



## 2009 M&A Outlook: Distressed and Small Deals Abound

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For fashion and retail brands looking for an investor or buyer, there's good news and bad news.

The bright spot is that there are actually still buyers out there looking to make deals despite the credit freeze and recession. The downer is that they only want to pay rock-bottom prices. Investor appetite for paying high multiples for apparel companies has gone the way of shoppers' willingness to pay full-price at retail.

Those firms remaining on the acquisitions hunt include:

- Kellwood Co., which is eager to acquire a denim brand.
- Bagir Ltd., the makers of technologically innovative men's and women's suits, which is eyeing Hartmarx Corp. and eager to buy a knit-shirt-blouse brand.
- Phillips-Van Heusen Corp., owner of Calvin Klein and other brands.
- Fashionology LLC, which last year bought Ellen Tracy.
- Rafaella Group, owned by Cerberus Capital.
- Better knitwear firm Ava.

And there are plenty of companies looking for buyers or investors, including Italy's IT Holding for its Ittierre operation and perhaps some of its other brands, which include Malo, Exte and Gianfranco Ferré; Lambertson Truex, which Samsonite is selling; Fortunoff, which is in Chapter 11 and might be headed toward liquidation; Peter Som; Brioni; de Grisogono; Mariella Burani Fashion Group and Mosaic Fashions, a subsidiary of the bankrupt Baugur Group that owns such U.K. chains as Karen Millen, Oasis, Coast and Warehouse.

Frederick Schmitt, managing director of Sage Group LLC, said that while both private equity and strategic buyers are worried about retail conditions and limited in their liquidity, two types of companies continue to be attractive investment candidates this year.

The first, he said, are companies that are still doing well even in the economic downturn. The second is a company in trouble that "needs to do a transaction to raise capital or fix their capital structure."

The problem with the first type is that anyone who can is holding off on selling. Tory Burch, which sources said continues to discuss the sale of a stake in the company with several interested parties, is a notable exception. But sources doubt whether a price will be agreed upon, because Burch doesn't require immediate outside investment.

"Who wants to sell at what they perceive to be at historical lows?" said Marc Cooper, managing director and partner at Peter J. Solomon Co. "This is a terrible time to be thinking about the sales process."

Hudson Jeans, a West Coast denim company that does more than \$60 million in volume, has been approached by numerous potential bidders, including Fireman Capital Partners, but the firm is willing to wait for the right price and partner, according to Hudson president and chief executive officer Peter Kim. Fireman Capital declined comment.

“Obviously, for the right price, anything is for sale,” Kim said. “But our business is good — we’re actually on track to grow this year — and we don’t need to sell if there’s not a substantial opportunity.”

A few big players may go on the block as the economy pushes them into bankruptcy — or pre-bankruptcy looking to be saved through investment — as has already happened this year for suit maker Hartmarx Corp. Numerous companies have expressed interest, including Bagir.

The cash-rich Bagir is potentially interested in making several acquisitions this year. In addition to eyeing the multibranded suit maker, Bagir would like to buy a knit-shirting-blouse company to help in its expansion beyond suits to tops, according to company executives.

“It’s like antique shopping,” said Tim Danser, Bagir vice president of marketing. “If you go in looking for one specific thing, you’ll overpay. We’re out looking for good deals on good companies.”

Bagir isn’t the only manufacturer looking to expand its business in these contracting times through a well-priced acquisition.

**“Companies have lost volume and are looking to recover it through an acquisition when they have a strong balance sheet,” said Jack Hendler, Net Worth Solutions Inc. president. “As the channels of distribution are shrinking, where do we put the product? We try to help pair them with a company that has distribution that they don’t.”**

**For example, he said a \$500 million vendor is looking to buy a company that has distribution at Kohl’s. Another trend he foresees is retailers and vendors linking up for a vendor’s brand to step in as the retailer’s private label, as stores seek higher margins and find their credit restricted. For example, he said a 50-door chain based out of Boston is looking for a casual women’s wear resource.**

Kellwood has been searching for acquisitions for months, particularly a denim company to create a competency in that category that its other brands could leverage. At the same time Kellwood explores selling Hollywould, the Sun Capital Partners-owned firm is said to be eyeing a mainstream-priced West Coast denim company, as well as Joe’s Jeans Inc., which has been trading for about 30 cents a share and has about 60 million outstanding shares. Kellwood declined to comment on which companies it is in talks with. Other companies are said to be interested in Joe’s, as well.

A spokesman for Phillips-Van Heusen said the company was still eyeing strategic acquisitions, with a cash position that is strong enough to weather the economic storm even with the purchase. Still, he noted, “the economy factors into all decisions today.”

Fashionology co-founder William Sweedler said the company receives several calls a day from companies looking for investors, and Fashionology is in talks to buy a profitable men’s brand and a profitable accessories brand, being cautious about distressed firms.

“Investing in fashion can be a dangerous business,” said Sweedler. “For the first time, I’m questioning free [not paying for the brand, just assuming ongoing costs] — which is what a lot of companies are going for right now. We’re not in deal mode — we’re in opportunistic mode — but our primary focus has to be on operating our existing business.”

Sweedler added the company is looking for brands with tangible licensing potential to guarantee contracted income, as well as diversified retail partnerships to mitigate the risk of any particular store going out of business.

But while there still might be deals done in 2009 despite the recession, the year follows a dismal 12 months for M&A activity overall.

If the pace from September to January continues through the rest of 2009 — which is what M&A leaders predict, based on both credit access and the general gloom in retail these days — this year may rival 2002's 23 deals for the fewest public ones done in the last decade, according to Factset Mergerstat LLC.

"It was a very tough year for M&A because 2008 was probably one of the toughest years in memory for retail performance," said Cooper of Peter J. Solomon, adding their restructuring group's work on the distressed market is paying the bills that M&A had formerly. "And 2009 has started off the same way 2008 ended."

There were 40 public arena deals within the sector in 2008, down 31 percent from 58 deals in 2007, which was down 22 percent since 2006's record 71 deals. Moreover, the total value of deals fell 56 percent to \$2.4 billion in 2008 from \$5.4 billion in 2007, according to Factset Mergerstat.

But not all of 2008 was a bust for industry M&A activity. The first eight months of the year saw 35 deals. The slowdown came between September and November, which saw only two deals, while December picked back up with three.

So far in 2009, two relatively small public deals have taken place:

- On Jan. 19, Sportsclick Inc., a Canadian wholesaler of licensed sports goods, acquired Southprint Inc., a Martinsville, Va.-based wholesaler of licensed NASCAR apparel, for \$2.4 million. Southprint had revenues of \$15 million in 2007.
- On Jan. 21, Technology Resources Inc. bought the Kona, Hawaii-based Shaka Shoes Inc. for about \$4 million, according to Factset Mergerstat, and the parent company has adopted its new acquisition's name.

Michael Dart, a principal at Kurt Salmon Associates and head of its private equity and strategy practice, said deals were being funded by putting down at least double the equity capital, versus debt capital, than required in the boom days of yore. With companies needing to put down 30 to 40 percent equity, versus 15 to 20 percent previously, the size of deals that can be done is limited. Dart said he expected middle market deals of \$20 million to \$300 million in enterprise value.

"Whatever deal you put in place [has to be able to allow the company to] survive continued negative comps for a continued time," Dart said. "Companies are maintaining all of their capital to maintain liquidity. They are gaining on their weaker competitors rather than buying them. But for contrarian investors with a reasonable amount of capital and a long holding period, this could be a great opportunity to make great long-term returns."

And while elective deals may have slowed due to increased caution, distressed deals have increased, according to M&A sources. In these cases, both size and swiftness are essential. Those deals can happen for as little as free — assuming the cost of running the brand going forward — up to a small multiple, said sources. They also must be fast, before the retail situation worsens.

“There are people looking for value transactions. A lot of larger — \$150 million and up, generally speaking — privately held businesses with equity know that if they can add some good top line to their business [by buying a \$30 million to \$70 million business], it will be of value,” said Allan Ellinger, senior managing partner of Marketing Management Group.