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PNDORA.CO - Q2 2016 Pandora A/S Earnings Call

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PRESENTATION

Operator

Good day ladies and gentlemen, and welcome to the second-quarter report 2016 conference call. Today's conference is being recorded. At this time, I would like to turn the conference over to Mr. Magnus Jensen, Head of Investor Relations. Please go ahead, sir.

Magnus Jensen - *Pandora A/S - VP, Head of IR*

Good day and welcome to PANDORA's conference call in connection with our Q2 2016 results, which we announced earlier today. My name is Magnus Jensen from PANDORA's Investor Relations and with me today are PANDORA's CEO, Anders Colding Friis; and CFO Peter Vekslund.

In accordance with the agenda on slide 2, Anders will present some of the highlights for Q2 before Peter will talk you through the numbers in more detail. Finally, Anders will conclude the presentation and following we'll be happy to take any questions you may have. Before handing over to Anders, I kindly ask you to pay attention to the disclaimer on page 3. Anders, please.

Anders Colding Friis - *Pandora A/S - President and CEO*

Thank you Magnus, and good morning everybody.

Please turn to slide number 4. Total revenue for the quarter increased 20% or 25% in local currency to DKK4.3 billion driven by double-digit growth in local currency in all of our three regions. All the individual product categories also increased with double-digit growth supported by continued relevant product offering, including the two product collections launched in second quarter of 2016, the Mother's Day and the High Summer.

Revenue from our concept stores including the eSTORE increased 39% compared to the second quarter of last year and during the quarter we opened 68 new concept stores and closed roughly 300 multibranded. The eSTORE which is planned to be opened in China and Canada in the second half of 2016 generated around 4% of Group revenue for the quarter and that compares to around 2.5% in second quarter of 2015.

Like-for-like sales growth for the Group was 7%. EMEA and Asia-Pacific continued a very positive trend, whereas Americas' like for like for the quarter was minus 1%. In general, Americas was impacted by a difficult retail environment, and some markets were in negative territory for the quarter. However, like for like in the US was positive at 2%.

EBITDA for the quarter increased to DKK1.6 billion and corresponded to an EBITDA margin of 37.2% compared to 36.4% in second quarter last year. The improvement was primarily driven by a higher gross margin, partially offset by the ongoing expansion in East Asia. Free cash flow was DKK576 million compared to minus DKK268 million in second quarter last year which was negatively impacted by a one-off of DKK642 million related to a settlement with the Danish tax authorities. Finally, at the end of second quarter 2016, we bought back shares for around DKK2 billion out of the total share buyback program of up to DKK4 billion for 2016.

Now please turn to slide number 5. Before turning to our regional revenue development, I would like to share a few words specifically on our results in the US. The development in the US was generally positive with revenue increase of 11% in local currency. The increase was driven by 2% like-for-like sales growth supported by flat to positive growth in all major regions. The northeast region was the strongest region at 4% growth driven by better conversion and a higher basket size.

The west region still suffers a bit from declining traffic in Las Vegas. As we experienced flat to declining footfall outside our stores in both High Street and in malls, overall we are pleased with the development in the US. One of the main drivers of the like-for-like growth was the increased focus on rings and earrings with the two categories increasing significantly compared to last year. The expanded category focus can have an impact on established categories, especially in the developed market like the US, and combined with a very strong quarter for the Disney Collection second quarter last year including the launch into shop-in-shops and multibranded stores in April, the revenue from charms in local currency was flat for the quarter. Excluding revenue from Disney charms, growth in the US would have been significantly higher.

Additionally our eSTORE in the US which have now been operating for more than a year contributed significantly to the growth driven by more than a 100% traffic increase since last year. So far we are very satisfied with the progress. In terms of the store network, we've added 36 new concept stores in the second quarter last year to a total of 335 stores in the US, while we closed around 400 multibranded stores as part of the cleanup.

Furthermore, during the first half, Jared, as planned, upgraded almost 100 of their stores to shop-in-shop. Status end of last week was that they had upgraded around 165 stores.

Please turn to slide number 6. Americas reported DKK1.7 billion in revenue, an increase of 5% or 10% in local currency compared to second quarter 2015. Like-for-like sales growth for the quarter was as mentioned minus 1%, impacted by negative like-for-like sales development in Brazil, Canada, and in the Caribbean Islands.

The overall growth in the region was driven primarily by the US, which generated revenue of DKK1.3 billion corresponding to 8% growth in Danish kroner. Revenue in Canada increased 3% in local currency, but decreased 5% in Danish kroner compared to second quarter 2015. While like for like was negative in Canada, impacted by a slower traffic in our stores, we've added seven new stores in the last 12 months. Revenue in EMEA was DKK1.9 billion, an increase -- and increased 28% in reported revenue or 32% in local currency.

EMEA concept stores like-for-like growth was 10%, or excluding the third-party distributors which include Russia, the EMEA like-for-like development would have been around 20%. Revenue in the UK which represent 25% of revenue for the region decreased 7% or 17% in local currency. Growth in the UK was primarily driven by strong performance in the existing store network, as well as the addition of net 36 concept stores. Like for like was double-digit driven by continued strong in-store execution.

We saw no immediate impact from the Brexit for the quarter, besides from the currency impact. Based on the current outlook for the UK following Brexit, we have no plans of changing our business approach, but we are prepared for a few bumps due to the current uncertainty regarding Britain's involvement with the EU.

Italy and France continued to perform very well, and revenue in the two countries increased with 40% and 70% respectively compared to second quarter 2015. Growth was driven by high double-digit like-for-like growth and the opening of 14 and 16 concept stores respectively in the last 12 month. Italy generated 25% of EMEA revenue, while revenue from France corresponded to around 15%.

Revenue in Germany increased around 70% for the quarter, generating around 10% of EMEA revenue. Second quarter last year was negatively impacted by a one-off provision of DKK53 million. Excluding this, growth in Germany would have been 17%. This was driven by low double-digit like for like, as well as the addition of net 33 new concept stores in the last 12 month. In the same period around 300 multibranded stores has been closed.

Finally, revenue in Asia-Pacific increased with 43%, or 51% in local currency to a total of DKK792 million. The quarter was again positively impacted by the conversion effect from the acquisition in Singapore and Macau from January of this year, and China since July last year. Excluding the one-off effect from this conversion, the growth was 24%.

Australia revenue increased around 30% compared to second quarter last year, driven primarily by high double-digit like-for-like growth, which continues to be supported by very high brand awareness and perception, as well as strong in-store execution. Furthermore, tourists, particularly from China are driving part of the growth in Australia. We observed an increasing share of tourists entering our stores, in a few store more than 50%, however the total effect on our business, difficult to quantify.

Revenue in Australia represented around 40% of the revenue from Asia-Pacific. Total sales out in Hong Kong was up with around 10% in local currency and generated around 15% of the revenue for the region. However, like for like in Hong Kong was negative primarily due to the high number of new store opened in the last 12 months, as well as the general decline in traffic due to the economic environment in the area.

Revenue in China increased significantly compared to last year and represented around 25% of revenue in Asia-Pacific for the quarter compared to around 8% in the second quarter of 2015. The increase was primarily driven by high double-digit like-for-like growth as well as the conversion of distributor revenue to retail revenue, which had an impact of around DKK65 million for the quarter.

Additionally, we opened nine new PANDORA-owned concept stores in China during the quarter to a total of 37 stores in the last 12 months. Year-to-date we've added 14 new concept stores and we are seeing a very positive progress in our plan. Therefore we now expect to open around 40 new concept stores in China in 2016, as well as in 2017 and 2018. This compares to previously communicated 30 stores in 2016 and 25 for 2017 and 2018.

In terms of pricing, we've done very limited changes to our prices in our different markets over the last four years. As a consequence, we are now in a situation where prices on a number of products, when we look across the different geographies, are out of sync. To align our pricing structure in the three regions, we've decided to do a number of price changes, which you will see in our stores starting from third quarter, and then phased in over the next 9 to 12 months.

The goal is not to have same prices in all market, but rather that the ranking of our products price-wise is similar across all market. You should not expect this to have any meaningful impact on margins as it includes both price increases as well as decreases, but rather, which is the goal, that we will have a more clear and uniform pricing structure across the Group.

Now please turn to slide number 6. Following a strong first half of 2016, we are on track to meet our full-year guidance which we revised in connection with our first-quarter results. We continue to expect revenue to be more than DKK20 billion for 2016 and the EBITDA margin to be above 38%.

CapEx for the year is now expected to be around DKK1.2 billion where we previously expected it to be around DKK1 billion. The upgrade is due to faster progress than expected in a number of business project including IT-related investments Thailand and [other].

Finally, we upgrade the expectations to number of new concept stores which we now expect to be higher than 300. Also, we now anticipate that they would be split with 50% in EMEA, 25% in Asia-Pacific, and 25% in Americas. Earlier, they were expected to be distributed 60:20:20.

With this, I give the word to Peter, who will give you some more details on the numbers.

Peter Vekslund - *Pandora A/S - Executive VP & CFO*

Yes, thank you Anders. And please turn to slide 8. For the quarter, revenue from concept stores and shop-in-shops increased 33%. The branded stores contributed was 77% of revenue, up 7 percentage point compared to Q2 2015.

Revenue from PANDORA-owned stores increased by 65% and represent 34% of revenue compared to 25% a year ago. The increase was driven by a good performance in our stores as well as the eSTORE, which as Anders mentioned, now represents 4% of total revenue compared to around 2.5% in Q2 last year.

Furthermore, we added 168 O&O concept stores to the network. The third-party distributor revenue decreased by 24% compared to Q2 last year primarily due to PANDORA's takeover of distribution, China, Singapore, and Macau. Excluding the three countries, revenue from third-party distributors decreased 5% compared with Q2 2015. The underlying decline was primarily due to the continued challenging business environment in Russia.

Please turn to slide 9. In Q2, we added net 68 new concept stores to a total of 366 new concept stores in the last 12 months. This includes the addition of 14 PANDORA-owned concept stores in the quarter and 168 in the last 12 months. Of the 168 stores, 29 was acquired from the former distributor in China, and 15 were acquired from our distributor in Singapore and Macau.

Shop-in-shops increased with 161 new stores for the quarter of which 98 was related to Jared upgrade. Finally, we have closed more than 300 multibranded stores in the quarter, primarily in the US and Germany.

Please turn to slide 10. Revenue from charms increased 10% for the quarter and represented 62% of revenue. Growth in charms was impacted by single-digit negative growth in Americas, primarily due to the strong introduction of Disney last year which mainly consist of charms. Revenue from charms in EMEA and Asia-Pacific increased around 20% and 50% respectively. Bracelets increased with 34%, driven by Moments and ESSENCE which was up 63%.

Two collections was helped by successful promotions in all regions and the launch of a number of new bracelets in the first half of the year. Together the revenue from charms and bracelets correspond to 79% of revenue and their growth contributed with 59% of the total growth for the quarter.

Rings continued to do well with revenue of DKK544 million and a growth of 42% compared to the second quarter last year. Revenue from rings was 13% of total revenue, compared to 11% same quarter last year.

Revenue from other jewelry, which contains earrings and necklaces, increased with 67% for the quarter. As part of our effort to become a full jewelry brand, we started to focus on earrings at the beginning of the year. The change in approach has not been to add more earrings to the assortment, but rather to increase focus in staff training and marketing and make sure we have the right earrings. So far we are satisfied with the development for Q2. Revenue from earrings increased more than 80% compared to Q2 2015 corresponding to 4% of total revenue. Also, necklaces did well and increased revenue with almost 60%.

Now please turn to slide 11. Gross profit was DKK3,260 million, corresponding to a gross margin of 75.3% compared to 71.5% last year. The increase was mainly driven by tailwind from favorable raw material prices having a positive impact of roughly 1.5 percentage point and an increase in revenue from owned and operated stores, with a positive impact of 1.5 percentage point.

Production complexity had a negative impact of approximately 1 percentage point. Furthermore, as a positive one-off, we reclaimed duties regarding prior years which has benefited US with approximately 1 percentage point for the quarter.

Finally, regarding recent raw material price increases, we do not expect any additional impact on gross profit for the year because we already fully hedged for 2016. So still 1 to 2 percentage points compared to 2015. But for 2017, which is partially hedged, we expect the headwind in very rough numbers of around 1 percentage point and for 2018 and onwards a headwind of around 2 percentage points compared to 2015 if prices stay unchanged.

Sales and distribution expenses increased 35% to 20.7% of revenue compared to 18.4% one year ago. The increase in share of revenue was mainly driven by additional owned and operated stores, which had an impact of around 3 percentage points. Marketing expenses increased 27%, from 9.4% of revenue for the quarter compared to 8.9% in Q2 2015. The increase in marketing was primarily PR and media.

Administrative expenses for the quarter increased 32% to DKK473 million equal to 10.9% of revenue, or an increase of 1 percentage point compared to Q2 2015. The increase was mainly driven by ongoing high IT expenses, our new offices in Singapore and China, as well as a one-off cost related to the transition into a new IT service provider correspond 1% of revenue.

Net financials provided a net gain of DKK57 million in contrast to a loss of DKK69 million in Q2 2015. Both amounts were primarily related to FX movements.

Net profit increased to DKK1.2 billion compared to DKK910 million last year.

Please turn to slide 12. The Group EBITDA for the quarter was DKK1,609 million, up 23% compared to the same quarter last year, equal to a margin of 37.2%. Americas increased the EBITDA margin by 2 percentage point to 40.3%. The increase was primarily driven by the improved gross margin including the one-off related to reclaimed duties which contributed with approximately 2.5 percentage point for Americas. The increase was partially offset by channel mix including more revenue from owned and operated stores.

EBITDA margin in EMEA was up by 0.2 percentage point to 36.5% primarily driven by a higher gross margin supported by operating leverage in the region due to the higher revenue. Furthermore, Q2 2015 was negatively impacted by a sales return provision in Germany with an impact of approximately 3 percentage point.

As expected, the expansion in Asia impacted the EBITDA margin for Asia-Pacific which decreased from 44.9% to 32.3% in Q2 2015. The decrease was primarily due to the increase in cost related to the expansion in China and Japan, including the takeover of the distributor in Singapore and Macau where we are establishing our own organization.

Combined, it had a negative impact of around 13 percentage point for the quarter. This includes a one-off inventory effect of around 3 percentage point on the gross margin related to the acquisition of the distributors in Singapore and Macau.

Please turn to slide 13. The operating working capital at the end of the quarter corresponded to 15.8% of the proceeding 12-months revenue, an increase of 1.4 percentage point compared to the end of last quarter. Increase was primarily due to higher inventories due to a planned inventory build-up ahead of the autumn/winter collection launch. Q2 CapEx was DKK352 million compared to DKK239 million in the same quarter last year. The increase was primarily due to the opening of owned and operated stores, increasing investments in the production in Thailand, as well as IT infrastructure projects.

Free cash flow for the quarter was DKK576 million compared to minus DKK268 million last year. The increase was driven by higher profits as well as Q2 2015 being negatively impacted by DKK642 million related to the settlement for the Danish tax authorities. The end of Q2, the total interest-bearing debt of DKK4.2 billion, and a net cash position of DKK540 million. Our net interest-bearing debt-to-EBITDA at the end of the quarter was 0.5, which is in line with our overall capital structure policy.

And with this, I'll hand over to Anders, who will summarize the quarter.

Anders Colding Friis - *Pandora A/S - President and CEO*

Thank you Peter.

Please turn to slide number 14. So in summary for the second quarter, revenue increased 20%, or 25% in local currency. We continued the rollout of stores with an addition of 68 new concept stores during the quarter.

Gross margin was 75.3%. EBITDA margin 37.2%. We had a free cash flow of DKK576 million. Revenue and EBITDA guidance was maintained while CapEx increased to approximately DKK1.2 billion. And we now expect to open more than 300 concept stores in 2016. So all in all, a second quarter for PANDORA where all our employees across the world have done a remarkable job.

We'll now open for any questions to the quarter. Operator, please.

QUESTIONS AND ANSWERS

Operator

Thank you. (Operator Instructions) Chiara Battistini, J.P. Morgan.

Chiara Battistini - *J.P. Morgan - Analyst*

I have a few actually. First of all on the UK, as I saw on the slide, you are saying UK like for like in quarter 2 was up low double-digits, which I think it was in line with Q1. And the total growth was -- actually, for the UK, was up 17% (inaudible) from your release, and despite a lot of space openings. So can I -- can you walk us through this mismatch between the space growth plus the like for like being that strong? And then the sell-in number up 17% or is there a mismatch between sell-in and sell-out we should be thinking of, and therefore very healthy inventories in the trade there?

Then, on the full-year guidance, as you are increasing the number of openings for the year by your leaving the sales guidance unchanged, are you telling us anything on the implied like for like for the H2, or we shouldn't be reading too much into that? Then on the shop-in-shops in the Americas, can I ask as I see that the multibranded doors are going down because I guess you are restating the Jared stores, but then I don't understand why the shop-in-shops were also down in Americas. So is there any one-off there that we should be thinking of in Q2 please?

Anders Colding Friis - *Pandora A/S - President and CEO*

I'll take the first question and then Peter will take the two next questions.

In the UK, yes, correct, like for like grew up double-digit. What you have to be very much aware of is that there's no direct link between us selling-in and the sell-out. What we have a focus on is very much the sales out of the stores, and if we just make sure that we have good like-for-like numbers, we also know that the sales-in will come. So there will, from quarter to quarter, be a bit of a mismatch, and I also think that was what you expected. So that is correct.

And then Peter.

Peter Vekslund - *Pandora A/S - Executive VP & CFO*

On the additional 25 stores that we are adding, that -- most of those will be opened late in the year and therefore the impact on our full-year revenue will be limited this year.

On the shop-in-shops, you're right on the conversion into -- on the Jared stores, but also please bear in mind that last year we introduced Disney into the multibranded channels, including shop-in-shops in the US, so we're up against a high number from last year.

Chiara Battistini - *J.P. Morgan - Analyst*

Perfect. Thank you very much. And if I just may add another one on the pricing comments you've made were very interesting. Can you give us some color on the kind of pricing architecture you are trying to achieve, so saying 100 in Europe, what would be the premium in the other markets please?

Anders Colding Friis - *Pandora A/S - President and CEO*

Maybe just a general note on what we are doing on pricing. What we've done is we've actually conducted a very big consumer study where we've looked at our pricing architecture across the markets. Historically, we've done the pricing in the markets, but what we can see is that actually across all markets the consumers have the same perception of the products, so that's the reason why we want to, you can say, clean it up.

If we look at our indexes, we normally have an index around 100 in Europe, we have a little bit less than that in the US, say, 90. And then when we go to Asia, we have a 120 and a little bit higher than that in China. So those are the general rules for it. And then because of currency movements, it'd be a little bit lower in Australia.

Chiara Battistini - *J.P. Morgan - Analyst*

Okay. Thank you.

Anders Colding Friis - *Pandora A/S - President and CEO*

You're welcome.

Operator

Kristian Godiksen, SEB.

Kristian Godiksen - *SEB - Analyst*

A couple of questions from me as well. Maybe if you could comment a bit on the discrepancy of the organic growth which is -- yes, basically you say is around 8.3%, if I take the one-third of the 25% growth in local currency, and then this 9% in sales-out like for like if you adjust for the third-party markets, I guess my question is should we continue to expect that the organic growth will be lower than the sales-out like-for-like growth as -- and basically what I'm saying is that will lower growth from non-concept store more than offset the stronger growth in the eSTORE which is with the latter not included in the sales-out like-for-like growth? So that was the first question.

And then secondly, maybe if you could comment a bit more and give some elaborations on what is it that is giving the negative like-for-like growth ex -- in Americas, ex the US, so both, a couple of questions on -- or comments on the Caribbean, Brazil, and also in Canada.

And then maybe just thirdly, if you could confirm a bit regarding all the one-offs that you see in the quarter, I (inaudible) in the call, was there any impact from the gross margin from the acquisition of the Singapore and Macau? And also maybe if you could comment a bit more on the one-offs regarding should we expect to continue to see some one-off regarding Jared sell in IT transition, is that also in Q2 alone and maybe also on the complexity what should we expect for the remainder of the year?

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Anders Colding Friis - *Pandora A/S - President and CEO*

Thank you Kris. And that was a lot of questions. I'll take your second question if I got it right, and then Peter will elaborate on the second. I'll talk a little bit about the like for likes in Americas.

If we look at Brazil, I think that everybody understands that Brazil is in a special state. We have in local currency in the market quite a growth of 22%, but at the same time we can see that our like-for-like numbers are negative. But I think Brazil is a little bit self-explanatory.

If we look at the Caribbean, you have to understand that Puerto Rico which is a big market for us is in a bit of a special state actually domestically, and that has put a limit to the consumers spending. At the same time, we see a bit less traffic in the Caribbean in general based on tourists.

And then the last market where we can see some negative development is Canada where we have, I would say, very low negative like-for-like numbers, nearly as low as you can get them. And I mean, Canada, I think that clearly we can see some of the oil producing states which are having a little bit of a softness, but at the same time, we also have to say that there is options for us to strengthen our in-store and retail execution and that is of course also part of it. So that gave you a bit of flavor on that and then Peter, he will elaborate on the other questions.

Peter Vekslund - *Pandora A/S - Executive VP & CFO*

Yes, first on your calculation taking our one-third of the growth to the like for like and just starting, it is one-third and it's rough because it's not exact math on that guidance, but the main component of the discrepancy you're looking for that is related to distributors, that is Russia, it's Spain and it's Taiwan, which is a drag on the number.

On the one-offs, starting on revenue, we have an effect from a conversion of DKK110 million related to China and also Singapore and Macau. We have IT where we had changed the supply of IT services impacting margins with 1 percentage point. And inventory buyback in Singapore and Macau impacts the margin was 0.5 percentage point. That was the overall.

Then on the complexity, we did see an impact in Q2 and our overall guidance for the year, that complexity will have an impact of probably in the low end of the range, 1 to 2 percentage point impact for the year. Finally -- yes, I think that was all your questions.

Kristian Godiksen - *SEB - Analyst*

Also maybe just regarding the -- just confirm that the IT transition also Jared so then it was only a Q2 specific, I know Jared sell-in was also in Q1, so maybe you could confirm that we should expect something in Q3 for either of those two components?

Peter Vekslund - *Pandora A/S - Executive VP & CFO*

I think on IT, you will never be done implementing IT systems and doing transitions, but what we can see now is that should be the one-off for the quarter and we have not planned for anything for the rest of the year.

Anders Colding Friis - *Pandora A/S - President and CEO*

And the percent that we are mentioning is a specific project which was in second quarter, so that will not come back.

Peter Vekslund - *Pandora A/S - Executive VP & CFO*

I mean it's mentioned in the media we're transitioning to NNIT.

Kristian Godiksen - *SEB - Analyst*

Yes, yes, it's just a question. I mean, that would --

Peter Vekslund - *Pandora A/S - Executive VP & CFO*

Kristian, apologies for that. That was the duty drawback in Americas. That is also a one-off 1 percentage point on the margins.

Kristian Godiksen - *SEB - Analyst*

Okay. And then maybe on the Jared sell-in, that's been going on now both for Q1 and Q2. Is that something we should expect will continue as they -- you said you've opened about 100 stores out of the 200 stores. So should -- I guess we should expect that to continue in -- when Jared upgrades the stores as we go along the year?

Peter Vekslund - *Pandora A/S - Executive VP & CFO*

There could be a bit more sell-in in Q3, and hopefully a lot of replenishment of the inventories as they start selling.

Anders Colding Friis - *Pandora A/S - President and CEO*

And we've actually upgraded by now 165 stores.

Kristian Godiksen - *SEB - Analyst*

Okay. And then maybe just coming back to my initial first question regarding the difference between the sales-in and sales-out, so basically what you're saying is that when you look at it, it's the third-party market which is the main reason of the two -- to say the sales-in like for like and the sales out like for like, so basically the eSTORE growing faster which is not included in the sales-out like for like is basically being offset by the lower growth in the third-party markets, but I guess also from other concept stores. Is that how we should think about it, so basically we should think about these two numbers being more or less the same going forward or --?

Peter Vekslund - *Pandora A/S - Executive VP & CFO*

I'm not making a direct link between those two, just saying in this quarter it's the distributors that is being a drag on the organic growth. And you're right on the other components you are mentioning like eSTORE which is included in organic growth, but not in the like-for-like growth.

Kristian Godiksen - *SEB - Analyst*

Okay. So you can't comment on new -- because eSTORE would all else equal, we know that for sure that is basically [doppling, right], you just said that yourself in the guidance traffic. So that should all else equal drag up your organic growth or -- and then on the other hand, the other component is taking it down, so -- but you can't give any flavor on what to expect, in which kind of magnitude the two components would affect going forward?

Peter Vekslund - *Pandora A/S - Executive VP & CFO*

So you're right on that one that just on the eSTORE that is traffic to the store that has [doppled]. It's not the revenue or --

Anders Colding Friis - *Pandora A/S - President and CEO*

We gave the revenue. It moved from 2.5% of our revenue to 4%.

Peter Vekslund - *Pandora A/S - Executive VP & CFO*

Yes.

Anders Colding Friis - *Pandora A/S - President and CEO*

And then if you look at EMEA specifically and look at the distributors, actually if you take out the distributors in EMEA, we would have had a like-for-like development of 20% and that is of course very much Russia which is on that.

Kristian Godiksen - *SEB - Analyst*

Yes. What I was referring to was just that in the eSTORE, it goes as you say from 2.5% to 4%, but in the same time also you have grown the business by let's say 30%. So no doubt that the eSTORE is growing faster than the rest of the business. So that is all else equal benefiting your organic growth number, but it's still lower than your sales-out like for like when adjusting for the third-party market, so it was just the moving parts there, what should expect -- what to expect going forward?

Anders Colding Friis - *Pandora A/S - President and CEO*

I think we've given you what we can.

Kristian Godiksen - *SEB - Analyst*

Okay. Okay, thanks a lot.

Anders Colding Friis - *Pandora A/S - President and CEO*

Welcome.

Operator

Anne-Laure Bismuth, HSBC.

Anne-Laure Bismuth - *HSBC - Analyst*

I just wanted to know is it possible to have the percentage of online sales in your Group sales and when -- where you plan to rollout the eSTORE next? My second question is -- sorry for that, but can you come back on the impact on gross margin that you've mentioned earlier about the raw material prices in 2017 and 2018? And finally what should we expect in terms of admin as percentage of sales-in year of 2016?

Anders Colding Friis - *Pandora A/S - President and CEO*

I'm sorry, but the first and the last question kind of didn't come through very well. The last question was --

Anne-Laure Bismuth - *HSBC - Analyst*

No, I was just asking about the percentage of online sales in the Group sales mix and where do you plan to roll out eSTORE next? My second question is about the raw material impact on gross margin in full year 2017 and 2018. And finally about the admin as percentage of sales for full-year 2016 that we should expect?

Anders Colding Friis - *Pandora A/S - President and CEO*

Okay. Well, I think that if we look at the eSTORE first, and then Peter can take -- will take the other question. The eSTORE as we've said was 2.5% of our revenue last year, and was 4% this year. So we've seen a very nice growth in that and that's why we've also included this quarter's announcement a number for that so that you can see how that is moving. And if we look at the expansion of that, we're going to open two new eSTOREs this year, one in Canada and one in China.

Peter Vekslund - *Pandora A/S - Executive VP & CFO*

On the impact of raw materials for 2016, we still see an impact, positive impact, 1 to 2 percentage point partially being offset by production complexity this year. Going to 2017, we see an impact of around -- in rough numbers, around 1 percentage point on the market and an additional 1% in 2018. So 17% minus 1%, 18% minus 2% compared to this year, in very rough numbers based on the current prices. On the admin percentage of sales, say for modeling purposes, still 9% to 10% for the full year.

Anne-Laure Bismuth - *HSBC - Analyst*

Thank you.

Anders Colding Friis - *Pandora A/S - President and CEO*

You're welcome.

Operator

Lars Topholm, Carnegie.

Lars Topholm - *Carnegie - Analyst*

Yes, a couple of questions on my side. On the Jared upgrades, from the data you have available, are you seeing any cannibalization from the existing US concept store base from Jared adding more square meters for PANDORA? And then, Anders, you mentioned you are making these price adjustments and my understanding is some of the growth you are experiencing in Australia is to Asian tourists and the price differences between countries in Asia. Should we expect that this exercise will shift demand from Australia to, for example, China or other parts of Asia?

And then a third question if I may. You mentioned Disney as a tough comp for Q2 this year. Can you elaborate more on how much Disney contributed to Q2 last year?

Anders Colding Friis - *Pandora A/S - President and CEO*

Let's start with the Jared upgrades, and clearly we are very happy with the [operating] -- I think that seeing the stores I actually had the pleasure of -- in July to see a few of the operation, it's looking very good. And clearly it's part of our development of our retail footprint, as a branded footprint. We cannot see and do not see at this time or expect for that sake to see a cannibalization on an overall basis between the different channels.

What we do is that we want to have more branded space, so we have upgraded Jared, but as you know and as we've said, we've also closed other unbranded and multibranded stores. So it's not like we see a lot of cannibalization on that. The price adjustments, and just to make this very precise, this is not a question of us changing our all indexes in the individual markets. They are going to stay as they are.

What we are doing is we are moving the individual prices around and you can say that where we've been -- actually a product in one market could be priced at the double price in another market just because the individual market thought that was the right thing to do. And that is not corresponding to the consumer's expectations on pricing. So actually what we are doing is we are aligning our prices, not sure they are going to be the same, but the prices are going to be in the same structure. So the ring would be -- if we have one price in one market which is an index, 100 markets the price would be roughly index 80 and in the index 80 market or 120 in an index, 120 market if that too makes it very clear what we're doing. But we're not moving between the different markets.

Lars Topholm - *Carnegie - Analyst*

So in other words, if your products are priced higher today in China than in Australia, that will also apply after this exercise?

Anders Colding Friis - *Pandora A/S - President and CEO*

Yes, we are not planning any changes to that.

Lars Topholm - *Carnegie - Analyst*

Excellent.

Anders Colding Friis - *Pandora A/S - President and CEO*

On Disney, first of all, Disney, that is a 10-year strategic partnership that we have entered into with Disney. In connection with introduction we had a large number of design variations being introduced last year and fewer this year. Also last year we expanded into the multibranded stores in the US. So overall we do see a significant negative growth in Disney this quarter compared to last year. But again we are in it for the long haul with Disney and do see a meaningful contribution to the US revenue on Disney.

Lars Topholm - *Carnegie - Analyst*

That I understand, but my question was different. It was what was the impact of this Disney sold into the shop-in-shops in Q2 last year because you mentioned it specifically as a swing factor for US, so just wonder if you can quantify it?

Anders Colding Friis - *Pandora A/S - President and CEO*

Yes, we mentioned it as a factor, but are not quantifying that in more details.

Lars Topholm - *Carnegie - Analyst*

Okay. Perfectly well. Thanks.

Anders Colding Friis - *Pandora A/S - President and CEO*

Welcome.

Operator

Michael Rasmussen, ABG.

Michael Rasmussen - *ABG - Analyst*

First of all, guys, in this set of numbers, can you tell us please what came as the most positive surprise and what was the most negative surprise versus your original expectations? And my second question, coming back to the eSTORE, do you plan to include this development in your like-for-like numbers as stores have been open for 12 months and also if you would give us the Q3 and Q4 share of revenues from last year?

And finally can you just for modeling purposes, marketing costs, are you still looking for close to 9% full-year and are we still looking at about 20% sales and distribution costs?

Anders Colding Friis - *Pandora A/S - President and CEO*

Yes. Positive and negative surprises, actually I think that when we look at the quarter it was actually as we expected. If you look at something we are very happy with, we can say that China has really moved very well and forward, so that's on a very good one.

Then of course you can always say that you are a bit surprised at what is happening in Brazil, but that is you can say expected with the development there. Any surprise where we would like it little better maybe is Canada where we can see that we can do better in some of the stores. So I would say that's probably the flavor on that, but overall 25% organic growth in the quarter in local currency is something we feel very good about.

eSTORE like for likes, we do not at this time have any view that we're going to include it in our like-for-like numbers. And what we wanted to give you this quarter was a flavor of how we're doing, so that was why we gave you those numbers this quarter, and so that you know where we have [the results]. But we are considering what to do in the future as well. And I'm not saying that we are never going to -- into it, but at this time we haven't made any decision on it. And --

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Peter Vekslund - *Pandora A/S - Executive VP & CFO*

Maybe just a short comment from my side on that. We did change our external disclosure from Q1 of this year. Of course we are evaluating that and that's also why we gave you the US like-for-like number this quarter as well as the eSTORE share of revenue. On the --

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Michael Rasmussen - *ABG - Analyst*

Peter, maybe you could -- for modeling, could share the Q3 and Q4, the share like you did 2.5% last year in Q2?

Peter Vekslund - *Pandora A/S - Executive VP & CFO*

We're not ready to share those at this call. But started out at 2.5% and 4%, so if you take in that range, you're not probably totally off.

Michael Rasmussen - *ABG - Analyst*

Okay. I would just assume that Q4 was somewhat higher.

Peter Vekslund - *Pandora A/S - Executive VP & CFO*

Yes.

Michael Rasmussen - *ABG - Analyst*

Okay. And on the costs --?

Peter Vekslund - *Pandora A/S - Executive VP & CFO*

Cost structures, no changes to that, so sales and distribution still around or slightly above the 20%, marketing 9% and admin in the 9% to 10% range.

Michael Rasmussen - *ABG - Analyst*

Thank you.

Magnus Jensen - *Pandora A/S - VP, Head of IR*

You're welcome.

Operator

Frans Hoyer, Jyske Bank.

Frans Hoyer - *Jyske Bank - Analyst*

Yes, I wonder if you could elaborate a little bit on the slow-down in sales growth in Europe from -- I think the number was 47% in Q1 and it's 28% roughly speaking in Q2. I understand the Russia part of that, but maybe there's more to it. Also would you or are you seeing any signs that the sensitivity of PANDORA sales to general economic trends that -- or the resilience to slower economic trends, are there any changes in how that is behaving in your view?

Anders Colding Friis - *Pandora A/S - President and CEO*

Well, I'll do the last one and then Peter can do the first one. The easy answer is, well, we still see a strong development also in markets where we -- even though we see general trends which is not supporting the growth that we have right now. Having said that, if you look at some of the markets which has been impacted, take Russia, take Brazil, of course we are also under influence of the development in the market.

Also in the US where we can see that more traffic is down, still 2% like for like in a market like that we find it is good, but it's not like we're totally resilient and I don't think we've ever been, but clearly as we become bigger in some of these markets, we will also see a little bit more impact.

Peter Vekslund - *Pandora A/S - Executive VP & CFO*

And the growth in Europe, we discussed the UK earlier at the call, so UK growth going from 30% down to 17%. Also Italy 70% growth in Q1 slowing down as the absolute figures gets higher to around 40%. And then Spain where we have a distributor, also some impact from that.

Frans Hoyer - *Jyske Bank - Analyst*

So I understand those are the numbers, but what is it you are seeing, Italy slowing from 70% to 40%, what is actually happening in your view? Is it just an inventory projection or is it something more structural?

Anders Colding Friis - *Pandora A/S - President and CEO*

I think that what is happening is as we build these markets and remember now Italy is 25% of EMEA which is as big as the UK --

Frans Hoyer - *Jyske Bank - Analyst*

Yes.

Anders Colding Friis - *Pandora A/S - President and CEO*

-- we are getting to a point where clearly the percentage growth is going to be smaller and it is what we expect that over time, clearly percentage-wise our growth is going to be smaller.

Frans Hoyer - *Jyske Bank - Analyst*

Okay. Thanks very much.

Anders Colding Friis - *Pandora A/S - President and CEO*

You're welcome.

Operator

Klaus Kehl, Nykredit Markets.

Klaus Kehl - *Nykredit Markets - Analyst*

Klaus Kehl from Nykredit Markets. Three questions if I may. First of all, I know that you have not given us any guidance about Q3, but could you just give us any indications for what you're seeing in UK after the Brexit vote? That would be my first question.

And secondly, Russia has been a drag on your numbers for quite a while, but I guess sooner or later revenues must simply, yes, start to decline. So can you give us any kind of flavor what it looks like for second half? And thirdly, you're seeing a very negative impact on your gross margin from the acquisitions that you made in Singapore, in Asia, but I guess you must sooner or later have worked your way through the inventories, but would it be fair to expect a marked improvement in second half of 2016? That would be my questions.

Anders Colding Friis - *Pandora A/S - President and CEO*

I think when we talk about guidance, we'll stick to our overall guidance for the year. I can say that the only thing we've seen, and that is also mentioned in our release, is that we've seen the currency impact in Britain so far. So that is what we can see and then we'll have to see -- do we expect to see some bumps on the road? Absolutely. And can consumer confidence be influenced by the negotiations and what is going to happen for the Brits to leave EU, absolutely.

And we will mention that as we see it, but as I said in Q2, the only thing we've seen has been the currency effect on it. And you can say, Russia, the same, we feel very good. It's -- you have to say it's about actually slightly below 1% of our total revenues in the Group. So it's a small part of it. And we will see how it works out. I think that in general in Russia we do a good job in a difficult market, and clearly we are influenced by what is happening, and that gives us some negative like-for-like numbers.

Peter Vekslund - *Pandora A/S - Executive VP & CFO*

And on Asia, the impact of margins, there's, say, two factors influencing the markets in Asia or the margins. One is the inventory buyback which impacted the quarter by 3 percentage point, and we are now through that inventory. So no further impact from that. We are, however, still building our organization in Singapore, in China, in Japan, and that does have an impact on our margins. That said, we believe we will get -- start getting a bit of leverage also in Asia as revenue picks up.

Klaus Kehl - *Nykredit Markets - Analyst*

Okay. And then just to be perfectly clear about UK, so what you're saying is that here for July and August, it's business as usual. Obviously the -- yes, the currency has moved, but your underlying development is fine, is that how I should interpret it?

Anders Colding Friis - *Pandora A/S - President and CEO*

I think -- we can comment on second quarter and also honestly if we look at the beginning of this quarter, we are still good. We haven't seen any major impact. So -- but I think that it is worth expecting that there will be some turbulence in UK going forward.

Klaus Kehl - *Nykredit Markets - Analyst*

Okay. Thank you very much.

Anders Colding Friis - *Pandora A/S - President and CEO*

You're welcome.

Operator

Piral Dadhania, RBC.

Piral Dadhania - *RBC - Analyst*

Most of them have been answered, but I was just curious as to your 2017-2018 gross margin guidance. You're looking for down 1 percentage point due to raw material headwinds in 2017, I think too in 2018. How much of that gross margin guidance factors in changing your pricing architecture starting in the second half this year? So I guess where I'm going really is how much should we expect prices to increase to help offset your raw material headwinds that you're facing in 2017-2018?

Anders Colding Friis - *Pandora A/S - President and CEO*

The very, very short and easy answer is none. The pricing architecture, and the changes we're doing in that, is not expected to have any material impact on our average prices in PANDORA. So that's not building in. What we have to be aware of is that we see an increase in prices of gold and silver, but we are also at an absolute -- we come from an absolutely low, so with the price increases that we see in the market on the spot market right now, we would be back in the beginning of 2015. So it's not like we've seen a totally ramp-up of commodity prices. So we are not planning any price increases to come for that. We need to be relevant in the markets where we operate and that is the way that we look at it.

Piral Dadhania - *RBC - Analyst*

Okay, brilliant. Thank you.

Anders Colding Friis - *Pandora A/S - President and CEO*

You're welcome.

Operator

Elena Mariani, Morgan Stanley.

Elena Mariani - *Morgan Stanley - Analyst*

A few follow-up questions from me please. The first on is in the US. So this quarter, you said that like for like specifically in the US was approximately 2%. I remember that in the first quarter it was positive as well. But have you experienced a slow-down specifically for the US in the second quarter versus Q1? And then do you think -- I know you've asked -- you've been asked this question before, but do you think that somehow your eSTORE performance is cannibalizing a little bit the brick-and-mortar performance there?

The second question is, again, on the gross margin next year and the following year. I understand your guidance around the raw material prices and around the pricing architecture, but do you see this negative impact to be fully compensated by the rollout of your own and operated stores? And this leads me to the -- my third question. Can you give us a rough idea of the split between own and operated stores and third parties within your overall concept stores openings guidance, and how this would affect gross margin, but also sales and distribution expenses over the next year or so?

Anders Colding Friis - *Pandora A/S - President and CEO*

I'll try to do the first part and then Peter will do the second part, and hopefully we'll get all of it there. If we look at US like for like, the reason why we gave the number is also because we've understood that has been a very, very big interest in this. And I would say, if you look at it, it's not a big difference, so it's roughly the same as we saw in the first quarter.

eSTORE cannibalization is a big question and I think the best market to look at for that -- we haven't seen anything and we are not feeling it in the US, but the best market to look at is actually the UK where we've been active for the longest period of time, and there we can see as we have increased our sales in eSTORE, and we've previously said that it's more than 10% of our revenue, we have not seen an impact on the like-for-like numbers.

So in our general thinking, the two channels work hand-in-hand and well together. Can there potentially be a little bit of impact and cannibalization here and there? Yes, of course, and that is also logical. But basically we believe the two channels work well together. So the total will be bigger as we have both available for the consumer. And then Peter will --

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Peter Vekslund - *Pandora A/S - Executive VP & CFO*

Yes, the impact of commodity prices on the gross margin, we gave some insight into the impact on 2017 and 2018. It's not like we are starting giving specific guidance on those two years. But we wanted to remove some of the uncertainty around impact of commodity prices. Just the impact on gross margin from owned and operated, that is positive on the gross margin, but there will be an increased cost of operating the stores on the sales and distribution cost which offset the positive impact on gross margin.

Elena Mariani - *Morgan Stanley - Analyst*

Okay. Thank you. And can you give us a rough idea of the implied split between owned and operated and third parties where you'll still rollout please?

Anders Colding Friis - *Pandora A/S - President and CEO*

I don't think we give a [chin up], but what you should expect over time is that the revenue part from owned and operated is going to increase a bit, one-third and to a little bit in 2016, but expected to grow a bit.

Elena Mariani - *Morgan Stanley - Analyst*

Okay. Thank you.

Anders Colding Friis - *Pandora A/S - President and CEO*

You're welcome.

Operator

Chiara Battistini, J.P. Morgan.

Chiara Battistini - *J.P. Morgan - Analyst*

I just have a few follow-up questions if I may. First of all, on your comment on Disney, following up on last question, you said Disney was a very big drag for the quarter two as -- and Disney was negative year on year in quarter two because of the timing of the shipments from last year.

Does that mean that the drag actually fades as you go into H2, so we should expect lower drag basically in H2? Then in -- on the inventories, inventories were particularly elevated in the end of the quarter. Is it just a matter of timing of shipments ahead of the autumn/winter collections for Q3 or are you -- I mean, are you happy -- I guess the question is are you happy about your inventory levels everywhere in the trade?

And finally just a follow-up on your comment on Brexit; you are expecting some bumps on the road, is your full-year guidance then also reflecting these expected bumps or not?

Anders Colding Friis - *Pandora A/S - President and CEO*

I'll start with the last one, and the answer is, yes, it is. When we -- and I'm not sure I fully got the Disney question here. Clearly what happened with last year and this quarter was that we opened for sales to a number of new stores and they increased their inventories on Disney. So -- and that was a first-half situation. So second half we will see less of that. So if that was the question the answer is yes.

Chiara Battistini - *J.P. Morgan - Analyst*

Yes. Perfect. Thank you.

Anders Colding Friis - *Pandora A/S - President and CEO*

(Multiple speakers) -- talk a little bit about --

Peter Vekslund - *Pandora A/S - Executive VP & CFO*

On the inventories, you are right that inventories are increasing. If you take inventories as a percentage of sales compared to same quarter last year, then they're actually at the same level 15.5% Q2 last year, 15.7% Q2 this year. So it's also -- or it's due to build-up for the autumn/winter as well as increased revenue.

Chiara Battistini - *J.P. Morgan - Analyst*

That's great. And just then just if I could understand correctly on the Brexit point and your guidance as you haven't seen bumps so if you don't -- if you continue not to see bumps, then your guidance is conservative for the year.

Anders Colding Friis - *Pandora A/S - President and CEO*

I think our guidance is our guidance. That's the way that is.

Chiara Battistini - *J.P. Morgan - Analyst*

Okay. Thank you.

Anders Colding Friis - *Pandora A/S - President and CEO*

You're welcome.

Operator

Kristian Godiksen, SEB.

Kristian Godiksen - *SEB - Analyst*

Just two short follow-ups from me. Maybe if you could elaborate a bit on the continued strong performance in the northeast region in the US outgrowing the rest of the US market, I guess should we expect -- or maybe you can confirm is there a difference in your performance in driving O&O stores' revenue compared to franchisees, concept store growth rates?

And if that is the case should we expect for you to maybe potentially take over more stores as you did in the northeast region with Hannoush? That was the first question.

And secondly, maybe just regarding now you are giving a bit more visibility on the gross margin expectations for 2017 and 2018, maybe if you could just confirm that should we expect anything other than raw material prices to affect your gross margin such as complexity, is that something that we should expect going forward or other items?

Anders Colding Friis - *Pandora A/S - President and CEO*

I'll do the first one, and yes, we had a strong performance in the northeast and we mentioned that because we actually feel quite proud about that. As you know the northeast was a region where we had some negative like-for-like development and some issues. We took over the Hannoush stores out there and it also supported very strongly the retail mindset that we want to have in the US organization.

So the learnings we have from the northeast region is clearly something that we are pushing into the other regions in the US. And in connection to that, yes, we will in our well-developed markets take a little bit more own and operated stores because we can see that it supports the retail mindset and our performance in the markets.

Peter Vekslund - *Pandora A/S - Executive VP & CFO*

On the gross margin and impact of commodity prices, we did give some extra flavor on 2017 and 2018 to remove the uncertainty around the impact of commodity prices. However, we are not for the time being ready to give more guidance regarding 2017 and 2018. We stick to current year guidance which we have confirmed in this quarter.

Kristian Godiksen - *SEB - Analyst*

Okay. Thank you. And maybe just a very short follow-up on the first one on -- so could you maybe give some thinking regarding how much of a share should we expect O&O stores or for the concept stores to make up in, yes, let's just say the medium term on the coming years?

Anders Colding Friis - *Pandora A/S - President and CEO*

I think that we've already touched upon that subject and what we said is expect around a third this year and expect that to grow a bit over the coming years.

Kristian Godiksen - *SEB - Analyst*

Okay. Okay, thanks a lot.

Anders Colding Friis - *Pandora A/S - President and CEO*

You're welcome.

Operator

[Ivan Briery, Podurance].

Ivan Briery - *Podurance - Analyst*

You mentioned that the FX had a 5% impact on sales. Could you give us the impact on EBITDA or EBIT please?

Peter Vekslund - *Pandora A/S - Executive VP & CFO*

On the impact of FX, for the full-year we expect a headwind of 3% and for the quarter, you're right, it was 5%. In terms of the margins for the quarter we didn't have any impact on the EBITDA margin.

Ivan Briery - *Podurance - Analyst*

Thank you.

Operator

We have no further questions queued.

Anders Colding Friis - *Pandora A/S - President and CEO*

Thank you very much for your questions and for participating in the conference. Have a great day.

Operator

Thank you. That will conclude today's conference call. Thank you for your participation, ladies and gentlemen. You may now disconnect.
