Q1 2022 Earnings Call

Company Participants

- Laurent Mercier, Chief Financial Officer
- Sue Y. Nabi, Chief Executive Officer

Other Participants

- Andrea Teixeira
- Carla Casella
- Lauren Lieberman
- Olivia Tong
- Robert Ottenstein
- Stephanie Wissink
- Steve Powers

Presentation

Operator

Good morning, ladies and gentlemen. My name is Brittany and I will be (Technical Difficulty). At this time I would like to welcome everyone to Coty's First Quarter Fiscal 2022 Results Conference Call. As a reminder, this conference call is being recorded today, November 8, 2021.

On today's call are Sue Nabi, Chief Executive Officer; and Laurent Mercier, Chief Financial Officer. I would like to remind you that many of the comments today may contain forward-looking statements. Please refer to Coty's earnings release and reports filed with the SEC where the company lists factors that could cause actual results to differ materially from these forward-looking statements. In addition, except where noted, the discussion of Coty's financial results and Coty's expectations reflect certain adjustments as specified in the non-GAAP financial measures section of the company's release.

I will now turn the call over to Ms.Nabi.

Sue Y. Nabi {BIO 21845588 <GO>}

Ladies and gentlemen, with our Q1 now complete and very encouraged by the success we are having further building on the strong foundation we put in place last year. The results we have delivered this quarter truly exemplify the virtuous cycle that we have set out to create. In essence it's a simple one where strong revenue growth combined with gross margin and cost initiatives simultaneously fuel profit expansion and strategic reinvestments, which in turn drive future growth momentum.

There are some key takeaways that I would like to first highlight. First, our Q1 revenue growth surpassed our expectations and guidance with growth coming from both our prestige and consumer beauty segments. We continue to see very strong demand for prestige products particularly because of these fragrances in the US and China with an impressive rebound in travel retail, this was further supported by our exceptional lineup of fragrance launches. Meanwhile, we continue to see a recovery and improvement in consumer beauty with particularly strong trends as at both CoverGirl and Max Factor.

This resulted in like-for-like revenue growth of 21% above our guidance of high-teens growth. Second, we reported very strong profit growth during the quarter this was fueled by a significant gross margin expansion of nearly 500 basis points as well as further cost reductions. Substantial growth margin expansion we have seen is a true testament to the strength of our business model as we double-down on accretive innovation and continue to premiumize our portfolio. Importantly, we continue to step up our investments in marketing. In fact, our working media doubled versus last year. Despite this, our adjusted EBITDA increased almost 70%, equating to 550 basis points of margin expansion, evidence that our virtuous circle is now in motion.

Third, we continue to execute and make progress across our strategic growth pillars. I would, of course be sharing some milestones with you today. However I am even more so excited for our Investor Day next week, when I will be joined by additional members of the Coty leadership team to provide and more in-depth update on the progress we have made on our strategic pillars, as well as our medium term trajectory.

Four, we see the momentum continuing into the year. We are on track for a great fiscal 22. Our growing confidence in the momentum drives our increased sales guidance for the year supported in particular by our initiatives across fragrance and cosmetics. Our nature -- I will now take a few moments to cover our revenue trends during the quarter before Laurent takes you through our financials. Then I will finish with an update on our strategic progress and our outlook.

Our Q1 revenues increased 21% Like-for-like. The Prestige segment grew 34% on a like-for-like basis even as we continue to reduce sales in low quality channels which represented a low single-digit negative impact in the quarter. We continue to experience very robust prestige fragrance trends, particularly in the US, China and Travel Retail with nearly all brands exhibiting strong growth in the quarter.

Our growth was further aided by our very strong launch calendar in the first quarter. This included Gucci Flora, Gorgeous Gardenia, Burberry Hero, Calvin Klein, Defy and the relaunch of Kylie cosmetics. Meanwhile, our prestige cosmetic sales more than doubled in the quarter. Our consumer beauty segment increased 3% like-for-like as the global mass beauty category returned to growth and we are seeing stabilization in our market share. Q1 growth was led by CoverGirl and Max Factor as both brands continue to benefit from the new brand positionings.

Moving to sales by region. We (inaudible) across all regions though the U.S. and China continued to be standout performers and travel retail saw a reversions. The Americas region grew 23% like-for-like in the quarter supported by double-digit growth in the U.S. as well as growth contribution from Latin America, Canada and Brazil. EMEA sales rose 17% like-for-like with the most impactful contributors be in the UK, Russia as well as local travel retail. The Asia-Pacific region increased 29% like-for-like with local travel retail tripling year-on-year and China seeing nearly 50% growth in the quarter proving our efforts in turning this market into a powerhouse are bearing fruits. We are particularly pleased with this results in China and the broader market, particularly given some incremental restrictions that occurred in the quarter due to COVID.

I will now hand the call over to Laurent to take you through our financial results.

Laurent Mercier {BIO 22079608 <GO>}

Thank you, Sue. I am very pleased with our first quarter results, which continued our very strong pace of profit growth. Importantly, our virtuous cycle of growth is now in motion, our profit was driven by strong gross margin improvement allowing us to continue to reinvest in our strategic growth initiatives, thereby further fueling top-line growth momentum.

Starting with our gross margin performance. Our Q1 adjusted gross margin of 53.4% increased by nearly 500 basis points from last year and 250 basis point from last quarter. This marks of third consecutive quarter of gross margin above 60%. Our gross margin performance was driven by favorable mix both from the outside growth of Prestige, as well as favorable product mix within the category. Lower excess and obsolescence, fixed costs absorption on the increased sales, pricing and revenue management, supply chain, productivity and material cost reduction program.

We continue to be very focused on further driving gross margin expansion both this year and in the years to come. As such we have a very clear multi-pronged multi-year gross margin attack plan in place, while we also expect we will continue to benefit from positive channel category and regional mix shifts. In gross margin expansion it's key towards the virtuous cycle we have created of sales and profit goals.

While the topic of inflationary pressure supply chain bottlenecks, and component shortages of dominating conversations across all industry, I am pleased to say that so far Coty is navigating through these uncertain environment quite well. This is a result of both the agility of our supply chain and procurement teams as well as the structure and drivers of our business model where we are over driving gross margin quality channels categories and innovation. While we have seen isolated constraints in certain components such as fragrance brands, silicon and paper of things proactively increased safety stocks to protect our key consumption periods as well as implemented dual sourcing initiatives all of which is proving to be effective.

On freight the vast majority of our freight is under contract rather than spot market, which has largely protected us from the excessive price hikes of recent months. At the same time of teams proactively increase Transportation lead time and secured freight capacity in advance to avoid potential freight constraints. And in the context of global supply chain bottlenecks and port congestion it is important to note that the majority of our inventory is manufactured in the region when where it is sold, which likewise protects our business. The net result of all these proactive efforts and business design decisions is that of service level in Q1 was very strong in the mid-90s and actually higher than the prior year which has allowed us to both over deliver on our sales guidance for the quarter, and deliver close to 500 basis point of gross margin expansion year-on-year.

And our outlook for Q2 service levels is in a similar range, despite higher than initially anticipated demand, which is also enabling us to raise our full year sales guidance. While we do expect the impacts from inflation, material and freight to be somewhat higher in H2 '22, the impact is quite manageable and we continue to expect our gross margin to expand in fiscal year 22 fueled by revenue management initiatives in both Prestige and Consumer Beauty. So, mix benefit of Prestige expanding as a precaution of the mix, improved absorption from higher production volumes and broader productivity efforts.

During Q1, we maintained our step-up marketing investment. A&CP was approximately 26% of sales, consistent with the level of Q4 and significantly above the 20% level a year ago. The year-over-year increase was primarily driven by working media, which more than doubled year-on-year. Importantly, we remain vigilant in investing in the highest ROI opportunity and being nimble in our resource deployment. You will hear more from Sue regarding the details of our success and progress in driving growth during the quarter.

However, let me highlight a few areas where we were putting our marketing dollars during the quarter. First we had a very busy launch calendar on the quarter, particularly within Prestige. We launched Gucci Flora, Gorgeous Gardenia, Burberry Hero, Calvin Klein Defy and the relaunch of Kylie Cosmetics among others. These launches showed tremendous success in the quarter and contributed to our strong performance. We continue to fuel our expansion into new categories and markets including prestige makeup in overall Asia. Finally, we continue to invest behind the repositioning of CoverGirl, Rimmel and Max Factor, which also promising results supporting consumer beauty business stabilization.

We continue to (inaudible) our marketing investment and drive profit growth through further cost reduction. During Q1 our fixed cost declined by 8% year-over-year. We achieved approximately 60 million of cost saving during the quarter with a front loaded delivery of our fiscal 22 savings target to enable sufficient flexibility in the P&L to deliver profit yet reinvest in our brand during this critical holiday period.

The primary drivers of these were, cost savings, lower fixed cost, and trade investments. We remain well on track to achieve over 90 million of savings in fiscal 22, recall this is net of cost inflation, reinstating bonuses, and structural organizational reinvestment behind our growth pillars. So it's important to note that these does not include our intended reinvestment A&CP. We have now achieved nearly $400 million of total savings and will remain well on track to reach our fiscal 23 target of a total of $600 million of savings, while we also continue to identify savings projects beyond fiscal 23.

Moving to profit delivery in Q1. Our adjusted EBITDA performance was exceptionally strong in the quarter, increasing 67% year-over-year to $279 million. This resulted in a margin of over 20%, up 550 basis points above our first quarter last year. This significant improvement was driven by strong sales growth, robust gross margin expansion and fixed cost leverage. We believe, the stellar performance this quarter is further evidence of the strength of both our strategy and business model, and we continue to target both revenue and profitability growth in the years ahead.

Turning now to our EPS, which included the following drivers. Adjusted EBITDA for Q1 of $279 million, depreciation of $78 million, income tax expense of $40 million which equates to a tax rate of approximately 29% in line with our expectations. As we previously noted, we expect a higher tax rate this year given our global principal jurisdictions allow now in Amsterdam and in US, $8 million of other item and $29 million of adjusted preferred dividends.

Please note that the preferred dividends were higher than typical in Q1, at a very high level despite due to accounting rule requirements associated with KKR conversions of accrued dividends into common shares as part of their first transaction in September. As a result, our Q1 diluted adjusted EPS and deduct $0.08. While not included in our adjusted EPS during the quarters, the Wella fair market value rose by $390 million. Looking ahead to Q2 and fiscal 22 I would like to provide some context of the different drivers of our adjusted EPS.

First, consistent with what I said last quarter, we continue to expect interest expense in the mid $200 million for fiscal 22 reflecting a lower net debt balance offset by somewhat higher cost of debt post the recent refinancing. Second as I previously mentioned we anticipate an adjusted effective tax rate tax rate of fiscal 22 in the high 20%. However, we know there is a high degree of uncertainty with effective tax rate projections in the current environment. Third, on the preferred dividends, following today's announcement actions with KKR, we anticipate a roughly $7 million quarterly run rate going forward following this transaction and assuming no further conversion of preferred shares.

Now, moving to free cash flow for the quarter, which was totally positive despite Q1 typically being seasonally weaker cash flow quarter as we build inventory for the key holiday consumption period. Importantly, working capital improved significantly in the quarter. We also continued strict management of CapEx and one-time cost. As a result, our Q1 free cash flow was 241 million. As we head into Q2 and beyond, we remain intent on further bolstering up cash flow as well as driving a steady reduction in our net debt.

Turning to our capital structure. When the Q1 with a financial net depth balance of approximately $4.96 billion which is a decrease of over $200 million from Q4. This is largely the result of our strong free cash flow. Factoring our 40% stake of Wella at quarter end valued at approximately $1.65 billion we ended the quarter with economic net debt of around $3.3 billion.

Please note that with the completion of the sale of an approximate 9% stake of Wella to KKR in October and today's announced sale of an over 4% we now own 26% of the Wella business. Based on our current ownership stake in Wella or economic net debt that at the end of Q1 '22 would have been closer to $3.9 billion. We continue to view our retain 26% stake in Wella as a financial stake. The recent transactions proves the valuation upside in this business as well as the liquidity of the stage. We will continue to be active and tactical in identifying opportunities to monetize this non strategies Wella assets and further reduced leverage.

Additionally, we are continuing to make progress in improving the maturity profile of our debt. We have secured commitments to extend our revolver maturity to fiscal '25, and reduce revolver capacity to $2 billion from previous $2.75 billion. This is on the back of our recent successful issuance of over 1.6 billion of senior secure notes, showing our strong progress in minimizing debt refinancing race. In fact, we have recently made some tactical decisions by monetizing some non-core assets to help further our deleveraging.

During Q2, we are executing several real estate divestiture resulting in approximately $150 million of cash proceeds so majority of which will flow in Q2. The sizable cash inflow for these transactions coupled with expected strong free cash flow in Q1, reaffirm our confidence in ending calendar year of 21 with financial net debt to EBITDA towards 5x as well to end calendar 22 with leverage of 4x. In the meantime, we remain committed to the partial IPO of our Brazil business. In light of the current economic volatility in Brazil we continue to monitor the market conditions to identify an opportune window to execute our partial IPO. Due to local Brazilian regulation we cannot offer further details at this time.

Before I hand the call back to Sue, I would like to quickly touch on the recent transactions regarding our preferred share and the simplification effect they're having on our capital structure. For some time now we have seen shrinking [ph] to further and looking shareholder value at Coty. Growing up sales and profit get averaging our balance sheet and the last being simplifying of capital structure. We have made great progress with (inaudible) and had a key effects [ph] towards further improvement.

During the first half of this year, our capital structure has become significantly more simplified to take care of conversion of approximately 50 million preferred shares combined with the subsequent redemption we have two transactions of around 75 million KKR preferred shares in exchange for roughly 14% stake in (inaudible). Make no mistake, these are positive developments for Coty.

We understand these events, particularly the secondary offering that took place in early September led to questions and volatility. However, these developments were a net positive for Coty, as well as for our shareholders including significant even further reduce the other hand of KKR preferred shares ownership. Confirmation of the significantly higher value of Wella, we have approximately 40% appreciation versus initial valuation while also proving the liquidity of the asset.

Freeing approximately $65 million of cash on the lower preferred dividend that we can use to further reinvest behind brand or use to work deleveraging. And the redemption of these convertible shares implied several cents of EPS accretion annually.

Let me now turn it back to Sue.

Sue Y. Nabi {BIO 21845588 <GO>}

Thank you very much for Laurent. So we continue to make strong tangible progress across our six strategic pillars in the first quarter with many more milestones plan for fiscal 22 and beyond. I will now, walk you through some of the key costs Laurent highlights and as a reminder, we will be covering each of these pillars and future initiatives in much greater detail next week November 18 at our Investor Day in New York City.

Starting with our first strategic pillar, stabilizing our consumer beauty brands. This is a pyramid we hope many of you recognized however, we believe it's important to remind each of you of our core consumer beauty brands and where they stand. I'm proud to say that we have a clarified view of the portfolio with each brand positioned in a clear priced year and competing against a defined competitive brand. CoverGirl, Rimmel and the Corollary Germany, the Manhattan brand compete directly against Maybelline, Max Factor and Bourjois compete against L'Oreal Paris, and Sally Hansen holds the unique position of providing an affordable alternative to nail, salon services.

As you all know, CoverGirl has been our first area of focus within Consumer Beauty, and I'm very pleased with the success we are seeing today. CoverGirl is the inventor of skin makeup and reach this high growth area in the U.S., which is nicely accretive to our cosmetics' portfolio. This has been supported by our strong launch Kind & Free range of [ph] clean, vegan and cruelty free beauty products, including Clean Fresh Makeup and Lash Blast Clean Mascara. In fact, we believe this renewed focus on Clean Makeup is further supporting our gains with key demographics as well as key retail partners such as Ulta with elevating CoverGirl as a leading example of an established mass brand leading the path to Clean Beauty.

I also want to note that Clean Beauty has the additional benefit of being margin accretive with these key innovations carrying a higher price point. I'm proud to say that since our reboot of CoverGirl at the end of March, the brand has gained market share in four of the last seven months and we expect the momentum to continue.

Importantly, CoverGirl is finally gaining shelf-space in the total -- in total in the US, led by a Kylie Clairol where the brand is significantly outperforming the cosmetics category and also improving productivity. And just as we discussed during our strategic update in April, we are reapplying the CoverGirl turnaround playbook to other consumer beauty cosmetics brands. We just launched our first clean makeup brands that Rimmel's called Kind and Free. This makeup line is 100% vegan, cruelty free, free from fragrance, mineral oils, and animal derived ingredients. On this slide you can see a brief add showcasing the manifesto of this recent launch.

(Audio-Video Presentation).

Kind & Free is our biggest consumer beauty launched in fiscal 22. Along with our retail partners we believe this will truly be a game-changing Innovation and we have been very excited with the recent test results. While Kind & Free is still only in pre-launch phase with a full national rollout and full media support going live in Jan, we are already beginning to see retail sales at key retailers picking up in recent weeks. For Max Factor, we are seeing very positive trends as the visuals and new assets have now gone live. Starting in the UK, Max Factor gained 20 basis points of market share in September. Across all customers, Max Factor is stable or gaining market share, which is a first for the brand in years. Similarly in the Netherlands, the brand gained 50 basis points of share. With the new brand positioning and campaign with Priyanka Chopra Jonas only starting in a couple of months ago, we are really encouraged to see that the brand is already stable or growing market share in over 75% of its markets. We have planned to keep the momentum going in December, as we continue to invest in media behind Max Factor.

Moving to our next strategic pillar of accelerating luxury fragrances. As previously mentioned, we have some outstanding fragrance launches during the quarter, further supporting our success in this key categories. Gucci Flora, Gorgeous Gardenia is one of these great launches. Ultimately our goal is to summon [ph] this fragrance within the top 15 global female fragrance icon, and the result of recent months as across geographies, channels and customers suggest that Flora is on-track to reach this. Globally, this is a first for us, with a key innovation seeing such strong immediate success across major geographies. In the U.S. it's already ranking number one since its launch across many across many of our key US retail partners. Similarly, in the UK, the fragrance is number three among female fragrances since its launch and supporting Gucci Flora as the number eight overall female fragrance line in UK.

In two of our key markets in Continental Europe, Germany and Italy. Flora sellout is also very strong supporting the Flora line to be number 8 in Germany while Gorgeous Gardenia is the number one female fragrance in Italy. The fragrance is also gaining strong traction in China, where it has been ranking as a top 10 female fragrance among our key brick-and-mortar retail partners, as well as on Tmall.

Within men's fragrances, we launched at Burberry Hero during the first quarter while the fragrance has similarly seen great success across all key regions and the fragrance remains on track to be a global mail icon. In the U.S. Hero has been the number one men's fragrance launch at many of our key retail partners since the launch with it sale out results far exceeding our initial plans. In Italy Hero has been a top 10 men fragrance launch ensuring the hero line is the top 10 overall men's fragrance line. In Germany Hero is already at top 20s men's fragrance line. In China Hero is also now a top 10 males fragrance since launch at many of our key brick-and-mortar Retail Partners and on Tmall. It's also encouraging to see that Hero is ranking top 3 in key travel retail locations where the launch is present.

Moving on to the acceleration of our prestige make up a portfolio we relaunched Kylie Cosmetics during July together with Kylie we updated all of the cosmetic products, assuring that each product was vegan, cruelty free with clean formulations. We have been very pleased with the performance of Kylie, both across channels and geographies since this relaunch. In fact, we have had launched a numerous connections that exceeded our initial targets. During the first quarter, the vertical [ph] collection dropped, and was one of the most successful collections ever. The recently launched it A Nightmare on Elm Street collection, also turned out to be one of the best ever Kylie Cosmetics collections. Kylie also introduced her highly anticipated baby-line during the quarter. This collection saw very strong set out trends within the first moments of becoming available online leading to over delivery relative to our initial plans. Importantly, this launchers and drops brought in a very significant amount consumer who are new to the brand.

It's also important to note that with the relaunch we have made Kylie cosmetics significantly more productive than the initial range with fewer SKUs but delivering very high sellout. Success of Kylie does not stop with this recent collections, but can be further extended to the performance in brick-and-mortar both in the US and abroad in Europe.

Kylie cosmetics is performing exceptionally well in the UK at our retail partners including the recently launched at Boots. Meanwhile, the recent launch across a number of Scandinavian markets with our retail partners kicks was one of the best ever day one launchers. US brick and mortar both skin and cosmetic sellout are up strong double-digits year-over-year. All of these confirm the true omni-channel nature and global appeal of the Kylie brand.

Moving to another of our Prestige makeup brands Gucci Beauty. The growth continues to be phenomenal, our Gucci makeup sales in the quarter tripling year-on-year. At the same time, sellout in the U.S. and China continues to grow in the triple-digit trends. As we've continue to build the Gucci makeup assortment sales represents a very important opportunity for the brand.

During the quarter, we launched at the Gucci Cushion Foundation with beautiful and distinctive packaging as you can see on this slide. The launch on core Gucci Beauty in the most loyal, most profitable and largest makeup category across Asia. This has proven highly successful as in China the Cushion Foundation was one of the top-ranking luxury cushions with Tmall and other key brick and mortar retailer.

Moving to our next strategic priority of growing our skincare portfolio. Our revitalization strategy -- for Lancaster remains on track while we saw some slow down during global in Hainan due to a COVID resurgence in China as cross border restrictions eased during September we saw rebound in both traffic and of course sales. I'm also pleased to say that we are seeing a further strengthening of this skin care portfolio, which now makes up the majority of Lancaster sell out in Hainan. We view this as further evidence that the repositioning of Lancaster towards the tool [ph] selection skincare brand is checking hold on this all-important prestige skincare market.

Moving to our fourth strategic priority of building e-comm and direct-to-consumer. We continue to experience very strong growth with e-comm rising 23% year-over-year, both Prestige and Consumer Beauty saw growth exceed 20%. On the total company basis, e-commerce represented the mid-teens percent of revenue at the end of the first quarter, but from a low teens percent from last year's first quarter. One of the key e-commerce highlights during Q1 was our performance at Ulta, driven particularly by the strength we are seeing on luxury fragrances. Our Prestige fragrances sell-out growth online at Ulta rose strong double digits with penetration in the high teens. During the quarter, Marc

Jacobs' Perfect had outstanding performance. This icon was chosen as the fragrance in August (inaudible) triple-digit-sell-out growth for the month, despite lapping last year's launch. As we build on our e-commerce momentum, our multi-pronged focus on fueling growth at pure players brick-and-click and DTC is clearly very (inaudible).

Moving now to our fifth strategic priority of expanding in China. As I previously mentioned the country did some -- did see some resurgence of COVID during the quarter finally towards the end of July and August with improvements in September. I'm pleased to say that despite this mixed backdrop. Our China sales grew close to 50% in Q1 and amongst the top ten Prestige Beauty companies in China, Coty sell out was again the fastest growing. This is in part supported by the momentum of Gucci and Burberry on Tmall which led to and 7x growth in our Tmall revenues. In addition, Chloe continues to be a standout performer with a sellout doubling year-over-year led by the in (inaudible) fragrance collection at (inaudible).

This achievement is particularly notable given the limited amount of media support that we have given Chloe at (inaudible). However, we remain very committed to further building on this success to become a more significant player within extra premium and artisanal fragrances in China, as well as across the globe. That now brings me to our outlook for the year.

Starting with our view on first half fiscal 22. As we have detailed, we saw very strong prestige revenue growth in Q1 at 34 like-for-like percent growth which in particular was amplified by the shipment of the key fragrance launchers I have just discussed. Yet at the same time we estimate our Prestige setup growth in Q1 was closer to the mid-teens. In consumer Beauty we estimate sell-in and sell-out were relatively aligned in the low-to-mid single digits. As a result the total Coty sellout in Q1 was a little over 10%. Given the strong cost reductions and profitability in Q1 we intend to reinvest more in marketing spending Q2 to further boost our set out during this critical holiday period capitalizing on the unprecedented momentum our brands are seeing. We therefore expect our Prestige sell out in Q2 to accelerate to high-teens growth with selling a bit below sell-out following the Q1 (inaudible).

We also expect Consumer Beauty sell-out to accelerate to mid to high single digits with selling inline to better. In total, this should be drive low teens like-for-like growth in Q2 with sell-out a bit higher. From the profit perspective, our strong gross margin and profit growth in the first quarter is further enabling us to fuel the growth investment in Q2. As a result, we expect to deliver first quarter fiscal 22 EBITDA growth in the low 20s year-on-year with EBITDA margins up approximately 100 basis points versus first half of Fiscal 21. It's important to stress that our key brands in both Prestige and Consumer Beauty are accelerating and in a unique momentum, which happens once in a decade and we will not miss this unprecedented opportunity to gain to gain market share and to lead and preempt new businesses in key regions. We therefore need to invest to secure our near and midterm growth that would be more and more profitable given the high margin nature of this new businesses, and our outstanding profit delivery in Q1 is allowing us to do just that.

Moving to full-year guidance now. We now expect fiscal '22, like-for-like growth of low-to-mid-teens above our prior guidance of low teens growth. Please keep in mind our guidance assumes no significant deterioration in regard to a resurgence of COVID and resulting restrictions or lockdowns. As we previously noted, while we have managed inflation and supply chain related headwinds quite well today. We will of course continue to monitor this situation, we are confident that our gross margin at you attack plan, the accretive innovations we are introducing such as Rimmel's Kind & Free or Gucci Flora, and the continued premiumization of our portfolio, which fuel gross margin expansion for the year as compared to fiscal 21.

All together, we expect fiscal 22 adjusted EBITDA of $900 million at a minimum, as we are intentionally reinvesting our gross margin gain and cost savings in our brands to maximize value and drive sustained momentum for the business into second house and of course beyond. I'm also very pleased to announce that with significant progress made in simplifying our capital structure that we are now in a position to provide EPS guidance. We've been very focused on getting a more solid handle on our underlying EPS and believe providing this level of guidance is an important milestone as we work toward becoming a more simplified company.

With that said, we target adjusted EPS of $0.19 to $0.23 for fiscal 22. Lastly, we continue to expect to in calendar 21 we've leveraged towards 5x and further reduce this to leverage up around 4x by the end of calendar 2022.

To conclude, we entered fiscal 22 with a goal of further building upon the great success we delivered last year. We ended Q1 with sales ahead of our guidance, while also delivering very strong gross margin expansion, both sequentially and versus last year in a volatile inflation and supply chain backdrop. As a result, we were able to not only reinvest in our growth initiatives but also drive adjusted EBITDA growth. Our Q1 exemplifies what we intend to do to the here as well as the debt to your circle cycle we had created with strong sales and gross margin fueling our profit and reinvestment.

Of course, we have no intention of slowing down our progress and we remain committed to aggressively executing on our strategic priorities. We intend to continue to demonstrate the tangible strikes we're making a quote each tier. We believe our brands are in a very unique position, which does not come around often and we fully intend to invest behind these brands and capitalize on the momentum we are seeing today. And very much look forward to providing and even more detail on our strategy and our objectives at our investor day on November 18th to be held at the New York Stock Exchange.

Thank you very much for your time today. We are now happy to take your questions.

Questions And Answers

Operator

(Question And Answer)

(Operator Instructions) And we'll take our first question from Steffi Wissink with Jefferies. Your line is now open.

Q - Stephanie Wissink {BIO 17692025 <GO>}

Thank you. Good day, everyone. We wanted to just unpack gross margins a bit more came in quite a bit stronger than we would have expected. So maybe, Sue, the question for you is, as you look across the portfolio, can you give us a little bit more insight into where you're seeing that margin's strength? And then I think as a follow-up Laurent, just if you could just talk through some of -- or help us quantify some of the key drivers. I think you listed five or six items that were contributing to the strength. If you could just help us contextualize where the bigger pieces or maybe versus some of the minor pieces. Thank you.

A - Sue Y. Nabi {BIO 21845588 <GO>}

So let's start with the first part. Thank you. So again, we're pleased very much with this gross margin performance in the quarter with as you said it's 500 basis points of improvement year-on-year and up 250 basis points up from last quarter. So this performance was driven by a number of different I would say factors. Of course, the first one and it's something that I've been insisting on since new joining Coty one year ago, a more favorable mix both from outside growth from Prestige, as well as a favorable product mix within the different categories. If you take the example of consumer beauty we've been operating on makeup, on mascara which are more accretive and more profitable categories than lip color, for example.

We've done a good work in terms of lowering E&O [ph] and this is clearly in sync with the ability to say, these are the products behind which were going to put our money in terms of media, so let's raise the volumes and we'll meet this, I would say new volumes raised because we are precisely investing behind what's doing well.

The other initiative that helps us a lot is the high era initiatives, as Laurent mentioned. Fixed cost absorption on the increased sales, this is another element, pricing and revenue management, supply chain productivity and of course, material cost reduction program. So, all these elements, all together helped us just to do this I would say, strong improvement on gross margin. Laurent, maybe.

A - Laurent Mercier {BIO 22079608 <GO>}

Yeah. I again, I cannot do if you were to indeed as well. Sue explained we're -- I mean, we are very discipline in this gross margin and indeed there are two big categories. So, the number one is exactly what Sue was explained, so it's really what we are doing on EMO, on productivity, on fixed cost and you saw already the result last year, because last year we were already back even better versus fiscal '19 and above 60%. So we are really continuing this stream. But where we are really intensifying the effort is what I will call is really on the value part of the gross margin, which is really is a bit above where exactly what to explain is really the mix, and this is really something to continue and which we amplify is a revenue management and obviously is also pricing.

So the recipe on the gross part remains the same, but definitely on the value part this is what we are really amplifying, we started and we will do even more in H2. So just one last statement to keep in mind is that we are going to continue this gross margin expansion all across the year, still keep in mind that gross margin in H2 is always lower versus H1 which is the typical seasonal patterns that we have in the industry.

Operator

And we will take our next question from Robert Ottenstein with Evercore. Your line is now open.

Q - Robert Ottenstein {BIO 1498660 <GO>}

Great. Thank you very much and congratulations on a terrific quarter. I was wondering if you could talk a little bit about what -- how not 11-11 is shaping up, a lot of seasonality in China and despite that you did extremely well. So have that shaping up as well as travel retail. And then, just on the cash flow side, perhaps talk about the seasonality of the cash flow and the fact that even in Q1, the cash was -- cash flow was so strong, do you expect that to continue throughout the year? Thank you.

A - Sue Y. Nabi {BIO 21845588 <GO>}

Good morning, Robert. Thank you for the question. So again, you've seen the results we've posted around China 50% of growth. This is really a great I would say a demonstration and KPI in terms of what we have put in place in terms of the number of brands we're going to focus on, in terms of our ability to take a significant amount of sales on TMall creating the right content behind the right brands with the right media investment. But I can tell you, is that the sales momentum that we've seen during the first quarter is tracking in line to better than Q1 in the second quarter. So clearly this will help us to do a strong execution into 11-11 in China. So, on the free cash flow, Laurent maybe you can take that one please.

A - Laurent Mercier {BIO 22079608 <GO>}

Yeah. Absolutely. So, Robert, and you're right we need to focus on these and as I mentioned indeed, usually Q1, I would say is a weaker quarter in terms of cash flow generation, because indeed this is quarter we are building inventory for Q2. And yes, this is what we are doing, but at the same time, you think you want the results of all the initiatives that we have kicked off already a year ago, which is really a full program on cash flow optimization where we are working on 10 specific streams. So, I would go in all the detail, but it's really that going through all your working capital items. One of them is inventories, we are now with better tracking and better monitoring is the forecast accurately on the demand. By doing that in fact we were able to optimize our inventory level while keeping at the same time a very good service level. So this is really something we are doing the same on the receivable with optimization on over dues. So really -- and also on all the working capital. So this is really that you see very -- you see the result in Q1 of all these initiatives and indeed it's either very great output and it confirms that's why we are confirming that our target to look towards the 5 times leverage by end of calendar '21. We are fully confident and this objective is going to be reached.

Now on total year fiscal year '22 we are not giving guidance on free cash flow, but definitely based on what I have just explained and combine of course, with a growth and combine also with the EBITDA that we are delivering, we feel good that fiscal year '22 free cash flow should be nicely higher than fiscal '21.

Operator

And we will take our next question from Andrea Teixeira with JP Morgan. Your line is now open.

Q - Andrea Teixeira {BIO 1941397 <GO>}

Yes. Hi. Thank you. Good morning. So just a clarification on the gross margin bridge. I remember, we were talking about pricing as you saw opportunity to take more actions even prior to COVID-19 with this (inaudible) initiative. How much less pricing did you take in the quarter and when you start to lap those price increases? And my other real question is the SG&A ratio that come in below expectations. Understanding that the team has emphasized the branding reinvestment remains a key focus for the company. Is that any seasonality we should be thinking of as you guide us for at least $900 million in EBITDA and what is driving these SG&A leverage overall, please? Thank you.

A - Laurent Mercier {BIO 22079608 <GO>}

So definitely, yes. On pricing, so these are indeed initiatives that we kicked off already last year, because I mean, this I will say commodity inflation is not coming as a surprise. So we flagged it already a few quarters ago, so that's why we initiated definitely some price increase. And as Sue explained several times and we are reading industry where highly desirable brand and also all the investments that we are doing and all the great assets, some stood at, I mean, we can afford and we can implement indeed some price increase definitely in our business. So, we continue this and we are on-track to take even more pricing initiative in H2. And again all this is really planned. As I said, we knew that there will be some material inflation and we know also that it still to continue in H2. So we have also the plans really to intensify and to accelerate this price increase in H2.

Then on SG&A. So ratio below expectations I will really make it in two parts so. Number one is really the continuity that of the work we kicked off last year, so it means that we have very strict plans and it's part of going to win, so really optimizing a lot of our fixed cost, a known people cost also like business servicing. So, here we are continuing. At the same time, we are making sure that even in the SG&A that we are reallocating some resources and we are also investing in the gross pillars either market, I mean we mentioned about China, for example. So we are making sure that we are investing also in SG&A in China or also in the key strategic pillars that Sue has as explained. So again, it's not only -- when you go through SG&A it's not only one bucket, we are making sure that these are different areas and we are keeping good discipline, but at the same time investing where we need to tune that. So, you see definitely the way we monitor our fixed cost. And on A&CP plan is to maintain roughly similar to Q1, mid to high 20s through the year.

Operator

And we'll take our next question from Steve Powers with Deutsche Bank. Your line is now open.

Q - Steve Powers {BIO 20734688 <GO>}

Yes. Hey. Thank you very much. Maybe picking up on that further little bit. So the momentum on the top line is very evident and fantastic, the positive mix you talked about is also evidence of making progress on productivity. So those are on the plus side of the ledger. On the other hand, cost inflation is real, the cost of -- and it remains bolstering your supply chain is also ticks up a bit. So when you talk about investing incrementally on your brands in the year, can you frame for us how much additional flexibility and incrementality you have in the plan as it stands today versus where you were when the plan started giving the momentum? I'm a little bit, just trying to understand how much incremental -- again incremental flexibility you have to invest in the high brand to feel further growth. Thank you.

A - Laurent Mercier {BIO 22079608 <GO>}

I can start really to give you a frame and indeed Sue can build on this. Again to give you the frame and you see the Q1 results that we are over delivering on EBITDA, we are over delivering on profit because as we just explained, thanks to gross margin and thanks to SG&A discipline. So we are delivering a very strong quarter, but we are not giving guidance quarter by quarter, we are giving the guidance on the fiscal year on the total year and we say that, we will deliver $900 million EBITDA at minimum, because we are very intentional on reinvesting behind our brands and where we have strong ROI.

So what I'm telling you is really to answer your point is that, yes, we have the flexibility and we are creating ourselves our own flexibility and you see it in Q1 and then we decide with Sue and with the management team on a regular basis, okay, where we have the strong ROI and we are allocating the resources when there is very strong ROI. And I can tell you of course and this is what Sue was explaining that now we have a lot more and more initiatives with very strong ROI. And we're -- and sometimes we can see that some tests and so on and not at the level we are expecting. We also very discipline that we keep the money and then we relocate to activities where there is a better return on investment. So, yeah, let's be very clear. We have the flexibility, we are creating our flexibility and we're very intentional on reinvesting behind our brands.

Operator

And we'll take our next question from Lauren Lieberman with Barclays. Your line is now open.

Q - Lauren Lieberman {BIO 4832525 <GO>}

Great. Thanks. Good morning. You run through a bunch of the recent successes in Consumer Beauty and the success you're seeing early indications with the relaunch of the major brands and repositioning. But, sales are still tracking kind of, like, 80-ish percent of where they were in the first quarter of '20, while Prestige is comfortably above where you were back then. So, just curious, if you could share, whether it's recent performance is some of the other brands that are not kind of growing as fast as those that have been repositioned or is it market recovery related? But kind of what you see is the impediment to getting back up to that fiscal '20 benchmark for consumer beauty? Thanks.

A - Laurent Mercier {BIO 22079608 <GO>}

Yeah. Good morning, Lauren. Thank you for the question. In fact what I would like to say is that I think we are in a way having figures that are imperative with what appears with Consumer Beauty businesses and mascara cosmetics businesses have been pushed in. What we are seeing today is that the momentum on behind CoverGirl which is the largest brand of Consumer Beauty is holding and I would even say is accelerating. CoverGirl is growing both in selling and in sellout during the quarter. And the recent weeks of news that you may have seen post quarter are showing four weeks of market share gain, including a strong 0.8 market share gain recently. And there is a lot more to come behind CoverGirl for Q2 and probably for the remainder of the year.

On Max Factor again, I've been describing the success we are seeing, is just the beginning, because we are just starting to see the visibility in stores and online and on TV of the new, I would say repositioning and already with this, we are seeing market share improvement in 70% of our markets and we know which has secured its number one position in UK already with prior to the relaunch of the brand has been doing a fabulous launch with Wonder Extension and mascara, that's one of the best-selling mascaras we know since many, many years and we just put on the market few weeks ago Kind & Free, which is the, I would say the implementation of the recipe of success of CoverGirl into Rimmel which is the number one brand in UK and in many countries. And Kind & Free is starting outstanding the well, we just received the test results of the advertising that I've been sharing with you a few minutes ago.

And again, we are constantly -- and that's the good news breaking I would say the records in terms of beating the best KPIs. So we are super confident that we are going to see an acceleration in Q2 in Consumer Beauty that's for sure. So there is nothing today that I can share with you, that would be in a way, a disappointment versus what we have envisioned or versus the work that we have been putting behind the brands. Every time we put repositioning, advertising, media pressure et cetera, we see it deliver, it's just a question of time, and you will see an acceleration in Q2.

Operator

(Operator Instructions) We'll take our next question from Olivia Tong with Raymond James. Your line is now open.

Q - Olivia Tong {BIO 22252574 <GO>}

Great. Thank you. So innovation really progressed well to drive recovery particularly in Prestige. So can you just talk a little bit about the innovation pipeline and how the development process has changed in recent years? And then I just want to follow up on Steve's question a little bit. Can you just quantify how much cost -- how much higher are costs versus your plans going into the year?

And then to the extent there are profit upsides as the year progresses, are there -- do you have bigger project planned for that upside, because you're already at 26% of sales on A&CP, so, I'd imagine it's not going to go much higher than that. Thank you.

A - Sue Y. Nabi {BIO 21845588 <GO>}

Yeah. Good morning, Olivia. So let me start with the first part of the question around the innovation pipeline and how the process has changed in the recent year? As you know, we've been putting in place a six-pillar strategy, the two first points of the strategy were, number one, stabilizing our Consumer Beauty business starting with our cosmetics brands in Europe and in the U.S. and the second part was to how can we accelerate the growth in the Prestige division, which we have demonstrated during this first quarter at over 30% of growth. And this had three parts, number one, accelerating our fragrance momentum and building a female top 10, top 15 fragrance, which since going to be the case with Gucci Flora, confirming our leadership position in male Prestige fragrances and this seems to be also the case with the Hero, Burberry Hero and Calvin Klein despite big successes.

Adding a new growth engine, which is Gucci makeup, Burberry makeup, Kylie Cosmetics and the three brands are outstandingly growing. If you think about Gucci makeup is triple-digit growth. So in a way, what you are seeing today in terms of growth and the way we are operating behind innovation is very, very easy to understand if you look back at the two key first points of the strategic pillar. So we are really delivering behind what we have been describing in April and that will be describing in much more details next week in New York on November 18. So, this was for the first part of the question around how we are dealing with innovation into the company. May be Laurent, if you want to take the second part, which is around our inflationary impact on costs.

A - Laurent Mercier {BIO 22079608 <GO>}

Yes, absolutely. So, Olivia, so, indeed on, again, I explained few times, so a few quarters ago, so what we raised is these indeed we were assuming a 50 basis point impact related to cost in our gross margin and this is what I explained before, so that's why we are already implemented some price increase already in H1, because we knew that this headwind will come.

Now what we are seeing indeed is that there is amplification as we all know on this inflation and now it's about size of 1 point -- 100 basis point in our gross margin equation, but here same story, we have all the plans in place and what I explained before is that we have proactive efforts on pricing that we are going to implement in H2 fiscal '22 to keep mitigating inflation, but also completely consistent with our journey, our value creation, with accretive innovation and building a better and healthier business.

A - Sue Y. Nabi {BIO 21845588 <GO>}

And to complement Laurent's point, I would really say that the pricing power of the company has been very well demonstrated during the quarter as most of the innovations behind King beauty in mass or behind the new fragrance launches makeup, they are all very, very strongly accretive to the profitability of the company. And really they're even sometimes being very, very premium to the market. The innovations are highly delivering in terms of sellout, it's really -- it's a great confirmation that the desirability and the ability to price of our brands.

Operator

And we will take our last question from Carla Casella with JP Morgan. Your line is now open.

Q - Carla Casella {BIO 2215113 <GO>}

Hi. I'm just wanted to see, how much for the cost savings that you achieved in the quarter. And if you've got any update on the time frame of the $600 million cost savings achievement? And then also does your leverage target by the end of calendar '21 and '22, do those include the addback for the go forward the remaining cost savings?

A - Laurent Mercier {BIO 22079608 <GO>}

Okay. Yeah. Thank you, Carla. So on cost savings, index of the $600 million the savings, is that -- so we delivered last year as you remember $314 million savings. This year, we are confirming to deliver $19 million savings and the rest will be in fiscal '23. So the $600 million saving will be delivered by end fiscal '23. So this is a plan we announced more than a year ago, as you could see we are perfectly on track, even better on this savings. With a very strong Q1, we delivered $60 million in Q1 and we are confirming the $94 million for this year.

What I want to (inaudible) also related to the savings is also with one-off cost which are lower versus initial plan. And this is also big lever to optimize our cap. So perfectly on track and with various transactions on fixed cost, contract terms and also on all the items on curves we need to and it's part of the gross margin.

So, on number two, which is the leverage target, so yeah, very good question. When we are think to work 5 times, this is just I mean EBITDA and net debt. So there is no add back in this calculation, the add back is something that we are using only for the covenant calculation and then the different number. But I'm insisting here that we meet what's 2 leverage time end of calendar '21 and to what's 4 times end of calendar '22 is excluding add backs from this steady plan.

Q - Carla Casella {BIO 2215113 <GO>}

Great. Thank you.

Operator

And we have no further questions on the line at this time I will turn the call back over to Ms.Nabi for any additional or closing remarks.

A - Sue Y. Nabi {BIO 21845588 <GO>}

Thank you everyone for your questions and we are super, super excited to see you next week in New York on the 18th a lot of, lot of things that are new that you would be super happy to discover about our potential growth in the coming months and years. Thank you very much.