N Brown Q3 Trading Statement

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Overview

Angela Spindler

Chief Executive, N Brown

Welcome

Good morning everybody, thank you very much for joining us this morning. I am here with Bethany Hocking and Craig Lovelace. Before we take your questions I am just going to give you an overview of the period, and add some additional perspective to the statement.

Revenue Performance

We are pleased with the revenue performance that we have announced; Group sales are up 4.1%, made up of product revenue up 4.3% and financial services up 3.7%, so we are ahead of consensus for both. We have also reported today a change to gross margin guidance, with product gross margin coming down slightly and financial services margin improving slightly.

Gross margin guidance

Just to add a bit of colour to this, in product margin the impact was largely the consequence of what I would describe as an unusual season from a weather and phasing perspective; so we have a higher participation from home and gift revenues, but additionally the mix in fashion sales favoured lighter-weight products. For example, t-shirts as a category and rainwear were up 17% and 10% respectively, but this was somewhat offset by lower sales in outerwear and heavier knitwear. This mix has therefore impacted margin guidance, as in the statement.

In financial services we are pleased to report an improvement in gross margin guidance as a result of continued improvement in the quality of the credit book. Just reiterating therefore, overall we are on track to meet full-year profit expectations.

Christmas trading

Specifically in terms of Christmas trading, Black Friday and Cyber Weekend created a real kick-off point for our peak trading period. This worked really well for us. Black Friday was a record day last year and it was a new record day this year at £5.8 million of sales, up £800,000 on last year. So we were pleased with that and, as I said, that really kick-started peak trading. The three Power Brands (JD Williams, Simply Be and Jacamo) saw active customers up 12% and all three brands recorded double digit revenue growth year-on-year, really driven by our online performance. Product offering continues to improve, as do our digital marketing capabilities.

JD Williams

Just on JD Williams specifically, we talked to you at the interims about the divergence between the JD Williams Brand, which we have modernised and is becoming a real go-to brand for the stylish, online 50-somethings, but then the more traditional titles within the JD Williams Group of titles, namely Ambrose Wilson and Fifty Plus. This trend that we described at the interims has continued in the period, so the JD Williams Brand was up double-digits, the traditional titles within the group were down high single-digits, so overall the JD Williams Group was marginally positive. We will update you at the prelims on the changes we are making to better target these quite distinct customer segments.

Online

Turning to the business overall, our transformation to a truly digital-first retailer has a taken another significant step forward this period. Online penetration was up five percentage points to 66%; this means that online sales were up 13%, and if we look at new customers, three quarters of demand from new customers now comes online. Mobile devices generated 68% of our traffic in the period, that is up ten percentage points year-on-year, and we yet again saw improvements in both conversion, which is already industry-leading, and cart abandonment rates, as we continually improve the online experience for our customers.

International

For International (USA and Ireland) it was another good quarter, up 20% and 4% respectively. Just to reiterate, we have reduced marketing investment in the USA until after the launch of the new website next year.

Stores

Moving onto stores, we are a bit disappointed in the performance of our stores; to remind you, we have 15 Simply Be/Jacamo stores and 13 High & Mighty stores, so the channel still only accounts for less than 3% of overall revenue. Like-for-like store sales were flat, with the main factor being year-on-year declines in footfall over the Christmas trading period.

Fit 4 the Future

On Fit 4 the Future, our business transformation project, we are now in the implementation phase and in this period we launched our Simply Be euro website which is really the foundation of our global multi-channel release, and PowerCurve, which is part of our credit release. These both landed seamlessly which we are delighted with and, whilst we still have a lot to do, these releases do mark a key milestone in our technical transformation.

Just further on that, we have previously shared the detail of our implementation schedule for the project, and we are flagging to you today a slight change to the roll-out plans which has been based on the learnings that we have made in this testing phase and will ensure that the customer experience is improved through the transition. The timing has been further influenced to avoid any disruption to peak trading. It is important to stress that the overall costs and benefits of the project are unchanged.

Summary

To wrap up, we are pleased with the figures that we are reporting today. Whilst there is still more to do, I am particularly encouraged with performance of our Power Brands which have been achieved with great products, a compelling presentation to our customers and excellent digital marketing initiatives. I will end there and hand over to you; Craig and I will be happy to take any questions that you might have.

Q&A

Joe Spooner (Jefferies): Good morning. Can you just talk a little bit about how the service proposition worked over some of the spikes in trading that you saw through the period?

Angela Spindler: We are really pleased with service. We announced at the interims the latest results from the Institute of Customer Service report, and we have just had our most recent results out which show that we are still number three in multi-channel retailers, just behind Amazon and John Lewis, and in fact over this trading period we have closed the gap on those two retailers even further. So that is good independent recognition of our customer service.

Just to give you some more factual commentary, our delivery time year-on-year improved, so we got our orders out to customers quicker in spite of higher volumes, and we recorded lower levels of customer complaints and goods-not-for-resale calls. So it has been a really good season and we are really pleased with operational performance over the trading period; our logistics team did a terrific job.

Joe Spooner: When you are talking about improving the customer experience through the implementation of the Fit 4 the Future, specifically what are you talking about in those comments?

Angela Spindler: As you know, there are two major projects under way. One is launching our new websites and, as I said, we have already got that live and up and running in a low-risk way on our Simply Be euro site. The other is the transformation of our credit proposition, giving us much more flexibility in terms of financial services. When we have gone into the testing phase we have recognised that we only want to make one change for customers, so we want to launch both the new credit offer and the new website at the same time; to do that is no more complex, but it does adjust the timing and moves things out a month to six weeks. We felt that for our Power Brands in particular we were then too close to peak trading for us to feel comfortable about the timing that that implied, so we have moved the launch of our Power Brands transformation over to the new site until after peak trading 2016. That is the reason for the change, and it is just the right thing to do.

Paul Rossington (HSBC): Well done today on your numbers. My question also relates to systems: can you just confirm that there are no day-to-day systems or critical systems that you need that could now be perceived as any kind of issue with regard to trading going forward? I know you have got the big project which is all about the long-term stuff, but I would just like to know that the day-to-day systems management is robust as well during this transformation phase.

Angela Spindler: Again, this relates to the customer service point that we made earlier; our performance in terms of IT service over Christmas was improved year-on-year in spite of huge increases in traffic to our site. Our IT systems remain robust. The issue, as I think we have explained many times, is not that our systems are vulnerable in that respect, but that we are not fast, agile and flexible enough to really trade the business in real time. These are the capabilities that the new sites give us, but we are not flagging any risk to the business as a consequence of this decision at all.

Paul Rossington: Thank you very much. You announced that you recruited somebody to come in and run your financial services customer service proposition; can you remind us whether he has landed in the business yet?

Angela Spindler: He starts on 1st February. It is Steve Johnson.

John Stevenson (Peel Hunt): Firstly, on financial services: is the credit quality too good? The margin boost has been very impressive; is there an opportunity maybe to be pushing out financial services revenues a little bit more strongly, perversely?

My second question was just on interest-free; I think you put on a 0% interest-free offer for peak. I wonder if you can talk about how that went, and how successful it was at recruiting new credit customers over the peak period?

Finally, just on the JD Williams suite of brands. Obviously traditional brands are going to be in long-term decline, but high single-digits seems a little bit faster than we might have anticipated; do you think that is down to the focus on the core JD Williams Brand or can you give us a bit more information on why the decline is so great?

Craig Lovelace (Group CFO, N Brown): Good morning, John. I will take the two financial services questions and then pass across to Angela for the third. Just on financial services, I do not think you will be surprised to hear me say, 'Steady as she goes.' I am heartened by the performance; there is a fine balance being struck here between tightening the credit pool too much, as you rightly point out, and clearly I am heartened by the new credit customers that we have recruited as well, but it will take time to evolve in terms of their credit history and to see what bad debt risk they represent. So I am heartened at the moment; this is more about the last 18 months and the changes in policy, in tightening of procedures, than really a story of just four months. So for me this is an evolution of what we explained in detail at the interims; I think it is 'steady as she goes' at the moment, although this performance is heartening.

On the interest-free point: this was a relatively small test and we are encouraged by elements of it, but clearly from a timetable perspective the period we opened the accounts up for new interest-free customers, I am still taking stock of the bad debt risk on those customers; it is still only a couple of months since they signed up and I need to give it at least three months to really get a representative sample as to the risk of those customers. Again, it has been a useful test, certainly well ahead of a time when we may or may not open it up more widely.

Angela Spindler: I will just pick up on the JD Williams question with the high-single-digit decline in some of the titles within the JD Williams Group. I agree; I think we can improve on that. It is a declining market, but we do already have a business unit, or a segment, if you like, which looks after traditional customers, and we have got brands within that which are doing very well; I would call out specifically the House of Bath as an example of that. What we are going to do is take the more traditional customers from the JD Williams Group and move them into that traditional business unit sector to better look after them from a marketing communications point of view.

So it is a declining market and strategically it is a hold rather than an invest-to-grow, but we certainly think we can do a bit better than we are reporting today and that is one of the opportunities for the coming season.

John Stevenson: Thank you. One last question: is there an implication for next year's consensus from the pushing out of Fit 4 the Future, particularly of the Power Brands? I do not know whether the cost benefit would give it a little bit of downside to next year's numbers.

Craig Lovelace: One thing that we have called out previously is that original plans we talked about at the interims were that some benefits would start to accrue in the second half of FY2017; I think some on the call will have embedded elements of benefits in, and I think they need to take on what we are speaking to in terms of the six months to date in that. So we are not going to be drawn on specific numbers; clearly we are not talking about the overall project in totality, but certainly the upper end of the range of forecasts may have benefits incorporated. There is no significant change in overall consensus.

Adam Cochrane (UBS): Good morning, two questions if I may? Firstly, on market share, how do you think you have performed on the clothing market share over the period? Within that specifically, I know you have been trying to make inroads into some of the smaller sizes, the 14s and 16s; can you see if there is a differential in your performance between your more traditional clothing sizes and some of the smaller sizes?

Secondly, on homewares there has clearly been a great performance; do you find that with homewares this is more cross-sell to existing customers or is homewares driving some new customers yet?

Angela Spindler: On market share, we are growing share in ladies and menswear; that is good because the market segments we are in are growing, so they are attracting more competition, as is always the case. So that is good news. On homewares, we do not market homewares independently; when we recruit customers we recruit to fashion, and then when we bring those customers in, based on our fashion proposition, we then sell a whole host of other products to them. We will continue with that strategy; so we are not using homewares to bring in new customers, but we are certainly finding that the customers who come to us are buying into our great homewares range. We are continuing to improve that range in the same way that we are working on our fashion ranges, but we do not use it as a recruitment vehicle; we invest our recruitment spend in fashion.

Adam Cochrane: In terms of the clothing piece, how is your push into the smaller sizes going? Is it a better performance than the larger sizes, in line?

Angela Spindler: Just to be clear on that, the reason that we include the smaller sizes within our ranges is because we want to be an inclusive brand rather than exclusively plus-size. We think that is important; we do not want to alienate anyone on the basis of size. So it is in there for a variety of reasons. To be clear, our bestselling sizes in Simply Be are 20–22, and our bestselling sizes in JD Williams are 16–18. We are seeing in JD Williams, particularly in the contemporary customers, that we are getting good growth in some of the smaller sizes, so we are appealing to a broader 50-plus market from a size perspective. Our ambition is to be a go-to fashion brand regardless of size, not because of size; that is something that is very important to us.

Matthew McEachran (N+1 Singer): Good morning. Can I just come back to the question of the JD Williams migration; you hinted that you think you can do better there, but could you just give us a bit more flavour? It is an area which is a little bit difficult, it has not been the most transparent area of the business and the plan; is there anything you can say today just to give us a bit of confidence that, going forward, that legacy part of the business, the older customers, you really can do better and the reasons why?

Angela Spindler: As I just explained a moment ago, we have split the business into three broad customer segments, driven really by the way people shop. So we have got our truly digital brands, which are Simply Be and Jacamo; well understood and growing nicely. We have then got what we call our 'department store brand' which is JD Williams group of titles; so exactly the same product offer and exactly the same marketing communications, but customers within that group were signed up to different titles. I will come back to that in a minute. Then we have got a third segment which is what we call 'traditional', and within that you have got brands like Julipa and House of Bath; it is predominantly a catalogue-driven, direct-mail driven old way of working, but it is still has an important and valuable customer base although the markets are declining.

Within 'department store' we have found that our more contemporary marketing communications – TV campaigns and digital marketing, as well as our renewed and improved direct mail activity which is still an important stimulus for sales – are really working well for that more contemporary customer, but are working less well for the more traditional customer which sits within those titles. We are going to move some of those customers over into the 'traditional' segment and look after them in the more traditional way in terms of how we communicate to them, so the frequency and style of our marketing communications.

It is as simple as that, really, and the best way to keep it simple is to say within the JD Williams group of titles, many of which have now migrated to the JD Williams Brand and that is working well, the most traditional style of customers is Ambrose Wilson. That is the reason we have not migrated it, and actually the fit from the perspective of what those customers respond to and how they choose to shop makes us feel that they are going to sit better within that traditional segment. So when we report going forward, you will actually see the business listed differently and it will therefore be more transparent about which segments our brands are coming from.

Matthew McEachran: What is the phasing? It sounds like this is well thought-through; have you actually already commenced that slightly different approach?

Angela Spindler: We have adjusted the programme for the season that we have just launched, Spring/Summer 2016, for those Ambrose Wilson customers.

Matthew McEachran: Thank you for that. Just coming back to the financial services side; I heard the question from John, and the response that you are happy with the 'steady as she goes' approach, but I just wanted to check whether the gross margin new guidance was entirely underlying, or is part of that driven by some more disposal of previously written off debtor files?

Craig Lovelace: It is underlying, Matthew. Just to clarify what we mentioned in October, we are now on what we call a forward-flow arrangement on our debtors, so ultimately we do not have significant slugs of debt to sell in one-time hits; it is part of an ongoing normal business model. Clearly as you improve the quality of your credit book you are going to have less debt to write off anyway. So that guidance, a slight nudge up, was generally a reflection of the ongoing move and improvement in the book.

Matthew McEachran: That is interesting, thanks. One final question: the way you have referenced performance in stores; just to check, are you viewing this as a temporary setback driven entirely by unusual conditions, or does it at all alter your thinking about the further rollout of stores?

Angela Spindler: We are not announcing any change to our strategy. The thing that we have not called out specifically in the statement, but it is definitely worth restating: the halo effect of our stores on our online sales in their catchments continues to be compelling in itself. We think our performance reflects what went on in the sector; we are still disappointed, we would have liked to have done better than flat in terms of like-for-like sales growth. However, we have put into play the efficiencies that we talked to you about from the store review at the interims. The stores still play a role in driving our overall business and, in that sense, are important to the strategy, but they are not a big driver of revenues. In overall revenue terms it is less than 3%, but it does help to drive online sales and that is key.

Matthew McEachran: That is what I thought you would probably say. Well done, thanks very much.

Simon Bowler (Exane): Good morning, just a couple from myself if that would be okay. Firstly, just to check something, it looks like there is no net space contribution in the quarter; is that the net of new stores opening and the clearance stores that you shut?

Angela Spindler: Yes, we did open one store, Exeter, which is not like-for-like; it is absolutely tiny in the scheme of things so it did not touch the dial on like-for-like sales. However, other than that, yes.

Simon Bowler: Okay, great. Just to follow up on the financial services where there is that change in gross margin guidance; it looks to be equivalent to somewhere around a £5 million improvement in the profitability flowing through this year, which feels like quite a high number coming through from that. Can you give some colour on how much of that change has come from low bad debt arising on sales that you have previously made, and how much is coming from forward assumptions on bad debt from sales made in the period?

Craig Lovelace: As I mentioned earlier, it is primarily the ongoing improvement in quality of the book. I am not seeing or calling significant ongoing big one-time sales of debt impacting upon that guidance change, so it is a general improvement and a general tightening of governance.

Simon Bowler: Sure. Finally, can you possibly just help in terms of thinking about the fourth quarter? I know you will not want to give too much guidance on this but, with regards to financial services in the fourth quarter, last year we saw a very steep revenue decline come through from that part of the business; how should we be thinking about that? Is whatever drove that something which we should be seeing bounce back this year, or is something more like a continuation of current growth rates a more reasonable way to be looking at it?

Craig Lovelace: With a smile, Simon, I will not be drawn on the fourth quarter; this is ultimately a call on the last four months, and we are not expecting a consensus for the full year to change, as we have commented.

Simon Bowler: Fantastic, thank you.

Angela Spindler: Thank you all for dialling in this morning and thank you for your questions. As I said at the outset, we are pleased with our performance in the quarter and it is a good step on our transformational journey as well. Bethany just wanted me to let you know that she is going to be around all day if you have any other questions that you would like her to help you with. Thanks again.

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