

Mu Capital Group



[16/09/2021]

MC.PA

Price (15/09/21)	€625.50
Market Cap (bn)	€315.7
EV (bn)	€362.3
Beta (5Y monthly)	0.92

Luxury Goods

Mean Price Target	€726.76
% Upside	16.2%

24m performance:



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Market Data:

52- Week Range	€390.70 - €716.60
Shares Out. (bn)	0.504
P/E (ttm)	33.4
PEG (5-yr expected)	[0.0]
EPS (ttm)	[18.77]
EPS growth	[0.0]%
Div./Yield	[\$7.00]/[1.13]%
Payout ratio	[31.97]%

Profitability:

Profit margin	[17.24]%
Op margin	[25.95]%
ROA (ttm)	[8.09]%
ROE (ttm)	[24.92]%

Financial Data:

Revenue (bn)	[54.92]
Revenue growth	[55.8]%
EBITDA (bn)	[16.04]
EBITDA growth	[0.0]%
EBITDA margin	[0.0]%

Leverage:

Net debt (bn)	[38.55]
Total debt/equity	[90.44]x
Current ratio	[1.10]
Cash ratio	[0.0]

LVMH

A diversified luxury offering and strong financial position makes LVMH an interesting opportunity towards the tail-end of the pandemic.

COMPANY OVERVIEW

LVMH, which stands for Louis Vuitton Moët Hennessy, is a French holding multinational corporation specialising in luxury goods. It controls 75 brands across spaces such as wine & spirits, fashion, cosmetics, jewellery, retailing with notable names such as Dom Perignon, Christian Dior, Benefit Cosmetics, TAG Heuer and Sephora. Such a wide array of products allows LVMH to supply consumers with all aspects of their luxury needs.

LVMH targets individuals with all magnitudes of disposable income, with products ranging from makeup the tens to superyachts in the tens of millions of euros. Many of its brand's products sit in the range of hundreds or thousands of euros, with a large portion of its consumer base being the upper and aspiring upper-middle classes. Items such as Louis Vuitton bags, Tiffany necklaces and Moët champagne are all symbols of wealth and prosperity, which is part of the appeal of many LVMH products – the people buying these products are buying the lifestyle they represent.

The company recorded a revenue of €44.7bn in 2020 which was spread across its different business groups and operating regions. Overall, the company's most important business was its fashion which drew in 47% of global revenue, whilst the most important region was Asia, which accounted for 34% of global revenue. Something interesting to note is the performance of different businesses in different regions. For instance, although fashion is the largest revenue draw globally, it is only makes up 33% of revenue in LVMH's home market of France, whereas it is 69% of Japanese revenue. Such large variances speak to the diversification of LVMH's offering, as whilst sectors may perform differently generally, they are not dependant on any single business subsidiary or region for their revenue. A more granular breakdown of total 2020 revenue can be seen below, broken down by region (fig. 1) and business area (fig. 2).

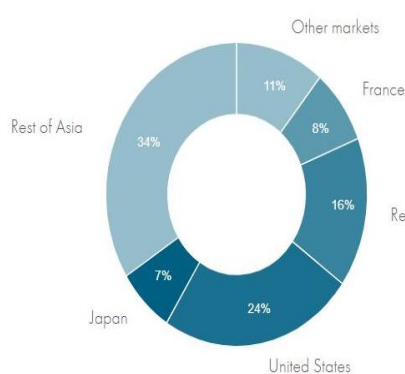


fig. 1

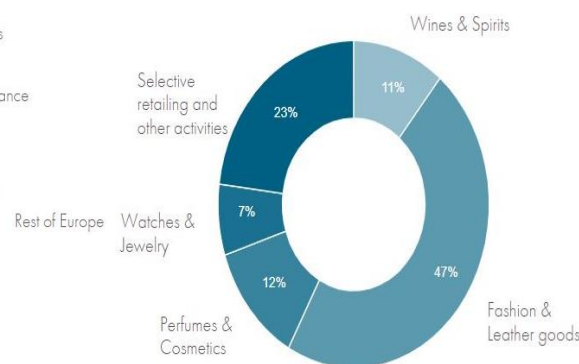


fig. 2

INVESTMENT RATIONALE

Data from the Office for National Statistics shows that spending of disposable income decreased most amongst high income individuals during the pandemic, with the highest quintile's spending decreasing by 20.6%. As this encapsulates the majority of LVMH's consumers, we can see this directly correlates with the 16.8% decrease in revenue the company saw between 2019 and 2020. As we move towards the end of the pandemic, we can expect that this spending will return to its previous levels, which is something we're already seeing with the company's half 1 report showing revenue is up 56% on the same period last year and organic revenue growth accelerating from 8% in Q1 '21 to 14% in Q2 '21.

Although LVMH has already had very strong growth in 2021, the price has dropped significantly since its €716.60 peak in July. The primary driver for this is several comments by the Chinese government regarding "adjusting excessive income" in the country, as well as markets being down in general as of late. Nothing solid has come of these comments yet, so now this appears to be merely spooked investors selling. More so than any implementation of a tax plan a larger risk would be a wholesale behavioural change in the Chinese market, but such a change would take time to occur assuming these comments amount to anything. This is a perfect time to buy LVMH, as there is still upside to be captured as freedoms return and spending continues to increase.

MARKET POSITION

LVMH operates across many different facets of the luxury goods market, with businesses in alcohol, fashion, cosmetics, and jewellery. The global luxury goods market was valued at \$224.8bn in 2020 and is expected to grow at a CAGR of 4.8% to reach \$296.9bn by 2026, according to Global Industry Analysts. In terms of specific businesses, the luxury fashion, cosmetics, and jewellery markets are expected to grow at CAGRs of 6.2%, 5.1% and 3.8% respectively over the same period. As the luxury goods market is dependent on the level of disposable income available to the higher income individuals it is positively correlated with the performance of the general economy. This means that in the short term we can expect growth to be catalysed in the short term by the return to typical full-time employment for many, whilst longer term areas such as ecommerce and developing markets are expected to sustain this growth.

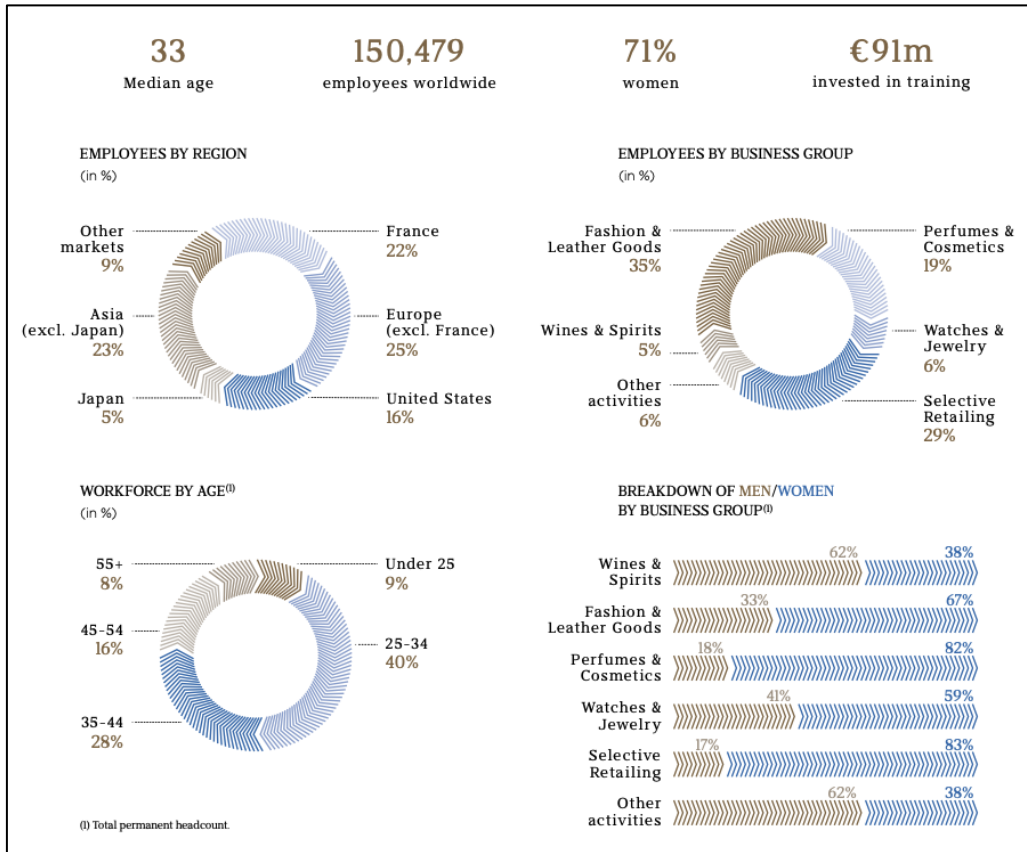
By having such a diverse portfolio of businesses, LVMH sits in a unique position within the luxury goods market. Its competitors fall into two different categories: those who are quite competitive within one business but lack diversification (e.g. Burberry, Kering and Estee Lauder) and those who have diversified but do not compete with in terms of scale (e.g. Ralph Lauren, Chanel and Hermes). What this means is that, although LVMH only has a 16% share of the total luxury goods market according to Jefferies, they are competitive amongst all the businesses within the market in a way that no other company is.

Something important to note is that despite sales and revenues being down over the COVID-19 pandemic, LVMH's market share increased from 9% to 16%, helped in part by the successful acquisition of the American jeweller and retailer Tiffany. This follows the market trend of top brands within the luxury goods market taking market share from smaller competitors as they find it more difficult to compete online, leading to mergers and acquisitions.

MANAGEMENT STRUCTURE

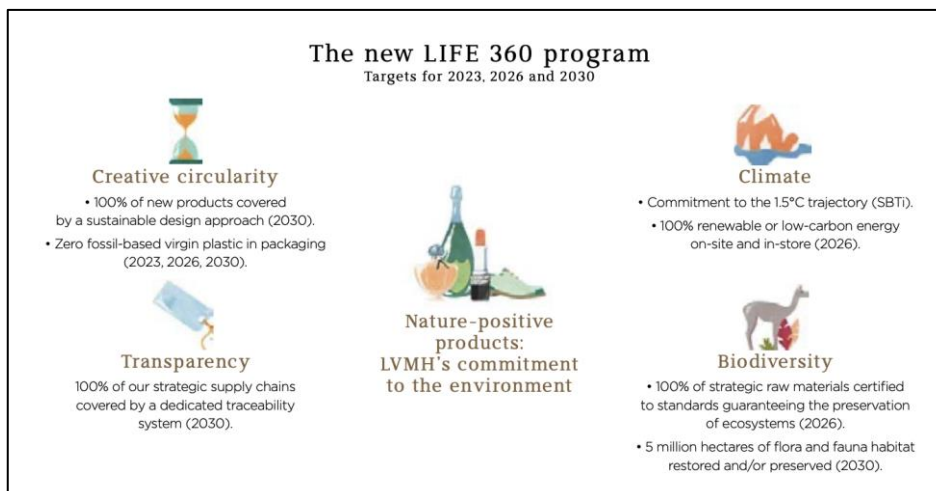
The group is organised into the Executive Committee and the Board of Directors. Bernard Arnault became Chairman and CEO of LVMH Moët Hennessy Louis Vuitton in 1989, after becoming the majority shareholder. He is also President of the Board of Directors of Groupe Arnault S.E. (his family holding group). Four of his five children all have official roles in brands controlled by Arnault, along with his niece. For example, his daughter Delphine has served as Executive Vice President of Louis Vuitton since 2013. The rest of the executive team are sufficiently experienced, with an average tenure of 13.2 years.

The image below outlines information about the employees of the group.



INTEGRITY AND ESG ANALYSIS

The company hasn't been subject to any major legal issues in recent times with a penalty total since 2000 of \$9,097,052, the majority of which is related to minor employment-related offences. Despite this, 89% of employees who answered the LVMH Global Pulse Survey commended the way the group responded to the covid-19 crisis. 93% said they were proud to belong to the Group and work for their maison. The company have made serious environmental commitments outlined below, and have an ESG risk rating of 'low' on Yahoo Finance.



OPPORTUNITIES FOR GROWTH

There are three primary drivers for growth for LVHM, and the luxury goods market overall. The first is the end of the COVID-19 pandemic. As previously discussed, the upper class making up most of the market's consumer base saw the largest drop in disposable income, so as those individuals recover their previous income levels towards the end of the pandemic, we can expect sales to increase. This is something we can already see in the first half of this year, with revenues being up 53% on the same period last year. The company's HI noted that although the US and Asian markets are up significantly, the European market was recovering more gradually, meaning that there is still growth to come in a major region for the company.

The second growth driver is the company's use of ecommerce. Whilst brick and mortar stores still have their place, and perhaps more so within luxury and experience-based markets, the world as a whole continues to shift towards an online marketplace. Many smaller and independent brands were slower to make this change and as a result are now finding it difficult to compete online with companies that have the resources and brand synergies that LVHM do. This has been the biggest factor in the recent increase in LVHM's market share, as this battle for online business has led to many acquisitions across the market which have consolidated the larger companies' positions.

The final, and perhaps most important, area of potential growth is the Chinese market. China made up 38% of LVHM's HI revenue and has been growing rapidly with a 30% revenue increase since the same period in 2019. China also exhibit the highest CAGR of any region at 6.7% between 2020 and 2026. China also has 400 million millennials, who are a growing consumer base as they age, which is 5 times larger than that of the US market which is the largest currently.

KEY RISKS

The largest risk to LVHM currently is the economic and political uncertainty in China. Xi Jinping's calls for wealth distribution in August spooked the market, although they have stabilised for the moment. In a worst-case scenario, where consumer tastes change in the Chinese market and new taxes on luxury goods are introduced, then LVHM would not be able to support its current valuation, as China is the largest growth sector for the company. However, there are several factors that could mitigate this - firstly it's entirely possible that these rather vague comments won't amount to anything of note. If they, the way it was talked about was to give more chances for people to become wealthy, which would then increase the size of the middle class which could create a tailwind for LVMH, which could offset decreased spending by the upper class. Another point is that 47% luxury goods are purchased by global tourists, so we could see a shift towards Chinese consumers buying overseas.

FINANCIAL EVALUATION



Financial Summary						
	2016	2017	2018	2019	2020	Sum of Previous 4 Quarters
Revenue	37,600	42,636	46,826	53,670	44,651	101,904
growth		13.39%	9.83%	14.62%	-16.80%	128.22%
EBITDA	8,615	10,086	11,919	15,936	13,086	31,803
growth		17.07%	18.17%	33.70%	-17.88%	143.03%
margin	22.91%	23.66%	25.45%	29.69%	29.31%	31.21%
EBIT	6,999	8,269	9,961	11,455	8,325	22,159
growth		18.15%	20.46%	15.00%	-27.32%	166.17%
margin	18.61%	19.39%	21.27%	21.34%	18.64%	21.74%
FCF	4,095	4,640	5,367	8,734	8,870	21,405
growth		13.31%	15.67%	62.74%	1.56%	141.32%
margin	65.57%	66.43%	63.08%	74.93%	81.31%	82.01%
Net Income	3,981	5,365	6,354	7,171	4,702	13,894
growth		34.77%	18.43%	12.86%	-34.43%	195.49%
margin	10.59%	12.58%	13.57%	13.36%	10.53%	13.63%
EPS	7.88	10.64	12.61	14.23	9.33	
growth		35.03%	18.43%	12.86%	-34.43%	

Fiscal Year	2016	2017	2018	2019	2020	Current (Ex-Qs)
Profitability Ratios						
Return on Equity	14%	18%	19%	19%	12%	
Profit Margin	11%	13%	14%	13%	11%	
Asset Turnover	63%	61%	63%	56%	41%	
Profitability	11%	13%	14%	13%	11%	
Leverage	214%	230%	219%	252%	280%	
Liquidity Ratios						
Current Ratio	1.51	1.41	1.40	1.17	1.58	
Cash Ratio	0.31	0.28	0.31	0.28	0.82	
Debt Ratios						
Debt to Equity	114%	130%	119%	152%	180%	
Interest Coverage Ratio	67.88	41.33	53.85	26.13	29.81	
Interest Coverage Ratio Applicable?	YES	YES	YES	YES	YES	
Valuation Ratios						
Earnings Per Share	7.88	10.64	12.61	14.23	9.33	
Price to Earnings	-	-	-	-	-	34.35
PEG	-	-	-	-	-	3.12
PEG Including Dividends	-	-	-	-	-	2.92
FCF Per Share	8.11	9.21	10.65	17.33	17.60	-
Price to Free Cash Flow	-	-	-	-	36.75	36.75
Dividend Per Share	3.58	4.19	5.39	6.45	4.83	-
Dividend Yield	-	-	-	-	-	0.75%

Profitability & Past Performance

- Sustained increase in sales and net income from 2016 to 2019. Dip in 2020 explained by covid, recovery since then indicates return to pre-covid trend.
- Profit margin seems to be relatively stable at around 13%
- Return on equity follows the same trend as net income / sales, suggesting that prior to covid, assets were being used more and more effectively to generate profits. ROE for the last 12 months is 24.92%.

Liquidity

- Current Ratio is remains above 1, so the company is able to meet any short term obligations.
- Cash ratio is below one which is a slight concern. However, this has increased in 2020 and the company has demonstrated its ability to generate cash.

Debt

- Debt/Equity ratio is fairly high, however the company is sufficiently able to meet its interest payments, and has previously demonstrated its ability to generate profits from its assets.

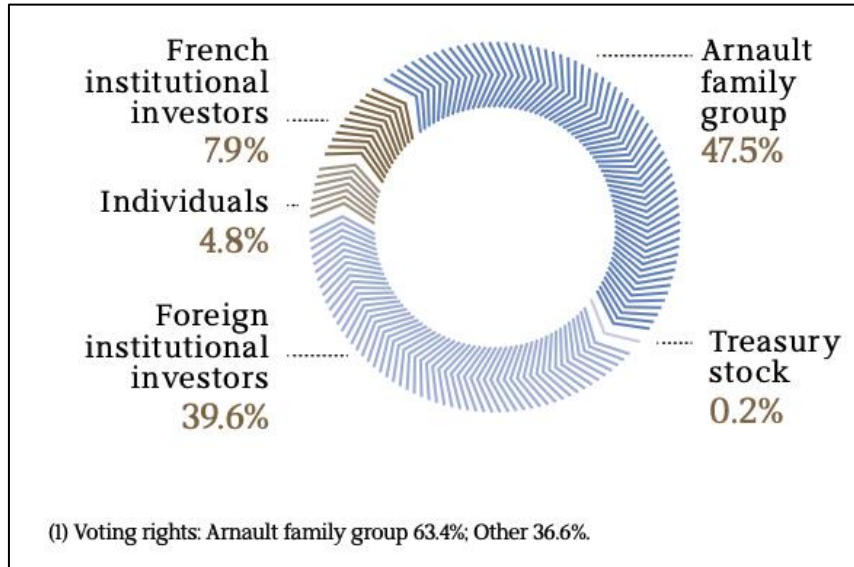
Valuation and Comparison Analysis

Company Name	Revenue	EBIT	(margin)	Net Income	(margin)	FCF Per Share	EPS	P/E	P/FCF	P/Sales	P/Book	P/EBITDA	EV/Rev	EV/EBITDA
Hermès	8137	3259	40%	2224	27%	12.65	2.50	60.05	99.9	19.48	19.59	37.24	19.18	43.97
Kering SA	15769	4420	28%	3357	21%	16.34	3.17	24.39	39.03	6.15	7.71	15.93	6.81	21.5
Compagnie Financiere Richemont SA	13144	1476	11%	1301	10%	5.93	0.27	41.26	17.01	4.84	3.6	23.88	5.07	30.69
Prada	2423	201	8%	-544	-22%	1.67	0.21	54.03	193.58	4.89	4.94	24.68	5.78	29.89
Mean	9868.25	2339	21.90%	1584.5	9.02%	9.1475	1.5375	44.9325	87.38	8.84	8.96	25.4325	9.21	31.5125
Median	10640.5	2367.5	19.63%	1762.5	15.59%	9.29	1.385	47.645	69.465	5.52	6.325	24.28	6.295	30.29
LVMH (EPA:MC)	54,922	14,301	26%	9,469	17%	17.61	18.77	34.46	36.72	5.93	7.91	20.32	6.66	22.79

- LVMH stands out amongst its competitors, beating the average for all factors considered in the comps analysis table.
- The PE ratio may seem high, however, it's lower than its competitors.
- The PEG may also seem high (3.12). However, it is important to consider that the PEG is based on previous growth rates. Past performance was hampered in 2020 as a result of the pandemic, this has a negative impact on the CAGR over the last 5 years. This makes the PEG artificially high as it doesn't reflect the growth seen before the pandemic, and the fast return to this trend.

SHAREHOLDER STRUCTURE

The image below shows the ownership structure of the company, a significant portion owned by the Arnault family and 47.61% in total owned by insiders. The family also have majority voting rights.



There are 503.61m shares outstanding, the float is 271.98m.