

Signet Jewelers Limited

Fiscal 2016 First Quarter Financial Results

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Ike Boruchow, *Sterne Agee*

Scott Krasik, *Buckingham Research Group*

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Janet Kloppenburg, *JJK Research*

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PRESENTATION

Operator:

Ladies and gentlemen, thank you for standing by. Welcome to the Signet Jewelers Fiscal 2016 First Quarter Financial Results call and webcast. During the call, all participants will be in a listen only-mode. After the presentation, we will conduct a question and answer session. Instructions will be provided at that time. If at any time during the conference you need to reach an operator, please press the star, followed by zero. Please note that this call is being recorded today, May 28th, 2015 at 8:30 a.m. Eastern time.

I would now like to turn the meeting over to your host for today's call, James Grant, Vice President of Investor Relations. Please go ahead, James.

James Grant:

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Good morning and welcome to our First Quarter Fiscal 2016 Earnings call. On our call today are Mark Light, CEO, and Michele Santana, CFO. The presentation deck we will be referencing is available under the Investors section of our website Signetjewelers.com. During today's presentation 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 factors, cautionary language and other disclosures in the Annual Report on Form 10-K that was filed March 26th with the SEC.

We also draw your attention to the Slide 2 in today's presentation for additional information about forward-looking statements and non-GAAP measures.

Now, I'll turn the call over to Mark.

Mark Light:

Thanks, James, and good morning everyone. In the first quarter we delivered very strong top line and bottom line results. Signet comps increased by 3.6% and earnings per share metrics showed impressive increases over last year. Most notably, adjusted EPS was $1.62, which was 25.6% increase over the prior year, and when measured on an apples-to-apples basis versus last year by excluding Zale our EPS was up $0.06 or 4.7%. Each divisions had store increases led by UK division with increase of 6.2% while our newest division, Zale, had a 5.6% increase. The Sterling division had 2.3% comp store increase which was the division's 22nd consecutive quarterly comp increase. In terms of merchandise, Signet's bridal and fashion diamond collection performed well across the organization, and by selling channel our broad base strength was evident with outlet and eCommerce delivering strong results.

Now let's focus on the performance by our divisions, starting with our Sterling division. Sterling delivered a 2.3% comp sales growth led by Kay with an increase of 3.6%, Kay's 25th consecutive quarterly increase. Kay saw strength in diamond jewelry across its merchandise portfolio, in bridal and fashion, branded and non-branded, and a variety of products. Examples include Neil Lane Bridal and Tolkowsky, Diamonds in Rhythm fashion pendants, and solitaire earrings and rings, and watches were strong also. We launched Pinterest and Instagram for Kay in time for Mother's Day. These are brand-new marketing platforms for our customers. And nearly every field operations key performance indicator improved year-over-year. Importantly our customer service index scores are the highest they have ever been.

Our Jared store had comp sales increase 0.2% while our total sales were up 4.4%. Jared had success around fashion collections such as Neil Lane Designs, Diamonds in Rhythm, Lois Hill, Earthly Treasures by Smithsonian and Le Vian, and in watches Movado and Citizen were very strong, and our Vera Wang test continues to perform well in Jared stores. We recently launched a test of incremental radio advertising in several markets that helped strengthen our bridal position. In addition, we also launched Jared's first ever brand book used for direct mail marketing and in-store use.

We continue to drive our critical traffic building repair and design center business. We recently launched a new managers training system for our design and service centers in our Jared stores to enhance our artisans' ability to deliver high quality product in even faster timeframes.

Given the investment and our initiatives in our Jared business, we feel we are well positioned to capture profitable market share.

Now moving on to our Zales division, Zales delivered a strong first quarter of 6.1% comps due to a variety of planned investments and initiatives around merchandising, marketing and field operations. Beginning with merchandising, our branded bridal and fashion diamond collections performed very well led by the Vera Wang Love collection, the Celebration Diamond and Unstoppable Love. As we continue to focus on

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expanding depth versus breadth in merchandise assortments our current brands continue to drive sales growth.

The Zale store teams are scoring well on key customer service and selling skills performance indicators. They are highly engaged and executing better than ever.

In the first quarter, there were a variety of other successes beyond our Zales store performances. Our Peoples stores in Canada and our Piercing Pagoda stores throughout the United States all delivered comps in excess of 6%, and eCommerce performed very well also.

Driving the results is our continued phenomenal collaboration between all of our division team members to 'Signetize' our business. And speaking of 'Signetizing', several areas are actively engaged in collaboration such as field operations, marketing and merchandising., And we are also seeing benefits from consolidated real estate and diamond-buying teams as well as alignment around our human resources departments. And, we are in the process of finalizing our technology roadmap for the next several years which will include a single IT function for the enterprise, a roadmap of common technology platforms for us to expand and grow our business, and digital experiences that enable us to know our customers intimately while seamlessly servicing them.

In the UK, the main drivers include initiatives around diamonds, success in fashion merchandise and watches and a continued focus on sales rather than tasks. The UK continues to drive diamond sales with their improved sales training and marketing initiatives geared towards bridal customers. Perfect Fit, the Forever Diamond, Neil Lane, Leo and Tolkowsky all were strong in the first quarter, as well as Le Vian diamonds, and our Vera Wang test performed well also. Outside the diamond category, watches and beads also did very well. Our UK division experienced strength across all selling channels. eCommerce sales increases were higher than total Signet eCommerce sales increases, and our new outlet stores performed well. Our UK division continues to embrace a culture of collaboration and is focused on continuously enhancing their diamond selling skills journey.

Signet continues to gain profitable market shares in both Sterling and in our Zale division, as well as for Signet overall. We have a highly collaborative, team-oriented mindset as we integrate our businesses. We continue to see progress against all of our strategic pillars and specifically in best in bridal; and our omnichannel approach is clearly thriving as we see strength across all of our selling channels.

To sum up, we're seeing terrific contributions and collaborations from all of our divisions. Zales continues to gain synergy and operational momentum. The UK is showing unprecedented comp growth as a result of our collaborative culture, and Sterling is consistently showing strength with positive comps and operating results. I feel as good as ever about our future for the near, the medium and long term.

And with that, I'll now turn the call over to Michele for a run-through on our financials.

Michele Santana:

Thank you, Mark, and good morning everyone. So starting with our sales performance, I'll point out a few highlights which Mark just provided an overview of the numbers.

In our Sterling division, total sales increased 4.5% to $944.2 million which included a same store sales increase of 2.3%. The average transaction price of Sterling increased by 4.7% and the number of transactions decreased by 3%. This is driven by our merchandise mix including bridal and higher price point fashion collections.

Our Zale division total sales were $437.1 million for the quarter which included a same store sales increase of 5.6%. Total sales also included an $8.6 million unfavorable revenue impact due to purchase

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accounting adjustments related to deferred revenue. As Mark indicated, sales were particularly strong in our Zale division and branded bridal and branded diamond fashion.

In our UK division, total sales decreased 3.4%, but increased 6.6% on a constant exchange basis. Sales were $146.5 million with a comp sales increase of 6.2%. The average transaction price increased by 3.6% and the number of transactions increased by 2.6% due to merchandise mix with strong performance in branded bridal, fashion diamond jewelry and fashion watches.

Moving on from sales, I'll walk through Signet's consolidated Q1 performance, then we'll turn and analyze Signet's adjusted results.

So on Slide 8, the table provides a reconciliation of Signet's adjusted results to our consolidated results. The difference between adjusted Signet and Signet are the columns reflecting purchase accounting and transaction costs with transaction costs including our integration related expenses. On a GAAP basis, EPS was $1.48 per share and at the high end of our guidance.

Purchase accounting adjustments, which include a reduction to deferred revenue, amortization related to inventory fair value step-up and amortization of unfavorable contracts, were dilutive to EPS by $0.09. Transaction costs were responsible for $0.05 cents of dilution. Transaction costs related to our integration were a couple of pennies per share higher than first anticipated and that's primarily due to timing associated with various consulting expenses. So let's move on and we'll look at operating income by division.

Operating income of $176.2 million or 11.5% of sales consisted of the following components. Sterling Jewelers was $178.2 million or 18.9% of division sales and that's up 50 basis points from last year and a record Q1 high. Zale operating income was $15.5 million or 3.5% of division sales inclusive of purchase accounting adjustments. Zale's performance consisted of $10.4 million of profit from the Zale's Jewelry operating segment and $5.1 million from the Piercing Pagoda operating segment. Now when excluding costs of $11.4 million related to purchase accounting, which we just previously discussed, the Zale division operating profit was $26.9 million or 6% of adjusted division sales. Our UK operating profit was $0.5 million or 0.3% of division sales versus no profit last year. Other, which primarily consists of corporate and administrative expenses and Signet's diamond sourcing subsidiaries include $6.4 million of transaction costs related to integration activities.

We're continuing to show the detail of adjusted Signet in the Zale operations to give further visibility into our results, which we'll expect that we'll do this until we fully comp in Q3. After that point, we'll provide Zale details consistent with our divisional disclosures.

The presentation on Slide 10 takes adjusted Signet, which is shown on the far right, and then breaks it into two parts. One part is Zale operations, shown in the middle columns, and the second part in the left-hand columns is adjusted Signet excluding Zale. Adjusted Signet excluding Zale is the rest of Signet inclusive of finance interest and taxes. From sales to operating income, this gives you comparability to prior year results. In addition, the information is provided to give you visibility as to how the Zale operations performed in the first quarter. So continuing on, let's review Signet's adjusted P&L results below the sales line.

Adjusted gross margin was $581.4 million or 37.8% of adjusted sales and that was down 80 basis points versus last year. The decrease in rate was driven by the addition of Zale which impacted the gross margin rate by 90 basis points as Zale currently operates with a lower gross margin structure than that of the Sterling division. Excluding the Zale division, the adjusted Signet gross margin rate would have been 38.7%, up 10 basis points, primarily due to favorable commodity cost. Adjusted SG&A was $450.9 million or 29.3% of adjusted sales, and that was up 70 basis points versus last year's rate of 28.6%. Excluding Zale, the adjusted SG&A rate was also 29.3% and that's due to higher planned advertising expense in our

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Sterling division and higher central costs due primarily to legal and payroll related costs. The increase in advertising expense, as Mark had previously mentioned, is due principally to the launch of new Jared radio and print advertising among a variety of other marketing initiatives and investments that impacted the rate by 40 basis points. This higher SG&A ratio is a function of investing for future growth and we expect our SG&A run rate to improve this year.

Other operating income was $63.5 million. This increase of $9.5 million was due principally to higher interest income earned from higher outstanding receivable balances. Adjusted operating income in the first quarter was 12.6% of adjusted sales. Excluding the Zale division, the adjusted Signet operating margin would have been 15.3%, leveraging up 20 basis points.

Adjusted EPS was $1.62 compared to $1.29 in the first quarter of fiscal 2015. On a comparable basis, that is when excluding this year's impact from Zale and capital structure and financing, EPS was $1.35, representing a 4.7% growth over last year.

Our strong operating results afforded us the opportunity to repurchase $21.9 million of Signet stock in the first quarter, in line with our capital allocation plan. At the end of the first quarter, there was $243.7 million remaining under Signet's 2013 share repurchase authorization program.

Now we'll move on to the balance sheet and we'll start with a look at our inventory. Net inventory at the end of the quarter at approximately $2.5 billion, an increase of nearly $1 billion or 63% over last year and that's driven in part by sales growth of 45%. The inventory level increase was driven primarily by the acquisition of Zale. To a lesser extent, inventory levels were also impacted by new store growth of $40 million and higher diamond inventory of $56 million associated with our bridal business and our diamond sourcing initiative. This higher level of diamond inventory reflects our continued initiatives around our Best in Bridal strategic pillar.

So now we'll turn attention to in-house credit metrics and statistics. In-house credit remains an important component of Sterling division's business and a competitive advantage. Net accounts receivable increased to $1.5 billion, and that compares to $1.3 billion last year, up 14.7% driven by higher sales and an increase in the credit penetration rate.

Our credit participation was 60.7% compared to 58.1% last year. The increase in credit participation was attributed primarily to credit decision engine improvements made in April of last year, higher outlet credit participation and strong guest acceptance of our credit offerings.

The average monthly collection rate was 12.6% compared to 13.2%, due primarily to three reasons. First, our customers continue to opt more for our regular credit terms which require lower monthly payments compared to the 12 month interest-free program. Second, our mix of bridal increases due to our Best in Bridal strategy and this creates a higher receivable average receivable balance. Our required scheduled payments do not increase proportionally with the higher merchandise mix shift. And finally third, like other consumer loans, more principal is paid off later, so as our portfolio has grown more in the last year, proportionately more of it will be paid later. So let's move on to a few other credit statistics around our in-house finance program.

Net bad expense for the quarter was $28.1 million compared to $22.3 million last year, an increase of $5.8 million, and that was driven primarily by the growth in receivable balance from increased penetration and change in the credit program mix. Other operating income was $63.5 million compared to $54 million last year. This was an increase of $9.5 million and is due primarily to more interest income on the higher outstanding receivables, as well as the shift away from interest-free programs. So the net impact of these two items was income of $35.4 million compared to $31.7 million in the prior year, or an increase of $3.7 million. Our portfolio continues to perform well as evidenced by the net impact of bad debt and other

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operating income, as well as the allowance as a percentage of accounts receivable being fairly consistent. So now we'll move on to our financial guidance.

Our financial guidance for the second quarter of Signet comparable store sales are expected to increase 2 to 3%. Second quarter adjusted EPS is expected to be $1.11 to $1.16. As a reminder, adjusted EPS is EPS less the two set of adjustments that are shown on Slide 15, being purchase accounting and our transaction costs related to integration.

Our Q2 comp sales projection reflects continued sales growth and a strong hurdle rate achieved by Signet last year driven by Sterling with 6.7% comp increase. Our comp guidance also reflects our current sales run rate. And, our guidance also reflects our proven ability to protect our bottom line and to drive financial results through EPS growth.

From an effective tax rate standpoint, Signet's fiscal 2016 annual rate is anticipated to be 28 to 29%, and the difference versus fiscal 2015 is principally the full year effect of owning Zale and having our capital structure in place.

Capital expenditure guidance for the full year is $275 million to $325 million and our net selling square footage is projected to grow approximately 2 to 3%, and I would reference you to our news release for further detail by division.

And lastly, I would like to reiterate our confidence in delivering our operating profit synergy goal of $150 to $175 million which, using our current weighted average shares outstanding, equates to $1.90 to $2.20 of earnings per share within the three-year period ending January 2018. As we previously guided, 20% of the synergies will be achieved by end of fiscal year-end and will be back-end loaded to the second half of this year. As a result, synergies are not a material component of our Q2 EPS guidance.

That concludes my remarks on the financials, and with that I would like to turn the call back over to Mark.

Mark Light:

Thank you, Michele. In conclusion, we have seen terrific contributions and collaboration from every division, and I want to congratulate and thank all of the Signet team members for a great first quarter. Their dedication and passion delivered significant value for Signet shareholders, and positions us for growth into the future.

Now, we'll take some time for your questions.

Operator:

At this time, those with questions should lift their phone receiver and press star, followed by the number one on their telephone keypad. To cancel a question, please press the number sign. Please hold for a brief moment while we compile the Q&A roster.

Your first question is from Dorothy Lakner with Topeka. Your line is open.

Dorothy Lakner:

Thanks and good morning everyone. Congratulations on a nice start to the year.

Michele Santana:

Thank you. Dorothy.

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Mark Light:

Thank you, Dorothy.

Dorothy Lakner:

Just looking over the comp results, Sterling obviously has many, many quarters of growth here, but, you know, Kay seems to be performing a bit better versus Jared. Is that just the comparison? I know last quarter you talked about some softness in particular areas of Jared's business so I just wondered if you could put a little color around that? Then also for Michele, maybe a bit more color on how you see the synergies sort of playing out in the back half of the year. Thanks.

Mark Light:

Thank you. I'll take the first one, Dorothy. As far as Jared goes, I want to start off by saying that we believe that Jared is definitely gaining profitable market share against their competitive set, and as you said, Dorothy, Jared has had positive comps for a while now. Jared itself has had 21 out of 22 quarters of positive comps, and so we feel relative to the Jared business we are definitely capturing profitable market share. That being said, we're always focused on enhancing and improving our business, and as I said in my prepared remarks, we are testing incremental radio to see how we can drive the business, we're testing new direct mail marketing. We have a lot of new exciting programs in place that we're testing for the fall season, so we're very confident that we can continue to capture profitable market share for Jared going forward.

Michele Santana:

Dorothy, on your synergy question, we have a clear line of sight in terms of our achievement of the synergies in the back half of the year. Previously, and then as part of my prepared remarks, I had mentioned we've guided to 20% of realization of synergies for fiscal '16, and broadly, you know, those synergies would follow that curve we talked about with 30% between revenue cross-selling, 20% from SG&A and 50% gross margin, so I think it will roughly follow that. Other than that, we're not going to really break down that synergy guidance, that 20% between what we expect to fall in Q3 and what we expect to fall in Q4, but we would expect to start seeing the synergy realization in the back half of the year.

Dorothy Lakner:

Versus really not any in the second quarter?

Michele Santana:

Yes, that's right, Dorothy. We said previously our expectation was it would really be immaterial in terms of synergies realized in Q1 as well as Q2, and that this was really a back half of the year story with synergies.

Dorothy Lakner:

Great. Thank you so much for the clarification.

Michele Santana:

Sure. Thank you, Dorothy.

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Operator:

Your next question is from Joan Payson with Barclays. Your line is open.

Joan Payson:

Good morning. Congratulations.

Mark Light:

Thanks, Joan.

Michele Santana:

Thanks, Joan.

Joan Payson:

So in terms of Zale having the kind of strong growth that it had in this quarter, is this the type of growth we can expect to see from that concept going forward, or do you expect further acceleration as more new initiatives are introduced?

Michele Santana:

I'll start off and then I think Mark can add a little bit of color. One of the expectations I would say is Zale, given it's low on the maturity curve in determines of growing that top line, you would expect that they are going to see acceleration of their sales at a much faster rate than what we would see with our other divisions. Mark, do you want to add some comment in terms of the pace or continued trend?

Mark Light:

Well, I don't know if you want to lock in the 6.1 for all of your modeling.

Michele Santana:

No.

Mark Light:

But we do feel good about where the Zale's business is going, and as Michele mentioned, as it relates to maturity curve, a lot of the business opportunities and initiatives that we're sharing with the Zale division come from initiatives we have learned were successful in our Sterling division for years. So as we said in our release, we do expect the Zales to have stronger increases going forward than the Sterling division. Whether or not they are at this rate we certainly hope so but we'll do everything in our power to make sure we can do as much as possible.

Joan Payson:

Great. In terms of the second quarter guidance, on the comp line, the 2 to 3%, it’s a little bit slower than what we have seen for a while now. What do you think is driving the deceleration? Is it based on the tougher Sterling comparisons, or something that you’ve seen so far in season?

Mark Light:

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First of all, I think Michele mentioned in her comments, we are going up against strong hurdle rates and we have to take that into consideration when looking at our guidance. So it starts with hurdle rates and then it goes into we're making investments for our business and a lot of those investments are back-ended, but we still think our guidance is going to be a healthy—is a nice increase for the business for the second quarter.

Michele Santana:

Yes, I would just pile onto Mark's it is a comp growth of 2 to 3%. We talked about the hurdle rates and the continued consecutive comp—quarterly comp growth that we're expecting to achieve, and current run rates have been factored into that and our proven when you look at our EPS guidance, I think it all comes down to our proven ability to execute and drive EPS growth.

Joan Payson:

Great. Thank you.

Mark Light:

Thank you.

Michele Santana:

Greetings, Joan.

Operator:

Your next question is from Simeon Siegel with Nomura. Your line is open.

Simeon Siegel:

Thanks. Good morning guys.

Mark Light:

Good morning.

Simeon Siegel:

So Sterling saw gross margin improvement which you called out. Could you talk about the impact you'd expect to see coming forward from promotional environment and then the commodity costs? Mark, to your point about the initiatives going onto Jared, can you talk about the drivers that could spur the reacceleration? Kind of your market share commentary, and then maybe any thoughts on when you would expect to see sales impact from that increased advertising? Thanks.

Michele Santana:

Why don't I kick it off with the gross margin? What I would say, Simeon, we don't give full year guidance in terms of gross margin, nor do we give quarterly guidance on what the gross margin levels are expected to be, but to give you some flavor in terms of directionally, we would expect that we're still going to see some benefit coming through from our lower commodity costs associated with our gold pricing.

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From a promotional standpoint, again, I would say that we're no more promotional than we have in the past, so I don't think promotions really have an effect or play into what we see on the gross margin line item. I guess, Mark, do you want to talk through some of the Jared marketing initiatives?

Mark Light:

Yes. First of all, as I said, we have tested incremental radio advertising in certain markets. We actually built the Jared division - when we started with Jared, before we could afford national TV, we built the Jared division on continuity radio and having radio is a wonderful way to develop our business and kind of describe what Jared is all about. So we're getting back into testing the radio, to see that we can get the lifts in certain markets and specifically for our Best in Bridal program for the Jared business.

Advertising is something that you don't see automatic sales lifts; it's something that's a building effect. We always test programs in the spring season to get a good understanding of the elasticity and what—we can do some type of relations as it relates to what type of growth we could expect in the fall. So a lot of this is very common for us to test different types of programs in the spring to hopefully rollout through the fall. So you have incremental advertising as it relates to radio, which was in the test mode. As I stated, we have our first ever branded book in our Jared store so both customers, current customers can get direct mail and our stores can sell off of that and that's something we hope, and as we analyze the results, something we carry through the fall. There are certain product launches that we're in test right now, Simeon, which I'm not going to share for competitive reasons, that we're very excited about that could be very strong launches or extended tests for the fall season and one, which I mentioned was Vera Wang. We're finding early results that Vera, her product is actually definitely doing very well with the Jared customers.

Simeon Siegel:

Perfect. Thanks a lot guys and good luck for the rest of the year.

Mark Light:

Thank you.

Operator:

Your next question is from Ike Boruchow with Sterne Agee. Your line is open.

Ike Boruchow:

Hi. Good morning everyone. Thanks for taking my question, and congrats on a great quarter.

Mark Light:

Thanks, Ike.

Michele Santana:

Thanks, Ike.

Ike Boruchow:

I guess I wanted to focus a little more on the Zale business. First, can you give some color—I'm sorry if I missed this—on their gross margin performance in the quarter year-over-year since we don't have the

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like-for-like compares to really look at? Then also, when we start to think about the synergies, Michele, you mentioned, blowing into the P&L in the back half, how should that process evolve? Should we begin by seeing procurement benefits that would benefit the gross margin line, or would we start by seeing cost saves on SG&A, or is it both simultaneously? Then the very last question would be the ADS agreement at Zale, should that start to add a few million dollars in EBIT to the segment every quarter beginning in Q4 this year, or how should we think about that?

Michele Santana:

In terms of gross margin with Zale, and really there's not a good comparison for you, unfortunately not. We didn't have them at Q1 and if you look at what their reported gross margins would have been, it's really apples and oranges because they were on a LIFO basis, so I can't talk directly to the gross margin other than we know it is lower than our Sterling division and it's an area of focus as it relates to our synergies. We anticipate 50% of our synergies are going to come through gross margin between our merchandising and sourcing initiatives, which really kind of leads then into your second question on how to think about the synergies and is it SG&A versus gross margin? I think you're going to start seeing them come through a little bit both at the same time. When we talk about our gross margin synergies, we'll start seeing some from the procurement process. The other one we talked about from a gross margin standpoint is our discount controls and so that is something that we've been currently working on, on getting more systematic, more visibility into the discount control process at Zale. So I think that's when we can start seeing it, at the tail end of this year, as well as we'll start getting some of the that SG&A savings coming in on the back half. So I think it will be a little bit of a blend between those two.

Then your final question, Ike, in terms of ADS, you're correct that ADS contract goes into effect in October, so we will have, at the tail end of the year, ADS in place and we would expect to see some benefit for that last quarter of the year.

Ike Boruchow:

Got it. Thank you.

Michele Santana:

Then just to remind you, Ike, on that front, we did—from a synergies standpoint we did exclude our ADS savings which has quantified that full-year effect as $22 million. That was excluded from our synergy number, but I think we'll see some benefit at the tail end of our fourth quarter.

Ike Boruchow:

Is the ADS benefit in gross margin or SG&A?

Michele Santana:

It would be in SG&A.

Ike Boruchow:

Okay. Great, thank you.

Michele Santana:

Thanks, Ike.

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Mark Light:

Thank you.

Operator:

Your next question is from Scott Krasik with Buckingham Research. Your line is open.

Scott Krasik:

Hi everyone.

Michele Santana:

Good morning.

Mark Light:

Hi, Scott.

Scott Krasik:

Let me pick that up; I'm having some problems with the phone. Hi. Can you hear me?

Michele Santana:

Yes.

Mark Light:

Yes, we can.

Scott Krasik:

Sorry about that.

Okay. Good quarter. Just qualitatively or quantitatively, I think Mother's Day is probably the signature event in 2Q. Can you talk about how people responded to your events there? Then there's a lot of talk around fashion watches starting to slow. You called out some pretty good results in watches. How would that affect your business? If people buy more fashion jewelry, would they buy other watches? Thoughts there as well. Thanks.

Mark Light:

Yes. As it relates to Mother's Day performance, Mother's Day is 10 days of our entire second quarter, so we feel—we obviously took Mother's Day into consideration and we feel good about the guidance that we gave you all, so that's as much as I'm going to say about Mother's Day performance.

As it relates to fashion watches and fashion jewelry, fashion watches, specifically the Movado brand is doing very well with us. Our Citizen brand which has a lot of fashion styling within their men's are doing well and continues to gain momentum in doing well. Then our UK, our time piece business is doing very well also. So as a whole, I'm not sure if I understand the question completely—how does fashion watches have an effect on fashion jewelry—we don't see a lot of tradeoff there. It's pretty much a different

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customer set. It is in the fashion world but there's components of it. What we see more commonly is within fashion jewelry you may have a tradeoff of a diamond necklace versus a bracelet or something of that nature. Hopefully that answers your question, Scott.

Scott Krasik:

It does, and then just more specifically to the beading part and charm part of your fashion jewelry business?

Mark Light:

Yes. In the UK our bead business is very strong. In our US business, whether it be Sterling or Zale's, we continue to see an improved run rate from the numbers that we shared with the market in the fourth quarter. So there's definitely an improved run rate going on and in the bead business is an important business for us and we continue to partner with all of our bead partners to continue to enhance our assortment and enhance our promotions and enhance our marketing.

Scott Krasik:

Awesome. Thanks guys.

Mark Light:

Thank you.

Operator:

Your next question is from Jeff Stein with Northcoast Research. Your line is open.

Jeff Stein:

Good morning guys. I'm wondering, as we look at your comp guidance for the second quarter, can you talk to us a little bit about what the assumptions are for the various divisions? In other words, kind of what is the assumption in US, UK and Zale's? Thank you.

Michele Santana:

Good morning, Jeff. Thanks for the question.

You know, Jeff, unfortunately we don't break down the guidance between the expectations whether it's store brand or even geography. I mean, you know, all I would add to that is, directionally, our UK, they really have some strong momentum going. We're really pleased and proud of the performance that they have. But beyond adding that little bit of color, we don't break it down by geography.

Jeff Stein:

Okay. I noticed that in the first quarter you closed 11 stores in the Zale's division, and I think if I recall back in Q4 you kind of indicated that we were looking for about flat for the year. So are you going to be adding locations, or has anything changed with regard to plans for openings and closings in that division?

Mark Light:

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Yes. In the Zale division, Jeff, we expect to open up to 35 stores, about 25 Zale's and 10 Piercing Pagoda store locations, and we plan on netting out at basically flat growth. So you've got 11 so far and there's a chance there could be another 20, 25 closed, but we watch that—literally, we watch it every month, every quarter, because a lot of these stores that used to be poor performing stores, now that are getting some of the synergies and the benefits of the collaboration from Signet, they suddenly turned to profitable stores as we have seen over the years both in our UK division and Sterling division. But for now, the plan will be up to 35 stores: 25 Zale's and 10 Piercing Pagoda, and probably closing about the same amount and being flat as far as square footage goes for the Zale division.

Jeff Stein:

Great, thank you. One quick one for Michele. The Other operating income line, you showed a real healthy increase there. Would that be kind of a run rate we should look to continue for the balance of the year? Or was there something in Q1 that would cause it to be higher than Q2 through Q4?

Michele Santana:

I would say, Jeff, there was nothing unusual in Q1 that would have caused that to be higher. But again, as you know, we won't give guidance for the full year on a financial line item or even on a quarterly basis. I think you can just look at our run rates and make some assumptions.

Jeff Stein:

Got it. Okay. Thank you very much.

Michele Santana:

Thanks much, Jeff.

Mark Light:

Thank you.

Operator:

Your next question is from Oliver Chen with Cowen & Company. Your line is open.

Oliver Chen:

Thanks a lot. Solid results, guys. Thank you.

Michele Santana:

Good morning, Oliver.

Oliver Chen:

Good morning. I know you've been doing strategic studies on the brand architecture as it relates to the opportunities and cross-sellings and the synergies on that side. Could you just elaborate on what might be possible in terms of making sure you segment your brands optimally across your banners? Then, on holiday, it would be nice if you could just give us a little refresher on what you're most excited about in terms of year-over-year innovation as you look forward to the holiday selling season.

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Mark Light:

Okay. As far as the brand segmentation studies, thank you for bringing that up, Oliver, because you give me a global opportunity to do a commercial here. On June 24th, we are hosting the Investor Conference and at that time we will be sharing with the market our brand segmentation and how we plan on taking our brands into the future our, store brands. But I'll give you a very quick overview, Oliver, because I won't give any adjustments, but the bottom line is the core of our customers in the US—Zale's, Kay and Jared's—within the mid-market, they actually have different customers, different base customers within that mid-market and it's very clear to us that there is different segmentation within the mid-market. We will define those segmentations to the market and to all of you at the Investor Conference so you can understand from our research and understanding our core customers how we can take our core customers for each brand—it was one of the nicest things that we found during the analysis of the Zale's acquisition—is that Zale's customers within the mid-market is actually different than that of Kay's and Jared, and so we're going to have strategies and initiatives how we can penetrate those segmented customers even further. So I need a lot more time, Oliver, to get into it and so please come to the conference and we'll be able to discuss it in more detail.

As it relates to what we're most excited about the holiday, I'm not going to share too much with you, Oliver, because we have a lot of competitors out there, but I will tell you between our merchandising and marketing teams there's a lot of exciting new tests in place, as much if not more than I've seen in our company over the last several years, that we are excited about launching in the fall, during this fall season, and again, I'm not going to share with you but I will just give you that I've been here a long time and we've got—this particular up and coming holiday season we have more in test that we're excited about than I remember for the last couple of years. So I'll leave you with that and hopefully the customers will react in the same way as I am excited.

Oliver Chen:

Thank you, that's helpful. As we look across retail, wearable technology does seem to be occupying the minds of consumers, and I know that you have an awesome bridal business, as well as a unique proprietary brand portfolio, but is that something you're seeing or thinking about as you plan product and demand creation on the marketing side?

Mark Light:

First of all, it's something we're definitely thinking about. Anybody who is selling any type of product on—whether it be worn on their body, their wrist, their neck, is a competitor of ours and wearable technology is something we're all over, and we're obviously talking to all of our current partners and looking into opportunities of what we can do to be in that facility and it's something we're all over.

As it relates to our current watch business, it is not affecting our watch business. Our business, as you've heard and seen, our watch business is doing well in the UK and the US, but we are all over wearable technology. We will stay very close to it. I'm sure in the near future, you'll start seeing some opportunities for the Signet business, probably more in the next year timeframe, but we are definitely all over it.

Oliver Chen:

Okay. The last thing is, on Jared, you have talked about it on the call—thank you for the details—but what's the story for the nature of the opportunity and the product assortment? Are you thinking that the gifting side of the business, in terms of I was just curious with respect to the price points of the portfolio, where you felt like maybe you could install more product or brand newness?

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Mark Light:

On both fronts of the business we see opportunities. On the gifting side, we definitely have some tests in place with some exciting things that hopefully will run through the Christmas season if the tests continue to do well. On the bridal side, as I stated, Vera Wang is testing very well on the bridal side and bridal business is of critical importance and if we're going to be best in bridal, our Jared needs to continue to invest in the bridal business. So, on both sides of the business we are testing and looking into enhancing both our gifting and our bridal business in the Jared business, as well as our entire business but obviously Jared has got a little bit more focused on it.

Oliver Chen:

Thanks guys. Best regards for the spring and summer, and holiday.

Mark Light:

Thank you.

Michele Santana:

Thanks, Oliver.

Mark Light:

Same to you, Oliver.

Operator:

Your next question is from Janet Kloppenburg with JJK Research. Your line is open.

Janet Kloppenburg:

Good morning everyone. Thanks for all of the detail this morning. Mark, just one more question on Jared. I'm wondering if you think that your initiatives can drive traffic improvement in the second quarter, or if your second quarter guidance on comp sort of assumes that there will be an unchanged trend but perhaps that it should improve as we move through the rest of the year? Then with respect to Zale, I wondered about the training program to upgrade the associates and how long we were in that process, because I think it's helping a lot.

Mark Light:

Thank you, Janet. As far as Jared goes, built into our guidance is our—within that overall guidance Jared's business is built into that, and we're not going to get much more detailed into that, but I will say, as I said it earlier, is that what we do during the second and third quarter—excuse me, the first and second quarter is a lot of testing going on for the fourth quarter. So a lot of the testing that we're doing will help benefit the third and primarily the fourth quarter.

As far as Zale's training programs go, I've said this over and over but diamond selling training is a journey. It's not—there's no destiny, and the Zale teams are doing tremendous on, first and foremost, understanding the basics of how to share with customers the features and benefits of selling a diamond, specifically selling Vera Wang and branded diamond programs, and we'll continue to enhance that journey and taking further and further steps in enhancing the Zale training team. So we have basic training going on now and we will advance the next level of training. We're right now getting their teams

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ready for career development training for next year, so this training is a true journey. And quite frankly, we have a very good template in our Sterling division that we're sharing with the Zale's team, and again going back to maturity curve, it will help the Zale business continue to grow but it's not something that it happens overnight.

Janet Kloppenburg:

Thank you, Mark.

Mark Light:

Thank you.

Operator:

Your next question is from Rick Patel with Stephens. Your line is now open.

Rick Patel:

Good morning everyone. Nice quarter.

Mark Light:

Thank you, Rick.

Michele Santana:

Thanks, Rick.

Rick Patel:

It's been about a year since you closed the Zale deal. Can you take a step back and reflect on how the integration played out so far? Perhaps what's surprised you to the upside and worked out better than you initially expected? On the flip side, what's been more challenging than you maybe initially planned for?

Mark Light:

Sure, I would say—I won't say it's surprises. What pleasantly pleases us is the way the Zale team members are engaging with not only our team but also collaborating with us and really embracing our strategies. The Zale team members, both in the stores and in their home office, really are embracing the Signet culture and the Signet values and the Signet strategies very well. I've been through a lot of acquisitions and one this big for the team members to engage and embrace our strategy so well is something we're so very pleased about at this pace.

We've shared this before and it's something we expected that with Zale's having some of the financial problems they had over the year that they didn't invest in their technology in the business and we expected there to be a lack of investment and we expected them to be behind the Sterling divisions in technology. When you get involved in a business and you really, really understand the business, we were surprised at how far behind they were in investment technology and how much we have to get involved and invest more through technology. That being said, we have plans for it. We have a great new Chief Information Officer named Dan Shull who we have a roadmap of the technology strategy in place but the technology was something that was a little worse than we expected it to be.

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Rick Patel:

Can you talk about pricing? Do you feel comfortable with where you are with the adjustments that you've made this yea, or should we expect some more refinements as we go through the year? As a follow-up, can you talk about the market prices for diamonds right now and how you expect they will impact input costs in the future quarters?

Mark Light:

As far as pricing, and Michele you can talk about it in more detail, there was no major price increases. There were some subtle pricing increases done in all of our divisions, it wasn't major, and in the marketplace, it's a challenging retail marketplace out there so I wouldn't plan on more increased pricing right now. Right now we want to capture a profitable market share but I wouldn't plan on more price increases. What was the second?

Michele Santana:

In terms of diamond pricing, Rick, what we said at the onset of the year and what we're seeing is really kind of a low to mid inflationary increase in the diamonds. Again, it always depends on cut, quality, size, et cetera. But low to mid is kind of where our head is at and what we're seeing on the diamond inflation side, and then earlier we talked about on the gold front that we are continuing to see the lower commodity cost. So that's how you should be thinking about it.

Rick Patel:

Thanks. Good luck for the rest of the year.

Michel Santana:

Thanks much.

Mark Light:

Thanks, Rick. Okay. We'll take one more question, Operator.

Operator:

Certainly. Your final question is from Bill Armstrong with C.L. King & Associates. Your line is open.

Bill Armstrong:

Good morning, Mark and Michele. Just one more on Jared. So it sounds like your overall transaction count was down. Were there specific product categories or areas that were weak and that you think offer some opportunity as we move through the back half of the year?

Mark Light:

Of course there's some categories that are weak, and the ones that are strong I shared with you earlier. I don't want to get into the product categories because our job as retail merchants is to constantly refine and enhance our business, and that's what I keep on sharing with you, Bill, is that our merchants right now are diligently looking at what's doing well, what's not. They're testing other opportunities and in gift giving programs we continue to enhance our traffic. It's important to understand that the average sale going up is definitely part of this Best in Bridal strategy and so we expect the average sale to go up. We

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want those units. We want to continue to increase transaction, of course, and we have got programs in place, but as a whole, the Jared market and the Jared business is different than the mall business. It's just something we believe, firmly, that we're capturing proper market share because a lot of our competitors outside the mall are having challenges in the retail jewelry marketplace. So we believe Jared's is capturing comparable market share, and then for the fourth quarter we'll have a lot of new programs in place to continue to do so.

Bill Armstrong:

Are you concerned with any possible slowdown in spending by maybe the higher end consumer on jewelry or other fashion categories or discretionary categories?

Mark Light:

No, we're not concerned. Actually, we have done a lot of research and a lot of surveys and the most important thing that we know is that our products, jewelry, is definitely in favor with the customers. We're in favor with—and it hasn't changed. So customers still very much appreciate and like to use jewelry to express their emotions, so we're not concerned.

If I have to say I'm concerned with anything is, other than us, we would like for more of our industry to advertise more. We need our industry. We are the only big national advertiser out there and to compete with the other products for that discretionary income, we need our industry to advertise more. We are going to, but our product is in favor and customers definitely like to express emotion through our products. So no, we are not concerned about that.

Bill Armstrong:

Great. Thank you very much.

Mark Light:

Thank you.

Michele Santana:

Thanks.

Operator:

As there are no further questions at this time, I'll turn the call back over to Mr. Light.

Mark Light:

Thank you. Thank you for taking part in this call. Our next scheduled call is on August 27th when we will review our second quarter results. Also, on June 24th, we'll host a conference in New York for the investment community. We'll have several insightful presentations, including content on our customer segmentation efforts and how we plan to differentiate our store brands to maximize our share of the mid-market of the jewelry industry. Thank you all again and good-bye.

Operator:

Thank you, ladies and gentlemen. This concludes today's call and you may now disconnect.

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