2019 Duff & Phelps Asia/EMEA/India YOUniversity Deal Challenge

November 2018

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I. Executive Summary

Executive Summary

D-zine Men's Apparel

- D-zine Men's Apparel ("DMA") engages in the sale of men's clothing and luxury products and is based in the United States.
  - DMA sells to customers throughout the U.S. and in select European and Asian markets.
  - The company offers a full line of clothing and specializes in high-end suits.
  - Revenue in 2017 was approximately $331 million and is expected to grow to $341 million in 2018. EBITDA in 2017 was approximately $48 million and is expected to grow to $53 million in 2018.
  - DMA is heavily leveraged and its financial performance has deteriorated since being acquired by a private equity firm in 2012. The company was unable to refinance its debt in recent years.
- DMA defaulted on principal payments in 2017. The debtholders have taken control of the company and have hired consultants to advise on exit scenarios that will maximize the value of their holdings.

II. Company Overview

Business Description (1/2)

- Headquartered in New York, NY.
- Founded in 1924 by George Koval, an eastern European immigrant tailor.
- Began by selling tailored suits out of a small shop in New York City.
- Expanded products over time to include a full line of men’s clothing and fashion accessories. All products are branded with the “DMA” trademark.
- Currently operates 99 stores, distributes to upscale department stores, and has meaningful online sales. The company leases all of its storefronts.
- Currently has direct sales channels in all major U.S. markets and has a small international presence, with 10 stores in Europe and Asia. DMA made attempts to expand its international presence in 2013 and 2014, but the company has since closed some of these new outlets.

Business Description (2/2)

- The DMA brand is known for being high quality and commands a premium price. DMA suits first gained widespread popularity in the 1940s when Frank Sinatra began wearing them during performances. Since then, the brand name has maintained its luxury image and is still known to be worn by celebrities and high profile executives.

- All DMA products are sourced from independent manufacturers. Most manufacturing takes place outside the U.S. DMA does not currently license its brands to third parties.

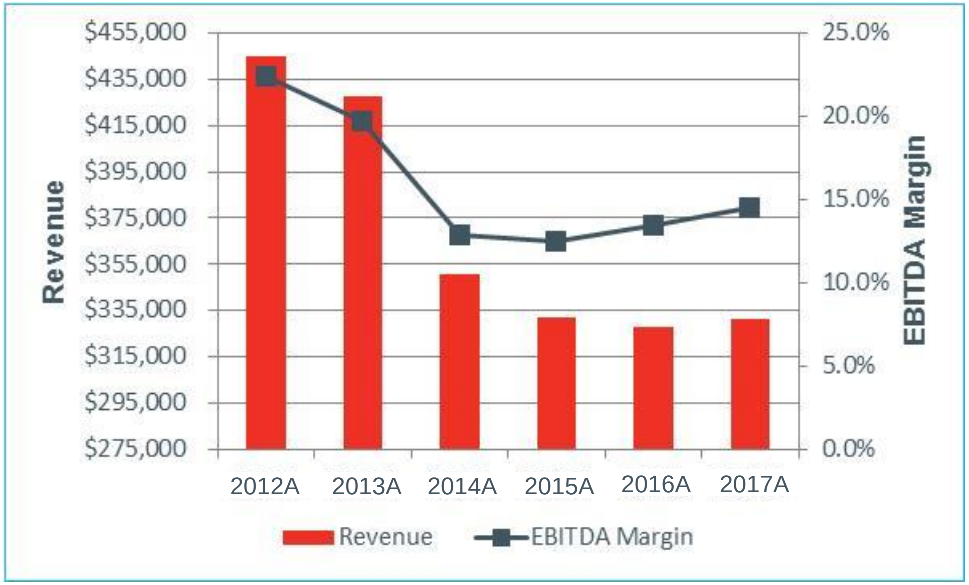
- The company's workforce includes approximately 1,000 employees and an experienced senior management team.

- In July 2012, DMA was acquired by a private equity firm for $1.1 billion. The acquisition was funded with 65% debt and 35% equity. The acquirer believed there was an opportunity to significantly expand international operations and sales.

- In 2014, DMA lost a large department store customer after disagreements about pricing and marketing strategies, which caused a significant decline in revenues.

Historical Financial Information (1/5)

Revenue ('000s) & Margin Trends



2012A – 2017A Highlights

- DMA lost a major upscale department store customer in 2014. While revenue has stabilized in recent years, results are still well below 2012 levels.
- EBITDA margin reduction in recent years is mainly the result of significant lost revenues. The company's cost cutting efforts have not kept pace with the declines in revenue.

Historical Financial Information (2/5)

Detailed Financial Results (thousands)

	2012A	2013A	2014A	2015A	2016A	2017A
Domestic Stores	$ 242,560	$ 230,917	$ 208,056	$ 200,049	$ 197,219	$ 200,137
International Stores	18,988	22,375	25,573	24,729	22,277	19,548
Company-Owned Stores	261,548	253,292	233,629	224,778	219,496	219,685
Department Stores	173,580	164,728	107,403	96,984	97,372	99,515
Online	10,075	9,803	9,597	10,106	10,793	11,862
Total Revenue	$ 445,204	$ 427,823	$ 350,629	$ 331,868	$ 327,662	$ 331,061
Costs of Goods Sold	$ 178,081	$ 173,696	$ 151,472	$ 141,044	$ 137,618	$ 138,052
SG&A	167,397	169,846	153,926	149,341	146,137	145,005
Total Expenses	$ 345,478	$ 343,542	$ 305,398	$ 290,385	$ 283,755	$ 283,057
EBITDA	$ 99,726	$ 84,281	$ 45,231	$ 41,484	$ 43,907	$ 48,004
Depreciation	11,534	11,133	9,350	8,916	8,819	8,898
EBIT	$ 88,191	$ 73,148	$ 35,882	$ 32,567	$ 35,088	$ 39,106
Capital Expenditures	$ 9,349	$ 10,696	$ 9,818	$ 6,969	$ 5,898	$ 5,628
Leverage Ratio	7.2x	8.5x	15.8x	17.2x	16.3x	14.9x
Other Metrics						
Domestic Stores	99	99	99	95	92	89
International Stores	8	11	14	14	12	10

Historical Financial Information (3/5)

Common Size (% of Revenue)

	2012A	2013A	2014A	2015A	2016A	2017A
Domestic Stores	54.5%	54.0%	59.3%	60.3%	60.2%	60.5%
International Stores	4.3%	5.2%	7.3%	7.5%	6.8%	5.9%
Company-Owned Stores	58.7%	59.2%	66.6%	67.7%	67.0%	66.4%
Department Stores	39.0%	38.5%	30.6%	29.2%	29.7%	30.1%
Online	2.3%	2.3%	2.7%	3.0%	3.3%	3.6%
Total Revenue	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%
Costs of Goods Sold	40.0%	40.6%	43.2%	42.5%	42.0%	41.7%
Sales & Marketing	37.6%	39.7%	43.9%	45.0%	44.6%	43.8%
Total Expenses	77.6%	80.3%	87.1%	87.5%	86.6%	85.5%
EBITDA	22.4%	19.7%	12.9%	12.5%	13.4%	14.5%
Depreciation	2.6%	2.6%	2.7%	2.7%	2.7%	2.7%
EBIT	19.8%	17.1%	10.2%	9.8%	10.7%	11.8%
Capital Expenditures	2.1%	2.5%	2.8%	2.1%	1.8%	1.7%

Historical Financial Information (4/5)

Growth Trends

	2012A	2013A	2014A	2015A	2016A	2017A
Domestic Stores	N/A	-4.8%	-9.9%	-3.8%	-1.4%	1.5%
International Stores	N/A	17.8%	14.3%	-3.3%	-9.9%	-12.3%
Company-Owned Stores	N/A	-3.2%	-7.8%	-3.8%	-2.3%	0.1%
Department Stores	N/A	-5.1%	-34.8%	-9.7%	0.4%	2.2%
Online	N/A	-2.7%	-2.1%	5.3%	6.8%	9.9%
Total Revenue	N/A	-3.9%	-18.0%	-5.4%	-1.3%	1.0%
Costs of Goods Sold	N/A	-2.5%	-12.8%	-6.9%	-2.4%	0.3%
Sales & Marketing	N/A	1.5%	-9.4%	-3.0%	-2.1%	-0.8%
Total Expenses	N/A	-0.6%	-11.1%	-4.9%	-2.3%	-0.2%
EBITDA	N/A	-15.5%	-46.3%	-8.3%	5.8%	9.3%
Depreciation	N/A	-3.5%	-16.0%	-4.6%	-1.1%	0.9%
EBIT	N/A	-17.1%	-50.9%	-9.2%	7.7%	11.5%
Capital Expenditures	N/A	14.4%	-8.2%	-29.0%	-15.4%	-4.6%

Historical Financial Information (5/5)

Balance Sheet as of December 31, 2017 ($ thousands)

		31-Dec-2017			31-Dec-2017
Cash & Cash Equivalents	$	36,074	Accounts Payable	$	31,155
Accounts Receivable		24,596	Accrued Expenses		34,975
Inventories		73,789	Current Portion of Debt		715,000
Other Current Assets		36,077	Other Current Liabilities		16,489
Total Current Assets		170,536	Total Current Liabilities		797,619
PP&E (net)		51,338	Long-term Debt		-
Intangibles		198,000	Other Long-term Liabilities		21,317
Goodwill		-	**Total Liabilities**		**818,936**
Other Assets		34,511			
Total Assets	**$**	**454,385**	**Equity**		**(364,551)**
			Total Liabilities and Equity	**$**	**454,385**

III. Management Plan

Management Plan Background and 2018-2021 Estimates (1/4)

- Management provided the plan on the following page for the business prior to entering bankruptcy. Management has stated that the projections assume the business continues to operate “as is.” Highlights of the plan include:
  - In 2017, DMA had its first year of positive revenue growth since the acquisition. Revenue growth in 2018 is expected to improve moderately before growth increases to industry average expectations in 2020 and 2021.
  - Gross margins are expected to improve in the next few years before leveling out in 2021.
  - As revenue growth returns, SG&A expenses are expected to increase at a slower pace than revenue. Therefore, EBITDA margins are projected to expand over the next few years before leveling out in 2021.
  - Capital expenditures are expected to continue to stay around historical levels (as a % of revenue) through 2021. No major capital spending projects are expected in the near future given that there are no plans to open new stores.

Management Plan Background and 2018-2021 Estimates (2/4)

Financial Projections

	2018E	2019E	2020E	2021E
Domestic Stores	$ 206,141	$ 214,386	$ 225,106	$ 236,361
International Stores	19,939	20,338	20,948	21,576
Company-Owned Stores	226,080	234,724	246,054	257,937
Department Stores	102,002	105,063	108,740	112,546
Online	13,048	14,353	15,788	17,367
Total Revenue	$ 341,130	$ 354,139	$ 370,581	$ 387,850
Costs of Goods Sold	$ 140,887	$ 144,843	$ 150,085	$ 155,140
Sales & Marketing	147,709	148,030	149,344	153,201
Total Expenses	$ 288,596	$ 292,873	$ 299,430	$ 308,340
EBITDA	$ 52,534	$ 61,266	$ 71,152	$ 79,509
Depreciation	9,130	9,431	9,810	10,209
EBIT	$ 43,404	$ 51,835	$ 61,341	$ 69,300
Capital Expenditures	$ 8,528	$ 9,208	$ 9,265	$ 9,696
Other Metrics				
Domestic Stores	89	89	89	89
International Stores	10	10	10	10

Management Plan Background and 2018-2021 Estimates (3/4)

Common Size

	2018E	2019E	2020E	2021E
Domestic Stores	60.4%	60.5%	60.7%	60.9%
International Stores	5.8%	5.7%	5.7%	5.6%
Company-Owned Stores	66.3%	66.3%	66.4%	66.5%
Department Stores	29.9%	29.7%	29.3%	29.0%
Online	3.8%	4.1%	4.3%	4.5%
Total Revenue	100.0%	100.0%	100.0%	100.0%
Costs of Goods Sold	41.3%	40.9%	40.5%	40.0%
Sales & Marketing	43.3%	41.8%	40.3%	39.5%
Total Expenses	84.6%	82.7%	80.8%	79.5%
EBITDA	15.4%	17.3%	19.2%	20.5%
Depreciation	2.7%	2.7%	2.6%	2.6%
EBIT	12.7%	14.6%	16.6%	17.9%
Capital Expenditures	2.5%	2.6%	2.5%	2.5%

Management Plan Background and 2018-2021 Estimates (4/4)

Growth Trends

	2018E	2019E	2020E	2021E
Domestic Stores	3.0%	4.0%	5.0%	5.0%
International Stores	2.0%	2.0%	3.0%	3.0%
Company-Owned Stores	2.9%	3.8%	4.8%	4.8%
Department Stores	2.5%	3.0%	3.5%	3.5%
Online	10.0%	10.0%	10.0%	10.0%
Total Revenue	3.0%	3.8%	4.6%	4.7%
Costs of Goods Sold	2.1%	2.8%	3.6%	3.4%
Sales & Marketing	1.9%	0.2%	0.9%	2.6%
Total Expenses	2.0%	1.5%	2.2%	3.0%
EBITDA	9.4%	16.6%	16.1%	11.7%
Depreciation	2.6%	3.3%	4.0%	4.1%
EBIT	11.0%	19.4%	18.3%	13.0%
Capital Expenditures	51.5%	8.0%	0.6%	4.7%

IV. Bankruptcy and Plan for Emergence

Bankruptcy Situation

- In July 2017, the principal on the company's debt came due. DMA was unable to refinance the debt and defaulted on its obligations.

- The company's equity holders recently proposed a plan for reemergence that was rejected by the bankruptcy court.

- The debtholders are now set to propose a plan for exit. The debtholders have no interest in running the business. Accordingly, the debtholders and Management have asked the consultants to research and assess the following two scenarios, which they believe are the best options for maximizing the value of the business:

Scenario 1: **Selling the company to a strategic buyer.**

Scenario 2: **Selling the company to a new private equity buyer that will operate the company on a standalone basis, but with a different branding and sales channel strategy.**

Scenario #1 (1/2)

- Under Scenario #1, a strategic buyer will be primarily interested in the brand. Buyers would look to maintain the integrity of the brand and employ a similar pricing strategy while merging the operations of the business with their own. Specific opportunities related to this strategy include:
  - In this scenario, buyers would have their own distribution network and would be able to rationalize DMA's distribution center in the U.S. The facility has been appraised recently at $25 million.
  - Management believes the right strategic buyer would be able to achieve approximately $20 million of annual revenue synergies by 2021 by driving additional sales through existing prestige department store and other high-end retail outlet channels.
  - Gross margins would be expected to improve to industry averages given scale and buying power improvements.
  - Additional cost savings of $10 million could be realized by a strategic buyer through management and back office headcount reductions.

Scenario #1 (2/2)

- Management has stated that 10 of its domestic stores operate at a loss. They believe these leases can be terminated through the bankruptcy for a relatively small fee. Closing these 10 stores would result in $7.5 million of lost annual revenue in aggregate, but SG&A cost savings would be approximately $8.0 million in aggregate. One time expenses associated with store closings and lease terminations would be approximately $3.0 million.

Scenario #2 (1/2)

- Under Scenario #2, a private equity buyer would pursue a different strategy in which the company would operate on a standalone basis and target new sales channels to spur revenue growth. Management believes that a strategic player is unlikely to pursue this strategy due to risk to the brand. Specific opportunities related to this strategy include:
  - Outside of its owned stores, DMA's products are currently only sold in the most upscale department stores. Management has recently explored selling a new line of clothing and accessories (under the DMA brand) at a lower price point through more mainstream department stores and retail outlets. Management believes an opportunity exists to substantially increase the company's revenue and estimates the following impacts of this strategy:
    - Revenue at company-owned stores would remain relatively similar to Management's current plan.
    - Revenue from the new channels would be expected to increase rapidly until reaching approximately $225 million in 2021.
    - Many of the existing customers (upscale department stores) would be expected to drop the DMA brand as a result of the new strategy. It is expected that revenue from the existing department store customers will be cut in half by 2021.

Scenario #2 (2/2)

- Given the introduction of a lower-priced product line, the gross margin improvements outlined in Management’s plan would likely not materialize. Gross margins are expected to remain flat at current 2017 levels.
- Cost savings associated with store closings would be expected to be the same as outlined in Scenario #1.
- SG&A expenses (not including savings associated with store closings) would be expected to improve (as a percentage of revenue) over Management’s current plan as the increased revenue would provide the company with scale advantages. By 2021, Management estimates SG&A as a percentage of revenue will be 600 bps lower than 2017 levels.

V. Trademark Dispute

Trademark Dispute

- DMA has been involved in a legal dispute with FPA, a maker of fine watches, over potential infringement of the DMA trademark.
  - FPA introduced a line of watches in Spain in 2013 under the brand "DMA".
  - DMA's two most successful international stores are in Spain (Madrid and Barcelona) and the company has registered its trademark with Spanish authorities. The company does not sell watches.
  - DMA sued FPA to stop the infringement of the name and to recover damages in late 2015, but legal proceedings are still ongoing. DMA's lawyers are optimistic that the company will be awarded damages and FPA will be required to stop usage or pay a licensing fee in the future.
  - FPA's DMA branded watches have experienced rapid growth as shown below:

FPA Sales of DMA-branded Watches

		2013A		2014A		2015A		2016A		2017A
Revenue	$	5,186	$	9,786	$	19,914	$	25,092	$	30,483
EBIT	$	1,462	$	2,828	$	5,895	$	7,628	$	9,511
as % Revenue		*28.2%*		*28.9%*		*29.6%*		*30.4%*		*31.2%*

VI. Deliverables

Deliverables (1/4)

Deliverable #1

- Perform a full Porter's Five Forces Analysis to assess the competitive landscape of DMA.
- Identify and briefly describe the opportunities and risk factors facing DMA.
- Provide a brief overview of the industry in which DMA operates.

Deliverables (2/4)

<u>Deliverable #2</u>

- Which Scenario is the more likely exit for the debtholders (i.e., maximizes value)? Conclusions should assess all facts and circumstances, including consideration of the value perspective of opposing parties (e.g., you must consider value perspectives of the potential buyer(s) and the seller). Assume a deal closing date (and valuation date) of December 31, 2017.
- Deliverables <u>must include, but are not limited to</u>:
  - Your team's recommendation on which scenario the debtholders should pursue. Assessment should include your recommendation on the price a buyer would be willing to pay and who the buyer would be.
  - Discounted cash flow (DCF) model(s) for DMA showing concluded enterprise value(s) and calculations for revenue, EBITDA , depreciation, capital expenditures, working capital, present value factors, and residual period amounts. Synergy considerations, if any, should be assessed and shown separately. Key inputs should also be detailed in the models.
  - Calculation of the weighted average cost of capital (WACC) for use in the DCF model(s).
  - Market approach analysis showing indicated enterprise value(s) that utilizes public information on comparable companies and/or recent transactions. Consider the appropriateness of the market approach relative to the income approach.
  - Qualitative list of issues analyzed, and support for final assumptions.

Deliverables (3/4)

Deliverable #3

- Discuss the reasons why DMA would sue FPA for trademark infringement. In what ways is FPA potentially harming DMA's business?
- Assuming DMA wins the trademark dispute, what amount of damages related to past infringing sales (prior to 2018) should be paid by FPA?
    - Consider the damages owed to DMA in the context of what licensing fees* FPA should have been paying for use of the DMA's name from 2013 through 2017.
- Going forward, would DMA benefit from establishing a relationship with FPA or would they prefer to stop FPA from selling DMA branded watches altogether? What circumstances might make either situation more favorable for DMA?

*Licensing fees are often calculated by multiplying branded revenue by a selected royalty rate (percentage). Support for a royalty rate selection is typically based on licensing agreements involving similar brands and/or the underlying profitability of the business.

Deliverables (4/4)

Form of all Deliverables*

- Please provide a document containing your qualitative analysis (likely completed in PowerPoint) and your quantitative analysis (likely Excel). Your deliverable should clearly present your conclusions and provide an understanding of how you arrived at them.

*Any assumptions that need to be made in the analysis will be accepted by the Committee as long at they are validated by qualitative and/or quantitative support.