

INDITEX

INDITEX
INTERIM HALF YEAR 2020

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Inditex Participants

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Conference Call Participants

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Geoff Lowery Redburn – Analyst
Rebeca McClellan Santander - Analyst
Chiara Battistini JP Morgan - Analyst
Warwick Okines BNP Paribas - Analyst
Aneesha Sherman Alliance Bernstein – Analyst

Introduction: Marcos López

Good Morning Ladies and Gentlemen. A warm welcome to the presentation of Inditex's Results for the Interim Half Year 2020. I am Marcos López, Capital Markets Director.

The presentation will be chaired by Inditex's Executive Chairman Pablo Isla. Here today with us are also our CEO Carlos Crespo and CFO Ignacio Fernández.

As usual, the presentation will be followed by a Q&A session starting with the questions received on the telephone and then those received through the webcast platform. Before we start we will take the disclaimer as read.

I'll now hand you over to Pablo.

Slide 4: FY2020 to date

Good morning to everybody and welcome to Inditex's results presentation.

Let me tell you that we have total confidence in our unique business model.

We continue developing the key lines of our long-term strategy: to extend our fully integrated store and online platform; to complete the digitalisation of the group; and to push forward the goal of increasing our level of sustainability.

I would like to start the presentation with an overview of fiscal 2020 year-to-date. Let me point out that we have seen a rapid recovery in operations over the course of the year.

Our Autumn/Winter season collections have been very well received by customers. As of today 98% of our stores are open and store sales have been recovering progressively. At the same time, it's certainly worth noting that online sales continue to experience outstanding growth in all markets.

As a result, Store and Online sales in local currencies from the first of August to the 6th of September were 11% below the demanding comparable of the previous year, marked by an increase of 8% from the 1st of August to the 8th of September 2019.

Slide 5: 2Q2020: Turning point

I would like to highlight that the Second quarter has marked a turning point in performance in 2020.

Over the Spring/Summer season Covid-19 has had a material impact on operations due to temporary stores closures and restrictions. Throughout this period, we saw outstanding progress in online sales.

Our supply chain has continued to operate normally due to the flexibility of the business model. Key features of our operations like the inventory integration have proven to be crucial during the season.

We have been driving efficiencies through the active management of operating expenses. The marked decrease in operating expenses in the period is a reflection of the efforts of everybody here at Inditex.

The second quarter of 2020 saw the recovery turning point, laying the foundations for a progressive return to normal trading conditions going into the second half.

At the beginning of the Autumn/Winter season practically all stores were open. We are seeing a continued improvement in in-store trading all the while online sales continue growing at a remarkable pace.

Slide 6: 2Q2020: Turning point

As you can see from this chart, a significant turning point was reached in the second quarter as the majority of stores reopened.

Slide 7: 2Q2020: Turning point

During the second quarter 2020 the Group's performance saw an inflection point laying the foundation for a return to normal trading conditions. The chart shows the monthly sales performance in the period versus last year.

Going into the second half of the fiscal year, sales trends have started to improve as stores have reopened. The strong trajectory of online sales has of course continued.

Slide 8: Online sales +74% in 1H2020

In the first half 2020 global online sales made outstanding progress.

This remarkable performance was greatly helped by our fully integrated business model, our single inventory position and the attractiveness of the product offer. Online sales grew +74% in the first half of 2020.

It is because of these features that today, Inditex's online operations enjoy sector leading growth rates and profitability.

The strong growth in online sales has continued going into the Autumn/Winter season.

Slide 9: Global store & Online sales in 1H2020

We have been seeing a progressive recovery in sales in the markets that have reopened stores. The different performance by geography depends mainly on the timing of the reopenings. Online sales continue to grow across the globe.

I'll hand you over to Ignacio now for the Financial Section.

Slide 10: Financial Summary

Thank you Pablo.

Slide 11: Interim Half Year 2020

As mentioned, the Covid-19 pandemic has had a material impact on our first half 2020 operations. Sales reached 8 billion euros in the period.

To minimise the impact, we have been actively managing our supply chain and inventory. The flexibility of our business model and the single inventory position has been pivotal in this process. As a result, gross profit reached 4.5 billion euros in the first half of 2020.

Over the period, we moved quickly to drive efficiencies by managing operating expenses in response to adjustments in sales volumes. Cost control has been crucial in the first half with many initiatives now in place.

Consequently, EBITDA in the first half 2020 reached 1.5 billion euros.

As a remainder, we charged 308 million euros to depreciation in the first quarter to complete the space optimisation process. Excluding this charge, both PBT and net income for the first half would have been +45 million euros and +39 million euros, respectively.

Slide 12: Second Quarter 2020

The second quarter of 2020 proved to be a turning point in the fiscal year, after which we saw a clear start to the recovery.

The active management of our supply chain and central inventory position have been instrumental in this process.

We have also acted rapidly on operating expenses to obtain efficiencies and adjust for sales volumes. A focus on cost control has been very important.

As a result, EBITDA reached 1 billion euros in the second quarter alone.

Slide 13: Sales

The sales performance has been marked by the timing of the temporary store closures and restrictions.

Online sales growth in the period has been very strong at +74%.

Slide 14: Gross margin

Gross profit reached 4.5 billion euros in the first half of 2020. The gross margin was 56.2%.

The gross margin evolution over the period is strongly linked to the high levels of flexibility enjoyed by our unique supply chain.

This is clearly illustrated in the inventory, which was 19% lower than the closing balance in the first half of 2019.

Slide 15: Operating efficiencies

Efficiency gains have allowed us to exercise a high level of control over operating expenses in the period. As you can see, operating expenses decreased a remarkable 21%.

All of the main components of operating expenses have shown good performance.

Slide 16: Depreciation

Depreciation and amortisation was 1.7 billion euros. This includes the full charge for the completion of the store optimisation programme in 2020 and 2021, announced back in June.

Slide 17: Financial results

The financial results line of the income statement includes the interest on lease liabilities of 65 million euros.

Slide 18: Flexible business model key to performance

The flexibility of the business model we run can be clearly seen in the evolution of working capital over this demanding period.

Despite the very material impact of lockdowns on sales, we have been able to use the flexibility of our supply chain to adjust the volumes. The single inventory position was pivotal to achieving this performance.

As a result, inventory fell 19% at the end of 1H2020 and demonstrates the flexibility of our business model. The closing inventory is considered to be of high quality.

These actions, in conjunction with the tight management of operating expenses helped to sustain the net cash position of 6.5 billion euros, an increase of 734 million euros over the end of the first quarter 2020.

Let me hand you over to Marcos now.

Slide 19: Concepts

Thank you

Slide 20: Store & Online Sales by concept

Over the first half we have continued with our expansion. We opened stores in 14 different markets. Global online launches have continued rapidly as you can see.

The weight of the different concepts on group sales remains broadly unchanged.

Slide 21: Sales by concept

Evidently, operations have been materially impacted over the first half of the year, but as mentioned by Pablo earlier, we saw a clear turning point over the second quarter.

We are seeing a progressive recovery across all concepts going into the Autumn/Winter season. The differences relate to each individual concept's geographic presence, location of stores and fashion profile.

Slide 22: Outlook

And now over to Pablo.

Slide 23: Global online developments

Thank you.

We continue to develop our 'global' online business. Online sales have been profitable and non-dilutive from launch. We foresee very strong progress in the run up to 2022.

This progress has been, and will continue to be, underpinned by a very high level of integration between physical stores and online. The benefits of this integration have been especially evident over the first half of this year.

Furthermore, we also expect to invest 1 billion euros in online capital expenditure for the period 2020 to 2022.

The ultimate aim is to accomplish full digitalisation of stores across the globe.

Online sales as a percentage of total sales are expected to continue rising over the long-term.

I'll now hand over to Carlos to comment on online and sustainability.

Slide 24: Online launch in Chile, Montenegro and North Macedonia

We continue furthering our global online reach with launches for Zara in Argentina, Uruguay, Paraguay, Peru, Bosnia-Herzegovina, Albania and Algeria over the first half of the year.

In August, Zara launched online sales in Chile, Montenegro and North Macedonia. In September, Zara has launched online in Tunisia and Andorra and will launch in Costa Rica, Guatemala, Honduras and Nicaragua before the end of the month.

Slide 25: Sustainability & Circular economy a key part of the strategy

Thank you.

As you know, sustainability has been a key part of our strategy for many years. Our commitment to a circular economy is best illustrated in these 5 main areas.

- The sustainability of the supply chain
- The use of renewable energies
- The commitment to sustainable fabrics
- The conversion into eco-efficient stores
- And a Zero-waste and recycling policy

We are happy to tell you that we're making good progress on all these initiatives. Now, I'll hand you back to Pablo.

Slide 26: Highly prominent and differentiated stores: Zara Paris

Thank you.

We continue to reinforce the differentiation of our stores by adding highly visible units. Our goal is to operate high quality, digital, ecoefficient stores in conjunction with a global online platform in order to provide a unique customer experience. Through these initiatives we are expecting increased profitability and lower capital intensity going forward.

A good example is the enlargement of the Zara store in Paris at Pont Neuf.

Slide 27: Highly prominent and differentiated stores: Zara Paris

This project includes a total refurbishment of the interior around a visually appealing central stairway.

Slide 28: Highly prominent and differentiated stores: Zara Berlin

The enlargement of the Zara store in Berlin at Tauentzienstrasse.

Slide 29: Highly prominent and differentiated stores: Zara Berlin

With an additional floor and new sustainable materials.

Slide 30: Highly prominent and differentiated stores: Zara Moscow

The enlargement of the Zara store in Moscow at Kusnetsky Most...

Slide 31: Highly prominent and differentiated stores: Zara Moscow

...with double fronted new interiors overlooking the pedestrian area.

Slide 32: Highly prominent and differentiated stores: Zara Beijing

...and a key project will be the relocation of the Zara store in Beijing at Wangfujing next month. This store will be the largest in Asia and one of the most technologically advanced stores in the whole group.

Slide 33: Unique business model; Global fully integrated Store&Online

In summary, we aim to further develop our unique business model by continuing with the global rollout of our fully integrated store and online platform.

Slide 34: Zara Woman A/W Collection

A good example of seamless store and online execution can be seen in the Zara Woman Autumn/Winter Collection.

Slide 35: Zara Man Bauhaus collection

the Zara Men Bauhaus capsule collection.

Slide 36: Zara Kids Naturales collection

Zara Kids Naturales collection.

Slide 37: Zara Jo Loves

The new Zara fragrances created by Jo Malone CBE.

Slide 38: Zara Home: Timeless Interiors

Zara Home's Timeless Interiors collection.

Slide 39: Massimo Dutti Limited Edition

Massimo Dutti's Limited Edition collection.

Slide 40: Bershka + NBA collection

Bershka's NBA capsule.

Slide 41: Pull&Bear Teen Collection

The Pull&Bear Teen collection.

Slide 42: Stradivarius STR collection

The Stradivarius STR collection.

Slide 43: Oysho Comfortlux

Oysho's Comfortlux collection and...

Slide 44: Uterqüe Official

...The Uterque new Official page on Instagram.

Slide 45: Dividend

And finally, the ordinary dividend for full year 2019 of 35 cents per share will be paid on the second of November 2020.

Inditex's dividend policy of 60% ordinary payout and bonus dividends remains in place.

As you all know the remainder of the bonus dividend (78 cents per share) will be paid in calendar 2021 and 2022.

Slide 46: Interim Half Year 2020 Results

Thank you for attending. That concludes our presentation for today. We'd be happy to answer any questions you may have.

Please go ahead Operator.

QUESTIONS & ANSWERS

Operator

The first question today comes from Richard Chamberlain, of RBC. Richard, please, go ahead.

Richard Chamberlain - RBC - Analyst

Thank you very much, just got a question on the online sales performance. Obviously, very strong in the first half and helping to offset store closures, but I wondered what kind of boost, what positive effect you'd seen from lower product returns in the first half? Would that be a material... online sales growth rate? Thanks.

Pablo Isla - Inditex – Executive Chairman

Well, thank you. The first thing I would like to tell you is that, as you were saying during the presentation, that we are very satisfied with online sales growth during the first half. I think it shows the strength of our online proposition and the strength of our business model with this single inventory position between stores and online. But when we see that we have 74% online sales growth, and as you know in Zara in general, but in Zara in particular, it's through our own webs and apps all across the world, you see how strong our online proposition is. So, thinking about the future, thinking about the medium term, I think we can say that of course we are a world leading online global retailer, at the same time as we have this full integrated approach between stores and online. And it's unbelievable, the effort made by our commercial teams. You cannot imagine, because of course there were a lot of restrictions, about how we could... well, first of all thinking about the product for sure, you see the colour of the presentation with these sophisticated dresses, I mean the effort made by the commercial teams and particularly if we think about the online teams, it is exactly the same, with all the limitations about the possibilities about taking the pictures and to be able to see this, so significant rate of growth, and in terms of customer deliveries. Also, you must keep in mind that during the period in which the stores were closed, something that for us is very important which is in store delivery, in store returns, was not possible. So, the effort has been unbelievable. So, what we can say is that we are very, very satisfied regarding all this effort from our commercial teams, first regarding the product, second regarding online, well, then, I would say also regarding the stores as soon as we were able to reopen the stores in the different markets, this is exactly the same. All our teams in the different countries, the way we have gone through this process of reopening and in terms of customer service and everything, it has been unbelievable. Well, now, answering your question, I would say that there's nothing very relevant, different from the usual what you are saying, so this online sales growth is a combination of existing customers and many new online customers, which we think is something very positive thinking about the future, and in terms of the online patterns regarding returns, there's nothing very materially different to what the usual pattern is.

Operator

The next question comes from c, of Société Générale, please, go ahead.

Anne Critchlow – Société Générale - Analyst

Good morning, thank you. What percentage of online orders at, say, Zara are now fulfilled from store inventory, please?

Pablo Isla - Inditex - Executive Chairman

Well, this figure, I would say this idea of single inventory positions, this idea of being able to use also the store's inventory for the online orders is something that is very meaningful and very relevant for us. But to think about a figure here, it could be even confusing, because it changes a lot depending on the moment in the season. What is key for us to have this possibility and particularly during the first half, it has been more relevant because we have seen a significant part of the first half in which the stores were closed, so that is why we have also been able to achieve this levels of sales, because we were able to use the inventories that we had in the stores. So, what I would say is that this single inventory position is something very relevant, and it is becoming more and more relevant, but it is not really very meaningful to give a figure, because it changes a lot, depending on the different moments of the season. But, what is very relevant for us is to have this possibility for us, in order to have a better offer for our online customers.

Operator

The next question comes from Geoff Lowery, of Redburn, Geoff please, go ahead.

Geoff Lowery – Redburn - Analyst

Good morning team. You've achieved remarkable things in the first half around operating expenses and around inventory. If we turn to the future and let's imagine that your sales recovered their 2019 level, would your OPEX base and your inventory be lower or higher than in 2019.

Pablo Isla - Inditex – Executive Chairman

It would have a lot to do with the global evolution of sales. In terms of inventory levels, as you know, of course, at this closing we are minus 19% in terms of the global inventory, but if you think about the year 2019, we were also decreasing the inventory during the whole year. So, thanks to this fully integrated approach, thanks to this single inventory position, we are able to run our business with even less inventory, and this is an effort that we are developing in the company. We began in the autumn-winter season, 2018, and we will continue with this effort, with this full integration, single inventory position. This could be always a trend that inventory would always grow below sales. But, I mean, it depends on how relevant growth in sales is. And in terms of costs, well, we can say that during this first half also, we have made big efforts in terms of management of the different lines of costs, of course rental expenses, personal expenses, other operating expenses, structural costs, every line of costs. You know that we have a significant part of our costs which are variable, around 50% of our cost base is variable, and then we will always continue managing costs in a very strict way, this is a key element in the way we approach the management of the company, but of course it also has to do with the evolution of sales. But, globally, we think we can be in normal conditions, year after year, we will be able to run the company with less inventory, as a proportion of sales, and with the cost efficiencies, also thinking about costs as a proportion of sales.

Operator

The next question comes from Rebecca McClellan of Santander. Rebecca please, go ahead.

Rebeca McClellan - Santander - Analyst

Yes, good morning. It just on the online acceleration that we saw in the second quarter. Does that make you review in your mind the store optimization program that you set out with the First Quarter results?

Pablo Isla - Inditex - Executive Chairman

Well, I think what we announced in the month of June makes a lot of sense, and what we are focused on now is to implement what was announced in the month of June. And we are not thinking about changing or reviewing things on a quarterly basis because of this or that. What I can tell you is that we believe very much in what we are doing and what I think is very remarkable about this first half is that we have seen how strong our online proposition is. When you see globally 74% online sales growth coming from a significant base, so it is not 74% coming from a low base, but coming from a significant base, we can see how strong our online proposition is with all the elements involved in that online proposition.

Operator

The next question comes from Chiara Battistini of JP Morgan, Chiara please, go ahead.

Chiara Battistini - JP Morgan - Analyst

Hallo, good morning, thank you for this email question. It would be on gross margin, if you could expand please, on the drivers behind the gross margin performance, thank you too? And whether you could confirm that actually Forex was a significant head winning Q2, so on an underlying basis you actually had positive developments in the gross margin net effects? And in this context, also, how should we be thinking about the gross margin evolution in the second half of the year, please?

Pablo Isla - Inditex - Executive Chairman

Well, regarding the gross margin, what I can tell you is that we are of course satisfied with the evolution of the gross margin and the main driver behind this gross margin is the execution of our business model, the flexibility of our business model, disability, if you remember when we were closing the first quarter, our inventory was already down compared to the previous year, so that is what is very remarkable, the ability that we have to run the company with a very low level of inventory, and then of course this means that we don't need to make significant discounts or promotions during the season. I would say this is the most remarkable feature about the gross margin. Thinking about the full year, we are thinking about a stable gross margin for the full year. You know that for us stable is plus or minus 50 basis points and in particular we would be thinking about a positive gross margin in the second half, but I prefer, Marcos, you can elaborate a little bit more and also about the currency impact.

Marcos López - Inditex

Yes that's right Pablo, in the sense that I think that in the management of the supply chain is what we find, the very good behavior of the gross margin of the first half. As Pablo mentioned, we expect it to be stable for the year, but positive over the second half, where you have different components. The first one is that you see the inventory position is minus 19%, so we are managing the supply chain very, very tightly. It's true that you will have some FX pressure in terms of presentation, because obviously in the

first half you've seen that the currency impact on the top line has been 100 basis points, and we expect probably 250 for the full year, and this will have some presentation, you know, impact on the gross margin and then you have to bear in mind that in Q4 last year we had made a provision, so you also have some comp. favourable on that side, so all in all, positive gross margin for the second half, probably stable for the year.

Operator

The next question comes from Warwick Okines of Exane BNP Paribas, Warwick please, go ahead.

Warwick Okines – Exane BNP Paribas - Analyst

Good morning everybody. Back on inventory, if I may? Having a very low level of inventory, as you've reported, have you actually had any product shortages at all, or do you feel like you've optimized the inventory level? And, perhaps just related, has the inventory that you took a provision on at the end of last year now all been cleared? Thank you.

Pablo Isla - Inditex - Executive Chairman

Well, yes, sure. It's mainly the flexibility of our business model, the ability to run the company with less inventory and we have not seen any significant problem regarding production or manufacturing. We want to operate our company with a lower level of inventory. We think it's very healthy, we really think it's the approach, even in this beginning of the season with minus 19% inventory level, the trading update is minus 11%, show it shows how healthy the inventory position is. You only have to look at any of our stores or to have a look at our webs and apps of the different brands and you can see how unbelievable the product is that we now have that we are offering now to our customers. This is applicable to all of our brands, so as I was saying at the beginning, it shows the strength of the business model, and also the strength of our commercial teams in all the different brands and in all the different countries around the world.

Operator

The next question comes from Aneesha Sherman of Bernstein, Aneesha please, go ahead.

Aneesha Sherman - Bernstein - Analyst

Hi, good morning. We've seen in the European apparel sector over the last few months that centre city store locations have performed far worse than shopping centre or suburban locations. Can you comment on whether you have seen a similar trend within your portfolio and how does that influence your strategy of opening these big centres for relocation for Zara, like some of the ones you showed in your presentation today? Thank you.

Pablo Isla - Inditex - Executive Chairman

When you run a company you should never take medium and long-term decisions because of some short-term impact of something external to the company, so this is the first thing I could mention. When you are running a company, you are thinking always not only in the short term, but also in the medium and in the long term. Having said that, we prefer not to elaborate very much on this or that particular type of store. What is very, very meaningful is that recovery that we are seeing in our sales globally. So, as we were saying during the presentation, store sales tend to recover progressively, and at the same time we have very strong online sales growth utilizing our single inventory position which is key for us. We believe very, very much in this approach. Globally, what we can say is that you must not forget last year, in the first five weeks of the second half, the comparable period to the one that we are presenting

right now with the trading update, sales growth was plus 8%. This means that our level of sales is very much in line with 2018. Even with everything that is going around in the world in many different countries, as you know when you read the news. I think that the most remarkable features in my opinion is the strength of the business model, the strength of our commercial teams, and also the strength of our online proposition.

Operator

Thank you very much. We are now finished with the telephone Q&A session, to address the questions received through the webcast platform.

James O'Shaughnessy

We've had a few questions on the webcast platform, the first of which, Pablo, is: How is Zara Home doing in the countries it's been launched on the Zara website?

Pablo Isla - Inditex - Executive Chairman

We began with this approach last year, when we launched Zara Home on the Zara webpage in the UK. Earlier this year we did the same in Belgian, Poland, and Holland. Last week, we launched in Germany, and we are planning China and Japan for later this year. This is an ongoing process and we can tell you that we are very encouraged by the evolution. At the same time, we are introducing some Zara Home corners in some Zara stores. This will be the case in Beijing, the store we were mentioning at the beginning, and it will also be the case in Nagoya, a very relevant store in Japan. So, we believe very much in this approach and particularly online. Now we have it in five different markets, very relevant markets, and we're planning during this year to extend it to China and Japan. So globally, we think it's a very good approach, introducing Zara Home progressively in the different markets and the Zara Home collection inside the Zara webpage.

James O'Shaughnessy

From what I can see, most of the webcast questions were covered during the presentation Q&A session. Last one would be:

Can you comment on the performance of recent online launches please?

Pablo Isla - Inditex - Executive Chairman

We mentioned during the presentation that we want to have a global online presence at the end of this year, and we have been very, very active, launching online in different markets in which we were not yet present. In every market in which we begin our online operations it tends to be satisfactory. Recently we launched in Chile and Argentina. In Argentina, for example, we have 11 stores, 10 of them in Buenos Aires, but we have had many orders from other parts of the country. This idea to continue developing our online presence in the markets in which we were not yet present is also something relevant for us and our plan as you know is to have this global online presence at the end of this year.

James O'Shaughnessy

I think that concludes the webcast questions, thank you.

Marcos López - Inditex

Thank you very much, this concludes today's Q&A session. Now please let me hand over to Pablo for the closing remarks.

Pablo Isla - Inditex - Executive Chairman

Well thank you and of course as we always say, any additional questions you may have, we are ready to answer through our Capital Markets Department, thank you very much for joining us during this conference call.
