FINAL TRANSCRIPT

Thomson StreetEvents℠

SIG - Q2 Fiscal 2012 Signet Jewelers Ltd Earnings Conference Call

Event Date/Time: Aug. 25. 2011 / 12:30PM GMT

THOMSON REUTERS

CORPORATE PARTICIPANTS

Tim Jackson
Signet Jewelers Ltd. - Director of IR

Mike Barnes
Signet Jewelers Ltd. - CEO

Ron Ristau
Signet Jewelers Ltd. - CFO

CONFERENCE CALL PARTICIPANTS

Rick Patel
BofA Merrill Lynch - Analyst

Bob Drbul
Barclays Capital - Analyst

Jennifer Davis
Lazard Capital Markets - Analyst

David Wu
Telsey Advisory Group - Analyst

Anthony Lebiedzinski
Sidoti & Co. - Analyst

Ike Boruchow
JPMorgan - Analyst

Bill Armstrong
C.L. King & Assocs. - Analyst

Rod Whitehead
Deutsche Bank - Analyst

John Baillie
Societe Generale - Analyst

David Berman
Berman Capital Management - Analyst

Michael Lopiano
Fidelity International - Analyst

Michael Friedman
Cumberland Associates - Analyst

PRESENTATION

Operator

Good day and welcome to the Signet Jewelers second-quarter results conference call. Today's conference is being recorded. At this time I would like to turn the conference over to your host today, Mr. Tim Jackson. Please go ahead.

Tim Jackson - *Signet Jewelers Ltd. - Director of IR*

Thank you, operator. Good morning and welcome to the conference call for Signet's second quarter fiscal 2012 results. I am Tim Jackson, Investor Relations Director. With me are Mike Barnes, CEO, and Ron Ristau, CFO. The presentation deck we will be talking to is available from the webcast section of the Company's website, www.Signetjewelers.com.

Before I hand over to Mike, I will give the Safe Harbor statement. During today's presentation, we will in places discuss Signet's business outlook and make certain forward-looking statements. Any statements that are not historical fact are subject to a number of risk and uncertainties and actual results may differ materially. We urge you to read the risk factors cautionary language and other disclosures in the annual report on Form 10-K that was filed with the SEC on March 30, 2011.

We also draw your attention to this slide.

Mike Barnes - *Signet Jewelers Ltd. - CEO*

Thanks, Tim. We are very pleased with the record results in our second quarter which reflects the ongoing success of our business driven by our competitive advantages. For the quarter, total Signet same-store sales were up 9.9% led by the US, with a 12.2% comp store sales increase and followed by the UK, which comped positive 1.4%.

Some other key highlights include operating margin was 12.8%, an increase of 430 basis points. Income before taxes was $99.8 million, up $45.1 million or 82.4%. Diluted earnings per share were $0.76, up $0.31, or 68.9% and the free cash flow was $61.4 million.

Reflecting the strength of our business model and its cash flow, the Board has declared a quarterly dividend of $0.10 a share. We feel this is an excellent way to return value to our shareholders while still maintaining financial flexibility to invest in future business initiatives.

Now looking at the results in a little more detail and starting with the US division performance. Total US sales were $643 million, up $65.3 million, an increase of 11.3%. Kay had another outstanding quarter and increased same-store sales by 13.5% up from the 2.7% growth achieved in the same second quarter of fiscal 2011.

Jared again performed extremely well with comps up 12.6% following a 14.1% increase last year. Outstanding two-year comps. Overall, US same-store sales increased by 12.2% compared to an increase of 6% last year.

Average selling price excluding the charm bracelet category was up 12% for Kay and 8.6% for Jared, 13.3% for the regional brands. This reflects not only price increases but also importantly our consumers trading up our pricing architecture including to new higher price point merchandise in the bridal category.

Operating income was $104.4 million up $43.7 million which was a 72% increase. The US division's operating margin increased by 570 basis points to 16.2%.

In jewelry retail, a superior in-store customer experience is central to our success. It's that final two feet of supply chain right over the display case that is crucial. It is here where the relationship with the customer is created where there is an opportunity to up-sell, to sell add-ons and where the sale is completed allowing the opportunity to create a customer for life.

Before joining Signet, I didn't fully appreciate the emphasis Signet placed on the customer experience. The sophistication of the systems underlying the in-store execution, the resources put into associate training and development and how central it is to the culture of our Company.

Our results call, I can't do it justice, but I would urge you to go into any of our stores and experience it for yourself and we hope that you will have the chance to attend our investor relations day and store visits on October 4 held in New York when we will have the opportunity to meet some of our store team members.

A great in-store customer experience takes many years of dedication to achieve and it is far from easy to replicate.

The in-store experience is particularly important in the bridal category, which was again one of our cornerstones of our performance. Neil Lane Bridal, largely a non-comp business in the second quarter and the range is now available in all Kay and Jared stores with the rollout to all regional stores planned for the third quarter.

There was further store expansion for the Tolkowsky Diamond as well, which is now available in 600 stores. Neil Lane Bridal and Tolkowsky Diamond have price points that are higher than the average bridal purchase for our mall stores and have been important contributors to the growth in average selling price and store productivity as well. Our unbranded bridal selection which still accounts for a majority of the bridal sales continues to offer great value to the customer.

Our non-bridal exclusive and differentiated brands outperformed with the charm category remaining strong. In particular, we benefited from the success of Charmed Memories which was largely a non-comp business in the second quarter and the Pandora range continued to show strong growth.

Another differentiated brand that performed well was Le Vian, which is also helping drive higher average selling prices. As a group, the exclusive and differentiated brand ranges for both bridal and non-bridal categories continues to gain momentum.

One reason for our continued strength is the effectiveness of our advertising execution. We again significantly increased investment in marketing and we continue to test advertising support for the bridal category and have achieved further encouraging results. We see this as a very important opportunity.

Another important element that drives not only advertising but also direct commerce is our web presence. We saw sales grow on our websites by 50% over the comparable quarter last year. We are upgrading both the Kay and the Jared websites in the third quarter ahead of the holiday season. They will be easier to use, have richer and more engaging content and will include a number of important new features. This is being done with our usual thoroughness and we will be testing the upgraded sites before launch.

Turning to the UK, we continued to operate well on a challenging economy and again outperformed nonfood retail sales in the quarter. Total sales were $154.6 million, up $12.6 million, an increase of 8.8% with same-store sales up 1.4%. At constant exchange rates, there was a 0.1% increase in sales. So we saw some sequential improvement from Q1.

Both watches in the bridal category including gold rings continued to perform well as did the charm category. E-commerce sales also continued to outperform in the UK with a 14% increase over prior year quarter two.

Average selling prices, excluding the charm bracelet category, were up by 5.3%. The UK consumer is shopping more to a budget rather than higher retail prices driving sales. It is therefore very important to be continually looking at the merchandise and making sure that appropriate opening price points are maintained.

While we continued to keep a tight control on costs, the operating margin was down by 150 basis points with the UK division's operating income being $2.8 million down by $1.9 million for the quarter. In the comparable quarter last year, the results benefited from a $900,000 surplus on a real estate sale.

Notwithstanding the fact that we did outperform the broad discretionary retail market in the UK, we fully recognize it is our responsibility to drive initiatives that will deliver the expected results. Our team members through all levels of the Company know that we must drive this process. So as in the US, we remain focused on providing a superior in-store customer experience with an emphasis on customer service and staff training.

In addition, we have a number of initiatives underway in the UK. For example, there is an increased emphasis on branded differentiated merchandise and new products in general. Some of these are specific to the UK market such as the Amanda Wakeley collection, while others such as Love's Embrace, Tolkowsky and Le Vian, draw from our US experience.

In H.Samuel we are having success with fashion jewelry lines including DKNY and Guess. Additional investment has been made in marketing with television advertising for H.Samuel ahead of Mother's Day being successful. This was done in conjunction with Chamilia. We have also increased customer relationship marketing for both H.Samuel and Ernest Jones.

I'm encouraged by the performance of the UK business in this challenging marketplace and I am pleased with the number of initiatives that we do have underway. Because in difficult times, it is those that have the perseverance and the financial strength to continue proper investment in their business and who innovate to create new and exciting product ranges that come out ahead. It is through these processes that the foundations for long-term success are built.

I will now hand the call over to Ron to go through the financials in a little bit more detail.

Ron Ristau - *Signet Jewelers Ltd. - CFO*

Thank you, Mike. Total sales for Signet increased 10.8% to $797.6 million compared to $719.7 million in the second quarter last year. The total Company comps store sales increased 9.9% versus an increase of 4.6% in the comparable quarter last year.

In the United States, sales increased to $643 million primarily reflecting comp store sales up 12.2% versus 6% of an increase last year. The space impact was adverse by 0.9%. In the UK, sales rose to $154.6 million reflecting a comp store sales increase of 1.4% compared to a decline of 0.5% last year. As reported, UK sales were favorably impacted by currency fluctuations which more than balanced the 1.3% adverse impact of reduced space.

Now looking at the reconciliation of the $45.1 million increase in income before taxes from $54.7 million up to $99.8 million. Gross margin was $294.8 million, an improvement of $57.6 million. The gross margin rate was 37%, up by 400 basis points. The drivers of the improvement were gross merchandise margin which improved by 90 basis points with the US up 110 basis points and the UK down 40 as we continue to successfully manage fluctuations in commodity costs as we have done for many years.

Net bad debt to total US sales ratio was at 4.4%, which was 80 basis points better than last year and we realized leverage on our occupancy expenses.

The SG&A expense was $224.5 million, up $20.8 million or 10.2% from last year. As a percentage of sales, they were down -- I'm sorry, they were 28.2%, down 10 basis points from last year and I will cover this more on the next slide. Other operating income was $32 million, up $4.8 million on last year primarily reflecting interest income on higher accounts receivable which have a 20 basis point favorable impact on the operating income margin.

The second quarter's operating income was $102.3 million, an improvement of $41.6 million or 68.5%. The operating margin was 12.8%, up from 8.5% last year in the second quarter, an increase of 430 basis points. Net interest expense was $2.5 million, a decrease of $3.5 million, a fall of 60 basis points as a percentage of sales. This primarily reflected the benefit of prepaying the private placement notes last year.

Income before income tax was $99.8 million, an increase of $45.1 million or 82.4%. As a percent of sales, that was 12.5% and improvement of 490 basis points based upon excellent execution in all aspects of our business. The quarterly tax rate was 33.6% reflecting the geographic mix of profits and favorable tax settlements in the comparable period.

Now looking at SG&A in more detail and focusing on the second quarter. The major contributing reasons for the increase of $20.8 million in the second quarter were as follows. We increased our net advertising investment by $4 million. $3.5 million of the increase was attributable to currency fluctuations. $1.5 million was attributable to higher 401(k) contributions, primarily in the US. $7.6 million of the remaining increase was a result of increased store staff costs which flexed with our increased sales and the balance primarily reflected increased investment in IT and credit infrastructure and other expenses.

On a year-to-date, the information is also included on a slide for your reference; we believe our SG&A remains extremely well controlled.

Our graph on receivables shows the second-quarter net debt -- net bad debt to sales ratio and a collection rate for the last 10 years. We note that for the period we achieved results broadly in line with the historic range. This improved by 80 basis points from 5.2% to 4.4% reflecting both higher sales and an improvement in the underlying performance of the receivables portfolio. We would point out that this is the seventh consecutive quarter that we have seen improvement in our bad debt ratios.

In-house consumer finance participation rate was 57.7% versus 56.3% last year, the increase driven by growth in our bridal business.

Turning briefly to the year-to-date results, for the year-to-date, total Signet same-store sales were up 10.1% led by the US with a 12.4% same-store sales increase, the UK up 0.8%. Operating margin was 13.1%, an increase of 370 basis points. Income before taxes was $217.6 million, up $88.8 million or 68.9%. Diluted earnings per share were $1.63, up $0.60 or 58.3%, and our free cash flow year-to-date was $153.8 million.

Free cash flow remained strong as compared to --. As compared to a year ago, free cash flow this year supports an increase in inventory which reflects higher costs and supports our sales growth. Inventory in total rose 6.8% as compared to Q2 last year and below our increase in sales. We remain pleased with the quality and level of our inventory.

Receivables moved in line with US sales and net cash used in investing activities was $38.3 million up from $14.4 million last year and reflecting our planned increase in capital expenditure. We ended the quarter with cash of $440.2 million down from $485.4 million a year ago. This reflects the prepayment of $280 million of private placement notes offsetting the cash generated in the last year.

In the year-to-date, we believe we have made excellent progress against all of our financial objectives for fiscal 2012. In particular, the improvement in gross margin has been very marked. Reflecting our performance in the year to date, we have increased our free cash flow guidance to $175 million to $225 million from our original target of $150 million to $200 million.

I will now turn it back to Mike.

Mike Barnes - *Signet Jewelers Ltd. - CEO*

Thanks, Ron. So far we have concentrated on the second quarter but since it ended, there has been considerable volatility in the financial markets and increased concerns about the economic outlook. This is clearly something that we are monitoring closely.

Given the great execution that our team members have demonstrated, we believe we are well positioned for the rest of the year and into the future to gain profitable market share.

Unlike many retailers, we have limited inventory risk. We also have a strong balance sheet and great cash flow. However, we must all recognize that the global economy is fragile at best, and we must always be prepared for whatever the unknown future holds.

If, and I emphasize if, we do face a challenging economic environment, it is just at such time the competitive strengths become even more important and the strong take the opportunity to build the base for future market share gains. We currently feel great about the rest of the year and are well prepared for the Holiday Season.

I will now open the call up for questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Rick Patel, Bank of America.

Rick Patel - *BofA Merrill Lynch - Analyst*

Thank you, good morning. Just two quick questions. First, can you just help us understand how much price increased on like-for-like products in the second quarter?

And then second, can you just talk a little bit more specifically about what is driving the trade up within the bridal category? Is it just Neil Lane and Tolkowsky being introduced in more stores or is there something else going on there?

Ron Ristau - *Signet Jewelers Ltd. - CFO*

Your first question I would say that we don't really go into the percentage price increases nor do we disclose that for competitive reasons. Obviously, our price increasing has been very successful. We are very careful and prudent with it, and it is something we have to do on an ongoing basis given the pressure on commodity costs but we have been very able to successfully more than offset the commodity price increases.

So I am sorry, Rick, I wouldn't go into the specifics of how much we have increased prices on an item-per-item basis.

Mike Barnes - *Signet Jewelers Ltd. - CEO*

Yes, good morning, Rick. On the bridal, I think that you hit it pretty well there. Obviously, our branded offerings are helping drive that business even higher for us, and it has been -- a big initiative for us this year has been to really focus on bridal anyway. The Neil Lane product is being very well received and we have been rolling it out to all the Kay and Jared stores and are rolling it out to the regionals as we mentioned on the call.

Tolkowsky has been successful as well. We have opened a lot more doors with that. We still feel like our branded differentiated bridal product will continue to drive that category for us in the future and we are very pleased with the results that we have seen there.

Rick Patel - *BofA Merrill Lynch - Analyst*

Great. Thank you very much.

Operator

Bob Drbul, Barclays Capital.

Bob Drbul - *Barclays Capital - Analyst*

Hi, good morning. The first question I have is can you talk a little bit about the sales trends throughout the quarters, the monthly progression of sales, and anything that you've seen since the quarter ended in terms of the comp?

Mike Barnes - *Signet Jewelers Ltd. - CEO*

I think that in the second quarter it was pretty consistent sales trend that we saw. So there was nothing remarkable about any one month in there. Since the second quarter has ended and now we have gone a full three weeks into the third quarter through three weeks of August, we are very pleased to say that the strength continues to hold. We have seen our sales remain pretty much in line with what we saw in the second quarter.

Obviously, we don't know what the economic future is going to hold for us, any of us, but we are cautiously optimistic that we are going to continue to execute at full throttle and our business will continue to be strong. We think we are well prepared to gain market share and well prepared for the Holiday Season.

Bob Drbul - *Barclays Capital - Analyst*

Okay, great. And then when you look at the price increases, I know you are not one to sort of give the price increases, but when you look at your ability to continue to raise price, do you think that you are nearing a level or are there any price sensitivities that you are leery of heading into the back half of the year?

Ron Ristau - *Signet Jewelers Ltd. - CFO*

We are always cautious with price increases, but we are also always provide a full range of pricing for customers so that as we take price increases we are cognizant of opening price points and a range of prices so that consumers can choose according to their pocketbook. We have successfully over a long period of time dealt with these rising commodity prices. We do not at this point in time see any major change in consumer behavior and we will continue to execute our price increases the way we have in the past. And we have been very successful with it, so no, there are no changes that we would call out.

Bob Drbul - *Barclays Capital - Analyst*

Okay, great. And my last question is, on the exclusive differentiated brand, could you give us a level of the penetration rate that percentage of sales in terms of what you view as the exclusive or differentiated percentage in the second quarter?

Mike Barnes - *Signet Jewelers Ltd. - CEO*

Yes, we have seen them continue to gain momentum as we mentioned. Last year as we have stated in the past, they were up to about 22% of our mix within our stores and that was up 300 basis points from the prior year. I don't know, Ron, I don't think that we have an interim percentage that we disclose on that, do we?

Ron Ristau - *Signet Jewelers Ltd. - CFO*

No, we don't disclose interim, but it has continued to improve, and we don't really set a target on it, it just continues to be driven by consumer, how the consumer reacts to these products.

Mike Barnes - *Signet Jewelers Ltd. - CEO*

So it has improved from the year end of 22% of our mix, but we don't have a number for you on that right now.

Bob Drbul - *Barclays Capital - Analyst*

Okay, thank you very much.

Operator

Jennifer Davis, Lazard Capital Markets.

Jennifer Davis - *Lazard Capital Markets - Analyst*

Hey, guys. Congratulations on yet another great quarter. And, Ron, thanks for that SG&A detail. That was really helpful.

Ron Ristau - *Signet Jewelers Ltd. - CFO*

Oh, good. I hoped it would avoid some of the questions we had on our last call. (multiple speakers)

Jennifer Davis - *Lazard Capital Markets - Analyst*

I know, right?

Ron Ristau - *Signet Jewelers Ltd. - CFO*

I am glad you found it helpful or useful.

Jennifer Davis - *Lazard Capital Markets - Analyst*

I have a couple of questions. Mike, first on the supply chain, could you talk a little bit about what you are seeing there? And if you are thinking about -- you know, back in 2006, you began testing the rough diamond initiative. I guess could you kind of give your thoughts on that? And then also was wondering what you are seeing in the competitive landscape with the mom-and-pops and higher commodity prices, what you are seeing in terms of store closing or kind of pressure there? Thanks.

Mike Barnes - *Signet Jewelers Ltd. - CEO*

Okay, thanks, Jennifer. As far as the supply chain, obviously that is something that we are extremely focused on. We've got some pretty big initiatives that we're working on there. We are looking at ways that we can strategically get closer to our suppliers and find ways to really strengthen the supply chain. We think that we have a great advantage competitively in the fact that we have the size and scale to really be able to work with people in a very large way. So we are looking at a number of initiatives. I wouldn't detail those out one by one for competitive reasons, but we think it is a competitive advantage that we have our ability to work closer with the supply chain, with our suppliers and we have got some initiatives that we are pretty excited about there that we think are going to help us secure the long-term supply of products that we need for our Company.

On the competitive landscape out there, especially vis-a-vis what is going on with the commodities, we think that we also have a competitive advantage in how we manage commodities because we do have a pretty substantial hedging program in place on commodities. And so I think the way that the commodities especially as they -- in a volatile way, tend to go up and down very quickly, I think it has less effect on us. We have a long lead time and an ability to really forecast out what the effect is going to be and adjust for it accordingly.

I think that is something that probably is not as easy for, as you mentioned, a lot of the mom and pops out there that pretty much just have to deal with what the day-to-day pricing drives and how it drives their business.

So I think it is a competitive advantage for us. I think that long term we will see it continue to help us increase our market share and I think that we will continue to see some consolidation in the industry. It obviously [slow] that the economy get better. Who knows where the economy is going right now based on all the volatility we have seen out there.

Our business, as I mentioned, has continued to remain strong even going into third quarter and we feel like we are well positioned.

Jennifer Davis - *Lazard Capital Markets - Analyst*

Great. Thanks and best of luck, not that you need it.

Operator

David Wu, Telsey Advisory Group.

David Wu - *Telsey Advisory Group - Analyst*

Hi, good morning, everyone. Congrats on a very solid quarter. First on the credit side, you mentioned that credit participation is up a little bit from last year and talked about the strong bridal business as a driver there. But can you also talk about perhaps how the approval rates have been trending and if you have made any meaningful changes at all with respect to the scorecards or the financing arrangements, such as the interest rates that you are charging?

Ron Ristau - *Signet Jewelers Ltd. - CFO*

Sure, we have made no changes in the scorecards, nor have we done anything to impact approval rates. Approval rates are about the same as they were last year. There have been no real movement in approval rates. As I mentioned, the bridal category, which is always strongly supported by credit because often times people in the bridal market are young people just getting started in their lives, does increase the penetration on a natural basis and also the fact that we have introduced the Neil Lane and Tolkowsky products, which are slightly higher in price would carry a little bit higher average financing. But nothing of any significance other than that and we just called it out because the bridal business, we think having our own in-house credit is a very, very strong competitive advantage and enables us to keep capturing market share in bridal.

David Wu - *Telsey Advisory Group - Analyst*

Great.

Ron Ristau - *Signet Jewelers Ltd. - CFO*

But we haven't changed anything from a -- there's no changes from a credit scoring perspective that is driving any of that.

David Wu - *Telsey Advisory Group - Analyst*

Excellent. And then secondly, can you talk about any new product launches in the fashion jewelry category in the back half of the year? Especially as you start to comp against the Charmed Memories launch in the fourth quarter?

Mike Barnes - *Signet Jewelers Ltd. - CEO*

Well, anything that we haven't launched yet we certainly wouldn't be talking about anyway. But we have got some great fashion jewelry offerings out there. We mentioned that the Le Vian range has continued to be strong for us as well. And the beads continued to be very strong for us. Charmed Memories has not even comped yet so we still have a big opportunity there. We have seen some great increases in the business for Charmed Memories.

And Pandora, as I mentioned, continued to have very strong double-digit comps and that's on a like-for-like comp basis. So we feel pretty good.

Another thing that I did mention in the call was that some of the fashion jewelry in the UK where we carry more fashion lines has done very well for us including DKNY and the Guess jewelry.

David Wu - *Telsey Advisory Group - Analyst*

Great, and then just lastly in terms of sort of the real estate out there, are you seeing better opportunities in the malls and any changes at all to your store expansion plans?

Mike Barnes - *Signet Jewelers Ltd. - CEO*

Well, our store expansion -- this year we had been quoting around 25 doors as we see the year coming into the back half and have a better, clearer picture of the store opening dates. It looks like we're probably going to open about 23 doors in the US total. And next year as we look forward to new store openings, basically we are still not seeing the kind of development we would like to see because we have an appetite to open a lot more stores than we are able to find great real estate for right now.

Having said that, as visibility becomes more and more clear for next year, we do think that we can open at least the same number of stores and probably even more than what we are opening this year in the United States. But we don't see the substantial increase in development that would be needed to drive that number much, much higher.

David Wu - *Telsey Advisory Group - Analyst*

Excellent. Thank you very much.

Operator

Anthony Lebiedzinski, Sidoti & Company.

Anthony Lebiedzinski - *Sidoti & Co. - Analyst*

Good morning. A couple questions, I realize that you don't want to give much details about the price increases but looking at price increases versus consumers trading up, which one do you think was a bigger factor in the second quarter?

Ron Ristau - *Signet Jewelers Ltd. - CFO*

I think it's a little bit of both, and the trade ups are occurring because as we indicated, we have the higher priced merchandise which has been well received as it relates to Neil Lane and Tolkowsky and products like that, but average prices have also gone up because of the price increase. Of the two if you were going to weight them, I would guess there is probably a touch more in the average price than it is trade up.

Anthony Lebiedzinski - *Sidoti & Co. - Analyst*

Okay, that's helpful. And the UK business, certainly a pleasant surprise in my view [over a year] now. Do you have any sense as what your share is of the UK market and also do you plan to do any website enhancements for your UK business?

Mike Barnes - *Signet Jewelers Ltd. - CEO*

We have been working on the websites in the UK. As I said, we are seeing double-digit increases on the web business there as well. It is something that we will continue to work on. We think that the web presence is very, very important to our Company on the go forward basis. It is where the world has gone to now. Social networking and the web is something that we intend to continue to focus on and invest in both in the UK and in the US market.

As far as share in the UK, we don't have any exact number on what our share of the market is there. We feel like -- we do know that we are far and away the market leader, but it is hard to get a good number on the UK market. It is a lot easier in the US, unfortunately. But we do track how we are doing retail wise and as I have mentioned, we definitely outperformed the overall discretionary retail market within the UK. So we feel like we are definitely holding our own on market share and possibly even gaining.

Anthony Lebiedzinski - *Sidoti & Co. - Analyst*

And my last question here is on the shareholder distribution, so certainly saw the good news about the cash dividend. So on an annualized basis, you will pay out about $35 million given your share count now. And you have well over $400 million in cash and will generate a lot of free cash flow this year. So what is your thinking going forward? Would you like to see the -- increase the dividend or is a share buyback still perhaps something you are thinking about?

Mike Barnes - *Signet Jewelers Ltd. - CEO*

Well, you know, this is something that the Board has been looking at for a long time, along with management here, and we thought it was very important to our shareholders to show that we felt like the financial strength that we had and the strong cash flows that we have been generating, we think that those are definitely something that we can continue to count on. And we felt it was a good time to give some value back to the shareholders and still retain the financial flexibility to make investments into our business, which is still the most important place where we can reinvest for the shareholder value.

This was a great start, quite frankly, and we are very, very happy to be able to announce the dividend today, and we think it is something that hopefully we will be able to add on to over the years as we move forward.

I wouldn't count out other methods of returning value to the shareholders. We keep our options open on that. Again, investing back into our business is our number one priority. We were able to do this and announce this dividend without having to change our financial flexibility in any way whatsoever and we are glad that we were able to -- shareholders -- I'm sorry, share repurchases is something that I wouldn't necessarily count out for the future. At some point in time, that is something -- I think is also a great way to return value to the shareholders.

And so we will continue to study and keep that open for the future but this was just a fantastic start for us, and we are very happy to be able to announce it.

Anthony Lebiedzinski - *Sidoti & Co. - Analyst*

Okay, thank you.

Operator

Ike Boruchow, JPMorgan.

Ike Boruchow - *JPMorgan - Analyst*

Hey, good morning. Congratulations on -- congrats on a great quarter, guys.

Mike Barnes - *Signet Jewelers Ltd. - CEO*

Thanks.

Ike Boruchow - *JPMorgan - Analyst*

I guess, Ron, I was pretty impressed with the product margins in the US. They have started to sequentially -- the rate of change started to come down in Q1 and then all of a sudden ticked back up from the 70 basis points increasing Q1 to 110 in Q2. Can you talk about exactly what drove that change and how should we think about the back half in terms of commodity costs and how that could be offset by your price increases and less discounting?

Ron Ristau - *Signet Jewelers Ltd. - CFO*

Well, first of all, I would say that when we started the year, we said we had an expectation that our gross margins in total would increase for the Company. We stay with those statements that the gross margin ratio in total will increase the gross merchandise margin is only a piece of that because we are also getting improvements in bad debts and leverage on the real estate costs which I indicated in the conference call.

The gross margin acceleration into the second quarter I think is more a factor of mix, more of the price to timing of some of our price increases. Price increases and the net effect of them over the year, they change a little bit by quarter, you get the most impact when you first start to do them so we do them usually in the April/May timeframe, so there's a little bit more impact in that second quarter and the commodity prices rise over time.

So I would say that the margins will be better but you can't naturally just take this quarter and project it forward. It does vary somewhat. (multiple speakers) that answers your other question. Okay?

Ike Boruchow - *JPMorgan - Analyst*

That's helpful. And then, Mike, you gave us some helpful color on the US and how that business trended throughout the quarter and quarter to date. Just curious about the UK. I know it is a smaller segment of your business but there has been a lot of macro headlines with problems over there. Any commentary on what you have seen in the last couple of weeks in that region?

Mike Barnes - *Signet Jewelers Ltd. - CEO*

Yes, I think definitely it is a much tougher marketplace right now and I think that within that marketplace on a comparative basis, we have outperformed the overall retail sector. It is difficult, but we are continuing, as I mentioned, to put new initiatives in place, new product ranges. We are leveraging some of the success that we have seen in the US with brands like Le Vian and Tolkowsky Diamonds, etc. We have the Amanda Wakeley, which is in the UK only, which is also a very popular range for us and has done very well.

So there are a lot of things we are doing. We are continuing our investments, as we mentioned and the UK business is still very stable for us, it is tough, but as things get better, we think we are well positioned.

Ike Boruchow - *JPMorgan - Analyst*

Okay, all right. Thanks. Best of luck, guys.

Mike Barnes - *Signet Jewelers Ltd. - CEO*

Thank you.

Operator

Bill Armstrong, C.L. King and Associates.

Bill Armstrong - *C.L. King & Assocs. - Analyst*

Good morning. Just to kind of follow up on that last question, so you have now had two straight quarters of positive comps in the UK and it looks like you have also reduced the number of store closings you are planning for this year there. So in light of the generally difficult macro environment in the UK, what are you seeing that may be offsetting all that that would be driving positive comps and telling you to maybe not close as many stores?

Mike Barnes - *Signet Jewelers Ltd. - CEO*

Well, you know, as I said, I think that our business is pretty stable there right now. Yes, it was great to see as slight as it was, to see some sequential improvement in the comps and have another positive comp quarter. That is fantastic for us in that marketplace. It's the execution -- it's the training that we give to our team members and our associates and our store managers and the way that they execute and the great product offerings that we have out there.

At the end of the day, it is all about execution in product and I think that we are far and away the leader in those two categories and I think that the results show that.

Bill Armstrong - *C.L. King & Assocs. - Analyst*

Okay, and in the UK, you have got Le Vian and Tolkowsky? Are those new initiatives over there?

Mike Barnes - *Signet Jewelers Ltd. - CEO*

They are not fully rolled out yet, so we have been testing in the UK market, but we have increased doors in recent quarters.

Bill Armstrong - *C.L. King & Assocs. - Analyst*

Okay, so it is not a complete rollout yet. Will we see a complete rollout by holiday? Is that the plan?

Mike Barnes - *Signet Jewelers Ltd. - CEO*

You know, honestly I don't have the rollout plan for those two brands in front of me. But I do know that in the second quarter we increased doors, so that they are fairly new as Ron just kind of mentioned, and we have been increasing our doors. So I mean they are working, I will put it that way. We are seeing great, great business with those brands. Our exclusive and our differentiated brands in both the UK and the US continue to help us drive a very strong business performance.

Bill Armstrong - *C.L. King & Assocs. - Analyst*

Would those brands have been basically non-comp in the second quarter then, Le Vian and Tolkowsky in the UK?

Ron Ristau - *Signet Jewelers Ltd. - CFO*

Le Vian probably a little bit less because there has been some Le Vian but Tolkowsky, more non comp.

Mike Barnes - *Signet Jewelers Ltd. - CEO*

Yes, more non-comp. We definitely rolled quite a few doors on Tolkowsky in the UK in the second quarter.

Bill Armstrong - *C.L. King & Assocs. - Analyst*

Okay, and then in the US, is Tolkowsky completely rolled out now or are we still working on that?

Mike Barnes - *Signet Jewelers Ltd. - CEO*

No, we are still working on that as well in the US. So you know, with the success that we have seen so far, obviously we still have a long way to go in getting it rolled out so it will be a while before we see that on a comp basis.

Bill Armstrong - *C.L. King & Assocs. - Analyst*

Got it, okay, great. Thank you.

Operator

Rod Whitehead, Deutsche Bank.

Rod Whitehead - *Deutsche Bank - Analyst*

Hi there. Congratulations again on a good quarter. Just coming back to the prices. Firstly, Pandora have basically said they have had a big problem and they feel that they put their prices up too quickly and too much. So first, I was wondering whether just in the last month or two you have seen the same resistance to Pandora higher prices that they have seen elsewhere in the US, they have specifically said their sales are down 30% in the US.

But secondly, moving away from Pandora, like Pandora, you have seen a big increase in the gross margin despite higher input costs. At what point should we be concerned that you might be being too aggressive on price increases? How do you yourself kind of monitor that issue?

Mike Barnes - *Signet Jewelers Ltd. - CEO*

Well, on the first question, regarding Pandora, we continue to see Pandora be a very strong business for us at Jared, and we continue to see strong double-digit comps. I think that if you look at the way we manage that business and how we assort it and how we choose our SKUs that we have done a very good job remaining in the sweet spot for our customers in both price and what we are offering to them in terms of newness and fashion.

So that business continues to be strong for us. I think a lot of it has to do with the fantastic execution that the team has done both here at the home office and in the field. So that it remains strong. As far as price increases and increased gross margin, a lot of the gross margin increases, as Ron has mentioned earlier, come through productivity, better bad debt percentages, etc., and we have said in the past that our gross merchandise margins, we would keep them relatively in line with prior years.

How do we monitor that? Very, very carefully is how we monitor it. We watch the sales reaction with any price increases that we do at any time on a very detailed level and we put a lot of work and study into it in advance. And we have said in the past if we see an overall net negative impact from price increases that we would have to really consider that on a go-forward basis. But so far again, I think the team has just done a fantastic job of planning it well, executing it well and following up with very careful look at sales post any price increases that we have done.

Ron Ristau - *Signet Jewelers Ltd. - CFO*

And, Rod, just again point out, we always maintain a range of pricing for our consumers and a range of price choices, so we have been very successful at this, and our price increase program, as Mike indicated, very artfully and skillfully done and we have seen no change.

Rod Whitehead - *Deutsche Bank - Analyst*

Thank you.

Operator

John Baillie, Societe Generale.

John Baillie - *Societe Generale - Analyst*

Hi, good morning, gentlemen. It's John Baillie. Just on the real estate markets on both sides, just wondering in the US malls where certainly in (inaudible) reviews you are paying base rents. Given the strength of your sales, how close are you getting to trigger incremental payments on the UK stores as you get the good like-for-like growth?

And secondly in the UK, with rent reviews, what is your experience? Are you getting unchanged rents or even cut in rents as the reviews come out?

Ron Ristau - *Signet Jewelers Ltd. - CFO*

Let me take that, John. The percentage rent is not significant. We continue to leverage our real estate costs and continue to believe that that will be true in the future, so while we do occasionally run into a percentage rent situation, it is well backed into our forecast and not a significant issue for us.

Relative to real estate costs, real estate costs continued to be -- there always have to negotiate on real estate costs, we do see in some of the areas in the UK that are falling out of favor, people willing to make rent concessions and we do get some benefits, but it is in the tune of 100s of thousands, maybe a couple million dollars. It is not all that significant to us.

We work at it constantly, but real estate prices have been stubbornly slow to adjust to some of the new economic realities, so it is an ongoing effort for us.

John Baillie - *Societe Generale - Analyst*

So you saying there is no real upward pressure on either side of the pond? Is that the reading?

Ron Ristau - *Signet Jewelers Ltd. - CFO*

No, we are not seeing any unusual pressure or other than a normal pressure on real estate prices, no.

John Baillie - *Societe Generale - Analyst*

Thank you.

Tim Jackson - *Signet Jewelers Ltd. - Director of IR*

Hello, operator?

Operator

David Berman, Berman Capital Management.

David Berman - *Berman Capital Management - Analyst*

Hi, guys. Great job on the numbers and the dividend. We want to see more dividends and share repurchases so good job from our side. Just wanted to ask you a question on the cost increases of gold and things like that.

There is obviously a lag effect because your inventories are at a lower cost, but the question becomes how do you decide -- how are you deciding when to raise your prices? Are you waiting for the prices of your cost to go up or are you doing it now? And there could be a windfall benefit obviously in your inventory and how much is that roughly?

Ron Ristau - *Signet Jewelers Ltd. - CFO*

Well, David, pricing, we take -- first of all, the first person we think about when we think about pricing is the consumer, and not putting through price increases rapidly if we do not have to. Our inventories work on an average basis so that we can see the average cost move over time and they move slowly and predictably in our systems because of the way that we manage them. And don't forget we are also, as Mike has pointed out, have active commodity hedging programs which tend to slow the rate of the increase in commodities versus the general market in our systems. So with all of those things working together, we do not seek to make windfall pricing changes in our business because we are focused on the consumer more than anyone else or on short-term profit capabilities.

So that really would not be something that we would look to do. We try to be predictable on our price increases. We try to do it at certain points in time during the year and certainly as we are getting ready for Christmas and holiday and the preparation of our websites and our catalogs and everything, we kind of lock in our pricing and don't move too much beyond certain points of time in the year. So I hope that answers your question.

David Berman - *Berman Capital Management - Analyst*

Yes, but at some point, obviously you're going to have to raise prices and sales, some of the gold stuff that you sell, and whether the customer likes it or not, I presume? I mean it just is what it is, right?

Ron Ristau - *Signet Jewelers Ltd. - CFO*

It is what it is, and we do raise prices on a predictable timeline for our consumers in most cases. Being that we do it, David, let me try to be less obtuse. We do it to a certain point in time. We do not do it in general past August or September because number one, we know what the prices are going to be based upon our inventory cost analysis, how it is going to roll through. We have already made those decisions and can see that coming so we know what our margins will be in the second half of the year.

We will take a look at that again after the Christmas and Valentine's Day timeframe, but with an inventory turn that moves in round numbers about once a year, we have got predictability in those rates and costs forward at least over a six-month timeframe.

David Berman - *Berman Capital Management - Analyst*

So our point of view of cost of inventory, I presume the market value of the cost is a lot how higher than what is shown in the books?

Ron Ristau - *Signet Jewelers Ltd. - CFO*

Yes, and that's -- that would be true if we were now to replace the inventory today, it would cost us much more in total, but luckily we never have to do that. We only have to replace as we sell.

The second thing is it speaks to the quality of our inventory program because don't forget, our inventory costs are slowly going up on a per item basis as the commodity costs roll into the inventory and for us to report on the increase sales only a 6% increase in inventory is really an outstanding job in inventory management by our teams in both companies watching the unit SKU movements, editing the lines where we see any slow up in the turn on SKUs and buying into those things that are performing well.

So we really have done an outstanding job on inventory management in order to limit the increases to what we have, to tell you the truth.

David Berman - *Berman Capital Management - Analyst*

I guess given the nature of your business, inventory management is probably more important than almost any other retailer, so --

---

Ron Ristau - *Signet Jewelers Ltd. - CFO*

Inventory management is key. We do have the one benefit of other retailers that our inventory doesn't turn bad as quickly as some other lines. But we are very focused on inventory management and supported with an excellent team in our impact teams and excellent system support. So it is a true competitive strength for our Company.

David Berman - *Berman Capital Management - Analyst*

Yes, no -- but I meant especially from a [price] point of view because obviously the values are high and you have got to really control it very carefully. But anyway, good job and thank you very much for the great results. Well done, guys.

Operator

[Michael Lopiano], Fidelity International.

Michael Lopiano - *Fidelity International - Analyst*

Gentlemen, congratulations on the great results. But how are you guys thinking about returns. You have a cash pile now which is about 15% of your market cap, how are you thinking about returns on incremental capital versus share buybacks and organic reinvestment given that returns on capital organic and investment issues are probably 20%, 25% at best. [Thus where your] share prices trading at versus most measures intrinsic value which suggests that you are probably at least 50% undervalued.

It just seems to me that buybacks can be very accretive at the current juncture. What are your thoughts?

Mike Barnes - *Signet Jewelers Ltd. - CEO*

Yes, I think buybacks are a great vehicle as well, quite frankly. But we also think that dividends are -- as I said ,we are very pleased that we did announce a dividend and if you look at the ongoing economic environment and the volatility that is out there, I think that really just speaks to the strength of our Company. So this was a really good start for us. We think initiating an ongoing dividend of $0.10 a share which would equate to $0.40 annually, is a great start. It doesn't mean that it is the end-all finalization of us looking at our capital structure and our balance sheet. That is something that is going to be ongoing.

The management and the Board here take that very seriously. We needed to start somewhere and this was a great way for us to start and give back some value to the shareholders. We will continue to look at other alternatives and it doesn't mean that we wouldn't use other distribution methodologies including share buyback in some point in time in the future. But right now with the opportunities that we have for our businesses, and with the situation of where the economy is at and the fragile nature of it, we think it is a good start and we should just take things step-by-step.

Michael Lopiano - *Fidelity International - Analyst*

Great. Thanks very much. Take care.

Operator

[Michael Friedman], Cumberland.

Michael Friedman - *Cumberland Associates - Analyst*

Good morning. Thanks for taking my question. I guess I want to chime in similarly with the previous gentlemen who probably owns a lot more stock than I do. I commend you on a great quarter. I commend the Board for taking the first step in implementing a dividend. But just looking at the stock market over the past few weeks, you don't often have opportunities to buy a business as strong a quality as yours for four times EBITDA or seven times earnings ex cash. And with $440 million sitting on your balance sheet and no long-term debt, to the extent the Board got comfortable implementing a dividend, I would urge you strongly to try to get comfortable maybe spending some of that -- some to buy back stock should it trade at evaluation anything like that in the future because it is extraordinarily accretive. The opportunity doesn't come around terribly often. And kind of whether you have $300 million plus theoretical debt capacity, a lot higher than that on your balance sheet or $400 million, you could be doing something very accretive.

Mike Barnes - *Signet Jewelers Ltd. - CEO*

Thank you for the comments. And I agree with you. It is something we need to watch very carefully. I will make sure that we do keep it as a Board topic with our Board and we will see how things develop on a go forward basis. Again, we just feel like it was a great way to start showing some value and sharing some value back to the shareholders and we will be looking at other alternatives as we move forward through time.

Michael Friedman - *Cumberland Associates - Analyst*

That's great. It was a great start and I commend you on it and keep up the good work.

Mike Barnes - *Signet Jewelers Ltd. - CEO*

Thank you very much. Appreciate that.

Operator

(Operator Instructions). David Berman, Berman Capital Management.

David Berman - *Berman Capital Management - Analyst*

Hi, just regards the dividend question, I just wanted to revisit that for a second. What -- in terms of the repurchasing, do you know what the accretion would be? Do you have a sense of how much it would be if you were to buy back stock?

Ron Ristau - *Signet Jewelers Ltd. - CFO*

Sorry, David. I'm not sure we understand your question. Accretion?

David Berman - *Berman Capital Management - Analyst*

Yes, the accretion to earnings per share. Do we have a sense of how much it would be -- when you did the calculation dividend versus the share re-buyback? Do we have a sense for that?

Ron Ristau - *Signet Jewelers Ltd. - CFO*

That depends upon how many shares you buy back and at what price you buy them back at, I suppose.

David Berman - *Berman Capital Management - Analyst*

No, no, obviously, but I am just saying because my sense is that (multiple speakers)

Ron Ristau - *Signet Jewelers Ltd. - CFO*

Our sense is that the dividend -- we thought that the dividend was a good place to start, as Mike has said. We feel that it rewards our shareholders on a long-term basis. It represents long-term belief in the strength of our operating model, and therefore, we chose to begin cash distributions with a dividend, and in the future (multiple speakers)

David Berman - *Berman Capital Management - Analyst*

Yes, I just wanted -- the only reason why I asked -- and I am pleased that you just articulated what you did was because I am in agreement with what you did and disagree with the gentleman before about using it for share buybacks. And I just wanted to make -- just share with the audience that I think you did do that calculation and do believe that the dividend was a superior method of returning shareholder cash.

Ron Ristau - *Signet Jewelers Ltd. - CFO*

Well, thank you. We appreciated it and we understand the ongoing debate, which is a very interesting growing debate, so we appreciate the comment. Thank you.

David Berman - *Berman Capital Management - Analyst*

Yes, thank you very much.

Operator

As there are no further questions in the queue, that will conclude today's question-and-answer session. I would now like to turn the call back for any additional or closing remarks.

Mike Barnes - *Signet Jewelers Ltd. - CEO*

Thank you for joining the call today. Our next scheduled results call is for the third-quarter results and this is expected to be on November 22. We'll look forward to speaking to you all then. I hope to see many of you at the IR day in New York on Tuesday, October 4. Thank you all.

Operator

That will conclude today's conference call. Thank you for your participation, ladies and gentlemen. You may now disconnect.
