

## **Sales slide sounds warning bells for J.C. Penney**

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Six months after J.C. Penney Co. launched a bold new pricing plan, customers still aren't buying it.

The midprice department store chain reported a bigger-than-expected loss and plummeting sales during the second quarter, as its customers remain confused by the new pricing strategy that ditched hundreds of sales in favor of everyday lower prices. The bleak performance marks the second straight quarter of steep sales declines since the plan was introduced Feb. 1.

The company also withdrew its profit guidance for the year. Its shares tumbled more than 8 percent in premarket trading.

Penney's poor results, released Friday, underscore how difficult it is for a company to change the way shoppers behave. In a still-struggling economy, shoppers are still looking for racks of "70 percent off" sales signs and coupons. The latest financial performance also tests the patience of investors and adds more pressure on its new CEO, former Apple Inc. executive Ron Johnson, to turn things around at the retailer.

Under Johnson, Penney is transforming everything from the items it stocks to store design. But the riskiest move has been its pricing, which is turning out to be an even tougher sale to shoppers than previously expected. The latest results cast more doubt it will work at all.

"This is worse on top of whatever I thought was going to be a bad story," said Brian Sozzi, chief equities analyst for research firm NBG Productions. "I am losing faith" in the pricing switch.

Johnson, however, promised to stay the course.

"We have now completed the first six months of our transformation, and while business continues to be softer than anticipated, we are confident the transformation is on track," said Johnson in a statement. "The transition from a highly promotional business model to one based on everyday value will take time and we will stay the course."

In May, Penney's stock plunged 20 percent, its biggest one-day decline in four decades, after the retailer posted a larger-than expected first-quarter loss and a 20.1 percent drop in revenue because of the poor reception from shoppers.

Things got even worse in the second quarter as Penney scrambled to backpedal and shift its marketing strategy to get shoppers back in the store.

The department store, based in Plano, Texas, said Friday that it lost \$147 million, or

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67 cents per share, in the quarter ended July 28. That compares with net income of \$14 million, or 7 cents per share, a year ago.

Revenue tumbled almost 23 percent to \$3.02 billion. Revenue at stores open at least a year fell 21.7 percent, worse than the 18.9 percent drop the quarter before.

Excluding one-time items, Penney's loss was 37 cents per share. Analysts had expected a 26-cent loss on revenue of \$3.2 billion.

The company said that its gross profit margins fell to 33.2 percent in the quarter, down from 38.3 percent a year ago.

Johnson described the balance sheet as "rock solid." The company said it ended the quarter with about \$888 million in cash and cash equivalents.

Its shares tumbled \$1.87, or 8.5 percent, to \$20.23 in premarket trading. The stock is down more than 50 percent since investors, initially enthusiastic, bid them up to about \$43 after Johnson announced the pricing plan in January.

Penney on Feb. 1 began using three-tier pricing with consistently lower daily prices that were 40 percent below last year, deeper monthlong sales on specific items and periodic discounts that are even more generous throughout the year. But Aug. 1, Penney eliminated the monthly sales events and increased the frequency of the periodic sales to every Friday. These had been called "Best Price" sales but are now being called "clearance."

Penney is keeping "Every Day" low prices, which has accounted for about 70 percent of sales since the company began the new strategy.

Johnson had said the new approach should make pricing easier for customers to understand.

"We thought, 'Why are we trying to teach customers new language to shop?'" Johnson said in a recent interview with The Associated Press. "We're just trying to be straightforward."

Penney is tweaking its advertising to better explain the change. That includes inserts in newspapers every Friday during the back-to-school season highlighting specific products like jeans. TV ads tout free children's haircuts at stores to draw shoppers.

The new ads are in stark contrast to the spots that introduced the new pricing plan. The "fair and square" brand campaign featured commercials with dogs, kids and bright colors — but little explanation of prices.

Some analysts hope Penney will attract more shoppers once it makes the stores more inviting. Starting this fall, almost half its merchandise will be new. It plans to some brands and redesigning others. Among the new brands shoppers will see are Vivienne Tam and Betsey Johnson, who will be selling affordable versions to Penney.

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Penney just launched shops for Levi's and its own jeans brand Arizona. It plans 100 shops within each of its stores by 2015 that will either focus on one brand or a variety of labels. The company also plans to add areas in its stores called Town Squares to offer services and advice.

Even that plan has had its hiccups. Last month, Macy's won a preliminary court ruling against Martha Stewart Living that would prevent it from selling some of its products like cookware and kitchen utensils at J.C. Penney. Penney has been counting on the popularity of the Martha Stewart brand to revitalize its business.

Penney said Friday that it no longer expects to meet its earnings guidance for 2012. It had expected a profit of \$2.16 per share. Analysts expected the company to earn \$1.26 per share for the year.

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