Department of Economics and Finance

Final Thesis in Financial Markets and Institution

“Mergers and Acquisitions in the Luxury Industry: LVMH acquires Tiffany”

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Academic Year 2020/2021

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Introduction

The luxury industry is a magical world that does not have the role to satisfy basic needs, but makes everyone who participates in it feel special.
From an etymological perspective, the word luxury comes from the Latin "luxus" which means superabundance, excess in the way of life or a display of wealth aimed at satisfying desires that transcend real needs (Cabigiosu, 2020).
Luxury is a mental attitude associated with superior quality , high status, and privilege. The concept of goods crafted manually by expert artisans and made with eventually rare, raw materials, was born many years ago, but it is still present today. Individuals who purchase luxury items, not only desire what is visually pleasant, but also wish to establish themselves as economically and socially successful, by owning something that is best and exclusive.
In fact, luxury is usually connected to experiences, feelings, and products that carry a high symbolic value for which the consumer is willing to pay exorbitant amounts. In fact, luxury prices are well above the average price of the category to which the product belongs, which is definitely not a simple result of production costs.
Initially, the concept of luxury was associated with aristocracy, especially in the fashion industry, where each piece was tailored for the customer and represented a symbol of prestige. It was thanks to Coco Chanel that the interpretation and the approach to fashion were revolutionized to a more modern and practical look. If many years ago the experience of luxury was limited to very few, elite consumers, now it has widened to new groups of buyers and new categories of products, while still maintaining its magical sense of exclusivity and distinction. The modern interpretation of luxury is not only about the product, but also about customer experience and brand value.
But, the luxury industry is not only made of clothes, jewels, cars, and so on… it is made of economics, finance, and strategies. It responds to economic forces that drive every market, like supply and demand, by customers behavior and preferences, and market movements. Companies gain and maintain their success if they are able to successfully control and exploit these factors.

This paper has the purpose of analyzing the various strategies implemented in this sector, focusing especially on how LVMH, one of the most famous and affirmed brands in the industry, has reached and is maintaining its leading position in the European market. This titan owes its almost undefeatable power to the successful implementation of the strategy of mergers and acquisitions, widening its portfolio of brands. In fact, "the name LVMH itself was generated in 1987 by the merger between Moët Hennessy and Louis Vuitton. In 1988, LVMH acquired Céline and from 1999 onwards, it started a comprehensive internationalization process, purchasing 25 leading brands" (Cabigiosu, 2020).

This is the perfect example of a brand that, instead of relying on the development of products, which could have easily suffered the effects of the economic crisis, based its exponential growth on financial strategies, especially on that of mergers and acquisitions, allowing it to adapt and exploit different economic scenarios.

The second purpose of this paper is to highlight the importance of financial instruments and operations, especially in highly competitive sectors, like the luxury one. These tools, if used smartly, lead to fast and steady growth, allowing the firms that use them to gain large market share and a dominant position.

In spite of the fact that financial strategies, and especially M&A, are often risky, they represent a very powerful resource that allows companies whose moves are based on it, to increase their value and to become leaders, like LVMH is today.

The paper is structured into three chapters in which are analyzed respectively the luxury industry, the analysis of M&A, and the specific case of LVMH.

The first chapter attempts to provide a universal definition of luxury, and to explain the main characteristics and ways in which the luxury industry and its participants operate. It will give an overview of the main actors and competitors, as well as of the specific factors that characterize this sector. In addition to that, it will conduct an analysis of the main drivers and causes that push operating firms to undertake M&A operations which are not widely diffused in other industries.

The second chapter presents and explains M&A operations, by considering and analyzing in depth their many aspects and sides. This section also measures their risks and benefits in order to illustrate why firms undertake them. The main purpose is to describe why, since they are not a widespread tool in other industries, are instead broadly employed in the luxury sector, which is characterized by high competition, and if they represent a valuable resource or a downside.

Lastly, the third chapter, conducts a study about one of the two main leaders of the luxury market, LVMH, which has made M&A the foundation of its expansion strategy. In particular, the chapter focuses on the recent acquisition of the iconic American luxury jewelry brand Tiffany & Co, which was concluded in January 2021. The end goal is to comprehend and present the reasons that have brought both firms to undertake and finalize the deal. This case is a perfect example of how, a well conducted cost benefit analysis, and evaluation of risks, can lead to the success of acquisition operations.

The conclusions of this paper will summarize and present the main results of the analysis of the luxury sector, the benefits provided by the "atypical" strategy of M&A, and the results of the implementation of the latter by the specific case under study.

1.The Luxury industry

1.1 Introduction

As it was stressed in the general introduction of this paper, it is very complicated to attribute a single and universal definition to luxury. The notion has changed throughout the years, is still unfolding, and is subject to relativity. The concept of luxury evolved from something that was accessible only to a very restricted strata of population, like aristocracy, to "new luxury", something that is closer to everyday life and is approachable

by a wider selection of customers, and that is identified by many authors as a transitional phase born after the wave of the second industrial revolution (Danziger 2005).
The perception of luxury changes in parallel to the social and historical context in which it is scrutinized, and is strictly linked to some factors: price, quality, uniqueness, aesthetic. The more a product is considered of high quality and distinguishable from others in terms of uniqueness, the more it is considered luxurious, and has a higher price associated with it. Because of the many facets that the concept of luxury possesses, in some cases, the term can be attributed to a negative connotation, normally associated with ostentation and immoderation. In fact, from "the root "lux" also originates the word "luxuria" which can be translated as "exuberance, profusion, luxury" and "lascivious and voluptuous life" (Lipovetsky and Roux 2003). Luxury has also been identified as something devious, as Kapferer (2012) explains, "identifying its origin in the Latin "luxation", i.e., distance, and suggests that luxury describes a considerable departure from the usual way of satisfying needs".
From these considerations, it is possible to understand the ambivalence associated with different interpretations and perceptions of luxury.
As we have seen, luxury is not tied only to the physical characteristics of a product, but is a full sensorial and personal experience, which has the power to hypnotize and create a feeling of belonging to a special and exclusive category. The customer feels selected , like he belongs to a small circle of carefully elected representatives: "the happy few" (Kapferer 1997). In addition to that, some luxury products are tailored to clients' personal requests, meaning that they are unique and inimitable pieces no one else will have. Custom-made items enhance the sense of exclusivity that a luxury product can offer. These attitudes can justify the exorbitant prices that customers are willing to pay and that are not a simple reflection of production costs.
In spite of the fact that there are many and generic definitions of luxury, the luxury sector is instead distinguishable by specific characteristics that influence its structure and the strategies adopted, especially when it comes to mergers and acquisitions, the main driver of this industry's concentration.
This chapter has the purpose to describe and present the specific attributes of the luxury sector and the reasons that push its actors to perform acquisitions, being in a market that

is highly competitive and that needs to frequently adapt to social, historical, and economic changes.

1.2 What is luxury?

As it has been previously addressed, there is no unique definition of "luxury".
"Some people think luxury is the opposite of poverty. It is not. It is the opposite of vulgarity."
— Coco Chanel
This quote is from the iconic Coco Chanel, founder of one of the main leading brands of the past and present scenario of the luxury industry. A common misconception when it comes to defining luxury is to associate this concept with "richness" or, as Coco says, "the opposite of poverty". In reality, it is true that luxury is often associated with high prices, but that is not what defines it. Luxury items are not a necessity and are not needed to satisfy our primordial needs, but they provide a sense of satisfaction and uniqueness to whoever purchases them. As Sombart states, luxury is any expense that exceeds what is necessary (Sombart, 1967).
Expensiveness is actually a consequence of different value drivers, some of which are functional and some of which are emotional. What defines a product as "luxurious" is a mix of those factors. Superior quality, materials, craftsmanship, service, expertise are only some of the fundamental characteristics that make luxury. In addition to those crucial factors, the real reason for which luxury is so expensive is that its perceived value is very high for consumers. Luxury items are sensed as rare, unique, they represent a symbol for status. For these reasons, luxury brands need to be very careful on how they are recognized and need to put a lot of effort into protecting and strengthening their image.
Luxury has been subject to different interpretations and evolution throughout history.
At the end of the nineteenth century, the term luxury acquired a new meaning related to complacency in what is excellent and expensive and to the pleasure of enjoying something comfortable beyond what is strictly necessary (Brun and Castelli, 2013).

At this time, the concept of luxury was still associated with aristocracy and customization, and products were sold to a highly restricted market.

It was only after the second industrial revolution that more people had the economic means to access luxury items. This era, with its historical changes, led to general economic progress, increasing the welfare of the economy as a whole, and for both firms and consumers. In fact, firms became highly productive which led to bigger gains. The larger volume of standard goods produced represents the foundation for the birth of modern luxury companies. The closer time got to the second part of the 20th century, the more massification became a widespread trend. This led to the creation of a new type of luxury called "Neo-Luxury" which brought a larger part of the population to the market. This transformation was illustrated by Silverstein et al. (2008) through the phenomenon of trading-up: the desire and intention to pay a premium price for goods that have a high degree of quality, aesthetic taste and attractiveness compared to products in the same category but that are not so unapproachable. Customers thus prefer to spend more on categories of products in which they are more interested in and in some selected brands (trading-up) and buy less of certain non-interesting products (trading down) to be able to invest what they save in new luxury products.

The tendencies above can be explained by the possibility to make an additional subdivision of the macrosector of luxury items in three micro-sectors. The first is the so-called "Inaccessible Luxury" which strongly connects to the concept of aristocracy, tailored and unique items that are produced in limited numbers and so are attributed a high exclusivity, which is in turn reflected on their very selectioned group of buyers. This category is characterized by high prices and high levels of customization and is associated with haute couture collections.

The second differentiation is called "Intermediate Luxury" and comprehends those goods that are sold still at elevated but lower prices than the ones in the previous category. They are not completely tailored and customized, but they are adaptable to each consumer's personal needs. Prêt-à-porter and ready-to-wear are included in this category.

Lastly, the third micro-sector is named "Accessible Luxury". The products that belong to this category are not luxurious themselves, but are considered as such because of the brand they belong to. The purpose is to appeal to mass sales as they can generate higher

volumes despite higher prices compared to that of other products in the same category. These kinds of luxury are targeted to consumers that own a lower income than that of the ones of the first two categories, but that try to reach the same social status through this type of purchase. The introduction of new luxurious product categories such as perfumery, eyewear and cosmetics is a typical way to allow even consumers who cannot afford to spend large amounts to have a bite of the world of luxury.

From the explanation above, it is possible to see how luxury has now become more accessible and almost a mass phenomenon. In spite of that, this new concept does not mean that luxury products are less valuable, but only that luxury can now be a source of pleasure and satisfaction for a large number of consumers.

In line with this pyramidal perspective, Kapferer's (2012) study in its analysis of business models highlights three different levels of brands. "Griffe" goes hand in hand with "Inaccessible Luxury" where the brand signs the unique and customized pieces that it creates for its restricted and elite group of customers. Secondly, "luxury brands" are associated with the second category, "Intermediate Luxury", and are produced in limited series with higher quality and level of industrialization. In this case, brand awareness represents an advantage by creating additional value and is what justifies the prices. The last category is then linked with "branded goods" that are produced in larger quantities, but sold at relatively lower prices to reach a wider target market.

In addition to that, not only luxury and brands can be organized into categories, but products as well. In fact, new luxury goods can be distributed in three different groups. The first, "accessible superpremium", includes those products that have a very high price compared to products within the same category, but that are accessible to middle class consumers as they do not have a particular value. For example, "Starbucks, an iconic new-luxury brand, charges around $1.50 for a tall coffee, about a 40% premium over a similar-sized Dunkin' Donuts cup, which costs about $1.10" (Silverstein & Fiske, 2014).

The second classification is "old-luxury brand extensions".

This refers to goods that are a cheaper version, hence sold at a lower price, of goods that have normally been purchased only by the rich.

Mercedes-Benz, Ermenegildo Zegna, Tiffany, and Burberry, are valuable examples of companies offering affordable products alongside their traditional ones (Silverstein & Fiske, 2014).

The last identification is referred to as “mass prestige” or “masstige”. These products occupy an intermediary position between luxury and mass products. “While commanding a premium over conventional products, they are priced well below superpremium or old-luxury goods. An eight-ounce bottle of Bath & Body Works body lotion, for example, sells for $9, or $1.13 per ounce. That’s a premium of 276% over an 11-ounce bottle of Vaseline Intensive Care, which sells for $3.29, or 30 cents an ounce. But it is far from being the highest-priced product in the category” (Silverstein & Fiske, 2014).

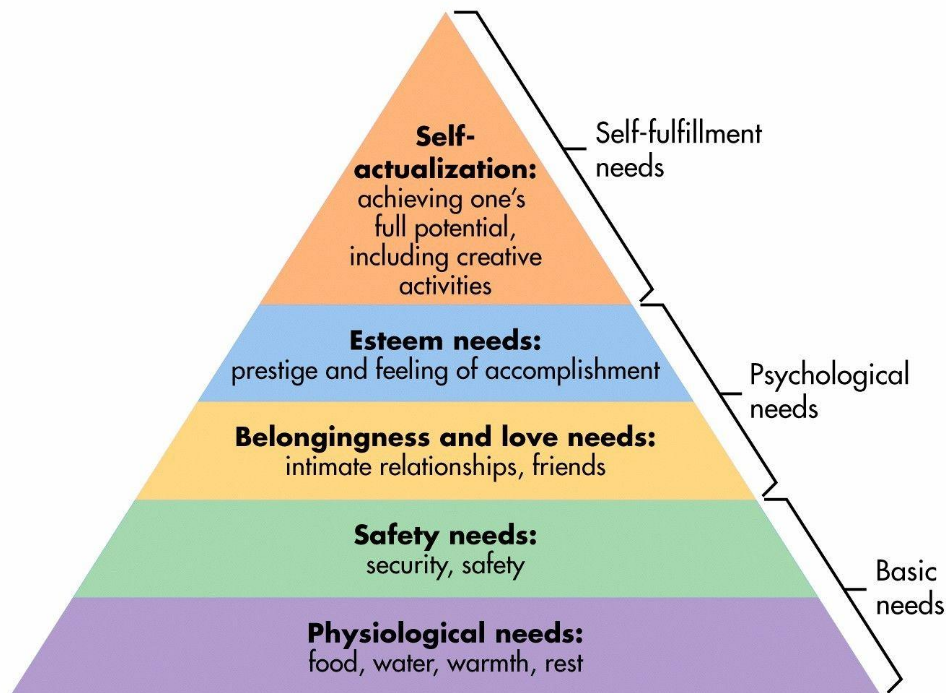
In the following paragraph, an analysis of the main characteristics that distinguish the luxury sector will be conducted, as well as an identification of the main competitors, and of the general economic situation of the luxury industry.

1.3 Characteristics

The luxury industry is characterized by the fact that normally, since price is also seen as a distinguishing factor, the more it rises, the more demand rises as well. Of course, this is only true up to some point.

The luxury good is defined in Microeconomics as that particular good for which demand increases more than proportionally as income rises, so that expenditures on the good become a greater proportion of overall spending. These goods present an elasticity of demand greater than one. In fact, in line with this definition, a German statistician named Engel proved that when there is a 1% rise in income, the consumption of the luxury goods increases more than 1% (Engel E., 1857). This discovery was made during a study about families’ spending habits in relation to their income. The results of this research showed that the more a family is poor, the greater their fraction of income spent on necessities, especially groceries. In spite of that, the increase in income did not go hand in hand with an increase in consumption of alimentary, in fact, in this case, consumers chose to buy superior or luxury goods. Since these findings have been discovered through Engel’s study, this characteristic of luxury products is called “Engel’s Law”. Luxury

goods behave in the opposite way of necessity goods, where demand increases less, in proportion, than income. The behavior of consumers towards the purchase of luxury goods can also be explained, through a social point of view, by Maslow's hierarchy of needs.



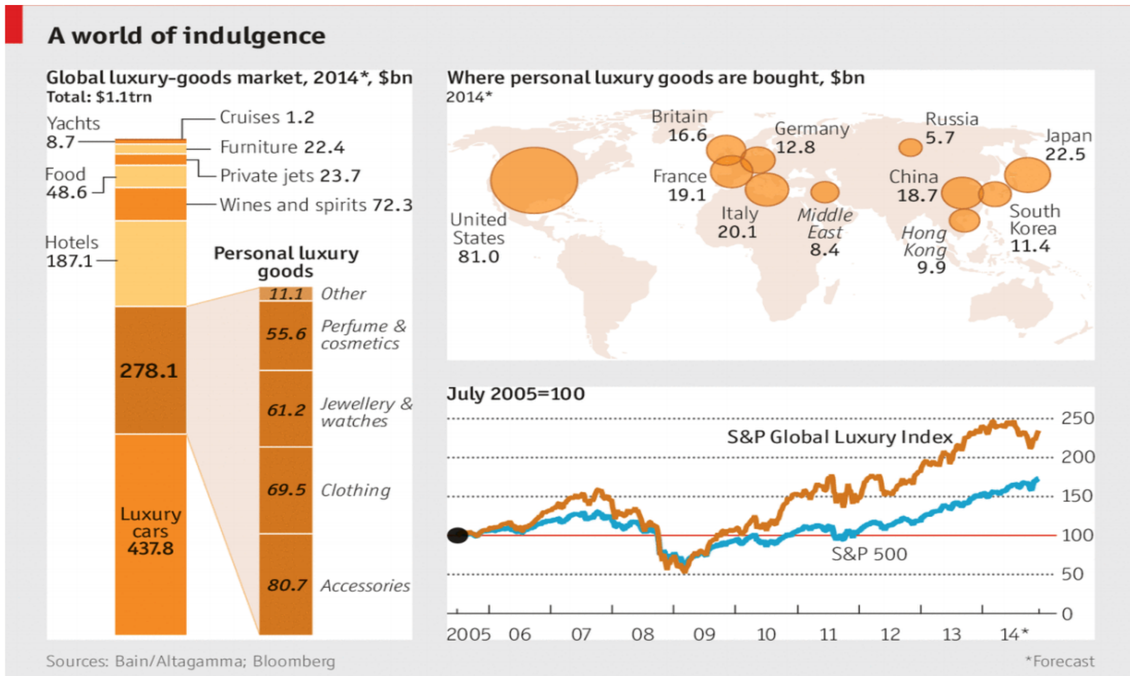
Source: https://www.simplypsychology.org/maslow.html#gsc.tab=0

This pyramid shows how after fulfilling basic needs, people will shift their consumption choices towards higher end goods.

For the reasons highlighted above, consumers are willing to pay very high prices for the desired items, often also during times of general and financial crisis. Indeed, not only the luxury sector seems to be the only one with very little or no negative effects from external factors, but it also has very positive forecasts regarding its growth trends, especially for the recovery after COVID-19.

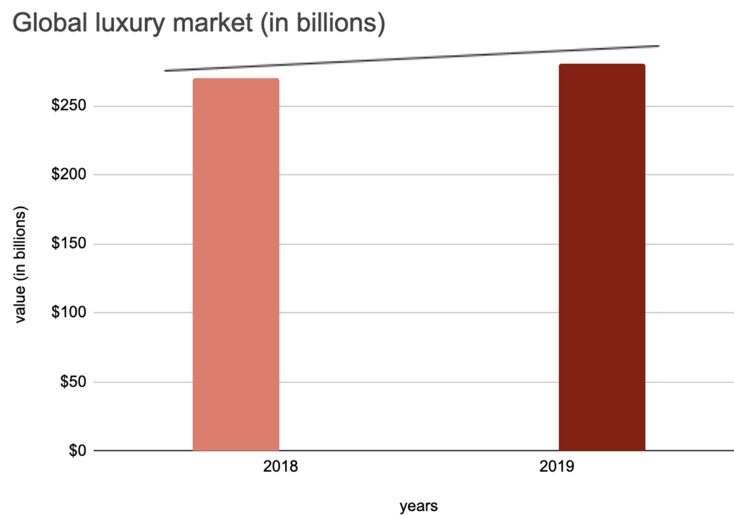
What distinguishes the luxury sector from the majority of the others is the capacity to overperform market returns.

In fact, as the following figure shows, while following market trends, it has amplified growth rates in between 2005 and 2008 and between 2009 and 2014.



Sources: Bain/Altagamma; Bloomerg Figure: The Economist

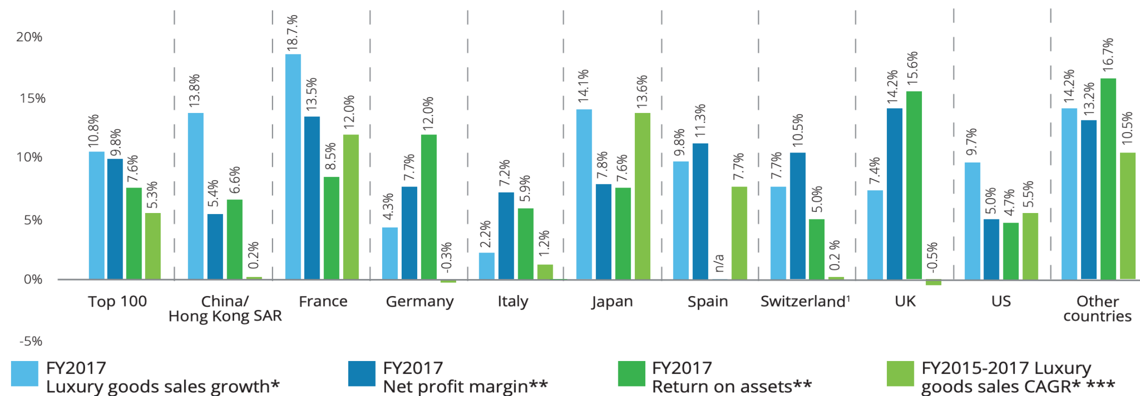
In 2019, the global luxury market size was valued at €281 billion, showing a growth of 4% from 2018 (Kering, 2019).



Personal elaboration of data from Kering Financial Document 2019.

Luxury firms are primarily located in Europe, US and Asia, and Italy accounts for the highest number of luxury brands in the Interbrand ranking (24 up to 100). By nationality, worldwide luxury fashion is characterized by the volume of Chinese (32%) and American consumers (22%). Chinese consumers increased their share by two percentage points versus 2018. Generations Y (Millennials) and Z contributed 100% to market growth in 2019. Those of this population in China and South-East Asia are more dynamic and attracted by personal luxury goods. Over the past ten years, China has accounted for 70% of the expansion in the luxury fashion market segment, and this dominance is expected to continue till 2025 (Kering, 2019).

Performance by country, FY2017



Results reflect the Top 100 companies headquartered in each country
* Sales-weighted, currency-adjusted composites
** Sales-weighted composites
*** Compound annual growth rate
¹ Net profit margin and return on assets based on data from two companies

Source: Deloitte Touche Tohmatsu Limited. Global Powers of Luxury Goods 2019. Analysis of financial performance and operations for fiscal years ended through June 2018 using company annual reports and industry estimates.

Source: "Performance by country 2017"- Deloitte & Touche

Many factors might impact the future of the luxury industry: the recent slowdown of economic growth in many countries, the recent adoption of protectionist policies in US and China, the digital revolution and the impact of technology on production systems, the influence of Millennials and Generation Z and the Brexit in the Eurozone, and of course, COVID-19. The consequences of the pandemic will be discussed in the next section, but

for now, it is possible to say that even though the effects of the virus did not spare the luxury sector, the latter was less influenced than other industries and forecasts a successful recovery in the upcoming years.

In almost every financial report or statistic analyzed, the luxury sector is divided into three micro-sectors depending on the nature of the products taken into account. The second most lucrative category of the luxury industry is “Personal Luxury”, and includes all physical goods that can be owned and personally consumed. Fashion and accessories fall into this category with an ulterior classification into soft luxury and hard luxury, in which the latter includes jewelry and watches.

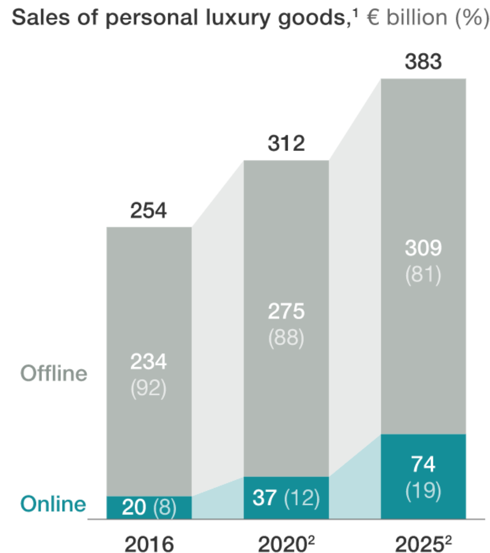
The most profitable category of the luxury industry is “Experiential Luxury” which comprehends luxury services that generate instant gratification. They can be sold by themselves like hospitality, fine wines and spirits, or as an additional experience to a product, for example good customization through online apps. Experiential Luxury represents the biggest fraction of the total revenues of the industry, has been rising in recent years, and is forecasted to grow even more because of the effects of COVID-19.

“Luxury Investment goods” constitutes the last group, including timeless and traditional luxury goods like yachts and private jets.

The most important aspect of luxury sales, in the online world. It has been a rapidly growing trend in recent times and is expected to skyrocket in the next few years as a consequence of the restrictions and changes in lifestyle caused by the pandemic.

Personal Luxury is the most analyzed division in the luxury industry because of the fact that the main market leaders (LVMH and Kering) operate in it.

The following results prove how it is expected that online luxury sales will more than triple by 2025, constituting nearly one-fifth of personal luxury sales, as it is shown in the chart below:



Source: Euromonitor, Forrester Figure: McKinsey&Company

As it has been already mentioned, the main characteristics of the luxury sector is its high competitiveness. To maintain their success in the industry, firms need to be able to evolve and adapt to social and economic changes, requiring more resources and competencies. Hence, the larger the size of a company, the more possibilities it has to survive and succeed. In fact, "the minimum size required to survive as an independent global luxury fashion firm is estimated to be one billion euros" .

It is not a case that the two leaders in the market, LVMH and Kering, are actually large groups of firms that have grown throughout the years by acquiring numerous brands, increasing the level of control in the industry, at the expense of smaller firms.

This trend started in the mid-1980s when many companies operating in the luxury sector started to invest more in M&As in order to promote rapid growth and increase their market share. This process gradually increased the concentration of the luxury industry,

especially in Europe, where several smaller family businesses are located. These firms, such as Gucci or Fendi, have a strong brand image, reputation, a clear value proposition and positioning but also lack the resources to face threats and opportunities mainly related to the emergence of new markets and new technologies.

In 2000, M&A operations had reached considerable numbers, but in the last twenty years, they have more than doubled. LVMH, Mayhoola, Kering and Michael Kors are examples of groups that have undertaken the most important and expensive acquisitions in the past twenty years, creating portfolios of brands extremely diverse to make their market position robust (Cabigiosu, 2020).

In Europe, LVMH and Kering, have become the main leaders, by acquiring many brands in different industries that range from wine to jewelry, but mostly focused on fashion. Today, because of their presence which includes a rich portfolio of brands, the structure of the luxury market is almost oligopolistic, as it is proven by the following table:

Top 10 luxury goods companies by sales, FY2019

FY2019 Luxury goods sales ranking	Change in ranking from FY2018	Name of company	Country of origin	FY2019 Luxury goods sales (US$M)	FY2019 Total revenue (US$M)	FY2019 Luxury goods sales growth*	FY2019 Net profit margin[1]**	FY2019 Return on assets**	FY2016-2019 Luxury goods CAGR[2]*
1	↔	LVMH Moët Hennessy-Louis Vuitton SE	France	37,468	60,069	16.8%	14.5%	8.1%	16.5%
2	↔	Kering SA	France	17,777	17,777	16.2%	14.7%	8.6%	23.3%
3	↔	The Estée Lauder Companies Inc.	United States	14,863	14,863	8.6%	12.1%	13.6%	9.7%
4	↔	Compagnie Financière Richemont SA	Switzerland	13,822	16,188	8.5%	19.9%	9.9%	2.4%
5	↑ 1	L'Oréal Luxe	France	12,334	12,334	17.6%	n/a	n/a	12.9%
6	↓ -1	Chanel Limited	United Kingdom	12,273	12,273	10.4%	19.6%	17.9%	12.5%
7	↔	EssilorLuxottica SA	Italy	10,624	19,463	6.0%	6.8%	2.3%	ne
8	↑ 1	Chow Tai Fook Jewelry Group Limited 周大福珠宝集团有限公司	China/Hong Kong SAR	8,411	8,500	13.9%	7.0%	7.5%	5.2%
9	↑ 1	PVH Corp.	United States	8,076	9,657	9.8%	7.7%	6.3%	8.7%
10	↓ -2	The Swatch Group Ltd.	Switzerland	8,014	8,294	-3.0%	9.1%	5.5%	2.9%
Top 10				**143,662**	**179,418**	**11.9%**	**13.3%**	**7.6%**	**11.7%**
Top 100				**280,640**	**320,291**	**8.5%**	**11.2%**	**7.4%**	**8.0%**
Top 10 share of Top 100				**51.2%**	**56.0%**		**71.7%[3]**		

[1] Net profit margin based on total consolidated revenue and net income
[2] Compound annual growth rate
[3] Top 10 companies share of total net profit for Top 100 companies—based on the 79 companies reporting net profits
e=estimate n/a=not available ne=not in existence (created by reorganization)

*Top 10 and Top 100 sales growth rates are sales-weighted, currency-adjusted composites
**Top 10 and Top 100 net profit margin, return on assets and asset turnover ratio are sales-weighted composites

Source: Deloitte Touche Tohmatsu Limited. *Global Powers of Luxury Goods 2020.* Analysis of financial performance and operations for fiscal years ended through 31 December 2019 using company annual reports, industry estimates, and other sources.

Source: "Top 10 luxury goods companies by sales, 2019"- Deloitte & Touche

In addition to the present success of the sector, it has been pointed out that the latter is in constant growth. There are several factors, called development drivers, that influence market trends.

As it has been mentioned before, demand for and consumption of luxury products increases as income does, so PIL or GDP, can be considered as the first main drivers. In spite of that, luxury purchases are not only linked with economic factors, but also with social and psychological aspects.

A curious phenomenon that sustains the previous statement, happened in Japan when, during one of the biggest recessions that the country occurred, the purchases of luxury items actually skyrocketed. This depends on the fact that consumers do not attribute the same importance to the price of luxury goods as they do to that of normal goods. In fact, contrary to what happens to demand of normal products when their price rises, that of luxury goods goes up the higher the price, because the bigger the increase of the latter, the more they are perceived as having higher quality and status, which in turn raises their demand.

Another important factor is currency and the exchange rates associated with it that have a direct impact on the revenues of international sales, and an indirect effect on buyers purchasing power. The main luxury goods manufacturers are located in Europe, more precisely the majority in Italy and France and a lower fraction in Switzerland, and so the currencies in which they produce are respectively the euro and the Swiss franc. In spite of the location of the production process, sales happen internationally, exposing firms to the US dollar and dollar-linked currencies, such as the renminbi and the Hong Kong dollar, and to the yen.

This might weaken the European currencies having a positive impact on earnings for French, Italian, and Swiss luxury companies, which might exploit a time lag depending on hedging strategies (Subdys, 2012).

Country breakdown: HSBC Luxury Goods coverage (by market capitalisation)

Country	Weights (%)
France	56.5%
Switzerland	15.1%
United States	9.1%
Italy	8.3%
Hong Kong	6.3%
UK	3.4%
Germany	1.3%

Source: Thomson Reuters Datastream, HSBC

Source: HSBC 2012

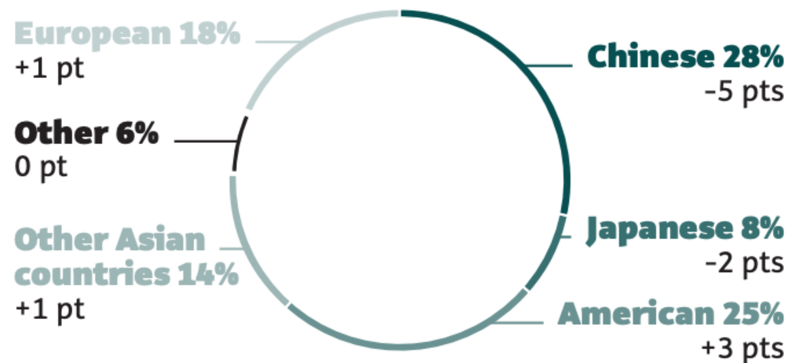
In spite of the fact that countries like the U.S. and Europe still have positive sales revenues, these markets are now more or less mature, and record lower and slower growth rates. Nowadays, the most profitable targets for luxury companies are developing countries like China, Brazil, and the Middle East.

The following table shows the eight largest countries in the worldwide personal luxury goods market in 2020 (revenue by location).

Rank	Country	Size *(in € billions)*	Reported YoY change	YoY change at comparable exchange rates	% of total market
1	United States	55	-27%	-26%	25%
2	Mainland China	44	+45%	+48%	20%
3	Japan	18	-24%	-25%	8%
4	South Korea	11	-24%	-16%	5%
5	United Kingdom	11	-35%	-34%	5%
6	Italy	10	-44%	-44%	5%
7	France	9	-44%	-44%	4%
8	Germany	8	-30%	-30%	4%

Source: Kering's financial document 2020

Normally, tourism constitutes a big part of revenue for these developing countries, but because of COVID-19, this trend has been deeply modified. Because of the travelling restrictions imposed by the authorities to contain the effects of the pandemic, international tourist flows came to a standstill, leading to a sharp drop in tourist spending and an increase in local purchases. “The proportion of consumers of nationalities that are traditionally active on their local markets increased, while the proportion of those who generally spend abroad dropped accordingly. For example, the proportion of consumers from China fell by 5 percentage points compared to 2019, while the proportion of American and European consumers increased by 3 points and 1 point, respectively” (Kering, 2020).



Source: Kering’s financial document 2020

Unfortunately, 2020 has been characterized by COVID-19, which has had impacts worldwide, causing deep economic, social, environmental, and psychological changes.

The consequences have modified global trends for both consumers and businesses. The way of living, everyday life routines, strategies for conducting business, consumers preferences, tastes, and habits are now different. Hence, the following paragraph will conduct an analysis of how the pandemic has transformed the luxury sector, the economic scenario as a whole, and the dominating trends.

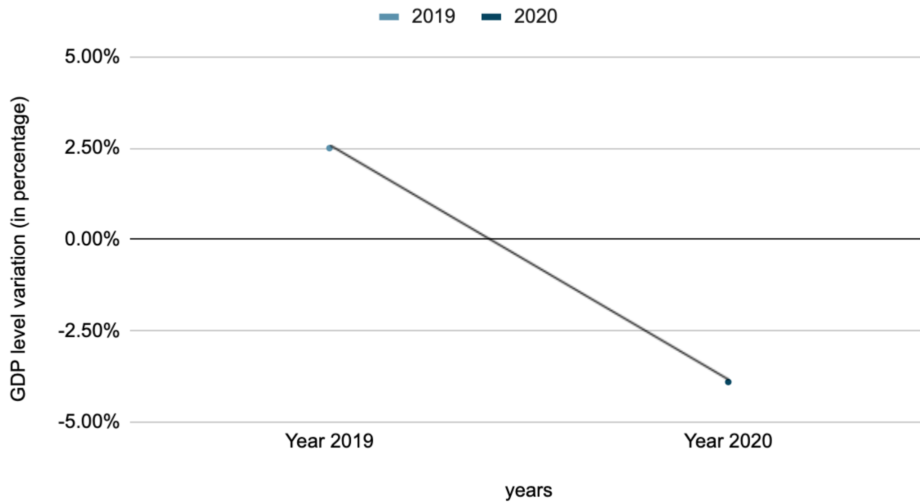
1.4 The effect of COVID-19

The current historical period is a clear example of how, in spite of the deep economic difficulties that have arised, the luxury industry never becomes a huge victim and seems to not be governed and affected by the usual forces that normally influence consumers' buying behavior.

Of course, even though the luxury industry has not been a huge victim, it has still suffered the effects of the pandemic. The impact was not homogenous, in fact, some brands were affected more than others. LVMH incurred losses amounting to -15%, Moncler posted a -18%, and Hermes seemed to be one of the least damaged with only a -6.5% loss (citation needed).

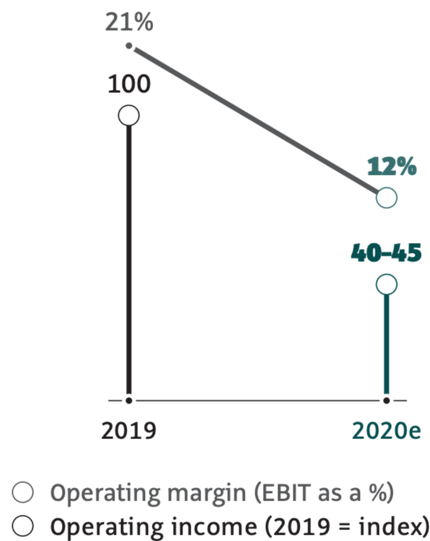
Although the main value drivers of the industry remain the same, the main causes of the losses are of both economic and social nature. Extended store closures in some of the industry’s key markets provoked a drop in revenues and also caused a drastic reduction in tourist numbers and spending, with a special impact on travel retail. According to IATA, global air traffic (based on the number of passengers) fell by over 60% in 2020 compared to the previous year. Another effect has been the acceleration of an existing trend to relocate spending, increasing sales in local markets, where 80% to 85% of purchases were made (Kering, 2020).

Since luxury purchases go together with income and welfare, it is trivial that the effect of a contraction in global GDP of 3.9% during 2020, vs. an increase of 2.5% in 2019 (Oxford Economics,2021), has led to a huge drop in sales.



Source: personal elaboration of GDP data trends in 2019 vs 2020

These changes had a significant impact on the profitability of sector participants, with a decrease in operating income estimated at approximately 60% in 2020 and operating margins for the sector narrowing from an average of around 21% in 2019 to 12% in 2020 (Kering, 2020), as it is displayed in the graph below:



Source: Kering's financial document 2020

As it has been briefly mentioned above, the nature of these trends was not only economic, but social as well. The pandemic and the measures that have been imposed by authorities to contain the virus have deeply affected everyone's mental health and habits.

There has been a drop in consumer confidence caused by a drop in earnings which consequently led to a decrease in spending. Geopolitical and social tensions, combined with uncertainty about major political and social changes happening all over the world (protests about racial and social issues, the presidential and senate elections in the U.S., sharp volatility on equity markets, Brexit negotiations, etc.), have had the same negative effects on consumer confidence and spending trends.

In spite of all of the negative results that have been presented above, not all the transformations have brought negative effects, and this new approach to the future and to new ways of experiencing luxury, can even represent an opportunity to exploit.

The luxury industry feels now more than ever the need to adapt to these changes.

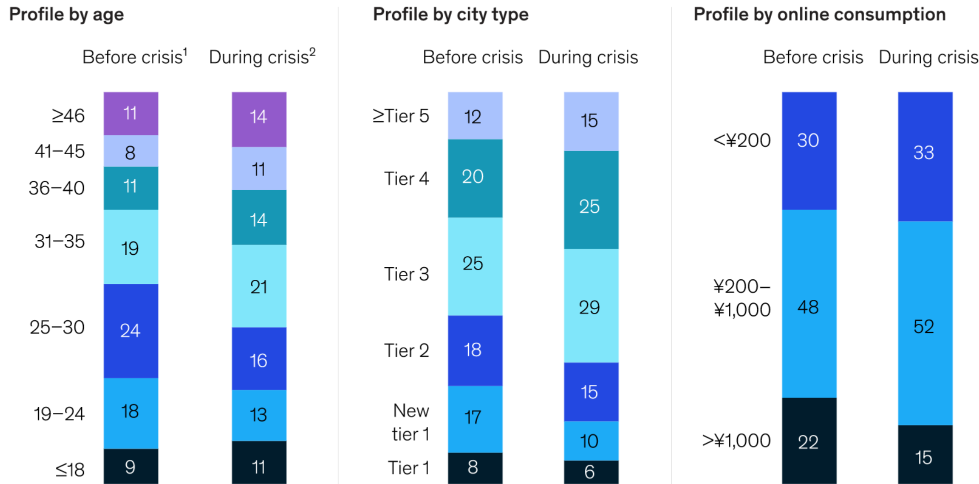
One of the many aspects that have been deeply transformed are fashion weeks and shows. Runways have always been not only part of marketing strategies, essential public events, and a necessary moment for advertising and public relations, but also a huge part of companies revenues and brand image. To avoid lacking on that front, and still have some kind of way to connect to their customers, many brands live streamed their fashion shows online. Even though it is expected to return to normality in the future, some changes in consumer habits will remain permanent. For this reason, luxury brands started integrating with technology more. It has not been, and still not is, an easy transition, because customers are used to extraordinary service in store and they expect something of the same quality through other platforms.

They seek a creative and differentiated product offering, together with a customer experience that is both personalized and integrated across physical and digital distribution channels.

In spite of the difficulties, to satisfy customers' needs, brands have been drastically increasing their use of online platforms, and online sales contribution to total personal luxury goods sales doubled. Hence, it is crucial for brands to allocate enough resources to create a digital reality that has a high acceptable level, companies will be successful if they will be able to offer a hybrid experience. Even though these changes might be hard

to implement, it is possible to witness how e-commerce is already attracting new segments, especially in China as it is shown by the following table.

E-commerce user profiles before and during COVID-19 crisis in China, %



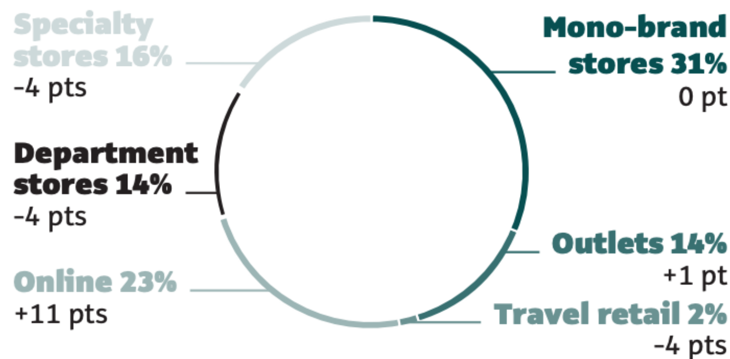
[1]Data from Jan 14, 2020, to Jan 31, 2020.
[2]Data from Feb 3, 2020, to Feb 16, 2020.
Source: QuestMobile

McKinsey & Company

Source: QuestMobile Figure: McKinsey&Company

Chinese consumers will continue to be the main growth driver but, because of the pandemic, luxury consumers in general are becoming more digital-oriented and are leaning increasingly toward innovation, especially as younger populations, like Y and Z, enter the market. Online sales of luxury goods grew at a record pace in 2020 and were up by 50% on a reported basis, representing the equivalent of five years of growth. As e-commerce became the market's leading sales format in 2020, driven by Asia, it is fundamental that companies are able to meet the expectations of a new type of consumers, whose buying decisions are more and more influenced by digital technology and buying habits that require a wider use of digital tools. Consequently, companies should invest in features like online editorial and marketing content, social media and including online shopping platforms, virtual interactive reality, AI, and mobile payments.
In spite of the fact that stores are slowly reopening, and in store sales are recovering, the new e-commerce reality will permanently be implemented alongside the physical one.

According to research from consultancy Bain and Company, online is expected to account for up to 30 % of the luxury market by 2025.
In support of these results, Kering reported that in 2020, its online sales accounted for nearly 23% of their total sales.



Source: Kering’s financial document 2020

Predictions for the future, especially for the year 2021, seem to be hopeful, as the world is slowly recovering. All of the factors that have been affected during 2020, are supposed to improve.
As the global economy gradually goes back to normal, GDP is forecasted to increase by 5 % (Oxford Economics, 2021).
If the vaccination campaign keeps being effective, it will be possible to travel again. Because of this, more and more people are expected to fly, increasing air traffic by more than 50% (IATA).
Less clear are the effects on the purchases of luxury goods in international markets. As it has been previously mentioned, local markets have increased their profitability, due to imposed travel restrictions. It will depend on the capacity of traditional luxury destinations, for example Hong Kong, to redefine its reputation as an exclusive location. New trends for this aspect are uncertain and will be influenced by consumers' new preferences and government actions. The distribution of sales and profits geographically will probably not be homogenous across countries, with Asia continuing to be the leader of this recovery. Global demand as a whole is expected to rebound by 2021, while still

not reaching the levels that it had in 2019, bouncing back to an average of 16% to 18% (Kering, 2020).

Additional predictions have been made for the longer term, regarding the years up to 2025.

According to Bain and Altagamma, the personal luxury goods market is expected to resume an annual growth rate of nearly 10% between 2020 and 2025, reaching €330 to €370 billion by the end of that period. This represents annual average growth of 10% to 15% between 2020 and 2022, and of 8% to 14% between 2020 and 2023.

This forecasted growth is expected to be possible thanks to upper-middle class consumers' purchases, especially in China, where clients could represent 46% to 48% of the worldwide personal luxury goods market in 2025; most importantly to generations Y and Z which are expected to account for 180% of growth; the development of new distribution channels, expected to account for more than 30%; and an increase in high-spending consumer classes such as high-net-worth individuals (HNWIs). The latter, according to Bain's estimates, ultra-high-net-worth individuals (UNHWIs) already represented 30% of the luxury market in 2019 and their share will continue to grow.

All of these trends are expected to drive an increase in the number of luxury market clients from c. 380–390 million in 2019 to c. 450 million in 2025 (Kering, 2020).

1.5 Conclusions

This first chapter has tried to give a general interpretation and understanding of the concept of luxury by presenting the different definitions and conceptions attributed to it, as well as providing an overview of the luxury sector, its main characteristics, its biggest competitors, and the strategies and conditions necessary to gain and maintain a successful position.

Moreover, an analysis of the negative and positive consequences of COVID-19 has been carried out, displaying the effects, both economic and social, of the previous years and portraying the forecasts for the near future.

It has been highlighted how the following years represent a glimmer of hope for the recovery of the global economy, and especially of the luxury sector, along with all the changes that will be encountered.

Since mergers and acquisitions represent the main expansionary strategy adopted by luxury companies, and a phenomenon of great extent, the following chapter will analyze the reasons why firms choose this approach, as well as the risks and the advantages it entails. Still nowadays firms prefer an external growth strategy conducted through M&A operations to affirm themselves into a sector and to survive inside a market that is increasingly becoming oligopolistic.

The next chapter will not only present M&A in general, but it will also explain how they have been used by the main market leaders, with a special analysis for LVMH, to reach and maintain their dominant position in the luxury industry.

2. Mergers and acquisitions

2.1 Introduction

The main characteristic of the luxury industry is that it is highly concentrated, and this aspect has been increasingly growing throughout the years. This is a consequence of the fact that the luxury sector is characterized by high competition, so firms need to follow certain strategies to survive and be profitable. The success of a company depends on its capacity to gain and sustain competitive advantage over time. Growth is usually the most secure way to assure competitive advantage and it can be of two kinds: internal and external.

Internal growth is about resources, knowledge, and competences that the firm already owns, while external growth is focused on a dimensional factor, and has as its objective the expansion of the firm and the gain of a larger and significant market share. The latter is pursued through different strategies such as joint ventures, strategic alliances, and M&A operations. All of these methods consist in agreements between two or more entities, but are different based on the level of integration between the two counterparties.

Mergers and acquisitions are the most integrated kind, and are considered a profitable strategy to reach rapid growth and a high level of competitiveness, so they have been the most popular approach in the luxury sector, by being increasingly invested in since the mid-1980s. In previous years, firms would allocate the majority of their investments on internal growth and thanks to their flexibility to changes in the economic scenario, they were able to adapt, survive, and grow their competitive advantage. On the other hand, more modern market conditions do not allow companies to rely exclusively on internal expansion because of the substantial financial resources needed, that are nowadays owned only by a few firms. In fact, "year after year, this process increased the level of the concentration of the luxury fashion industry, especially in Europe, where several smaller family businesses are located. These firms, such as Gucci or Fendi, have a strong brand image, reputation, a clear value proposition and positioning but also lack the resources to face threats and opportunities mainly related to the emergence of new markets and new technologies" (Cabigiosu, 2020).

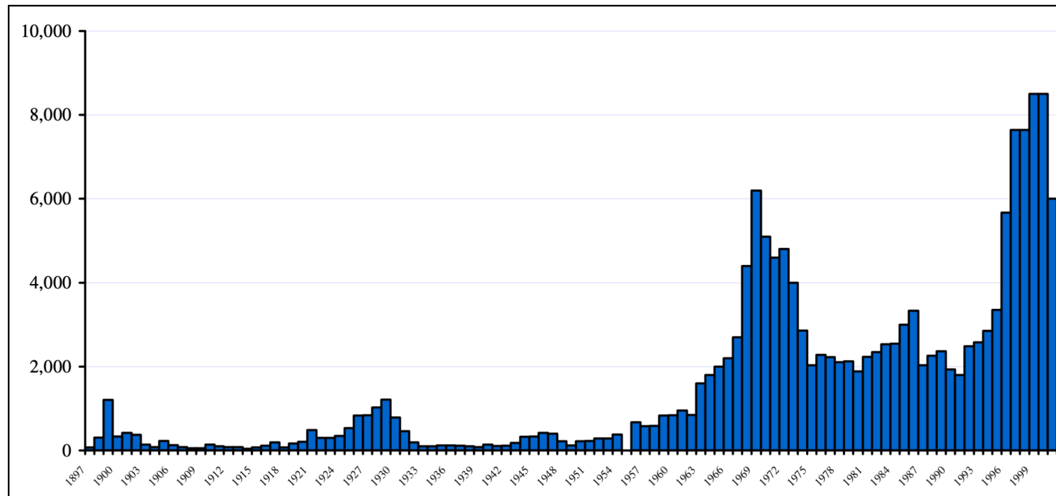
M&A are normally classified as extraordinary finance operations that lead to a dimensional growth of the company.
The following chapter has the purpose to define M&A operations, their risks and advantages, the different kinds that exist, as well as the reasons behind firms' decisions to adopt them, and the different disposable payment methods.

2.2 What are M&A?

"Mergers and acquisitions (M&A) is a general term used to describe the consolidation of companies or assets through various types of financial transactions" (Hayes, 2021).
They are usually classified as extraordinary finance transactions, exploited by firms to expand, and in the simplest case, involve two firms, one that acquires and one that is acquired.
Often, the terms merger and acquisition are thought to be the same thing, but they actually differ in meaning. An acquisition is a financial transaction between two companies, in which one buys the other, establishing itself as the owner. In a simple acquisition, the acquiring company obtains the majority stake in the acquired firm, which does not change its name or alter its organizational structure.
Differently a merger is a process in which two firms of similar size agree together to become a new different entity that is jointly owned and operated. In this situation, the boards of directors of the two companies approve the combination and seek shareholders' approval.
The phenomenon of M&A has been increasingly growing, even though it has never followed a linear trend, always presenting itself in a cycling way, and being mostly identified in the American and British markets. Thanks to the studies of Martynova and Renneboog (2008), who analyzed more than a century of transactions in the U.S., it is possible to organize the evolution of M&As in six big cycles (Martynova & Renneboog, 2008).
This research has moreover highlighted the fact that each cycle has occurred in periods of economic recovery, after a period of crisis or recession of the American economy. In addition to that, it has been shown that the waves normally fall in periods of expansion

and booming stock markets. In fact, it is notable that all waves ended with the collapse of stock markets. These results make it safe to say that M&A waves can successfully occur only if the external capital market is in good conditions.

US merger waves since 1897 (total number of deals)



Source: “Century of Corporate Takeovers: What Have We Learned and Where Do We Stand?” Ecgi. Global.

Recently, many increasing M&A operations trends have been recorded, especially in 2018 where 265 transactions have taken place, of which 73 focused on luxury fashion and took place mainly in Europe, a total that represents a 22% increase compared to the previous year. Personal Luxury Goods is the area that has witnessed the biggest amount of deals, thanks to the Cosmetics & Fragrances sector which led to a growth of 57% (*Lusso, boom di operazioni M&A nel 2018*, 2019).

At the beginning of the 21st century, M&A operations reached impressive numbers, and in the last twenty years, they have more than doubled. “LVMH, Mayhoola, Kering and Michael Kors are examples of groups that have undertaken the most important and expensive acquisitions in the past twenty years, creating portfolios of brands extremely diverse to make their market position robust” (Cabigiosu, 2020).

Nowadays, large groups continue acquiring fashion companies with profitable resources and brand images. They provide them additional financial sources to promote their brand

and increase their size and market share. Companies have begun acquisitions of new and consolidated brands to improve and differentiate their identities and continue to expand by serving multiple segments.
Some characteristics of the luxury industry can help to understand merger motives: high gross margins and different operating costs. Hence, firms exploit synergies advantages including the creation of common distribution and manufacturing networks, economies of scale and scope, as well as gains of market power that, as it has been mentioned, is a fundamental stimulus for the consolidation activities observed during the last two decades.
As it has been mentioned many times, the luxury panorama is dominated by two main leaders, LVMH and Kering, which owe most of their success to the profitable implementation of M&A.
The name LVMH itself was generated from the merger between Moët Hennessy and Louis Vuitton in 1987. In 1988, LVMH acquired Céline and from 1999 onwards, it started a comprehensive internationalization process, purchasing 25 leading brands. In the fashion and leather goods division, the Maison has 18 brands which, in 2018, recorded sales of €18,455 million: Berluti, Céline, Christian Dior, Emilio Pucci, Fendi, FENTY, Givenchy, Kenzo, Loewe, Loro Piana, Louis Vuitton, Marc Jacobs, Moynat, Nicholas Kirkwood, Patou, Pink Shirtmaker and RIMOWA.
Kering's most important acquisitions have been those of the Gucci group and Yves Saint Laurent in 1999. This was followed by those of Bottega Veneta and Balenciaga. Partnerships were also established with artists such as Stella McCartney and Alexander McQueen.
Some of the most valuable acquisitions in the luxury sector were the Kering purchase of 42% of the Gucci Group for $3 billion in 1999, that of Christian Dior in 2017 for $13.7 billion by the Arnault family (Cabigiosu, 2020),
and the Michael Kors acquisition of Versace for €1.83 billion in 2018 (Euronews, 2018).
It is interesting to observe the effects that the announcement of M&A operations has on the stock market. It has been shown that the positivity level at which markets respond is directly proportional to the perceived brand image, so the higher esteemed and the more familiar a brand already is, the better the market reaction. In spite of that, since Europe is

dominated by two huge conglomerates, and so the luxury sector can be considered almost as an oligopolistic market, M&A operations can actually raise concerns, as customers worry about market power abuse and unreasonable price-settings.

To categorize the purposes of M&A, Weston and Halpern developed two classes of theories. The first class summarizes explanations referring to the overall non-profitability of M&As, aimed at sales and control growth, but eventually emerging gains are supposed to be offset by transaction costs. The second category of theories encompasses operations aimed at maximizing value attempting to explain different types of capital market reactions. There are different financial motivations such as diversification effects that are expected to reduce bankruptcy costs, and economic reasons include the expected exploitation of synergy potentials. Another motivation might be the attempt to take advantage of information asymmetries in case the acquirer has information about the target firm other market actors have no access to. Finally, corporate control can be considered a driver, which requires that the target equity has been underperforming, and is applicable if the acquirer intends to benefit from simple control measures such as management replacements after deal completion.

2.3 Types of M&As

There are many general distinctions between the different types of mergers and acquisitions operations. The classical classification is done depending on the nature and the direction of the operation, as well as the relationship between the two counterparties. The different types of mergers and acquisitions that are identified following the previous criteria are: horizontal, vertical, conglomerate, and roll-up (which are the most common types), and congeneric, market-extending, and product-extending (which are less popular).

Horizontal mergers seem to be the most diffused, and they happen between two companies that are in direct competition and share the same product lines and markets. Normally, when companies operate in the same scenario, competition levels are higher, which leads to greater synergies, potential gains and market share for firms that decide to

pursue this type of strategy. The latter often occurs because larger companies try to exploit larger volumes of production through economies of scale and to gain competitive advantages.

Vertical ones involve two or more companies that provide different supply chain functions for a common good or service. Most often, the merger is performed to increase synergies and gain more control of the supply chain process. Its advantages are reduced costs and increased productivity and efficiency.

A conglomerate is a corporation that is made up of a number of different, sometimes unrelated businesses. In a conglomerate, one company owns a controlling stake in a number of smaller companies all of whom conduct business separately and independently. Their purpose is to diversify business risk by being present in a number of different markets, although some of them prefer to participate in a single industry. Many conglomerates are thus multinational and multi-industry corporations, like LVMH and Kering. Each one of a conglomerate's subsidiary businesses runs independently of the other business divisions; but, the subsidiaries' managers report to the senior management of the parent company. The advantages of this strategy are risk diversification, lower operating costs, and fewer resources for the parent company. Roll-up mergers take place when an investor buys companies in the same industry and merges them together. This process consists in taking many small companies and combining them into a bigger entity. Often used to mitigate competition in markets that are fragmented, the positive effects of this type of merger are an increase in size, better positioning, and an easier opportunity for economies of scale. In addition to that, they are used to merge companies with complementary resources to offer a diversified and complete type of business. Congeneric mergers involve two companies that are in the same or related industries or markets, but do not offer the same products. In a congeneric merger, the companies may share similar distribution channels, representing synergies for the merger. The acquiring company and the target company may have overlapping technology or production systems which facilitates the integration process. The advantages would be for the acquirer who may see the target as an opportunity to expand their product line or gain new market share. Market- extending regards two companies that sell the same products in different markets, while product-extending two companies that sell different but

related products in the same market. An additional classification of mergers and acquisitions can be done depending on two different financing methods, purchase mergers and consolidation mergers. The former occurs when a company buys another company through cash or through another type of debt instrument. Usually, the acquiring company is more driven to conclude the deal because it is taxable, meaning that they can exploit tax benefits. These include the reduction of taxes payable by the acquiring company if assets are written up to the actual purchase price, and the gap between the book value and the purchase price depreciates annually. Consolidation mergers consist in the combination of two companies into a new entity, forming in this way a new company that is brand new and different from the original ones. Taxes are applied the same way as in purchase mergers. In addition to the above mentioned types of mergers, there is a category that differs from the others because of the objectives that it wishes to achieve. It is called an industry convergence M&A and involves a radically different kind of reconfiguration and companies that seem to belong to very different sectors. It consists in creating an industry and a business model based on the unproven assumption that resources of existing industries. whose boundaries are disappearing, can be pulled together and create profitable synergies. Even though the results might be very positive, implementation represents a big challenge for management. Not only buying and integrating smartly is fundamental, but also the intuition about whether an industries' boundaries are actually disappearing or not represents a huge risk because it is only theoretical and, if wrong, it will result in failure. Talking about mergers, the term takeover, which is commonly associated with the concept of acquisitions, needs to be mentioned. In fact, it is important to highlight the takeover bid, a type of corporate action where a company makes an offer to buy another company in exchange of cash, stock, or a combination of both. There generally exist four types of takeover bids: friendly, hostile, reverse, and backflip. The first type happens when both companies agree to cooperate and negotiate the terms of the deal. Both companies will approve the deal and recommend shareholders to vote in favor of the bid. A hostile takeover can happen in two different ways: it may involve the acquirer going directly to the target company's shareholders with the bid, or trying to replace the target's management team. Differently from a friendly takeover, the target company does not agree to go through with the

merger, and may try to implement certain defense strategies, such as poison pills or a golden parachute, to avoid the deal taking place. A poison pill consists in the attempt of the target company to make itself look less desirable and is usually quite effective as it also significantly increases the cost of acquisitions and creates big disincentives to avoid unwanted attempts. Instead, a golden parachute is a substantial benefit given to top executives if the company is taken over by another firm. After that, the executives are terminated as a result of the merger or takeover. Benefits can be of different forms such as stock options, cash bonuses, and generous severance pay. Golden parachutes get their name because they have the objective to provide a soft landing for employees that will lose their jobs as a result of the takeover. Hostile takeovers can be attempted through different strategies as for example a tender offer (a bid to purchase some or all of the shareholders' stock in a corporation), a proxy fight (shareholders join forces and attempt to gather enough shareholder proxy votes to win a corporate vote), or a substantial purchase of the company's stock in order to have enough control over it. The second to last type of takeover is a reverse bid, where a private company tries to buy a public corporation. Since the public one is already listed and traded on an exchange, this takeover can make the private company listed as well without having to go through the long and complicated steps of filing the necessary documents to complete an initial public offering (IPO). Lastly, a backflip takeover is a kind of bid in which an acquirer attempts to become a subsidiary of the target. After the implementation of the process, the acquirer retains control of the combined corporation, which normally keeps the name of the target. This type of takeover is very rare and it is normally used to help the acquirer which may be struggling in the market, by enhancing brand recognition. Hence, M&As strategies can be undertaken for many reasons but, in most cases, are caused by necessities or by the intention to reach a certain goal in a faster way by investing in underrated market companies. In conclusion, there are as many different types of M&As strategies as different desired objectives, and the following section has the purpose to analyze them.

2.4 Objectives

The process through which M&As are implemented is not standard as it depends on the desired objective. Normally, M&As take place only if they increase the value of the firm. Haspeslagh e Jeminson (Haspeslagh & Jeminson, 1992), explain through their book that a fundamental distinction between achievement and creation of value needs to be made. The former happens when there is a transfer of value from the target to the acquirer or when the latter can enjoy fiscal benefits. This consists of one of the steps that lead to the creation of value. The creation itself can exist only if both companies are successfully integrated. In general, the main motives for which M&As strategies are pursued can be divided into five basic goals : synergies, growth, increased supply-chain pricing power, elimination of competition, and tax purposes. The first is accomplished by combining business activities to generate an overall performance efficiency increase and costs decrease, due to the fact that each company exploits the other company's strengths. Growth is a very popular and desired goal that can be reached through mergers. The acquiring company has an opportunity to grow market share without investing too many resources. The third goal is accomplished through the buyout of one of the suppliers or distributors of the supply chain. This allows the business to eliminate an entire tier of costs. In fact, buying out a supplier, helps the company to save on the margins that the supplier was previously adding to its costs. Moreover, by buying out a distributor and gaining more power over the supply chain, a company is often able to easily ship out products at a lower cost. Another one of the main reasons for which a company decides to implement an M&A strategy is to reduce or eliminate competition. The acquirer can gain a larger market share and reduce competition by merging or acquiring its rivals. In spite of the benefits, it might be a costly operation since a large premium is usually required to convince the target company's shareholders to accept the offer. To lower the price, shareholders of the acquiring company usually try to sell their shares, in order to balance the acquirer paying too much for the target company. Lastly, companies perform M&As for tax purposes.This might actually represent an implicit rather than an explicit motive. For instance, the U.S. has the highest corporate tax rate in the world so, some of the best-known American companies have resorted to corporate “inversions”, a technique

that involves a U.S. company buying a smaller foreign competitor and moving the merged entity's tax home overseas to a lower-tax jurisdiction, in order to substantially reduce its tax bill (Picardo, 2019). In 2010, McKinsey&Company conducted a research highlighting the most popular reasons for which companies decide to implement M&As. In most cases, which account for 64% of the total, the necessity to acquire new resources, capacities, and competencies has been identified as the main driver. Following, 55% is represented by the attempt to expand in different markets and geographical areas. Lastly, the remaining 36% is generated by the desire to increase the size and gain a bigger market share. More in general, the decision of a company to merge with or acquire another company is driven by two types of reasoning: financial or strategic. The former justifies a M&A strategy only if it generates economic benefits. These results are obtainable only if the companies are worth more together than separately, and if the deal creates value by decreasing competition in a way that it would have not been possible otherwise. In spite of that, financial objectives are not the most common. In fact, the majority of the time, M&A strategies are implemented to reach strategic objectives as firms do not singularly own the necessary resources and, by merging together, are able to obtain them without spending a big amount of credit money. The latters are aimed at influencing the structure of the market or the sector in which the firms and their competitors operate. The main purposes are to increase barriers to entry and the creation of obstacles for competitors to reduce their number. In spite of that, there exist specific legal limits regarding the sizes of the merging companies. If the firms are too big, and so the magnitude of the new company exceeds certain thresholds, the operation might lead to the modification of competition inside the market. The effects of M&As influence both the capital structure and the market reaction. It is trivial that the acquiring company will have more long-term ramifications than the target company. For the latter, an M&A transaction gives its shareholders the opportunity to cash out at a significant premium, especially if the transaction is an all-cash deal. If the acquirer pays partly in cash and partly in its own stock, the target company's shareholders get a stake in the acquirer, and thus have a vested interest in its long-term success. The benefits for the acquirer depend on the deal size: the larger the potential target, the bigger the risk to the acquirer. A company may be able to withstand the failure of a small-sized acquisition, but the failure

of a huge purchase may severely put the firm in danger. After a M&A transaction, the acquirer's capital structure will be modified, depending on how the deal was designed. An all-cash deal will substantially decrease the acquirer's cash holdings. For this reason, all-cash deals are often financed through debt. While this method increases a company's indebtedness, the higher debt load may be justified by the additional cash flows contributed by the target firm. Another way to finance M&A transactions is through the acquirer's stock. In order to use stock as currency, shares must often be premium-priced and management of the target company needs to be convinced that accepting the acquirer's stock rather than hard cash is a good idea (Picardo, 2019). For what it regards the market reaction, the latter is very uncertain, as it can be favorable or unfavorable, depending on the perception of the validity of the deal. Normally, the biggest effect is recorded on the target company's shares that rise to a level close to that of the offer, if the latter represents a significant premium to the previous stock price. In some cases, it might happen that the target's shares will trade at a price that is superior to the offer one depending on some possible assumptions: either that the target company is desired enough to attract a rival proposal, or that the acquirer has underestimated the offer and has to raise it. On the other hand, it might happen that the target's stock actually trades below the offer price. This might happen when the payment is supposed to happen through stocks or through stocks plus cash, and so the price of the acquirer stock drops when the deal is announced. Generally, when a M&A is performed, the stock prices of both companies tend to move in predictably opposite directions, at least over the short-term. Since shareholders are the key to conclude the takeover, if the takeover bid equates to a lower stock price than the current price of the target company, it would not be in their best interest to authorize the deal. For this reason, most of the time, the target company's stock rises because the acquiring company pays a premium, in order to provide an incentive for the target company's shareholders to approve the transaction. In spite of that, there are exceptions to the rule. As it has been mentioned, if a target company's stock price recently dropped because of negative earnings, then being acquired at a discount may be the only solution for shareholders to compensate for the loss of their investments and gain part of them back. This happens especially when the target company is burdened with large amounts of debt, and cannot obtain financing from the

capital markets to reduce it. As it has been previously highlighted, the effects on the acquirer's stock are often negative after the acquisition, also for additional reasons than the previous ones. This might happen if investors believe that the premium paid is too high, if there are struggles in the management of productivity and the integration of different cultures in the workplace, if some issues regarding the timeline of the deal arise, or if additional debt or unforeseen expenses happen as a result. These effects are noticeable only in the short run, in fact, companies would not perform the transactions if they were not profitable in the long run. Hence, in the future, if the acquirer's management has been able to fairly value the target company and successfully integrate the two entities, its stock price is expected to significantly increase. From these results it is possible to notice how the announcement of a M&A deeply influences the market, triggering high volatility. Buying stocks during the uncertainty period could be as profitable as it is risky because, if for some reason the transaction is not concluded, investors lose. In addition to the effects on the external market, a merger also affects shareholders and the internal environment and organization of both firms. The shareholders of both companies may experience a dilution (decrease) of voting power because of the increased number of shares released during the merger process. This phenomenon is prominent in stock-for-stock mergers, when the new company offers its shares in exchange for shares in the target company, at an agreed conversion rate. The effect on shareholders of the acquiring company is minimal, as they experience a non significant loss of voting power, while that on the shareholders of the target company may be bigger as they suffer a drop of their voting powers. The internal organization of firms is also deeply affected by the new changes. Leadership positions are often modified, as well as rearrangement of executives and board members, while concessions are usually made during merger negotiations. As it has been shown, mergers and acquisitions strategies are associated with numerous advantages, and these often cloud the judgment of managers about the actual complexity of the process. The personal benefits and rewards, as well as the expected rise in the price of stock, often deceive directors' attention from their illusory appearance and from the many risks associated with the deal. One of these "traps" could be the misleading belief that since diversification is considered the fastest way to reduce risk, then it should also be

considered one of the main objectives to pursue. Even though this might be true, it is way easier for investors than for the firm. The former do not recognize the increased value of a diversified company and so are not willing to pay a premium for it in a perfect market where diversification opportunities are not limited at the individual level. An additional deluding scenario takes place when an acquisition of firms with a low growth rate is performed. Such an operation does not bring a real economic benefit, nor an increase in value, for either of the two counterparties. What often happens in this situation is that a false appearance of economic gain is created by financial managers, through a strategy called "bootstrap game". The counterparties hope that the bootstrap game will increase the post merger company stock price relying on the hope that investors who aren't carefully watching the actions of the company do not understand why earnings per share have increased. Instead of identifying an artificial increase, investors may believe the earnings per share increased because of real growth and gain created through the merger which in turn increases the value of the post-merger stock. The effects may lead to a temporary increase in stock price, even though it generally manifests in future years. "In order to maintain the earnings-per-share ratio at an artificially high level, the company would have to continue to expand by merger at the same rate. Once the company stops mergers and expansions, earnings per share will decrease and the stock price along with it"(Garcia, 2019). Lastly, the idea that two united companies might obtain loans at more favorable conditions than if they were two separate entities, is often a pitfall. This would be true in an efficient market because two firms that, if separate, do not reciprocally secure their own debts, after the merger are required to guarantee against the liabilities of the other, and is the reason why the assumption of an easier financing was born. In practice, this is not a complete benefit because the company is obliged to undertake the debts of the others if it desires a lower interest rate. The value of a liability is given by the difference between the value of a liability exempted from the risk of insolvency and the value of an option (put) of the investor's insolvency. From this definition, it easily follows that it is true that the merger increases the value of the obligation, but only through the reduction of the value of the option of the investor's insolvency. In conclusion, this paragraph has analyzed the reasons behind M&As strategies and their objectives, as well as the risks associated with them. In addition to the main three "traps",

there have been mentioned ten of the most common hazards that regard M&As. These include: overpaying for the target company, overestimating synergies, weak due diligence practices, integration shortfalls, little attention to culture and change management, overall lack of communication and transparency, failure to capture synergies, threats to security, unexpected costs associated with the deal, unforeseen market disruptions. The next section will analyze the value creation of such operations and why and how they are implemented in the luxury sector.

2.5 Value creation in the Luxury sector

Because of some of the specific characteristics of the luxury sector, such as big margins, potential synergies, common distribution channels, economies of scale and scope, and the possibility of increasing market share, M&As operations are quite popular in the industry. Starting in the mid 80s, because of the evolutive tendencies of the market, many firms have tried to reposition themselves. Due to the high competition, many companies started to expand, reaching the maximum historical number of transactions in 2000. As it has been previously shown, the four fashion market leaders, LVMH, Kering, Richemont, and the Swatch group, have accounted for the majority of such activity. By creating portfolios of products and brands, increasing diversification, and gaining large market share, the current structure of the luxury market is almost oligopolistic. Most operations have seen Italian investors as their actors, but in terms of value, the majority is generated by international ones. Kering and LVMH have performed some of the most valuable acquisitions in the sector. For example, in 1999, Kering purchased 42% of the Gucci Group for $3 billion), while LVMH has acquired Bulgari in 2011, and Loro Piana in 2013, for a value of 4.300 millions of euros in the first case and 2 billions in the second (D’Ascenzo, 2014).

Table 1: Details on luxury companies involved in M&A transactions

Company	Industy	Home Country	M&A Deal Involvements		Average Transaction Value (GBP)
			Acquiror	Target	
LVMH	Luxury Conglomerate	France	51	-	275,902,141
PPR	Luxury Conglomerate	France	36	1	565,817,749
Richemont	Luxury Conglomerate	Switzerland	6	-	1,607,500,000
Swatch	Luxury Conglomerate	Switzerland	6	1	n.a.
Christian Dior	Fashion	France	1	1	39,300,000
Escada	Fashion	Germany	2	-	10,800,000
Etienne Aigner	Fashion	Germany	-	2	6,561,847
Gucci	Fashion	Italy[20]	19	19	961,064,771
Hardy Amies	Fashion	United Kingdom	1	2	743,400
Hermès International	Fashion	France	3	-	10,563,333

Source: "Wealth creation by M&A activities in the luxury goods industry". European Business School, Department of Finance.

The reason why most of the attention is focused on the fashion industry is because it represents the most active sector in terms of mergers and acquisitions. KPMG advisory has conducted research that shows how "the fashion segment has recorded in 2011 the peak of a multiple of 14.7 times the gross operating margin (EBITDA), against the smaller 7.6 times of retail and 7 times of food & beverage" (D'Ascenzo, 2014). The main leaders of the luxury industry are proof that M&As have mostly positive consequences. In fact, the results of operation have significantly gotten better after the conclusion of the deals. These successful outcomes are probably due to the consolidation, widening, and diversification of products and brands portfolios. Investors are deeply interested in highly diversified conglomerates because it is easier and faster for them to put their money into an already diversified and well market positioned company, instead of diversifying their portfolio through more numerous and smaller investments. The evaluation of an M&A strategy in the luxury industry, and more specifically in the fashion sector, needs to be conducted in relation to the specific characteristics of the market in which it has to be performed. A careful analysis of the process of M&As in the luxury industry is characterized by the difficulties that managers have to encounter in the

decision making process and by the main factors that distinguish this sector from the others. If mistakes are made during the evaluation period, consequences might include the failure of the entire operation. Generally, there are some phases that characterize the decisional process, starting from the identification of an opportunity on the market, the evaluation of possible alternative targets with their respective specific characteristics, and lastly the final choice of the firm and the opening of negotiations. It does not always happen that all of the steps are followed, so decision making processes are conventionally divided into five categories: nova, off-the-shelf, appraisal, historical, search, which are organized based on complexity and completeness. The most suitable process is selected from time to time depending on the specific characteristics of the sector. Since the luxury sector is mostly based on brand image and perception, it is very important that M&A operations are considered stable and credible. Some strategies such as "idea-driven" and "reframing" are used to pursue this objective, and consist in defining in advance all of the details of the operation to minimize uncertainty. If a different goal is desired, for example to increase innovation, some techniques like "issue-based" and "object directed process" are selected; they try to define the problem without setting tight margins for operations. Since competition is high, and everything moves quite fast in the luxury sector, firms need to quickly finalize deals, opting for processes like "ready made". Through the latter, it is possible to identify firms in the market that are ready to be acquired or merged with. To finalize the deal, it is important that the targeted company respects all of the criteria set by the acquirer and that somehow creates additional value. Decision making processes are not only chosen based on the objectives that the firm is trying to achieve, but it also depends on the financial resources available and the preferred payment method. The following section will present and analyze the latter as well as providing an overview of M&As transactions and processes.

2.6 Payment Methods

As in every economic transaction, the latter is performed if and only if the estimated benefits exceed the estimated costs. The calculations depend on the type of payment method chosen by the firms. To determine what payment method suits the transaction best, it is necessary to analyze the specific characteristics of the counterparties and the purpose of the agreement. The two most diffused payment methods are stock-for-stock and all cash or all stock. “A stock-for-stock merger occurs when shares of one company are traded for another during an acquisition” (Gallant, 2020). This type of transaction is usually the choice of companies that do not have and do not plan to raise significant amounts of capital, because it is cheaper and more efficient, as it is often performed as a combination of shares and cash. There are different options through which the acquiring company can pay for the assets. The acquirer can exchange cash for the shares of the target company and pay each shareholder a specific amount for each share. Another way is for the acquirer to exchange with the target company its own shares at a predetermined conversion rate. The latter “is the number of common shares received at the time of conversion for each convertible security. The higher the ratio, the higher the number of common shares exchanged per convertible security” (Hayes, 2020). In addition to that, deals can be finalized with a combination of cash and stock or with all stock compensation, conventionally called a stock-for-stock merger, which is not taxable. Moreover, most of the time, a stock-for-stock is not performed in full. It is not uncommon that a portion of the transaction is completed through a stock-for-stock merger while the remainder is completed through cash and other equivalents. “An all-cash, all-stock offer is a proposal by one company to purchase all of another company's outstanding shares from its shareholders for cash” (Kenton, 2020). As it has been mentioned earlier, shareholders are the main actors needed to finalize an acquisition. To prepare them in the best way, the acquirer company tries to convince the most uncertain shareholders to agree, offering a premium over the current price of the shares. The latter might happen also in all cash transactions because a share price is always negotiated for the target company. This type of payment is often very profitable for the shareholders of the acquired company who become able to make a capital gain, (an increase in capital asset’s

value), if the new company is believed to have a higher value than what it had before the transaction. This happens even though some decisions, for example employee cuts, might represent a loss for the target company, but a profit for the new combined entity, which is able to gain higher profit margins by lowering costs. If this payment method is chosen, it is possible that the acquiring company does not have all the cash needed to finalize the deal right away. To solve this problem, the acquirer can issue new equity, or request a loan. In the first case, through the issuance of new debt instruments, the company can raise cash from investors who buy the new securities and that will need to be paid the principal plus interest in the future, more specifically at maturity. An alternative method to raise cash is through an IPO, but this can be done only if the firm is not already public. In the case of a shortage of cash, the acquirer can borrow it from a bank or a financial company. To establish if asking for a loan would be a profitable solution, the company needs to conduct a cost-benefit analysis, since a transaction of the magnitude of the amount needed for a merger would be quite complex, necessitating more than one bank, and having high interest rates. The main risk of this financing method is that the debt might be transferred to the new entity, preventing it from receiving additional loans in the future, and from investing in other projects before having repaid the interest of the loan. Additional complicating factors might present in an all-cash transaction, such as different exchange rates if the companies are located in different countries, and taxable earnings. When a payment is completed in cash, the cost of the acquisition is equal to the difference between the payment made and the current value of the target firm as an independent entity.

The formula can be summarized as follows:

$$Cost = cash - VAb$$

The payment and the resulting acquisition will be performed only if the economic benefits are greater than the economic costs, and the difference between them represents the net value. The cost of the deal is the actual amount that the acquirer pays, which does not necessarily reflect the real value of the target. If the latter is public, the starting price

might be based on the market price multiplied by the number of outstanding shares, leading to:

$$\text{Cost} = (\text{cash} - VMb) + (VMb - VAb)$$

where VMb represents the premium and VAb represents, as before, the value of the target company as a separate entity. If, instead, the selected payment method is stock-for-stock, the cost will depend on the value of the shares of the new entity. This will be represented by:

$$\text{Cost} = N \times Pab - Vab$$

Where N is the number of outstanding shares and Pab the price of each. In the United States, after a M&A operation is concluded, there are some legal steps that need to be taken. The most important one is the filing of the SEC Form S-4, (or Registration Statement), by a publicly traded company with the Securities and Exchange Commission (SEC). Its purpose is to record every data associated with a merger or acquisition. This form needs to be filed also when companies are exchanging securities for cash.

2.7 Conclusions

As it has been shown, to successfully implement and complete an M&A strategy is not easy. The operation itself is very complex, and the lack of complete and precise information, as well as the failure to profitably integrate the two entities, result in failure. In fact, only 20% of the total M&A operations performed are concluded efficiently. Many reasons might lead to fiascos, having excessive security, incomplete information, failure to integrate, and external influences as the main ones. If meticulous attention is applied to the process, and managers' desires do not cloud their rational judgement, success is more likely to occur. As it has been highlighted, one of the main objectives of M&As is the expansion of companies, especially in the luxury sector, due to its highly competitive structure. The eagerness to reach this objective often leads managers to push the

transactions, without a comprehensive understanding of the details and the complex implications of the deal as a whole. The lack of understanding of specific factors, as well as poor knowledge, and/or inefficient planning, causes errors starting in the initial stages. The result is the ineffectiveness of the whole operation, which in turn creates a vicious cycle, which is the main reason why M&As happen in waves. An M&A operation can be considered successful if it creates value, and it has been shown that, in the latest years especially, this has been the case. In fact, in spite of the risks and the numerous elements that need to be taken under consideration, the number of M&As operations in the luxury industry is continuously growing. The purpose of this chapter has been to present the main characteristics of the mergers and acquisitions phenomenon, the different existing types, their payment methods, the reasons behind them, and the associated advantages and risks. On the other hand, even though the given panoramic has been quite exhaustive, it cannot be applied in the same way to every sector. Hence, the following and last chapter of this paper, will further analyze the opportunities and dangers associated with M&As, taking into account a specific case. Starting from the creation and the success of one of the main leaders in the luxury industry, LVMH, it will analyze the numerous acquisitions performed by the latter, focusing particularly on the last chronological one, which is the acquisition of Tiffany & Co, finalized in 2020.

3. LVMH: a case study

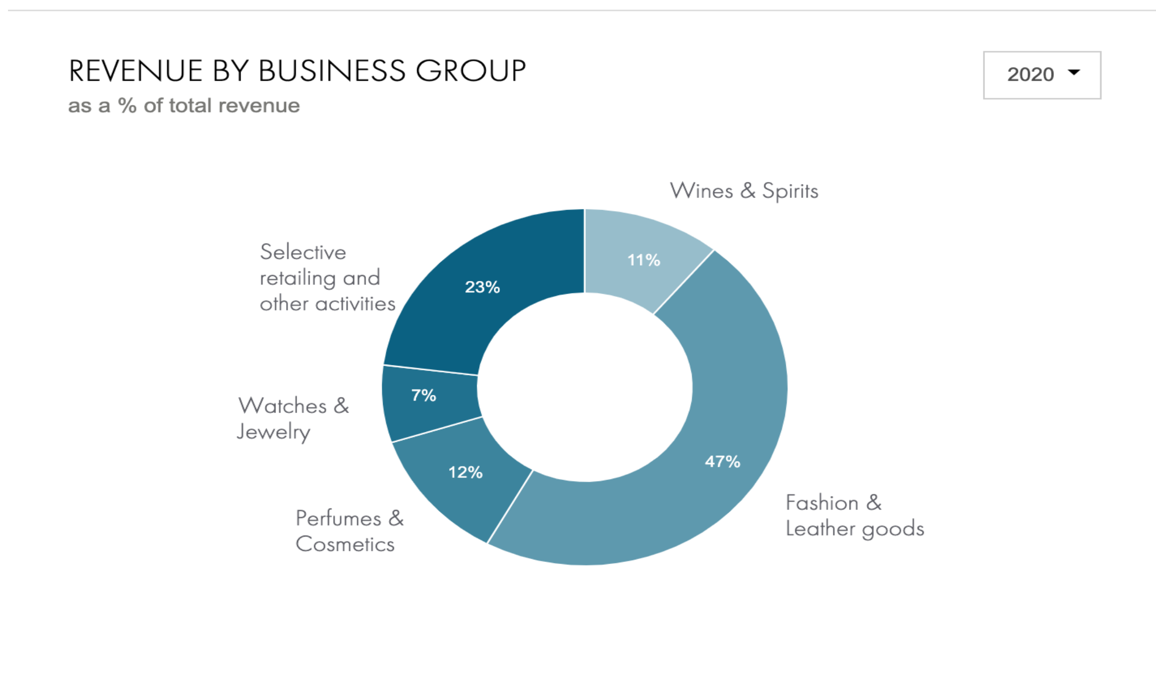
3.1 Introduction

Throughout this paper, it has been reported many times how the luxury sector scenario is dominated by two huge conglomerates, LVMH and Kering. This chapter has the purpose to analyze the former, which is not only a leader in the market, but also one of the most active firms in the implementation of mergers and acquisitions strategies. In fact, the name LVMH itself has been originated by the merger between Moët Hennessy and Louis Vuitton, which took place in 1987. Throughout the years, the company continued its expansion by performing more M&As activities, and now counting 76 brands (generating revenues of about $59 billion in 2019), with the newest one being Tiffany & Co (Davis, 2020). LVMH is a remarkable example of how to elude the risks associated with M&As strategies and use the latter as a successful way to expand and maintain competitive advantage and a leading market position. The conglomerate's achievements can be attributed to its admirable capacity of managing an extensive portfolio of brands, allowing each of them to preserve its identity and positioning, and only exploiting the common benefits and revenues. In the next paragraphs an analysis of the history of the group will be conducted, as well as the main reasons for its success, leading to its last accomplishment, the acquisition of Tiffany & Co., which has been concluded in 2021. A special focus will be devoted to the motives that brought to the implementation of this deal, how both firms behaved during the negotiations, and what were the risks and opportunities associated with such a transaction. Lastly, it will try to highlight the recent benefits generated by this deal, even though there has not been enough time to conduct an extensive analysis, since the acquisition has been finalized only a few months ago.

3.2 What is LVMH?

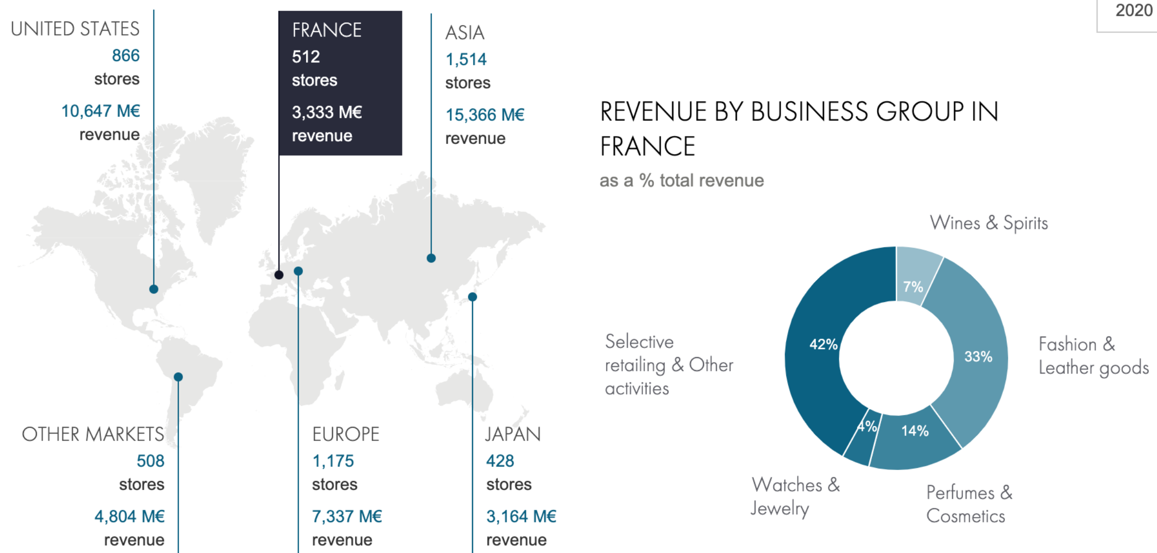
As it has been mentioned, LVMH was generated by the merger of two firms, Louis Vuitton and Moët Hennessy. Hence, to provide a more complete picture, it is necessary to briefly analyze the history of these two parent companies. Louis Vuitton takes its name from its founder, who gave it life in 1854, and its success has been rapidly increasing since then. In fact, only one year later, in 1855, he opened his first international store, based in London. After the death of Louis Vuitton, in 1892, his son, Georges, succeeded him, taking control of the company. His intention and vision were to shape the firm into an international corporation. Since many competitors had been trying to imitate the company and its designs, in 1896, the organization made a worldwide patent on the Monogram Canvas signature, also launched in that year, and still one of the main symbols of Louis Vuitton's designs. Georges tried to expand his project internationally and opened many stores all over the world and by 1913, the Louis Vuitton Building opened on the Champs-Elysees, being the largest travel-goods store in the world at the time. After that, maisons also opened in New York, Bombay, Washington, London, Alexandria, and Buenos Aires. An important milestone for the firm happened in 1987, through the creation of LVMH where Moët et Chandon and Hennessy, leading manufacturers of champagne and cognac, merged respectively with Louis Vuitton to form the luxury goods conglomerate. This event led profits for 1988 to increase by 49%. By 1989, Louis Vuitton came to operate 130 stores worldwide, and continued its trend of acquisitions, while nowadays the company is present in 50 countries and owns more than 460 stores worldwide (Wikipedia contributors, 2021). The other leader that originated the merger was Moët et Chandon, which was established in 1743 by Épernay wine trader Claude Moët. The company took its final name in 1833, after Pierre-Gabriel Chandon de Briailles, joined the company as a partner. The firm's success rapidly increased thanks to its clientele of nobles and aristocrats. This tradition has been kept to this day as Moët & Chandon holds a royal warrant as supplier of champagne to Queen Elizabeth II. In 1971, Moët & Chandon merged with Hennessy Cognac, and then with Louis Vuitton in 1987 forming the LVMH (Louis-Vuitton-Moët-Hennessy) group (Wikipedia contributors, 2021a). The propensity to expand through M&As operations, started in 1988 with the

acquisition of Givenchy, a luxury fashion and perfume house. Thanks to the leadership of the owner, Bernard Arnault, LVMH has acquired many companies, now owning a portfolio of more than 70 brands. The group, led by the particular vision of Arnault, bases its main expansionary strategy and owes its success to the implementation of M&As operations aimed at taking control of big luxury brands. What makes LVMH so unique and able to maintain its significant market share is the strategy of letting the subsidiaries be managed independently, being divided into six branches: Fashion Group, Wines and Spirits, Perfumes and Cosmetics, Watches and Jewelry, Selective Distribution, and Other Activities. In spite of the complex structure of the conglomerate, each of the divisions behaves as an autonomous unit having its own manager, while still being under the general control of LVMH. The fashion segment is one of the most important and profitable, and it owes its astonishing results to the acquisition tool. The synergies that have resulted from these strategies constitute one of LVMH main advantages through a significant reduction of costs.



Source: “Group key figures” - LVMH investors webpage

In spite of that, most revenues are still generated by Louis Vuitton, whose products' demand often exceeds the available supply which leads to the creation of waiting lists for certain items that increase the brand's exclusivity and prestige. LVMH has also been able to expand its customer base by acquiring some American brands, which had a more juvenile style. The latter move allowed the company to generate a growth rate which exceeded by more than double the industry average, while decreasing materials' costs by 20%.



Source: "Group key figures" - LVMH investors webpage

LVMH is now one of the most profitable companies in the luxury industry, with revenues of 53.7 billion euros as of 2019. As it has been shown, its success was generated by many acquisitions and is sustained thanks to the firm's capacity of letting them behave

independently, while still exercising a certain degree of control. In the following sections, the reasons, benefits and risks of the performed acquisitions, especially the controversial Tiffany & Co. one, will be analyzed.

3.3 LVMH acquires Tiffany & Co.

Mergers and acquisitions represent the fundamentals of the financial strategy of LVMH. The conglomerate's latest move has been the acquisition of Tiffany & Co., a colossus in the luxury jewelry and specialty retailer, which has been concluded at the beginning of 2021. To better understand the reasons that led to the acquisition, it is necessary to explore Tiffany & Co.'s history. The iconic company is headquartered in New York City and sells jewelry, sterling silver, china, crystal, stationery, fragrances, water bottles, watches, personal accessories, and leather goods. Tiffany's diamond and sterling silver jewelry are what made the company famous as the Tiffany Setting ring design, conceived by founder Charles Tiffany, became a symbol of luxury and exclusivity. As it has just been mentioned, Charles Lewis Tiffany founded the firm in 1837, but the latter reached its success in the early 20th century, under the artistic direction of his son Louis Comfort Tiffany. Tiffany is now a multinational company which, by 2019, operated 326 stores globally in countries such as the United States, Japan, and Canada, as well as Europe, the Latin America and Pacific Asia regions (Wikipedia contributors, 2021b). Tiffany is now one of the most recognizable and classic brands, also thanks to its signature color and diamond shaped engagement ring. It has gained its popularity by being mentioned in various works, such as the renowned movie *Breakfast at Tiffany's* starring Audrey Hepburn who became one of the firm's main symbols.

Tiffany and LVMH reached a finalized deal at the beginning of 2021, when the acquisition was officially concluded. In spite of that, the process was quite controversial.

Arnault has always been very determined to acquire the iconic American brand and, before the pandemic, was willing to pay up to $135 a share. In spite of that, COVID-19 had an impact on the demand of luxury goods, making Tiffany's share price drop by almost 9%. In the light of these updated facts, LVMH declared to not be able to acquire Tiffany at that moment, and asked for a delay of almost a month for the closing of the

deal. The French conglomerate tried to justify its decision by also citing a letter from the French foreign affairs' ministry where he suggested postponing the operation because of the United States' threats of taxing French products. In response, Tiffany sued LVMH in a Delaware court on the grounds of the latter's intention to deliberately block the process of obtaining Antitrust approvals for the acquisition in order to renegotiate the price, and seeking to force the conglomerate to respect the initial deal. As a result, LVMH intended to countersue the American brand on the basis of a crisis mismanagement, caused by Tiffany's negative earnings during Covid-19. In spite of that, the two counterparts have been able to solve any legal controversy, and the respective BODs approved the transaction's terms and obtained all of the required permissions (Tg24, 2020). As a matter of fact, they obtained Antitrust approval, as both of them already operated in the same market segments and their combined activity would have not led to an increase of market share of one of the two counterparties substantial enough to reduce competition. It is curious to observe how the acquisition happened during a period of economic crises. It was indeed mentioned in the previous paragraphs, that empirical evidence shows how M&A operations happen in waves during times of booming economy. In this specific case, the agreement can be justified by the ability of LVMH to exploit unfortunate market conditions to negotiate itself a much more convenient compromise.

De facto, if the deal were to be closed respecting the initial offered price, the acquisition would have cost $16.2 billions. But, as it has been explained, due to the negative effects caused by the pandemic, and the crises that distressed the economy, the offer was lowered $131.5 per share, for a total of $15.8 billions all paid in cash (Caruso, 2020).

3.4 Reasons for acquisition

The results of the acquisition will be analyzed in the following sections, so it is now necessary to first present the reasons that pushed LVMH to acquire the iconic American company. Tiffany & Co. is a multinational, operating more than 300 retail stores worldwide as part of its omnichannel approach. According to Alessandro Bagliolo, Tiffany's CEO during 2019, the latter year was one of the most profitable, boasting net profits of $586 millions, which made the firm a very attractive target for the French giant.

In addition to that, 2018 generated very positive results in many geographical areas, especially in the United States. In fact, the latter represents the sector in which Tiffany has its biggest presence and amount of sales, and from which it generates most of its revenues, which amount to almost half of the firm's total profits. The company also had great outcomes in the Asia-Pacific region, most of which were generated by China. Unfortunately, in spite of the previous astonishing results, Tiffany has not been spared from the negative effects of the pandemic. In fact, in 2020 net earnings of $541 million were 8% lower than the prior year, results that led LVMH to reconsider its initial offering price (Tiffany Co, 2020).

TIFFANY & CO. AND SUBSIDIARIES CONDENSED CONSOLIDATED STATEMENTS OF EARNINGS
(Unaudited, in millions, except per share amounts)

	Three Months Ended January 31,		Twelve Months Ended January 31,	
	2020	2019	2020	2019
Net sales	$ 1,357.8	$ 1,320.6	$ 4,424.0	$ 4,442.1
Cost of sales	498.5	478.6	1,662.1	1,631.1
Gross profit	859.3	842.0	2,761.9	2,811.0
Selling, general and administrative expenses	590.4	573.6	2,029.3	2,020.7
Earnings from operations	268.9	268.4	732.6	790.3
Interest and other expenses, net	10.6	11.9	42.3	46.8
Earnings from operations before income taxes	258.3	256.5	690.3	743.5
Provision for income taxes	57.1	52.0	149.2	157.1
Net earnings	$ 201.2	$ 204.5	$ 541.1	$ 586.4
Net earnings per share:				
Basic	$ 1.67	$ 1.68	$ 4.47	$ 4.77
Diluted	$ 1.66	$ 1.67	$ 4.45	$ 4.75
Weighted-average number of common shares:				
Basic	120.4	121.7	121.1	122.9
Diluted	121.2	122.1	121.6	123.5

Source: "Tiffany Reports Fourth Quarter and Full Year Results" - Nasdaq 2020

Tiffany & Co. 's price drop increased its desire to be acquired by LVMH, as it forecasted that the acquisition would help them restore their losses. As proof of this, only the announcement of the deal itself generated a trading up of 2.58% for LVMH's share price, which bumped up to $126.07. After the disputes, and having analyzed the pros and cons of the operation, LVMH officially announced it had acquired 100% of Tiffany & Co. in 2021. The acquisition of Tiffany & Co. by LVMH represents the luxury sector's biggest-ever deal. In fact, the French conglomerate has been able to conclude the deal with an overall discount of $425 millions, betting that it has the ability to restore Tiffany's fortunes by investing in stores and new collections. LVMH has believed in Tiffany's potential in spite of the difficulties that the latter encountered during the COVID-19 pandemic. The reasons behind the acquisition were LVMH's intentions to strengthen the jewellery and watch division, where it only owns Bulgari and Tag Heuer, while also strengthening its US presence. In addition to that, the sector in which Tiffany operates has been quite profitable. Indeed, the luxury jewelry business enjoyed a 7% increase in sales in 2018 to about $20 billion, according to Bain & Co. Moreover, the industry has high barriers to entry, which is an advantage for Tiffany against new entrants. Despite the past success of the jewelry industry and of Tiffany itself, many might ask why LVMH would want to acquire a company that has not been performing well in the near past. The answer is that LVMH has proven to be able to recover companies that weren't profitable at a certain point, with the acquisition of Bulgari being a significant example. In 2011, the French group bought 51% of Bulgari's capital, and issued a public offering for the remaining part. It did that because, due to the Great Recession, Bulgari was not performing well, so LVMH exploited the opportunity to take control of the brand, expand, and create successful synergies.

All of LVMH moves, including Bulgari and Tiffany's acquisition, have been profitable, well-managed, and far-sighted. The positive results that have been generated and that will be analyzed in the following paragraphs are concrete proof of it.

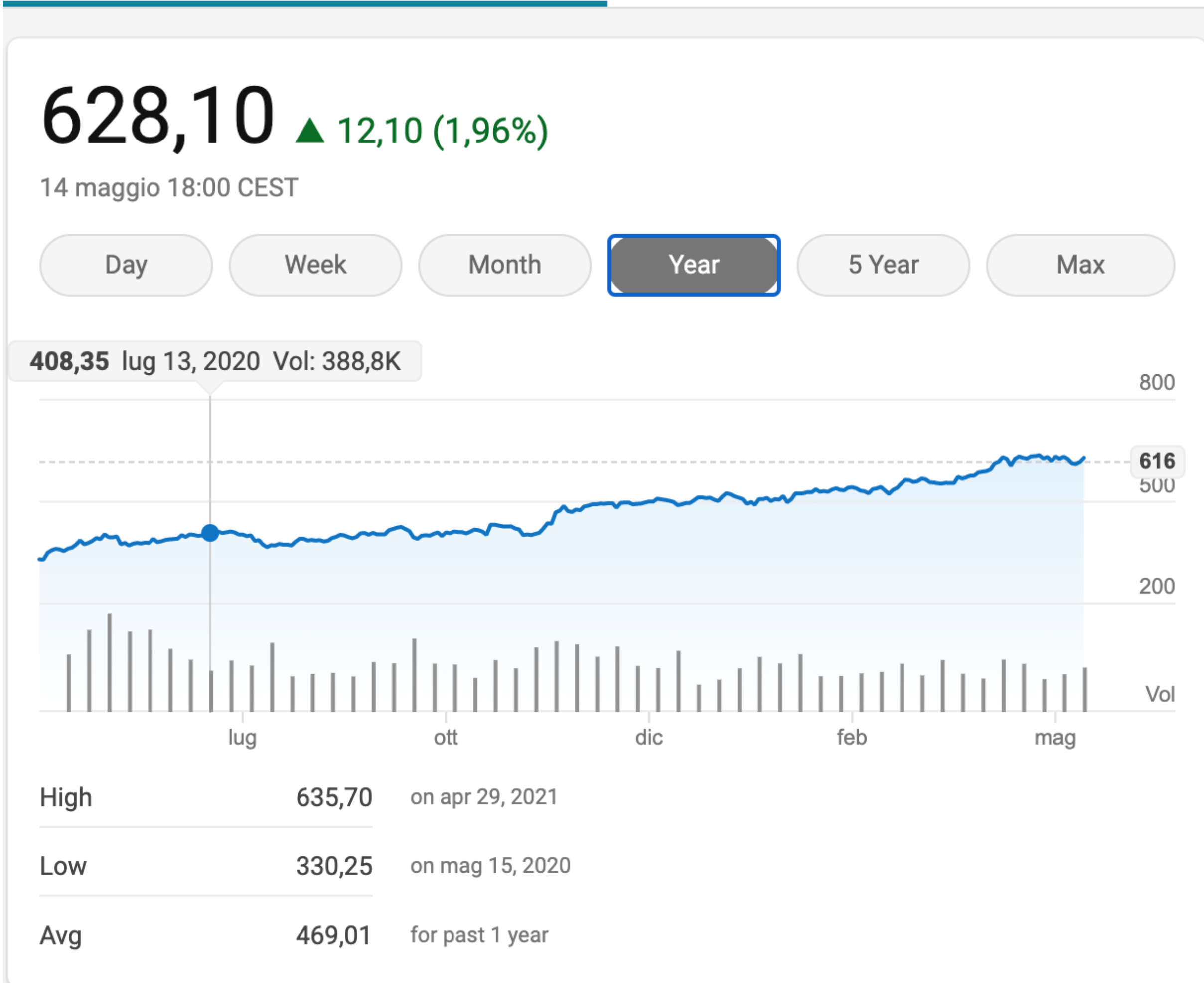
3.6 Benefits and results

As it has been proven by facts and history, LVMH has an admirable capacity of turning brands around in spite of their poor performances. The critical position and the difficulties that Tiffany was facing, made it a perfect target for the French company. The latter has always believed in Tiffany's potential, and was sure to be able to revive the brand from its difficult situation and missed opportunities. To help the floundering brand, LVMH plans to contribute to Tiffany's finance and help manage the firm's logistics functions, while also supplying digital services that it already uses to advise many other houses.

LVMH's strategy had more than one objective to pursue. First of all, it wanted to make itself more appealing to younger generations and planned to reach a youthful audience by forging Tiffany to be more engaging to millennials. It planned to do so by increasing the marketing budget and by introducing new products into the market, as well as renewing retail stores. Even though Tiffany is a luxury brand, not all of its products have exorbitant prices. In fact, in addition to diamonds and almost inaccessible precious stones, the jewelry company also has some offerings that could be reachable even by younger shoppers. Until that moment, one of LVMH main competitors, the Richemont group, had been the leader in the hard luxury industry, thanks to its control of Cartier and Van Cleef & Arpels, which are very profitable jewelry brands, with a strong success in Asia. It is no secret that one LVMH main ambition was to expand in the Asian market and the acquisition of Tiffany represented a perfect opportunity to do so. In reality, because of the pandemic, Tiffany suffered negative results in Mainland China, with an 85% decline in sales during February 2020. In spite of that, a few months later, thanks to an increased focus on internal consumption, Tiffany recorded a 30% increase in April, which continued in May with a growth of 90% against a substantial decline of global sales during the same month (*Bogliolo guarda già al futuro con Lvmh: Tiffany: -45% in febbraio-aprile, «ma ripresa robusta in Cina»*, 2020). Hence, the Chinese market represented an extraordinary opportunity for the American company to make itself desirable again. So, after the acquisition, LVMH should expand its product line and focus on targeting a younger audience, as well as the conquest of the Asian market.

Through this acquisition, the two brands were able to boost each others' value, which was reflected in the conglomerate's stock price. Already the day after the announcement of the

conclusion of the deal, LVMH price per share performed an increase of 2.6%, by surmanting for the first time ever the $500.00 price.
The implemented transition regarded also the internal and organizational structure of Tiffany. Some in-house management changes have been realized as LVMH transferred a big part of Louis Vuitton's leaders to the newly acquired firm. As a fact, it appointed two senior managers of Louis Vuitton as new directors of Tiffany, as well as renewing the design team from which the artistic director Reed Krakoff, and the chief brand officer Daniella Vitale have been removed. Moreover, after Alessandro Bogliolo had served as Tiffany's CEO for four years (2017-2021), after the acquisition he was replaced by Anthony Ledru, another senior executive of Louis Vuitton, who is now Tiffany's current Chief Executive Officer. Also Bernard Arnault's son, Alexandre Arnault, will fill a position of executive vice president and head of product and communication teams. The former Louis Vuitton's CEO, Michel Burke, will step up as Tiffany's new president (*Azioni LVMH a livelli record dopo aver completato l'acquisizione di Tiffany*, 2021).
It can be said that Louis Vuitton really embraced the American company, by creating a lot of synergies. Furthermore, the French conglomerate should review all of Tiffany's stores and currently employed online strategies. The acquisition had a clearly positive impact also in the financial sector even months after the conclusion of the deal. In fact, as of today, the stock price of LVMH is up to $628.10 per share. Even though LVMH does not public the results of single brands, it is quite intuitive that part of this impressive performance is due to the analyzed acquisition.



Source: Refinitiv

The previous statement is proved by the graph above, which shows the trend of LVMH stock price from the end of 2020 up to now. As it can be observed, LVMH share price reached $500.00 in December, when the acquisition was concluded, and it has been continuously increasing since then. The latter is substantial evidence that the acquisition of the American brand has been a quite brilliant and profitable move for the French conglomerate. This has been possible thanks to LVMH's ability to successfully manage the transaction and the subsequent decisions, as well as effectively exploiting available

synergies. As the conclusion of the acquisition is still recent, it is not possible to find empirical data about LVMH's jewelry and hard luxury sections' new performances. In spite of that, the stock price's trend is a powerful indicator of the results that can be expected in the future publication of LVMH's 2021 financial reports.

3.7 Conclusions

The latter chapter has shown how LVMH's admirable success is the result of beneficially performed acquisitions of important brands. The French company does not intend to stop with its expansion strategy and plans to keep expanding through more M&As operations, which have been proved to be a risky, but if well implemented, very powerful tool.
LVMH accomplishments are not due only to its financial operations, but mainly to its unique capacity of exploiting synergies and ability to manage brands as a conglomerate while still letting them maintain their own identity and partial independence. All of the houses have maintained their style, traditions, customers, and values, which are shared by the French group, which only acquires brands that share its same vision.
It is not yet known whether LVMH will acquire any more companies but, on the basis of the previously analyzed facts, it is very probable that it will do so.

Final conclusions

The purpose of this paper has been that of explaining the mechanisms of M&A operations in the luxury sector, as well as understanding the underlying reasons that pushed a huge conglomerate like LVMH to make them the basis of its expansionary and competitive strategy. The evidently profitable results of the latest acquisitions of the group, have highlighted its capacity to salvage frailing firms while enhancing its own value, mainly by exploiting synergies. In spite of the fact that LVMH has always been able to use M&As to its advantage, these types of transactions have not always been seen as a fair tool. In fact, it is generally believed that they deprive firms of their own identity. In spite of this common assumption, the French conglomerate has proven that, if implemented correctly by leaving companies their own autonomy while still being managed under a common umbrella, these deals can actually be a very positively powerful tool. The importance of M&As is constantly growing mainly because of the current historical period. COVID-19 has negatively marked an era, by causing huge economic losses. In a scenario like this, where the economy as a whole, and the luxury sector, are slowly recovering, it is extremely important to gain competitive advantage. It is trivial that in a highly competitive industry such as the luxury one, the bigger a firm is, the easier it is to emerge. For these reasons, M&As constitute one of the quickest ways to expand and hence preserve competitive advantage in a difficult, but hopefully bettering economy, especially for leaders, like LVMH, that wish to maintain their position. The variety of LVMH's portfolio constitutes one of its biggest strengths as it allows it to obtain a prevailing position in each of the sectors it wishes to target. Moreover, one of the main points of this thesis is that there is not a unique reason for why mergers and acquisitions are performed. They bear risks and advantages, and some of the times are the result of an attempt to save a poorly performing firm. The latter sentence can be proved by the analyzed acquisition, that of Tiffany & Co., which has generated positive results for both the acquirer and the target.
Indeed, the latter has been able to recover while still maintaining its managerial autonomy, and the former has successfully expanded its portfolios of brands and products, as well as its position in the Chinese market, and its appeal to a younger audience.

Through the results that have been analyzed until now, it can be confidently concluded that mergers and acquisitions, if carefully and intelligently performed, represents a perfect forceful instrument to quickly expand and gain and maintain a big competitive advantage.

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Ringraziamenti

This paper is a symbolic representation of the end of a cycle. It embodies my commitment, my determination, my passion, and most importantly my growth. The last three years have been unexpected and completely different from my plans. They have deeply changed my life and the person I am now, giving me a clearer vision of the one I aspire to be, and of where she is headed. I want to devote the most important and meaningful expression there is, “thank you”, to all the people who have helped me get where I am today, through my ups and my downs.

The first and biggest thank you goes to my parents. They did not only support me financially, but they have been my rock, my guidance, my friends, and my mentors for the whole time. No matter how big or small the distance between us, they were always right there. Thanks to my mum who is the person without I would not be here today, and who has taught me to always believe in myself, no matter how dark some periods may be. Thanks to my dad, who has taught me that results come from sacrifice and to always follow what I love. Thank you for always supporting my choices, advising me, but leaving me free to make my own mistakes and learn from them. I just want them to know how deeply grateful I am, and I hope this milestone will make them proud of me and repay them, at least in part, for everything they have always done for me.

I thank Luiss Guido Carli, because I found a home and a family when I felt really lost. It gifted me indelible memories and people, especially my colleagues, who have been so much more than friends for me. It made me stronger and helped me realize that I am much more capable than what I thought I was.

I thank my supervisor, Professor Di Colli, for his kindness, his availability, his patience, his passion, and his admirable capacity to not only successfully teach, but to connect with his students.

Thank you to my friend Gianluca, because he has not only been a colleague, but a brother and an ally. Thank you for making studying more fun and less stressful, thank you for not letting me feel scared, thank you for trusting me and opening up to me, and thank you because you saw that I deserved more and you made me see that too. Words cannot explain how highly I think of you and how special you are, and I am more than sure that you will accomplish great things in life. I wish you all the best.

Thank you to all the people who have been present for only part of this journey. I thank the ones that left because I learned when it’s time to let go, and I thank who is still here, no matter what and no matter the distance, because there are some bonds that are so much stronger than kilometers and time. I thank Marina, who is my life long friend and a sister to me. I thank my roommate, Anna Lea, to have shared everyday with me, and for the patience she has. And I thank my friend Melissa who even if has only recently entered my life has already meant so much to me and who has taught me what real strength is.

To what has been, but more importantly to what it will be… The best is yet to come.