

The Pressure Is On: Retail Anxiety Builds As Economy Weakens

By David Moin with contributions by Cate T. Corcoran

Fear plus frustration equals premature — and aggressive — markdowns.

That seems to be the current state of play as the struggling economy has turned retailing into a challenging game of inventory management, urgent belt-tightening and guesswork planning for seasons ahead.

Skyrocketing food and gas prices are pinching consumers at all income levels, and industry executives are said to be scurrying to get their receipts and expenses in line with their rate of sales. The cold, hard reality is that the merchandise in stores today was ordered almost six months ago — when the economy, while weakening, was in better health. Making things worse is that no one knows when the economy will hit bottom, with many saying there won't be any improvement for at least two years.

"I've never experienced anything like this before," said Jane Elfers, chief executive officer of Lord & Taylor. "When I speak to veterans of the industry, who have been in the business for 40-plus years, they tell me they've never seen anything like this, either. It really puts the pressure on retailers to innovate to get customers to shop."

And if they don't, the warning signals are flashing: On Friday, Linens-N-Things became the latest in a growing list of retailers declaring bankruptcy this year.

Meanwhile, markdowns are creating greater angst than usual. Last week, consumers on retailers' e-mail lists found their in-boxes full of promotions. Macy's, Bloomingdale's, J. Crew, Neiman Marcus, Endless and Sigerson Morrison were offering anywhere from 20 to 40 percent off, usually with free shipping.

"The sales are across the board, not just online," said an executive at a large, multichannel retailer. "Everyone is trying to get rid of inventory they bought a lot earlier, and not have it hanging around in the fall."

On Friday, Saks Fifth Avenue raised some eyebrows with advertisements in New York newspapers promoting 40 percent off selected merchandise. The flagship had many red signs atop racks flagging 40 percent off, across the designer sportswear and couture floors as well as bridge and contemporary labels. Most often, spring goods were on sale, whereas Fall One deliveries appeared at full price. The main floor had plenty of handbags at 30 percent off, drawing swarms of shoppers.

Stephen I. Sadove, chairman and ceo of Saks Fifth Avenue, reiterating comments made at a Lehman's conference last week, said, "It's our intent to clean up our inventories by the end of the season. It's

better to sell product on first markdowns rather than second markdowns."

The sale, announced privately Thursday and Friday, and advertised for Saturday, was a week ahead of last year's.

"Everybody gets crazy when it's designer merchandise getting marked down earlier," said one luxury retailer. "It's not as big of an issue with bridge and contemporary."

Last week also saw some retail downgrades by Standard & Poor's, including Barnes & Noble, due to "a challenging macroenvironment, increased price competition and the lack of a Harry Potter book to boost traffic and sales in fiscal year '09."

Pier One also was downgraded because "sales of home furnishing items typically lag a rebound in housing, which we do not see occurring this year." And Bed Bath & Beyond got downgraded due to "near-term margin compression on potential clearance sales from the closure of Linens-N-Things locations."

What's got many in the industry talking is an ominous prediction from J.C. Penney's chairman, Myron "Mike" Ullman 3rd, who last month said the nation is halfway through the subprime mortgage crisis. Ullman said \$2 trillion in home values have dissolved and consumers could stand to lose another \$2 trillion. The \$19.86 billion Penney's is reducing store openings to 36, from 50, leading to a savings of \$200 million in capital expenditures. There will be 20 major store renovations, down from the 65 originally planned, and the retailer is "moderating" the inventory buy, which is generally purchased four to nine months ahead of the selling season.

After 39 years in the retail business, "I don't think I've been in an environment so unpredictable....For 2008 to 2009, there is a very difficult outlook," Ullman said at an analysts' presentation. "We really don't know what '08 and '09 will look like."

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— Greg Furman, Luxury Marketing Council

The middle market, to which Penney's, Kohl's, Macy's and Target cater, and the aspirational market, such as Nordstrom and Coach, for those shopping at a rung below designer price points, appear to have been the hardest hit by the economic downturn. **"The aspirational market just kind of tanked out. Those in the \$250,00 to \$500,000 income have been tanking with the market," said Greg Furman, chairman and founder of the Luxury Marketing Council, at a panel discussion conducted by the group last week.**

Douglas Gollan, president of Elite Traveler, the private jet luxury magazine whose readers have an average household income of \$5.3 million, said, "I'm very bullish on very rich people. I'm not as positive on the entire market. What's happening in the economy I would compare to a Category 5 hurricane."

Throughout the industry, there is no consensus on how long retail will struggle or when the economy will turn. Lincoln Palsgrove 4th, senior marketing manager for the South Street Seaport, who

participated in the panel, said business at the Seaport "is looking pretty rosy because we have foreign visitors." However, he believes retailing overall is "in for some tougher days into 2009."

A more optimistic prognostication came from Robert H. McCooey Jr., senior vice president of new listings and capital markets at The Nasdaq OMX Group. "I get to go around and meet business leaders and see ceo's confident about the fundamentals. Most run their businesses in the mind-set of a short but shallow recession." He added that "bringing the IPO market back to life will be a sure sign of recovery."

The industry will be closely eyeing April sales results, which get reported this week. They are expected to be better than those in March, but still in the negative column for many retailers.

"Thanksgiving weekend was the last positive performance, and there has been a continuing downturn since then," observed Arnold Aronson, managing director of retail strategies at Kurt Salmon Associates. "April will not be fully indicative of any major reversal of the negatives."

Contemporary sportswear; sandals, particularly gladiator styles; bathing suits, and cotton sundresses have fared well at many stores, though suits, in men's and women's, and the kids' businesses are said to be poor. Other sportswear is considered to be doing just OK, as are handbags and jewelry. Retailers said that during hard times, people are still treating themselves to simple pleasures, such as ice cream, the movies and coffee (primarily less expensive ones — Starbucks last week scaled back its U.S. expansion after poor financial results). Because consumers are eating out less and cooking at home more, food retailers are expected to do well, as are drugstores.

Department stores through much of this year have been tracking at midsingle negative comps, with women's fashion chains even more negative, while big discounters such as Wal-Mart and those on the high end, such as Neiman Marcus, have performed slightly up or a little behind.

Burt Tansky, chairman and ceo of the Neiman Marcus Group, speaking last week at a seminar organized by the Emanuel Weintraub Associates consulting firm, described the business climate by saying: "It can be bleak, but it can also be finite. Since World War II, recessions, on average, have lasted 11 months." As for how Neiman's is weathering the storm: "We are on a diet. We are planning conservatively, controlling our expenses and finding ways to be efficient....Trading down is not an issue. The customer may pull back but won't pull out or trade down." They're tightening their "alligator and ostrich" belts, he said.

According to one department store ceo, "Business is rough everywhere. You've got to keep managing the inventory and getting ahead of it and making sure receipts are in line with projected sales. Sales are getting worse and worse, so you need to make sure the inventories are aligned with sales projections based on the true trend. April is going to be better than March, but that has to do with the extra day of Easter. We are still seeing down comps. We were up against bad comps from a year ago and it's still bad and that shows how bad it is really."

Generally, retailers can stop shipment on receipts four or five months ahead of delivery, depending on whether it's basics or fashion goods and depending on the vendor. European luxury designers are likely to have stricter arrangements with retailers, whereas companies such as Liz Claiborne and Jones tend to construct gross margin agreements with stores.

Fortunately for them, there are new markets emerging, such as Russia, and off-pricers like Marshalls

and TJ Maxx are waiting with open arms. The outlet business continues to grow, as well.

Through the adversity, a silver lining is emerging. "Retail leaders are getting better at reading the tea leaves," said Aronson.

Though many store executives have been issuing somber views, sometimes to provide realistic or lowered expectations to Wall Street, "retail leaders are not 'cry wolf' kind of people and are reacting to what's going on in the economy and the difficulties their customers are facing," he continued. "They recognize that this downturn is different from others because it has more variables occurring all at once." He cited unemployment rising at 5.2 percent; record-high gas prices, at \$3.62 last week for regular; housing that starts at a record low, off more than 20 percent, and the high euro, causing rising prices on imports.

"Most retailers are reacting to these conditions prudently by moderating new store expansion, tightening inventories and addressing expense levels until the storm clouds clear," Aronson said. "It's the perfect storm of many real economic issues."

"It's tough, definitely difficult and volatile," said one executive from a national women's fashion specialty chain. "You can have a good day and then a not-so-good day. There is no constant trend. [The consumer] is very interested in the deal. Pricing is so much more competitive. If you turn on a promotion, you see a reaction. Everybody is constantly having a sale. If the product is good, and if it's different, she's willing to pay, but you've got to get her over the hump with a promotion. It's very tough. We are planning for business to be tough for a while, but we really don't know for how long. We are buying less than last year. Our planning is conservative. We are not planning comp growth. Our holiday planning is pretty much set at this point. Department stores are the most promotional I've ever seen them. But everybody is being very promotional."