HUGO BOSS

Transcript – Q&A Session

May 4, 2022

Please note that the transcript has been edited to enhance comprehensibility. Please also use the webcast replay to listen to the Q&A session on the day of earnings publication.

Elena Mariani (Morgan Stanley): First, on wholesale. Did I understand correctly that the timing of shipments has negatively affected Q1 sales, as growth in wholesale versus '19 would have been around +12% adjusting for timing effects? What does that mean for the second quarter? Should we factor in an extra EUR 25 million of sales? What can we expect for the coming two quarters in terms of wholesale growth? Is your order book for Fall/Winter even stronger than Spring/Summer? Could you also quantify the expansion in wholesale? Is it about gaining new customers, or selling more to existing accounts gaining extra shelf space?

My second question is on your top-line guidance for fiscal year 2022. Q1 was stronger than expected, also on the retail front, where a few months ago, you didn't really have full visibility. Today, you're keeping the guidance unchanged, implying a slightly more bearish outlook for the rest of the year, which is understandable given the macro picture. But is there something that you are seeing in April, early May trends that make you believe that versus 2019, sales could slow down meaningfully? Have you noticed anything in terms of consumer sentiment, excluding China, that has changed over the past few weeks? Or should we assume instead that the growth rate versus '19 into the second quarter is pretty much similar to the high teens that you have seen in Q1?

Yves Müller (CFO): First of all, on wholesale, for which we report sales growth separately for brick-and-mortar wholesale and for digital wholesale, with the latter being included in total digital sales. Overall, in the first quarter, total wholesale (brick-and-mortar and digital) recorded a sales increase close to 20%. The timing shift from the first quarter into the second quarter of around 10 percentage points, which is equivalent to around EUR 25 million, will benefit Q2 performance – unless there will be similar deliver shifts from Q2 to Q3. Regarding the order book, we already said that orders for Spring/Summer 2022 were up plus 30% versus pre-pandemic levels. We also disclosed that for Fall/Winter 2022, it was even plus 40%. Consequently, also on the wholesale front, we are witnessing an acceleration in terms of order values, especially for the second half of the year. And this ensures additional shelf space from two directions: the very good wholesale orders reflecting strong like-for-like growth, and, on top of this, getting more shelf space by (re-)introducing our brand lines BOSS Black, BOSS Orange, BOSS Green and BOSS Camel. Overall, I feel very confident with our wholesale order books.

On your question regarding the top-line guidance, let me emphasize that we heavily invested into our brands and brand momentum. I am very pleased that our marketing investments translated into a very strong top-line performance, getting a true return on our investment in terms of top-line acceleration. Besides that, our data on digital, social media, and brand momentum, are all very positive. Compared to pre-pandemic levels, sales growth for Q3/21 was +7%, Q4/21 was +12%, and Q1/22 was +17%, reflecting an acceleration of momentum, making us very confident. I can confirm that we continued this momentum in April on a global scale, especially in Europe and in the Americas, which together account for 80% to 85% of Group sales. We are confirming our outlook today, as we had a very strong first quarter or first four months. On the other hand, there are several macroeconomic uncertainties. You might regard this as a conservative outlook, but clearly, there are macro uncertainties that let us rather stay on the more conservative side.

Elena Mariani (Morgan Stanley): Just to clarify: in Q1, the overall wholesale business was up 20%. Including the effect of the timing of shipments, it would have been plus 30%, more or less. And then your order book for Spring/Summer was up 30% and for Fall/Winter it's up 40% vs. 2019? And a final clarification on April: you're still up double digits versus 2019 so far?

Yves Müller (CFO): That's right.

Jürgen Kolb (Kepler Cheuvreux): First of all, what have you learned about your customer over the last quarters with the new collections and new ideas behind it? You can probably talk in more detail about the digital business as it has more transparency?

Secondly, on gross margin, up 120 basis points. How are the individual drivers going to develop in the coming quarters, specifically on the sourcing and freight cost side. Are these expected to further rise in the coming quarters? Or is that a more or less continuous cost level going forward?

Yves Müller (CFO): Starting with the second question on gross margin. Freight cost will remain a clear headwind for us during the next quarters. This is the reason why we remain somewhat conservative as we are guiding gross margin to remain more less stable in FY 2022 as compared to FY 2021. We recorded high quality sales growth in Q1 as we strongly reduced markdowns, having led to higher full-price sales. Our new collections are resonating well with the consumer. All this drove gross margin. But we only have three months in our books and we still have to observe this. It could be an upside if the strong full-price sales momentum will remain, enabling us to compensate for ongoing freight cost increases, because freight cost will remain high. You have seen the pictures of the Shanghai harbor, and also the war in Ukraine is adding to high freight costs. We try to compensate this with higher full-price sales.

On your first question regarding our customer base: our customer base gets younger, and BOSS is really developing into a true 24/7 lifestyle brand. Customers are buying sneakers, denim, and jersey, with these product categories really going through the roof. We even witnessed some sold-out situations in some parts of our collections, even in the United States. With the BOSS brand we are focusing on the millennials, and with HUGO on Gen Z. We are witnessing that the average age of our customers is coming down and that we are attracting new, younger consumers for both brands, BOSS and HUGO. In digital, we obviously try to re-target them via our CRM initiatives as we know around 2/3 of our customers from the physical and digital business. The results are very strong, turning first consumers into true fans of our brands.

Michael Kuhn (Deutsche Bank): First, on OpEx and especially marketing spending. As expected, quite a big increase in the first quarter, maybe a bit bigger than anticipated, marketing spending at EUR 80 million. Could you give us some indications on phasing of OpEx, especially marketing, over the upcoming quarters? Will there be some kind of another 'big bang' marketing quarter? Or will it be more stable over the remainder of the year both in absolute terms and also as a percentage of sales?

Secondly, on gross margin and the significant improvement driven by lower markdowns. Comps will get a bit tougher over the remainder of the year. Do you still expect a similar big improvement from that factor, or will it come down?

Finally, on the price increases. You've mentioned recently that keeping your prices stable also helped you gaining space from competition. You're now also moving up. Do you see similar price increases among your competitors? Do you keep that competitive advantage? What overall situation do you experience pricing-wise in the marketplace?

Yves Müller (CFO): On your first question regarding the marketing investments. Our marketing investment of EUR 80 million in Q1 primarily relates to the comprehensive branding refresh and the marketing campaigns for BOSS and HUGO. These were two broad-based, very big marketing campaigns, so it was a deliberate investment, primarily variable, with no long-term commitments behind these costs, in order to fuel top-line growth. As a percentage of sales, marketing expenses totaled 10.4%. As part of our "CLAIM 5" strategy, we want to step up our marketing investments to 7% to 8%. Having recorded 10.4% in Q1, we will most likely come out at the upper end of this range this year, implying that there will be less spending over the next quarters.

Regarding gross margin, it might look conservative that we confirmed our guidance of a more or less stable gross margin development for full year 2022. We had a strong gross margin in Q1. But we will stay with our conservative view, because there are headwinds from freight cost. If the strong brand momentum continues, we might further increase the level of full-price sales, but it's still too early to call.

Regarding price increases: feedback from our customers emphasizes our very good price value proposition, even after price increases. We will increase prices in the mid- to high single-digit range over the next two seasons. Our competitors go for at least the same price increases. Therefore, our overall price advantage should remain.

Thomas Chauvet (Citi): First, regarding retail-related OpEx. At your CMD in August 2021, you provided a bridge to the 12% EBIT margin target for 2025. This included a targeted 700 bps reduction in store-related costs as a percentage of sales, towards a level of ~19%. Can you elaborate on how this plan is shaping up? Can you provide an update on the closure of unprofitable stores, as you are targeting for ~100 closures?

Secondly, on your gross margin. You're confirming flat gross margin for the full year. But if later in the year, full-price sales and channel mix would more than offset freight cost and general cost inflation, as in Q1, would you consider to reinvest these gains into OpEx, particularly in marketing, as you did in the first quarter?

Finally, on April trading. You said that momentum continued in April. But with China probably down – I would guess, at least 30% now, versus minus 13% in the first quarter given the temporary store closures – that would suggest that the U.S. and Europe should have further accelerated versus Q1 on a three-year stack basis. Is this a fair assumption?

Yves Müller (CFO): On your last question regarding momentum in Europe and the Americas: I can confirm that the strong momentum of Q1 continued into April from an overall perspective, which includes mainland China. The development in Europe and Americas was particularly strong.

Regarding gross margin, we haven't decided yet whether we will invest any potential gross margin gains that might come up, as it's too early to call it out. As part of "CLAIM 5", we will step up the investments into our business. For 2022, all those investments into product, brands and digital are already included in our budget and in our full year guidance. So, we feel comfortable overall.

Regarding your question on the store network: we run ~450 freestanding stores globally and we are optimizing around 80-100 each year. In Q1, we opened 4 new stores and closed 8 others. This sort of attitude will continue. Regarding the optimization of our retail portfolio, we are on a good way, generating efficiencies along our execution of "CLAIM 5."

Thomas Chauvet (Citi): Did store-related costs as a percentage of sales come down year-on-year in Q1?

Yves Müller (CFO): Yes, they went down.

Thomas Chauvet (Citi): On your 50 store openings in China that you have planned: are you considering postponing these? And is this captured in your CapEx guidance?

Yves Müller (CFO): Yes, it's all captured. We continue to look for new locations as we want to grow our store network in mainland China by around 10 to 15 POS per annum. Our exposure to China is still less than 10% of Group sales, meaning that there remains strong growth potential in the Chinese market. Currently, of course, there are COVID-19-related restrictions. But we will follow our strategy to open additional stores, talking to landlords and signing new good locations for both brands, BOSS and HUGO.

Antoine Belge (BNP Paribas): First, coming back to your marketing campaigns. You surprised the industry with the high quality of people you recruited for your campaigns. Can you elaborate a bit on the impact, i.e. the type of demographic groups or age/gender that the campaigns triggered in terms of consumer?

Secondly, can you talk about womenswear and HUGO, highlighting the specific dynamics of these two parts of your business?

Christian Stöhr (VP of Investor Relations): First, we are seeing momentum catching up very strongly on social media across key channels. For BOSS, we have identified Instagram as our leading channel. And by nature, we're now really targeting a much younger cohort, the millennials, which is our core target group for the BOSS brand. And HUGO is seeing a nice balance between male and female consumers becoming fans of the brand. It's a great achievement that BOSS has become the fastest-growing brand on Instagram in Q1 among our peer group and also recorded strong engagement rates. This is also a direct consequence of the fact that our cast of brand ambassadors included a number of high-profile female celebrities and influencers, including Alicia Schmidt, but also Hailey Bieber. At HUGO, we are targeting an even younger generation, Gen Z. Our marketing initiative at the Coachella Festival resulted in really strong numbers, outperforming our own expectations: the engagement rate of 26% was much better than we had hoped for.

Yves Müller (CFO): Regarding womenswear and HUGO: if you compare growth rates versus 2019 in the first quarter, HUGO was up 26%, BOSS Menswear was up 17%, and BOSS Womenswear was on par with 2019 levels. This also reflects the direction we are taking in terms of lifestyle/streetwear: HUGO is resonating particularly well with the highest growth rate with a lot of product categories really moving forward, especially denim, jersey, and sneakers recording excellent growth. This growth will be further fueled by our collaboration with Replay in the coming months. On womenswear, you could argue we are 'only' on par versus 2019 levels. But our new SVP Business Unit BOSS Womenswear, Kristina Szasz, only started in September 2021. The first collection she had influence is the upcoming Fall/Winter collection. And we see first positive signs in terms of orders, with our overall Fall/Winter 2022 wholesale order, as you know, being up 40% versus pre-COVID levels.

Manjari Dhar (RBC): First, on the new store concept: can you give a bit more color on the performance that you're seeing from these new versus existing concepts?

Secondly, how are you thinking about Asia ex China? Is this to be more of a focus moving forward?

Yves Müller (CFO): On your second question, in Asia ex China, our performance is very strong, up now close to double-digit versus 2019 levels. Markets like Japan, Australia and Southeast Asia are coming back strongly after the long-lasting lockdowns.

Regarding our new store concept, it's too early to call it out. We have just rebranded or opened ~30 freestanding stores with the new concept. However, initial feedback of our consumers is very positive. But most of these stores are new locations where we have first qualitative feedback from the customers but no reliable KPIs yet on a like-for-like basis.

Volker Bosse (Baader Bank): First, on China. What is the background of the year-on-year sales decline in Q1? How much is related to the COVID-19 lockdown? And how is the situation with the consumer boycott: are your influencers able to promote your products?

Secondly, on collaborations. Can you provide a sneak preview on what to expect regarding collaborations for the rest of the year?

Yves Müller (CFO): Let me emphasize that we enjoyed a very strong performance in mainland China before the recent lockdowns. This means that we aren't witnessing any type of consumer boycott. Even on the contrary: we are signing new Chinese influencers. The current performance is purely related to the COVID-19-related restrictions as 30% of our stores are currently closed or operating with reduced opening hours. Traffic is down in the affected regions, and that's the only reason for our current performance. Once the lockdowns will be over, we expect sales to pick up very quickly.

On collaborations, we will continue to surprise you in the coming months and quarters. For BOSS, we plan collaborations for collections with Anthony Joshua, and with Matteo Berrettini among others. And there is more to come in the second half of the year. For HUGO, there is the collaboration with Replay coming up, but we have much more in the pipeline to keep brand momentum strong.

Philipp Frey (M.M. Warburg): First, on the implementation of price increases, particularly regarding your strong wholesale order book for Fall/Winter 2022. Are you able to raise prices for these orders as well? Or, if not, will you only increase your own retail prices, thus making this collection even more attractive for your wholesalers?

Secondly, on your inventory position, which seems very tight. Are you happy with the current inventory level or are you concerned regarding the replenishment speed?

Yves Müller (CFO): We are increasing prices from a retail perspective. Our wholesale partners based their orders for Fall/Winter 2022 on lower prices and it is ultimately up to them to decide if they also want to increase prices. We cannot and will not influence this. But, yes, they are aware of the fact that we are increasing prices for retail.

Regarding our inventory position, which we continuously reduced over the past few quarters. It has further strengthened, given the size and growth of our business. Also the quality of our inventory has improved. With less-aged merchandise overall, we are going in the right direction. But, of course, we still see potential to further optimize our inventory position in order to reduce trade net working capital as a percentage of sales.