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Strategic Buyers Step Up to the Plate; Credit crunch has led to a drying up of private equity money and an opportunity for strategic purchases

BY BRENNER THOMAS

NEW YORK—The slowing economy has touched every corner of the apparel industry, even how companies are bought and sold.

The private equity concerns that had voraciously snapped up fashion companies in the last few years, lured by the potential for fast growth and high margins, are pulling back, and homegrown apparel companies are stepping in, according to merger and acquisition experts. “The deals these days are far more strategic than financial,” said Allan Ellinger, senior managing director of Marketing Management Group, an apparel consultant.

The old paradigm in which an investor group, like Permira, buys a fashion company, like the Valentino Fashion Group, in hopes of maximizing revenues and eventually selling the enriched brand, has given way to fashion companies buying other fashion companies in order to achieve a strategic goal, be it increasing market share or moving into new classifications or tiers of distribution.

To wit: G-III, an outerwear maker, bought Wilsons The Leather Experts earlier this year, giving the company a turnkey retail business and a stake in the outlet distribution of its outerwear. Another active buyer, sourcing giant Li & Fung, continues to move up the supply chain as it nabs worldwide distribution facilities and U.S. wholesalers, including Giant Merchandising, a T-shirt maker, and Van Zeeland, a handbag importer. “Li & Fung is looking to move beyond their original mandate and this market is providing some good deals,” said Andrew Jassin, managing director of the Jassin-O'Rourke Group, a retail apparel consultant.

Jack Hendler, president of Net Worth Solutions, a fashion and retail M&A firm specializing in selling midsize brands, said private equity comprised 70 percent of his deals until last year. Now that figure is down to 50 percent. “We still have some of what I call strategic equity buys where the buyer is an investment group that already has holdings in apparel.” He cites one such deal in which a private equity group is buying an activewear brand in order to capitalize on the brand's good relationship with Kohl's. But aside from those types of deals, pure strategic plays are on the rise.

Experts said the number of transactions in 2008 is on par with recent years, but deals are taking longer to close, a result of tighter credit. Hendler said he's also handling more distressed sales, in which challenged companies look for a buyer to stay afloat. Since Labor Day, half of the inquiries to his office have been from “stressed” vendors. “Between tightening credit and slower sales, some companies need strategic partners to survive.”

Tighter credit will also lead to more employee stock ownership plans, according to Jassin. These plans allow companies to raise capital, but maintain control by offering ownership stakes to their employees.

Multiples, or the number that helps determine a company's value, have fallen as the prospect of fast growth fades. Simply put, a company's earnings multiplied by this number gives an estimate of the purchase price. Multiples for apparel companies have fallen a full point in the last year according to Hendler, from 4.5 to 3.5.