



To: US Retail Partners
From: Darrell Rigby and Kris Miller

It's official: On Monday the National Bureau of Economic Research announced that the US economy has been in a recession since December 2007. But in what has been a lackluster year and holiday season for retailers so far, the Thanksgiving weekend provided better-than-expected results. It is unlikely, however, that one positive weekend will be enough to overcome what could turn into the worst holiday season on record. November same-store sales growth was the lowest in over 35 years. This followed the recent release of largely disappointing third-quarter results. Even online sales are suffering, with slowing growth since May that turned negative for the first time ever in November. And ongoing macroeconomic deterioration makes continued sales declines a possibility. Though there were pockets of good news such as a slight increase in consumer confidence and falling gas prices, unemployment reached a 15-year high in November, following its fifth straight monthly increase.

Consumers made a brief appearance over the Thanksgiving weekend

A number of organizations have provided what are in effect real-time estimates of sales over the holiday weekend. Each organization employs its own survey techniques, definitions and sample sets, which leads to some variation in the results. The general consensus is that sales on Black Friday and the Thanksgiving weekend were up. Traffic measures vary significantly, however, depending on whether or not online shoppers are included.

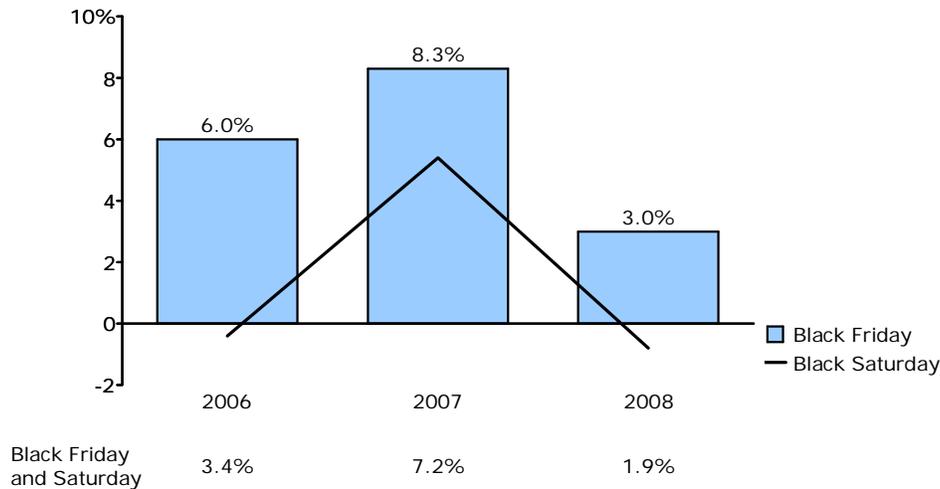
According to ShopperTrak, GAFO sales on Black Friday increased 3% over 2007, to \$10.6 billion (**Chart 1**).¹ Although notably slower than last year's 8%-plus increase, sales exceeded expectations. Bill Martin, ShopperTrak's cofounder, called Friday's results "truly amazing and . . . a testament to the resiliency of the American consumer."

¹ GAFO is a measure of sales at stores that sell merchandise normally sold in department stores. It reflects sales of general merchandise; clothing and clothing accessories; furniture and home furnishings; electronics and appliances; sporting goods, hobby items, books and music; office supplies, stationery and gifts. See Chart A in the Appendix for definitions of sales measures.

Although sales on Saturday trailed off – down 0.8% versus 2007 – combined growth for the two days was 1.9%.² And although shoppers spent more on average than last year, ShopperTrak reported a dramatic 19.3% drop in foot traffic versus 2007 for the three-day period, the largest drop the company has ever recorded.

Chart 1:

ShopperTrak: Black Friday and Saturday sales growth, 2006-2008



Source: ShopperTrak

The National Retail Federation (NRF), which measures combined sales at brick-and-mortar stores and online, estimated that 172 million shoppers visited stores and Web sites from Thursday to Sunday, a 17% increase over last year’s 147 million. The number of Thanksgiving Day shoppers increased dramatically, up 48% to 16.2 million. And doorbuster specials drew consumers to stores, making Friday the busiest shopping day of the weekend, with nearly 74 million shoppers. The NRF also reported that average spend increased 7.2% over 2007, to \$372.57 per shopper – this following a drop last year of 3.5%.³

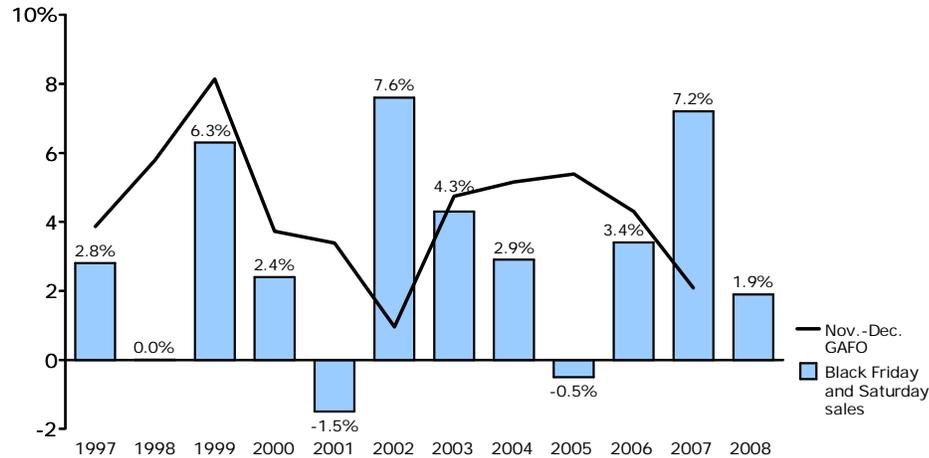
Despite the positive weekend news, the outlook for the holiday season remains bleak. Historically there has been little correlation between sales over Thanksgiving weekend and overall holiday sales, suggesting the bump in sales last week may not be an indication of stronger holiday sales to come (*Chart 2*).

² ShopperTrak’s sales figure is derived from the Census Bureau’s GAFO retail sales data, as well as its own intelligence on shopper movement and sales statistics.

³ The NRF data are based on a survey of 3,370 consumers that asked how much they planned to spend over the course of the weekend, including how much they had already spent.

Chart 2:

Year-over-year change in Black Friday and Saturday sales and November-December GAFO, 1997-2008



Source: ICSC (1997-2002 Black Friday and Saturday sales); ShopperTrak (2003-2008 Black Friday and Saturday sales); Census Bureau (GAFO)

Not all Black Friday discounts were extraordinary, but most attracted shoppers

Many luxury retailers offered unprecedented deals this Thanksgiving weekend. As a writer for *The New York Times* remarked, “Sixty percent off is the new black.” Among those lowering prices significantly was Saks, which cut fall fashion and accessory items by as much as 70%. And Barneys New York customers received an e-mail promotion for 50% off goods in its “designer freak-out sale.”

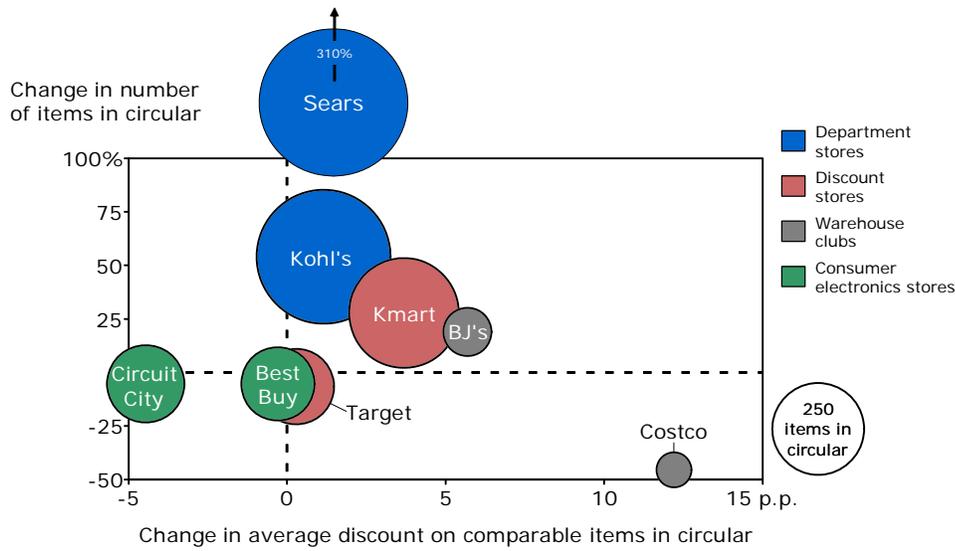
A number of retailers published Black Friday ads earlier than usual this year, trying to build consumers’ excitement and draw them into stores. And Friday’s doorbusters did entice shoppers with rock-bottom prices on lots of popular items. Department stores led the charge, offering deeper discounts across a wider variety of products (*Chart 3*). As we discussed in our last newsletter, Sears quadrupled the number of items it featured in its Black Friday circular, publishing a massive 48-page book with close to 700 items on sale. Kohl’s touted its “tremendous after Thanksgiving deals,” increasing both the number of items on sale and the average discount compared to 2007. Promotional depth at warehouse was also greater, with discounts at BJ’s averaging more than 5 percentage points higher than last year. And although it offered discounts on fewer items than it did last year, Costco increased the depth of its discounts by an average of 12 percentage points on featured products.

But not all retailers offered significantly better deals than they did in years past. Target’s 2008 Black Friday ad offered roughly the same depth and breadth of discounts as last year. Best Buy and Circuit City also offered a similar number of doorbuster specials in

2007 and 2008. But while Best Buy's discounts were in line with last year's, Circuit City's average reduction was almost 5 percentage points less than the store offered in the past (see *Chart 3*).

Chart 3:

Change in depth and breadth of Black Friday discounts, 2007-2008



Note: Change in number of items measures the percentage change in the number of items featured in Black Friday circulars from 2007 to 2008; change in average discount measures the percentage point difference between 2007 and 2008 discounts on comparable items; number of comparable items by retailer ranged from 10 to 44; the diameter of each circle in the chart indicates the approximate number of items the retailer advertised
 Source: Company Black Friday circulars

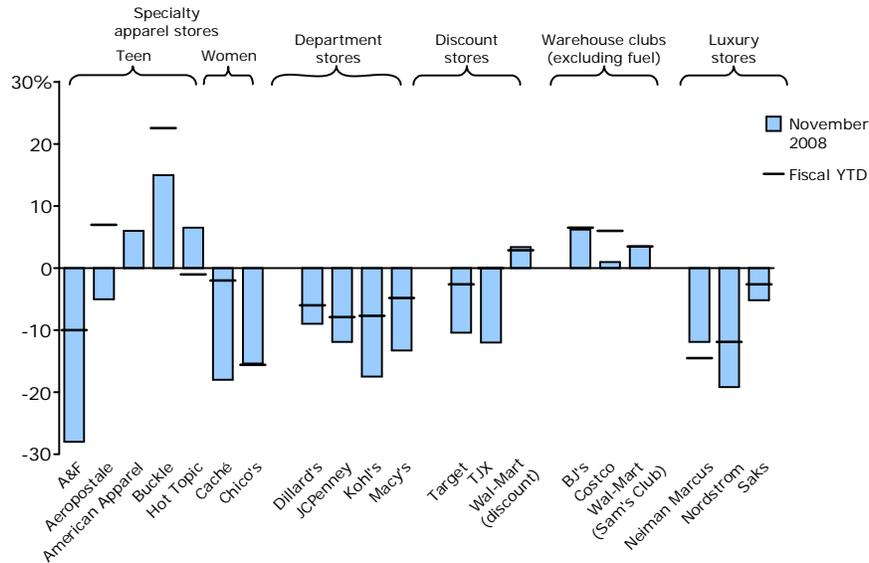
Retailer performance deteriorated further in November

Before we discuss November's results, it is important to note that a late Thanksgiving may skew monthly data this year. There was one less post-Thanksgiving shopping week in November this year than there was in November 2007 – a month that delivered relatively strong growth. Although there is little correlation between the number of days between Thanksgiving and Christmas in terms of overall holiday sales, the effect of fewer shopping weeks in November is likely driving November results even lower.

Although sales were up Thanksgiving weekend, the rest of the month was challenging. November same-store sales fell 2.7% compared to last year (*Chart 4*), marking the second consecutive month of overall decline. This represents the worst monthly same-store sales performance since the International Council of Shopping Centers (ICSC) began tracking the metric in 1969. And excluding Wal-Mart, same-store sales were actually down 7.7%, the sharpest drop since this aggregate was first calculated in 1991. These weak results prompted the ICSC to revise its holiday forecast down for the second time: It now predicts flat to -1.0% growth in November and December same-store sales.

Chart 4:

Change in same-store sales,
November 2008 and fiscal year to date



Note: Costco includes US stores only; Costco's November same-store sales for all locations increased 3.0%; Nordstrom includes full-line stores only; BJ's, Costco and Neiman Marcus 2008 YTD numbers are through October; American Apparel has not reported 2008 YTD numbers
Source: ICSC; Financo; company press releases

Luxury stores were among the hardest hit in November, dropping 10.5% compared to last year, though the decline was not as significant as October's 19.2% drop. But luxury sales were fueled by the heavy discounting discussed above, which means those sales came at the expense of margins. Heading into the holidays, and before the effect of Thanksgiving sales were felt, third-quarter earnings per share (EPS) were down sharply. Saks was down 300% from the third quarter of 2007, and Nordstrom was down 50% over the same period (*Chart 5*).

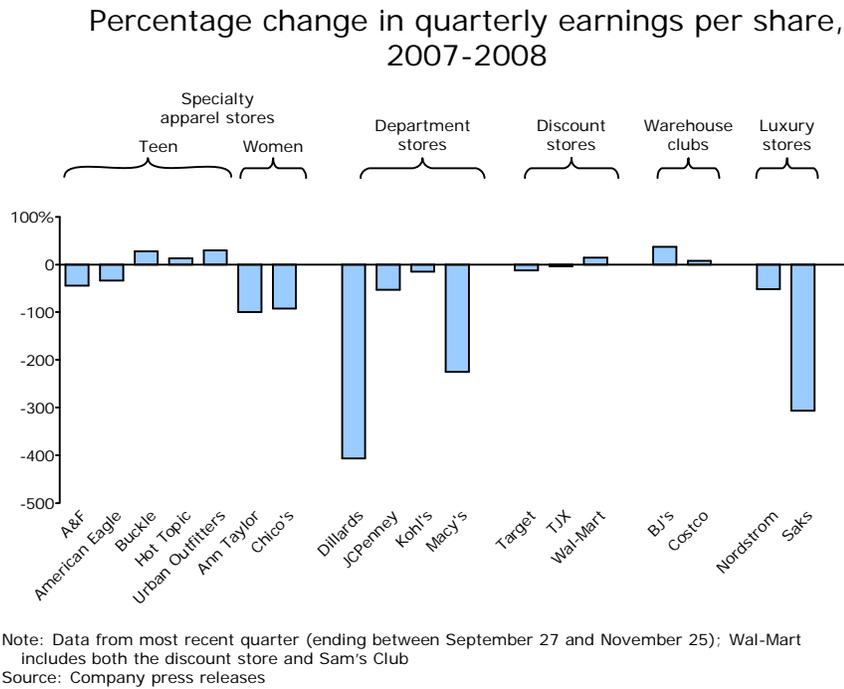
Department stores also saw steep drops in same-store sales, down 13.3% in November (*see Chart 4*). Lower sales volume and heavy promotional activity negatively impacted their third-quarter earnings as well, with drops ranging from 14.8% at Kohl's to over 400% at Dillard's.

Within the specialty apparel category, the teen segment continues to perform better than women's. American Apparel, Buckle and Hot Topic all showed positive same-store sales growth in November. But some teen apparel retailers suffered last month. After a run of positive same-store sales, Aeropostale's growth turned negative in November. And Abercrombie & Fitch's same-store sales dropped significantly, down 28.0% versus November 2007. According to Piper Jaffray's *Taking Stock with Teens* report, teenagers think of A&F as the most expensive retailer in the survey sample, which may explain the company's poor performance in the face of widely available discounts at other clothing retailers. Women's apparel stores that target a more mature demographic have been suffering for a while. Some analysts suggest this is a function of women in their 30s, 40s

and 50s cutting back for themselves before cutting back for their families, and a reflection of the economic uncertainty produced in particular by a lack of job security and tight credit. Both Chico's and Ann Taylor, for example, reported 90%-plus drops in third-quarter EPS (see Chart 5).

Warehouse clubs had the strongest growth in November, with same-store sales (excluding fuel) up 2.3%. Within this segment, BJ's again led the way with same-store sales up 4.1% and its third-quarter EPS up 37.1%. Costco also had positive results, posting 1.0% domestic same-store sales gains (excluding fuel) and an EPS gain of 8.0%. Wal-Mart led the discount category with domestic same-store sales growth of 2.0% and a company-wide increase in EPS of 14.3%. Wal-Mart's growth was fueled by both its traditional customer base and new customers trading down and seeking out lower prices.

Chart 5:



Cyber-Monday gave a momentary boost to rapidly declining online sales growth

On Cyber-Monday – the Monday after Thanksgiving, when people return to work and to faster Internet connections at their offices – comScore estimates shoppers spent \$846 million, a 15% increase over 2007 but lower than last year's 21% growth. Online sales growth on Monday eclipsed growth the rest of the weekend: Sales on Thanksgiving Day and Black Friday grew just 2% this year compared to 25% growth last year. Cyber-Monday 2008 was the second biggest day of online shopping on record. The biggest day remains last year's "Green Monday," the second-to-last Monday before

Christmas. This is typically the final opportunity for consumers to receive items by Christmas with (often free) standard shipping.

Web traffic was up 10% over last year on Cyber-Monday according to the Nielsen Online Holiday eShopping Index. The Akamai Net Usage Index for Retail reported peak traffic of 6.7 million users per minute at online retail sites, up from 4.6 million last year. And just as consumers flocked to brick-and-mortar discounters for low prices, their online counterparts were also popular destinations. On both Black Friday and Cyber-Monday, Wal-Mart and Target were two of the most visited sites on the Web. But the two most popular destinations on both days were eBay and Amazon.com (*Chart 6*).

Chart 6:

Top 10 visited retail Web sites

Black Friday	Cyber-Monday
1. eBay	1. eBay
2. Amazon.com	2. Amazon.com
3. Wal-Mart	3. Wal-Mart
4. Target	4. Target
5. Best Buy	5. Best Buy
6. Circuit City	6. Sears
7. Dell	7. Dell
8. Sears	8. Overstock.com
9. Kohl's	9. Netflix
10. JCPenney	10. Toys "R" Us

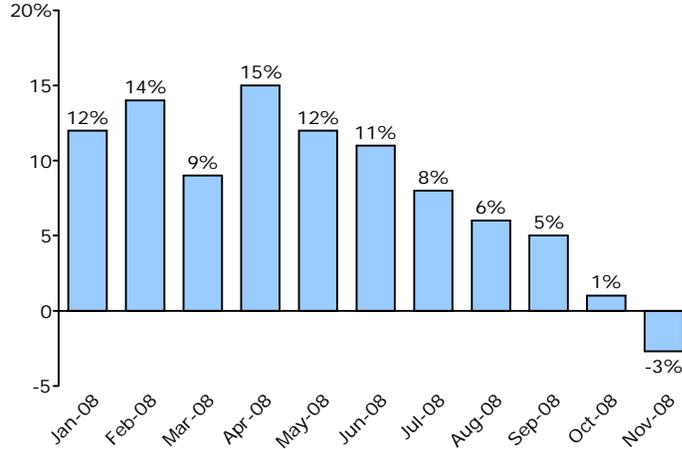
Source: Nielsen Online

Still the sales boost over the long weekend did little to speed slowing online sales. According to comScore, November e-commerce fell 2.7% – the first incidence of negative growth since the company began tracking the data in 2001, and a continuation of a seven-month slowdown (*Chart 7*). The Census Bureau recently released its official third-quarter e-commerce sales results, which show just 4.6% growth over last year, even lower than the 6% growth estimate that comScore recently announced (*Chart 8*).

December online sales are not expected to rebound much. In a November 25 forecast of holiday sales, comScore predicted flat growth versus 2007, when sales grew 19% over the holiday period. And comScore chairman Gian Fulgoni warned that if financial markets deteriorate further or if more banks or retailers fail, “all bets are off,” suggesting online holiday sales could be even worse.

Chart 7:

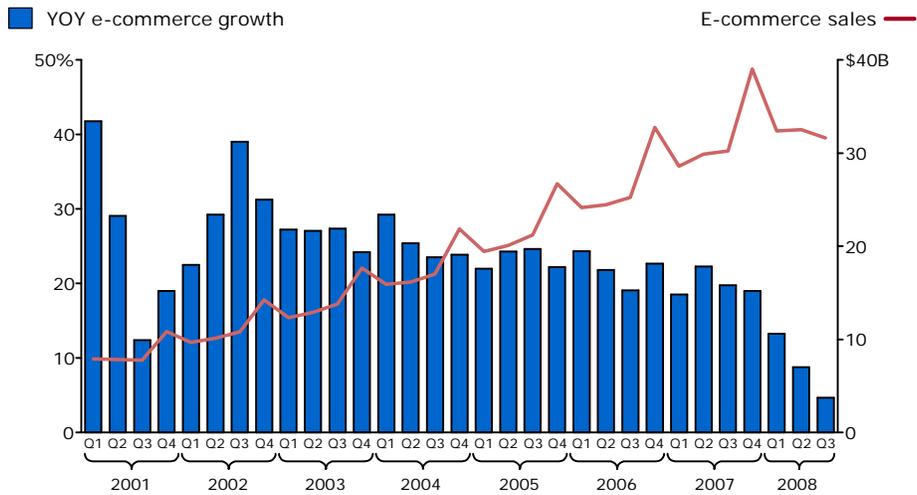
Retail e-commerce growth rates,
January-November 2008



Note: Excludes travel, auctions, autos and large corporate purchases
Source: comScore

Chart 8:

Quarterly e-commerce sales and growth,
2001-2008



Note: Third-quarter 2008 data are preliminary; e-commerce sales are sales of goods and services where an order is placed online by the buyer, or price and terms of sale are negotiated online; payment may or may not be made online
Source: Census Bureau

Promotions influenced where people shopped and what they bought

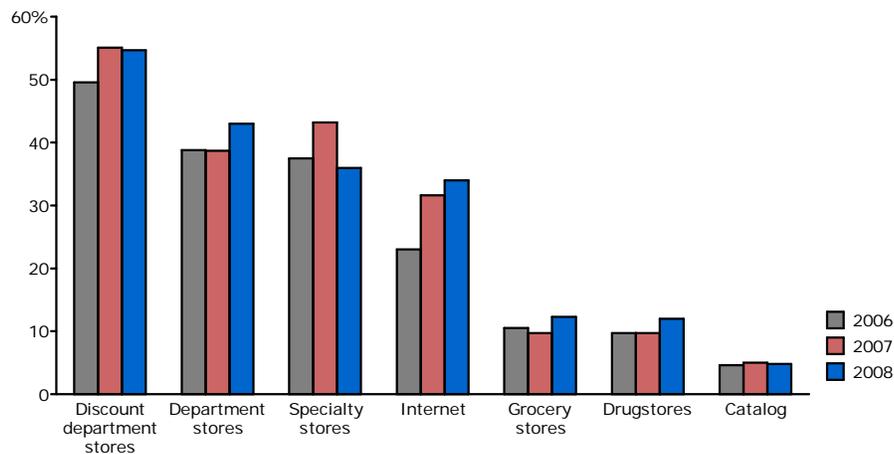
Discount stores were again the most popular destination for shoppers over the weekend, as consumers focused on value and price (*Chart 9*). And department stores were the second most popular shopping destination, beating out specialty stores – likely a function of their heavy promotional activity.

Clothing and clothing accessories were again the most popular items purchased over the weekend (*Chart 10*). Here the sales increase may have been driven by a renewed focus on practicality and value. In Bain’s recent work with market research firm Communispace, many consumers reported plans to spend less on “wants” this year and more on “needs.”⁴ One respondent remarked that “money is tight. We will be giving practical things, like clothing.” Another shared a similar sentiment: “In this economy, the only things I can justify giving are the things the person can actually use. No more trinkets and extras.”

Consumer electronics offerings were also near the top of the list, driven by popular items like Nintendo Wii and the Wii Fit game and accessory kit. Consumers also took advantage of promotions on brand-name HDTVs and digital cameras.

Chart 9:

Where people shopped on Thanksgiving weekend,
2006-2008

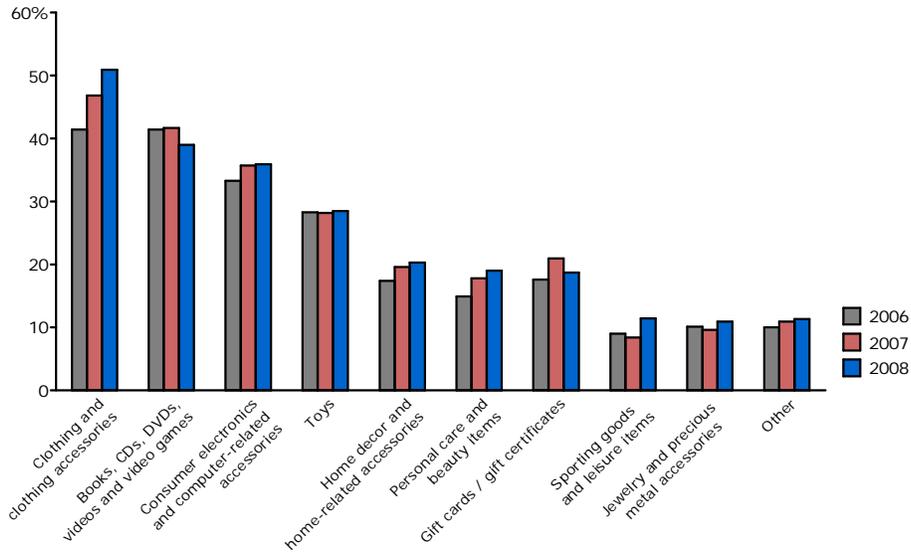


Note: Based on a consumer survey of 3,370 people; Thanksgiving weekend spans Thursday through Sunday
Source: NRF/BIGresearch survey

⁴ A Communispace community, or panel, is a private online site where up to 400 invited prospects and customers regularly spend time brainstorming, sharing feelings and experiences, and discussing trends to help a company figure out its marketing and business strategies. These private communities are facilitated by Communispace to keep the “conversation” relevant and insightful.

Chart 10:

Gifts people bought on Thanksgiving weekend,
2006-2008



Note: Based on a consumer survey of 3,370 people; Thanksgiving weekend spans Thursday through Sunday
Source: NRF/BIGresearch survey

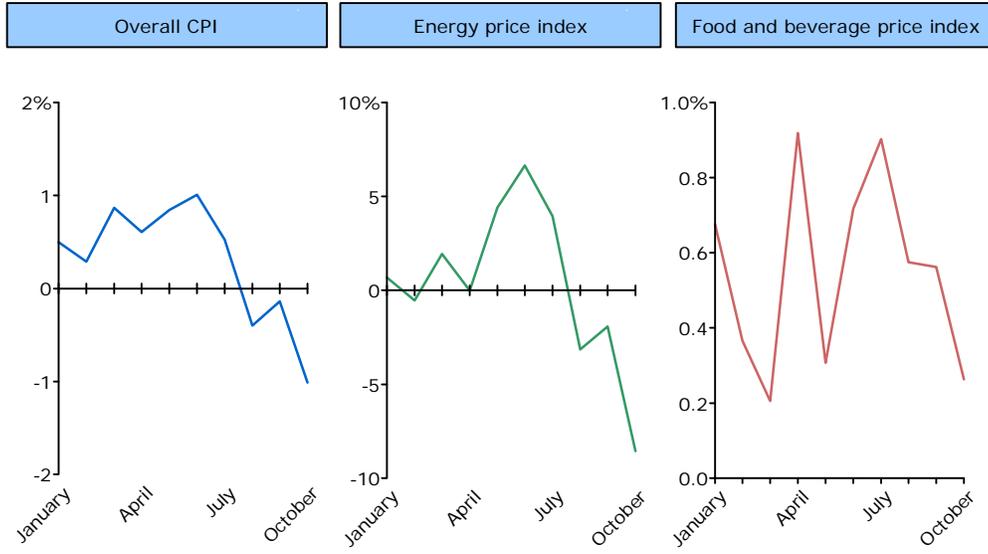
General macroeconomic deterioration continues to overshadow pockets of good news

The Conference Board’s Consumer Confidence Index rose to 44.9 in November from the previous month’s all-time low of 38.8. The increase surprised economists, who had predicted the index would remain unchanged. The change may well have been influenced by falling energy and food prices. Consumer prices excluding fuel and food fell in October for the first time since 1982, and the overall CPI decreased by 1% (*Chart 11*), the steepest drop since the index was first calculated in 1947. Additionally, gasoline reached a 46-month low in November at \$1.81 per gallon (*Chart 12*).

But a critical measure of economic health is unemployment, and that rate continues to grow. After four months of increases, November’s monthly unemployment rate reached a 15-year high of 6.7% (*Chart 13*). And nonfarm payrolls fell by 533,000 in the month, the largest drop in 34 years and much higher than experts’ prediction of a 320,000 decrease. November marks only the fourth month in the last 58 years in which nonfarm payrolls have fallen by more than 500,000. This rapid spread of unemployment and the growing concern over job security are two reasons why consumers are pulling back on expenditures. Consumer spending saw its biggest drop since the 2001 recession, falling by 1% in October (*Chart 14*).

Chart 11:

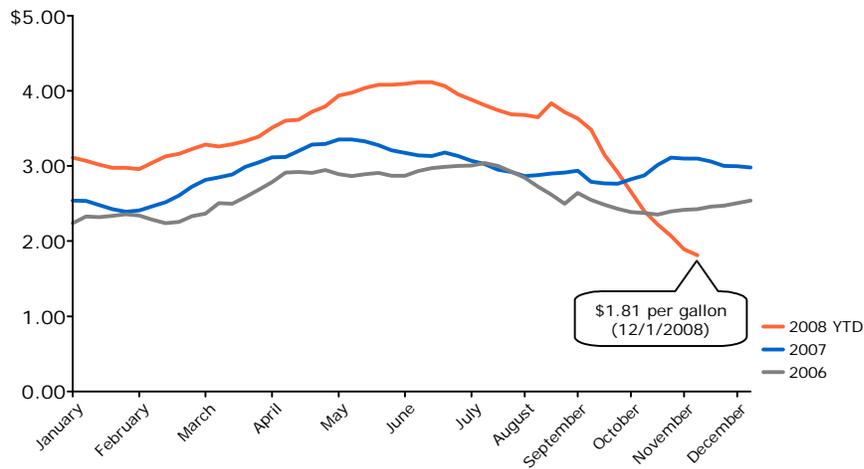
CPI monthly growth, 2008 YTD



Source: Bureau of Labor Statistics

Chart 12:

US regular gasoline average weekly retail price, 2006-2008



Note: Weekly average retail gasoline prices for all formulations of regular-grade gasoline
Source: Energy Information Administration

Chart 13:

Unemployment rate and change in nonfarm payrolls, 1980-2008

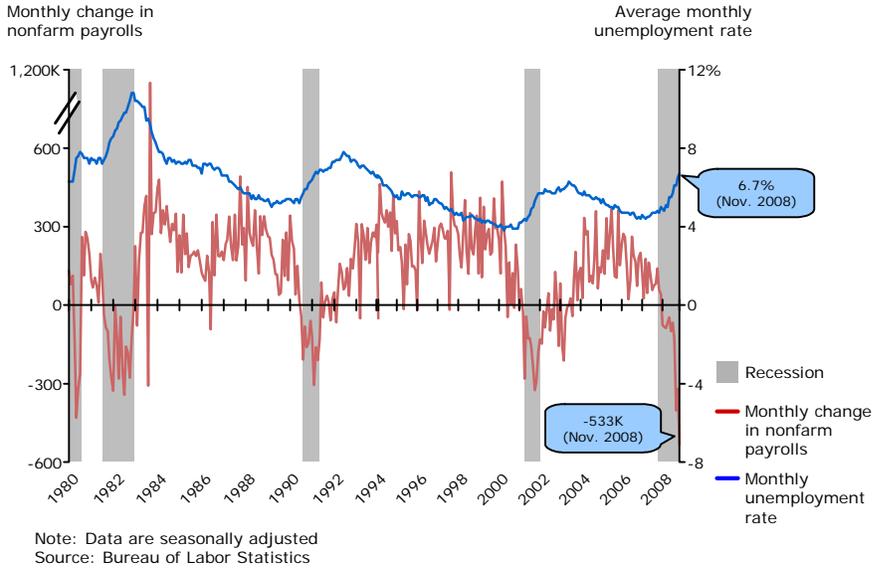
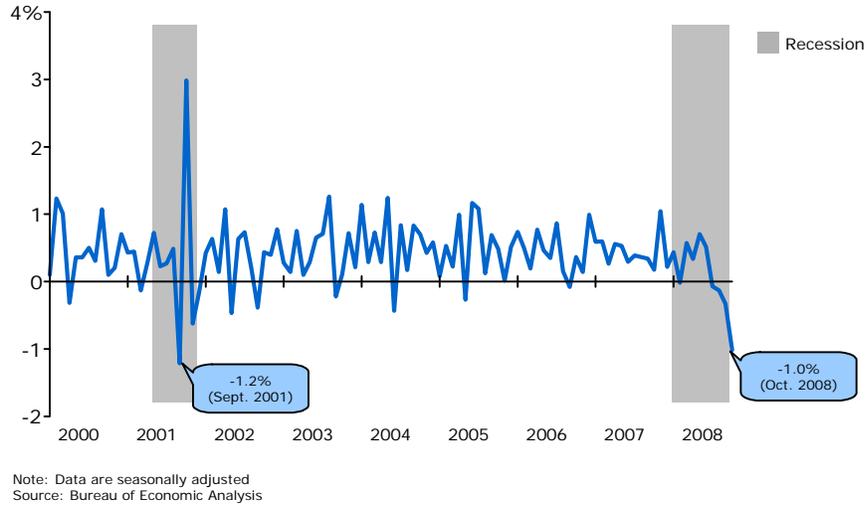


Chart 14:

Monthly consumer spending growth, January 2000-October 2008



The United States has officially been in a recession since December 2007. Although most post-World War II recessions have lasted an average of just ten months, the general consensus is that this one will not end any time soon. Real GDP shrank by 0.5% in the third quarter, and forecasts from Goldman Sachs and Morgan Stanley are for decreases of up to 5% in the fourth. This would represent the lowest quarterly growth since the 1982 recession.

In our next newsletter, we will explore some of the critical planning requirements for retailers to effectively manage through this prolonged recession.

Newsletter schedule

Our next newsletter will be released in mid-December. We will then release a final issue with a wrap-up of the 2008 holiday season in mid-January (*Chart 15*). Please let us know if you have any questions or need additional analysis.

Chart 15:

Indicator and newsletter schedule

Data source	Dec				Jan			
	10	17	24	31	7	14	21	28
US Census Bureau Advance Retail Sales				▲ 12-Dec			▲ 14-Jan	
Monthly same-store sales						▲ 8-Jan		
Michigan Consumer Sentiment Index		▶ 12-Dec	▲ 23-Dec			▶ 16-Jan		
Consumer Confidence Index					▲ 30-Dec			▲ 27-Jan
Bain Holiday Newsletter	◆◆				◆◆			

▶ Denotes preliminary data release

Appendix

Chart A:

Definitions

	GAFO	GAFS	GAF	General merchandise	Nonauto retail sales
• General merchandise stores	✓	✓	✓	✓	✓
• Clothing and clothing accessories stores	✓	✓	✓		✓
• Furniture and home furnishing stores	✓	✓	✓		✓
• Electronics and appliances stores	✓	✓			✓
• Sporting goods, hobby, book and music stores	✓	✓			✓
• Office supplies, stationery and gift stores	✓				✓
• All other retail trade sales not included in GAFO (excluding auto and auto parts)					✓
• Auto and auto parts sales					

Source: Census Bureau; analyst reports

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