Pandora A/S

Transcript: Investor Presentation, Annual report 2018

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Operator

Welcome to the Pandora Annual Report for 2018. For the first part of this call, all participants will be in listen-only mode and afterwards, there will be a question and answer session. Speakers, please begin.

0.00.11

Michael Bjergby

Good morning everyone and welcome to this conference call for Pandora's full-year results for 2018. My name is Michael Bjergby. I am head of the Pandora Investor Relations team and with me here today in Copenhagen at the Pandora office I have our COO, Jeremy Schwartz, I have our CFO, Anders Boyer, and my IR colleagues Brian and Christian. Anders, before leaving the floor to you, please everybody flip through the disclaimer on slide 2. Anders, all yours.

0.00.42

Anders Boyer

Thank you, Michael, and good morning to everyone. This is Anders Boyer. On slide 3, you can see the short agenda for today starting out with the full year 2018 results and highlights. Then moving on to Programme NOW and this is where we will spend most of the call today before moving on to the full-year guidance and a couple of comments to that.

So please move on to slide no. 4. The key highlight for today is that we are announcing the next steps in the programme, Programme NOW. As you know, we launched Programme NOW back in 2018 in November with a change of the network expansion strategy as the first big step where we radically reduced the number of store openings and franchise acquisitions. And today, we are announcing the next four important steps and they are a commercial reset, it is about reigniting a passion for Pandora, it is significant cost reductions and it is about new ways of working. And Programme NOW is all about setting up the company to drive sustainable growth. It is a 2-year comprehensive roadmap that we have ahead and that is where we will be spending the majority of the time today. Another key highlight of course today is that we did deliver on the full-year guidance for 2018 with 3% revenue growth in local currency and an EBITDA margin of 32.5%.

On slide 5, you will find a few numbers for the full year of 2018. And our financial performance in 2018 was clearly not satisfactory. We did deliver on our latest guidance, and we did deliver substantial profits and we also did generate a lot of cash and that is obviously good but we also made two downgrades of our guidance during 2018 which you are all acutely aware of and that is why we call it unsatisfactory or disappointing results. But the revenue growth of 3% as you can see in the top left corner of the slide as well as the EBITDA margin of 32.5% in 2018, it was within the guidance that we made back in November. The important like-for-like KBI ended at -4% for 2018 and that compares to a flat total like-for-like in 2017. We did see that most bigger markets declined in like-for-like in 2018 but we also saw that the large important US market improved from -2 in 2017 to a +1 in 2018. And we also saw China improving throughout the year after having had a very difficult first quarter last year, we ended 2018 with a +4% like-for-like in China in Q4 after we had also just been slightly positive in the second and third quarters. I would also just like to highlight the good cash conversion that we saw in 2018 as you can see almost at the bottom to the left, 86% cash conversion in 2018 and that is the highest that we have had since 2014. And we do keep generating quite some cash and we returned DKK 6 billion to the shareholders last year as you probably know but we will also see later on in the presentation that we will keep transferring a lot of cash back to shareholders during 2019.

A few comments on slide 6 to the Q4 numbers. Essentially just three quick key messages around like-for-like, EBITDA and cash as well. Total like-for-like was down 7% in the fourth quarter and we also saw a low level of -5% back in Q1 of 2018 but like-for-like in the fourth quarter was the lowest level that we had seen during 2018. We had expected that like-for-like in Q4 would be low and we had included that in the guidance that we made back in November. But it emphasises the need for Programme NOW and it emphasises the need to change.

The EBITDA margin ended better than what we had expected in Q4. And especially considering that we are in the low to mid end of the revenue guidance for the year and the EBITDA margin ended above the midpoint of the full-year guidance and that means that Q4 specifically was almost 36% EBITDA margin and it is among others the initial impact from Programme NOW cost reductions which are visible in the Q4 margin. When you dig into the cash flow numbers for Q4, specifically we also see that the effect of the change of network expansion strategy that we announced back in November is visible and the cash flow related to M&A in the fourth quarter was only DKK 83 million compared to DKK 1.1 billion for the full year.

Moving on to slide 7 and the revenue bridge for Q4 Y/Y, you will note on this slide and on slide 8, the next chart, that we have put numbers on the waterfall charts and we hope and believe that that should be helpful for you in understanding how the business develops and what the drivers are between last year and this year. It is, I should say, rounded numbers that we put on the chart and therefore, it does not add fully up if you try to make the math across the chart. Forward integration still contributed quite a lot in the fourth quarter to revenue growth even though we did not sign any new deals during the fourth quarter but we will obviously see a run-rate impact of all the acquisitions that we already made for some quarters still but it will go down quarter by quarter as we go through 2019.

And as you will see later on for 2019, we guide with an impact for the full year of 2 percentage points revenue growth from forward integration. You will probably also note that the bucket here in the chart that we call timing of shipments & other – it is smaller than in the last quarter, Q3, and there are indeed less one-off like elements in the fourth quarter compared to prior quarters. And that bucket, timing of shipments & other that also includes the net impact of various other items like continued destocking in the wholesale channel and some impact from closing multi-branded points of sale.

On slide 8, we have an equivalent EBITDA margin bridge and, as I just said, the EBITDA margin did end stronger in Q4 than expected but the margin was obviously quite heavily impacted by deleverage that we see in the business as a consequence of the negative like-for-like and with the gross margins that we have, it hits pretty hard on the EBITDA margin and that is the -3 percentage points bucket that you can see on the chart here.

The forward integration impact will gradually disappear. The technical forward integration impact will gradually disappear during 2019 as we gear down on forward integration but in Q4, it still had a negative impact of around -1 percentage point compared to the fourth quarter of 2017 and that is the first building block that you can see in the chart here.

And as you can also see, we have been able to offset some of the negative leverage impact through cost reductions but it is only partially and cost reductions support the margin by around 150 basis points in the quarter and all in all, we are pleased with that and pleased to see the almost 36% EBITDA margin in the quarter.

Lastly, a small nice story on cash conversion and cash generation in the year and the quarter. And as I just said, the cash conversion – that is on slide 9 – our cash conversion in 2018 was the highest since 2014 as you can see to the upper left part of the chart and that goes hand in hand with the reduction of working capital by around 2% of revenue which you can see to the lower left-hand part of the chart. And the biggest driver in that was an increase in trade payables and that follows the decision that we made back in August last year to tighten the payment terms with suppliers so in 2018, we have actually had a positive cash flow from trade payables of DKK 762 million due to the intensified focus on this area. I am actually quite happy with that. And we also had a lot of focus on DSO both in Q4 and Q3 and we saw the Days Sales Outstanding (DSO) decreasing down to 50 days in the fourth quarter and that is more or less flat compared to the 47 days back in Q4 of 2017. We are actually not fully where we want yet but getting to a flat DSO Y/Y after having had some quarters with a significant increase is a good step forward. But now it is time to dig into Programme NOW and Jeremy, please.

0.11.08

Jeremy Schwartz

Thank you, Anders. So let us have a closer look at Programme NOW. Please turn to slide 11. I want to first remind you that Pandora's Q4 results, as Anders just said, we announced the launch of Programme NOW, the immediate decision to stop the buyback of franchisees and the scaling back of store opening plans. We also said that we would share our situation diagnosis and next steps at this investor call and that is where I shall start.

The diagnosis involved consumer studies and focus groups surveying around 28,000 people worldwide to understand consumer needs and behaviours, Pandora's brand health and the appeal of the product design and shopping experience. We have also done a rigorous deep dive into Pandora's business to find any consistent patterns across countries, channels, products and retail metrics that are significant. All of our cost lines have been scrutinised and significant opportunities to improve the cost base have been found and finally, our company-wide processes, structures, capabilities and the way we make decisions have been reviewed. As a result, we have implemented significant changes and created the next major steps on the Programme NOW.

What we believe as a management team is that Pandora has the potential to restore long-term sustainable growth and shareholder value.

Please turn to slide 12 to share the diagnosis. We have identified four key interconnected causes of our like-for-like decline. I will go through each of these starting on the left. We found the brand has what we have called a blurred brand experience. Because although Pandora has the highest industry-prompted brand awareness, the brand positioning promise and storytelling needs to be sharper and more culturally exciting with more impact across all touchpoints digitally, socially, on eCommerce and in stores in order to recruit new consumers around the world today.

Our next item: Weak initiatives on charm collecting. Although Pandora sold more than 900,000 charms per week, bracelet sales are increasing and good progress is being made on innovation. The whole company needs to pursue a stronger initiative to drive buyers and non-consumers to buy and then return to buy more bracelets and more charms to grow their collections.

Next is what we have called Over Push. The brand's expansion in countries and the stores in eCommerce has made the brand more available to more consumers worldwide but the recent intensity of the promotional activities as well as an immature merchandising and assortment process may be changed and must be changed to protect and enrich the brand equity, execution and consistency.

We have strong competencies but the global direction and executional speed and impact has been compromised by the way we go to market locally and this is changing as we speak. These four issues are being forcefully and forcibly addressed to build on the strong Pandora foundation and DNA.

Please turn to page 13. As you know, Pandora is the most well-known jewellery brand in the world. Not simply because it sells charms but because Pandora's magic product DNA, its manufacturing craftsmanship and value for money created an idea that has had universal and timeless relevance for people and of course generates shareholder value so it is worth restating Pandora's magic product DNA. We create precious miniaturised little jewels that frankly others struggle to match. Each piece contains a meaningful human story and what every brand is seeking today, personalisation. The whole Pandora concept is personisable with stories that every woman can apply. Now, you know this about our charms but the Pandora magic DNA applies to all our categories. For example, our three wishbone rings can represent three children or three friends. The feather earrings are precious with 99 stones set in them and more and more necklaces are being worn in layers and are being personalised. So we will grow all our other categories. But to arrest our decline, we have to focus on reinvigorating the charms business.

So let me talk you through our specific charms initiatives on the next slide 14. Our research shows that charms are in demand. In fact, 73% of all charm owners of Pandora say they will buy new bracelets and new charms once they finish building their current bracelet. A third of all Pandora owners have several bracelets which they interchange for different styles and when they have different moods. And yet, 74% of the non-owners who actually would consider buying Pandora know very little about Pandora charms.

Now this is where it gets interesting because our research shows that we have strong assets to leverage. Pandora actually answers a significant underexploited global consumer jewellery market needs space. It is to help women express their individuality and that is exactly what our charms help women do.

In addition, we are a cross-generational brand. In fact, I have been pleasantly surprised on arrival here to see how we as a brand right now are recruiting Gen Z customers and even younger than that and Millennials right through to baby boomers which we all know many brands would like to say they do too.

On the right you can see that to respond to this, we are building a charm collecting system. First of all, we need to attract new customers by innovating new bracelets, charms, having new collaborations and limited editions and using all of the best marketing resources that we can rally to hand.

Leading the way women wear and style their multi-charm bracelets in our advertising with influences and social media, online and in store is a key objective of ours. And then driving multiple-charm collecting, not least by inventing a digital first reward system to drive loyalty and capture rich data – something that Pandora is so lacking today. But none of this is business as usual. It requires disruption.

Please turn to the next slide 15. In a world where consumers are overwhelmed by marketing messages and choice, we need to create a disruption to the Pandora brand. Disruption in a positive sense. And our vision is this: First, to make the brand come alive by expressing the brand in a culturally relevant and sharp way across all our touchpoints to re-excite customers to actively re-engage with us. We need to step change the habit of collecting by attracting new and lapsed consumers to buy, to wear, to collect charms complemented of course by our other categories. We will act with commercial responsibility, creating a healthier promotional activity, control range of products and becoming more agile in the wholesale channel. We will pursue executional excellence with the global leadership setting the plans that the countries will execute excellently on eCommerce, in stores and with franchise partners. And finally, this will be underpinned as we push the pace to capture data and drive personalisation across social, eCom and omnichannels. All of this is captured in Programme NOW.

Please turn to the next slide. And it is in what we are calling: Reigniting a passion for Pandora. This is the Programme NOW transformation of the consumer experience across all touchpoints.

Please turn to chart 17. Reigniting a passion for Pandora is the cornerstone of Programme NOW. There are four major steps of Programme NOW which we will go through one by one in the next slide. Excuse me. A commercial reset, reigniting a passion for Pandora, reducing costs and implementing new ways of working.

Let us turn to slide 18 to see how these are implemented over time. Along the top, you can see time and you can see then the four work streams. The commercial reset has already started in Q1 and will continue all year as we adjust our promotional plans and adapt our inventory levels. The work streams of reducing costs and implementing new ways of working have started and will continue for the 2-year transformational period as we remove costs, build capabilities and improve processes.

Now 2020 is an important year for Pandora. It is the 20th anniversary of the launch of the Moments charms and bracelets platform. Now a celebration like this gives us the perfect springboard to re-engage new and existing consumers with our brand and therefore 2020 is the year to ignite a passion for Pandora. However, with Q4, Singles Day and Christmas being such a critical moment to attract new customers and drive sales, we see this as actually the true start of the initiative Reigniting a Passion for Pandora and aim therefore to make Q4 bigger and better than ever before. Until that time, the teams are working on the contents that can be brought to market at that time.

Now, let us look at the concrete actions in each of the work streams in more detail. Please turn to slide 19. And I am going to start with the commercial reset and on the left. The commercial reset is the right thing to do for the brand and the business but it will have a negative short-term impact. Firstly, we are reducing our promotional intensity outside of the key gifting and retail promotional periods to both protect our brand equity and allow us to amplify the product launches between promotional periods. At the same time of course, as the next point, we will continue to amplify specific promotional periods such as Mother's Day, Chinese New Year, Black Friday in the sale and we will continue to develop new brand building as well as price promotional mechanics. At this stage, we estimate the net impact to be around -2-4 percentage points on like-for-like in organic growth but of course, we are seeking to amplify our non-promotional activities to neutralise this at the same time.

On the right: We will optimise our wholesale inventories and we will reduce the size of our NPI sell-in packages. That is our new product, sell-in packages, because this will reduce the initial stock purchase but will allow our customers to accelerate the re-ordering of faster selling products and reduce the stock build-up of potentially slower moving products that we have launched. We estimate this will have an organic growth impact of around -1 percentage point.

We are also initiating an inventory programme to take back some of our slow-moving residual old stock in selected markets and this will have a negative 2 percentage points impact on EBIT. Now, these are tough decisions to make because of the short-term negative impact which of course we don't take lightly.

But it is absolutely vital for the long-term health of our brand to create a strong foundation for reigniting a passion for Pandora and to attract new and lapsed consumers.

Please turn to slide 20. We have already started working on 5 key areas to reignite a passion for Pandora and on the left is where we are today and on the right is how we see each work stream unfolding towards customers. Let us start with the brand where we have a new promise. We are working on a new visual identity, digital assets and communication is being developed. We aim to launch a new brand communication and social engagement that will be both strategic but also disruptive from the end of 2019.

Our new products. We are developing new products and do this while we are rationalising the assortment so that the new products match the new brand promise and in 2019 through 2020, we will launch new products including a new charms bracelet platform, new collaborations that we have never done before, limited editions and many other exciting products that I can see are in development.

And we are going to do this at different price points with specific entry price ones too to recruit those new consumers who are slightly more price sensitive. In media, we are testing econometric modelling and personalisation to validate elasticities in what we call the upper and lower funnel of recruitment, i.e. new consumers versus existing consumers and in Q4 2019, we have allocated an increased media budget to our base investment which together will amplify our new content with progressive targeting of new and lapsed consumers.

Coming to eCommerce, something I think you know that I am passionate about since joining Pandora has been to transform our eCommerce omnichannel data and loyalty reward offer. With the current retail environment continuing this rapid change, of course eCommerce is absolutely key for us and an area where I know Pandora has not been on the forefront of development. Right now, we are continually improving what we can call the basics of product landing page with more consumer-relevant and inspirational content and storytelling and of course, we are continuing to accelerate our omnichannel roll-out in the US while at the same time, we have kicked off and are starting our loyalty award programmes scoping and development but the more material changes investments are being conducted to step change our position in eCommerce and omnichannel and they will become progressively more evident in Q4 and of course through 2020.

At the same time, we do hope to start piloting our new loyalty scheme and accelerate data capture to underpin our personalisation and clienteling strategy. Finally, in stores we have started to design a new store concept. It is focused on the merchandising and the product navigation first and foremost as well as creating a more inspiring and engaging environment.

We have an ambitious goal. It is the pilot stores at the end of this year and then take some of the inspirational elements and put them across the prime areas of our estate so that we can signal change.

Just for clarity, from a store CAPEX point of view, we are working within the existing spend per store, although we will now grade the investments by store format and turn every potential so that we can flex the investments, which we don't do now.

In addition, the roll-out programme is targeting end-of-lease refits and new store openings though we have allocated some of the 200 million of CAPEX that you know about for some of our prime locations which we may need to bring forward the refit in case from the end-of-lease date.

Please turn to page 21 for a review of the next work stream of Programme NOW. To better act as one global company, we are starting a journey to change the way we operate as an organisation. In order to create that sharp, compelling brand, we are making our chief creative officer, Stephen Fairchild, fully responsible for our global brand execution alongside his role leading product development.

We created and are operating now a single global to local trading calendar. And this has been implemented with up to 14 trading periods by country to allow us to amplify product launches separate to the promotional activation. To build world class leadership competencies, we are creating a new global merchandising function which to date has not existed in the company and I am very pleased to announce that we have recruited a senior vice president for global merchandising effective immediately.

Thirdly, we are in much closer dialogue with the franchise and multiple-brand partners to rebuild a sense of partnership and I am personally involving myself by participating in annual meetings and events.

Finally, we are creating a stronger performance culture. One where we are changing and aligning the incentive programmes with shareholder value creation. One where we will have one set of numbers and one where we will have and do have now a monthly performance review and comments at the KBIs.

Now, I have been through three of the four work streams of the programme now and I will hand over now to Anders to the final piece.

0.28.56

Thank you, Jeremy. On slide 22, we have some details on the cost reduction opportunity and the cost reduction opportunity is quite big and also bigger than we thought when we started our diagnosis some time back. And it should be recalled that the DKK 1.2 billion opportunity comes on top of the DKK 350 million we announced back in connection with the Q2 announcement in August last year so in total those two buckets together are something like 7% of our revenue and I guess when you see such a big number you may wonder whether we are moving into dangerous territory or whether we are too aggressive and we don't think so because most of the cost reduction levers you can see on this slide are more of a, I guess you can call it tactical nature than some fundamental change in the structure of the company. So we have divided the cost reduction opportunity into 5 categories and we will follow up on progress on these throughout the duration of Programme NOW and for each of these categories, we have shown to the right on the chart here a cost reduction range and as you can calculate, it would sum to between DKK 1.0 billion and DKK 1.4 billion if you take either the low end or the high end of the range, respectively, and on average, as we have stated here, we expect to land at around DKK 1.2 billion in further cost reductions.

As you can also see on the slide here, there is no one big silver bullet cost reduction bucket which accounts for a majority of the cost out, but it is several smaller components which then add up to the DKK 1.2 billion.

We are in fact in full execution mode on several of the levers here already and that includes among others travel expenses, points of sale material and several of the levers within cost of sales. And I should also mention that earlier today, it was announced that we have had to reduce our work force in Thailand by around 700 employees as part of that programme. Of the DKK 1.2 billion, we expect to realise DKK 600 million already here in the calendar year 2019.

As you can see on slide 23, Programme NOW is obviously a core part of what we will be doing and working on during 2019 and 2020 and therefore, we will obviously follow up on it quarter by quarter until the programme ends and when we meet next time in May, we will update you on the progress on the cost reductions, the commercial reset, but not least dig further into the initiatives within reignite a passion for Pandora.

Then before we get to the Q&A, I will just spend a couple of minutes on the guidance starting on slide 25. I think many of you had already guessed that we would be changing our guidance metrics in 2019. We have discussed that with several of you and we have also mentioned it in connection with both the Q2 and Q3 announcements in 2018. So going forward, we will be guiding on organic growth and on EBIT margin and we believe that both metrics better reflect where shareholder value is created in a company like ours and then obviously, the implementation of IFRS 16 makes the EBITDA margin somewhat off KPI going forward.

And we hope you agree and that it makes sense to you as well. But when we change guidance metrics and then at the same time we go through a significant transformation, we understand and realise that it can be difficult to track the numbers so therefore, we have decided to provide quite some specific assumptions and building blocks for 2019 and hopefully, that helps you understand the big drivers of the financial performance in 2019.

On slide 26, we have shown a waterfall for the revenue growth in 2019. And we have separated it into two buckets, one being the normal business I guess you can call it and that is what we have labelled "before commercial reset". If you look at the upper left-hand part of the chart. And after those two building blocks, we have the impact of the commercial reset. And the reason we do that obviously is that the commercial reset is of a one-off like nature and it is a deliberate decision that we have made and it will impact the revenue in 2019. In 2019, we expect to add about 75 concept stores to the network down from the 250-259 that we have opened net in 2018 so that is a 70% reduction in the net openings going into this year.

And as you can see on the chart, the expansion of the network is expected to add around 4 percentage points to organic growth this year. Total like-for-like is expected to be negative down to high single digit and that is what you can see in the grey text box above the waterfall. And that high single digit, up to high single digit negative like-for-like includes the impact from the commercial reset. Excluding the impact from the commercial reset, total like-for-like is expected to be mid-single digit negative. And that then will take us to organic growth between 0 and -2 excluding the impact from the commercial reset and that is the second grey/black bar that you can see on the chart here. The sell-in packages then are expected to reduce organic growth by 1 percentage point as Jeremy mentioned earlier on while the reduction of promotions will impact like-for-like and organic growth equally by around -2 to -4 percentage points.

And consequently, the organic growth guidance that we are putting out today is between -3 and -7% in 2019. When we look at the total reported revenue growth, forward integration obviously has an impact as well. That is not included in organic growth but forward integration will positively impact total revenue growth by around 2 percentage points in 2019 and that includes all the forward integration deals that have already been completed in 2018, including the acquisition of the distributor in Taiwan.

And that then means that total revenue growth in local currency is expected to be between -1 and -5% in 2019.

On the EBIT margin guidance on slide 27, the starting point to the left obviously is the actual number for 2018, the 28% EBIT margin. The first building block is then the margin enhancing elements that we mentioned back in connection with the Q2 2018 announcement. As you may recall, then back then we mentioned the opportunity to improve the margin by 3 percentage points due to among others less forward integration, lacking wholesale destocking, cost reductions etc. and that is still the case except that the wholesale inventories are still expected to destock further in 2019 and thus the margin improvement in 2019 from these elements is 2 percentage points.

And then after that we have the net impact between the DKK 600 million NOW cost reductions and the DKK 500 million NOW reinvestments into the business that we are making. That is the +2.5% building block and -2% building block. Then going a little bit further to the right, you have another bucket of -0.5 percentage point and that includes a couple of different things, higher production time on new products but also the small upside from converting to IFRS 16 and that is about the +30 basis points impact or so. That takes us to the EBIT margin guidance of 26-28% before restructuring costs and the other upper end and this means that the upper end of the guidance for 2019 is in line with the actual EBIT margin in 2018 of 28.2%.

The restructuring costs in Programme NOW and in 2019 are quite large and that shows both the size of the transformation that we are going through but it also shows something about the size of the cost reductions that we are pursuing.

And in 2019, the restructuring costs are expected to amount to around 6 percentage points of revenue or up to DKK 1.5 billion and that consists of the cost of the inventory buyback programme that is around let us say DKK 0.5 billion, DKK 500 million and that is the single biggest element of the restructuring costs and the remaining 4 percentage points are about the programme execution as such and that includes 3 main buckets, the first one being cost related to reducing cost, terminating contracts, severance payments etc. It is about cost related to consultancy support and I should mention that part of that is partly success-fee based and it includes thirdly one-off costs related to defining the new brand and the new store concept and including some potential write-downs of capitalised store fixtures and points of sale material.

Last on the guidance on slide 28, just starting out with a more accounting technical comment and that is that we are changing the target for the capital structure policy to reflect IFRS 16. It is a pure accounting matter and that means that our capital structure policy will be changed from currently between 0 and 1 x net interest-bearing debt to EBITDA to between 0.5 and 1.5 x EBITDA.

For 2019, the Board of Directors and Management propose total cash return to shareholder amounting to DKK 4 billion and that is around 13-14% of the company's market cap as of today. And in line with our cash distribution policy that we have announced together with the annual report back in 2016, we propose a dividend of DKK 18 per share and a share buyback programme of DKK 2.2 billion.

As we are stating here in the first bullet on this slide, we will obviously also look at the leverage ratio excluding restructuring costs when we consider the amount of cash returns to shareholders and consequently, it might be that the reported leverage ratio including restructuring costs temporarily exceeds the upper end of the new capital structure interval during 2019.

Before we get to the Q&A on slide 29, we clearly have had our challenges during 2018 but it is also clear to us that Pandora has some very strong assets to build on. A cross-generational brand, a magic product DNA, a large global network across touchpoints and not least state-of-the art crafting facilities. And based on these assets, we do see a way back to sustainable growth and that means positive like-for-like and we do see a way back to maintaining continued industry-leading margins. And we say that because we have laid out a comprehensive 2-year roadmap as part of Programme NOW based on the diagnosis that we have made and we say it because we have identified significant cost opportunities which will both allow us to invest significantly in growth initiatives while at the same time supporting our margins. And that is why we call our equity story a turnaround opportunity and not a turnaround in a classical sense but a turnaround in the sense of the belief in the future of Pandora and thereby a turnaround of the multiples that our company is trading at.

That concludes our presentation. Now we are ready to move on to the Q&A.

0.43.29

Operator

Thank you. Ladies and gentlemen. If you wish to ask a question, please press 01 on your telephone keypad. Our first question comes from the line of Chiara Battistini of J.P. Morgan. Please go ahead. Your line is open.

0.43.45

Chiara Battistini

Good morning. Thank you for taking my questions and thank you for the extensive presentation. The first one would be if we can go back to the products and the strategy on the products. Can you talk more about the initiatives – the initiatives you are planning to implement how you are planning to prioritise the charms and the bracelets of all the other categories and how you see the balance between the core so the charm bracelets and the other categories and also how you think about the product cycle and the product innovation given that that was a very big focus at the beginning of last year. And the second question would be on the CEO, if you could give us an update on the CEO appointment and where you stand on that if you are still actually actively looking for one as there was no mention in the press release this morning and also can you remind us what kind of profile you are looking for for a new CEO and what kind of company you are trying to hire him from, please. Thank you.

0.44.44

Michael Bjergby

Thank you very much for these questions. I think as the IR with number two that the CEO is still – the search for a new CEO is still progressing and there is no news on this so far and then handing over to, I think, Jeremy for the question on the product strategy.

0.45.02

Jeremy Schwartz

Yes, thank you. Thank you for your question. I think the first point I want to make is and the reason for talking about the magic product DNA is for us all to realise that Pandora has an idea that applies equally to all categories so to remove or reduce the thoughts of either/or or one or the other, we are able to increase all the categories, however, as I have stated we have to focus and prioritise when you have four or five categories that you are seeking to grow. Not least for our efforts and not least for our store staff. And therefore, we are going to return our efforts and our thinking and our time to growing the collectability of charms and bracelets while at the same time bringing this idea of collecting to the other categories, but I will express the priority so the priority is charms and bracelets and the collecting of those. Next will be necklaces because we see that we are performing well there and we have headroom and the collectability and the style of wearing multiple necklaces is growing. We will continue to focus on rings because again, interestingly from a stylistic point of view, the multiple wearing of rings is hot and that will be the priorities that we will take. You talked about product lifecycle. I think there are two elements there. I come from a school of thought that fundamentally believes that brands and businesses have what I would call core icons. It is those things that are growing year after year, that make up the core business, that have something about them that is timeless and one needs to nurture and grow those at the same time as you think about innovation and we will do that and are focusing back on the core icons alongside innovation. In terms of product lifecycles you know we are seeking new icons with the launches and we will succeed with some where something just hits the money and an example is on the rings for example it is a wishbone ring which I mentioned. I only mention that because again it has got a sort of timeless capability to represent the product DNA and new generations can understand that and connect. But other things, we need to create what we are calling engineering scarcity so the reason we mention here specifically collaboration and limited editions is that marketing now is not just about advertising or promoting something new. It is leveraging scarcity to create demands and therefore, the product lifecycle with some products will be extremely short so that we can create that excitement and those queues that Pandora is so famous for outside our store and online. Thank you.

Chiara Battistini

Thank you very much so … what about the product and the number of SKUs we should be expecting pure SKU versus what we had in the past and maybe more focus on these shorter-term collaborations or..

Jeremy Schwartz

Right so the answer is yes to your question and I will give the why. The why is because in order for us to cut through all of the marketing noise in the world that I expressed we need to be clear to the consumer which are the key products that we personally believe are what I would call show stoppers. Things that we want millions of people to buy and to do that, we will have to reduce the number of the products we are launching and tighten the existing assortment to improve our navigation and shopability both in stores and online.

Chiara Battistini

Thank you very much. Thanks.

0.48.53

Operator

Thank you. Our next question comes from the line of Elena Mariani of Morgan Stanley. Please go ahead. Your line is now open.

0.49.02

Elena Mariani

Hi, good morning everybody and thanks very much for the extremely detailed plan. Two questions from me. The first one is a bit more on the medium-term plan. 2019 seems to be like the start of your journey. How should we think about 2020 and the following years so in essence, how long do you think it will take to fully implement this extremely comprehensive plan? Do you expect in 2020 to go back already to positive like-for-like and to profitable growth? And what do you expect could be your sustainable EBIT margin in the medium term? You are talking about like-for-like growth that could be low to mid-single digit as a mid-term financial aspiration and how about your EBIT margin target? And question number 2 would be on your distribution network. You don't seem to believe that your network is too big and you don't seem to be overdistributed. Do you expect to perhaps consider some store closures as well given that at the end of the day, you are growing very well in your eCommerce platform and perhaps in some of the markets, you might have opened too many stores? I can see from your 2019 guidance that 4% of your organic growth is going to be driven still by store openings. How should we expect this to evolve in the future? And I know I am allowed to ask only two questions but one small follow-up from Chiara's one. Jeremy, would you be open to consider the CEO role – just in the remote case you were asked by the Board? Thank you.

0.50.47

Michael Bjergby

Thank you Elena. I think I will just start out to say that we are not guiding in 2020 and we do not have the guidance for the mid-term but maybe Anders you can provide some comments on the cost programmes and the investments that you see are required.

0.50.59

Anders Boyer

Yes, thanks. Hi Elena, it is Anders here. I thank you for that introduction, Michael, because it is too early to be specific about 2020 yet but I guess a couple of things and points we can give and obviously I think that 2019 is expected to be sort of the biggest transition year if you like and as always in transitions like this, you get the cost before you get the benefit and that is typically how it works out so looking at a couple of data points I think I can give you can call that. Obviously 2019 will be impacted by the commercial reset. Both on the top line and on the bottom line and with the numbers that we have just gone through and obviously, those are of a one-off impact and then going into 2020, we should obviously, you will see the run rate impact and additional impact of the cost reduction opportunities. We will not get all the way to DKK 1.2 billion in the calendar year 2020 but as a run rate that is where we will get by the end of 2020 but exactly how that plays out on the bottom line depends on decisions that are still to be made on how much are we reinvesting in the business to drive the top line, but at least we know there will be more cost reduction opportunities flowing into the P&L come 2020.

0.52.38

Jeremy Schwartz

Thank you. I will take the next question. I think the first point is that as we have noted, we will have a net opening of 75 stores and as we have indicated, those will focus on Latin America and China and we can see great opportunity in places like Colombia, like Mexico that we are actively developing and of course China as we said. The second point is within that net number there are the natural closings that we are doing as we are finding some malls in certain areas are becoming less popular and we have come to end-of-lease and that makes good business sense. We are looking at other markets where we can see opportunities. The likes of UK and Italy. But unlike some other retailers, we have a margin structure which means that from a prioritisation point of view, reigniting the brand, the priority areas for us to put our energy in – i.e. on the things we have expressed before and ahead of a significant network redesign. That is not to say it has not been worked on but it is not a key message to say in terms of our transformation project. Thank you.

0.53.55

Elena Mariani

Maybe the CEO question?

0.53.59

Jeremy Schwartz

Yes I don't think it is appropriate to make a comment like that, but thank you for the question.

Elena Mariani

Thank you – thanks very much.

0.54.04

Operator

Thank you. Our next question comes from the line of Lars Topholm of Carnegie. Please go ahead, your line is now open.

0.54.12

Lars Topholm

Thank you and congrats for reaching your Q4 guidance. I have two questions for this round. So, to begin with, your new plan includes, I understand it as 14 events instead of 10 drops. It includes smaller sell-in packages, which means that franchisees have to rely more on replenishment orders which presumably will go up and also a new concept to be launched in Q4 2019. And my question is, doesn't this add more complexity that could potentially put stress both on your supply chain and your production or how do you see that? Maybe specifically in the light that our understanding is there is still problems with delivering certain sizes of the reflection bracelets for example so the question is, how are you sure your organisation is ready to handle increased complexity? And then a question number two, if I may, because you provide the building blocks for your guidance but 16% of your 2018 revenue came from wholesale multi-brand dealers. How do you expect that to perform in 2019? Thank you.

0.55.41

Jeremy Schwartz

Well, perhaps I will answer a couple of those and we will share. So, I think, you know the first point is one of those aha-moments when this company as we have stated has been through a pioneering phase of opening countries and stores to create this great global network but in so being focused in the pioneering phase, it was not necessarily working as a global company and that is why we have made that point. What we actually discovered in the first weeks was that most retailers operate a trading event plan with between 10 and 14 separate activity events, that is the nature of in a country having holidays, having launches, having promotions, having weekends and paydays. But actually at the global level, the company was running a cadence around drops, that was the language of the centre, and that was focusing really simply on new products, well, as you know, a business in retail does not just operate on new products and as I have expressed, it is about driving the core and therefore there was a disalignment between the way the business was thinking such that by simply saying we will operate as a great retailer, both ecommerce retailer and store retailer and have one view of the world in which the products have to complement and the promotions have to work beside and with and the holidays have to be amplified, we will have coherence and less complexity and that is what we are achieving. Second point, so hopefully that is a clear answer and absolutely, it is about less complexity and more clarity across the whole business. On the small sell-in packages, as you know, Lars, because I have just been with the 900 franchisees of the US, Canada and South America last weekend, talking to them, and actually, we all believe in a sell-out just in time model for efficiency. So, the smaller sell-in pack will ensure that within that NPI launch, if there happened to be some items that are slower selling that the franchisee or the wholesaler will not then have a large number because the pack would have been large of an item that doesn't sell so well and therefore have to deal with the complexity of then clearing that through some lower price or sale or holding onto stock until another time but rather can now, as sales become evident, order the things they want more quickly and have less of the things that aren't selling so well. In terms of a new concept, you know, of course our job, and that is why we are creating a new global merchandising function, is to balance the need for all frankly consumer companies to stimulate demand through innovation and driving the core with managing complexity of that very fact and one of the things that we have not been great at planning is as the first question life cycle management which is the ability to actively remove items which are not moving fast and ensure that the range does not expand because of that lack of active discontinuity. So, our job is to work out and we will work out how to do that. In terms of the last point, you know, we haven't really had a supply issue on the Reflexions bracelet, funnily enough, we have had just an issue with the sizing and that issue has now been addressed so we are in a good stage there and hopefully, that sort of mistake won't be repeated. Thank you.

0.59.25

Lars Topholm

Just to follow up, Jeremy, on your comments regarding the smaller sell-in packages, I clearly see the value proposition from the franchisee's perspective that they can run smaller inventories but my question was more if your supply chain and production can handle a situation where you have more replenishment orders or if you move towards what you can call a more just in time principle in supply, does this mean that you just move the inventory from the franchisee to Pandora itself?

1.00.02

Jeremy Schwartz

No, I fundamentally believe we have absolutely the capability of doing that and I think the best proof is that we run an ecommerce business which is about just in time of delivery of small packages. It is true that in the US, we have had some issues in the last quarter but as we have indicated, we are on the case and sorting those out and that was more to do with, as you know, a new system we put in place that had some hiccups. We just said as it is but that is being sorted and I am confident we will work that through.

1.00.34

Lars Topholm

Thanks. And then on the multi-brand revenue assumptions for 2019?

1.00.42

Anders Boyer

Thank you on that. Multi-brand was quite significantly down or other points of sale quite significantly down in 2018 and we do expect that channel to reduce or decline in revenue still in 2019 and I guess one way to look at it is that there are free components of the development in the multi-brand channel, it is like-for-like, it is net opening or rather closing in this case of multi-brand stores and then it is about sort of changes in inventories, destocking and among those elements, I think you should still expect some closing of multi-brand stores but probably less so than in 2018, I can't even remember, was it 325 points of sale that we closed, in 2019 it will probably be a bit less than that but overall, that channel is still expected to decline in 2019.

1.01.45

Lars Topholm

And by the same pace as in 2018 or more or less?

Anders Boyer

It's quite significant in, I would say, in 2018 in that channel, obviously also heavily impacted by the forward integration, so yeah, not forward integration that one but the destocking was quite significant in 2018.

Lars Topholm

So, still down but not as much as in 2018?

Anders Boyer

That could be a good modelling starting point, yeah.

1.02.19

Lars Topholm

Perfect. Thank you guys for taking my questions.

Operator

Thank you. Our next question comes from the line of Michael Rasmussen of ABG. Please go ahead, your line is open.

Michael Rasmussen

Thank you very much. First of all, I would like to talk a little bit about 2019 and the quarters. Could you add a little bit more clarity on how we should expect the quarters, in particular the Q1? I mean obviously, you do have a bit more difficult comp on the group organic growth while when we look at China specifically, you will obviously get some benefits from the timing of Chinese New Year and Valentine's and I understand it also the inventory reductions programme is probably not going to hit, at least a lot, in the Q1. So, can you add a couple of building blocks just to set the scene here for Q1? My second question is focused on the slide that you presented in the appendix on slide no. 34 in the slide pack and what I particularly noticed here is that the gift giving category is the one that declined the most when you asked consumers from 2016 to 2018, so how exactly are you going to address this specific issue here and maybe if you can also just give us an update on what you see gift giving as a percentage of sales or what you estimate that is in the fourth quarter? Thank you.

1.03.53

Anders Boyer

It's Anders. I can start with the first question on the quarters. In general, I am a little bit hesitant to say too much about how to expect the top line, bottom line to be between the quarters. I think that's how we think in general but it is even more so going through a transformation like we are with some bigger than normal moving parts. Having said that, there are a couple of things that we can say and one is that the first quarter and the first half is likely to be lower than the second half of the year. As not surprising in a transformation like this, you will often see to get to have the cost before you get the upside. I think that is one statement to put out there but you should also expect that the top-line initiatives that we are implementing will mainly have a positive impact in the second half and one of the slides that Jeremy went through, you can see that the marketing investments as an example mainly come all the way back to the fourth quarter of the year, not all of it but it is back-end loaded and that means that you should expect the first half of the year to be slow.

1.05.28

Jeremy Schwartz

I move now onto the second question. I think the first thing is you know we are a brand, as you can see, that is bought not only as a gift but also for oneself and one also needs to understand that these are gifts that are given not between just a man and a woman but between women friends, an important shift. This is the reason that we have stated that the brand in the way it communicates needs to have a role in today's culture as I mentioned and the reason is that within the brand tracker, we can see that our brand awareness continues to grow but the brand heat is perhaps softening and that is down to relevance. So first of all, we believe that the activity we are planning will recapture that connection, not just to the receiver but to a giver, so that is point one. Point two: The reason that we are saying that Q4 needs to be bigger and better and the start of the reignition is exactly for the reason that you have identified, that gifting is critical, and within that, the gifting range we have for Christmas is being reviewed and refreshed. And I think we can say probably around 60% of our sales are in some form itself noted as gifting but as I say, that can be grandmother to daughter or granddaughter as well as husband to wife which this is normally referring to or man to woman, sorry. Thank you.

1.06.57

Michael Rasmussen

Great. Thank you so much.

Operator

Thank you. Our next question comes from the line of Hans Gregersen of Nordea. Please go ahead, your line is open.

Hans Gregersen

Good morning. Turning to the DKK 1.2 billion cost savings programme as you alluded to previously, Anders. You mentioned that there would be some reinvestment cost but can you give across the entire cost cutting programme an indication of partially phasing but also how much of the 1.2 will be reinvested and how much will go to profitability? That is the first question. Secondly, on the like-for-like outlook, you have not shared too much information about this and in this report, I don't know if more is going to come later but could you, without going into a number guidance, give us sort of a layout for how you see the like-for-like recovery occurring over the next three years? Thank you.

1.07.55

Anders Boyer

Hi, Hans. I can start on the first question on the cost reduction. We can't be specific yet on how much we will reinvest of the DKK 1.2 billion. This year, we are starting with reinvesting DKK 0.5 billion, 500 million, in the business. That is quite skewed towards the latter part of the year and then what that looks like going into 2020, that depends on several things obviously, so we will have to – can't be more specific but what is certain obviously is that we will get a further margin upside in 2020 from the cost reductions if we look at things on an isolated basis and then a bit more going into 2021. So we have said DKK 600 million in cost reductions this year and then DKK 1.2 billion as a run-rate going out of next year and then we can do a little bit of math of what that means for the calendar year 2020 but you probably get to a number that is sort of in very, very round numbers around a billion for the calendar year 2020.

1.09.10

Jeremy Schwartz

And I will take the second question so as we indicated both…

Hans Gregersen

Anders, just to understand your question – am I right to, I mean, you mentioned 600 in reinvestments this year. I assume that these investments are ongoing reinvestments so it is not like one-off, it is more like recurring reinvestments?

1.09.30

Anders Boyer

Yeah, it's DKK 500 million in reinvestments but you are absolutely right, it is here to stay, if you like, the DKK 500 million or another number, higher number, let's say if we find out that we might put even more money behind marketing and our brand machine, given that what we invest this year is mainly in the latter part of the year, it might be a different number going into 2020, but the starting point is that it is recurring, it is not a one-off.

1.10.00

Hans Gregersen

So the conclusion is that less of the DKK 1.2 billion I should assume be hitting the profit line?

Anders Boyer

That is correct. It will be a net impact but what that net impact is, it's a DKK 100 million net OPEX in 2019. What exactly that number looks like going forward, that is too early to say.

Hans Gregersen

Okay, thank you.

1.10.22

Jeremy Schwartz

So Hans, in regards to your like-for-like, as we shared in November and we are doing now, we see that 2019 is going to be negative like-for-like and really I think in this environment, it is too early to make promises or statements on the future outlook but we are only two months into a 24-month programme but I think as we have articulated, the modelling we are doing is showing that we can get back to a positive like-for-like and of course, the purpose of our next calls and so on will be to update you in as much transparency as we feel comfortable to do.

1.11.03

Hans Gregersen

But Jeremy, would it be fair to argue that the return to positive growth numbers would be a multi-year exercise based on your past retailing experience?

1.11.15

Jeremy Schwartz

Yes, I think it is still a bit too early to make a statement but let's take that as a good assumption. I think one thing that is worth noting, of course, is that we are prioritising our countries so that we can give ourselves and yourselves a proof of concept and we are taking the big countries of the US and China as our priorities and we believe that that will allow us to see positive momentum which we can then copy and roll out to other countries as a proof of concept approach and I think that is an exciting way of skinning the cat.

1.11.55

Hans Gregersen

Thank you very much.

Operator

Thank you. Our next question comes from the line of Anne-Laure Bismuth of HSBC. Please go ahead, your line is now open.

1.12.08

Anne-Laure Bismuth

Yes, hi, it's Anne-Laure Bismuth from HSBC. I have two questions on my side. I just want you to come back on the product positioning and I know that you did this extensive presentation and you plan to redefine the clear brand positioning for Pandora but you are also planning to launch a new platform by as late as Q4 2019 but what do you plan to do differently now to make this launch successful? That is my first question regarding the product side of the equation and the second one is about the fact that you flag that the organisation is mainly decentralised so what is the key action that you are now taking to make it more centralised and also are your regional managers reporting directly to you or do you plan to … all these local managers, regional managers will be incentivised regarding the performance that they have to deliver? Thank you.

1.13.23

Jeremy Schwartz

So I think to answer your first question, obviously just one point, you know, we have launched the Reflexions bracelet and we are very happy with the initial start and remember that these sorts of platforms or these sorts of innovations are not about an instant hit. This is about building a base from an idea, making people continuously aware and getting recruitment and trial and then, of course, the collecting. I think the thing I want you to think about most is that we are going to be having a marketing model and a business model that is coming back to the idea of collecting. So yes, things are about a new product but it's in the context of getting more people to buy that and collect it as part of a behaviour. So, I am going to leave, that's the important consideration I want you to walk away with in terms of the way we are going to approach building consumption of the new products that we launch. And as I mentioned earlier, it is about dramatizing the really key products worldwide and I will just spend one minute on that because it relates to your second point. So what we have observed from an execution point of view, country by country we have visited is there is an inconsistency in the way that we dramatize the innovation we have and make it visibly discoverable by our consumer and the reason is twofold: First of all, we have a completely decentralised merchandising and management approach which has been successful in the past but has led to what I call a pick and mix approach and the global consumer or the consumer across the globe is more similar than it is different and when we find a big idea that may have taken us two years to develop, we need to get behind it and amplify it worldwide. So, that's the approach. So, I have half answered your question, so the second half therefore is the reason that we are empowering Stephen Fairchild, our chief creative officer to not only be now with a broader remit of creative and brand and therefore control all touch points but giving him the authority to determine worldwide what are the priorities and what will be executed so that we get amplifications worldwide. Your last point, yes, the regional vice presidents do report in to me directly. Thank you.

1.15.50

Anne-Laure Bismuth

Thank you.

Operator

Thank you. Our next question comes from the line of Thomas Chauvet of Citi. Please go ahead, your line is now open.

1.15.58

Thomas Chauvet

Thank you. Good morning. Two questions please. The first one, your plan to reduce promotional activity will hit LFL by 2-4 points in 2019. Are you expecting this pressure to totally disappear in FY 2020 it feels we are still in an environment where consumers are expecting ongoing promotions, even from established brands. More generally, have you been thinking of reducing your price architecture with lower price points, perhaps for charms? What are your most recent consumer insight surveys saying on the ideal price points for those products? Secondly on the inventory buyback. How confident are you that DKK 500 million is enough? Would you revisit the need to do more buyback, say, in 6 months' time? And just practically, will this merchandise be totally destroyed and are you issuing refunds to retailers or credit notes or swapping products? Thank you.

1.17.00

Ladies and Gentlemen, if I have to achieve one thing in this communication, it is to make sure that it is absolutely clear what I am about to say. We are going to maintain the promotions on all the large retail global trading gifting events. We are focusing on those promotions in between those events which either have demonstrated little elasticity or have meant that the amount of retail time that we have allocated to dramatizing our new products has been so squashed that they have only had sometimes two weeks. So you could call it the surround sound promotions, the noisy little things that are contributing not so much but are impacting both the brand equity perception of the consumer i.e. that we are promoting all the time or/and stopping consumers seeing and really finding the new products that we want to launch. It is highly important that this message got through to you and I hope that has got extremely clear. The second point is – actually I hand back to you for the inventory buyback.

1.18.06

Anders Boyer

Thank you, Jeremy, and Thomas, it is Anders here on the inventory buyback programme. We will do what is right and we think that what is right is amounting to around DKK 500 million, 2 percentage points of revenue in 2019. If we come or should we come to the conclusion that another number is right, we will still do what is right and then pursue that number. I think that is what we have to do when we go through a transformation like this or as always. But having said that, we have made quite some analyses already during the last 4-5-6 months on this issue and this, the number has been circulating around this 2 percentage points of revenue, DKK 0.5 billion for some time. But I should note that the visibility in parts of the channel is not really good but having said that, I think DKK 500 million is a good estimate of what it takes to get to a reasonable level. But there is no one size fits all. We will do this, because I am afraid as a finance guy that if you try to go with one size fits all, you end up paying a too big part of the bill. We have to do this in a clever way, on a selected basis with selected partners and not as a broad-based model but only where and when needed.

1.19.45

Jeremy Schwartz

So I didn't answer your second question so I will quickly come back to that on pricing. So first of all, we actually have a very sophisticated pricing architecture, not only do we now have strong global pricing corridors and that was reinforced by the reduction of prices in China by 15% and the increase in price in Australia by 5% but actually our products are all pre-tested on a price-value curve and are positioned with their quality versus their price. However, even though we have been launching more new products at the lower price point, their visibility to consumers for whom price is important is not where it needs to be and therefore, we are working with nothing confirmed to yourselves on both visibility of entry level pricing and products and also launching additional products that have a greater entry price point. We don't believe that we have to do any wholesale price reduction but it is about discoverability and visibility of particularly those lower price points within our range to those consumers for whom that is important.

1.20.49

Thomas Chauvet

Thank you, Jeremy. Just a follow-up to Anders, maybe, on the buyback. When you say it hits, it's 2% of your revenues, are you issuing credit notes or swapping products with retailers? In other words, in your organic revenue guidance, does this imply 2 points positive impact from the utilisation of credit notes by retailers?

1.21.15

Anders Boyer

Thank you for actually asking that question, Thomas, because that is a very important clarification. With the way that we intend to structure it, it will not hit revenue but go directly into cost of sales and that in many aspects also makes it easier to identify and control, looking at it with the CFO eyes. But it will not hit organic growth, that is not the intention.

1.21.41

Thomas Chauvet

Thank you.

Operator

Thank you. Our next question comes from the line of Magnus Jenson of SEB. Please go ahead, your line is open. Correction, our next question actually comes from the line of Piral Dadhania of RBC Capital Markets. Please go ahead, your line is now open.

1.22.00

Piral Dadhania

Yeah, thanks a lot. I just have one follow-up, if I may, upon your store estate and how you plan on.. you know, why there isn't more of a focus on evolving or potentially downsizing the store estate as you try and reignite the brand in other aspects of your strategy. Could you perhaps maybe just talk around what your evaluation criteria are for any leases that come up for expiry from an IRR perspective? Because just because these stores are profitable or cash generative today, it doesn't mean they necessarily will be in the next 3-5 years and then just following on from that, what is your implicit footfall assumption for the like-for-like guidance that you have given for 2019? Are you expecting footfall into physical stores to remain broadly stable Y/Y or is there an implicit ongoing deterioration of footfall into stores? Thank you.

1.23.01

Jeremy Schwartz

So perhaps I will answer a couple of those and Anders and I will split. So, again, I guess it is important just to be cautious with the emphasis that we have placed in this presentation to not imply that this is not important to us but we wanted to prioritise our messaging to you and therefore, of course we are all the time revisiting our network and for example therefore, when we first of all have any store that is coming up for lease renewal, we are creating a five-year view of that profitability depending if it is a five-year lease or a three-year lease in Asia and so without a doubt we are looking at their economics over time and would not make any decision that was not sensible in that regard. That is point one. Point two: In terms of traffic development, in essence we are assuming that traffic will continue to decline but we are developing rapidly or as rapidly as we can tools that at a store level or through our ecommerce can slow down that rate. Examples will be things such as click and collect which is obviously one tool of drive to store and looking at other drive to store CRM tools while also developing clienteling tools which will enable and empower our store staff to proactively call their best consumer. So there are tactics that are being developed, some of them because their IT link takes time but we are without a doubt working on that. With regard to the network so just to be specific, we are by country looking at our network and looking at tactics where we believe we have got over availability within a town as opposed to pure country and where we need to close a store to create the sense which we are naming engineering scarcity. So, without a doubt, that is being worked on but it is not being worked in this way I have done in other jobs where it has been a wholesale no. 1 priority, it is a business as usual priority as opposed to as a Programme NOW initiative.

1.25.13

Anders Boyer

Yeah, I think Jeremy has answered basically all of it but maybe what I can add with sort of slightly different words is that when we look at a new store or a potential renewal of a lease agreement, we use some pretty tight criteria. The standard assumption is that the case will have to make sense based on a declining like-for-like, negative like-for-like, that is not what we plan for in the longer run but that is what we say, it has to be solid based on a certain negative like-for-like but then obviously, we look at how we address that catchment area, that geographical area already among our own stores, among other points of sale, wholesale distributors, online, and then we reconsider, what is the best way to address that catchment area for the next number of years? And then that leads to a decision on whether to close the store, relocate it or extend it, extend it for a bit longer time or shorter time, depending on how we feel about the exact business environment and business case for that area.

1.26.35

Piral Dadhania

Great, thank you.

Operator

Thank you. Our next question comes from the line of Magnus Jenson of SEB. Please go ahead, your line is now open.

1.26.46

Magnus Jenson

Thank you for taking my questions. Firstly on promotions, could you tell us how much you actually plan to reduce promotion in 2019 in terms of days and further to that, how large a share of sales was generated on promotions in 2018? Secondly in terms of your net working capital, you mentioned at the Capital Markets Day a level at around 15% and you are actually already now at 11% and given that you also mentioned that you can possibly reduce inventory further. Can you give some flavour to what kind of level we should expect when we look ahead? Thank you.

1.27.30

Jeremy Schwartz

We are targeting by country and it does vary by country, a reduction of 50% in the numbers of days approximately that we will have promotions. Obviously, again, to reinforce, we are not touching any of the major promotional event periods which are where the majority of actual promotional sales are executed, so that is the approach we are taking. We are looking at probably around a third of our sales by country because it varies by country were in 2018 on promotion of some sort.

1.28.19

Anders Boyer

Yeah, hi Magnus, good to hear your voice again. And you mentioned that 15% in working capital that we mentioned it, it might almost have been you who mentioned it one year ago but it is true that we are at a lower level at this point in time ending 2018 at around 11% of revenue and there may be a bit further upside but I think in the big scheme of things, I think we have sort of taken the biggest upsides already with what we have already done in 2018.

1.29.02

Magnus Jenson

Thank you very much, guys

Operator

Thank you. Our next question comes from the line of Zuzanna Pusz of Berenberg. Please go ahead, your line is open.

1.29.14

Zuzanna Pusz

Hi. I have two questions, please. So first of all on your marketing strategy so you mentioned you are planning to make some changes to how the brand is marketed but can you discuss these changes in a little bit more detail? Because I think historically, if I remember correctly, Pandora was quite reluctant to collaborate with any celebrities or influencers so is this something you are planning to change? And also related to that, I understand that the strategy plans from last year have been abandoned but I think back then it was discussed that you were targeting around 8% of sales and there was a different marketing spend. But if you actually compare to other jewellery brands or let's say branded goods players that level tends to be higher, above 10%. So do you have any thoughts around the sustainable level of marketing to make sure that you invest in the brand enough? Second question is on the inventory buyback. So I understand that if it's necessary, you may decide to do a little bit more but how did we find ourselves in the, I mean how did you find yourself as a brand there in the first place? Because I think there were some obviously issues with the inventory levels before there was a buyback in the past and generally, that was meant to be pretty well-monitored across the organisation so can you just give us a bit more colour, are you planning to change the way you monitor the inventory levels in the channel just to make sure that actually you don't end up with having too much inventory in the channel? And just a very quick follow-up, it's on the first question actually, on the question around the weight in terms of what we could expect throughout the year, now I understand that it makes sense, you have initially more cost upfront so the outlook is likely to be back-end loaded but it is just that over the past two-three years that was the case, so I think it would be just quite useful to have an idea of really to what extent H1 could be weaker versus H2 just for us to know what the expectations should be. Thank you very much.

1.31.20

Jeremy Schwartz

Okay, well, I will take the first point. So the first thing is that we have stated that we need to create an environment of positive disruption. In making that statement it implicitly means that sacred cows for example need to be challenged and that we have to therefore be much more connected to today's culture and the relevance to that. So I think what we can see or what I have seen is that we have been – I would use the word conservative – in the way that we have expressed and connected and represented consumers and in the way that we have embraced tools such as celebrities and collaborations that other brands have seen have been a very effective tool nowadays to connect with people. So I think it's a combination of a new set of eyes, it's a combination of having a call to action and a reference point that we have to reignite this brand, we have got to be disruptive and no stone can remain unturned to get there. So I think those would be the main reasons why we will do things differently against that context of having a greater role in today's culture to excite and engage consumers. In terms of your marketing spend question, to be honest, where the teams have been very effective, frankly before I arrived, is to reduce the number of media agencies for example that we use from 7 down to 2 and through not only that but a strong focus that we are now doing on performance management including econometric modelling. We are extracting greater value and return from every Danish Krone or Dollar or Pound or Euro that we are spending so we are looking more at productivity than necessarily exclusively the amount we are spending, though of course we have allocated and plan allocating more investment for Q4 and as we have indicated, we can imagine through our econometric modelling that we will spend again more potentially in 2020 if that is what it shows is a good investment decision.

1.33.40

Anders Boyer

And Zuzanna, on the buyback programme, it is clearly something that we have on the agenda even though the revenue that we have from our franchise partners is a smaller percentage of the total revenue than in prior years, it is still a very big part of Pandora and we would like this to sort of be a standard part of our agenda that we are always quite close to knowing and understanding what kind of inventory sits with the partners. But we also should see the change that we are doing with the sell-in packages, the new product introduction sell-in packages that is a way to structure ourselves to systematically avoid having too high inventories in the channel so that has been one of the results of the diagnosis that we have made. And then it is true that we have made, if that was the question, we have made sort of a structured buyback programme in the past as well but it dates all the way back to 2012 so it is quite some time back. And then on the seasonality, I would love to sort of try to be more specific and help you out more but it is just a sort of by nature more bumpy when you go through a transformation as we do, I would be hesitant to say more than what I did on the call earlier today.

1.35.17

Zuzanna Pusz

Okay, perfect. Thank you very much.

Operator

Thank you. Our next question comes from the line of Chiara Battistini of JP Morgan. Please go ahead, your line is open.

Chiara Battistini

Hi, thank you, sorry, just a couple of follow-up questions, very small. First on the cost savings, you gave a very helpful split of the cost savings between COGS and OPEX on slide 22 by 2020. Is it fair to assume a similar split also in 2019 so roughly 30% of savings coming from COGS in 2019? And the second question, the second small follow-up question: The 75 net openings, would you be able to split it between gross openings and closures, please? Thank you.

1.36.06

Anders Boyer

Hi Chiara, I can start on the cost savings. I would actually expect the cost of sales being a somewhat higher relative share of the cost savings in 2019 than in 2020. We are sort of a bit ahead of the curve I guess you can call it within cost of sales, also stemming from the fact that our organisation in Thailand has been more used to always work with a sort of continued cost improvement mindset and therefore, the relative share of cost reductions from cost of sales is higher, a bit higher in 2019.

1.36.52

Jeremy Schwartz

I think on the second question, actually at this moment, we just like to keep it at the 75 net openings, you know, it's a number from an opening and closing that will move, so we will update you further in the year on a more precise view as we get clearer. Thank you.

1.37.10

Chiara Battistini

Thank you and just, sorry, a couple of follow-ups on those. On the cost of goods sold then the savings, is it more like 50-60% of savings of 2019 coming from cost of goods sold?

1.37.20

Anders Boyer

I wouldn't go that high but it is higher than what you would be able to calculate from slide 22.

Chiara Battistini

Okay, perfect. And on the number of stores, can we confirm that in countries like the UK or the US in 2019 we are actually going to see net closures without being precise on the numbers?

1.37.40

Jeremy Schwartz

You could assume that as a good opening position, yes.

Chiara Battistini

Okay, perfect. Thank you very much.

Operator

Thank you. Our next question comes from the line of Fredrick Ivarsson of Kepler Cheuvreux. Please go ahead, your line is now open.

1.37.56

Fredrick Ivarsson

Thank you, hi guys. First one on the redesigning of the ecommerce. I guess you mentioned some new features and sorry, I am just curious if you could elaborate a little bit on that? I guess you mentioned click and collect as one for instance. That is my first question. The second one is I guess another follow-up on the timing when looking into 2019 but focusing more on the cost savings as well as the restructuring costs. How should we think around the phasing throughout the year? Will it be clearly visible already in Q1 or more sort of accelerate throughout the year? Thank you.

1.38.35

Jeremy Schwartz

As you know, ecommerce is a combination of two things: Thousands of incremental improvements and big substantial changes. So, when you look at our site now, actually it requires combination of the two and the first ones are the simple thing of the product landing page, it is the place where every brand makes or breaks its sales and the product performance so we are step changing the way that every single product appears under a gold silver bronze sort of structure so that we can dramatize and bring inspiration to the products and then we are developing more helpful services from recommendation engines and other services that you progressively see to help our consumers sort and find the products that they really want in a more frictionless way amongst our assortment. Secondly on omnichannel, as we have explained, we are rolling out all elements of omnichannel which is go in store, send to home, click and collect and endless aisle, an online inventory, a view of inventory so all of those elements are being progressively rolled out in the US and when we feel that they are faultless or working to the level we want, we are going to roll those out in other countries against the plan that we have. Thank you.

1.39.51

Anders Boyer

And then two short answers on the cost savings and restructuring costs. On the cost savings, it will be building up over the year but there will also already be some impact, a little impact in Q1, given that we have started already back in late 2018. And on the restructuring cost seasonality, you should expect sort of the opposite impact, that it starts a little bit lower but then the cost will be higher sort of after Q1.

1.40.26

Fredrick Ivarsson

That is very clear. Thank you.

Operator

Thank you. Our next question comes from the line of Lars Topholm of Carnegie. Please go ahead, your line is open.

Lars Topholm

Yes, two additional questions from me. Anders, I think in your presentation, you mentioned a new incentive programme aligned better with shareholder value creation. I wonder if you can comment a bit on that, what are the elements, what are the changes, who is it valid for? And then a second question goes to your e-store revenue growth of 25%, that is a market slowdown compared to previous quarters. I wonder if you have any explanations to that and should it bother us going forward? Thank you.

1.41.16

Anders Boyer

Hi, Lars, I can start up with the incentive programme and maybe starting up with the short-term incentive programme so far, so the range of participants as such is not changing but what we are changing is the elements that ourselves and the organisation is measured on and that means that it is pretty simple, it is three elements: It is like-for-like total like-for-like that we are measured on, it is EBIT margin and it is the impact of Programme NOW specifically on the cost reductions, those are the three elements that the board and management have chosen that should be driving the short-term incentive programme. And then we have also said in the annual report that the KPIs for the long-term incentive programme is also being revisited along the same lines so there will be more communication about that following the AGM.

1.42.25

Jeremy Schwartz

Okay, in terms of your question about the e-store, obviously our objective is to continue to drive and secure strong growth on our ecommerce sites around the world because it's a key component and obviously we want it to outpace the growth or the decline in stores to give us a net growth strategy. We are in EMEA in particular going to be slowing down the immediate rate of growth because there is a sales tab that is visible to the consumer all year around as opposed to just during sales and we are going to progressively pulse and turn that off so I think this fits into again that bucket that we said at the very beginning, we are going to do the right things for the brand and the business and the brand equity. If that means some short-term pay-in, it is the right thing to do to give us long-term sustainable value and shareholder value. Thank you.

1.43.20

Lars Topholm

So, should we expect a further slow-down in ecommerce growth going into 2019?

Jeremy Schwartz

I think that would be a good assumption, Lars.

Lars Topholm

Thank you.

1.43.33

Operator

Thank you. Our next question comes from the line of Omar Saed of Evercore ISI. Please go ahead, your line is open.

Omar Saed

Thanks for taking my question. We wanted to ask about the shift you have been talking about to the concept of collectability. Can you talk about how you have arrived at this strategic direction for the brand, what were the key factors or data that gave you the confidence in this new direction … and second, will this shift also change the nature of the products? In other words, are you moving away from gifts and the emotional value of charms, the personal meaning they signify to a couple? And also maybe talk about the timing of when these product changes are going to show up in the private line. Thank you.

1.44.19

Jeremy Schwartz

Okay, the concept of collectability is at the very core of why Pandora is the largest, most well-known jewellery brand in the world. It is the fact that we have, for example 15% of our consumers who own 20 or more charms. It is the fact that we have an average consumption for example of a ring that may be two times per year for a customer but when it comes to charms, it is 4-6. So it is fundamental to why we are where we are and that is why we are going to drive it again but with more deliberation and a greater forensic approach. In terms of when the activities will start, they are going to progressively start and I will give myself permission to be vague, if I may, because this is also dependent on a loyalty reward programme which will take some time to pilot and then roll it out – not dependent on that but connected to that. In terms of the emotional charms, we will absolutely not be moving away from emotional charms because it is that element that connects to the element I explained to you of expressing one's individuality and individuality is expressed through the emotions and experiences that people are having. So rather, we are going to be looking at more occasions and different moments that people want to express their emotions through our charms, rings, necklaces and all of those components. And you will see it progressively happening obviously, most of the first half of this year has been put to bed over a year ago so this is a refocus in development that will progressively hit our business. Thank you.

1.45.57

Omar Saed

Thanks, Jeremy.

Operator

Thank you. Our next question comes from the line of Hans Gregersen of Nordea. Please go ahead, your line is open.

Hans Gregersen

Yeah, thank you for the follow-up. Jeremy, in the NOW analysis phase that you have been through, if we look on product development, what conclusion have you arrived at? Because that must also be a part of the like-for-like problems. Second question goes to the franchise operators, what will happen to, what are you doing to help them and how do they see the benefit from the actions you are doing both short and medium term?

1.46.40

Jeremy Schwartz

Okay, so obviously, product is key and we are first of all going to ensure that we continue to create products in all of the categories that are a combination of disruption and relevance and that is why, for example, we are going to look for collaboration because that creates the relevance and the disruption that we need to have for example. The second thing is all about standout and visibility and I have explained that. Our execution at a country or online level has been blurred and not as sharp as we need and therefore, it is as much about the way we dramatize what we are launching, the relevance and the cultural fit with what we show as simply just changing the product in itself. And that is why we have expanded what we are saying is required in reigniting a passion for Pandora from more than just a product story because it is the way we execute as much as the product itself. Thank you.

1.47.50

Hans Gregersen

But Jeremy, could I just… sorry, you mentioned collaboration, if I understood it correctly. Would that be more as Disney and secondly to that, you mentioned that there will be fewer DV launches. If I look on your slide 35, that is not really what the numbers are showing to a large degree.

1.48.11

Jeremy Schwartz

So first of all, Disney is a good example of a collaboration and one which has proven to be highly effective and we will continue with that but that is the sort of collaboration we are talking about. In terms of the reduction in DVs, it is a progressive approach that we are going to take because the question I was asked was about the future as opposed to this year per se where, as I mentioned already, the majority of the first three quarters have already been secured before I arrived.

1.48.45

Hans Gregersen

Thank you.

Operator

Thank you. Our next question comes from the line of Elena Mariani of Morgan Stanley. Please go ahead, your line is open.

Elena Mariani

Thanks very much. I also have two small follow-ups. The first one is on ecommerce and on the omnichannel capabilities that you might consider to implement. I remember that this has been a critical point in the past because not all the franchisees were supportive of omnichannel experiences so I was wondering how you plan to tackle this and whether you found a solution that could work for all so that this could be implemented across your entire distribution network? And the second small question is on gross margin guidance for full year 2019. I understand you don't want to go into too much detail but is it fair to assume that the current EBIT margin guidance coupled with the cost savings and the cuts in promotions would imply gross margin to be under substantial pressure in 2019 given that the cost savings you have identified are mostly related to OPEX? If you could give us any sort of broad indication, that would be very helpful. Thank you.

1.50.00

Jeremy Schwartz

On omnichannel, first of all, I think you know it would be very fair to say that Pandora is behind the curve but we are going as quickly as we can to catch up and therefore, and the approach we are taking, as I have earlier mentioned, is to focus on America as what I am calling a beacon country so that we can focus our efforts. Secondly, as I mentioned, I was with the franchise advisory council last weekend or the weekend before last and I have had very constructive conversations with them and I believe we can see a joint way forward which we are both and all excited about.

1.50.42

Elena Mariani

Thank you very much

Operator

Thank you. Our next question comes from the line of Michael Rasmussen of ABG. Please go ahead, your line is open.

Michael Rasmussen

Yeah, thank you, two quick follow-up questions. First of all, on slide no. 22, if I calculate the high end and the low end, that could be indicating that you are actually targeting cost savings of between DKK 1 billion and 1.4 billion or is that simply due to rounding? And then my second question on the new store designs that you have obviously flagged here, is the cost sharing split between the franchisees and yourself, is that changed? And when we look into 2020, should we assume CAPEX as a percentage of sales to go above the 5%, maybe due to this? Thank you.

1.51.36

Jeremy Schwartz

I think first of all, we are not envisaging or at this stage planning any cost sharing split changing per se and as we indicated in principle, the approach is to take our existing CAPEX approach and to flex it, to be more discerning between different formats but fundamentally not to change the approach. Anders, do you want to answer that?

1.52.02

Anders Boyer

Yeah. And then Michael on the first question on the cost reductions, it is true that it adds to 1.0 if you take all the numbers to the left and 1.4 if you take all the numbers to the right on slide 22 and that is deliberate and I guess as expected when you go into a programme of this size and so big cost opportunities, there is a range. But what we feel comfortable saying is that it sort of nets out to around DKK 1.2 billion when it is all done and dusted by the end of next year.

1.52.41

Michael Rasmussen

Thank you very much, guys.

Operator

Thank you. Our last question comes from the line of Zuzanna Pusz of Berenberg. Please go ahead, your line is now open.

1.52.52

Zuzanna Pusz

Thank you for taking my last question, it is just a follow-up. Now, I understand that obviously there is no kind of long-term margin guidance in place but just to understand sort of the margin trajectory in the coming years, I mean there has been a couple of questions around inventory buyback, marketing and I think you made it clear that if it is necessary, you would be willing to maybe to do some additional buybacks, invest a bit more if it's needed for the brand. So, when we think of the outlook you have given for this year, I think it is 26-28% adjusted EBIT margin, is that sort of the bottom of profitability we should expect? Or if it is less in coming years it turns out you need more investments, you will be willing to do this? And basically, do you have any thoughts on what should be a sustainable margin of a business like Pandora? Thank you.

1.53.48

Anders Boyer

I think the upfront answer is that it is too early to say and be specific but what we can clearly confirm is that we will keep being a company that has very high profit margins, we also had that in 2018 for that matter and that is clearly where we see that the company will keep operating. But exactly what that number or range of numbers will be, that remains to be seen.

1.54.21

Zuzanna Pusz

Okay, perfect. Thank you very much.

Operator

Thank you. There are no further questions at this time. Please go ahead, speakers.

Jeremy Schwartz

I would just like to take this opportunity on behalf of Anders and myself to thank you for your attention and your questions. We look forward to meeting many of you and continue to appreciate the support that you are giving us and look forward to working with you in the future. So, have a good rest of the day and see you all shortly over the next week.