

NOVEMBER 7, 2005

RETAILING

BW 50: Coach's Split Personality

How the retailer manages to keep both fashionistas and outlet shoppers happy



While Other Fashion brands fret over whether consumers will reach for their wallets this holiday season, Coach Inc. () is already feeling festive. On Oct. 25 the New York handbag maker announced its 14th straight quarter of double-digit growth in existing stores. Fueling that growth are customers such as New York public-relations executive Andrea Martin, who keep coming back for fresh iterations of weekend bags, wallets, wristlets, and more, often dropping hundreds of dollars to ensure that their purses match their pants each season. "It's not such a splurge for something you can use a few times a week," says Martin, who already owns three Coach bags. "The quality of their stuff is amazing."

Coach has expertly managed its brand to reinforce that upscale image. But fashionistas like Martin might be shocked to learn that the fastest-growing part of Coach's business these days is the factory store. That's where Coach sells off last season's accessories or irregular products at discounts of about a quarter off. Sales in those outlets grew 36% in the past quarter, vs. 14% in full-price stores. Overall, quarterly sales grew 30%, to \$449 million, and earnings jumped 48%. Coach's torrid growth streak helped earn it the No. 17 spot on the BusinessWeek 50 list of top corporate performers.

The challenge now is to make sure the rapid growth in the bargain-bin end of the business doesn't dilute the luxury feel of the Coach brand. After all, brands from Calvin Klein () to Tommy Hilfiger () took an image dive when their goods drifted too far into discount channels. But that won't happen to Coach, vows Chairman and Chief Executive Officer Lew Frankfort.

LOYAL UP AND DOWN

For one thing, he has developed a strategy that strictly separates fashion-forward Coach fans from the ones who love snapping up out-of-date gear on the cheap. The company's 85 factory outlets are normally located at least an hour's drive or 60 miles from its 199 full-price stores. Because Coach never offers discounts in its regular stores or via the Web -- and doesn't allow department stores to mark down Coach goods either -- those who want bargain-priced products can get them only at outlets. And they won't get access to the latest products, which are rolled out each month in regular stores. Instead, they get discontinued models or older styles that are manufactured specifically for outlets. "It allows [Coach] to dispose of items that don't work, in a very different channel," says Kurt Barnard, president of Barnard Retail Consulting Group.

As a result, there's very little overlap between shoppers at opposite ends of the spectrum. According to Coach's consumer research, the average full-price shopper is 35, college-educated, and a single or newly married working woman. Factory outlet shoppers are, on average, 45, college-educated, married, and likely to spend 80% of their Coach dollars at outlets. "They're as brand-loyal as our full-price shoppers," says Frankfort, who notes that outlet fans drop about \$770 a year on Coach products, vs. the full-price average of \$1,100. "These are professional moms who want beautiful, well-made brands at low prices." Having this fall's gold-pleated Hobo bag or coyote fur-lined pocket duffel isn't a top priority.

UPSCALE FLAGSHIPS

At the same time, those who do covet the latest fashions continue to find satisfaction in Coach. The beauty of the brand, according to Barnard, is its positioning as an ultra-luxe label that nevertheless boasts relatively reasonable price tags. Though Coach sells a python satchel for \$1,900, that's a relative bargain compared with a \$14,800 crocodile bag from Gucci. Coach bags typically cost around \$200 to \$400. Yet a lot of buyers put it alongside names such as Gucci, Versace, and Dior. What makes Coach shoppers feel like they are in the same league as those tony names are the goods' quality and eye-pleasing designs, as well as the luxurious stores where they are sold.

In order to drive home those upscale associations, Frankfort is putting chic flagship stores in some of the world's most expensive retail real estate. The company is opening massive stores this November on Beverly Hills' Rodeo Drive and New York's Madison Avenue. "The flagship serves as a beacon for the brand," says the Coach chief. Still, the bulk of stores are in more modest locations that pump out the hottest new products. That's the right strategy, says retail real estate consultant Steven Greenberg, who argues that too many companies go flagship-crazy at the expense of the bottom line. Coach, he says, "is extremely prudent."

Still, Frankfort's hopes are clearly pinned on wooing those Coach shoppers who crave the trendiest bags and accessories. He credits the fast growth in the factory channel with a fresh effort to upgrade merchandise there. He expects the number of outlets to top out at around 100, while the full-price universe easily could reach 350 stores in North America over the next several years. "Our destiny lies in our ability to grow full-price stores," he says. That's why the two new palatial flagships are crucial to Frankfort -- to keep the brand image strong and sales even stronger.

By Diane Brady in New York