tapestry

COACH | kate spade | STUART WEITZMAN

SPEAKERS' NOTES FOR CONFERENCE CALL

Moderator: Christina Colone
November 7, 2024
8:00 a.m. ET

Operator:

Good day, and welcome to this Tapestry Conference call. Today's call is being recorded.

At this time, for opening remarks and introductions, I would like to turn the call over to the Global Head of Investor Relations, Christina Colone.

Christina Colone:

Good morning. Thank you for joining us.

With me today to discuss our first quarter results, as well as our strategies and outlook, are Joanne Crevoiserat, Tapestry's Chief Executive Officer and Scott Roe, Tapestry's Chief Financial Officer and Chief Operating Officer.

Before we begin, we must point out that this conference call will involve certain forward-looking statements within the meaning of the private securities litigation reform act. This includes projections for our business in the current or future quarters or fiscal years. Forward-looking statements are not guarantees, and our actual results may differ materially from those expressed or implied in the forward-looking statements. Please refer to our annual report on Form 10-K, the press release we issued this morning, and our other filings with the Securities and Exchange Commission for a complete list of risks and other important factors that could impact our future results and performance.

Non-GAAP financial measures are included in our comments today and in our presentation slides. For a full reconciliation to corresponding GAAP financial information please visit our website, www.tapestry.com/investors, and then view the earnings release and the presentation posted today.

Now, let me outline the speakers and topics for this conference call. Joanne will begin with highlights for Tapestry and our brands. Scott will continue with our financial results, capital allocation priorities and our outlook going forward. Following that, we will hold a question-and-answer session, where we will be joined by Todd Kahn, CEO & Brand President of Coach. After Q&A, Joanne will conclude with brief closing remarks.

I'd now like to turn it over to Joanne Crevoiserat, Tapestry's CEO.

Joanne Crevoiserat:

Good morning! Thank you, Christina, and welcome everyone.

As noted in our press release, our first quarter results **exceeded expectations**, showcasing the **brand magic** and **operational excellence** that are the foundation of our strategic growth agenda. Importantly, our **strong and consistent performance** is a credit to our **exceptional global teams** who continue to **navigate the dynamic backdrop with focus and agility, while positioning our brands and business for the future**.

[PAUSE]

Touching on the highlights of the quarter:

- **First, we achieved total revenue in-line with prior year on constant currency basis, outpacing our outlook and reflecting the benefits of our globally diversified business model – with continued solid growth at Coach.**
    - By geography, we achieved **international revenue gains of 2%** <u>at constant currency</u>, which included an increase of 27% in **Europe** and a 2% decline

in the total APAC region**.**

        - In **Greater China specifically,** sales declined 5%, consistent with the top end of our guidance range and ahead of the industry, which included a sequential trend improvement throughout the quarter. **Importantly, we are delivering a high level of <u>innovation, relevance, and value to consumers</u>**, while continuing to invest in our brands, teams, and platforms to support long-term growth in the region and with this important consumer cohort.
    - And, in **North America**, revenue declined 1% compared to last year, including an anticipated decrease in wholesale, **while profit rose, driven by gross and operating margin expansion.**

- **Second, we remained focused on building new and lasting relationships with consumers across our portfolio**.
    - During the quarter, we acquired **approximately 1.4 million <u>new</u> customers** in North America alone, with increases across all brands. Over **half of these customers were Gen Z and Millennials**, **consistent with our strategy to recruit younger consumers to our brands.** And, they continue to transact at a higher AUR than the balance of our customer base.
    - At the same time, we **improved lapsed customer reactivation** in North America – which highlights our ability to successfully engage our existing customer base as we welcome new consumers to our brands.

- **Third, we delivered compelling omni-channel experiences, engaging our customers wherever they choose to shop our brands**.
    - **To this end, we maintained strength in Digital, which grew high-single-digits versus prior year and represented over 25% of revenue at accretive margins**. Our Digital business is underpinned by Tapestry's leading capabilities, which have enabled us to enhance the consumer experience across their purchase journey.
    - **Our global brick and mortar sales decreased at a low-single digit rate in the quarter,** as expected, though we maintained strong profitability.

- **Fourth, we fueled fashion innovation and product excellence, as we remain focused on bringing creativity, quality, and compelling value to consumers around the world**.
    - **This is clearly on display at Coach, where we delivered continued growth in handbags, with AUR gains – underscoring the vibrancy of the brand and product offering.**
    - Our success is also reflected in our strong gross margin – as we achieved a record first quarter margin – with further opportunity for expansion long-term.
    - **Importantly, underpinning our margin gains is our agile supply chain – a key competitive advantage – which enables us to deliver craftsmanship and value globally,** while effectively adapting to the rapidly evolving landscape.

[PAUSE]

- Overall, we generated **record earnings per share**, **which exceeded our expectations, increasing at a double-digit pace compared to the prior year**, while making strategic investments in our brands and business. **Importantly, this outperformance enabled us to raise our guidance for the full year, consistent with our commitment to driving growth and shareholder value.**

[PAUSE]

Before turning to a discussion of our results in more detail, I'd like to briefly address the **pending acquisition of Capri**. Two weeks ago, the U.S. District Court granted the FTC's preliminary injunction, which we believe is incorrect on the law and facts. We appealed the decision, consistent with our obligations under the merger agreement. **While we await that outcome, it's important to reiterate that <u>we are in a position of strength and continue to focus on our compelling organic growth plan, building powerful</u>**

brands, and delivering for our consumers.

[PAUSE]

Now moving to our results and strategies by brand.

Coach continued to deliver standout results, highlighting the enduring power and relevance of the brand and its distinctive Expressive Luxury positioning. **Importantly, our teams are driving strong consumer engagement through innovative product, storytelling, and experiences, fueling our brand heat and growth**. To this end, during the quarter, we achieved 2% constant currency revenue gains at exceptional margins, highlighted by 330 basis points of gross margin expansion and a 90-basis point lift in operating margin with meaningful runway for growth ahead.

Now, touching on our progress in the first quarter – centered on our focus to deepen our connection with consumers to fuel continued desire for the brand:

- **First, we grew our leathergoods offering, led by our iconic handbag platforms and the success of new product introductions.**
    - The **Tabby** family once again outperformed, over-indexing with new and younger consumers and nearly doubling versus last year. The **Tabby Shoulder Bag 26** continued to anchor the offering, and we further expanded the family with the introduction of **Times Square Tabby**.
        - As we shared last quarter, based on the power of Tabby and in keeping with our commitment to put the consumer at the heart of all we do, we launched a test that brought the **Tabby 26 to our outlet channel at full price**. This test continues to exceed plan, and as a result we rolled it out to more locations – with Tabby now available in over 200 outlet stores globally, again at full price.
        - **Importantly, the learnings from this test continue to inform our broader strategies for FY25 and beyond, as we explore**

additional opportunities to scale innovative products and marketing campaigns across channels.

- In addition, during the quarter we launched **the New York family**, featuring the **Brooklyn and Empire bags** – which **surpassed our expectations globally and cemented their place as new pillars for the brand**. The Brooklyn Shoulder Bag 20 at $295 was the top recruitment-driver of Gen Z consumers, while the Soft Empire Carryall 40 at an AUR of $695 – was a viral sensation on TikTok. **Importantly, the New York family is incremental and differentiated**, with new minimalist branding, and soft leather that's clearly resonating with consumers globally. In fact, the early success **of Brooklyn earned it a spot on the Lyst, ranking second among the '10 Hottest Products.'**

- **Overall, Coach's growth in handbags and accessories continued to outpace the industry, which included mid-single-digit AUR gains globally, led by North America**. **And, we see further runway longer-term given our innovation pipeline and brand heat.**

[PAUSE]

- **Next, we remained focused on** **fueling lifestyle,** expanding the brand's reach in categories including footwear, ready-to-wear, and Men's - where we are underpenetrated and have a 'right to win' - by driving customer recruitment, purchase frequency, and lifetime value. We have a strong pipeline of innovation, notably in footwear, with **the launch of the new Highline sneaker in the current quarter**.

[PAUSE]

- **Turning to marketing… we continued to have meaningful conversations with consumers through <u>purpose-led marketing – driving cultural relevance and engagement with our brand</u>.**
  - This fall, we launched a new campaign **Unlock Your Courage**, featuring Coach ambassadors Elle Fanning, Naza, Youngji, and Charles Melton in a series of short films designed to inspire authentic self-expression – consistent with our brand mission.
  - Importantly, because of our efforts, we've seen significant gains **in unaided awareness, share of search, and purchase intent among GenZ consumers in the U.S. and globally** – **reinforcing brand momentum and that our strategies are working**.
  - **In addition, our campaigns and brand-building efforts are breaking through globally.**
    - **To this end, during the quarter we made the strategic decision to increase our top of funnel marketing investments across international markets, notably in China. This reinforces the confidence we have in our brand and product offering, driving greater consumer engagement and helping to drive outperformance versus the industry in China specifically.**

- **In addition, we also drove brand desire through <u>unique experiences</u>.**
  - **We connected with younger consumers in the world of gaming with a collaboration with Roblox & ZEPETO**. Since the launch, more than 12 million unique users interacted with our content, and we've seen an increase in brand consideration and purchase intent from consumers on the platform.

- **Overall, our holistic brand-building activities helped to drive increases in new customer acquisition** as we welcomed approximately 930,000 new customers to Coach in North America **<u>– a strong increase versus prior year</u>**. Of these new customers, approximately 60% were Gen Z and Millennials, consistent with our strategy to recruit younger customers.

[PAUSE]

Looking ahead to holiday, we will continue to focus on brand-building through customer engagement, executing our strategies with discipline. We are confident in our product pipeline, building on the traction we're driving in the business through the continuing success of Tabby, expansion of the New York Family, the launch of newness within our Coach Originals Collection, and a compelling assortment of seasonal novelty, reinforced by emotional marketing campaigns that **amplify our brand, purpose, and product**.

[PAUSE]

In closing, Coach is a storied brand driving modern relevance – fueled by a strong team methodically building sustainable growth. With customer understanding at the heart of our work, we continue to bring to life the brand's unique creativity, purpose, and value to a new generation of consumers, with significant runway ahead.

[PAUSE]

Now, moving to Kate Spade…

During the quarter, we continued to **reinforce our foundation for the future**. While revenue declined, as expected, profit margins again expanded versus prior year, led by continued gross margin expansion and diligent expense management.

Moving forward, **we have a clear imperative for growth**. Last month, we welcomed new brand CEO Eva Erdmann to the organization. Eva brings a strong track record of leading global consumer luxury brands and driving consistent, profitable growth. Eva and I share confidence in the meaningful opportunities at Kate Spade by **bringing a sharpened focus on brand building and enhanced execution. Importantly, under Eva's leadership, the team is working with intention to advance our long-term strategies, while acting with urgency to address the things we can immediately improve in support of this vision.**

Now, touching on our results for the quarter:

First, we remained focused on strengthening the brand's core handbag offering – key to our growth agenda.

- In September, we launched the **Deco collection** in Specialty, which is over-indexing with new, younger consumers at strong AUR and margins, while the **Phoebe** and **Spade Flower** programs in outlet remain foundational. At the same time, we also recognize that we need to amplify this progress through more **holistic brand-building initiatives** – **ensuring that we are distorting our efforts to telling more focused, cohesive, and relevant brand and product stories to drive consumer engagement – and that work remains underway.**

[PAUSE]

Turning to Kate Spade's lifestyle offering – during the quarter, **we delivered strong growth in jewelry, in keeping with our strategic intent**. This growth was driven by Millennial and GenZ recruitment, and we see continued opportunity ahead.

[PAUSE]

Next, we remain focused on maximizing the omni-channel opportunity to drive customer engagement and grow the brand.

- In keeping with this focus, in October, we launched a trial on Amazon, with a range of products, including an emphasis on gifting. The initial learnings are promising, and we see an opportunity to leverage the platform's broad consumer reach, specifically with younger cohorts –as we've successfully done with Coach over the last year.

[PAUSE]

<u>Turning to marketing, we are committed to fueling brand heat to drive consideration and accelerate customer acquisition.</u>

- **During the quarter, we acquired approximately 445,000 new customers to the brand – representing an increase versus prior year**. That said, we need to drive stronger outcomes, particularly in our core category, to achieve our growth ambition.
- To that end, over the last quarter our team launched new consumer insights ethnographic work to sharpen our focus and break through with the brand's target audience – and we've immediately implemented action plans for the holiday and into the Spring, which will bring more focus to our execution – from our assortment, to our styling, as well as our storytelling efforts. Importantly, we will **distort our marketing investment into upper funnel campaigns with more relevant messages for our target customer, capitalizing on the brand's strong unaided awareness in the U.S. to build greater brand desire and purchase consideration.**

[PAUSE]

Finally, we also continue to operate with discipline and a focus on maintaining a healthy brand and business – which is foundational to our ways of working and highlighted by our continued gross and operating margin expansion in the quarter.

Touching on holiday, our goal is to drive customer acquisition through focus and relevancy. To do this, we will lead with gifting – a hallmark of the brand

– while launching a social-first campaign that will celebrate the joy of the holiday season in a new and unexpected way.

[PAUSE]

Overall, while results for Kate Spade met our expectations in the quarter, we're not satisfied with the performance and we're <u>sharpening our roadmap for long-term growth</u>. This is a unique, purpose-driven brand with significant <u>potential with consumers on a global scale</u> – and we are leaning in with intention to <u>deliver sustainable, profitable growth</u>.

[PAUSE]

Now, turning to Stuart Weitzman…

We drove revenue gains for the quarter, with growth in North America offsetting continued softness in Greater China. Importantly, though financial results remain challenged we made progress in keeping with our strategic focus on brand building and delivering higher profitability long-term.

Touching briefly on our focus areas across product and marketing:

- During the quarter, **new styles**, including the **Vinnie** pump and **Naomi** boot families resonated with consumers, while growth in **flats** continued. In addition, we refreshed our **iconic styles** – which remain the bedrock of the brand. We launched new constructions to modernize and enhance the fit of key families, including Nudist and Stuart.

- **Product innovation drove traction at wholesale, with the business growing double-digits on both a POS and net sales basis in North America in the first quarter.** Further, order bookings year-to-date are up nearly 30% to last year. This will support an improvement in revenue and profitability trends this year and beyond – consistent with our strategy to drive growth in this important channel for the brand and category.

- Turning to marketing, during the quarter **we drove brand desire** through emotional storytelling in keeping with the brand's purpose of inspiring strength and confidence.
    - **Following the brand's 'How Lovely to be a Woman' campaign launch** featuring new, talented, and multi-faceted brand ambassadors, **we saw an increase in customer acquisition, Google search, and organic digital traffic in North America – which reinforce brand health and represent leading indicators of stronger business results in the future.**

For **holiday** – the key boot selling season – we are focused on delivering innovation across our icons and building on the early success of new introductions, while driving sustained wholesale growth, where's there's momentum. In addition, we will continue to deliver purpose-driven marketing with the rollout of additional chapters of our 'How Lovely to be a Woman' campaign.

Overall, we continue to see long-term potential for the brand, with an empowered team focused on driving customer engagement and improved financial results.

[PAUSE]

In closing, Tapestry delivered strong earnings growth in the first quarter, outperforming expectations. Our results continue to demonstrate the power of brand building, customer centricity, and operational excellence. I want to reiterate my appreciation to our exceptional global teams who continue to drive our success.

From this position of strength, we raised our outlook for the full year. We remain <u>focused and confident in the bold ambition we have for our existing brands and business</u>. I believe the best is yet to come for Tapestry.

[PAUSE]

Before turning the call over to Scott, I want to take a moment to recognize **Andrea Resnick**. This marks Andrea's 97th and final earnings call with Tapestry, ahead of her retirement later this year. Andrea joined the company to take it public and has had a truly amazing career.   She is an institution at Tapestry and a legend in the IR and Corporate Communication worlds. Andrea created a gold standard for thoughtful and transparent communications, which have become a bedrock at our company. On behalf of everyone at Tapestry, we are grateful for her many contributions and wish her all the best in her next chapter.

With that, I'll now turn it over to Scott.

Scott Roe:

Thanks, Joanne, and good morning, everyone.

Our first quarter performance continued to build on our track record of consistent and disciplined execution. To this end, in Q1 we outperformed expectations across revenue, operating income, and earnings, delivering strong EPS growth and cash flow generation despite the volatile backdrop.

[PAUSE]

Now, moving to the details of the quarter, beginning with revenue trends <u>on a constant currency basis.</u>

Sales were in line with the prior year and above our guidance for the quarter.

- These results were led by growth internationally, which grew 2% at constant currency. By region:
  - **Europe**, revenue grew 27% above last year, driven by increased local consumer spend and strong new customer acquisition, notably with Gen Z.
  - **In Other Asia,** revenue rose 10% led by growth in Australia, New Zealand, and South Korea, while **Japan** sales declined 4%.
  - And, in **Greater China**, revenue declined 5%, at the high-end of our guidance range. During the quarter, we again delivered Digital growth. And brick and mortar trends – while negative – improved throughout the quarter supported by better traffic trends which have continued into Q2. **Despite the overall challenging market backdrop, we are confidently investing in the region, delivering compelling product, and value, and positioning our brands and business for long-term growth.**

- In **North America,** sales declined 1% compared to the prior year, due to a planned decrease in Wholesale, while North America Direct was positive. Importantly, both gross and operating margin rose versus last year as we supported long-term brand health.

Now, touching on revenue by channel for the quarter.

- **Our direct-to-consumer business was in-line with the prior year**, which included a high-single digit increase in Digital revenue and a low-single digit decline in global brick and mortar sales.
- **Wholesale revenue was in-line with prior year,** which included International growth, including on Digital platforms where we continue to expand our reach.

[PAUSE]

Moving down the P&L, we achieved a **record first quarter gross margin**, delivering gross margin expansion of 280 basis points versus prior year. This year-over-year increase was driven by 180 basis points of operational outperformance, which exceeded plan, as well as a benefit of approximately 60 basis points from lower freight expense, and a 40-basis point tailwind from FX.

Turning to SG&A, we continue to make ongoing strategic investments in our future. To this end, SG&A rose 3%, led by higher marketing spend versus prior year and expectations, in support of our brand-building initiatives.

Taken together, **operating margin** increased approximately 90 basis points in the quarter, driving operating profit growth ahead of prior year and expectations.

And, first quarter **EPS of $1.02** exceeded our guidance and represented growth of 10%.

[PAUSE]

Now, turning to our balance sheet and cash flows…

- We ended the quarter with $7.3 billion in **cash and investments** and **total borrowings** of $7.3 billion, which reflects the bond financing related to the proposed acquisition of Capri of $6.1 billion.
- **Free cash flow** was an inflow of $94 million.
- **CapEx and implementation costs related to Cloud Computing** for the quarter were $30 million.
- **Inventory levels** at quarter-end were 9% above the prior year, reflecting a higher level of in-transits, consistent with expectations, **as we continued to leverage the benefits of our supply chain,** navigating the Red Sea and port disruptions with only modest impact. **Importantly, as we enter the holiday season, our inventory is current and well-positioned globally,** and we continue to expect to end Q2 and the full year with inventory above prior year.

[PAUSE]

Turning to our dividend program…

- Our Board of Directors declared a quarterly cash dividend of $0.35 per common share, representing $80 million in dividend payments for the quarter.
- For the fiscal year, we continue to expect to return approximately $325 million to shareholders through the dividend for an annual rate of $1.40 per share.

[PAUSE]

Now, moving to our guidance for FY25 which is provided on a non-GAAP basis… We are raising our Fiscal 2025 outlook, which incorporates our first quarter outperformance. We view this guidance as prudent and achievable, as we remain clear-eyed about the realities of the external environment, balanced with the opportunities we see for our business.

For the fiscal year:

- We now expect revenue of over $6.75 billion, representing growth of approximately 1% to 2% versus prior year on a reported and constant currency basis.
- Touching on sales details by region at constant currency…
  - We expect high-teens growth in **Europe**, where we are underpenetrated and have strong traction.
  - In **Other Asia**, we anticipate mid-single-digit gains, while in **Japan**, we're forecasting a low-single digit decline.
  - In **North America**, we expect revenue to be approximately in-line with to slightly above prior year, as we continue to support a healthy business.
  - And in **Greater China**, we expect revenue to be in the area of prior year.

- In addition, our outlook now assumes **operating margin** expansion over 50 basis points versus last year.
  - We anticipate **gross margin** expansion to drive this increase, due to improvements in both AUR and AUC. Both freight and FX are expected to have a negligible impact on gross margin changes in FY25.

  - On **SG&A**, we expect expenses to increase roughly in-line with the pace of revenue growth for the year. Importantly, we're continuing to diligently control costs, while investing in our highest impact growth initiatives, including making incremental investments in marketing versus our prior outlook. For modeling purposes, you can expect a modest decline in Corporate expenses versus prior year, while making ongoing investments in our brands.

- Moving to below-the-line expectations for the year…
  - **Net interest income** is expected to be approximately $20 million, which incorporates the Fed's 50 basis point rate cut in September, with some further rate cuts assumed throughout the year.
  - The **tax rate** is expected to be approximately 19%.
  - And, our **weighted average diluted share count** is forecasted to be in the area of 238 million shares.

- Taken together, we are raising our **EPS** guidance to $4.50 to $4.55, representing mid-single digit growth compared to last year and ahead of our prior guide of $4.45 to $4.50.

- Finally, we anticipate **free cash flow** of approximately $1.1 billion, excluding any deal-related costs.

- And, we expect **CapEx and Cloud Computing Costs** to be in the area of $190 million.
  - We expect around two-thirds of the spend to be related to store openings, renovations, and relocations, with the balance primarily related to our ongoing Digital and IT investments.

[PAUSE]

Touching on the shaping of the year…

- **We expect constant currency sales to be up slightly in the first half of the year**, **with low-single-digit growth planned in the back half of the year**.
    - In Q2 specifically, we expect sales to grow in the area of 1% to 2%, on a reported and constant currency basis.
- Turning to **operating margin**, we expect expansion in both the first and second halves, with the first half expansion led by gross margin gains and second half increases driven by SG&A leverage.
- **Taken together, we expect <u>balanced EPS growth</u> of mid-single digits for the first and second halves, with Q2 forecasted to <u>approach</u> $1.70.**

[PAUSE]

Now, to briefly address the proposed acquisition of Capri. We are appealing the district court's order, as required by our merger agreement, and have paused all integration planning efforts during this period. Given the present dynamics, we are not reaffirming the financial aspects of the deal and will provide updated comments if and as appropriate.

[PAUSE]

With that, I'd like to share with you in more detail how we're thinking about our **capital allocation priorities looking forward**. **Our capital allocation framework is focused on the goals of driving healthy growth and sustainable shareholder value.**

To do this, we have **<u>foundational commitments</u>**:

- First, to **invest in our brands and businesses** to support long-term, sustainable growth.
- Second, is our **dividend**, and we expect to maintain a rate of $1.40 per share in FY25, with a goal over time of increasing our dividend at least in line with earnings to achieve the stated target payout ratio of 35% to 40%.

<u>Beyond these foundational commitments, our robust cash flow generation</u>

<u>provides us with balance sheet flexibility for value creation.</u>

- To note, we are **firmly committed to our solid investment grade rating and our long-term gross leverage target of <u>below</u> 2.5x.**
- **Keeping this long-term leverage target in mind, there is a clear opportunity to utilize excess free cash flow for share repurchases**. **We have contingency plans ready, pending the outcome of the appeal, and we believe our shares represent a compelling opportunity given the strong organic growth runway in our business and this would represent our immediate priority** should we be unable to move forward with the proposed acquisition of Capri.
- And finally, consistent with our commitment to **being disciplined financial operators and allocators of capital**, we consistently evaluate opportunities for **strategic portfolio management**, utilizing our rigorous, four-lens framework to ensure all actions meet our strategic and financial growth criteria.

[PAUSE]

In closing…

- We **delivered a successful quarter, demonstrating our commitment to driving disciplined growth.**
- We achieved **<u>record</u> gross margin and EPS, with double-digit earnings gains,** as we remained focused on executing our compelling organic growth plan, **positioning us to raise our outlook for the full fiscal year.**
- **<u>Importantly, our distinctive brands, talented global teams, data-driven platform, and strong cash flow are competitive advantages. Together they provide us with strategic and financial flexibility to deliver accelerated organic growth and enhanced shareholder value in FY25 and for years to come</u>.**

[PAUSE]

I'd now like to open it up and take your questions.

[Q&A SESSION]