Transcript

N Brown Group Q3 Trading Update

19th January 2017

Presentation

Operator

Hello and welcome to today's N Brown Q3 Trading Statement Call. Throughout the call all participants will be in a listen-only mode, and afterwards there'll be a question and answer session. Just to remind you, the conference call is being recorded. Today I'm pleased to present Angela Spindler. Please begin your meeting.

Angela Spindler

Good morning everyone, and thank you for joining us today. I'm here with Craig and Bethany. I know that you've got a few retailers reporting today, so we're committed to finishing promptly at 09.00. But just before we open up for questions, I'm just going to very briefly share my perspective on the period with you.

So, I'm really pleased with the performance we're reporting. It's also worth noting that it's against a good Christmas last year, so the comp was pretty tough. I think the biggest takeaway for me is the benefits that our improved trading agility has given us. And this was evidenced by our performance particularly in Cyber Fortnight, which was a record two weeks for the business in sales and profits.

So, what do I mean by trading agility? So, I'm referring to data-driven decision making executed in real time around how we deliver value to customers in a really targeted way. We can do this now because of the changes we've made to our processes and our capabilities, and because our business is now of course largely online.

So, moving to performance in a bit more detail. Hopefully you've all had a chance to read the statement, but to briefly recap the headlines: Product revenue up 5.9%, Financial Services down 0.5% and the Group therefore overall up 4.1%.

I am most pleased with our ladieswear performance, which was up double-digits. And this was the first time this key category has recorded double-digit growth since 2008, so a real achievement. Ladieswear volumes were up 23%. Traditional, having been down 4% in H1, was up low single digit in the period, so the actions we took to improve performance here are working well. Fifty Plus, which as you know we are in the process of migrating into JD Williams, was also significantly better this period, so sales were flat, which is a marked turnaround from minus 18% reported in H1. All three Power Brands again recorded good growth for the period. The three in total were up 10%. And just for your reference, if we do include Fifty Plus within the Power Brands revenue, it's still up high single digit.

So, turning to Financial Services: the quality of the debt book is significantly improved, so interest received was up. Non-interest items such as admin charges were down, and therefore the overall profitability of the book is strong, which is reflected in our improved gross margin guidance. So, a good result.

We've also made a few other small guidance changes which are detailed in the statement. Overall, we are comfortable with market expectations. We aren't expecting consensus to change today.

We are, as you know, still in transformation, with our systems project, Fit for the Future, a key element of this. It remains on track. The USA site launched in September and is doing well. The next milestone is the High and Mighty site in Q1. This will also include the launch of our new Financial Services system on that brand, and then we move on to Fashion World in Q3.

So, all in all we're pleased to report a good performance over the period. Effective and efficient promotions supported by data analytics, and keen prices funded by sourcing improvements, are working well with customers.

And just briefly from a macro perspective, there are some well-documented industry headwinds such as FX, national living wage, cost inflation and, although our lack of a large store estate does partly insulate us from some of these, we're of course not immune from them. However, against the continued challenging backdrop I am confident in our trading prospects going forward.

So, I have, as I said at the beginning, I have Craig here with me, and we are now happy to open it up to your questions.

Q&A

Operator

Thank you. Ladies and gentlemen, if you do wish to ask a question please press 01 on your telephone keypad. If you wish to withdraw that question you may do so by pressing 02 to cancel. There will be a brief pause whilst questions are being registered.

And our first question comes from the line of Kate Calvert from Investec. Please go ahead, your line is now open.

Kate Calvert

Morning, happy New Year to you. Two questions from me. Can you talk about why you've decided to delay Simply Be re-platforming into next year?

And my second question is the drag on Financial Services revenue from the non-interest line: should we expect this to continue into next financial year as well?

Angela Spindler

Okay, morning Kate and happy New Year to you. I think we can still just about say that. So, I'll take the question on the Fit for the Future programme, and then I'll hand to Craig to take the Financial Services one.

On Fit for the Future, there is no technical reason why we've shifted from Simply Be to Fashion World. Fashion World requires all of the functionality technically that Simply Be does, it's an online-dominated brand. The portfolio of products we sell is wide. It includes a large Home & Gift offer which requires direct despatch technology, support and supplier integration. So, all of the technology we require for Simply Be, we also require for Fashion World. It also participates highly in credit, so it's a great test bed for the Financial Services business. It is a big brand, so just to be clear it's bigger than Jacamo. However, in the interests of just de-risking the programme because we can, we've chosen to do it that way round. But there is no difference at all to the timelines of the technology to support Fashion World relative to Simply Be.

Kate Calvert

Okay.

Craig Lovelace

So, Kate on your second question on the Financial Services book: as you'd expect, we're not going to give Financial Services guidance for FY18 today. Consensus notwithstanding does look pretty sensible for Financial Services. Overall, we're heartened by the continued improvement in the quality of the book, and I think realistically the continued quality of that book into next year would realistically mean that those charges would continue to go in the direction that you've seen. Although I think it's really important that the most important revenue line by the vast majority in Financial Services is the interest income line.

Kate Calvert

Okay, thank you.

Operator

Thank you. Our next question comes from the line of Adam Cochrane from UBS. Please go ahead, your line is now open.

Adam Cochrane

Good morning and congratulations on the numbers. A couple of questions please. Firstly, is there any change in the sort of marketing spend as you went through this quarter versus last year? I know that you've been talking about re-profiling marketing spend to different occasions; do you think that had a positive impact?

And then secondly, you've done quite a lot of work on increasing open to buy and flexibility. As the trading patterns happened over the last few months, has that increase in flexibility enabled you to chase more stock or be more flexible? Has that impacted your numbers at all? Thanks.

Angela Spindler

Okay, thanks Adam. First of all, on marketing spend: our ratio in terms of the efficiency of our spend has improved slightly. The shift of our media investment is much more towards digital activity and TV and away from paper. That's a trend that's been underway for the last three years, and we have continued to adjust that mix. So, no new news in that respect, but a continued momentum in the shift of spend away from paper and into other media.

I think the bigger difference in terms of our investment to drive sales in this period is in the efficiency of our promotional spend and our markdown. We have a new merchandising tool which is part of the Fit for the Future transformation programme. We did speak at the interims about that launching early and about that influencing our ability to mark down more efficiently for the sale. It also influenced our performance over Cyber Weekend, so we're really pleased with that and that's something we're going to be able to leverage more going forward. But that's a bigger difference in terms of our investment profile and capabilities than the continued change in shape of the marketing programme.

The second part of your question was about stock flexibility, and again we've talked about this at the interims and its continued progress. Probably the best way to call it out is about our open to buy at the start of the season. So, we're now very much around the sort of 50/50 mark in terms of commitment at the start of the season. So of course, we've just gone through or are just in the process of starting the new season. We are a lot more open and a lot more flexible as we move through spring/summer. And that was the case in autumn/winter, so our ability to repeat contributed to our performance.

The strongest way to articulate the impact is to talk about The Cut. So, The Cut was a marketing campaign on JD Williams where we selected just a collection of 300 lines that were right across the portfolio in terms of their price point. So, it wasn't an opening price point activity, it was about delivering great value on iconic pieces, and we had price benchmarked them so we know they were offering industry-leading value in our sector. Those lines were the ones that we featured in our advertising and that was across multiple media. And they performed really strongly, and we were able to repeat on them. So, there's some flow-through of that into margin rate, but from a cash margin perspective we are really pleased with the performance of that initiative. And again, it speaks to our flexibility. We can repeat now in some instances within seven days, and our capability is moving forward to really trade the business. So, yes, is the short answer to the question.

Adam Cochrane

In terms of The Cut, for example, when you talked about the ladieswear volume being up low-20s and sales being up, I don't know, 11 or whatever the number was, is the difference between those two some of the investments you're making into pricing and things like the performance of The Cut?

Angela Spindler

Yes, some of that is. Some of it is about the promotional activities that we would have done across Cyber Weekend, which would have been a bit broader in their remit. Some of it is about what we did talk about at the interims and was more of a balance sheet improvement action, which is significant clearance. So, that's more of a one-off as we reduce the participation of last and previous stock in our stock file. And that's gone well in the season, but of course as we guided, that has had an impact in margins. So, it's a combination of those three things.

Adam Cochrane

Okay, thank you.

Angela Spindler

Thank you.

Operator

Thank you. Our next question comes from the line of Simon Bowler from Exane. Please go ahead, your line is now open.

Simon Bowler
Hi, two question from myself, if that's okay? First, just a quick follow-up on one of Adam's questions. I think you mentioned your marketing efficiency ratio improved over the period. I'm just wondering if you could kind of shed a little bit of light on how exactly that is calculated and what exactly that is?

And then secondly, I appreciate it's very early days in terms of the trial, but you made the comment about differing interest rates and say the initial view is encouraging. I was just wondering if you could share some light on what you would view to be encouraging from those trials?

Angela Spindler
Yes, marketing efficiency – I mean, obviously, this is a trading statement. We'll talk more about the shape of our investment when we are together in April. But just to reiterate the shape of the business: the ratio of spend for catalogue businesses, marketing to demand, is very different to digital businesses, so there is a benefit to the increasing shift of the business to online. And it gives us the opportunity to explore different media and really drive the top line harder. But there's nothing new in that. That's a dynamic that we've talked about previously, and that continues to play its part in our growth and in the way we manage our marketing budget. And I'll just hand to Craig to talk about your second question.

Craig Lovelace
Simon, as you called out, it is early days. We went live, these were variable rate trials for new customers on discrete brands, and that went live just before peak so we're not even through two months' trading yet. It is nonetheless an encouraging early start, and we will clearly enunciate further on that in more detail come the prelims. A positive start.

Simon Bowler
Okay, very clear. One more quick question, if that's okay? Just in regards to the operating cost, which looks like it's coming in towards the top end of your guidance: what there has changed versus your expectations? Have you put greater volumes through the business, were you expecting? Which lines have moved versus your expectations when the range was two to four?

Craig Lovelace
It is primarily volume, Simon. So, an 11% increase from a volume perspective this period has factored through. So, as we called out, that is the predominant reason.

Simon Bowler
Very clear, thank you very much.

Operator
Thank you. Our next question comes from the line of John Stevenson from Peel Hunt. Please go ahead, your line is now open.

John Stevenson
Thanks, morning all, happy New Year. A couple of questions from me please. First up, just in terms of the transition in Fifty Plus and also the recovery in the traditional brands; if you could give a little bit more information about how that process is going and sort of what happened over peak, and therefore expectations going forward.

And secondly, just in terms of the overall Fit for the Future campaign; obviously some changes in terms of order of events now. Is there anything which we should expect in terms of the quantum of gross benefits coming through next year?

Angela Spindler
Morning, John. Yes, so I'll speak to the first one. So, traditional titles is a slightly different story to Fifty Plus, so I'll deal with that first. As you know, we have taken some action to improve performance of our traditional titles. Whilst it's not our long-term strategy, it's an important and profitable part of our business and so we've guided to improving it to flat or just positive. So, we're pleased with the performance at low single digits positive in the period. It's driven by, very simply, better product, so an improved range. We cut that back quite dramatically, if you remember, and we went too far for that customer. So, we've improved the product range and we've improved the presentation and made it more relevant for that consumer. So, we were

presenting them, if you remember, with more contemporary visuals connected with that product range, and it just didn't work as well. So, we've reverted in terms of the presentation style and that's resonated. So, that's on traditional. Like I say, it's a declining part of our business but it's great to see it back in growth.

Fifty Plus is reported within JD Williams so we've called it out separately. That was minus 18% in the first-half; it's now flat. We've begun the process of migrating a lot of those customers over to JD Williams, and we can see the evidence of that working. The second phase of that will happen this season. Some of the customers, to be clear, will be migrated over into the traditional part of the business, just because of the way they shop and the items that they buy. So, we're being really quite targeted in the way we handle that file, because it's still an important cohort of customers in terms of scale. But the majority of them are moving onto the JD Williams brand, and again we're seeing a migration online from that portfolio of customers. So, really good progress in the period on both of those customer cohorts, as they were a drag in H1 which we've neutralised in this trading period.

John Stevenson
Do you think that'll flow into spring/summer?

Angela Spindler
Yes.

John Stevenson
In terms of the traditional titles and stabilising the rate of attrition?

Angela Spindler
Yes, we think we can keep that steady now. So, we think we've got to a pretty good place in terms of marketing efficiency and the way in which we're ring-fencing both the budget and the resources. And we think we can just manage that business within that new structure. So, yes, we're pleased with that and we think we've got the right approach in place.

Coming onto Fit for the Future, there is really nothing else to tell you. We are on track. We've launched the USA. We did, as we anticipated, learned a lot from that launch; more around business process than the technology, which has been stable right from the beginning and worked well. So, we're really encouraged by that. So, no, we're on track. We've chosen Fashion World because it uses all the technology, so our full technology suite is landed when we land Fashion World. But we've felt it prudent and sensible to do it in the lowest risk way we could, but still at scale, and that's why we shifted to that brand. No other reason at all.

Craig Lovelace
And John, as you will have seen from the interims, Fashion World has an even higher preponderance of credit usage, so in many respects it tests the credit platform even more readily and earlier.

John Stevenson
Okay, perfect. So, no changes to the timing of gross benefits?

Angela Spindler
No, sorry, I forgot that part of the question. No, we're not changing the flow of benefits or the timing of them.

John Stevenson
Okay, brilliant. Thank you very much.

Angela Spindler
Thanks, John.

Operator
Thank you. Our next question comes from the line of Joe Spooner from Jefferies. Please go ahead, your line is now open.

Joe Spooner
Good morning. Can you just talk a little bit about the improvement in the returns rate that you've noted in the statement? I guess with the strength of womenswear, you might have expected that to move against you a little bit just on mix there.

Angela Spindler
Of course. No, it's a really important part of the P&L, as you'll know, particularly for online retail, so we're really pleased to see continued momentum in the improvement there. And particularly, as you say Joe, with the higher participation of ladieswear one might have expected a slight change in that.

It does really come down to three things: quality and price, so value for money, always correlates with a returns ratio; fit, so we've moved on again in terms of our fit capabilities and we're getting great feedback from customers in terms of fit, particularly on ladieswear but also on menswear where we've made some changes there; and of course, there is a third element working in our favour which is the participation of cash customers, who are typically lower returners, just generically. So, no, that continues to improve.

Joe Spooner
Very clear, thank you.

Angela Spindler
Thanks, Joe.

Operator
Thank you. And as another reminder, if you do wish to ask a question please press 01 on your telephone keypads now. There'll be a further pause whilst questions are being registered.

And we have a question from the line of Matthew McEachran from N+1 Singer. Please go ahead, your line is now open.

Matthew McEachran
Morning guys, a couple of questions from me please. One is a follow-up to Joe's question in relation to the returns rate, but looking a bit more at the wider – what you measure as a customer satisfaction index. I mean, I can see there's some volume of customer complaints on some of the review sites, which isn't surprising given your growth in volume. But I just wondered if you could talk overall about customer satisfaction and accuracy of delivery, and just generally dealing with customer complaints overall, please?

Angela Spindler
We haven't included commentary on that in the statement because we don't typically, but I am happy to report that our customer satisfaction rating for the period year-on-year was up. It is a more challenging period from a customer satisfaction perspective as you pointed out, because you're stress-testing the whole of your supply chain and infrastructure as well as your partners' in terms of home deliveries. But the other piece of news which I'm delighted to share is our service days were a day faster on average year-on-year, which speaks to the benefits starting to come through of our Alliance warehouse building. So, you know we doubled our pick-face capacity, so that has enabled us to deliver better next-day service but also increase our speed of delivery. So, from a service perspective a very strong period for us; again, as I say, leveraging the benefits of our investment which we've talked to before.

Matthew McEachran
Yes, okay, that's great. Thank you for highlighting that. And then the second question just around the mix within your average basket. I mean, you've obviously got still in this period lower average pricing, but you talk about increased number of items in the basket. Have you got to the point where the average basket is back to neutral again, or even possibly into growth? Or is the average basket still down year-on-year?

Angela Spindler

The average basket is just slightly down, Matthew. That's a combination as well of slightly lower Home & Gift participation versus Fashion. And also, obviously things like The Cut price investment and the volume that we've pushed through, and also I mentioned earlier the kind of clearance activity, which will have all played into that average.

Matthew McEachran

Yes.

Angela Spindler

But we're happy with the dynamics there, and we know we've put some pressure on the supply chain through the volumes, and Craig's talked to the Opex impacts of that. But, you know, we shouldn't forget the participation of the clearance activity, which was somewhat a one-off in the period.

Operator

Thank you. Our next question comes from the line of Paul Rossington from HSBC. Please go ahead, your line is now open.

Paul Rossington

Good morning everyone, well done on the update today. Just a quick question more about the outlook. You've mentioned that there are a number of sector headwinds which are going to face this sector this year. I'm just wondering: if there were one or two that you would focus on, what would they be?

And secondly, how do you view the potential outlook for demand for credit, given where you sit today? Thank you.

Angela Spindler

So, thanks for the question, Paul. So, the main headwind that has entertained us, if that's the right word – because a lot of the others, whilst they're there, there's nothing you can do about them and they will be what they will be. And I think the dynamic towards online shopping really offsets a lot of that for us. But the currency headwind is material, and we've talked about that and given some guidance on how that plays into our numbers. I'll perhaps hand over to Craig to give a bit more granularity on that.

Financial Services: typically as interest rates go up, that correlates with a reasonably good performance in Financial Services. However, I think the more important point to make there is as we move through the systems project, our improved flexibility in terms of what we offer to consumers and how we can target our proposition really gives us confidence in the future growth from that part of our business. But, as you know, that's sort of linked to the timetable for Fit for the Future. Albeit we have this workaround in place at the moment on lower interest rates for new customers, which is an interesting trial which will inform how we then use our better technology going forward. So, we're quite excited about our prospects in that sector because of what we're doing, rather than the market itself.

I'll hand over to Craig to perhaps give a little bit more colour on the currency, but that's certainly the main headwind that we've factored in.

Craig Lovelace

Thank you, Angela. Yes, I would fully agree. When we spoke in October, from a hedging perspective we were 50% hedged for FY18 at an average rate of 1.30, and as we sit at the moment we're 73% hedged at an average rate of 1.28. So, slightly more cover than normally one would expect, but actually in a solid position, notwithstanding clearly the volatility remains significant and acute at times depending on the day.

Just on the book, I would echo what Angela's said. I mean, we are clearly alive to interest rate challenges. It's much more – ultimately the book remains affordability-based, and we still believe that the work we've done to continue to improve the quality, the rehabilitation of customers, all speaks to still an ongoing improvement in the quality of the book and the attraction of new customers. So, it is in a decent place from that perspective.

Paul Rossington
Got it. Thank you very much.

Operator
Thank you. And as there appear to be no further questions, I return the conference to you, Angela.

Angela Spindler
Okay. So, very quickly from me, thank you so much for dialling in and thanks for your questions. Goodbye from Craig and I, but just to let you know, Bethany is around all day if you need any further colour to what we've talked about this morning. So, thanks everybody, bye.

Craig Lovelace
Bye-bye.

Operator
Thank you. This now concludes our conference call. Thank you all for attending, you may now disconnect your lines.