

Lululemon Athletica Inc at ICR XChange

Company Participants

- John Currie, EVP, CFO
- Laurent Potdevin, CEO

Other Participants

- Bob Drbul, Analyst, Nomura Securities

Presentation

Bob Drbul {BIO 3131258 <GO>}

Good afternoon, everybody. My name is Bob Drbul and I'm from Nomura Securities. It gives me great pleasure today to be here with Lululemon. I think we were talking about some of my opening comments; it has been a very interesting year. And what a difference a year makes, especially for Lululemon.

What we like about Lulu essentially is in the loyalty among the consumer, the unit story, the unit growth opportunity that is global, the story that is there. And as the management team has transitioned, it is always a good sign when you transition a management team from outgoing CFO to a new CFO, that we think is also very talented.

We have got Laurent Potdevin, is the CEO. He will be speaking. John Curry, the CFO, will also be speaking and Chris Tham is in the front row here as well. And Jody Raitts, the director of investor relations, is also here with us today. So with that, I would like to turn the microphone over to Laurent.

Laurent Potdevin {BIO 18481730 <GO>}

Good afternoon. I think this mic is on. Wow. It is a big crowd for the end of the day. I mean, I don't know if it's been as grueling for you guys as it's been for us. But the timing of these meetings back-to-back was intense.

Anyway, John and I are very pleased to be here today to give you an update on the business. So I will do a brief presentation. John will go a little bit further into the press release we issued this morning. Then we will go into a function show. And I am assuming that is why you guys are all here for. And you will get a glimpse of our Spring 2015 products for both men's and women's.

So before we begin, this is just a reminder that this presentation will include forward-looking statements, statements that are covered by the safe harbor provision. And you can find more details in our SEC filings.

Quick overview; I mean, I couldn't be happier and more proud of the performance that the team delivered during holiday season. We continued to build on the momentum that we saw in Q3. Clearly, hit an inflection point late in Q2, early in Q3. And we continued to build on that momentum during the holiday with higher traffic, sequentially improving comps. And just a great holiday season with less markdowns than last year.

And what I would like to do is share a quick personal story that really, in my mind, really sort of helped me to visualize the Lululemon opportunity. So on December 26, I was in Los Angeles where my kids live with their mom and my parents had flown from Europe. My daughter was going to a volleyball tournament and needed an outfit. So we decided to go to the El Segundo store, which is the closest to their home.

And away from the madness of Boxing Day in Canada at 1030 in the morning, I was really hoping that I would get through and shop within fairly quiet environment. And I walked into a jam-packed store. The music was blasting. People were lining at the cash register. People were lining at the changing room, like arms loaded with products. And the energy was incredible.

I mean, guests were engaging with educators. Guests were engaging with each other. And we have called our educators, educators for a reason for a long time. And for some reason, we have continued to call our stores, stores. But that environment was so much more than a store. I mean, it was a community hub and the energy that you experience in that location was just incredible.

And that is how I feel and see the Lululemon opportunity. I mean, it is a market that we created. We have got amazing product. We are leading the market with very strong margin and we deliver guest experience that are unique and second to none.

So when I think about the global opportunity, I really take the El Segundo store and I take that around the world, both in stores and online, across gender with men's and women's around the globe. And in the future across a number of new categories.

A lot of people have said, well, what are your -- what a difference a year will make. And I wasn't around last year. And I certainly took my share of pummeling early on. So -- but when I think about this past year. And despite all the headwinds that you guys are very well aware of, I think the team delivered tremendous performance.

Nine months ago we had set out to achieve three goals. One was to strengthen the foundation of the business so that we could scale the business and -- around the globe and start growing more across multiple categories. It was to reignite our product engine and it was to accelerate our global expansion.

We have clearly strengthened our business foundation. Our product flow, our predictability has greatly improved. Our quality at the store level is impeccable. And our guest experience continued to be so incredibly unique.

And we are very much on track to finish that foundational work by the end of 2015 and see the full impact of our work in Q1 of 2016 when our designers, developers and R&D will have had a chance to work through the entire go to market calendar and see their product come to life. From a standpoint reigniting our product engine, Tara and Jennifer have done an outstanding job in a very short period of time re-assorting, reflowing the assortment, shifting the balance of product and really chasing the product where we had opportunities with our fashion group. And what we saw in Q4 with tremendous performance of our bottoms, it is clearly an indication that we have turned the corner in reigniting our product engine.

And finally, when you think about accelerating our global expansion, we opened a store in London. We just opened a store in Singapore. We are about to open our second store in London in Chelsea next week or the following. And we have identified a number of showroom locations.

So we are going to be staying very true to our go to market strategy, which is about building showrooms, getting involved in the communities, gaining momentum with ambassadors. And we are going to do that over a shorter period of time so that we can accelerate our international growth.

So we had three pretty significant growth goals to achieve over the past year. And the team delivered outstanding performance. So moving forward, I mean, we're going to continue to build on our current momentum and 2015 -- I think John described 2015 really well on our Q3 call when he called it an overlap year. I mean, some of the investment that we have made in terms of building the foundation are going to sort of normalize and phase out. I mean, we still have a couple of large projects, including merchandising, planning. And allocation. Then we are going to ramp up some investments around product innovation in raw materials in silhouettes and in categories, as well as investments in the area of being very guest-centric both in store and digitally. So you can expect to see operating margin leveraging in 2016.

When you think about the key success factor of Lululemon, it has always been about the product, brand and community. And guest experience. And what you saw in Q4 with better product flow, better predictability is that you saw the ability to see these three circles come together. And for the first time -- and this is tremendous -- this is a tremendous unlock in terms of the potential of the brand, I mean, the three areas are starting to work really closely together.

So being able to predict the product coming into the store allowed us to do much better product notification for our guests. It has allowed us to build campaigns that will deliver seamlessly across digital and in stores. And it has allowed us to much better educate our educators in-store so that they could, in turn, educate our guests.

So we have got three fantastic leaders in those three areas with Delaney leading store experience, with Duke Stump that recently joined us to lead brand and community. And with Tara leading the product group. And we are really at a time now where we can switch from playing defense to playing offense. And so I am really looking forward to those three leaders come together and unlocking so much of the potential that we have got ahead of us. And clearly, as we start playing offense, innovation is going to be fueling all three elements of that business.

So product, well, we are leading through the design of innovative products. And the white space of -- some of you saw our white space area last year. I mean, these guys have done a tremendous work. That, combined with the talent that we hired on the design side, is really giving us the tools to continue to lead in a way that is unprecedented and really sort of focus on innovation from a raw materials standpoint, from a silhouette standpoint across men's and women's. And down the road across multiple categories.

And we are at a time now where, with better product flow and with better predictability, we can really start working with our vendor. We can move away from working on the tactics of supply chain to really sort of looking down the future and working on the innovation with them. So very clearly a year of stabilizing the business, creating momentum from a product standpoint. And now moving full steam ahead.

Guest experience is clearly something that we have always done really well. And our focus is going to be in a couple of areas. One, from a digital standpoint, we have got a tremendous opportunity to create more intimate, more personalized relationships with our guests. And so we are implementing CRM. We are doing a full global redesign of our website.

But think about, given that we have touched every guest experience, I mean think about -- and I use that example because she is a friend of mine. I mean, she is a consultant. She lives in Park City. She does most of her buying online. When she goes to the store or, at this point in time, our new store in Park City, we don't know who she is.

And so think about an environment where she goes to the store, we know exactly who she is. We know what kind of activities she gets involved in. And when she goes on vacation to Hawaii, when she lands, we actually can connect her with one of our ambassadors and gives her like a class next to a hotel. So the ability to really leverage technology, CRM. And from a product standpoint, our RFID project is really going to allow us to create much more intimate and continue to build on what is already a very good and a very unique and powerful guest experience.

Then, from a store standpoint, I mean, we have got -- we are not oversaturated. We have got a very strong footprint and we are starting to play with different formats. So the economics always have to work first. But you are starting to see us play with different formats.

So in SoHo, we opened a men's only store. We are opening a larger footprint in Flatiron New York or in Robson Vancouver or in Miami recently. And so we are sort of playing with different formats and trying to leverage the men's opportunity. And when it comes to men's, I mean, we are trying the men's only store. But we also really like the idea of the side-by-side because she still shops for him a lot. So a real focus on guest experience.

And finally, from a brand and community standpoint, it is really sort of deepening our voice. I mean, taking all the work that we do so well at the grassroots level and sort of giving it -- amplifying that voice so that it has got global resonance. And I am really personally very passionate about the balance of doing good and doing well. So in the near future you kind of expect a little bit more focus on increasing our purpose in that sense. And really sort of having a mission that makes us a little bit more inclusive. And that is going to resonate with our guests very, very strongly.

So with that said, 2014 was a year of stabilizing the business. We did -- the whole team did a great job battling all sorts of headwinds. I mean, the first six months were certainly interesting and not what I had necessarily anticipated. But our work is paying off. The second half of the year, it has been tremendous. We're going to continue to build on the momentum that we have created. And I am really, really excited about 2015.

So before I turn it to John, I really want to thank him for his guidance, his advice. I mean, this past year would have been many times more difficult for me if I didn't have him by my side. And while we are sorry to see him go, we know that he is going to have a ton of fun skiing.

So and Stuart, who most of you -- a lot of you guys know, is a fantastic hire that -- we conducted the search together. So very, very excited for John and for Stuart. And obviously, John is leaving us in a very strong position, with a very, very strong financial team with Chris, Jody. And Winston. So with that, I will let John dive a little bit deeper into our numbers.

John Currie {BIO 1494810 <GO>}

Thank you. Both Bob and Laurent said it. But I just have to say it as well. What a difference a year makes. This year I am here with a CEO. That is an improvement. And I am not standing up here explaining reduced guidance. I have the pleasure of summarizing the increased guidance that we were able to announce this morning.

We really had a tremendous holiday season. We came in with some headwinds in terms of store openings and currency and port disruptions. But we mitigated those to some extent. And strong product assortment, continuation of strong traffic trends that we started seeing in Q3 really allowed us to deliver a better than our expectations for Q4.

And the strength was across the board. It was both in women's and in men's. And it was both in stores and on e-commerce. So just briefly, as we announced this

morning, we increased our revenue guidance for the quarter to \$595 million to \$600 million. So the top end of that range is increased by \$15 million and we, of course, narrowed the range because we are closer to the end of the quarter.

That translates to a combined comp for the quarter of 6% to 7%, up from previous low single-digits. And with the leverage on the higher volume, there is strong flow through to EPS and our guidance is now \$0.71 to \$0.73, an increase from the previous \$0.65 to \$0.69. For the year, that takes us to just under \$1.8 billion with a positive (three) combined comp and normalized EPS in the range of \$1.80 to \$1.82.

So we feel great about a strong finish to 2014 and we feel that momentum carrying into 2015. Now 2015 -- I don't know how many times I have said today that I am not giving guidance on 2015 yet. But let me just talk a little bit about some of the factors impacting the P&L and the margin profile.

Let me start by talking about currency, because with lower oil prices, Canada being a petrodollar, there has been quite a significant exchange reduction in the Canadian dollar versus the US dollar over the past two to three months, even since we last gave guidance. In the past, when most of our revenue was in Canada, a drop in the Canadian dollar was quite catastrophic. And the point is really bad is not the case anymore.

When the Canadian dollar is lower, of course it reduces our reported revenue in US dollars. It also compresses our gross margin, because we buy product in US dollars, even when it is sold in Canada. But because our head office is in Vancouver in Canada, the SG&A that is also in Canadian dollars offsets the negatives in the revenue and the gross margin line. And in fact, we have quite a nice natural hedge at this point. If anything, a lower Canadian dollars slightly benefits us. So again, four or five years ago that was a much different conversation. And I think it is important to point out that shift.

Other factors, as we head into 2015, in addition to the momentum we felt in Q4 in terms of traffic, the stronger product assortment that is going to help drive topline in 2015. We have lots of growth drivers ahead of us still. We are going to end the year at 200 stores in the US, which is 2/3 of the way to our target of 300. And we have a robust pipeline for 2015 and beyond to complete that buildout in addition to continuing -- to increase our penetration on our e-commerce channel.

ivivva, our second concept, which will end the year with 22 stores, has really hit its stride. It is doing \$1000 a square foot. And so it is time to put our foot to the gas a little bit. We are looking to add up to 20 stores for ivivva next year.

In terms of margins, we talked a lot about -- for the last year about all the work that Tara and Jennifer are doing to shore up the supply chain, all the investments in systems and people and talent and process change. And those are well underway and on track. But as we have said before, most of the benefit of that you will see in 2016.

In 2015, there will be some benefit on the margin. We certainly stabilized our merchandise margins. We will see some improvement in airfreight. But for the most part, the benefits from that, you will see next year.

As Laurent mentioned, 2015 is sort of an overlap year in terms of investment on the supply chain. It was a heavy year in 2014, a lot of systems and other initiatives that we were putting the finishing touches on in 2015. And we are shifting our focus to more forward-looking -- playing offense investments including our R&D, our white space facility. And an increased focus on innovation in our product.

In addition to investments on the supply chain, again, we are looking to play offense in terms of other areas of investment, include technology, guest experience, innovation. And the brand. So all of this is a way of saying 2015 -- we feel like we are entering 2015 in a strong position.

The question is not are we going to show leverage in 2015. The question is really, as we shift to playing offense, what are the right investments that are enough to be really driving a longer-term growth of the business without taking on too much beyond what we can execute well.

So again, we are still working on the final touches of our 2015 budget with our board. But again, the number one in question isn't are we showing leverage. It is really how do we are we doing the right things to support the long-term growth of the brand, because that is really what is important in the long run.

So that is the end of the prepared remarks ahead of the function show. So if the audience listening to this on webcast, this concludes the formal part of the presentation. And thank you for joining us today. We will turn off the audiovisual and the webcast.

This transcript may not be 100 percent accurate and may contain misspellings and other inaccuracies. This transcript is provided "as is", without express or implied warranties of any kind. Bloomberg retains all rights to this transcript and provides it solely for your personal, non-commercial use. Bloomberg, its suppliers and third-party agents shall have no liability for errors in this transcript or for lost profits, losses, or direct, indirect, incidental, consequential, special or punitive damages in connection with the furnishing, performance or use of such transcript. Neither the information nor any opinion expressed in this transcript constitutes a solicitation of the purchase or sale of securities or commodities. Any opinion expressed in the transcript does not necessarily reflect the views of Bloomberg LP. © COPYRIGHT 2024, BLOOMBERG LP. All rights reserved. Any reproduction, redistribution or retransmission is expressly prohibited.