

Luxottica S.p.A



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Agenda



- Business description/Summary
 - Revenue Breakdown
- Metrics
- Thesis Points (Includes VAR)
- Risks
- Catalysts
- Recommendations
- Questions

Business Description



- Luxottica operates in two areas:
 - Manufacturing/wholesale and the operation of retail stores.
- The manufacturing and wholesale sector designs, manufactures, and distributes the glasses
 - Both house brands and premium brands.
- Luxottica S.p.A has 11 factories: 6 in Italy, 2 in China, 1 in India, 2 in US
- In 2008—50 million glasses produced (23 million frames and 34 million sunglasses) sold in 130 countries.

Company History



- Founded by Leonardo Del Vecchio in 1961 in Italy.
- Their IPO occurred in 1990 on the NYSE (ADR--American Depository Receipts. Translation: Shares without the voting power) and Milan Stock Exchange (la borsa italiana)

Business Description



- Retail stores include:
- LensCrafters, The Sunglass Hut (some w/ Macy's), Perale Vision, ILORI, OPSM, Oakley "O" Stores, Laubman and Pank, Bright Eyes, David Clulow, as well as Sears and Target Optical.
- They also sell to many private opticians

Breakdown of Retail



North America	China	Europe	Asia—excluding China	SAfrica, Middle East, SAmerica
Lenscrafters--962	Lenscrafters--178	Sunglass Hut--81	OPSM--319	60 Sunglass stores
Perale Vision—729	Sunglass Hut—6	Oakley “O” Stores--11	Laubman and Pank--130	
Sunglass Hut—1,562	Other--65	David Clulow--64	Sunglass Hut--203	
Sears Optical--878			Oakley “O” Stores--15	
Target Optical--331			Budget Eyewear--76	
Oakley “O” Stores-99			Bright Eyes—151	
Sunglass Icon--99				

Types of Glasses



- Our brands appeal to “consumer’s age, lifestyle and fashion consciousness.”
- House Brands:
 - *Avant Garde, Ray-Ban, Oakley, Persol, Vogue, Arnette, Revo, Luxottica , Sferoflex, K&L (Killer Loop), Eye Safety Systems, Mosley Tribes and Oliver Peoples*
- Luxury:
 - *Chanel, Prada, Miu Miu, Dolce & Gabbana, D&G, Bvlgari, Tiffany & Co, Versace, Versus, Salvatore Ferragamo, Burberry , Polo Ralph Lauren, Donna Karan, DKNY, Brooks Brothers, Anne Klein, Paul Smith Spectacles*
- List prices range from 129 (excluding frequent discounts) to 360

Luxury Brand



Brand	Expiration of Worldwide license
Burberry	2015
Bvlgari	2010 (Renewable until 2014)
Dolce Gabbana	2010 (Renewable until 2015)
Versace	2012 (Renewable until 2022)
Prada	2013 (Renewable until 2018)
Polo	2017
Ferragamo	2011 (Renewable until 2013)
Chanel	2011 (Renewable until 2014)

House/Designer Breakdown



	2008	2007	2006	2005	2004
Designer Brands	33	42.7	41.2	35.9	32.8
House Brands	67	57.3	58.8	64.1	67.2
Total Sales	100	100	100	100	100

	2008	2007	2006	2005	2004
Optical	40.4	41.6	42.8	44.2	42.7
Sunglasses	59.6	58.4	57.2	55.8	57.3

Services



- Luxottica provides many services to customers besides sale of glasses
- US retail stores have lens finishing services, faster turnover, better quality
- US retail also has in house ophthalmologists and opticians

Revenue Breakdown



- Net Sales by area—
 - 59% from United States
 - 13% from Asia
 - 28% from Rest of World, Europe, South Africa, South America, Middle East...
- 60% of net sales come from Luxottica's retail stores whereas 40% come from wholesale to other operations

Business model/strategy



Keep cost structure below 2008 levels

- Accounts receivable in days v. around a month in 2004
- Spending from 300 mill Euros in 2008 to 200 mill Euros in 2009
- Reduce advertising
- 30 million of wholesale efficiencies in 2009

Business model/Strategy cont.

- Maintain strong presence in developed nations and expand into developing countries
 - Just signed deal to expand to Aus/New Zealand
- Keep the mix between sun and prescription and price strong

Metrics



- P/E—26.9 (from Google)
- Market Cap—11.6 billion
- Price/Book—3.43
- Current Ratio—1.25 (as of end of 2008)
- Debt/Equity—1.91
- EBITDA—869.1
- ROIC—6.3%
- Beta—1.36
- Altman's Z-Score 4.71

Thesis Points (Includes VAR)

- Inelastic demand
- Great services
- Great product mix
- Expansion into emerging markets
- Large niche, little competition
- Market Misconception

Inelastic demand for eyewear

- Luxottica falls partially under the healthcare category
- It is unique in its field because unlike other healthcare companies, Luxottica faces no burdensome regulation/lawsuits
- People need glasses to see, ergo inelastic demand

Services—VAR on Lenscrafters

- Luxottica's retail stores offer great service
- Advantage: Because they are national chains, Luxottica offers great glasses service anywhere in the nation for free (on most reasonable repairs)
- I have taken advantage of these services in New York, Augusta Maine, Salem and Charlottesville Virginia
- Private doctors cannot do this

Services



- Lenscrafters NYC
 - Full charge for glasses not bought there, 50% for major repairs less than a year
- Lenscrafters Chicago
 - Same, minor adjust free from any source, replacements free lenscrafters
- Pearle Vision Miami—free repair if warrantee
- Lenscrafters Boston--Most repairs free, same as Chicago

Lenscrafters/Peral Vision--VAR

- I have had better eye check ups at Lenscrafters than NYC doctor!
- Friendly and personable staff (in NYC, Maine, and Virginia)
- Great selection
- Offer many discounts, sales and AAA membership
 - On phone, two/three Lenscrafters told me about 50% off promotions
- Because of in house services, little wait time except for specialized finishes

Lenscrafters/Pearl Vision--VAR

- Lenscrafters/Pearl vision offer the happy medium
- Problems with doctors: after having your eyes messed with, don't feel like buying glasses. Less selection and same prices
- Problems with Wal-Mart: Limited selection and poor quality, staff lethargic and blew off appointment
 - Their optical retail operations emphasize product quality, selection, customer service and convenience. They do not compete primarily on the basis of price.

Both: Long wait time for glasses

Consumer's POV



- “if you like smart looking frames, and don't want to spend too much \$\$, this [Target Optical] is your place!”
- “David Clulow in Covent Garden however, eased the horror of buying my first pair of glasses....The lenses were fitted for me on the spot - this usually takes five odd days - and the service was impeccable. Overall I would highly recommend David Clulow”
Covent Garden. (England)

The unhappy campers...



- Pissedcustomer.com—many replies from LC employees/managers
- Angry blogger OPSM, New Zealand
 - “Hi, my name is Vanessa and I'm the current manager of OPSM Coastlands. Your blog site was referred to me by a colleague. And after reading your rating of our shop I am shocked by the poor customer service that you have received...I would really appreciate the opportunity to show you how awesome our customer service is now and also improve our rating with you. Please feel free to drop into the store, or give me a call (our number's in the phone book). Look forward to your reply, Vanessa Tames”

Margins



- Product Margins:
- “Not disclosed due to competition issues”
- HSBC estimates for house brands are 14% whereas luxury is 18%
- Website says sunglasses are “VERY profitable”

Selection



- Luxottica has the strongest portfolio of glasses in the world:
- Many brands to cater to many different customers, glasses “hedging”
- Optical: Less costly v. designer
- Sunglasses Sports market (Oakley) v. fashion v. leisure (Rayban)

Examples—of “hedging”



Expansion into Emerging Markets

- Feb. 8th Luxottica and Essilor plan joint merger to expand in Australia/New Zealand Markets
- Oct. 27 Luxottica opens first stores in Philippines, increases footprint in South Africa
- May 27 Luxottica acquires 40% of Multioptics—390 stores in South America

Large Niche, Little Competition

- Has the largest market share of its competitors:
 - Marcolin S.p.A (81 million dollar market cap, poor brand mix)
 - Charmant Group (Private, brands are obscure except for Lacoste, sells to private people)
 - De Rigo S.p.A (Private, more involved in production/design)
 - Marchon Eyewear (No stores, health-care software line too. Private, smaller company)
 - SAFILO Group (skewed mix, significant indebtedness led to financial restructuring, traded on pink sheets only)
 - Second largest competitor to Luxottica
 - Viva International (smaller private company, only in 60 countries, v. Luxottica's 130)
 - Couldn't tell info about company unless a customer (intransparent!)
- Very fragmented market overall

Competition--stats



- Luxottica doesn't really fall under an industry

	Operating Margin	Market cap	ROAA	P/E
Luxottica	14.41	8.78 billion	5.74	27.4
Marcolin	7.4	88 million	4.07	15.4

Market Share VAR



- Adele Sanna (Italian TA)—
 - Knew about Luxottica, not about competitors. Said that Luxottica was the largest

Stefano Grazioli (Comm school prof)-

In high school, Ray Ban was dominant player in town

UVA glasses poll/1st misconception

- Seeing brand names might scare investors.

- “Luxottica Group SpA (LUX) makes and sells high quality eyeglass frames and sunglasses, including such brands as Ray-Ban, Vogue, Luxottica, Chanel, Prada, Versace, Bulgari, DKNY, Brooks Brothers and Anne Klein. “ From stockerblog

Yet, talking to UVA students and observing them, 40% seem to wear Luxottica products (eye or sunwear)

- Lee
- Jonathan
- Two girls at Runk Dining Hall w/ D&G glasses

Market Misconception



- Based on its description of “fashion, luxury and sports eyewear.”
- Though they do sell high end, most of their sales are from the mid-range products
- Not like normal products of Prada, Gucci, Bvlgari, Dolce Gabbana
- Functional device that need to be of high quality (glasses) v. Fashion accessory (expensive clothes)
- 60% house brand sales

Risks (includes VAR)



- Debt
- Euro v. Dollar
- Lawsuits/Weather
- Knockoffs

Debt



- Luxottica has a fair amount of debt, why?
 - Nov. 2007 acquisition of Oakley (2.1 billion Euros) and general economic downturn

Total Debt	2008	2007	2006	2005
In thousands of Euros	2,805,502	2,719,140	1,319,262	1,528,909

Debt--Rebuttal



- Net debt to trailing 12 months EBITA hit a peak of 3.0 at end of 2008
- By end of 2008, that number is 2.6
- Mr. Hubert of HSBC told me that their model predicts: 2.3 by end of 2010 and 1.7 by 2011
- Mr. Hofkin of William Blair & Company had the following remarks:
 - “In general, given the *substantial efficiencies* the company has engineered in its business...and the *increased stability* of operating results, I do not see the debt burden as a significant risk going forward.”

Currency Issues



- The main currency issue is that Luxottica generates most of its revenue (59%) from the United States
- Yet, most of its expenses are in Euros (6 factories in Italy plus corporate HQ)
- Because receivables and payables are of a short term nature, Luxottica does not engage in hedging activities

Lawsuits/Weather



- As being part of the healthcare business, Luxottica is subject to potential lawsuits
- Unseasonably rainy/cool weather can hurt sales of sunglasses

Counterfeits



- Many people I talked to who had “Ray-Ban” type glasses had knockoffs.
- However, the quality was poor (quite flimsy) and the fact that they did not have the Ray-Ban logo would not pose a major risk

Catalysts



- Oakley—underrepresented in Europe, and in emerging markets. Europe’s young, active population needs performance sunglasses
 - Just set up European HQ in Switzerland
 - Brand is “underrepresented in almost every market outside US/UK”
 - In Winter Olympics, Speed skating, XC skiing, many athletes had Oakley Glasses, snowboarding
 - TDF for summer Bike shops

Oakley acquisition is priced in, but not necessarily European growth

Catalysts Continued



- Expansion into emerging markets, expanding infrastructure in Brazil and South Africa
 - Aus/New Zealand too
- Sales grow at 1.5 times that of developed countries
- Improving financials
- Consumers will tighten up replacement cycle from 3-5 years to 1.5

Recomendations



- Watch list
- In email IR she and investors “consider Luxottica expensive, so overvalued and not undervalued”
 - P/E is high
- Entry point--\$23-24 based on average P/E for company
- Sell out point--\$30 based on catalyst factors stated earlier

Questions?

LUXOTICA[®]
GROUP

VAR

- Hard because no phone access to Italy
- Adele Sanna, Italian TA
- Stefano Grazzoli, Comm school prof
- Three Lenscrafters
- Two perale visions
- Viva international sales rep
- Assorted UVA students with glasses (sun/perscription)
- Internet review forum sites

- Not VAR but contacts:
- Analyst, Mr. Hoffman of William Blair
- Analyst, Mr. Hubert of HSBC
- Investor Relations Luxottica, Nicoletta