Canadian Retail Giant Faces Grim Reality

Description

Several months ago, I wrote an article warning about the prospects for North America's oldest company, retail giant **Hudson's Bay** (TSX:HBC). Since the article was published, there have been some interesting developments at the company.

Bid to take the company private

In mid-June, Richard Baker, former CEO and current chairman, made a bid of $1.3 billion to take HBC private. Baker, along with his father Robert Baker, owns National Realty Development Corp., one of the largest privately held real estate development companies in the U.S.

Baker and his buyout consortium, who already own 57% of the company, offered $9.45 per share — a nearly 50% premium on the stock. The stock subsequently jumped over 40% the day the news of the offer broke.

However, minority stakeholders were unimpressed with the offer, arguing that the real value of the company lies in is real estate holdings. These shareholders claim that the true value of the stock is between $28 and $33 per share. The company's real estate holdings include the recently renovated Saks Fifth Avenue flagship store in New York. In an effort to drum up cash, HBC sold the iconic Lord & Taylor flagship store on Fifth Avenue last year for $1.1 billion.

Store closings inevitable

No doubt HBC will be forced to close more stores. The company is in the midst of shuttering all locations of its Canadian home store, Home Outfitters, by the end of 2019. This is most likely the tip of the iceberg.

As the company remains under pressure, it will be forced to sell more property or close more stores to remain operational. There is a question as to how much of the company's prime real estate can be divested while keeping retail operations afloat. If the company continues to sell property to raise capital, it would be forced to rent some space for the stores it keeps open, creating a vicious real estate circle.

Most notable among those opposing the privatization deal is the New York hedge fund, Land & Buildings Investment Management. The hedge fund is run by activist investor Jonathan Litt, who has steadfastly pushed for change at HBC. Litt calls the proposed deal a “woefully inadequate offer due to the exceptional assets the company owns.”

At the request of all parties involved, a Hudson’s Bay board committee has hired **Toronto-Dominion Bank** to evaluate the deal. TD Bank is expected to recommend whether the company should accept the offer, reject it in its entirety, or try to negotiate further.

Profits decline

Even as CEO Helena Foulkes is pulling out all of the stops to save HBC, her efforts have been unsuccessful thus far. In addition to closing all of the Home Outfitter stores, the company is planning to close 20 Saks Off Fifth locations and 10 Lord & Taylor locations.

In the June first-quarter earnings release, HBC reported a decline of $48 million in gross profit year over year. Foulkes has managed to reduce selling, general, and administrative expenses by $54 million. She has also committed to focus solely on North America by selling all of the company’s stakes in German real estate and retail for $1.5 billion.

Bottom line

Last year, a plan to take high-end retailer **Nordstrom** private ended abruptly when only one offer was received. A special committee was formed, which was holding out for a better price than offered by the Nordstrom family, the only bidder. When no other bidder emerged, the company ended the potential sale process.

It is possible that the HBC privatization bid could end with the same fate. With the face of retail changing rapidly in North America, no one knows how America’s oldest retailer will fare. At this point, I would take a wait-and-see approach before buying the stock. There is just too much uncertainty to make this dying retailer look attractive.

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