Mix and match the industry

The luxury and cosmetics financial factbook

2017 edition

EY

Building a better working world

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Welcome to the seventh edition of EY's luxury and cosmetics financial factbook. The report combines publicly available data with input from leaders who work with the world's leading companies in the sector. It looks at current trends, the evolution of operating aggregates, key financial parameters and valuation ratios.

The luxury and cosmetic industries are rapidly evolving. Consumers and trends are changing; client attitudes toward consumer products are bringing new perspectives around brand values and company behaviors; technology, digital and social media are reshaping consumers' approach to luxury purchases as well as luxury brands' approach to distribution channels. We are in the middle of the most disruptive revolution the luxury sector has ever seen.

There's more complexity. No longer are there clear trends, but instead different trends for different markets, product segments and levels of positioning in the value pyramid of products. Consumers play the "mix and match" game across products, markets and distribution channels, and companies have to stay close to the client, as we wrote in the 2016 factbook edition, "Keep calm and care about your consumer."

Likewise, we adapted the factbook to include more focused and detailed analyses. The luxury market for both fashion and cosmetics cannot be seen any more as a whole and single place, but must be deeply analyzed for its different components and segments to show the different trends and the pace of growth. In this edition, we have included a specific focus on the premium and entry-to-luxury segments. The luxury segment drove growth in the past, but the premium and entry-to-luxury segments are showing the highest potential in the coming years, with an expected compound annual growth rate (CAGR) of 6% and accessories are driving growth in both segments.

Here are some snapshots from the 2017 edition:

- **From the high-end luxury segment driving growth in the past decade, to the premium and entry-to-luxury segments' momentum:**
  - While high-end luxury drove growth in the past, with a 2009–12 CAGR of +11.7%, the premium and entry-to-luxury segments seem to have the highest potential in the coming years, with an expected 2016–20E CAGR of +6% vs. 3% to 4% for high-end luxury.
- **Accessories (bags, shoes and small leather goods) will continue to drive the growth, both in high-end luxury and the premium and entry-to-luxury segments, but at a different pace.**
  - Shoes are the confirmed champion category and are expected by 2020 to grow to 11% in the high-end segment and by 7% in the premium and entry-to-luxury categories.
  - The growth in bags is slowing down impacting overall growth, but shoes are accelerating it, especially in the high-end luxury segment (with an expected growth by 2020 of 11% for shoes and only 6% for bags).
- **There's a change in the way luxury is targeting its consumer from countries to nationalities and leading cities around the world.**
  - Mainland China represents less than 10% of the market as a country, while Chinese consumers generate more than 30% of the business (with Europe as their first shopping destination).
  - The US and Western Europe remain the first- and second-largest countries by size, respectively (the US with €131b and Europe with €109b in 2016, considering both the high-end luxury and premium and entry-to-luxury segments).
- **The high-end personal luxury market was worth €318b globally in 2016, reflecting a growth slowdown trend (2012–16 CAGR of +2.8% vs. a 2009–12 CAGR of 11.7%). Why are high-end luxury sales slowing?**
  - Retail footprint saturation, especially in China, showed one closure for every two openings in 2014, compared with one closure for every opening in 2016.
  - Growing consumer sophistication is seen also in China, where, like in the rest of the world, consumers are shifting from a high-end luxury total-look approach to a mix-and-match attitude, purchasing certain items from high-end product specialists and combining these with more accessible products.
  - There's increasing transparency thanks to online diffusion, with 60% of purchases digitally influenced along the purchase value chain.
- **The fashion premium and entry-to-luxury markets were worth €101b in 2016 and show strong dynamism. What is boosting the growth in the premium and entry-to-luxury segments?**
  - There's a rising urban middle class, especially in China and India (with an expectation of 1.1b people in the world in the next 15 years).
  - A strong price increase in the high-end luxury segment is opening an opportunity for the premium and entry-to-luxury segments in the €500 to €1,500 retail range. The price of iconic luxury items grew as much as three times in last 10 years.
  - There's a growing mix and match trend among consumers, which is led especially by millennials.
  - Traditional high-end luxury core consumers increasingly are interested in trading down to the premium and entry-to-luxury segments and, in some cases, also to fast fashion (especially for apparel). Last year, 41% of them did it.
  - A strong move to casual wear, like sneakers and down jackets (i.e. casualization wave), originated in the high-end luxury segment but generated an even larger opportunity in the premium and entry-to-luxury segment. In 2016 sneakers were worth €3b in the high-end luxury segment and €7b in the premium and entry-to-luxury segments in 2016.
- **Italy has a very rich industrial footprint in the premium and entry-to-luxury segments, with successful small and medium enterprises with renowned high-quality products whose brand awareness, tradition and goodwill go far beyond the revenue of a company. Five challenges premium luxury and entry-to-luxury companies have to face to win in the market include:**
  - Managing new generations and structured finance entering into the equity of companies
  - Reaching full retail potential: focus on channel EBITDA,[1] sustainable growth and delivering a strong like-for-like performance
  - Creating true merchandising capabilities: rationalize collection structure (width and breadth), manage collection development process rigorously and flawlessly, and optimize retail buying
  - Grow internationally: create a sustainable international go-to-market road map
  - Embracing digital transformation: increase capacity for reaching and engaging clients regardless of the sales channel (multi-brand, mono-brand and e-commerce strategies, etc.)

[1] Earnings before interest, taxes, depreciation and amortization.

- **The cosmetic market is growing nicely at a constant 4% rate, with the make-up segment being the most dynamic.**
  - The "selfie generation," the impact of social media and longer life expectancies all are expanding the use of cosmetic products by consumers of all ages (from teenagers to older generations).
- **Asia-Pacific represents 37% of the total cosmetics market and e-commerce is now a fact of life.**
  - 56% of potential growth in the personal luxury goods segment in the next five years will come from emerging markets.
  - Online sales are growing by more than 20% per year, accounting for more than 11% of the consumption of select cosmetics. This trend should continue as Chinese consumers use their smartphones for shopping more than their Western counterparts.
- **Consumer reward innovative companies with increased market share and ask for very specific products; and always want seamless, innovative, and customized services both pre- and post-sale.**

Although there is concentration in the industry, it is estimated that 65% to 80% of the market share is available for consolidation, creating acquisition opportunities in segments with high-growth potential (e.g., skin care, make-up, fragrances).

From a financial perspective, luxury and cosmetic companies outperformed the market, attracting investors' interest in increasing valuations again, both from a trading multiple and an M&A transaction perspective.

The M&A market is still hot in terms of the number of deals, in line with a booming 2016, although the average deal size is decreasing. In fact, the interest of buyers is more in middle-market companies, more active in the entry-to-luxury segment or in certain product categories (bags, accessories etc.). There are promising opportunities in companies "born digital" and small accessible luxury brands with high-growth potential. The US and Italy are the top countries attracting the interest of buyers in the fashion M&A arena, with an increasing role for financial sponsors, which now account for almost half of the transactions.

The cosmetic industry was also very active in 2016 from an M&A perspective, and the market is keeping up at the same level in 2017, in terms of deal count. Strategic buyers take the lion's share because they are focused on acquisitions based on the following major drivers: acquisition of new products to complement their brand portfolio, expansion in new markets (mainly emerging), research of new and innovative distribution channels, and research of innovation through digital and partnerships with high-tech companies developing new devices. The interest of the financial sponsor is growing rapidly, too.

Also in the 2017 edition of the factbook, you will find contributions from our sector leaders about selected topics of interest.

We hope you find this thought-provoking report to be insightful and helpful in wider discussions within your organization.

Do not hesitate to contact us with any comments or suggestions.

Thank you,

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Index evolution

The EY luxury and cosmetics index (represented by the companies included in the EY factbook) has outperformed the market over the last eight years with a total return of 110%, corresponding to an average yearly significant return of 8.1%.

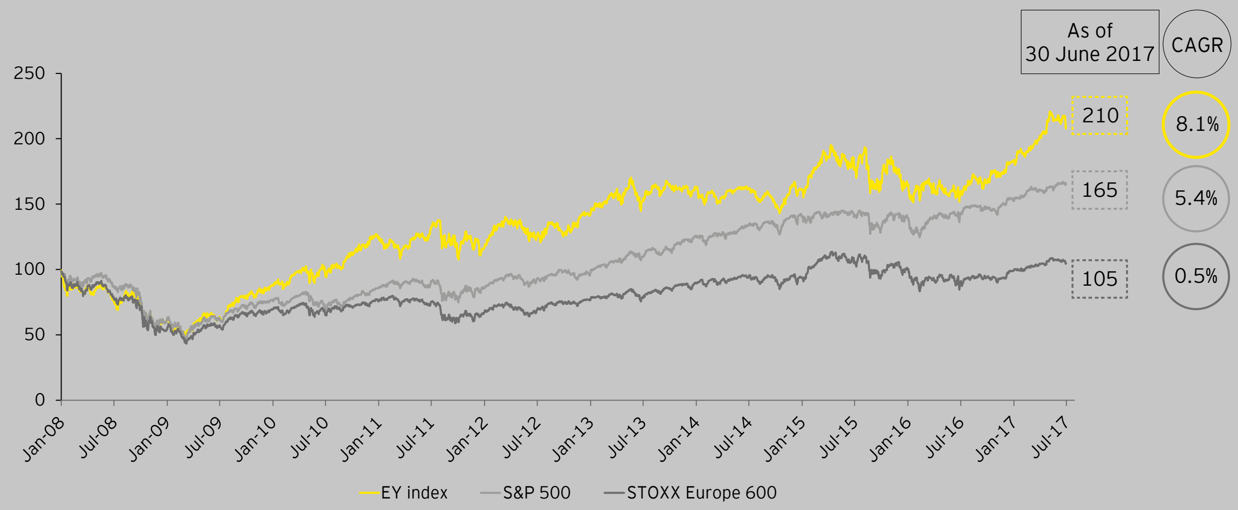
The EY index has outperformed the market particularly over the last 12 months, with a total return of 32%. The companies that showed an outstanding increase in market capitalization were LVMH and Kering in luxury and L'Oréal and Shiseido for cosmetics.

LVMH almost reached €100 billion in market capitalization, mainly driven by a rebounding demand for luxury goods in China and Europe, and sales and margins beyond estimates (with the Louis Vuitton brand driving the growth). Kering's strong performance was also due to a jump in sales (pushed mainly by Gucci and YSL), continuing its strategy of organic growth.

L'Oréal benefited from the global growth of the make-up segment, successful e-commerce strategy and new brands acquisitions. Shiseido was boosted in 2016 by strong sales in its prestige brands, and also by adding an acquisition and a new license (Dolce & Gabbana beauty).

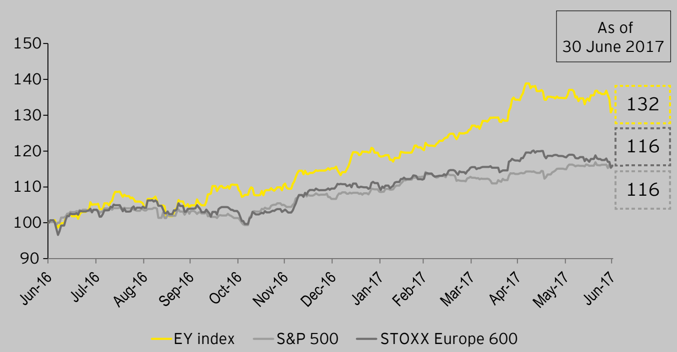
EY luxury and cosmetics index evolution compared with major indices

(Base 100 as of 1 January 2008)



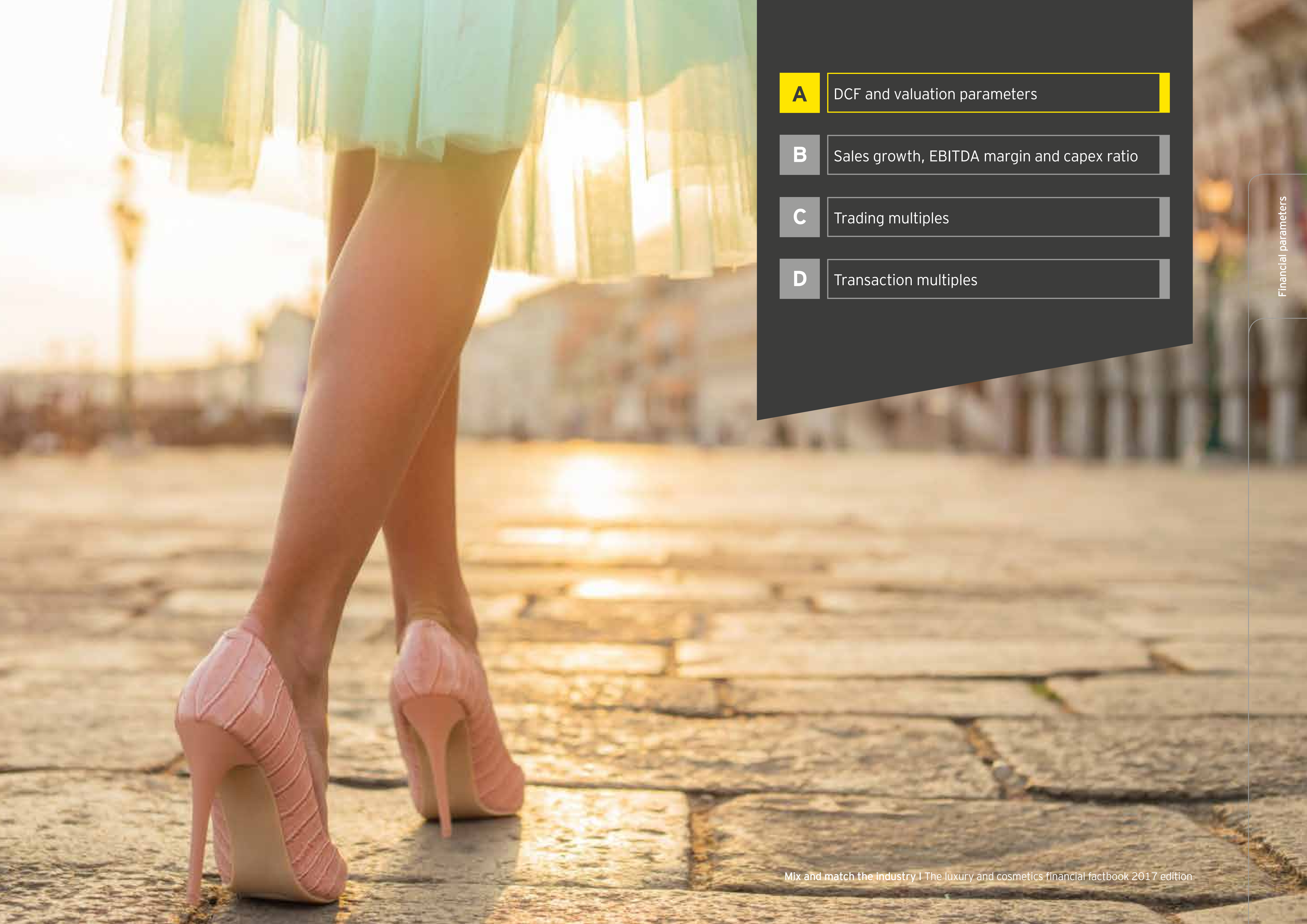
EY luxury and cosmetics index — last 12 months

(Base 100 as of 1 July 2016)



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 and revenues (each of these two parameters weighing as a half). The relative weights have been revised for each company's inclusion after its initial public offering (IPO). Finally, the evolution of the EY index has been compared with those of the S&P 500 and STOXX Europe 600 indexes, using 1 January 2008 as a starting date (rebased to 100).

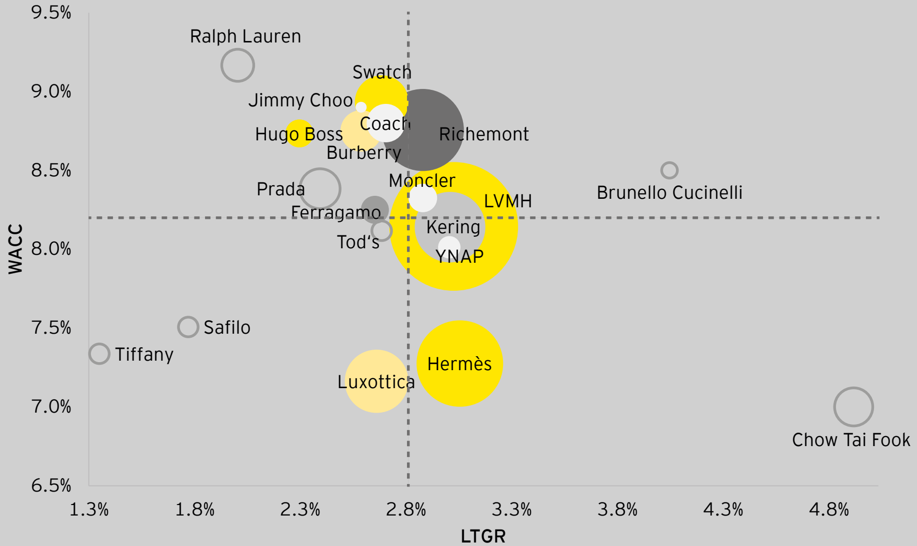
Financial parameters



A | DCF and valuation parameters

Market capitalization of almost all luxury companies has increased on average by 17% compared with last year

- Market capitalization of almost all luxury companies has increased on average by 17% compared with last year, with LMVH achieving almost €100 billion of market capitalization.
- Weighted average cost of capital (WACC) ranges from 7.0% (Chow Tai Fook) to 9.2% (Ralph Lauren), influenced particularly by geographic exposure (companies that operate principally in developed countries have, on average, lower rates) and gearing* (a higher D/E gives a premium on cost of capital and cost of debt).
- Luxury companies are on average debt free with an average indebtedness of 1.2%, almost unchanged if compared to last year.
- Long-term growth rate (LTGR) is in line with last year's figure (2.7% in 2017 compared with 2.6% in 2016), thus confirming the growth of the sector.



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

Sources:

- WACC and LTGR: based on consensus of several brokers' reports for each company.
- Market capitalization and beta: EY elaboration based on "S&P Capital IQ" data, www.capitaliq.com, 31 March 2017.
- Gearing: EY elaboration based on companies' FY2016 financial statements.

Luxury companies	Market capitalization (€m)	WACC	Gearing	Beta	LTGR
LVMH	€99,688	8.1%	4.3%	1.02	2.9%
Hermès	€44,865	7.3%	(4.9)%	0.81	2.9%
Richemont	€40,553	8.8%	(16.2)%	0.95	2.8%
Kering	€29,944	8.1%	12.5%	1.03	2.9%
Luxottica	€24,176	7.2%	5.0%	0.81	2.6%
Swatch	€17,200	8.9%	(7.4)%	1.02	2.6%
Tiffany	€10,732	7.3%	3.7%	1.04	n/a
Coach	€10,317	8.8%	(12.7)%	1.07	2.5%
Prada	€9,625	8.4%	0.5%	0.68	2.3%
Burberry	€8,862	8.8%	(11.8)%	1.19	2.6%
Chow Tai Fook	€8,795	7.0%	3.0%	0.76	4.9%
Ralph Lauren	€6,174	9.2%	(12.9)%	1.38	2.0%
Michael Kors	€5,656	n/a	(1.6)%	0.90	n/a
Moncler	€4,964	8.3%	(2.1)%	0.75	2.8%
Ferragamo	€4,703	8.3%	0.3%	0.89	2.6%
Hugo Boss	€4,636	8.7%	3.2%	0.87	2.3%
YNAP**	€3,002	8.0%	(1.3)%	0.87	2.9%
Tod's	€2,318	8.1%	2.2%	0.86	2.6%
Brunello Cucinelli	€1,463	8.5%	3.6%	0.69	3.8%
Jimmy Choo	€709	8.9%	18.4%	0.87	2.5%
Hengdeli	€684	n/a	20.2%	1.06	n/a
Safilo	€407	7.5%	16.0%	0.80	1.8%
Average		8.2%	1.0%	0.92	2.7%
Median		8.3%	1.4%	0.88	2.6%
Maximum		9.2%	20.2%	1.38	4.9%
Minimum		7.0%	(16.2)%	0.68	1.8%

**YOOX NET-A-PORTER

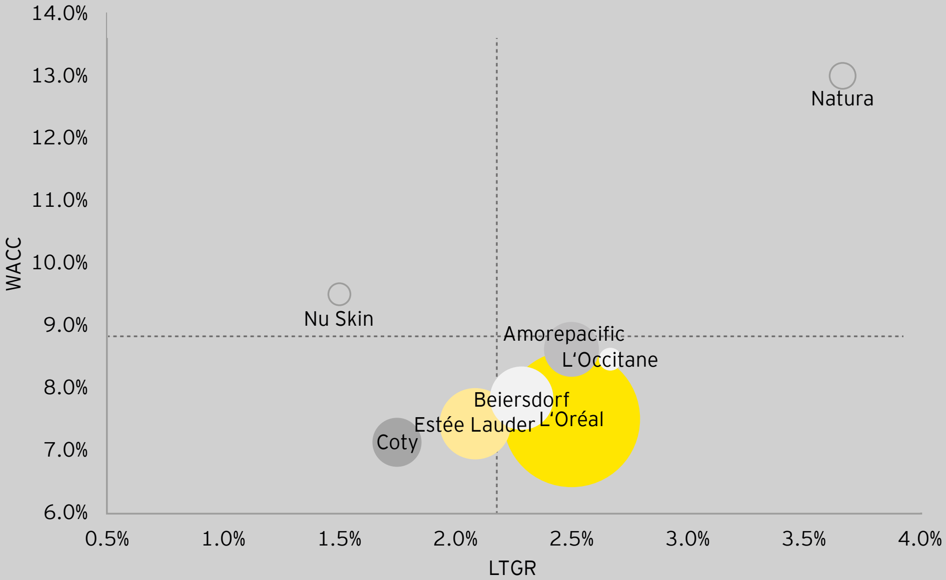
Notes:

- *Gearing is defined as the ratio between net financial position and enterprise value (EV).
- Companies are sorted in decreasing order based on the market capitalization in euros observed as of 31 March 2017 (one-month average).
- Beta corresponds to levered beta measured on a weekly basis over a two-year period.
- Data point denoted as n/a represents information not available.

A DCF and valuation parameters

Market capitalization of cosmetics companies has increased on average by 18% compared with 2016

- The average WACC is slightly higher than the luxury sample, with Natura being a clear outlier in the sample, and it also is affected by local valuation parameters.
- Cosmetics companies show an overall low average gearing of 6.8% of the market capitalization, with few exceptions.
- The average LTGR has decreased (2.4% vs. 2.9%) compared with 2016 due to a slowdown in emerging markets.



Cosmetics companies	Market Capitalization (€ m)	WACC	Gearing	Beta	LTGR
L'Oréal	€98,762	7.5%	0.2%	0.87	2.5%
Estée Lauder	€29,105	7.4%	8.1%	0.84	2.1%
Beiersdorf	€19,811	7.8%	(5.4)%	0.78	2.3%
Amorepacific	€14,872	8.6%	(2.7)%	1.41	2.5%
Coty	€13,122	7.1%	30.7%	0.75	1.8%
Shiseido	€9,914	n/a	6.7%	0.94	n/a
Natura	€3,575	13.0%	32.8%	0.95	3.7%
L'Occitane	€2,739	8.5%	(11.8)%	0.78	2.7%
Nu Skin	€2,571	9.5%	2.3%	0.66	1.5%
Average		8.7%	6.8%	0.89	2.4%
Median		8.1%	2.3%	0.84	2.4%
Maximum		13.0%	32.8%	1.41	3.7%
Minimum		7.1%	(11.8)%	0.66	1.5%

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

Sources:

- WACC and LTGR: based on consensus of several brokers' reports for each company.
- Market capitalization and beta: EY elaboration based on "S&P Capital IQ" data, www.capitaliq.com, 31 March 2017.
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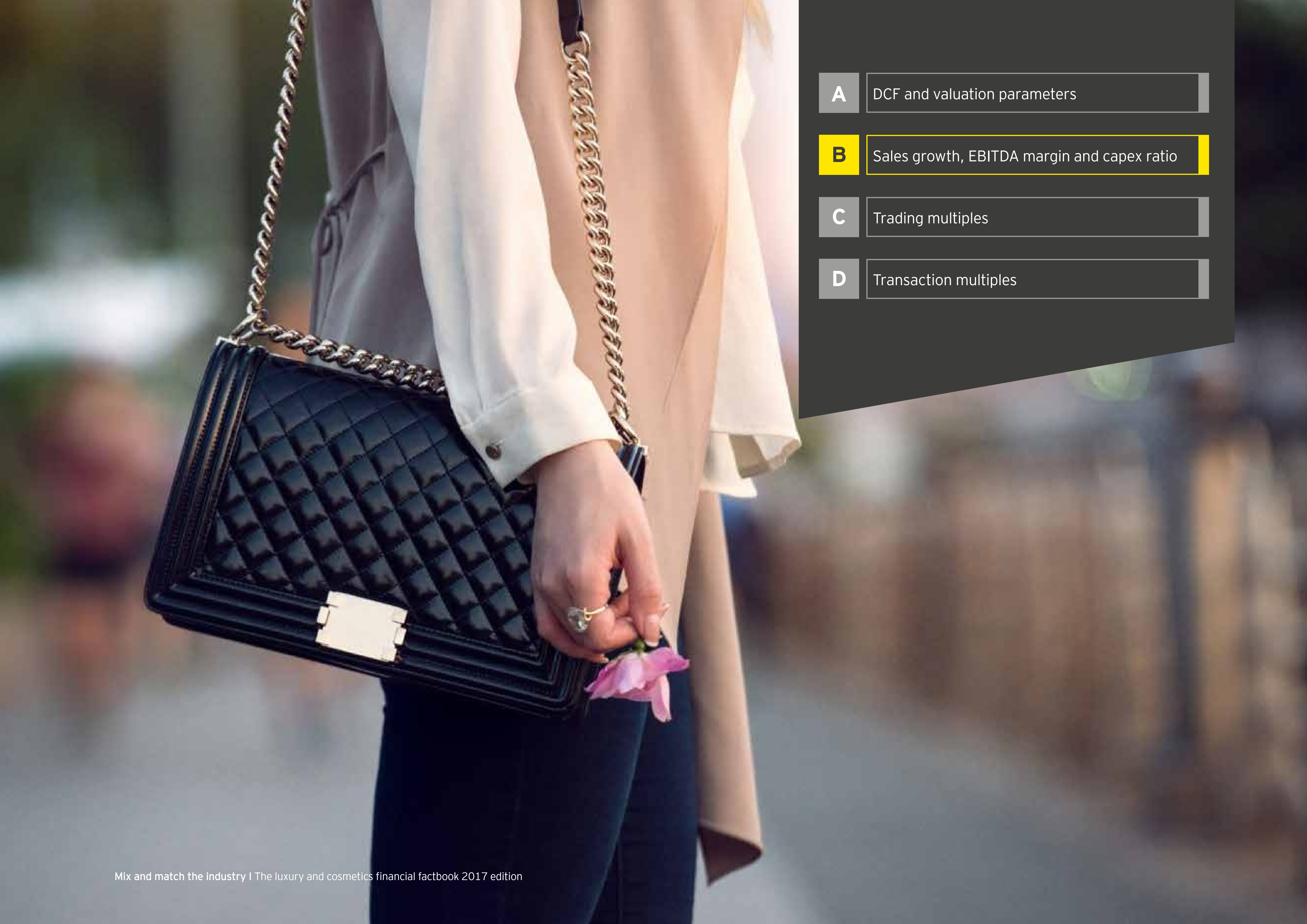
- Data point denoted as n/a represents information not available.



A DCF and valuation parameters

B Sales growth, EBITDA margin and capex ratio

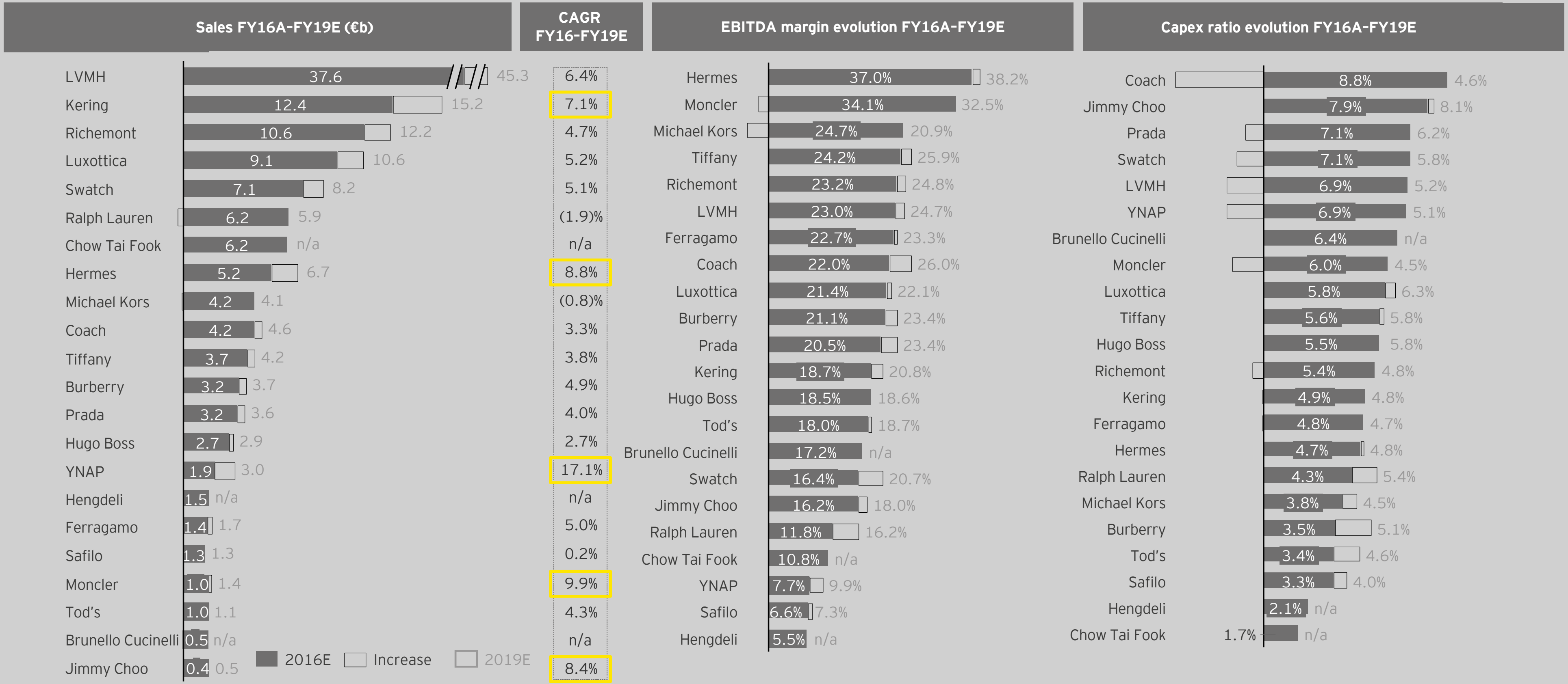
C Trading multiples

D Transaction multiples

B Sales growth, EBITDA margin and capex ratio

Emerging markets and online will drive growth in the luxury market in the next three years

- Notwithstanding the higher competition, geopolitical and macroeconomic uncertainties, and Western market saturation, the big luxury companies continue to show high expectations of growth in sales for the next three years, mainly driven by emerging markets and the growth of online channels (YNAP is No. 1 in sales growth expectations).
- Margins are also expected to be higher in 2019 than in 2016 for almost every company, with relevant increases in profitability expected for Swatch (+4.3 percentage points of EBITDA margin estimated at 20.7% in 2019) and Coach (+4.0 percentage points of EBITDA margin estimated at 26% in 2019).
- Capex ratios, on the contrary, are showing a decrease for many of the major luxury groups. Following the expansive "retail rush" in the past years and considering the need for a more integrated approach among the various distribution channels, luxury companies are changing their budget allocations with higher stakes allocated to digital.



Average CAGR FY16A-FY19E: 5.2%

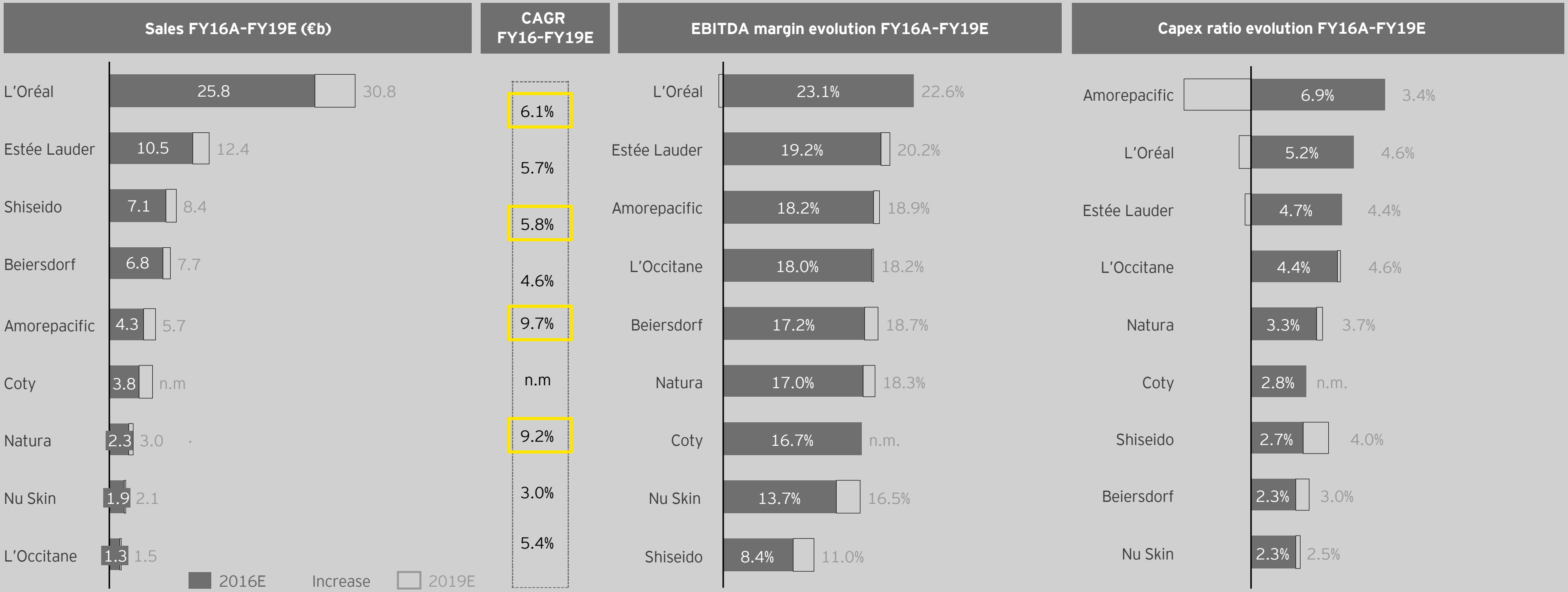
Average EBITDA margin FY16A: 19.2%

Average capex ratio FY16A: 5.3%

B Sales growth, EBITDA margin and capex ratio

Sales growth for cosmetics companies will come mostly from online sales in the next three years

- Cosmetics companies are expected to register high growth in the next three years, benefiting from the surge in online sales, and will reassess around a more realistic 2.4% in the long run.
- Margins are expected to increase in the coming years, also as a result of the positive effect of acquisitions carried out in recent years by certain top players and the accretive impact on margins of the integration of the new brands.
- Capex, on average, is stable (3.8% in 2016 and 2019E), although with different specific trends for each company. Some companies will increase capex, others will lower investments depending on each company's strategy going forward and on the brand-building efforts envisaged for future years.



Average CAGR FY16A-FY19E: 6.2%

Average EBITDA margin FY16A: 16.8%

Average capex ratio FY16A: 3.8%

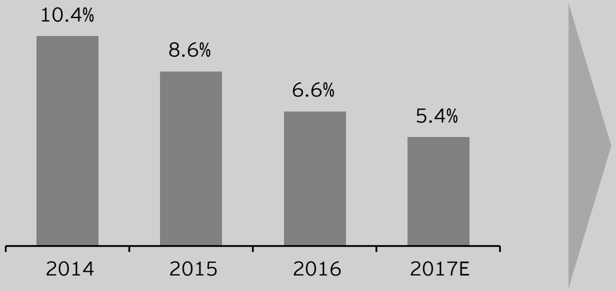
*Note: FY16-FY19E analysis for Coty is not meaningful (n.m.) due to the acquisition of the 43 Procter & Gamble brands that took place in 2016.

B Sales growth, EBITDA margin and capex ratio

A historical analysis of luxury's operating aggregates and sales growth

- After years of strong growth, sales are expected to increase at a slower pace due to a natural slowdown in the market. The global economy is recovering but luxury goods companies need to continue innovating to fuel growth. Some categories are expected to grow more than others, such as jewelry, watches, accessories and eyewear, following the consumer trend to "mix and match", which increases spending in these categories. Some uncertainty from several broker's point of view stands in the economic and geopolitical events that could influence consumer trends and, most of all, tourism flows, which are a relevant source of income for luxury companies.
- The analysis for the main KPIs (EBITDA margin, average capex ratio and average advertising examples) represents the historical effective average of these KPIs for our panel of reference.
- EBITDA margin average decreased from 21.8% in 2014 to 19.2% in 2016, with a very slight increase expected in 2017, which will be confirmed at year-end. In recent years, luxury companies heavily invested in intangibles and retail development to support growth, lowering the EBITDA margin. The capex ratio has slightly declined, partially due to the positive results in the topline derived from new store openings, but also due to the shift from brick and mortar to e-commerce, with companies slowing down traditional retail openings.

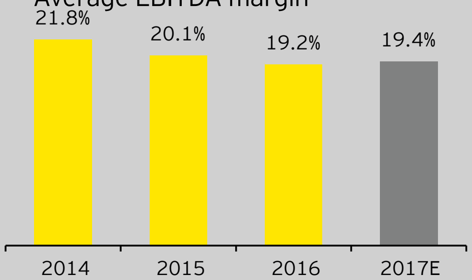
Expected average sales CAGR: a historical, forward-looking analysis



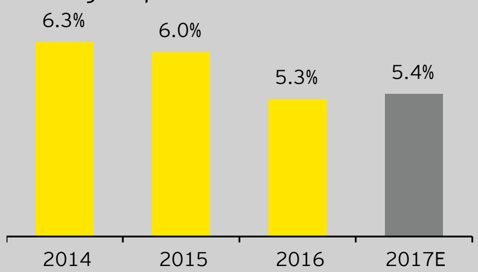
- *The analysis shows consensus for the three years after the year indicated. For example, the average sales CAGR in 2017 of 5.4% represents the consensus for sales growth in the FY17E to FY19E time frame and the average sales CAGR in 2016 of 6.6% represents the consensus for sales growth in 2016 for what at the time was the forecast for the time period from FY16E to FY18E.*
- *This analysis has been done annually for the previous four editions of the factbook (starting in 2013), allowing us to present the evolution of consensus throughout the years and provide a historical, forward-looking picture.*

Historical analysis of operating aggregates vs. 2017E

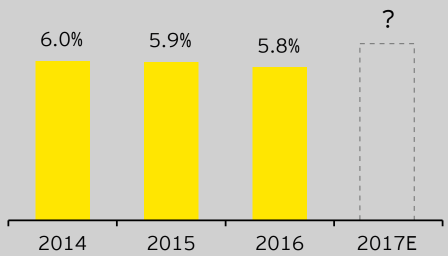
Average EBITDA margin



Average capex ratio



Average advertising expenses*



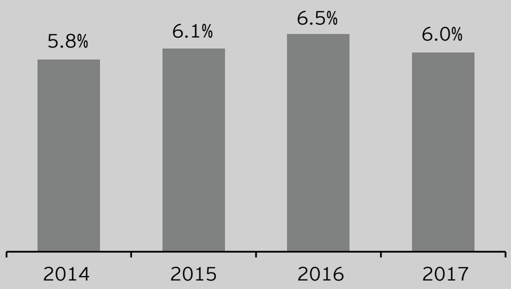
*No consensus is available for advertising expenses.

B Sales growth, EBITDA margin and capex ratio

A historical analysis of cosmetics operating aggregates and sales growth

- The cosmetics sector, on average, has increasing sales CAGR expectations driven by the rise in consumption per person (including increased use of men's skin-care products). All global beauty care players are expanding in the emerging markets of Asia-Pacific and Latin America due to rising income levels. In the coming years, an increasingly attractive channel mix will support growth through e-commerce, directly operated stores (DOS) and travel retail channels.
- The average EBITDA margin of the panel is fairly stable around 17%, slightly less than luxury companies due to the higher advertising spending and the elevated number of sales representatives needed to promote products in stores.
- The average capex ratio is less it is for luxury companies and mostly stable around 4%, given the lower investments in retail development (with almost no retail in the sector).
- The cosmetics sector is a big spender in the advertising industry. In fact, advertising expenses are well above 20% on average.

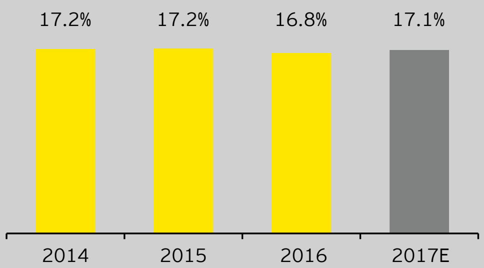
Expected average sales CAGR: a historical, forward-looking analysis



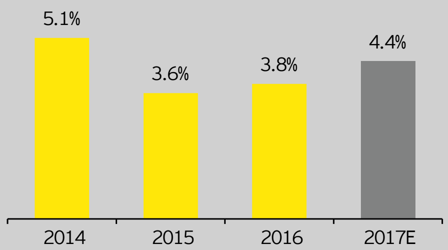
- *The analysis shows consensus for the three years after the year indicated. For example, the average sales CAGR in 2017 of 6.0% represents the consensus for sales growth in the FY17E to FY19E time frame and the average sales CAGR in 2016 of 6.5% represents the consensus for sales growth in 2016 for what at the time was FY16E to FY18E.*
- *This analysis has been done each year for the previous four editions of the factbook (starting in 2013), allowing us to present the evolution of consensus throughout the years and provide a historical, forward-looking picture.*

Historical analysis of operating aggregates vs. 2017E

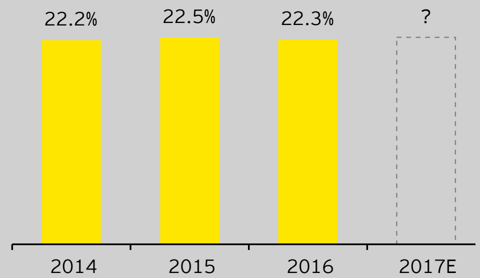
Average EBITDA margin



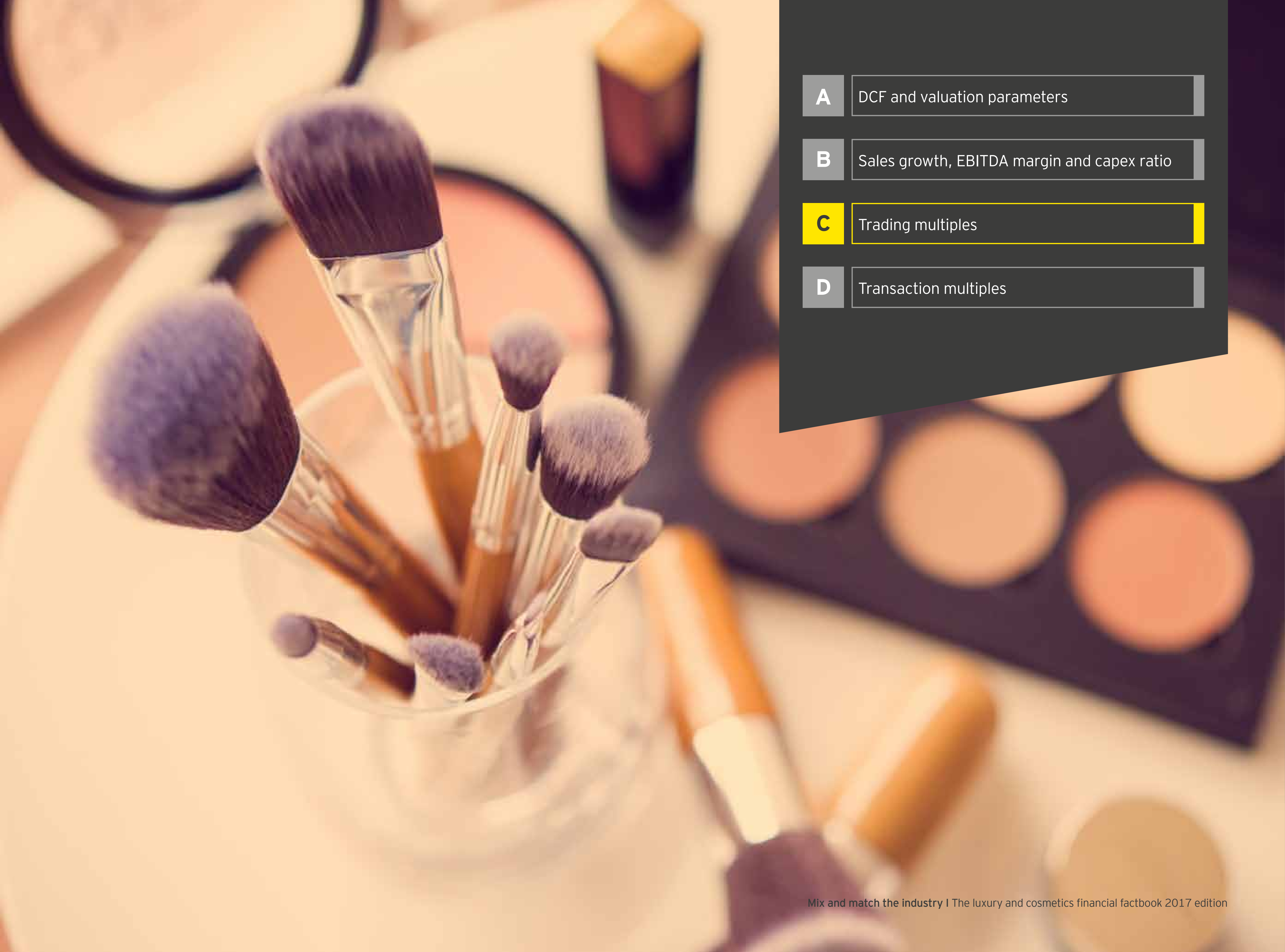
Average capex ratio



Average advertising expenses*



Note: Nu Skin is excluded from the average of advertising expenses as they were less than average due to a different business model. The advertising consensus is represented by a single asterisk above.

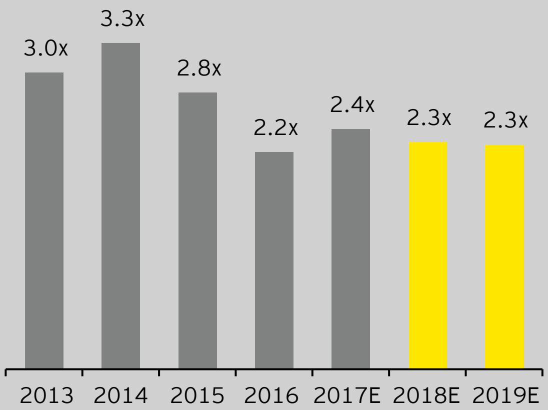


C Trading multiples

Luxury market multiples are rebounding in 2017

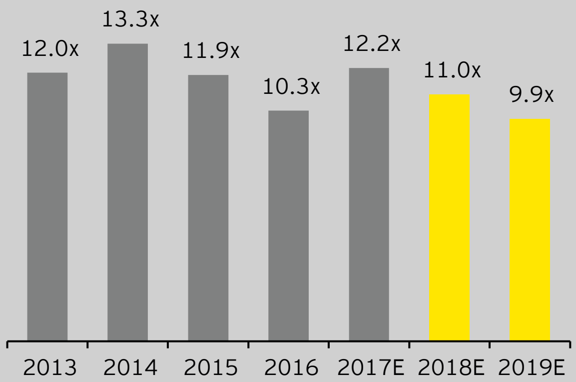
- We have analyzed the evolution of the trading multiples of luxury companies in the past editions of the factbook up to 2016, and the expected average multiples for 2017E, 2018E and 2019E.
- After the peak in FY2014, market multiples declined in the two following years, rebounding in FY17 due to bullish markets that showed higher valuations for most companies. Companies with higher expectations of growth are also the ones with the highest trading multiples, bringing up the average multiple of the panel and proving that investors are betting on the sector.
- Average multiples for the luxury sector include accessible luxury companies with a lower positioning that have on average a lower multiple. For example, the panel would have an average EV/EBITDA multiple in 2017E of 13.6x if only the high-end luxury companies were to be included, while the average multiple of the whole panel is 12.2x.

EV/sales



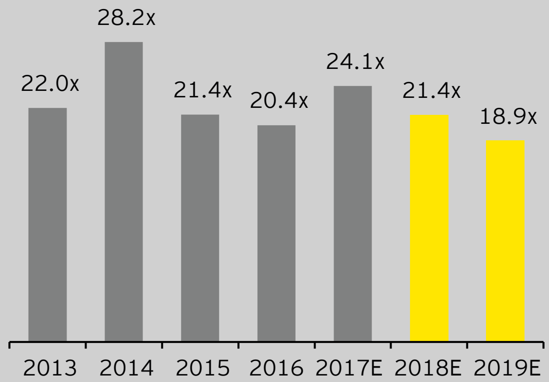
Average 2013-17E: 2.7x

EV/EBITDA



Average 2013-17E: 11.9x

Price to earnings



Average 2013-17E: 23.2x

Source: based on consensus of several brokers' reports for each company.

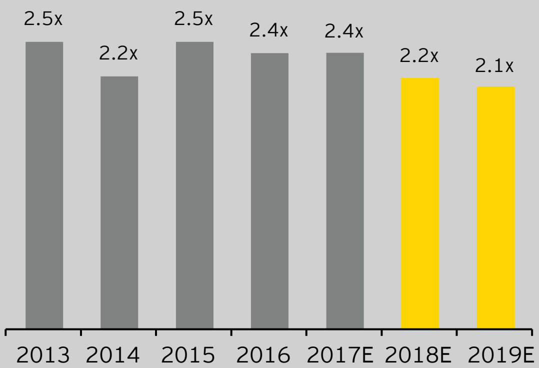
Note: Year represents the year of the factbook launch from 2013 to 2017. Each year, the multiple is calculated as the ratio between EV as of 31st of March that year and the forecast sales/EBITDA/earnings for that year. The figures for 2017-2018E and 2019E represent the forward multiple analysis for the factbook launch in 2017, and calculated as the ratio between the EV of 31 March 2017 and the sales/EBITDA/earnings expected for 2017, 2018 and 2019.

C Trading multiples

Cosmetics multiples are rebounding in 2017

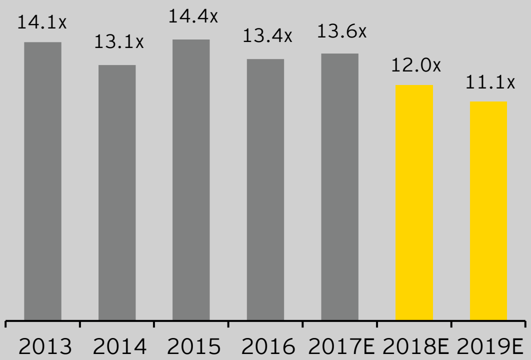
- The charts below show the evolution of the expected trading multiples of cosmetics companies over the past editions of the factbook for each year up to 2016, and the expected average multiples for 2017E, 2018E, 2019E.
- Cosmetics companies followed a different path than luxury companies with a decreasing trend in multiples from 2016 to 2017. Today the sector is becoming more attractive for investors, which see high-end cosmetics companies as highly capable of capitalizing (both organically and inorganically) on changes in consumer demand patterns, and exploiting the new channel mix. The recent boom in make-up among consumers, led by the new social beauty craze can, in fact, be further leveraged by using alternative channels such as e-commerce to reach additional consumers all around the world pushing top-line growth. These expectations are yet to be fully reflected in market valuations.

EV/sales



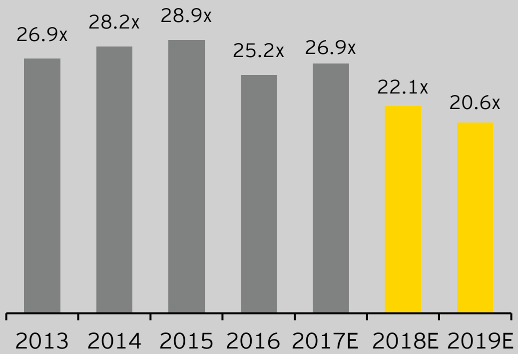
Average 2013-17E: 2.4x

EV/EBITDA



Average 2013-17E: 13.6x

Price to earnings



Average 2013-17E: 26.9x

Source: Data based on consensus of several brokers' reports for each company.

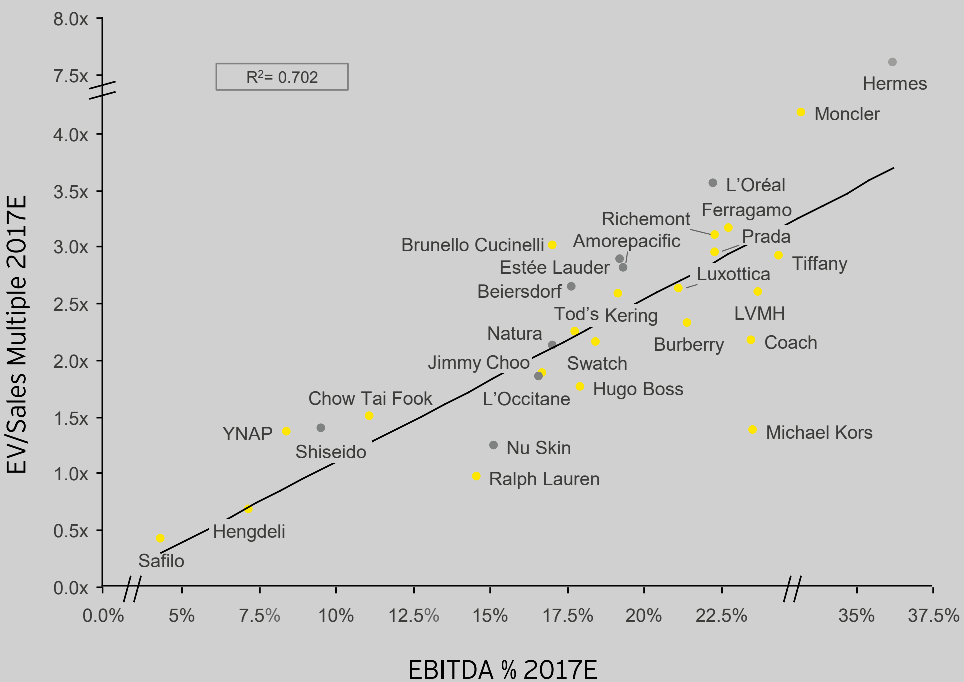
Note: Years shown represent the years the factbook has been published. Each year the multiple is calculated as the ratio between EV as of 31st of March that year and forecast sales/EBITDA/earnings for that year. 2017E-2018E and 2019E represent the forward multiple analysis for factbook launch 2017, calculated as the ratio between EV as of 31st March 2017 and sales/EBITDA/earnings expected for 2017, 2018 and 2019

C Trading multiples

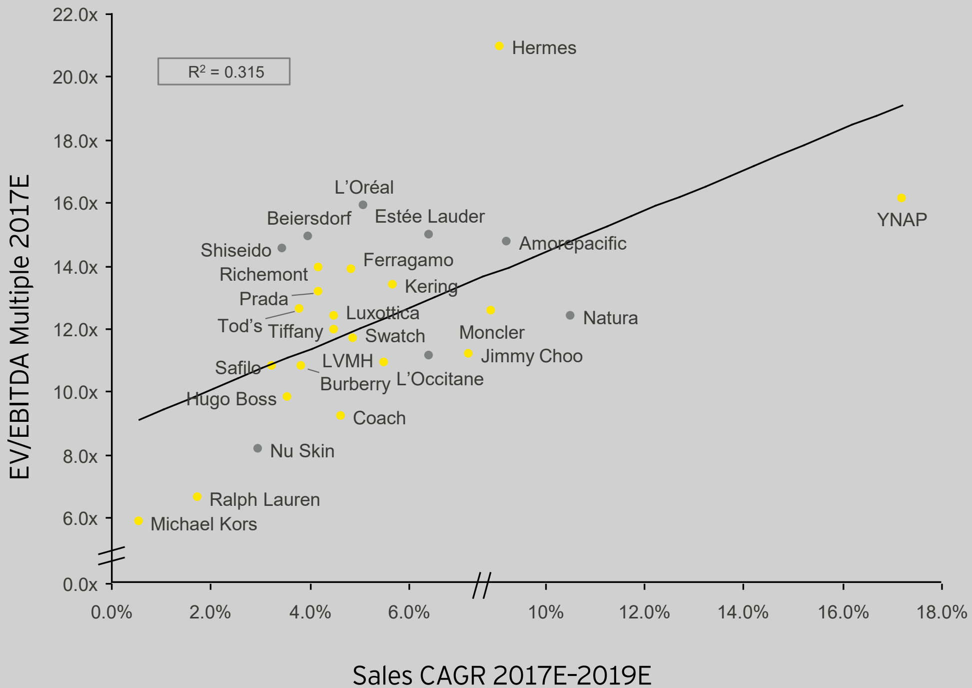
In 2017, investors appear more focused on profitability than growth

- Regression analyses show a strong correlation between EV/sales levels and profitability. High profitability levels of a luxury company are, in general, associated with the strength of the brand and its capacity to command premium prices compared with its competitors. This makes its revenues more "valuable," with a direct relevant effect on the EV/sales multiple.
- The correlation between EV/EBITDA and sales growth is less robust (and less than 2016), showing that investors seem to focus more on profitability than growth.

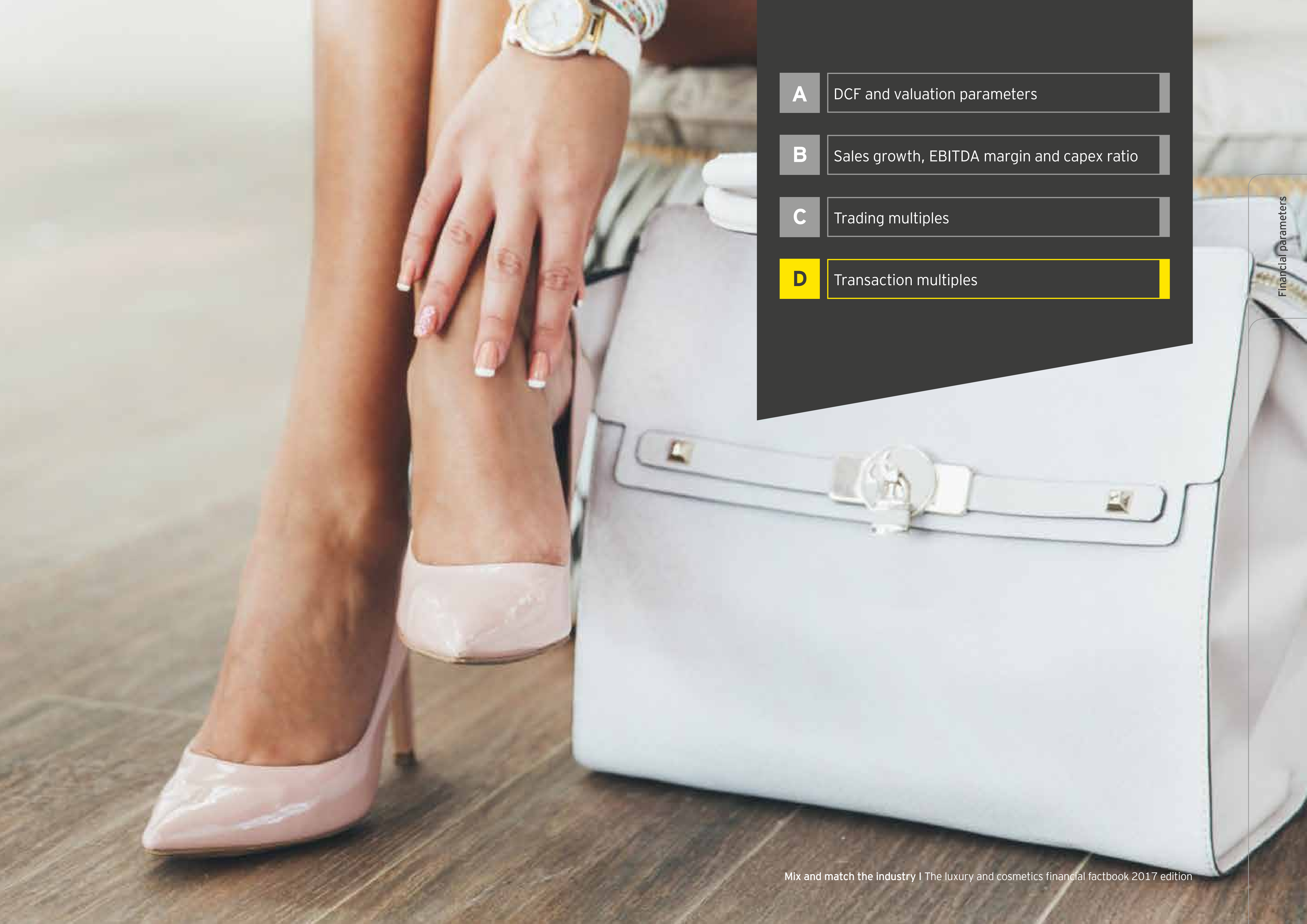
Regression analysis: EV/sales 2017E multiple vs. EBITDA margin 2017



Regression analysis: EV/EBITDA 2017E multiple vs. sales CAGR 2017E–2019E



Note: Please note that Cuccinelli, Chow Tai Fook, Hengdeli and Coty do not have consensus available for sales 2019E and are therefore not representet in the regression analysis between EV/EBITDA 17E and sales CAGR 2017-2019E.



D Transaction multiples

Apparel and cosmetics were the hottest sectors in 2016, with investors attracted by the growth potential of digital and accessible luxury, which is currently driving consumer spending

Deal count: 2015 vs. 2016 by target sector

Selected global 2015–16 transactions

- Armonia/Aspesi
- Shangdong Ruyi/Groupe SMCP
- Investcorp/Corneliani
- Mayhoola/Balmain SA
- L Capital/Pepe Jeans

- CVC/Douglas Holding
- Coty/43 P&G Brands
- Capvis/Gotha Cosmetics
- Revlon/Elizabeth Arden
- Coty/GHD Hair

- D'leteren/Moleskine
- Carlyle/Golden Goose
- Samsonite/Tumi
- Coach/Stuart Weitzman
- Gangtai/Buccellati
- Onward Luxury Group/Moreau-Paris

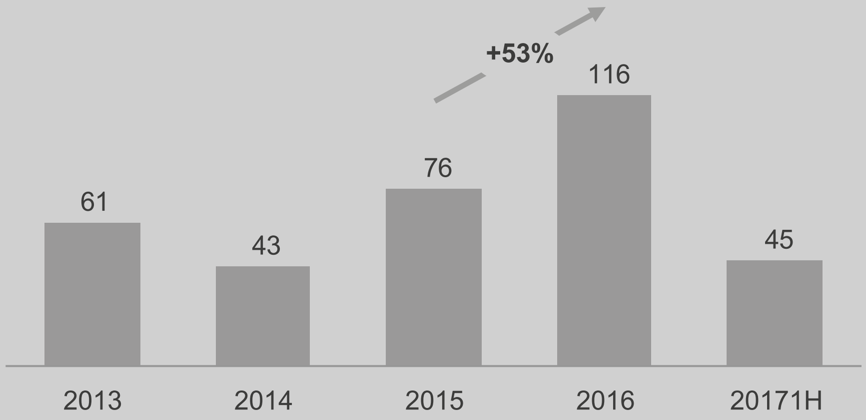
- Vente-Privee.com/Privalia Venta Directa
- YOOX/NET-A-PORTER Group
- Shisheido/ Match & Co.
- Coty/Younique

Note: please note that Armonia/Aspesi means that Armonia acquired Aspesi. This is true for all the 2015-16 transactions highlighted on the right.

D Transaction multiples

Luxury M&A arena has been very active in recent years and there are many promising opportunities in companies "born digital" and small accessible luxury brands with a high growth potential

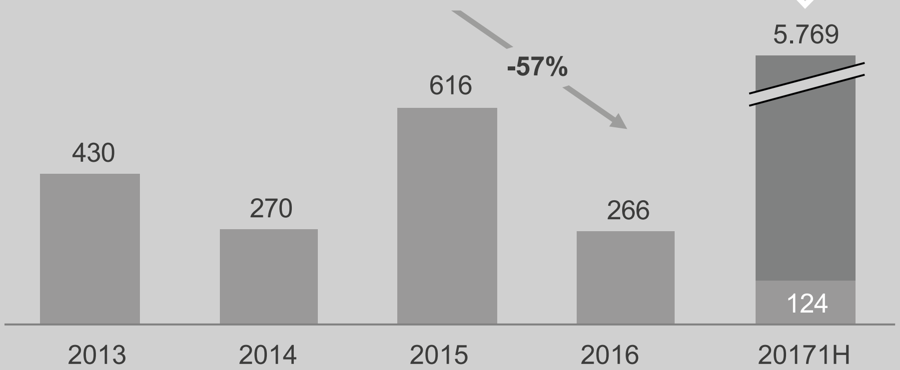
Number of completed deals



- It was a very active year in 2016 in terms of the number of transactions, with 53% more compared with 2015, reflecting investor expectations of the potential in the luxury market. It is expected to grow in future years and is driven still (mostly) by spending in emerging countries.
- The interest has been for middle-market companies, as this segment is the fastest growing, together with accessories.

Average deal size (€m)

The average deal size is €124m without the three jumbo transactions (acquisition of minority of Christian Dior, merger of Essilor – Luxottica, and the acquisition of a minority of Burberry)

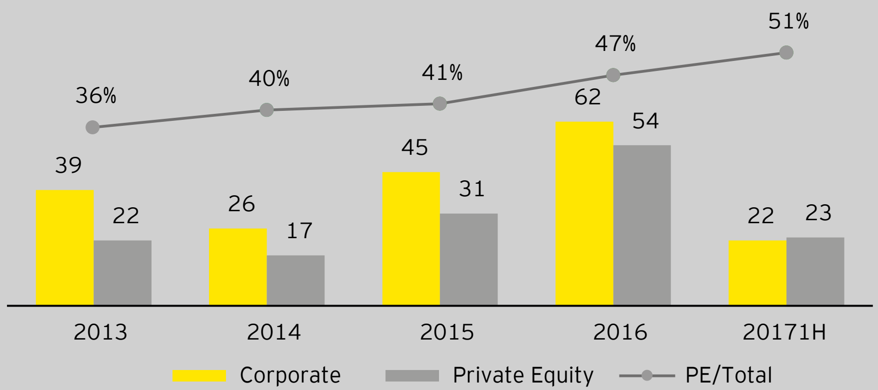


- The average deal size reflects the fact that 2015 was an exceptional year for large-scale transactions, with higher-than-average multiples due to the high-end positioning of the acquired companies, such as YOOX and NET-A-PORTER Group, Hugo Boss by Zignago Holding, Pepe Jeans by L Capital and Stuart Weitzman by Coach, just to name a few.
- 2016 was characterized by many transactions with several targets of a smaller size and lower positioning, showing interest by private equity funds in middle-market companies. Some relevant large-scale transactions in 2016 had undisclosed deal details, so the average deal size is slightly biased.
- In 2017, the year began with the jumbo deal between Essilor and Luxottica; the acquisition by Bernard Arnault (LVMH) of the outstanding shares of Christian Dior (minority); and the acquisition of 3% of Burberry Group by Groupe Bruxelles Lambert SA, which skews the average deal size (the graph on the left shows the average deal size with and without these deals).

D Transaction multiples

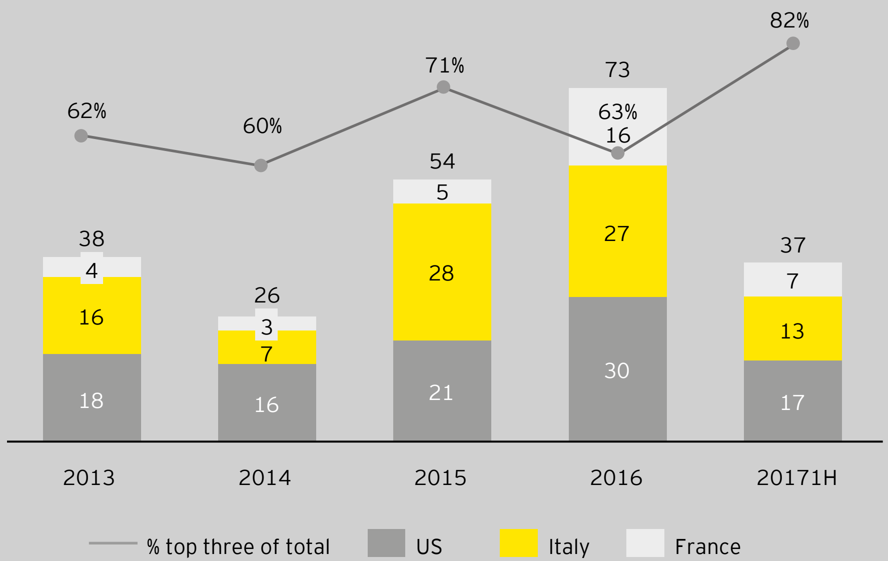
PE activity picking up in 2016

Number of completed deals by type of buyer



- Private equity activity in the sector has increased significantly in the past years, reaching 47% of the total activity in 2016, fueled by dry powder of funds and credit availability.
- The luxury sector has always been of interest for financial investors given the high growth potential and profitability. Valentino and Versace are clear examples.
- Currently, private equity funds are showing interest in the premium and entry-to-luxury brands, which are expected to outpace the growth in luxury brands in coming years.

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



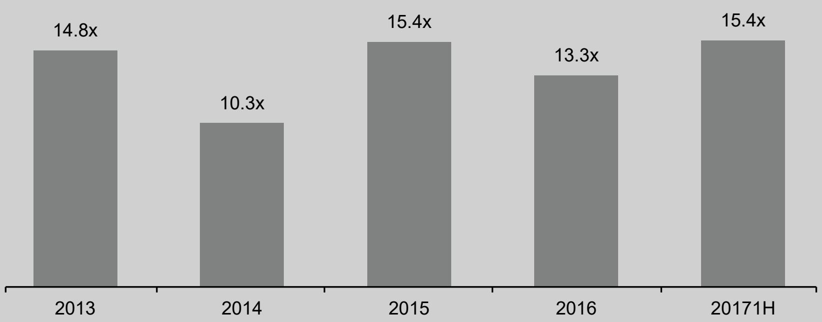
- Italy, the US and France remain the top countries attracting the interest of buyers in the fashion and luxury arena.
- This is partially linked to the fact that these countries also lead in terms of the total value of the luxury market.
- While the US is the largest Western market, France owns the most known global luxury brands through its major luxury groups. Italy, in addition to having major luxury brands, is the place where new companies and brands appear on the international markets, backed by strong product and craftsmanship capabilities.

D Transaction multiples

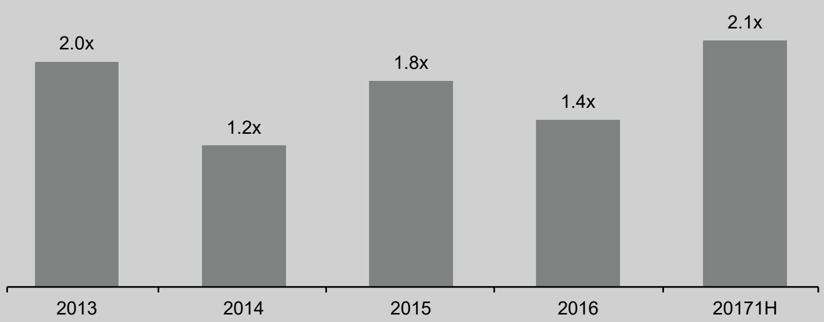
High-end luxury companies still attract the highest valuations

- M&A multiples in 2016 were slightly lower compared with the previous years, which is partially explained by the fact that 2015 was an exceptional year with some major transactions (YOOX NET-A-PORTER GROUP, Roberto Cavalli, Pepe Jeans and Hugo Boss) that led both to a high average deal value and to higher average multiples.
- 2016 was characterized by some lower valuations, driven mainly by transactions in which fashion houses divested the less-profitable brands to focus on the core business. At the same time, 2016 was a good year for M&A, with major transactions characterizing the arena, driven by the big luxury groups that had not been investing for a couple of years (G-III apparel, which acquired Donna Karan and Karl Lagerfeld; PVH Corp., which, acquired TH Asia; Mayhoola, which acquired Balmain and the remaining stake of Pal Zileri; LVMH, which acquired Rimowa).

EV/EBITDA (FY13–171H)



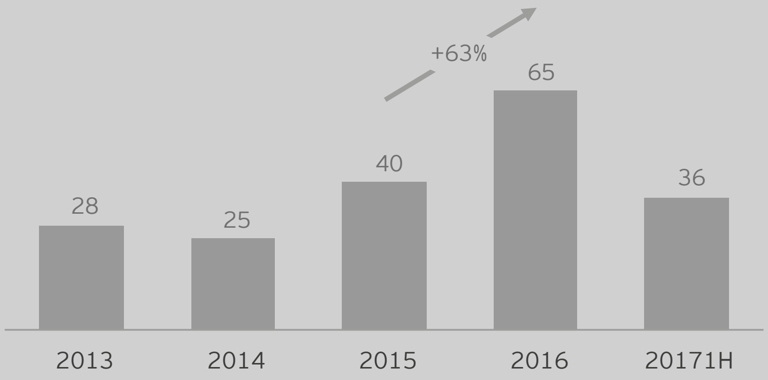
EV/sales (FY13–171H)



D Transaction multiples

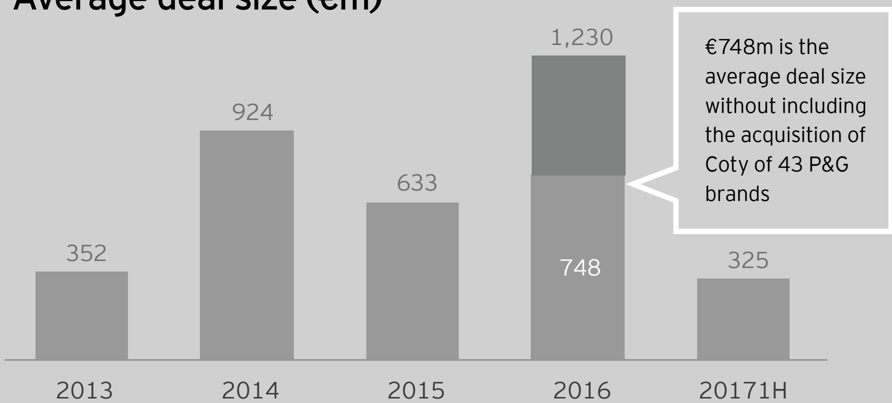
Cosmetics was the most active sector, together with apparel, in 2016, with 65 transactions proving investors' expectations of the growth potential of the product category

Number of completed deals



- The cosmetics industry was the most active in 2016 in terms of transactions in 2016 with 65 transactions compared with the 40 transactions in 2015.
- The cosmetics industry is polarized, with the first three companies (L'Oreal, Unilever and P&G) representing more than 30% of the global market characteristic that is driving M&A in this segment. As a matter of fact, investors are mainly strategic players looking to further consolidate by acquiring companies in high-potential segments (skin care, fragrances and make-up with a particular interest in customized, natural and innovative products, which are the most targeted products by consumers. Strategic players have completed transactions based on products, the level of innovation, opening new markets and distribution channels.
- Consumption is driven by emerging markets and online sales (11% of total selective cosmetics) and digital is, therefore, the main challenge going forward.

Average deal size (€m)

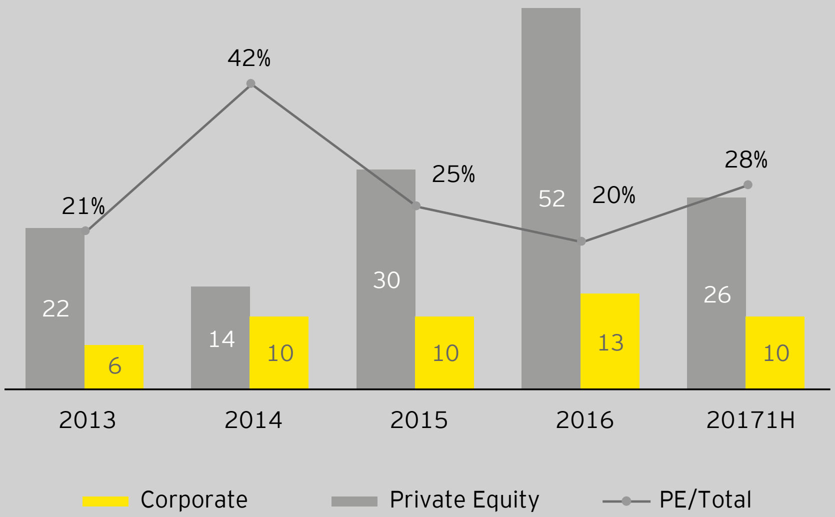


- The average deal size is fairly stable, with the megadeal in 2016 represented by the acquisition by Coty of 43 P&G brands, skewing the average.
- The average deal size in cosmetics transactions is very polarized, with many microtransactions (less than €50m in EV) and some large transactions in which the buyer is usually a large multinational company (L'Oréal, Estée Lauder and Johnson & Johnson) or a large private equity fund acquiring large cosmetics companies, such as Investindustrial which acquired Artsana, Cerberus Capital Management which acquired Avon and CVC which acquired Douglas.

D Transaction multiples

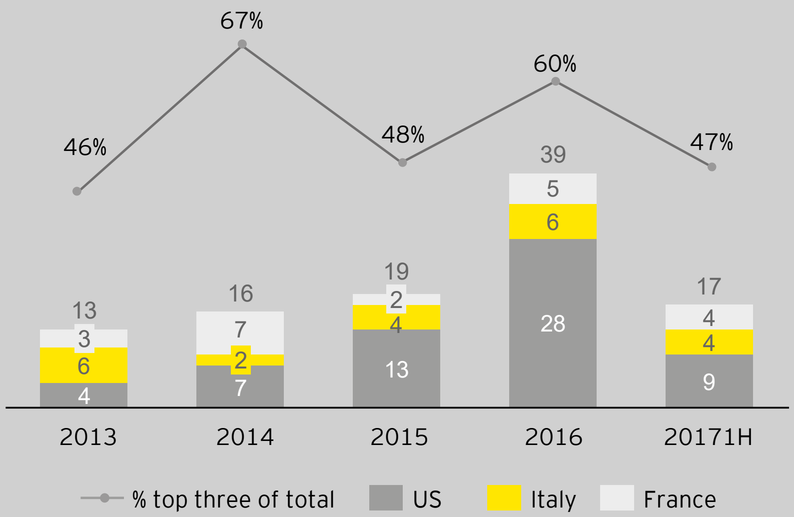
Trade buyers still remain the tier 1 acquirers for cosmetics companies, continuing consolidation in the industry

Number of completed deals by type of buyer



- Leading cosmetics companies have been acquiring small, innovative companies and larger companies to continue consolidation in the industry.
- Cosmetics have become very attractive for private equity funds, which are chasing niche opportunities to help companies with their growth strategy. PE intervention will allow small companies to become sufficiently sizable and thus be more attractive to the big cosmetics conglomerates at the moment of the PE's exit.
- There is a high potential for digital companies in the cosmetics arena as this, at the moment, is a fairly unexplored area. Some transactions in e-commerce have been, in fact, tracked in 2016 (for example the acquisition of Match & Co. from Shiseido and the acquisition of Younique by Coty).

Number of completed deals sorted by top three geographies of the target



- The US, Italy and France, again, lead as the countries with the largest part of the M&A activity in the industry.
- However, the M&A activity is less polarized as the three major countries, depending on the year, historically accounted for between 46% and 67% of the transactions in the industry. Other relevant countries in the M&A market include the UK and Germany.

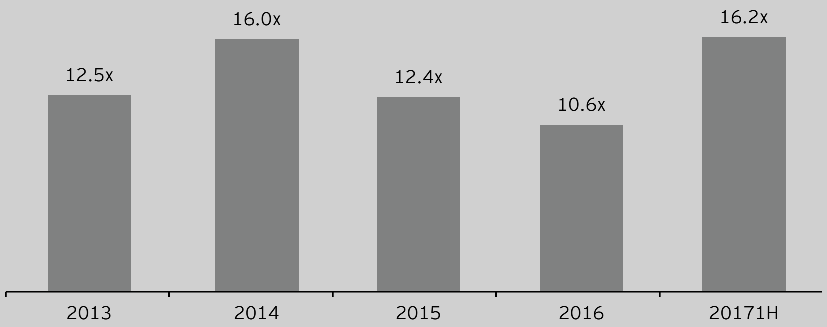
Financial parameters

D Transaction multiples

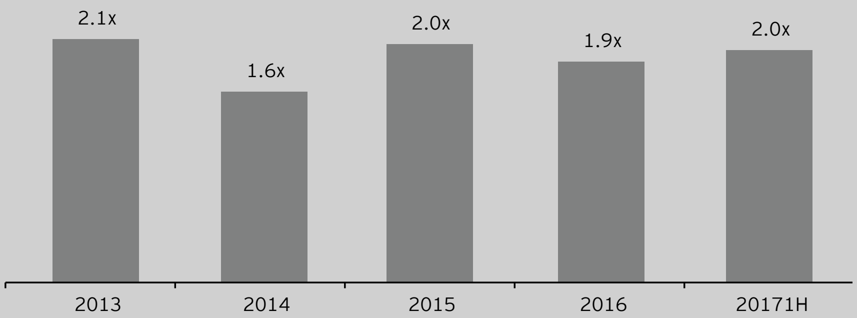
Transaction multiples in the cosmetics industry are peaking, with high valuations for companies with high-end positioning if acquired by large cosmetics groups

- M&A multiples are, on average, lower than market multiples given the lower size of the acquired companies, but show higher variance over the years.
- In the industry, there are a number of drivers that lead to M&A, where large cosmetic and personal care corporations make the rules of the acquisition game: research new products, enter new markets and distribution channels (including digital and direct to consumer (DTC)), offer innovative and high-tech products.
- Apart from the jumbo deal in 2016 represented by Coty's acquisition of 43 Procter&Gamble brands that accounted for €11.3b worth of deal value, the remaining deals were fairly small and with lower valuations.

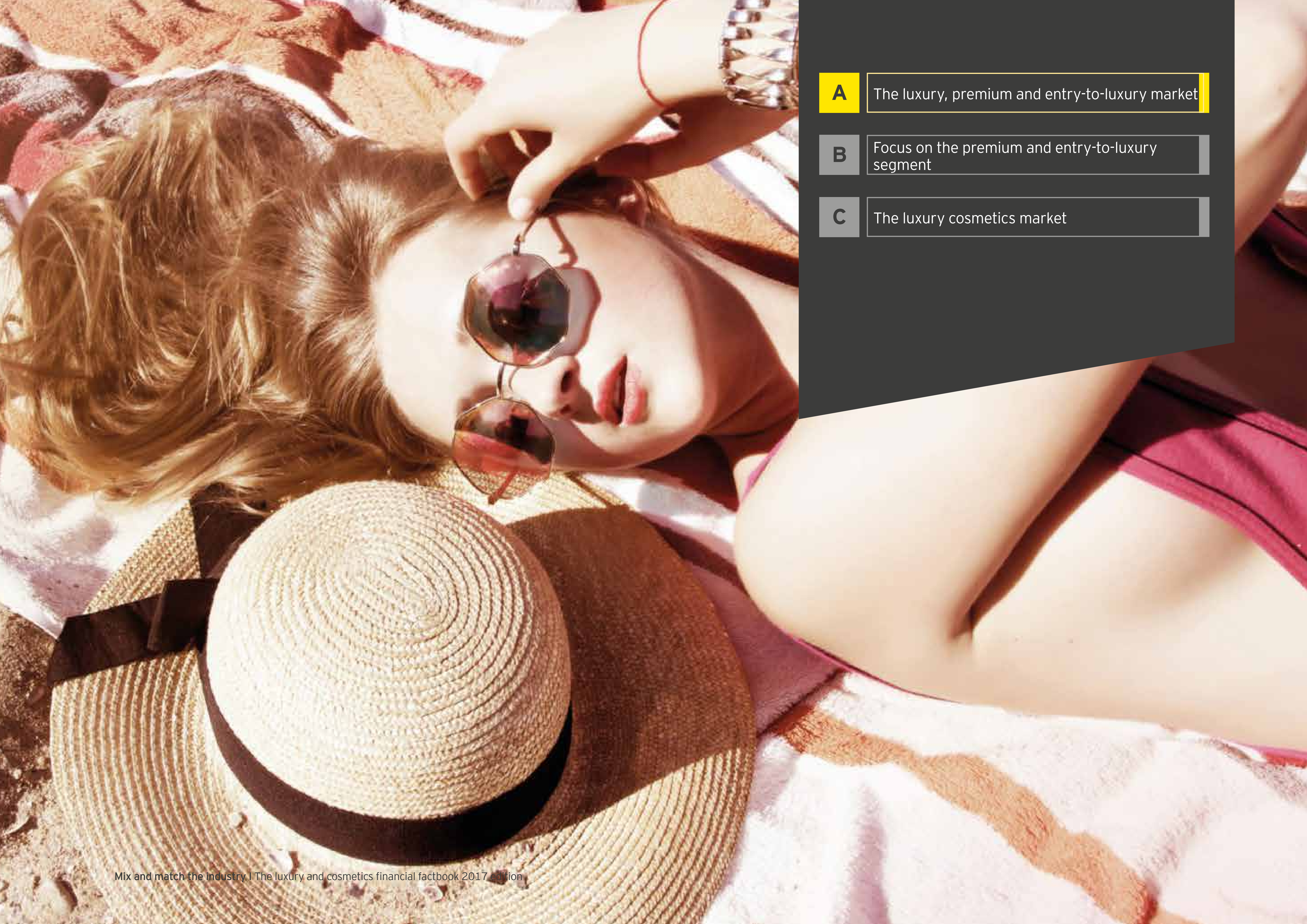
EV/EBITDA (FY13–171H)



EV/sales (FY13–171H)

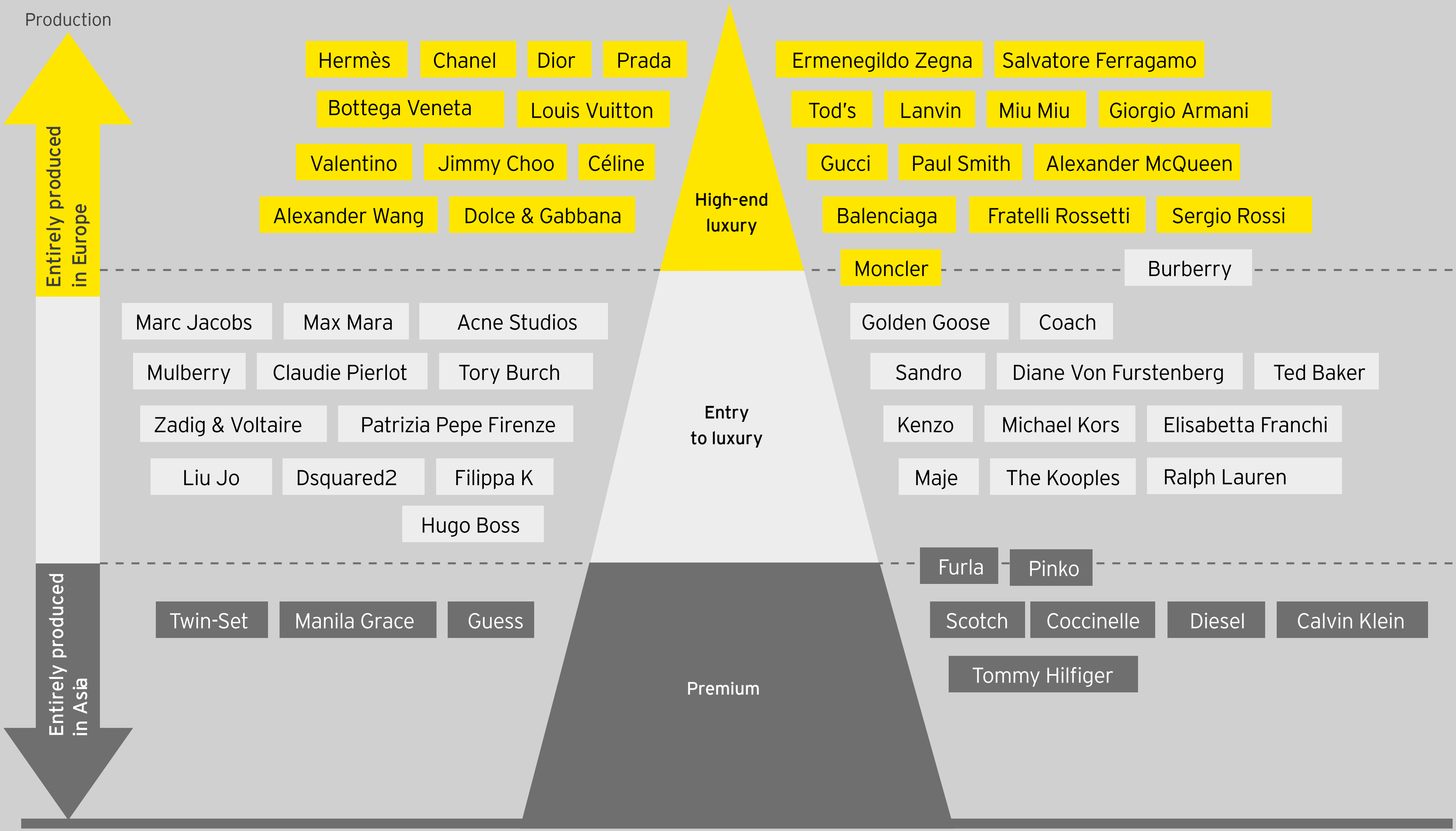


Industry overview



A The luxury, premium and entry-to-luxury market

Entry-to-luxury segment has become more crowded in recent years, with many brands representing success stories

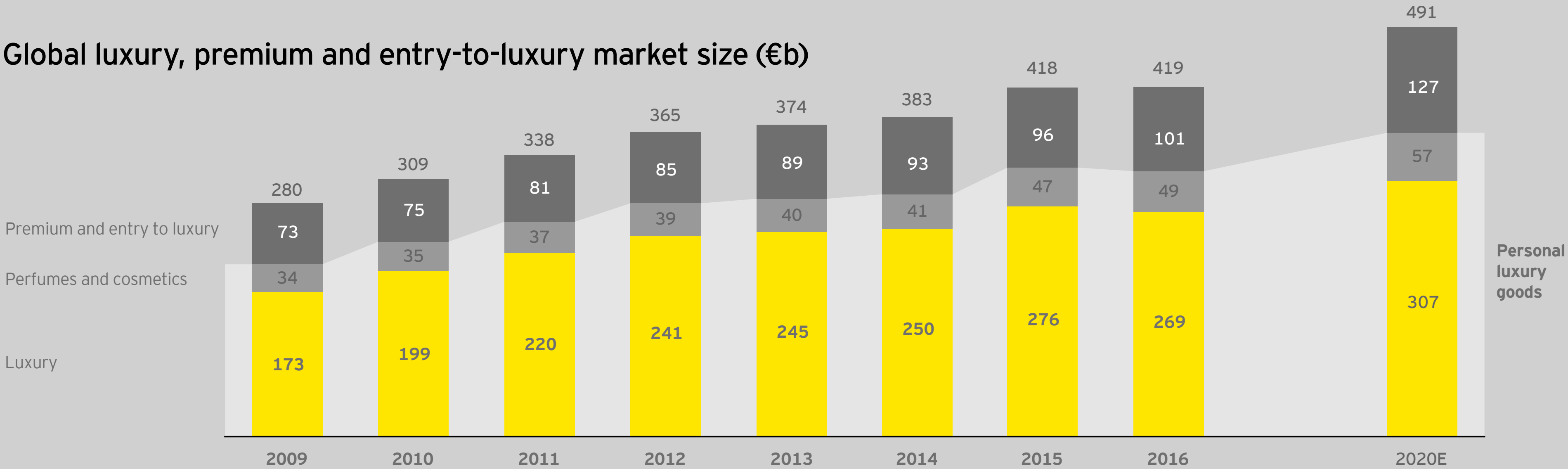


A The luxury, premium and entry-to-luxury market

While luxury drove growth in the past, premium and entry-to-luxury segments have the highest potential in coming years with an expected compound annual growth rate (CAGR) of 6%

Global luxury, premium and entry-to-luxury market growth (%)

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



Source: EY analysis of Fondazione Altagamma data.
[*] E: Expected

A The luxury, premium and entry-to-luxury market

Accessories are driving growth in both luxury and premium segment, with luxury shoes remaining market-leading category

	Luxury		Premium and entry-to-luxury	
	2016	2020E	2016	2020E
Shoes	€16b +7% CAGR	€24b +11% CAGR	€18b +6% CAGR	€23b +7% CAGR
Accessories	€63b +8% CAGR	€79b +6% CAGR	€10b +10% CAGR	€13b +6% CAGR
Watches & Jewelry	€124b +4% CAGR	€121b -1% CAGR	€15b +7% CAGR	€18b +5% CAGR
Apparel	€66b +4% CAGR	€83b +6% CAGR	€58b +4% CAGR	€73b +6% CAGR

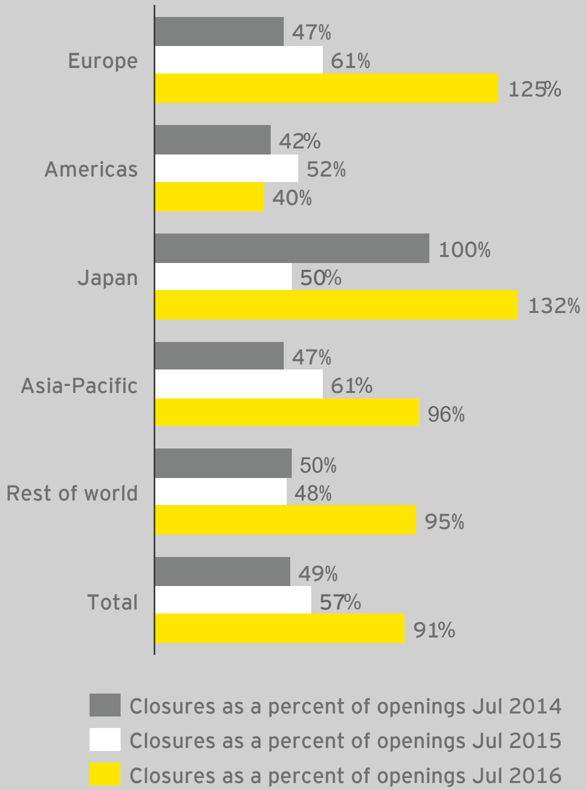
2016 CAGR: The CAGR is calculated for the period between 2010 and 2016.
2020 CAGR: The CAGR is calculated for the period between 2016 and 2020E.

Source: EY analysis of Fondazione Altagamma data.

A The luxury, premium and entry-to-luxury market

Why is luxury slowing down?

A From one closure for every two openings to one closure for every opening



B Retail struggles to deliver strong like-for-like performance

In-store traffic

Stable conversion

Price increase

Units per transaction (UPT)

Rent increase

C Consumers more sophisticated

From total look approach to selectiveness on **heritage-branded products** per product category.

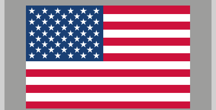
Digital transparence shows **60%** of consumers are digitally influenced.

Globe-trotting luxury consumers.

Source: EY analysis of Fondazione Altagamma data and Bernstein data.

A The luxury, premium and entry-to-luxury market

China is the fastest-growing country for luxury goods, despite a recent slowdown

	Luxury		Premium and entry-to-luxury	
	2016	2020E	2016	2020E
	€23b +13% CAGR	€26b +3% CAGR	€8b +10% CAGR	€10b +7% CAGR
	€105b +11% CAGR	€124b +3% CAGR	€26b +7% CAGR	€32b +6% CAGR
	€76b +4% CAGR	€87b +2% CAGR	€33b +1% CAGR	€38b +3% CAGR
	€114b +4% CAGR	€127b +2% CAGR	€34b +7% CAGR	€47b +8% CAGR

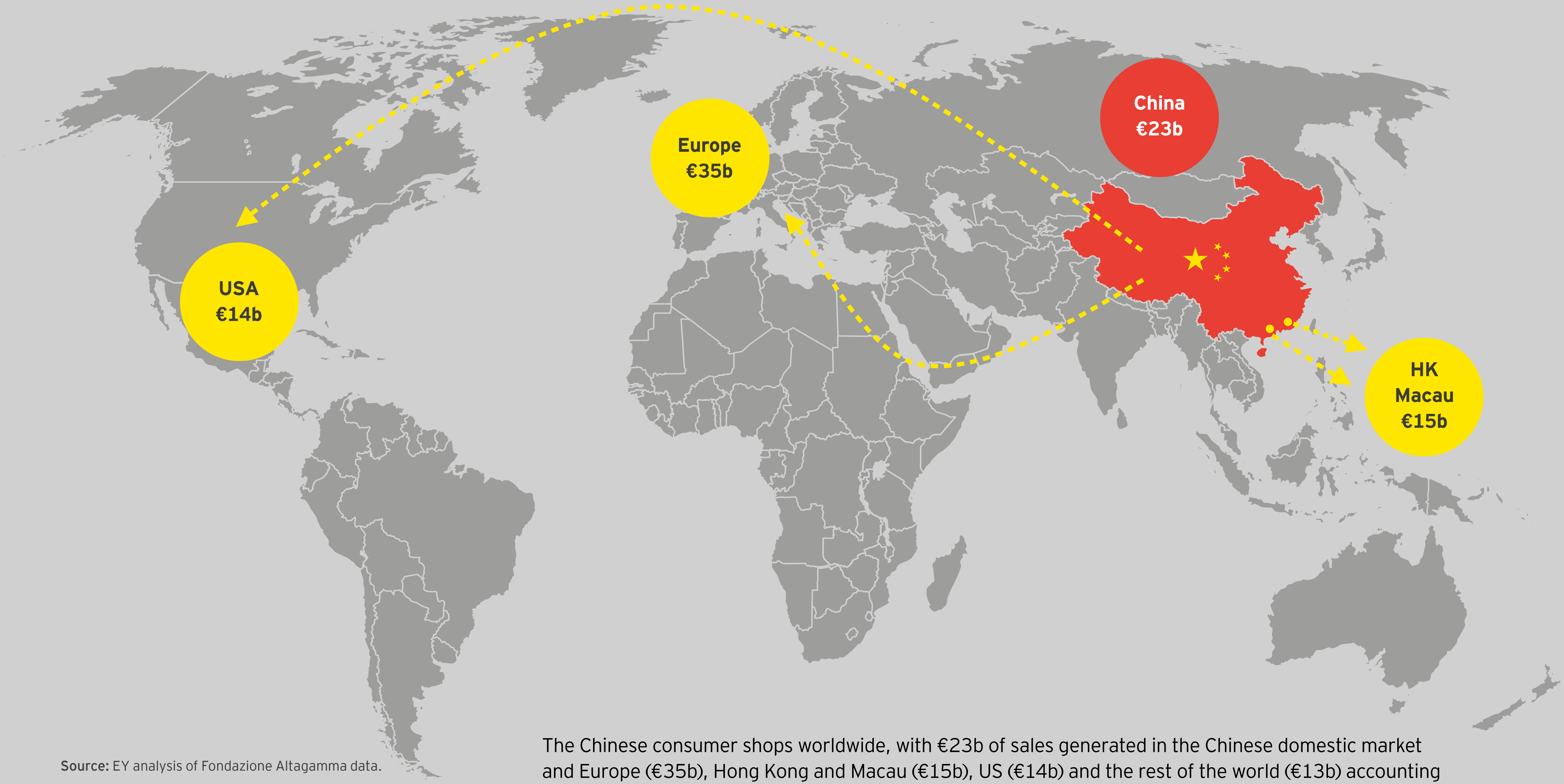
Luxury figures include luxury cosmetics (2016: €49b).

2016 CAGR: The CAGR is calculated for the period between 2010 and 2016.
2020 CAGR: The CAGR is calculated for the period between 2016 and 2020E.

Source: EY analysis of Fondazione Altagamma data.

A The luxury, premium and entry-to-luxury market

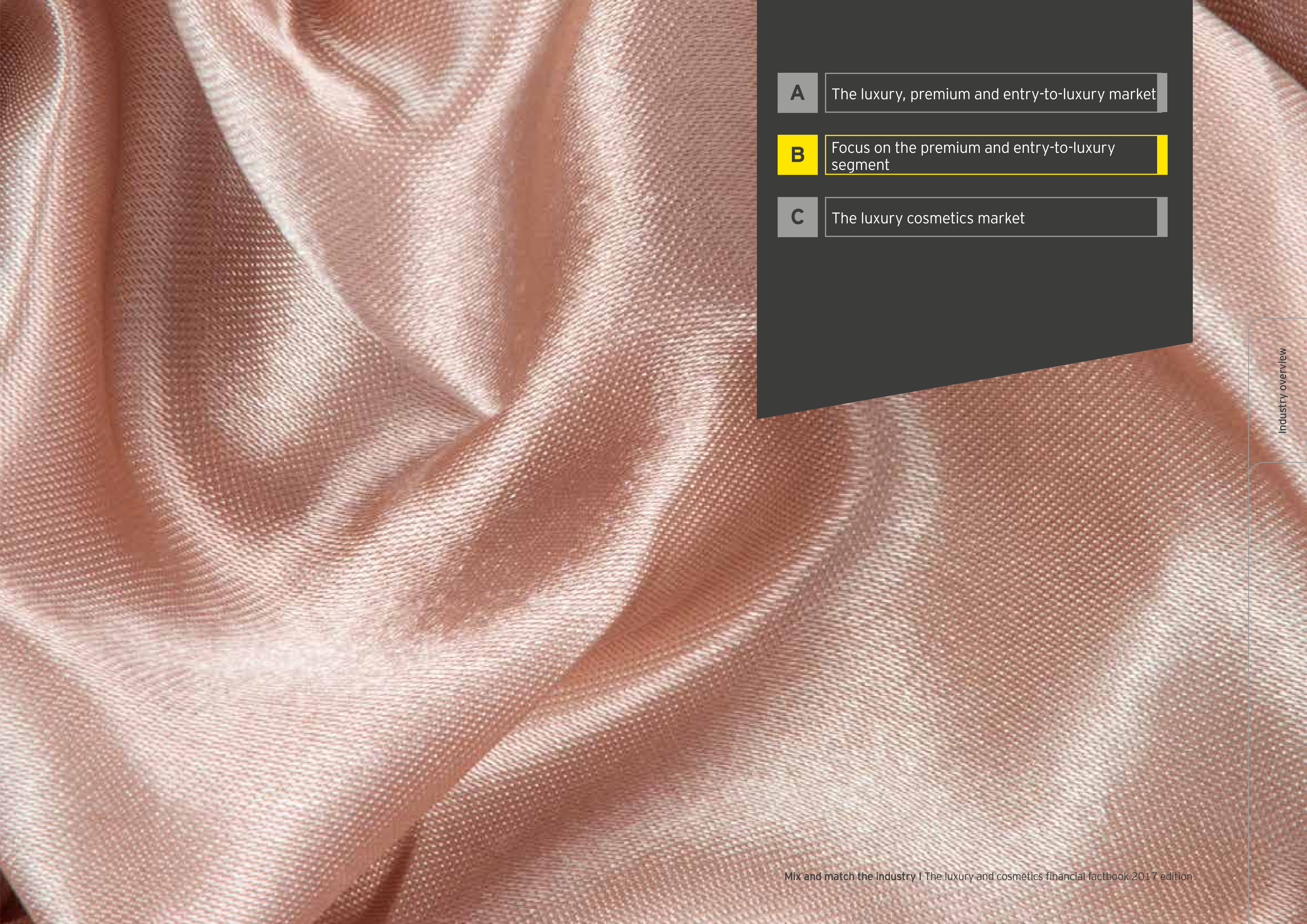
The Chinese consumer accounts for more than €100b sales across the globe, with Europe, Hong Kong, Macau and US as top-four shopping destinations



Source: EY analysis of Fondazione Altagamma data.

Note: Figures include luxury cosmetics market value (€49b).

The Chinese consumer shops worldwide, with €23b of sales generated in the Chinese domestic market and Europe (€35b), Hong Kong and Macau (€15b), US (€14b) and the rest of the world (€13b) accounting for the remainder.



B Focus on the premium and entry-to-luxury segment

Globally, millennials are savvy consumers with common purchasing drivers and behaviour, regardless of geographic barriers

Why are millennials going to drive growth in the premium and entry-to-luxury segment?

Aspirations

Millennial luxury consumers do not have the same aspirations and values as their predecessors and, thus, reject the traditional status quo.

80% of millennials have different top-three ethical values compared with baby boomers.

Style

Casual wear is becoming the choice, even for traditionally more formal occasions.

75% of millennials perceive a decrease in the appeal of formal wear in favor of casual wear.

Value

Millennials have a strong perception that price doesn't reflect the true value of many high-end luxury products purchased and they seek to pay for true tangible quality.

55% of millennials perceive a misalignment between the price paid and the product acquired.

Digital

Millennials are more informed and savvy in their choices compared with previous luxury consumers and digital influence plays an important role in their purchasing behavior.

68% of purchases by millennials are digitally influenced.

Source: EY analysis of Fondazione Altagamma data.

B Focus on the premium and entry-to-luxury segment

Premium and entry-to-luxury acceleration boosted by five macro trends

1	Rising urban middle class	**Urban middle class population expected to increase by 1.1b within next 15 years, reaching 5.1b by 2030** The developing countries are leading the main growth in the urban population, with China and India playing a leading role. China is expected to grow circa 220m and India circa 160m within the next 15 years, with a 35% increase in their urban populations.
2	Price increase in luxury products	**Steep incline in luxury price index (circa 3.0x from 2010 to 2016)** An increase in the price range of luxury products drives the luxury brand to be positioned for ultra-rich individuals.
3	Mix and match	**Increase in apparel purchases driven by value per occasion, results in consumers mixing brands in different price ranges** Luxury apparel with a high per-wear cost leads consumers to mix clothes and accessories from premium and mass brands.
4	Trading down	**Traditional luxury consumers increasingly opening portfolios to premium and fast fashion** Forty-one percent of luxury and entry-to-luxury consumers also purchase premium luxury products, especially accessories and fast-fashion products.
5	Casualization	**Changing fashion trends, booming "*sneakerization*"** "*Sneakerization,*" the wave of casual sports footwear has impacted luxury brands and, in particular, the shoe category. Following the boom, the sneaker market increased its value to €3b, with a market coverage of 19% of the total shoe segment.

Source: EY analysis of Fondazione Altagamma data.

1 Rising urban middle class

Urban population is expected to increase 1.1b in 15 years

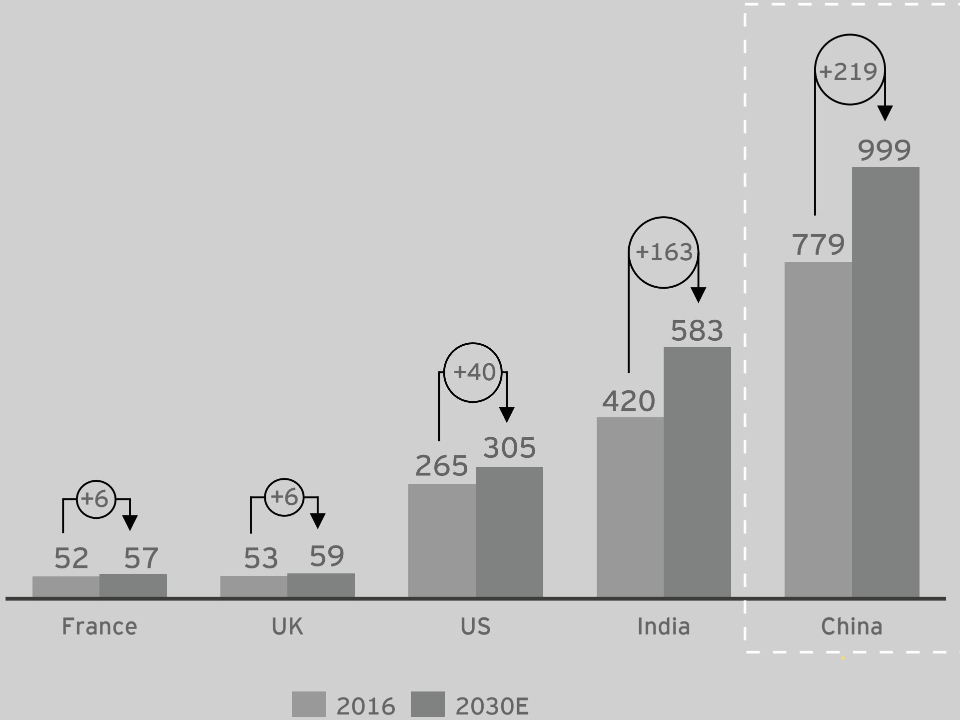
Growth of global urban population

Unit: billions of individuals (2016-2030E)

Global population expected to increase by 1.1b (+30% compared with 2016), with all growth coming from the middle class.

Growth of global urban population focuses on five nations

Unit: millions of individuals (2016-2030E)



Share of 2020 to 2030 increase by country, with China and India leading growth.

<1%	*<1%*	*4%*	*15%*	*20%*

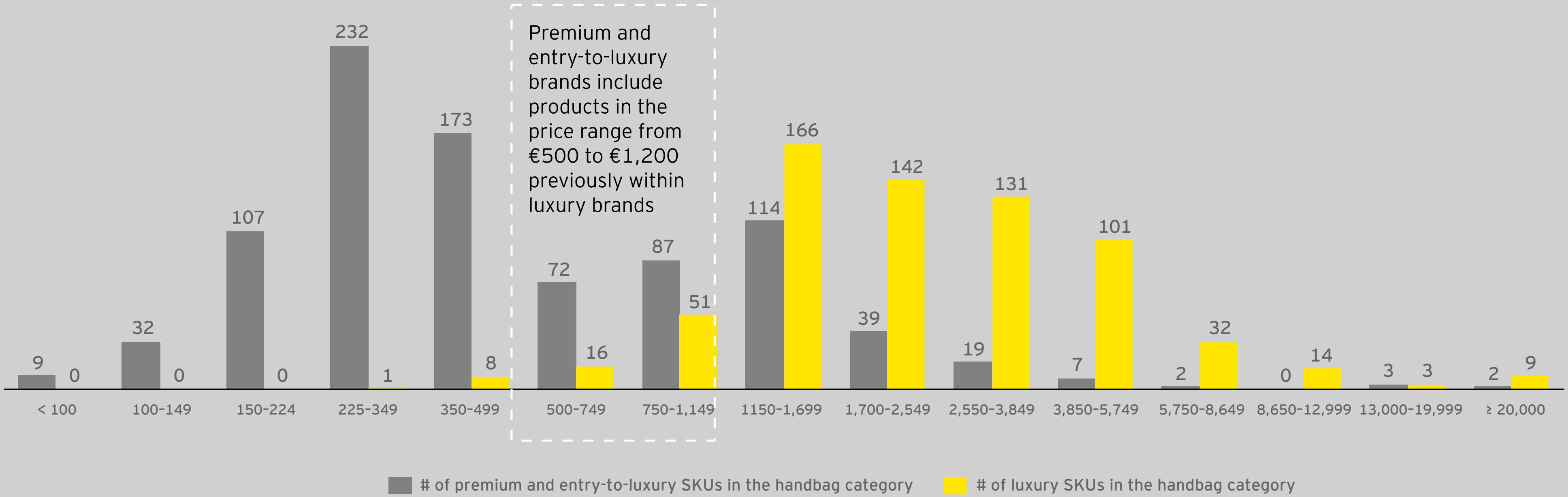
Source: EY analysis of Fondazione Altagamma data.

2

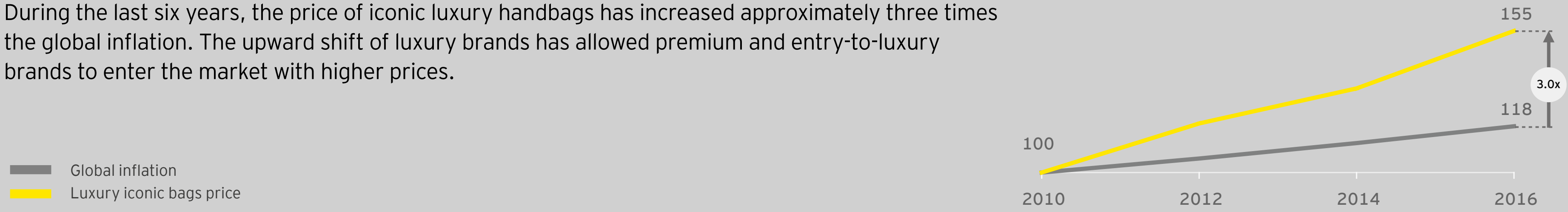
Price increase in luxury products

Significant price increases in iconic luxury products (3 times the global rate of inflation) in the last 10 years provided opportunity for premium and entry-to-luxury brands in €500 to €1,200 price range

Premium and entry-to-luxury vs. luxury market prices in 2016: an analysis of number of stock keeping units (SKUs) per price range in the handbag category.



During the last six years, the price of iconic luxury handbags has increased approximately three times the global inflation. The upward shift of luxury brands has allowed premium and entry-to-luxury brands to enter the market with higher prices.

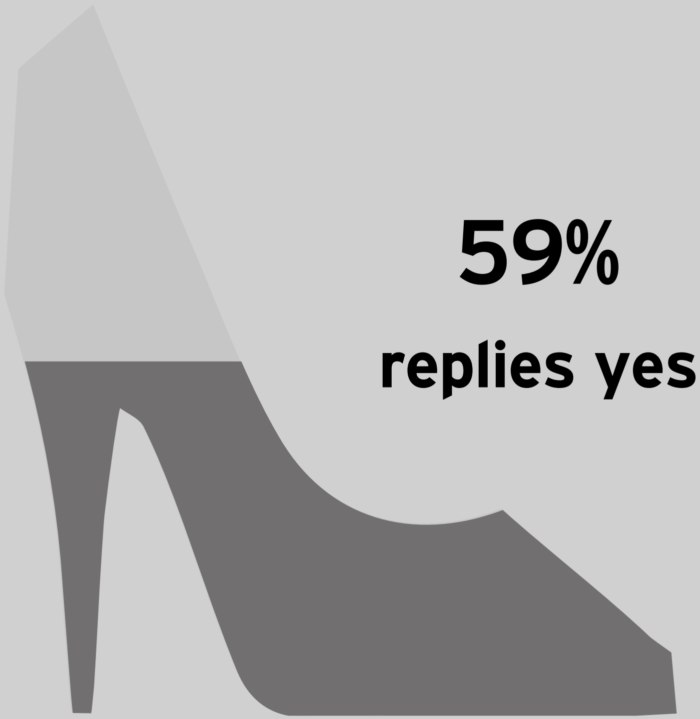


Source: EY analysis of Fondazione Altagamma data.

3 Mix and match

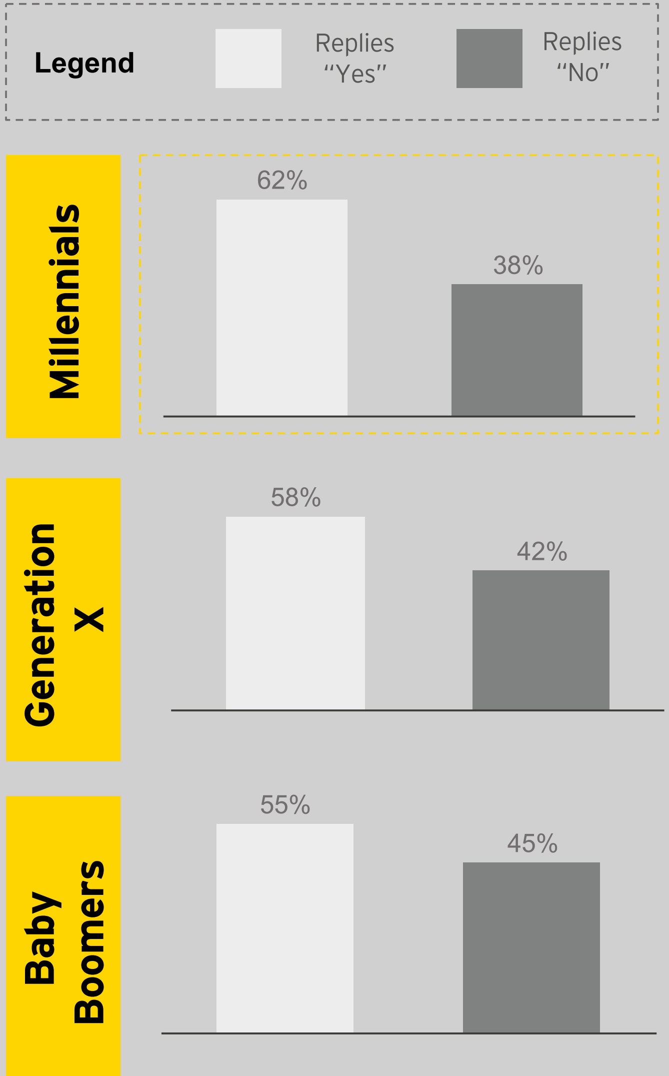
Mix-and-match trend: the value/outfit drives shopping habits especially for millennials

Do you like to mix-and-match luxury items with non-luxury items?



59%

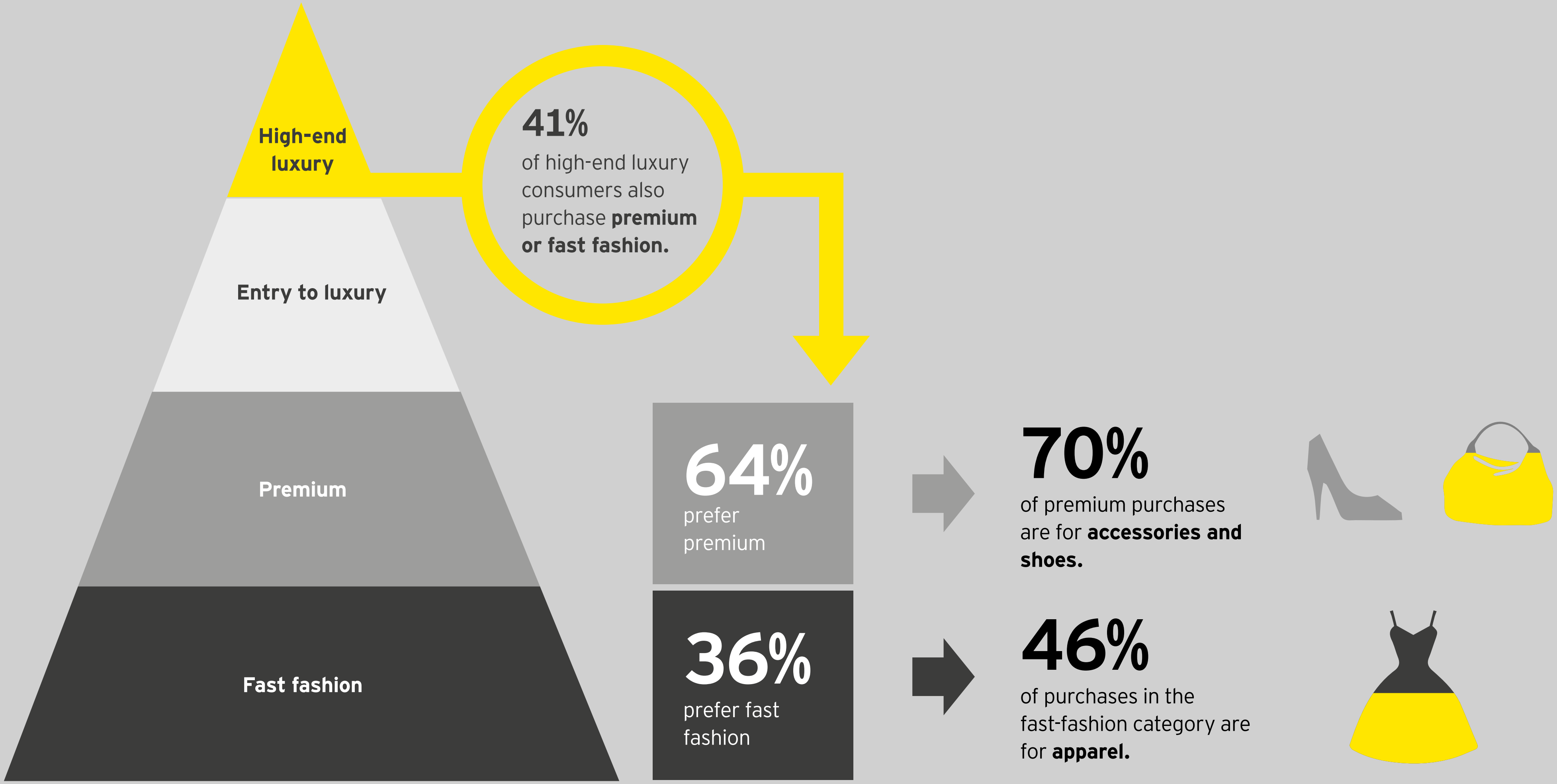
replies yes



Source: Altagamma, EY Interviews

4 Trading down

Luxury consumers are trading down, shifting part of their spending from luxury to premium and/or fast-fashion brands



Source: EY analysis of Fondazione Altagamma data.

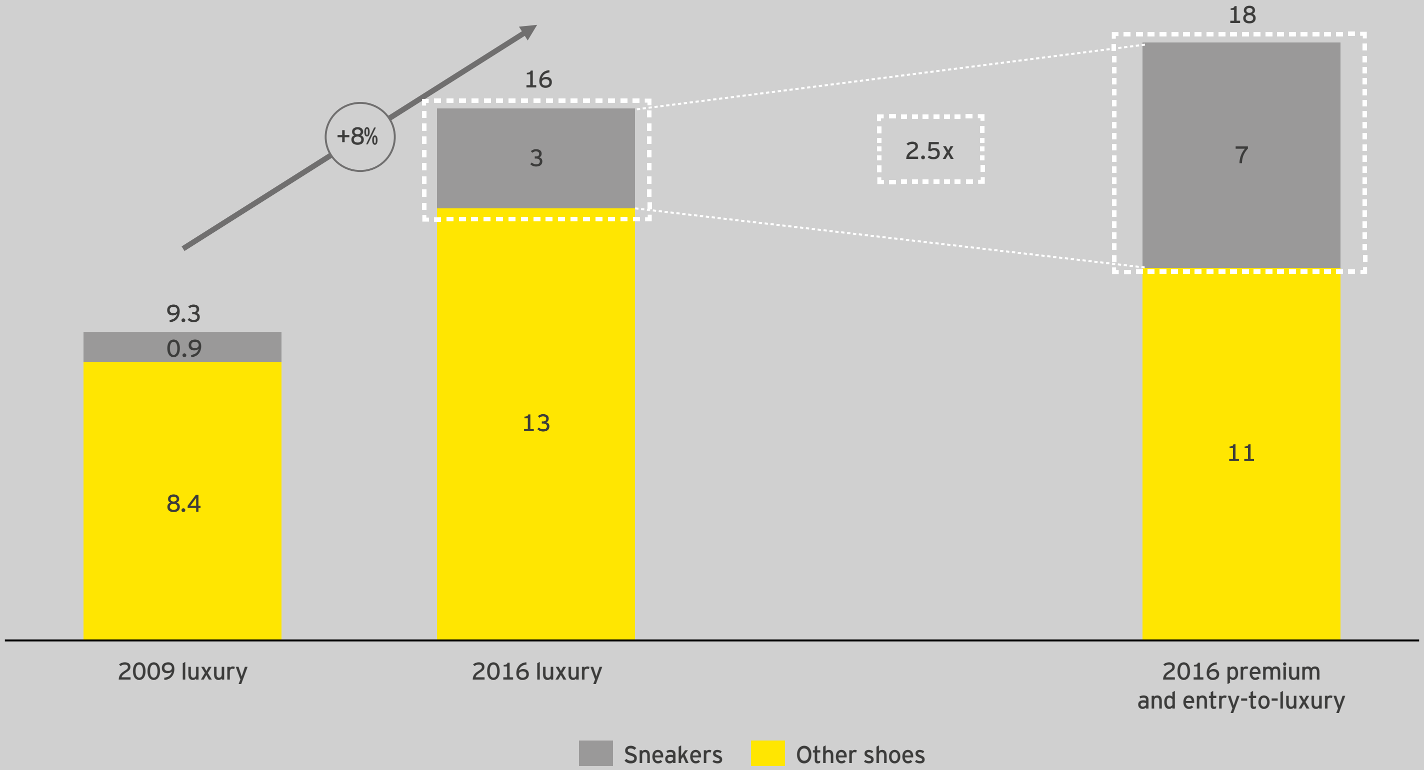
5 Casualization

Luxury opens the road to new opportunities, launching new trends like casualization, but premium and entry-to-luxury segment benefits most from new trends in terms of growth

Luxury | **Premium and entry-to-luxury**

Luxury sneakers market (€b)

Premium and entry-to-luxury sneakers market (€b)



Source: EY analysis of Fondazione Altagamma data.

B Focus on the premium and entry-to-luxury segment

Five challenges premium and entry-to-luxury companies have to face to win in the market

There are many successful small and medium enterprises with renowned high-quality products whose brand awareness, tradition and goodwill will go far beyond the amount of revenue of the company.
The size and the financial structure limit the opportunity for those companies to fully express their brand and product potential in international markets. Main challenges companies will face in the coming years:

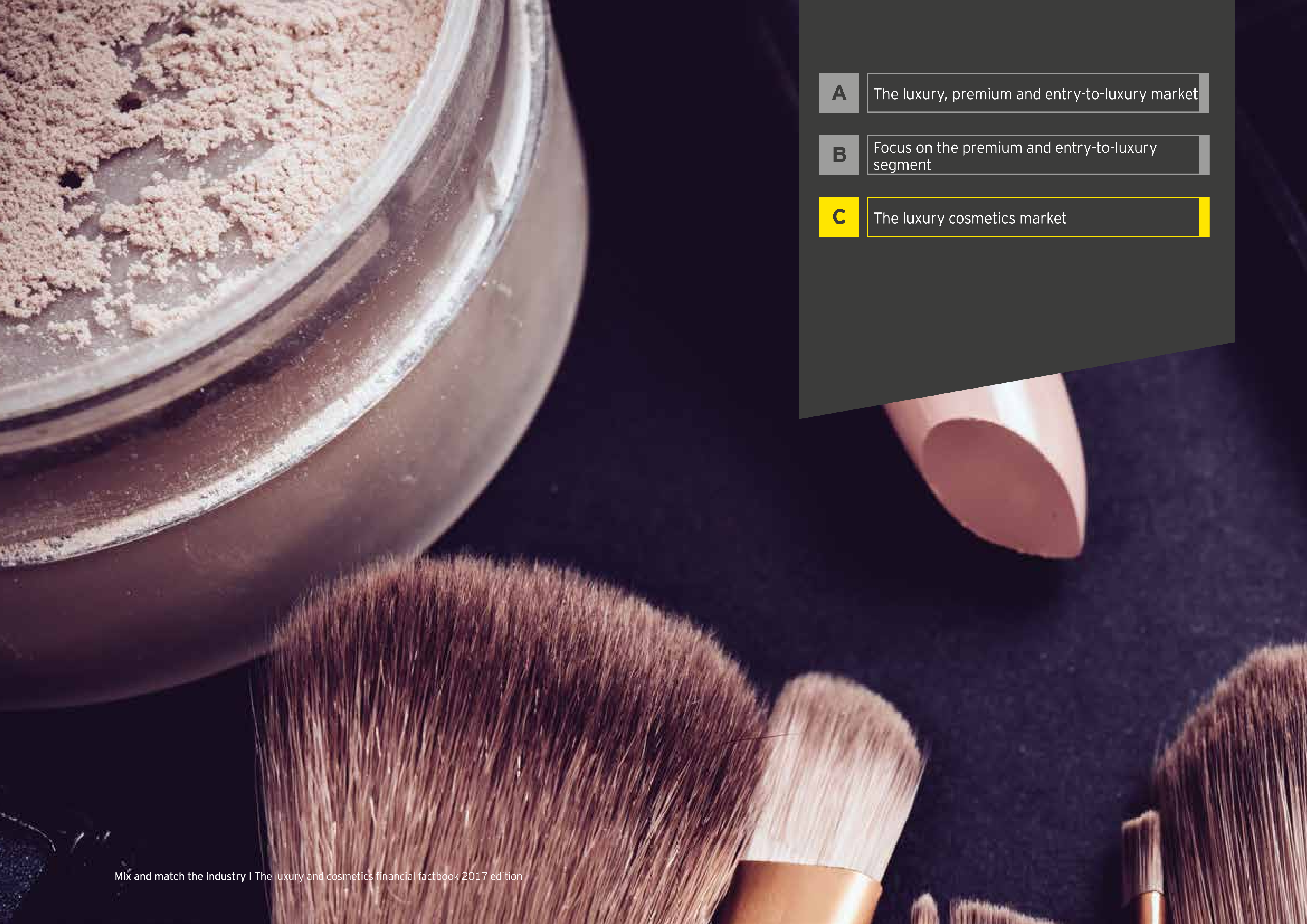
Management
Getting the necessary skills onboard to guide growth.

Retail
Improving existing retail network performance and increasing shareholders' return on investment by creating a truly sustainable and profitable selective retail expansion.

Merchandising
Rigorously managing product offerings through: rationalization of collections (depth and width) based on feedback from the market, brand expansion opportunities, and optimization of retail network buying.

International expansion
Developing a sustainable international expansion.

Digital
Implementing digital capabilities to keep up with change and make the right decisions rapidly to gain advantage in the market.



A The luxury, premium and entry-to-luxury market

B Focus on the premium and entry-to-luxury segment

C The luxury cosmetics market

The luxury cosmetics market

The global luxury cosmetics market in 2016*

€49b

+4%

+8.4%

The make-up segment is the most dynamic:

"selfie generation," strong impact of **social media.**

digital

China

is the largest country in terms of **per-capita spending** among, millennials, Generation Z, (aged between 14 and 24):

#1 China
#2 USA
#3 France

Revenues of the **top 3 companies** in the cosmetic sector, represent about 30% of the global market ...

30%

... however consumers push **innovative companies** to **gain market** share asking for very specific products, natural, innovative and customized ...

65%–80% of market share can be gained

... by creating **consolidation opportunities** in segments with a high-growth potential (skin care, fragrances, make-up).

Asia-Pacific represents

37%

of total cosmetic market**

56% of growth in the next 5 years will come from emerging markets.

+20,7%

Online sales will accelerate growth in 2017, accounting for **11% of consumption** of selective cosmetics.

In 2017 **digital advertising will surpass TV** in marketing expenditure for the personal care sector.

$191b

i.e., 36% of total advertising expenditure

*excluding mass market.
**all data except for the size of the global luxury cosmetics market includes mass market
"Sources: 2016 L'Oreal Annual report, Cosmetica Italia Report, Euromonitor and EY analysis

C The luxury cosmetics market

Drivers and strategy of global cosmetic players

1 Product

- Research of premium/prestige products.
- Introduction of a range of affordable cosmetics.
- Focus on natural products.
- Address need for multi-cultural skin-care and make-up products.
- Development of hybrid skin-care and make-up products.

Innovation 2

- Leverage high tech partnerships to develop apps and other digital tools to interact with the consumer (for example: YouCam make-up beauty app, Smart Hairbrush a brush connected to an app to establish hair health).
- Develop digital savviness.

3 Market

- Focus on scaling up niche brands in each market.
- Diversification by markets and local habits (Asia) when targeting mature age groups.
- Research of new distribution platforms in emerging markets.

Distribution 4

- Multi-channel distribution.
- Specialized multi-brand.
- Exclusive retailers which guarantee a unique retail experience with exceptional service and personalized products.
- Direct-to-consumer channel (DTC) which provides unique consumer and data insights to companies.

EY insights

A Blockchain and counterfeit goods in the luxury market

B Impact of major transfer pricing developments on luxury sector in China

C M&A activities in Switzerland's second-largest export industry

D US market dynamics for European premium beauty brands

E The retail industry repositions from brick and mortar to e-commerce

F Achieving customer centricity through digital transformation

EY insights

A Points of view from EY global sector and other industry professionals

Blockchain and counterfeit goods in the luxury market

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The counterfeit goods market

Counterfeit goods are an endemic and growing problem with serious tangible and intangible implications for luxury brands. For a business striving to maintain low distribution and high demand, combined with its dependence on brand equity, counterfeit goods directly conflict with the strategies of the luxury market companies. Consumers also are impacted, with many unknowingly purchasing imitations believing they are genuine. Research exploring the effect of counterfeit goods on the luxury brands perception shows that both consumers' brand associations and how consumers perceive the quality of luxury brands are affected by counterfeit products.

Stopping counterfeiting is a priority for luxury brands, with most companies operating a "zero tolerance policy" against counterfeiters. They employ large teams to scour the wholesale, resale and retail markets to monitor the sale of counterfeit goods. In recent years, luxury brands have become more aggressive in their attempts to combat counterfeits, in part triggered by the rise of fake goods on e-commerce and social media platforms. Today, the majority of counterfeit goods are sold not on street corners but online, posing a new challenge to retailers. The ability to monitor the sales of fakes over the internet has led many brands to take legal action against online retailers that facilitate the sale of fakes.

A Points of view from EY global sector and other industry professionals

Blockchain and counterfeit goods in the luxury market

Preventive measures often used by luxury brands are authentication techniques, which are used to validate the authenticity of a product and thereby making replication more difficult. This includes techniques such serialized bar codes and track-and-trace systems (linking product codes to database systems). While these are the most widely used anti-counterfeiting tools within the luxury market, the current unique codes and certificates of authenticity are easily replicated and provide no easy way for consumers to validate product authenticity. Other, more-advanced technologies are available, such as taggant fingerprinting (uniquely coded microscopic materials that are verified from a database), encrypted microparticles (unpredictably placed markings, such as numbers, layers and colors, not visible to the human eye) and terahertz spectroscopy; however, these come at a significant cost and, again, they do not offer a consumer-friendly means of authentication.

Blockchain: an innovation to protect from counterfeit goods

With so much at stake, it's understandable that EY and luxury brands have started exploring how technologies could protect both luxury brands and consumers from counterfeit goods. One possible solution is blockchain technology.

What is blockchain?

Blockchain is a technology that allows digital information to be shared among parties, but not copied. Data on a blockchain exists as a shared and continually updated record of the truth that is immutable and trusted. As the data is decentralized, meaning that it isn't stored in a single location but instead across a network, the records on the blockchain are both verifiable and public. This means that all parties in a network have access to the same information and that it cannot be hacked, given that no centralized version of the data exists.

How could blockchain combat counterfeiting in the luxury market?

Blockchain's immutable and verifiable nature makes it ideal for issues of trust and traceability within businesses. In the context of the luxury counterfeit problem, blockchain could offer a revolutionary way to record and verify authenticity, track ownership and, in turn, combat counterfeiting.

By using a blockchain technology platform, luxury retailers could register their products on the blockchain. The data about each item takes the form of individual "blocks," each of which is "chained" to the next block in a linear, chronological order using a cryptographic signature. Other details about the product, such as the location of manufacture, point of sale and ownership, also could be recorded.

By employing other technologies, such as QR codes or radio-frequency identification tags, consumers could use smartphones to access the secure and digital ledger to see the details about the origin and authenticity of a luxury product they've purchased. Brands also could enable other functionalities, such as the ability to record ownership and track reselling.

A Points of view from EY global sector and other industry professionals

Blockchain and counterfeit goods in the luxury market

Four ways of purchasing

1. Directly from store

2. Online from store

3. Secondary market e.g., Net a Porter

4. Off-price, market e.g., ebay, Amazon, Alibaba

Where most counterfeits are sold

Now: authenticity without blockchain

Goods tagged with printed authenticity cards/label that includes unique serial number → Customer purchases products

Counterfeiters replicate authenticity card and products → Customer unknowingly purchases a fake

Use case: improved authenticity with blockchain

Authentic goods are registered onto the blockchain and associated with barcode → Customer purchases product, scans product with app to verify authenticity, logs ownership

Counterfeiters unable to replicate authenticity → Fewer customers duped into buying a fake product

This newfound visibility into the supply chain replaces trust with objective authentication, a hugely valuable tool when combatting counterfeiting. For the supply side, this approach makes the production of convincing fakes more challenging since counterfeiters cannot register products on the blockchain. Furthermore, from the demand side, fewer consumers will be duped into unknowingly purchasing fake products, which, in turn, will reduce the loss of sales resulting from the purchase of counterfeit goods.

There also are indirect benefits of the brand. First, with fewer counterfeit products on the market, the damage to a brand and the loss of brand equity will be reduced. Second, the ability to better track and guarantee the authenticity of products within the resale market will incentivize consumers looking for cheaper products to buy secondhand, in turn reducing the demand for fakes.

A Points of view from EY global sector and other industry professionals

Blockchain and counterfeit goods in the luxury market

A perfect solution?

It must be acknowledged that while blockchain does offer a credible alternative to the current authentication techniques, it is not a silver bullet to the pervasive issue of counterfeiting. There always will be those consumers who consciously purchase counterfeit goods and manufacturers able to meet that demand. A blockchain solution could be powerful, however. A holistic approach that is both preventive and reactive is required in combatting counterfeiting. This should include a combination of robust anti-counterfeiting strategies, strict law enforcement and improved authentication techniques.

As the use of e-commerce sites by counterfeiters becomes increasingly prolific, there has never been a more important time for luxury brands to consider new and innovative ways to combat this issue.

EY is investing in research and continues to hire professionals, including cryptographers, physicists, mathematicians and software developers, to facilitate the mature and scalable design of blockchain services. Inside the EY blockchain labs, these professionals work to support companies in developing and applying block chain services to help accelerate their journey toward becoming digital enterprises.

B Points of view from EY global sector and other industry professionals

Impact of major transfer pricing developments on luxury sector in China

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Introduction

In *The luxury and cosmetics financial factbook – 2015* edition, tax partners of EY member firms in China' introduced readers to a range of tax challenges facing luxury businesses in China. Since that time, many of the trends that were noted have accelerated. This is especially true with respect to transfer pricing (TP), in which the regulatory scheme has been comprehensively updated. Luxury groups with Chinese operations need to react quickly if they have not already done so, and should be prepared to consider operational or TP policy changes if necessary.

TP concerns the price of transactions between related companies involving goods, services, intangible property (IP) and financing transactions. For example, if a Chinese distribution subsidiary purchases product from its foreign parent, the "transfer price" is the price it pays upon import. Similarly, if a Chinese manufacturing subsidiary licenses IP from the foreign brand owner, the TP concerns the amount of the royalty paid.

TP integrally is linked with corporate income tax, customs duty, consumption tax (CT) and value-added tax (VAT). For income tax, the TP or royalty paid to a foreign brand owner is a deduction, meaning the higher the price, the *lower* the taxable income. For customs purposes, it is the TP itself that is subject to tax, meaning the higher the price, the *greater* the customs duty. In the case of CT and VAT, tax will be collected on the TP upon import and refunded on the final sale.

In this article, we will discuss the relevant latest developments from the Organisation for Economic Co-operation and Development (OECD) and the United Nations (UN) and how China has localized the base erosion and profit shifting (BEPS) initiatives, which may have a profound impact on luxury and cosmetics multinational companies operating in China. We also will share our experience on the ground and observations in relation to the luxury and cosmetic sector from a TP perspective.

Developments: OECD and UN

TP has been a central component of the most significant development in the field of international tax in more than 50 years, the project led by the Group of Twenty and the OECD regarding BEPS. The BEPS project involves work on 15 "action items" covering the gamut of international tax issues, including four relating to TP.

The central premise of the BEPS project is that profits should be taxed when economic activities are performed and when value is created. Multinationals were seen as having artificially shifted profits into low-tax jurisdictions; BEPS reforms are designed to make this impossible in the future. Chinese tax authorities are concerned about profit shifting and want to claim their share of profits that have been

B Points of view from EY global sector and other industry professionals

Impact of major transfer pricing developments on luxury sector in China

lightly taxed. Taxpayers who are not involved in profit shifting or aggressive tax planning often are finding themselves under suspicion as well.

Because TP directly affects profits, manipulation of TP is one way that profits can be artificially shifted. Even if there is no manipulation or intentional profit shifting, Chinese tax authorities – like their counterparts in other tax jurisdictions – are keenly interested in TP since they determine how much profit each jurisdiction can tax.

Under BEPS reforms, the location of the decision-making that is core to profit and value creation is especially important for TP purposes. While the performance of more routine activities needs to be compensated, the decision-maker often is the related party that earns any extraordinary profits or bears any loss. When it comes to the development of IP, which often is the driver of extraordinary profits, BEPS TP rules focus on the development, enhancement, maintenance, protection and exploitation (DEMPE) functions.

To monitor TP compliance and assess and select audit targets, many tax jurisdictions require local taxpayers to document their TP. For instance, China has had documentation requirements since 2008. The BEPS project has put in place a new three-tiered documentation framework that is being implemented by jurisdictions throughout the world, including China. This framework consists of a country-by-country (CbC) report, a master file and a local file.

Typically, large multinational groups will be required to file a CbC report with the tax authority where the multinational has its headquarters. That tax authority then shares the CbC report with other tax authorities through treaty-based exchanges. The CbC report provides data about such indicators as revenues, profits, taxes, assets and headcount of all members of the multinational group. Tax jurisdictions will be using CbC reports to identify companies to audit. For example, if a group is paying very little tax in China in relation to its assets or headcount but recorded considerable related-party transactions, Chinese tax authorities surely will take a very close look at their TP policies.

The master file is a document that is prepared by the multinational group's headquarters. It provides a high-level overview of the group's business, including its IP and financing strategies, as well as an overview of the group's global TP policies. The headquarters will provide the master file to each of its subsidiaries around the world, which then may provide it – together with the local file – to the tax authorities in the country where they do business. It is, therefore, important that multinationals exert effort to make their master file and their local files consistent with each other.

The local file is similar to documentation that taxpayers prepared prior to the BEPS reforms. It documents the TP policies of a particular member of the multinational group and demonstrates that they comply with global standards (the so-called "arm's-length principle"). As we shall see, China's local file requirements are far more extensive than the OECD's recommendations.

The UN is on a parallel course with the OECD in terms of creating guidance about TP principles and documentation. Its guidance, however, is focused on the specific issues faced by developing countries. In May (2017), the UN released an updated practical manual for this purpose. China contributed a chapter to the practical manual outlining China's specific views about a number of issues, including market premium, as discussed below.

Developments: China

In 2016 and 2017, China issued two public notices that localize BEPS recommendations for China. In June 2016, Public Notice 42 implemented the BEPS threefold documentation framework. Then, in April 2017, Public Notice 6 implemented many of the other BEPS TP reforms.

As we predicted in 2015, China has escalated reporting and disclosure requirements to a new level. China's requirements with respect to CbC reporting and the master file largely are in line with the OECD's recommendations. However, China has imposed much more extensive disclosure and analysis requirements for the local file. These

B Points of view from EY global sector and other industry professionals

Impact of major transfer pricing developments on luxury sector in China

requirements take effect for local taxpayers' 2016 tax year. The first local file must be prepared by June 30, 2017.

Public Notice 42 also greatly increases the reporting burden for disclosure of related-party transactions on companies' Chinese tax returns. Other than the CbC reporting forms, the number of related-party transaction reporting forms (RPT forms) has nearly doubled from 9 to as many as 16. This reporting requirement also takes effect for the 2016 tax year and the new forms must be filed with taxpayers' tax returns due 31 May 2017.

Many luxury business companies are struggling with some of the disclosure requirements of the local file and the RPT forms. In the last few months during this first year of implementation, a number of difficult requirements are being worked through, including:

- RPT forms require disclosure of the effective tax rates of related parties in other countries, as well as an indication of any preferential tax treatments they enjoy. Gathering this sort of extraterritorial information proved to be an administrative challenge and a challenge to corporate disclosure policies.
- The local file requires a value-chain analysis. The lack of guidance about how to prepare such an analysis poses challenges. Although the master file also requires disclosure of supply chains, companies are considering whether to make the additional effort of isolating the value chain relating to Chinese business, which may differ from the global supply chain. Taxpayers are also required to provide financial statements and disclose value-chain profits for each related party within the relevant value chain, presenting extraterritorial disclosure challenges even more daunting than the effective tax rate disclosures. In addition, the guidance in Public Notice 42 is silent about the disclosure treatment for multinational groups operating multiple brands and product groups with different value chains, which is fairly common within the luxury sector.
- The local file also requires an analysis of location-specific advantages (LSAs). The LSA concept is emphasized by Chinese tax authorities both in regulations and in practice. The notion is that companies operating in the Chinese market should earn higher profits because of LSAs, especially location savings and market premium. Luxury businesses do not tend to enjoy location savings, given that few have manufacturing operations with low-cost labor. However, luxury businesses are finding challenging to analyze potential market premiums, given that luxury products often sell at higher prices in China than they do in other markets. In this context, Public Notice 6, which allows for non-adjustment of LSAs when local comparables are utilized, seems to be offering some breathing space for luxury goods operators in China.

China's contribution to the UN practical manual reveals Chinese tax authorities' views about market premium. They take note of the heavy sales and marketing activities of Chinese subsidiaries building brand awareness in China and correlate it with exponential growth in sales revenue. They take the view that additional profits resulting from the unique characteristics of the Chinese market (e.g., consumer preference for foreign brands and imported luxury products and China's large population with growing wealth) should be taxed in China, tying it to the BEPS concept of value creation or claiming the existence of local marketing intangibles. The tax authority may also discount the contributions of foreign intangibles based on these concepts. Finally, they note that many Chinese nationals go abroad to purchase luxury products, having acquired the taste for them in China but being deterred by higher prices in China. It is suggested that portions of the sales revenue and profits from foreign sales to Chinese customers may be attributed to the Chinese subsidiary.

Luxury business taxpayers sometimes find themselves at odds with the tax authorities' views of market premium. There are a number of reasons for higher prices in China that have nothing to do with profit

[1]SAT Public Notice [2016] No. 42 – Public Notice on Matters Regarding Refining the Reporting of Related Party Transactions and Administration of Transfer Pricing Documentation.
[2]SAT Public Notice [2017] No. 6 – Public Notice on Supervisory Measures for Special Tax Investigation Adjustments and Mutual Agreement Procedures.

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shifting and do not reflect a market premium. A major reason for high prices is the high indirect tax burden (customs and CT and VAT) imposed on luxury products. These taxes account for a significant portion of retail prices. Under recent CT reforms, tax rates on cosmetics are being reduced and a number of luxury players are reducing prices in response.

Another reason for the higher prices of luxury products in China is that the cost of operating in the Chinese market is higher than elsewhere in the world. In location-savings inquiries, the notion of location dissavings is well understood. This could be called market "dis-premium." For example, relatively expensive television advertising is much more important in the Chinese market. Also, since store image is particularly important in China, extensive store renovations are needed more frequently than in mature markets.

Public Notice 6 also implements other BEPS reforms, including DEMPE analysis and disregard transactions with related parties that are located in low-tax jurisdictions and have limited substance. Luxury business companies that are members of corporate groups that include such low-tax, low-substance entities are considering ways to limit their exposure to these provisions.

Public Notice 6 modifies the OECD's DEMPE framework by adding an additional "P" for promotion (i.e., DEMPEP). While promotion could be seen as covered by other DEMPE functions, such as enhancement or exploitation, this modification to the framework reflects China's intense focus on Chinese market activities. This is a very relevant consideration for luxury businesses because promotional activities are core to their businesses in China. Moreover, if the Chinese subsidiary is found to have a level of decision-making authority over Chinese promotional activities, there is an even greater risk that tax authorities will argue a business owns significant marketing intangibles.

As a result of the DEMPEP framework and the Chinese marketing intangibles issue, some luxury business companies are reconsidering whether a limited-risk-distributor arrangement, which is very common among companies in the sector, continues to be viable in China. Consideration increasingly is being given to the profit-split analysis or other nontraditional TP approaches.

Audit environment: China

The luxury sector has long been a focus of Chinese tax authorities for investigation. The statute of limitations for TP audits is 10 years, so audits launched in 2017 will review related-party transactions conducted in years as far back as 2007. The amounts at issue can be very large; there have been many cases in tier-one cities involving more than RMB100 million of additional tax liability arising from TP adjustments.

Chinese tax authorities keep statistics of three types of tax collection efforts: investigation, services and administration. In 2016, formal investigations reportedly generated RMB9.4 billion of tax revenue. However, RMB42.2 billion of tax revenue was attributed to "administration," which includes informal and follow-up investigations.

Seemingly routine TP inquiries from the authorities should not be taken lightly. Authorities put great pressure on taxpayers to reassess their TP, make self-assessments and pay additional taxes.

Authorities are aggressively challenging luxury and cosmetics product taxpayers that have lower profits than their industry peers, or have losses. During the past few years, authorities have developed databases based on RPT form disclosures, TP documentation and other data. These databases give them unprecedented visibility into the TP and

[3]Location savings are the net cost savings derived by a multinational company when it sets up its operations in a low-cost jurisdiction.
[4]Market premium relates to the additional profit derived by a multinational company by operating in a jurisdiction with unique qualities that impact the sales and demand of a service or product.

[5]Cosmetic products are divided into high-end and general categories. For high-end cosmetic products, the CT rate would be reduced from 30% to 15%. For general cosmetic products, the CT rate would be reduce to 0%, effective October 1, 2016.

B Points of view from EY global sector and other industry professionals

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reported profits of luxury sector businesses. The tax authorities are using this information to rebut taxpayer claims that their losses are attributable to industry downturns or other competitive factors.

The luxury market in China has suffered a number of setbacks in the past few years due to foreign exchange issues and the government's anti-bribery campaign. However, when tax officers see flagship stores in expensive, upscale malls and extensive advertising campaigns, they form an impression that these high-profile luxury stores all should be making a lot of profits.

Tax authorities take note of the significant advertising and promotion expenses in China, but they don't stop there. They also start looking at the high rental costs associated with flagship stores and similar costs. The authorities argue that these costs are essentially advertising for the benefit of the brand owner and that the Chinese subsidiary should be compensated by the brand owner with a service fee for its advertising services. We not only have seen some multinational companies choose to adopt this sort of TP arrangement, but we also are aware of some instances of such arrangements between luxury brand owners and unrelated franchisees. When designing a TP arrangement, serious consideration should be given to this approach.

Even before Public Notice 42, authorities have been looking at value chain profit. That is, they are focusing on the worldwide group's global profits rather than Chinese-specific profits.

In addition, authorities are focusing on decision-making. For loss-making entities, taxpayers may argue that the Chinese subsidiary makes the decisions and bears the risk of losses. Conversely, when there are profits, taxpayers may argue that the brand owner makes the decisions and the Chinese subsidiary only deserves a routine return (i.e., a limited-risk-distributor arrangement). Addressing these issues requires careful consideration and taxpayers should pay attention to how they are disclosed and analyzed in their local files and master files.

So far, we have not encountered tax authorities arguing in audit cases that a Chinese subsidiary that has been building the brand in China should be rewarded for Chinese customers purchasing abroad. However, as noted above, this argument has been raised in China's contribution to the UN's practical manual. It potentially can be addressed through the service-fee approach, i.e., rewarding the Chinese subsidiary for all of its brand-building and advertising activities, regardless of the level of sales actually made in China.

For many luxury taxpayers, the only notable related-party transaction is the purchase of merchandise by the Chinese subsidiary. These companies often are caught between customs authorities (demanding higher transfer prices) and corporate income tax authorities (demanding lower prices). Due to the constraints of compliance with customs authorities' demands, many companies have found it a struggle to properly implement a limited-risk-distributor arrangement, which would limit the Chinese subsidiary's profit level. Consideration can be given to profit-split methods or service-fee arrangements to bridge the gap between customs and income tax.

In fact, during customs valuation audits and investigations, one of the most common challenges is the arm's-length nature of the import price. In China, it is very common for customs offices to request companies' TP documentation when they challenge the declared dutiable value. Given the new disclosure requirement under Public Notice 42, there is much more information (e.g., the value chain analysis, additional details related to intragroup services and location-specific advantages) that previously was unknown to customs that may cause reassessment of the customs valuation. Therefore, while lots of attention should be given to BEPS and TP, taxpayers should not underrecognize or address the related customs and trade implications.

Conclusions

Given the above, multinational companies likely will have growing needs for dispute resolution and avoidance of international double taxation resulting

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from TP disputes. China has recently updated its guidance about advance pricing agreements (APAs) and mutual agreement procedures (MAP). A bilateral APA is an agreement between the tax authorities and the taxpayers on both sides of a related-party transaction regarding TP arrangements in the future (and retrospectively in select countries). Similarly, MAP involves the tax authorities trying to reach agreement regarding taxpayers' TP arrangements. The difference is that MAP occurs years after the related-party transactions occurred — specifically, after one or the other tax authority has challenged the TP arrangements and sought to collect more taxes.

In light of the many challenges they face, luxury businesses may want to consider pursuing APAs to get in front of the issues so they do not face double taxation due to tax authorities taking different positions. If, on the other hand, a luxury business already is facing a large tax adjustment relating to its TP, the possibility of taking the case to MAP seriously should be considered.

In all events, luxury industry taxpayers should take a hard look at their businesses and their current TP arrangements in China, and revisit their strategies to monitor TP risks in daily operations. We recommend they talk to a trusted advisor to assess whether adjustments are needed to take into account the ever-changing local audit and regulatory environment. China should be an integral part of any multinational's global risk management and TP documentation strategies.

[6] SAT Public Notice [2016] No. 64 — Enhancement of Administration of Advance Pricing Arrangements.
[7] Public Notice 6.

C Points of view from EY global sector and other industry professionals

M&A activities in Switzerland's second-largest export industry – securing supply as central driver of consolidation in the watch component industry

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In last year's edition, we identified three waves of consolidation in the Swiss watch brand landscape. In a first phase, the Swiss watch groups The Swatch Group and Compagnie Financière Richemont began acquiring luxury watch manufacturers to complement their brand portfolios, followed by the strategic diversification of French luxury groups such as LVMH and Kering into "Swiss-made" watch activities. Finally, Asian buyers expanded into the affordable luxury space of Swiss watch brands but were hampered due to the recent domestic market developments.

In April 2017, it was announced that CVC Capital Partners would acquire Breitling, one of the last large, independent Swiss luxury watch brands. The remaining independent luxury brands comprise the likes of Rolex, Patek Philippe, Audemars Piguet and Chopard, most of which have expected valuations in the billions, making them too expensive for the majority of potential investors.

Contrary to the reduced M&A activities of Swiss watch brands, the watch component industry provides further potential consolidation opportunities due to anticipated changes on the supply side and market pressure to increase the value add of a luxury watch.

Legislative changes paired with market trends lead to expected supply shifts of watch components. In December 2009, The Swatch Group, historically obligated to supply the watch industry with certain critical watch parts and movements, announced its intention to reduce, and ultimately stop, its supply of entire watch movements from its own manufacturing company ETA (ETA SA Manufacture Horlogère Suisse) to competing third-party watch manufacturers. After complaints by several watch manufacturers were filed with the Swiss Competition Commission (i.e., COMCO), The Swatch Group (ETA) is being forced by a court order to deliver its watch movements to third parties at historical levels, and phasing out until the end of 2019. A hard stop in 2020, however, is not to be expected. In past years, The Swatch Group reported a decrease in sales of -10.6% in 2016 (a -3.0% decrease in 2015) to €7.1bn. With every additional month of decreasing sales, the continuation of selling its ETA movements to third parties becomes likelier, and production overcapacity needs to be addressed to avoid margin erosion. Third-party sales of movements are not only an efficient way to cover fixed costs, but also a means to soften a further topline decrease. It is of little surprise that rumors arose that Swatch Group would continue to supply main competitor Richemont with ETA movements beyond 2019. Nevertheless, a substantial market share could be released during the next years by ETA forcing watch brands outside of the Swatch Group to look for alternative sources of individual watch parts and assembled movements.

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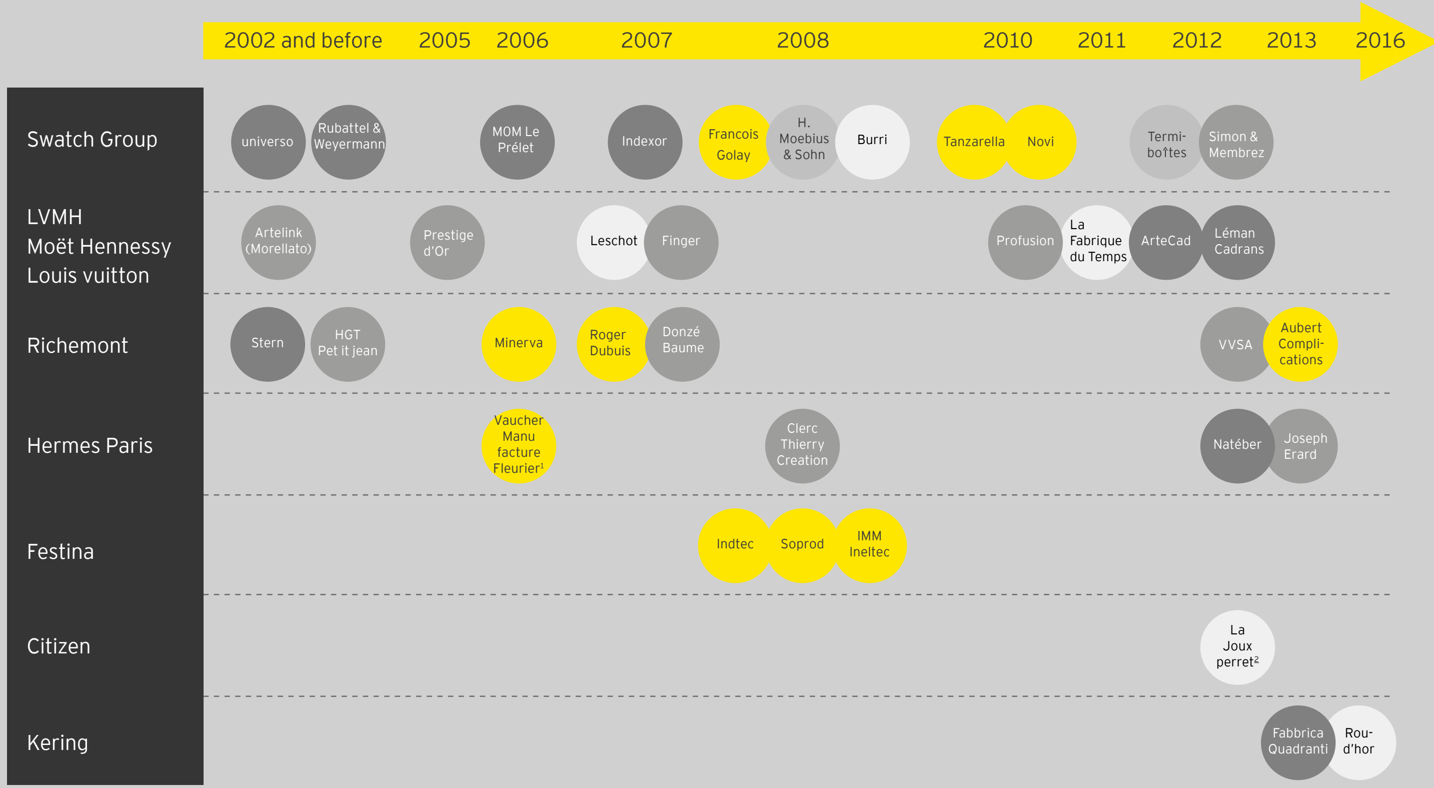
M&A activities in Switzerland's second-largest export industry – securing supply as central driver of consolidation in the watch component industry

Another factor impacting the Swiss watch market is an amendment to the so called "Swissness" law. To enhance and protect the Swiss-made label, the Swiss parliament passed an amendment to the Swissness law, which took effect in January 2017. The amendment requires that for Swiss-made watches, at least 60% of the production costs are attributable to operations carried out in Switzerland, applying not only to the movement and final inspection, but to the entire watch (including already mentioned earlier, wristlet and case). Further, the Federation of the Swiss Watch Industry FH stipulated that to carry the label Swiss-made, the watchmaker must also execute the technical development of the movement and the watch as a whole in Switzerland.

Together, the phasing out of ETA and the amendment to the Swissness law are two of the most important elements for private equities and financially strong industry players. However, their success is highly dependent on the strategy pursued by Swatch Group because ETA will remain the cost leader for a long time and, therefore, largely decides the size of its market share.

* It should be noted that if Swatch Group is not able to fully utilize their production facilities of ETA with own in-house demand they will most likely use the remaining capacity to sell aggressively priced movements on the market



Movements · Mechanical parts · Cases & wristbands · Dials & hands · Others

Figure 1 Key consolidators securing their supply of critical watch parts

Sources: EY research, merger market

[1] Only 25% stake

[2] Citizen acquired Prothor Holding consisting of La Joux Perret, Protoctec and Arnold & Son

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Examples for such vertical integrations at luxury groups are Hermes and LVMH, each acquiring various component manufacturers, including watch dial specialists Nateber by Hermes and ArteCad by LVMH.

Competing with luxury groups for the critical supply of watch parts are larger, independent watch brands and movement manufacturers. While the larger, independent watch brands, such as Breitling and Chopard, decided to build in-house competencies and today manufacture their own movements, smaller players, mainly in the affordable luxury segment, mostly lack the financial power and scale to efficiently run in-house manufacturing and have to rely on independent movement suppliers. Such independent movement producers include Sellita and Ronda, both already benefiting from the ongoing phasing out of ETA.*

Upstream consolidation of watch parts supplier gains increased private equity attention

Independent watch brands as well as movement manufacturers rely on independent component suppliers from Switzerland, capable of flexibly delivering high-precision parts. To achieve necessary economies of scale, upstream consolidation has started with component suppliers and increasingly is attracting private equity involvement. Of course, following a more dynamic and opportunistic route to achieving a return on their investment, some enter into a wager on the phaseout of ETA. Quilvest, a leading global independent wealth manager and private equity investor, for example, has followed a dynamic buy-and-build strategy around Groupe Acrotec, having assembled a portfolio of nine operating entities (excluding further subsidiaries), making Groupe Acrotec a strong player in the industry. In 2016, the company was sold to another private equity firm, Castik, which also supports an ambitious buy-and-build strategy, having acquired the Swiss gemstone manufacturer Gasser-Ravussin and Mimotec, a component and anti-counterfeit technology manufacturer, within this first year.

Other examples of private equity involvement in the Swiss watch component industry are Vinci Capital and SVC (Helvetica Capital), which invested in the component and movement manufacturer Bandi; multi-family office Verium, which holds Christ & Heiri, a high-precision cogwheels, pinions and worm gears producer, Helarb Fund, which owns the four assets Decotech, Li Calzi, Monyco and Fehr & Cie, and Findos Investor within its portfolio company Roventa-Henex, a manufacturer of private-label Swiss watches; and HQ Equita's investment in Stettler Sapphire (sold to the strategic investor Groupe IMI in 2016).

With expected shifts in the supply of watch components, increasing market pressure on all participants and a high level of market fragmentation today, the sector yields interesting growth opportunities for buy-and-build strategies of private equities and financially strong industry players. However, their success is highly dependent on the strategy pursued by Swatch Group because ETA will remain the cost leader for a long time and, therefore, freely decides the size of its market share.

* It should be noted that if Swatch Group is not able to fully utilize their production facilities of ETA with own in-house demand they will most likely use the remaining capacity to sell aggressively priced movements on the market

D Points of view from EY global sector and other industry professionals

US market dynamics for European luxury beauty brands

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US market is a sizable, growing beauty market

European luxury beauty brands have seen great success in the US market. Powerhouse brands such as L'Oréal, Nivea and Lancôme have become as ubiquitous in the US as they are in their home countries. Other luxury brands, such as Chanel and Dior, also have made impressive strides in the US, ranking 3rd and 13th, respectively, on *Women's Wear Daily's* Power 25 list of beauty's strongest brands. While the potential for success in the US market is significant, European luxury beauty brands must understand the underlying growth drivers, market structure and evolving consumer demographic shifts that will equip them for success when entering the growing, yet highly competitive, US market.

The US is the largest market globally for beauty and personal care – more than five times the size of the largest European markets, including Germany, France and the UK. The industry also is expected to grow at a steady pace, driven by the luxury segment, which is forecasted to increase at a higher rate through 2020. In addition to being the largest market for luxury beauty brands, the US market is growing faster than the European market. With its size and strong growth trajectory, the US should be an attractive growth priority for European luxury brands to expand their global footprint.

Success in a highly competitive US market

The US beauty and personal care market is more consolidated than the European market. In the US, the top 10 companies collectively capture a greater share of the luxury market segment than do the top 10 companies in the European luxury segment. This relative consolidation leads to fierce competition. For example, the top three players in the US – Estee Lauder, L'Oréal and Coty – jointly command nearly half of the luxury segment's sales and exercise significant influence over the coveted share of finite shelf space at key retailers.

Brand proliferation facilitates competition, allowing top players to populate the category with a multitude of brands that seem new to consumers and yet actually are owned in the same portfolio. This appearance of competition keeps the consumer experience new and fresh (keeping consumers coming back and, therefore, keeping retailers happy), while establishing a strong barrier to entry for truly new brands to enter the market. This market consolidation results in a significant competitive barrier for new brands to capture a share of the US market.

As a result of significant competition and product proliferation, distribution channels play a critical role in both the market entry strategy and growth

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potential of beauty brands entering the US market. Fundamental differences between the distribution channel mix of the European and US markets demand a localized distribution strategy, which is critical for the growth of European brands in the US marketplace.

While one of the primary distribution channels in Europe historically has been specialty retail, the US beauty and personal care channel mix has been more diverse, leveraging mass and mixed retailers like Target and Walmart, while the specialty retail channel has been burgeoning. The rising popularity of specialty stores, such as Ulta Beauty and Sephora, has cultivated a strong presence by appealing to US consumers' growing preference for both luxury brands and a premium in-store experience. These specialty retailers have meaningfully changed the way US consumers buy their beauty products by cultivating a desire to shop and explore across brands and fueling their appetites to discover new brands. As a result, in the last 10 years, Sephora has more than doubled its store count to around 400 and Ulta Beauty has more than quadrupled its footprint to more than 900 stores by end of 2016. Mixed retailers have been forced to respond: traditional retailers, such as Nordstrom, have improved access to luxury beauty products and now allow their customers to "try before they buy" by enticing them with trials and samples. Both department stores and mixed retailers will continue leveraging beauty as an important means of drawing foot traffic to their stores.

European brands with visions of growing in the US would benefit by leveraging their experience in specialty retail while building a presence in the robust mixed retailer channel in the US. Additionally, the growing online distribution and direct-to-consumer channels offer an asset-light and quick entry into the US market and represent strong growth opportunities through which a luxury brand can attain high visibility with little investment.

US demographic shifts fuel opportunity and innovation

A key consumer segment in the US that is driving growth is the millennial population. The US millennial generation, at a median age of 37, is the largest population segment in the US at 75 million, and is larger and younger than Europe's millennial population. Millennial consumers are an enormous and maturing commercial force, commanding both trendsetting power and spending power. Millennials are more likely to spend money on products and experiences they perceive as valuable and they have new digital outlets to communicate this value. In an era in which millennials' social lives are influenced by and documented on social media, millennial consumers have an added incentive to be especially engaged in their beauty routines and they aren't afraid to splurge on luxury beauty products. In addition, the rise of social media influencers, who wield increasing sway over millennials' luxury beauty purchases, has enabled this multi-tiered and sophisticated customer base to help shape a brand's presence on social media and, ultimately (ideally), inspire consumer loyalty. Because US millennials (and their social media influencers) are such a highly influential population, both economically and socially, European brands need to better understand what motivates these youthful customers to create products and experiences that will establish a loyal following in the US market.

In addition to the millennial population, European brands must be cognizant of the diverse, multicultural US population. The expanding purchasing power of this segment presents a compelling opportunity for companies to develop products that address a wide spectrum of beauty concerns. There are ample opportunities for companies to further penetrate the skin care, hair care and oral care categories in the US by addressing specific unmet multicultural needs. Companies developing multicultural beauty offerings are likely to outpace the growth of the overall beauty market as this diverse consumer population seeks products to address specific unmet needs.

Finally, beyond these demographic shifts, consumers' increasing preference for plant-based, organic and

US market dynamics for European luxury beauty brands

natural beauty products has spurred investment and innovation as companies race to capture market share in this growing category. Natural products appeal to these consumers, both from ethical considerations (concern for environment and sustainability) as well as health concerns (fear of harmful ingredients). Globally, the natural and organic beauty market is estimated at $11 billion in 2016, and is likely to double by 2024, with the US acting as a significant growth catalyst.

Alignment of distribution model and investment capacity

To efficiently access the dynamic US marketplace, European brands have commonly partnered with US distributors and retailers to quickly leverage local resources, networks and market knowledge with minimal investment. For example, BeYu, a German masstige brand, entered the US in 2015 through a partnership with local distributor BAM Brands USA. BeYu relied heavily on the distributor to make key decisions about expansion, including hiring a public relations agency and establishing partnerships with online and offline retailers. BeYu made limited investment in building a physical presence and focused on retail partnerships to reach its target customers, and the company plans to maintain this distribution model to further grow and strengthen its US presence.

On the other hand, some European players see strong value in having a physical presence and building direct client relationships to establish a strong local brand presence. A recent success story is Dutch brand Rituals Cosmetics. The company entered the US market in 2013 through luxury department stores alongside its e-commerce site. After the initial phase, Rituals invested heavily in establishing two stand-alone, company-owned stores in premium New York markets. Currently, the brand is operating 11 stores in New York and has a presence in 23 Barneys and Cos Bar stores. In addition to specialty retail, Rituals also offers business-to-business distribution for law firms, corporations, health care and hotels, and even aspires to open stores in US airports in the near future.

Conclusion

The colossal size and high growth rate of the US luxury beauty and personal care market represents an attractive growth opportunity for European beauty brands. However, fierce competition, dissimilar channel dynamics and rapidly evolving consumer preferences are significant challenges through which European brands must navigate strategically. There is a compelling opportunity for European brands to leverage their rich experience to capture market share in specialty retail, a channel in which US consumers have demonstrated greater levels of sophistication and have higher expectations of beauty products. While opportunity abounds for European brands that wish to enter the US, it remains critical to identify appropriate and meaningful partnerships with local players to navigate the vast, complex and mature US market.

E Points of view from EY global sector and other industry professionals

The retail industry repositions from brick and mortar to e-commerce

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There is a shift occurring in America's shopping patterns and significant corresponding changes in the retail industry are also taking place.

As a key area of focus for the media, stock market analysts and consumers alike, the retail industry has seen increased levels of scrutiny and attention play out over the past few years. The world is watching as an inevitable shift occurs from brick-and-mortar retail toward e-commerce, with e-commerce continuing to command more and more of the overall retail sales market share. Retailers and brands must innovate and adapt to keep up with the changing times and the shift toward online sales. Brick-and-mortar locations will be forced to create a new luxury experience to survive and retain consumers and incentivize them to visit store locations instead of purchasing online.

As technology has evolved, consumers have adapted to the ease and convenience of shopping online. They can immediately locate and purchase the exact item that they are looking for online, compared with spending an afternoon in a mall and potentially coming home with additional items they did not initially want or need. Any items they desire are available at the click of their fingertips. This convenience has created a luxury that keeps consumers at home and at their computers when they are ready to shop, much more than ever before. As brick-and-mortar retail sales decline and online shopping takes their place, the industry will see a sizable shift.

Online shopping represents both a challenge and an opportunity for retail brands going forward. The rise of e-commerce sales began more than 20 years ago, following the creation of the internet, however, the past five years have given rise to a sharp increase in online sales, evidenced by the demands and desires of consumers.

The increase in online sales is undeniable, as evidenced by recent sales data. Although American department store revenues were down 7.2% as of December 2016, sales at all US retailers increased by 4.4%. Shopping is still very much taking place, just via a different method. In 1999, e-commerce sales accounted for 0.6% of all US retail sales. By the third quarter of 2016, this number grew to 8.4%. Total retail online sales worldwide were approximately $22 trillion in 2016, an increase of 6% from 2015. It is estimated that online sales will continue double-digit growth in the coming years and sales will reach $27 trillion dollars and more than 14% of total spending by 2020. A large bulk of worldwide e-commerce is expected to come from China, accounting for approximately 47% of global online sales worldwide in 2016. This is followed by North America, with online retail sales increases of 15.6% in 2016 compared with 2015.

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These changes are reflected in the US labor market as well. Since 2000, employment at traditional, non-discount department stores has decreased by 45%, while the number of e-commerce jobs has more than tripled. The shift from brick-and-mortar retail sales to online shopping ultimately will impact real estate as well. As brick-and-mortar locations decrease, consolidate and close, distribution warehouses outside of cities and metropolitan statistical areas increase to house and ship the goods.

For luxury brands that historically have not sold items online, e-commerce is viewed as the next opportunity to grow in Chinese markets.

Initially, many luxury brands have been hesitant to adapt to changing times and move online due to a desire and strategy of preserving and enhancing in-store experiences instead of maximizing sales. Many luxury brands view a strong, inaccessible, non-diluted brand associated with luxury, style and excellence more highly than increasing the topline. Since 2015, luxury brands that typically have maintained an image of inaccessibility, have begun to adapt to the changing times and move into the e-commerce space.

When Chanel took this plunge it was shocking to the retail world because Chanel always maintained a brand image that must be experienced in person. This was followed by announcements from Fendi and Tom Ford that they, too, would join the world of e-commerce. Brands are beginning to realize that by adding e-commerce, they provide opportunities for both the in-store experiences and increased sales online.

Although some luxury brands have remained cautious to enter the world of e-commerce, such as LVMH-owned Céline, some have embraced it. Michael Kors began serious initiatives to implement and grow online sales in 2014, resulting in 73% online sales growth in the third quarter of 2014. Michael Kors was also early to start promoting products via Instagram. Burberry also has been a leader in digital innovation, making all product offerings available for online purchase early in the game. Early on, Burberry sought to implement luxury in a digital context. Hermès has used online shopping as an opportunity to create an interactive experience, including the House of Scarves element, showcasing their most famous product.

It is essential now, and will continue to be essential going forward, that luxury brands adapt to e-commerce and view it as an opportunity by creating an online luxury experience and investing in the people and technology to successfully implement an e-commerce strategy, such as implementation of omnichannel retailing. In 2016, Neiman Marcus shifted to an omnichannel strategy and many other retailers are doing the same. Retailers currently are in the stage of experimenting with different online strategies and figuring out what will work for their brand. Those that successfully implement these strategies will be able to increase their revenue and potentially their exposure by reaching consumers on a greater number of platforms.

Although the media actively are covering the numerous retail store closures, specifically department stores, throughout the United States, many of these stores historically have had weak results. This could in fact be a good thing for the brands as they let go of the least profitable locations to cut costs and focus resources on the more successful locations and creating a powerful online presence.

More than 3,300 store closings have been announced for 2017. Michael Kors announced in May 2017 that it will close 100 to 125 of its 614 full-priced retail stores during the next two years, at a cost of approximately $125 million. To counter the closures and associated expenses, the company plans to raise prices by 10% over time. However, the company believes the store closures will produce $60 million in annual savings and, ultimately, increase sales. Sports Authority has closed 140 stores so far in the United States and plans to continue closing more. Further brands such as Gap, Barnes & Noble, Office Depot, Walgreens, American Eagle Outfitters, Aeropostale, Khol's, Macy's and Walmart have announced plans to close stores, or are in process of

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closing stores, throughout the United States.

Although frequent retail store closures make for catchy headlines in the media, the fact is that in many cases these stores are not profitable and closures will result in increased savings and efficiencies for the corresponding companies. America's retail square footage per capita is overextended compared with other nations. The United States has more than six times the square footage per capita compared with the United Kingdom. That's approximately 40 square feet of retail space per person in America, the largest ratio in the world. Further, the top eight markets in the United States comprise more than 30% of the retail space in the country, thus making those markets the most vulnerable. The decrease of brick-and-mortar space will result in significant cost savings for brands that can save on commercial leasing rent expenses, as well as in other areas, which can be utilized for more profitable stores or e-commerce initiatives. The current shrinkage of United States retail square footage per capita is a necessary adjustment needed in the market.

For existing brick and mortar survival and for upcoming new retail developments to thrive, the key is about creating an experience for the consumer. To succeed, retail locations must implement aspects into brick and mortar that create an activity instead of merely a location to make purchases. This will be a key differentiating aspect of enticing consumers to make purchases in person instead of online.

For example, when the Dallas, Texas-based luxury fashion namesake Forty Five Ten expanded into a new development in downtown Dallas across the street from the original Neiman Marcus, they mixed up the usual retail model. Forty Five Ten opted to create a lounge-like feeling where shoppers would want to spend their day, with aspects such as personal electronics charging stations, lounge seating, refreshments, a full restaurant, a champagne bar and more. The shift will occur from selling things to selling experiences. Some retailers, such as Story, located in the Meatpacking District of New York City, offer yoga and meditation classes inside their stores, sponsored by different health- and wellness-focused vendors. Coffee bars and full beverage bars are common as well. New York City retailer Fair Folks & a Goat offers a $35-per-month membership for unlimited coffee and espresso in its store.

Apple historically has been a leader in this space. Apple's products can be purchased at a variety of other retailers, such as Amazon and Best Buy, and on their own website; however, Apple has created an in-person experience that draws consumers into the stores.

The strategy is shifting from big box and cookie-cutter retail locations to shopping specifically tailored to a certain brand or urban location, targeting more than just luxury shoppers. There always will be those shoppers who want to try items in person before purchasing, or want to spend a day at a unique shopping center. It will be up to the retailers, brands and malls of the world to attract these brick-and-mortar shoppers with enhanced shopping experiences that become activities in and of themselves.

The key takeaway from this theme of the retail industry is that sales are not declining, they are merely shifting from a brick-and-mortar presence to online. Consumers prefer shopping from the comfort of their own homes, unless going in person to the store offers a unique and entertaining experience. Brick-and-mortar shopping will never cease to exist, it will evolve into more sophisticated platforms and it will decrease in volume and square footage to make way for the global shift to online shopping.

F | Points of view from EY global sector and other industry professionals

Achieving customer centricity through digital transformation

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It was a difficult year for the fashion and luxury industry in 2016, characterized by a general slowdown in growth and margins reduction.

In all market segments, product categories and geographic areas, the industry was troubled by uncertainties in the global macroeconomic and geopolitical sphere, changes in consumer behavior and pressures to produce more with less; there is less time, less money and fewer resources.

In short, companies have to face a turbulent, uncertain and mutilated environment in which the consumer is increasingly sophisticated, unpredictable and technologically savvy.

- Consumers are more demanding; they look for product and service customization without boundaries between online and offline channels. Today, the customer journey moves repeatedly between the online channel (web, social and e-commerce) and offline ones (stores), and companies face the need to integrate and balance all channels.
- They are better informed, by searching information online, even when inside the store. They visit e-commerce sites and continuously monitor discounts and promotions on the web.
- They fundamentally are more aware and looking for value and authenticity. The internet has brought them transparency, not only for prices.
- They join communities and are, therefore, constantly connected to other consumers, and publish and read feedback and reviews on blogs and social networks.
- They always are connected, busy and without fixed schedules; they buy throughout the entire 24-hour horizon.
- At the same time, they are more fickle, changing ideas very easily and with alternative shopping options a click away. Beyond the growth of e-commerce, it is estimated that more than 60% of sales in the industry are influenced by digital.
- They seek new interaction experiences with the brand and the playful element of the buying process is becoming more important. An example is virtual reality (VR), which is entering the fashion world with a leading role: 13 catwalks were featured in VR during the 2016 New York Fashion Week. In addition, some brands, such as Dior and Tommy Hilfiger, are using VR in their stores to effectively communicate the "identity" of their brand.

Consequently, to operate successfully in this context, it is more important than ever to put the "consumer in the center," to understand them, to study their online and offline behaviors, and to achieve this, a truly digital transformation of the business is needed.

The stated objective of fashion and luxury companies

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is to know the customer deeply, not only by their personalities but also through their buying habits, propensity to use the technology, experiences, and presence on social networks and the internet.

The digital transformation that companies face is a complex challenge that requires a long-term vision.

Vision is culture.

Culture is a strategic project, a non-tactical common thread.

These days, we notice how many companies use technology without having a clear vision, often generating great confusion. Often large projects that are very expensive are launched in an unorganized way, and thus do not lead to the company's goal.

Digital transformation is, therefore, necessary and covers all of a company's areas: starting from its core business and to the point of actively involving other divisions, such as customer relationship management (CRM), information technology (IT) and digital.

It is particularly relevant to understand to which point the big players in the sector have arrived in the implementation of their "digital agenda." According to the Digital IQ Index 2016, which evaluates the digital skills of 85 brands in the fashion and luxury sector every year, only Kering – including the Gucci brand – and Burberry managed fully and effectively to use digital as a differentiator in the competitive dynamics. Another 23 brands – including Coach, Ralph Lauren, Tory Burch, Kate Spade, Michael Kors, Louis Vuitton, Tommy Hilfiger and Cole Haan – are experimenting and innovating in mobile and social networks with a consistent digital presence. For the other 62 brands, however, there still is a lot of room for improvement in their digital transformation to put the consumer at the "center."

In our experience, there are three priorities for this digital agenda.

1. **CRM** is a model of processes and systems for collecting and managing customer and prospect data. It is aimed toward optimally managing the relationship between customer and prospect data and the brand in the optics of development, marketing and sales service. However, the human element (customer) that CRM impacts significantly should remain a primary consideration.
2. **Digital marketing**, that is, a strategy for optimizing communication and engagement with customers, increasingly is driven toward the so-called "one-to-one" personalization of content.
3. **Omnichannel** is the strategic integration of online and offline channels at the level of people, processes and information systems to optimize sales opportunities. Omnichannel strategy allows companies to improve their customers' knowledge and increase sales by integrating data from different touch points and managing the online channel and social networks internally.

To better interpret and frame the possible digital excellence paths of these three priorities, EY has developed a digital positioning matrix (see Figure 1) that links the knowledge of the final customer and the level of digitalization of the transaction.

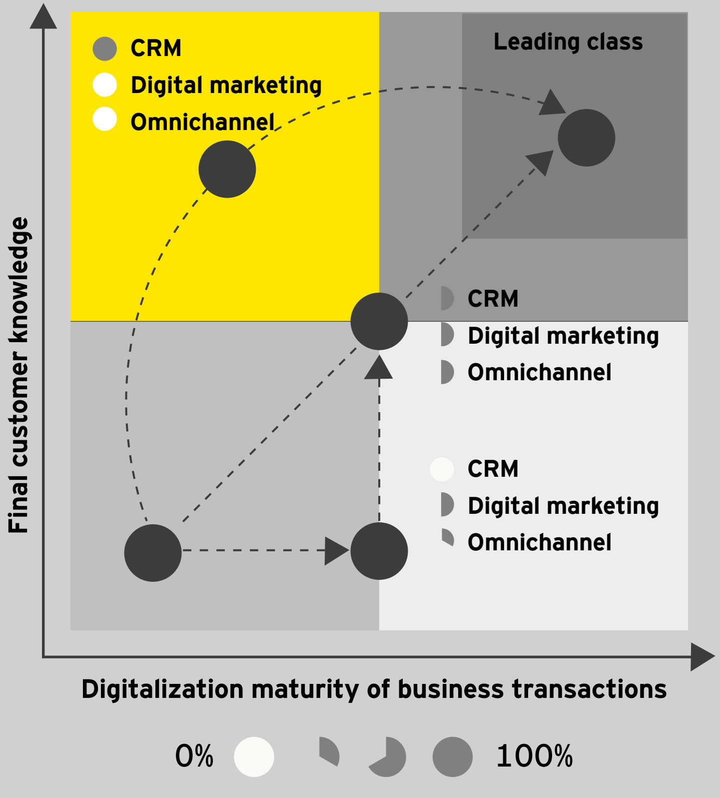

Figure 1 – The digital positioning matrix developed by EY.

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On the X axis of the matrix is the maturity of the digitalization of the transaction, showing how the company has evolved digitally.

- E-commerce owner vs. outsourcing
- Social network integration and managed altogether
- Management of prospects (potential reachable customers yet to make a purchase)
- Management of unknown (potential customers expressing interest in the brand on social networks, but without any contact points)
- Advanced business intelligence about online buying and browsing behaviors

And on the Y axis, you can see customers' detailed knowledge. (It ranges from almost casual, everyday in-store customer management to highly detailed and integrated customer loyalty cards from different channels.)

As can be seen in the matrix, for companies, there is more than one path that can be implemented to aim for excellence and ranking among the leading class; the roads are multiple and depend on the brand's initial positioning.

Defining and implementing an effective CRM strategy is the first step, and it's important because it helps promote the next steps of the process, the digital transformation happening in this industry. In fact, knowledge about the final customer and its management in a single database (with the consequential possibility of segmenting and clustering) are also key elements of adopting an omnichannel strategy and customizing digital marketing content.

Companies operating in the fashion and luxury sector are moving on two directives: some work mainly using the knowledge of the final customer, starting from the customer cards, which, in addition to the records, also gather a customer's behavioral features, while others move toward digitization by providing new ways of digital interaction (chat, web, mobile, social, etc.), integrating, more or less strategically, new channels.

There is a lot of talk about "omnichannel management," but this is not possible without a true digital transformation, which, by definition, must start from the knowledge about the customer.

Focus on CRM, therefore, as the starting point of digital transformation!

CRM often is referred to as software. Actually, it is not a product nor an application, but a business strategy whose purpose is knowledge of the final customer and building long-term, personalized and loyal relationships.

An effective CRM strategy can enable a virtuous and customized *customer experience* on all channels and offers economic and brand awareness benefits.

- ***Sales increase from loyal customers***
  - A loyal consumer spends about 40% more than an occasional consumer in one year. Companies with a good *customer experience* have a customer dropout rate of less than 18% and an upselling and cross-selling index more than 15%.
  - An increase in the sell-through of full-price products is due to more effective customer segmentation.
- ***Customer insights benefit the entire value chain***
  - CRM insights tend to be more integrated with merchandising processes and activities, management and development of a network of stores, and with commercial forecasting and budgeting.
  - There is a cost-to-serve reduction and increase in the efficiency of delivering the service through an appropriate service-level differentiation.
- ***Marketing investments optimization***
  - Both in the traditional and digital channels with a one-to-one optic, companies that have targeted marketing and communication investments for specific customer clusters have achieved a much

Achieving customer centricity through digital transformation

Figure 2 – An example of an effective CRM model

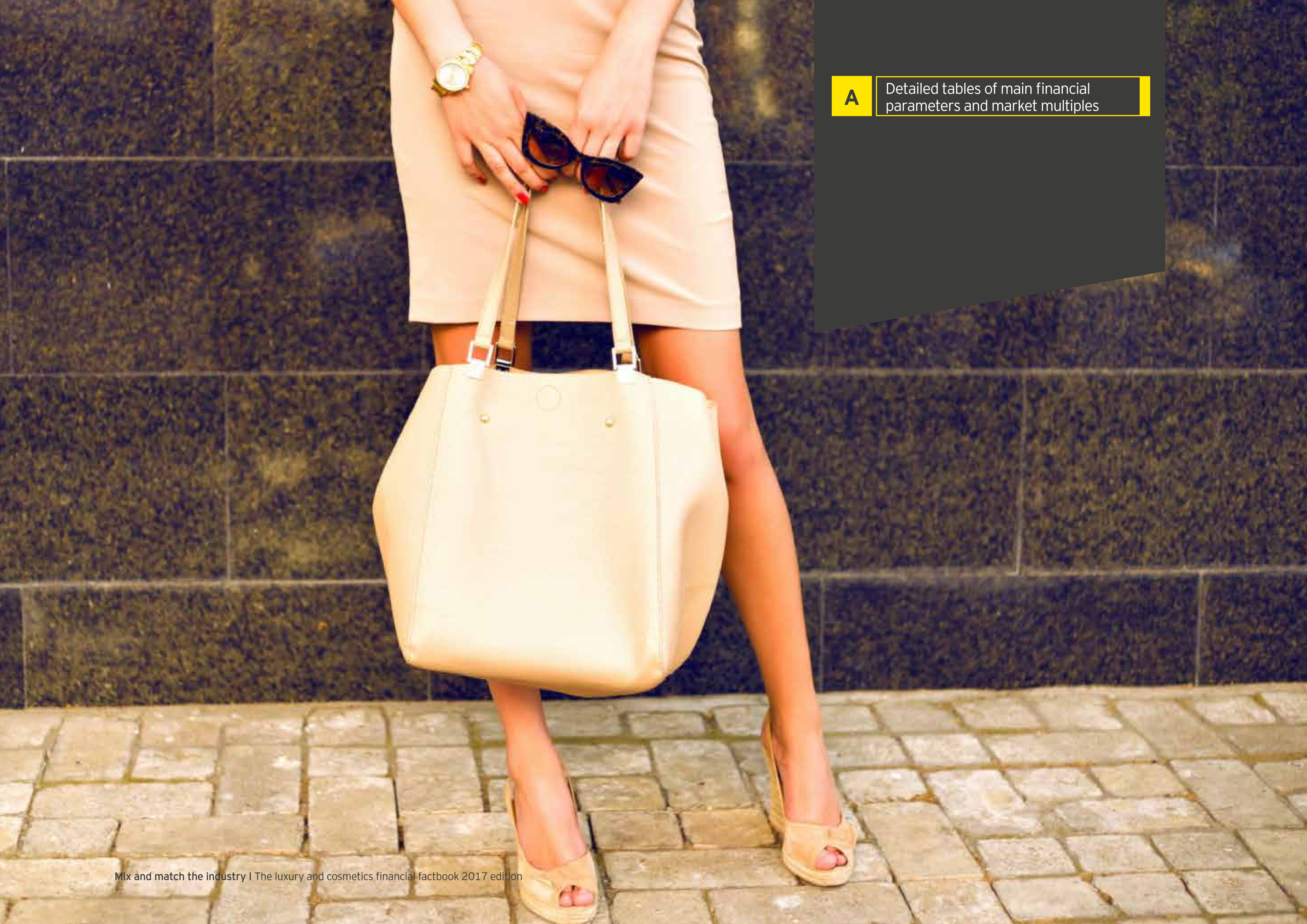
greater return on investment.

- ***Increase in corporate value***
  - CRM and customer intelligence investments affect equity.
  - Financial analysts state that companies that invest in CRM have a lower trade risk (~ 0.5 to 1 point more of the multiplier of the earnings before interest, taxes, depreciation and amortization).
- ***Essential tool for compliance with the new European general data protection regulation.*** It is known that by May 25, 2018, companies will have to comply with the new European Personal Data Protection Directive, active since May 24, 2016. The management of a single customer database, a single view of the same customer, and the correct management of opt-in and opt-out rules is crucial for compliance with the privacy law.

Implementing an effective CRM model requires not only investment in technology resources, but involves an effort to define the data model and business processes to support the brand's goals, in addition to an important investment in human capital (in fashion and luxury companies, professional specialists more and more are being requested and, often, they come from other sectors).

To conclude, an effective CRM model (see Figure 2) is a real and proper Copernican Revolution that puts the consumer at the center. Only through the introduction of a CRM can a fashion and luxury company finally become customer centric. Then it can continue on the road to digital transformation to sort out all of today's and tomorrow's challenges in an increasingly complex context, but one rich with future opportunities.

Appendix



A Detailed tables of main financial parameters and market multiples

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)	2016A/E	2017F	2018F	2019F
Jimmy Choo	0.4	0.5	0.5	0.5
Brunello Cucinelli	0.5	0.5	0.6	n/a
Tod's	1.0	1.1	1.1	1.1
Moncler	1.0	1.2	1.3	1.4
Safilo	1.3	1.2	1.2	1.3
Ferragamo	1.4	1.5	1.6	1.7
Hengdeli	1.5	1.6	1.6	n/a
YNAP	1.9	2.2	2.6	3.0
Hugo Boss	2.7	2.7	2.8	2.9
Prada	3.2	3.3	3.5	3.6
Burberry	3.2	3.5	3.6	3.7
Tiffany	3.7	3.8	4.0	4.2
Michael Kors	4.2	4.1	4.0	4.1
Coach	4.2	4.2	4.4	4.6
Hermès	5.2	5.6	6.1	6.7
Chow Tai Fook	6.2	6.1	6.3	n/a
Ralph Lauren	6.2	5.7	5.7	5.9
Swatch	7.1	7.5	7.8	8.2
Luxottica	9.1	9.7	10.1	10.6
Richemont	10.6	11.3	11.8	12.2
Kering	12.4	13.6	14.4	15.2
LVMH	37.6	40.7	42.9	45.3
Total	124.5	131.5	137.9	136.3

EBITDA margin	2016A/E	2017F	2018F	2019F
Hengdeli	5.5%	7.2%	7.4%	n/a
Safilo	6.6%	4.3%	5.9%	7.3%
YNAP	7.7%	8.4%	9.4%	9.9%
Chow Tai Fook	10.8%	11.1%	12.2%	n/a
Ralph Lauren	11.8%	14.6%	15.1%	16.2%
Jimmy Choo	16.2%	16.8%	17.3%	18.0%
Swatch	16.4%	18.5%	19.7%	20.7%
Brunello Cucinelli	17.2%	17.1%	17.3%	n/a
Tod's	18.0%	17.8%	18.3%	18.7%
Hugo Boss	18.5%	17.9%	18.3%	18.6%
Kering	18.7%	19.2%	20.0%	20.8%
Prada	20.5%	22.4%	23.6%	23.4%
Burberry	22.1%	21.5%	22.7%	23.4%
Luxottica	21.4%	21.2%	21.7%	22.1%
Coach	22.0%	23.5%	24.8%	26.0%
Ferragamo	22.7%	22.8%	23.3%	23.3%
LVMH	23.0%	23.8%	24.4%	24.7%
Richemont	23.2%	22.4%	23.5%	24.8%
Tiffany	24.2%	24.4%	24.9%	25.9%
Michael Kors	24.7%	23.6%	20.4%	20.9%
Moncler	34.1%	33.3%	33.1%	32.5%
Hermès	37.0%	36.3%	36.7%	38.2%
Average	19.2%	19.4%	20.0%	21.9%

Cosmetics

Sales (€ b)	2016A/E	2017F	2018F	2019F
L'Occitane	1.3	1.3	1.4	1.5
Nu Skin	1.9	2.0	2.1	2.1
Natura	2.3	2.5	2.8	3.0
Coty	3.8	6.6	7.7	7.7
Amorepacific	4.3	4.8	5.6	5.7
Beiersdorf	6.8	7.1	7.4	7.7
Shiseido	7.1	7.9	8.2	8.4
Estée Lauder	10.5	11.0	11.7	12.4
L'Oréal	25.8	27.9	29.3	30.8
Total	64.0	71.2	76.2	79.6

EBITDA margin	2016A/E	2017F	2018F	2019F
Shiseido	8.4%	9.6%	10.6%	11.0%
Nu Skin	13.7%	15.1%	15.4%	16.5%
Coty	16.7%	n/a	n/a	n/a
Natura	17.0%	17.1%	17.9%	18.3%
Beiersdorf	17.2%	17.7%	18.2%	18.7%
L'Occitane	18.0%	16.6%	17.5%	18.2%
Amorepacific	18.2%	19.4%	18.8%	18.9%
Estée Lauder	19.2%	19.3%	19.8%	20.2%
L'Oréal	23.1%	22.3%	22.5%	22.6%
Average	16.8%	17.1%	17.6%	18.1%

Detailed tables of main financial parameters and market multiples

Luxury and cosmetics multiple analysis

	EV/Sales			EV/EBITDA			Price to earnings		
Trading multiples	2017E	2018E	2019E	2017E	2018E	2019E	2017E	2018E	2019E
LVMH	2.6x	2.5x	2.3x	10.9x	10.1x	9.5x	21.4x	19.4x	18.0x
Richemont	3.1x	3.0x	2.9x	13.9x	12.6x	11.5x	25.6x	22.9x	20.4x
Swatch	2.2x	2.1x	2.0x	11.7x	10.4x	9.5x	23.7x	20.4x	18.2x
Hermès	7.6x	7.1x	6.4x	21.0x	19.3x	17.3x	37.3x	34.1x	29.5x
Kering	2.6x	2.4x	2.3x	13.4x	12.1x	11.1x	19.9x	17.7x	16.0x
Coach	2.2x	2.1x	2.0x	9.2x	8.4x	7.6x	18.3x	16.3x	14.8x
Luxottica	2.6x	2.5x	2.4x	12.4x	11.6x	10.9x	25.9x	23.8x	22.0x
Ralph Lauren	1.0x	1.0x	0.9x	6.6x	6.4x	5.7x	15.8x	14.9x	12.9x
Tiffany	2.9x	2.8x	2.7x	11.9x	11.2x	10.3x	23.3x	21.5x	19.6x
Burberry Group	2.4x	2.3x	2.2x	11.1x	10.1x	9.7x	21.3x	18.9x	17.3x
Hugo Boss	1.8x	1.7x	1.6x	9.8x	9.3x	8.8x	19.6x	17.9x	16.6x
Safilo Group	0.4x	0.4x	0.4x	10.8x	6.9x	5.3x	n/a	n/a	n/a
Tod's	2.2x	2.2x	2.1x	12.6x	11.9x	11.2x	24.0x	22.3x	20.8x
Prada	2.9x	2.8x	2.7x	13.2x	11.9x	11.6x	28.0x	24.6x	22.8x
Salvatore Ferragamo	3.2x	3.0x	2.9x	13.9x	13.0x	12.4x	22.6x	20.9x	19.7x
Brunello Cucinelli	3.0x	2.7x	n/a	17.6x	15.9x	n/a	34.2x	30.2x	N/A
Michael Kors	1.3x	1.4x	1.3x	5.7x	6.9x	6.4x	10.0x	10.6x	10.2x
Hengdeli	0.7x	0.7x	n/a	9.5x	8.8x	n/a	23.4x	20.3x	n/a
Chow Tai Fook	1.6x	1.5x	n/a	14.3x	12.7x	n/a	21.6x	18.3x	n/a
Moncler	4.2x	3.8x	3.5x	12.6x	11.5x	10.8x	21.3x	19.5x	17.9x
Jimmy Choo	1.9x	1.7x	1.6x	11.2x	10.1x	9.1x	20.5x	18.6x	16.5x
YNAP	1.4x	1.1x	1.0x	16.1x	12.3x	10.0x	48.0x	35.4x	27.7x
Average	2.4x	2.3x	2.3x	12.2x	11.1x	9.9x	24.1x	21.4x	18.9x

	EV/Sales			EV/EBITDA			Price to earnings		
Trading multiples	2017E	2018E	2019E	2017E	2018E	2019E	2017E	2018E	2019E
L'Oréal	3.5x	3.4x	3.2x	15.9x	15.0x	14.2x	24.8x	23.1x	21.6x
Estée Lauder	2.9x	2.7x	2.5x	15.0x	13.7x	12.6x	25.4x	23.1x	21.0x
Beiersdorf	2.6x	2.5x	2.4x	14.9x	13.9x	13.0x	25.9x	23.9x	22.3x
Natura	2.1x	1.9x	1.7x	12.4x	10.6x	9.5x	22.4x	17.7x	15.0x
Shiseido	1.4x	1.3x	1.3x	14.5x	12.7x	12.0x	42.9x	34.0x	30.5x
L'Occitane	1.8x	1.7x	1.6x	11.1x	10.0x	9.0x	22.2x	20.4x	18.2x
Coty	2.7x	2.3x	2.3x	15.2x	11.5x	10.0x	37.4x	19.8x	15.8x
Amore pacific	2.8x	2.4x	2.4x	14.8x	13.1x	12.5x	25.3x	21.5x	20.1x
Nu Skin	1.2x	1.2x	1.2x	8.2x	7.7x	7.1x	16.1x	15.3x	n/a
Average	2.4x	2.2x	2.1x	13.6x	12.0x	11.1x	26.9x	22.1x	20.6x

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