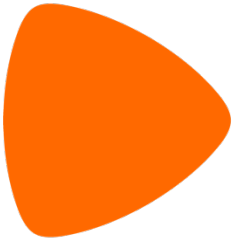


Louvain School of Management

Fundamental Equity Valuation

Zalando SE

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zalando

Foreword

I am sincerely grateful to my supervisor, Professor Philippe Grégoire, for his invaluable guidance throughout this research journey. His insightful feedback, and most importantly, his encouragement to adopt a personal approach to valuation instead of simply replicating standard banking practices have been instrumental in elevating the quality of this thesis. Though not without its challenges, especially given my background as an Investment Banking Intern at ING, I am thoroughly convinced that his mentorship has taken my work to the next level.

I am also thankful to Laurent Clerbois, Senior Investment Banking Associate at Degroof Petercam, for generously providing financial data and offering critical insights on various aspects of my valuation.

Furthermore, I wish to express my deep gratitude to my father for engaging in countless brainstorming sessions with me during the development of my assumptions. His unwavering support has been a constant source of inspiration.

Finally, I would like to thank my family as a whole for their continuous support during my studies.

N.B.: Starting from this point, the pronoun "We" will be used instead of "I" throughout this report as a personal preference in adherence to scientific writing style.

List of Abbreviations

A	Actual
Adj	Adjusted
AI	Artificial Intelligence
AVG	Average
Bn	Billion
CAGR	Compound Annual Growth Rate
CapEx	Capital Expenditures
CAPM	Capital Asset Pricing Model
COGS	Cost of Goods Sold
D&A	Depreciation and Amortization
DACH	Germany, Austria, Switzerland
DCF	Discounted Cash Flow
E	Estimated
EBIT	Earnings Before Interests, and Taxes
EBITDA	Earnings Before Interests, Taxes, Depreciations, and Amortizations
EBT	Earnings Before Taxes
EM	Exit Multiple
ESG	Environmental, Social, and Governance
EUR	Euros
FCFF	Free Cash Flow to the Firm
FS	Fashion Store
GGM	Gordon Growth Model
GMV	Gross Merchandise Volume
M	Million
N.B.	Nota Bene
Nb	Number
NOPAT	Net Operating Profit After Taxes
NWC	Net Working Capital
OAS	Option Adjusted Spread
OPEX	Operating Expenses
PB	Partner Business
PP	Percentage Points
PV	Present Value
Q	Quarter
RoE	Rest of Europe
TV	Terminal Value
WACC	Weighted Average Cost of Capital
Zalando	Zalando SE
Δ	Delta

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Introduction

Valuation is as much science as art. On one hand, “it is based on principles of finance and accounting”, while on the other hand, “it is an art to be able to forecast the future of a company based on the knowledge that you acquire” (Glode, 2022). Thousands of analysts strive daily to determine whether a company’s stock price is undervalued, overvalued, or correctly valued for successful investments. However, almost none of them agree on the same target price. This is where the art of corporate valuation comes into play. Obviously, each valuation is slightly subjective and tends to incorporate some bias. The only questions are how much and in which direction. Damodaran (2017) notes that “the direction and magnitude of the bias in your valuation are directly proportional to who pays you and how much you are paid”.

In this report, we will conduct a fundamental analysis of Zalando as a whole to provide our best and least biased estimates of its true and fundamental value. Our approach emphasizes personalization and originality, challenging typical banking practices throughout the report.

We begin by presenting Zalando, delving into the intricate details that make it the European leader in online fashion. This includes an explanation of Zalando's complex business model, ambitious vision, strategy, and the competitive landscape it operates in. We proceed with a historical financial analysis and a SWOT analysis to enhance our future forecasting.

The second part of this report outlines our top-down approach to forecasting Zalando's future financials over a five-year period. These forecasts are largely based on future market trends, historical key driver evolution, and some carefully documented assumptions.

Next, in the third part, we perform two versions of the Discounted Cash Flow valuation: one using the terminal value derived from the Gordon Growth Method and the other using an Exit Multiple based on a peer analysis. These methods yield an implied share price for Zalando.

We then conduct both an ESG and a Reputation analysis to assess whether a premium or discount should be applied to our implied share price.

Finally, we present a sensitivity analysis on four specific factors influencing our forecasted FCFF, incorporating elements identified in our SWOT analysis. This tailor-made sensitivity analysis is based on realistic scenarios, producing a valuation range from which our final target price will be derived.

This report concludes with a definitive buy or sell recommendation based on the various levels of analysis performed compared to the share price of Zalando as at July 31, 2023.

Our analysis, conducted within an academic framework and entirely free from any financial interests, might well be leading to a sound recommendation for consideration. The decision now rests in your hands.

Part 1: Company Presentation

Company history

Zalando is a European online fashion retailer that was founded in 2008 in Germany by Robert Gentz and David Schneider, just before the financial crisis hit. The founders of Zalando were supported by the Samwer brothers, who are significant investors in the e-commerce market. Zalando initially specialized in the online sale of shoes before gradually expanding into a wider fashion offering. The company quickly set new standards in online retail by offering free delivery and a 100-day right-of-return policy (Zalando SE, 2023). Zalando's first international markets were Austria and Switzerland, followed by the Netherlands in 2010 (Zalando SE, 2023). Today, Zalando serves over 50 million active customers across 25¹ European countries and has a logistics network that includes 13 fulfillment centers. The company currently employs around 17,000 people from over 140 countries and is led by a management board comprising Robert Gentz (Co-CEO), David Schneider (Co-CEO), Dr. Sandra Dembeck (CFO), Dr. Astrid Arndt (CPO), and David Schröder (COO) (Zalando SE, 2023). The group is listed on the Deutsche Börse XETRA since 2014 and joined the DAX-40 index in September 2021. In 2022, Zalando achieved a revenue of 10.3 billion EUR.

Segments

Zalando's internal management structure is divided into three segments ("Fashion Store", "Offprice", and "Others") based on a sales channel perspective.

Fashion Store

The main segment is the Fashion Store, which includes the Zalando app and website as sales channels. This segment accounts for 81.78%² of Zalando's total revenue in 2022 (Zalando SE, 2022). The Fashion Store segment itself is divided into two subsegments, namely the Wholesale segment and the Partner Business segment.

The Wholesale segment simply means that Zalando buys inventory from brands and sells it for its own account to customers. In 2022, the Wholesale segment contributed the largest share of

¹ Annex 2 – Zalando's geographical expansion

² Annex 3 – Segment results of the group 2022

Zalando's Fashion Store Gross Merchandise Volume (GMV)³ at 64% and of Zalando's total GMV at 56%. The company views the Wholesale model as “an essential pillar in its assortment strategy and one of the strongest tools that they have to secure "must-have" assortment for their customers across Europe” (Zalando SE, 2022).

The Partner Business segment “enables brands and retailers to sell their merchandise via Zalando while maintaining full control over their offer, content, and pricing” (Zalando SE, 2022) in exchange for a commission and a fixed monthly fee. The commission fee for sales on Zalando is determined by the product type and its price, typically ranging somewhere between 5% and 25% (Koongo, 2023). The total average take rate is not disclosed by Zalando and will thus be estimated in Part 2. Partner Business GMV contributed 36% of Zalando's Fashion Store GMV and 32% of Zalando's total GMV at the end of 2022 (Zalando SE, 2022). Zalando aims to increase its share of Partner Business GMV towards 50% of Fashion Store GMV by 2025, with a 75% share of items shipped through Zalando Fulfillment Solutions (Zalando SE, 2021). “Zalando Fulfillment Solutions (ZFS) is a key add-on service to the Partner Program which allows brand partners to leverage Zalando's European logistics network across 23 markets” (Zalando SE, 2022).

Offprice

The Offprice segment includes the sales channels Lounge by Zalando (Lounge by Zalando app and website), 13 brick-and-mortar outlet stores across Germany, and B2B overstock management. This segment is the second largest segment after the Fashion Store segment, and it accounts for 15.44%⁴ of Zalando's total revenue in 2022 (Zalando SE, 2022).

Others

The Others segment bundles the emerging business Zalando Marketing Services, the integrator business Tradebyte, and the global fashion media brand Highsnobiety, acquired in July 2022 (Zalando SE, 2022). This segment accounts for the remaining 2.78%⁵ of Zalando's total revenue in 2022 (Zalando SE, 2022).

³ Gross Merchandise Volume = The value of all merchandise sold to customers after cancellations and returns and including VAT, dynamically reported.

⁴ Annex 3 – Segment results of the group 2022

⁵ Annex 3 – Segment results of the group 2022

Vision and strategy

The company's vision is to be the "Starting Point for Fashion" and it aims to achieve this by focusing on three core strategic dimensions (Zalando SE, 2022). Firstly, they aim to grow their active customer base by being relevant to multiple customer audiences across Europe. Secondly, they continue to focus on driving their transition towards a true platform business model, enabling business opportunities for brands and retailers by connecting them to consumers across Europe. Lastly, they are committed to building a fashion platform with a net-positive impact for people and the planet by leveraging the scale of Zalando and the strong relationships with their partners (Zalando SE, 2022).

Market

Zalando mainly operates in the e-commerce market for fashion and lifestyle products, which is divided into three segments: Apparel, Footwear and Accessories. Zalando is active in all three of them. More recently, Zalando expanded into new markets such as the e-commerce market for beauty products, within its Fashion Store segment, and the e-commerce market for home furniture, within its Offprice segment. However, both these categories are considered marginal as they represent less than 5% of Zalando's 2022 revenues according to Nils Poeppinghaus, Senior Manager Investor Relations at Zalando.

The fashion e-commerce market is highly competitive and dynamic, with various types of players competing for market share. These include brand marketplaces like Zalando, ordinary players with an established online presence like H&M, and generalists like Amazon. According to Statista, Europe is experiencing significant growth in fashion e-commerce, with a projected Compound Annual Growth Rate (CAGR) of +10.45% from 2022 to 2027 in the countries where Zalando operates (Statista, 2023).

To provide a comprehensive overview, Table 1 presents a peer group of Zalando's competitors who operate in the same regions and present similarities in their respective business models. The listed competitors will be further used in our relative valuation to determine Zalando's terminal value.

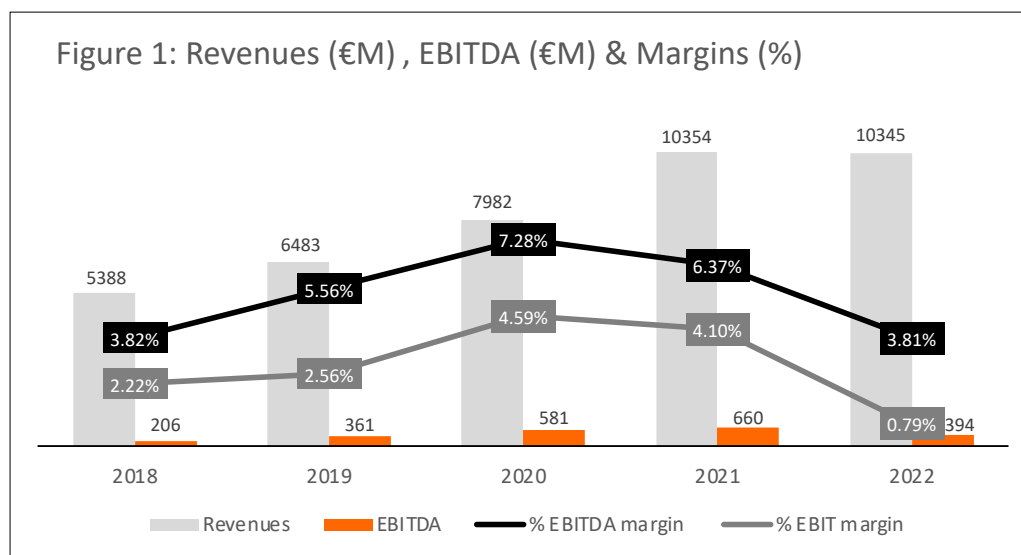
Table 1: Competitive overview			
Company	Revenue	Description	Listed
About You	€1.7bn	“Founded in 2014 in Hamburg, About You is one of Europe's fastest-growing online fashion stores of scale. It digitizes the classic shopping stroll by creating an inspiring and personalized shopping experience on the smartphone. With more than 45 million unique active users per month, About You is currently active in 26 European markets” (About You, 2023).	Yes
Asos	€4.6bn	“Founded in 2000, Asos is an online fashion and cosmetic retailer based in London, England. The website is aimed at young adults, ships to 196 countries, and cooperates with more than 850 brands. By incorporating smaller brands into its business, ASOS not only gained more profit from individual sellers but increased its popularity among younger generations and fashion enthusiasts” (Statista, 2022).	Yes
Boohoo	€2.3bn	Founded in 2006 and headquartered in Manchester, Boohoo is an online fashion retailer that primarily sells its own brands Nasty Gal and MissPap. It designs, sources, markets, and sells clothing, shoes, and accessories for men, women, and children.	Yes
Boozt	€0.6bn	Founded in 2009 and headquartered in Malmö, Sweden, “Boozt is a multi-brand online fashion & lifestyle shop with more than 1000 brands split into the main categories; Women, Men, Kids, Sports, Beauty and Home” (Boozt, 2023). It mainly sells Nordic brands, but it also has a wide selection of strong international brands.	Yes
Farfetch	€2.2bn	“Farfetch, headquartered in the United Kingdom and operating on a global scale since 2008, is a marketplace selling products from its own inventory and third-party sellers. The company positions itself as a luxury fashion retail platform” (Statista, 2022).	Yes
Next	€5.8bn	Headquartered in Leicester, UK, Next is one of the largest clothing and home product retailers in the UK, with a significant international online presence and a chain of physical stores. Next offers a wide range of clothing, footwear, accessories, and home goods for men, women, and children, catering to different styles, sizes, and budgets.	Yes
Shein	n.a.	Founded in 2008 and headquartered in China, Shein is an international online fashion retailer known for its fast-fashion business model and strong online presence around the world. It primarily sells its own brands offering a wide range of trendy clothing, footwear, accessories, and beauty products for women, men, and children at affordable prices.	No
Vinted	n.a.	Founded in 2008 and headquartered in Vilnius, Lithuania, Vinted is an online peer-to-peer marketplace for buying, selling, and swapping second-hand clothing, footwear, accessories, and home goods. Vinted operates primarily through its website and mobile app, providing a platform for individuals to connect and transact in a secure manner.	No

Source: Company data, FactSet, Statista

Historical financial analysis

In this section, we will analyze different financial metrics and their evolution over the past five years in order to help us better forecast the future.

Revenues, EBITDA and Margins



Source: FactSet

Zalando's revenues nearly doubled from 5,388 million EUR in 2018 to 10,354 million EUR in 2021, exhibiting a robust CAGR of +24.33% over that period. The EBITDA has come from 206 million EUR to 660 million EUR over the same period, growing at an impressive CAGR of +47.44%.

In contrast to its steady growth in previous years, Zalando faced a more challenging year in 2022 with revenues remaining stable at 10,345 million EUR and EBITDA declining to 394 million EUR, lowering both CAGR for the '18-'22 period to respectively +17.71% and +17.60%. This signals a significant deviation from its growth trajectory over the last few years. The company's management board attributed this deviation to a range of external factors that impacted the e-commerce industry as a whole. Specifically, as pandemic-related restrictions lifted, consumers returned to in-store shopping, causing a reversal of the adoption of e-commerce that was more significant than initially anticipated. Additionally, a higher-than-anticipated increase in inflation hurt consumer sentiment, further impacting sales. Finally, supply chain bottlenecks at the beginning of the year followed by elevated inventory levels across the market in the second half of the year added further challenges for Zalando to overcome (Zalando SE, 2022).

The EBITDA margin stayed relatively low over the years, ranging between 3.81% and 7.28%, with a historical average of 5.37%. The EBIT margin fluctuated between 0.79% and 4.59%, with a historical average of 2.85%. This is one of the reasons explaining Zalando's ongoing shift in business model from a lower margin wholesale business model to a higher margin pure marketplace business model.

Cost structure

In 2022, Zalando incurred total costs of 10,263 million EUR, accounting for 99.21% of its revenues. Over the past five years, operational costs on average represented 97.15% of Zalando's revenue, resulting in a modest operating income margin of 2.85%. Table 2 provides a detailed breakdown of Zalando's costs into four categories: cost of goods sold (COGS), fulfillment costs, marketing costs, and administrative expenses.

Table 2: Cost structure (€M)	2018	2019	2020	2021	2022	AVG 18-22
Revenues	5388	6483	7982	10354	10345	
All costs	5269	6317	7615	9930	10264	
<i>% of revenues</i>	97.79%	97.44%	95.40%	95.90%	99.21%	97.15%
Cost of goods sold	3107	3724	4588	6028	6289	
<i>% of revenues</i>	57.67%	57.45%	57.48%	58.22%	60.79%	58.32%
Operating expenses	2162	2593	3027	3902	3975	
<i>% of revenues</i>	40.12%	39.99%	37.93%	37.68%	38.42%	38.83%
Fulfillment costs	1497	1772	2050	2585	2704	
<i>% of revenues</i>	27.78%	27.33%	25.68%	24.97%	26.14%	26.38%
Marketing costs	397	522	659	925	792	
<i>% of revenues</i>	7.37%	8.05%	8.26%	8.94%	7.66%	8.05%
Administrative expenses	268	299	318	391	479	
<i>% of revenues</i>	4.97%	4.61%	3.99%	3.78%	4.63%	4.39%

Source: Company data, FactSet

Historically, COGS has consistently been the largest component of Zalando's costs, representing 58.32% of its revenues. Fulfillment costs represent 26.38% of revenues, while marketing costs and administrative expenses account for 8.05% and 4.39% of revenues, respectively. These proportions have remained relatively stable over time, with variances of approximately 3 percentage points for COGS, 3 percentage points for fulfillment costs, 2 percentage points for marketing costs, and 1 percentage point for administrative expenses.

It is noteworthy that, in 2022, all types of costs, except for marketing costs, experienced a slight increase in proportion to revenues. This reflects the difficult year that Zalando and the industry as a whole faced in 2022.

Tax rate

In order to later determine Zalando's Free Cash Flows to the Firm (FCFF) for our DCF valuation, we first need to estimate the tax rate based on EBIT instead of EBT. To achieve this, we conducted a historical analysis and calculated Zalando's yearly tax rate over EBIT. Over the past four years, Zalando's tax rate over EBIT has been relatively stable, fluctuating between approximately 25% and 30%, with an average of 27.52%. We made the decision to exclude 2018 from our average tax rate calculations as it deviated significantly from the norm. Going forward, we will employ this average tax rate in our forecasts to determine Zalando's FCFF.

Table 3: Tax rate	2018	2019	2020	2021	2022	AVG 19-22
EBIT	119	166	367	424	81	
Income taxes	58	49	92	120	22	
% of EBIT	48.38%	29.63%	25.15%	28.22%	27.06%	27.52%

Source: Company data, FactSet

Depreciation & Amortization, Capital Expenditures and Net Working Capital

Depreciation and amortization (D&A) expenses have shown fluctuations ranging from approximately 1% to 3% of revenues over the past five years, with an average of 2.52%. It is noteworthy that this average is slightly lower than the D&A to revenues proportion of 3.02% observed in 2022.

Zalando's capital expenditures have shown stability as a percentage of revenues throughout the past five years. On average, capital expenditures represent 3.93% of total revenues, which is slightly higher than the 3.40% proportion observed in 2022. However, it is worth noting that these capital expenditures do not include external acquisitions, such as Zalando's significant acquisition of Highsnobiety for 127 million EUR in 2022.

Regarding changes in working capital, there was a notable shift in 2020, transitioning from a negative to a positive value, which reflects the company's altered working capital requirement during the pandemic. However, due to the exceptional circumstances surrounding the pandemic, we have excluded 2020 when calculating Zalando's average change in working capital. Over the years, variations in working capital have remained relatively minimal, averaging around 0.67% of revenues in absolute terms.

Table 4: D&A, CapEx & ΔWC	2018	2019	2020	2021	2022	AVG 18-22
Revenues	5388	6483	7982	10354	10345	
Depreciation & Amortization	87	195	215	235	312	
<i>% of revenues</i>	1.61%	3.01%	2.69%	2.27%	3.02%	2.52%
Capital Expenditures (-)	278	307	250	333	352	
<i>% of revenues</i>	5.17%	4.73%	3.13%	3.22%	3.40%	3.93%
Changes in Working Capital (-)	-24	-58	73	-80	-60	
<i>% of revenues</i>	-0.44%	-0.89%	0.92%	-0.77%	-0.58%	-0.67%*
*Excluding 2020						
Source: Company data, FactSet						

Capital Structure

Zalando's total debt reached a record high in 2020, amounting to 1,768 million EUR⁶. This surge was mainly attributed to the issuance of two tranches (A and B) of convertible bonds in August 2020, each worth 500 million EUR. These convertible bonds were utilized to fund the company's impressive growth during the pandemic, taking advantage of low interest rates. Tranche A (DE000A3E4589) has a five-year tenor and matures in August 2025, while Tranche B (DE000A3E4597) has a seven-year tenor and matures in August 2027. FactSet reports on July 6, 2023, an Option Adjusted Spread (OAS) of 2.55% for tranche A and 4.26% for tranche B, providing insight into the additional yield demanded by investors for the embedded options in these convertible bonds.

Table 5: Debt analysis	Amount (€M)	Maturity	OAS
Tranche A (DE000A3E4589)	500	Aug-25	2.55%
Tranche B (DE000A3E4597)	500	Aug-27	4.26%
Source: Company data, FactSet			
Retrieved on 06/07/2023			

It's important to note that Zalando's remaining long-term debt consists of capital and operating lease obligations, which should not be considered in the computation of the Weighted Average Cost of Capital (WACC). After a decrease of 10.92% in 2021, Zalando's total debt increased back by 9.00% in 2022 to reach 1,717 million EUR. By taking advantage of debt financing and its tax advantages, Zalando's total debt-to-total capital ratio has been increasing over the years, reaching 43.84% in 2022. It is worth noting that Zalando's capital structure has displayed a relatively stable pattern over the past three years, fluctuating between approximately 42% and 45% of debt-to-total capital. Therefore, the most recent capital structure will be employed as target capital structure in the calculation of the WACC.

⁶ Annex 1 - Historical financials

SWOT Analysis

Strengths

- Unassailable scale advantage:

Zalando is the largest pure-play online fashion and lifestyle retailer in Europe, enjoying an overall 11.76% market share in the 25 European countries where it is present (Statista, 2023). With a 2022 revenue 6 times bigger than its nearest competitor About You, Zalando enjoys a dominant position in the market. This scale advantage acts as a barrier to entry for new operators attempting to address the online mass market. Zalando's well-established strategy of connecting brands, retailers, and manufacturers through its end-to-end e-commerce solution further strengthens its position in the market. Additionally, the company has established a robust logistics and delivery network with its 13 fulfillment centers in 7 countries (Zalando SE, 2023), enabling efficient and reliable order fulfillment for its customers.

- Extensive customer base:

Zalando's focus on the wider apparel market allows it to target a larger addressable market compared to competitors such as About You, Asos and Boohoo which primarily target younger cohorts. In this respect, Zalando serves over 50 million active customers across 25 countries in Europe (Zalando SE, 2022). This extensive customer reach provides the company with a significant opportunity for continued growth. Moreover, among these 50 million active customers, two million are members of Zalando Plus, which represents a strong loyalty base that spend three times more than non-Plus members (Zalando SE, 2022), indicating the potential for higher customer engagement.

- Strong cash position:

Zalando's robust cash position of 2,025 million EUR⁷ as of December 31, 2022, covering more than its total debt of 1,717 million EUR, provides the company with financial flexibility for future investments and growth initiatives, while also enabling it to weather economic

⁷ Annex 1 - Historical financials

uncertainties and potential market fluctuations, ensuring a strong foundation for long-term sustainability.

Weaknesses

- Low pricing power:

Zalando faces challenges in controlling and raising the prices of items sold on its website due to intense competition in the online fashion market. Moreover, its reliance on partnerships and agreements with external brands restricts independent pricing decisions, and its price-sensitive customer base limits its ability to increase prices. This low pricing power leads to low margins, which could impact its profitability. However, Zalando's ongoing shift in business model should increase its pricing power on its B2B clients and consequently increase its margins.

- Limited control over product quality:

Zalando has limited control over product quality when dealing with third-party sellers. By operating as a marketplace, it allows various sellers to offer their products on its platform. This lack of control can result in inconsistencies in product quality, potentially impacting customer satisfaction and increasing returns. Zalando should implement stringent quality control measures and provide clear guidelines to its sellers to mitigate this weakness.

Opportunities

- Increase the share of wallet in established markets:

One opportunity to capitalize on is to increase the share of wallet in the top five markets. For instance, in the DACH (Germany, Austria, Switzerland) countries, Zalando's active customers already account for 23% of the total population (HSBC Global Research, 2023). This can be achieved through category extensions, such as expanding into beauty and premium apparel, which can lead to higher average transaction values. Deepening customer relationships through targeted communication and leveraging the Zalando Plus membership program can also drive an increased share of wallet. For instance, Zalando's recent acquisition of Highsnobiety helps them identify the right customers to target with premium product drops. The two million Plus customers spending three times more on average than non-plus customers, represent less than 4% of the total active customer base of Zalando (Zalando SE, 2022).

- Expansion into recently entered and new markets:

The continued shift in consumer spending to online channels across Europe, coupled with the 10.45% annual projected growth of the online fashion market, presents a positive market opportunity for Zalando. For instance, in Eastern Europe, Zalando's active customers account for only 3% of the total population (HSBC Global Research, 2023). Moreover, the online penetration rates for fashion e-commerce in large addressable markets in Eastern Europe and Southern Europe are currently less than half those of developed markets like Germany and the UK (Statista, 2022). This presents significant growth opportunities for the company.

- Optimization of Zalando Fulfillment Services:

By expanding the reach of its fulfillment services (ZFS) as a third-party provider, Zalando can access a larger portion of the European apparel and lifestyle market that falls outside Zalando's primary focus. This strategic move that was launched last year has opened up opportunities for ZFS to generate additional revenue through incremental fees. In one year, ZFS has successfully handled over 50,000 items on behalf of ten key partners, highlighting the early success and potential of this venture (HSBC Global Research, 2023).

- Leveraging artificial intelligence:

Zalando, far-sighted in its approach, recognized the potential of artificial intelligence (AI) long before it gained widespread public attention with the emergence of AI-generated prompt-and-response tools like ChatGPT in late 2022. By proactively investing in AI and data science, Zalando has positioned itself at the forefront of technological advancements in the fashion retail industry. However, we believe that AI remains more of an opportunity than a fully established strength for the company, given the continuous evolution and disruptive nature of this technology in the fashion retail industry.

Zalando has long understood the multitude of benefits that AI can bring to its business and has accordingly positioned AI as one of its key priorities. The company already employs around 120 researchers dedicated to machine learning and 2500 software engineers across various teams, enabling the development of advanced AI capabilities (ai.nl, 2022). One such example is the Algorithmic Fashion Companion (AFC) launched in 2018, which utilizes machine learning algorithms to identify different clothing items and provide outfit suggestions based on

customers' previous purchases. Zalando's commitment to enhancing its services extends to using AI for logistics optimization, fraud prevention, and meeting seasonal demand effectively. Robots at fulfillment centers assist human workers in item identification, retrieval, and delivery, while smart algorithms provide insights into delivery timing and customer satisfaction (Karl, 2022).

As Zalando continues to invest in AI, it unlocks a wealth of opportunities. For instance, AI can play a pivotal role in reducing returns caused by sizing issues, improving operational efficiency and customer satisfaction simultaneously. Furthermore, AI can drive sustainability initiatives by optimizing warehouse networks, reducing delivery times, and minimizing single-item shipments, thereby reducing the company's environmental footprint. Additionally, AI can power customer segmentation, personalized product recommendations, and intelligent site search to enhance the overall shopping experience. Predictive analytics can enable Zalando to anticipate customer purchases, optimize inventory management, recommend ideal price points, and achieve contextual personalization (Kellet, 2023). By harnessing the potential of AI, Zalando can deliver the right products to the right customers at the right time.

Threats

- Competitive environment:

Even though it is the largest pure-play online fashion and lifestyle retailer in Europe, Zalando's competitive environment remains intense, with the presence of established competitors and the potential entry of new players. Zalando must continuously innovate and improve the user experience to meet customer expectations and differentiate itself from competitors. Neglecting necessary changes could result in customer migration and revenue losses (Zalando SE, 2022).

- Macroeconomic downturn:

Economic uncertainty and volatility can affect consumer spending patterns and purchasing decisions, potentially leading to decreased demand for fashion and lifestyle products. The high inflation in 2022 has hurt consumer sentiment and was one of the reasons for the low sales in 2022. Additionally, the high inflation has led Germany, Zalando's main market and Europe's largest economy, to fall into a "technical recession" after two consecutive quarters of contraction, i.e., -0,5% GDP growth during the last quarter of 2022 and -0.3% GDP growth in

the first quarter of 2023 (Federal Statistical Office of Germany, 2023). In Europe, the consumer price inflation has risen to its highest level since the 2008 financial crisis, potentially leading to a reduced portion of the disposable household income being allocated to fashion expenses (Zalando SE, 2022).

- Cyber-attacks and data protection:

To safeguard customers and the business, it is necessary to continuously monitor threat intelligence and adapt security measures in response to new and emerging threats. Zalando prevented about 500,000 suspicious emails from entering their environment and blocked over 19 billion attacks in 2022. Millions of users entrust Zalando with their personal information, so it is its responsibility to handle it responsibly and guard it against unauthorized access. In this regard, Zalando must consistently abide by various local legal frameworks regarding data protection and privacy in order to avoid facing harsh penalties (Zalando SE, 2022).

Table 6: SWOT summary	
Strengths	Weaknesses
<ul style="list-style-type: none"> - Unassailable scale advantage - Extensive customer base - Strong cash position 	<ul style="list-style-type: none"> - Low pricing power - Limited control over product quality
Opportunities	Threats
<ul style="list-style-type: none"> - Increase the share of wallet in established markets - Expansion into recently entered and new markets - Optimization of Zalando Fulfillment Services - Leveraging artificial intelligence 	<ul style="list-style-type: none"> - Competitive environment - Macroeconomic downturn - Cyber-attacks and data protection

Part 2: Forecasting

Revenues

Baseline

To forecast Zalando's revenues, we employed both a geographical approach, aligned with Zalando's reporting, distinguishing revenues from the DACH countries (Germany, Austria, and Switzerland) and revenues from the Rest of Europe (Belgium, Croatia, Czech Republic, Denmark, Estonia, Finland, France, Hungary, Ireland, Italy, Latvia, Lithuania, Luxembourg, Netherlands, Norway, Poland, Romania, Slovakia, Slovenia, Spain, Sweden, and the United Kingdom) and a business model approach. To address the dynamic and rapidly evolving nature of Zalando's industry, we have focused our predictions on the next five years. This timeframe allows us to provide forecasts that are relevant and reliable, considering the challenges associated with accurately projecting cash flows beyond 2027. Additionally, Zalando's historical cash flows have exhibited significant year-to-year variations, limiting their reliability as a benchmark for future projections. In our analysis, we referred to Statista's latest growth forecasts for the online fashion market, which is Zalando's core revenue driver. These forecasts were examined on a country-by-country basis, covering the period from 2022 to 2027. We specifically focused on these forecasts as other product categories, such as beauty products (within the Fashion store segment) and home furniture (within the Offprice segment), reportedly contribute to less than 5% of Zalando's revenues, as confirmed by Nils Poeppinghaus, Senior Manager Investor Relations at Zalando.

Instead of using the average yearly growth rate across all countries in which Zalando operates, we allocated weights to the yearly growth rates, based on Zalando's 2022 GMV in each country, which is derived from Zalando's respective market share in each country (see Annex 4). This approach helps mitigate the impact of very high or very low growth rates in countries where Zalando has a smaller presence. Given that Zalando experienced an increase in GMV between 2021 and 2022, while Statista reported an average decline of 2.55% in the total market during the same period, we made a slight adjustment to moderate Statista's initial growth rate of +13.04% for the period between 2022 and 2023. This adjustment was achieved by using the 2021-2023 growth rate instead of the 2022-2023 growth rate for countries that demonstrated a decline between 2021 and 2022. By doing so, we aim to present a more accurate representation of Zalando's actual performance in the market. Based on these calculations, we arrived at a

weighted adjusted growth rate for Zalando's GMV of +10.25% in 2023, +15.51% in 2024, +14.60% in 2025, +5.15% in 2026, and +6.39% in 2027.

To calculate the revenues based on the forecasted GMV, we have to take into account the variations in business models. Indeed, over the past five years, Zalando's GMV has grown on average by 4.53 percentage points more than revenues each year, mainly due to the strong growth of the Partner Business (Zalando SE, 2022). Consequently, we have chosen to split the projected GMV into two categories: Partner Business GMV, which represents the GMV generated through Zalando's pure marketplace business model (Partner program and Connected Retail), and Rest of GMV, which reflects the part of GMV that is mainly generated through the Wholesale and Offprice segments.

In forecasting the growth of Partner Business GMV, we made certain assumptions. Firstly, we assumed that the proportion of Fashion Store GMV to total GMV would remain stable at 88%. Secondly, we predicted that the Partner Business GMV would follow Zalando's business plan, increasing from 36% of the Fashion Store GMV in 2022 to 50% in 2025. This projection appears achievable, considering the similar growth of this proportion in the past two years. As we lack further indications beyond 2025, we decided to maintain it at a constant 50% for 2026 and 2027. Table 7 illustrates the progression of both the Partner Business GMV and the Rest of GMV over the 2022-2027 period.

Table 7: Zalando GMV by business model (€M)	A2022	E2023	E2024	E2025	E2026	E2027	CAGR 22-27
GMV	14798	16314	18844	21595	22708	24160	10.30%
% Growth		10.25%	15.51%	14.60%	5.15%	6.39%	
Partner Business GMV	4683	5736	7454	9491	9980	10619	17.79%
% Fashion Store GMV	36%	40%	45%	50%	50%	50%	
% of GMV	32%	35%	40%	44%	44%	44%	
Rest of GMV	10115	10578	11390	12104	12728	13542	6.01%
% of GMV	68%	65%	60%	56%	56%	56%	

Source: Company data, Statista, Juan Coppens estimates

Using this information, we can then calculate Zalando's projected revenues by breaking them down into revenues from Partner Business and Other revenues. To estimate revenues from Partner Business, we multiply the Partner Business GMV by Zalando's take rate. The take rate represents the fees collected by online marketplaces for enabling third-party transactions (Modern Treasury, sd) and is calculated as a percentage of the GMV.

Although we don't have specific details about Zalando's average take rate, aside from a selling commission ranging between 5% and 25% and an unknown fixed monthly fee, we make an

estimation by examining the typical take rates of companies with a pure marketplace business model. The graph in Annex 5 – Platform take rates, illustrates the take rates of 37 different online platforms. Among these companies, six are primarily involved in the online fashion industry: StockX, GOAT, Etsy, Poshmark, Faire, and Farfetch. Their respective take rates are 12%, 13%, 17%, 19%, 19%, and 32%.

To determine Zalando's take rate, we decided to use the average take rate of 19%⁸. This choice appears reasonable, considering that Farfetch (32%) operates as a luxury brand marketplace and can command a higher take rate while still ensuring brand profitability. On the other hand, brands selling on platforms like Etsy (17%) generally have lower gross margins and, therefore, can only accept a lower take rate to maintain profitability.

To calculate the remaining revenues, we make the assumption that the proportion of Other revenues to Rest of GMV in 2022 will remain constant at 93%. With this information, we can determine the growth rates for overall revenues, resulting in +6.12% in 2023, +9.89% in 2024, +8.74% in 2025, +5.15% in 2026, and +6.39% in 2027, as presented in Table 8.

Table 8: Zalando implied revenues forecasts (€M)	A2022	E2023	E2024	E2025	E2026	E2027	CAGR 22-27
Revenues	10345	10978	12063	13117	13793	14675	7.24%
% Growth		6.12%	9.89%	8.74%	5.15%	6.39%	
Revenues from Partner Business	890	1090	1416	1803	1896	2018	17.79%
% Growth		22.50%	29.94%	27.33%	5.15%	6.39%	
% of total revenues	8.60%	9.93%	11.74%	13.75%	13.75%	13.75%	
Other revenues	9455	9888	10647	11314	11897	12658	6.01%
% Growth		4.58%	7.68%	6.27%	5.15%	6.39%	
% of total revenues	91.40%	90.07%	88.26%	86.25%	86.25%	86.25%	

Source: Company data, Juan Coppens estimates

Below, Table 9 illustrates the geographic distribution of revenues for the upcoming five years knowing that revenues generated in the DACH countries accounted for 43% of total revenues in 2022 and assuming that this proportion will remain stable over time.

Table 9: Zalando implied revenues by region (€M)	A2022	E2023	E2024	E2025	E2026	E2027	CAGR 22-27
Revenues	10345	10978	12063	13117	13793	14675	7.24%
% Growth		6.12%	9.89%	8.74%	5.15%	6.39%	
DACH	4448	4720	5187	5640	5931	6310	7.24%
% Growth		6.12%	9.89%	8.74%	5.15%	6.39%	
% of total revenues	43%	43%	43%	43%	43%	43%	
Rest of Europe	5897	6257	6876	7477	7862	8365	7.24%
% Growth		6.12%	9.89%	8.74%	5.15%	6.39%	
% of total revenues	57%	57%	57%	57%	57%	57%	

Source: Company data, Juan Coppens estimates

⁸ Annex 6 – Computation average take rate

Adjustments

These implied growth rates assume that the market will evolve exactly as predicted by Statista, that Zalando's growth will be proportional to the market growth, and that revenues in both regions will keep the same proportion. However, as we believe this may not perfectly reflect Zalando's future growth, we have made further adjustments based on different factors that we mentioned in our SWOT analysis.

- Macroeconomic factors:

While Statista's figures were updated in July 2023 and claimed to incorporate the market impacts of the Russia-Ukraine war, it is noteworthy that Zalando experienced only a modest revenue growth of +2.3% during the first quarter of 2023. This lower growth was attributed to "a continued challenging economic environment with high inflation" (Zalando SE, 2023). As a result, we have opted to adjust the overall growth forecast derived from Statista's figures for 2023 by deducting 3.8 percentage points. This adjustment aligns more closely with Zalando's actual growth performance in the first quarter of the year.

- Competitive factors:

Given Zalando's dominant market leader position and its already strong presence in all three DACH countries, the task of gaining additional market share or defending its current share becomes increasingly challenging compared to other European countries where it assumes a more outsider position. Over the past three years, Zalando's Fashion Store revenues have exhibited higher growth rates in the Rest of Europe than in the DACH region. This growth rate delta was 2.85 percentage points in 2021, 5.70 percentage points in 2022, and 3.88 percentage points in the first quarter of 2023.

To establish a benchmark for future projections, we used the delta of Q1 2023 (compared to Q1 2022), which stands at 3.88 percentage points. However, as Fashion Store revenues contribute to 81.78% of the total revenues, we multiplied the delta by this proportion, resulting in 3.17 percentage points.

Consequently, in order to accurately reflect the growth rate disparity between the regions, we decided to subtract 3.17 percentage points from the implied yearly revenue growth rates for the

DACH countries from 2023 to 2027. This adjustment allows us to account for the varying growth dynamics across different regions.

- Internal factors:

As stated in the opportunities section of our SWOT analysis, Zalando's two million Plus customers, who spend three times more on average than non-Plus customers, currently make up less than 4% of the total active customer base (Zalando SE, 2022). However, by increasing the number of Plus members to 5% of the total active customer base, Zalando could mathematically boost its revenues by approximately 1.85%. Achieving this increase in proportion, which would require around 500,000 additional Plus members, is feasible within a year's time. We base this belief on the fact that Zalando managed to increase the share of Plus members by approximately 1.8 percentage points between 2021 and 2022, adding around 1 million new Plus members.

Following a similar pattern, we anticipate that this proportional increase of 1 percentage point in Plus members can be replicated each year until 2027, resulting in the proportion of Plus members reaching 9% of all active customers. As a result, we have decided to incorporate a 1.85% increase into the overall revenue growth forecast for the years 2023, 2024, 2025, 2026, and 2027, reflecting the potential growth stemming from this initiative.

Overall, Table 10 provides a summary of our various growth adjustments. In 2023, the projected growth rate for the DACH countries has been revised downward, leading to a total reduction of 5.12 percentage points. In the following years, from 2024 to 2027, there will be a continued downward revision with a yearly decrease of 1.32 percentage points. Similarly, for the Rest of Europe, the forecasted growth rate for 2023 has been revised downward, leading to a total reduction of 1.95 percentage points. Nevertheless, the outlook for the years 2024, 2025, 2026, and 2027 has been revised upward, with an additional 1.85 percentage points in growth rate for each year.

Table 10: Growth adjustments (pp)	E2023	E2024	E2025	E2026	E2027
DACH growth adjustments	-5.12%	-1.32%	-1.32%	-1.32%	-1.32%
Macroeconomic factors	-3.80%				
Competitive factors	-3.17%	-3.17%	-3.17%	-3.17%	-3.17%
Internal factors	1.85%	1.85%	1.85%	1.85%	1.85%
Rest of Europe growth adjustments	-1.95%	1.85%	1.85%	1.85%	1.85%
Macroeconomic factors	-3.80%				
Competitive factors					
Internal factors	1.85%	1.85%	1.85%	1.85%	1.85%

Source: Juan Coppens estimates

This leads us to a final projected growth of +1.00% in 2023, +8.57% in 2024, +7.42% in 2025, +3.83% in 2026, and +5.07% in 2027 for the revenues in the DACH countries and of +4.17% in 2023, +11.74% in 2024, +10.59% in 2025, +7.00% in 2026, and +8.24% in 2027 for the revenues in the Rest of Europe. Table 11 displays our final revenues forecasts for Zalando over the next five years, which are 10,635 million EUR in 2023, 11,741 million EUR in 2024, 12,829 million EUR in 2025, 13,562 million EUR in 2026, and 14,508 million EUR in 2027.

Table 11: Zalando Final Revenues Forecasts (€M)	A2022	E2023	E2024	E2025	E2026	E2027	CAGR 22-27
Revenues	10345	10635	11741	12829	13562	14508	7.00%
% Growth		2.80%	10.40%	9.27%	5.71%	6.97%	
DACH	4448	4493	4878	5239	5440	5716	5.14%
% Growth		1.00%	8.57%	7.42%	3.83%	5.07%	
% of total revenues	43.00%	42.24%	41.54%	40.84%	40.11%	39.40%	
Rest of Europe	5897	6142	6863	7590	8122	8791	8.32%
% Growth		4.17%	11.74%	10.59%	7.00%	8.24%	
% of total revenues	57.00%	57.76%	58.46%	59.16%	59.89%	60.60%	

Source: Company data, Juan Coppens estimates

EBIT

In order to forecast Zalando's EBIT for the next five years, we started by forecasting Zalando's future expenses. While the historical proportions of each expense type on revenues were relatively stable over the years and their averages could thus have served as a potential benchmark for our projections, we decided to dig deeper and make some adjustments in order to better reflect Zalando's change in business model, aimed at increasing its margins.

- Costs of goods sold (COGS)

In line with our revenue forecasts, we made the decision to break down Zalando's Cost of Goods Sold (COGS) into two categories: COGS from Partner Business revenues and COGS from Other revenues, as they exhibit significant differences. In the context of companies with a pure marketplace business model, they refer to these costs as "Costs of Net Revenues" instead of COGS, often encompassing expenses related to customer support, site operations, and payment processing. However, for the sake of standardization, we refer to them as COGS from Partner Business. Since Zalando does not provide a more detailed breakdown than global COGS, we estimated the COGS from Partner Business by considering the average proportion of Cost of Net Revenues to revenues from the sample of companies used in the estimation of Zalando's take rate. Due to some companies in the sample not being publicly traded and not disclosing such information, we included two additional pure marketplaces, namely eBay and

Fiverr. This allowed us to arrive at an average 2022 proportion of 33.32%⁹ for Costs of Net Revenues to revenues. By multiplying this average proportion by the proportion of revenues generated through the Partner Business, we calculated Zalando's estimated proportion of COGS to revenues attributable to Partner Business.

With knowledge of Zalando's 2022 proportion of COGS to Total revenues, which stands at 60.79%, we then estimated Zalando's COGS from Other revenues at 63.38% of Other revenues, derived from the difference. Table 12 illustrates our approach and already demonstrates a decrease in the proportion of Zalando's COGS to total revenues over the years due to the proportional increase in the Partner Business segment.

Table 12: Implied COGS to revenues (%)	A2022	E2023	E2024	E2025	E2026	E2027
COGS to Total revenues	60.79%	60.39%	59.85%	59.25%	59.25%	59.25%
PB COGS to PB revenues	33.32%	33.32%	33.32%	33.32%	33.32%	33.32%
% PB revenues to Total revenues	8.60%	9.93%	11.74%	13.75%	13.75%	13.75%
Other COGS to Other revenues	63.38%	63.38%	63.38%	63.38%	63.38%	63.38%
% Other revenues to Total revenues	91.40%	90.07%	88.26%	86.25%	86.25%	86.25%

Source: Company data, Juan Coppens estimates

In our analysis of Zalando's historical cost structure (Table 2), we observed that the COGS to revenues proportion increased by approximately 1.5 percentage points from 58.22% in 2021 to 60.79% in 2022, due to factors like prolonged sales periods and high inflation (Zalando SE, 2022). It appears that the average proportion of Cost of Net Revenues to revenues from our marketplace sample also exhibited the same trend, going from 31.78% in 2021 to 33.23% in 2022, representing an increase of about 1.5 percentage points. This suggests that the proportion of other COGS to Other revenues has likely followed a similar evolution.

Given our belief that inflation will decrease in the upcoming years and that Zalando may gradually pass on some of these inflationary effects to its clients, our forecast indicates a positive outlook for Zalando's COGS to revenues proportion in the coming years. We expect Zalando's COGS to recover the 1.5 percentage points increase from 2022 by 2025 at the latest, which implies a gradual decrease of -0.5 percentage point spread over the next three years. Table 13 below outlines our final COGS estimates for Zalando based on this analysis.

⁹ Annex 7 – Evolution of COGS from pure marketplaces

Table 13: Final COGS to revenues (%)	A2022	E2023	E2024	E2025	E2026	E2027
COGS to Total revenues	60.79%	59.89%	58.85%	57.75%	57.75%	57.75%
PB COGS to PB revenues	33.32%	32.82%	32.32%	31.82%	31.82%	31.82%
% PB revenues to Total revenues	8.60%	9.93%	11.74%	13.75%	13.75%	13.75%
Other COGS to Other revenues	63.38%	62.88%	62.38%	61.88%	61.88%	61.88%
% Other revenues to Total revenues	91.40%	90.07%	88.26%	86.25%	86.25%	86.25%

Source: Company data, Juan Coppens estimates

- Operating expenses

In 2022, Zalando's operating expenses represented 38.42% of its revenues, marking an increase of approximately 0.8 percentage point compared to the previous year. Upon closer analysis, we observe that both fulfillment costs and administrative expenses have experienced a respective increase of approximately 1.2 and 0.9 percentage points. These increases can be attributed to investments made in areas such as customer convenience for fulfillment costs, which includes initiatives like express deliveries for Zalando Plus members, and an increase in personnel and IT costs for administrative expenses (Zalando SE, 2022). Conversely, marketing costs have been reduced, leading to a decrease of approximately 1.3 percentage points in their proportion to revenues.

Moving forward, we believe that fulfillment costs will remain at a high level, mainly due to the expected growth in logistics expenses associated with our forecasted increase in Zalando Plus members. Therefore, we forecast that the 2022 proportion to revenues will remain the same in the next five years.

Regarding marketing costs, we anticipate no further reductions in 2023, as the efficiency measures implemented in 2022 have already yielded significant results. As we know, cuts in marketing costs are current during difficult years. We believe marketing costs will thus increase back to their historical average proportion of 8.05% of revenues (see Table 2). However, we do not forecast further proportional increases, essentially tanks to Zalando's recent acquisition of Highsnobiety, aimed at improving Zalando's customer targeting efficiency.

As for administrative expenses, we anticipate that the lower forecasted inflation rates in the short term, combined with increasing economies of scale in IT infrastructure through Zalando's utilization of AI and new technologies, will offset the high increase observed last year in the future. Historically, Zalando has achieved yearly economies of scale in its administrative expenses, transitioning from a proportion of 4.97% of revenues in 2018 to 3.78% in 2021, representing a 1.19 percentage points decrease over 4 years, or a yearly improvement of

approximately 0.3 percentage point. Therefore, we project a consistent annual 0.3 percentage point improvement for the next five years.

This leads us to the following final projected EBIT margins: 1.60% in 2023, 2.94% in 2024, 4.34% in 2025, 4.64% in 2026, and 4.94% in 2027. These projections are in line with Zalando's own estimates, which stand at approximately 5% to 6% adjusted EBIT margin by 2025, equivalent to an EBIT margin of 3.91% to 4.70% using the historical proportion of EBIT margin on adjusted EBIT margin¹⁰. Table 14 below illustrates our projected EBIT of 170 million EUR in 2023, 345 million EUR in 2024, 557 million EUR in 2025, 630 million EUR in 2026, and 717 million EUR in 2027.

Table 14: Zalando EBIT Forecasts (€M)	A2022	E2023	E2024	E2025	E2026	E2027	CAGR 22-27
Revenues	10345	10635	11741	12829	13562	14508	7.00%
Cost of goods sold	6289	6370	6910	7409	7832	8378	5.90%
% of total revenues	60.79%	59.89%	58.85%	57.75%	57.75%	57.75%	
Operating expenses	3974	4096	4486	4864	5101	5413	6.37%
% of total revenues	38.42%	38.51%	38.21%	37.91%	37.61%	37.31%	
Fulfillment costs	2704	2780	3069	3353	3545	3792	7.00%
% of revenues	26.14%	26.14%	26.14%	26.14%	26.14%	26.14%	
Marketing costs	792	856	945	1032	1091	1167	8.07%
% of revenues	7.66%	8.05%	8.05%	8.05%	8.05%	8.05%	
Administrative expenses	479	460	473	478	465	454	-1.06%
% of revenues	4.63%	4.33%	4.03%	3.73%	3.43%	3.13%	
EBIT	81	170	345	557	630	717	54.55%
% EBIT Margin	0.79%	1.60%	2.94%	4.34%	4.64%	4.94%	

Source: Company data, Juan Coppens estimates

NOPAT

To estimate Zalando's future Net Operating Profit After Tax (NOPAT), we multiplied our projected EBIT by (1 - tax rate). In this case, we have assumed a stable tax rate of 27.52% derived from our analysis conducted in the historical financial overview section. Table 15 illustrates our forecasted NOPAT, indicating expected values of 123 million EUR in 2023, 250 million EUR in 2024, 404 million EUR in 2025, 456 million EUR in 2026, and 520 million EUR in 2027.

Table 15: Zalando NOPAT Forecasts (€M)	A2022	E2023	E2024	E2025	E2026	E2027	CAGR 22-27
EBIT	81	170	345	557	630	717	54.55%
Tax rate	27.06%	27.52%	27.52%	27.52%	27.52%	27.52%	
NOPAT	59	123	250	404	456	520	54.35%

Source: Company data, Juan Coppens estimates

¹⁰ Annex 1 - Historical financials

Free Cash Flow to the Firm

Using our projected NOPAT figures, we can easily calculate Zalando's future Free Cash Flow to the Firm (FCFF) by adding back depreciation & amortization expenses, subtracting capital expenditures and changes in working capital.

In our projections, we opted to use the 2022 D&A to revenues proportion of 3.02% for 2023, departing from the historical average. This decision aligns with our forecasts of increasing CapEx in proportion to revenues, as explained in the paragraph below. We assume that D&A expenses will equal CapEx in the long run. Consequently, we have modeled a yearly proportional increase of 0.18 percentage point to align D&A with CapEx in our terminal year, i.e., 2027.

Despite the data in Table 4 showing Zalando's CapEx accounting for a lower proportion of revenues over the past three years compared to the five-year average, we decided to utilize the historical average proportion of 3.93% in our projections for the next five years. This approach ensures that our forecasts incorporate, at least partially, the potential expenses associated with future acquisitions.

Regarding changes in Working Capital, we based our projections on the adjusted historical average of -0.67% as computed in Table 4. By using this adjusted average, we aim to provide a more accurate representation of the company's typical working capital trends and mitigate the impact of extraordinary events, such as the pandemic, on our projections.

Table 16 illustrates Zalando's projected FCFF, with anticipated values of 117 million EUR in 2023, 265 million EUR in 2024, 443 million EUR in 2025, 523 million EUR in 2026, and 617 million EUR in 2027.

Table 16: Zalando FCFF Forecasts (€M)	A2022	E2023	E2024	E2025	E2026	E2027	CAGR 22-27
Revenues	10345	10635	11741	12829	13562	14508	7.00%
EBITDA	393	510	742	1014	1138	1287	26.76%
<i>% EBITDA Margin</i>	3.80%	4.79%	6.32%	7.91%	8.39%	8.87%	
NOPAT	59	123	250	404	456	520	54.35%
<i>% of revenues</i>	0.57%	1.16%	2.13%	3.15%	3.37%	3.58%	
Depreciation & Amortization	312	340	397	457	508	570	12.81%
<i>% of revenues</i>	3.02%	3.20%	3.38%	3.56%	3.75%	3.93%	
Capital Expenditures (-)	352	418	461	504	533	570	10.14%
<i>% of revenues</i>	3.40%	3.93%	3.93%	3.93%	3.93%	3.93%	
Changes in Working Capital (-)	-60	-71	-79	-86	-91	-97	10.03%
<i>% of revenues</i>	-0.58%	-0.67%	-0.67%	-0.67%	-0.67%	-0.67%	
Free Cash Flow to the Firm	80	117	265	443	523	617	50.50%
<i>% of revenues</i>	0.77%	1.10%	2.25%	3.45%	3.85%	4.25%	

Source: Company data, Juan Coppens estimates

Part 3: Valuation

WACC

To calculate the present value of Zalando's forecasted Free Cash Flow to the Firm, we employ the Weighted Average Cost of Capital (WACC) as the discount factor. The WACC is utilized because these cash flows are accessible to both debt and equity investors. With a capital structure comprising 56.16% equity and 43.84% debt, a cost of equity estimated at 11.66%, and an after-tax cost of debt of 4.52%, we arrive at a WACC of 8.53%

Table 17: Weighted Average Cost of Capital	Weight	Cost
Equity	56.16%	11.66%
Debt	43.84%	4.52%
WACC		8.53%

Cost of equity

To compute Zalando's cost of equity, we employ the Capital Asset Pricing Model (CAPM), which incorporates the risk-free rate and a risk premium based on the investment's beta and the market risk premium:

$$\text{Cost of equity} = \text{Risk-free rate} + \text{Levered beta} \times \text{Market risk premium}$$

For the risk-free rate, we utilize the yield of long-term bonds, specifically the latest (23 June 2023) "AAA Rated 30-Year Eurozone Central Government Bond Par Yield," which stands at 2.36%. Utilizing Zalando's levered beta of 1.69¹¹, obtained from Bloomberg, in the CAPM calculation, we apply a market risk premium of 5.5% as recommended by KPMG in their latest report (KPMG, 2023). Considering Zalando's significant size as a listed company with a substantial float percentage, no additional risk premium is deemed necessary.

After applying the CAPM formula to these inputs, we arrive at a final cost of equity of 11.66%.

Table 18: Capital Asset Pricing Model	
Risk-free rate	2.36%
Beta	1.69
Market equity risk premium	5.50%
Cost of equity	11.66%

¹¹ Annex 9 – Beta

After-tax cost of debt

$$\text{After-tax cost of debt} = \text{Pre-tax cost of debt} \times (1 - \text{Tax rate})$$

To determine Zalando's pre-tax cost of debt, we added the respective Option Adjusted Spread (OAS) of each tranche of Zalando's convertible bonds (Table 5) to the risk-free rate of German treasury bonds with similar maturities¹². This led us to total costs of 5.82% for Tranche A and 7.06% for Tranche B. By calculating the weighted average of these costs, we arrived at a total pre-tax cost of debt of 6.44%.

Next, to derive Zalando's after-tax cost of debt, we multiplied the pre-tax cost of debt by (1 - tax rate). For this calculation, we used the German corporate income tax rate, which stands at 29.8% (Bray, 2023). Consequently, the after-tax cost of debt was computed as 4.52%.

Table 19: Cost of debt	Cost
Tranche A (DE000A3E4589)	5.82%
Tranche B (DE000A3E4597)	7.06%
Pre-tax cost of debt	6.44%
German corporate income tax rate	29.8%
After-tax cost of debt	4.52%

Terminal value

There are two primary methods for calculating the terminal value of a company in a discounted cash flow valuation: the Gordon Growth Model (GGM) and the Exit Multiple (EM) method. The GGM assumes that a firm's cash flows will grow at a constant rate indefinitely beyond a certain point, while the Exit Multiple method uses a multiple of earnings in the final estimation year. In the academic context of this work, we will consider calculating both options.

Gordon Growth Model

$$TV = FCF_{2027} \times (1 + \text{perpetual growth rate}) / (WACC - \text{perpetual growth rate})$$

To compute Zalando's terminal value using the GGM method, we used a stable perpetual growth rate of 1.5%, representing the estimated long-term GDP growth rate for OECD countries (OECD, 2021). By multiplying our estimated 2027 FCF of 617 million EUR by (1+

¹² Annex 8 – Risk-free securities

perpetual growth rate) and then discounting this value by (WACC – perpetual growth rate), we obtain a terminal value of 8,913 million EUR for Zalando in 2027.

Table 20: Terminal Value GGM (€M)		E2027
FCFF E2027		617
Long-term growth rate		1.5%
Discounted Terminal Value		8913

Exit Multiple

To determine an appropriate exit multiple, we initially examined the current EV/EBITDA multiples of companies within our peer group. We selected the EV/EBITDA multiple as it is capital-structure neutral and allows for meaningful comparisons across companies operating in industries where fixed assets have less significance, such as the online retail industry, as it excludes depreciation and amortization (D&A) effects.

Our peer group comprises Asos, Boohoo, Boozt, and Next, as they closely resemble Zalando's business model despite minor differences presented in Table 1. We excluded About You and Farfetch due to their negative EBITDA, which would result in a negative and hence non-meaningful multiple, as well as Shein and Vinted since they are not publicly listed, from our original peer group (Table 1).

Table 21 displays the respective E2023 EV/EBITDA multiples of our peer group, sourced from S&P Capital IQ on 31/07/2023, along with the calculated median. The median EV/EBITDA multiple is proving to be a better metric than the average EV/EBITDA as it mitigates the impact of potential outliers on our valuation.

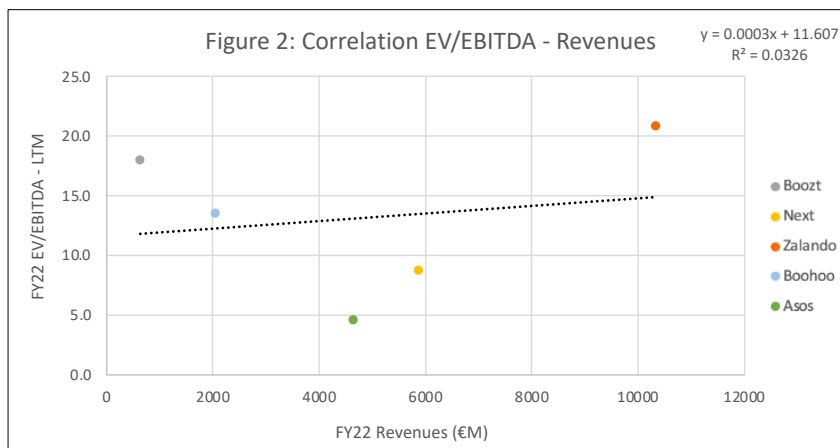
Table 21: EV/EBITDA Multiples	
Peer Group	E2023
About You	n.m.
Asos	8.3
Boohoo	9.9
Boozt	15.1
Farfetch	n.m.
Next	8.9
Median	9.4
Source: S&P Capital IQ	
Retrieved on 31/07/2023	

Nevertheless, we have expanded our analysis to explore various factors that may influence these multiples, aiming to identify and validate the most suitable exit multiple for Zalando. Specifically, we investigated the historical correlations between the EV/EBITDA multiples and

three key factors: Size, Margin, and Growth. To minimize the potential self-fulfilling correlations of analyst estimates, we utilized the EV/EBITDA multiple of the last twelve months (LTM) at the closing date of the most recent fiscal year.

- Size:

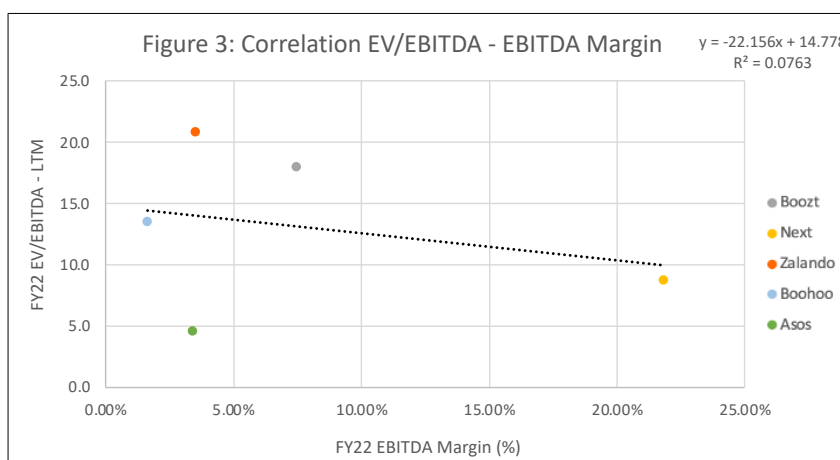
For the size factor investigation, we utilized the revenues realized in each company's last fiscal year. However, the graph in Figure 2 indicates an R^2 of 3.26%, suggesting that there is no historical correlation between the EV/EBITDA multiple and the company's size.



Source: FactSet

- Margin:

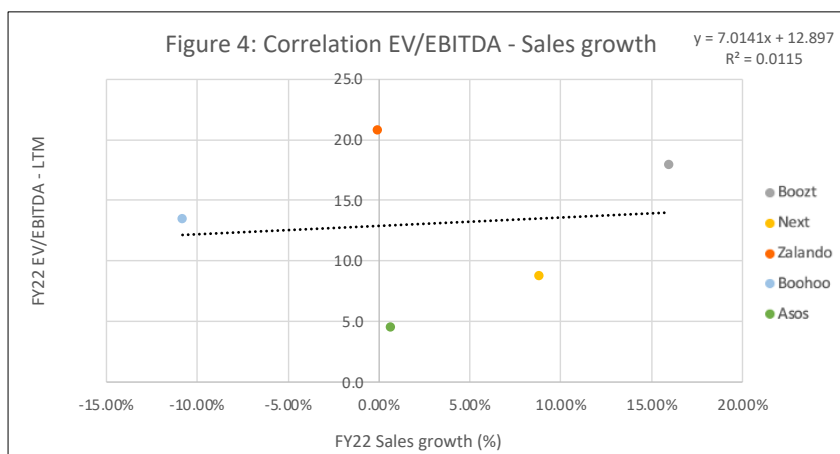
To explore the margin factor, we considered the EBITDA margin achieved in each company's last fiscal year. However, the graph in Figure 3 reveals an R^2 of 7.63%, signifying no historical correlation between the EV/EBITDA multiple and the company's margin.



Source: FactSet

- Growth:

In the investigation of the growth factor, we took into account the sales growth achieved in each company's last fiscal year. Yet, the graph in Figure 4 shows an R^2 of 1.15%, leading to the conclusion that there is no historical correlation between the EV/EBITDA multiple and the company's sales growth.



Source: FactSet

To ensure a more comprehensive analysis, we supplemented our investigation by considering the 3-year average for each factor¹³, as the last fiscal year for most of the peer group might not accurately represent their historical performance. However, even with this additional approach, the respective correlations were once again found to be negligible or non-existent. Consequently, we are confident that utilizing the median E2023 EV/EBITDA multiple of our peer group, which stands at 9.4x, provides the most suitable approximation for Zalando's 2027 exit multiple. To derive Zalando's terminal value, we multiplied this multiple by our forecasted 2027 EBITDA of 1,287 million EUR and obtained a terminal value of 12,099 million EUR. To find the present value of this terminal value, we discounted it by $(1+WACC)^n$, where n represents the fifth period (2027). This calculation yields a terminal value of 8,036 million EUR.

Discounted Cash Flow

In this section, we will perform the Discounted Cash Flow (DCF) valuation to compute Zalando's implied share price. The process involves discounting Zalando's projected Free Cash

¹³ Annex 10 – Multiples analysis

Flows to the Firm and terminal value to their present values. By applying the appropriate discount rates $(1+WACC)^n$, we calculated in Table 22 the present value of the forecasted free cash flows and summed them up to reach a total of 1,465 million EUR.

Table 22: Discounted FCFF (€M)	E2023	E2024	E2025	E2026	E2027
FCFF	117	265	443	523	617
Discount factor	1.09	1.18	1.28	1.39	1.51
PV of FCFF	107	225	347	377	410
Sum of PV of FCFF	1465				

Source: Juan Coppens estimates

From there, we need to add the present value of the terminal value to the sum of the present values of the forecasted FCFF, resulting in the implied Enterprise Value. Next, to derive Zalando's implied Equity Value, we deduct Zalando's net debt of -308 million EUR. Finally, to calculate Zalando's implied value per share, we divide the implied Equity Value by the number of outstanding shares as at July 31, 2023. As shown in Table 23 and Table 24 below, using the terminal value derived from the GGM method yields an implied value per share of 40.54 EUR, whereas using the terminal value obtained with the EM method yields an implied value per share of 37.22 EUR.

Table 23: Discounted Cash Flow (GGM) (€M)	(€M)
Sum of PV of FCFF	1465
PV of GGM terminal value	8913
<i>% of enterprise value</i>	<i>85.9%</i>
DCF Enterprise value	10378
Net debt (-)	-308
DCF Equity Value	10686
Shares outstanding (M)	264
DCF Value per share	40.54 €

Source: Juan Coppens estimates

Table 24: Discounted Cash Flow (EM) (€M)	(€M)
Sum of PV of FCFF	1465
PV of EM terminal value	8036
<i>% of enterprise value</i>	<i>84.6%</i>
DCF Enterprise value	9501
Net debt (-)	-308
DCF Equity Value	9809
Shares outstanding (M)	264
DCF Value per share	37.22 €

Source: Juan Coppens estimates

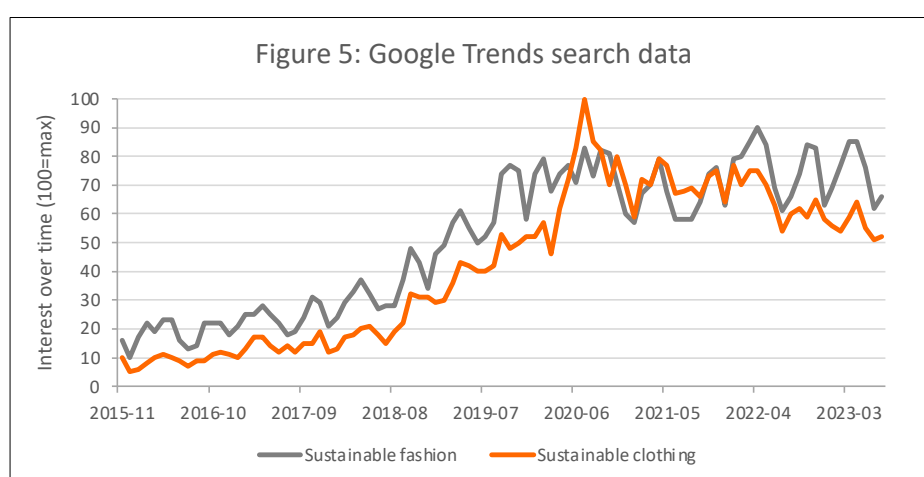
For the rest of our report, we have chosen to base our analyses on the implied value per share derived from the Exit Multiple method. This decision is driven by our belief that Zalando's future cash flows beyond 2027 may not exhibit the stability and predictability required to justify the use of a perpetual growth rate. As a "growth stock" that does not pay dividends yet and that operates in a dynamic and rapidly evolving industry, Zalando's financial outlook is subject to various uncertainties. By employing the Exit Multiple method, we can capture a more realistic estimation of Zalando's terminal value by considering market multiples applicable to the industry.

Part 4: ESG Analysis

Awareness

Fast fashion has frequently been linked to ESG concerns. The industry's intricate supply chains often hide low wages and limited employee rights, drawing significant scrutiny. Instances of poor health and safety records have also come to light, resulting in devastating consequences in some cases. The fashion industry is responsible for 10% of global carbon emissions each year, surpassing the combined emissions of aviation and maritime shipping (World Bank, 2019), and for approximately 40 million tonnes of textile waste each year (McKinsey, 2022), thus posing substantial risks to natural resources. Past ESG incidents have proven to be detrimental to companies operating in the sector, leading to stock price declines, stricter regulations, financial penalties, and reputational damage (HSBC Global Research, 2021).

Over the few last years, we observe a rising awareness of sustainability issues among consumers, investors, and policymakers. According to a survey conducted by McKinsey in 2019, nine in ten Generation Z consumers feel that fashion companies should take responsibility for addressing social and environmental concerns. Moreover, data from Google Trends indicate a strong increase in global search volumes for sustainable fashion and sustainable clothing since 2015, with a peak during the COVID-19 pandemic. In this regard, we believe that online fashion platforms like Zalando are particularly exposed to these developments.



Source: Google Trends

In the meantime, the European Commission has adopted a new action plan for the circular economy, which includes an objective to ensure the application of circular economy principles

throughout textile manufacturing, product lifecycle, consumption, and waste management. Under the waste directive framework of the European Union, member countries are required to implement the segregation of all textile waste by 2025. Additionally, several European nations have implemented extended producer responsibility schemes that hold brands and retailers accountable for post-consumer waste. These schemes also require financial contributions from producers to support the collection, recycling, and reuse of products (McKinsey, 2022).

Zalando's strategy

We have identified three primary risks associated with ESG factors for an online fashion e-commerce company like Zalando: environmental impact, supply chain transparency, and human capital. In this section, we will evaluate how Zalando addresses these risks through its sustainability strategy “do.MORE”, initiated in 2019, with the aim of becoming "a sustainable fashion platform with a net-positive impact on people and the planet" (Zalando SE, 2022).

- Environmental impact

To minimize risks associated with its environmental impact, Zalando has been focusing on its carbon footprint, its packaging and its products. (Zalando SE, 2022)

In terms of carbon footprint, Zalando focuses on minimizing emissions and switching to renewables. The company has been carbon neutral within its own operations, deliveries and returns since 2019. It has set a 2025 goal of reducing its own (Scope 1 and 2) GHG emissions by 80% against 2017 levels, to be aligned with the Paris Agreement. This measure has been very effective as Zalando has already reduced its emissions by 78% in 2022 (Zalando SE, 2022). However, most of the fashion footprint comes from upstream supply chain activities beyond its own operations, such as material production, preparation, and processing (Scope 3). Therefore, Zalando has a 2025 target that 90% of its suppliers will have their own Science Based Targets (SBTs). Today, already 58% have set their SBTs (Zalando SE, 2022).

In terms of packaging, Zalando has set a target to eliminate all single-use plastics in its packaging by 2023. In 2022, it had already achieved 49% of this target by replacing plastics with recycled materials such as paper and polybags. However, they expected to miss by short their self-imposed deadline for single-use plastic elimination by the end of 2023 (Zalando SE, 2022).

To improve its environmental initiatives for products, we believe Zalando should prioritize the assessment of environmental impacts associated with different clothing fibers, encompassing factors like water usage, pollution, microfiber release, and emissions. Currently, Zalando has set a target to generate 25% of its Gross Merchandise Volume (GMV) through sustainable products by 2023. To support this goal, Zalando has made sustainability-related information easily accessible to customers through interactive icons representing various sustainability attributes. This enables customers to access valuable details such as the percentage of certified materials used in a product (Zalando SE, 2022). Zalando also introduced a "pre-owned" section on its website in 2020, allowing customers to browse and purchase second-hand clothing items. Our evaluation of the pre-owned platform indicates that Zalando has made significant efforts to enhance the consumer experience compared to other similar platforms. The platform offers high-quality clothing images, size filtering, free shipping without a minimum spending requirement, and convenient returns. Furthermore, products purchased through Zalando's main platform can easily be traded in for pre-owned items. Incentives such as free shipping and the option of receiving a Zalando gift card or making a charitable donation encourage customers to participate in the trade-in program. Second-hand clothing and repair services hold potential for achieving a more sustainable and circular fashion industry. However, it remains unclear how this initiative can generate substantial revenue for Zalando and other industry players. To unlock additional revenue opportunities, companies like Zalando could consider gradually transitioning towards a rental clothing model with monthly subscribers. This approach would ensure guaranteed revenue streams while minimizing the overconsumption of new clothing (HSBC Global Research, 2021).

- Supply chain transparency

In recent years, the retail sector has faced increased scrutiny, exposing pervasive social issues that primarily revolve around supply chain transparency. Instances such as the uncovering of unlawful labor practices within Boohoo's supply chain and the recurring controversies surrounding Shein, involving poor working conditions and the presence of harmful chemicals in their clothing items, highlight the challenges faced by Zalando's peers. It is evident that improvement in this area is necessary for all fast fashion retailers and platforms to address.

Zalando has made considerable progress in addressing supply chain transparency risks, particularly with its own brand, ZIGN. The company is committed to tracing the origin and production of all materials used in garment manufacturing. For ZIGN and its private label

items, detailed information about Tier 1 suppliers and some Tier 2 suppliers can be accessed on Zalando's website or through a QR code embedded in the product's label (Zalando SE, 2022). This represents a significant advancement in industry-wide transparency, a path that Asos has also embarked upon by mapping Tier 3 suppliers (HSBC Global Research, 2021). Zalando has gone further than some of its counterparts by introducing "value-based browsing," allowing customers to easily filter items based on sustainable criteria such as "circular design, improved production, innovative materials, organic materials, recycled materials, and responsibly sourced materials" (Zalando SE, 2022). Nonetheless, we believe Zalando should continue to prioritize transparency wherever feasible. Notably, the company became the first retailer to adopt in 2020 the Brand and Retail Module (BRM) of the Higg Index as a mandatory brand assessment tool, ensuring that all brands on the platform report on social and environmental standards (Zalando SE, 2020). This represented a significant step towards enhancing clarity, credibility, and comparability in the fashion industry. However, recent evaluations by Norwegian authorities have raised concerns about greenwashing associated with Higg labels, leading Zalando to remove filters based on the Higg Index from its website (Mathews, 2022).

- Human capital

To minimize risks associated with its human capital, Zalando has prioritized people as a key pillar in its sustainability strategy. The company has specifically emphasized ethics, employee skill development, and fostering diversity and inclusion.

In terms of ethics, Zalando committed to exclusively collaborate with partners who adhere to their heightened ethical standards by 2023. Zalando has made significant strides in its human rights efforts, including the publication of a new Policy Statement on Human Rights Strategy, the implementation of a human rights risk assessment, the launch of training programs on living wages and child labor prevention, the establishment of a complaint and grievance procedure, and the appointment of a Human Rights Officer to meet legal requirements (Zalando SE, 2022). These initiatives demonstrate Zalando's commitment to upholding human rights across its operations and supply chain.

Regarding the enhancement of employee skills, the OECD predicts that approximately 1 billion individuals will require reskilling by 2030 (Zahidi, 2020). In alignment with this, Zalando has made a commitment to support 10,000 individuals in the workforce by 2023. The company

aims to provide skilling opportunities that align with future job demands in technology, commercial, and operations functions. As of 2022, Zalando had already accomplished 50% of its target by offering skill development opportunities to 5,016 individuals (Zalando SE, 2022).

Finally, Zalando launched its "do.BETTER" strategy in 2021, entirely dedicated to advancing diversity and inclusion within the company. Building on this commitment, Zalando made significant progress in 2022. It conducted its first D&I survey, increasing understanding of employee experiences. Zalando prioritized building an inclusive workplace, introducing accessible facilities and facilitating "D&I Dialogues" for team discussions. They achieved a notable milestone of 37.5% female representation in leadership positions, with a target of 40-60% by the end of 2023. Zalando developed 24 dedicated D&I Action Plans and implemented inclusive leadership training. Customer-focused efforts included enhancing digital accessibility, expanding the inclusive beauty assortment by 60%, and collaborating with 63 Black-owned brands (Zalando SE, 2022). These initiatives reflect Zalando's commitment to an inclusive work environment, diverse leadership, and customer-centered diversity and inclusion.

Peer analysis

Considering the complexity of assessing ESG performance and the multitude of factors involved, we undertook a comparative analysis of Zalando's ESG efforts with those of its peers using existing ESG ratings from different agencies. A company's ESG score is a comprehensive evaluation of its performance and transparency across the environmental, social, and governance dimensions (Spirova, 2023). Table 25 below showcases the scores and ratings for each listed company within Zalando's peer group.

Table 25: ESG ratings analysis					
Peer Group	Truvalue ESG Score (/100)	Sustainalytics	ISS ESG Rating	MSCI ESG Rating	
About You	60	16.2 (Low risk)	C (Medium)	N/A	
Asos	54	21.1 (Medium risk)	C- (Medium)	N/A	
Boohoo	44	26.3 (Medium risk)	D+ (Poor)	N/A	
Boozt	50	22.8 (Medium risk)	N/A	N/A	
Farfetch	61	22.2 (Medium risk)	D+ (Poor)	N/A	
Next	62	15.5 (Low risk)	C+ (Medium)	AA (Leader)	
Zalando	65	13.5 (Low Risk)	B- (Good)	AA (Leader)	

Source: FactSet, Sustainalytics, MSCI

Upon examining Table 25, it becomes apparent that Zalando consistently outperforms its peers in every rating category. While recognizing that there is still room for improvement, Zalando clearly stands out as a sustainability leader in the fast fashion industry.

Impact on valuation

The debate surrounding the outperformance of ESG investing compared to other investments remains ongoing. Existing literature presents conflicting perspectives on whether high ESG scores influence risks, returns, and share prices, resulting in varied outcomes across different countries (Spirova, 2023). However, it is evident that ESG investing is on the rise. The total assets under management of United Nations Principles for Responsible Investment (UN PRI) signatories, committed to incorporating ESG information in their portfolio decisions, have significantly grown from a few hundred billion dollars in 2006 to a staggering \$120 trillion by 2021, nearly tripling the capitalization of U.S. markets (PRI, 2021).

Zalando, as a leading ESG player in the online fashion industry, is likely to attract considerable interest from ESG-focused European investors, extending beyond catering to a niche group of sustainability-minded consumers. Institutions and individuals increasingly prioritize selecting investments aligned with their values and priorities. Consequently, companies are now evaluated not only based on their financial performance but also on their ESG performance (Zimmerman, 2022). A McKinsey report revealed that 25% of executives and investors would be willing to pay a premium of 20-50% for a company with a positive ESG track record compared to one with a negative record. Even those who believe that ESG has no direct impact on shareholder value would still pay a 10% premium for strong ESG companies. The overall median premium, as reported by respondents, stands at approximately 10% (McKinsey, 2020). Acknowledging the scope for improvement, but recognizing Zalando's prominent position within its industry, one could make a case for incorporating an ESG premium in our valuation.

However, a recent study from EDHEC – Risk Climate Impact Institute on whether ESG investing improves risk-adjusted performance concludes that “ESG strategies should be valued for the unique benefits that they can provide, such as making a positive impact on the environment or society, as opposed to being promoted on the basis of disputable claims regarding their outperformance potential.” Therefore, in the absence of clear empirical evidence on whether relative ESG superiority would lead to any outperformance, we have decided not to incorporate an ESG premium.

Part 5: Reputation Analysis

Measuring a company's reputation in the stock market can be challenging due to its intangible nature, which is why it is not often part of typical analyst reports. However, reputation plays a major role in valuation. According to LPE Research (2020), a positive reputation lowers investment risk, fosters trust, and boosts confidence in the company's future behavior and share price. Conversely, a negative reputation leads to a valuation discount. To assess Zalando's stock reputation, we applied LPE Research's measurement methodology in Table 26, which assigns a number of points to five criteria: share price behavior, shareholder structure quality, governance and focus on shareholder value, social and environmental focus, and communication consistency (LPE Research, 2020).

With 0 points scored out of 20, Zalando's share price behavior becomes the primary factor responsible for the loss of more points. The significant volatility observed in Zalando's share price over the past three years leads to erratic movements and a notable deviation from its trend.

Moving on to the shareholder structure, Zalando earns a respectable 15 points out of 20, signifying a predominantly qualitative arrangement. According to FactSet, 60.8% of Zalando's float is owned by 403 institutional investors. Moreover, 12 out of the top 15 institutional investors can be classified as “major” (>\$100Bn AUM), and collectively represent 33.96% ownership, which is already higher than the 32.6% threshold to obtain 10 points.

The third criterion, governance and focus on shareholder value, stands out as Zalando's highest score, with 16 out of 20 points. This achievement is attributed to various factors, including the involvement of Baillie Gifford & Co., Zalando's reference shareholder, in previous activist campaigns against different companies. Additionally, both CEOs hold a significant stake in Zalando (5.14% combined), and neither of them holds a seat on the board of directors. However, there is room for improvement in terms of the number of days spent engaging with investors.

Regarding the social and environmental focus, it is evident from the ESG analysis that Zalando demonstrates a high level of commitment to improving these areas and has given them priority within its overall strategy. Nevertheless, it remains a fact that Zalando has not yet fully realized its mission of becoming a company with a net-positive impact on the planet and people. Hence, Zalando scores 12 out of 20 in this area.

Finally, although Zalando's communication has shown remarkable consistency over the last 3 years, there is a need for improvement in the quality aspect due to the lack of granularity in its results and the unclear transparency surrounding its business models. It also loses five points due to the profit warning issued in June 2022, impacting its guidance achievement. Consequently, Zalando earns a score of 12 out of 20 for communication and consistency.

Overall, Zalando scores 55 out of 100, placing the company in the fifth decile, indicating an "average reputation on the stock market" according to LPE Research's stock reputation measurement category. As a result, we have chosen not to apply a premium or a discount to our valuation based on this assessment. For more details on the specific attribution of points, please refer to Annex 12 – Reputation analysis.

Table 26: LPE Research - Stock Reputation Analysis		
Criteria	Data	Nb of points
1. Share price behavior		0
1.1 Erratic share price movements		0
Erratic movements probability (>3.5% compared to DAX)	14.30%	0
1.2 Share price deviation from its trend		0
Standard deviation compared to 200-day moving average	31.19%	0
2. Quality of shareholder structure		15
2.1 Ownership by 'major' institutional investors		10
Proportion of "major" institutional investors (% of float)	>33.96%	10
2.2 Shareholder loyalty		5
Proportion of funds selling out their shares each quarter	7.58%	5
3. Governance and focus on shareholder value		16
3.1 Reference shareholder		5
Typology of the reference shareholder	Activist	5
3.2 Board structure		4
Board members being major shareholders	1	2
Roles of CEO and Chairman of the board separated	Yes	2
Percentage of independent board members	11.11%	0
3.3 Focus of the CEO		5
Stock ownership in numbers of years of salary	>22.4	5
3.4 Investor Relations intensity		2
Nb of days per year dedicated by the CEO to investors	7	2
Nb of days per year dedicated by the CFO to investors	10	-1
Nb of analysts covering the company	31	1
4. Social and environmental focus		12
4.1 Social impact reporting and priority		5
Formal prioritization of social impact	First priority	3
Social performance indicators reporting	Detailed & regular	2
4.2 Impact of operations and products on people		2
Impact of operation on people	Neutral	1
Impact of products/services on customers	Neutral	1
4.3 Environmental impact reporting and priority		5
Formal prioritization of environmental impact	First priority	3
Environmental performance indicators reporting	Detailed & regular	2
4.4 Impact of operations and products on the environment		0
Impact of operation on the environment	Negative	0
Impact of products/services on the environment	Negative	0
5. Communication and consistency		12
5.1 Communication quality		7
Business model communication	Somewhat detailed	1
Strategy communication	Very detailed	2
Capital allocation communication	Somewhat detailed	1
Results and performance communication	Somewhat detailed	1
Communication coherence	Coherent	2
5.2 Consistency		5
Strategy consistency	No change (3y)	2
Reporting consistency	No change (3y)	2
Accounting consistency	No change (3y)	1
5.3 Guidance		0
Guidance achievement	Profit warning (2022)	0
Conclusion	Decile	Total
Average reputation on the stock market	Fifth decile	55

Source: See Annex 12 – Reputation analysis

Part 6: Sensitivity Analysis

In this section, we will conduct a share price sensitivity analysis to establish a valuation range. However, unlike conventional banking practices that perform sensitivity analyses by plotting variations in the WACC against variations in the Exit Multiple, we will concentrate on factors directly influencing our FCFF projections. Recognizing that our FCFF projections rely on more Zalando-specific assumptions than the WACC and Exit Multiple, we consider this approach to be of greater interest as it establishes a link between the elements identified in our SWOT analysis and the factors that impact Zalando's sales and costs, thus directly influencing its FCFF. In this process, we have identified four main factors that could impact our valuation and on which we will perform different scenarios influenced by elements from our SWOT analysis. These factors are the market share, the shift in business model, the take rate, and the inflation rate.

Market share

In our baseline scenario, Zalando's GMV predictions are founded on the assumption that the company's overall market share will remain stable at 11.76% over the years, namely due to its leader position. However, this proportion could fluctuate both upwards and downwards. Zalando's wide product offering, along with its favorable return policy and increased utilization of AI tools, has the potential to drive an upswing in its market share, as seen in the past. Conversely, failure to continuously enhance user experience and security measures against cyber-attacks could prompt customers to shift to competitors or potential new entrants.

To ensure a realistic range for market share variation, we examined Zalando's historical market share fluctuation between 2018 and 2020, considering it did not expand into new countries during this period. We observed an average annual increase of 0.56 percentage point. Factoring this over the next five years using GMV growth rates as discount factors, we arrived at a total variation of 2.17 percentage points¹⁴. Based on this variation in market share, we arrive – ceteris paribus – at a share price range between 31.68 EUR and 43.83 EUR.

Table 27: Sensitivity: market share - share price			
Factor	Pessimistic	As-is	Optimistic
Market share	9.59%	11.76%	13.93%
Implied share price	31.68 €	37.22 €	43.83 €

¹⁴ Annex 13 – Sensitivity analysis: market share

Shift in business model

As previously mentioned, Zalando is currently in the process of transitioning from a wholesale to a partner business model. Our baseline scenario relies on Zalando's business plan, which targets a 50% share of Fashion Store GMV through its partner business segment by 2025. With no guidance provided beyond 2025, we assumed the proportion would remain steady at 50%. However, considering the past two years' performance, Zalando has achieved a yearly increase of 6 percentage points in proportion, indicating that its business plan might be deemed conservative. Zalando's attractive pure marketplace model entices brands with immediate access to over 50 million customers while retaining control over their products. Hence, we consider a positive scenario, where Zalando's Partner Business proportion to Fashion Store GMV increases by 6 percentage points annually until 2027, as a realistic optimistic scenario.

Conversely, selling on Zalando's platform entails brands paying a monthly fee, and the post-Covid return to brick-and-mortar shopping has reduced the allure of e-commerce compared to the pandemic period. Additionally, the conventional wholesale segment offers a means for brands to shift inventory risks to Zalando. Therefore, we believe a scenario where Zalando achieves its 50% objective with a one-year delay remains plausible. This would translate to a 3.5 percentage points increase in Zalando's Partner Business GMV to Fashion Store GMV until 2026, and we assume no further growth beyond the objective's attainment. By modeling these variations in business model proportions to Fashion Store GMV, we arrive – ceteris paribus – at a share price range between 37.09 EUR and 39.62 EUR.

Factor	Pessimistic	As-is	Optimistic
PB GMV/FS GMV	50% by 2026	50% by 2025	66% by 2027
Implied share price	37.09 €	37.22 €	39.62 €

Take rate

In our baseline scenario, we have initially estimated Zalando's take rate at 19% based on a peer analysis. However, given Zalando's prominent position as the clear leader in the online fashion market, granting access to over 50 million customers, it holds a relatively high pricing power in the Partner Business segment compared to its Wholesale segment. This situation could lead Zalando to consider increasing its take rate, as it provides an easy leverage for margin growth. Conversely, Zalando might also contemplate lowering its take rate to impede competitors' similar transitions to such business models or to deter potential new entrants.

To establish both a lower and a higher take rate range, we opted to calculate the average take rate of the three companies with the lowest rates and the three companies with the highest rates within our peer group of six companies. This approach yields a lower average take rate of 14% and a higher average take rate of 23%¹⁵. By plotting this variation in take rates, we arrive – ceteris paribus – at a share price range between 34.96 EUR and 39.02 EUR.

Factor	Pessimistic	As-is	Optimistic
Take rate	14%	19%	23%
Implied share price	34.96 €	37.22 €	39.02 €

Inflation rate

In our baseline scenario, Zalando's GMV projections are directly derived from Statista's figures, which consider the latest inflation rate estimates in the European market¹⁶. As inflation had a significant impact on Zalando's 2022 results, we included this factor in our sensitivity analysis. However, the impact was particularly severe due to the extreme situations created by the pandemic and the Russia-Ukraine war. To maintain a realistic approach, we chose not to modelize such extreme variations in inflation rates as they were linked to extraordinary events. Instead, we examined two more plausible scenarios.

In the first scenario (A), we assume inflation will be more persistent than forecasted, decreasing by 0.5 percentage point per year slower than predicted, and achieving the 2% inflation ECB target by 2028 instead of 2027. In the second scenario (B), we consider the possibility of current ECB measures effectively fighting inflation, resulting in a decrease of 0.5 percentage point per year faster than predicted, achieving the ECB target by 2025. However, in both scenarios, we kept our projections for 2023 unchanged since we are already at mid-year and do not foresee any additional variance. Both scenarios have implications for Zalando's revenues and costs.

On the revenue side, the relatively small variations in inflation are not expected to severely impact consumer sentiment. Therefore, we adjusted the projected GMV by adding the yearly inflation delta. Regarding costs, we modeled the effects of the variations in predicted inflation rates on four different types of costs: COGS, Fulfillment costs, Marketing costs, and Administrative expenses.

¹⁵ Annex 6 – Computation average take rate

¹⁶ Annex 14 – Sensitivity analysis: inflation rate

A) Slower decrease compared to forecasted figures¹⁷:

- For COGS, we postponed the 1.5 percentage points recovery described in our baseline scenario by one year.
- Fulfillment costs, already proportionally high to revenue in our baseline scenario and indirectly linked to high energy prices, remain unchanged.
- In terms of Marketing costs, we increased their proportion to revenues using the higher proportion observed in 2021, as the realized cost cuts between 2021 and 2022 may not be sustainable due to continued price increases.
- For administrative expenses, we maintained our projected proportion for 2023 over the next four years, considering that salary cost increases could not be entirely offset by projected IT economies of scale.

B) Faster decrease compared to forecasted figures¹⁸:

- For COGS, we kept our proportion to revenues from the baseline scenario unchanged as the timing would be too short to accelerate the 1.5 percentage points recovery.
- Fulfillment costs, being more volatile, were decreased back to the 2021 proportion to revenues as our forecasted inflation rate for 2024 reaches a similar level to 2021.
- For Marketing costs, we reverted to the 2022 proportion to revenues, assuming that all marketing efforts necessary for entering new countries would be compensated by salaries increasing less than forecasted, combined with improved marketing efficiency as described in our baseline scenario.
- In terms of administrative expenses, we decided to keep the proportions to revenues from our baseline scenario, reflecting already impressive economies of scale.

Overall, by plotting this variation in forecasted inflation rates, we arrive at a share price range between 25.84 EUR and 44.24 EUR.

Table 30: Sensitivity: inflation rate - share price			
Factor	Pessimistic	As-is	Optimistic
Inflation rate	2% by 2028	2% by 2027	2% by 2025
Implied share price	25.84 €	37.22 €	44.24 €

¹⁷ Annex 14 – Sensitivity analysis: inflation rate

¹⁸ Annex 14 – Sensitivity analysis: inflation rate

Conclusion

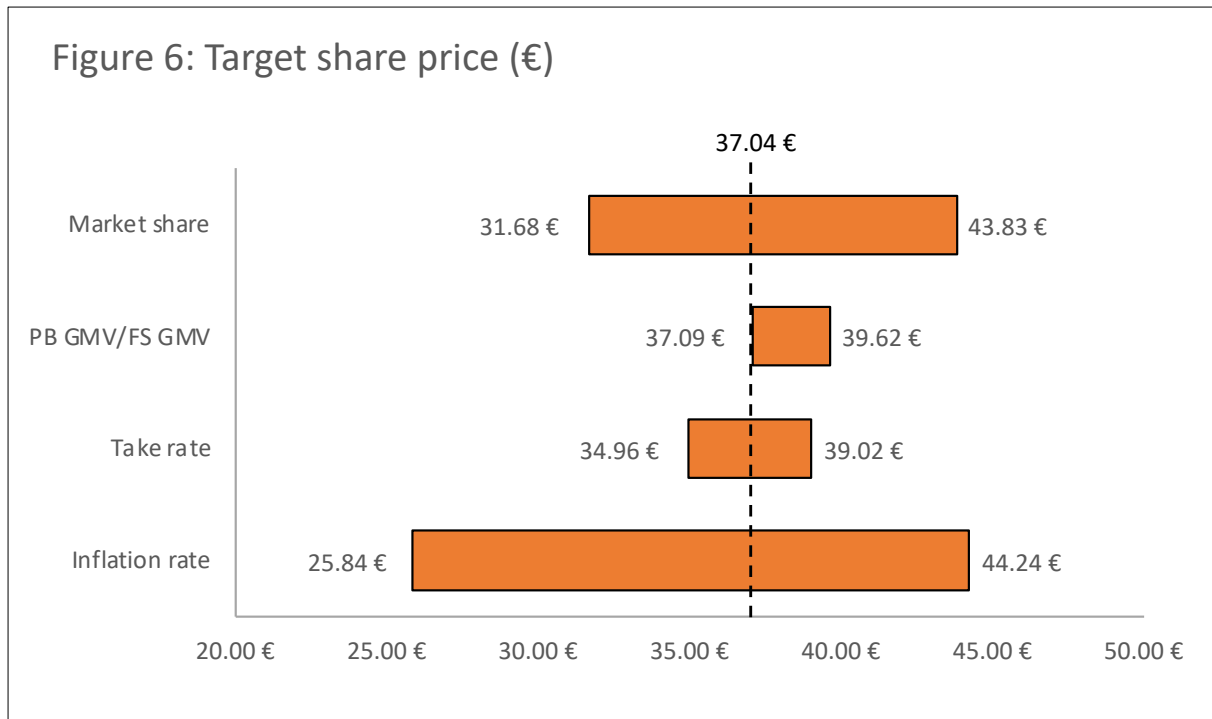
The objective of this report was to determine whether Zalando is currently undervalued, overvalued or correctly valued on the stock exchange. To do so, we provided you with our personal approach in estimating Zalando's intrinsic value.

Upon delving into the study of Zalando, the company immediately emerged as a fascinating entity, being the European leader with an 11.76% market share in the online fashion market and having known extraordinary growth since its creation in 2008, with a tremendous acceleration during the pandemic followed by a dramatic downturn in early 2022. Our historical analysis of Zalando's last annual reports in the European online fashion market allowed us to pinpoint the key drivers of its revenues and costs. Understanding Zalando's fundamentals enabled us to identify relevant peers for our subsequent work. By studying market tendencies and risks, we developed our SWOT analysis.

Subsequently, we adopted a top-down approach to determine Zalando's Gross Merchandise Volume (GMV), derived from European online fashion market growth statistics. Forecasting the cost structure of various business segments led us to our projected Free Cash Flow to the Firm (FCFF). With this framework in place, we initiated the valuation exercise, where the key determinant was the Weighted Average Cost of Capital (WACC) at 8.53%, utilized in the two Discounted Cash Flow (DCF) analyses: one based on the Gordon Growth Method (GGM) and the other on a carefully selected Exit Multiple of 9.4x EV/EBITDA. We opted for the second approach, leading to an implied share price of 37.22€.

To rigorously challenge the results of this financial calculation, we conducted an exhaustive ESG and reputation investigation, which confirmed the found value. Building on this foundation and considering our SWOT analysis, we identified four critical factors to drive our sensitivity analysis. The fluctuations in market share would impact scale advantages, pricing power, and service optimizations. The implementation of the Partner Business Model and variations in the take rate would influence sustainable cash position, expansion, and potential share of wallet. Additionally, we considered inflation effects to highlight exposure to the macroeconomic environment.

This comprehensive sensitivity analysis culminated in the valuation presented in Figure 6. By assigning equal weight to each factor, we arrived at an average target price of 37.04 EUR.



Based on that, we consider Zalando's current share price to be undervalued and, therefore, provide a BUY recommendation. Our target share price of 37.04 EUR indicates an upside of 17.95% compared to the company's closing price of 31.40 EUR on July 31, 2023. However, we urge investors to remain cautious given the sensitivity of Zalando's valuation to the different scenarios studied in our sensitivity analysis.

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Appendices

Annex 1 - Historical financials

Income Statement (€M)	2018	2019	2020	2021	2022
GMV	6638	8208	10696	14333	14798
<i>% Growth</i>		23.65%	30.31%	34.00%	3.24%
Revenues	5388	6483	7982	10354	10345
<i>% Growth</i>		20.32%	23.13%	29.72%	-0.09%
<i>ΔGMV growth - Revenues growth</i>		3.34%	7.18%	4.29%	3.33%
COGS	3107	3724	4587	6028	6289
<i>% of revenues</i>	57.67%	57.45%	57.47%	58.22%	60.79%
Gross profit	2281	2759	3395	4326	4056
<i>% Gross margin</i>	42.33%	42.55%	42.53%	41.78%	39.21%
Operating expenses	2162	2593	3027	3902	3975
<i>% of revenues</i>	40.12%	39.99%	37.93%	37.68%	38.42%
Fulfillment costs	1497	1772	2050	2585	2704
<i>% of revenues</i>	27.78%	27.33%	25.68%	24.97%	26.14%
Marketing costs	397	522	659	925	792
<i>% of revenues</i>	7.37%	8.05%	8.26%	8.94%	7.66%
Administrative expenses	268	299	318	391	479
<i>% of revenues</i>	4.97%	4.61%	3.99%	3.78%	4.63%
EBIT	119	166	368	424	81
<i>% EBIT margin</i>	2.21%	2.56%	4.61%	4.10%	0.79%
Interest expense	10	17	49	70	42
EBT	109	149	318	354	39
Income Taxes	58	49	92	120	22
<i>% Tax rate</i>	52.89%	33.00%	28.99%	33.81%	56.70%
Net income	51	100	226	235	17
<i>% Net income margin</i>	0.95%	1.54%	2.83%	2.26%	0.16%
EBITDA	206	361	583	660	393
<i>% EBITDA margin</i>	3.82%	5.57%	7.30%	6.37%	3.80%

Source: Company data, FactSet

AVG EBIT Margin / Adj EBIT Margin	'18-'22
AVG Adj EBIT Margin	3.65%
AVG EBIT Margin	2.85%
AVG EBIT Margin / Adj EBIT Margin	78.02%

Source: FactSet, Company data

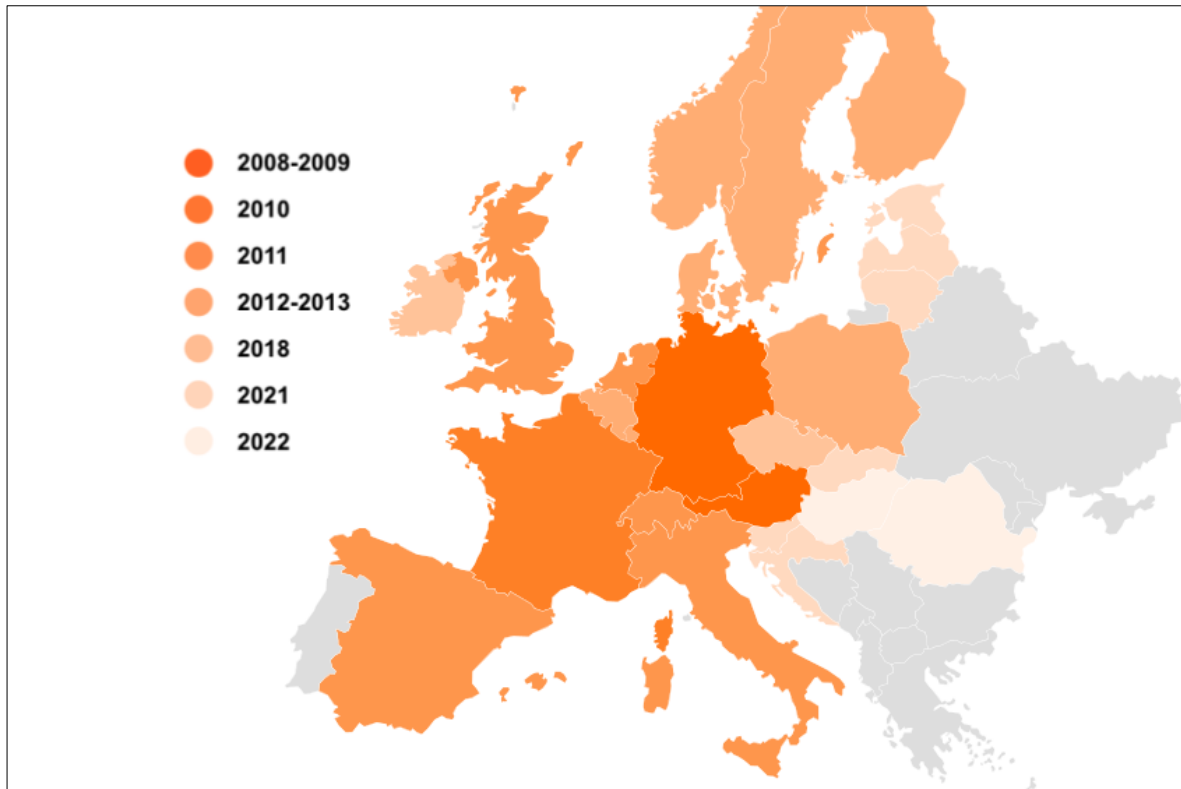
Cash Flow Statement (€M)	2018	2019	2020	2021	2022
Operating activities	213	327	528	616	460
<i>% Growth</i>		53.62%	61.40%	16.68%	-25.41%
Net income	51	100	226	235	17
Depreciation & Amortization Expense	87	195	215	235	312
Changes in Working Capital (-)	-24	-58	73	-80	-60
Deferred Taxes & Investment Tax Credit	4	-82	108	12	-23
Other Funds	48	57	52	54	94
Investing activities	-207	-290	-218	-336	-476
<i>% Growth</i>		40.24%	-24.94%	54.15%	41.77%
Capital Expenditures (-)	278	307	250	333	352
Acquisitions (-)	0	0	0	0	127
Sale of Fixed Assets & Businesses	59	23	33	0	0
Purchase/Sale of Investments	13	-6	-1	-3	3
Financing activities	-76	-57	1354	-640	-246
<i>% Growth</i>		-24.51%	-2463.18%	-147.25%	-61.57%
Change in Capital Stock	-73	0	55	-178	-132
Issuance/Reduction of Debt, Net	-3	-3	1366	-378	-3
Repayments of Operating Lease Liabilities	0	-54	-67	-85	-111
Exchange Rate Effect	0	2	4	4	-1
Net change in cash	-70	-18	1668	-356	-263

Source: Company data, FactSet

Balance Sheet (€M)	2018	2019	2020	2021	2022
Total assets	3234	4333	6495	6897	7626
<i>% Growth</i>		34%	50%	6%	11%
Cash and cash equivalents	995	977	2644	2288	2025
Trade and other receivables	395	462	603	727	913
Inventories	820	1098	1361	1547	1810
Other current assets	264	341	327	433	537
Property, plant and equipment	546	708	810	959	1146
Assets from usage rights	0	526	480	584	679
Intangible assets	189	193	236	263	414
Other non-current assets	25	28	34	95	103
Total liabilities & equity	3234	4333	6495	6897	7626
<i>% Growth</i>		33.99%	49.89%	6.19%	10.57%
Total liabilities	1685	2649	4344	4678	5427
<i>% Growth</i>		57.26%	63.96%	7.70%	16.00%
Trade payables and similar liabilities	1299	1708	2051	2437	2934
Short-term debt	3	71	451	101	130
Other current liabilities	312	328	438	560	603
Long-term debt	6	484	1317	1474	1587
Other non-current liabilities	65	59	87	107	173
Total equity	1549	1684	2151	2219	2199
<i>% Growth</i>		8.69%	27.76%	3.15%	-0.88%

Source: Company data, FactSet

Annex 2 – Zalando's geographical expansion



Source : (Zalando SE, 2022)

Annex 3 – Segment results of the group 2022

Segment results of the group 2022 (€M)	Fashion Store	Offprice	Others	Total
GMV	13008	1790	0	14798
% of total GMV	87.90%	12.10%	0.00%	
Revenue	8460	1598	287	10345
% of total revenue	81.78%	15.44%	2.78%	

Source: Zalando Annual Report 2022

Annex 4 – Online fashion market evolution: DACH & RoE

DACH: Online fashion market (€Bn)	ZLD mkt share	A2022	E2023	E2024	E2025	E2026	E2027	CAGR 22-27
Germany	12%	22.29	25.21	28.45	31.91	33.49	35.5	9.75%
% Growth		-5.39%	13.10%	12.85%	12.16%	4.95%	6.00%	
Austria	24%	2.9	3.47	4.19	5.03	5.36	5.82	14.95%
% Growth		2.84%	19.66%	20.75%	20.05%	6.56%	8.58%	
Switzerland	29%	2.98	3.56	4.36	5.32	5.67	6.16	15.63%
% Growth		6.43%	19.46%	22.47%	22.02%	6.58%	8.64%	
DACH		28.17	32.24	37	42.26	44.52	47.48	11.01%
% Growth		-3.46%	14.45%	14.76%	14.22%	5.35%	6.65%	

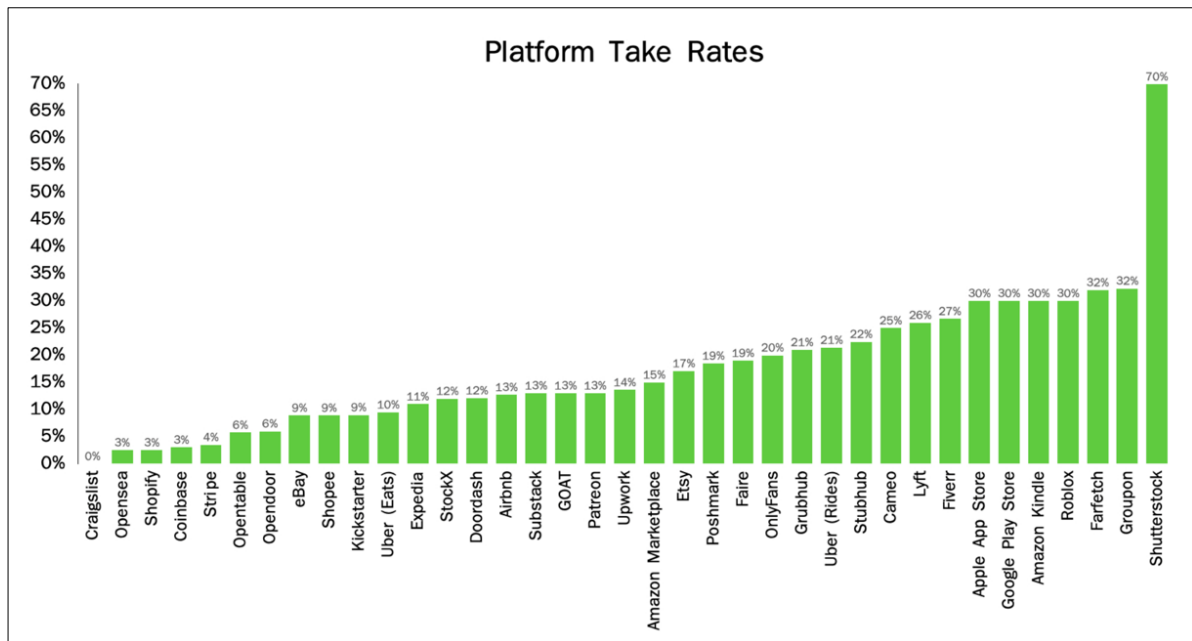
Source: Statista

RoE: Online fashion market (€Bn)	ZLD mkt share	A2022	E2023	E2024	E2025	E2026	E2027	CAGR 22-27
Belgium	25%	2.53	2.92	3.4	3.93	4.16	4.46	12.01%
% Growth		-0.78%	15.42%	16.44%	15.59%	5.85%	7.21%	
Croatia	16%	0.22	0.26	0.31	0.36	0.38	0.41	13.26%
% Growth		-12.00%	18.18%	19.23%	16.13%	5.56%	7.89%	
Czech Republic	16%	0.98	1.1	1.25	1.42	1.5	1.6	10.30%
% Growth		-2.00%	12.24%	13.64%	13.60%	5.63%	6.67%	
Denmark	41%	1.75	1.87	2.08	2.29	2.36	2.46	7.05%
% Growth		-1.13%	6.86%	11.23%	10.10%	3.06%	4.24%	
Estonia*	1%	0.18	0.21	0.25	0.29	0.31	0.33	12.89%
% Growth		-5.26%	16.67%	19.05%	16.00%	6.90%	6.45%	
Finland	37%	1.35	1.51	1.71	1.92	2.02	2.14	9.65%
% Growth		-2.88%	11.85%	13.25%	12.28%	5.21%	5.94%	
France	13%	19.8	21.78	24.02	26.31	27.17	28.27	7.38%
% Growth		-6.52%	10.00%	10.28%	9.53%	3.27%	4.05%	
Hungary*	1%	0.3	0.37	0.45	0.53	0.57	0.61	15.25%
% Growth		-3.23%	23.33%	21.62%	17.78%	7.55%	7.02%	
Ireland*	1%	1.44	1.64	1.9	2.19	2.34	2.53	11.93%
% Growth		0.70%	13.89%	15.85%	15.26%	6.85%	8.12%	
Italy	17%	13.35	16.66	20.67	25.52	27.46	30.01	17.59%
% Growth		3.89%	24.79%	24.07%	23.46%	7.60%	9.29%	
Latvia*	1%	0.17	0.2	0.24	0.28	0.3	0.32	13.49%
% Growth		-5.56%	17.65%	20.00%	16.67%	7.14%	6.67%	
Lithuania*	1%	0.2	0.25	0.32	0.41	0.45	0.49	19.63%
% Growth		17.65%	25.00%	28.00%	28.13%	9.76%	8.89%	
Luxembourg*	1%	0.33	0.36	0.41	0.46	0.49	0.52	9.52%
% Growth		0.00%	9.09%	13.89%	12.20%	6.52%	6.12%	
Netherlands	15%	6.42	7.1	8.01	8.99	9.35	9.83	8.89%
% Growth		-2.13%	10.59%	12.82%	12.23%	4.00%	5.13%	
Norway	42%	2.11	2.36	2.71	3.08	3.25	3.46	10.40%
% Growth		0.00%	11.85%	14.83%	13.65%	5.52%	6.46%	
Poland	17%	3.43	3.5	4.03	4.64	4.84	5.14	8.43%
% Growth		13.20%	2.04%	15.14%	15.14%	4.31%	6.20%	
Romania*	1%	1.86	2.25	2.64	3.08	3.37	3.69	14.68%
% Growth		-4.62%	20.97%	17.33%	16.67%	9.42%	9.50%	
Slovakia*	1%	0.42	0.49	0.58	0.69	0.74	0.8	13.75%
% Growth		0.00%	16.67%	18.37%	18.97%	7.25%	8.11%	
Slovenia*	1%	0.23	0.28	0.33	0.4	0.43	0.46	14.87%
% Growth		4.55%	21.74%	17.86%	21.21%	7.50%	6.98%	
Spain	10%	6.94	7.14	8.22	9.42	10.01	10.72	9.09%
% Growth		7.93%	2.88%	15.13%	14.60%	6.26%	7.09%	
Sweden	29%	2.73	2.87	3.31	3.66	3.82	4.03	8.10%
% Growth		-3.19%	5.13%	15.33%	10.57%	4.37%	5.50%	
United Kingdom*	1%	36.5	41.19	46.29	51.62	53.56	56.29	9.05%
% Growth		-5.27%	12.85%	12.38%	11.51%	3.76%	5.10%	
Rest of Europe		103.24	116.31	133.13	151.49	158.88	168.57	10.30%
% Growth		-2.30%	12.66%	14.46%	13.79%	4.88%	6.10%	

Source: Statista

*Countries for which Statista does not provide a specific market share because lower than 2%, we assumed it at 1%.

Annex 5 – Platform take rates



Source: (Jaipuria, 2021)

Annex 6 – Computation average take rate

Take rate (%)	
StockX	12%
GOAT	13%
Etsy	17%
Poshmark	19%
Faire	19%
Farfetch	32%
Average	19%
Average 3 lowest	14%
Average 3 highest	23%
Source: Jaipuria, 2021, Juan Coppens computations	

Annex 7 – Evolution of COGS from pure marketplaces

COGS (% of revenues)	2021	2022
StockX	Private	Private
GOAT	Private	Private
Poshmark	Private	Private
Faire	Private	Private
Etsy	28.10%	29.02%
Farfetch	54.95%	55.83%
Ebay	25.34%	27.71%
Fiverr	18.73%	20.73%
Average	31.78%	33.32%
Source: FactSet		

Annex 8 – Risk-free securities

Risk-free securities	Maturity	Rate
Treasury bond (DE000BU22015)	Jun-25	3.27%
Treasury bond (DE0001141869)	Oct-27	2.80%

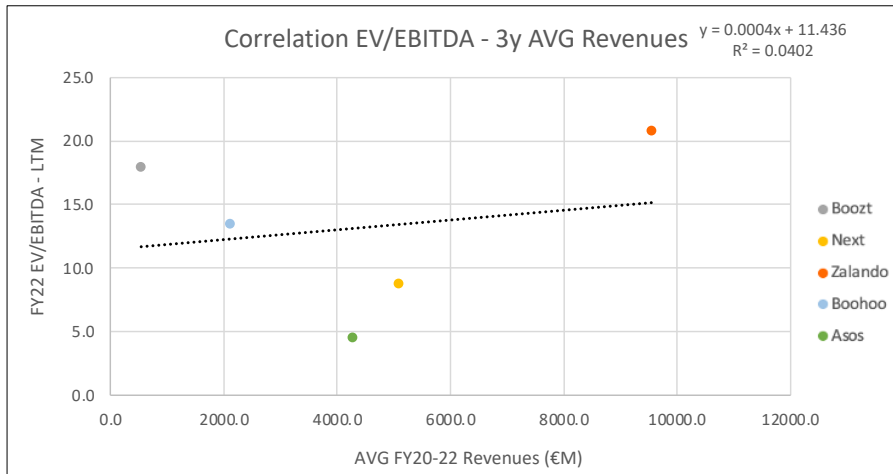
Source: FactSet

Annex 9 – Beta

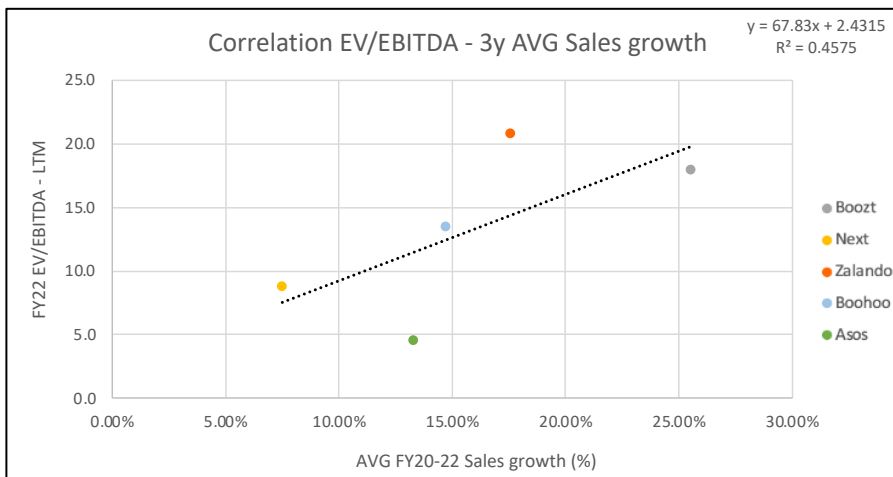


Source : Bloomberg

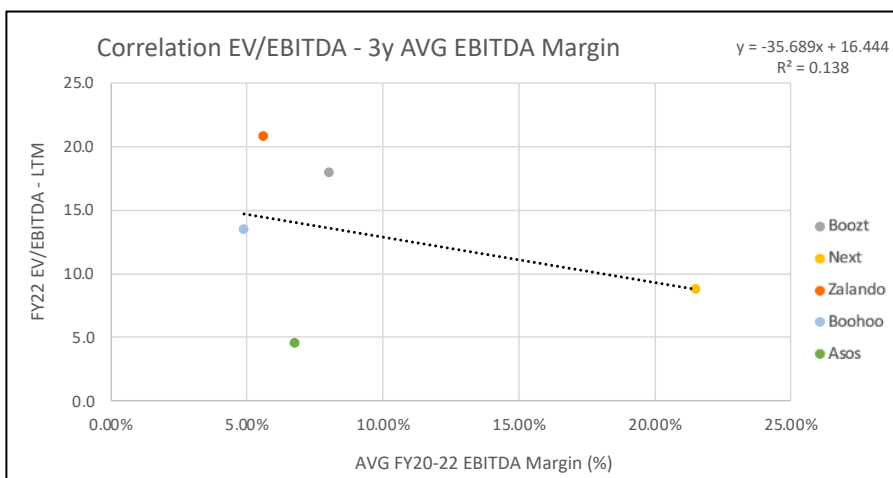
Annex 10 – Multiples analysis



Source: FactSet

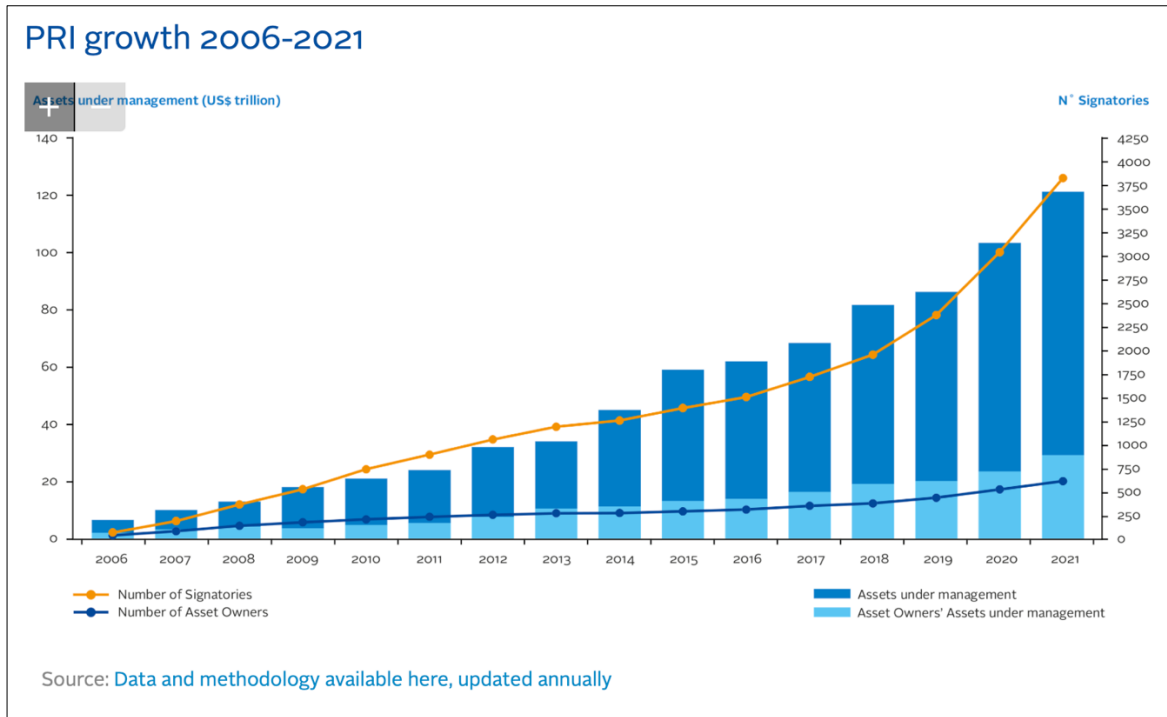


Source: FactSet



Source: FactSet

Annex 11 – PRI growth 2006-2021



Source : (PRI, 2023)

Annex 12 – Reputation analysis

1.1 Erratic share price movements	
Reference index	Germany DAX (187653)
Trading days	769
Trading days with deviation > 3.5%	110
Proportion	14.30%
Number of points associated	0
Source: FactSet, LPE Research	

1.2 Share price deviation from its trend	
Standard deviation of share price compared to 200-day moving average	31.19%
Number of points associated	0
Source: FactSet, LPE Research	

2.1 Ownership by 'major' institutional investors	
Institutional investors	403
Institutional ownership of float	60.80%
Major institutional ownership of float	>32.6%
Number of points associated	10
Source: FactSet, LPE Research	

Comment: Difficult to know the exact percentage owned by "Major" institutional funds (more than \$100 Bn AUM), but it is for sure above 32.6% as in the top 15 institutional investors, 12 can be considered major and represent together 33.96% ownership.

2.2 Shareholder loyalty	
Number of funds at the beginning of last quarter	396
Number of funds that sold out their shares last quarter	30
Proportion	7.58%
Number of points associated	5
Source: FactSet, LPE Research	

Comment: Having no access to three-year data, the analysis is performed on last quarter only

3.1 Reference shareholder	Type	Ownership	Activism
Baillie Gifford & Co	Institutional	11.20%	Medium
Povlsen Anders Holch	Person	10.09%	N.A.
T. Rowe Price Associates	Institutional	5.22%	High
Number of points associated			5
Source: FactSet, LPE Research			

Comment: The three largest investors are two institutional funds and one individual investor. The largest or reference shareholder, Baillie Gifford & Co, has been attributed a "Medium" activism threat score by FactSet as it has previously been involved in 3 activist campaigns against 3 different companies. Therefore, I decided to give a score of 5 out of 5.

3.2 Board structure	
Members of the board of directors that are major shareholders	1 (Povlsen Anders Holch)
CO-CEOs	David Schneider & Robert Gentz
Chairman of the board of directors	Kelly Bennett
Roles of CEO and Chairman of the board of directors are separated	Yes
Independent board members	1
% of indep/total board members	11%
Number of points associated	4
Source: FactSet, Company data, LPE Research	

3.3 Focus of the CEO	
Fixed remuneration (€)	78385
Equity-settled share-based payment transactions (€)	1755712
Stock ownership as years of salary	22.40
Number of points associated	5
Source: Company data, LPE Research	

Comment: This is the compensation of both CEOs over one year only, but as they are both the co-founders of Zalando, they hold together a relevant stake in Zalando of 5.14% that would far exceed 22.4 years of annual salary.

3.4 Investor Relations intensity	
Days CEO spent with investors per year	7
Days CFO spent with investors per year	10
Number of analysts covering Zalando	31
Number of points associated	2

4.1 Social impact reporting and priority	
Formal prioritization of social impact	First priority
Social performance indicators reporting	Detailed and regular
Number of points associated	5
Source: Company data, LPE Research	

Comment: First priority because:

- Has been made a pillar of their global strategy: Zalando aims to have a net-positive impact on people and planet.

- Developed a special D&I strategy do.Better
- Launched a company-wide D&I survey.
- Conducting audits to proactively identify and eliminate biases and systemic barriers.

4.2 Impact of operations and products on people	
Impact of operation on people	Neutral
Impact of products/services on people (customers)	Neutral
Number of points associated	2
Source: Company data, LPE Research	

Comment:

Neutral impact of operation on people because:

- According to Glassdoor, Zalando has an overall rating of 3.7 out of 5, based on over 2,423 reviews left anonymously by employees.
- Ranked #7 world's top female friendly companies in 2022 by Forbes (Forbes, 2022)
- Negative employee growth in 2019 (Macrotrends, 2022)
- Planned job cuts in 2023 were reported by the Financial Times, which said the online retailer's workforce would shrink by up to 5% (Storbeck, 2023)
- In 2014, Zalando was accused of bad working conditions (The Local DE, 2014)

Neutral impact of products on customers:

- Zalando sells all types of clothes, we wouldn't argue that these clothes particularly contribute positively to the development, health and well-being of its customers.

4.3 Environmental impact reporting and priority	
Formal prioritization of environmental impact	First priority
Environmental performance indicators reporting	Detailed and regular
Number of points associated	5
Source: Company data, LPE Research	

Comment: First priority because:

- Has been made a pillar of their global strategy: Zalando aims to have a net-positive impact on people and planet.
- Developed a special sustainability strategy do.More.

- Appointed a sustainability committee.
- Aims to be in line with Paris agreements.

4.4 Impact of operations and products on the environment	
Impact of operation on the environment	Negative
Impact of products/services on the environment	Negative
Number of points associated	0
Source: Company data, LPE Research	

Comment: Negative impact of operations and products on environment because even though Zalando makes huge efforts in reducing its impact on the environment, it remains as of today negative. However, the future looks bright for Zalando with its vision of becoming a company with a net-positive impact on people and planet. It is well on-track with its ambitious objectives of reducing their negative impact.

5.1 Communication quality	
Business model communication	Somewhat detailed
Strategy communication	Very detailed
Capital allocation communication	Somewhat detailed
Results and performance communication	Somewhat detailed
Communication coherence	Coherent
Number of points associated	7
Source: Company data, FactSet, LPE Research	

Comment:

- Business Model: clear description of different segments and geography, but opacity about proportions and results
- Strategy: clear description of vision (starting point for fashion), goals & financial targets (ex: triple GMV in 5y, DD growth in the LT, 3-6% Adj. EBIT margin by 2025, etc.), strategy (3 pillars), plans & projects (open at least 7 fulfillment centers in 5y)
- Capital allocation: brief explanation of CapEx & M&A
- Results: quarterly publication of key performance indicators, but lack of granularity
- Communication coherence: clear equity story, no incoherences found.

5.2 Consistency	
Strategy consistency	No change
Reporting consistency	No change
Accounting consistency	No change
Number of points associated	5
Source: Company data, FactSet, LPE Research	

Comment: Over a three-year period, there have been almost to no changes in strategy, reporting and accounting. It demonstrated a high consistency in annual reports 2020-2022.

5.3 Guidance	
Guidance achievement	Profit warning
Number of points associated	0
Source: FT, LPE Research	

Comment: Zalando issued a profit warning on 24th of June, 2022 (Storbeck, 2022).

Annex 13 – Sensitivity analysis: market share

Market share variation (pp)	E2023	E2024	E2025	E2026	E2027
Yearly increase/decrease in market share	0.56	0.56	0.56	0.56	0.56
Discount factor	0.91	0.75	0.66	0.82	0.73
PV of yearly increase/decrease in market share	0.51	0.42	0.37	0.46	0.41
Sum of PV of yearly increase/decrease in market share	2.17				

Source: Juan Coppens computations

Annex 14 – Sensitivity analysis: inflation rate

Inflation rate	E2023	E2024	E2025	E2026	E2027
Baseline scenario (Statista)	6.31%	3.34%	2.44%	2.14%	2.01%
Pessimistic scenario	6.31%	3.84%	2.94%	2.64%	2.51%
Δ vs baseline	0.00%	0.50%	0.50%	0.50%	0.50%
Optimistic scenario	6.31%	2.84%	2.00%	2.00%	2.00%
Δ vs baseline	0.00%	-0.50%	-0.44%	-0.14%	-0.01%

Source: Statista, Juan Coppens estimates

Revenues growth rates (%)	E2023	E2024	E2025	E2026	E2027
Baseline scenario	2.80%	10.40%	9.27%	5.71%	6.97%
Pessimistic scenario	2.80%	10.95%	9.27%	5.71%	6.97%
Δ vs baseline	0.00%	0.55%	0.00%	0.00%	0.00%
Optimistic scenario	2.80%	9.85%	9.34%	6.03%	7.11%
Δ vs baseline	0.00%	-0.55%	0.07%	0.32%	0.14%

Source: Juan Coppens estimates

COGS to Revenues	E2023	E2024	E2025	E2026	E2027
Baseline scenario	59.89%	58.85%	57.75%	57.75%	57.75%
Pessimistic scenario	60.39%	59.35%	58.75%	58.25%	58.25%
Δ vs baseline	0.50%	0.50%	1.00%	0.50%	0.50%
Optimistic scenario	59.89%	58.85%	57.75%	57.75%	57.75%
Δ vs baseline	0.00%	0.00%	0.00%	0.00%	0.00%

Source: Juan Coppens estimates

OPEX to Revenues	E2023	E2024	E2025	E2026	E2027
Baseline scenario	38.51%	38.21%	37.91%	37.61%	37.31%
Fulfillment costs	26.14%	26.14%	26.14%	26.14%	26.14%
Marketing costs	8.05%	8.05%	8.05%	8.05%	8.05%
Administrative expenses	4.33%	4.03%	3.73%	3.43%	3.13%
Pessimistic scenario	38.51%	39.40%	39.40%	39.40%	39.40%
Δ vs baseline	0.00%	1.19%	1.49%	1.79%	2.09%
Fulfillment costs	26.14%	26.14%	26.14%	26.14%	26.14%
Marketing costs	8.05%	8.94%	8.94%	8.94%	8.94%
Administrative expenses	4.33%	4.33%	4.33%	4.33%	4.33%
Optimistic scenario	38.51%	36.65%	36.35%	36.05%	35.75%
Δ vs baseline	0.00%	-1.56%	-1.56%	-1.56%	-1.56%
Fulfillment costs	26.14%	24.97%	24.97%	24.97%	24.97%
Marketing costs	8.05%	7.66%	7.66%	7.66%	7.66%
Administrative expenses	4.33%	4.03%	3.73%	3.43%	3.13%

Source: Juan Coppens estimates

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