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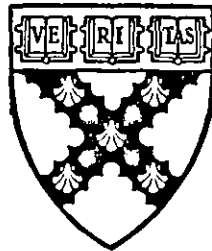
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**EXPENSES AND PROFITS OF
LIMITED PRICE VARIETY STORES
IN 1943**

CHAINS AND INDEPENDENTS

**BY
EDWARD C. BURSK**



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**HARVARD UNIVERSITY
GRADUATE SCHOOL OF BUSINESS ADMINISTRATION
BUREAU OF BUSINESS RESEARCH
SOLDIERS FIELD, BOSTON 63, MASSACHUSETTS**

DIGEST

**EXPENSES AND PROFITS OF LIMITED PRICE VARIETY
STORES IN 1943**

CHAINS AND INDEPENDENTS

For the thirteenth consecutive year the Harvard Bureau of Business Research has collected and analyzed sales, margin, expense, and earnings data for limited price variety chains in North America. This year for the first time a study of figures for independent variety stores has been added to the survey. The research was sponsored by members of the Limited Price Variety Stores Association, and the bulletin was written by Edward C. Bursk, Assistant Professor of Business Administration.

A digest of the findings follows:

In spite of the many and varied new situations presented to store managements by war conditions, variety stores, both the independents and those operated by chains, were able to show satisfactory operating results in 1943. Salient characteristics of the picture presented by these reports were as follows:

Chains

(1) Sales per store continued to advance in the face of merchandise difficulties, at a typical rate of 14% over 1942.

(2) The number of stores operated remained practically unchanged.

(3) Consequently, total sales volume per chain typically increased at the same rate as sales per store (14%). Aggregate sales showed an increase of 6% over 1942 for all comparable reporting firms.

(4) Earnings before income taxes remained on the average at the same high level as in 1942 — 10% of sales.

(5) Gross margin and total expenses, at 36% and 29% of net sales respectively (based on the combined results for all reporting firms), exhibited fractional decreases over the results for 1942.

(6) The decline in the expense rate, less marked than for the previous two years, was the net result of fractional decreases

in tenancy costs and the lesser items of expense, partially offset by a rise in salaries and wages of $\frac{1}{2}$ of 1% of the sales dollar.

(7) The rate of stock-turn exceeded that for 1942, because of the lower average value of dollar inventories carried and the increase in sales.

Independents

(1) Sales per store averaged \$51,000 based on the combined results for all reporting stores. The median figure based on the results of all firms taken individually was \$43,000.

(2) The rate of sales increase over 1942 was typically 18%, which was higher than that experienced by the chains as a whole but remarkably suggestive of the smaller chains. This was the only comparison with 1942 results that was possible.

(3) Earnings before income taxes amounted to slightly less than $9\frac{1}{2}$ % of sales, a record which compares favorably with that of the chains as a whole.

(4) Both the typical gross margin of 33% and the typical expense rate of 26% were lower than the comparable figures for chains as a whole.

(5) The net comparative result for the independent variety stores was higher earnings on the whole than for the small variety chain organizations.

(6) The rate of stock-turn tended to be higher for the independents than for the small chains.

The decline in gross margin of the variety chains in 1943, although small, marked at least a temporary reversal in the upward trend which began in 1939. Sales and expense rates, for their part, did not show a reversal in direction, but the degree of change slackened off; sales did not increase so rapidly in 1943 as they had in 1942, and the expense rate was not reduced so much.

The significance of the tightening up in the operating picture of the variety chains, as reflected in the decline in rate of sales increase and rate of expense reduction, with gross margin remaining virtually unchanged, cannot be appraised with assurance as yet. It is interesting to observe, however, that in 1943 department stores showed an acceleration in rate of sales advance and also were able to make a substantial reduction in the expense rate.

This contrasting experience is particularly suggestive because of the fact that in earlier years results of variety chains have tended to anticipate those of department stores.

That rate of sales increase in itself, and entirely apart from the volume reached, has a definite and discernible influence on operating results has been demonstrated repeatedly in Bureau studies. A firm relation appears to prevail between rapid increases in sales and decreases in expense rates. Department store results in 1943 emphasized this situation, and the experience of the variety chains again reflects the relationship. As store managements approach a period in which rate of sales increase may be expected to change, particularly if the change is to be a downward one, it becomes important to anticipate, so as to allow for, the probable effects upon operating factors. Already in 1943 the larger variety chains appear to have entered a period, not of decline in volume, but of decline in rate of increases.

One of the noteworthy showings of the 1943 figures is the difference in rate of sales advance for the large and the small chains. In 1942 the rate of sales growth was fairly uniform for both groups, but in 1943, while the smaller chains were able to maintain the rate of advance, the larger chains were not.

The expense rate in 1943 was generally higher for the larger chains than for the smaller chains, although expense percentages for salaries and wages in the former group were lower. Nevertheless, it was the smaller chains which were able to make a reduction in this item as compared with the previous year; this reduction thus appears to be definitely related to the relatively rapid rate of sales increase of the smaller chains. Higher tenancy expense for the larger chains more than offset their advantage in expense for salaries and wages.

In general, the net profit figure was similar for all size categories. The only significant exception was the definitely lower profit of the smallest chains, which had a disproportionately narrow gross margin.

A separate analysis of long-term trends revealed the following significant facts:

- (1) Gross margin showed a rising trend until 1943.

(2) Total expense rate has declined since 1938 to slightly below the 1931 level.

(3) Net profit has fluctuated widely, but has increased steadily since 1938. Increasing income and excess profits taxes, however, have more than offset this increase, and net gain after taxes has declined.

(4) Average sales per store have been nearly doubled since 1932.

These long-term trends in the operations of variety chains accord in general with those for department stores, with the variety chains showing the greater stability. There is a suggestion, from both expense and gross margin figures, that variety chains have become in many respects low-price department stores.

Changes shown in the importance of the various merchandise lines carried by variety chains are considered in detail in the Bulletin. These changes are particularly interesting in that they appear to reflect not only wartime shortages but also definite trends in the character of the chains themselves.

Operating results for the 33 independent stores which reported to the Bureau in 1943 compared favorably with those for the chains. There was a decided similarity between the figures for small department stores and the independent variety stores. Independent variety stores apparently experienced no competitive disadvantage in comparison with either small department stores or small chain organizations. Advantage in gross margin, expense, and earnings, as a matter of fact, was with the independents in 1943 rather than with the small chains. The favorable gross margin of the independent stores suggests a tribute to the services of the buying groups with which most of the stores reporting were voluntarily associated.

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Boston 63, Massachusetts
August, 1944

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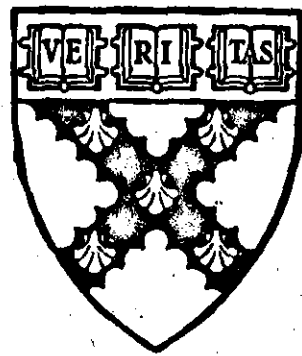
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HARVARD COLLEGE

FOREWORD

For the thirteenth consecutive year the Harvard Bureau of Business Research has collected and analyzed sales, margin, expense, and earnings data for limited price variety chains in North America. This year for the first time a study of figures for independent variety stores has been added to the survey.

The research has been made possible by the members of the Limited Price Variety Stores Association who for many years have given the program financial support. The Bureau is grateful for the continued interest of the association and for the efforts of the chain controllers and their staffs and the proprietors of individual stores who prepared the essential basic reports. It is gratifying to know that the executives of 45 chains and 31 independent stores were willing, in a period of acute personnel shortages, to allocate time to the project.

The accounting and statistical work was supervised by Miss Esther M. Love under the direction of Professor Elizabeth A. Burnham. The program benefited greatly from the practical advice of Professor Malcolm P. McNair who has long taken an active part in the retail cost research. The bulletin was written by Professor Edward C. Bursk.

MELVIN T. COPELAND
Director of Research

BOSTON, MASSACHUSETTS
August, 1944

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Chart I. Limited Price Variety Chain Expenses and Profits: 1943

(with 1942 percentages for comparison)

Items	1943		1942 ¹
	Aggregate Dollar Figures (in thousands) for 43 Chains Operat- ing 5,291 Stores	1943 Net Sales =100%	1942 Net Sales =100%
<i>The chief source of revenue for these chains, of course, was</i> Net Sales	\$1,284,636	100.00%	100.00%
<i>A primary charge against this revenue, and the largest single expenditure, was represented by,</i> Net Cost of Merchandise Sold	\$818,061	63.68%	63.34%
<small>Which included the cost of merchandise purchased for resale delivered at the stores, less trade and cash discounts, plus or minus the amounts taken from, or added to, inventories during the year.</small>			
<i>Other costs which had to be met were those for operating the chains, as follows:</i> Salaries and Wages	\$192,629	15.00%	14.54%
<small>Comprising salaries, wages, and bonuses of all employees including executives, but excluding pensions and payroll taxes;</small>			
Tenancy Costs	\$91,067	7.09%	7.49%
<small>Including rentals, taxes, and insurance paid on leased real estate; taxes, insurance, depreciation, repairs, and interest on owned real estate; and heat;</small>			
Light, Water, and Power	\$9,791	0.76%	0.85%
Depreciation on Fixtures and Equipment	\$8,129	0.63%	0.67%
Supplies	\$9,902	0.77%	0.85%
Taxes	\$13,335	1.04%	1.07%
<small>Not including taxes on real estate, or on income, but comprising other taxes imposed by national, state, and local governments;</small>			
All Other Expense (including interest)	\$42,528	3.31%	3.35%
<small>The charge for interest included interest paid on borrowed capital and, in addition, an imputed charge for interest at the rate of 6% on net worth except real estate, leaseholds, and goodwill. Interest at 6% on the real estate equity and mortgage interest were included in Tenancy Costs. Interest received was credited to the Interest account.</small>			
<i>Thus, for merchandise and chain operation combined, these firms experienced a</i> Total Cost of	\$1,185,442	92.28%	92.16%
<i>After meeting these costs, there remained a</i> Net Profit of	\$99,194	7.72%	7.84%
<small>Which constituted the net profit from merchandising operations.</small>			
<i>The chains, however, received</i> Sundry or Other Revenue, Net	\$31,217	2.43%	2.39%
<small>Including any profit or loss on real estate operations; the amount charged in expense for interest on net worth; dividends from manufacturing or foreign subsidiaries; and other miscellaneous revenue.</small>			
<i>And, therefore,</i> Total Net Business Profit Amounted to	\$130,411	10.15%	10.23%
<small>This was the earnings of these firms before income taxes.</small>			
<i>Taxes on income and excess profits, after credits for debt retirement and postwar refunds, amounted to</i> ²	6.20%	6.20%
<i>Thus leaving available for dividends, withdrawals, and surplus</i>	3.92%	4.03%

¹Data for 1942 are based on aggregate dollar figures for 39 chains with net sales of \$1,210,485 and operating 5,285 stores.

²For each year a total of 30 firms, representing nearly 99% of the aggregate sales volume, reported information on income taxes. The averages for these taxes and net gain after taxes are therefore based on a smaller number of reports than the other data in the chart and will not necessarily add exactly to the net gain before taxes.

APPENDIX

Base of Percentages. All percentages in this bulletin, unless otherwise indicated, are based on net sales as 100%.

Gross Margin. Gross margin is the amount remaining after the deduction of net cost of goods sold from net sales. Net cost of goods sold is billed or invoice cost of goods sold, less cash discounts taken and allowances received, plus transportation charges, and plus proper charges for merchandise depreciation and stock shortages.

Transportation Charges. In this account are included all transportation charges on merchandise shipped either directly to individual stores by manufacturers or to chain warehouses. Any transportation costs incurred by the chains for transferring merchandise from warehouses to stores or between stores likewise is included in this item. The transportation charges are considered as a part of the cost of merchandise.

Salaries and Wages. The salary and wage classification embraces all items of payroll expense both in stores and in the central organizations, including the compensation of chief executives. One change in the definition of the account made for the 1936 study and continued in following years should be noted: pensions, formerly included in salaries and wages, are now considered as miscellaneous expense.

Tenancy Costs. Tenancy costs comprise all expenses on property used in the business. They therefore cover, in the case of leased property, not only rentals paid but other payments made in lieu of rent, such as taxes, insurance, repairs, and amortization of leaseholds. Charges on owned real estate included in this account comprise taxes, insurance, repairs, and depreciation on owned real estate, plus a fair charge for interest on equity in land, buildings, and improvements, as well as interest actually paid on mortgages. The definition of the tenancy cost account for 1943 differs in two respects from that for 1929, 1931, and 1932, but is the same as that obtaining in the years 1933 through 1942. Charges for amortization of major improvements on leased property, formerly combined with charges for depreciation on fixtures and equipment, have been allocated to the tenancy cost item. Also, since many of the firms lease stores for which heat is provided by the landlords, the cost of heat has been included with other real estate charges in order to assure comparability.

Interest. In order to obtain comparability between businesses using different methods of financ-

ing, interest at the rate of 6% on the average net worth exclusive of real estate, leaseholds, and goodwill is considered as an expense, as well as interest actually paid other than mortgage interest. Interest computed on real estate equity and mortgage interest are considered as tenancy expense. From the sum of the actual interest payments and the interest on owned capital is deducted the amount of interest and dividends received.

Total Expense including Interest. Total expense including interest is the complete cost of doing business, comprising, in addition to the usual outlays, salaries of executives, proprietors, and partners; rental charges for owned real estate; and interest on owned capital.

Net Profit. The above procedure with respect to interest leads to a narrow definition of net profit as a theoretically residual sum over and above a customary interest return on invested capital.

Net Other Income. Net other income has three component parts: profit or loss from real estate operations; interest on net worth other than real estate; and other revenue, net. In the first of these are included net profit or loss on owned real estate not used in the business, interest previously charged as expense on the investment in owned real estate used in the business, profit or loss on real estate which has been sublet, and profit or loss of any subsidiary real estate holding companies. Under interest on net worth is credited back the interest at 6% on the average net worth, excluding real estate, previously included as an operating expense in arriving at the net profit on merchandising operations. Miscellaneous revenue, including such receipts as dividends from manufacturing and/or foreign subsidiaries and income from weighing machines and telephones, is considered as sundry revenue, net. Commissions or net profits from leased or concession departments were included here by several chains.

Net Gain before Income Taxes. To arrive at the final net gain or net business profit, net other income is added to the net profit. Therefore the net gain figure, while not affording, from a statistical standpoint, so valid an interchain comparison as the net profit figure, may be taken as roughly approximate to net business profit in the commonly understood sense. Net gain is expressed both as a percentage of net sales and as a percentage of the average net worth. The use of the average net worth as a base for this figure introduces the complication of differing policies in regard to real es-

rate for a chain which, either directly or through a subsidiary real estate corporation, owns many of the stores operated, the total average net worth is large in proportion to the net sales volume; and as a result the rate of return on invested capital is low as compared with that for a chain owning little or no real estate.

Taxes on Income and Excess Profits. Taxes on income and excess profits have been considered as deductions from net gain. In this tax figure a deduction has been made for the 10% credit whether used currently for debt reduction or set up as a postwar rebate.

Taxes (except on real estate or income). This tax account includes all tax expense except real estate taxes, included under tenancy costs, and federal and state taxes on net income. Where state or municipal taxes on sales or gross income are not collected directly from customers but are absorbed by the chain as expense, such cost is included under sales taxes, a subdivision of the tax account. Other tax expense includes special chain taxes, licenses, taxes on equipment and merchandise inventory, corporate taxes, the federal capital stock tax, payments for unemployment and old age taxes made in compliance with the Social Security Act, and other taxes not specifically mentioned elsewhere.

Rate of Stock-turn. The rate of stock-turn, or rapidity of merchandise turnover, is calculated by dividing the cost of merchandise sold by the average inventory at cost. For chain enterprises the average inventory includes merchandise both in stores and in warehouses. Stock-turn figures of two types have been computed: the first rate, available for all chains, is based on the average of the beginning and ending inventories; and the second rate, available for part of the chains only, is based on the average of 12 monthly inventories.

Leased or Concession Departments. Eleven of the 43 chains indicated that leased departments or concessions were operated in some of their stores in 1943. Volume in such departments usually was small in relation to total sales, and the firms were requested to exclude the revenue from total sales and consider the commissions received under net other income.

For a few chains, however, leased department or concession sales amounted to more than 3.0% of the total volume. In such cases adjustments were made to insure comparability of the operating percentages. Two alternate methods were suggested to the firms as acceptable bases for the

adjustments. The first method was to exclude the leased department sales from total sales, estimate the indirect expenses incurred by the chain in behalf of the departments, and exclude these charges from expense; the difference between commissions and the estimated indirect expenses was to be considered under other revenue. The second method was to include the leased department sales in chain sales and add to chain operating expenses estimates of the expenses incurred directly by the leased or concession departments. An amount corresponding to these direct expenses was then added to the commissions and included in the gross margin with the difference between leased department sales and this figure charged to merchandise cost.

Methods. The statements used in the study were carefully examined for comparability and completeness of data. Whenever questions arose concerning the omission of or the interpretation of material, letters were written to the individual firms requesting additional information. Usually the necessary material was forthcoming. In other cases when it seemed probable that the omission of a figure by a firm was equivalent to a zero entry, zero figures were used in arriving at the averages presented. When it was evident that one reported expense figure covered two or more accounts, adjustments were made to allocate the amount to the proper accounts. In still other instances where material was not reported, the averages were based on a reduced sample; usually medians only are presented in this latter case, and asterisks in the tables indicate the lack of averages for such items.

Aggregates and Averages. Some of the figures included in this report are averages based on aggregate dollar figures. Such aggregate figures manifestly are weighted according to sales volume. These average figures based on dollar aggregates obviously do not afford a good year-to-year comparison unless only identical firms are used, since the averages are substantially affected by the omission or addition of one or two large firms.

Median Figures. Many of the other data presented in this report consist of median figures. These figures are based on percentages computed for each firm in the group individually. Such figures, therefore, give equal weight to each chain, irrespective of sales volume and number of stores. The median is the middle figure in an array of percentages listed in order from the smallest to the largest.