URBAN OUTFITTERS, INC.

Second Quarter, FY'22 Conference Call
August 24, 2021

Participants

Richard A. Hayne, Chief Executive Officer
Frank Conforti, Co-President & COO
Margaret Hayne, Co-President & CCO
Sheila Harrington, Global CEO, Urban Outfitters & Free People Groups
Tricia D. Smith, Global CEO, Anthropologie Group
Melanie Marein-Efron, CFO
Azeez Hayne, Chief Administrative Officer and General Counsel
Dave Hayne, Chief Technology Officer, URBN and President, Nuuly
Barbara Rozsas, Chief Sourcing Officer
David Ziel, Chief Development Officer
Oona McCullough, Executive Director of Investor Relations

Good afternoon, and welcome to the URBN second quarter fiscal 2022 conference call. Earlier this afternoon, the Company issued a press release outlining the financial and operating results for the three- and six-month periods ending July 31, 2021.

The following discussions may include forward-looking statements. In today's commentary, unless otherwise noted, all comparisons will be made to the second quarter of fiscal 2020, referred to as LLY. It's important to note at this time, the global COVID-19 pandemic has had and continues to have a significant impact on URBN's business. Given the uncertainty about the duration and extent of the virus' impact to the global retail environment, content discussed on today's call could change materially at any time. Accordingly, future results could differ materially from historical practices and results or current descriptions, estimates and suggestions. Additional information concerning factors that could cause actual results to differ materially from projected results is contained in the Company's filings with the Securities and Exchange Commission.

On today's call you will hear from Richard Hayne, Chief Executive Officer, URBN, and Frank Conforti, Co-President and COO, URBN. Following that, we will be pleased to address your questions. For more detailed commentary on our quarterly performance and the text of today's conference call, please refer to our investor relations website at www.urbn.com.

I will now turn the call over to Dick.

Dick Hayne

Thank you, Oona, and good afternoon everyone. Today we announced record-breaking second quarter results, so I'll begin my prepared remarks by thanking all Brand, Creative and Shared Service teams for a truly remarkable performance. Your hard work and careful execution produced one of the strongest quarters in URBN's history, so thank you.

I will now provide a brief, high-level overview of those results and then provide some thoughts on the consumer and our prospects for the third quarter and beyond.

Total Company sales grew by more than 20% reaching a record $1.16B in the quarter. Total retail segment 'comp' sales advanced by 40% versus LY and 22% against LLY. Powerful consumer demand across most product categories, especially apparel, plus strong execution by our teams drove positive double-digit retail segment 'comps' at all brands.

The second biggest accomplishment in the quarter, just behind the amazing retail segment 'comps', was the strength of full-priced selling and the corresponding decrease in markdown sales at each brand. URBN established a new record low markdown rate with all three brands handily besting their LLY rates. This helped to generate outstanding merchandise and gross profit margins despite large increases in delivery and logistics expenses. The combination of strong gross profits with tightly controlled SG&A expenses led to record Q2 operating income and earnings per share of $1.28 – more than twice LLY's result.

As we look to the back half of the year, we believe that URBN's prospects shine brightly. Most importantly, consumer demand for our products continues to be robust; she remains optimistic, has money to spend and wants fashion newness in her wardrobe and home décor. To date, we have seen negligible impact on sales from the recent rise in Delta cases and all brands continue to experience strong regular price 'comps'. 'Comp' sales in August at the Free People and Anthropologie brands are approximately in-line with second quarter results, while the Urban brand 'comps' have slowed beginning in mid-July. This is primarily due to much lower back-to-school promotional activity versus two years ago. The Urban brand has intentionally walked away from most back-to-school discounting as it seeks to reposition its price/value equation. We believe retail segment 'comps' for the Urban brand in Q3 could moderate to the high single-digit range. August-to-date, total URBN retail segment 'comp' sales are mid-teens positive, and we believe Q3 'comp' sales will most likely end in that range.

Now, I'll turn the call over to Frank who will provide more details on segment and brand performance and our thoughts on the third quarter.

Frank Conforti

Thank you, Dick, and good afternoon everyone. I also want to start by congratulating all URBN teams on a remarkable quarter. We recognize these results come amidst a still challenging environment and are grateful for your hard work and dedication, thank you. Now I will give you some more details on our results.

Starting with the retail segment. Store performance improved significantly from recent quarters. Stores registered healthy AUR and conversion gains that largely offset negative store traffic. 'Comp' store sales in North America landed down just slightly, while 'comp' store traffic was high-teens negative. By region, traffic in the Southeast and Southwest markets continued to outperform the major metro markets in New York and California, but all markets showed impressive improvement from Q1 levels. In Europe, while all stores were open during the quarter, traffic levels remained below that in North America as some jurisdictions continued to impose severe operating restrictions.

The already booming digital channel in North America continued to flex its impressive muscles registering mid-double-digit sales increases which easily offset the low, single-digit negative store 'comp'. In Europe, the digital channel recorded another blockbuster performance barely missing triple-digit growth for a second consecutive quarter. In total, digital performance was driven by increased sessions, improved conversion and higher AOV.

Moving to the wholesale segment, sales decreased by 30% versus LLY. This decrease was the result of lower sales at Free People wholesale. As we have discussed previously over the course of the past year, Free People wholesale has adjusted its customer mix cutting back some accounts to better align with its go-forward strategy of concentrating on full-price selling. While this strategy has reduced sales in the short term, we believe this is benefitting the overall brand and this has resulted in strong operating profit in the quarter, despite supply chain cost increases, and we believe the strategy will result in better operating income versus LLY in the second half of this year.

Partially offsetting the decline in Free People wholesale sales is the Urban Outfitters wholesale business. Urban delivered $5M of revenue in the quarter, up 480% from LLY. Urban wholesale launched in fall of 2018 offering their BDG line of sustainably produced denim jeans and separates to select retailers. The Urban brand continues to build on their initial BDG launch success and has added their iets frans line to their wholesale distribution. We are looking forward to the Urban brand continuing to build on this growth success.

I will now provide more details by brand, starting with the Urban Outfitters brand. The Urban brand delivered a 20% retail segment 'comp' vs. LLY. This was the result of strong double-digit digital sales and positive store 'comps'. This impressive sales performance came despite a significant decrease in promotional events during the quarter. As Dick noted earlier, the brand is repositioning itself, moving away from frequent promotions and moving to offering an everyday accessible opening price point in key categories. Due to the strategic focus on key prices points, regular price selling has accelerated, and promotional activity has been reduced significantly resulting in the brand delivering its lowest ever second quarter markdown rate. Full price selling, which jumped by more than 40%, was led by women's apparel followed by home goods. A strong retail segment sales 'comp' of 20%, fueled by stronger regular price selling, led to mid-teens operating profits for the brand.

Now turning to Anthropologie. The brand delivered a 14% retail segment 'comp' vs. LLY, which represents significant improvement from previous quarters. Retail segment 'comp' sales accelerated each month in the quarter fueled by double-digit digital sales which more than offset negative 'comp' store sales. From a product perspective, all categories were 'comp' positive, Home continued to perform exceptionally well, but the improvement in total 'comp' was driven by a pronounced acceleration in apparel whose trend improved nearly 20 percentage points in the quarter vs. Q1. Accelerating topline, significant improvement in gross profit margin and well controlled expenses resulted in a strong mid-teens operating profit for the brand.

The Anthro customer is shopping again and is looking to refresh her wardrobe with newness in all categories. Not only is she refreshing her wardrobe in the more occasion-based categories such as dresses that she has not worn in some time, but she also continues to respond to newness in the more casual aspects of her wardrobe. Due to the strength in apparel, the brand took the opportunity to execute toward a more regular price business by decreasing apparel promotional events by 82% versus LLY, which contributed to a historically low second quarter markdown rate for the brand. Early fall reads are nicely positive driven by similar trends within apparel. This past weekend the brand launched a rebranding campaign for Pilcro sustainable, inclusive denim that will continue through the fall. Anthro believes it has the opportunity to be a denim destination for their customer and believes the rebranding of Pilcro will enable the brand to capitalize on this opportunity.

Now I will call your attention to the Free People brand. Once again, the Free People team produced an extraordinary quarter with retail segment 'comps' achieving a staggering 53% gain vs. LLY. Every product category recorded at least a strong double-digit 'comp', while the FP Movement brand retail segment sales grew by over 300% versus LLY. The total Free People brand generated powerful, triple-digit direct 'comps' which easily offset the slightly negative store 'comps'. Store sales showed sequential improvement in the quarter with July store 'comps' turning positive. Free People's extremely low markdown rate for the quarter led to over 400 basis points improvement in merchandise markdown rate. Strong sales and gross margin growth all led to an impressive 20% retail segment operating profit rate for the brand.

Lastly, I will speak to Nuuly. As noted on our last call, as the country began reopening this spring, our subscription rental business saw a positive shift in customer behavior. Many subscribers who had paused their subscription last year resumed their monthly deliveries. During the second quarter our growth of subscriptions slowed due to low availability of inventory in certain categories the consumer was demanding such as dresses. We then chased into a better inventory position in these categories and our subscriber trends have improved. We are looking forward to continuing our subscriber growth over the second half of the year and learning more about the customer preferences for their rental experience.

Now I will discuss our thoughts on our third quarter and full fiscal year 22 financial performance. As Dick noted, similar to the second quarter, we remain optimistic about the opportunity ahead of us this year.

Of course, there are always challenges to overcome and risks to our plans. The impact of COVID-19 is still driving numerous problems and costs pressures in many areas of the business. Logistics, sourcing, fulfillment, and the overall labor market remain constant areas of focus right now. We have several strategies in place to try to mitigate the impact of cost and performance challenges in these areas.

We believe the third quarter could continue to show healthy sales improvement vs. FY'20. We believe our retail segment 'comp' sales growth could land in the mid-teens range, while the wholesale segment sales could decrease at a rate similar to the second quarter due in part to the realignment of the Free People brand customer base to focus on more regular price selling. Together this would result in total company sales in the low double-digit range.

Based on current sales performance and forecast, we believe our gross profit margins for the third quarter could show over 100 basis points of improvement to FY'20. Much like the second quarter, this improvement could be largely driven by lower markdown rates as a result of strong consumer demand, solid product performance and disciplined inventory control. We believe favorable markdowns could offset lower initial mark-ups and deleverage in delivery and logistics expenses. Lower initial mark-ups are likely to be due to increased freight and commodity price increases. Deleverage in delivery and logistics expense are likely to be driven primarily by the increased penetration of the digital channel as well as increased labor expenses.

Now moving on to SG&A. Based on our current sales performance and plan, we believe SG&A for the third quarter could grow at a rate just below our sales growth rate. Our planned growth in SG&A is primarily due to greater marketing and creative spend to support our robust digital channel growth. Additionally, our SG&A growth is a result of planned incentive-based compensation which was largely not achieved in FY'20. As we have done in past quarters, our teams will manage SG&A relative to actual sales.

Please note, we have managed our SG&A rate of growth well below our sales growth for the first half of the year. While I do believe we can continue to leverage SG&A in the third quarter, and back half of the year, I do think that our SG&A growth rate will trend closer to sales for the remainder of the year. The difference between the first and second half is due to increased marketing expenses as well as increased labor expenses in stores and the home office.

We are currently planning our effective tax rate to be approximately 24% for the third quarter and full year FY'22.

Capital expenditures for the fiscal year are planned at approximately $285 million. The spend is primarily related to providing increased distribution and fulfillment capacity to support our growing digital business and secondarily, to opening new stores.

Due to the logistics and sourcing extended lead times, we are strategically bringing inventory in earlier than normal in certain categories like home and garden in order to try and protect holiday sales. We believe this will elevate our inventory a bit at the end of Q3 vs. LLY.

Lastly, we are planning on opening approximately 26 new stores and closing 11 stores over the second half of the year. Our new store opening number does not include franchise partner locations in international markets.

As a reminder, the forgoing does not constitute a forecast, but is simply a reflection of our current views. The Company disclaims any obligation to update forward looking statements.

I will now turn the call back to Dick.

Dick Hayne

Thank you, Frank. Before closing today, I want to give an update on two of our more prominent growth initiatives – FP Movement and Nuuly. FP Movement, as you will remember, is a sub-brand launched by the Free People team that offers fashion activewear and accessories across three channels of distribution – digital, stores and wholesale. Movement delivered another standout quarter in Q2 growing total brand revenues by more than 200%. The brand currently operates 54 shop-in-shop locations inside Free People Collection stores and 13 standalone stores, 9 of which have opened since the beginning of Q2. The standalone stores are profitable and performing well above our pro-forma expectations. In fact, AOV, UPT and conversion in the standalone stores are all performing above Free People Collection stores in comparable markets. We plan to open an additional 6 Movement stores in the remainder of FY'22 and another 15 to 20 in FY'23. During the quarter the Movement teams successfully grew their customer base by more than 80% versus LY and over 300% versus LLY. This led to strong triple-digit direct channel growth. The brand's rapid growth and continued success across all channels and categories re-enforces our belief in the large market opportunity FP Movement enjoys.

Moving to Nuuly, this brand currently operates a growing subscription rental service for women's apparel. Today, the brand announced the launch of its sister brand – Nuuly Thrift, a peer-to-peer, resale marketplace where anyone can buy or sell women's, men's or kids apparel and accessories via an iOS device. The Nuuly team plans to launch its app later this fall. Both Nuuly platforms – Thrift and Rent – will support its mission to be a curated destination for anyone who loves fashion and is exploring how to wear, buy and sell it in ways that are gentler on the planet – and on their wallets. Nuuly Thrift will give sellers an option to receive their payout directly into their bank account or they can choose Nuuly Cash and instantly earn an extra 10% on their payout. Nuuly Cash, including the extra 10%, can then be spent back at Nuuly Thrift or at any of the URBN family of brands, on-line or in stores. This should create a cycle of buying and selling within the URBN ecosystem while also creating value for the customer.

We're excited about the growth opportunity presented by Movement and Nuuly. Both can be large businesses in their own right and both can integrate and be synergistic with our existing brands. I expect you will be hearing more about them on future calls.

That concludes our prepared remarks. I want to thank our brand, creative and shared service leaders. I also thank our 19,000 associates worldwide for their hard work, dedication, and amazing creativity. I thank our many partners around the world for their extra efforts in helping us overcome numerous supply chain disruptions, and finally, I thank our shareholders for their continued interest and support. I will now turn the call over for your questions. As a reminder, please limit your questions to one per caller.