URBAN OUTFITTERS, INC.

Fourth Quarter, FY'21 Conference Call
March 2, 2021

Participants

Richard A. Hayne, Chief Executive Officer
Frank Conforti, Co-President, COO & CFO
Margaret Hayne, Co-President & CCO
Sheila Harrington, Global CEO, Urban Outfitters & Free People Groups
Hillary Super, Global CEO, Anthropologie Group
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, Director of Investor Relations

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

The following discussions may include forward-looking statements. It's important to note at this time, the global COVID-19 pandemic has had and continues to have a significant material 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. To find disclosures and reconciliations of non-GAAP measures that we use when discussing our financial results, please refer to our earnings release in the Investor Relations section of our website.

On today's call you will hear from Frank Conforti, Co-President, URBN, and Richard Hayne, Chief Executive Officer, 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 Frank.

Frank Conforti

Thank you, Oona. Good afternoon everyone and thank you for joining our call.

On today's call, I will discuss our thoughts on our first quarter and full fiscal year 22. While we certainly have more clarity than we did at this time last year, there is still a meaningful amount of uncertainty in the year that lies ahead.

Even with this uncertainty, both Dick and I believe there are plenty of reasons to remain excited and optimistic about FY'22 and beyond. We feel confident about our overall strategy but have less clarity on the timing and magnitude of recovery.

For example, we are confident consumer spending will rebound this year and believe apparel spending will be a beneficiary of the rebound. We believe, as consumer confidence improves, and the impact of the virus continues to wane, the consumer will want to go out and socialize more. When they do, they will want to wear new things.

We are confident store traffic will improve. We have less clarity about the level and timing of that improvement. February has been a difficult month to draw conclusions about traffic trends as severe weather patterns negatively impacted the North American business and nearly all our European stores remained on lockdown. Despite that, we are beginning to see signs of improvement, especially in the warmer weather stores.

We are also confident that our brands are well positioned to take advantage of the improved consumer spending on apparel. We have strong brands that our consumers come to for trend right product and inspiring shopping experiences both on-line and in stores. We have swift sourcing capabilities and the ability to air product into country to chase consumer demand as it begins to build.

I am also personally confident that I will 'enjoy' plenty of challenges explaining our performance: be it vs. LY or LLY, or by channel, or by geography. There are a lot of moving pieces right now.

On that note, let me cover a quick housekeeping item. This year, when speaking to our results, we will largely focus on comparing results to FY'20. While we are starting the year more challenged than two years ago due to the ongoing impact of COVID-19 on stores, we believe this is the right comparison and measurement for our business performance.

Now, I will speak to the first quarter and a bit about full year FY'22.

It is important to note that COVID-19 is not only negatively impacting our store sales performance, it is also disrupting our inventory flows. We continue to experience delays and increased costs in bringing product into the U.S. and U.K from Asia. These delays impact our ability to replenish and deliver timely new receipts to all channels. We do believe these challenges will gradually moderate as the quarter and progresses.

We believe the first quarter will show a steady sales improvement vs. FY'20 as the quarter progresses. Right now, we believe first quarter total Company sales could come in low single digit positive vs. FY'20. This could be the result of Retail segment sales being up low single digits and Wholesale segment sales decreasing by low double digits. One of the biggest unknowns impacting Retail segment sales is when all of our European stores will be able to resume trading.

Based on our current sales performance and forecast, we believe our gross profit margins for the first quarter could be down several hundred basis points to FY'20. Deleverage in delivery and logistics expense resulting from the increased penetration of the digital channel to the total business could be the primary cause of this decline.

Please keep in mind, on a standalone basis, our digital channel is far more profitable than our store channel. Quarter-to-date, our store sales are meaningfully below levels in Q1 FY'20. Since store occupancy expense is largely fixed, reduced sales create considerable deleverage in the store results. When the channel P&Ls are combined, the increased penetration of the more profitable digital channel provides a significant benefit to store occupancy expense as a rate to sales. We believe this is likely what will occur in the first quarter. If store sales improve throughout the quarter and year, which we believe is likely, the opportunity for gross margin recovery increases.

Now moving on to 'SG&A'. Based on our current sales performance and plan, we believe 'SG&A' could grow in the low single digit range for the first quarter and in the mid-single digit range for the full year vs. FY'20. Our growth in 'SG&A' is primarily due to planned 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. The growth in these expenses could be partially offset by lower direct store controllable costs. As we have done in past quarters, our teams will manage 'SG&A' relative to actual sales.

We are currently planning our effective tax rate to be approximately 30% for the full year FY'22. We believe the first quarter effective tax rate could come in somewhat lower than our annual rate due to the timing of profits and losses.

Capital expenditures for the fiscal year are planned at approximately $250 million. The spend is primarily related to construction on a new distribution facility in North America in addition to the completion of our automation equipment in our new facility in the UK.

Our new North American facility just outside of Kansas City, Kansas, will take approximately two years to complete phase one. This facility will support the growth and expansion of our Retail segment business in North America by providing more efficient and faster inventory processing, as well as faster and more consistent delivery times to our stores and digital customers.

Lastly, we are planning on opening approximately 55 new stores and closing 21 stores this year. Our new store number is larger than in previous years due to the addition of FP Movement store growth as well as the availability of favorable lease terms on new stores.

The obvious question is, why open stores with the uncertainty around store traffic? The answer is the economics of our new stores are significantly favorable to our existing ones. Currently, we are successfully negotiating variable rent (also known as percentage rent) on most of our new stores. This provides reasonable protection against traffic fluctuations. Additionally, we are receiving significant capital reimbursements on many of our new or renewal locations making the capital investments in these new stores minimal. Lastly, our new stores are located primarily in secondary markets where traffic patterns are currently outperforming major metropolitan areas.

While our new stores have these benefits, many of our existing locations do not. We will need to negotiate better occupancy costs at these existing locations when leases expire, or we will be forced to close them. When I speak about the learnings we look forward to this year, a better understanding of where store traffic and volume will reset to once the virus retreats is obviously at the top of our list.

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.

Now, I am pleased to turn the call over to Dick Hayne, CEO of URBN.

Dick Hayne

Thanks Frank, and good afternoon everyone. Today, I'll discuss our current business trends, the year ahead and give an update on several of our growth initiatives. As a reminder, when I use the word 'comp' in reference to our current year sales, it will mean a comparison against FY'20 sales or double LY, not against last year since those results were obviously very distorted by COVID. We will use this double LY standard for the remainder of FY'22.

Let me begin with our current trends: as previously disclosed in our Q4 sales release, all three brands showed significant improvement in January versus what I would characterize as 'disappointing' holiday sales. Throughout January, sales strengthened as new inventory arrived.

Beginning in early February, this trend was interrupted by abnormal weather events that depressed store traffic. As more typical weather patterns returned to the US toward the end of February, store traffic and sales in North America showed meaningful improvement. This helped to drive mid-single digit positive Retail segment 'comps' for the month, with all brands in North America positive.

Meanwhile in Europe, virtually all our stores remain closed due to government mandates. Digital sales in Europe more than doubled and offset much of the store loss, but total Retail segment 'comp' sales in February decreased by high single digits in Europe.

Combining these factors, we believe total Company Retail segment 'comps' could be positive for the quarter. The magnitude of 'comps', however, depends on many factors including, when stores in Europe are permitted to re-open.

During Q4 and February, both the Anthropologie and Urban brands continued to benefit from strong Home sales. This, even though new Home inventory receipts from Asia were delayed by four weeks or more, as Frank discussed earlier. Compared to the prior year, current customer backorders for Home products are up over 350% and now exceed $20M. We expect the timeliness of inbound freight to slowly improve over the next several months which should help 'comp' sales as we ship backorders to customers, but we also believe freight costs will remain elevated for much of the year.

While Home products are selling briskly, performance within the all-important apparel category is spotty at both larger brands. Dressier apparel underperformed in January and much of February, while casual apparel was mixed, some classes selling well and others not. Obviously, COVID-related stay-at-home mandates impacted customer buying behavior. More recently, however, we're seeing signs of customer interest in 'going-out' type apparel beginning to emerge. We believe as vaccines become more widely distributed, new COVID cases continue to fall, and government restrictions begin to loosen, women will feel more comfortable venturing out and apparel demand will accelerate. The exact timing is hard to predict, but we believe it will coincide with spring weather.

Moving to Free People, this brand seems immune to the virus; their business has remained positive throughout the pandemic except for a brief period last March. Almost all Free People product categories enjoyed success in both January and February. This drove strong double-digit Retail segment 'comps' in both months. Positive outliers include casual apparel, shoes, and of course, FP Movement.

Movement is one of our most exciting growth initiatives. In Q4, new Movement customers grew by 138% and digital sales advanced by more than 150%. All channels – digital, retail, and wholesale posted strong gains, and that trend has continued into Q1. During the fourth quarter, we opened two more standalone Movement stores – Boulder, CO, and Coconut Grove, FL. Along with the first store that opened in Century City last October, these standalone stores performed nicely above plan in February.

This year we're excited to open an additional ten locations across the country. Given the abundance of available locations and favorable lease terms, we plan to increase that number next year. With Movement achieving outstanding results across all channels, including standalone stores, triple-digit gains in digital sales, high productivity in the 54 shop-in-shops inside Free People stores, plus a growing wholesale account base, we believe Movement is poised to grow revenues from just shy of $100M last year, to over a quarter billion dollars in FY'24.

Another exciting growth initiative is Anthro Living. This past year the Anthropologie team rebranded the home category as Anthro Living and delivered positive Retail segment 'comps' in all four quarters despite stores being closed or impaired. During the year, the Anthro Living digital customer base grew by over 60%. We believe the brand offers a unique aesthetic in this category and will continue to deliver outsized growth with the ability to more than double revenues and exceed a billion dollars in sales in the next five years.

Finally, I would like to make you aware of a marketing initiative we began testing in early February. It's a paid membership program we call UP. In exchange for an annual fee, UP provides membership benefits across our entire portfolio of brands. UP is designed to drive increased frequency, capture a greater share of wallet, improve retention, provide opportunities for greater cross-brand exposure and selling, and attract new customers.

We believe the ability to access benefits at all URBN brands for the price of one membership fee offers a key differentiator for our program. The test launched in two markets, Dallas, and Atlanta, and will run for six to twelve months depending on the rate of sign-ups and the speed of our learnings. We look forward to sharing more about the UP initiative on future calls.

Before closing, I know many of you saw our January announcement concerning management changes at the Urban brand. I want to congratulate Sheila Harrington on a well-deserved promotion to CEO of both the Urban Outfitters and Free People brands. Sheila started with Free People in 2002 as the head retail merchant in charge of opening the first Free People store. She has been instrumental in building this now iconic brand over the past 19 years. She's been responsible for driving positive 'comps' for 16 of the past 17 quarters and incubating the FP Movement brand. Right now, she's actively searching for a head merchant for the Urban brand in North America as Gabrielle Conforti has left URBN to pursue another opportunity. I'm confident Sheila will be successful in her new role, and besides maintaining positive quarterly 'comps' at Free People, will now help drive consistent growth at the Urban brand, as well.

In closing, I thank all brand and shared service leaders, their teams and our 19,000 associates world-wide. Back in March of 2020, when the pandemic first hit North America, we imagined that URBN would incur a very substantial loss for FY'21. Instead, we made a profit. The hard work, resiliency, and creativity of our teams, together with the cooperation from many of our partners around the world, made that happen, and I thank all of you. I also thank our shareholders for their continued support. That concludes my prepared remarks. Now for your questions.