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Special Analysis

2Q Retail Update

Key Takeaways

- Value and digital leaders outperformed: Retailers like Walmart, Costco, and TJX saw strong gains driven by value positioning and e-commerce growth, while traditional and discretionary-heavy players lagged.
- Macroeconomic headwinds persist: Unpredictable tariff policy has created business uncertainty, cautious consumer spending and expected higher inflation.
- Market bifurcation widened: Retail winners are scaling through digital investment and capex, while weaker players continue to lose ground amid declining traffic and profitability.

	Comps	Sales Change	Δ Gross Margin (bps)	Inventory Change	Quarter-End Date
U.S.					
Walmart	4.8%	4.8%	10	3.8%	7/31/25
Target	-1.9%	-0.9%	-130	2.2%	8/2/25
BJ's Wholesale	2.3%	3.4%	20	-1.7%	8/2/25
Costco	6.4%	8.1%	10	-2.9%	8/31/25
Dollar General	2.8%	5.1%	120	-5.6%	8/1/25
Best Buy	1.6%	1.6%	-20	1.9%	8/2/25
Kohl's	-4.2%	-5.0%	30	-5.0%	8/2/25
Macy's	1.9%	-2.5%	-80	-0.8%	8/2/25
Gap	1.0%	0.1%	-140	8.9%	8/2/25
Urban Outfitters	5.6%	11.3%	110	15.1%	7/31/25
Abercrombie	3.0%	6.6%	-230	9.9%	8/2/25
TJX	4.0%	6.9%	40	13.9%	8/2/25
Ross	2.0%	4.6%	-70	4.7%	8/2/25
Academy	0.2%	3.3%	-	16.2%	8/2/25
Dick's Sporting Goods	5.0%	5.0%	40	7.1%	8/2/25
Home Depot	1.0%	4.9%	-	7.7%	8/3/25
Lowe's	1.1%	1.6%	30	-3.0%	8/1/25
McDonald's	2.5%	5.4%	-	19.6%	6/30/25
Chipotle	-4.0%	3.0%	-40	13.6%	6/30/25
Bloomin'	-0.1%	0.3%	-20	-22.9%	6/29/25
Kroger	3.4%	0.1%	60	3.0%	8/16/25
Albertsons	2.8%	2.5%	-60	5.4%	6/14/25
Amazon	N/A	13.3%	170	19.7%	6/30/25
Wayfair	N/A	5.0%	-10	14.1%	6/30/25

Mass Merchandisers

The broader mass sector posted solid 5% comps, continuing to be led by the value leaders, while Target lagged even more than normal due to recent consumer boycotting. Walmart U.S. comps rose 4.6% and Sam's Club comps were +5.9% ex-fuel, with continued share gains across income cohorts and strong consumables pull. BJ's delivered +2.3% ex-fuel, supported by healthy transaction volume and membership growth. Costco's U.S. comps (ex-fuel) advanced 5.1%, with e-commerce up 13.5% on strength in big-ticket categories. Target comps remained negative (—1.9%), though digital grew +4.3%, one of the few bright spots in an otherwise pressured quarter. The biggest news was the leadership change announced: Target veteran, Michael Fiddelke was named as the Company's next CEO, set to take the helm at the start of FY26. Omnichannel execution remained a key theme. Walmart U.S. e-commerce grew 26% with improving unit economics, including a profitable consolidated e-commerce business. One-third of store deliveries were made in under three hours and over 20% in under 30 minutes, underscoring consumer demand for speed and convenience. BJ's digital sales rose 34% on strength in curbside pickup, BOPIC, ExpressPay and same-day delivery. Costco also posted double-digit online growth, led by jewelry, appliances, and home categories.

Dollar stores benefited from trade-down activity and lapping Family Dollar closures in 2024. Dollar General posted +2.8% comps with growth across every major category and increasing penetration among middle- and higher-income households. Management reiterated its strategy to hold prices within 3 to 4 points of mass competitors while maintaining its $1 price tier on key items. Dollar Tree delivered +6.5% comps, aided by broadening appeal among higher-income shoppers; the Company highlighted progress in rolling out its multi-price 3.0 format (now over 4,240 stores) and announced an Uber Eats partnership. The Family Dollar divestiture, completed in early July, frees the Company to reinvest in its higher-return formats. Five Below comps rose 12.4%, but management flagged that tariffs would weigh on 3Q margins by roughly 160 bps. Ollie's reported a very strong 2Q25, with sales up 17.5%, supported by 88 new stores (17%-unit growth) in operation and 5% comp growth. Management raised its FY25 store opening target to 85 (vs. 50 in FY24) and sales guidance. In 1H25, 54 new stores were opened.

Tariffs were the key swing factor across earnings calls. Walmart leaned into thousands of rollbacks not only to maintain unit growth but also to reinforce its value positioning and brand perception as the low-cost leader, highlighting varying elasticity across income cohorts. Costco emphasized its ability to mitigate cost pressures through sourcing and private-label strength. Dollar General noted low direct import exposure, though some price pass-through is occurring. Dollar Tree acknowledged tariffs as a meaningful headwind but said its "five levers" (sourcing, mix, pricing, merchandising, and supply chain efficiencies) are helping offset much of the impact, allowing the company to reaffirm its outlook assuming current rates hold. Five Below was more explicit, guiding to an unmitigated tariff drag in 3Q.

Overall, the consumer backdrop remains bifurcated. Value and convenience continue to attract both lower-income households under pressure and higher-income households seeking value, visible in the widening income mix at the dollar chains and continued momentum at clubs. With back-to-school complete and holiday ahead, the sector looks poised to remain two-speed: value-focused big-box and club players sustaining momentum, while discretionary-heavy banners like Target continue to struggle. The key watchpoints for 2H25 will be any escalation of tariffs beyond current levels, consumer discretionary elasticity into holiday and labor-related cost pressures that remain in focus.

Department Store & Off-Price Apparel

In 2Q25, the department store sector continued to show a clear divergence between off-price and traditional department stores, shaped by shifting consumer behaviors and economic pressures. Off-price chains such as TJX Companies, Ross Stores and Burlington Stores reported strong performances, with TJX achieving 6.9% YoY growth and a 4% rise in comparable sales, Ross posting a 4.6% sales gain and 2% comps gain, and Burlington seeing a 10% increase in sales and a 5% rise in comps. This robust performance underscores the resilience of the off-price model, as these retailers continue to attract cost-conscious consumers seeking brand-name merchandise at discounted prices.

Traditional department stores faced challenges, although top-line trends did improve in 2Q. Macy's net sales fell 2.5% from store closures, while comps came in a better than expected 1.9%. This was the strongest comp performance in 12 quarters, led by growth at Bloomingdale's and Bluemercury. However, the Macy's banner comps were also positive, up 1.2%, leading management raise its FY25 sales guidance. Kohl's sales remained in the red, down 5%, though the trend is improving.

Consumer spending patterns highlighted disparities across income levels. High-income consumers continued to drive retail growth, with 65% planning to maintain or increase spending during the holidays (McKinsey), while low-income households reduced expenditures due to rising costs in housing, utilities, and groceries, as well as stagnant wage growth. Compounding these pressures, the introduction of new tariffs in 2025 has raised the U.S. effective tariff rate to ~20%, the highest since 1933, impacting input costs for retailers, especially those sourcing from China and Vietnam. Adapting supply chains and pricing strategies to navigate tariff pressures will be crucial to sustaining profitability.

Overall, the performance gap between off-price and traditional department stores highlights the rising importance of value-oriented offerings. Retailers targeting lower-income shoppers who are caught between the value of off-price competitors and higher-end formats like Nordstrom and Bloomingdale's are most exposed to further challenges (e.g., JCPenney and Kohl's).

Apparel

Tariffs weighed heavily on profitability across the specialty apparel sector in 2Q25, as companies reported millions in added import costs alongside diverging sales trends. Performance split sharply between outperformers and retailers struggling to sustain momentum. Urban Outfitters led with 11.3% sales growth and a 5.6% comp increase, followed by Abercrombie & Fitch with 6.6% revenue growth and comps up 3%. By contrast, Gap's $3.72 billion in revenue was flat YOY with comps up just 1% and American Eagle's comps fell 1% on mid-single-digit pricing pressure. Lower-income-focused players Cato Fashions and Carter's, though challenged overall, reported improved same-store sales of 9% and 2.2%, respectively.

Most companies issued cautious guidance for 2H25, citing ongoing macro uncertainty and tariff exposure. Abercrombie cut its FY25 profit outlook by 170 bps, citing $85 million in added tariff costs for the remainder of FY25. Lululemon incorporated a $240 million gross profit hit into its forecast, while Victoria's Secret doubled its tariff estimate to $100 million and warned of an operating loss in 3Q25. Gap projected $150 million to $175 million in additional costs, and American Eagle forecasted $20 million in 3Q and $40 million to $50 million in 4Q. Both Gap and American Eagle also highlighted higher inventory costs, underscoring the mounting margin pressures driven by tariffs. Off-price retailers fared better, with TJX reporting a flat merchandise margin and Burlington reporting merchandise margin expansion, reflecting the strength of their flexible sourcing models.

Despite tariff headwinds, signs of resilience are emerging in the apparel industry as supply chains adjust. Off-price remains the sector's bright spot, while specialty chains are bifurcated, with leaders such as Abercrombie and Urban Outfitters on one side and underperformers like Gap, American Eagle and Carter's on the other. To offset margin pressure, companies are shifting sourcing, renegotiating with vendors and refining pricing strategies. Those able to balance pricing power with supply chain flexibility appear best positioned to capture share once the environment stabilizes.

Restaurants

The restaurant sector remains under pressure from slowing traffic and transactions as concerns about weakening macroeconomic trends and tariff-driven inflation have pushed customers, in particular lower-income customers, to reduce outside food spending and increase cooking at home. While restaurant chains broadly continue to raise menu prices to pass on their own inflationary costs, companies are also relying on increased marketing and promotions, including LTOs and value offerings, to improve their brand positioning and win market share in a competitive environment. Menu innovation and expanded loyalty programs have also taken on importance in encouraging lapsed customers to return and driving repeat visits. Results in 2Q were mixed across categories and concepts. McDonald's (2.5%) and Burger King (1.3%) flipped back to positive comps, while Wendy's (-3.6%), Starbucks (-2%), Chipotle (-4%) and Jack in the Box (-7.1%) remained negative. Some QSR/Fast Casual competitors saw comps weaken sequentially from 1Q but stay in the black, including CAVA (2.1%) and Taco Bell (4%). In the full-service category several larger chains reported solid mid-single digit comp growth, including Darden's Olive Garden (5.9%) and LongHorn Steakhouse (5.5%), Texas Roadhouse (5.8%), and Dine Brands' Applebees (4.9%), with the latter seeing positive traffic for the first time since 1Q23 that management attributed to a new 2 for $25 value platform and expanded marketing. Similar strategies were less successful at the sister banner IHOP (-2.3%), and at other struggling operators such as Red Robin (-3.2%) and Denny's (-1.3%).

Electronics

The consumer electronics industry experienced modest improvement in 2Q, driven by an uptick in demand for smaller devices such as mobile phones and laptops. However, the sector remains under pressure as lagging technological advancements are being met with headwinds from tariffs, inflation, and the resumption of student loan payments all weighing on consumer spending power. Best Buy's recent results highlight these broader trends, with sales and comparable sales both rising 1.6%, led by gaming, computing and mobile devices, though this was partially offset by ongoing weakness in larger-ticket categories like home theater, appliances, tablets and drones. In contrast, ODP's performance remains challenged; its most recent quarter saw sales and comps decline 7.6% and 5%, respectively. The Company's business solutions division, its primary area of focus, also recorded a 6.3% sales drop, reflecting softer business-to-business demand for furniture, technology and supplies. Despite the ongoing near-term challenges, retailers continue to expect a gradual recovery, driven by replacement demand as older devices phase out, upcoming holiday promotions, and growing interest in AI-powered products. Still, meaningful growth in the sector will likely remain limited until macroeconomic conditions improve and innovation cycles gain momentum.

Home Improvement

In 1H25, the home improvement sector experienced steady but modest growth, with interest rates and inflation still weighing most heavily on the discretionary DIY segment. Larger remodeling projects remain under pressure, while smaller jobs and Pro demand helped stabilize results. Home Depot reported 2Q sales growth of 4.9% year-over-year, with U.S. comps up 1.4% and online sales rising more than 10%, reflecting ongoing digital adoption and fulfillment improvements. Lowe's also turned in a positive comp quarter, supported by strength in Pro and online sales, along with weather-related rebuild activity. However, discretionary DIY spending remains sluggish, limiting overall momentum. Specialty players are showing early signs of recovery: Floor & Décor posted positive comps of 0.4% for the first time since 4Q22, while The Tile Shop's negative comps trend is moderating, improving from -5.8% in 4Q24 to -4.1% in 1Q25 and -3.5% most recently.

At the retailer level, the competitive focus has shifted firmly toward the Pro contractor market, where both Home Depot and Lowe's have pursued acquisitions to expand their reach. Home Depot closed its acquisition of SRS Distribution earlier in the year and added GMS Inc. in June 2025 for approximately $5.50 billion, significantly broadening its building materials distribution platform for "complex Pro" customers. Lowe's countered with the April acquisition of Artisan Design Group, adding design, distribution, and installation capabilities in interior finishes, followed by an August agreement to acquire Foundation Building Materials for $8.80 billion, further deepening its penetration into commercial and contractor channels. Beyond the two leaders, the sector remains positioned for further consolidation, with ongoing M&A activity likely among distributors and specialty retailers. At the macro level, the Federal Reserve made its first interest rate cut since late 2024, trimming the target federal funds rate by 25 bps in September 2025 to a new range of 4.00%-4.25%, down from 4.25%-4.50%. The Fed has signaled two additional rate cuts remaining in 2025, reflecting concerns over a slowing labor market and above-target inflation that is proving more persistent than expected. These shifts in monetary policy are likely to have meaningful implications for home improvement, as lower borrowing costs could help spur activity in larger renovation projects and new construction, improving affordability, though mortgage rates are expected to decline only gradually, and high costs and economic uncertainty may continue to temper consumer willingness to invest in big-ticket home improvements.

Sporting Goods

After three years of sliding sales and margins, sporting goods retail continued to rebound in 2Q, with most retailers reporting positive growth. Gains were supported by most categories including soft goods, though outdoor categories such as hunting remained weak.

Academy posted its first positive comp quarter since 2021, up 0.2%, while pulling forward inventory purchases in anticipation of tariffs—driving a 16% YoY increase. Management slightly raised the low end of its sales guidance and now expects FY25 comps between —3% and +1%. The Company remains on track to open at least 20 new stores this year.

Ahead of its merger with Foot Locker, Dick's reported another solid quarter, with comps up 5% and continued online strength. Foot Locker, by contrast, saw sales decline 2.4% from store closures and international weakness, partly offset by 1.4% comp growth in North America. Dick's took a more cautious outlook for 2H25, citing tariff headwinds. Management believes it can revive Foot Locker's struggling mall-based business by leveraging scale, strengthening vendor relationships, and improved apparel execution.

Sportsman's Warehouse delivered its second consecutive quarter of positive sales, with comps up 2% in 1H25, and guided for at least flat FY25 sales with modest EBITDA improvement—enough to support a potential credit upgrade from its current E2 rating. Like peers, it also pulled forward inventory, which is expected to unwind in 2H25.

Big 5 Sporting Goods remained an outlier, with 2Q sales down 7.5% from store closures and a 6% comp decline. Worldwide Golf's takeover of Big 5 is expected to close in 2H25, but the companies have yet to outline a strategic direction. Store level investments are needed and we speculate that Big 5 may shift toward more focused assortments, including golf or other specialty sporting goods.

Overall, while 2Q results point to broad stabilization, the durability of the rebound remains uncertain. Tariff pressures and a more cautious consumer backdrop could quickly erode recent gains, leaving margins vulnerable. For credit investors, the sector's improvement looks more cyclical than structural, with only the strongest operators likely to sustain momentum into 2H25.

Grocery

In 1H25, grocery consumers remained under pressure from elevated food costs, with many continuing to trade down to private label products and embrace value-focused retailers. Private label sales grew 4.4% year-over-year in the first half of 2025, reaching an annualized pace of $277 billion and widening the gap over national brands, which saw only modest growth of about 1%. The improvement in store brand quality, particularly in refrigerated, frozen, and fresh categories, has made private label an increasingly attractive option for budget-conscious shoppers. Online grocery also maintained strong momentum, with U.S. e-commerce grocery sales climbing nearly 28% year-over-year in June to $9.8 billion. Consumers are increasingly drawn to digital-first options for their convenience, efficiency, and competitive pricing, with delivery and curbside services continuing to gain traction. While inflationary pressures are easing in some categories, shoppers remain highly price-sensitive, reinforcing trends toward promotions, value packs, and store brand alternatives.

At the retailer level, consolidation and expansion remain central themes. Dealmaking has shifted to midsized players, highlighted by C&S Wholesale Grocers' recently completed $1.77 billion acquisition of SpartanNash. We expect deal volume to grow going forward. Meanwhile, Aldi continues its aggressive growth strategy, with plans to open more than 225 stores in 2025 and to convert roughly 220 Winn-Dixie and Harveys locations by 2027, positioning its U.S. footprint at about 2,600 stores by year-end. Walmart is similarly pushing ahead with plans to add 150 new stores over five years, while Sprouts, Publix, and Lidl remain active in selective expansions. The sector overall is in growth mode, but retailers, including Kroger are pruning underperforming units to remain competitive. With private label growth accelerating, online grocery surging, and discount chains expanding aggressively, the grocery landscape in 2025 is increasingly defined by scale, efficiency, and consumer demand for value.

Online Retailers

Online shopping remains a key focus and driver of retail growth as both pure-play e-commerce players and traditional retailers continue to double down on digital investments. With discretionary categories still soft, most online gains again came from essentials and convenience-driven purchases. In 2Q25, U.S. online sales rose roughly 5% YOY and represented 16.3% of total retail sales, up from 16.1% in the prior quarter (U.S. Census data).

Walmart reported a 24% increase in online sales, with profitability supported by improved delivery efficiency and an expanding omnichannel reach. Roughly one-third of store deliveries were fulfilled in under three hours, underscoring consumers' growing appetite for speed and flexibility. BJ's Wholesale posted a 34% digital sales gain (52% on a two-year stack) fueled by strong adoption of curbside pickup, BOPIC, ExpressPay and same-day delivery. Costco delivered 13.6% online growth, highlighting consistent strength across jewelry, home, and appliances, while membership engagement and digital traffic remained key contributors. Target's digital sales grew modestly but continued to be weighed by softer discretionary demand, as management emphasized ongoing investment in store-based fulfillment and Drive-Up service enhancements to restore momentum. Even the dollar segment has taken notice with Dollar Tree and Dollar General expanding delivery access through partnerships with Uber Eats and DoorDash as both retailers work to strengthen convenience and engagement across their platforms.

Amazon continued to focus on expanding selection, lowering prices, and improving delivery speed to strengthen its customer value proposition. Paid unit growth rose 12% YOY, reflecting steady demand for everyday essentials, which accounted for roughly one in every three items purchased. Chewy reported 2Q net sales growth of 8.6%, exceeding its 7% to 8% projection, as active customers rose 4.5% to 20.9 million. Autoship sales increased 15%, reaching 83% of total revenue and outpacing overall growth, reflecting continued strength in customer acquisition, retention and spending. Net sales per active customer rose mid-single digits to $591 million.

Overall, online retail growth in 2Q25 reflected continued strength in value, essentials and convenience-oriented shopping. Retailers with fulfillment networks in place and scaled omnichannel platforms remain best positioned to capture share as online penetration deepens heading into 2H25.

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