HUGO BOSS

Transcript – Q&A Session

November 5, 2024

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.

Frederick Wild (Jefferies): Could you provide insights on current trading in September and October, ideally with a regional split?

Secondly, on gross margin in Q4, how are you accounting for factors like freight costs, promotional activity, and FX impacts? It seems the full-year gross margin might come in below 62% – any comments on that?

Yves Müller (CFO/COO of HUGO BOSS): Regarding current trading, we observed a gradual improvement from July through September, with October performing similarly to the end of Q3. This is encouraging, though we remain prudent given current consumer sentiment and macroeconomic uncertainties.

On gross margin, we recorded a 200-basis-point structural improvement from sourcing efficiencies in Q3, but some external factors had a greater impact than expected. Freight rates, which have stayed elevated since March, negatively impacted gross margin by about 100 basis points. Promotional activity remained somewhat elevated, consistent with prior quarters, and impacted margin by approximately 50 basis points. Looking to Q4, we expect to maintain the structural improvements in gross margin. On the other hand, freight costs are likely to stay elevated in the near term – although we expect a certain relief to come in over the next months and quarters. Promotional activity is anticipated to remain at similar levels we have seen so far this year. This said, Q4's comparison base will be somewhat easier, which should also support performance as we close out 2024.

Grace Smalley (Morgan Stanley): First, on OpEx: based on previous guidance for H2, we understood that OpEx control would be more weighted toward Q4, yet you've already shown strong OpEx control in Q3. Could you clarify what drove this better-than-expected performance? Also, what is your outlook for Q4 OpEx growth? If promotions should remain a headwind for gross margin in Q4, are there additional levers in the OpEx base to offset that?

Secondly, can you provide any updates on your 2025 targets, specifically the sales goal of EUR 5 billion and the EBIT margin target of at least 12%, and how we should view the timeline for achieving these?

Yves Müller (CFO/COO of HUGO BOSS): Regarding OpEx, as we discussed in August, our goal was to limit OpEx growth to low single digits in H2. We achieved strong cost control in Q3, positioning us at the lower end of this range, and we aim to maintain this level of control in Q4, keeping underlying OpEx growth limited to low single digits. On promotions, we expect them to stay relatively stable in Q4 vs. Q3, without further deterioration. We've seen that many competitors have destocked their inventories, and we anticipate maintaining our position without increasing promotional intensity.

As for our mid-term targets, namely EUR 5 billion in sales and an EBIT margin of at least 12%, given the ongoing macroeconomic uncertainties, it's likely these will take longer than 2025 to achieve. We will provide a more concrete update on our 2025 outlook in March. At the same time, our "CLAIM 5" strategy is set to run through 2025, and we'll provide an update on our mid-term strategy over the course of 2025.

Manjari Dhar (RBC Capital Markets): Following up on Grace's question, in Q2, you mentioned ramping up savings initiatives through the second half. Could you provide more detail on potential savings expected in Q4 and possibly next year? Also, how much of these savings might be sustainable long-term?

Secondly, can you share insights on the competitive landscape and your outlook on opportunities to gain additional market shares?

Yves Müller (CFO/COO of HUGO BOSS): Regarding cost savings, our approach centers on creating structural efficiencies. One example is our sourcing efficiencies, which have resulted in a structural gross margin improvement of 200 basis points in Q3. But we're not only addressing cost of goods sold but also focusing on overall cost efficiencies, including marketing. We've made progress in maximizing the impact of each euro spent on marketing, as evidenced in Q3. Our marketing-to-sales ratio stands at 7.4% in Q3, fully in line with our target range of 7% to 8%. On the administrative side, we've made strides in controlling expenses by implementing a hiring freeze and reducing spending in non-business-critical areas. A key element in our cost management strategy is aligning costs with sales development, and in Q3, this was effectively executed: sales growth came in at 1% currency-adjusted, while we successfully reduced our cost growth rate from 9% to 1%, a notable achievement.

In terms of the competitive landscape, we indeed continue to gain market share, especially in the wholesale channel, where we operate in a multi-brand environment. Our strong price-value proposition and the appeal of our brands' 24/7 lifestyle image have been instrumental in this success. Additionally, our order book for the upcoming spring and summer seasons is robust, indicating that we are well-positioned to maintain our market share. Notably, we also saw a promising uptick in our replenishment business in Q3, with wholesale reorders gaining momentum.

Jürgen Kolb (Kepler Cheuvreux): First, on China: although China now accounts for only 5% of your business, it's clearly a weak market environment currently. Are you considering any strategic adjustments, such as reviewing your store network or making supply chain changes? You mentioned a new store opening, which suggests you're not planning to reduce exposure, but any further comments on China would be helpful.

Secondly, on free cash flow: earlier this year, you provided a guidance of around EUR 500 million. Do you still anticipate achieving that, or are there any potential revisions?

Yves Müller (CFO/COO of HUGO BOSS): Yes, regarding China, the current exposure is indeed around 5%. Strategically, we are prioritizing larger store formats to enhance the customer experience, which aligns with Chinese consumer preferences. That's why we are opening a "halo" store on Nanjing Road in Shanghai this December, adding to last year's opening in Guangzhou. Typically, our store sizes in China are smaller than our international locations, so we're shifting to larger spaces there to meet demand for a premium customer experience. On the product side, Chinese consumers currently favor sports-oriented items, which aligns well with our BOSS Green line, especially lighter outerwear. They are also favoring BOSS Camel, currently making up about 25-30% of our assortment in China, but BOSS Green is expanding rapidly. Our digital approach has also evolved, with strong growth on TikTok, where we are actively engaging through live-streamed product offerings. While Tmall has been challenging, our TikTok presence is strong, driving sales and brand visibility.

Year-to-date free cash flow, including IFRS 16, stands at approximately EUR 200 million – a notable improvement of around EUR 280 million when compared to last year. However, reaching the EUR 500 million target would require an additional EUR 300 million in Q4. Given the current macroeconomic uncertainties and weak consumer sentiment, achieving this level may be difficult, but we remain focused on getting as close as possible to that target.

Michael Kuhn (Deutsche Bank): First, on product initiatives: you mentioned the positive contribution from HUGO BLUE this quarter, and we're also seeing contributions from the "Selected by Beckham" product range. Could you provide a recap of those impacts and outline your plans for the coming quarters, especially considering that the dedicated capsule collection with Beckham is yet to launch?

Secondly, regarding brick-and-mortar retail, could you share insights on space productivity in the recent quarter and your expectations for the next few quarters?

Yves Müller (CFO/COO of HUGO BOSS): Regarding product initiatives, we're pleased with the performance of HUGO BLUE, which is projected to account for up to 10% of HUGO's sales by year-end. As for our collaboration with David Beckham, he featured in our BOSS Fall/Winter campaign launched in August, significantly boosting social media engagement – more than double compared to last year's figures. Dedicated product initiatives with Beckham will kick off at the end of January 2025 with a prominent underwear campaign, where we'll spotlight key products alongside Beckham. So this partnership is expected to have a commercial impact starting in Q1 2025.

As for brick-and-mortar retail, retail productivity in Q3 declined by 6%, currently at EUR 11,600 per square meter. This decrease was primarily driven by lower traffic, although we've offset this somewhat with higher conversion rates and increased sales per transaction. Lower consumer sentiment continues to impact traffic globally, particularly in mono-brand environments. However, in multi-brand environments, such as department stores, we see higher footfall and are gaining market shares.

Rogerio Fujimori (Stifel): Could you provide some detail on the best-performing categories and price points for BOSS Menswear, BOSS Womenswear, and HUGO in Q3, as well as any categories or price points that underperformed?

Additionally, could you elaborate on recent retail trends in the UK, both for brick-and-mortar retail and hugoboss.com?

Yves Müller (CFO/COO of HUGO BOSS): Starting with the UK, we observed a slight improvement quarter-over-quarter in both brick-and-mortar and digital channels compared to last year. While sales are still down year-over-year, there are indications that the market may have reached the through.

In terms of product categories, formalwear, particularly performance tailoring, has been a top performer. We're also making substantial progress in shoes and accessories for both Menswear and Womenswear, including a strong sneaker offering.

Zuzanna Pusz, UBS: First, on channel dynamics: you've highlighted strong wholesale performance and noted that third-party digital has also been strong. Typically, wholesale would trend closely with retail, but could you explain this divergence? Are you expanding points of sale or gaining market share in wholesale?

Secondly, on OpEx, you've managed costs very effectively, but is there a limit to how much you can reduce? Given your historically lean approach, could you reach a point where further cuts become challenging if market trends stay weak?

Yves Müller (CFO/COO of HUGO BOSS): First, on the difference between retail and wholesale performance, our retail, which is mostly mono brand, has been impacted by low traffic. However, in the multi-brand wholesale environment, we are outperforming due to a strong product lineup and competitive price-value proposition, which is resonating well with customers. This competitive edge helps us gain market share, especially in multi-brand setups where comparisons with other brands highlight our value. This trend holds true for both offline wholesale and our digital wholesale channels. Specifically, in Q3, our digital partnerships showed strong results, driving total digital up by 6%. This outperformance relative to peers is driven by our consistent value offering across both online and offline channels.

On the cost side, there is still room for optimization: in terms of gross margin, we will continue to improve our sourcing efficiencies through vendor consolidation and by reducing the complexity of our collections, allowing us to buy more units per SKU. This helps optimize cost structures within our COGS. At the same time, we also see opportunities to further optimize our store portfolio, including adjusting the mix across our good, better, best locations to further control OpEx.

Zuzanna Pusz, UBS: Could you provide any specifics on your wholesale account base? For instance, how many wholesale accounts do you have now compared to last year?

Yves Müller (CFO/COO of HUGO BOSS): Our wholesale growth is largely based on our existing accounts. Currently, our top 20 wholesale accounts contribute close to 60% of our wholesale business, which highlights a concentrated portfolio. We're focused on growing with these top partners, aligning closely with their needs and our "win with the winners" approach. Additionally, our wholesale brick-and-mortar channel includes the franchise side. Over recent years, we've added around 80 new mono-branded franchise stores, particularly in regions like Latin America, Southeast Asia, the

Middle East, and Eastern Europe. This expansion is factored into our overall wholesale growth trajectory.

Thomas Chauvet (Citi): First, on digital: you mentioned the 6% digital growth in Q3 was mostly from multi-brand partners. Could you break down the growth between digital wholesale and digital retail in Q3, and perhaps year-to-date? And what is the share of own retail within digital this year?

Secondly, on gross margin, could you share how much air freight usage has come down over the past 12 months and any further reductions you expect? You mentioned recent increases in freight costs – were these across all types of freight, including sea containers?

And lastly, following up on store productivity, what was the year-on-year square meter increase in brick-and-mortar retail for both Q3 and the nine-month period?

Yves Müller (CFO/COO of HUGO BOSS): As laid out, our overall digital growth of 6% in Q3 was driven by the robust performance of our digital partner business. On the other hand, digital retail itself was relatively stable in Q3. Overall, the shares of retail and wholesale within digital are broadly equal.

On gross margin and air freight, we are currently at a low to mid-teen percentage for air freight in our overall freight mix, and we aim to reduce this further to a high single-digit share. This ongoing reduction has a positive impact on costs and our environmental footprint, with improvements expected to continue into 2025. As for the recent freight cost increases, these were broad-based, affecting both sea and air freight spot rates.

Regarding store productivity, we experienced a low single-digit increase in retail space year over year.

Martin Ben Rada (Goldman Sachs): First, regarding the freight impact on gross margins, your comments on the pressures and headwinds were helpful, but how far into next year do you anticipate this being a headwind?

Secondly, on the growth in your wholesale order books: when we last spoke, it was around the mid- to high single-digit growth level. Can you provide any updates on that?

Yves Müller (CFO/COO of HUGO BOSS): As for freight rates, we are actively working to reduce our air freight share as part of our structural improvements. This reduction will have a positive impact on our gross margins moving into next year. However, if higher freight rates persist, they could negatively impact our margins. We will provide more guidance on this in March 2025.

Regarding our wholesale order books, I can confirm that we recorded growth in the mid- to high single digits for the spring and summer collections. However, for the fall collections, it's too early to provide a precise update, as we are just beginning the selling phase, which started two weeks ago.

Anthony Charchafji (BNP Paribas): First, regarding HUGO BLUE, you mentioned it should represent close to 10% of HUGO's sales by year-end. I assume primarily through wholesale, with low cannibalization of the rest of HUGO. If we exclude HUGO BLUE from your wholesale figures, would it be fair to say that the underlying wholesale performance would be rather flattish rather than up mid-single digits?

Secondly, on retail in terms of contribution from space and like-for-like. The first half showed low single-digit space contributions. Can you provide an update on that and your expectations for next year?

Lastly, do you anticipate any price increases?

Yves Müller (CFO/COO of HUGO BOSS): Regarding the performance of HUGO BLUE: first, I can confirm that in brick-and-mortar wholesale, BOSS grew around 4%, hence in line with our overall performance. And even if we exclude HUGO BLUE, the overall performance in brick-and-mortar wholesale would still be in positive territory, however somewhere in the low single digits.

Regarding like-for-like retail sales, due to our extensive renovation and optimization program, we are not reporting like-for-like metrics. However, productivity was down 6%, while retail space increased low single digit year over year.

As regarding outlook, we will provide the 2025 outlook in our next session in March.