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In Focus: Business Insights

Think Tank

New Reality Requires New Strategy for Old Guard Fashion Firms

By Allan Ellinger

As the fashion and retail landscape continues to evolve at warp speed, "old guard" vendors and newer digitally native e-commerce companies are rapidly converging at an M&A intersection of mutual need. While online players offer the right combination of technology, data-driven consumer insights and social engagement as well as aesthetics, established, traditionally rooted firms bring operational excellence, product development and sourcing capabilities, in addition to sorely needed working capital.

Veteran brands and labels would be wise to find a next-gen partner to intelligently enter the digital fray as it is often cheaper to buy it than to build it.

It appears that patience in the venture capital and private equity communities for next-generation fashion and retail-tech companies is waning, given burn rates that are too high and success rates that are too low. As capital is beginning to dry up for still unprofitable e-commerce start-ups, opportunities for strategics will open up at prices worth negotiating. The core competencies of design, manufacturing and sourcing, logistics and importing remain intrinsic to the fashion industry and where – via the right strategic relationship – one can provide digital retailers with much-needed business acumen, a strong balance sheet and leverageable infrastructure.

Look at the evolving strategies at Wal-Mart, Tommy Hilfiger and PVH. These "old guard" retailers and brands are jumping into this new industry paradigm, risking capital and brand equity for the opportunity to remain viable with new consumers tomorrow. At Wal-Mart, the $3.3 billion Jet.com acquisition brought digital entrepreneur Marc Lore to the retailer, and he is quickly putting his fingerprint on the organization with new acquisitions and hires that position Wal-Mart to better compete digitally with Amazon et al. Lore has been given the necessary autonomy needed to drive a new business model supported by Wal-Mart's world class logistics and infrastructure. Kudos to Wal-Mart for stepping out of its comfort zone and trying and testing new retail approaches.

An intensive focus on social media and a new consumer is at play at PVH's Tommy Hilfiger. Shifting its operating model to see-now-buy-now, creating the fashion event Tommyland at Venice Beach, leveraging Gigi Hadid's celebrity power and youth appeal, and employing a digitally focused global media campaign all have amplified the voice and reach of the Tommy Hilfiger brand and altered its business model, better equipping the company to compete as a nimbler, just-in-time, fashion brand.

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PVH has been active on the acquisition front as well. In March 2017, this 137-year-old apparel company purchased True & Co. a five-year-old born on the web direct-to-consumer e-commerce bra brand, adding to its Calvin Klein, Warner's and Olga intimates businesses. PVH will now have in-house data analytics that drive True & Co.'s success and can be leveraged across PVH's brands while providing category expertise, global brand management and supply chain know-how that will support True & Co.'s next leg of growth.

Success in today's fashion industry is increasingly tenuous amid the growing number of store closures and bankruptcies in tandem with the seemingly daily arrival of yet another "fashion tech digital disruptor" and the continuing onslaught of Amazon. This year, many traditional apparel brands and labels will see sales volume decline in tandem with fewer points of distribution and competition from the newest flavor of the day. Even established brands with strong consumer loyalty are navigating a choppy landscape as consumer demands are changing faster than their ability to keep pace.

The rate of change is unprecedented and it is working its way through the apparel ecosystem, from design, textile production to assembly and manufacturing, to logistics and distribution and finally to point of sale as digitization impacts the entire supply chain.

These challenges and more will increase for the next few years as creative destruction continues. Over the long haul, the digital shift should generate efficiencies that yield enhanced profitability. Opportunities co-exist with these challenges. But, this requires a new framework, out-of-the-box thinking, and a willingness to test and try new business models. The need for a new vision replete with new goals, new brand and marketing strategies and as importantly, new level talent is a must.

Internal, radical organizational and cultural change is extremely difficult, it often takes too long and can upset the corporate structure. An alternative route is to find a strategic partner that has the digital know-how and the social media savvy that your business lacks, while offering the depth of industry experience digital disruptors need in order to achieve, profitable growth. The right combinations can supercharge both partners and result in synergies benefiting both parties.

This isn't about next season, or next year. This is about long-term survival. The biggest risk today is to do nothing. Simply put, inactivity or indecision is not a strategy.

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Year-to-Date, Pace Slow for M&A Activity

- According to the S&P, transaction values have declined 16 percent.

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According to the latest year-to-date data from S&P Capital IQ, merger and acquisition activity in the U.S. has decelerated with the number of deals lower than the same period last year as well as total transaction value.

To date, there have been just over 6,400 total transactions in the 11 sectors covered by the S&P, which reflects a 4.3 percent decline in deal volume from the same period last year. Transaction values are off double digits, the firm said in its report.

Richard Peterson, principal analyst at the firm, said that "with announced U.S. M&A dollar proceeds in 2017 off 16 percent from year-ago activity, the slump in several sectors' deal [counts] represents another cautionary sign for deal making this year."

The analyst noted that real estate remains the top sector, followed by consumer discretionary – which includes retail and fashion apparel deals. Peterson said real estate M&A activity garnered 32 percent of the total number of deals so far this year. "While that percentage approximates real estate deals share of announced M&A shares at this time last year, the sector has experienced the second-biggest single drop in deal count year-over-year with a decline of 99 transactions," Peterson added.

The firm also said that the second "most frequently targeted sector for U.S. M&A deals to date" is the consumer discretionary market. "However, this sector has suffered the biggest year-over-year drop in number of deals as deal count is 114 lower than a year ago," Peterson said. "Contributing to this result has been a drop in the number of retail industry deals as to date this year there have been 159 announced M&A transactions. That represents the lowest deal count at this point in time for the retail industry since 2009 when 121 M&A transactions were announced."

In the consumer staples market, the S&P said dealmaking was robust. The energy sector is also faring well with the number of deals outpacing last year. "As for areas seeing a notable slowdown in M&A deals, the information technology has reported 854 announced U.S. M&A deals to date this year, the slowest pace of deals since 2013," Peterson said. "Similarly, this year's financial sector M&A deal count of 422 is the most sluggish since the 2013 period when 406 transactions took place."

The analyst also said the pace of dealmaking in the industrial sector is also down.