The Unusual Suspects - Fashion House Moncler Acquires Uprising Fashion Brand Stone Island in a €1.15B Deal.

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"For a long time, I have been looking around for a company that would allow me to create value for Moncler and that could accelerate our growth path. The first time I met Mr. Rivetti, I immediately realized that we share the same vision and that he was the right person to shape the future together." - Remo Ruffini, CEO Moncler

Deal Overview

- Acquirer: Moncler (MONC.MI)
- Target: Stone Island
- Industry: Luxury Fashion
- Transaction Amount: €1.15B
- Announcement Date: Dec. 07, 2020
- Target Advisor: Citigroup & Cornelli Gabelli

Every crisis presents an opportunity. This is just as true for industries that have been particularly affected by the Covid pandemic. Moncler, as one of the best-known fashion houses, has taken this saying particularly to heart. In a €1.15B deal, the company managed by Remo Ruffini acquired Sportswear Company S.p.A., better known as Stone Island. Ruffini, who holds a 27%-stake in Moncler, describes the deal as a get-together of two Italian families representing exceptionally strong brands for a joint project. In a combination of a maximum cash-out for Moncler and a share offer to the Rivetti family, the owners of Stone Island, the deal was closed back in December last year. With the first acquisition in the company's history, Moncler has added a strongly positioned, fast-growing brand to its portfolio.

Mr. Ruffini potentially has found a rough diamond. Above average performance and sustainable growth over the past decade have promoted Stone Island to the Champions League of fashion labels. Although expansion has been at halt last year, Stone Island appears to be well prepared for the coming continuation of its growth strategy. Standing at the beginning of an international expansion, they seem to resemble the Moncler of 10 years ago. Moncler will share its knowledge and experience with Stone Island to fully express its growth potential.

Companies Overview - Stone Island

Back in 1872, Guiseppe Rivetti founded his first wool factory producing functional wool garments, which later merged with the Turin-based group GFT. Two generations later Carlo Rivetti, who fully controlled Stone Island up to December 2019, initiated a radical change. After decades of fashion production, Rivetti felt like creating something more timeless: sportswear. He left GFT in 1993 to acquire 100% of C.P. Company, an innovative sportswear manufacturer. Stone Island was already a part of C.P. as a secondary line, founded 10 years earlier by Massimo Osti. This marked the beginning of a well-known success story. Launching their first flagship store in Milan in 1999 and their e-commerce platform in 2007 moved Stone Island closer to the center of attention.

Stone Island has often been profiting from demand in sub-cultures. The Paninaro youth was one of the first movements to recognize Stone Island as a desirable luxury good. The launch of their Shadow Project in 2011 and subsequent partnerships with two of the biggest streetwear brands, Supreme and Nike, explain much of their current success. Stone Island also excels in both retail and wholesale. With 28 directly operated stores and strong positioning in the retail sector, the company managed to build a high degree of awareness. Stone Island has always surged to be an entry-to-luxury clothing company standing out through its military-inspired, R&D-intensive products and vision. This resembles their proclaimed self-image: The pursuit of continuous experimentation and research, coupled with a touch of healthy madness.

The label with the famous badge logo has displayed an impressive performance in the past. Even in a year of lockdowns that hit the fashion industry with a 23% decline on average, Stone Island managed to grow by 1%. The company has generated a 10-year CAGR of 18% including their 2020 performance, while the EBIT-margin has now been above 25% for three consecutive years (Exhibit 1).

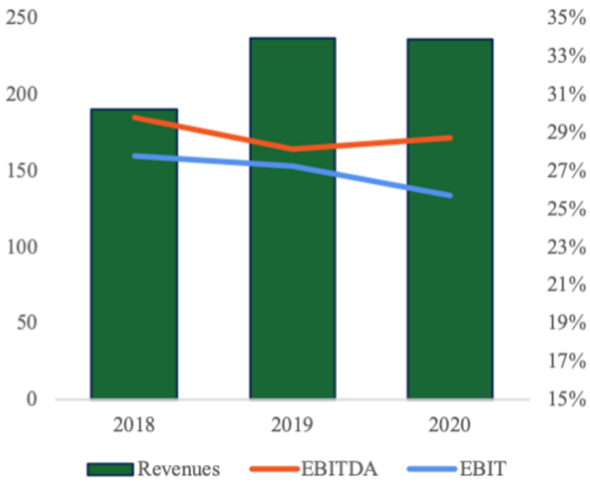

Figure 1: Source: Bain Deal Report – Stone Island Financials.

Companies Overview – Moncler

Moncler was founded in 1952. The name is an abbreviation that stems from its place of establishment, a French mountain town called Monestier-de-Clermont. From the beginning, Moncler worked with the material down. Starting off with sleeping bags, they quickly went on to produce their nowadays well-known down jackets. Moncler began to equip mountaineers for extreme expeditions. The shift towards the less harsh weather conditions of alpine sun terraces was established in the 1980s under the famous designer Chantal Thomass. By making use of the rising mountain holidays trend, this decision turned out to be a success. The Maison de Mode was acquired by Italian entrepreneur Remo Ruffini in 2003, who is still active as the Chairman and Managing Director. With Ruffini, Moncler managed to reinvent itself. Under the mission "born in the mountains, living in the city", they transformed from their old, dusty image to a more fashionable 4200-strong workforce.

7 years after their successful IPO in 2013, Moncler has developed the standing of an en-vogue, well-performing fashion label. Since then Moncler has achieved a revenue CAGR of 12% and an average EBIT-margin of over 28%. The 12% revenue decline in 2020 is still much higher than the luxury fashion market average of -23% (Exhibit 2).
The past and present financial performance seem to impress investors as well. The share price climbed by 25% last year, leading to an increase of market capitalization by a whopping €4.1B. The company with a 72% female quota is one of the most profitable enterprises within the luxury sector. Ruffini's implemented changes spell success for his firm.

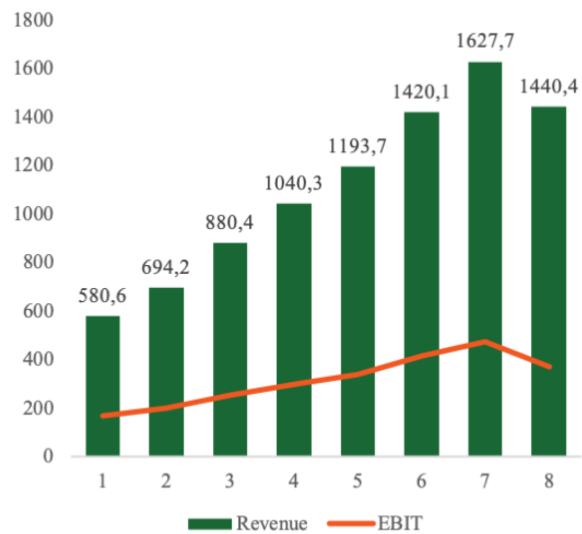

Figure 2: Source: Moncler Annual Report – Moncler Financials.

State of the Industry – Luxury Fashion

The fashion sector is divided into four segments. Absolute luxury forms the summit of the pyramid, while the entry-to-luxury segment stands just below. Branded mass brands and premium brands form the basis (Exhibit 3).

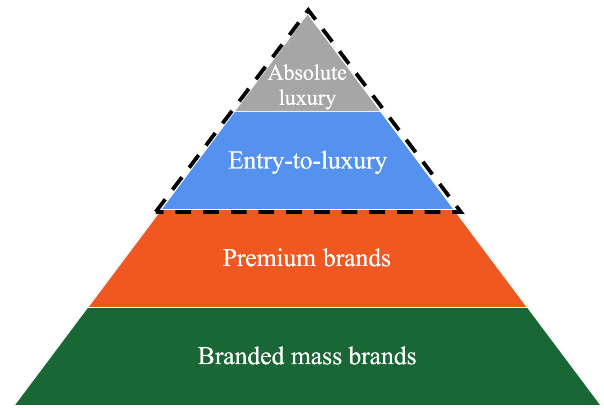

Figure 3: Source: Bain Deal Report - Market segmentation

The top two segments of the pyramid represent the luxury fashion industry, which generated sustainable growth over the years before 2020. The market grew at a CAGR of 8% between 2016 and 2019. In this period, the 20 fastest-growing firms generated an average CAGR of 16.9%. Moncler ranks at 10th position, while Stone Island, who just didn't make the list due to size, would have ranked 2nd. The industry is also shaped by a consolidation trend. Big corporations control the sector and often gobble promising contenders. 9 out of the 10 biggest companies in the sector are of such kind. Those 9 companies make up 47% of the Top 100 lists revenue. LVMH, the fashion group controlled by Bernard Arnault, has solely acquired 12 companies in the past decade. Most deals have surpassed the €1B benchmark. The consolidation trend has also reached Moncler back in 2019 when Kering, another large fashion group, was associated with a takeover. Ruffini denied the rumors and has taken a step in the opposite direction one year later.

The Covid pandemic has knocked the luxury fashion industry off-balance. With revenues of €217B last year, the market nosedived by 23%. EBIT margins have fallen to 75% of the prior-year level, profits to 40%. 7 out of 10 luxury executives estimate a bounce back to 2019 revenues soonest in the first half of 2023 (Exhibit 4).

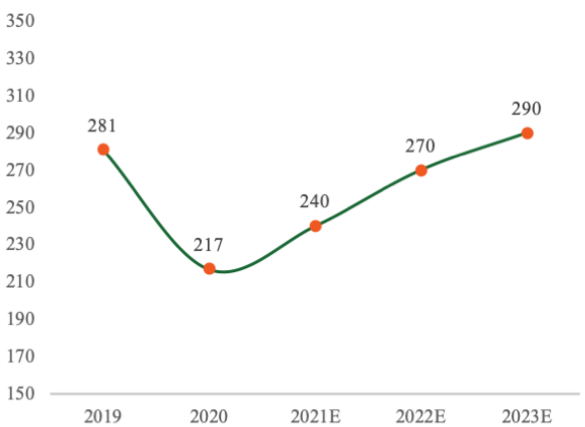

Figure 4: Source: Bain Deal Report – Market recovery until 2023E

However, Covid-19 also got the bar rolling in many areas. E-commerce luxury doubled its weight in the total market in 2020 as online influenced purchases gain in importance. The sector is set to rise to €110B until 2025 making up over 30% of the luxury market share. 2020 also boosted China's chances of, one day, becoming the world's biggest market. In five years' time, China will increase from 30% to almost 50% market share (Exhibit 5).

Deal Structure

In order to evaluate Stone Islands price tag, we have applied a discounted cashflow evaluation (DCF). On the basis of 14 comparable listed companies, Stone Island has been valued under the

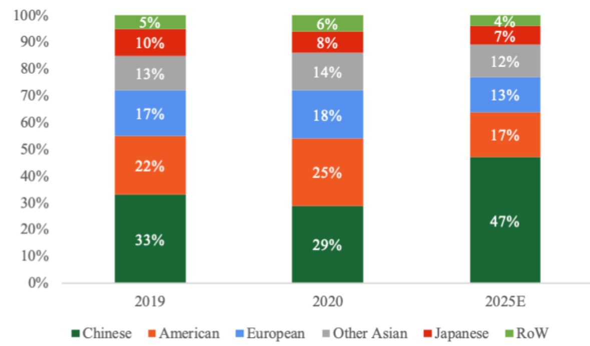

Figure 5: Source: McKinsey Industry Report – Luxury goods market by consumer nationality

going-concern approach. The average market KPIs have been adjusted to suit the private, growth-oriented target. The deal size of €1.15B reflects a slight overestimation of the actual value of Stone Island. According to the model, Moncler has paid a surplus of €69.5M, an overestimation by 6.4%. The acquisition price is also higher compared to similar deals last year. The sneaker company Golden Goose has been sold to the PE investor Permira in February 2020. With a revenue of €291M and a higher EBITDA margin of 32%, the company shows financial similarities to Stone Island. The EBITDA multiple was 14.1x while Stone Island has been sold for a multiple of 16.6x. The expected synergies will primarily foster future growth by increasing market power and CAGR. Stone Island is set to resume its growth path in the following years and the addition to Moncler's portfolio will have a positive impact on its financial numbers. SGFER combined the two companies' financial results for the past 7 years, by using a weighted average, and contrasted the results to the financials of Moncler by itself (Exhibit 6). In a combination of a maximum cash-out for Moncler of €748M and up to 10.7M shares at €37.51 per share to the Rivetti family, the deal was negotiated back in December last year and is to be closed in the first half of 2021.

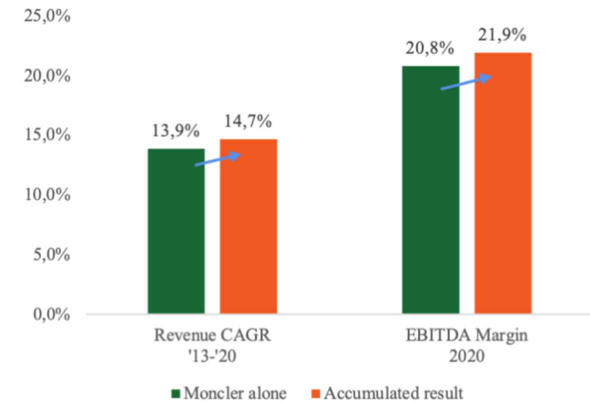

Figure 6: Source: Moncler Annual Report, Bain Deal Report – Combined financials.

Carlo Rivetti will join Moncler's Board of Directors in order to protect Stone Island's brand identity and autonomy in the integration process. For Mr. Ruffini, Stone Island also seems to be a nostalgic purchase. The company resembles the financial situation of Moncler 10 years ago, who at this point recorded a revenue of €283M and 30% EBITDA-margin. Under the wing of the new parent, the company hopes to achieve similar performance with Stone Island in the future. Moncler will share its knowledge and experience concerning the expansion in Asian and American markets. The consolidation trend might be perceived as a risk for the two companies at first sight. But the fact that the two French groups LVMH and Kering have grown so big has also created potential upsides further down the food chain.

[1]corresponds to the average price of the last three months

Potential Risks & Potential Upsides

The digitalization of the luxury fashion industry has been accelerated by the Covid pandemic. The rise of digitally enabled purchases by 50% in 2020 emphasizes the shift towards an online consumer experience. In Italian fashion, Moncler lags a little behind in this transformation. While most luxury companies aim to generate 20-25% of their sales online, e-commerce only makes up 8% of Moncler's revenues. In the course of the Genius strategy, Moncler has put a lot of effort into establishing a worldwide omnichannel e-commerce platform. The number of orders placed has already increased by 70% YoY after launching online shops in Korea, USA and Canada. The acquisition of Stone Island is certainly helping to seize e-commerce opportunities, as they show a high level of awareness online. Besides operating their own e-commerce platform since 2007, Stone Island is said to be among the best performing casual fashion brands for e-retailers like Mr. Porter. The integration into the Moncler family is supporting Ruffini's digital ambitions. The potential risk of losing track online has been averted by taking digitization measures. The following years will show if strengthening the digital culture of Moncler will turn into an upside.

The main risk linked to M&A transactions is overestimating synergies. In this case, the operating synergies appear to be a major potential upside of the deal. Both companies strive for continuous innovation concerning garments and fashion. Both companies build on their edgy heritage with a similar history rooted differently. Both companies show a strong brand asset. While their logos differ from each other, they are both very distinguishable from their competitors.

The role of China in the future luxury market cannot be stressed enough. Until 2025, China will be the most important market for the industry. This trend underlines a potential risk in the acquisition. Since Stone Island shows limited exposure to the Chinese market, it will be tough to establish a competitive position in 5 years time. Nevertheless, there are also macroeconomic trends that mitigate this risk. The luxury goods sector is highly correlated to wealth trends and economic growth. The significant slowdown in the Chinese economy might negatively impact revenues. Additionally, Chinese luxury consumption primarily consists of tourism shopping. Time will tell if Stone Island can resume its growth path under the wings of Moncler. The underlying synergies and Mr. Ruffini's experience in building a fashion empire will support them on their journey.