(BN) Coach Droops as Kors Grabs Handbag Customers in Slowdown: R etail

+--+

Coach Droops as Kors Grabs Handbag Customers in Slowdown: Retail

2012-08-01 04:00:01.0 GMT

By Cotten Timberlake

Aug. 1 (Bloomberg) -- Coach Inc. Chief Executive Officer Lew Frankfort has beaten Wall Street sales estimates in 85 percent of all quarters for the past five years, through good times and bad.

Not yesterday, when Coach reported North American comparable sales that missed analysts' predictions as well as its own projection. Concerned about Coach's ability to hold on to its market share, investors pushed the stock down the most in almost 11 years.

The largest U.S. maker of luxury leather goods is facing rising competition from companies, such as Michael Kors Holdings Ltd., piling into the lucrative handbag category that Coach has dominated for more than a decade. A slowdown in U.S. consumer spending amid weak economic growth hasn't helped. Analysts at Piper Jaffray Cos. and Jefferies Group Inc. yesterday dropped their recommendations that investors buy the shares.

"Coach needs to sustain the strength of their full-line stores and reinstate consumer interest" in their outlet stores, Matt Arnold, a Des Peres, Missouri-based analyst with Edward Jones & Co., who recommends buying the shares, said in a telephone interview. "That is not going to be easy in this environment."

Coach, based in New York, helped invent mass luxury with
$299 handbags that are affordable for middle-income consumers.
As the U.S. market pioneer, the company reaped the rewards. For the past 12 quarters, revenue has grown an average of 14 percent. Net income has risen 14 percent or more in each quarter of Coach's just-finished year.

Long-Term Growth

Frankfort, speaking to investors on a conference call yesterday, reiterated his long-term goals for the company.

The Coach team is "very confident in our long-term growth prospects and our ability to drive our business at a double- digit pace," Frankfort said.

Sales at North American stores open at least a year advanced 1.7 percent in the quarter ended June 30, compared with a gain of 10 percent a year earlier. Jennifer Davis, an analyst at Lazard Capital Markets, had projected an increase of 5 percent. Coach forecast growth of at least the same pace as the previous quarter's 6.7 percent gain.

Kors's North American comparable sales soared 37 percent in its most recent quarter.

Market share losses hurt Coach's comparable sales, Michael Binetti, a UBS AG analyst, wrote in a note to clients yesterday.

Coach fell 19 percent to $49.33 at the close in New York yesterday, for the biggest drop since Sept. 17, 2001. The shares, down 19 percent this year, had almost tripled in value from the beginning of 2009 to the end of 2011.

Handbag Sales

Frankfort's ability to beat estimates quarter after quarter through the recession and lackluster recovery was due in part to the fact that handbags are one of the luxuries women are still willing to buy. While consumers began spending less on jewelry this year, prompting New York-based Tiffany & Co. to cut its profit and sales forecasts in May, handbag sales marched on.

In recent years, women have switched their spending from clothes to handbags, which last longer, can be worn more often and don't have to fit. In 2011, Americans spent $8.5 billion on bags, according to Accessories magazine, an industry publication. Handbag sales have been growing about 10 percent a year, according to Coach. Compare that to the women's apparel market, which has been growing about 4 percent.

As a result, the fragmented fashion accessories category has attracted growth-hungry bag makers -- rivals Coach didn't need to worry about before.

Kors Competition

One is Kors. With a 9.5 percent share, the Hong Kong-based company has become a "significant threat" to Coach's 35 percent share of the U.S. handbag market, Binetti wrote in a July 23 report. If Kors meets its own current-year targets, it can gain another 3 percentage points of share, creating headwinds for Coach's revenue and earnings per share, estimated Binetti, who is based in New York and has a neutral rating on the shares.

In addition to Kors, Coach is facing competition from Tory Burch LLC, Fifth & Pacific Cos.' Kate Spade and Ralph Lauren Corp. At the same time, Americans have curbed discretionary purchases amid slow economic growth that has made joblessness stubborn. Consumer spending in the U.S. stagnated in June as incomes increased. Household purchases, which account for about 70 percent of the economy, were unchanged in June after a 0.1 percent decrease the prior month, according to a Commerce Department report yesterday.

Promotional Environment

Coach said "an increasingly promotional environment" prompted slower-than-expected growth at its factory outlets, which Frankfort said were "entirely responsible" for the sales growth deceleration. The company said it re-instituted discount coupons late in the quarter, which was helping.

Robust handbag demand will continue, Frankfort said. Still, with rivals circling, Frankfort has been building alternate sources of growth. Yesterday, he called out efforts to build up non-handbag goods in the Legacy line, which was introduced last month and recalls Coach's original designs. He mentioned outerwear, jewelry, watches and scarves.

He cited 60 percent sales growth in China, and a doubling of sales in men's goods in the year that ended June 30.

As the shares sank, he sought to assure investors: "We're driven to win."

For Related News and Information:
Coach's new products: COH US <Equity> TCNI NP <GO> Coach earnings matrix: COH US <Equity> TCNI ERN <GO> Retail and consumer headlines: RTOP <GO> Luxury links: LUXU <GO> Retail sales: RTSL <GO> Top Stories: TOP<GO>

--Editors: Robin Ajello, Cecile Daurat

To contact the reporter on this story:
Cotten Timberlake in Washington at +1-202-654-1286 or ctimberlake@bloomberg.net

To contact the editor responsible for this story:
Robin Ajello at +1-212-617-7261 or
rajello@bloomberg.net