Case 1-2: True Religion Jeans: Will Going Private Help It Regain Its Congregation?*

True Religion Board Accepts $835 Million Takeover Bid

> *"It's been more than half a year since the 10-year-old high-end-jeans seller, no longer the must-have brand, put itself up for sale.*
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> *True Religion Apparel Inc., the Southern California purveyor of pricey designer denim, may have gotten too small for its britches. More than half a year after putting itself up for sale amid growth struggles and fluctuating stock, the high-end-jeans seller said its board unanimously accepted an $835-million takeover offer from investment firm TowerBrook Capital Partners."*
>
> —*excerpt from* The Los Angeles Times[1]

True Religion Brand Jeans

Founded in 2002 by Jeff Lubell, True Religion had become one of the largest premium denim brands in the United States by 2012. Although True Religion made its debut in upscale department stores and trendy boutiques a decade earlier, the company owned 86 full-price retail stores and 36 outlet stores in the United States as well as 30 stores in international markets by the end of 2012. The company's domestic retail store business accounted for about 60 percent of revenues and 64 percent of operating profit before unallocated corporate expenses in 2012. Just five years earlier, the U.S. retail store segment generated only 17 percent of sales and 25 percent of operating profit before unallocated corporate expenses (see Exhibit 1).

Lubell's vision of the company had come true—at least partly. The company had transformed itself from a jeans designer into an apparel retailer with it own brand à la Buckle and Diesel. At the same time, True Religion had managed to shift its product mix so that sportswear accounted for almost 35 percent of sales in its company-owned stores. Lubell felt these two ingredients were critical to establishing True Religion as a "lifestyle brand." The ultimate in product differentiation, many companies attempt to create so-called "lifestyle" brands that transcend product category and inspire deep consumer loyalty. Becoming a lifestyle brand was the key to insulating True Religion from the inevitable fluctuations in fashion trends.

Moreover, True Religion's sales had grown at an average annual rate of almost 22 percent from 2007 to 2012 (see Exhibit 2). The company's return on invested capital was an impressive 27 percent, and its return on average assets was 12 percent in 2012. Despite these factors, press articles and analyst reports on True Religion described the company as "the struggling maker of premium denim."[2] A *New York Post* article titled "Escape from Hell for True Religion" described private equity firm TowerBrook as the company's "savior."[3]

What had gone wrong at True Religion? Was the change in ownership the answer to the company's problems? Could True Religion regain its status as the must-have premium denim brand in the United States? Would the company be forced to pull a "Rock & Republic" and reposition itself as a mid-priced brand? Was premium denim destined to go the way of Flash Dance legwarmers and Crocs as fast fashion from the likes of H&M became more mainstream? Private equity investors had snapped up stakes in both established and up-and-coming premium denim brands in the previous five years. With soon only one publicly traded premium jeans maker (Joe's Jeans) left, should investors stay away from the industry?

A Brief Recap of the Recent History of the U.S. Denim Market

Calvin Klein popularized the concept of premium jeans in the late 1970s. The designer burst onto the jeans scene with shockingly high prices, a skin-tight fit, and a controversial advertising campaign featuring a very young Brooke Shields. As Brooke Shields confided to U.S. consumers that nothing came between her and her "Calvins," the $35-per-pair jeans flew off store shelves. At the time, mainstream Lee and Wrangler blue jeans retailed for about $12 per pair on

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*This case was prepared by Bonita Austin for the purposes of class discussion. It is reprinted with permission.

Exhibit 1 True Religion Brand Jeans Operating Segments ($ in thousands)

Net Sales	2007	2008	2009	2010	2011	2012
U.S. Consumer Direct	$29,268	$75,314	$129,030	$189,097	$251,334	$281,583
U.S. Wholesale	111,390	153,235	123,203	104,874	86,268	99,215
International	31,728	40,044	54,479	64,443	78,974	83,824
Core Services[a]	870	1,407	4,289	5,300	3,222	2,663
Total Company Net Sales	$173,256	$270,000	$311,001	$363,714	$419,798	$467,285
Gross Profit						
U.S. Consumer Direct	$22,380	$57,669	$95,276	$136,915	$178,341	$197,328
Gross Margin	76.5%	76.6%	73.8%	72.4%	71.0%	70.1%
U.S. Wholesale	60,007	78,670	65,882	53,362	44,445	50,452
Gross Margin	53.9%	51.3%	53.5%	50.9%	51.5%	50.9%
International	15,498	19,255	30,115	34,402	45,821	49,080
	48.8%	48.1%	55.3%	53.4%	58.0%	58.6%
Other	870	1,407	4,289	5,300	3,222	2,663
Total Company Gross Profit	$98,757	$157,003	$195,564	$229,981	$271,831	$299,525
Total Company Gross Margin	57.0%	58.1%	62.9%	63.2%	64.8%	64.1%
		Restated	Restated			
Operating Profit	2007	2008	2009	2010	2011	2012
U.S. Consumer Direct	$11,875	$27,810	$44,766	$64,641	$88,453	$93,726
Operating Margin	40.6%	36.9%	34.7%	34.2%	35.2%	33.3%
	$0.252					
U.S. Wholesale	36,405	71,884	60,107	46,265	37,116	44,333
Operating Margin	32.7%	46.9%	48.8%	44.1%	43.0%	44.7%
International	14,718	16,761	25,167	17,487	15,927	7,895
Operating Margin	46.4%	41.9%	46.2%	27.1%	20.2%	9.4%
Core Services[b]	−15,856	−47,579	−52,443	−58,471	−66,885	−67,837
Total Company Operating Profit	$47,143	$68,877	$77,598	$69,923	$74,612	$78,118
Total Company Operating Margin	27.2%	25.5%	25.0%	19.2%	17.8%	16.7%
Assets	2007	2008	2009	2010	2011	2012
U.S. Consumer Direct	$10,167	$36,603	$55,763	$68,418	$78,089	$90,654
U.S. Wholesale	41,248	43,030	31,159	35,001	26,182	27,584
International	6,519	8,362	16,897	24,940	41,700	54,764
Core Services[c]	55,324	78,457	125,987	167,525	214,182	232,714
Total Company Assets	$113,258	$166,452	$229,806	$295,884	$360,153	$405,716

[a] Licensing revenues generated by royalty agreements.
[b] Unallocated corporate expenses.
[c] Unallocated corporate assets.

Source: True Religion Apparel Inc. 10K - 2007, 2008, 2009, 2010, 2011, 2012.

average. Suddenly, jeans were no longer functional wardrobe staples. They were sexy fashion statements. The jeans craze peaked in 1981 when retail sales jumped to a record $6 billion and 520 million pairs.[4] As designer jeans fell out of favor and the prime 14–24-year-old jeans-buying cohort aged, domestic annual jeans sales slid to 416 million pairs by 1985.

Following a protracted decline in the 1980s, the market surpassed its earlier peak and hit annual sales of 511 million pairs in 1995. Denim jeans unit sales grew at a strong 7 to 10 percent per year from 1990 to 1996. Then, in 1997, the denim market experienced a sharp slowdown in growth that lasted until the end of 1999—rising just 3 percent per year on average. For some industry players the slowdown meant disaster. Levi Strauss saw its sales plunge more than 13 percent in 1998, almost 14 percent in 1999, and nearly 10 percent in 2000. U.S. textile giants Cone, Swift, and Burlington cut prices and idled production lines—all victims of a denim glut at retail caused by a shift in fashion trends.

Exhibit 2 True Religion Brand Jeans Selected Financials ($ in thousands except per share amounts)

	2007	2008	2009	2010	2011	2012
Revenues	$173,256	$270,000	$311,001	$363,714	$419,798	$467,285
Cost of Goods Sold	74,429	112,999	115,439	133,735	147,969	167,762
Gross Profit	$98,827	$157,001	$195,562	$229,979	$271,829	$299,523
Gross Margin	57.0%	58.1%	62.9%	63.2%	64.8%	64.1%
Selling, General & Administrative Exp.	51,685	88,125	117,965	160,057	197,218	221,406
Operating Profit	47,142	68,876	77,597	69,922	74,611	78,117
Operating Margin	27.2%	25.5%	25.0%	19.2%	17.8%	16.7%
Other Expense (Income)	−1803	−1065	−169	−403	637	−94
Pretax Profit	48,945	69,941	77,766	70,325	73,974	78,211
Taxes	21,100	25,570	30,434	26,690	28,197	31,513
Tax Rate	43.1%	36.6%	39.1%	38.0%	38.1%	40.3%
Net Income	$27,845	$44,371	$47,332	$43,635	$45,777	$46,698
Redeemable Noncontrolling Interest	0	0	0	139	810	683
Net Income Attributable to True Religion	$27,845	$44,371	$47,332	$43,496	$44,967	$46,015
Net Margin	16.1%	16.4%	15.2%	12.0%	10.7%	9.8%
Earnings Per Share (Diluted)	$1.16	$1.83	$1.92	$1.75	$1.80	$1.82
Average Shares Outstanding (Diluted)	23,949	24,270	24,659	24,852	25,026	25,328
Selected Balance Sheet Figures	**2007**	**2008**	**2009**	**2010**	**2011**	**2012**
Cash & Short-Term Investments	$34,031	$62,095	$110,479	$153,792	$200,366	$186,148
Accounts Receivable	27,898	33,103	27,217	27,856	23,959	31,647
Inventory	20,771	25,828	34,502	41,691	53,320	65,655
Propterty, Plant & Equipment	11,579	28,006	39,693	48,448	53,698	61,565
Total Assets	113,258	166,452	229,806	295,884	360,153	405,716
Accounts Payable	$9,597	$10,633	$11,717	$17,234	$22,872	$30,868
Total Debt	0	0	0	0	0	0
Shareholders' Equity	95,247	142,250	197,854	249,032	299,788	332,935
Total Liabilities & Rquity	229,806	166,452	229,806	295,884	360,153	405,716
Rent Expense	$3,700	$9,300	$16,200	$24,100	$30,600	$37,600
Advertising Expense	1,200	3,900	5,400	8,000	7,900	11,700
Number of Company-Owned Stores	15	42	73	94	109	152

Source: True Religion 10Ks 2007–2012

The introduction of new stretch fabrics and widespread acceptance of "casual Friday" and other office "dress-down" days stimulated demand for khaki, carpenter, and cargo pants and cut into denim demand in the late '90s. Casual wear for work became so socially acceptable during the "dot-com bubble" that even staid Wall Street firms permitted employees to wear "golf casual" rather than formal business attire to work on Fridays in spring and summer. Nevertheless, even as demand for basic five-pocket denim jeans suffered from the shift in consumer preferences in casual wear in the late 1990s, demand for women's fashion jeans grew. Angelo La Grega, president of VF Corporation's Mass Market Denim Division, noted in a 1997 interview with *Women's Wear Daily*, "The business is moving from pure commodity to fashion basics."[5] The primary reason for the resurgence in demand for fashion jeans was the availability of denim jeans in exciting new washes and finishes.

"Distressed" and "dirty" denim hit retail shelves in spring 2000. The new distressed jeans tapped into consumers' taste for vintage denim. Distressed, dirty jeans were already "broken in," wrinkled, and stained and looked as if the owner had worn them for years. The Italian jeans maker Diesel had pushed dirty denim for several seasons before it gained approval from other designers. A few designers like Kenneth Cole also experimented with the new stretch denim, a cotton denim that incorporated 2 percent Lycra spandex to improve wearing comfort.[6]

Against that backdrop, Jerome Dahan and Michael Glasser introduced their 7 For All Mankind premium denim line to a consumer market hungry for fashion innovations. The new denim label would fuel the hottest upscale denim market since the late 1970s and eventually would spark product improvements at every price point in the jeans spectrum. Aspiring as well as established designers would introduce literally hundreds of denim labels in the new decade as they answered the siren call of high growth and high profit margins. Retailers eagerly snapped up new offerings, as their customers demanded the latest hot jeans. The premium denim market, defined as jeans retailing for $100 or more, would jump from a dollar market share of about 1 percent in 2000 to about 10 percent of retail sales in 2012.

U.S. Premium Denim Industry

Many industry observers believed that the estimated $1.7 billion (retail) premium denim market had begun to mature in 2006. Overall U.S. denim jeans ownership peaked at 8.2 pairs of jeans per consumer that year. The appeal of denim was strong, but average jeans ownership had fallen to 6.7 pairs per consumer by the end of 2012.[7] According to a 2012 Cotton Inc. consumer survey, 75 percent of women and 73 percent of men stated they "loved or enjoyed wearing denim." Still, those figures were down 3 percentage points each from the same survey in 2007.[8]

With nearly seven pairs of jeans in the typical American woman's closet and the move away from fashion jeans to basics, it had become increasingly difficult to persuade consumers to buy new pairs of jeans. At the same time, the premium market had shown it was not immune to economic downturns. After years of torrid sales growth, the premium jeans industry experienced its first slowdown in 2007 with sales down about –5 percent. Although the industry seemed to defy economic weakness with sales up an estimated 17 percent in 2008, premium denim revenues slumped an estimated –8 percent in 2009 and fell about –10 percent in 2010.

Industry sales jumped about 11 percent in 2011 and rose an estimated 7 to 8 percent in 2012 to about $1.7 billion at retail as the U.S. economy improved (see Exhibit 3). Nevertheless, the outlook for the market was cloudy. True Religion and Joe's Jeans reported good growth in sales to retail accounts in the first quarter of 2013, but True Religion's company-owned store growth was fueled by sales to outlet stores. 7 For All Mankind brand reported disappointing sales results in the second quarter of 2013 (down –5 percent) due to softness in the upscale department store channel. Moreover, 7's management forecasted implied domestic growth for the brand of only 2 percent per year on average from 2012 to 2017—suggesting tepid growth for the industry as 7 was one of the largest premium denim brands in the United States.

Many investors were worried about the so-called aspirational shopper. While the core luxury buyer had returned to high-end shopping as the recession ended, aspirational shoppers had largely stayed away. At the same time, enormous improvements in bargain-priced jeans' fabric, fit, and styling encouraged consumers to "trade down" from expensive brands to stalwarts like Levi's, Lee, and Gap jeans. Some analysts estimated that as much as 70 percent of luxury brand sales and 50 percent of the growth in the luxury market was derived from so-called "aspirational" shoppers prior to the recession.[9] Aspirational shoppers—middle-class consumers with luxury tastes—had household incomes between $75,000 and $150,000. Easy credit and rising home prices fueled spending and made the aspirational shopper the target of many brand marketing campaigns in the heady days before the housing bubble burst and unemployment surged to post–Great Depression highs.

Prior to the recession, many premium denim labels defined themselves as "aspirational brands": expensive but not as pricey as couture brands that charged thousands for each piece of clothing. Numerous press articles declared the death of the aspirational shopper and a new "bargain hunting is cool" zeitgeist that would survive after the economy rebounded. A November 2012 consumer survey by Accenture showed nearly two-thirds of American shoppers did not intend to return to pre-recession spending patterns.[10]

While not everyone believed that the aspirational shopper was gone for good, Tiffany's earnings disappointments for holiday 2012 and in the first quarter of 2013 were attributed partly to weakness in aspirational shopper spending on the brand along with increasing product prices. Without the aspirational shopper, new premium denim customers were likely to prove hard to come by in the U.S. market. Still, the Accenture study showed half of the consumers surveyed were likely to make a small luxury purchase in the next six months. Although more consumers were likely to purchase a luxury or gourmet food item, 48 percent of consumers surveyed said they were likely to purchase luxury apparel to mix into a wardrobe of more affordable items.[11]

Investors also were concerned about fashion trends and prices. Embroidered, embellished, and distressed jeans were all the rage from 2002 to 2005. In those days of skyrocketing demand, premium denim designers had many ways to differentiate their products and cash in on current fashion trends. As the U.S. economy began to slow, flashy fashion jeans fell out of favor with consumers whose interest in "basics" increased as their incomes declined. On

Exhibit 3 2012 Selected Financials—Jeans Companies ($ in thousands except per share amounts and betas)

	Buckle	Guess	Joe's	Levi's	Fifth and Pacific[a]	True Religion	VF Corp
:evenues	$1,124,007	$2,658,605	$118,642	$4,610,193	$1,505,094	$467,285	$10,879,855
:ross Profit	499,315	1,067,123	56,170	2,199,331	842,975	299,523	5,061,975
:ross Margin	44.4%	40.1%	47.3%	47.7%	56.0%	64.1%	46.5%
'perating Profit	$258,175	$274,525	$10,717	$333,979	–$34,451	$78,117	$1,465,267
'perating Margin	23.0%	10.3%	9.0%	7.2%	–2.3%	16.7%	13.5%
iterest Expense	$0	$1,640	$376	$134,694	$51,684	$0	$93,605
et Income	164,305	178,744	5,565	143,850	–74,505	46,015	1,086,138
PS (fully diluted)	$3.44	$2.05	$0.08	NA	–$0.68	$1.83	$9.70
iares Outstanding	48,059	86,540	66,849	NA	109,292	25,328	110,205
ash	$144,022	$335,927	$13,426	$406,134	$59,402	$186,148	$597,461
ccounts Receivable	3,470	324,971	812	500,672	121,591	31,647	1,222,345
ventory	103,853	369,712	31,318	518,860	220,538	65,655	1,354,158
ital Assets	477,974	1,713,506	86,024	3,170,077	902,523	405,716	9,633,021
ccounts Payable	$34,124	$191,143	$10,893	$225,726	$174,705	$30,868	$562,638
ital Debt	0	1,901	0	1,729,211	406,294	0	1,844,598
areholders Equity	289,649	1,100,868	71,739	–101,508	–126,930	332,935	5,125,625
preciation	$33,834	$87,197	$1,456	$122,608	$74,411	$13,373	$196,898
pital Expenditures	30,297	99,591	2,779	83,855	82,792	21,994	251,940
mpany Owned Stores	440	1,118	28	511	213[c]	152	65[e]
ensed/Franchised Stores	0	985	0	1,800	11	0	0
ta (as of 7/22/13)	1.04	1.71	1.30	NA	2.62	1.08	0.77
are Price (7/22/13)	$56.42	$31.78	$1.35	NA	$23.17	$31.90	$194.86
n Brand as % of Sales	34%	100%	100%	100%	100%	100%	100%
. Comparable Store Sales Change	2.1%	–6.6%	10.0%	NA	10.0%[c]	2.7%	NA
. Sales	100%	50.8%	95.8%	50%	95%[d]	82.1%	60%[e]
ernational Sales	0%	49.2%	4.2%	50%	5%	17.9%	40%

rmerly Liz Claiborne-owns Lucky Jeans.
iess comparable store sales and sales mix for North America.
cky Brand Jeans stores only.
timated Lucky Jeans sales only. Does not include other FNP brands.
or All Mankind only.

plus side, a good pair of dark jeans was considered must have" item for women. *Glamour* magazine put is at #7 on its list of "10 Wardrobe Items Every Woman uld Own."[12] On the negative side, Topher Gaylord, 1-president of 7 For All Mankind, commented in a 2009 rview with the *New York Daily News*, "We really don't eve consumers today understand the value of premium im."[13] It was hard to differentiate a plain, dark blue of expensive jeans from less expensive basic jeans. n interview with Reuters, industry analyst Eric Beder , "Premium denim slows down when the trend goes :. How do you recognize it's premium? How much dif- itiation is there in that pair of $189 jeans compared to a pair when they are just dark and straight?"[14]

Skinny jeans had played well with consumers over the past five years, but they were as difficult to differentiate as other types of basic jeans. Colored denim and jeggings (denim leggings) had attracted consumers back to the premium market in 2011 and 2012. In general, they did not command super premium prices and so gave consumers a more affordable entry-level price point during the recession. Those offerings continued to drive premium purchases in 2013, but premium jeans designers were scrambling to find the next big thing in jeans. Designers were experimenting with wax and rubber coatings as well as patterned denim. Thus far, nothing had taken off with consumers. Moreover, the dip in denim's overall popularity from 2008 to 2012 had not gone unnoticed by retailers. Retailers cut denim jeans floor space allocation and increased floor space for women's dresses and skirts and men's athletic wear and non-denim pants in 2012–2013 compared with 2010–2011.[15]

Price points continued to be an issue for premium denim designers in 2013. Prior to the recession, consumers had been willing to pay sometimes as much as $600 for a pair of jeans that was "just right." "It was all just a fad," said Jeff Rudes, founder of fast-growing J Brand premium jeans.[16] Even though the economy improved, many consumers remained reluctant to pay up for the "right" pair of jeans. *The Wall Street Journal* and *The New York Times* ran stories about the gulf between premium jeans prices at the cash register and the price the designers paid to make consumers' favorite jeans. A 2011 *Wall Street Journal* article quoted Lubell as saying True Religion's best-selling "Super T" jeans cost only about $50 to make, wholesaled for $152, and retailed at $335 per pair.[17] The press coverage only served to reinforce consumers' doubts about whether the most expensive jeans were "worth it."

Notably, only about 15 percent of 7 For All Mankind's denim jeans were priced at $200 or more in 2013—up from 5 percent in 2009 but down sharply from 25 percent in 2008 and the pre-recession peak of 30 percent.[18] A survey of the Internet shopping sites of the top five premium jeans brands revealed that on average four of the five had prices below $200 on 83 percent of their jeans. True Religion was the outlier with 56 percent of its product line priced at $200 or above. Interestingly, the company had chosen to buck the industry trend and had increased the amount of pricier jeans in its line, up from 45 percent in 2010.

Industry insiders were concerned about a new tariff on U.S. exports of women's jeans to the European Union that became effective on May 1, 2013. The 38 percent tariff was tough on the premium jeans industry as about 75 percent of all premium jeans were manufactured in Los Angeles. Lower-end jeans typically were produced outside of the United States due to the relatively high U.S. labor costs. The tariff was three times larger than the old tariff on women's jeans. "Made in the USA" carried cachet with consumers in the European premium jeans market. Lowering costs by relocating manufacturing to low–labor cost countries was likely to hurt the brand images of expensive jeans as the brands risked losing their authenticity by moving out of the United States. Some premium denim makers were experimenting with less expensive fibers in order to lower costs, but consumers so far had not flocked to the cotton blends.

Premium denim labels had already experienced cost pressures as cotton prices hit a post–Civil War high in 2010. The 68 percent jump in average cotton prices in 2010 was followed by an additional surge of 48 percent in 2011. Denim designers cheered as cotton prices plunged 43 percent in 2012. The price relief continued through March 2013. Drought conditions and lower acreage allotted to cotton production by farmers in the United States along with aggressive cotton stockpiling by the Chinese government pushed cotton prices up in April and May 2013. A cotton price spike was the last thing the premium denim makers needed, given consumers' reluctance to pay up for jeans.

Still, it appeared that Americans' nearly 140-year old love affair with denim was still going strong in 2013. The question for the industry remained was the market still "Rich & Skinny"—like denim guru Glasser's premium brand—or had it become more like Cheap Monday, the Swedish line of mid-priced jeans?

Competitive Landscape

Despite the exodus of weaker brands during the recession, the premium denim market remained crowded. The top four premium jeans brands held an estimated combined 70 percent share of the market in 2012—up from an estimated combined share of 65 to 68 percent in 2007, but down from an estimated 80 percent in 2009. Conventional wisdom held that the underlying slowing industry growth combined with the economic downturn would result in a shakeout that would leave the strongest premium denim makers in control of the market. That had not turned out to be the case. In fact, only three of the top five brands in 2010 remained in the top five in 2012; J Brand and Hudson had replaced Citizens of Humanity and Rock & Republic in the top five. True Religion and 7 For All Mankind were still the top brands in the segment, but both had shown signs of losing some of their grip on the category in the past two years. The remaining 30 percent of the market was split between dozens of denim labels.

A July 2013 Internet survey of the five major U.S. upscale department stores and two prominent denim boutiques revealed that each carried 66 different brands of women's premium jeans on average. The same retailers carried only 28 brands on average in December 2010. However, some retailers sold many more brands. Notably, trendsetting California-based Revolve Clothing offered 86 different brands of premium women's jeans—up from 55 in 2010. Similarly, Nordstrom sold 74 brands of women's premium jeans compared with 45 brands in 2010. The explosion in brands highlighted several features of the premium denim market.

First, it remained relatively easy to launch a new brand and gain retail shelf space. Though this was long a major barrier to entry in consumer products categories, the fickle nature of many premium denim consumers made getting retail distribution much less of a problem for an innovative denim entrée. Fashion consumers were always on the lookout for the latest, most fashionable items. The shift from the fashion jean to the wardrobe staple had not diminished the importance of innovation in style, fit, finish, and fabric to consumers. Brands that missed key fashion trends frequently were discarded in favor of upstarts, and retailers were happy to offer the products as with an average retail mark up of 2.2 times wholesale; their premium denim margins were high.

Second, upscale retailers continued to try to differentiate their stores from their rivals' stores through product offerings and a fashion "point of view". Established large brands had to fend off the advances of upstarts and smaller brands as jeans lines attempted to segment the premium market and carve out their own niches. The high margins and returns of the larger players along with low capital requirements enticed new "jeaners" or denim specialists to enter the segment. As denim designer Mik Serfontaine stated in a 2010 interview for the Sundance Channel documentary *Dirty Denim*, "Make up some samples and take it to the trade show—you're in business."[19] Moreover, established fashion designers such as Donna Karan and Helmut Lang could knock out a few jeans styles and get shelf space on the strength of their broad apparel lines. While these designers might not pose a serious threat to the big premium brands, if industry growth remained low after the economy rebounded, the premium denim labels would have to deal with them as every market share point would be important.

Third, the success of a premium denim line depended heavily upon the market and fashion insights of the head designer. It was notoriously difficult for even the savviest designers to generate hit after hit in the fast-moving fashion world. Once a semiannual event, new style launches had become a monthly event in some market segments such as the popular fast fashion category. Retailers such as H&M, Forever 21, and Zara had begun to transform the fashion industry. H&M wanted to "surprise" its customers and always have something new in stock in order to generate repeat business. Zara could design and produce its own products and get them on the shelf within a month. The biannual fashion cycle had become a year-round fashion cycle.

Premium denim was not immune to the nearly constant pressure to introduce new products to induce consumers to purchase—especially now that the underlying growth of the U.S. premium denim market appeared to have experienced a secular slowdown. With seemingly everyone wearing either premium jeans or less-expensive jeans with premium features, consumers needed a reason to buy new jeans. In late 2010, Jeff Rudes gave consumers something new to purchase by testing and then launching a line of brightly colored jeans under his J Brand line. So far, nothing had emerged to take the place of the popular colored jeans or the ubiquitous skinny jean, and both were easily copied.

Retailers constantly were on the lookout for the next hot brand as premium denim buyers were fickle. In a recent Cotton Inc. survey of premium denim consumers, 84 percent of those surveyed indicated they were willing to try a new brand.[20] In fact, jeans designers launched new brands even in the depths of the recession and downturn in the market. Current/Elliott is "...the most refreshing denim line to come out of LA's jeans scene in a long, long time," according to a Vogue magazine article. Current/Elliott gained traction in upscale department stores as the new "it-jeans" following its 2008 launch. The brand looked as if it had staying power as upscale department store retailers devoted nearly 70 percent more "e-shelf space" or Internet shelf space to the line as to True Religion in 2013.

Table 1 shows the top 11 women's premium jeans brands by e-shelf space devoted to them by the five major upscale department stores, and two denim boutiques in July 2013, compared with e-space in the same Internet stores in December 2010. Upscale retailers cut physical shelf space devoted to premium jeans in their

Table 1 July 2013 e-Shelf Space Survey Top Premium Denim Brands Selected Upscale Retailer Internet Sites

	Internet Shelf Space	
Designer (Women's)	**2010**	**2013**
7 For All Mankind	13%	8%
AG Jeans	3%	5%
Citizens of Humanity	11%	5%
Current/Elliott	4%	5%
Genetic Denim	2%	2%
Hudson	3%	4%
J Brand	6%	10%
Joe's	7%	3%
Paige Premium	7%	4%
NYDJ	6%	4%
Rag & Bone	1%	5%
True Religion	6%	3%
All Others	31%	42%

Sources: Internet sites of Bergdorf Goodman, Bloomingdale's Neiman-Marcus, Nordstrom, Revolve Clothing, Saks, and ShopBop.com brick-and-mortar stores but nearly tripled the amount of premium jeans on their Internet shopping sites between December 2010 and July 2013.

While it was not possible to draw a direct line from e-shelf space to market shares, the Internet survey clearly showed smaller jeans brands had encroached upon the e-shelf space of the larger brands as retailers increased their efforts to satisfy the desires of their customers for hot fashion items and unique looks. J Brand, AG Jeans, and Rag & Bone were the big winners with the retailers surveyed. J Brand, now majority owned by Star Capital, had been an up-and-comer prior to the recession. The three early movers in the premium denim market—7 For All Mankind, True Religion, and Citizens of Humanity—each lost a substantial amount of e-shelf space between 2010 and 2013. Given True Religion's aggressive push into the retail business it is not surprising that the company's major retail accounts would choose to cut back their shelf space allocations. Still, the e-shelf space loss again raised the question of whether the older brands remained relevant a decade or more after their launches into the category. Had J Brand, AG Jeans, and Rag & Bone done a better job in creating fashion trends than the industry stalwarts? If so, would their design teams be able to keep their fingers on the pulse of the fickle fashionista?

Manufacturing Process and Supply Chain

One bale of cotton can be made into 215 pairs of men's jeans or 250 pairs of women's jeans, according to the National Cotton Council.[21] At 480 pounds per bale and a 2012 average world cotton price of about $0.89 per pound, raw cotton accounted for an estimated $1.71 per pair of women's jeans. How did less than $2 per pair of cotton result in jeans that retailed for $100 to $350 per pair?

Premium jeans ranged from traditional 100 percent cotton denim jeans to jeans made from stretch denim—a combination of cotton and spandex—to jeans made from denim fabric composed of cotton and small amounts of polyester. Nevertheless, cotton was the major raw material for premium jeans. The top five cotton-producing nations were China, India, the United States, Pakistan, and Brazil in 2012. The big five accounted for 79 percent of the world's cotton supply, according to the U.S. Department of Agriculture. China alone produced 29 percent of the world supply of cotton. Number-two producer India supplied 22 percent of the world's cotton. At number three in the world, the United States produced 17.3 million 480-pound bales of cotton or 14 percent of the world supply.[22] China was the largest consumer of cotton in the world. The United States was the largest exporter of cotton in the world.

Cotton prices had been in a long-term decline as worldwide production costs fell with farm technology and farming practice improvements. After hitting their lowest levels in more than 30 years in 2001, cotton prices rebounded in 2002 only to slump for another four years. Prices rose slightly over 10 percent in 2007 and about 14 percent in 2008.[23] As a result of the "worst global consumption contraction in 65 years," cotton prices fell 12 percent on average in 2009. Unusually low stockpiles, heavy rains and flooding in China and Pakistan, and export restrictions in India reduced the cotton supply and pushed prices up to a 150-year high in 2010. Calendar year prices were up 68 percent on average to nearly $1.00 per pound. Prices surged an additional 48 percent on average in 2011 to about $1.05 per pound before easing back to $0.89 per pound in 2012.[24] While cotton prices continued to ease in the first quarter of 2013, they picked up again in May and June. Cotton consumers were worried that the combination of aggressive stockpiling by the Chinese government, drought conditions in much of the United States, and less acreage earmarked for U.S. cotton production would push prices back to 2011 levels. At $0.93 per pound, June's cotton prices were well below cotton highs in 2011 but far above historic levels of around $0.66 per pound.

U.S. denim producers dominated worldwide production and exports of the fabric for many years but had been surpassed by China due to favorable production costs. U.S. production had declined for years as manufacturers closed American mills and relocated capacity to lower-cost countries. North Carolina–based Cone Mills, known as the "King of Denim," was the world's largest producer of denim fabric for most of its 120-year existence. While the company remained a major player in the industry, Cone struggled against low-cost international competition and the phaseout of U.S. denim fabric quotas. The company was known for its ability to produce high-quality denim and had been the sole supplier of denim to Levi's for nearly 40 years.

Established in 1891 by the Cone brothers, Cone Denim was a subsidiary of publicly traded International Textile Group in 2013. The division had found a profitable niche in serving premium denim customers. Massive restructuring efforts and a focus on high-valued-added materials allowed the company's denim division to turn a profit in 2009 and remain profitable for the next three years—despite high cotton prices. International Textile Group's bottom-weight woven fabrics division generated $566 million in revenues and $29 million in operating profit in 2012. The division's operating margin improved somewhat as its product mix shifted to more profitable lines. Nevertheless, sales declined slightly in 2012 as the company was forced to pass on the relief in cotton prices to its customers in the form of price cuts. Unfortunately, much of its inventory remained tied to the older, higher cotton costs. Management remained concerned about the outlook for cotton prices as customers were reluctant to accept higher denim costs but demanded lower denim prices as soon as cotton prices eased.

Most domestic premium jeans companies preferred to source denim fabric from U.S. suppliers like Cone's famous White Oak Mill. Their designers felt the fabric was superior in quality and gave their jeans "authenticity" associated with being made in the United States. Premium denim jeans companies all demanded high quality, and many were willing to pay for Cone's special vintage selvage denim made on narrow Draper fly-shuttle looms that went out of production in the 1970s. Highly prized by denim zealots for its durability and beauty, selvage denim was used only in the most expensive jeans. According to Kenneth Kunberger, International Textile Group's chief operating officer, Cone's White Oak Mill was the only mill in the world using the old fly-shuttle looms in 2012.[25] Some premium jeans makers swore by Japanese and Italian denim fabric. At any rate, denim fabric makers like Cone and privately held Swift Denim had low margins and little bargaining power. As it had been for more than a decade, the issue for U.S. denim makers in 2013 was survival in the face of intense competition from foreign competitors.

In jeans made of stretch denim, cotton content typically ranged from 95 to 99 percent with spandex making up the rest of the fiber in the stretch denim fabric. The incorporation of spandex into cotton denim allowed women's jeans to be form fitting but comfortable due to the "give" of the spandex fibers. The use of "stretch" in premium jeans was limited by spandex's inability to withstand harsher finishing treatments like bleaching as well as the lack of rigidity of high spandex content denim and its relative lack of durability. High cotton prices and the 38 percent tariff the European Union imposed on U.S. premium denim exports in 2013 had denim designers experimenting with less expensive alternative fibers such as Tencel. Premium denim consumers still demanded cotton garments and had not yet accepted alternatives.

Each pair of jeans used about 1.5 yards of denim fabric. While basic denim went for $2 to $3 per yard, premium denim typically sold for about $7 per yard but could wholesale for $15 or more per yard. The usual fabric cost per pair was around $11. Most upscale jeans companies did not own their own manufacturing capacity; rather, they used contract manufacturers to cut and sew the fabric into jeans. There were thousands of cut-and-sew operations around the world, but the U.S. premium brands all used U.S. manufacturers. About 75 percent of all premium denim was made in Los Angeles in 2012. The premium denim companies liked the shorter lead times and lower shipping costs as well as high quality control they got by using domestic suppliers. In addition, they felt U.S. consumers wanted and expected their expensive jeans to be "made in America"—the inventor of blue jeans. Manufacturing costs came in at about $10 per pair with another $2 per pair spent on shipping.

Garments went from the factory to denim laundries, which were responsible for the all-important finishing process. Many jeans designers hung their shingles out in Los Angeles due to the prevalence of laundries in the LA area. "Raw" jeans underwent a variety of labor-intensive finishing processes including special washes, sand blasting, painting, bleaching, ripping, tearing, the addition of whiskers, the application of resins, baking, and pocket embroidery. One popular process, stonewashing, literally involved putting jeans in huge washers full of pumice stones in order to break the denim fibers down and make them softer.

One pair of jeans could undergo 15 different treatments before achieving the desired "look." The finishing process added about $12 per pair to the cost of a pair of premium jeans.[21] However, some washes could run to $16 per pair or even much higher. In the Sundance Channel documentary *Dirty Denim*, Chip Foster (co-founder of Chip N Pepper) points out a pair of jeans with a $25 wash made to give the appearance of having been worn extensively.[26] According to the designer, it would take approximately six years of wear to get the same look provided by the expensive wash.

Lubell dissected the manufacturing cost of a pair of $310 (retail) True Religion "Phantom" jeans for *The Wall Street Journal* in 2011.[27] According to Lubell, raw Phantom jeans cost $56 to make. Wash expenses added $6 to $16 per pair to the cost of the jeans for a total manufacturing cost of $62 to $72 for a finished pair. True Religion marked up the jeans 2.2 to 2.5 times to $140 to $160 per pair and sold them to retailers. Retailers then tacked on an additional $150 to $170 per pair to arrive at the cash register price of $310 per pair. The retail markup on a pair of premium jeans averaged 2.2 times. Through this markup process, the designers and their retail partners captured the lion's share of the profits in the industry.

The contract manufacturing model had worked well for denim designers, even though it created an opportunity for jeans cut-and-sew operators to forward vertically ntegrate into jeans design and marketing. Drawing on ts experience in manufacturing denim, Grupo Denim aunched Vintage Revolution premium jeans in fall 2010. The Mexican company was vertically integrated into pat-ern design, manufacturing, and finishing. Grupo Denim ired premium denim veteran Michael Press as CEO. Vintage Revolution debuted in 400 major department and specialty stores in the United States. Vintage Revolution jeans retailed for $118 to $140 per pair as Grupo Denim had a significant cost advantage compared with other premium jeans marketers and chose to pass on some of its savings to consumers. Despite the company's cost advantages, the line tumbled from the premium ranks to the low end of the mid-priced tier of the market—retailing for $35 to $40 per pair at Sears and other mid-priced department stores in 2013.

Outsourcing was the north in the U.S. premium denim market, but some prominent premium denim designers began to bring key aspects of the manufacturing process in-house from 2010 to 2013. Most notably, 7 For All Mankind started manufacturing operations in its Vernon, California, headquarters by bringing in-house denim cutting, embroidery and finishing. The company added sewing to the internal process in 2011. The company intended to make all of its own jeans without relying on outside contractors. "One [factor] was controlling our destiny, having more control of our process. There was some cost advantage. The other was speed to market. In today's world, we need to be quicker," said Barry Miguel, president of 7 For All Mankind.[28] 7 For All Mankind was unusually well equipped to handle the challenge of backward vertical integration as its parent company, VF Corporation, was the largest apparel company in the world and had been making Lee jeans since 1889 and Wrangler's since the 1940s. VF Corporation hoped to bring its expertise in research and development as well as enormous purchasing power to 7 to hold down cost increases and develop innovative products. VF Corporation CEO Steve Wiseman liked to say the company was the largest zipper buyer in the world.

Retailers' demand for quicker speed to market was a powerful motive for producing domestically. Peter Kim, president of Hudson Jeans, said that in 2010 he could take eight to 12 weeks to produce and ship a new style and between six to eight weeks to fill a reorder. A year later, Kim said he needed to deliver new styles in six to eight weeks and fill reorders in two to six weeks. Hudson's approach was to outsource most production tasks to companies in the LA area—all within a few miles of the firm's headquarters. Bringing all of the production process in-house would reduce the turnaround time on new products even further. However, Hudson's Kim noted that doing the entire manufacturing process in-house "was like running 10 or 12 other businesses."[29]

J Brand's approach was to share its headquarters space with an independent but captive manufacturer. It was this relationship and proximity to the factory that allowed Jeff Rudes to observe the return of colors to the high-fashion runways in Europe in September 2010 and launch a test line of brightly colored denim jeans in Barney's NY five months later. A short time later, J Brand rolled out its line of colored denim nationwide.

While it was possible for the jeans companies to backward vertically integrate into the finishing end of production, very few U.S. designers had opted to do so as it generally fell out of the area of management expertise and required meaningful capital investment. Citizens of Humanity brand was an exception as the line reportedly produced 1,000,000 pairs of jeans per year in its own denim laundry in Los Angeles.[30] Moreover, different laundries had developed distinctive skills with different types of finishes. LA's washhouses were known for their high levels of technical skill and for innovation. As industry growth slowed, more denim companies might opt for ownership of denim laundries despite the barriers to entry. The wash and other finishing treatments had become increasingly important differentiating features of premium denim lines—making keeping the finishing details proprietary critical to success. Washhouses typically did not work exclusively for one premium denim customer. While the designers endeavored to keep details about fit and finish secret, it was extremely difficult to do so given the nature of the denim laundries and their processes. Many denim designers had so far opted to stick with the traditional contract manufacturing model, but the model appeared to be changing in 2013.

Lifestyle Brands and the Diesel Model

As the ultimate in product differentiation, many companies attempt to create so-called "lifestyle" brands that transcend product category and inspire deep consumer loyalty. Three of the top five best-selling premium denim companies were attempting to transform their denim labels into lifestyle brands by emulating the Diesel model. Once thought to be the key to continued high growth, "lifestyle brand status" may have become critical to survival by 2013.

In the 2007 Touchstone movie *Wild Hogs*, the character Dudley Frank (played by William H. Macy) proudly declares; "I got a tat." He pulls down his black leather jacket to reveal a multicolored version of the Apple corporate logo tattooed on his right shoulder.[16] Dudley Frank, a computer programmer, identified so closely with the Apple brand and its core values, he chose to have it etched into his skin.[31]

Only a handful of companies had been able to establish such a strong association with a particular way of living that their brands symbolized the core values embodied in that lifestyle: Ralph Lauren, Harley-Davidson, Nike, Apple, Abercrombie & Fitch, Diesel, and a few others. Examples of failed attempts to transform regular brands into lifestyle brands abounded, such as McDonald's, Starbucks, Microsoft, and Uggs.

The appeal of the lifestyle brand was threefold: potential for sales growth, brand premiums (high margins), and protection from downturns in product cycles. Developing a strong emotional bond with consumers that went beyond product functionality could allow a company to go beyond using mere line extensions to generate growth. Lifestyle brands had the potential to move into a whole host of related product categories. In some cases, a brand could be used as a growth platform even in product categories that were seemingly unrelated to its original market due to the strength of the brand's identity with its associated lifestyle. Harley-Davidson, the motorcycle manufacturer, successfully extended its brand to a wide variety of product categories including clothing, footwear, eyewear, jewelry, Christmas ornaments, trucks, and wine bottle stoppers, among others.

The creation of a strong sense of identity with a brand by consumers also had the potential to let a company charge a premium for its products as relative prices could be less important than the consumer's relationship with the brand. In addition, diversifying into related product categories such as footwear for an apparel label could help protect a brand from downturns related to changes in fashion trends—thus reducing risk in the volatile fashion business. The measure of success in creating a lifestyle brand was the degree to which revenues and profits were diversified away from the original product line.

Within the domestic premium denim market, both of the top premium denim companies were attempting to do just that—create lifestyle brands that would allow them to move outside of the denim business. 7 For All Mankind and True Religion were attempting to emulate the Diesel brand model. Although the brand's roots were in the denim market, only about 35 percent of Diesel's revenues were derived from denim sales by 2010. Sales of products as diverse as wine, cars, fragrances, sunglasses, shoes, and watches as well as non-denim apparel generated the remaining 65 percent of revenues.[32] In addition to product diversification, the company had forward vertically integrated into wholly company-owned and partly owned (with distributor partners) retail stores around the world. It also operated a Web site that both promoted the Diesel lifestyle and sold products. The company's motto, [Diesel] "For Successful Living," and its Web site's invitation to consumers to join "the cult" highlighted the strong linkage between the brand and its customers.

Founded in 1978 by Renzo Rosso and Adriano Goldschmeid, the Italian denim company sold through 5,000 distribution points in 80 countries including 300 Diesel brand stores. With 50 stores in the United States in 2010, *The Wall Street Journal* put the privately held company's worldwide sales at $1.81 billion.[33]

Premium denim juggernaut 7 For All Mankind had taken its company-owned store count from 10 in the United States in 2008 to 65 worldwide by the end of 2012. In addition, there were 60 independently operated 7 For All Mankind partnership stores in international markets. Perhaps more importantly, 7 management recognized that the key to a successful lifestyle brand was its core brand identity. Successful luxury lifestyle brands such as Dior, Gucci, Armani, and Versace all embodied the lifestyle and values of iconic designers. In order to more clearly define its core brand identity to the consumer, 7 hired acclaimed actor and director James Franco in 2012. Franco added his fashion and directing sensibilities to 7's 2012 and 2013 advertising campaigns. Franco directed a series of films, titled "The Beautiful Odyssey," for 7 that appeared on the brand's YouTube channel.

True Religion had increased its U.S. store base from 89 in December 2010 to 86 full-priced stores and 36 outlets. The company owned another 20 full-priced stores and 10 outlets in international markets. As True Religion transformed itself into an apparel retailer, it had been successful in gaining ground in non-denim categories with its most devoted consumers. By the end of 2012, sportswear generated 35 percent of sales in True Religion stores, up from 20 percent in 2008. Nevertheless, the company had been largely unsuccessful at persuading its influential wholesale accounts to take on its non-denim offerings. The company's self-described California hippie–Bohemian chic with influence from the Wild West image appeared to have proven to be difficult to translate into a clear brand identity that could transfer to non-jeans product categories in a way that resonated with retailers and consumers. Somehow True Religion management needed to persuade its less devoted consumers that the Buddha strumming a guitar and the horseshoe stitching on the back pockets of its jeans were timeless symbols of a desirable lifestyle.

In a March 2008 interview with *Women's Wear Daily*, Diesel's Steve Birkhold said; "It will take these brands a long time to get to what Diesel already has, which is the full lifestyle. You can't go from being a flat denim brand with a huge wholesale distribution to being a lifestyle denim brand with a niche retail distribution unless you have the product engine to fuel it. That's where I think Diesel is differentiated."[34]

7 For All Mankind and the Premium Denim Market

The premium denim market was populated with fanciful brand names and was characterized by all the melodrama of the best television soap operas. Rich & Skinny, Citizens of Humanity, Earnest Sewn, True Religion, Joe's Jeans, Rag & Bone, Paige Premium, and Not Your Daughter's Jeans were some of the premium denim labels launched on the heels of 7 For All Mankind's successful debut. "7," as it was affectionately referred to in the fashion press, was the brainchild of LA designer Dahan and salesman Glasser.

Dahan was the head designer for Lucky jeans and a former designer for Guess jeans. Glasser started the sportswear brand Democracy in 1990. The two men approached Peter Koral, owner of California sportswear maker L'Koral, in 2000 with the idea of launching a new jeans line at the nearly unheard of price points of $100 to $160 per pair. In contrast, the average price paid for jeans in the U.S. market was just less than $21. More than half of the jeans sold in the United States that year retailed for less than $20 per pair. "Designer" denim had been all but dead for nearly 20 years. Nevertheless, Koral agreed to provide financial backing to the venture in return for a 50 percent ownership stake in the line.

For the first time in denim's history, designers turned their attention to creating a pair of jeans whose function was to flatter and enhance women's figures rather than to serve as durable casual wear or a skintight spot to paste a designer name for those fortunate enough to both afford it and carry it off. Dahan deconstructed the basic five-pocket jean and reengineered it with an eye toward enhancing and flattering women's bodies. He added a distinctive stitching design to the back pockets of 7s so consumers could easily identify the product and be identified with it. Dahan used a stylish bootcut coupled with a low-rise, slim-fit, high-quality denim and subtle detailing to create a one-of-a-kind silhouette. One 20-something woman commented in a 2003 *Boston Herald* industry article, "I remember when 7 jeans would pay for themselves because when you went out you'd look so good that guys would buy you drinks."[35] As Charles Lessor, the former CFO of competitor True Religion Brand Jeans, noted succinctly in the same article, "It's all about the butt."[36] 7s made a woman's derriere look great, and women rushed to stores to buy them. Celebrity trendsetters like Cameron Diaz were photographed wearing 7s in everyday life. The line's popularity exploded, and it generated an unprecedented $13 million in first-year sales accompanied by $2 million in net profits. Two years later in 2003, the brand did $80 million in sales before jumping to $130 million in revenues in 2004.

The brand's success did not go unnoticed. Los Angeles became the denim capital of the world despite the fact that North Carolina–based mega-brands Lee and Wrangler's operations were far from the glitz of the City of Angels and brand leader Levi's was headquartered in San Francisco. There was a veritable volcanic eruption in the number of premium denim brands between 2001 and 2003. According to STS Market Research, consumers purchased 297 denim brands in 2001. That number jumped to 350 in 2002 and 438 in 2003—a 47 percent increase in two years, accounting for a third of all apparel brands purchased in the United States.[37] The new brands mimicked the 7 model of in-house design, outsourcing production and finishing, using the highest-quality denim, and selling to trendy upscale boutiques and high-end department stores.

Below the surface at 7 For All Mankind, things were not going well between the partners. Dahan and Glasser left 7 and filed a $20 million lawsuit against Peter Koral in 2002. The lawsuit accused Koral of using profits from 7 to prop up his knitwear business and failing to live up to the partners' oral agreement to establish 7 as a separate entity once sales hit $12 million. Koral claimed he plowed all the profits back into the brand. Further, he maintained that his partners gave up their share of the company by leaving to start a competing product line. A judge awarded the two men $55.5 million in September 2004, $50 million for the combined 50 percent share of 7 and $5.5 million in profits from 2001 and 2002.

With $20 million in net profits on $60 million in sales in their second year of business, it is no wonder that Dahan and Glasser immediately applied their expertise to creating another premium denim brand. The two started Citizens of Humanity in 2002 using the same general business model that had served them so well with 7 For All Mankind. Glasser focused his merchandising and marketing efforts on the same accounts he did business with at 7 like Nordstrom, Barney's, and Neiman Marcus. Dahan updated his designs and added new washes and detailing.

Citizens had an even bigger first year than 7 due to soaring demand for high-priced denim. In 2003, the line generated $23 million in sales. Sales leaped to $80 million reportedly accompanied by a whopping $35 million in profits in 2005. The brand sold in 35 countries with about 90 percent of its revenues coming from the sale of women's jeans. Dahan bought out his partner in 2005 and then sold 66 percent of Citizens to the Boston venture capital m Berkshire Partners in 2006. According to press ac-unts, the majority stake in the privately held firm fetched 50 million to $300 million or 3.8 to 4.5 times estimated 06 sales of $100 million. With the backing of Berkshire rtners, Citizens purchased GoldSign jeans from Adriano oldschmeid along with his denim laundry in 2007 for an ıdisclosed sum.

In March 2005, Peter Koral sold 50 percent of 7 For l Mankind to the investment bank Bear Sterns. Although ecific terms of the deal were not disclosed, Mr. Koral nfirmed publicly that Bear Sterns paid $75 million to 00 million for its stake in the firm. The brand had sales about $200 million in 2004 so the deal was valued at 75 times to 1.0 times sales. The buzz on Wall Street was at the line had the potential to morph into a large global 'estyle brand. Denim giant VF Corporation picked up all 7 For All Mankind in mid-2007 for a cool $775 million. ıe maker of Lee, Wrangler, and Rustler jeans pegged 2007 les of the #1 premium denim brand at about $300 million, ıluing the brand at nearly 2.6 times sales.

'F Corporation and 7 For All Mankind

F Corporation was the world's largest apparel company ith 2012 revenues of $10.8 billion. The company began ı 1899 as a glove and mitten manufacturer but diversified ıto women's silk lingerie in 1914. The company retained ıe initials "VF" after dropping the Vanity Fair moniker ollowing the acquisition of Lee jeans in 1969. Lee was one f the oldest apparel brands in the United States, having een established in 1899 (about 25 years after Levi Strauss). 'F went on to acquire Wrangler and Rustler as part of s friendly acquisition of Blue Bell in 1986. In 2007, VF Corporation acquired 7 For All Mankind, the leading pre-nium denim brand in the United States.

VF Corporation adopted a new corporate strategy n 2004. Its vision was to "grow by building leading life-tyle brands that excite consumers around the world."[38] n other words, the company wanted to transform itself nto a global lifestyle apparel company with 60 percent of evenues being derived from lifestyle brands by 2015. As part of that initiative, it sought to stay on top of the ap-parel market by combining design and science to create alue-added products for consumers. According to com-pany statements, "innovation is about much more than delivering a new product, fabric, or style...Innovation s a holistic process, one that touches every aspect of our nterprise—branding, supply chain management, global xpansion, even our corporate citizenship initiatives."[39] Management saw growth in lifestyle brands, an increase in company-owned stores, and international expansion as keys to longer-term success. In particular, VF Corporation planned to double the number of company-owned stores and increase its product mix to 60 percent lifestyle brands by 2015. By the end of 2012, VF owned 1,129 stores around the world, including 1,049 single-brand stores. Direct-to-consumer sales accounted for 21 percent of global revenues.

VF had massive global operation in which it man-aged 450 million units across 36 brands in nearly every country in the world in 2012. Unlike many of its competi-tors, VF used a mix of 29 company-owned-and-operated manufacturing facilities and 1,900 contract manufacturers. As is noted in VF's 2012 10K filing, company-owned facili-ties in the western hemisphere generally delivered lower-cost product, but contractor-sourced goods offered more flexibility and shorter lead times. As a result, VF balanced the need for lower-cost manufacturing costs with the abil-ity to hold lower inventories resulting from the use of contractors. In addition to global sourcing of raw materials and manufacturing, the company used "best of class" tech-nology to manage its resources. Best of class technology extended to inventory management at the retail level. VF employed a point-of-sale inventory management system that allowed it to gather daily sales information down to the individual store and SKU level (size, style, color detail). The company believed this point-of-sale inventory system gave it an advantage over its less sophisticated competi-tors. Its five largest customers accounted for 16 percent of 2012 sales and were all located in the United States. The company's single largest customer was Wal-Mart, which accounted for 8 percent of 2012.

The company's brands were organized into "coali-tions" including jeanswear, outdoor, imagewear, sports-wear, and contemporary. The jeanswear coalition was made up of the so-called "heritage brands" Lee, Wrangler, and Rustler. VF management felt the jeanswear and image-wear (licensed and work apparel) coalitions would likely generate strong profits and cash flow with low-single-digit growth longer term. The outdoor, sportswear, and con-temporary coalitions were to be the growth engines of VF in management's view. These lifestyle brand groups were expected to grow at a mid-single-digit to low-double-digit rate in the long term.

7 For All Mankind was placed into the newly cre-ated contemporary group in August 2007, which also in-cluded the recently acquired lucy[R] brand. When acquired in August 2007, domestic sales accounted for 75 percent of 7's total revenues. By the end of 2012, international rev-enues had jumped to 37 percent of brand sales. While some of the increase was due to VF Corporation's aggressive

expansion in international markets, the U.S. business had suffered due to the recession and slumping premium denim industry sales. 7 For All Mankind's large share of the premium segment made it difficult for the brand to outperform the category.

Nevertheless, 7 appeared to be struggling to maintain its position in the market as it lost ground to the likes of True Religion and J Brand, and the premium denim category recovered. VF Corporation had taken a nearly $200 million impairment charge to the 7 brand in 2010—indicating that the asset was no longer worth the $775 million that the company paid for it less than three years earlier. At VF's June 2013 Investor Day, management stated that 7's 2012 total revenues came in at $300 million[40]—putting the brand's revenues at about the same level as estimated 2007 revenues.

While management expected an average of 7 to 8 percent annual growth through 2017, first-half 2013 results were discouraging. 7's revenues fell in the second quarter reportedly due to softness in the high-end department store channel. Management revised its 2013 growth forecast to "low single digit growth" from "high single digit growth" as 7's revenues fell 5 percent or more in the quarter.[41] Recent results raised questions about the relevance of 7's brand to premium denim consumers and the likelihood that the brand could make the jump to lifestyle status

A strong competitor in all of its markets, the North Carolina–based VF Corporation spent $575 million on advertising and promotions in 2012. The company possessed a formidable stable of brands including Timberland, North Face, Nautica, Vans, Reef, and Majestic. As of June 2013, the company had $320 million in cash and $1.9 billion in total debt. Shareholder's equity stood at $5.2 billion.

VF Corporation Acquires and Repositions Rock & Republic from Super Premium to Mid-Priced

VF picked up the assets of rival premium denim label Rock & Republic out of bankruptcy in March 2011 for $58.1 million. Notably, VF did not retain the services of the brand's flamboyant founder, Michael Ball.

According to company press, Rock & Republic "transcends the denim world with its luxe yet edgy approach to fashion." Its first collection "mixed an edgy, rebellious style with sophistication," which "inspires music and fashion industries alike." The company paired with Victoria Beckham (Posh Spice) to create signature jeans marketed under the Rock & Republic brand name, but the relationship soured and was dissolved. Co-founded by Ball and Andrea Bernholtz in 2002, Rock & Republic retailed its premium denim jeans for $186 to $330 per pair. The privately held company had become something of a force in the premium denim market by appealing to the fickle tastes of the most fashion-forward, affluent young consumers. Rock & Republic was all about trendy and fast. Nevertheless, the company moved in sync with the rest of the premium denim segment away from embellished jeans to cleaner and less provocative styling and raised its waistlines in 2007. Company co-founder Bernholtz commented to *Women's Wear Daily*, "It's [the rise is] just not as low as it was before with everything hanging out. It's that quarter of an inch between sexy and slutty."[42]

Rock & Republic reportedly did $2.4 million in sales in 2002 and about $23 million in 2004. Ball claimed the company did more than $100 million in sales in 2006. The outspoken Ball said he had a plan that would allow Rock & Republic to "literally dominate our market in the next fifteen years."[43] Ball's plan revolved around transforming Rock & Republic into a full-line lifestyle brand including shoes, eyewear, and retail store ownership.

While it was easy to dismiss the outspoken Ball as an insignificant player in the denim market, Rock & Republic's success with the fashion-forward consumer had other companies looking over their shoulders. The jeans featured a distinctive, stylized "R" on each back pocket, high-quality denim, and a flattering fit. The brand commanded even higher price points than True Religion, and consumers appeared willing to pay them. As Ball told the *Daily News Record* in a 2006 interview, "If you want Rock, you have to pay top dollar—you have to pay to be in the VIP section."[44] Ball's view of the brand's cache may ultimately have been its downfall as the company was forced to file for bankruptcy in 2010.

VF Corporation quickly moved to reposition the line and take advantage of its appeal to fashion-forward consumers. In April 2011, VF announced that Rock & Republic would be available exclusively in Kohl's department stores. The line launched in Kohl's 1,150 mid-priced family-oriented U.S. stores in spring 2012. According to the company's fact book, 52 percent of the company's $4.2 billion in revenues were derived from exclusive brands like Rock & Republic. The retailer's objective was to "continue to offer exceptional value, quality, and convenience."[45] Rock & Republic women's jeans retailed for $88 on Kohl's Web site but were regularly sale-priced at $49.99 or below. Details on Rock's first year as a mass-market brand were not available, but Kohl's management seemed pleased with the line's performance.

Joe's Jeans

Moroccan-born Joe Dahan (no relation to Jerome Dahan of 7 and Citizens fame) entered the fashion business with a line of men's formal wear and dress shirts in 1986 that rang up $8 million in sales when Joe was just 17 years old.[46] From 1996 to 2001, Dahan was the head designer for Azteca Productions, a private-label manufacturer of sportswear and denim. Dahan entered the premium denim market in 2001 with five styles of fashion jeans under the Joe's Jeans brand. The products retailed for $124 to $155 per pair. In March 2001, Innovo Group purchased the rights to the Joe's Jeans brand from Azteca and moved into the premium denim market. Innovo later changed its name to Joe's Jeans and trades on the NASDAQ market under the JOEZ symbol.

Joe's Jeans emphasized fit rather than the hottest trend. As Dahan said in a 2005 interview, "We've always been about clean, even when the market was embellished. We're not about fast or trendy."[47] Joe's Jeans aficionados sang the praises of the line, claiming the jeans had an "insanely good fit." Dahan's attention to fit paid off with first year sales coming in at $9.1 million. The line retailed at tony department stores like Barney's New York, Nordstrom, Bloomingdale's, and Macy's as well as boutiques catering to affluent shoppers. The company's 10 largest customers accounted for 61 percent of sales in 2012. Nordstrom, Bloomingdale's, and Macy's were Joe's three largest customers. In 2009, the three together accounted for 47 percent of sales. Joe's, like its larger competitors, had moved to open its own retail stores in order to boost margins and reduce its dependence on upscale department store retailers. By the end of 2012, Joe's owned 11 full-priced retail stores and 19 outlet stores in the United States. Total sales rang up at more than $118 million in 2012 with about 95 percent of sales derived from the U.S. market.

Joe's took two major steps to improve its position in the U.S. market in 2012 and 2013. Hedging its bets on premium denim, the company launched an exclusive line else™ sold primarily by Macy's. The new line was priced at $68—putting it squarely in the mid-priced segment of the jeans market. From February to December 2012, else™ generated about $7.5 million in sales. In July 2013, Joe's announced it had reached an agreement to purchase premium denim brand, Hudson for about $98 million. Marc Crossman, president and chief executive officer of Joe's Jeans, stated, "We are extremely excited about joining forces with Hudson Jeans. Once the acquisition is complete, we expect to nearly double the size of our business, meaningfully increase our international and e-commerce penetration, and enhance our overall prospects for growth."[48] Crossman went on to say that he expected to be able to leverage the company's sourcing capabilities to realize cost savings and significantly reduce input costs. With the addition of Hudson, Joe's became a more formidable competitor in the premium denim industry.

True Religion Brand Jeans

Lubell had struck out on two occasions previously in his attempt to shift from textile salesman to independent jeans designer. He and his wife launched two jeans labels in the late 1990s—Bella Dahl and Jeffri Jeans—and lost both after running out of cash. Events turned ugly when Bella Dahl Inc. couldn't keep up with payments to its factory and had to file for bankruptcy in late 2000. Several lawsuits later, Lubell was on his own with no assets or ownership in his jeans creations. In 2002, the Lubells launched a new premium denim line, True Religion Brand Jeans. Lubell registered his new line's trademarks in his name and formed a holding company that he owned and controlled called Guru Denim. Things would turn out differently this time for the 46-year-old Los Angeles resident.

The brand hit store shelves in December 2002 with five styles of women's jeans available in five different "washes" under the True Religion label. (7s were only available in two basic styles at the time.) The corporate logo appeared on every tag and featured a fat, smiling Buddha strumming a guitar. According to a November 2002 *WWD* article, "True Religion has an "evolutionary" mannish styling." *WWD* interviewed Lubell for the article and quoted him as saying "there are a lot of women who love to wear their boyfriend's jeans or husband's jeans. This plays off of that." The jeans had one of the lowest rises on the market and some of the highest prices. Lubell created "buzz" for the line by sending celebrity trendsetters free pairs of jeans with the hope they would appear in photos in the popular press wearing jeans with True Religion's signature horseshoe-shaped back pocket stitching. The strategy worked, and the line's sales took off. First-year sales came in at $2.4 million and jumped to $27.7 million in 2004.

The popularity of "distressed," "destroyed," and "embellished" jeans helped drive growth in the premium denim segment for years. The Joey Destroyed model had been one of True Religion's best-selling products. The jeans model featured pre-washed denim that had been artfully aged and ripped so that most of the front of the left thigh was made up of strings rather than solid fabric. The designers added in a ripped left knee and extensive tearing on the front of the right thigh to complete the destroyed look (an extreme version of distressing). Embellished jeans also had been very popular for a number of years in the early part of the product lifecycle. So-called embellishments ranged from elaborate embroidery to the addition of sparkly crystals and metallic threads. True Religion marketed women's jeans with intricate embroidery on the back pockets like the Miss Groovy, Buddha, Fairy Girl, Godiva, and Geisha Girl designs. All of these popular "looks" required a substantial amount of additional labor to produce relative to basic denim looks. They all commanded a significant premium to the more basic models in the True Religion portfolio with prices starting well above $200 per pair. Some True Religion models went for more than $500 per pair at retail.

In 2008, premium denim designers responded to the mood of the times and moved away from elaborate finishing details back to more basic styles as consumers became interested in styles that would stay fashionable for years rather than for a season. True Religion followed suit and emphasized the lower-priced, more basic items in its lineup. Nevertheless, the brand remained one of the highest priced on the market with an average selling point of $196 for women's jeans and $192 for men's jeans in 2009. In company-owned stores, True Religion's price peaked at a staggering $272 per pair in the first quarter of 2009. The company had not been as successful historically in the basic end of the premium market as had 7 and Citizens. Indeed, True Religion's wholesale sales plummeted 20 percent during 2009 and 15 percent in 2010, followed by an 18 percent drop in 2011.

The company relied on Lubell's fashion sense and ability to spot the right trends to sell the "hottest" jean styles. He occupied the unusual position of CEO and "chief merchant" at True Religion. Lubell had an impressive track record, but True Religion's sales to the wholesale off-price channel had become worryingly large by 2009. The company used off-price retailers such as Nordstrom Rack as well as its own outlet stores to sell slow-moving and obsolete inventory. Moreover, the recession and a series of fashion missteps cost True Religion some of its followers. Lubell initially dismissed skinny jeans as a fad and was slow to introduce a True Religion version of the popular pants. Lubell considered True Religion to be a trendsetter rather than a follower. After all, he pioneered the incredibly popular oversized stitching on jeans as well as the ultra-destroyed look among others. According to Diana Katz, an analyst at Lazard Capital, "He thought they'd trend back to bell bottoms and wider bottoms, but it never happened."[49] Similarly, Lubell missed the colored denim trend and refused to lower prices on True Religion products. After a lot of sales pressure, Lubell rolled out a lower-priced line of simpler, cleaner jeans with a small, unobtrusive logo on the back pocket. True Religion consumers did not respond well to the line as part of the appeal of the brand lay in its garish oversized back-pocket stitching and instantly recognizable logo. Moreover, the jeans were priced at $230 compared with $150 for similar jeans from competing brands. The line was discontinued.

True Religion planned to introduce a new "core denim" assortment in 2013 and increase the differentiation between its women's and men's jeans. While True Religion had struggled in the women's denim segment, the company's men's line held its own from 2009 to 2012. The company made three other key changes in 2013. It shifted some design responsibilities for its European business to Europe from California and began a consumer preference study. The company expected the study to give it insights into consumer purchase behavior that would allow its designers a greater opportunity to spot promising fashion trends. Finally, Lubell stepped down as the company's chief merchant and CEO in March 2013. Lubell would remain a creative consultant to True Religion but would no longer be responsible for its designs and operations. In this way, True Religion's board hoped to avoid the fate of Rock & Republic and reinvigorate the brand.

True Religion's Strategy

The company's initial strategy was to emphasize distribution through upscale department stores and boutiques and outsource every function except design and marketing to third parties. By the end of 2005, True Religion jeans sold in about 600 specialty stores and boutique shops as well as about 200 upscale department stores. Its customer lineup was a "who's who" of upscale retailers including Nordstrom, Neiman Marcus, Saks Fifth Avenue, Barney's, Henri Bendel, Bergdorf Goodman, Bloomingdale's, and Marshall Fields. By late 2006, True Religion's focus had shifted away from selling products wholesale to selling its products through company-owned stores.

True Religion management, under then-President Michael Buckley, had started to vertically integrate into retail for several reasons. First, the company had faced resistance from retailers when it tried to diversify away from denim jeans into adjacent clothing categories such as sportswear. Big retailers viewed True Religion as a denim label—not as an apparel brand. Owning its own stores allowed True Religion to introduce a broader range of apparel to its customers. Management hoped that the sell-through figures from company-owned stores on non-denim items would persuade its retail accounts to carry the full line of True Religion apparel. Diversifying into other apparel categories and related product lines was absolutely critical to achieving management's goal of creating a lifestyle brand.

In its full-priced company-owned stores, sales of non-denim items had increased from 10 percent of sales to 35 percent of sales in six years. However, non-denim items only accounted for an estimated 20 percent of the company's total U.S. sales, as True Religion largely had been unable to persuade its retail accounts to carry its non-denim items. Moreover, the company's licensing revenues were a puny $2.7 million in 2012—down from more than $5 million in 2010. Licensing was critical to establishing a lifestyle brand especially for a relatively small company with specialized management expertise. In order to expand into non-apparel categories, True Religion needed partners—partners that would manufacture and market True Religion–branded fragrances, sunglasses, jewelry, watches, and any other products that fit with True Religion's brand image.

Second, the margins in the company-owned stores were even higher than True Religion's very high denim margins as the company captured the retail markup as well as its traditional wholesale markup. Management estimated that retail store gross margin would come in at 75 percent and "four-wall contribution margin" would be about 40 percent as the company captured the benefits of the typical retail markup on its products as well as existing wholesale margin. Third, company-owned outlet stores gave True Religion a place to sell seconds, irregulars, and slow-moving merchandise. Without these outlet stores, True Religion brand products could surface in any type of discount outlet—potentially damaging the brand's premium positioning. Prior to 2007, True Religion jeans appeared in Filene's Basement, Costco, Century 21, and similar outlets on occasion.

Fourth, retail industry mergers and bankruptcies periodically caused manufacturers to miss sales and earnings forecasts. Using company-owned stores helped reduce the firm's dependence on retailers and reduced the risk of major disruptions in sales. Company-owned stores and e-commerce accounted for 60 percent of revenues in 2012 compared with 17 percent in 2007. In total, True Religion owned 122 stores in the United States and 30 international stores at year-end 2012. Over time, management planned to open 100 stores in the United States. Nordstrom and Nordstrom Rack remained True Religion's most important retail account. While 2012 figures were unavailable, Nordstrom alone accounted for 15.2 percent of the company's net sales in 2009.

As True Religion expanded the number of company-owned stores, its retail business took off—growing 57 percent per year on average for the five years ended December 2012. Operating profit before unallocated corporate expenses grew at a slower rate but nonetheless averaged 51 percent per year growth over the period. At first glance, it was difficult to understand how the company could have been characterized as "struggling" and in need of a "savior." Investors were focused on four issues: the sharp slowdown in growth in the U.S. direct-to-consumer business (company-owned stores) and the accompanying huge drop in gross profit margin for the segment, the persistent weakness in wholesale sales especially in women's jeans, and the collapse in profits from international markets that occurred despite strong sales growth in those markets.

Some of the slowdown in the direct-to-consumer segment growth in the United States was attributable to the law of large numbers. As the business became larger, it took a greater and greater amount of incremental sales in absolute dollars to generate the same sales growth rate. In 2009, the direct-to-consumer business reported a 71 percent jump in revenues to $129 million or an increase of about $54 million. The same $54 million increase would have resulted in only 21 percent growth in 2012 as the business had nearly doubled to $251 million. Nevertheless, investors were concerned when the high-flying direct-to-consumer business reported a mere 12 percent increase in revenues despite almost a 12 percent increase in the total number of stores owned. The company's same store sales (sales in stores open for 13 months or more) were up 2.7 percent for the year.

At the beginning of the retail store expansion plan, then-company President Buckley estimated that retail store gross margin would come in at 75 percent and "four-wall contribution margin would be about 40 percent as the company captured the benefits of the typical retail markup on its products as well as existing wholesale margin. For the first few years of the expansion, management's prediction turned out to be an accurate one as gross margin for the consumer direct segment (company-owned stores and e-commerce) leaped to a peak of nearly 77 percent in 2008 before dipping to 74 percent in 2009 and ending up at about 70 percent in 2012. Similarly, segment operating profit margin before unallocated corporate expense plunged from a peak of 40.6 percent in 2007 to 33.3 percent in 2012. Some of the dropoff in profit margins was attributable to the costs of rolling out so many stores in a relatively short period of time. However, most of the decline in profitability was a result of two factors: an unfavorable mix shift toward sales in outlet stores and the overall decline in average denim prices paid in the company's stores. Both factors suggested the underlying appeal of the brand was waning among the fashion-forward affluent crowd True

Religion had wooed so assiduously for the past decade. More shoppers looking for True Religion jeans in outlet stores was likely a result of fewer shoppers being willing to pay up for jeans priced above $200 per pair, in line with industry trends toward lower-priced jeans. The fashion missteps that had plagued the company over the past few years had forced True Religion to discount more of its product line to move the product. Exhibit 4 below shows the decline in average prices paid by consumers for True Religion Jeans (excluding sportswear) in company-owned stores from their peak in the first quarter of 2009 through the fourth quarter of 2012.

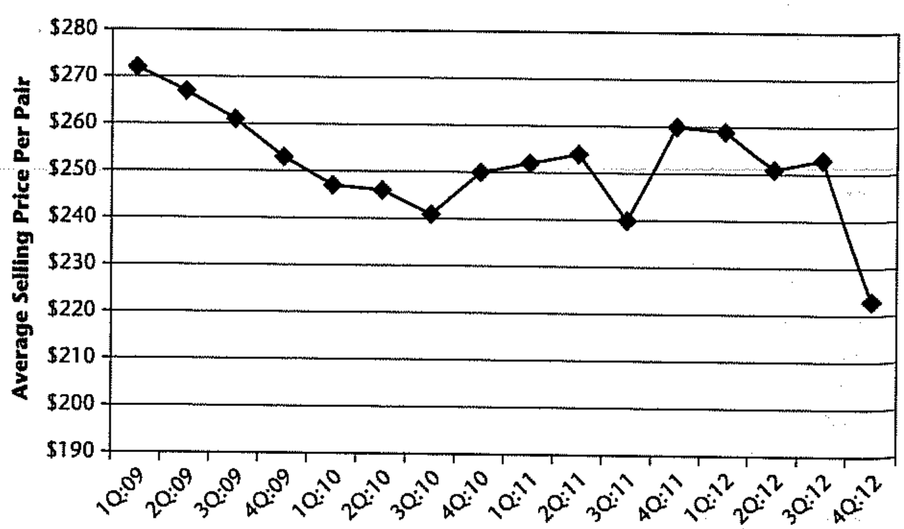
At the same time, company-store growth appeared to be fueled mainly by store expansion and discounting, True Religion's wholesale business had increasingly shifted away from full-line department stores toward off-price channels. In recent quarters, shoppers had gravitated to the most heavily discounted True Religion items in off-price stores. The combination of all of these factors had investors spooked as concerns about the underlying health of the brand came to the forefront. One bright spot for the brand suggested it had not yet lost its cache. Sales to the specialty boutique channel had increased for 11 straight quarters. Much of the brand's success in its early days was due to the endorsement of specialty boutique owners. Improving sales trends with these savvy buyers could signal that the brand was regaining its momentum in the U.S. market.

True Religion's brand positioning as a "Made in the USA" product based upon a unique combination of a Wild West, cowboy heritage paired with a California-hippie-bohemian image had played well in international markets, especially in Japan during the brand's early days. Affluent Japanese consumers paid top dollar for American icons like vintage Levis. True Religion capitalized on its American origins by purchasing its high-quality denim fabric from Cone Mills and using domestic contract manufacturers and LA washhouses to finish its jeans. Management felt the "authenticity" of an American-made jean was a critical aspect of the brand's image—particularly in international markets. Eric Beder, an analyst with Brean Murray, told the *Los Angeles Times* in 2009, "In the U.S., people care that their jeans are manufactured here. To consumers outside the U.S., it's crucial... In order to be considered a real premium brand, you need to have the Made in the USA label on it."[50] True Religion offshored production of non-denim items such as hoodies and T-shirts, where country of origin was not important to consumers.

An enormous disappointment in Japanese sales in 2006 prompted management to reconsider the distributor model. Full-year sales to Japan plunged 50 percent from about $30 million to about $15 million. True Religion fought accusations from the financial press that it had "stuffed" the Japanese retail trade with product in the back half of 2005 in order to meet aggressive sales forecasts. Management's analysis of the retail distribution for the brand in Japan suggested that the company needed to pull back and eliminate marginal accounts in order to preserve the brand's exclusive image. As a result of the lessons it learned in Japan, management decided to switch from a distributor model to company-owned subsidiaries or joint ventures in order to better control the brand's retail placement and image. While distributors still accounted for a large part of True Religion's international sales in 2012, the company began to transition in 2008 from a wholesale business to a retail business following

Exhibit 4 Average Price/Pair Company-Owned Stores

Sources: True Religion quarterly management comments and author's estimates.



the pattern it used in the U.S. market. True Religion operated 20 full-priced stores and 10 outlets in international markets at the end of 2012.

International sales growth came in at a strong 26 percent average annual rate for the five-year period ended December 2012. Operating profits were about $15 million in 2007 and rose to a peak of about $25 million in 2009. The company's wholesale business struggled even as its retail business (company-owned stores) gained traction in key international markets. International operating profits declined sharply to about $7 million in 2012 as the company rolled out its retail stores and established in-house sales forces in many international markets. Selling, general, and administrative expenses for the international division climbed 121 percent per year on average over the five-year period. SG&A jumped 38 percent in 2012 alone. Management asserted that the increased expenses were needed to establish its retail business in international markets. Investors impatiently awaited improved international profits and margins.

Management Changes and the Future of True Religion

The company named denim industry veteran Buckley to the newly created post of president in April 2006. Buckley was president and CEO of Ben Sherman's North American business from 2001 to 2005. Prior to 2001, Buckley served as a vice president of denim giant Diesel USA for four years. He was to be responsible for day-to-day operations, including retail expansion, licensing, sourcing, and production. Lubell would remain in his post of chairman and CEO but devote more of his time to product design. Lubell commented to *WWD*, "Now I feel like I have a true partner and associate to help build the company and realize my vision of becoming a $1B brand."[51]

In August 2006, the company tapped Levi Strauss Europe designer Ziahaad Wells to be its design director. The following March, True Religion named Peter Collins as CFO. Collins was the former corporate controller for Nordstrom. Collins managed a staff of 100 and was an expert on compliance with Sarbanes-Oxley requirements. In addition, Collins had valuable accounting experience in international operations. He reported to Buckley in his new position at True Religion. In January 2010, True Religion added Lynn Koplin as COO. Koplin was formerly president of Tommy Bahama's women's division.

True Religion's financial performance generally was strong between 2006 and the first quarter of 2009. The company was well on its way to establishing 100 company-owned stores in the United States. The True Religion brand appeared strong at the #2 position in the U.S. market. Then, in May 2010, Buckley abruptly resigned from the company. Two days before his resignation, Buckley sold more than 193,000 shares of stock. The company offered no explanation for Buckley's resignation and promptly replaced him with Mike Egeck about two weeks later. Egeck had served as the CEO of 7 For All Mankind. Four months later, True Religion reported disappointing sales and earnings and lowered its full-year 2010 forecast. The timing of Buckley's departure and the speed at which he was replaced suggested Lubell was aware that Buckley planned to leave—or had forced him out. As chairman and CEO, Lubell had an enormous amount of influence with the company's board of directors. Egeck left True Religion to "pursue other opportunities" in August 2011. Egeck was reportedly "poached" by Hurley to become its CEO. True Religion promoted Koplin to replace Egeck. Koplin now succeeds Lubell as the company's interim CEO.

True Religion's strategy and objectives had been clear under the guidance of Lubell and Buckley. The company stuck to its approach of adding retail stores and transforming itself into an upscale purveyor of its own brand under Egeck and after his departure. Although neither Lubell nor Koplin had publicly commented about the Lubell's long-standing objective of reaching $1 billion in sales, the company's actions demonstrated that it pursued "lifestyle" brand status for the denim label. It was not clear in July 2013 that the company's sale to private equity firm TowerBrook would enhance its position in the premium denim industry. Always a strong cash generator, True Religion had not suffered from a lack of capital to fund its expansion plans. Nevertheless, the sale did afford the company an opportunity to bring in fresh management and design talent while giving Lubell a graceful and profitable exit from the company. Would TowerBrook prove to be more patient than institutional investors? Would new ownership give the team at True Religion more freedom to experiment with design out of the public spotlight? Could True Religion regain its "must have brand" status in the important U.S. premium denim market, or would the brand be forced to reposition itself at lower price points to survive? Lubell's tenure as chairman, CEO, and chief merchant had been an eventful and profitable one. What would Lubell do now with his $25 million golden parachute from the sale of True Religion?

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