URBAN OUTFITTERS, INC.

Second Quarter, FY'16 Conference Call
August 17, 2015

Participants

Richard A. Hayne, Chief Executive Officer
Frank Conforti, Chief Financial Officer
David McCreight, CEO, Anthropologie Group
Margaret Hayne, CCO, URBN & President, Free People Brand
Ted Marlow, CEO, Urban Outfitters Group
Trish Donnelly, President Urban Outfitters North America
Azeez Hayne, General Counsel
Barbara Rozsas, Chief Sourcing Officer
Calvin Hollinger, Chief Operating Officer
David Ziel, Chief Development Officer
Dave Hayne, COO, Free People Brand
Oona McCullough, Director of Investor Relations

Good afternoon, and welcome to the URBN second quarter fiscal 2016 conference call. Earlier this afternoon, the Company issued a press release outlining the financial and operating results for the three and six month period ending July 31, 2015.

The following discussions may include forward-looking statements. Please note that actual results may differ materially from those statements. 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.

We will begin today's call with Frank Conforti, our Chief Financial Officer, who will provide financial highlights for the second quarter. Dave Hayne, Chief Operating Officer, Free People Brand will provide a brief update on the Free People brand. Richard Hayne, our Chief Executive Officer, will then comment on our broader strategic initiatives. Following that, we will be pleased to address your questions.

As usual, the text of today's conference call will be posted to our corporate website at www.urbanoutfittersinc.com.

I'll now turn the call over to Frank.

Frank Conforti, CFO

Thank you Oona and Good afternoon everyone.

I will start my prepared commentary discussing our recently completed fiscal year 2016 second quarter results versus the prior comparable quarter. Then I will share our thoughts concerning our current quarter.

Total Company sales for the quarter increased by 7% to a second quarter record of $867 million. This sales increase was driven by a 4% retail segment comp, a $15 million increase in non-comparable sales, including the opening of 4 net new stores and 21% growth in wholesale sales. Please note that currency translation negatively impacted our sales growth rate, by approximately 165 basis points for the quarter.

Within our retail segment 'comp' the direct-to-consumer channel continued to outperform stores posting positive gains driven by increases in sessions, average order value and session conversion. Negative 'comp' store sales, resulted from decreased transactions and units per transaction, partially offset by higher average unit selling prices.

By brand, our retail segment 'comp' rate increased by 14%, 4% and 2% at Free People, Urban Outfitters and the Anthropologie Group, respectively. This marks the third quarter in a row all brands have posted positive retail segment comp sales growth, the 13th quarter Free People has posted double-digit comp gains and the 12th quarter in a row Anthropologie has posted positive comp sales gains. Our URBN Retail Segment Comp was strongest in May followed by June and July which came in fairly consistent with each other.

Free People Wholesale delivered another strong quarter as sales grew 21% to $72 million. These results came from double-digit sales growth at department stores partially driven by the success of our category expansion, namely Intimately Free and Free People Shoes.

Now moving back to total URBN results, gross profit for the quarter was up 5% vs. the prior comparable quarter to $318 million. Gross profit rate, declined by 71 basis points to 36.7%. The decline in gross profit rate, was primarily due to higher delivery and fulfillment center expenses.

The deleverage in delivery and fulfillment center expenses was partially due to the increase in direct-to-consumer channel penetration to total sales, as well as the incremental costs associated with the transition of the South Carolina fulfillment center to Gap, Pennsylvania. We are proud to share that our transition has gone extremely well. All three brands' direct-to-consumer businesses have been completely moved to our new facility which is now up and running. The expenses related to the transition have come in better than expected, and we believe only negatively affected the second quarter gross profit margin by approximately 40 basis points, much less than we originally planned. We are still forecasting approximately 25 basis points of incremental expense in the third quarter related to the transition but the overall expense and deleverage for the year is trending lower than what we had originally planned. A big congratulations and thank you is in order to our Shared Service teams for their hard work and extraordinary execution.

Total ‘SG&A’ expenses for the quarter increased by 8% to $214 million. Total ‘SG&A’ as a percentage of sales, deleveraged by 29 basis points to 24.7%. This minor ‘SG&A’ deleverage, was partially due to increased marketing expenses, which were used to drive higher direct-to-consumer traffic.

Operating income for the quarter decreased by 1% to $104 million, with operating profit margin deleveraging by 100 basis points to 12%.

Net income for the quarter was $67 million or $0.52 per diluted share.

Turning to the balance sheet, inventory increased by 6% to $384 million. The growth in inventory was primarily related to new and ‘non-comp’ stores as well as the Wholesale Segment. Comparable retail segment inventory, decreased by 2% at cost, while decreasing 7% in units. The decrease in retail segment comp inventory is due to improved inventory planning and control as the business continues to works towards managing to a lower weeks of supply.

We ended the quarter with $339 million in cash and marketable securities. During the second quarter, the Company repurchased and retired 6.6 million common shares for approximately $236 million. We now have 15.2 million shares remaining on the most recent Board of Directors’ authorization to repurchase shares.

On July 1st, we entered into a 5 year $400 million Asset Backed Revolving Credit Facility. This Facility gives us additional flexibility to use more cash strategically when appropriate. We utilized $115 million of this line during the second quarter to fund some of the share repurchases previously discussed.

As we look forward to the remainder of fiscal year 2016, it may be helpful for you to consider the following:

We are planning to open approximately 32 new stores during the year. By brand, we are planning approximately 4 new Urban Outfitters stores in North America, 13 new Anthropologie stores globally, including 1 new European store, and 15 new Free People stores in North America.

Our gross margin rate for the third quarter could increase versus the prior year. This growth could be driven by meaningful improvement in the Urban Outfitters brand’s maintained margin if their product performance and inventory management continues to progress favorably. The overall URBN rate improvement could occur while the Anthropologie and Free People brands maintained margins normalize down from their near record setting performances from a year ago to rates more similar to where they landed for the second quarter this year.

With that said, please take note that thus far in August, for all brands, our direct-to-consumer business has posted strong gains consistent with the second quarter, while our store sales have started out slower than what we planned and where we finished the second quarter. There are many factors that could be impacting our store performance and there is too little data at this time to draw any solid conclusions.

Based on our current plan, we believe 'SG&A' could grow at a high single-digit rate for the year with the third quarter growth rate looking fairly similar to what we recorded for the second quarter. This increase would be driven by DTC investments related to marketing and technology and selling support investments to support our new store growth.

As I noted earlier, the effects of foreign currency translation resulted in an approximately 165 basis point reduction to sales and an approximately 30 basis point reduction in operating profit. If today's rates held constant, and all else in the business held constant, such as shares outstanding and planned profit rates, we believe foreign currency translation could negatively affect our earnings per share by approximately 3% for the full year fiscal 2016. This would be based on our current businesses in the Canadian and European Markets.

Capital expenditures for fiscal year 2016 remain planned at approximately $140-150 million driven primarily by new stores and the completion of our new east coast fulfillment center.

Finally, our fiscal year 2016 annual effective tax rate is planned to be approximately 36%.

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 it is my pleasure to pass the call over to our Free People Brand Chief Operating Officer, Dave Hayne.

Dave Hayne, COO, Free People Brand

Thank you Frank, and good afternoon everyone. It's a pleasure to be speaking with you today. I'm excited to provide an update on the positive momentum at Free People in the second quarter.

Last year on this call, we started off by discussing a record-setting quarter, and I'm very pleased to do the same today. The Free People brand achieved a consolidated second quarter revenue record with a 20% top line increase over last year. These results were driven by a strong retail segment comp of 14%, and continued robust growth of 21% from the wholesale segment. This performance is even more exciting when viewed on a two-year basis, where second quarter revenue has grown by nearly 60% since fiscal 2014. Certainly an achievement of which all of our teams can be proud.

Strong product is the lifeblood of our business, and our design and merchant teams have consistently delivered compelling assortments that have repeatedly brought our customers back to the brand. And this Spring was no different, with many product wins to speak of. The customer continues to vote for our dress collection, with our strategy of expanding into party dresses providing a very healthy boost to the business. Our intimates collection has outperformed expectations in all channels, and our own-label shoe assortment saw significant gains in the quarter. Our activewear line, FP Movement, continues to impress us in the direct-to-consumer channel, making us even more excited to launch Movement to the wholesale market this fall for spring delivery. Our teams look forward to developing these concepts further, as well as exploring new category expansions in the future.

Moving to the wholesale channel, the team closed July with their single strongest sales month ever, and enter the back half with future bookings on pace with the current trend. Our department store partners had success across both their bricks and digital storefronts, with particular strength coming from our expansion categories. In fact, our expansion categories drove over a third of our total wholesale growth in the quarter, with success across both our department store and specialty store partners. Our four-pronged domestic strategy has been working for us: 1) invest in shop-in-shops in key department store doors, 2) offer replenishment programs to key accounts, 3) open expansion classes to existing accounts, and 4) onboard new accounts to both our core collection and expansion categories. This has provided a successful framework for developing our legacy domestic business, and we see room to continue this momentum.

Moving overseas, our wholesale team now supports over 300 global accounts with over 500 doors in 35 countries. Our relationship with I.T in Hong Kong continues to grow, with 3 new shops opened this spring, and a new department store relationship in Mexico offers new potential for the brand closer to home. We've seen particular strength in Europe, where our London team has doubled their business by improving operational execution, and developing domestic relationships such as our partnership with ASOS, and our two new Paris shop-in-shops in Galeries Lafayette. Additionally, our existing London presence in Selfridges recently expanded to a 400 square foot shop-in-shop, and this location is already the most productive we have globally. The team has also partnered with new distributors in Spain, Italy and Germany which helped to open 40 new specialty accounts in those countries in the quarter.

Alongside these wholesale developments, our retail team recently celebrated the opening of our first self-operated shop in London, a pop-up boutique on King's Road which will remain open into next year. Although only a small space, many of the operational complexities of opening stores in a new market have now been overcome by the team, and we're excited that the stage is now set for permanent stores in the UK and Europe in the years ahead. More definitively, we expect to open at least one permanent store in London in the first half of next year.

On the domestic front, our retail team drove record second quarter sales, and successfully opened 3 new stores in the quarter, following 4 new stores in Q1, bringing the current count to 108 total stores in North America. Additionally, later this fiscal year, we plan to open 9 new or relocated stores which average approximately 3,700 selling square feet per store, the largest of which, a relocation in Denver's Cherry Creek Mall, will total 5,300 selling square feet, over 3 times larger than our current store in the center, with plenty of room to support our successful category expansions such as intimates, shoes, and movement, in addition to our core collection and accessory assortments.

Not to be overlooked, we also completed a significant expansion of our Rockefeller Center store, more than doubling our selling space to nearly 6,500 SSF. This prominent store is now able to carry the widest assortment in our fleet, including shoes, party dresses, movement, and even a small home capsule. We couldn't be more pleased with the new store presentation, and initial reaction to the broader product assortment has been very encouraging. Our larger format store initiative is now well underway, and we're eager to learn from, and develop, this critical area of our brand's future growth.

Moving online, our direct-to-consumer business experienced very healthy growth in the quarter, with our customer base increasing 37% alongside a nice bump in conversion rate. Our domestic growth outperformed the total growth, as we experienced a noticeable slowdown in our international DTC growth rate which we believe is primarily due to currency fluctuations against the US Dollar. Despite these challenges, our localized UK and China online businesses generally outperformed other global markets, with China in particular showing nice acceleration against last year's growth rates. We believe this is just more proof to the importance of website localization.

As has already been mentioned, the wider URBN team successfully migrated our fulfillment operations to our new Pennsylvania facility. It's hard to overstate just how impressive this new building is in person, and it's also hard not to be impressed with just how flawlessly the transition went for all of our brands. On behalf of all of our brands, I'd like to congratulate all of the shared service teams supporting the design, build and transition on a job very well done.

Meanwhile, the mobile migration we've been witnessing in DTC has continued, with mobile devices now accounting for over 55% of our visitors and nearly 30% of our sales. To better support our ecommerce future, and better position ourselves for the new mobile era, the Free People team and our shared service partners have been hard at work building the future web platform for all of our brands. When our new platform launches in the back half of this year, we expect a faster shopping experience, improved functionality, broadened FP Me capabilities, more seamless mobile presentations, and generally a more robust foundation from which to build the shopping and experiential platforms which will be at the core of our brands and businesses for years to come.

I cannot talk about the core of who we are without also saying a word about the creative process. The Free People brand has been a success with customers because we endeavor to infuse creativity into everything we do…be it product design and imagery, catalog shoots, editorial content, store environments, marketing videos or local brand events. Whatever it be, the creative teams that touch these areas are truly the essence of who we are as a brand, and it's this sentiment that we aspire to leave fresh in our customer's mind, with the hope that she recalls us favorably in the future.

Thank you very much for your time; I will now turn the call over to our CEO, Dick Hayne.

Dick Hayne, CEO

Thank you, Dave. Good afternoon everyone.

Amazing, is the word that comes to mind when I hear the Free People story. Thirteen consecutive quarters of double-digit 'comp' sales growth – it's a remarkable story and a tribute to the extraordinary performance of the Free People team – congratulations to Meg, Dave, Sheila, Krissy and their teams. Given the many new initiatives including international expansion and new product category introductions, I believe the brand has the opportunity to continue that growth. However, after many years of strong 'comp' store increases, the Free People stores are operating at an extremely high level of productivity, so I believe that future top line growth for the Free People brand will likely come less from 'comp' store sales increases and more from opening additional and larger stores, and from expanding their other two channels of distribution.

Let me now discuss second quarter results at our other two brands, first Urban Outfitters. Speaking on last year's Q4 conference call, Trish Donnelly said one of our biggest priorities is to re-establish positive sales momentum. I'm pleased to report the brand recorded a healthy 4% retail segment 'comp' with the North American group outperforming its European counterpart.

However, the 4% 'comp' in Q2 only tells part of a very positive brand story. Importantly, the productivity gain was driven by a high, single-digit increase in regular price sales. Year-over-year increases in both conversion and average transaction value drove the 'reg' price increase and demonstrate the willingness of the Urban customer to buy at full price when we provide her with compelling product and an exciting experience. As in the first quarter, six of Urban's eight major product categories delivered positive, regular price 'comps' including the all-important women's apparel division.

One of the brand's most important achievements for the quarter was a 400+ basis point improvement in the year-over-year markdown rate. Fewer markdowns more than offset a decrease in IMU and resulted in significant merchandise margin improvement for the brand.

Urban's product deliveries throughout the second quarter and into the third continue to show additional IMU improvement. We believe this will positively impact merchandise margins in the second half of the year. In addition, ending inventory at the Urban brand, on a 'weeks-of-supply' basis, was the leanest it has been in three years, thus providing opportunity for further markdown improvement in Q3.

On the same conference call, Trish also outlined initiatives around store productivity. During the first half of FY16, the brand made good progress on these initiatives. The first is category distortion. The brand team looked at sales by product category and compared them to the floor space allocated to each category. Next, the team planned additional space for emerging strong categories like beauty, intimates and dresses, while right-sizing the space allocated to others. In July, the team tested a prototype store with the new floor set and a number of category shop-in-shops. Customer response has been very positive, so the Urban team is now in the process of reproducing this floor set across the store fleet.

In addition to better category distortion, the brand is working to increase selling space in existing stores by shrinking the back-of-house, hold less back-stock in stores, create a supply chain that requires less time to flow new product into our distribution channels and integrate more digital capabilities into the store experience.

As an example of this last initiative, the brand tested the use of in-store beacon messaging for those customers using the UrbanOn app on their smartphones. Fifty-four percent of the customers receiving those messages chose to interact with them; many times higher than the open rate of standard e-mail messaging. Furthermore, customers who chose to open the messages were three times more likely to make a purchase than an average Urban brand shopper.

Most of these productivity initiatives are currently in the design and testing stage. If proven successful they will be adopted across all stores. This ‘new way’ of operating is an iterative process tied to our long-term strategic vision and not a one-season project meant to drive immediate results.

Overall, I’m pleased with the considerable progress the Urban brand teams have made over the past twelve months in terms of improving the product, the brand position and the brand experience. Urban has reconnected with its core customer and is, once again, a fashion leader for young adults. I thank Ted, Trish, Meg and their teams for their hard work throughout this process. I hope the results are as gratifying to them as they are to me, and I’m excited to see the progress the brand will make over the next twelve months.

Turning your attention now to the Anthropologie brand, its second quarter performance was very close to what we expected it would be when we last spoke on our May conference call. The brand delivered its 12th consecutive quarter of positive ‘comp’ sales growth, but due to some product misses, margins came in below the same quarter last year. Many categories delivered solid growth but a few, notably dresses and accessories, were poorly executed, and those product misses negatively impacted the overall brand performance.

David and his team’s sharp focus on inventory management enabled them to mitigate the markdown pressure and maintain solid merchandise margins. Furthermore, the team made timely adjustments throughout the quarter adding new styles, and taking additional promotions, as necessary, to clear through slower moving merchandise. Overall, the brand finished the quarter in a healthy inventory position, and generated an operating margin that, although not an Anthropologie record, would be the envy of most other apparel retailers.

I believe the brand will continue to make adjustments to their assortments throughout the back half of the year, and I believe they are positioned to post healthy, but not record, margins over the next few quarters.

At this time last year URBN unveiled its Vision 20|20 strategy at our investor day conference. For those who attended you may recall our growth strategy was:

- Expand the number of products our brands offer.
- Grow all of our distribution channels across all geographies and allow them to accommodate a larger product assortment, and
- Improve operational capabilities and become more efficient.

All of the URBN brands are working to execute this vision. I listed a number of examples of how the Urban brand is in the process of making improvements to its operational capabilities. In addition, Dave noted in his commentary how the Free People brand benefitted greatly from launching new product categories.

Over the past year, the Anthropologie brand has had many strategic successes, as well. The brand recognized the opportunity to build much larger businesses in categories adjacent to apparel and so invested in talent and infrastructure to expand the offering in a number of these categories, most notably, Home, Beauty and Shoes. Each has performed well. In addition, the brand successfully integrated the BHLDN and Terrain concepts into the Anthropologie group and those concepts are now growing rapidly.

Strong customer response to these Anthropologie product expansions, as well as, similar successful expansions at the Free People and Urban brands, have increased our confidence in the longer term strategy we presented last September. Opening large format stores and redesigning existing stores to gain more selling space to house the expanded product is part of the strategy, so I'm pleased to report that the Anthropologie brand has now signed leases for four large format stores. The first two, both scheduled to open in spring of 2016, will be expansions of the current stores in Portland, OR and Newport Beach, CA. By next summer, the brand plans to open a new large format store in the Stanford Shopping Center, in Palo Alto, CA. This is a relocation of a much smaller store in a secondary location in that same market. The new Palo Alto store will feature expanded assortments of all of the brand's product categories, plus a large beauty offering, a BHLDN and Terrain shop-in-shop, and an Anthro café.

Larger stores, each offering expanded product assortments is one part of the strategy, but as we emphasized last September, our product expansion strategy is an important component in driving growth in all of our distribution channels. Indeed, product expansion has been instrumental in helping the direct-to-consumer and wholesale channels achieve vigorous growth. In his commentary on Q2 sales, Dave credited the expansion classes for approximately 1/3 of the gains in Free People's wholesale sales. In addition, we estimate that expanded product accounted for more than 40% of the powerful, double-digit, direct-to-consumer sales growth in the quarter.

So, to summarize, we are making steady progress on implementing all three components of our strategic plan and have already seen many successes from our efforts to date. All brands have carefully, but steadily, offered larger, non-redundant product assortments across a number of categories and, in several cases, have added entirely new categories. Without question this has helped to drive our top-line growth in the direct and wholesale channels.

At the same time we are launching initiatives to make very important operational improvements, like better category distortion in stores, faster reaction to customer demand, more efficient use of store space, and better integration of technology. More product and improved operations will allow us to continue to expand our distribution and meet our Vision 20|20 goals. We are in the early stages of implementation, but have already tasted its benefits. We're excited by the opportunities it provides and the growth it envisions. I will update you annually on our progress.

Before I turn the call over for your questions, since this will be Ted's final URBN conference call, I wanted to thank him publicly one more time for the extraordinary impact his leadership has had on the Urban brand over the past 15 years. Ted, I wish you and Sara the very best, and I thank you for your friendship and the many contributions you have made to the Company.

Finally, in closing, I thank our 23,000 associates world-wide for their inspiring dedication, drive and creativity. I also recognize and thank our many partners around the world, and finally, I thank our shareholders for their continued support.

That concludes my prepared remarks. I now turn the call over for your questions.