

Conference Call 3Q -9M 2009 Results - November 11th 2009

Roberto Vedovotto - CEO

Good evening to you all and welcome to Safilo's third quarter and nine months 2009 results conference call.

Today's agenda will be focused on the following topics:

- Review of the third quarter and nine months 2009 performance;
- Update on current trading and initiatives ongoing;
- Update on the proposed recapitalization plan and expected next steps.

Christian De Felice, Francesco Tagliapietra and Barbara Ferrante are here with me and together we will answer the questions you might have.

KEY THEMES

The key themes of our Q3 2009 business performance are the following:

- Still very weak business performance in the context of ongoing challenging and uncertain market conditions; there is still uncertainty in particular on the long term sustainability of the early signs of recovery;
- After an encouraging improvement in June, being the first month of the year in which we registered flat sales versus the corresponding previous year month, July was again extremely weak. August and September showed no real consolidation trends;
- From a product portfolio standpoint we continue to experience a shift of sales towards more "accessible" products in the sunglass business and are therefore progressively introducing new products in our collections in order to provide new entry price points to mitigate the price/mix effect;
- Our prescription business, usually more resilient, registered a weaker than expected performance in the third quarter;
- From a geographical standpoint, our performance in America remained stable, in line with the previous two quarters. Very tough trading conditions were again more evident at the department stores and retail channels level;
- Asia continued to be the most challenging area, in particular Japan, still not giving any sign of recovery;
- Europe, on the other end, registered a small improvement especially in countries like France and Spain that, together with some other continental European markets, benefited from the results achieved by the Carrera collections outside Italy;
- From a channel standpoint, the wholesale business continues to experience difficult trading conditions;
- The retail channel performance at comps sales level is still declining at a double digit rate and profitability for the channel is negative;
- On the back of this difficult trading environment, our operating performance further deteriorated due to the underutilization of our Italian plants given the still weak order intakes. The restructuring of our manufacturing footprint is still ongoing according to the plans already communicated to you;
- Our working capital position has been slightly improved.

In order to present you our ongoing operating performance for the last 9 months, my comments will refer to our adjusted results, excluding the extraordinary charges already registered in our first half results. Let me remind you that in June we booked total extraordinary non cash items of €128.1 million, €7.4 million euro related to the restructuring of our production activities and 120.7 million euro related to the write down of the goodwill value allocated to some Cash Generating Units.

In addition, the completion of the proposed transaction with HAL (and specifically the disposal to HAL of the non-strategic retail network) would result in additional non-cash, non-recurring losses amounting to approximately Euro 28 million, that we have already written down in the third quarter.

Q3 2009 RESULTS HIGHLIGHTS

Because of the difficult market environment described, third quarter results were characterized by a decline of sales although in the context of a very weak operating performance.

In particular, total sales were down in Q3 by 7.0% reported, 7.7% at constant currency, taking the total decline of the nine months at 10.5% reported, 13.3% at constant currency.

EBIT was negative for €7.6 million euro or minus 3.6% of total sales (2.9% or 6.6 million euro in Q3 2008).

We closed the third quarter with a net loss of €22.1 million euro, taking the net result of the nine months to a loss of €30.0 million euro.

9M 2009 RESULTS HIGHLIGHTS

Key financial highlights:

- 9M Total Sales were €774.7million (€212.6million in Q3); a decline of 10.5% and 7.0% vs. 9M2008 and Q3008;
- 9M EBITDA was €55.0million (€3.5million in Q3); a decline of 46% and 79% vs. 9M2008 and Q3008;
- Net financial position of €586 versus €592 million registered at the end of June.

Ongoing Projects

Given the difficult market conditions, we are taking serious strategic actions to cope with the present environment. In particular, as announced few weeks ago, we are currently working to finalize the €300 million euros recapitalization approved on the 19th of October by the Board of Directors, in connection with the binding agreement reached with HAL Holding. I will give you more details on this, later on during this conference call.

In addition, we are implementing other projects and initiatives at the industrial, organizational, and commercial / product level to strengthen our business, including:

Marketing:

- Increase the level of integration with our clients;
- Focus on visual merchandising;
- Focus on house brands;
- Focus on wholesale channel;
- Increase the appealing propositions for all our fashion brands;
- Shifting the price mix in order to rebalance the products portfolio.

Production

- Reduce the number of models and SKUs;
- Finalize the restructuring plan still ongoing;
- Improve working capital management;
- Starting operations in China at a rate of around 30% of maximum capacity

New Products Offering

Gucci

We have worked closely with Gucci to extend one of the leaders in the luxury eyewear market collections with a line of Youth oriented styles. Gucci strongly believes in the potential of this project. There is a clear connection between Gucci and the so called 'iPhone generation'. We are targeting this segment to gain more territory in the 18-30 y.o. market. Mid October saw the launch of the worldwide website www.gucciweb.com, supported by print and on-line activity.

Dior and Armani

We are focusing on new projects also for our other top brands, Armani and Dior, which will soon be launched and will be presented to you at the beginning of next year.

Service

After the intense destocking operated by our clients in the last three to four months, it is paramount to provide a higher quality service both in terms of positioning and time to market. I have mentioned to you our 'Project Smile', a software already integrated in around 300 key account stores at year end. Developed in collaboration with TXT, it suggests the replenishment of the best product assortments, allowing a better defined management of their and our inventories. At the same time, we are upgrading our planning systems as well as implementing best practices in our production plants.

Q3 2009 RESULTS - ANALYSIS

Distribution channel standpoint:

Let's now analyze in detail the Q3 results in terms of distribution channels, countries and products.

Wholesale revenues were down in the third quarter by 9.5% reported and 10.4% at constant exchange rates. As commented in previous occasions, we continue to have, in this channel, a strong focus on quality of receivables rather than sales.

The Retail business was up 13.2% in the third quarter reported, up 14.4% at constant currency. As of September 30 2009, we had 326 stores vs. 307 stores at the end of September 2008. Comps sales were however down around 15.5% in the third quarter (-17.2% in the nine months), with the weaker performance registered by the Mexican stores, still hit by the drastic tourists drop.

In terms of profitability, as already anticipated in mid-October, EBITDA in the third quarter was €3.5 million euro (1.6% of total sales), compared to €16.7 million euro (7.3% of total sales) in Q3 2008.

In particular, in the wholesale business, EBITDA reached 2.2% of revenues, compared to 8.1% recorded in Q3 2008.

The retail business registered yet again a negative EBITDA of 626 thousand euro, taking the total EBITDA loss in the nine months 2009 at €3.2 million euro. This result was mainly impacted by the negative comps sales and by the start up costs related to the new stores opened during the period.

The main drivers of our operating performance have been the following:

Gross Margin declined 270 basis points in Q3 2009 compared to Q3 2008, reaching 54.2% of total sales. In the nine months 2009, this Margin was slightly declining over the corresponding period last year (declining by 50 basis points), driven by the components already described during 1H, including (i) new product development and (ii) industrialization processes.

The Gross Margin in the third quarter was still affected by a higher incidence of our fixed cost base, in light of some further underutilization of our production capacity. The level of obsolescence remained in the quarter in line with last year third quarter.

SG&A remained high, due to the higher impact of retail costs and the higher incidence on sales of fixed costs, including Advertising & Promotion expenses or royalties which are related to the achievement of minimum guaranteed and are fixed on the basis of the previous year results.

In this area, we also decided to increase our allowance for doubtful accounts in order to be fully prepared at year end shouldn't market conditions not improve. In this context, in the wholesale channel in the third quarter, total SG&A costs declined by around 4% in spite of the increased allowance.

From a geographical standpoint:

The Americas declined 7.9% in Q3 reported, slightly improving the performance at constant currency compared to previous quarters (-8.8% vs -10% in Q2 and -12.2% in Q1). The area decreased by 3.6% in the nine months (-10.6% at constant currency).

We continue to be satisfied with the performance of our products at the independent opticians (3os) level, especially in the prescription frames business.

Europe 11.7% during Q3 (-19.5% in the first half), better than previous quarters (-17.8% in Q2; -21.1% in Q1) on the back of improved trends in countries like France and Spain. These markets benefited from the results registered by the house brand Carrera, which is growing also outside Italy.

Asia was, again in this third quarter, the worst performing area, with sales down 16.9% reported (-17.6% at constant currency). Japan continues to be impacted by its strong exposure to high-end, luxury eyewear, while a generally depressed average purchasing ticket still affects business performance in other important markets of the area, like China and Hong-Kong.

From a product category standpoint:

Sunglasses sales in the third quarter declined by 6.1%, compared to the double digit drop registered in H1. As already mentioned, we are acting quickly to provide collections fine-tuned with changed consumers' demand, also for our fashion brands.

The US is surely the market where consumers are more reactive to these new product/price propositions.

The prescription frame business declined in the third quarter by 14.1%, mainly due to the tougher comparison with the same period of last year. Please note that the segment had in fact registered a growth in Q308, especially in the month of September in the USA, thanks to some new product releases.

From a financial standpoint:

Below the operating line, net financial charges, declined in the third quarter to €9.7 million from €14.2 million registered in Q3 2008. In the quarter, we registered net forex gains of around €2 million euro due to the US\$ spot rate at the end of September.

Net result in the third quarter was impacted by taxes of almost €5 million euro, as there was no accrual of deferred tax assets in spite of the accumulated losses.

Free Cash Flow in the nine months 2009 registered an outflow of €12.3 million euro, compared to an outflow of 25.5 million in nine months 2008. We had a positive free cash flow of €6.3 million in Q3 2009, as a result of the following initiatives:

- Improved working capital management. Here, we had a decrease in trade receivables as well as in inventories. The decline in inventories is related to the great attention we are placing to the streamlining of production outputs and to the quicker exit of slow rotation products. Trade receivables and payables declined as a result of the normal business cycle and for the dramatic drop in sales we are experiencing;
- The lower cash flow from operating activities was due to the lower results of the period and a decrease of investing activities, standing at €28.3 million in the nine months 2009 (around 9 million in Q3) versus €76.2 million in the nine months 2008 during which Safilo acquired the Mexican and Australian retail chains and invested in the new production plant in China.
- Capex in the nine months included around €10 million for maintenance of our production factories and €8 million cash out related to the new plant in China, while we invested around €4 million in retail.

As a result of the above results, our net financial position at the end of September 2009 was of €586.3 million, cyclically higher than the position at 2008 year-end, of €570 million.

CURRENT TRADING

The month of October was very weak. Sales were down high single digits, with the worst performance still registered in Asia. Order intake in the month was down around 12-13% as I had already indicated last time we spoke. It is still too early to provide you with a feedback on November but we keep seeing a prudent approach from our clients in placing their orders as they want to understand how the Christmas season will start:

- high-end accessories are still the most impacted by the general consumers' trading down;
- we are widening our product mix to satisfy better and better our consumers both in terms of design and purchase power. This is progressively increasing the (negative) price/mix effect on our business;
- Carrera remains strong.

RECAPITALIZATION PLAN

The recapitalization plan disclosed to the market will enable Safilo to strengthen its capital structure and reach the necessary flexibility to effectively implement the strategic guidelines described. We expect to have a cash inflow for a total amount of €283m that will rebalance the current capital structure.

Condition precedent to the overall recapitalization plan is amongst others the successful completion, by November 18, 2009, of the cash tender offer launched by HAL for the outstanding Safilo Notes 2013. The company has been informed by HAL that only 1.03% has been tendered at the Early Bird date (in addition to the 38.76% committed prior to the Tender Offer by existing Note-holders). The company has also been informed that currently HAL does not own any of the Safilo Notes itself. As a result, the chance that the tender will not be successful can not be neglected.

In such event, the overall recapitalization plan might not take place and the company would again be in a highly leveraged situation and will in all likelihood default under its banking facilities by year-end.