

retailthinktank

KPMG | Ipsos

Annual.
review

2020

KPMG/Ipsos Retail Think Tank
Review of 2020



Non-essential goods' retailers ramped up their on-line services and home deliveries added to the cost burden

Quarter 1 COVID-19 obliterates hope of improved retail health for the foreseeable future

There was plenty to look forward to, as we launched into 2020 after 5 quarters of deteriorating retail health on the trot and a modest lift in GDP of +1.4% in 2019. The conclusive outcome of December's general election, the claim that a Brexit deal was "oven ready" and record levels of employment just shy of 33 million all combined to breathe apparent political and economic certainty into the lungs of the nation and revive hope for better times to come.

Despite the mildly positive general outlook, the KPMG/Ipsos Retail Think Tank (RTT) did not anticipate an immediate bounce back to retail health in Quarter 1 2020. Members were particularly concerned about the 5 months of falling average weekly earnings causing consumer

demand to waver going into the new year and the thin margins that retailers were making. It therefore expected its Retail Health Index (RHI)¹ to flatline in Quarter 1 vs Quarter 4 2019. Total sales growth figures² of +0.4% in January and +0.1% in February appeared to vindicate the projection. Then in March everything changed when COVID-19 became a pandemic, hitting the UK hard.

By the end of the month almost 20,000 cases including Boris Johnson, the Prime Minister, had been confirmed, leading to the first lockdown and closure of non-essential stores from 23rd March. Total sales shrunk by -4.3%³ despite the surge in grocery and on-line sales after the lockdown was announced, as consumers rushed to stockpile basics.

At its April meeting, the RTT acknowledged that the virus' influence had been responsible for downgrading its RHI score in Quarter 1 from its forecast of remaining flat to a decline in health of 3 points, to a new low of 71.

The collapse in non-essential store sales failed to be made up on-line and despite a wave in stockpiling causing grocery sales to surge, this was deemed insufficient to compensate for the loss of demand elsewhere. Both other drivers of the index also suffered. Costs escalated with supermarkets employing thousands of extra workers, non-essential goods' retailers ramped up their on-line services and home deliveries added to the cost burden. Stiff competition put pressure on prices and with it, on margins.

Quarter 2

Retail health hits an all-time low, but pent-up demand offered a lifeline for retailers

The RTT was fearful that COVID-19 would obliterate any hope of improved retail health for the foreseeable future. It forecast that the RHI would drop by a further 9 points in Quarter 2, impacted heavily by the continued lockdown on non-essential stores.

Members welcomed the relief provided by government intervention to fixed costs in the form of a business rate holiday and the employee furlough scheme, they thought that these savings would be outweighed by the additional variable costs working their way through the supply chain in the food sector and from stock write-offs in the non-food sector. In the event the actual RHI score for Quarter 2 plummeted by 10

points to 61, another new low, and a record fall in any quarter since the RHI was established in 2006, some 4 points greater than in Quarter 4 2008, when the financial crisis crashed the economy.

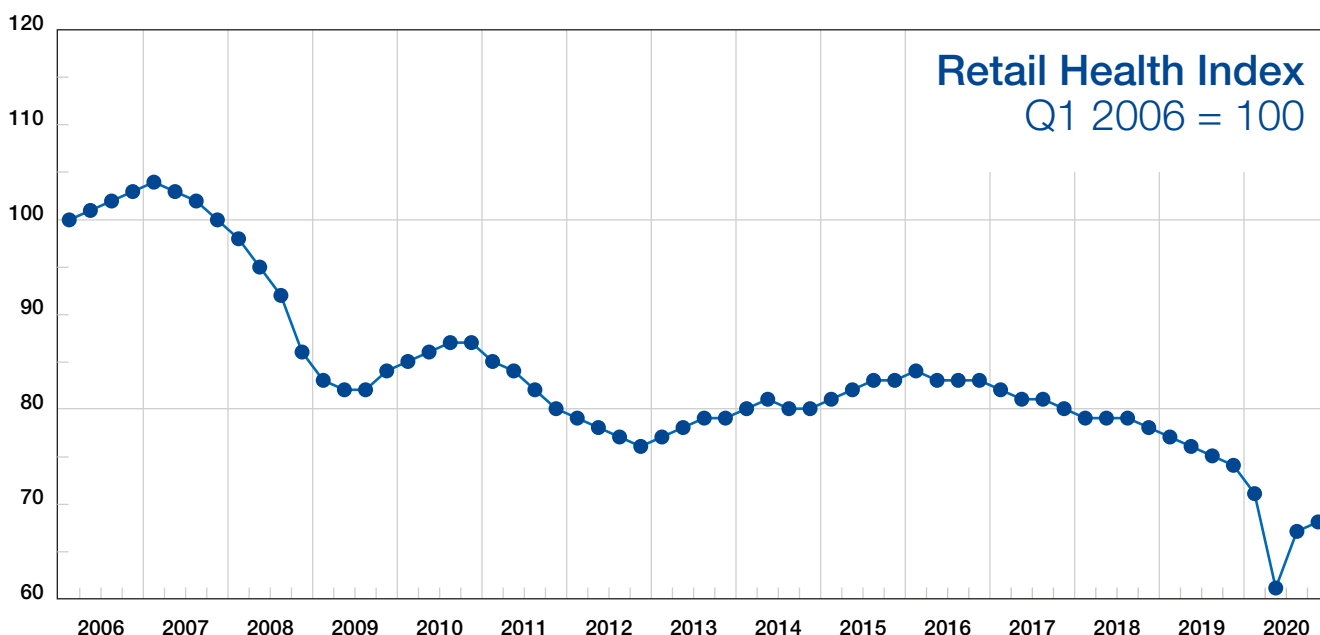
With the protracted lockdown and the announcements of a swathe of non-food retailers including Oasis, Warehouse, Laura Ashley, Debenhams and Cath Kidston filing for administration or notices of intent, the RTT conceded that the sector's health was haemorrhaging badly and was even worse that it had forecast to be at its half way point in the year.

The closure of restaurants and pubs together with the travel restrictions had, however, caused food and beverage consumption

at home to rocket, representing a bit of a bonanza for the grocery sector. This, together with the edict that all non-essential stores in England could re-open from 15th June, provided they met government guidelines on offering a safe shopping environment, gave the RTT cause for some optimism in Quarter 3.

The fact that many people had foregone summer holidays abroad and had not spent as much as they would normally do on travel, hospitality and clothing meant that the households' saving ratio jumped to 27.4% in Quarter 2⁴ (against a run rate of 8%) and this was expected to release some pent-up demand for goods in the months ahead.

On a more cautious note, Members shared some concern over the growing pressures on costs as the furlough scheme was expected to be unwound and rent demands to return. Likewise it believed that margins would become strained in the coming quarter as competition to win a share of the consumer purse would bring heavy price-slashing. Weighing up all these factors, the RTT forecast that the RHI would bounce back by +3 points in Quarter 3.





“Consumers fell back into their stride quicker than expected, eager to return to shopping in stores...”

Quarter 3

Retail health saw a recovery, but the run-up to Christmas would paint a different picture

It transpired that the health of the sector in Quarter 3 was stronger than anticipated by the RTT. The RHI rose by +6 points from Quarter 2 to Quarter 3, lifting it to 67 and recovering over half the ground it lost during lockdown.

Stronger demand played a key part in driving health upwards. Consumers fell back into their stride quicker than expected, eager to return to shopping in stores, as well as continuing on-line, and by the end of September footfall was up to two thirds of the previous year.

The extra money in people's pockets was certainly a key factor for the bounce, but extra incentives such as the cut in stamp duty

also played their part. Homeware and electrical goods, in particular, saw strong growth in sales. Grocery sales continued to fly, notwithstanding the Government's Eat Out to Help Out scheme that ran throughout August.

Besides the strong recovery in demand, Members also recognised the contribution of lowering cost pressures aiding retail health. They conceded that this was partly a function of deferral, care of the Government's furlough scheme and business rate relief, but also rental holidays and movement away from quarterly payments. Many of the costs associated with gearing up the online channel were not considered to be a further drain

to health in the quarter. Margins, too, remained well managed and under control, so had no impact on the state of retail health.

In formulating its thoughts about the outlook for Quarter 4, the RTT was acutely aware that the situation was a very fluid one. The possibilities of a second national lockdown and a No Deal Brexit were both real threats. The belief was that the pent-up demand of the summer would have run its course by Quarter Four and households would be back on its normal spending trajectory, acting as a slightly positive driver of sector health.

Members were conscious that some verticals in the non-food sector were facing a challenging Golden Quarter, particularly formal and occasion wear, but that buoyancy in the grocery sector would counter this. More concern to retail health was the view that costs would begin to creep up, as the various support programmes were due to end and home delivery would ramp up over the holiday season. Overall the RTT projected that the RHI would rise again in Quarter 4, but by only 1 point, well below the recovery enjoyed in Quarter 3.

Quarter 4

Retail health continues to recover, but at a more modest rate

As Members had forecast, retail health in Quarter 4 notched up another point to 68, finishing the year 6 points down on where it had begun. The gain was orchestrated by strengthening demand, particularly in October, after Covid restrictions had been lifted and for food throughout the quarter, especially premium food and drink over the festive period as some consumers were determined to enjoy their Christmas fare, in the absence of “eating out” and normal family gatherings.

The improvement in demand would have been stronger were it not for the introduction of Tier 4 restrictions on 20th December that acted as a major dampener in the final few days before Christmas

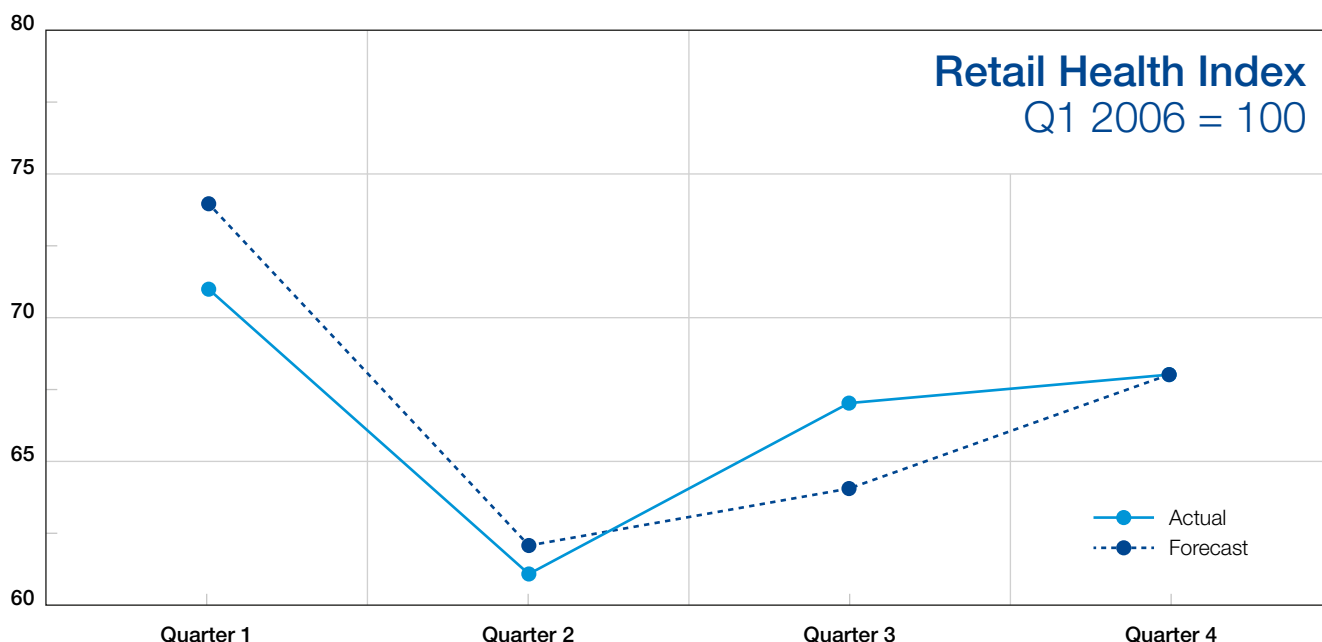
Day. On the upside there was less need for heavy discounting by retailers. Margins held relatively stable across the quarter, despite the tactical use of Black Friday discounts to encourage people to buy early and so avoid the challenges created by last minute spikes in logistics.

In contrast to the previous quarter, costs came under pressure thanks

mainly to the surge in online shopping, created by the second national lockdown, and raising order fulfilment and delivery expense. The RTT was quick to commend retailers for the success they had in ramping up their online services so preventing the website crashes and logistics bottlenecks feared from demand peaking in the golden quarter.

A scarcity of freight containers bringing stock imports into the country, combined with supply chain contingencies, while Brexit negotiations remained in the balance – also contributed to higher costs. Some of the cost savings accounted for in Quarter Three had been attributed to the Government’s business rate holiday, but announcements made by some supermarkets and essential retailers in Quarter Four to pay for some/all of waived business rates removed that relief in the final quarter and beyond into 2021.

“Margins held relatively stable across the quarter, despite the tactical use of Black Friday discounts”



2020 In Summary

Retailing was one of the sectors worst hit by the impact of COVID-19. The 6-point decline in the RHI over 2020 marked the fourth consecutive year of deteriorating health, but the headline drop masks the full story.

Despite the closures of non-essential stores in Q2 and Q4 pulling down demand, the rapid expansion of online sales and the switch in spend from eating out to home-cooking helped counter the loss and consequently demand was not the heaviest drain on the health of the sector over the year.

Both rising pressures on costs and margin were more damaging to retail health than the softening in demand. Weaker demand and strong competition in the non-food sector, especially among fashion retailers, led to heavy discounting which hit margins and overall retail health hard over the course of the year.

Though welcome Government and industry initiatives helped cushion property and people costs, the rapid switch to online operations and investment programmes to make stores and logistics centres safe places to shop and work added significant overall cost burdens.

By the year end, many categories in non-essential retail had had their worst ever performance, while the opposite was true of essentials. Going into 2021, retail is in a phase of deconstruction and re-construction which will ultimately result in its re-definition.

Endnotes

1 The Retail Health Index is an assessment of the state of retail health based on the drivers of demand, costs and margin. The aggregate score is derived from both quantitative and qualitative data (published and otherwise) reviewed by Members. Any change in the score reflects a move from the previous quarter's position.

2 BRC/KPMG Retail Sales Monitor

3 BRC/KPMG Retail Sales Monitor

4 Office for National Statistics

www.retailthinktank.co.uk



About the KPMG/Ipsos Retail Think Tank

Creation of the Retail Think Tank (RTT)

Conceived and created in 2006 by Helen Dickinson, OBE (former Head of UK Retail at KPMG and now CEO of the British Retail Consortium) and Tim Denison Head of Retail Intelligence at Ipsos, the RTT provides an authoritative and trusted window on what is happening in UK retailing and offers thought leadership on key areas influencing the future of retailing. It is now co-chaired by Tim Denison and Paul Martin (UK Head of Retail, KPMG). The intended audience for the outputs of the RTT is primarily retailers, but includes anyone with an active interest in the sector.

Who are we?

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We assess the “health” of the retail sector in the UK

- Traditionally it has proved incredibly difficult to get a true view of the state of affairs of the sector due to the sheer volume of data and large variation in how it is generated and then interpreted.
- We look back at the last quarter and ahead over the next 3 months and consider retail health in terms of its three principal drivers: Demand, Margin and Costs
- We publish the Retail Health Index (RHI) which draws on both qualitative and quantitative data reviewed by the RTT

We write White Papers

- Thought leadership on current topics influencing the retail sector
- Issued quarterly throughout the year
- The 2020 White Papers covered:
 - Our outlook for 2021
 - Online vs physical – is there a level playing field and does it really matter?
 - What retail sectors will emerge stronger and which will be most challenged in the wake of the pandemic
 - Life after COVID-19: the immediate fallout and the long-term implications

Where to obtain further information
www.retailthinktank.co.uk

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