

**you**

Let **SWEAT FLOW** from your pores once a day to regenerate your skin.

**Jealousy** works the opposite way you want it to.

**Friends are more important than money.**

**Be creative.**

**Will you choose a life of a glass half empty or a glass half full?**

**DANCE, SING, FLOSS AND TRA**

**lululemon athletica** incorporated on November 21, 2005, is a designer and retailer of technical athletic apparel operating primarily in North America and Australia. The Company's yoga inspired apparel is marketed under the

lululemon athletica brand name.

The Company offers a range of performance apparel and accessories for women, men and female youth. Its apparel assortment, including items, such as fitness pants, shorts, tops and jackets, is designed for healthy lifestyle activities such as yoga, running and general fitness.

Lululemon's fitness-related accessories include an array of items, such as bags, socks, underwear, yoga mats, instructional yoga digital versatile discs (DVDs) and water bottles.

The Company's products are sold through 174 corporate-owned stores in North America, including 47 in Canada and 108 in the United States. Its retail stores are located

primarily on street locations, in lifestyle centers and in malls.

Chip Wilson, the founder of Lululemon has created a PR nightmare for the company and stepped down from his post as Chairman of the Board in November, 2013. The athletic apparel company has faced increased scrutiny over the past few months for discriminating against plus-sized customers and eluding to using this as part of the company's strategy.

In November 2013, Wilson came under fire for suggesting that some women's bodies were not made for his brand's yoga pants, saying, "Frankly some women's bodies just don't actually work for [the pants]."

Christine Day, a former Co-President of Starbucks International, was the CEO of Lululemon from 2010 to 2013. After the PR debacle, it was announced Day would leave her position, and was soon replaced by Laurent Potdevin, former CEO of Tom's Shoes.

Investors are worried about the first quarter and beyond. Shares of Lululemon closed trading Monday down nearly 17% at \$49.70, following its \$22 million quarterly sales forecast reduction earlier in the day.

This downturn has much to do with the PR debacle of 2013, but also with the increase of smaller, independent brands to the market.

The retailer that popularized, and once dominated, yoga wear now has challengers on multiple fronts. They include Gap, which is opening Athleta yoga stores alongside Lululemon locations around the country, under-the-radar brands like Prana and Gaiam, and the athletic-wear giants Nike, Under Armour and Adidas. Offering yoga apparel at a much lower price point, these brands are gaining popularity, although Lulu is a marketing machine with a mini-empire and cult-like following.

The chain has a different strategy for stoking demand for Wunder Under pants, Scuba hoodies and racerback tanks. Unlike most retailers, Lululemon doesn't use software to gather customer data, doesn't build lots of new stores, doesn't offer generous discounts and purposely stocks less inventory than it can keep on its shelves. Instead, the Vancouver company stays in close contact with its customers and cultivates a sense of scarcity. During a time when most retailers have used discounting to drive sales, it uses pricing power to its advantage to keep items flying off the shelves.

The success a "scarcity" model, in which its outlets keep only a limited supply of stock. Customers know that they have to buy an item right away if they want to get their hands on it, which "creates these fanatical shoppers. Lululemon also rarely offers sales, which means its customers buy everything at full price. Its yoga pants, for example, range from \$75 to \$128, while similar products

can be found at the Gap at prices as low as \$25. Call it the Apple model. The strategy is to continually refine Lululemon's core products, which results in clothes that are aesthetically pleasing, functional — and pricier.

The brand was built through word of mouth and community. “We’re becoming a global brand but we’re very much local in the communities in which we operate,” said Laura Klauberg, vice-president of global brand and community. Company representatives encourage local yoga instructors and athletes to become brand “ambassadors” to promote sales and product knowledge.

Billboards are few and far between, and television advertising is non-existent. Print ads appear only in Yoga Journal. Even the shopping bags printed with aphorisms like, “Friends are more important than money” and “Have you woken up two days in a row uninspired? Change your life!” Although menswear is growing in focus, the target market remains women – from teens to those in their mid-60s – who are interested in staying healthy and fit.

Lululemon employs unconventional and inexpensive marketing strategies. While other fitness-wear lines (especially multinational sports shoe brands) pay crazy money for big name celebrities to push their lines, lululemon appoints community ambassadors and doesn’t pay for them, instead giving them \$1000 worth of product and inviting them to teach for free in their stores. This is, apparently, a very radical thing to do in the fitness apparel

industry. Only running “occasional” print ads in a handful of yoga and running magazines. Basically, they have eschewed traditional advertising strategies in favor of getting into the local community and marketing through word of mouth and local influencers.

The Vancouver-based athletic apparel company's stock is now trading at a two-year low following the PR debacle 2013 and slow traffic in January caused the firm's second reduction in a month's time of its fourth-quarter revenue and earnings guidance. Here are a few reasons why some say the stock is currently imploding:

**Quality-control issues.** Last year, Lululemon had to recall 17 percent of its pants because they were too sheer. Even though the company claims to have fixed that issue, customers have complained that the pants pill and shred. Shoppers who spend \$100 on yoga pants expect good quality, and these incidents have tarnished perception of the company.

**Competition.** A swarm of competitors came into the picture at exactly the wrong time. Gap's Athleta, Under Armour, and Oakley, are just a few competitors making premium exercise gear. The quality issues plaguing Lululemon gave shoppers an incentive to check out other retailers.

**Marketing disasters.** Late last year, Lululemon founder Chip Wilson gave an interview implying that women complaining about sheer or pilling pants were too large to be wearing them. After a public outcry, he stepped down. The company has also been criticized for encouraging employees to attend a retreat that has been compared to Scientology.

**Inexperience.** Lululemon expanded rapidly after going public eight years ago. But the company has no experience dealing with downturns. "The company has never operated in an environment of declining sales demand," writes John Zolidis at Buckingham Research. Zolidis says this means that the current decline won't be an easy fix for Lululemon.

**Lack of preparation.** Lululemon needed to prepare an expansion plan for when business began to slow down, Brian Sozzi, chief equities strategist at Belus Capital Advisors, said. But now, the company's new CEO has a long way to go. Sozzi states, "The goal for him will not only be to reignite comps through new categories and global expansion, but to find ways to re-engineer the product to bring down costs and set gross margins back into expansionary territory—and then prepare them for another slowdown cycle well into the future".

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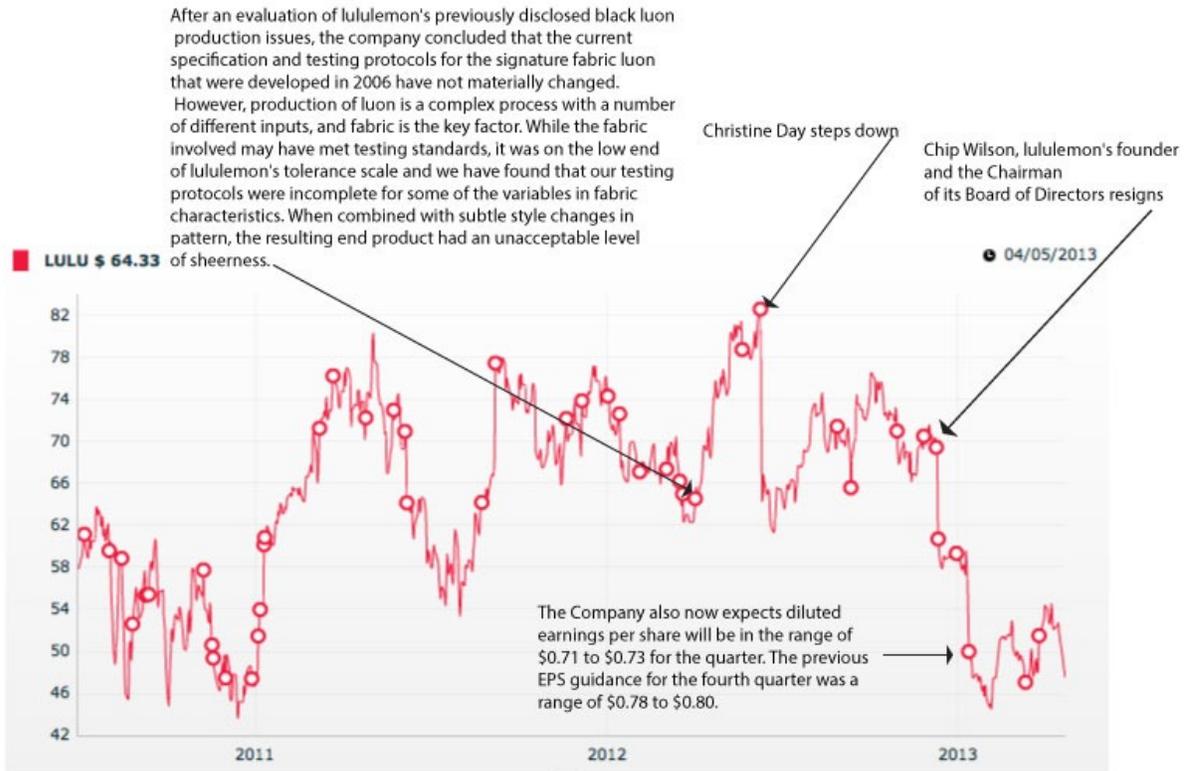
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Analysts, for the most part, are increasingly positive about the company's future, particularly as American shoppers emerge from deep freeze. Sharon Zackfia, who covers the company for William Blair, argues that it's not just a yoga company, but a company that makes quality athletic clothing for women, an important segment not yet dominated by "a vertically integrated retailer," which is to say an entity that controls everything from manufacturing to the store experience. Nike, by contrast, is a wholesaler, and Lululemon is not likely to try to be Nike. "You can go to Sports Authority to get stuff made by Nike for women," says Zackfia, "but you just don't feel indulgent there."

Staying small and retaining the special feel of a brand that's like a club sounds good, but Lulu may have foreclosed on that vision when it went public. Market pressure makes it very difficult for public companies to choose the long-term good of a brand over the near-term demands of earnings reports. The perfect example is Starbucks, which lost its cachet by expanding into every strip mall and airport concourse and can't seem to get it back at any price.

Right now, Lulu floats at that magical spot between obscurity and ubiquity. Few brands have ever been able to stay there. Stay tuned...

## Effects on Share price



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