

# URBAN OUTFITTERS, INC.

First Quarter, FY' 14 Conference Call  
May 20, 2013

## Participants

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

Good afternoon, and welcome to the URBN first quarter fiscal 2014 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, 2013.

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 2014 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 14%, to a first quarter record of \$648 million. This increase was driven by a strong retail segment comp rate of 9%, opening 7 new stores during the quarter, a \$32 million increase in non-comparable sales, and a 16% jump in wholesale segment sales.

The 9% increase in retail segment comp sales was fueled by continued robust direct-to-consumer growth and positive comp store sales. Direct-to-consumer growth was driven by an increase in visitors and improved conversion rate. Positive comp store sales resulted from increased transactions, partially offset by lower average unit selling prices, while units per transaction were flat.

By brand, our retail segment comp rate was 44%, 8% and 6% at Free People, Anthropologie and Urban Outfitters, respectively.

Free People Wholesale delivered another strong quarter as sales rose 16% to \$36 million. These results came from double digit sales growth to specialty stores and department stores.

Gross profit for the quarter increased by 18% to \$239 million. The gross profit rate improved by 125 basis points to 36.8%. The improvement in gross profit rate was primarily due to a reduction in merchandise markdowns mainly driven by improvements at the Anthropologie brand. We also improved our initial merchandise margins and leveraged store occupancy expenses. These gains were partially offset by deleverage in delivery expense primarily related to an increase in penetration of direct-to-consumer sales.

Total selling, general and administrative expenses for the quarter increased by 11% to \$166 million. Total SG&A as percentage of sales, leveraged by 70 basis points to 25.5%. The SG&A leverage was primarily due to improvements in direct store controllable and selling support expenses driven by positive retail segment sales.

Operating income for the quarter increased by 38% to \$73 million, with operating profit margin improving by 196 basis points to 11.3%.

Net income was \$47 million or \$0.32 per diluted share.

Turning to the balance sheet, inventory increased by 9% to \$325 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 1%, driven primarily by additional inventory to fuel strong direct-to-consumer sales growth.

Lastly, we ended the quarter with \$638 million in cash and marketable securities.

As we look forward to the remainder of fiscal year 2014, 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 16 new Urban Outfitters stores globally, including 5 new European stores, 9 new Anthropologie stores globally, including 2 new European stores and 14 new Free People stores in North America.

We are planning for continued year-over-year gross margin growth, with a goal of producing at least 50 basis points of margin improvement for the year. We believe our gross margin growth opportunities will be primarily driven by lower markdown rates and higher initial margins resulting from improved product execution and continued focus on inventory management.

We continue to focus on effectively managing our selling, general and administrative expenses, but remain committed to investing in our business to drive long-term sales and margin growth. These investments relate to increased spend in technology systems and talent to boost web and store-based initiatives. Additionally, we plan on increasing marketing and customer analytics headcount, as well as marketing spend, to further customer acquisition and retention efforts. Due in part to these investments, we expect total SG&A to increase in the mid-teens for fiscal 2014. I want to note that our first quarter SG&A growth rate was lower than planned. This was mostly due to timing of new headcount and is not indicative of our plans going forward.

Capital expenditures for fiscal year 2014 are planned at approximately \$190-\$210 million driven primarily by new stores and the expansion of our home office.

Finally, our fiscal year 2014 annual effective tax rate is planned to be approximately 36.5%.

As a reminder, the forgoing does not constitute a forecast, but is simply a reflection of our current views. The Company disclaims any obligation to update forward looking statements.

Now I will pass the call over to our Anthropologie Group Chief Executive Officer, David McCreight.

Thank you Frank, and good afternoon everyone.

I am happy to be here today to update you on our progress at Anthropologie. On an earning's call a little more than one year ago, we shared our assessment of the health of our brand, state of the organization and business, and path to regaining momentum with our customers.

As you may recall, we outlined several specific priorities:

- Correcting course in design and merchandising
- Returning full-price and markdown sales to past ratios
- Improving 4-wall productivity
- Turbo-charging our DTC investments for growth
- Reversing the trends in the house-file

To begin, we returned our customer to the forefront of discussions and decision-making, challenging our understanding of and connection to her. We encouraged professional curiosity in order to engage a broader base of talent throughout the organization. We re-examined our organizational structure and how it supported our goals. Lastly, we added more analytical rigor to investments and processes to improve returns and efficiency.

Now with a clearer view of our customer in mind, we shifted the product and marketing efforts into a broader range of aesthetics and moments in her life. We moved away from dependence on the quirky-preppy look and emphasized other areas of our brand's aesthetic reach with softer, sensual feminine looks, as well as adding elements of bohemia. Additionally, we identified other moments in her daily life where we thought Anthropologie had opportunity and began building into 'weekend casual' and expanding our 'desk-to-dinner' offerings. And finally, we worked to recapture our customers' attention by adding back in thoughtful design details for which Anthropologie had become so well known.

In examining the organizational structure, we moved to clarify accountabilities and speed decision-making by tightening and re-aligning the structure across merchandising, design, creative, store operations, and marketing.

Now with professional curiosity on the rise, requests for deeper analysis were welcomed and improved the results of many projects. The impact of data at Anthropologie has been felt most notably in merchandise purchasing decisions, evaluation of our house-file and our go-to-market strategies, the growth of our direct-to-consumer business and our site selection process. Currently, we are rigorously studying our store workflow and staffing models with the goal of shifting more time to front of house activities to deepen the already strong relationship our stores have with their customer.

Thus far, her response to the changes in the Anthropologie brand experience and product offer has been encouraging. From our listening posts in stores, from employees and social media to the more objective metrics of product revenue, house-file health, and product margin, our Q1 results were solid. Regular price brand comps grew in the low teens for the quarter, leaving us excited by the higher quality composition of our revenue, particularly in response to some of the changes in our apparel. As we saw in holiday, our product margins continued their robust expansion, with our own brand product leading the way. We exited the quarter with significantly less markdown inventory compared to prior year. And our trailing twelve month customer counts grew double digits across retention, acquisition, and reactivation (with multi-channel buyers growing rapidly).

While we have regained some of the momentum that we targeted about one-year ago, we are in the never-ending effort to surprise and delight her. In the near term, we are continuing to work on: increasing the appeal of our offering across all product divisions; becoming more nimble in our product design; amplifying the reach of our story telling; improving the accuracy of our product distortions and store allocations; continuing the pace in our development of our on-line experience into one that is as compelling as our stores; and mining our growing database for insight and more effective ways of speaking to her, to name a few.

The recent progress has done nothing to lessen my enthusiasm for the longer-term prospect of building the Anthropologie brand platform. I am thrilled with the resonance of our brand, and the scale and vitality of our customer set. To deliver on the potential with our customer, we plan on expanding our product range in existing categories as well as adding adjacent categories where important to her; reaching new customers through our continued investment and growth of our direct-to-consumer channel and driving further geographic expansion. We are a great brand, with a strong connection to our customer. We have a motivated team, and compelling business model that we believe will fuel growth for years to come.

In closing, I'd like to thank the Anthropologie team for passionately embracing the changes over this past year. I am proud of the Team's progress in how we work together and the many ways we continue to inspire 'her'.

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

Thank you, and good afternoon, everyone.

David, I'm so pleased by the progress Anthropologie has made over the past twelve months. Your product offering is now more compelling and customer appropriate and your marketing is once again inspiring your customers. Congratulations to you and the entire Anthropologie team for a job well done.

While the turnaround at Anthropologie certainly helped to drive URBN's record first quarter sales, Anthropologie was not alone. The Free People brand produced outstanding 'comp' gains across all of their channels. In fact, all brands continued to build upon the successes established last year and each posted record first quarter sales.

We have repeatedly stated that driving top line growth in ways that are accretive to the bottom line is our number one financial objective. You may recall us discussing the four initiatives to achieve this goal. They are:

- expand and enhance the direct-to-consumer channel at each brand
- continue to build additional stores in under-penetrated domestic markets
- expand each brand internationally using all of our channels of distribution and, importantly,

- continue to expand product choices and categories and enter adjacent businesses.

Concerning this last initiative, our product expansion and foray into adjacent businesses will be accomplished through a combination of internal development and external relationships which may include licensing, partnerships, joint ventures and acquisitions.

I'm pleased to report that during the first quarter, we made progress on each of these four initiatives.

- First, expanding the direct-to-consumer channel. During the quarter this channel continued its breathtaking growth. Each brand posted strong, double-digit sales increases and total direct-to-consumer penetration to total retail sales jumped by more than 400 basis points. On a year-over-year basis, web traffic was up by almost 20%, mobile sessions more than doubled and conversion improved by 56 basis points. Better use of data analytics, personalization and segmentation contributed to new direct-to-consumer customer growth of 46% and re-activated customers grew by 45%. Also during the quarter, the Free People brand launched their FP Me site which is designed to engage their customers with the brand and with other Free People customers. In the first three months, FP Me members uploaded more than ten thousand pictures of themselves and their friends wearing Free People product.
- As for domestic store growth, during the quarter we opened a total of five new stores in the US. This includes two new Anthropologie stores and three new Free People stores. We estimate that during FY14, we will open a total of approximately 30 new domestic stores.
- Turning to international expansion, in the first quarter, we opened one new Urban store in Europe and one in Canada. For the year, we plan to open approximately one new Urban and one new Anthropologie store in Canada and five new Urban and two new Anthropologie stores in Europe. In addition, Free People hired a European sales manager and leased a wholesale showroom in London which should open in the next few weeks. Both actions should help increase wholesale sales and address the very low penetration of Free People product in the European market. As for Asia, in April, Free People wholesale, in partnership with World Co. Ltd. of Japan, opened its first 'pop-up' shop in the Tokyu Department Store in Tokyo's Shibuya shopping district. This shop received an overwhelmingly positive response from Japanese shoppers which bodes well for further wholesale penetration of the Japanese market. Later this year, Free People will work with World to launch a Japanese direct-to-consumer business, as well.

- Finally, product expansion in the direct-to-consumer channel across all brands grew by 46% in the first quarter versus the same quarter last year. Several new product category introductions over the past several years have driven some of this increase. The on-line launch of Anthropologie petites in fiscal year 13 proved so successful that they increased the style count and tested this product in one store during the first quarter. Based on the results of that test, petites will be rolled out to a number of additional stores in the remaining quarters of fiscal year 14. Free People's line of intimate apparel continues to grow steadily and now accounts for more than 15% of that brand's direct business. We expect to offer additional categories in all brands and are currently in discussions with a number of potential business partners that could facilitate our entry into other adjacent and complementary businesses.

Turning to other initiatives for fiscal year 14, this year we have two important new operational goals. The first is to improve our inventory turnover. Given the implementation of new technology that allows a single view of inventory across both retail channels, and the capability to fulfill a customer order from any point of distribution including the stores, we believe we have the opportunity to meaningfully reduce our weeks of supply.

Our second goal is to further reduce our time from order placement to market delivery. We are working on a number of supply chain, brand design and communication initiatives that will enable us to reduce our overall time to market.

Both of these operational goals should help us to better please the customer and, at the same time, allow us to improve our financial performance. I will update you on our progress on these two important initiatives at the end of fiscal year 14.

Before I turn the call over for questions, I would like to recognize and thank our brand leaders and our 20,000 associates worldwide. This is an exciting time for our business; a time packed with change and uncertainty, but also one of unparalleled opportunity. The inspired work of our many talented co-workers allows us to meet the challenges of change and keep winning. I am profoundly grateful for the opportunity to lead this amazing community. Thank you.

At this time I will open the call to your questions.