HUGO BOSS

Transcript – Q&A Session

November 4, 2021

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 your guidance. The market has perceived your 2021 fiscal year EBIT guidance as a bit conservative. You have clarified that you intend to grow your OpEx and invest more starting from the fourth quarter. Can you be a little bit more precise there? What's the level of OpEx inflation that we should expect going into year-end? And how will gross margin evolve? Typically, the fourth quarter has a relatively high gross margin level – should we expect this to happen? Or are you already investing into the product, which is one of the reasons why your gross margin, over the medium-term, is about to move somewhat down?

Secondly, on your strategic priorities going into fiscal year 2022. You've laid out quite a few of them. You've talked about a new store format, your focus on digital and that you've hired several new managers. But you have also a lot going on in terms of rebranding, having 'BOSS Orange' and other sub-brands reemerging as well. So how should we think about fiscal year 2022 and all the initiatives that you have laid out in August; what is going to come through over the next 12 months?

Yves Müller (CFO): On current trading: in the month of October, we have seen an acceleration in our top line, something that we view as very positive as we are clearly enjoying strong momentum. On the other side, for the months of November and December, we still see some uncertainties. Especially in Europe, infection rates are rising again, and there are some uncertainties around what the local authorities will be doing in terms of restricting public life. We have seen lockdowns in some Eastern European markets, including Russia. We are thus a little bit cautious when it comes to the remainder of the year. Please be aware that Q4 is very important for our business because of the holiday season, and a lot of commercial events taking place. On top of that, while we expect no material impact from the ongoing supply chain disruptions on our top-line in Q4, current headwinds with regard to freight and duty cost are expected to continue weighing on our gross margin also in Q4 – in around the same magnitude that we have experienced in Q3. We are monitoring this very closely. On OpEx, fully in line with our CLAIM 5 growth strategy - we want to double the business from around EUR 2 billion in 2020 to EUR 4 billion by 2025 –, we will invest into our business, more specifically into our brands and marketing, as well as into digital. So we will clearly step up our investments already in Q4, something that is reflected within our guidance.

Regarding our strategic investments in 2022, I can assure you that we are clearly putting the pedal to the metal at full steam. In line with our claim of "Boosting Brands", already in January, the branding refresh will become visible within our Spring Summer collections, as our products will be incorporating the new branding; and a clear point of difference will become visible for our consumers. We will accompany this with a big marketing campaign for both brands, BOSS and HUGO, kicking off at the end of January – something that will clearly boost both brands right at the beginning of the season. In terms of our claim "Product is King", our Spring Summer collection will incorporate the branding refresh, while also our brand lines – Green, Orange, Camel – will become visible. Order intake from our wholesale partners on these collections has been up double-digit. In early 2022, we will also relaunch our online flagship hugoboss.com, thus improving the customer journey and – importantly – drive traffic and conversion, something that our Digital Campus is working on right as we speak. Another important step in Q1 will be the roll out of our new store concept, as our new anchor store in London Oxford Street will open in the first quarter of 2022, something we're all very excited about. As you can see, execution of our CLAIM 5 strategy is really in full swing. Our strong Q3 results are a clear proof positive that we are going into the right direction. And there is much more to come, starting in early 2022.

Elena Mariani (Morgan Stanley): You say that you're going to invest more in the fourth quarter. In Q3, OpEx was up 2% versus 2019. For Q4, should we expect OpEx to be up, for example, high single digit versus 2019?

Yves Müller (CFO): Yes. Already in Q3 we saw that marketing investments were up by 6% versus 2019. So with the range that you were indicating, you are more or less there.

Jürgen Kolb (Kepler Cheuvreux): First, can you give us some indications on China? In Q3, how did sales develop in your own stores and online? And what are you seeing so far in Q4?

Secondly, on the pricing strategy for Spring Summer 2022, and for Fall Winter 2022. What's your strategy in terms of pricing for next year?

Yves Müller (CFO): Sales performance in China was somewhat muted from the end of July throughout much of August, given new COVID restrictions having weighed on store traffic, with people traveling less but rather staying at home. On the other hand, our business in China has clearly gained momentum towards the end of the quarter. In the month of September, sales exceeded 2019 levels in the high teens, while having even accelerated in October. While we regard this as a clear positive sign, there are uncertainties around COVID-19 remaining for the months of November and December. But we are cautiously optimistic, as October has seen an acceleration in both channels – brick-and-mortar and online.

In terms of our pricing strategy for 2022, and the increase in raw material prices and freight cost: for the time being, we have not taken the decision to adjust our prices, but we will continue to monitor the situation very closely. We will most likely decide in early 2022, if there will be a persisting trend of cost inflation within our industry.

Antoine Belge (Exane BNP Paribas): First, on gross margin: can you please quantify the impact of your initiatives with regard to mitigating supply chain headwinds in Q3? Do you expect this to be around the same level in Q4? And, consequently, what is your expectation on gross margin for full year 2021. In the past, you indicated that gross margin in 2021 is expected to come in somewhere between the levels recorded in 2019 and 2020. Is it fair to assume that now, gross margin should be somewhat closer to the 2020 level?

Secondly, regarding your view on the U.S. market, which seems to be on fire for your company. Some consumer goods companies are a bit cautious about what's happening in the U.S. So what's your view on a possible "hard landing" of the U.S. market? And maybe some comments more specifically around HUGO BOSS, especially in terms of your initiatives of increasing the quality of distribution beyond recent collaborations with the NBA and Russell Athletic?

Yves Müller (CFO): On gross margin, it is fair to assume that higher freight and duty cost related to the global supply chain disruptions will continue to weigh on our gross margin for the time being. As a consequence, we expect Q4 gross margin to come in at around the same level as in Q3 – which is somewhat lower than we had originally anticipated, due to the increase in freight cost, which has been a hit of around 160 basis points in Q3 as compared to 2019 levels.

Regarding the U.S. market, I can confirm that we recorded an acceleration in sales momentum in the month of October. Business thus remains strong, especially driven by local demand. In November, when international tourism is expected to pick up again, we expect further tailwind to our self-managed turnaround in the U.S. With our new management team, we have successfully changed our brand image in the U.S. over the last 18 months, from a "suit-only" company to a true 24/7 lifestyle brand, with the collaborations of BOSS and Russell Athletics as well as the NBA clearly supporting in this regard. We see a lot of new, younger customers, and they are rebuying. Overall, our U.S. business is clearly going into the right direction, and we are confident that this will continue.

Michael Kuhn (Deutsche Bank): You already flagged the risks for the fourth quarter. How are recent developments – for example the renewed store closures in some markets – impacting your business? Are the rising infection rates in several European markets already impacting store traffic?

Yves Müller (CFO): It's too early to comment on this. The lockdowns in Russia, for example, will be only temporarily, as we have to close our stores for around 10 days. On the other hand, for example, as lockdowns in Australia have now been lifted, we are recording decent performance in this market. Therefore, it depends – market by market –, so it's clearly too early to call it out. And while I already commented on current trading in October, we will have to observe developments now week by week.

Michael Kuhn (Deutsche Bank): So no impact yet on store traffic from the rising infection rates?

Yves Müller (CFO): No.

Philipp Frey (M.M. Warburg): First, did I get it correctly that bonus accruals drove the increase in your admin expenses in the third quarter?

Secondly, on 2022, given the supply chain disruptions: what's your view on the ordering behavior of your wholesale partners? Do you fear that there is "over-ordering" occurring? Or are you gaining market share as you were one of the few brands who's committing to volume?

Yves Müller (CFO): I can confirm that the increase in admin expenses is related to higher payroll cost in terms of accruals for short-term and long-term incentives, reflecting our recent business performance, and also recent share price performance, as our Long-Term-Incentive-Program is linked to the latter, among other things.

Secondly, the strong increase in our order intake for Spring Summer 2022 is NOT linked to our wholesale partners buying out of the situation of fearing shortages from supply chain issues. We are fully confident that this is first and foremost reflecting our branding refresh and our great product improvements within our collections. So we haven't witnessed that partners were overbuying because of supply chain issues. At the end, we clearly want to be more relevant to the end consumer with good products, and we want to gain market share.

Rogerio Fujimori (Stifel): First, on new retail space contribution, which was around five percentage points in Q3 and year-to-date. Should we expect a similar level of new retail space contribution also in Q4 2021 and in FY 2022, based on planned store openings?

On the Americas, where total own retail points of sale increased from 269 at the end of Q2 to 301 at the end of Q3. As the number of freestanding stores remained broadly stable, what happened in Q3 in terms of shop-in-shops and outlets? Or in other words, what was the contribution from space to retail growth in the Americas in Q3?

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Yves Müller (CFO): Regarding retail space in Q4, you should not expect major changes as it is the most important quarter from a commercial perspective and you don't do major renovations in Q4. Space should thus remain rather stable.

Regarding the U.S., we added around several shop-in-shops to our business in Q3. At Macy's, for example, we added 17 shop-in-shops, reflecting our strong business with that partner. In terms of our strong Q3 performance in the U.S., however, this was no major driver.

Thierry Cota (Société Générale): First, can you comment on promotionality at the end of Q3 and potentially in Q4? Did promotionality in your industry has come down, also given ongoing supply chain disruptions? Gross margin in Q3 was potentially better than what we expected at the beginning of the summer.

Secondly, on the acceleration of your business in October: is this over 1 year, or also on a 2-year stack basis?

Finally, on your comments related to the store network. I was wondering about the broadly stable number of freestanding stores as compared to the rise in the number of overall points of sale. Besides the new shop-in-shops in the Americas, have there been any other factors, i.e. shop-in-shops elsewhere and/or potentially outlets?

Yves Müller (CFO): First, regarding markdown activity, I can clearly confirm that it was lower in Q3 as compared to Q2.

On current trading in October: yes, I was referring to an acceleration of our top-line performance on a 2-year stack basis, as this is the best comparison base for the time being, reflecting pre-pandemic levels.

Finally, on retail points of sale: the number of freestanding stores is more or less stable as we are still in the middle of optimizing our store portfolio in line with our CLAIM 5 strategy. We are investing into those locations that are very promising and good for the brand. So the increase in total points of sale was primarily related to shop-in-shops, first and foremost at Macy's in the U.S., and at Hudson's Bay in Canada.

Thierry Cota (Société Générale): So, as you said previously, space is not going to have much of an impact either on Q3 or going forward?

Yves Müller (CFO): Yes, correct.