

A Work Project, presented as part of the requirements for the Award of a Master's degree in Finance from the Nova School of Business and Economics.

**A STRATEGY TO MERGE, A COMPARISON OF LVMH MOËT  
HENNESSY – LOUIS VUITTON SE & L'ORÉAL S.A.**

LEONIE ANNA SOPHIE IRIS LÄHN

Work project carried out under the supervision of:

Margarida Soares (NOVA SBE)

Prof. Dr. André Schmidt (EBS University, Oestrich-Winkel)

05-09-2021

## **Abstract**

LVMH and L'Oréal both follow very different strategies regarding acquisitions, yet being successful in their own way. While L'Oréal solely focuses on the cosmetics segment, LVMH acts as a conglomerate acquiring firms such as jewelers, hotels, or perfume producers. This thesis summarizes findings in the literature on acquisitions about both strategic and financial motivations. Further, these findings are applied on the two firms being analyzed. As both firms are successful, while following completely different acquisition strategies, there is no winner at the end of this thesis. Instead, the comparison between the firms' strategies yields interesting similarities as well as differences.

**Keywords:** Strategy, Consulting, Finance, Merger & Acquisition, LVMH, L'Oréal, comparison

## **Table of Contents**

List of Abbreviations .....	i
List of Figures and Tables.....	ii
List of Figures .....	ii
List of Tables .....	viii
1 Introduction.....	1
1.1 Problem Definition and Objectives.....	1
1.2 Course of the Investigation .....	2
2 Literature Review .....	2
2.1 Strategic Literature Review .....	3
2.1.1 Competition and Competitive Strategies .....	3
2.1.2 International Competition & Entry Modes .....	5
2.1.3 Strategic Motives for Mergers and Acquisitions .....	6
2.1.4 Strategic Conglomerates .....	8
2.2 Finance Literature Review .....	10
2.2.1 Cost of Capital .....	10
2.2.2 Financial Motives for Mergers and Acquisitions.....	11
2.2.2.1 Growth and Market Power.....	12
2.2.2.2 Access to Capital and Synergies .....	13
2.2.2.3 Financial Synergies: Reduction of Cost of Capital.....	14
2.2.2.4 Timing.....	15
2.2.3 Wealth Effects of Mergers and Acquisitions Activity .....	15
2.2.3.1 Introduction.....	15
2.2.3.2 Short-Term and Long-Term Wealth Effects.....	16
2.2.3.3 Value Generation of Mergers and Acquisitions.....	17
2.2.4 Financial Conglomerates .....	18
3 Application.....	20
3.1 Overview of The Companies .....	20
3.1.1 LVMH Moët Hennessy Louis Vuitton .....	20
3.1.2 L'Oréal S.A. ....	20
3.2 Strategic Analysis .....	21
3.2.1 Competition.....	21
3.2.1.1 Competition: Awareness, Motivation, and Ability .....	21
3.2.1.2 Competitive Stand.....	22
3.2.2 Strategy .....	24
3.2.2.1 Strategic Overview.....	24
3.2.2.2 Cost Leadership, Differentiation, or Focus.....	25
3.2.2.3 Market Commonality and Resource Similarity .....	27
3.2.2.4 Diversification and Relatedness.....	29
3.2.3 Growth Without Acquisitions .....	31
3.2.3.1 Organic Growth .....	31
3.2.3.2 Strategic Alliances, Licensing, and Subsidiaries .....	33
3.2.4 Acquisitions .....	35
3.2.4.1 Overview of Acquisitions .....	35
3.2.4.2 Types of Acquisitions .....	35
3.2.4.3 Acquisition Motives.....	37

3.2.4.3.1	LVMH and Tiffany Co. ....	37
3.2.4.3.2	L’Oréal and IT Cosmetics.....	41
3.2.4.4	Exceptional Case: Conglomerate.....	43
3.3	Financial Analysis.....	45
3.3.1	Financial Overview.....	45
3.3.2	Merger Motives.....	46
3.3.2.1	Macroeconomic and Microeconomic Factors.....	46
3.3.2.2	Increase in Prices & Decrease in Costs.....	52
3.3.2.3	Purely Financial Motives .....	55
3.3.2.4	Financial Synergies: Cost of Capital.....	57
3.3.2.5	Timing.....	61
3.3.3	Wealth Effects of Mergers and Acquisition Activity .....	63
3.3.3.1	Short-Term Wealth Effects .....	63
3.3.3.2	Long-Term Wealth Effects .....	66
3.3.3.3	Conglomerate Discount .....	67
4	Discussion.....	67
4.1	Strategic Discussion.....	68
4.1.1	Competition.....	68
4.1.2	Acquisition Strategies .....	69
4.1.3	Growth .....	71
4.1.4	Strategic Conglomerate.....	73
4.2	Finance Discussion .....	74
4.2.1	Mergers and Acquisition Motives.....	74
4.2.2	Wealth Effects of Mergers and Acquisitions Activity .....	78
4.2.3	Financial Conglomerate .....	80
4.3	Summary .....	80
5	Conclusion .....	82
	Reference List .....	84
	Appendix.....	92
	Honourable Declaration .....	100

## **List of Abbreviations**

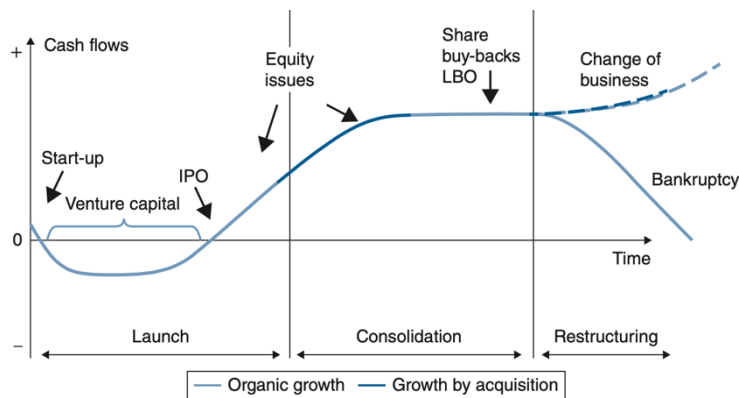
<b>Abbreviation</b>	<b>Meaning</b>
bn	Billion
CAPM	Capital Asset Pricing Model
CoC	Cost of Capital
EVA	Economic Value Added
FMCG	Fast-Moving Consumer Goods
IRR	Internal Rate of Return
L'Oréal	L'Oréal S.A.
LVMH	LVMH Moët Hennessy Louis Vuitton
M&A	Mergers & Acquisition
mm	Million
NOPAT	Net Operating Profit After Tax
NPV	Net Present Value
R&D	Research & Development
Tiffany	Tiffany & Co.
U.S.	United States of America
WACC	Weighted Average Cost of Capital

**List of Figures and Tables**

**List of Figures**

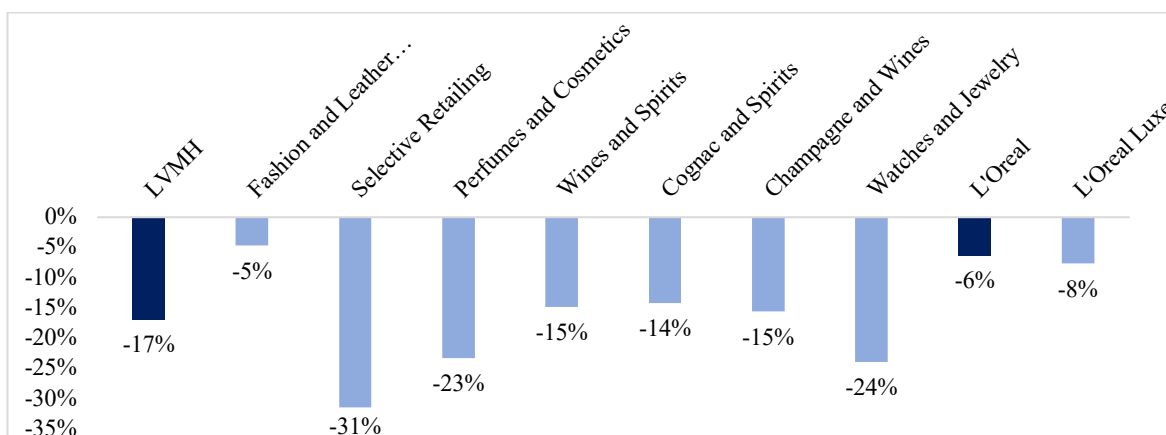
**Figure 1**

**The Lifecycle of The Firm (Vernimmen, Quiry, Dalocchio, Le Fur, & Salvi, 2017)**



**Figure 2**

**Difference in Sales From 2019 to 2020 for LVMH and L’Oréal (Bloomberg L.P., n.d.-g, n.d.-z)**



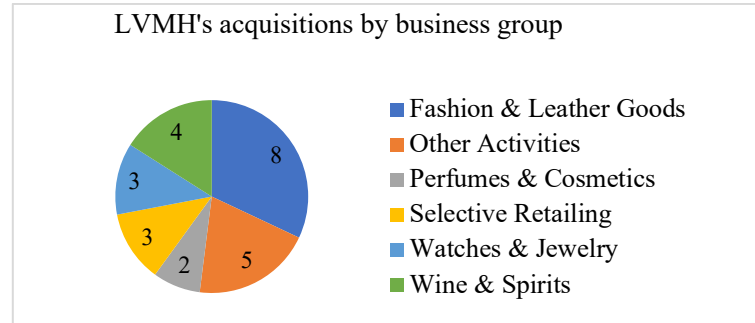
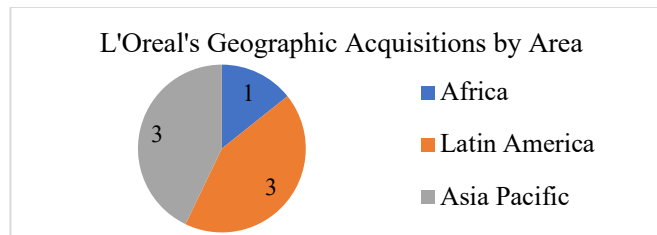
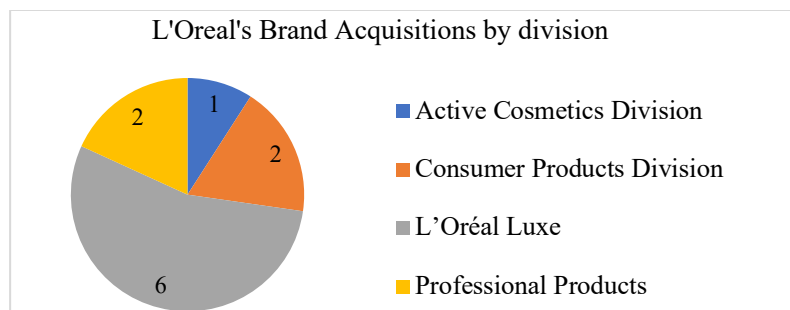
**Figure 3****LVMH's Acquisitions by Business Group (Bloomberg L.P., n.d.-ae)****Figure 4****L'Oréal's Geographic Acquisitions by Area (L'Oréal S.A., 2021a, p. 23)****Figure 5****L'Oréal's Brand Acquisitions by Division (L'Oréal S.A., 2021a, p. 23)**

Figure 6

**Comparison of Total Debt/Total Asset Ratios in Percent Between L'Oréal, Unilever, and Estée Lauder (Bloomberg L.P., n.d.-b, n.d.-i, n.d.-an)**

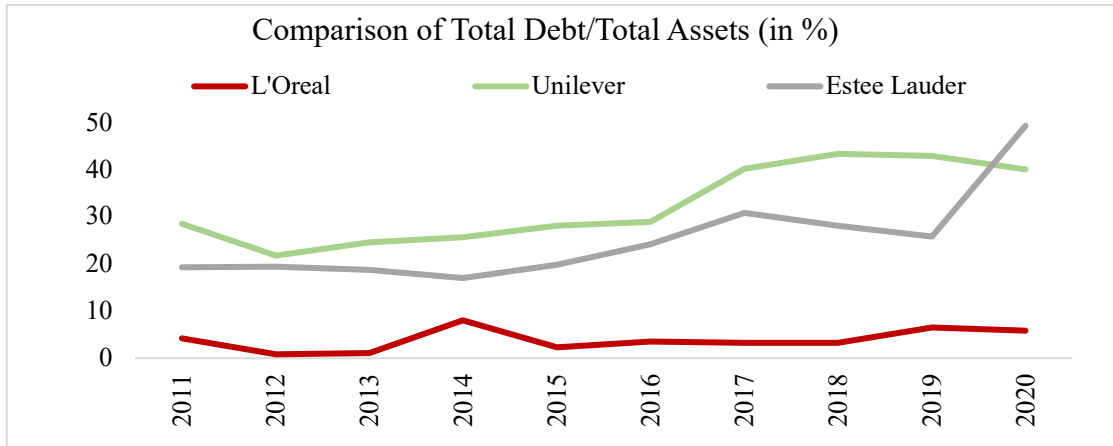
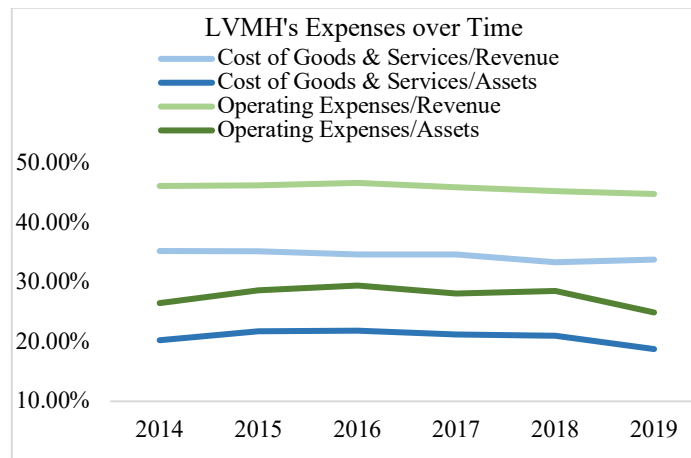


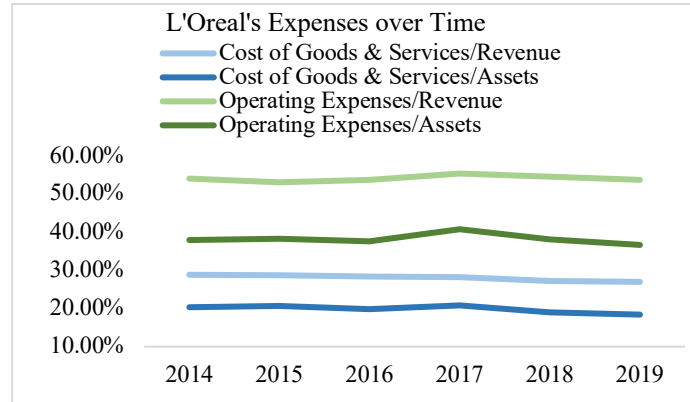
Figure 7

**LVMH's Expenses Over Time (Bloomberg L.P., n.d.-z)**



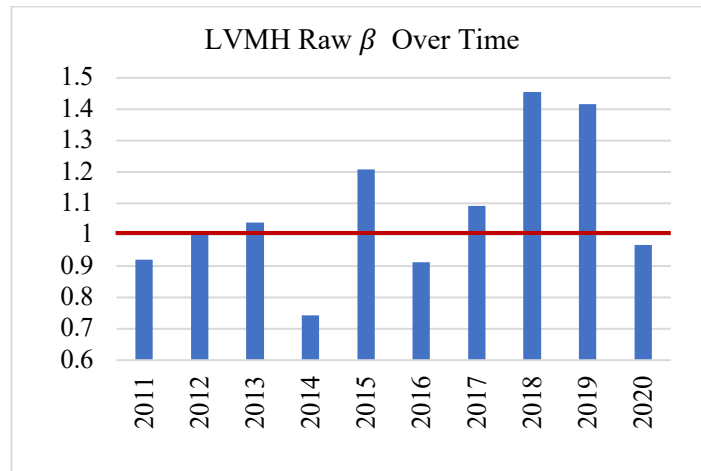
**Figure 8**

**L'Oréal's Expenses From 2014 to 2019 (Bloomberg L.P., n.d.-g)**



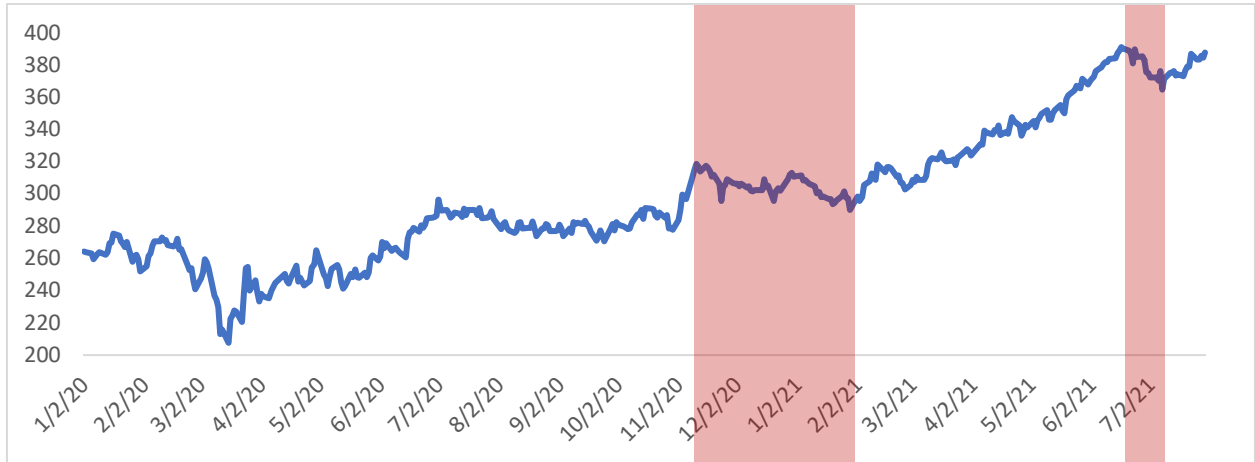
**Figure 9**

**LVMH's Raw  $\beta$  From 2011 to 2020 (Bloomberg L.P., n.d.-aj)**



**Figure 10**

**L'Oréal's Share Price From 01/02/2020 to 07/30/2021 in € (Bloomberg L.P., n.d.-n)**

**Figure 11**

**Logarithmic Returns of LVMH and Tiffany Around the Announcement Date (Bloomberg L.P., n.d.-af, n.d.-am)**

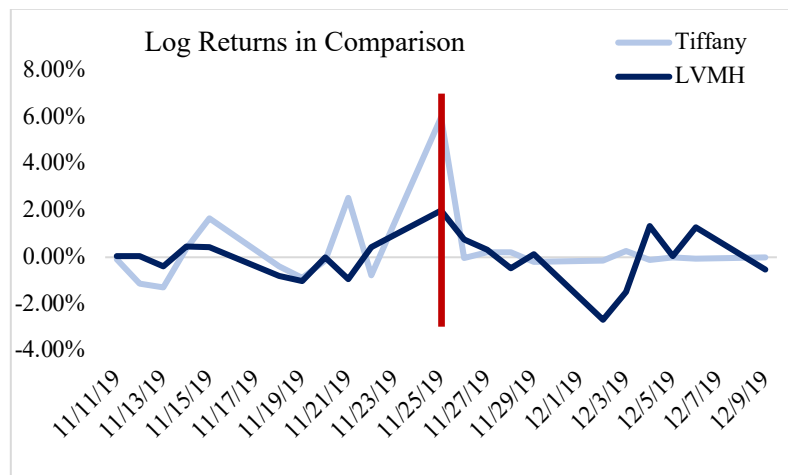
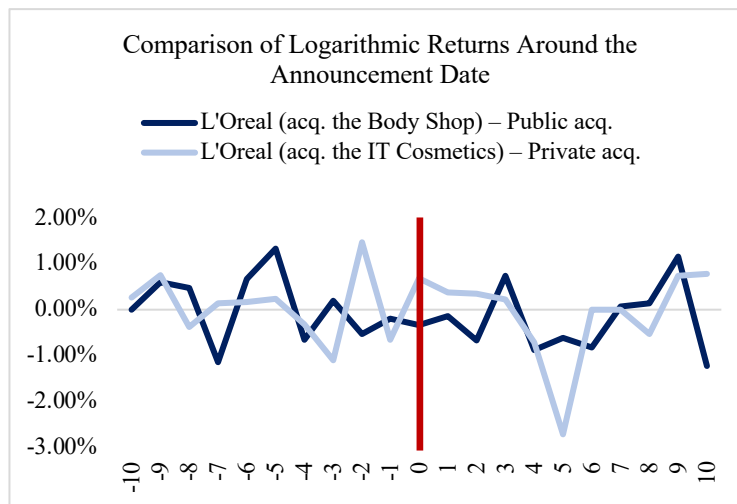


Figure 12

**Comparison of Logarithmic Returns of L'Oréal for Both The Body Shop and IT Cosmetics  
in the Event Window Around the Announcement Date (Bloomberg L.P., n.d.-m)**



**List of Tables****Table 1****LVMH's Average Revenue (Growth), Gross Profit, and Gross Margin From 2015 to 2019  
(Bloomberg L.P., n.d.-y)**

	<b>2015</b>	<b>2016</b>	<b>2017</b>	<b>2018</b>	<b>2019</b>	<b>Average</b>
Revenue (€ mm)	35,664.00	37,600.00	42,636.00	46,826.00	53,670.00	43,279.20
Revenue Growth (in %)	16.40%	5.43%	13.39%	9.83%	14.62%	11.93%
Gross Profit (€ mm)	23,111.00	24,561.00	27,853.00	31,201.00	35,547.00	28,454.60
Gross Margin (in %)	64.80%	65.32%	65.33%	66.63%	66.23%	65.66%

**Table 2****LVMH's Equity Values From 2018 to 2020 (Bloomberg L.P., n.d.-ad)**

	FY 2018	FY 2019	FY 2020
Total Equity (€ mm)	33,957.00	38,365.00	38,829.00

**Table 3****L'Oréal's Average Revenue (Growth), Gross Profit, and Gross Margin From 2015 to 2019  
(Bloomberg L.P., n.d.-f)**

	2015	2016	2017	2018	2019	<b>Average</b>
Revenue (€ mm)	24,290.20	24,916.30	26,023.70	26,937.40	29,873.60	<b>26,408.24</b>
Revenue Growth (%)	7.80%	2.58%	4.44%	3.51%	10.90%	<b>5.85%</b>
Gross Profit (€ mm)	17,296.00	17,847.70	18,664.50	19,605.80	21,808.90	<b>19,044.58</b>
Margin (%)	71.21%	71.63%	71.72%	72.78%	73.00%	<b>72.07%</b>

**Table 4**

**Bloomberg's Multiples Analysis for LVMH Among Different Industry Classifications  
(Bloomberg L.P., n.d.-t, n.d.-u, n.d.-v, n.d.-x)**

<b>Companies</b>	<b>Count of Companies mentioned more than once</b>
Christian Dior SE	4
Hermes International	4
Lululemon Athletica Inc	3
Cie Financiere Richemont SA	3
PRADA SpA	3
Shenzhou International Group H	3
adidas AG	3
Kering SA	3
Swatch Group AG/The	2
VF Corp	2
Moncler SpA	2
ANTA Sports Products Ltd	2
Li Ning Co Ltd	2

**Table 5**

**Increase in the Number of LVMH's Consolidated Companies Between 2012 and 2020  
(LVMH, 2013, pp. 184-189; 2021b, pp. 264-271)**

	<b>Wine &amp; Spirits</b>		<b>Fashion &amp; Leather Goods</b>		<b>Perfumes &amp; Cosmetics</b>		<b>Watches &amp; Jewelry</b>		<b>Selective Re-tailing</b>		<b>Other Activities</b>	
	2012	2020	2012	2020	2012	2020	2012	2020	2012	2020	2012	2020
Number of consolidated companies	87	95	272	435	95	138	93	112	112	119	87	315
Absolute Increase		8		163		43		19		7		228
Relative Increase		9%		60%		45%		20%		6%		262%

**Table 6****Comparison of LVMH's and Tiffany's Expenses Between 2020 and 2021 (Bloomberg L.P., n.d.-aa, n.d.-ak)**

In € mm	S2 2020			S1 2021
	LVMH	Tiffany	Σ	LVMH
Operating Expenses	10,585	971.7	11,556.7	11,993
Selling, General & Admin	10,734	972.6	11,706.6	11,903

**Table 7****Percentage Increase in LVMH's Expenses in 2019 and 2020 (Bloomberg L.P., n.d.-aa)**

In € mm	S1.19-S2.19	S1.20-S2.20
Operating Expenses	11.91%	9.60%
Selling, General & Admin	12.04%	10.67%

**Table 8****LVMH Expense Simulation (Bloomberg L.P., n.d.-aa)**

In € mm	S2 2020	S1 2021 exp. with S1.19-S2.19 increase	S1 2021 exp. with S1.20-S2.20 increase	S1 2021 actual	Δ S1.19-S2.19	Δ S1.20-S2.20
Operating Expenses	10,585.00	11,845.43	11,600.98	11,993.00	147.57	392.02
Selling, General & Admin	10,734.00	12,026.58	11,879.45	11,903.00	-123.58	23.55

**Table 9**  
**LVMH's Issued Bonds for The Tiffany Acquisition (LVMH, 2021b)**

Nominal Amount (bn)	Maturity	Date to Maturity as of 2020	December 31, 2020 (€ mm)
GBP 850	2027	7	970
EUR 1,250	2024	4	1,251
EUR 1,250	2026	6	1,244
EUR 1,750	2028	8	1,734
EUR 1,500	2031	11	1,487
GBP 700	2023	3	788
EUR 1,500	2025	5	1,494
EUR 1,750	2022	2	1,754
		<b>Σ</b>	<b>10,722</b>

**Table 10**  
**Comparison of Acquisition Payment Types of LVMH and L'Oréal (Bloomberg L.P., n.d.-l, n.d.-ae)**

Comparison of Payment Types	# of Deals	
	LVMH	L'Oréal
Cash	64	31
Stock	5	1
Cash, Stock & Debt	1	
Cash or Stock	1	
Cash & Debt	1	
Undisclosed	111	52

## **1 Introduction**

### **1.1 Problem Definition and Objectives**

LVMH Moët Hennessy Louis Vuitton (LVMH) and L'Oréal S.A. (L'Oréal) are two of the most successful companies today. They both use acquisitions to further grow and expand their standing in the market and have shown improved performance for some time now. Interestingly, although they are both very successful, the two firms follow very different overall acquisition strategies, which are analyzed in this thesis. While L'Oréal solely focuses on the cosmetics market, LVMH acts as a luxury conglomerate that is active in several markets including handbags, hotels, and retail facilities. This difference in approach motivated me to further investigate how and why both firms thrive while pursuing completely different acquisition strategies. As both companies are successful in their respective markets and industries, it is not possible to indicate which of the two is more successful than the other. They are, however, driven by different motivations, which will be discussed in this thesis, and their strategy to merge comprises the main topic of this work.

Although LVMH and L'Oréal pursue different acquisition strategies, an analysis of these shows that they also have many things in common. The main findings of this work show that strategic motivations are of higher importance than financial ones. The analysis showed that financial indicators alone do not explain the firms' acquisition motivations and, more importantly, their success, as the purely financial indicators do not yield significant positive results. Instead, both LVMH and L'Oréal mainly seem to acquire for strategic reasons. While both firms technically have the necessary funds and expertise to grow without Merger & Acquisition (M&A) activity, they still acquire firms that are already established in the market and have made a name for themselves. For example, one of LVMH's latest acquisitions is Tiffany, a U.S. jewelry company. While Tiffany is a successful company in the jewelry segment in its own right, it is also well known because of the film *Breakfast at Tiffany's* and owning its own Tiffany blue. It can thus be concluded that one important motivation for an acquisition is the acquired brand and its name, which is naturally backed up by the strategic and financial fit of the acquisition. Significantly, the luxury and cosmetics sector seem to mainly be driven by what *feeling* the companies are selling to the consumer, instead of the product that is being purchased as such.

## **1.2 Course of the Investigation**

This thesis aims to qualitatively compare and analyze LVMH and L'Oréal's acquisition strategies based on strategic and financial indicators. It commences with a literature review that summarizes current and historical findings regarding acquisition strategies, which are subsequently applied to LVMH and L'Oréal. The literature review not only aims to describe the main drivers for acquisitions but also starts by explaining why competition is relevant in the first place, and why low costs of capital are beneficial to a company. The practical part of the thesis provides a more detailed overview of the two firms, including their historical development, current standing in the market, and future prospects. Although the literature review and the practical part are divided into strategic and financial analyses, these two aspects are not entirely separable in practice as they are ultimately interlinked and strategic decisions influence financial performance and vice versa.

As this thesis is qualitative, to ensure the quality of the data most information was derived from the companies' disclosed information. As companies do not disclose confidential information to the competition, not all data is publicly available, and thus some data was also collected from external sources such as (mainly) newspaper articles. The financial data was acquired from Bloomberg.

## **2 Literature Review**

In any industry, firms must compete with several rivals for market shares. Therefore, a firm must stay competitive in both a passive and an active way to counter attacks from incumbents and (possible) new market entrants. Besides generic growth possibilities, there are other options that a firm can consider to remain ahead of the competition, namely acquisitions. There is a great deal of literature available on the topic of M&A, including the motivations, risks, and consequences of these decisions. This literature review primarily focuses on the motivations and implications of acquisitions and disregards topics such as cultural fit or integration strategies. Two theoretical viewpoints deal with M&A in more depth, namely the strategic point of view and financial point of view.

## **2.1 Strategic Literature Review**

### **2.1.1 Competition and Competitive Strategies**

Firms usually face competition from other rivals in their respective industry. One exception is the case of the monopoly, where there is only one player in the market to which competitive strategies do not apply. How and for what reason firms react to competition has been reviewed in the literature.

Hitt, Ireland, and Hoskisson (2016, pp. 148-152, 174-215, 221) introduced drivers of competitive behavior that are based on market commonality and resource similarity. High market commonality occurs when rivals compete in several markets. Any competitive action or response of a rival in such a case not only affects the competition in one market but possibly other markets as well. High resource similarity addresses the aspect of a firm's (in-)tangible assets and thus the higher the similarity, the more similar are the rivals' strengths and weaknesses. The three drivers of competitive behavior include awareness, motivation, and ability. For example, to perform competitive actions, a firm must first be aware of the competition, which means that it knows of the existence and the impact of competitiveness. This is most likely when the firm has very similar resources while it competes with its rivals in several markets. Furthermore, the firm must have the motivation to compete, either defensively or offensively, unless it believes that either action would impair its market position or if not responding at all would not do any harm to the firm. The motivation is influenced by the market commonality and it is greater in cases of lower market commonality with the rival since a high market commonality would involve too much risk for the firm and too much effort involved in competing against this one rival. Finally, the firm's ability is identified as a driver for competitive behavior. This includes its available resources, such as financial capital or people, and the necessary flexibility required for competition (Hitt et al., 2016).

Assuming the case of competitive behavior, there are different tactics in terms of internal generic strategies. Successful strategies to compete in an industry have been identified (Hitt et al., 2016; Porter, 2008): overall cost leadership, differentiation, and focus. By decreasing any type of costs within the organization, a firm can earn above average returns in an industry and is, therefore, better positioned than its rivals. However, a firm must ensure that quality does not suffer under the cost leadership strategy since quality is equally important. Furthermore, a firm can decide to differentiate its products or services. This differentiation from

rivals places the firm in a unique position in the industry and it can take several forms, such as brand image, technology, or customer service. The established loyalty provides the firm with a lower price sensitivity on the consumer side, and increased margins to earn above-average returns in an industry. The focus strategy either emphasizes a particular buyer group, a product's segment line, or a geographic market (Porter, 2008).

For the fast-moving consumer goods (FMCG) industry, Gell, Gjerstad, Shinall, and Istvan (2017) introduced a three-step approach to creating value in a stagnating and developed FMCG. This stagnation is due to several factors, including the emergence of small competitors that challenge megabrands. The authors then introduced the build-buy-broker approach to counter this. In this approach, they recommend that firms should continuously grow organically (to build), and also acquire targets (buy) to enable the firms to enter high-growth markets. A firm also needs to broker, which includes the reevaluation of existing assets owned by the firm. Subsequently, a firm must aim to find the right owner for all assets and eventually sell noncore assets that do not fit the firm anymore (Gell et al., 2017).

Ansoff, Kiple, Lewis, Helm-Stevens, and Ansoff (2018) introduced a competitive analysis to improve a firm's performance in an industry. The competitive strategies are established in the firm's business areas. They found that, even though a firm follows an optimal strategy in each of its business areas, some areas are simply not as profitable as others. Therefore, Ansoff et al. (2018) introduced the strategic portfolio analysis as a subsequent step. In this analysis the business areas are reevaluated, compared, and prioritized.

Although the preceding strategies mainly focus on the business-level strategy, the corporate-level strategy of each firm also needs to be explored. The corporate-level strategy asks where to compete, in other words how to select and manage different businesses competing in different markets for a competitive advantage (Hitt et al., 2016). Different levels and types of diversification exist, where not only the level of diversification is analyzed but also the relatedness of the different businesses. Relatedness includes the sharing of product markets, technologies, and distribution channels. A conglomerate is found when there is a high level of diversification and low relatedness between the businesses. One of the main reasons why a firm wants to diversify is to increase value by having a better overall performance. Additionally, a diversified firm has more security when one business unit experiences difficulties as the other diversified business units can make up for the loss and the overall firm is more

secure (Hitt et al., 2016). A general view includes four concepts of corporate strategies: portfolio management, restructuring, transferring skills, and sharing activities. It was found that transferring and sharing skills and knowledge are the most successful drivers (Porter, 1989).

### **2.1.2 International Competition & Entry Modes**

Competition in global industries, that is, internationally, and the entry into new markets increases a firm's ability to earn above-average returns, but also exposes it to more risks and challenges that need to be addressed. In this context, particularly the decision regarding internal growth through greenfield ventures as opposed to external growth through acquisitions is of great interest and is therefore evaluated in this chapter.

Since globalization is increasingly progressing, firms must be able to compete on an international level. The basic benefits of an international strategy include the increase of market size, economies of scale (and learning), and location advantages. Therefore, incentives to engage internationally as a firm include the extension of a product's lifecycle due to a larger market size to sell it to; easier access to raw materials since the firm can receive these materials from everywhere anytime; the integration of operations on a global scale; better use of fast-developing technologies; and the opportunity to access customers that are in emerging markets and have not previously been targeted.

Furthermore, when it comes to the entry into a new business, Porter (2008) analyzed the market and found that entry itself only works because of imperfect markets, that is, if markets worked perfectly then above-average returns could not be realized. In addition to internal development, acquisitions provide a possible way to enter a market in a way that does not add a new firm to the market. However, this "game" is very difficult to win as there are several imperfections on the acquisition market that lead to reduced returns including superior information on the buyer side. Furthermore, firms that are in a bad state would attract fewer bidders and thereby reduce the acquisition price (Porter, 2008).

Hitt et al. (2016) developed a more detailed pool of choices for entering a new market. Their entry choices include exporting, licensing, strategic alliances, acquisitions, and new wholly-owned subsidiaries (greenfield investments). While exporting is a rather easy entry mode to start with, it involves very high costs compared to the low control a firm has when simply exporting their goods to a different country. Licensing, however, works slightly differently from exporting. In this case, a foreign company not only buys the right to sell but

also produce a firm's product in its host country market. While this is comparatively cheap and exposes the firm to a low risk, licensing provides the firm with little control and modest returns. For a firm to have more control over the production and sales of a product, it can engage in a strategic alliance. This includes the collaboration with a different firm to jointly enter a foreign market. While the profits will be divided between the firms, the risks, resources, and costs are also divided between the firms in the strategic alliance. However, a firm must bear the difficulty in integration with the other firm in mind since the two firms might have completely different corporate cultures. Another entry mode involves cross-border acquisition. The major advantage of acquisitions is that they provide the fastest way to enter any market or industry. However, an acquisition is associated with high costs of purchasing the target, difficulty in information gathering, and negotiations with the target firm on how to integrate it into the buyer firm, in addition to the problems of regulatory requirements in the target country. The final entry mode is the new wholly-owned subsidiary or greenfield investment. While this is the most complex, and probably the most expensive entry mode, it enables the firm to keep all the returns and also to gain maximum control over the new entity. Regarding entry modes, the authors recommend that exporting, licensing, and strategic alliances are good for first entering into a new market, whereas acquisitions and greenfield ventures are favorable when a firm wants to completely enter the market or industry and have a strong presence there (Hitt et al., 2016).

### **2.1.3 Strategic Motives for Mergers and Acquisitions**

As one of the market entry modes, acquisitions have been analyzed in the literature and this section summarizes the motives for engaging in acquisitions. As a firm is constantly searching for ways to create more value for its shareholders, acquisitions provide a welcome opportunity to earn above-average returns in an industry. The reasons for engaging in acquisitions are therefore quite straightforward and include overcoming entry barriers, reducing the costs of new product development and hence an increased speed to market, lower risk compared to a greenfield venture, increased diversification, a reshaping of the firm's competitive strategy, and the development or learning of new capabilities, in addition to the increase in market power. When it comes to how and where to acquire, both related diversification strategies and conglomerate strategies can be successful (Hitt et al., 2016).

Furthermore, in their article Haleblan, Devers, McNamara, Carpenter, and Davison (2009) created a framework to identify additional reasons why firms are interested to acquire. In a five-step approach, they reviewed empirical findings from different fields and distinguished between antecedents, moderators, and other acquisition outcomes. The antecedents include topics such as value creation, managerial self-interest, environmental factors, and firm characteristics that all influence the engagement in acquisitions. Value creation includes market power – among others – as was also identified by Hitt et al. (2016), and resource deployment. Managerial self-interest tends to be a value destructing antecedent since, in this case, acquisitions are not performed in the best interest of the company but in that of the management. This includes compensation, as CEOs receive a higher salary or bonus no matter how the acquired entity is performing after integrating it, which leads to managerial hubris where CEOs overestimate their skills and abilities and engage in acquisition activities that are detrimental to both the buyer and the seller of the firm. Although Haleblan et al. (2009) found several motivations to acquire, they failed to address the basic question regarding which motives drive acquisition behavior the most.

In his study, Halpern (1983) made a very similar distinction to Haleblan et al. (2009) by introducing two acquisition theory classes, namely non-value maximizing behavior and value maximizing behavior of acquirers. Non-value maximizing acquisition behavior focuses on maximizing growth, sales, or both, as the main goals. However, the losses from negotiating and problems resulting from these types of acquisitions make them unprofitable. Halpern (1983) found that especially conglomerates and firms with active acquisition programs follow this theory class of acquisitions. On the other hand, value-maximizing acquisitions are driven by the same requirements as any investment decision, which probably results in a profitable out-come of an acquisition. Similarly to the limits of the research by Haleblan et al. (2009), Halpern (1983) also failed to identify a single driver for engaging in acquisitions.

A more specific view on the drivers of acquisitions was developed by Gell et al. (2019) due to their focus on the FMCG industry. They identified three factors that increase acquisition behavior: First, industry headwinds. Second, fighting decreasing growth rates in the developed markets and the emergence of small firms that are very popular with young consumers. Third, the ongoing interest in private equity.

Another contribution to the literature was made by Louri (2001), who analyzed the reasons for multinational firms to enter foreign markets using the example of entries in Greece. One significant advantage of M&A over greenfield investments is that incumbent firms in that industry do not react in a hostile way since no new firm is entering the market, but rather an existing firm is merely being acquired. Louri (2001) also found that acquiring a firm reduces the risk of being unfamiliar with the foreign market. This view was indirectly supported by Farrell and Shapiro (1990), who viewed horizontal mergers as a transfer of industry-specific assets that are not only composed of physical but also of organizational capital.

When Louri (2001) mentioned the aspect of familiarity in the market where the firms acquire, she referred to an older edition of Caves (2007), who also analyzed the differences between acquisitions and greenfield investments. Louri (2001) also found that acquired firms already have a functioning local management that knows the foreign market being entered better than the multinational firm does. Therefore, the acquiring firm is not only purchasing physical assets, but also a very valuable stock of information regarding the market's environment. She found that this is especially the case for rapidly growing firms that usually have a smaller information stock than similar multinational firms that have grown more slowly.

Whereas all these motivations to engage in acquisitions are logical in themselves, it remains unclear which of the motives are primarily driving acquisition behavior as this cannot be conclusively answered by the literature.

#### **2.1.4 Strategic Conglomerates**

A conglomerate is a special form of unrelated diversified international strategy. Tremblay and Tremblay (2012) defined conglomerate mergers as being neither horizontal (among the competition) nor vertical (along the value chain). In fact, conglomerates consist of firms that produce unrelated products, in other words, products that are neither substitutes nor complements<sup>1</sup>. The authors distinguish between pure and impure conglomerate mergers. Whereas pure conglomerates are active in separate markets with entirely unrelated products. Impure ones are active in markets that are not entirely separate and consist of market extension mergers, where one product is sold in different geographic markets, and product extension mergers, where products are sold that are somewhat related, that is, imperfect substitutes.

---

<sup>1</sup> “Substitutes” refers to when one good is consumed instead of another, e.g., wine and beer cannot be consumed at the same time. “Complements” are goods that increase value when used together, such as a bike and a helmet.

The reasons and motives to engage in conglomerate mergers are not straight-forward since merging unrelated firms does not seem to generate benefits in terms of the synergies achieved (Amihud & Lev, 1981). Tremblay and Tremblay (2012) therefore investigated different reasons why firms engage in conglomerate mergers and found that the most straight-forward reason was risk reduction through diversification.

In addition to the aspects of increased efficiency and risk reduction that motivate conglomerate mergers, managerial motives have also been identified. In many firms, ownership and managerial control fall under separate persons. If a manager's income is dependent on the performance of the company, in combination with the fact that conglomerate mergers are generally not greatly challenged by the authorities, the manager might seek fast growth using a conglomerate merger as a means to achieve this goal. This view is also shared by Mueller (1978), who stated that such managerial objectives to increase a firm's growth are increasingly achieved by engaging in mergers that are beyond the traditional industry boundaries of the firm; and Sinha (1999), who found that firms that engage in conglomerate mergers are usually less profitable beforehand. Only diversification can increase the profitability of such firms and, in turn, increase the managers' income. Furthermore, a manager might engage in a conglomerate merger that could make him indispensable for the firm. A third reason to engage in conglomerate mergers is the difference in risk preference between the owner and the firm's manager. While owners are rather risk-neutral, managers are assumed to be very risk-averse since their income is mostly tied to the firm's performance. This goes along with the principal-agency theory of different motivations between managers and owners. A final reason involves the CEO of a firm. CEOs that aim to "build an empire" may be overconfident and overinvest in conglomerate mergers to satisfy their vision (Tremblay & Tremblay, 2012).

A conglomerate can cross-subsidize by using funds from one market to increase the market share in another. This view was also confirmed by (Cox, 2006). Besides identifying the risk reduction resulting from diversification as being a primary motive for engaging in conglomerate mergers, Cox (2006) also viewed conglomerates as a source of internal capital market funds. The advantage of internal capital market funds lies within the reduced Cost of Capital (CoC) resulting from, among others, reduced transaction costs. By generating this free cash flow within the conglomerate, investments in different firms become easier, and returns are entirely captured within the conglomerate.

Several difficulties are encountered when attempting to conduct an empirical evaluation of conglomerate mergers to determine the reasons for these transactions or to observe the consequences resulting from them. Since conglomerates are active in different markets to diversify their product portfolio, it is very difficult to make comparisons between them. Furthermore, it is challenging to prove that the conglomerate is the main cause for any improvement in a firm, although this admittedly is true for any kind of merger. Despite these challenges, different evaluation methods show that many conglomerate mergers increase a firm's market value, which makes conglomerates an interesting strategy overall (Tremblay & Tremblay, 2012). In contrast, Mueller (1978) found that conglomerate mergers usually do not account for profits for the acquiring firm, and therefore do not enhance its welfare.

Conglomerates have also been given special attention by Hoberg and Phillips (2011). In their paper, they analyzed in which industries conglomerate firms produce by examining the value creation through the operation in related industries and potential industry complementarities. They found that conglomerates tend to operate in less remote industries and with high profitability. This closeness can either be in terms of the product space or opportunities between the industries. Since conglomerates and their strategy are more difficult to replicate, they also face less competition overall.

## **2.2 Finance Literature Review**

From a financial point of view, there are several additional reasons for M&A. These range from reasons of timing to tax reasons and the optimal usage of debt. Financial synergies, including the reduction in CoC, is one important factor in deciding whether to merge.

### **2.2.1 Cost of Capital**

CoC is used when calculating the value of a firm, which is important for potential investors, lenders, and other stakeholders. To compute the value of the firm according to the Discounted Cash Flow method, the Free Cash Flows produced by the firm are discounted to the present with the CoC being the discount factor. This Weighted Average Cost of Capital (WACC) is the average CoC for the firm. The discount rate not only needs to represent the time value of money but, more importantly, the risk profile of the firm (the same argumentation is applied to a project). The higher the discount rate, the riskier the business is, as a higher discount rate reduces the present value. Another way to view the discount rate is that it is the least return that is expected by both capital providers. Riskier businesses require

higher returns to compensate the capital providers for the increased risk, and subsequently the increased probability of default. This holds true under the assumption of risk averseness, which will be assumed across the argumentation presented since it is closest to the situation in real life. An evaluation of the CoC is relevant for both the acquirer and the target (Gaughan, 2007; Vernimmen et al., 2017, pp. 491-542, 555-617, 748-835; Welch, 2011).

However, the CoC is not only a measure of risk but also serves as a basis to measure whether value was added. Measures of value include the basic Net Present Value (NPV) or Economic Value Added (EVA). Simply put, value is created if the profit exceeds the CoC and is destroyed when it does not. Furthermore, using the CoC as an indicator is superior to using the Internal Rate of Return (IRR) as the CoC takes the risk of the business or project into account (Vernimmen et al., 2017).

Overall, considering the CoC is a very powerful way of not only demonstrating the risk of a business but also of considering the value added or destroyed. This measure is very important to financially evaluate whether an M&A is a profitable business decision or not.

### **2.2.2 Financial Motives for Mergers and Acquisitions**

As discussed in the previous chapter, there are many strategic reasons why companies should engage in M&A transactions. However, there is also a range of financial reasons why firms should engage in M&A. While some are purely financial motivations or indicators, many financial motives partly overlap with strategic ones.

As frequently mentioned in the literature, mergers occur in *waves*. Martynova and Renneboog (2005) found similarities across different merger waves that included mergers taking place in times of positive economic and political (recovery) and in times of booming stock markets and credit expansions (Renneboog & Vansteenkiste, 2019). They either do so by simultaneously reacting to changing market conditions, or they occur sequentially, as one player mimics the other after observing their behavior (Martynova & Renneboog, 2005).

Vernimmen et al. (2017) also found other factors that explain why M&A take place. They explained the motives with macroeconomic and microeconomic factors. Macroeconomic factors, such as technological change and innovation increase the number of M&A, as young companies with new ideas seek financing and support from mature companies looking for growth opportunities, for example, Apple buying Beats. Furthermore, Vernimmen et al. (2017) introduced changes in scope as being a major reason for M&A. This includes

companies having to operate on an international level to maintain a competitive position, which requires financing. Additionally, restructuring in many industries on a legal basis results in M&A taking place as deregulation moves many markets towards privatization. Moreover, financial markets have moved from banks being the sole investor to using the financial market as a whole and, due to this, firms have a broader spectrum of corporate finance.

### **2.2.2.1 Growth and Market Power**

Growth is a major reason to engage in M&A. However, in this case, there is an overlap between the financial and strategic viewpoints since growth is intertwined between the two. Engaging in M&A increases the speed of growth compared to organic growth, as it allows a firm to enter new markets without planning an entry strategy by themselves, and it also allows firms to expand not only the scope of their products very easily but also broadens their customer base. To enable growth through M&A, increased market shares are also important as they improve the competitive position of a firm. Engaging in M&A can either improve a firm's positioning compared to its competitors or prevent competitors from growing (Renneboog & Vansteenkiste, 2019). Campbell, Edgar, and Stonehouse (2011) created a list of success factors for a takeover to generate value. To evaluate the target, not only purely financial indicators, such as balance sheets and intangible assets are important, but also the competitiveness, which includes factors such as market share and product competitiveness. Although the exact relevance of these factors and whether they really generate value in practice are discussed below, they must nevertheless be included to perform a proper valuation.

*Growth.* Vernimmen et al. (2017) viewed growth through M&A as something natural to a firm over its life cycle as can be seen in the graph (Figure 1). After the initial launch, the cash flows increase at a high rate in the phase of consolidation, reaching a decline in growth and, in the restructuring phase, either the firm either files bankruptcy or a change of business is undertaken. This change of business can, according to the authors, best be attained by M&A as only relying on organic growth may lead to bankruptcy. As companies or industries mature, the need for growth becomes more important and organic growth is often too difficult and time consuming to attain. While M&A, on the other hand, are not an easy approach to manage, their benefits still outweigh the costs of doing so (Vernimmen et al., 2017).

*Market power.* In their paper, Devos, Kadapakkam, and Krishnamurthy (2008) also addressed the topic of market power together with increased efficiencies and tax reasons. They

emphasized the relative importance of the three factors influencing M&A and whether (or how) they create value. The market power mechanism works as follows: In a competitive environment, the merged entity can increase its sales price while, simultaneously, negotiating lower prices to pay to its suppliers. This allows the entity to increase profits or decrease costs (or both) at the expense of rivals and other stakeholders such as customers, suppliers, or the government. Nevertheless, the authors concluded that efficiency improvements rather than increased market power are the main source of value in M&A (Devos et al., 2008).

Vernimmen et al. (2017) also identified *microeconomic factors* boosting M&A. To reduce a company's costs, engaging in M&A is a tool to decrease administration, distribution, and Research & Development (R&D) costs. This was also highlighted by Jensen and Ruback (1983) who found that reducing costs is influenced by economies of scale, vertical integration, and more organized and technological productions. Other financial motives not only include increased leverage and avoidance of bankruptcy costs but also making use of underutilized tax shields. Tax efficiencies were also mentioned by Renneboog and Vansteenkiste (2019), who included the factor of acquiring targets in tax-friendly countries. Furthermore, although unclear whether these effects are solely attributable to M&A activity, the management of inefficient targets and reduced agency costs resulting from jointly managing specific business units might also generate value from M&A (Jensen & Ruback, 1983).

Vernimmen et al. (2017) also found increases in market share to be a contributing factor for engaging in M&A. Focusing on complementarity, they found both geographic and product complementarity to be tools to broaden a company's scope. Not only investments but also divestments can be of importance, as companies might also decide to again focus on their core business and therefore sell some of their business units. Another important microeconomic factor they highlighted is the time saved through an M&A. Regarding new geographical markets, the authors found riskiness to be another important factor, as entering new countries in a greenfield investment comes with increased risks. By entering new countries through acquisitions, risks are reduced, and earnings are increased (Vernimmen et al., 2017).

#### **2.2.2.2 Access to Capital and Synergies**

In his paper, Lewellen (1971) discussed the sources of merger success. He distinguished between operating and financial synergies and aimed to identify only the financial reasons for which firms engage in M&A. As an example, he explained how target and acquirer

together can utilize unused debt in cases where the target has unused debt that the acquirer could utilize. Together, after the M&A, they can optimally use the unused debt. While a high level of debt may cause firms to go bankrupt, debt also has several advantages over equity. One advantage is that debt can be cheaper for a firm than equity because, due to the higher risk of equity, a higher return is expected and required. Equity also shows increased information asymmetry compared to debt, as the true value of debt is more easily agreed upon than equity is. Having a new capital structure after an M&A may allow the combined entity to raise more debt and thereby optimally utilize the new entity's capital structure. However, this reallocation or optimization of capital structure can also be performed by good management and does not necessarily require a merger per se (Lewellen, 1971). Another advantage of debt, and probably the most important one, touches on the topic of taxes as interest expenses that must be made on the existing debt can be deducted from the tax a firm must pay. This so-called *tax shield* increases value for shareholders as the tax savings translate into savings for the firm. The tax shield amounts to the interest expense multiplied by the applicable tax rate. Consequently, as more money is available to capital providers, the tax shield increases the overall value of the firm as the tax shield is now added to the value of an unlevered firm, that is, an only-equity firm (Vernimmen et al., 2017).

Vernimmen et al. (2017) added to the discussion on optimal capital usage by indicating that some firms, for example, casinos, also need to deleverage and therefore seek for an acquisition to properly use the excess cash. Another situation might be that companies need to present capital gains on a regular basis, making M&A an appropriate means of doing so (Vernimmen et al., 2017).

### **2.2.2.3 Financial Synergies: Reduction of Cost of Capital**

“Financial synergy refers to the impact of a corporate merger or acquisition on the CoC to the acquiring firm or the merging partners” (Gaughan, 2007). This means that through M&A, CoC can be reduced. As previously mentioned, companies aspire to reduce CoC. However, there is a process behind the decreased CoC resulting from M&A. As explained earlier, the cost of capital is mainly a representation of the risk of a business or a project. The higher the risk, the higher the expected return to the capital investors to compensate them for this increased risk. If, however, through an M&A engagement, the cash flow streams are not perfectly related, that is, diversified, the risk of the combined entity is reduced because, due

to the imperfect correlation of cash flows, the two firms will most probably not experience bankruptcy at the same time, making one entity the “insuring” factor for the other one. This, in turn, reduces the CoC of the combined entity as capital investors value the firm as less risky since volatility is reduced. However, it is somewhat unclear in the literature whether these gains are mainly caught by debtholders, who then invest in a less risky business, and at the expense of shareholders (Gaughan, 2007).

Nonetheless, a merged entity can still experience advantages by simply becoming a larger entity as, due to being a larger and subsequently less risky firm, the entity has better access to financial markets and can issue securities at a lower CoC. These lowered CoC are in comparison to the single cost of capital for both firms before the M&A (Gaughan, 2007).

#### **2.2.2.4 Timing**

Timing is another very important reason for engaging in M&A. When engaging in a possible merger, a valuation is performed to determine the price of the merger. However, the value of a firm fluctuates over time and often does not correctly reflect the true value as it over- or undervalues the real value. By using undervaluation due to mispricing, the acquiring company can benefit from an increase in share price after the acquisition when the markets understand and correct this mispricing. Not only does the acquiring company pay less for the target, but it also benefits from the positive correction in value after the M&A (Gaughan, 2007; Lewellen, 1971). However, mispricing is not only an important point on the target side but also on the acquirer side. If the stock market is overvalued, acquirers may use this overvaluation to invest in an M&A transaction by paying in shares, as this makes it cheaper for the buyer (Myers & Majluf, 1984; Nelson, 1959).

### **2.2.3 Wealth Effects of Mergers and Acquisitions Activity**

#### **2.2.3.1 Introduction**

When it comes to the effects of an M&A deal, the views in the literature are divided. While short-term effects on the stock are quite easily measurable, the long-term effects present a problem, as the effect of an M&A cannot easily be distinguished from other effects at a later point (Martynova & Renneboog, 2005). Several approaches to measure the effects of M&A activity are presented in the literature in which the acquirer, the bidder, and the combined entity must be analyzed. However, they also include other stakeholders such as employees, customers, suppliers, managers, and bondholders. Managers of both target and

acquirer firms are of great importance for Welch (2011), as he found that target managers lose in acquisitions, whereas the effect on bidder managers is often positive. This is interesting, as it seems to be the opposite case for shareholders (Martynova & Renneboog, 2005).

### **2.2.3.2 Short-Term and Long-Term Wealth Effects**

It is believed that, in the short run, both the target and the acquirer somehow create value through M&A. However, most of the gains are found to be captured by the target, which is why many acquirers overpay in takeovers (Martynova & Renneboog, 2005; Welch, 2011). Whereas the target's share prices increase significantly at or around the announcement, the effect for the buyers is insignificant.

Short-term changes in return are usually measured using an event study, in which the returns around the announcement date of the takeover are analyzed (Renneboog & Vansteenkiste, 2019). To measure the short-term reaction in numbers, the abnormal return when the information of the transaction goes public can be observed. The abnormal return is the realized return less the expected return. The actual return is only realized through the announcement, or the execution of the M&A, or both. The expected benchmark return can be calculated by the Capital Asset Pricing Model (CAPM), Fama-French model, or other factor models (Martynova & Renneboog, 2005). The abnormal returns in the short term are found to be significantly positive for the target, while those for the acquirer are much lower (Jensen & Ruback, 1983).

Additionally, Martynova and Renneboog (2006) analyzed over two thousand European takeovers and found that, in the short term, most of the effects go towards the target with the announcement effect and the price increase amounting to between 9% and 21% for the target and 0.5% and 0.9% for the acquirers. They found that different takeover attributes, such as the type of takeover and the means of payment, influence the effect on both the acquirer and the target. They also found that acquisitions of private targets yield higher returns for the bidder than of public targets. The reasons for this include the illiquidity of target shares and the resulting price discount when acquiring, even when faced with the higher risk of correct valuation (Martynova & Renneboog, 2006).

When it comes to the long term, the effects on both the acquirer and the target remain unclear, as this is highly dependent on the model. Therefore, the question whether takeovers generate value in the long run or not currently remains unanswered. However, this question

is of great importance, as the actual performance of a takeover only becomes visible in the long run when integrating the target, that is, when synergies are actually being realized and not simply anticipated (Martynova & Renneboog, 2005; Renneboog & Vansteenkiste, 2019).

### **2.2.3.3 Value Generation of Mergers and Acquisitions**

Overall, it thus remains an interesting question whether M&A generate value for the engaged entities or not. As the literature remains divided when it comes to this question, several authors have different views on this topic.

For example, in their literature review, Jensen and Ruback (1983) found that M&A engagement increases value for the target firm and does not destroy value for the bidding firm. On the contrary, Welch (2011) argued that the overall benefit for both parties is equal to zero, as the benefit of the target is usually outweighed by the overpayment of the acquirer. On the other hand, Devos et al. (2008) argued that, even if the overall effect of a takeover is negative, also compared to other competitors' performance in the industry, it might still be the case that without the takeover the firms would have experienced an even worse performance. This would thus in a way still represent a value generation from the merger.

Having this in mind, Martynova and Renneboog (2005) found both positive and negative returns to be a representation of inefficient markets as any synergies should have been reflected in the original price reaction when making the M&A public. This goes back to the market efficiency hypothesis that states that information is incorporated into the share price when available, and not when actually implemented.

To explain M&A performance, Das and Kapil (2012) found 46 unique measures, which they put into categories that go beyond the prevailing measurement of abnormal returns in stock markets. Their categories are accounting/financial measures (such as asset growth or return on equity), market measures (such as returns to shareholders), other subjective measures (such as satisfaction), and objective measures, where all examples are positively related to M&A performance. Some objective measures include the age of the firm or the deal value, all of which are negatively related to M&A performance. However, the authors did not find a simple guideline for successful M&A as most of the information is only known ex-post. They found that the focus should lie on the interdependence of M&A performance measurements as these are interlinked (Das & Kapil, 2012).

However, there are many concerns when measuring the long-term effects of M&A, as the distinction is not easily made between merger effects and other effects over time (Martynova & Renneboog, 2005). Simply using accounting measures or stock returns mixes different effects with each other (Renneboog & Vansteenkiste, 2019). Furthermore, acquirers often engage in more than one takeover at the same time, making the extraction and measurement of a single transaction that the acquirer engages in more difficult. Additionally, as the acquirer is often larger than the target, the same dollar amount will increase the target's relative value more than that of the acquirer, which again makes it difficult to compare the gains in value for both in terms of absolute and relative values (Jensen & Ruback, 1983).

#### **2.2.4 Financial Conglomerates**

In the case of a conglomerate M&A, Lewellen (1971) introduced the aspect of diversification when it comes to corporate earnings. The more diversified the business, the more diversified and more stable the earnings. Gaughan (2007) called this effect the “coinsurance effect”, which results from imperfectly correlated cash flow streams of the different companies engaging in an M&A deal. Gaughan (2007) found that this is true for companies having a negative covariance, that is, if company A's cash flows are decreasing, then company B's cash flows are increasing. Shleifer and Vishny (2003) also found that, in the long run, acquisitions in different industries yield higher returns, supporting the view of diversification.

However, there are voices of concern when it comes to using M&A activity to diversify a business in a perfect market, as diversification could be accomplished by the investors themselves without the need for an expensive M&A (Lewellen, 1971; Vernimmen et al., 2017). In this case, the firms would already be included into the investors' portfolio anyway. Gaughan (2007) raised very similar concerns when stating that capital providers invest in a single company with corresponding cash flows that fit the individual portfolio. The diversification could be achieved at a lower cost by the investors themselves. Whether M&A activity for diversification is ultimately beneficial thus remains unclear (Gaughan, 2007).

In addition to agency problems providing a reason for conglomerate mergers, financial synergies or internal capital markets are also found to be of great importance because a larger diversified company can lend in between divisions without having to touch external financial markets unless these are found to be efficient and inexpensive. However, Martynova and Renneboog (2005, 2006) found this to be a problem since, in this case, divisional leaders

become competitors concerning who earns the most funding, which in turn would lead to inefficient distributions. Bargaining problems and difficulties in the back office, or bureaucracy, were also found to be a problem in diversifying takeovers. Overall, unrelated takeovers were found to be value-destroying, as a focused business is preferred by both investors and the market, as was explained previously. The effects of the announcement are found to be higher in unrelated than in related takeovers. Conglomerates are therefore often traded at a large discount that amounts to up to 15%. It was found that divesting towards more related business units indeed improves the performance of these firms, which encourages more companies to do so. To conclude, not only agency problems but also inefficiently led funds lead to conglomerates being value destroying (Martynova & Renneboog, 2005, 2006). Based on the findings, the question arises whether conglomerates are even a desirable type of firm, as most of the evidence speaks against this form of unrelated business units. Indeed, Vernimmen et al. (2017) also pointed out that the value of the conglomerate is smaller than the sum of all its business units. This difference, the so-called “conglomerate discount” is deducted by the investors due to a fear of mismanagement of the funds by investing in the conglomerate instead of investing in good outside opportunities that gain profit.

One might now wonder why conglomerates even exist in the first place if they either do not increase value, or are discounted in their value by the market, or both. The literature suggests that some companies do not suffer from this as these companies are still regarded as being optimally managed. For instance, General Electric is an example of a highly successful conglomerate, which shows that, despite the rather pessimistic findings in the literature, forming conglomerates can be a viable and profitable approach for some companies (Vernimmen et al., 2017). In fact, what might be a problem regarding market timing and overvaluation, could be an opportunity regarding conglomerates. For example, if a whole industry is overvalued, making it more expensive to bid for targets, looking for potential takeovers in other industries that are not that overvalued might be a smart thing to do. While the other authors presented here emphasized the value destruction of conglomerates, it must be noted that these evaluations were mostly performed in the short term and that when analyzing the long-term returns, conglomerates were shown to be value increasing (Shleifer & Vishny, 2003).

### **3 Application**

#### **3.1 Overview of The Companies**

##### **3.1.1 LVMH Moët Hennessy Louis Vuitton**

LVMH Moët Hennessy Louis Vuitton (LVMH), founded in 1987 by the merger of Louis Vuitton and Moët Hennessy, is one of the largest luxury firms today. The conglomerate with its philosophy “Passionate about creativity” holds 75 “Houses” (Maisons) in six distinct business groups, namely Wines & Spirits, Fashion & Leather Goods, Perfumes & Cosmetics, Watches & Jewelry, Selective Retailing, and Other Activities (see Appendix A). Fashion & Leather Goods are the most profitable group, contributing 47% of the revenue in 2020. LVMH operates in 80 countries worldwide, with Asia (excluding Japan) and the U.S. being the highest revenue markets respectively accounting for 34% and 24% of the revenue in 2020. Headquartered in Paris, France, LVMH is employing over 150,000 people and operating more than 5,000 stores. While the Arnault family group both directly and indirectly only holds 47.5% of the shares, it has 63.4% of the voting rights, thereby ensuring that the management power remains in the family with Bernard Arnault being the Chairman and Chief Executive Officer. With a revenue drop from €53.670mm in 2019 to €44.651mm in 2020, LVMH also suffered from the impacts of the COVID-19 pandemic. However, LVMH’s share price has been increasing over the past three years and has already recovered from the losses as a result of the COVID-19 pandemic in early 2020 (LVMH, 2021a, pp. 10-11, 321).

##### **3.1.2 L'Oréal S.A.**

Founded in 1909 by Eugène Schueller, (L'Oréal) employs over 85,000 people worldwide. Under Chief Executive Officer Nicolas Hieronimus, who was appointed in May 2021, L'Oréal operates as one of the largest cosmetics companies in the world. Jean-Paul Agon was the company’s CEO since 2006 and its Chairman since 2011—he further remains as Chairman as of 2021 (L'Oréal S.A., 2020b, pp. 2-8, 12). In contrast to LVMH, the company exclusively focuses on one business, namely beauty. Operating in 150 countries, the company runs five distinct business divisions: Consumer Products, L'Oréal Luxe, Professional Products, and Active Cosmetics. In 2020, its most profitable divisions were Consumer Products and L'Oréal Luxe representing 41.8% and 36.4% of its sales, respectively. Furthermore, their defined business segments are Skincare and sun protection, Makeup, Haircare, Hair coloring, Fragrances, and Others, which together comprise 35 brands (see Appendix B).

L'Oréal's biggest geographic market is in Asia Pacific, which accounted for 35% of its sales in 2020, followed by Western Europe and North America (26.8% and 24.7% of sales in 2020). In 2020, L'Oréal generated revenues of €27.992mm, down from € 29.873mm in 2019. Its share price has also been increasing for more than three years, also having recovered from the reduced profit due to the COVID-pandemic in early 2020. As of 2020, the largest shareholders of L'Oréal were Ms. Françoise Bettencourt Meyers and her family (33.17%) and Nestlé (23.20%) with the same amount of voting rights attributed to the shareholders. Nestlé is represented in L'Oréal's board of directors with two directors, vice-president Paul Bulcke and Béatrice Guillaume-Grabisch (L'Oréal S.A., 2021a, pp. 8, 14-17; 2021b, pp. 34-37).

## **3.2 Strategic Analysis**

### **3.2.1 Competition**

#### **3.2.1.1 Competition: Awareness, Motivation, and Ability**

*LVMH.* Regarding competition, LVMH is very aware that it is not only relevant for LVMH as a whole but in each of the Maisons it runs. This awareness is highlighted in their report which has a dedicated subchapter in which they claim to not only compete in products but also in geographies. As the luxury industry is fast-paced and highly demanding, each player must react accordingly. LVMH does so by recruiting people that support the craftsmanship that meets the industry demands. The firm's motivation is not only to grow but also to expand internationally and cope with digitalization, all of which is achieved through a well thought out strategic positioning that relies on the employees' skills. LVMH emphasizes the importance of its employees, as they are the ones that have to react to a fast-paced environment with sudden changes all along the value chain (LVMH, 2021b, pp. 12, 19-32).

Competitiveness, as explained by the literature, is defined by the financial ability to compete, the number and ability of the people involved, and a certain degree of flexibility to react to sudden changes on the part of rivals. As for LVMH, the financial ability is there: with an average<sup>2</sup> revenue of €43.279mm that has been growing by almost 12% yearly on average, it can present reasonable numbers in the financial department. With an average gross profit of €28.454mm, LVMH had a margin of almost 66%, on average (Table 1). By employing over 150,000 people in a very decentralized manner, the conglomerate takes a range of measures

---

<sup>2</sup> The average was taken for the years 2015–2019, while 2020 was excluded since a separation of theoretical company performance from the impact of the COVID-19 pandemic is not possible.

to achieve flexibility in the market. For example, Louis Vuitton produces some of its goods externally to keep up with demand and LVMH is currently not using its €15.8bn credit line to do so in bad times. Having kept the level of equity constant and holding a considerable amount of cash (reserves) also ensures flexibility (Table 2) (LVMH, 2021b, pp. 2, 41).

*L'Oréal.* L'Oréal also seems to be very aware of the competitive environment it operates in, as it competes with a range of different companies worldwide. One of the goals identified by L'Oréal is the achievement of performance measures, which is highly dependent on the performance of other competitors in the market. Performance conditions for directors are based on growth, both in terms of consolidated profit and growth in sales compared to competitors. To increase motivation in this regard, conditional shares are only granted if L'Oréal outperforms its competitors in terms of growth. Furthermore, the director's compensation is linked to the growth in comparison to competitors as these are the performance indicators that have been laid down. Jean-Paul Agon's variable compensation is composed of 60% financial measures that include growth as compared to competitors. On top of the €2,200,000 fixed compensation, Agon received additional variable compensation of €2,168,831 in 2019, followed by €859,831 in 2020. Additionally, Employee Share Ownership Plans were issued in 2018 to include employees in the growth of the firm. The company also emphasizes the pressure it faces regarding competition, by reacting with increased investments and research to keep up with the fast-changing environment. The beauty company summarized its focused strategy under the notion of "Universalization" (L'Oréal S.A., 2021a, pp. 20, 90). Like LVMH, L'Oréal also successfully competes in its industry. With an average revenue of €26.408mm (see Footnote 2), which grows at an average rate of almost 6% per annum, the beauty company presents an average gross profit of €19.044mm, which accounts for a 72% margin (see Table 3). L'Oréal also takes a variety of measures to ensure the required flexibility. One way of achieving this flexibility together with its employees is the flexible and remote working policy that has already been implemented in 2017. Furthermore, L'Oréal is taking advantage of innovations such as robots and automation processes to react quickly to changes in demand (L'Oréal S.A., 2021a, pp. 25, 211).

### **3.2.1.2 Competitive Stand**

*LVMH.* LVMH reports its markets shares by division and product. Its champagne brands account for shipment shares of 21.3% in the Champagne region, whereas Hennessy is the

market leader in Cognac with a share of 52%. While no market share is reported in the Fashion & Leather Goods and the Watches & Jewelry division, it should be highlighted how fragmented the overall market is for these segments, which suggests that there is no market leader as the market is large enough for many players to exist. However, LVMH's brands are represented worldwide, making it a very globalized firm in this segment. As part of the Selective Retailing division, their Duty-Free Shoppers (DFS) are performing very well in the competitive market. Sephora seems to be more of a "miracle child," as it managed to become a market leader in the U.S. and Canada, and increase its market shares in France and the Middle East (LVMH, 2021b, pp. 20-31).

*Defining LVMH's competitors.* While the identity of competitors should generally be fairly straightforward to determine, it is more challenging in the case of LVMH. On the one hand, LVMH competes with other luxury conglomerate holdings like itself. On the other hand, all 75 Maisons are in competition with their rivals in the respective market segments. When considering the leading luxury companies, the list would include LVMH, EssilorLuxottica, Richemont, Kering, Chow Tai Fook, Swatch, Hermès, Ralph Lauren, Tapestry (Formerly Coach), and Capri Holdings (formerly Michael Kors). According to this data, LVMH on average accounted for 36% of sales for the past 10 years among the top 10 (EY, November 9, 2019). Extracting Bloomberg's multiples analysis from different industry classifications, the most frequently mentioned competitors are Cie Financiere Richemont SA and Kering SA (see Table 4). When considering the most valuable luxury brands in the world, Louis Vuitton's biggest competitors would be Chanel, Hermès, Gucci, Rolex, Cartier, Christian Dior, Saint-Laurent/Yves Saint Laurent, and Burberry (BrandZ & Kantar, 2020).

From the above, it is clear that the question regarding the identity of LVMH's biggest competitor is not an easy one to answer. Nonetheless, some names occur more often in competition analyses, such as Kering and Richemont, which will be used as LVMH's biggest and most powerful competitors in the luxury market (see Appendix C and D for a list of brands). However, analyzing market shares is not as black and white as in the books. While, for example, Hennessy has a very high market share in the Cognac industry, the question remains how this translates to LVMH's market share in the overall luxury industry.

*L'Oréal*. The French beauty firm not only competes with luxury brands such as LVMH but also with other companies such as Unilever. According to L'Oréal, its list of main competitors include Unilever, Procter & Gamble, Estée Lauder, Shiseido, Beiersdorf, Johnson & Johnson, Henkel, LVMH, Kao, and Coty. In 2019, L'Oréal was by far the global leader in the cosmetics market with \$33.4bn sales, followed by Unilever and Estée Lauder with sales amounting to \$22.5bn and \$15.9bn, respectively. L'Oréal attributes its success to its single-focused beauty strategy that allows the company to respond quickly to changes relating to beauty in society. L'Oréal operates in 150 countries worldwide and has largely recovered from the 2020 pandemic crisis. In particular, during this time consumer products grew faster than the overall market, which is mainly due to e-commerce with the main drivers being Garnier and L'Oréal Paris. Its high-end division, L'Oréal Luxe, has also outperformed the market in the previous year due to increased digital presence, mainly with Lancôme, Kiehl's, and Helena Rubinstein. Active Cosmetics, which also performed well despite the crisis, built CeraVe to now be one of the top five players in dermatological cosmetics worldwide. Lastly, L'Oréal's professional division that equips hairdressers and stylists again realized in 2020 how crisis-proof this segment is (L'Oréal S.A., 2021a, p. 89; 2021b, pp. 34-56).

### **3.2.2 Strategy**

#### **3.2.2.1 Strategic Overview**

*LVMH*. LVMH presents six pillars as its business model, in which it rather takes the role of a decentralized back office, thereby leaving most of the responsibility with its Houses. These Houses should grow organically and vertically integrate along the production process. Furthermore, the balance between geographic markets and different business products is viewed as a strong positioning against unfavorable market changes (LVMH, n.d.). Each group defines its own strategic goals, where Wines & Spirits focus on value-enhancing business decisions and Perfumes & Cosmetics emphasize their creativity while focusing on the global expansion, thereby largely concentrating on Dior. The top priorities of Fashion & Leather Goods are the development of Louis Vuitton's quality and exclusive distribution, as well as continuing the growth of Dior and maintaining the success of Celine, Loewe, Fendi, and Loro Piana. The Watches & Jewelry business group aims to integrate Tiffany & Co., LVMH's latest acquisition, as well as further developing its craftsmanship, distribution, and

manufacturing facilities. Meanwhile, the Selective Retailing group is more focused on its overall development of successful Maisons such as Sephora (LVMH, 2021a, pp. 46-104).

*L'Oréal.* The company solely focuses on one business, namely beauty. While L'Oréal operates in different segments of the beauty market, including high-end products and more affordable beauty items, it still focuses on a single business. Focusing on one unique strategy allows L'Oréal to react quickly to changes in the market regarding customers and their needs. L'Oréal is implementing its strategy by integrating acquired brands and boosting their organic growth (L'Oréal S.A., 2021a, pp. 3, 14).

### **3.2.2.2 Cost Leadership, Differentiation, or Focus**

As shown in the literature, to compete in a given market, a company must decide whether to follow a cost leadership, differentiation, or focus strategy.

*LVMH.* Being one of the top players in the luxury industry, LVMH is not following a cost leadership strategy as its promise is the best quality and craftsmanship in the market, which has a certain price tag attached to it. However, choosing between differentiation and focus is more challenging than it may seem at first. To some extent, LVMH follows a differentiation strategy by creating a certain luxury brand image that is associated with almost all of its Maisons. However, the French conglomerate does not exclusively focus on one segment line, product, or geographic area, as emphasized by the six pillars that comprise its operating model, with one pillar addressing the balance between segments and geographies to ensure growth (LVMH, 2021b, p. 12). While the geographic or product focus is not given, LVMH indeed addresses a certain buyer group, namely one with enough money to purchase its products. However, this again is not entirely true for all its Maisons. For example, when on sale, Fenty's "Mattemoiselle Plush Matte" Lipstick costs as much as NYX Cosmetics' "Lip Lingerie Nude Matte" Lipstick, with NYX Cosmetics being part of L'Oréal's affordable business divisions (Fenty Beauty LLC, 2021; NYX Professional Makeup, 2021). While some of LVMH's Maisons are not as luxurious as Louis Vuitton or Moët & Chandon, non-high-end brands provide an entry for the luxurious Maisons. One very good example of this is Tiffany & Co. While their strategy was developed before LVMH acquired the U.S. jeweler, the example is still representative of LVMH's more affordable Maisons. Tiffany has a section on their website dedicated to lower-income customers called "Gifts \$500 & Under," in which

all products are sold for \$500 and below. While one could argue that Tiffany is not increasing its revenues and prestigious images through this campaign, it is very strategic as it attracts customers at a very young age with a rather low income. Subsequently, as a result of this approach, up-selling to such customers at a later stage in their lives when their income has increased is far easier as they will hopefully purchase more expensive Tiffany products although the customer acquisition took place much earlier at lower costs (Cohan, 2019). Nonetheless, the overall luxury and excellent craftsmanship LVMH advertises with most of its Maisons is rather expensive, and therefore addresses a certain income group worldwide. LVMH emphasizes this through the six pillars in its operating model that follow growth, sustainability, and a commitment to excellence, which can be seen as a focus on the production and the brand (LVMH, 2021b, p. 12). Overall, LVMH therefore appears to follow both a differentiating strategy through its brand image, and a focus strategy by addressing a certain group.

*L'Oréal.* In terms of cost leadership, differentiation, or focus, it is very interesting to classify the French beauty brand, as the answer is not as obvious as it may seem beforehand. While L'Oréal does not directly follow a cost leadership strategy, its affordable division Consumer Products offers high-quality products at affordable prices. Brands such as L'Oréal Paris, Maybelline New York, or Essie, are affordable brands represented in basic drug stores all over the world. While price and quality should not be a tradeoff, L'Oréal seems to place great value on ensuring the highest quality possible. Indeed, being a large holding company ensures that lower-end brands benefit from other cost savings and synergies to keep the products' quality at a high standard. This view is supported by the fact that L'Oréal reports its Research & Innovation costs on a consolidated level and, in its reports, speaks about the Group holding more than 20 research centers. Differentiation, that is, the unique position a company is located at within an industry, can be accomplished through a very specific brand image, well-functioning technology, or excellent customer service. While L'Oréal claims to focus on all three of the factors mentioned, the company, with its four very different divisions, does not seem to follow a differentiation strategy. Instead, L'Oréal focuses on one aspect: beauty. While this does not include one buyer group or a specific geographic market, it does address one product line, namely the beauty cosmetics segment. However, within this

segment, L'Oréal addresses different customer groups ranging from high-end customers and hairdressers to low-end consumers and price-sensitive consumers (L'Oréal S.A., 2021a).

### **3.2.2.3 Market Commonality and Resource Similarity**

#### Market Commonality

As described in the literature review, market commonality occurs when rivals compete in more than one market at the same time. Having 75 Houses in six business groups, the question of multiple markets regarding LVMH need not be further discussed. However, while L'Oréal is mostly focused on beauty cosmetics, they compete in different markets within this industry. This includes their affordable section, the high-end lines, the products for professionals, and their dermatologic division. While LVMH only dedicates one of its business groups, namely Perfumes & Cosmetics, to beauty, L'Oréal divides its segments into Skincare and sun protection, Makeup, Haircare, Hair coloring, and Fragrances. As LVMH is a luxury holding, they mostly compete with L'Oréal's high-end lines and dermatologic division. Its affordable section only indirectly competes with LVMH's Maisons as it operates in a different price segment and therefore addresses different customer groups. However, lower-price brands could indeed compete with LVMH's luxury brands, as competition cannot be ruled out entirely due to the price. While LVMH's products might also be used in a professional environment, L'Oréal dedicates one business group solely to this target group and is therefore not a direct competitor to LVMH in this case. Overall, LVMH competes against L'Oréal in the Perfumes & Cosmetics business group, by competing with L'Oréal's Skincare and sun protection, Makeup, and Fragrances segments.

*LVMH.* Regarding LVMH and its most important competitors Kering, Richemont, Dior, and Hermes, LVMH mostly competes with Kering and Richemont in different markets. Founded in 1963, Kering also operates in the luxury segments Couture and Leather Goods, Watches and Jewelry, and Kering eyewear. Its categories include Leather goods, Shoes, Ready-to-wear, Watches and Jewelry, and Others such as eyewear and textile accessories. Kering's Houses include big brands like Gucci, Yves Saint Laurent, or Balenciaga (Kering, 2021). On the other hand, Richemont operates 26 Maisons in the segments Jewelry, Watchmakers, Online distributors, and Fashion and Accessories, with its jewelry segment accounting for 51% of the sales in 2020. Founded in 1988, the Swiss company now holds brands

such as Cartier, Iwc Schaffhausen, Net-A-Porter, and Chloé (Compagnie Financière Richemont SA, 2021). As shown, LVMH competes with both Kering and Richemont in several markets. LVMH and Kering are rivals in the Leather goods, Shoes, Watches and Jewelry, and textile accessories segment, while LVMH and Richemont compete in the Jewelry, Watchmakers, and Fashion and Accessories Segment, with online distribution being an overall competition in today's world. For example, acquiring Tiffany & Co. LVMH not only affects Richemont's Jewelry segment but also broadens LVMH's overall standing in the luxury sector, thereby affecting Richemont's performance.

### Resource similarity

Resource similarity is an important aspect for both companies, although not with every one of LVMH's divisions. Needless to say, a yacht has different (in-)tangible assets than jewelry or a handbag. However, comparing the resources between LVMH and L'Oréal is closely related to comparing the market commonalities as this only affects LVMH's Perfumes & Cosmetics group. However, when it comes to resources, LVMH competes with nearly all of L'Oréal's business divisions and segments, as the resources used are very similar overall. Nonetheless, since it affects more of L'Oréal's business, the resource similarity is more important to L'Oréal than it is to LVMH as only one of its groups is affected by L'Oréal.

For LVMH and its main competitors, Kering and Richemont, the situation looks very different. As all three operate, amongst others, in the Watches and Jewelry segment, which requires very specific resources, the resource similarity is higher between these direct competitors and LVMH.

On the firm level, LVMH and L'Oréal do not show a high degree of market commonality and only a moderate level of resource similarity. As these two factors determine the similarity of the two firms in terms of strengths and weaknesses, it can be concluded that LVMH and L'Oréal, on the firm level, are not very similar. However, LVMH's Perfumes & Cosmetics group and L'Oréal share very similar traits, making LVMH's group look very similar to L'Oréal as they share many of the same strengths and weaknesses when it comes to the overall market. However, the effect on LVMH seems to be very low as the Perfumes & Cosmetics group only accounted for 12% of LVMH's 2020 sales, and therefore a definite statement cannot be made regarding LVMH in this context. While resource similarity usually

influences a firm to react to sudden changes in a competitive environment, both LVMH and L'Oréal demonstrated their ability in this regard as was previously discussed.

#### **3.2.2.4 Diversification and Relatedness**

As mentioned in the previous chapters, diversification and relatedness are important for the strategic decisions of a firm. Relatedness refers to markets, technologies, and distribution channels that are shared between distinct business units of a firm, while diversification regards its products and markets. Conglomerates require both a low level of relatedness together with a high level of diversification.

*LVMH.* LVMH follows a diversified strategy when it comes to markets with its 75 Maisons in six distinct business groups. The Chairman also stated that the conglomerate not only diversifies geographically but also business-wise (LVMH, 2021a, pp. 6-12).

The Maisons operate independently, but also have a common responsibility, as defined by LVMH's six pillars regarding the operating model. The development and use of synergies between the different Maisons should nonetheless be exploited (LVMH, 2021b, p. 12). Intra-Group synergies are used for negotiating advertising space and in department stores, while distribution is also shared between the Maisons, thereby increasing the presence and expansion of the brands through economies of scale. This especially benefits the Perfumes & Cosmetics business group, which also contributed to most of the intra-Group sales with €792mm in 2020 (overall intra-group sales amounted to €938mm in 2020) (LVMH, 2021b, p. 248).

Most of LVMH's brands in the Perfumes & Cosmetics group are sold through the group's retailers. For example, Christian Dior perfumes, Make Up For Ever, and Kendo are sold through Sephora. R&D is also conducted in the same centers, for example in the center located in Saint-Jean-de-Braye, France. The production of Benefit, Perfumes Loewe, and Fresh, mostly takes place in other Maisons under the LVMH umbrella. In the Fashion & Leather Goods group, LVMH is responsible for the retail distribution in its network, which consists of more than 2,000 stores. LVMH even acquired the calfskin supplier Tanneries Roux in 2012. The Watches & Jewelry group can benefit from a large range of shared resources that include design, investment, and productivity, in addition to the negotiation with suppliers and centralization of diamond purchases. The Maisons TAG Heuer, Hublot, Zenith, Bulgari, Montres Dior, Chaumet, and Fred produce together in their production facilities in Switzerland. LVMH's Other Activities are very diverse in terms of the relatedness in their

production or distribution, as this group includes a yacht builder, a newspaper, and a hotel chain. Overall, the highest level of relatedness can be found in the Perfumes & Cosmetics and the Watches & Jewelry groups (LVMH, 2021b, p. 25).

While LVMH focuses on diversification, relatedness may well be observed within the business groups. Key examples include the Watches & Jewelry and the Perfumes & Cosmetics business groups that benefit from shared resources. However, the overall relatedness in the group is rather low. Therefore, LVMH can be seen as a conglomerate, with some exceptions regarding the relatedness in distinct business groups.

*L'Oréal.* L'Oréal, as the group supporting its brands, provides the R&D, Digital, and Operations sections in the firm. Operations include the sourcing, production, packaging, and distribution of each brand's products. Furthermore, L'Oréal plans and monitors the strategic, financial, and Human Relations segments, in addition to the brand communications. Brands are heavily supported by media investments to boost growth and sales. However, these contributions are mostly applicable to the French subsidiaries operating in France. The non-French subsidiaries develop strategies that are specific to their markets, which includes individual target groups, sales channels, production, and overall choice of market. As a group, L'Oréal still provides support and indicators to all its subsidiaries for aspects such as packaging, purchasing, and manufacturing. The Group division thus leads the global operations strategy, which is also audited regularly. The manufacturing is organized into special units, such as haircare, makeup, or skincare. The most important shared resource, however, appears to be the R&D facilities that L'Oréal built over the years. With a Research & Innovation budget of €964mm, 21 cosmetic research centers, and 13 evaluation centers, L'Oréal employs nearly 4,000 people in this area. Additional support is mostly obtained by sending specialists to the respective geographic locations, advising on all relevant factors for pursuing and monitoring L'Oréal's strategic and financial goals (L'Oréal S.A., 2021a, pp. 14-15, 23, 43).

L'Oréal markets, however, are more similar as the company is solely active in the cosmetics market. While its divisions target different customers, up- and cross-selling are perfectly possible as a young person with less financial means will have different possibilities later, thereby possibly switching from the Consumer Products division to the Luxe division.

### **3.2.3 Growth Without Acquisitions**

#### **3.2.3.1 Organic Growth**

To evaluate LVMH's and L'Oréal's organic growth, both fiscal years 2019 and 2020 were considered in the analysis to partially separate the company effect itself from the impact of the COVID-19 pandemic.

*LVMH.* The French conglomerate has always balanced its growth between acquiring and boosting organic growth in its existing Maisons. In 2019, out of the 15% revenue growth overall, 10% was due to the organic growth of its 75 Maisons. For example, its Perfumes & Cosmetics business group achieved overall organic revenue growth of 9%, mainly by satisfying in-creased demands in East Asia. Furthermore, its champagne houses benefited from organic growth of 4% by increasing its product prices in conjunction with keeping the quantities constant. Sephora, as part of the Selective Retailing group after its acquisition in 1997, was mainly responsible for the 4% revenue growth in the business group. LVMH provided several reasons for Sephora's strong performance in 2019. Besides opening 110 additional stores and renovating key stores, it also boosted innovation in digitalization, introduced new marketing campaigns, and offered increased personalization in the shopping experience and product selection (LVMH, 2020, pp. 18, 26, 32, 36).

In 2020, LVMH's market in Asia (excluding Japan) grew, as travel restrictions increased domestic consumption. As one of its six pillars, LVMH emphasizes internal growth and makes it a top priority in its operating business model. Another pillar is addressing the balance between products and geographies, enabling the conglomerate to continue growing due to its good positioning. For example, in 2020 the Perfumes & Cosmetics business group achieved growth in its brands due to decisions such as launching a new perfume by Maison Francis Kurkdjian or by pairing new launches with diversity and sustainability, such as Guerlain. The whiskey producers Glenmorangie and Ardbeg increased their brand positioning by winning awards. Sephora also continued growing in 2020 through new brands, thereby increasing its positioning in the haircare and skincare segment "Good for skin.you.all," and implementing several international campaigns. While Sephora opened many more stores in 2019, it opened a new flagship store in Paris to ensure its presence in the French capital (LVMH, 2021b, pp. 12, 32).

*L'Oréal*. In 2019, growth in the Professional Division was mainly driven by geographic growth in the U.S. and the Asia Pacific region. In the consumer products division, L'Oréal also used new product launches to ensure growth. Examples include the L'Oréal Paris “Rouge Signature” and “Revitalift Filler.” Garnier is experiencing growth through its campaigns in organic products; however, it is also profiting from its successful tissue masks and cleansing waters, which were increasingly sold in the emerging markets, thereby increasing its presence in new geographic markets. L'Oréal Luxe's business division also experienced growth by increasing its market share in several geographic regions through its Travel retail market and its expanded digital sales (L'Oréal S.A., 2020a, pp. 22, 34).

By integrating its acquired brands, L'Oréal boosts organic growth by actively penetrating several markets. In 2020, the company experienced growth in its new markets, despite the global pandemic. The main drivers in these markets were the performance of the Active Cosmetics division and the boost of digital sales in markets such as Latin America, Eastern Europe, the Middle East, and Africa. L'Oréal's Luxe division experienced a recovery in 2020 by increasing its digital and individualized presence in the market and by the launch of new products. Giorgio Armani, Valentino, and Yves Saint Laurent launched new perfumes in the fiscal year that were successful in increasing their overall brand standing. The Active Cosmetics division also improved its performance by increasing its overall digital presence and store campaigns. One main growth driver of this division is the increasing awareness of and preference for medicals in the beauty segment, which drives sales of L'Oréal's Active Cosmetics division. Vichy also benefitted from the launch of a new anti-aging serum that met the approval of consumers. The Professional products division experienced growth due to the increasing importance of product distributors, such as SalonCentric. Its brands succeeded in the market due to the launch of new products and the good sales performance of its existing products. The Consumer Products division experienced growth by partnerships with retail stores, media investments, and increasing its digital presence. Successful products were in the hair color, skin care, and makeup segments. Especially haircare and skincare benefitted from the successful launch and popularity of existing L'Oréal Paris and Garnier products. As digital experienced a major increase in demand, L'Oréal has hired almost 50,000 employees dedicated to this topic. Nicolas Hieronimus, the former Deputy CEO, identifies overall growth in demand to be due to the increasing number of upper- and middle-class consumers,

young people purchasing beauty products at a younger age, men engaging in beauty, beauty conscious seniors, and urbanization (L'Oréal S.A., 2021a).

### **3.2.3.2 Strategic Alliances, Licensing, and Subsidiaries**

*LVMH.* LVMH does not hold all its brands as direct subsidiaries, but subsidiaries are held by sub holdings that, in turn, are owned by LVMH. These sub holdings include Moët Hennessy, LV Group, or Sofidiv (see Appendix E and F). LVMH is therefore further away from its Maisons than expected. For example, LVMH only holds 66% in Moët Hennessy, which, in turn, holds 100% of Dom Pérignon (LVMH, 2021b, pp. 6-7). Nevertheless, there is a range of advantages that correspond to this type of holding. A holding has a more advantageous tax system, not only because of the reporting to the mother company but also because the profits and losses can, to some extent, be taxed together. This serves as a safety net for the conglomerate. On the other hand, if subsidiaries need financial help, the holding can more easily distribute money to them. Furthermore, profits can be more easily stored at the end of the fiscal year instead of distributing or reinvesting them right away, thereby allowing the holding to wait for better investment opportunities. Another advantage is that the company will not be distributed after the death of a family member overseeing the company, which is significant when bearing in mind that the Arnault family group owns 47.5% of the shares with 63.4% of the voting rights and Bernard Arnault is the Chairman and CEO. Probably the two most important reasons for LVMH to take the approach outlined above are the decrease in risk and the independent brand image to the outside. By owning a variety of holdings and sub holdings, the risks related to each brand are minimized for the overall holding as they operate independently and by keeping the brands further away from the name “LVMH” they are more likely to develop and establish themselves on the market rather than being associated – for better or worse – with the parent company (Breit, 2021).

Although, as of 2020, LVMH does not have any active licensing programs, they do invest in Joint Ventures. For example, LVMH holds 50% in both a wine estate in Gironde, France, and activities operated by Belmond, Peru. Furthermore, the conglomerate holds 40% of the company that owns the building LVMH is headquartered in Paris, France. They also hold a 45% stake in an Indonesian retail company that, in turn, owns sale licenses in duty-free shops at airports. Other stakes include JW Anderson (46%), L Catterton Management (40%) managing investment funds, and Stella McCartney (49%).

*L'Oréal*. To treat skin inflammations such as eczema, L'Oréal entered a licensing agreement with Microcos, which researches bacterial biotechnologies. In 2020, the company also continued its licensing agreement with Dr. Takami, a high-end skincare brand, thereby increasing its stake by also expanding the agreement with Takami clinics. Takami, licensing Takami Co.'s products and owned by Dr Hiroshi Takami, was acquired by L'Oréal in early 2021 into the L'Oréal Luxe division. L'Oréal also has a range of subsidiaries operating in the respective regions they are headquartered in. By mostly owning 100% of these subsidiaries, L'Oréal also has full control of them and, as all goals and rules mentioned in L'Oréal's report fully apply to the subsidiaries, "the Group" includes all subsidiaries (see Appendix G). In the past, L'Oréal engaged in a licensing agreement with Prada (2019), a strategic agreement with Nestlé (2014), and licenses with Armani and Valentino (2018) (L'Oréal S.A., 2021a, pp. 22, 72, 307). The agreement with Prada, signed in December 2019, included the production, development, and sale of beauty products for Prada. The long-term agreement aimed to combine both companies' expertise in the given sector, which is beneficial for L'Oréal in the L'Oréal Luxe Division by including this "emblematic" brand (L'Oréal S.A., 2020a, p. 22). In 2018, L'Oréal decided to renew its license agreement with Armani until 2050, showing long-term confidence and commitment from L'Oréal's side. The license agreement with Valentino includes fragrances and beauty products that will be produced, developed, and sold under the Valentino brand name (L'Oréal S.A., 2020a, pp. 40, 72). L'Oréal's relationship with Nestlé is interesting as it is based on the partnership between Liliane Bettencourt and Nestlé that was in place since 1974. However, after she died in 2017, the shareholder agreement expired and Nestlé decided not to renew the agreement. Over the years, the agreement also included not increasing each other's shares as L'Oréal was defending a takeover from Nestlé. However, Nestlé is not planning on selling its shares in L'Oréal as these were very profitable to the food group throughout the agreement (Bürgi, 2018). Nonetheless, L'Oréal and Nestlé entered into agreements such as the Joint Venture Laboratoires INNEOV or Galderma, both with a 50-50 stake. Inneov was created to produce cosmetic supplements. However, the joint venture was terminated in 2015 as it did not meet the expectations of both parties (L'Oréal S.A., 2002; Reuters Staff, 2014). In 2004, Bettencourt and Nestlé signed a memorandum of

understanding to provide for the merger of Gesparal with L'Oréal. As of 2020, Nestlé held 23.20% in L'Oréal and has provided two directors (L'Oréal S.A., 2021a, p. 356).

### **3.2.4 Acquisitions**

#### **3.2.4.1 Overview of Acquisitions**

*LVMH.* LVMH acquires in all its business divisions worldwide. Acquisitions are made to either complement the portfolio, enter niche markets, or expand geographically. Examples include Maison Francis Kurkdjian, a perfume niche firm, Belmond, which is active in luxury tourism, and Château d'Esclans and Château du Galoupet, to expand the market for high-end rosé wines. All the acquisitions were made under the umbrella of “luxury,” with more recent acquisitions, such as Rihanna’s Fenty, entering the more culturally diversified market (Fenty Beauty by Rihanna was acquired in 2016, Fenty in 2019) (LVMH, 2021b, pp. 5, 14-34).

*L'Oréal.* Acquisitions are a major pillar of L'Oréal’s success. The French cosmetics company acquires on a regular basis to add to the portfolio and react to changes in demand. Through acquisitions, the company aims to expand both in terms of brands and geography. The acquired brands, after being integrated, support L'Oréal’s long-term organic growth and complement the overall portfolio. Under the universalization strategy, L'Oréal solely acquires brands that belong to the beauty and cosmetics segment. For example, the company acquired ModiFace in 2018 to accelerate its digital strategy (L'Oréal S.A., 2021a, pp. 22-23).

#### **3.2.4.2 Types of Acquisitions**

*LVMH.* Since 2012, LVMH has acquired companies in all its business groups as can be seen both in the acquisition selection and in the difference between consolidated companies the conglomerate holds (see Appendix H, Figure 3, and Table 5). Since LVMH, unlike L'Oréal, does not provide a list of acquisitions, previous acquisitions were used to predict in which business group the greatest increases in growth were recorded. While the increase in consolidated companies does not differ between acquisitions and greenfield investments, it is the closest measure one can find that indicates where LVMH invests most in.

When analyzing the selected acquisitions LVMH made in the past, it becomes clear that most of the acquisitions were made in the Fashion & Leather Goods business group (eight acquisitions), followed by Other Activities and Wine & Spirits (five and four acquisitions, respectively). Comparing the overall increase in consolidated companies between 2012 and

2020, one finds that the highest absolute increase can be found in the Other Activities business group (+228), followed by Fashion & Leather Goods (+163). These absolute numbers correspond with relative increases in consolidated companies of +262% in Other Activities, followed by in Fashion & Leather Goods (+60%), Perfumes & Cosmetics (+45%), Watches & Jewelry (+20%), Wine & Spirits (9%), and Selective Retailing (+6%).

While some business groups had significantly fewer consolidated companies, this does not touch on the topic of the overall value or importance of these firms to LVMH. For example, Fenty's acquisition only increased the number of consolidated companies by three, but it was an important milestone towards a culturally diversified portfolio of Maisons as well as a brand in itself. Furthermore, while Selective Retailing had the smallest increase in consolidated companies in both absolute and relative numbers, it accounted for an average of 30% revenue proportionate to total sales. The analysis of historical acquisitions also gives insight into where LVMH's focus lies in this respect.

When comparing LVMH's acquisitions with the past performance of its business groups, Fashion & Leather Goods and Selective Retailing contributed the most to overall sales, with an average of 36% and 30% of all sales, from 2012 to 2019. Again, 2020 was excluded from the revenue analysis due to the unexpected disruption caused by the COVID-19 pandemic. The business groups Wine & Spirits, Perfumes & Cosmetics, and Watches & Jewelry contributed 13%, 12%, and 9% to overall sales, respectively. Interestingly, the average revenue growth between 2012 and 2019 was more aligned. All business units' revenue grew between 10% and 13%, except for Wine & Spirits, which grew at a rate of 6%.

LVMH seems to acquire mostly in business groups that already account for a large amount of percentage of sales (Fashion & Leather Goods and Selective Retailing), with corresponding high average rates of revenue growth. However, many acquisitions were also made in the business group with the least average rate of revenue growth, namely Wine & Spirits, which probably requires the biggest boost in performance overall.

*L'Oréal.* L'Oréal acquires companies to either purchase a brand or expand into a geographical market. Out of the eighteen acquisitions that are mentioned in the annual reports since 2012, eleven were made for brand reasons, and seven were made for geographic purposes (see Appendix I).

Out of the eleven brand acquisitions made, six were made in the L'Oréal Luxe division, two in each Consumer Products and Professional Products, and one was made in the Active Cosmetics Division. However, the Consumer Products division accounted for an average of around 47% of all revenues of the Group, and L'Oréal Luxe for approximately 30%. Regardless, L'Oréal Luxe showed the highest average growth with around 11% yearly, whereas Consumer Products only grew at an average rate of approximately 8% yearly. Most acquisitions were therefore made in a division with a medium contribution to overall sales, but with high average growth rates.

Acquisitions for geographical reasons were made in the “new markets,” namely Africa, Latin America, and Asia Pacific. Out of the seven takeovers in total, three were made in Latin America and the Pacific, and one was made in Africa. Firms were acquired in India, Brazil, Kenya, China, and South Korea. Between 2012 and 2019, most of the sales were generated in Western Europe and North America (32% and 26% of total sales, respectively), while Asia Pacific generated around 24% of sales and the remaining areas (Eastern Europe, Latin America, Africa, and the Middle East) contributed less than 10% each. Most of the growth occurred in Asia Pacific with an average of 13%, followed by Africa/Middle East with 8%, and North America with 7%. The remaining areas grew at an average rate of 3% or lower. Acquisitions were both made in regions with high contributions to revenue and high growth rates, and in regions with rather low contributions to sales and low growth rates.

### **3.2.4.3 Acquisition Motives**

The literature review identified a range of motives why acquisitions occur. While some of these can be identified from the accessible publications of both firms, a range of information is undisclosed and therefore estimated in this thesis. A list of acquisition motives is discussed in the following section based on an example for both LVMH and L'Oréal.

#### **3.2.4.3.1 LVMH and Tiffany Co.**

On November 25, 2019, LVMH announced in a press release that it entered an agreement to acquire Tiffany & Co. The original deal structure had a value of \$16.2bn, which was later adjusted to \$16.1bn due to subsequent events. With more than 300 stores worldwide, Tiffany is a leading luxury jewelry brand that was founded in 1837. Employing more than 14,000 people, Tiffany joined LVMH's Watches & Jewelry business group in designing and producing jewelry, watches, and accessories. LVMH was expected to benefit from Tiffany's

strong standing in the jewelry industry and its good positioning in the U.S., as this region still bears expansion potential for LVMH. Tiffany was expected to benefit from LVMH's resources, investments, and know-how about the industry. LVMH initially invested in Tiffany's development to boost long-term growth. To secure long-term growth Tiffany will expand onto the Asian market and will probably focus on specific product pillars or existing jewelry lines. The jewelry company might also focus more on high-end consumers by increasing offers in the jewelry segment. Therefore, the acquisition aimed to retain the existing customer group as well as expand it. The deal was expected to increase LVMH's Watches & Jewelry business group's profit, proportionate to overall profits, from 7% to 13%, which almost doubles that of the whole business group (LVMH, 2019; 2021b, p. 47; Olbertova, 2019; Piscioneri, Aloisi, & White, 2021; Spencer, 2019).

As the fifth largest jewelry firm worldwide, Tiffany has been in a turnaround period for some years as the management and executive level had to undergo several changes. Its margins also decreased slightly in the recent past (before the COVID-19 pandemic) due to changes in millennials' taste, to which Tiffany had difficulties in reacting accordingly. While Tiffany is still one of the best-known jewelry companies, it is underrepresented in Asia and Europe, despite being second after Cartier in China. Acquiring Tiffany would increase the number of LVMH U.S. stores by 16%. LVMH has increased its presence in the U.S. in recent years by, for example, acquiring Rihanna's Fenty, and opening a Louis Vuitton factory in Texas. This deal was the largest under Mr. Arnault to date (Arnett, 2019; Olbertova, 2019; Piscioneri et al., 2021; Spencer, 2019; Televisory, 2019; Tsang & Friedman, 2019).

While the jewelry industry has high entry barriers, LVMH bypassed these barriers by acquiring Tiffany, which already has a developed standing in the industry. Especially since Tiffany manages its own diamonds and other raw materials supply, LVMH can bypass these huge entry barriers that players in jewelry industry are presently faced with. Entry barriers are present in a range of industries and markets. While some of these barriers are too expensive to break, others would consume too much time or require too much expertise. Entry barriers include high upfront investments, incumbents' reactions, technological knowledge and patents, and licenses. High upfront costs are a major entry barrier for LVMH. Especially in the Watches & Jewelry industry, upfront investments are especially high as a firm must not only build plants, but also find raw material suppliers and, if necessary, mines in case

diamonds are being used for production. These entry barriers go hand in hand with the reduction of costs of developing new products, avoiding investments in R&D, information acquisition, and learning new capabilities. As Tiffany never outsourced its diamond supply chain and other materials relevant for the production, LVMH could simply acquire Tiffany's supply chain and vertically integrated business model. Furthermore, Tiffany owns manufacturing facilities that LVMH can use, thereby eliminating the need for high investments upfront. Lastly, LVMH acquired all the jeweler's stores, with the flagship store on 5th Avenue in New York City being of the greatest importance historically due to the film *Breakfast at Tiffany's*. Since Tiffany's products range from the *Under \$500* section to diamond necklaces and the famous engagement ring line, its product portfolio is already reasonably large, which would allow LVMH to now support specific jewelry lines or expand its watches section. No matter which of these LVMH decides to pursue, the products are already there, and Tiffany has been a well-known brand for more than one century, who even *owns* the color, Tiffany Blue. Since Tiffany is also successful in e-commerce, LVMH also received access to this information and success strategy (Piscioneri et al., 2021; Spencer, 2019; Televisory, 2019).

Through the acquisition of Tiffany, LVMH could further diversify its Watches & Jewelry business group. As silver jewelry has a high margin of up to 90% and is mostly purchased by younger consumers with less money, LVMH could complement its business group that includes high-end brands such as Bulgari. By expanding its target consumer group, LVMH can diversify its overall business and follow its strategy of expanding further into the U.S. where LVMH still has room for improvement (Piscioneri et al., 2021).

LVMH has already proven itself to be a successful acquirer, by having the necessary experience. In 2011, LVMH successfully acquired Bulgari, and therefore some strategies could be copied for Tiffany's integration post-merger. However, Tiffany and Bulgari are not interchangeable as they have a focus on different products, such as silver for Tiffany and gold for Bulgari. LVMH historically proved its success in acquiring jewelry brands, as Bulgari has doubled its revenue since the acquisition. Just like Bulgari was successful with non-jewelry accessories, Tiffany could engage in the same strategy by, for example, selling scarves (Arnett, 2019; Spencer, 2019; Televisory, 2019; Tsang & Friedman, 2019).

LVMH and Tiffany can benefit from a range of possible synergies and create value from the acquisition. By not having to publish quarterly results and, thereby focusing on short-

term rather than long-term results, Tiffany can invest more time in its development under the umbrella of LVMH than it could do previously. This enables Tiffany to focus more on digital strategies, for example (Arnett, 2019; Spencer, 2019). Tiffany will also benefit from LVMH's back-office and from joining the French conglomerate's distribution network and supplier relationships. Since LVMH's relationship and partnerships are much stronger due to a larger number of Maisons, LVMH not only has the knowledge but also the manpower for growth, which leads to the next value creation, namely bargaining power in terms of, for example, marketing. While Tiffany mostly benefits from shared advertisements with other LVMH Maisons, negotiating with advertisement suppliers will also become more advantageous to LVMH as its bargaining power will increase. Together with LVMH's knowledge about where and how to advertise, both companies will increase their profits and Tiffany can, for instance, focus on regaining its market share among millennials. Tiffany would also have a better reputation among suppliers and distributors by operating under the French conglomerate's umbrella (Arnett, 2019; Olbertova, 2019; Piscioneri et al., 2021; Spencer, 2019; Televisory, 2019; Tsang & Friedman, 2019).

While the previously mentioned synergies mainly benefit Tiffany by entering LVMH's developed strategy, LVMH's main benefits from this acquisition are based on competition and increased market power. The jewelry market is one of the fastest-growing global markets, and further expansion into this market is essential for companies wanting to remain competitive in this dynamic environment. As jewelry was also less impacted by the 2020 pandemic, it therefore also presents an attractive investment (Olbertova, 2019; Piscioneri et al., 2021). Since there are only a handful of large players in the (luxury) jewelry market, the acquisition of Tiffany was probably one of the last opportunities for LVMH to expand into this market. Acquiring a U.S. company further strengthens LVMH's international standing, as possible political unrest could make globalized operations more difficult (Arnett, 2019; Olbertova, 2019). The acquisition of Tiffany not only increases LVMH's standing in the jewelry market but also improves LVMH's exposure to the U.S. market while expanding into improvable geographic markets will increase both firms' overall geographic exposure. For example, LVMH is expected to increase its U.S. sales, where luxury goods are highly in demand, from 24% to 26% through this acquisition, which would increase LVMH's overall presence in the U.S. Regarding Tiffany's geographic positioning, it is currently focused on

the U.S. with definite room for improvement in Europe (11% of sales) and Asia-Pacific (28% of sales), specifically in Mainland China. As Tiffany is expected to find itself facing great competition in Asia-Pacific, where Tiffany is only 2<sup>nd</sup> to Cartier in China, together with LVMH it could increase overall market share in these areas. On its part, LVMH not only expanded its customer base to the overall U.S. market, but also to the millennial generation, thereby having a younger, and larger, clientele than before. Regarding the industry, LVMH will further expand from the so-called “soft market” to the “hard market”, that is, from clothing or handbags to watches or jewelry. Entering the fastest growing industry would make LVMH’s watches and jewelry section the same size as that of competitor Richemont that holds brands such as Cartier and Van Cleef & Arpels, as the revenue of LVMH’s Watches & Jewelry products would increase to \$9.6bn. Expanding LVMH’s exposure to the watches & jewelry market might also benefit LVMH’s other Maisons operating in this industry (Arnett, 2019; Olbertova, 2019; Spencer, 2019; Televisory, 2019; Tsang & Friedman, 2019). It is expected that large competitors, like Richemont or Kering, will follow with other major acquisitions or changes in the watches & jewelry segment. Lastly, the LVMH-Tiffany-deal increased the gap between large holdings and independent brands and therefore, the overall effect on the industry and society remains unclear (Tsang & Friedman, 2019).

#### **3.2.4.3.2 L’Oréal and IT Cosmetics**

On July 22, 2016, L’Oréal announced that it would acquire IT cosmetics for \$1.2bn in cash. The skincare and makeup brand was only founded in 2018 (L’Oréal S.A., 2016). TSG Consumer Partners, a private equity firm that previously held IT Cosmetics, earned 25 times the amount they invested in the firm in 2013 (Berman, 2016). In 2015, IT Cosmetics increased its sales by 56% (Minaya, 2016), mainly due to consumer engagement. Founder Jamie Kern Lima always presented new makeup products by applying it on her problem skin, thereby boosting direct sales and consumer engagement (Collins, 2016). Lima remained CEO of the company until 2019 after which her three-year contract ended (Sorvino, 2019).

By acquiring IT Cosmetics, L’Oréal received access to roughly 300 beauty products (L’Oréal S.A., 2016), thereby reducing the cost of developing new products. Since IT Cosmetics actively innovates its products to, for example, find the optimal makeup coverage for problem skin (L’Oréal S.A., 2016), L’Oréal also acquired information about these innovations, which saved it from having to invest in R&D in this area. L’Oréal also learned new

capabilities from IT Cosmetics, as founder Lima engaged in a direct sales model by advertising her products on her skin (Collins, 2016). IT Cosmetics was sold in stores such as QVC, Sephora (owned by LVMH), and Ulta, whereas L'Oréal did not have a strong standing in QVC (Collins, 2016; L'Oréal S.A., 2016). Furthermore, L'Oréal was also experiencing a difficult time in Asia and Latin America (Caldwell, 2016) as the beauty industry was only growing by 3% a year (Sorvino, 2017). Nonetheless, L'Oréal's Luxe division has increased the most compared to other divisions (Minaya, 2016). This acquisition, therefore, helped L'Oréal to overcome entry barriers, be present in a larger variety of distribution facilities, and increase its growth in the U.S. market. It also captured a very young beauty company, as IT Cosmetics was only active for eight years in 2016, but had become very successful in a very short period. As IT Cosmetics joined L'Oréal alongside Urban Decay and other makeup brands, instead of diversification, L'Oréal is more focused on a complementing strategy in the beauty segment, especially in terms of makeup and hybrid skincare (Collins, 2016), which is aligned with its defined strategy of universalization.

L'Oréal uses its global network and infrastructure to improve IT Cosmetics' performance on the market (L'Oréal S.A., 2016). As L'Oréal has the manpower and knowledge about the makeup market, IT Cosmetics can benefit from this and improve its overall standing in the market. Not only did L'Oréal double IT Cosmetics' size since the acquisition, but it also pushed the makeup brand to become 2<sup>nd</sup> in the U.S. luxury makeup market (Sorvino, 2019).

As the beauty industry was only growing by 3% back in 2016, organic growth was not a successful strategy, especially for mature firms, and acquisitions had to be made to remain successful on the market (Sorvino, 2017). Indeed, as growth was declining back then, firms such as L'Oréal, Coty, and Estée Lauder participated in acquisition battles to obtain the fastest growing and most fashionable brands (Sorvino, 2017). This would, in turn, motivate incumbents to acquire as well. While IT Cosmetics was initially considering doing an Initial Public Offering (IPO), it then received multiple offers from potential buyers and was finally sold to L'Oréal for 6.6 times the revenue (Collins, 2016; Sorvino, 2017). Interestingly, IT Cosmetics' seller TSG already had a long relationship with L'Oréal in the past. Also, L'Oréal already engaged in acquisitions from rivals, as it bought Yves Saint Laurent Beauty from Kering in 2008 (Berman, 2016).

It seems that L'Oréal was mainly motivated by competitive structures as it was facing a company receiving several bids, and therefore needed to close the deal before anyone else did. L'Oréal managed to increase IT Cosmetics' size over the years, and therefore its acquisition motives must have been a mix between competitive pressure and possible synergies.

#### **3.2.4.4 Exceptional Case: Conglomerate**

Conglomerates represent a special form of strategy that a firm can adopt. While L'Oréal has a focused strategy on beauty and cosmetics, LVMH engages in a more diversified strategy, as can already be seen from its six different business groups. This section analyzes LVMH's conglomerate structure based on the information gathered in the literature review.

Conglomerates can either be pure or impure, with impure conglomerates being active in markets that cannot be entirely separated. While LVMH's products at first glance do not seem related – champagne is very different to a necklace and a hotel – LVMH's Maisons operate under one umbrella, namely luxury goods. Indeed, all LVMH's Maisons could be identified as indirect substitutes, as they are all somehow related. As craftsmanship and high-end products are a pillar of LVMH's success, their products supplement each other as their promises are very similar: under the highest standards of quality, excellent products and experiences can be purchased for a correspondingly high price.

Moreover, risk reduction plays a role in conglomerates as by having a range of unrelated businesses in one company, changes in the overall environment do not affect the conglomerate as much as it would affect other types of firms. The impact of the COVID-19 crisis provides a good basis to analyze this theory. While the personal luxury goods market experienced a 23% decrease in value from 2019 to 2020 (Fondazione Altagamma, 2021), LVMH's sales only dropped by 17%. Although value and sales are not the same measures they are presumed to give an indicator of the development of the industry resulting from the health crisis. However, L'Oréal only experienced a decrease in sales of 6% and comparing LVMH's Perfumes & Cosmetics business group with L'Oréal's Luxe yields decreases in revenue of 23% and 8%. The decrease in LVMH's sales, however, was very different between business groups. Whereas selective retailing experienced a 31% drop in sales, Fashion & Leather Goods only experienced a 5% sales decrease (see Figure 2).

Economies of scale and scope in terms of marketing were also mentioned as a motive for pursuing a conglomerate strategy. While LVMH's products are unrelated, its target group is

similar, namely high-end luxury-seeking consumers and therefore much of its marketing can be targeted to the same group while advertising different products.

Lower transaction costs, together with higher monitoring costs, were discussed in the literature. While LVMH provides its Maisons with back-office support, it leaves the autonomy, and the corresponding responsibility, to the Maisons. While monitoring costs are subsequently rather low, as the Maisons' performance is measured at the end of a given period instead of monitoring them daily, the overall effect of this approach remains unclear as, because the Maisons work independently and autonomously, the decrease in overall transaction costs is unclear. Regarding the shift from inefficient management to efficient management, LVMH replaced Tiffany's Chief Executive Officer, Executive Vice President, and Chairman of Tiffany Board of Directors with executives from Louis Vuitton and RIMOWA.

Ownership at LVMH is a complicated construct. The Arnault Family Group, (in-) directly, holds 47.48% of the share capital in LVMH, whereby 6.23% are directly held by the Arnault Family Group, and 41.25% by Christian Dior SE. However, the Arnault Family Group holds 97.50% of Christian Dior SE and thus, overall, the Arnault Family Group holds 47.48% of the shares with a corresponding 63.46% of voting rights (LVMH, 2021b, p. 321). Therefore, the mentioned conflicts between management and ownership do not seem to apply to LVMH. The ultimate long-term strategy pursued by the Arnault family is not clear.

Anticompetitive effects are also relevant for conglomerate mergers as they might prevent competition in the overall industry. This can happen in the value chain in which the first and last steps have already been acquired by the conglomerate, thereby increasing the pressure for the middle stage. As LVMH's operating model identifies one pillar as being vertical integration, this might be relevant to the conglomerate. Furthermore, LVMH owns several companies along the production process from vineyards and fur producers over production facilities and retail stores, thereby covering most parts of the value chain. Therefore, LVMH's strategy could indeed pressure the industry as a whole. For example, by owning a fur company, other players in the fur market are not able to compete with LVMH's acquisition, at least when it comes to the sales to LVMH. Together with the ability to cross-subsidize within the conglomerate, LVMH could indeed cause competition to shrink in several areas of its business. Nonetheless, LVMH cannot engage in competitive behavior with all its rivals, as each battle is fought in more than one industry or segment. This is indeed the case with

Kering and Richemont, with whom LVMH competes in different markets. In contrast, LVMH only directly competes with one L'Oréal business group and one of L'Oréal's divisions, which makes it more difficult for L'Oréal to fight back than for Kering. Nonetheless, LVMH acquiring Tiffany was seen as triggering a range of other acquisitions by main players in the luxury goods industry. Especially Kering and Richemont, both operating in the jewelry segment, could fight back soon. One could view Richemont's latest leather handbag acquisition Delvaux to be a reaction to LVMH's Tiffany acquisition (Richemont, 2021).

Another motive for conglomerates is the lack of overall competition because conglomerate strategies are very difficult to replicate entirely, in contrast to a strategy like L'Oréal's. The closest competition arises in terms of similarity, although, while there is an overlap between LVMH and its two main competitors, the extent of overlap seems to be manageable.

### **3.3 Financial Analysis**

#### **3.3.1 Financial Overview**

*LVMH.* The French conglomerate's revenue has been increasing over the past years, with an obvious decline in revenue in 2020, as from 2019 to 2020 revenues dropped from €53.670mm to €44,651mm. However, these are expected to recover in the coming years and even increase to € 66.128mm in 2022. The same trend applies to gross profits and operating income (Bloomberg L.P., n.d.-z). LVMH's total liabilities increased from €58.142mm to €69.842mm from 2019 to 2020, corresponding to a Debt/Assets ratio of 26.17% and 34.54%, respectively. Its total available line of credit exploded from 2018 to 2020, from €3.200mm in 2018 to € 21.100mm in 2019 and € 15.800mm in 2020 (Bloomberg L.P., n.d.-ab, n.d.-ad).

*L'Oréal.* In 2019, L'Oréal generated a revenue of € 29,873.6mm (Bloomberg L.P., n.d.-z), which has been increasing by a yearly average of 5.85% since 2014. Despite the decrease in revenue due to the health crisis, the French cosmetics firm is expected to recover its revenue very soon up to a value of € 33.173.1mm by 2022. Between 2011 and 2019, L'Oréal's cash ratio increased by a yearly average of 16.02% (Bloomberg L.P., n.d.-ab), which is an indicator of high liquidity. On the other hand, its Total Debt/Equity and Total Debt/Total Assets ratios also increased by a total of 50.68% and 54.12% from 2011 to 2019.

### **3.3.2 Merger Motives**

Based on the literature, there are several motives to engage in M&A activity. However, these are very theoretical and difficult to measure with the company data available to the public. One concern includes the reported debt of the acquirer as this number includes all business segments of a firm and does not differentiate between single entities. Therefore, optimal usage of debt cannot be verified with the data available. This becomes even more difficult when a private target is acquired, as data about debt is not made public beforehand. The following analysis is therefore largely based on estimations and projections from the data that is available to the public. As the literature on M&A activity indicated, takeover activity occurs in so-called “waves” when the economic environment is favorable. However, this is not a motive for M&A activity itself, but simply for when acquisitions take place. Additionally, whereas some acquisitions might look like simultaneous or sequential actions to rivals, they are most probably just reacting to favorable market conditions, which is why this will not be further analyzed here.

#### **3.3.2.1 Macroeconomic and Microeconomic Factors**

Several macroeconomic and microeconomic factors that increase acquisition rates have been identified. Whereas macroeconomic factors include technological change and an increased pool of corporate finance instruments, microeconomic factors include a decrease in costs or time saved through acquiring.

*LVMH.* Just like other companies in the 21st century, LVMH must also react to changes in the digital landscape as technology, especially e-commerce, is becoming more relevant. For example, acquiring Tiffany with its innovative brand and its developed e-commerce presence also accelerated technological growth for LVMH. Changes in market scope, resulting from the increased level of globalization, are mastered by LVMH through M&A deals as acquisitions cover not only a variety of products but also geographies. The French conglomerate acquired Fenty in the U.S., the winery Ao Yun in China, and Rimowa in Germany. Its suppliers are also spread worldwide. By having a subsidiary in almost all countries LVMH is active in, individual responses to changes in the competitive landscape can be ensured. Nowadays, firms have a broader spectrum of securities to use in corporate finance that move away from only banks granting loans. Of LVMH’s total outstanding debt, 65.26% are bonds and 34.74% are loans (Bloomberg L.P., n.d.-ag). This indicates that LVMH is making use of

the increased possibility to raise money. Only for the Tiffany acquisition, which was paid in cash, did LVMH raise more than €10bn in bonds in the year 2020 (LVMH, 2021b, p. 41).

Microeconomic factors have also been mentioned as a factor that increases the number of acquisitions. By increasing the size and volumes of production, a firm can reduce a range of costs. These include unit, R&D, administration, and distribution costs and is linked to a higher bargaining power towards suppliers. As mentioned in the strategic practical part, LVMH shares administration, R&D, and distribution activities among the group. Especially marketing and retail space bargaining power is increased with every acquisition as the French conglomerate not only knows the favorable spots and stores but also has the bargaining power to share space by, for example, advertising several Maisons under one banner. To determine whether LVMH incorporates these cost decreases, operating expenses, and selling, the general & admin expenses were compared between the second half of 2020 and the first half of 2021, as Tiffany was consolidated in January 2021. First, the sum of these two expenses in S2 2020 was compared to LVMH's expenses in S1 2021, having consolidated Tiffany. LVMH's expenses were higher than the sum of the two in S2 2020 (Table 6). However, this increase in expenses on LVMH's part may also mainly be due to the partial recovery from

	S2 2020			S1 2021
	LVMH	Tiffany	Σ	LVMH
Operating Expenses	10,585	971.7	11,556.7	11,993
Selling, General & Admin	10,734	972.6	11,706.6	11,903

Table 6: Comparison of LVMH's and Tiffany's Expenses between 2020 and 2021 in € mm (Bloomberg L.P., n.d.-aa, n.d.-ak)

the COVID-19 pandemic and therefore may not be as meaningful as expected. To have a better picture of whether LVMH was able to decrease expenses through acquisitions, the percentage increases in expenses were calculated for S1 to S2 2019 and S1 to S2 2020 (Table 7). These

historical increases were then applied to the expenses of S2 2020 and compared to the actual value of S1 2021. The differences in simulated and actual expenses yielded differences that are

	S1.19-S2.19	S1.20-S2.20
Operating Expenses	11.91%	9.60%
Selling, General & Admin	12.04%	10.67%

Table 7: Percentage Increase in LVMH's Expenses in 2019 and 2020 in € mm (Bloomberg L.P., n.d.-aa)

lower than the expenses for Tiffany in S2 2020 (Table 8). By disregarding LVMH's firm increases in the absent Tiffany's acquisition yield indicated that LVMH and Tiffany, together as one entity, reduced their expenses. These numbers indicate that LVMH can reduce several costs when acquiring new Maisons.

LVMH also makes use of takeover for increasing its overall scope in terms of geographies and products. Under the umbrella of luxury products, LVMH has acquired Maisons active in jewelry, handbags, retailers, and newspapers, which have been acquired all over the world and are thus offering their products worldwide (see Figure 3). As with acquisitions, one hereby gains access to every asset the target has, from supplier relationships to overall specific knowledge about the products offered, and a lot of time can thus be saved. This

	S2 2020	S1 2021 exp. with S1.19-S2.19 increase	S1 2021 exp. with S1.20-S2.20 increase	S1 2021 actual	Δ S1.19-S2.19	Δ S1.20-S2.20
Operating Expenses	10,585.00	11,845.43	11,600.98	11,993.00	147.57	392.02
Selling, General & Admin	10,734.00	12,026.58	11,879.45	11,903.00	-123.58	23.55

Table 8: LVMH Expense Simulation in € mm (Bloomberg L.P., n.d.-aa)

becomes relevant as every sector matures and acquisitions become a means to an end to compete with rivals on the market. Based on the analysis, there is evidence that LVMH is acquiring for these reasons. Technically, LVMH could increase its market share in Watches & Jewelry by itself but acquiring Bulgari and Tiffany also means acquiring supply chains and brand awareness, thereby saving years of development. The French conglomerate also aims to absorb direct competitors, with Hermès being the best example of the ruthless level of competition in the luxury industry. Starting in 2010, Chairman and CEO Arnault secretly acquired a large stake in Hermès through equity swaps that allowed for reporting the stake at a later date. Hermès and LVMH have been in legal disputes over this, as Mr. Arnault almost held one quarter of the Birkin bag creator by 2014. Arnault was overruled by the court and was not allowed to purchase any more Hermès shares for five years and promised to roll over most of his stake to LVMH shareholders (Jolly, 2014). LVMH’s acquisition strategy and worldwide expansion can also be seen in the risk profile of the company. LVMH has very mixed outlook ratings from Moody’s and Standard and Poor’s (S&P) (Bloomberg L.P., n.d.-s), which are stable and negative, and good current ratings with Moody’s A1 and S& P’s A+ and A-1. However, as S&P chose to give LVMH a negative outlook, LVMH’s future risk profile might change.

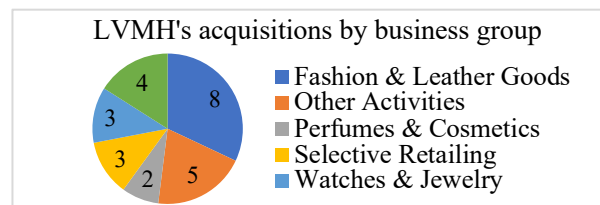


Figure 3: LVMH’s Acquisitions by Business Group (Bloomberg L.P., n.d.-ae)

Regarding cash, LVMH has been increasing its level of cash and cash equivalents from € 2.303,00mm in 2011 to € 5.673,00mm in 2019 and € 19.963,00mm in 2020 (Bloomberg L.P., n.d.-ad), whereas the big increase from 2019 to 2020 was mainly due to the cash raised for the Tiffany acquisition. One reason for this increase could be the acquisitions done by LVMH since then. However, this does not seem to be the main reason, as LVMH paid for the Tiffany acquisition in cash, thereby not indicating a need for cash but rather an excess of cash. To finance the Tiffany acquisition, LVMH issued eight bonds in 2020 totaling a value of €10.722mm. Of the eight bonds issues, seven have a time to maturity of fewer than 10 years, indicating confidence in the proper integration and profitability of acquiring Tiffany (see Table 9). The need to deleverage by making acquisitions does not seem to be a motivating factor for LVMH to engage in acquisitions. LVMH's debt has been increasing from €9.243,00mm in 2011 to € 37.531,00mm in 2020 (Bloomberg L.P., n.d.-y), corresponding to

Nominal Amount (bn)	Maturity	Time to Maturity as of 2020	12/31/2020 (€ mm)
GBP 850	2027	7	970
EUR 1,250	2024	4	1,251
EUR 1,250	2026	6	1,244
EUR 1,750	2028	8	1,734
EUR 1,500	2031	11	1,487
GBP 700	2023	3	788
EUR 1,500	2025	5	1,494
EUR 1,750	2022	2	1,754
		<b>Σ</b>	<b>10,722</b>

Table 9: LVMH's Issued Bonds for the Tiffany Acquisition (LVMH, 2021b)

a change in Total Debt/Total Assets from 15% to 35% (Bloomberg L.P., n.d.-ab). This increase in debt would rather indicate an increase in leverage through operations, as well as acquisitions. Since LVMH raised debt to finance the Tiffany acquisition, deleveraging does not seem to be a contributing factor for LVMH, and, in fact, the opposite is rather true. Regular capital gains, however, could be a reason why LVMH engages in acquisitions.

Whereas the actual number of capital gains depends on when the investor purchased the asset, it corresponds to an increase in a firm's capital assets. LVMH's share price has greatly increased since 2010, with an all-time high of €510.90 by 12/31/2020 (Bloomberg L.P., n.d.-af). Overall, the need for capital gains could be a contributing factor, as LVMH and its acquired Maisons realized high capital gains over the years. Furthermore, while LVMH is further diversifying its conglomerate and not focusing on one particular segment, it does divest when it no longer sees a fit. For example, in 2005, LVMH sold Christian Lacroix to an American luxury duty-free retail group, in 2016 LVMH sold Donna Karan International for \$650mm, and it is currently speculated that Marc

Jacobs could also be sold in the near future. Especially Christian Lacroix and Donna Karan experienced significant losses and required investments that were too high for the French conglomerate (LVMH, 2005; Williams, 2016).

*L'Oréal.* Just like LVMH, L'Oréal also must react to challenges such as digitalization. To tackle this challenge, L'Oréal has introduced the Corporate Digital Department to support digital strategies. For example, in 2018 L'Oréal acquired ModiFace (Mandell, 2018), an augmented reality and artificial intelligence brand. ModiFace was acquired for its technology that is being used for a variety of different beauty products. L'Oréal must also compete in the international market to maintain its competitive positioning; therefore, its acquisitions do not only expand the French beauty firm's product portfolio, but also its geographic footprint. Acquisitions for geographic reasons were made in Africa, Latin America, and Asia Pacific. L'Oréal is also making use of non-bank approaches for financing its activities. While L'Oréal still uses bank loans for medium-term financing, it issues both marketable instruments and commercial papers in France and the U.S. to finance its operations in the short-term (L'Oréal S.A., 2021a, p. 290). L'Oréal also makes use of lease debt, which is a big item in debt distribution. While Europe on average accounted for 32% of all sales between 2012 and 2019, its revenue only grew by 2% yearly, on average. On the other hand, on average, Asia Pacific grew its annual revenue by 13% between 2012 and 2019 (Bloomberg L.P., n.d.-h).

Several other microeconomic factors influence L'Oréal's decision to engage in acquisitions and R&D, administration, and distribution costs are of great importance here. A higher bargaining power towards suppliers is also a motivation to engage in acquisitions. Distribution, for example, is provided by L'Oréal through its Operations department for all its brands as this includes not only distribution but also packaging (L'Oréal S.A., 2021a, p. 14). The R&D department is also shared by different brands, which is why costs can be saved there. As suppliers are instructed to deliver raw materials to L'Oréal plants, and not to its brands' plants, one can infer that L'Oréal is mainly responsible for supplier relationships. Therefore, the French beauty company is likely to benefit from increased bargaining power with suppliers and thereby reduce costs. L'Oréal makes use of acquisitions to expand not only geographically, but also product-wise. Out of the 18 acquisitions in the past years, seven have been made for geographical reasons and the remainder were made to expand the overall product

portfolio (Figure 4). Acquisitions also accelerate L’Oréal’s speed in terms of growth. While L’Oréal would also have the means to build new brands itself, acquisitions save much time and, subsequently, money. ModiFace again is a good example of this, as L’Oréal acquired a company that has been successfully working on specific technologies for many years. In a mature industry, acquisitions are found to be one of the only ways to increase or maintain market share, although acquisitions become a scarce good at that point. To maintain, and increase its market share, L’Oréal is engaging in a range of acquisitions.

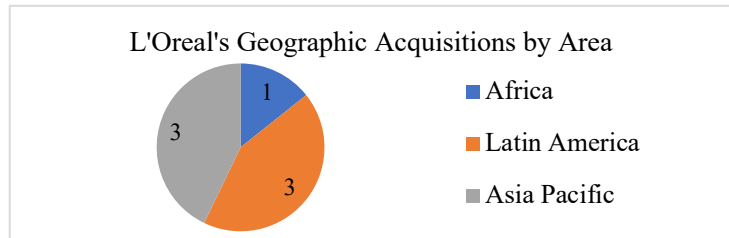


Figure 4: L’Oréal’s Geographic Acquisitions by Area (L’Oréal S.A., 2021a)

Estée Lauder acquired much less than L’Oréal, and Unilever is acquiring in all its different segments, with the beauty segment not being the focus of acquisitions. As these two firms are right behind L’Oréal in terms of sales, these global players must all find a way to maintain their standing. However, L’Oréal is engaging in the largest number of acquisitions in the beauty market of these Top Three, thereby increasing its market share. Additionally, L’Oréal is acquiring companies that do not fully complement its portfolio, but rather present a change due to different consumer demands. This can be seen by the number of acquisitions made in the Active Cosmetics division, which currently experiences a high demand (Figure 5). Acquisitions are also motivated by the decrease in risk that comes from diversifying its cash flows. L’Oréal’s ratings show its low risk of default, as Moody’s defines L’Oréal’s outlook as stable, and Standard & Poor (S&P) classifies the French beauty firm as A-1+ (Bloomberg L.P., n.d.-e). These numbers indicate a low risk. The need for cash, to deleverage, or to generate required capital gains were indicated as being motivating factors for acquisitions by the literature. L’Oréal’s cash and cash equivalents have been increasing constantly from €987.6mm in 2016 to € 2.666,0mm in 2020. While the simple increase in cash does not disclose whether this is due to acquisitions, which, in turn, would present a motivation for making acquisitions, L’Oréal’s payment types do. Almost 60% of

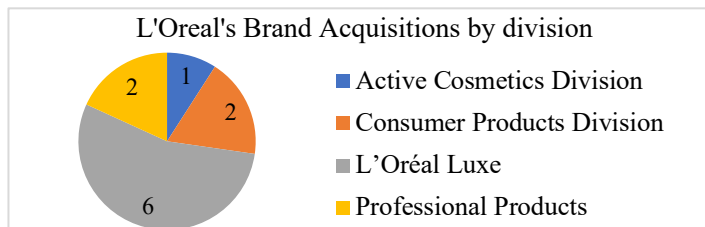


Figure 5: L’Oréal’s Brand Acquisitions by Division (L’Oréal S.A., 2021a)

cash equivalents have been increasing constantly from €987.6mm in 2016 to € 2.666,0mm in 2020. While the simple increase in cash does not disclose whether this is due to acquisitions, which, in turn, would present a motivation for making acquisitions, L’Oréal’s payment types do. Almost 60% of

cash equivalents have been increasing constantly from €987.6mm in 2016 to € 2.666,0mm in 2020. While the simple increase in cash does not disclose whether this is due to acquisitions, which, in turn, would present a motivation for making acquisitions, L’Oréal’s payment types do. Almost 60% of

acquisitions were paid in cash, which is why the need for cash does not seem to be a contributing factor for the company to engage in acquisitions (See Table 10) (Bloomberg L.P., n.d.-l). Regarding the need to deleverage, L'Oréal has maintained a low level of Total Debt/Total Assets between 2011 and 2020, with a value of around 6% in 2020 (Bloomberg L.P., n.d.-j). Whereas this low number could be due to acquisitions before 2011, L'Oréal has maintained a level below 10% over this period while engaging in many

Comparison of Payment Types	# of Deals	
	LVMH	L'Oréal
Cash	64	31
Stock	5	1
Cash, Stock & Debt	1	
Cash or Stock	1	
Cash & Debt	1	
Undisclosed	111	52

Table 10: Comparison of Acquisition Payment Types of LVMH and L'Oréal (Bloomberg L.P., n.d.-l, n.d.-ae)

acquisitions. Comparing this ratio to that of L'Oréal's main competitors, Unilever and Estée Lauder, reveals that L'Oréal has an extraordinarily low ratio of Debt/Assets (See Figure 6). Overall, the need to deleverage does not seem to be a motivating factor for L'Oréal to engage in acquisitions. Capital gains, on the other hand, might be a relevant factor for L'Oréal. Its

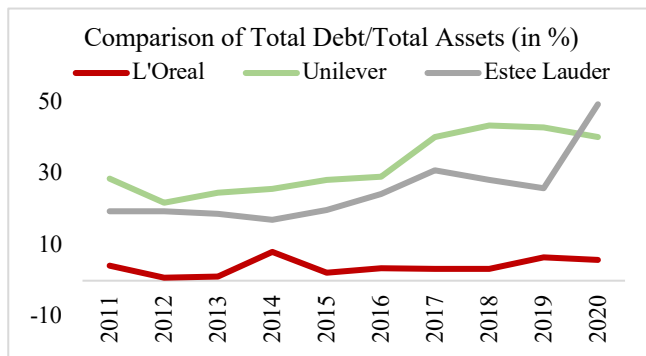


Figure 6: Comparison of Total Debt/Total Asset Ratios in Percent between L'Oréal, Unilever, and Estée Lauder (Bloomberg L.P., n.d.-b, n.d.-i, n.d.-an)

L'Oréal sold its Johnson Product Brands to Wella in 2000 (L'Oréal S.A., 2000). Furthermore, The Body Shop that was acquired by L'Oréal in 2006, was sold to Natura in 2017 (Butler, 2017). As The Body Shop's sales fell by 5% in 2016, and operating profit fell by 38%, the ethical brand could not be held by L'Oréal anymore as its profitability was not given. In 2020, L'Oréal sold Roger & Gallet to Impala (L'Oréal S.A., 2021a, p. 40).

### 3.3.2.2 Increase in Prices & Decrease in Costs

An increase in prices and decreases in costs is an overall motivation to engage in M&A activity. An increase in prices could be measured relative to a price index (U.S. Bureau, n.d.), in which a basket of goods at one point in time is compared to a basket at another point in time. However, this is out of the scope of this work since it incorporates many additional

share price has also greatly increased since 2009, with a record price of €310.80 on 21/31/2020 (see Appendix J). Whereas refocusing on one business is not relevant for L'Oréal, as the French beauty company already focuses on cosmetics, divestments also happen in the company. For example,

difficulties such as slightly adjusted products and the available data is not sufficient for such an analysis. Therefore, the focus here lies on the decrease in costs.

*LVMH.* While LVMH might acquire a jeweler such as Tiffany in the present, it could also increase its price for Belmond's hotel price per night. Therefore, the effect of price increases is out of scope. However, LVMH has a broad range of opportunities for increasing prices, not only because it can raise prices within different Maisons, but because it can also modify products to an extent that increases in prices are undetectable and accepted.

Decreasing costs, however, is naturally highly favored by LVMH. As the administration, distribution, production, and R&D costs decrease with more acquisitions through the synergies realized, supplier power will also decrease. As mentioned previously, the increase in bargaining power ranges from diamond suppliers to retail spots and advertisement banners, which can all be very effectively used by LVMH's back-office organization. Additionally, production and R&D facilities are shared among the Maisons, thereby further saving costs. Costs are mainly being saved through economies of scale, vertically integrating, and organizing products. These factors were touched upon previously, where LVMH was found to integrate vertically by, amongst others, acquiring vineyards and wineries, as well as fur producers. Furthermore, the acquisition of Tiffany increased the vertical integration as, before the acquisition, Tiffany already had much of the vertical integration in-house. To quantify

the reduction of costs, a comparison was made between the increase in revenue and the increase in costs over the years. This is important because an absolute increase in, for example, marketing costs does not necessarily reflect the mismanagement of costs. Instead, with rising revenues and more products being sold, one needs to invest more in

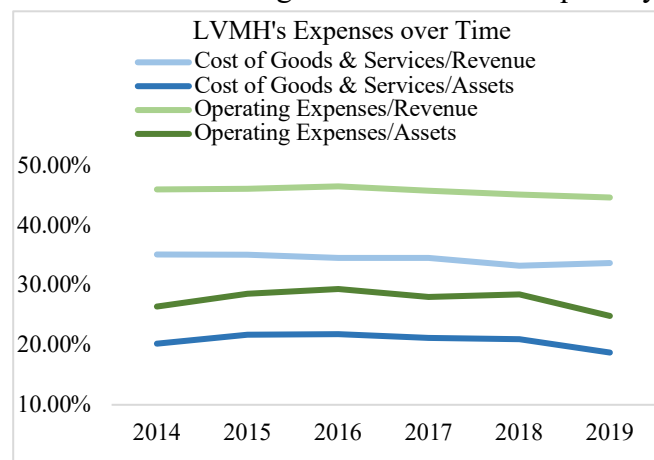


Figure 7: LVMH's Expenses over Time (Bloomberg L.P., n.d.-z)

marketing operations. Other costs follow the same argumentation. Cost of goods & services and operating expenses were plotted against revenue and assets to show how LVMH's profitability evolved over time (Figure 7). The year 2020 has been left out in this graph. Both types of costs slightly decreased as related to assets over time, whereas the cost of goods &

services and operating expenses as of revenue were quite stable. While stable ratios as of revenue do not indicate a decrease in costs, the evolution of these costs without acquisitions is not presented here. Properly integrated acquisitions that lower this ratio could be equaled out by increases in costs in other Maisons or business groups not affected by acquisitions. Therefore, no definite statement can be made at this point. Nonetheless, LVMH managed to keep the ratios shown stable – or even decrease them – indicating some increases in profitability.

*L'Oréal*. Increases in L'Oréal's prices are as difficult to measure as those of LVMH and are thus also out of scope for this thesis. Decreasing costs are the main motivation to engage in acquisitions. Not only could L'Oréal save R&D and administration costs, but it could also decrease production and distribution costs. If expected synergies are realized, L'Oréal and its brands would benefit from cost decreases. Since L'Oréal is responsible for R&D, Digital, and operations for the whole group, it has the necessary know-how to ensure that a real benefit is derived from possible expected synergies. A new company entering the Group will benefit from this support while being able to fully focus on its core business. For example, packaging and distribution are performed by L'Oréal, whereby economies of scale can be realized and bargaining power in distribution can be increased with an increasing number of brands. To find how L'Oréal's costs evolved over time, costs of goods & services and operating expenses were plotted as of revenue and assets (Figure 8). As was the case with LVMH,

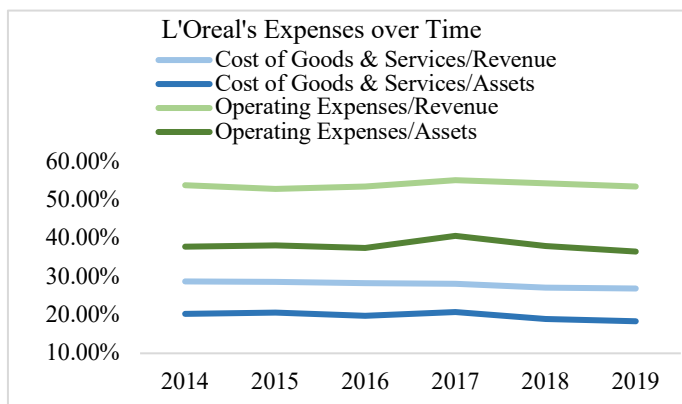


Figure 8: L'Oréal's Expenses from 2014-2019 (Bloomberg L.P., n.d.-g)

the year 2020 was not considered so as not to skew the results based on this exceptional year that was largely shaped by the COVID-19 pandemic. As one can clearly see, L'Oréal managed to keep all ratios quite stable over the years. Again,

while these ratios do not indicate the values without acquisitions over time, and are quite stable, decreased costs through acquisitions might be equaled out by increases in other business areas. Therefore, no definite statement about cost decreases as of revenue and assets can be made here. Overall, L'Oréal

managed to keep the presented ratios stable or slightly decreased them, indicating some cost savings and increases in profitability. Interestingly, these ratios are higher than LVMH's ratios shown before, indicating a slightly lower profitability regarding costs of goods & services and operating expenses than LVMH.

Drawing a conclusion from only these numbers, L'Oréal does not seem to decrease costs through acquisitions as much as expected. There is one caveat, however: perhaps the increase in costs would be even higher without acquisitions, whereas L'Oréal's acquisition would still indicate decreases in cost. Overall, no definite statement can be made at this point, although it appears that L'Oréal's acquisition strategy is not as cost-saving as expected.

### **3.3.2.3 Purely Financial Motives**

Regarding other financial motives for M&A, the literature suggests that increased leverage could be a motivating factor for acquisitions, as two combined entities can have higher leverage than the firms on a stand-alone basis. Since LVMH does not report its levels of debt by business group, quantifying this number is very difficult. Additionally, to separate the effect of regular increases in debt from increases due to acquisitions only, presents another significant challenge. To avoid bankruptcy costs, targets can be acquired by a buyer that can improve the performance again and compensate for the possible costs of distress. However, LVMH acquires firms that are successful and in good financial health (Arnett, 2019). Also, to decrease LVMH's probability of default, it can either sell off poorly performing Maisons or acquire additional firms that lower this probability. However, the latter does not seem to be the case as, instead of buying new firms, existing Maisons that are not living up to the conglomerate's expectations are being sold (see the example of Christian Lacroix and Donna Karan International). Therefore, LVMH does not seem to acquire firms in distress, but rather to acquire Maisons that were already successful beforehand. The French conglomerate also does not seem to take over new Maisons to decrease its probability of default, but rather to sell off poorly performing Maisons if an improvement under the LVMH umbrella is no longer possible. To strengthen this argument, LVMH's one-year default probability was analyzed (Bloomberg L.P., n.d.-r). The default probability remained at low levels after the financial crisis. Since 2010, LVMH never showed a one-year default probability of more than 0.3%, with a current value of 0.0005%. Except for the increase in default probability to 0.15% in 2016, due to the decrease in luxury consumption, the one-year default probability level

remained low. The five-year credit default swap behaved similarly. Comparing these values with the “France – Consumer Discretionary: Apparel & Textile Products” group shows that LVMH, Kering, and Hermès lie within the lowest default probability bracket of 0% to 0.002%. Eight out of 15 peers lie within the good default probability group of between 0% and 0.52%, six are within the “high yield” values of 0.52% to 10% default probability, and one lies within the distressed area. LVMH thus does not seem to need to acquire for the reasons of avoiding bankruptcy costs. If, at all, it acquires Maisons to further diversify its portfolio and decrease its already low probability of default.

Tax efficiencies, on the other hand, could be a contributing factor to LVMH resulting from acquisitions as the list of consolidated companies includes subsidiaries around the world and taxes are paid in the country of operation. Having subsidiaries around the world also ensures closeness to the market they are operating in. Whereas the French statutory tax rate for the years 2018, 2019, and 2020 amounted to 34.4%, 34.4%, and 32%, LVMH’s effective tax rate was equal to 26.3%, 27.4%, and 32.7%, respectively. When calculating the effective tax rate, differences in tax rates for foreign companies are subtracted. The values that were subtracted in 2018, 2019, and 2020 were 8.8%, 8.7%, and 6.0% (LVMH, 2021a, pp. 255-256). While this is an indicator that foreign subsidiaries decrease LVMH’s effective tax rate, it does not prove that this is a motivation for acquisitions. Furthermore, even Louis Vuitton has many subsidiaries around the world, which does not correspond to an acquisition but rather to the opening of a foreign subsidiary. Overall, there does not seem to be valid proof regarding this hypothesis, but surely LVMH is trying to save taxes through foreign subsidiaries. Inefficient target management also seems to be somewhat relevant for LVMH acquiring Tiffany, as it was undergoing major changes in recent years including the fact that, in 2017, an activist investor drove its CEO to leave. Perhaps this was one of the reasons for Tiffany’s difficult times as revenue growth was fluctuating between -3.41% and 6.53% between 2015 and 2020 (Bloomberg L.P., n.d.-al).

*L’Oréal.* L’Oréal does not disclose information regarding the level of debt on a brand level and therefore no statement can be made about increased leverage being a contributing factor for acquisitions. The avoidance of bankruptcy costs on both the target and buyer sides were also analyzed for L’Oréal and revealed similar results to those of LVMH. As L’Oréal

sells off brands that are not successful, for example, Johnson Product Brands, The Body Shop, and Roger & Gallet, L'Oréal tends to sell poorly performing brands that are increasing L'Oréal's probability of default rather than buying new brands to actively decrease this probability. While L'Oréal would have the necessary funds to compensate for one poorly performing brand, it does not wait until possible bankruptcy costs evolve and sells the brand before it reaches this stage, thereby protecting itself as a group from higher default probabilities. Indeed, the French beauty firm acquires other firms that are in good shape, such as IT cosmetics. When seeking proof for this argument, one sees that L'Oréal's one-year default probability has remained at extraordinarily low levels since the financial crisis, with the default probability remaining between 0% and 0.002% since then (Bloomberg L.P., n.d.-p). L'Oréal was affected less than LVMH during the difficult times in the luxury markets and also shows lower default probability values than LVMH or its competitors (see Appendix K). This result does not indicate the need to further lower its default probability, as L'Oréal has managed to keep this value low for a long time now.

Tax efficiencies mostly result from having subsidiaries in tax-friendly countries, yet it is stated that each subsidiary reports and pays taxes in the location in which it operates. L'Oréal claims that tax-friendly countries are only chosen for operations (L'Oréal S.A., 2021a, p. 229), yet the French company saves money by having at least some operations in these countries. Although L'Oréal most probably performs tax optimization, it seems unlikely that this is a driving factor M&A, as many of the consolidated companies are located in non-tax-friendly countries. Whereas L'Oréal seems to boost many of its brands after their acquisition, inefficient target management does not seem to be a primary motivation to acquire brands as the brands acquired were already successful, either by having a special product, an innovation, or a valuable geographic footprint. While L'Oréal could perhaps do better, the management of a successful company cannot necessarily be described as being inefficient. Other topics in this context, such as increases in market share or reducing costs by operating business units together, were already discussed before and will not be covered again here.

#### **3.3.2.4 Financial Synergies: Cost of Capital**

Financial synergies were found to mainly occur due to decreased CoC when firms engage in M&A. Since the Weighted Average Cost of Capital, or WACC, is composed of the cost

of equity and debt, together with the share of debt and equity, these numbers are of relevance when quantifying the hypothesis.

*LVMH.* From 2011 to 2020, the French conglomerate's WACC was fluctuating between 6.81% and 12.31% with an average of 9.34% and no overall trend being detectable (Bloomberg L.P., n.d.-ai). The fluctuations were mainly driven by changes in the cost of equity, as the cost of debt was decreasing overall from 3.37% in 2001 to 0.08% in 2019, and even had a negative value of -0.17 in 2020. Another reason for LVMH's decrease in the cost of debt could be indicated by the hypothesis that larger firms have better access to debt capital markets than smaller firms. Since 2011, compared to its peers, LVMH had a decreasing cost of debt value, which decreased somewhat faster than that of its competitors. Additionally, it also experienced fewer fluctuating increases than its peers, which could be an indicator that the large conglomerate LVMH has better access to debt and, in turn, lower cost of debt, due to its overall strategy. Comparing LVMH's WACC to that of its main competitors Richemont and Kering reveals that their WACC and cost of equity move together (Bloomberg L.P., n.d.-a, n.d.-d). As the literature indicated, higher levels of diversification would decrease a firm's CoC as the coinsurance effect would step in and reduce the probability of bankruptcy. While LVMH's diversifying acquisition strategy would seem to promise a lower CoC, this does not seem to be the case in practice. Instead, the WACC and cost of equity of all three peers largely move together. Since the cost of equity is mainly responsible for the changes in WACC, it also needs to be analyzed. The cost of equity consists of both the operating risk of the firm and the risk of debt, that is, the capital structure risk. Furthermore, equity holders are residual claimants after debt holders, which means that the more leverage a firm has, the higher the risk of bankruptcy, and the higher is the cost of equity (Vernimmen et al., 2017). As LVMH's weight of debt decreased over the years, the level of leverage did not influence the changes in the cost of equity. The cost of debt would also decrease if LVMH is more diversified, as the cash flows would coinsure each other and reduce the probability of bankruptcy. The fluctuations in the cost of equity could therefore either be affected by changes in the industry's systematic risk, or by changes in operating risks. Systematic risk is the risk that cannot be diversified away by an individual firm but rather is the risk that every firm in the same industry faces. Assuming that not all three competitors analyzed have high operating risks, one can indicate that changes in WACC are mainly due to the systematic risk of

the industry. Analyzing some acquisitions and the resulting changes in the CoC, such as Bulgari in 2011 and Tiffany being announced in 2019 and completed in the beginning of 2021, one sees that LVMH's CoC decreased right after these acquisitions. Nonetheless, two years after acquiring Bulgari, LVMH's WACC increased again.

As LVMH's WACC did not decrease as the literature proposed it would, perhaps LVMH is not as diversified as was believed (See Figure 9). One way to find whether a firm is diversified or not is to look at the company's  $\beta$ . The  $\beta$  measures how the firm, or portfolio, moves with the overall market and incorporates the market volatility. For example, a  $\beta$  between zero and one indicates that the firm is fluctuating less than the overall market, while a  $\beta$  over one means the opposite. The closer a firm's  $\beta$  is to one, that is, the closer it moves with the market, the more diversified the firm is because the market only incorporates systematic risk, whereas individual firms also incorporate unsystematic risk. Unsystematic risk can be diversified away, which means that diversified firms should have a  $\beta$  close to one, that is, the market. Having a look at LVMH's Raw historical  $\beta$  shows that it moves between 0.7 and 1.5. The  $\beta$  was measured against the French stock market index CAC 40. Since the  $\beta$  of equity was usually found to be between 0.5 and 1.5 (Vernimmen et al., 2017), LVMH lies right in this range. As LVMH's  $\beta$  has been fluctuating, no definite statement about its diversification can be made. However, in 2020 after announcing the Tiffany acquisition, LVMH had a  $\beta$  of 0.968, indicating a high level of diversification.

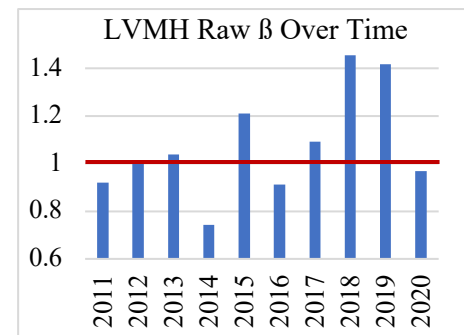


Figure 9: LVMH's Raw  $\beta$  from 2011-2020 (Bloomberg L.P., n.d.-aj)

As mentioned in the literature, the WACC becomes relevant when evaluating profitability measures, such as the EVA. As many other factors influence the EVA, LVMH's EVA is not only influenced by the WACC (Bloomberg L.P., n.d.-ai). Despite this, one can see that with high values of WACC, the corresponding EVA values are either low or even negative. On the other hand, in 2017, when EVA was at a high of 3,253.02, LVMH's WACC amounted to 8.22%. Looking at the Net Operating Profit After Tax (NOPAT) and Capital Charge that is used to calculate EVA reveals that increases in EVA are mainly due to increases in NOPAT and not to decreases in invested capital. The capital charge, on the other hand, is affected by both the WACC and the total invested capital. Over the years, one sees that while the WACC

As mentioned in the literature, the WACC becomes relevant when evaluating profitability measures, such as the EVA. As many other factors influence the EVA, LVMH's EVA is not only influenced by the WACC (Bloomberg L.P., n.d.-ai). Despite this, one can see that with high values of WACC, the corresponding EVA values are either low or even negative. On the other hand, in 2017, when EVA was at a high of 3,253.02, LVMH's WACC amounted to 8.22%. Looking at the Net Operating Profit After Tax (NOPAT) and Capital Charge that is used to calculate EVA reveals that increases in EVA are mainly due to increases in NOPAT and not to decreases in invested capital. The capital charge, on the other hand, is affected by both the WACC and the total invested capital. Over the years, one sees that while the WACC

fluctuates, the total invested capital constantly increases. Therefore, increases in the capital charge are not mainly due to increases in WACC, but rather decreases in capital charge are due to decreases in WACC.

Overall, given the data of LVMH and its peers, one can conclude that the French conglomerate does not seem to have an advantage in terms of its WACC compared to its main competitors. What the data does not show, however, is what the companies' WACC would look like without the acquisitions made since 2011. A definite statement regarding the effects of LVMH's diversifying acquisition strategy, however, cannot be made. Furthermore, it is not clear whether LVMH is truly a conglomerate in the financial sense. Perhaps LVMH is not viewed as a completely diversified company, as all its Maisons are in the luxury segment, and while the conglomerate's Maisons are diversified in terms of their products, they are still subject to similar movements in the economic landscape. The main driver for increases in EVA seems to be the NOPAT, that is, the good economic performance of LVMH. The WACC does, however, play an important role in lowering the capital charge and, subsequently, in increasing the EVA.

*L'Oréal.* L'Oréal's WACC from 2011 to 2020 varied between a low of 6.43% and a high of 11.51% (Bloomberg L.P., n.d.-o). Increases in WACC were mainly due to increases in the cost of equity, as the cost of debt was constantly decreasing, even reaching negative values. Since the financial crisis in 2008, equity weights have been increasing, and have been higher than 96% since 2010. Therefore, decreases in WACC are not caused by increases in debt, but rather by decreases in the equity cost. Comparing this to competitors Unilever and Estée Lauder shows that L'Oréal is right in the middle of the three (Bloomberg L.P., n.d.-c, n.d.-ao). L'Oréal's costs of debt, on the other hand, are much lower than that of its peers since 2014. This could be an indicator of L'Oréal having better access to debt, either due to its size or lower default rates. Together with L'Oréal generating the highest revenue in the cosmetics market, the low cost of debt shows the good state the French beauty company is in.

As all three peers engage in acquisitions, it seems reasonable to expect a similar WACC. However, Unilever is diversifying its portfolio more than L'Oréal and Estée Lauder do (Unilever, n.d.), as it runs divisions such as Home Care, Beauty & Personal Care, and Foods & Refreshment. According to the theory, this approach should yield a lower WACC. As

Unilever's WACC is not lower than the other ones', Unilever is either not making use of the diversification effect or L'Oréal and Estée Lauder make up for being more focused and thereby decrease their default probabilities. Another reason could, again, be due to the systematic risks all three firms are facing as, despite their good performance, the WACC cannot be lowered further because of the systematic risk.

L'Oréal's EVA has also been influenced by its WACC, as high values in WACC correspond to rather low values in EVA. Since 2012, the main driver of EVA does not seem to be WACC anymore, as the WACC was constantly below 10% since then (Bloomberg L.P., n.d.-o). Increases in EVA are mainly affected by increases in the NOPAT, which means that the economic profitability was due to better operations instead of lower CoC. Increases in the capital charge are influenced by the WACC and by the total invested capital that has been increasing over time.

Overall, L'Oréal's WACC, cost of equity, and cost of debt show good values. As the overall company effect cannot be separated from the acquisition effect, a definite statement regarding the effect of acquisitions on the overall WACC cannot be made. Nonetheless, L'Oréal shows the lowest cost of debt among its peers, indicating better access to debt markets overall. This could either be due to size in general, low debt weights, or benefitting company characteristics. The EVA is mostly influenced by the NOPAT, but a high WACC decreases the EVA.

### **3.3.2.5 Timing**

Timing was also found to be an important factor when making acquisitions as not only the target but also the acquirer can be over- or undervalued. If the target is overvalued, bidders will overpay and, if the buyer is overvalued and pays in shares, it can use this overvaluation to its benefit. However, in the case of an industry valuation, these effects cancel each other out and advantages can thus only be used when acquiring outside the industry.

*LVMH.* LVMH, by engaging in a range of acquisitions, might be subject to overpaying for targets in terms of acquisition premia. Looking at the premium paid in M&A activity, one sees that 32.66% of the deals included an acquisition premium of less than 10%, and 44.96% had current premia of less than 10% (Bloomberg L.P., n.d.-ae). Furthermore, 10% of all deals had an acquisition premium between 10% and 20%. While many of LVMH's forms of payment are undisclosed (64.50%), most of the disclosed payment types were in cash. While

paying in shares signals an overvaluation of the acquirer, cash does not send this signal and reduces the risk of the payment for the target. However, acquisition premia also represent the potential synergies of the transaction, which is why a higher premium does not necessarily mean that the acquirer is overpaying, as high premia are only an indication of potential overpayment and include the transfer of most expected synergies to the target.

Whereas several analysts regard LVMH as being overvalued (Claire Domergue, 2021; GuruFocus, 2021; Market Screener, 2021), Mr. Arnault sees LVMH to currently be undervalued (Zubair, 2021). Either Mr. Arnault is overconfident about the French conglomerate's future, or he has as yet undisclosed information about his firm that enables him to make such statements. However, if he really was that confident about LVMH's future, he could have partly paid in shares for the Tiffany acquisition instead of raising debt. Other indicators of overvaluation include high multiples such as Price/Earnings, high Price/Book, and high Enterprise Value/EBITDA ratios, as they indicate a price higher than the firm's quantifiable numbers. However, when analyzing the peer group, LVMH is in the middle regarding these multiples, and therefore a definite statement cannot be made regarding LVMH's overvaluation compared to its peers (Bloomberg L.P., n.d.-w). As multiples are just a relative valuation, an overvaluation of the whole sector remains unclear.

*L'Oréal.* As not many of L'Oréal's acquisition prices paid are disclosed (Bloomberg L.P., n.d.-l), the possible overpayment for targets is difficult to evaluate. However, most of the current premia paid were below 10%, and most of the premia paid were between 10% and 20%, with some premia paid being between 70% and 80%. This indicates that, in most cases, L'Oréal does not seem to overpay. However, there are some cases where L'Oréal overpaid by up to 80%, indicating an overvaluation of both the target and most of the expected synergies attributed to the target, being incorporated into the acquisition price. Of the disclosed acquisitions, most were made in cash.

Having a look at multiples reveals that, among the peer group "Europe Household Products Manufacturing Valuation Peers," (Bloomberg L.P., n.d.-q). This could be an indicator of the overvaluation of L'Oréal. However, these multiples also provide information about the over- or undervaluation of the entire industry. If L'Oréal was indeed overvalued, according to theory, the French cosmetics company would use its shares as a currency for acquisitions.

Nevertheless, L'Oréal mostly used cash to acquire new brands, which does not support the overvaluation theory. Indeed, some sources say that L'Oréal is overvalued and that the company will experience decreases in its share price in the future (Schönberger, 2020; Trefis Team, 2020). These statements were made in 2020, and the actual share price did experience decreases in December 2020 and again in July 2021 (Figure 10).

Overall, there are signs of L'Oréal being overvalued according to several multiples and different sources. While L'Oréal mostly paid for acquisitions in cash, it remains unclear whether its upcoming acquisitions will be paid in cash or stocks. It must be noted, however, that L'Oréal mostly acquires private companies, therefore only stock-for-cash deals could be possible in the first place.

### 3.3.3 Wealth Effects of Mergers and Acquisition Activity

#### 3.3.3.1 Short-Term Wealth Effects

*LVMH.* Regarding short-term wealth effects, small event windows are created around the announcement date to determine the effect of the acquisition announcement. To evaluate LVMH's reactions in share prices and returns, the acquisition of Tiffany was analyzed. To compute the returns, logarithmic returns were computed based on daily closing prices. The event window around the announcement date was set twenty days around the announcement

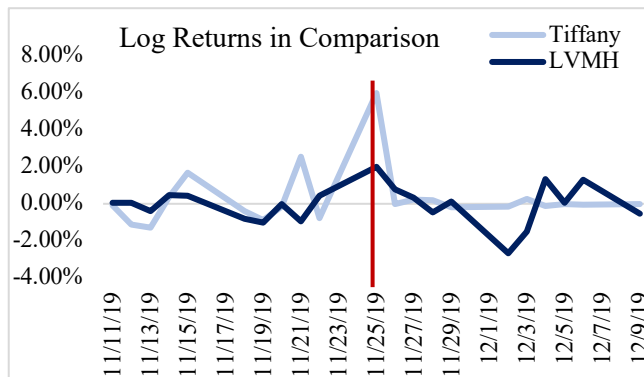


Figure 11: Logarithmic Returns of LVMH and Tiffany around the announcement date (Bloomberg L.P., n.d.-af, n.d.-am)

date of November 25, 2019. Figure 11 shows the logarithmic returns during the estimated event window. It can be observed that both LVMH and Tiffany benefitted from increases in logarithmic returns on the announcement days. However, Tiffany's logarithmic return on the announcement day amounted to

5.98%, whereas LVMH's return only amounted to 2.00%. Furthermore, the returns over the time window and the returns on the ten days after the announcement date were analyzed. LVMH's logarithmic return over the complete time window amounted to -0.93%, and -1.24% over the ten days after the announcement date. Tiffany's responding logarithmic return over the complete time window was 5.94%, and 6.20% over the ten days after the announcement, which was significantly higher than LVMH's. These negative market reactions towards

LVMH after the acquisition announcement could indicate two things. Firstly, the market might have thought that most of the synergies will be attributed to Tiffany, which is why LVMH will not capture much of the expected synergies. Secondly, the market might have considered that LVMH is overpaying for Tiffany, and will suffer from that overpayment in the future, which is why the share price decreases around the announcement. As expected, synergies might have been no surprise to the market, as LVMH has already shown through the successful integration of Bulgari in the past, and the decrease in returns was thus probably mostly due to the market thinking that LVMH overpaid for Tiffany.

The measurements of M&A performance found by (Das & Kapil, 2012) yielded positive results. Accounting measures include asset growth, profit, return on equity, return on investments, and sales growth, which all positively influence M&A performance (Bloomberg L.P., n.d.-z, n.d.-ac, n.d.-ad; LVMH, 2021b).

The overall results were aligned with the literature, as the target of an acquisition experiences positive returns around the announcement date, whereas the buyer experiences nil or negative returns. This implies that the market assigns more synergies to the target than it does to the acquirer. Following the media coverage that has previously been analyzed, this result is not surprising as Tiffany was expected to benefit most from the transaction. The increase in returns right before the announcement date was probably due to the anticipation of the deal outcome as well as possible insider trading. While the acquisition was only completed in 2021, the replacement of Tiffany's executive level was also in line with the literature that states that the target manager suffers more from the acquisition than the buyer management. However, evaluations of M&A performance show a positive outlook for LVMH over the years, which could also be attributed to Tiffany joining the conglomerate.

*L'Oréal.* To measure the short-term gains or losses from acquisitions, the purchase of IT Cosmetics was analyzed. An event window of twenty days was created around the announcement date of July 22, 2016. Again, logarithmic returns based on daily closing prices were calculated to measure the effect of the announcement. Since L'Oréal was taking over a private company, share prices and returns are only available for L'Oréal. Indeed, L'Oréal's share price increased from €173.35 on July 21, 2016, to €176.2 on July 27, 2016, just around the announcement of the acquisition. L'Oréal yielded a logarithmic return of 0.69% on the

announcement day, compared to the day before. However, the logarithmic return over the entire event window was negative and amounted to -0.23%, and the logarithmic return in the ten days after the announcement was at -1.49% (Figure 12). This was mainly due to a decrease in share price from €176.2 on July 27, 2016, to €169.35 on August 3, 2016.

The literature suggests that acquisitions of private firms should yield higher returns than the purchase of a public firm. To quantify this number, the acquisition of The Body Shop was also analyzed, which was announced on March 17, 2006, and finalized on July 12, 2006.

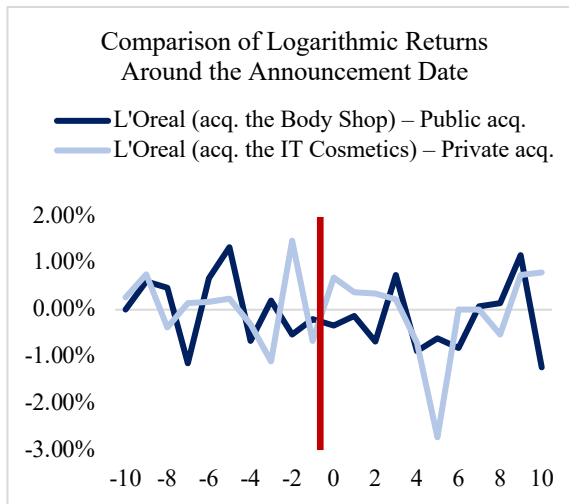


Figure 12: Comparison of logarithmic returns of L'Oréal for both The Body Shop and IT Cosmetics around the announcement date (Bloomberg L.P., n.d.-m)

L'Oréal experienced a negative logarithmic return of -0.34% on the day of the announcement. Over the entire event window, it realized a logarithmic return of -1.82%, and in the ten days after the announcement, a logarithmic return of -2.22% (Figure 12). The Body Shop, on the other hand, yielded a logarithmic return of 9.94% on the announcement day, which corresponds to a logarithmic return over the entire event window of 12.74%, and of 0.17% after the announcement date. Comparing the logarithmic returns of L'Oréal when acquiring The Body Shop and IT Cosmetics reveals that with IT Cosmetics, L'Oréal yielded a better return over the entire event window and after the announcement, although it was still negative. L'Oréal's logarithmic returns over the entire event window amounted to -1.82% when acquiring The Body Shop, and to -0.23% with IT Cosmetics. The logarithmic returns after the announcement were -2.22% with The Body Shop and -1.49% with IT Cosmetics. While both acquisitions yielded negative returns, L'Oréal yielded better logarithmic returns when it acquired IT Cosmetics. This is in line with the theory that states that bidders yield better returns when acquiring private targets. There is one caveat, however, in that the market could simply have viewed IT Cosmetics as being a better target than The Body Shop, regardless of the company being private.

The measurements of M&A performance identified by (Das & Kapil, 2012) were also analyzed. Asset (growth), revenue (growth), gross profit (growth), GAAP net income

(growth), return on common equity, return on assets, return on capital, and return on invested capital were analyzed. All measures yielded positive results except for the GAAP net income growth that decreased by a yearly average of -3.66% and a total decrease of -23.63% from 2014 to 2019 (Bloomberg L.P., n.d.-g, n.d.-j, n.d.-k).

Overall, the negative logarithmic returns of L'Oréal on and around the announcement day of both acquisitions are fully aligned with the literature, as the bidder is often found to be experiencing negative returns in acquisitions. Despite this, most of the M&A performance measures yielded positive results, and the acquisition of IT Cosmetics was found to be successful, thus L'Oréal can be viewed as a successful acquirer and integrator.

### **3.3.3.2 Long-Term Wealth Effects**

As indicated by the literature, the long-term wealth effects of a takeover are practically impossible to quantify, as, after several years, the effect of the acquisition cannot be disentangled from the overall development of the company. This is due to the fact that firms not only engage in different acquisitions over time but also grow organically and increase their return through good management. What the literature does state is that internal competition to receive funding, for example, is value-destroying.

*LVMH.* While LVMH introduced its Internal Competition Law Compliance Charter in 2012, internal competition remains as all Maisons operate independently from each other and must take responsibility for their performance. On average, Intra-Group financial debt's share of overall gross borrowings amounted to 28.51% between 2011 and 2019 (LVMH, 2021b). This could be an indicator of internal competition between the Maisons caused by the acquisitions of LVMH. Another aspect that was highlighted in the literature was that in cases where the firm's industry is overvalued, acquisitions in other industries generate long-term value. While all LVMH's Maisons are in the luxury industry, they operate in different segments. Therefore, acquisitions in hotels, yacht builders, newspapers, or retail stores, indicate that LVMH is valuing its option along several segments to provide long-term growth and profitability. Calculating LVMH's long-term total algorithmic returns yielded a return of 127.83% (01/02/2017–12/31/2019) and 849.58% (01/02/2009–12/31/2019) (Bloomberg L.P., n.d.-af, n.d.-ah). While these returns look very good and are promising, some factors need to be considered when observing these numbers, because single acquisitions cannot be separated from the overall development of the company. Overall, although LVMH's long-

term performance as a whole looks good, the challenge of separating the acquisition effect from other effects remains.

*L'Oréal.* L'Oréal. As L'Oréal does not disclose information such as intra-group borrowings, the internal competition hypothesis cannot be fully verified. However, as all of L'Oréal's brands operate independently, chances are high that there is internal competition. This is especially likely since L'Oréal's brands all operate on the cosmetics market, and sometimes even in the same segment. L'Oréal's total long-term algorithmic returns yielded 34.61% (01/02/15–12/29/17) and 305.90% (01/02/09–12/31/19). While the analysis yields positive results, in this case the long-run single acquisition effects also cannot be separated from other effects.

### **3.3.3.3 Conglomerate Discount**

Conglomerate discounts occur when the conglomerate, as a whole, is valued less than the sum of its parts, that is, its subsidiaries. As L'Oréal follows a focus strategy, only LVMH can be considered for a conglomerate discount. However, conglomerate discounts must not necessarily occur if the management of a company is exceptionally good. LVMH's conglomerate discount has been estimated to be between 5% and 10% (Gauvillé, Ireland, Spillecke, & Tillson, 2016; Ryan, 2019). Calculating the conglomerate discount, however, presents difficulties as this requires the values of all subsidiaries. Since LVMH does not disclose information about its Maisons separately, calculating the intrinsic value of each Maison is nearly impossible. The intrinsic values of each Maison could thus only be calculated at the time of acquisition, but this value has probably changed under LVMH and over time in general, and therefore these numbers would not provide relevant information.

## **4 Discussion**

The literature review, together with the practical part, yielded interesting results about both LVMH and L'Oréal. As the literature review summarized why M&A activity occurs, the practical part aimed to quantify these findings. While many findings coincided with the proposals made in the literature, others did not. The discussion will be divided into a strategic and financial discussion, as the overall thesis was divided into these two topics.

## **4.1 Strategic Discussion**

### **4.1.1 Competition**

Many findings in the strategic review were rather apparent as they are the basic fundament of competing in M&A activity. Both LVMH and L'Oréal are aware of their competition in the overall market, they are motivated to engage in this competition and to increase their market share, and they can successfully do so. For example, LVMH has an undrawn available credit line of €15.8bn to provide the necessary flexibility needed, while L'Oréal, on the other hand, even makes its performance measures and bonuses for, amongst others, Agon, dependent on the performance in comparison to that of its rivals.

While L'Oréal's competitors are rather easy to identify, as L'Oréal's market is limited to cosmetics, defining LVMH's competition is more challenging than it would seem at first glance. While Kering and Richemont are competitors in the sense that they are all luxury conglomerates, LVMH engages in a range of competition. LVMH's competitors in the champagne market are different from those in the luxury handbags segment, or to their rivals in the yacht building market. Therefore, LVMH must cope with an even larger number of competitors than L'Oréal, although Kering and Richemont remain its closest rivals in terms of size, overlap, and importance. LVMH only reports market shares by business group, which makes sense as the markets LVMH operates in are very different. Nonetheless, Maisons such as Hennessy or Sephora are market leaders in their respective segments. L'Oréal, on the other hand, is a leader in worldwide sales in the cosmetics market and clearly defining its most important competitors, which suggests that the French cosmetics company is the overall cosmetics market leader worldwide.

To have a stronger competitive standing, not only towards customers but also towards suppliers and retailers, LVMH is emphasizing vertical integration more than L'Oréal does. For example, acquiring Tiffany expanded LVMH's vertical integration in the diamond supply chain as this is done in-house at Tiffany's. Additionally, LVMH is not only producing but also harvesting its vineyards. Lastly, it is acquiring along the whole value chain, including a fur producer, a production facility, and retailer Sephora. Vertical integration can be beneficial in two ways: by saving overall transaction costs and by increasing the overall market power. Regarding LVMH, cost savings are a large part of this strategy as, for example, acquiring Bulgari and Tiffany will reduce several costs. The latter part, the increased market

power, seems to be the more relevant aspect for LVMH as the luxury conglomerate is not only acquiring Maisons, such as Tiffany but also acquires vertically, for example, a fur producer. By doing so, LVMH is surely increasing its market power along the whole vertical value chain and, in turn, increases its power among suppliers and other stakeholders in the production process, as LVMH now does not rely on outside fur suppliers, but has this delivery in-house, and is thus changing the fur competition and the brand competition where these materials are being used.

Overall, both L'Oréal and LVMH are performing well in their own way regarding overall competition and market share. As L'Oréal's market is narrower than the one LVMH operates in, L'Oréal has fewer rivals to compete with, and its overall market share might thus look bigger than that of LVMH. However, LVMH is engaging in more than one market at the same time and, therefore, its market share cannot be directly compared to that of L'Oréal. Even if one would simply compare LVMH's Perfumes & Cosmetics business group with L'Oréal, the comparison would be flawed as this business group is only one of six distinct business groups LVMH is running. Therefore, a direct comparison of LVMH and L'Oréal is not easily made in terms of competition and market share.

#### **4.1.2 Acquisition Strategies**

Discussing the overall strategy of LVMH and L'Oréal yields very interesting results. Although one might think that LVMH's diversified portfolio would follow a differentiation strategy instead of a focus strategy, in reality, the results look different as, indeed, LVMH follows both. On the one hand, it follows a differentiation strategy by creating a luxury image around all its available products, while on the other hand, it mostly focuses on one buyer group that has sufficient funds to buy its products. One might also assume that L'Oréal is strictly following a focused strategy as it only operates in the cosmetics market. However, L'Oréal's affordable Consumer Products division is offering high-quality products at low prices, following a cost leadership strategy. L'Oréal's overall strategy, however, does focus on beauty cosmetics products, simultaneously addressing different buyer groups and creating different brand images around its consolidated brands. While LVMH's stuck-in-the-middle situation is regarded by experts as a vicious cycle that requires immediate action to further succeed (Porter, 2008), LVMH has shown that by following two strategies at the same time, one can succeed in practice, contrary to the opinions from the literature.

Whereas L'Oréal and LVMH do not have a high market commonality with each other, LVMH and its other competitors compete in different markets at the same time. Actions in one market, such as LVMH acquiring jeweler Tiffany, can be responded to in another market, such as Richemont acquiring leather goods producer Delvaux. This makes LVMH's overall competitive strategy more challenging. As LVMH chooses to diversify its business and operate in several markets at the same time, it requires much more awareness and flexibility than L'Oréal does, given L'Oréal's limited competitors and business groups. Although this makes competition more difficult, it also provides LVMH with more ways to fight its competitors than L'Oréal has at its disposal. Considering the resource similarity of LVMH, L'Oréal, and their competitors, LVMH and L'Oréal do not have many touchpoints with each other, but they do with other competitors. However, by competing in the Watches & Jewelry and Wines & Spirits markets, LVMH must face higher and more challenging resource similarities as raw materials such as diamonds and champagne vineyards are scarcer than the raw materials used for manufacturing makeup.

LVMH and L'Oréal were further analyzed regarding their relatedness and level of diversification. Not surprisingly, L'Oréal has a high relatedness within its divisions by sharing packaging, Research & Innovation facilities, and manufacturing, etc., and a low level of diversification. Surprisingly, LVMH was shown to have a rather high level of relatedness compared to what one might anticipate. Furthermore, while one would suspect no – or a very low – level of relatedness in a conglomerate such as LVMH, the analysis showed the opposite, as especially within the Watches & Jewelry and Perfumes & Cosmetics business groups, a high level of relatedness was discovered. While the level of relatedness is not high across the group as a whole, it is rather high within individual business groups. Contrary to the literature (Hitt et al., 2016), LVMH manages to have both a level of relatedness between business units and diversification overall. However, there is one important caveat regarding LVMH's diversification that becomes relevant across the whole analysis. While LVMH, on the surface, seems to be a perfectly diversified luxury conglomerate operating in independent markets, having analyzed LVMH and its businesses reveals some doubt in this regard, as even though LVMH's products and markets seem different, they all operate under the umbrella of luxury products and therefore a complete distinction between the French conglomerate's markets cannot easily be made. While the production of its products varies significantly, the products

themselves might not be as different as they may seem at first glance as they all are luxury products that make a statement when they are purchased and which promise a certain feeling attached to the act of purchasing them. Therefore, the view of LVMH being a completely diversified company cannot be confirmed without also considering important the caveats mentioned before.

#### **4.1.3 Growth**

While both LVMH and L'Oréal are known for their acquisitions, they also focus on organic growth to boost their overall profitability. For example, 10% out of 15% of LVMH's 2019 revenue growth was due to organic growth. The finding of emphasizing organic growth on top of simply acquiring additional firms goes hand in hand with the literature stating that a firm should not only acquire but also build, that is, grow organically (Gell et al., 2017). Together with strategic alliances and joint ventures that both companies are engaging in, they also seem to focus on non-M&A-related growth. This makes sense, as both LVMH and L'Oréal have the knowledge and resources to integrate their brands and make them successful. While I expected to find that L'Oréal would better integrate its brands due to its focus and depth of knowledge regarding the cosmetics industry, it was shown that both LVMH and L'Oréal integrate very well, and also divest from time to time.

LVMH only engages in selected joint ventures or strategic alliances, such as a wine estate or a retail company that owns licenses in airport duty-free shops. L'Oréal, on the other hand, entered its last big joint venture with Nestlé when they introduced Venture Laboratoires INNEOV and Galderma. However, the relationship with Nestlé is difficult as explained previously (Bürgi, 2018). Of the two firms, only L'Oréal is actively engaging in licensing agreements to both boost research in the skincare segment, and production and distribution agreements with luxury brands such as Prada, Armani, and Valentino.

Acquisitions at LVMH and L'Oréal are made in somewhat similar ways. Both companies acquire for product expansion and geographic reasons to complement their overall portfolio. While L'Oréal only acquires brands in the cosmetics market, LVMH engages in takeovers of luxury firms overall. LVMH's acquisitions range from hotels to handbag producers to vineyards, whereas one of L'Oréal's acquisitions that was *furthest* away from cosmetics was ModiFace in 2018. Since 2012, most of LVMH's acquisitions were made in the Fashion & Leather Goods and Wines & Spirits business segments, whereas the former business group

contributes to most of the group's overall sales and grew at the highest average rate of 13%. In contrast, the Wines & Spirits business segment only contributed to 13% of sales on average, with an average yearly growth rate of only 6%, which is the lowest revenue growth rate among the business groups. Among L'Oréal's acquisitions complementing its product portfolio since 2012, most were made in the L'Oréal Luxe division, which accounted for six out of eleven acquisitions. While the L'Oréal Luxe division only ranks at number two in proportionate average sales (30%), its revenue grew at the highest rate of all divisions (11%). Geographic acquisitions were made in areas with both the highest revenue growth (Asia Pacific with 13%) and lowest revenue growth (Latin America with 1%). Both LVMH and L'Oréal acquire in both the areas/segments that already have high revenue proportions and growth rates and in low-performing areas and segments that require a boost in economic profitability. Therefore, the two companies aim to support the weak segments and further develop and grow the *strong* segments.

Regarding the two firms' acquisition motives, interesting findings were made by using one key example for each. U.S. jeweler Tiffany mainly complements LVMH's portfolio in a geographic and vertical integration way, whereas acquiring IT Cosmetics was mainly motivated by improving L'Oréal's standing in stores, such as QVS, further strengthening L'Oréal's makeup and hybrid skincare segment in addition to acquiring for competitive first-come-first-serve reasons. Both acquisitions are perfect examples of the companies' takeover strategies and some acquisition motives are very similar. These include barriers to entry, reducing costs to develop a new product, avoiding R&D costs, information acquisition, learning new capabilities, back-office synergies, etc. Both LVMH and L'Oréal acquire for competitive reasons. While LVMH's acquisition of Tiffany was one of the last opportunities to acquire a relevant and established jewelry firm, IT Cosmetics received a range of other bids for the company and considered going public itself. Both Tiffany and IT Cosmetics are appropriate targets to reshape the competition in favor of the two French companies. However, other reasons for acquisition differ between the two companies. For example, while L'Oréal acquired IT Cosmetics to further enhance its universalization strategy and complement brands, such as Urban Decay, Tiffany is supposed to further diversify the Watches & Jewelry segment. Although Tiffany and Bulgari are similar acquisitions, and some integration strategies can be repeated, they do focus on different products and different customer groups.

Both LVMH and L'Oréal mostly let their integrated brands operate independently with different support systems from the group. Tiffany will most likely share production facilities with LVMH's other jewelry Maisons, in addition to the shared advertisement space that is being used by the group. L'Oréal, on the other hand, focuses more on R&D, digital, and operations support from the group to its brands.

While not immediately attributed to acquisition motives, LVMH has a complicated organizational structure. LVMH has sub-holdings that are, in turn, holding LVMH's Maisons. While this has a range of financial reasons, primarily it reduces the risk of the parent company and distances its Maisons from the parent company to an extent that they are viewed more as being an individual brand instead of just LVMH's daughter company. Furthermore, the whole ownership structure regarding Christian Dior SE is more complicated at LVMH. L'Oréal, on the other hand, still has strings attached, with Nestlé holding a large stake in L'Oréal and providing two directors on the management board, including a vice-president. This could indicate a lower degree of freedom at L'Oréal than for LVMH, as the Arnault family group holds 47.5% of the shares, with a corresponding 63.4% of voting rights.

#### **4.1.4 Strategic Conglomerate**

A variety of literature has focused on conglomerates as a special form of strategic decision. Managerial self-interest, as proposed by the literature, does not apply at LVMH as the Arnault family group is a major shareholder and has most voting rights, with Bernard Arnault being the CEO and Chairman. Many of the findings in the literature have been confirmed by the analysis performed. For example, internal capital funds within conglomerates (Cox, 2006), are actively being used by LVMH. Another example is the anticompetitive effects that conglomerates evoke (Mueller, 1978). Acquiring Tiffany did increase the gap of a few large firms holding most jewelry brands and independent brands, thereby showing an increase in industry concentration. Lastly, the findings in this thesis also support the literature that conglomerates are operating in rather close industries to realize some synergies (Hoberg & Phillips, 2011). LVMH's business groups all operate under the luxury umbrella, having many similarities in terms of advertising, distribution, or target group.

Contrary findings were made regarding the risk reduction through diversification, which is one of the main reasons to engage in conglomerates (Tremblay & Tremblay, 2012). The COVID-19 pandemic provided a good opportunity to evaluate whether LVMH's

conglomerate strategy decreases overall risk. Interestingly, while LVMH's sales decreased by 17% in 2020, L'Oréal's sales only decreased by 6%. To compare the luxury market, L'Oréal Luxe's division was further compared to LVMH's Perfumes & Cosmetics business group. While the former only experienced a decrease in sales of 8%, the latter had to deal with a collapse of 23% in sales. Interestingly, the opposite would have been expected due to LVMH being a conglomerate with supposedly decreased risk. However, the overall sales decrease shows that LVMH experienced almost triple the sales drop that L'Oréal did. This could also be due to luxury goods consumption being cut first when a crisis hits the economy as such goods might rather be seen as "unnecessary."

## **4.2 Finance Discussion**

### **4.2.1 Mergers and Acquisition Motives**

In addition to the strategic motives to engage in M&A activity, the reasons from a financial point of view were also discussed. As was the case in the strategic part, some findings correspond with the literature, and others do not.

The literature identified several macro- and microeconomic factors that increase the number of acquisitions (Vernimmen et al., 2017). The macroeconomic factors all seem to play a role in LVMH and L'Oréal's acquisition strategies, as both firms must react to the technological change and internationalization of the overall market. While Tiffany is improving LVMH's standing through its successful e-commerce, L'Oréal acquired ModiFace, an artificial intelligence brand working for cosmetics companies. Having different approaches by either taking over a company that is already successful in the technological business, or a company solely focusing on technological aspects, both aim toward achieving the same goal, which is responding to major changes in the 21<sup>st</sup> century. Both firms are also making use of non-bank financing. Whereas of LVMH's total debt outstanding, 65.26% are bonds, L'Oréal only uses bank loans for medium-term financing and uses short-term marketable instruments and commercial papers to finance itself in the short term. L'Oréal, compared to Unilever and Estée Lauder, has shown extraordinarily low total debt to total assets ratios over the years.

Both firms engage in acquisitions that expand their portfolio on a product basis and geographically. Time is also an important factor for deciding on acquisitions, as both LVMH and L'Oréal take over firms that are already established in the market. This also goes along with the overall strategy of the two firms, which plays a big role in their financial

performance and evaluation. However, there are differences in the competitive behavior of the two firms. Whereas L'Oréal places a high emphasis on competition and performance in comparison to its rivals, it seems to act less ruthlessly than LVMH does. One piece of evidence for this is the behavior of Mr. Arnault, who secretly acquired a large stake in competitor Hermès and tried to acquire the company through the back door. While L'Oréal engages in more acquisitions than some of its competitors, it has not initiated such an aggressive and hidden takeover approach. Furthermore, the literature suggested a decrease in risk due to acquisitions. As risk is described by measures like ratings, these were analyzed in this thesis. While L'Oréal received the ratings stable and A-1+, LVMH currently has a negative outlook by S&P. Unlike the prediction that LVMH would have a more stable and secure cash flow due to its diversification strategy and, in turn, a better rating, this is not the case in practice, which could also indicate that LVMH is currently overvalued. With its focused strategy, L'Oréal has a better and more stable outlook, which goes hand in hand with the results obtained from analyzing both firms' one-year default probability, as L'Oréal default probabilities of 0% were lower than those of LVMH. This is related to the extraordinarily low debt to assets ratios but does not translate into a higher decrease in WACC, as one would expect.

Divestments are another important factor that comes with investments. Both L'Oréal and LVMH have sold some of their unprofitable brands, such as L'Oréal selling The Body Shop or LVMH selling Christian Lacroix or Donna Karan International. While both engage in divestments, LVMH seems to be harsher in this regard, as it divests more than L'Oréal does. Nonetheless, in a conglomerate with 75 Maisons, those that are not delivering as they should need to be sold off to secure long-term overall profitability and growth.

Interesting findings were made when analyzing the costs for both firms. While acquisitions should decrease costs such as cost of goods & services or overall operating expenses, this was not found to be the case for LVMH and L'Oréal. However, the challenge in this analysis was that there are no numbers that show what these ratios would look like without acquisitions. Therefore, acquisitions lowering these ratios might be equaled out by increases in costs in other brands or divisions in the two companies. It must be noted, however, that L'Oréal's operating expenses as of revenue and assets over time were higher than the corresponding ratios of LVMH, whereas LVMH's cost of goods & services as of revenue was higher than L'Oréal's. This shows that LVMH seems to keep the operating expenses at a

more profitable level than L'Oréal, indicating a better integration of Maisons and leveraging of synergies. Indeed, comparing the second half of 2020 for LVMH (without Tiffany) with the first half of 2021, when Tiffany was consolidated, the results indicated lower operating costs for the conglomerate.

Many of the purely financial motives cannot be quantified as the necessary data is not available. There were some indications that both LVMH and L'Oréal use tax-friendly countries for some of their subsidiaries. However, as stated in both their registration documents, subsidiaries operate and pay taxes in the countries they operate in, which is why this does not seem to be a major financial motive. Inefficient target management was one of the reasons for LVMH acquiring Tiffany, which has been going through a challenging time in terms of personnel changes. However, this does not seem to be the main factor for both firms. Since both acquire targets that are successful in their own right, their management cannot be completely inefficient, otherwise, they would have not been successful in the first place. If at all, LVMH and L'Oréal manage their acquisitions more efficiently. One must note that the IT Cosmetics founder, Lima, remained CEO for three years after the acquisition, indicating that inefficient target management was not a contributing factor for L'Oréal to acquire the U.S. makeup brand. The cash levels were also analyzed. Especially LVMH's bonds, which were issued to finance the all-cash acquisition of Tiffany, give an important signal: as the maturity of most of the bonds were below ten years, this shows that LVMH trusts in the success of Tiffany's acquisition and integration.

The most important financial reason to engage in M&As is the reduction of the CoC, or WACC (Gaughan, 2007), where the WACC was expected to be reduced mostly for LVMH, according to the hypotheses in the literature that state that diversification would lower the CoC because the coinsuring factor of a conglomerate should lower the overall risk of cash flows. Since the WACC is driven by both the cost of equity and the cost of debt, both numbers were analyzed. LVMH and L'Oréal's cost of debt has been decreasing since 2001, indicating that acquisitions enable better access to the debt market by both being more diversified through holding more separate business units, and simply by being a larger firm. However, the fluctuations of cost of equity also resulted in movements of the WACC, instead of the WACC decreasing due to acquisitions. This result is very interesting in two ways. According to the literature, the WACC should decrease over time through acquisitions. Also, as LVMH

is a conglomerate, it should have a lower WACC than L'Oréal and its other rivals. As decreases in WACC increase profitability measures, such as the EVA, the EVA was also analyzed. For both firms, increases in the EVA were not mainly due to decreases in WACC but rather due to an increase in NOPAT. Nonetheless, the EVA is measuring profit considering the WACC, or the CoC, and therefore increases and decreases in EVA are influenced by the WACC. Overall, both LVMH and L'Oréal showed no advantages over their competitors in terms of their WACC, but they rather move together in this regard. This lets me conclude that the fluctuations in WACC were mainly due to the systematic risk of the overall industry.

Other interesting findings were made regarding timing, which has been identified as being a major factor when engaging in acquisitions (Gaughan, 2007; Lewellen, 1971; Myers & Majluf, 1984; Nelson, 1959). Both LVMH and L'Oréal do not seem to overpay for their targets, as their acquisition premia paid are very low, and for LVMH over half were below 10%. While L'Oréal does not usually overpay, and then only in some cases with an 80% premium, LVMH seems to hold its acquisition premium even lower, which could indicate better bargaining power or more accurate valuations from LVMH. As the French conglomerate has more experience in different segments than L'Oréal does, this could be a contributing factor when (over-)paying for targets. While the above observations were made in terms of the targets being overvalued, the buyers can also be overvalued and use this to their advantage. When comparing multiples for LVMH and L'Oréal, interesting results were obtained. Whereas LVMH finds its relevant multiples to be right in the middle of its peers, L'Oréal is leading the list of peers with every important multiple. This is an indicator of overvaluation compared to the peer group. However, both L'Oréal and LVMH are not paying their acquisitions in shares, as the literature would suggest when indicating and making use of buyer overvaluation. Many of the firms acquired were also private targets. However, there is always one important caveat when using multiples, namely while multiples provide information about the valuation of a firm compared to its peers, they do not generate information on whether the industry is over- or undervalued. Therefore, LVMH being in the middle regarding its multiples must be viewed with caution. However, in several press papers, there have been more voices raised regarding LVMH being overvalued. Overall, LVMH and L'Oréal do not seem to overpay for their acquisitions, yet both show signs of overvaluation

themselves. While most of the previous acquisitions were made in cash, it will remain of high interest whether future takeovers will still be made in cash.

In summarizing the financial M&A motives, these were shown to yield moderate to no advantages to engage in acquisitions. While some of the financial effects were simply not as strong for LVMH and L'Oréal as predicted based on the literature, others were found to be the opposite. Therefore, for both LVMH and L'Oréal, acquisitions seem to be made more for strategic than for simple financial reasons.

#### **4.2.2 Wealth Effects of Mergers and Acquisitions Activity**

The wealth effects of M&A activity were measured in both the short-term and the long-term. In the short term, the literature suggested that the target's returns would increase, and the buyer's return would either be very small, nil, or negative (Martynova & Renneboog, 2005; Welch, 2011). LVMH and Tiffany were analyzed, in addition to L'Oréal and IT Cosmetics, and L'Oréal and The Body shop. The Body Shop was included to provide an example of a private and public target, as L'Oréal is acquiring a majority of privately held brands. The findings in this thesis perfectly correspond with the literature in this regard. LVMH's logarithmic return on the announcement day was 2.00%, while Tiffany's was 5.98%. L'Oréal's logarithmic return on the announcement day of the acquisition of IT Cosmetics amounted to 0.69%, and on the day it announced acquiring The Body Shop it was -0.34%. The Body Shop, on the other hand, yielded a logarithmic return of 9.94% on the announcement day. These findings support several findings from the literature. Firstly, the target's returns are higher than the buyer's, secondly, the buyer's return is either very small or negative, and lastly, the buyer's return is higher when acquiring a private target.

Some measurements of M&A performance that have been proposed by the literature were analyzed, including the age of the firm, the value of the deal, or the occurrence of M&As, being negatively related to the performance of the acquisition (Das & Kapil, 2012). As all these measures were true for both LVMH and L'Oréal, and the short-term returns did not look advantageous for the two French firms, these might be reasons for the low or negative returns on the announcement day. However, one could counter at this point that age comes with acquisition experience which, in turn, comes with increased value creation. As mentioned previously, some of the successful Bulgari integration strategies could be used on Tiffany. The same is true for Urban Decay and IT Cosmetics.

There are caveats, however, regarding the findings mentioned above. Firstly, returns illustrate relative changes in the share price and, consequently, Market Capitalization. This means that the same absolute increase in share prices has different effects depending on the overall market capitalization, which is usually higher for the acquirer than for the target. As LVMH's market capitalization at the end of 2019 amounted to €208.612,80mm, and Tiffany's to \$16.243,2mm, the returns found have to be analyzed carefully. As the numbers for market capitalization for L'Oréal do not go back to 2006, this cannot be completely verified. Since L'Oréal only paid £652mm for The Body Shop in 2006 (Butler, 2017), this indicates that L'Oréal was indeed the larger firm. Secondly, even a small event window cannot fully separate the announcement effect from other effects within the 21 days analyzed. Especially LVMH, being a large holding, could incorporate other effects from different business groups into the share price at the time of the event. Thirdly, the acquirer might engage in multiple acquisitions and projects at the same time as the time from negotiation to integration could amount to several years. In LVMH's case, in 2019, together with acquiring Tiffany, Fenty's new label in which LVMH holds 50.01%, was also launched. Fourthly, as some of the possible synergies were already anticipated before the announcement, the official announcement could have a weaker effect on the share price. This could indeed be the case as positive logarithmic returns were recorded for L'Oréal both before acquiring The Body Shop and IT Cosmetics. Another caution when interpreting the results is indicated when regarding The Body Shop and L'Oréal's negative returns on the announcement day. As The Body Shop was sold in 2017, the market could have already anticipated in 2006 that the expected synergies will not be fully realized for L'Oréal, as The Body Shop was simply not a good fit for the French cosmetics company. This, however, cannot be verified.

While long-term wealth effects would be a very useful indicator to measure the overall value creation or destruction of M&A activity, measuring long-term returns with regard to acquisitions is nearly impossible. The reasons for this are quite straightforward, as after five or ten years the acquisition effect can no longer be separated from other effects in a firm—as firms not only acquire more than one target in a given timeframe but also grow organically and enter into other agreements, extracting the one acquisition effect is impossible. However, the analysis of the internal competition in both LVMH and L'Oréal yielded interesting results about possible long-term results of acquisition activity. As LVMH's Intra-Group debt share

of overall gross borrowings amounted to almost 30%, this indicates a high level of internal competition to receive these funds to launch new products or boost performance. While L'Oréal does not disclose these numbers, one can guess that several brands under the L'Oréal umbrella, and competing in the same cosmetics market, must have some internal competition.

#### **4.2.3 Financial Conglomerate**

While conglomerates were found to experience conglomerate discounts in the literature (Martynova & Renneboog, 2005, 2006), there is not enough evidence to clearly state whether LVMH is traded at a conglomerate discount. In conjunction with other analysts stating that LVMH is overvalued anyway, this becomes very difficult to quantify. Another important point made was that, while the conglomerate might reduce the risk of the cash flow and diversify the firm, the investors can do so by themselves in their portfolio without the need of an expensive M&A (Gaughan, 2007; Lewellen, 1971; Vernimmen et al., 2017). This indeed is a valid point, as an investor could build a portfolio with a similar risk profile as LVMH has. The expensive acquisitions must then be compared to the financial benefits LVMH provides its investors with. LVMH's short-term returns, financial synergies such as the WACC, and the lacking reduction of risk due to diversification (as one could see compared to L'Oréal in the COVID-crisis), do not seem to present financial advantages due to LVMH being a conglomerate. Nonetheless, LVMH's shares are increasing to record highs, indicating that the conglomerate's strategy must be appropriate in practical terms. It seems, however, that the success of LVMH's acquisition strategy is mainly due to its strategic implications rather than its financial ones.

The question of whether LVMH is also a conglomerate in the financial sense is also relevant. As LVMH's  $\beta$  does not indicate a fully diversified firm, I could imagine that the cash flows are more correlated than expected in a conglomerate, which is also indicated by the fact that, as all Maisons are operating in the luxury segment, they do seem to correlate somehow.

#### **4.3 Summary**

The discussion about LVMH's and L'Oréal's financial and strategic indicators regarding acquisitions yielded interesting results. However, most of the financial results were negative for both companies. An analysis of the financial indicators alone does not align with the success the two companies have been having for some years and even decades. This lets me

conclude that financial reasons are not primarily responsible for LVMH and L'Oréal's acquisition strategies. While both companies of course consider financial indicators in their acquisitions, their overall drive for acquisitions appears to be more strategically motivated. However, financial indicators naturally also play a role in the overall evaluation within the two companies as their financial performance increased over the years. This means that both analyses cannot be entirely separated, as they are closely aligned.

Strategically, LVMH and L'Oréal show many similarities in their acquisition strategies, probably more than one would initially expect. However, their distinct strategies, diversification, and universalization, can be observed when analyzing the two firms in more depth. While both companies mostly let their brands operate independently, both groups provide some back-office support to let their brands focus on their core abilities. While one would expect L'Oréal to integrate their brands better than LVMH, due to a focus and, in turn, increased knowledge about one market, LVMH disproves this view. Indeed, the conglomerate has many synergies that are exploited by its acquisitions, which among others include production, distribution, advertising space, and supplier relationships. However, there is one main motivation that is not as present in the literature. Regarding LVMH and L'Oréal's experience, knowledge, financial resources, and other relevant factors, both firms could create each of their brands on their own, but still, they choose to acquire. One motive, and maybe the most relevant one, to engage in these types of acquisitions, is to obtain the names and associations of the brands acquired. LVMH does not only acquire Tiffany and its value chain, but it also acquires *Tiffany Blue* and the association with Audrey Hepburn in *Breakfast at Tiffany's*. L'Oréal is also not simply acquiring IT Cosmetics' innovative makeup product, but founder Lima's close relationships and connections with its customers that derived from her directly applying the makeup her company produces on-screen after showing her skin issues. While neither LVMH nor L'Oréal would acquire a firm in bad shape, the acquired brands and its names and associations do play an important role and cannot simply be replicated by the two. The acquisition of companies that are in a good shape is aligned with the financial indicators that were analyzed. While the financial analysis on its own does not prove the success of an acquisition, the brands acquired must live up to a certain standard.

While LVMH can be regarded as a classical conglomerate, it should nonetheless be considered that although LVMH's products are very different from each other and are being sold

in different market segments, the overall market seems to be identified as a “luxury market.” Therefore, in a way it is questionable whether LVMH classifies as a conglomerate in the strictest sense. In fact, the analysis has rather shown that, if LVMH is indeed a conglomerate, it is a weak one because its business groups are still so related that they do not reduce the overall risk as expected, as they react to similar changes in the economic environment and can be classified as being in a very similar market overall.

To conclude, it can thus be stated that both LVMH and L’Oréal show many similarities in their acquisition strategies, yet their differences are distinct as they follow different overall strategies, namely diversification and universalization. While financial motives do not seem to be the primary driver for their acquisition engagement, their strategic motivations do play a key role in this regard. Moreover, while the strategic and financial analyses were performed separately, they are not distinct performance measures. Without a well-considered strategy, financial performance would deteriorate and without making sure that debt levels and timing are optimal brands cannot be properly integrated into the respective strategic visions. While increases in market share and the removal of competition, which might even go as far as a monopoly, are strategically motivated, these would subsequently translate into financial benefits. Therefore, although performed separately, the financial and strategic evaluations are of a give-and-take nature and cannot be seen as separate entities.

## **5 Conclusion**

This thesis aimed to answer the question regarding how LVMH and L’Oréal choose their respective acquisition strategies. As both firms have been very successful in the past, and show record numbers after the decreasing performance during the COVID-19 pandemic, the goal of this thesis was to evaluate and compare their distinctive strategies. Following the literature review, the practical part was designed to test whether the findings in the literature apply to LVMH and L’Oréal or not. While many findings were similar to what the literature proposed, some findings in this thesis yielded different results. Although the strategic and the financial aspects were analyzed individually, they do go together in practice, as a strategic decision influences financial performance and vice versa.

While LVMH and L’Oréal follow different strategies that are very diversified on the one hand and very focused on the other hand, the comparison yielded both similarities and differences between the two firms. Interestingly, both firms’ financial indicators do not fully

explain their acquisition strategies, as they are sometimes even negative as a result of an acquisition. Instead, the strategic indicators seem to be the main driver for why LVMH and L'Oréal engage in acquisitions. Even though a thorough financial analysis of their potential targets is performed, and only well-performing firms are acquired and held by the two firms, the strategic motivations dominate the decision to acquire. The most important factor to choose their targets, however, is based on the branding that the acquired companies have, as both LVMH and L'Oréal would have the necessary funds and knowledge to solely follow greenfield investments. However, when purchasing different firms, they also purchase their names and what they stand for, which cannot simply be copied by LVMH and L'Oréal. Another interesting conclusion was made about LVMH and whether it classifies as a conglomerate. Although its business groups are independent of each other; they still operate under the luxury umbrella and are therefore influenced by similar drivers in the economy. This lets me conclude that LVMH does not classify as a pure conglomerate.

To conclude, both LVMH and L'Oréal are successful with their distinctive strategies, and no clear “winner” could be identified from this analysis. However, these two completely distinct acquisition strategies both yield success for both companies and it will be very interesting to see what the future brings and whether both LVMH and L'Oréal maintain their current strategies or will deviate from them a few years from now.

One major limitation of the research was the lack of availability of public data on LVMH and L'Oréal, including information about possible synergies and performance measures for each of the companies' brands before and after the acquisitions. Furthermore, information about the internal valuation of targets and the target selection or negotiation process was lacking. Information regarding price increases is very difficult to evaluate with the given data. Other limitations include the separation of acquisition effects and other company effects. This is relevant for both the short-term and the long-term effects, whereas the long-term effects are even more difficult to separate. Overall, the most challenging limitation to overcome was the lack of data, either because it is not public or because it is not measurable, as, for example, the performance absent acquisitions. Finding a way to separate acquisition effects from other effects, especially in the long-term, is an important future research question.

## **Reference List**

- Amihud, Y., & Lev, B. (1981). Risk reduction as a managerial motive for conglomerate mergers. *The bell journal of economics*, 605-617.
- Ansoff, H. I., Kipley, D., Lewis, A., Helm-Stevens, R., & Ansoff, R. (2018). *Implanting strategic management*: Springer.
- Arnett, G. (2019). *What acquiring Tiffany for \$16.2 billion does for LVMH*. Vogue Business. Retrieved June 28, 2021, from <https://www.voguebusiness.com/companies/what-acquiring-tiffany-does-for-lvmh-luxury-richemont>
- Berman, L. (2016). *L'Oréal Will Apply IT Cosmetics for \$1.2B*. TheStreet. Retrieved June 28, 2021, from <https://www.thestreet.com/markets/mergers-and-acquisitions/l-or-eacute-al-will-apply-it-cosmetics-for-1-2b-13649644>
- Bloomberg L.P. (n.d.-a). *Cie Financiere Richemont SA (CFR SW) - Weighted Average Cost of Capital, 2011-2020*. Retrieved July 19, 2021, from Bloomberg Terminal
- Bloomberg L.P. (n.d.-b). *Estee Lauder Cos Inc/The (EL US) - Financial Analysis, Liquidity, 2011-2020*. Retrieved August 13, 2021, from Bloomberg Terminal
- Bloomberg L.P. (n.d.-c). *Estee Lauder Cos Inc/The (EL US) - Weighted Average Cost of Capital, 2011-2020*. Retrieved July 19, 2021, from Bloomberg Terminal
- Bloomberg L.P. (n.d.-d). *Kering SA (KER FP) - Weighted Average Cost of Capital, 2011-2020*. Retrieved July 19, 2021, from Bloomberg Terminal
- Bloomberg L.P. (n.d.-e). *L'Oreal SA (OR FP) - Credit Ratings Profile*. Retrieved August 11, 2021, from Bloomberg Terminal
- Bloomberg L.P. (n.d.-f). *L'Oreal SA (OR FP) - Financial Analysis, BBG Adjusted Highlights, 2014-2022 (Estimated) in EUR*. Retrieved July 10, 2021, from Bloomberg Terminal
- Bloomberg L.P. (n.d.-g). *L'Oreal SA (OR FP) - Financial Analysis, BBG Adjusted Income Statement, 2014-2022 (Estimated) in EUR*. Retrieved July 11, 2021, from Bloomberg Terminal
- Bloomberg L.P. (n.d.-h). *L'Oreal SA (OR FP) - Financial Analysis, Income Statement by Geography, 2012-2019 in EUR*. Retrieved July 10, 2021, from Bloomberg Terminal
- Bloomberg L.P. (n.d.-i). *L'Oreal SA (OR FP) - Financial Analysis, Liquidity, 2011-2020*. Retrieved August 13, 2021, from Bloomberg Terminal
- Bloomberg L.P. (n.d.-j). *L'Oreal SA (OR FP) - Financial Analysis, Profitability, 2011-2020*. Retrieved July 12, 2021, from Bloomberg Terminal
- Bloomberg L.P. (n.d.-k). *L'Oreal SA (OR FP) - Financial Analysis, Standardized Balance Sheet, 2014-2020 in EUR*. Retrieved July 10, 2021, from Bloomberg Terminal
- Bloomberg L.P. (n.d.-l). *L'Oreal SA (OR FP) - Mergers & Acquisitions, Deal Breakdown*. Retrieved August 12, 2021, from Bloomberg Terminal
- Bloomberg L.P. (n.d.-m). *L'Oreal SA (OR FP) - Share Price, Daily Last Price, 01/01/1984-12/31/2020 in EUR*. Retrieved August 5, 2021, from Bloomberg Terminal
- Bloomberg L.P. (n.d.-n). *L'Oreal SA (OR FP) - Share Price, Daily Last Price, 01/01/2020-07/30/2021 in EUR*. Retrieved July 30, 2021, from Bloomberg Terminal
- Bloomberg L.P. (n.d.-o). *L'Oreal SA (OR FP) - Weighted Average Cost of Capital, 2011-2020*. Retrieved July 18, 2021, from Bloomberg Terminal
- Bloomberg L.P. (n.d.-p). *L'Oreal SA (OR FP) - Bloomberg Default Risk, 1999-2021 in EUR*. Retrieved August 13, 2021, from Bloomberg Terminal

- Bloomberg L.P. (n.d.-q). *L'Oreal SA (OR FP) - Equity Relative Valuation, Analyst Courated, BI Europe Household Products Manufacturing Valuation Peers (BIHPCCEV Index), 5 Years*. Retrieved from Bloomberg Terminal
- Bloomberg L.P. (n.d.-r). *LVMH Moet Hennessy Louis Vuitton SE (MC FP) - Bloomberg Default Risk, 1999-2021*. Retrieved August 12, 2021, from Bloomberg Terminal
- Bloomberg L.P. (n.d.-s). *LVMH Moet Hennessy Louis Vuitton SE (MC FP) - Credit Ratings Profile*. Retrieved August 11, 2021, from Bloomberg Terminal
- Bloomberg L.P. (n.d.-t). *LVMH Moet Hennessy Louis Vuitton SE (MC FP) - Equity Relative Valuation, BICS Best Fit (Algo), Global, Mkt Cap > 4.23B, 5 Years in EUR*. Retrieved July 15, 2021, from Bloomberg Terminal
- Bloomberg L.P. (n.d.-u). *LVMH Moet Hennessy Louis Vuitton SE (MC FP) - Equity Relative Valuation, Global Industry Classification Standard, Global, Apparel, Accessories & Luxury Goods - Sub Industry, 5 Years in EUR*. Retrieved July 15, 2021, from Bloomberg Terminal
- Bloomberg L.P. (n.d.-v). *LVMH Moet Hennessy Louis Vuitton SE (MC FP) - Equity Relative Valuation, Industry Classification Benchmark, Global*. Retrieved July 15, 2021, from Bloomberg Terminal
- Bloomberg L.P. (n.d.-w). *LVMH Moet Hennessy Louis Vuitton SE (MC FP) - Equity Relative Valuation, Industry Classification Benchmark, Global, Clothing and Accessories - Subsector, 5 Years in EUR*. Retrieved July 18, 2021, from Bloomberg Terminal
- Bloomberg L.P. (n.d.-x). *LVMH Moet Hennessy Louis Vuitton SE (MC FP) - Equity Relative Valuation, Sustainable Industry Classification System, Global, Apparel, Accessories & Footwear - Subsectors, 5 Years in EUR*. Retrieved July 15, 2021, from Bloomberg Terminal
- Bloomberg L.P. (n.d.-y). *LVMH Moet Hennessy Louis Vuitton SE (MC FP) - Financial Analysis, BBG Adjusted Highlights, 2014-2022 in EUR*. Retrieved July 10, 2021, from Bloomberg Terminal
- Bloomberg L.P. (n.d.-z). *LVMH Moet Hennessy Louis Vuitton SE (MC FP) - Financial Analysis, BBG Adjusted Income Statement, 2014-2022 (Estimated) in EUR*. Retrieved July 10, 2021, from Bloomberg Terminal
- Bloomberg L.P. (n.d.-aa). *LVMH Moet Hennessy Louis Vuitton SE (MC FP) - Financial Analysis, BBG Adjusted Income Statement, SI 2019-SI 2021 in EUR*. Retrieved August 10, 2021, from Bloomberg Terminal
- Bloomberg L.P. (n.d.-ab). *LVMH Moet Hennessy Louis Vuitton SE (MC FP) - Financial Analysis, Liquidity, 2011-2020 in EUR*. Retrieved July 10, 2021, from Bloomberg Terminal
- Bloomberg L.P. (n.d.-ac). *LVMH Moet Hennessy Louis Vuitton SE (MC FP) - Financial Analysis, Profitability, 2011-2020 in EUR*. Retrieved July 17, 2021, from Bloomberg Terminal
- Bloomberg L.P. (n.d.-ad). *LVMH Moet Hennessy Louis Vuitton SE (MC FP) - Financial Analysis, Standardized Balance Sheet, 2011-2020 in EUR*. Retrieved July 10, 2021, from Bloomberg Terminal
- Bloomberg L.P. (n.d.-ae). *LVMH Moet Hennessy Louis Vuitton SE (MC FP) - Mergers & Acquisitions, Deal Breakdown*. Retrieved August 12, 2021, from Bloomberg Terminal

- Bloomberg L.P. (n.d.-af). *LVMH Moët Hennessy Louis Vuitton SE (MC FP) - Share Price, Daily Last Price, 01/02/2017-12/31/2020 in EUR*. Retrieved July 14, 2021, from Bloomberg Terminal
- Bloomberg L.P. (n.d.-ag). *LVMH Moët Hennessy Louis Vuitton SE (MC FP) - Short and Long Term Debt, in EUR*. Retrieved July 25, 2021, from Bloomberg Terminal
- Bloomberg L.P. (n.d.-ah). *LVMH Moët Hennessy Louis Vuitton SE (MC FP) - Total Return Analysis, 01/02/2009-12/31/2019 in EUR*. Retrieved July 16, 2021, from Bloomberg Terminal
- Bloomberg L.P. (n.d.-ai). *LVMH Moët Hennessy Louis Vuitton SE (MC FP) - Weighted Average Cost of Capital, 2011-2020*. Retrieved July 19, 2021, from Bloomberg Terminal
- Bloomberg L.P. (n.d.-aj). *LVMH Moët Hennessy Louis Vuitton SE (MC FP) - Yearly Historical Raw Beta, Based on Daily Closing Prices, Relative to CAC Index, 2011-2020*. Retrieved July 30, 2021, from Bloomberg Terminal
- Bloomberg L.P. (n.d.-ak). *Tiffany & Co (TIF US) - Financial Analysis, BBG Adjusted Income Statement, Q1 2019-Q4 2020 in EUR*. Retrieved August 10, 2021, from Bloomberg Terminal
- Bloomberg L.P. (n.d.-al). *Tiffany & Co (TIF US) - Financial Analysis, Growth, 2015-2020*. Retrieved July 15, 2021, from Bloomberg Terminal
- Bloomberg L.P. (n.d.-am). *Tiffany & Co (TIF US) - Share Price, Daily Last Share Price, 01/03/2017- 12/31/2019 in USD*. Retrieved July 15, 2021, from Bloomberg Terminal
- Bloomberg L.P. (n.d.-an). *Unilever PLC (ULVR LN) - Financial Analysis, Liquidity, 2011-2020*. Retrieved August 13, 2021, from Bloomberg Terminal
- Bloomberg L.P. (n.d.-ao). *Unilever PLC (ULVR LN) - Weighted Average Cost of Capital, 2011-2020*. Retrieved July 19, 2021, from Bloomberg Terminal
- BrandZ, & Kantar. (2020). *BrandZ Top 100 Most Valuable Global Brands 2020*. Diffusion Sport. Retrieved July 5, 2021, from [https://www.diffusionsport.com/wp-content/uploads/2020/07/2020\\_BrandZ\\_Global\\_Top\\_100\\_Report.pdf](https://www.diffusionsport.com/wp-content/uploads/2020/07/2020_BrandZ_Global_Top_100_Report.pdf)
- Breit, T. (2021). *Holding GmbH: Wann ist sie von Vorteil und wann eine Gefahr für Ihre Firmen?* Steuerberatung Breit. Retrieved July 1, 2021, from <https://www.steuerberatung-breit.de/holding-wann-ist-sie-von-vorteil-und-wann-eine-gefahr-fuer-ihre-gmbhs/>
- Bürgi, M. (2018). *Nestlé kappt die Banden mit den Bettencourts*. Handelszeitung. Retrieved July 18, 2021, from <https://www.handelszeitung.ch/unternehmen/nestle-kappt-die-banden-mit-den-bettencourts>
- Butler, S. (2017). *L'Oréal to sell Body Shop to Brazil's Natura in €1bn deal*. The Guardian. Retrieved July 15, 2021, from <https://www.theguardian.com/business/2017/jun/09/loreal-body-shop-natura-aesop>
- Caldwell, G. (2016). *Largest Acquisition For 8 Years; L'oréal To Acquire It Cosmetics For US\$1.2 Billion*. Global Cosmetics News. Retrieved July 5, 2021, from <https://www.globalcosmeticsnews.com/largest-acquisition-for-8-years-l-oreal-to-acquire-it-cosmetics-for-us-1-2-billion/>
- Campbell, D., Edgar, D., & Stonehouse, G. (2011). *Business Strategy : An Introduction*: Macmillan International Higher Education.
- Caves, R. E. (2007). *Multinational enterprise and economic analysis*: Cambridge University Press.

- Claire Domergue. (2021). *The LVMH Share Shows All The Signs Of Being Significantly Overvalued*. LUXUS+. Retrieved July 15, 2021, from <https://luxus-plus.com/en/the-lvmh-share-shows-all-the-signs-of-being-significantly-overvalued/>
- Cohan, P. (2019). *Four Reasons \$16.2 Billion Tiffany Acquisition Makes LVMH Stock A Buy*. Retrieved July 9, 2021, from <https://www.forbes.com/sites/petercohan/2019/11/25/four-reasons-162b-tiffany-acquisition-makes-lvmh-stock-a-buy/?sh=76910c36659b>
- Collins, A. (2016). *L'Oréal to Acquire IT Cosmetics for \$1.2B*. WWD. Retrieved July 3, 2021, from <https://wwd.com/business-news/financial/loreal-to-acquire-it-cosmetics-for-1-2b-10495227/>
- Compagnie Financière Richemont SA. (2021). *Annual Report and Accounts 2020*. Richemont Company Website. Retrieved from <https://www.richemont.com/en/home/investors/results-reports-presentations/>
- Cox, R. (2006). Mergers and acquisitions: A review of the literature. *Corporate Ownership & Control*, 3(3), 55-59.
- Das, A., & Kapil, S. (2012). Explaining M&A performance: a review of empirical research. *Journal of Strategy and Management*.
- Devos, E., Kadapakkam, P.-R., & Krishnamurthy, S. (2008). How Do Mergers Create Value? A Comparison of Taxes, Market Power, and Efficiency Improvements as Explanations for Synergies. *The Review of Financial Studies*, 22(3), 1179-1211. doi:10.1093/rfs/hhn019
- EY. (November 9, 2019). *Sales of the leading luxury companies worldwide from 2012 to 2021 (in billion euros) [Graph]*. In Statista. Statista. Retrieved July 1, 2021, from <https://www.statista.com/statistics/245697/sales-of-the-leading-luxury-companies-worldwide/>
- Farrell, J., & Shapiro, C. (1990). Horizontal mergers: an equilibrium analysis. *The American Economic Review*, 107-126.
- Fenty Beauty LLC. (2021). *Mattemoiselle Plush Matte Lipstick*. Fenty Beauty Company Website. Retrieved July 4, 2021, from <https://fentybeauty.com/products/mattemoiselle-plush-matte-lipstick-candy-venom>
- Fondazione Altagamma. (2021). *Value of the personal luxury goods market worldwide from 1996 to 2020 (in billion euros)*. Statista. Retrieved July 21, 2021, from <https://www.statista.com/statistics/266503/value-of-the-personal-luxury-goods-market-worldwide/>
- Gaughan, P. A. (2007). *Mergers, acquisitions, and corporate restructurings*: John Wiley & Sons.
- Gauvillé, G., Ireland, L., Spillecke, S., & Tillson, C. (2016). *LVMH – A sum-of-the-parts story*. Credit Suisse. Retrieved July 16, 2021, from [https://research-doc.credit-suisse.com/docView?language=ENG&format=PDF&sourceid=csplusresearchcp&document\\_id=807319880&serialid=Z%2BzqgGJA1C4RZ%2FsiE2w%2FLcdTBdPull92SsODcIXKeds%3D&cspId=null](https://research-doc.credit-suisse.com/docView?language=ENG&format=PDF&sourceid=csplusresearchcp&document_id=807319880&serialid=Z%2BzqgGJA1C4RZ%2FsiE2w%2FLcdTBdPull92SsODcIXKeds%3D&cspId=null)
- Gell, J., Friedman, D., Wald, D., Shinall, P., Wilson, T., & Sanchez Arroyo, C. (2019). *Riding the M&A Wave in Consumer Goods*. Boston Consulting Group. Retrieved June 25, 2021, from <https://www.bcg.com/publications/2019/riding-mergers-acquisitions-wave-in-consumer-goods.aspx>
- Gell, J., Gjerstad, K., Shinall, P., & Istvan, B. (2017). *Why Consumer Goods Companies need To Build, Buy, and Broker*. Boston Consulting Group. Retrieved June 24, 2021, from

- <https://www.bcg.com/en-us/publications/2017/consumer-goods-companies-build-buy-broker-2017-consumer-value-creators.aspx>
- GuruFocus. (2021). *LVMH Moet Hennessy Louis Vuitton SE Stock Is Believed To Be Significantly Overvalued*. GuruFocus.com. Retrieved July 15, 2021, from <https://www.gurufocus.com/news/1490296/five-below-stock-is-believed-to-be-fairly-valued>
- Haleblian, J., Devers, C. E., McNamara, G., Carpenter, M. A., & Davison, R. B. (2009). Taking stock of what we know about mergers and acquisitions: A review and research agenda. *Journal of management*, 35(3), 469-502.
- Halpern, P. (1983). Corporate acquisitions: A theory of special cases? A review of event studies applied to acquisitions. *The Journal of Finance*, 38(2), 297-317.
- Hitt, M. A., Ireland, R. D., & Hoskisson, R. E. (2016). *Strategic management: Concepts and cases: Competitiveness and globalization*: Cengage Learning.
- Hoberg, G., & Phillips, G. M. (2011). *Conglomerate industry choice and product differentiation*. Retrieved from <https://www.nber.org/papers/w17221>
- Jensen, M. C., & Ruback, R. S. (1983). The market for corporate control: The scientific evidence. *Journal of Financial Economics*, 11(1-4), 5-50.
- Jolly, D. (2014). *LVMH Boss and Hermès Family in Pact*. The New York Times. Retrieved July 15, 2021, from <https://www.nytimes.com/2014/09/04/business/international/lvmh-and-hermes-strike-deal-to-end-shareholder-dispute.html>
- Kering. (2021). *2020 Universal Registration Document*. Kering Company Website. Retrieved July 4, 2021, from [https://keringcorporate.dam.kering.com/m/726533d8fa257732/original/Kering\\_2020\\_Universal\\_Registration\\_Document.pdf](https://keringcorporate.dam.kering.com/m/726533d8fa257732/original/Kering_2020_Universal_Registration_Document.pdf)
- L'Oréal S.A. (2002). *L'Oréal And Nestlé Announce A Joint-Venture Project* [Press release]. Retrieved from <https://www.loreal.com/de-de/germany/press-release/group/loral-and-nestle-announce-a-jointventure-project/>
- L'Oréal S.A. (2020a). *2019 Universal Registration Document*. L'Oréal Company Website. Retrieved July 4, 2021, from [https://www.loreal-finance.com/system/files/2020-08/LOREAL\\_2019\\_Universal\\_Registration\\_Document\\_en.pdf](https://www.loreal-finance.com/system/files/2020-08/LOREAL_2019_Universal_Registration_Document_en.pdf)
- L'Oréal S.A. (2020b). *L'Oréal announces the succession of Jean-Paul Agon as Chief Executive Officer from 1 May 2021* [Press release]. Retrieved from <https://www.loreal-finance.com/eng/news-release/loreal-announces-succession-jean-paul-agon-chief-executive-officer-1-may-2021>
- L'Oréal S.A. (2021a). *2020 Universal Registration Document*. L'Oréal Company Website. Retrieved from [https://www.loreal-finance.com/system/files/2021-03/LOREAL\\_2020\\_Universal\\_Registration\\_Document\\_en\\_0\\_0.pdf](https://www.loreal-finance.com/system/files/2021-03/LOREAL_2020_Universal_Registration_Document_en_0_0.pdf)
- L'Oréal S.A. (2021b). *L'Oréal 2020 Annual Report*. L'Oréal Company Website. Retrieved from [https://www.loreal-finance.com/system/files/2021-03/LOREAL\\_2020\\_Annual\\_Report.pdf](https://www.loreal-finance.com/system/files/2021-03/LOREAL_2020_Annual_Report.pdf)
- L'Oréal S.A. (2000). *L'Oréal Announces Divestiture Of Johnson Product Brands To Wella Ag* [Press release]. Retrieved from <https://www.loreal.com/de-de/germany/press-release/group/loral-announces-divestiture-of-johnson-product-brands-to-wella-ag/>
- L'Oréal S.A. (2016). *L'Oréal signs agreement to acquire IT Cosmetics* [Press release]. Retrieved from [https://www.loreal-finance.com/system/files/publication-content/documents/LOreal\\_acquisition\\_IT\\_Cosmetics\\_EN\\_2016\\_07\\_22.pdf](https://www.loreal-finance.com/system/files/publication-content/documents/LOreal_acquisition_IT_Cosmetics_EN_2016_07_22.pdf)

- Lewellen, W. G. (1971). A pure financial rationale for the conglomerate merger. *The Journal of Finance*, 26(2), 521-537.
- Louri, H. (2001). Entry through acquisition: Determinants of multinational firm choices. *Review of Industrial Organization*, 19(2), 199-209.
- LVMH. (2005). *LVMH sells the company Christian Lacroix* [Press release]. Retrieved from <https://www.lvmh.com/news-documents/press-releases/lvmh-sells-the-company-christian-lacroix/>
- LVMH. (2013). *2012 Reference Document*. LVMH Company Website. Retrieved from [https://r.lvmh-static.com/uploads/2014/10/document\\_de\\_reference\\_2012\\_va.pdf](https://r.lvmh-static.com/uploads/2014/10/document_de_reference_2012_va.pdf)
- LVMH. (2019). *LVMH Reaches Agreement with Tiffany & Co.* [Press release]. Retrieved from <https://r.lvmh-static.com/uploads/2019/11/lvmh-tiffany-press-release-en.pdf>
- LVMH. (2020). *2019 Universal Registration Document*. LVMH Company Website. Retrieved from <https://r.lvmh-static.com/uploads/2019/12/lvmh-urd-2019-va.pdf>
- LVMH. (2021a). *2020 LVMH Annual Report*. LVMH Company Website. Retrieved from [https://r.lvmh-static.com/uploads/2021/03/lvmh\\_rapport-annuel-2020-va.pdf](https://r.lvmh-static.com/uploads/2021/03/lvmh_rapport-annuel-2020-va.pdf)
- LVMH. (2021b). *2020 Universal Registration Document*. LVMH Company Website. Retrieved from <https://r.lvmh-static.com/uploads/2020/06/lvmh-document-denregistrement-2020-va-interactif.pdf>
- LVMH. (n.d.). *The LVMH model*. LVMH Company Website. Retrieved July 12, 2021, from <https://www.lvmh.com/group/about-lvmh/the-lvmh-model/>
- Mandell, J. (2018). *L'Oreal Says 'In Your Face' To Competition With Strategic Acquisition*. Forbes. Retrieved July 3, 2021, from <https://www.forbes.com/sites/jannamandell/2018/03/16/loreal-says-in-your-face-to-competition-with-strategic-ai-and-ar-acquisition-modiface/?sh=bf117201f38c>
- Market Screener. (2021). *LVMH Moët Hennessy Louis Vuitton SE : Volatility should make a big comeback*. MarketScreener.com. Retrieved July 15, 2021, from <https://www.marketscreener.com/quote/stock/LVMH-MOET-HENNESSY-LOUIS-4669/news-strategies/Volatility-should-make-a-big-comeback-33317631/>
- Martynova, M., & Renneboog, L. (2005). *Takeover waves: triggers, performance and motives*: Tilburg University.
- Martynova, M., & Renneboog, L. (2006). Mergers and acquisitions in Europe. *Advances in corporate finance and asset pricing*, 13-75.
- Minaya, E. (2016). *L'Oréal to Acquire IT Cosmetics in \$1.2 Billion Deal*. The Wall Street Journal. Retrieved July 5, 2021, from <https://www.wsj.com/articles/loreal-to-acquire-it-cosmetics-in-1-2-billion-deal-1469211932>
- Mueller, D. C. (1978). The Effects of Conglomerate Mergers. *Management Research News*, 1(3), 6-6. doi:10.1108/eb027703
- Myers, S. C., & Majluf, N. S. (1984). Corporate financing and investment decisions when firms have information that investors do not have. *Journal of Financial Economics*, 13(2), 187-221.
- Nelson, R. L. (1959). *Merger movements in American industry, 1895-1956*: Princeton: Princeton university press.
- NYX Professional Makeup. (2021). *Lip Lingerie Nude Matte Lipstick*. NYX Cosmetics Company Website. Retrieved July 16, 2021, from [https://www.nyxcosmetics.com/lip/lipstick/lip-lingerie/NYX\\_315.html?dwvar\\_NYX\\_315\\_color=Embellishment](https://www.nyxcosmetics.com/lip/lipstick/lip-lingerie/NYX_315.html?dwvar_NYX_315_color=Embellishment)

- Olbertova, M. (2019). *Opinion: A Deal Between LVMH and Tiffany Represents A Win-Win For Both Parties*. Luxury Society. Retrieved July 4, 2021, from <https://luxurysociety.com/en/articles/2019/10/opinion-deal-between-lvmh-and-tiffany-represents-win-win-strategy-both-parties>
- Piscioneri, F., Aloisi, S., & White, S. (2021). *More carats and sparkle: How LVMH plans to change Tiffany*. Retrieved July 9, 2021, from <https://www.reuters.com/article/us-lvmh-tiffany-changes-focus-idUSKBN29V0JH>
- Porter, M. E. (1989). *From competitive advantage to corporate strategy*: Springer.
- Porter, M. E. (2008). *Competitive strategy: Techniques for analyzing industries and competitors*: Simon and Schuster.
- Renneboog, L., & Vansteenkiste, C. (2019). Failure and success in mergers and acquisitions. *Journal of Corporate Finance*, 58, 650-699.
- Reuters Staff. (2014). *Nestle and L'Oreal to end Inneov joint venture in 2015*. Reuters. Retrieved July 6, 2021, from <https://www.reuters.com/article/loreal-nestle-idUSWEA00GJR20141127>
- Richemont. (2021). *About Us – History*. Richemont Company Website. Retrieved August 31, 2021, from <https://www.richemont.com/en/home/about-us/history/>
- Ryan, C. (2019). *Why Luxury Giants Keep Popping the Question*. The Wall Street Journal. Retrieved July 16, 2021, from <https://www.wsj.com/articles/why-luxury-giants-keep-popping-the-question-11574076074>
- Schönberger, D. (2020). *L'Oreal: The Leader In The Beauty Market*. Seeking Alpha. Retrieved July 16, 2021, from <https://seekingalpha.com/article/4371421-loreal-leader-in-beauty-market>
- Shleifer, A., & Vishny, R. W. (2003). Stock market driven acquisitions. *Journal of Financial Economics*, 70(3), 295-311.
- Sinha, D. K. (1999). On conglomerate diversification. *Atlantic Economic Journal*, 27(1), 115-115. doi:10.1007/BF02299183
- Sorvino, C. (2017). *How Jamie Kern Lima Built IT Cosmetics Into A \$1.2 Billion Business*. Forbes. Retrieved July 4, 2021, from <https://www.forbes.com/sites/chloesorvino/2017/05/17/jamie-kern-lima-loreal-beauty-it-cosmetics/?sh=206402ea3b4f>
- Sorvino, C. (2019). *L'Oreal's Only Female CEO, The Founder Of IT Cosmetics, Is Leaving*. Forbes. Retrieved July 16, 2021, from <https://www.forbes.com/sites/chloesorvino/2019/08/29/loreal-only-female-ceo-the-founder-of-it-cosmetics-is-leaving/?sh=4593e83e715a>
- Spencer, M. (2019). *LVMH Adds Tiffany in \$16.2B Blockbuster Deal*. WWD. Retrieved July 4, 2021, from <https://wwd.com/business-news/financial/lvmh-seals-tiffany-deal-for-16-2-billion-1203377516/>
- Telesivory. (2019). *Acquisition of Tiffany by LVMH: An Analysis*. Telesivory. Retrieved June 27, 2021, from <https://www.telesivory.com/blogs/-/blogs/acquisition-of-tiffany-by-lvmh-an-analysis>
- Trefis Team. (2020). *At Multi-Year High Of \$64, L'Oreal Stock Too Expensive?* Forbes. Retrieved July 16, 2021, from <https://www.forbes.com/sites/greatspeculations/2020/07/01/at-multi-year-high-of-64-loreal-stock-too-expensive/?sh=42716c16b228>

- Tremblay, V. J., & Tremblay, C. H. (2012). *Horizontal, Vertical, and Conglomerate Mergers*. New York, NY: Springer New York.
- Tsang, A., & Friedman, V. (2019). *Luxury Giant LVMH to Buy Tiffany for \$16.2bn*. The New York Times. Retrieved July 3, 2021, from <https://www.nytimes.com/2019/11/25/business/lvmh-tiffany-deal.html>
- U.S. Bureau. (n.d.). *Consumer Price Index*. U.S. Bureau of Labor Statistics. Retrieved August 12, 2021, from <https://www.bls.gov/cpi/>
- Unilever. (n.d.). *Our Brands*. Unilever Company Website. Retrieved July 20, 2021, from <https://www.unilever.com/brands/>
- Vernimmen, P., Quiry, P., Dallochio, M., Le Fur, Y., & Salvi, A. (2017). *Corporate Finance : Theory and Practice*. Newark, UNITED KINGDOM: John Wiley & Sons, Incorporated.
- Welch, I. (2011). *Corporate finance: Ivo Welch*.
- Williams, R. (2016). *LVMH sells Donna Karan International for \$650m*. Financial Times. Retrieved July 17, 2021, from <https://www.ft.com/content/6cf12528-526a-11e6-9664-e0bdc13c3bef>
- Zubair, M. O. (2021). *Insider Buying Report: LVMH Moet Hennessy - Louis Vuitton SE*. 2iQ Research. Retrieved July 15, 2021, from <https://www.2iqresearch.com/blog/insider-buying-report-lvmh-moet-hennessy-louis-vuitton-se-2021-01-05>

**Appendix****Appendix A****List of LVMH maisons (LVMH, 2021b)**

*Wine & Spirits:* Ao Yun, Ardbeg, Belvedere, Bodega Numanthia, Cape Mentelle, Chandon, Château Cheval Blanc, Château d'Yquem, Cheval des Andes, Clos des Lambrays, Clos19, Cloudy Bay, Dom Pérignon, Glenmorangie, Hennessy, Krug, Mercier, Moët & Chandon, Newton Vineyard, Ruinart, Terrazas de los Andes, Veuve Clicquot, Volcan de mi Tierra, Woodinville

*Fashion & Leather Goods:* Berluti, Celine, Christian Dior, Emilio Pucci, FENDI, Givenchy, Kenzo, Loewe, Loro Piana, Louis Vuitton, Marc Jacobs, Moynat, Patou, RIMOWA

*Perfumes & Cosmetics:* Acqua di Parma, Benefit Cosmetics, Cha Ling, Fenty Beauty by Rihanna, Fresh, Givenchy Parfums, Guerlain, Kenzo Parfums, KVD Vegan Beauty, Maison Francis Kurkdjian, Make Up For Ever, Marc Jacobs Beauty, Parfums Christian Dior, Perfumes Loewe

*Watches & Jewelry:* Bvlgari, Chaumet, Fred, Hublot, TAG Heuer, Tiffany & Co., Zenith

*Selective Retailing:* DFS, La Grande Epicerie de Paris, Le Bon Marché Rive Gauche, Sephora, Starboard Cruise Services

*Other Activities:* Belmond, Cheval Blanc, Connaissance des Arts, Cova, Investir, Jardin d'Acclimatation, La Samaritaine, Le Parisien, Les Echos, Radio Classique, Royal Van Lent

**Appendix B****List of L'Oréal Brands (L'Oréal S.A., 2021a)**

*Consumer Products Division:* L'Oréal Paris, Garnier, Maybelline New York, NYX Professional Makeup, Stylenanda, Essie, Dark & Lovely, Mixa, Magic Mask, Niely

*L'Oréal Luxe Division:* Lancôme, Kiehl's Since 1851, Armani, Yves Saint Laurent, Biotherm, Helena Rubinstein, Shu Uemura, IT Cosmetics, Urban Decay, Ralph Lauren Fragrances, Mugler, Viktor&Rolf, Valentino, Azzaro, Diesel, Atelier Cologne, Prada, Cacharel, Yue Sai

*Professional Products Division:* L'Oréal Professionnel, Kérastase, Redken, Matrix

*Active Cosmetics Division:* Pureology, La Roche-Posay, Vichy, CeraVe, SkinCeuticals, Decléor

### Appendix C

#### **Kering's Luxury Houses As of December 31, 2020 (Kering, 2021)**

*Couture and Leather Goods:* Gucci, Yves Saint Laurent, Bottega Veneta, Balenciaga, Alexander McQueen, Brioni

*Watches and Jewelry:* Boucheron, Pomellato, DoDo, Qeelin, Ulysse Nardin, Girard-Perregaux

*Other:* Kering Eyewear

### Appendix D

#### **Richemont's Maisons And Brands (Compagnie Financière Richemont SA, 2021)**

*Jewellery:* Buccellati, Cartier, Van Cleef & Arpels

*Specialist Watchmakers:* A. Lange & Söhne, Baume & Mercier, Iwc Schaffhausen, Jaeger Lecoultre, Panerai, Piaget, Roger Dubuis, Vacheron Constantin

*Online Distributors:* Watchfinder & Co., Net-A-Porter, Mr Porter, The Outnet, Yoox, Online Flagship Stores

*Fashion & Accessories / Other:* Alaïa, Alfred Dunhill, Az Factory, Chloé, Delvaux, Montblanc, Peter Millar, Purdey, Serapian

### Appendix E

#### **List of LVMH's Subsidiaries And Investments As of 2020 (LVMH, 2021b)**

*Subsidiaries (>50%):* Sofidiv SAS (100%), Christian Dior Couture SA (100%), Bulgari SpA (100%), LVMH Miscellanées SA (99.99%), Vicuna Holding SpA (100%), Moët Hennessy SAS (58.67%), LV Group SA (99.95%), Rimowa Group GmbH (100%), Le Bon Marché SA (99.99%), Parfums Christian Dior SA (99.99%), Moët Hennessy Inter. SAS (58.67%), LVMH Services Ltd (100%), LVMH KK (100%), P&C International SAS (100%)

*Equity investments (<50%):* GIE LVMH Services (20%), Loewe SA (5.44%)

Appendix F

LVMH’s Organizational Chart As of 2020 (LVMH, 2021b)



## Appendix G

### List of L'Oréal's Subsidiaries And Investments (L'Oréal S.A., 2021a)

*Main French Investments (>50% ownership):* Azzaro Mugler Beauté France, Beauté Recherche & Industries, Cosmétique Active International, Cosmétique Active Production, Cosmeurop,, EpiSkin, Fapagau & Cie, Faporeal, Finval, Gemey Paris - Maybelline New York, Holdial L & J Ré, La Roche-Posay Laboratoire Pharmaceutique, Noveal, Nutricos Technologies, Laboratoire Sanoflore, L'Oréal Fund For Nature Regeneration, L'Oréal Produits de Luxe International, LOA3, BOLD (Business Opportunities for L'Oréal Development), LOA7, Real Campus by L'Oréal, LOA10, Retail Excellence 4, Prestige & Collections International, Magic Holdings International Limited, Sicôs & Cie, Soprococ, Soproréal, Sparlys, Thermes De Saint Gervais, Les Bains Le Fayet

*Main International Subsidiaries (>50% ownership):* Atelier Cologne (Luxembourg), Beautycos International Co. Ltd (China), Beautylux International Cosmetics (Shanghai) Co.Ltd (China), Biotherm (Monaco), Canan Kozmetik Sanayi Ve Ticaret A.S. (Turkey), Cosmelor Ltd (Japan), Cosmephil Holdings Corporation (Philippines), Egypteloc LLC (Egypt), Elebelle (Proprietary) Ltd (South Africa), ERWITON S.A. (Uruguay), Interbeauty Cosmetics Ltd (Israel), Kosmepol Sp. z.o.o. (Poland), L'Oréal Adria d.o.o. (Croatia), L'Oréal Argentina SA (Argentina), L'Oréal Australia Pty Ltd, L'Oréal Balkan d.o.o. (Serbia), L'Oréal Baltic SIA (Lithuania), L'Oréal Bangladesh Ltd (Bangladesh), L'Oréal Brasil, L'Oréal Belgilux S.A. (Belgium), L'Oréal Brasil Pesquisas e Inovacao Ltda, L'Oréal Bulgaria EOOD L'Oréal Canada Inc., L'Oréal Central America (Panama), L'Oréal Central West Africa (Nigeria), L'Oréal Ceska Republika s.r.o (Czech Republic), L'Oréal Chile S.A. (Chile), L'Oréal China Co Ltd (China), L'Oréal Colombia S.A. (Colombia), L'Oréal Cosmetics Industry S.A.E (Egypt), L'Oréal Côte d'Ivoire, L'Oréal Danmark A/S (Denmark), L'Oréal Deutschland Gmbh (Germany), L'Oréal East Africa Ltd (Kenya), L'Oréal Ecuador (Ecuador), L'Oréal Espana S.A. (Spain), L'Oréal Finland Oy (Finland), L'Oréal Guatemala S.A., L'Oréal Hellas S.A. (Greece), L'Oréal Hong-Kong Ltd, L'Oréal India Private Ltd (India), L'Oréal Investments B.V. (The Netherlands), L'Oréal Italia Spa, L'Oréal Kazakhstan Llp (Kazakhstan), L'Oréal Korea Ltd (South Korea), L'Oréal Liban SAL, L'Oréal Magyarorszag Kosmetikai Kft (Hungary), L'Oréal Malaysia SDN BHD (Malaysia), L'Oréal Mexico S.A de C.V (Mexico),

L'Oréal Middle East (United Arab Emirates), L'Oréal Nederland B.V. (The Netherlands), L'Oréal New Zealand Ltd (New Zealand), L'Oréal Norge A/S (Norway), L'Oréal Osterreich Gmbh (Austria), L'Oréal Pakistan Private Ltd, L'Oréal Panama S.A., L'Oréal Peru S.A. (Peru), L'Oréal Philippines Inc., L'Oréal Polska Sp. Z.O.O. (Poland), L'Oréal Portugal Lda, L'Oréal Romania SRL (Romania), L'Oréal Saudi Arabia (Saudi Arabia), L'Oréal Singapore Pte Ltd (Singapore), L'Oréal Slovensko s.r.o. (Slovakia), L'Oréal Suisse S.A., L'Oréal Sverige AB (Sweden), L'Oréal Taiwan Co Ltd (Taiwan), L'Oréal Thailand Ltd, L'Oréal Turkiye Kozmetik Sanayi Ve Ticaret Anonim Sirketi, L'OREAL UAE General Trading LLC (United Arab Emirates), L'Oréal UK Ltd (United Kingdom), L'Oréal Ukraine, L'Oréal Uruguay S.A., L'Oréal USA Inc., L'Oréal Venezuela C.A., L'Oréal Vietnam Co Ltd, L'Oréal West Africa Ltd (Ghana), Masrelor LLC (Egypt), Nanda CO Ltd. (Korea), Nihon L'Oréal KK (Japan), L'Oréal Travel Retail Americas Inc. (USA), Procosa Productos de Beleza Ltda (Brazil), P.T. L'Oréal Indonesia, P.T. Yasulor Indonesia, Scental Limited (Hong-Kong), Venprobel (Venezuela)

*Main Investments (<50%):* Sanofi (9.39%), LIPP Distribution (Tunisia) (49%)

## Appendix H

### List of Selected LVMH Acquisitions Since 2012

Announce Date	Target Name	Business Group	Comment
5/3/12	Tanneries Roux SAS	Fashion & Leather Goods	
2/27/13	South Johnstone crocodile farm	Fashion & Leather Goods	
7/8/13	Loro Piana SpA	Fashion & Leather Goods	
7/31/13	Hotel Saint-Barth Isle	Other Activities	
9/20/13	Nicholas Kirkwood Ltd	Fashion & Leather Goods	
4/14/14	Clos des Lambrays	Wine & Spirits	
2/4/19	Boursier.com SA		online financial information and news services in France
11/14/14	Bite Beauty	Perfumes & Cosmetics	
6/25/15	Le Parisien/Aujourd'hui en France	Other Activities	
7/11/15	Sephora Digital Sea Pte Ltd	Selective Retailing	
8/4/15	Sephora Digital Sea Pte Ltd	Selective Retailing	

1/26/16	Pelham Media Ltd	Other Activities	
10/4/16	RIMOWA GmbH	Fashion & Leather Goods	
1/11/17	Ile de Beaute JSC	Selective Retailing	
4/25/17	Christian Dior Couture SA	Fashion & Leather Goods	
11/21/17	Colgin Cellars Inc	Wine & Spirits	
3/29/18	456 North Rodeo Dr/Beverly Hills	Other Activities	
4/30/18	Repossi Diffusion SAM	Watches & Jewelry	
9/26/18	Jean Patou SAS	Perfumes & Cosmetics	
12/14/18	Belmond Ltd	Other Activities	
5/20/19	Chateau du Galoupet SAS	Wine & Spirits	
7/16/19	Bopel Srl	Fashion & Leather Goods	Other Leather and Allied Product Manufacturing Industry
8/7/13	Scentsa/CA		
11/25/19	Tiffany & Co	Watches & Jewelry	
11/29/19	Chateau d'Esclans SASU	Wine & Spirits	
1/28/20	BMC SpA	Watches & Jewelry	Other Miscellaneous Manufacturing
6/14/12	Arnys SA		Import/Export company
6/18/21	Emilio Pucci Srl	Fashion & Leather Goods	

## Appendix I

### Selected Acquisitions of L'Oréal Divided in Product and Geographic Expansion (L'Oréal S.A., 2021a)

Brand Acquisitions	Geographic Acquisitions	Year	Division	Country	Area
Urban Decay		2012	L'Oréal Luxe		
	Vogue	2012		Colombia	Latin America
	Cheryl's Cosmeceuticals	2013		India	Asia Pacific
	Emporio Body Store	2013		Brazil	Latin America
	Interbeauty	2013		Kenya	Africa
Decléor and Carita		2014	Professional Products		
NYX Professional Makeup		2014	Consumer Products Division		

	Magic Holdings	2014		China	Asia Pacific
	Niely Cosméticos	2015		Brazil	Latin America
IT Cosmetics		2016	L'Oréal Luxe		
CeraVe		2017	Active Cosmetics Division		
Logocos		2018	Consumer Products Division		
Pulp Riot		2018	Professional Products		
Valentino (license)		2018	L'Oréal Luxe		
	Stylenanda	2018		South Korea	Asia Pacific
Prada (license)		2019	L'Oréal Luxe		
Azzaro		2020	L'Oréal Luxe		
Mugler		2020	L'Oréal Luxe		

### Appendix J

L'Oréal's Daily Share Price From 01/01/1984 to 12/31/2020 in € (Bloomberg L.P., n.d.-m)



## Appendix K

## LVMH's Default Risk compared to the 'France - Consumer Discretionary: Apparel &amp; Textile Products' group (incl. Bloomberg's default risk scale) (Bloomberg L.P., n.d.-e)

Issuer	Default Risk
Hermes International	IG1
Kering SA	IG1
LVMH Moet Hennessy Louis Vuitton SE	IG1
Christian Dior SE	IG3
Delta Plus Group	IG5
Chargeurs SA	IG8
Deveaux SAS	IG9
Damartex SA	IG9
SMCP SA	HY2
ST Dupont SA	HY2
Oxbow SASU	HY3
Salomon SAS	HY4
Lafuma SA	HY4
Groupe JAJ	HY6
Le Tanneur et Cie	DS2

MC FP Equity		IG1		Default Probability (%)		0.0005%	
Default Risk		IG - Investment Grade		HY - High Yield		DS - Distressed	
	Default Probability (%)		Default Probability (%)		Default Probability (%)		Default Probability (%)
IG1	0.0000 - 0.0020	HY1	0.5200 - 0.8800	DS1	10.0000 - 15.0000		
IG2	0.0020 - 0.0040	HY2	0.8800 - 1.5000	DS2	15.0000 - 22.0000		
IG3	0.0040 - 0.0080	HY3	1.5000 - 2.4000	DS3	22.0000 - 30.0000		
IG4	0.0080 - 0.0152	HY4	2.4000 - 4.0000	DS4	30.0000 - 50.0000		
IG5	0.0152 - 0.0286	HY5	4.0000 - 6.0000	DS5	50.0000 - 100.0000		
IG6	0.0286 - 0.0529	HY6	6.0000 - 10.0000				
IG7	0.0529 - 0.0960						
IG8	0.0960 - 0.1715						
IG9	0.1715 - 0.3000						
IG10	0.3000 - 0.5200						

*For the digital version of the thesis this document has been signed by the author and added as the last page of the PDF file.*

### Honourable Declaration

I certify that:

- (a) the thesis being submitted for examination is created by my own account.
- (b) my research has been conducted ethically.
- (c) the data and results presented are the genuine data and results actually obtained by me during the conduct of the research.
- (d) where I have drawn on the work, ideas and results of others this has been appropriately acknowledged in the thesis.
- (e) where any collaboration has taken place with other researchers, I have clearly stated in the thesis my own personal share in the investigation.
- (f) the thesis has not been presented to any other examination committee before. (An exception applies only to dual degree programmes in which a joint thesis has to be submitted to both the EBS Business School and the partner university.)
- (g) the thesis has not been published before.

Oestrich-Winkel, 05/09/2021 (date: day / month / year)

Leonie Lahn (signature)

LEONIE ANNA SOPHIE IRIS (first name in BLOCK LETTERS)

LÄHN (last name in BLOCK LETTERS)