Watches of Switzerland

Full Year Results | Video Webcast

13th of July 2023

Transcript

THE WATCHES OF SWITZERLAND GROUP

Disclaimer

This transcript is derived from a recording of the event. Every possible effort has been made to transcribe accurately. However, neither Watches of Switzerland nor BRR Media Limited shall be liable for any inaccuracies, errors, or omissions.

Operator: Thank you very much sir. Ladies and gentlemen, if you would like to ask a question, please do press star one to register a question. Please also ensure your mute function is not activated, light signals reach your equipment. So once again, please press star one for questions.

Our very first question today is coming from Antoine Belge, calling from BNP Exane. Please go ahead.

Antoine Belge: Yes, hi good morning everyone. It's Antoine at BNP Exane. Three questions if I may. First of all, in the previous conference call you had mentioned that the first quarter, which were modest sales decline, so is that still the case and to what extent you're, I don't know, a bit more optimistic or a bit less on that number compared to last time? Second question is about the dynamics of the wait list, here I'm not talking about necessarily how long they are, but more how people react when they're called. I mean I still seeing some people maybe postponing a bit their purchases, any update on that? And finally, you have a guidance of flat margins, I've noticed that you're not the only ones that the pound sterling had strengthens, but yet you're maintaining the guidance in value, so are there sort of setting factors? And more in general, what sort of top line is sort of required as a minimum to reach that flat margin guidance? Thank you very much.

Brian Duffy: Thanks Antoine and good morning. So, we're not going to say anything more specifically on Q1 trading, we've confirmed our guidance overall and if I recall what we'd indicated before about Q1 being modest decline was based upon delivery schedule from our key partners and some very tough year-on-year comp. So, none of that has effectively changed and we're confirming our guidance and can't really say anything else about Q1 overall at this point. Wait list behaviour hasn't changed either. We're still adding more people to the registration of interest list than we're taking off, demand remains very, very strong and positive. And consumer behaviour really hasn't changed from anything I've indicated in the last couple of calls that we've had. Anders, you want to talk about margin?

Anders Romberg: Yeah, sure. So, we expect, as we pointed out, margin to come in line with FY23 for FY24, and that's driven by more solid growth in luxury watches than we expect to see come through in jewellery. And we're going to have headwind from interest free credit in the first half, and then we start analysing higher interest rates in the second. So, more impact in the first versus second.

In terms of FX, obviously, we haven't changed the range from 1.65 to 1.7, so we have cover to come in at current rates. We do reforecast our sales and profits on a weekly basis and are confident about our guidance.

Antoine Belge: All right. Maybe just to follow up in terms of area of cost where you could have some flexibility, are there some things like, I don't know, marketing or more structural cost savings that you could achieve in case the environment would pull a bit weaker than stated?

Anders Romberg: I mean, we obviously review our investment strategy as part of our trading meetings, which we again conduct on a weekly basis. So if there's pressure coming in terms of interest for the interest rate hikes that we had planned for some coming through this year, obviously, we will take the appropriate action to offset some of the effect of that.

Brian Duffy: Antoine, if I could just add that you look at the year that we're reporting fiscal year 23, there was a lot of moving parts in the year. We stuck with our guidance the entire year and we are prepared in terms of actions, in terms of contingency and that sort of thing to make sure that we're giving out guidance that we feel confident we can deliver on it. So I think we are looking at a more stable situation than you would've said, but weather conditions that we experienced and had to respond to last year.

Antoine Belge: Okay, thank you very much.

Brian Duffy: Thank you. Cheers.

Operator: Thank you Mr. Belge. Thank you. Sorry about that, sir. Our next question will be coming from Jonathan Pritchard calling from Peel Hunt. Please go ahead.

Jonathan Pritchard: Good morning. Two if I may. Firstly, on interest free credit, has the percentage of sales going through on interest free credit changed, and how do you intend to mitigate the impact of further interest rate rises? Is making that a more expensive offer? And secondly on Europe, is there a pipeline at all? I know you've talked a lot about acquisitions, but just looking out 18 or 24 months, is there a pipeline of stores that you have or are we settling at seven for the time being, having a look and hoping for acquisitions?

Anders Romberg: So, I'll take the interest. So, we have planned for base rate increase in our guidance. If rates were to climb even farther, obviously we would take, as we pointed out, actions on our other cost base to offset that. We think that in the US, probably rates will not continue to move upwards. And so, we don't see that as a risk here. In the UK, clearly there is potential of further rate increases and we have monitored that and come up with a list of offsets that we should take action on if that was to occur.

In terms of the penetration of interest free credit remains pretty much in line with what we experienced last year.

Brian Duffy: On Europe, John, we're very pleased with our progress in Europe with the stores that we've opened. Our analysis of the market was that it was under invested in terms of retail and support of marketing. And I think we've proven that to be the case for the stores that we've opened in Stockholm and in Copenhagen and now adding that Dublin and Berlin. So, I think we've proven our contention. Our strategy was always to have full presence of our model in Europe, which would include representing all of our key brand partners. We think we would really only achieve that effectively through acquisition. So, it's been a key part of our strategy alongside the development of mono brands.

There are other opportunities for mono brand development that we continue to look at. But we'd like to be able to progress and deliver on an acquisition and obviously we're actively working on it. Once we're fully present, then there's other opportunities. There's airport retail, there's e-comm and there's a full suite if you like, of a flexible response of retailing that we could do for the market. So, feeling positive about Europe and want to do more than we're doing at the moment.

Jonathan Pritchard: Okay, lovely. Thank you very much.

Brian Duffy: Yes.

Operator: We'll now go to Jon Cox calling from Kepler Cheuvreux. Please go ahead.

Jon Cox: Yeah, good morning guys. I have some questions on the pre-owned market. You mentioned it doubled for you during the year, but can you give us an absolute figure in terms of group revenue where you are, I'm guessing somewhere close to 10% of group revenue is maybe in the pre-owned watches? And then just a follow-on, I think it is really great news, the whole Rolex certification scheme. Can you just talk through the dynamics? I guess, you've had a lot of watches in that you've been buying. You've sent them off to Rolex and I'm just wondering about the lead times and the process. And I'm wondering if ultimately do you think you would actually be doing the certification? Because I understand there is quite a big bottleneck at Rolex at the moment, which obviously will cap potential sales from that scheme. And obviously if you could do the certification, that would probably be very helpful. Thanks very much.

Brian Duffy: So, we're very pleased with our progress on pre-owned. So obviously in the US, we've bought Analog: Shift who are great guys and a great brand and we've really built that very effectively. Here in the UK, we've expanded our abilities to both procure and rework and present a pre-owned product.

It's nowhere near 10% though, and we're not giving out an exact number. But if you go back a couple of years, we are reporting that pre-owned was only 1% of our sales. So, you're pretty far off at 10%, but we have very high ambitions for CPO with Rolex. Effectively, Rolex are directing that whole activity to authorised retailers like us. It will increase the supply of Rolex effectively to our clients and representation in store. And you're right that just working out all the logistics and processes are the key priorities right now. We've had good experience so far.

We've given watches, they've been authenticated, they're back with us again, all been on schedule. There's been a great deal of preparation done. The first experience we're going to have is in the US next week and that will happen. And experience so far is watches has given turned around in the timeframe that was indicated and back with us again. And we are now working on the in-store presentation and distribution. So, we are not experiencing a bottleneck, but we have to see how all these logistics work. On when we will authenticate and refurb the watches and in time, it's our assumption that we will, maybe it will happen quicker in the US and the UK would be my bet. But its Rolex being appropriately careful as they always are and doing something that's significant for the market and just 100% making sure that everything is as it should be.

So, they're doing all of the authentication and refurb. And effectively, we've managed to take some work away from them by extending our capability of rework and so on for new Rolex products, products that have been just serviced. So, we've kind of created our own capacity. So, we are feeling good about it all and I think it's fair to say that we would anticipate at some point in the future that we would be doing the authentication and refurb work and slow down or speed up rather that whole process of getting product back to market. But we feel very, very positive about the prospects for Rolex CPO and other brands in the years ahead. And it'll feature obviously in our long range plan.

Jon Cox: So, at the moment if I walk into one of your stores with a Rolex, I can sell it to you on the spot?

Brian Duffy: You always could.

Jon Cox: Because I... You always could. Yeah, exactly. Yeah. And-

Brian Duffy: Yeah, you always could. And what we supplemented it with is we have a team doing online, a lot of this activity is digital. So, we have a team doing valuations online. And in the UK, all of our product today is coming directly from consumers. In the US there are agents around that can supplement. But yes, you can walk in and we'll value your product and we have people fully trained to do that. And then we have a kind of centralised experts, but it works very well.

Jon Cox: Yeah. But I'm just wondering, are you getting a load of people coming in with their Rolexes saying they want to sell it? And then obviously if it takes you a lot of time to turn it around, get the Rolex certification, does this have an impact on your inventory or your sort of like it's tying up cash for six months or 12 months until you can get it back into the store to sell it?

Brian Duffy: I honestly don't think the working capital element... It's longer than getting supplied by new Rolex product and contacting people on the waiting list and selling it obviously. But we're not really expecting it to be a significant working capital issue at all. We're working on the logistics. Rolex is very, very efficient in everything that they do. It is all getting done locally by the way. So here in the UK, it's London. US, it's New York. So no, we're not expecting it to be a significant drain on working capital or build up of stock at all.

Jon Cox: And maybe just a follow-up, maybe more of a technical question. This is on the new relationship you mentioned with Audemars Piguet, like a joint venture. A, I'm just wondering how do the financials work on that? Is that more like a royalty payment or does it come in at the associates line? And then as an add-on, obviously AP is doing most of it now in theory in-house. Is there room given the changes in the management at AP to maybe bring back some of that business into this new model? And maybe do you see potential elsewhere with this model, or is it not something you really want to pursue too much because maybe the profitability is not quite as good as the group?

Brian Duffy: The profitability is attractive, the return on investments attractive. We really do own 100% of the store rather than a significant minority. Yes, but even a significant minority of a AP store is a valuable investment. And obviously the proportion of the investment is relative to the proportion of the returns. So, they're very good deals as far as a model that Audemars prefer. Obviously, they'd be very clear in saying they only want to be in mono brand situations. They don't want to be in multi-brand, but we were hopeful, and we are hopeful of doing more projects like this with them.

But this will be our first big one and it's a big deal in Manchester. It's a beautiful store, it's a beautiful location, it's a great city and we think they'll do really well. The change in the CEO, obviously, we've got to wait and see if that results in any change in strategy. I'm not anticipating that it would, but you never know. Different CEOs might have different ideas, but it's a hugely successful brand and it's demand hugely exceeding the supply. And this AP house that we'll be doing with them I think will be a really successful and exciting project.

Jon Cox: Great. Very helpful. Thank you.

Brian Duffy: Cheers.

Jon Cox: Thanks.

Operator: Next question is coming from Natasha Brillant calling from Credit Suisse. Thank you.

Natasha Brillant: Hi, morning. Thanks for taking my questions. Three from me, please. So firstly, M&A perhaps has been a bit slower than we might have anticipated, so just keen to understand why that might be. It strikes me that both the US and Europe are quite fragmented markets, lots of opportunities, perhaps even more in a tougher macro environment. So, what might be the catalyst for us to see a bit more on the M&A side? And then a couple of questions for Anders. First of all on you mentioned cost savings in the events of rate rises, so I just wanted to confirm that you'd only execute on those additional cost savings if rates would be higher than you budgeted for.

Or in other words, are there scenarios of potential cost savings or upside risk on the margin that you could roll out as the year goes on, even if interest rates are as you expect? And then the second question, last question for Anders, just since you've re-joined the business, any particular observations or anything that surprised you? Any thoughts to share with us? Thank you.

Brian Duffy: Natasha. Hi. The M&A, we're actually ahead of what we've put in our long range plan for M&A, but we did more upfront. Are we working hard on it today to do more UK, US, and Europe? Yes, we are. The opportunity and I think the compelling logic for scale is as you describe it. I think it is obvious it's a fragmented markets, US and Europe, so it remains a big focus. We are not going to change our financial formula that we're using. Might there have been an element of some people who are willing to sell in principle but maybe wanted to enjoy how super strong the market was a year ago? Yeah, I think there could have been an element of that possibly. But we're working on it. We'll give you a full update on what we think the potential is when we do the long range plan, but nothing's changed in terms of the opportunity and our ambition.

Anders Romberg: In terms of cost savings as obviously we're not wasting money just to point that out. But obviously, we can have choices to make whether or not we would engage with a third party activity that we otherwise would've done and defer that out to a later stage and things like that. So it is in those areas. We're not looking at conducting any restructuring or anything of that nature. We don't see any need for that. The business is performing really well and we're in for the long haul. So no change in strategy at all in that sense. But it is more about being picky and choose-y about which services we actually go out and acquire.

On your question, observations after my return, obviously I really enjoy working in this company. That's why I'm back.

So really fascinating to come back, I must say. A lot of things has remained the same with obviously progressing in the business. I think the recruitment process has been good. We've added some really strong talent in merchandising, which I really enjoy to see. Finance team remains super strong, so all of that has worked out really well. Business in the US continues to grow. Fascinating, so I love being back.

Brian Duffy: I just maybe add from our standpoint, Anders seems a bit more relaxed and more suntanned. That's probably the main observation.

Natasha Brillant: So, yeah, that's a good thing. Thank you very much.

Brian Duffy: Thank you.

Operator: Thank you so much, ma'am. Our next question is coming from Kate Calvert calling from Investec. Please go ahead.

Kate Calvert: Morning everyone. A couple from me. The first question is could you comment on the amount of stock which has gone into your summer sale this year compared to last year and pre-Covid levels? Is it more or similar? My second question is on Mayors. Could you comment on how your refurbishments are performing in terms of payback and how many have you got left to do? A final question, a bit more technical. Could you just break out your mono-brand expansion issue, the 20 you're opening by region please? Thank you very much.

Brian Duffy: Yeah, we are participating in the summer sale as you'll have seen. We've been reporting more or less since last Christmas. So, the jewellery market's been tougher than expected and tougher than what we had planned for when we obviously bought into stock. So, we have a bit more jewellery stock than is ideal. We have some areas of watch discontinuations as well, where we have the stock and obviously want to trade through that effectively. So, we are participating in the summer sale. Historically we always did. In fact, the last couple of years we did too. But we're participating a bit more than we did over the last couple of years, but still overall less than what we were doing historically, pre-Covid. We're giving reasonable discounts, still very profitable, obviously, and contributes to sales performance. It's predominantly in the month of July.

Mayors refits-

Anders Romberg: So, we've done seven out of the 13, so we have six to go in Mayors. Obviously, the payback on that acquisition has been significantly ahead of what we expected when we acquired them. The purchase price, as disclosed, was about eight times trailing EBITDA. We haven't specifically said what the payback was, but way beyond our wildest imagination.

Brian Duffy: Yeah, and also we would've done all the Mayors month one if we could have done, but, A, when we are refurbing, we do more than refurbing, we tend to expand, we relocate. Like we did in Lenox, for example, we relocated. In Merrick Park, we relocated. So, we look to do more with the stores. We look to get more brand representation. Then with those Rolex design, everything takes a bit of time. So we're looking forward to them all being done. The new formats really, really work. There's no question. Significant increases in traffic with maintained conversion, so that's where the sales upsides are coming from.

On the mono-brand. I don't think we've given a split by region overall. I don't think it'd be that hard to guess. I mean, the return that we're looking at is not that different by region either. So, if you got it wrong, a wee bit here or there, I don't think it'd make any difference to any models. But we are continuing to roll out, it's the same partners that we're rolling out with overall and so that's got good momentum.

Kate Calvert: Great, thanks very much.

Operator: Thank you very much ma'am. Ladies and gentlemen, once again if you have any questions or follow-up questions, please press star one at this time. We now go to Adrian Duverger, calling from Goldman Sachs. Please go ahead.

Adrien Duverger: Hey, good morning. Thank you for taking my questions. The first one, we'll just be on the visibility of the supply of products, particularly with the reopening of Asia and stronger tourism demand in Europe, especially relative to the UK. The second one is just within the UK, do you see any difference in performance between London and the other cities? And do you see any softening of consumer demand or down trading by consumer price point? I'll have the same question regarding the US, so what you see in terms of underlying trends. Anything to call out with regards to traffic or conversion in the US? Thank you.

Brian Duffy: Hi Adrian. Thanks for your questions. Supply of product, yeah, the impact of China opening, but we don't see... What happens in terms of supply is we get numbers at the start of the year from Rolex, from Patek and those numbers are always honoured in terms of units. If they ever changed, it's a change upwards, it's never down. I don't think that people are assuming that during lockdown there was a huge reduction of what was going into China and now there's a huge increase. I really don't think those dynamics happened. I think, as was the experience with us during lockdown, supply was maintained and actually sales were reasonably maintained as well overall. So, I think it's much less of a big deal with our key brands than might be for luxury overall.

In terms of London Regional, the... No great change. I mean, I think London still doesn't have the full traffic back in terms of UK tourism coming into London. It's better, West End, traffic overall progressively getting better, but not at pre-Covid levels yet. People aren't still working full-time here. I think there's a lot more four day working happening, three day, four day, but still not up to where it was before. Obviously, tourism pretty much disappeared when lockdown happened. There's a bit of it back, but of course we have the VAT situation here in the UK, so even with tourists back, we won't be getting the same impacts that we did previously because people could shop tax-free in Europe in a way that they can't do here. So, we haven't experienced them. We're not projecting any significant upturn in the split of our tourist business. Our business in the UK remains 97% domestic.

We have seen an uptake in the airport, and Heathrow is back and running, I think, pretty efficiently again from my experience. Really pleased for the people there, they've been through an awful lot with lockdowns and systems issues and whatever, but they've now got a good level of traffic. I think we're having a reasonably normal summer, by that I mean a pre-Covid type summer overall. Good traffic, good efficiency, hoping that the controller issues in Europe won't negatively impact that overall. But traffic's goods, retailing is good. At Gatwick as well, traffics good and retailing good, and a wee bit better than we might have expected.

In the US, I think we're very well positioned geographically. Florida has been a great economic response to all of what happened in Covid, so the state is booming. Obviously that's the biggest part of our business in the US. Vegas is also booming. A lot happening in Vegas. We got the Formula One coming up in November, but apart from that, a lot of construction happening. Still a lot of expansion and hotel occupancy is very, very high. So Vegas has been great. New York, similar to London, you've still not got the number of people back working in New York as there was pre-Covid. Tourism in New York actually is good, so a lot of traffic in Hudson Yards and SoHo, actually very good. Those stores have done wonderfully well for us since we opened them back in 18/19.

So, we're not seeing any real consumer... What the consumers done over the last couple of years and continues to do so is trade upwards. We're selling more gold, less steel and gold, more steel and gold, less steel. So generally, the consumers trading up upwards, so was a trend towards yellow gold in both watch and jewellery, which is positive for price points. So, we haven't seen a trade downwards because of economic concerns amid...

Operator: Mr. Duverger, does that answer your question, sir?

Adrien Duverger: Thank you very much.

Operator: Thank you sir. As we have no further questions, I'll turn the call back over to Brian for any additional or closing remarks. Thank you.

Brian Duffy: Yeah, well just thanks everyone again for joining us. We are very pleased with the fiscal year 23, record sales and profits and return on investment. So we're thrilled about that and pleased to be maintaining our guidance. We are working on a long range plan, giving it a great deal of attention and when we present it to you in Autumn, it'll be very much thought through and our best view of what this five year period is going to give us. We're very, very confidient in our sector. That said, we're in a great place with a luxury watch category, with jewellery and within that great place clearly our model is working very effectively. Very pleased in other areas too, like ESG where we've made great strides, the work our foundation's doing, the engagement of our employees.

Finally, just to our employees, to our colleagues out there, a massive thank you for the continued hard work and focus and positivity that they show. They are a real inspiration, and they take a lot of credit for the performance that we've managed to deliver. So positive all round. Thank you for joining us and we'll look forward to updating you with the quarterly update following Q1. Thank you.