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BRBY.L - Burberry Group PLC Third Quarter Trading Update Conference Call

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**John Guy** *RBS - Analyst*

**Fraser Ramzan** *Nomura International plc - Analyst*

**Julian Easthope** *Barclays Capital - Analyst*

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**Sophie Dargnies** *HSBC - Analyst*

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

**William Hutchings** *Goldman Sachs & Co. - Analyst*

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

## PRESENTATION

**Operator**

Good day, and welcome to the Burberry Group plc third quarter trading update and interim management statement conference call. Today's conference is being recorded.

At this time, I would like to turn the conference over to Ms. Stacey Cartwright, EVP, Chief Financial Officer, please go ahead.

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

Good morning, and welcome to Burberry's third quarter trading update call. With me this morning I have Fay Dodds, our IR Director. As usual, I'm going to provide a brief summary of our performance and then we will be happy to take your questions.

So in the third quarter, total revenue increased by 21% at constant exchange rates, 22% at reported rates; Retail accounted for over 70% of revenue in the third quarter and grew by 23% in total, 13% of which was from comparable stores, with mainline outperforming.

There was double-digit mainline comparable store growth in Asia, Europe and Rest of World and robust high single digit comparable store growth in the Americas, against a strong period last year.

During the quarter, flagship markets, which benefit from the traveling luxury customer, such as London, Hong Kong and Las Vegas, performed well. Northern Europe continued to outperform the southern countries. And China comparable store growth was again strong, up around 30% on top of the over 30% growth in the prior year.

And this Retail growth was driven by the consistent execution of our key strategies; so average selling prices were up, due to the outperformance of Burberry London, as well as higher full price sell through. Core outerwear and large leather goods contributed half of the mainline growth. And we saw strong growth from newer initiatives, such as men's tailoring and men's accessories.

Across fragrance, eyewear and watches, the combination of product innovation, the Burberry Body women's fragrance launch and improved in-store presentation led to sales in our stores increasing by more than 60% in the quarter.

Turning now to Wholesale, we continue to expect mid-single digit growth for the second half as a whole, with good growth from Asia travel retail, emerging markets and the targeted US department store doors, where we're investing in dedicated shop in shops across all categories. But as we've explained before, we've also taken advantage of the momentum in the business to further elevate the brand's positioning.

Second half Wholesale revenue would show mid-teens growth if you exclude the impact of these planned actions, which include converting Spanish menswear and our Saudi distribution to Retail; further rationalizing the brand's distribution in Europe and also the US.

And so the 4% growth reported for the Americas in this quarter is the net result of the robust Retail performance, I referenced earlier, plus the accelerated clean-up of US Wholesale.

For the third quarter, Wholesale revenue increased by 15% underlying, with early deliveries in Europe and emerging markets. Our key Wholesale accounts are now embracing monthly flow, to bring newness to their customers, ordering more this year to support the November and December floor sets than they did in the previous year.

And finally on Licensing, where revenue was up 12% on an underlying basis, Japan was broadly flat quarter on quarter but we had excellent growth from our three global product licenses.

The third quarter saw further progress on each of our five key strategies. Under the first, leverage the franchise, we continue to invest in digital technology in-store. We have iPads now in nearly all stores and retail theater in 180 stores. That's up from about 100 at the start of the year.

Combined with the refreshed burberry.com site and further innovation and social media, customers now have a pure brand experience across all mediums. And they can transact through whichever channel they choose, leading to further strong growth in digital commerce for the quarter, as an example.

Under non-apparel, which is around 40% of sales, the third quarter Retail performance was driven by core styles, with innovation in the iconic Haymarket and house check, which together with the elevated solid leather collections, drove strong increases in average unit retail.

Men's non-apparel continued to show significant growth in all categories.

And under the third of our strategies, retail-led growth, we've continued to invest in flagship markets. New openings in the third quarter included stores in Paris, Sao Paulo and Hong Kong. And our major flagship projects in Chicago and Regent Street are on plan.

For the second half, we're now expecting between 13% and 14% space growth, compared to our previous guidance of up at around 15%, reflecting some timing differences and a few additional closures of underperforming stores and concessions.

In underpenetrated markets, we continue to see good growth in emerging markets, especially India, where we now have seven directly operated stores. During the third quarter a net four franchise stores were opened, including our first store in Johannesburg, South Africa and Zagreb, Croatia.

And finally, the fifth of the themes, operational excellence, the clear highlight was the rollout of SAP in China, giving us now a full global visibility for the first time, enabling further improvements in supply chain, the global buy and optimizing replenishment. We continue to build our capabilities in consumer insight and analytics.

In conclusion, we're pleased with our third quarter performance, especially in this all important Retail channel. The consistent execution of our key strategies is serving us well and will be our focus in the future, mindful as ever of the challenging macro environment.

So with that, I'm now pleased to take your questions.

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## QUESTIONS AND ANSWERS

**Operator**

Thank you. (Operator Instructions). Thomas Chauvet, Citigroup.

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

I've got two questions. The first one I'm trying to understand what is the underlying growth rate of your developed market consumers, so the European and American, given there's a lot of moving parts here?

On the US, could you give us an estimate of America Retail/Wholesale growth excluding the effects of Wholesale rationalization but also excluding the effect of the advance deliveries from Q4 to Q3 in Wholesale?

And for Europe, similarly, would you be able to estimate the growth to the local clientele, so excluding tourism effect? I know you don't have CRM in place, but what is your best estimate?

And secondly, in fragrance licensing, can you remind us the key terms of your existing relationship with Interparfums? And what are the main options for you at the end of the revaluation period on July 31?

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

Okay, well, I'll take the fragrance first. The terms of license are that the license runs until 2017, but there is a clause in the license which allows us to seek a valuation of, and if we like the valuation and decide to proceed, to buy that license out, with the key date there being July 2012.

At the very least, we could carry on as we are. But we are looking at what the options might be that are more advantageous, both strategically and financially to Burberry. And, hence, the discussions that we've commenced with Interparfums, both to invoke the license valuation exercise, but also to talk about what other arrangement might be put in place, some sort of joint arrangement to run the business going forward. So those conversations are ongoing. And you're absolutely right, Thomas, a key day in that is July this year.

Then in terms of the underlying growth rate, you said it yourself, Thomas, we don't have CRM data right now. So it is very difficult for us to distinguish between the different consumer segments. I will say that, certainly, if you're looking at Europe, northern Europe is performing more strongly than southern Europe. So the northern European local consumer, I would say, is definitely holding up better than maybe the southern European consumer.

You asked about underlying growth rates in the US, if you strip out I think, just about everything by the sound of it --

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

Just Wholesale, Wholesale rationalization and the advance deliveries, how much did that --?

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

Advance deliveries, that isn't -- that's why we give guidance for the half rather than for the quarter, to strip out the fact that if you ship something in the last week of December versus the first week in January, it can be very distortive to -- and give a misleading impression for the quarter.

So the important thing is that we're maintaining the guidance for the half as a whole. So we're talking about mid-single digit growth on a reported basis, mid-teens on an underlying basis. And within that you've got good, strong growth out of the underlying Wholesale account, and you're offsetting that with the non-anniversarying of off-price clearance, which is basically sales to people like Nordstrom Rack, and Saks or Fifth. But we have been doing, and we've terminated as of this year.

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**Fay Dodds** - *Burberry Group plc - IR Director*

Thomas, if you look at that mid -- clean mid-teens guidance for the second half as a whole, you will see that underlying US department stores are performing better than that, if you ignore the clear up, as are emerging markets, as is Asia travel retail.

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

Thank you very much.

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

Thanks Thomas.

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**Operator**

Warwick Okines, Deutsche Bank.

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

Just -- if I may, just try a couple more on the US. On the Retail performance, in the first half, I think you talked about the Americas being one of the strongest markets, which implies strong double digit, and you're talking today about single digit. You referred to the comp space, I was just wondering if you could maybe just flesh out to what extent that slowing is purely a comp based phenomenon.

And secondly, I think in the past you've given a dollar value on US Wholesale sales. I think you've talked about less than $200 million. I was just wondering if you could say what proportion you would call legacy, just to give us a sense of how much clean up needs to take place.

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

Okay, I'll pick up the comp point. The first half, absolutely the Americas performed with one of the -- was one of the strongest regions, but it was up against the softest comps. They were broadly flat, to negative, in the first half of '10/'11, for example. They bounced back very significantly in Q3 of '10/'11, into double-digit comps, so clearly the high single digit comp is up against a much stronger comparable period last year.

In terms of the off-price, I don't know whether we've --

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**Fay Dodds** - *Burberry Group plc - IR Director*

I don't want to get into specific numbers. I think again, the best way of answering that question is if you go back to the half two Wholesale guidance, the discrepancy between the mid-single reported, and the mid-teens clean number, the biggest part of that is the US. So it's quite a significant factor in the second half, and you'll see a continuation of that into the first half of next year.

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

Okay, thanks very much.

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**Operator**

John Guy, RBS.

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

Just a couple of questions from me please. First of all, with regard to average selling prices, I know you talk about them being strongly up. Could you give us a little bit more indication as to price mix and ASP movement during the quarter?

And secondly, when I'm looking at the replenishment rates, could you refresh us in terms of where you are on rates of replenishment within men's and women's, and within women's, splitting out the outer wear and the leather goods business. Thanks.

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**Fay Dodds** - *Burberry Group plc - IR Director*

Yes, in terms of the average selling price, again, if you look at our comp growth, most of that is driven by average selling price increase, and that is mix. So it's outer wear, it's large leather goods, it's the strong outperformance of Burberry London, and some really good growth in men's tailoring; so very much a continuation of the trend that we've been talking about for quite some considerable time.

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

And then in terms of replenishment rates, really no change from the trend that we gave you at the half-year; so stronger on replenishment in non-apparel, womenswear is stronger than menswear, and that's largely driven by the strength of the outer wear business there.

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

Okay, and just a follow-up, obviously no comment specifically around margin today, given that it's, A), a trading update. But there seems to me to be quite a few signals that there are some positive implications around margin, off the back of around 50% growth driven, out of core outer wear, large leather goods.

You talk around knitwear and men's accessories, again positive in terms of margin, and you beat estimates by in excess of 100 basis points on the Retail/Wholesale gross margin in the first half of the year. So it all seems reasonably positive, in terms of looking out into the full year, relative to where the street is today, in terms of full year numbers.

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

Yes, and all of those factors, you're absolutely, John, contribute to our confidence in being able to say that we will be putting that modest improvement on Retail/Wholesale operating margin, for the full year. So, yes, everything is contributing nicely to that.

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

Okay, great, thanks very much.

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

Thanks, John.

**Operator**

Fraser Ramzan, Nomura.

**Fraser Ramzan** - *Nomura International plc - Analyst*

Just one quick one. Do you have any comment you could make on inventories at this point please?

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

Really, continuation of where we were in November. So inventories are pretty clean, nicely current and, clearly, we've got a lot of inventory that is replenishment focused which, again, stands us in good stead, should we be in the position of finding that we're over inventoried, and just be a case of slowing down the pipeline of replenishment, rather than needing to offload at a discount.

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

Thanks, Fraser.

**Fraser Ramzan** - *Nomura International plc - Analyst*

Fantastic, thank you very much.

**Operator**

Julian Easthope, Barclays Capital.

**Julian Easthope** - *Barclays Capital - Analyst*

Just the last quick question about the licenses. Within the perfume license, obviously you're looking at for the July period, but you've also got the watch license that comes up at the end of the year. I just wondered if you had any thoughts as to whether or not you'd want to gain more control over that one, thanks.

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

I think it's too early to say anything on that, Julian. We're very happy with Fossil. I think they've stood us in good stead, and we will look to see what the most appropriate arrangement is when we come to that as well.

**Julian Easthope** - *Barclays Capital - Analyst*

Thank you.

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

Thanks, Julian.

**Operator**

Simon Irwin, Liberum Capital.

**Simon Irwin** - *Liberum Capital - Analyst*

Three quick ones for you. Firstly, just going back to licenses again. Obviously, if you assume that Japan was flat within that, then you've obviously got some very strong trends within license income. How much of that is very much completely oriented around the launch of Burberry Body and how much of a follow through would you expect in those growth rates, purely from that launch?

Second question would be have you seen any differing trends in terms of the local versus travel percentage, such as you're aware of it, particularly within Europe?

And thirdly, are you changing your behavior or becoming more cautious about any of your Wholesale partners, particularly in southern Europe, in terms of the way you supply them?

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

Okay, there's quite a lot in there. First of all on licenses, yes, Japan broadly flat is a very nice performance out of watches, eyewear and fragrances. Fragrance the absolute stand out performer, as you would expect, with the launch of Burberry Body.

I don't know that we can give any growth rates for the future, off the back of that, other than clearly having made this launch now, we're keen to keep that fresh and front of mind, and to keep marketing levels up at, not quite the same as the launch, certainly, front of mind as we go through 2012.

The second question was around differing trends between local and the travelling luxury consumer, I go back to, I don't know that we've got any solid CRM data yet, that would enable us to give you anything meaningful there. We do still see, in many of the flagship markets, a nice presence from the local consumer, but that is obviously less prevalent in the southern European markets.

And then your last question was around caution on dealing with European Wholesale, I think is where you were going. So, clearly we've been cleaning up a lot of the smaller legacy accounts, in Europe, as part of our specialty store clean up. They're smaller. They don't have the same resources to portray the brand appropriately. And I think it's very timely in terms of the economy as well, that these are exactly the guys who we've been turning off season after season.

**Simon Irwin** - *Liberum Capital - Analyst*

Okay, in terms of the overall progress of cleaning up European Wholesale, what's the net impact at the moment, in terms of that that you're shutting down, and that that you're adding? Should we think about it in broadly flat terms, or is it still a drag?

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

Well no, we think about in broadly flat terms, because we have got growth from the top 10 customers in Europe; nice, solid growth from the top 10 customers, and there's a few million pounds of revenue that we are turning off from what can be hundreds of small, specialty accounts.

**Simon Irwin** - *Liberum Capital - Analyst*

Tremendous, thank you very much.

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

Thanks, Simon.

**Operator**

Sophie Dargnies, HSBC.

**Sophie Dargnies** - *HSBC - Analyst*

I have three questions. The first one, can I have a quick follow-up on the US? Did you see some difference between East and West Coast, in this last quarter?

And also, if the rationalization will continue next year, what could be the impact? Can you still have the same impact that you tell us for H1 2013?

On -- just, overall, for the quarter, did you see some difference month by month, or -- and did you see some difference also, by region, month by month, especially in the US and Asia?

And then the third one, can you tell us if you're still quite comfortable with the current PBT this year?

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

Okay, I'll go backwards up the list and let Fay pick up the end ones, I think. I think consensus has around GBP375 million PBT for this year, we certainly don't see any reason for that to change today.

In terms of quarterly trends, nothing of significance to call out, it's not that we saw any deteriorating trends or any converse trends across the three months, so no real trend aspects there.

And in terms of East and West Coast, I don't think there's anything, again, to call out there. It's more about the flagship markets performing that little bit more strongly.

**Fay Dodds** - *Burberry Group plc - IR Director*

Yes, and in terms of the half one Wholesale impact, clearly, we'll give you our full guidance in April once we've collected up the order books. But there is still going to be quite a significant impact from the US cleanup in that first half.

**Sophie Dargnies** - *HSBC - Analyst*

Okay, thank you very much.

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

Thanks, Sophie.

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**Operator**

Annabel Gleeson, Redburn Partners.

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**Annabel Gleeson** - *Redburn Partners - Analyst*

You've reported slightly slower space growth than we expected, so how should we be thinking about CapEx for the year end and also CapEx next year and space growth next year?

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

Okay, the sales space growth, I think we did say maybe around 15% for the half, we're now saying 13% to 14% for the half. Nothing of any major significance there, there's not any particular projects that have been delayed or anything like that. It's more around square footage, once you've actually evaluated what net selling square footage is versus back of house square footage, a few roundings down there. And a couple of men's prospective concessions in El Corte Ingles that actually we've chosen to close rather than turn into concessions.

In terms of space growth going forward, we've said historically about 10% per annum, so this was always going to be a little bit of a bonus year, if you like. That said, we're finalizing the budgets as we speak for '12/'13 and I would say the pressure is more to the upside of that 10% number.

CapEx, we talked about a range of GBP180 million to GBP200 million for this year. I suspect we'll be more towards the lower end of that range, but clearly a lot depends on the timing of actual cash out the door around some of the big flagship projects, what goes out in March, what goes out in April. We still have a number of major flagship projects lined up for '12 and '13 as well. And, again, against the backdrop of the 25% IRR that we look to achieve on all of our projects, so I would say again I would be expecting that number to be not too similar to this year's CapEx number.

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**Annabel Gleeson** - *Redburn Partners - Analyst*

Thanks very much.

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

Thanks, Annabel.

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**Operator**

(Operator Instructions). Rogerio Fujimori, Credit Suisse.

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

Just two quick questions, any quick color on your other key Asian markets beyond China, I mean Korean, Taiwan and Australia?

And my second question is basically on your overall pyramid after recent outperformance of Burberry London, how the -- has the composition change, i.e. the weight of London and Brit versus, say, 12 months ago? Thank you.

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**Fay Dodds** - *Burberry Group plc - IR Director*

Okay, in terms of the composition of the Asian region we saw a very good growth in what we call Greater China, so obviously China, Hong Kong, Taiwan and Macao. Korea, which is a big mature market for us on the Retail side has been a little bit softer, but we're seeing strong growth from the travel retail side and then nothing really to call out on the smaller markets.

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

Okay, and then in terms of the London mix, yes, London is picking up a share of the mix. So, historically we always talked about Prorsum being 5% to 10% of the business, London being maybe 35% of the business and Brit perhaps being more like 60% of the business. You're seeing Brit become more like 50% of the business overall now, with the extra being picked up by London.

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

Thanks. And this is a structural change or more driven by cyclical factors?

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

No, no, no I think it's structural; it is part of the mix shift in the business and the elevation of the ground.

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

Okay, thank you very much.

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

Thanks, Rogerio.

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**Operator**

William Hutchings, Goldman Sachs & Co.

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**William Hutchings** - *Goldman Sachs & Co. - Analyst*

I just had one question, which is on your like-for-like performance in China which -- we were surprised that it sustains up at this 30% rate and I wonder if you could give us a bit more color. Is this you materially outperforming peers? Or do you just think the whole market is still running along with (multiple speakers)?

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

Yes, such as we get data on our peers and, obviously, we have recruited individuals in from other luxury brands, so we do pick up odd snippets from time to time. We do think, yes, we're outperforming our peers.

Remember, we've got some self-help factors that perhaps some of them don't have. So we acquired the business back in September 2010, so we put a new team on the ground. We put support in from the regional team. We've got new merchandising strategies in there. We've been improving the supply chain performance into the region. And then, of course, in the last couple of months we've implemented SAP as well. So there's quite a lot of infrastructure support, which helps us improve the merchandising, improve the decision making and drive the business forward.

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**William Hutchings** - *Goldman Sachs & Co. - Analyst*

That's great, thanks and sorry, I have just one more follow-up on that. And has that allowed you, not just on a like-for-like basis, but allowed you to change your thinking about store openings because you've got better visibility?

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

I think -- I don't think it's changing our perspective on numbers of stores to go for. It may be that it's giving us further confidence to go to some of those bigger locations and know that we can get the productivity, the sales per square foot out of them.

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**William Hutchings** - *Goldman Sachs & Co. - Analyst*

Fantastic, thank you very much.

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

Thanks, Will.

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**Operator**

Louise Singlehurst, Morgan Stanley.

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

Just a quick comment from me, quick question to end up. There was a lot of talk about plan B at the end of last year and, obviously, you've come in with very good numbers over Christmas with 13% like for like. How are you thinking about the budget process going into the end of the year and what's the tone internally? Thank you.

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

The management team is, obviously, very alert and vigilant when it comes to trends or external metrics etc. So fair to say that everybody is being very responsible about how to budget for '12/'13. We've talked about having a base budget in place in terms of investment, with the opportunity as we go through every month with dynamic re-forecasting to release more monies as we go, on the assumption that trading holds up. But everybody is being very responsible and going for a kind of base budget approach and some, should the opportunities be there.

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**Fay Dodds** - *Burberry Group plc - IR Director*

And I think it's worth reminding you that we're much better positioned in the event of any downturn this time than last time in terms of we've now got SAP globally, much higher percentage of our sales and inventories on the replenishment side, the planning team being able to work with the regions to kick in and make sure they're buying the right inventory, so a lot more solid infrastructure than we had last time round.

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

Super, thank you.

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

Thanks, Louise.

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**Operator**

As there are no further questions in the queue. I'd now like to just hand the call back to Miss Cartwright.

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

Well, thank you very much everybody for your attention. We look forward to speaking with you again on April 17, which is when we will be publishing our second half trading update. Thanks very much.

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**Operator**

That will conclude today's conference call ladies and gentlemen. Thank you for your participation. You may now disconnect.

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