

# **URBAN OUTFITTERS, INC.**

Third Quarter, FY'12 Conference Call  
November 14, 2011

## **Participants**

Glen T. Senk	Chief Executive Officer
Eric Artz	Chief Financial Officer
Oona McCullough	Director of Investor Relations
Glen Bodzy	General Counsel
Frank Conforti	Chief Accounting Officer
Freeman Zausner	Chief Operating Officer

## **Introduction**

### **Glen**

Good afternoon, and welcome to the URBN quarterly conference call. With me today is Eric Artz, Chief Financial Officer, Oona McCullough, Director of Investor Relations and select members of our executive team.

Earlier this afternoon, the Company issued a press release outlining the financial and operating results for the three and nine month periods ending October 31, 2011.

Eric will begin today's call by providing details on our performance, I will continue the prepared commentary with closing remarks, then the group and I will be pleased to answer any questions you may have.

As usual, the text of today's conference call, along with detailed management commentary, will be posted to our corporate website at [www.urbanoutfittersinc.com](http://www.urbanoutfittersinc.com). I'll now turn the call over to Eric.

## Eric

Thank you Glen.

The following summarizes our Third Quarter Fiscal 2012 performance versus the comparable quarter last year:

- Net sales increased 6% to \$610 million.
- Income from operations decreased 30% to \$73 million, or an operating margin of 12.0%.
- Net income was \$51 million or \$0.33 per diluted share.
- Comparable Retail Segment sales, which include our Direct-to-Consumer channel, decreased 3%, including an increase of 14% at Free People, flat comparable sales at Urban Outfitters and a decrease of 7% at Anthropologie.
- Total Company comparable store net sales decreased 7%.
- Direct-to-Consumer comparable net sales rose 15% with Direct-to-Consumer penetration increasing to 20%.
- Wholesale net sales increased 13% to \$39 million.
- Gross profit decreased 8% to \$216 million, while gross profit margins decreased 571 basis points to 35.4%.
- Selling, general and administrative expense, expressed as a percentage of net sales, increased 53 basis points to 23.4%.
- Total inventories increased \$78 million to \$367 million, or a 27% increase over the prior year period.
- Finally, during the quarter the company repurchased and retired 13.3 million common shares for \$322 million, thus completing the 10 million shares authorized for repurchase by our Board of Directors on August 25, 2011.

Turning to our key business metrics, I'll begin by providing detail on sales for the quarter.

New and non-comparable store sales contributed \$62 million to the consolidated net sales increase. The Company opened 16 new stores in the quarter—4 Anthropologie stores; 4 Free People stores; 7 Urban Outfitters stores, and 1 BHLDN store.

Within the quarter, total Company comparable store sales were strongest in September, followed by August, then October.

Within North America, sales at Anthropologie and Urban Outfitters were strongest in the South and weakest in Canada, while sales at Free People were strongest in the West and weakest in the Northeast. In Europe, sales at Urban Outfitters were strongest in Continental Europe and weakest in Ireland.

By store type, sales at Anthropologie were strongest in free standing locations and weakest in malls, while Urban Outfitters were strongest in malls and weakest in street locations. Sales at Free People were strongest in lifestyle centers, and weakest in street locations.

The comparable store net sales decline was driven by a 1.3% decrease in average unit selling prices, a 1.5% decrease in average number of units per transaction and a 4.5% decrease in total transactions.

Direct-to-Consumer revenue increased 17% to \$123 million, including a 15% increase in comparable sales. The penetration of Direct-to-Consumer net sales to total Company net sales increased 180 basis points to 20%, with results largely driven by a 31% increase in website traffic to over 37 million visits.

For Retail Segment sales, home was strongest at Anthropologie, men's accessories and intimates were strongest at Urban Outfitters, and intimates were strongest at Free People.

Wholesale Segment sales for the quarter increased 13% to \$39 million, driven by an 18% increase at Free People, offset by the reduction in Leifsdottir sales as a result of the decision to exit the channel in May of this year.

I'd now like to turn your attention to gross margin, operating expense and income.

Gross profit in the quarter decreased 8% to \$216 million, and the gross margin rate decreased 571 basis points to 35.4%. This decline was primarily due to increased markdowns to clear slow moving women's apparel inventory at Anthropologie and Urban Outfitters, as well as occupancy deleverage caused by negative comparable store sales.

Total selling, general and administrative expenses for the quarter, as a percentage of sales, increased by 53 basis points to 23.4% due primarily to deleverage in direct selling and supervisory costs driven by negative comparable sales.

Our effective tax rate for the third quarter decreased to 32.8%, from our year-to-date rate, primarily due to favorable revisions to federal and state tax estimates resulting from our tax return filings in the quarter.

Total inventories increased \$78 million to \$367 million, or a 27% increase over the prior year period. Comparable Retail Segment inventories at cost, which include our Direct-to-Consumer channel, were 18% higher at quarter's end, while comparable store inventories increased 12%. The balance of the increase was due to acquisition of inventory to stock new retail stores.

As we look forward to the fourth quarter, it may be helpful for you to consider the following:

- First, we plan to open 21 new stores in the fourth quarter bringing our annual new store total to 57 this year; including, 14 Anthropologie stores in North America, 1 Anthropologie store in Europe, 20 Free People stores in the United States, 14 Urban Outfitters stores in North America, 7 Urban Outfitters stores in Europe and 1 BHLDN store.
- Second, given our intra-quarter sales trend during the third quarter, we ended the quarter with higher than desired inventory levels. As a result, fourth quarter gross margins could be lower than what we experienced in the third quarter, on an absolute basis. We are committed to managing our year-end inventory to a more appropriate level.
- Third, we continue to focus on effectively managing our selling, general and administrative expenses. Our estimated leverage point for expenses in the fourth quarter is an approximate 2% comparable store sales increase.
- Fourth, we are planning for fiscal 2012 capital expenditures of \$180-\$190 million.
- Finally, our annual effective tax rate is estimated to be 36%, resulting in an estimated fourth quarter tax rate of 38%.

As we look forward to fiscal 2013, we are planning for low double digit square footage growth and are targeting 55-60 new stores.

As a reminder, the forgoing does not constitute a forecast, but is simply a reflection of our current views. So with that as a financial backdrop, I'll turn the call back over to Glen who will proceed with his closing commentary.

## **Glen**

Thank you Eric.

Let me begin my prepared remarks by stating that the organization and I were dissatisfied with our third quarter financial performance. While the absolute results compare favorably with many of our industry peers, the relative performance falls significantly short of our historical accomplishments and goals.

The course ahead is as clear to us as the challenges encountered. We have four key priorities:

- First, and most importantly, improve the women's apparel offering at both Anthropologie and Urban Outfitters.
- Second, manage the inventories aggressively to achieve an optimal inventory position as we enter the spring season.
- Third, continue to finance growth opportunities including distorted investment in our Direct-to-Consumer channel, and continued brick and mortar expansion, where our new store productivity continues to exceed that of the average fleet.
- And finally, ensure a smooth transition with the recent organizational changes, including a thorough on-boarding of our new senior executives.

Despite our disappointment in the quarter, there are several highlights I'd like to note:

- At Anthropologie North America, Direct-to-Consumer comparable sales improved sequentially versus the second quarter; and across all channels—bottoms, dresses, shoes and the home business were positive and strengthened through the quarter. The tops category, which represents more than half of the apparel business during this timeframe, is where the challenge lay. This is a fashion issue, plain and simple. We need more compelling product, and the team is hard at work mining the selling attribute information and challenging the supply chain to adjust and move as quickly as possible to improve the offering.
- At Urban Outfitters North America, Direct-to-Consumer comparable sales also improved sequentially versus the second quarter, including a strong overall advance in women's apparel. Across all channels, women's bottoms, dresses, accessories and intimate apparel along with men's and home continued to build momentum during the quarter. We believe the assortment and stores are much improved, and the holiday prototype results were encouraging, although it is too soon to predict success across the chain as the full assortment has yet to reach all stores.
- Free People delivered another strong quarter with solid results across their retail, Direct-to-Consumer and wholesale channels, and they remain on track to open 20 new stores this year, more than double the number of stores they opened last year which is a testament to the strong top-and-bottom line results the team continues to deliver.
- Our European businesses also displayed meaningful progress during the quarter in what has certainly been a difficult and volatile macro environment. Comparable store sales improved sequentially through the quarter for both Urban Outfitters and Anthropologie, and both brands posted strong Direct-to-Consumer sales.

As a merchant at heart, I realize that I am an eternal optimist, so I ask that you not misconstrue my enthusiasm as an indication of our performance. This is a cyclical business, and I cannot tell you when our trend will improve. If history is any indication, I believe we will come out of this cycle stronger—that we have the operating model, core structure, brands and most importantly, talent to achieve our goals. I also believe you will know when we are on the upward trajectory—you will see it in our product, the stores and our websites.

We have a clear long-term vision for our Company and our prospects for growth. We are a multi-brand, multi-channel, multi-national retailer with tremendous opportunity within our core brands in North America and abroad, with seeds for additional growth in our new concepts.

Before opening the call to questions I would like to thank the entire URBN organization for their hard work and dedication and our shareholders for their continued support. At this time I will invite questions, limiting each caller to one question.

Thank you.