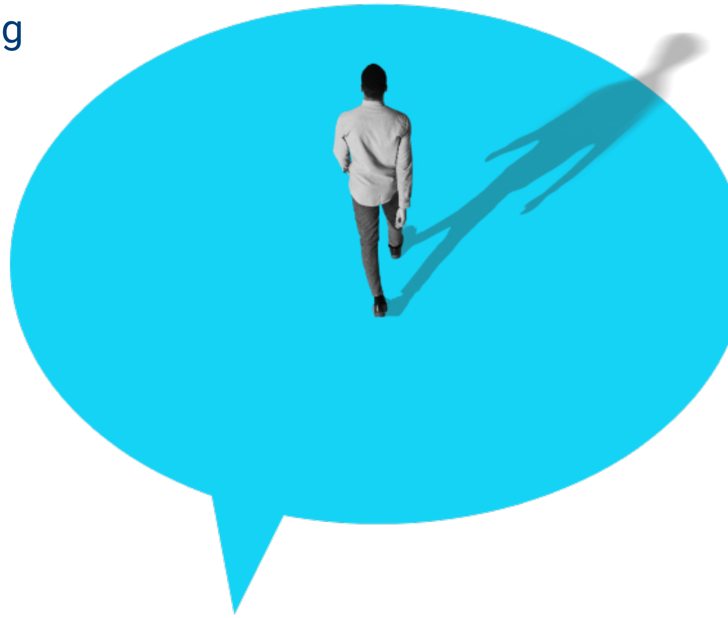
SANDON CAPITAL

city chic

CASE STUDY

Collaborative engagement in action

Formerly known as Specialty Fashion Group, Sydney headquartered City Chic (ASX:CCX) is today an omni-channel retailer catering to plus-size women in Australasia, North America and Europe. Online sales represent over 70% of the company's total sales.



THE OPPORTUNITY

The legacy Specialty Fashion Group brands – Autograph, Crossroads, Katies, Millers and Rivers – were performing poorly and masking the strong revenue, profit and cash flow growth of the City Chic brand. Whilst the company had historically generated strong cash flows, following a number of poor decisions the company was facing serious difficulties and the vultures had begun to circle.

Conventional thinking, helped along by press reports of pressure from banks, was that it was a 'failed' or 'failing' company. Whilst this may have been partially true of some of its legacy brands, the market completely overlooked the enormous potential of the City Chic brand. There were also a number of private equity investors interested in acquiring the City Chic business.

Sandon Capital saw a number of opportunities for value to be unlocked in the company reflecting on the fact that it was a number of poor decisions made by the incumbent management team that had brought on the difficulties faced by the Company.

Sandon Capital was obliged to change its approach however, when it became apparent that shareholder pressure was mounting to sell the City Chic brand to save the business (even though we never thought the business was in jeopardy). Sandon Capital decided that:

- rather than sell off its high-quality assets to repair the balance sheet and appease debt providers, the company could be recapitalised by existing shareholders and then rationalise its store network; and
- once recapitalised and the operations stabilised, the company could use its abundance of franking credits to efficiently return cash to shareholders in the form of fully-franked dividends.

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THE ACTIVIST CAMPAIGN

Sandon Capital had planned to conduct a campaign to force board and senior management changes. Not long after Sandon Capital began buying shares in early 2017, the company disclosed it had received a non-binding indicative offer (NBIO) to acquire all the shares of the company. This meant Sandon Capital's activist plans were on-hold. Months later the NBIO would lapse, and the share price fell, reaching a nadir of 10 cents per share in December 2017.

As these events unfolded and through private engagement with the Board in mid-2017, we formed the view Sandon Capital's interests would be best served by supporting the independent directors, led by Chair Anne McDonald.

Sandon Capital escalated its discussions with the Board in the first quarter of 2018 following:

- the company's announcement of a structural review in November 2017;
- a number of press reports in early 2018 that the company's debt providers were turning the screws; and
- rumours in the press that opportunistic acquirers were looking to takeover part or all the company.

Sandon Capital proposed a recapitalisation via an underwritten rights issue. This aligned with the Board's own view on capital management following its structural review. With a recapitalisation proposal as its backstop, the company went one better and announced the sale of its underperforming legacy brands in May 2018. This move unshackled the City Chic brand from the underperforming brands, raised cash to repair the balance sheet, and negated the need for the rationalisation and refurbishment of the company's old and tired store network.

Sandon Capital continues to engage with the company, predominantly in the area of capital management. Through judicious acquisitions, the company has opportunistically deployed capital in offshore markets in order to grow itself into a truly global women's plus-sized omni-channel retailer. When combined with organic growth in its existing business, the strong growth in profits has seen the company's share price increase by a factor of 60 times (60x) since the lows seen in late 2017.

SUMMARY

In mid-2017 Sandon Capital approached the Board with a capital adjustment proposal as part of a strategy to firm up the company's financial position. The Board was responsive to our proposal and ongoing input as they successfully navigated the company out of financial crisis whilst maintaining the potential for strong future growth.

INVESTMENT STATUS

Sandon Capital remains a shareholder of CCX.

CURRENT VIEW

CCX is a core holding for Sandon Capital. It remains moderately priced for a company that is generating very strong profits, cash flows and returns on capital. Management continues to demonstrate its ability to navigate challenging retail conditions and deliver solid growth, both organically and through acquisitions.

Plus-sized fashion is an underserved, growing global market. Investors will continue to reap the rewards of CCX's focus on its plus-size customers through its "A World of Curves" strategy. Its opportunistic acquisitions to expand in new geographies, sees CCX well-placed to benefit from the global economic rebound from the pandemic.

Thinking of investing?
Contact us.

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