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# Transcription

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**Speakers:** Euan Sutherland and Nick Wharton

# Presentation

## Operator

I am pleased to present Euan Sutherland, Chief Executive Officer.

## Euan Sutherland

Thank you very much and good morning, everybody, and thank you for joining us on today's call, where we will be covering the performance of the business in the second half of the year, together with the further evolution of our senior team. As always, I'm joined by Nick Wharton, our CFO, and I'll hand over to him in a moment to briefly run through the detail of this statement. By means of a trading overview, though, I'm pleased to report that the positive sales growth delivered across the year has been maintained in this final quarter. This is particularly pleasing against a tough comparative from last year, and a broadly unhelpful weather pattern across most of Europe. While our strategy will increasingly diversify our business in terms of category, geography and channel, Europe remains the most significant part of our business at this time.

This strong sales performance reflects the benefits of our high level of continuity ranges, meaning that we carry product all year round to provide some protection against unseasonal weather, and also our e-commerce business, which continues to go from strength to strength, outperforming even some pure-play market leaders. In addition to trading strongly through the half, we have made good progress against our strategic goals. We will provide more flavour regarding this progress with our results presentation in July, but it's worth focusing on a few highlights just from the past six months today.

We continue to embed a deep understanding of our customer throughout the business, informed by a growing bank of true customer insight. This is particularly important across our expanded category and design teams, ensuring that our core and new innovations reflect the requirements of our growing customer base. Based on our early success, our confidence in our efforts to extend and broaden the appeal of the brand through ongoing innovation is growing. The launch in this period of premium menswear, but more importantly and to a larger extent Superdry Sport, have benefited our like-for-like sales while expanding the brand footprint and adding interest to the store experience. Our Execute strategy focuses on expanding our business globally, having opened 136,000 square feet of net new space in the year, measurably ahead of our long-term guidance of 100,000 square feet per annum. We have also extended our global footprint through our wholesale partners, adding 48 franchises 4 licensed stores and 27 wholesale concessions.

This global expansion will continue, adopting the right entry model for each country. To illustrate this, in the balance of this week we will see us open a new 8,000-square-foot owned store in Copenhagen in Denmark, and a franchise store in Łódź in Poland, where franchise stores are being used to establish the brand in that country. Our longer-term development opportunities in North America and China are each progressing in line with our plan, with the key focus in each market being the successful opening of our first stores in China and six stores in the northeast of the USA [in the balance of this calendar year].

Finally, we need to underpin our growth through our Enable programme in people, systems, processes and infrastructure. During the year, the key developments have been the completion of my senior team through the extra roles of Nick Tatum [Global Retail Director] and Paula Kerrigan [Transformation Director] to the Executive team, and the first part of our DC plan in consolidating our retail stock into a single pick; both successfully completed prior to peak season. I'll now hand over to Nick to go through some of the detail, and come back to close the script.

## Nick Wharton

Thank you, Euan, and good morning, everybody. I'll work through the announcement, starting with sales. The performance through the second half-year was well balanced across our sales channels, with Group sales growing by 20% from similar levels of growth in each of our retail and wholesale channels.

The largest sales growth constituent, and indeed our largest medium-term value opportunity, remains new store expansion in Europe. In the half, year-on-year space has grown by about 24%, which is broadly in line with the full-year increase, and specifically the half saw us open about 73,000 square feet of new space, of which almost 90% was outside the UK. And with a total store footprint in mainland Europe at the start of this year of only around 190,000 square feet, this represents both a significant uplift and future opportunity in territories where the brand is already present and well understood, and where we have a history of generating strong returns on capital.

Turning now to the quarter. Within the quarter, like-for-like momentum from the first three quarters was maintained, despite the challenging comparative. While, importantly, stores, e-commerce and wholesale were all positive like-for-like in this period, e-commerce remains by far our fasting-growing route to customer. Indeed, our e-commerce growth was very strong, not only in the quarter but across the entire half, and this will lead to a direct impact on the sales and distribution cost base from the higher unit cost to serve in this channel. From a product perspective, our fastest-growing range was womenswear, where we are seeing a building positive design impact from the new category team that we established just over a year ago.

Second-half performance in our Wholesale division is pleasing and reflects the positive response to our increased focus and development of this channel. It did benefit in part from new business from our US operation, however, the majority of the sales increase results from an increase in our customer base that Euan outlined, and also increased sales per customer, where again womenswear has been the primary category driver.

Turning now to gross margin. With a relatively even split of growth across Wholesale and Retail in the second half, this removes the mix impact that that was a material component of our first-half performance. Therefore, our second-half performance really just reflects the continued sourcing gains and direct sourcing benefits that rest within our medium-term guidance of long-term accretion of between 0–30 basis points per annum. And therefore, accordingly, we are guiding toward the upper end of the margin guidance given at the half-year.

While the final quarter of the year represents our lowest-volume quarter, our sales delivery will convert to higher profitability. Our guidance for the 52-week period is for underlying PBT between £72.5 million and £74.0 million, against a market expectation that we believe is £72.3 million. And, converting that to operating margin, we would anticipate a marginal strengthening year on year in our core business, with a dilution at the Group level from our initial losses in the US and China, which in total are about £4 million, in line with the guidance we gave at the time of the interims.

Finally to our net cash position. We continue to generate healthy cash flows, readily funding our organic growth and providing capacity for a progressive ordinary dividend stream which commenced in the half with the payment of our maiden interim dividend of £5 million. That completes my summary, so I'll hand back to Euan.

### Euan Sutherland

Thank you, Nick. Just before going to questions, I just want to comment briefly on our other RNS made today regarding the change in the working relationship with James Holder. We've made a whole series of management changes over the last 18 months, each aimed to strengthen the capability within the business and to play to the strengths of key individuals, particularly our founders. This next step today is a further example of this measured approach. The change that we've made today balances James' desire to spend more time on some of his personal interests, while remaining heavily involved with the Superdry brand, with the benefit to the Group of focusing James alongside Jules on the continued stretch and development of the business. The reality is that the heads of design in men's and womenswear and their teams have been independently managing the mainline ranges for the past year, and James has been less involved, focusing more strategically on some of the big innovations that we've talked about in the last six months. This formalises the working pattern that has been present in the business over that period of time.

So, with that, I think we'll pause and go to questions. Thank you.

## Q&A

### Operator

The first question comes from the line of Richard Chamberlain from RBC.

### Richard Chamberlain

Couple of questions from me, please, Euan. I just wondered if you could comment first on the e-com performance; was it equally as strong in the UK and outside the UK, and any material difference?

And then the second one is on wholesale. I just wondered how important were the opening of the franchise stores in the quarter, and where are those located?

## Euan Sutherland
E-com: pleasing, as we've said, as Nick covered. The performance across the world has been very balanced, we've got very big markets in the UK and Western Europe, we've got a growing e-com base in the US and we've seen some very strong rest-of-the-world performances too. So I think that is an early example of us moving the base of the business to be a global base. It's the fastest way we can do that in e-com, so the e-com performance is incredibly balanced across all of our territories, so strong growth across the world.

In Wholesale, franchise stores are important to us. The split of franchise and multi-brand large accounts and independents, again, are fairly balanced across our portfolio. So a continuing pipeline of good franchise stores is a key part of our plan. We've got good visibility of that pipeline continuing into FY17, and the mix again is Europe and the kind of Rest of World territory for us, which tends to go east and kind of south of Europe. We don't have any franchise stores in the US, don't intend to go franchise in the US. So, good growth in Rest of World franchises and in Western Europe; particularly Germany saw some good franchise locations open. Poland I mentioned just in my brief intro, and that's an interesting and growing market for us on a franchise basis. So, again, pretty balanced.

## Richard Chamberlain
Were there many franchise agreements shut down in the UK, or sort of closed in the UK, or was it mainly expansion?

## Euan Sutherland
No, we didn't. We closed the UK franchised stores in the past, so there wasn't any net negative there. We do see a bit of churn in the rest of the world, and the 48number reported today is a net number. In terms of closures, about five or six.

## Nick Wharton
There's the odd bit of relocation that you would see in any sort of store portfolio; particularly the scale of the franchise portfolio being still materially larger than the owned store portfolio. The progressive move in the UK, essentially, is more to move out of concessions we have with House of Fraser, as we have a bigger presence in our own stores in the UK and can transfer those sales largely to our existing own stores. So that's the biggest move of non-owned stores in the UK.

## Operator
Michelle Wilson at Berenberg.

## Michelle Wilson
Three questions from me, please. First of all, can you give us the e-com penetration at the moment? You mentioned that was a big driver of like-for-like sales. And can you give any of the details around the differences in cost to serve between e-commerce and retail? What kind of differences are we talking about there? And as you put down the expanded distribution network, how should we think about the margin progression there? Is the expansion of the distribution network something that can offset the differences in cost to serve between e-commerce and retail?

And then also, in terms of the US business, you added six stores in the quarter, I think you said, or over the last half. Is the intention now to continue to roll out stores in the US, or is that a number that you're happy with, and how are you focusing on reaching break-even?

And then my third question, please – sorry, there's a lot there – but the third question, just for the cash on the balance sheet. So you've got £102 million on the balance sheet now; what's the plan for that cash? Is the expectation to buy out any more of the franchise partnerships, or is that cash that can be returned to shareholders?

## Euan Sutherland
Let me pick up the USA point first, Michelle, and then I'll hand to Nick, who can probably group some of those together. The six stores are going to open, they haven't opened yet, so just to be clear on that, they are going to open first half of this financial year and the first one's opening July time. They're all North Eastern Seaboard, New York, Philadelphia, Chicago. And are better locations, better size, so fits the brand.

Outlook for the US: I think it's fair to say that we exited the last financial year in a much better shape than we entered it last year; happier with the three channels to market there, Retail, Wholesale and e-commerce. We did a lot of work in the last 12 months to get the offer right; the teams, the people, the investment right. So we still feel that we're on track for that break-even goal. The very interesting next steps will be how the six [trial] stores perform. Just to be clear, those stores haven't opened yet. They will be opening in the summer through to the autumn.

## Nick Wharton

In terms of e-com penetration: we will give the absolute level of e-com growth at the time of the prelims, but it's probably helpful to give you a steer in terms of direction. We're seeing very material growth in e-commerce as a benefit of not only the single pick consolidation but also an advantaged proposition that we've talked about before. So having a growth around the 40% mark would be reasonable for us; across the second half-year, so it's not just a quarter four factor. And that obviously has the carry-through that I referred to in terms of the sales and distribution cost to serve relative to a retail proposition. We started the year with an 18% retail participation of e-commerce, so you can work out from that that it's moving healthily into the twenties percent. From a cost-to-serve perspective, the big variables are essentially around the unit cost of delivery. We are delivering free, which is part of our advantaged proposition, across the world, regardless of spend, and we are delivering relatively small number of units to a single point. Therefore the biggest constituent of the sales is the delivery. Also we have other variable costs around customer acquisition, for example digital marketing. We also have variable hosting costs and processing of returns, where we believe we have a favourable level of returns against the sector average, but returns are still a component of that variable cost. So those are the four biggest elements of the relative cost to serve versus shops.

In terms of the distribution network: one of the benefits we'll get through our distribution network development is proximity to customer. So what we will see in that delivery component, when we've established our DCs during this year, is a reduction in that delivery cost due to average proximity to customer, whereas now we deliver globally from the UK to all our customers from an e-commerce perspective.

Finally, in terms of the cash on the balance sheet, we're essentially where we were in terms of when we talked about our capital policy at the prelims, in that our preference remains to invest that cash to support the growth of the business. We have capital guidance – CAPEX for this year of £50 million, next year will not be dissimilar, driven primarily by the amount of owned space growth across Europe. But also, in terms of the opportunities, there are small opportunities to buy back wholesale relationships. The majority have been done, and the material ones have been done within Scandinavia and with Europe, and obviously with the US, but we will take those opportunities where they drive value.

I refer to the fact that we've introduced an ordinary dividend, the maiden interim dividend was about £5 million and the total for the full year will be of the order of £15 million. Representing a new call on cash for us, year on year. We will continue to have our capital position under review, and our commitment is that when our cash holding is demonstrably excessive, we will return it to our shareholders.

## Michelle Wilson

Thanks very much. Can I just ask a quick follow-up on the delivery point? When you talked about the investment in the distribution network, getting you closer to the customer and lowering the cost of delivery, when should we start to see those benefits coming through?

## Nick Wharton

That will be calendar 2017. We are going to be very measured in how we introduce the new DC infrastructure. We have said before that as a management team, with our experience of this kind of change, it teaches you to be disciplined. Therefore we will undertake a progressive implementation, we won't change all channels to our new European DC at the same time. I would point out that we will be making some OPEX investment in FY17 in order to mitigate the risk of the migration from one DC to multiple DCs. This will not be dissimilar to what we did this year with our single pick implementation. We invested in the delivery proposition and labour, as an example, in order to mitigate that risk. We will probably spend a couple of million pounds in mitigating that risk during FY17. We regard this as a manageable operational cost and the right investment to make, and not something we perceive as being exceptional in any sense.

## Michelle Wilson

Okay. Brilliant. That's really helpful. Thank you.

## Operator

John Stevenson at Peel Hunt.

## John Stevenson

First up: could you just talk a little bit about range performance? Particularly Idris, and then we've had the sport ranges, men's and women's. Just give a bit of colour to what's been selling and how range has developed.

And then a second question on US wholesale. Spring/summer has changed the platform of partners you've got now, how's that going to continue to migrate into autumn/winter. Has there been a step change?

## Euan Sutherland

On the range development the comments I'd make are: womenswear continues to be the fastest-growing category, albeit from a smaller base, but it's a reasonable size now, and that's been a continued process and progress over the last 18 months or so. There's lot of innovation; innovation in the ranges themselves, in the collections that we launch to the market and how we display them in the store. So, for the first time, we've moved away from a category approach into a collections approach. That's worked incredibly well in womenswear, and is now being introduced, in part, in menswear too. Slightly different buying patterns between men and women, but that has really helped our female ranges.

We've seen innovation and progression in the core main line, which is incredibly encouraging. On top of that – and we look at it as innovation in main line, which is, as you know, the vast majority of our product – supplementing it with new pipeline of innovation. Idris was the first of that. Idris launched late in the pre-Christmas run-up, 27th November and has performed well and continues to perform well. The most important thing for us is that we gained some valuable data points as this was the first time that we'd really been in this market. We have been able to construct our autumn/winter 2016 range for Idris off the back of that data. Meanwhile, we had to update it with the spring/summer 2016 range, which is, as you see, landing in stores right now. A small update, lighter colours, some lighter weights. But I guess in total on Idris, we are very happy with the progress, and you should see the next big step on coming through autumn/winter 2016.

On its heels was testing of Superdry Sport, which if you remember, we tested in womenswear – the first category innovation to test in womenswear rather than in menswear – and then we tested that last summer. We supplemented it with a slightly bigger womenswear range in January, which again went very well. An indication of a far more measured and data-based approach to product evolution. The findings were included in the development of menswear, and the ranges were delivered into the business in March. Although it's a small part of the business, it is performing incredibly well, and we are adding to the range, both in volume and depth and also in the number of options. The ranges have gone into owned retail, but is now being sold into wholesale too, so it will start to appear in franchise stores and in wholesale outsets around the world. Idris is just landing in the US as of this week, for a small capsule of spring/summer. The main launch for Idris is in autumn/winter in the US. There's certainly some considerable interest from our wholesale partners, which has underpinned some of the growth that we've seen second half on wholesale.

As a final comment the innovation stream is very important to us. Part of the formalising of the James Holder role is to allow him to step away from some of the day-to-day roles, which is really what he's been doing over the last 12 months, and focus on the freedom and the creativity to give us an even stronger pipeline of new innovation. And that's underpinned by the data that says our customers want to wear our brand on more occasions and in more life stages, so there's quite a scientific approach under the art that sits with the creative team.

## Operator

Kate Calvert from Investec.

## Kate Calvert

On Germany, could you talk a bit about the performance of your stores there in terms of the ones that have gone like-for-life? And what are your thoughts in terms of the pipeline of new space? Are you getting the sort of space you want there quite easily?

## Nick Wharton

As we said in December, we still have a relatively small population of like-for-like stores in Germany. That will be materially different by this autumn, where we'll be able to give a more meaningful statistical population. However, the ones we've got are maturing in line with our expectation, and recognising that we believe there's a – not unreasonably, there's a longer maturity profile in our European stores than in the UK, where brand awareness is lower. But that obviously leads to some like-for-like progress over that maturity profile, and the performance we're seeing is in line with our expectation. Obviously, variances by store, but the average of a small population is roughly where we thought it would be.

## Euan Sutherland

The pipeline remains strong. What's interesting about the German market is it is technically our most sophisticated market, i.e. we have owned stores, franchise stores, multi-brand wholesale, e-com and affiliate e-com. We think, based on the data that we're getting out, that the multi-channel delivery is benefiting the German consumer in understanding the brand. So, in our brand goals to drive a multi-channel customer experience, Germany is right up there with the UK, underpinned by good bricksand-mortar stores. I was in Germany two weeks ago, and I think we signed up another four or five locations. They're good locations and good sizes. So we're pleased with how Germany is shaping up, and pleased with the pipeline.

Kate Calvert

Great. Thanks very much.

Operator

And as there are no further questions registered, I will return the conference back to you.

Euan Sutherland

Okay. Thank you very much, everybody. If there's any other follow-up questions, we're around all morning and can pick up anything from there. Thanks a lot, and we'll see you in July.

Nick Wharton

Thank you all.

Operator

Ladies and gentlemen, this concludes today's conference call. Thank you all for attending, you may now disconnect your lines.