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## Lululemon Athletica

Lululemon Athletica (Lululemon, or Lulu for short) was founded in 1998 by Dennis J. “Chip” Wilson. By 2015, the company had grown to \$1.8 billion in revenue.<sup>1</sup> The brand had a “cult-like” following among young upscale women, sometimes referred to as “Luluheads,” for whom the clothing was their go-to attire not only for yoga and other exercise but also for everyday casual wear.

In June 2015, Wilson’s involvement with the company was coming to a close. Wilson, who remained active in the management of the company until 2012 and served on the board until February 2015, already had sold half his shares to a private equity firm, Advent International, for \$845 million, and the company had filed for him to sell his family’s remaining shares, which were valued at roughly \$1.3 billion.<sup>2</sup>

This final step in Wilson’s separation from the company he had built was not a surprise. His relationship with the company’s board of directors had grown increasingly acrimonious after controversial statements Wilson made to the press in the wake of product quality problems in 2013. Further, Wilson’s wife and son had begun a new retail venture, Kit and Ace, which some viewed as competing with Lululemon. Regardless of the motivation, the timing of Wilson’s stock sale could prove fortuitous. Although the women’s segment of the activewear category was growing, competition in the category had intensified with both Under Armour and Gap’s Athleta investing heavily. In 2015, Lululemon’s growth rate slowed and its earnings per share declined.<sup>3</sup> Analysts held differing opinions about the company’s future. Some speculated that the company might have ample room for growth both with its core female customer base and with men, who accounted for a relatively small portion of Lululemon’s revenue. Others feared that the fashion-conscious women who favored Lululemon might be tiring of the look and ready to move on to some other form of casual wear and that men might be reluctant to adopt a brand so strongly tied to women and yoga. Had Wilson sold his stock at its peak, or had he gotten out too soon?

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## Company Overview

In 1979, Chip Wilson founded Westbeach Snowboard Ltd., a company devoted to surf, skate, and snowboard clothing. While at Westbeach, Wilson worked with suppliers to create an expensive stretch fabric for high-end long underwear. Shortly after selling the company in 1997, he took a yoga class and experienced a post-yoga “high” that convinced him that the practice of yoga would grow. Wilson believed he could leverage his experience with technical performance fabrics to create yoga attire that would be both more functional and flattering than the cotton clothing that was common at the time. Wilson and his team created yoga pants that stretched and moved with the body while also lifting and shaping the wearer’s posterior. Initial feedback from yoga practitioners who tried the pants convinced Wilson the product was a winner.

The first Lululemon store opened in 2000, in Vancouver, Canada. The company’s stated mission was “creating components for people to live longer, healthier, more fun lives,” with the vision of “elevating the world from mediocrity to greatness.”<sup>4</sup> This mission and vision took inspiration from Ayn Rand, author of the 1957 novel *Atlas Shrugged*. Rand espoused the philosophy that “naked pursuit of self-interest should be society’s highest ambition.”<sup>5</sup>

Wilson created the name Lululemon with the goal of incorporating the letter L multiple times. He believed that, because the letter does not exist in Japanese phonetics, the multiple Ls would create the perception that the brand was North American and this would heighten its appeal to Japanese consumers. Wilson’s focus on how the company would be perceived by the Japanese was the result of his prior success in selling a previous company to Japanese investors.<sup>6</sup> The company logo, which resembles the symbol for Omega, is a stylized “A” for Athletica.

By 2006, Lululemon had revenue of \$84 million and gross margins of 51 percent.<sup>7</sup> When it launched its IPO in July of 2007, the company had 59 stores in Canada, the United States, Australia, and Japan.<sup>8</sup>

Although Chip Wilson stepped down as CEO prior to the IPO, he remained involved in management of the company under the title of chief innovation and branding officer until January 2012 and continued in his role as chairman of the board until 2013.<sup>9</sup> Wilson resigned from the board in 2015.

In 2015, the company reported revenue of nearly \$1.8 billion and gross margins were in excess of 50 percent. Nevertheless, year-over-year growth had slowed from 106 percent in 2006 to just under 13 percent in 2015, which raised concerns about the future.<sup>10</sup>

## Target Customers

Wilson defined the target customer for Lululemon as a woman between 18 and 34 years old who was fit, health-conscious, fashion-forward, and had high disposable income.

*[She is] a sophisticated and educated woman who understands the importance of an active, healthy lifestyle [and who] is increasingly tasked with the dual responsibilities of career and family and is constantly challenged to balance her work, life and health, pursues exercise to achieve physical fitness and inner peace, and purchases based on an actual need for functional products and a desire to create a particular lifestyle perception.<sup>11</sup>*

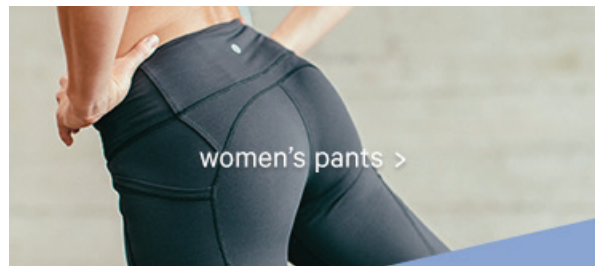
Lululemon developed the “Ocean” persona to inspire the line of clothing. Ocean is a 32-year-old professional woman who is single and earns \$100,000 per year. Wilson described Ocean as “engaged, has her own condo, is traveling, fashionable, has an hour and a half to work out a day.” Ocean was intended to be aspirational for younger women and nostalgic for older women.<sup>12</sup>

Women were drawn to Lululemon clothing because, as a New York City yoga instructor explained, “Lululemon was the first place that provided workout clothes that women weren’t embarrassed to be seen in [and in which] they could even grab dinner after yoga if they wanted to.”<sup>13</sup>

When the company expanded into menswear, it added the “Duke” persona. Duke is 35 years old and makes more money than Ocean. He was described as an “athletic opportunist’ who enjoys surfing in the summer and snowboarding in the winter,” and he is willing to pay for quality.<sup>14</sup>

## Product Line

Initially, Lululemon focused on yoga apparel. Its signature Groove pants were made of Luon, a fabric that was developed and produced by a single supplier in Taiwan, Eclat Textile Co.<sup>15</sup> The pant had flat seams and special gussets that created a snug gluteal enclosure (**Figure 1**). Wilson observed, “Women wanted well-fitting athletic clothing that also attracted the eye.” He also said the pants were designed to provide a “remarkable rear view.”<sup>16</sup> Over time, the company expanded the product line to include jackets, hoodies, pants, shorts, and underwear for both men and women for a variety of sports.



**Figure 1:** Lululemon’s Signature Yoga Pants

Lululemon built its reputation by offering innovative, high-quality products, many of which were protected by design patents, which the company enforced vigorously. In 2012, Lululemon sued Calvin Klein for infringement on a patent covering the overlapping fabric design of the waistband on their popular Astro pants.<sup>17</sup> In 2014, it sued Haneswear for infringement on a patent protecting its tank top with a built-in bra. Both cases were settled out of court.<sup>18</sup>

Nevertheless, both the validity of some product claims and product quality had been called into question on occasion. In November 2007, the company asserted that its VitaSea clothing was made from seaweed and had “anti-inflammatory, antibacterial, hydrating and detoxifying benefits.” When laboratory tests failed to support these claims, a Canadian oversight agency required that they be removed.<sup>19</sup>

In March 2013, Lululemon was forced to recall 17 percent of its popular black yoga pants because the fabric was too sheer. The negative impact of the recall was compounded when women trying to return the pants at some stores were asked to put them on and bend over so that the staff could assess just how sheer they were.<sup>20</sup> Shortly thereafter, in November 2013, customer complaints surfaced that the yoga tights were prone to “pilling” of the fabric in the inner thigh. Further, in June 2015, the U.S. Consumer Product Safety Commission and Health Canada issued

a joint recall of 300,000 Lululemon tops, citing the concern that the plastic and metal tips on the elastic draw cords in the neck area had the potential to snap back and cause injury to the wearer's face if they were accidentally pulled.<sup>21</sup>

## Promotion

Lululemon relied on grassroots/community-based marketing to build the brand. It recruited a select set of yoga instructors, chosen because they embodied the corporate culture and were respected in the community, to serve as brand ambassadors. These instructors received free clothing; in exchange, they conducted free yoga classes for customers in Lululemon stores. In addition, all certified fitness instructors were eligible to receive a 15 percent discount in exchange for providing product feedback.<sup>22</sup> Message boards for posting community information related to health and wellness events were also placed in the stores.

Reusable bags featured the company's manifesto (Figure 2) and served to promote healthy, positive living. The slogans, such as "Friends are more important than money" and "Do one thing a day that scares you," were seen by some as inspiring and by others as contrived. Detractors questioned the fit between the fundamental values that underpin yoga and the company's emphasis on self-interest and focus on selling expensive gear designed to enhance one's appearance.<sup>23</sup>

Lululemon used sponsorship of teams and events to raise its profile with male athletes. It provided the uniforms for the 2012 Olympic Men's Volleyball Team, as well as the shorts and shirts for the 2013 Wall Street Decathlon.<sup>24</sup>

The company did not invest in traditional advertising, but occasionally YouTube videos were posted and gained broad viewership. For example in 2011, the company created a tongue-in-cheek video building on the "Sh\*t [People] Say" theme ([https://www.youtube.com/watch?v=IMC1\\_RH\\_b3k](https://www.youtube.com/watch?v=IMC1_RH_b3k)). The strategy of poking fun at yoga culture (and by implication Lululemon customers) was a bit risky but the video received a generally positive response and was viewed by millions. During the 2014 holiday season, the company adopted a more serious tone, posting a video that drew on yoga principles in arguing for giving "presence" rather than "presents" (<https://www.youtube.com/watch?v=86qAkvaCgso>).

However, controversial statements made by Wilson generated negative press coverage on multiple occasions. In 2005, Wilson mocked the difficulty that the Japanese had pronouncing the company name and referred to plus-sized clothing as a "money-loser" because it required 30 percent more fabric but could not be priced 30 percent higher. In 2009, he enraged some customers when, in a blog post, he linked the introduction of birth-control pills to rising divorce rates and



Figure 2: Lululemon's Manifesto

argued that birth-control pills, coupled with the stress women experience in the working world, led to a rise breast cancer in the 1990s.<sup>25</sup> And in 2013, Wilson deflected criticism that the company's yoga pants pilled because of poor quality by remarking that "some women's bodies just actually don't work for yoga pants." Wilson also said the pilling was caused by "rubbing through the thighs, how much pressure is there over a period of time."<sup>26</sup>

## Pricing

Lululemon employed a premium pricing strategy. In 2015, its trademark yoga pants retailed for \$98 compared with \$79 or less for competitors' brands. Further, it employed the strategy of limiting the supply of items to discourage consumers from waiting for items to go on sale. As a result, the vast majority of items sold at full price. Indeed, a market arose for used Lululemon clothes and even for the stores' reusable shopping bags. Clothes had sold for 60 percent of their original price online; bags, which were free at the store, had sold on e-Bay for \$5.<sup>27</sup>

## Distribution

Lululemon products were distributed through company-owned stores and direct-to-consumer channels. In 2015, 280 Lululemon stores with more than 8,600 employees were located around the world. Direct-to-consumer sales accounted for 17.9 percent of revenue.<sup>28</sup>

The retail stores were relatively small, but they had a very high average sale per square foot because of the high price of the products. The revenue per square foot for a Lululemon store in 2014 averaged \$1,675.16, making it the fourth-highest revenue per square foot retail store, behind Apple (\$4,798.82), Tiffany (\$3,132.20), and Michael Kors (\$1,895.65), and well ahead of chains such as The Gap (\$361).<sup>29</sup>

Lululemon store managers had considerable autonomy in the operation of their stores. They hired employees, selected the layout of merchandise, and managed store events. Store employees were referred to as "educators" and received extensive training – 30 hours in their first three months on the job. They were encouraged to personalize their interactions with customers by writing the customer's name on their dressing room door. Further, a large folding table was located in the dressing room area so that employees could both eavesdrop on customers' conversations as they refolded merchandise and be on hand to offer input and retrieve alternative sizes.

Consistent with Wilson's philosophy, the company prioritized personal achievement for its employees. All employees set – and posted in the common break room – goals for one, five, and ten years. They also were encouraged to attend motivational seminars at the Landmark Forum<sup>30</sup> and to wear Lulu attire at yoga classes. The company covered both of these expenses. At the outset, the company hired only professional yoga instructors as educators, but it quickly concluded they were not "Type A" enough for the company's culture. Instead, it turned to hiring runners who enjoyed yoga.<sup>31</sup>

Wilson pioneered a policy, which was continued by his successors, of paying above the going retail wage and offering good healthcare benefits to full-time employees to generate loyalty and reduce turnover. Employees also received generous discounts on the clothing and were encouraged to take free weekly yoga or fitness classes. Nevertheless, some employees posted complaints online

about unpaid work hours and the need to embrace the company culture (“gotta drink the Koolaid”). Others noted that the quality of the work experience was heavily dependent on the store manager. (“If you find a store with a good manager, your job will be amazing. If not, it will be horrible.”<sup>32</sup>)

## The Activewear Market

In 2014, the U.S. apparel market reached \$206.3 billion. Activewear accounted for 16 percent of the market, or \$33.7 billion. Whereas the growth of the overall apparel market was a mere 1 percent, the activewear segment grew by 7 percent.<sup>33</sup> Some of this growth appeared to occur at the expense of jeans, which declined by 6 percent.<sup>34</sup> Industry analysts suggested that the athleisure trend (the fashion trend of wearing workout clothing in other settings) would continue to grow the activewear category given the trend’s fit with millennials’ attitudes as well as overall wellness trends that incorporated physical activity into everyday life. A recent NPD press release noted, “In today’s world, it seems everyone is an athlete, an outdoorsman, and a yogi. Or wants to be. Or at least wants to look like one.”<sup>35</sup> In fact, the top uses for activewear were casual/everyday use, followed by athletic/sport/exercise and school.

Activewear included a broad range of sports- and activity-inspired clothing and footwear. Not all competitors enveloped by the industry term covered that full gamut, however; brands and retailers had strategically carved out their own spaces in the very large activewear sandbox. Both Under Armour and Athleta (the most recent addition to Gap’s stable of retail brands) sought to capitalize on the market growth, with a particular focus on women.

## Under Armour

Under Armour was founded in 1996 by Kevin Plank. The initial product line was focused on men’s athletic wear, such as compression shorts and moisture-wicking shirts, which were inspired by Plank’s memories of his discomfort during hot-weather football practice sessions when he played football at the University of Maryland. In 2006, the company expanded its product line to include footwear, beginning with cleats for various sports and then adding training shoes. In 2010, the company began to invest heavily in the women’s athletic-apparel market as an avenue for continuing its growth. In 2015, the company’s revenue was \$3.96 billion, which represented a 28 percent growth over the previous year.<sup>36</sup>

Under Armour distributed its products through independent retailers (70 percent of sales, nearly 20 percent of which came from big-box sporting goods retailers) and direct-to-consumer channels (30 percent of sales). It gained visibility through its relationships with Major League Baseball, the National Hockey League, and collegiate athletic teams. The company also had been effective in using celebrity athletes in its advertising, sometimes anticipating which players would achieve superstar status and signing them just before they gained such prominence. These included such athletes as Stephen Curry, who was crowned as the National Basketball Association’s most valuable player, and golfer Jordan Spieth, who won the Masters’ tournament, after they had signed as spokesmen for Under Armour.

Under Armour’s campaign targeting women emphasized goal achievement. This was conveyed by featuring world-class female athletes such as Olympic skier Lindsey Vonn and Olympic gold-medal soccer player Lauren Cheney. The *I Will What I Want* campaign, which began in 2014,

leveraged the insight that a segment of women perceived sports and other active endeavors as an exercise of will. In 2013, roughly 30 percent of Under Armour's sales were to women, and Plank speculated that one day the company's sales to women would exceed its sales to men.<sup>37</sup>

In a Bloomberg interview, Chip Wilson indicated he had considered buying Under Armour in 2012 when Lululemon's value was double that of Under Armour. By 2015, however, Under Armour's value was triple that of Lululemon, and some speculated that Lululemon might be bought instead.<sup>38</sup>

## Athleta

Athleta was founded in 1998 as a catalog and website company devoted exclusively to women's activewear. It was acquired by Gap in 2008 for \$150 million and opened its first full-scale retail store in San Francisco in 2011.<sup>39</sup> By 2015, the company had more than 100 stores.<sup>40</sup>

Seeking to capitalize on activewear growth and to compensate for the decline in jeans at Gap's other three retail brands, Athleta targeted women who "always want more out of sports and life," and who sought athletic and active wear for the "performance lifestyle," which was how the company referred to the athleisure trend. The advertising campaign *Power to the She* had been characterized as presenting the brand as apparel that had it all, for women who wanted it all (Figure 3).<sup>41</sup>

Experts noted that Athleta had taken more than a few pages out of Lululemon's playbook, particularly in its yoga apparel line.<sup>42</sup> It employed a community-based approach to marketing, providing discounts to fitness professionals and holding workout classes in its stores, a number of which were located within a mile of Lululemon stores.

It also highlighted the technical performance features of its attire, for example by making its fabrics "unstinkable" by incorporating natural silver salts. And, like Lululemon, Athleta put its heaviest emphasis on design.

That said, Athleta differed on a handful of dimensions, both tactical and strategic. The company focused solely on women. It also had developed broad product lines around casual wear and running and water sports, recently adding attire for tennis and golf. Price points in competing products with Lululemon, like yoga pants, were about 20 percent lower at Athleta. In addition, Athleta gave fitness professionals greater discounts on attire: 30 percent versus 15 percent at Lululemon. Finally, Athleta offered a broader range of sizes. While Lululemon focused solely on sizes 2 to 12, Athleta offered sizes 00 to 16 in stores, with plus-size and maternity options online.



Figure 3: Athleta's Power To The She Campaign

## Summary

Lululemon was at a transition point. The company's initial success was built on serving the neglected attire needs of a narrow segment, yoga practitioners. The flattering fit of the clothing led many women to use the gear not just for yoga or other sports but also for everyday wear. Thus, Lululemon was an early player in crossover apparel that became known as activewear or athleisure. The size and growth of this category had attracted large, well-funded competitors. The company's challenge now was to develop a strategy for competing in this new environment. Where do the growth opportunities lie in the activewear market? How well-aligned with these opportunities are Lululemon's brand positioning and marketing mix strategy compared to other players in the activewear market? Answers to these questions will determine whether Chip Wilson sold his company stock at its peak or got out too soon.



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