

# What are the odds ...?

Following an extremely mild autumn, many retailers were itching for a cold season to help correct margins, but it hasn't worked out to be a perfect picture at all.



Warren Head

The listed reporting season began with a superb result from Kathmandu which upgraded its annual forecasts in August, confirming its favouritism with once-coy stockbroking analysts. The news from other retailers was erratic with softening spending in an uncertain economic climate underscored by the toll of the Christchurch earthquakes. Briscoe chief executive Rod Duke says he has never experienced such "prolonged negative economic conditions."

The closure and substantial demolition of stores in the red-zoned Christchurch CBD has removed retail floor space and reduced competition in the city. Those returning in the coming year(s) will find demand created by office workers heavily reduced; in a survey of the city's CBD businesses, Colliers International reported 21% as unlikely to return – this would equate to 100,000 m<sup>2</sup> office space. They say they cannot measure Christchurch retail demand at all.

However, all of the city's major shopping centres will re-open: Eastgate after a partial rebuild of carparking damaged in the February 22 earthquake and a remodelling of some store frontages. Property owner NPT

revalued this asset downwards, reflecting loss of rental growth.

Rental trends vary sharply in other major cities. Colliers says Auckland Queen Street retail has experienced a rise in both prime rentals (+1.1%) and capital values in the 12 months to June 2011. "We anticipate more positive rental and capital value growth over the next two months. In contrast, Wellington's premier retail street Lambton Quay had a 2.1% decline in prime rentals and a 4.3% decline in prime capital values in the 12 months to June 2011."

Debt deleveraging by New Zealand households is not stopping any time soon but it may be losing intensity, says the ANZ Bank. Its economic team takes a conservative view of trend growth for the next five years, but they do see scope for a 'springboard recovery from the second half of 2011 and into 2012'. Christchurch will be a huge source of economic growth – but only when the rebuild begins and as yet no one is sure if there is enough spare capacity to meet the demand.

Kathmandu's sales curve defies market trends during a tough winter season for most retailers. While major Australian retailers David Jones are in the doldrums

and Colorado has retrenched staff, the adventurer Kathmandu has recorded a substantial improvement against the general trend. July year sales of NZA\$306m, up \$60.2m, or 24.5%, have allowed the company to project a net profit of \$63m-\$65m, up 31-36% on 2010's \$47.9m result.

Kathmandu cites investment in inventory as helping to kick sales upwards; customers have revelled in the favourable weather since Easter, and new stores have been busy. Chief executive Peter Halkett said "our key strategies of new store roll-outs, upgrading of existing stores and on-going growth in our product range have all delivered increased sales."

Other retailers have found it harder to translate blue skies into sales.

## Hallenstein Glasson

The mild autumn in New Zealand (especially during May) saw Hallenstein Glasson's turnover fail to match that of last year. Group sales for the 17 weeks to 29 May this year declined -2.4% on the same period last year and net profit was down 16.5%. The group's new chief executive, Graeme Popplewell, said that speciality fashion (Glassons' market segment) was experiencing

aggressive discounting. Margin erosion was likely, due to competition and the need to clear winter stock.

Sales growth of 6.1% was achieved in Australia where climatic conditions have been more favourable and Glassons Australia has performed well. Seven Hallenstein Glasson stores were closed in Christchurch by earthquake damage.

Forsyth Barr retail analyst Guy Hallwright says, "The Australian sales increase implies that New Zealand sales through February-May were down around -5.5%, vs. -0.9% in the first half. The bulk of the decline is likely to have been in Glassons."

## Postie plus improving

Postie Plus Group produced a 4.75% sales gain to \$29.64m in the April 2011 third quarter, with gross margin improving. Nine-month sales reached \$86.18m, up 4.6% on 2010. Although three of PPGL's Christchurch stores remained closed, customer demand appears to have diverted to other PPGL stores in the city. The group's new chairman, Richard Punter, said "Whilst the market continues to be tough, the group is continuing to make healthy growth in market share

with its Postie same store-sales showing an increase of 3.35%.”

The performance indicates a favourable consumer response to the group’s ongoing rebranding of the postie stores and high-energy marketing. Campaigns featuring both Jayne Kiely and former entrant in *New Zealand’s Next Top Model* TV series, Ruby Higgins, are apparently quite effective. PPGL is unlikely, however, to elude the effects of the mildest start to winter in 75 years.

## Restaurant brands disrupted

With 19 stores, Christchurch represents a significant part of Restaurant Brands’ turnover and earnings and, whilst fully insured from a loss-of-margin point of view, lost sales from store closures since 22 February to the end of the first quarter exceeded \$3m.

The \$25.1m net profit for 2011 was driven by another bumper year for KFC with its record sales of \$235.8m – 5.6% up on prior year and 4.4% up on a same-store sales basis. “This is even more impressive when you consider this was achieved after posting 9.2% same-store sales growth in the previous year,” says chief executive Russel Creedy. These sales generated record earnings with \$52.1m EBITDA, up 12.7% on the prior year.

During a strong year for transformation, nine stores were transformed and four new KFCs built. Total KFC store numbers are now 89 with 50 having been transformed. Promotional activity included the launch of KFC Grilled and, whilst controversial, the Double Down bread-less burger proved a sales success.

The trend is not unblemished, with Starbucks pouring less coffee and overall sales down 11.3% while Pizza Hut sales decreased by 27.7%.

The market is aware of the possible introduction of a fourth brand, Taco Bell, into New Zealand. Restaurant Brands told its annual meeting it has not made a

decision on this. Creedy said “We have had early discussions with Yum!, the owner of the brand, and have spent some time visiting Taco Bell in the States and evaluating their stores and product offerings.

“We believe that the brand does have “legs” in New Zealand, but there is a considerable amount of work yet to do before we can make a decision to undertake a pilot in this country”.

## ‘On the money’

Briscoe group “continues to confound its critics by delivering consistently outstanding results,” says managing director Rod Duke. By getting the basics right, Briscoe was “very much on the money for these unpredictable and challenging times.”

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Rod Duke, MD Briscoe Group.

The 2011 profit result of \$24.1m, up 14.6%, was described by stockbrokers First NZ Capital as ‘how it should be done’ and Macquarie called it ‘the best of the bunch’.

Duke told the annual meeting, “The significant changes we made to the way we operate, and the skill of our team to execute has reduced the cost of doing business while at the same time increased our competitiveness.”

Duke says, “In the over 20 years I’ve been operating in this country, I don’t recall experiencing such prolonged negative economic conditions. There can be no doubt that there has been an unquestionable shift in consumer attitudes towards saving, borrowing and spending, and that this is having a widespread impact on retail sales.

“Retailers are bearing the brunt for this changing behavior – and, of course, as one would expect,

the devastating Christchurch earthquake to have made matters worse.” The coincidence of Easter and Anzac Day impacted group sales by around \$5m.

“Fortunately, that is not scheduled to re-occur until 2038,” Duke said, drily. “The Christchurch earthquake was quite a different matter.”

During the early part of the quarter, all of our seven stores (in the city) were closed and all required re-stocking, some minor repairs, some major repairs and one requiring demolition and re-build.”

“I also sense that the Global Financial Crisis has caused customers to change their behaviour patterns – but NOT to trade down on quality as normally

happens in recessions, but to save or pay down debt. So, an additional task for us as retailers will be to deal with a slow or stalled economy, offer goods and services that reflect changing customer preferences and entice customers to spend rather than save or retire debt. This, I believe, will require an increased media spend and perhaps deeper discounting”.

He added that the five key drivers of financial health in a retail business are: sales, gross margin, stock-turn and management of expenses and, of course, profit. “Our entire focus is on increasing these drivers, no matter what ...”

Briscoe’s second-quarter sales of \$97.8m were 4.83% up on the \$93.3m that quarter of 2010 – off a very strong promotional programme, with the homeware segment up 4.17% and the sporting goods segment by

6.34%. First-half sales of \$194m are up 2.09%. Rod Duke says pressure on gross profit margin has remained strong, reflecting competitive market pressures and tight inventory control. First-half profit is tracking at least at \$10.2m which would be 57% above the tax-adjusted, full-2010 year result of \$6.6m.

## Ecoya exceeds targets

Fragrance products manufacturer and distributor Ecoya Ltd. completed its first financial year to March 2011 with revenues of \$14.3m and a 4m loss, thus exceeding prospectus forecasts of \$8.0m revenue and a loss of \$5.2m.

Ecoya executive chairman Geoff Ross says, “The current year has started very well with solid growth in both Ecoya and Trilogy. Whilst there may be challenges in the retail sector, Ecoya is very positive about sustainable growth opportunities this year.”

The Australian market continues to be strong for the Ecoya brand with annual sales of NZ\$6.5m which is 76% up on 2010. Sales of the Ecoya brand outside the original market of Australia continue to grow and fourth-quarter sales were treble those of 2010’s last quarter. The Trilogy brand, which Ecoya acquired last year, is also doing well. Ecoya expects revenue to exceed \$20m next year and profitability to follow. ■

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