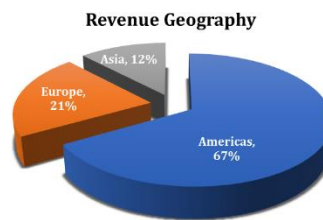


RALPH LAUREN CORP (RL: NYQ)

SECTOR: CONSUMER DISCRETIONARY (LARGE-CAP)

Current Price: 79 \$
1 YR Change: -11.95%
Incorporation: 1997
Beta (Public Source): 0.7348
Valuation Type: Fairly-Valued



Company Description

Ralph Lauren Corporation is one of the leading luxury enterprises involved in designing, marketing and distribution of lifestyle products, including apparel and other licensed product categories. The Company operates through three segments: Wholesale, Retail and Licensing. The Brand "Ralph Lauren" is akin to luxury and quality, a name that commands significant goodwill in consumer's mind.

SWOT

Strength	Weaknesses
<ul style="list-style-type: none"> - Brand Name, The Logo & The Experience - Luxury power-player that is not "mortally" affected by cheaper players - Strong Balance Sheet 	<ul style="list-style-type: none"> - Sales growth negative for coming years - Restructuring charges
Opportunities	Threats
<ul style="list-style-type: none"> - A luxury company no one wants. - Governance reforms slowly getting in place. - David Lauren 	<ul style="list-style-type: none"> - Segment is prone to sudden deaths. - Another Versace, Pierre Cardin in making?

Poor Man's Valuation:

(millions \$)	Cash From Ops. 5 Years	Capex 5 Years	Free Cash Flow 5 Years	Current Assets - All Liabilities	WACC	Shares Outstanding (m)	Expected Market Cap.	Share Price	Cheap or Expensive
Basic Valuation									
Historical	4712	2122	2590	584		82.21		\$ 79	Fairly Valued
Forecasted									
Base Case 20 Years	18848	8488	10360	584	10%	82.21	6795	\$ 83	5%
Bull 20 Year Forecast (+40%)	26387	11883	14504	584	10%	82.21	9368	\$ 114	44%
Bear 20 Year Forecast (-40%)	11309	5093	6216	584	10%	82.21	4222	\$ 51	-35%

Investment Summary

Investing in luxury is usually a bet on the "name" behind the brand, consider Ralph Lauren or Versace, one running and other barely surviving. The business model survives on retaining the brand's "pricing power", consider Pierre Cardin or Versace, once loved luxury powerhouses that either became cheap or irrelevant and just died. Imagine Ralph Lauren lowering prices every year, there are just too many sharks (H&M, ZARA etc) in that pool. Recently Stefan Larsson's departure was pretty much inevitable as you can't replicate the business model of offering trendy clothes for lower prices at Ralph Lauren, something Mr Larsson was quite used to of doing (GAP, H&M). Naturally a misfit, I believe replacing him was a good decision. The nature of this business demanded someone like Brunello Cucinelli, but perhaps he has a business at hand to take care of. Generating significant free cashflow and in the midst of a storm of cost cutting, I believe that David Lauren may step up anytime in future. The business is still doing fine as number of doors and retail stores have been increasing on yearly basis. In the end, all it boils down to is revenues, as from 2009 till 2016, company's revenues are 48% higher whereas the stock is around 50% higher than mid-2009. I believe the enterprise is cheaper than other luxury alternatives and fairly-priced overall. Is this the Coca Cola moment for Ralph Lauren? Hard to say when equity levels are so elevated but if the analyst thinks the brand will survive, Ralph Lauren can be a good purchase at a fair price. Fairly valued, Ralph Lauren offers a fair value play in the luxury space.

FAIRLY VALUED

Average volume 1.28m
Free float 56.08m
P/E (TTM) 46.01
EPS (TTM) 1.75
Shares outstanding (m) 82.21m
Market cap (\$) 6.60bn

FINANCIALS

	2015	2016
Current Ratio	2.80	2.55
Quick Ratio	1.58	1.39
Debt/Equity	0.14	0.23
ROIC (10Yr Avg)	-	15.2%
Interest Coverage	59.06	27.29

VALUATION

Base Growth Rate	1%
Wacc	10%
Forecast Period FCF (m)	2126
Terminal value (m)	5628
PV terminal value (m)	3494
Total EV (m)	5621
Debt (m)	1000
Cash (m)	1085
Equity Value	5706
Shares Outstanding (m)	82.21
Fair Value Share Price	€ 69

Segments Source: Annual Report/Company Website

Locations & Segments

Detail	2009	2010	2011	2012	2013	2014	2015	2016	CAGR
Total Revenues	5018	4978	5660	6864	6943	7453	7620	7405	5.7%
Cash from Ops	774	906	688	885	1019	907	894	1007	3.8%
Capex	185	201	255	272	276	390	391	418	12.3%
Wholesale Revenue	2749	2532	2777	3246	3138	3486	3495	3297	2.6%
Wholesale Doors	6097	8940	9955	11047	10625	11453	12747	13502	12.0%
Americas	2104	4402	5943	6587	6043	6459	7308	7741	20.5%
Europe	3873	4421	3919	4377	4504	4864	5311	5625	5.5%
Asia	120	117	93	83	78	130	128	136	1.8%
Retail Revenues	2074	2263	2704	3438	3624	3798	3956	3933	9.6%
Retail Stores	329	350	367	379	388	433	466	493	5.9%
MAIN Americas	64	65	60	61	56	57	58	56	-1.9%
MAIN Europe	19	20	21	26	27	27	27	29	6.2%
MAIN Asia	3	17	22	16	32	54	58	59	53.0%
MAIN Latin America	3	3	3						
Club Monaco	66	63	58	59	59	60	64	77	2.2%
Rugby Retail	11	11	12	16	1	0	0	0	-100.0%
Factory Retail	163	171	191	201	213	235	259	272	7.6%
Americas	136	137	140	143	148	150	165	168	3.1%
Europe	23	24	31	35	40	50	54	58	14.1%
Asia	4	10	20	23	25	35	40	46	41.8%

- Luxury can be capital intensive too. Ever since 2009, the company has achieved a CAGR of ~5% of sales growth on the basis of ~12% capex growth.
- Retail revenues have had a *larger growth rate* (9.6%) than the wholesale segment (2.6%) which may indicate that capex has more effective in the retail part of the business.
- Lower wholesale revenues make sense as space is being flooded by the likes of Inditex and Primark.
- Naturally keeping own stores requires more capex and goes more in line with creating the "Ralph Lauren Experience" as is reflected by the sales figure.
- U.S still forms the biggest chunk of sales cake.

Strategy and Corporate Governance

- **Strategy includes expansion in Asia and Europe:** Both are plausible regions for growth in the long run. In the short run, I don't see any growth in the regions.
- **Corporate Governance has been rough:** The incoming of Stephen Larsson was treated positively however he was a different animal for the luxury space. Ralph is built on luxury not price cuts, on experience and exclusivity rather than opening a shop in every nook and corner possible (as in H&M)
- **David Lauren:** Will have enough experience and trust of his father to grab the baton. As in inheritance, passing on the baton, especially in a case of a company so wired and built around a single individual can be extremely hard.
- **No compromise (by Ralph) also says something good about the business:** Ralph is not willing to sacrifice The Ralph Lauren experience over any short-term pricing/marketing strategies that a new CFO usually brings according to the "New CEO for Dummies" manual

Model & Assumptions

Revenue Builder	2015	2016	2017	2018	2019	2020	2021
Revenues	7620	7405	7194	7269	7233	7148	7092
% Change	2%	-3%	-3%	1%	0%	-1%	-1%
EBIT	1035	582	771	800	786	781	773
% Sales	14%	8%	11%	11%	11%	11%	11%
Depreciation	294	310	289	298	294	292	289
% Sales	4%	4%	4%	4%	4%	4%	4%
Capex	391	418	384	371	289	286	284
% Sales	5%	6%	5%	5%	4%	4%	4%
FCF	503	589	512	559	649	586	501
% Change	-3%	17%	-13%	9%	16%	-10%	-14%

Explanation

- > Sales modelled with a decline in short term horizon. EBIT is modelled to fall significantly over historical average as charges will bite and it helps establish a base case for the enterprise.
- > Depreciation kept in line with historical standards whereas capex is **expected** to fall.
- > Free cashflow hovers around \$500m which ultimately gives a small upside to the current market valuation.
- > Cost of capital is 10% -debt is low but sector is prone to wild swings- same as other investment cases as fight for capital -in my view- must be judged on the equal footing.

Reporting Quality

Annual Report	Comprehensive.
Auditor's Opinion for Parent Organization	Ernst & Young: Clear.
ESG & Sustainability reporting	High.

Explanation

- > Comprehensive annual report along with a detailed Corporate Governance and Citizenship Report
- > ESG mitigates reputation damage risk which is largely associated to the supply chain part of the luxury industry. Consider the recent buying of a snake farm by Hermes just to tackle the social perspective around luxury.

ESG Materiality Matrix Reported & Assessed	High: Citizenship Report
Quantitative Identification of all key ESG metrics	High: Citizenship Report

Usefulness of ESG metrics in current scenario?

ESG is relevant to the industry as luxury consumers demand a more social role for such businesses. Consider Associated British Foods getting negative PR for employing bad supplier policies in developing world. While lower price may eventually lead consumers to overcome such concerns, paying a *high price* for a product made *unfairly* will not go well with customers in the long run.