Coty's 3Q22 Prepared Remarks Transcript

May 9th, 2022

Sue Y. Nabi, Chief Executive Officer

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Ladies and gentlemen,

- I am proud to share with you today that our Q3 earnings mark the seventh consecutive quarter of Coty reporting results inline to ahead of expectations
- In what is undoubtedly an increasingly complex environment, our teams around the world have been executing with passion, drive, resiliency, and flexibility, showing that Coty's turnaround continues to gain speed and momentum
- As you recall, our objective is to make Coty into a true beauty powerhouse, which includes sustainably growing our sales ahead of the beauty market, growing our profit ahead of sales, and steadily deleveraging our balance sheet
- Our results fiscal year to date clearly evidence the progress on each of these objectives, as we enter the virtuous cycle where strong revenue growth combined with gross margin and cost initiatives, simultaneously fuel profit expansion and strategic re-investments, which in turn drive future growth momentum

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- There are a few takeaways from our results that I would like to highlight
- First, consistent with our expectations, the strong reinvestment during Q2 drove substantial momentum for our brands, fueling acceleration in our Q3 revenue growth to 19% LFL, ahead of our guidance of mid teens growth
- Second, we had another quarter of exceptionally strong performance on gross margins and delevereging our balance sheet. Despite the various inflationary headwinds that we and others in the industry continue to experience, our Q3 gross margins increased 240 basis points YoY.
- As this strong gross margin result is due in part to the continued strong execution of our global supply chain team, I am pleased to share that the Coty leadership team has now

been rounded out with Graeme Carter recently joining as our new Chief Global Supply Chain Officer. With extensive supply chain experience across P&G, Unilever, Avon, and Amazon, Graeme will lead the end-to-end Global Supply Chain function from planning to manufacturing to warehousing and distribution. He will work closely with Dr. Shimei Fan to collaborate on sustainability initiatives and on reducing the environmental impact of Coty's supply chain.

- At the same time, our unwavering focus on cash generation, and this quarter's $210 million cash distribution from Wella, allowed us to lower our net debt by $200 million and drive our financial leverage to 4.7 times.
- Third, we continue to execute and make progress across each of our six strategic growth pillars.
- Finally, our strong results year to date give us confidence to reiterate our guidance for our full year revenues and EBITDA, while raising our adjusted EPS guidance by approximately 1 cent to a new range of 23 to 27 cents
- In this volatile macro environment, I believe that Coty is taking all the right steps to ensure that we continue to succeed in the short and long term, including:
    - Continuing to premiumize our portfolio in both divisions,
    - Maintaining a transformation office working hand-in-hand with our global pricing teams taking actions in real time,
    - Simplifying our supply chain while maintaining a more localized approach,
    - Strengthening our culture and talent retention,
    - And focusing on syncing price increases with added value for the consumer

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- 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

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- Starting with our revenue performance

- Following the 16% LFL revenue growth that we reported in the first half of FY22, our sales growth accelerated to 19% growth in Q3 on the back of the strong and impactful media investment to date
- This substantial revenue growth came in nicely above our guidance of mid teens growth, and importantly the sell-in and sell-out in the quarter were broadly aligned
- The strong growth momentum was fueled by 25% LFL growth in Prestige, primarily driven by volume growth but also a nice contribution from price/mix of approximately 6% through some initial price increases and equally importantly, the continued shift of our Prestige portfolio towards more premium lines
- Our Prestige business growth outpaced many other key prestige beauty players, confirming the momentum seen in the fragrance category globally as well as the benefit of Coty's balanced geographical footprint
- The tremendous success of Gucci Beauty and Burberry across fragrances and makeup continued into Q3, combined this quarter with strong performance in Hugo Boss through the successful recent relaunch of The Scent franchise for Millenials
- At the same time, Consumer Beauty also recorded strong 10% LFL growth in Q3, in a market which is currently moderately positive
- As with Prestige, the bulk of Consumer Beauty's sales growth was driven by volume expansion, with a low single digit contribution from price/mix
- And again this quarter, our Consumer Beauty sales growth included continued strength in our key cosmetics brands CoverGirl, Rimmel, Sally Hansen and Max Factor, as well as strength in mass fragrances and bodycare

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- Moving to sales by region
- We saw growth across all regions in Q3, though the U.S., Europe and Travel Retail clearly outperformed
- In fact, the triple digit growth we saw in our global Travel Retail business was market-leading, which truly speaks to the amazing progress Coty has made in the last couple of

years in expanding our footprint of beautiful counters, and broadening our category presence into prestige makeup and ultra-premium fragrances

- Revenues in the Americas +17% LFL in Q3, driven by broad based strength in nearly every market. Specific to the U.S., we saw strong double digit growth in both our Prestige and Consumer Beauty businesses, with no sign of slowing so far in the booming fragrance category.
- EMEA sales growth accelerated to +23% LFL, as the markets lapped the COVID restrictions of the prior year. We saw double-digit growth across nearly every market and particularly strong Travel Retail momentum.
- Asia Pacific grew +10% LFL, fueled by significant momentum in APAC Travel Retail. It's worth highlighting our sales in APAC Travel retail actually surpassed pre-COVID levels, even as passenger traffic in that region remained below 2019

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

Laurent Mercier, Chief Financial Officer

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- Thank you Sue.
- I am once again pleased with our results this quarter, as we continued to deliver strong gross margins, profit and cash flow above expectations
- As I have said in recent quarters, our performance, especially on a year-to-date basis, demonstrates the virtuous cycle we have created

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- Starting with our gross margin performance

- Q3 adjusted gross margin of 64.6% increased by 240 basis points from last year, while on a year-to-date basis, our adjusted gross margin expansion was robust at 450 basis points to 64.2%
- I am particularly pleased with the gross margin performance, given we are lapping last year's one-time benefit of around 200 basis points while also experiencing ~150 basis points of inflationary headwinds in the quarter
- Our Q3 gross margin was driven by:
    - Strong margin improvement in our prestige business, fueled by the favorable product mix shift as the more premium fragrance lines outpaced the more entry premium lines
    - The continued mix shift towards Prestige;
    - Pricing and revenue management;
    - Supply chain productivity improvements; and
    - Higher absorption on the increased sales volume
- We remain very focused on further driving gross margin expansion this year and in the coming years
- However, as the inflationary pressure increases, we expect year-on-year gross margin expansion to be limited during the fourth quarter
- We continue to execute on our multi-pronged, multi-year gross margin attack plan, while we also remain well positioned to benefit from positive channel, category, and regional mix shift

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- I will now give a brief update on inflation and supply chain
- While the topics of inflation and supply chain have been quite dynamic for some quarters now, since we last spoke, the environment has become increasingly volatile
- Since our last earnings call, we have seen the outbreak of war in Ukraine as well as the resurgence of COVID in China and resultant lockdowns in key parts of the country

- Similar to many other companies, we have faced a heightened level of disruption in recent months – both on supply chain and inflationary pressures
- We are being impacted by select component constraints and long lead-time distances in U.S. and Travel Retail
- Despite the increased disruptions, I am proud to say the team has navigated this quite well to date, by actively managing constraints through safety stocks, alternative materials, and dual sourcing
- And as mentioned earlier, we saw a step-up in inflationary pressure in Q3 to ~1.5% of revenues
- Thus far, we have been able to mitigate the impact of materials inflation through continued favorable mix benefits and pricing actions
- Importantly, despite the increased headwinds, our actions have allowed us to maintain a solid Q3 service level in the low 90s, while also delivering revenue ahead of our guidance and strong gross margin expansion of 240 bps
- As we move into Q4, we do expect inflationary pressures will continue to step up

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- Now moving to our Q3 marketing investments
- Inline with what we indicated last quarter, A&CP investments were approximately 27% of sales in Q3, and up significantly versus last year
- Importantly, our focus is ensuring we are investing this media in the areas with the highest short term and medium term opportunities, and reallocating dollars as needed
- During the quarter this included:
    - Continued investment behind our key, successful innovations like Gucci Flora and Burberry Hero, and the recently launched Hugo Boss the Scent in Prestige, and Rimmel Kind & Free in Consumer Beauty
    - We also continued to invest behind our white space expansion opportunities such as Prestige makeup, where sales again nearly doubled this quarter, and in skincare

    - We also invested behind our key Consumer Beauty brands, resulting in further market share gains
- Looking to Q4, we anticipate maintaining our A&CP investment in the high 20s %

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- During Q3, we maintained strong discipline of our costs
- As I discussed last quarter, while our core savings projects are continuing over the course of the year, these gross savings are being offset in 2H22 by the expected increase in inflation as well as the expected step-up in investment in 2H22 behind our growth pillars including digital, skincare, and China
- As a result, we delivered neutral net savings in Q3, in line with our expectations.
- Importantly, we have already delivered over $90M of net savings for fiscal 2022, which is the net savings level we had targeted for the year and we still expect to close the year approximately at this level.
- We continue to make significant progress with our All In to Win transformation program, across 5 key work streams, driving meaningful improvement on cost, gross margins, sales growth, and cash
- As we move into FY23, a number of new savings initiatives will start to kick in, including savings from the closure of one of our fragrance factories in Germany on track for this summer, savings from material value analysis, a sizeable step-down in depreciation expense, amongst other items
- However, I do want to highlight that with the rising inflation globally across COGS and fixed costs, as well as our continued reinvestment in our growth pillars, the year-on-year savings may not be as easily visible in the P&L going forward
- We remain fully committed to continuing to deliver our savings initiatives and to work diligently to largely offset inflationary headwinds through a combination of pricing actions, continued premiumization and portfolio mix management

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- Moving to our profit delivery in Q3 and year-to-date

- For the quarter, adjusted EBITDA was flattish at $183M, which is particularly strong given the significant 400 basis points increase in A&CP investment versus last year
- It's worth noting that while the Q3 EBITDA performance in Prestige was quite strong, with year-over-year growth and margin expansion, the profitability in Consumer Beauty was lower as a result of significant investment to support the key initiatives of the quarter including Rimmel Kind & Free, CoverGirl's skincare line, Max Factor Miracle Pure, and Bourjois' successful repositioning in France
- Looking to Q4, we would expect the marketing investment and therefore profitability to be more normalized across Prestige and Consumer Beauty
- Year-to-date, our adjusted EBITDA performance was very robust, increasing 22% to $773M with a margin of nearly 19%
- Our year-to-date profit growth was driven by:
    - Strong sales growth;
    - Outstanding gross margin expansion; and
    - Continued fixed cost leverage
- Meanwhile, we were still able to support our brands and step-up our media investments, with year-to-date A&CP increasing by 600 basis points

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- Now moving to our EPS, which includes the following drivers:
    - Adjusted EBITDA in Q3 of $183M;
    - Depreciation of $69M, which is beginning to reflect the expected depreciation decline as certain P&G transaction investments are now fully depreciated;
    - Net interest of $63M;
    - Income tax expense of $18M, equating to a tax rate of approximately 34%, which was in line with our expectations; and
    - $3M of adjusted preferred dividends
    - As a result, our 3Q diluted adjusted EPS ended at 3 cents, an increase of 2 cents versus the prior year

- Fiscal year to date, the diluted adjusted EPS totaled 29 cents, more than double the prior year
- As a reminder, changes in Wella's fair market value are excluded in our adjusted EPS
- However, during the quarter Wella's fair market value included two adjustments
- First, the fair value mechanically declined by $210M as a result of the cash shareholder distribution we received in the quarter
- And second, due to improvements in both Wella's performance to date and expectations for the coming years, Wella's fair value rose by approximately $61M
- Looking ahead to Q4 and for fiscal 2022, I would like to provide more context on the different drivers of our adjusted EPS
    - First, we continue to expect net interest expense for the year to be in the mid $200s
    - Second, we continue to anticipate an adjusted effective tax rate for fiscal 2022 in the low 20% level.
    - Third, assuming no further conversion of preferred shares, we expect to maintain the quarterly run-rate of roughly $3M for the preferred dividend going forward
    - Finally on share count, we expect diluted shares around 880M

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- Moving on to our free cash flow
- I continue to be very pleased with the progress that we are making on our free cash flow
- Due to seasonality, Q3 is typically a weaker free cash flow quarter, and while this continued to be the case, we saw some one-time benefit in the quarter from the the Wella TSA exit
- As a result, our free cash flow was only slightly negative, which is a significant improvement year-over-year
- Importantly, we continue to execute on our cash Olympics program as well as drive strong profit delivery in the quarter

- As a result, fiscal year-to-date free cash flow was very robust, coming in at approximately $627M
- This represents a substantial increase of more than 3 times or $480M improvement from the prior year
- For Q4, we currently expect a more negative free cash flow result, primarily reflecting the sequentially lower EBITDA, a build up of inventory to protect business dynamics during the current supply constraints, and some phasing elements
- Yet, even taking into account this Q4 outlook, I am encouraged to say that we remain on track to deliver strong free cash flow in fiscal 2022

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- Moving on to our capital structure
- During Q3 we received previously announced Wella shareholder distribution, of which, we have received approximately $210M, and expect to receive approximately $30M by the end of our fiscal year
- The total distribution is approximately $10M lower than previously anticipated, due to the combination of volatile debt market conditions and Wella's recent acquisition of a high-growth hair brand
- And with the slightly negative free cash flow offset by FX and other items, we ended Q3 with a financial net debt balance of around $4.2 billion, which is a decline of over $200M from Q2
- As a result, our leverage at the end of Q3 stood at 4.7x, down from 4.9x at the end of Q2
- I am pleased by this improvement, which clearly shows that we remain well on-track to drive our leverage towards 4x by the end of calendar 2022
- Factoring in our 26% stake of Wella at quarter-end, valued at over $1.0Bn, we ended the quarter with economic net debt of approximately $3.28Bn
- I will now turn the call back to Sue

Sue Y. Nabi, Chief Executive Officer

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- Thank you Laurent
- We continued to build momentum across our 6 strategic pillars in Q3, with many additional initiatives in the works

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- Let's start with our first strategic pillar: stabilizing and growing our Consumer Beauty brands
- As I shared on the last earnings call, for the first time in 5 years, the Coty Consumer Beauty business not only stabilized share but actually gained market share on a global basis
- These market share gains continued into Q3, with our global share up 60 basis points in January, 80 basis points in February, and 70 basis points in March
- This is underpinned by strong results in our color cosmetics brands, which together account for roughly two thirds of our Consumer Beauty business
- Our share growth was achieved in a global mass beauty market which is moderately positive, allowing Coty's portfolio sell-out growth to continue in the mid single digits
- While the path to sustained Consumer Beauty expansion may not be linear, these exceptional results confirm that our Consumer Beauty brands are as relevant as ever, and with the right products, communication strategy, in-store execution and the right teams, we can truly continue to excel.

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- Let me give a little bit more detail on the share momentum we are seeing in our key mass color cosmetics brands
- As with last quarter, our 4 biggest color cosmetics brands – CoverGirl, Rimmel, Sally Hansen, and Max Factor – are all gaining market share on a global basis
- Starting with Rimmel

- Q3 was the quarter when we rolled out distribution of the new, clean, vegan cosmetics range called Kind & Free across key markets, supported by impactful digital and traditional marketing
- In fact, with the communication strategy anchored in reaching Gen Z consumers through Tik Tok, our Kind & Free Tik Tok challenge reached 5.5 billion views – a tremendous result for just the first 3 months
- And with Rimmel as the first established mass brand to bring clean, vegan makeup to consumers across Europe, Middle East and Australia, the launch has clearly resonated with consumers around the world, driving strong market share gains
- In fact, fueled by tremendous sell-out performance online, Rimmel has gained over 200 basis points of share in its core UK market
- Moving to CoverGirl, since launching the revamp of the CoverGirl brand in March of last year, the brand has gained market share in the majority of the periods driven by the Magnificent 8 franchises
- As you may have seen in the most recent Nielsen data for April, CoverGirl slipped into share loss, driven by the Eye subcategory, where we have been impacted by 2 factors
- First, we are dealing with temporary supply constraints for Lash Blast Clean mascara, given the success of the launch, which should be resolved in the next couple of months
- And second, we are lapping the strong media investment behind the Clean mascara launch last year
- On the other hand, the other Mag 8 franchises continue to be strong and tracking inline with the market, with share gains in Simply Ageless and Exhibitionist. In fact, we are now starting to activate CoverGirl's rebirth stage 2 with a "Cool / Indie beauty attack," including the launch of its first TikTok channel in February as well as the Exhibitionist mascara+ lip launch, which will be fronted by the new CoverGirl brand ambassador, Kelsea Ballerini, a multi-platinum country music artist
- And as part of CoverGirl's effort to reach a diverse consumer base while also tapping into the current nostalgia for the 90s, which is also particularly on trend right now with

Gen Z consumers, we just announced that Queen Latifah will once again be a CoverGirl ambassador

- On Sally Hansen, the brand continues to gain share in the Nail category, fueled by innovative launches like the Insta Dri Peeps collection, as well as continued growth of Good. Kind. Pure clean and vegan nailpolish
- Finally, on Max Factor, the brand's premium positioning, impactful marketing led by Priyanka Chopra Jonas, and the strong results of the Miracle Pure line – which fits right into the skinified makeup trend – is leading to global success for the brand
- As a result, Max Factor is now gaining share online and offline in the UK, Spain, Czech Republic and Poland
- And last but not least, we have recently kicked off the repositioning of our fifth cosmetics brand, Bourjois, in its core French market
- The new campaign for Bourjois coupled with the relaunch of its innovative Twist Up mascara, drove Bourjois to outpace the cosmetics category by 4 times in March, with Twist Up now the best selling mascara in France
- We are excited by these broad-based positive results, which reinforce our confidence that we have the right brands, playbooks and people to turn around our Consumer Beauty business

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- Turning to the second pillar of our strategy, accelerating our luxury fragrance business with a particular focus on strengthening our share in female fragrances
- Q3 continued the trend of market-leading growth for the fragrance category globally, with over 20% growth both year-over-year and versus 2019
- We continue to see this fragrance boom being fueled by increasing usage by Gen Z and male consumers, ongoing premiumization, and the ever-growing importance of social media platforms like TikTok to enable consumers to discover new scents and connect with a growing community of perfume lovers

- While fragrance category growth in first half FY22 was driven primarily by the U.S. and China, in Q3 we were pleased to see growth acceleration in Europe as well, not just year-over-year but also versus 2019
- Against this attractive backdrop, Coty's innovation continues to excel
- Our blockbuster launches this past Fall, Gucci Flora Gorgeous Gardenia and Burberry Hero, continue to lead
- Gucci Flora remains the #1 fragrance launch in the U.S. fiscal year to date, and maintains strong positions across other key global markets
- Burberry Hero remains the #3 male launch in the U.S. fiscal year to date, and likewise strongly positioned in other key markets
- Adding to the success of these two launches, we have recently relaunched Hugo Boss The Scent male & female perfumes, and the results have been extremely strong, with this top Coty brand gaining share in key markets like Germany, the UK, and Italy
- We also continue to cement Burberry Her as an iconic fragrance franchise globally, the recent launch of Burberry Her EDT has been remarkably successful in the U.S., boosting the Burberry Her overall franchise to the #3 spot in the U.S.
- Finally, the success of the ultra-premium Chloe Atelier Des Fleurs fragrance collection – particularly with Asian consumers – has propelled Chloe to be one of our fastest growing fragrance brands in both China and APAC Travel Retail
- This string of successes confirms the strong capabilities we have built in our fragrance business that will amplify Coty's leadership position in fragrances

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- Part of the second strategic pillar is also becoming a key player in prestige makeup, and our momentum here continues
- Our prestige makeup sales have nearly doubled YoY in both Q3 and fiscal year to date, with growth across Gucci makeup, Burberry makeup, and Kylie cosmetics

- And although Gucci's and Burberry's full entry into makeup are still relatively new, it is really encouraging to see that in China, makeup now accounts for roughly half of brand sales for both Gucci and Burberry
- This reinforces our view that these highly desirable brands have the full right to play and win, in top prestige cosmetics markets like China
- Similarly, on Kylie, we built momentum with two exciting collections – the Valentine's Day collection and the Kendall collection – while also expanding international distribution, including key UK airports, Sephora Mexico and Sephora Brazil, with great initial results
- All of this progress confirms our ambition to grow prestige makeup to at least 10% of our sales, as we continue to expand our brands' distribution and assortment

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- Turning to our third pillar, building out our skincare business
- Let me start with our strategic focus brand, Lancaster
- As you know, our strategy to turn Lancaster into a scientific skincare brand, excelling in repair and protection, is focused first on Hainan and mainland China
- With 4 Lancaster doors now open in Hainan, our offline and online activations are resonating with Chinese consumers, and Lancaster achieved a record month of sales in February
- In mainland China, our successful activations with Sephora have driven Lancaster to become Sephora China's #1 exclusive brand, up from the #2 position last quarter
- And importantly, our hero 365 Skin Repair Youth Serum is now driving over 20% share of business in both Hainan and mainland China, on track to become our #1 hero SKU
- On the Consumer Beauty side of the business, we are continuing to build consumer awareness and visibility for the recently launched CoverGirl skincare line of 5 SKUs
- As we saw with other U.S. mass cosmetics brands that entered skincare in recent years and initially in the cosmetics wall, building up awareness and sales takes time

- This test, learn, and refine approach has been our philosophy from the beginning when entering new white spaces
- We are taking learnings from these initial months of trial, and will continue to improve the CoverGirl Skincare execution as part of the Fall 22 wall resets, specifically the visibility of the range as part of the CoverGirl wall
- Finally, we remain on track to launch the new Kim Kardashian skincare line by the end of our fiscal 22, so stay tuned for more news on this exciting line
- In all, we continue to lay the foundations for strategic skincare initiatives, as we see FY23 as the year of skincare acceleration for Coty

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- Turning to our fourth strategic pillar, building our e-commerce and DTC expertise
- Focusing on our e-commerce results, we continue to make strong progress, with e-commerce sales in Q3 up 11%, with similar growth across Prestige and Consumer Beauty, even as we cycle the strong e-commerce growth and penetration of the prior year which were elevated due to COVID restrictions in many markets
- As a result, our e-commerce penetration fiscal year to date reached high teens, including mid 20s penetration in Prestige and approximately 10% penetration in Consumer Beauty

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- And as we have continued to discuss, our digital transformation encapsulates so much more than just e-commerce, and we continue to reach new milestones with each month
- In terms of new distribution, we are excited to share that Farfetch – the leading online luxury retail site – has entered the luxury beauty space, and 10 Coty brands were among the first to be part of the launch
- We are excited about this great opportunity for Coty to reach a new high-end audience, create further synergies with our Fashion Houses and gain access to 1st party consumer data.

- As for new models of reaching consumers and paths to purchase, we are continuing to upskill our employees and beauty advisors on best practices in livestreaming, with more and more markets joining this trend, led in particular by China and the U.S.
- Examples include Burberry in-store livestreaming on Tmall, Max Factor in-store & KOL livestreaming on Douyin, Kylie beauty livestreaming on TikTok, Facebook and Nordstrom.com, and Rimmel Kind & Free livestreaming on the Namshi e-retailer site
- All of these livestreaming activations are driving increased sales and growing follower bases for each of these Coty brands
- Finally, on new digital tools, our recently launched advanced virtual try-on tool for Sally Hansen is off to a great start, as we have seen consumers doubling their time on the Sally website, trying on an extra 8 shades per user, and doubling intent to purchase
- We have a robust roadmap to rollout this Augmented Reality feature across key brands and markets in the next 6-9 months

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- Moving on to China, our sales in mainland China were positive for the quarter on the back of strong January and February, even as traffic declined in March when COVID lockdowns were instituted across many cities
- At the same time, it's important to highlight that when including sales in Hainan, combined China sales were positive in March as well
- And I'm proud to report that Coty's Prestige business was once again the fastest growing amongst the Top 10 prestige beauty companies, with our sell-out up 14% in Q3 compared to a flat overall market
- Like others, we continue to carefully monitor the regulations and consumer preferences, remaining flexible to activate our brands in the locations and channels where consumers are gravitating
- What is clear is that we have the key elements in place to fully accelerate our China business once lockdowns ease
- Specifically, Tmall & other e-com are already a third of our sales

- From a category exposure, as I mentioned earlier, makeup is already half of Gucci and Burberry sales
- And within our fragrance business, ultra-premium collections such as Gucci Alchemist Garden, Burberry Signatures, and Chloe Atelier des Fleurs already account for ~10% of these brands' fragrance sales

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- That now brings me to our outlook for the year
- Following the very strong sales growth we reported for Q3, we remain on track with our guidance for second half '22 LFL sales growth in the mid teens %
- This includes the high teens LFL sales growth we reported today for Q3, followed by low double digits LFL sales growth in Q4
- As a reminder, two weeks ago we announced that after careful consideration, including analysis of relevant U.S., U.K., and other applicable sanctions, we have decided to wind down our Russian operations starting immediately.
- As such, our Q4 growth is weighed down by our full exit from our Russia business, as well as COVID-related lockdowns in China
- Moving down the P&L, we expect Q4 FX headwind to sales of approximately 4% to 5% (at current rates)
- We expect rising inflationary headwinds to limit year-over-year gross margin expansion in Q4
- We continue to expect discrete tax headwinds in 2H22, with full year FY22 adjusted effective tax rate in the low 20s
- For total FY22, we continue to expect LFL sales will be at the upper end of our guidance range of low-to-mid teens percentage growth
- We continue to expect FY22 adjusted EBITDA of $900 million, as we navigate the inflationary environment while intentionally reinvesting gross margin gains and costs savings in our brands to maximize value.

- With FX providing a net benefit at the EBITDA level both in Q3 and YTD, compared to previous expectations for FX headwinds in 2H22, we intend to reinvest to fuel topline initiatives while still delivering $900 million in EBITDA at actual rates.
- And with the strong YTD EPS delivery, we are raising our FY22 adjusted EPS guidance to 23 to 27 cents, up from our previously guided range of 22 to 26 cents.
- While it is too early to comment on FY23, we do want to remind everyone that our previously outlined target for CY22 adjusted EBITDA approaching $1 billion was based on the full scope of the Coty business
- With numerous country sanctions effectively prohibiting Coty from operating in Russia, resulting in our exit from the market, and Russia plus local Travel Retail accounting for a mid single digit percentage of our annual adjusted EBITDA, the new Coty scope mechanically implies CY22 adjusted EBITDA approaching $950 million
- And we remain confident in the favorable category and market dynamics in many parts of the world, as well as in the levers at our disposal, to reach this CY22 adjusted EBITDA level
- As a result, we continue to target leverage towards 4x exiting CY22 and approximately 2x exiting CY25.

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- To conclude, our goal for FY22 was to build upon the great success we delivered last year, and we are continuing to build on this momentum quarter after quarter despite the dynamic global backdrop
- We grew sales and sell-out strongly in the first nine months, with broad-based strength across Prestige and Consumer Beauty
- We delivered gross margins, profit and cash ahead of expectations, setting the stage for strong delivery for the total year
- We continued to make progress across each of our strategic pillars, with many more exciting initiatives ahead

- In short, we are maintaining our pattern of consistent strong delivery as we progress on our ambitions to become a true beauty powerhouse
- Thank you for your time today. We are now happy to take your questions