

Sears Holdings Corporation: In Need of a Turnaround Strategy

Founded in 1893, Sears Roebuck grew over the course of the next century to become the world's largest retailer. Indeed, by 1962—the year that Sam Walton opened his first Walmart discount store—approximately one out of every 200 U.S. workers received a Sears' paycheck.¹ Even after being surpassed by Walmart as the largest retailer in 1989,² Sears continued to hold a spot on the Fortune 500 list and was still one of the country's largest retailers after its merger with Kmart in 2005.³ However, less than 10 years after the merger, the new Sears Holdings Corporation (SHC) found itself in crisis. With intense competition from retail giants such as Walmart and Target (and new competitors such as Amazon and Costco), Sears CEO Edward Lampert faced some serious questions. Eight years into the merger, Sears had closed almost one-third of its stores and had seen annual revenues drop by over 30%. Even more concerning, Sears' operating profits had dropped more than 140 percent (see **Exhibit 1**; also see **Exhibits 2 & 3** for comparative data on Walmart and Target, respectively). Not only had operating profits

EXHIBIT 1 Sears Holdings Corporation Financials (\$ Millions)

Fiscal Year	2013	2012	2011	2010	2009	2008	2007	2006	2005
Income Statement Items									
Revenues	\$36,188	\$39,854	\$41,567	\$42,664	\$43,360	\$46,770	\$50,703	\$53,016	\$49,455
Cost of Sales	27,433	29,340	30,966	31,000	31,374	34,118	36,638	37,824	35,743
S&A Expenses	9,384	10,660	10,664	10,425	10,499	11,060	11,468	11,574	10,892
Depreciation & Amortization	1,352	830	853	869	894	981	1,049	1,143	942
Operating Profit	(927)	(838)	(1,501)	437	667	302	1,586	2,529	2,123
Interest Expense	(254)	(267)	(289)	(293)	(248)	(272)	(286)	335	328
Income Taxes	(144)	(44)	(1,369)	(27)	(111)	(85)	(550)	933	715
Net Income	\$(1,365)	\$(930)	\$(3,140)	\$133	\$235	\$53	\$826	\$1,492	\$857
Balance Sheet Items									
Cash and Cash Equivalents	\$1,028	\$609	\$747	\$1,359	\$1,689	\$1,173	\$1,622	\$3,839	\$4,440
Merchandise Inventories	7,034	7,558	8,407	8,951	8,705	8,795	9,963	9,896	9,068
Property & Equipment, Net	5,394	6,053	6,577	7,102	7,709	8,091	8,863	9,113	9,823
Total Assets	18,261	19,340	21,381	24,360	24,808	25,342	27,397	29,906	30,573
Current Liabilities	8,185	8,414	9,212	8,643	8,786	8,512	9,562	9,912	10,350
Total Liabilities	16,078	16,168	17,040	15,746	15,373	15,643	16,730	17,200	18,962
Total Equity	2,183	3,172	4,341	8,614	9,435	9,699	10,667	12,706	11,611

Source: Sears Holdings Corporation, Annual Reports, 2006–2014.

2 Sears Holdings Corporation: In Need of a Turnaround Strategy

EXHIBIT 2 Walmart Financials (\$ Millions)

Fiscal Year	2013	2012	2011	2010	2009	2008	2007	2006	2005
Income Statement Items									
Revenues	\$476,294	\$468,651	\$446,509	\$421,849	\$408,085	\$404,374	\$377,023	\$348,992	\$312,101
Cost of Sales	358,069	352,297	334,993	314,946	304,106	304,056	284,137	264,152	237,649
Operating, SG&A Expenses	91,353	88,629	85,025	81,361	79,977	77,520	70,934	64,001	55,739
Operating Profit	26,872	27,725	26,491	25,542	24,002	22,798	21,952	20,497	18,713
Interest Expense	2,216	2,063	2,159	2,004	1,884	1,900	1,794	1,529	1,178
Income Taxes	8,105	7,958	7,924	7,579	7,156	7,145	6,889	6,365	5,803
Net Income	\$16,022	\$16,999	\$15,699	\$16,389	\$14,370	\$13,400	\$12,731	\$11,284	\$11,231
Balance Sheet Items									
Cash and Cash Equivalents	\$7,281	\$7,781	\$6,550	\$7,395	\$7,907	\$7,275	\$5,569	\$7,767	\$6,193
Inventories	44,858	43,803	40,714	36,437	33,160	34,511	35,180	33,685	31,910
Property & Equipment, Net	115,364	113,929	109,603	105,098	99,544	92,856	93,875	85,390	74,600
Total Assets	204,751	203,105	193,406	180,782	170,706	163,429	163,514	151,587	138,187
Current Liabilities	69,345	71,818	62,300	58,603	55,561	55,390	58,454	52,148	48,825
Total Liabilities	123,412	121,367	117,645	109,535	97,777	96,350	98,906	90,014	85,016
Total Equity	81,339	81,738	75,761	71,247	72,929	67,079	64,608	61,573	53,171

Source: Walmart Stores, Inc., Annual Reports, 2006–2014.

EXHIBIT 3 Target Financials (\$ Millions)

Fiscal Year	2013	2012	2011	2010	2009	2008	2007	2006	2005
Income Statement Items									
Revenues	\$72,596	\$73,301	\$69,865	\$67,390	\$65,357	\$64,948	\$63,367	\$59,490	\$52,620
Cost of Sales	51,160	50,568	47,860	45,725	44,062	44,157	42,929	40,366	34,927
SG&A Expenses	15,375	14,914	14,106	13,469	13,078	12,954	12,670	11,852	11,185
Depreciation & amortization	2,023	2,142	2,131	2,084	2,023	1,826	1,659	1,496	1,409
Operating Profit	4,229	5,371	5,322	5,252	4,673	4,402	5,272	5,069	4,323
Interest Expense	1,126	762	866	757	801	866	647	572	463
Income Taxes	1,132	1,610	1,527	1,575	1,384	1,322	1,776	1,710	1,452
Net Income	\$1,971	\$2,999	\$2,929	\$2,920	\$2,488	\$2,214	\$2,849	\$2,787	\$2,408
Balance Sheet Items									
Cash and Cash Equivalents	\$695	\$784	\$794	\$1,712	\$2,200	\$864	\$2,450	\$813	\$1,648
Inventory	8,766	7,903	7,918	596	7,179	6,705	6,780	6,254	5,838
Property & Equipment, Net	31,738	30,653	29,149	25,493	25,280	25,756	24,095	21,431	19,038
Total Assets	44,553	48,163	46,630	43,705	44,533	44,106	44,560	37,349	34,995
Current Liabilities	12,777	14,031	14,287	10,070	11,327	10,512	11,782	11,117	9,588
Total Liabilities	28,322	31,605	30,809	28,218	29,186	30,394	29,253	21,716	20,790
Total Equity	16,231	16,558	15,821	15,487	15,347	13,712	15,307	15,633	14,205

Source: Target Corporation, Annual Reports, 2006–2014.

declined sharply, but Sears' return on equity and return on assets had plummeted as well (see Exhibits 4 & 5). In a January 2014 blog post, Lampert said that the poor financial performance did not clearly reflect the company's true success. In particular, Lampert cited customer engagement growth in Sears' *Shop Your Way* program, a digital loyalty program that not only gave customers opportunities to save on Sear's products, but also served as a social network that allowed shoppers to connect and share their shopping experiences.⁴ Despite Lampert's optimism, investors appeared to share analysts' concerns about Sears' future: since 2010, SHC market capitalization has fallen nearly 75 percent (see Exhibit 6). As Brian Sozzi of Bellus Capital Advisors put it, "Sears is in crises. Sears is not investing in their name brands so they can keep the customer coming back to the store for them. I view Sears in a slow death spiral."⁵

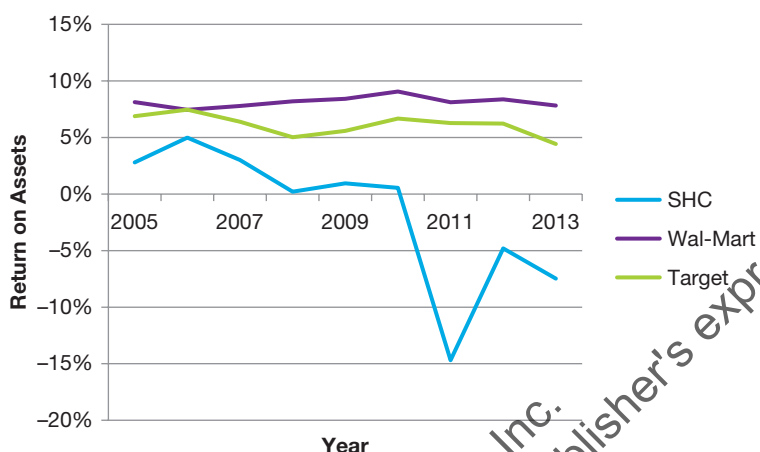


EXHIBIT 4 Return on Assets

Source: Sears Holdings Corporation, Walmart Stores, Inc., and Target Corporation, Annual Reports, 2006–2014.

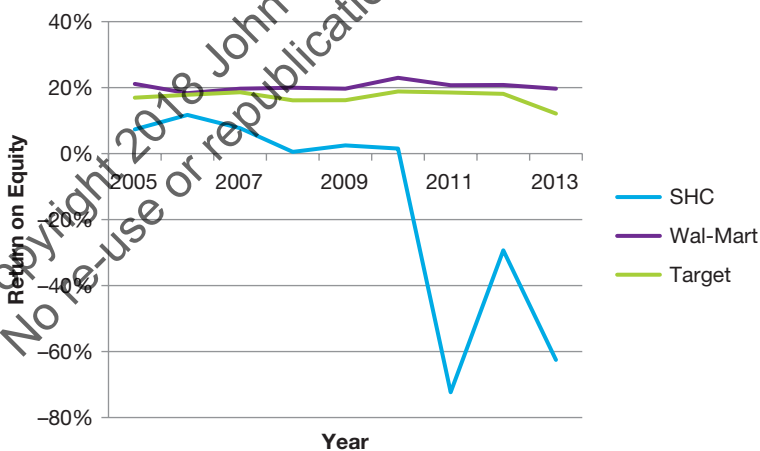


EXHIBIT 5 Return on Equity

Source: Sears Holdings Corporation, Walmart Stores, Inc., and Target Corporation, Annual Reports, 2006–2014.