



Upslope Capital Management

ALTERNATIVE \ VALUE \ CONCENTRATED

Investment Overview

October 2017

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Salvatore Ferragamo

Upslope Capital Management: Investment Strategy



Core of portfolio is comprised of concentrated *long* investments in high-quality businesses

✓
(This Idea)

Supplemented with diversified *long* investments in more moderate-quality and/or challenged businesses

Individual *shorts* focused largely on secular losers, fads, and challenged business models

Fashion Icon



Salvatore Ferragamo assisting Ms. Loren with one of his creations in 1955

Investment Idea: Salvatore Ferragamo Italia SpA (SFER:IM)

Investment Snapshot⁽¹⁾

- Idea: *long* SFER:IM
- Current Price: €23
- Est. Fair Value: €30
- 52-wk Range: €19 - 30
- Market Cap: €3.9 bn
- Enterprise Value: €3.8 bn
- ADV: €6 mm
- Dividend Yield: 2.3%

Investment Thesis Highlights

- Leading global luxury brand, with rich history
- Attractive underlying financial model
- Poor sentiment due to near-term challenges
- Strong, new executive & creative leadership compelled to action
- Reasonable valuation on current, conservative estimates

Legendary designer and producer of luxury shoes, leather goods, and apparel

Company Overview

Ferragamo: Overview & Brief History

Then

- Founded in 1927⁽¹⁾ in Florence, focused primarily on women's footwear
- Significant sales presence in Italy; minimal international presence (ex-US)
- Wholesale focus: ~70% of sales
- Private, family-managed business

Now

- Diversified luxury goods designer: > 60% of earnings from non-shoe businesses
- Global sales: < 10% of sales from Italy; dominant, early presence in Asia
- Retail focus: ~65% of sales, with ~675 stores
- 2011 IPO; independent management team

What the Brand Has Always Stood For

- "Made in Italy"
- Unique, high-quality design & materials
- Attractive design *and* comfort
- "Affordable luxury" price point

Founded 90+ years ago as the "shoemaker to the stars," Ferragamo has become one of the most respected fashion brands in the world

Product Offering

Footwear (43% of 2016 Sales)



Leather Goods (37%)



Apparel (7%)



Accessories (6%)



Fragrances (6%)

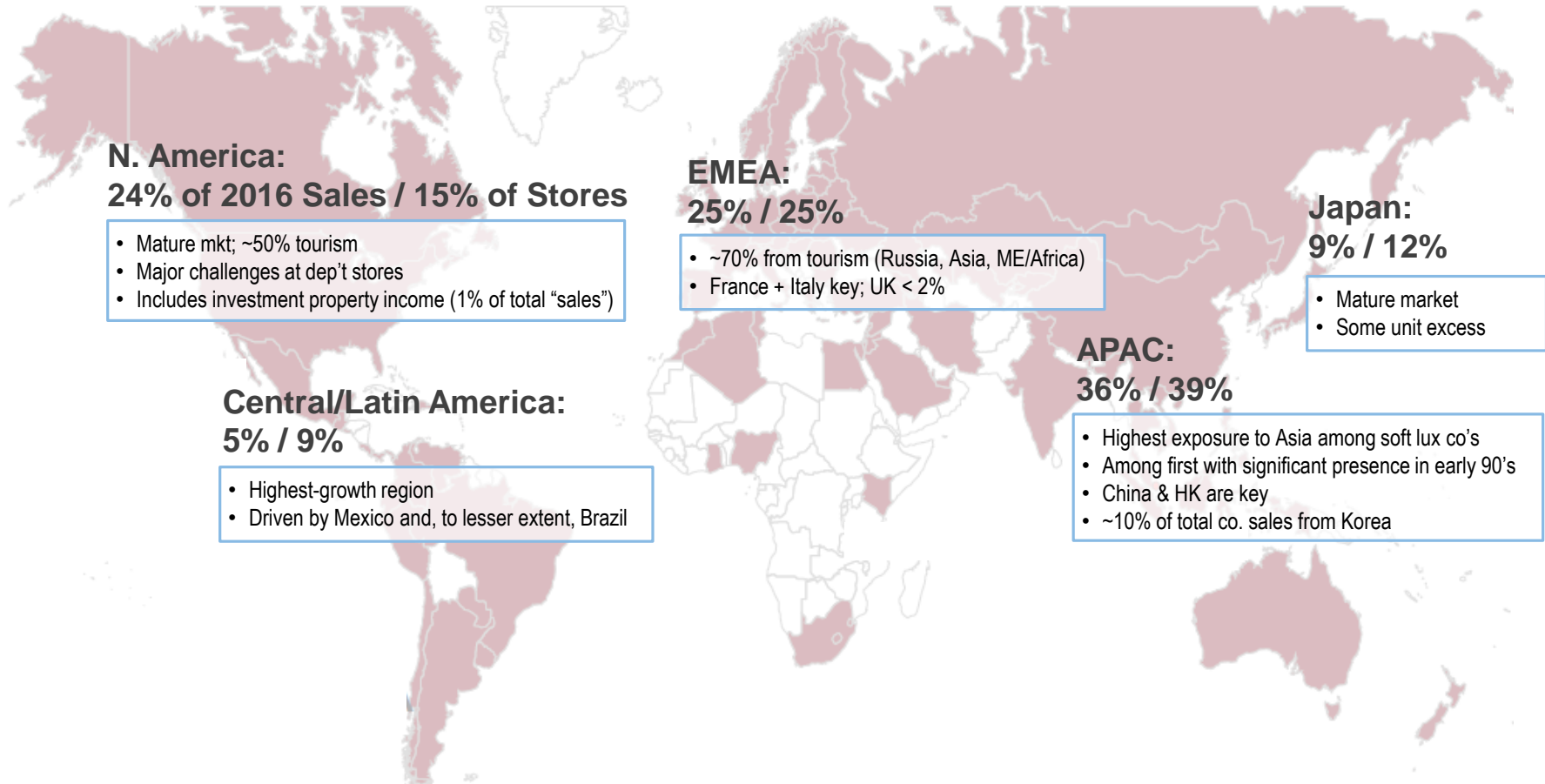


Licenses & Services (1%)



Ferragamo outsources the vast majority of its production processes, while keeping development, design, and quality control in-house

Emerging Market Consumers Account for >50% of Sales⁽¹⁾



~675 units in Ferragamo's store base; strong physical presence in Asia

Management Background

Key Executives

CEO – Eraldo Poletto

- In-role since: 2016 (August)
- Previously: CEO of Furla, a family-owned, Italy-based handbag business. Additional experience as sr. exec. and member of executive committee at Brooks Brothers International
- Prior CEO had been in-role for 10 years and was the first non-family member to lead Ferragamo

CFO – Ugo Giorcelli

- In-role since: 2017 (March)
- Previously: CFO of Amplifon, a €3 bn (MCAP) publicly-traded producer/provider of hearing aids

Chairman – Ferucci Ferragamo

- In-role since: 2006
- Eldest son of Salvatore Ferragamo
- Started working with the company in 1963; ultimately served as CEO from 1984 to 2006
- **CEO of family holdco that owns ~58% of shares**

Compensation Basics

- CEO base salary: €333,000
- Variable comp generally < 40% of total

Variable Comp Drivers

- 50% from total shareholder return (2016-2020)
- 50% from:
 - Sales growth
 - Distribution channel growth
 - Management conduct
 - Growth vs. peer benchmark

Additional Comments

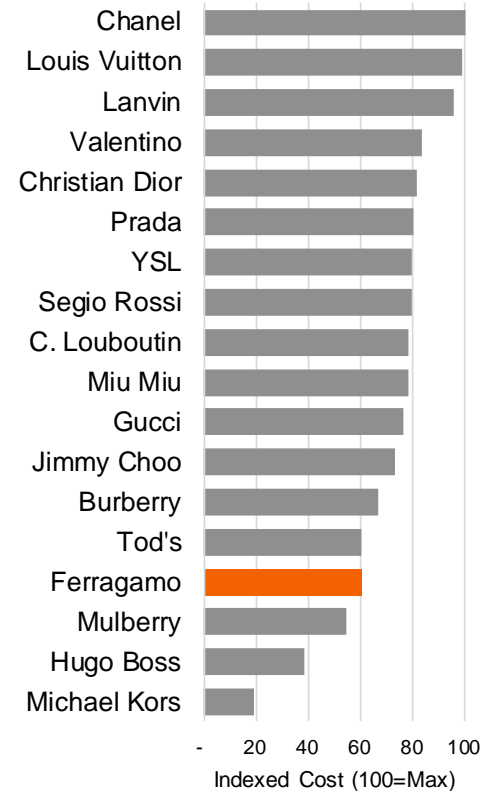
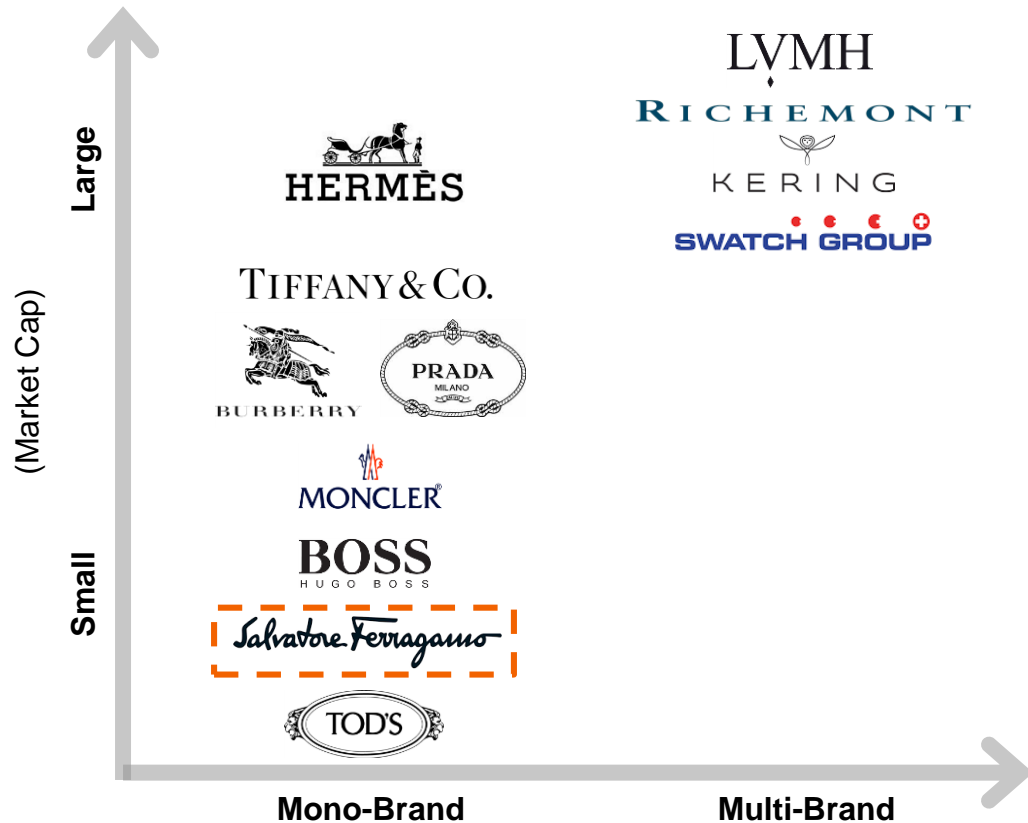
- We assess the executive comp structure as below average
- However, given dynamics of family-controlled business, we are less focused than usual on financial compensation metrics

Independent management team, family-controlled business
(which we generally consider a good thing)

Ferragamo Positioning: Global Luxury Brands

Corporate Structure/Size

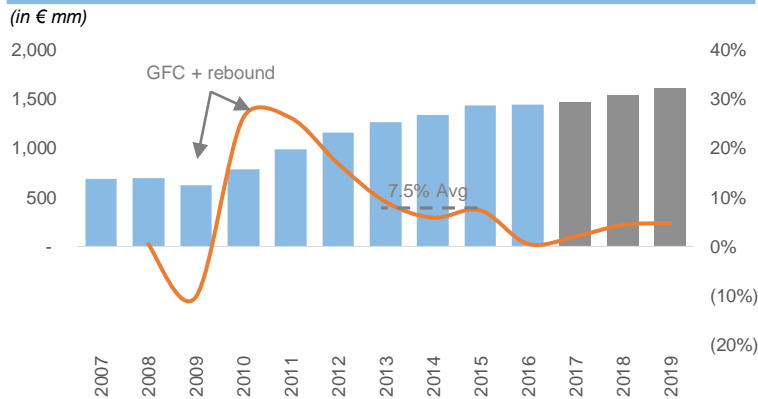
Product Position⁽¹⁾



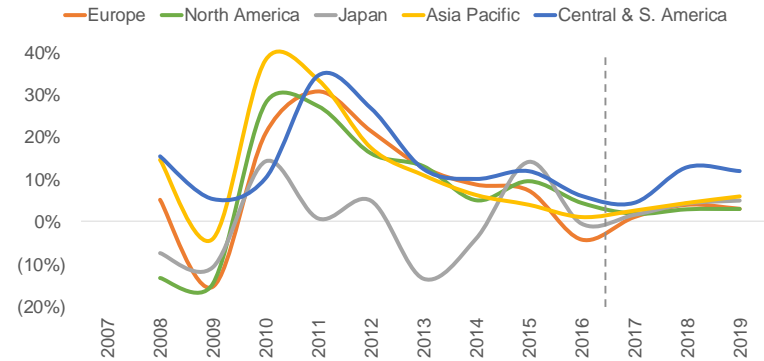
Ferragamo is a *relative* niche player, focused largely on “affordable luxury”

Financial History

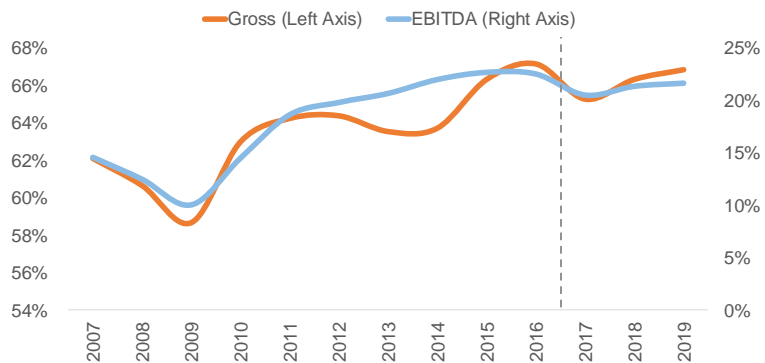
Revenue & Revenue Growth



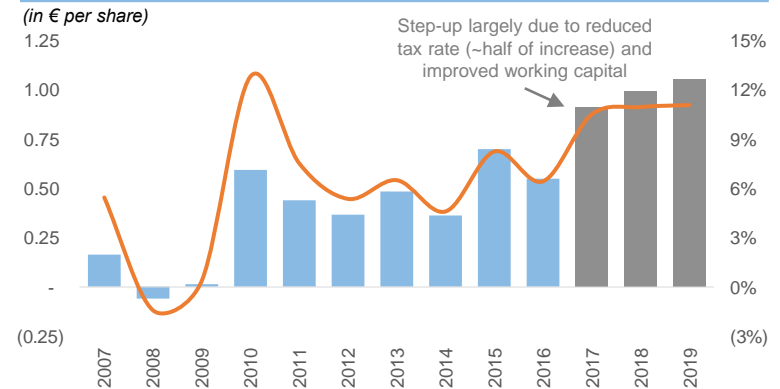
Revenue Growth by Region



Gross & EBITDA Margins



Free Cash Flow⁽¹⁾/Share & FCFE Margin

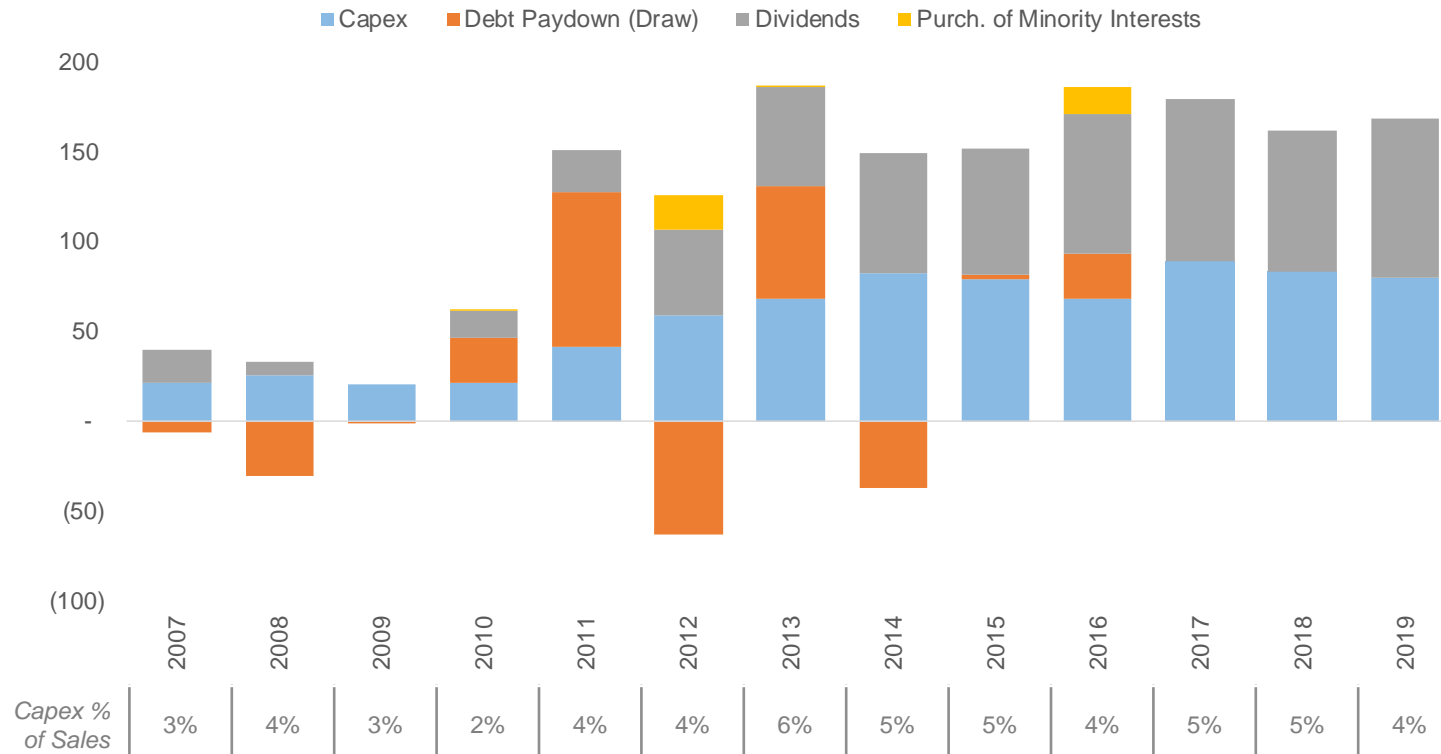


Strong margins and cash flow, despite recent soft top-line performance

Capital Allocation

Historical Allocation of FCFE

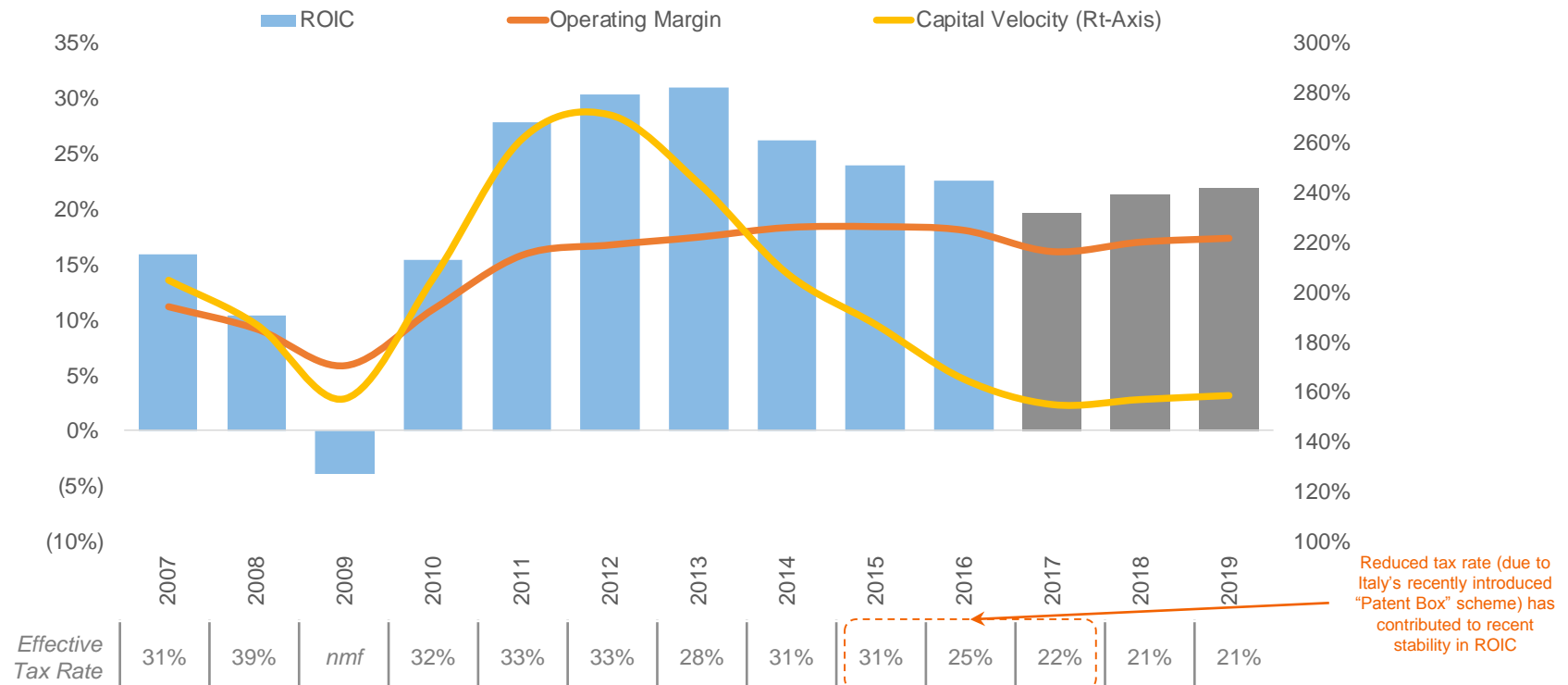
(in € mm)



Capital allocated largely to capex and a modest dividend

Capital Returns

ROIC Decomposition



With steady margin expansion and a recent tax boost, ROIC has generally been sustained > 20% post-crisis, despite sluggish top-line growth

Investment Thesis & Risks

Investment Thesis

1. Leading Global Luxury business, with Rich History and Durable Brand

- Family-owned (~70%) and controlled; strong oversight focused on long-term value
- Continues to be viewed by the fashion community as one of the top global luxury brands

2. Attractive Financial Profile

- LT revenue CAGR ('07-'16) of 9%, Adj EBITDA and FCF/Share CAGRs of 14% (both)
- Returns on capital > 20% since financial crisis, despite top-line headwinds and recent challenges

3. Strong, New Leadership Compelled to Action

- 2nd-ever independent management team (previous CEO/CFO “retired” after ~10 years in-role)
- CEO & CFO are accomplished operators, tasked with revitalizing the brand and improving retail unit performance
- New design leadership has received positive early marks; full roll-out from new team this Fall/Winter

4. Challenged Sentiment

- Stock underperformed peers by ~40% (LTM), in part due to challenges with U.S. wholesale (sharp comp declines)
- Sell-side uninterested in supporting the stock (few “Buy” ratings); 2017 widely viewed as “transition year” to avoid

5. Reasonable Valuation on Conservative Estimates + Levers to Pull

- Expectations for 2017/18 appear low, valuation is reasonable, and SFER has clear opportunities to revitalize the co.
- Management goals imply significant upside to LT estimates

Near-term challenges and uncertainty have created low expectations
for one of the top global luxury brands

Investment Risks

1. Ongoing Retail Challenges

- Severe challenges in wholesale (~35% of sales) could continue to pressure sales and margins
- Quickly evolving retail market (channel shifts, consumer preferences for brands/luxury) could challenge the brand

2. Unpredictable Fashion Trends + Execution Risk

- Fashion trends can change quickly, and we are not well-positioned to judge changes far in advance
- Although we are enthusiastic about the new design team, updating the brand's style poses a major risk

3. Foreign Exchange Risk

- Weakness in emerging market currencies (esp. China, Mexico) could create pricing challenges
- Generally maintains some FX hedges; but, challenging to analyze/forecast with precision

4. Geopolitical Risks

- N. Korean saber-rattling: significant exposure to Japan (9% of sales) and South Korea (est. 10% of sales)
- Global terrorism: > 1/3 of sales are from tourists (either en route or in foreign countries)

5. Other Risks

- Reduced disclosure: recently switched from quarterly to semi-annual reporting under new mgmt. team
- 'Unknowns' involving investment in Italy-based, family-controlled business (weaker information flow)

Biggest risk: can new leadership successfully revitalize the brand?

Model & Valuation

Model / Case Summary

	2017	2018	2019	2020	2021	2022	Forecast	'07-'16
Revenue Growth							<i>CAGR</i>	<i>CAGR</i>
Bull	3%	7%	8%	8%	7%	6%	7%	
Base	2%	4%	5%	5%	4%	3%	4%	9%
Bear	1%	(11%)	12%	2%	2%	2%	1%	
EBITDA Margins							<i>Avg</i>	<i>Avg</i>
Bull	21%	23%	24%	24%	25%	25%	24%	
Base	21%	21%	22%	21%	21%	21%	21%	18%
Bear	20%	17%	20%	20%	19%	19%	19%	
FCFE Margin							<i>Avg</i>	<i>Avg</i>
Bull	11%	11%	11%	12%	13%	14%	12%	
Base	11%	11%	11%	11%	11%	11%	11%	6%
Bear	10%	14%	6%	10%	10%	10%	10%	
ROIC							<i>Avg</i>	<i>Avg</i>
Bull	21%	24%	25%	26%	27%	28%	25%	
Base	20%	21%	22%	22%	22%	22%	21%	20%
Bear	19%	14%	20%	19%	18%	18%	18%	
EPS Growth							<i>CAGR</i>	<i>CAGR</i>
Bull	(9%)	21%	15%	11%	11%	9%	9%	
Base	(14%)	13%	8%	2%	4%	3%	2%	24%
Bear	(19%)	(30%)	47%	(1%)	(1%)	(1%)	(4%)	

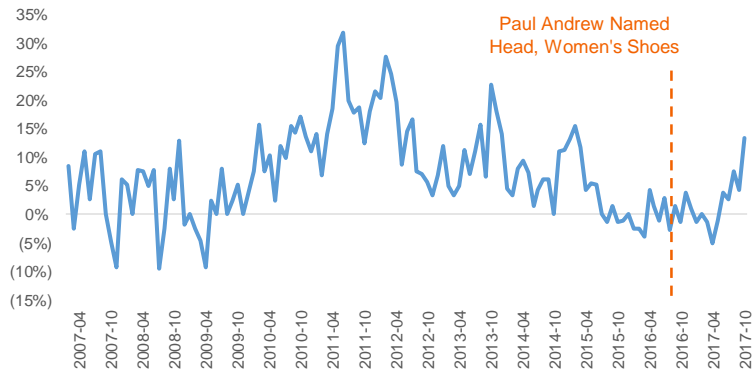
Model Notes

- **Base Case:** cont'd below-trend (hist.) top-line growth + steady margins
- **Bear Case:** 2018 recession followed by ST rebound and permanent impairment to top-line; stagnant margins
- **Bull Case:** top-line growth and margins in-line with management's LT targets (2x industry growth + operating leverage)
- Note: Historical ROIC ex-'08/'09 = 24%

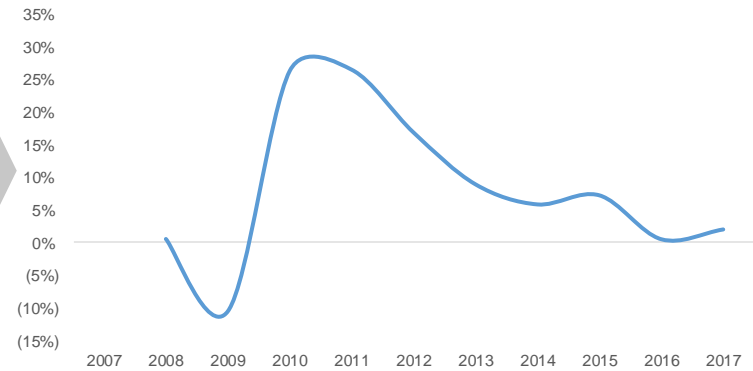
Base Case (~consensus) appears conservative, in our view

Why the Bull Case is Not Out of the Question: Green Shoots in Online Search Interest for “Ferragamo”

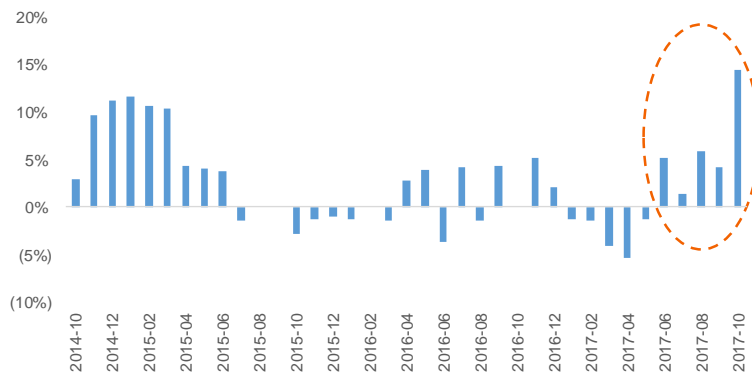
Y/Y Growth in Online Search Interest



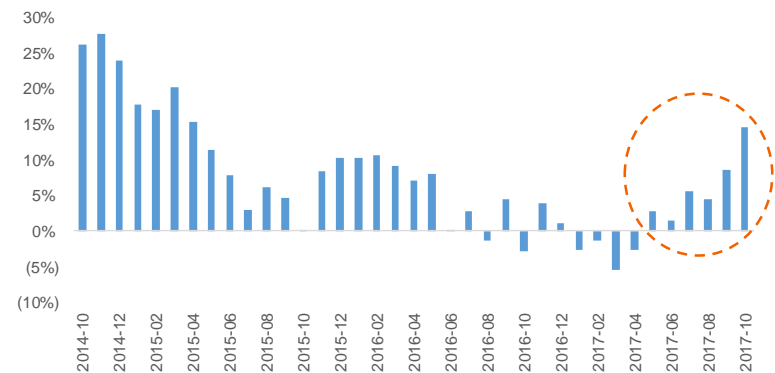
Product Sales Growth – Correlation?



L3Y - Y/Y Growth in Search Interest(1)



L3Y - 2Y Stack for Search Interest(1)



Given the nature of ‘fashion,’ online interest in the brand seems a noteworthy performance indicator

Valuation Detail (Base Case)

	Current Price	Target Price	DCF Valuation	Exp. Total Return
	€ 23.0	€ 30.0	€ 24.5	33%
FCFE Yield				(Key Metrics)
2017	4.0%	3.0%	3.7%	€ 154
2018	4.3	3.3	4.1	168
2019	4.6	3.5	4.3	178
2020	4.7	3.6	4.5	184
EV / EBITDA				
2017	12.7x	16.6x	13.5x	€ 301
2018	11.7	15.3	12.5	327
2019	11.0	14.4	11.7	347
2020	10.8	14.1	11.5	355
Price/Earnings				
2017	22.3x	29.1x	23.7x	€ 1.03
2018	19.7	25.8	21.0	1.16
2019	18.3	24.0	19.6	1.25
2020	18.1	23.6	19.2	1.27
				Data as of:
Diluted Shrs	168.8	168.8	168.8	2017 YE est.
MCAP	3,878	5,065	4,134	--
Net Debt	(58)	(58)	(58)	2017 YE est.
Pension	10			2016 YE act.
TEV	3,830	5,007	4,076	--
Dividend	0.54	0.54	0.54	2017 YE est.
Case:	Base			
Est. Source:	Model			

Price Target Rationale

- Takes into consideration Base Case, as well as Bull and Bear Cases
- Consider valuation on Base Case est's as reasonable, Bull Case as very attractive (reduces EBITDA and P/E mult's by > 1x and 2x)
- Under Bear Case, look to post-recession valuation – which also appears reasonable (not that we wouldn't expect significant ST drawdown)
- Luxury goods co's have historically traded at ~30% premium to global equity indexes (P/E)
- Historically⁽¹⁾, SFER has traded ~12x and 24x NTM EBITDA and EPS

Given Ferragamo's attractive financial model and the prospects for a "turn-around," we view current valuation as attractive

Comparable Companies

Fundamentals

Company	Dividend Yield	Net Lev. 2017	Revenue Growth			EBIT Margin			EBITDA Growth			Adj EPS Growth		
			2017	2018	2019	2017	2018	2019	2017	2018	2019	2017	2018	2019
Burberry Group Plc	2.6%	(1.3x)	0%	2%	5%	16%	18%	18%	5%	9%	7%	7%	12%	9%
Hugo Boss Ag	4.8%	0.1x	1%	3%	4%	12%	13%	13%	(5%)	5%	7%	(5%)	6%	10%
Jimmy Choo Plc	1.7%	1.7x	12%	7%	8%	12%	12%	12%	6%	11%	12%	88%	9%	13%
Kering Sa	2.2%	1.3x	20%	7%	7%	18%	18%	19%	33%	11%	10%	48%	14%	12%
Lvmh Moet Hennessy Louis Vuitton Se	2.5%	1.0x	11%	6%	6%	19%	20%	20%	10%	9%	7%	20%	10%	9%
Mulberry Group Plc	0.3%	(1.4x)	6%	4%	4%	4%	5%	6%	(1%)	11%	5%	(3%)	17%	4%
Tod'S S.P.A.	3.6%	(0.0x)	(3%)	3%	4%	12%	13%	13%	(21%)	5%	7%	(11%)	9%	10%
Compagnie Financiere Richemont Sa	2.6%	(2.3x)	12%	5%	6%	19%	20%	21%	21%	12%	9%	48%	13%	11%
Swatch Group Ltd. Bearer	2.1%	(0.8x)	3%	5%	5%	13%	15%	16%	16%	18%	12%	29%	26%	15%
Average	2.5%	(0.2x)	7%	5%	5%	14%	15%	15%	7%	10%	8%	24%	13%	10%
Median	2.5%	(0.0x)	6%	5%	5%	13%	15%	16%	6%	11%	7%	20%	12%	10%
Salvatore Ferragamo S.P.A.	2.3%	0.0x	1%	2%	4%	18%	16%	17%	(0%)	(7%)	9%	17%	(14%)	13%

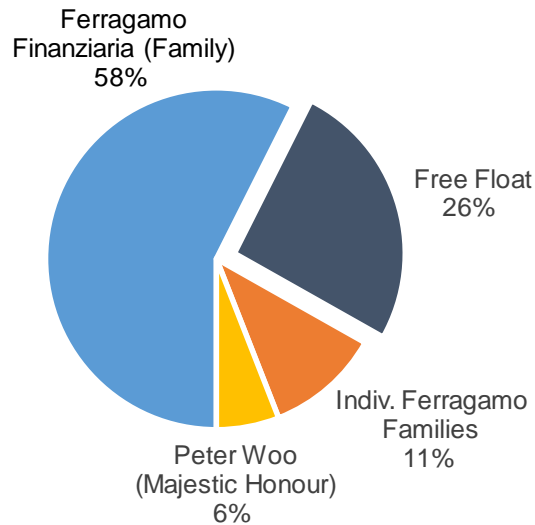
Valuation

Company	Price (Local)	TEV (\$US mm)	EV / Revenue			EV / EBITDA			FCFE Yield			P/E		
			2017	2018	2019	2017	2018	2019	2017	2018	2019	2017	2018	2019
Burberry Group Plc	18.43	\$9,598	2.5x	2.5x	2.4x	11.8x	10.8x	10.0x	4.4%	4.4%	5.4%	23.4x	20.9x	19.2x
Hugo Boss Ag	76.50	6,615	2.0x	2.0x	1.9x	11.1x	10.6x	9.9x	5.3%	5.3%	5.8%	21.3x	20.1x	18.3x
Jimmy Choo Plc	229.60	1,376	2.5x	2.3x	2.2x	14.5x	13.0x	11.7x	0.6%	0.7%	3.3%	25.2x	23.2x	20.5x
Kering Sa	352.00	59,165	3.3x	3.1x	2.9x	15.8x	14.2x	12.9x	1.9%	3.4%	3.9%	24.8x	21.8x	19.4x
Lvmh Moet Hennessy Louis Vuitton Se	237.40	150,279	3.0x	2.8x	2.7x	12.3x	11.3x	10.5x	3.1%	3.8%	4.1%	24.7x	22.4x	20.6x
Mulberry Group Plc	10.79	852	3.5x	3.4x	3.2x	33.0x	29.9x	28.5x	1.3%	1.0%	1.1%	105.8x	90.7x	87.0x
Tod'S S.P.A.	56.10	2,261	1.9x	1.9x	1.8x	11.3x	10.7x	10.0x	5.8%	5.0%	5.3%	23.3x	21.3x	19.3x
Compagnie Financiere Richemont Sa	89.05	41,508	3.2x	3.0x	2.8x	13.3x	11.9x	10.9x	3.7%	4.3%	4.8%	26.0x	23.0x	20.8x
Swatch Group Ltd. Bearer	400.60	21,552	2.7x	2.5x	2.4x	14.4x	12.3x	11.0x	3.5%	2.2%	3.9%	29.1x	23.1x	20.2x
Average			2.7x	2.6x	2.5x	15.3x	13.8x	12.8x	3.3%	3.4%	4.2%	33.7x	29.6x	27.3x
Median			2.7x	2.5x	2.4x	13.3x	11.9x	10.9x	3.5%	3.8%	4.1%	24.8x	22.4x	20.2x
Salvatore Ferragamo S.P.A.	22.97	4,571	2.6x	2.5x	2.4x	12.7x	11.7x	11.0x	4.0%	4.3%	4.6%	22.3x	19.7x	18.3x
Salvatore Ferragamo S.P.A. @ PT	30.00	5,976	3.4x	3.3x	3.1x	16.6x	15.3x	14.4x	3.0%	3.3%	3.5%	29.1x	25.8x	24.0x

SFER trades mostly in-line with peers – but on estimates that appear to reflect little prospect of a material ‘turn-around’

Ownership Structure

Ownership by Group



Note: Peter Woo (Majestic Honour is the entity he controls) is one of Ferragamo's key Chinese distribution partners and a Board Member

Top 20 Shareholders

	% of SFER	% of Port.
1 Allianz Global Investors GmbH – Frankfurt	1.4%	2.3%
2 OFI Global Asset Management, Inc.	1.4	0.4
3 European Value Partners	0.8	2.8
4 AXA Investment Managers Paris	0.9	1.1
5 Fidelity (FIL Fund Management Limited)	0.7	1.9
6 Threadneedle Asset Management Limited	0.6	0.6
7 Azimut Capital Management SGR S.p.A.	0.7	1.4
8 Vanguard Group Inc	0.6	0.0
9 Edmond de Rothschild Asset Management (F	0.6	2.5
10 Robeco Institutional Asset Mgmt BV	0.4	1.4
11 Wellington Management Company LLP	0.4	0.6
12 Juno Investment Partners	0.3	8.2
13 Anima Sgr S.p.A	0.3	1.0
14 March Gestión de Fondos SGIC	0.3	1.2
15 Kairos Partners SGR SpA	0.3	1.3
16 HSBC Global Asset Management (France)	0.3	1.6
17 Dimensional Fund Advisors LP	0.3	0.0
18 La Financière de l'Echiquier	0.2	2.5
19 Pioneer Investment Management SGRpA	0.2	0.2
20 William Blair Investment Mgmt	0.2	0.2

The Ferragamo family still controls a majority of shares;
we view them as a positive influence

Conclusion

Closing Thoughts

Signs that Ferragamo is out of favor?

- ✗ Widespread fear of retail (especially brick-and-mortar)
- ✗ Major share price underperformance over LTM
- ✗ Consensus writing off 2017 as “transition year” to avoid

Why we like Ferragamo:

- ✓ Valuable, durable brand that has become temporarily out of favor
- ✓ Family-owned business with fresh, accomplished executive and design leadership
- ✓ Low expectations + significant levers to pull at both the product and retail levels
- ✓ Reasonable valuation on achievable consensus estimates

Should Ferragamo’s new leadership start gaining traction, it’s not hard to envision SFER quickly being viewed as a “Gucci Turnaround 2.0” story

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