HUGO BOSS

Transcript – Q&A Session

November 3, 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.

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Grace Smalley (Morgan Stanley): First, on brick-and-mortar retail sales relative to 2019, as you recorded a sequential acceleration in Q3. Please comment on whether that was broad-based across all geographies and whether also price increases contributed positively?

Secondly, on October trading, and again, whether you've seen that momentum in brick-and-mortar retail continued into October?

Yves Müller (CFO and COO): I can confirm that in Q3, momentum in brick-and-mortar retail accelerated versus Q2, with broad-based growth across all parts of our business, which we're very happy about! This gives us high confidence that with the brand momentum and our product initiatives, including our global campaigns, we are well on track.

When it comes to current trading in October, we have not seen any slowdown in consumer demand. We are very happy how we started into Q4.

Manjari Dhar (RBC): First, on your order books for wholesale. Could you give a little more granularity on how that's looking by region?

Secondly, how are you thinking about marketing spending for Q4 and as we head into next year?

Yves Müller (CFO and COO): Our wholesale order books for Pre-Spring 2023 and Spring/Summer 2023 are very strong, up double-digit versus the prior year. This is first and foremost driven by our initiatives across the different sub lines for BOSS - Black, Camel, Green and Orange – meaning that growth is broad-based. Importantly, our wholesale order books are strong across all business units – BOSS Menswear, BOSS Womenswear and HUGO – as well as across all geographies. Please note that, of course, our wholesale business in Asia Pacific is comparatively small. So it vastly refers to Europe and the Americas.

On marketing, it's worth mentioning that in Q3, we stepped up our marketing investments by 39%, or EUR 20 million, as compared to 2021. These investments strongly drive brand momentum, and this will also continue in Q4. As laid out in our CLAIM 5 strategy, we expect marketing investments within a range of between 7% and 8% for the outer years.

Kathryn Parker (Jefferies): First, on China. Please provide a little more color on what you've seen in October in terms of traffic and whether there have been any meaningful differences between cities or between full-price and off-price?

Secondly, on your sales guidance going into Q4. What do you expect for the different regions?

Yves Müller (CFO and COO): On China, first of all, it is very encouraging that, once lockdowns are over, our business picks up very quickly. At the same time, we have recently experienced lockdowns in several cities like in Chengdu and the Guangdong area, with 15% of our stores in ML China having been affected in the month of September. So it's an "on and off" situation. This is also something that is reflected in our guidance since China is expected to stick to its "no COVID" policy. On the other hand, we are stepping up our game in marketing over there as well, having for example signed swimmer Wang Shun as our new local campaign face. Finally, during Golden Week, where our trading was on par with the prior-year level. So, overall, we are happy how we started into October.

On our top-line guidance, which also reflects the ongoing macroeconomic uncertainties. On the other hand, as of today, we have not seen any kind of slowdown in global consumer demand. We are therefore very encouraged how we started into Q4. Growth continues to be broad-based in nature, same as in Q3.

Jürgen Kolb (Kepler Cheuvreux): First, on your collaborations such as HUGO x Replay. What level have those collaborations reached as a percentage of sales? How much did this drive your better sell-through rates?

Secondly, you mentioned that your wholesale order books for Pre-Spring 2023 and Spring/Summer 2023 look very encouraging, up double-digit. Any changes in fashion trends to call out, going into next year?

Yves Müller (CFO and COO): First, on the share of collaborations. We have recently initiated several collaborations at both brands, BOSS and HUGO, like for example BOSS teaming up with the NBA for yet another launch in Q4, and HUGO currently collaborating with Replay. In terms of the overall sell-through, these kind of collaborations are quite comparable with our regular collections. So while they are not significantly driving overall sell-through, we are very encouraged on how they are inspiring the consumer and help us to grow our customer base. This means we will continue to do these type of collaborations as they are creating a lot of buzz for both our brands, BOSS and HUGO.

Regarding our wholesale order books for the upcoming seasons, we have seen in particular smart casual and formalwear picking up lately. The suit is back, with our brands interpreting it in a modern way: very comfortable, performance-driven and highly innovative. We have seen tremendous demand on the formalwear side. But also at BOSS Orange, Green and Camel, order books are up double-digit. This means that our growth in wholesale is broad-based, with a particular strong performance of BOSS Black and smart casual in particular.

Samuel Parry (Berenberg): First, on CapEx, as you have lowered guidance again this year. Did you slowed the pace of store refreshes? Are you still on track to get this done by 2024? And please remind us how many stores you've refurbished so far?

Secondly, on price increases: how did consumers respond to your price increases for Fall/Winter 2022? And what increase are you planning, if any, for Spring/Summer '23?

Yves Müller (CFO and COO): Regarding CapEx, our investments remain focused on digital and retail, as laid out in CLAIM 5. Lowering the CapEx guidance was rather driven by operational issues such as shortages of material and workforce. We remain fully committed to invest into our new store concept, which is resonating very well with the global consumer. We receive very good feedback, and record strong conversion. So we will keep on investing into our retail network as this is driving store productivity. So far, we have implemented the new store concept in around 60 own retail points of sale, that includes around 25 stores, 25 shops and 10 outlets. And we will definitely continue to invest into this concept going forward.

Regarding pricing, we have implemented price increases for the current Fall/Winter collections within the mid- to high single-digit percentage range. Our consumers are accepting these price increases very well. We are recording very strong sell-through rates in retail, gaining market share with BOSS and HUGO. This is crucial during these times of elevated macroeconomic uncertainties, as the stronger brands win over the weaker brands, and we are really gaining market share within premium apparel, despite having increased our prices moderately. This said, and since we are enjoying ongoing strong brand momentum, we intend to increase prices again for Pre-Fall 2023 within the mid-single-digit range.

Melania Grippo (BNP Paribas): First, on the Americas. Your growth in the Americas remains quite strong, also when comparing it to 2019. Please provide some color regarding your in-store performance in the region, some sort of like-for-like growth? What have you done to improve so much in the region?

Secondly, on millennials and Gen Z. In terms of sales, how much do these two customer groups contribute meanwhile, as compared to 2019?

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Yves Müller (CFO and COO): Regarding Americas, where we have enjoyed strong momentum throughout 2022 so far, and even recorded an acceleration in brick-and-mortar retail in Q3. As compared to 2019 levels, brick-and-mortar retail sales in the Americas were up a strong 48% in Q3, currency-adjusted. This is directly related to a strong improvement in store productivity with the main driver being the fostering of our 24/7 lifestyle image in the U.S. market, and a particular strong focus on sportswear and on casualwear items. Historically, in the U.S., BOSS was rather perceived as a "suit-only" brand. Now, with these adjustments on the assortment side, we are having tremendous success. So we are very encouraged by the performance in the U.S., and momentum continues to be strong also in October.

On the consumer: as part of our comprehensive branding refresh, our global campaigns were and continue to be first and foremost dedicated to social media, to attract younger consumers, in particular millennials for BOSS and Gen Z for HUGO. We are creating a tremendous buzz on social media, thereby driving a strong increase in younger consumers, fueling top-line growth. Overall, we thus managed to reduce the average age of the BOSS customer by around 3 years over the last quarters, fully in line with what we intended to achieve.

Thomas Chauvet (Citi): First, on retail productivity, which is up by over 20% in the first nine months to a level of EUR 11,600 per square meter, thus exceeding pre-pandemic levels. Please comment on the most important drivers, particularly whether you've benefited a lot from your rightsizing initiatives, and whether you're happy with this kind of store productivity improvement?

Secondly, on your EBIT guidance: the top end of your full year 2022 EBIT guidance (EUR 330 million) implies just under EUR 100 million of EBIT in Q4. While that's on par with last year, it's around 20-25% below 2019 levels. Please explain how you get there, especially with regard to your OpEx budget for Q4.

Finally, on outlets. In 2019, outlets represented about one third of our your retail sales. Could you indicate how this figure looks like in the first 9 months of 2022 and whether you've seen a change in trends over the last quarters with maybe better momentum in outlet versus your freestanding stores or shop-in-shops?

Yves Müller (CFO and COO): Store productivity over the last 12 months improved to a level of EUR 11,600 per square meter, clearly exceeding 2019 levels. The major drivers are traffic and strong conversion rates, mainly driven by our strong price-value proposition, the improved product mix in our stores, the renovation of stores, as well as the optimization and space reduction of oversized stores. Also going forward, we continue to aim at further driving store productivity, as laid out in CLAIM 5, as this will drive operating leverage.

We increased our EBIT guidance for full year 2022, now expecting EBIT within a range of EUR 310 million and EUR 330 million. A comparison with 2019, however, is not fully appropriate, as our CLAIM 5 strategy execution is in full swing! This means that we are having ongoing investments into the brands, the product and into digital. All this is aimed to make strong progress along our CLAIM 5 journey and fuel top-line growth to achieve EUR 4 billion sales and an EBIT margin of 12% in 2025. So we are not managing things with a focus only on the quarter, but are managing mid- and long term, and this means keeping brand heat high, further fueling brand momentum.

Regarding outlets, I can confirm that the sales share has decreased somewhat over time. Currently, the strongest growth within retail as compared to 2021 comes from freestanding stores, reflecting our focus on driving our full-price business. The latter enjoys very strong momentum as our current collections clearly outperform previous ones. And in relative terms, the growth in the full-price business is stronger for the time being than in the outlet channel.

Michael Kuhn (Deutsche Bank): Briefly on cost that become a bigger headwind over time. Can you differentiate between underlying OpEx inflation and the investments as part of CLAIM 5? Obviously, not that much about marketing, but all other cost items? Can you quantify what do you pay for rents and especially inflation-linked rents, for energy, and the current personnel cost share in OpEx?

Yves Müller (CFO and COO): Obviously, we are closely monitoring our cost situation. Overall, we are clearly in investment mode. We invest into marketing, into product, into digital and into retail. Regarding the latter, we are optimizing our store portfolio. As laid out in CLAIM 5, by 2025 we want to reduce our brick-and-mortar retail cost as a percentage of sales by around 700 basis points versus 2019 levels. So we want to drive efficiency in retail and we are well on track in executing this. Overall, however, there are a lot of different moving parts when it comes to rightsizing stores, renegotiating rents, etc. with some positive effects here and there compensated by cost inflation. So it's very difficult to model. But overall, please consider that we continue to drive efficiency in brick-and-mortar retail, thereby retail cost should go down as a percentage of sales going forward. Overall, as of today, we were able to mitigate the negative impact of inflation by price increases.

Thierry Cota (Société Generale): First, there has been a material drop in global freight prices and costs recently. While these have been very volatile over the year, based on where they are today, what kind of gross margin tailwind do you expect for next year?

Secondly, on your revenue growth expectations for Q4 that are implied in your new outlook. If we take the midpoint, revenue growth would drop to single digit in Q4 on a reported basis, even with price increases and the anticipated FX tailwind. And at the upper end, growth would be in the low teens. So this would imply quite a significant slowdown, particularly as you flagged that, as of today, you don't see any change in demand, which is highly encouraging, for instance given pretty weak German market data for apparel in October. So why this gap quarter-on-quarter, when comparing Q4 expectations to the most recent performance?

Finally, you mentioned delivery shifts in wholesale. Can you please quantify the headwind in Q3. And have there been any notable one-offs in Q3 EBIT?

Yves Müller (CFO and COO): On your last question: the wholesale delivery shift effect from Q3 into Q4 was around EUR 30 million. And there are no material one-offs in EBIT to call out.

On your first question, regarding freight costs. It's worth mentioning that freight costs are usually locked in with a time delay of around 6 months. Therefore there is always some kind of time delay before the positive impact becomes visible in the P&L. This said, if freight costs stay on the current low level, the gross margin tailwind would be around 50 to 100 basis points for 2023 and the outer years.

Regarding the revenue guidance, this year we rather "under promised and over delivered", having taken a rather cautious stance as we are living in a world of elevated macroeconomic uncertainties. So far, however, we have not experienced any slowdown in consumer demand, and that also includes Germany.

Rogerio Fujimori (Stifel): First, on strong current trading in the U.K. We know you had an important flagship store opening lately on London's Oxford Street. How have you been able to decouple from the broader retail trends we see in the U.K.?

Secondly, on gross margin for Q4. How should we think about the building blocks relative to Q3 in terms of FX, sourcing, cost inflation, the price increases, eventually any levels of promotional activity that you're expecting in Q4?

Yves Müller (CFO and COO): Regarding current trading: overall, we have a very strong positioning in the U.K. We have a very high market share in menswear, close to 10%.

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And yes, we have opened a new flagship store on Oxford Street, and we will have a store event next week. However, on the other hand, our Regent Street store is currently closed for renovation. All this said, our performance in the U.K. is very strong, emphasizing the fact that these days, the stronger brands outperform the weaker brands.

Regarding gross margin, which we are guiding to be at least on the prior-year level in 2022. After the first 9 months, we are actually 80 basis points above last year. We are at 62.0%, which is at the top end of our CLAIM 5 guidance range, with the outperformance versus last year clearly reflecting the ongoing strong momentum in our full-price business, as well as overall less discounting in the wake of our strong brand momentum. For Q4, we expect the moving parts to be quite similar: freight costs will remain on an elevated level, impact of FX will most likely be negative again. On the other hand, we continue to expect lower discounts and higher full-price sales year over year.