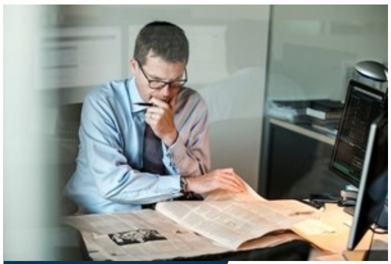


Friday Morning Coffee

Nr. 161 — Houston, we have a problem !

I went to Paris beginning of August on a weekend trip for the first time since the start of the pandemic. Not that this is relevant in itself, but the reason I mention it is that I experienced first hand that luxury shopping is alive and well. In a traditionally quiet Summer month where most Parisians are on the Côte d'Azur, clients, both local and foreign, were numerous in the Hermes and LVMH flagship stores. Also, both Beau Marché and Samaritaine were crowded like COVID-19 was a distant memory. It can therefore not come as a surprise that the biggest luxury companies have just published stunning Q2 results. Organic growth rates year-on-year were indeed above the keenest analyst estimates : LVMH +82% , Kering +95% and Prada +66% ! Outlooks given by managements for the second half of the year are encouraging.

After closing our successful investment case in Prada earlier this year as our fair value was reached, we do not have any investment left in the soft luxury goods sector. Swatch is our only holding in hard luxury. While still attracted to the earning power of these businesses with strong brands and moats, we could simply not get our arms around the valuations. This week however, something changed.

China president Xi Jinping sent luxury goods stocks sharply lower as he outlined his plan for "common prosperity", including potential income regulation and redistribution. Chinese shoppers are the most important by nationality for the luxury sector. Swatch generates half of its sales with Chinese consumers, Prada 35%, Kering and LVMH roughly 1/3. According to Jefferies, as little as ten thousand very wealthy Chinese individuals generate one quarter of all luxury sales to the Chinese. Houston, we have a problem !

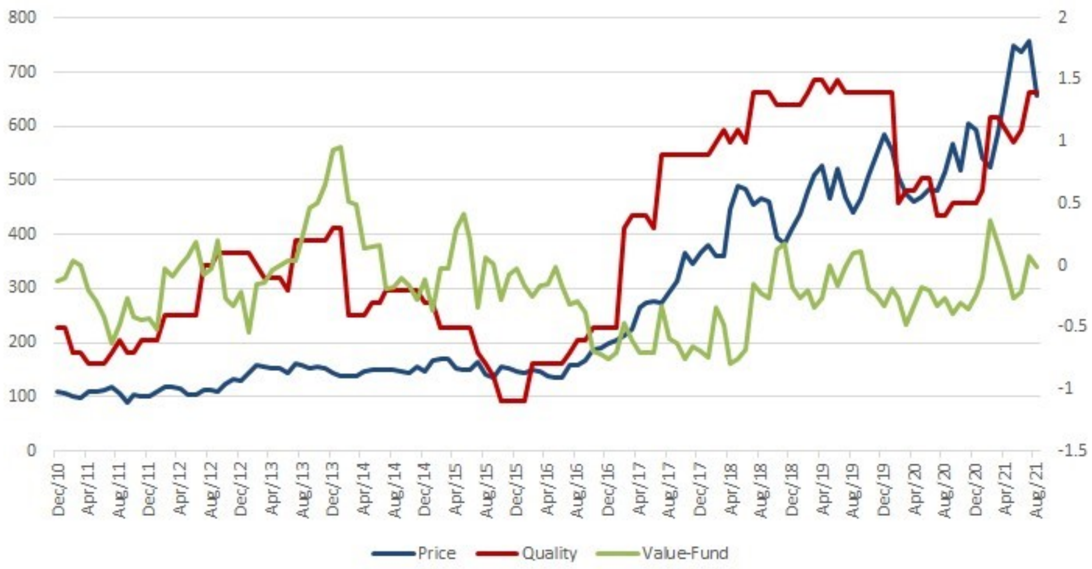
Source : Bloomberg

Friday Morning Coffee

European Capital Partners

Nr. 161 — Houston, we have a problem !

Or shall we rephrase: Houston, we have a buying opportunity. Companies like Kering start indeed starting to look much more attractive in our proprietary quality-value framework :



Source : ECP

In our analysis, we consider Kering a company with superior and increasing quality now trading at an average valuation compared to the average European company.

If luxury stocks continue to be under pressure without any more precise actions from the Chinese government, it may well create an interesting opportunity for long term investors to access these compounding quality businesses at a decent valuation. Stay tuned.

I wish you a nice weekend,

Léon Kirch, CFA
Partner & Chief Investment Officer
August 20th, 2021