

# URBAN OUTFITTERS, INC.

First Quarter, FY'15 Conference Call  
May 19, 2014

## Participants

Richard A. Hayne, Chief Executive Officer  
Frank Conforti, Chief Financial Officer  
David McCreight, CEO, Anthropologie Group  
Margaret Hayne, President Free People Brand and CCO, URBN  
Ted Marlow, CEO, Urban Outfitters Group  
Wendy B. McDevitt, President, Terrain  
Glen A. Bodzy, General Counsel  
Barbara Rozsas, Chief Sourcing Officer  
Calvin Hollinger, Chief Administrative Officer  
Matt Kaness, Chief Strategy Officer  
David Ziel, Chief Development Officer  
Bill Cody, Chief Talent Officer  
Dave Hayne, COO, Free People Brand  
Oona McCullough, Director of Investor Relations

Good afternoon, and welcome to the URBN first quarter fiscal 2015 conference call. Earlier this afternoon, the Company issued a press release outlining the financial and operating results for the three month period ending April 30, 2014.

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 first quarter. David McCreight, CEO, Anthropologie Group will provide a brief update on the Anthropologie 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, along with detailed management commentary, will be posted to our corporate website at [www.urbanoutfittersinc.com](http://www.urbanoutfittersinc.com).

I'll now turn the call over to Frank.

Thank you Oona and good afternoon everyone.

I will start my prepared commentary discussing our fiscal year 2015 first quarter results versus the prior comparable quarter. Then I will share our thoughts concerning the remainder of the year.

Total Company sales for the quarter increased by 6% to a first quarter record of \$686 million. This increase was driven by a \$29 million increase in non-comparable store sales, opening 5 new stores, and a 27% jump in wholesale segment sales. Our retail segment 'comp' rate was flat for the quarter.

Within our retail segment 'comp' the direct-to-consumer channel continued to outperform stores posting positive gains driven by an increases in average order value and web and mobile site visitors. 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 25% and 8% at Free People and Anthropologie Group, respectively, and declined 12% at Urban Outfitters.

Free People Wholesale delivered another strong quarter as sales surged 27% to \$46 million. These results came from double-digit sales growth at department stores and specialty stores.

Gross profit for the quarter was flat to the prior comparable quarter at \$239 million. Gross profit rate declined by 209 basis points to 34.8%. The decline in gross profit rate was primarily due to deleverage in store occupancy costs driven by negative store comps at the Urban Outfitters brand and pre-opening rent expense related to new stores. Lower merchandise margins at the Urban Outfitters brand resulting from poor performing product also contributed to the decline.

Total 'SG&A' expenses for the quarter increased by 8% to \$179 million. Total 'SG&A' as a percentage of sales deleveraged by 45 basis points to 26.1%. The 'SG&A' deleverage was primarily due to increased marketing expenses which drove higher direct-to-consumer traffic.

Operating income for the quarter decreased by 18% to \$60 million, with operating profit margin deleveraging by 254 basis points to 8.7%.

Net income was \$37 million or \$0.26 per diluted share.

Turning to the balance sheet, inventory increased by 7% to \$349 million. The growth in inventory was primarily related to the acquisition of inventory to stock new and 'non-comp' stores. Comparable retail segment inventory increased by 2% at cost, while decreasing 5% in units.

We ended the quarter with \$517 million in cash and marketable securities. Our cash and marketable securities balance declined from year-end primarily due to our share buyback activity in the quarter. During the first quarter, the Company repurchased and retired 9.7 million common shares for approximately \$353 million. This activity completed the August 27, 2013, Board of Directors authorization to repurchase 10.0 million shares.

As we look forward to the remainder of fiscal year 2015, it may be helpful for you to consider the following:

We are planning to open approximately 35-40 new stores during the year. By brand we are planning approximately 12 new Urban Outfitters stores globally, including 3 new European stores, 15 new Anthropologie stores globally, including 3 new European stores and 12 new Free People stores in North America.

If current trends continue, our gross margin for the second quarter could deleverage versus the prior year similar to Q1, due to lower product margins and property expense deleverage resulting from continued weakness at the Urban Outfitters brand. The deleverage in gross margin could happen despite the continued sales and profitability momentum at the Anthropologie and Free People brands.

We believe 'SG&A' could grow at a low, double-digit rate for the year. This increase would be driven by increases related to direct and selling support expenses to support our new store growth and continued investments in technology and marketing expenditures to further customer acquisition and retention efforts.

Capital expenditures for fiscal year 2015 are planned at approximately \$215-\$235 million driven primarily by a new fulfillment center in Gap, Pennsylvania, the expansion of our home office and new stores.

Finally, our fiscal year 2015 annual effective tax rate is planned to be approximately 35%. Please note that this annual rate includes a favorable non-recurring federal building rehabilitation credit related to our home office expansion at the Philadelphia Navy Yard which we believe we could receive in the second quarter of the current fiscal year.

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 Anthropologie Group Chief Executive Officer, David McCreight.

Thank you Frank and good evening to everyone.

I am pleased to be here this evening to update you on the progress at Anthropologie, as well as share some of our priorities for the upcoming year.

As Dick mentioned on the last earning's call, this past year was one of strong progress in the organization and tremendous financial results for the Anthropologie Group. Although last year was not considered a particularly good one for specialty apparel, the brand's continued resonance with the customer is testament to the teams' ability to please 'Her' with compelling product and creative story telling. And the quality of our revenue and operating earnings is evidence that we can deliver this unique experience very productively.

In addition to solid comp growth, record revenue and record operating income from the past year, I am even more pleased with the broad-based progress we made in identifying ways to efficiently become more meaningful to 'Her'. Improvements were made across the organization in delivering a world-class, in-store experience, accelerating the pace of enrichment to our digital experience, improving how we design and merchandise with 'Her' in mind, and continuing to invest more wisely.

While weather this past quarter was not friendly to most fashion businesses, Anthropologie continued last year's momentum by delivering a similarly strong performance in Q1. Our brand revenue grew 10% with retail segment comps up 8% on top of last year's 8% comp. More impressively, the quality of our growth remained sound with regular price retail segment comps up low double-digits. Other indicators of the broad-based progress were seen by increased participation in our "Anthro" membership program which grew 15% from last year and our rapidly improving digital and social engagement metrics. The team's efforts helped us deliver a record quarter for sales and operating income dollars and set a new Q1 record for merchandise margin rates.

For the balance of this year, our plan is to build upon the recent accomplishments of the Anthropologie brand by investing in product and distribution expansion to drive future growth. We will continue to make strides in the appeal of our apparel offer and the strategic expansion our home and accessories assortments. Towards the end of 2014, you will see us test changes in our home decor, jewelry, shoes and bags offerings. But this year, we also plan to take further steps in building out the Anthropologie Group strategy. This past fall, we tested a shop-in-shop concept for both Petites and BHLDN within a sample of Anthropologie stores and on Anthropologie.com. The success of the BHLDN integration and introduction of the Petite collection supports the strategy of building the Anthropologie Group with brand and category adjacencies around our core customers. Still in the learning stage, indications are that this is not only a terrific digital strategy, but delivers accretive financial results in our stores as well. As a result, we are placing the BHLDN URL on the highly trafficked Anthropologie site and have expanded the store presence. We currently have 5 BHLDN and 20 Petite shop-in-shops with an eye towards other expansions and possible acquisitions in the future.

To expand our distribution we are committed to invest in talent and technology to evolve our digital brand experience; to forge new ways of deepening connections with our customer, similar to what we have done so successfully in our stores. And while digital commerce is generally viewed as border-less, we will be testing international digital expansion through search and potential partnerships. We also have expansion opportunities in our stores; our analysis suggests that we can add over 1 million square feet of space in North America and Europe alone. So we are bringing our stores to 15 new communities this year, compared to 9 last year.

As a life-stage fashion brand, the past is not necessarily an indicator of the future. But despite the high level of performance over the past few years, I am confident that there remains a great deal of opportunity to grow within our current business model. We have a financially healthy and engaged customer, a unique position in the market, and meaningful expansion opportunities remaining in proven geographies. I am not suggesting that our growth will be consistent and linear, but I am suggesting that we are in the early to middle innings of growth for the Anthropologie Group concept. As we remain vigilant to her ever-changing needs and how to meet them, the opportunity for Anthropologie is truly a remarkable one.

I would like to thank the thousands of fellow Anthropologists in communities across North America, and the UK, including my leaders and the teams in the Home office's for their passion, talent, creativity and commitment to delighting our brand fans....which make the growth potential of Anthropologie Group so compelling.

Thank you for your time, and I will now turn the call over to Dick Hayne.

Thank you, David.

Congratulations to you and the entire Anthropologie team on an exceptional quarter. It's been exciting to watch the progress your team has made over the past two years. More importantly, it is nice to see the positive customer response to your improved product offerings and creative execution. I know you believe, as I do, that there are many additional opportunities for the Anthropologie brand; that said, thanks for the impressive results this quarter.

Like Anthropologie, the Free People brand performed at an exceptionally high level in the first quarter. Both brands delivered record sales, regular price 'comps' which exceeded total 'comps' and record operating profits. Free People's retail segment 'comps' grew by 25%. Amazingly, this increase was accomplished on top of a 44% increase in the previous year's first quarter.

Within Free People, all channels excelled in the quarter. Wholesale, once again, showed acceleration in revenue growth with an impressive 27% increase. This was driven domestically by account and category expansion, and internationally by new outlets in Asia. During the quarter, our partner in Japan, World Co. Ltd., opened five additional Free People shops in Tokyo, Osaka and Kyoto, and in Hong Kong, the brand partnered with Lane Crawford to open a 700 square foot shop-in-shop in their Lab Concept. This shop, combined with a Chinese language e-commerce website that is scheduled to launch this summer, should give the Free People team a better understanding of the Chinese customer and prepare the way to open wholesale shops within Mainland China.

Besides offering desirable products, the Free People brand continued to produce some of the most compelling imagery and customer engagement in the industry. This helped to drive increased productivity in both the direct-to-consumer and store channels.

Now, as pleased as we were with the first quarter performance of the Anthropologie and Free People brands, that is how disappointed we were with the performance of the Urban Outfitters brand. Total retail segment 'comps' for the Urban brand decreased by 12% in the quarter, initial margins lagged the prior year and promotional activity increased. April 'comp' sales were significantly less negative than the first two months of the quarter, however, this was expected due to the Easter calendar shift. I believe the Urban brand's product assortment is slowly improving; it is certainly becoming less 'one note' and more focused on our core, young adult customer.

I also believe the stores and the web look better than they did several months ago, but clearly, there is still much work to be done for Urban to regain its fashion footing. Due to lower than planned sales in April, the Urban brand ended the first quarter with some excess inventory, so promotional activity in the second quarter is likely to be greater than in the same period last year.

To reiterate what I said on our conference call two months ago, we believe there are no fundamental structural changes in the young adult market. There are, of course, fashion changes, and the success of each brand depends on the accuracy with which it predicts those changes and offers compelling products and imagery that reflect those changes.

I can assure you that the Urban teams have been working diligently to build a fresh product assortment and marketing plan that we believe will resonate with our 18 to 28 year-old customer base this fall.

Now, let me turn to the growth initiatives the brands are working on this year. David already reviewed the Anthropologie brand initiatives, so I won't repeat them.

The Free People brand plans to drive growth on three different fronts: product expansion, geographic expansion, and improved marketing.

As for product expansion, the merchant and design teams are successfully continuing to expand the assortments. Shoes, intimate apparel, special occasion dresses, and, most recently with the launch of Free People Movement, active wear, now compliment the base apparel assortment. This product expansion has helped to drive sales across all channels and we believe will fuel future growth, as well.

Geographic expansion will be accomplished by opening new stores in North America, by adding wholesale accounts and shop-in shops overseas, and by expanding the international direct-to-consumer business. The 12 new stores that Free People plans to open this year in North America will average approximately 3000 square feet. This is nearly twice the size of many of the earlier stores and will allow the brand to offer more of the expanded product assortment. As the store size has grown over the last few years productivity has actually increased and four-wall profitability has jumped, as well.

The wholesale business has also benefitted from expanded product offerings. Nearly 45% of wholesale's first quarter domestic sales growth came from expanded product categories and that penetration will likely grow as the wholesale shoe assortment begins shipping early this fall. The wholesale showroom in New York recently doubled in size to accommodate the expanded offering.

Wholesale is also aggressively pursuing additional international business. Recently opened showrooms in London and Tokyo are attracting new customers and the number of shop-in-shops in Europe and Asia is expected to grow throughout the year. In Q1, versus the same period last year, international wholesale sales jumped by 105%.

Growth in the direct-to-consumer channel remains strong, propelled by the increased product offerings, very 'sticky' social media marketing and increased customer engagement on both the web and mobile platforms.

Now, as you would expect, the Urban brand is currently focused mainly on creating more compelling fashion and communicating that through more creative displays and on-line imagery, but there are a number of growth initiatives, as well. Like Free People, the Urban brand is planning to grow by expanding product assortments, expanding the brand reach and by improved marketing. Product categories slated for growth include: living and home, beauty, music, and some food offerings.

In addition, this March Urban launched Without Walls which is an active lifestyle category extension. There are currently eight small Without Walls shops inside existing Urban stores and a Without Walls website which can be accessed directly or through the Urban website. Customer response to this new concept has been good, and we will be opening additional shops and adding active product to more Urban stores.

As Urban continues to expand geographically, the emphasis will be on opening more of the newer store formats which offer a differentiated and expanded experience. I recommend that you visit the recently opened and highly successful Space Ninety 8 in Williamsburg or the Space 15 Twenty development in Hollywood. Both of these locations offer a lifestyle mix of products, food and drinks, events and services – all in an expanded space.

Finally, please note that I'm near the end of my comments and haven't mentioned the weather once. While the abnormal weather earlier this spring certainly had a negative impact on sales, the Anthropologie and Free People brands demonstrated with their record-setting performances, that compelling product and experiences can overcome most weather-related issues. We remain very confident that the Urban brand will course-correct and re-join its sister brands as a top performer.

In closing, I thank our 22,000 associates for their amazing dedication, drive and creativity. I also recognize and thank our many partners around the world. Finally, I thank our shareholders for their continued support.

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