DTC filling the gap left by international tourists

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SOMETHING NEW is on the horizon when brands sound optimistic even when their retail and wholesale businesses are lagging. Although the recent dips have a lot to do with the drop in spending by international tourists, brands are also feeling more confident for another reason. They have something to fall back on: They're omnichannel now.

And direct-to-consumer in all its forms, from outlet stores to ecommerce to retailer-driven consumer clubs, is providing brands with a lot of tools for honing their strategies. While Coach focuses on operational and merchandising innovations in its stores, Kate Spade is totally excited about its new ship-from-store strategy. Direct-to-consumer revenue at Under Armour grew 33 percent in the first quarter, and at VF the DTC is helping to buoy revenues.

We checked in with these brands in May. Here's what else they had to say.

Kate Spade, which operates 64 outlet stores, says its new ship-from-store initiataive is driving omnichannel sales upward.

Kate Spade posts Super-duper comps

Kate Spade & Company's first-quarter 2016 sales of $274 million was up 14.5 percent, and that's not including the company's direct to consumer segment, where same-store sales rose 19 percent, or 8 percent when ecommerce is taken out. To date, this comp momentum is the healthiest in retail and attests to expanding market share in handbags and accessories. This market is growing at a low single-digit pace with better full-price selling.

On the May 4 call with investors, CEO Craig Leavitt talked about the outlet channel, where most of Kate Spade's margin erosion is concentrated.

"Decelerating traffic from the international tourist base is causing a more promotional environment overall in the outlet channel," Leavitt said. "But remember, we have an extremely low crossover between our full-price and our Kate Spade Outlet consumers, and that gives us a great deal of confidence in terms of being able to maintain our market share in the outlet channel without diluting the brand.

"Overall we continue to focus on our quality sale efforts and merchandise our markdown," he said. "We will make sure we are using markdowns [for] aging inventory or challenging products and not using storewide promotions that we've seen in the past. Merchandising our markdowns is a key strategy for us to ensure that the consumer has a desire to buy our product at full price as well as meet the needs of our Kate Spade Outlet customers."

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> **George Carrara, president and COO Kate Spade**

George Carrara, president and COO, addressed Kate Spade's omnichannel impact on Q1, particularly the ship-from-store strategy.

"Our industry-leading first quarter comp was driven by double-digit growth in both sectors of our ecommerce business and we expect this performance to continue as the year progresses," Carrara said. "In brick-and-mortar where our comp was 8 percent, it was really understated and it would have been a double-digit comp if not for two important factors: first, declines in international store traffic, and second – this is new – ship-from-store.

"Ship from store is a new omnichannel initiative that drove sales for the first time in Q4, continued to drive sales in Q1, and will continue to drive sales for the rest of the year," he said. "These ship-from-store sales are credited to the ecommerce channel and as a result, decrease the reported comp on the brick-and-mortar side. We will continue to blur lines with the omnichannel initiatives."

Kate Spade and Company entered Q2 with a store fleet of 261 company-owned stores: in North America, 105 full price and 64 Kate Spade Outlet stores, and internationally, 24 full-price, 14 Kate Spade Outlet and 53 concessions. Another 121 partnered stores and 28 licensee-operated partnered locations bring the total Kate Spade store footprint to 409 units. The company plans to open 15 company-owned stores and a total of 40 to 45 net company-owned and partner-operated stores in 2016. During the first quarter nine partnered and JV stores and five company-owned stores opened.

Innovation pushes Coach outlet growth

Coach reported sales of $1.03 billion – an 11 percent sales gain – for its third quarter 2016, which ended April 2. Coach brand sales rose 3 percent to $954 million, and in North America, Coach brand sales grew 1 percent to $499 million. Coach North America comps were flat while comp trends accelerated during the period in full price, and Coach Factory store sales were positive in February and March, and into April.

CEO Victor Luis told analysts on April 26 that Coach is holding its own despite the instability of the international shopper.

Coach's Snoopy fashion vignette, designed by Stuart Vevers, was well received at Coach Factory Stores, which posted positive sales in the first three months of 2016.

"In spite of volatile tourist spending flows, as well as macroeconomic and promotional headwinds, both our retail and our Coach Factory Stores in North America sequentially improved from the holiday quarter, and e-commerce was an overall contributor as well," Luis said. "Our international businesses posted strong growth…highlighted by double-digit increases in Mainland China and Europe, as well as sales gains in Japan and Other Asia.

"Taken together, we are delighted with how our plan for the Coach brand continues to unfold and is driving improvement across our financial metrics," he said. "We are on track to return to positive comps in North America in the fourth quarter and to achieve an inflection in our profitability."

Product with heightened emotional appeal drove improvement at Coach Factory Stores, Luis said.

"Our Snoopy fashion vignette was particularly well received," he said, "and we will continue to surprise and delight the consumer in this channel with increased levels of innovation. We continue to transition the fleet into our modern luxury concept, driving comp improvement. Stuart Vevers' designs and updates represented over 90 percent of the Coach Factory Store assortment with key new styles in women's along with reimagined styles performing well. On the men's side, bags and backpacks drove our business. The exceptional response to the Snoopy fashion vignette proves that the Coach Factory customer will respond to innovation and novelty."

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> **Coach**

Men's represents about 17 percent of Coach's global sales and the company projects mid-single growth in fiscal 2016 (which ends June 30). The company expects men's to build into a $1 billion business. In North America an intensified focus on men's in key stores has been tested, and having received a strong consumer response, will be rolled out to an additional 25 full price and 40 Coach Factory doors.

Andre Cohen, president of Coach North America, added insight on the company's outlet strategy.

"Both full price and Coach Factory stores actually improved at a similar rate sequentially," Cohen said, "so we are pleased with the performance in both retail and in Coach Factory outlet locations. We have always maintained that full-price retail would lead, and in absolute terms, the full-price retail performance is slightly ahead of outlet. We have been working design and innovation into the outlet channel.

"We realize, that when you have real innovation and emotion, as we had with Snoopy, it trumps price. It was successful and it's something that we're trying to replicate over the next few quarters, both in terms of these one-offs and in terms of putting more design and innovation into the outlet channel."

Coach's overarching strategy is to elevate the brand's image to modern luxury via stores that are sophisticated, warm and inviting. Innovations in the outlet channel, notably men's standalone Coach Factory stores, have not produced the same productivity improvement as in the 67 renovated full-price stores.

"We have not moved the needle that much," Cohen explained. "We've used our Woodbury Common store as a pilot where we've made small alterations such as moving more products to the floor from the wall and it positively affects conversion. We had fragmented the stores a bit too much, eliminating a 360-degree view when entering the store.

"We're making many small operational improvements, and the good news is that at Woodbury, where we started these tweaks about two to three months ago, we have seen an improvement in conversion and [dollars per transaction]. So good learnings, and we will continue implementing them throughout the chain."

As of March 26, 2016 Coach operated 446 stores in North America, including 204 Coach Factory stores, 196 Japanese stores, 181 in Greater China, 105 in Asia, and 37 in Europe for a total of 965 Coach stores and 61 Stuart Weitzman stores.

Under Armour races ahead in all channels

Net revenues rose 30 percent at Under Armour in the first quarter 2016 to $1.05 billion driven by double-digit gains in all channels, geographies and categories. Wholesale revenues rose 28 percent to $744 million while Direct-to-Consumer (DTC) grew 33 percent to $266 million. Two standout categories include international (56 percent sales gain to $149 million) and footwear (64 percent sales gain to $264 million). Footwear benefitted from the Stephen Curry signature basketball line, the launch of Under Armour's first smart running shoe and a new line of golf shoes.

On the April 21 call with investors, CEO Kevin Plank spoke of two major achievements: expansion in China, where Q1 sales exceeded the 2014 total, and the upcoming addition of 120 more stores. Bringing NBA player Stephen Curry, to China drove footwear sales there to nearly one-third of the Under Armour's total sales in China.

On the ecommerce front, Under Armour now operates 26 global sites and noted that more than 50 percent of U.S. traffic came through mobile devices in Q1, mirroring the rapid transformation in how consumers access the Under Armour brand.

"Our women's e-commerce growth rate continues to outpace the growth on the men's

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side," Plank said. "This year our total women's business is projected to exceed $1 billion." With the recent bankruptcy filing of Sports Authority as well as a fairly pervasive retail malaise, Under Armour's ability to achieve 30 percent growth is a testament to the vitality of the Under Armour brand.

Longer term, Plank's strategy of Connected Fitness, where Q1 sales rose 119 percent to $19 million with its community of 160 million athletes is promising as it adds 100,000 people daily, thereby expanding the community of connected athletes and ultimately Under Armour shoppers.

"Data is the new oil," Plank said. "Those who have the data, those who understand the consumer, are going to win. Under Armour's Connected Fitness community of 160 million plus registrants every single day are volunteering information; how much they slept, how active they are, what they did when they exercise, how hard they exercise. One million are using our Gear Tracker asking us to tell them when they should buy a new shoe by evaluating the type of terrain they're running on and the distance they're running on. The information we're getting is extraordinary.

"Frankly, we are in the first inning of this world and we have the ability to use data as a key initiative for Under Armour Connected Fitness. Our Q1 Connected Fitness revenues are equal to what we did in all of 2015. We see premium and subscription as opportunities. Our job is to find synergistic ways that enhance consumer engagement and drives value to the community. We've put up a $200 million revenue target by 2018 for Connected Fitness."

As of March 31, 2016 Under Armour's store fleet consisted of 198 company-owned stores globally, comprised of 162 Under Armour Factory House stores and 36 full price Under Armour Brand House stores.

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Direct-to-consumer business model sets a new pace at VF

VF Corp.'s first quarter 2016 revenues were flat at $2.8 billion led by a 7 percent gain in the direct-to-consumer category and a low single-digit comp gain. Outdoor/action sports and jeanswear coalitions outperformed consolidated revenue growth as both coalitions reported a 2 percent sales gain, to $1.6 billion and $711 million, respectively. These two coalitions represented a combined 83 percent of Q1 revenues. The remaining coalitions all reported revenue declines.

A low-teens gain in the outerwear & action sports business drove DTC revenue growth, which represented 26 percent of Q1 revenues, or $738 million, up from 24 percent a year ago. This gain was offset by a mid-teens percentage rate decline in sportswear and a high single-digit decline in the contemporary brands coalition.

CEO Eric Wiseman told investors on April 29 that VF's direct-to-consumer is where the gains are.

On the April 21 call with investors, CEO Kevin Plank spoke about the upcoming addition of 120 more stores around the globe; the brand now operates 132 outlet stores.

"Our fastest-growing brands this quarter is a tie between The North Face and Kipling, each with 8 percent currency-neutral growth," Wiseman said. "The real strength in the quarter came from our DTC business. This tells us that our brands and products are resonating strongly with consumers who are happy to show their approval by buying. However, our wholesale business is still navigating through the inventory carryover from what was a challenging fourth quarter at retail in general."

Global performance by brand:

The North Face saw mid-teens growth in DTC and a low single-digit gain in wholesale

Vans' revenues rose 2 percent, with a nearly 20 percent increase in DTC, offset by wholesale declines

Timberland's revenues increased 3 percent with low single-digit growth in both D2C and wholesale

In the Americas, VF president and COO Steven Rendle said reduced traffic and a warm winter had hurt performance for Timberland (though women's boot sales were up nearly 50 percent), the sportswear coalition, Nautica and Kipling.

CEO Wiseman pointed out that retailers are demonstrating cautious buying behavior while consumers are in a buy-now-wear-now mode.

"This explains the big disconnect between our DTC numbers, which are very strong, and our weak wholesale numbers," he said. "Fortunately, with our supply chain excellence, we are able to respond to that demand when it comes…You're seeing one of the strategic reasons we have a direct-to-consumer channel. We are able to adjust our inventories within our stores very, very quickly because it is all our inventory. And we think that is one of the reasons that our DTC business was up 8 percent in Q1 versus our wholesale business, which was up low single digits.

"We are able to react for our wholesale partners at the same speed, but we can't comment about the inventory they have in their stores. They buy based on what they see consumers wanting [based on] what their current inventory situation is – not just in our brands but across their total operation.

"Because the entire inventory in The North Face Company is North Face inventory, we can move it back and forth and in and out of our stores, and this makes us a bit more nimble. We think it is one reason we are seeing growth. We have a different business model."

The VF store fleet at the end of Q1 totaled 1,541 VF-owned stores (up from 1520 at the end of 2015) including 180 The North Face Stores, 500 Vans stores, 250 Timberland stores, 60 Kipling stores, 30 Napapijri stores, 50 Lucy stores, 80 Nautica stores, 80 7 For All Mankind stores, 30 Splendid stores, one Ella Moss store and 75 VF Outlet stores. Approximately 70 percent of VF-operated stores are full price and 30 percent are outlet. V