



University of St.Gallen

MODULE 9

L'ORÉAL

The Power of Programmatic M&A: How L'Oréal's external growth strategy ensure future organic growth

This case was collected and researched by Prof. Dr. Thomas Bieger, Yannik Breitenstein, Dario Mitterer and Tanguy Leloup, Director of M&A at L'Oréal who not only served as interview partner but also helped with great support to edit the case.

It serves as a basis for the discussion of business issues in class and is not intended to illustrate correct or wrong actions in management situations.

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IMP-HSG, Institute for Systemic Management and Public Governance

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Tanguy Leloup, Director of M&A at L'Oréal, is reflecting on the acquisitions of the iconic Mugler and Azzaro fragrances from Clarins, which are great examples of how the Group is continuously fueling growth through a very targeted M&A strategy.

A century-old company with one sole vocation: creating beauty

L'Oréal was founded in 1909 by the young chemist Eugène Schueller who was engaged in formulating, manufacturing, and marketing hair dyes products¹.

It has since been dedicated to only one sole vocation: creating beauty. This exclusive focus on a single line of business brings a clear competitive advantage. The Group draws on over a century of expertise in cosmetics and an in-depth understanding of consumers, underpinned by its insight into beauty cultures, needs, desires and aspirations.

Today, L'Oréal is active in more than 150 countries, covering all product categories (from haircare to skincare and sun protection to fragrances and makeup), distribution channels (department stores, owned retail, specialty retail, wholesale, ecommerce, travel retail), and price categories. With the trend towards “singularization”, based on its deep understanding of beauty cultures, it is evolving from the concept of “beauty for all” to “beauty for each” with the goal “to provide tailored, inclusive beauty solutions that meet specific, individual aspirations”. “Strategy in this regard is based on careful attention to consumers and a deep respect for their differing needs, lifestyles, desires and traditions”.

Strategy forged on innovation and acquisitions

As stated on the webpage of L'Oréal “[...] the founder of the Group forged the first link in what is still the DNA of L'Oréal: research and innovation in the service of Beauty”². This has lived up through the years and nowadays, more than a billion euros are still invested every year to create “effective, inclusive and sustainable” beauty products. As part of its R&I budget, L'Oréal is also putting great efforts into Green Sciences and Beauty Tech.

The years in the aftermath of World War II – with its strong economic development, paved the ground for the international growth of the group. Already at that time, acquisitions of brands were already an important instrument to gain market shares, expand market reach and enter new beauty categories. Hence, throughout the decades, that's how L'Oréal progressively put its grip on today's most famous brands such as Lancôme (1967), Garnier (1967), Biotherm (1971), Vichy (1980), Helena Rubinstein (1988), Maybelline (1996), Kiehl's (2001), Yves Saint Laurent Beauty (2008), NYX (2014), Cerave (2017), Azzaro and Mugler (2020) and Aesop (2023).

Today, L'Oréal runs a global flotilla of 36 global brands, plus an additional ca. 40 mid-sized and regional brands. Out of the 80+ brands, only 3 have been created in-house: L'Oréal Paris, L'Oréal Professional and Kerastase. The portfolio of brands is organized around 4 complementary divisions with each one developing a specific vision of Beauty for its respective market: Professional Products Division, Consumer Products Division, L'Oréal Luxe and the Dermatological Beauty Division.

L'Oréal's balanced growth across Divisions, geographic Zones and categories demonstrates the relevance of its multipolar model: strategically centralized (incl. marketing and product development) and operationally decentralised (sales and services). Altogether, this model is driving long term growth and is proving resilience during turbulent economic times.

In 2022, L'Oréal's revenues amounted to over 38 billion euros (multiplied by 1.7 in the last 10 years), and recorded an Operating Profit of 7,45 billion euros (19% margin)³.

Programmatic M&A to ensure L'Oréal's future organic growth

Programmatic M&A as an element of strategy implementation is at the core of the business model. These acquired companies, through their integration and deployment, are helping to accelerate the Group's penetration of their markets and drive organic growth going forward.

Whereas in many industries and for many companies, large-scale M&A transactions are still common, L'Oréal relies on a programmatic M&A approach. McKinsey describes this approach as "carefully choreographing a series of deals around a specific business case or M&A theme – rather than relying on episodic 'big bang' transactions"⁴. The focus lies on mid-sized targets rather than on mega-mergers. This programmatic approach is described as the one most likely to create value for the company.

Following this approach, companies embark on an ongoing M&A process based on a purpose, vision, and strategy that define their search focus. In the case of L'Oréal, during the last 10 years, about 25 acquisitions in form of company or license deals were closed. Due to the learning curve effect, M&A can become a core competence.

Growth through M&A activities can have different aims and potential benefits, such as building up scale, entering new frontiers (markets, categories), speeding up the development of capabilities, or optimizing and reorganizing one's portfolio.

The target screening and evaluation process in M&A can be depicted in a funnel (cf. figure 1). The funnel approach can be used to evaluate M&A opportunities by creating a long list and then narrowing it down based on group priorities, growth ambitions and financial targets.

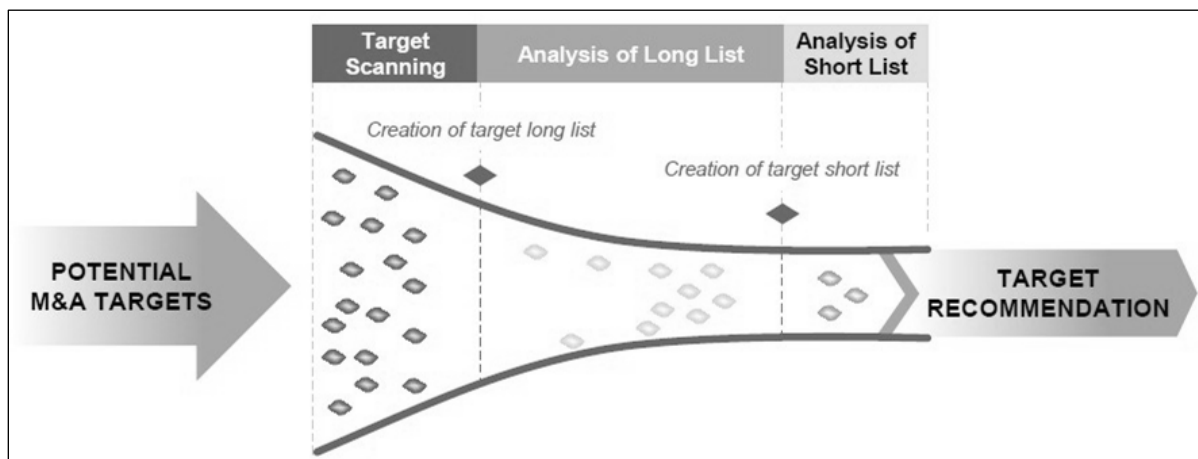


Figure 1: Funnel approach to evaluating M&A targets (source: Arthur D. Little, 2022)⁵

Leveraging on key identified priorities and strategic frames, L'Oréal's M&A team, Divisions and Zones are constantly on the lookout for potential M&A targets. Potential targets must contribute to L'Oréal's purpose and vision, but also to future growth. A pipeline of opportunities (at different stages of maturity) is constantly nurtured with internal and external partners to evaluate strategic interests and enter potential rounds of negotiations / M&A process with the identified targets.

A potential M&A target must have a strong strategic and financial fit, and with significant synergies to be extracted. Key to a successful M&A is: First, a clearly defined strategy to extract and create value from the acquisition; Second, a well-prepared integration process, laying down both Day 1 model and target model (i.e. "end-state" within L'Oréal organization) and identifying (and anticipating) any potential business, legal, or tax issues early on. Third and lastly, post-deal execution with a focus on the realization of the Business plan and the value creation opportunities that were identified during the acquisition process.

At L'Oréal, a dedicated integration team takes charge. Following a sophisticated integration "playbook" that structures and documents the process, the multifunctional team starts executes the integration strategy of the newly acquired companies. The key challenge is to find a suitable balance to integrate the brands into the L'Oréal systems and thus to realize synergy and growth potential and at the same time preserve, as Mr. Leloup said, "what we cherished in the brand: its unique positioning, its essence, values and philosophy, its differentiated capabilities and expertise or its customers". The challenge is even greater when acquiring small companies (and with a relatively short history) that are not yet properly structured but hold the promise of a fantastic potential.

Hence, L'Oréal's integration strategy is to protect what makes the brand unique and successful while providing a secure platform for growth. The goal is to make the brand profitable and gradually expand it thanks to the strategic positioning and sales competence of L'Oréal to other regions. A successful example is the CeraVe brand in the Dermatological Beauty division which has increased its sales from 100 million euros in 2017 to over a 1 billion euros in 2022.⁶ Value creation is continuously monitored throughout the years, with ratios such as ROCE continuously updated.

The Mugler and Azzaro case

Back in 2019, acquiring Mugler and Azzaro represented for L'Oréal the unique opportunity to add complementary, successful and worldwide renowned brands to its Designer brands fragrance business (Armani, Prada, Cacharel, Diesel, Viktor&Rolf, Maison Margiela, Atelier Cologne, etc.). But most and foremost, this represented a unique opportunity to reach the number one position in the global fragrances market. Mugler's key attractions also reside in highly valued uniqueness:

- Mugler has been a true pioneer in sustainable luxury with its lifetime bottles that can be refilled in-stores with Mugler Fountains.
- Rich CRM and loyalty program built around a vibrant community. "Loyalty has been the Mugler way to build, in the long run, a 'love brand'", how Leloup added.
- The brand's spectacular DNA, with a first immersion for L'Oréal into Fashion and ownership of all collection archives to support the brand's image and equity.

During the due diligence process and through the preparation of the integration, Mugler's creative studio was seen as essential for the fragrance business and the investments and cost of running it considered as critical brand marketing costs that will continue to nurture the brand's equity and vision with new contents, inspiration, and vision.

From an economic standpoint, market performance was good – and most importantly there were important synergies with the existing designer brand fragrance business unit of L'Oréal. "Mugler will pursue their international development while benefiting from the resources of the world's beauty leader in marketing, distribution, and innovation".

Links and sources

Interview with Tanguy Leloup from 21 March 2023

¹ <https://www.loreal.com/en/group/culture-and-heritage/l-oreal-history/>

² <https://www.loreal.com/en/group/culture-and-heritage/l-oreal-history/>

³ <https://www.loreal-finance.com/en/annual-report-2022/>

⁴ <https://www.mckinsey.com/capabilities/strategy-and-corporate-finance/our-insights/how-one-approach-to-m-and-a-is-more-likely-to-create-value-than-all-others#/>

⁵ https://www.adlittle.com/sites/default/files/viewpoints/ADL_Bye_bye_comfort_zone.pdf

⁶ https://www.loreal-finance.com/system/files/2023-02/OA_NH_CAGNY_230223.pdf