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RETAIL BUSINESS TREND REPORT

BRINGING RESEARCH TO RETAIL

NOVEMBER 2003:

Third quarter gross domestic product came in at a revised 8.2%. Capital spending increased a strong 14% in the third quarter and corporate profits remain strong, up 11.8% in the third quarter versus a 4.6% gain in the second quarter. The U.S. Leading Index advanced in October, up 2.9% on a year-to-year basis. Factory sector results are improving and employment is slowing increasing.

October retail sales, excluding autos, rose 0.2%. On an annualized basis, retail sales, excluding autos, rose 6.2% for the trailing twelve months and 5.3% for the ten months through October versus 2002. Building materials/hardware stores continue to show strong results, with restaurant sales recovering. Auto and gas retailers are lagging.

We continue to expect the fourth quarter of 2003 to show solid growth for the economy, with a moderation from the third quarter's brisk pace of economic activity. Positive results from businesses, modest job growth, low interest rates, and a strong stock market support this view. For the first three weeks of November, retail sales appear sluggish. Entering into the holiday shopping season beginning on November 28th, retail sales should show stable, yet moderate growth. This near-term view is predicated upon a slower pace of consumer demand, which drives retail sales, as is indicated by a recent sharp contraction in the M2 money supply, and deterioration in real wage growth.

In this issue, our research note examines the cost associated with changing prices at U.S. supermarket chains.

STEVEN KEITH PLATT
DIRECTOR

I. ECONOMIC OVERVIEW

MACRO ECONOMIC INDICATORS-BUSINESS:

(% change)	2000	2001	2002	2003-1 st Qtr.	2003-2nd Qtr.	2003-3rd Qtr.	2003-4th Qtr.
Real GDP	3.8%	.3%	2.4%	1.4%	3.3%	8.2%	
Capital Spending	7.8%	-5.2%	-5.7%	-4.4%	7.3%	14.0%	
Corporate Profits	----	-7.2%	7.6%	+\$20.4B	+\$80.6B	+105.5B	
Labor Productivity	3.0%	1.9%	5.4%	2.1%	7.0%	8.1%	

(% change)	JN-03	FB-03	MR-03	AP-03	MY-03	JN-03	JL-03	AG-03	SP-03	OT-03	NV-03	DC-03
Durable Goods Orders	1.6	-0.5	1.5	-2.6	0.3	1.9	2.0	-0.3	2.1	3.3		
Durable Goods Shipments	2.5	-1.9	0.4	-1.1	0.1	1.5	2.6	-1.7	1.4			
Leading Index	0.0	-0.5	-0.2	0.1	1.1	0.4	0.6	0.4	-0.2	0.4		
ISM Manuf. Survey (absolute)	53.9	50.5	46.2	45.4	49.4	49.8	51.8	54.7	53.7	57.0		
Industrial Capacity Utilization	----	----	----	----	----	----	----	74.6	74.9	75.0		

MACRO ECONOMIC INDICATORS-CONSUMER:

(% change)	JN-03	FB-03	MR-03	AP-03	MY-03	JN-03	JL-03	AG-03	SP-03	OT-03	NV-03	DC-03
Personal Consumption Expenditures	----	0.0	0.8	0.0	0.5	0.7	1.0	1.1	-0.3			
Change in Unemploy. Level (000)	-409	148	-5	341	212	360	-296	-157	68	-194		
Change in Employ. Level (000)	1,097	-128	-60	339	-200	251	-260	147	-52	441		
Unemp. Rate	5.7	5.8	5.8	6.0	6.1	6.4	6.2	6.1	6.1	6.0		
Personal Income	0.1	0.2	0.2	0.2	0.4	0.4	0.3	0.3	0.3	0.4		
Consumer Credit												

Real Wage Growth													
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MACRO ECONOMIC INDICATORS- RETAIL:

	2000	2001	2002	2003-1 st Qtr.	2003- 2nd Qtr.	2003-3 rd Qtr.	2003-4th Qtr.
Large Retailer After-Tax Profit Ratio	----	1.82%	2.6%	2.4%	2.5%		
Large Retailer Profits	\$73.4B	\$79.1B	\$81.2B	\$8.57B	\$9.08B		
Large Retailer Return on Equity (net Income)	----	----	----	12.44%	12.96%		
Large Retailer Return on Assets (net Income)	----	----	----	4.80%	5.07%		

(% change)	2000	2001	2002	E. 2003	E. 2004
Retail GDP	7.5%	4.6%	5.9%		
Retail Construction	----	----	-8.0%	2.0%	3.0%

	JN-03	FB-03	MR-03	AP-03	MY-03	JN-03	JL-03	AG-03	SP-03	OT-03	NV-03	DC-03
Retail Sales (% change; x auto)	----	----	1.5	-0.9	0.3	1.2	1.2	1.1	0.2	0.2		
Retail Sales (\$ in millions; x auto; adj.)	235	233	236	234	235	238	240	243	243	244		
Retail Inventories (% change; x auto)	----	----	----	----	----	----	----	----	0.8			

II. MAJOR RETAIL SECTOR TRENDS:

BUILDING MATERIALS, GARDEN AND SUPPLY STORES

Sales remained strong in October. On an annualized basis, revenue is up 15.1% for the trailing 3-months and 12.5% for the trailing 12 months. The outlook for these retailers is robust, as the housing market continues to show strength, which is a strong indicator of the outlook for these retailers. Sales of existing and new homes continue to show growth. October existing home sales declined 4.9%, but this only indicates an easing from historically high sales levels. Similarly, October sales of new homes were 3.5% below September, yet 10% above the October 2002 rate. Building permits for new homes rose 5.2% and housing starts rose 2.9% in October.

Monthly % Change	JN-03	FB-03	MR-03	AP-03	MY-03	JN-03	JL-03	AG-03	SP-03	OT-03	NV-03	DC-03
Sales	----	----	7.2	0.2	0.1	2.6	2.2	0.6	1.3	1.6		

FOOD AND BEVERAGE STORES

Food retailers continued to struggle in October. On an annualized basis, sales are down 3.6% for the trailing 3-months and up 2.6% for the trailing 12 months. Some non-grocery food retailers are delivering lower prices and, in certain instances, a more convenient format. Consumers are responding accordingly. Grocery stores continue to confront this intense competition and search for ways to differentiate the food buying experience. While new store development has been dropping, the pace of remodeling is increasing. These retailers are also experimenting with a variety of new concepts, including selling gas and toys, adding drive-thru pharmacies and banks, dollar sections, etc.

Monthly % Change	JN-03	FB-03	MR-03	AP-03	MY-03	JN-03	JL-03	AG-03	SP-03	OT-03	NV-03	DC-03
Sales	----	----	0.5	-0.1	-.04	1.0	0.9	0.3	0.3	-0.9		

HEALTH AND PERSONAL CARE (DRUG) STORES

Robust sales gains continued in October. On an annualized basis, sales are up 5.6% for the trailing 3-months and 6.9% for the trailing 12 months. Prescription reimbursements, Medicare reform and non-drug store retailers may impact pharmacy sales dominance; and many other channels are viable alternatives for front end sales. Innovation in food offerings, leveraging convenience, and expanding service offerings such as bank kiosks, 24-hour pharmacies, drive-thrus, nationwide prescription availability and online diabetes centers, for example, are insulating many drug store chains from other retail challengers.

Monthly % Change	JN-03	FB-03	MR-03	AP-03	MY-03	JN-03	JL-03	AG-03	SP-03	OT-03	NV-03	DC-03
Sales	----	----	0.8	0.1	0.3	1.3	1.4	0.6	0.3	0.5		

CLOTHING AND ACCESSORY (APPAREL) STORES

Generally continue to lack direction. On an annualized basis, sales are up 4.4 % for the trailing 3-months and up 4.6% for the trailing 12 months.

Monthly % Change	JN-03	FB-03	MR-03	AP-03	MY-03	JN-03	JL-03	AG-03	SP-03	OT-03	NV-03	DC-03
Sales	----	----	1.5	-1.4	1.7	1.2	1.3	0.0	0.9	0.1		

GENERAL MERCHANDISE STORES

Sector specific; but overall moderate growth. On an annualized basis, sales are up 4.6 % for both the trailing 3-months and for the trailing 12 months.

Monthly % Change	JN-03	FB-03	MR-03	AP-03	MY-03	JN-03	JL-03	AG-03	SP-03	OT-03	NV-03	DC-03
Sales	----	----	0.2	-0.8	1.2	0.8	1.6	0.9	0.2	0.0		

III. RESEARCH NOTE

“The Magnitude of Menu Costs: Direct Evidence From Large U.S. Supermarket Chains”
The Quarterly Journal of Economics, August 1997

By Dr. Daniel Levy, Bar-Ilan University, Dr. Mark Bergen, University of Minnesota and Research Fellow, The Platt Retail Institute, Dr. Shantanu Dutta, University of Southern California and Robert Venable, Robert W. Baird & Company

This seminal research presents insights into the cost associated with changing prices at four large U.S. supermarket chains. The authors found that changing prices is a complex process, requiring dozens of steps and involving a nontrivial amount of resources. Interestingly, they found that these supermarkets spent \$105,887 annually, per store, changing prices. On a relative basis, this price changing activity comprised 0.70% of revenue, 35.2% of net margin and cost \$0.52 per price change, on average (it is noteworthy that these costs are higher in States that require item pricing). They also found that these supermarkets changed 15-16% of their prices each week. Cost is defined here to include the following: the labor cost of changing self prices; the printing and delivery of price tags; the cost of mistakes made during the price changing process; and, the cost of in-store supervision.

These findings are noteworthy for a variety of reasons. First, knowing the true cost associated with changing prices may have an impact on how a retailer manages this process. In addition, knowledge of these costs may impact the viability of electronic shelf labeling systems which, as a result, may become more commercially viable. Finally, with intergraded CRM, loyalty cards and emerging RFID applications, more rapid price adjustments may be required; yet currently may be cost prohibitive. Thus, other technology-enhanced applications may become important to consider.

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