Dunelm
Interim Results FY24
Live Video Webcast

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Transcript

Nick Wilkinson: Good morning and welcome to the Dunelm Interims presentation covering the first half of our financial year to 30th December. My name is Nick Wilkinson, and Alison Brittain, Karen Witts and I are really delighted to welcome you to the offices of Peel Hunt in London. Thank you for joining us and giving us your time this morning. Whether you are here in person, or joining virtually, I hope you are well, and feel connected to the continuing story of Dunelm.

Those of you who came to our recent event for investors in November know that we are at heart a product company. A product company that's also busy innovating in the ways that we connect our products to an ever-growing number of customers. So, with images from our spring summer 24 collections, we'll use this presentation to bring to life how we are developing the business, and the results we are achieving. It's our normal running order. A short overview from me, then Karen will go through H1 results and guidance, and I'll be back to update on our plans, before we take your questions.

So with our Spring and Easter products demonstrating that everyone needs a bit of Dunelm in their life, and with a spring in our step let's get started.

In a complex environment we've continued to perform strongly. Consumers remain under pressure, we're in growth but our markets are not. And I'm pleased with the shape of our financial performance in the half. Our H1 profits are up by 4.8% on the prior year. In balance with our sales growth, up by a similar level, achieved through good discipline on gross margins, in particular, and costs. We have announced progression of our interim dividend, and a special dividend of 35 pence per share, maintaining our track record in terms of cash generation and distribution. Active customer growth and market share growth are also strong. Karen will explore these and our financials in more detail shortly. And a particular thank you to all my colleagues listening, and all of our supplier partners, for everything you do every day to grow and adapt, and to deliver for our customers and other stakeholders.

Retailing is always about today's sales, but it's important to achieve today's sales through actions which also deliver long term, sustainable, compounding growth. In the half we traded well. We feel we have struck the right balance so far this year, and the evidence is in our combination of volume and margin growth. With strong comparables in our prior year, and with hard-pressed consumers focused on really seeking out value, as well as some seasonal joy and fun, it was an environment which saw considerable volatility in our market from week to week. Growth in both volume and sales was driven by market share gains. We were extremely focused on offering customers outstanding value, and we did this by leveraging the breadth of our price architecture, from good, our opening price points, to our better and best tiers, and a few thousand carefully selected reductions to our regular prices. In a market which was more promotional, we were disciplined, focused on a genuine Winter Sale, and our established rolling programme of special buy lines. We adapted to volatility in the market, achieving our sales growth with good grip on input costs and inventory. Indeed our cash gross profit increased by 8% year on year. And we've ended the half with the right stock, and good sell through of Christmas ranges. With a long term lens I am pleased that our sales were driven more by volume than price. Customer growth and frequency are effectively volume measures of our business, and here the breadth of our growth was excellent. We saw more customers shop with us in all regions of the country, in all age groups, and in all income groups up to one hundred thousand pounds per annum. That breadth is the result of investing, through the current economic cycle, in our offer, in our total retail system. We'll come onto our plans shortly, but first we'll take you through the half and I'll hand over to Karen.

Karen Witts: Thanks Nick, and good morning everyone. Thank you for making the time to spend with us today.

I'll start with a summary of our financial results. As Nick said, we are pleased to be reporting another strong half year performance. I'll go through the various elements in more detail, but at headline level, we delivered £872.5m sales in the first half of FY24 and that's 4.5% higher than the same period last year. As Nick has described, our growth was volume driven as we offered our customers relevance, choice and outstanding value at every price point. Our gross margin was also strong at 52.7%, 160bps higher than the previous year. Whilst this expansion was primarily driven by reductions in freight rates, we also managed our input costs well, and were disciplined on pricing and promotion. We speak about operational grip and this has been important in a period of uncertain consumer demand. We have managed costs, with a focus both on managing inflationary pressures and on how we choose to invest in the business for the future. Profit before tax of £123m grew by 4.8%, slightly ahead of our sales growth, with EPS of 44.6p 2.6% down year on year, mainly reflecting last year's increase in the rate of corporation tax. Our cash generation was strong at £91m and we ended the half with £6m of net cash on the balance sheet. The Board has declared an interim ordinary dividend of 16p, up 6.7% year on year, and we are also announcing a special dividend of 35p per share.

This next slide explains how we grew sales well in a complex environment. We saw sales progression both in stores and online, with digital sales making up 36% of our total; two percentage points higher than the same period last year. As I said in my introduction, and consistent with our guidance in September, our sales growth was driven by volume, which we believe is important for long term sustainable and profitable growth. And we grew both market share and customer numbers. As we continue to develop product mastery and category strength, we saw a good performance in areas such as Cook and Dine, and Furniture. We know that our customers like plenty of choice, within a curated range, so we carefully expanded online sku availability. Nick will give colour on how our ongoing investment in digitalisation is improving the customer experience of our site and is further helping to drive sales.

We saw good growth in our active customer numbers, which increased by 4.2%. As Nick described in his introduction, our growth was broad based by category and by customer type. We saw growth in all regions, all age groups, and all income levels, except our highest income level group, which was flat. We were pleased to see strong growth in younger age groups and in London. Shopping frequency also continued to grow and was up by 1.1%. As you know, we use GlobalData reporting, over a last twelve month period to track our market share. This tells us that the combined market for homewares and furniture over 2023 was broadly flat, and with our growth of 5% over the same period, we gained 50 basis points of market share. We saw an increase in both the homewares and furniture markets. We are focused strategically on gaining share across the combined market, and increasingly we think of furniture as several categories, as we showed in our November Investor event and we've reminded you of that in the appendix to this presentation. So, we are going to move to a single disclosure for the combined market, which we will continue to update on twice a year, and we will show you our long-term progress over key categories as appropriate.

I said I'd return to the drivers of our gross margin. As I highlighted, the year-on-year growth of 160 basis points came primarily from a net benefit from freight costs. That is, lower freight rates, with a slight headwind from foreign exchange. As you may remember, the margin in the second half of our year is always lower than the first half, as it contains our two main sale events. The foreign exchange headwind in H2 will be a bit stronger than in the first half, and we are managing the current Red Sea issues, where the longer shipping routes are adding 2 -3 weeks to shipping times, and we are incurring surcharges because of this. Operationally, availability is still strong and new season stock is arriving in stores and online as we speak. We expect the overall profile of H1 versus H2 to be similar to prior years, and we are comfortable maintaining our full year guidance of 100 basis points of gross margin rate growth year on year.

Moving on, we work hard on the combination of tight operational grip and thoughtful investment. Year on year operating costs grew by £8m to support volume growth. We experienced a £10m inflationary headwind in H1, largely driven by wage costs. We partly offset this through efficiency savings from areas like marketing optimisation and tight management of external storage costs. In September, at our prelims, we explained that we wanted to continue to invest in the digitalisation of the business and also to take a step up in brand marketing as we evolved our eco system. In this case by developing our Home of Homes brand platform. We also expanded our store estate and continued with our rolling programme of store refits. These initiatives added around £16m to year-on-year costs. Looking forward, the forthcoming rise in the national living wage rates means that upward inflationary pressure will continue in H2. We are maintaining our guidance of a cost to sales ratio of about 39%.

Let's move onto the bottom part of the P&L. You can see that our profit before tax has grown by 4.8%. Net financing costs of £3.9m include interest on IFRS16 lease liabilities of £3m. We feel fortunate that we are not having to finance significant amounts of debt in these times. Our effective tax rate increased from 20.8% in H1 FY23 to 26.3% in this half. The majority of this increase related to the increase in the rate of corporation tax. The remainder of the increase above the headline rate of tax related to more disallowable property related expenses, and a deferred tax adjustment, which is non-repeating. The increase in the tax rate was reflected in our EPS of 44.6p, which is 2.6% lower than it was last year. Just for noting, without the change in corporation tax rate, EPS would have increased by 3%.

Moving on to cash flow, you can see how we generated and spent our free cash of £91m. Cash conversion of 72% included the impact of increased capex and higher tax payments. We had a modest working capital outflow; and stock levels and quality are good. Capex of £20m was in line with our anticipated accelerated store activity. We opened 4 new stores in the half, two superstores and 2 smaller format, compared with 3 in the prior year. We also refitted 12 stores. Dividend payments of £54.5m were slightly higher year on year, and we ended the half in a small net cash positive position of £6m.

Our capital allocations methodology supports attractive shareholder distributions. This is a reminder of our continued strong shareholder returns record. With profit growth, a strong balance sheet position, and confidence in our future prospects, the Board has declared an ordinary dividend of 16p, which is a 7% increase, and a special dividend of 35p, both to be paid in April. Net debt after dividend commitments is 0.3 times, and therefore in line with our target range.

Before handing back to Nick, I'd like to close with the following guidance. Despite operating in an uncertain environment, we are confident that we will see full year gross margin around 100bps higher than FY23. We are maintaining our guidance on operating costs at around 39% of sales. With 4 stores opened in the first half of the year, we are well on track to deliver 5-10 new stores in the full year. We expect our full year tax rate to be consistent with the half. And finally, we expect our full year profit before tax to be in line with market expectations. Thanks for your attention, and now let's go back to Nick.

Nick Wilkinson: Thank you, Karen. Building the Home of Homes, building Dunelm into a bigger market leader. How are we getting on. But firstly, lets think about the world in which we are operating.

In a changing world, it's never been more important to be focused on customers. Muti channel shopping is now established in homewares as the overwhelming preference for most consumers. Very few say that they are an online only or a store only customer in our categories. But channels aside, consumer attitudes are evolving at pace. And consumers are diverging in terms of what they are looking for in terms of their attitudes to home, what they expect from the products that they'll buy, and how they want to shop. Responding to this, we feel advantaged as a specialist. We have breadth and depth. Breadth of categories, price/quality tiers, and styles. And depth of knowledge in product design and supply chains and services that allows us to adapt and innovate, able to grasp and control more levers, and be relevant for consumers. We have also significantly increased our consumer insight capability in recent years. From listening directly to customers, more rigorous testing of new initiatives, and by leveraging the data which flows into us from digital and physical channels. This allows us to focus our efforts on the most meaningful changes for most customers. It's incredibly exciting to be working at a time when technology and data capabilities allow us to serve up the right products, through the right channels and content, to appeal to different customer needs, effectively and efficiently. If you attended our investor event in November you will have seen some examples of this, as we build our offer and identity.

So let's get a bit more specific, and I'll bring to life how we are building the Home of Homes. They are familiar themes to those of you close to our business and these are the levers we are using to drive our market share growth. Strengthening our customer offer in particular with regard to value and choice. Extending and digitalising our total retail system, with more stores planned and continued digital optimisation. And evolving our marketing into an ecosystem that is both national and local, digital and physical. Across these three themes we continue to invest with discipline and long-term focus. And we continue to have fun, and not take ourselves too seriously. Our average item is just over £14, you can get a great coffee for about £2, our colleagues are friendly, and we like to give our customers a little bit of joy when they are shopping.

We are continuing to evolve our pricing hierarchy. We always aim to have good, better and best price/quality tiers in our core ranges. In reality that's often a simplification. In plain dye sheets we have over a dozen tiers between the lowest priced good tier to the highest priced quality tiers. The key to doing this successfully is that each tier needs to have meaningful differentiation. From a £2 pillowcase pair made from a soft touch microfibre, to £35 for a pillowcase of the finest cotton from Dorma. We are not changing the proportions of our range in each tier, but we are introducing more innovation this year into our better and best tiers as disposable income and confidence increases for some consumers. For example in bedding introducing, under our Edited Life label, fine linens priced from £80 for a duvet set for a single bed. Another example is the work we have done in upholstered furniture to offer quick delivery lead-times of 5 days, and a wider choice of styles and sizes of sofas, sofa beds and occasional chairs. We've done this without growing the size of the range we stock, removing duplication as we become more confident in product selection, and thereby improving availability. The resulting sales and share growth has been positive, and we think there's a lot more to go after. Cook and dine is another part of our business where we are growing strongly from a lower base in terms of market share. Less of a new category for us than furniture, it's an area where we have recently increased our investment in product design and sourcing. We've improved ranges in kitchen storage and glassware, for example, and we've introduced some popular third party brands where these are additive to our offer. One final example. As we've described before we're adding more choice, and entering new areas, by adding to our online ranges that are delivered directly to consumers. This is still curated product, with the same product quality focus and outstanding value for money. Through it we learn about new areas and build new relationships. We're now up to just over 80,000 products, and recent additions include a much wider range of ottoman or storage beds and headboards

Being a good company is central to our thinking across the business. The progress we are making on our net zero roadmaps for materials, manufacturing and circular design is resulting now in better product choices for our customers. Good and circular are the words we use to describe all of this. We also include here our work in ethical sourcing, in our communities and with charity partners. This is increasingly important in building brand trust, for digital shoppers especially who often come across us first through a specific product page or social post. More of our range is now able to carry our Conscious Choice label, meaning it comes from more sustainable materials and sources. As we strive to make these choices available at no more cost to consumers, we are seeing good, high quality supply of recycled polyester and more sustainable cotton. We are moving away from mixed materials, which are less valuable when recycled. For example, our Elements collection of bedding will now be made from 100% cotton rather than a polyester cotton mix. Another nice example is the exclusive collection we've launched with the sustainability-focused seafood restaurant chain Rockfish. Coastal-inspired tableware and textiles. Made from recycled ceramics, durable stoneware and recycled fabrics. Mugs from £7, and in fact we are doing children's sized mugs as well as adult sized one, with those from £5. Being a good partner to community causes is part of our DNA. Born in the pandemic, the Delivering Joy campaign this Winter was our biggest ever with over 125,000 gifts donated by our customers to local good causes, through our store teams. Double the number of the previous year, the campaign again grew virally and was picked up on news channels across the country.

Moving on to our retail system and we'll start with stores. Our stores continue to underpin our total retail system, amplifying our digital channels and being a key part of our marketing ecosystem, combining the benefits of physical shopping with the convenience of our digital offering. At the start of the year we announced plans to increase the rate of our new store openings, broadening the range of sizes and locations, from which we continue to test and learn. We are on track with these plans, opening four stores in the first half, including both superstores and smaller formats, and across a range of location types from a large shopping centre, to suburban schemes, to our more typical out of town sites. We are really pleased with performance to date, and continue to see our new stores pay back very quickly, on average in less than three years. We will continue to carry on testing and learning from our different store types, and a good example of this is the progress of two contrasting stores in the table on the right which opened at the end of 2022. Weymouth is a 30,000 sq ft out of town superstore, creating a new catchment area for us with drive times to existing stores over 40 minutes from Weymouth. Feltham is half the size, and you could call this store an infill, as its fairly close to existing Dunelm stores in West London. But with over 400,000 adults in a 20 minute catchment, and a large number of urban customers not owning a car, it significantly increases our reach and convenience for consumers in this part of London. These two very different stores will both achieve very attractive paybacks. As well as achieving good sales densities they are also growing our online sales. In Feltham we've seen a particularly high proportion of click and collect sales, while Weymouth has triggered a material increase in online home delivery sales in its catchment. As well as new stores, we continue to innovate in format and design, the learnings from which flow into our refit programme. Both into the major refits we do to update older stores, and into smaller changes we roll back into many stores, such as the new displays we have for Dorma bedding. We're testing new cook and dine formats in several stores at the moment.

In our digital channels you may recall that we have been breaking up our site into smaller, more manageable pieces of code, so-called micro front ends. In November we introduced this to our product details pages. These are our highest traffic pages, and we've seen a material increase in their speed and performance. The table shows the Google ranking for page views classified as having a good customer experience, which is a multi-factor assessment of page speed and stability. Dunelm.com has moved up 4 places in the ranking, from being quite frankly a site which was too slow to being in the pack with the biggest and best pureplays and multichannel retailers. The improvement is material, we estimated that over 15 days of our winter sale our customers saved a cumulative 40,000 hours on our website. A faster site improves our SEO rankings, organic traffic, and conversion. Improved site architecture allows our engineers to work on development and optimisation in smaller teams, with more domain knowledge, and to test and release more efficiently. A change we made a few weeks ago, shown on the right hand side, has improved the presentation of delivery options, allowing customers to check for local store availability more easily and intuitively. This small change is still meaningful. This one's worth an incremental 1% of digital channel sales.

And finally, the third area moving on to our marketing ecosystem. This picture is from our brand campaign, which is a long-term investment in building brand awareness and consideration across multiple product categories. It's also a short-term investment because we tested the in-year sales incrementality the previous Autumn. When we run the campaign again this spring with creative which we're currently shooting we will repeat the incrementality test, by holding out in one region. Our marketing ecosystem spans many different channels which reinforce each other in terms of effectiveness and efficiency. Let me bring it to life with some examples of what we're doing.

On personalisation we're building, with a goal to deliver content that feels specific and relevant to our customers, based on their interactions with us. We've made some good initial steps and have good foundational capability in terms of data and systems, and in terms of people. We continue to test and learn in areas like complementary product recommendations on the site, or the best incentive to offer those customers who we assess as having a low propensity to re-purchase. We'll shortly start to personalise our email newsletter distribution, for example not sending our fiver friday email which feature products for less than £5 to those customers who are less attracted to lower priced products, instead sending them alternative content. Performance marketing continues to be an area of optimisation. In paid search, new campaigns and landing page designs are improving our returns and making multiple marginal gains. In social media marketing we're less developed, so we are incrementality testing on Meta and Pinterest to confirm the scale of new opportunities. Meanwhile we remain focused on generating free traffic and growing our SEO rankings. Locally, our store run Facebook groups are thriving, and every store works hard to build followership. In Cwmbran when we opened that store recently we had 5,000 followers on day 1 of opening. They'll choose local charity partners to help them, they'll create content based on what they want to promote in their store, and they're now tapping into local influencers as well as national ones, letting local influencers film in their shops to make videos for their community. And sometimes we'll help with some centrally arranged special events to give them a boost and have some fun. The picture is from a broadcast we did last week with ITV's This Morning, which got good free coverage across our Facebook groups.

So, with a spring in our step. We continued to perform strongly in the first half, outperforming a challenging market and demonstrating operational grip. The breadth of growth both across our product categories and across different customer groups is the result of many disciplined actions and decisions to raise the bar on our customer offer and our operations funded from the margins and the cash that our business generates so well. We'll carry on focusing on making good long-term decisions. Offering more value and choice, extending our operating model and marketing, and building the Home of Homes. And we will continue to navigate and adapt to continued economic uncertainty. So far in the second half we are pleased with trading. And we expect to deliver full-year PBT in line with market expectations.

Thank you for listening.