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PRESENTATION

Operator
Good day, and welcome to the Estee Lauder Companies second quarter fiscal 2025 earnings release and conference call. (Operator Instructions) Please note, this event is being recorded. I would now like to turn the conference over to Ms. Rainey Mancini. Please go ahead.

Rainey Mancini ***Estee Lauder Companies Inc - Senior Vice President - Investor Relations***
Hello. On today's webcast are Stéphane de La Faverie, President and Chief Executive Officer, and Akhil Shrivastava, Executive Vice President and Chief Financial Officer. Since many of our remarks today contain forward-looking statements, let me refer you to our press release and our reports filed with the SEC, where you'll find factors that could cause actual results to differ materially from these forward-looking statements.

To facilitate the discussion of our underlying business, the commentary on our financial results and expectations is before restructuring and other charges and adjustments disclosed in our press release. Unless otherwise stated, all organic net sales growth also excludes the non-comparable impacts of acquisitions, divestitures, brand closures, and the impact of foreign currency translation.

You can find reconciliations between GAAP and non-GAAP measures in our press release and on the investors section of our website. As a reminder, references to online sales include sales we make directly to our consumers through our brand.com sites and through third party platforms. It also includes estimated sales of our products through our retailers' websites. Throughout our discussion, our profit recovery and growth plan will be referred to as our PRGP. During the Q&A session, we ask that you please limit yourself to one question so we can respond to all of you within the time scheduled for this webcast.

And now I'll turn the webcast over to Stéphane.

Stéphane de La Faverie ***Estee Lauder Companies Inc - President and Chief Executive Officer***
Thank you, Rainey, and hello to everyone. Akhil and I are pleased to be with you today for our first earnings score as CFO and CEO of the Estee Lauder Companies. We are incredibly honored to lead our iconic company defined by our core values and portfolio of beloved brands. Having met with many employees, retailers, business partners, investors, and other stakeholders since being named CEO, three months ago, I am more convinced than ever that our fundamentals are strong.

We have a strong foundation to leverage, given our brand equities, high quality products and exceptional talent. Our focus is clear restore sustainable sales growth and achieve a solid double digit adjusted operating margin over the next few years as we aim to become the best consumer centric prestige beauty company.

Let me begin by reflecting on the drivers of our challenge performance over the last few years. Before turning to how we plan to realize our ambition for much improved results. To consumer sentiment in China greatly pressured the prestige beauty industry and our business.

Given our strategically strong share in prestige beauty with the Chinese consumer, we were disproportionally impacted. At the same time, the increasing complexity of our organization, coupled with a narrow focus on too few markets and channels to drive growth prevented us from tapping into the prevailing strength of prestige beauty around the world. This was especially true in North America.

Simply said, we lost our agility. We did not capitalize on the higher growth opportunities quickly enough in channels, markets, media, and prestige price tiers, nor fuel new consumer acquisitions aggressively enough. We also did not deliver sufficient levels of on trend innovation in our time to market often put us behind trend.

This happened as prestige beauty become nimbler, driven by both incumbents and new entrants, as we learn with our own indie brand the ordinary, along with faster moving consumers magnifying our issues. Compounding matters, lower sales in higher margin areas of our business coincided with our overall expense base becoming too large as we invested in capabilities ahead of growth that didn't materialize.

Our bold new strategic vision of beauty reimagined is designed to address these factors to restore sustainable sales growth and deliver a solid double digit adjusted operating margin over the next few years. We are reimagining our operating model to be leaner, faster, and more agile through the biggest transformation in our history to best serve consumers globally.

Beauty Reimagin has five action plan priorities to achieve our ambition. First, accelerate best in class consumer coverage. We are going to put the consumer at the heart of our business. To do so, we plan to rapidly expand our portfolio presence in consumer preferred high growth channels, markets, media, and price tiers to fully participate in the growth opportunities of price (inaudible) .

We have numerous areas in which to capitalize geographically in the US, the UK, and emerging markets, and by channel from travel retail in Western markets to online platforms, specialty multi globally and pharmacies in Europe globally and pharmacies in Europe. By doing so, we expect to better diversify our growth drivers.

Second, create transformative innovation. We aim to deliver faster market on trend innovation with an eye towards in-demand subcategories, benefits, and occasions. For instance, there are several dynamic subcategories in skincare like body, of makeup, like multi-benefit lip products, and of fragrance like lifestyle for home, for our brands to either enter or expand.

We will innovate across price tiers, from entry prices to luxury, making sure to bring products to market at attractive price points for new consumer acquisition. As we look to step change our innovation, we are committed to tripling the percentage of our innovation that is launched in less than a year. But boost consumer facing investments to accelerate new consumer acquisition.

First and foremost, we plan to do this by increasing visible advertising spending, optimizing marketing programs, and eliminating current ANP spending that is unproductive. Moreover, this also includes greater investment in selling to support our freestanding store acceleration for our luxury and artisanal fragrance brands to drive growth.

Fourth, fuel sustainable growth through both efficiencies with today's announcement of our now expanded PRGP. We've made significant progress to date in the PRGP, having delivered over 60% of our fiscal 2025 objective in the first half of the fiscal year.

This has primarily been driven by addressing elevated excess and obsolescence, realizing strategic pricing through fewer discounts, lowering professional service expenses and restructuring our workforce. However, greater expense reduction is necessary. We have experienced further volume deleverage since the plant's inception, driven by moderated industry growth projection and geopolitical uncertainty, as well as the company specific issues as described.

We must redesign our expense structure for an evolving mix of business to better align with prestige, beauty growth drivers and given the significant changes in the travel retail industry. We're embarking on our biggest operational transformation in our company's history, enabled by now an expanded PRGP. We are redesigning how much and where we spend, further rationalizing our non-consumer facing investments and significantly evolving our operating model to be more efficient.

The new areas we have identified and adopting a more competitive approach to procurement, improving supply chain network efficiencies, and outsourcing of select services, the latter of which we plan to do with proven global partners. We are advancing well in the design of the outsourcing program with our potential partners.

We are laser focused on right sizing expenses with the dual mandate to meaningfully reinvest in consumer facing initiatives to drive top line growth and achieve a solid double digit adjusted operating margin over the next few years.

And as we return to delivering sustainable sales growth, we will be positioned once again to realize operating leverage to further improve profitability. We plan to give more detail on our growth algorithm once we have more fully operationalized the action plan priorities of beauty reimagined.

Fifth, reimagine the way we work. We are removing complexity and simplifying our organization. In doing so, we will provide for greater focus on execution, excellence for the consumer. Moreover, we are unburdening our smaller brands so they can be more successful in a larger organization while driving greater benefits of scale for larger brands.

As we make these changes, we will empower faster decision making in part through a flatter and leaner organization. The foundation of our beauty reimagined strategic vision is a new framework where we are clear on our strengths so that we can more optimally allocate resources. Our strengths are where we will lead and excel brand desirability, consumer experience, innovation, quality, and hand to hand execution.

In support of our strengths and for certain other areas of our business, we are hardwiring AI through the organization. We are at an exciting moment in time for the company with AI as we've been working with the best in class technology partners. Their resources, technology and investments combined with our use cases and proprietary data are enabling us to deploy AI in a cost effective manner to drive efficiencies with high quality and differentiated outputs.

As one example, we are leveraging AI to forecast our demand and plan for our material and production needs, which has resulted in our weighted average forecast accuracy reaching new heights. This better synchronizes our demand and supply and delivers significant improvements in inventories. Added proof that the initiatives that we are deploying to restore stronger operating margins are sustainable.

We are ready to dramatically scale the integration of AI into our workflows from product development to marketing, supply chain, back office, and beyond to accelerate processes and improve decision making. What's most exciting, we expect AI to free up resources to unleash even greater creativity by our brand teams for the consumer.

As part of the expanded PRGP, we also plan to work with other external partners to outsource areas of our business that are not core to where we want to lead an excel. Since I became CEO, we've moved quickly to jumpstart Beauty Reimagine in my first 30 days.

First, we announced this morning, we established a new consumer centric executive team through a combination of elevated top talent internally and recruiting externally. The new flatter linear team structure and governance model are designed to significantly improve collaboration and speed of decision making with clearer accountability across brands, regions and functions in support of our action plan priorities.

Second, and as I said a few minutes ago, we strategically expanded PRGP, including its restructuring program with the full support of our Board of Directors. This was a decision we did not take lightly, and it will result in a reduction of several 1,000 additional positions.

Third, we dramatically simplify certain work streams across brands, regions, and functions to enable teams to focus more on external execution to drive sales growth. As we execute Beauty Reimagin, we are embracing a test and learned mentality. When we see an early wind, we will endeavor to move with speed to scale it. Conversely, we will seek to move quickly to exit what's not working.

We are putting a new organizational structure in place to empower colleagues to act as owners as we improve communication, accountability and collaboration to be more decisive and faster to action. Encouragingly, as demonstrated in the second quarter, we have some momentum on which to build across the five action plan priorities of Beauty Reimagined.

As we accelerate best in class consumer coverage, nine brands have now launched on the US Amazon premium beauty stores, including the successful launch of the Ordinary in January. Last March, Clinique was our first brand to launch on Amazon store font, at which time it also doubled down on its authentic dermatologist heritage with strong commercial execution across all channels.

Given Clinique's resounding success in the US, demonstrated by eight consecutive months of prestige beauty share gain through December, it launched in Canada Amazon premium beauty stores during the second quarter.

Across markets, in Asia Pacific, we continued to build our presence on TikTok Shop, Line and Shopee with more brands launching in some markets on these high-growth platforms. And we are thrilled that The Ordinary is debuting in Mainland China this month with its proven disruptive launch strategy.

We also realized excellent results as we extended the reach of our luxury and artisanal fragrance brand with our experiential in-store offerings, led by Le Labo and Editions de Parfums (inaudible) Malleas each delivered strong double-digit organic sales growth.

As we deliver our plans to create transformative innovation, Clinique, Estee Lauder and [La Mer] strategic launches for the nighttime usage occasion demonstrate the gains we can deliver where we have the right to play and win. In Mainland China, La Mer grew in retail, in contrast to the industry's decline in prestige skin care, driven by its new rejuvenated nice.

Clinique CX, the brand's new advanced post-procedure treatment franchise for China further epitomizes our aspirations. Clinique CX debuted in November at the Chinese Dermatologist Association with Medical Device 2 classification after less than 12 months development from concept to launch. We also announced the opening of a new BioTech Hub in Belgium in December and the collaboration with MIT in January to further accelerate the company's cutting-edge biotechnology innovations.

Finally, we saw the fruits of our labor when we boosted consumer-facing investment to reach new audiences, as seen by Jo Malone London's significant growth with men in the second quarter. Before I close, I want to speak briefly about our third quarter outlook. While we are not satisfied with our third quarter outlook, it primarily reflects weak retail sales trend in our Asia travel retail business, which deteriorated in the second quarter driven by Korea. While our retail sales trends in Hainan were still negative in the second quarter, they improved sequentially, fueled by our retail activations.

For the third quarter, we expect overall soft retail trends to persist in Asia travel retail, significantly pressuring our organic net sales despite the improvement we made with our in-trade inventory levels in the first half of fiscal 2025, which we intend to maintain across current levels.

In order to reignite our retail sales growth, we are strategically increasing consumer-facing investments around the world in the third quarter. We expect the benefits of the PRGP to both fund these investments and modestly offset the meaningful operating deleverage from the sales decline.

In closing, while we have much work to do, we are confident that Beauty Reimagined is the way to realize our ambition to restore sustainable sales growth and achieve a solid double-digit adjusted operating margin over the next few years.

To our employees, thank you for your passion and contribution at this pivotal moment in our company's history. I am grateful for all the ideas that you've shared with me over the past months, and I'm energized for what we can achieve together. This is our shared vision.

I will now turn the call over to Akhil.

Akhil Shrivastava ***Estee Lauder Companies Inc - Executive Vice President and Chief Financial Officer***
Thank you, Stéphane, and hello, everyone. It's an honor to be with you today in my new role as CFO of Estee Lauder Companies. I'm energized to partner with Stéphane as we boldly drive the execution of Beauty Reimagined, our transformative strategic vision.

While we've made progress with initiatives under our PRGP, we recognize there's still much to accomplish. As we collaborate with our global teams to simplify processes and execute with speed and agility, we are confident we can achieve a leaner cost structure through significantly expanding our PRGP. We believe this evolution positions us to invest more in consumer-centric activities that drive recruitment and fuel sustainable, profitable growth and cash generation for the long term.

I'll discuss this in more detail shortly. But first, let me recap our second quarter results, covering overall performance, organic net sales by region and product category, margin, cash flows, restructuring charges and other items.

Organic net sales declined 6%, at the high end of the outlook range we gave in October. Adjusted EPS was $0.62 in the quarter, exceeding our outlook. This reflects better than expected gross margin expansion given a higher than expected category mix in skincare. It also reflects disciplined expense management, while we continue to invest in consumer facing activities to support growth in key areas of the business.

Starting with our regions. In Asia Pacific, net sales decreased 11%, primarily driven by double digit declines in Mainland China, Korea and Hong Kong SAR, mainly due to subdued consumer sentiment. The decline in Korea also reflects our November 2024 exit of Dr. Jart from the travel retail channel as well as the impacts of recent political and social unrest. These declines were partially offset by double-digit organic net sales growth in Japan, where both domestic and traveling consumers continue to fuel growth across nearly all channels of distribution.

Organic net sales in EMEA fell 6%. This reflects continued retail softness in our Asia travel retail business, which resulted in lower replenishment orders. Organic net sales were flat in the Americas. This was mainly due to the 1% decline in North America where we still have relatively high exposure in slower growth channels. This was partially offset by double-digit online sales growth, which included early shipments for The Ordinary's launch in Amazon's US Premium Beauty store in January.

Moving on to product categories. Organic net sales decreased 12% in Skin Care and 8% in Hair Care. The challenges in Asia Pacific and our Asia travel retail business have the greatest effect on our Skin Care category. This more than offset the sales growth we saw in the Americas led by double-digit growth from The Ordinary.

In makeup, organic net sales decreased 1%. The collective decline from TOM FORD, M·A·C and Smashbox more than offset the high single-digit growth from Clinique's launched last March and Amazon's US Premium Beauty store. Fragrance organic net sales increased 2%. Le Labo continued to excel with strong double-digit sales growth across all geographic regions driven by [HEDO] products and innovation.

Now turning to our margins. For the quarter, our gross margin expanded 310 basis points compared to last year. This reflects net benefits from our PRGP that drove the reduction in excess and obsolescence, lower discounts, benefits from our strategic pricing actions and operational efficiencies.

Operating expenses increased 500 basis points as a percent of sales during the quarter. This reflects a 210 basis points increase in advertising, promotion and innovation expenses. This includes our investments to fuel performance during holiday and key shopping moments and drive consumer engagement for new product launches.

We also saw an increase of 130 basis points from higher selling expense. This reflects higher costs to support key activations including during holiday and our distribution expansion. And our sales deleverage offset the net benefits realized under the PRGP. I'll expand on this later.

Operating income decreased 20% to $462 million, and our operating margin contracted 200 basis points to 11.5% compared to 13.5% last year. Our effective tax rate for the quarter was 42.6%, compared to 37.7% last year. The increase is primarily due to the unfavorable impact of previously issued stock-based compensation and a change in a global mix of earnings.

Diluted EPS was $0.62, compared to $0.88 last year. As of December 31, we have recorded $403 million of charges under our PRGP restructuring program. These charges primarily relate to initiatives aimed at transforming various functions, brands and regions.

During the quarter, we recorded $861 million of impairment charges related to TOM FORD and Too Faced. This reflects challenges in Asia Pacific and our Asia travel retail business for TOM FORD and continued underperformance from Too Faced. The increase in the weighted average cost of capital also contributed to the impairment charges for both brands.

Moving now to our cash generation, CapEx investments and dividend payments. For the six months, we generated $387 million in net cash flows from operating activities, compared to $937 million last year. Lower net cash flows from operations this year as compared to last year is due to the decrease in earnings adjusted for noncash items and an unfavorable change in operating assets and liabilities. This includes the fact that last year, we made a very significant year-on-year reduction in our inventory.

We invested $273 million in capital expenditures compared to $527 million last year. The reduction in capital expenditures was primarily driven by the prior-year payments relating to the manufacturing facility in Japan. It also reflects the improvements we have made to optimize expenditures as we are determined to improve our free cash flow.

Turning to dividends. We returned $366 million in cash to stockholders. Looking ahead, to harness the full growth potential of our strategic vision as we transform how we operate and invest in our business, we must boldly pivot with a consumer-centric mindset, focused on cost discipline, optimizing our resources for growth and fueling consumer-facing investments to further ignite our brands.

Now I'm going to elaborate on our PRGP that is a critical enabler of this strategic vision. We have made significant progress in executing our plan thus far. While we remain on track to deliver the previously communicated $1.1 billion to $1.4 billion in net benefits, the current headwinds we are facing are now expected to partially offset these benefits.

To date, the net benefits we have realized thus far have been more than offset by our operating deleverage. Our profitability has been pressured by our sales volume declines: mix, ongoing inflation and a cost base that was scaled in anticipation of growth that did not materialize. We have also continued to invest in consumer-facing activities and distribution expansion to fuel sustainable growth.

To address these challenges and accelerate our return to sustainable sales growth and profitability, we have made the decision to further expand the PRGP, including its restructuring program. Anchored by the five key action plans Stéphane discussed, the expanded PRGP is essential to our operational transformation, fueling investments for growth, not ahead of it. We are focused on improving operational efficiencies, optimizing our cost structure to be leaner and enhancing leverage across the business, especially during periods of volatility and low sales growth.

This transformation enables us to reallocate resources, allowing us to better prioritize and increase consumer-facing investments. By doing so, we are better positioned to address changes in our mix of business whether driven by internal or external factors.

Related, we have made the difficult decision to expand our restructuring program. With all initiatives under the program, we now expect a net reduction of 5,800 to 7,000 positions globally, including approvals to date. Approvals for specific initiatives under this restructuring program in total are still expected to be completed by the end of fiscal 2026.

In the now expanded restructuring program, we expect to take total charges of $1.2 billion to $1.6 billion and generate annual gross savings of $800 million to $1 billion before taxes. A portion of these savings is expected to be reinvested in consumer-centric activities and additional investments to fuel growth.

The actions under the PRGP, including its restructuring program, are expected to be substantially executed in fiscal '25 and '26 and completed in fiscal '27. We expect nearly all of the full run rate benefits to be realized during fiscal '27.

Overall, we aim to accelerate our return to sustainable sales growth and deliver a solid double-digit adjusted operating margin over the next few years. We are moving with a sense of urgency to execute the action plans of Beauty Reimagined to start delivering annual sales and margin improvement quickly. As Stéphane said, we plan to share more details once the Beauty Reimagined action plans are operationalized.

Let me now discuss our outlook. We expect our business to continue to be challenged by subdued consumer sentiment in China and Korea, pressuring Asia travel retail. In light of this, along with evolving global geopolitical uncertainty, we anticipate continued volatility and low visibility in the near term. As a result, we are only providing an outlook for the third quarter.

We expect a strong double-digit sales decline in our global travel retail business in the second half of the fiscal year. This reflects shipments based on our expectation of persistent industry retail softness and incremental pressure from the change in selling policies at several Korean retailers. Additionally, recall that we resumed replenishment orders in the third quarter last year, making for a difficult comparison.

However, we are encouraged that, for the second quarter, our retail trends, while still negative, improved sequentially in both Mainland China and globally, excluding travel retail. We anticipate our retail sales trends, excluding travel retail, to significantly improve in the third quarter as we increase consumer-facing investments.

Given that context, let me walk you through our specific outlook for the third quarter. We expect organic net sales for our third quarter to decrease 10% to 8% compared to last year. As I previously mentioned, this is primarily driven by a strong double-digit decline in our global travel retail business. In the rest of the business, we expect the net sales decline to moderate. Currency translation is expected to negatively impact reported net sales by 2 percentage points.

For the third quarter, we anticipate moderate gross margin expansion, reflecting a tailwind from the in-period charge last year, which was triggered by the previous pull-down of production. We also expect continued benefits from the PRGP as an offset to our expected sales volume deleverage and continued consumer-facing investments.

We expect our third quarter effective tax rate to be approximately 36%, compared to 30.5% last year. The increase primarily reflects the estimated change in our geographical mix of earnings. We expect third quarter adjusted EPS of $0.20 to $0.30, primarily driven by the expected strong sales decline in global travel retail. Currency translation is expected to dilute EPS by $0.04.

In closing, we acknowledge that we have a lot of hard work ahead. But we are empowered by a Beauty Reimagined vision. With its mandate to pivot boldly with the consumer-centric mindset, speed and agility, we are confident and better positioned to accelerate our return to sustainable sales growth and long-term profitability.

On behalf of Stéphane and our new leadership team, I want to extend a heartfelt gratitude to our talented employees around the world. Together with you, we are driving the critical transformation to unlock the full potential of our beloved company.

That concludes our prepared remarks. I'll now turn it over to the operator to begin the Q&A session.

QUESTIONS AND ANSWERS

Operator
(Operator Instructions)

Bryan Spillane, Bank of America.

Bryan Spillane ***Bank of America - Analyst***
Thanks, operator. Good morning, everyone. Thanks for all of the detail today, very, very helpful. And I know there's a lot that you've got going on. But Stéphane, maybe just to step back for a sec, I guess as we were -- I was just reading through the press release this morning and listening to the prepared remarks, some of what I'm hearing or what it comes across is there's some prioritization happening, meaning by changing the organization structure internationally, it's going to create, I think, more focus in some of those regions that maybe needed them.

And in that light, can you talk a little bit about the portfolio? I know there's been some new stories about the potential to maybe sell some brands. But absent that, just how are you looking at the portfolio and prioritizing where the investments go, and maybe there are certain brands or categories that you'll run more for cash? Just trying to get a better understanding of maybe how you're looking at the portfolio itself and prioritizing.

Stéphane de La Faverie ***Estee Lauder Companies Inc - President and Chief Executive Officer***
Thank you, Bryan, no, thank you, very good question. I'm happy to discuss. First of all, your question is on the organization. Obviously, you saw as part of the press release we put out this morning, obviously, the change and the evolution of our organization. First and foremost, this organization was thought through to be leaner and faster. Obviously, we are -- if you look at the organization at three blocks, one about the regions, one about the brand and one the operation, we've really looked at every single of the element to be able to just like act faster and to deploy and execute the Beauty Reimagined strategy in a much faster way.

To your point, Bryan, the realignment of the regions across four clusters allow us to have a much more focus, one on the Americas, looking at it on the total region. One in Asia with the integration of travel retail as part of this region, which allows us to have like much further and greater alignment between the local market and travel retail on the activities that we are going to run.

Then you have also the entire alignment of the EMEA, UK and the newly created emerging market. We've said it for a long time, emerging market is a key focus of our acceleration going forward. So creating a new organization that allows us to focus on markets such as India, Middle East, Southeast Asia, and you name it, will allow us to really capture the fast-growing middle class in this market and to position our brand in every key market.

And obviously, China gets elevated and reporting directly to me, obviously, based on this strategic importance and, frankly, the continuous importance of the market and the long-term outlook of China that is very good.

When it comes to the portfolio of brands that you've discussed, obviously, we are -- what we are doing is that we are conducting on a regular basis a thorough analysis of where our brands needs to just like deploy and where their strengths is. We undertake always every year a full portfolio review of our brand, and we do it with the Board, and we do it also with every single of our brands.

We look at categories, we look at region, we look at HEDO product, we look at new innovation and where we want to accelerate them and make sure that we transform. One, we accelerate what works, and that's what I said in my prepared remarks. We want to pivot and to be much more agile. Stop what is not working in brand and in region. And accelerate innovation going forward as part of the second pillar of Beauty Reimagined, which is the creation of this transformative innovation plan that will allow us to accelerate.

In all of that, it will allow us to really deploy our brand with a lot more agility based on the brand organization, the regional organization and, at the same time, the full review that we are doing on every single of our brand on an ongoing basis. And frankly, the last one, I would say, we are committing to drive the maximum value for each of our brands and each of our regions around the world.

Operator
Lauren Lieberman, Barclays.

Lauren Lieberman ***Barclays - Analyst***
Great. Thanks. Good morning, everyone. I was curious, Stéphane, if you could talk a little bit about how you manage the pace of reinvestment. Because I noticed once or twice through the prepared remarks, you discussed one of the challenges in the past was investing ahead of the curve, investing for growth that didn't materialize. But at the same time, we need to keep reinvesting, right?

So I mean to my years, I feel like the difference between one in the other is just a matter of success rate in ROI, right? If the sales had materialized, those investments would not have been deemed unsuccessful. So I just need a little help in understanding that change in approach on spending ahead of sales growth versus spending to drive sales growth. Thanks.

Stéphane de La Faverie ***Estee Lauder Companies Inc - President and Chief Executive Officer***
Thank you, Lauren, and great to hear from you. So on the -- my prepared remarks, what I said what we did in the past is, obviously, we've invested ahead of growth in our capabilities. We did a lot of investment, as you may recall, in term of manufacturing network, in terms of system operating model, innovation centers around the world, for us to be able to just make sure we meet the consumer and being able to just like deliver with a more regional manufacturing network.

What I'm referring to in terms of investment is really much in line to the Beauty Reimagined vision, which is investing in consumer facing. So it's really much shifting our investment going forward to be where the consumers are, investing in the right media platform, being in the right distribution network with the right innovation. So in some way, is reducing our investment in SG&A and accelerating all investments in consumer-facing like advertising, like promotions that we have in any given market depending on the profile of each of the brands.

So the commitment is for us to, as you saw the profile of Q2 and Q3, is really to invest in our brand and consumer facing to really be able to accelerate retail. That's the essence of Beauty Reimagined, is to be able to free up the resources in the P&L to allow us to invest in consumer-facing to reignite retail. And our commitment is to have strong retail growth to rebuild strong double-digit organic operating margin, but at the same time for us to grow in both markets.

Our ambition is definitely to gain market share in the key markets, in the key brands and key categories around the world. And as we said it previously, our strategy is to rebalance the growth, to access this growth in the West, from East to West, we need to invest in consumer-facing and just like to make sure that we can accelerate.

And today, we have already some strong momentum as we see in various places such as like campaign that we've done with Estee Lauder on Thursday Night Football campaign in the US, or also Jo Malone men's campaign that we said we were going to accelerate the capture of new consumers, and we did it in men, and we have a tremendous growth in this category.

At the same time, also Clinique, we stated over and over again, with the move that we did close to -- in March of last year, we've been able to just capture lapsed consumers and new consumers through the expansion into Amazon Premium Beauty stores. And as a result, we have had eight months of consecutive market share gain in the US market.

So all these elements gives us the confidence to really invest in our brands in the right geography, but also where we have some successes around the world. So the investment is more going forward targeting again the consumer acquisition and to be able to reignite overall growth.

Akhil Shrivastava ***Estee Lauder Companies Inc - Executive Vice President and Chief Financial Officer***
I would add a few things, Lauren, that we are making a clear distinction here between consumer-facing and fixed costs. So as Stéphane said, on consumer facing, a lot more discretion, there's a lot more variability and a lot faster learning to quickly pivot our plans.

In the past, we made some investments which are big bets in fixed costs and capabilities, then you are stuck with them. And that's the big distinction we are making in pouring all our investments, to drive the business and constantly pivot. And that's what we'll keep driving regularly month by month, quarter by quarter, and constantly pivot.

Operator
Dana Telsey, Telsey Group.

Dana Telsey Telsey ***Telsey Group - Analyst***
Hi, good morning, everyone. Stéphane, as you think of the new initiatives you're putting in place with the Beauty Reimagined as we go through the next year or two years, what are the markers you're looking for to show the proof points that it's working? And how are you thinking about the travel retail channel as we move through this? Thank you.

Stéphane de La Faverie ***Estee Lauder Companies Inc - President and Chief Executive Officer***
Thank you, Dana. Look, there's five pillars to our Beauty Reimagined vision. And on terms of markers or KPI, we are tracking and we are creating actually a very thorough way of like tracking and follow every single of our action to just make sure that everything we do is going to deliver on this promise that we are making today.

The first one is the consumer coverage. What I mean about consumer coverage is our ability to just capture the consumers where they are. We know we didn't make fast move in terms of new distribution when the consumer was moving. And that's what we've demonstrated with the move that we made a few months ago with Amazon and many others like TikTok Shop in Asia and even in the US. So we are going to really measure how quickly we move in this channel and how much we can like capture lapsed consumer but also new consumer.

The second thing is our transformative innovation. I'm committed with the team to really accelerate innovation in a dramatic way to meet the consumer. We have many great examples already like La Mer, Clinique, Estee Lauder in the US and in China, but also throughout all our France brand. If you think about it, even like Le Labo going from strength to strength has been also about their ability to deploy the right innovation in the right geography around the world.

The first thing is, what we discussed in the prior question, is the consumer facing. So making sure that we are going to track, like Akhil said, month after month, quarter after quarter, the return on investment on every single investment we make in consumer-facing. And we're becoming more and more sophisticated in leveraging insights, leveraging data to meet like the consumers where they are.

And hardwiring AI through the organization not only will allow us to become better in supply chain, like I highlighted, but also to use AI to better target consumers with the right assets, but the right media targeting around the world.

The fourth one, which is the PRGP. The PRGP allows us to obviously, reduce the SG&A, free up like the necessary investment to invest in innovation and advertising, and at the same time resume and restore a solid double-digit operating margin in the next few years.

And the last thing, which we are going to track and already tracking inside the organization, is the simplification of ways of working. I made it clear in my operating -- my prepared remarks, sorry. We become -- we lost agility -- the agility came from the complexity of the organization. My commitment is to simplify the ways of working and that we can track it, and we track it every day already by simply reducing the number of meetings internally, to focus more externally.

I personally spent the month of December to meet with every single retailer in North America and some around the world. I'm about to embark in multiple travels around the world, we meet with our partners, retailers, et cetera, to be laser-focused on making sure that we reignite retail.

So I would say in that, we have a very clear tracking, a very clear vision. And this Beauty Reimagined vision has been deployed to the new executive team and throughout the organization and will continue to be deployed as we speak, to make sure that we all speak the same language with one clear objective, which is, again, to reveal strong retail growth, grow above market and to gain share and to resume the strong double-digit operating margin.

And so your second part of the question on travel retail. Travel retail remains an important part of the business. But it is very clear that we are reducing overall the dependency on travel retail and reducing the volatility of our overall business.

That being said, I want to just be clear, travel retail is an important channel for us to recruit and retain consumers. And in many instances, as certainly you've seen, it is a window of creating brand desirability for our brand around the world.

We know like the rest of the organization, we didn't capture growth enough with travel retail in the West. So while we are reducing dependency in travel retail in the East, we are also seeking new opportunities in the West with new brands and new categories that we have in our portfolio that we can deploy in a much faster way and creating a greater impact.

Dana Telsey Telsey *Telsey Group - Analyst*
Thank you.

Operator
Dara Mohsenian, Morgan Stanley.

Dara Mohsenian *Morgan Stanley - Analyst*
Hi, good morning. So we spent a lot of time on the execution plans with the reorganization, the detail is very helpful. I was just hoping also to get a bit more perspective from you on the softer cultural changes among the workforce that are needed behind the organizational changes, the cultural points you're most focused on emphasizing over the next few years.

And just also, how important is bringing in outsiders, whether it's the management, which appears limited so far, even use of consultants, external help as you look to sort of implement these detailed plans that you've outlined? .

Stéphane de La Faverie *Estee Lauder Companies Inc - President and Chief Executive Officer*
Thank you. I love this question. Obviously, cultural change is going to be critical because it has to be completely honest and transparent. This vision of Beauty Reimagined will be able to execute it as a team we commit behind one basically the vision, which we are. And that's the reason why we deployed this new executive team, already announced like this morning, and I've spoken to every single leader, and all of them are committed behind it.

It is about -- we all love this company. We know that culture is like very important. Our values remain extremely strong. And we are actually also realizing and recognizing where our strengths are. And this is the reason why I mentioned in my prepared remarks that we are bringing some external partners to help us in this transformation.

There are a lot of like great partners that have done that multiple times, and we are recognizing like, today, we need somehow in this execution of the PRGP. And I'm really committed with the vision we have at the support of the Board, at the support of the executive team that we are going to continue to build on our culture and our values and make this company way more agile than it has ever been before.

I mentioned it also, we are going through the biggest operational transformation in our history. This is going to take a lot of hard work. This is going to take partners outside that are going to help us and guide us. But I know ultimately that every single person that I spoke into -- two in this company today, within the Estee Lauder Companies, is absolutely committed to change, is absolutely committed to just bring speed and agility and everything that we are doing so we can rebuild this company to the rightful place that it belongs, which is really at the top.

Akhil Shrivastava ***Estee Lauder Companies Inc - Executive Vice President and Chief Financial Officer***
Dara, I would add one thing. I mean, of course, as Stéphane talked about, I mean, really what he's asking us all to do as leaders to support in this is really build a culture of three things that I take away very importantly from what he's telling us.

One, each one of us are owners and leaders and really empowered and accountable. Secondly, the consumer is at the heart of everything we do, whatever be your function, whatever be your work, wherever you are in the company. And then thirdly, a clear focus on value creation, and long-term value creation while navigating some of the challenges. And these things are, as a leadership team, we all are owning it along with our employees around the world.

Dara Mohsenian ***Morgan Stanley - Analyst***
Great. Thanks.

Operator
Oliver Chen, TD Cowen.

Oliver Chen ***TD Cowen - Analyst***
Hi, Stéphane and Akhil, as you think about prestige, what's your thoughts on the future of prestige in terms of hybridization, masstige, ingestibles in the broader sense of what the consumer thinks or doesn't think about what prestige means.

Also on your innovation pipeline, which looks quite exciting, what might be nearer term versus longer term? Because there's many great things that are underway. And as we think about the operating margin, just the recipe for expansion back to history, if there's a way to simplify that. I'm sure it's a combination of fixed cost leverage as well as innovation. Thank you.

Stéphane de La Faverie ***Estee Lauder Companies Inc - President and Chief Executive Officer***
Thank you, Oliver. I'll start and Akhil can add a little bit more flavor to the margin. So let me just start from the top of like your question about the outlook on the market. Frankly, the long-term fundamental of the beauty market are very, very strong and remains strong.

Remember, we play in the areas where middle class is extremely important to future growth. And middle class is continue to rise in many markets around the world, that is in the East, that is in the West, in many markets around the world.

We also, I believe, have a moment in time, we are living a great opportunity in terms of distribution expansion. The buyers have like been completely redefined when it took -- it comes to like distribution and how and where you can connect with the consumers. As we demonstrated, we go from our own freestanding stores with brands like Le Labo or Jo Malone, but at the same time, we are also like able to operate in channels like Amazon Premium Beauty prestige that allows us to connect with the consumer, and seek new consumer and continue with this principle of recruiting and sourcing from mass market into like prestige and luxury where we are.

And I would say, the third thing and very important thing, is this ability to connect with consumers faster and in an even closer way than we've ever done it before. So the combination of these three elements, I really believe like shows great potential for the overall industry.

And as part of the Beauty Reimagined, finally, we are also focus on capturing this part of the business that we haven't had access to in the distribution, but also at the same time, how we're going to target consumers better. Because our fundamentals are strong, our portfolio of brands is strong. We just need to make sure that our brands with the right innovation is going to be visible to the consumer. So every investment we make from an end-to-end connect from what they see and where they shop and the ability for us to just like capture that in a very agile and very quick way around the world.

Obviously, you're talking about pricing. Pricing has -- also challenged because of the buyers that have transformed completely from a distribution standpoint. We have brands like La Mer that continues to grow from strength to strength, being able to just grow and significantly gain share in markets like China in the last quarter.

And at the same time, you have The Ordinary, which is, by definition, the brand that is really capturing, at the entry of prestige, a lot of consumers, as demonstrated by our ability to move huge amount of units in multiple points of distribution. And we are very excited with the launch earlier this week of The Ordinary at Amazon because it will allow us to just like capture a greater number of consumers and that we can just aspire to do it in many places around the world.

So what I would say, we have a portfolio that is well diversified from the top of luxury to the entry of prestige with a world of beauty that I believe is well positioned to continue grow based on this indicator of growing middle class, new distribution and the ability to connect with the consumer in a much more tailored and personal way than ever before.

Akhil Shrivastava ***Estee Lauder Companies Inc - Executive Vice President and Chief Financial Officer***
Thank you, Stéphane. Hello, Oliver. So Stéphane touched upon our sales growth. I mean, of course, as we

look, we are driving the three critical things for long-term value: sales growth, margin and cash flow. And from a margin perspective, you saw that our margins are in the single digit right now. We have demonstrated a clear way to improve gross margin over the last few years, and there is still a lot more work to do here, and we are confident based on the work we have already done and what we see ahead that with the whole zero-waste mindset and the supply chain efficiency, we can make significant progress here. So that would be a critical building block as we go towards solid double-digit margin in the next few years.

Within OpEx, we are -- you saw that we have increased -- we have doubled the restructuring program. So that's a significant increase on the employee cost opportunities that would be there. Secondly, as Stéphane called out, we are step-changing our work on procurement, which means every single line item of our expense is an opportunity to improve. So that's the second big pillar.

And the third big pillar is shared service, where we have done work in the past few years but we have an opportunity to step-change with some of the leading partners around the world. So with all of those building blocks, we remain confident that we can move towards a solid double-digit margin in the next few years. And of course, we will share with you more details on the upcoming forums.

Oliver Chen *TD Cowen - Analyst*
Okay. Very helpful. Thank you. One quick follow-up. M&A, Stéphane and Akhil. There are a lot of good founder-led brands and innovations happening everywhere. How are you going to think about M&A within your culture or not in terms of as you look forward to new opportunities?

Stéphane de La Faverie *Estee Lauder Companies Inc - President and Chief Executive Officer*
I think, Oliver, on the M&A, as you know, part of our strategy, we are laser-focused with Beauty Reimagined to really reignite growth and rebuild profitability. And as such, we are in, obviously, our portfolio is key. As I said, we have some strengths that we need to accelerate and we have areas where we know we need to transform. And this is what we are going to tackle in the next few months, to really making sure that we are putting every single of our beautiful brand in the right position to really accelerate and contribute to the overall growth of the company.

When it comes to M&A, we will come to you like in the future. But obviously, every time there's an opportunity, we have a team, a great team, that is looking at what is available, but it has to be looked with the lens of, one, is it complementary to the portfolio? Is it going to add one thing? And at the same time, we need to just also like manage and balance our overall balance sheet, overall in the near term.

Akhil Shrivastava *Estee Lauder Companies Inc - Executive Vice President and Chief Financial Officer*
Yes. The only thing I would add is that we clear priorities to delever in the short term, our balance sheet. And then, of course, we are brand builders and we are constantly looking at opportunities. But in the near term, as Stéphane outlined, our priority would be to deleverage the balance sheet.

Operator

Olivia Tong, Raymond James.

Olivia Tong ***Raymond James & Associates, Inc. - Analyst***
Great. Thank you so much. You had mentioned a lot about increased complexity of the prestige beauty portfolio, clearly lots of changes both domestically and globally over the last several years. Presumably, you've gone to your key retailers in your early days as CEO. Can you elaborate on your discussions with them?

And then also, the game plan to capture more of the consumer in Asia, especially given their increased willingness to accept local brands in the premium segment despite obviously very significant investments that you've made. And then lastly, in Western markets, what you're doing to differentiate yourself versus your competition in key categories. Thank you.

Stéphane de La Faverie ***Estee Lauder Companies Inc - President and Chief Executive Officer***
So Olivia, like if I'm clear on the question you're asking is, obviously, like from what are we doing from a differentiation, obviously, to win. And I think the second pillar of Beauty Reimagined with the transformative innovation stimulus plan in a way that we are putting out there is really for us to be able to connect with the consumer in a greater way and in a faster way. As committed, we are going to triple the number of launches that we are going to bring to market within less than a year.

That allows us, when you think about this overall acceleration of innovation, to better tailor innovation by retailer to connect with the consumer at different places around the world. And there are clear retailers, frankly, from our own (inaudible) to consumer to the partners that we are working that are defined to be more about the trial and recruitment when some others are much more about like retention and recruitment.

So we are really tailoring not only an innovation plan to accelerate, but also an innovation plan that allows us to be able to react to an increased fragmented distribution around the world that allows us to just capture all the consumers.

So I would say, in this one, complexity can be managed as long as you have the right innovation that goes to the right consumers in the right distribution. And now in that, as part of the first pillar of Beauty Reimagined, is to meet the consumer where they are with the right product, but also at the right price point.

And I think this is one of the new elements that we are bringing to just make sure that, yes, La Mer can play in the price tier where they are, but you have multiple brands that have the right to play at different price points of prestige and luxury. And that's what we intend, and you are going to see a lot more innovation coming tailored by consumer by distribution by price point across, frankly, all the four categories that we operate in and the many subcategories that we see growing in the future. I hope it answers your question, Olivia.

Operator

This will conclude our question-and-answer session as well as our conference call for today. Thank you for attending today's presentation. You may now disconnect.