EUROPEAN VALUATIONS

MARKET SECTOR INSIGHTS – JULY 2021

Fashion Market

As the coronavirus pandemic sent shockwaves around the world, the industry suffered its worst year on record with almost three quarters of listed companies losing money.

Global Outlook

McKinsey Global Fashion Index analysis shows fashion companies posted an approximately 90 percent decline in economic profit in 2020, after a 4 percent rise in 2019. The State of Fashion 2021 ("SoF"), a joint report from Business of Fashion and McKinsey & Company, explained, "For the fashion industry, 2020 was the year in which everything changed. As the coronavirus pandemic sent shockwaves around the world, the industry suffered its worst year on record with almost three quarters of listed companies losing money. Consumer behaviour shifted, supply chains were disrupted, and the year approached its end with many regions in the grip of a second wave of infections."

The report also highlighted some of the "silver linings" the industry has seen. "While the crisis has visited a devastating impact on businesses and jobs, it may also have accelerated responses that can lead to positive outcomes. Indeed, many fashion companies have taken time during the crisis to reshape their business models, streamline their operations, and sharpen their customer propositions," stated the report.

Fashion Industry Outlook

The SOF report's predictions for industry performance in 2021 are focused on two scenarios. The first, more optimistic "Earlier Recovery" scenario envisages that global fashion sales will decline by between 0 and 5 percent in 2021 compared to 2019. In this scenario, the industry would return to 2019 levels of activity by the third quarter of 2022.

The second, "Later Recovery" scenario would see sales growth decline by 10 to 15 percent throughout 2021 compared with 2019. In this case, fashion sales would only revert to 2019 levels in the fourth quarter of 2023. In either scenario, the firm expects challenging trading conditions to persist throughout 2021 and for high levels of bankruptcies, store closures and job cuts to continue.

Dynamic E-Commerce Growth

As social distancing and staying home continue to impact consumer behaviour, the primary driver of growth in 2021 will continue to be digital channels. SOF's Earlier Recovery scenario anticipates dynamic digital growth throughout the world in 2021 compared to 2019, with more than 30 percent online growth in Europe and the US and over 20 percent growth in the already highly digitised Chinese market.

In the Later Recovery scenario SOF predicts, "The US would see sales decline by 22 to 27 percent in 2021 compared to 2019, and pre-COVID performance in the country would not return until after 2025. Although significantly impacted, Europe would fare slightly better than the US overall in this scenario, with sales down 14 to 19 percent compared to 2019. However, the European luxury segment would suffer a considerable hit. If new lockdowns were to be implemented and travel restrictions persist, luxury sales in Europe could drop up to 40 percent and only recover to their pre-crisis level by the third quarter of 2023."

Brexit and the Fashion Industry

In February 2021, more than 400 figures from the UK fashion industry signed an open letter to the prime minister warning that post-Brexit red tape and travel restrictions threaten their survival. Many businesses are considering relocating to the EU as a result of the post-Brexit trading challenges.

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According to the latest data from Liv Ex, Bordeaux's trade share by value fell to In response, a government spokesperson said, "We are working closely with businesses in the fashion industry to ensure they get the support they need to trade effectively with Europe and seize new opportunities as we strike trade deals with the world's fastest growing markets."

"We are aware that some businesses are facing challenges with specific aspects of our new trading relationship with the EU. To this end, we are operating export helplines, running webinars with policy experts and offering businesses support via our network of 300 international trade advisers. This is on top of the millions we have invested to expand the customs intermediaries sector.

Focus on Supply Chain

The supply chain is quickly becoming a way for retailers to offer consumers a differentiated service, but making the supply chain faster, more predictable and cheaper is a difficult triad to manage simultaneously.

As retailers buckle down and prepare for potentially challenging times ahead, supply chain improvements can be a significant growth driver. But rather than just investing in trends like smart packaging in reaction to competitors, retailers would do well to think about accumulating long-term competitive advantages through wider supply chain strategies and also through experimenting and investing in new technologies that will help them stay ahead of the competition.

Overall, trade-related forces are expected to lead to some changes in the fashion industry. Escalating trade tensions are expected to cause international brands to re-examine their sourcing, perhaps to the benefit of countries involved in newly negotiated trade agreements.

UK Retail Sales

According to latest figures from the ONS, retail sales volumes declined by 1.4% between April and May 2021 following a sharp increase in April when retail restrictions were eased; despite the monthly decline, over April and May combined, average total retail sales volumes were still 7.7% higher than in March 2021 and were 9.1% higher than in February 2020 before the impact of the coronavirus (COVID-19) pandemic. The largest contribution to the monthly decline in May 2021 came from food stores where sales volumes fell by 5.7%; anecdotal evidence suggests the easing of hospitality restrictions had had an impact on sales as people returned to eating and drinking at locations such as restaurants and bars.

Non-food stores reported a 2.3% increase in monthly sales volumes in May 2021 with household goods stores (for example, hardware and furniture stores) and "other" non-food stores reporting the largest growth of 9.0% and 7.7%, respectively. The large increase in sales volumes in April, followed by a relatively small fall in May, has resulted in the volume of sales for the three months to May 2021 being 8.3% higher than in the previous three months; there was strong growth in automotive fuel sales and non-food retailers of 19.3% and 17.8%, respectively.

The proportion of retail sales conducted online remains substantially higher than before the pandemic, but in May all retail sectors, with the exception of food stores, reported a fall in their proportions of online sales as consumers returned to physical stores.

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UK Consumer Spending

According to Barclays, overall UK consumer spending in May increased by 7.6%, as consumers continued to return to non-essential retail venues as indoor hospitality has re-opened across much of the UK. Spending on essential items rose 11.4%, the highest year-on-two-year growth reported since before the onset of the pandemic. This was partially driven by 17.7% growth in supermarket spending, but also helped by a continued increase in fuel spend at -3.7% compared to -8.1% reported last month, as consumers were more comfortable travelling further afield to visit friends and family. This comes as nearly seven in ten (68%) say they are comfortable spending time with friends and family outdoors, and six in ten (61%) say they are comfortable doing so indoors.

Spending on non-essential items returned to growth for the first time since October 2020, up 5.8% compared to the same period in 2019, the highest level of growth since pre-COVID. This was driven by strong performance in clothing (+8.5%) and department stores (+8.6%) as consumers hit the high street. Sports & outdoor retailers also saw major growth, up 47%, as Brits geared up for a summer of sport and outdoor activities. While restaurants as well as bars and pubs saw respective declines of 53.2% and 19.4% for the month overall, these were marked improvements on the -74.4% and -67.2% reported in April. In fact, spending in bars and pubs saw a 1.4% growth among 16-24-year-olds, as younger people returned to socialising at the earliest possible opportunity.

EU Retail Sales

In April 2021, the seasonally adjusted volume of retail trade fell by 3.1% in both the euro area and in the EU, compared with March 2021, according to estimates from Eurostat, the statistical office of the European Union. In March 2021, the retail trade volume increased by 3.3% in the euro area and by 3.2% in the EU. In April 2021 compared with April 2020, the calendar adjusted volume of retail trade increased by 23.9% in the euro area and by 22.4% in the EU.

US Retail Sales

US retail sales declined in May 2021, after a stimulus-related splurge in the prior two months, suggesting consumers are starting to shift more of their spending to services as the economy reopens. The total value of retail purchases fell 1.3% in May following an upwardly revised 0.9% gain in April, Commerce Department figures showed recently. While consumer spending is expected to continue strengthening, the pace will probably moderate as enhanced unemployment benefits expire and stimulus checks are spent. A sustained pickup in inflation may also cause consumers to limit discretionary expenditures.

-Economic Impact of Coronavirus-

Undoubtedly, coronavirus is a black swan event – something that happens once in a century. Its spread has left businesses around the world counting costs, with many investors fearing the spread of coronavirus will pose an insurmountable challenge to the economic growth of all major countries across the globe. Almost every industry has been affected, with governments scrambling to somehow arrest the economic decline. Central banks in more than 50 countries, including the US Federal Reserve and the Bank of England have cut interest rates to try to strengthen their economies. Furthermore, most countries have announced unprecedented stimulus packages in the hopes of reviving their economy.

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Effect on Global Demand

Owing to the pandemic, in the first half of 2020, restaurants, cinemas and shops around the world emptied, while flights, road traffic and energy use also fell steeply. Now more than one year later, consumer demand is still much below pre pandemic levels.

The retail industry has been hit hard. Lockdowns in many major economies until the middle of May 2020 and then again at the end of 2020 and the beginning of 2021 with only essential shops being allowed to open has meant huge losses for retailers, leading to many retailers shutting up shop.

It is clear now that the spread of coronavirus has led to a decline in global consumer spending, the heart of global economic activity. Moreover, employee layoffs in various industries are becoming increasingly common, in many cases on a large scale. This might lead to further pullback in consumer spending, at least in the near future, exacerbating the economic impact of coronavirus.

Decline in Optimism

After sounding a note of optimism at the end of 2020, respondents to a recent McKinsey Global Survey are thinking about 2021 with high hopes for economy's prospects. Majorities of executives continue to believe that conditions in their home economies and in the global economy will improve this year. Yet their positivity has moderated since the previous survey; compared with December, smaller shares of respondents now predict that economic conditions will get better.

Regionally, respondents in Greater China have been the most optimistic about economic conditions at home. But in several other regions, sentiment has taken a negative turn. In Asia–Pacific and in Europe, the shares of executives expecting their home economies to improve decreased by 15 and 11 percentage points, respectively, since December. The decline in optimism is most acute in Latin America, where 30 percent of respondents now expect improvements in their home economies. In the previous survey, 56 percent of executives there said the same.

UK Economic Forecast

The International Monetary Fund has downgraded forecasts for the UK's recovery this year while the expansion of the global economy, aided by accelerating vaccine rollouts, is expected to gather pace. Illustrating the severe impact of the pandemic on the UK economy, the IMF said in its latest forecast that the UK's national income, or GDP, would expand by 4.5% this year, down 1.4 percentage points from the 5.9% growth forecast made last October.

This follows a contraction in UK GDP of 9.9% in 2020, the biggest fall for any G7 country. The UK's acceleration of its vaccination program is not expected to give an extra boost to UK growth until 2022, when its growth rate is upgraded by 1.8 percentage points to 5%.

Global Economic Forecast

According to a report by the IMF, although recent vaccine approvals have raised hopes of a turnaround in the pandemic later this year, renewed waves and new variants of the virus pose concerns for the outlook. Amid exceptional uncertainty, the global economy is projected to grow 5.5 percent in 2021 and 4.2 percent in 2022. The 2021 forecast is revised up 0.3 percentage points relative to the previous forecast, reflecting expectations of a vaccine-powered strengthening of activity later in the year and additional policy support in a few large economies.

The projected growth recovery this year follows a severe collapse in 2020 that has had acute adverse impacts on women, youth, the poor, the informally employed

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and those who work in contact-intensive sectors. The global growth contraction for 2020 is estimated at -3.5 percent, nearly one percentage point higher than projected in the previous forecast (reflecting stronger-than-expected momentum in the second half of 2020).

The report further adds that the strength of the recovery is projected to vary significantly across countries, depending on access to medical interventions, effectiveness of policy support, exposure to cross-country spill overs and structural characteristics entering the crisis. The recovery will be driven primarily by countries such as India and China, forecast to grow by 8.8% and 8.2%, respectively. Recovery in large services-reliant economies that have been hit hard by the outbreak, such as the UK or Italy, is expected to be slow.

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EUROPEAN VALUATIONS

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