Tailoring the luxury experience

The Luxury and Cosmetics Financial Factbook 2019 Edition

Building a better working world

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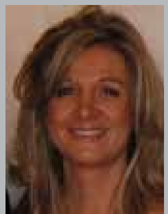

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Tailoring the luxury experience

EY-Parthenon vision for the future of the luxury industry and the challenges for heritage and digitally native brands

This year's report confirms that the trend that has been witnessed in the luxury goods industry in recent years is continuing, with fast growth in the premium, entry to luxury, perfume, and cosmetics categories.

The year 2019 marks a new era for the luxury fashion and cosmetics players; the rules of the game have changed and old winners must learn how to play differently to stay at the top. According to EY, those who have excelled in the past need to know how to redefine themselves, while preserving their identity. They must find ways to *tailor a unique luxury experience* for each customer, beyond the product offered. Traditional players face competition from digitally native brands, or newborns with a strong e-commerce and social media presence, a diversified go-to-market strategy, and loyal customer base, all derived from an innovative identity that feels closer to the new generation of luxury shoppers.

The newcomers are giving shape to a new paradigm revolving around the concept of *"coolness,"* featuring exclusivity, the ability to provoke and disrupt, the desire to reach customer intimacy, the willingness to communicate a purpose and, of course, *sexiness*. Their reliance on online channels to grow and achieve sales has put into question the relevance of brick-and-mortar retail in the new era.

Indeed, the future of retail has been thoroughly debated in recent years, finding a way to support in-store traffic after the rise of digital (-30% store traffic from 2012 to 2018). The numbers of store closures have been surpassing the numbers of store openings. However, despite the fact that more than 70% of purchases are influenced by online channels, physical transactions remain almost 90% of the total purchases. The brick-and-mortar footprint remains a "must have," although the retail channel, usually EBITDA dilutive for multichannel companies, is under increasing profitability pressure. How do companies provide required shareholder returns? How can they drive high-conversion traffic to stores? How do they make sure customers entering the store find what they are looking for, enjoy a stunning shopping experience, make purchases and exit the store feeling even more emotionally engaged with the brand?

Executive summary

To win the game in an arena where the most important concept is that of coolness, fashion companies have many cards to play that can lead to an improved retail conversion rate. The areas to invest in should be intelligence (predictive analysis), product development (including agile development and digital prototypes), lean production, and optimized merchandising and buying. The in-store customer engagement should be supported by digital technologies and evolved loyalty programs.

The beauty and cosmetics industry is also undergoing rapid transformation. It has been evolving from a female-only industry to include men and men-specific products starting in the early 2010s, and it is now expected to develop a gender-neutral approach. Industry products must reflect such evolution by reaching higher standards of personalization and inclusion, providing gender-specific products is no longer enough to meet consumers' evolving tastes and beauty ideals. Product offerings today should result from a careful analysis of the consumer and be tailored to their skin type, needs and color, all of which can be achieved through new technologies, including, but not limited to, skin detection and recognition tools.

Consumers expect brands to share and reflect their growing passion for social and environmental causes, as well as concerns over risks related to long-term exposure to chemical substances, resulting in, one the one hand, more natural and organic labels, and on the other, a growing appeal for minimalistic beauty based on tradition, rituals and simple regimens — something previously seen in Japan. The growing level of product sophistication will see the role of influencers and makeup artists rise as they become a key vehicle to inform consumers about the new offering and its potential.

The key question now is who is better positioned to successfully tailor the luxury experience and succeed in this new landscape: heritage, digitally native or heritage brands that understand the new rules of the game?

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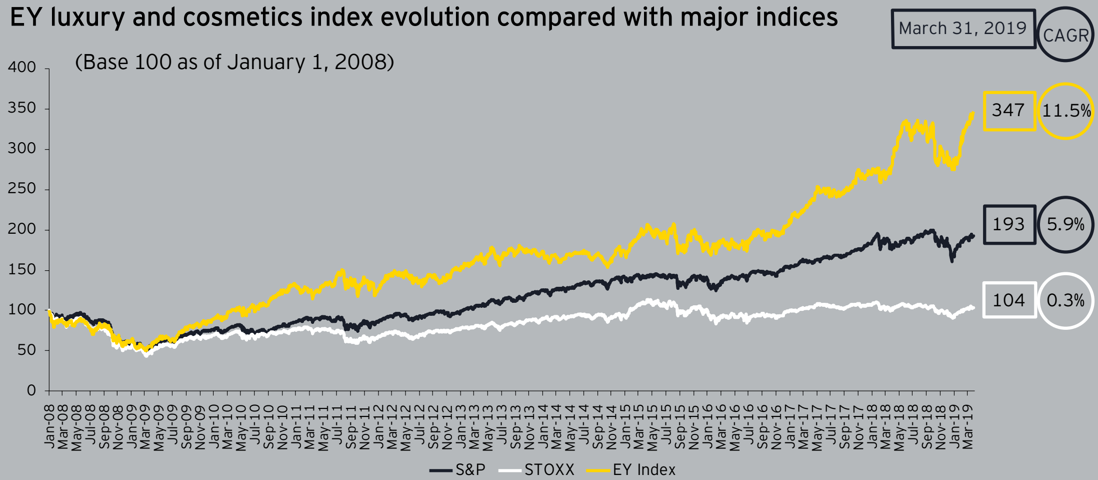
Index evolution

The EY luxury and cosmetics index (represented by the companies included in *The Luxury and Cosmetics Financial Factbook 2019 Edition*) has outperformed the market over the last 11 years with a total return of 210% and with an average yearly return of 11.5%.

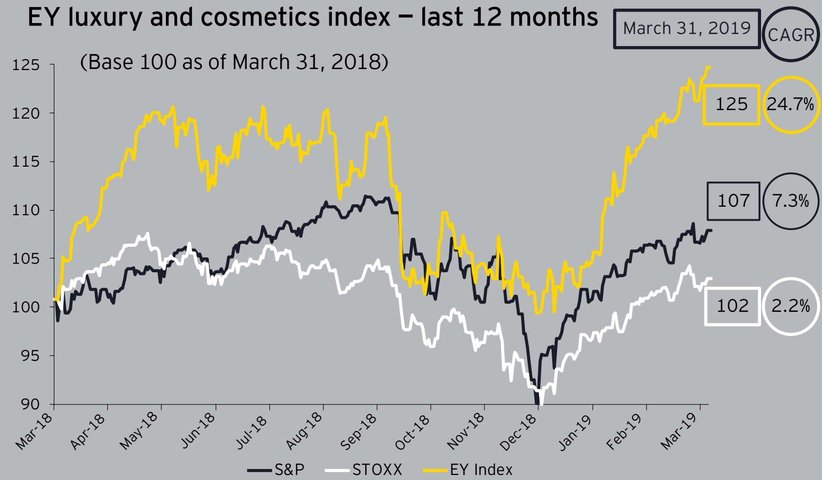
During the last year (from March 2018 to March 2019), the EY Index performed better than the Standard & Poor's index (S&P). The total return of the EY luxury and cosmetics index is higher, with a yearly return of 24.7% (compared to 7.3% of the S&P and 2.2% of the STOXX index). Both in the luxury and cosmetics sectors, growth is mainly driven by an expanding consumer base in Asia, particularly China, as well as profit expectations derived from technological disruption and luxury e-commerce. Some insights about the stock performance of the main companies included in the EY index are reported below.

- Last year was marked by the IPO of UK luxury clothing e-tailer Farfetch, whose stock surged 35% above the last offer price in its trading debut on September 21, 2018, raising $884m to help fund ambitious expansion plans. The company sold 44.2 million shares priced at $20 each, above its $17 to $19 previously anticipated price range, reflecting strong investor demand and growing strategic relevance of web sales for high-end brands. Furthermore, "marketplace" companies, such as Farfetch, often trade at a higher premium than traditional retailers because they don't carry the risk of being stuck with unwanted product. During the IPO, Farfetch also realized a private placement: Kadi Group Holding (a subsidiary of JD.com, and Farfertch's strategic partner fueling expansion plans in China), agreed to acquire one-third of the shares needed to keep its holding of the company (13.9%) unchanged.
- Louis Vuitton Moët Hennessy (LVMH) achieved a record year with €46,826m in revenues in 2018, an increase of 10% over the previous year. Organic revenue growth was 11%, driven by the fashion and leather goods division. Accordingly, it increased its market capitalization by more than 28% (compared to March 31, 2018), reaching €158,157m. LVMH also announced a strong first quarter in 2019 (+11% sales on a like-for-like basis), which was welcomed by the stock market with a record high share price performance.
- Safilo's net sales for 2018 equaled €962.9m, down 4.0% at constant exchange rates and 7.0% at current exchange rates compared to €1,035.3m in 2017. The negative performance is in line with management's expectations following the termination of the Céline and Gucci license agreements, the latter of which changed to a four-year production agreement.
- L'Oréal reported +7% organic sales growth in FY18, its best in at least a decade, fueled by significant investments in marketing and digitalization. The L'Oréal Luxe and Active Cosmetics divisions both recorded double-digit growth. The big brands were the star performers, particularly in the L'Oréal Luxe division, where Lancôme's sales crossed the €3b mark, and in the Active Cosmetics divisions with star brands La Roche-Posay, Vichy and SkinCeuticals. In terms of geography, the Asia-Pacific market recorded the biggest growth (+24.1% on a like-for-like basis compared to 2017). The record performance was rewarded with a 30% growth in market capitalization compared to March 31, 2018 (reaching €129,938m).
- Kering's market capitalization has increased, reaching €62,367m on March 31, 2019, from €48,497m on March 31, 2018. Kering's houses delivered +26% revenue growth in 2018, driven by the Gucci brand (which recorded +33.4% compared to the previous year).

EY luxury and cosmetics index evolution compared with major indices

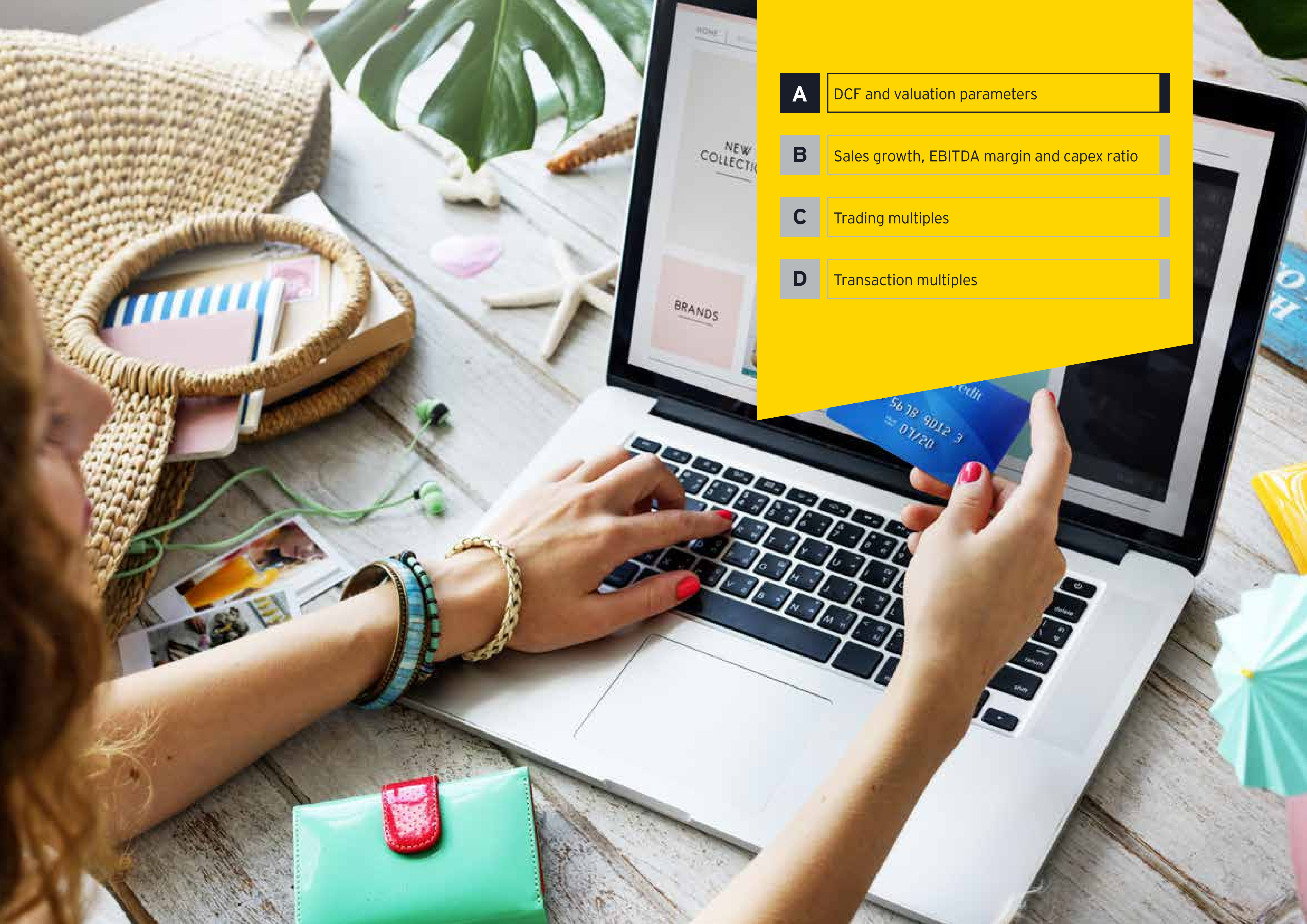


EY luxury and cosmetics index – last 12 months



Note: The EY index is a representation of the luxury and cosmetics companies analyzed within the factbook. A specific weight has been attributed to each company included in the EY index based on its market capitalization. The relative weights have been revised for each company's inclusion after its initial public offering (IPO) after eventual delisting and semi-annually. Finally, the evolution of the EY index has been compared to those of the S&P 500 and STOXX Europe 600 indexes using January 1, 2008, as a starting date (rebased to 100). Compounded annual growth rate (CAGR) is compounded by the average growth rate. The panel is principally comprised of those luxury companies listed in main luxury markets identified and other relevant companies. Data is drawn from S&P Capital IQ.

Financial parameters



A DCF and valuation parameters

B Sales growth, EBITDA margin and capex ratio

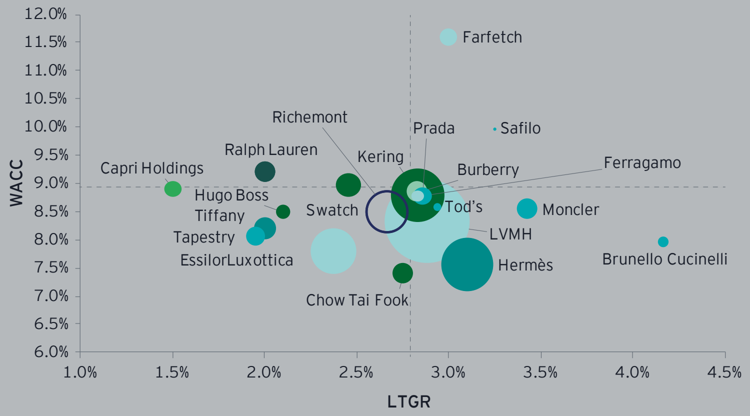
C Trading multiples

D Transaction multiples

A DCF and valuation parameters

On average, market capitalization of the luxury companies in the panel has increased by 14% compared with 2018, mainly driven by Kering, LVMH and Hermès (respectively, recording +29%, +28% and + 27% market capitalization growth)

- The average increase in market capitalization has been 13.6% compared with last year, with LVMH surpassing the €150b threshold.
- The weighted average cost of capital (WACC) ranges from 7.4% (Chow Tai Fook) to 11.6% (Farfetch). Farfetch's higher cost of capital can be attributed to the company's lack of profitability so far, as well as the risk of not securing partnerships with new brands, together with the fact that it is a new, less consolidated, and more unpredictable business.
- Luxury companies present on average an indebtedness of 1.1% higher compared to last year. Some of the causes of increased indebtedness are: (i) several acquisitions occurred during the year (e.g., Richemont's acquisition of Yoox Net-a-Porter), (ii) repurchases of shares (e.g., Tiffany repurchased 3.5 million shares for approximately $400m), (iii) dividend distributions (e.g., Prada used its funding primarily for distribution of dividends for €197.6m, as well as capital expenditures and cash investments, and (iv) low market interest rates encouraging new debt.
- The average long-term growth rate (LTGR) is in line with last year's figure (2.7% in 2019, compared with 2.9% in 2018), confirming the expectations of growth in the sector, albeit slightly less optimistic.



Note: The bubble size reflects market capitalization. Dotted lines represent average values.

Sources:

- WACC and LTGR: based on consensus of a sample of more than 150 independent broker reports (an average of 4 per company).
- Market capitalization and beta: EY analysis based on public data sourced from "S&P Capital IQ" data, www.capitaliq.com, March 31, 2019.
- Gearing: EY analysis based on public data sourced from companies' FY18 financial statements.

Luxury companies	Market capitalization (€m)	WACC	Gearing	Beta	LTGR
LVMH	€158,157	8.3%	4.2%	1.25	2.9%
Kering	€62,367	8.8%	2.7%	1.30	2.8%
Hermès	€60,300	7.6%	(5.6)%	0.65	3.1%
EssilorLuxottica	€44,456	7.8%	5.1%	0.77	2.4%
Richemont	€36,247	8.5%	(7.1)%	1.00	2.7%
Swatch	€13,116	9.0%	(6.9)%	1.01	2.5%
Tiffany	€10,601	8.2%	3.7%	0.68	2.0%
Moncler	€8,993	8.5%	(5.2%)	0.59	3.4%
Burberry	€8,973	8.9%	(12.1)%	1.10	2.8%
Chow Tai Fook	€8,863	7.4%	11.9%	0.66	2.8%
Ralph Lauren	€8,628	9.2%	(16.8)%	0.67	2.0%
Tapestry	€8,501	8.1%	1.1%	0.82	2.0%
Farfetch	€7,248	11.6%	(7.9)%	1.60	3.0%
Prada	€7,027	8.8%	5.0%	0.61	2.9%
Capri Holdings	€6,063	8.9%	25.9%	0.55	1.5%
Hugo Boss	€4,328	8.5%	0.8%	0.81	2.1%
Ferragamo	€3,165	8.8%	(5.3)%	0.65	2.8%
Brunello Cucinelli	€2,243	8.0%	0.8%	0.26	4.2%
Tod's	€1,397	8.6%	6.1%	0.44	2.9%
Safilo	€203	10.0%	22.5%	0.89	3.3%
Average		8.7%	1.1%	0.82	2.7%
Median		8.6%	0.9%	0.72	2.8%
Maximum		11.6%	25.9%	1.60	4.2%
Minimum		7.4%	(16.8)%	0.26	1.5%

*Tapestry: Coach Inc. changed its name to Tapestry in 2017 and includes Coach, Kate Spade and Stuart Weitzman.

**Michael Kors acquired Jimmy Choo in 2017 and Gianni Versace in 2018, following which it changed the Group name to Capri Holdings.

***EssilorLuxottica is the legal entity deriving from the merge of Essilor and Luxottica, completed at the end of 2018.

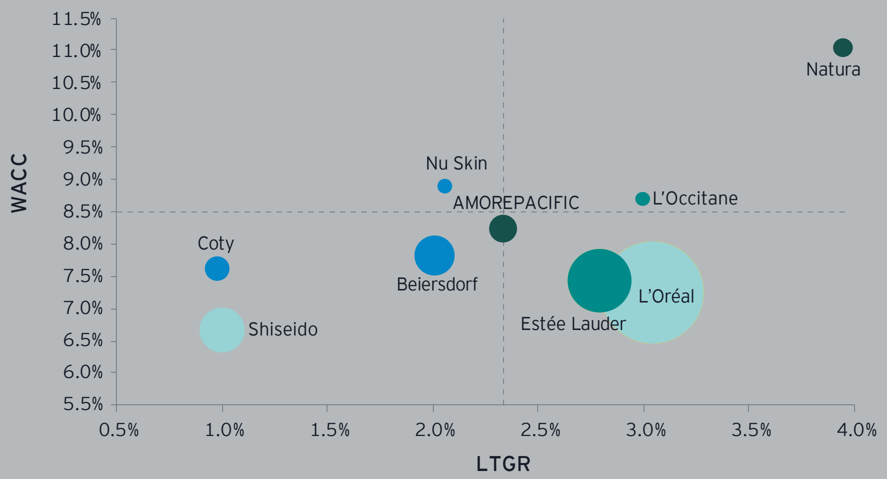
Notes:

- Companies are sorted by decreasing order based on the market capitalization in euros observed as of March 31, 2019 (one-month average).
- Gearing is defined as the ratio between the net financial position and enterprise value (EV) .
- Beta corresponds to levered beta measured on a weekly basis over a two-year period.

A DCF and valuation parameters

Market capitalization of cosmetics companies has increased on average by 16% compared with 2018, mainly driven by positive performance of L'Oréal (+30%), Shiseido (+26%) and Estée Lauder (+18%)

- The average WACC is 8.2%, in line with 2018 value (8.3%), with Natura's WACC remaining an outlier with a value of 11.2% (vs. 10.1% last year). Being based in Brazil, Natura's WACC is also affected by local valuation parameters.
- Once again, cosmetics companies show a higher average gearing ratio compared to luxury companies (7.1% of cosmetics vs 1.1% of luxury), with Natura and Coty raising the average. Both have had a structurally high gearing ratio. The average gearing ratio further increased after the acquisitions carried out in recent years (The Body Shop was acquired by Natura in 2017 and the 43 brands of Procter & Gamble (P&G) were acquired by Coty in 2016). Natura is carrying out a deleveraging strategy that has led to a significant reduction in the ratio, which is now half of the value in 2018 (from 47.3% in 2018 to 23.4% in 2019). Natura announced the acquisition of Avon in May 2019, thus, an increase in the gearing ratio in the short term is foreseeable.
- The average LTGR slightly increased to 2.3% in 2019 (vs. 2.2% in 2018), reflecting the investors' positive growth expectations.



Note: The bubble size reflects market capitalization. Dotted lines represent average values.

Sources:

- WACC and LTGR: based on consensus of a sample of more than 150 independent broker reports (an average of 4 per company).
- Market capitalization and beta: EY analysis based on public data sourced from "S&P Capital IQ" data, www.capitaliq.com, March 31, 2019.
- Gearing: EY analysis based on public data sourced from companies' FY18 financial statements.

- L'Oréal achieved €130b market capitalization after several acquisitions during FY2018: the French group acquired the South Korean e-commerce company Nanda Co. Ltd. to reinforce its presence in South Korea, Societe des Thermale de la Roche-Posay to sustain and reinforce the dermatologic position of the group, the German cosmetics company LOGOCOS Naturkosmetik AG, the American Pulp Riot and the Canadian augmented reality and artificial intelligence company Modiface Inc. to accelerate the digitalization strategy to provide a better beauty experience.
- Among the most notable changes in market capitalization are AMOREPACIFIC and Coty. The former, to continue its downsizing strategy, sold the Chartres Fragrance Factory to Christian Dior SA and suffered a weak domestic demand that highly impacted the performance and brought its market cap to €9.6m from its €14.4m 2018 value. The latter experienced a fluctuating share price impacted by supply chain disruptions and soft demand for its mass market cosmetics brands, resulting in a market capitalization decrease of around 35%.

Cosmetics companies	Market capitalization (€ m)	WACC	Gearing	Beta	LTGR
L'Oréal	€129,938	7.3%	(1.9)%	0.81	3.0%
Estée Lauder	€51,049	7.5%	2.1%	0.75	2.8%
Shiseido	€24,866	6.5%	0.5%	0.75	1.0%
Beiersdorf	€19,887	7.9%	(6.2)%	0.48	2.0%
AMOREPACIFIC	€9,699	8.2%	(5.4)%	1.18	2.3%
Coty	€7,424	7.7%	48.5%	0.89	1.0%
Natura	€4,578	11.2%	23.4%	1.05	3.8%
Nu Skin	€2,698	9.0%	1.1%	0.84	2.0%
L'Occitane	€2,432	8.5%	2.0%	0.16	3.0%
Average		8.2%	7.1%	0.77	2.3%
Median		7.9%	1.1%	0.81	2.3%
Maximum		11.2%	48.5%	1.18	3.8%
Minimum		6.5%	(6.2)%	0.16	1.0%

Notes:

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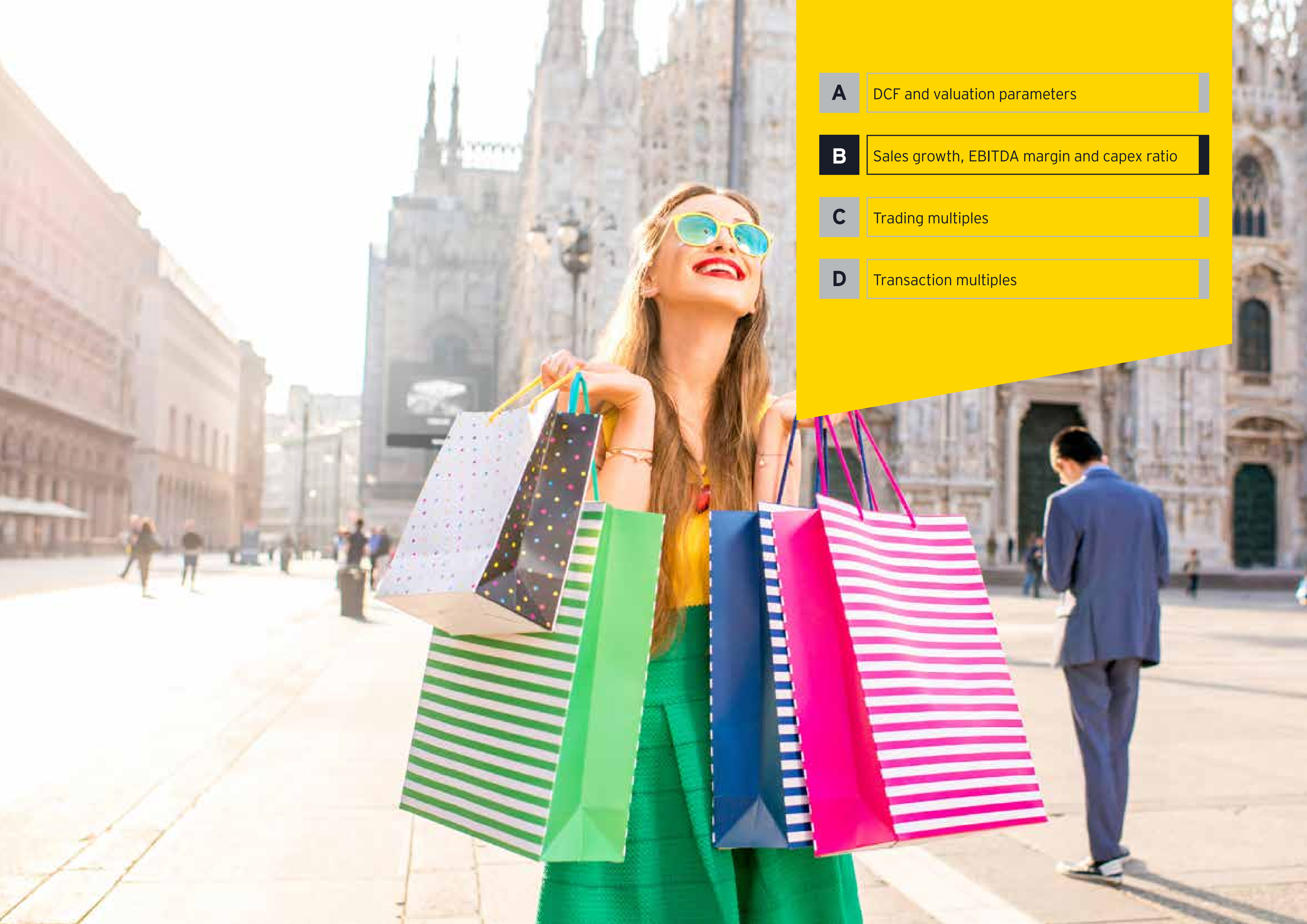
- Gearing is defined as the ratio between the net financial position and the EV.
- Beta corresponds to levered beta measured on a weekly basis over a two-year period.



A DCF and valuation parameters

B Sales growth, EBITDA margin and capex ratio

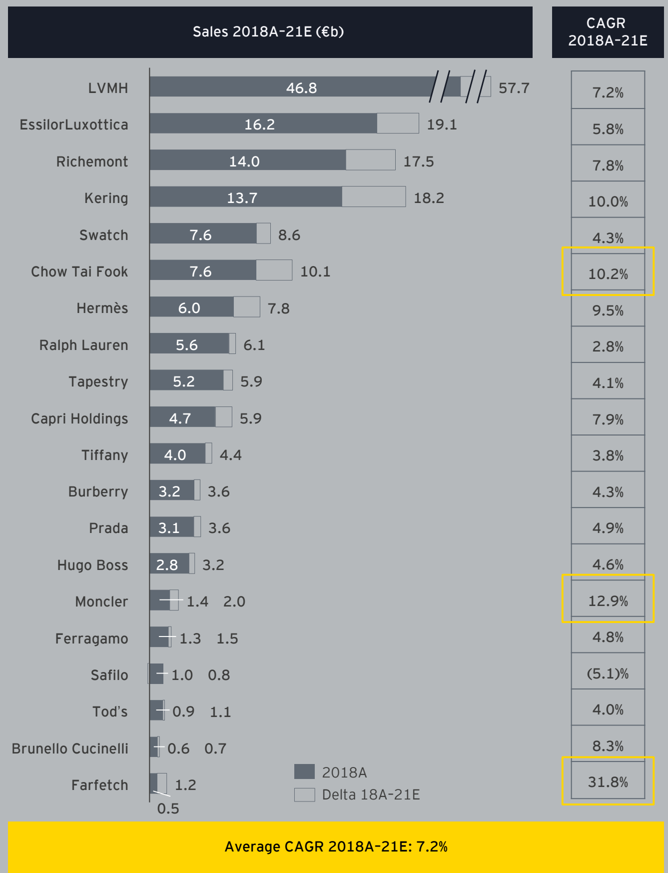
C Trading multiples

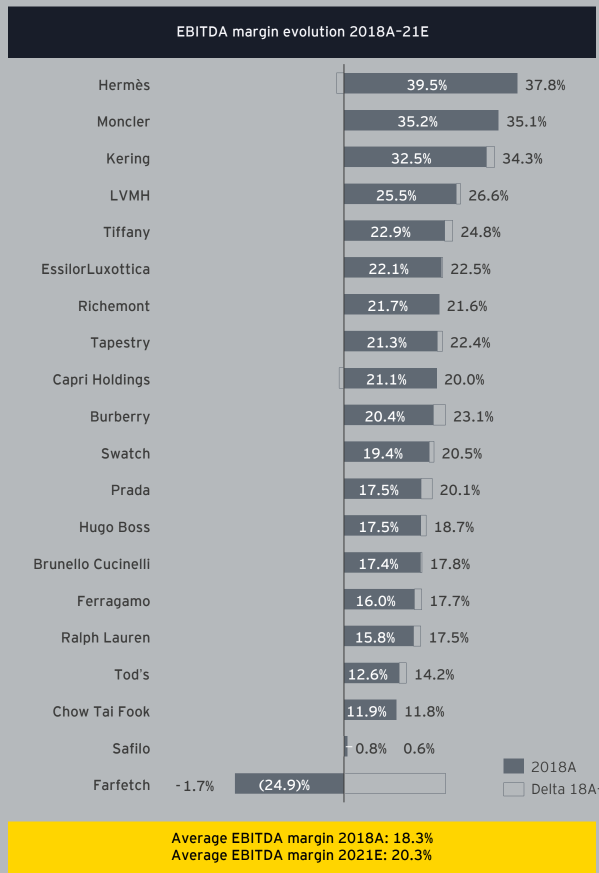
D Transaction multiples

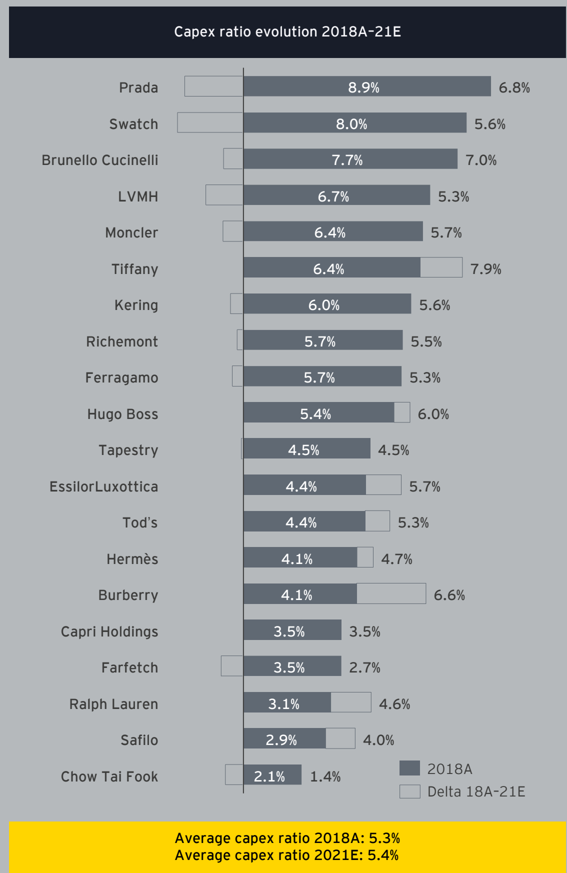
B Sales growth, EBITDA margin and capex ratio

Sales in the following years are expected to continue to increase, driven by fast-growing Asia-Pacific economies and evolving value propositions, resulting in positive industry performance

- Despite the evolving macroeconomic environment and the potential for disruption from shifting trading relationships, the luxury sector should continue a trend of sales growth for the next three years, driven by fast-growing Asia-Pacific economies and evolving value propositions globally (for instance, through the shift toward a digital experience and customization of products). Farfetch is number one in sales growth expectations, in line with the company's continuous sales increase (61.8% CAGR FY15–FY18). This increase in expected sales is also due to Farfetch and JD.com's (China's largest retailer) announcement that they will expand their strategic partnership to provide luxury brands in China.
- Margins are expected to be higher in 2021E (2021 expected) than in 2018A (2018 actual) for almost all panel companies. Expectations for the next three years have been revised to a milder future EBITDA margin (last year's expectations for the year 2020 saw an average EBITDA margin of 24.3% against this year's 2021 expectations of 20.3%). Reasons include the industry-wide move from offline to online channels, increasing costs for both online and offline distribution, as well as increased complexity from an organizational standpoint.
- The main investment priority remains developing well-integrated, omnichannel capabilities. The higher average capex ratio (+5.3% compared to 4.7% in 2017) reflects executives' continuous efforts to respond to industry digitalization, both in the physical channel as well as from a managerial standpoint throughout the purchase or development of advanced software. From an operational perspective, investment efforts were oriented at addressing the cost structure and improving productivity to preserve margins, due to structural changes in the industry and increased competition.







Note: Please note that the calculation of the average follows the simple average method.

B Sales growth, EBITDA margin and capex ratio

A historical analysis of luxury's KPIs and a forward-looking view of 2019E

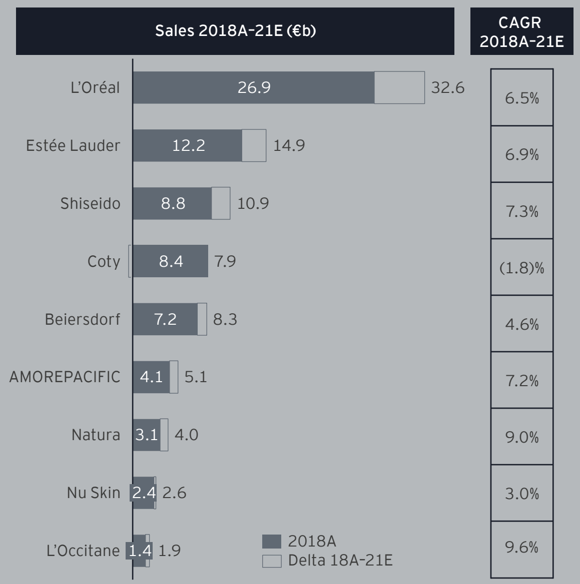
Note: the analysis has been performed like for like for the historical period. As a consequence, the averages may differ from previous editions of the factbook since the panel has changed. In particular, in 2019, Michael Kors, after the acquisitions of Jimmy Choo (in 2017) and Versace (in 2018), changed the name to Capri Holdings. In 2018, Luxottica and Essilor merged to form the new legal entity EssilorLuxottica. Furthermore, Farfetch was isolated from average calculations as it is an outlier, given its extremely high sales growth, as well as its negative EBITDA margin.
Please note that the calculation of the average follows the simple average method.

- The growth year-on-year (YoY) from 2018A–19E is weaker compared to previous years. However, this is mainly attributable to the fact that 2017A–18A growth was extraordinarily high due to several large acquisitions in the industry, such as Yoox Net-a-Porter by Richemont and the acquisition of Kate Spade by Tapestry (completed in FY18), which resulted in the aggregation of sales. In 2019, this trend is expected to stabilize as the industry becomes increasingly consolidated.
- In the upcoming years, luxury companies will continue to leverage investments in e-commerce and social media to connect (and sell) directly to customers. The strategy is shifting the balance of power between fashion houses and multi-brand retailers, traditionally considered industry power brokers. The direct-to-consumer strategy allows more control of how the products are presented and creates a more intimate connection with the consumer.
- The average EBITDA margin of the panel is fairly stable at around reflecting the ability to offset the additional costs faced by industry leaders related to maintaining stores and websites, as well as handling logistics and distribution.
- The average capex ratio is increasing for the third year in a row. Future investments will be especially driven by the need to (i) further develop omnichannel and e-commerce; (ii) build customer relationship management capabilities; and (iii) improve in-store experiences and invest in brand building. Prada remains the company with the highest capex ratio (ranging from 10.2% in 2014A to 8.9% in 2018A), with approximately 50% of the total capital expenditure of 2018 invested in the retail area, primarily for store restyling and relocation projects and, to a lesser extent, in the store openings of the period. Other capital expenditures were used to build up the manufacturing and logistics structures in Italy, improve the corporate areas, and fund the digital transformation process.
- Advertising expenses have remained fairly stable during the last few years, with growth mainly the result of to an increased focus on digital ad spending.

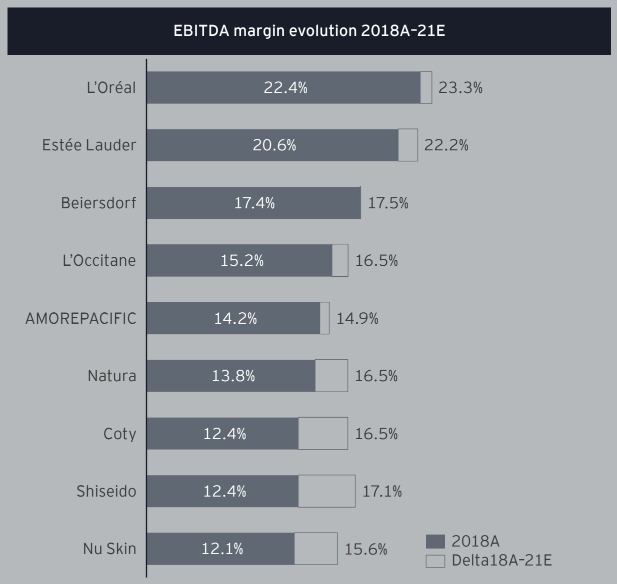
B Sales growth, EBITDA margin and capex ratio

Overall, sales growth in the following years will come from changing demographics characterized by aging consumers who want to appear young, new geographies (Middle East, Asia and Africa), and acquisition of niche and indie industry disruptors (e.g., rising independent brands focused on the authenticity of the product)

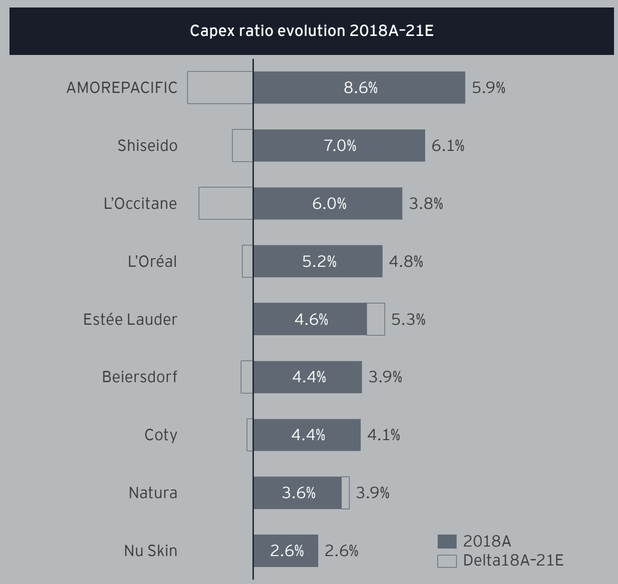
- Cosmetics companies are expected to register high growth in the next three years, albeit with slightly lower sales growth estimates compared to last year (average CAGR 2018A-21E of 5.8% vs. 2017A-20E expectations of 7.5%). Milder growth is mainly attributed to revised expectations of Coty (9.1% CAGR in 2017A-20E vs. (1.8)% CAGR of 2018A-21E), as the company announced it would restructure its operations and take a $3b write-down on the multibillion-dollar beauty business it acquired from P&G in 2016. Overall, sales growth in the following years will come from changing demographics (aging consumers who want to appear young), new geographies (Middle East, Asia and Africa), and the acquisitions of niche and indie disruptors from global brands.
- Margins are expected to increase in future years partly driven by (i) benefits and synergies achieved from the consolidation trend of the past years; (ii) willingness to pay a premium price for brands with a unique value proposition; and (iii) growing customer loyalty to a specific brand.
- Capex ratio, on average, has decreased since last year (5.4% in 2017A and 5.2% in 2018A) and it is expected to further decrease to 4.7% in 2021E. The company whose capex ratio is expected to increase the most in the 2018A-21E period is Estée Lauder (with an expected increase of 0.7%, followed by Natura with an expected increase of 0.3%). Estée Lauder plans to bring its capex budget to around 5% to 6% of sales over the next three years (from 4% to 5% historically) as management looks to invest in increased supply chain capabilities and capacity, as well as enhance the customer experience and further update some of its facilities.



Average CAGR 2018A-21E: 5.8%



Average EBITDA margin 2018A: 15.6%
Average EBITDA margin 2021E: 17.8%



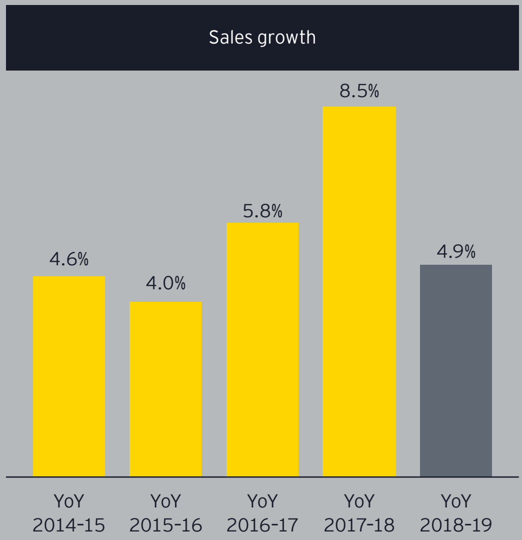
Average capex ratio 2018A: 5.2%
Average capex ratio 2021E: 4.7%

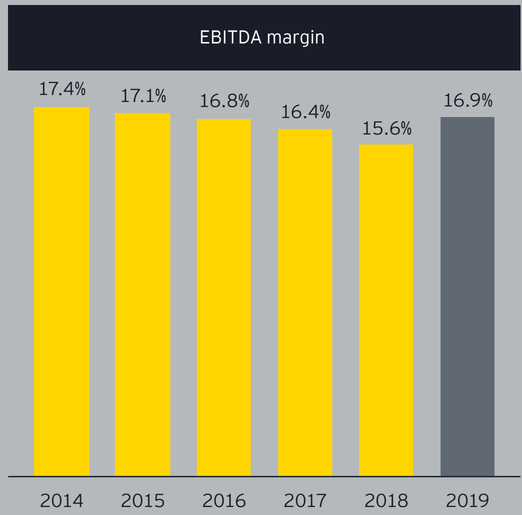
Note: Please note that the calculation of the average follows the simple average method.

B Sales growth, EBITDA margin and capex ratio

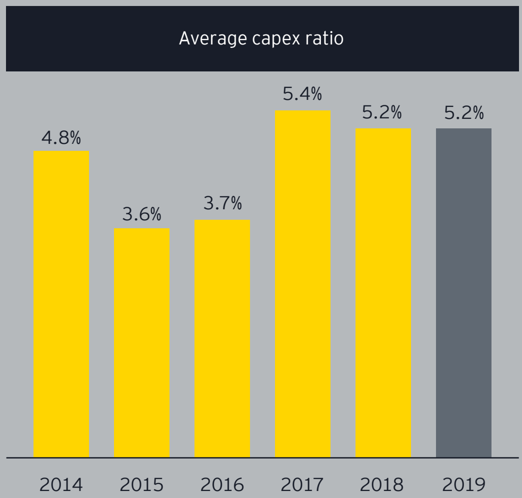
A historical analysis of cosmetics' KPIs and a forward-looking view of 2019E

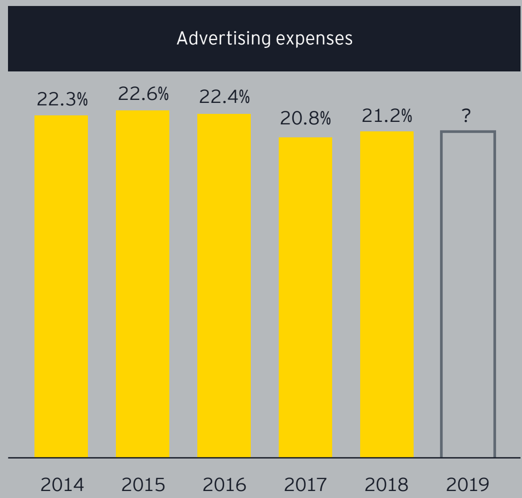
Average historical financials and consensus for 2019E





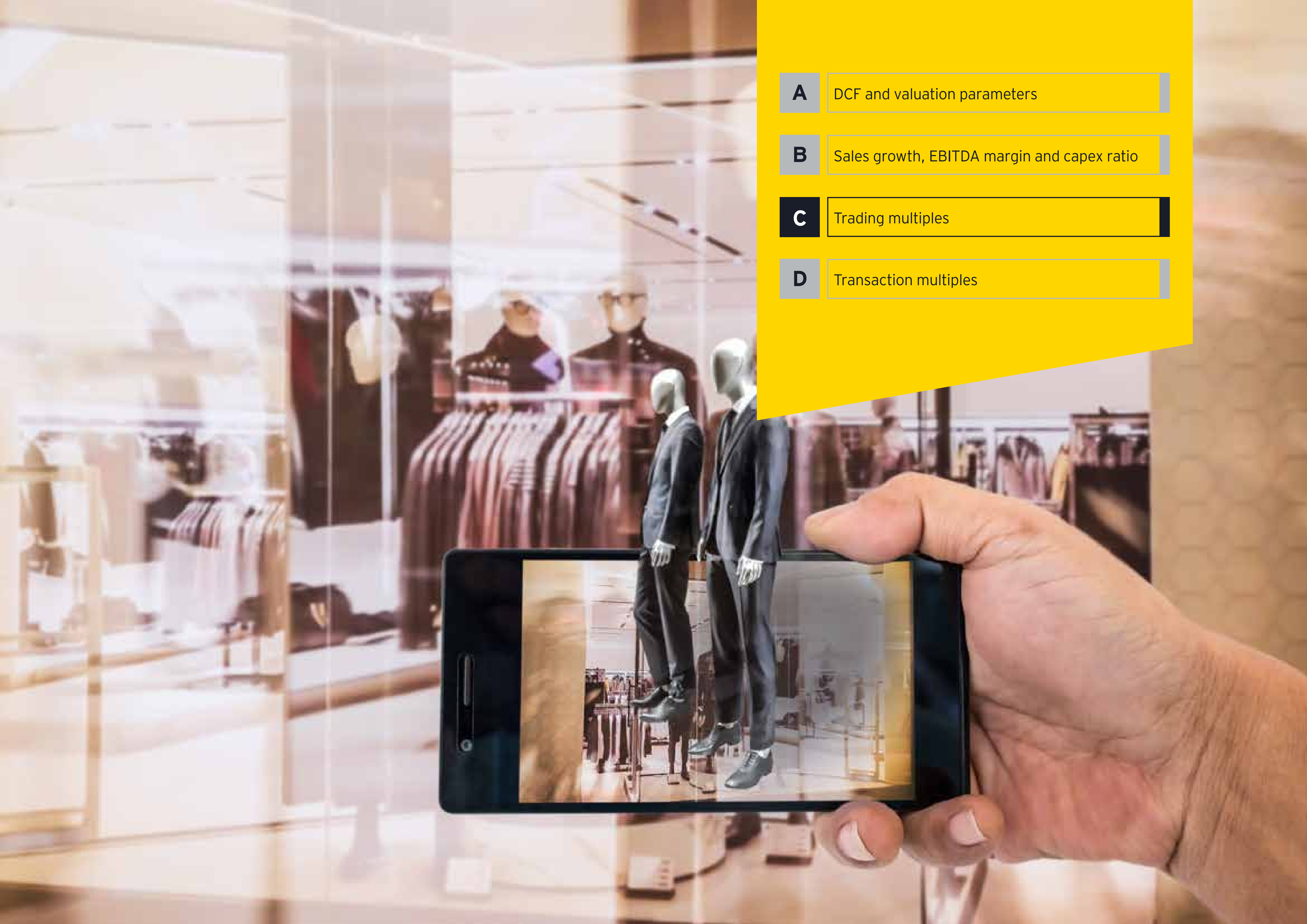
Average historical KPIs and consensus for 2019E





Note about YoY sales growth: Coty is excluded from the average of 2017A and 2018A YoY sales growth as fiscal 2017A financials have consolidated numbers for the acquisitions of the P&G beauty business as of October 1, 2016, which impact 2017 and 2018 YoY sales. Coty is included in the average again starting from 2019E. Similarly, Natura is excluded from the average of the same period, consequently due to the consolidation of numbers for the acquisition of The Body Shop (in 2017), which impacts the 2017A-18A YoY sales. Natura is included again starting from 2019E.
Note about advertising expenses: Nu Skin is excluded from the average of advertising expenses as they are lower than average due to a different business model. Additionally, Shiseido has been removed from the average in 2014A and 2015A since information for 2016A, 2017A and 2018A is not available.

- In the past three years the market continued to experience growth, driven by expansion of the high-income class and the rising number of consumers in emerging economies.
- In the cosmetics sector, average YoY sales growth has been high, ranging from 4.0% to 5.8% in the period 2016-17. FY18 registered record-high YoY value due to several large acquisitions and the consequent aggregation of sales that involved companies in the panel (for instance, Natura's acquisition of The Body Shop). The YoY sales growth is expected to return to its historical average value as M&A opportunities for megadeals decrease.
- The average EBITDA margin of the panel is fairly stable, although slightly decreasing, ranging from 17.4% in 2014 to 15.6% in 2018. The lower EBITDA margin in 2018 can be partly attributed to Natura's performance (-4% compared to 2017). The company has been rethinking its commercial strategy and regaining part of the market share lost in Brazil in the previous years. The strategy came at a margin expense as Natura (i) changed its sales rep commissioning model; (ii) increased marketing expenditures; and (iii) faced cost pressures from raw materials given the limited price elasticity.
- The average capex ratio expected in 2019 is in line with the 2018 value of 5.2%. Shiseido is among the companies that in 2018 committed the most resources to investments. The company plans on continuing this trend in the next three years, investing in supply chain management as it works to establish supply chain capacity.
- Companies are increasingly focusing advertising efforts on online marketing campaigns due to the prospected growth of e-commerce. The market is witnessing a trend of multinational companies setting up websites and brand-specific Facebook accounts and Twitter profiles in order to address local tastes with several products advertised as being available "only online." On average, advertising expenses are around 21%.



A DCF and valuation parameters

B Sales growth, EBITDA margin and capex ratio

C Trading multiples

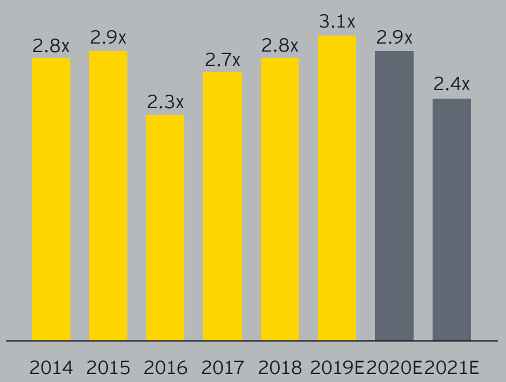
D Transaction multiples

C Trading multiples

Luxury multiples are further rebounding in 2019E

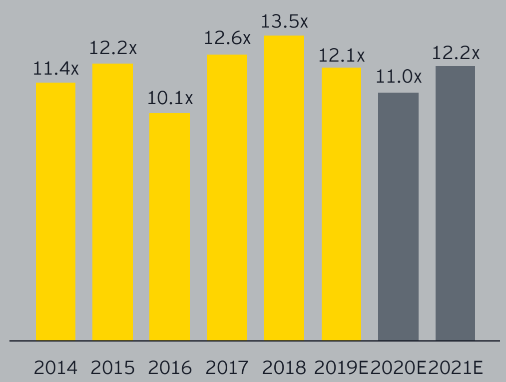
- The charts below analyze the evolution of the trading multiples of luxury companies of our current panel on March 31 of each year from 2014A to 2018A, and the expected average multiples for 2019E, 2020E and 2021E.
- In line with last year's expectations, luxury multiples in 2018A followed the rebounding trend announced in 2017A. This has been mainly driven by a trend for consolidation, as well as the continuous pursuit of opportunities to increase omnichannel presence, which led online retail players to generally experience higher valuations than traditional retail.
- Leading practices in the luxury market often relate to having an ecosystem, approach which may consist of (i) establishing mutually beneficial and long-lasting partnerships with other players in the industry, e.g., Farfetch and JD.com in China; (ii) leveraging digitalization to establish a deeper connection with consumers and increase customer loyalty by setting up communities and creating a sentiment of belonging; and (iii) acknowledging that the company itself is part of a larger social ecosystem and committing to being environmentally and socially focused companies, an aspect of increasing relevance to young shoppers worldwide.

EV/sales



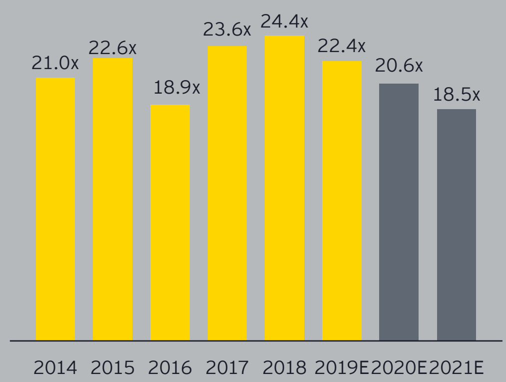
Average 2014A–19E: 2.8x

EV/EBITDA



Average 2014A–19E: 11.9x

Price to earnings



Average 2014A–19E: 22.0x

Source: Data based on consensus of several brokers' reports for each company. Additionally, please note that Capri Holdings was founded in 2018 and, therefore, only the information for FY18 and expected values for 2019, 2020 and 2021 are included.

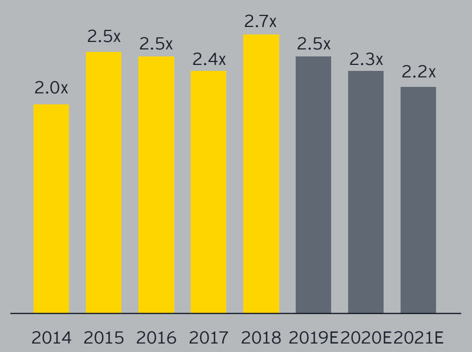
Note: Each year, the multiple is calculated as the ratio between EV as of March 31 of that year and forecast sales, EBITDA and earnings for that year. The information for 2019E-20E and 2021E represents the forward multiple analysis for the factbook launch in 2019, calculated as the ratio between the EV as of March 31, 2019, and the sales, EBITDA and earnings expected for 2019, 2020 and 2021. The historical transaction multiples exclude Farfetch and EssilorLuxottica, as these represent newly listed entities.

C Trading multiples

Cosmetics multiples are stabilizing following an exceptional 2018

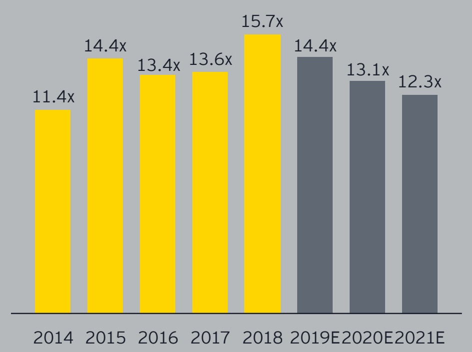
- The charts below show the evolution of the expected trading multiples of cosmetics companies in our current panel on March 31 of each year from 2014A to 2018A, and the expected average multiples for 2019E, 2020E and 2021E.
- In a period of economic upturn, per capita spending on beauty products is on the rise. Among the trends driving sales are: organic and natural products, products and services focused on an aging population that wants to stay young, and men's products and services. The positive trend in the market is keeping valuations high; however, 2019E valuations are slightly lower compared to 2018. This is partly due to the fact that 2018 was an exceptional year, with stock prices reaching all-time highs, notwithstanding the considerable volatility of markets that registered up to 5% intraday changes.
- To further contribute to the exceptionality of the year 2018, the higher EV of Estée Lauder and Shiseido led to increased EV/sales and EV/EBITDA multiples. The reasons for the increase in the EV were the acquisition of Deciem Inc. by Estée Lauder in June and the change in management of Shiseido (new CEO). In 2019, the average EV multiples of the panel were negatively affected by AMOREPACIFIC, which recorded a lower market capitalization compared to last year due to the slow recovery from weak domestic demand and restructuring efforts.

EV/sales



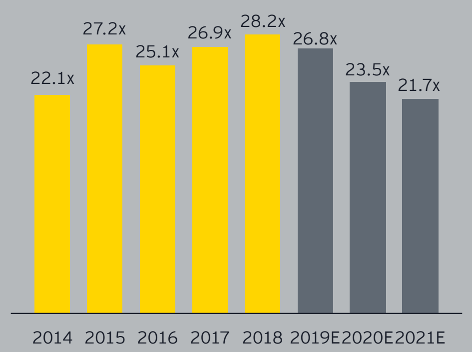
Average 2014A-19E: 2.4x

EV/EBITDA



Average 2014A-19E: 13.8x

Price to earnings



Average 2014A-19E: 26.0x

Source: Data based on consensus of several brokers' reports for each company. Please, note that AMOREPACIFIC and Nu Skin were added in the factbook panel in 2017. To make our analysis more meaningful, we have added them to the panel in previous years as well.

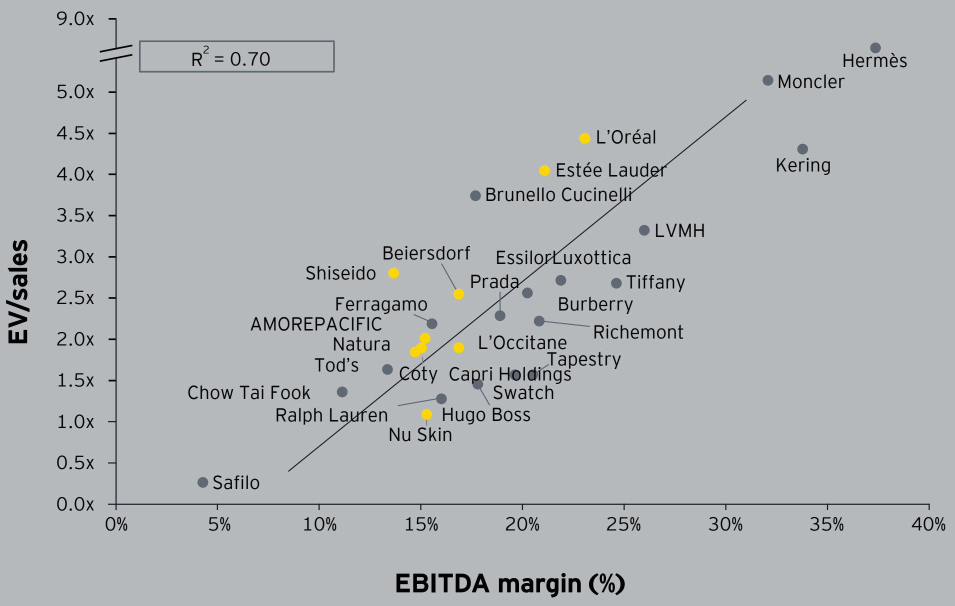
Note: Each year, the multiple is calculated as the ratio between EV as of March 31 that year and forecast sales, EBITDA and earnings for that year. The information for 2019E-20E and 2021E represents the forward multiple analysis for the factbook launch in 2019, calculated as the ratio between EV as of March 31, 2019, and sales, EBITDA and earnings expected for 2019, 2020 and 2021. Please note that the calculation of the average follows the simple average method.

C Trading multiples

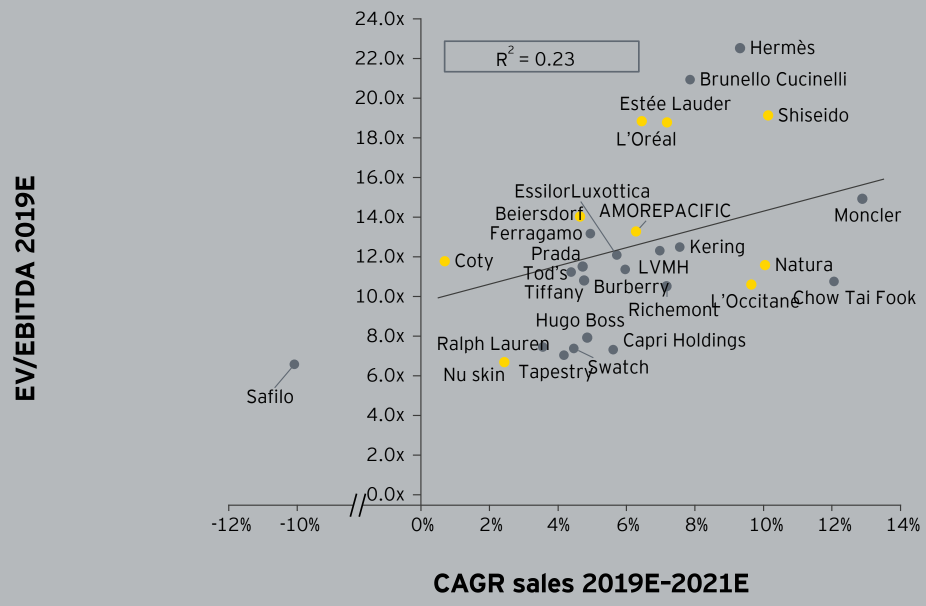
In 2018, investors seem to focus more on profitability than growth, confirming a historical trend

- A regression analysis shows the presence of a strong correlation between EV/sales levels and profitability (R2 = 0.70, p-value = 0.00). In increasingly competitive environment in which industry players are facing growing costs to position themselves in the e-commerce segment and meet customer demands, the profitability level remains an important investment criterion driving EV/sales multiples.
- The correlation between EV/EBITDA and sales growth is less strong than the correlation between EV/sales and profitability (R2 = 0.23, p-value = 0.01), but higher compared to the 2018 value (R2 = 0.17). This result reflects investors' increasing reliance on sales expectations as an indicator of value. This partially confirms the established belief that future industry leadership will belong to those companies who better leverage their brand and digital presence to transform online traffic into sales. Furthermore, many of the rising stars in the luxury arena are familiar with the digital world, and in 2018 recorded double-digit growth and have recorded double-digit growth, raising investor interest in the outlook of sales growth – an indicator of success.

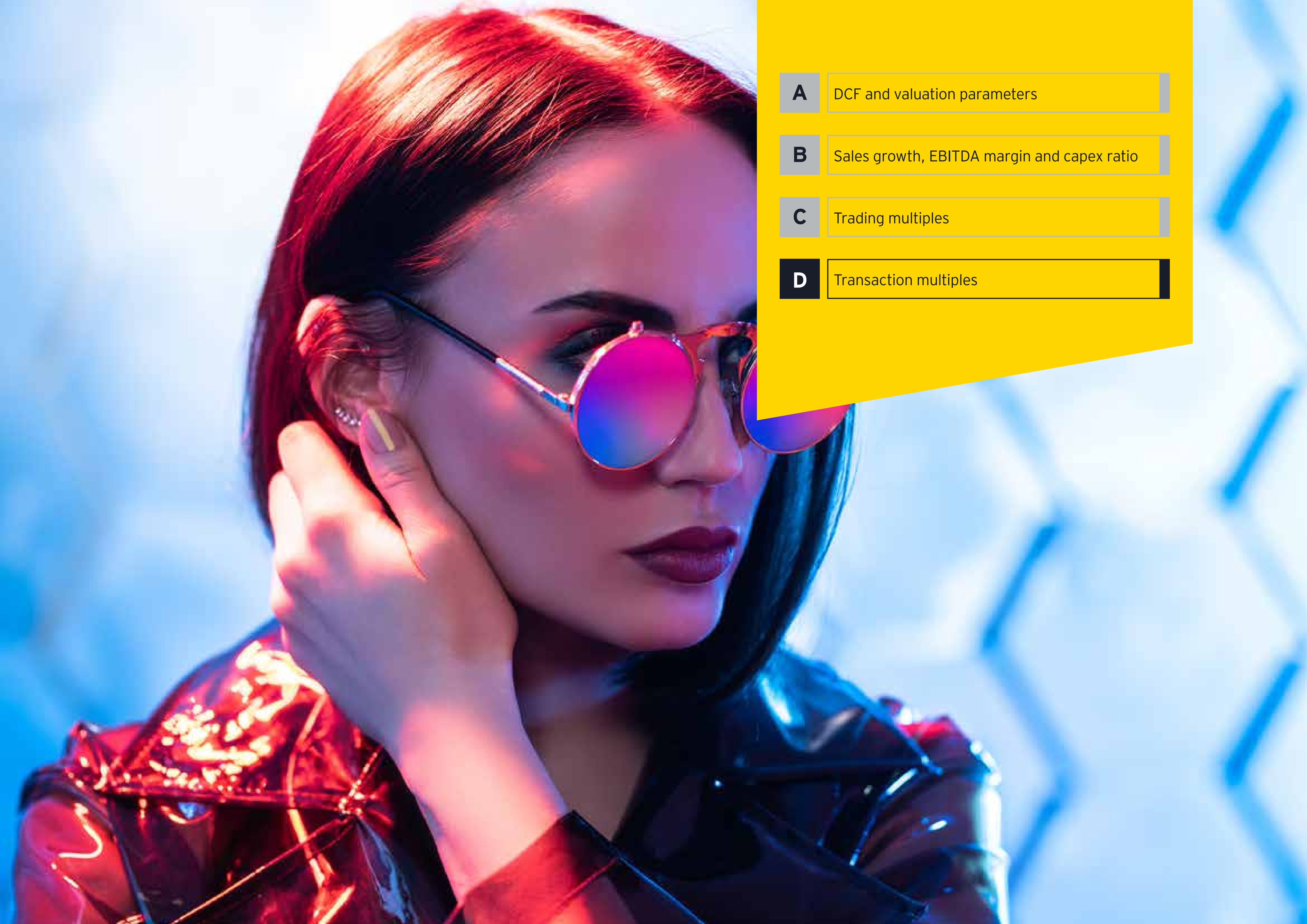
Regression analysis: EV/sales 2019E multiple vs. EBITDA margin 2019E



Regression analysis: EV/EBITDA 2019E multiple vs. sales CAGR 2019E–21E



Note: Farfetch is not represented in either regression analysis because it is an outlier, both for the expected CAGR and for its negative EBITDA margin.

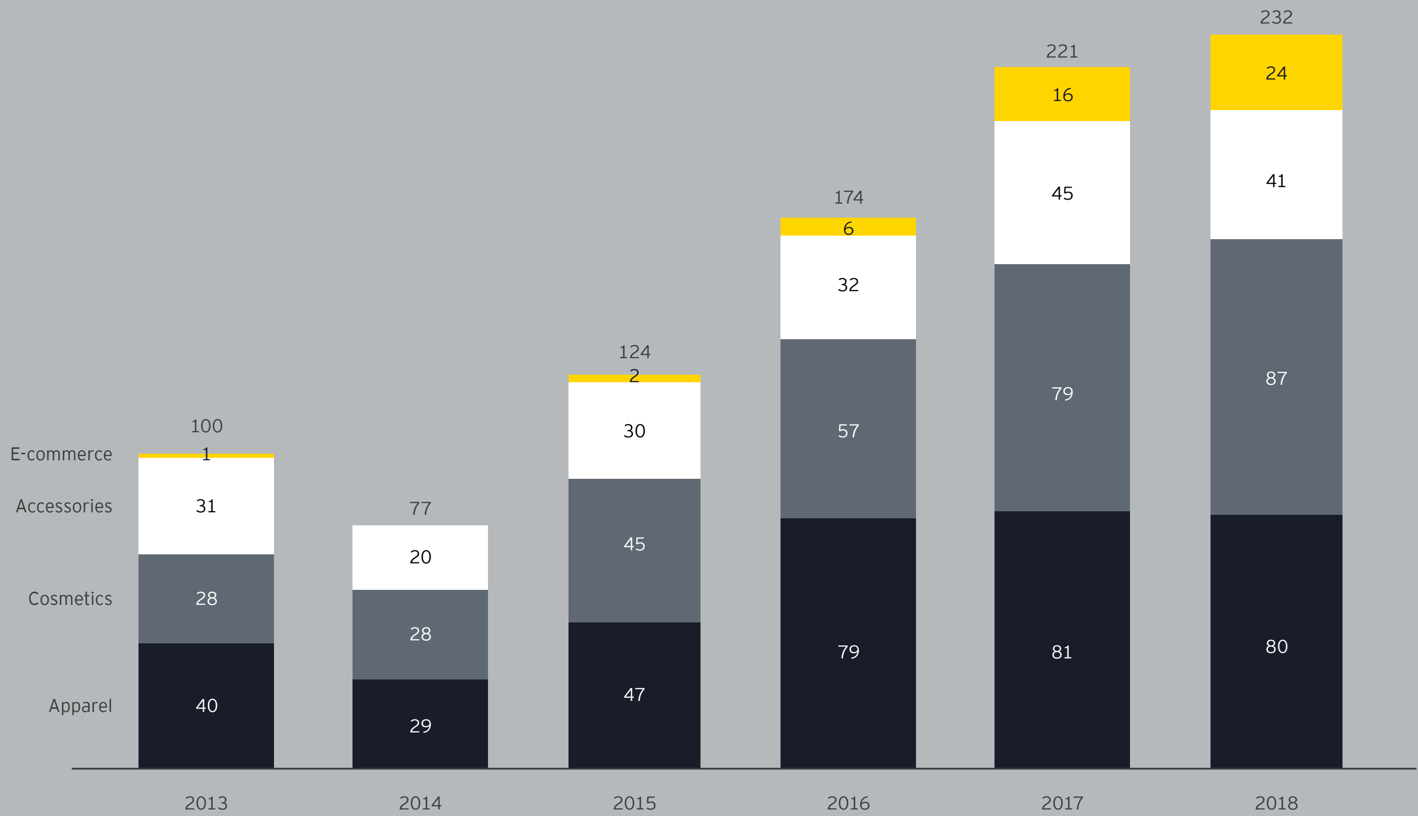


- A DCF and valuation parameters
- B Sales growth, EBITDA margin and capex ratio
- C Trading multiples
- D Transaction multiples

D Transaction multiples

The year 2018 was characterized by an abundance of acquisitions in the luxury fashion and cosmetics universe, driven by a trend toward consolidation. Cosmetics and e-commerce were the hottest sectors. The former attracted investors through the growth potential of digital innovation, whilst the latter played an increasingly strategic role as luxury retailers continue their rapid shift toward e-commerce

Number of completed deals by sector



Selected global 2018 transactions

- Michael Kors/Gianni Versace
- Fosun International/Jeanne Lanvin
- Sapinda Holding/La Perla
- Ermenegildo Zegna/Thom Browne
- Authentic Brands/VF Corp. (Nautica)

- P&G/First-Aid Beauty
- Yves Rocher/Sabon Shel Paam
- Ginza Stefany/Avon Products; Evermere
- L'Oréal/Pulp Riot
- P&G/Walker & Company Brands

- VF Corporation/Altra Running
- Luxottica/Barberini
- Ted Baker/No Ordinary Shoes
- Shandong Ruyi/Bally International
- Camuto Group/DSW & Authentic Brands Group

- Richemont/Yoox Net-A-Porter
- L'Oréal/Nanda Co.
- Flight Club New York/GOAT
- JD Sports Fashion/The Finish Line
- Stadium Goods/Farfetch

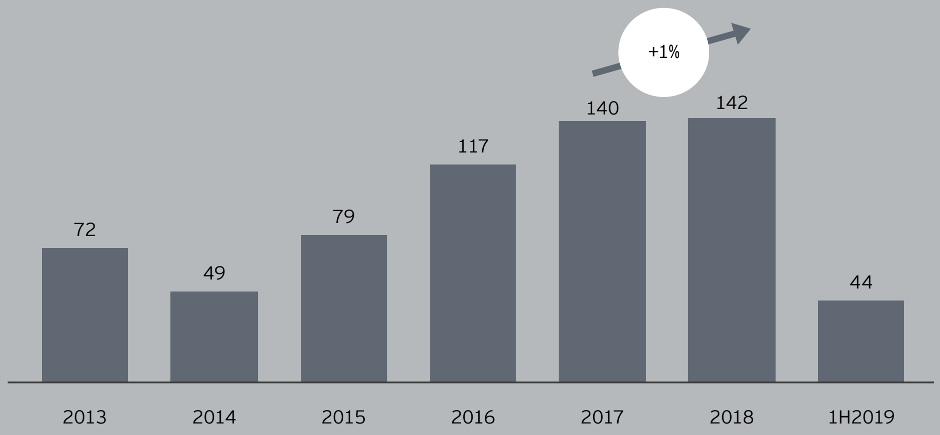
Notes:

- Apparel includes transactions related to apparel, sportswear and lingerie.
- Cosmetics include transactions related to cosmetics, dermocosmetics and third-party producers.
- Accessories include transactions related to accessories, eyewear, jewelry and watches, and shoes.
- E-commerce includes transactions related to e-commerce for both luxury and cosmetics companies.

D Transaction multiples

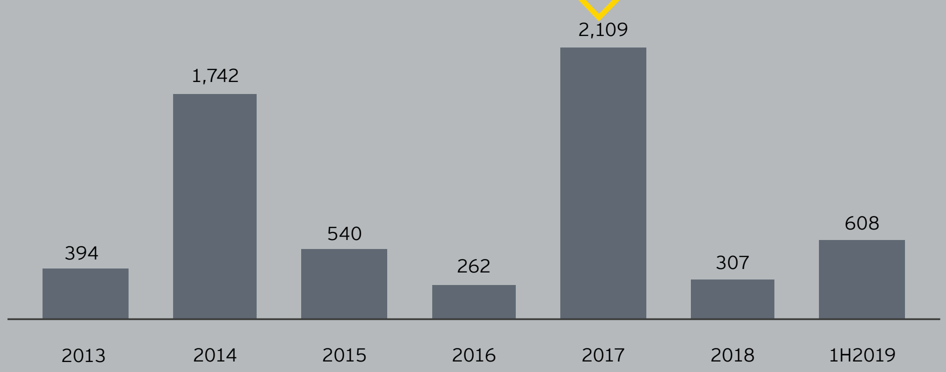
In 2018, M&A activity in the fashion and luxury arena reached an all time high with 142 transactions, the year was characterized by smaller deals compared to 2017, albeit involving well-known brands with an average deal size of around €307m

Number of completed deals



Average deal size (€m)

The average deal size is €527m without the three jumbo transactions (acquisition of 26% stake of Christian Dior, 3% of Burberry and the merger of Essilor and Luxottica).



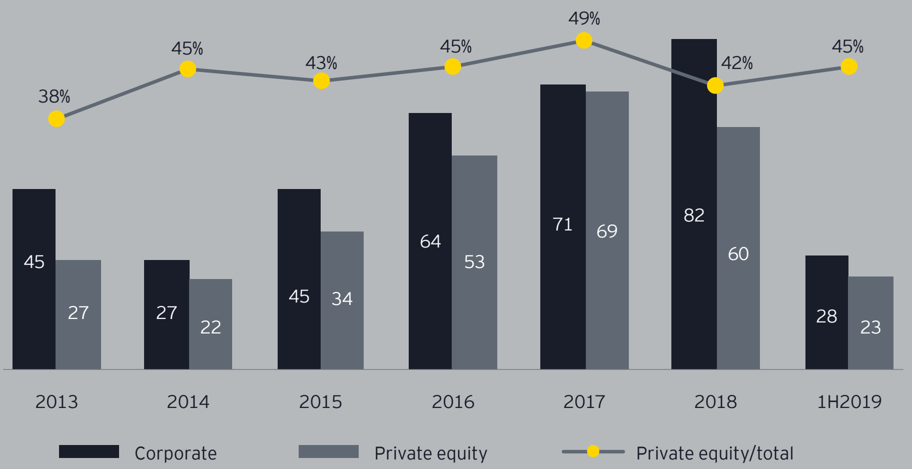
Note: EY analysis of Mergermarket data. 1H stands for first half.

- The growth trend continued in the year 2018, showing an increase of 1% in terms of the number of transactions compared to 2017, depicting continued investor confidence and positive expectations.
- Asian investors continued to show interest in European fashion and drove M&A activity. In 2018, two names emerged as Asian powerhouses in luxury fashion: Shandong Ruyi and Fosun International. The former has acquired Swiss luxury brand Bally, and the latter was involved in high-profile deals such as the acquisition of the French couture label Lanvin and the lingerie brand Wolford.
- In the current landscape the real battle is how to win consumers' attention, both online and offline. This has translated into a key driver for M&A. For example, GOAT Group, the world's largest online marketplace for authentic sneakers acquired Flight Club New York, an influential sneaker consignment store with a store presence in New York and Los Angeles. The acquisition provides the online high-end sneakers marketplace Goat with its first bricks-and-mortar presence, proving how the correct mix of online and offline presence is deemed to be key for thriving in the current competitive scenario.
- The targets have been mainly middle-market companies and startups, resulting in a smaller average deal size. Nevertheless, the year was also characterized by few large transactions that saw: (i) the establishment of new fashion ecosystems such as Capri Holdings (after Michael Kors acquired Jimmy Choo in 2017 and Gianni Versace in 2018), (ii) consolidation efforts (such as Rue La La's acquisition of Gilt Groupe, Inc.), and (iii) the integration of online and offline channels to remove friction in the consumer journey (Richemont's acquisition of Yoox Net-A-Porter for €3.4bn).
- The year 2019 commenced with a large acquisition in the sportswear segment, namely the acquisition of Amer Sports by a consortium led by ANTA Sports for a value of €5.6bn. The average deal size for the first quarter of 2019, excluding the Amer Sports transaction, is €295m.

D Transaction multiples

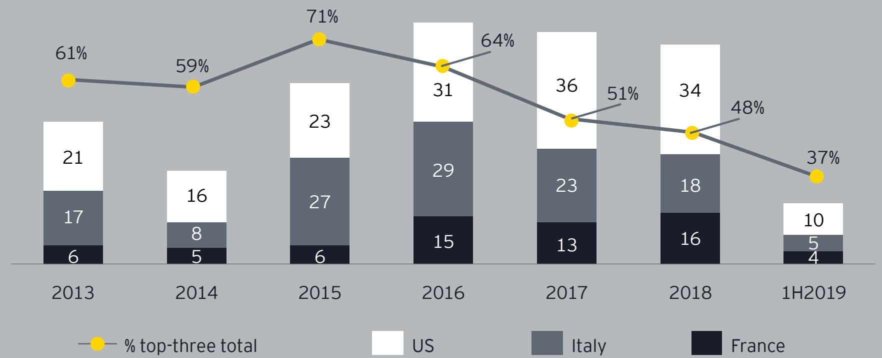
Private equity activity, fueled by dry powder, represented 42% of total M&A activity in the fashion and luxury sector in 2018. The strong presence of private equity funds, however, is challenged by competition from strategic players. M&A operations conducted by large industry players have been increasingly common in a landscape where consolidation seems to be the key to success

Number of completed deals by type of buyer



- After the strong and high returns reaped by large funds that have invested in the fashion industry over the past years (Blackstone with Versace, Carlyle with Moncler and Permira with Valentino and Hugo Boss investments), many other private equity funds have recognized the potential of the fashion industry and have increased their investment in the sector. For instance, Italian fund FSI acquired a 41% stake in fashion label Missoni S.p.A., and in 2019 Italian fund QuattroR SGR S.p.A. acquired 60% of the Italian label Trussardi to support it in the relaunch.
- The apparel sector has seen the largest number of private equity investments, and sportswear in particular is where private equity funds are investing. For instance, Chinese IDG Capital invested a minority stake in the French sportswear group Rossignol.
- The strong presence of private equity funds, however, is challenged by competition from strategic players. A landscape where consolidation seems to be the key to success. Corporate investments have increased in number of M&A deals on a YoY basis, from 71 deals in 2017 to 82 in 2018. Strategic investors seem to follow a similar trend as private equity investors, noticeably with investments in the sportswear, shoes and e-commerce sectors.

Number of completed deals sorted by top-three geography of target



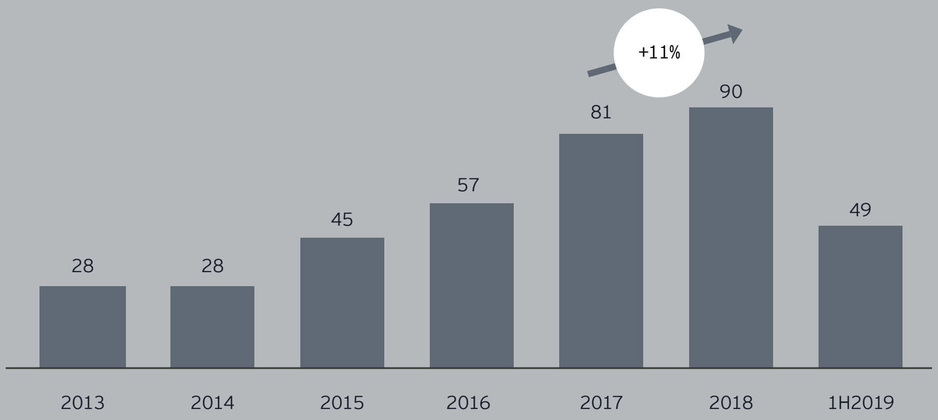
- Italy, the US and France have been the top countries attracting the interest of buyers in the fashion and luxury arena in 2018. Other European nations were also attractive to investors, such as Sweden, Denmark and Germany, where the deal count has increased manifold (+13 cumulated compared to 2017). Notably, the Stockholm-based company Acne Studios sold a minority stake to IDG Capital and I.T Group in a €419m deal.
- The US was targeted particularly for sportswear, casual brands and footwear companies, such as the acquisition of Oboz Footwear by Kathmandu Holdings, CABH Holdings (Rothy's) by Goldman Sachs and Altra Running by VF Corporation.
- Italy and France have been targeted for brands with heritage, mostly in the entry-to-luxury and high-end-luxury arenas. For instance, FSI SGR invested in Missoni, Sapinda Holding in La Perla and Luxottica in Barberini, the world's leading optical sunglass lens manufacturer.
- The year 2019 started with majorly Italian investments, such as QuattroR SGR S.p.A's investment in Trussardi, Morellato S.p.A. in French company Mister Watch and Equinox in Manifattura Valcismon (its portfolio of sportwear brands includes Castelli, Sportful and Karpos).

Note: EY analysis of Mergermarket data.

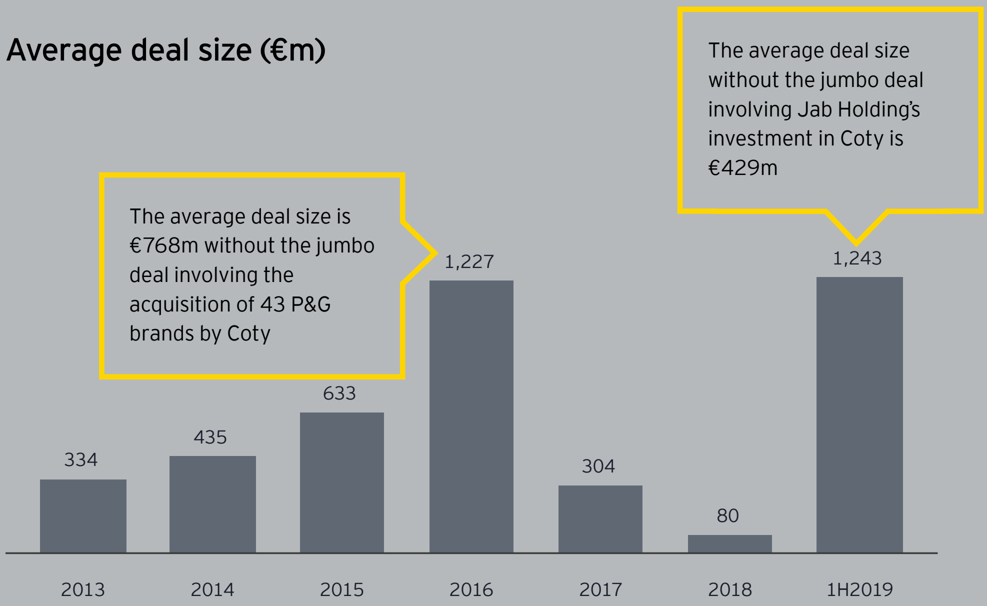
D Transaction multiples

In the beauty industry, the M&A fever of the past years has reduced the pipeline of good-sized opportunities (above €150m) and, as a result, industry players are targeting smaller businesses and bringing down the average deal value size

Number of completed deals



Average deal size (€m)



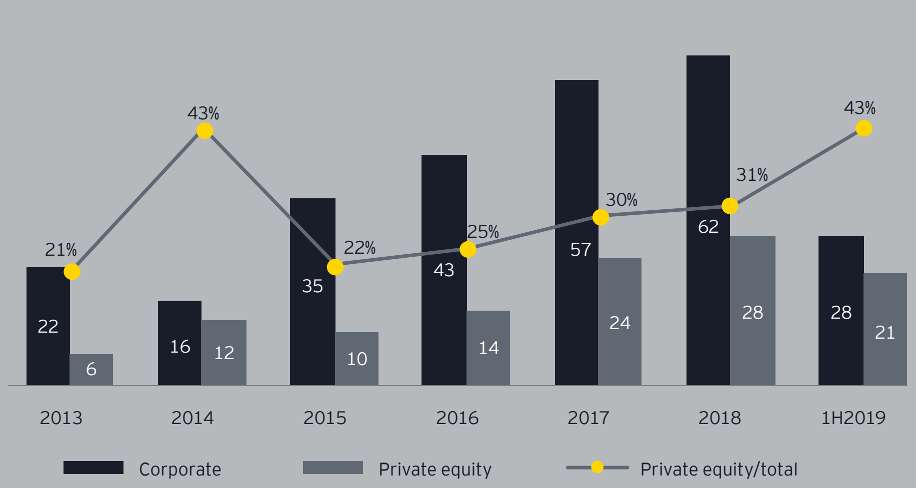
Note: EY analysis of Mergermarket data.

- The number of transactions remains high, reaching a peak of 90 in 2018 (+11% from 2017). The need to rapidly respond to market complexity and consumers' expectations is driving M&A activity.
- Large players are investing in brands that tailor to specific skin types. For instance, P&G acquired First-Aid Beauty, with a product line catered to skin issues such as acne, dryness, dullness, redness and aging, and invested in Walker and Company Brands, selling consumer-centric health and beauty products for people of color.
- Investors continue to see strong growth potential in the Asian market, particularly in the South Korean beauty industry. Following the 2015 investment of beauty giant Estée Lauder in the Korean company Have & Be Co., and Unilever's investment in Carver Korea in 2017, in 2018 L'Oréal acquired the South Korean cosmetics and fashion firm Nanda Co., whose brands include Stylenanda and makeup line 3CE.
- The M&A fever of the past years has reduced the pipeline of good-sized opportunities (above €150m) and, as a result, industry players are targeting smaller businesses and bringing down the average deal value size.
- Industry leaders are turning to startups to enable cosmetics to become connected and customizable. The Japanese giant Shiseido, for instance, acquired Olivo Laboratories, which developed and patented a technology designed to act as a second skin. French player L'Oréal, instead, acquired Modiface Inc., Canadian developer of augmented reality technology applied to the beauty sector. These acquisitions, along with other investments such as Unilever PLC in Equilibra S.r.l. and GlaxoSmithKline plc and P&G in Snowberry, also highlight the strategic choice of large corporates to pursue premiumization.
- This year is set to be another interesting year for dealmaking activity in the cosmetics industry, with Brazilian Natura announcing its intention to acquire US label Avon, valued at approximately €2.7b and Jab Holding increasing its stake in Coty (€14b deal value).

D Transaction multiples

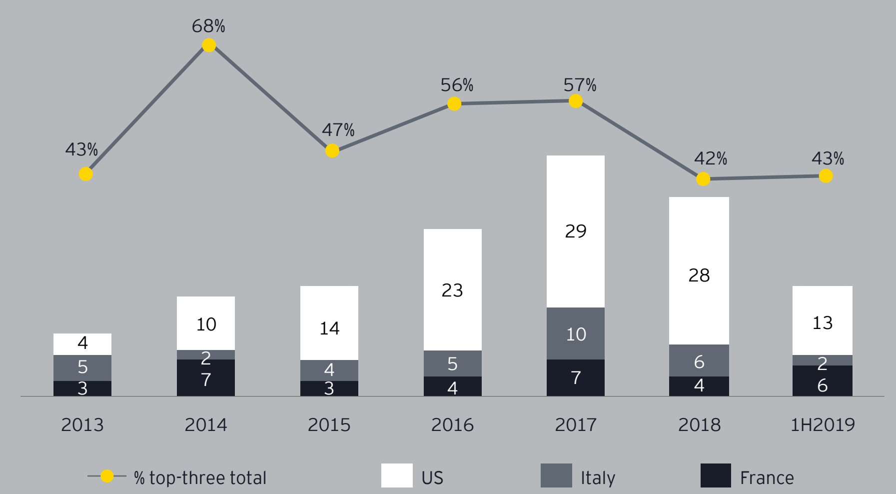
Notwithstanding the usual predominance of trade buyers, the sector has attracted more interest from private equity funds in 2018, which accounted for 31% of the total deals. Private equity interest in the industry is likely to continue in the upcoming years, led by the presence of companies with innovative and technological products, high margin potential, and international ambitions, as well as strong industry fragmentation which calls for aggregation

Number of completed deals by type of buyer



- While strategic M&A is fueled by players' need for (i) innovative technology, (ii) geographic expansion, and (iii) targeting new demographic or customer types, a number of other characteristics inherent to the beauty industry are increasingly appealing to private equity funds. These are: (i) the presence of companies with strong potential for internationalization, (ii) high margin profiles, (iii) fast innovation and technological advancements, and (iv) a highly fragmented industry.
- Consequently, the percentage of private equity-backed deals over the total deals has been increasing over the past four years, reaching 31% in 2018. Confidence in the industry potential has led diversified private equity funds to invest in the beauty sector in 2018, for instance, Peninsula invested a minority stake in the Italian brand Kiko.
- Private equity interest in the industry is likely to continue in the upcoming years. In 2019, Bain Capital Private Equity announced its acquisition of a majority stake in Maesa, which deals with "engineering beauty," namely to design, produce, and plan marketing campaigns and services for beauty companies and retailers.

Number of completed deals sorted by top-three geography of target



Source: EY analysis of Mergermarket data; Euromonitor; EY analysis.

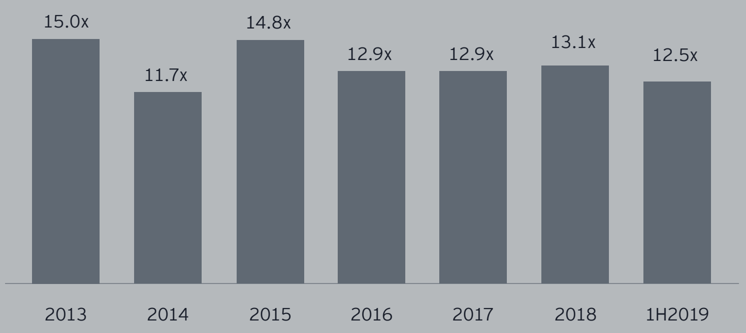
- The US is the No. 1 target country for private equity funds. American leadership is partially explained by the fact that the US is home to many small, digitally native brands. Typically, these brands have some or all of the following characteristics: proprietary data, strong e-commerce and social media presence, as well as brand loyalty, product development innovation, and a diversified go-to-market strategy.
- The characteristics of digitally native brands are increasingly of interest to investors. In 2018, the vegan makeup brand Lime Crime, for instance, was acquired by Tengram Capital Partners. Similarly, in 2019, Edgewell announced the acquisition of Harry's, a direct-to-commerce brand targeting men with quality shaving products, for €1.2bn.

D Transaction multiples

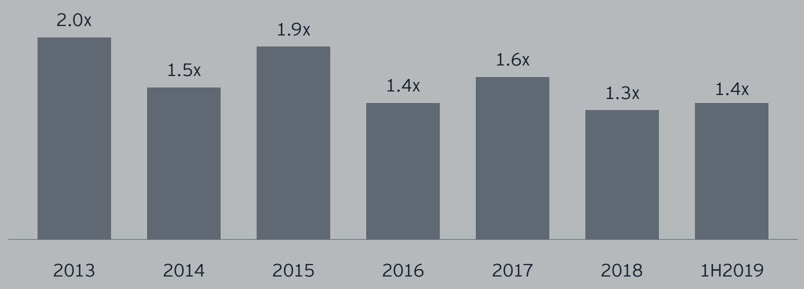
Transaction multiples in the luxury and cosmetics industry remain stable, with multiples in line with 2017 values

Luxury

EV/EBITDA (FY13–1H2019)

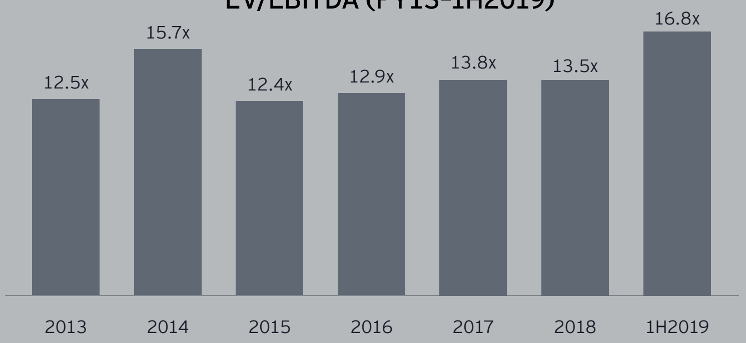


EV/sales (FY13–1H2019)

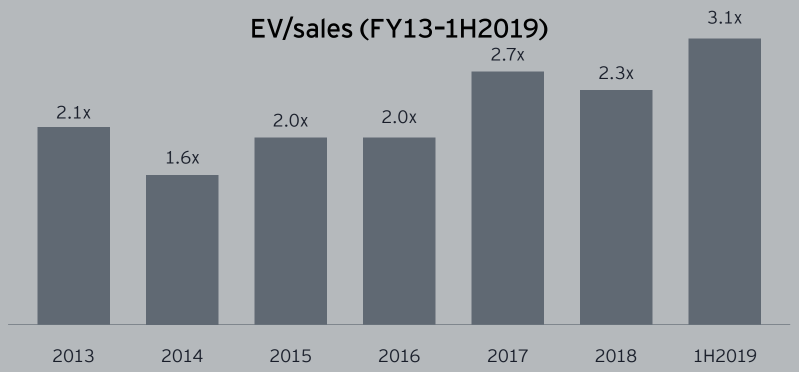


Cosmetics

EV/EBITDA (FY13–1H2019)



EV/sales (FY13–1H2019)



Source: EY analysis of Mergermarket data.

In the case of fashion luxury companies, transaction multiples are in line with 2017 values. The highest multiple refers to the acquisition of a Norwegian sportswear brand by Canadian Tire Corporation (EV/EBITDA of 26.9x). The acquisition aimed at strengthening Canadian Tire Corporation's core retail businesses across multiple banners, increase its brand offerings in Canada and its ability to grow its brands internationally, justifying an above-average multiple.

In the case of cosmetics companies, average M&A transaction multiples in 1H2019 are affected by an outlier. Namely, the acquisition of Japanese Ci:z carried out by Johnson & Johnson, with a transaction multiple EV/EBITDA of 25.9x.

Industry overview

A Industry overview

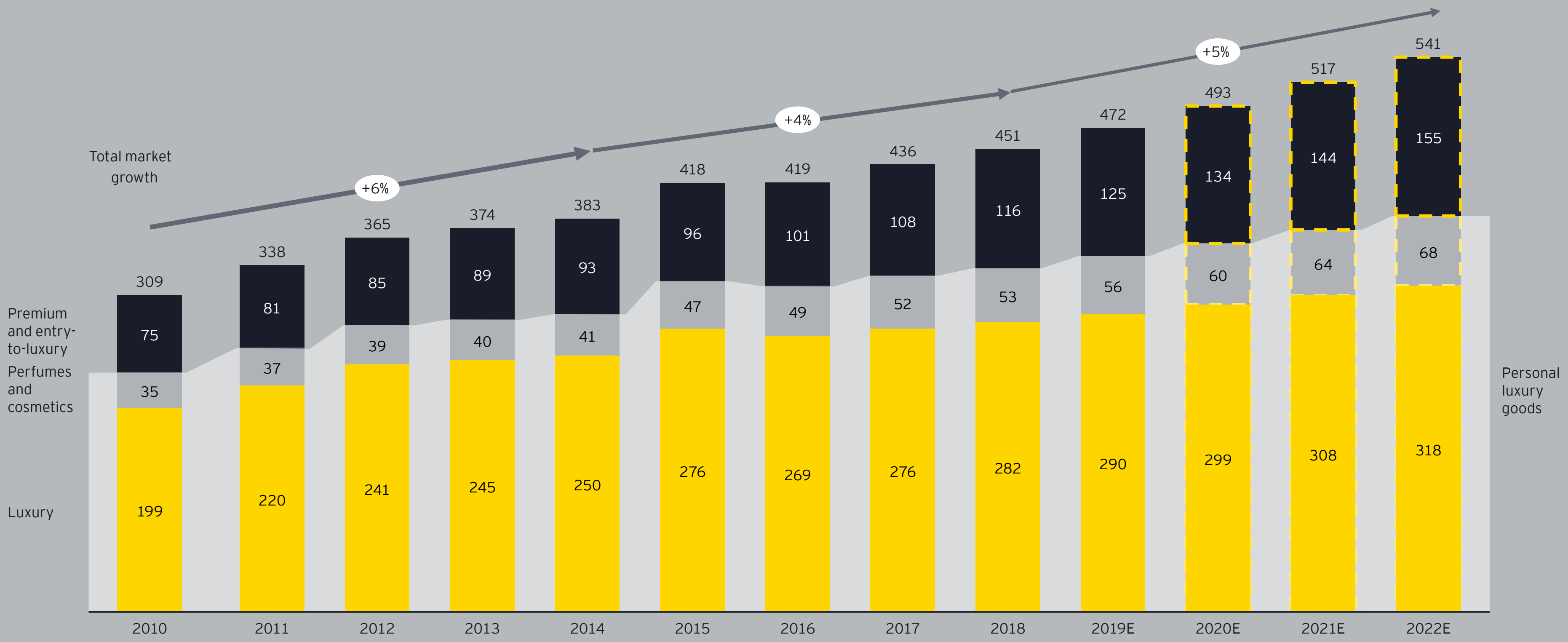
A Industry overview

Luxury market is expected to maintain a moderate trend (+3% CAGR 2018-22E), while overall sector growth will be driven by premium and entry-to-luxury segment (+7.5% CAGR 2018-22E)

Luxury, premium and entry-to-luxury market growth

	CAGR (2010-14)	CAGR (2014-18)	CAGR (2018-22E)
Premium and entry-to-luxury	5.4%	5.8%	7.5%
Perfumes and cosmetics	4.1%	6.7%	6.4%
Luxury	5.9%	3.1%	3.0%

Global luxury, premium and entry-to-luxury market size (€b)



A Industry overview

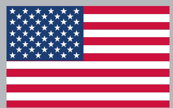
Product categories leading luxury growth are shoes and secondarily accessories, while premium segment growth affects all categories

	Luxury		Premium and entry-to-luxury	
	2018	2022E	2018	2022E
Shoes	€19b +8% CAGR	€27b +10% CAGR	€20b +6% CAGR	€25b +6% CAGR
Accessories	€69b +7% CAGR	€84b +5% CAGR	€12b +8% CAGR	€18b +9% CAGR
Watches and jewelry	€125b +1% CAGR	€128b +0% CAGR	€17b +7% CAGR	€23b +8% CAGR
Apparel	€69b +3% CAGR	€79b +3% CAGR	€67b +5% CAGR	€89b +8% CAGR

2018 CAGR: The CAGR is calculated for the period between 2014 and 2018. 2022 CAGR: The CAGR is calculated for the period between 2018 and 2022E.

A Industry overview

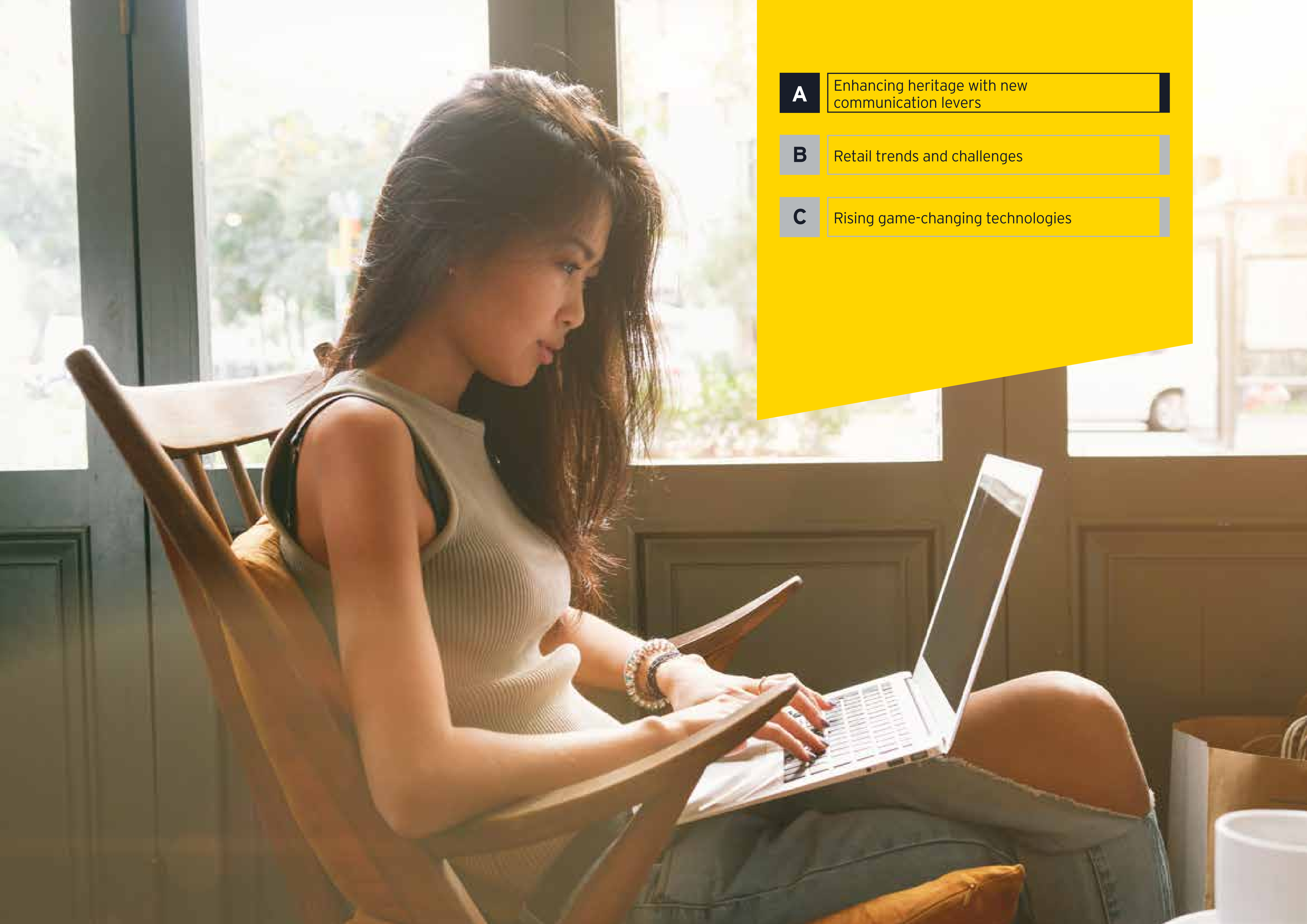
Chinese customers will increasingly buy luxury products in mainland China, and premium market is expect to grow globally

	Luxury*		Premium and entry-to-luxury	
	2018	2022E	2018	2022E
	€24b +5% CAGR	€48b +19% CAGR	€9b +8% CAGR	€11b +6% CAGR
	€112b +6% CAGR	€118b +1% CAGR	€31b +7% CAGR	€43b +9% CAGR
	€81b +3% CAGR	€83b +1% CAGR	€36b +2% CAGR	€41b +4% CAGR
	€118b +2% CAGR	€137b +4% CAGR	€41b +8% CAGR	€60b +10% CAGR

* Includes perfumes and cosmetics.

2018 CAGR: The CAGR is calculated for the period between 2014 and 2018. 2022 CAGR: The CAGR is calculated for the period between 2018 and 2022E.

Luxury industry overview

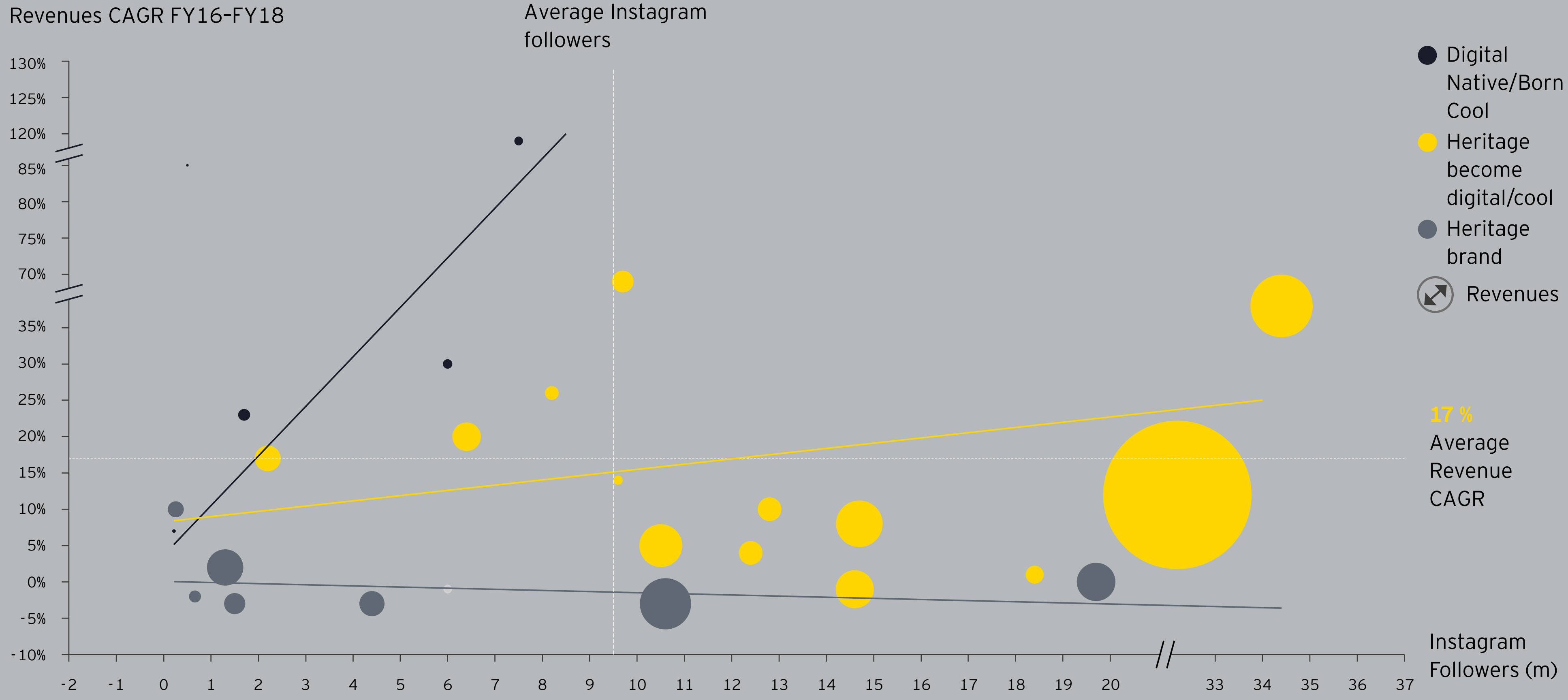


A Enhancing heritage with new communication levers

In a moderately growing luxury market, performances are polarized and the winners are heritage brands that understood how to become "cool" by rearranging their image through contemporary communication levers

Benchmarking analysis of key players – Revenue CAGR and EBITDA margin

	Revenue CAGR	Instagram Followers (m)
Digital Native/Born Cool	+53%	3
Heritage become digital/cool	+16%	15
Heritage brand	+2%	5



Source: EY analyses on AIDA (financials), Instagram (followers).

Note: The criteria for the three labels take into account lyst.com and google.com search data, conversion rates and sales, as well as brand and product social media mentions and engagement statistics worldwide over a three-month period.

A Enhancing heritage with new communication levers

Successful brands understood how to communicate their distinctive values and attributes in every touch point with the client, following an omnichannel approach: online communication and in store (brand.com and physical) customer experience

Coolness means...

Exclusivity (aspirational for many, available for few)

- Cool is distinctive, referring only to a narrow elite
- What is cool may come from everyday life and common people, but it is accessible only to a few

Provocation and disruption

- The brand creates emotions and remains top of customers' mind

Sexiness

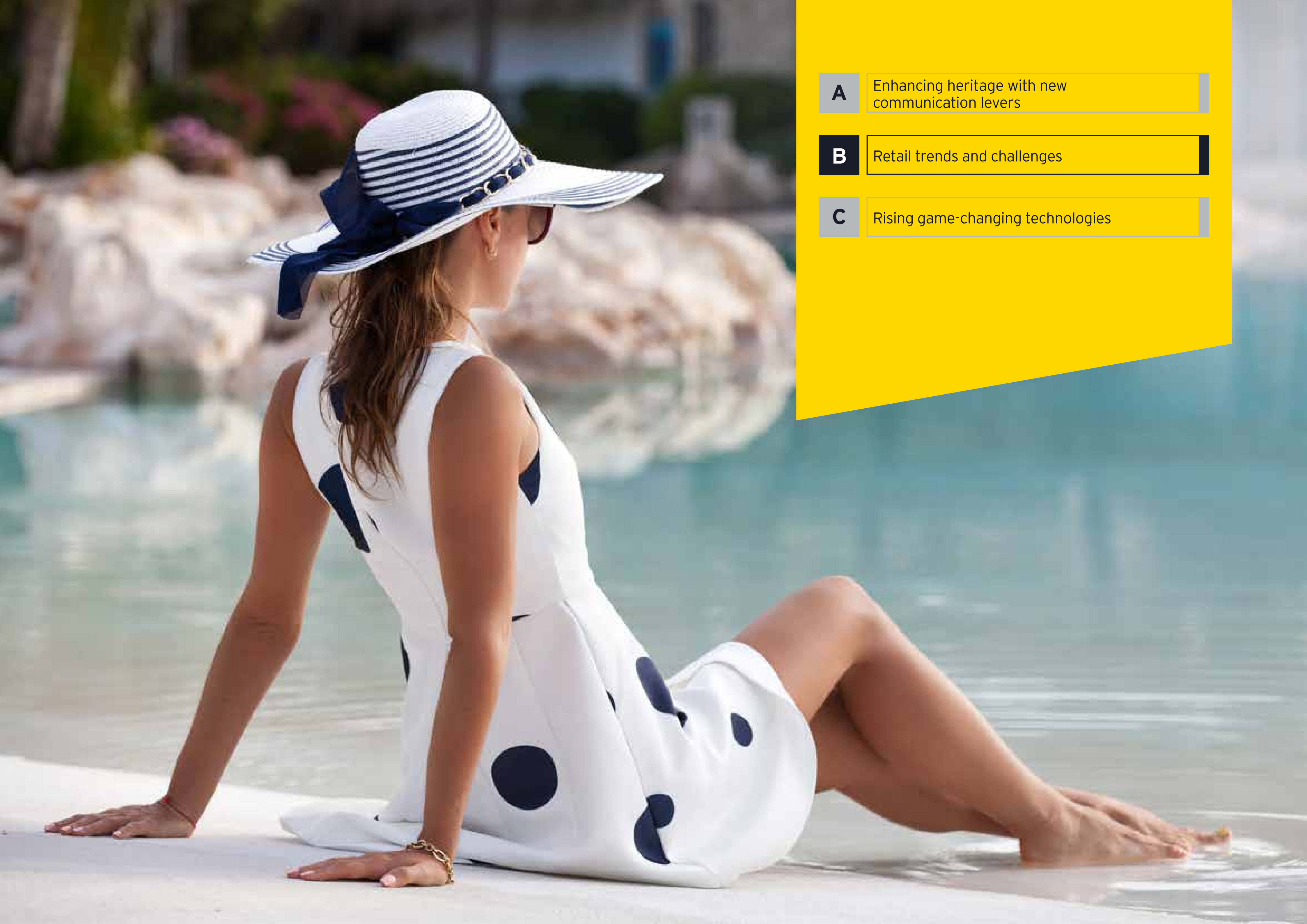
- Coolness is the expression of a new sensuality that is imaginative, intimate and delicate. It that may sometimes be provocative and able to capture the imagination of consumers and bring new one closer to the brand

Purpose

- Coolness is not about the product itself, but rather about the ability to communicate purpose, passion, business coherence and transparency

Customer intimacy

- The brand raises an intimate feeling within the client, who feels known and appreciated as an individual with unique tastes and preferences in every brand touch point
- Customized and geolocalized marketing, tailored initiatives addressed to a single client for a personal approach



A Enhancing heritage with new communication levers

B Retail trends and challenges

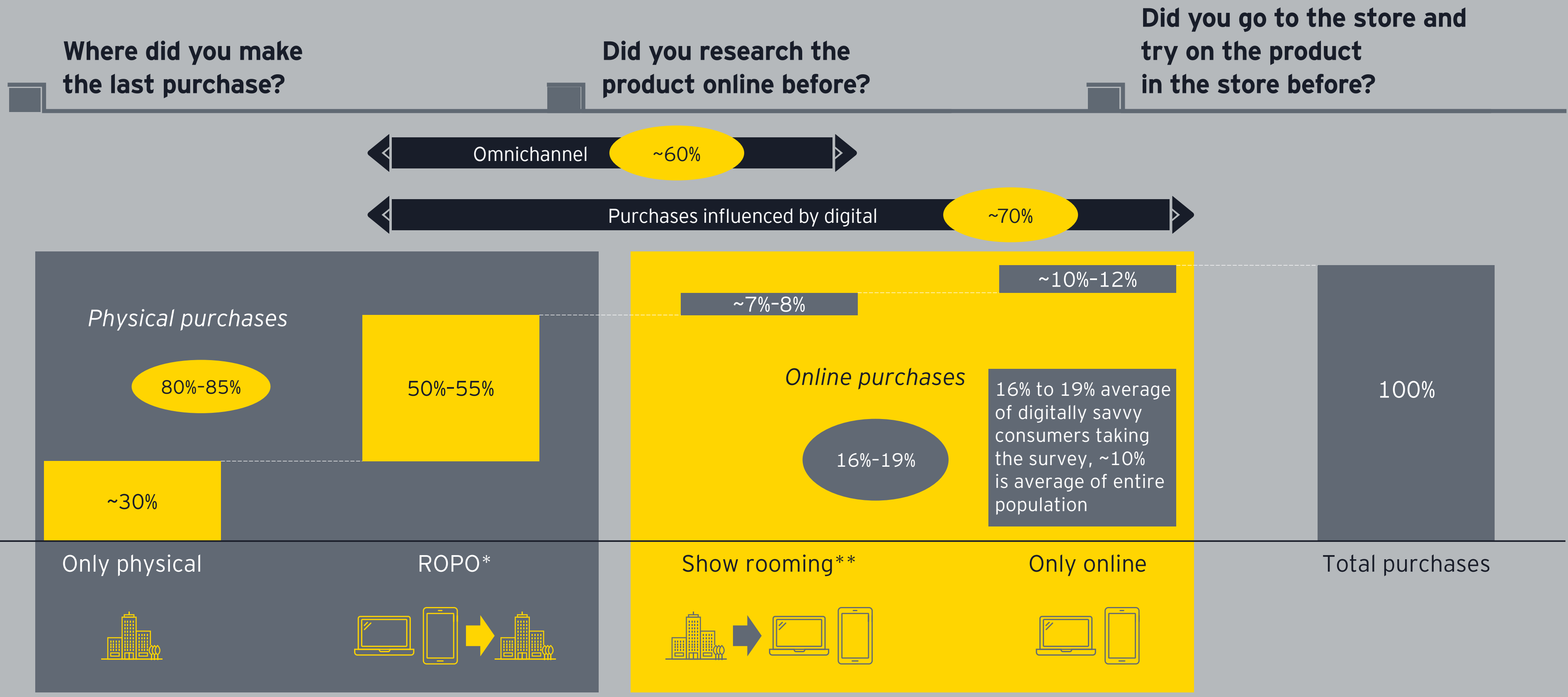
C Rising game-changing technologies

B Retail trends and challenges

Online presence is the brand demand generator (60% to 70% of purchasing decisions mature online), but the footprint is key for conversion (90% of transactions occur in a physical store)

Market consensus	Overall share of online sales, across markets and segments, is around 10% to 12%

Sample data from surveys (% relative to last purchase)

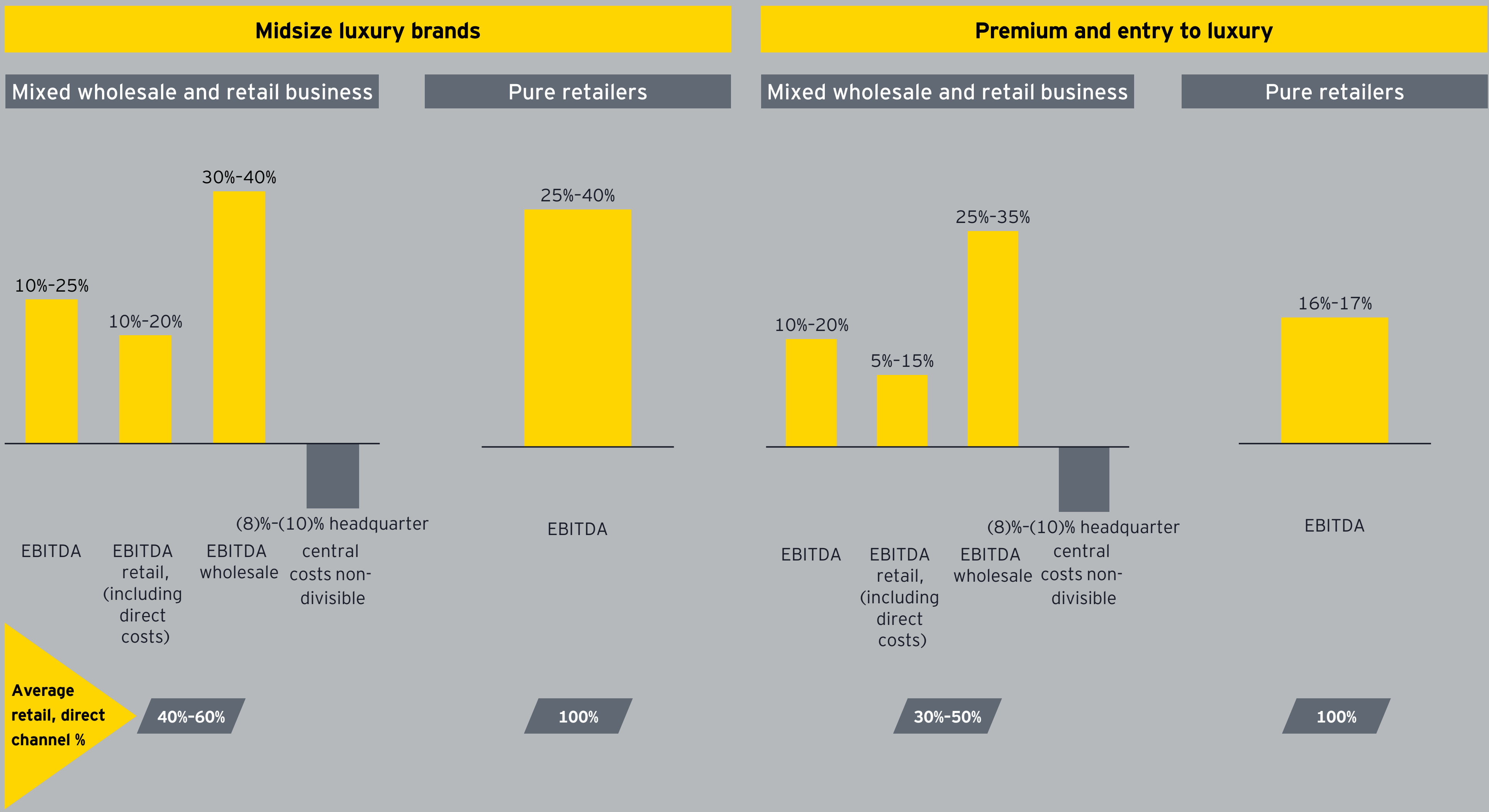


Source: Euromonitor data; EY database of over 10 customer surveys run in the past 18 months (covering over 50,000 costumers) for premium and luxury brands.

Note: * ROPO research online purchase offline. ** Show rooming means the customer saw the product in the physical shop and bought online.

B Retail trends and challenges

Retail is typically EBITDA dilutive for mixed wholesale and retail players and there is increasing pressure on profitability from market challenges. Retail success has become a priority to provide the shareholders' return and convert consumers' interest into sales

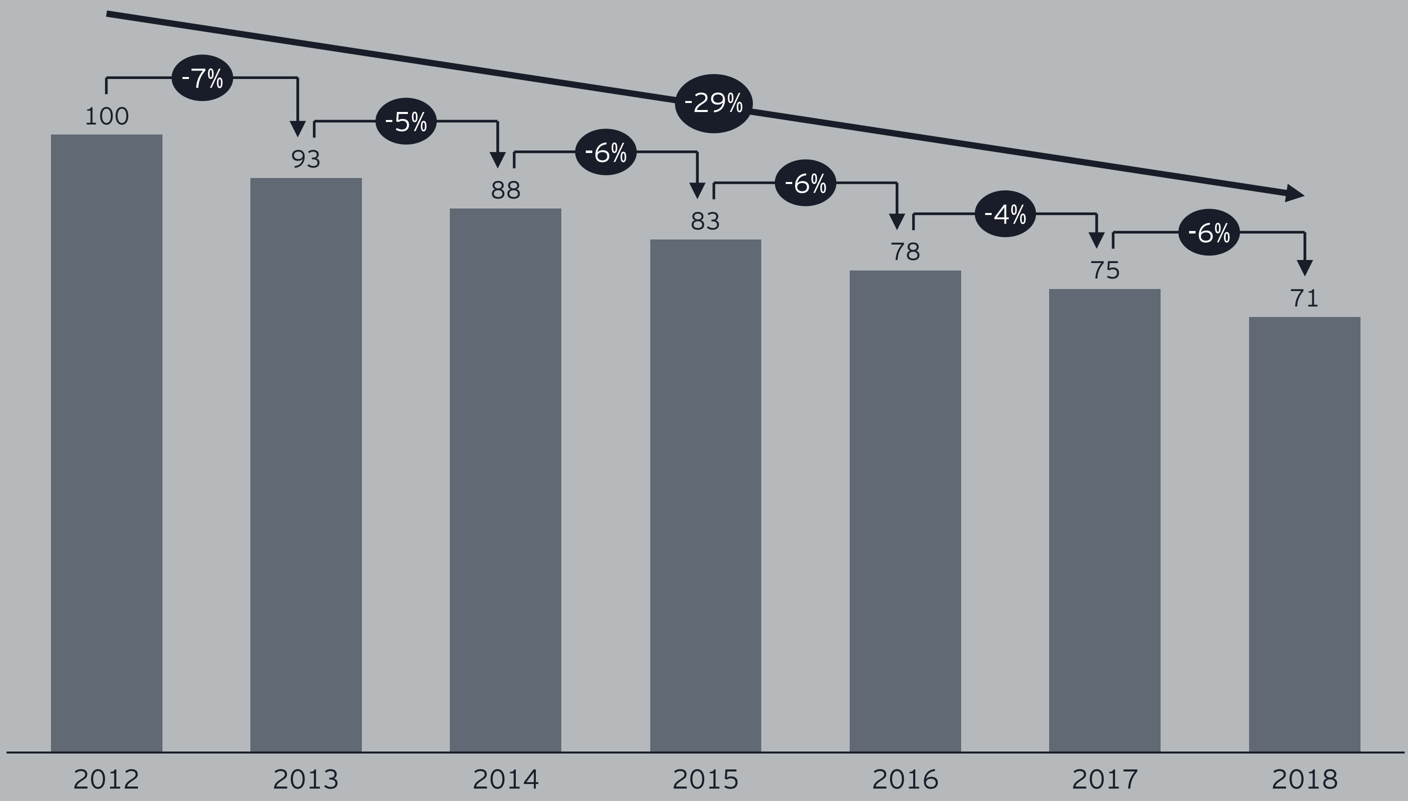


Source: EY-Parthenon analyses; company annual reports.

B Retail trends and challenges

Retail performance is put under pressure by a structural decline of store traffic in shopping districts (falling with a -6% CAGR, from 2012 to 2018)

Fashion and accessories store traffic YoY change (%)



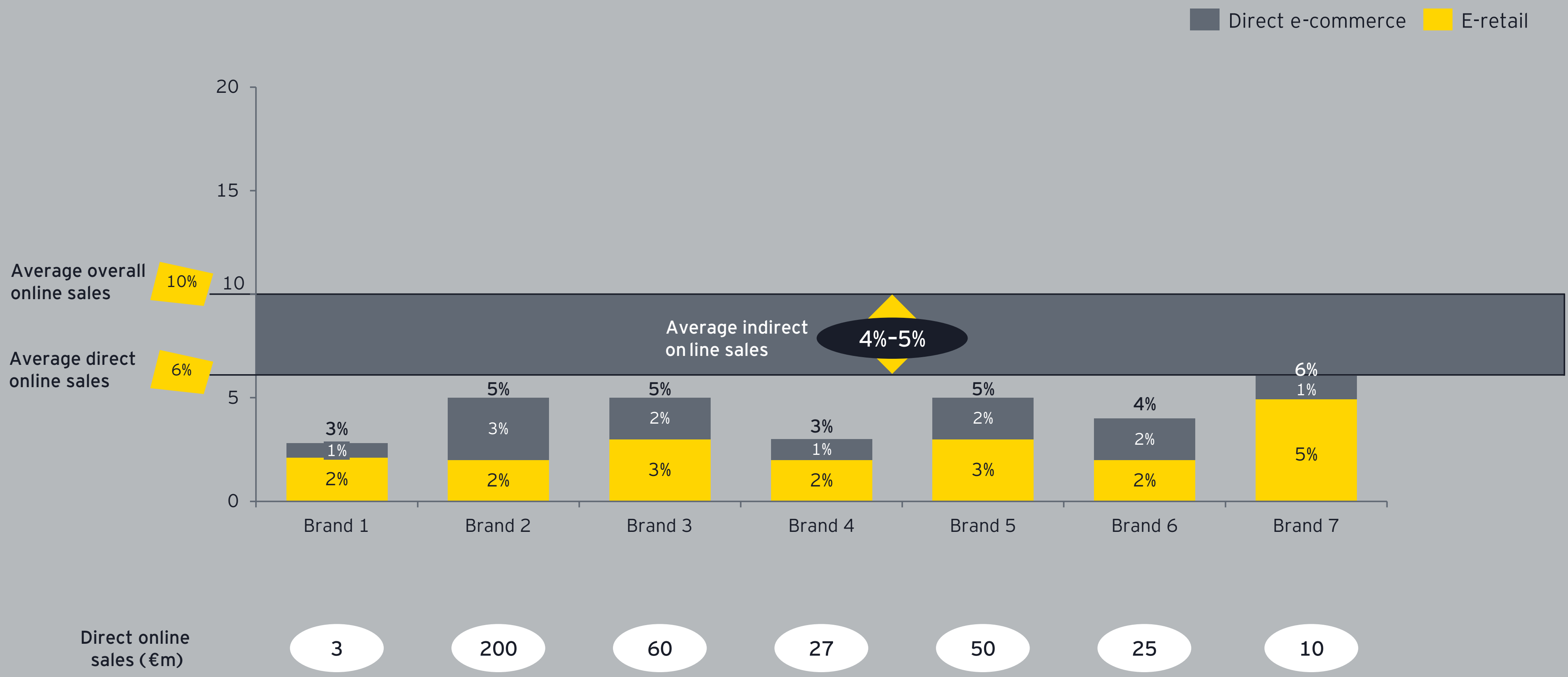
- Fashion and accessories store traffic has been in constant YoY decline in the last five years
- The CAGR over this period has been -6.0%
- Over the period, store traffic fell by 29%

Source: EY analysis; ShopperTrak data; and Wells Fargo Securities data.

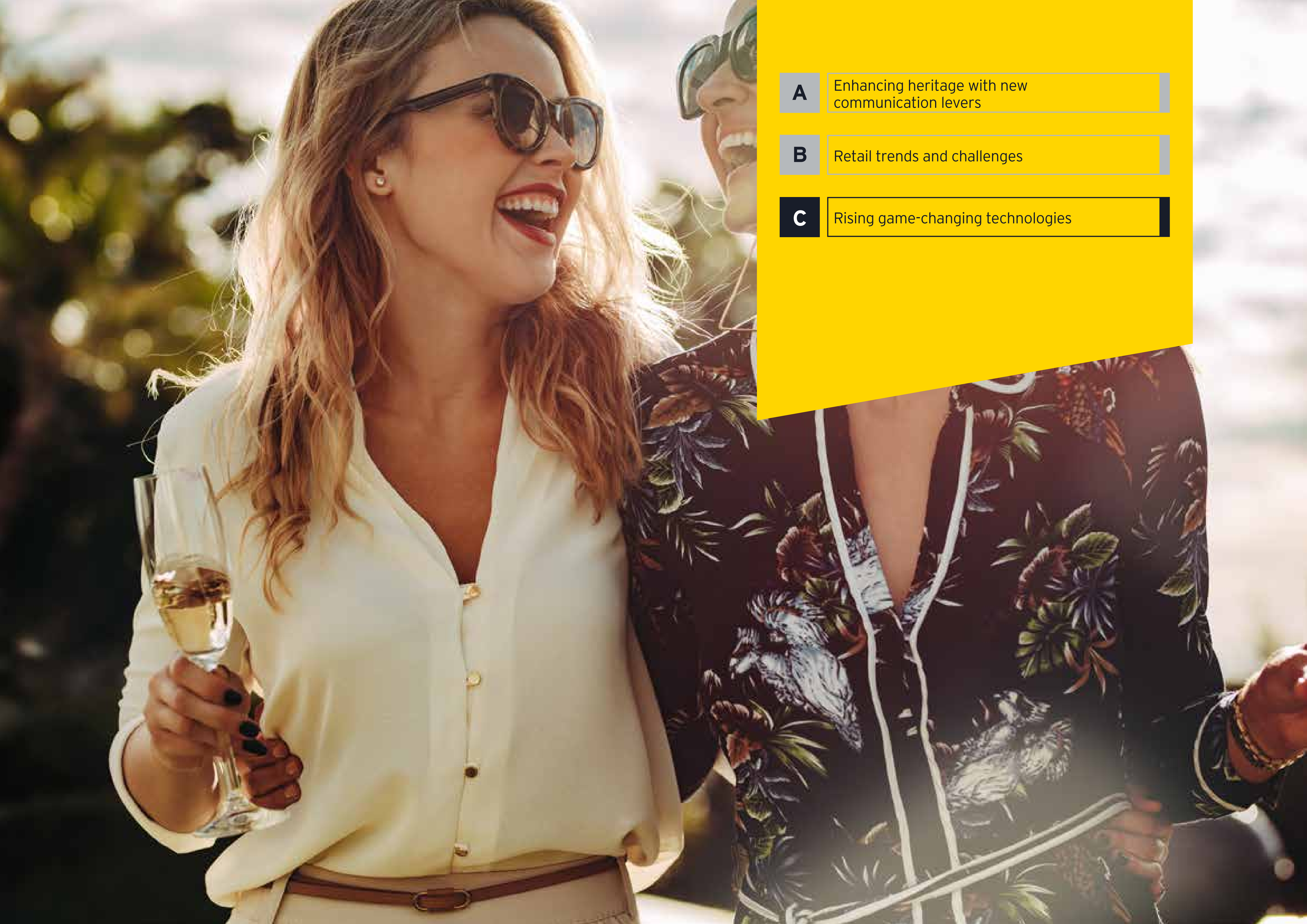
B Retail trends and challenges

Almost half of online sales occur on indirect online channels, where brands have little or no control over what products, at what price and in which environment products are sold

Benchmark e-commerce luxury and premium markets



Source: Public information and EY analyses.



- **A** Enhancing heritage with new communication levers
- **B** Retail trends and challenges
- **C** Rising game-changing technologies

C | Rising game-changing technologies

Fashion is facing the disruption game and rising technologies are fundamentally changing the rules of the game

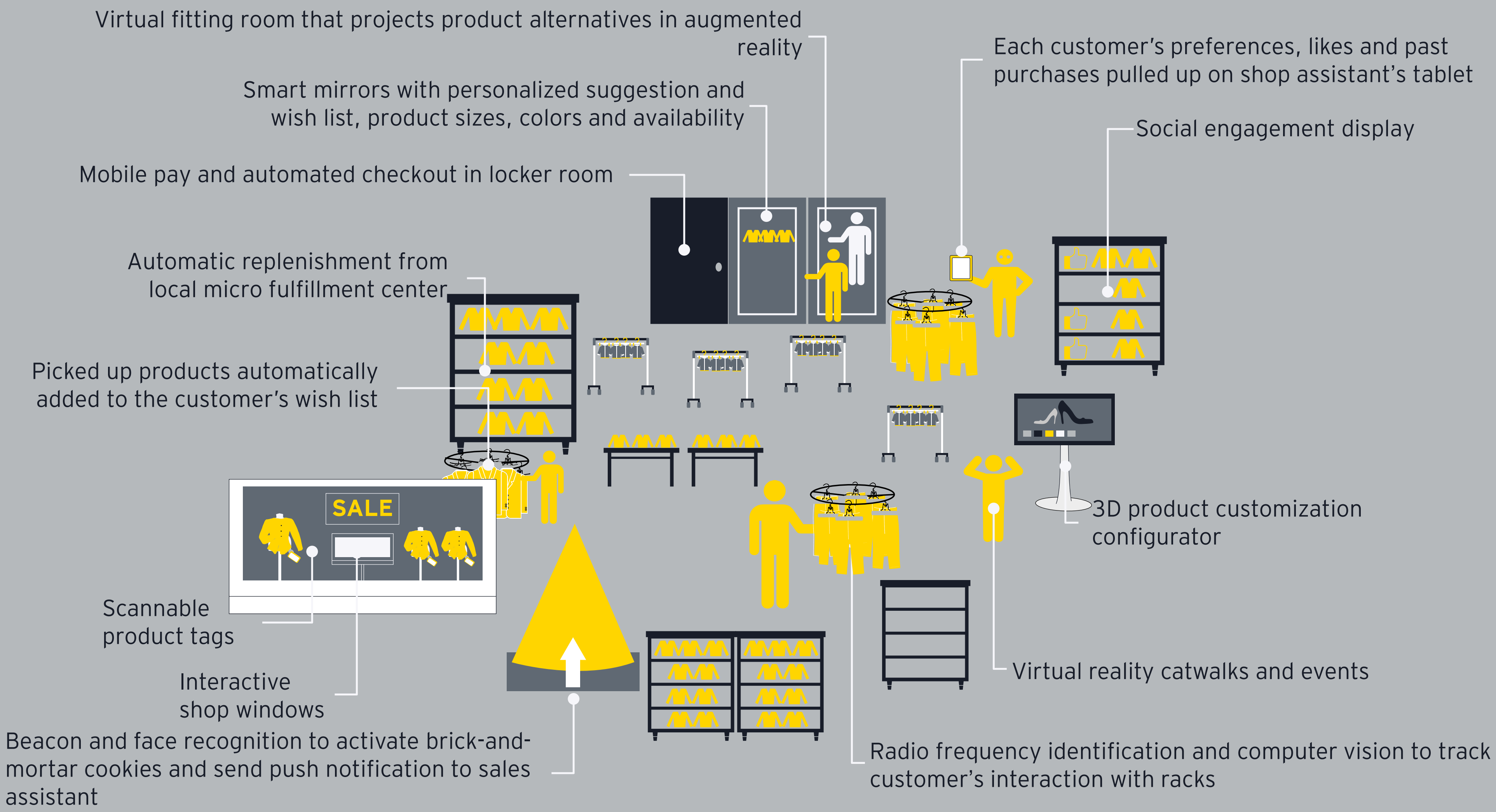
Key purchasing factors	Intelligence	Product development	Merch and retail buying	Customer engagement	Production	Logistics and fulfillment	Retail conversion
	Steps leading to the retail conversion						
Here and now Customers want to buy what they see, when they see it, anywhere	Predictive analytics can anticipate customer behavior and link these insights to the retail strategy	Collaborative and digital asset management solutions can speed up the product development process	Data-enabled fast replenishment cycles make certain customers find the product in store without increasing stock	Drive-to-store technologies and strategies can target the "right" customer for the products in store	Technologies that enable small product batches to shorten the calendar, making products more timely and relevant	Micro fulfillment, inventory ensure management, local and shared inventory (AV), last-mile delivery to make certain of availability	Universal login, brick-and-mortar cookies make customer data and preferences available to the store personnel
Experience The act of buying a product must be an enticing experience itself	Curation, search, chatbots and visual recognition enhance the experience, while generating valuable data			Digital technologies help by reshaping the role of the retail store for the era of the experience		Automated checkout, digital payment, evolved loyalty program enhance the experience in the store and after	Virtual reality and augmented reality, virtual fitting rooms, smart mirrors, etc., can drastically change the customer experience in store
Exclusivity Cool may come from everyday life, but it is accessible to only a few		Agile development, digital prototypes, virtual showrooms to test products and stretch brands for drops and collaboration		Sophisticated use of digital tech and social networks helps engage a more exclusive target audience	Technologies that allow for small production batches make it possible to run exclusive capsule and collaboration		Focus next slide
Purpose Authenticity, commitment to a cause, even political stances		Digital tech, end-to-end enablers make product development cheaper, creating feasible go-to-market route for small niche brands		Digital technologies enable circular economy business models: rent, pre-owned and pre-loved, refurbished	Smart materials for more sustainable products and blockchain tracing technologies for radical transparency	Digital off-price solutions help reduce the environmental impact of fashion production	
Intimacy Engaging at a personal level and instilling a sense of belonging	In store data collection and radio-frequency identification (RFID) analysis gather data about customer preferences and in-store behavior	Virtual prototyping makes product development cheaper, enabling wider and more experimental collections	Artificial intelligence and localized merch software can make products more relevant and retail buying more focused	Customized suggestion, personal shopping platforms let brands engage at a more intimate level	Mass customization (made to order, 3D printing, print on demand, sewbots) raises the bar in terms of engagement	Digitally enabled omnichannel in-store pickups and returns enable a more personal relation with customers	Availability of customer data and the rise of sizing technologies enable a more intimate in-store relationship

Source: EY-Parthenon analyses; company annual reports.

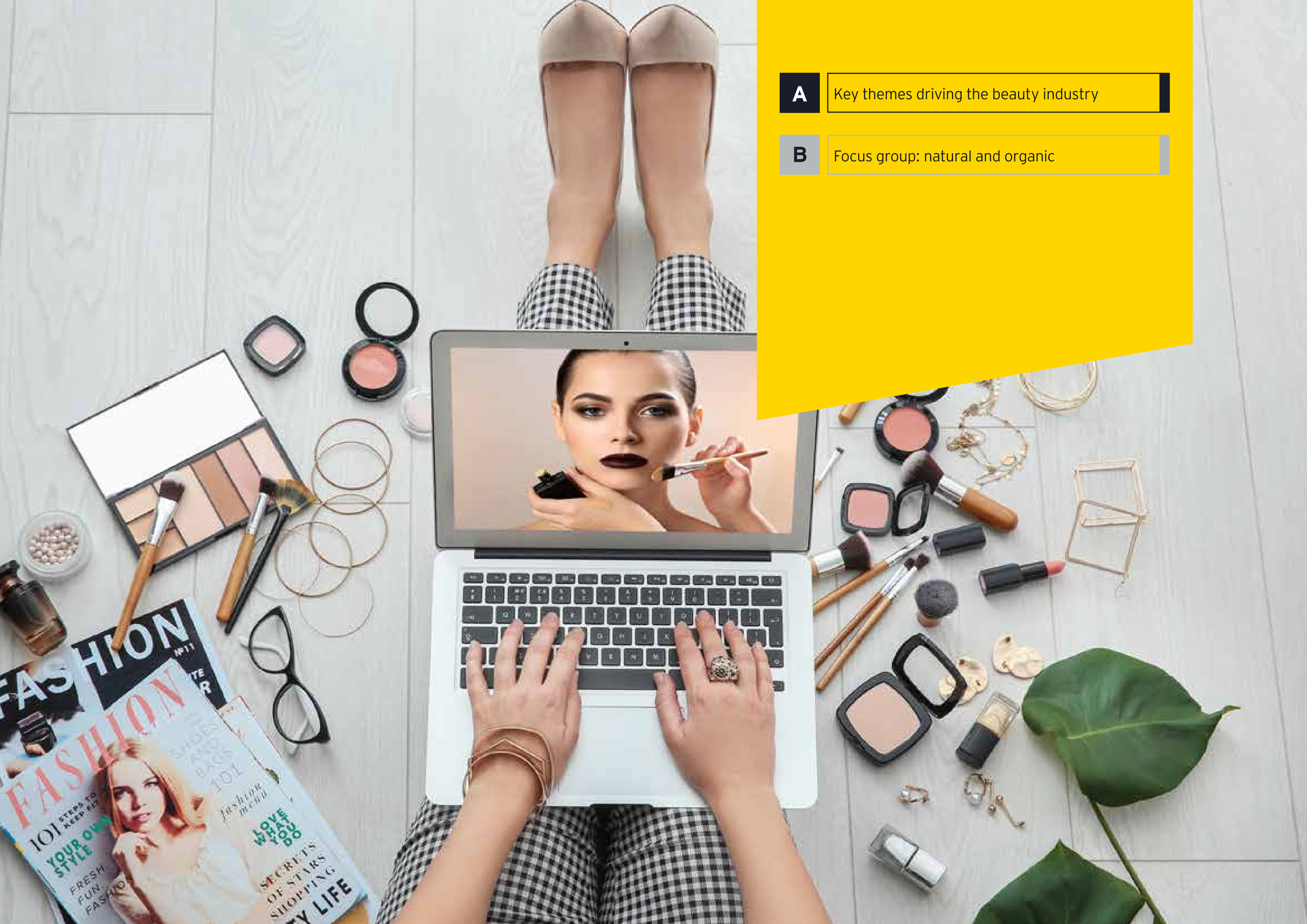
Very relevant | Relevant | Moderate relevance

C Rising game-changing technologies

A number of technologies have been developed specifically to enhance the in-store customer experience and improve conversion and other retail performances



Cosmetics industry overview



A Key themes driving the beauty industry

B Focus group: natural and organic

A Key themes driving the beauty industry

Customers demand more personalized, gender neutral, organic, and minimalistic skin care and cosmetic products to be presented and offered through innovative technological tools

Gender evolution

While some categories are still strongly focused on gender, makeup is going toward a gender-neutral approach

Natural and organic

Consumers, in particular younger generations, are increasingly passionate about environmental causes

Influencers and makeup artists

The role of the influencers and makeup artists to sustain the brands, to inform about the products and their use

Beauty tech products

With the spread of Internet of Things, it is expected we will see more beauty devices become affordable and mainstream

Personalization and inclusion

Customers are looking more and more into the possibility of creating their unique products

Japanese beauty boom

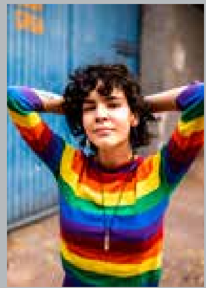
Thanks to its perception of a minimalistic and luxurious approach to beauty, Japanese cosmetics are spreading worldwide

A Key themes driving the beauty industry

Gender evolution will fuel the beauty and cosmetics market

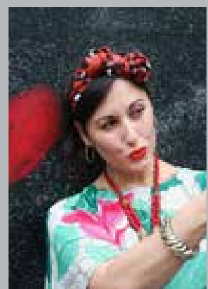
1960s

1990s



2000s

Up to a few years ago, the cosmetics industry was focused on the female application



2010s

The 2010s saw “just-for-men” applications become an increasingly relevant growth driver

Just-for-men CAGR 2018-23E

+7.5%	Skin care
+6.8%	Fragrances
+6.2%	Hair care

2020s

The complete novelty is the overgender approach, mainly boosted by the LGBTQ community and focused on the color cosmetics category

Gender neutral

The gender-neutral strategy will contribute to the color cosmetics category turnover with €5 to €6b in 2023

Source: Euromonitor data, Instagram (pictures), EY analyses.

A Key themes driving the beauty industry

Personalization can be inclusive

"It was important that every woman felt included in this brand

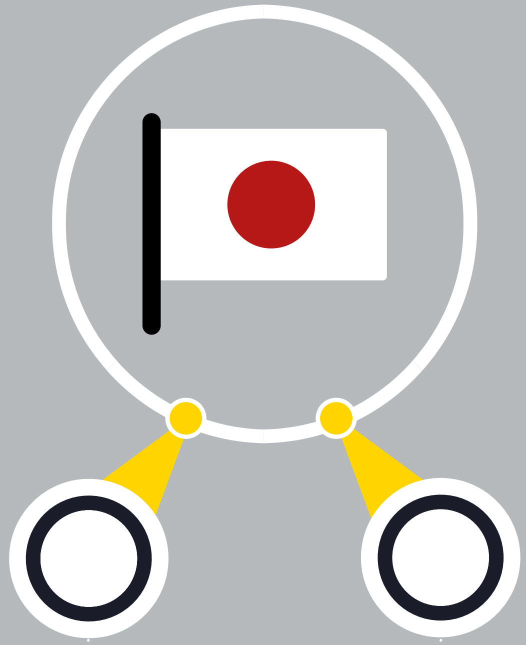
I never could have anticipated the emotional connection that women are having with the products and the brand as a whole. Some are finding their shade of foundation for the first time, getting emotional at the counter

Rihanna
Fenty Beauty brand, Time 2017

Source: Lang, C. (November 16, 2017) *"Rihanna on Building a Beauty Empire: 'I 'm Going To Push the Boundaries in This Industry'"*, Time magazine

A Key themes driving the beauty industry

Japanese style beauty based on tradition, rituals, simple regimens with multipurpose products will grow double digit in the next few years



Kao Corporation reached €12.124m in 2018

Pillar of the future growth:

- 4% of the sales value invested in R&D activities
- A distinctive corporate image
- High-profit global consumer goods company
- High level of return for shareholders
- Net sales target for 2030: ¥2.5t

Shiseido reached €8.802m in 2018 with a focus on skin care (approximately 50% of total turnover)

Pillar of the future growth:

- Future selection and concentration of brand business
- Acceleration of digitalization and new business development
- New value creation through innovation
- People first
- New global management model

Source: Euromonitor data; company annual reports (2018 for Shiseido, 2019 for Kao Corporation); EY analyses.
Note: Euro-to-yen conversion = 0.01.

A Key themes driving the beauty industry

Influencers and makeup artists

Makeup artists: the making of and professional use

- Through close collaboration with brands and celebrities, makeup artists are going to represent the way to communicate the features and the use of the products
- They work for everyone involved: the single celebrities, for the brand directly, for the fashion shows, for the magazines as beauty contributors
- Most brand-new companies invest in a makeup artist, leveraging their reputation to enhance their brand awareness in a short period of time
- Their presence on various social media is huge, and their content production, based on pictures and videos (mainly making), is spread out through Instagram, Pinterest and YouTube

The influencer evolution

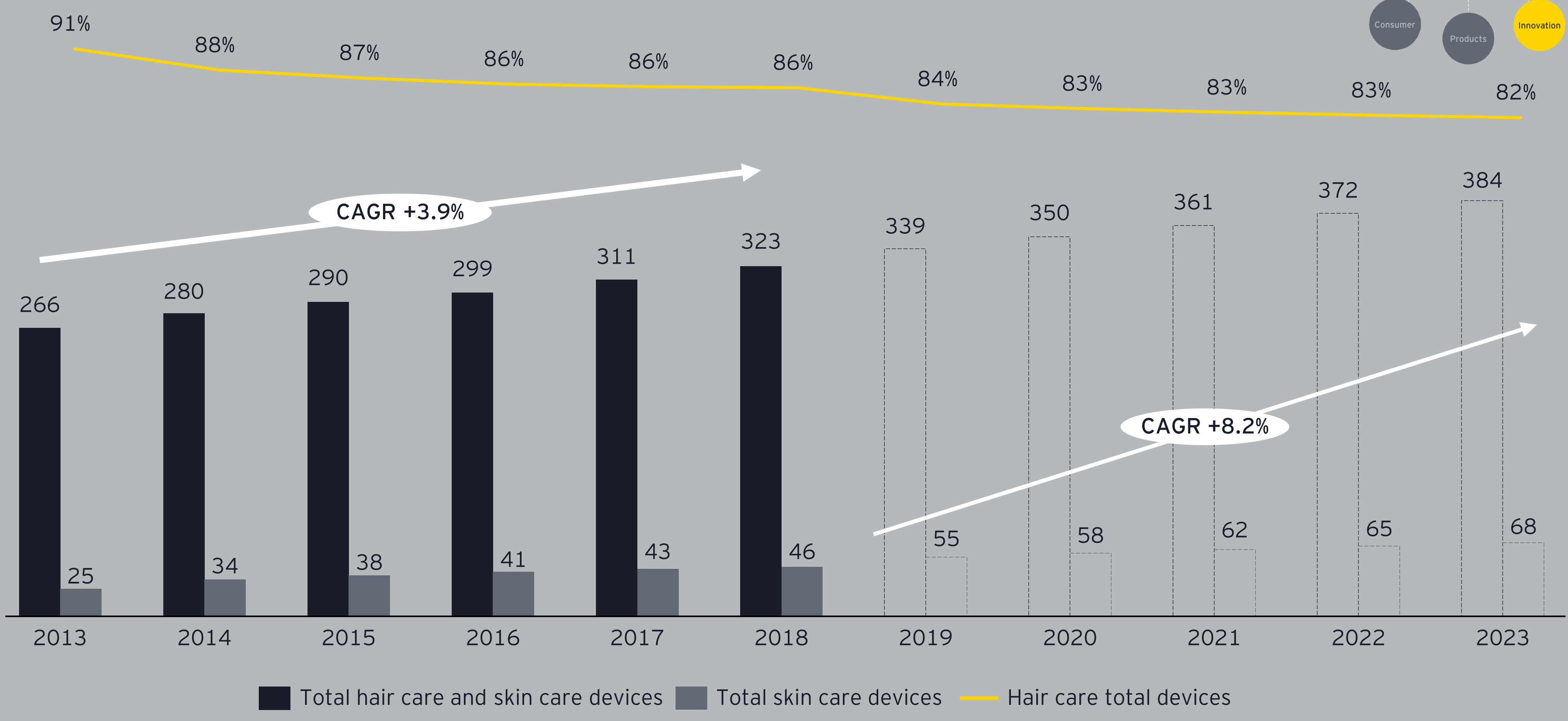
- The traditional role of the influencer is mainly based on the promotion of brands and recommendations as products' features evolve
- Rihanna launched Fenty Beauty in 2017 after collaborating with MAC Cosmetics; Fenty Beauty is developed with LVMH and is sold through Sephora stores worldwide; Fenty Beauty label generated €500m in the first year of activity
- Chiara Ferragni, launched a limited edition co-lab with Lancôme in May 2019, distributed online by Lancôme at Douglas and at Nordstrom in US

Source: Instagram (pictures), EY analyses.

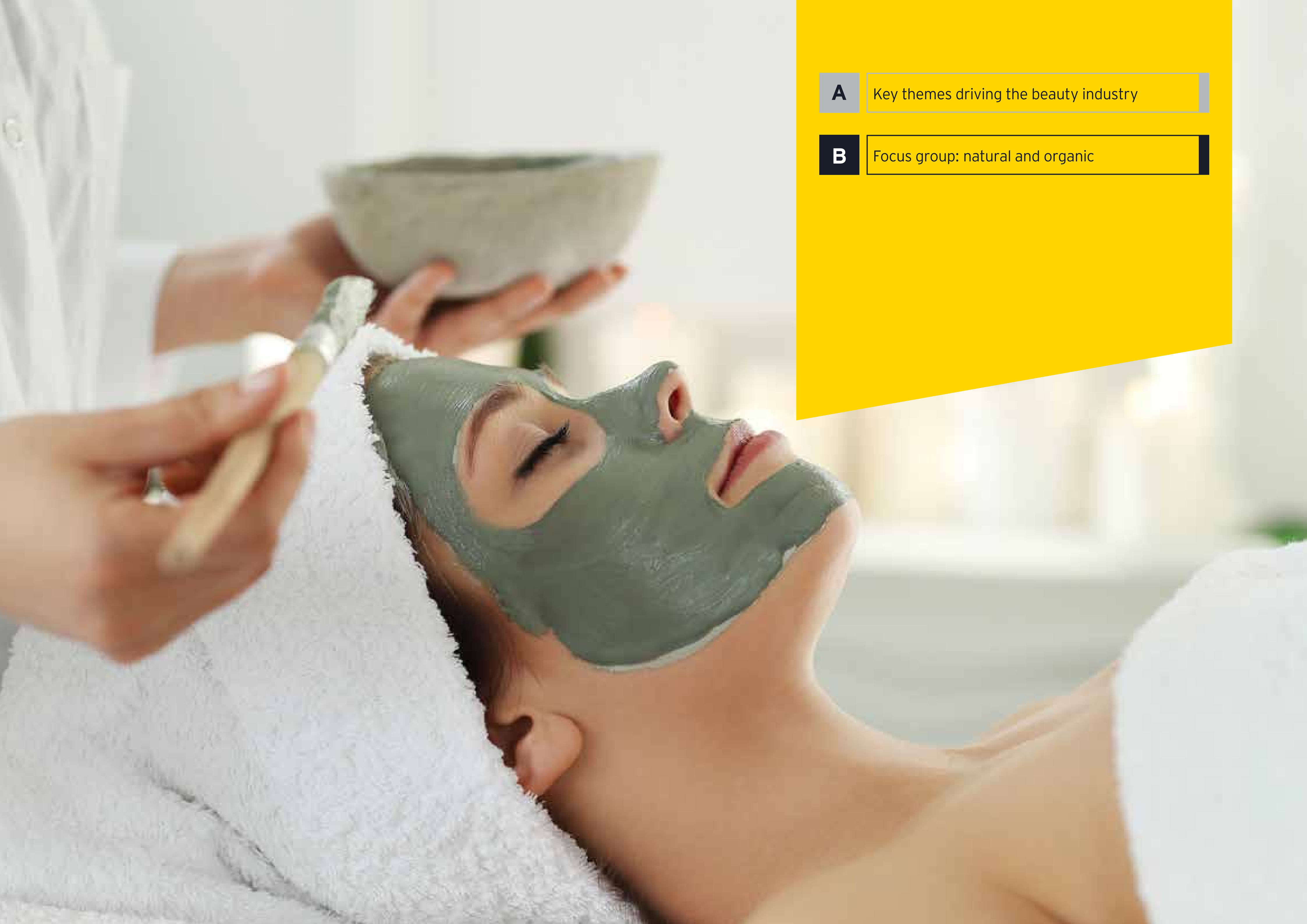
A Key themes driving the beauty industry

A new generation of devices based on artificial intelligence, augmented reality and smart diagnosis are acting as virtual makeup experts and integrated with social media

Hair care and skin care devices volumes (millions, %)



Source: Euromonitor data; EY analyses.



B Focus group: natural and organic

How important is sustainability in a consumer's mind? Conscious and subconscious think differently. Umana Analytics and EY unveiled the hidden answer

- The study was conducted in collaboration with Change it to Umana Analytics (www.umana-analytics.com), a company specialized in market research and consumer neuroscience.
- The study was carried out on the product category facial creams, on a sample of 400 women (as described on page 58). To avoid sample bias, the products presented to the women were brand free and were marked as organic or not organic.

- **The conscious answer – methodology: conjoint analysis**
  - Conjoint analysis is an established research technique used to model the consumer's decision-making process.
  - Consumers evaluate and compare a range of different products, each of them with a unique combination of features and attributes.
  - A conjoint analysis is designed to extrapolate the importance of each product attribute and the impact that a change in the product configuration may have on the consumer's willingness to buy.
  - Each product is described by a series of features (i.e., attributes), such as the price or brand. Each attribute has multiple variations (i.e., levels). Participants are exposed to a series of product configurations and asked to declare how likely they are to buy each product combination on a scale from 0 to 100.

- **The subconscious answer – methodology: implicit association task**
  - Studies have shown that human behavior is driven by brain processes that operate below our conscious awareness, to the point that it is almost autopilot that determines most of our decisions. For this reason, it is not possible for market research to only rely on self-reported answers of the interviewees (i.e., explicit answers) as they can be easily influenced by social expectations or by the mental representation that we have of ourselves.
  - The Implicit Association Task (IAT) is a response-time measure designed to detect the strength of associations between target categories (organic and classic inorganic cosmetics) and attribute categories (positive and negative). Since its presentation by Greenwald, McGhee and Schwartz in 1998, it has been widely used and applied under rigorous scrutiny by the scientific community.

The study
definition of topic and methodology

EY Building a better working world | umana

Conjoint analysis
Selected method to carry out the investigation on the conscious mind

Subject of investigation
What are the key factors influencing the willingness to buy facial day cream?

Implicit association task
Selected method to carry out the investigation on the subconscious mind

Subject of investigation
What is the emotional response to organic products? How much does the organic characteristic affect the willingness to buy?

B Focus group: natural and organic

The panel of the study included 400 women currently living in the US and UK in large cities with medium to high incomes and currently between 23 and 54 years old

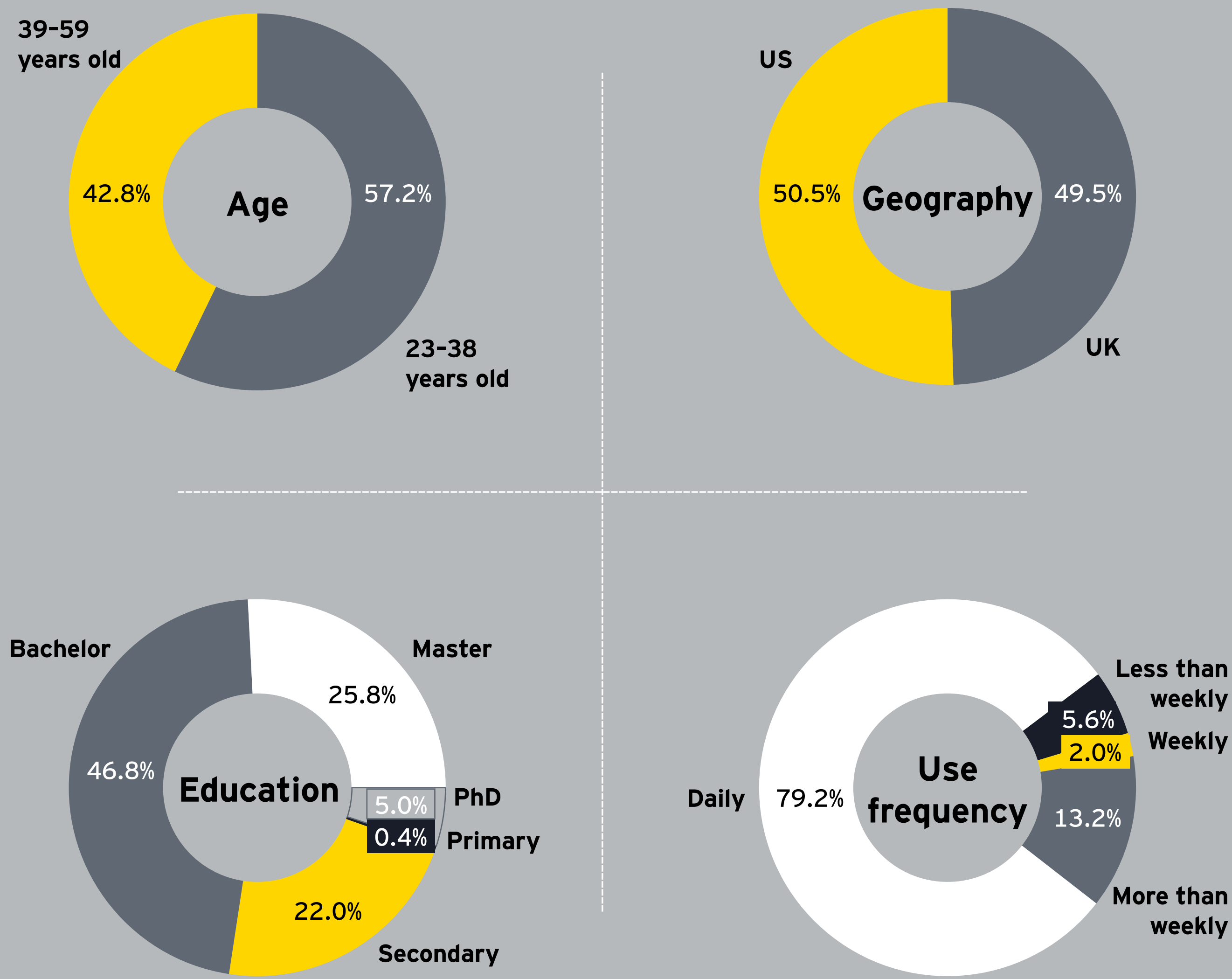
Presenting the panel

The panel was constructed in order to reflect this specific target segment.

The panel included 400 women currently living in the US and UK in large cities with with medium to high incomes and currently between 23 and 54 years old.

The age range was specified in order to directly explore and compare millennials (23 to 38 years old) with the previous generation, i.e., Gen X (39 to 54 years old).

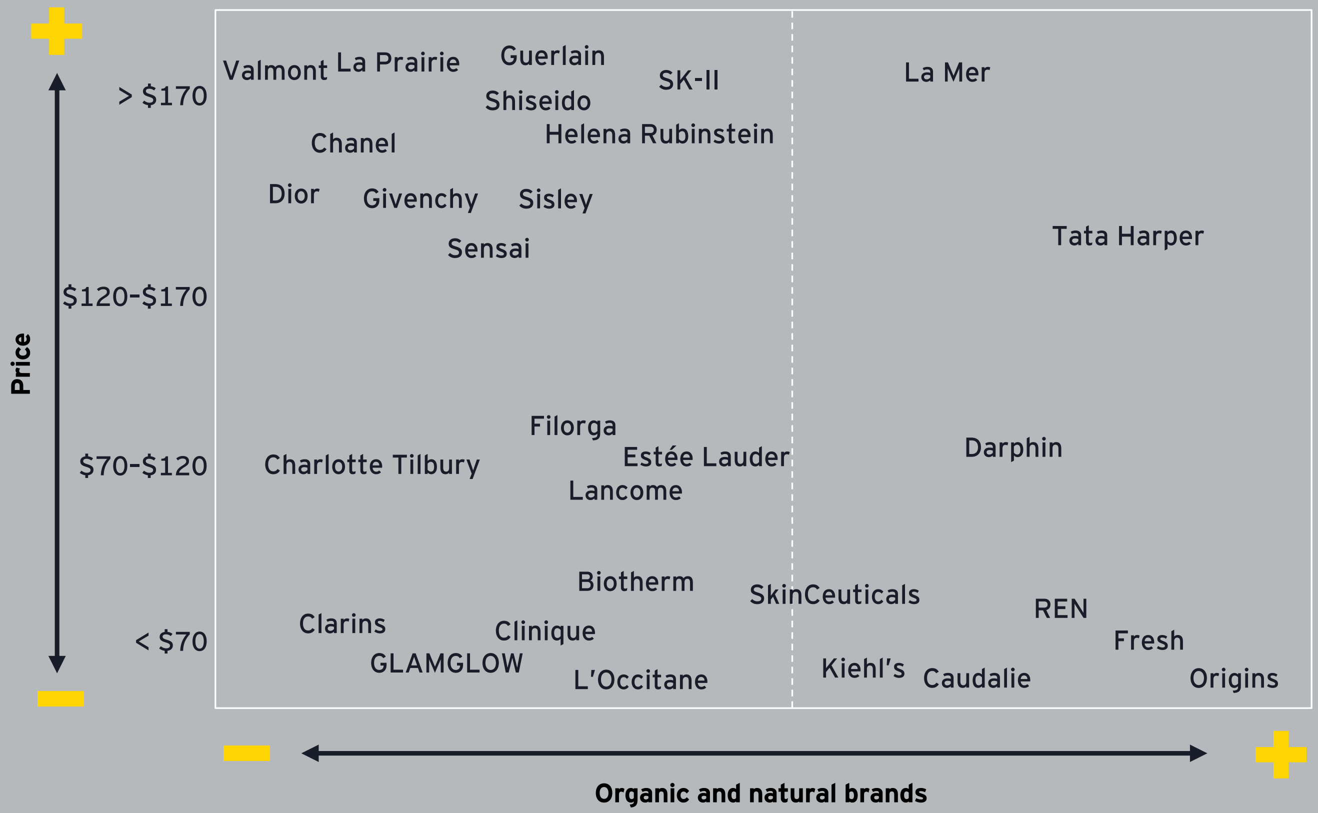
This comparison can provide significant insights for businesses. In fact, preferences, expectations and behaviors of millennial consumers are widely acknowledged to be different from previous generations and a consistent number of businesses still struggle when trying to engage with millennial customers.



B Focus group: natural and organic

The features and attributes of the facial creams used in the study were selected on the basis of a market benchmark that identified four price ranges a spectrum of perceived levels of sustainability of the products present today on the market

Market benchmark to determine the product clusters used in the study



Features

- Contains minerals
- Organic
- Hypoallergenic
- Parabens-free
- Fragrance-free
- Acetone-free

Source: Brand.com website; Sephora website.
Note: Positioning based on highest price product for the category moisturizing cream (no anti-age or specific treatments) for selected brands as of January 7, 2019.

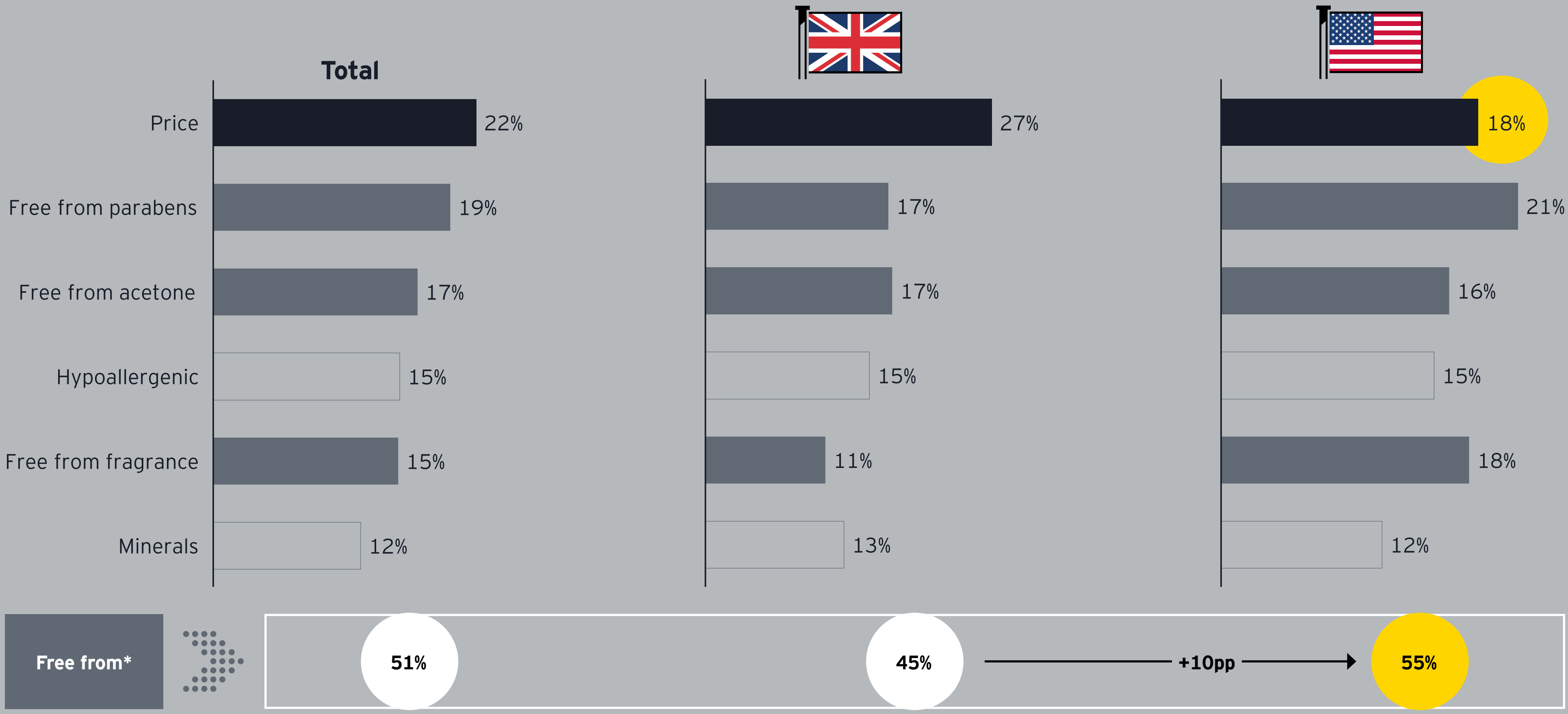
B Focus group: natural and organic

Compared to British consumers, US respondents' willingness to buy is less affected by price, while more affected by the presence or absence of the additional chemical components in the product

Subject of investigation: what are the key factors influencing the willingness to buy facial day cream?(1/2)

Conscious

Key factors influencing willingness to buy (UK vs. US) (% of respondents)



Source: Umana Analytics conjoint analysis and IAT; EY analyses.
Note: *Free from = free from parabens, acetone and fragrance

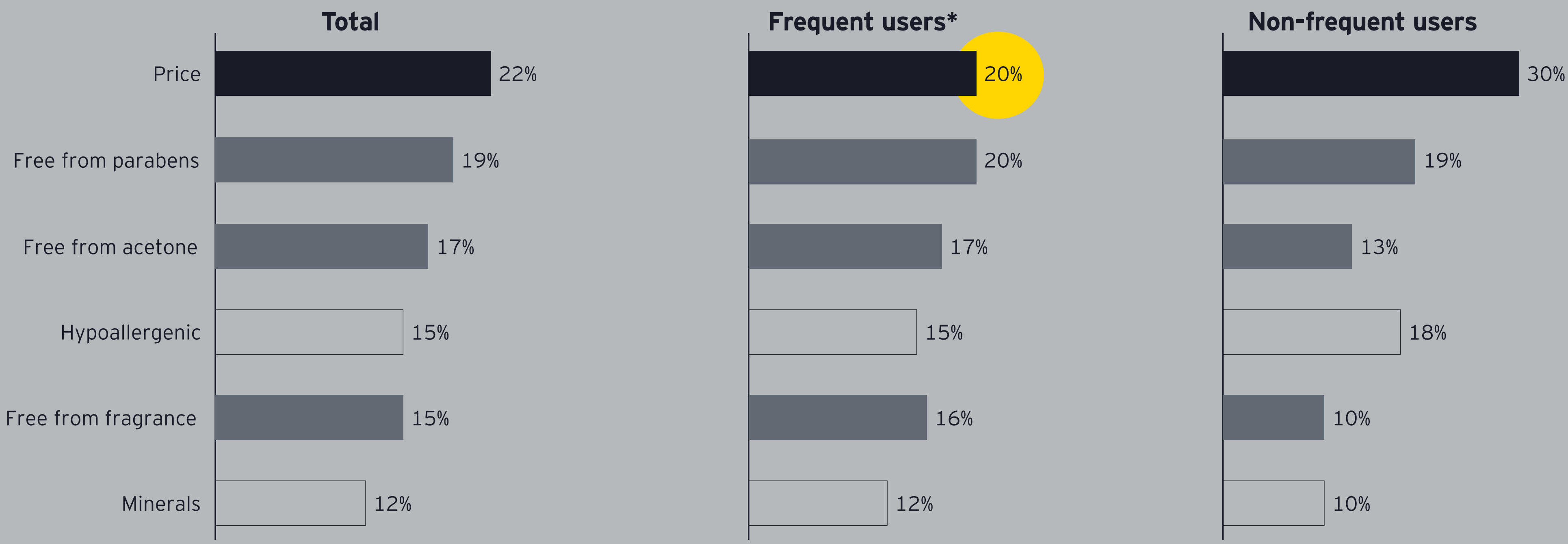
B Focus group: natural and organic

Overall, frequent users seem to appreciate a product free from chemical additional components more than non-frequent users, for whom price is by far the most relevant factor

Subject of investigation: what are the key factors influencing the willingness to buy facial day cream? (2/2)

Conscious

Key factors influencing willingness to buy (frequent vs. non-frequent users) (% of respondents)



Free from

51% 52% 43%

Source: Umana Analytics conjoint analysis and IAT; EY analyses.
Note: * Frequent users = daily or more than weekly consumers.

B Focus group: natural and organic

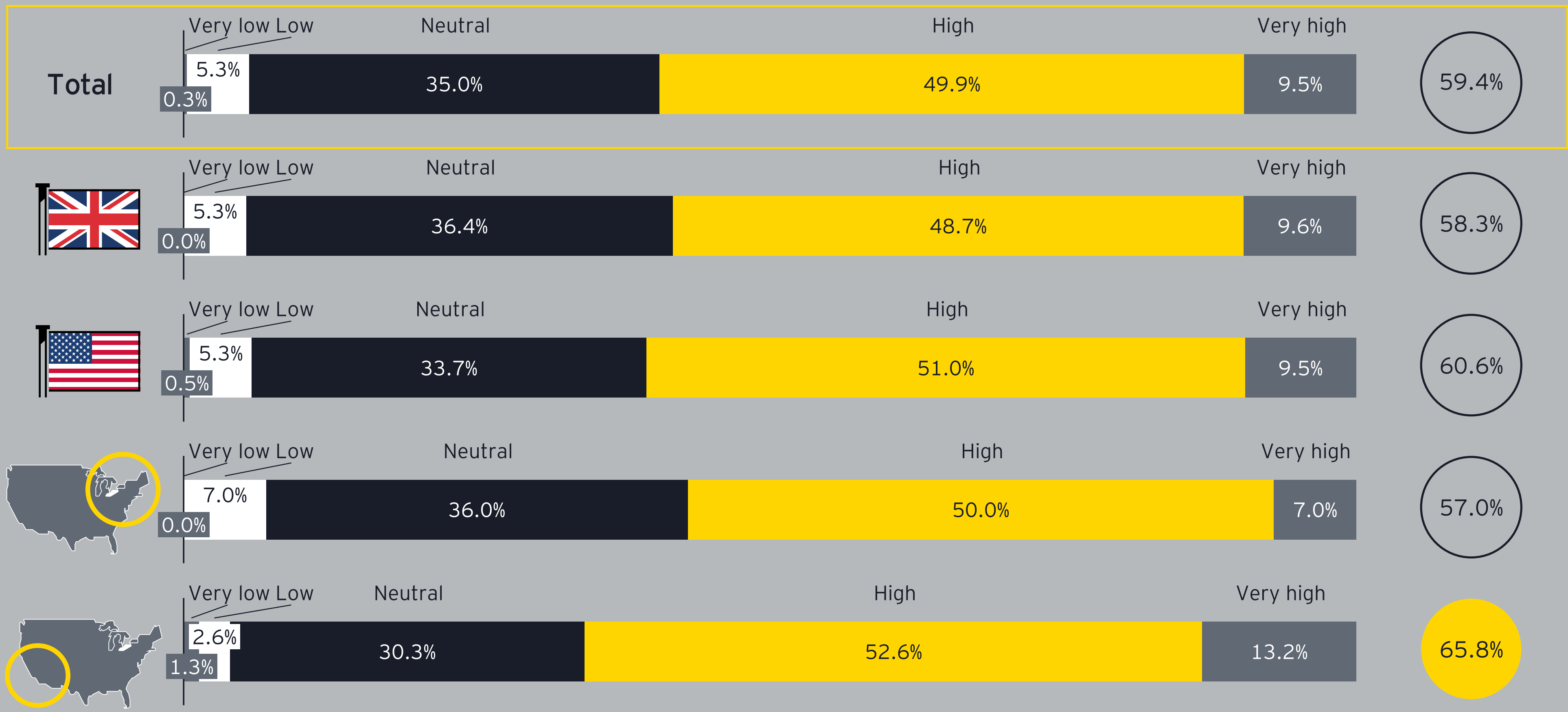
American consumers, particularly those located on the West Coast, appear to be affected by organic characteristics more than the British

Subject of investigation: what is the emotional response to organic products? How much does the organic characteristic affect the willingness to buy? (1/2)

Subconscious

Strong propensity*

Propensity for organic products (% of respondents)



Source: Umana Analytics conjoint analysis and IAT; EY analyses.
Note: * Strong propensity = high and very high.

B Focus group: natural and organic

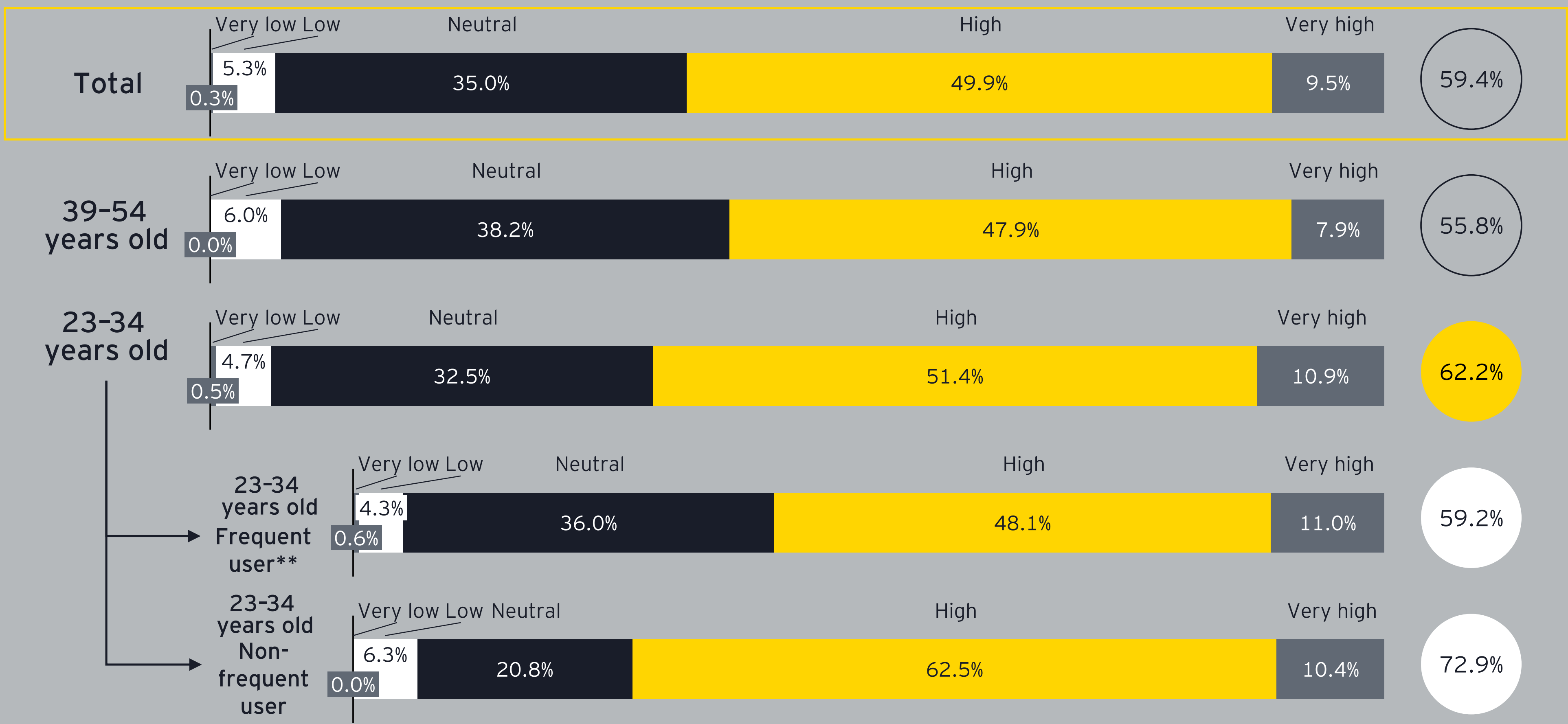
While conjoint analysis identified frequent users as the most concerned about natural ingredients, IAT identified non-frequent users as having the highest propensity for organic products

Subject of investigation: what is the emotional response to organic products? How much does the organic characteristic affect the willingness to buy? (2/2)

Subconscious

Strong propensity*

Propensity for organic products (% of respondents)



Source: Umana Analytics conjoint analysis and IAT; EY analyses.

Note: * Strong propensity = high and very high. ** Frequent users = daily or more than weekly consumers.

B Focus group: natural and organic

Conclusions

Subject of investigation

What are the key factors influencing the willingness to buy facial day cream?

- Overall, price is the most relevant criterion (22% of respondents)
- US respondents are more aware about the additional chemical components and less influenced by the price compared to British consumers; accepting to pay more for a "free from" product
- Frequent users seem to appreciate a product free from chemical additional components more than non-frequent users, for whom price is by far the most relevant factor

Subject of investigation

How much does the organic characteristic affect the willingness to buy?

- 59.4% of the total respondents show a high propensity for organic products
- US population is on average more sensitive to organic topics; 65.8% of Americans (from the West Coast) show a high propensity for organic products
- 72.9% of the millennials and non-frequent users subconsciously prefer organic products

Source: Umana Analytics conjoint analysis and IAT; EY analyses.

Appendix

A Detailed tables of main financial parameters and market multiples

Luxury and cosmetics sample of companies and associated operating aggregates (sales and EBITDA margin)

Luxury

Sales (€b)	2018A	2019E	2020E	2021E
LVMH	46.8	50.4	53.6	57.7
Richemont	14.0	15.2	16.2	17.5
Swatch	7.6	7.9	8.2	8.6
Hermès	6.0	6.6	7.1	7.8
Kering	13.7	15.7	17.0	18.2
Tapestry	5.2	5.4	5.7	5.9
EssilorLuxottica	16.2	17.1	18.1	19.1
Farfetch	0.5	0.7	1.0	1.2
Ralph Lauren	5.6	5.7	5.9	6.1
Tiffany	4.0	4.0	4.2	4.4
Burberry	3.2	3.2	3.4	3.6
Hugo Boss	2.8	2.9	3.0	3.2
Safilo	1.0	1.0	1.0	0.8
Tod's	0.9	1.0	1.0	1.1
Prada	3.1	3.3	3.4	3.6
Ferragamo	1.3	1.4	1.5	1.5
Brunello Cucinelli	0.6	0.6	0.7	0.7
Capri Holdings	4.7	5.3	5.6	5.9
Chow Tai Fook	7.6	8.1	9.0	10.1
Moncler	1.4	1.6	1.8	2.0
Total sales	146.2	157.1	167.4	179.0

EBITDA margin	2018A	2019E	2020E	2021E
LVMH	25.5%	25.8%	26.0%	26.6%
Richemont	21.7%	20.5%	20.9%	21.6%
Swatch	19.4%	20.0%	20.8%	20.5%
Hermès	39.5%	37.7%	37.8%	37.8%
Kering	32.5%	31.7%	32.4%	34.3%
Tapestry	21.3%	21.0%	21.9%	22.4%
EssilorLuxottica	22.1%	21.8%	22.2%	22.5%
Farfetch	-24.9%	-20.9%	-9.8%	-1.7%
Ralph Lauren	15.8%	16.3%	16.9%	17.5%
Tiffany	22.9%	24.3%	22.7%	24.8%
Burberry	20.4%	21.0%	21.8%	23.1%
Hugo Boss	17.5%	17.7%	18.1%	18.7%
Safilo	0.8%	4.0%	7.5%	0.6%
Tod's	12.6%	13.2%	13.9%	14.2%
Prada	17.5%	18.9%	19.0%	20.1%
Ferragamo	16.0%	15.8%	16.7%	17.7%
Brunello Cucinelli	17.4%	17.4%	17.5%	17.8%
Capri Holdings Limited	21.1%	20.0%	19.8%	20.0%
Chow Tai Fook	11.9%	11.5%	11.8%	11.8%
Moncler	35.2%	34.5%	34.6%	35.1%
Average	18.3%	18.6%	19.6%	20.3%

Cosmetics

Sales (€b)	2018A	2019E	2020E	2021E
L'Oréal	26.9	28.7	30.3	32.6
Estée Lauder	12.2	13.0	13.9	14.9
Beiersdorf	7.2	7.5	7.9	8.3
Natura	3.1	3.3	3.7	4.0
Shiseido	8.8	9.0	10.1	10.9
L'Occitane	1.4	1.6	1.7	1.9
Coty	8.4	7.8	7.8	7.9
AMOREPACIFIC	4.1	4.5	4.7	5.1
Nu Skin	2.4	2.5	2.6	2.6
Total sales	74.5	77.9	82.7	88.2

EBITDA margin	2018A	2019E	2020E	2021E
L'Oréal	22.4%	22.9%	23.1%	23.3%
Estée Lauder	20.6%	20.9%	21.7%	22.2%
Beiersdorf	17.4%	17.0%	17.3%	17.5%
Natura	13.8%	14.8%	15.9%	16.5%
Shiseido	12.4%	14.3%	15.4%	17.1%
L'Occitane	15.2%	17.1%	17.4%	16.5%
Coty	12.4%	15.1%	16.2%	16.5%
AMOREPACIFIC	14.2%	15.1%	14.6%	14.9%
Nu Skin	12.1%	15.3%	15.6%	15.6%
Average	15.6%	16.9%	17.5%	17.8%

Source: EY analysis of actual data from companies' financial statements and expected data based on consensus of several brokers' reports for each company.

A Detailed tables of main financial parameters and market multiples

Luxury and cosmetics multiple analysis

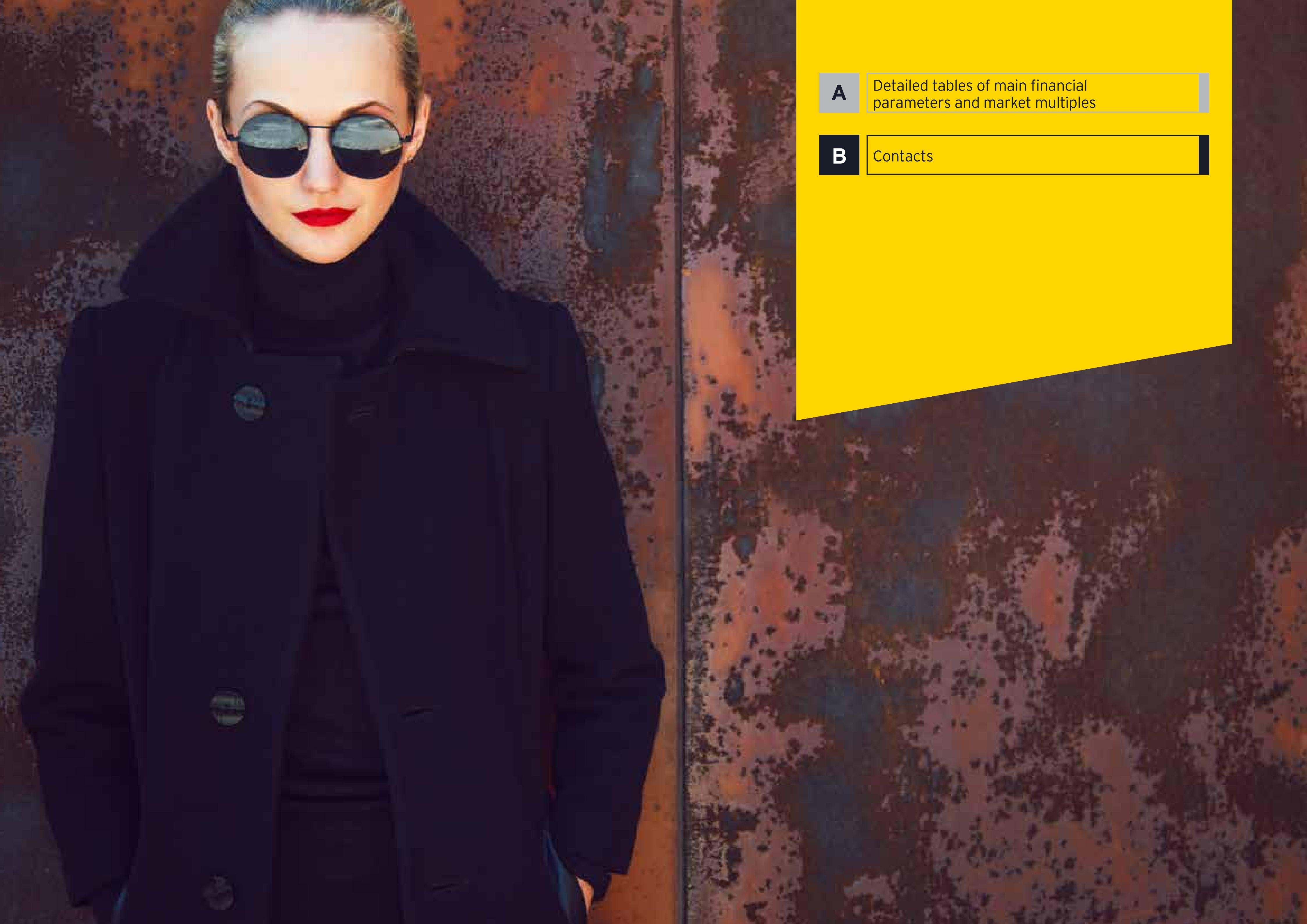
Luxury

	EV/sales			EV/EBITDA			Price to earnings		
Trading multiples	2019E	2020E	2021E	2019E	2020E	2021E	2019E	2020E	2021E
LVMH	3.3x	3.1x	2.9x	12.9x	12.0x	10.9x	22.6x	20.9x	18.8x
Richemont	2.2x	2.1x	1.9x	11.1x	10.2x	9.3x	20.2x	17.9x	15.7x
Swatch	1.6x	1.5x	1.5x	7.9x	7.3x	7.1x	17.8x	16.0x	16.0x
Hermès	8.7x	8.0x	7.3x	23.1x	21.3x	19.4x	41.3x	37.4x	33.5x
Kering	4.1x	3.8x	3.5x	13.1x	11.8x	10.3x	20.8x	18.0x	15.6x
Tapestry	1.6x	1.5x	1.5x	7.6x	6.9x	6.5x	12.5x	11.3x	10.4x
EssilorLuxottica	2.8x	2.6x	2.5x	12.7x	11.8x	11.0x	23.5x	21.7x	20.0x
Farfetch	10.9x	8.2x	6.5x	n/a	n/a	n/a	n/a	n/a	n/a
Ralph Lauren	1.3x	1.3x	1.2x	8.0x	7.4x	7.0x	16.4x	14.8x	13.5x
Tiffany	2.8x	2.6x	2.5x	11.4x	11.8x	10.1x	20.1x	18.8x	17.3x
Burberry	2.5x	2.4x	2.2x	11.9x	10.9x	9.6x	22.7x	20.6x	18.1x
Hugo Boss	1.5x	1.4x	1.4x	8.5x	7.9x	7.3x	16.5x	14.7x	13.7x
Safilo	0.3x	n/a	0.0x	7.1x	3.4x	52.5x	n/a	n/a	n/a
Tod's	1.5x	1.5x	1.4x	11.8x	10.6x	9.9x	25.9x	22.5x	19.7x
Prada	2.3x	2.2x	2.1x	12.1x	11.4x	10.3x	23.6x	25.2x	21.4x
Ferragamo	2.2x	2.1x	2.0x	13.7x	12.4x	11.2x	29.1x	26.2x	23.0x
Brunello Cucinelli	3.7x	3.5x	3.2x	21.5x	19.8x	18.2x	40.6x	39.1x	36.0x
Capri Holdings Limited	1.6x	1.5x	0.0x	7.9x	7.5x	0.0x	9.0x	8.3x	7.8x
Chow Tai Fook	1.3x	1.2x	1.0x	11.3x	9.9x	8.4x	15.2x	13.8x	11.8x
Moncler	5.3x	4.8x	4.2x	15.5x	13.8x	12.0x	25.2x	23.6x	20.6x
Average	3.1x	2.9x	2.4x	12.1x	11.0x	12.2x	22.4x	20.6x	18.5x

Cosmetics

	EV/sales			EV/EBITDA			Price to earnings		
Trading multiples	2019E	2020E	2021E	2019E	2020E	2021E	2019E	2020E	2021E
L'Oréal	4.4x	4.2x	3.9x	19.4x	18.2x	16.8x	30.2x	28.2x	26.1x
Estée Lauder	4.0x	3.8x	3.5x	19.4x	17.4x	15.9x	31.0x	27.8x	25.5x
Beiersdorf	2.5x	2.4x	2.3x	14.6x	13.8x	13.0x	25.9x	24.2x	22.6x
Natura	1.8x	1.6x	1.5x	12.1x	10.2x	9.1x	30.2x	22.6x	18.0x
Shiseido	2.8x	2.6x	2.3x	19.7x	16.9x	13.9x	45.3x	36.5x	29.5x
L'Occitane	1.9x	1.7x	1.6x	11.2x	9.9x	n/a	18.4x	15.9x	n/a
Coty	1.9x	1.9x	1.8x	12.3x	11.5x	11.0x	17.0x	15.3x	14.2x
AMOREPACIFIC	2.1x	2.0x	1.8x	13.9x	13.3x	n/a	29.2x	27.9x	25.1x
Nu Skin	1.1x	1.0x	1.1x	7.2x	6.7x	6.7x	13.7x	12.7x	12.5x
Average	2.5x	2.3x	2.2x	14.4x	13.1x	12.3x	26.8x	23.5x	21.7x

Source: EY analysis of actual data from companies' financial statements and expected data based on consensus of several brokers' reports for each company.



B Contacts

Contacts

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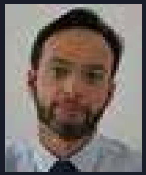

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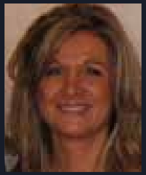

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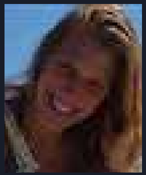

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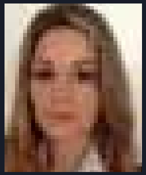

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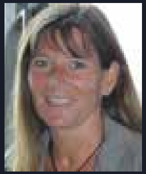

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