JCAP

E-Commerce
United Kingdom

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Coverage Initiation

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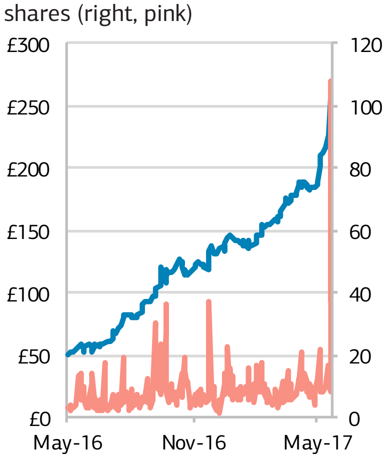
Boohoo.com (BOO LN)

Price	£2.64
Market Cap	£2,980.00
Rating	**SELL**
Price Target	**£1.31**
Difference	50%
Forecast Growth 2018	58%
Current Multiple of Sales	10.1
J Cap Multiple of Sales	5.0

Boohoo (BOO LN) last share price in GBP (left, blue) and volume in mln shares (right, pink)



Source: Bloomberg

Boohoo.com (BOO LN)

All Dressed Up

Few Are Chosen

Pretty much anyone can go into online retailing. Survivors are those that can manage their growth, and Boohoo is challenged. Online reviews suggest that the quality of services is materially declining. Ebitda has been propped up by cutting marketing costs, but gross margins are in decline, and heavy capex lies ahead.

Over-Valued

At 10x sales, the valuation of Boohoo.com is simply too rich. Growing into its valuation would entail very significant capital expenditure as well as faultless execution. The stratospheric rise and abrupt decline of U.S. company Nasty Gal, now acquired by Boohoo, is an object lesson in how tough that is to do.

Family Business

Around 50 family-owned companies operating out of the same premises as BOO create the possibility, if not the reality, of opaque related-party transactions that could potentially make Boohoo's margins appear better than they really are. Some of the co-located companies are disclosed suppliers. At the time of AIM admission, in 2014, Boohoo was buying 40% of its product from family companies.

Low Entry Barriers

There are a dozen businesses almost exactly like Boohoo in Manchester, England, and most of them seem to be struggling to make money. We don't see what should give Boohoo a sustainable advantage.

We Choose ASOS

Competing against Amazon is very tough, but if anyone can do it, industry-leader ASOS is the more likely candidate.

Summary View

Boohoo may be stumbling.

Boohoo, an online clothing site, is offering a cheap but edgy line of fashion under a powerful brand emotionally connected to its target buyers. Its growth has been phenomenal. But the hard thing in this business is not really creating the brand but sustaining it through profitable growth. It's science, not art. Right now, Boohoo seems to be stumbling. The growth is there—BOO has nearly tripled sales in the scant two years between 2015-2017, from GBP 139 mln to GBP 295.6 mln—but customers grumble about slipping standards. Spending on marketing has been suppressed but that probably won't last. To compete, heavy capital investment lies in BOO's near future. The company is unlikely to grow into its rich valuation and maintain profit levels.

On top of that, Boohoo's margins seem too good to be true. One-quarter the size of industry leader ASOS, Boohoo boasts more than double its ebitda and net margins. Meanwhile, Boohoo buys from a blinding array of family-owned companies—and then acquires the companies. Even a sincere effort to keep it all at arm's length would find the arrangements challenging.

The Company

Boohoo.com (BOO LN) is a U.K.-based, online-only "fast fashion" retailer. Founded in 2006 and listed in 2014, BOO sells private-label fashion products for both women and men, targeting the younger, 16- to 24-year-old demographic. Already by 2013, 35% of orders were by mobile. By 2017, mobile orders were 70%.

Boohoo's brand is affordable, young, not too sappy but not off-putting.

BOO has developed a great brand, affordable, young, not too sappy but not off-putting. It suits the Instagram generation, who prefer to order clothes on their phones rather than visiting shops and who may toss out an outfit after wearing it once to a party. BOO manages fast inventory turns: it trials a limited number of each design, monitors sales when launched, and then orders more of the most popular styles. The company's design process starts three months ahead of a new season.

BOO hails from the Midlands, the heart of the U.K. textiles and fashion industry, where small manufacturers ruthlessly pare their costs in order to eke out perilously thin margins. Boohoo's home, Manchester, is a hothouse for online fashion and home as well to ASOS and Missguided, the as-yet unlisted runner-up in the online fast-fashion world. A century ago, 80%

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of the world's cotton passed through Manchester, whose Dickensian brick architecture housed dyeing, cutting, weaving, and sewing mills. The great offshoring movement of the 1970s-1990s changed that, and England's textiles industry hollowed out.

As the large mills folded up and manufacturers moved operations overseas, fast fashion, with its demand for small runs and quick time to market, brought small, low-cost textile shops back to Manchester. The Cheetham Hill area of Manchester is the hot, molten core of the city's wholesale industry, streets filled with small textiles firms, import-export companies, and wholesalers. Cheetham Hill has a disproportionate share of immigrants, many of them Muslim and non-English speaking, and they are a vulnerable source of cheap labor. Cheetham Hill is also known as a minor capital of knock-off fashion and accessories. Companies coming out of this region learn how to manage costs. This is the region where Boohoo was born.

Warehouses in the Cheetham Hill area of Manchester. | Photo by J Capital June 7, 2017

Online players come and go, distinguishing themselves with a slightly different look and a nuanced positioning. The largest and most successful of the online fashion companies is ASOS ("As Seen On Screen"), which, at GBP 1.44 bln, is four times the size of Boohoo. Next comes Boohoo, then the as-yet-unlisted Missguided, which reported GBP 117.2 mln in revenue in the year ending February 28, 2016, which was half of Boohoo's revenue

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at the time. Other local firms include Manier de Voir, Matalan, Lavish Alice, Little Black Dress, Sosander, She Likes, and more. Those are just the online companies. Offline/online fast-fashion contenders include The Hut, Matalan, Topshop, and the oldsters, Zara. H&M, Mango. The Midlands region, as well as being a center of textiles design and manufacturing, has birthed a half dozen catalogue-sales companies, and some of these moved their businesses online.

The Fung Global Retail and Technology report estimated the U.K. online clothing market at nearly GBP 11 bln in 2016, accounting for 23% of total clothing sales in the U.K. Online clothing sales grew by 7.5% in 2016, compared with a scant 1% growth for apparel offline, and Fung Global expects online clothing sales to rise by 10% in 2017.

The founders and partners of Boohoo are Carol Kane and Mahmud Kamani, who met, according to a published interview with Kane, in 1993, when she was employed by a Kamani family company, Pinstripe Clothing, as a designer. Mahmud Kamani, whose father reportedly founded Pinstripe, has been involved in sourcing and clothing wholesale for decades.

They are said almost defiantly to have chosen the name Boohoo a decade after the spectacular collapse of Boo.com, a sportswear and fashion sales website that had been started by the Swedish founders of the book website bokus.com. Ernst Malmsten, one of the founders, wrote a book on the experience called Boo Hoo. Boo.com went down in flames when the inexperienced pair overspent and were unable to manage staff and inventory expansion. Let's hope it was not a prophetic choice of names.

The Stock

Boo trades on the Alternative Investment Market (AIM), a sub-market of the London Stock Exchange. The market cap is GBP 2.937 bln. The company is trading at 123 times TTM earnings, 75x forward earnings, and more than 10x FY 2017 sales. The Street expects earnings growth of 50% in 2017 and revenue growth of 58%.

All fine and good for a young internet company. But the stock has gone parabolic: it's up 422% in one year. That's just silly.

Reasons to Doubt

Despite its small size, Boohoo has gross and net margins well above those of competitors. ASOS has almost the same business model and volumes almost four times as high as Boohoo's as well as heavy investment in IT and warehousing. Unlisted competitor Missguided, whose business model is identical, , according to statutory reports has gross margins almost 20 points lower than those of Boohoo.

Table 1. Margin Comparison

Gross Margins		FY 2014	FY 2015	FY 2016	FY 2017
	ASOS	49.7%	50.1%	50.0%	48.3%
	Zalando	43.3%	45.1%	47.6%	44.5%
	Boohoo	62.8%	60.8%	57.8%	54.4%
	Missguided	43.0%	44.2%	55.5%	
Ebitda Margins					
	ASOS	5.9%	6.6%	7.0%	5.3%
	Zalando	4.0%	4.2%	6.6%	7.0%
	Boohoo	10.7%	9.0%	9.3%	11.4%
	Missguided	1.8%	5.4%	28.0%	
Net Margins					
	ASOS	3.5%	3.5%	3.6%	2.4%
	Zalando	2.1%	4.1%	3.1%	4.0%
	Boohoo	7.7%	6.0%	6.4%	7.9%
	Missguided	0.0%	0.4%	0.8%	

Note: ASOS 2017 financials are for the six months to February 28, 2017.
Source: Bloomberg and British regulatory filings

Yet ASOS gets twice the order value that BOO gets.

Table 2. Order Value: BOO vs. ASOS

ASOS	2014	2015	2016	2017
Order value	62.82	68.74	70.84	
Items per order	2.66	2.79	2.82	
BOO				
Average Order Value	£36.59	£35.28	£33.59	£37.76
Number of Items per Basket	2.38	2.56	2.62	2.89

Source: Company Reports

Not That Type of Business

If Boohoo were truly a business with superior margins, it would be less likely to underpay its workers. But television and magazine exposes in England have charged Boohoo with paying below minimum wage. Boohoo runs a quasi-military warehouse operation in which staff are penalized for being five minutes late and lose their jobs for infractions like asking leave to stay with a sick child. Here is a report by the British Channel 4 program Dispatches. Dispatches reported that certain factory workers affiliated with BOO are paid GBP 3 per hour—well below the required minimum. The Dispatches report says that BOO docks its employees' pay for smiling, using a phone, and other small infractions. Ten of the 12 reviews on Glassdoor are negative and have comments like "The company is run by crooks and nepotism is everywhere." The company does not look like a high-margin operation.

Boohoo uses an outsourcing company called Tailored Recruitment Services to staff up its warehouse.

Manufacturing Margins?

As we see it, there are two ways to explain BOO, neither especially positive. The first is that, by dint of negotiating skill and good inventory management, the company has managed to get to GBP 300 mln in sales while remaining profitable. But perils lie ahead, and BOO will revert to the industry mean. The second and more likely possibility is that BOO is creating the illusion of high margins where those margins do not exist. How? By buying from family-owned intermediaries that bury costs. If that were the case, BOO could easily compensate these money-losing suppliers with the generously priced shares.

There are 53 other companies registered at Boo headquarters.

Given Boohoo's set-up, such an arrangement would be hard to avoid. Apart from Boohoo itself, we have found 53 companies registered at 49-51 Dale Street in Manchester, the Boo headquarters, all owned by Kamani family members or BOO directors and mostly not part of the listed company.

Public reports say that several of these co-located companies are clothing wholesalers. Yet they have no web presences, phone numbers, warehouses, or employees with Linked In profiles. Many of the companies do not even have financial statements. They are granted filing exemptions for being small companies or else are identified as dormant. The companies that have filed financial statements for the most part have a lot of debt.

So, what are these companies doing? Some of them hold or manage property. One is a legitimate restaurant operation. But mostly, they seem to be paper companies.

Aerial photo of the Dale Street BOO headquarters where more than 50 companies owned by related parties are headquartered. | Google Satellite image June 12, 2017

Here are a few of the more puzzling companies:

- **Express Car Hire Ltd.:** Despite its name, Express Car is listed in public records as a clothing manufacturer agent. Jalaludin Kamani, Mahmud Kamani's brother, is 33% owner of the company.

- **Goldleaf Financial Services,** of which Jalaludin and Nurez Kamani are directors, is registered for "Retail sale via mail order houses or via Internet." Mahmud Kamani resigned as its director in 2015.

- **Jogo Associates.** This was a wholesaler of clothing and footwear and was a key business of Mahmud Kamani. But Jogo was not dissolved until 2014, after the BOO listing. CEO Mahmud, his brother Nurez, brother Jalaludin, and his wife, Rabia Kamani, all had ownership stakes, and Paul Gary Papworth, finance director at Pretty Little Thing, served as a director.

- **East (So-Sho) Limited,** owned by Mahmud Kamani brother Nurez, is engaged in the wholesale of clothing. Mahmud Kamani gifted shares in Boohoo to Nurez.

- **Joboo Ltd.**: Dissolved in November 2014, this company was engaged in "Retail sale via mail order houses or via Internet."

- **Jogo Estates:** Liquidated in 2015, this company was engaged in the wholesale of clothing.

- **Manchester Trading Limited:** This active company, owned by Nurez and Jalaludin Kamani, is classified as a wholesaler of clothing and footwear.

- **The Red Orange Clothing Company** is classified as a wholesaler of clothing and footwear.

- **Pinstripe Clothing:** This company is the predecessor of 21Three-Clothing, which operates PrettyLittleThing—as of January 2017, a subsidiary of Boohoo.

- **Earways** is an electronics and telecommunications company. Boohoo does not sell electronic products, and this company may be completely unconnected. But Boohoo does provide music playlists. (It also offers hotel and resort recommendations).

- **Shuffleme Ltd.**, owned by Jalaludin Kamani and, apparently, two of his sons, does "interactive leisure and entertainment software development."

Many of the companies were dissolved shortly after Boohoo listed. However, a dozen or so Kamani-related companies have recently been registered at The Robert Street Hub, a co-working space in Manchester a little over a mile from the Boohoo headquarters. The Hub is owned by Jalaludin Kamani, brother of Mahmud. It offers not only a working space but financing to companies that set up there. We found 20 active companies in British government records that appear to be related to BOO shareholders at the Robert Street Hub.

Is BOO transacting with these paper companies, owned by executives and family members of the CEO?

Inextricable

Boohoo has a surprisingly large number of disclosed related-party transactions. At the time of its listing, Boohoo disclosed over GBP 12 mln in payments to related-party companies, including wholesalers Jogo Associates and Pinstripe Clothing, which are owned by the Boohoo founder's family. In 2016, Boohoo purchased a piece of land from a member of the Kamani

It's hard to conduct business on an arm's-length basis.

family.

In the track-record year, a full 40% of Boohoo's COGS were from disclosed related-party companies. As Boohoo was then gunning for an IPO, and many shareholders in the supplier companies were also shareholders in Boohoo, it would have been hard to undertake the transactions on a completely arm's-length basis.

The proximity of related companies in physical location and business scope raises a risk of margin manipulation; it would be hard to transact business on an arm's-length basis. For example, in the track record year, supplier Jogo Associates reported sales of GBP 30.33 mln. The company's gross margin was just 15%. In the same year, Wasabi Frog, aka Boohoo.com, reported gross margins of 54.5%. Jogo had a net margin of 0.38% and by 2015, had declared insolvency.

In the 2016 fiscal year, Boohoo was still contributing to the Jogo Associates Limited Pension Scheme, GBP 1.6 mln in that year. Jogo accounts are available only through 2014. But could that contribution have defrayed trading losses at Jogo?

Other cases where Kamani family members engage in financial transactions with BOO are rife. For example, Jalaludin Kamani, served as a director of BOO, and Kamani gifted 61.7 million shares, representing 5.5% of the company, to another brother, Nurez.

There are more related-party transactions:

- At the time of listing, the company's solicitor, Steven Grant of Pannone LLP, was a shareholder and director.
- In FY2016, Boohoo spent GBP 1.6 mln to acquire property from the Jogo Associates Limited Pension Scheme, of which Mahmud Kamani is a beneficiary. That company is registered in the Cayman Islands and financial reports are not available.
- BOO uses the marketing services of The White Cube Creative Limited, a marketing company owned by the husband of Carol Kane. In 2016, BOO disclosed paying The White Cube GBP 71,000. The amount seems small, but White Cube is a very small company. The company does not report its revenue, but for 2016, White Cube had total assets of GBP 3,370—basically enough for two laptop computers—and cash in the bank of GBP 8,144. The company owed GBP

11,144 to creditors. White Cube maintains a website with a Gmail address and a cell phone number. It seems likely that Boohoo is White Cube's only client.

- Boohoo's financial advisor and broker for its AIM admission was Zeus Capital. Zeus founder Richard Ian Hughes was also a shareholder in Wasabi Frog. At the time of AIM admission, Hughes' wife, Clare Hughes, owned 20.4 mln shares in Boohoo, nearly 4% of the company. In May, tax fraud charges against Richard Hughes were dismissed. The charges had to do with his Zeus Partners business, which sold film investments to investors as a strategy for tax relief. Other Zeus-assisted IPOs include Purplebricks Group (PURP), a cut-rate online real estate broker, Xafinity (XAF), a pension advisor, and BCA (used cars online). Purplebricks and British Car Auctions have been targeted by accusations of somewhat troubling business practices.

The Robert Street Hub, registered location of at least 18 companies. The Hub also advertises that it offers investment to promising companies.
| Photo by J Capital, June 7, 2017.

PrettyLittleThing

Boohoo acquired 66% of PrettyLittleThing (PLT), a competing business, from Kamani's sons in January this year. PLT looks more or less the same as Boohoo and serves the same demographic. But Boohoo presumably bought some volume and created incentives for the sons to accelerate the business. In March 2014, BOO had purchased a three-year call option from the sons, Samir, Adam, and Umar, that allowed BOO to acquire the company for GBP 5 mln. PLT had revenues of GBP 17.0 mln in the 2016 fiscal year.

Adam, Samir, and Umar do not really look like nose-to-the-grindstone businessmen.

Youtube is full of videos of the Kamani boys partying with sports figures and models in the middle of the day. Umar seems to spend most of his time as a boxer. Adam likes to party as much as his brothers.

When it listed, Boohoo said it would leave AIM and move to a more highly regulated exchange but management said later that they were fine with AIM. In April 2016, after publishing the accounts, BOO's management said, "[t]he board . . .considers that AIM remains the more appropriate market for the company at this point in its development."

Incentives

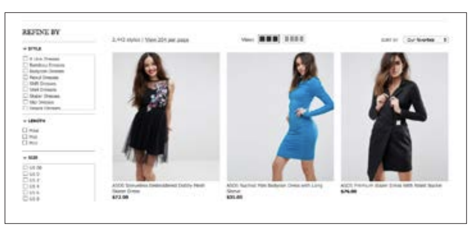
BOO announced on June 12 that CEO Mahmud Kamani had sold 11,252,502 of his shares into the 36,570,632 shares that were placed. On April 27, CFO Neil Catto sold 1.56 mln shares in the open market. These share sales by management are surprising for a company that is growing so rapidly.

Managing Growth

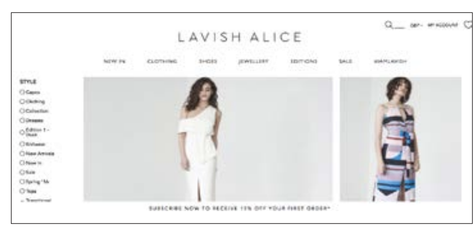
Even without considering the impropriety of so many related companies, Boohoo seems unlikely to manage its growth without hiccups. The first risk for BOO is supply. Boohoo has about 150 suppliers, 70% of them in the U.K. and 50% of product sourced entirely from within the U.K.—a fact the company claims as an advantage, since the pound is weak. But local buyers say they do not believe the U.K. has the capacity to meet Boohoo's growth requirements. In FY 2017, Boohoo fulfilled 11.1 mln orders. That means the company sold 32 mln items (about three items per basket), and half of them were sourced within the U.K. But the U.K. value chain in textiles is populated by small, fragmented companies, with an emphasis on the luxury end of fashion. Suppliers cannot meet the demand from fast fashion for cut-make-trim (CMT) items, most especially for women's jersey dresses, a specialty of BOO's. Industry reports indicate that fewer than a dozen textiles manufacturers in the U.K. employ more than 100 machinists, and BOO, with roughly 1% of the clothing market in the U.S., is competing with far bigger players. One sourcing expert estimated that BOO would be able to obtain within the U.K. only a small fraction of the dresses it sells. Furthermore, at the prices Boohoo sells at, the company would be forced to source from small manufacturers that must accept very low margins. As the company grows, those sourcing practices seem unsustainable.

Competitor ASOS recently published a list of its suppliers as part of an effort to support more sustainable supply practices. We telephoned 26 of them in the U.K. and China. Few would talk about their customers at all. Only one said it supplied Boohoo but through an intermediary instead of directly. Asked why Boohoo might be able to obtain lower prices than other buyers, that company said, “People don’t play by the rules on all occasions.” The competitive environment in online fashion is indeed cutthroat, leading industry alliances to pledge higher standards. The University of Leicester Center for Sustainable Work and Employment Futures has been at the forefront of work to ensure compliance with minimum employment standards.

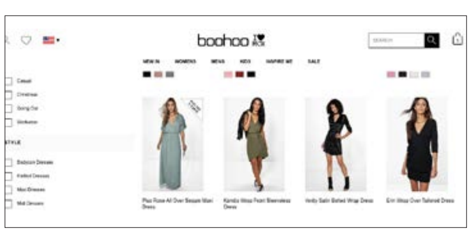
Boohoo does not have exclusive relationships with the suppliers, which may produce and sell the same style of clothing to BOO’s competitors, according to buyers.



ASOS

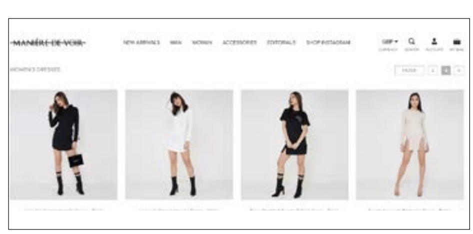


Lavish Alice



Boohoo

Sosander



Maniere de Voir

Logistics

Boohoo owns a 150,000-sq-ft warehouse in Burnley, England, about 40 miles from Manchester, and is building an extension on an abutting piece of land to add 100,000 sq ft more. BOO fulfills all of its orders worldwide from the Burnley location and plans to continue that practice, making back the extra shipping cost on efficiency savings. Distribution expenses are 23% of revenue—a 3-point improvement over 2016, but far higher than those for ASOS, which spends 15.4% of revenue on distribution. Much of the valuation rests of the belief that this number can come down with greater scale.

Quality of distribution appears to be declining and the cost is higher than that for competitors. For deliveries in the U.K., BOO charges a flat fee of GBP 3.99 for standard delivery, GBP 4.99 for next day, GBP 7.99 for evening delivery. You can pay GBP 9.99 and get free next-day delivery to a locker location for a year. In the U.S. prices are USD 6 for Super Saver (8-10 business days), USD 10 Standard (six business days), and USD 16 for 2-3 business days. These terms are dramatically less attractive than Amazon's. They are also more expensive than ASOS. In the U.K., ASOS offers GBP 2.53 for standard delivery (five business days), GBP 7.6- for delivery within two days, and, like BOO, GBP 9.95 for a year of second-day delivery. In the United States, delivery is USD 4, USD 12, or, for 12 months, USD 19. Delivery is free on orders over USD 50. But given that BOO's average order value is much lower than ASOS', the higher-priced shipping would be a deterrent.

Online customer reviews indicate that the quality of service on Boohoo.com has deteriorated over the last two years. BOO received the worst rating from 74% of the 442 reviews on Reviewcentre.com and 62% of the 351 reviews on Sitejabber.com. BOO received a "terrible" rating from 51% of 337 reviews on Productreview.com. Reviews of Boohoo and PrettyLittleThing on TrustPilot are consistently negative and cite long delivery delays, unapproved charges made to PayPal accounts, "non-existent" customer service, and low-quality products. Boohoo seems to respond to nearly every negative review, and in many ways trustPilot seems to be used to air grievances rather than to offer neutral or positive feedback. But Boohoo in its reports to investors consistently cites positive ratings from TrustPilot, which makes the negative reviews relevant.

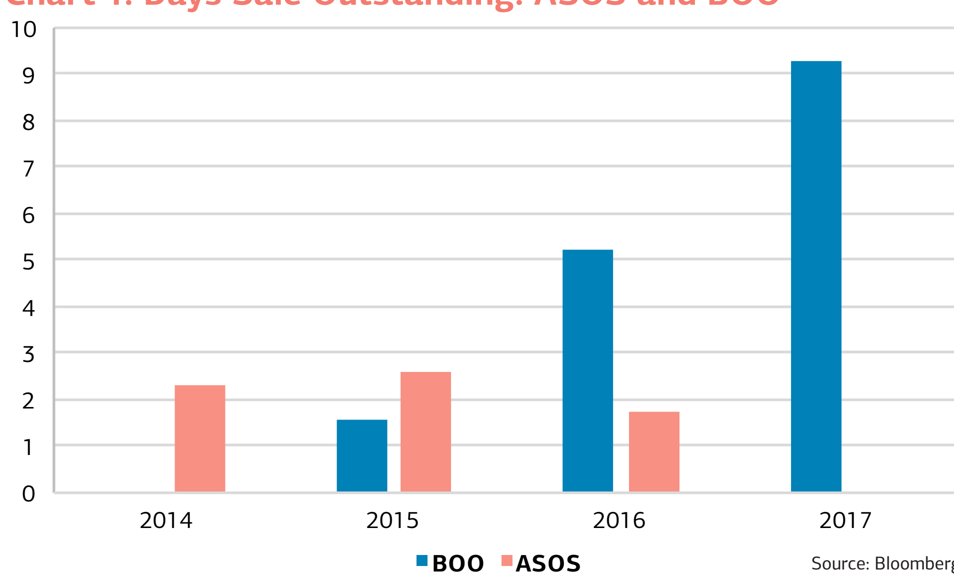
Boohoo uses third-party delivery services. Courier services Boohoo uses include Hermes, Parcelshop, Collect+, and Royal Mail. The expedited delivery service seems to be a particular problem. A typical review, from Daniela Ferreira, published on Friday, April 14, 2017 reads:

> Don't order from them! They're scammers!
>
> You guys are a freaking joke! Everyone in here is having the same problem as me! Paid for a 2 day deliver and never got my package. Tried to contact the joking a$$ company that you guys use for delivery and they put me on hold for 21 minutes hold, went on their Instagram and every single comment they have under their pictures is of costumers complaining of lost packages and late deliveries... I'm trying to contact you guys and I'm not getting a word back!
>
> I spent almost $200 of very hard working money and you guys scammed me! I'll do anything in my power to show people that this company is a JOKE!

In 2015, Boohoo started working with Dubai-listed logistics provided Aramex in Australia, and now Boohoo uses Aramex in Europe and the United States. But those markets are very marginal for Aramex which reports having around 10% of its workforce of 14,275 in Europe and North America. Aramex is a specialist in the Gulf region and the Levant.

BOO's days sales outstanding have ballooned from 1.5 in FY 2015 to 9.3 in the most recent fiscal year. This may indicate channel stuffing.

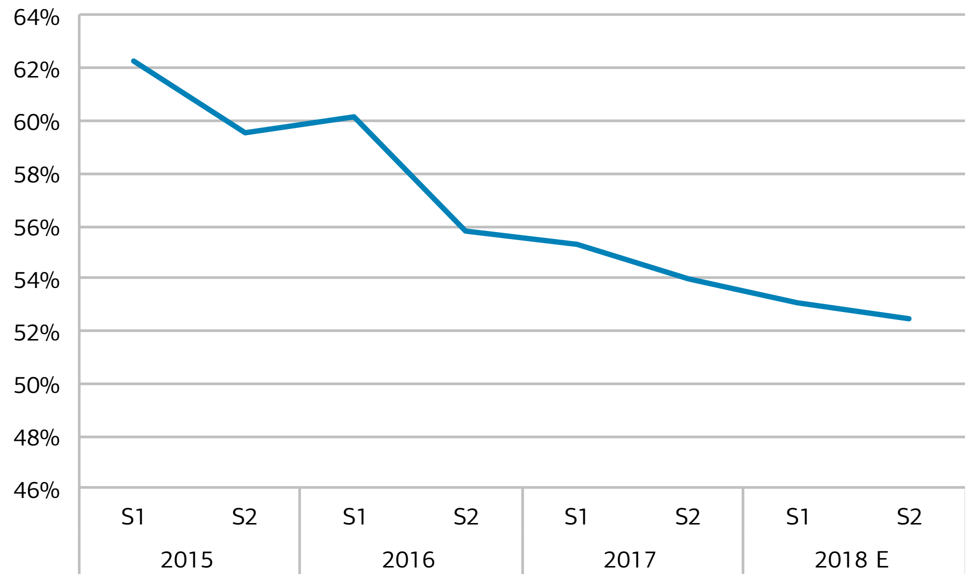
Chart 1. Days Sale Outstanding: ASOS and BOO



Source: Bloomberg

BOO's margins are declining, but the Street seems not to be concerned.

Chart 2. BOO Gross Margins



Source: Bloomberg

Capital Investment Needs

On June 7, Boohoo announced that it will raise GBP 50 mln in new equity, largely to support the expansion of its Burnley warehouse. That will be added to GBP 30.7 mln spent in the last year. Of that, just GBP 14.6 mln was spent on IT and the warehouse, 5% of revenue compared with 6% for ASOS.

Boohoo's Burnley warehouse. | Photo by J Capital, June 8, 2017

Site of the warehouse expansion. | Photo by J Capital, June 8, 2017

Boohoo's Burney warehouse operation looks impressive form the outside. But the company does not break out spending on IT and does not seem to have room to be implementing good warehouse management tools. ASOS, by contrast, spent GBP 60 mln on IT tools alone in 2016 and plans another GBP 100 mln or so in 2017.

The spending requirements may be under-appreciated by investors. To compete in e-commerce, companies need to have the best IT, the best warehousing, the best logistics. If Amazon, ASOS, and other players are any model, expansion will require much heavier capital spending.

The US Expansion

Most recently, BOO bought NastyGal, a bankrupt website that sells teenage girl's clothing, for USD 20 mln, to build its presence in the U.S.

Since the acquisition, BOO has added lower-priced items to the website. Formerly, a typical jersey dress selling on NastyGal might go for USD 60 or more; now there are many dresses available for USD 30-40. But that would seem to suggest that the already money-losing site might lose a little more. NastyGal was formerly selling third-party brands such as Citizens of Humanity and Levis but now displays only private-label products. The site is glitchy; it has a lot of errors and very modest variety and inventory.

The brand does seem worth acquiring: it has a good reputation among young women for fashion-forward designs. But there was not much else to buy in NastyGal. Like Boohoo, NastyGal was a star: internet Retailer estimated that Nasty Gal's five-year compound growth rate was 92.4%, compared with a median 15.3% among online apparel sites.

Marketing Spend

Boohoo appears to spend liberally on marketing; the company's ads are plastered all over the London Tube. But the company does not break out sales and marketing costs nor does it provide detail on its investor calls. In the 2016 Interim report, for example, BOO says that increased marketing spend is driving international growth, but it does not disclose that marketing spend.

A January 2015 article in The Drum reported that, in 2013-14, Boohoo had spent 14% of revenue on marketing but underperformed on profit. In the same year, competitor ASOS spent 5% of income on sales and marketing. Boohoo attributed the poor performance that year to spending too little on marketing.

For the fiscal year ended February 28, 2017, Boohoo reported that marketing spend declined by 10% but would not provide more explanation. That decline is what buoyed the company's margin.

But Boohoo seems to need spending to acquire customers. The company says its customer acquisition cost (CAC) is GBP 8 in the U.K. and higher elsewhere. The average consumer spend is GBP 37.76 in the most recent period. Given that Ebitda margin was 11.4% for that period, BOO is making about GBP 4.30 per customer per year. That means it takes two years for the company to recoup its CAC.

Pricing promotions and increased marketing costs will continue to drive down BOO's margins. From Black Friday 2016 to the end of 2016, the BOO app sent push notifications on almost a daily basis announcing 50-70% off pricing promotions. In London in early April and Manchester in June, the tube and airport seemed to be wall to wall with BOO advertisements. This cannot be cheap.

Bull Case

Company IR, in response to questions about margin, says that Bohoo management, while at Pinstripe, had long experience supplying traditional retailers and also ASOS. It employs a strong buying team with good negotiating skills. This is corroborated by industry sources. Return rates, they say, are a relatively low 23%.

An industry expert who knows the Boohoo business attributed that company's superior margins to Kamani's strong negotiating ability. This expert said that Kamani uses accounting methods "at the edge of what is legally permissible" but not over the line. Kamani is said to be a visionary with a powerful managerial ability to keep costs down.

Often in these cases, success is just about timing. Boohoo made it to market and thus got access to financing. Given the company's fashion sense and strong buying capabilities, Boohoo may be the real thing, and it's worth paying a premium for growth.

Boohoo has strong traction and cachet with fashionable young women, and there is a place on the internet for fashion specialists. We just think that ASOS is more likely to take it.

Boo.com, the fashion site founded by a Swedish couple, crashed and burned on the dotcom era belief that business on the internet was fundamentally different form offline business and could grow almost effortlessly given enough money and the right mix of talented people. The Boo team, after burning about GBP 110 million, left nothing behind. Let's hope the name is not haunted by its history.