

Challenges for Dillard's, and Others at the Mall

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Dillard's Inc. has had some tough times lately.

The Little Rock retail chain's stock price, which peaked above \$140 last April, was trading in the high \$80s last week — having rebounded from \$61 in early January.

Dillard's net income for the year that ended Jan. 30 was \$269.4 million, down 18.8 percent from the previous year.

And the bad news didn't stop there. Late last month, Deutsche Bank Securities Inc. of New York and Zacks Investment Research of Chicago downgraded Dillard's stock from hold to sell.

But Dillard's isn't alone in having a tough time attracting customers. Department stores are “one of the worst sectors in retail, maybe the worst,” said Howard Davidowitz, chairman of Davidowitz & Associates Inc., a retail consulting and investment banking firm in New York.

Since the beginning of 2015, Macy's and Nordstrom Inc. have both seen their stock value plummet by almost one-third; Kohl's Corp. stock is down by more than 22 percent.

Davidowitz said department stores are having a difficult time because, among other reasons, they are “high-cost operators.”

He said being an anchor of a mall and operating a multilevel location is expensive. Low-cost operators like T.J. Maxx and Ross Stores Inc. don't have those operating expenses and carry many of the same items as department stores for 30 to 40 percent less, Davidowitz said.

These days, department stores are growing by adding discount stores — or sections

in their stores — to their portfolios.

Customer avoidance of malls is another challenge for department store retailers, said Britt Beemer, founder of America's Research Group of Charleston, South Carolina.

Beemer's research showed that during most weeks of the 2015 Christmas season about 19 percent of consumers shopped at an enclosed mall. That figure was 21-23 percent in 2014 and more than 28 percent five years ago.

Consumers are choosing Wal-Mart or Target to save money, he said. "That's why I think department stores are in trouble," Beemer said.

In addition, department stores aren't relevant to millennials, said Ron Friedman, the national leader of retail and consumer products at Marcum LLP of Los Angeles, an independent public accounting and advisory services firm. "Young kids just don't want to go to department stores," he said.

Friedman said enclosed malls could eventually become ghost towns if they don't begin to add features to attract customers. "The consumer wants to go into environment where there are a lot of shops, there's a lot of entertainment," Friedman said.

He suggested that department stores add attractions such as coffee shops or cafes and offer Wi-Fi to bring customers in.

Not every industry observer has written off enclosed malls.

"When you look at the malls that are 1.8 million SF or larger, you realize they are not going away," said Soozan Baxter, owner of Soozan Baxter Consulting of New York, which provides comprehensive leasing services to landlords and is a retail adviser.

Earlier this month, the Beverly Center in Los Angeles, announced it was undergoing a \$500 million renovation. "They're not doing that to be irrelevant," Baxter said.

"They're doing that to make sure they have the best offerings."

Dillard's Numbers

Dillard's fourth-quarter net income of \$84 million was down 35.6 percent compared with the same quarter a year earlier.

Same-store sales for the quarter that ended Jan. 30 were down 2 percent, marking the second consecutive quarter with a decline in same-store sales. In its third quarter, same-store sales were down 4 percent. Same-store sales are sales at stores that have been open at least a year and are considered an indicator of a retailer's health.

"The fourth quarter was difficult," Dillard's CEO William T. Dillard II acknowledged in a news release. "As sales came in less than planned, we worked hard to control our inventory during an unusually competitive environment."

Paul Trussell, a research analyst for Deutsche Bank, wrote in a March 7 research note that Dillard's was given a sell rating because it had a weak fiscal year 2015 and he doesn't think the company will improve. After hitting a record high of \$142.22 on April 10, 2015, Dillard's stock price has declined. It opened at \$88 on Thursday.

Trussell also said Dillard's lags behind in its e-commerce sales. He said online sales were less than 5 percent of total sales, while other department stores have online sales of 10 to 20 percent.

Dillard's "presently lacks the infrastructure or management initiative to catch up," Trussell wrote.

Dillard's spokesperson Julie Johnson Bull said the company is followed by several sell-side analysts, those who work for brokerage that manages individual accounts.

"While they all have access to the same information, they often have differing opinions regarding Dillard's," she wrote in an email to Arkansas Business. "We do not comment on analyst reports as a matter of policy. Moving forward, we are going to continue to focus on exceptional customer experiences, both instore and online, to set ourselves apart in the marketplace."

For the fiscal year that ended Jan. 30, Dillard's reported sales of just under \$6.595 billion, dropping about \$25 million from the previous year.

Davidowitz, however, said Dillard's might be in a better position than other department stores because, starting in 2008, it culled out underperforming stores.

“So Dillard's has put some of the problems with the bad stores behind it, and some of the others, like Macy's, are dealing with it now,” he said. In September, Macy's said that it was closing 40 of its stores out of about 770.

Discount Departments

Some department stores are turning to discount stores as a way to grow.

More than four decades ago, department stores had a bargain basement section for discounts, Davidowitz said. “That was the best area of the store,” he said. “That's where all the customers were.”

And now they are returning.

Macy's announced earlier this year that it was opening Macy's Backstage, an outlet store located within some Macy's stores.

On the company's website, it touts, “score the best bargains for her, him & your home — at prices so low every day, you won't need a coupon.”

Davidowitz said Nordstrom's fastest growing division is Nordstrom Rack, its discount store. The merchandise comes from Nordstrom's stores and boasts savings of 30-70 percent off of regular prices.

“The Rack is designed to provide the ultimate treasure hunt to style-savvy customers,” Nordstrom said in a March 2 news release that announced a Nordstrom Rack was coming to Memphis. The approximately 33,000-SF store at the Poplar Commons is scheduled to open in the fall of 2017.

Kohl's said in 2015 that it was opening its Off-Aisle discount stores, which are stocked with items that have been returned to Kohl's. This year, it plans to add two more Off-Aisle stores in Wisconsin.

Dillard's hasn't announced it is opening any new discount stores, but it operates 24

clearance stores across the country.

“Department stores have all kinds of initiatives underway to help themselves,” Davidowitz said. “They’re not sitting there doing nothing.”

Department Store Same-store Sales

	1Q14	2Q14	3Q14	4Q14	1Q15	2Q15	3Q15	4Q15
Dillard's	2.0%	1.0%	-1.0%	3.0%	-1.0%	1.0%	-4.0%	-2.0%
J.C. Penney	7.4%	6.0%	0.0%	4.4%	3.4%	4.1%	6.4%	4.1%
Kohl's	-3.4%	-1.3%	-1.8%	3.7%	1.4%	0.1%	1.0%	0.4%
Macy's	-0.8%	4.0%	-0.7%	2.5%	-0.1%	-1.5%	-3.6%	-4.3%
Nordstrom	3.9%	3.3%	3.9%	4.7%	4.4%	4.9%	0.9%	1.0%
Saks Fifth Avenue	2.6%	2.2%	1.0%	2.6%	0.6%	0.1%	-3.6%	-1.2%

Source: Deutsche Bank Securities Inc. Same-store sales are sales trends from stores that have been open at least a year .