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Special Report
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Dressed for success
Specialty clothing retailers

By Toon Van Beeck

Cornering niche markets in this retail sector requires setting the business apart from the competition

In 2011 the US economy will expand, consumer sentiment and income will grow, and unemployment will fall. These factors will spur spending, and clothing retailers will benefit

In an era where specialization is a prerequisite for business success, the term "specialty retailer" sounds almost redundant. In fact, specialty retailing is a highly competitive segment, and those that prosper have unique characteristics that set them apart from the competition. IBISWorld has identified eight specialty clothing retailers that are expected to generate a combined $208.5 billion in revenue during 2010 and account for about 0.3% total economic output. Family Clothing Stores, which is expected to pull in a little over $83.3 billion in sales this year, is the largest, while Clothing Accessory Stores generates just over $7.0 billion at the other end of the spectrum.

Specialty clothing

Like all US retail categories, this sector felt the heartaches that the recession caused. Revenue declined for six of the eight specialty clothing industries during the 2006 to 2010 period, and only Clothing Accessory Stores managed to generate substantial growth (annualized 4.9% per year). Since 2006, poor consumer sentiment levels, a sharp drop in per capita disposable income and a high and rising unemployment rate negatively impacted these industries.

Despite the downturn, IBISWorld forecasts improved sector performance for the four-year period to 2014. All eight industries are expected to expand at an average annualized rate, and Clothing Accessory stores will lead the way with average growth per year of 7.2%. This industry also exhibits the most favorable profit margin, with average returns at 11.0% of revenue while the majority of the others have profit margins between 3.0% and 5.0%. IBISWorld projects that the US economy will expand about 2.7% through 2011, consumer sentiment will rise to its highest level since 2007, per capita disposable income will grow its fastest since 2007, and unemployment will begin to fall. These factors will spur spending, and clothing retailers will benefit – hence the favorable growth in the coming years.

IBISWorld's industry risk scores are another key barometer of industry health, as they measure the difficulty of operating in an industry. As summarized in the following table, specialty retailers generally exhibit greater risk than the economy as a whole. This is evidenced through the relatively high scores as observed in the table, with only Family Clothing and Children's & Infants' Clothing Stores exhibiting a level of risk below the entire US economy. Firms that operate in riskier industries like Men's Clothing Stores, which has the

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highest risk score among the eight specialty retail industries, may exhibit greater failure, higher competition, stronger barriers to entry or expansion problems in the coming 18 months.

The major players

The clothing retailing industry is very competitive. Of the eight identified industries in this report, six possess a high level of competition intensity while the remaining two have medium levels. Competition tends to be high and concentration tends to be rather low, meaning hundreds of thousands of individual operators compete with one another. Meanwhile, external competition such as that from mass merchants in the department stores industry like Macy's, Target and Sears, also pressures the industry. Together, competition combines to pose challenges for specialty clothiers. There are, however, a number of large operators, and IBISWorld has identified close to 30 that have market share greater than 3.0% in their respective industries. As seen on page three, the overall size and performance of these companies have differed since 2006.

The clothing sector

Incorporating the industries of Men's Clothing Stores, Women's Clothing Stores, Children's & Infants Clothing Stores, Family Clothing Stores, and Lingerie, Bridal, Swimwear & Uniform Stores, the clothing sector houses the largest of specialty clothing retailers. Firms like Limited Brands (Victoria Secret), The Gap, TJX, Ross Stores and Toy's "R" Us (operating under Babies "R" Us) operate in this space, and most of these larger players are finding ways to post positive numbers.

IBISWorld's analysis shows that since 2006, the big-name player and those that have a somewhat sizeable market share have exceeded the industry average in terms of performance. The majority of the industry's major players outdid average revenue during the past four years and generated a greater profit margin than what the industry's average cost structure stated.

Of note within the clothing sector is Jos A Bank Clothiers (9.8% market share within Men's Clothing Stores). This company has managed to achieve an average annualized growth of 13.4% since 2006 while also achieving a gross profit margin of about 15.0% during the past year. This company has some of the lowest cost of goods sold (COGS) among all identified specialty clothing retailers, and its COGS are also lower than the industry average for Men's Clothing Stores. This is just one area in which they

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	2010 Revenue ($m)	2006-10 Annualized growth (%)	2010-14 Annualized growth (%)	Average profit margin (%)	Industry risk score
Family clothing stores	83,305.9	-1.7	2.6	3.9	Medium
Women's clothing stores	38,645.4	-2.6	2.4	4.6	Medium-High
Jewelry stores	29,644.6	-3.8	3.6	7.3	Medium-High
Shoe stores	19,863.5	-6.6	1.5	3.9	High
Lingerie, bridal, swimwear and uniform stores	11,920.2	-1.9	2.9	3.9	High
Children's and infants' clothing stores	9,630.1	0.3	3.2	3.0	Medium
Men's clothing stores	8,511.6	-3.6	0.7	4.3	High
Clothing accessory stores	7,025.3	4.9	7.2	11.0	Medium-High

SOURCE: IBISWORLD

Specialty clothing retailers continued

have managed to succeed, and this success has certainly aided in their strong profit figures.

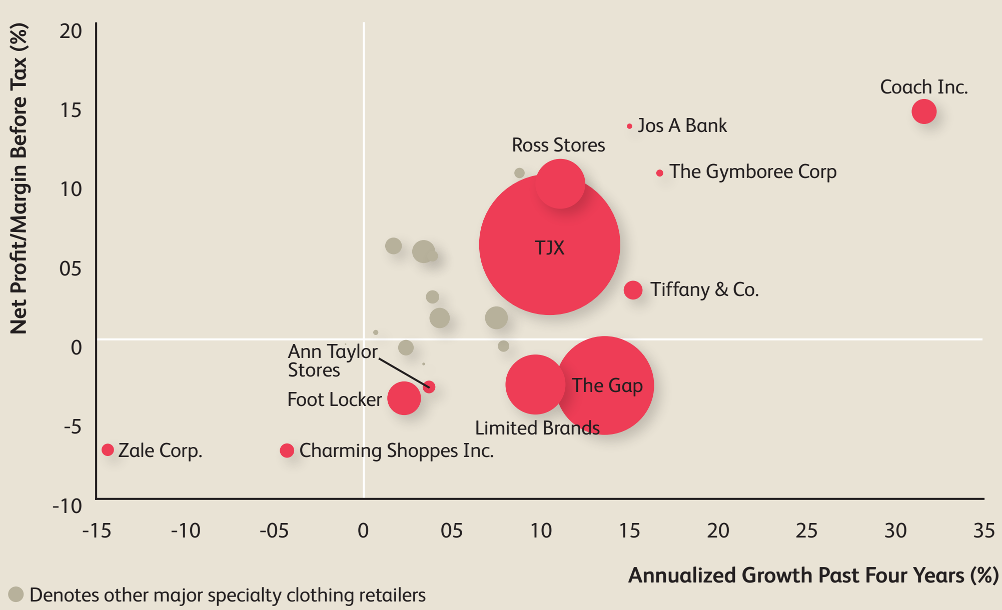
The Gymboree Corp is another major clothing sector player that stands out. Operating in the least risky of all identified specialty clothing retail industries (Children's & Infants Clothing Stores), the Gymboree Corp has bridged the gap to its larger rivals as one of the biggest players in its respective industry. Back in 2006, The Gymboree Corp held roughly 7.0% of the Children's & Infants Clothing Stores market, however today they hold about 9.3%. Toys "R" Us (private company) is clearly the industry's largest player with a 23.5% market share, while The Children's Place Retail Stores ranks second. The Children's Place Retail Store observed an average decline in revenue of about 0.5% per year since 2006 compared to The Gymboree's 10.5% growth, meaning one player has decreased its share while the other has expanded and improved its competitiveness. It may be a matter of time before the Gymboree Corp becomes the number-two player in this industry.

Last for review comes the sector's largest industry: Family Clothing Stores. The biggest players here are The Gap (16.3% market share), TJX (15%), Ross Stores (9.3%) and Abercrombie & Fitch (3.3%). Note that these players have a roughly similar operating performance to one another, falling roughly within the same "band." The Gap though achieved the greatest profit margin, while Ross Stores experienced the strongest growth since 2006. Family Clothing stores is considered a less risky industry, and volatility in this sector is somewhat reduced as a result because the retailed items are deemed essential. For investors seeking risk aversion, this industry may be the best of all specialty clothing retailers.

The jewelry sector

During the past few years, the Jewelry environment has been one of the riskiest industries in which to operate. Today, the

Major Specialty Clothing Retailers



NOTE: FIGURES REPRESENT THE MOST RECENT PUBLISHED ANNUAL YEAR

SOURCE: IBISWORLD

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level of risk has diminished and the outlook looks more favorable, however, the industry still falls within the “medium-high” risk band. Risk, however, also brings high returns, and the comparison between Tiffany & Co. versus Zale Corp is a worthy consideration.

Tiffany & Co. ranks among the more successful specialty clothing retailers over the past four years, with strong annualized growth and a profitable business. This is in great contrast to Zale, which has seen poor annualized growth and losses. Signet Group, the largest player within the Jewelry Stores industry, falls between these two players in terms of past performance.

Although growth has been relatively slow for Tiffany & Co. since 2006, the company has maintained its profit margin. This has been critical to success, but the same cannot be said for Zale Corp., one of its closest competitors.

Zale Corp. has observed strong declines in revenue and profits since 2006 and is considered a struggling retailer. The market position of Zale Corp. is vastly different than Tiffany & Co., as it has a greater focus on mid-tier jewelry prices that makes customer attainment difficult because of greater competition from discount retailers and department stores. As a result, generating solid returns is difficult, and consequently this company ranks in the lower end of specialty retailers.

From an industry perspective, Jewelry Stores face difficulties in terms of strong external competition, the rising price of gold and a slow return of disposable expenditure that may hamper performance. In light of these conditions, struggling retailers like Zale’s may need to improve their key success factors such as stock control, fashion trends and product presentation as well as its brand and profile in the market.

The accessory and shoe sectors

As noted earlier, the Clothing Accessory Stores industry is certainly the standout performer among IBISWorld’s eight identified retail industries. Growth, profit margins and outlook are all positive, so it is little wonder that Coach Inc. is one of the best performers of the identified companies.

Coach Inc., like Tiffany & Co., works on the principle of “affordable luxury.” This was essential during the recession, and the company has managed to maintain its brand image while continuing to generate sales. This is a tremendous effort, as many high-end retailers have been negatively impacted by wealthy individuals also looking to cut back during the recession. Coach Inc. managed, however, to keep its price level during these tough years and increase sales within its factory stores, which has helped to eliminate any tarnishing to its brand. COGS for this company are the lowest among all the identified retailers, and this is yet another key factor to its strong performance. The outlook looks very good for this industry, so expect Coach Inc. to continue to improve its performance.

Finally, Foot Locker is yet another large retailer that has experienced a difficult time during the past few years. The company operates in a tough industry with high levels of competition, a high percentage of COGS, one of the highest risk scores for these identified retailers and relatively low average profit margins at 3.9%. Despite these impediments, the company has maintained average revenue declines (3.7%) that are lower than the industry average (6.6%) since 2006, meaning they have retained market share as a whole. Also, the company’s profit is close to the industry average, which also represents a positive performance. Compared to peers like Collective Brands and Brown Shoe

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Company, however, Foot Locker's performance has not been as strong. Foot Locker is the second largest US shoe retailer, but the Brown Shoe Company is closing the gap while Limited Brands has extended its strength with this recent performance. Once again, a focus on the key success factors and industry drivers is critical, as the achievement of these will help maintain Foot Locker's market share and help the company return to growth.

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