Twitter Thread by Robert King

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The baby wakes me up at 5am these days, so let's talk about $RH. I've been following $RH for half a decade now, and I started off with a profound misunderstanding of the company. When $RH started its membership program back in 2016, I thought it was a stupid idea and 1/

a half-assed way to graft a Costco membership dynamic onto what was supposed to be a high-end furniture store. Very confusing. Of course, I was the one who was stupid because my girlfriend at the time (now wife) was an interior designer, and I didn't bother to ask her about /2

it. $RH employs a bunch of interior designers to help you with your design needs, and you get access to them for the $100 membership fee + you get 25% off all full-priced items. What's going on here? $100 to save hundreds of dollars + you get interior design services? You 3/

might think it's $100 fee to have the interior designer upsell or sell more products, and it… sort of is? But what I didn't know and hadn't bothered to ask my gf/wife was how interior designers worked. It turns out that if you're a licensed interior designer, you get 20-25% 4/

off high-end furniture for your clients anyway. And once she told me this everything clicked. The $100 rate was a way to aggregate clients for their internal RH interior design folks, and these interior designers were going to get a 25% discount on their purchases anyway, so 5/

this was a very low cost way for $RH to pull you into a membership program, guarantee a certain amount of clients for their internal sales/interior design team, etc. Duh. Okay, so now I realize that when a smart company does something that looks stupid to me, maybe I 6/

should stare at it a little harder. So when $RH decided to start a restaurant and install coffee bars, I tamped down on my instinct to scream "DON'T YOU KNOW RESTAURANTS ARE LOW MARGIN?!?" and asked myself, okay, why might this work? $RH places their coffee bars & restaurants 7/

the way $AAPL locates its Genius Bars — in a manner that forces you to walk through the store. The RH Chicago Flagship has the restaurant in the middle courtyard. The RH NY in Meatpacking has the restaurant on the top of the building (which usually lies fallow) and the coffee 8/

bar on the third floor. Here’s Chicago… 9/



…and here’s NY on opening day. You might want to ask yourself a Peter Lynch question here — have you ever seen this long a line for a furniture store opening before? Actually, have you ever seen people queue in line for a furniture store, period? 10/



Okay, so $RH forces you to walk through a beautifully designed building in order to get lunch or coffee. So what? Well, $RH has basically downshifted its cash & carry business (<1% of the revenues) so how does $RH keep top of mind? Recall that for most people, furniture is a 11/

once every 10 year purchase, but I suppose if you're a $RH customer, you might be re-updating your space every 4-5 years? That's a long time between visits, and when you're in the purchasing frame of mind, you're probably just going to go with the availability bias of what 12/

furniture stores you can recall at that particular moment. If you're coming into the store on a monthly or bi-monthly basis for dinner or daily for coffee, that's good for $RH! Moreover, $RH is using normally "fallow" space for their F&B business, which is how they also 13/

approach their outdoor business. Focus briefly on that last paragraph for a second and let me take a tangent that will tie it to a thing I forgot about $W. "Well, why can't other people do that? Well, other people don't build galleries as big as we do." That should trigger a 14/

Gary G. Friedman - *RH - Chairman & CEO*

Yes. I think it's -- look, outdoor, I'd say, outdoor business is a lot like the general RH business. I think when you build a brand like ours, you, in many ways, are creating a market. And you're inspiring people to purchase and invest versus other purchases and investments they may have made based on what they see. And no different than Apple created a new market. They didn't look at the cell phone market and say, how big -- I mean Apple created an entirely new market around smartphones. And the iPhone, nobody thought it would sell in China. It became the best-selling phone in China. When you create a really good product, and not just a single product, I'm talking about a full integrated branded proposition, you have an opportunity to create a new market, right, to disproportionately expand a market because you're putting something out there that wasn't there before, right?

And I think that's happening in many places, right? You can look at a lot of brands that are creating new markets. So in outdoor, it's much of the same. If you just stood back and said, "Huh, where do you go buy outdoor furniture?" There's not a lot of consumer-facing outdoor furniture stores, right? They're kind of out off the beaten trail, kind of in weird places. You can come up with the names, you've driven by them before. But if that is high-end outdoor furniture, where do you go? Where do you even see it? Where do you even get inspired to buy it? It's -- no one really presents it because it tends to be more seasonal in nature as far as the peaks of the business. Yes, I used to joke around and I used to tell people is what -- you might remember a business called Smith & Hawken, right? And they opened like 50 stores and then almost went bankrupt and they took another go at it. And I would say, "Why didn't Smith & Hawkins make any money? And they say, "Geez, we don't know." I said, "Well, for the most part, they had to pay rent, right?" And they paid ground floor rent for a very seasonal business.

And if you look at our strategy and what we've done with rooftops and terraces and things like that, we've -- in our new galleries, we present somewhere between 20 and 30 outdoor collections, depending on the outdoor garden space and the rooftop space. Nobody faces the customer

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like that in the outdoor furniture business. And because we're facing the customer like that in this firing environment, we're creating a new market, and we're creating a new market in outdoor furniture at a very high return on invested capital.

So we really like that business. And you say, "Well, why can't other people do that?" Well, other people don't build galleries as big as we do. So their rooftops can never be as big or they don't control the real estate like we do. And they don't -- very hard to emulate what we're doing, right? And that's -- and why the physical nature of our business is so important, right? Like I would say that a website is an invisible store, right? You don't see it, you don't pass it, you have to be prompted to go to it. And if there's physical stores, people drive by, they see -- if you're in the right locations, you're in the -- you're going to be constantly visible and you can present products and categories in ways that you can't online, where the online -- an online business is very democratic, right? We -- everybody has the same size screen. Holly's home store can look as big as RH online. And when I say Holly's home store, it's nobody named Holly. It just refers to a higher-end local furniture specialty store that someone is running. And -- but those kind of businesses can't do what we do. And that's why we're so disruptive. So when you disrupt like that, you're taking share. But even most -- more importantly than taking share, you're creating a new market. And that's how we think about it.

bell in your head, because that's what Munger has said about Nebraska Furniture Mart. Why does sizing matter? Because people don't go to four furniture stores because they like it. (Okay, maybe my wife does, but that's because she used to be in the field.) They go to four 15/

Well, let me do it for you. Is this a low-priced store or a high-priced store? (Laughter). It's not going to have a runaway success in a strange city as a high-priced store. That would take time. Number two, if it's moving $500 million worth of furniture through it, it's one hell of a big store, furniture being as bulky as it is. And what does a big store do? It provides a big selection. So what could this possibly be except a low-priced store with a big selection?

But, you may wonder, why wasn't it done before, preventing its being done first now? Again, the answer just pops into your head: it costs a fortune to open a store this big. So, nobody's done it before. So, you quickly know the answer. With a few basic concepts, these microeconomic problems that seem hard can be solved much as you put a hot knife through butter. I like such easy ways of thought that are very remunerative. And I suggest that you people should also learn to do microeconomics better."

furniture stores because they HAVE TO. They didn't find what they needed in the first three stores. So if selection is one of the main criteria that consumers use, you can either (1) go BIG (NFM, RH) or (2) go online (AMZN, W) where there are no constraints to section. 16/

Something something cumulative knowledge. 17/ https://t.co/YktFazIsTX

> Some additional thoughts on $W. A lot of knowledge is cumulative in investing. $W only made sense to me after spending a significant time following $AMZN and $RH. Gary Friedman spent a significant amount of time on one of the Restoration Hardware conference calls talking 1/
>
> — Robert King (@robertqking) January 3, 2021

Back to the main storyline, so $RH can eke out much better economics on the F&B business, the outdoor business, etc. because they're not paying ground rent! How brilliant is that? They're literally sitting around looking at their RE and saying, huh, why isn't there something 18/

we're doing in this part of the store? And, of course, if you look at what's happened with RH Meatpacking, they've basically anchored the area for other super high-end retailers, which is great because they're opening RH Guesthouse in the old Pastis location down the block. 19/

Anyway, if you like business/furniture/retailing, and you're not reading Gary Friedman's shareholder letters and listening to his conference calls, you're doing yourself a disservice. Gary says he's climbing the luxury mountain, and he's the first one

in a long time that 20/

seems like he might make it. He has basically no competition between bespoke furniture and, like, Pottery Barn — and he's using his brand to enter into everything from hotels to residences. (I still haven't quite figured out how the last two help the business, but a few 21/

posts up I learned not to generate hot takes, so we'll see how they develop.) /fin