November Article

Il Cavallino Rampante

A popular Italian saying says that God had to invent dreams because of Italian ice cream and cars. I am not particularly fond of ice cream but since last month I no longer have to dream of having a Ferrari since I can be the owner of a couple Ferrari's shares for a reasonable amount of approx. USD 51 (NYSE:RACE).

Ferrari went public last month following a well-defined strategy by Fiat-Chrysler's CEO, Sergio Marchionne, to raise funds for its EUR 48bn R&D program at Fiat-Chrysler. This program included the sale of a 10% stake in Ferrari that would value it between USD 9.6bn and USD 10.4bn. The results of the IPO came out on within the range with a share price of USD 52 (USD 9.8bn) which corresponds to an Net Income to EV multiple of 40, more in line with values of luxury brands than automotive companies.

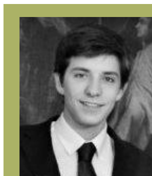
The roadshow made for Ferrari was supported by two selling points that differentiate it from every other car company. The first one is the exclusivity of the cars sold that directly relates to the prices charged, the stickiness of sales, and indirectly to the operating margins (18%, well above market average but still below most luxury fashion companies). The second is the brand value itself and how it can be explored even more in the future - with theme parks, merchandising products or range expansion, for example.

These characteristics are allied with a perspective to increase sales from the current 7000 units per year to a whopping 9000 units in 2019 (30% increase), whilst at the same time maintaining current margins. These inputs made Mr Marchionne and the investors believe that Ferrari would be worth 14 times the current EBITDA of EUR 693M.

As an irrational agent and a feverous car enthusiast I have to say I find the price of Ferrari within all reasonable standards, even more if you consider you will actually own a "Ferrari". However through some quantitative and qualitative valuation one can see the value is a bit far off.

First of all it will be difficult to increase sales volume without compromising existing margins and current demand. After all, Ferrari's exclusivity is based on its long waiting list and limited production. Given such, one might wonder if without the ultra-exclusivity the top 1% will remain interested in buying one of these cars at the current prices. The second problem comes from the lack of investment both in the Scuderia and in the road cars if Mr. Machionne decides not to reinvest the proceeds of this deal in Ferrari - as it was announced. Besides looking good, a Ferrari has to perform well and win titles in order to compete with a much bigger Mercedes-Daimler and if it the cars don't run well and don't win titles sales will be affected. Thirdly there is a concern about the health and duration of the contracts with Maserati to produce their V8/V6 engines. This is an important topic seeing that these contracts will represent almost 5% of Ferrari's revenues by 2020 and unlike Ferrari, Maserati is more exposed to cyclical conditions.

When putting these values all together there is a consensus that the true value of Ferrari should lie anywhere between EUR 6.2 and 7.6 bn. This value represent a EV/EBITDA multiple between 9 and 11 which is still much higher than the average for the automotive industry (approx. 7) and it is one that I think reflects both the exclusivity of the company and the challenges it will face in the next few years including the slowdown in its "growth markets" such as China or the Middle East that represent almost 17% of total sales volume.



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