

PLRA Daily REIT Note
August 22nd, 2024



Yesterday's reports reinforced everything in Tuesday's Walmart note. In particular, this beat from **Target** was a point-by-point match for what I quoted from WMT:

While the economic data remains mixed, **we see a consumer that is still willing and able to spend...** comp growth of 2% [was] driven entirely by traffic, [and] every one of our core categories saw traffic growth... comps were strongest in June and July, [and] traffic grew in all three months... we saw **HSD growth in our digital comps, and even faster growth in same-day services**, [which] now account for more than two-thirds of our digital sales...

So this time, let's zero in on fashion...

Discretionary trends have been improving for a full-year now, and **this momentum was most evident in our apparel assortment**, which delivered LSD comp growth... to see that category return to growth helped us from a [margin] mix perspective...

...and follow it through the equally impressive beat/raise from **TJX**...

Marmaxx drove MSD increases in both comp sales and customer transactions, [with] comp strength across all regions... AUR has been pretty consistent, [so] the comp was driven mostly by transactions... as far as the customer, we see **positive results from all the income demographics** we look at...

...and another letdown from **Macy's**:

Net sales were down 4.4% and comps were down 3.6%... **the quarter obviously played out softer than we expected**. It started to get softer in the middle of the quarter...

If you're not following these names closely, just note that WMT and TJX are trading at all-time highs and shooting straighter on the calls, which makes them easier to quote directly. M and TGT have gotten more defensive and spin-heavy, and I'm trying not to bury you in explanations of all their internal jargon and segmentation.

But this market share story that I'm emphasizing is dead simple, especially in discretionary categories. Mass and off-price retailers are winning on **traffic share**, service, selection, attachment, and **head-to-head price competition**. Full-price settings are losing share in all the same ways.

All the macro angles that this twitchy market wants instead — *those* are the stories that are getting more complicated every quarter, because they are just not there in the data. If you want to explain this divergence in retailer results in terms of low-income vs. high-income customers, or a discrete

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“trade down” cohort in between, or jobs, inflation, interest rates, political rhetoric... look, it *could* be happening that way, but the signals have been weak, or they’re not there at all.

If we retreat to a broader point about the consumer getting “cautious,” that’s harder to dispute. But then we’re *not* explaining the divergence in results, or saying anything very investable.

I’ll give you a couple examples of these missing signals. The first is the lack of divergence in M’s growing comp salad:

<p style="text-align: center;">★macy’s</p> <hr/> <table style="width: 100%; border-collapse: collapse;"> <tr> <td style="width: 80%;">Net Sales</td> <td style="text-align: right; border-bottom: 1px solid red;">-4.4%</td> </tr> <tr> <td>Comparable O+L+M Sales</td> <td style="text-align: right; border-bottom: 1px solid red;">-3.6%</td> </tr> <tr> <td>Go-Forward Macy’s Business Comparable O+L+M Sales¹</td> <td style="text-align: right; border-bottom: 1px solid red;">-3.3%</td> </tr> <tr> <td>Go-Forward Macy’s Locations Comparable O+L Sales²</td> <td style="text-align: right; border-bottom: 1px solid red;">-2.3%</td> </tr> <tr> <td>Macy’s First 50 Locations Comparable O+L Sales</td> <td style="text-align: right; border-bottom: 1px solid red;">+1.0%</td> </tr> <tr> <td>Non-First 50 Go-Forward Macy’s Locations Comparable O+L Sales</td> <td style="text-align: right; border-bottom: 1px solid red;">-3.7%</td> </tr> <tr> <td>Non-Go-Forward Macy’s Locations Comparable O+L Sales</td> <td style="text-align: right; border-bottom: 1px solid red;">-6.5%</td> </tr> </table>	Net Sales	-4.4%	Comparable O+L+M Sales	-3.6%	Go-Forward Macy’s Business Comparable O+L+M Sales ¹	-3.3%	Go-Forward Macy’s Locations Comparable O+L Sales ²	-2.3%	Macy’s First 50 Locations Comparable O+L Sales	+1.0%	Non-First 50 Go-Forward Macy’s Locations Comparable O+L Sales	-3.7%	Non-Go-Forward Macy’s Locations Comparable O+L Sales	-6.5%	<p style="text-align: center;">bloomingdales</p> <hr/> <table style="width: 100%; border-collapse: collapse;"> <tr> <td style="width: 80%;">Net Sales</td> <td style="text-align: right; border-bottom: 1px solid black;">-0.2%</td> </tr> <tr> <td>Comparable O+L+M Sales¹</td> <td style="text-align: right; border-bottom: 1px solid black;">-1.4%</td> </tr> </table> <p style="text-align: center;">BLUEMERCURY</p> <hr/> <table style="width: 100%; border-collapse: collapse;"> <tr> <td style="width: 80%;">Net Sales</td> <td style="text-align: right; border-bottom: 1px solid blue;">+1.7%</td> </tr> <tr> <td>Comparable Owned Sales</td> <td style="text-align: right; border-bottom: 1px solid blue;">+2.0%</td> </tr> </table>	Net Sales	-0.2%	Comparable O+L+M Sales ¹	-1.4%	Net Sales	+1.7%	Comparable Owned Sales	+2.0%
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For example, the third-party marketplace (“+M”) was meant to pull the online comps ahead of the stores, like we just saw from WMT. It doesn’t seem to be happening (-3.3% vs. -2.3%). Why not?

Well, in the [April note](#) that I linked on Tuesday, I summarized my own theory of how these online marketplaces interact, and why logistics and scale would matter more than the current customer base. So far that’s been very predictive, and I haven’t heard anything on these calls to challenge it.

Or what about the good old A+ mall shtick, or the “resilient” high income customer? Are those still meant to be predictive, or have they just become faith-based mantras? Because even these top 50 Macy’s (out of ~500) are still comping below TJX and TGT. And Bloomingdale’s is worse...

Q: Wondering if you could talk about performance by income demographic, particularly as the quarter played out and we saw that weakness overall...

A: Yeah, I think there was a pretty consistent reaction across all of our nameplates, in terms of the second quarter being softer than the first. So you have to believe that everybody is being a little more cautious, as they watch what’s going on in the macro environment, and are just being more judicious in the purchases they make...

See what I meant? And what about the 150 underperforming stores they’ve tagged for closure?

So **one of the things we expected on the non-go-forward stores is that they would actually perform worse** — we effectively performed better than what we’d actually planned. So customers are still shopping those stores, [and] when we think about the year-over-year performance, they’re slightly better...

More specifically, these stores underperformed by 500bps last year, and now you can see they've closed almost half of that gap (-3.7% vs. -6.5%). So on the bright side, maybe they'll slow down those closures? In fact, they're speeding them up:

Demand for those properties has been strong. We are pleased with the pace and the quality of dealmaking, and now expect to close ~55 stores this year, vs. prior expectations of ~50...

Which is consistent with the story I've been telling the whole time. The brief Covid pause in department store closures was just that — a brief pause — and the reopening sales boom was never going to make many non-viable anchor locations viable again. We're essentially back to the 2019 setup and closure outlook, or worse. So if anything, they've got some catching up to do.

I'm aware that M's store rankings do not map perfectly to mall letter grades, and again, I won't drag you through the whole Macy's or mall story, which I've reviewed in plenty of other notes this year. In terms of anchor closures at valuable REIT malls, I'm still less a bit less worried about Macy's this year than JWN and others.

But Macy's is only tracking a year or two behind them, and the bottom line is that the entire mall format seems to be returning to its pre-Covid pace of long-term secular decline. Which already matters for in line leasing and tenant credit, even at malls with a few years to go before their next dark anchor.

Now let's zoom in on one particular item and brand:

Q: On the merchandising side, what are you seeing in handbags and shoes to lead that acceleration? I think that's been a tougher category. And a similar question [on] some of the women's brands that you called out...

A: We are seeing green shoots in ready-to-wear. So that's why we're citing those examples... in terms of handbags and shoes, we were pleased to see the disparate or the magnitude of the difference in our F-50 stores in those two categories... in the case of handbags, I think we cited the fact that we're starting to see some light at the end of the tunnel on brands like Lauren by Ralph Lauren and Karl Lagerfeld. And **the Coach business has been particularly good lately...**

Right — it's been a good year for Coach, with a popular new retro line. From their call last week:

The Tabby family delivered another quarter ahead of expectations, over-indexing with new and younger consumers, and nearly doubling versus last year. Quilted Tabby continued to outperform, and we further expanded the family with the Tabby Backpack...

Not such a good year for Kors, which they're still on the hook to acquire. (Unless the FTC bails them out.) But let's stick with what's working:

Further, given the power and halo of Tabby and consistent with our goal of meeting consumers where they are, we broke the distribution paradigm through **a test that brought Tabby 26 to over 100 outlet locations globally, selling at full price**, and the test is exceeding our plan. Importantly, the learnings from this test are informing our broader strategies in fiscal '25 and beyond...

So this ties into another longer-term PLRA theme, about outlet centers "becoming the new mall." But for our purposes here, it's just reinforcing my general traffic-first approach to retail real estate.

In this case, even if every brand wants a “premium environment” for their full-price distribution... there are too many MSAs where those environments no longer have much traffic share, or no longer exist at all. Meanwhile, their online channels and targeted marketing are never quite as effective as they make them sound. So you when you have a hit on your hands, and you want to maximize sales volume while it’s still hot, you still have to go where the traffic is:

Q: It sounds like you're doing a really good job selling full price product at outlets. So how we should think about the opportunity to lean into that, vs. what might be a more choiceful consumer shopping that channel?

A: Again, we're seeing progress in all our channels... [and] we're blurring the line, because the consumer is channel agnostic. They don't see outlet and retail the way we in the industry have historically seen it. When we spend 9% on marketing, a lot of it on upper funnel — particularly focused on [lines] like Tabby — that consumer is walking into our outlet stores... **that might be their best store in that community**; they may be a tourist traveling, and that's the only visit they make for shopping...

[And] of course, we're selling it at full price. So we're excited by this opportunity. We're going to extend it to a number of other brands. In fact, the Brooklyn bag that I mentioned, next month you'll see it in select outlets as well...

Now, in terms of those consumer sentiment narratives, what’s the “missing signal” here?

Well, “trade down” is becoming another fuzzy term in consumer land, but let’s think about the most basic kind of cyclical trade down effect that the market’s looking for, and how it would show up at the format or trip level. Say you’ve got your mall customers buying \$400 handbags, and your outlet customers spending \$150. In a consumer downturn, a discrete cohort from the mall group reduces their budget, and goes to outlets or TJs instead. When consumers are flush again, there will be an overlapping cohort that increases their budget, and trades back “up” to the mall.

In my view, much of that story has been scrambled beyond repair by the rise of e-commerce. On the brick & mortar side, it’s better to start with this overwhelming secular trend of “value” environments taking traffic share, and try to explain that first.

In my account of it, the full-price environments have just been losing their appeal, and there are a lot more customers cross-shopping across all these formats already. As the malls decline, or the surviving “A” malls become more overpriced and boring and entertainment-heavy, they have gradually shifted more of their shopping away from malls.

In other words, it’s not budget driven, it’s experience driven. And part of what people want in a shopping experience is variety and comparison, which in turn pressures price. But that’s not really a trade-down, because it’s happening even when customers are not tightening their budgets.

So when you’re comparing these two narratives, and you see the same product working at the same price across multiple settings, and rolling out from A locations to more Bs *within* each setting... that’s a point in my favor. It’s a point against the idea that consumer investors *or* real estate investors can still “insulate” themselves by focusing on higher end demographics, and leaning back into the worn-out “premiumization” playbook.

And it’s not a great long-term sign for discretionary retail formats, because it means that we’re offering less customer segmentation to a fashion tenant.

Let's switch over to TJX, and take that from one more angle:

Q: Can you talk about AUR in the quarter, the balance between mix shifts and like-for-like price increases? And any changes you might be seeing in customer behavior around value?

A: We have been bottom-up, still adjusting retails where appropriate. **If you look at our merchandise margin, though, the story is becoming more and more about buying better,** and not just the retails...

I'm sure you've been seeing all the talk [about] what could happen in the market if retails come down on certain categories. [But] our merchants are excellent at this, [and] we're always retailing the goods based on the out-the-door retails that we see at the competition. So we feel as though we will have that covered...

Q: [But] some perspective on the market-share gains? Marmaxx comps obviously compare very nicely to what we've seen out of the department store channels, and others thus far. At the same time, we are seeing some of the mass retailers report better results in general merchandise, including some more positive commentary on apparel. So could you speak to how you're protecting your flank?

A: We've been looking at the same numbers... [and] in the US, as you just stated, there's a lot of good information out there. So the first thing we do is we look at the Marmaxx total, with new stores, and you can see clearly that we're gaining market share in total. Now as to where it is, **we have some information in apparel and home that would say we're picking up market share in both.** [But] it depends how you slice out some of the discounters... for example, we have a pet business in our home area. We have a lot of consumables, like the gourmet food that we carry, that's in our home business.

CFO: Greeting cards, wrapping paper.

Yeah, where is that in those businesses? [But] we look for any sign of [rising] competition... are their comp sales any healthier than ours? Right now, we haven't seen it. And whoever is doing better business, we shop them very aggressively to look at our values in the fashion categories they carry...

So again, the (understandable) anxiety in both of those questions comes from this idea that we're seeing an across-the-board pullback in consumer *budgets*, or a growing pullback that's creeping up the income spectrum. In which case you might see margin pressure offsetting some of this off-price traffic growth, or more of that traffic going to Walmart.

But if you take my view that it's more about the full-price channels being *overpriced*, then you'd see exactly this ongoing off-price flywheel that TJX is describing. Because even with leaner inventories on the full-price side, more consumers are passing on those prices at the mall (or online, or not even noticing them) and there's just as much overstock for Marmaxx:

Q: [So] what surprised you the most in the first half?

A: We know there's always going to be a lot of availability of goods, [but] **it's off the charts**, even a little bit more than we would have thought. So that affects how much we leave open for more of the closeout hand-to-mouth buying in the back half. And as you can imagine, [we're] leaving more liquidity, because clearly there's no lack of availability...

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