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PRI MONTHLY RETAIL ANALYTICS

“BRINGING RESEARCH TO RETAIL”

Several prominent financial firms have recently made upward revisions to their first quarter estimates of GDP (i.e., Morgan Stanley, 4.4% vs. 3.3% last month; J.P. Morgan, 4.0% vs. 3.5% a week ago). This is in reaction to a slew of positive economic news. The Fed’s Beige Book, released on 9 March, for example, notes that “all twelve Districts indicate that economic activity has increased...”. The Chicago Fed’s National Activity Index rose by 0.37 in February, up from 0.13 in January, which also indicates a continuation of growth in economic activity. Notwithstanding, we anticipate 2005 will be a year of moderating economic growth. We are maintaining our conservative bias, forecasting full-year GDP growth of 3.4%-3.7% (versus 4.4% in 2004 and 3.0% in 2003).

On a positive note, consumer spending and business capital spending continues to underpin the economy. In addition, 262,000 new jobs were added in February versus an average rate of new job creation of 182,000 per month over the past six months. So why are we so stubbornly conservative in our view? Part of this is attributable to my close relationship with my Grandmother, who lived through the depression (I was always her favorite). Most of this sentiment is, however, attributable to interest and inflation rate risk.

The Leading Economic Index supports our view. The Index rose 0.1% in February, following a 0.3% drop the previous month. However, on a quarterly basis, the year-to-year change indicates a deceleration. The January-February average indicates a 0.3% year-to-year gain, as compared with a peak increase of 4.3% achieved in the second quarter of 2004. The composite ISM manufacturing index also fell in February for the third straight month, indicating a growing factory sector, but at a slower pace compared with prior months. In addition, 2004 Productivity growth slowed to a 4.0% gain, versus 4.3% and 4.4% in 2002 and 2003, respectively.

The Federal Reserve is now publicly addressing inflation risk. A recent Fed release stated that “pressures on inflation have picked up in recent months, and pricing power is more evident.” Inflation data, as measured by various indexes, confirms this. The GDP price index rose 2.2% in 2004 vs. a 1.8% gain in 2003. The GDP price index excluding food and energy advanced 1.9% in 2004 vs. a 1.6% increase in 2003. The Consumer Price Index (up 0.4% in February vs. a 0.1% increase in January; the core Index is up at an annual rate of 2.8% for the first two months of the year, compared with a 2.2% increase for all of 2004); the Producer Price Index (up 0.4% in February vs. a 0.3% increase in January; the Intermediate Goods Index is now up at an annual rate of 8.4% for the first two months of the year); and, the upward trend of unit labor costs (up 0.4% in 2004 versus decreases of 0.4% in 2003 and 1.1% in 2002), justify our concern about inflation.

On the retail front, the outlook continues to remain positive. Retail sales rose 0.5% in February, versus 0.3% in January, 7.7% ahead of February 2004. Excluding autos, retail sales rose 0.4% in February, versus 1.0% in January. For the trailing three-months, retail sales, excluding autos, rose at an annualized rate 7.7% for the trailing three-months and 8.4% for the trailing twelve-months. Personal income rose 0.3% in February, rebounding from January’s decrease of -2.5%, up 5.8% from a year ago and up 6.3% for the trailing three-months. The rate of Personal Saving slowed to 0.6% in February from 0.8% in January, which may indicate consumers were diverting cash from savings to fuel spending. Personal spending increased by 0.5% in February, up from 0.1% in January. The January-February data indicates an increase in consumer spending for the quarter, but at a slowing rate from the fourth quarter gain of 4.2%. The Bank of Tokyo-Mitsubishi Weekly Leading Indicator of Non-Auto Retail Sales supports this view, indicating a slight moderation in March retail sales, showing a month-to-date increase of 1.0% versus 4.7% this time last month.

Capital spending on equipment and software rose an impressive 18.4% in 2004. The outlook for capital spending remains positive going into 2005. After tax corporate profits (the grease, if you will) rose 12.5% in 2004. In addition, capacity utilization rates increased to 79.4% in February. As production capacity tightens, capital spending will also benefit. Early indicators support this view. Shipments of non-defense capital goods excluding aircraft dropped 2.6% in February vs. a 3.6% gain in January. However, the January-February average for these shipments rose at an annual rate 12.4%, compared with a 6.2% increase in the fourth quarter. In addition, non-residential construction expenditure growth rebounded in 2004 by 1.3%, following three consecutive years of declines. Non-residential construction expenditures advanced by 1.2% in January.

In this issue, our research note compares the short and long-term effects of promotions and advertising on consumer purchase behavior relative to brand choice and purchase quantity.

STEVEN KEITH PLATT
DIRECTOR

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“MANAGING ADVERTISING AND PROMOTION FOR LONG-RUN
PROFITABILITY”

MARKETING SCIENCE, VOL. 18, NO. 1, 1999

BY: BY KAMEL JEDIDI, COLUMBIA UNIVERSITY, CARL F. MELA,
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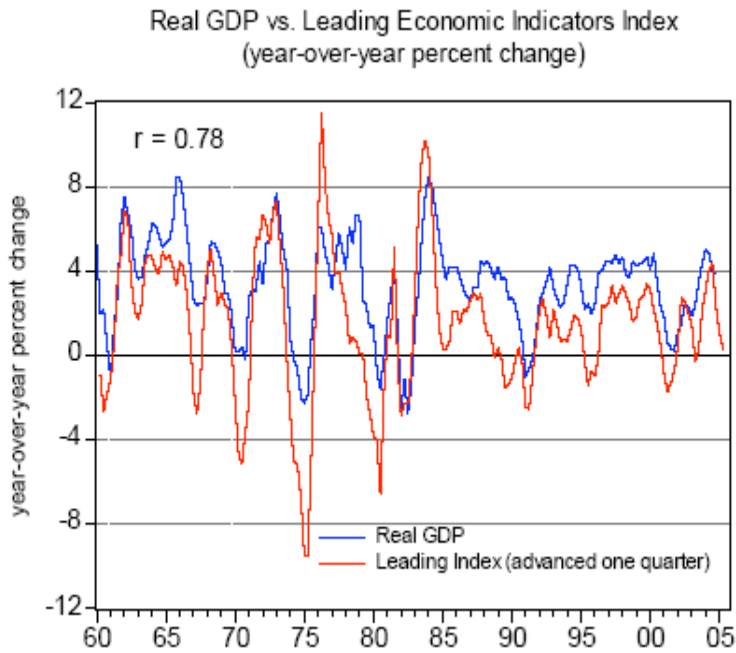
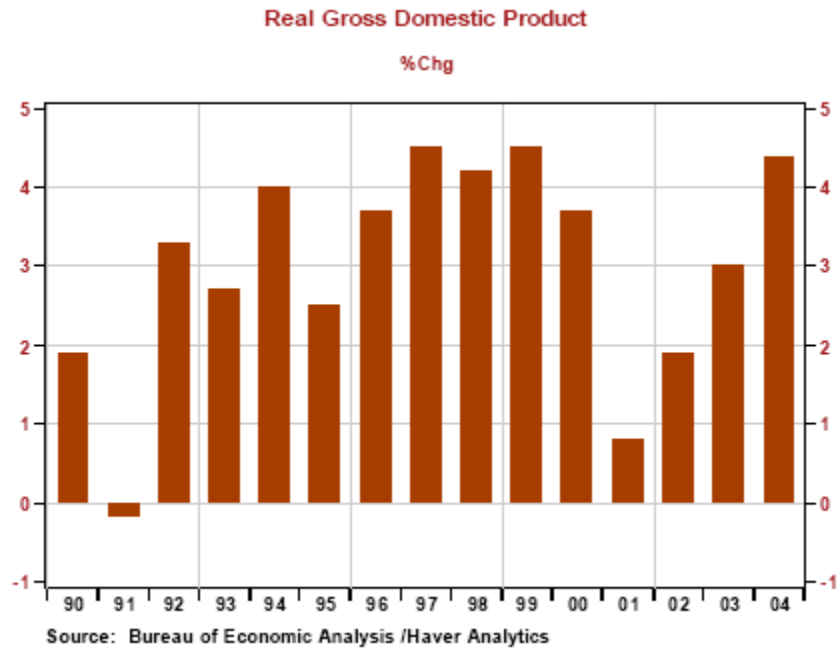
PRI’s mission is to initiate and secure the funding of studies on specific retail business issues. PRI functions as a conduit, bringing together retail executives with leading researchers. The genesis of the Retail Institute is the recognition of the wealth of knowledge being produced at the University level, on the one hand, and the need for more advanced yet practical business research and insight at the retail level, on the other. It is, therefore, the Retail Institute’s main objective to serve as a knowledge bridge between the University and retail industry and its related vendors. It will achieve this objective through the commercialization of the resources of its Research Fellows and University relationships.

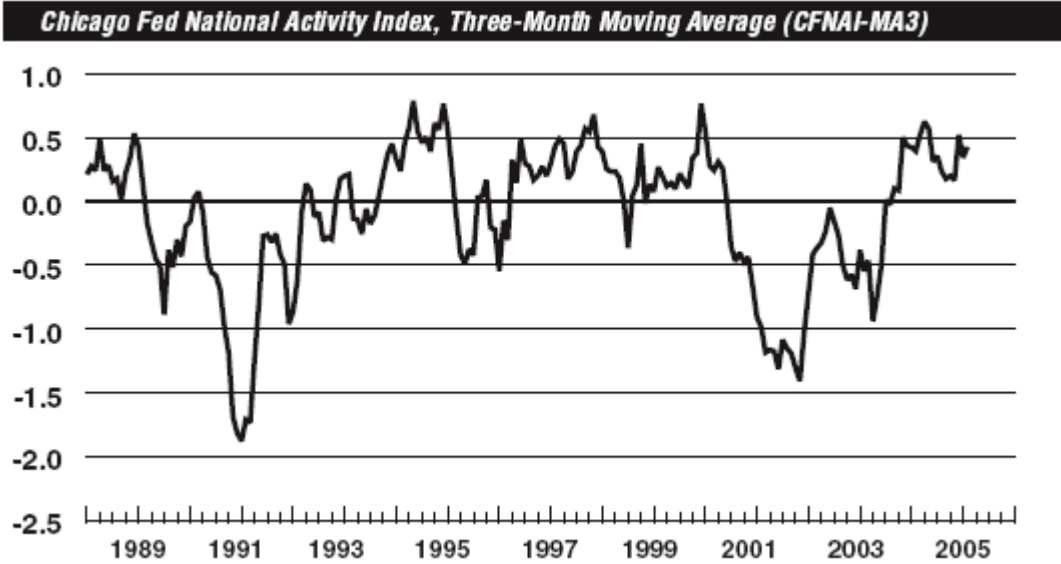
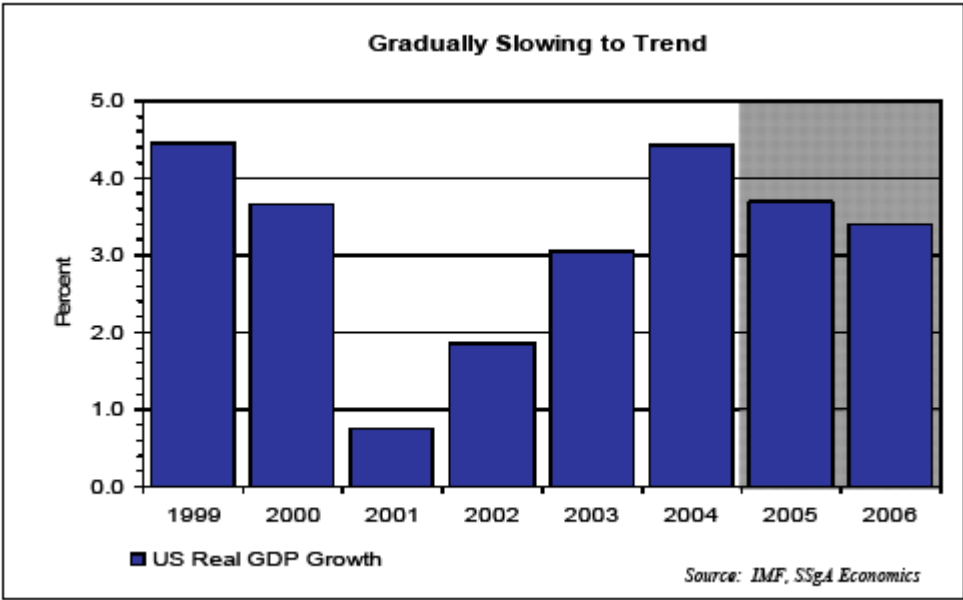
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I. ECONOMIC OVERVIEW

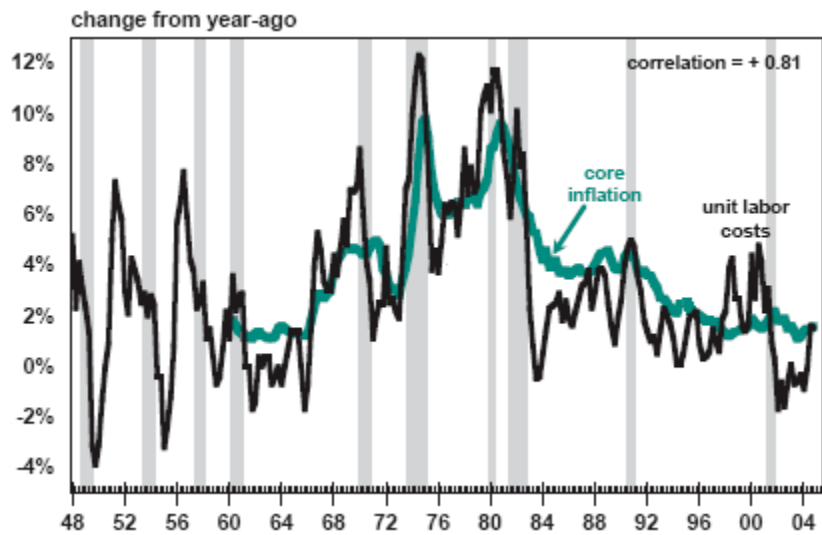
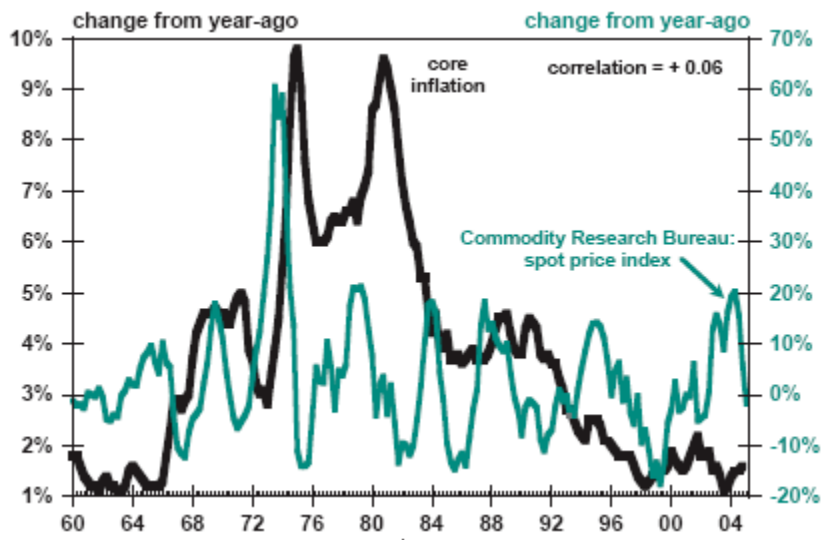
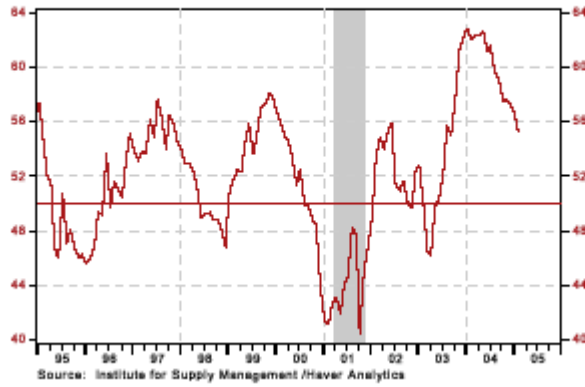
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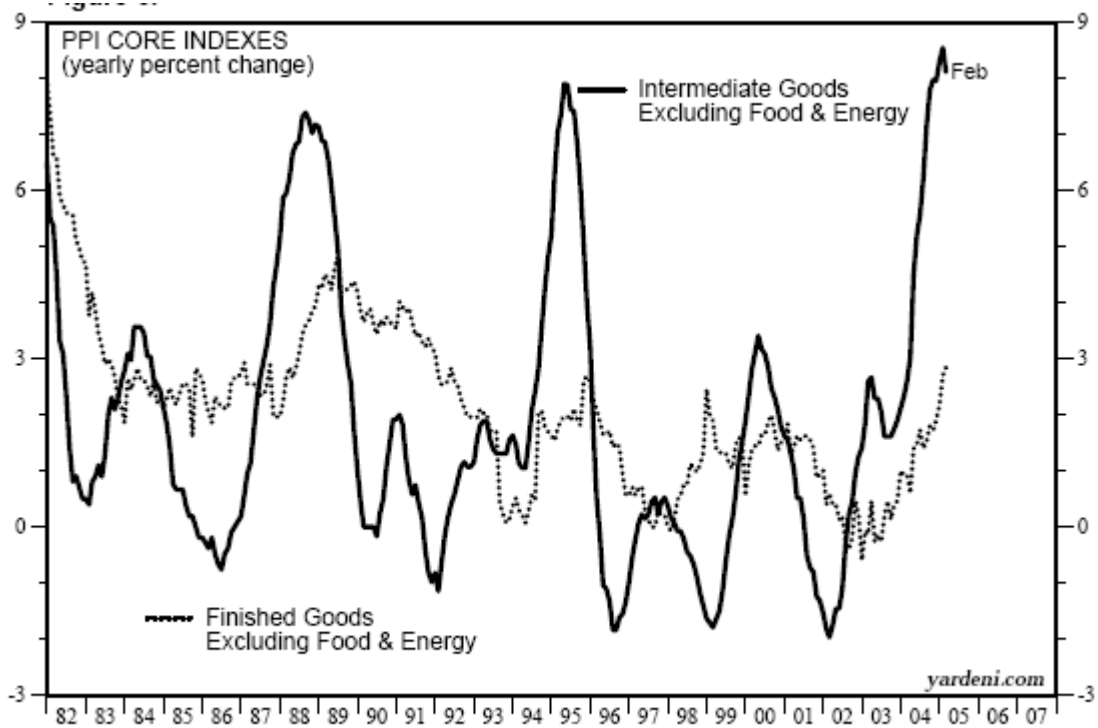




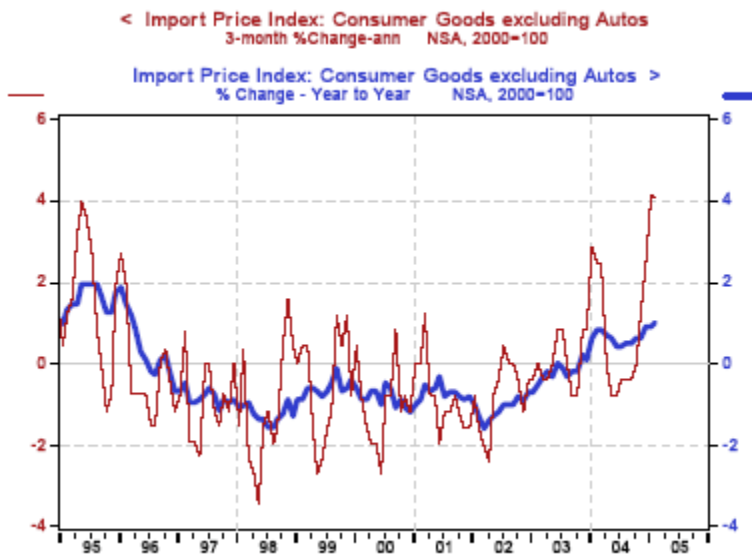
ISM: Mfg: PMI Composite Index

SA, 50+ = Econ Expand

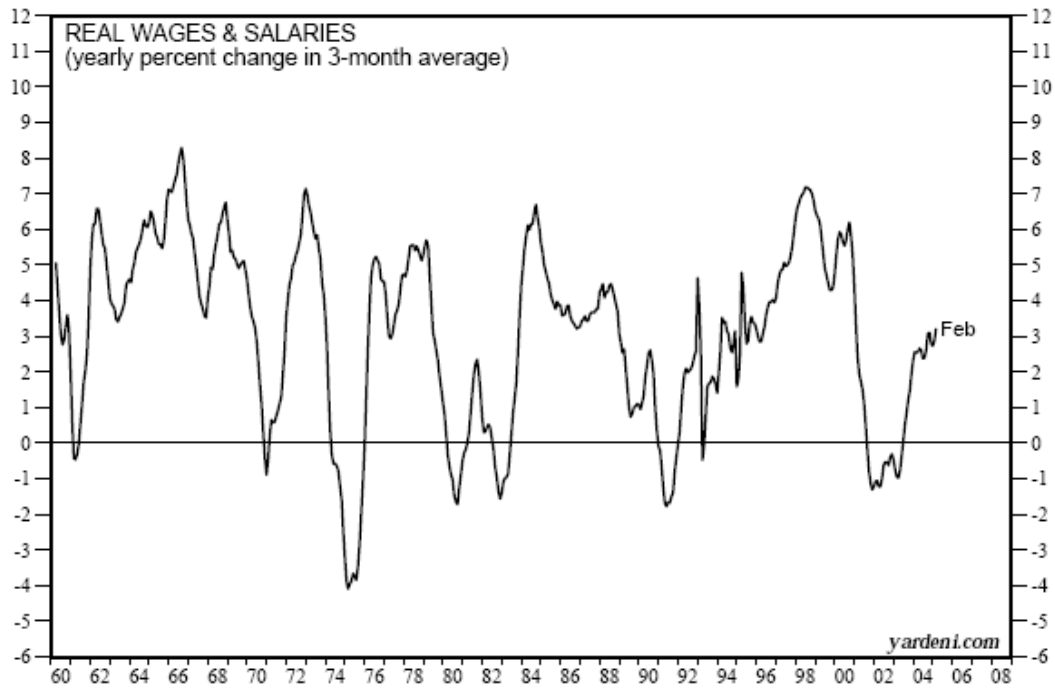




Source: U.S. Department of Labor, Bureau of Labor Statistics.



MACRO ECONOMIC INDICATORS-CONSUMER:

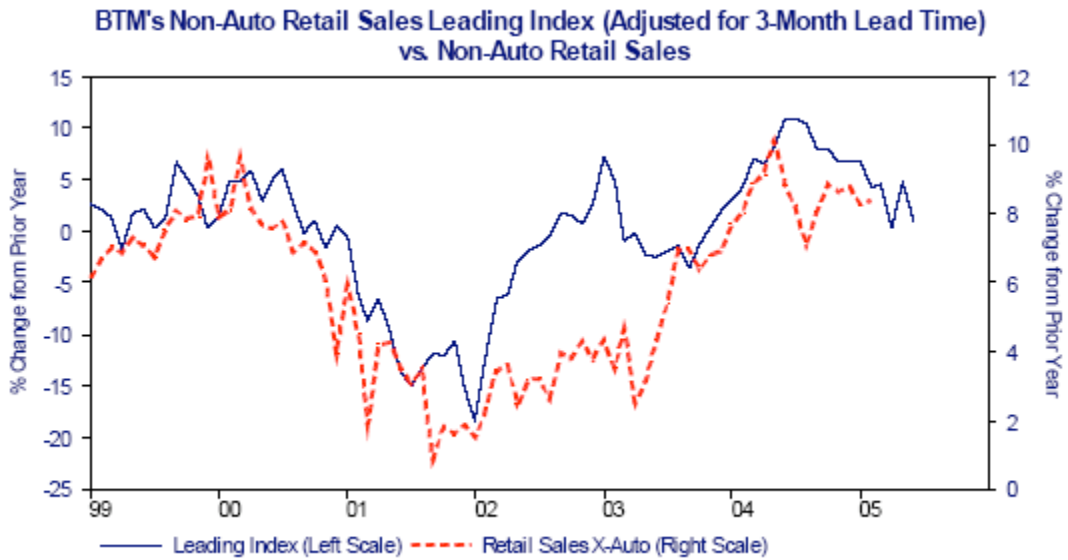
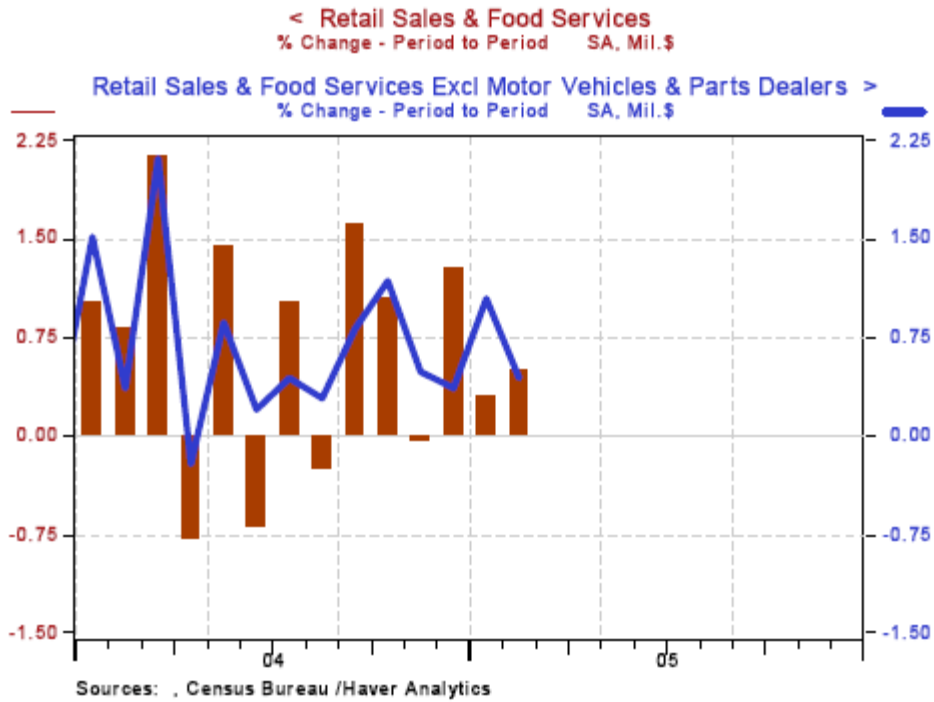


Personal Income & Consumption

	(month/month % change)			(% change : a.r.)
	Feb	Jan	Dec	3-month
Personal Income	0.3	-2.5	3.7	6.3
Real Disposable Income	0.1	-3.0	4.2	4.7
Personal Spending	0.5	0.1	0.9	6.1
Real Personal Spending	0.3	-0.1	0.9	4.5
Savings Rate (percent)	0.6	0.8	3.7	0.6 *

* value at 3 months ago

MACRO ECONOMIC INDICATORS- RETAIL:

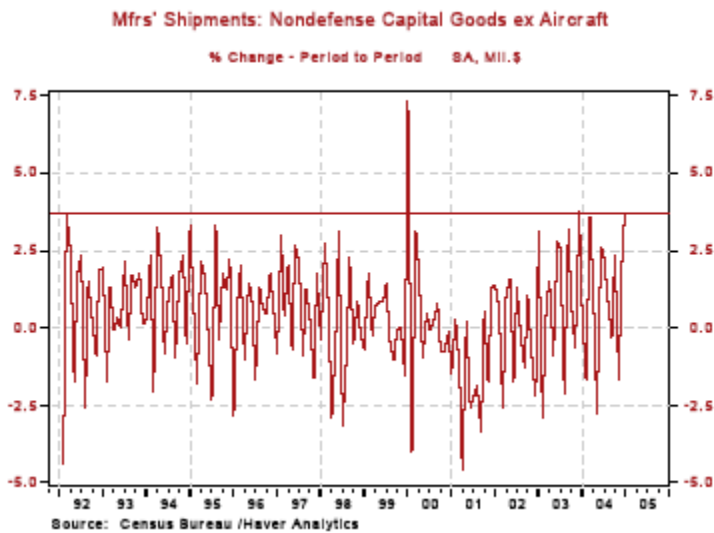
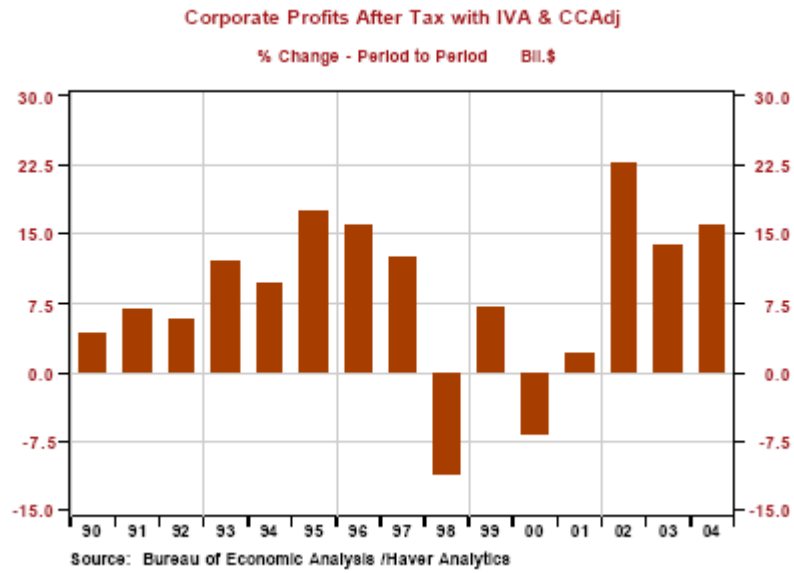


Large Retail Corporations	2004-1 st Qtr.	2004-2nd Qtr.	2004-3 rd Qtr.	2004-4th Qtr.	2005-1 st Qtr.	2005-2nd Qtr.	2005-3 rd Qtr.	2005-4th Qtr.
Operating Income Ratio	5.1%	4.7%	4.0%	----%	----%	----%	----%	----%
After-Tax Profit Ratio	2.9%	3.3%	2.8%	----%	----%	----%	----%	----%
Return on Equity (after taxes)	15.43%	16.89%	14.34%	----%	----%	----%	----%	----%

(% change)	JN-04	FB-04	MR-04	AP-04	MY-04	JN-04	JL-04	AG-04	SP-04	OT-04	NV-04	DC-04
Retail Sales (% change; x auto) vs. prior month	1.0	0.4	----	----	----	----	----	----	----	----	----	----

(\$ millions)	1999	2000	2001	2002	2003	2004
Retail Sales (% change)	8.5%	7.34%	2.9%	2.5%	5.4%	8.0%

MACRO ECONOMIC INDICATORS- RETAIL IN-STORE DEVELOPMENT:



II. MAJOR RETAIL SECTOR TRENDS:

BUILDING MATERIALS, GARDEN AND SUPPLY STORES

Sales declined -1.3% in February. On an annualized rate, sales are up 4.4% for the trailing 3-months and are up 13.1% for the trailing 12 months.

Monthly % Change	JN-05	FB-05	MR-05	AP-05	MY-05	JN-05	JL-05	AG-05	SP-05	OT-05	NV-05	DC-05
Sales	0.6	-1.3	----	----	----	----	----	----	----	----	----	----

FOOD AND BEVERAGE STORES

Sales rose 0.2% in February. On an annualized rate, sales are up 4.5% for the trailing 3-months and are up 5.5% for the trailing 12 months.

Monthly % Change	JN-05	FB-05	MR-05	AP-05	MY-05	JN-05	JL-05	AG-05	SP-05	OT-05	NV-05	DC-05
Sales	0.6	0.2	----	----	----	----	----	----	----	----	----	----

HEALTH AND PERSONAL CARE (DRUG) STORES

Sales rose 0.3% in February. On an annualized rate, sales are up 11.1% for the trailing 3-months and are up 7.5% for the trailing 12 months.

Monthly % Change	JN-05	FB-05	MR-05	AP-05	MY-05	JN-05	JL-05	AG-05	SP-05	OT-05	NV-05	DC-05
Sales	2.3	0.3	----	----	----	----	----	----	----	----	----	----

CLOTHING AND ACCESSORY (APPAREL) STORES

Sales rose 1.1% in February. On an annualized rate, sales are up 12.5% for the trailing 3-months and are up 5.0 for the trailing 12 months.

Monthly % Change	JN-05	FB-05	MR-05	AP-05	MY-05	JN-05	JL-05	AG-05	SP-05	OT-05	NV-05	DC-05
Sales	1.7	1.1	----	----	----	----	----	----	----	----	----	----

GENERAL MERCHANDISE STORES

Sales rose 0.7% in February. On an annualized rate, sales are up 10.5% for the trailing 3-months and are up 6.6% for the trailing 12 months.

Monthly % Change	JN-05	FB-05	MR-05	AP-05	MY-05	JN-05	JL-05	AG-05	SP-05	OT-05	NV-05	DC-05
Sales	0.9	0.7	----	----	----	----	----	----	----	----	----	----

DEPARTMENT STORES

Sales rose 0.5% in February. On an annualized rate, sales are up 6.0% for the trailing 3-months and are up 0.9% for the trailing 12 months.

Monthly % Change	JN-05	FB-05	MR-05	AP-05	MY-05	JN-05	JL-05	AG-05	SP-05	OT-05	NV-05	DC-05
Sales	0.3	0.5	----	----	----	----	----	----	----	----	----	----

III. RESEARCH NOTE

“Managing Advertising and Promotion for Long-Run Profitability”

Marketing Science, Vol. 18, No.1, 1999

By Kamel Jedidi, Columbia University, Carl F. Mela, University of Notre Dame, Sunil Gupta, Columbia University

This study compares the short and long-term effects of promotions and advertising on consumer purchase behavior relative to brand choice and purchase quantity. For the practitioner, this research is relevant in determining the appropriate spend on promotions and advertising. Because the ad/promotion tradeoff is brand specific, the researchers advance a model that is calibrated using over eight years of accumulated data from a (non-food) consumer packaged-goods company. This model is unique in that it considers: (1) both consumer response to short-term marketing activities measured and the long-term effect of these activities on consumer responsiveness (i.e., prior exposure to discounts increase price sensitivity), and (2) the impact from competitive actions. The outlined approach is very flexible and can be used to examine the trade-off between short-term and long-term marketing effects in many other industries and contexts. Some of the papers conclusions include the following:

1. This research confirms that advertising has a long-run positive effect on brand choice, while promotions may hurt it.
2. Advertising did not affect consumer price sensitivity. In the long-run, however, promotions cause consumers to become more price sensitive and less discount sensitive in their brand choice.
3. In the long-term, promotions make it more difficult to increase regular prices and greater discounts will be necessary to have the same impact upon consumers.
4. Deep discounting less frequently maximizes sales in the short-term, yet their impact diminishes over the long-term. Shallow but more frequent promotions are more effective.
5. The impact of promotions is greater in the short-run than the long-run.
6. Most of the effect of price, advertising, and short-term promotions is on consumer brand choice decisions (as compared to quantity decisions).
7. In the long-term, the effect of promotions on quantity purchases may be greater than that of brand choice.
8. Increases in advertising and decreases in price have mixed effects on brand profitability. Increasing promotions would negatively impact long-term profits.

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