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ATLANTIC CAPITAL MARKETS



BOOHOO. BUY, SELL OR AVOID

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Investors love a good growth story and over the years Boohoo has certainly ticked the boxes. The online fast-fashion retailer has delivered phenomenal growth....but at what cost!!

The business is currently taking the onslaught of the scandalous news of slave like labour conditions, below minimum wage pay and no measures taken during the pandemic to protect staff of their suppliers, so what may well be cheap and fast fashion certainly isn't cheap for everyone involved.

Boohoo have been quick to try and distance themselves from the suppliers, it is just a shame that the suppliers didn't offer workers the same sort of distance during lockdown for their staff.

But perhaps the biggest shock to me is... how much of a shock it is to others!

What I mean is, something that never really made sense is how can a business that sells items for so cheap make such a profit?

Cheap and Cheerful

Boohoo is a leading online retailer in what's called 'fast fashion'. Fast fashion is low cost clothing that copies current fashion trends. The aim is to get new trends to market as quickly and cheaply as possible. Boohoo's target market is 16-24-year-olds, who tend to change their wardrobes frequently but don't want to spend too much. The average item sold by Boohoo is £13, though a typical order will involve purchasing 3 items. At such a low price point, you only need a few wears of something to get your money's worth. Boohoo offers its 8+ million customer base a huge amount of choice that no high street shop could ever come close to matching. Their websites carry over 30,000 different items.

A Northern Giant

Boohoo was founded in 2006 by Mahmud Kamani and Carol Kane, and previously supplied high street chains such as Primark and New Look. Boohoo's core products include dresses and tops, with a selection of over 27,000 styles of clothing. The pair clearly work well together and liken their partnership to a brother-sister relationship. Kamani dealt with operations and IT. Kane is the fashion and marketing guru. The company's headquarters remain in Manchester and has its giant distribution centre in Burnley. The UK remains Boohoo's key market, but the international side is growing, particularly in the US and Europe.

Acquisition Machine

Boohoo hasn't hung around when it comes to acquisitions with the firm understanding that a strong foothold in the US markets was needed early on. The acquisition of NastyGal, which is headquartered in Los Angeles, gave Boohoo an important leg-up into the huge US market. NastyGal, which started in 2006, the same year as Boohoo, had grown its sales rapidly but had troubles behind the scenes with the nitty gritty side of business – things like product sourcing and infrastructure – areas that Boohoo excel in. Boohoo may have



got themselves an absolute bargain as they acquired the business out of Chapter 11 bankruptcy for £16mn. The next acquisition was Pretty Little Thing, which saw Boohoo take an initial stake of 66% back in 2017 and recently completed the full acquisition earlier this year.

Boohoo then shifted focus to the UK and more established brands as they bought Karen Millen and Coast's online businesses from administrators last summer and will be integrating the Oasis and Warehouse online operations into its platform in the coming months. Most recently Boohoo made the move to buy Oasis and Warehouse for £5.3mn as it upped its profit thanks to resilient trading amid the lockdown. The group agreed the deal with restructuring expert Hilco Capital, which bought the Oasis and Warehouse brands and stock from administrators in April. Boohoo announced the deal as it unveiled "very strong" trading despite the coronavirus crisis, with UK sales surging 30% in the three months to May 31.

Technical Chart



Recent Developments

Boohoo have hit the news for all the wrong reasons. It was all looking very bullish as the firm initially reported strong figures from trading during the pandemic with a huge surge in sales during lockdown. The selection of brands was growing and all was looking rosy, that was before the news broke of what can only really be described as modern-day slavery conditions. Workers being paid a pittance, squalid conditions and no consideration at all for social distancing or the working conditions for the staff.



But, is it really that much of a shock? Or more an inconvenient truthLet's be frank something that never really made sense, is how can a business that sells items for so cheap make a profit?

.....and make enough to also fund all the acquisitions. The general customers for the business 16-24-year olds seemed to be happy to look the other way and everyone in the market marvelled at their performance in such hard conditions and now it all seems so obvious as to why. The murkiness that has surrounded the supply chain for years was clearly hiding something and in hindsight the almost Dickensian working conditions, illegal pay rates and labour exploitation have been going on for years. This isn't something that has just emerged either, the companies largest share holder has been pushing the firm for years over the lack of transparency in the supply chain, and poor working conditions.

So, is it time to Buy?

With all the news you would expect to see the shares trading at a serious discount and the share price has dropped 50% but in reality just back to march levels. This does make the share price interesting but hardly a bargain, especially when you also factor in the high risk premium of any further developments.

Since the initial accusations against Boohoo the company has taken strong steps and ordered a full independent review of its UK supply chain. It has asked a senior barrister to lead the investigation and is also spending £10m to investigate and eradicate supply chain malpractice. However, this is not the first time the issue has arisen and last time around it managed to get swept under the carpet lively but this time around it could take quite sometime to get the problem resolved, and at what cost? Clearly the reason they turn a profit is due to the low cost of the clothing they buy so how will this translate to their profits if they really are trying to eradicate supply chain misconduct.

However they come out of this it is clear that the company is going to face higher costs going forward. The £10m outlay to improve its supply chain will come out of the group's bottom line. The firm may also have to increase the prices it pays to suppliers. That would reduce profit margins moving forward. The higher costs that boohoo is looking at will undoubtedly impact revenue and thus impact the groups profitability and share price over the long run. City analysts were expecting the company to report a net profit of £93m for 2021. The £10m supply chain cost will reduce this by 11%. Higher production costs may reduce future income. Also, retailers' boycotts of the brand may impact sales.

The one saving grace and what could save them is that the online clothing market is booming, and Boohoo is one of the world's leading online fashion brands and biggest presence in this space.

The biggest factor affecting my view at the moment is the uncertainty, markets don't like uncertainty, I don't like uncertainty!! and whilst some of the levels we are seeing at the moment could turn out to be fantastic buying levels the lack of clarity on how they are going to navigate the crisis is enough to put me off until further clarity is sought.



There has also been reports that Boohoo is facing a modern slavery investigation, which could result in a high court injunction or an unlimited fine. Therefore, this could be just the beginning of a prolonged period of uncertainty for the Boohoo share price.

The rapid share price movements will undoubtedly attract the day traders and those with a high-risk appetite but for the long term I would avoid the stock until some form of clarity is gained towards the current situation.

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