fashionette

Retail

29 October 2020

Growth is in fashion

fashionette aims to become the leading data-driven online platform for premium and luxury fashion accessories across Europe, replicating its success in Germany. Management expects revenue growth to exceed market growth (Statista forecast of 17% pa in 2020–23) as its geographic coverage and product offer is enhanced via a combination of organic and inorganic growth. In the near term, revenue growth could exceed profit growth as the company invests in building a strong customer base across more countries.

Data-driven online platforms

fashionette is a leading online platform that offers premium and luxury fashion accessories, with a strong representation in the DACH region. Management believes its key competitive advantage is its internally developed IT platforms and use of data that enable the majority of business functions and processes to be data driven. This, along with a broad portfolio of products and luxury brands that is likely to increase, gives management confidence that it can exceed wider market growth rates as it diversifies away from the DACH region.

Sales growth to lead profit growth

fashionette has grown its revenue at a CAGR of 11.6% in FY17–19, while expanding its EBITDA margin from 6.0% to 9.3%, which is towards the top end of other consumer-facing platforms. The new management's increased focus on data and expanding the product range has led to an acceleration in revenue growth in 9M20 (+24% y-o-y) driven by new customer growth, which compares favourably with the overall luxury goods market. As the company expands across Europe and builds its customer base, its EBITDA margin is likely to reduce over the next few years as it develops its customer base and the lifetime value of those customers.

Valuation: Strong growth expected

Consensus forecasts are not yet available. With few direct listed peers, we compare fashionette's valuation to a range of online and offline retailers of luxury and non-luxury goods as well as luxury goods companies. On FY19 sales, fashionette's EV/sales multiple of 2.2x is at a discount to the average for both groups of peers, 2.8x and 4.9x, respectively. The retailers enjoyed higher revenue growth on average than fashionette, but its sales have accelerated in FY20. Its EV/(FY19 EBITDA) of 23.3x is at a 19% discount to the average multiple for the retailers (28.7x), but a 44% premium to the average for luxury goods (16.2x).

Historical financials

Year end	Revenue (€m)	PBT (€m)	EPS (€)	DPS (€)	P/E (x)	Yield (%)
12/16	0.0	(0.0)	N/A	0.0	N/A	N/A
12/17	58.8	0.3	N/A	0.0	N/A	N/A
12/18	65.2	1.2	N/A	0.0	N/A	N/A
12/19	73.2	2.8	N/A	0.0	N/A	N/A

Source: fashionette

Price €31

Market cap €192m

Share details

Code	FSNT
Listing	Deutsche Börse Scale
Shares in issue	6.2m
Last reported net debt at 30 June 2020 (before IPO)	€3m
Pro forma net cash at 30 June 2020 (includes €37m primary IPO proceeds)	€34m

Business description

fashionette is an online platform for premium and luxury fashion accessories in Europe, with websites live in eight European countries. Geographically, the DACH region is its core, representing c 89% of revenue in FY19. It is seeking to diversify by geography and product offering.

Bull

- Broad product and luxury brand offer.
- Fragmented markets with strong growth outlook.
- Data-driven processes expected to optimise the cost of acquisition and lifetime value of customers.

Bear

- Premium and luxury demand is sensitive to economic growth.
- fashionette brand name is less well known across new geographies that are targeted for growth.
- Profit growth may lag revenue as it invests to acquire market share in new geographies.

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Edison profile page

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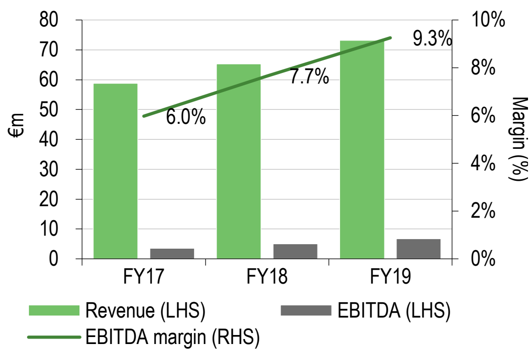
Company description: Online luxury fashion accessories

fashionette is an online platform for the sale of premium and luxury fashion accessories, predominantly handbags, shoes, sunglasses, watches and jewellery to consumers. The majority of its revenue (c 89% in FY19) is generated in the DACH region, but the company has ambitions to replicate its success across other major European economies, and to increase its product offer. Its aim is to become the leading European data-driven online platform for premium and luxury fashion accessories. Management is confident that its revenue growth will outperform estimates for growth in the online luxury market in FY20–23 of 17% pa (source: Statista).

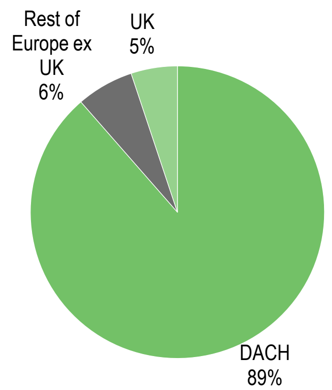
The company was founded in Düsseldorf in 2008 and registered under the name Luxury Fashion Trade GmbH. The website was relaunched in 2010 with a focus on handbags in Germany. In 2015, the business angels and venture capitalists exited as GENUI, a private firm that invests in medium-sized companies, bought into the company. As revenue grew, the shareholders continued to invest in the business's technology and processes. In April 2019, the current CEO, Daniel Raab and COO/CTO, Thomas Buhl, joined fashionette with a mandate to drive the next phase of the company's expansion, both organic and inorganic. Having grown revenue at CAGR of 11.6% in FY17–19, the impact of the new management team and the investment in IT and processes is clear, as revenue growth accelerated to c 24% for the first nine months of FY20 (9M20). The company had an average of 137 employees during H120.

Exhibit 1: fashionette's financial history



Source: fashionette

Exhibit 2: FY19 revenue by region



Source: fashionette

fashionette listed on the Scale segment of the Deutsche Börse on 29 October 2020. In total 3,605,000 shares were placed at a price of €31/share versus the offered price range of €30–38, representing gross proceeds of c €111.8m, and gross primary proceeds to the company of €37.2m. Within 6.2m shares in issue post IPO, the free float is 58% and fashionette's market value is €192m. Assuming the greenshoe option is issued, GENUI will hold 37% and management will hold 5% of the total outstanding shares.

Prior to IPO, management indicated the proceeds will be invested as follows: M&A €17m; international marketing €17m; and internal investments €4m.

Broad geographic coverage and product offer…

When founded, the company focused on the selling of premium and luxury handbags in Germany. Over time, fashionette has increased its geographic coverage and its product range to include shoes, sunglasses, watches, jewellery and gifts for men. In H120, fashionette's order value mix by category was: handbags 60%, shoes 24%, sunglasses 6%, small leather goods 4% and other 6%.

According to fashionette's data, over 80% of its customer base is female, 70% are below the age of 50, and more than 75% have a net disposable income of more than €2k per month, which supports its high average order value of €284 in H120.

At present, the company has websites live under the fashionette domain name in eight European countries (Germany, Austria, Switzerland, France, Italy, the Netherlands, Sweden and the UK) as well as the fashionette.com domain name.

fashionette offers products from over 150 international brands including, Burberry, Chloé, Gucci, Jimmy Choo, Max Mara, Ray-Ban, Tiffany & Co, Versace and Victoria Beckham. We believe that typically the company has immediate access to new ranges from the luxury brand owners. It also offers a private label range of lower-priced products, mostly in the jewellery category.

The number of products available per country varies due to the stage of development of fashionette in that country, the tailoring of the product offer to the country's taste, as well as distribution restrictions by the brand owners. As shown in Exhibit 3, the number of products available per country ranges from 12,318 in France to 14,177 in Germany. The proportion of products that are being discounted, ie 'sale' items, is typically 47–48% in most countries with a slightly higher proportion of c 51% in Switzerland. The relatively low revenue earned in countries outside the DACH region given relatively similar numbers of products on offer highlights the company's potential in these new markets as it seeks to diversify outside of the DACH region.

Exhibit 3: Number of products available per country

	Austria	France	Germany	Italy	Netherlands	Sweden	Switzerland	UK
Handbags	4,884	4,117	4,886	4,262	4,855	4,825	4,681	4,590
Shoes	2,537	2,071	2,539	2,077	2,515	2,516	2,478	2,384
Accessories	3,150	2,733	3,150	2,813	3,143	3,129	3,044	3,015
Jewellery & watches	2,403	2,321	2,403	2,321	2,325	2,285	1,287	2,200
Gifts for men	1,199	1,076	1,199	1,064	1,196	1,189	1,101	1,109
Total products	14,173	12,318	14,177	12,537	14,034	13,944	12,591	13,298
'Sale' items	6,776	5,926	6,780	6,079	6,720	6,672	6,381	6,303
'Sale' items % of total	47.8%	48.1%	47.8%	48.5%	47.9%	47.8%	50.7%	47.4%

Source: fashionette websites, Edison Investment Research

Exhibit 4 shows the prices of a very small sample of its products across the company's websites in each country.

Exhibit 4: Sample of product prices by country

Product	Austria (€)	France (€)	Germany (€)	Italy (€)	Netherlands (€)	Sweden (SEK)	Switzerland (CHF)	UK (£)	Implied SEK/€	Implied CHF/€	Implied £/€
Burberry Mini Camera Bag Vintage Check Archive	726	726	726	726	726	8,059	842	Not for sale	11.1	1.16	N/A
Chloé Marcie Round Small Bag Cashmere Grey	765	Not for sale	765	765	765	8,492	887	680.9	11.1	1.16	0.89
Valentino Rockstud Camera Crossbody Bag Grained Poudre	920	920	920	Not for sale	920	10,212	1,067	818.8	11.1	1.16	0.89
Prada Slingback Pumps Leather Black	629	629	629	Not for sale	629	6,982	730	559.8	11.1	1.16	0.89
Gucci Sunglasses Man Acetate Havana	237	Not for sale	237	Not for sale	237	2,361	275	210.9	10.0	1.16	0.89

Source: fashionette websites, Edison Investment Research

We can see that pricing in the euro-denominated countries is uniform.

...with pioneering data-driven processes…

Management believes that its key competitive advantages are its internally developed IT platforms and use of data that enable the majority of business functions and processes to be data-driven, which minimises the potential for human error in a traditionally emotion-based industry. The data and processes enable it to analyse competitors' product offerings and pricing, its own customers' past behaviour and creditworthiness in order to forecast future customer behaviour, adjust the product offer and pricing accordingly, to allocate marketing spend more effectively, while ensuring the optimisation of fulfilment and working capital control.

fashionette offers many payment options including the offer of credit and payment by instalments. Debts are factored immediately. The existing factoring contracts with RatePAY and BFS finance run until August 2021 and February 2021, respectively. fashionette's loss on receivables expense has reduced from €553k in FY17 (0.9% of revenue) to €226k in FY19 (0.3% of revenue), which highlights the success it has had following investment in helping to better identify the creditworthiness of potential customers.

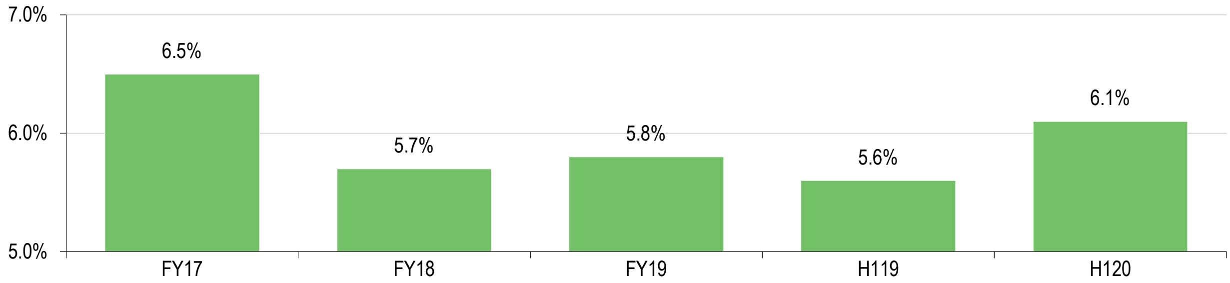
…and outsourced fulfilment and distribution…

Since 2016, fashionette has had a comprehensive fulfilment agreement with BFS Baur Fulfillment Solutions, under which BFS provides all logistic services, ie the receipt and storage of inventory, and the picking and packing for customer orders. This agreement will end in September 2021. In October 2020, fashionette entered into a new fulfilment contract to provide the same services with a new provider, ITG GmbH Internationale Spedition und Logistik, due to commence in Q221.

Distribution to end customers is performed by third-party logistics companies including DHL in Germany and UPS in the UK.

Management claims that its fulfilment operations are highly efficient compared to its peers.

Exhibit 5: Fulfilment cost as percentage of order value



Source: fashionette

…has delivered high brand recognition and customer satisfaction

According to the prospectus, fashionette has a high customer satisfaction level, scoring 4.8/5.0 on Trustpilot and Trusted Shops and a Net Promoter Score of 70%.

Strategy: Replicate success beyond the DACH region

Management's aim is to build fashionette into the leading online platform for premium and luxury fashion accessories in Europe. The markets are fragmented and expected to deliver high rates of growth. In order to achieve this management plans to:

- Expand geographically, where it is less well known, reducing its dependence on the DACH region, and effectively trying to replicate its success in Germany. In H120, fashionette's order value by country was: Germany 81%, Austria 7%, the Netherlands 4%, the United Kingdom 4% and Switzerland 3%. The primary area that is targeted for expansion is the Benelux region and then France and the United Kingdom. The United Kingdom is less of an immediate focus given the ongoing negotiations around Brexit.
- Increase the product categories available through the platform. From a sole original focus on handbags, the categories on offer have gradually been extended to include footwear, accessories such as wallets, scarves, gloves and sunglasses, and jewellery and watches. Potential new categories include beauty and care products.
- Extend the number of products available in existing categories on offer, notably sunglasses, jewellery and small leather goods.

To be driven by organic and inorganic growth

The growth ambitions are to be achieved by a combination of organic and inorganic growth. With respect to M&A, management has indicated that c €17m of the IPO proceeds (total proceeds of €37m) will be allocated to acquisitions. It has indicated that 54 potential acquisition targets have been identified, of which 20 have been contacted. From the 20 companies that have been contacted, seven have revenue of less than €10m pa, and 13 have revenue of more than €10m, which suggests a wide range of potential acquisition multiples given the money that has been allocated to M&A.

Management's acquisition strategy is as follows:

- Acquire majority stakes
- Acquire companies:
  - in existing and adjacent product categories,
  - with proven growth potential,
  - that are EBITDA positive, and
  - with revenue and cost synergies.
- Acquisitions should be mainly cash funded

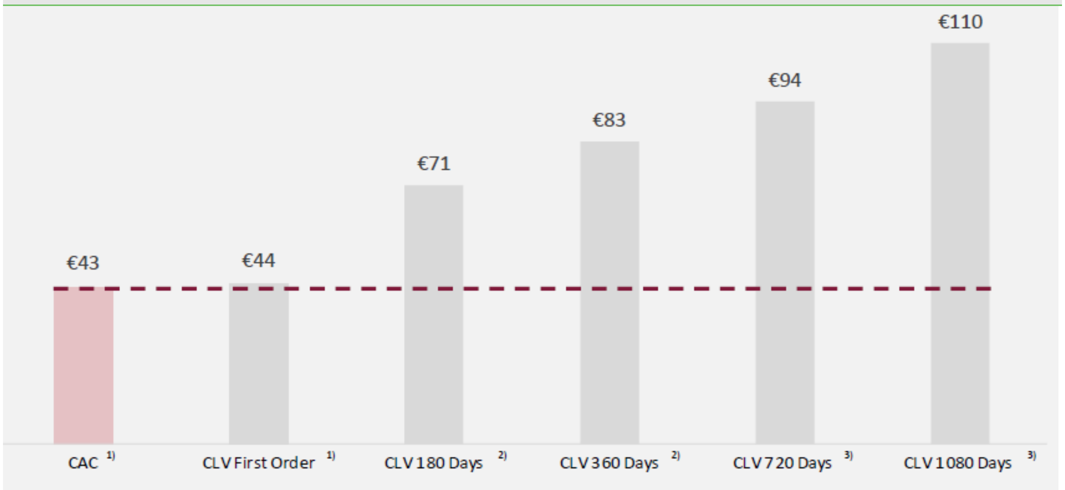
Core KPIs

As management executes on the above strategy, it is less concerned about profit margins in the near term, and will have a greater focus on key performance indicators (KPIs) including the numbers of active and new customers, average order value (AOV), customer acquisition cost (CAC) and customer lifetime value (CLV) as it grows market share outside DACH. Other KPIs include site visits, mobile share of site visits, number of orders, order value, marketing cost ratio and fulfilment cost ratio.

Management believes that the extension of the product range and into new categories, as well as continuous improvements in the way data helps the decision making will increase the AOV.

Exhibit 6 highlights how the CLV of cohorts from 2017–20 have evolved versus the initial CAC.

Exhibit 6: fashionette's customer acquisition cost (CAC) vs customer lifetime value (CLV)



Source: fashionette. Note: 1) 2020 cohort; 2) 2019 cohort; 3)2017 cohort; all trailing six months June.

Recent newsflow and upcoming catalysts

fashionette's revenue growth has accelerated in FY20, as the benefits of management's focus on the use of data, as well as the increasing product offer have come through, and despite the disruption caused by COVID-19.

Following revenue growth of 11% in FY18 and 12.1% in FY19, year-on-year revenue growth in H120 increased to 19.2% as the number of orders increased by 30% to 243k, and the number of new customers increased by 36%, the lower implied AOV and spend per customer reflects the maturity profile. For 9M20 revenue growth accelerated further to 24%, implying growth in Q320 of c 32%, as new customer growth continued to show good momentum.

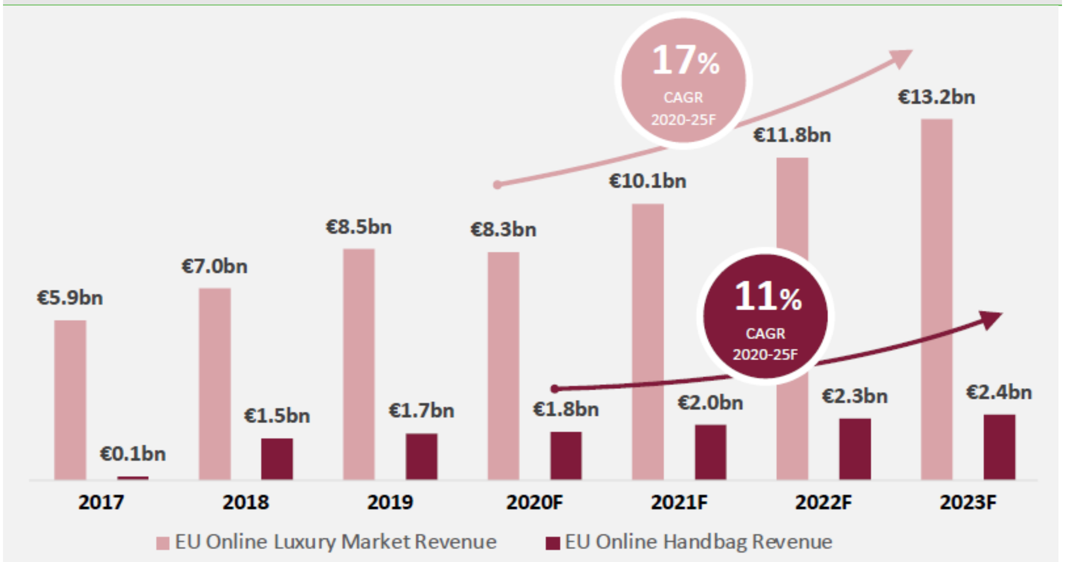
The outbreak of COVID-19 led to some minor supply disruption, most from Italy. However, new/more stock keeping units (SKUs) added in April and an increase in marketing spend led to the reported strong revenue growth.

Management has a positive outlook for the remainder of FY20 and FY21 given the ongoing move to online and the expectation of continued growth in new customers.

Market overview

The long-term growth of demand for luxury goods has been influenced by several factors including economic growth and affluence, consumer aspiration and travel, distribution, marketing, entry-level price points, and the emergence of new product categories.

Exhibit 7: EU premium and luxury market revenue growth forecast



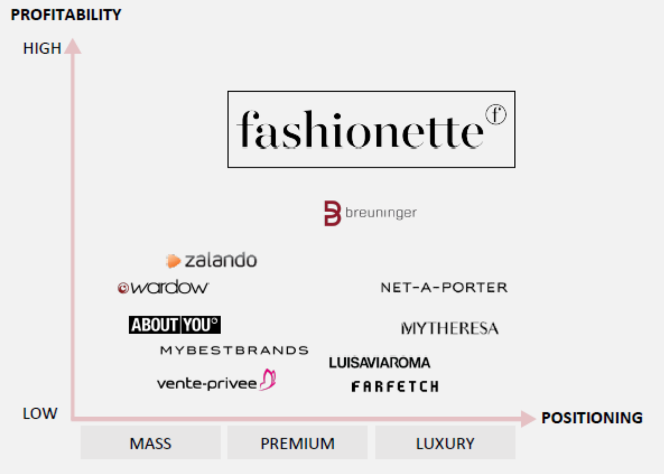
Source: Statista July 2020, fashionette presentation

The key markets to which fashionette is exposed are the European online luxury and handbag markets. Per Statista, at €8.5bn and €1.7bn respectively in 2019, the estimated compound annual growth rates (CAGRs) for these markets in 2020–23 are 17% and 11%, respectively. The total European luxury goods market was estimated to be worth €86.4bn in 2019, therefore online penetration of 9.8% is low relative to other retail categories. The online premium and luxury markets are expected to grow at a higher rate than the total offline and online markets due to demographic changes and the increasing acceptance of technology, albeit parts of the total market are likely to be less suitable to increasing online penetration.

Management is confident that fashionette's long-term revenue growth will exceed the estimated market growth rates given its strategy to grow geographically, the expansion of the existing product offer and into new products categories, and its ability to increase market share given the strength of its technology, data, insights and processes.

Statista estimates that both markets will decline in 2020 due to the economic and social impacts of COVID-19. The company's year-on-year revenue growth of 24% in 9M20 looks impressive in the context of the wider market declines, and is supportive of management's aspiration to exceed market growth rates. During H120, fashionette enjoyed an increase in the number of active customers (23.0%) and the number of orders (29.9%), offset by a decline in the AOV (-10.3%).

Exhibit 8: fashionette's position in the premium and luxury fashion accessories market



Source: fashionette

fashionette's competitors include a wide range of online and offline retailers and marketplaces, with varying levels of overlap with the company's product offer and specialisations, as well as the luxury brand owners' own online and offline distribution. The competitors are general e-commerce retailers (eg Amazon, Boozt); fast fashion retailers and market places (eg Asos, Boohoo and Zalando); premium/luxury e-commerce retailers and marketplaces (eg Yoox Net-a-Porter, MyTheresa and Farfetch); offline retailers (ie department stores); and other online players with a more limited offer (eg Wardow and Edel Optics).

Management believes that fashionette is well positioned versus its competitors as its suppliers, ie the brand owners, are protective of how their products are distributed; it offers a wide range of brands (150) versus its competitors; and it is solely focused on segments of the luxury/premium markets.

Management

Management board

The management board consists of two directors:

- **CEO Daniel Raab**. Mr Raab joined fashionette in 2019 and is responsible for strategy, category management, finance, brand marketing and human resources. His previous roles include senior management positons in retail/e-commerce (Amazon) and media (ProSiebenSat1), and he has extensive expertise in the fashion and accessories markets (Gucci and Hermès). Before the IPO, Mr Raab's shareholding was c 3.4% of the company.
- **COO/CTO Thomas Buhl.** Mr Buhl is responsible for operations, performance marketing, business intelligence, product management and IT. His previous roles include senior leadership positons in e-commerce with Amazon and Karstadt, and as a consultant to Cyberport. Mr Buhl's pre-IPO shareholding was 2.3% of the company.

Supervisory board

The supervisory board consists of five directors:

- **Chairman Dr Oliver Serg.** Dr. Serg is the founder and managing partner of GENUI, the investment company that owned 94.3% of fashionette pre IPO.

- **Deputy Chairman Stefan Schütze.** Mr Schütze is also currently a member of the board of Finlab as well as having mandates at Patriarch MultiManager, Coreo, Cyan, TubeSolar and Kapilendo.
- **Karoline Huber**
- **Christian van der Bosch**
- **Rolf Sigmund**

Shareholders and free float

In total 3,605,000 shares were placed at a price of €31/share versus the offered price range of €30–38, representing gross proceeds of c €111.8m, and gross primary proceeds to the company of €37.2m.

The source of the IPO shares was as follows:

Exhibit 9: Source of IPO shares

	Shares	Price (€)	Gross proceeds (€m)
Primary capital increase	1,200,000	31	37.2
Secondary issue	1,500,000	31	46.5
Upsize option	500,000	31	15.5
Greenshoe	405,000	31	12.6
Total	3,605,000	31	111.8

Source: fashionette

With 6.2m shares in issue post IPO, the free float is 58% and fashionette's market value is €192m. Assuming the greenshoe option is issued, GENUI will hold 37% and management will hold 5% of the total outstanding shares.

Prior to the IPO, management indicated the net proceeds of the IPO will be invested as follows: M&A (€17m); international marketing (€17m) and internal IT investment (€4m).

Financials

We note that fashionette reports under German GAAP rather than IFRS and include summary financial statements without forecasts below.

Income statement

In Exhibit 10 we show a summary of fashionette's income statement for FY17–19, and for the progress it made in H120 versus H119. Note that we exclude FY16 from the summary as the company was in its infancy, generating revenue of €80k and EBITDA of less than €2k.

Exhibit 10: Summary income statement and KPIs

€m	FY17	FY18	H119	H219	FY19	H120
Total revenue	101.0	115.9	60.9	67.8	128.7	70.7
Growth y-o-y (%)		14.8%			11.0%	16.1%
Less credit notes	(42.2)	(50.7)	(28.0)	(27.5)	(55.5)	(31.6)
As % of total revenue	41.8%	43.7%	46.0%	40.6%	43.2%	44.6%
Revenue	58.8	65.2	32.8	40.3	73.2	39.1
Growth y-o-y (%)		11.0%			12.1%	19.2%
Cost of sales	(34.1)	(38.0)	(19.4)	(23.9)	(43.3)	(23.9)
Other operating income	0.6	1.0	0.3	0.8	1.1	0.4
Gross profit	25.2	28.3	13.7	17.2	31.0	15.7
Gross margin	42.9%	43.3%	41.8%	42.7%	42.3%	40.0%
Personnel expenses	(4.9)	(5.7)	(3.3)	(3.3)	(6.7)	(3.4)
Other operating expenses	(16.8)	(17.5)	(7.9)	(9.6)	(17.5)	(9.4)
EBITDA	3.5	5.0	2.5	4.3	6.8	2.8
EBITDA Margin	6.0%	7.7%	7.5%	10.7%	9.3%	7.3%
Depreciation and amortisation	(1.9)	(2.4)	(1.2)	(1.3)	(2.5)	(1.2)
Operating profit	1.6	2.6	1.2	3.0	4.3	1.6
Operating margin	2.7%	4.0%	3.8%	7.5%	5.8%	4.1%
Net interest	(1.3)	(1.4)	(0.7)	(0.8)	(1.5)	(0.8)
PBT	0.3	1.2	0.5	2.3	2.8	0.8
Income tax	(0.6)	(0.9)	(0.4)	(1.0)	(1.4)	(0.5)
Other taxes	(0.0)	0.0	0.0	0.0	(0.0)	0.0
Net income	(0.3)	0.3	0.1	1.3	1.4	0.3
Net margin	(0.5%)	0.5%	0.3%	3.2%	1.9%	0.9%
KPIs:						
New customers	157.8	139.0	62.8	84.3	147.1	85.3
Growth y-o-y (%)		(11.9%)			5.8%	35.8%
Active customers ('000) (last 12 months)	216.4	214.0	219.8		238.5	270.3
Growth y-o-y (%)		(1.1%)			11.4%	23.0%
Average order value (€)	273.6	309.0	317.0		306.3	284.2
Growth y-o-y (%)		12.8%			(0.9%)	(10.3%)
Number of orders ('000)	366	379	187	231	418	243
Growth y-o-y (%)		3.6%			10.3%	29.9%
Customer Acquisition Cost (CAC) (€)	51.3	58.2	54.3		52.0	42.7
Growth y-o-y (%)		13.5%			(10.7%)	(21.4%)
Marketing cost ratio (% of AOV)	8.1	6.9	5.8		6.0	5.3
Fulfilment cost ration (% of AOV)	6.5	5.7	5.6		5.8	6.1

Source: fashionette

fahionette has generated strong organic growth, as revenue increased from €58.8m in FY17 to €73.2m in FY19, with year-on-year growth rates of 11% in FY18 and 12.1% in FY19. Its EBITDA has grown from €3.5m in FY17 to €6.8m in FY19, and the EBITDA margin has increased from 6.0% in FY17 to 9.3% in FY19. A reduction in the gross margin (due to mix) has been offset by a relative improvement in the ratio of other operating costs to revenue (mainly advertising), while investing in staff and infrastructure to facilitate future growth.

In the first six months of H120, revenue growth accelerated to 19.2% to €39.1m but the gross margin fell by 180bp to 39.0% and the EBITDA margin declined by 20bp y-o-y to 7.3% as fulfilment costs increased on a relative basis. The majority, ie 89%, of fashionette's revenue was earned in the DACH region in FY19, but we expect this relative contribution will diminish over time as management focuses on growing in the rest of Europe, with its initial focus being on the Netherlands.

Revenue: Mid/high teens growth since FY17

fashionette reports two figures for revenue: total revenue is the value of goods that are shipped to customers, and revenue is the 'net' revenue retained after accounting for products that are returned by customers (referred to as credit notes by the company). Credit notes as a percentage of total revenue has ranged from a low of 40.6% in H219 to a high of 46.0% in H119: ie almost half of all products shipped to customers are returned to the company. The level of returns is predominantly driven by the mix of products that are sold. For example, a customer who wishes to buy sunglasses is more likely to order multiple pairs to try at home before making a final decision on which to keep and which to return, but a customer who buys other accessories, such as a handbag or scarf, is more likely to order fewer items and therefore not return as many items. The level of returns does not present a significant risk to the company's gross margin as more than 99% of items that are returned are ultimately resold.

The company's pricing strategy is, typically, not to discount aggressively versus its competition, but to follow price reductions quickly, helped by its in-house technology that closely monitors competitor activity. As shown earlier in Exhibit 4, pricing tends to be quite uniform across the individual countries

Management expects to generate higher revenue growth than the market growth rate of 17%, as online penetration of the respective markets will increase.

Gross margin: Driven by revenue mix

In Exhibit 10, we highlight the gross profit and gross margin, which includes cost of sales as well as other operating income. The latter includes foreign currency translation and credit notes from suppliers that are received as unsold inventory ages. Other operating income has averaged c 1–2% of revenue during this period, and at €1.1m in FY19, of which €214.6k was income from currency translation, it represented an important contribution to fashionette's EBITDA of €6.8m.

The most important driver of gross profit is the sales mix, as the gross margins on products vary from the low 30s (eg entry-level items and sunglasses, which is a competitive market) to the low 60s (for own brand products and fragrancies). On a full year basis, the gross margin has been relatively stable at c 42–43% but there is some seasonality: the first six months being lower than the second six months of the year, and gross margin declined by 180bp from H119 to 40% in H120. The gross margin does not represent a significant KPI for management, who have a greater initial focus on driving scale and CLV.

Unlike many of its online peers, markdown risk to the gross margin is very limited given the nature of the products, which are typically not seasonal.

With a high range of brands on offer, supplier concentration is low, with just one (unnamed) brand representing more than 10% of cost of sales. The company considers every brand to be a single supplier, such that the larger quoted luxury goods companies that own multiple brands, eg Kering, would increase the apparent supplier concentration albeit there is no group buying across the brands.

The majority of fashionette's cost of sales are sourced in euros, with a small percentage sourced in Swiss francs. As a result, there is limited foreign currency transaction and translation risk.

EBITDA margin: Expansion due to more efficient advertising, but expected to reduce

fashionette's EBITDA margin expansion in FY17–19 was predominantly due to operating leverage of other operating costs as its revenue scaled quickly. Other operating costs include premises, advertising, distribution, payment transfers, IT, and bad debts. In aggregate they have declined as a percentage of revenue from 28.6% in FY17 to 23.9% in FY19. The main sources of the margin gains have been: advertising, which declined from €8.3m in FY17 to €7.6m in FY19, equivalent to 3.6pp of margin enhancement, but significantly does not appear to have affected revenue growth given the recent acceleration; and bad debts, a less material cost, which has declined from €553k in FY17 to €226k, a contribution to margin of 50bp. Premises and distribution costs have been broadly stable relative to revenue.

Personnel expenses have broadly grown in line with revenue, at a relatively consistent 8–9% of revenue, as average staff numbers grew by 12% from 121 in FY17 to 136 in FY19, and the average cost per employee increased from €40.8k in FY17 to €49.1k in FY19.

Management expects the EBITDA margin to reduce to 3–4% for the next two financial years, driven by the expected reduction in gross margin, due to mix, as well as increased investment in operational costs and advertising as management targets growth outside the DACH region.

Balance sheet and cash flow

Exhibit 11: Summary balance sheet

€m	FY17	FY18	FY19	H120
Non-current assets	**20.9**	**19.7**	**18.0**	**17.1**
Goodwill	18.4	17.0	15.6	14.9
Intangibles	2.2	2.4	2.1	1.7
Property, plant & equipment	0.3	0.3	0.3	0.3
Current assets	**22.5**	**25.1**	**27.9**	**25.9**
Cash	3.6	2.7	2.3	1.6
Inventories	12.1	15.0	15.9	17.0
Trade receivables	6.0	7.0	8.5	6.5
Current liabilities	**(16.8)**	**(17.9)**	**(17.6)**	**(14.3)**
Trade payables	(7.7)	(6.6)	(5.3)	(5.4)
Borrowings	(6.3)	(8.6)	(8.5)	(4.6)
Net assets	**26.6**	**26.9**	**28.3**	**28.6**
Working capital cycle:				
Trade debtor days	37	39	42	30
Inventory days	132	148	138	133
Trade creditor days	83	65	45	42

Source: fashionette

fashionette has positive net assets and shareholders' funds, with the majority of the non-current asset base represented by goodwill. The company has no long-term borrowings; all debt is short-term bank overdrafts. With respect to working capital, the assets were relatively stable from FY17–19 but there has been a notable reduction in trade debtor days during H120. On the liability side, trade creditor days have fallen as the business has grown.

Exhibit 12: Summary cash flow

€m	FY17	FY18	H119	H219	FY19	H120
Operating cash flow	**8.3**	**(0.6)**	**(1.1)**	**3.0**	**1.8**	**4.3**
Net income	(0.3)	0.3	0.1	1.3	1.4	0.3
Depreciation and amortisation	1.9	2.4	1.2	1.3	2.5	1.2
Working capital	4.1	(4.6)	(3.3)	(1.0)	(4.2)	2.3
Tax paid	0.4	0.1	0.1	0.5	0.6	(0.3)
Investing cash flow	**(1.7)**	**(1.2)**	**(0.4)**	**(0.3)**	**(0.8)**	**(0.3)**
Net capex	(0.2)	(0.1)	(0.0)	(0.0)	(0.1)	(0.0)
Intangibles	(1.5)	(1.1)	(0.4)	(0.3)	(0.7)	(0.3)
Free cash flow pre interest	**6.6**	**(1.8)**	**(1.6)**	**2.7**	**1.1**	**4.0**
Net interest	(1.2)	(1.3)	(0.7)	(0.8)	(1.5)	(0.7)
Free cash flow post interest	**5.4**	**(3.1)**	**(2.3)**	**1.8**	**(0.4)**	**3.3**
Closing cash	3.6	2.7	1.1	2.3	2.3	1.6
Closing debt	6.3	8.6	9.2	8.5	8.5	4.6
Closing net debt/ (cash)	**2.7**	**5.8**	**8.1**	**6.3**	**6.3**	**3.0**
Net debt/ EBITDA	0.8	1.2			0.9	
As % of revenue:						
Operating cash flow	14.1	(1.0)	(3.5)	7.4	2.5	11.0
Net capex	(0.3)	(0.2)	(0.1)	(0.1)	(0.1)	(0.1)
Intangibles	(2.6)	(1.6)	(1.3)	(0.8)	(1.0)	(0.8)
Free cash flow pre interest	11.2	(2.8)	(4.9)	6.6	1.5	10.2
Free cash flow post interest	9.2	(4.8)	(6.9)	4.6	(0.6)	8.4

Source: fashionette, Edison Investment Research calculations

fashionette's free cash flow generation turned positive in H219, following 18 months of cash outflows. The improvement was due primarily to a move to positive operating cash flow and a modest reduction in investment in tangible and intangible assets, on an absolute basis and relative to revenue. Operating cash flow generation increased due to the higher profitability as well as working capital moving from being a consumer of cash to a source of cash, which is consistent with the reduction in trade debtors days noted above. The company is not capital intensive given fulfilment and delivery is subcontracted to third parties.

The positive free cash flow led to an improved financial position with net debt of €3.0m at the end of H120, down from a peak of €8.1m at the end of H119.

Valuation

As consensus forecasts are not yet available, we look at valuation metrics based on financial performance in the last reported financial year and compare fashionette to two groups of peers: companies that operate online platforms/marketplaces with exposure to the consumer or are offline retailers of luxury brands, and the luxury goods companies that own the brands that are sold by fashionette.

Exhibit 13: Peer group multiples

			Market cap	EV	Sales growth (%)		EBITDA margin (%)		EV/Sales (x)		EV/EBITDA (x)	
	Currency	Price	(local, m)	(local, m)	FY0	FY1	FY0	FY1	FY0	FY1	FY0	FY1
ONLINE/ OFFLINE CONSUMER:												
Amazon	USD	3286.3	1,646,089	1,625,709	20%	32%	15.5%	14.6%	5.8	4.4	37.5	30.2
ASOS	GBP	4591.0	4,573	4,486	19%	16%	8.2%	7.2%	1.4	1.2	16.7	16.4
Boohoo	GBP	273.6	3,439	3,114	44%	33%	10.2%	9.6%	2.5	1.9	24.6	19.9
Boozt	SEK	152.2	8,797	8,625	23%	23%	6.3%	8.4%	2.5	2.0	40.1	24.3
Calida	CHF	28.2	233	228	(1%)	(21%)	12.7%	9.6%	0.6	0.7	4.5	7.4
Delticom	EUR	3.5	43	126	(3%)	N/A	N/A	N/A	0.2	N/A	N/A	N/A
Ebay	USD	53.6	37,479	40,872	(0%)	(8%)	34.2%	36.7%	3.8	4.2	11.1	11.4
Farfetch	USD	29.0	9,846	9,810	69%	51%	(11.9%)	(5.4%)	9.6	6.4	N/A	N/A
Shop Apotheke Europe	EUR	151.4	2,709	2,714	30%	32%	(2.7%)	1.4%	3.9	2.9	N/A	N/A
Studio Retail	GBP	238.0	205	499	0%	0%	0.0%	0.0%	0.0	0.0	0.0	0.0
Watches of Switzerland	GBP	400.0	956	1,399	3%	10%	9.5%	14.2%	1.7	1.6	17.9	10.9
Zalando	EUR	81.2	20,761	20,207	20%	20%	6.5%	7.0%	3.1	2.6	48.1	37.2
Zooplus	EUR	142.8	1,022	1,023	14%	17%	0.8%	2.8%	0.7	0.6	86.9	20.4
Average					**18%**	**17%**	**7.4%**	**8.8%**	**2.8**	**2.4**	**28.7**	**17.8**
Average excl. lossmaking companies							**11.5%**	**11.2%**				
LUXURY GOODS:												
Burberry	GBP	1408.0	5,690	6,242	(3%)	(11%)	20.6%	21.0%	2.4	2.7	11.5	12.7
Essilor Luxottica	EUR	111.4	48,913	53,929	8%	(16%)	N/A	17.6%	3.1	3.7	N/A	21.1
Hermès	EUR	825.4	87,234	84,939	15%	(10%)	40.5%	34.2%	12.3	13.7	30.5	40.1
Kering	EUR	545.6	68,974	76,885	16%	(16%)	37.9%	31.4%	4.8	5.8	12.8	18.4
LVMH	EUR	418.9	211,652	234,987	15%	(16%)	26.0%	24.5%	4.4	5.2	16.8	21.2
Moncler	EUR	37.0	9,570	9,587	15%	(14%)	35.3%	34.9%	5.9	6.9	16.7	19.7
Mulberry	GBP	164.0	98	185	(10%)	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Prada	HKD	33.6	85,849	12,210	3%	(21%)	30.9%	24.1%	3.8	4.8	12.2	20.0
Richemont	CHF	60.8	31,776	30,663	2%	(11%)	17.0%	17.1%	2.2	2.4	12.6	14.2
Swatch	CHF	200.8	10,330	9,470	(3%)	(28%)	17.7%	9.0%	1.1	1.6	6.5	17.7
Tiffany	USD	128.9	15,642	16,089	(0%)	(19%)	22.9%	17.5%	3.6	4.5	15.9	25.7
Average					**7%**	**(14%)**	**29.8%**	**25.6%**	**4.9**	**5.6**	**16.2**	**20.9**
fashionette	**EUR**	**31.0**	**192**	**158**	**12%**		**9.3%**		**2.2**		**23.3**	
Premium/ (discount) to average online/offline consumer					**(6%)**		**2%**		**(21%)**		**(19%)**	
Premium/ (discount) to average luxury goods					**6%**		**(21%)**		**(56%)**		**44%**	

Source: Refinitiv. Note: Priced 27 October 2020. FY0 = last reported financial year.

The online/offline consumer peers include companies with quite different exposures to fashionette from the perspective of geographic coverage and products offered. The majority of these companies demonstrated strong sales growth in FY0, most enjoying growth rates from the high teens upwards, and are expected to do so again in FY1 albeit at a lower rate. The wide range of EBITDA margins reflect the product categories offered and growth strategies. fashionette's sales growth of 12% was lower than the average for these peers during FY0, but its strong sales growth in 9M20 of +24% is higher than the average expected for the group in FY1. Its EV/sales multiple of 2.2x is at discount to the average peer multiple of 2.8x. Its EBITDA margin of 9.3% in FY0 was higher than the peers' average margin of 7.4% but below the 11.5% of the profitable companies. fashionette's EV/EBITDA multiple of 23.3x is at a discount to the average multiple 28.7x.

In FY0, fashionette reported stronger sales growth than the average of the luxury goods peers of 7%, but this included a wide range of growth rates, some negative. In FY1, the luxury goods companies are expected to have a more challenging year given the economic weakness caused by COVID-19. fashionette's EBITDA margin of 9.3% is lower than the majority of the companies, reflecting the brand ownership and more global coverage of the luxury goods companies. Its EV/sales multiple for FY0 of 2.2x is at a discount to the average for these companies of 4.9x, but its EV/EBITDA for FY0 of 23.3x is at a premium of 44% to the average for the group of 16.2x.

Sensitivities

The company's financial performance and hence its share price will be sensitive to the following factors:

- **Economic outlook**: despite having strong long-term growth drivers from demographic and technological changes, and increasing consumer aspiration, the demand for luxury and premium items is vulnerable to changes in the macroeconomic outlook and consumer incomes, including for example a COVID-19 driven recession.
- **Consumer tastes and fashions:** fashionette offers a wide range of fashion items therefore it may be exposed to changes in national tastes or fashion misses by key brand owners.
- **Managing growth:** this includes hiring and retaining skilled staff and adapting to local markets as it expands overseas, acquiring new expertise as it enters new markets, both geographic and new product.
- **Increasing M&A:** management and the majority shareholders have clear ambitions to grow fashionette organically and inorganically. While they have a history of experience of successful M&A, it is possible that acquisitions do not fulfil their initial expectations.
- **Competition:** fashionette competes with a range of companies in different countries, which may have substantially larger resources and growth aspirations.
- **Reliance on luxury brand owners:** fashionette is one of many distribution platforms for the large, global luxury goods companies, which may change their views on how they are distributed as competition increases.
- **Reliance on third-party infrastructure providers:** fashionette outsources its fulfilment and distribution to third parties under long-term contracts and is therefore susceptible to disruptions in their ability to service fashionette's customers, and in more diverse geographies as the company expands. In FY21, the company will change its outsourced fulfilment provider, which raises the potential for disruptions in the changeover process.
- **Currency:** as fashionette expands outside Germany, it will have increasing exposure to non-euro currencies including the British pound, Swiss franc and Swedish kroner, with no natural hedging of the majority of the cost base. In addition, the company may source more products in other non-euro currencies, specifically the Swiss franc as the business expands.

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