Second Quarter 2024 Results

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Christian Stöhr (SVP Investor Relations): Good morning, ladies and gentlemen. Welcome to our second quarter 2024 financial results presentation. Hosting our conference call today is Yves Müller, CFO and COO of HUGO BOSS. Before I hand over to Yves, allow me to remind you that all revenue-related growth rates will be discussed on a currency-adjusted basis, unless otherwise specified. Also – and just like in the past – I would like to ask you to limit your questions during the Q&A session to a maximum of two. And with that, let's get started and over to you, Yves.

Yves Müller (CFO/COO): Thank you Christian, and a warm welcome from Metzingen, ladies and gentlemen. We are delighted that you are taking part in our conference call today. Over the next 30 minutes, I will present a detailed overview of our second-quarter and half-year performance, focusing on the most recent operational and financial developments. Just as importantly, I will also walk you through our updated top- and bottom-line expectations for fiscal year 2024.

As you are all aware of, and as the current reporting season has demonstrated, our industry is navigating through a period of persistent macroeconomic and geopolitical uncertainties. A period during which spending on luxury and premium apparel has been impacted by subdued consumer demand. And while this has resulted in a normalization of industry growth for several quarters in a row, the slowdown was particularly evident in the second quarter, as the global retail environment has seen a further pullback in many key markets around the globe. As a company with almost two third direct-to-consumer business, we were ultimately not able to completely escape these industry developments.

Following an overall solid start to the year, with sales up 6% in the first quarter, our top-line momentum has therefore decelerated somewhat. However, with a sales decline of 1% in the second quarter, we were able to limit the external impact on our business to quite some extent, thus continuing our relative outperformance of the market. This is testament to the continued brand momentum of BOSS and HUGO, which I will come to in a moment.

The weak consumer backdrop inevitably also impacted our bottom-line performance, with EBIT down 42% to 70 million euros in the three-month-period. This development also reflects higher operating expenses, which more than offset an otherwise robust gross margin expansion in the second quarter.

Now, before diving into the details of our top- and bottom-line performance and our future approach to navigate the current market uncertainty, allow me to clarify a few things first:

despite the current macro context, we are witnessing no signs of a structural slowdown in brand momentum. Quite the contrary: following a period of successful and relentless strategy execution, we remain absolutely convinced of the strength of our two brands BOSS and HUGO.

Three years ago, in August 2021, we presented "CLAIM 5" for the very first time to all of you. A strategy that has always been geared towards putting our two iconic brands back into the spotlight, revitalizing BOSS and HUGO, and winning over a new, younger, and more diverse audience.

By investing in our brands and products, digital capabilities, global touchpoints, and our operational and organizational backbone, we have successfully boosted brand relevance and accelerated top-line growth. In doing so, "CLAIM 5" enabled us to deliver a true kick-start and a strong comeback after the pandemic, driving above-trend and high-quality top-line growth for now twelve consecutive quarters.

This also holds true for the second quarter. Despite the aforementioned 1% sales decline, our top-line once more outperformed the broader industry development. This is proof positive that "CLAIM 5" is and remains the right strategy for our Company, even in times when the overall market conditions are deteriorating. By sticking to our game plan and consistently executing our strategic priorities, we are confident we can and will unleash the full potential of our brands.

Over the past three years, "CLAIM 5" has fueled significant growth for our Company. Having achieved our initial sales target of 4 billion euros already last year and continuing to strongly exceed 2019 revenue levels by more than 50% are clear testaments to the power of "CLAIM 5" and our successful strategy execution. It is precisely for this reason, why we will stick to our strategic actions, leveraging our numerous growth opportunities in the quarters to come.

You may be wondering what this means for future investments: let me therefore be clear that we remain committed to investing in strategically relevant areas of our business. This first and foremost includes our brands and products, as we will never compromise on brand relevance and price-value proposition. At the same time, we will remove any spending in non-strategic areas of our business for the time being, to cope for the more challenging market environment – something I will talk about in more detail in just a few minutes.

The increased relevance and improved visibility of our two brands is nowhere more evident than on social media. Our comprehensive investments into star-studded brand campaigns, fashion events, and high-profile collaborations led to BOSS and HUGO dominating key platforms such as Instagram and TikTok. Since introducing "CLAIM 5," we have added more than 10 million new followers on social, while recording an impressive 120 billion impressions

and around 3 billion engagements. This demonstrates our ability in successfully turning Millennials and the Gen Z into true fans of BOSS and HUGO.

Converting our growing fan base into loyal customers is as least as important. Year over year, we managed to grow our global member base by around 30% to almost 10 million registered customers. Retaining their loyalty to our brands in the long term is of particular importance, which is why we are taking customer engagement to the next level.

In this context, in Q2, we have successfully launched HUGO BOSS XP, our new membership program, centered around our well-established HUGO BOSS app. Over the coming quarters, we will roll out this program worldwide, as we are committed to further expanding our member base and binding even more customers to our brands and products.

Thanks to the relentless execution of our strategic actions, today we are operating out of a position of strength: our brands are significantly more desirable, our product offering reflects our 24/7 lifestyle image, our touchpoints are more appealing, and our customer base is bigger and more loyal than ever before.

And while all of this may not free us from today's macroeconomic challenges, it makes our business model more resilient. As a result, we were able to increase our sales by 3% in the first half of the year, despite the overall external framework.

Growth continued to be broad-based, with both our brands, as well as most regions and most channels contributing: this includes sales for BOSS Menswear being up 2%, while BOSS Womenswear improved 4%. HUGO even grew 6% in the first half of 2024, supported by the successful launch of HUGO BLUE.

Looking at the second quarter in more detail, the overall sector slowdown weighed in particular on sentiment in some of our key retail markets. In EMEA, sales decreased 2% in Q2. While retail traffic in the UK remained weak, with no improvement as compared to the first quarter, sales in continental Europe experienced a slowdown during the three-month period. This affected our performance in key markets such as Germany and France. At the same time, we were able to maintain our double-digit growth trajectory in the emerging markets.

Also in the Americas, we continued our growth journey in the second quarter, with sales up 5%. This primarily reflects further sales improvements in the important U.S. market, driven by our brands' successful 24/7 lifestyle positioning, which drove momentum in the department store business. In Latin America, momentum remained equally resilient, with sales continuing their double-digit growth in the second quarter, while Canada remained on the prior-year level.

To conclude on the regions, sales in Asia/Pacific decreased 4% in the second quarter, reflecting sales declines in China, as muted consumer confidence weighed on domestic retail consumption. At the same time, Southeast Asia & Pacific recorded another robust performance in the second quarter, with revenues up high-single digit, supported by a particularly strong performance in Japan.

To finish off on our Q2 top-line performance, let's take a quick look at our distribution channels. With sales up 5%, I am pleased to report that our momentum in brick-and-mortar wholesale continued. This is even more remarkable considering the current market conditions, demonstrating that we keep gaining market shares also in this channel, as we continue to be a brand of choice for our global partners.

In brick-and-mortar retail, however, sales remained 2% below the prior-year level, with traffic declines partly compensated by higher conversion rates. As already mentioned, this mainly reflects the challenging retail environment in the UK and China. When excluding these two markets, brick-and-mortar retail sales were up 1% in the second quarter.

Last but not least, our digital business was down 4% in Q2. Importantly, our digital flagship hugoboss.com continued its growth trajectory also in the second quarter, up 3% versus the prior year. This is proof positive that our many initiatives to accelerate the omnichannel experience are paying off.

With the performance in the second quarter and first half year in mind, let's now take a look at how we will take things from here on. And let me start by saying that we anticipate the global macro headwinds to remain present for the time being and uncertainties regarding consumer sentiment to remain elevated.

And while we remain steadfast in our commitment to continue driving above-trend growth in the future, we are taking a rather conservative view on the consumer for the remainder of the year, irrespective of our long-term growth potential.

Consequently, we now expect Group sales in 2024 to increase by 1% to 4% in Group currency, with a slightly negative currency impact. This in turn means that we do not necessarily factor in an improvement in top-line growth in the second half of 2024, although – objectively speaking – Group revenues and our brick-and-mortar retail business in particular should be benefitting from a more favorable comparison base in H2. Likewise, we should not ignore that our order intake for Winter 2024 and Spring 2025 looks encouraging, as do many of our upcoming brand and product initiatives we have in the pipeline for H2.

The signing of our long-standing strategic partnership with David Beckham is one of these strategic investments that will further boost our BOSS Menswear business. Alongside recurring ambassadors Naomi Campbell and Gisele Bündchen, David will also star in our upcoming global 360-degree BOSS brand campaign, launching in just a few weeks from now.

On top of that, BOSS will return to the stages of Milan Fashion Week in September, while we will also continue creating a buzz with high-profile collaborations – including those with the NFL for BOSS, and Red Bull for HUGO. Last but not least, with "THE CHANGE" we have launched a new sneaker icon for BOSS only a few days ago, taking another stride forward in our footwear range. It is crafted with HeiQ AeoniQ, enabling us to gradually increase the share of this cellulosic filament yarn in our overall product range. This, ladies and gentlemen, concludes my remarks on our top-line performance and expectations for the second half year. Let's now move over to our bottom-line development.

For several years, as part of "CLAIM 5," we have been strengthening our operational and organizational platform. And you may remember that, already in March, we told you that we would begin leveraging this platform, focusing on driving effectiveness and efficiency across our organization. Going forward, this approach is meant to support our future gross margin development, while also improving the overall productivity within our cost base.

By looking at our gross margin development, there is clear evidence that these measures have already started taking effect. We are successfully leveraging our operations platform to enhance the productivity of our global sourcing activities. This includes achieving greater economies of scale, optimizing vendor allocation and freight modes, and reducing the reliance on airfreight. Coupled with more favorable product costs, these efforts translated into robust gross margin improvements, up 50 basis points in the second quarter and up 30 basis points in the first half to a level of 62.1%.

And let me be very explicit in saying that we anticipate our strong focus on leveraging sourcing efficiencies to provide even greater support for gross margins in the second half of the year. We therefore expect our gross margin development to accelerate further, forecasting a gross margin above 62% for the full year 2024, thus aligning with our mid-term target range of 62 to 64%. This also reflects our confidence that we will be able to continue compensating for adverse channel-mix and currency effects, higher freight rates, as well as ongoing uncertainty related to the promotional environment.

Moving over to operating expenses, which grew 7% in the first half of the year, and 9% in the second quarter, respectively. This development primarily reflects higher brick-and-mortar retail expenses, up 12% both in the second quarter and in the first half, driven by inflation- and expansion-related cost increases. Marketing investments, on the other hand, grew only 1% in the first half year, including a timing shift from the first into the second quarter in light of major brand events. Importantly, at 7.8% of Group sales, marketing investments in H1 remained within our target range of 7 to 8% as outlined in "CLAIM 5."

And while administration expenses were up 8% in Q2, they only increased 3% in the first six months, as first benefits from improving organizational efficiency partly compensated for digital investments and overall cost inflation.

Now, taking into account that the macro environment is likely to remain challenging for the time being, we are accelerating our cost discipline from here on. In doing so, we will protect our bottom-line development in 2024 and beyond. In particular, by removing spending in non-strategic areas of our business, and further simplifying our organizational structure, we are committed to noticeably mitigate the cost increase going forward.

The majority of our cost saving initiatives will focus on sales, marketing, and administration:

- In sales and distribution, we are optimizing staffing in our own stores and shops based on current traffic trends. At the same time, we are reducing all non-business-critical service costs, while also driving CapEx efficiency by optimizing investment per square meter. This in turn means that, when it comes to store renovations, we are now clearly prioritizing our best and Halo stores, while taking a much more conservative approach to renovating locations in Tier-2 cities.

- In marketing, we are enhancing effectiveness, by investing in an even more targeted manner and prioritizing brand initiatives with maximum return.

- Finally, in our global admin functions, we have already adopted a much more restrictive hiring approach, in addition to strongly removing spending in areas such as travel, consultancy, and hospitality. On top of this, we are pausing non-business-critical projects for the time being, as we prioritize key strategic gamechangers such as the global rollout of HUGO BOSS XP or our important Digital TWIN initiative.

Overall, we expect these measures to notably mitigate the increase in our fixed cost base already in the second half of the year, with operating expenses anticipated to increase between 1 and 3% in H2. Our measures will therefore provide a considerable tailwind to our bottom-line development in 2024 and beyond.

Given our confidence to further improve gross margins, and our determination in implementing measures to swiftly improve operational and organizational efficiencies, our bottom-line performance is expected to accelerate in the second half of this year. Consequently, we are now targeting a full-year EBIT of between 350 and 430 million euros, taking into account the overall market uncertainty.

Before opening the floor to your questions, let's also review our most important balance sheet items, starting with inventories. Tight inventory management is and remains a key priority within "CLAIM 5," as we remain committed to further optimizing inventory levels. On that, I am pleased to report that in the second quarter, we were able to bring down inventories by 7% currency-adjusted versus the prior-year period, highlighting that inventory management is well under control. Consequently, as a percentage of Group sales, inventories came in at 24.9% and thus below the prior-year level, while also improving compared to the end of fiscal year 2023.

Moving over to trade net working capital, for which we continue to expect the moving average of the last four quarters approaching 20% of Group sales by year-end, down from 21.2% at the end of June. This projection reflects in particular our ongoing progress in optimizing our inventory position.

On capital expenditure, we now anticipate investments to come in at around 300 million euros and thus at the lower end of our initial guidance range, reflecting our increased focus on CapEx efficiency to support profitability in 2024 and beyond.

Finally, we continue to expect free cash flow to accelerate strongly in 2024, having recorded meaningful progress in the first six months already. Supported by our initiatives to further optimize inventories and drive CapEx efficiency, this should enable us to generate a free cash flow of around 500 million euros in this fiscal year.

Ladies and gentlemen, let me conclude with some final remarks:

- There is no doubt that with "CLAIM 5," we implemented the right strategy at the right time. Over the past three years, and amidst an increasingly challenging market environment, HUGO BOSS has consistently invested in high-return, value-creating opportunities across its brands, products, and consumer touchpoints. Our strategic capital allocation, prioritizing long-term growth over short-term margin gains, underscores our unwavering commitment to maximizing shareholder value in the long run.

- Our investments have enabled us reinforcing brand strength and achieving above-trend top-line growth. During a period marked by a significant slowdown in industry growth, both BOSS and HUGO have expanded market shares, showcasing the resilience and appeal of our revitalized brands.

- While remaining vigilant in the current context, we approach the second half of the year with confidence and determination. Our updated full-year guidance reflects our strong belief in our strategic direction and key initiatives, including our accelerated approach to enhancing efficiencies and safeguarding profitability. These measures, coupled with our ongoing strategic investments, position HUGO BOSS to emerge even stronger once market conditions normalize.

And with this, we are now very happy to take your questions.