Transcript – Q&A Session

May 4, 2023

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.

Grace Smalley (Morgan Stanley): First, on order books: given your increased revenue guidance for full year 2023, can you please quantify the trends in your order books, as you called out robust trends. And are there any forward-looking indicators that are giving you confidence in the expected ~10% revenue growth for this year?
Secondly, on inventories: given elevated inventory levels in Q1, can you be more specific on what you expect in terms of that gradual normalization in inventories going forward? What should we expect in terms of inventory growth in Q2, and what by the end of this year? And then, beyond your own inventories, please also comment on the state of inventories at your wholesale partners.

HUGO BOSS

Yves Müller (CFO and COO of HUGO BOSS): First, on wholesale orders: we are currently in the sell-in phase for our Winter 2023 collections and it is still too early to comment on this. But regarding our order books for Fall 2023, which have already been concluded, we saw very strong demand. We are very encouraged by the development of our wholesale business, and we continue to enjoy strong momentum, as we see partners continuing to increase their orders. This also gives us a good indication that the sellout at our wholesale partners is extremely well. We are clearly gaining market shares, and we are very happy with our order intakes.
Secondly, on inventories: as already highlighted back in March, we expect inventories in the first half of the year to continue increasing. This said, and as supply chain disruptions are now easing, we anticipate a gradual normalization of inventories in the course of the year, starting from mid-of 2023 onwards. Overall, for 2023, we target inventories to decline moderately vs. 2022-levels in absolute terms.

Jürgen Kolb (Kepler Cheuvreux): First, on your FY/23 guidance: how much of the EBIT guidance increase is due to the expected stronger sales growth and how much is due to additional relief from lower logistics costs or raw material prices?
Secondly, on current trading: You are sounding very optimistic and positive about the current momentum. Can you provide us with some current observations from the individual markets, in terms of April trading by region?

Yves Müller (CFO and COO of HUGO BOSS): On current trading. We are very happy with the overall performance in April. As of today, we have not seen any material changes in consumer demand. Asia/Pacific is performing strongly, driven by the reopening of China. And while the comparison base from last year is somewhat low given last year's lockdowns in China, especially in Shanghai, also from an absolute point of view, China is performing strongly. And also, across our other two regions, EMEA and the Americas, so far, we continued our strong momentum.

Regarding our guidance increase in terms of EBIT: first of all, we will implement a second round of price increases starting with the Fall 2023 collection from May onwards, in order to compensate the increased sourcing costs. Secondly, we continue to be optimistic for the second half of the year when it comes to gross margin improvements. Thirdly, and as we experienced already in Q1, we continue to drive operating leverage, especially in our brick-and-mortar retail business. So based on our forecast of an at least stable gross margin for full year 2023, and anticipating further efficiency gains, we remain fully committed to improve our profitability this year. In 2022, we improved our EBIT margin by 100 basis points to a level of 9.2% and, as laid out in our guidance for fiscal year 2023, we remain fully committed to increase our EBIT margin also this year.

Manjari Dhar (RBC Capital Markets): First, please quantify the major moving parts within your gross margin in Q1.
Secondly, please give a little bit more color on the FX impact to net financial expenses.

Yves Müller (CFO and COO of HUGO BOSS): On gross margin: simplifying this by taking all things into account, the slight decline of 30 basis points in Q1 was mainly related to some negative FX effects reflecting the stronger U.S. dollar versus the euro year over year. Going forward however, and based on current exchange rates, we expect currencies to rather become a tailwind for gross margin development, particularly in the second half of the year. At the same time, in Q1 we succeeded in broadly compensating for ongoing elevated sourcing costs thanks to our pricing initiative, which we successfully implemented in the second half of last year.
Secondly, on net financial expenses: First of all, we recorded higher interest expenses related to the discounting of lease liabilities under IFRS 16 against the backdrop of the rising interest rate environment. And this factor will remain. Besides that, an unfavorable development of foreign exchange rates contributed to the increase in net financial expenses, in particular with regard to the Russian ruble.

HUGO BOSS

Chiara Battistini (JP Morgan): First, on pricing versus volumes: What was the contribution from pricing versus mix versus volume in Q1? And how to think about that for the full year?

Secondly, on your full-year sales guidance: what assumptions did you embed for the American market, given the steep change in growth that you saw in Q1?

Yves Müller (CFO and COO of HUGO BOSS): On prices in Q1: as a reminder, we increased our prices back in summer 2022 within the mid-single-digit range for our full price collections and we will do another price increase for the Fall 2023 collection, which will be delivered and distributed starting from May onwards. Taking this into account, I assume that the pricing effect in Q1 had an impact in the low single-digit range. And it will be around mid-single-digit starting with the second half of this year.

Secondly, on the Americas: for full year 2023, we expect high single-digit to low teens growth in reported terms.

Thomas Chauvet (Citi): First, to confirm what you said on April trends: Are you saying that at Group level, April is in line with the strong double-digit growth you've seen in Q1? And if so, the ~10% sales guidance for the full year implies a mid- to high single-digit year-on-year growth for the remainder of the year, and also a sharp slowdown in terms of 4-year stack growth. So, do you expect to start suffering in some geographies from macroeconomic headwinds?

Secondly, on retail productivity: I expect that you recorded a robust improvement in store productivity also in Q1. Please elaborate on your store optimization program and whether you still regard 400 stores at the end of 2025 as the right number?

Yves Müller (CFO and COO of HUGO BOSS): First, on our top-line expectations. First of all, let me confirm once again that current trading looks very strong and that we remain very happy with the overall performance. Within our full-year guidance, we continue to factor in the elevated macroeconomic and geopolitical uncertainties. This being said, we must also not forget that the comparison base versus last year is becoming increasingly more difficult starting with the second quarter, given last year's strong performance.

On store optimization: we are currently operating 472 freestanding stores worldwide. And we are continuing our store optimization program. It's visible in our P&L that we are making progress quarter-over-quarter in reducing our brick-and-mortar retail cost as a percentage of sales. In terms of the further development of the number of freestanding stores, we will provide you with an update on our Capital Markets Day on June 14 and 15. And on store productivity: we recorded strong store productivity improvements last year and another 18% improvement now in Q1. We are now standing at a level of around 12,200 Euros per square meter in brick-and-mortar retail. This is a very strong performance, better than we originally expected. As this also has implications for our medium-term thinking on our store network, we will give you an update at our Capital Markets Day.

Andreas Riemann (ODDO BHF): First, on BOSS Camel. How is the performance? In which markets do you sell BOSS Camel? And what is the plan going forward?

Secondly, on your full-price business: your full-price business supported the gross margin in FY 2022 and also in Q1 2023. Where are you on this journey: have you now reached a certain limit that is difficult to cross? Or are you halfway there?

Yves Müller (CFO and COO of HUGO BOSS): On BOSS Camel: to put everybody on the same page, we started with this brand line in Fall/Winter 2022 and we are continuously improving this collection. It sells extremely well in the Asian markets, but we are also selling it in EMEA and in the Americas. BOSS Camel is a perfect bridge to affordable luxury as the collection resonates very well with the consumer. We are improving collection by collection, and we are gaining more traction on BOSS Camel.

On full-price sales: we already improved our full-price sell through last year. Also now, our full-price sales remained strong throughout the entire first quarter. So, we remain very happy with our full-price sell through. On the other hand, you can always improve your full price sell-through rates. So, there are still opportunities to further improve in the quarters and years to come.

Michael Kuhn (Deutsche Bank): Firstly, on Asia and specifically on China: you achieved 25% growth on relatively low comps. So, there is improvement, but not significant improvement. Do you see further improving momentum in that region? And would you say that the brand relaunch in China is as successful as in other regions?
And secondly, on free cash flow, which was quite negative in the first quarter, including the working capital effect. With regards to the expected improvements later in the year, what level of free cash flow should we expect you to generate in 2023?

Yves Müller (CFO and COO of HUGO BOSS): Actually, I disagree with your finding that our performance in China is relatively bad. 25% is a very strong performance because in Q1 of last year, the stores were still open. The lockdowns actually started in Q2. The performance is also strong compared to pre-pandemic levels. So, we are very happy about the start in Q2 and we see tremendous progress. And even now, in the first days of May, we see very strong results in China.
Regarding free cash flow: the free cash flow generation will be rather back-end loaded, towards the second half of the year. We are well aware of how our trade net working capital will develop. And we are going to invest EUR 200 million to EUR 250 million in terms of capital expenditure.

Rogerio Fujimori (Stifel): Firstly, you flagged that the promotional activity levels were down year-on-year in Q1, given the strong momentum of the brands. Was there any change in April? And any change on how you are budgeting for the remainder of the

year, given what you see at competitors? Or does your EBIT guidance have a buffer for higher promotional activity in H2?
Secondly, please comment on what was driving your 34% growth in brick-and-mortar retail in the Americas, which is obviously well ahead of anything that we see across the sector.

Yves Müller (CFO and COO of HUGO BOSS): First, regarding the U.S.: We are very happy about our performance in the U.S. We still have tremendous opportunities and potential in the U.S. As you might recall, our sales levels in the last years were almost on the same levels like in the U.K. So, if you take the population times 6, there is lots of potential in the U.S. Also, our 24/7 lifestyle brand image is now much more visible in the U.S. where we used to be perceived as a "suit only" brand in the past. With the introduction of sportswear, we strongly improved the perception of our brand. Also, our cooperations, such as with the NBA or, most recently, the NFL, help us to gain traction, especially among younger consumers, thus enabling our customer base to grow nicely in the U.S. And don't underestimate the celebrities that we are collaborating with. Also, we took the deliberate decision to go to Miami for our BOSS Fashion Show. So we continue to invest in the U.S., where we still see a lot of growth potential.
Secondly, regarding promotional activity, which in Q1 was on par with the prior-year level. We are enjoying strong brand momentum. Also, in April and May, we don't see that promotional activity is increasing. So for the time being, we are happy with the current development.

Rogerio Fujimori (Stifel): So, does your gross margin guidance includes a buffer for higher promotional activity in H2?

Yves Müller (CFO and COO of HUGO BOSS): Please understand that we don't comment further on the drivers within our gross margin guidance.

Antoine Belge (BNP Paribas): Firstly, can you please elaborate further on the different key markets in Europe?
Secondly, regarding the correlation between margins and top line. If I'm going to run the numbers here, EUR 4 billion of sales and EUR 400 million in EBIT would imply a 10% EBIT margin. Originally, you aimed for delivering EUR 4 billion of sales and an EBIT margin of 12% by 2025. So, is it all due to supply chain costs and freight inflation? Or did you decide to invest more into the business given that the top-line growth was stronger than originally expected?
Finally, on you Capital Markets Day: Are you going to update 2025 targets? Or, since we are in 2023, are you going to go give targets until 2027 or 2028?

Yves Müller (CFO and COO of HUGO BOSS): Starting with the question on our Capital Markets Day: Please understand that I won't comment on what we are going to communicate at our Capital Markets Day at this point in time.
On your first question regarding EMEA performance: In Q1, we recorded a very strong performance in Germany, up 28%, a very strong performance in France, plus 17% and an excellent performance in the Middle East being up high double-digit. Performance in the U.K. was on par with the prior-year level, given the high comparison base last year. However, compared to pre-pandemic levels, the U.K. was growing 33%, thus even exceeding the levels of Germany and France. Overall, the strong performance in Europe in Q1 was broad-based, but with different comparison bases.
And, regarding our guidance: you already gave half of the answer, which is that freight cost and also sourcing cost increased. Also, the optimization of our store network takes some time as we won't renovate all our freestanding stores at once, but rather 100 to 120 stores each year. So, while the sales of EUR 4 billion are in sight 2 years earlier, we remain fully on track to also further improve our operating margin going forward, especially when it comes to driving further efficiency gains in brick-and-mortar retail.

Louise Singlehurst (Goldman Sachs): First, going back to the overall environment. You had a very strong start to the year. Can you provide any color around traffic and conversion rates, and how that might differ across regions?
Secondly, on brick-and-mortar retail and wholesale, where growth rates have been comparable, both up 26% in Q1. Is there anything to highlight in wholesale? Can you elaborate on the opportunity for new wholesale doors in the U.S.? And what was the impact of new space in Q1?

Yves Müller (CFO and COO of HUGO BOSS): Sales growth in brick-and-mortar retail was 26% while store productivity was up 18%, mainly driven by higher traffic across regions. Also, average retail price and sales per transaction improved. As we are fostering our 24/7 lifestyle brand image, units per transaction are increasing, as we dress our customers from head to toe, which is improving our ticket.
Regarding the U.S. market and the opportunities for further doors. We have a very strong business with Macy's within the concession model. We added an average of around 20 doors over the past collections. Macy is very happy with our performance and thus, we are getting more doors. We are now at around 80 doors and we are expanding to Tier 1 and Tier 2 cities to exploit further growth opportunities. The same is true for big partners like Nordstrom where we are expanding, for example, with BOSS Camel and BOSS Womenswear.

Thierry Cota (Société Générale): Two follow-up questions. First, on the balance sheet: You expect inventories to be down in absolute terms at year-end, with trade working capital as a percentage of sales up 2 percentage points. Inventories should be down as a percentage of sales in that situation. Is it correct to assume that the rise will come from a less favorable payables and receivables development?
Secondly, back on revenues and on the stores, could you give us the percentage of stores which were refurbished as of today? How do sales densities compare between before and after the refurbishment?

Yves Müller (CFO and COO of HUGO BOSS): First of all, you are right that we expect inventory levels in absolute terms to be down at year-end. On the second part of your assumption, you are wrong because for trade networking capital as a percentage of sales, which we are guiding to be at around 17% at year-end, you need to consider the moving average of the last 4 quarters, divided by the sales of the last 12 months. So, it also includes the TNWC levels of Q1, Q2 and Q3. And since they are elevated, this will also drive the moving average.

Regarding the progress on renovating our freestanding store network: by the end of Q1, around 1/3 of our store universe is meanwhile either new or refurbished. We will be more explicit at the Capital Markets Day, but once we remodel a store, we see a decent increase in productivity, above our expectations.