Rent the Runway

Thamina Stoll - September 29, 2015
Customer Value Proposition:
- unintentionally changed over time: 1) “Netflix for fashion”, great value and convenience —> 2) “I’ve never felt so special”, try something new, feel confident & beautiful; right dress, on time, “feels-like-new” —> It’s not about the dress, it’s about the woman!
- superb service, treating customer with utmost respect, giving fashion advice (customer insights team trying to compensate the fact that women cannot try on dresses)
- special services: second size free of charge, reservation system, $25 for second dress
- need: designer apparel business $149 billion, $80 million dresses alone (2008) —> 150,000 members within 2 months
- beneficial for both customers & designers —> young women cannot afford the brands they truly desire and designers cannot access young women to build brand loyalty —> RTR as a new customer acquisition channel that exposes younger women to designers’ brands
- target group: age 15-30 —> were initially able to expand age range and attract “older” women —> however, expansion of inventory (= investment) necessary

Technology and Operations Management:
- Made the right employment decisions —> firing website designer & developers
- Decision not to outsource warehouse operations right —> more control
- Lack of CTO disadvantage —> for example: SEO & more engineers necessary
- in the beginning not a clear division of jobs —> might not have been the most efficient way to work + subject to misunderstandings —> clear division of duties later
- lack of experience in designer apparel business an advantage because it allowed the co-founders to approached the industry with a fresh perspective on how to change it

Go-to-market Plan:
- market trials (Harvard, Yale & email) —> good way of testing need & customer behaviors
- beta version: invitation only in the beginning —> makes women feel special due to exclusivity —> However, one week too short to really get a sense for demand, 1-2 months might have been better in my opinion
- word of mouth & personal network very powerful
- referral program ($20 store credit) worked really well (just like with Dropbox) —> direct incentive
- initial buzz through fashion blogs & one big story (Vogue —> New York Times) —> NYT article generated 60,000 new members
- minimum viable product approach smart —> allowed RTR to collect the maximum of learning about customers with the least effort (again, longer beta test phase might have been beneficial)
- Brand ambassadors on college campuses —> good idea, no information on how it went
- CAC fairly low —> organic growing works really well (again, just like Dropbox)

Other positive aspects:
- co-founders benefitted from carefully listening to designers to learn about their interests & fears to create a service that was synergistic with their needs
- 98% of RTR’s customers rented brands they had never owned —> proof of concept: RTR excels as customer acquisition channel (“gateway drug to designer fashion”)
- customer insights team very valuable & part of the “Cinderella experience” —> product innovation highly benefitted from stylist service
- proof of concept: a woman gets an average of 2 compliments per night with her own wardrobe, and 12 when she rents from RTR
Profit Formula:
- dresses purchased at wholesale prices (40-50% of retail prices)
- barely any marketing costs (a few thousands for PR prelaunch)
- fixed/variable costs: warehouse, employees
- lots of unpaid interns
- capital investments: big —> inventory (1000 dresses)
- working capital: rental fees
- barely any competition (2 main competitors, RTR's concept is better)

Financial analysis:
- for simplicity I'm only focusing on middle-tier dresses because I'm assuming "cheap" and expensive dresses are balancing each other out
- A Middle-Tier Dress needs to be rented 3.6 times to cover its cost (purchase + shipping, dry cleaning, credit card processing, and packaging) before it can begin to generate a profit. However, since every dress is shipped twice, free of charge we need to double that number = 7.2 times
- every dress comes in 7 sizes (0,2,4,6,8,10,12) and we're assuming that they don't have every size only once —> let's assume every size 2 times (in the beginning), for simplicity we're not taking into account that most women will rent medium-sized dresses (4-8) and that RTR has probably purchased more of medium sizes than small and large sizes
- 800 dresses in the beginning = 57 different styles
- 14 dresses for each each style = 14 x $323 = $4,522 for each style
- 800 x $323 = $258,400 (inventory)
- 7.2 x 800 = 5,760 purchases to cover costs before beginning to generate profit
- they add 200 more dresses in January —> 7,200 purchases
- 2,000 orders after two months = $180,000 revenue (based on $90 revenue) —> 12.5% of customers order more than once (for simplicity we're assuming more than once = 2) —> 12.5% out of 2000 = 250 —> 2000-250 = 1750 customers = only 1.1% of all registered members actually ordered within the first two months (not that great)
- 7,200 - 2000 purchases = 5,200 purchases left they need to cover costs x $90 = $468,000
- salary for 8 employees —> for simplicity, let's assume everyone earns 60,000 a year = $480,000 + warehouse in Manhattan ($75,000/year based on 2,500sf with $30/sf) = $555,000 + $258,400 = 813,400 investment + additional 200 dresses = $813,400 + $64,600 = $878,000 —> $878,000 + $468,000 = $1,346,000 = costs to break even
- future potential: based on market trial prior to launch, 5% of the women who were contacted via email rented, so let's assume RTR is able to increase their number of customers from initial 1.1% to 5% —> 5% out of 150,000 registered members = 7,500 customers —> 7,500 - 1,750 (early customers) = 5,750 new customers x $90 (revenue) = $517,500 —> if we're assuming that 12.5% of these new customers order more than once (remember, we're assuming more than once = 2 times), we end up with an additional $64,688 —> $582,188
- $1,346,000 - $582,188 = $763,812 to break even
- another aspect we have to keep in mind: 60,000 word-of-mouth referrals —> 30,000 $20 credit —> $600,000 in store credit —> not money that RTR loses but money that they don't earn (assuming that all 30,000 members are actually using their credit at some point — > if only 5% of registered members use it —> $30,000)
Final thoughts and recommendations

- My numbers of expected future revenue are quite conservative —> Due to organic growth and the success of word-of-mouth referrals, the number of members will constantly grow and produce revenue; I’m also convinced that RTR will be able to increase the percentage of customers from 5% to maybe 10% or even 15% because their service is very customer-friendly and most of the customers seem to love RTR
- The chances that RTR is going to break even or coming close to breaking even in their first year are reasonably high if they’re following their initial plan
- While adding accessories, “cunsumerables” & maybe shoes seems to be the next logic step, I would advise against an early expansion even though the demand is high —> customers won’t stop using the service just because there are no accessories available and the time will come when it will definitely make sense to expand RTR’s product range
- Right now, I would focus on optimizing business operations —> RTR still needs to hire a CTO, tackle SEO, improve the website to increase conversion rates, find a way to work as efficiently as possible and most importantly continue learning from their customers —> 2 months is not enough time to learn
- Another funding round is too risky because it puts a lot of pressure on the company to constantly expand its inventory —> expanding inventory raises the risks because you don’t know how well certain products will perform and dresses don’t generate profit for a very long time
- and just because the CVP has changed very quickly that doesn’t mean that the range of products has to change equally fast —> not offering accessories won’t deprive RTR from offering their customers that special “Cinderella experience”
- If RTR focuses on too many different things at the same time without improving their operations first, that might even result in a decline of service quality because the team would have to split their attention and couldn’t solely focus on dresses anymore —> and as of now, their superior customer service is crucial to the company’s success
- On top of that, an expansion would mean that the company would have to restructure its entire operation system (warehouse set-up, re-train customer service team, probably hire more people, adjust website and packaging, etc.) —> a complete restructure after 2 or 3 months? —> too risky
- tasks: improve business operations by learning and being patient, increase conversion rate, enjoy growing number of registered members and paying customers because they will come due to the immense power of word-of-mouth referrals