Signet Jewelers Ltd at ICR XChange
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Corporate Speakers

• Todd Slater	Lazard Capital Markets	Analyst
• Mike Barnes	Signet Jewelers Ltd	CEO Designate
• Ron Ristau	Signet Jewelers Ltd	CFO

PRESENTATION

Todd Slater: Hello everybody, we're going to get started in just a minute, so if you could take your seats. My name is Todd Slater and I'm at Lazard Capital Markets, and it's great to see you all here. The company that we are now introducing is Signet, the owner and operator of the greatest jewelry brands in the world, in the US and the UK. I would just say that, in all the industries that I cover and have the pleasure to cover I don't think there is any one industry such as this, where the leader is such a giant spread between the best in class and the rest of the pack. So this is one of those unique cases and one of the reasons why I think Signet continues to be uniquely positioned to grow and to take share and take share profitably. It gives me great pleasure to introduce the two speakers here today from Signet. Mike Barnes to my right, who is the CEO Designate, and Ron Ristau the CFO, thank you very much and enjoy the presentation.

Mike Barnes: Thank you Todd. As Todd said, I'm Mike Barnes. Good morning and thank you for coming. I am the Chief Executive Designate of Signet. I joined the business about 5½ weeks ago after a very long tenure with a company called Fossil that I was with; and I will become CEO at the end of January when Terry Burman, our long serving CEO, retires. Also presenting, as Todd mentioned, is Ron Ristau.

Before we start, I would like to mention that during today's presentations we will, in places, discuss Signet's business outlook and make certain forward-looking statements. Any statements that are not historical facts are subject to a number of risks and uncertainties, and actual results may differ materially.

We urge you to read the Risk and other factors and cautionary language in the annual report on Form 10-K that was filed with the SEC in March 2010. We also draw your attention to the slide on the screen.

So why invest in Signet. We have a record of gaining profitable market share over many years. We believe this is as a result of our developing sustainable competitive advantages.

These advantages include: The quality of our sales associates, excellence in customer service and a great in-store experience, as well as our very experienced divisional management teams; our ability to leverage our supply chain leadership; the development and growth of differentiated branded merchandise; high customer awareness driven by our ability to advertise on national television with a significant budget and utilizing quality advertising campaigns; the superior locations of our stores; and within the US market, our in-house customer financing capability.

These advantages are supported by our balance sheet strength and our financial flexibility.

We believe we are well positioned for growth, particularly when many competitors continue to face significant operational and financial pressures.

Yesterday we announced our sales performance for the Holiday Season, with same store sales up 8.1% in the 9 week period. We are very pleased with our Holiday Season performance, particularly in the US division which increased same store sales by 11.7%. This was on top of a 7.5% rise in comp store sales last year.

We believe that our long term strategy of focusing on the further development of products that differentiate us from our competitors, our best in class customer service, and great marketing campaigns that leverage our leading share of voice have once again proven to be successful.

The UK business was somewhat negatively impacted in the weeks immediately prior to Christmas by exceptionally adverse winter weather, but I'm very happy to report that post Christmas sales have been positive. In addition the Divisional management team has done an excellent job of maintaining good control of gross merchandise margins and cost controls.

Reflecting the very strong Holiday sales, we now expect income before income tax for Fiscal 2011 to be between $287.5 million and $302.5 million, resulting in diluted earnings per share of $2.20 to $2.32, up 20% to 27% on Fiscal 2010, with operating margins up in the US and stable in the UK.

These results include a $47.5 million non-recurring 'Make Whole' payment due to the prepayment of the private placement notes. Excluding the 'Make Whole' payment, income before income taxes is expected to be between $335 million and $350 million, giving diluted earnings per share of $2.54 to $2.66, up 39% to 45% on Fiscal 2010.

The underlying effective tax rate is forecast to increase to about 34% due to an increased mix of US profits and the timing of certain share awards vesting.

Free cash flow was strong and is anticipated to be between $275 to $300 million before the 'Make Whole' payment, significantly above our target at the start of the year.

Signet is the world's largest specialty retail jeweler and operates 1,884 stores in two major markets.

In the US, which accounts for about 80% of our sales, Kay is the number one brand and targets the middle market. Kay's typical customer has a household income of about $75,000. The average selling price, excluding the charm bracelet category, is about $325. Most of the stores are in regional malls, but there is a growing off mall store base as well. There are 910 stores located throughout all 50 states.

Jared is the leader in the upper middle market. Its typical customer has a household income of about $95,000. And the average selling price, again excluding charms, is about $750. It's the

only national off-mall jewelry superstore, and we have grown it organically over the last 15 years. There are currently 180 stores located in 35 states. Overall our US store space is about 55% regional mall based and 45% off-mall.

In the UK, which accounts for the other 20% of sales, H.Samuel is the market leader with 337 stores and is targeted at the middle market, while Ernest Jones is the leader in the upper middle market segment and has 202 stores.

While the market position of the US and UK division are very similar, there are major differences in merchandise mix, reflecting cultural differences between the two markets. In the US you can see from the slide that the dominant category has been diamonds, while in the UK there is a much more even category share led by diamonds and watches, and then followed fairly closely by the Gold and Silver category, which illuminates the differences culturally between the two markets.

Looking at the US division in more detail. In 2009, the total jewelry and watch market was worth just under about $60 billion, with the specialty sector, in which we operate, being a little less than half that at $28.3 billion. Our share of the specialty sector in 2009 was 9.1%, and we are twice the size of our nearest competitor.

The bridal category, which consists of engagement, bridal and anniversary jewelry, account for about 50% of our US sales, up from about 45% of sales three years ago. The other 50% is split between gift giving and self reward.

A major driver of our performance has been the growth of differentiated branded ranges, and their share of our US sales is expected to increase by about 300 basis points during Fiscal 2011. Differentiated ranges are branded items available only at our stores.

Our success in the bridal category has been based on the interaction of our strategic strengths in superior customer service, which enhances the overall customer experience, our supply chain advantages and our ability to offer in-house consumer finance which is particularly tailored to this consumer.

We see opportunities to grow bridal sales even further due to the development of exclusive branded merchandise programs that we currently have in test. If these tests continue to be successful, they have the potential to enable us to more consistently support bridal merchandise, and our Kay and Jared brands, with national television and print advertising throughout the year. We believe this could be a significant new competitive advantage for us.

Within the bridal category, we have two established differentiated brands: The Leo Diamond, which has been described by De Beers as the most successful branded diamond program, and is sold in both Kay and Jared; and the Peerless Diamond, an Ideal cut diamond which is exclusive to Jared.
We are currently testing and developing two new bridal ranges. First a range called ‘Perfected by Tolkowsky’, which is an Ideal cut diamond sold in Kay; and then Neil Lane Bridal, which is the first differentiated setting we have sold, and is being tested in both Kay and Jared. Neil Lane

designs jewelry for celebrities and he's based in Los Angeles. He also designs the ring for the "Bachelor" TV show, which I'm sure most of you are familiar with, through which he has built significant name awareness in our market sector.

Another initiative in the bridal category has been the launch of "Design a Ring" on the Jared website, which supported by virtual inventory, has driven very strong growth in sales of loose diamonds in-store, which are then set by our jewelry workshop, located within every Jared store.

In the gift giving and self purchase sectors, the first major differentiated range was Open Hearts by Jane Seymour, which was launched in 2008. This was followed by Love's Embrace in 2009. While these are exclusive to Signet, we have also developed relationships with some brands where distribution channels are tightly controlled or where we can obtain exclusive designs. A good example of this is Le Vian, an internationally renowned designer and manufacturer of jewelry featuring colored gemstones. We also in 2010, launched Charmed Memories, a charm bracelet range sold in Kay, that has been very successful for us.

In addition to differentiated brands, we also have continuing success in Jared with Pandora, which has attracted many new customers to the Jared demographic.

Our development of differentiated brands make our stores stand out from competitors as unique destinations, and provides our well trained sales associates a powerful selling proposition. These brands also have slightly higher merchandise margins and there is significantly less exposure to competitive discounting.

We drive brand awareness and purchase intent as part of the national television advertising for Kay and Jared. This is becoming increasing important as generic marketing support for diamond jewelry has been largely diminished in the US.

Our scale and proven record of success in developing differentiated branded merchandise enables us to better leverage our supply chain strengths.

Another competitive advantage is the size of our marketing budget, and it is expected to be about $175 million in Fiscal 2012, according to our preliminary budgets. The size of our budget means that for Kay and Jared we are able to use national TV advertising, which is the most effective and efficient form of marketing for jewelry. Our expenditure is made even more productive by the use of highly effective, and well recognized campaigns such as 'Every Kiss Begins With Kay' or 'He went to Jared'.

We have used these campaigns to support our differentiated ranges and this has been a very important factor to the success.

We continue to invest in our internet capability as well, through the introduction of a design your own ring capability in Jared, an increased use of virtual inventory, improved co-ordination between in-store and web-based systems and the development of new selling tools, such as those we are rolling out for Le Vian.

Customer service remains a key differentiator in the jewelry sector as each item is under lock and key, and requires an experienced sales presentation. We have a highly qualified and trained sales force. All of our stores have at least one qualified diamontologist as all store managers have to be so qualified.

We continually train our store staff in customer service and selling skills. This training is based on daily monitoring of key performance indicators, corporate initiatives and monthly customer feedback. Our store staff are well motivated with field incentives based on individual as well as store performance.

This is supported by a very strong corporate culture, with all field managers having had to have been a Signet store manager at some point in time.

We also have strong after sales service support. We train and employ about 1,100 skilled jewelry artisans to better service our customers. This is also an important element in the success we have had in selling extended service plans.

In the US mid-market jewelry retailing, the ability to provide credit is an important sales enabler, and in the US we do this in-house. 50% to 55% of our US sales are transacted using our in-house credit, and we use a specialized, customized scoring system rather than a generic scoring model.

The average outstanding balance is relatively small, at about $1,000 and we have a monthly collection rate of 12% to 14%. We want our customers to repay their credit balance as soon as possible of course so that they can buy more jewelry from us. Our credit customer has a higher average purchase transaction and has a lifetime value 3.5 times greater than our other customers.

We have an excellent historic record of prudently managing credit but during the economic downturn, we experienced, like all credit providers, an increase in bad debt; currently I'm happy to say we are experiencing a rapid recovery towards the better historic norms.

Our ability to identify differentiated merchandise is only one example of our supply chain strengths, which are based on our leading market share, a strong balance sheet, the quality of our buying and merchandising systems and our proven ability to execute.

We also have the most sophisticated direct sourcing of polished diamonds in the middle market. Our scale and systems enable us to better test merchandise before we invest in major product launches. As a result we have a reduced inventory risk and are better able to identify winners and game changers before our competitors.

Turning to the UK division. We are the market leader and are about 1.7 times the size of the number two player. In addition we have the number 1 and 2 specialty jewelry websites in the UK. The business has a high return on capital and solid operating margins. Reflecting the UK economy, it has been under pressure in recent years, however the divisional management has successfully managed costs and gross merchandise margin very tightly and so it has continued to have good cash flow generation.

In Fiscal 2011, despite same store sales being down about 2%, operating margins are expected to be little changed.

The UK division has many of the same competitive advantages as the US: there is a well trained sales force in place; a direct sourcing supply chain capability; merchandise expertise and buying power based on superior scale; great expertise in customer relationship marketing; in addition, the business can utilize best practice and exclusive merchandise from the US division as warranted.

So why invest in Signet. Before I hand it back over to Ron, I would like to reiterate why we believe you should invest in Signet.

We have the potential to gain further profitable market share over many years based on our bridal expertise, the development of differentiated brands, our utilization of national television advertising and our superior customer service; all of which lead to an enhanced customer experience.

Our supply chain strengths allow us to effectively manage commodity cost fluctuations; and our strong financial performance and balance sheet mean that we can continue to make strategic investments at a time when many of our competitors are under operating and financial pressure, and we are able to maintain our customer finance programs when many third party suppliers are reducing credit availability.

Therefore we believe we are well positioned for growth in Fiscal 2012, and beyond.

And now I'd like to turn it over to Ron.

Ron Ristau: Thank you Mike. Good afternoon everyone. I'd like to briefly take you through a demonstration of Signet's financial flexibility and strength, and then speak to some key points reletive to our business in 2012. Our company, which has an excellent record of growth in comp store sales and space growth, and strong operating margins, was impacted by the economic downturn in Fiscal 2009.

Our response was rapid and effective. Costs, inventory and capital expenditure were significantly reduced, while we continued to develop our differentiated brands and gain market share.

In Fiscal 2010, as a result of these activities, we generated $471.9 million in free cash flow. Our comps have also recovered quickly and year to date are up 6.6%, and our operating margin has recovered and is expected to range from 10.5% to 11.0% of sales as we have increased merchandise margins, leveraged our cost base and net bad debt return towards historic levels.

As a result, our adjusted diluted EPS which increased by 22% in Fiscal 2010, is now expected to be up by 39% to 45% in Fiscal 2011, and in the last two years we have generated over $750 million in free cash flow. We have moved from a net debt position of $470 million in Fiscal 2009, to a net cash position, which will range from $220 million to $245 million by the time we complete this year.

Our ability to maintain and increase our gross margin is also a key factor in our success. Over the past three years our merchandise margins have increased, despite fluctuations in commodity costs. This is due to our supply chain flexibility, merchandise initiatives, and price increases. This combined with leverage on store costs as productivity has increased again, and a return of the US net bad debt levels to historic norms, has moved gross margins forward.

In Fiscal 2011, we expect gross margin to improve by 320 to 370 basis points, lead by our performance in the US, and we will continue our focus on gross margin as we move forward. As we stated before, net bad debt is moving back to historic levels.

The granting of credit intelligently to facilitate jewelry sales is one of our key competitive strengths. Our strong balance sheet enables us to self fund this activity.

We have an excellent long term record of managing credit, and as you can see from this slide, between 1998 and 2008 our bad debt percentage ranged from 2.8% to 3.4% of US sales. During the economic downturn we did of course experience higher bad debt levels, primarily due to the rapid changes in employment levels, but we have again rapidly recovered.

Note that our credit process that Mike indicated is designed for rapid repayment and the generation of new open to buy for our customers. So in this year we would expect our bad debt to again improve by 130 to 150 basis points, reaching 4.1% to 4.3% of sales.

From a capital spending perspective, we historically, when we were building out the chain, we were spending a lot of capital, approximately $123 million between 2004 and 2008.

We have very demanding criteria for store site selection, which has produced a store fleet that we believe represents superior locations versus our competitors. We remain ready, willing and able to open new stores as these criteria are met, and developers become active again. During the economic downturn, capital expenditure was carefully managed, reaching approximately $43.6 million in 2010. In Fiscal 2011, spending was increased to support store maintenance and information technology, however as we look forward, further increases will be required.

We hope to increase next year new store activity, continue to support the existing fleet with refurbishments worthy of the sector leader and to further leverage our competitive strength in IT infrastructure and internet capabilities.

Our operating margins, which during the period 2002-2007 averaged approximately 12.5%, we’re moving back toward that direction.

We experienced declines during the economic downturn, particularly in Fiscal 2009, as our store productivity fell and bad debts increased.

As this chart demonstrates we are seeing strong recovery in these trends as these trends reverse. Operating margins will be up to between 10.5-11.0% of sales, a 240-290 basis point improvement from Fiscal 2009 [should be Fiscal 2010].

The primary drivers of our recovery are improving levels of store productivity, and bad debts which are moving back towards historic trends. We believe these two trends are strong and position us well as we move into Fiscal 2012.

Turning to the preliminary outlook for 2012. We will focus our operating strategy on driving sales growth and reinforcing our competitive advantages, with particular emphasis on the differentiated brands we've mentioned and marketing to drive comp store sales increases.

We plan again to maintain tight control of gross margin and SG&A costs, helping us to achieve operational leverage from sales growth. We will however experience some intelligent increases in costs, primarily in marketing expenditures to drive sales growth and spending for associate support.

We plan some additional investment in working capital to support sales growth, particularly in differentiated brands where we do expect to roll out the Neil Lane and Tolkowsky programs that Mike spoke about. We continue to look to improve inventory productivity where practical, but our investment will go up slightly in Fiscal 2012.

Capital expenditure, as I mentioned, will be higher, as we expect to carry out more new store refurbishments further reducing our backlog**,** and we do target to open more new stores in the US – approximately 25 stores at the current time.

Investment in management information systems and internet capabilities will be increased to further drive our competitive advantage in these areas. While increasing investment, we will of course maintain our disciplined approach and will continue to apply our demanding return on investment criteria.

Another key number you should be aware of is that next year we expect our interest expense to range from $6 to $7 million as the Make Whole payment we experienced this year will not repeat, and the impact of debt pay-off is reflected fully in our results.

We will see our effective tax rate range as the US continues to increase its percentage mix of profits, and we are currently planning it at approximately 36%.

So we believe we are well positioned for 2012, thank you for your attention to the presentation, please join us in our break out sessions, which are scheduled for 12:50 and 4:10 this afternoon.

Thank you very much.