INDITEX

FY2016 Results

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CONFERENCE CALL TRANSCRIPT

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Michelle Wilson Berenberg – Analyst
Adam Cochrane UBS – Analyst
José Rito BPI – Analyst
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Presentation

Operator

Good Morning Ladies and Gentlemen. Welcome to the presentation of Inditex Results for Fiscal 2016. The presentation will be chaired by Mr. Pablo Isla, Chairman and CEO.

This presentation will be followed by a Q&A session comprising two parts: The first part will be dedicated to questions received on the telephone, followed by those questions received through the webcast platform. Mr. Isla you have the floor.

Slide 3

Good morning to all the participants in this webcast conference call regarding INDITEX Results for Fiscal 2016.

I am Pablo Isla and here with me today are Ignacio Fernández, our CFO and Marcos López, Capital Markets Director.

Slide 4: 2016: Overview

2016 has been a year of very strong execution for Inditex globally.

Slide 5: 2016: Overview

We operate a global sales platform that fully integrates stores and online and offers huge growth potential. Our business model combines stores and digital seamlessly, and we are ready for the opportunities that this brings with current and new customers.

In 2016 Inditex had a very strong operating performance. We have achieved very satisfactory sales growth.

The year has been marked by strong cash flow generation, investment and increased dividend payments.

We finished 2016 with operations on 5 continents, through 8 concepts, 7,292 stores globally and online sales in the most relevant markets. We start 2017 with a unique platform that can access growth opportunities globally.

Slide 6: FY 2016 Overview

I would like to highlight some key lines of these results.

In 2016 Inditex continued expanding in a very strong way. Sales grew 12%. LFL sales increased strongly at +10% over a highly demanding comparable of +8.5%. We achieved positive LFL´s across all geographies and in all concepts in 2016.

New space in prime locations and online launches are on track. We are currently operating online in 43 markets, with a wide geographical coverage and rapid growth.

Cash flow generation was very strong. Funds from operations grew +13%.

Based on the performance of our business over the year the Board of Directors is proposing a 13% increase in the dividend to be paid in relation to these results.

2016 has been marked by very strong activity on many fronts. I would like to cover a number of initiatives carried out by Inditex.

Slide 7: Global fully integrated Store & Online sales platform

We are in a unique position as we enjoy a global sales platform that fully integrates stores and online as the best way to respond to the demands of our customers.

We operate a highly differentiated business model, with a central inventory position, distribution to all our stores globally at least twice a week and orders received by our customers between 2 and 48 hours.

Slide 8: Highly prominent and differentiated stores

Over Fiscal 2016 we have reinforced significantly the differentiation of our key global flagships with very visible store openings and enlargements.

Two key examples are the Zara global flagship at Shinjuku in Tokyo. The store comprises 3,000 square metres in a landmark location.

Slide 9: Highly prominent and differentiated stores

Last autumn we opened a global flagship for Zara at Plaza de Cataluña in Barcelona of 4,500 square metres.

Slide 10: With very prominent flagships for 2017 (Castellana Madrid)

New space in prime locations is set to grow over 2017 with highly prominent flagships.

A key example will be our global flagship of 6,000 square metres for Zara at Paseo de la Castellana in Madrid. This will be the largest Zara store in the world, in a unique location.

Slide 11: With very prominent flagships for 2017 (Opera Paris)

We are also reopening the global Zara flagship at Opera in Paris.

Slide 12: With very prominent flagships over 2017 (White City)

We are enlarging our store in White City London.

Slide 13: With very prominent flagships over 2017 (Dubai Mall of Emirates)

We will also enlarge our flagship at Mall of Emirates, Dubai.

Slide 14: With very prominent flagships over 2017 (Festival City Qatar)

We are opening our flagship in Doha Festival City in Qatar.

Slide 15: With very prominent flagships over 2017 (Zara Nagoya at Sakae)

We are also opening a flagship store in Nagoya.

Slide 16: With very prominent flagships over 2017

I would like to wrap-up this section with a very unique project: The Zara flagship in Mumbai at Ismail Building in the landmark Flora Fountain. This heritage building has been subject to total renovation and the Zara at 5,000 square metres will be the largest in the market.

Slide 17: Global online sales

Our strong store presence works perfectly in conjunction with our global online sales presence.

We believe that Inditex is in an excellent position to take advantage of global growth opportunities. We have strong potential to continue expanding profitably in the coming years.

Slide 18: Financial Summary

Let me now hand over to Ignacio who will present some of the key aspects of our financial performance and I will join you later for the Outlook section.

Slide 19: FY 2016

Thank you.

In Fiscal 2016 Inditex had a very strong operating performance.

Net sales reached 23.3 billion Euros, EBIT 4 billion Euros and Net Income 3.2 billion Euros.

Slide 20: Strong Cash flow generation

A key feature of 2016's financial performance is the strong cash flow generation and capital efficiency.

Funds from Operations increased 13% to 4.4 billion Euros.

Ordinary Capital Expenditure grew 4% to 1.4 billion euros while new space in prime locations increased 8% and online operations have been extended globally to 43 markets.

At the same time the dividend paid in 2016 increased 15% to 1.9 billion euros and the net cash position has grown 15% to 6.1 billion euros.

In summary Inditex continues to enjoy a strong financial position.

Slide 21: Sales

Starting with sales I want to tell you that Inditex's performance in the period has been very satisfactory with sales growth of 12%. The translation of sales in currencies different to the Euro deducted 3% from the reported figure.

Slide 22: New Space in prime locations globally grew 8%

Over 2016 Inditex´s new space in prime locations grew 8% to 4.4 million square metres. We have invested strongly in the optimisation of our stores through the introduction of new images, refurbishments and enlargements.

Slide 23: Global sales platform

The ongoing expansion of our Group has resulted in a global sales platform, with a presence in 93 markets on 5 continents, both in the northern and southern hemispheres.

Slide 24: Gross Profit

Regarding the Gross Margin we can say that we are satisfied with the evolution in 2016.

Gross profit has increased 10% to 13.3 billion Euros, resulting in a 57% gross margin on sales. We have sustained our commercial policies over the period.

Let me highlight that excluding currency fluctuations our gross margin on sales would have increased in 2016.

Slide 25: Tight control of operating expenses

Operating expenses are under control. They have grown 11% reflecting the strong LFL sales performance, the significant addition of retail space and the employee participation plan. This line includes all the start-up costs for new space, refurbishments and the rollout of online sales.

Slide 26: Flexible business model

Operating working capital remains negative as a result of the business model. The working capital evolution is in line with the performance of the business.

Slide 27: Concepts

I will now hand over to Marcos who will elaborate on the performance of the Inditex concepts.

Slide 28: Sales by concept

In terms of space addition and online launches, we are on track. Continuing with our global expansion we have opened stores in 56 markets over the period. Global online launches have continued at a very rapid pace.

Regarding the performance by concept in 2016 Zara continues to represent approximately 2/3rds of group sales, the younger concepts around 1/3rd.

Slide 29: Concepts

I would like to highlight the strong operating performance of the Group over 2016. Let me point out that in this period all Inditex concepts have achieved positive LFL sales growth and double digit EBIT margin and strong Return on Capital Employed.

Slide 30: Concepts

The younger concepts grouped together have also performed very well.

I would like to highlight that Bershka, Pull&Bear and Oysho have performed very strongly.

All concepts continue their ongoing online rollout.

Slide 31: Outlook

I will now hand over to Pablo for the Outlook section.

Slide 32: Global growth opportunities

In the coming years we will continue to invest in the expansion of our business across a number of markets, all of which offer attractive long term returns through our sales platform that fully integrates stores and online.

Inditex is present on five continents and in all the key markets demonstrating the Group´s global reach. We manage a diversified sales platform in 93 markets. The current base offers huge growth potential for the coming years.

Slide 33: Global growth opportunities: Europe

In Europe, we continue to see huge growth opportunities. It is an area of growth for all our concepts and we have a very strong presence in all the markets.

We see great potential to continue expanding profitably in Europe.

Slide 34: Global growth opportunities: Asia

Asia accounts today for 24% of Inditex’s sales. We enjoy a very strong position in all the key markets of the region. In 2016 Zara launched in Vietnam and Massimo Dutti launched in India.

We are following a multi-concept expansion strategy in Asia and we have an online presence in China, Japan and South Korea. In March 2017 we launched online in Singapore and Malaysia with Thailand and Vietnam to follow in the coming weeks.

We see strong long-term potential for Inditex in Asian markets.

Slide 35: Global growth opportunities: Americas

We also see strong growth opportunities in the Americas, with a number of attractive growth markets. In 2016 we launched in Aruba, Nicaragua and Paraguay.

We are following a multi-concept and an online sales strategy in the Americas.

We have a significant online presence in the United States, Canada and Mexico.

Slide 36: Global growth opportunities: Australia and South Africa

We have continued expanding Zara in Australia and South Africa over 2016, confirming the global reach of our business model.

In 2016 Zara launched in New Zealand and Zara Home launched in South Africa.

We will continue to add very significant stores in these markets over the coming years.

Slide 37: Global online sales

Inditex's online operations have seen very rapid growth in recent years. Our business model allows a swift expansion of our online sales globally.

Zara has built an online sales presence in practically all European markets, The United States, China, The Russian Federation, Japan, South Korea, Mexico and Canada, the world's main economies. The concepts also have an established online sales presence in Europe. Additionally, some of the concepts are present in the United States.

We will continue to roll out online sales progressively in all the markets in which we are present with stores.

Slide 38: 2016: All concepts online in Europe & Turkey

In 2016 we rolled out online sales for all the concepts across Europe and Turkey.

Slide 39: 2017: India

The next step will be the online launch of Zara in India in 2017.

Slide 40: Strong growth opportunities

We continue to see strong growth opportunities driven by our global fully integrated Store and Online model.

We are in a unique position as we enjoy a global platform that fully integrates stores and online as the best way to respond to the demands of our customers.

Slide 41: Store & Online: Spring Summer Collection

We continue developing new initiatives in a fully integrated way as seen in the launch of Zara's Spring/Summer Collection…

Slide 42: Store & Online: Join Life

… and the organic cotton collection Join Life.

Slide 43: Strong differentiation of store base

Over recent years we have worked intensively on the optimisation of our retail base.

We have opened more than 2,470 prime stores. We have also refurbished 1,882 stores with the new image and enlarged 763 global flagships, while absorbing 705 small units into neighbouring stores.

Over this period, 75% of total retail space has been subject to optimisation initiatives.

Slide 44: Strong Capital Efficiency

We will continue reinforcing the differentiation of our global flagships with very visible store openings and enlargements in prime locations.

We expect a lower capital expenditure requirement for expansion. We see capital Expenditure growing below space growth.

In the coming years we expect a significant addition of new space in prime locations annually in conjunction with an increasing contribution from organic growth and online sales.

Our growth profile remains the same with slightly different components and lower capital intensity.

Slide 45: FY2017 Outlook

2017 will be another year of strong expansion for Inditex.

We expect 320,000 square metres of new space in prime locations in conjunction with our global online sales rollout.

We plan to open between 450 and 500 stores and to absorb 150 to 200 small units into neighbouring stores.

We see Capital Expenditure for 2017 at around 1.5 billion euros.

Slide 46: 13.3% increase in dividend

Regarding shareholder remuneration the Board of Directors will propose at the General Shareholders Meeting a 13% increase in the dividend for Fiscal 2016 to 0.68 euros per share.

This means the dividend per share has increased 113% since 2010.

The total dividend payment in 2017 will come to 2.1 billion Euros.

Slide 47: FY2017 Outlook

Finally, let me tell you that Store & Online sales in local currencies, adjusted for the calendar effect of an extra trading day in February 2016, have increased by 13% from 1 February to 12 March 2017.

As you all know, the Spring/Summer season is influenced by the performance over the Easter period due to its significant sales volumes.

And this is all from us. We will be pleased to answer any questions you may have.

Questions & Answers

Operator

The first question today is from Anne Critchlow from Société Générale. Please go ahead.

Anne Cristhclow – Societé General - Analyst

My question is about the Americas. You talked about expansion opportunities and mentioned some South American countries. What is your view of the potential for expansion in the U.S, given a possible border adjustment tax or other trade barriers?

Pablo Isla - Inditex - Chairman & CEO

About the U.S. market, we continue seeing very strong opportunities for us in the U.S. market. Our approach to the market is a combination of this fully integrated approach between stores and online as you know. This fully integrated approach, and thinking about the stores, is the combination between the relevant flagship and high-street locations and very relevant openings and so in shopping malls. So we continue seeing strong growth potential for the U.S. market this year and in the coming years and we have not changed at all our plans about our development and expansion in the U.S. market.

Anne Cristhclow – Societe General - Analyst

Thank you.

Operator

The next question is from Andreas Inderst from Macquarie. Please, go ahead.

Andreas Inderst -Macquarie – Analyst

I have a question on your cash position. It increased sharply, the net cash to six billion. You pay a solid dividend, yet based on my forecasts we should see continued rise in net cash position if you keep the pay out as it is now. What's your take on the dividends going forward and the payout and what is the plan in terms of use of cash? Thank you.

Pablo Isla - Inditex - Chairman & CEO

Thank you. Iin terms of the cash flow that we generate, our first priority is to invest in the long term profitable growth of the company. And thanks to the cash flow generation we are able to combine this with what we consider to be an attractive and predictable shareholders remuneration policy. You have seen how we have been consistently increasing the dividend in the last few years more than 100% increase since the year 2010. Having in mind this global policy, each year the board of directors takes a decision about what dividend to propose to the shareholders meeting. With all these elements in mind, this year the proposal is to increase the dividend 13%, which is very much in line with what has been the net cash position increase, which has been 15%. So we are distributing 2.1 billion Euros to the shareholders in the form of dividends and our idea is to continue with this global policy and having in mind this global policy every year the board of directors needs to take a decision about what dividend to propose to the shareholder's meeting. But our first priority is to invest in the long term profitable growth of the company, and being able to combine this with an attractive and predictable shareholders remuneration policy. And this is what we have been doing during the last years, as we were saying during the presentation.

Michelle Wilson - Berenberg – Analyst

Ok, thank you.

Operator

The next question comes from Richard Chamberlain from RBC. Please go ahead.

Richard Chamberlain - RBC - Analyst

Thanks very much. I wanted to ask a question about pricing, please. We have seen in recent years a flatter trend in pricing between markets as a price harmonisation to some extent with Europe. And I just wondered if you think that process has now reached an end for Zara in other formats and if so, what the implications are for margins going forward. Thanks.

Pablo Isla - Inditex - Chairman & CEO

The first thing I would tell you is, as we were saying during the presentation, that during the year 2016, excluding currency fluctuation, our gross margin on sales would have increased. At the beginning of this year (2016) there was a significant currency impact. That is why at the beginning of the year 2016 we were saying as an estimation, stable gross margin in local currencies. And in local currencies our gross margin would have increased during the year 2016. If we think about the year 2017, what we can tell you always at the beginning of the year, we talk about a stable gross margin as our estimation for the year, of course, this year one may say it will be similar. What we can tell you is that the current exchange rates we do not anticipate at all a declining gross margin in fiscal 2017. And then, answering your question precisely, regarding prices, we are not touching prices all the time or every year. We have always a medium and long term approach in terms of our price structure. As you know, we take Europe as the average, then we have Spain and Portugal a little bit below because of historical reasons; a lot of markets more or less at the same level, and then two or three markets a little bit above. But globally, our price architecture is quite flat and our pricing policy is quite stable globally as a company. So, no big changes from that point of view and we are not obsessed with currencies here and there to move our prices. Always a medium and long term approach.

Richard Chamberlain - RBC - Analyst

Ok thanks and just related to that then, I guess that you are not seeing any impact on margin as yet from higher online competition or more of a move to free delivery, free returns from online players in the market. You do not think that is impacting Inditex's margin at the moment?

Pablo Isla - Inditex - Chairman & CEO

We are managing our company with this fully integrated approach between stores and online. We are not seeing any impact coming from that point of view. No, no.

Richard Chamberlain - RBC - Analyst

Ok thanks very much.

Operator:

The next question comes from Michelle Wilson from Berenberg. Please go ahead.

Michelle Wilson - Berenberg - Analyst

Good morning. I wanted to ask a question on the performance by division. Just noting that EBIT margin development for the likes of Zara and Pull & Bear was very resilient but we saw a bit of margin dilution in Zara Home, Massimo Dutti and Stradivarius. Is there any reason why there is a bit of weakness there? Is there any investment taking place?

Pablo Isla - Inditex - Chairman & CEO

Usually we always say it is better, because as we have eight different formats, it is always better to analyze all the brands different from Zara together, and year after year you see a very similar performance to the one of Zara. In any particular year because of the calendar of openings, because of comparables, because of different reasons there could be one, two brands over-performing and one or two brands underperforming. There is nothing really significant from that point of view. It is a normal evolution of the business and particularly depending on the brands when you see brands in which the absolute figures are small, a little change in the calendar of openings it could mean a change in the evolution of the EBIT. But globally we have, as you were seeing during the presentation, very healthy EBIT margins in all the different brands and very healthy return on capital employed in all the different brands.

Michelle Wilson - Berenberg - Analyst

Thank you and just a quick follow-up on one of the questions earlier. Is it possible to quantify for us the effects impacts on margins in the current year? You mentioned that gross margin would have been positive in the current year if it was not for the currency fluctuation. Are you able to quantify the effects and impacts of margins?

Marco Lopez – Capital Markets Director

I think that Pablo has mentioned that we are not anticipating any currency impact on the gross margin.

Michelle Wilson - Berenberg - Analyst

Sorry. For the year 2016, for the year end of January 2017?

Marco Lopez – Capital Markets Director

I think we mentioned what we really wanted to mention. If it were not for FX impacts, the gross margin would have increased.

Michelle Wilson - Berenberg - Analyst

Thank you.

Operator:

Next question comes from Adam Cochrane from UBS. Please, go ahead.

Adam Cochrane – UBS - Analyst

Good morning. Can you tell me the impact of the store absorption program that you are doing in terms of benefit to like for like or the overall impact on the business, please?

Pablo Isla - Inditex - Chairman & CEO

It depends on when the store was refurbished or enlarged. In the beginning it is not in the like for likes, but after two years it begins to be part of like for likes. So, if we take a five years period, three years of that would be, more or less, included in the like for like sales growth and the last two years would not be included in the like for like sales growth. So as with any other store, when we enlarge a store for us, in terms of how we account, it is like a new store. So at the beginning it is not included in the like for likes, but after two full years it begins to be part of the like for like sales figure.

Adam Cochrane – UBS - Analyst

So when you close a store, do you see a good sales uplift in the enlarged store?

Pablo Isla - Inditex - Chairman & CEO

Yes. Usually, if not, we would not continue doing it. So, we believe very much in this strategy of opening new stores, but also enlarging, refurbishing and improving the images of existing stores and absorbing small neighboring stores. It is something that is working in every market and that we are developing, and we will continue with this approach in the coming years.

Adam Cochrane – UBS - Analyst

So just to be clear, when you close the store, the sales transfer over to the new one, if you enlarge the store, then that goes out of like for like. But if you do not enlarge the store would that sales transfer be included within like for like?

Pablo Isla - Inditex - Chairman & CEO

If we do not enlarge the store, of course. But most of the absorptions have to do with enlargement of stores.

Adam Cochrane – UBS - Analyst

Thank you.

Operator:

The next question comes from José Rito, from BPI. Please go ahead.

José Rito - BPI - Analyst

Good morning. Just to confirm, because in the past you had a reference in terms of space growth for the coming years between 6 and 8%. We have a reference for 2017 but just to confirm that the previous reference of 6 to 8% is also to be maintained after 2017. Thank you.

Pablo Isla - Inditex - Chairman & CEO

Yes. This is the range of space growth that we are planning to have, not only in 2017 but also in the coming years, 6 to 8%.

Operator:

The next question comes from Warwick Okines from Deutsche Bank. Please, go ahead.

Warwick Okines - Deutsche Bank - Analyst

One, clarification on the guidance for gross margins that you gave, I think you said stable for the year ahead but then I thought I heard you say that a current exchange rates you don't expect it to decline at all in gross margin. Does that mean you are guiding towards the upper end of your normal stable gross margin range or did I mishear you?

Marco Lopez – Capital Markets Director

What we have said is very clear. We always guide towards stability in gross margins. In 2016 we have also mentioned that excluding currency effects the gross margin would have increased and what we are mentioning right now is that the current exchange rates we do not anticipate any, impact from currencies in the gross margin for 2017.

Pablo Isla - Inditex - Chairman & CEO

You can assume what you were saying. We always say that stable is minus or plus 50 basis points and for this year at current exchange rate we are excluding the minus part of the guidance.

Warwick Okines - Deutsche Bank - Analyst

Understood. Thank you. My question was around absorptions. Again, I think you did quite a lot more than you originally guided at the beginning of the year. You did 165 against your guidance of 100 to 120. Just interested beyond Spain, what markets you are particularly seeing these absorptions in?

Pablo Isla - Inditex - Chairman & CEO

It is spread all across the different geographies. Of course, there is the case of Spain, but if you analyze, there are a lot of markets in which you have absorption of smaller stores. So there is not any particular market to mention from that point of view. It is very spread all across the company. It is a global strategy for us.

Warwick Okines - Deutsche Bank - Analyst

Okay. Was there any particular reason why you did so many more this year than you planned? Was it just the availability of the deals to close stores?

Pablo Isla – Inditex - Chairman & CEO

Yes, it is more the second. At the beginning of the year, as you know, we always have around 70% of the new openings already signed, and then it is the evolution of the business during the year.

Warwick Okines - Deutsche Bank - Analyst

That's great. Thank you very much.

Operator

Ladies and gentlemen, we are now finishing with the telephone Q and A session to address the questions received through the Webcast platform. Thank you.

Operator 2:

We have had a number of questions via the Webcast platform. The first of which is: Last year you launched Massimo Dutti in India and this year you are opening a large flagship in Mumbai and launching Zara online. Do you see a large business opportunity in India?

Pablo Isla – Inditex - Chairman & CEO

Well, what we can say is that we currently have 21 stores in India with Zara and Massimo Dutti, and our idea is to continue expanding in this market. India is a very attractive market for us and in the year 2017 there are two relevant things for us in India. One is the opening of this Zara flagship in Mumbai. We were talking about this during the presentation; it is a 5,000 square meter store. It will be our largest store in India, and then the second element in the autumn/winter season will be the launching of our online business for Zara in India, so an attractive market, and we think, that with significant growth opportunities for us in the medium and long term.

Operator 2:

The second question on the Webcast platform relates to the Spanish market. Can you comment on sales in this market, please?

Pablo Isla – Inditex - Chairman & CEO

What we can say about Spain is that we continue being very active in the market. We were mentioning also during the presentation, talking about last year the opening here in La Coruña or the opening in Barcelona. Then, of course, for the next year we have this big flagship in Paseo de la Castellana in Madrid, which is a Zara, but we could say the same as big flagship of Massimo Dutti in Barcelona. So lots of things are going on with all the different brands, we continue very active in the market, we continue having very healthy sales growth. Of course, in Spain we are not increasing our space. Our space tends to be stable in the last few years. We have this policy of opening relevant stores, absorbing smaller stores. In fact, if you analyze our sales in Spain in a three years period, so from 2014 to 2016, we have achieved more than 20% sales growth and all of that is like for like sales growth, because we are not increasing our space. So, we continue being very active in the Spanish market and this is our approach thinking about the coming years.

Operator 2:

Another question is: Perhaps you could provide some color on the employee profit sharing plan.

Pablo Isla – Inditex - Chairman & CEO

Well this plan, as you know, the first year for the plan was 2015. Then this is the second year, 2016. We think it is having a very positive impact all across our company, and it is the idea of sharing with all our employees the positive evolution of the company. So that is why we have, the board of directors, has decided to extend the plan for another two year period: the years 2017 and 2018. So we think it is very relevant in terms of the commitment and to recognize the contribution of all our employees all over the world to the evolution and the performance of the company.

Operator

That concludes the Webcast questions.

Pablo Isla - Inditex - Chairman & CEO

Thank you very much to all of you for joining us today. And, of course, if you have further questions, we are ready to answer them through our capital markets department. Thank you very much.