



9M2017 Results

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CONFERENCE CALL TRANSCRIPT

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Important notice: Although we try to accurately reflect the speech delivered, the actual speech that was delivered may deviate from this transcript.

9M2017 Results Conference Call

Inditex Participants

Pablo Isla - Chairman & CEO

Ignacio Fernández - CFO

Marcos López - Capital Markets Director

Conference Call Participants

Anne Critchlow Societe General – Analyst

Richard Chamberlain RBC – Analyst

Rebeca Macclellan Santander –Analyst

Andrew Hughes UBS – Analyst

Chiara Battistini JP Morgan – Analyst

Andreas Inderst Macquarie – Analyst

Cedric Lecasble Raymond James – Analyst

9M2017 Results Conference Call

Operator

Good Morning Ladies and Gentlemen. Welcome to the presentation of Inditex Results for the Interim Nine Months 2017. The presentation will be chaired by Mr. Pablo Isla, Chairman and CEO.

This presentation will be followed by a Q&A session comprising two parts: The first part will be dedicated to questions received on the telephone, followed by those questions received through the webcast platform. Mr. Isla you have the floor.

Slide 3

Good morning to all the participants in this webcast conference call regarding INDITEX Results for the Interim Nine Months 2017.

I am Pablo Isla and here with me today are Ignacio Fernández, our CFO and Marcos López, Capital Markets Director.

Slide 4: 9 Months 17: Strong execution globally

The Interim Nine Months of 2017 has been a period of strong execution for Inditex globally.

Slide 5: Global fully integrated Store & Online

Our business model combines stores and digital seamlessly, and we are ready for the opportunities that this brings with current and new customers. We operate a global platform that fully integrates stores and online and offers huge growth potential.

Slide 6: Interim Nine Months 2017: Overview

Inditex performance in the period has been strong. Sales have increased 10%. We have achieved positive LFL sales growth in all geographical areas over the period.

Our operations have also shown high efficiency and tight control.

We have opened stores in 52 different markets, demonstrating the reach of Inditex's business model. We have also continued our global online rollout with launches in 8 markets.

We have a worldwide presence and have further diversified our operations over the period. We continue to see significant growth opportunities for Inditex globally.

The year so far has been marked by very strong activity on many fronts. I would like to cover a number of recent initiatives carried out by Inditex.

Slide 7: Zara: Venice flagship

We have reinforced significantly the differentiation of our key global flagships with very visible openings.

I would like to highlight our global flagship in Venice at Fondamenta Oresolo.

Slide 8: Massimo Dutti: Shenzhen Flagship

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Massimo Dutti has also opened a very impressive flagship in Shenzhen at Mix C World.

Slide 9: Bershka: New image at Tokyo flagship

Bershka has recently introduced a new image in its global flagship in Shibuya in Tokyo

Slide 10: Pull&Bear: Launch in Vietnam,

Pull&Bear has launched in Vietnam with a first flagship at Hoh Chi Min's Vincom Centre. This centre also includes stores for Zara, Massimo Dutti and Stradivarius.

Slide 11: Stradivarius: Escape Editorial

Stradivarius has launched the Escape Editorial for the holiday season,

Slide 12: Zara Home: New look on Instagram

Zara Home has introduced a new look in Instagram.

Slide 13: Oysho: Launch in Switzerland

Oysho has recently launched its first store in Switzerland with a flagship at Place du Molard in Geneva.

Slide 14: Uterqüe: Atelier collection

Uterqüe has introduced the Atelier collection for the Festivities

Slide 15: Financial summary

Let me now hand over to Ignacio who will present some of the key aspects of our financial performance and I will join you later for the Outlook section.

Slide 16: Interim Nine Months 2017

Thank you.

In the Interim Nine Months of 2017 Inditex has had a strong operating performance. All the lines of the profit and loss account show significant growth.

We have achieved Net sales of 18 billion Euros, EBIT of 3 billion Euros and Net Income of 2.3 billion Euros.

Slide 17: Sales

Starting with sales I would like to tell you that In the Interim Nine Months 2017 Sales grew 10%. LFL sales growth has been strong.

Slide 18: Gross Profit

Gross profit has increased 9% to 10.3 billion Euros, resulting in a 57.4% gross margin on sales. We have sustained our commercial policies over the period.

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Slide 19: Operating expenses

Operating expenses are tightly under control. They have grown 10% reflecting the growth in sales and include all the start-up costs.

Slide 20: Current accounts

Operating working capital remains negative as a result of the business model. The working capital evolution is in line with the performance of the business.

Slide 21: Concepts

I will now hand over to Marcos who will elaborate on the performance of the concepts.

Slide 22: Performance by concept

Over the Interim Nine Months we have continued with our global expansion. We have opened stores in 52 markets so far this year. Global online launches continue at a very rapid pace.

Regarding the performance by concept in the Interim Nine months 2017 Zara continues to represent approximately 2/3rds of group sales, the younger concepts around 1/3rd.

Slide 23: Performance by concept

The younger concepts grouped together have performed satisfactorily.

I would like to highlight that Oysho, Uterque, Bersha and Pull&Bear have performed strongly.

Slide 24: Outlook

I will now hand over to Pablo for the outlook section.

Slide 25: FY 2017 Outlook

With respect to expansion in 2017 let me highlight that we are on track. Ordinary Capital Expenditure for 2017 will be around 1.5 billion Euros.

For the coming years we continue to see strong growth opportunities, with Capital Expenditure growing below space growth.

Regarding the outlook for the Second Half of 2017, I would like to add that Store & Online sales in local currencies from the 1st of November to the 11th of December have grown by 13%.

Just as a reminder, we made our final 2017 dividend payment of 1.1 billion Euros on the 2nd of November.

Slide 26: Global growth opportunities

We will continue to invest in the expansion of our business across a number of markets, all of which offer attractive long term returns through our sales platform that fully integrates stores and online.

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Inditex is present on five continents and in all key markets demonstrating the Group's global reach. We manage a diversified sales platform in 94 markets. The current base offers huge growth potential for the coming years.

Slide 27: Global Store & Online

Inditex's online operations have seen very rapid growth in recent years. Our business model allows a swift expansion of our Store & Online platform globally.

Zara has built an online presence across the whole of Europe, Asia and the Americas.

We will continue to roll out online progressively in all the markets in which we are present with stores.

Slide 28: Global Store & Online

We have recently completed the online launch of Zara in practically all South East Asia.

In October we launched Zara online in India with a strong reception.

Slide 29: Store & Online: Outerwear Collection

We are in a unique position as we enjoy a global platform that fully integrates stores and online as the best way to respond to the demands of our customers.

We continue developing new initiatives in a fully integrated way as Zara's recent Outerwear Collection...

Slide 30: Store & Online: Knit Trends

The Knit Trends Editorial ...

Slide 31: Store & Online: Smooth Textures Collection

The Smooth Textures collection...

Slide 32: Store & Online: Join Life

... and the organic cotton collection Join Life.

Before closing I would like to highlight some selected Zara store openings in prime locations and enlargements from recent months.

We continue to reinforce significantly the differentiation of our key global flagships with very visible stores.

Slide 33: Zara Miami

I would like to begin with the flagship store that Zara opened last month in Miami at Aventura Mall with 3,200 square metres, followed by another Zara in the Miami Brickell City Center.

Slide 34: Zara Shenzhen

In China Zara has opened a flagship store of 3,200 square metres at Uniwalk in Shenzhen.

9M2017 Results Conference Call

Slide 35: Zara Nagoya

In Japan we opened our flagship at Sakae in Nagoya

Slide 36: Zara Seoul

Zara also enlarged its store at Gang Nam in Seoul

Slide 37: Zara Hanoi

And Zara has opened a flagship in Vietnam at Hanoi following the strong reception of the first store in Hoh Chi Min.

And this is all from us. We will be pleased to answer any questions you may have.

Questions & Answers

Operator

Ladies and gentlemen, the telephone Q&A session starts now. If you would like to ask a question, press 01 on your telephone keypad. We request that you kindly limit yourself to only one question per turn. If you have further queries, you may press 01 again after the next person's question has been addressed. If possible, we recommend that you do not use your mobile or answer free phone. There will be a short silence while questions are being registered. Thank you. The first question comes from Anne Critchlow, from Societé Generale. Please go ahead.

Anne Critchlow - Societé Generale - Analyst

Thank you, good morning, everyone. I am just wondering what the currency impact was on sales in the third quarter. It looks like about -3%, but could you confirm that? And on an FX neutral basis, what happened to gross and EBITDA margins in the third quarter?

Marcos López – CEO

Yes, regarding your question, the currency impact over the first nine months is around -1%, as we mentioned in the previous conference call. What we still expect for the year is something between -1% and -1.5%. So, no changes versus previous guidance. And I don't think I understood your second question.

Anne Critchlow - Societé Generale - Analyst

If you stripped out currency with the gross and EBITDA margins have been up?

Marcos López - CEO

We have mentioned in previous calls that without the currency impact, the gross margin, obviously, would have been positive.

9M2017 Results Conference Call

Anne Critchlow - Societé Generale - Analyst

And could you put a figure on that?

Marcos López – CEO

I prefer not to be more specific over a short period of time.

Anne Critchlow - Societé Generale - Analyst

Okay. Thank you

Operator

Next question comes from Richard Chamberlain from RBC. Please go ahead.

Richard Chamberlain - RBC - Analyst

Thanks very much, good morning everybody. A couple of property related questions, please. Why was the depreciation charge not up, it was flat actually in Q3? It was lower than I expected. That was the first one. And then the second one is, there is a press article suggesting Inditex might be selling and leasing back some stores in Spain and I wondered if you could just talk through why Inditex might be doing that. Is that around a shift online in the market?

Pablo Isla - Inditex - Chairman & CEO

Regarding the second part of your question, I think there's nothing really particularly relevant there. As you know, our expansion policies focused on store expansion on a leasehold basis. These are stores in Spain that we acquired in the '90s, a long, long time ago when it was the only way to secure them. So, these are good stores and we will continue with them on a leasehold basis. So nothing really relevant. And regarding the first part of your question, Marcos.

Marcos López - CEO

Regarding depreciation, you know that depreciation reflects the asset base, the additions over the period, impairment, reversal of impairment and under IFRS this is a more fluid caption now. But nothing specific to tell.

Richard Chamberlain - RBC - Analyst

Ok, so it was around probably timing of impairments. Is that it?

Marcos López - CEO

Exactly. The combination of all.

Operator

Next question comes from Rebecca McClellan from Santander. Please go ahead.

Rebeca McClellan - Santander - Analyst

Good morning. I have just one question, please. Given the sort of environment which is very volatile, how can Inditex continue to ensure and protect its reactivity and scale up the business?

9M2017 Results Conference Call

Pablo Isla - Inditex - Chairman & CEO

What you are asking about is what the essence of our business model is. For us, as we have mentioned many, many different times, the essence of our business model is this flexibility and this ability to react during the season, what we call "the low level of product commitment" at any point in time during the season, the possibility to react, the proximity sourcing. So this is the essence of the business model and this is what we are more focused on, all of our commercial teams and what for us is the most relevant thing all across the company. Of course, when we talk about our strategy, this is the most relevant part and then we have many other initiatives, strategic initiatives, as you perfectly know. This idea of global flagships absorbing smaller stores, RFID implementation and many different things that contribute to the fully integrated approach, of course, between the stores and online, that contribute to the evolution of the business. But what you were mentioning in your question is for us the most relevant thing and the essence of our business model to maintain this flexibility, this ability to react, and this is what continues to be the case for sure.

Rebeca McClellan - Santander - Analyst

So you don't think there is any pressure on that reactivity given the growth and the scale of it going forward.

Pablo Isla - Inditex - Chairman & CEO

No, we are quite used to reasonable rates of growth every year, so, everything adapts to this rate of growth, as has always been the case. So, this will continue to be the case in the coming years.

Operator:

Next question comes from Andrew Hughes from UBS. Please go ahead.

Andrew Hughes - UBS - Analyst

Good morning, everybody. I have a question on your global distribution and particularly your dark stores. I know there was an article in the press a few months ago about a big new distribution centre at Lelystad to facilitate faster online delivery. Is that a completely separate program from your dark stores and should we expect to see more local distribution centres opened up worldwide?

Pablo Isla - Inditex - Chairman & CEO

Nothing is changing really from the point of view of distribution or logistics model. For us, what is key is to maintain the centralised inventory position, as you know, because of our strategy, because we do not decide until the last minute what we are going to send to each of these stores in the world, and then, having in mind this centralised inventory position, we are permanently investing in our logistic platforms. But regarding what you were mentioning about Lelystad, this distribution centre, it is not particularly related with that. It has much more to do with the global growth and the company and the global development of the company. But without changing anything, what for us is the most relevant thing without changing anything regarding this centralised inventory position that for us is absolutely key.

Andrew Hughes - UBS - Analyst

Thanks, so Lelystad, is it a one-off big distribution centre outside of Spain?

9M2017 Results Conference Call

Pablo Isla - Inditex - Chairman & CEO

As you know, we permanently investing in logistics, it has to do with the growth of the company, and then, the investments in logistics, every year, we invest in all the logistic platforms, and from time to time we build a new distribution centre for Zara or for any of the other brands depending on the growth prospects in the coming years. So, it has to do with a normal evolution of the company.

Andrew Hughes - UBS - Analyst

Ok. Great. Thanks very much for that.

Operator:

The next question comes from Chiara Battistini from J.P. Morgan. Please, go ahead.

Chiara Battistini – J.P. Morgan - Analyst

Good morning, thank you very much for taking my question. I have a quick one on cash. As your cash position at the end of the 9 months was up 24% year on year on balance sheet, I was wondering whether you could give us some more colour on how you are thinking about the best use of cash and your priorities for the use of this cash piece. Thank you.

Pablo Isla - Inditex - Chairman & CEO

Thank you. You know that always, when we talk about our cash flow generation and our cash position, we always say that the first priority for us is to invest in the long-term term profitable growth of the company. But of course, as far as we are having very healthy cash flows, we are able to combine this with what we consider an attractive and predictable shareholders remuneration policy, and in fact, we are regularly increasing the dividends. Well this year, last year, because it is against 2016 results, dividend growth was 13%. So, we are regularly and progressively increasing the dividends, and this is our global approach. And then, every year, in the month of March, in the full year results presentation, is when we elaborate a little bit more about the cash position and the distribution of dividends that there is. So, I think that it is better to wait until the month of March, when we always update about the distribution of profits.

Chiara Battistini – J.P. Morgan - Analyst

Ok. Thank you very much.

Operator:

Next question comes from Andreas Inderst from Macquarie. Please go ahead.

Andreas Inderst – Macquarie - Analyst

Thank you. I have two questions. First one on pricing. I know you don't like to comment on that, there are persistent rumours of price cuts, but maybe you can help us in terms of communicating how you see pricing within the group and also relative to the market. Thank you.

Pablo Isla - Inditex - Chairman & CEO

9M2017 Results Conference Call

Regarding pricing, what we can tell you is that our pricing policy is very much stable in all the different geographies. We always have a medium and long-time approach and what we offer to our customers, as you know, is the latest fashions, very high quality and affordable prices in the different markets. So there is nothing really relevant from that point of view. Stable prices globally.

Andreas Inderst – Macquarie - Analyst

And another pushback we get is on your stores versus online. There is a lot of people out there who doom physical stores. Obviously, you have a high focus on triple A locations, but if you look at the total store portfolio, how many stores do you regard in B, C locations as a percentage of your total network?

Pablo Isla - Inditex - Chairman & CEO

Well, what we can tell you is that for us, what is key is what we call this fully integrated approach between stores and online. We believe very much in this approach, stores and online are helping each other from many different points of view. This fully integrated approach has to do with everything, with the image of the campaigns, of course, with the possibility of in-store deliveries, in-store returns, ordering online from the stores. So many, many different things. This is what we believe works for us. All of our stores are relevant stores and, as you know, in the last few years, we have been going through this store optimisation programme, opening relevant flagships, enlarging existing stores and absorbing smaller stores. What we can tell you is that in the last few years, around 80% of our total space has been upgraded in one sense or another. So, we believe very much in this fully integrated approach.

Operator:

The next question comes from Cedric Lecasble from Raymond James. Please go ahead.

Cedric Lecasble – Raymond James - Analyst

Good morning. Thank you for taking my question. The only question I have is on the inventories, the other ones have been already been answered. You ended the quarter after a tough October with high inventories and at the end year on year and on the previous quarter. Given a very strong start to the Q4, are you confident that inventories will come back to more normalised levels?

Marcos López – Inditex - CEO

Cedric, as you know, the inventory is just a snapshot of the situation. What we follow is product commitment. As you have said, the inventory level and you put it in the context of the trading update is very, very normal. So I wouldn't rate anything specific into that. The trading update speaks for itself in terms of the inventory position.

Cedric Lecasble – Raymond James - Analyst

Thank you.

Operator:

Ladies and gentlemen, we are now finished with the telephone Q&A session to address questions received through the webcast platform. Thank you.

Operator 2:

9M2017 Results Conference Call

We had a number of questions on the webcast platform, the first of which is as follows. Can you provide an update on the roll-out of RFID across the concepts, please?

Pablo Isla - Inditex - Chairman & CEO

Yes, I was mentioning RFID during the Q&A session. What we can tell you, as you know, is that RFID is a very important part of our strategy. The main aim of RFID is to improve our customer service, of course, then there are many other aspects of RFID in our customer service which are relevant to us, but regarding specifically your question, we have already rolled out RFID in virtually all Zara stores at the end of last year and now we are starting with Massimo Dutti and Uterqüe, that will be fully implemented in the year 2018. And we are expecting in the next two to three years to have RFID fully implemented in all our stores of all different brands in the different countries of the world. It is a very relevant project for us from many, many different points of view.

Operator 2:

Thank you. The other question was: Can you provide some colour on the launch of online in India, please?

Pablo Isla – Inditex – Chairman & CEO

Yes, what we can say is that we launched Zara online in India in October the 4th and the reception was quite strong. We are happy about the reception. This year has been relevant for us in India, because we also opened our Zara flagship in Mumbai at Ismail Building. It is a 5,000 square meter store. We continue seeing good prospects for us, very relevant prospects in the Indian market. We are present with Zara, Massimo Dutti, now with this online presence and our idea is to continue developing our presence in this attractive market.

Operator 2:

Thank you. And finally, perhaps a little bit of an update on progress in Vietnam.

Pablo Isla - Inditex - Chairman & CEO

Yes. We were referring a little bit to Vietnam during the presentation. As you know, last year we opened our first store in Vietnam, in Ho Chi Minh City, with a very strong reception, and then also in Ho Chi Minh we have opened Massimo Dutti, Pull & Bear and Stradivarius, and very recently we have opened our first Zara store in Hanoi. We were presenting the image during the presentation. In fact, I was there the day before the opening and it was very easy to feel the excitement all across the city about our opening. So, what we can say is that Vietnam is a very attractive market for us and the idea to continue developing our presence with Zara and with the different brands.

Operator 2:

Thank you. That concludes the webcast questions.

Pablo Isla - Inditex - Chairman & CEO

Thank you very much and in any case, of course, as always, we will be ready to answer any additional questions you may have to our capital markets department. Thank you very much.

Operator:

9M2017 Results Conference Call

Ladies and gentlemen, this concludes our conference call. Thank you all for attending. You may now disconnect your lines.