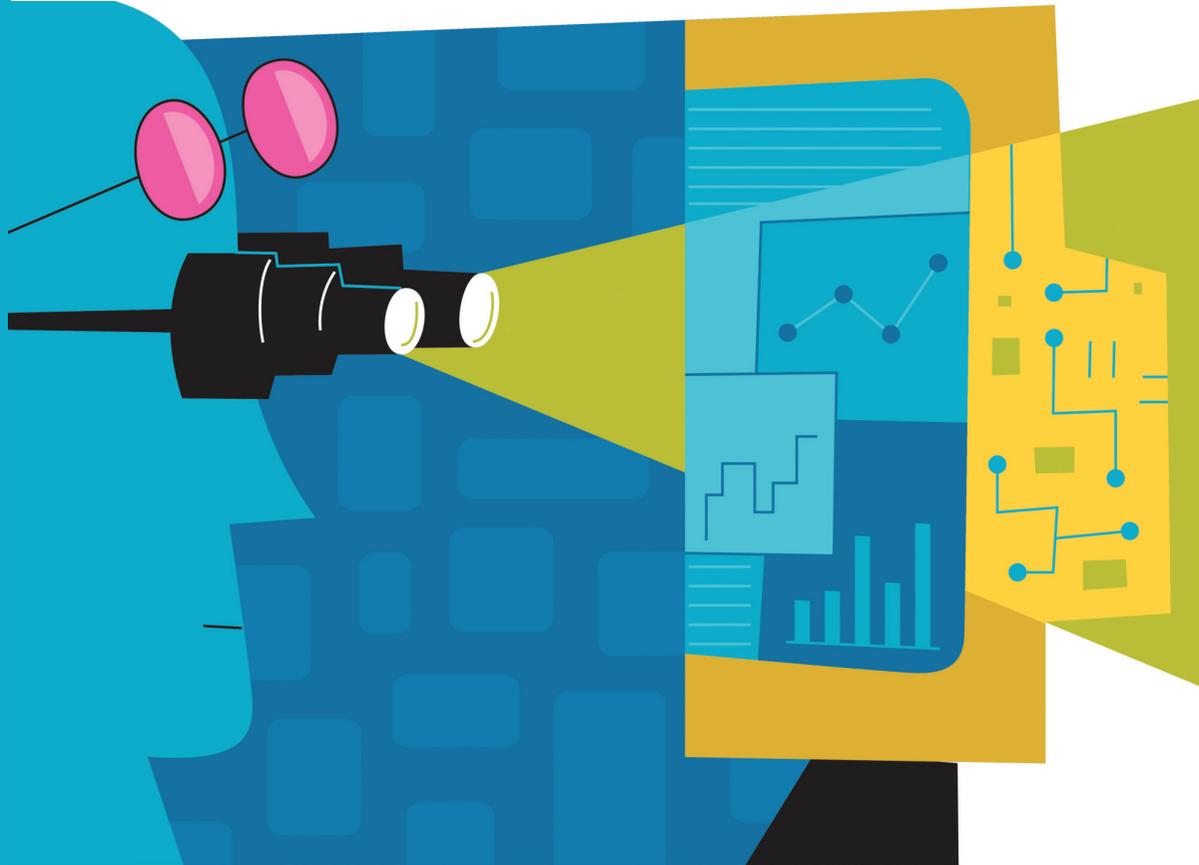


# How to Assess a Retailer's Expansion Potential from Afar



**One of the key factors** when deciding whether or not to invest in a retailer is its potential to add stores, which is typically the main engine of revenue growth.

If the company opens up sales by store as part of due diligence, a detailed multivariate regression model can be used to come up with a solid estimate of expansion potential. But if not, it's also possible to do an outside-in assessment that will yield a solid approximation, which can be used to validate management's (or analysts') forecasts or to independently develop a forecast from scratch.

Armed with such an objective perspective, private equity firms and hedge funds can better predict a retailer's future store growth and revenue and, ultimately, make a better-informed investment decision.

## Ann Taylor and LOFT

Women's apparel retailer Ann Taylor caters primarily to professional women searching for work-appropriate clothing and accessories. In 1996, in response to the by then well-established trend of less formal attire in the workplace, the company launched LOFT, which offers more casual clothing and attracts a younger clientele. Management currently believes that it can open 100 LOFT

stores in addition to its current 516 while it continues to downsize the number of original Ann Taylor locations.

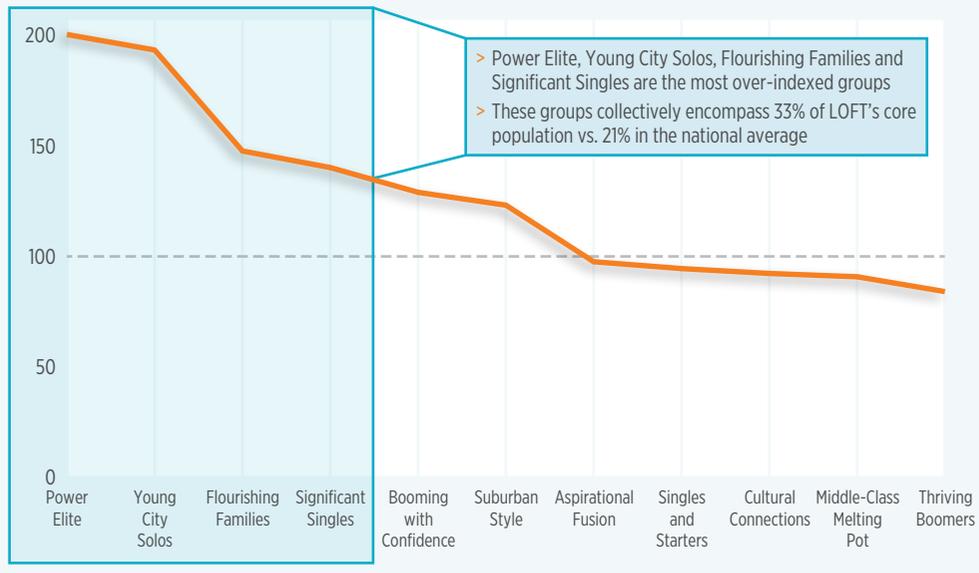
To assess management's forecast, we did the following:

1. We identified the mix of different psychographic segments within 15 minutes of each current LOFT location to find out where LOFT over-indexes. (See page 61.)

- For each segment that is overrepresented in LOFT markets, we determined the threshold-level concentration required for a “successful” store. The median level is usually a good starting point, but given the shift to e-commerce and declining traffic in almost every retail format, a more conservative approach for future projections is the 75% percentile. (See Exhibit 1.)
- We took a database of all existing retail locations (around 42,000) and screened them against the criteria established in step

- to come up with the total potential number of new location sites. (See Exhibit 2.)
- We then eliminated any sites within specified drive times of the new locations. The typical starting point is the existing median drive time between locations but, again, given changing retail patterns, a more conservative approach increases the drive time. We determined that LOFT locations, as with comparable mall-based apparel retailers that we’ve analyzed in the past, can successfully be opened within 10 minutes of each other.

**EXHIBIT 1: LOFT Psychographic Segments**  
(LOFT Distribution vs. National Distribution, within 15-Minute Drive-Time Radius)



**THE FOUR DEMOGRAPHIC GROUPS WHERE LOFT OVER-INDEXES**

**Young City Solos**—Younger and middle-aged singles living active and energetic lifestyles in metropolitan areas

**Significant Singles**—Middle-aged singles and some couples earning mid-scale incomes supporting active city lifestyles

**Flourishing Families**—Affluent, middle-aged families and couples earning prosperous incomes and living very comfortable, active lifestyles

**Singles and Starters**—Young singles starting out, and some starter families, in diverse urban communities

**EXHIBIT 2: Population in Key LOFT Psychographic Segments**  
(Index to National Average % of Population, within 15-Minute Drive-Time Radius)



5. The final step was to do a reality check by looking at competitor locations, as well as the demographics and income in the trade areas, to make sure that the psychographic segments were truly representative of more basic measures.

In the end, we determined that there are in fact approximately 175 potential locations for future LOFT stores in the United States alone.

### Hibbett Sports

Hibbett Sports, a full-line sporting goods retailer, operates mostly in the Southeast, Southwest and Midwest, primarily in small-to mid-sized markets. Currently, it has 879 stores in 29 states, a number management believes it can grow to more than 1,300, with approximately 420 new stores.

Hibbett Sports tends to open in small markets that most national and other large chains do not and features a smaller footprint (roughly 5,000 square feet vs. 55,000 for competitors' chains, on average). It offers a mix of merchandise specifically tailored to the local market, such as that of sports teams favored by its surrounding populations: primarily ethnically mixed, middle-aged couples with modest incomes and little to no college education. And just 30% of Hibbett Sports' stores have another location within 20 minutes—consistent with the

company's strategy of having just one store in each of its small markets.

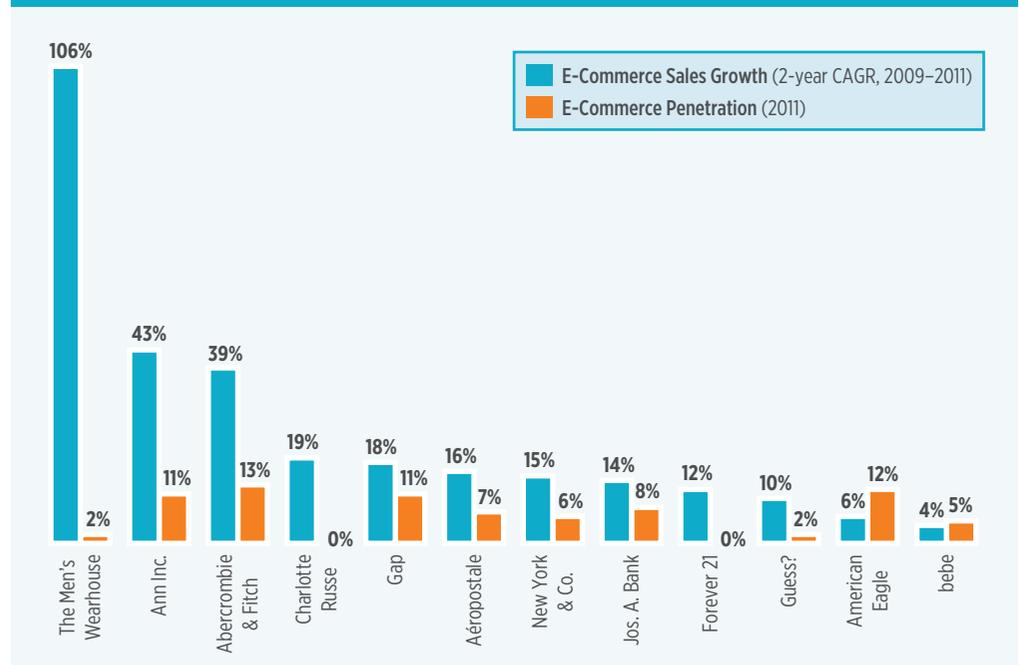
Applying the same method of analysis to Hibbett as we did to LOFT, we determined that Hibbett could open 298 stores, 122 fewer stores than the 420 management had projected.

In order to achieve the forecast of 420, the company would have to pack more stores into a smaller radius, change its existing store format or modify the economics of the business itself. Identifying which strategy management has in mind, especially as brick-and-mortar expansion is increasingly impacted by the growth in e-commerce, would be necessary in order to further evaluate the company's store growth potential.

### An arm's-length starting point

Few factors are as important to a retailer's growth as its ability to open new stores, even as e-commerce continues to rise in importance. Indeed, our formula can easily accommodate the addition of e-commerce sales and sales projections (see Exhibit 3), including those expected to cannibalize brick-and-mortar sales down the road. And further analysis can and should be conducted once inside information, such as the sales and profitability of each location, is obtained. ❖

EXHIBIT 3: E-Commerce Overview



**AUTHOR**

**Drew Klein**

Manager, Private Equity and Strategy Practice  
[drew.klein@kurtsalmon.com](mailto:drew.klein@kurtsalmon.com)