

Financial and Marketing Analysis on Hermes International SA

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Abstract. Since its establishment in 1837, Hermes has been adhering to quality, culture is driven, handmade, and adhere to the development of high-end, from the original harness store development into today's famous super luxury giant. This paper analyzes Hermes from two aspects, its own financial situation and the surrounding industry market. In terms of financial performance, Hermes showed a good recovery from the negative effect of COVID in 2020, creating a leading position over the industry in sales revenue. Combined with well turnover and debt-paying ability, the business performance is generally in stable growth. In terms of the market analysis, the SWOT and industrial competitor analysis was made to point out the actual utilities of Hermes' strategies. Hermes insists on the family's absolute control of the brand to ensure the maintenance of the family business model. In strategies, the membership system and hunger marketing to increase user engagement, the little discount style also creates a noble image of the brand.

Keywords: Hermes; Financial Analysis; SWOT Analysis.

1. Introduction

1.1 Luxury Market Background

In recent years, the size of the global luxury market has grown steadily. Even though overall sales in 2020 were affected by COVID-19, the luxury market is still full of resilience. In FY2020, the cumulative sales of the global top 100 luxury companies reached 252 billion USD, with an average sale of 2.5 billion USD, and a comprehensive net profit margin of 5.1% [1]. The pace of growth in the luxury market in 2021 is also unprecedented. The personal luxury goods market has seen a V-shaped recovery, with sales breaking pre-pandemic records.

Notice that the share of the top 10 in the top 100 luxury sales reached 51.4%. The overall competition level of the industry is obvious. The head company is competing in the high-end market, and the competition is fierce. Hermes benefits from its brand position, with outstanding revenue and profitability, and strong growth trends. Hermes International achieved industry-leading net margins. In FY2020, its net profit rate among the top 100 enterprises was the highest, reaching 21.7%. It has become one of the top 100 enterprises with higher profits for several consecutive years, achieving a net profit rate of more than 20% from the fiscal year 2016 to the fiscal year 2020.

1.2 Objection

This paper will use the idea of relative comparison and absolute comparison to analyze Aimasi Company from itself to the industry.

Firstly, via financial analysis, this paper gave the fundamentals including sales revenue, gross profit, and operating profit of Hermes in FY2020 and FY2021. Calculating the current ratio and quick ratio, revealed the protection degree of current assets to current liabilities. It also investigated the security of Hermes Company's short-term debt repayment. Besides, the debt financing ratio of the company in the financing policy is discussed through the financial leverage ratio.

Secondly, in the market analysis part, this paper chose Hermes and LVMH Group for comparison. The actual performance of the two luxury giants in the past two years was compared in terms of sales and various financial indicators. What's more, the SWOT model was made to find out the favorable and worthy factors of Hermes Group, as well as the unfavorable factors which should be avoided.

The existing problems and suggested solutions were found, clarifying the company's future development direction.

2. Basic Descriptions of Hermès

Hermès is a French luxury goods manufacturer international company, founded by Thierry Hermès in 1837 as a harness shop in Paris [2]. With fourteen product divisions that are leather, ties, scarves, men's and women's wear, perfumes, watches, gloves, footwear, tableware, decorative arts, stationery, jewelry, and enamel wear, Hermès has iconic status in the world of luxury. The company is owned by two brothers Pierre-Alexis and Axel Dumas. Both are co-chairmen of the brand [3]. Axel Dumas is the Chief Executive Officer (CEO), and Pierre-Alexis is the company's creative director, whose father, Jean-Louis, revolutionized Hermès, growing it into an international luxury retailer. Hermès has been globally the most valuable luxury brand consistently, which ranks 23rd among the Best Global brands with a brand valuation of 18 billion dollars.

As luxury goods are very special commodities, their core value of them lies in the unique cultural connotation of high quality, which is the fundamental reason why the price of luxury goods can transcend the value of the commodity itself [4]. The core of luxury research is to study the culture and values inherited by enterprises. Therefore, this paper aims to explore the corporate core culture values of Hermes, the world's top luxury goods company, from the perspectives of financial performance, strategic development, and peer comparison. Furthermore, the recipe of Hermes' eternal classic and success may provide a practical reference for other luxury corporations.

3. Financial Analysis of Hermes

Table 1. Consolidated income statement

in millions of euros	2021	2020
Revenue	8,982	6,389
Cost of sales	(2,580)	(2,013)
Gross margin	6,402	4,376
Sales and administrative expenses	(2,137)	(1,699)
Other income and expenses	(734)	(696)
Recurring operating income	3,530	1,981
Other non-recurring income and expenses	-	91
Operating income	3,530	2,073
Net financial income	(96)	(86)
Net income before tax	3,435	1,986
Income tax	(1,015)	(613)
Net income from associates	34	16
Consolidated Net Income	2454	1390
Non-controlling interests	(8)	(4)
NET INCOME ATTRIBUTABLE TO OWNERS OF THE PARENT	2446	1385
Basic earnings per share (<i>in euros</i>)	23.37	13.27
Diluted earnings per share (<i>in euros</i>)	23.30	13.21

At current currency rates, the Group's consolidated revenue in FY2021 was €8,982 million, increasing 40.59% from €8,982 million of FY2020 according to the consolidated income statement of Hermes (Table 1). At steady exchange rates, this growth over the course of two years reached 33%. In comparison to 2020, the gross margin rate increased by 2.8 basis points to 71%. This gain is due

to a leveraging effect on fixed production costs, a consistent increase in productivity, and a spectacular rate of inventory disposal. Sales and administrative costs totaled €2,137 million, up from €1,699 million in 2020. This amount included €421 million for communications costs, compared to €279 million in 2020, when numerous events had to be cancelled or postponed due to the health crisis.

According to Table 1, other revenue and costs totaled €734 million, up from €696 million in 2020. They also comprise €512 million in depreciation and amortization (€468 million in 2020), of which €50 million (€46 million in 2020) refers to property, equipment, intangible assets and plant, and the remaining €50 million to rights-of-use. The increase in depreciation and amortization is due to ongoing expenditures in the production facilities, distribution network, information systems, and digital technology. 122 million euros worth of additional costs are also connected to free share plans. Recurring operating income reached €3,530 million, an increase of 78% from 2020. After a remarkable first half with a profit of 41%, the second half stood at 38% due to an increase in hiring and communication costs, as well as the detrimental effects of currency rates.

3.1 Current Ratio and Quick Ratio

The current ratio measures Hermes's ability to pay current, or short-term, liabilities (debts and payables) with its current, or short-term, assets, such as cash, inventory, and receivables.

Table 2. The current ratio and a quick ratio of Hermes at the end of FY2020 and FY2021

	31/12/2021	31/12/2020
Inventories and work-in-progress	1,449	1,289
Current assets	8,845	6,650
Current liabilities	2,575	1,839
Current Ratio	3.43	3.62
Quick Ratio	2.87	2.92

Table 2 above shows at the end of FY2020 and FY2021, the current ratio is 3.43 and 3.62 respectively, which are both greater than integer 1, demonstrating that the business has the capacity to sustain its financial viability in the short term. Additionally, as Hermes remained the current ratio greater than 2.0, Hermes has more current assets than current obligations, therefore even if half of the company's existing assets cannot be realized soon, all of its current liabilities may still be settled.

The quick ratio is used to assess a company's capacity to use its current assets to pay off maturing debts immediately. The current ratio's relevance is to show the guaranteed degree of current assets to current liabilities and check the security of short-term debt repayment. The quick ratio at the end of FY2020 and FY2021 are both more than 1.5, which sends a safer signal for external investors in the company's solvency

3.2 Leverage

Table 3. The financial leverage and changes over the past 5 years

	2017-12	2018-12	2019-12	2020-12	2021-12
Financial Leverage	1.34	1.36	1.5	1.5	1.47
% Year Over Year	-	1.49%	10.29%	0.00%	-2.00%
Debt/Equity	0	0.01	0.14	0.2	0.17
% Year Over Year	-	-	1300.00%	42.86%	-15.00%

The financial leverage ratio shows how Hermes uses its debt to adjust equity capital gains, reflecting its financing through debt. A smaller reduction in financial leverage in FY2021 compared to FY2020. Hermes makes most of its merchandise itself, so it does not need to rely on third-party suppliers, giving it greater control over its finances.

4. Marketing

4.1 Hermes vs. LVMH

Hermes and LVMH, two world-class luxury groups, have maintained ideal and stable growth in sales and business in various industries in the past two years, and have not been greatly affected by the epidemic. In FY2021 (Table 4), the revenue of Hermes increases from 6.88 billion to 8.98 by 30.52%, while the revenue of LVMH increases from 44.65 to 42.22 billion by 43.83%. Hermes and LVMH, two of the world's largest luxury goods companies, have maintained ideal and stable growth in sales and business in each industry over the past two years. Under the shadow of the pandemic, the two companies have shown their strong ability to bear pressure as the world's leading luxury companies. Local old customers and strong growth in e-commerce have made up for the slump in international traffic.

Table 4. The revenue comparison between Hermes & LVMH (2020-2021)

	Hermes		LVMH	
	2021	2020	2021	2020
Revenue (Bil)	6.88	8.98	44.65	64.22
Operating Income (Bil)	2.37	3.6	8.31	17.12
Net Income (Bil)	1.53	2.45	4.7	12.04
EBITDA (Bil)	2.74	4.03	13.78	23.28

4.1.1 Solvency Analysis

The quick-freeze ratio reflects the short-term debt-paying ability of two top luxury companies. Whether an enterprise can repay short-term debt depends on the amount of short-term debt and the liquid assets with variable debt paying. According to Table 5, LVMH's quick-freezing ratio is 0.47, lower than Hermes' 2.84, and also lower than the 1.0 standard that is generally suitable for listed companies in the industry. The amount of working capital a firm has left after current assets have paid off current liabilities helps us assess its risk of servicing short-term debt. In terms of the current ratio, LVMH's current ratio was 1.17, also lower than the industry's evaluation level of 2.0. This indicates that although LVMH has achieved an ideal recovery state under the impact of the epidemic, its performance is still weaker than that of its peer Hermes, the latter has a high short-term solvency.

Table 5. The solvency ratio comparison between Hermes & LVMH, 2021

	Hermes	LVMH
Quick Ratio	2.84	0.47
Current Ratio	3.6	1.17
Interest Coverage	119.53	77.99
Debt/Equity	0.2	0.73

4.1.2 Operating Capability Analysis

The average number of times an accounts receivable is changed into cash over the course of a year is known as the accounts receivable turnover rate, which represents the pace at which an accounts receivable is transformed into cash. According to the comparative analysis (Table 6), both companies will have a significant improvement in this metric for the fiscal year 2020 to 2021. Among them, Hermes increased by 36.96% and LVMH by 36.41%, which were almost the same in terms of growth amplitude. However, the absolute advantage of Hermes indicates that the company has more turnover times of receipting accounts, shorter account age, stronger asset liquidity and fewer bad debt losses, which also confirms the company's strong short-term solvency.

Purchasing inventory, putting it into production, and taking back sales are only a few examples of how inventory turnover is used as a comprehensive index to track and assess the management state of the two businesses. As can be seen from the table, Hermes has a fast inventory turnover rate, a low

inventory occupation level, strong liquidity, and a fast conversion speed of inventory into cash, accounts receivable, etc. This may be due to the way Hermes pre-orders its products (such as Birkin bags), which are crafted and manufactured by hand, tend to lag behind customers' pre-orders. Thanks to the timeless heritage of Hermes, some customers have to queue for years to buy a classic Hermes bag, which explains why Hermes has a fast turnover in inventory and money tied up in inventory. The total asset turnover rate reflects that the management quality and utilization efficiency of all assets of Hermes have reached a good state in the past two years.

Table 6. The turnover ratio comparison between Hermes & LVMH (2020-2021)

	Hermes		LVMH	
	2020	2021	2020	2021
Receivable Turnover	22.51	30.83	14.39	19.63
Inventory Turnover	1.66	1.88	1.19	1.38
Fixed Asset Turnover	2.29	2.77	1.48	2.03
Total Asset Turnover	0.61	0.72	0.44	0.55

4.2 SWOT analysis

4.2.1 Strengths

The Dynamics of an Exclusive Omnichannel Distribution Network

The integrated and exclusive distribution network has been maintaining and strengthening its omnichannel offering. The majority of the network's nodes are branches maintained by the Group under the Hermès name [5]. To meet the unique needs of its consumers and provide a unique shopping experience in each of its 303 stores worldwide, each one offers a customized assortment of products, achieving great responses, and capturing the extreme needs of customers everywhere.

The internal distribution strategy used by Hermès demonstrated its efficiency amid the health crisis by avoiding the steep slope during COVID-19. The House's tools were altered to reflect a changed customer relationship in order to adapt appropriately to the needs and restore a special relationship with clients [6]. With reimagined formats, Hermès has been able to adaptably embrace the digitization of usage while maintaining relationships with its devoted local clientele. In 2022, efforts to open and renovate the shops in New York, Barcelona in Spain, Shanghai and Wuhan in China and so on, will continue the store network's qualitative development (Qatar). In about 20 stores around the world, upgrades and expansions will be prioritized. The House will advance its digital strategies by offering an ever-expanding selection of online sales and services to increase traffic and attract customers.

Strong Brand Image

Hermès is well-known and offers a wide range of goods. The business is successful in maintaining product differentiation and high standards. Furthermore, it participates in a variety of sponsorships to promote its brand internationally.

Healthy Economic Growth

Despite the mixed gains, no division of the Hermes group papered a revenue loss last year, with the off-the-rack wearings and accessories lines, watches, and other business lines (jewelry and homewares) posting the most significant gains. Ready-to-wear and accessories segment revenue grew 59% year on year and 44% from 2019. The watch division was particularly strong, with revenues up 73 %t year on year and 77% from 2019. Among them, the new men's watch H08 is quite popular. Revenue from other business lines grew 57% year on year and 95% from 2019, with both jewelry and homewares performing well.

In terms of the performance of economic growth, Hermes has experienced average annual revenue growth rates of 12% and net income growth rates of 15% over the period of the last decade, respectively. In FY2021, the revenue summed to be €8,982 billion, with €3,530 million in recurring operating income, €532 million in operating investments, and stock market capitalization of €162.15 billion.

4.2.2 Weakness

Lack of capacity due to scarcity

The emphasis on scarcity, which has kept Hermes at the top of the luxury pyramid, could in turn be a brake on growth. In the fourth quarter of 2021, Hermes Group revenues grew 11%, but a shortage of capacity pushed revenues in the leather goods division down 5.4%. Hermes shares fell as much as 8.4% after the results were released, their biggest drop in the past five years. A lack of production capacity is the main reason for the poor performance of Hermes's leather goods division. In the fourth quarter of 2021, sales in the leather goods division fell 5.4%, worse than the 2.3% decline expected by analysts. The squeeze is reflected in shortages of key products such as Birkin and Kelly bags, which typically account for half of Hermes group revenues. With the economy recovering and stores opening, consumers' long-held desire to shop has exploded, and demand for luxury goods has rebounded strongly [7]. But Hermes has been unable to take full advantage of the upturn because of capacity constraints.

4.2.3 Opportunities

Promotion In the New Media Industry

“For success to endure, Hermes heirs may require one more thing. The company is a digital laggard.”, says The Economics. In 2021, only 2-3% of its sales will come from the website, half that of its rivals. Its Instagram account, which measures brand awareness, has just 10m followers, compared with 41m for Chanel or Gucci. It lacks young consumers who energize the brand. According to Citigroup, only a quarter of Hermes's sales are to Gen-Z (typically the generation born between 1995 and 2010) or millennials (the oldest of whom are about to turn 40).

4.2.4 Threats

Brand Takeover

LVMH owns a big part of Hermes stocks. Hermes, however, is doing everything it can to stop that from rising. LVMH bought a large stake in Hermes in 2010 and the brand has feared a hostile takeover ever since. Hermes sees this as more of a "culture war" than a financial one. To prevent a takeover, Hermes set up a separate family holding company to control 50 percent of the shares to protect them from LVMH.

5. Suggestion

5.1 Stick to the High Price Threshold with Subtle Adjustments

Considering the special commodity attributes of luxury goods, the pricing strategy of luxury goods enterprises needs to consider macro and micro aspects to attract target customer groups while ensuring its scarcity. Hermes adheres to the traditional positioning of the top brand, with only a few entry-level products under the advanced membership system. The ultra-high pricing means of enterprises refuse to compromise with the consumption trend and aim at the high-end group to maintain the top brand position. Hermes' top premium ability is based on brand value, the "positioning drift" is the last thing they can accept. In order to maintain its top market position and maintain a high price level, Hermes shows a strong performance in terms of price. It not only rarely launches discounts, but also realizes "preserving value" through regular price increases.

In terms of brand building, Hermes adheres to single-brand and multi-series strategies to continuously contribute to the upgrading of brand value. But as rivals such as LVMH and Kering group have seen their revenues soar through social networks and catering to young consumers, Hermes has also made cautious adjustments [8]. For example, in October 2017, it opened a limited-time store on WeChat public account to sell the smart Watch Apple Watch Hermes Series 3 launched in cooperation with Apple.

5.2 Handmade to Ensure Quality and Unique

At the beginning of its establishment, Hermes adhered to the principle of manual production [9]. Although the progress of industrialization has made manufacturing more efficient and accurate, Hermes's original intention has not changed. As Axel Dumas, the sixth generation of Hermes, said, "The main strength of Hermes comes from the love of craftsmanship. The philosophy of Hermes is to let craftsmanship survive. [10]" To this day, Hermes continues to integrate the raw material supply chain upstream, acquiring leather processing companies, and hiring craftsmen in France to stitch every Kelly bag and Birkin bag. Hermes raises silkworms on Brazilian farms and hires local artisans to make silk in Lyon, keeps its own perfume laboratory specially recruit smell discriminator to design the smell of each perfume. Meticulous manual craftsmanship is a solid guarantee for product quality, and the individual craftsmanship style reflects the difference of artistic expression and meets the customization needs of the guests to the greatest extent.

6. Conclusion

Due to the financial analysis, the overall operating performance of the company lies in a stable growth state. In recent years, revenue has remained above 6 billion euros. In the past ten years, the gross margin has maintained at 66%-70%, and the net margin has maintained at 17%-24%, which ranks a leading level in the luxury industry. What's more, the financial ratio indicators are maintained at a stable and controllable level, reflecting the company's healthy operation state from the inside out.

Due to the market analysis with SWOT and industry comparison, Hermes maintains a sense of scarcity and distinguishes itself from other groups in advertising methods. The success of Hermes begins with the ingenuity of the original founder and carries forward to the inheritance of future generations. It benefits from the sincere unity of the family and the recognition and love of the brand value and culture.

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