
Economic Impact of the Attack on the Retail Sector

This report is based on research and analysis conducted by Booz-Allen & Hamilton.

SUMMARY

The retail industry of New York City's five boroughs produces \$50 billion a year in revenue for the city's economy, and employs more than 280,000 workers, generating \$7 billion in annual wages. In Lower Manhattan alone, the retail sector's yearly sales exceed \$1.2 billion. The retail industry adds glamour to the city.

Retail, however, is highly sensitive to local business cycles. Thus, it is no surprise that retailing has been one of the sectors hardest hit by the events of September 11th. Although the growth of New York City's retail industry had already been slowing before September 11th, the attack devastated many of Lower Manhattan's retailers and significantly exacerbated the sector's slowdown throughout the city.

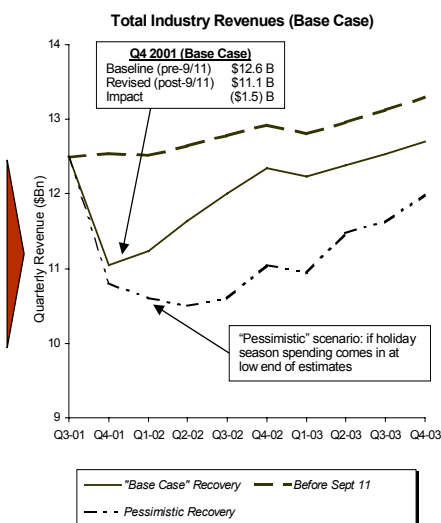
- ❖ All retail employees working in the Twin Towers apparently survived the attack, but the destruction of the World Trade Center Mall obliterated approximately eighty stores⁴ and damaged many nearby retail locations. All together, approximately \$700 million in inventory and fixtures was destroyed.
- ❖ In the wake of the attack, many retailers closed, at least temporarily. Those located in or near the disaster zone lacked access and telecommunications and wanted to avoid the risk of further incidents. Voluntary and involuntary closures are estimated to have cost New York retailers approximately \$300 million in lost revenues.
- ❖ The events of September 11th caused consumer confidence and store traffic to plummet, affecting New York City more than the rest of the country. While seasonally adjusted retail sales in September declined by 2.2% nationally, sales plunged 14% from expected levels in New York City.
- ❖ Lower Manhattan retailers suffered the most significant impact. Many have already gone out of business. Other retailers closed their stores for significant periods, and some that are now open are experiencing sales declines of more than 50%.

⁴ Excluding eating and drinking establishments

- ❖ Both store traffic and purchase patterns have shifted. Consumers are shopping closer to home, often in less upscale stores. Consumers are also spending less and, by some accounts, are buying smaller-ticket items. Fear stemming from concerns about personal safety is now causing many nonresidents to avoid shopping in the city entirely.
- ❖ Department stores, as well as those that sell specialty apparel, footwear, accessories and luxury-goods in Midtown Manhattan saw sales plummet 30% to 40% in September. In some luxury-goods stores sales plunged more than 50%. This is due in part to their reliance on tourists and visitors from beyond the five boroughs.
- ❖ Discount retailers and sellers of necessities, such as food and over-the-counter drugs, fared better than most. Retailers of discretionary goods (specialty apparel, footwear, accessories, luxury goods, and consumer electronics) and durables (such as appliances and furniture, all of which are purchases that can be postponed) saw the steepest declines in sales.
- ❖ With the approach of the holiday shopping season, a period that traditionally provides retailers on average 30% of annual revenue, many businesses have introduced aggressive promotions to move merchandise, and have slashed inventories in anticipation of weaker consumer demand.

Impact Estimation by Segment for 4Q 2001

Segment	Assumptions	Impact ⁽¹⁾	% Sales Decline
FOOD & DRUG "Necessities"	▶ Food minimally impacted, drug might be affected by shift to value purchases	\$110-160 M	< 3%
DURABLES	▶ Consumers delaying major discretionary purchases	\$400-450 M	8-9%
SPECIALTY	▶ High-end specialty affected by shift toward value items	\$280-340 M	10-12%
IMPULSE "Small Ticket"	▶ Effect of tourist/day tripper traffic declines mitigated by shift to lower ticket	\$20-50 M	3-5%
DEPARTMENT STORES	▶ High-end Manhattan locations hardest hit - significant traffic decline	\$100-150 M	15-18%
CONSUMER ELECTRONICS	▶ Partly supported by new product cycles (e.g., X-Box)	\$30-60 M	7-8%
MASS MERCHANDISE	▶ Flat to positive trend due to customers' "value" mindset	\$10-30 M	< 3%
Direct Sales Impact (Ground Zero)		\$250-300 M	
TOTAL EST. IMPACT		\$1.3 - \$1.7 B	



Source: US Dept. of Commerce, Claritas, Inc., BA&H analysis.

Note: (1) Impact relative to industry projections prior to September 11th.

Industry leaders and analysts remain uncertain about the scale and timing of a recovery. If, as most expect, current trends continue, fourth quarter revenues in New York City could drop approximately 10% to 15%, or \$1.5 billion below expectations prior to September 11th. A drop in revenues of this magnitude could lead retailers to employ up to 23,000 fewer workers than normal during the holiday season, which typically involves an increase in hiring.

To help retailers in Lower Manhattan, the hardest hit segment of retail, several actions can be taken soon to accelerate recovery in the area. Small business must be specifically supported through access to loans and grants. In addition, the plan to revive and rebuild Lower Manhattan should explicitly address the need for a strong retail presence with an appropriate mix of stores.

More broadly, other actions should be aimed at speeding the recovery of New York City's entire retail economy, particularly in Manhattan. Overall efforts should address consumers' financial and safety concerns. A sales tax holiday would help spur spending by both resident and nonresident shoppers. Integrated programs, designed in coordination with the tourism and travel sectors, could promote New York City as a shopping destination. These programs can be successful in bringing back the tourist shoppers, who are so critical to Midtown and Lower Manhattan retailers. Additional programs, designed to attract residents and commuters, could involve cooperation between employers and retailers to encourage workers to shop for the holidays. Given consumers' safety concerns, security must be bolstered by relying on measures initiated by both public and private sectors.

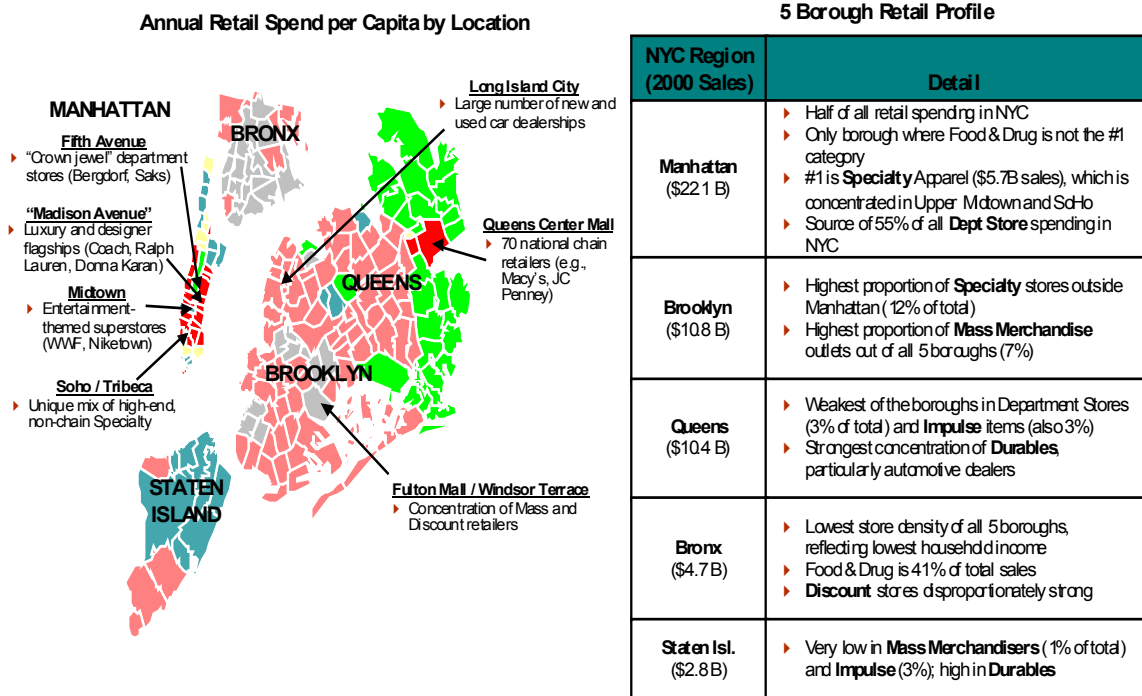
A SNAPSHOT OF NEW YORK CITY'S RETAIL SECTOR

The retail industry in New York City employs more than 280,000 workers, generating \$7 billion in annual wages. The retail industry in the city generates revenues that exceed \$50 billion a year. In Lower Manhattan alone, the retail sector's yearly sales exceed \$1.2 billion. New York City's retail sector relies on a relatively large and lower skilled workforce; on average, these employees earn \$25,500 a year. Operating margins are only 8% to 10% in most retail sectors. The added value produced by the sector yields a total GCP contribution of approximately \$11 billion.⁵

Retail, like the media and entertainment sector, helps to give the city its allure and sophistication. The glamorous image retailing projects is most closely tied to Manhattan, which accounts for 50% of sales across the five boroughs, even though only 20% of New Yorkers live in Manhattan. Offering the most concentrated shopping experience in the country, Manhattan is the only place in the U.S. where specialty and apparel is the number one retail sales generator in virtually every zip code.

⁵ Excluding wholesale trade, eating and drinking establishments, and counties outside the five boroughs

Midtown Manhattan Has the Highest Concentration of Retail Sales Driven by Specialty Apparel and Department Stores



Source: U.S. Department of Commerce, U.S. Census Bureau, Claritas Inc., BA&H analysis.

Specialty retailers look to New York City to refine their image. Donna Karan, Ralph Lauren and Calvin Klein built their flagship stores on Madison Avenue, while national chains such as Saks Fifth Avenue, Bloomingdale’s and Macy’s have their premier stores in other key Manhattan locations. Pockets of brilliance dot the landscape in subsectors such as home design, consumer electronics and specialty apparel. High-end design centers such as ABC Carpet & Home and designer food emporia such as Dean & DeLuca and Fairway all call Manhattan home. In addition, there are the homegrown mini-chains — J&R Music World, Models’, Century 21, Nobody Beats the Wiz, and H&H Bagels. Accessories are more than an afterthought. Tiffany’s and Coach, for example, garner some of their highest sales per square foot in their Midtown flagship stores.

Subsectors

Food and drug is the top retail category in New York City, and durables (including home furnishings, appliances, and automobiles) are second. Together, these categories account for 57% of total spending. Specialty (which includes apparel, footwear, accessories, and luxury goods) is third, claiming 16% of retail dollars.⁶ Department stores account for an additional 6% of total retail spending.

Consumers

In total, the retail sector is supported each year by the more than eight million residents of New York City and more than 50 million commuters, day-trippers (visitors from beyond the five boroughs) and tourists. In Manhattan, approximately one-third of retail sales are attributed to non-New York City residents. Day-trippers spend \$3.3 billion per year in Manhattan, while tourists spend \$2.2 billion. Lower Manhattan attracts 7.2 million visitors yearly and is home to a small, but affluent population, of more than 20,000 residents, many of whom are financial services employees.

Recent Trends

Over the last ten years, retail in New York City enjoyed significant growth along with the expansion of the economy and the growth of local tourism. From 1990 to 2000, average growth in retail segments was about 6% to 7%. Nevertheless, in the last eighteen months, there were signs the rate of growth was slowing. On average, retail growth was expected to soften in 2001 to 3.1%. Analysts and retailers worried aloud about the coming holiday season. "I see no evidence the overall economic environment will improve," said Michael Jeffries, chief executive officer of Abercrombie & Fitch, on September 4.

THE IMPACT OF THE SEPTEMBER 11TH ATTACK

Direct Effects

All retail employees apparently escaped from the Twin Towers when it was attacked, but the destruction of the World Trade Center Mall obliterated approximately eighty stores⁶ and approximately \$700 million in inventory and fixtures. Nearby stores also sustained damage. As a precautionary measure, many businesses in and around the New York City area closed for at least a day. Mandatory roadblocks needed to speed rescue and

⁶ Although specialty is #1 in Manhattan, including the other boroughs brings it down to #3 for NYC

firefighting efforts further hampered retail activity in the vicinity of the disaster zone. As a result of telecommunications failures, merchants throughout Lower Manhattan were unable to process charge card purchases for weeks after the attack. Voluntary and involuntary closures are estimated to have cost retailers about \$300 million in lost revenues.

Insurance can be expected to cover half the losses in most categories, depending on the type of coverage and provisions for “business interruption.” Many small businesses had little or no coverage. Some observers expect premiums to rise 15 % to 25 % as a result of September 11th.

Broader Sales Impact

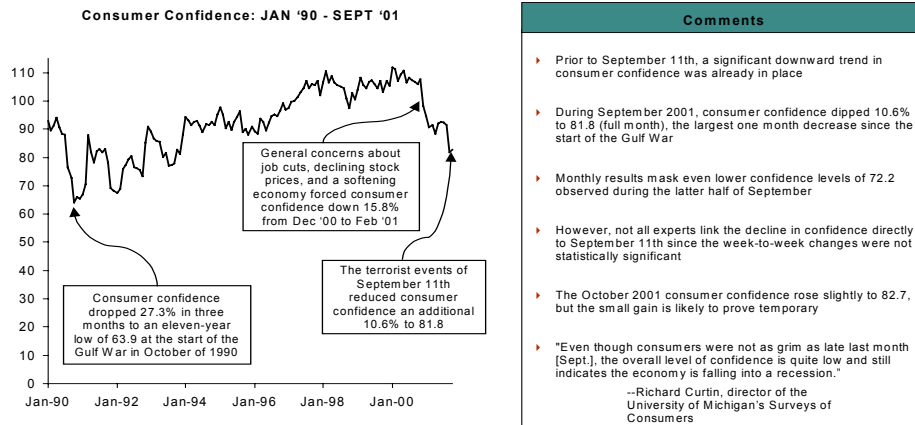
Although the United States as a whole saw seasonally adjusted retail sales fall 2.2% in September, New York City retail sales plunged about 14% below expectations prior to September 11th. Hardest hit were the most discretionary categories — luxury goods, specialty apparel, footwear, accessories, department stores, and consumer electronics. The total shortfall in September sales, versus expectations, was about \$690 million, with \$210 million of that in the specialty and department store categories.

The attack caused many nonresident shoppers to stay home. Tourist travel to New York declined 60% from normal levels in the weeks following September 11th. Meanwhile, resident and day-tripper shopping visits were hampered by public transportation problems. Access restrictions, such as the ban on single-occupant vehicles entering Manhattan below 68th Street, particularly hurt Manhattan retailers. One month after September 11th, domestic airline travel to New York City decreased 20% from normal levels and international travel decreased by 30%.

Fears about personal safety further deterred shoppers. In a recent survey conducted by Harris Interactive for this report⁷, 40% of tri-state respondents said they would decrease trips to New York City out of concern about future attacks. This apprehension has undermined consumer confidence in a population already experiencing economic uncertainty. Prior to September 11th, jobless claims and layoff announcements were up; consumer debt had climbed almost 6% since 1998, and personal bankruptcies were up 17% in 2000 in New York. Adding to the city’s malaise in September, consumer confidence nationwide dropped 10.6%, the largest one-month decline since the Gulf War.

⁷ Quantitative survey designed by Booz Allen Hamilton and conducted online by Harris Interactive from October 12 to 18, 2001. The survey targeted four distinct geographic segments: New York City residents (N=682), Tri-State residents of counties with substantial numbers of New York City commuters (N=682), other “U.S. Domestic” (N=2,542), and an international segment (N=5,683). Samples were drawn from a database of seven million potential respondents ages 18 and older and were weighted for gender, race, age, and income of the relevant population.

**As a Direct Result of the September 11th
Consumer Confidence Plummeted to a Degree Not Seen Since the Gulf War**



Source: Data from University of Michigan *Surveys of Consumers*, "Consumer confidence" and BA&H analysis.

Some New York City retail sectors held up better than others. Anything deemed indulgent fell off the retail map. A shift to value purchases was observed in many segments. Red meat sales were reportedly down. Chicken sales were up. Fancy dresses were out. Off-price apparel was in. Cottons and flannels were in, displacing luxury silk items. In addition to changing what they bought, consumers also changed the types of stores they shopped in. Nearly 35% of respondents to a Deloitte Research consumer survey said they had spent less at "upscale specialty" stores since September 11th. On the other hand, food and drug, discount and mass-merchant retail businesses were more resilient, rebounding almost immediately after the attack.

Retailers' Response

Many retailers reacted quickly and cut inventories, scaled down orders and tried to move products through price promotions. Bergdorf Goodman even cancelled all remaining fall orders. Some retailers expressed intentions to pare back on seasonal hiring. Many in the industry anticipate a period of extraordinary discounting. Automobile manufacturers have already spurred sales through "0% financing" techniques. High-profile stores have offered deep discounts, some for the first time. Markdowns are ubiquitous in all five boroughs. Deep discounts will help retailers to mitigate the negative impact on their revenues, but will certainly reduce their margins.

THE OUTLOOK FOR RETAIL AFTER SEPTEMBER 11TH

Although sales rebounded somewhat in October, views of industry analysts and experts diverge widely on whether or not the trajectory will be maintained. Many retailers describe the day-to-day volatility in revenues as unprecedented.

A bottom up, sector-by-sector analysis of New York City retail suggests that sector revenues could drop on average 10% to 15% below preexisting trends. This is in line with retailers' expectations.⁸ Uncertainties, however, abound. To what extent will fears of public places abate? Will there be additional attacks? Will tourists and day-trippers return? How effective will retailer promotions be? Which retail segments and areas of the city will be the hardest hit in the long term?

In addition, the following challenges have serious implications for retailers:

Transportation and other access problems will persist

Beyond the fourth quarter, transportation hassles and shifts in retail traffic patterns have the potential to undermine the vibrancy of Lower Manhattan in particular. Although Lower Manhattan retail outlets represent only 5% of Manhattan's total sales, they are a potpourri of cultural and shopping venues that help define Lower Manhattan neighborhoods.

Visitor traffic may not rebound quickly

Department stores receive half their revenues from tourists and day-trippers, while specialty apparel, footwear, accessories, luxury goods and consumer electronics stores derive 30% to 40% of their revenues from nonresidents. These discretionary segments face considerable risk if visitor traffic does not rebound quickly — a risk compounded by a normal decline in both sales and tourism in the first quarter.

Small Businesses are struggling

Small businesses face significant financial problems, as cash flows fall below fixed costs, and those businesses fail to make critical payments on leases, loans and utility bills. According to the Alliance for Downtown New York, Lower Manhattan retailers are experiencing revenue declines of at least 20% — and in some cases far more. With declines such as these, many small businesses will fall far short of break-even. The large-

⁸ Retail impact analysis conducted by Booz Allen Hamilton for this report. Pre-attack baseline for each of eight retail subsectors based on analyst, retailer, and industry expert projections; impact analyzed using estimated changes in overall consumer confidence and in store traffic for various recovery scenarios.

scale failure of small businesses could endanger the unique character of New York retailing, which has a large number of independent establishments.

Consumers are worried about safety

Eliminating security risks should be a priority for retailers, if only because they concern staff and consumers. Retailers should take immediate measures to ensure that their stores are safe.

Retailer costs are likely to rise

Losses from the attack will certainly increase insurance premiums. In addition, increased consumer concerns about security will force retailers to provide higher levels of protection for their shoppers. Presently, it is unclear how expensive these measures are going to be, but any measures, however, will affect retailers' costs.

Price wars and other disruptive market aggression may surface

In the longer term, declining store sales could lead to retail price wars and aggressive long-term promotions. A loss of pricing discipline in department stores, for example, could make it even more difficult for small stores to survive, and could have a detrimental impact on industry margins in the long term.

Fourth Quarter Outlook

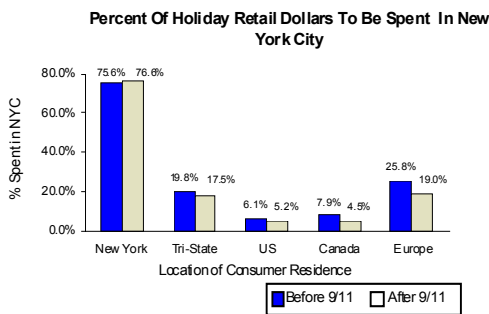
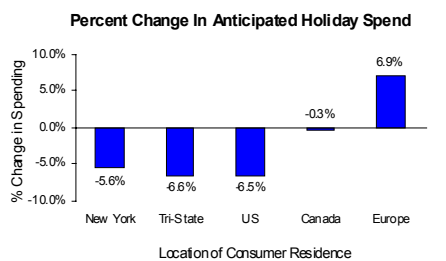
Industry leaders and analysts remain uncertain about the scale and timing of a recovery. If, as most expect, current trends continue, retail revenues in New York City could drop about \$1.5 billion or 10% to 15% below pre-September 11th baseline expectations of \$12.6 billion in the fourth quarter. A drop in revenues of this size could lead to a loss of approximately 23,000 jobs versus normal hiring levels, which typically spike in the fourth quarter.

Certain segments within the overall retail sector are expected to weather these challenges better than others. The grocery and drug segments will probably perform well across all five boroughs, given consumers' intentions to reduce travel and eat at home more often. For example, in a recent survey, more than 20% of New Yorkers polled after September 11th stated that they intend to spend less than last year on dining out. Many mass merchandisers and discount stores outside Manhattan will benefit from the trend to buy less expensive, more value-oriented products.

Retailers of larger ticket durables could see steep revenue declines of 8% to 9% since lower consumer confidence levels appear to be translating into lower spending. As a result of the September 11th attack, 40 percent of consumers surveyed for this study said that they are less likely to make a major purchase. Retailers and manufacturers are offering incentives to draw back consumers. However, it is unclear whether such actions will do more than simply shift early 2002 sales revenues into the fourth quarter of this year.

Department stores and specialty stores will probably sustain a disproportionately large share of the impact, in large part as a result of decreased tourist traffic. Department and specialty stores are more reliant than other sectors on nonresident customers, and a large number of domestic and foreign residents surveyed say they will probably not or definitely not visit New York City in the next 12 months because of the attacks. The sales impact for each of these segments could reach 1% to 12% for specialty stores and 1% to 18% for departments stores during the fourth quarter. Within this segment, high-end Manhattan locations will be the hardest hit.

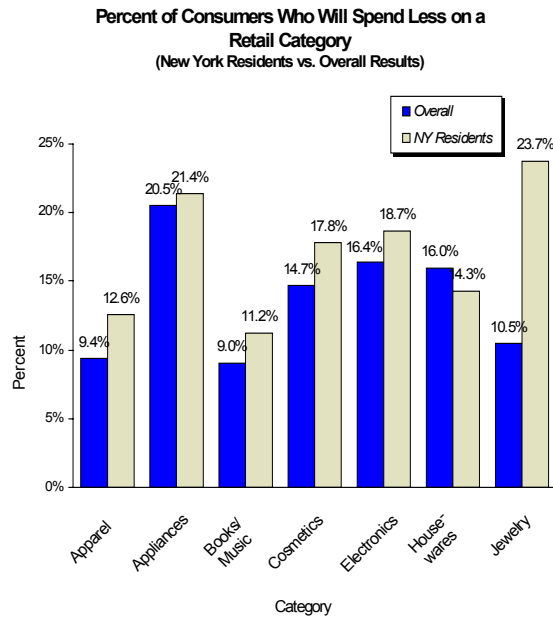
Overall, Consumers Will Spend Less...



Comments
<ul style="list-style-type: none"> Most consumers, with the exception of Europeans, plan to spend less this holiday season
<ul style="list-style-type: none"> Residents of the Tri-State area and U.S. consumers plan to scale back holiday spending by a greater percentage than New Yorkers <ul style="list-style-type: none"> Approximately a 6.5% decrease for Tri-State and other U.S. residents New York consumers only plan to decrease their holiday spend by 5.6%
<ul style="list-style-type: none"> New Yorkers were the only group which intends to spend more of their retail dollars within the City during the upcoming Holiday season <ul style="list-style-type: none"> New Yorkers stated they typically spend 76% percent of their holiday dollars within the City Since the attacks, that percentage has risen slightly to 77%
<ul style="list-style-type: none"> Residents of the Tri-State area, the other U.S. locations, Canada, and Europe all indicated that less of their holiday retail spend would take place in New York City <ul style="list-style-type: none"> European residents indicated the largest reduction in spending at 6.8% The Tri-State area decline of 2.3% is greater than the reduction for other U.S. residents (0.9%)

Source: Harris Interactive Survey; BA&H analysis.

...and shift purchases away from big-ticket to smaller ticket items



Source: Harris Interactive survey and BA&H analysis.

Comments
<ul style="list-style-type: none"> ▶ A large percentage of consumers surveyed indicate that they will spend less on several retail categories <ul style="list-style-type: none"> – Spending scaled back on appliances, jewelry and electronics – Smaller ticket items, like books, apparel, and housewares are less affected ▶ In general, people in New York plan to spend less relative to the overall population <ul style="list-style-type: none"> – 21.4% of NY residents (vs. 20.5% for the overall population) said that they will spend less on appliances – 23.7% of New Yorkers (10.5% overall) plan to spend less on jewelry ▶ There are some bright spots: <ul style="list-style-type: none"> – Overall, 7% of consumers plan to spend more on apparel – Almost 8% indicate that they will spend more on Books & Music – Over 70% of consumers plan to spend the same on each category

RECOMMENDATIONS FOR SPEEDING RETAIL’S RECOVERY

Actions can be taken in the short term to accelerate New York City’s full and timely recovery. Many of these actions would naturally focus on Manhattan, the hardest-hit retail market in the nation.

Give Manhattan a sales tax holiday

Temporary retail tax abatement is a powerful and proven method for spurring sales. New York area consumers have shown great willingness to respond to promotions; past tax abatements, even with caps, have increased sales by 7% to 10% on average. A tax abatement would draw both day-trippers and residents. Decisions about the timing, length and geographic scope of the abatement need to be made quickly. For instance, should such an abatement apply only in Manhattan or in all five boroughs?

Promote New York City as a shopping destination

Bringing back the tourist shopper — so critical to Midtown and Lower Manhattan retailers — should also be a top priority. Advertising and PR campaigns with potential participation of celebrities that say New York City is open for business would be helpful. But other cities, like Hong Kong, that have had to weather the reaction to a catastrophe have found that getting tourists to visit again requires hotel/airline packages with incentives compelling enough to overcome security fears.

Work with employers to get workers out shopping for the holidays

Local employers can take initiatives to show employees their commitment to the city and to help retail recovery in Manhattan, including “time off” programs to give their staffs the opportunity to do holiday shopping. Local retailers indicate that they would be pleased to support this by offering special discounts and services.

Bolster security without alarming customers

Security at retail stores will require both public and private initiatives. Consumers and employees in New York City and across the nation are asking for more visible protection. High-traffic areas and stores should increase security without creating alarm. Increased use of guards and surveillance equipment should be combined with emergency preparedness plans.

Support small retail businesses

Previous economic downturns have forced significant numbers of small retailers in New York City out of business. Survival rates could be raised in the short term, if the grants and loans flow quickly. Facilitation services could include insurance-industry outreach, expedited grant and loan applications, and corporate mentoring programs. Programs should focus particularly on small retailers in Lower Manhattan, since these businesses have seen the sharpest dropoff in revenues from the attack.

Rebuild Lower Manhattan by thinking outside of the box

The plan to revive and rebuild Lower Manhattan should explicitly address the need for a strong retail presence with an appropriate mix of stores. Before September 11th, many Lower Manhattan shoppers expressed dissatisfaction with the area’s retail and services. Now there is a chance to attract a mix of stores that would better meet the demands of local residents and workers.

Short-term actions should focus on store traffic flows — in particular, on giving shoppers an incentive to shop in stores in Lower Manhattan and the means to do so. Job placement programs (like outplacement support for displaced and laid-off workers) and PR campaigns could help. Ultimately, however, the health of New York City’s retail sector is a function of the well-being of the New York City consumer and the return of visitors from around the country and the globe to one of the most glamorous retail destinations in the world.

