Burberry

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Julie Brown, Chief Operating & Financial Officer

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Questions From

Unidentified Analyst

Helen Brand, UBS

John Guy, MainFirst

Edouard Aubin, Morgan Stanley

Thomas Chauvet, Citigroup

Melanie Flouquet, JP Morgan

Rogerio Fujimori, RBC Capital Markets

Zuzanna Pusz, Berenberg

Introduction & Highlights

Marco Gobbetti, Chief Executive Officer
Good morning everyone. Thank you for joining us today for Burberry's Preliminary Results presentation.

Before we begin, I would like to say a few words about our Chairman, Sir John Peace, who is sitting here with us. As you will have seen from last month's announcement, Sir John will be stepping down from the role and from the Board after the company's Annual Shareholder Meeting on the 12th of July.

On behalf of the Board and everyone at Burberry I would like to thank Sir John for his immense contribution to the business and as Chairman for the past 16 years. Sir John has presided over a period of extraordinary change, leading Burberry's evolution into one of the most valuable luxury brands in the world. Thank you Sir John.

Applause

At the same time we bid farewell to Christopher Bailey and I would like to take this opportunity to acknowledge, once again, his tremendous contribution to Burberry. Christopher leaves an incredible legacy and strong foundations on which we can build the future of the brand.

As we communicated, Dr Gerry Murphy has now been appointed to the Board as Chairman Designate. He will start tomorrow and will succeed Sir John after the AGM. In Dr Murphy we have found a superb candidate, with extensive experience in the consumer and the retail industries. I am delighted that he will be leading the Board and I am really looking forward to working together as we implement our strategy.

In terms of our agenda for today, Julie will start by covering our financial results and guidance, as well as operational excellence. After this I will give a brief update on our strategic progress and close by taking any questions you have.

I'll begin with a few words on our results. In line with expectations Group revenue is up 2%, adjusted for Beauty, with comparable store sales up 3% and adjusted operating profit up 5%.

Overall, in the context of a buoyant luxury market, this was a good year and these results represent strong execution through a period of transition. Customers responded well to our innovation in product and our conversion improved as we focused globally on retail excellence.

Our top customers increased their spend and our Digital channels performed well.

We have also seen some encouraging early signs of the new strategy, which I will come back to later.

Given the scale of our ambition for the brand and the significant amount of change in the business over the last 12 months, I believe these results mark a positive start as we implement our strategy in the coming year. And with that, over to Julie.

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Financial & Operational Review

Julie Brown, Chief Operating & Financial Officer
Thank you Marco and good morning ladies and gentlemen. We have dedicated considerable focus this year to improving execution and exercising financial discipline and we're encouraged by our positive results for the year.

During this presentation, unless otherwise stated, I will refer to constant exchange rates. So revenue was £2.7bn, up 2% adjusting for the Beauty deal. Including the impact of Beauty, revenue was down 1%.

Adjusted operating profit was £467m, up 5%, and our operating margin improved 110 basis points at CER.

Adjusted diluted EPS was up 10%, positively impacted by tax and share repurchases. Free cash generation was strong at half a billion pounds. And return on invested capital increased 90 basis points to 16.3% at reported rates.

And finally, we announced a full year dividend of 41.3 pence, up 6% in line with our policy.

We closed the year with net cash of £0.9bn after £0.5bn of share repurchases and dividends. And we have announced a new buyback today of £150m to be completed in full year '19.

So this slide shows the changes to our revenue by channel and first I'll give you more insight into our Retail business performance. So Retail grew 3%, with comparable store sales growth of 3%, split 4% in the first half and 2% in the second.

Growth was led by volume and underpinned by conversion, improving in all regions and supported by retail excellence initiatives, which Marco will cover in more detail later.

Space was broadly neutral in the year, with our strategic store closures beginning in the fourth quarter.

Wholesale, excluding Beauty, was flat, reflecting our initial actions to reduce non-luxury doors, and that said, we were ahead of guidance due to higher levels of in season orders in the second half.

Licensing grew 21%, benefiting from Beauty transitioning to a license model, offset by reduced royalties from some of our other agreements. The total business, excluding Beauty Wholesale, grew by 2%.

In terms of the regional growth trends looking at Retail and Wholesale performance in the full year, Asia Pac was our strongest performing region with 5% growth in Retail/Wholesale and a mid single digit comparable sales growth.

Mainland China delivered a high single digit comp and Hong Kong returned to growth in the full year, positively impacted by both local and tourist spend in the final quarter. The Chinese consumer, our largest nationality globally, grew mid single digits in full year '18.

EMEIA grew 1%, with comp sales unchanged. The first half was stronger than second as we expected. The UK was impacted by some exceptional prior year comps due to Brexit and closed the year with a low single digit growth. Continental Europe was impacted by reduced tourist spend in half two. And Wholesale in EMEIA was broadly stable.

And finally, our business in the Americas declined marginally with two major factors to note. Firstly, we saw encouraging Retail trends in the US, with growth returning in half two as our retail excellence initiatives delivered positive conversion and traffic improved through the year. For the year as a whole Retail comp was up low single digits.

Secondly, we initiated planned changes to distribution in line with our strategy, the consequence of which was a high single digit percentage decline in Wholesale.

We have been evolving our business model towards Retail and now following the Beauty transaction over 80% of our sales are derived from our own directly operated stores.

Looking at this by product, this chart shows our Retail and Wholesale performance combined; therefore growth rates are somewhat depressed, by the inclusion of the Wholesale business.

In mainline stores customers responded really positively to seasonal updates and innovation. The highest growth product category was in apparel, with men's at 4% and women's at 2%.

Our focus on outfitting the customer drove strength in tops, skirts and trousers in the second half.

And in April 2018 we've refreshed our Heritage trench programme, updating the style, streamlining the colours and further enhancing our most iconic product.

Accessories grew 1%, with strength in small leather goods. In March this year we began our leather transformation and with the first of our strategic bag launches, the Belt bag, and we're very pleased with the early response.

This slide shows the major components of our income statement. Gross margin improved at constant currency, benefitting from an improved Beauty margin and positive channel mix, partially offset by higher inventory charges year on year. At reported rates gross margin declined 50 basis points due to a currency headwind.

For the full year adjusted operating profit grew 5% CER, 2% reported, and our margin improved to 17.1%, which I'll return to later. Adjusted operating items totalled £57m, largely due to restructuring charges relating to our cost efficiency programme. These total £54m this year and we maintain guidance for cumulative costs to reach £110m by full year '19.

Adjusted EPS was ahead of profit, due to the combined impact of an improved tax rate and the accretive impact of the share repurchase programme. Our tax rate improved 70 basis points on the previous year to 25.1%.

Then let me summarise the improvement in our operating margin in more depth. So firstly the cost savings programme delivered ahead of plan, with savings of £44m in the year, bringing cumulative benefits to £64m. And we're now over half way through our commitment to deliver annualised savings of £120m by full year '20.

Secondly, we benefitted from improved profitability from Beauty and channel mix. However, during the year we continued to face upward pressure on the cost base, due to property and manpower inflation and inventory charges.

And finally we made strategic investments in technology, in digital, retail excellence and leadership initiatives.

So now turning to the cash flow, the business remains strongly cash generative, with £484m of free cash flow and cash conversion at 128%.

A few key points to call out, working capital improved as fashion inventory reduced by 5% and receivables decreased following the collection of debtors from Beauty.

Capital spend was similar to last year at £106m and this was lower than we guided due to the phasing of projects. Capital investment will step up in the coming year and I will return to this in the guidance.

This slide shows the movement in cash during the year in line with our capital allocation framework. We generated free cash of £590m before capex, and in the year the main outflows related to capital expenditure, our dividend, and the buyback programme.

We returned over £500m to shareholders by way of the dividend at £169m and the buyback at £355m. We received a one off inflow from Coty of £150m, including £30m for the inventory transferred. And in total our net cash at March 2018 was £0.9bn, or on a lease adjusted basis net debt of £0.3bn.

Turning to guidance, in November we explained that our transformation has two important phases. First we expect a period of transition as we rationalise distribution and invest to reenergise the brand. And we believe this period of investment will enable us to deliver long term sustainable value. In the second phase, we expect growth to accelerate to high single digit revenue growth and a meaningful improvement in margin.

In full year '19 therefore there is no change to the broadly stable revenue and margin guidance issued in November.

Taking revenue guidance first, our actions to improve distribution will impact both Retail and Wholesale revenue. For Retail we expect a minus 1% impact from space as we evolve the store network. And secondly for Wholesale we expect a low single digit decline for the full year, with most of the impact being felt in the second half.

Regarding other items of guidance we're on track to deliver £100m of cumulative cost savings and expect cumulative one off charges of £110m as we previously guided. Earnings per share is expected to benefit from a continued reduction in our tax rate by 100 basis point to 24% and the commencement of our share buyback programme.

Capital expenditure will increase to £160m to £170m as we improve our store network in a number of key markets, including relocating a number of our stores in China and continuing to invest in digital and technology.

Regarding foreign exchange, as usual, we have run our model at the end of April spot rates. This implied a negative impact of £45m on revenue and £40m on profit compared with the prior year. However, since the month end currency has moved slightly in our favour and reduced the profit headwind to closer to £30m to £35m. Do note that this could reduce our operating margin by around 100 basis points in the coming year on a reported basis. And to help with modelling through the year we have included a high level sensitivity analysis in the appendix.

You will have seen the announcement earlier this week for the acquisition of our leather goods business in Italy. We expect payment to the vendor to be up to €26m, of which €15m will be paid on completion, and the balance will be paid over the following three years. We expect no impact on adjusted operating profit guidance for full year '19 or full year '20.

Finally, a note on disclosure, in our drive for simplification we are moving all functions in the business to a single retail calendar and this includes the statutory reporting calendar. So from the 1st of April 2018 we will make this change. There will be no material difference to comparability in the full year, but there will be small quarterly differences due to sales days and these are explained more fully in our appendix.

So this concludes our financial review and I'd like to just summarise. Our results in 2018 are in line with forecast, the cost savings are ahead and we have very strong free cash flow. 2019 is expected to be in line with the strategy that we announced in November. And we continue to focus on maximising longer term value for our shareholders at a time when the outlook for Burberry and the luxury sector more widely continues to be very attractive.

Now I'd like to turn to strategy and a few words on operational excellence before Marco reviews our strategic progress more broadly.

So operational excellence is changing the way we work in Burberry and over the past two years we have simplified our operating model, we've launched Burberry Business Services, we've delivered significant procurement benefits and we've delivered major change programmes in supply chain and in IT.

And as an example I'm proud to update you on the progress we've made with Burberry Business Services. We identified the building in Leeds this time last year. We went live in October with five major functions, finance, HR, procurement, IT and customer service. We received over 12,000 job applications and have now recruited a fully-fledged team of several hundred people, taking over major processes and benefiting from true cross-functional working.

And the benefits from this are just beginning as we're now at the stage of implementing Lean Six Sigma as a way of working to remove duplication in our processes. Our procurement team have also delivered a record level of savings across major categories of spend. And with a further 20 projects in the pipeline we expect to release more value in the coming year.

As mentioned we've now delivered savings of £64m and are on track with the £120m annualised by full year '20.

But stepping back from individual projects we're also working hard to build a culture of simplification, agility, efficiency, and discipline across our business, which will be critical to underpinning our strategy. And with that I'm pleased to hand back to Marco.

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Strategic Progress

Marco Gobbetti, Chief Executive Officer

Thank you Julie. I'd like to take a few moments now to update you on our strategic progress. Last November I shared with you our strategy to reenergise the brand and inspire the luxury consumer. The recent changes in our sector and the ever evolving consumer confirmed that we have the right strategy in place to deliver sustainable long term value.

As you know our strategy has six elements. We have the opportunity to drive revenue through evolving our product, communication, distribution and digital. Underpinned by our work on operational excellence and inspire people.

Over the last six months we have focused on strengthening our foundations to deliver the strategy. We are still in the early stages of our transformation, with the majority of change still ahead of us. But so far I'm pleased with the progress.

I'd now like to share with you a handful of key insights. Firstly, I wanted to say a few words about Riccardo whose creative vision is at the heart of our strategy. I believe Riccardo is one of the most talented and influential designers of our time. His designs have a contemporary elegance and his skill in blending streetwear with high fashion is highly relevant to today's luxury consumer.

He brings expertise across categories, including womenswear, menswear, leather goods and accessories. Riccardo also embraces the British spirit that is at the heart of Burberry and he's excited to nurture it.

Since he arrived a couple of months ago Riccardo has already formed great relationships with the teams across the business. He has embraced Burberry's icons, and as many of you will have seen, styled a series of looks celebrating essential pieces such as the Heritage trench coat and the cape. You can see some of the images here which were released on Instagram last week.

As you know product transformations take time. We expect the majority of Riccardo's product be delivered by May or June next year, with the arrival of our autumn/winter collection. Of course in the meantime we will continue to have exciting launches and we will be mindful of managing our inventory as we undertake this transition.

We are all very excited about this new era for Burberry and I am personally really enjoying working together again with Riccardo.

Over the past few months we have been making good progress in the way that we deliver product and interact with our customers. We are still at the start of this evolution, but have begun to deliver frequent fresh product drops and capsules, continuously engaging customers with newness and excitement.

A good recent example of this is the February Runway capsule. Let me highlight three things on this. Firstly, it was tighter and more productive than previous capsules. Instead of making all our Runway product available for immediate purchase after the show, as we have done in the past, this year we tightened the offer, sending a highly edited, strong fashion message to the consumer, whilst delivering triple digit revenue growth by option.

Secondly, we see this as the natural evolution of our go to market strategy, answering customers' desire for newness and innovation, with frequent, even unexpected product drops. It's a new way of working for us and one we will continue to develop going forwards.

Thirdly, in terms of customer, the February capsule both attracted new young customers and resonated well with our existing top tier clients. In line with our strategy it achieved higher than average outfitting rates, with customers buying complete looks.

Of course the capsule is a small part of our overall product offer and the majority of the product transformation is only just beginning now with Riccardo onboard. That said, it is an encouraging sign.

Also from the world of product we have begun to transform our leather goods. We have created a new handbag architecture around a range of customers, end uses, and silhouette preferences, whilst ensuring value is perceptible. You will have seen some of the newer handbag styles already in stores and you can expect more innovation to arrive over the next few months when we will be refreshing some of our core shapes and launching a number of new styles.

Earlier this week I was delighted to share the news that we have entered into an agreement to acquire a business from one of our long standing Italian partners, CF&P. Based in Florence in an area renowned for high quality manufacturing, CF&P has industry leading expertise and specialises in the development and manufacture of luxury leather handbags and accessories.

With this acquisition we will create a new centre of excellence for leather goods, covering all activities from prototyping, product innovation, engineering and the coordination of production. It will also give us greater control over quality, cost, delivery and sustainability.

CF&P employees, including the team of expert craftsmen, who have worked closely with us for more than a decade, will transfer to Burberry upon the completion of the transaction later this year.

This is a significant milestone for us and will create a strong foundation for our leather goods strategy.

We have also started to evolve the way we communicate with our customers. And I am now going to show you a quick video that brings to life the changes we have made so far.

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Video Played

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Marco Gobbetti, Chief Executive Officer
As you can see we have had some exciting new collaborations across creative, product, and experiences this year and evolved our voice across social channels and on burberry.com.

Of course with a new designer now onboard this is a major area of focus and we will reenergise our creative and visual language in line with his vision.

Moving to how our customers experience the brand physically, there are two key elements, the shape and quality of our network and the service within each of our stores. Both of these elements are important and take time. While the evolution of our overall network is a multiyear project, on service we can, and have already, started making changes.

I have asked Gianluca Flore, President of our Americas region, to lead the work on service and retail excellence globally. And we have now prioritised a number of immediate measures, including introducing a Global Retail Leader's programme, testing a new digital client-telling tool with improved functionalities across client service, product information and after sales and rolling out merchant led product training across our network.

We are also piloting a new approach to how we interact with customers, touching everything from how they are greeted when they walk through the door to their experience after purchasing.

While I was travelling in Asia last month I spent time with our team in our Kerry Centre store in Shanghai, one of the locations where we are piloting this new approach. And it was great to hear how excited the teams were about our new ways of working and to see how the changes are making a real difference to our customer.

Clearly we are just at the early stages of this transformation, but partly due to these efforts in retail excellence, as Julie mentioned earlier our Retail metrics for the year have shown some promising signs. Mainline conversion improved, we saw significant business from appointments with higher conversion and ATV in these sessions. We were also pleased to see increasing spend from our top tier clients.

Turning to the shape of our distribution, we're well on track with the first stages of our plan, focusing on three areas. In mainline we are refining our portfolio in line with the strategy, closing a number of smaller stores in non-strategic locations and investing in stores in high visibility influential fashion markets.

One example of this is our new Middle East flagship store which will open next month in Dubai. And over the coming months you will start to see more changes to the look and feel of our stores.

In Wholesale we launched a number of successful partnerships with image driving wholesalers such as Dover Street Market where this image was taken.

In the US we continue to have good conversations with our Wholesale partners, who are supportive of our strategy and are progressing well on evolving our distribution.

The impact of our Wholesale transformation will begin to be visible later on this year.

And turning to our outlets, we have confirmed the closure of a net six outlets, including three in the Americas, in line with our plans.

As you know digital innovation is always at the forefront of our plans at Burberry, we recently launched our collaboration with Farfetch around the February show, with our global inventory now available through the platform, expanding our distribution to more than 150 countries and extending our reach. And the results so far have been well ahead of targets.

We are also working with Farfetch to identify the next wave of technological advance for the industry, as the first brand to partner on the new Dream Assembly programme.

Before we turn to questions I wanted to end with a few points about our people. With new leadership in place we have taken the opportunity to simplify our governance and clarify accountabilities across all commercial and creative functions. As part of this work, we have created the new role of Chief Commercial Officer, responsible for all our regions and reporting to me. I'm delighted to have welcomed Gavin Haig into this role. His wealth of experience in luxury retail is a major asset as we drive forward the strategy, particularly in the transformation of our distribution.

Over the last year we have also continued to strengthen our wider leadership population. We have filled a number of very senior positions across the business with internal candidates and enhanced the Group by bringing in external expertise and fresh thinking. In total around 40% of our vice president and above population is new to role in the last 12 months.

It is a great testament to the talent and commitment of our people that we have accomplished so much during this period of change. I am continually humbled and inspired by the passion, energy and dedication to the brand that our people have here at Burberry.

So to summarise, over the last six months we have focused on strengthening our foundations to deliver the strategy and we have seen some promising early signs. Our progress so far gives me confidence that we are building the right platform for our full brand transformation. And we remain on track with our financial expectations.

There is a lot to do and we are far from complete, but we are all very excited and energised for what is ahead. And now I'd be pleased to take your questions.

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Questions and Answers

Unidentified Analyst
[Inaudible audio too faint] … side, whether you plan to be increasing prices and according to what format; impotently, if you could tell us what you plan to do on pricing in leather goods and whether you continue to see Burberry as a price follower in that area? Thank you so much.

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Marco Gobbetti, Chief Executive Officer
So starting from the distribution side, clearly we have laid out in our strategy an elevation strategy of distribution per area, per region. There are some regions where obviously there is more work to do, we called out America, where, particularly on

Wholesale, we have consolidation that we are in the process of working on with our partners.

The good thing is that the partners, they really see what we are doing and where we are going and they are really, really, really keen to partner with us. So I think that we have had very good conversations from the beginning with them. We are laying out detailed plans and so I'm really confident that that will be - actually it will become an asset for us very soon.

In terms of America and in terms of Retail, there is always, like in every other country I would say, there is an upgrading to do in certain areas. But overall I would say that the quality of our Retail presence in the market in terms of our stores, our physical stores in the market, is very strong. We have - obviously the look and feel of the stores that is going to be an important part of the elevation of the brand. But in terms of the physical stores I think we're quite satisfied there.

In Europe it's a slightly different situation where again in terms of Retail network I think we have a strong Retail network, there are obviously some opportunities to improve that we always try to capture, but in general it's good. And we don't have the same issue that we have in America with Wholesale distribution.

And in Asia, you know we've spoken last time about Japan, clearly Japan is a little bit behind for the history that we have there, but we're catching up very quickly there. I think we're very pleased with the plans that we have ahead and the discussions with department stores, similar to the discussion in America about expanding and increasing our presence there. And again in terms of Retail in Japan we have a good network.

In China we have done and we are doing a number of operations to improve our presence in certain malls, or in certain areas where we have opportunities. So from that point of view I think from the Retail side it's going to be about upgrading where there is opportunity and refreshing clearly the look of the stores.

In terms of product and pricing, I think we explained that the strategy also sees the completion of the movement from three labels to one label, which clearly in terms of product will have some effects in terms of certain categories where prices will be more precise and within a smaller band than before.

In terms of leather goods, which is an important point for us, we have the opportunity to strengthen our offer in the top of the range, which is the range where we play with our Belt bag, which is the first example of that strategy. And there clearly the purchase of our leather goods partner there, creating this centre of excellence, creating the brain from where the whole strategy and development and creation of our leather goods will happen I think is going to be very important for us.

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Helen Brand, UBS
A couple of questions from me. Firstly you talked about the new product drops in May and June time, outside of the leather goods, what do you think the key product categories that you'll be focusing on for reinvigoration might be?

Secondly, maybe one for you Julie, the H2 gross margin looked quite weak, down almost 200 bps on my back of the envelope calculations. I was just wondering if you could talk through the drivers behind that H2 gross margin and particularly talk to the inventory provisions that you've taken within that as well?

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Marco Gobbetti, Chief Executive Officer
Should I start with the categories and the product drops? As we said our strategy of going to market is going to be about frequent deliveries, and frequent deliveries and product groups clearly are going to cover all of the categories that we consider fundamental for us.

We have already started actually even before May and June which is the delivery of our Fall collections, that delivers over three or four drops, we have had the refresh of our Heritage trench coat programme, which is very, very important for us and which started in April. We will have Gosha, the second capsule of Gosha that will also deliver in the beginning of July.

So this project of continuing with frequent deliveries is something that is really, really important for our strategy and will continue across category. You know handbags, as we said, we are building an architecture of handbags and around there, there will be continuous evolvement of product, new products, animation and updating of existing products in the offer.

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Julie Brown, Chief Operating & Financial Officer
Okay so the question on the gross margin. Obviously for the full year on a like for like basis at constant exchange rates the gross margin has improved. It’s the exchange effect that’s pulling the gross margin down by 50 basis points for the full year.

And then you mention the second half specifically. The second half has been impacted by inventory provisions that we’ve taken. Clearly we’re going through a creative change at the moment in the transition from Christopher to Riccardo and therefore we’ve looked at the product lines in particular, and we’ve made some provisions against stock levels that we anticipate being there going forward.

So that has really changed the gross margin or lowered the gross margin in the second half. But on a like for like basis constant currency the margin for the full year is better.

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John Guy, MainFirst
If I could maybe just go onto the recent acquisition, the leather manufacturing acquisition that you've made. If I think about total internal manufacturing I think is probably low double digit for you at the moment so roughly around 10%. Are you planning to increase your level of in-house manufacturing? Is this first acquisition that you've made now in leather goods the first of many? Is there going to be a step change here or are you selectively targeting certain areas within the business?

And secondly one for you Julie, just on opex, down around 10%, £70m or so; what was or can you quantify the Wholesale Beauty related cost effective dropout that we’ve seen in the second half of the year, because that’s clearly quite a big slug and I assume that’s a one off? Thanks.

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Marco Gobbetti, Chief Executive Officer
Let me answer first on the leather goods acquisition. The aim we have in our strategy is to develop those skills that are strategic to the achievement of the strategy. And in leather goods the skills of pattern making, prototyping, developing, industrialisation, coordination of production, those are the key because they complement and they complete our creative skills in design and talented design. So having synergy across those two very important centres of excellence is really what will deliver I think additional value.

We don't think in terms of controlling a certain percentage of production directly okay. But we certainly think which are the strategic areas where we need to be integrated with those skills that are essential. I remind you that in Yorkshire we control all of the production of our trench coats and the weaving of the gabardine for the trench coats. So those we think are really critical skills for us.

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Julie Brown, Chief Operating & Financial Officer
Okay, so taking the other part to your question. So we have had a benefit this year in terms of the change in the Beauty business and the license to Coty so clearly there was marketing spend going through previously in Beauty. So we'd anticipate, because we did the deal at the half year essentially we'd anticipate some benefit from Beauty in the first half but not as much as we've received this year, just because of the phasing of the spend, it tends to be more Christmas orientated. So the biggest savings being in this year versus next.

Even if you strip out Beauty you know basically our profits were still growing so it's been a contributor this year, but not the only contributor because the cost saving programme has been also really important to us this year.

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Edouard Aubin, Morgan Stanley
Just two questions from me. Just coming back on the leather goods - bags, so as you mentioned you've launched in March and April the Belt and the Bucket. Can you just elaborate if you are happy with the reception, the sales so far? I know it's very early days. And to what extent Riccardo Tisci going forward will be involved with the category himself into the design? And what he did at Givenchy in terms of the bag category specifically?

And my second question is on online. You are one of the most distributed brands or luxury brands in platforms in Europe and Asia, either you selling directly on YNAP or Tmall or some resellers are selling on these platforms. Is that an issue for you and do you think you have a good enough grip on your distribution online in these two regions, Europe and Asia?

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Marco Gobbetti, Chief Executive Officer

Okay. In terms of the handbags and the launch of Belt, the early days are quite encouraging. I just tend by nature not to get overexcited about this because I think you have to see the stamina over the long term of a handbag of that sort because it's a classic, it's a pillar - can become a pillar for us as a handbag. So I don't want to judge it on a very short period of time but the beginning is encouraging. And it's very encouraging because it's being bought by top tier clients, existing clients as well as new clients; it's being bought across the regions. So early signs are fairly good.

Riccardo is going to play a part in the accessories, an important part in the accessories. He has already started working a lot with Sabrina, our head of design in the accessory area. They work very well together and they have actually too many plans and too many ideas that we'll need somehow to trim in order to get to market with all of those.

So I think that from that I think we're very excited and I think that we have obviously a huge opportunity in that area. And Riccardo is somebody that has demonstrated already his capacity, not only handbags but in other accessories, small accessories, costume jewellery, shoes, very important category, not today but can become in our mind a very important category going forward.

The second part of your question about digital, well I think - the important thing is not the number of partnerships you have, it's the quality of the partnerships you have. And I think we have frankly I think probably some of the best partnerships in the industry, because we have been early adopters, early supporters of the big important platforms. And we are perhaps a little bit ahead of the rest of the pack in terms of the quality, also of the partnership. The Farfetch agreement is an example of that. When there is innovation, when there is a possibility to make it qualitative, controlled, we always try to be first and do it with our partners. So it's actually a great leverage for us and we're very proud and very happy to continue there.

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Thomas Chauvet, Citigroup
Two questions. One on outlets and one on cost. Marco on outlets as you're aiming to elevate the brand you've indicated you would close some outlets. You've closed seven I think, last year, if I understood correctly there'll be six closures in the current fiscal year. Can you first indicate whether this channel has been quite profitable for you over the last year or two? It is the case for some of your peers and they're growing very fast in this channel. And would you be able to share, given this is probably going to come down from here, the weight of Retail sales generated in outlet for the fiscal '18?

And secondly maybe a question for Julie on cost. In the past you said that Burberry would have a typical underlying constant FX cost inflation of 5%, but that over time you would aim to bring it down to 3% or 4%. When you look at the wages and rents, two key items in your cost base and their evolution in the next couple of years, what kind of underlying inflation are you expecting in the transition period FY'19/'20? Thank you.

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Marco Gobbetti, Chief Executive Officer
So on outlets, you know, first of all you know we don't disclose the percentage of sales of outlets and we're not going to disclose them going forward. But I think I've laid out in the strategy the importance that the outlet activity has for us. So I made very clear that we are going to continue to use this network of stores to exit the inventory that will

remain at the end of every season. So there's a physiological need to have these outlets and they are very useful from that point of view.

What we are doing, the net closures, which are six I believe this year - net, they correspond to the rationalisation of the network. There are some areas and some outlet centres that are not important or interesting for us anymore and we close them. In the same way that I described in the mainline we're really focusing on what matters and trying not to disperse our energy into smaller, lower activities that - of Retail, whether it's outlet or mainline.

So this is really where you will see it and you will see continuing but it's not going to mean that there will be a major shift in the outlet strategy. But certainly there will be some adjustments there.

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Julie Brown, Chief Operating & Financial Officer
Turning to cost. So the first thing is we've mapped all the costs in the business in terms of characterising how they should behave when sales are moving. So from marketing all the way through to all the admin costs. So we've fully mapped them and they're owned in the accountable structure that we've got in the business.

In terms of inflation on the cost base there are two major areas where we see inflation coming through in the cost base. One is the manpower cost and clearly we've got - our largest region is Asia so there is pressure, upward pressure on the manpower cost through inflation. And also the lease cost base relating to our stores.

So when you take that all into consideration we'd expect to see a growth rate on that of around 4% to 5% and including investment it will probably be at the higher end of that range. Without some of the investments we're making it would be lower

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Melanie Flouquet, JP Morgan
So I have three questions but they are quick. The first one is regarding the transition period. I was wondering whether you could share with us a bit how you are going to manage it, because the last collection of Christopher Bailey seems to have had a great resonance to its core traditional consumer base and even younger consumers as you said. So do you contain the inventories to make sure that people invest in your collection and the new designer? How do you manage this transition with a pretty successful collection just done? And also linked to that sorry, will you have capsule collections already marked by Tisci before the May to June drop in 2019? That's my first question.

The second question is I'm a bit surprised because, and maybe this is a stupid question, but usually we have a lot of people from the management team present today, and today we have only the two of you and Charlotte today. So I was wondering is this a sign of a change of the way you are going to communicate? Is this a sign of a change of a more centralised management? So whether you could share with us because usually we have a crowd of people around.

And my last question is on inventories, it's really a quick one, promise. Just whether the inventory provision - how sizeable is it? Was your gross margin actually up excluding this underlying in H2? Thank you.

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Marco Gobbetti, Chief Executive Officer
Okay. In terms of the transition and in terms of the February collection I think we are actually fully embracing the February collection which was a very strong collection. And we have - as you know we have launched and we discussed it before a capsule, readily available the day of the show, and that has performed extremely well. And we are going to be delivering the rest of the collection across the normal delivery time which is from mid July - from July until the end of September. So we are going to carry through with our normal course of delivery and collections.

Riccardo's first collection is going to be at the Runway that you will see in September, and the Runway starts delivering in February of next year. So when I refer to May or June I mean that by May or June we will also start delivering fall which will have been designed by Riccardo, and at that point we will start to have a more complete offer, not 100% complete but a much broader offer of products that will have been designed by the new creative team.

In terms of the management being here, I think there is no message to be had. I think there are a few scattered members of the team here and it doesn't mean that we're going to be more centralised at all. I think we have collectively - I think the team is doing a fantastic job. I'm really proud as I said of what they have accomplished this year and we are totally transparent as you know with our team and the members. Gavin would have been here but he's already in Asia and he's working and has been travelling. So no nothing, no message to pick up there.

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Julie Brown, Chief Operating & Financial Officer
No they're just working.

Laughter

So coming back to the point about the inventory. So when you look at our accounts you'll see that the inventory provision level has risen. So we normally operate on the basis of about a 15% provision. It's increased to an 18% provision. So there's an element of inventory charges which are really linked with the creative transition when we're looking at the stocking levels, and so we've got about an extra charge of £14m in the accounts relating to that this year.

I think as Marco said we will obviously do the buys. When we do the open to buys we'll do them tightly and we'll manage the inventory as we go through the year and the transition from Christopher's collection to Riccardo's in a very pragmatic way. And that's all been built into the guidance that we've given for the year. So we'll manage this very pragmatically as we go through.

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Charlotte Cowley, VP, Investor Relations

I think we've just got time for a couple more so if we take Rogerio and then Zuzanna. Thanks.

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Rogerio Fujimori, RBC Capital Markets
May I ask a question about the millennial segment or the younger clientele, how do you see the brand performing in this younger age group? An idea of how much it accounts for total global sales perhaps, particularly in Asia, and is it changing?

And my second question is on handbags, how it performed in the second half? And within accessories is it still about half of your total accessory business? Thank you.

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Marco Gobbetti, Chief Executive Officer
Sorry the last part of your question was?

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Julie Brown, Chief Operating & Financial Officer
Handbags.

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Rogerio Fujimori, RBC Capital Markets
How it performed in the second half or Q4 and is it still about half of your total accessory business? Thank you.

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Marco Gobbetti, Chief Executive Officer
In terms of millennials, clearly millennials is - the age of our customers is one way to analyse and to plan how we and what we market to our customers. It is a way and it's an important analysis, but in our opinion it's not the only one. In fact there are a number of elements, even within a category, that define how they approach a brand or a product. So we really tend to look at a broader set of values, of attitudes, even of data about our customers.

So clearly millennials is one of the elements. We're not breaking down numbers about the composition of our customer base. We have seen as we said for example in the February capsule, we have seen an increase from a younger clientele in general, but at the same time we were very pleased because we also saw an increase from our existing and from our top tier clients. So as I said I think they are important but I think there is a broader set of values that we want to look at in terms of the metrics.

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Julie Brown, Chief Operating & Financial Officer
So in terms of our accessories business it's now about 40% of the total business. Handbags as a percentage of our total Group are around 20%, just shy of 20%. So bags overall are about half of our accessories business in total.

What we found last year is the small leather goods was driving the accessories business very well, the leather component very well. And some of the recent launches we've made like the Belt has only been launched in March, one size. And we've now got more sizes rolling out in April. The smaller sizes which tend to be more popular with the Asian clientele are coming out right now. So we're seeing good inflection with the Belt. It's early days but good inflection with that one.

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Marco Gobbetti, Chief Executive Officer
And I want to make a comment on that. This is building a strong architecture; a strong collection on handbags is a process okay. So while we have one good performing bag it doesn't mean that we have completed our work. I think we are so ambitious in this category that I think it's going to be an ongoing process across new styles, across existing styles. As I said before about different silhouettes and uses that the customers today are looking at in the collection.

So really there is a lot, a lot, a lot of work there and you will see it progressively building into an offer that I think will look significantly different over the next six to twelve months.

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Zuzanna Pusz, Berenberg
Thank you so much for taking my questions. I will give you a break on handbags and I will ask two questions, one on Farfetch and the other one actually a follow up from Melanie's question.

So first of all on Farfetch do you plan any additional collaborations with Farfetch beyond what you've announced so far? I mean different peers of yours have - worked with Farfetch in different capacities whether it's a 90 minute delivery in major cities or Chanel have recently launched more work on their retail experience. So I'd be just curious to know if you plan a bit more with them or do you plan to focus any additional digital initiatives, if you just plan to do them internally?

And the second question it's just a clarification so it's a quick one. So am I right to understand that the capsule collection available straight after the fashion show in September will be the one designed by Riccardo? Because I understand there is a lead time involved, so given that he just joined in March I just wanted to make sure that the capsule collection launch in September will be really his? Thank you. Will be designed by Riccardo Tisci.

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Marco Gobbetti, Chief Executive Officer
Releasing in September, is that the question?

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Zuzanna Pusz, Berenberg
Yeah.

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Marco Gobbetti, Chief Executive Officer
In terms of Farfetch, clearly I think we are enjoying a fantastic partnership with them. So do we have other initiatives coming? For sure. Definitely we are - they are a great partner of ours. They are not the only partner, but they are a great partner with us, and we always look for new initiatives and new ideas that can enhance the client's journey with us online.

So we'll certainly continue to work with them on different things. I think we have done two pretty major things with them just now; including this new Dream Assembly type of accelerator that I think is going to be quite interesting.

In terms of Riccardo's Runway show, I don't think you really expect me to divulge everything about what we are going to do in September. So there are a lot of ideas around September. There is a build up to that. We have big plans but I think it's a little too early now to disclose all of them.

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Charlotte Cowley, VP, Investor Relations
Thank you very much everybody. I'm afraid we are out of time. Thank you very much for coming and we look forward to updating you in July.

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Marco Gobbetti, Chief Executive Officer
Thank you.

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