platt | retail | institute

P.O. Box 158
Hinsdale, IL 60522
Phone: 630-920-1844
Email: skp@plattretailinstitute.org
www.plattretailinstitiute.org

Volume Four	Number Three	November 2006

PRI QUARTELY RETAIL ANALYTICS

"BRINGING RESEARCH TO RETAIL"

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.

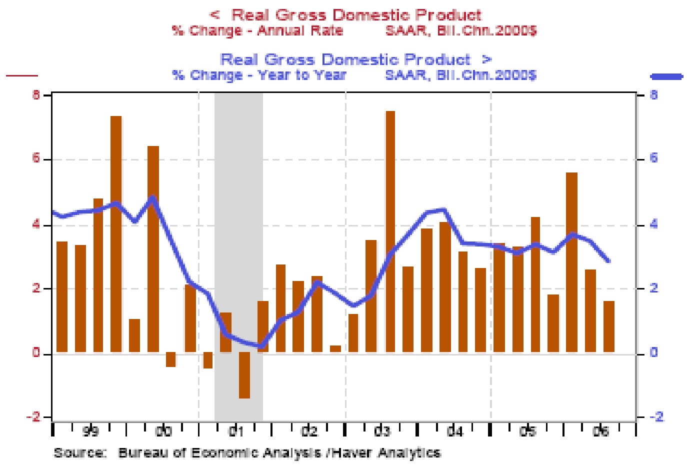
Hinsdale, IL
www.plattretailinstitute.org

I. BUSINESS OUTLOOK

BUSINESS INDICATORS

As we advanced last quarter, the U.S. economy is slowing. Third Quarter gross domestic product, the broadest measure of the economy's health, rose at a 1.6% annualized rate, versus 2.6% in the second quarter, which is half of the average 3.2% growth rate achieved during the past four years (see Chart 1).

Chart 1



The slowdown in the housing market (see Chart 2, for example, which depicts the slowdown in housing starts), will eventually impact employment. While the unemployment rate was a positive 4.4% in October (see Chart 3), the rate of employment is considered a lagging indictor. Reduced home values, increasing interest rates, and stagnant employment will be a drag on consumer spending at some point, indicating a weakening in the future.

Chart 2

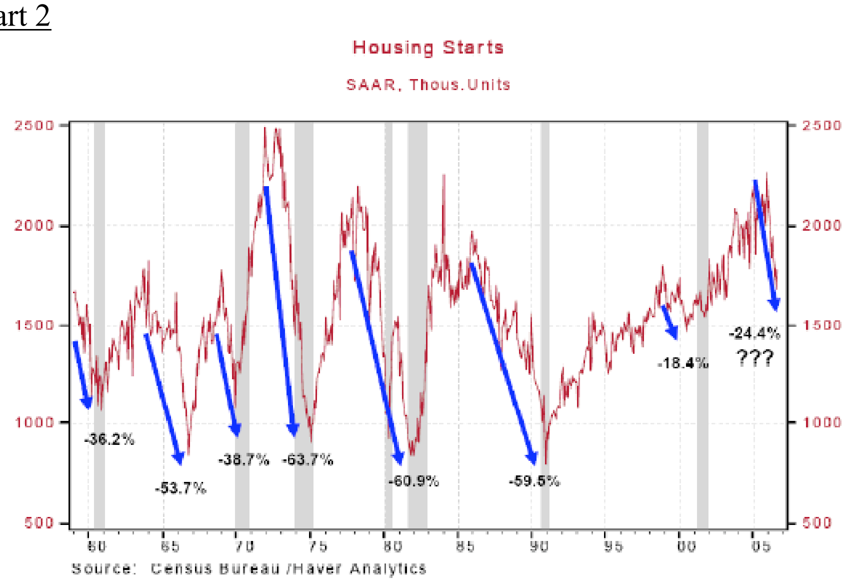
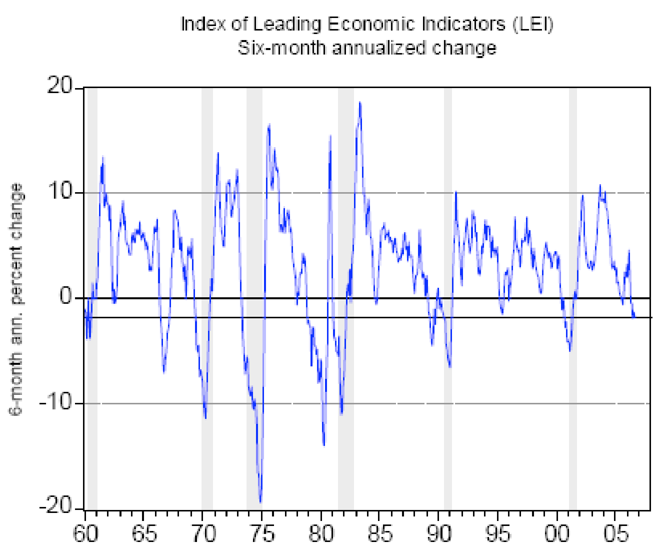


Chart 3

Support for this position can also be found by considering the Index of Leading Indicators, which gained 0.1% in September, following two monthly declines. Year-to-date, the LEI has posted five monthly declines (see Chart 4).

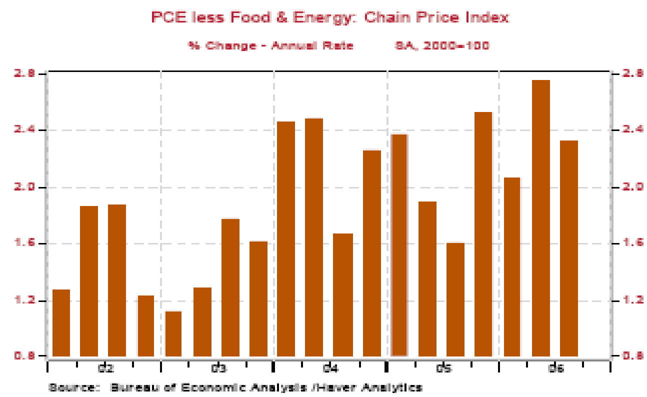
Chart 4



Source: Northern Trust Company

Look for 2006 GDP to register at 3.3% (following a 3.5% rate of growth in 2005 and 4.2% in 2004), slowing to 2.6% in 2007. On the inflation front, the core personal consumption expenditure price index, excluding food and energy, shows a deceleration in the third quarter to a 2.3% annualized increase from 2.7% gain in the second quarter (see Chart 5). This could indicate an easing in interest rates early in 2007, as the Fed moves to restart the economic engine.

Chart 5

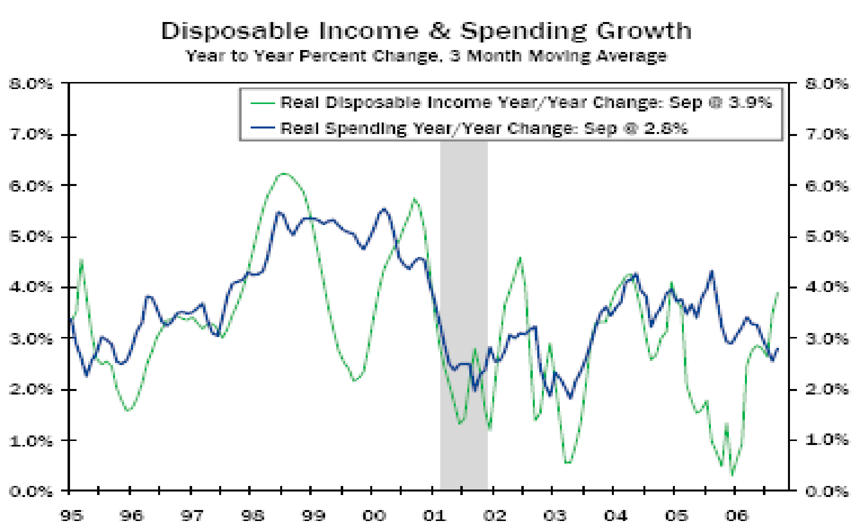


RETAIL INDICATORS

During September, retail sales fell by -.04%. This weak headline number was negatively impacted by an average 13% decline in gas prices during the month. Retail sales excluding the volatile auto, gas and building materials sectors, in fact, rose by 0.8% in September. On an annualized rate, sales are up 7.2% for both the trailing three and twelve month period excluding the auto, gas and building materials sectors. Yet we foresee an easing ahead.

Consumer spending grew at an annual rate of 3.1% in September. However, on a year-to-year basis, consumer spending grew only 2.8% in the third quarter, the smallest increase since the second quarter of 2003. As illustrated in Chart 6, this occurred despite strong wage and salary growth, and a falling of gas prices.

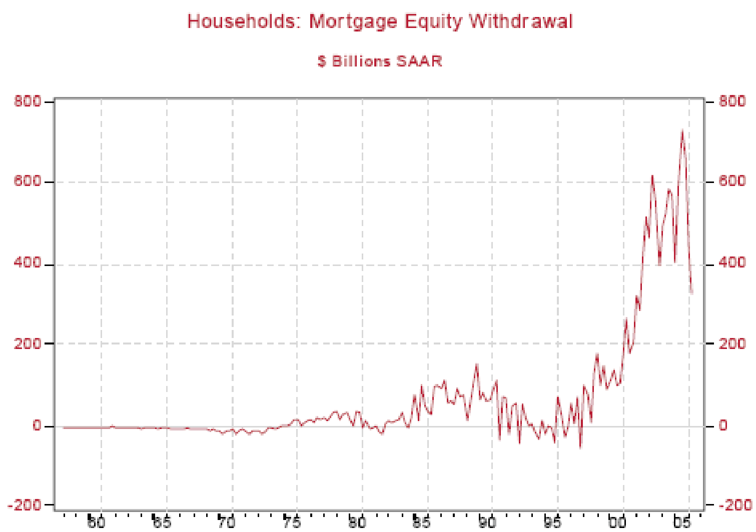
Chart 6



Source: Wachovia Economics Group

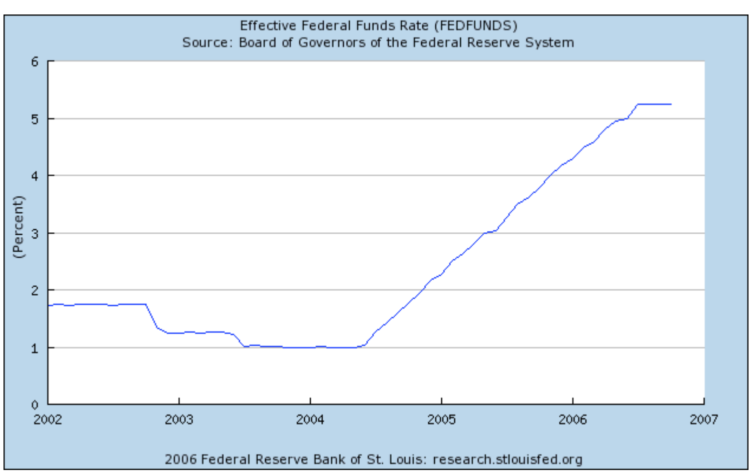
It is our view that the economy has been fueled, in part, by the wealth effect of cheap money being extracted from residential real estate (see Chart 7). As access to this easy money dries up (see Chart 8, illustrating the low federal funds rate for 2002 to 2004, which is now being reversed) and debt service costs increase, it will impact consumer spending. One need only recall a similar asset burst in stocks that resulted in a mild economic downturn in 2001. Average spending has exceeded income for some time, saving rates are in negative territory, and consumer debt burdens are high, thus consumers will have no place to go to reconstitute their balance sheets but to pull back on spending. On the other hand (punt, punt), robust capital spending, export strength, strong employment and wage gains, combined with falling gas prices could render our opinions moot (would not be the first time-but we don't think so).

<u>Chart 7</u>



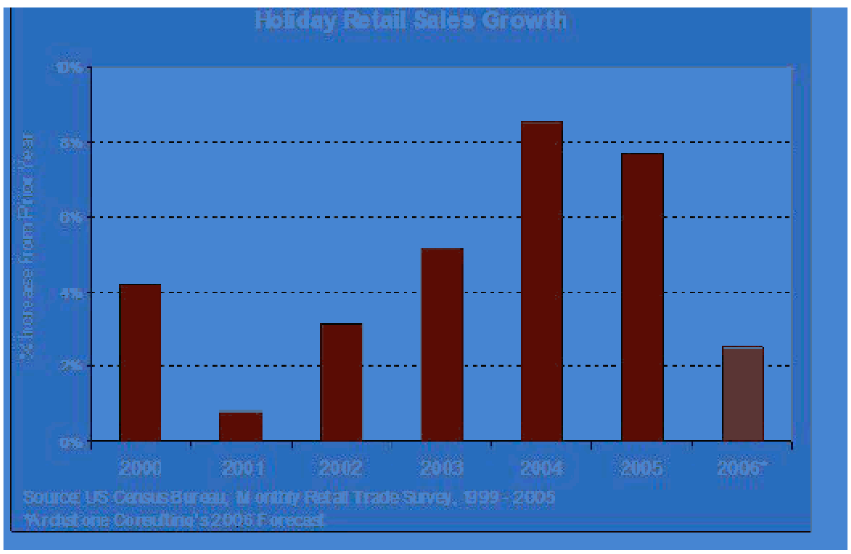
Source: Northern Trust Company

<u>Chart 8</u>



Evidence of this can be found, for example, by considering that Wal-Mart Stores October comparable retail sales grew at only 0.5%, their weakest showing since December 2000. Worse, the large retailer predicts flat November same-store sales. While department stores performed well in October, the results achieved at stores like Wal-Mart, Costco (October same-store sales of 4.0%, short of 4.6% analysts projected), and Target (October same-store sales of 3.9%, short of 4.2% analysts projected) were softening, which we believe are more indicative of the overall trend in consumer spending. And the National Retail Federation expects holiday sales to rise 5% this year, versus 6.1% last year. While 5% sounds positive, the average annual rate of increase for the past 10 years, also according to the NRF, is 4.6%. Thus, even at 5%, such an increase in sales for the holiday period indicates only a slight improvement. Archstone Consulting looks for only a 2.5% increase in holiday sales (see Chart 9).

<u>Chart 9</u>



Other evidence of this forthcoming deceleration in consumer spending and retail sales can be found by looking at retail plans for store construction. According to McGraw Hill Construction, second quarter retail construction spending growth was 2.5%, versus 4.8% in the first quarter. And at Home Depot, construction contracts fell 51% in the first half of 2006, while Target's were off 20%. Therefore, it may be said that if you do not think they will come, do not build them. This seems to be the sentiment of some major retailers.

II. MAJOR RETAIL SECTOR TRENDS

BUILDING MATERIALS, GARDEN AND SUPPLY STORES

Sales rose 0.6% in September. On an annualized rate, sales are up 7.3% for the trailing 3-months and are up 8.3% for the trailing 12 months.

FOOD AND BEVERAGE STORES

Sales fell -0.5% in September. On an annualized rate, sales are up 0.3% for the trailing 3-months and are up 3.4% for the trailing 12 months.

HEALTH AND PERSONAL CARE (DRUG) STORES

Sales rose 0.2% in September. On an annualized rate, sales are up 6.2% for the trailing 3-months and are up 7.3% for the trailing 12 months.

CLOTHING AND ACCESSORY (APPAREL) STORES

Sales rose 3.0% in September. On an annualized rate, sales are up 17.1% for the trailing 3-months and are up 10.7% for the trailing 12 months.

GENERAL MERCHANDISE STORES

Sales rose 1.1% in September. On an annualized rate, sales are up 8.3% for the trailing 3-months and are up 6.3% for the trailing 12 months.

DEPARTMENT STORES

Sales rose 1.0% in September. On an annualized rate, sales are up 4.2% for the trailing 3-months and are up 2.3% for the trailing 12 months.

III. RESEARCH NOTES

CONSUMER RESPONSIVENESS TO MOBILE MARKETING
By Kristina Heinonen and Tore Strandvik
Hanken Swedish School of Economics and Business Administration
Helsinki, Finland
Paper presented at the Stockholm Mobility Roundtable, Stockholm, 2003

Marketing messages delivered to cell phones ("mobile marketing" or "MM"), represents an outstanding opportunity to interact with customers. This is due to the ability to individually reach consumers with highly personalized messages in a timely manner. The potential downside of MM may be consumer response to privacy invasion, which can lead to a negative consumer reaction. This raises the issue of what is the likely consumer acceptance/effectiveness of MM as a new marketing media.

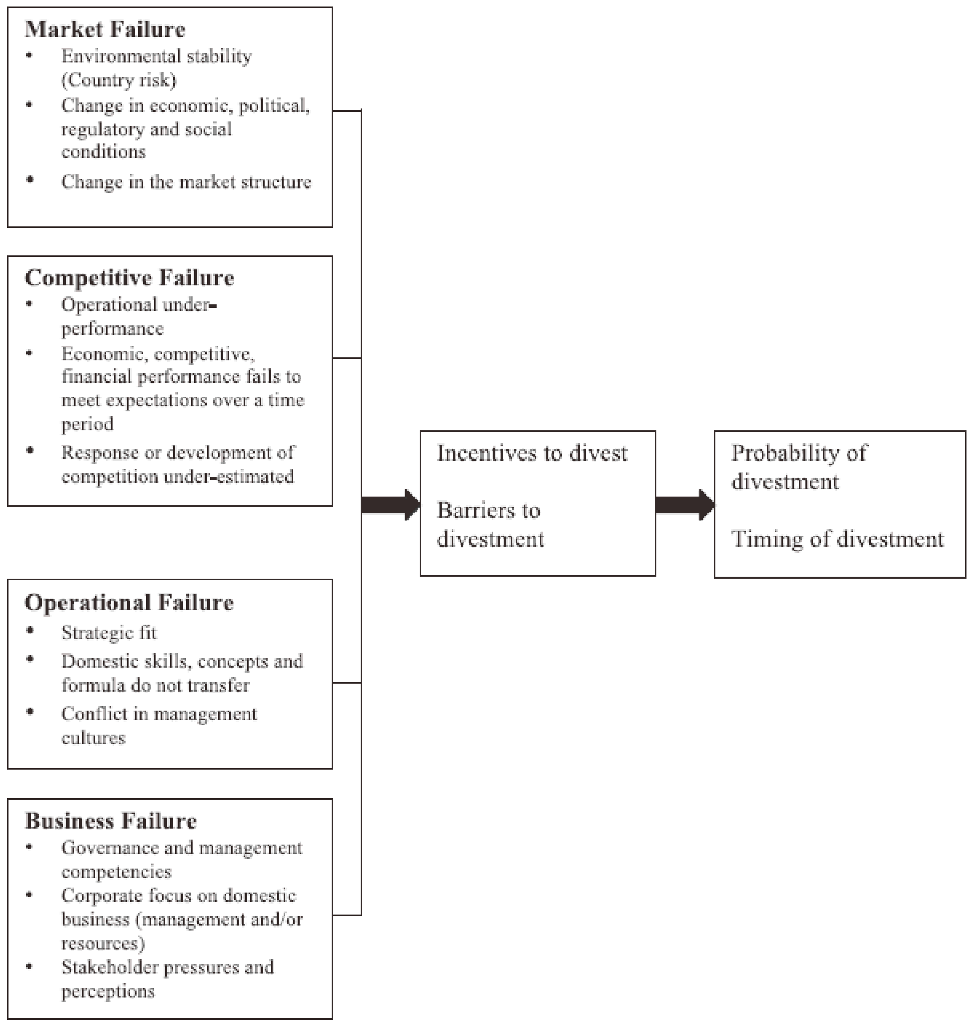
In this Paper, the researcher's advance that measurement of MM's effectiveness should be grounded in understanding consumer responsiveness to the message received. Responsiveness is defined as a consumer's willingness to receive and respond to the marketing message delivered. Their methodology to measure consumer responsiveness encompasses both consumer perceived relevance to the content of the marketing communication (the degree to which the message is focused upon and retained following exposure, shifts attitudes and/or intentions, and the consumer's response to the message), and the consumer's disturbance/acceptance of the marketing channel (how, when and where the consumer receives the message).

Applying this methodology, the researchers conducted a study to ascertain consumer responsiveness to MM versus several other forms of marketing communication. They found that consumer response to MM was lower than that found for direct mail and commercial e-mail. However, they also found that a certain segment of consumers welcomed such messages.

MM is a new marketing channel, and its implications are not yet fully understood. This Paper did not consider responsiveness to MM's delivered to consumers while in-store. Yet this can represent an outstanding application for MM. As MM is considered to be more personal than other channels, messages must be highly personal and of high interest. In a store, such personalization may be achievable.

FAILURE IN INTERNATIONAL RETAILING: RESEARCH PROPOSITIONS
By Steve Burt, University of Stirling, John Dawson, The University of Edinburgh, and Leigh Sparks, University of Stirling
International Review of Retail, Distribution and Consumer Research, October 2003

With many retailers eyeing large overseas markets, such as China and India, as new markets for expansion, a review of various factors that should be considered to avert failure may be insightful. In this paper, the researchers advance both external and internal causes for the demise of retail internationalization efforts. They further isolate this as markets that fail to materialize as expected (market failure), competitive factors (competitive failure), operational challenges related to managing an overseas operation (operational failure), and domestic business factors that impede the retailer's ability to operate an international business (business failure). The following chart illustrates this:



While the researchers do not provide a methodology for ranking these risks, they do provide a useful framework for considering the various factors that a retailer should consider when contemplating expanding into new markets.

(Our research notes are published monthly, and can be found on the National Retail Federation's website at: http://www.nrf.com/RetailResearch/View.aspx).