SMCP

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SMCP Half-Year 2018 Results

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Welcome and Disclaimer

Célia d'Everlange

Head of Investor Relations, SMCP

Opening remarks

Good morning, everyone. This is Célia d'Everlange, Head of Investor Relations speaking. Thank you for being with us this morning for the SMCP half-year results. I am here with Philippe Gautier, CFO of the company. As usual we will go through the presentation and then we will have the Q&A session. Before I hand it over to Philippe, I invite you to go through our usual disclaimer on page two, that you start to know. I think now we can start. I hand over to Philippe.

Half-Year 2018 Results

Philippe Gautier

CFO, SMCP

Preamble

Thank you, Célia, good morning everyone. Thank you all for joining. I am very happy to present to you another semester of very strong results for H1 2018, in line with our expectations. This is a semester which shows the robustness of our business model and our capacity to generate long-term profitable growth.

Very strong H1 2018 results

If we start with our key performance indicators on page three. Back in July you saw our sales numbers. As a reminder, we talked about +12.4% of reported growth, +15.5% at constant currency and +5.8% of like-for-like sales growth. In terms of profitability, the adjusted EBITDA is up +14.8%, with a margin reaching 17%. This is above our expectations thanks to both ecommerce and the APAC regions performing very well, and even a bit better than our internal forecast. Just for you to note, this is called adjusted EBITDA because this is the EBITDA before the management LTIP; that is the only difference.

Regarding free cash flow, we generated €28.6 million; this is before €13.6 million of IPO-related cash-outs, which were booked last year and paid this year.

Finally, the net income, which has seen a huge increase. We reached €27.4 million in H1 2018 versus €1.1 million in H1 2017, which you know, was impacted by IPO-related one-offs. This is also because we now start to see, as expected, the strong benefits of our recent IPO in terms of reduction of our interest costs.

Very strong sales driven by outstanding international growth

Moving on to slide four, I just want to quickly remind you of our sales numbers. Growth has been very strong and more importantly, very balanced throughout the brands, with all them growing by double digits. If we talk about region, there has been a broad growth, well balanced, among Greater China, the Americas and Europe. France has been resilient, despite a continually tough market. It was –2.4% in France according to IFM; that means that we saw further market share gains in France.

International sales have been one of the biggest engines of growth this semester, being at +27.2% at constant currency, with high-double-digit growth in all regions.

In a little more detail, EMEA has shown a very robust performance, at +14.2%, constant currency, while the Americas and APAC continued to generate outstanding growth levels of +28.3% and +50.9%, at constant currency, respectively. Furthermore, the sales dynamic has been pretty even between Q1 and Q2.

Another semester of strong profitable growth

I will now talk about our adjusted EBITDA, which is on slide five. We have a strong growth of adjusted EBITDA, up +14.8%. This means reaching a margin of 17%. As you see on the left side, the growth comes mainly from sales momentum; this is the largest driver, which is consistent with our growth profile. However, we also have some gains coming from the incremental EBITDA margin.

Looking a bit more in detail at our margin structure, the gain in our margin is largely driven by two main factors. The first one is retail margin, up +0.2 points to 36.6%, with ecommerce and APAC exceeding our expectations in H1 2018. The company has grown the most in these two areas and as you will recall, they are the most profitable in terms of return margin.

All in all, we have managed to totally absorb the very slight reduction in gross margin that we saw in Q1, which was related to the mix between winter sales and summer sales. We sold more discounted items from winter collections than usual due to the very unfavourable climate that we had in Q1.

The second factor is our strict control of our SG&A. We have SG&A which are around 19.6% of sales in H1 2018, down -0.2 points versus last year. This again reflects a strict control of our cost bases, whilst we are maintaining, at the same time, the pace of investment to prepare for future growth, being very careful to choose the right investments, for example, in terms of infrastructure and talents. It is important to know that we have the capacity to be reactive in our cost management. We can tighten the belt in case of slow-down, while we can accelerate slightly our investments whenever we see business upstart.

Strong net income driven by our profitable growth profile and significant deleveraging

If I move to the net income on slide six, we can see a very strong net income at €27.4 million compared to €1.1 million last year. There were €19.1 million of one-offs related to the IPO in H1 2017. To have a point of reference we have calculated the net income excluding one-offs. On a comparable basis, we have come from €20.2 million in H1 2017 to €27.4 million in H1 2018. Again, therefore, a very significant progression by almost 36% versus last year.

To give a bit of detail around the one-offs that I am talking about, a net amount of €19.1 million is coming from, first, other income and expenses, up to €9.8 million. This includes costs related to free preferred shares, €7.2 million; you then have IPO fees, mostly, for €2.6 million. Second, €14.5 million is due to financial charges. We had costs related to the early redemption of the bond, at €2.7 million, and €11.8 million of charges related to the shareholder loan, which no longer exists post-IPO. You then also had a related tax impact.

Let us come back to the structure of the P&L and the main drivers of the net income increase. As you can see on the right part of the chart, the strong net income comes from, one, the profitable growth profile of the growth. We have €11 million of EBIT gains before LPIT, which includes the positive impact of the adjusted EBITDA accretion and decrease of D&A as a percentage of sales from 4% to 3.6%. Development is in line with the group's controlled investment strategy. Secondly, you have the evolution of non-recurring charges and LTIP. Lastly and most importantly, we have the significant deleveraging of the group compared to last year thanks to free cash flow generation, as well as the IPO.

The financial results are reduced by €19.8 million, down from 6.9% of sales in H1 2017 to 2.2% in H1 2018.

Solid H1 2018 free cash flow generation

What about cash? This is on page seven. We have a solid free cash flow generation. It starts, obviously, with the adjusted EBITDA of €83.9 million. Then we had a change in working capital of €32 million. This is still a little bit inflated due to, one, higher purchases to respond to the strong international demand, and then some timing effects. These effects are the result of, one, you have very quick international expansion, particularly APAC and the Americas, which required us to ship more products earlier to absorb slightly higher lead time. We also had a low base of comparison last year, especially on Maje. We had earlier delivery of orders for the new collection this year compared to last year, which took place a little bit later in the season. Overall, our inventories continue to be very sound. The old collections, i.e., seasons two years old or more, continue to be a very small part, less than 10%; this is a very good metric.

The impact of higher working capital will gradually fade away as the basis of comparison starts to normalise, while also implementing an enhanced process to managers internationally. Looking at the third item, we have CAPEX at €22.1 million, representing a very balanced split between store expansions, around 50%, as well as renovation and infrastructure investment. The CAPEX represents 4.5% of sales, which is in line with our commitment and corresponds to what we need to fuel our expansion.

All that results in a free cash flow of €28.6 million. This is before the €13.6 million of IPO-related costs, which are cash-out of €2.3 million linked to the IPO, and cash-out of €11.2 million linked to the free preferred shares allocations.

Continued deleveraging over the semester

What is the result of all that in terms of deleveraging? Let us look at page eight. We have posted a continued deleveraging over the semester from 1.9 times to 1.7 times adjusted EBITDA. This was driven mostly by operations, with €28.6 million of free cash flow generation. This is before the impact of IPO-related cash-out and financial charges. As you know, we have gone through a gradual refinancing of our debt at the IPO. We had €471 million of high-yield bonds at a cost slightly below 6%. We reimbursed €271 million last year. Now, with €20 million of additional reimbursements this year our high-yield bonds still stand at €180 million. Consequently, financial charges have been significantly reduced compared to H1 2017, talking about P&L effects, so we have a cost of net debt down from 5.9% in H1 2017 to 4.8% in H1 2018.

The next step now will be the refinancing of the remaining high-yield bonds, with a non-call period ending in May 2019. We will look at several cheaper options for refinancing. In this case we will see continuous reductions in our cost of debt towards 2%, which is the cost of our RCF.

Outlook

To wrap up, before I pass the floor to Q&As, I will make a few concluding remarks concerning the outlook for the future.

Moving to page ten, I will be very brief as changes in guidance already occurred at the end of July. As you remember, in light of our H1 sales and 2018 sales, that exceeded our expectations, we upgraded our sales growth guidance for 2018 from a range of +11–13% at constant currency to above +13% at constant currency. At the same time, we confirmed the adjusted EBITDA margin guidance at around 17% for the year. Therefore, I am reconfirming our guidance today.

Thank you all for your attention. I am now happy to take your questions.

Q&A

Mariana Horn (Berenberg): I have two questions, please. The first one is on your levels of D&A, which, as you mentioned, in H1 are a bit lower than what was anticipated for the full year. Can you confirm what your expectations are for the full year 2018 and also the mid-term, if it is still around 4% as a percentage of sales? Could you also confirm what your expectations are for the LTIP charge for the full year because it appears that, also, in H1 it was a bit lower? I just wanted to understand if this was more to do just with the timing of it, of how you report it, or whether we could expect lower levels for both of these items over the full year too?

My second question is on the trends that you had in recent months. Could you give us maybe some qualitative comments on the trends that you have with those maybe in the month of July and August, and maybe if you could contrast that between Asia and Europe, and especially in Asia, China.

Lastly, the question that you always get: could you comment on the level of promotional activity that you have been seeing in the environment, and maybe not so much at the group level, but have you seen any changes by region? I am referring more to Europe and specifically also in France. Thank you.

Philippe Gautier: I will transfer through your various questions. On D&A we are not changing our outlook, so around 4%. As you remember, D&A are relatively contained. This is due to our level of CAPEX, which is currently a rate of 4.5%. You can expect D&A to be slightly below that, so around 4%.

If we talk about the LTIP charge, there was not too much of a change, actually. We would expect to be between €15–20 million. If you recall, this is mostly an IFRS non-cash charge. You then have a little bit of social charges in there.

If I talk about the trend in July, I would say it was mostly not really different from what we saw before. In general we are satisfied with the developments in July and August, as a matter of case. You have similar trends in the sense that you will not be surprised Asia continues to be very strong, North America as well. Obviously, the French market continues to be tough, so that is not very surprising.

Moving to your last point on promotional activity, I would say, in general and maybe I am talking particularly about France, on the market you can expect promotional activity to be quite heavy because the start of the season was pretty weak, with all the climatic effects you had. Now we are always better than the market and we tend to be more conservative in terms of promotional activities. That is where we do not change our policy on that. We talked about an average discount rate of about 28%; this is not really changing for us.

Mariana Horn: Okay, thank you very much.

Chiara Battistini (JP Morgan): My first question would be on whether you have any update on the appointments for the next CEO of Sandro, please?

My second question is on your pricing policy going into the autumn/winter collections. Could you comment if there was any change on your pricing policy for that? Could you perhaps give some colour on the initial reactions to the autumn/winter collections that I think have started to hit the stores in the last few weeks?

Finally: one quick question your tax rate. That was quite high in H1, so I was wondering if you could expand on how come the tax rate is so high, around 39%. What should we be expecting for the full year, please? Thank you.

Philippe Gautier: Taking your three questions, first the question of the CEO of Sandro. Today, we have a very happy CEO of Sandro, who is Daniel Lalonde. He has been taking over the job with a lot of enthusiasm as an interim CEO. He is working alongside Evelyne and Ilan, so there is a lot of continuity there. We do not have much more to say right now. We are in the process of the recruitment, so no big update compared to what we said last time. We feel we have a great set up.

In terms of the pricing policy, what I would say is in general not much changed. The only change you could consider relates, actually, to interest, like to our forex rate. As you have seen, you have now the US dollar slightly stronger. If you look at our indexes, there is no change, we are around 150 in China; US slightly higher, we are around 130, we were more around 120, and Hong Kong is a similar level; UK is around 120; as you can see, Europe is 100. It is very stable here; it is just the forex which is changing.

On the tax rate, maybe just to break that out a little bit, what we are reporting is in-the-line income tax. We have also the large tax called CVAE in France. That means that, excluding that, we would be closer to 34%. We use the French tax rate as a guide for our overall. What we expect for the full year, so with CVAE, we expect around 39%. We do not expect too much change here. We had a slight timing effect in H1 due to some US deferred tax elements, but that is quite marginal.

Chiara Battistini: Just on the autumn/winter collections, is there any colour you can share on the initial reactions in the last few weeks?

Philippe Gautier: Yes, sure. In general I would say it is still a little bit early to comment. As I mentioned, our market is always promotional, so you had still the impact of the sales period. It is still a bit early to comment, I would say.

Chiara Battistini: Understood.

Philippe Gautier: However, in general, as I mentioned, we are satisfied with the overall current trading. That is satisfactory, in line with our current expectations.

Chiara Battistini: That is great. Thank you very much.

Philippe Gautier: You are welcome.

Marie-Line Fort (Societe Generale): Could you explain to us the decrease in Sandro's EBITDA margin for the first half and also the increase for Maje? We suspect that organic growth has been better for Maje than for Sandro. However, can you share with us some colour for that point? Could you also come back on your expectation about the currency impact for the full year on your turnover? I just remember that you should expect 300 basis points; is it still the same for the full year? Thank you.

Philippe Gautier: A couple of things: if you look at Sandro, we have an EBITDA margin of 16.5% versus 17.6% last year. I would say primarily we have a very high basis of comps last year with Sandro, so last year the EBITDA rate was up 1.5 points. If you remember, we had the fastest digital growth of the group, which is improving the EBITDA rate and very strong success in general on the collection.

I would say the major thing is that we have opened more stores in Europe for Sandro in 2017 already, which has a full year impact on 2018. It is likely that you will have a little bit more of that on Sandro than on Maje. Then, the pre-collection was a bit more summery for Sandro, so you had a little bit more impact of the unfavourable climate in Q1 compared to Maje.

Marie-Line Fort: Okay.

Philippe Gautier: However, if you look at that, I would say it is primarily the comp basis from last year.

If I talk about Maje, last year was a little bit lower and we had some higher rents from new locations, for example Champs Élysées, and this has now rendered. The other factor for Maje is you have very strong growth of Maje in APAC; this is helping. Sandro is also growing in APAC but Maje a little bit more. I would say those are the main aspects.

Now moving to forex, we expect a little bit less in terms of forex impact, so we would say around 1.5 points in H2. That is a total of around 2% for the full year in terms of negative forex; that is on the top line. As you know, there is no material impact on our EBITDA rate coming from forex, because we have some natural hedge.

Marie-Line Fort: Thank you very much.

Philippe Gautier: You are welcome.

Marion Boucheron (Raymond James): Just two questions for me, please. One, could you please update us on stores opening, those openings you planned throughout the year? You were at 38 in H1, so what are you expecting in H2? I was also wondering if you could give us more granularity on where the brands stand, the differences between the ecommerce sales of each brand you were just mentioning, if there is a driver of central margins. Could you provide us more differential between the brands?

Philippe Gautier: A couple of things: in terms of store openings, in the metrics we are looking at, we are mostly looking DOS, directly operated stores, rather than the total with partners. This is because we feel DOS is the most meaningful and the biggest part of our business by far.

There is not much change here; we are still talking about 80–90 openings for the year. If you remember the key things are we would have about 40% of them in Europe, about 40% of them in Greater China and then 20% for the balance of the world. We had some openings in France. However, this is more like a timing effect of stores that were closed before we relocated and opened this year. In general, in France, we would rather expect to be quite stable. That is in terms of the store openings.

If I look at the digital share for each of the brands, in general, if you look at H1, we have reached 14.3% of digital penetration. We usually have a big step up in H1, and usually what you have in H1 is more similar to what you have in the full year. This is compared to about 12% last year. Right now, the brand where you have the highest penetration is Claudie Pierlot, Maje is around the average and Sandro is slightly lower. That is the idea.

Murielle André-Pinard (HSBC): I have one follow-up question regarding CAPEX. Could you just tell us what kind of infrastructure CAPEX you did in H1 and what level of CAPEX we can expect for the full year?

Philippe Gautier: We are not really changing our guidance for the full year in terms of CAPEX. If you look at the big things, infrastructure CAPEX, here we talk about mostly it could be either logistics, ecommerce, IT systems. In terms of infrastructure, this year we have spent about €7 million versus €5 million last year. I would say it is not very different from usual. We have some IT investment and we have a lot of IT projects going on. We have started roll-out of Oracle, for example; that is an important one. I would then mention what is slightly higher than usual is we had some investment on a new headquarters, which is in Paris, for the brands Maje and Claudie Pierlot. They have just moved a couple of days ago to a different place, which is Rue Marengo, it is very near the Louvre. That is the type of investment that we do and they are good to go for several years. They now have great working conditions to accommodate the new people that we have ,and we will recruit in these two brands. This is one example.

Murielle André-Pinard: Okay, and for the full year, for infrastructure?

Philippe Gautier: For the full year, in general, we expect around 5% CAPEX and for the split, over the year, let us say about half is expansion and about half would be infrastructure or refurbishment. You remember we are also very careful to refurb our stores, particularly in France. We have been working on stepping up the look and feel of our stores in France and being sure that they are always in perfect condition.

Murielle André-Pinard: Okay, thank you.

Philippe Gautier: You are welcome.

Marion Boucheron: Thanks for the follow-up. How would you explain why Maje was more successful in Asia-Pacific in the past half year?

Philippe Gautier: That is a great question. I think, maybe, to qualify a little bit my statements, I told you, in general, you have seen that, for the group, you have growth in

China, currency constant which is at a level of around +50%. If you look, Maje is a bit higher than +50%. We are between +50–60%, then Sandro is in the mid-40s. In reality, we have fantastic growth of our two brands, mostly Maje and Sandro in China; they are really extremely desirable. I would say one thing particular to Maje is that you have the 20th anniversary of Maje, and we had great activation this year, globally but particularly in China. We had big events in Beijing with some celebrities, etc. You had also brand day activation: we were selected for the Tmall brand day for Maje. So we have a couple of items like this which are a little bit exceptional. In reality both of our brands are extremely successful and desirable in China.

I would say one of our focuses is to develop more Claudie Pierlot. Claudie Pierlot is still a bit more at the early stage in China. There is a huge potential to grow the brand in China for Claudie Pierlot, and this is a big initiative for 2018. Both brands really very, very desirable in China.

Marion Boucheron: Okay, thank you.

Murielle André-Pinard: I just have a question on the EBITDA guidance. In fact, you maintained it around 17%. However, if we consider the performance in H1 and if we consider generally H2 is more profitable, can we say that the 17% is a kind of floor for the full year?

Philippe Gautier: Yes, that is a great question. What I would say is, if you look at the H1 performance, maybe to judge a little bit the performance, as you have seen we had a little bit of very slight margin pressure, as I mentioned. However, in reality, we were able to more than offset that. That is where you see that the retail margin is up significantly. That is driven by APAC, very, very strong, and digital. Digital was also, in China, very strong. We saw over +50% growth, currency constant, in APAC in the quarter. We do not expect necessarily to do +50% every single quarter, even if we are very bullish about China. You have also an impact with slightly higher partner sales. They had a higher retail margin than the rest. This is the impact of timing. I would say this was a rather good performance in H1.

For the full year, I am not changing the guidance: around 17%. I talked about the positive; if you look, it is slightly negative. As you know, we continue to expand in Europe and this is slightly dilutive on the margin. That continues to be a big focus, so this will have an impact on H2. Then, we continue to invest in SG&A. We invest in IT, we invest in monitoring, we invest in our Asian platform. Then, for example, I talked about the HQ for Maje and CP, so we have slightly higher rents. That is the balance, and that is where we expect to be still, around 17%.

Murielle André-Pinard: Okay, thank you.

Philippe Gautier: Thank you very much, everyone. Thanks for all your questions and have a great day.

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