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HEARD ON THE STREET

The Mall Meltdown Continues

Mall-based retailers reported dismal earnings last week, reminding investors of the sector's fundamental problems

Gap shares fell 9% on Friday after the retailer warned it may have to rely on promotional activity in coming months. **PHOTO:** JIM YOUNG/BLOOMBERG NEWS

By Elizabeth Winkler

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Retailers' earnings season has gone from bad to worse. The bleeding intensified last week, with shares of Abercrombie & Fitch plummeting 26% on Wednesday, the biggest percentage decline since the company went public. PVH Corp., owner of brands including Van Heusen, Tommy Hilfilger, and Calvin Klein, dropped 10% that day, too. On Thursday, women's wear chain J.Jill was down a jaw-dropping 53% and on Friday, Gap Inc. slid 9%.

It is hard to miss what all of these retailers have in common: They are mall-based.

While retailers posted generally strong numbers in 2018, raising hopes of a retail renaissance, this year has seen a reversion to the pre-2018 trend: department stores and mall-based retailers giving up share to discount stores and e-commerce. The perceived renaissance now seems to have been largely a function of lean inventories, not an actual increase in demand. Now inventory is high again, and retailers are resorting to promotions.

Gap, for example, warned Friday that it may have to rely on promotional activity in coming months to move unsold merchandise off shelves. That will weigh on gross margins. The company, which posted its weakest quarterly sales in three years, has suffered not merely at its namesake brand, where comparable-store sales were down 10% for the quarter, but also at Old Navy, typically its best performer. Comparable-store sales there fell 1%. By comparison, in the same period last year they climbed 3%.

Gap Chief Executive Art Peck partially blamed the company's poor performance on weather, calling the three-month period ended May 4 "one of the coldest, wettest quarters in memory." Of course, weather is rarely a satisfying explanation, especially when a Gap rival like Zara is succeeding with a leaner supply chain and rapid merchandise turnover.

Many of these retailers are scrambling to restructure. In February, Gap announced plans to spin off its more successful Old Navy brand into its own public company. That sent shares up 20%, though the deal won't be completed until 2020. This past week, Abercrombie & Fitch said it plans to shut several flagship stores world-wide.

Investors should expect more announcements of this sort and much more restructuring. Whether such plans will actually succeed remains to be seen. An independent Old Navy seemed like a good idea—until last week's report included a sales decline. At some point, investors will have to contend with the fact that for some retailers, restructuring can only fix so much.

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