

CULTI
MILANO

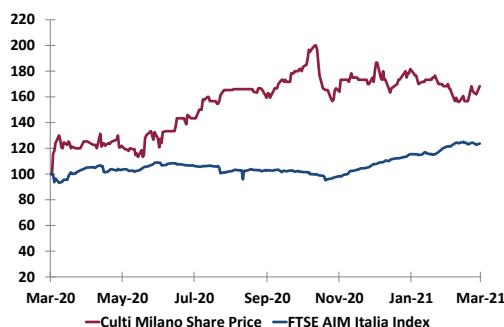
FLASH NOTE

OUTPERFORM

Current Share Price (€): 5.10

Target Price (€): 8.24

Culti Milano - 1Y Performance



Source: S&P Capital IQ - Note: 09/03/2020=100

Company data

ISIN number	IT0005257347
Bloomberg code	CULT IM
Reuters code	CULT.MI
Industry	Household & personal products
Stock market	AIM Italia
Share Price (€)	5.10
Date of Price	09/03/2021
Shares Outstanding (m)	3.1
Market Cap (€m)	15.8
Market Float (%)	22.8%
Daily Volume	500
Avg Daily Volume YTD	2,389
Target Price (€)	8.24
Upside (%)	62%
Recommendation	OUTPERFORM

Share price performance

	1M	3M	1Y
Culti Milano - Absolute (%)	1%	-6%	70%
FTSE AIM Italia (%)	3%	15%	24%
1Y Range H/L (€)	6.00	3.00	
YTD Change (€)/%	-0.10	-2%	

Source: S&P Capital IQ

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High performance in 2020 despite market challenges, with boost on sales and profitability

2020 outperforming 2019

Culti has communicated pre-closing figures for 2020: revenues at €13.4m, better than our expectations of €10.2m, EBITDA at €3.2m (24% margin) vs. our estimate of €1.5m. Pro-forma consolidated revenue, including full-year consolidation of 51% of Scent Company acquired in June 2020, is estimated at €15.3m with EBITDA at €3.6m. 2020PC Net cash is €2.3m, from €1.7m in FY19.

Culti Milano share price gained 70% over last 12 months, outperforming the AIM Italia index, which in the same period increased by 24%.

Acquisitions, online sales and international network driving performance

According to Management, sales increased across all business segments and geographies especially in Italy and Far East, where further growth is expected.

We see that the Company is delivering on its strategy and is going to reach a sound critical mass and industry-standard profitability.

Change in estimates factor-in alternative channels sales contribution and inorganic boost

€m	Revised			Previous			Change % (Rev. vs. Prev.)		
	2020PC	2021E	2022E	2020E	2021E	2022E	2020PC	2021E	2022E
Revenues	13.4	16.8	18.5	10.2	11.0	12.7	31%	53%	46%
EBITDA	3.2	3.9	3.9	1.5	1.6	1.9	113%	142%	105%
Margin	24%	23%	21%	15%	15%	15%			
Net (Debt) Cash	2.3	4.2	6.5	2.2	3.0	4.2	5%	41%	55%

Source: EnVent Research

Target Price €8.24 per share (from €6.88), OUTPERFORM rating confirmed

The new business mix is scaling and expanding the group potential. Despite the pandemic challenges on consumption and retail, revenue and profitability are over pre-Covid levels. Our updated valuation through DCF yields a target price of €8.24 per share, from €6.88 of our prior note, implying a 62% upside potential on Culti's stock price at €5.10. We confirm our OUTPERFORM rating on the stock.

Key financials and estimates

€m	2017A	2018A	2019A	2020PC	2021E	2022E
Revenues	6.2	7.0	8.8	13.4	16.8	18.5
EBITDA	1.1	0.7	1.4	3.2	3.9	3.9
Margin	18%	10%	15%	24%	23%	21%
Net (Debt) Cash	3.9	3.0	1.7	2.3	4.2	6.5

Source: Company data 2017-2020PC; EnVent Research 2021-22E - Note: since 2019 consolidated figures

Investment case

Company

Culti Milano (Culti) is an Italian home and business spaces fragrance and personal care company positioned in the premium and luxury segments, designing and distributing products under its own brand, through seven stores in Italy and a wide presence in European and Asian prestige department stores. The full line of products is also promoted through the online site (www.culti.com).

One of the main strategic goals of the Company is to rebalance its geographical presence through the opening of new DOS (Directly Operated Stores) in Italy and in other European and US cities.

Drivers

Industry drivers

Made in Italy. The Italian home fragrance industry has a high-quality production and style recognized worldwide, plus can call for higher prices around the world purely by carrying such a tag. No other country enjoys such “best in class” endorsements, or reputation, worldwide. The Italian industry, as a whole, has until recently underestimated this potential to strive and penetrate in international markets. This reputation, to be viewed as a competitive advantage and difficult to be challenged by competitors of other geographies, provides unique opportunities to those Italian companies able to make the most of the unexplored potential of *Made in Italy* products conceived for lifestyle lovers.

Home fragrances niche market still underexploited and open to home luxury and lifestyle. The performance of luxury brands in the last two decades has been mainly driven by the relentless increase of the population of the so called HNWI - High Net Worth Individuals. Exposure to population in emerging markets, both locally present and through customers travelling abroad and buying goods in Europe, together with the global reach of digital communication, have boosted internationally the awareness of the best products and brands. This, in turn, has paved the way and prepared fertile ground for dedicated home collections of luxury brands, a new business opportunity for industry segments which were previously “uncharted territory”.

Switching to lifestyle brands. Many fashion labels and luxury brands propose themselves as lifestyle symbols. Several luxury apparel brands have expanded their product offering to include lifestyle products and service lines such as housewares, furniture, fine dining and hotels. The trend has just begun, and the relative maturity of apparel and traditional accessories opens doors to a new wave of stylish home products. Italian companies are the best positioned in this arena thanks to their design and creativity capabilities.

Online luxury sales expect strong growth. McKinsey expects online luxury sales to more than triple by 2025, implying that nearly one-fifth of personal luxury sales

will take place online (Source: McKinsey, *The age of digital Darwinism*, 2018).

Digital communication and online sales suitable for the home fragrances industry. Digital communication and word of mouth are changing the way shoppers make their decisions, challenging established brands and offering more accessibility to emerging ones, in B2B and B2C markets. Unlike other luxury sectors, as there is a lack of dominant brands in the general home lifestyle segment, this makes it easier to reach shoppers and buyers in a number of touch points, without having to struggle with a pre-imagined restricted list of brands to choose from. Online purchases are trouble-free and in addition, repeat purchases of returning customers would be swift and easy, also promising better margins when compared to other trade channels.

Company drivers

Brand image. Culti Milano's luxury brand represents world renowned Italian design and style, being the Company producing with Italian selected craftsmen and using high quality materials. The *Made in Italy* tag attracts a premium price and has strong appeal globally. Culti has built a reputation for being Milan's home fragrance connoisseur, and intends to strengthen its brand awareness to become a lifestyle company. Culti Milano stands for sophisticated fragrances, well-being in one's preferred places and emotional dependence on its own fragrance.

Iconic products. Culti has a unique attitude towards innovation and focus on well-being and lifestyle of consumers. Its home fragrances collections stand out of the crowd for creativity, boldness and imagery. In 1990, Culti introduced, in a conservative and sluggish market, collections that marked a change for the entire industry. Culti's most popular fragrances Tessuto and Aramara have been on the market for 25 years and are recognized as a status symbol.

Lean business model and wide distribution network. Culti's business model is diverse from most competitors and is structured to be lean, based on the direct management of the value chain, with the main focus on style and product development like a "maison". The production is outsourced through a suppliers and assemblers network selected for high quality standards. Culti's distribution model is based on a worldwide network of agents and distributors, with corner shops and walls in over 40 European and Asian department stores, seven stores in Italy (two in Milan, Naples, Bari, Forte dei Marmi, Turin, Rome) and e-commerce.

International presence. Diversified global reach, with further room to expand in the USA, in Europe and in Asia. The projected opening of new stores in some strategic geographical locations represents the next step to achieve a stronger worldwide presence.

Culti free from the maturity risk. A typical concern for luxury companies is the sustainability of growth and a permanent question is how high is the chance of becoming mature and lose appeal. Probably the most challenging task for industry leaders is reconciling volume and profit targets with retention of exclusivity and

identity. Culti's business model is likely to be immune from the lifecycle of fashion products and of ever-changing trends being based on iconic *standards* that are bound to last for generations.

Challenges

Winning the digital gamble. Major brands are going digital, establishing a revenue stream from e-commerce and profiting of the benefits of digital advertising and online presence, through a well-built corporate website, social media and online multi-brand stores. Differently, luxury players are more cautious about digital and e-commerce. Culti is no exception, having a direct relationship with end consumers for a part only of its business, while direct e-commerce could be a conflicting channel with the multi-brand, multi-product stores network. However, we expect that the growing importance of digital media will sooner or later force to go digital. The challenge is in guessing the right timing. First typical phase is selling online either through partners or through their own e-shop, only offering a reduced product range and not advertising it much. Then, it would be critical to reach not too late the tipping point when to scale-up quickly e-commerce operations, with significant investments.

Slowdowns of markets pushes promotional sales. With the growing middle class seeking good quality and consumers in mature markets looking for bargains, the off-price channel in the luxury goods market has more than doubled over the past few past years

Low exposure to key markets. The establishment of a structured presence into the traditionally most important markets for luxury goods, namely North America and the so called luxury cities, might require time and significant investments.

Currency issues. Most European luxury goods manufacturers produce in EUR (in France and Italy) and sell throughout the world, with exposure to USD and Dollar-linked currencies. Changes in the EUR/USD exchange ratios are critical to exports.

M&A and cash management. The most common issue with acquisitions in the fashion and luxury sector is that they do not produce many synergies. As a consequence, given the high multiples commanded by the potential sellers, cash generation and payback could become an issue in any potential deal.

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Date	Recommendation	Target Price (€)	Share Price (€)
17/10/2017	OUTPERFORM	5.74	4.41
28/03/2018	OUTPERFORM	5.74	4.36
27/09/2018	OUTPERFORM	4.67	3.81
15/04/2019	OUTPERFORM	3.94	2.58
12/08/2019	OUTPERFORM	3.32	2.60
21/04/2020	NEUTRAL	4.12	3.64
13/10/2020	OUTPERFORM	6.88	5.70
09/03/2021	OUTPERFORM	8.24	5.10

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