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Fox Paine Pursues Make-up Makers  
by Kelly Holman

San Francisco's Fox Paine & Co. has taken a shine to the beauty products industry.

The buyout firm has formed New York-based platform company Cradle Holdings Inc. in a bid to roll up premium beauty product companies.

The campaign is already well under way. On Feb. 7, Cradle Holdings closed its second acquisition in two months of a prestigious company: 130-year-old London-based fragrance house Penhaligon's. In December it bought New York-based Erno Laszlo, a skin care line started by a Hungarian dermatologist 75 years ago. Terms were not released.

To lead the foray into beauty products, Fox Paine has recruited a cadre of experienced cosmetic and fragrance executives for Cradle, led by Robert Nielsen, a former group president of Estee Lauder Cos. Inc., who will be chief executive. Nielsen has launched designer cosmetics and fragrance brands such as Aramis, Clinique, Prescriptives and Tommy Hilfiger during his 46-year tenure in the industry.

"We see an opportunity to partner with Bob Nielsen and the management team he has developed to grow profitable, branded cosmetics and fragrance companies," said Saul Fox, chief executive of Fox Paine & Co., commenting on the firm's first foray in the industry.

They are targeting brands that are marketed in upscale specialty retailers such as Barneys New York Inc., Bergdorff Goodman, Harrods, Henri Bendel's and department stores such as Bloomingdale's and Saks Fifth Avenue, among others. Fox says the time couldn't be more opportune. "The valuations of these companies has been extraordinarily high over the last several years. Our sense now is that valuations are more in line with historical norms."

Stocks of publicly traded cosmetics companies certainly bear out Fox's sentiments. For instance, Estee Lauder's stock has fallen from above \$50 per share to \$30.71 in the past two years. Even lower-end Revlon Inc., a drug-store brand, has fallen to \$4.55 per share compared with \$7.25 a share two years ago.

For buyout firms, established cosmetic companies offer high margins and strong cash flow. Moreover, the production of the products does not demand much capital expenditure. Advertising, distribution and marketing are key factors in driving growth, Fox said.

Fox admits that the sales of high-end products have declined as a result of the recession, but he expects Cradle's management team to steer the company through the difficult market.

"Specialty brands have shown tough staying power even under difficult conditions, and in time they could become attractive to LVMH Group and similar companies," said Mark Vidergauz, chief executive of Los Angeles investment bank firm The Sage Group, which specializes in consumer-related transactions.

A bouquet of independently-held cosmetic and skin lines that offer potential acquisition opportunities for Cradle include California-based Lorac Cosmetics, Smashbox Cosmetics and Two Faced Cosmetics; and, in New York, brands such as Paula Dorf, Peter Thomas Roth, Tony & Tina's and Trish McEvoy.

The number of independent cosmetic companies, many bearing the names of make up artists, have been reduced as large trade conglomerates have entered the beauty space. For example, French luxury goods giant LVMH has built up a large high-end beauty and specialty cosmetics portfolio in the last several years. LVMH Perfumes & Cosmetics group has acquired San Francisco's BeneFit Cosmetics; Blissworld of New York; Los Angeles' Hard Candy; Fresh Inc. in New York; Make Up For Ever in France; and Urban Decay of Mountain View, Calif., among others.

Fox Paine isn't the only financial buyer eyeing the sector. Two years ago, in January 2000, Encino, Calif.-based salon beauty supplier PureBeauty raised \$25 million from Boston private equity firm Heritage Partners to fund its growth.

The strategy for buyout firms is to build the companies up and then sell them to a large strategic acquirer, said Vidergauz, whose firm advised PureBeauty. The companies have been selling at one to three times revenue, said Brien Rowe, managing director of Sage Group.

However, the measure of profitability is less important when determining the value of smaller brands. More important in these deals are the brand's popularity, its distribution network, volume and market share, said Brien Rowe, managing director of The Sage Group.

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