A look at the evolving fundamentals of the footwear marketplace

Inside

SHOE REVIEW

FDRA FOOTWEAR EXECUTIVE REPORT

FOOTWEAR DISTRIBUTORS AND RETAILERS OF AMERICA

"FDRA's mission is to support the footwear industry as its business intelligence hub on a range of issues, and be its voice and advocate in Washington, DC and around the globe on government regulations, trade and tax policy. Join us."

MIKE JEPPESEN
FDRA Chairman and President of Global Operations at Wolverine Worldwide

FDRA is the footwear industry's business and trade association

Founded in 1944, FDRA is governed and directed by footwear executives. We are the only trade organization focused solely on the footwear industry, serving the full footwear supply chain and boosting the bottom lines of its members. How? Innovative products, training and consulting on footwear design and development, sourcing and compliance, trade and customs, advocacy, and consumer and sales trend analysis for retailers selling shoes around the world. FDRA also runs the footwear industry's weekly podcast *Shoe-In Show* featuring leading footwear executives and experts discussing key business trends.

FDRA members range from small family-owned footwear businesses to multi-national footwear companies. Members include the majority of U.S. footwear manufacturers, brands, retailers and importers. In all, FDRA supports over 250 companies and 500 brands worldwide, representing 80% of total U.S. footwear sales, making us by far the largest and most respected American footwear trade and business association.

FDRA leadership team

MIKE JEPPESEN
FDRA Chairman
President, Global Operations
Wolverine Worldwide

CLIFF SIFFORD
FDRA Vice Chairman
President & CEO
Shoe Carnival

JENNIFER BENDALL
FDRA Treasurer
Vice President, Government & Public Affairs, NIKE

ED ROSENFELD
FDRA Ex Officio Chairman
Chairman & CEO
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ANDY GILBERT
Chairman
Membership Outreach
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Chairman
Diversity & Workforce Development
Converse

KELLIE DAVIES
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Sourcing & Compliance
Target

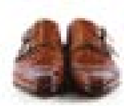
JOSUE SOLANO
Chairman
Product Safety
BBC International

OLIVER NG
Chairman
Asia Outreach
Ever Rite Factory Group

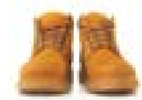
MATT PRIEST
President & CEO
FDRA

WHY IS OVER 90% OF THE FOOTWEAR INDUSTRY MEMBERS OF FDRA? BECAUSE WE BOOST THEIR BUSINESS.

Footwear Customs Classification Guidance

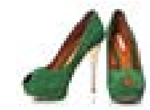


Exclusive Sales Data and Trends



Social Compliance and Product Safety Expertise

Customized Sourcing Strategy Support



How FDRA accomplishes its mission

INTELLIGENCE

FDRA is the footwear industry's business intelligence hub providing data, analysis, and insights on a range of key issues impacting the entire footwear industry, from design and sourcing to retail and fashion.

SOLUTIONS

FDRA is the footwear industry's thought leader finding innovative solutions to a range of challenges impacting the footwear industry, from sourcing to product safety regulations and beyond.

ADVOCACY

FDRA is the footwear industry's voice on government policy pushing for the elimination of global footwear barriers and tariffs that drive up costs for companies and consumers.

EDUCATION

FDRA is the footwear industry's leading educator hosting a range of events from webinars to major summits to *Shoe-In Show*, focusing on industry challenges, best practices, and common solutions.

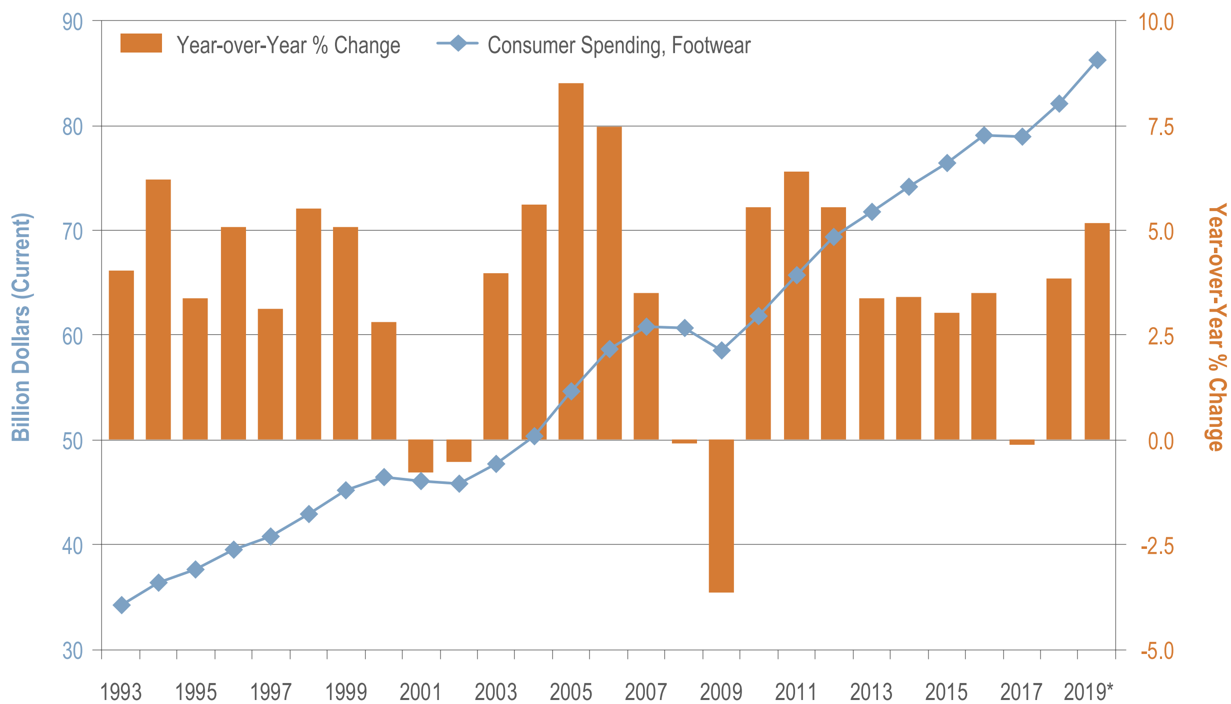
The U.S. footwear industry in 2019 tells a tale of two markets, one of confidence and persistent growth, and the other more cautious, beset by record duties, tight margins, and fading employment. The optimists point to record footwear demand and imports, record equity markets, ten straight years of economic growth, and a record 109 straight months of growth in the labor market. The pessimists counter with trade wars, impeachment inquiries, signals of a recession over the horizon, surging duties, and shuttered storefronts. These seemingly contrary signs in fact are all in play this year, leaving footwear companies in a tumultuous sea of shifting policies and paradigms. FDRA is here to help the industry navigate these chaotic waters by keeping members abreast of these evolving trends and to address and capitalize upon them as one voice.

U.S. consumer appetite for footwear remains hearty in 2019

The high tide of the ongoing—if mature—economic expansion is helping raise most ships, including demand for footwear. The U.S. Bureau of Economic Analysis reports consumer spending on shoes and other footwear over the first three quarters of the year rose more than 5% from the same period in 2018. FDRA estimates full-year spending will rise to a record of more than $86 billion, higher nine of the last ten years. Naturally, some are faring better than others. While some outlets downsized and even closed in 2019, others are reporting record sales, with burgeoning online sales accounting for a growing share of footwear demand.

Within total consumer demand for footwear, shoe stores are advancing deeper into 2019 with a strong expansion that continues to point to a robust year in 2019. Sales over the first nine months of 2019 suggest full-year sales in this channel may reach upwards of $39 billion, a figure that is coming more into focus as the year progresses. FDRA estimates about a two-in-three chance that full-year shoe store sales will expand from 5.7% to 6.7%, a range that is narrowing with each passing month. If realized, shoe store sales also will rise to a record this year, similarly higher nine of the last ten years.

Record Year for U.S. Consumer Spending on Footwear



* FDRA forecast

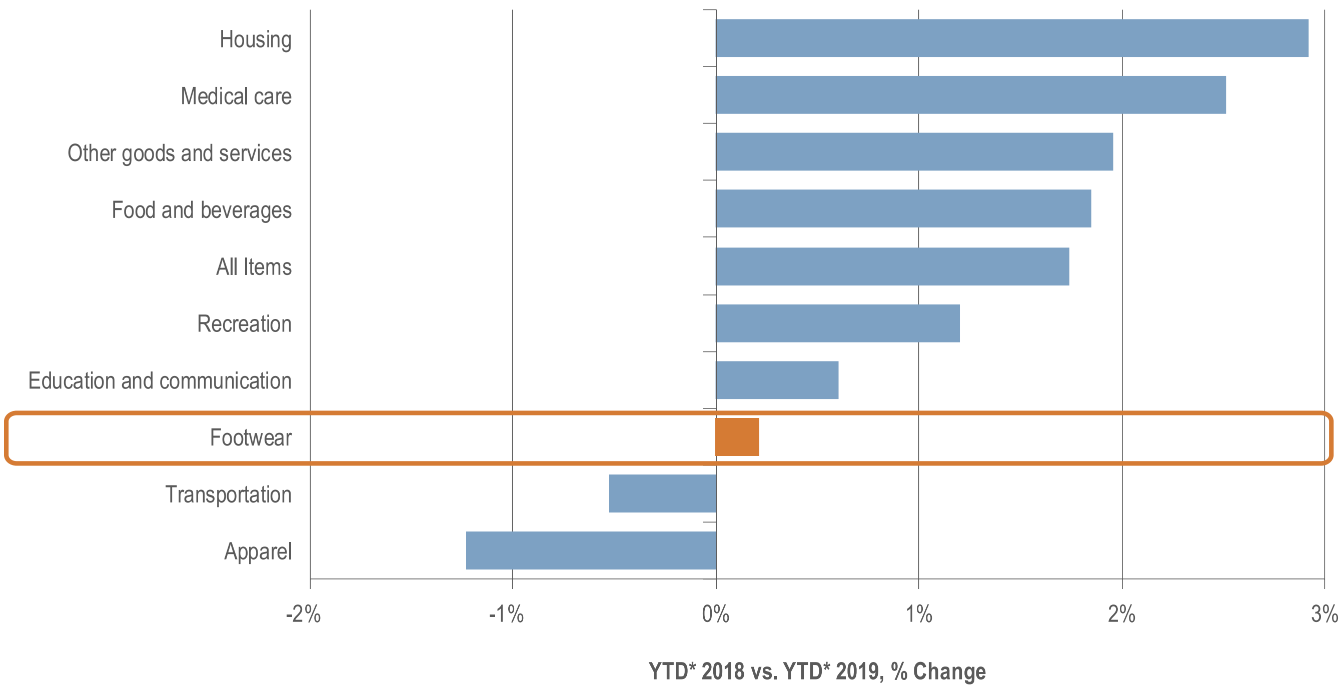
Source: U.S. Bureau of Economic Analysis

Causes and implications for little change in footwear prices in 2019

While footwear demand is faring well in 2019, retail prices for footwear are little changed, in spite of broadly higher prices across the consumer marketplace. Over the first ten months of the year, overall retail prices are up 1.7% from the corresponding period in 2018, led by gains in housing (up 2.9%) and medical care (+2.5%). But year-to-date footwear prices are up a modest 0.2%, as a -1.1% drop in womenswear is offsetting modest gains in men's and children's footwear prices so far this year. As a result, while overall retail prices for goods and services continue to slowly gain traction in this low-interest rate and low-unemployment environment, prices for footwear—particularly women's footwear—remain on the defensive. On balance, these sagging prices imply persistently tight margins and squeezed profits for footwear retailers already facing creeping costs for labor, rent, merchandise, distribution, and other inputs.

Overall retail prices for goods and services continue to slowly gain traction in this low-interest rate and low-unemployment environment, while prices for footwear—particularly women's footwear—remain on the defensive.

Footwear Prices Rise Slower than Prices in most other Retail Sectors in 2019



* YTD = January – October

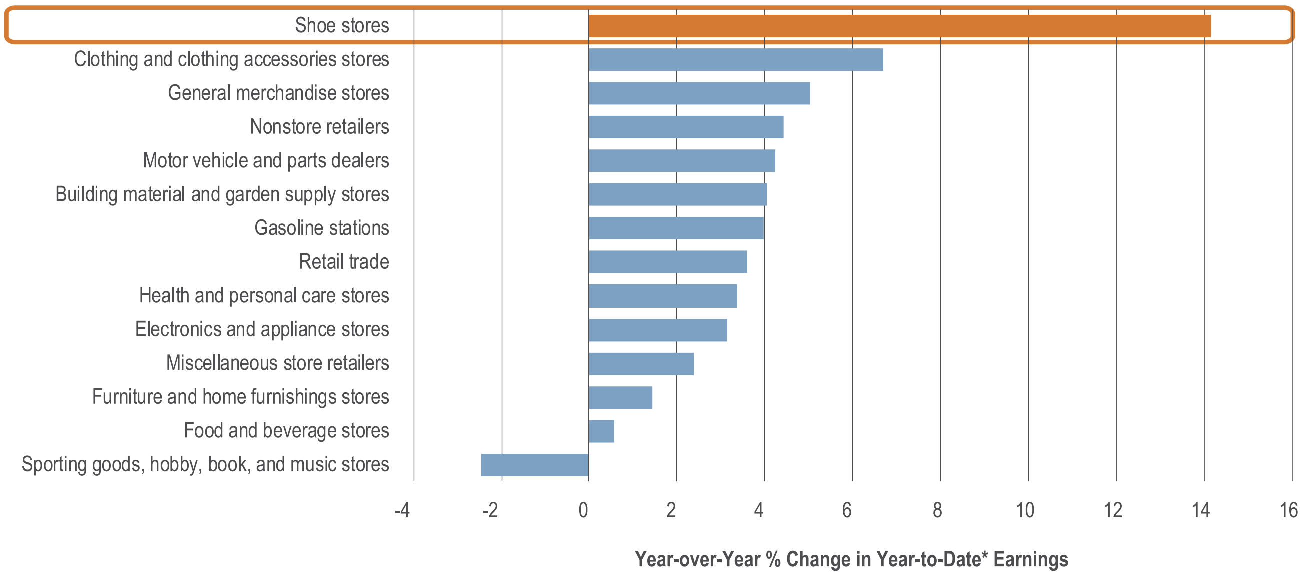
Source: Bureau of Labor Statistics

Amid the tightest labor market in half a century, workers' weekly earnings across the retail spectrum are climbing, leaving shoe stores few options but to boost wages aggressively to offset an exodus of employees seeking higher wages elsewhere and to compete for a shrinking supply of skilled workers.

Shoe stores boost worker pay to attract and retain talent in tight labor market

The U.S. shoe store labor force is posting some intriguing—and seemingly incongruent—trends in 2019, indicative of a retail sub-sector in transition as the number of outlets declines but sales grow to a record and competition across the economy for a dwindling supply of labor remains fierce. Amid the tightest labor market in half a century, workers' weekly earnings across the retail spectrum are climbing, leaving shoe stores few options but to boost wages aggressively to offset an exodus of employees seeking higher wages elsewhere and to compete for a shrinking supply of skilled workers. Average hourly earnings across the overall retail market grew a seasonally-adjusted 4.4% in October from a year earlier to a record $19.85, forcing shoe store employers to increase average hourly wages aggressively to attract and retain skilled workers. Indeed, so far this year shoe stores have boosted average hourly wages 14.1% from the same period in 2018, well above wage hikes in other retail sectors.

Growth in 2019 Average Weekly Earnings at Shoe Stores is well above Industry...



* YTD = January – September

Source: Bureau of Labor Statistics

But even with this sharp hike, average hourly wages at shoe stores still lag wages paid across the broader retail market, causing shoe stores to continue to struggle with staffing. At $18.47 per hour, the year-to-date average wage paid at shoe stores trails the $19.60 average hourly rate paid across the overall retail market. As a result, employment in this retail sub-sector faded again in the latest month to the lowest in more than six years. So far this year, shoe stores are seeing their number of workers fade faster in 2019—in spite of sharply higher wages—than all other retail sectors.

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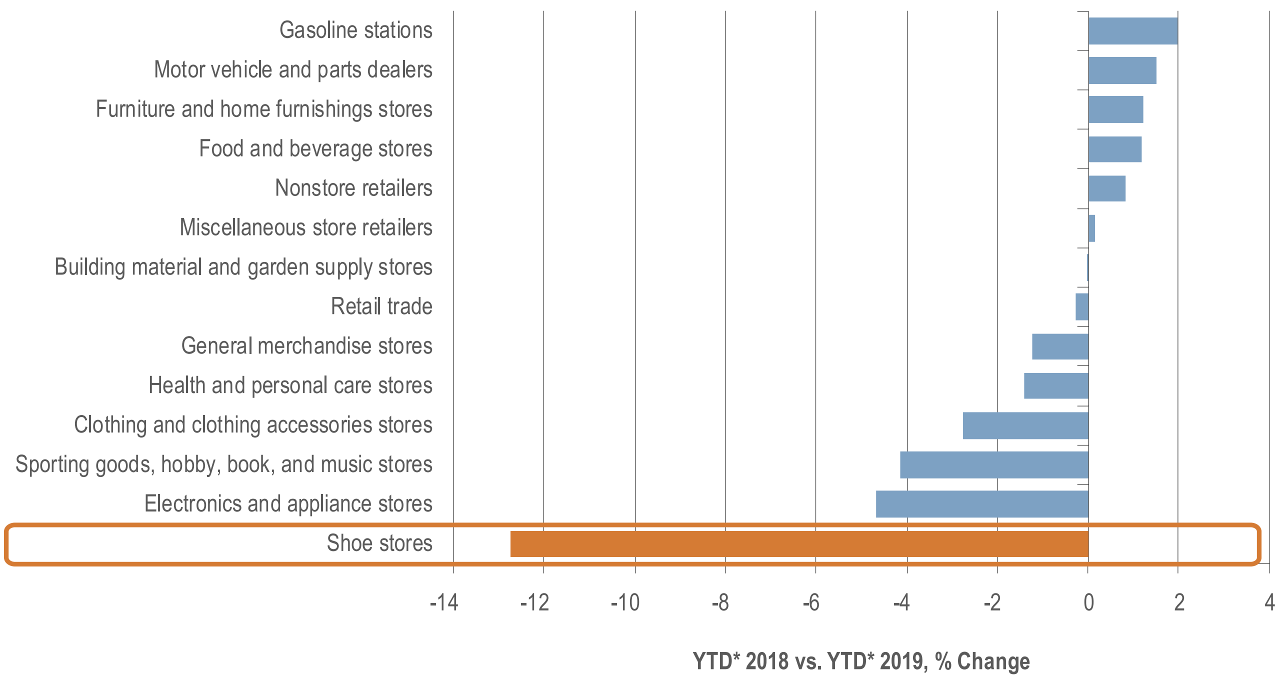
...but Shoe Stores see Employment Fade Faster in 2019 than all Other Retail Sectors



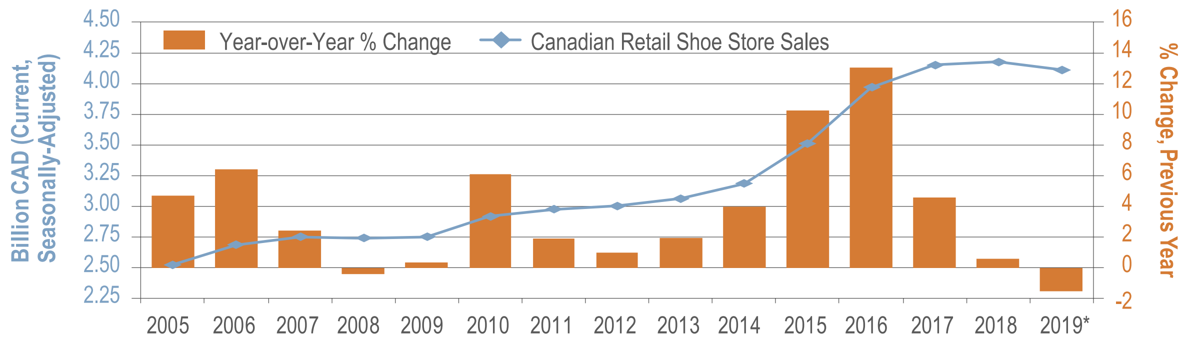
* YTD = January – October

Source: Bureau of Labor Statistics

O Canada: annual shoe store sales to fade for first time in a decade

The Canadian economy practically came to a halt in the first two quarters of 2019, bringing unwelcome implications for annual footwear demand. After three straight months of contraction this spring and summer, Canadian shoe store sales are on track to see a modest decline in 2019, *the first annual contraction in a decade* for this retail sub-sector, confirming our long-held view that full-year Canadian shoe store sales would fail to match the previous year's record sales of nearly CAD4.2 billion. Looking ahead, the IMF expects the Canadian economy in 2020 will grow modestly in sympathy with the U.S. economy, suggesting Canadian retail sales—and by extension, shoe store sales—may remain flat-footed well into the new year, a dramatic change for a market that has grown an average 4.1% each year over the last decade.

Annual Canadian Shoe Store Sales set to Contract for First Time in a Decade



* FDRA forecast
Source: Statistics Canada

Modest rebound—at best—for European market in 2019

European sales of textiles, clothing, footwear, and leather goods are set to gain some traction in 2019, confirming our outlook several months ago. The market shrank -0.6% in 2018, the first decline in five years. But over the first nine months of 2019, year-to-date sales are up 1.4% from the same period last year. FDRA estimates there is about a two-in-three chance that full-year sales of textiles, clothing, and footwear will grow from 1.0% to 1.7% in 2019, a range that is likely to narrow with each passing month. If this pattern repeats itself again this year as we continue to expect, 2019 will see a relatively modest rebound—at best—in sales of textiles, clothing, and footwear from last year, lukewarm news for participants across the supply chain dependent on this key market. With the European retail footwear marketplace larger than the U.S. market, this likely dull growth puts more of the onus on the U.S. consumer to bear the burden of driving footwear demand, a daunting task in light of dimming economic prospects for the country.

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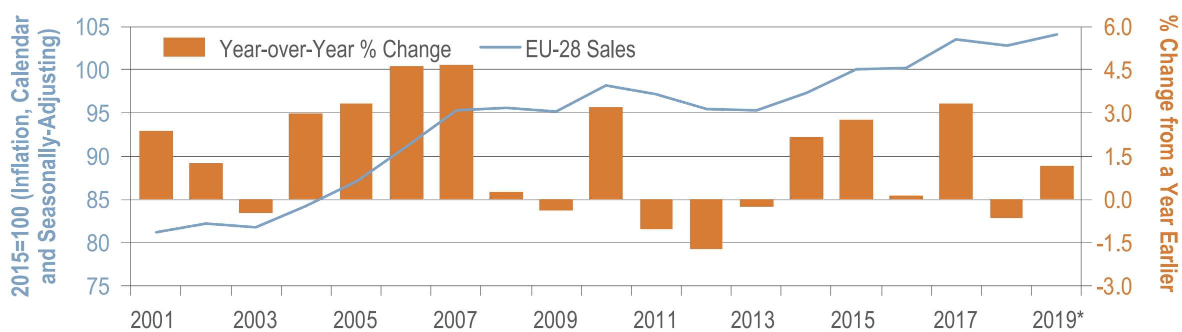
EU Sales of Textiles, Clothing, Footwear and Leather Goods Rebound in 2019



* FDRA forecast
Source: Eurostat

U.S. footwear imports higher in 2019, but tariffs *much* higher

Owing to robust consumer demand for footwear, the volume and value of U.S. imports are set to rival records in 2019, but landed costs are poised to climb to uncharted highs also, propelled by Trump tariff hikes. The *volume* of shipments over the first nine months of the year are up 2.9%, with full-year shipments poised to challenge the 2015 record of nearly 2.5 billion pairs. The *value* of footwear imports so far in 2019 are up an even larger 4.3%, with the dollar value of annual shipments also set to rival the 2015 record of $27.2 billion.

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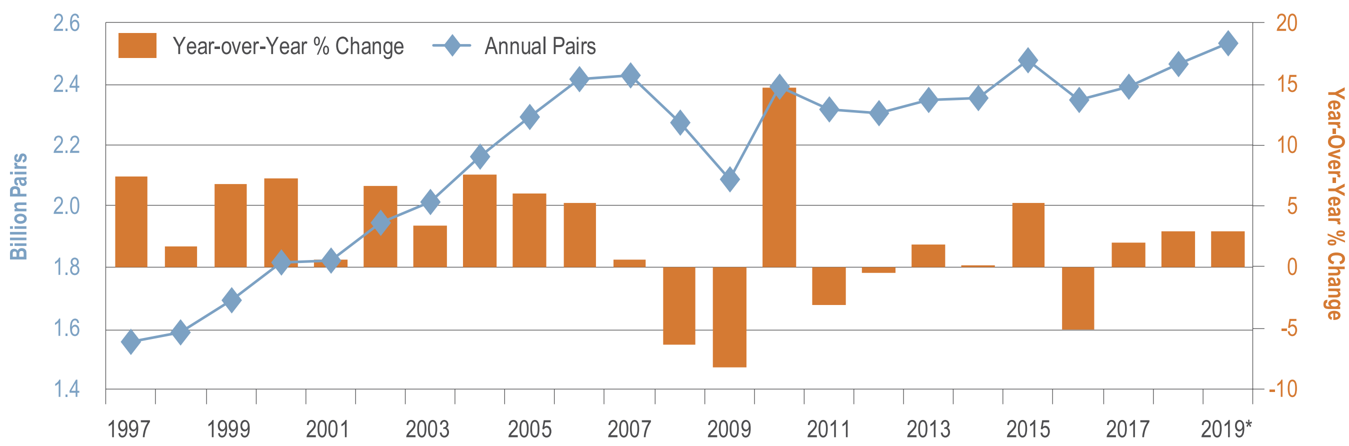
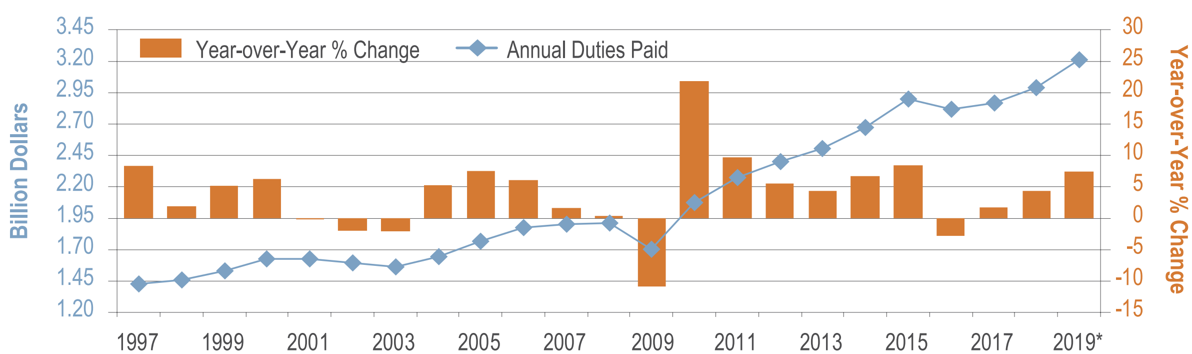
Volume of U.S. Footwear Imports to Climb to a Record in 2019



* FDRA forecast

With the *value* of imports rising faster than the *volume*, the average unit cost of shipments so far this year also is higher. In part, the cost increase comes from surging tariff rates from the U.S./China trade war. FDRA estimates full-year tariffs on footwear imports will rise to an unprecedented $3.2 billion, higher nine of the last ten years. What's more, in the absence of any cessation in the trade war, FDRA looks for these tariffs to climb even higher well into 2020, once the final two tranches of tariffs against footwear from China are fully implemented. Unless, of course, the phase one agreement is reached.

Duties Paid on U.S. Footwear Imports to Jump to a Record in 2019



* FDRA forecast

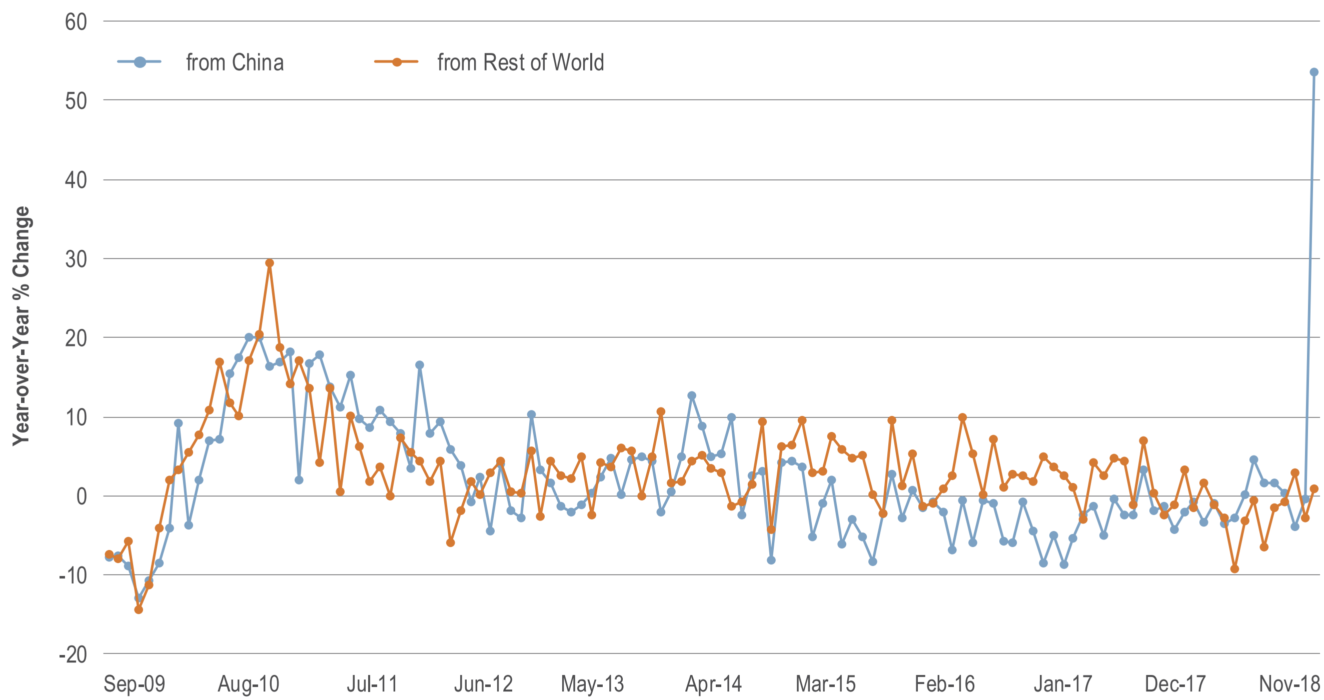
Source both charts: USITC

The Trump administration's 4th tranche against imports from China went into effect September 1, also known as List 4a, and footwear importers and retailers have already witnessed a dramatic surge in duties per pair, with the likelihood that tariffs will surge to a record in 2019.

Make no mistake: Trump tariffs behind rocketing duty costs

After the Trump administration's 4th tranche against imports from China went into effect September 1, also known as List 4a, footwear importers and retailers have already witnessed a dramatic surge in duties per pair, up a record 31.3% in September from a year earlier. Upon closer inspection, the average duties per pair from China rocketed an eye-watering 53.6% in this latest month, while the average duties per pair from the rest of the world rose a tepid 0.9%. This first month's hike is raising the likelihood that tariffs will surge to a record in 2019 as discussed earlier.

Duties per Pair Surge in September... but only from China

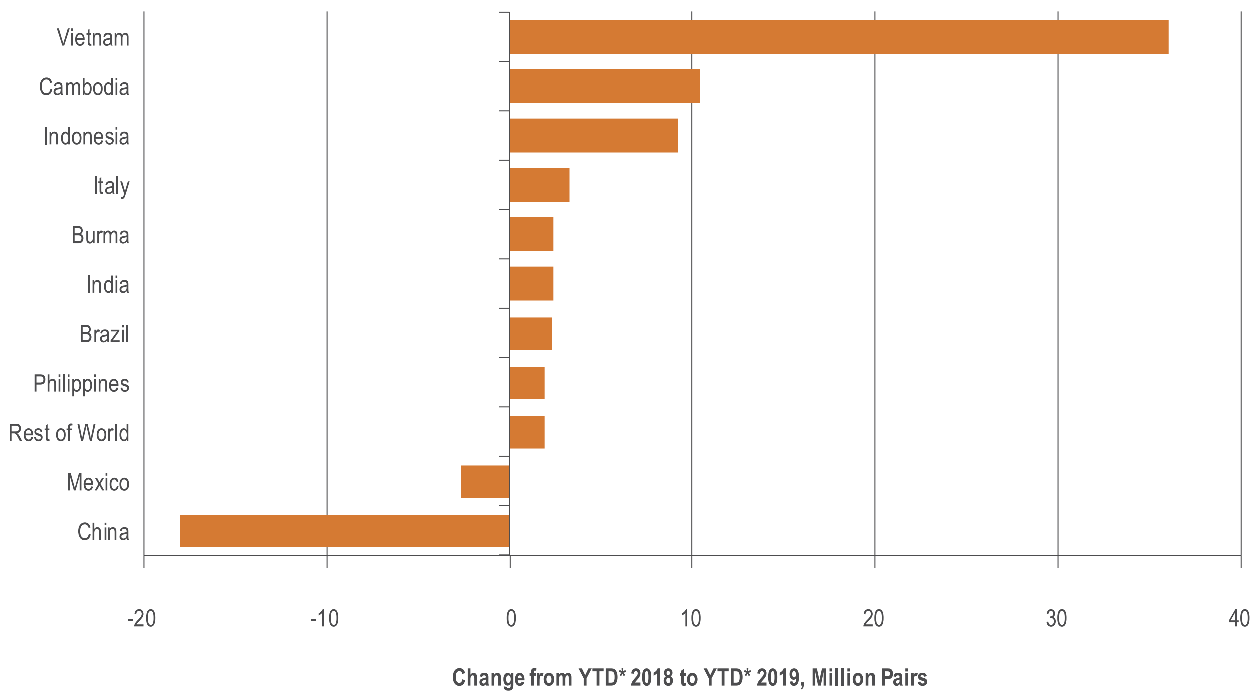


Source: USITC

On the surface, U.S. imports of footwear have been relatively flat in recent years. And 2019 promises to continue the trend, with shipments perhaps rising to challenge the 2015 records. But under the surface of footwear sourcing is the continuing shift to Vietnam as a growing powerhouse origin. While China remains—by far—the largest footwear supplier to the U.S. market, Vietnam's gradual ascent has been undeniable. Over the last decade China's share of U.S. footwear imports shrank from a record 76% and is poised to contract to a 21-year low of 51% in 2019. The lost share has been captured almost entirely by Vietnam, whose share over the same period jumped from 7.8% to 25.0%. Perhaps this long-term evolution is more impressive when viewed more closely, that is year-over-year. Shipments in 2019 have grown from most key suppliers, albeit modestly... +/- 5 million pairs. But shipments from Vietnam to America are up nearly *36 million pairs*, far overshadowing changing shipments from all other suppliers and clearly taking share from China.

China remains by far the largest footwear supplier to the U.S. market, while Vietnam's gradual ascent has been undeniable.

Vietnam Accounting for most of Growth in 2019 U.S. Footwear Imports



Source: FDRA calculations based on USITC data

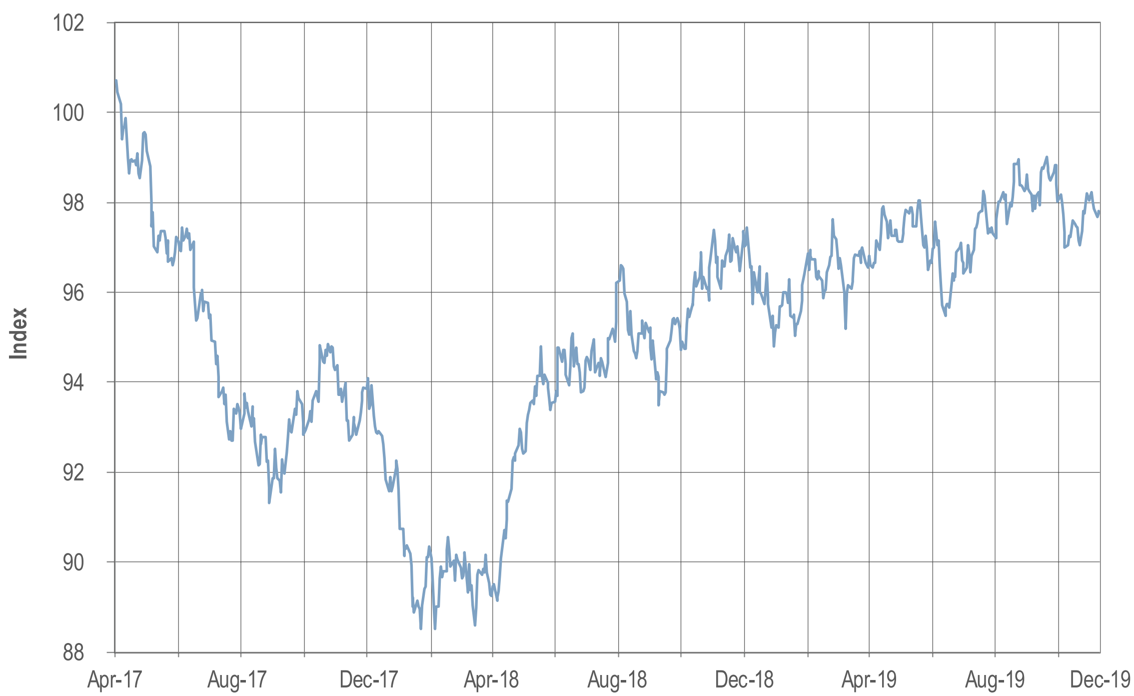
Each month FDRA shares key pricing drivers and trends for a range of commodities and currencies impacting the footwear supply chain here, helping members anticipate the outlook for these markets. Periodically through the year, FDRA shares more in-depth discussion and forecasts into these markets as conditions warrant.

Policies and prospects for the dollar

Of course, footwear manufacturing and distribution involves a wide range of materials and commodities, along with exposure to foreign currency fluctuations. These materials can include natural and synthetic rubber and leather, foam cushioning materials, nylon, polyester, and canvas, as well as polyurethane and plastic compounds, among others. Exposure to volatility in prices for these commodities and currencies can risk a footwear company's profitability, so anticipation of and the ability to hedge against this volatility are key.

Perhaps no other factor impacts costs involved in global footwear manufacturing and sourcing more than the value of the dollar, both as the key denomination for many commodities traded globally and as a global currency. The dollar remains elevated if relatively flat over the last few months, despite the Federal Reserve cutting its benchmark rate three times in three months, a move that typically weighs on the dollar. Even after these cuts, the Federal Funds rate remains relatively high compared with negative rates overseas, helping support the dollar against other currencies, particularly the euro and yen. Following the last rate cut on October 30, the Federal Reserve's chair Jerome Powell said he sees "A sustained expansion of economic activity, a strong labor market, and inflation near our symmetric 2% objective as most likely," hinting to congress there will be no more rate cuts this year. What's more, the Fed historically has been hesitant to adjust interest rates in an election year, more evidence that the dollar may not be depressed by further rate cuts anytime soon. Accordingly, a still-strong dollar is likely to continue to weigh on prices for U.S. imports and commodity prices, a welcome prospect for footwear retailers that have had little opportunity to raise prices appreciably recently.

U.S. Dollar Index Nearby Futures near a 30-Month High



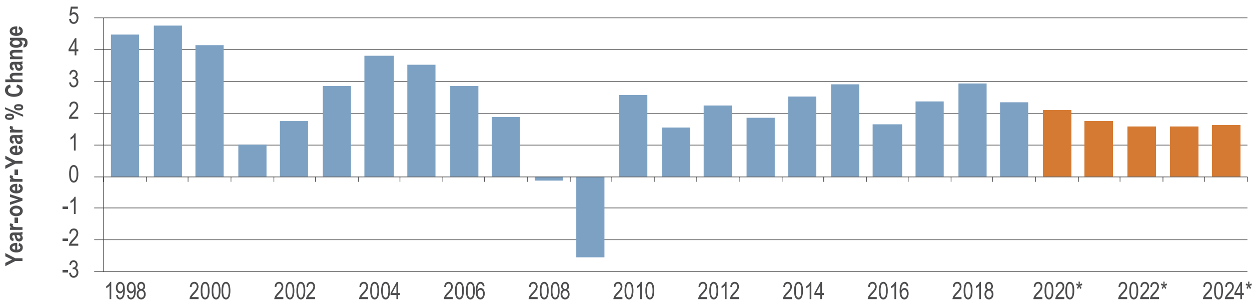
Source: ICE Futures U.S.

U.S. economy lets the good times roll... but for how much longer?

At more than ten years and counting, the American economy has enjoyed its longest streak of growth since 1854, which is as far back as economists have attempted to date business cycles. While the streak is welcome, GDP growth has been subdued—not surpassing 3% for any calendar year—and uneven, with roughly half of GDP growth from 2009–2015 going to the top 1% of households. After slowing sharply in the last three quarters of 2018, the pace of global economic activity remains weak in 2019, and rising trade and geopolitical tensions have increased uncertainty about the future. The IMF sees U.S. economic activity continuing to slow the next few years before levelling out at a tepid 1.6% in 2022–2025. FDRA's forecast is a bit more downbeat, echoing similar outlooks from the New York Fed, JPMorgan Chase & Co. and others. On balance, with the current expansion quite long in the tooth, the outlook for U.S. GDP growth remains precarious with risks tipped to the downside.

The American economy has enjoyed its longest streak of growth since 1854.

U.S. Economy Posts Tenth Straight Year of Expansion, but Slower Growth Ahead

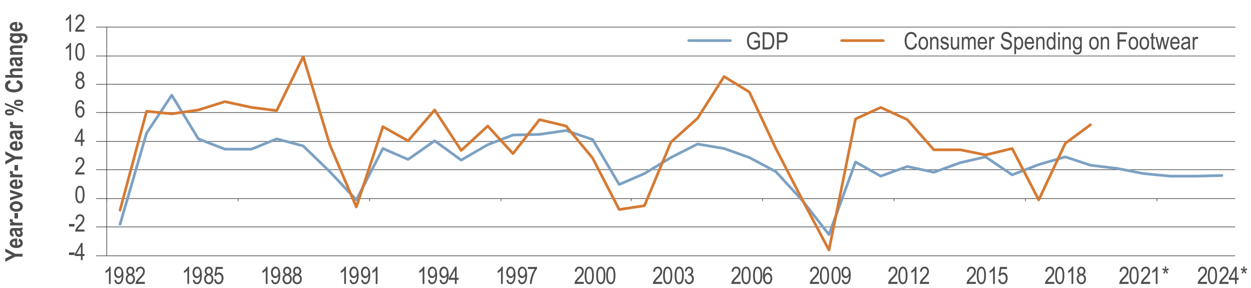


*Sources: Bureau of Economic Analysis & *IMF forecasts*

If growth slows, will a sinking tide lower all ships?

With consumer spending accounting for roughly 70% of economic activity in the U.S., a slowing economy typically implies flagging consumer demand. In turn, a more sated consumer may curb spending—particularly discretionary spending—across a range of categories including footwear. While the accompanying graph shows year-to-year changes in footwear spending typically are more volatile than changes in GDP, a sinking tide tends to lower all ships. On balance, prospects for slower growth ahead are likely to translate into moderating demand for footwear, a key issue with unwelcome repercussions across the footwear supply chain.

Gains in U.S. Consumer Spending on Footwear may Ease as GDP Growth Slows



*IMF forecasts

Sources: U.S. Bureau of Economic Analysis & IMF

Keep up with industry business and consumer trends with Shoe-In Show

FDRA's Shoe-In Show is a weekly podcast of news, views, and interviews with industry players. The footwear industry is in an age of constant change—from how we design and produce footwear to how we market and sell shoes to consumers around the world. Old business models are being shattered and remade in ways that cannot be explained in 140 characters. That's why we started this show—to have in-depth conversations about the business of footwear with the people actually designing, making, marketing, and selling shoes.

Our goal is to pull back the curtain and get industry leaders to open up and give an insider look at the industry and their businesses. Listeners will hear amazing personal stories and unique approaches to current challenges facing the industry, as well as best practices, trends, and tips from experts and executives.

Join co-hosts Matt Priest and Andy Polk each week as we have in-depth and dynamic conversations about the business of footwear, and probably have a laugh while you're at it. Visit www.shoeinshow.com to listen.

The footwear industry's weekly podcast featuring executives and experts

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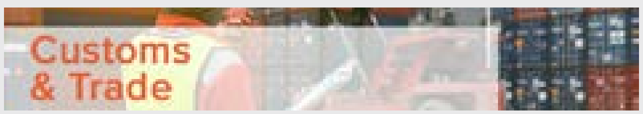
2020 Professional Development and Events

Events posted throughout the year at **fdra.org/events-and-training**.

Make sure you're active in FDRA Working Groups



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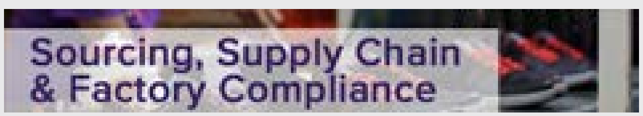

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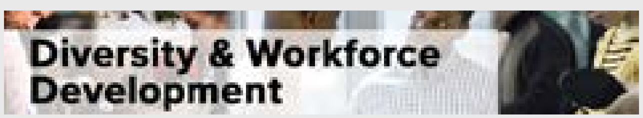

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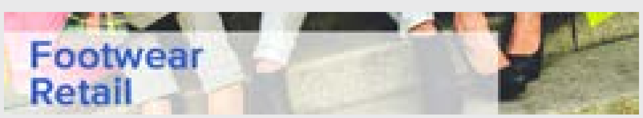

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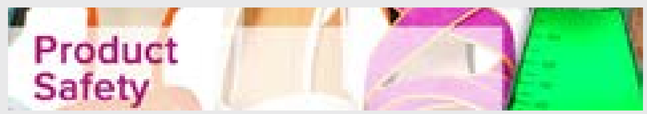

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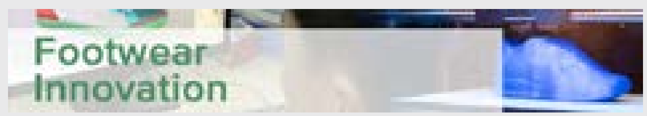

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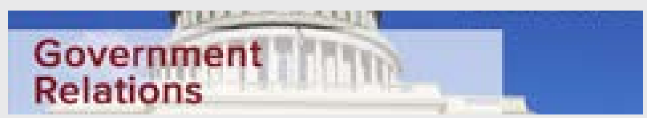

fdra.org/govrelationswg

Keep up-to-date on footwear business trends each week on FDRA.org