

Case 2: Ann Taylor: *Survival in Specialty Retail*

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- 1 In the summer of 2008, headlines announced that the declining economy was generating a “wave of retail closures” among many well-known companies, including Home Depot, Pier 1 Imports, Zales, Gap, Talbots, Lane Bryant, and Ann Taylor. The Chief Executive of J.C. Penney’s called the 2008 situation “the most unpredictable environment in his 39-year retail career”.¹ One industry group forecasted that nearly 6,000 retail stores would close in 2008, a 25 percent increase from the previous year. A representative from the National Retail Federation (NRF) suggested that these businesses should “look at where they’re underperforming and how can they change their operations so that they have a little bit more power in another area, or a little bit more growth potential.”² Kay Krill, President and CEO of Ann Taylor Stores Corporation (ANN), was already considering this advice.
- 2 Krill had been appointed President of ANN in late 2004, and succeeded to President/CEO in late 2005 when J. Patrick Spainhour retired after eight years as CEO. At that time, there had been concern among commentators and customers that the Ann Taylor look was getting “stodgy”, and the question was how to “reestablish Ann Taylor as the preeminent brand for beautiful, elegant, and sophisticated occasion dressing”.³ In order to reestablish the brand, Kay Krill had acknowledged the importance of the consumer, since for Ann Taylor to succeed long term, “enough women still need to dress up for work”.⁴
- 3 Krill’s challenge was based in the ANN legacy as a women’s specialty clothing retailer. Since 1954, Ann Taylor had been the wardrobe source for busy socially upscale women, and the classic basic black dress and woman’s power suit with pearls were Ann Taylor staples. The Ann Taylor client base consisted of fashion conscious women from the ages of 25 to 55. The overall Ann Taylor concept was designed to appeal to professional women who had limited time to shop and who were attracted to Ann Taylor Stores by its total wardrobing strategy, personalized client service, efficient store layouts and continual flow of new merchandise.

Source: *The CASE Journal* 5, no. 2 (Spring 2009). TCJ 050202. This case is intended to be used as the basis for class discussion rather than to illustrate either effective or ineffective handling of a management situation. © 2009 by the authors and The CASE Association.

- 4 ANN had two divisions focused on different segments of this customer base:
 - • Ann Taylor (AT), the company’s original brand, provided sophisticated, versatile and high quality updated classics.

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- Ann Taylor LOFT (LOFT) was a concept that appealed to women with a more relaxed lifestyle and work environment and who appreciated the more casual LOFT style and compelling value. Certain clients of Ann Taylor and Ann Taylor LOFT cross-shopped both brands.
- 5 Ann Taylor Factory was the company's newest division. The merchandise in these stores was specifically designed to carry the Ann Taylor Factory label. The stores were located in outlet malls where customers expected to find these and other major label bargains.
- 6 ANN had regularly appeared in the Women's Wear Daily "Top 10" list of firms selling dresses, suits and eveningwear and the "Top 20" list of publicly traded women's specialty retailers. The listings recognized the total company, i.e., the result of the impact of all three divisions. Financial data from 2004–2008 shows the performance of LOFT compared to AT (See [Exhibit 1: AT vs. LOFT Financial Performance 2004–2008](#).)
- 7 In October of 2004, for the first time, the LOFT division outsold the flagship Ann Taylor (AT) division stores.⁵ In the second quarter of 2004 LOFT had opened its 300th store, passing the Ann Taylor division in total square footage. Since its emergence as a distinctly competitive division, LOFT had been such a success for the company that some analysts credited the division for "keeping the entire ANN corporation afloat".⁶
- 8 In the company's 2007 Annual Report Krill acknowledged the ongoing challenge: To be successful in meeting the changing needs of our clients, we must continually evolve and elevate our brands to ensure they remain compelling—from our product, to our marketing, to our in-store environment.⁷
- 9 Although Krill believed that the overall Ann Taylor brand still had its historic appeal, the question remained whether that appeal could be sustained indefinitely in such a risky and uncertain specialty retail environment where success was so dependent on the "ability to predict accurately client fashion preferences."⁸
- 10 Krill was evaluating the company and its growth prospects. Macroeconomic conditions had worsened, and the retailing environment was being threatened by slowing consumer demand. As one analyst put it, More mature female shoppers are probably more likely to be very careful how they spend their money in this economy. They are not your footloose-and-fancy-free teen shoppers. These consumers are far more likely to open their pocketbooks only if the merchandise is right (and now, probably only if the price is right, too).⁹
- 11 Within the company, Krill was contemplating how to revitalize the flagship AT store brand, and what effect that would have on the recent growth of LOFT. In addition, ANN had recently launched a beauty business as a department within the AT and LOFT stores, had expanded the high end fashion offerings in AT as a separate *Collections* line, announced the opening of LOFT Outlet stores to complement Ann Taylor Factory, and was considering a new concept store specifically targeting the "older" segment of women ages 55–64. Krill was firmly committed to long-term growth, and felt that she could pursue that growth agenda even as the economy had worsened. However, she was confronted with significant questions. For example, was her agenda too aggressive? Were the actions she had undertaken the kinds of moves needed to unleash what she believed was the firm's "significant untapped potential"?¹⁰

EXHIBIT 1: AT vs. LOFT Financial Performance 2004–2008

(Net sales in millions)

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	February 2, 2008	February 3, 2007	January 28, 2006	January 29, 2005	January 31, 2004
Total Company	\$2,396.5	\$2,343.0	\$2,073.1	\$1,853.6	\$1,587.7
Ann Taylor	866.6	912.8	873.9	854.9	867.9
Ann Taylor LOFT	1,174.4	1,146.5	991.9	826.6	588.8
Other*	355.6	283.7	207.3	172.2	131.1

*Includes Ann Taylor Factory stores and Internet business

Comparable Store Sales Percentage Increase (decrease)

Total Company	(3.3)%	2.8%	0.1%	3.6%	5.3%
Ann Taylor	(3.7)%	3.1%	0.6%	(2.7)%	3.2%
Ann Taylor LOFT	(5.4)%	1.9%	(0.3)%	12.8%	9.4%

The following table provides consolidated income statement data expressed as a percentage of net sales. All fiscal years presented contain 52 weeks, except for the fiscal year ended February 3, 2007, which contains 53 weeks:

	February 2, 2008	February 3, 2007	January 28, 2006
Net sales	100%	100%	100%
Cost of sales	47.8	46.3	49.1
Gross margin	52.2	53.7	50.9
Selling, general & admin expenses	44.4	44.1	44.6
Restructuring & asset impairment	1.3	—	—
Operating income	6.5	9.6	6.3
Interest income	0.3	0.7	0.4
Interest expense	0.1	0.1	0.1
Income before income taxes	6.7	10.2	6.6
Income tax provision	2.6	4.1	2.7
Net income	4.1%	6.1%	3.9%

% Change From Prior Period	2/2/08	2/3/07	1/28/06	1/29/05
Net Sales	2.3%	13.0%	11.8%	16.7%
Operating Income	(30.6)%	70.8%	24.8%	(38.7)%
Net Income	(32.0)%	74.6%	29.4%	(37.2)%

Source: Company financials at <http://investor.annaylor.com/>

ANN TAYLOR BACKGROUND

- **12** Ann Taylor was founded in 1954 as a wardrobe source for busy socially upscale women. Starting out in New Haven, CT, Ann Taylor founder Robert Liebeskind established a stand-alone clothing store. When Liebeskind's father, Richard Liebeskind, Sr., a designer himself, as a good luck gesture gave his son exclusive rights to one of his best selling dresses, "Ann Taylor", the company name was established. Ann Taylor was never a real person, but her persona lived on in the profile of the consumer.

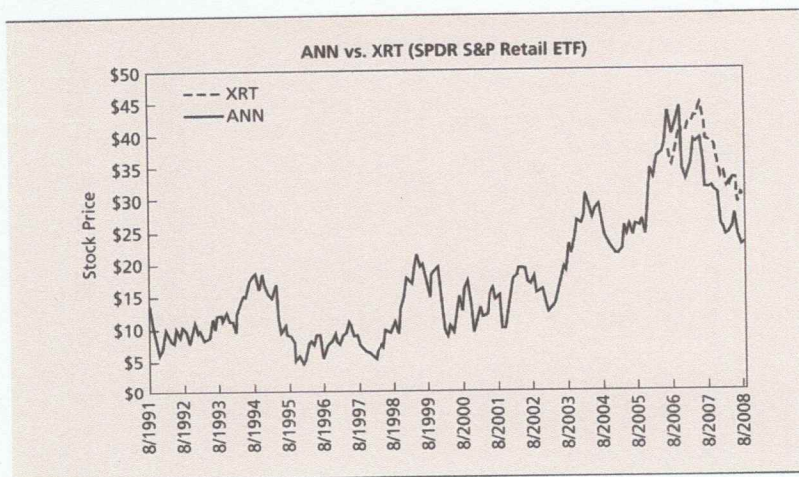
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- **13** Ann Taylor went public on the New York Stock Exchange in 1991 under the symbol ANN. In 1994 the company added a mail catalog business, a fragrance line, and free standing shoe stores positioned to supplement the Ann Taylor (AT) stores. The mail order catalog attempt ended in 1995, and the lower-priced apparel concept, Ann Taylor LOFT, was launched. LOFT was meant to appeal to a younger more casual and cost-conscious but still professional consumer. CEO Sally Kazaks incorporated more casual clothing, petite sizes, and accessories in an attempt to create a one-stop shopping environment, to “widen market appeal and fuel growth”.¹¹
- **14** Following losses in fiscal 1996 that could be attributed to a fashion misstep—cropped T-shirts didn’t fit in with the workplace attire—Kasaks left the company. New ANN CEO Patrick Spainhour, who had been Chief Financial Officer at Donna Karan and had also had previous experience at Gap, shelved the fragrance line, and closed the shoe stores in 1997.
- **15** Originally the LOFT stores were found only in outlet centers, but later expanded to other kinds of locations. In 1998 the LOFT stores in the discount outlet malls were moved to a third division, Ann Taylor Factory (Factory). The Factory carried clothes from the Ann Taylor (AT) line. The concept offered customers direct access to the AT designer items “off the rack” without elaborate promotion, and with prices regularly 25–30 percent less than at the high end Ann Taylor (AT) stores. The LOFT concept was revamped and stores were opened in more prestigious regional malls and shopping centers. By 1999 LOFT clothes were a distinct line of “more casual, yet business tailored, fun, and feminine”, and were about 30 percent less expensive than the merchandise at the flagship Ann Taylor (AT) division’s stores.¹² At that time, the LOFT was under the direction of Kay Krill, who had been promoted to the position as Executive Vice President of the LOFT division.
- **16** Ann Taylor attempted a cosmetic line in 2000, which it discontinued in 2001. In 2000, the Online Store at www.anntaylor.com was launched, only to be cut back in late 2001 when projected cash flow goals were not met. In early 2001 Spainhour restructured management reporting relationships, creating new President positions for both Ann Taylor (AT) and Ann Taylor LOFT divisions. Kay Krill was promoted from executive vice-president to president of LOFT. Spainhour commented that, Kay has been instrumental in developing the strategy for the Ann Taylor Loft concept since its inception. Her in-depth understanding of the Ann Taylor Loft client, and strong grounding in the Ann Taylor brand, combined with her proven ability in driving the development of this division, make her an ideal choice for the new President position.¹³
- **17** Kay Krill was made president of the entire ANN corporation in 2004, bringing both Ann Taylor and LOFT under her control. In February of 2005 Kay Krill announced that LOFT had reached \$1 billion dollars in sales, stating, This is an important milestone for our Company. In an intensely competitive and fragmented apparel market, Ann Taylor LOFT has been one of the industry’s most successful and fastest-growing apparel retail concepts since its launch in 1998 LOFT’s success reaffirms the importance of maintaining a strong connection with our client and evolving with her wardrobe needs over time.¹⁴
- **18** In June 2005 ANN completed a move to new headquarters in Times Square Tower in New York City.¹⁵ In the fall of 2005, Chairman and CEO J. Patrick Spainhour retired and President Kay Krill was elevated to the CEO position. In a conference call following her promotion, Krill stated her goals as “improving profitability while enhancing both brands”, “restoring performance at the Ann Taylor division and restoring the momentum at LOFT”.¹⁶

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- **19** Krill felt the outlook for fiscal year 2006 was cautiously positive, and announced continued plans for expansion and related capital expenditure. The stock responded with new highs, moving to a peak of over \$40 in late 2006. At that time, analysts were mainly supportive citing “confidence in the retailer’s strong management team, improving store products, and conservative inventory management”.¹⁷ ANN’s stock price subsequently retreated in 2007, along with the rest of the retailing sector. (See [Exhibit 2: ANN Stock Price 1992–2008](#); [Exhibit 3: Stores Operational Data](#). For full financials and operating statistics for 2004–2008, see [Exhibits 4–6](#).)
- **20** Challenges in the macroeconomic climate prompted Krill to announce a restructuring plan in 2008. In the 2007 Annual Report letter to shareholders Krill said, We understand that the economy invariably goes through cycles. We firmly believe that the manner in which we approach growth and manage our business through these cycles will differentiate us and determine our success in the market over the long term. In this regard, we have planned fiscal 2008 cautiously and realistically, focusing on three key areas—the evolution of our brands and channels, the reduction of our overall cost structure, and the continued pursuit of growth.¹⁸

EXHIBIT 2: ANN Stock Price 1992–2008



For comparison purposes, the adjusted close stock price of the Exchange Traded Fund (ETF) S&P Retail SPDR is included. This fund began trading on 6/22/2006. The top ten holdings (22.48% of total assets as of 8/2008) in this fund (in alphabetical order) consist of Aeropostale Inc., AnnTaylor Stores Corp., Brown Shoe Co., Inc., Charming Shoppes, FootLocker, Inc., Genesco Inc., Limited Brands Inc., Ross Stores Inc., Supervalu Inc., and Tiffany & Co.

Derived from: <http://finance.yahoo.com/q/bc?s=ANN&t=my&l=on&z=l&q=l&c=>

EXHIBIT 3: Stores Operational Data

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	FY2007	FY2006	FY2005	FY2004	FY2003
Employees, Total	18,400	17,700	16,900	14,900	13,000
Inventory Turns*	4.7	5.0	4.7	4.5	4.1
Net Sales/sq ft	\$ 457	\$ 474	\$ 461	\$ 471	\$ 456
Net Sales (Revenue)/ Employee	\$130,603	\$130,227	\$123,008	\$124,743	\$122,467
Average sq ft/Store					
Ann Taylor	5,300				
Ann Taylor LOFT	5,700				
Ann Taylor Factory	6,700				

*Inventory turns can be calculated differently, depending on whether yearly average or year end inventory values are used. These numbers are from ANN's 10K filing.

Specific Store Detail

Fiscal Year	Total Stores Open at Beginning of Fiscal Year	No. Stores Opened During Fiscal Year			No. Stores Closed During Fiscal Year	No. Stores Open at End of Fiscal Year				No. Stores Expanded During Fiscal Year
		ATS	ATL	ATF		ATS	ATL	ATF	Total	
2003	584	8	61	1	6	354	268	26	648	8
2004	648	10	77	8	5	359	343	36	738	6
2005	738	9	73	15	11	357	416	51	824	12
2006	824	11	52	7	25	348	464	57	869	16
2007	869	14	52	11	17	349	512	68	929	14

Source: Company Reports at <http://investor.annaylor.com>

EXHIBIT 4: Income Statements

AnnTaylor Stores Corp. Annual Income Statement (In Millions of US\$)					
	Jan08	Jan07	Jan06	Jan05	Jan04
Sales	2,396.510	2,342.907	2,073.146	1,853.583	1,587.708
Cost of Goods Sold	1,028.442	980.007	923.336	827.378	669.638
Gross Profit	1,368.068	1,362.900	1,149.810	1,026.205	918.070
Selling, General, & Administrative Expense	1,063.623	1,033.173	908.966	842.590	694.590
Depreciation, Depletion & Amortization	116.804	105.890	93.786	78.657	51.825
Operating Profit	187.641	223.837	147.058	104.958	171.655
Interest Expense	2.172	2.230	2.083	3.641	6.665
Non-Operating Income/Expense	7.826	17.174	9.318	5.037	3.298
Special Items	(32.255)	0.000	(16.032)	0.000	0.000
Pretax Income	161.040	238.781	138.261	106.354	168.288
Total Income Taxes	63.805	95.799	56.389	43.078	67.346
Net Income	97.235	142.982	81.872	63.276	100.942

Source: Standard & Poor's.

THE APPAREL RETAIL INDUSTRY

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- **21 History** Prior to the development of a retailing industry, the only option for upper-class wealthy women who desired to be fashionable was to hire local dressmakers to create one-of-a-kind personalized garments. Women with more limited resources had few options until the 1800s. Enterprising seamstresses began mass-producing dresses at that time, utilizing the increased availability of textiles and the invention of the sewing machine. The increasing availability of diverse products led to the creation of the variety store, the precursor of the current department store. At the same time, entrepreneurial seamstresses previously working as personalized dressmakers began to open specialty stores for fashionable women's clothing. Thus came the origins of modern retailing, with both department stores and specialty retailers co-existing in many downtown locations.

EXHIBIT 5: Balance Sheets

AnnTaylor Stores Corp. Annual Balance Sheet (In Millions of US\$)					
ASSETS	Jan08	Jan07	Jan06	Jan05	Jan04
Cash and Equivalents	134.025	360.560	380.654	62.412	337.087
Short-Term Investments	9.110	0.000	0.000	192.400	0.000
Total Receivables	16.944	16.489	17.091	12.573	12.476
Inventories	250.697	233.606	204.503	229.218	172.058
Current Assets—Other	97.115	79.950	73.964	90.711	55.747
Total Current Assets	507.891	690.605	676.212	587.314	577.368
Gross Plant, Property & Equipment	1,148.003	1,105.240	995.897	853.770	542.449
Accumulated Depreciation	586.733	541.132	483.132	419.442	276.880
Net Plant, Property & Equipment	561.270	564.108	512.765	434.328	265.569
Intangibles	286.579	286.579	286.579	286.579	286.579
Deferred Charges	0.288	0.652	1.017	1.382	4.886
Other Assets	37.727	26.559	16.333	17.735	17.471
TOTAL ASSETS	1,393.755	1,568.503	1,492.906	1,327.338	1,151.873
LIABILITIES					
Accounts Payable	125.388	106.519	97.398	88.340	52.170
Accrued Expenses	132.924	139.910	114.272	116.514	77.330
Other Current Liabilities	54.564	52.989	45.916	38.892	32.120
Total Current Liabilities	312.876	299.418	257.586	243.746	161.620
Long Term Debt	0.000	0.000	0.000	0.000	125.152
Deferred Taxes	1.960	—	—	—	—
Other Liabilities	239.435	219.174	200.838	156.848	34.465
TOTAL LIABILITIES	554.271	518.592	458.424	400.594	321.237
EQUITY					
Total Preferred Stock	0.000	0.000	0.000	0.000	0.000
Common Stock	0.550	0.559	0.558	0.545	0.336
Capital Surplus	781.048	753.030	711.224	657.382	510.676
Retained Earnings	762.948	664.934	527.325	445.410	393.926
Less: Treasury Stock	705.072	368.612	204.625	176.593	74.302
Common Equity	839.484	1,049.911	1,034.482	926.744	830.636
TOTAL EQUITY	839.484	1,049.911	1,034.482	926.744	830.636
TOTAL LIAB & COMMON EQUITY	1,393.755	1,568.503	1,492.906	1,327.338	1,151.873
Common Shares Outstanding	60.880	69.373	72.491	70.632	68.067

Source: Standard & Poor's.

EXHIBIT 6: Statement of Annual Cash Flows

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AnnTaylor Stores Corp. Annual Statement of Cash Flows (In Millions of US\$)					
INDIRECT OPERATING ACTIVITIES	Jan08	Jan07	Jan06	Jan05	Jan04
Net Income	97.235	142.982	81.872	63.276	100.942
Depreciation and Amortization	116.804	105.890	93.786	78.657	51.825
Deferred Taxes	(9.361)	(10.809)	(15.421)	(5.022)	3.771
Funds from Operations—Other	58.850	41.290	28.022	23.163	13.133
Receivables—Decrease (Increase)	(0.455)	0.602	(5.024)	0.056	(1.909)
Inventory—Decrease (Increase)	(17.091)	(29.103)	24.715	(57.159)	10.926
Accounts Payable and Accrued Liabilities—Inc (Dec)	0.550	37.580	28.185	62.196	12.725
Other Assets and Liabilities—Net Change	10.665	7.499	75.188	4.092	(1.795)
Operating Activities—Net Cash Flow	257.197	295.931	311.323	169.259	189.618
INVESTING ACTIVITIES					
Short-Term Investments—Change	(16.422)	0.000	192.400	117.975	0.000
Capital Expenditures	139.998	165.926	187.613	152.483	71.364
Investing Activities—Net Cash Flow	(156.420)	(165.926)	4.787	(34.508)	(71.364)
FINANCING ACTIVITIES					
Sale of Common and Preferred Stock	17.935	30.038	50.285	22.822	20.329
Purchase of Common and Preferred Stock	(347.575)	(185.129)	(48.153)	(121.698)	(12.781)
Excess Tax Benefit from Stock Options	2.328	4.992	0.000	—	—
Financing Activities—Other	0.000	0.000	0.000	(0.022)	(1.536)
Financing Activities—Net Cash Flow	(327.312)	(150.099)	2.132	(98.898)	6.012
Cash and Equivalents—Change	(226.535)	(20.094)	318.242	35.853	124.266
Interest Paid—Net	1.723	1.769	1.293	1.770	2.202
Income Taxes Paid	77.355	94.723	47.030	58.226	56.147

Source: Standard & Poor's.

- **22** The movement of the U.S. population into the suburbs, along with an increasing use of automobiles, led to the development in the 1930s and 1940s of planned shopping centers and highway strips of unified shopping stores. This expansion included the first free-standing stores with on-site parking, as run by Sears Roebuck & Co. The shopping mall concept expanded further in the 1950s. Usually “anchored” by either supermarkets or department stores, these shopping centers also allowed specialty and department retailers to co-exist in the same physical location.
- **23** By the 1980s, there were 16,000 retail shopping centers in the U.S.¹⁹ However, as customers showed their increased interest in more convenient and quicker service, alternatives to traditional ‘brick and mortar’ shopping centers appeared. They included non-store direct mail order, infomercial and shopping channel TV venues, and online options. Many retailers also made a strategic decision to create specialty clothing departments and focus on items such as sports wear, or appeal to specific niches such as either large-sized or petite women.²⁰ In addition, response to the threat of discounter department stores like Target and Wal-Mart prompted some established specialty firms to create separate divisions focused on lower priced fashions.²¹
- **24 Industry Sectors** Practically speaking, industry watchers tended to recognize three separate categories of clothing retailers. Industry publications such as the Daily News Record (DNR—reporting on men’s fashions news and business strategies), Women’s Wear Daily (WWD—reporting on women’s fashions and apparel business), and industry associations such as the National Retail Federation (NRF) reported data within the clothing sector broken out by:

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- • Discount mass merchandisers like Target, Wal-Mart, TJX (TJ Maxx, Marshall's, A.J. Wright, Bob's Stores), and Costco.
- • Multitier department stores (those offering a large variety of goods, including clothing, like Macy's and J.C. Penney's, and the more luxury-goods focused stores like Nordstrom's and Neiman Marcus).
- • Specialty store chains (those catering to a certain type of customer or type of goods, e.g. Abercrombie & Fitch for casual apparel).
- **25** More specifically in the case of specialty retail, many broadly recognized primary categories existed such as women's, men's, and children's clothing stores (e.g., Victoria's Secret for women's undergarments²², Men's Wearhouse for men's suits, Abercrombie Kids for children aged 7–14²³). Women's specialty stores were “establishments primarily engaged in retailing a specialized line of women's, juniors' and misses' clothing.”²⁴
- **26** A unique form of organization that sometimes appeared as competition in the specialty retail category was the clothing designer. Originally an evolution of the custom seamstress, for one-of-a-kind garments, fashion design houses such as Liz Claiborne and Ralph Lauren could also produce their creations in bulk, as ready-to-wear clothing. These firms were generally considered apparel wholesalers, with their items normally for sale to the clothing retailers, such as Macy's, but well-established designers could also build their own specialty stores to sell directly to the consumer.

SPECIALTY RETAILER GROWTH: BRANDING CHALLENGES

- **27** Unlike department stores that sold many different types of products for many types of customers, specialty retailers focused on one type of product item, and offered many varieties of that item. However, this single product focus increased risk, as lost sales in one area could not be recouped by a shift of interest to another entirely different product area. Therefore, many specialty retailers constantly sought out new market segments (i.e., niches) that they could serve. However, this strategy created potential problems for branding²⁵. A participant at the 2007 NRF convention commented, Brand building, acquisition, and tiering is hotter than ever in retail and consumer products—so much so they may be contributing to shorter life spans for some brands and perhaps diluting the value of all. In any event, the massive proliferation of brands in recent years—some out of thin air, others even reborn from the grave—brings with it a minefield of potential dangers.²⁶
- **28** Gap, Inc. was an example of a specialty retailer that had added several brand extensions to appeal to different customer segments. In addition to the original Gap line of casual clothing, the company offered the following: Old Navy with casual fashions at low prices, Banana Republic for more high-end casual items, and Piperlime as an online shoe store. However, in 2005 Gap had also spent \$40 million to open a chain for upscale women's clothing called Forth & Towne, which closed after only 18 months. The store was supposed to appeal to upscale women over 35—the “baby boomer” segment—but, instead, the designers seemed “too focused on reproducing youthful fashions with a more generous cut” instead of finding an “interesting, affordable way” for middle-aged women to “dress like themselves.”²⁷

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- **29** Chico's FAS, Inc. was another specialty retailer who tried brand expansions. Chico's focused on private-label, casual-to-dressy clothing to women 35 years old and up, with relaxed, figure-flattering styles constructed out of easy-care fabrics. An outgrowth of a Mexican folk art boutique, Chico's was originally a stand-alone brand. Starting in late 2003, Chico's FAS decided to promote two new brands: White House/Black Market (WH/BM), and Soma by Chico's (Soma).
- **30** Chico's WH/BM brand was based on the acquisition of an existing store chain, and focused on women 25 years old and up, offering fashion and merchandise in black and white and related shades. Soma was a newly developed brand offering intimate apparel, sleepwear and active wear. Each brand had its own storefront, mainly in shopping malls, and was augmented by both mail order catalog and Internet sales. The idea was that the loyal Chico's customer would be drawn to shop at these other concept stores, expecting the same level of quality, service, and targeted offerings that had pleased her in the past.
- **31** Although Chico's had been a solid performer during the decade, surpassing most other women's clothing retailers in sales growth, a downturn in 2006 caused Chico's shares to fall more than 50 percent when the company reported sales and earnings below analysts' expectations. Chico's had seen increasing competition for its baby boomer customers, and said it had lost momentum during 2006, partly because of "fashion missteps" and lack of sufficiently new product designs. The company's response was to create brand presidents for the three divisions to hopefully create more "excitement and differentiation."²⁸
- **32** In an attempt to better manage the proliferation of brands, many firms, similar to Chico's, created an organizational structure where brands had their own dedicated managers, with titles such as executive vice president (EVP)/general merchandise manager, chief merchandising officer, or outright "brand president."²⁹ Since each brand was supposedly unique, companies felt the person responsible for a brand's creative vision should be unique as well.
- **33** An alternative to brand extension was the divestiture of brands. In 1988 Limited Brands³⁰ acquired Abercrombie and Fitch (A&F) and rebuilt A&F to represent the "preppy" lifestyle of teenagers and college students aged 18–22. In 1996 Limited Brands spun A&F off as a separate public company. Limited Brands continued divesting brands: teenage clothing and accessories brand The Limited TOO in 1999, plus-size women's clothing brand Lane Bryant in 2001, professional women's clothing brand Lerner New York in 2002, and in 2007 the casual women's clothing brands Express and The Limited. Paring down in order to focus mostly on key brands Victoria's Secret and Bath & Body Works, the corporation had made it clear as of 2007 that it was still not done reconfiguring itself.³¹

WOMEN'S SPECIALTY RETAIL—COMPETITORS AND THE "OLDER WOMEN" SEGMENT

- **34** The National Retail Federation, a Washington, D.C.-based trade group, reported that the retail niches showing the greatest growth in 2006 were department stores, stores catering to the teenage children of baby boomers, and those apparel chains aimed at women over 35.³² The four major women's specialty retailers who were trying to target older upscale shoppers were Ann Taylor, Chicos FAS, Coldwater Creek and Talbots. Ann Taylor was the only one of these with a significant brand extension for the younger professional, but all four were promising a shopping

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environment and merchandise clearly focused on women over 35. (See [Exhibit 7](#): Selected Retail Performers.)

- **35** Talbot's CEO Trudy Sullivan noted, Nobody is clearly winning in the 35+ consumer space right now ... we need to absolutely wow her with this irresistible product and none of us have done that.³³

EXHIBIT 7: Selected Retail Performers, end of 2007

Company/ Ticker Symbol	2007 Revenue (millions)	Comparable Stores Sales Increase (Decrease)		# of Stores	Locations Served	Merchandise Market Served	Comments
		2006	2005				
Ann Taylor/ ANN	\$ 2,396.5	(3.3%)	2.8%	929	46 states plus Puerto Rico	Specialty Women's—private label "total ward- robing strategy" to achieve the "AnnTaylor look" in suits, separates, footwear & accessories	Brands are Ann Taylor for updated professional classics, Ann Taylor LOFT for lower priced more casual wear, AnnTaylor Factory for outlet priced garments developed specifi- cally for this market
Talbots/ TLB	\$ 2,289.3	(5.7%)*	1.3%*	1,421	47 states plus Canada, United Kingdom	Specialty—women's apparel, shoes, accessories via store, catalog, Internet	Brands are Talbots, modern classics for women; Jill for casual women. Brands target high income, college educated profes- sionals 35 years old & up. Talbots Kids, Talbots Mens were closed in 2007.
Chico's FAS/ CHS	\$ 1,714.3	(8.1%)	2.1%	1,070	47 states plus U.S. Virgin Islands & Puerto Rico	Specialty Women's—Privately branded clothing, intimate garments & gifts for fashion- conscious women with moderate-high income	Brands are Chico's for women 35+, White House/Black Market for women 25+, Soma intimates
Coldwater Creek, Inc./ CWTR	\$ 1,151.5	(7.9%) averages	8.5%	336	48 states	Specialty Women's— apparel, acces- sories, jewelry, gifts via instore, catalog, Internet, also Spa locations	Offers Coldwater Creek brand of cosmetics, personal care products to women over 35 with incomes in excess of \$75K. Socially responsible.

* Does not include J. Jill Data Source: 10K filings, plus data from "Top 100 Retailers", *Stores: A magazine of the NRF*, July 2008, downloadable by link at http://www.nrf.com/modules.php?name=News&op=view&view_id=543

Selected Retail Performers, 2008 Financial Data

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Company Name	Total Revenue*	Net Income*	Inventory Turnover	Revenue \$ per Employee
Abercrombie & Fitch Co.	\$ 3,749.8	\$475.7	9.89	\$ 37,981
AnnTaylor Stores Corp.	\$ 2,396.5	\$ 97.3	9.92	\$ 130,603
Charming Shoppes, Inc.	\$ 3,010.0	(\$ 83.4)	7.35	\$ 99,941
Chico's FAS Inc.	\$ 1,714.3	\$ 88.9	13.48	\$ 120,212
Coldwater Creek Inc.	\$ 1,151.5	(\$ 2.5)	8.65	\$ 87,665
Limited Brands Inc.	\$10,134.0	\$718.0	6.73	\$ 57,869
Talbots, Inc.	\$ 2,289.3	(\$188.8)	6.73	\$ 138,288
The Gap, Inc.	\$15,763.0	\$833.0	9.38	\$ 105,375

Company Name	Selling Gen & Admin % Tot Rev	Gross Margin %	Operating Margin %	Net Profit Margin %
Abercrombie & Fitch Co.	47.54	66.97	19.75	12.69
AnnTaylor Stores Corp.	44.38	52.21	6.48	4.06
Charming Shoppes, Inc.	25.83	26.95	-2.62	-2.77
Chico's FAS Inc.	49.44	56.53	7.08	5.18
Coldwater Creek Inc.	40.02	39.1	-0.93	-0.22
Limited Brands Inc.	26.27	34.95	10.95	7.09
Talbots, Inc.	33.1	32.12	-8.14	-8.25
The Gap, Inc.	N/A	36.11	8.34	5.28

Data from Mergent Online, as of 2008. *dollars in millions

- **36** This group of women, born between 1946 and 1964, was part of the “baby boomer” demographic, and the purchasing power of these women had not gone unnoticed.³⁴ Accounting for nearly half of the \$102.7 billion in women’s clothing purchases in 2007, these women were very diverse, ranging from “traditional types who prefer flat shoes and ankle-length skirts to women who resemble characters from *Desperate Housewives*.”³⁵
- **37** To respond to this diversity in the marketplace, woman’s specialty retailer Talbot’s Inc. acquired catalog and mail order company J.Jill Group in 2006. J.Jill was a woman’s clothing specialty retailer offering quality casual fashion through multi-channel mail order, Internet, and in-store venues. J.Jill targeted women ages 35–55, while Talbot’s focused on the 45–65 age group. The acquisition positioned Talbot’s as “the leading apparel retailer for the highly coveted age 35+ female population,” and allowed the company to “protect the distinct identity of each brand, while maximizing the synergies” in its business model.³⁶
- **38** Coldwater Creek, with its large jewelry, accessory, and gift assortment in addition to apparel, targeted women over 35 with incomes in excess of \$75K by appealing with a Northwest/Southwest lifestyle approach that included a group of Spa locations. Coldwater’s customer was not considered “trendy” by any means: “She’s never going to be a fashion leader ... but she wants to look modern.”³⁷ Coldwater Creek created a common brand identity for its three distribution channels: catalog, Internet, and in-store shopping. This distinct brand image yielded the best shareholder return in the group (Coldwater Creek, Chico’s FAS, Ann Taylor, and Talbot’s) since 2002, with a 33.8% revenue growth in fiscal year 2006.³⁸
- **39** Chico’s FAS was one of the first to introduce the concept of apparel designed for the lifestyle of dynamic mature women who were at the higher age end of the boomer demographic.³⁹ Chico’s, along with Coldwater Creek, was one of the recipients of the 50+Fabulous Company award in 2007, an award that promoted positive images of women who were in their 50’s or older. The founder of 50+Fabulous had established this award to promote “the value of 50+ women in the workplace and beyond”, noting, “companies have been slow to recognize the vast potential” of this demographic.⁴⁰

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- **40** In August of 2007 Kay Krill announced ANN would be creating a new chain of stores expected to launch sometime in 2008 or 2009, targeting this “older women” segment, stating, “While there are a number of companies that currently play in the broader boomer market, we believe that this particular segment has been the most significantly underserved and a huge opportunity for us.”⁴¹
- **41** Some analysts wondered about this move into an overlooked but risky market that “has tripped up several competitors like Gap.” They pointed out that although ANN’s clothes were expected to be more fashionable, the company still faced stiff competition, made even tougher given the uneven performance of AT and LOFT.⁴² In 2008, as a result of the overall economic conditions, Krill announced that this new concept offering would have to be delayed at least until 2009.⁴³

ANN OPERATIONAL INFORMATION⁴⁴

- **42** At the end of fiscal year 2007, ANN had 929 stores in 46 states, the District of Columbia and Puerto Rico, with flagship locations in New York, San Francisco, and Chicago. (See [Exhibit 3: Stores Operational Data](#) for specifics.) The company had also had an online presence since 2000, and transacted sales at www.annaylor.com and www.annaylorLOFT.com. This “very profitable” Internet channel was considered “a meaningful and effective marketing vehicle for both brands”, representing 10 percent of AT sales, less than that for LOFT, and was a way for ANN to reach out to the international market.⁴⁵
- **43** Substantially all merchandise offered in ANN’s stores was exclusively developed for the company by its in-house product design and development teams. ANN sourced merchandise from approximately 231 manufacturers and vendors, none of whom accounted for more than 4 percent of the company’s merchandise purchases in Fiscal 2007. Merchandise was manufactured in over 15 countries, including China, the Philippines, Indonesia, Hong Kong and Thailand.
- **44** ANN’s planning departments analyzed each store’s size, location, demographics, sales, and inventory history to determine the quantity of merchandise to be purchased for and then allocated to the stores. The company used a centralized distribution system with a single warehouse in Louisville, Kentucky. At the store level, merchandise was typically sold at its original marked price for several weeks. After that, markdowns were used if inventory did not sell. Store planners recognized that the lack of inventory turnover could have been because of poor merchandise design, seasonal adaptation or changes in client preference, or that the original price points had been set incorrectly.
- **45** Recent ANN initiatives had focused on improving supply chain speed, flexibility and efficiency. Reduced floor inventory levels combined with the use of new “quick-sourcing” software were meant to help create quicker inventory turns. Faster turns would lead to continual updating of floor merchandise and a greater emphasis on “full-price selling”.⁴⁶ As a result, ANN was hoping to see fewer markdowns and higher margins. The new “quick-sourcing” software was just one example of continued efforts to improve the company’s information systems.
- **46** ANN had initiated a real estate reinvestment program focused on enhancing the look and feel of 43 stores in 2005, in a move toward the “store of the future”.⁴⁷ In addition, the firm had begun a real estate expansion program designed to reach new clients either by opening new stores,

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relocating stores, or expanding the size of existing stores. Store locations were determined on the basis of various factors including

- • Geographic location
- • Demographic studies
- • Anchor tenants in a mall location
- • Other specialty stores in a mall or specialty center location or in the vicinity of a village location
- • The proximity to professional offices in a downtown or village location
- **47** Two potential concerns were emerging for ANN as a result of its recent investments in store expansion and remodeling. First, the increasing sales volume threatened to put stress on the company's internal distribution system. The distribution center in Louisville had been investing in incremental improvements through automation and software integration. However the distribution center had only sufficient capacity to supply 1,050 stores. After that, ANN's logistical experts cautioned that the building footprint would have to be expanded.⁴⁸
- **48** A second concern was whether projected earnings, given economic weakness, would actually be able to cover the projected long-term lease obligations that were being added. One analyst had warned, Store expansion is a risk for all apparel retailers. Gap Inc., for example, spent massively to add stores in the 1990s and ... the stores became a big cost overhead once Gap's clothes stopped selling well.⁴⁹

ANN TAYLOR'S BRAND IDENTITY

- **49** When ANN went public in 1991, the Ann Taylor brand, with its historically loyal following, was a candidate for brand extension. At one point in its history, the company had five separate store concepts: Ann Taylor (AT), Ann Taylor's Studio Shoes, Ann Taylor LOFT, Ann Taylor Petites (clothing for women 5'4" and under), and Ann Taylor Factory. In addition, ANN's management had experimented with a make-up line and children's clothes. By 2005, the company had closed the shoe stores, reduced the accessories inventory that stores carried, and eliminated the make-up line. However, ANN was still offering petites, as a separate section in the AT and LOFT stores, and experimenting with children's clothes and sleepwear through the LOFT division. A separate maternity section in selected LOFT stores was also undergoing a trial period.
- **50** Since 1999 analysts had warned that ANN needed to be wary of cannibalization within the brands. The analysts speculated that customers might turn away from Ann Taylor (AT) in order to buy at LOFT. ANN had always tried to respond to the customer with "wardrobing", a philosophy of "outfitting from head to toe", combining relaxed everyday wear with more dressy pieces.⁵⁰ Since LOFT sold more relaxed but still tailored items at a lower price than AT, it was possible that some of AT's customers shopped at LOFT for things that they previously would have bought at AT.
- **51** The industry was used to brand extensions such as Gap's Old Navy chain. In contrast to Gap, LOFT used "Ann Taylor" in its name, reinforcing the perception of customers that they could get the same brand for less. As one analyst put it, It's not clear that the Ann Taylor customer will continue paying \$88 for a silk cardigan sweater when she knows she can pick up a similar cardigan for \$39 ... a few blocks away at LOFT.⁵¹

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- **52** As new CEO in the fall of 2005, one of Krill's first actions was to recruit Laura Weil to a new position as Corporate Operations Officer (COO). Weil came from American Eagle Outfitters where she had focused on financial issues involving real estate, pricing, sourcing, and logistics. In addition, Weil handled the divestiture of underperforming assets. In her role as COO at ANN she would be expected to "focus on inventory management and merchandise planning, information systems and supply chain operations".⁵²
- **53** The appointment of Weil and four other staff changes reconfigured ANN's top management structure. Krill created three positions that reported directly to her—COO, Executive Vice President (EVP) of planning and allocation, and EVP/chief marketing officer. The three additional positions provided specific expertise while still allowing Krill to "lead both divisions [AT & LOFT] in a more hands-on-way". Krill then focused on merchandising and marketing, especially brand differentiation.⁵³ AT and LOFT continued to have separate EVP's for merchandising and design, and Senior Vice Presidents for divisional marketing, design, sourcing and store direction.
- **54** Krill had asked her staff to spend time with ANN customers and develop "brand books" or profiles of the typical Ann Taylor (AT) and LOFT clients.⁵⁴ The "Ann" (AT) marketing profile was of a married 36 year-old working mother with two children and a household income of \$150K. She would lead a busy, sophisticated life. When giving a presentation to a client, she'd wear a formal suit with a blouse, not a camisole, underneath, and her idea of dressing down at work might be a velvet jacket with jeans.
- **55** In contrast, the typical LOFT client was married, in her 30's with children, worked in a laid-back less corporate environment, and had a household income between \$75K and \$100K. She would call her style "casual chic" and might wear pants and a floral top with ruffled sleeves to work, while on the weekend she would wear a printed shoulder-baring halter top with cropped jeans. Krill had always felt that both AT and LOFT were recognizably different from one another. In 2005, Krill stated that there was "a pretty clear differentiation", with "special occasion and work primarily being the focus" at AT, and "more relaxed, separates and fashion" at LOFT.⁵⁵
- **56** In support of the AT brand, the company also expanded its focus on special events with the introduction of its *Celebrations* collection. The company introduced *Celebrations* into the AT stores as a line of classic, elegant dresses and coordinating accessories for special occasion, such as weddings and engagement parties. Of particular interest to long-term ANN customers was the introduction of dye-to-match sashes and accessories for bridesmaids, with fully coordinated jewelry and shoe styles, offered in petites as well as regular sizes (petites being women shorter than 5'4" in height). The expansion of the selection in petite sizes, especially online, was seen as a "great opportunity", since some department stores had reduced their petite offerings.⁵⁶

TOP MANAGEMENT TEAM TURNOVER

- **57** As Krill was working to resolve branding issues between divisions, improve efficiencies and find ways to grow the company, she also had to deal with a variety of top management team resignations. In the spring of 2006 COO Laura Weil left abruptly after only a few months. Weil's many responsibilities at ANN included merchandise planning; information systems; all supply chain operations including sourcing, logistics and distribution; real estate; construction and

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facilities, and purchasing; as well as finance, accounting and investor relations.⁵⁷ Krill decided not to replace Weil and eliminated the position on the organizational chart. Krill assumed leadership of LOFT again, playing a dual role while searching for a new divisional president.

- **58** Krill commented, "I believe that building a winning team is critical to fully realizing our company's full potential".⁵⁸ However, it appeared that creating that "winning team" was taking longer than anticipated. One source wondered about the pressure on Krill, especially since she didn't have a "strong operating partner" to help with merchandising and other creative decisions.⁵⁹
- **59** Even though Krill had made differentiation between AT and LOFT a top priority, analysts continued to challenge Krill's efforts, noting that it had been hard to get both divisions moving forward simultaneously. As one analyst said "it just seems like it's a struggle to get both of these divisions firing on all cylinders at the same time".⁶⁰ Krill responded to the comment that consistency had been a problem: The notion that Ann Taylor got soft because I was supporting the LOFT team is really a completely inaccurate comment. As CEO of the company I have to spend my time on many things, and if one of our businesses is softening in any way I will focus extra time on it.⁶¹
- **60** In August 2007, long-time CFO James Smith and Chief Marketing Officer Elaine Boltz both resigned, and then in July 2008 long-time Chief Supply Chain Officer Anthony Romano also left to "pursue other interests".⁶² Although she had hired a new CFO and Chief Marketing Officer in late 2007, these departures left Krill once again without a lot of depth at the top.⁶³ However, Krill had had experience with management turnover as she had had to deal with seven resignations, seven new hires, and two promotions in her upper management team over two years' time. As of the end of 2008 she had finally filled the AT and LOFT Divisional President positions. (See [Exhibit 8](#): Summary of Personnel Changes at ANN.)

FUTURE PLANS AND INITIATIVES

- **61** As part of a multi-year restructuring program begun in 2008, ANN was focused on reducing excess costs, and planned to do so by closing underperforming stores, downsizing ANN's corporate and divisional staff by eliminating approximately 260 positions, reducing executive compensation bonus payout as a result of higher performance goals, and consolidating "all purchasing activities under a centralized strategic procurement organization to leverage scale".⁶⁴ The restructuring program included a suspension of the share repurchase plan and a scale back of capital spending, and was expected to result in ongoing annualized savings of approximately \$80 to \$90 million.⁶⁵ The pre-tax costs of this restructuring were forecasted to be \$65 to \$70 million over the period from 2008 to 2010, but Krill felt