

# Neiman marcus

[Business](#), [Company](#)



Neiman Marcus (NM), which mainly serves the high-end retail market, is currently facing a tough future. Although it currently enjoys high profit margins and has made significant improvements in its existing brand performance, its growth has plateaued. NM believes that there is only limited potential for growth of its current full-line stores while maintaining its exclusivity. As a result, it is considering other growth opportunities. The strategic goal is to increase its revenue by at least \$150 million over the next 6 years while maintaining its attractive profit margins of 15%.

Of the number of possible growth options, we recommend NM to grow via the Galleries concept. We believe that this concept is in line with its current core strength of creating and maintaining customer loyalty with luxury customers. Moreover, it can benefit from its existing customer base, efficient sales force and brand name. Our financial analysis further shows that the concept has the potential to match the revenue and profit goals.

However, NM needs to carefully choose the gallery locations since there are some risks associated with direct competition with existing leaders and confusion among its current customers about the shift in brand-focus.

Growth Options Neiman Marcus (NM) serves the high-end retail market mostly in US. Before analyzing the range of growth options available to NM, we performed a SWOT analysis to understand NM's current competitive situation. NM clearly targets the affluent US population and intends to serve the luxury market.

The company's goal is to create a personal shopping experience for its customers, and that involves having a highly competent sales staff as well as

setting up a unique buying experience. One of the biggest competitive advantages for NM is the customer based marketing programs and events, like the InCircle programs which enhances customer loyalty. The catalog advertising is another core-competency that NM can leverage greatly from, since it drives about 50% of the sales of the customer that also shop at the stores. NM invests heavily in training and retaining its sales forces via programs like the “ Optimum Selling Program” and competitive compensation to the employees. It leverages the sales force to create a personal shopping experience to the affluent customer with the objective of enhancing the customer relationship and increasing the average customer spend. Considering that the target consumer segment is the affluent consumer who earns over \$200, 000 annually, there is limited growth potential within this high premium segment since acquiring new customers with high buying power needs is difficult.

Thus, the focus is to increase customer retention and find creative ways for customers to spend more on NM products, with the following approaches

- Brand extension :“ Galleries” for jewelry; Specialty store for shoes
  - Geographical extension: Expand into Europe; increasing retail space within stores;
  - Portfolio extension: Acquisition(Saks); Open Sale-price stores like“(Nordstrum) rack”
  - Relationship extension : Enhance relationship with emerging designers
- Brand extensions via Galleries for the jewelry category would put NM in direct competition with the likes of Tiffany’s Co.

This might impact the top line (Revenues) more than the bottom line (net income), considering that it would involve higher costs for development of the stores, and heavy investments in advertisement and customer retention. Geographic extensions like expanding into Europe would not have high impact on the top line nor is bottom line, considering there 50% higher penetration of designer owned stores. Moreover, NM might need significant time and investment to create its brand name and competent sales force team in such new but fiercely competitive market.

Portfolio extension: Acquisition of Saks would definitely have a positive impact on both the top line and the bottom line. However, NM would need to be careful on how this would affect its relationship with the employees and the designers. However, sale-price stores would likely dilute the brand image for NM, and alienate some of its existing consumers. Enhancing relationship with emerging designers would probably impact NM most on the bottom line than on the top line, considering it would be able to leverage purchasing power with the emerging designers, and extract higher margins from the merchandise. do we need to estimate top line/bottom line impact? ] Of all these options, the Galleries and Acquisition of Saks are the ones that can leverage NM's core competencies to the best ability. These avenues provide an opportunity for leveraging the marketing catalogues, customer relationships, and employee satisfaction and retention. The acquisition of existing brands such as Saks is subject to more extraneous factors (negotiations, stock valuations, government regulations, merger risks, brand value distortion) and therefore unclear as a long term strategy.

Neiman Marcus' Positioning. Based on our understanding, we believe NM's current positioning statement is: For the affluent customer who takes great pride in buying only top-line luxury clothing and accessories, NM store is your one-stop place for all your fashion needs since we only stock best assortment of designer boutiques and our friendly knowledgeable staff knows exactly what you are looking for. NM's positioning is to attract the affluent consumer, with a household income of over \$100, 000, by providing high-end luxury lines of women's and men's apparel, Jewelry, Cosmetics/fragrances, Gifts, Women's shoes and Accessories.

The core competencies that NM engages to differentiate itself in the marketplace are exclusive high-end designer merchandise, personable, knowledgeable and highly competent sales staff that aims at not only achieving a high level of customer satisfaction, but also establishing themselves as a personal shopper for the customer. The sales staff is cross-trained in multiple departments, and is empowered to build long term relationships with their customers.

This enables NM to provide a customized and personal experience for its clientele, thus encouraging them to be repeat customers and increase their spend at NM. NM utilizes another core-competency of catalogs for direct marketing, thus creating avenues to increase spend by the customers. One of the differentiators for NM, an un-imitable competency that creates barriers of entry is the customer based marketing programs, and events. The InCircle program is targeted to enhance customer relationships and brand loyalty.

Special events and incentives are creating for the “creme-de-la-creme” spenders via the InCircle program that provides these customers to become repeat consumers via exquisite rewards programs and one-on-one customer service. About 40% of sales at NM were estimated from these programs and events organized by NM. Direct competitors for NM include Saks 5th avenue and Nordstrom. Saks and NM differed in their approach to store formats. While NM had primarily focused on full line stores, Saks had developed other formats like resort stores, Main street stores, Off 5th stores, thus targeting different consumer segments.

Nordstrom on the other hand had similar merchandise portfolio as NM, and was known for the level of personal customer attention and service it provided by building key relationships. NM on the other hand provided multiple competencies that included specialty store variety (for specific designers) and department store scale and service. Quantitative Analysis of the Galleries Concept We performed a quantitative analysis to evaluate the Galleries concept. We made some key assumptions for the analysis. First, the revenue per sq. ft. for the three lines: fashion jewelry, precious jewelry and gifts would be equal to the current NM revenues in these departments. Second, the annual percentage revenue growth for Galleria would be equal to NM’s current annual revenue growth of 7%. Third, the allocation of space within the 10,000 sq. ft. Galleria would be allocated to the existing ratios within the three departments. Using these assumptions, as shown in Exhibit a, we calculated the revenue per sq. ft. for the three lines. Using these values, we computed the expected revenue (base year) for one Galleria.

We next constructed the pro-forma (Exhibit b) for one galleria for the next 6 years. We assumed that the revenue growth would be the same (7%), the gross margin and hence the COGS would be constant (56% which is the current weighted COGS for these three department). As seen in the pro-forma, we estimate each galleria will have revenues of \$10.8 million and Cash-flow (assuming EBT = EBTDA) of \$2.1 million by year 6. Using Present Value of the Cash flows (assumed equal to EBIT) at 15% discount rate, we estimate the payback period for each galleria on the initial investment of \$5 million to be 5 years (2003 assuming base year is 1998).

With additional revenue per galleria in Year 6 estimated at \$10.8 million, to achieve a financial goal of \$200 million in additional revenue from the galleries by Year 6, NM would need to open 19 (200/10.8) galleries. This would require an overall investment of about \$95 million in capital in the current year. The quantitative analysis indicate that if the three constituent departments of the galleries can perform at least at par with current levels (mainly in terms of revenue per sq. ft. and gross margins), NM is very likely to fulfill the goal of \$200 million in surplus revenue growth by year 6.

In fact, since the payback period (at 15% discount rate) is 5 years, the IRR return from the investment is expected to be more than the required 15%. Thus the quantitative analysis is definitely in favor of the galleries concept.

Qualitative Analysis of the Galleries Concept The Galleries concept is to aimed to expand the per-customer spend of the target affluent consumer, by providing specialty stores for specific merchandise category. One of the viable options is to consider a Gallery which includes the departments that

provide the highest revenue per sq. ft. namely Precious jewelry, fashion jewelry and Gifts, again targeting the same affluent customer segment. This concept makes sense for NM since it can leverage from its current strengths – loyalty program, dedicated and knowledgeable staff, and its existing brand value. Moreover, expanding the gallery concept in US where it already has an established brand name and elite-status makes perfect sense. However, as discussed before, the Jewelry and Gifts gallery concept would end up going head-to-head with a Tiffany's store. Therefore NM needs to address the following risks for ensuring significant market share capture.

First, considering that the flagship Tiffany's store has a sales/sq ft ratio of over \$3000 , NM needs to either increase the retail space for precious jewelry to improve from the overall expected \$721 / sq. ft revenue (this is because precious jewelry in current NM stores earn a much higher \$1669/ sq ft), or decrease the store gross selling space for the gallery. Second, expanding the number of Galleries excessively might rebrand NM in the minds of customers as jewelry focused company and might affect the sales of its other flagship products such as women's apparel and shoes in original NM stores.

Therefore, NM needs to be careful in choosing the locations of these new galleria stores and try to not choose locations where they currently exist. With regards to the locations of the new Gallery stores, we believe that NM needs to choose locations that are not competitively served (by Tiffany's) in the Jewelry category, and also locations that do not have heavy overlap with its current locations. It is also important not to deviate from the target



affluent consumer with high buying power index. Thus, we recommend the following top 3 locations for NM to open the initial Gallery stores to ensure impactful market share capture. Based on how the galleries perform in these markets, NM can use the same criteria to open galleries in other markets.

Seattle - Top most 1996 BPI; No Tiffany presence; some overlap with NM stores  
Cleveland - Ranked 2nd 1996 BPI; No Tiffany presence; some overlap with NM stores  
Sacramento - Ranked 3rd 1996 BPI; No Tiffany presence; high overlap with NM stores  
Conclusion Based on the analysis of NM's current positioning and its core competencies, we believe the Galleria concept presents a good growth opportunity for NM.

Quantitatively, the concept has potential to fulfill both of NM's current goals: revenue growth (\$150-\$200 million revenue growth over 6 years) and profit margin (Payback period for initial investment is under 6 years at desired 15% cost of capital). However, NM needs to be careful in choosing the locations for two reasons: to avoid head-to-head competition with existing jewelers such as Tiffany's and to avoid confusion of its brand focus in the minds of its existing rich customer base.