process and the volumes far better than we've ever done before.

So, yes, we always planned for more effective inventory management in this period of time. Clearly, with the sales slowdown, we didn't deliver as much back into working capital as we might otherwise have liked to do, but this all consistent with the drive for operational excellence in the back end of the business.

You mentioned the point about not buying for outlets, well, that's something that's gone forever in terms of procuring. And we didn't do a huge amount, but we did do some in the distant past. This is now much more about managing through the pipe, for higher full price sell through in the mainline stores to start with, and ultimately having less inventory available for the outlets, which is absolutely fine; all consistent with our strategy of running fewer, albeit larger, outlets in the longer term.

Fraser Ramzan - *Nomura International Plc - Analyst*

[You don't think they'll likely think] (inaudible) fashion inventory risk into the important seasonal period?

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

No, we've got what we think is the right blend of current season merchandise. Yes, you can call it fashion. Remember, the way in which the pillar is structured, really, it's only Prorsum at the very top end that is high fashion; and then you've got, obviously, London and Brit; and we've got a high percentage of replenishments inventories as well.

Angela Ahrendts - *Burberry Group plc - CEO*

I was just going to say, half the business today on replenishment. But do understand, we are only now putting the replenishment module in place to have technology manage that for us.

Unidentified Audience Member

(inaudible - microphone inaccessible). So, just a quick question on China, if we can, in terms of the credit that come through in the exceptionals in the first half. Can you talk about your change in underlying assumptions for that business, and how that's changed versus 12 months ago? Thank you.

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

Again, this leads us back into another accounting point. As you know, when we acquired the China business back in-house two years ago we pointed out that we had a 15% economic interest held by a minority partner, with a put-and-call option associated with that.

On the put option, we are required to reassess every six months what that future liability might be in 2020 should that put option get exercised. That requires us to take a view on what sales projections there are that are likely to be in place for that business through to 2020.

Worth saying that the valuation isn't just based on the growth of that business, it's also linked to, for example, the overall Burberry multiple. So a number of complex factors that go into the calculation. But in the way in which we've reassessed what that likely cost might be in 2020 and discounted back to its present value, we have moderated, to a small degree, our growth expectations for China; and, clearly, at a lower starting point when you take it as of September 2012 anyway.

I would say it's just a -- not that big a moderation. We had significant sales growth in. We're still expecting significant sales growth, just not as significant as it was before.

So this is nothing to do with a view on China being less attractive than it was before; it's still a hugely attractive market. Everything that you read about that market remains consistent, in our view, as well. It's just from an accounting point of view it means that there's a credit back at this particular six-month period.

Unidentified Audience Member

Just a final one, if I may. On the Regent Street store, can you just talk about the impact that's had on traffic and on Bond Street; whether there's a difference in customer profile that goes to both of those stores? Thank you.

Angela Ahrendts - *Burberry Group plc - CEO*

Honestly, it's far too early to tell. The store's literally been open a month, and we don't know. The traffic on Regent has been absolutely sensational, and, again, due to all of the PR, all the marketing that's taking place.

And almost consider, Regent Street, that is an asset now that, no different than Burberry Body, we will leverage that asset to lure -- London is the second highest tourist market in the world today, and we will use Regent Street to lure traffic from all over the world there. But we don't have a lot of indication right now. And honestly, just opened up the men's store at Knightsbridge, so it too, being new, is getting a lot of traffic. But, hopefully, in the next couple of months we'll have a clearer picture on the different customer bases.

Annabel Gleeson - *Redburn Partners - Analyst*

Annabel, Redburn. Could you break down your gross margin between FX, price increase, and mix?

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

Yes. I'm only going to talk directionally because you can have teams of accountants trying to work out and compartmentalize every -- and depending upon where they come at the calculation get a slightly different answer. But the order in which I talked about them is the order of importance.

So the modest price increase is number one; followed by the FX benefits we picked up on sourcing, and we had some of that in the second half of last year. The mix shift to retail is actually -- comes a much lower third; it's much smaller compared to the first two.

Annabel Gleeson - *Redburn Partners - Analyst*

How does FX move into H2?

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

Well, as I said, on the sourcing piece, there's a lot of that that we picked up in the second half of last year anyway. So whilst there's a little bit that'll go into H2, it's not to the degree that you saw in the first half.

Annabel Gleeson - *Redburn Partners - Analyst*

Could you quantify the pre-opening costs within the half of this year?

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

Yes. The pre-opening costs, as I talked about, the pipeline of flagship new openings is probably the strongest we've ever had. As you heard, they've all opened literally September, October, and here into the first week of November with Chicago, so over the course of the first half we were carrying several million pounds worth of incremental pre-opening costs.

Annabel Gleeson - *Redburn Partners - Analyst*

How does that compare to last year?

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

Incremental, that was incremental.

Annabel Gleeson - *Redburn Partners - Analyst*

Okay. And last question, can you confirm that you were always intending to bring the perfume and cosmetics license in-house?

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

Always, going back to when?

Angela Ahrendts - *Burberry Group plc - CEO*

Exactly, yes.

Annabel Gleeson - *Redburn Partners - Analyst*

Well, since you announced it. Since you announced that you were buying out the license.

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

I'm not sure where the question's --

Angela Ahrendts - *Burberry Group plc - CEO*

We wouldn't have announced it if we didn't plan on --

Annabel Gleeson - *Redburn Partners - Analyst*

Well, I guess the question is were you always planning to bring it -- do it yourselves? Or were you actually planning to partner?

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

Yes. Yes, it was always the plan to gain greater control over that. And the question, as you've heard from the various presentations, is around to what degree you would use third parties to fulfill certain of the activities.

Annabel Gleeson - *Redburn Partners - Analyst*

Okay, thank you.

Nick Hawkins - *Cenkos Securities - Analyst*

Nick Hawkins, Cenkos. Can I ask about performance related, please? In the second half, should we expect a similar reduction?

Secondly, what happens next year if sales accelerate again? Does that just flow straight back into the P&L, or does it -- is it taken out? I don't quite understand how it forms in the first place.

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

The GBP15 million of performance-related pay impact that we called out in the first half is made up of two parts. So, yes, there's the shorter-term bonuses, but there's also the expectations on share scheme payouts, and those are highly complex.

And we have a number of models, as you'd expect, because there are vesting percentages that apply differently across the next three years, depending upon outturn. So it's not quite as straightforward as saying, well, it'll be the same amount in the second half. It also depends upon what the P&L outturn is for the second half.

So this is what we will manage, we continue to manage, dynamically internally. If the sales performance is better than expected, clearly, there'll be some investment back into performance-related payouts. If sales performance isn't there then clearly there's some add-back to the P&L. So it is one of the variable elements of the P&L account, and this is evidence in motion, if you like, of that leverage being added back.

To your second point, if sales pick up in '13/'14, to whatever degree, then, yes, we'd expect there to be investment back into the performance-related payments accordingly.

Julian Easthope - *Barclays Capital - Analyst*

Julian Easthope, Barclays. Just coming back to the perfumes and cosmetics business, when I looked at Interparfums, who, I'll admit, I don't know at all, they said that they'd basically been investing in their own distribution and they were, therefore, distributing themselves within US, UK, and three other markets. Was that the case for the Burberry contracts? And, if so, is that internal distribution easily outsourced?

Secondly, just so that we don't get caught next year in terms of the gross margin and OpEx, within that perfume business, is there a similar split -- or similar margin on gross margin and OpEx to your normal business? Or will bringing that in-house distort the gross margin and OpEx for next year, too? Thanks.

Angela Ahrendts - *Burberry Group plc - CEO*

On the fragrance and beauty piece, they, as Matt said, have nearly a couple hundred distributors around the world. There were a couple of key markets that they were distributing themselves but, honestly, not themselves; they've had a joint venture with a company called Clarins in a couple of those big markets.

So we can either opt to continue to work with Clarins, as they have; we can opt to go with another partner in those markets. And, again, we did a five-month transition agreement to give ourselves time to figure all that out.

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

Then in terms of the gross margin and OpEx mix, yes, it is a little different to the mainline business, and we'll give you some clarity about that as we go into '13/'14.

Bear in mind that one of the most significant differences is that this is a business model which requires a lot more in terms of the percentage of sales devoted to marketing than we have in the core business. And, obviously, therein lies some of the opportunity that Angela referred to in terms of being able to leverage that one-third spend that they have and the two-third spend that we have.

Angela Ahrendts - *Burberry Group plc - CEO*

Great. Well, thank you very much, again, for joining us, and I think there's still coffee at the back.
