

Consumer Business Compass

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Retail and Consumer Product Practice

The Big Picture

Retail CFOs Weigh-In on Economy, Inventory and the Upcoming Holiday Season

Last year, the credit crisis and financial market meltdown caused a significant and immediate decrease in consumer spending. Retailers were caught off guard with too much inventory and panicked, which led to unprecedented discounts throughout the 2008 holiday season and into 2009. Despite their efforts, 2008 was the worst holiday season in 40 years and retailers have since spent the majority of 2009 cutting costs wherever possible to stay afloat.

As the 2009 holiday season approaches, retailers have an opportunity to strategically balance their inventory in time to prevent deep discounting. However, they are still apprehensive about their inventory and see any decisions as being critical to the holiday season's success. In fact, a recent study by the Retail and Consumer Product Practice at BDO Seidman, LLP found that retailers are split on what is the greater risk to holiday sales – too much or too little inventory.

Inventory Balance Top of Mind for Retailers

According to the BDO Seidman Retail Compass Survey of CFOs, success this holiday season will depend on the right inventory balance. Sixty percent of chief financial officers (CFOs) at leading U.S. retailers say that too much inventory will pose a greater risk to holiday sales results than insufficient inventory levels. Still, a large minority (40%) cite insufficient inventory as the bigger concern.



Retailers are caught between a rock and a hard place. Reducing inventory is necessary, but retailers run the risk of hindering selection, which can lead to disappointed customers and fewer sales. On the other hand, merchandise overflow can lead to a frenzy of deep discounts, which can cheapen the brand and slash profits.

When it comes to increasing inventory levels, 62 percent of the CFOs say that they will ramp up buying by the first half of 2010. Specifically, 21 percent will increase purchases in the fourth quarter of 2009, 19 percent will do so in the first quarter of 2010 and 22 percent will wait until the second quarter of 2010. Seventeen percent will increase inventory in the third quarter of 2010, seven percent cite the fourth quarter and 14 percent will not increase inventory purchases until 2011 or later.

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Retailers Say Layoffs Most Successful Cost-Cutting Strategy in 2009

In addition to inventory management, retailers have implemented several cost-cutting strategies throughout 2009. When asked which cost-cutting strategy has been the most effective so far, CFOs cite layoffs the most (38%), followed by inventory reduction (30%), delayed expansion (23%), lease re-negotiation (7%) and store closings (2%).

Fortunately, for the remainder of 2009, CFOs say that they will focus most heavily on inventory reductions (36%) and delaying expansion plans (30%) to cut costs, rather than layoffs (19%). Further, 11 percent will focus on lease renegotiations and four percent will close stores.

Ultimately, retailers will continue to cut costs wherever possible until consumer spending and confidence picks up. On a positive note, many of them have an eye towards increasing inventory for the Spring and Summer seasons.

Retailers See Light at the End of the Tunnel

Retailers have their work cut out for them for the remainder of 2009 and through the beginning of next year, but they do see a light at the end of the tunnel. A large majority (83%) of retail CFOs predict that we will see a meaningful turnaround in the economy in the second quarter of 2010 or later. Forty-one percent expect to see a turnaround in the second quarter of 2010, while 15 percent cite the third quarter of 2010, 10 percent cite the fourth quar-

ter of 2010 and 17 percent don't expect to see a turnaround until 2011 or later. Last year, the highest concentration (28%) of CFOs predicted a meaningful turnaround in the second quarter of 2009.

These findings are from the most recent edition of the BDO *Seidman Retail Compass Survey of CFOs*, which examines

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the opinions of 100 chief financial officers at leading retailers located throughout the country. The retailers in the study were among the largest in the country, with revenues of more than \$100 million, including 10 percent in the top 100 based on annual sales revenue.

Some of the major findings of the BDO Seidman Retail Compass Survey of CFOs:

Battle of the Stimulus Packages.

Retailers have had to mitigate the recession with little help from the government. In fact, 69 percent of CFOs say that the American Recovery and Reinvestment Act has been unsuccessful in stemming the recession. When comparing the 2008 and 2009 stimulus acts, retailers are torn about which package provided the most relief. While the 2009 stimulus package is credited for helping to avoid a depression, it came with a \$787 billion price tag and little direct consumer

stimulus. Although short-lived, the Stimulus Act of 2008 included a series of rebate checks to qualified taxpayers and helped boost comparable store sales in May, June and July of 2008 (positive 3.0 percent, 4.3 percent and 2.6 percent, respectively). Still, when asked which one had a more positive impact on consumer confidence, 41 percent of retailers chose the 2008

package while 41 percent chose the 2009 package, 17 percent said that neither package had much of an impact and one percent said they had equal impact.

Retailers React to Healthcare Reform

Managing healthcare costs is a significant challenge for any business and the retail industry, which is the second largest employer in the US, bears a large brunt of the burden. How retailers react to healthcare reform will be critical to its success but at the end of the day retailers need employees to run operations and healthcare will be considered just another cost of doing business. In fact, 71 percent of chief financial officers (CFOs) at leading U.S. retailers do not think they will reduce headcount as a reaction to healthcare reform. While it is encouraging that most retailers will avoid layoffs as a result of reform, a large majority (80%)

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of those who do not eliminate positions will pass increased healthcare costs onto employees. The remaining retailers (20%) do not anticipate that employees will incur increased health-care costs.

Comparable Store Sales Dismal

A strong majority (72 %) of retailers cite decreased sales when comparing comparable store sales in the first half of 2009 to the first half of 2008, up from 44 percent of CFOs that cited a decrease in sales in 2008 when looking back on the first half of 2007, and 22 percent of CFOs in 2007 who reported a decrease when looking back on the first half of 2006. Sixteen percent say that comparable store sales were flat in the first half of 2009.

No Optimism for Comparable Store Sales for the Rest of the Year.

Looking forward, half (50%) of the CFOs anticipate that comparable store sales revenue will decrease in the second half of 2009 when compared to the second half of 2008, while 26 percent say sales will be flat and 24 percent cite sales will be higher. Overall, CFOs predict that comparable store sales for the second half of 2009 will be down four percent from the second half of 2008.

Comparable Store Sales Expected to Tumble in 2009

Overall, the CFOs estimate that the average comparable store sales growth for all of 2009 will tumble by seven percent. This is the first year that the BDO Seidman Retail Compass Survey of CFOs has predicted a decrease in both comparable store sales and overall sales for the year.

Rescuing Retail: Bucking the Liquidation Trend among Retailers

The headlines have not ushered in much good news for retailers this past year, as the pace of bankruptcy filings has picked up and affected many well-known companies. In a climate where consumer spending is down and businesses can no longer rely on financing options to see them through the downturn, many retailers have found themselves in the unlikely position of liquidating their retail operations.

But now, there may be some hope for retailers who are facing bankruptcy court and fear liquidation. Recently, Against All Odds, a mall-based retailer of hip-hop style urban clothing, emerged with a plan from bankruptcy court that will enable the company to continue operations as a new, restructured entity.

“In conjunction with the Debtor’s attorneys, we were able to negotiate a restructuring plan around a sale transaction and secure a guaranteed 14 percent recovery for general unsecured creditors,” said David Berliner, a partner at BDO Consulting, a division of BDO Seidman, LLP. “While liquidation is often the ultimate result these days, particularly in the case of a retail bankruptcy, this case proved that experience and creativity can yield more palatable results for all parties.”

In order to emerge from bankruptcy successfully, companies should focus heavily on core business strategy, inventory management and strategy for exiting bankruptcy. Against All Odds worked with BDO to prepare cash-flow forecasts, bankruptcy schedules, statement of financial position, liquidation analyses, monthly operating reports, financial projections and the evaluation of stores to be closed. In addition, BDO acted as a liaison with landlords regarding rent concessions being negotiated as a result of the bankruptcy. As a result of these efforts, Against All Odds was able to continue as a going concern, backed by third-party investors, as a new, restructured entity named New Deal, LLC.

It’s hard to predict how the economic environment will evolve for the remainder of 2009 and into 2010, but it is realistic to assume that more retailers will face restructuring. Ultimately, it’s important that struggling retailers explore all of the options available in order to prevent liquidation.

Retail businesses seeking assistance with restructuring or turnaround matters should contact a professional to assist them with options and ensure they get the best possible outcomes.

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Overall Sales Plummet in First Half of 2009

When comparing sales revenue in the first half of 2009 to the first half of 2008, the majority (86%) of retail CFOs report flat (20%) or decreased (66%) sales, up from 64 percent last year and 44 percent in 2007. Only 14 percent of retail CFOs say sales increased when comparing the first halves of 2009 and 2008, which is down from 36 percent who cited an increase last year when comparing sales revenue to the first half of 2007. In 2007, 56 CFOs cited an increase when comparing sales revenue to the first half of 2006.

Bleak Overall Sales Outlook

Looking forward, nearly half (49%) of the CFOs anticipate that overall store sales revenue will decrease in the second half of 2009 when compared to the second half of 2008, while 23 percent say sales will be flat and 28 percent cite sales will be higher. Overall, CFOs predicted that total store sales for 2009 will be down 5.6 percent from 2008.

Consumer Confidence Linchpin of Recovery

More than half (51%) of CFOs say that a rebound in the economy will depend on an uptick in consumer confidence. Other responses include lower unemployment levels (29%), a rebound in the housing market (13%), a rebound in the financial markets (6%) and lower fuel costs (1%). When asked what will have the greatest impact on consumer confidence for the rest of 2009, most of the CFOs cite unemployment (64%), followed by the weak housing market (20%), personal credit availability

(11%), the 2009 Stimulus Act (4%) and high fuel costs (1%).

Unemployment Delivers Blow to Consumer Confidence

Unfortunately, unemployment is top of mind this year, with 62 percent of CFOs citing it as the issue having the greatest impact on consumers so far in 2009. Last year, fuel costs (57%) were cited as the primary issue impacting consumers in the first half of 2008, while this year only two percent of CFOs cite fuel costs. Looking forward to the balance of 2009, more CFOs (64%) cite unemployment as having the greatest impact on consumer confidence, followed by the housing market (20%), personal credit availability (11%) the 2009 Stimulus Act (4%) and high fuel costs (1%).

In regards to the recession, 41 percent of CFOs are predicting that the economy will experience a meaningful economic turnaround in the second quarter of 2010. The second highest concentration of CFOs (17%) cites that the economy will not turnaround until 2011 or later.

Consumers Keen on Green

Only half (50%) of the retailers surveyed sell green products. However, of those who do sell sustainable products, 63 percent are noticing an increase in consumer demand for them.

No Comeback for Layaway

Retailers, most notably Kmart and Sears, reinstated layaway programs last November largely in response to the economic downturn. However, while the option to pay in installments does appeal to budget-conscious consumers, its comeback will likely be

short-lived. Despite a flurry of high profile layaway programs, a large majority (86%) of retailers do not plan to offer layaway programs for the 2009 holiday season – only 14 percent of retailers say they have layaway programs in place.

Did You Know...

According to BDO Stoy Hayward research, 71 percent of consumers would be happy to look elsewhere if they encountered poor customer service.

Holiday sales are expected to decline one percent this year to \$437.6 billion.

Source: NRF.

BIGresearch found that almost three-fourths of Americans are watching unemployment levels to signal the end of the recession.

According to consulting firm Hay Group, about 40 percent of retailers plan to reduce the number of people hired by as much as a quarter.

Retail Forward forecasts flat growth—compared with a 4.5 percent decline a year ago—for the holiday fourth quarter in the key holiday retail segments combined.

According to the U.S. Department of Commerce, shopping center sales grew by 0.6 percent in September compared with its prior month, while total retail sales fell 1.5 percent.

Last year, retailers invested in internal IT staff and increased training budgets 20 percent. **Source: NRF Annual IT Budget Survey, conducted by AMR Research.**

Thirty-nine per cent of retailers said sales volumes rose in the year to September, compared to 36 percent who said they fell. **Source: The CBI Distributive Trades Survey.**

Mark Your Calendars...

The following is a list of upcoming conferences and seminars of interest for retail and consumer product executives:

November 2009

November 3 – 5	BAI Retail Delivery Conference & Expo Boston Convention & Exhibition Center, Boston, MA
November 9 – 11	Chain Store Age Executive SPECS Sheraton Wild Horse Pass, Phoenix, AZ
November 15 – 17	PLMA's Private Label Trade Show Rosemont Convention Center, Chicago, IL
November 17 – 18	Retail Week Fashion Summit 2009 Jumeirah Carlton Tower, London, UK
November 18 – 20	MAPIC The International Market for Retail Real Estate 2009 Palais des Festivals, Cannes, France

December 2009

December 3 – 4	NRF Taxation Committee Winter Meeting Neiman Marcus, Dallas, TX
December 8	RILA's Government Affairs Committee Meeting TBD

BDO Seidman Retail & Consumer Product Practice

BDO Seidman, LLP has been a valued business advisor to retail and consumer product companies for almost 100 years. The firm works with a wide variety of retail clients, ranging from multinational Fortune 500 corporations to more entrepreneurial businesses, on myriad accounting, tax and other financial issues.

For more information on BDO Seidman's service offerings to this industry vertical, please contact one of the regional service leaders below:

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