

## **N Brown FY21 Full Year Results**

### **Steve Johnson:**

Good morning everybody and welcome to N Brown's full year results for FY21. I am joined by Rachel Izzard our CFO and unfortunately, once again, we're unable to be with you in person – as always, I hope you are all safe and well.

So, turning to the running order this morning: Firstly, I'll give you a brief overview of our progress during the year. I will then hand over to Rachel who will talk you through the Group's financial results. I will then talk a bit more about our strategic progress before turning to the outlook for FY22 and then we'll open up for Q&A.

FY21 was a year of transformation with a significant amount of strategic change in the business. Our revenue has continued to recover from the sharp downturn we saw at the start of the pandemic in March last year. We saw improvements in every quarter, driven by our strategic brands, and we have returned to product revenue growth at the start of this financial year. Within the business we have made significant progress accelerating the strategic transformation of the Group across our brands, product and digital capabilities and I will provide further details on this later in the presentation.

In January we gave guidance on our expected EBITDA performance for the year and I'm pleased to report EBITDA ahead of our guidance. Finally, our successful equity raise, which completed in December last year, leaves us with a deleveraged balance sheet and in a significantly stronger financial position to invest in our strategy.

I'll now hand over to Rachel to talk you through the financial results for the year.

### **Rachel Izzard:**

Thank you, Steve. Let me start with giving you a financial summary of the Group's performance in the year. As we have previously disclosed, from mid-March there was an immediate and severe reduction in customer orders and revenue. This was followed by a steady recovery in every quarter and in our final quarter of the year our strategic brands returned to growth. The net result of the sharp decline and subsequent steady recovery was Group revenue down £108.7 million compared to the prior year.

As part of our strategic changes, we have a more volume variable cost base and in the year we were able to offset more than 80% of the decline in gross margin through maximising efficiencies in the cost base, with the adjusted operating cost to group revenue ratio stepping down a material 7.3ppts in the period. Our ability to flex the levers of margin and operating costs meant that our adjusted EBITDA only declined £20.2 million and the largest driver of this variance was the £15.4 million additional IFRS 9 Covid-19 provision.

As previously guided we have re-assessed the IT intangible assets useful lives in light of the revised strategy enabled by the equity raise, and the pace of change in the tech environment, and have accelerated the non-cash amortisation, hence the adjusted profit before tax variance being higher

than the adjusted EBITDA. As a result of this resilient EBITDA performance, tight management of working capital and non-operational cashflows, and support from all stakeholders including our shareholders, we have eliminated unsecured debt and extended our financing facilities.

We entered the pandemic with the RCF fully drawn at £125m and have finished the year with an undrawn RCF, net cash of £80.8 million and a £196.1 million reduction in adjusted net debt in the year.

Let's look at the revenue performance in more detail. You can see from the chart that product revenue recovered every quarter and this was driven by the performance of our strategic brands, JD Williams, Simply Be, Jacamo, Ambrose Wilson and Home Essentials. Customer return rates as we moved through the initial pandemic period were lower than we initially anticipated before we understood the customer behaviour, so we have also shown the product revenue VLY rephased for returns between Q1 and Q2 of last year, and this smooths the revenue trajectory. Overall, returns were 8.8 percentage points lower in the year. This was equally split between the mix effect of lower returning Home and Gift products as well as an underlying improvement through the pandemic period.

Across the year, our home offer has been key to enabling us to pivot towards the shift in our customers demand to products for the Home and Garden. As a result Home & Gift as a percentage of overall mix moved up from 29pts to 41pts.

Our Financial services revenue was down as expected in light of the smaller debtor book due to lower product sales and solid customer repayments throughout the year. The Group's adjusted gross margin was 44.4%, compared to 52.5% in FY20. Product gross margin declined 7.4ppts to 43.6% primarily as a result of the strategic decision to pivot the customer offer towards Home & Gift to respond to customer demand. Whilst Home & Gift has a lower gross margin it also has a much lower returns rate, and overall has been good for absolute gross margin. Product gross margin also tempered as a consequence of discounting to clear down older stock, a continued highly promotional clothing market, and increased freight rates from the second half of the financial year. The Financial Services gross margin declined 9.6ppts to 45.8% due to the movement in the impairment provision for future expected credit losses. Whilst the underlying arrears rate has improved, in accordance with IFRS9, we need to look ahead and estimate future expected credit losses. The Group increased the impairment provision initially by £17m in H1 as a result of the estimated impact of Covid-19 on future default rates. At the end of FY21 the impact has been reassessed at £15.4m. The overall provision rate has moved from 10.9% in FY'20 to 14.1% in FY'21.

Moving onto our cost base, establishing a stable, efficient and flexible cost base is one of the core enablers of our strategy. We made significant progress in this financial year with our adjusted operating costs to Group revenue ratio improving by 7.3 percentage points to 32.5%.

Let's look at the component parts. Marketing costs were the largest reduction and were down 55.7% in the year to £60.3 million. This was as a result of swift and decisive action at the start of the pandemic to maximise efficiency and preserve liquidity. But we were also gained significant benefit from developing our use of predictive AI to understand Customer Lifetime Value by type of sale enabling us to target digital marketing spend much more efficiently.

Looking at payroll costs, in H1 when the revenue impact was the most severe, under the government CJRS support scheme we furloughed a level of staff across the business and received £3.8m of support. This allowed us to work through the challenges that Covid 19 initially presented for our business and preserve a significant number of jobs for our colleagues. Our Warehouse and Fulfilment costs were down 17.0% to £64.8m. This was faster than the decline in product revenue, which was down 14.4%, helped by lower return rates and enabled by working with suppliers to ensure full volume flexibility. Admin and payroll costs declined 6%. This was driven by an immediate response to Covid-19 with minimal discretionary spend and travel, and continued head office efficiencies across all areas.

The customer loan book has been resilient throughout the year – repayment rates have been consistent or better than the previous year and customer arrears have been lower. Throughout the pandemic and in line with the FCA’s guidance we have offered customers Covid-19 payment deferrals where appropriate, and those customers were charged no interest for the period of their deferral. The amount of balances on a payment deferral peaked at around 3% in May last year and is now comfortably below 1%. Arrears are 1.3 percentage points lower than the prior year and the pie charts show that amount of ‘up to date’ balances have increased 3.3 percentage points in the year. As expected the debtor book contracted 7.8% in the year as a result of lower product sales and increased repayment rates. Within this you can see the improvement in quality with the bigger contraction being seen in debtor balances which are more than 28 days. Overall, we were pleased with the stability in context of the pandemic year, and the improved customer arrears position.

Exceptional items were significantly lower than the prior year as we have now reached conclusion over the majority of legacy issues with legacy tax structures resolved and the FCA customer redress deadline behind us. This year, the main component was £7.9 million of exceptional costs incurred as a result of our strategic changes. These included total redundancy costs of £5.2 million in order to align the Group’s people costs to deliver an organisational design that supports the revised strategy.

The final point to note on this slide is we continue to have a contingent liability with respect to the claim and counter claim with Allianz. As it is not possible to reliably estimate the amount of any potential financial outflow of this dispute we have continued a contingent liability as opposed to a provision relating to Allianz’s claim of £29.4 million plus interest. As this develops over the coming year we will update this accordingly.

Moving onto the balance sheet and cash. Our net cash generation was £158.4 million in the year compared to broadly neutral in the prior year. Let me walk you through the building blocks. We made significant progress with our working capital efficiency in the year and were able to reverse last year’s £18.7 million outflow and generate £19.5 million through targeted initiatives including successfully clearing through a level of older stock balances. Working capital was released from the contracting debtor book and was similar to the prior year whilst we maintained stability in the securitisation financing. Lower exceptional items and tight capex control reduced our non-operational cash outflows in the year which resulted in net cash from operations being retained of £64.9 million. The equity raise then delivered net proceeds of £93.5 million and dividends were suspended. Overall this combination of managing the business and the successful equity raise resulted in £158.4 million of net cash generation. This leaves us fully undrawn on our unsecured RCF facility, and with a net unsecured cash position of £80.8m, well set for trading and investing into the new financial year.

That leads me to looking ahead and guidance for our new financial year. We expect to return to overall growth with Group revenue up between 1 and 4%. Since the start of FY22 we have returned to product revenue growth and for the full year we currently expect product revenue growth of between 3% and 7%. Similar to FY21, Financial services revenue is expected to be lower as a result of a smaller debtor book at the start of FY22 as this naturally lags the change in trend for product sales by between 6 months and a year. We expect capex of £30 to £35 million, depreciation and amortisation of c.£40 million inline with the FY'21 level and reflecting the acceleration of our strategy, and net interest costs of c.£ 16 million. Overall we currently expect FY22 adjusted EBITDA to be in the range of £93m to £100m. This level of adjusted EBITDA combined with the investment in capital expenditure and working capital for growth, will enable the Group to have a continued strong unsecured net cash position. The Board will consider the resumption of dividend payments at the end of FY22. Finally, FY22 year-end adjusted net debt is expected to be in the range of £280m to £300m.

I'll now hand you back to Steve to talk you through progress on our strategy in the year.

**Steve Johnson:**

Thank you, Rachel. I'll now talk you through our strategic progress in the year. Last June we announced our refreshed strategy to return N Brown to sustainable growth by developing stronger brands and product propositions for our customers, driving profitability through the retail business and continuing to offer attractive and flexible credit solutions. Since then we have made significant progress in transforming the Group in the year and we are now firmly in the "accelerate" phase of our strategy driven by our five growth pillars:

1. Distinct brands to attract a broader range of customers
2. Improved product to drive customer frequency
3. New Home offering for customers to shop more across categories
4. Enhanced digital experience to increase customer conversion, and
5. Flexible credit to help customers shop

These growth pillars are underpinned by our people and culture, data and a sustainable cost base appropriate for a digital retailer. I'll now give you an update on each of these pillars and enablers.

As I said last year, our review of the markets in which we operate highlighted that we needed to extend our reach to a broader set of customers through a portfolio of brands with clearer, more focused propositions. This year we have progressed our simplification journey, reducing the total number of brands by 25% to nine in total. We discontinued the High & Mighty and House of Bath brands, successfully migrating customers to Jacamo and Ambrose Wilson respectively. The Figleaves website has also closed and we now offer Figleaves on Simply Be.

We are now communicating what makes our brands special and unique to our customers through monthly product innovation campaigns such as 'Alfresco Dining' for Home Essentials and 'Denim Re-engineered' for Jacamo. Our use of social media has accelerated throughout FY21. Revenue generated

via social media was up 27% across the Group, with a total of 1.9m followers across Facebook and Instagram. In our 5 strategic brands we saw an 80% increase in Instagram followers.

Looking ahead to this financial year we will undertake a range of activities, including expanding the presence of the core retail brands through increased investment in brand building activity and through more specific, targeted activity through digital and social channels. We will focus on ensuring that our brands are visible in the most relevant way to our target customers. Our first broadcast campaign was launched on Monday for JD Williams. We're also continuing to improve our photographic approach. We are upgrading our in-house studio capability to a market leading LED Studio solution. It balances efficiency with the ability to deliver market leading aesthetics and create a more aspirational digital experience to drive conversion and re-trade rates. All photography for Simply Be, JD Williams, Jacamo and Ambrose Wilson will be shot in this new studio.

Refining and improving our product offering is central to driving our new brand propositions, encouraging customer loyalty and frequency and we have made good progress in three key areas. First, we started the process of improving our product 'handwriting' through clearly defined designs for each brand, investing in fabric, quality and consistency of fit. These changes to our design process mean that our prints are now completely unique to us and our palettes and product are designed with a specific customer in mind. In the year, we increased the proportion of own designed womenswear ranges from 53% to 57%. Secondly, we have redefined our good/better/best price architecture with the purpose of creating product which represents great quality and value as well as introducing new brands which stretch the range within the 'best' category. We have rationalised our ranges to ensure there is less duplication and a clearer more considered offer and these investments are being well received by our customers. We have also made significant progress with launching new third-party brands on our websites, with Hugo Boss and Ralph Lauren both launched on Jacamo in the year. Finally, we have continued with our commitment to embed sustainability throughout the organisation, our product ranges and all our processes. We introduced our sustainably sourced Jacamo men's denim range and 85% of our women's denim offer is now sustainably sourced. We have also further consolidated our supplier base, with an 18% year on year reduction in the total number of suppliers. Throughout the pandemic we were able to respond with increasing flexibility to shifting customer demands and delivered on average a one week improvement in lead times on product changes throughout the year.

Looking ahead we will accelerate our initiatives around improving our product hand-writing, transforming our pricing architecture and driving our sustainability agenda. We are investing in our design team with a particular focus on 'print' and the "famous for" categories such as lingerie, denim and footwear. We are continuing our strategy of attracting exciting new third party brands to extend the top end of our ranges. We added Finery and Nobody's Child on Simply Be and we plan to add French Connection, Sonder and Khost to JD Williams later this year. We are entering the second year of our sustainability roadmap with the focus being on ensuring all denim ranges will have sustainable properties, completing the roll out of Green Polyethene bags across Jacamo and Simply Be and reviewing recycling options for our customers.

We launched our Home Essentials brand as a standalone trading site on 1st April 2020 which coincided with an increase in consumer demand for Home and Garden. We were quick to pivot our offering to address new customer demand trends, for example by expanding our electrical and home office proposition which saw increased demand, particularly during the first national lockdown. This drove

an increase in Home & Gift sales of 25.4% compared to the prior year. In line with our social media strategy we launched Facebook and Instagram pages for Home Essentials in the year, which have now gained over 82,000 followers. This encouraging start has demonstrated the opportunities available to us to inspire and serve even more potential customers through these channels and will support our customer acquisition strategy for the brand.

Looking ahead we will continue to invest in key product categories such as furniture and bedding to accelerate Home Essentials' second year as a standalone website. This will be supported by broadcast campaigns and continued social media activity to drive customer recruitment.

Our strategic priority for enhancing the digital experience for our customers is to transform the website front end journey. This year we have implemented Bloomreach to optimise and personalise each customer's digital experience. This has driven a 19% increase in 'click through rates' from search to the relevant product page and a 55% reduction in 'zero results'. Our agile approach to digital transformation enabled us to launch the standalone Home Essentials website as well as migrate customers from High & Mighty and House of Bath to Jacamo and Ambrose Wilson respectively. We have also started developing new APIs for social media integration to enable more automated re-targeting of customers. Once embedded, this will increase efficiency and is expected to benefit conversion.

Looking ahead we will focus on our strategic priority of transforming the website front end. This is because our existing websites are built on a legacy technology stack, which has been developed over many years. Thanks to the capital raise, we are now accelerating our investment in new front-end websites to improve the customer experience through a cleaner website resulting in better conversion rates and search optimisation benefits. An additional benefit to this is an improvement to site speed which is key to enhancing search engine optimisation. This will include a new sales journey, improved search, navigation, product listing, details pages, bag and checkout functions.

Our focus at the start of the pandemic was on protecting our customers and our business by ensuring continuity of service whilst minimising any risk exposure and ensuring good customer outcomes. N Brown's current credit platform is built on a mainframe system which is robust but lacks flexibility to make changes to enhance the customer proposition. Customer behaviours have evolved and are generally shifting towards a range of more flexible payment products, which the Group's current system cannot currently service. To deliver more modern products, we need to develop a new Financial Services platform that has the flexibility to offer these products and our development project is underway. Good progress has been made in FY21 to enhance the use of different data sources and analytical tools and techniques to drive improvements in our lending proposition. We continue to work with Aire using their proprietary AI models to enhance our creditworthiness process and have also successfully launched a new lending model using the DataRobot tool which has further enhanced our capability.

Our strategic focus for the medium term will be on the delivery of the new Financial Services platform and the launch of new credit products that will broaden the appeal of our proposition. We continue to embed regulatory changes such as the Senior Managers and Certification Regime and remain focussed on providing inclusive financial services to our customers to enable them to shop our compelling products across our brands.

So moving to our 3 enablers, the first of which is People & Culture.

Our colleagues are our biggest asset and they continue to show commitment like no other in their flexibility and adaptability in response to the change in ways of working due to the pandemic. We have remained fully operational throughout this difficult period and we are grateful to our colleagues for the part they have played in this. We have made some important changes to our Executive and Leadership team in the year. Rachel started as CFO in June last year and Sarah Welsh became our first CEO of Retail earlier in the year. In the team underneath the Executive Board, we made important changes, particularly in Product where we have strengthened the team through a series of senior hires and appointments with a new Group Buying Director, Group Design Director and a newly created role of Group Sourcing, Sustainability, Quality and Fit Director. Finally as we emerge from the lockdowns we have adopted new ways of working to ensure that we balance the need for effective collaboration and remote working.

We continue to increase our use of data across the business to understand our customers better and drive continued efficiencies in revenue, marketing and product ranging. We have completed discovery projects to determine the optimal pricing strategies for our brands and we are in the process of building models which will determine how to maximise revenue, margin or other strategic KPIs through promotional pricing. Our use of AI to develop a model to predict customer lifetime value now informs our marketing decisions and has been crucial in reducing unprofitable marketing expenditure and making our cost base more efficient and sustainable. The Group has continued to invest in its people and infrastructure with new key hires such as Data Scientists, Architects and Product Managers to build out modern, cloud-based data structures increasing our ability to deliver rapid insight-to-action analytics.

The final enabler of our strategy is developing a sustainable and appropriate cost base to help build retail profitability. As Rachel outlined, we took swift and decisive action to respond to the pandemic and were able to reduce our adjusted operating costs by 28.9% in the year. We had previously identified a range of sustainable efficiencies in our marketing costs and were able to accelerate these in response to the trading environment. This resulted in our marketing costs falling 55.7% in FY21, far in excess of the 13.0% decline in Group revenue with significant reductions in Paper, PPC, and TV and outdoor media. Targeted initiatives across the entire cost base resulted in adjusted operating costs as a percentage of revenue significantly improving from 39.8% in FY20 to 32.5% in FY21.

For the first time we are now reporting digital customer metrics. However, it's important to remember that this initial disclosure reflects the impact of Covid-19 on the business in FY21 and we are now focused on driving improvements across these measures in FY22.

Total website sessions remained relatively high in the year, despite a 55.7% reduction in marketing expenditure, supported by our ability to pivot into the products the customer was looking for such as home office and garden. As expected and in-line with other retailers, conversion was lower in FY21 due to more customers browsing during the pandemic. The reduction in orders in FY21 was reflective of customer demand and within this there was a significant pivot from Clothing & Footwear to Home & Gift. AOV was broadly similar to the prior year reflecting the strong Home & Gift performance in the year offsetting the price sensitivity in clothing & footwear. The increase in AIV was driven by the mix effect of Home & Gift as this category typically has higher average prices. This mix effect also resulted

in a small decrease in 'items per order' as Home & Gift items typically have a higher price point. Total active customers declined in the year, primarily driven by the reduction in 'Other brands' customers. FS arrears fell due to an increase in the quality of the loan book and an increasing propensity for our credit customers to pay down their balances in the year. Our relentless focus on improving the experience for our customers resulted in NPS increasing by 2ppts in the year to 63.

This year we launched our new 4 year sustainability plan, SUSTAIN, which encompasses our People and our Planet pillars and aligns with the values of the business. We are also proud to have signed up to the BRC Climate Action Roadmap to help the Retail Industry, including supply chains, to hit net zero carbon emissions by 2040. We recognise the huge potential in sharing knowledge and learning from other retail leaders as we join forces and work collaboratively towards a Net Zero UK. Since the beginning of the Covid-19 outbreak we have supported both our local communities affected by the crisis and those who are working tirelessly on the frontline. Through the donation of net sales proceeds from a range of products sold across our sites, we have donated over £20,000 to NHS Charities Together. We also made donations of clothing and household items to frontline NHS staff in Manchester and donated face masks and face shields to a local care home near to our main distribution centre.

This slide highlights the progress we have made in the first year of Sustain. Our focus in the year was on plastics. I'll pull out one of the initiatives and give you more detail. We successfully conducted a trial of Green Polyethylene (Green PE) despatch bags and from 1 March 2021, replaced 90% of our packaging with Green PE despatch bags. This is a bio-based plastic, manufactured from polymer derived from sugarcane and therefore produced from an entirely renewable source. The despatch bags are also recyclable, and their sustainable properties mean that we will save an estimated 112 tonnes of carbon per annum. The roll out of Green PE bags will be extended to 100% of our packaging by the end of 2021. We also made good progress in energy efficiency with a new LED lighting project at our main warehouse and using sustainable swing tickets for JD Williams, Jacamo and JD Williams products.

We first laid out our medium term targets when we announced our equity raise in November last year. We remain confident of achieving our medium term product revenue growth of 7% per annum and an adjusted EBITDA margin target of 14%. From a balance sheet perspective we intend to maintain a net cash position. As Rachel commented, at the end of FY22 we expect to have a strong unsecured net cash position and at that point Board will consider the resumption of dividend payments at the end of FY22.

FY21 was a year of significant strategic progress, the business stayed profitable and is now in a much stronger position than it was at the start of the pandemic. Our product revenue has returned to growth and we expect to deliver adjusted EBITDA this year of between £93 and £100 million. We are heartened by the strategic progress we have made, however we remain cautious on the external environment given the uncertainty around the relaxing of the government restrictions and the end of the furlough scheme. We are confident that our strategy is the right one and we have demonstrated throughout the year that we have a flexible and agile business model which is able to react swiftly to the external environment and deliver for our customers. We remain committed to our medium term targets of 7% product revenue growth per annum and a 14% adjusted EBITDA margin and achieving these will deliver sustainable returns for shareholders.



And now we'll turn to Q&A, so if you are not already dialled into the conference call, please do so now and we will take your questions in a moment.

**Operator:**

First question comes from Andrew Wade of Jefferies. Andrew, please go ahead, your line is open.

**Andrew Wade:**

Hi there, team, and thanks for the presentation. There's obviously a huge amount going on in FY22 in terms of progressing the strategic element, but given how much is going on, could you sort of point us in the direction what you see as the sort of key changes and the things that we should be keeping an eye out for most?

**Steve Johnson:**

Yeah, sure Andy. I think that's a great question. Across our five strategy pillars and if I just talk to those really, really sort of at the high level, and I think what we will expect to see is some sort of further brand advertising, and certainly more sort of appearance at the top of the funnel in social media for our brands as we start to sort of land those. And we have some really exciting plans and actually, JD Williams has already started going live on Monday last week. So, on the brand, there'll be a bit more sort of visibility and a bit more investments, I guess. On the product side, that's an ongoing journey. We've already made good changes already. We've launched some new brands. Our own label is improving and we know that from internal metrics and we're going to keep going at that, because we think that, you know, there's a massive opportunity if we continue to improve that for our customer proposition. And in relation to the home business -- and that one will be a bit sort of as we go. You know, we've launched the website, we're keen to get it going, we've focused on new customer recruitment and it really helped it in the pandemic, but it's something that we're going to focus on really strongly. And also when it comes to the sort of critical pieces in relation to financial services and our digital capabilities, the teams are really stuck into now and delivering the sort of front end for our business and really replacing the old mainframe technology that essentially still powers the presentation there for our retail business and powers all the decision making in financial services. So, it's really important that this business changes that infrastructure out in the medium term. The guys are working on the retail side of the business first, they've made a start -- we got the money, we started spending it and at this stage it's really, really early days but certainly that will be the area that we talk to at the half year and also to bring you up to speed with that. But fundamentally the technology side is an area that is the key thing in our business this year. Hopefully that's helpful.

**Andrew Wade:**

Yeah, absolutely, thank you very much. And I guess as we go through the year, sort of reflecting the fact that your revenue trends have improved through the year, the comps obviously get more challenging as we go through the year. Should we be thinking about that sort of increase in spend on brand building and marketing as being a key driver behind how you're going to continue to deliver revenue growth against those increasingly challenging comparatives?

**Rachel Izzard:**

Yes, so -- Andy, I can take that one. You're correct, we are investing in marketing, our marketing costs will step up faster than our revenue expectation this year and not for the underlying kind of efficient digital marketing below the line, but for getting back into the above the line and brand building, so we're expecting a significant step up in marketing, but we know we've got the efficiency baked in underneath and we've got some level of kind of operational gearing with growth coming back as well. So, yeah, we'll get back into the brand side of the marketing spend, keep the digital below the line, spend very efficient, effective -- that should help power through on the product retail side. As you

say, as we start cycling up to tougher comparisons at the back end of the year plus those steady improvements that Sarah's making for the product side, in particular on the clothing and fashion segments, those already green shoots and particular, as Steve said, and some of our own brand label with a good, strong sell through rates, so that will progress as well as we go through the seasons, through the year. So, those two pillars in particular will help us through quarter to quarter, the technologies, the longer-term play.

**Andrew Wade:**

Right, so very helpful, very clear. Thank you.

**Steve Johnson:**

Thanks, Andy.

**Operator:**

The next question comes from Darren Shirley of Shore Capital. Darren, please go ahead, your line is open.

**Darren Shirley:**

Thank you and morning all. A few for me as well, if you don't mind. Noticing the reduction in sort of the COVID provision and from £17 million at H1 to £15.4 at the year end, I mean, what is the timeline to sort of further the assessments of those provisions? Is the potential for more good news as we move through the current financial year? Any thoughts on that will be good. I mean, we've obviously seen a reduction in cost, some of which will be sort of COVID-related, but some will be structural -- I mean, you've just highlighted there, Rachel, you're now going to be spending a bit more on marketing. If you could give us an idea of sort of how we should look at costs going forward, maybe as a percentage of sales or something like that would be useful. And then finally, just give us a bit of colour on how you see sort of gross margin outlook for the current year, I mean particularly in product, because there's a lot of talk of inflation at the moment, obviously cartons higher, freight cost, labour, any sort of colouring how your opposition there relative to growing pressures will be good as well, thanks.

**Rachel Izzard:**

Okay. I think Darren Steve has just handed that all firmly to me! So, the £15.4 million provision, when we closed out last fiscal year, FY20, we estimated it in our post year which you'll note was £8 - 18 million, half year would put £17 million aside. We tried that up to £15 at the year end. And what we've got driving the data underneath that, we use kind of macroeconomic indicators like unemployment, but we don't actually anchor particularly strongly in our correlation to that. We anchor more strongly to understanding where the customers are seeing kind of stress with their financials. So, we've looked at internal and external data now to see where customers are on payment deferrals due to COVID, so we've got relatively modest deferrals that peaked at three percent and is currently at 0.3 percent, but we've also got the external data now where we can check all our customers and see if they've availed of a deferral elsewhere, either with secured or unsecured lending, and that's a large part of what's driving our provision where we can see customers who are currently or have recently been on a payment deferral.

Now, as that unwinds over the coming months, and the furlough support from a government perspective steps out in September, we'll have another look at it at half year, and then we'll do the full drains up review at year end, at the end of FY22, Darren, to see where the actual behaviour landed versus our expectation. Because what we're doing, and you can see it in the appendices, of the slide deck, where a customer is looking up to date and they're in stage one for the provision model, if they're currently on a payment holiday with us or another provider, or recently have been, we've

moved them from stage one to stage two, because we think it's likely they're under stress. If they can then get themselves back out of stress and up back into stage one, by the time we get to full year definitely we'll know that. But at half year we'll have another kind of look at it. So, half year, we'll talk to you again about it; full year it will be the full drains up to see where we actually land.

That's the IFRS 9 provision. Next question was the cost to sales ratio, is it going up, down, or sideways. So, what I would say, we've done hard yards this year to make sure we are as volume variable as we can be, you could see it in warehouse and fulfillment costs, you could see it in marketing, and even within our S&As our admin costs, we've got a level of volume variability within that as well. So, I would expect it to move as revenue goes up, I would expect costs to go up but we've still got a little bit of operational gearing to go in the fixed cost element of admin. But going the other way, it's a conversation we just had about marketing and getting back in to the above the line side. So, we would expect marketing cost to grow at two to three times the pace that revenue is growing, but we've got some operational gearing still to go in the fixed cost space. So, I wouldn't expect to be exactly the same year on year cost to sales ratio, but I'm not expecting it to go up materially either. So a two to three point increase next year versus this year, as we step back into that marketing but also get some economies of scale through the cost base is where I'm expected to be, but we will be flexible with how we go through the year and where we see the revenue really trending through.

And that leads me into your final question, which was gross margin pressure, a lot going on within gross margin in particular from a product perspective. So, from a mixed perspective, moving back into as clothing and fashion starts to respond, in particular in our own brand, that usually has a positive impact on our gross margin because our own brand clothing is our higher margin segment versus, in particular, home and, in particular, technology. But, as you say, there are pressures going the other way for inflation, but in particular in terms of freight rate, we saw that in quarter four, and within our guidance, we are assuming that level to the current level of freight rate is continuing through the year. So, inclusive with our guidance, an EBITDA of £93 to 100 million is an assumption on continuing tough levels for freight rates. And that's the biggest cost side kicking into the gross margin. So, we haven't guided tightly on gross margin percentages because we need to retain the flexibility to offer the product segment that the customer wants through the year. Now, that could be into fashion, it could be back into home or it could be a mix between the two; it's why we've kept our outlook guide and top-level growth and EBITDA, because we believe we've got the flexibility between type of product we can offer and between the cost flexibility we've now got with gross margin to then be able to flex and hit an EBITDA with confidence. But the mix within that, across products, FS and different types of gross margin, that will still show a lot of development as we go through the year. So, short answer is it's not a single point guidance, we've got a lot of moving parts, but we've got the level of flexibility to be able to deal with those moving parts now.

**Darren Shirley:**

Well, thanks, Rachel, that was all very clear and just one more, if you don't mind, I don't -- I don't want to hog the line, but in terms of have you seen any change in sort of the mix of your customers using cash, taking credit, taking credit and rolling over, has that changed over the last 12 months?

**Steve Johnson:**

Yeah, and I think from our perspective, Darren, we're very, very focused on our medium-term strategy, so we're responding to things on a day-by-day basis, but ultimately, as you can hopefully all see from the results, we've taken our opportunity to really strategically accelerate our sort of focus on our strategy last year. So, the customer file is moving around, again it's not dissimilar to Rachel's answer in terms that we need to see how things shake out, what customers buy into this year, et cetera. I am pleased to sort of say that actually our customers have started shopping back to C&F, and that's a good start from our perspective and we'll talk more about that at the June -- sort of quarterly update.

But fundamentally, there's a lot going on in that customer file, but it is all strategically related, and it is all sort of based on analytics driving where we spend our money. And ultimately what we want to do is get the best return from our marketing spend and, you know, ultimately, we're sort of less concerned whether that's cash or credit. Cash customers can deliver as much profit as credit customers where they're really, really, really loyal, and credit customers we'd like to see the file growing with our investment in our I.T. technology. But as we talked about earlier, the technology sort of investments are going retail first, financial services second. And on that basis, I would just say we'll need to talk about that in the future.

**Darren Shirley:**

Okay, thanks for that, Steve and Rachel.

**Rachel Izzard:**

Thank you.

**Steve Johnson:**

Thank you.

**Operator:**

I'll just remind participants once again to press star followed by one if you would like to ask a question. We have a question from Matthew McEachran from N+1 Singer. Matthew, please go ahead.

**Matthew McEachran:**

Yeah, thanks very much. Just a few follow ups if that's okay. Can we just come back to home and to the -- tie it in with credit penetration and bad debt? So, what's been the experience, I mean, that's an unprecedented kind of makeshift driven by the core business and then the introduction of home essentials. Just get a little -- give us a little bit of flavour about how credit has performed and bad debt. And then, at the end of -- just finalizing on home, if you could give us a sense of as to whether or not the ongoing growth of Home Essentials, you know, could see you roughly maintain sales levels in the home category this year, or whether or not you -- you know, you definitely feel it steps back.

**Steve Johnson:**

We'll take the latter part to that question, Matthew, first of all. I -- so, you know, let's keep in mind this time last year, when we were selling home product, we were selling hot tubs, trampolines, computer desks, computers, we were selling anything that was sort of related to COVID. And actually for us, we were able to pivot very quickly into those areas because we had stock, we were able to spin up our websites. So, we did very well sort of respond to that, given we're largely a clothing and footwear business. And fundamentally, we need to see how this turns out. So, I wouldn't expect the same level of demand in home as we had at this time last year, we also got very few returns this time last year, for obvious reasons. And, of course, a mix shift since sort of clothing and footwear will change the mix on returns again, so I want to make that point. Again, I think we're a little bit early into the year, other than I would sort of just highlight the point again, we're seeing customers shopping back into clothing and footwear in our new products coming through, which we're very, very pleased about.

In terms of sort of customer credit and bad debts, et cetera, as the presentation shows actually, the arrears rate has reduced quite significantly. And this is as a result of a couple of things, we continued to get better, and better, and better at this, and we've highlighted technologies that have helped us with our decisions that are improving customer outcomes, and also, we've seen faster pay back through COVID which is quite sort of common, I think, at a sort of market level on this subject and I've certainly seen it in other businesses results as well. So, stood here today, actually, Matthew, we're in

a better position than we were, so I wouldn't be too concerned about that other than I come back to the sort of predicted COVID overlay which fits within the IFRS 9 provision. And clearly at this stage we have a disconnect between, you know, the performance of our file and the provision increase which is really a predictive piece about the future. We don't know and as Rachel has pointed out, we'll talk more about that at the half year. But as things stand, if performance continues as it is, then we should be in a very good position.

**Matthew McEachran:**

Yeah, that's very good. And in terms of the business, you got a lot more data analytics, which you're putting to good use. In terms of cohorts that have historically come through home, what would -- you know, is -- what has been the historic trend in terms of cross selling into clothing and footwear and fashion? Is this an area which is a good lever to catapult into that category, or actually are they -- do they tend to shop in home and do very little elsewhere?

**Steve Johnson:**

Well, there is some cross shopping and that occurs historically. That's a really difficult question to answer, Matthew, I'm not trying to be sort of --

**Matthew McEachran:**

Yeah -- no, I understand it's difficult, just your best guess, yeah.

**Steve Johnson:**

We set up Home Essentials in the middle of the pandemic, so the shopping behaviour around Home Essentials is not necessarily helpful in predicting future sort of cross shopping. I expect us, you know, to be able to do that, that is part of the strategy, so if you go back to the five pillars, the whole, you know, reason for sort of launching a home business is we think we can do well in it and we think it's very relevant to increase that cross shopping piece that we're sort of targeting.

So, that's where I would expect it to go, over the sort of medium to longer term. It's just the data from last year, again, you know, hot tub shoppers are not, you know, not necessarily going to give us the data we need to really understand those patterns truly at this stage. But I think, again, by half year, hopefully we'll have something more that we could sort add a bit of colour to.

**Rachel Izzard:**

And particular, we stood out on JD Williams a lot more because JD Williams is more of the department store brand, and through last year you could see the customer very much pivoting into -- the basket was going towards shopping for the home. And then you could see it pivoting back into clothing and fashion. So, you see that cross shop at its most extreme in JD Williams, and in particular we've got very clear kind of predictive analytics around the value of customer, the customer likes on value. If somebody's long standing credit customer with us, if they've shopped on both home and fashion, then re-trade rate is the highest out of any re-trade rate and their long-term customer lifetime value is the highest. And so, we're very clear with how we kind of focus our time and resources and energy with the team on where we know, kind of, customers stay with us and shop with us.

But as Steve said, we've then got some odd exceptions through the pandemic year of you saw some real spikes of customers that essentially are the one-and-done, but we did make money on the one-and-done because they came in, bought the hot tub, we made money on that transaction, they moved on. But we do get the ability to re-trade and re-market to them through the year, so we can try and keep some of them with us, so it's not a sort of complete always a one-and-done. But you could see some really different behaviours through the year. The JD Williams I think is where it -- where what you're talking about is the most prevalent of that win-win where we've got credit as well as cash and

we've got the opportunity to serve the customer with both home and with fashion.

**Matthew McEachran:**

Yeah, that's interesting. Okay, thank you. The next question just goes back to some of the discussion earlier on the Q and A, just around the product sales guidance. I mean, obviously we do have these very, very unusual comps, you know, we've had lockdown three through part of the first quarter, et cetera, et cetera, we know all of that. But just looking at the guidance, the guidance gets you only within, you know, 10 percent of the two-year equivalent. So, I'm just wondering -- and everyone in the markets is looking for the two-year numbers, I mean that's the, you know, all our clients are demanding those numbers and some reference point to pre-COVID. So, is there anything you could tell us, just in terms of how you budgeted for that product sales growth in terms of the two-year trend? Because it feels -- it feels still like a modest number and I'm not really pushing through into real growth without wanting to sound too cynical.

**Steve Johnson:**

No, I understand the question, I think. I mean, the one thing I would remind you is the business is going through a transformation when looking at the organizations and while most businesses are transforming clearly, this one is going through a fundamental one. And so, you know, if I look last year, our product revenue is only down 13 percent for a 55 percent reduction in marketing.

Now, some of that was cost saving at the start, but some of that is very, very strategic. And I think a comparison to two years doesn't really sort of do justice to what we're trying to do in the medium term here, which is, ultimately, when you look back through last year, we took a really accelerated view of the things that we were probably going to do over two to three years. A massive reduction in the marketing spend, a massive reduction -- a massive change in the way that we are speaking to our customers, the building up of sort of social media files, and data and analytics driving sort of forensic decisions within the organisation, the 25 percent reduction in our sort of brands from a rationalisation perspective, all of that took place last year. So, in the middle of the pandemic, you know, we were able to take really, really radical actions.

And on that basis, you know, the business just looks different to being two years ago. So, at this stage we're looking where we are now and we're looking ahead, we're not looking back two years. I do understand that people will be asking you for that, but, you know, it's a completely different business.

**Matthew McEachran:**

Yeah. And just a quick one on the drags. I mean, there's been no mention of house and bath and Figleaves where you're -- you're obviously trying to drive an improved profitability of, you know, of less revenue. Could you just give us a sense as to what the drag year on year is from those two? You know, within you three to seven, what's the drag from those two?

**Rachel Izzard:**

So their particularly high in half one as well. That's what I was going to say to House and Bath and High and Mighty cycled out at the end of quarter two last year. We tucked them in under remaining brands, but as you say, you retain a core kind of very loyal customer, but we knew we'd lose the long tail but did it for the right profitability reasons. So, House and Bath and High and Mighty will be a particular half one drag, and Figleaves is a drag across the full year. We're not, in particular by quarter, we're not giving exact details with that, but it is a good -- just trying to think --

**Matthew McEachran:**

Must be a couple of points, or something?

**Rachel Izzard:**

It is very different in particular in the first half of the year, it is. And as you said, we did that for profitability reasons, because you look at our EBITDA margin even in FY21, it was 11.9 percent and that's inclusive of a two point drag with that IFRS 9 COVID provision, so we're essentially at our 14 percent EBITDA margin level that we used in terms of our medium-term targets.

But we're looking for profitable growth at a decent punchy EBITDA margin, rather than massive growth at low single-digit margins --

**Matthew McEachran**

Indeed. Yeah, yeah, much better quality earnings. No, no, I get that. Okay, well maybe if we just pick up --

**Rachel Izzard:**

It's a cuter story to sell, but it definitely generates a good return. So yeah, bigger drag in the first half of the year, some level of drag through the whole year as those other brands restructuring, and a focus on EBITDA margin, not just top line.

**Matthew McEachran:**

Yep. Okay, thank you very much, just a couple of other quick ones. Within your EBITDA guidance, and -- which is obviously got that cost, you know, assumption build in, do you build returns rates back into -- you know, back to what they were pre-COVID on a like for like category basis? Is that your assumption, even though it may not yet have already happened?

**Rachel Izzard:**

Short answer, yes, so -- but the bigger answer is the like by like by segment, because it's the mix element.

**Matthew McEachran:**

Yeah, that's what I mean. Yeah, yeah, yeah. That's fine.

**Rachel Izzard:**

That's the biggest swing. We will see a big swing from a mixed perspective as we come back into clothing and fashion. We do assume progressively the pandemic behavior washes out, but we will still retain a certain level of improvement in fit-type behavior on the fashion side, in particular, because we already had a relatively low returns rate compared to the broader fast fashion market. And our focus on fit through the year, we are seeing underlying slight improvements in returns rate relative to what we're doing strategically with the product.

**Matthew McEachran:**

Yeah, great, okay. Thank you. And then the final one, just in relation to supply. I mean, I get the sense that your supply and availability isn't being particularly affected by, you know, global issues, but I just wondered if you could maybe just talk about India, specifically, in relation to whether or not you've got any concern as we move forward towards -- well, towards autumn, winter.

**Steve Johnson:**

Yeah, I think that's a great question, Matthew. It is this something we have on a sort of watching brief. We're continuing to work with our suppliers. If you look at India there, the factories are still producing in India at this stage. The various lockdowns and various things going on across the world and India, you know, our sort of thoughts go to a lot of the sort of colleagues who are impacted by that. Bangladesh is another one of our sourcing areas as well, as is Turkey, which currently went into a

lockdown. So at the moment our stock position is actually quite strong. And we have not seen any significant disturbance from the sort of short-term issues that have existed, other than a few minor disruptions in some categories, like garden furniture.

And we have it on a watching brief as we go forward, but ultimately at this point and time, our stock position is strong and also in Q2 that sort of comparison to our stock position this time last year -- as we hit Q2, our stock position in Q2 last year was reasonably low. And principally because we took radical actions at the start to preserve liquidity. So, there actually it was cycling against a better position this year, even if we have some disruption in the supply market. But we are working globally to make sure that the business not only has the right levels of stock, but ultimately is supporting, where we can, some of our colleagues in other countries.

**Matthew McEachran:**

Yep, yep. Excellent, that's great, thank you very much indeed.

**Steve Johnson:**

Thanks, Matthew.

**Operator:**

We have no further questions, so I'll hand the call back to yourselves, Steve and Rachel.

**Steve Johnson:**

I'd just like to say thank you. The business, I believe, is exiting the pandemic, at this stage, stronger than when it went in. We remain committed to our medium-term strategy and all the actions we're taking in this business is to create shareholder returns in the medium term. Our product revenue guides in the medium term of seven percent per annum at a 14 percent EBITDA margin that we remain confident in. And with that, I wish you a good day. Thank you.

**Rachel Izzard:**

Thank you all.