

ESTEE LAUDER COMPANIES INC

Form 10-K

August 22, 2011

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**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

FORM 10-K

(Mark One)

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended June 30, 2011

OR

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from to

Commission file number 1-14064

The Estée Lauder Companies Inc.

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(Exact name of registrant as specified in its charter)

Delaware
(State or other jurisdiction of incorporation or organization)

11-2408943
(I.R.S. Employer Identification No.)

767 Fifth Avenue, New York, New York
(Address of principal executive offices)

10153
(Zip Code)

Registrant's telephone number, including area code **212-572-4200**

Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Name of each exchange on which registered
Class A Common Stock, \$.01 par value	New York Stock Exchange

Securities registered pursuant to Section 12(g) of the Act:

None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes No

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

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Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act.

Large accelerated filer
Non-accelerated filer
(Do not check if a smaller reporting company)

Accelerated filer
Smaller reporting company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes No

The aggregate market value of the registrant's voting common equity held by non-affiliates of the registrant was approximately \$9.43 billion at December 31, 2010 (the last business day of the registrant's most recently completed second quarter).*

At August 15, 2011, 118,983,321 shares of the registrant's Class A Common Stock, \$.01 par value, and 75,982,041 shares of the registrant's Class B Common Stock, \$.01 par value, were outstanding.

Documents Incorporated by Reference

Document	Where Incorporated
Proxy Statement for Annual Meeting of Stockholders to be held November 11, 2011	Part III

* Calculated by excluding all shares held by executive officers and directors of registrant and certain trusts without conceding that all such persons are affiliates of registrant for purposes of the Federal securities laws.

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THE ESTÉE LAUDER COMPANIES INC.

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Forward-Looking Statements and Risk Factors

This Annual Report on Form 10-K includes forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. Such statements include, without limitation, our expectations regarding sales, earnings or other future financial performance and liquidity, our long-term strategy, restructuring and other initiatives, product introductions, entry into new geographic regions, information systems initiatives, new methods of sale and future operations or operating results. Although we believe that our expectations are based on reasonable assumptions within the bounds of our knowledge of our business and operations, we cannot assure that actual results will not differ materially from our expectations. Factors that could cause actual results to differ from expectations are described herein; in particular, see Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations Forward-Looking Information. In addition, there is a discussion of risks associated with an investment in our securities, see Item 1A. Risk Factors.

Unless the context requires otherwise, references to we, us, our and the Company refer to The Estée Lauder Companies Inc. and its subsidiaries.

PART I

Item 1. Business.

The Estée Lauder Companies Inc., founded in 1946 by Estée and Joseph Lauder, is one of the world's leading manufacturers and marketers of quality skin care, makeup, fragrance and hair care products. Our products are sold in over 150 countries and territories under a number of well-known brand names including: Estée Lauder, Aramis, Clinique, Origins, M A C, Bobbi Brown, La Mer and Aveda. We are also the global licensee for fragrances and/or cosmetics sold under brand names such as Tommy Hilfiger, Donna Karan, Michael Kors, Sean John and Coach. Each brand is distinctly positioned within the market for cosmetics and other beauty products.

We are a pioneer in the cosmetics industry and believe we are a leader in the industry due to the global recognition of our brand names, our leadership in product innovation, our strong market position in key geographic markets and the consistently high quality of our products and High-Touch services. We sell our prestige products principally through limited distribution channels to complement the images associated with our brands. These channels, encompassing over 30,000 points of sale, consist primarily of upscale department stores, specialty retailers, upscale perfumeries and pharmacies and prestige salons and spas. In addition, our products are sold in freestanding company-operated stores, our own and authorized retailer websites, stores on cruise ships, direct response television (DRTV), in-flight and duty-free shops and certain fragrances are sold in self-select outlets. We believe that our strategy of pursuing selective distribution strengthens our relationships with retailers, enables our brands to be among the best selling product lines at the stores and heightens the aspirational quality of our brands.

For a discussion of recent developments, see *Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations Results of Operations Overview*.

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For segment and geographical area financial information, see *Item 8. Financial Statements and Supplementary Data Note 20 Segment Data and Related Information.*

We have been controlled by the Lauder family since the founding of our Company. Members of the Lauder family, some of whom are directors, executive officers and/or employees, beneficially own, directly or indirectly, as of August 15, 2011, shares of Class A Common Stock and Class B Common Stock having approximately 86.8% of the outstanding voting power of the Common Stock.

Products

Skin Care - Our broad range of skin care products addresses various skin care needs for women and men. These products include moisturizers, creams, lotions, serums, cleansers, sun screens and self-tanning products, a number of which are developed for use on particular areas of the body, such as the face or the hands or around the eyes. Skin care products accounted for approximately 42% of our net sales in fiscal 2011.

Makeup - We manufacture, market and sell a full array of makeup products, including lipsticks, lip glosses, mascaras, foundations, eyeshadows, nail polishes and powders. Many of the products are offered in an extensive array of shades and colors. We also sell related items such as compacts, brushes and other makeup tools. Makeup products accounted for approximately 38% of our net sales in fiscal 2011.

Fragrance - We offer a variety of fragrance products for women and men. The fragrances are sold in various forms, including eau de parfum sprays and colognes, as well as lotions, powders, creams and soaps that are based on a particular fragrance. Fragrance products accounted for approximately 14% of our net sales in fiscal 2011.

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Hair Care - Hair care products are offered mainly in salons and in freestanding retail stores and include hair color and styling products, shampoos, conditioners and finishing sprays. In fiscal 2011, hair care products accounted for approximately 5% of our net sales.

Given the personal nature of our products and the wide array of consumer preferences and tastes, as well as competition for the attention of consumers, our strategy has been to market and promote our products through distinctive brands seeking to address broad preferences and tastes. Each brand has a single global image that is promoted with consistent logos, packaging and advertising designed to enhance its image and differentiate it from other brands.

Estée Lauder - Estée Lauder brand products, which have been sold since 1946, are technologically advanced and high performance products with a reputation for innovation, sophistication, and superior quality. The broad product line principally consists of skin care, makeup, and fragrance products that are presented in high quality packaging.

Aramis and Designer Fragrances - Our Aramis and Designer Fragrances division creates, markets and distributes fragrance and skin care products, including the following brand names:

- **Aramis** - We pioneered the marketing of prestige men's fragrance, grooming and skin care products with the introduction of Aramis products in 1964.
- **Lab Series** - Lab Series Skincare for Men, introduced in 1987, offers a full range of products for cleansing, shaving, treatment and body that are especially formulated to answer the unique needs of men's skin.
- **Tommy Hilfiger** - We have an exclusive global license arrangement for a line of men's and women's fragrances and cosmetics under the Tommy Hilfiger brand name. We launched the line in 1995 with a men's fragrance, *tommy*. Today, we manufacture and sell a variety of fragrances and ancillary products for men and women.
- **Donna Karan Cosmetics** - In November 1997, we obtained the exclusive global license for a line of fragrances and other cosmetics under the Donna Karan New York and DKNY brand names, including certain products that were originally sold by The Donna Karan Company. We launched the first DKNY women's fragrance in fiscal 2000 and the first DKNY men's fragrance in fiscal 2001. Under this license, fragrances have been expanded to include extensive lines of companion bath and body products.
- **Michael Kors** - In May 2003, we entered into an exclusive global license agreement for fragrances and beauty products under the Michael Kors brand name. The fragrances, as well as ancillary bath and body products, are sold primarily in department stores, specialty stores and freestanding Michael Kors boutiques.
- **Sean John Fragrances** - In 2005, we entered into an exclusive license agreement to develop fragrances and other beauty products under the Sean John brand name. Sean "Diddy" Combs played an active role in creating the signature scent, *Unforgivable*. The *Unforgivable* fragrance, as well as other fragrances and ancillary products, are primarily available at select department and specialty stores as well as travel retail outlets around the world.
- **Coach** - In 2006, we began creating fragrances and related products for Coach which were sold exclusively in Coach stores. In 2010, we converted the arrangement to a license. The collection is available in department stores, Coach stores in the United States, retail stores in Japan and Hong Kong, and online at coach.com. We launched the first Coach fragrance in Spring 2007 which embodies the many personalities of the Coach woman-timeless, chic and sophisticated. The signature fragrance launch has since been followed with ancillary beauty products.

Clinique - First introduced in 1968, Clinique skin care and makeup products are all allergy tested and 100% fragrance free and have been designed to address individual skin types and needs. The products are based on the research and related expertise of leading dermatologists. Clinique skin care products are generally marketed as part of the 3-Step System: Cleanse, Exfoliate, Moisturize. Other Clinique skin care products include de-aging solutions to help prevent, halt and diminish the visible effects of sun, wind, stress and pollution and assist in repair to help visibly restore contour, minimize the look of lines and wrinkles. Clinique also offers lines of fragrances.

Origins - Origins was introduced in 1990. Origins seeks to create high-performance natural skin care that is powered by nature and proven by science. Origins sells its products at our freestanding Origins stores and through stores-within-stores (which are designed to replicate the Origins store environment within a department store), at traditional retail counters and in perfumeries. Origins also has a license agreement to develop and sell products using the name of Dr. Andrew Weil.

M A C - M A C products comprise a broad line of color-oriented, professional cosmetics and professional makeup tools targeting makeup artists and fashion-conscious consumers. The products are sold primarily through a limited number of department and specialty stores and at our freestanding M A C stores. We acquired the companies behind M A C in three stages: in December 1994, March 1997 and February 1998.

Bobbi Brown - Acquired in October 1995, Bobbi Brown is an exclusive beauty line developed by celebrated makeup artist Bobbi Brown with a focus on service and teaching women to be their own makeup artists. The Bobbi Brown line includes color cosmetics, skin care, professional makeup brushes and tools, accessories and fragrances. Bobbi Brown products are primarily sold through a limited number of department and specialty stores.

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La Mer - La Mer products primarily consist of high-end moisturizing creams, lotions, serums and other skin care products. The line, which is available in very limited distribution in the United States and certain other countries, is an extension of the initial Crème de la Mer product that we acquired in 1995.

Aveda - We acquired the Aveda business in December 1997 and have since acquired selected Aveda distributors and retail stores. Aveda, a prestige hair care leader, is a manufacturer and marketer of plant-based hair care, skin care, makeup and fragrance products. We sell Aveda products to third-party distributors, prestige salons and spas, cosmetology schools and Aveda Experience Centers, certain non-U.S. department stores and specialty retailers. We also sell directly to consumers in company-operated Aveda Experience Centers and Aveda Institutes, as well as online.

Jo Malone - We acquired London-based Jo Malone Limited in October 1999. Jo Malone is known for its unique fragrance portfolio and luxury products for the bath, body and home. Products are also available through a company catalogue, at our freestanding stores, online and at a very limited group of specialty stores, in approximately 25 countries throughout the world.

Bumble and bumble - In September 2006, we acquired the then-outstanding minority equity interest in Bumble and bumble. We acquired a controlling majority equity interest in June 2000. Bumble and bumble is a New York-based hair care company with two salons that creates high-quality hair care and styling products distributed through top-tier salons and select prestige retailers. We also provide business and hair design education to the Bumble and bumble network of independent salons.

Darphin - In April 2003, we acquired Laboratoires Darphin, the Paris-based company dedicated to the development, manufacture and marketing of prestige skin care products which are distributed primarily through high-end independent pharmacies and specialty stores.

BeautyBank - BeautyBank is the entrepreneurial think tank of the Company. BeautyBank is dedicated to the ideation, development and incubation of innovative new brand concepts for the Company globally. Brands developed and marketed under the BeautyBank umbrella include:

- **FLIRT!** - Established in 2004 by BeautyBank, FLIRT! is primarily available at Kohl's Department Stores and Kohls.com. FLIRT! is a color-oriented makeup line that allows consumers to be their prettiest and freedom to be their flirtiest.
- **GoodSkin Labs** - Established by BeautyBank in 2007, this line of skin care products was created with the expertise of a dermatologist and is sold in a number of countries around the world.

Tom Ford Beauty - In April 2005, we entered into a license agreement to develop and distribute fragrances and other beauty products under the Tom Ford brand name. In November 2006, we introduced Tom Ford Black Orchid, the brand's first signature fragrance. In fiscal 2012, we plan to introduce a full-range luxury cosmetics line. Tom Ford products are available in department stores, perfumeries, pharmacies and select Tom Ford retail stores.

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Ojon - In July 2007, we acquired Ojon Corporation, a company based in Canada which markets naturally-derived, wildcrafted hair and skin care beauty products using ingredients found in the world's rainforests. Ojon products are sold through DRTV and specialty stores.

Smashbox - In July 2010, we acquired Smashbox Beauty Cosmetics, a privately held, photo studio inspired prestige cosmetics company based in Los Angeles. Smashbox sells its products principally in the United States through specialty stores, DRTV and the Internet, as well as internationally through distributors and select retailers.

In addition, we manufacture and sell products under the Prescriptives, American Beauty and grassroots research labs brands. We also develop and sell products under licenses from Kiton, Missoni and Daisy Fuentes. In fiscal 2011, we acquired the license to develop Ermenegildo Zegna products, which we will begin selling in fiscal 2012.

Our heritage brands are Estée Lauder, Aramis and Designer Fragrances, Clinique and Origins. Prescriptives was a heritage brand until fiscal 2010, when we exited the global wholesale distribution of the brand. M·A·C and Bobbi Brown are our makeup artist brands.

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Distribution

We sell our products principally through limited distribution channels to complement the images associated with our brands. These channels include more than 30,000 points of sale in over 150 countries and territories and consist primarily of upscale department stores, specialty retailers, upscale perfumeries and pharmacies and prestige salons and spas. In addition, our products are sold in freestanding company-operated stores, our own and authorized retailer websites, stores on cruise ships, DRTV, in-flight and duty-free shops and certain fragrances are sold in self-select outlets.

We maintain a dedicated sales force which sells to our retail accounts in North America and in the major overseas markets, and in the travel retail channel. We have wholly-owned operations in over 40 countries, and a controlling interest in a joint venture that operates in three countries, through which we market, sell and distribute our products. In certain countries, we sell our products through selected local distributors under contractual arrangements designed to protect the image and position of the brands. In addition, we sell certain products in select domestic and international military locations. For information regarding our net sales and long-lived assets by geographic region, see *Item 8. Financial Statements and Supplementary Data Note 20 Segment Data and Related Information.*

We sell Aveda products principally to independent salons and spas, cosmetology schools, third-party distributors and specialty retailers and directly to consumers at our freestanding Aveda Experience Centers and certain Aveda Institutes. There are currently about 8,200 points of sale, primarily in the United States, that sell Aveda products. Bumble and bumble products are principally sold to about 3,200 independent salons and specialty stores, primarily in the United States. Darphin products are principally sold through high-end independent pharmacies, principally in Europe, representing approximately 3,400 points of sale.

As part of our strategy to diversify our distribution, we have been selectively opening new single-brand, freestanding stores that we operate. The Origins, Aveda and M A C brands are the primary focus for this method of distribution. At this time, we operate approximately 625 single-brand, freestanding stores worldwide, the majority of which are in the United States, and expect that number to increase moderately over the next several years. We also operate approximately 125 multi-brand stores.

We primarily sell BeautyBank products in approximately 1,100 Kohl's Department Stores in the United States and internationally in pharmacies and perfumeries, representing approximately 5,000 additional points of sale.

We currently sell products from 15 of our brands directly to consumers over the Internet through our own e-commerce and certain of our m-commerce sites. Some or all of these brands are sold over the Internet in the following countries: the United States, Canada, the United Kingdom, France, Germany, Austria, Brazil, Australia, Korea, China, and Japan.

As is customary in the cosmetics industry, our practice is to accept returns of our products from retailers if properly requested, authorized and approved.

Customers

Our strategy is to build strong relationships with selected retailers globally. Senior management works with executives of our major retail accounts on a regular basis and we believe we are viewed as an important supplier to these customers. Our largest customer, Macy's Inc., sells products primarily within the United States and accounted for 11%, 11% and 12% of our consolidated net sales for fiscal 2011, 2010 and 2009, respectively, and 10% and 11% of our accounts receivable as of June 30, 2011 and 2010, respectively.

Marketing

Our marketing strategy is built around "Bringing the Best to Everyone We Touch." Mrs. Estée Lauder formulated this marketing philosophy to provide "High-Touch" service and high quality products as the foundation for a solid and loyal consumer base. Our marketing efforts focus principally on promoting the quality, value and benefits of our products. Each of our brands is distinctively positioned, has a single global image, and is promoted with consistent logos, packaging and advertising designed to enhance its image and differentiate it from other brands. We regularly advertise our products on television and radio, in upscale magazines and newspapers, the Internet, and through direct mail and photo displays at international airports. In addition, our products receive extensive editorial coverage in prestige publications and other media worldwide. Promotional activities and in-store displays are designed to introduce existing consumers to different products in the line and to attract new consumers. Our marketing efforts also benefit from cooperative advertising programs with retailers, some of which are supported by coordinated promotions, such as purchase with purchase and gift with purchase. Such activities attract consumers to our counters and allow us to introduce them to our products. Our marketing and sales executives spend considerable time in the field meeting with consumers and key retailers and consulting with demonstrators at the points of sale. These include Estée Lauder Beauty Advisors, Clinique Consultants, Aramis Selling Specialists, Origins Guides and M·A·C and Bobbi Brown Makeup Artists. At in-store counters, demonstrators offer consumers a

"High-Touch" experience with personal demonstrations to market individual products as well as to provide education on basic skin care and makeup application. We conduct extensive sampling programs and we pioneered gift with purchase as a sampling program. We believe that the quality and perceived benefits of sample products have been effective inducements to purchases by new and existing consumers.

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Our High-Touch approach promotes the total value we offer, by leveraging our in-person and virtual assets, as well as merchandising and education, to provide a customized consumer experience. To support this initiative, we are expanding our efforts to evolve our e-commerce-based online strategy into a multi-pronged digital strategy encompassing e-commerce, as well as digital and social media. We have dedicated resources to implement coordinated, brand-enhancing strategies across all online activities. We use the Internet to educate and inform consumers about certain of our brands. Currently, 18 of our brands have marketing sites, 15 of which have e-commerce capabilities. In order to continue to offer unparalleled customer service and set the standard for prestige beauty shopping online, we partner with key brick and mortar retailers to strengthen their e-commerce business and drive sales of our brands on their sites, continue to innovate to better meet consumer online shopping preferences (e.g., how-to videos, ratings and reviews and mobile phone and tablet applications), and support e-commerce and m-commerce business via digital and social marketing activities designed to build brand equity and consumer engagement.

Most of our creative marketing work is done by in-house creative teams. The creative staff designs and produces the sales materials, advertisements and packaging for products in each brand.

Global net expenses for advertising, merchandising, sampling, promotion and product development costs were \$2,345.8 million, \$2,015.9 million and \$1,878.8 million in fiscal 2011, 2010 and 2009, respectively. These amounts include activities relating to purchase with purchase promotions that are reflected in net sales and cost of sales and gift with purchase promotions that are reflected in cost of sales.

Information Systems

Information systems support business processes including product development, marketing, sales, order processing, production, distribution and finance. We expect that these systems will continue to provide pertinent inventory and sales data in the short term. However, as part of our long-term effort to enhance these systems and increase productivity, we are implementing our Strategic Modernization Initiative (SMI), which includes an enterprise-wide global program that we expect will deliver a single set of integrated data, processes and technologies, which would be scalable and used to standardize business processes across brands, operating units and sales locations. As part of SMI, we anticipate the continued migration of our operations to SAP, with the majority of our locations being enabled through fiscal 2013.

In parallel with our SAP deployment, we are creating a more focused global information technology organization utilizing industry standard processes. We are also taking this opportunity to rebalance our information technology resources to better align with our global business growth. We plan to continue to explore opportunities to create a more efficient organization.

Of the many systems currently being utilized, the most significant to our business needs are: (i) a centralized data repository of essential attributes for each of the products we offer, or plan to offer, which enables us to globally manufacture and market products of consistent quality; (ii) a sales analysis system to track weekly sales at the stock keeping unit (SKU) level at most significant retail sales locations (i.e. sell-through data), increasing our understanding of consumer preferences and enabling us to coordinate more effectively our product development, manufacturing and marketing strategies; (iii) an automated replenishment system with many of our key domestic customers, allowing us to replenish inventories for individual points of sale automatically, with minimal paperwork; and (iv) an inventory management system to provide us with a global view of finished goods availability relative to forecasted requirements. As we continue to modernize our key processes and the related systems and infrastructure, we have recently started the development of upgraded capabilities to support our human resource and retail operations. The initial focus for fiscal 2012 will be in North America. The plan is to progressively deploy these systems globally over the next three years as appropriate according to local requirements and priorities.

Research and Development

We believe that we are an industry leader in the development of new products. Marketing, product development and packaging groups work with our research and development group to identify shifts in consumer preferences, develop new products and improve, redesign or reformulate existing products. In addition, research and development personnel work closely with quality assurance and manufacturing personnel on a worldwide basis to provide ongoing technical assistance and know-how, to ensure consistent global standards for our products and to deliver products with attributes that fulfill consumer expectations. The research and development group has long-standing working relationships with several U.S. and international medical and educational facilities, which supplement internal capabilities. Members of the group are also responsible for regulatory compliance matters.

We do not conduct animal testing on our products or ingredients, nor ask others to test on our behalf, except when required by law. We evaluate our finished products in clinical tests on volunteer panels.

As of June 30, 2011, we had approximately 550 employees engaged in research and development. Research and development costs totaled \$85.7 million, \$79.5 million and \$81.6 million in fiscal 2011, 2010 and 2009, respectively. Research and development costs are expensed as incurred. We maintain research and development programs at certain of our principal facilities and facilities dedicated to performing research and development, such as our new Shanghai research and development center, see *Item 2. Properties*.

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Manufacturing, Warehousing and Raw Materials

We manufacture our products primarily in the United States, Belgium, Switzerland, the United Kingdom and Canada. We continue to streamline our manufacturing processes and identify sourcing opportunities to improve innovation, increase efficiencies and reduce costs. Our major manufacturing facilities operate as focus plants that primarily manufacture one type of product (e.g., lipsticks) for all of the principal brands. Our plants are modern and our manufacturing processes are substantially automated. While we believe that our manufacturing facilities are sufficient to meet current and reasonably anticipated manufacturing requirements, we continue to identify opportunities to make significant improvements in capacity and productivity. To capitalize on innovation and other supply c