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**Berkshire Partners: Bidding for Carter’s**

In the spring of 2001, Boston-based pr vate equity firm Berkshire Partners was considering a

leveraged buyout (LBO) of the William Carter Co., a leading producer of infant, baby, and children’s apparel in the United States. Berkshire Partners, which had extensive experience investing in the retail and manufacturing sectors, was initially drawn to Carter’s because of the strong brand name the company had developed during its 136-year history, as well as for the strength of the senior management team. (See **Exhibit 1** for a profile of Berkshire.)

To investigate the option of a potential LBO, Berkshire assembled a five-member team, to be led by managing directors Ross Jones and Bradley Bloom and senior associate Michael Ascione. (See **Exhibit 2** for biographical sketches.) The team would have less than eight weeks to move through all the stages of a Goldman Sachs-led auction—from initial research and due diligence to valuation and bid strategy.

In addition to running the auction and thereby serving as Carter’s agent, Goldman Sachs (GS) would be offering “staple-on” financing. Under this arrangement, t**h**e winning bidder would have the option to finance the deal through a prepackaged capital structure proposed by Goldman Sachs.1

# Carter’s

Carter’s was founded in 1865 in Needham, Massachusetts. Over the course of 136 years in the

highly competitive apparel industry, the company became the largest branded manufacturer of

toddler and baby apparel in the United States and also a leading maker of young children’s clothing. Dividing its market into five segments—layette (i.e., newborn), baby sleepwear, baby playwear, young children’s sleepwear, and young children’s playwear—the company sought to outfit children for the first six years of life, “from birth to bus.”

In the early 1990s, the company found itself struggling. Owned at the time by insurance company Mutual Benefit Life and Wesray Capital Corp., Carter’s had developed unprofitable product lines in swimwear and underwear, and many of its more decorative features (zippers, cut bows, etc.) were not well received by consumers. In 1992, the company installed a new management team led by CEO

Frederick J. Rowan, with the intention of “steering it back to its core niche of soft, comfortable

1 Morgan Stanley had recently made a similar offering to the eventual buyer of Dresser Equipment Group—underwriting $1.1 billion in debt financing after leading the auction. While staple-on financing was not a typical practice, it was becoming more common.

Professor Malcolm Baker and Research Associate James Quinn, Global Research Group, prepared this case. HBS cases are developed solely as the basis for class discussion. Cases are not intended to serve as endorsements, sources of primary data, or illustrations of effective or ineffective management.

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**205-058 Berkshire Partners: Bidding for Carter's**

clothing.”2 Rowan arrived with 39 years of experience in the industry, most recently running the Bassett-Walker and Lee Jeans division of VF Corporation. Many members of his executive team were also former managers with VF Corporation.

With a strategy of simplifying Carter’s products, Rowan and his team returned to producing what they called “high-volume, basic apparel.” Product design remained relatively consistent from year to year: About two-thirds of the apparel was carried forward from season to season with the same fabric and construction, varying only through color and artistic layout.

Rowan and his team also focused on improving the capabilities of their supply chain while exploring offshore sourcing options. Throughout the company’s history, it had relied on domestic manufacturing to produce its clothing. But amidst an increasingly global environment in which more and more U.S. companies were outsourcing production abroad, Rowan sought cost improvements and “manufacturing flexibility” through manufacturing abroad. In 1992, Carter’s closed two of its domestic sewing plants and made plans to close six additional sewing plants and its main textile mill. Central America and Mexico soon became the company’s first international production sites.

By 1996, with operating and financial performance beginning to turn around, Carter’s was acquired in a leveraged buyout by Investcorp S.A., the Bahrain-based firm best known for its investments in Gucci Group, Saks Inc., and Tiffany & Co. Investcorp (see **Exhibit 3** for profile) paid approximately $208 million. This included $56.1 million in senior debt and $90 million in subordinated debt. The purchase was consistent with the firm’s philosophy of injecting “patient capital” into North American and European companies; this simply involved waiting for the business to improve before selling it or taking it public.

At the time of the Investcorp LBO, Carter’s was doing business with over 400 wholesale accounts, including department stores, national chains, and specialty stores. It had also established a major domestic presence with its outlet stores: The company operated roughly 150 retail outlet stores across the country. Consumers could purchase Carter’s merchandise through these outlets stores at a deep discount, with the outlet stores offering new products, holdovers from excess inventory, as well as assorted Carter’s brand accessories and licensed products.

Beginning in 2000, Carter’s launched a new brand called *Tykes*. A departure from its two mainstay brands, *Carter’s* and *Carter’s Classics*, the *Tykes* brand was aimed at the discount channel. Its introduction coincided with a series of conversations with executives from Target, an emerging general merchandise retailer. Target was interested in expanding the store’s offerings in baby and children’s “lifestyle” clothing. With the assurance that Carter’s could keep its shelves “automatically replenished,” the companies struck a long-term deal in which the *Tykes* brand was made immediately available at all 972 Target stores across the country.

By the summer of 2001, Rowan seemed to have Carter’s on a path of operational and financial success. From 1992 to 2000, the company increased revenue at a compound annual growth rate of 9.5%, with earnings before income, taxes, depreciation, and amortization (EBITDA) increasing 22.1%. (See **Exhibit 4** for selected financials.) Analysts attributed much of the company’s growth to improved brand recognition, a lower cost structure, expansion into the discount channel, and the movement of some manufacturing operations offshore—while recognizing Investcorp as an able and willing partner in managing the growth.

2 Chris Roush, “Investment Bank Buys Morrow’s William Carter Co.,” *The Atlanta Journal-Constitution*, November 1, 1996.

**2**

**Berkshire Partners: Bidding for Carter's 205-058**

## Up for Sale

In mid-2000, having watched over the growth of its investment in Carter’s, Investcorp decided it was time to sell its stake in the company. Investcorp typically looked at a range of exit options, but at the time the initial public offering (IPO) market was at a near standstill. In Jones’s view: “Investcorp might have been able to take this company public in 2001. But they were at the end of a five-year period, and they wanted liquidity. So to sit there, take another year or two to work their way out of a public stock was not something they wanted.” He added: “They’ve [Investcorp] got a network of investors that fund them, but if you don’t have good returns coming out to keep talking about, it makes it harder to raise money. So in the normal course they were looking to generate a win through the sale of Carter’s.”

Amidst rumors that a handful of potential strategic buyers had passed on the deal, including apparel companies Jones Apparel and OshKosh B’Gosh, Investcorp initiated an auction among financial buyers. Christopher O’Brien, a member of Investcorp’s management committee, added: “The nature of this company’s business is that it is not particularly related to economic swings. We thought it was a company that financial buyers would find attractive in this marketplace.”3

# Berkshire Partners

Berkshire Partners was founded in the mid-1980s by five individuals committed to creating a private equity firm “based on successful relationships, hard work, analysis, and the open decision making of all individuals.”4 By 2001, the firm comprised roughly 10 managing directors, 4 principals, 12 investment staff (associate level), and 2 advising directors. In a given year, the firm reviewed some 1,200 potential deals, with the intention of whittling the pool down to five to six closed deals. Jones estimated the number of times per year the firm completed full due diligence and submitted a final bid at about 12: “Our batting average is pretty good—we tend to go all the way on things we think we have pretty good odds of winning. So we’re not making a run at 40 things and getting five. We’re doing it on 10–15, and we might get almost there on another handful.”

For each deal under serious consideration, Berkshire formed a deal team comprising four to five people. A managing director served as lead partner for each team. A team would typically contain an additional managing director, a principal, and one or two investment staff. According to Jones, “As a firm, our work is very inclusive and collaborative in our efforts to uncover all the key information.” While the deal team took responsibility for “making a recommendation and then doing due diligence and bringing back an investment package,” ultimate investment decisions rested with the firm as a whole.

In analyzing a potential deal, Berkshire relied largely on its internal staff to carry out the analysis and would “use a Bain and McKinsey to help us answer or flush out a couple of issues that we just don’t have the resources to do.” Beyond that, the firm relied on leading Boston law firms to carry out due diligence on contracts, leases, patents, and trademarks. Ernst & Young (E&Y) handled the firm’s accounting due diligence, which principally involved looking at quality of earnings.

According to Ascione, getting the capital structure right was “an art, not a science.” He added: “There are a lot of factors that go into determining the right financing structure. To start, there’s purchase price—dollars needed to ultimately buy the company. And, of course, there are your

1. Kelly Holman, “Berkshire Buys William Carter Co.,” *The Daily Deal*, July 17, 2001.
2. Berkshire Partners Web site, “Our Partnership,” [http://www.berkshirepartners.com/1\_0\_partnership.shtml,](http://www.berkshirepartners.com/1_0_partnership.shtml) accessed December 1, 2004.

**3**

**205-058 Berkshire Partners: Bidding for Carter's**

returns. Obviously, if I hold purchase price steady, and I increase my leverage, my equity returns will increase, and so on.” Berkshire managers believed the equity portion of the capital structure at the time needed to be at least 25% in order to achieve the desired ratings outcome and demonstrate to the lending base that Berkshire was making a serious commitment. At the time, investment banks were willing to lend at a rate of roughly four to five times EBITDA, with the multiple determined largely by market conditions. Ascione continued, “This is coupled with the challenge of asking yourself: Is this the appropriate amount of leverage for a business of this type; what do the ratings look like; how difficult will it be to get the financing completed; and what does that mean in terms of your total financing costs? These are all the variables that you play with to try to figure out the optimal capital structure for the business.”

After taking an equity position in a private business, Berkshire saw its role as supporting management in a variety of ways, including a) helping to prioritize key objectives, b) reviewing organizational design, c) helping to “build the bench” of key managers, and d) even leading the integration process in the event of a subsequent acquisition. Jones added:

I would say that we’ve done a lot of work over the last several years to be more thoughtful about how to address opportunities for companies up front and align strategically with management. So in thinking about how we add value, it is important to look at the work we do in due diligence not only as critical to making a smart investment decision, but also a critical foundation to operate from during the life of the investment.

At any given time, Berkshire held a portfolio of roughly 25 investments. About half of these businesses required very little of Berkshire’s management attention—the firm “was on top of these businesses” and fully expected to exit them in due course. About one-quarter of the businesses required a moderate level of attention, and another one-quarter required Berkshire to be “very focused on them.” Businesses garnering the largest amount of attention did so “because it’s the early stages, or we could still have a meaningful impact and they’re very important to our firm’s success.”

Berkshire’s typical exit strategy was sale of the company, rather than an IPO, by a ratio of about four to one. The firm’s conditions for exiting via an IPO were threefold: 1) a strong brand, 2) strong growth potential, and 3) a dramatic need for capital. Unlike many other private equity firms that often used an IPO to close out their ownership stake, Berkshire was more likely to initiate an IPO in the middle of its ownership with the intention of staying involved with the management and helping the company to grow. In many cases, a follow-on offer would ensue.

# Berkshire’s Bid for Carter’s

When Berkshire Partners received an invitation to participate in the auction for Carter’s, the investment team was initially optimistic about a potential match between the two organizations. The firm had developed a focus on “building strong, growth-oriented companies in conjunction with strong, equity-incented management teams.”5 Berkshire viewed Carter’s not simply as an apparel company in the retail space, but more as a consumer products company. According to Jones, Carter’s being “a really strong brand that could be leveraged across multiple channels” was something that “we found very appealing, and in general find appealing.”

1. Berkshire Partners Web site, “Press Releases,” [http://www.berkshirepartners.com/5\_1\_17\_press.shtml,](http://www.berkshirepartners.com/5_1_17_press.shtml) accessed September 1, 2004.

**4**

**Berkshire Partners: Bidding for Carter's 205-058**

## Initial Meeting

On the first Tuesday of May, Berkshire’s five-member team traveled to New York to meet with Carter’s management. The Carter team included the CEO, president of marketing, executive vice president of operations, executive vice president of global sourcing, and CFO. The meeting provided an opportunity for the respective managers to get to know one another, to discuss the ground rules for the auction, and to begin a dialogue about the future growth strategy for Carter’s. To a person, the Berkshire executives were very impressed with the Carter team, acknowledging their experience, commitment, and “confidence in their five-year plan.” (See **Exhibit 5** for four elements of growth strategy.)

The initial meeting also opened lines of communication between Berkshire and Goldman Sachs, which Carter’s had engaged to run the auction process. In the early weeks of May, Berkshire’s team had a number of discussions with Goldman Sachs. The deal was being shown to a limited number of financial buyers (“more than 2, less than 10”), and not all potential buyers would be given the opportunity Berkshire had been given to meet with the management team prior to submitting a preliminary bid. In addition to running the auction, Goldman Sachs was providing staple-on financing for the deal, although the buyers were not limited to the Goldman financing structure and could choose to submit a bid that would be financed by other sources. (See **Exhibit 6** for proposed capital structure.)

Members of the Berkshire team acknowledged that a staple-on financing structure, if not actually compared against competing offers in the market, could create a conflict of interest for an investment bank. A bank’s dual role of auctioneer and financier, if unchecked, could pressure a buyer to accept inferior financing terms in order to win the bid. Ascione stated:

There were a lot of tensions inherent in the new staple-on structure. The investment banks were concerned externally about how it would affect their reputations, and the private equity guys weren’t that excited about it. They felt it limited their ability to get an edge in the bidding process by bringing more creative financing to deals. What the staple-on did provide, however, was generally a more expedited financing process.

Nevertheless, the Berkshire team came away from the meeting in New York eager to look carefully into the deal. In the ensuing days, Goldman furnished Berkshire with a summary of financial projections put together by Carter’s management (see **Exhibits 7a**, **7b**, and **7c**). GS also indicated that the process required potential buyers to submit equity bids of at least $130 million to be considered.

## Preliminary Bid, Due Diligence

Berkshire submitted its preliminary bid on May 16, 2001. In preparing the bid, the Berkshire team consulted closely with its entire investment staff; though it understood its preliminary bid would not be binding, the team wanted to put forth at least a good-faith offer to sustain the interest Carter’s had shown.

Based on its preliminary bid as well as ongoing discussions with Goldman and Carter’s management, Berkshire was invited to participate in a second and final round of bidding along with a “handful” of other bidders. In addition, Berkshire was invited to a second management meeting in New York. The meeting provided Berkshire, which was accompanied by bankers and financial advisors from CSFB, Bank of America, and Bain, the opportunity to probe further the key components of Carter’s strategic plan while also deepening the personal relationships between the two parties. Berkshire viewed the meeting as collegial and productive. According to a member of the

**5**

**205-058 Berkshire Partners: Bidding for Carter's**

Berkshire team: “The team has worked hard in a short period of time to understand Carter’s. We have been aided in our process by a management team that is exceptionally adept at producing analysis and cutting data. It has given us comfort that the internal controls and systems of the company are in very good shape. Management is clearly on top of their business.”

Following this second meeting in New York, Goldman Sachs indicated that Berkshire was one of “two or three real people” under consideration, saying that while Berkshire had not been the high bidder during the preliminary round, Carter management rated the team high in “intangible” factors such as the rapport with which the two parties conducted business.

Goldman Sachs assured Berkshire that the choice of financing partner was “irrelevant” to the process, adding that “in no way will a bidder be disadvantaged by using a non-Goldman source.” As such, Berkshire solicited the views of a range of potential partners:

We asked Merrill, First Union, Bank of America, CSFB, and Lehman for their views on the deal. . . . Merrill, First Union, and Lehman all offered initial structures that were essentially similar to the Goldman Sachs staple-on financing. Bank of America and CSFB are currently contemplating a mix of senior, high-yield, and mezzanine or PIK [pay-in-kind] preferred. . . .

Both firms are continuing to work on the deal.

Before submitting its final bid, Berkshire researched the prospect of offering Carter’s in an IPO. In the face of a widely accepted view that the IPO market was weak to non-existent, the research suggested that there was, indeed, a market for a Carter’s IPO, predicting a favorable IPO opportunity as early as the fall of 2001. IPO pricing looked to be in the area of 16 to 18 times 2002 earnings. (See **Exhibit 8** for comparable company data.) At the time, interest rates were falling, with one-year U.S. Treasuries dipping to 3.7%, down from 6.1% the previous summer. The 10-year U.S. Treasury bond yield had fallen less, to 5.2%, down from 6.1%. LIBOR was at about 4.3%.

## Final Bid

With one week to go before the June 28 final bid deadline, the five-member Berkshire team sent a high-priority memo to colleagues in the investment department indicating it was time to complete the valuation of Carter’s—and to determine both a final bid and the required equity commitment.

**6**

**Berkshire Partners: Bidding for Carter's 205-058**

**Exhibit 1a** Berkshire Profile

Berkshire Partners is an active investor in the private equity market. In 2001, the firm managed approximately $1.7 billion of equity capital. Through its 15-year investment history, Berkshire completed 70 acquisitions or growth capital investments with a primary focus on building solid, growth-oriented companies in conjunction with strong, equity-incented management teams. Berkshire invests in a number of industries including manufacturing, retailing, transportation, telecommunications, and business services. Its private equity transactions have taken several forms: leveraged buyouts, recapitalizations, growth capital investments, privatizations, and industry consolidations. Investors consist primarily of university endowments, public and private pension funds, insurance companies, foundations, and financial institutions.

Source: Berkshire Partners Web site, “Press Releases,” [http://www.berkshirepartners.com/5\_1\_17\_press.shtml,](http://www.berkshirepartners.com/5_1_17_press.shtml) accessed September 1, 2004.

**Exhibit 1b** Berkshire Partners Capital under Management (in millions of dollars)

$1,200

$985

$387

$59

$125

$168

$800

$400

$0

Fund I - 1984 Fund II - 1986 Fund III - 1992 Fund IV - 1996 Fund V -

1998/2000

Source: Adapted from Berkshire Partners Web site.

**7**

**205-058 Berkshire Partners: Bidding for Carter's**

**Exhibit 2** Biographical Information

**Bradley M. Bloom** has invested in private companies since the late 1970s and has been a director of several of Berkshire’s retailing and manufacturing companies. Before founding Berkshire, he was a partner of the Thomas H. Lee Company for seven years and spent two years with The First National Bank of Boston. He earned an A.B. from Harvard College and an MBA from Harvard Business School.

**Ross M. Jones** joined Berkshire in 1993 and has worked with and been a director for a number of companies in business services, manufacturing, retailing, and communications. Prior to joining the firm, he worked at Bain & Co., where he assisted clients in a variety of industries, including food processing, container manufacturing, and steel distribution. He also worked in the investment banking division of Morgan Stanley & Co. Jones earned a B.A. from Dartmouth College and an MBA from Stanford University’s Graduate School of Business.

**Michael C. Ascione** joined Berkshire in 2001. Previously, Ascione was an associate at Inverness Management LLC, a private equity firm. He also worked as director of business development for an IT services firm. Earlier in his career, Ascione was a financial analyst in the corporate finance and principal investment areas at Goldman Sachs & Co. He received a B.A. from Boston College and an MBA from Harvard Business School in 1998.

**Frederick J. Rowan**, II, joined us in 1992 as president and chief executive officer and became chairman of our board of directors in October 1996. Prior to joining us, Rowan was group vice president of VF Corporation, a multidivision apparel company and, among other positions, served as president and chief executive officer of both The HD Lee Company Inc. and Bassett-Walker, Inc., divisions of VF Corporation. Rowan, who has been involved in the textile and apparel industries for 38 years, has been in senior executive positions for nearly 26 of those years. Rowan began his career at the DuPont Corporation and later joined Aileen, Inc., a manufacturer of women’s apparel, where he subsequently became president and chief operating officer.

Source: Adapted from Berkshire Partners Web site and Hoovers.com.

**8**

**Berkshire Partners: Bidding for Carter's 205-058**

**Exhibit 3** Investcorp Profile

Investcorp is a leading global investment group with offices in New York, London, and Bahrain. Since 1982, it has completed transactions in North America and Western Europe, with a total acquisition value of approximately $19 billion. Investcorp and its clients currently have investments in U.S. companies including Stratus Technologies, Jostens, Inc., Werner Holdings, TelePacific Communications, and Independent Wireless One. U.S. investments that have been taken public by Investcorp include Prime Service, Tiffany & Co., Circle K Corporation, Saks Fifth Avenue, and CSK Auto Corporation.

* Acquisitions are typically funded with a combination of debt and equity. Unlike other private equity firms, Investcorp underwrites the equity portion of these investments using its own capital.a
* Investcorp had a shareholder capital base of $1.2 billion and total assets of $4.1 billion, of which $1.8 billion is in liquid funds.

Source: Adapted from Berkshire Partners Web site, “Press Releases,” [http://www.berkshirepartners.com/5\_1\_17\_press.shtml,](http://www.berkshirepartners.com/5_1_17_press.shtml) accessed September 1, 2004; and from Investcorp Web site, “About Investcorp,” <http://www.investcorp.com/> Template1a.aspx?pageid=AI6.0, accessed September 1, 2004.

aSubsequent to each acquisition, Investcorp offers the equity to its client base of individuals and institutions. The firm believes that because each investment is placed separately with its clients, it must account for the success of every investment on an individual basis, thus focusing attention on the performance of every one of its portfolio companies.

**9**

**205-058 Berkshire Partners: Bidding for Carter's**

**Exhibit 4** Carter’s Historical Financial Data (in thousands of dollars)

|  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- |
|  | | | | | | **Six Months Ended June 30,** | **Six Months Ended June** |
|  | **1996** | **1997** | **1998** | **1999** | **2000** | **2000** | **30, 2001** |
| Wholesale sales | 188,991 | 219,535 | 236,486 | 231,284 | 256,094 | 105,300 | 123,655 |
| Retail sales | 129,244 | 143,419 | 171,696 | 183,312 | 215,280 | 88,374 | 97,370 |
| **Total net sales** | **318,235** | **362,954** | **408,182** | **414,596** | **471,374** | **193,674** | **221,025** |
| Cost of goods sold | 200,798 | 227,332 | 256,482 | 271,844 | 293,340 | 121,521 | 140,996 |
| **Gross profit** | **117,437** | **135,622** | **151,700** | **142,752** | **178,034** | **72,153** | **80,029** |
| Selling, general and administrative | 96,905 | 112,531 | 124,278 | 120,773 | 137,513 | 62,729 | 68,827 |
| Nonrecurring charges | 8,834 | 0 | 0 | 7,124 | 0 | 0 | 4,272 |
| **Operating income** | **11,698** | **23,091** | **27,422** | **14,855** | **40,521** | **9,424** | **6,930** |
| Interest income | 0 | 0 | 0 | 0 | -303 | 0 | -68 |
| Interest expense | 9,706 | 17,571 | 18,525 | 17,748 | 16,294 | 7,919 | 7,907 |
| Earnings before income taxes | 1,992 | 5,520 | 8,897 | -2,893 | 24,530 | 1,505 | -909 |
| Provision for income taxes | 2,097 | 2,429 | 3,616 | -869 | 9,731 | 607 | -364 |
| Extraordinary items, net of tax | 2,351 | 0 | 0 | 0 | 354 | 354 | 0 |
| **Net Income** | **-2,456** | **3,091** | **5,281** | **-2,024** | **14,445** | **544** | **-545** |
| **Other Data:** |  |  |  |  |  |  |  |
| EBITDA | 29,558 | 36,926 | 43,021 | 38,834 | 58,041 | 17,526 | 20,627 |
| Capital expenditures | 7,756 | 18,625 | 22,262 | 8,957 | 20,185 | 5,908 | 3,549 |
| Working capital, net | 70,792 | 87,482 | 99,480 | 81,508 | 84,336 | 93,550 | 81,470 |
| Property, plant & equipment, net | 48,221 | 53,011 | 59,674 | 51,776 | 54,441 | 49,483 | 48,565 |
| Depreciation and amortization | 9,026 | 13,835 | 15,599 | 16,855 | 17,520 | 8,102 | 9,425 |
| Total debt | 145,000 | 157,100 | 167,600 | 142,300 | 141,400 | 156,250 | 156,700 |
| Redeemable preferred stock | 18,234 | 18,462 | 18,682 | 18,902 | 19,116 | 19,016 | 19,236 |
| Common stockholders’ equity | 57,488 | 56,721 | 58,739 | 53,615 | 65,397 | 52,832 | 63,525 |

Source: Adapted from company materials.

**10**

**Berkshire Partners: Bidding for Carter's 205-058**

**Exhibit 5** Carter’s Growth Strategy

* **Capitalize on leading market position** Noting that the top eight wholesale customers represented 74% of wholesale revenue and that the company was the leading retailer in the baby and young children’s apparel market, management intended to “build on relationships with major customers, and to develop our network of profitable retail outlet stores.”
* **Diversify distribution channels** Management estimated the discount market for baby and young children’s apparel at approximately $5.3 billion annually.
* **Continue to extend Carter’s into the two- to six-year-old playwear market** Carter’s estimated the size of the combined baby and young children’s playwear segments at $9.5 billion annually. Management also observed that no single competitor represented more than 7% of the baby playwear market or 5% of the young children’s playwear market.
* **Increase operating efficiencies** 2003 was the target date for 100% offshore sourcing of manufacturing. In addition, the company was in the process of reducing its product development cycle by implementing initiatives to shorten each stage of the development calendar.

Source: Adapted from company materials.

**Exhibit 6** Goldman Sachs Proposed Capital Structure (in millions of dollars)

|  |  |  |  |
| --- | --- | --- | --- |
| **Tranche** | **Amount** | **Maturity** | **Fully Drawn Cost** |
| Revolvera | 60.0 | 5 years | LIBOR + 3.00% |
| Term Loan B | 125.0 | 7 years | LIBOR + 3.75% |
| Total Credit Facility | 185.0 |  |  |
| Senior subordinated notes | 175.0 | 10 years | 10.875% |
| Source: Adapted from company materials. |  |  |  |

aProjected $17.5 million funded at close, of which $12.5 million is related to seasonal working capital.

**11**

**205-058 Berkshire Partners: Bidding for Carter's**

**Exhibit 7a** Summary of Management Projections (in thousands of dollars)

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
|  | **2001E** | **2002P** | **2003P** | **2004P** | **2005P** | **2006P** |
| **Net Sales** | **537,300** | **618,800** | **711,600** | **817,300** | **938,800** | **985,740** |
| % growth | 13.8% | 15.2% | 15.0% | 14.9% | 14.9% | 5.0% |
| **Gross Profit** | **221,900** | **260,900** | **302,400** | **348,300** | **400,400** | **420,420** |
| Margin | 41.3% | 42.2% | 42.5% | 42.6% | 42.7% | 42.7% |
| **SG&A** | **146,800** | **172,200** | **193,300** | **214,100** | **238,800** | **250,740** |
| % of sales | 27.3% | 27.8% | 27.2% | 26.2% | 25.4% | 25.4% |
| **EBITDA** | **75,100** | **88,700** | **109,100** | **134,200** | **161,600** | **169,680** |
| % of sales | 14.0% | 14.3% | 15.3% | 16.4% | 17.2% | 17.2% |
| **EBIT** | **55,100** | **67,600** | **87,300** | **109,800** | **133,500** | **140,175** |
| % of sales | 10.3% | 10.9% | 12.3% | 13.4% | 14.2% | 14.2% |
| **Capex** | **20,500** | **19,500** | **21,000** | **21,500** | **22,500** | **22,500** |
| % of sales | 3.8% | 3.2% | 3.0% | 2.6% | 2.4% | 2.3% |

Source: Adapted from company materials.

**Exhibit 7b** Revenue Projections by Channel (in millions of dollars)

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
|  | **2000A** | **2005E** | **2005E–**  **2000A**  **Change** | **% of**  **Projected Growth** | **Projected CAGR** | **96–00**  **CAGR** |
| Kohl’s | 35.0 | 137.0 | 102.0 | 21.9% | 31.4% | 56.1% |
| Kids R/Babies R Us | 36.8 | 61.8 | 25.0 | 5.4% | 10.9% | 16.5% |
| Other Wholesalea | 181.2 | 255.2 | 74.0 | 15.9% | 7.1% | 2.7% |
| Targetb | 4.0 | 100.0 | 96.0 | 20.6% | 90.4% | -- |
| Outlet Stores | 215.3 | 329.0 | 113.7 | 24.4% | 8.9% | 13.6% |
| Full-Price Retail Stores | 0.0 | 56.0 | 56.0 | 12.0% | -- | -- |
| **Total** | **472.3** | **939.0** | **466.7** | **100.0%** | **14.7%** | **10.4%** |

Source: Adapted from company materials.

aIncludes JC Penney, Mervyn’s, Federated, May, Sears, and others. Also includes off-price and some licensing.

bFull target rollout to all 972 stores completed in January 2001. Management projected $25 million in revenue for 2001.

**12**

**Berkshire Partners: Bidding for Carter's 205-058**

**Exhibit 7c** Revenue Projections by Product (in millions of dollars)

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
|  | **2000A** | **2005E** | **2005E–2000A**  **Change** | **% of Projected Growth** | **Projected CAGR** | **96–00**  **CAGR** |
| Wholesale Baby | 120.0 | 177.0 | 57.0 | 12.2% | 8.1% | 9.4% |
| Wholesale Sleepwear | 91.9 | 130.0 | 38.1 | 8.2% | 7.2% | 11.5% |
| Wholesale Playwear | 24.1 | 125.0 | 100.9 | 21.6% | 39.0% | -1.3% |
| Off-Price | 17.0 | 22.0 | 5.0 | 1.1% | 5.3% | 4.2% |
| Outlet Baby | 40.7 | 61.5 | 20.8 | 4.5% | 8.6% | 18.0% |
| Outlet Sleepwear | 34.3 | 48.7 | 14.4 | 3.1% | 7.3% | 11.7% |
| Outlet Playwear | 83.9 | 148.3 | 64.4 | 13.8% | 12.1% | 11.1% |
| Outlet Other | 56.4 | 70.8 | 14.4 | 3.1% | 4.7% | 14.2% |
| Target (Baby) | 4.0 | 100.0 | 96.0 | 20.6% | 90.4% | -- |
| FullPrice Retail | 0.0 | 56.0 | 56.0 | 12.0% | -- | -- |
| **Total** | **472.3** | **939.3** | **467.0** | **100.0%** | **14.7%** | **10.4%** |

Source: Adapted from company materials.

**13**

**205-058 -14-**

**Exhibit 8** Comparable Company Data, June 2001 (in millions of dollars except where noted)

**Stock**

**Earnings**

**Interest-**

**5-Year**

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Source: Adapted from company materials.

|  |  |  |  |  |  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
|  | **Price 6/13/01** | **P/E 2001E** | **P/E 2002E** | **Growth Rate** | **IPO**  **Date** | **Equity Betaa** | **Revenue** | **EBIT** | **EBITDA** | **Bearing Debt** | **Market Capitalization** | **Average Leverage** | **Net Income** |
| Nike | $41.35 | 19.2x | 15.8x | 15% | 1980 | 1.0 | 9,488.8 | 1,014.2 | 1,211.6 | 1,296.6 | 7,224.3 | 8.4% | 589.7 |
| Jones Apparel Group | $40.90 | 13.7x | 12.0x | 17% | 1991 | 1.1 | 4,115.3 | 645.9 | 757.3 | 1,482.1 | 5,343.6 | 17.1% | 327.6 |
| Tommy Hilfiger | $13.65 | 9.0x | 7.9x | 10% | 1992 | 1.3 | 1,836.7 | 194.6 | 302.1 | 567.0 | 1,245.7 | 18.1% | 130.2 |
| Liz Claiborne | $24.92 | 12.3x | 10.9x | 12% | 1981 | 1.2 | 3,186.7 | 333.4 | 417.9 | 519.6 | 2,650.2 | 4.4% | 184.6 |

aEquity betas were calculated based on five-year monthly returns.