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Burberry Group plc

First Quarter Trading Update Analyst Call

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Burberry

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Questions From

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Julie Brown, Chief Operating and Financial office

Good morning and thank you for joining Burberry's Q1 trading update call. My name is Julie Brown, Chief Operating and Financial Officer of Burberry. With me this morning is Julian Easthope, our Head of IR.

Slides are available to accompany this presentation on the IR section of our website and a transcript will also be made available.

I will spend a few minutes running through our performance over the first quarter and the progress we have made against our strategy before taking your questions.

Comparable store sales grew by 1%, impacted by COVID-related lockdowns in Mainland China which fell 35%.

We remain encouraged by our global performance, with comparable store sales growing 16% outside of Mainland China.

We saw a strong performance in EMEIA with comp growth of 47%, driven by local clientele

Throughout the period, we delivered a strong programme of unique and immersive brand activities that generated excitement among our communities.

This included the Lola campaign, the TB summer monogram and a celebration of the Queen's Platinum Jubilee, in partnership with the Royal Palaces, attracting a high level of engagement from our customers

We continue to see a good underlying performance with our focus categories with leather goods performing well outside Mainland China, driven by the extended Lola product range and marketing activations.

Outerwear was impacted by Mainland China where lockdowns affected demand – but excluding this, comp sales remained strong, rising 19%

The roll out of stores in the new format is progressing well and we expect to complete a further 65 stores this year

During the first quarter we continued to build on our commitments to inclusion and communities as I will describe later

Finally, we commenced the £400m share buyback on the 1st July to be completed by the end of this Fiscal Year

Turning to slide 3 and the breakdown of our retail sales

As mentioned, comparable store sales grew by 1% in the period

Space fell 1%, leading to flat retail sales at constant currency.

Currency was a 5% tailwind in the quarter, leading to retail revenue landing 5% up compared with last year.

Moving now to slide 4

Regionally, we saw strength in EMEIA, Japan and SAP, with wide variations between markets. Comparing our performance with Q1 last year:

EMEIA grew 47% as the business annualised the lockdowns in Q1 FY22. Sales to local clients were strong at above pre-pandemic levels, and sales to American tourists rebounded.

Americas fell 4% against a tough comparative

In the region, we saw very strong growth in outerwear with bags also doing well.

This drove a good increase in AUR in line with our strategy to focus on higher priced categories.

This was offset by pressure in the entry price products – especially shoes and soft accessories.

Overall we are pleased with the region that is showing comp growth of around 30% ahead of pre-pandemic levels

Asia Pacific fell 16% impacted by lockdowns in Mainland China.

Mainland China fell 35% as mentioned and the rest of Asia continued to show strong growth at 14%

Growth was driven by SAP up 22% and Japan up 32%

Korea was broadly stable given the tough comparators last year, but importantly, ahead of pre-pandemic levels by over 30%.

I want to change the focus now to brand and product as we continue to invest in the business.

During the quarter we have generated a high level of engagement on social media as well as driving traffic to our website and adding almost half a million new profiles to our CRM.

I shall start with product, and the extension of the Lola range.

This has been accompanied by an extensive campaign across all media, commencing in April with a launch including Bella Hadid that drove very strong engagement.

The campaign focused on showing Lola's strong, smart and present attitude from every angle.

We launched the Lola in a new set of pastel colourways, and released six Lola Limited-Edition animations; with only 100 of each style available.

Pop-ups and pop-ins have been a key focus with 70 opened in Q1 and over 85 planned throughout the campaign.

This has been supplemented by a strong visual merchandise display and a 3D augmented reality functionality on our website that allows our customers to virtually place a true-to-scale model of our signature Lola bag within their environment, enhancing the luxury experience.

This has resulted in a strong level of engagement on social media. For example the Bella collaboration Reel achieved a very high level of views on Instagram, and strong follower growth on Tik Tok, collectively driving earned media value and traffic to Burberry.com.

At the start of the new quarter we partnered with online gaming platform Roblox to release our first virtual handbag collection based around the Lola shape.

Designed in partnership with one of the Roblox community's most established designers, Builder Boy, the exclusive Lola range features experimental designs inspired by Burberry's long-standing affinity with the outdoors.

Staying with product, we launched the TB Summer Monogram collection in May with a new campaign starring Gisele.

The offering covered all major product categories with an emphasis on the Lola and summer clothing.

The collection united two of Burberry's icons to form a bold print that symbolises a synergy of the past and the present, with the classic Check merging with the TB Monogram.

We maximised reach and customer engagement across channels through 20 pop-ups and pop-ins globally.

The collection saw the first ever branded takeover of Loulou Ramatuelle beach club in Saint-Tropez that included a bespoke iteration of the collection that was available to purchase at a pop-up store in the resort.

This is being followed by a series of takeovers in four other regions globally.

We also celebrated the launch of the TB Summer Monogram with a dedicated partnership with Neiman Marcus that involved an exclusive immersive pop-up and takeover of one of their key stores.

It was the first time in Neiman Marcus' history that the entire exterior of a store has been taken over by a brand when we wrapped it in the TB Monogram.

Overall the summer monogram programme has seen strong reach and engagement on Instagram with the main film reel being our most viewed of all time.

As part of the monogram celebration, we partnered with Mythical Games for a second consecutive year to launch a new NFT collection in their flagship title, Blankos Block Party.

The NFT collection included a limited-edition Burberry Blanko, a unicorn named Minny B, as well as a selection of Burberry branded in-game accessories such as the boombox, which players can add to their virtual portfolio.

As part of the collaboration, we created a bespoke social space within the game, a cabana style resort named 'The Oasis', where players can come together to connect, explore and enjoy a unique virtual experience.

Moving on to ambassadors.

We continue to partner with those who share our belief in pushing boundaries, welcoming South Korean Premier League footballer Son Heung-min into the Burberry family.

This was greeted with a significant amount of social media attention with the post seeing our highest level of engagement on Instagram, 21% ahead of our previous high.

Moving on now to the customer where we continue to elevate the in store experience, rolling out our new design concept to six more locations in the quarter, including two stores in Japan, one in Hong Kong S.A.R., China and three in EMEIA. We remain on track to achieve our target of adding 65 newly designed stores bringing the total to 112 by the end of the year.

In the refurbished stores we continue to see a higher level of AUR and an improvement in store productivity and are pleased with the performance of our new stores.

We were proud to be an official partner of The Queen’s Platinum Jubilee Pageant, sharing messages of support at 80 bus stops along the route in London from children at Armley Park Primary School, a beneficiary of our partnership with Marcus Rashford MBE, the National Literacy Trust and Macmillan Children’s Books.

To mark the occasion, we designed a limited-edition scarf inspired by our beautiful native woodlands.

We also sponsored the Superbloom floral installation at the Tower of London alongside which we created a large floating meadow. All foliage from the meadow will be replanted by Burberry volunteers with local community projects across the city.

Turning to sustainability

At Burberry we recognise that the long term success of our business depends on investing in the environmental sustainability of our operations, the resilience of our supply chains and our management of climate change impacts.

This month we became the first in our sector to receive SBTI approval for our target to reach net-zero emissions by 2040.

As part of our commitment to reaching our targets, we are taking steps to innovate in the product space to drive more sustainable outcomes. For example

We currently source over 90% of our leather from certified tanneries with the aim to achieve 100% by 2025

Over half of our men's bags are now made of recycled nylon and

We are moving towards more sustainable coated canvas collections which contain more that 40% bio based raw materials

Also in the quarter we continued to build on our commitments to inclusion.

In June, we marked Pride with the media partner Dazed in a three-day celebration of creativity and community in London.

Alongside workshops, panels and mentorship sessions, we commissioned a large-scale mural by interdisciplinary artist Jota Mombaça and an original poem authored by performance poet, trans visibility campaigner and model Kai-Isaiah Jamal.

We continued to support longstanding charity partners providing resources to the LGBTQ+ community, including Stonewall and the Albert Kennedy Trust.

As part of our support for young communities, we recently celebrated the achievements of students in our Burberry Inspire programme at Leeds Playhouse with a showcase of dance, film and art.

We also celebrated our Burberry Inspire students with a gathering in New York of over 200 students, teachers, and guests.

Now finally turning to the Outlook:

We continue to target HSD revenue growth and meaningful margin improvement in the medium term.

While the current macro-economic environment creates some near term uncertainty, our performance in China has been encouraging since stores reopened in June

Given the COVID related disruption in Q1, we expect a more pronounced phasing of profits into H2

There is no change to the guidance on a number of fronts:

Retail space to remain broadly stable in the year

Wholesale also expected to be stable in the first half

Capital expenditure is guided to £170 to 180m

The effective tax rate guidance remains to around 22%

Inflationary pressures are being actively managed and we maintain our GM guidance for the full year, however, gross margin as usual is likely to be higher in the second half

There are two areas to draw to your attention

Rising interest rates are now expected to lead to around a £7m cash interest receivable

Currency movements are now expected to result in around a £190m sterling tailwind to revenue and around a £90m to adjusted operating profit based on July 11th effective rates.

We have commenced the £400m share buy back programme that we expect to complete by the end of financial year.

To close, having successfully established a strong platform, we are well set to accelerate growth, continuing to execute our clear strategy through our teams and united by a shared purpose. Thank you for listening, and we can now move on to the Q&A.

Thomas Chauvet Citigroup,
Good morning Julie and thank you for taking my questions. I've got 3, please. The first one, I was just wondering how you feel about the local U.S. and European consumer base at the end of the quarter, the beginning of July as well. This morning, you mentioned I think in a media interview that sneakers, slides and now you said soft accessories were softer in the period, but you also said there was no impact of rising cost of living on the younger consumers. I thought that was maybe a little bit contradictory. We've seen in the last couple of months slowdown in U.S. luxury credit card spend. So just wanted to know how you feel about these 2 clusters on the local consumer basis?

Secondly, on the store footprint, so you closed the beautiful Canton Road flagship store in Hong Kong. I think Causeway Bay was also closed last year. I was curious to know how much of the remaining 10 stores you have in Hong Kong represent as a percentage of your sales now? And now how do you feel about the global store footprint post pandemic? Do you have other plans to shrink it in some locations due to perhaps the lack of tourists in certain areas?

And just finally, on FX, could you explain, if it's not too complicated, for me, the reason why the incremental tailwind on revenue is having actually a slightly negative impact on profit? And is there anything specific to sourcing in particular?

Julie Brown
Okay. Thank you very much, Thomas, for the questions. So first of all, just taking the local trends that you mentioned in the U.S. and EMEIA. I'll take EMEIA first. As you probably know, our EMEIA business pre-pandemic in this quarter was 60% tourists. So it was heavily dependent on travelers. We have been very successful in converting a large part of the EMEIA business to be a local clientele-driven business. And you know we're pleased to say that compared with pre-pandemic levels, we've got positive growth in terms of locals in EMEIA and also overall in EMEIA in terms of getting above pre-pandemic levels now in our full-price business. So I think a great achievement and very encouraging performance this quarter with the 47% growth.

In terms of the U.S., what we're seeing in the U.S. is that some of the product categories that performed extremely well last year have been under pressure this year, and it's largely to do with the sneaker business and the slides, which were very popular last year. We've seen in the U.S. that there's been a move towards the higher-priced categories. So outerwear and leather goods has done extremely well in Americas. This is partly our strategy to move to the higher-AUR categories, but it's also, I think, a market trend as people have moved away from the more casual wear, more towards the formal wear has come more closely into demand.

In terms of the impact on younger consumers, we haven't seen a major impact at this point. I think the two are consistent in the shift from casual to more formal, and I think that's the biggest influence of the overall situation. Regarding U.S. credit card spend, we also saw that data, and we're still seeing strength in the higher parts of the credit card expenditure, higher parts of the market and less so pressure in the lower parts of the market. So for luxury brands, actually, that's still a positive move in our sector.

Turning to the store footprint. Sorry, I would just say about Americas as well. As you know, we were up against some very tough comps in Americas. In the first quarter of last year, we were one of the first brands to produce very high growth. And our full-price growth in Americas last year in this quarter was up 114%. So we are up against some very, very tough comparators. That will also be the case in the second quarter, but then that pressure eases off considerably in the second half.

So then moving to the store footprint and Canton Road. I mean we're always making changes to the store footprint depending on how we see the appropriateness of the adjacencies in the area, and we do take into consideration longer-term trends, which would include potentially permanent changes in traveling. So we continue to support Hong Kong, but we have made some rationalization in the overall portfolio in Hong Kong.

We've now got a high single-digit number of stores in that region. Still seeing it as very important, but clearly less of an attraction in terms of Chinese tourists going to that region at the moment.

If we move on to foreign exchange. As far as foreign exchange is concerned, we always update the currency variance depending on the latest forecast in the business. And the mix of currencies is always very different within revenue, cost of goods and operating costs. So it doesn't move in a linear way. It's quite a complex calculation that takes place in our business based on the latest trends in terms of product mix and also geographical mix. So yes, compared with the May guidance, there is a different mix in expectations at each level, and this is causing the main difference. `

Chiara Battistini JPMorgan.
Good morning and thank you for taking my questions. I also have 3, please. Firstly, maybe just going back to the American consumer and also taking into consideration the tourism part that is developing now. Can you give us a comment on the American cluster overall, so looking at domestic and the traveller, if you're seeing similar trends overall for the cluster versus the previous quarters or anything different also taking into consideration the tourists?

Second question still on tourism. Tourism has now really picked up in the calendar Q2, could you highlight any difference in customer behaviour or patterns that you're seeing today versus the way that tourists used to shop pre-pandemic? And the last question on your comment on China, you mentioned that the performance has been encouraging since reopening. I was wondering if you could share a bit more colour on how you define encouraging and any further comment you could give on that, please? Thank you

Julie Brown
Thanks, Chiara. So first of all taking Americas for consumer and tourism, we have seen a change in the tourist patterns. We've seen a rise in tourists coming from America. We've seen a good uptick coming into EMEIA, which is really positive news. In terms of the trends of the Americans as a nationality, yes, we have seen pressure on the overall American nationality. And I think it's largely linked to the product category shift that we're seeing as people have gone towards more formal wear. Very importantly, when we look at the trend in Americans versus pre-pandemic levels, we're seeing a growth of 62%. So very strong performance underlying in Americas versus pre-pandemic, but we do get these quarterly fluctuations.

Turning to tourism generally in the second quarter. We've seen an uptick in tourism. As we mentioned, Americans are traveling more. We're also seeing an uptick in Continental Western Europeans traveling. In terms of other nationalities traveling, the Chinese are still down by over 90% in terms of coming to Europe. And Asians coming to Europe, it's down by about 50%. This is both versus pre-pandemic levels. So some parts of the world were obviously resuming their travel patterns earlier than others.

In terms of the behaviours compared with pre-pandemic, it's really interesting this because more recently, and I think as we've moved towards more formal settings and away from casual settings and working from home, the categories that did well pre-pandemic are also now resuming post pandemic. So we're seeing a good uptick in leather goods. We've seen a very strong uptick in outerwear, if you strip out Mainland China. And also, we're seeing a very good return in scarves, and that business was under a lot of pressure before. The 2 categories that are under more pressure now than they were is clearly the entry-price products. So slides, sneakers are the category that are under pressure. I think it's partly, though, due to the very strong comp that we had in the prior period.

And then your third question relating to China reopening. Yes, I mean we've had the stores closed for more than 2 months in this latest 3-month period. They opened during the course of June. We've seen a very positive uptick in Chinese consumers, but it does still vary by the week. So it's not a consistent pattern at this point in time. And we are conscious that with regard to China, there are still quite serious pressures on, I think, the population because of the testing regime, they still have to do a PCR test within 72 hours of going out. And that obviously has an impact overall on traffic. We just pick up this higher degree of caution. But it's good news that they're opening, and we've got all the stores open. We just recently had one go back into closure. But basically, the vast majority are now open, which is good news, I think, for this next quarter.

Carole Madjo Barclays
Hi, yes, good morning. A few questions from me as well. First of all, to come back on the U.S. market. So to better understand this pressure you're talking about, is it fair to assume that the sales last year were also boosted by these consumers wanted the market on the back of the stimulus checks, et cetera, and that they have not disappeared? Could this be a fair read at all? That's the first question.

And then, sorry, to come back on the Chinese market. I missed if you have given a number during the previous question. And is it also fair to assume that towards the last month of June, you were seeing sales down at around mid-teens or low teens in June on the back of the, of course, much weaker decline in the start of the quarter? And that's the questions I have. And last point, still on China. Can you give us an update on the brand ambassador search? Maybe explain also why it's taking so long to find a local brand ambassador in the country?

Julie Brown
Okay. Thank you for the questions. In terms of the U.S. market, it's really difficult to unpick the reasons for buying certain product categories and certain trends. And we

didn't see a significant impact from stimulus checks when we were looking at the customer data last year, but it's very, very difficult to absolutely tell. What we are seeing is the bigger trend seems to be the move towards more formal wear. So the fact that we're now seeing outerwear and leather goods performing at a strong level and we're seeing small leather goods, accessories, sneakers performing at a lower level, we think it's more to do with just the consumer move towards more formal settings. And we think that's the major driver. But undoubtedly, there will have been some impact last year, probably particularly in this quarter relating to government stimulus.

Turning to China. As I mentioned, we're seeing different figures in different weeks depending on the situation, we're not giving an exit rate relating to June, but there was a marked improvement as we went through the month. Clearly, the most impacted month was the first one in the quarter. It eased up a little bit in the second month and then a considerable upswing as we went into June. But because we're still seeing variability as we go through week to week and including week to week in July, we prefer not to give an absolute number on that one. And then I think your final question was relating to brand ambassador and search, but the line was a bit tricky. Would you mind just repeating that?

Carole Madjo Barclays
Yes. It was just if you could give us an update on the search of a brand ambassador in China, if you have found anyone. And if not, why do you think it's taking so much time to find someone? Thanks.

Julie Brown
Okay. Thank you. I mean we continue to work with influencers in China. It's obviously a key market, and we take a very long-term view. But we did pivot some of the work we were doing about 12 months ago. And what we're now doing is very much focusing on a number of areas. I mean key influencers, local influencers are key. Chengdu is also important. We did a recent brand exhibition in Chengdu, which was very, very popular. And we've also been working with a women's development forum to support women's development in China. We're also now getting ready for Chinese Valentine's Day and a number of key activations. So it continues to be an area of real importance to us.

Carole Madjo Barclays
Okay. Sorry. But are you still looking for someone then? Or is the influencers enough in terms of marketing strategy for you in the country?

Julie Brown
Yes. I mean we're always working with the agencies in China in terms of ambassadors and influencers. But the majority of our work at the moment is done with some top influencers in the country.

Antoine Belge BNP Paribas Exane,
Yes and good morning. It's Antoine at BNP Exane. So some questions. First of all, coming back on the medium-term guidance of high single-digit organic growth. I think it's also confirmed for the full year but with the, I would say, a slow start to the year on the sort of wholesale guidance, is it possible to know what sort of assumption you're making on the Chinese market for the remainder of the fiscal year for you to be able to achieve that high single digit? My question number two is regarding the more recent price increases that were put through in the quarter. Is it possible for you to quantify them and a little bit of granularity? And so if you started to see maybe a bit more price elasticity on those price increases? And finally, just sort of follow-up question on the FX. So you're talking about different mix. Is it fair to say that maybe what has changed is due to the weakness in the Chinese market and probably, there are less profit of translating the Chinese currency into British pound?

Julie Brown
Thank you, Antoine. So taking you to both, with regard to the guidance, high single-digit growth, yes, we're still seeing that. And the major assumption that we're making there is, we obviously knew that China was going to be under pressure in the first quarter. We are assuming that there will be some level of disruption in the second quarter but relatively minor compared with the first. So we're not envisaging a full lockdown, for example. And then going into the second half, we're seeing strength as the country rebounds from the lockdowns they've been experiencing. We have seen previously some very good upswings in terms of consumer behaviour. So we're basically anticipating a recovery in half two.

In terms of the price increases, as you know, we put a leather goods price increase through, which was high single digits in May last year. And we've put through further price increases in the first quarter of this year and towards the end of last year, again, with high single digit across a sizable proportion of the leather goods business in both periods. And then in addition to that, we've also put through some recent price increases in rainwear and Jersey wear and also scarves. So in terms of elasticity of those price changes, we've seen no adverse movement with regard to that. We're seeing all the categories respond well. As I mentioned, in terms of the changes in the product categories, it tends to be driven more by macro and the return to formal wear and a very difficult comp base in terms of shoes rather than any particular relation to price resistance. We're seeing no price resistance at this point in time.

And then foreign exchange, I think the most important thing to say is that this doesn't move in a linear way. I appreciate the point about the revenue and the profit being different. But we based the forecast of the foreign exchange guidance on the mix of currencies which were in the forecast at the time we take the sensitivity. So as the business moves, both geographically and by product category, it does affect the exchange variance. So basically, we can go into this in more detail, if you like, with the IR team offline, but it's basically based on our forecast as we run from now through to the end of the year.

Antoine Belge BNP Paribas Exane,
Thank you. Maybe just a follow-up again on the guidance for the year. So I think in the U.S., so first quarter down 4%, and then you highlight comps still tough in Q2 and then a bit easier in the second half. So I mean, is that fair to say that you're expecting a sort of, I don't know, a flattish market for the year or actually hoping for a positive outcome if H2 is quite robust?

Julie Brown
Yes. In Americas, yes, we're seeing the overall trends in Americas has been positive. We were conscious, though, that Americas in our first half of last year was very high. It was very strong. And therefore, we're up against some very tough comps, particularly in the first quarter, also into the second, and then that pressure eases off considerably in the second part of the year. So overall, we would see positive trends upcoming in half 2 in Americas and potentially also some growth in the second quarter. But clearly, we have to keep the situation under review based on macroeconomics and trends overall in the market. Thank you very much

Thierry Cota Societe Generale
Yes good morning. This is Thierry from SocGen. Three questions for me. First, at the current effects and with the data you just updated, can you tell us what is the EBIT margin target for next year, not at constant currency but at reported currencies are at the current levels? Would an estimate of an equivalent of 21.5% rate compared to the 20% constant currency that you reiterated, would 21.5% be a fair assumption? Secondly, on this year, could you comment on the OpEx inflation that you expect for the year and that you're budgeted at constant currency? And lastly, on the gross margin, you did highlight that H1 would be weaker than H2. It's generally the case. Presumably, maybe will be more the case this year given the China situation. Can you give us a sense of the scale of dilution of the gross margin you expect in H1 versus last year?

Julie Brown
Okay. Thank you very much, Thierry. So obviously, we're not in a position to give extreme accuracy with regard to the margin. And I think you were asking for next year regarding that rather than this year. We are holding the CER guidance at around the 20% mark for full year '24, which is the medium-term guidance. And currency, I just turn to Julian, but currency at the moment is giving a lift of about...

Julian Easthope
180 bps.

Julie Brown

180 bps. So it would take you to slightly above your estimate Thierry based on current rates of exchange. Taking your second question regarding OpEx inflation. In terms of OpEx inflation, we're seeing overall in our cost base, this is the OpEx base, around 4% to 5% inflation. It's a combination of seeing pressure on people costs because of the merit increase. However, the benefit we have got is that because there's a large part of the OpEx base which is based on the lease portfolio, it does mean that there's a degree of mitigation against current inflationary pressures on the operating cost of the lease portfolio, which is very helpful in our business.

And then turning to the gross margin. Yes, we normally have a stronger gross margin in the second half, no doubt. And we are seeing this additional pressure that is going to come in the first half of this year, largely due to the lockdowns we've experienced in China. So it will definitely be more pronounced. We'd anticipate that when you look at sort of CER rates, which is probably the best way to look at it at the moment, we anticipate this current year being slightly below where we were last year. But we are taking a huge amount of actions to protect gross margin. So working very closely with merchandising, allocation, planning and supply chain to ensure that we can mitigate those pressures on the gross margin, both through procurement efficiencies but also the work we've been doing relating to some of the price increases that have been going through to offset those inflationary pressures.

Charmaine Yap Redburn
Hi there, morning, thank you. Its Charmaine from Redburn. I also have 3 questions, please. The first one, in terms of your split of sales by product category. Given the outperformance on leather that you've mentioned and outerwear, I was wondering if you're able to share some broad percentages of those categories or in other words, if I look at your sales split by accessories, it has maintained quite stable in recent years. Would it be fair to think that now large leather goods are now closer to 60% of accessory sales and maybe soft accessories lower at 20%? Any breakdown there would be helpful. And the second question is in terms of your customer base. I was wondering if you have any cohort of particularly high spenders. So I'm trying to get a sense of if there's any potential skew, for example, would it be the case that 5% of your customer base contribute 40% of sales, something like that? Or is it more balanced across all customers in your stores? And the last one in terms of managing the cost inflation. Are you able to give a bit more sense how are you doing that? Like where are there more cost savings that you will have to look for? And if so, in which areas? Thank you

Julie Brown
Thank you very much. Thank you. So first of all, turning to the product categories. There hasn't been a very significant shift at this point in time. Leather goods is slightly increasing as a percentage of our overall business. It used to be around 20%, slightly below that. It's now just moving above the 20% mark. So in full year '22 because it's

more consistent than just giving you a quarter, it was around 21%. And outerwear is now around 30% of our business. This was last year. Rainwear is around 12% of our business. Other accessories, shoes, scarves, tends to be in the in the mid-teens area. And then children's remains a relatively small part of our business at around 5%. So that's in terms of the product categories.

In terms of the customer base. We don't have to disclose the split of the customer base in terms of the ratio of different categories of customers. But in terms of balance, it's fairly well-balanced across the regions. We have through this pandemic period retained a very core audience of high-spending discerning customers who still look to buy into the classic pieces and also look for exclusivity in the range. And customization is also a key driver, particularly during the festive period.

And then turning to your final question, which was around concentration of cost-saving areas. I think the biggest focus in terms of offsetting the inflationary pressure that we've got is really around the gross margin. So we see pressure in cost of goods. That is largely coming from freight cost, logistics, linked to the price of oil and energy, and also product supply, supply chain costs. And so the biggest focus area is mitigating those costs through procurement efficiencies and in discussions with our suppliers.

There are no other major areas of significant cost savings coming through because we completed the cost-saving program, which amounted to a cumulative saving of GBP 205 million. And we've been basically reinvesting that money into the front-end commercial part of the business. But management of cost inflation just is part of what we do, part of the business.

Charmaine Yap Redburn
Just to clarify the leather goods when you say, for full year '22, 20% of overall business, is that large leather goods and small leather goods as well?

Julie Brown
Yes. That's the combined total, yes.

Charmaine Yap Redburn
Okay. And also just to follow up on the cost pressures. So what sort of rates are you looking at in terms of the pressure? Is it high single-digit levels?

Julie Brown
In terms of cost pressure, it does depend on the categories. So overall, we're seeing significant increases in transportation costs, and they are actually rising in the double-digit category. Commodity prices are rising more or less in the mid-single digits, some are moving into double digits. And then labour inflation tends to be, I guess, a mid-single digit. Overall, it varies by different regions across the world, but those are broadly the expense areas. As I mentioned, the overall OpEx increase is remaining at around the 4%

to 5% level, and this is largely supported by the lease portfolio because our leases tend to be in the region of 4- to 5-year leases, sometimes 6-year leases. So they give us a fairly long-dated degree of protection against overall inflationary pressures.

Liwei Hou CICC
Good morning Julie. This is Liwei from CICC. Thank you for taking my questions. I've got 3 questions if I may. The first 2 are on China. So the first question is we just saw the China GDP number: first half, only up 2.5%; second quarter, slight growth of 0.4%. So there is apparently a slowdown of China's economy. My question is, are we seeing this bifurcation of demand in China similar to the U.S., i.e. core customers buying more, but we're seeing aspirational customers disappearing? That's my first question.

Julie Brown
Okay. Thank you. Yes, I mean we saw the headlines on China this morning. Clearly, there is an economic pressure coming through in China. But the biggest impact on our business at this stage is certainly COVID and COVID-related policies. We anticipate once the COVID restrictions are removed to a higher degree and the testing requirements relax, that's when we see usually a very significant surge in demand. And I'm sure that that will also cause a surge in demand in the Chinese economy more globally because of the stated objectives of the Chinese government. So I think we anticipate the second quarter being stronger in China for sure. And then we do anticipate a much stronger second half as China resumes. So I think that takes care of the first one regarding the economy.

The second part of your question relating to aspirational customers, we still see China as a very important medium and long-term opportunity and largely because there is a significant growth in the middle class in China anticipated. I think the data is from something like 350 million to 500 million over the next 3 years. And that means, therefore, that there's a golden opportunity for luxury companies in China to take advantage of that overall macro factor.

Liwei Hou CICC,
Got it. And my next question is regarding the COVID restrictions in China, it's a big country. Shanghai is one of the most impacted. Chengdu and Shenyang, with more room to move around. So are we seeing maybe a growth in Chengdu, Wuhan and Shenyang, for example, compared to Shanghai? And just a little bit detail within China would be helpful.

Julie Brown
Yes. We've got very strong growth in Shanghai. So the major cities still see major growth, Shanghai and Beijing. We are seeing growth also in the Tier 2 cities in China. But at the moment, the trends are very difficult to read because the lockdowns are by far having the single-biggest impact. So I think overall, if we put the lockdowns on one side for the moment, then we still see strong growth in the major cities, but we're also seeing a more rapid expansion, pre the lockdowns, in Tier 2s. And I think that's probably the

biggest thing to call out. Chengdu, we see as important, and this is one of the reasons we decided to do the Burberry Generation exhibition in Chengdu. It was an immersive exhibition to celebrate local Chinese creative community. And as mentioned, we've also been doing work with the Chinese Women's Development Forum, which is a 3-year designer training program designed to empower women with comprehensive tailored training to support design skills and also encourage entrepreneurial skills. So we're very focused on that in a number of areas.

Liwei Hou CICC
Got it, thank you for your comment. And my last question is based on Thomas' question earlier on regarding the store footprint. It appears that we are trimming stores in selected locations. Does that mean we will keep ramping up our e-commerce to substitute the sales? And then will that lead to a continuously improving margin? Will that be one of the key margin driver, e-commerce and physical mix from that perspective?

Julie Brown
Okay. Thank you. Thanks for the question. In terms of stores, we always do look at the store portfolio. We've undertaken a considerable number of relocations in stores. We also did a strategic program of 38 store closures that we undertook. And these are programs really to determine the right store footprint for the company in the future. In relation to the digital channel, we see them as being very complementary rather than being a substitute for the other because the beauty of digital is that it's a way of communicating with our consumers, it's a way of attracting consumers and building a stronger CRM database and then finally, it's an e-commerce channel. But what the beauty of digital really is that it's omnichannel. It's all about making a completely smooth transition for a customer between on and offline as they wish to show up and as they wish to share information about Burberry. So we see it as very much complementary, very much omnichannel rather than either/or. It's actually additive. You'll see us focusing on both going forward.

Operator
Ladies and gentlemen, this concludes our question-and-answer session. I would like to turn the conference back over to Julie Brown for closing remarks.

Julie Brown
Okay. Thank you very much, everyone, for joining us today. We appreciate you joining the call, and we look forward to giving you a fuller update with our half year results and strategic update with Jonathan in November. Thank you.