Brunello Cucinelli Group

"2013 Nine Months Results Call"

November 12, 2013

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OPERATOR: Good afternoon. This is the Chorus Call operator speaking. Welcome to the Nine Months Results of the Brunello Cucinelli Group. Following the first introductions, there will be a chance to ask questions. Speakers will be Mr. Brunello Cucinelli, CEO and Managing Director, Moreno Ciarapica, CFO, and Pietro Arnaboldi, Investor Relations Manager.

I would now like to give the floor to the President and CEO, Mr. Brunello Cucinelli.

BRUNELLO CUCINELLI: Good evening ladies and gentlemen. And welcome my esteemed investors and analysts. In the very first part of the presentation, I'd like to provide you with the results of the first nine months, just the summary, and then following on from that, I'd like to give you an outline of the full year 2013 because it's drawing to a close. Then Moreno Ciarapica, our CFO will provide you with more specific data. Then I will like to take the floor back, in order to give you an idea about visibility on 2014/2015, the new Men's wear collections and so on and so forth.

So what we can say is that we have enjoyed nine very interesting months. It is November the 12th today, so we could even say that the year is nearly closed. So in the first nine months of the year, the net revenues amounted to €251.7 million with a 14.3% increase at current exchange rates, then EBITDA €45.8 million, plus 15%, i.e., then as to markets, of course, overseas sales were the most important. The US markets, I will go back to that, it's a top market for us, grew by 26.4%. Then Europe also grew pretty well, 20.5%. And China also grew pretty well, a very tiny market for us, 16.7% and the rest of the world grew alike, 9.3%. Our very esteemed Italy decreased by 2.6%, so a slight drop, but we will go back to this later on, because my impression is that the new start, the new recovery has definitely started.

So we have then, over the first nine months, we have invested a lot, €34 million altogether, we have €8.5 million amortization and depreciation, we have a net income of €23.5 million with an increase by 10.2% and to end, we have a net debt, net financial position amounting to €23.6 million.

So what I would like to do now is to read out to you the two lines of the press release that I wrote myself, that are basically the following. We are very pleased with the way our company has performed in the first nine months of the year. Economic results have been particularly interesting, and therefore, we can envisage a very, positive 2013.

As for the orders backlog for Spring/Summer 2014, it went really, really well. We have the impression that step-by-step, we are somehow reaping the fruits of the major investments we made in an image of a company operating in the world luxury market, the so called "absolute" segment, whilst respecting craftsmanship, quality and hopefully creativity too by manufacturing its products entirely in Italy, products that are really typical of our cultural heritage. So this was my comments to the results.

So as I was saying before, we have reached mid-November, so we can definitely say that the year is drawing to a close. So 2013 full year, a very special year then, we do not want to use adjectives that are too much over the top because in a time like this, it is not really fair and nice to highlight and emphasize very special results. But for us, it has been a very interesting year, very much so, not just in terms of data, but also because in terms of taste, products, and the Italian image represented by our products.

So revenues well, then EBITDA also very well, and as you can imagine, it will a double-digit EBITDA, but you see six months results for us and the yearly results are very, very important and they matter more than quarterly results because maybe, if you just shift a bit the delivery timing with the wholesale, figures might change by some tiny points.

We have enjoyed the special year deliveries, why, because we managed to be very, very exact and precise also with multibrands by bringing our deliveries ahead. As to sell out 12th of November to-date, in multibrand stores, it's nearly the end there, the end of the year. And in America, you know, after the Thanksgiving Day, they do sales there. So we can say that sell-out why it has been an excellent season like-for-like 8.2 you know, that we…the sale for like-for-like ranges between 6%, 7.5%, this is what we deem a fair like-for-like.

I apologize; I have a rough result, so investments CAPEX very, very important, at the end of the year we will have invested between €40 and €41 million, so very important, amortization and depreciation around €14 million. And our net financial position should be around minus €16 million. So these are our estimates from here to the end of the year.

As to our stores network, we have our 700 multibrand accounts, representing 1,000 doors (Ph) more or less, and you know how much value we attach to the multibrand channel. As of today, we have 97 stores, there is still one left to open, Copenhagen at the beginning of December, 58 of which of these stores are DOS stores and 39 of which as of the end of the year, 40 of them…there will be 40 franchises, so 58 US and 40 franchises at year end. You know, that we tend to open franchise stores in locations like Copenhagen for example or Doha or Bucharest, these are the locations whereas we opt for the DOS stores in Europe and America, in main first tier cities.

Then as to the later stores that were opened, very, very special for us. Especially the last one, we have been really searching for the right location in Munich and by the way, it is performing really well. We just opened the Dallas store in September and as to mention important franchisees, we opened Ekaterinburg, then Copenhagen is due in a few days. So at the end of the year, we can say that the great deals and operations in 2013 have been the buying back of the two London stores, the buying back the three stores in Hong Kong and the opening of Munich in Germany that I mentioned before.

So as for our revenues, at the end of 2013, will be made up 55% from our multibrand and 45% stemming from monobrand stores, Once again, that highlight the value of multibrands because I really believe that it is the guardian of the brand, that is those who really tell you how the brand is doing, the brand is fresh, if the brand is old, and also they do talk to tell you about your corporate organizations. So we attach a lot of importance to it. Of course, by multibrand we mean the top department stores in America or Harrods in London, Le Bon Marché in Paris, Breuninger in Germany, all the top operators in the luxury field.

So what about our markets at the end of the year, maybe I can make a tiny error by some sense. I think US will account for 34%, Europe around 33%, Italy around 20%, China some 5%, and rest of the world 8% for the markets breakdown. So as you can see America weighs a lot for us and Europe weighs a lot to, and this does not mean the other markets do not weigh or do not matter. But going back to the value of the product, you see this kind of products that we sell it must perform in an excellent way in Europe and America, because European, Italian, American clients and customers they are all on the same wave length, so their judgments really is important and fundamental for us.

As to Italy, I was saying before, that in the first nine months of the year, we have reached minus 2.6% figure, and we think that the year…to the end we will be around 2% more or less the same result flat. But I think it is a great result and you know, why because orders for Spring/Summer that were placed between the end of August and September, and the beginning of October to. You actually see some signs of recovery in Italy, and this recovery is more perceptible in larger cities, and in tourist destinations it is slightly less stellar in provinces, but this is you know, the way it is.

And the last thing about 2013; I would say that at the end of the year, we will have more or less 1,040 employees. So this is a pretty important figure. So I would like to close by saying that 2013 is going very well. We are particularly pleased, we are especially happy with the IPO, we are very, very happy with you investors, analysts, who have given us a lot of esteem, never requesting anything different from what we are doing, unanimously, sharing our way of doing things, and we thank you for that.

And I will give the floor to Mr. Moreno Ciarapica, who will go a bit more into detail. And then maybe, I would like to give you an overview about next year and then Q&A. So I would like to conclude by saying that, next week I will be flying to New York to meet you, then at the beginning of December, Moreno Ciarapica will be going to London because you know, that as of January the 1st all these co-figures will start going into office. I will have my co-CEO and Moreno his co-CFO and like everybody to have their co, so we can possibly envisage the future for this company in five years. So Moreno the floor is yours. Thank you.

MORENO CIARAPICA: Thank you and good evening, ladies and gentlemen. So maybe we can start analyzing revenues, Slide #4 in the presentation, I would like to remind you that we have been affected by seasonality typical of the sector and these elements have affected quarterly results, both in terms of revenues, margins, balance sheet and income statement. I would like to also remind you of the delivery timing of the Fall/Winter collection, they have impacted the three months sales results favoring the second quarter results against the June/September ones.

And then now in terms of geographies, Brunello has tackled Italy till-date. But I would like to go a bit more into detail. So these net revenues total €251.7 million, with a 14.3% growth at current exchange rate, and at constant exchange rate this growth amounted to 15.9%, this has a negative impact…currency negative impact, amounting to some €3.6 million, which is…and it is mainly linked to the yen performance, and it was particularly evident in the third quarter. Results achieved were driven by the significant growth of overseas markets as a whole and on average 20.5% there.

So we talked about Italy, very slight decrease, that it's…to us is a great figure for a future new start, but as a matter of fact it confirms the improvement against the trend reporting the first nine months of 2012, thereby confirming the strong appeal of our brands to international clients and customers of absolute luxury, that drive sales in the main cities.

So as I was saying before, when I talked about exchange rates before, well it is obvious that the impact of Forex on us has just a nominal effect in terms of the exposure of our revenues and the operating costs, that are borne in countries where different currencies than the euro is in circulation because our production is 100% Italian.

And I want to say that, in terms of margins, our hedging policy for the exchange rate risk is such that we have no impact on margins. This is a significant factor; we have always repeated that in a time when currencies are subject to very significant fluctuation, it is important to remind you of this fact.

North America and Europe, Brunello has already talked about it in great…at great length, I can say that net of monobrand stores, North America there were 16 boutiques with some new openings, and together with a prestigious presence of our brand is a most important top luxury department stores just to name a few, Neiman Marcus, Bergdorf Goodman, Saks and Harry Rosen in Canada. The consequence is an exclusive precedence and it's in line with the profile of the interest of very high-end consumer.

As to Europe, the network of direct monobrand stores has reached 19 units, including the significant important opening of Munich. As we were saying, that we had been looking for it for a long time in a market like the German speaking market that is usually very important for our company with Switzerland, Austria and Holland with sales exceeding 10%. So in such an important area the Munich store definitely represents a significant result also in terms of image for the company.

As far as Europe is concerned another important figure is the one concerning the Russian market and Eastern European countries. Here to growths are pretty interesting and revenues coming from these markets reached nearly 10% of total revenues.

Then our presence in Greater China 4% of sales is still very selective and controlled, we are investing in a convinced way there, well aware of the potential of this market of the medium-term, and of course, well aware of the increasing of the growing interest of the Chinese consumer even when they travel abroad for tourism. So we have recently received a study on touristic flows, whereby Chinese shopping aboard actually account for 25% of total international tourist shopping aboard. And Italy and these pie charts represent 16%...accounts for 16% of purchases by international tourists worldwide. So it's a very interesting figure for us.

As to the rest of the world, revenues were driven by Korea and Japan, the two main market of this macro area; in particular Japan representing 5% of total sales is a very, very interesting market for us. And in 2014, as we said in the prospectus, a new operation…renegotiation operation will occur and it's particularly important because of the level of sophistication of this market. This said; I would now like to move onto the income statement analysis to Slide 11 to be precise.

And I would like to analyze the main items, the adjusted items of the income statement thereby excluding the first nine months 2012, the one-off charges, the non-recurring charges €6.2 million borne last year for IPO. So we will be making a comparison here, and within this comparison, performance confirms the soundness and sustainability of results, we would like to remind you of the impact of multiple variables on quarterly results, thereby, it is necessary and just like to analyze results for the whole year. As to the results of the first nine months, they highlight a significant increase as it had been the case the previous quarters. So a significant increase by 2030 basis points of the first margin, because due to higher margins in the retail channel, thanks to the growth of this retail channels that moved from 22.8% in the first nine months 2012 to 31.5% in the first nine months 2013.

Then, we had…we booked a 220 basis points increase of SG&A, and made up mainly of items they have to do with the business developments in channel mix. Then, we have higher amortization and depreciation as Brunello mentioned from €4.7 million to €8.3 million in the first nine months 2013 against the previous nine months period.

As a whole, EBITDA margin increases by 20 basis points from 17.9% to 18.1%. As far as the expected full year 2013 is concerned, we confirm that this performance will continue. So the first margin increase will be proportionate to the increase of SG&A. And as far as the detail of the changes that results in an EBITDA increase from €39.8 million to €45.8 million.

At Page 12, you see all the items, the costs they have to do with the business developments and channel mix, and then you can move on to Page 13 in the slide, where you can see that the SG&A increase was driven by the increase of costs for the development of the sales network, because the new…both for the management of new stores and the setup of structures in China and UK that was needed to manage the monobrands wholesale network and the direct stores network.

Personnel costs basically increased due to the increase of stuff in direct US network, and the number of employee…store employees and office staff went up from 383 to 585 units, mainly due to staff in the stores. In terms of value, the weight of personnel cost, an increase incidence from 14.1% to 14.4%, rents went up from 4% to 5.5%, than we have A&P flat from 5.4% to 5.6%, transports and duties, due to a higher incidence in markets where we operate directly these duties increased by 3.7% to 4.2% in terms of balance sheet.

Now, moving on to Slide 15 of the presentation; we can see all the changes in terms of net working capital. There is a very healthy and positive management of net working capital, enabling not just to absorb the natural increase of inventory, that moves up from €65 million to €77 million, as that is basically to do with the growth at retail channel, I would like to remind you that direct boutiques as of 30th September 2012 we had 32 then, and today we have 61 boutiques.

But…and this management of NWC, it can improve the weight of an NWC on the rolling revenues of the last 12 months to 27% to 24%. As for the expectation for the end of the year of NWC, they…we believe that you will be lower than the 24.5% of the first nine months of 2013.

And to conclude, we have the net financial position going from €14.4 million as of 30 September, 2012 to €23 million in 30 September, 2013 basically driven by major investment €34 million…in this €9 million (Ph)…versus €16.7 million in nine months ‘12. But we can see that versus 30 June, 2013, this net financial position has decreased significantly €30 million as of 30 of June, and this development will continue also in the last quarter. Brunello already said, our expectations are to achieve €16 million net financial position at the end of the year €9 million to €16 million.

I think that my presentation is finished. So thank you for your attention, I give the floor back to Brunello for an overview on the future, your conclusion and then your questions. Thank you.

BRUNELLO CUCINELLI: So, let’s tell the truth, 2012 very, very good and 2013 also very good. We are very, very pleased and satisfied, and we are glad also for the allure that is experienced by the brands. The perception is that we work and behave very well that we have and we have…we enjoyed a very strong exclusivity (Ph) rates in our products, our products are expensive and no one ever asks us, whether we manufacture outside of Italy, which means they are…we have a very strong identification of our brands as 100% made it Italy.

Next month there will be an important meeting on Luxury in Italy, and the title is the “Value of Territory.” In this case, I think the company enjoys a lot's of value in this territory. And I think that we can say that, if we had a company in a very classic ordinary industrial district, in a city maybe the allure enjoyed by the brand would have been lower. So maybe in the last five minutes, I like to devote to the main outlines and highlights of 2014 and 2015, what we project for there…for them.

So we are an apparel company, a ready-to-wear company, it is very important as of today 67% women's wear, and the rest men's wear, maybe next year, there will be more of a balancing off between men's wear and women's wear, we have a ready-to-wear company, the incidence of accessories is about 15%-16%, they might go up to 17% one day, but please keep considering us a ready-to-wear company specializing in daywear…luxury daywear, because we also do cocktail party cloths, but you know, how important it is to be well dressed during the day in a chick way. So we believe and trust high craftsmanship and quality, it's not up to us to judge or to pass the judgments on creativity. But, we need to be budgeting for quality and craftsmanship.

In next March, we will be moving to the new facilities. We have doubled the facilities, you know, the plan dates back to seven years ago, but since here in Ivrea (Ph) we are run by the office for the fine arts, it takes quite a long time from project to actually implementation. So it's usually 5, 6 years in March we will be moving there, we will have 26,000 square meters owned and 10,000 square meters rented. So in order to abide by the 30% rule that we have inside the company, I know that it's not always easy, it's not easy to be reversible in this case, 10,000 square meters rented and then 26,000 owned. So having rented them means that one day if needed, you can dispose of them. So the objective is always the same, over the next two years we would like to have 50% monobrands and 50% multibrands evenly spread by opening per annum roughly 11, 12, 13 stores and maybe this includes maybe doubling the size of a store, expanding on to two floors, or doubling the size of it, so like it's going on in London. So out of these 12 stores per annum, 8 will be DOS, 4 franchised stores with the same…pursuing the same strategy that we have been pursuing so far, that is opting for franchised stores in markets where we do not really feel confident enough.

As for the market in the next few years, we think that the balance should be the following, between 33% to 34% US, with Canada included obviously, 32% Europe, excluding Italy, Italy roughly at 18.5%, China around 6%, and then ROW 9%. Well, basically not many changes are there compared to today, maybe the breakdown, women's wear and menswear, it could be 62…61%, women's wear, 37, 38% menswear, thanks to the new operation that we are currently making and the new segment that we'd like to explore the menswear suits.

So in these four years…so that includes 2012 when we went public, 2013 and then '14 and '15, so as a whole €120 million altogether invested at the end of this year together with last year we will have had €66 million, €67 million, so 2012 and 2013 and we imagine that for the next two years €50 million invested over the two years.

We have decided to make significant investments, major investments, but to tell you the truth, we believe first of all in the Italian product, high quality product and this is the reason why we have decided to perform this great purchase as of January the 1st of Da Vinci (Ph), this great Carrara based industry that dates back to 100 years back with a very high quality heritage of suits, men's suits and outerwear. Yes, we will be investing some million euros there, but we will have €6 million there, but we will have another, yet another token to show to the world, a token of our image, in this case we have acquired the knowhow in one of the best companies in the world. So now we can turn up at our client's doorsteps with an even more important allure we believe.

Well, I have to say that some thing is happening that we had not expected to be so positive in the United States. The last department stores in the US are allotting us very special selling spaces where we can actually set up our hot shop, they are placing us on the floor next to the best brands in the world, Hermes, Chanel, and Dior, well, basically because we sell ready-to-wear and this also means to…investments for us because as you know, we are to set up these selling space, but when they decide to grant you such an important significant selling space in a very top excellent floor, it means that your brand has reached a very healthy level and you can envisage a very special future ahead. So this investment, the purchase of Da Vinci, it really makes us even nobler.

Well, maybe three minutes on the products. We can say that we have reached the level, the EBITDA level that we mentioned very often in our meetings. We would like to fluctuate between 18%, 18.5%, and 19% of revenues. This is a healthy EBITDA attached to a ready-to-wear company. You see, I seriously believe that we must be very careful on this because since we manufacture very expensive items, those who buy these items have all the reason to collect information about your profitability. And honestly speaking, we would like our profitability to be just fair and if we make a fair profit, we will probably continue to enjoy the best clients that we have had so far, the best customers.

You see everybody talks about conquering the favor of the new rich, but we ourselves, we would like to retain the old traditional rich people of the old, contemporary old world, so that they can talk to their children round to buying very high quality products as it is actually the case. And then the new rich will follow suit. But you know, the old rich are much more demanding, they are much more attentive and selective, very demanding in terms of quality especially, and we do not want to lose that. Of course, you know, that I’ve always been scared by that and…but I was saying today to Moreno and the others in the Board, you see, we have company that in terms of net debt always fluctuates between 3%, 4%, 5% of revenues in a time of great development, you see these are quite comforting results.

Now going back to the product, it is a very special time for us, a great momentum. And on the one hand, we need to be…to have the courage to be strongly exclusive, we must have the courage not to open too many stores and to be a brand if you allow me even more exclusive than what it is, I would even there use this term and please do not be set aback by it. Maybe we would like to be…maybe less known than we are today, so exclusivity combined with very topnotch quality, and believe me, an extremely high level of craftsmanship. Over the last two years, I’ve seen so many special things, it’s never happens, unprecedented. I’ve never met anyone in the last two years who has actually said to me, I am relocating my production abroad. No, on the contrary, I have met people saying I am bringing back part of my production to Italy and I like this very much because this basically highlights our production capacity or the million companies that are maybe not very well known, but they are really are a main source.

Exclusivity, quality and craftsmanship you know, we have invested very much in visual merchandising. I have always argued that visual merchandising plays a significant role, very important for women’s wear even more so for menswear, so much so that in early January, we will be presenting ourselves to…if you are free please come and see us in Florence (Ph), where we will have this [indiscernible] will be twice as much as it was last year in terms of size, so we will be displaying half the sporty chic clothes that we usually have and then the other half devoted to formal wear, but maybe revisited in a fresher way and in a younger way with a very high quality of fabrics and with a more contemporary fit.

So the other day, I was told by an Italian friend that he was saying, have you realized that in the Italian luxury, you are the only one that is left, because all the rest are French, why was that, because we had a meeting on luxury wear, where the topic was, what is…what will be the value of Italy for luxury. I argued that it will have a very high value. All the statistics say that 60% of products in the absolute luxury industry…well, all these products are manufactured in Italy, even for our well esteemed French operators and players. So of course, we have a very special value as Italians. We have to manufacture special things made in Italy. We must be willing to listen to our counterparties.

So as I was saying at the meeting the other day, we must thank you investors and analysts because really, seriously we have tried to implement all that you have suggested. Honestly, you never required things that were out of the blue, but you see how this idea…you see, you have been very important analysts and investors. You should know that in our culture, we have the idea of listening. Of course, you all know that when you are successful, you really struggle to listen, but we try and do the opposite.

So I would conclude by saying, a very special year really, but after taking a look at the growth projection of the luxury market in the next two years, I can say that we must expect something interesting, but not just for our company. And I am extremely pleased with this. The brand is surrounded by a very special allure, this topic of gracious fair growth and healthy profit, we talked about it. We are very, very positive in our conviction.

So now, before any questions that you might have as an Italian, I'd like to wish all the best to Romero Finney (Ph) from Montclair, who is approaching the IPO and I'd like…and he really represents Italy and our way of working. So best wishes Remo, thank you and thank you for your esteem. So let's now open the floor for discussion. And as I was saying before, with many of you, we have a meeting scheduled next week when I will be in New York, many others I will meet in New York, and then Moreno will be meeting many of you in London in early December. Thank you very much.