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Navigating the Dealmaking Market

PJ SOLOMON's Cathy Leonhardt and David Shiffman on the private equity retreat, recession worries and the longevity of streetwear.

By Evan Clark

PJ SOLOMON's Cathy Leonhardt and David Shiffman

Dealmaking is a tricky game even when everything's great.

But with a recession looming, retail reinventing at light speed, direct-to-consumer brands encroaching and private equity companies seeking cover, the complexity around mergers and acquisitions is only multiplying.

To get a read on the market, WWD sat down with investment bankers Cathy Leonhardt and David Shiffman — coheads of retail at PJ SOLOMON, which has a long history of wheeling and dealing in fashion and retail.

The pair has been working together for years and have an easy banter, often completing or amplifying each other's thoughts as they dissect the market.

"Dealmaking in retailing broadly has been slower this year," Leonhardt said. "To add to that, we haven't seen those billion-dollar deals that we've seen in previous years — there was always one or two."

There are some areas of strength, but they're very specific.

Shiffman pointed to off-price (TJX Cos. Inc. and Ross Stores Inc.), global sport (Nike Inc. and Lululemon Athletica Inc.) and streetwear (Supreme) as very strong categories in the market.

Streetwear is relatively new to that list and, so, still more uncertain.

"The question is, 'Is it here to stay?' Or whether it will prove to be a fad," Shiffman said, noting Supreme has real scale, but that there are dozens of smaller players looking to grow. "It's hard to pick the winners there."

And buyers today want to be pretty sure they have a winner.

Acquirers are paying close attention to the economic cycle and growing ever-more aware that the last recession ended in June 2009, more than a decade ago, where the average period between recessions since World War II is under five years.

"We are so late in this cycle, that it's now starting to sink in," Leonhardt said.

Shiffman added that both buyers and sellers are coming to the table with business plans that are acutely aware of the economy.

"Everyone takes that five-year plan and…is now factoring in some sort of recession," he said.

That kind of math is particularly important when it comes to private equity, which Shiffman said has arguably been the most important buyer of retail for decades. The private equity firms are sophisticated buyers, using both debt and equity, taking companies off the public market in leveraged buyouts and returning them with initial public offerings.

"Not only have you not seen any big deals, you haven't seen the traditional LBOs," Shiffman said. "We would argue that private equity continues to exhibit that retreat" in retail and favoring other sectors, including consumer goods, health, wellness and beauty.

"There's too much uncertainty," he said. "Retail's still going through incredible transformation and disruption… if you're private equity and you don't know if you can get [an acquired company] public and you don't know if there's a strategic buyer…that leaves you with a recap.

"They're afraid of where we are in the cycle," he said. "They don't know what the exit will be and as such, they move to the sidelines."

But if recession worries are ruling the private equity pocket book, that also opens up opportunities for some particularly well-positioned companies.

Leonhardt said of the private equity crowd: "The one thing they will all consistently tell you is, we will pay a much-higher price for that business we believe can weather a recession."

While the private equity firms largely bide their time, retailers are out looking for deals that will help them transform their businesses.

"I do think you're going to see more brands and retailers acquire some of these DTC brands and it's for consumer, it's for technology, it's for capabilities," Leonhardt said. "And it may not be the end all, be all for them to solve their own business problems, but I think they have to do this. And we're aware of several that are in the making.

"It's just, you gotta get out of your own way, just like Walmart did," she said. "You really need some DNA and innovation to bring into the company. The question is, What price do you pay? In a risk-adverse environment, it comes down to dollar price point. 'I'm not paying five-times revenues, I'm paying $100 million and that's the amount I can risk in this environment.'"

That might be the key question for almost everyone: How risky is it to move forward with a deal and how risky is it to not and stay the same in an on-the-go world?