HBC faces investor skepticism despite cost cuts

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Retailer faces fresh headwinds as it prepares to release fourth-quarter results

Hudson's Bay Co. is trying to shrink itself to success.

The Toronto-based retailer is closing stores and divisions or parts of them, betting on its stronger chains, especially its luxury Saks Fifth Avenue. It's working on improving the basics, particularly at its weakest banners: discounter Saks Off 5th and the U.S. chain Lord & Taylor.

But as HBC prepares to release its fourth-quarter results, which included the crucial holidayshopping period, it faces a slowing economy and a sluggish retail market that has already contributed to a disappointing performance at some other Canadian retailers.

Helena Foulkes, who arrived as chief executive at HBC just more than a year ago, is looking to instill confidence in anxious investors that she can right the ship after years of declines. The stock price, which closed at $7.39 on Friday, has tumbled 74 per cent since peaking in mid-2015 after HBC's return to the public market in late 2012.

"Helena has been doing the right financial moves so far, but her real leadership and success will depend on getting the HBC retail engine back to work," said Hugh Latif of consultancy Hugh Latif & Associates.

Those financial manoeuvres include selling the Lord & Taylor flagship store in Manhattan to office-sharing startup WeWork and spinning its ownership of Germany's Galeria Kaufhof into a joint venture. The deals generated about $1.7-billion, helping the retailer reduce its debt and gain much-needed breathing room.

Ms. Foulkes has taken other decisive actions. Last year, HBC decided to close up to 10 Lord & Taylor stores and sold its flash-sale website, Gilt.

Now, it is shutting all 37 of its Home Outfitters stores in Canada as well as up to 20 of its Saks Off 5th outlets in the United States. And the company is looking for a new leader for its namesake Hudson's Bay chain in Canada after Alison Coville, a long-time employee who had been at the helm less than two years, left on March 1. Ms. Foulkes has replaced other top executives.

The CEO is focusing on boosting customer service and improving store and e-commerce operations at Hudson's Bay, Saks Off 5th and Lord & Taylor. "I talk a lot about fixing the fundamentals," she said in a mid-December interview.

Industry observers acknowledge Ms. Foulkes is making progress, but remain cautious.

"New leadership and culture have certainly driven impressive operating improvements and significant debt reduction," said Chris Li, retail analyst at Macquarie Capital Markets, which has an "underperform" rating on the stock. "But market conditions remain challenging with limited earnings visibility."

After divesting half of Kaufhof, HBC's third-quarter loss from continuing operations increased to $124-million or 52 cents a share from a loss of $116-million or 64 cents a share a year earlier. Sales rose 5.6 per cent to $2.19-billion.

Analysts on average expect HBC to post earnings a share in the fiscal fourth quarter, which started Nov. 4, of 25 cents, compared with 9 cents a year earlier and revenue of $3.2-billion compared with $4.7-billlion, according to Refinitiv.

Kathleen Wong, retail analyst at Veritas Investment Research, said HBC improved its North American same-store sales in the third quarter but still lagged department-store peers such as Nordstrom Inc., Neiman Marcus and Macy's Inc.

Many investors have stuck with HBC because of the potential value of its real estate, including the prized building in New York that houses the flagship Saks store on Fifth Avenue. But Ms. Wong, who recommends selling HBC shares, said the value of its commercial properties is tied to the retailers it leases to and its most important tenant is its own stores. "The Catch-22: If HBC raises rents to its retail operations, it reduces the value of those operations, but if its retail operations pay below market rents, then its real estate value is likely to lag," Ms. Wong said in a January report. "There is no easy solution to this dilemma."

The only way to realize the full value of HBC's real estate is to close the stores and find a buyer for the real estate, she says.

Activist Jonathan Litt, whose Stamford, Conn., company is believed to have owned about 3 per cent of HBC last fall, has called for a broader selloff of the retailer's properties, including the Saks flagship, and much of its other businesses. Mr. Litt couldn't be reached for comment last week.

Since his renewed call for more changes last November, retail sales in Canada have been soft and retailers such as home-improvement specialist Lowe's Canada and mattress specialist Sleep Country Canada Holdings Inc., have posted weak sales. Other retailers are closing, including Payless ShoeSource Canada Inc., while Sears Canada Inc. shut its last stores more than a year ago, providing opportunities for Hudson's Bay to win new customers.

Ms. Foulkes said she is moving quickly to fill the void. In the shoe department at some Hudson's Bay and Lord & Taylor stores, for example, she is testing putting the boxes of footwear out on the floor and letting shoppers serve themselves, which is a common practice at discounters.

Wayne Drummond, chief merchant at Hudson's Bay, said last month the pilot has been a success in men's and "not as clear" in women's, where there are more styles and sizes. "It's still a work in progress."