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MANAGEMENT DISCUSSION SECTION

Operator: Good day, everyone, and welcome to the Estée Lauder Companies Fiscal 2018 Fourth Quarter and Full Year Conference Call. For opening remarks and introductions, I would like to turn the call over to the Senior Vice President of Investor Relations, Ms. Rainey Mancini. Please go ahead.

Laraine A. Mancini

Senior Vice President-Investor Relations, Estee Lauder Cos., Inc.

Good morning. On today's call are Fabrizio Freda, President and Chief Executive Officer; Stéphane de la Faverie, Global Brand President of Estée Lauder; and Tracey Travis, Executive Vice President and Chief Financial Officer.

Since many of our remarks today contain forward-looking statements, let me refer you to our press release and our reports filed with the SEC, where you'll find factors that could cause actual results to differ materially from these forward-looking statements.

To facilitate the discussion of our underlying business, the commentary on our financial results and expectations is before restructuring and other charges, the impacts of the recently enacted U.S. tax law, and other adjustments disclosed in our press release.

You can find reconciliations between GAAP and non-GAAP figures in our press release and on the Investors section of our website.

During the Q&A session, we ask that you please limit yourself to one question, so we can respond to all of you within the time scheduled for this call.

And now, I'll turn the call over to Fabrizio.

Fabrizio Freda

President, Chief Executive Officer & Director, Estee Lauder Cos., Inc.

Thank you, Rainey, and good morning, everyone. Fiscal year 2018 was an outstanding year for our company. By focusing on strategic priorities and investing in our multiple engines of growth, we delivered double-digit sales and earning per share gains in all four quarters. In constant currency, full year sales rose 13%, nearly twice the rate of global prestige beauty, and diluted EPS increased 24%. This was the ninth consecutive year of record sales and one of our best performances in the last decade.

Coming off an excellent fourth quarter, we expect our strong growth to continue in fiscal year 2019. Our success last year was broad based, with higher sales in every region, in every major product category, which is consistent with our long-term growth strategy. What made our performance particularly strong were our overachievements in Asia and in skin care globally.

We strengthened our hero franchises with new products, expanded in fast-growing, brand-building channels and invested in the areas that touch younger consumers. Our growth was all the more remarkable given the challenges we faced. Competition intensified from new brands and business models, and doors closures and weak traffic affected certain brick-and-mortar department store in the U.S. and UK. On a macro level, Brexit and other tensions caused greater political and economic volatility.

Our results speak to the soundness of our strategy, the sustainability of our business and the resilience of our organization. Sales climbed globally in virtually all our brands. La Mer reached an exciting milestone; its net sales topped \$1 billion for the first time. We have now four brands in our portfolio whose net sales have crossed the \$1 billion threshold and each grew globally.

Estée Lauder had a stellar year, achieving record global sales and growing an outstanding 22% in constant currency, demonstrating its huge worldwide appeal. Estée Lauder generated strong growth in skin care and makeup, and across markets and consumer groups. Stéphane will elaborate in a few minutes.

Clinique's growth was driven by solid global skin care gains, particularly moisturizer, its largest subcategory, and its hero franchise, Moisture Surge. Clinique had strong gains in many emerging markets and in Asia, where its hero franchises grew more than 30%. Clinique continue to diversify its distribution and Tmall became its largest door in Asia. We are upbeat about Clinique's outlook. Its skin care innovation program this year will be especially strong and [ph] leverage trends (00:04:29) of growing consumer interest.

M•A•C delivered global growth, which was supported by strategic investment in advertising to accelerate the brand in fast-growing areas of Asia and travel retail. This winning strategy is similar to the approach we took with our Estée Lauder brand several years ago, which is paying huge dividends for the brand now.

M•A•C sales in China more than doubled. In its first full year on Tmall, it was the top-selling prestige makeup brand. Although M•A•C continue to struggle in North America, we actively began turning it around by expanding it further in specialty-multi retail in the U.S. and Latin America, strengthening its innovation program. We are optimistic about [ph] M•A•C's future, expected (00:05:21) to deliver stronger global growth in fiscal year 2019.

Many of our small and mid-sized brands grew sharply and several are on track to become billion dollar brands within the next few years. We grew our recent acquisitions with successful new products and expanded distribution, which attracted new consumers. We increased our focus on innovating in skin care, believing there will be a resurgence in the category.

As consumer demand grew, we were ready with products for different concerns and age groups, and products with instant benefits, which made the compelling visuals online. Our effort resulted in skin care being our fastest growing category fueled by La Mer, Estée Lauder and Clinique as well as Origins and GLAMGLOW.

Much of the category's growth came from Asia/Pacific and travel retail where we gained share. Many of our brands also grew in North America. La Mer creative digital content and authentic storytelling helped to build greater awareness, which led to share gains in every region and channel. Importantly, in markets where we can accurately measure, more than half of La Mer consumers were new to the brand.

Estée Lauder strong sales boosted its global rankings to number one in prestige skin care and number two in total prestige beauty for calendar year 2017. Our makeup business remain healthy with Tom Ford and Estée Lauder leading the growth, along with M•A•C in Asia.

Our newness brands, Too Faced and BECCA, expanded internationally, mostly in specialty-multi retailers, and Too Faced opened its first freestanding store which is located in London. With improving retail trends and a greater presence in direct-to-consumer channels, Too Faced grew 22% in fourth quarter. And with strong innovation, it is well positioned to post strong results globally in the year ahead.

Our luxury and artisanal brands continue to drive our fragrance growth, led by Jo Malone London and Tom Ford, which introduced successful scents and opened new doors. Jo Malone solidified position in the UK, its home-base, where it gained share. Just last week, Jo Malone launched on Tmall and sales during the first few days have been very strong. Combined, our newer brands Le Labo, Frédéric Malle and By Kilian contributed already approximately one quarter of the total category growth.

[indiscernible] (00:08:16) growth in hair care as Aveda [ph] tapped (00:08:19) into the natural and wellness trend with its plant-based product. Successful launches in hero franchises such as Invati played a key role. Our innovation was concentrated on fewer, bigger launches in the largest subcategories, with a focus on supporting our best-selling hero franchises. This strategy produced terrific results. Sales from our top 30 new skin care product and initiative rose more than 30% from the year before.

We continue to expand in the fastest growing prestige channels, travel retail, online and specialty-multi. In travel retail, in calendar 2017, we gained share across all categories, became the top ranked beauty company in Asia/Pacific airports and reinforced our global leadership position in skin care and makeup. Our successful travel retail strategy benefited from higher global passenger traffic. Chinese travelers are important shoppers in the channel and their increasing travel helped meet growth across our portfolio.

Once again, our online business strived with our own brand sites, retailer sites and third party platform all growing. There were more than 430 million visits to our brand.com sites this year. And these sites have become more than just point-of-sales. They are also influential editorial platform and equity-building vehicles. During the year, we opened 200 new online doors globally and launched e-commerce in five new markets.

We truly are a global enterprise, and nearly three quarters of our markets generated gains. As sales outside North America had expanded, our international business has become one of our best growth engines, now accounting for nearly 70% of our sales.

Emerging markets around the world have been a significant growth vehicle. Sales in our emerging market jumped 24% and accounted for 15% of our total business. We intend to continue to invest in many of these markets in fiscal year 2019, laying the ground for our continued growth as the purchasing power of their middle classes continue to increase.

Our Asia/Pacific region generated the fastest growth, led by an acceleration in China and the resurgence in Hong Kong. Our China business grew rapidly in every category, every channel and in virtually every brand. China net sales well exceeded \$1 billion for the first time. The country's prestige beauty growth is benefiting from heightened interest from Gen Z, a millennial consumer, who have considerable spending power and an appetite for high quality luxury product and we tapped into that opportunity. For example, more than 40% of Chinese consumer who were new to La Mer are in their 20s.

We had mixed results in Europe, Middle East and Africa, with strengths across developed markets like Italy as well as several emerging markets like Russia. We gain share in Western Europe and in Eastern Europe, but sales fell in the Middle East where our results were also affected by our decision to adjust inventories on multiple brands. The UK market slowed as Brexit affected consumer confidence, which primarily impacted certain brick-and-mortar department and freestanding stores.

We increased investment in [ph] new winning (00:12:14) channels. Online was a bright spot, driven by retailer.com. M•A•C was our first brand on ASOS, an online company that caters to younger consumer. It was followed by GLAMGLOW, Too Faced and others. Prestige beauty was buoyant in North America. And in each

major category, we had brands that gained share in the U.S., La Mer in skin care, Estée Lauder and Too Faced in makeup and Jo Malone and Tom Ford in fragrances.

We have been pivoting our distribution towards faster-growing channels and the scales started to tip in our favor. Our incremental sales in specialty-multi and on our brand.com sites were greater than the decline we experienced in brick-and-mortar department stores.

Our business trend in U.S. department stores overall showed improvement from the year before and our sales on their online sites are rising rapidly. However, total U.S. department stores sales declined mainly due to the liquidation of Bon-Ton.

Over the past two years, we have successfully offset the loss of more than \$150 million in annual net sales in North America from the closing of Bon-Ton, Sear Canada and other department store doors. Despite these challenges, we had growth in North America in fiscal year 2018.

Our Clinique brand was the most impacted by the loss of Bon-Ton and dozen of other department stores doors. Nonetheless, Clinique recouped a large portion of the business by staying in touch with consumer immigrating them to other Clinique doors. In total, Clinique North America retail sales increased by focusing on fast-growing channels, product categories and new consumer segments.

Our strategic investment in advertising spending on all of our brands helped get our product noticed. Now, each brand has a digital [ph] president (00:14:28) and digital accounted for nearly two-third of our ad spending, up sharply from about 50% the year before.

People are the heart of our company and we announced our benefits to build loyalty and attract the best talent. We expanded our benefits around adoption, child and elder care, and awarded a special bonus to employees who don't receive equity-based compensation to recognize their terrific contribution.

As we realigned the company focus to strengthen our position in the areas that will lead future growth, we hire and develop talented employees with skills needed in these new areas. We also began offering learning and training opportunity online throughout LinkedIn Learning helping our employees build competencies in a variety of areas.

We are proud that our commitment to our employees is being recognized. Our company was named the Top-Rated Workplace by the jobsite Indeed and recognized by Forbes as one of America's Best Employers for Women.

Fiscal year 2018 gave us a lot to celebrate, but we are now focused on the future. To that end, we updated our 10-year compass, which identifies industry and demographic trends. These insights confirmed the strategic focus areas where we have invested to [ph] build growth (00:16:04) and where we plan to continue over the next few years, including skin care, online, traveling consumers, digital marketing and omni-channel retail.

We will continue to seek growth globally among a more diverse and growing middle-class, especially in growth markets like China and in our U.S. home market. We are the number one prestige beauty company in the U.S., which still remains the largest market and where we are focused on regaining share.

We continue to build distribution in high growth channels and leverage better data and analytics to tailor our product assortment by retailer and by specific doors. This help us address hyper local demand by having the right

products on the right shelves with relevant messages. We [ph] forecast continued (00:16:57) growth in our EMEA region, with strengths in both Western Europe and emerging markets, along with a return to growth in the Middle East.

Our innovation pipeline is powerful and focused on hero franchises, elevated packaging and new technologies deployed against key subcategories. We expect this will help our growth become more balanced across our four product categories. Fast-moving technology innovations continue to enhance the luxury beauty experience and we are advancing features like augmented reality and voice-assisted shopping, which are gaining favor among consumers. Behind the scenes, we are focusing on improving our capabilities in data and analytics. Using cutting edge tools and techniques, we are connecting data and insights to measurable actions across our brands.

Now, I want to update you on the review of certain testing related to product advertising claims support that we discussed in our last call. The review is ongoing and based on the review to date, the company does not believe that this matter will be material.

In addition, we are closely watching the evolving global issue concerning tariffs and trade, including Europe and China, important markets for us, where we intend to remain focused on our long-term growth. We believe we will have some flexibility to address the potential impact of existing and proposed tariffs and remain committed to satisfying global consumers with our quality products.

Our strategy is solid, has been validated by our updated compass and should allow us to continue to deliver strong top line and double-digit EPS growth over the next few years. Our growth will be supported by Leading Beauty Forward, which is projected to deliver greater savings than originally planned.

We will invest a portion of the savings in area driving the next stage of growth, including digital advertising, social media, talent acquisition, technology, and other capabilities. At the same time, we are driving efficiencies throughout the organization and leveraging growth, enhancing our profitability. Tracey will give you an update in few minutes.

Global prestige beauty is exciting, dynamic and fast-growing, with a proven successful strategy and brands and products [ph] that coveted (00:19:34) around the world, we expect to continue to drive industry leading sales and gain share.

I want to thank my leadership team, and all the company global employees for truly remarkable results even in the midst of ongoing challenges. We look forward to delivering another year of strong top and bottom line results.

I'm happy now to introduce Stéphane de la Faverie, Global Brand President at Estée Lauder, who will discuss our iconic brand's stellar year and the strategies that have kept it relevant to a new generation.

Stéphane de la Faverie

Global Brand President, Estée Lauder, Estee Lauder Cos., Inc.

Thank you, Fabrizio. Good morning, everyone. I joined The Estée Lauder Companies over seven years ago and was honored to become the Global President of the Estée Lauder brand two years ago. Today, 72 years after its founding, our flagship brand is not only the largest in the company, but one of the fastest growing as well. Estée Lauder is stronger than ever and demonstrate that our authentic roots make the brand relevant for women of all ages, backgrounds and ethnicities around the world.

The brand strategy which is fully aligned with the company 10-years compass has resulted in accelerating growth. The fourth quarter of fiscal 2018 was the fifth consecutive quarter of double-digit sales increase, [ph] cumulating growth at (00:21:01) nearly 22% in constant currency for the full year. The brand gained share in virtually every market around the world.

The main element of our success, our focus on hero products, digital marketing and social engagement and fast growing channels. Our winning strategy is also concentrated on the turnaround of our home market, the U.S., and the acceleration of our business as we sell and delight emerging middle-class Chinese consumers around the world.

The first element of our strategy is our focus on hero products which has reinvigorated the brand, generated strong double-digit growth in both skin care and makeup globally. Skin care outpaced the growth of the overall brand for the year. The brand's largest franchise, Advanced Night Repair, has been growing high double-digit in virtually every market and channel.

The July 2017 launch of Advanced Night Repair Eye Matrix Concentrate has been a resounding success and help solidify our leadership in the eye treatment subcategory. Every one of our top five skin care franchise is growing and addressing different consumer benefits and needs.

Makeup grew at about the same rate as the overall brand, enabling Estée Lauder to gain share globally, largely driven by our Double Wear foundation franchise. The collection has been supported by newly activated communications around wider range of shades and form such as Cushion Compact to address the need of consumer worldwide.

Our success in the recruitment and retention of all consumer age group is evidence that our strategy to modernize the brand has paid off. Today, Estée Lauder [ph] consumer are about (00:22:56) one-third millennial, one-third Gen X and one third ageless. This mix puts us in a strong position to continue to win in all prestige channel and in our key product categories around the world.

In addition, the brand global spokesmodel celebrate women of all ethnicity and ages to help the Estée Lauder brand win in virtually all markets. Our newest face is Anok Yai, a Gen Z who was born in Egypt of the Sudanese descent. She joins millennial actress Yang Mi from China and our longstanding American model Carolyn Murphy to name just a few.

The second part of our strategy is our focus on being a truly digital first brand. About two-third of our global media spend is in digital and social, helping us to reach new consumer on platforms such as Instagram, Facebook, Weibo, WeChat and KakaoTalk.

We are partnering with major digital and social players worldwide to leverage improved consumer insights and data to enhance our storytelling, connect in a deeper way with consumers and build campaign with even stronger returns on investments. In addition, we have activated the use of influencers. We have super-influencers including our latest celebrity model, Karlie Kloss and Violette, our digital-native Global Beauty Director.

We utilized influencer in many markets and leveraged our beauty advisor, who had been trained to become what we call Estée micro-influencers. Taken together, the voice of the brand has been unleashed in a more authentic and powerful way. The strategy has helped us to better connect with younger consumer at the point of sales and decision-making, which is done on social and digital platforms.

And further, we continue to evolve our distribution. In fiscal 2018, over 50% of our business came from fast-growing channel, which includes specialty-multi, online and travel retail. In specialty-multi, our expansion into Ulta in the U.S. has allowed us to reach younger consumer, many of whom are new to the brand. Today, half of our consumers are Ulta, are millennials.

Our global online business grew 60% and represent more than 10% of our total sales and even more than 20% in the U.S. and China. Online is growing from our own brand.com sites, retailer.com and third-party platform like Tmall, which allows us to connect with new consumers everyday particularly in smaller cities where we have less physical presence which makes our consumer reach extremely efficient.

We're also experiencing a rapid acceleration in travel retail where Tmall doing exceptional work to support the desirability and the equity of the brand by connecting with consumer throughout their journey standing at home, into the airport and at their final destinations.

From a geographical standpoint, I'm proud to say that net sales in every regions are growing, including a solid performance in North America for the year. In fiscal 2018, the Estée Lauder brand passed \$1 billion market retail for the first time in the U.S. and gained share in makeup in 10 out of the last 12 months.

In the U.S., we are the number one prestige beauty brand in over 350 department stores and a number one brand on retailer.com nationally. In addition, we continue to hold top ranks in skin care and in age-specialist and foundation subcategories.

Thanks to a laser-focused strategy on hero franchises, online acceleration and the rapid diversification of our distribution, we gained over 1 million new U.S. consumers, who are younger, more diverse and more affluent than the average existing consumer of the brand. We believe we have successfully turned around the U.S. business and are poised for continued growth going forward.

The Estée Lauder brand now generates 80% of its business outside of North America and we've been particularly successful in Asia/Pacific. We continue to be the number one luxury beauty brand in the region led by exceptional performance in China. For the second consecutive year, we were the only brand ranked as Genius by the L2 research firm, which placed us as the top brand in Digital IQ.

These performances are fueling our already strong brand equity and desirability with Chinese consumer around the world. In addition, we continue to serve Chinese consumer with a deep understanding of their needs and diversity by creating relevant products and communication uniquely designed for them.

Estée Lauder is also outperforming in the UK, growing 5% in the context of a flat prestige beauty market. Our Double Wear Liquid foundation is the top luxury beauty SKU in the market. We also have strong momentum in our markets in our European and Latin America region, thanks to a consistent global strategy.

Last but not least, as part of our Leading Beauty Forward initiatives, our teams around the world has been relentless in reallocating resources effectively to focus on consumer engagement activities while delivering increased profit margin to the company. We reduced certain selling costs by increasing productivity in profitable distribution channels, rationalizing non-profitable doors and accelerating our distribution shift to less costly models.

Our promotion expense has also been significantly reduced as a percentage of net sales. As a result, we dramatically increased our advertising spend especially in digital, and in addition, we continue to price in line with inflation and further improve our gross margin.

In summary, thanks to a strategy aligned with the company, we believe our success is repeatable and sustainable. Our great progress in fiscal 2018 was largely driven by same-store growth, no distribution expansion as well as an increase in repeat purchase from existing consumer, high new consumer acquisition, especially among younger ones, and strong creativity and innovation.

All of it taking together makes the Estée Lauder brand a sustainable and profitable growth engine for the company, and at the same time, demonstrate that big brands can grow fast while building desirability and exclusivity around the world.

I would like to personally thank my extraordinary boss, Jane Hertzmark Hudis, my amazing team, and my colleagues around the world for their commitment to the iconic Estée Lauder brand and to our success.

And now, I will turn the call over to Tracey.

Tracey Thomas Travis

Executive Vice President & Chief Financial Officer, Estee Lauder Cos., Inc.

Thank you, Stéphane. And I believe many of the elements of the strategy you just articulated are already inspiring the plans of our other big brands. My commentary today excludes the impact of restructuring and other charges and adjustments, including those related to our Leading Beauty Forward initiative and the new U.S. tax legislation. All net sales growth numbers are in constant currency unless otherwise stated.

Starting with the fourth quarter, net sales rose 12% to \$3.23 billion compared to the prior year. All regions grew with the largest contribution coming from Europe, the Middle East, and Africa. Net sales in the region rose 16%, led by strong double-digit increase in global travel retail.

The momentum achieved in the travel retail channel reflects a 6% rise in international passenger traffic, share growth in all travel retail regions as well as double-digit gains across virtually all of our brands.

In addition to travel retail, the EMEA region also benefited from double-digit sales growth in Greece and India as well as solid growth in Italy, Russia and Benelux. This growth was partially offset by weaker results in other markets, notably the Middle East, the UK and Germany.

Our business in the Asia/Pacific region rose 24%. Continued momentum in China and Hong Kong both with strong double-digit growth, largely drove these results which was broad-based across brands, product categories and channels. We also achieved solid sales growth in Japan, Australia and Thailand.

Net sales in the Americas grew 2%, Latin America rose 8% led by double-digit increases in Mexico and Colombia which were partially offset by a sales decline in Brazil.

Sales in North America rose 2% as growth in Canada, brand.com and specialty-multi retailers were partially offset by continued softness in department stores, including certain door and retailer closures, as previously discussed.

The continued rebound in skin care led product category growth this quarter. Skin care sales grew an outstanding 26% with strong contributions to growth from innovation within key hero franchises such as Estée Lauder, the

Estée Lauder brand's Advanced Night Repair franchise, La Mer's The Moisturizing Cool Gel Cream and Clinique's Dramatically Different and Moisture Surge franchises. Origins and GLAMGLOW also contributed to the growth and all regions grew skin care sales.

Net sales in makeup grew 2%. Many of our brands reported higher sales. Estée Lauder benefited from the continued success of Double Wear foundations. Tom Ford lip and eye products drove growth in Asia/Pacific and travel retail.

Too Faced launched Super Coverage concealer and extended shades in its Born This Way Foundation line and La Mer launched its Luminous Lifting Cushion Compact in Asia. These gains were partially offset by declines from M•A•C and Clinique. M•A•C's outstanding growth in Asia and travel retail was offset by continued weakness in the U.S. and UK in bricks-and-mortar as well as inventory rebalancing in the Middle East.

Sales of fragrances grew 9% led by the continued strength of our luxury and artisanal brands. Jo Malone limited edition collection Blossom Girls collection was popular in Asia and travel retail and a variety of Tom Ford fragrances resonated across all regions. Le Labo continued its strong comp door growth and expanded its reach in the Middle East, Australia, Europe, and travel retail.

Our hair care sales rose 6%, primarily driven by Aveda's launch of Invati Advanced, the professional color line Full Spectrum Demi+ and the relaunch of Cherry Almond shampoo and conditioner. Bumble and bumble's expansion in specialty-multi retailers also weighted growth in the category.

For the quarter, our gross margin improved 20 basis points compared to the prior year due primarily to favorable pricing and mix, partially offset by higher obsolescence and the higher cost of some new products.

Operating expenses increased as a percent of sales by 110 basis points, primarily reflecting the significant planned increase in advertising support behind digital activities, partially offset by efficiencies in selling operations. As a result, operating income rose 3% and operating margin decreased by 90 basis points.

Diluted EPS of \$0.61 was 20% above the prior year and grew 11% in constant currency. Earnings per share for the quarter included \$0.05 of favorable currency translation.

Now, let me cover few highlights of our full-year results. Net sales grew 13%, of which incremental sales from our most recent acquisitions contributed approximately 2 percentage points.

Our gross margin decreased 10 basis points as favorable manufacturing costs and foreign exchange transactions were more than offset by the full-year impact of the fiscal 2017 acquisitions.

Operating expenses as a percent of sales improved 80 basis points, primarily due to greater efficiencies in our selling model. We strategically redeployed these savings into digital advertising, social media and influencer outreach.

Our full-year operating margin rose 70 basis points to 16.6%. This margin included 40 basis points of favorable currency translation and 20 basis points of dilution from the fiscal 2017 acquisitions.

Our Leading Beauty Forward Initiative and ongoing cost saving programs contributed more than \$270 million in savings, which helped offset the strategic investments we made to support future growth. The changes in our P&L

reflect the accelerated restructuring of our cost structure to increase our flexibility to both reinvest in areas of profitable growth and to mitigate risk.

Our effective tax rate for the year came in at 22.3%, an improvement of 540 basis points over the prior year, driven by excess tax benefits on share-based compensation and the lower U.S. statutory rate.

Net earnings grew 31% to \$1.7 billion and diluted EPS rose 30% to \$4.51. Earnings per share included \$0.20 of favorable currency translation and at constant exchange rates grew 24% for the year.

In fiscal 2018, we recorded approximately \$193 million after-tax or \$0.51 per share in restructuring and other charges for our Leading Beauty Forward Initiative. We are making remarkable progress on the program and have identified additional opportunities with existing initiatives as well as new ones.

We plan to approve specific initiatives under Leading Beauty Forward through fiscal 2019 and complete them by the end of fiscal 2021. We now expect to incur charges of between \$900 million and \$950 million before taxes, in aggregate, over the life of the plan. Through this plan, we've established more efficient and effective shared services and procurement organizations, which are generating savings and allowing us to invest in critical areas of the business for future growth.

We now expect the annual net benefit before taxes to range from \$350 million to \$450 million, which represents an improvement in the cost-benefit ratio. This will afford us greater flexibility to meet our profit objectives while also continuing to invest for sustainable growth and manage additional risk.

We also recorded three items related to the new U.S. tax legislation which we consider non-recurring. These charges, the combined impact of which is \$427 million or \$1.14 per share, are provisional and are expected to be finalized within the one-year window allowed by the Tax Act.

Moving on to cash flows. Cash generated from operations jumped an impressive 43% to \$2.6 billion reflecting our outstanding earnings growth, improvements in our working capital management and the benefit of certain one-time items related to tax refunds. We utilized \$629 million for capital improvements, primarily for consumer-facing counters and gondolas, retail stores and e-commerce support, as well as supply chain improvements and IT.

We returned cash to stockholders at an accelerated pace in fiscal 2018. We repurchased 6 million shares of our stock for \$759 million, representing a significant increase versus the prior year. We paid \$546 million in dividends, reflecting a 12% increase in our dividend rate, the ninth consecutive year of double-digit dividend growth. In total, cash return to shareholders rose 45% compared to last year.

Overall, fiscal 2018 [sic] [2018] (00:39:44) was an outstanding year for our company. Our sales growth of 13% far exceeded our long-term target of 6% to 8% annual growth in constant currency and was enabled by our improved insight and analytics on where to invest.

We delivered 50 basis points of organic operating margin growth in line with our objectives. Importantly, we did so while making strategic investments to build capabilities and support our brands for the long-term health and sustainability of our business.

We delivered double-digit growth in earnings per share in line with our long-term targets. We saw a 12-day improvement in inventory days to sell. We recruited new talent and invested in our existing employees to align our capabilities to future needs.

So looking ahead, global prestige beauty growth has been exceptional in recent years, and we do expect it to rise in the range of 5% to 6% annually over the next few years, barring a significant political or economic macro event. Our goal is to grow at least one point ahead of the industry with possibly 1 percentage point of that sales growth contribution coming from acquisitions over the next three years.

Our Leading Beauty Forward initiative, which launched two years ago, is providing the fuel to innovate, accelerate changes to meet future demand, and engage effectively with consumers. We continue to target average annual margin improvement of approximately 50 basis points and double-digit EPS growth over the next three years.

Capital investments have historically averaged between 4% and 5% of sales annually. We do expect this level to increase to between 5% and 6% per year over the next three years as we invest more to increase the capabilities and capacity of our supply chain, enable enhanced consumer experiences with our new technology and invest in our facilities to optimize some of our workspaces.

We are dedicated to pursuing working capital improvement to free up cash, particularly in inventory. Our progress in this area has been slower than expected. This is partially due to the complexity in the shifting geographic mix of our business. Our strongest growth is coming from geographies further from our manufacturing facilities, increasing inventory and transit time. We now plan to reach approximately 165 inventory days to sell by the end of fiscal 2021.

Now, let's take a look at our expectations for the fiscal 2019 full year and first quarter. We are implementing the new revenue recognition accounting standard beginning in the first quarter of the fiscal year. We will adopt the new standard on a modified retrospective basis through cumulative adjustment to retained earnings.

This method does not require us to restate prior year periods. However, throughout fiscal 2019, we will provide a bridge between the new standard and the old one. The guidance we are providing today reflects the new standard, but we have also bridged to the comparable growth expectations we have for our business.

The new rule will impact where we reflect certain costs in the P&L along with the timing of revenue recognition. As such, our sales and profit growth as well as margins will be affected. Additionally, our initial revenue deferral based on this implementation will impact fiscal 2019 results.

The main impacts are: the cost for certain promotional goods such as samples and testers will be reclassified from advertising and promotion to cost of goods, certain payments to customers such as the cost of in-store demonstration will be reclassified from selling, general and administrative expenses to a reduction in net sales, and the timing of our revenue recognition will be impacted primarily by customer loyalty programs and certain promotional goods provided to retail customers.

The overall effect on fiscal 2019 is expected to be a reduction of net sales, an increase in cost of goods and a reduction in operating expenses. This will negatively impact sales growth for the year by approximately 1 percentage point, decreased gross margin by 260 basis points and decreased operating margins by approximately 30 basis points.

Earnings per share growth is expected to be negatively impacted by 2 percentage points for the year due primarily to the change in timing of revenue recognition on some promotional programs. The changes in timing of revenue recognition for certain promotional goods will also cause variability in our quarterly sales this year. We

anticipate that revenue deferrals in the first half of the year will begin to be recognized in revenue in the second half of the year.

For the year, net sales are forecasted to grow 7% to 8% in constant currency and excluding the impact of the new revenue recognition accounting standard at the high end of our long-term goal.

Pricing and targeted expanded reach are expected to each contribute approximately 2 points to our growth and the strength of our existing business will account for the remainder. We expect growth to continue to be driven by Asia/Pacific, the beginning of a turnaround in the Middle East and improvement in North America. All major product categories are expected to grow with the greatest contributions from makeup and skin care, our two largest categories.

Currency translation is expected to turn unfavorable in fiscal 2019 as the dollar strengthens. Based on June 30 spot rates at \$1.16 for the €1, \$1.31 for the £1 pound and \$6.63 for the CNY 1, we expect currency translation to negatively affect reported sales for the full fiscal year by about 2 percentage points.

We expect to continue to achieve cost savings through indirect procurement, A&P effectiveness and selling costs within our ongoing programs and from Leading Beauty Forward, which are expected to increase to approximately \$350 million this year.

Some of the savings will be reinvested in increased digital marketing and advertising to support strong growth as well as for the expansion of our smaller brands. Cost savings provide us with the fuel and the flexibility to both invest more in capabilities, advertising and brand expansion as well as deliver margin growth.

As we mentioned on our second quarter call, additional provisions of the U.S. Tax Act become effective for us in fiscal 2019. We now expect that the fiscal 2019 effective tax rate will be approximately 24% which includes the impact of a lower U.S. statutory rate as well as our current estimates related to the provisions from the Tax Act that go into effect this year. The impact of the accounting or stock-based compensation is not included in our estimates.

Diluted EPS is expected to range from \$4.62 to \$4.71 before restructuring and other charges. This includes approximately \$0.20 of dilution from currency translation. In constant currency and with comparable accounting, we expect EPS to rise by 9% to 11%.

In fiscal 2019, we expect cash flow from operations of approximately \$2.4 billion, slightly lower than fiscal 2018 due to the prior-year one-time benefits for tax refunds and the first installment of the toll tax.

Capital expenditures are planned at approximately \$835 million or 5% to 6% of sales as discussed earlier. Our sales in the first quarter are expected to rise 9% to 10% in constant currency using comparable accounting for revenue recognition. Currency translation and the accounting change are each expected to negatively impact growth by 2 percentage points to 5% to 6% reported, including both of these items.

We expect first quarter EPS of \$1.18 to \$1.21, including dilution of about \$0.04 from currency translation. EPS growth in constant currency and comparable accounting is forecast to rise by 7% to 10% for the first quarter.

In closing, we are clearly pleased with our outstanding results in fiscal 2018 and are excited about the momentum behind our strategic initiatives. Global prestige beauty is a fast-moving and competitive industry and the macro

environment grows more volatile by the day. Our ability to adapt in this rapidly-changing landscape is a testament to our sound strategy and to our amazing people.

That concludes our prepared remarks. We will be happy to take your questions at this time.

QUESTION AND ANSWER SECTION

Operator: [Operator Instructions] Our first question today comes from Erinn Murphy with Piper Jaffray.

Erinn E. Murphy

Analyst, Piper Jaffray & Co.

Q

Great. Thanks. Good morning. And a lot of great content in those remarks. I guess my question first is on the U.S., you called it out being positive in the fourth quarter. Can you talk a little bit more about the dynamics that you're seeing between the department stores and then the growth, in particular, you've been seeing within specialty-multi and online? And then, Tracey, as you think about the guidance for fiscal 2019, what are you assuming for the growth rate within the Americas? Thank you.

Fabrizio Freda

President, Chief Executive Officer & Director, Estee Lauder Cos., Inc.

A

So, on the U.S., we do see improvements, mainly coming from the strong retail.com of our department stores. And we are encouraged also to see brick-and-mortar business in North America department store doing better than last year. However, in addition, remember that we are facing the liquidation of 250 stores of Bon-Ton that have significantly impacted our business. For perspective, Bon-Ton just in fiscal year 2018 was for us \$68 million in net.

And as I said, we had to face the closure of the equivalent to \$150 million in net of department store doors in the past two years. So, this has impacted. But despite that, we have been offsetting this with the improvement in retail.com of department store and by the very good performance that we see in specialty-multi and in our online sites. So we are committing – we're really committed to continue to collaborate with our department store partners, with our specialty-multi traffic to continue drive traffic.

And also, I want to say that we have – under Leading Beauty Forward, we have restructured our field sales force and the new field sales force is just being deployed [ph] early July (00:51:15). And we have reduced the paperwork and administration activity resulting in a 70% increase in consumer-facing activity and products certain more tailored to each store starting this August. So, we're pretty positive on what we're doing to turnaround the business in the U. S.

Tracey Thomas Travis

Executive Vice President & Chief Financial Officer, Estee Lauder Cos., Inc.

A

And as it relates to the Americas for fiscal 2019, we're expecting low-single digit growth.

Operator: Our next question comes from the line of Dara Mohsenian with Morgan Stanley.

Dara W. Mohsenian

Analyst, Morgan Stanley & Co. LLC

Q

Hey. Good morning. So, first off, Tracey, can you give us the impact to earnings from FX if you use spot rates today, I'm estimating another \$0.08, \$0.09 of earnings impact for the full year? Does that sound like it's in the ballpark? And then, hopefully, that's just a clarification question, so hopefully that doesn't count as my question.

The broader one, Fabrizio, I wanted to get your thoughts on the potential for tariffs on the U.S. beauty industry in China. You mentioned, specifically, you've assumed some impact in your fiscal 2019 guidance. So I was hoping you could be more specific there. And are you basically sort of assuming an impact just from already announced plans, or are you assuming there may be some factors that emerge that aren't transparent today either directly or indirectly on consumer spending, whatever it maybe that have an impact on your outlook for fiscal 2019? Thanks.

Fabrizio Freda

President, Chief Executive Officer & Director, Estee Lauder Cos., Inc.

A

Yeah. You start.

Tracey Thomas Travis

Executive Vice President & Chief Financial Officer, Estee Lauder Cos., Inc.

A

So, on the currency, I'm not sure I picked up exactly on your question, but we expect a negative currency impact this year of \$0.20. And obviously, we experienced a positive currency impact in fiscal 2018.

Fabrizio Freda

President, Chief Executive Officer & Director, Estee Lauder Cos., Inc.

A

Yeah. On the tariffs, so the tariff in China is not being yet implemented, it's only a proposal. So first of all, it is not clear if the proposed tariffs will be implemented or not. But for information, currently less than one-third of our products that we sell in China are currently originated in the U.S. On the other side, if tariffs were applied, we will be also impacted from imports of components from China into the U.S.

The other thing to consider is that we have 80% gross margin. So the impact on tariffs on this kind of industry will be less onerous than what happens on commodities. We believe we can mitigate the impact of tariffs if they had to happen through some flexibility within our guidance, our manufacturing footprint, our LBF programs. And we will do our best to manage tariffs if they happen without impacting pricing directly because we will stay oriented to the long-term. We want to continue serve the Chinese consumer in the long-term, continue growing market share in China and we will stay focused on that.

I want also to clarify that we are already managing tariffs in Europe, which actually is a bigger business, which are fully reflected not only in our guidance and in our fourth quarter partially – in our fourth quarter, but definitely in our guidance for next year. And we are managing this also doing our best not to do price increases because of tariffs or relative to tariffs. So that's our situation, but we continue to hope that tariffs will not be applied also because beauty is not a category of tension and represents benefit for all countries.

Operator: Our next question comes from the line of Andrea Teixeira with JPMorgan.

Christina Brathwaite

Analyst, JPMorgan Securities LLC

Q

Hi. Good morning. It's Christina Brathwaite on for Andrea. Thanks for taking our question. So I just wanted to talk a little bit more about the [ph] raise in (00:55:30) Leading Beauty Forward savings guidance. Can you just dive into what the drivers are there or have you found some more incremental savings? And should we expect that

[indiscernible] (00:55:40) in the Americas [ph] top facility (00:55:42), we were surprised to see that turned negative this quarter? So, any kind of color on when that can stabilize would be great. Thank you.

Tracey Thomas Travis

Executive Vice President & Chief Financial Officer, Estee Lauder Cos., Inc.

A

Yeah. So let me answer both of those questions. And as it relates to the Americas, just recognize that in the Americas segment, we also have our corporate expenses. So from these accruals for the corporation, we have somewhat of our global production expenses related to some of our advertising programs flows throughout Americas segment. So those are some of the drivers along with some incremental spending for programs, just for some of our brands in the Americas.

As it relates to Leading Beauty Forward, some of the additional programs that we've added and we've spoken about them before, enabling our creative team to create more digital assets are really transforming the processes and the technology in our creative areas in order to be able to create more digital assets, restructuring some of our field organization to actually create more support organizations for them so that they can spend more time out in stores coaching and selling with our beauty advisors and with our selling staff.

In our supply chain area, we're investing to increase the agility and speed of our supply chain. Certainly managing all of the complexity that we see in our global network as well as the frequency with which innovation is happening in our portfolio.

Operator: Our next question comes from the line of Ali Dibadj from Bernstein Research.

Ali Dibadj

Analyst, Sanford C. Bernstein & Co. LLC

Q

Hey, guys. I have a few questions just about your momentum and just to get a sense of whether that can continue. And really along two dimensions, one is I want to get underneath what's happening between your strong topline guidance for next year and your, at least, less than consensus EPS growth. And I guess taxes; your tax rate is changing and all that. But what's your like-for-like EBIT margin percentage going to change? There's a concern among investors that, yes, you're growing, but you're buying your growth. And in fact, your investments will have to continue to increase, whether it'd be on M•A•C or channel shifts. [indiscernible] (00:58:13) you shouldn't be doing, it's just that your margin is going to be under pressure as you invest a lot more. So, that's one part of momentum.

And the second one is it you feed anything at all to temper the enthusiasm of the Chinese consumers globally, obviously big part of your topline and your margin mix across travel retail and Asia Pacific? I mean, we certainly heard some companies voicing some very, very recent like past couple of weeks worry about the Chinese consumer getting a little bit more concerned around trade wars, everything else impacting their businesses. So thanks for those two on momentum.

Fabrizio Freda

President, Chief Executive Officer & Director, Estee Lauder Cos., Inc.

A

Yeah. Let me start just the overall on the first and Tracey will give you also her specifics. We are really committed to the 50 points of margin growth in the next years. And all what we see we will deliver this. There are impacts on taxes, accounting, currencies, and we're managing through this. And I hope you realize we are trying to put it on the table in the most transparent possible way the assumptions that we are taking in managing the complex amounts of restatement.

But as far as the ongoing business, the combination of Leading Beauty Forward programs together with the margin accretive aspects of many of the new channels and markets, in which we are expanding, should guarantee us to continue increasing half margin points and invest in growth at the same time.

To be clear, the promotional discounting as a percentage of sales is going dramatically down. So, our investment is all about brand equity building and we have gone for a few brands that we advertised, with 30 brands in our portfolio advertised. So, creating the power of long-term growth in the new kind of channels that we are addressing. So, to be clear, this wing of channels goes with this wing of support with the consumers. And they go hand in hand and are providing us a stronger engine of growth than in the past. And as I said, thanks to the other element of margin, the 50% margin.

Tracey, if you want to add?

Tracey Thomas Travis

Executive Vice President & Chief Financial Officer, Estee Lauder Cos., Inc.

A

No, I think you've answered it well. So – if you, Ali, think about fiscal 2018, we actually delivered 70 basis points of organic margin expansion. So, we did have positive currency benefit of 40 basis points, the acquisitions did suppress our margin by about 20 basis points. So, when you look at all of those factors, we delivered about 50 basis points organic operating margin in line with our objectives.

So, to Fabrizio's point, on average, our model suggest that we can comfortably deliver 50 basis points on average of margin expansion – operating margin expansion and continue to invest in all of our growth areas. That certainly is enabled by Leading Beauty Forward and some of the work that we're doing under that program over the next few years.

Fabrizio Freda

President, Chief Executive Officer & Director, Estee Lauder Cos., Inc.

A

On China, today, we do not see a sign of slowdown of Chinese consumer [ph] in Too Faced (01:01:52) out there – neither in China Mainland, nor in the travelling corridors that we are monitoring. So, however, we want to clarify that the assumptions in our guidance for the year assume a certain level of normalization of the growth of China and travel retail in the rest of the fiscal.

But in term of the power of the long-term opportunity, I remain completely convinced that China market has the potential of a double-digit growth year-after-year, because the fundamentals drivers are not changing, the rising of the middle class, the love of luxury and beauty particularly, the ability of the online execution in China to serve the 650 cities where we do not have physical distribution and the ability to have our physical distribution designed in the most productive way of the world with the super high productivity, because only focus on high traffic areas and the rest is served by online.

So, that model is extremely powerful and has long-term potential. Now, may it go to up or down, so depending on the overall economy trend in the U.S. or other potential thing impacting in the short-term obviously, yes. That's why, we are assuming a certain normalization next fiscal year, but this remains one of the biggest long-term opportunities in front of our company in my opinion.

Operator: Our next question comes from line of Caroline Levy with Macquarie.

Caroline Levy

Analyst, Macquarie Capital (USA), Inc.

Q

Good morning. Congrats on an amazing year. I would like to just get your assumptions for what's going to happen in the European department store environments in fiscal 2019? And maybe even longer term, it looks like the UK is facing a bankruptcy today. I don't even know if it's a chain that you're operating in? But do you see it going the way of the U.S. and are you prepared for that in the way that you've done your projections? And maybe just fill us in on how it might be different from what we've seen in the U.S. please?

Fabrizio Freda

President, Chief Executive Officer & Director, Estee Lauder Cos., Inc.

Q

Yeah. First of all, what is very different from what we have seen in the U.S. is the penetration of department stores in Europe. So, if you mean UK – I'll talk to UK in a second, but in Western Europe, the penetration of department stores is very, very limited. So, the amount of selling square meters per person, are really completely different. So, the impact in Europe, even if there was the same [ph] worrying trend (01:04:45) that we have seen in the last years in the brick-and-mortar retail in the U.S., it will not have anywhere a similar impact.

The other thing is that the – frankly, the online penetration in Western Europe is significantly lower than the one that is in the U.S. and so the ability of moving sales online in Western Europe for the moment has been inferior, and because of that the brick-and-mortar is more solid and less exposed to sudden changes in this area.

As far as the UK is concerned, there are some department stores, which have been affected by crisis House of Fraser is the most significant one. And we are monitoring the consequence. We are in House of Fraser. For perspective, in proportion to the U.S. is that the comparison you are making, House of Fraser is less than 10% of our UK business and is more – in proportion is what Bon-Ton was for the U.S. But there is – for the moment, we don't have signs that this retailer will close. Actually, we have sign that will be restated and some doors we've closed that will be rationalized for a business that could be even stronger after this rationalization.

But in the UK, the same thing is happening. Meaning sales are going to the luxury part. They are growing more in the online area – or the online channels. And so the mitigating factor, we are doing so much earlier and better in online there that obviously this is compensating. The other part which is more specific to Estée Lauder is that don't forget that in the UK, we have [ph] boots (01:06:43), which is a significant percentage of our business, and so our business in UK is less concentrated in department stores.

Operator: Our next question comes from line of Steve Powers with Deutsche Bank.

Stephen Powers

Analyst, Deutsche Bank Securities, Inc.

Q

Yeah. [indiscernible] (01:07:01) can you hear me?

Tracey Thomas Travis

Executive Vice President & Chief Financial Officer, Estee Lauder Cos., Inc.

A

Yeah.

Stephen Powers

Analyst, Deutsche Bank Securities, Inc.

Q

Okay, great. Hey. So, first just to cleanup on the guidance, Tracey, and then a longer term question. The first one is just, can you talk a little bit more about why the revenue recognition change had a \$0.10 impact this year? Is that something you'd get back in 2020 or is that more a permanent step down or catch up from where you ended 2018? That's the cleanup question.

And then thinking more, I guess, strategically, Fabrizio, I wondered if you could just expand more on what you see as opportunity in emerging market outside of China. Clearly, in fiscal 2019, [indiscernible] (01:07:41) tell with a significant amount of macroeconomic volatility, but even with that I think your guidance implies opportunities for growth in that block of markets.

And as you think about your 10-year compass recognizing the importance of the markets like the U.S. and Western Europe and China, I'm just curious as to your expectations for other emerging markets as a driver of growth for Estée Lauder? Thanks.

Tracey Thomas Travis

Executive Vice President & Chief Financial Officer, Estee Lauder Cos., Inc.

A

Okay. So as it relates to revenue recognition and the \$0.10 of EPS impact, it is an accounting and reporting issue only. It is a shift in terms of when we can recognize revenue relative to our promotional programs. So it requires us to defer a portion of our revenue until certain promotional activities have occurred, which is different than how we were accounting for it in the past.

So it is a shift forward and we would expect though being under this guidance. Next year will be comparable, but it will also shift some revenue forward. But at least fiscal 2020 and fiscal 2019 will be comparable. Our commercial activities will not be impacted. There is no change to our shipping patterns or to actually the timing of promotional activities. Just – and the spend related to those activities will not change as well. It's just the recognition of revenue, so it is a shift.

Fabrizio Freda

President, Chief Executive Officer & Director, Estee Lauder Cos., Inc.

A

And as far as emerging markets, we really believe that emerging markets will continue to be a driver of growth. However, emerging markets are by definition more volatile. And that's why we look at it as a portfolio where we have several emerging markets. We are building in each one of them at different speed. And with the flexibility of allocating resources every year to the one that represents the best opportunity, not only growth but also return on investments.

So its portfolio markets where we use enormous amount of flexibility depending on the situation with clear long-term goals to have strong market share in each one of them in the medium-term. So today, we have reached already 15% of our business. As we said before, growing 24%, we expect this to continue.

In the next year [ph] what (01:10:02) we have in mind is that we see continuous accelerating opportunity as exciting I should say in India where we are going all the way, in Russia in this moment is very strong. We see the opportunity next year to stabilize Middle East that has been a drag to our overall portfolio and we see the opportunity to restart growth in Brazil.

Obviously, we are waiting to see the elections in October/November. But that could be a great opportunity if this comes. We expect to continue success in Mexico and in other areas where we are doing really, really well, and amplify the portfolio in new markets in Asia, like the Philippines, Indonesia where we are seeing some amazing growth in this moment and great opportunities for the future.

But as I said, there will be every year one or two of these markets, there will be an issue and one or two that will be in those areas a tremendous opportunity. So you should see us as having the flexibility to direct our investment as needed year-after-year, while we stay focused on the long-term.

Operator: Our next question comes from the line of Olivia Tong with Bank of America Merrill Lynch.

Olivia Tong

Analyst, Bank of America Merrill Lynch

Q

Good morning. Thanks. First, I was wondering if you could give a little bit more detail on the investments that you're doing in M•A•C in North America, and then talk about what your profit expectations are for 2019 in the U.S. But more broadly, the U.S. has obviously been a struggle for sometime and I know you're not interested in expanding it to the largest online provider. But where is the line on the sand on incremental retail expansion beyond like the Ulta and Sephoras and such? I mean, would you consider partnering with other retailers potentially specialty apparel or other ones to sort of spur activity in your home market? Thank you.

Tracey Thomas Travis

Executive Vice President & Chief Financial Officer, Estee Lauder Cos., Inc.

A

So, Olivia, I'll start. In terms of M•A•C, as you're aware, we have expanded M•A•C in Ulta. It's doing quite well. We will look for further expansion there. The brand is doing quite a bit as well in terms of their social media programs to improve the productivity per door of the business here in the U.S.

And as it relates to specialty and whether or not we would partner with a specialty retailer, I mean certainly the M•A•C brand has done that in the UK with ASOS. If there were one here that had the same type of characteristics that we look for in terms of a third-party presence for our brands online, then we would consider that as well. But there's a tremendous amount going on with the M•A•C brand in terms of everything from in-store experience to driving their online business more and certainly other considerations.

Fabrizio Freda

President, Chief Executive Officer & Director, Estee Lauder Cos., Inc.

A

And again, I want to add just innovation. So M•A•C is working on innovation in the U.S. It's working on improved digitalization in the U.S. So it's not only a distribution swing. It's not only an improvement in distribution. It's an improvement in every single aspect of the brand that we are working on and we believe will deliver results. In terms of which retailers to partner with, frankly in this moment, in the U.S. we're really focused on growing same door in the best possible way.

It is a matter of – as I said, with the new sales force, with much more attention to consumer-facing activities, we can improve our activity in stores on all fronts and we can support our current retail partners to deliver much more from our brands and continue the online expansion where we are doing fantastic in the U.S. And the current model of brand.com and retail.com is working very well [indiscernible] (01:14:02) third-party platforms of high quality, we'll definitely consider them.

And with that strategy, the Lauder brand, if you heard the presentation of Stéphane, is exactly the strategy the Lauder brand is following in the U.S. as Stéphane just explained what great results the brand had. Maybe Stéphane, you want to clarify that again?

Stéphane de la Faverie

Global Brand President, Estée Lauder, Estee Lauder Cos., Inc.

A

Yeah. Absolutely, Fabrizio. I think like in the U.S. – like we mentioned in introduction, I think we've seen now a sustainable turnaround of the brand and actually we see our like-for-like growth in store being actually super than our overall growth. So basically the half and the renovation that [ph] we've put on our top (01:14:42), the shift of distribution for accelerated like fast-growing channel has actually proven that today there is a sustainable growth without necessarily needed today to increase distribution. But like Tracey said, if opportunity comes, then we will explore them.

Operator: Our next question comes from the line of Jason English with Goldman Sachs.

Jason English

Analyst, Goldman Sachs & Co. LLC

Q

Hey. Good morning, folks. Thank you for squeezing me in. I guess I wanted to follow-up on Olivia's question around the Americas profitability, because maybe I missed it, you addressed that. The margins have clearly come under a lot of pressure. You mentioned that this year you had some of the corporate expense allocation, which was a headwind, particularly in the fourth quarter. Can you quantify that to give us an underlying read for the business?

And then thinking on the forward, we've got growth in online. We've got growth in specialty-multi. But it seems like that's going to be balanced to potentially more than offset by deleveraging your own freestanding stores, department stores. Is there a path to margin recovery that will get you back in sort of the historical high-single-digit range, or is this sort of permanently rebased or even worse, is there a glide path where it can continue to be pressured on the forward?

Tracey Thomas Travis

Executive Vice President & Chief Financial Officer, Estee Lauder Cos., Inc.

A

So, I'll start, Jason. In terms of – the North America team has done a terrific job in terms of recognizing the retail environment and the declining traffic as well as, as Fabrizio said, the door closures that we've experienced in the U.S. with right-sizing and resizing the business in order to stabilize margin and then start to improve margins. So in the fourth quarter, the bulk of the decline was related to corporate expenses. And the North America business was relatively flat in terms of profit.

In terms of what we expect going forward, we do expect – as I said, we do expect North America to deliver or the Americas to deliver low-single-digit growth. So we do expect North America as well to deliver low-single-digit growth. And with some of the continuing work that they're doing as it relates to executing some of the Leading Beauty Forward initiatives and some of the other programs that they're working on to really improve door productivity in the remaining doors and certainly the top doors in the U.S., we do expect to start to see margin recovery in the Americas and in North America for sure.

Fabrizio Freda

President, Chief Executive Officer & Director, Estee Lauder Cos., Inc.

A

Yeah. And in term of the balance of the distribution, the question there is this year and I said it in my prepared remarks, the scale is changing in our favor. So this has been – fiscal year 2018 has been the first year where the extra sales we've built in fast-growing channels were superior to the sales we lost in brick-and-mortar department stores and freestanding stores. So that's the key thing that happened. So if you exclude the impact of the very big

door closures from the year, as I explained, \$164 million over two years, \$68 million of Bon-Ton in fiscal year 2018, if you exclude these closures, the scale is in our favor.

I mean, we have now the right platform of distribution to grow same doors in the correct way for the future. So a lot will be about the power of our innovation, the power of our investment in media, the power of get interaction from the brand. And then, keep in mind that the door closures also were pretty good in maintaining the consumption on our brands even when the door closed. However, there is a transition period when door closed where this has to happen that can have a short-term impact on sales, it happened already in fiscal year 2018.

Operator: Our next question comes from the line of Lauren Lieberman with Barclays.

Lauren R. Lieberman

Analyst, Barclays Capital, Inc.

Great. Thanks. Good morning.

Q

Tracey Thomas Travis

Executive Vice President & Chief Financial Officer, Estee Lauder Cos., Inc.

Good morning.

A

Fabrizio Freda

President, Chief Executive Officer & Director, Estee Lauder Cos., Inc.

Good morning.

A

Lauren R. Lieberman

Analyst, Barclays Capital, Inc.

I was wondering if you can talk a little bit about Clinique, and some of the metrics you [indiscernible] (01:19:05) Estée Lauder and M•A•C in terms of their – those brands' performance in some of the stronger doors. So, if you were to look at Clinique I guess particularly in the U.S., and if it's possible sort of exclude the departments – the brick-and-mortar department store channel, are you seeing any sort of positive encouraging signs on Clinique? How it's resonating with different consumer demographics or cohorts in terms of age group? I know you mentioned Moisture Surge, but any other franchises, how they are – how they have been doing? Thanks.

Q

Fabrizio Freda

President, Chief Executive Officer & Director, Estee Lauder Cos., Inc.

Yeah. Okay. Tracey indicates I should answer this one.

A

Tracey Thomas Travis

Executive Vice President & Chief Financial Officer, Estee Lauder Cos., Inc.

I won't. I mean, no, I can answer. I mean, Clinique is doing incredibly well in Ulta, it's doing very well online. So in the U.S., Clinique, we are certainly starting to see, as you indicate Lauren, a pick up outside of the department store channel. The innovation this year and certainly heading into next year is quite strong. So we're quite excited about what we've seen thus far from Clinique.

A

Moisture Surge, they continue to innovate under that franchise. It's doing very well. Dramatically Different, which is their legacy franchise, they introduced a new jelly product which is my daughter's particularly fond of. So that too is doing quite well. And their Fresh Pressed franchise is also doing well.

So they've got a lot of great skin care heading – innovation heading into next year and they've got some exciting new innovation that will let the brand announce and tell you about going forward. So we're very encouraged by the signs that we see from Clinique this year. And again, as Stéphane indicated, we certainly have the track record for having a large brand resume growth in North America and in the U.S. even with the current environment.

Fabrizio Freda

President, Chief Executive Officer & Director, Estee Lauder Cos., Inc.

A

Yeah. And I just want to add I'm really passionate about the work that Clinique is doing at this moment. I think we will see Clinique results in North America in the next years getting better and better. The innovation, as Tracey said, is really promising in my opinion, particularly the skin care innovation.

And also I want to remind that Clinique is the most affected of all our brands to these closures. So the results of Clinique, being able to grow retail in the last quarter in North America in presence of Bon-Ton since April basically not taking shipments and not working and in the closures of what happened in Sears in Canada in the previous period and in other doors closures. So Clinique has been able to offset all of this and stabilize or grow depending by category in a way that as soon as this negative will moderate, we will see the power of Clinique acceleration.

Operator: Our next question comes from the line of Steve Strycula with UBS.

Steven Strycula

Analyst, UBS Securities LLC

Q

Hi. Good morning. Few questions on China. I wanted to – first of all, Tracey give us context as to how large China is. I know it's growing very rapidly. [ph] Is it around (01:22:19) 9%, 10% of company sales? And what it did grow in fiscal 2018? And then I have a follow-up. Thanks.

Tracey Thomas Travis

Executive Vice President & Chief Financial Officer, Estee Lauder Cos., Inc.

A

Okay. So you are spot on, China is about 9% – little over 9% of our sales now with the results that we saw in terms of China growth. We don't comment on individual country growth. But rest assured that China grew very, very, very strong double-digits in fiscal 2018, so great performance in China.

Steven Strycula

Analyst, UBS Securities LLC

Q

Okay. And then a follow-up for Fabrizio, just wanted to understand, it sounds like you're getting a lot of incremental consumers across China even with Tmall's presence. Can you give us a sense as to how Tmall's – your ramp on that platform has impacted different tiers of cities like Tier 1, Tier 2 versus Tier 3 and Tier 4? And how if at all has it impacted department store sales within Greater China? Thank you.

Fabrizio Freda

President, Chief Executive Officer & Director, Estee Lauder Cos., Inc.

A

Yeah. The [ph] growth of (01:23:24) China has been extraordinary like doors. And so our department store in China have, as we speak, the strongest like door growth they have had in the last 10 years. So Tmall in that sense is not negatively impacting the department store growth.

The reason for that is that, as you indicated, we are in about 118 cities with our physical distribution in China today across all our brands. Obviously, 118 is the number of Lauder that other brands much less when you go to brands like M•A•C or others we're still in – I think around 50 or whatever, 60 cities. So there is an enormous amount of physical distribution opportunity within the top 100, and let's say, 120, 150 cities of China.

But the Tmall reached 650 cities. And from the data we see, the large majority of our sales in this area come from the cities where we do not have physical distribution. And that is a very efficient model because the physical distribution in the 118 cities is very efficient because the productivity per door is high and growing, and the new consumers in the city where physical distribution is not yet there or where the level of productivity will not justify physical distribution for the time being can access the brands via Tmall or via brand.com. This model is working and creates this increase of consumers in a very efficient way and also with reasonable capital cost.

Operator: Our final question comes from Dana Telsey with Telsey Advisory Group.

Dana Lauren Telsey
Analyst, Telsey Advisory Group LLC

Q

Thank you. Stéphane, just wanted to touch on, as you think about the Estée Lauder brand and the improvement that it's made, how do you think about the distribution channels for this business? What should it ultimately be and how do you see the margin opportunities? Thank you.

Stéphane de la Faverie
Global Brand President, Estée Lauder, Estee Lauder Cos., Inc.

A

Thank you. Thank you for your question. I think what I was trying to highlight in the presentation that we had is we've been able to have this amazing growth without increasing distribution. We have some shift of distribution in some areas of the world, but we really believe that today [indiscernible] (01:25:57) growth is coming from on one side strengthening our position in the existing distribution, specially focusing on all our flagship doors around the world, but at the same time making sure that we serve the consumer in the fast-growing channel like specialty-multi, online and travel retail. And we really believe that this new distribution that is growing faster than the average is really helping us today to increase the desirability and the equity of the brand overall in the world.

So today, the opportunity is in front of us. The Estée Lauder brand is basically like building on all this opportunity and really believe, again, that makes the model a very sustainable and profitable model actually for the company going forward. And the most exciting things should pass for all big brands actually to be able to just like apply the same strategy and to grow like that globally.

Fabrizio Freda
President, Chief Executive Officer & Director, Estee Lauder Cos., Inc.

A

And I just wanted to underline that being able to grow 22% without increase distribution, since our profitability is a lot influenced by same door sales, that obviously speaks highly for the ability of the Lauder brand to continue improving profitability.

Operator: That concludes today's question-and-answer session. If you were unable to join the entire call, a playback will be available at 1:00 PM Eastern Time today through September 3. To hear the recording of the call, please dial 855-859-2056, passcode number 10665254. That concludes today's Estée Lauder conference call. I would like to thank you all for your participation and wish you all a good day.

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