Finance a key asset for luxury, fashion in pandemic era

By Dominique Muret - November 16, 2020

The Covid-19 pandemic and its attendant lockdowns have shone a light on the fragility of the fashion and luxury sector. Companies have realised that, in order to deal with constantly growing market uncertainty, geographic and product diversification are no longer sufficient. It is also absolutely necessary to demonstrate a high degree of financial solidity, and to diversify one’s sources of funding. As a result, financial operations have multiplied in the fashion and luxury sector following the pandemic's outbreak.

From share buyback to green bonds, bond-backed loans, debt renegotiation with banks, access to state funds, recapitalisations and calls to investors, fashion and luxury labels have devised and deployed all kinds of financial tools to protect themselves and deal with the crisis, whilst continuing to expand. Evidence of this intense activity is the number of CFO hirings in recent months, often going hand in hand with changes in corporate vision, as well as the rising influence of CFOs themselves. As in the case of Joanne Crevoiserat, CFO of US group Tapestry (owner of Coach, Kate Spade and Stuart Weitzman), who was appointed CEO in the summer.

“The current crisis has shown how important corporate finance is, and how it is now regarded as an increasingly essential management resource. Of course, first you need to have quality products. But in the end, it is corporate finance that makes the difference,” said Stefano Caselli, professor of banking and finance at Milan’s Bocconi University.

Caselli explained to FashionNetwork.com that the crisis sparked by the pandemic is prompting a need for corporate financing at various levels. “The first level is survival finance, urgently needed liquidity that is usually provided by governments, either directly or via banks. Then there is a second level, when companies seek greater solidity through external funding. And once the market becomes uncertain, they need to further boost their cash flow, or to access financial tools enabling them to recapitalise their business,” said Caselli.

According to Caselli, the role of capital markets should be reassessed, because companies listed on the stock exchange “are better equipped to deal with the crisis. [Being listed] enables them to be more visible, to attract
Exchange are better equipped to deal with the crisis. [Being listed] enables them to be more visible, to attract more funding and attention from investors, while facilitating financial operations like bond issues, recapitalisations and the like.”

Among the various tools available, labels resorted first and foremost to the redemption of their own shares during the first lockdown phase, as nearly all fashion and luxury stores and businesses were closed for two months in March and April, virtually the world over. Italian fashion groups Aeffe (owner of Moschino) and Salvatore Ferragamo, among others, started share-buyback programmes at that time. At the end of January, Bernard Arnault bought back LVMH shares worth €11.7 million, while the Kering group continued with its share-buyback programme, which began in October 2019, throughout H1 2020.

“At the start of the pandemic, businessmen were chiefly stressed about three elements: their employees’ health, their businesses and their savings. Buying back their own shares was a way of bolstering their companies and avoiding take-overs at a time of great fragility and uncertainty. In some cases, entrepreneurs made specific deals with other shareholders in order to guarantee a hard core of support, enabling them to fend off any attack,” a banker told FashionNetwork.com.

“Buyback operations were defensive in nature at the start of the crisis, designed to protect companies while making their share price less volatile, but now they are far less frequent,” said Caselli. Several groups, like PVH, Tod’s and L’Oréal, actually decided to forego such operations, even if they had been already approved and triggered, being “mindful of preserving cash reserves in a highly volatile context.” Others, like EssilorLuxottica, nipped such programmes in the bud.

In order to deal with the business standstill caused by the pandemic, the majority of fashion and luxury labels have resorted to urgent bank loans or bond issues. But a new environment is taking shape, with other challenges on the horizon, requiring new investments. Companies are more indebted than they were in 2019, and need to generate enough cash to pay these debts, and also to address the challenges they currently face in the fields of digital transformation, sourcing and operations.

The fashion industry is therefore looking at innovative funding solutions. One of them, green finance, is now extremely popular. In recent months, scores of fashion labels have resorted to green bonds and sustainability-linked loans (SLLs). These are two different types of financing: SLLs are linked to sustainability goals companies have pledged to achieve, while green bonds are used to finance specific projects.

In the second half of 2020, these financial tools have literally boomed, and are used extensively by companies to fund their sustainability efforts. Prada was the first luxury group to access a loan linked to sustainability targets in
fund their sustainability efforts. Prada was the first luxury group to access a loan linked to sustainability targets in November 2019, while US group VF Corp (owner of Timberland, The North Face and Vans) was one of the first fashion groups to issue green bonds, in February. Salvatore Ferragamo and Moncler followed suit in July, and in September it was Burberry’s turn to herald its intention of issuing sustainability bonds.

At the same time, Chanel launched a fundraising effort worth €600 million by issuing bonds linked to its sustainable development goals, the luxury label’s first foray on the bond market. The bonds are indexed on the label’s programme to reduce carbon emissions. Chanel has pledged to fight global warming and has drawn up a programme which includes penalties should goals not be attained.

Another recent example is that of Adidas. After a first, standard bond issue in September, the German group launched a further sustainability bond issue for €500 million, designed to fund “purchases of recycled materials for sustainably sourced products, investments into renewable energy production and energy-efficient buildings as well as various initiatives to create lasting change for under-represented communities,” as Adidas indicated in a press release.

“This kind of investment has the advantage of being extremely tangible, because it's linked to specific conditions and goals. It's a win-win operation,” said Caselli, adding that “investors have an appetite for novelty and are looking for profitable opportunities. Companies for their part are able to access fresh capital by showing they can innovate, and doing so sustainably. It's a new way of creating jobs and wealth.”
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The market uncertainty and volatility caused by the pandemic has prompted a boom in ethical and sustainability concerns, with a heightened focus on companies’ environmental, social and corporate governance (ESG). Issuing sustainability-linked bonds (SLBs) is good for a company’s image, and this type of funding is likely to become even more advantageous, after the European Central Bank decided at the end of September to purchase SLBs and to accept them as collateral.

Fashion labels are also accessing other sources of finance, resorting for example to the banking system, via state-backed loans. In Italy, the fashion sector has benefited from direct loans issued by state-controlled investment bank Cassa Depositi e Prestiti (CDP), providing quicker access to finance than ordinary banks.

Liu Jo was granted a €15 million loan and OTB (the group that owns Diesel, Marni and Margiela) one worth €50 million, to fund their respective expansion plans. Stefano Ricci too has signed a financing contract with CDP, in China, through its Shanghai subsidiary. The contract is worth CNY30 million, equivalent to €4 million, and is designed to help boost the label’s presence in China.

The situation is much more complicated for start-up labels and emerging designers. Finding production partners is still possible, but accessing funds to put in place all the other activities needed for a label’s development, such as marketing and advertising, has become “very, very difficult,” according to Luca Rizzi, in charge of the Tutoring & Consulting division at Italian show organiser Pitti Immagine.

“It's no longer possible to talk to banks. After the pandemic's second wave started, all our contacts have dried up,” said Rizzi, unable to conceal his regret. Pitti Immagine is currently mentoring 25-26 labels and, in order to support them, it is striving to set up partnerships with business angels, family offices and investment funds.