February 23, 2016

Beyond Capital: Designers Look for Deals That Bring Expertise

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Proenza Schouler RTW Spring 2016
Giovanni Giannoni/WWD

NEW YORK — As celebrities, buyers, editors — and now just regular Joes — all jockey for position at the runway shows this month, the most important front-row seat might be reserved for someone else: potential investors.

Experts said there's a slow boil of designer dealmaking going on behind the scenes in the U.S. and that it's taking a new and different flavor than it has in years past. That's because designers are caught between frayed retailers, cautious consumers, an impossible production schedule and spastic digital evolution.

Many are looking for not just a capital infusion but a partner to help them build businesses that live up to their brand recognition.

"It's not enough to find an investor who just has a lot of money and wants a quick in and out," said Daniel Silver, cofounder of men's wear brand Duckie Brown. "We need a creative investor."

The 15-year-old self-funded company is ready to expand, but Silver said he could use some help developing the brand's infrastructure and potentially tapping into more factories.

"We're looking for someone who really understands that this is a long-term investment and that we actually have real talent and passion here," said Silver, who described the process of talking to potential backers as "dating," with a continual give and take.

"It's business, you have to be realistic and you have to be willing to negotiate," he said. "You get a lot of Wall Street people who are young, who want to invest or who want to be part of the glamour of fashion. Well, there are many things that fashion is, but if you can find the glamour, you can have it. It's a lot of hard work."

Duckie Brown isn't alone in trying to strike the right balance and find both capital and expertise. There are plenty of brands out there trying to shake the money tree. But would-be investors say brands still have an overinflated sense of what they're worth, while sellers argue that you get what you ask for and that while it's nearly impossible to negotiate a price up, it can be negotiated down.

"There's been a very heated marketplace with valuations," said Ron Frasch, operating partner at Castanea Partners, which took a stake in Proenza Schouler last year. "We're not sure that those valuations are always appropriate, particularly with a young brand, with a number of elements that are unproven and would have to be validated to justify the prices."

Frasch, who was previously president at Saks Fifth Avenue and chief executive officer at Bergdorf Goodman, said people are still trying to figure out just the right way for brands and investors to partner up.

"While there's interest, there's probably not a lot of [sale] activity right now, which is not unusual at this time of the year because people are just validating 2015 results," he said. "I would assume there would be more activity later in the spring season."

Still, there has been a fair bit of dealmaking in the U.S. over the last nine months. Since last summer:

• Vivian Chou's Bright Fame Fashion took a controlling interest in Thakoon.

• Farol Asset Management and a group of investors put money into Cushnie et Ochs.

• American Eagle Outfitters bought Todd Snyder in an $11 million cash and stock deal.

• Brentwood Associates acquired the 103-door J. McLaughlin chain.

• Lee Equity-backed InterLuxe bought A.L.C.

• Castanea Partners invested in Proenza Schouler, joining Andrew Rosen, John Howard and others.

• Resonance took a stake in Costello Tagliapietra to relaunch the label as a shirt-centric brand. Resonance, founded by Lawrence Lenihan, also has invested in Gaby Basora's Tucker label, Norisol Ferrari, Tommy John men's underwear, Lolly Wolly Doodle children's wear and Body Labs' three-dimensional body mapping.

For every signed contract there seem to be several failed hook ups or lingering romances that just haven't been consummated.

Alexander Wang was said to be in talks with General Atlantic, which has a stake in Tory Burch, but those discussions fell through. Prabal Gurung was also said to be looking for an investor, while Thom Browne's Japanese backer wanted to offload its stake. None of these deals has come to fruition as of yet.

Gary Wassner, ceo of industry factor Hilldun and chairman of fashion investor InterLuxe, said the market has been "very active," with "lots and lots of brands for sale, from small to medium large. Everybody seems to have a banker and everything's in process. There's a lot out there. It's reflective of the changes in the industry."

But designers still have to reach a certain scale before bringing in big time money.

Wassner said a brand needs to build its volume to $10 million or above with "blood, sweat and tears" until its "proof of concept" can be measured. Then a partner can come in and provide capital but, more importantly, the know-how needed to expand on the brand's core. "It's not necessarily the case that it's just the money any longer," he said. "Money isn't the answer."

Counter-intuitively, it can also be harder to invest in a smaller company.

Douglas Hand, an attorney at Hand Baldachin Amburgey who specializes in fashion, said professional fees to close the deal can eat up a meaningful amount of the capital.

"The transaction costs can make it difficult to put $1 million in," Hand said. "It's a challenging space, but there are more groups looking to do it. We are seeing more deal activity at the lower end of the spectrum in terms of valuations and I think that's a function of more institutional groups forming investment metrics around small companies."

Small is a relative term, of course, but there are certainly more investors today who are ready to contemplate stakes in brands that have sales in the neighborhood of $15 million, or even smaller for a brand that's really hot or has an interesting technological angle.

The good news for designers is that there are plenty of investors in the wings (and sometimes the front row).

David Pascual and Wall Street veteran Faye Landes recently founded Back to the Future Ventures with an eye toward making three or four consumer deals a year, with investments ranging from $1 million to $15 million. Glen Senk continues to pound the pavement looking for deals for his Front Row Partners, a partnership with Berkshire Partners formed in 2014.

Not everyone's in a buying mood, though. François-Henri Pinault, chairman and ceo of Kering, said last week in laying out his strategy for the parent of brands such as Gucci, Bottega Veneta and Saint Laurent that future acquisitions remain on hold while investments in the company's current portfolio will be conditional on the brands' free cash flow and same-store sales. "The growth of the market in the short-term will often be less rapid than at the beginning of the decade," he said. "We are present today in the most important cities and locations in the world. Our priority is to extract more value from them. We will do this in particular by continuing to increase our same-store sales and this will have a direct impact on the growth of our margins."

Ultimately, investors might be willing to wait and see how the fashion market plays out and what new opportunities present themselves.

"All of the contemporary brands have had some difficulty over the past three to six months; everybody's looking for a bailout of some kind," said Jesse Cole, president at Design & Industry, which helps brands find licensing and other deals. Cole would know as former ceo of Haute Hippie, the promising contemporary brand that was sold to Hilco a few months after he left the firm in June.

"There's plenty of money in the private equity world, but those investors realize it's a buyer's market. There are more people out there who are in trouble than they're willing to admit to," he continued. "Everybody's looking for growth capital and it's available, but not on the brand's terms, more on the investor's terms. And that's going to create some kind of stand off."