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Burberry

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BURBERRY

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Performance Review

Christopher Bailey, Chief Creative and Chief Executive Officer
Hi everybody and thank you very much indeed for joining us today. I will begin in a moment with some comments on today's results and initiatives underway across the business, including our plans for Festive. After that Carol will take you through the detailed financials and then I will wrap with some thoughts about the longer term opportunities.

Also as usual you'll see that many of our senior leadership team are present today and I hope you'll have a chance to chat to some of them if you've not done so already.

So turning to the first half, Burberry delivered a robust financial performance, in what was a challenging environment for luxury globally. Revenue was unchanged year-on-year, adjusted profit before tax increased by 3% and we increased the dividend by 5% to 10.2 pence as we moved towards our target of a payout ratio of around 50%. This is consistent with the Board's confidence in the long term prospects for Burberry and its focus on value creation for shareholders.

By channel while Wholesale and Licensing were broadly in line with guidance over the half, Retail comps slowed to down 4% in the second quarter, from up 6% in the first. I'd like to take a moment to put this deceleration into context by considering four macro factors that were its major drivers before covering our responses.

Three of these trends stem from changes in Chinese consumer behaviour. First, given the importance of the Chinese consumer to the luxury sector, our Retail sales were affected by a slowdown in total Chinese spending. This reflected weakening consumer sentiment following the stock market turbulence and economic uncertainty over this summer.

Second, the continued deceleration of Hong Kong, as mainline Chinese visitors chose increasingly to travel elsewhere the luxury sector as a whole experienced dramatic declines in traffic and Burberry was no exception. Given the significant contribution of Hong Kong to our business this had a meaningful impact on our top and bottom lines. The third related trend was a shift in travelling Chinese consumption to Continental Europe and Japan, helped by favourable exchange rates.

Our strong first half performance in these markets reflected this shift, with comps in excess of 50% in Japan and 20% in Italy, France and Spain. However, their relatively smaller contribution to our global business impacted our financial profile when compared to our peers.

Taken together these three trends resulted in a modestly negative performance from the Chinese consumer globally in the second quarter, with the downward pressure from China and Hong Kong more than offsetting good growth elsewhere.

Beyond these China related trends I would highlight a fourth macro factor, the recent volatility in the US. While our smaller markets of Canada, Brazil and Mexico delivered double digit Retail comp growth in the period, the US slowed markedly in the second quarter. This reflected uneven demand from both the domestic and tourist consumer.

The drivers here remain hard to read against a backdrop of a generally positive economic picture. However, we believe recent stock market volatility may have influenced local sentiment and that the strong dollar discouraged tourist spend.

In this context we have been dynamically addressing the things that we can control. In product we are actively managing challenges in certain categories, you will see from the pie chart in your packs that growth across categories was broadly consistent over the half, however accessories were more resilient than apparel in the second quarter, and a significant proportion of the slowdown in apparel was driven by outwear, excluding rainwear. So while trench coats continued to perform strongly, our heavier-weight winter styles were weaker, and we believe that unseasonably warm weather in many markets was a factor here. With the introduction of our new unlined cashmere coats and other product initiatives we have already seen improvement in this category in recent weeks.

In tandem with tackling product challenges we have been quick to optimise opportunities. This has included fast tracking replenishment best sellers like our Banner bag, and responding to strong demand for fashion products including ponchos and dresses.

We've also enhanced marketing strategies in support of core lines such as our Heritage trench coats and cashmere scarves, both of which performed strongly. And we were pleased to see AUR increase globally in the half, reflecting our strategy of mix and brand elevation and a good indicator of overall brand health.

In Retail we have extended our Customer Value Management programme and bolstered our Burberry Private Client teams to provide an enhanced service to more of our customers globally. And we are using data and insight to reallocate our marketing spend to best effect in this volatile environment. To give you just one example, in Hong Kong we have switched our investment from iconic out of home sites that target tourists to emails, events and media more relevant to the local customer and Carol will touch on this in a little more detail in just a second.

All these actions helped to drive improved conversion across all channels globally year-on-year, including an 8% increase in mainline.

Finally, as you would expect, we have further sharpened our existing focus on driving productivity and efficiency throughout our business. As I've said before this agenda covers ongoing actions across product, Retail and processes globally. Galvanising our organisation to realise improvements in this area has been a personal priority since I took up this role over 18 months ago and has taken on still-greater importance in recent months.

There are two specific dimensions of this agenda that I'd like to highlight today. The first is our acceleration of cost efficiencies during the second quarter. Decisive action since July has resulted in around £20m of savings against our plan this year; from areas including travel, hiring and other expenses. And, in addition to these tactical measures we continue to assess all dimensions of our cost base, strategically, for the future.

Second, beyond expenses we are taking action to improve the overall productivity of our business with a number of major projects currently underway. Let me give you just a couple of examples. First our ongoing IT system upgrade, this is already enabling more responsive decision making across the business and will unlock further operational efficiencies over time as new releases come onstream.

For example we're already seeing benefits in terms of managing our inventory, as you'll hear from Carol this was in line with sales for the first half, despite the environment. And we are looking forward to the next phase of our online and offline inventory merge in the UK and US later this financial year, building on an earlier pilot introduction in China.

The second initiative I would highlight is our move to one label. This will make the Burberry shopping experience more intuitive for the customer in all channels, while retaining the breadth and diversity of our existing collections, as well as our price points. We have been trialling this approach in around 5% of our stores over the past six months, with positive results; including a low double-digit uplift in sales compared to the control group.

The move to one label will drive efficiency from design, to sourcing, to stores and is an important step in our ongoing drive to focus and rationalise our assortments, as we spoke to you about last November. And finally we are pleased to report that the news has been very positively received by our global network of Wholesale partners.

In addition to these actions underway across the business I'd now like to turn to our plans for Festive specifically. Last week we were glad that some of you could join us for the launch of this year's Festive campaign at our Regent Street flagship and we'll be sharing the campaign again at the end of this meeting for those who couldn't make it.

With our biggest trading weeks still to come, we are of course mindful of the external uncertainties. That said, we have never been better prepared internally to execute this Christmas and Lunar New Year, after 12 months of meticulous planning. To give you a flavour of what this means in practice let me offer a handful of very specific examples.

In product we have a more extensive and more compelling gifting assortment than ever before. This includes a particular emphasis on expanding our entry price points and heroing our iconic products, with the cashmere scarf proudly front and centre this year.

And as we focus on having the most exciting and covetable product in our stores at this critical moment, we have also fast tracked the monogramed Runway rucksack from the September show. This style sold out on Runway Made to Order within 24 hours and we introduced a waiting list to meet the demand. The first deliveries will now take place in mid December two months ahead of our original schedule, and with wider distribution to stores globally in early January.

And more broadly our operational readiness is better than ever with our strongest delivery position to date across all of our collections.

In marketing I would first highlight our festive campaign, launched last week it has already generated a fourfold increase in coverage, reach and as many impressions through social media in two days as across the entire eight week campaign last year.

And we have also expanded the distribution of our Book of Gifts which you will find on your tables today. We've introduced two physical formats, created an online version, enhanced store distribution and increased partner outreach, all in support of a near tripling of its circulation year-on-year.

Finally in service our customer value management tool is now live in more than three quarters of our store base, in readiness for the weeks ahead. This is supporting a greatly enhanced outreach programme to our global customer base and a planned doubling of festive appointments through our expanded Burberry Private Client teams.

And we are also planning almost 200 festive events in stores around the world, these include a new 'Personalised for You' format, that celebrates our heritage through live demonstrations of the craft skills involved in the making of our iconic products. This resonated very strongly with customers when we premiered the concept for our Shinjuku and Seoul launch events last month. And I should note that we are similarly well positioned for Lunar New Year in February, including with a dedicated marketing campaign and an innovative, personalised WeChat partnership.

While not at the same scale as Festive, Lunar New Year represents the second most important peak for our business and we have shifted gear in our preparations over recent years accordingly.

Since the start of the third quarter comparable sales, although volatile, have improved overall relative to the second quarter. And so, ahead of the key festive period we continue to assume mid single digit percentage growth in the second half; but the external environment remains challenging and uncertain.

With that I'd like to share a short video summarising some of our highlights from the first half, I will then pass to Carol, before coming back and ending with some brief thoughts on the future.

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Financial Review

Carol Fairweather, Chief Financial Officer
Good morning. I will now talk through our financial performance for the first half. Against the background of a challenging and uncertain environment for luxury, our revenue for the first half was unchanged, while adjusted PBT grew by 3% underlying. Retail/Wholesale profit was up 5% underlying, reflecting slower than expected sales partly offset by tight cost control versus our plan and about a £30m reduction in performance-related pay.

As planned, Licensing profit was down 13% underlying as we took direct control of our business in Japan. Our cash position remained strong and we have declared a 5% increase in the interim dividend to 10.2 pence.

Turning to revenue, which we've already reported - so let me just summarise the key points. Revenue in the first half was £1.1bn, with a negligible FX impact. In Retail revenue grew 2% underlying, with comparable sales moving from 6% growth in the first quarter, to a 4% decline in the second quarter, with all regions slowing.

As Christopher has explained, our geographic mix with a small business in Japan and a relative overrepresentation in the UK was not helpful in the half.

Digital again outperformed, although it slowed in the second quarter, reflecting softer demand from domestic consumers - its primary customer base.

Elsewhere Wholesale was down 3% underlying and Licensing down 18% underlying, both broadly consistent with guidance.

Before I turn to profit, given the challenging environment we're facing in Hong Kong, I thought it might be interesting to show you what Pascal and the team have been doing over the last year. In analysing our Retail performance in all regions we think about it in the framework of the retail equation; looking at footfall and conversion to give the number of transactions and them units per transaction and average selling price to give an average transaction value.

This data is used throughout the organisation, from the store manager looking at it weekly, to the Board reviewing it from a strategic perspective. As you can see from the chart on the right the sector wide decline in traffic that Christopher has referenced has been a clear headwind for mainline comp growth. But this has been partly mitigated by the improvement in conversion, up over 20% in the half, as we focus on our retail productivity. And with both units per transaction and average unit retail slightly positive.

We achieved this through an intense focus on product, such as fast tracking, best-selling, or exclusive lines, especially in leather goods. Customer service, be it engaging with our existing local customers through our CVM programme, or running nearly a hundred events during the half to recruit new local customers, for example through partnerships with the financial sector. And marketing to support traffic as best we can, redirecting our spend towards domestic customers who are now about 25% of our revenue.

In addition, as part of our preparation for Festive, we've also opened two pop up Scarf Bars.

We also tightly controlled operating expenses; given that our largest cost is rent, which is mainly fixed, we have been seeking to renegotiate with our landlords and have been successful in a number of cases. With the support of our long-term partner at Pacific Place, we recently reached a lease restructuring agreement for our Hong Kong flagship store. During the next financial year the store will reduce in size, but will remain our flagship and our largest store in Hong Kong, while significantly boosting sales per square foot and protecting profit.

The second largest expense is salaries, where we have recognised store staffing, while ensuring that we continue to deliver a consistently high level of service. Retail headcount is down nearly 25% year-on-year at the end of September. All of which means that despite Hong Kong remaining a challenging market for luxury, it is still a high margin market and all of our stores are individually profitable.

So moving now to profit, as this slide shows, our adjusted operating profit was £152m in the first half, with a 5% underlying increase in Retail/Wholesale profits, offset by the planned decline in Licensing and a £3m negative FX impact. The FX impact in Licensing of about £2m reflects the sterling/yen hedge rate and there was minimal impact in Retail/Wholesale as the strength of sterling against the Euro was almost entirely offset by weakness against the US and Hong Kong dollar and the Chinese renminbi.

Currency markets have remained volatile and given the movement in exchange rates from the 30th September to 31st October with sterling weakening against most of our major trading currencies over that period, the overall impact from FX in the full year would now be broadly flat compared to around £10m benefit when we spoke last time. Although of course rates may well move again over the course of the second half.

Turning to Retail/Wholesale, this shows how profit has moved year-on-year. As you know there is a strong link between pay and performance at Burberry. So in the first half we saw a reduction in the performance-related pay charge of about £30m compared to last year. While this will help protect this year's profits, on our current planning assumption that the charge returns to a more normalised level, this would become a headwind in the next financial year.

So looking at the Retail/Wholesale profit in more detail, gross margin was up 100 basis points to 68.7%, this increase is largely due to a one off inventory charge relating to Beauty that we incurred in the first half last year, which is not repeated. And elsewhere in gross margin there was a small benefit from channel mix as Retail outperformed Wholesale, but this was largely offset by an adverse geographic mix, given Asia and particularly Hong Kong, a high margin market, slowed.

As you can see from this slide operating expenses were £611m in the half, including the reduction in PRP.

We continued to invest in the business with the majority of the absolute cost increase coming from new or refurbished stores, while protecting our investment in marketing and technology, which along with all other costs, we keep under regular review.

In addition we saw modest increases from general inflation and a small negative impact from FX. These were offset by lower variable costs, such as turnover rent as sales slowed, and a very tight control over all discretionary costs.

As part of our ongoing productivity and efficiency agenda that Christopher has spoken about we have taken swift action to control costs from a hiring freeze, to reducing travel and expenses and other discretionary costs. This will save about £20m in the current year against what we had planned to spend. As the programme was initiated in July this will be H2 weighted.

And now turning to Licensing, as you know the licenses in Japan which use the Burberry name and which have been in place since 1980 expired at the end of June. As a result, Licensing income from Japan reduced by £10m in the half versus the prior year. In the second half, as planned, we expect Licensing income from Japan to be down about £16m. The income in the second half comes from the licence transition payment and the new licence for the Blue & Black labels now branded Crestbridge. And looking forward to next year, License income from Japan for the full year is estimated at about £10m with the first full year of the new Crestbridge labels.

So whilst Licensing income from Japan will go from around over £50m in 2015 to about £10m in 2017 we believe this was absolutely the right thing to do for the brand and the business, in what remains the second largest luxury market in the world.

From September the only Burberry branded product in the mainline channel in Japan is our Global Collection, sold through our 35 directly operated stores, concessions and digital, complemented by Beauty, distributed by our new partner Shiseido.

Moving down the income statement I would highlight two things, firstly the adjusting items income of £1.8m compared to a charge of £10.5m last year. The charge for the amortisation of the Beauty intangible was £7.5m in both periods, while the China put option calculation resulted in a £9.3m credit this half, largely reflecting lower long-term growth forecasts for the business in China.

Secondly the effective tax rate for the year is estimated to be around 23% in line with guidance and slightly below last year, primarily due to the reduction in the UK corporation tax rate.

Our business remains highly cash generative with £167m cash in flow from operations, depreciation was £63m, with about £140m expected in the full year, and our seasonal working capital outflow was £26m below last year.

I am particularly pleased with our inventory position at 30th of September. At £478m it was £4m lower than last year, down 2% at constant FX. Replenishment accounts for about one third of our inventory and is broadly flat year-on-year, despite sales being below our plan. This reflects vigilant monthly reforecasting and reordering.

We also continue to benefit from our investment in technology and planning teams, for example the automated allocation system that Donald talked about last November is now live globally.

And finally we're excited about the innovative trial we are doing to support the Scarf Bar, holding more inventory centrally and less in the regions, allowing us to dynamically react to global sales trends, maximising revenue whilst minimising inventory. And although still early, the total increase in scarf inventory year-on-year is less than half the increase in sales.

And this chart shows the major cash outflows in the first half. Capital expenditure was £80m, with over half in Retail biased to our flagship markets, and the balance on IT and other projects including the purchase of the land for the new manufacturing facility in Leeds. And we continue to expect capital expenditure of around £180m for the full year.

Other major outflows, a tax of £56m and the final dividend of £112m, and we finished the half with £459m worth of cash, an increase of about £150m compared to the same time last year. And once you adjust for our leases, this is the equivalent to about £550m of net debt.

And finally for the first half we have declared a dividend of 10.2 pence per share, up 5% compared to 9.7 pence last year as we move towards our target dividend payout ratio of around 50%, based on adjusted diluted EPS in FY16.

The slide in your pack gives our normal guidance for the balance of the financial year, which is a challenging and uncertain period for the luxury sector. And you have seen this morning how we're responding. Christopher has talked about some of our product and marketing strategies as we enter Festive and the business wide focus on productivity.

As we look forward, while growth in the luxury sector is widely expected to slow, we remain intensely focused on executing our strategies, both short and long-term, to deliver sustainable profitable growth and value creation.

So thank you and I'll now hand back to Christopher.

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Outlook

Christopher Bailey, Chief Creative and Chief Executive Officer
Thank you very much Carol. So I hope that has given you some helpful further context about the current drivers of our performance and what we're doing in response. However, as a management team our job is not only to run this business day-to-day, it's also to focus on the years ahead, always thinking about how we can drive sustainable growth and value creation over the long term.

So I'd like to close by taking a little step back from the current context and sharing a few thoughts about the future. As we look ahead current macroeconomic uncertainty notwithstanding there is no doubt that the fundamentals of the luxury industry are changing. Growth in Chinese luxury spending is moderating, competition in digital is intensifying, pricing leverage and space growth are tempering and customer behaviour is rapidly evolving. For these reasons, and more, sector growth is now forecast at just 1-2% in 2015 compared with 7% just a couple of years ago.

But our ambition remains to outperform in this new context, because we continue to see significant opportunities ahead, as the customer evolves and becomes more digitally-minded.

Our confidence begins with our brand. In this next phase we believe what brands stand for and their ability to stand out from the crowd with a unique point of view will become more and more important. We have tremendous advantages here. Burberry will celebrate its 160th anniversary next year. It has seen many changes over its long lifetime and today we believe the brand has never been stronger. It has a clear and distinctive identity, grounded in our iconic products, the trench coat and the cashmere scarf, and their Made in the UK provenance.

The strong recent performance of these core products reflects the emphasis we have placed on celebrating our heritage over the past year. Most recently I'd highlight the launch of our Scarf Bar with an expanded assortment of colours and an enhanced personalised monograming offer; as well as a new in store and online presentation. This has resonated with our consumer and we have many more exciting plans in the pipeline.

And just last week we announced our plans for a new state-of-the-art trench coat manufacturing and weaving facility in Leeds. This will respond to increased capacity demands in our aging sites, while safeguarding the craftsmanship of this iconic product for the future.

While protecting and celebrating our history is a critical part of our brand identity, ensuring its contemporary relevance is every bit as important. This blend of British heritage and creativity and innovation is a big part of what makes Burberry distinctive in the sector; from the design of our products to our digital mindset and broad appeal.

In the Digital space, in the past six months alone, we have launched on Apple Music, we previewed our show and our new campaign on Snapchat and we developed on-platform commerce partnerships with LINE and Kakao, the leading mobile messaging platforms in Japan and Korea. All these were sector world firsts. And we now have about 38 million followers across our social media platforms worldwide. These are just a few examples of how we are constantly shaping the brand for the present and the future, whilst remaining true to the codes of its past.

The global strength of our brand is the foundation from which we will realise the many growth opportunities that exist for our brand and our business by channel, by region and by product category, and we have plenty of fuel in the tank.

By channel we have further to go in our ambition to become a truly great retailer, and this is one of our most important priorities. With Retail now around 70% of sales we have flipped our channel mix from a decade ago and established a network of stores in outstanding locations around the world. However we still have significant benefits to realise as we focus on embedding best in class retail disciplines right across our day to day operations. This includes targeting productivity levels more consistent with those of the best of our Retail led luxury peers, whilst of course being mindful of our product mix.

We have a major opportunity here, not least in respect of driving loyalty and conversion, including enhancing our service proposition and more effectively leveraging the more than 10 million customers in our database.

Another major focus by channel is continuing to build upon the leadership position we have established in Digital, of which ecommerce is of course an integral and an important part.

As the sector becomes increasingly digitally engaged the landscape is more crowded than ever. But we have some of the best talent in the industry and an infrastructure built to support the full end to end customer journey. Recent examples of this include our new mobile site and improved tablet platform, and upcoming changes that will significantly upgrade the performance of Burberry.com in China and Japan with much, much more to come.

But perhaps our greatest differentiator is the digital mindset that runs through every part of our business, always linking the physical with the digital worlds. We will continue to use this to our advantage in the months and the years ahead.

By region I would highlight the significant opportunities that remain for the brand in the two largest luxury markets in the world, Japan and the US. Following the expiry of our licences earlier this year we are now fully engaged with building the business in Japan with an outstanding initial response to the Global Collection and a strong plan for the future.

While still early on in our journey we recently opened our sixth standalone store in Shinjuku and six more department store concessions, as well as assuming operation of ten children’s wear concessions. All represent excellent progress as we establish ourselves in this very exciting market.

Less well-rehearsed, however, is the scale of the opportunity that remains for us to reposition the brand in the US, both through our Retail presence and critically our Wholesale footprint, including through Digital given the US consumers’ propensity to shop online.

Our move to one label will be an important part of this process, as we look to bring a more coherent expression of the brand to the consumer in this market, and to ensure global consistency in our positioning.

And we are evolving our management team for this next phase of our growth in the US with Donald Kohler, who I think you all know, taking the reins in the Americas region a couple of months ago. We will of course ensure that we are sharing learnings and best practices globally as we transition these two critical markets over time.

Finally, by product category we will use the lens of our successful Heritage trench and Scarf Bar initiatives to perfect our offer in bags and leather goods, where we remain significantly underpenetrated. And we will naturally continue to innovate and perfect the outerwear that is our DNA.

Elsewhere in product, we see particular opportunity ahead in Beauty, with exceptional momentum in our nascent makeup business and a major men's fragrance launch, Mr Burberry, that will be coming out in Spring of 2016. This will be a pivotal moment for our wider men's business as we reinforce the link between fashion and beauty that has become a real brand differentiator, and which has been so much a part of the success of My Burberry.

And the launch this year of partnerships with industry leaders Sephora and Shiseido further demonstrates the potential of our brand in this category.

So we're looking to the future, both near term and longer term, with confidence. And while the external environment continues to challenge, we will do as we always do and focus relentlessly on the things within our control.

From the brand, building its great momentum and realising its further potential, always with a Digital approach, to the product with so much to play for in expanding and perfecting what we have; to our customer vision as we prioritise enhanced retail disciplines and position the brand for further success in both new and existing markets.

And finally I would drive to become more efficient, productive and responsible in everything that we do, from controlling costs and optimising our investments to a continued focus on culture and purpose, including with the recent launch of our apprenticeship schemes and all of our ongoing sustainability efforts.

With that thank you very much indeed for listening and we will now be happy to take your questions.

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Questions and Answers

Question
Thank you very much Christopher. Two questions if I may. The first one about branding. So you move to a single label and this is a very important decision in the history of a company like Burberry, and I kindly ask you to give us an idea of what will be the end goal, the target? We will expect a brand with this wide price positioning going forward or we expect a brand that will expand more the high end or more the entry level products? So what will be the brand? How will be the positioning in five years?

Always related to this question is the transition plan. The transition plan means nowadays you have got in the stores three brands, London, Prorsum and Brit. How you will manage the transition? We will expect markdowns of these products going forward? Tomorrow morning we will find that the same trench coat that is a continuation product with a new label and in the same rack the one with the old label at the same price? And so give us just an idea of if there is any impact on profitability and markdowns.

And the second question is about Japan.

And the last one about Japan is in your plan when Japan will have a positive yield margin, will not be an investment anymore and will bear its fruit? Thank you.

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Christopher Bailey, Chief Creative and Chief Executive Officer
So in terms of the label, first of all the whole intention was to give clarity and consistency to our global consumers. What we are doing is we're looking very holistically at all of our collections. We will continue to have the broad - the depth of the offer, and also the price points. So today where you have Brit, London and Prorsum, maybe I can just give you one example.

Today you might have two biker jackets in Burberry Prorsum, two biker jackets in Burberry London and two biker jackets in Brit. The market may need three. We will retain the same price points, so we will continue to have the high fashion, we will continue to have the more casual and we will continue to have the wear to work. They will all sit together but there will only be three instead of six. So what we're doing is we're making sure that the consistency of the message is Burberry.

Today customers are not coming to us to say that they're looking for three different wardrobes, they're looking for one wardrobe and we're confusing the customer because they have to find number one a Brit and number two a London and number three a Prorsum on different floors around for example a department store.

We have been very quietly doing some testing for example on Saks Fifth Avenue. We have got a Burberry store that is a curated version of all of our lines, so what you will see there is you will see the heritage trench coat which doesn't change, it goes across everything. But alongside it you will have things in there where we're mixing all three labels. We've also done that with Nordstrom in Vancouver.

We've been testing this again very quietly through curated stores, our store in Soho where customers are coming in with an end product in mind and instead of trying to get - for example in our Regent Street store today they may find that same biker jacket, they may have to go to the ground level, they may have to go to the second floor and they may have to go to the first floor. The price points will be able to sit together and we will make sure that we merchandise them so that they all sit together so we will still have the depth of price points, but it's really for the end consumer in mind.

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Question
So in five years time should we expect that Burberry will be positioned higher than today?

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Christopher Bailey, Chief Creative and Chief Executive Officer
We're not looking at it in terms of a high - it will naturally elevate the brand because we will have consistency, so for example perhaps in some Wholesale stores in the Americas we may not be in some of the lower price points areas, but we will hopefully have one

strong Burberry point of view in that store that has the more casual, the more formal and the more fashion. So this is about elevating the brand and the perception, but it's not about saying that all price points are going up. We will naturally see AUR rise slightly, but it's not about raising our price points.

And the transition, it's a very, very thoughtful plan. We've been working on this for 12 to 18 months. Some of you may have noticed that over the last 18 months in our campaigns we've taken all the labelling off the campaigns. We've also been very quietly transitioning our Brit only stores and London only stores to Burberry stores, and we have got a very, very thoughtful plan over the next two to three years of how we will move product around and how we will make sure that we have that consistent viewpoint.

So it's a very - we're taking a very thoughtful, very strategic approach to the transition. We've been working with our Wholesale teams, and as I mentioned we've had an incredible reaction with our Wholesale teams all around the world because they like the clarity and the consistency that the brand will have. And it's a journey that we're going on with them, how we will transition within our Wholesale stores.

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Carol Fairweather, Chief Financial Officer
Do you want me to take the one on Japan? So in terms of we talked to you this time last year about the fact that our plan for Japan was to get to around £100m of revenue and £25m worth of EBIT. We said that as we were securing the right space and Pascal and the team have been incredibly demanding to make sure we only got the right space, we said that might nudge out now to more like 17/18 and we're still well on track to deliver that. As you've seen today we've got six free mainline stores now, 19 concessions plus the children's wear concessions. So at the moment we're seeing very strong reaction, and our plans are on track to deliver around £25m and £100m sometime from 17/18 onwards.

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John Guy, MainFirst
Three questions please. If I could just start with the gross margin, when we're looking at the half I think there was about 100 basis points impact on the fragrance one off. You had a ten basis points or so positive impact at the FX. So when you're looking at the geographical and the channel splits can you give us an idea in terms of what happened there in terms of the gross margin? That's my first question.

My second question, on slide 7 you talked about the Hong Kong Retail equation with the conversion up 20%. Is it fair to say within that bar, although obviously not quantified, that the traffic was down in the region of 50%? Just to clarify that.

And with regards to the AUR increase, that looks reasonably small obviously relative to I guess an eight to nine year historic AUR CAGR so maybe could you just talk about that?

And finally on the opex as a percentage of sales up 70 basis points in the half. That includes I think the 30 million one offs, so if we're looking at the underlying it was 59.4% up 340 basis points. Now I appreciate you tend to have a higher opex weighting as a percentage of sales in the first half, but you know even in the environment that we're in at the moment that's probably getting close to 1,000 basis points higher than say the global soft luxury average. I appreciate you're more ready to wear than some other players, so before you give me that one I'll just get that in there, maybe you could just talk about how you see gross margin and opex and I appreciate what you normally say, but is it time to start to really reign that in? Thanks.

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Carol Fairweather, Chief Financial Officer
So in terms of your gross margin, as you said most of the increase in gross margin this half came from the non-recurrence of the Beauty write off that we took last year, tiny - 10 bps from FX, and the rest was really channel mix being largely offset by regional mix. So nothing significant in those two, very net-net, not very much at all to call out between regional and channel mix. Retail obviously grew stronger than Wholesale, a little bit of margin depression from the Asian market slowing more quickly than the other markets.

And then going forward we have talked for a while now about looking to maintain gross margin, clearly tightly managing inventories but really continuing to - having made that shift to Retail having seen the improvements from inventory, looking to maintain gross margins going forward, but not looking for significant gross margin benefits going forward.

Then your second question about the Hong Kong Retail equation, certainly traffic I think we've been talking - I don't know if we put an absolute number on it but you're not far off in terms of the percentages you're quoting, so very significant traffic declines as we've gone through the last year.

Your comment on AUR in Hong Kong, I mean we've talked about AUR increases moderating both in terms of like for like price increases and through the way in which we have had AUR increases from moving through the product hierarchy if you like. I mean in Hong Kong we had taken prices down a tad and we've been able to offset that then by elevation in other categories. So we're happy with the AUR movement we've seen in Hong Kong over the last year.

And then back to opex as a percentage of sales, you are absolutely right we are always an H2 weighted business, and therefore I wouldn't read too much into having backed out the PRP charge or the underlying opex percentages. We had guided earlier in the year to the fact that we expected Retail/Wholesale margins not necessarily to increase this year given the investment we were making in those key flagship markets in Japan. This was another year where we would continue to invest, but our goal to drive modest improvement in that margin over time remains absolutely unchanged. The productivity agenda that Christopher has spoken to, it's about driving the top line through making sure we seize that opportunity to become a best in class retailer. We talk about the gap between our productivity and peers and where we are today, so we see the opportunity to drive EBIT margin over time coming both from the top line, less so from gross margin, and then from the operating cost initiatives with this tight control over all costs, looking at new ways of working, behaving more efficiently, plus with the investments we'll be getting from some of the IT infrastructure upgrades. So, no change to our guidance for the medium term on margin.

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John Guy, MainFirst
Okay thanks.

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Luca Solca, Exane BNP Paribas
Going back to line consolidation, I found it very interesting that you trialled already in 5% of your stores. So if you could enlighten us on how this worked and what were the moving parts that made the business grow faster. This is particularly interesting because I understand the efficiency side and the reduction in complexity in the supply chain, but I was more curious to understand how this translated into better sales?

As far as the wholesale impact is concerned, maybe a naughty question but is there a possibility that wholesale customers are happy for the wrong reasons in a way, because they will now have one minimum purchase requirement for one line rather than several, and therefore their commitment could potentially be going down? And how do you make sure that your space that you currently have on different levels or at different floors within department stores is not gobbled up by competitors? We are noting quite a significant increase in the mid price space for example.

Lastly, it's very reassuring to see that trading is off to a good start, but you say yourselves that this remains a very volatile market and hopefully it's also going to be off to a good finish. But I wonder what plans you have in terms of cost control that could help you through a continuing volatile market which seems to be on the cards? Thank you very much.

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Christopher Bailey, Chief Creative and Chief Executive Officer
So in terms of the curated we've been doing for over six months, we've done it in all three regions, so Asia, the Americas and Europe. And what that was really about is saying instead of looking at our customer through the eyes of our three labels, looking through the eyes of what the final customer wants to buy and what that market is right for.

So instead of having the parameters of the labels, we've been mixing the labels, so for example you may have a jacket that went down the runway next to a t-shirt that was from Brit because we're seeing more and more that customers are mixing all of those.

And this is actually being led by our customers because we know from the analysis that we've got that our customers cross all the different lines and they're shopping all the different lines. So instead of trying to force our customer to go into the lines that we've got, we're trying to say actually this is a curated approach for the right location, for the right customers.

And in terms of for the wholesale teams, you're right, it's absolutely a conversation about if you're on three levels today how can you go to a one level? And we're working very carefully. I just mentioned Saks Fifth Avenue, we've got a couple of examples where we've started to do that where it's in all of our interests to grow the business, none of us want to reduce the business in our Wholesale, and they are really partnering with us to make sure that we've got the right spaces.

This is really about long term brand consistency and also protecting the brand for the long term and making sure that we've got one destination for our customers where they see the whole world of Burberry instead of having to go to lots of different floors. And we know that the industry is starting to go in that way and we need the clarity. And it's not just the clarity for the customer. As you can imagine it will give us a lot of clarity internally. We have got a lot of duplication inside because of the way that we've got these three different labels, in terms of people, in terms of products, in terms of all the processes. So it's of course significant. It's primarily for our customer but will give us a lot more simplification and less duplication internally as well.

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Carol Fairweather, Chief Financial Officer
And then to your question on costs, you know you've seen what we've been able to do this year in terms of holding a very tight control of cost versus our plan and that's come through a headcount freeze, only prioritising very critical roles mainly in our Retail organisation through looking at all areas of T&E, other areas of discretionary spend. And looking at how, back to the productivity agenda, we can work in more efficient ways, be it working digitally as teams rather than flying people in and out.

So we'll keep very tight control over the short term, and our objective has been not to increase costs other than in those areas where we have chosen to prioritise investment. And you'll see that most of the cost increases in the first half came from investments in new stores and refurbishments. You know, as we look forward in the very short term a lot - about 70% odd of our costs are probably fixed given the fact it's in rents, depreciations, warehousing, etc. So we will be focusing on the costs that we can control.

We don't have a long tail of unprofitable stores for example which is why it's balancing really how much cost action we want to take depending on what our outlook is be it short term, medium term or longer term. And we've very dynamically managing that as a team in terms of at the moment we have protected marketing spend for example. We think that's absolutely the right thing to do and we've invested in Digital. We could choose if things slow dramatically to do something different, but we're having to manage through this day to day balancing the need to protect profits in the very short term with driving increased EBIT margin over the long term, always doing what's right for the brand. So I can't give you an exact answer but rest assured we're on it.

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Warwick Okines, Deutsche Bank
Three questions. Firstly back on the brand label rationalisation, is this strategically important in managing to capture more of your Wholesale space in the form of concessions, Retail concessions, or indeed is it just helpful if it's not a strategic priority?

And secondly coming back to the fixed cost comment you just made, were operating leases down in the first half, bearing in mind contingent rents may have fallen versus new space growth?

And thirdly a quick one, was Beauty margin accretive in Retail/Wholesale in the first half?

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Christopher Bailey, Chief Creative and Chief Executive Officer
So in terms of the label I think it's really important to just put the label change in context because we introduced the labels about nine or ten years ago. Nine or ten years ago we were a predominantly Wholesale business and we created the labels for that business. Today, so a decade later on, we're now 70% Retail. So we are predominantly Retail led which is why the label change needed to happen.

It's also about our Retail/Wholesale mix. It's about consistency for a customer. And it's also about simplification inside the company. But predominantly it's for the protection of the brand going forward. And we're not talking about any changes in marketing spend, but instead of having to market Brit, London, Prorsum, it's now Burberry. And that's a big deal as well because we know that we designed the labels for a Wholesale model, but today, because that mix is very different, it's exactly the opposite. We've now designed the company for the future.

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Carol Fairweather, Chief Financial Officer
And then to your question on operating leases, as we said we have had some benefit from lower rents in certain stores where we're on a variable element, but back to what was effectively the underlying cost increases in Retail/Wholesale it's largely come from new stores. So if you think about versus this time last year we've got the new Japan stores, we've got the Korea flagship just open, we have preopening costs in Galaxy Macau ,so there's quite a lot of fixed lease commitment which is why when you look at the net debt number you can see that net debt has actually gone up compared to where we were in March, but there has been some relief from the turnover rents in certain areas where we've had lower revenues and we're on variable operating leases. But net-net we've actually had an increase in terms of total lease commitment.

And then your comment on Beauty margin, nothing significant really to call out other than the fact that we have benefited from the inventory write off costs not recurring this year, and that was the most significant impact on Beauty. Other than that nothing really significant on Beauty margins impact on Retail/Wholesale to call out for the half.

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Julian Easthope, Barclays Capital
I've got three questions as well if I may. First of all clearly the luxury market does appear to be slowing currently, but do you think longer term there are going to be any

major differences between the growth rates of the different categories whether it's accessories or apparel, or whatever categories you want to define?

The second is really coming back to Digital and costs. There does appear globally to be - those companies that have invested heavily in digital to have seen much faster top line growth, but you actually have to pay for this through incremental costs, and yet the costs - I think most people were expecting to come to an end but they never seem to, there's continued investment. Do you think this is just a feature of the business longer term that these new ideas come up, you have to invest in them and therefore the underlying cost base will continue to rise?

And lastly in terms of Japan, Japan has been obviously a fantastic market this year. Does that actually reflect its way into rental costs? When you're negotiating for new sites in Japan, whilst you might be winning on Hong Kong are you losing on Japan because of the strength of the market? Thank you.

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Christopher Bailey, Chief Creative and Chief Executive Officer
So I'll take the first one. In terms of the luxury sector changing we're absolutely all of us seeing that. We feel that it's going certainly towards a more digitally orientated customer experience. That doesn't mean that bricks and mortar stores are not important, they are. The lines between those two though are becoming more and more blurred, and our customers are using mobile much more and using their mobile within bricks and mortar stores.

But just to talk about our opportunities, because we have just taken Japan in house over this summer, we see tremendous opportunity in Japan which is a very digitally led country, as well as the US where we - the US is our smallest retail country by mix, and again it's our number one digital country. So I can't overestimate how important Digital is for Burberry.

We also see at Burberry non-apparel having huge potential. You know when we see the world is getting warmer which every year we do, non-apparel is a much more seasonless category and we know that we've got tremendous opportunity there.

And then just in terms of our productivity of all of our existing footprints, whether they be Digital, Wholesale or our own Retail, we know that we have got a big opportunity there to expand on how we are more productive in those spaces. But our customers are much less interested today and going forward in whether they shop on their social media platforms, whether it's on a Burberry owned platform, what country they're in, currency, everything is becoming much more transparent globally. So we know that those changes are happening and we have got a culture within the organisation that is very aware of those changes.

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Carol Fairweather, Chief Financial Officer
And then just in terms of you asked about investment in Digital going forward I think, is that what you were asking? Yes so I mean as Christopher said Digital is so important,

it's fundamentally embedded right throughout our organisation so it's not just about the website itself, it's about how we continue to invest in digital marketing, how we invest in digital payment systems, how we invest in the website.

So within our ongoing guidance you know we see capex maybe moderating to something more like £150m as we look out for the next three years, and our Digital investment will be incorporated within that. So in the same way that we continue to look at how we need to prioritise investment, I think Digital is fundamentally embedded in our ways of working and we will continue to invest in Digital but always looking through the financial lens and making sure that we're getting the right returns, albeit they're more difficult to exactly evaluate versus a store proposal or whatever.

So it will just continue to be investing in opex and in capex in Digital, be it in making sure we've got the right Digital expertise in terms of mindset or be it within sort of capital investment in the site or payment systems or the single pool of inventory that we've talked to you about before; but always balanced within our overall investment portfolio if you like.

And then just back to Japan and rents there, I mean the market is hugely competitive. You know you'll know that we haven't yet got a store on Ginza, that's because we again have been balancing the right location, delivering the right returns, paying the right rents. That said we're delighted with the stores we have been able to open in Shinjuku and in Osaka, so we'll be mindful there's another one or two flagship stores we want to get in Japan but we're working with Pascal and the team to make sure we only do that at the right time, with the right location, adjacencies and returns.

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Christopher Bailey, Chief Creative and Chief Executive Officer
Maybe Julian just to continue on the Digital agenda, we've got an incredibly clear strategy on our Digital goals. We've got a very strong end to end consumer experience and we continue to invest in our Digital infrastructure. And maybe John you want to just say a couple of words?

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John Smith, Chief Operating Officer
Sure, yes thanks Christopher. Just adding a few points about Digital really. I mean at the moment Christopher mentioned we've been investing in our mobile experience for example, at the moment 45% of all of our traffic is coming through mobile which was a statistic unheard of a couple of years ago. And imagine therefore if we hadn't made that investment in mobile we wouldn't be able to get that traffic.

As you know we've been for years equipping our sales associates with iPads in store, every sales associate has one, and a good percentage, as you've heard us say before, 27% of our digital sales is coming through that investment. Imagine if we hadn't made it, and when we're out of stock in store of a particular size or colour if we weren't able to buy it off Burberry.com then we wouldn't be getting those sales. So I'm just giving these statistics to emphasise the fact that all of the investments we've made absolutely are paying back in terms of driving the top line, there's no question.

And because we've invested in the entire journey from the moment a customer ever first hears of us, we've extended our reach through things like Snapchat, Line, Kakao and all these other social platforms. Christopher mentioned a number of 38 million followers earlier. That number is 30% higher than it was this time last year. That's an amazing growth. Now again if we hadn't made that kind of investment it wouldn't happen. And also in the case of third party digital platforms like Tmall and Amazon, you saw in the release we've had double digit growth in that third party digital sales over the first half. So if we hadn't done all those then we wouldn't get the growth.

Now of course the costs associated with it are fully baked into our numbers and have been for a long time because we've been doing it for a long time. Of course we need to keep upgrading, we need to invest in new technologies, consumer technologies as well as software, things in store and so on, but essentially you see the economics of Digital fully baked into our cost base already. And as Carol has already said, we're not likely to see any significant rise in our capex from it so it's kind of already there now, so we're reaping the benefits of the investment that we've made essentially.

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Rogerio Fujimori, RBC
Christopher you haven't talked much today about men's, it's been an area of growth for the brand so could you comment on category dynamics and Burberry's performance?

And just to be clear on the US brand elevation strategy, what does it mean for your outlet footprint? Does it mean more Wholesale rationalisation? That's it.

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Christopher Bailey, Chief Creative and Chief Executive Officer
So in terms of men's there is not much more news to talk about. It's seen very similar trends to our women's business. We have seen an incredible uplift in our Heritage and our trench coats as well as our scarves. Non-apparel, we continue to grow that business and it's becoming a very, very important business. And in April of 2016 we're launching a new men's fragrance which will give us a real moment to put a spotlight on our men's business and as you can imagine there will be a lot of emphasis on men's, not only in the fragrance world but as we always do a very big halo effect across apparel and non-apparel.

In terms of the US, that is really about - and Donald is over there so maybe Donald will say a couple of words, but we have a real elevation project going on in the US. It is a very Retail driven organisation but as you will have seen we've been putting a lot of investment into our own stores. We just reopened Soho in New York very recently, Los Angeles - Rodeo Drive, San Francisco. We are working very closely with all of our Wholesale partners to elevate because we know the perception in the US has a long way to go, we know that we have got a lot of product opportunities there and it's a long term plan that we've got in the US.

Donald do you want to just say a couple of words?

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Donald Kohler, President, Burberry Americas
Yes I mean I would concur with Christopher. I mean Retail is our focus and we have been investing in the stores up through this year and we'll continue to do so as we go forward. In my first ten weeks I've been out to see a number of stores and we have still opportunity within our own Retail footprint. Wholesale will continue to rationalise where it's appropriate, but the focus is really on getting to the single destinations that we spoke about. And again we've done that very well over the course of the last year, so the best example was in Saks Fifth Avenue in Manhattan and then Nordstrom Vancouver. The outlet footprint will not change dramatically; we are still going after our originally stated strategy of fewer outlets, but potentially larger.

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Guillaume Gauville, Credit Suisse
Good morning everyone. Two questions, maybe the first one for Carol. I'm sorry; it's another question on costs. But if I look at your second half like for like guidance mid single digit, first half was 1% so let's say 2%, 3%, 4% for the full year it still seems to imply when you commented on PBT consensus in the trading update, it still implies a 100 basis point plus of cost deliverage. I ask the question again but have you worked out really what kind of like for like you need to actually avoid that cost leverage? I know some of your peers actually comment on that and it's "low single-digit is enough".

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Carol Fairweather, Chief Financial Officer
I'll take that one first. I mean you know clearly we've got many sensitivity scenarios that we run at different levels of revenue, understanding what the impact will be on margin as I said before. You know our focus right now has been on holding costs flat where we can, so not increasing costs in any discretionary areas. As you look forward, you know if you work out where we are at the moment we have said that we may not necessarily see margin accretion in this year, but we had already talked about that pre the slowdown we saw in Q2. We've taken rapid cost action as a result of Q2 in order to protect both profit and the margin as best we can.

And so we're relentlessly looking at all discretionary non-business critical spend right across the business, and then we're also looking at ways of working and how we can, under the productivity agenda continue to maintain costs, and as we grow revenue under the productivity agenda as well that's what will drive the margin accretion. But right across the business, from every area I would say right from design through to finance at the back end, we've been really rigorous about holding costs and only prioritising investment in those real key areas mainly around marketing, technology, product development that we believe will drive that growth in the future.

So a very different mindset I think over the last six months in terms of the approach to costs within the organisation, and as we look forward that will enable us to manage as best we can whatever the outlook looks like. And as I said earlier to Luca, it really depends on what view you take on short, medium or long term growth. And at the moment we're very much managing to the short term while balancing still long term investment in those areas that we believe will drive long term brand appropriate growth.

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Guillaume Gauville, Credit Suisse
Right thank you. And the last one maybe for Christopher, I mean you have been CEO now for more than a year so maybe just could you tell us what were the key highlights, the key challenges over the past year and how you look ahead in the next year?

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Christopher Bailey, Chief Creative and Chief Executive Officer
Being here.

Laughter

This is the highlight. Yes I mean it's quite - you know I've been with the company for 15 years and my role has - I feel every six months my role evolves and changes. You know what I feel fortunate about, and I hope you've had a chance to meet many of them, is that I continue to work with the best, most talented people not only in our sector but across many different sectors, and we continue to bolster that team. I hope you'll have a chance to meet Leanne Wood and Fumbi Chima, two new people in our senior team.

So we continue to invest in people, we continue to look at different ways of working. And my role is about making sure that we have a strong vision, a strong strategy, that we continue the innovation and creativity that has made the company successful to date whilst being very responsible about the way that we run the company. And you know continuing to have fun like days today.

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Guillaume Gauville, Credit Suisse
Thank you very much.

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Annabel Gleeson, Redburn Partners
A very quick one I promise, on opex again I'm afraid. But when you've talked about you know getting rid of Brit, London, Prorsum, you said that there is some duplicality between what you're doing. Should we think of this as an opex opportunity? Are you going to kind of look at restructuring how you're maybe managing the whole organisation?

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Carol Fairweather, Chief Financial Officer
No, I mean as Christopher said earlier I mean this was very much about responding to the fact that we've become more of a Retail business, to the way in which consumers like to shop. That said, under the productivity agenda we're looking at ways of working

right across the organisation, across a number of different initiatives about how we become more focused, simplified, more effective as an organisation. So nothing specific in relation to this particular initiative, but it will reduce complexity, allow for some simplicity and that absolutely sits alongside all the other initiatives we're looking at - it's really about how do we become a more efficient organisation, how do we change our ways of working.

We've grown rapidly. We're at a slightly different stage now and that's why we have this intense focus on both optimising the top line, making our stores more profitable, and how do we really now make sure that we control costs, prioritising investment and becoming much more efficient in terms of ways of working as an organisation, right across the organisation.

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Annabel Gleeson, Redburn Partners
Thank you.

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Christopher Bailey, Chief Creative and Chief Executive Officer
So I just want to say thank you very much indeed for joining us today and for giving us the opportunity to just talk a little bit about the current context and our reactions to what's happening, but also to give us a chance to talk to you a little bit about the future and all the growth opportunities that we've got ahead.

Just going back to the present, it is coming up to Festive; it is our biggest trading season. You've all got the book of gifts on your tables, we can take orders today or you can go online or into any of our stores. But to get you in the spirit we are going to share with you the ad campaign, the film that we've done for Festive, that has had an incredible response. So thank you very much again and here's the Festive film.

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