



Game Change Conference

CONSUMER & RETAIL 2016

*A recap of Privcap's inaugural
consumer and retail conference*

Privcap/Report

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David Snow

Co-founder & CEO

Gill Torren

Co-founder & President

Marketing & Sales

Michelle Diller

Director of Marketing & Events

Scott Pestronk

Sales & Client Relationships Coordinator

Erin McDonald

Marketing & Events Coordinator

Content

Matthew Malone

SVP, Content & Digital Strategy

Andrea Heisinger

Editor

Production & Design

Rachel Shim

Production & Design Coordinator

Benjamin Asbell

Production & Design Assistant

Nathan Pardee

Video Production Manager

Jake Hard

Production Assistant

Contacts

Editorial

David Snow / dsnow@privcap.com

Matthew Malone / mmalone@privcap.com

Andrea Heisinger / aheisinger@privcap.com

Sponsorships & Sales

Gill Torren / gtorren@privcap.com

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About Privcap

Privcap is a digital media company that produces events and thought-leadership content for the global private capital markets. Privcap offers communications services to market participants.

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David Snow

CEO & Co-founder,
Privcap

Consumed With Disruption

Privcap Game Change: Consumer & Retail 2016, a debut event, brought together private equity investors, institutional investors, and executives from the consumer sector, all of whom are hyper-aware of one thing—massive technological disruption.

Disruption is raining down on giants like Amazon, which controls more and more of consumer spending every day and is disintermediating nearly all retail outlets. Disruption is bubbling up from new venture-backed competitors that continue to find staid sectors, like mattresses (see Casper), where a higher degree of customer service can quickly win loyalties and upend the established order of brands.

It's no surprise, then, that to brands relying on old methods to sell and communicate with their customers, the future looks terrifying. And even technologically savvy companies worry about keeping up with the pace of change.

Private equity and venture capital are uniquely positioned to help legacy players compete and adapt to changing consumer buying preferences. Private capital can not only back the Caspers and Warby Parkers of the world but also go after slow-moving market dominators. What's more, there was a strong sense among delegates at the event that this opportunity to invest in disruption is only in the third or fourth inning. As always, the smart money is playing the long game.

Enjoy the report,

David Snow
@SnowsNotes

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What You Missed at

Privcap Game Change:

CONSUMER & RETAIL 2016

A roundup of notable thoughts from the event's panels

Our inaugural private equity consumer and retail conference, Privcap Game Change: Consumer & Retail, was a great success. The event, held October 19th at the Marriott Marquis in New York, drew nearly 200 delegates, including consumer executives and entrepreneurs, investment advisors and fund-of-funds, and private equity fund and investment managers.

The day featured a series of panels, one-on-one interviews, and breakout sessions to discuss the challenges, opportunities and disruption facing consumer brands today, and how private equity and venture capital

firms are helping address them.

Among the topics: how consumer-facing companies can tap new geographies and new demographics; how data can help companies maximize revenue; and a “smackdown” discussion on the differences—and similarities—of millennials and baby boomer generations, and how those in the consumer industry can capitalize on their spending habits.

It was clear that no matter what the sector or target demographic, consumer brands need to keep up with disruptors and innovators, or get lost in the shuffle.

Here's what some of the expert panelists had to say:

“Prepare for a successful strategic exit—that's the holy grail for us. If you expand globally, it also grows the pool of strategic buyers.”

– **Irena Blind**, principal, TSG Consumer Partners, as part of the panel on the “Key to Growth in New Markets” panel.



AUA's Unanue, Swander Pace's Mark Poff, and TSG's Blind onstage at the event.

“With family-owned companies, distance creates barriers and fear.”

– **Andy Unanue**, a managing partner at AUA Private Equity Partners, on the challenges of getting some businesses to expand geographically. Unanue was on the “Key to Growth in New Markets” panel.

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“Harry’s was going to come out with a woman’s razor. We said, ‘Don’t.’”

– Keynote interview **Mike Duda**, managing partner of creative and investment agency Bullish Inc., on advising the men’s shaving product company it invested in how not to expand its customer base.

“They need immediacy. They need to be immediately satisfied. They need transparency. They have brand loyalty—they’re just looking for different things.”

– **Karen Kenworthy**, a partner at Stripes Group, weighing in on what millennial consumers want as part of the “Generational Smackdown: Millennials vs. Baby Boomers” panel.



“If you put a dollar in front of a CMO [chief marketing officer], how do you know what the return on that chopped-up dollar is? You don’t, because there are so many [marketing] channels.”

– **Eric Roth**, managing director and consumer group lead at Lazard Middle Market LLC, as part of the “Generational Smackdown” panel.



“Most retailers, when they acquire a customer—it takes two to three transactions to break even.”

– **Artem Mariychin**, co-founder and CEO of data company Zodiac, speaking on the “Consumer Big-Data Breakthrough” panel.



Physical Risks in Retail

The cloudy outlook for physical retail means investors should look for consumer companies that sell "experiential" offerings

■ PHYSICAL LOCATIONS REQUIRE CAREFUL SCRUTINY

When considering an investment in a retail business with physical locations, very specific due diligence is required to ascertain the health of the stores. Key metrics include "capture rate" (the percentage of people walking into the store versus walking by) and "in-store conversion rate" (those who actually make a purchase).

■ BE DIGITAL FIRST

Entrepreneurs thinking of launching a consumer brand should start sans stores and begin building a direct customer relationship online. Physical locations can then be gradually added, and there should be a big focus on service.

■ EXPERIENTIAL RETAIL IS WINNING

Given how easy it is to have products and services delivered to consumers online, it is important for retailers to focus on creating a unique experience in their physical stores. This gives restaurants an advantage over drugstores.



Anand Philip
Senior Managing Director,
York Capital



Frank Fazzinga III
Managing Partner,
Grace Beauty Capital

Why an Online Presence Is Crucial for Direct-to-Consumer

If you're going to cut out the middle man, you need to make that connection with the customer

■ IT IS POSSIBLE TO BEAT AMAZON

Direct-to-consumer businesses are never going to beat Amazon on price, so they need to sell the experience. DTC companies should also realize that Amazon is great for customers seeking out what they already know they want, but not so good for customers who need help in deciding what they want.

■ SOCIAL MEDIA IS KING IN DTC MARKETING

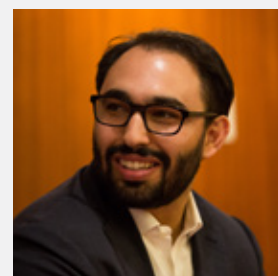
In order to maximize the DTC revenue stream, social media is your friend. The irony is that when a smaller company wants to get bigger, it can take more chances and be less cautious in figuring out what works, but as the company grows, its social media output becomes more cautious.

■ HAVING RELIABLE DATA IS THE GAME CHANGER IN DTC MARKETING

Penrose Hill will not do any marketing that the company cannot reliably track for results and key learnings. That is why social media and online platforms are so important; radio and print efforts are difficult to measure.



Philip James
Founder & CEO,
Penrose Hill



Gregg Rubin
General Partner,
Polaris Founders Capital



A Plus-Sized Turnaround

With the plus-sized fashion retailer on the brink of a second bankruptcy in three years, James Rhee became CEO. In a keynote interview, he told Privcap CEO David Snow about his wildly successful growth strategy.

James Rhee
Executive Chairman, CEO,
Ashley Stewart

Without any experience running a retail chain or as a chief executive officer, James Rhee decided to gamble.

“We bet the farm on just loyalty,” says the executive chairman and CEO of Ashley Stewart, and founder and president of FirePine Group, which was founded in 2009 to invest in special situations requiring structured capital and operational catalysts, with a focus on the branded retail-consumer product industry. He explained that he saw the potential in a business

“One of the major bloggers in plus-size says that ‘James, inside he’s a plus-sized African-American woman.’ To me, that was about as high a compliment as I could get. That means I understood the customer and I was being a fiduciary for the customer.”

– James Rhee, Ashley Stewart

that was a rare boutique-style store for plus-size women with locations in urban neighborhoods.

“We personalize the brand,” Rhee says. “We have people talk to the brand in the store as a person, so our store managers are called ‘Ms. Ashley’ in a lot of our communities. Every customer on social, it was like she’s talking to Ashley Stewart.”

In the beginning, the company would respond to every social media post personally, but Rhee says it’s getting harder now because of the brand’s popularity. “The strategic goal from week one was we were going to be this woman’s best friend... No matter what that takes, that’s the strategy.”

Rhee says he rewrote the business plan, and that nearly the entire staff was “changed out.” The company completed a change-of-control transaction in June 2016, without using “a dollar of debt.” Rhee says he used operational leverage instead. “The trick is to buy extremely cheap, in distress, and then you have to grow.”

When asked how the new business plan allowed for the company to keep

its loyal customer base while also attracting new business, Rhee told the story of a compliment he received in a Boston Globe piece about Ashley Stewart.

“One of the major bloggers in plus-size says that ‘James, inside he’s a plus-sized African-American woman.’ To me, that was about as high a compliment as I could get. That means I understood the customer and I was being a fiduciary for the customer.”

Forty percent of Ashley Stewart’s online business now is from white customers, which Rhee says is “up from zero.” He credits this expansion to not focusing on race or size but on “buying affordable nice fashion that’s on-trend for women.”

Social media has also been a huge driver in the growth of the business, using everything from contests to attend brand-sponsored concerts to traditional social word of mouth.

“It’s really focusing on a customer base and letting them advocate for you,” says Rhee. “What we are trying to run is truly what I call a ‘social commerce strategy.’” ■

Why 'Open and Transparent' Brands Win



Carol Lapidus
National Leader,
Consumer Products Industry,
RSM US LLC

The head of consumer products for RSM explains the brave new world of social media and transparency for brands—whether they're ready or not for this marketing game change

Privcap: How important are peer-to-peer recommendations in the consumer and retail business?

Carol Lapidus, RSM: According to a Nielsen online survey, consumers only trust about a third of the information that they receive directly from brands. But they trust 90 percent of the information they receive from their personal connections. What that says is [you should] develop consumers who are going to share, who are going to like, who are going to refer your brand to others.

Consumers value brands viewed as honest and transparent. What does that mean in practice?

Lapidus: The consumer wants to know that the brand is open about what the product does, what it doesn't do, how best to use the product. They want to know all the information that's necessary about a product. And they want to hear it in a concise manner. And if it's the right information and it's given to them in the right manner, they're going to share it with their friends.

What can a brand do when it encounters a real or perceived drop in quality?

Lapidus: It's so important for brands to not hold back information, especially in times of trouble

when there is a question as to the product. Act on it immediately. As we saw years ago when we had these security breaches, a company like Target wasn't as open and honest, and they lost a huge amount of their share of business in that year and in the following year. But you have other breaches where you had companies like Home Depot that are upfront, honest, told everybody exactly what happened. They didn't lose any of their customers for something like that.

Using social media, brands must now put out sharable content. How different is that from old-school marketing?

Lapidus: Well, what we say to clients is, "The best thing to do is to put out good content." So put out content about that product, but also put out content about your company, about the beliefs, about how you do your business, about your social and environmental, even political views. This is what's getting the consumer talking right now.

What should brands do with feedback they receive on social media from customers?

Lapidus: One of our clients that sells fashion to millennials is online. They're on Instagram. They're on Facebook. They've got a really good social media platform.

They listen to their consumer and they say, "Wow, that's a great idea." Or if it's not feasible, they respond to them and tell them why it's not going to work, but that's such a great idea. And sometimes they'll get some type of a bonus or a personal invitation to attend an event when they're responding to something like this, because it's really important to listen to the consumer. ■

Strategies for Staying Competitive Online

Brands big and small, old and new, are having to find out how to remain competitive in a crowded brand presence online



■ SMALLER BRANDS CAN BE MORE ADAPTIVE THAN BIG ONES

While giant brand names such as Procter & Gamble and Unilever have a lot of money and manpower behind them, smaller companies adapt faster. Anita Balaji of The Carlyle Group recounts how its portfolio company, haircare brand OGX, rose from obscurity to go head-to-head with Pantene and Garnier through social media engagement.

■ DISCUSSING A COMPANY'S ONLINE STRATEGY IS CRUCIAL

Having a discussion about how to present your brand online is important, no matter the company. Valerie Tomasello of fashion brand 3.1 Phillip Lim talked about how any misstep in social media or otherwise can go viral, but also that the right strategy can magnify the brand in a positive way without costing a lot.

■ LOOKING AT AN ONLINE PRESENCE SHOULD BE PART OF DUE DILIGENCE

Before investing in a company, poring over how it presents itself online and on social media is a must. While Carlyle doesn't have operating partners specifically for a portfolio company's online presence, Balaji says that if a company has a poor showing online, it is unlikely they would invest in the first place.



Valerie Tomasello
Vice President of Marketing,
3.1 Phillip Lim

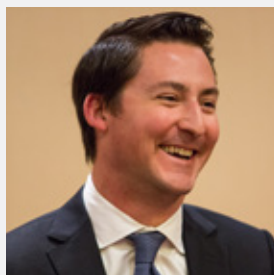


Anita Balaji
Principal,
The Carlyle Group

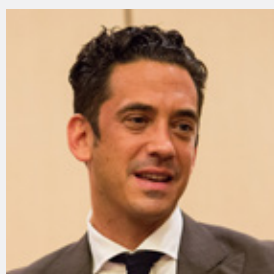
KEY FINDINGS

What to Watch in Food and Beverage

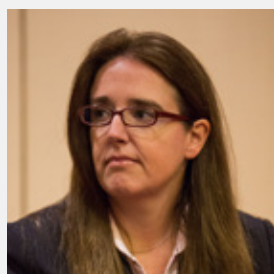
The business of selling food and beverages to consumers is being disrupted



David Briske
Principal,
Permira



John Meadow
Founder & President,
LDV Hospitality



Cristin Singer
Partner,
National Leader—Food & Beverage,
RSM US LLP

■ SUCCESS IN FOOD AND BEVERAGE IS NOT ABOUT TRENDS

When Permira decided portfolio company Popcorners would use all non-GMO ingredients, it was because that seems to be something consumers will care about for the long term. However, trying to keep up with the latest fad, whether it's quinoa or kale or the next "superfood," is not something well-suited for private equity or even a restaurant group to latch onto.

■ CRAFT BEER'S GAINS ARE DUE TO A SEARCH FOR AUTHENTICITY

The popularity of smaller breweries can be pegged to consumers' search for products with a story, made by a small producer. Private equity has certainly decided it's an industry that's not going away, and invested accordingly.

■ SUBSCRIPTION SERVICES ARE WORTH A CLOSER LOOK

Whether it's a meal kit service like Blue Apron or a box of healthy snacks, consumers are on board with the idea of receiving a carefully crafted box on a set schedule. Both Briske and Cristin Singer of RSM agree this is a business model worth watching.

The Day in Photos

Images from Privcap's first consumer and retail conference



▲ Attendees network during a break between panels.



▲ Peter Fader, a professor of marketing at the Wharton School, speaks on a panel about using consumer data.





▲ Privcap's David Snow leads an audience Q&A session with panelists.



Information Is the Disrupter

Consumers now have access to a dizzying array of information about the products and services they use. And few entrepreneurs have benefited from this information disruption more than Bo Peabody, a co-founder of Village Ventures and current venture partner at Greycroft Partners. In a keynote interview, Peabody talked about his current project, Renzell, and how the wealth of customer data is fueling software companies and marketing behavior.

USING CUSTOMER BUYING PATTERNS TO PREDICT FUTURE BEHAVIOR

There's a whole new class of companies using data models and machine learning to figure out what is likely to happen with a customer's buying patterns, and then, says Peabody, giving "lots of ideas that are related to the different channels you use to do marketing, based on what they think will happen [and] based on the profile of someone who's never bought.

"Now we've got so much data on so many people. And there just aren't that many types of people, so as long as you have a little bit of information about somebody, you can start to predict how they're going to behave.

"That's pretty powerful for companies," says Peabody. ■

DISRUPTING HOW YOU REVIEW RESTAURANTS

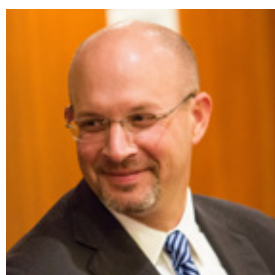
Renzell, a membership club for those who like to eat in high-end restaurants, involves taking a 70-question survey about your dining experience. How is that different from the many existing outlets (Yelp, Zagat, Chowhound) for people to put in their two cents about restaurants?

Peabody says what sets these opinions apart is that they're based on "very granular surveys with a lot of data. And then we crunch that data, and we give it back to the restaurants, and we turn it into ratings."

What he thought was missing from the plethora of restaurant review data was using it to suggest things based on a person's profile, or based on the profile of someone similar to them. "The only place that data has somehow missed is the restaurant ratings and review system. Any time you go to make a big purchase—and by the way, when you go to these restaurants, it's a big purchase—you're using data."



Bo Peabody
Venture Partner,
Entrepreneur-in-Residence,
Greycroft Partners

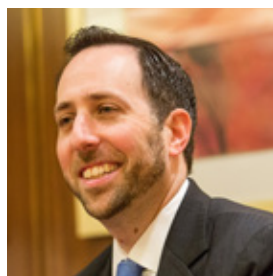


Jeremy Holland
Principal,
The Riverside Company

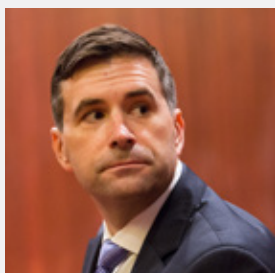
Deal Flow Dynamics in the Consumer Sector



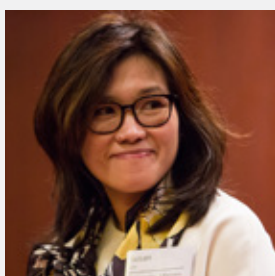
Daniel Galpern
Partner,
TZP Group



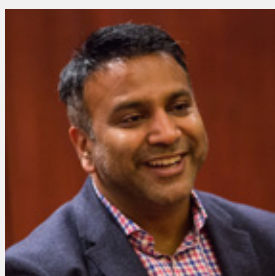
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Partner,
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Anu Goel
EVP Strategic Clients &
Growth Solutions,
SPINS

Want to buy or sell a brand? Today there's no shortage of opportunities.

■ DEAL FLOW IS STRONG—AND WILL STAY THAT WAY

Yes, there's a lot of dry powder and cheap money, so deals are abundant and multiples are high. They are likely to stay that way, at least for the foreseeable future. There's simply too much capital that needs to be put to work; don't expect momentum to slow anytime soon.

■ GOOD COMPANIES ARE GETTING HARDER TO FIND

The robust deal environment has lasted several years, meaning that companies have been picked over and the best have been scooped up. So successful managers need operational expertise to create and realize value in their newly acquired companies.

■ FINDING A GOOD PARTNER IS STILL ABOUT THE BASICS

Even for smaller consumer businesses, the pool of potential partners is deep—money could come from lower-middle-market PE, from strategics, or anywhere in between. When choosing a firm to work with, ask a simple question: If times get tough, are these the people I'll want helping me work it out?

Why Product Differentiation Is Key

Product differentiation is a complex business—understanding and defining the key selling points for your own product line takes commitment, data, and insight

■ WHEN EXPANDING IN NEW REGIONS OR COUNTRIES, KNOW YOUR MARKET

When it comes to consumer brands, private equity often lends its expertise to expand in new markets. That requires careful planning and diligence. Firms often find that their brand strategy isn't portable, so having local intelligence is critical.

■ KNOW THE DIFFERENCE BETWEEN A DIFFERENTIATOR AND 'TABLE STAKES'

Over time, what once was a differentiator becomes mainstream. Take the world of yogurt—being organic is no longer enough. To stand out, firms are now moving beyond organic into ingredients like grass-fed milk. Smart brands constantly evolve to stay ahead of—or define—features and changes that will drive consumer choice.

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