

N Brown Q3 Trading Update

Steve Johnson:

Good morning, everyone, and thank you for joining the trading update call. I'm Steve Johnson, CEO of N Brown, and with me is Craig Lovelace, our CFO. I'll start off with some highlights before handing over to you for Q&A. As I'm sure you've all had the chance to read this morning's statement, I'll keep it relatively brief.

In short, the business is performing as we expected with trading during peak cyber and Christmas periods about where we thought it would be in what continues to be a challenging and competitive market. As expected, and as we outlined at our half-year results, our products sales have continued to decline as we've scaled back off-line marketing and recruitment. This is entirely consistent with our stated strategy of focusing on online profitable growth and improving marketing efficiency.

Pleasingly, online power brands with our core product focus were up 6.4 percent with Simply Be, Jacamo, and JD Williams all delivering online growth between 6 and 7 percent within the period. The group's digital sales now account for nearly 79 percent of product revenue, up from 71 percent in the same period last year. Despite the highly promotional environment, we're pleased to report a stable margin performance as we benefited from a more targeted and efficient approach to our promotional activity. This means that we've been able to maintain our product margin guidance for the full year up between zero and minus 100 basis points. We saw good performance and good progress also in Financial Services which continues to perform well with revenue up nearly 10 percent, and international has begun to stabilise following some of the changes we've made particularly to our marketing strategy, where we are starting to reengage with our target customer base.

So, based on a maintained margin guidance, continued strong financial services performance, and improved operating efficiency, our full-year expectations are unchanged, and with that, I'll open up the questions, so over to the operator.

John Stevenson, Peel Hunt:

Good morning, Peel Hunt. Couple of questions, please, if you can. Just from my experience in the details behind the 23 drop in Traditional in terms of which brand it's coming from, I guess maybe on from that, what's the plan here? Are you going to manage the business through cash? Is it sort of minus the cash but expected to wither on the vine, or was there a sort of more strategic [unintelligible] to be had?

And then second question is on gross margin. Obviously, it's been a very, very promotional backdrop as you pointed out. Can you talk a little bit about sort of year-on-year promotion levels on how you managed, how basically you traded the season most sort of pulled back from mode level to promotions we've seen elsewhere?

Steve Johnson:

Yeah, so we'll cover the traditional question first, John, so I mean in terms of where the big

decline is, I think it would be okay to point at the fact that the biggest decline is in one of our brands called House of Bath. House of Bath is predominantly a paper-based activity and having spent some time exploring I guess the marginal benefits of that paper activity, we've taken some strong management actions, specifically on that brand, so the majority of the fall-off would relate specifically to that area.

In terms of the second part of that question, which is how do we see Traditional going forward, well, I'm going to give the same answer I gave at the interims, which is at the end of the day what we're keen to focus on is online shoppers. Traditional shoppers - we do have some online shoppers. It's not all paper-based, and we will be encouraging as many shoppers online as possible, but we will also be absolutely focused on making sure that any off-line activity, any paper-based activity produces a positive return, so we're not walking away from Traditional. What we are saying is that we would like as many of those customers to come with us as possible into an online journey, and we have targeted pieces of work on that.

And I guess in relation to the second question, which was around how we held the product margin, well there's a combination of different factors that I would say play into this, but fundamentally we have accelerated over the past few months, our use of data and analytics. We are specifically building models that are helping us with our promotional activity and they are looking at profit pool analysis around sales that we operate at any point in time, and therefore getting that balance between the right top level and the right bottom level to produce the greatest profit pool. So, a lot of it is in relation to our well-articulated strategy of focusing on data and analytics to drive profitable growth. And I think, you know, there's little more at this stage I'd go into, aside from, you know, we are three or four months into accelerating that, and we will expect that to continue and we'll get better at it over time.

Craig Lovelace:

The only thing I'd add to what Steve stated is of course that consistently we've said don't just get fixated on just the product gross margin line. From a promotional perspective, we will see both the marketing pot and gross margin depending on what the benefit from the customer will be and sometimes a combined pot. So again, our guidance has changed, you'll see that ties in further to the outside on operating costs. We will counter play those two if we feel a product promotional discount is better placed than marketing. We will make those calls. But it's all part of a combined focus on data analytics and ROI.

John Stevenson, Peel Hunt:

Okay perfect. And I think just coming back around to Traditional brands point, I mean it gets an annual basis, 260 million-ish. And, you know, are you saying, "Okay, this is just going to continue to decline into, you know, a £150 million business," or is there actually, you know, are you intending to sort of hold on to more of what you've got, or take [unintelligible] brand?

Craig Lovelace:

Yeah, just taking a step back, as well, I mean we're not going to give that long-term guidance at the current time, but the reality is there is also a cohort of customers increasingly shopping online and we are well placed to serve those. So, I think to think "Traditional" as an overarching category we're dialing back from in totality is the wrong way to look at it. We're dialing back

from methods, which are predominantly offline, costly, and non-profitable. We genuinely believe there's a growing cohort of customers, especially in the Ambrose Wilson brand, who are online, who we serve well, and have a long-term proposition. So, that's a very high-level answer to a detailed question, but I wouldn't be considering in the mid-term a total dial-away from traditional, because I think that's walking away from longstanding, valuable, profitable customers.

Steve Johnson:

We have in essence online shoppers who want to shop us, and you know, our job here is to encourage more of those to step across that channel.

Matthew McEachran, N+1 Singer:

Good morning guys, Matthew here, a couple of questions if that's okay. Can we do a little bit more analysis on the offline marketing kind of comments you've been making. I mean we know that there is a large pool of investment that goes into print. Could you maybe just give us a flavor of how much you've changed, you know, in these three to four months that you're referring to and, yeah, how much more there is to go for on that side as you realign the spend?

Craig Lovelace:

The targeted move away from paper into online modes has been one that the group has been really demonstrating over the last three to four years. I mean the acceleration's been in keeping with the strategy, and I'm not going to call out specific percentages, but the reality is we've been very targeted in identifying in particular those what we would call off-the-page adverts, which often are just highly promotional, stimulate a one-time purchase, don't necessarily see a customer returning, and certainly have no attraction to the customer to consider the personal account. So, that ultimately when you add in the operating costs, is making you no money. Those are the areas we've really accelerated in keeping with our strategy, more than perhaps has been in the last three to four months. That's the core cohort.

Matthew McEachran, N+1 Singer:

Yeah, yeah. I mean, I guess what I'm trying to get to is, is this the thin edge of the wedge? Is there a substantial pool still to reassign as we go into the new financial year or did you achieve a lot of that in this period?

Craig Lovelace:

We mustn't focus our eyes, not just on paper. I think we have ramped up our spend, obviously, on digital and the same technique that we're applying to paper and customer attribution, we're applying [unintelligible]. Do we actually get a profitable outcome from our digital spend as well? So, I think that there is still more to go on efficiency.

We have brought our paper spend down, but it still makes up an important percentage of our cost, so I do think there's still space to go, but it's not just about paper as well, it's about overall how marketing is performing and, so we are still broadly £160 to £170 million as our operating cost, so I do think there is opportunity, but it's in a targeted way.

Matthew McEachran, N+1 Singer:

Yes, okay thanks for that. And then the second question was just in relation to the overall guidance on cost. You know, some of it is around this marketing, but presumably there is some volume-related reduction in cost as well. Then has any of your planned investment, reinvestment in costs been deferred or is there none of that, it's all underlying efficiency and volume-related savings?

Craig Lovelace:

It's underlying efficiency and it's exactly as you say Matthew. We're being careful, especially given the macro backdrop, but the fact is it is in plan and it is predominantly, given the shape of our P&L, it's predominantly coming from marketing cost.

Matthew McEachran, N+1 Singer:

Okay. All right, that's great thank you very much.

Caroline Gulliver, Jefferies:

Just to focus on the positive for a little bit, looking at your power brands online that were up 6 to 7 percent, is there any highlights by product category for each of the three brands you could draw us to, and then it's a second related question regarding the market as a whole. What sort of seasonality or changes by month through the period have you seen given that we've had some quite sort of widespread swings during the trading period across the industry?

Steve Johnson:

Yes, and we have indicated that it was broadly in line with our expectations. Actually, in the Black Friday week we had a record week for this business. We've chosen not to major on that because in the round it's pretty much where we expected it to be. We did actually ship over 1 million parcels out of our distribution centre in that week for the first time ever, so we were breaking records that week, it was great. I think one of the highlights for me in terms of product sales is again relating to our focus internally within ladieswear dresses, so our own brand ladieswear dresses were up around 10 percent over that period, over the peak trading period, and I was delighted with that for obvious reasons, in the sense of it's not just about what we're taking different decisions on it in terms of discounting, but it is also about the products that we sell, and getting a 10 percent increase in our own brand dresses through that period was very pleasing actually. So, in essence, there are some highlights and ones we're very pleased with. In terms of the shape, I'm aware that other retailers reported a spike in sales on the run-up to Christmas. We ourselves saw a slight increase in December over November for exactly the same reasons, but again, in the round pretty much where we expected it to be over the period.

Craig Lovelace:

And the only drawback to that Caroline is it's of the 18-week trading statement. September was a tough month. I think we're in keeping with the market on that, everybody's focus is clearly on November and December, but September was clearly a tough month and we saw improvements as we went through until October, but that clearly is reflected within the overall 18 weeks.

Caroline Gulliver, Jefferies:

That's great and we've talked quite a bit about marketing this morning and wanted to know if there is anything you're doing in terms of sort of more brand-building marketing as opposed to some specific promotion or, you know, cost for acquisition marketing? I'm just thinking about brand awareness, that sort of thing.

Steve Johnson:

Yeah, so, I mean, we have got an ongoing piece around sort of brand awareness and we've continued with that through the periods. I can say to a question earlier, "Have we cut back from anything in terms of investment in the future?" No, and awareness is an area that we continue to invest through the period in the same way that we were before. The statement does highlight that we are considering I guess propositions around sort of JD Williams particularly, which again is consistent with what I said at the interims, we are working through that, you know, and hopefully there'll be an opportunity to talk some more about that as we move forward and certainly at the year-end results. But at this stage I think you can just take assurance that we are continuing to focus on building our brands.

Jean Roche, Schroders:

Good morning. Just wanted to know on this massive services side, have you made any changes to your minimum payment at all over the period? And how does this compare, just remind us, of last year's, if so?

Craig Lovelace:

So, the straight answer is, no Jean, we've made no changes at all. The book is at it was. The impact changes seen 12 months ago, the book it as it was in October, so no changes.

Jean Roche, Schroders:

So, it's still 4 percent, is that right?

Craig Lovelace:

As a minimum payment broadly, yes. But that is a small cohort of our customers pay the minimum payment. So, there's a broad range but the 4 percent has remained unchanged. We've not done anything to that at all.

Jean Roche:

Okay, and why are there non-interest lines marginally ahead because they had been slowing down hadn't they?

Craig Lovelace:

They make up a very small percentage overall. So, from that perspective is just generally normal performance of the book. Interest makes up the vast majority of the financial services revenue line north of 90 percent.

Jean Roche:

Okay. And remind me what your APR is again?

Craig Lovelace:

As a headline APR, it's broadly 58 percent, but there are wide mixes there and we've continued to run successfully trials certainly on Simply Be and Jacamo at 24.9 percent as well.

Simon Bowler, Numis:

Ah, morning team. Couple of question if it's okay? First one just on the gross margin, I guess sort of a solid out turn during this period, but I think I'm right in saying it comes against kind of a particularly weak comparative in the half past year and that four months, is the idea of gross margins flight, is that your view of the underlying run rate as we look beyond this kind of current trading period?

Craig Lovelace:

On gross margin, it is a message of stability. The real focus, as Steve says, has been on promotions and we've been very targeted on that. That discipline, that focus on data analytics is one we expect to carry through into next year. I'm not going to necessarily make any calls on next year given the macro uncertainties, but one thing I will say is from a hedging perspective we are hedged for FY20 so from an FX perspective, which has in the past been a big impact on us, we are hedged where I want to be for the full elements of next year. I think it's too early to say opportunities exist, but stability in this market on margin, I'm comfortable with.

Simon Bowler, Numis:

Okay, that all makes sense. On marketing, the low end of your cost guidance is kind of full year cost down 4 percent say, it looks like second half marketing costs could have fallen somewhere approaching double digit, particularly if we exclude the one-and-a-half million incremental kind of VAT cost. Is that or thereabouts the correct read on that, or has there been greater flex in some of the operating cost lines?

Craig Lovelace:

Marketing is the primary driver but that is a reasonable read on things.

Simon Bowler, Numis:

Fine, and then again without meaning to kind of get too far ahead of myself, when we think about next year you've obviously got the headwinds in marketing, just the mechanical VAT flex, would you still be hoping for marketing to fall in absolute terms, like can you offset that headwinds with some of these underlying savings and efficiencies you're going for? Or is that kind of steps too far?

Craig Lovelace:

For us the focus is on the return on the spend and so at this stage if we got a materially better return on the existing rebate spend, that would be a good outcome. I think in the realm, given £160 million budget it will be a mix of both some absolute savings and greater efficiency. But at this stage, that's somewhat early to tell. But I do think that the group is driving toward a more efficient way of marketing.

Simon Bowler, Numis:

Okay, sure. Thank you.

Kate Calvert, Investec:

Morning, Kate here. Just in terms of JD Williams, you make the comment that you're re-evaluating its proposition, what is causing you to re-evaluate the proposition? Is this the underperformance of the old Fifty Plus cohort or is there something more fundamental there? And my second question is to do with the performances Simply Be Jacamo because there is a bit of a divergence between the online and offline. Can that version be explained by a realignment of your marketing spends?

Steve Johnson:

Okay. So, I mean, I guess covering the last question first of all, I'll cover that one, the performance of the business is absolutely related to the focus that we've been putting on in relation to getting our pounds away wisely. And I guess, therefore, you could look at it on the basis that we are building models that effectively are going to give us online growth. But we are going to be sort of balancing where we spend our money to achieve that online growth, which brings me to the JD Williams question that you asked. I mean, you know, there is absolutely no doubt the headwinds that we have historically talked about, and that you are implying through the sort of Fifty Plus migration, has given us pause for thought. I think, again, I'll come back to the areas of focus that I said we would look at in October; one of the key areas was a look at our brands and how we effectively market our brands and through specifically the eyes of JD Williams given we were wrestling with that headwind, which you're aware of. And on that basis, you know, that's where we are choosing to spend our time first. But I wouldn't read into that, that there is an underlying problem in the way that you have asked the question because ultimately, I come back to the online growth. And the business on the online channel is growing. We just need to make sure that we are doing what we can to be as inclusive to that entire customer base in the way that we execute our propositions.

Craig Lovelace:

Okay, the one thing I'd add to what Steve says, there's been a lot of questions on marketing today and a lot of them have actually focused on paper efficiency and dialing back paper. One thing we've increasingly been seeing over the last four to six months, when you're paying for pay-per-click on digital marketing, we have seen more and more competition in terms of pricing increases on pay-per-click and we are generally seeing more people moving into that space being prepared to pay more for key words and you are then getting back into that efficiency debate. Are you getting bang for buck? Just spending money on search terms when many others are, with cost inflation and that going very significantly upward, sometimes it does not make just sense just to pile your money into a digital channel just because it's digital. So, I think we've been more disciplined on that by necessity and by focus and that is their structural point that we've really seen over this peak period. So, to a degree, this is from memory, but broadly sits at 65 to 75 percent and increasing.

Kate Calvert, Investec:

Okay, thanks so much.

Clive Black, Shore Capital:

Thank you. Morning, guys. Couple of points. Firstly, with respect to Financial Services, can you just talk about the drivers of what was quite strong growth, but also how representative the

last quarter is, so we don't get in a state, carried away going forward? Within that respect, maybe just characterise the quality of the book at the moment? And secondly, you make reference in your statement to senior management regime. Would you just give some colour as to what we should be anticipating at the preliminary results around further disclosure on that front please?

Craig Lovelace:

Yeah, so the book has had another period of robust growth. It's less than it has been and clearly, we're now sort of some 18 months past some of those changes made on min pay, but the book performs well from a perspective of having continued to de-risk the back end of the book. So those customers who are regularly in default certainly with our first nine lends as well, we've been more focused on clearing out the back end but also new credit recruits. We've continued to use data, we've continued to use analytical techniques to refine the risk profile of people coming onto the book. So, from that perspective, in terms of arrears default rates, provisioning rates, the book continues to perform as it has done for the last two to three years in terms of a consistent improvement in quality, and a diminution in risk. So, that's been a consistent message, which I'm comfortable with, given the size of this book and the number of people on accounts. And this is, to Jean's previous point, this is a "cleaned book", quote unquote, because we haven't made any policy changes, it's business as usual. We've seen some early encouraging uptake from some of our lower rate trials. But it continues to move in the right direction. In terms of the rate of growth, I think again there's still some impacts being felt from some of the changes made over a year ago. It's an encouraging perspective, but over a longer period of time you would, as has historically been the case, the book normalises more to a rate of growth akin to products. So, it's moving, continuing to be in the right direction, slow and steady.

I think on your second question on what we've called SM & CR. This is really an early, very early stage flag from us to highlight some regulating change in the background. I will talk a lot more about it when we come to market in May. But the reality is for many businesses, the change in this regime from the FCA will require them to more carefully think about how they run the business, how they run a regulated business. We are in our early stages of diligence, but if I look at some comparable businesses, they've gone down the route of perhaps separating out legal entity structures, adding in more governance structures in accord with a regime that for us will be applicable in December. We are one of 25 enhanced firms by way of our revenues. So, we have work to do over this year. It is still early stage. What do I think the ramifications will be? It may be enhanced reporting, it may be enhanced governance. We've got work to do and I'll update at the Prelims But I just felt it was worthwhile to make people aware about the general FCA implementation of the regime change over this year.

Steve Johnson:

Thank you for the questions and thank you for taking the time to dial in. From my perspective the business is performing as expected and we've traded where we wanted to through the period. Pleased again with the ability to hold margin performance and guidance into a full year. And with that, I thank you for your time. Thank you.

Craig Lovelace:

Thanks everyone.