A challenging year anticipated for SA retailers

By Tasmika Ramlakan

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In the fourth quarter of last year, as Covid-19 appeared to be receding and the country had moved to a virtually lockdown-free scenario, the SA retail sector undoubtedly would have been looking forward to a significant uptick in festive season trade and hoping for that momentum to be maintained into, and through, 2021.

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Unfortunately, the pandemic had other ideas, and the country – as is the case worldwide – finds itself facing an unsettling year ahead as the widespread Covid-19 second and third waves unfold.

However, against this grim backdrop, a recent report by ratings agency, Moody's, could offer some hope to the local retail sector. Moody's analysts raised their retail performance expectations, effectively halving the 30% sector losses they had previously predicted and changing their outlook from negative to stable.

These predictions appear to have been made at a global level, and the situation facing the retail sector in developing regions, including South Africa, is considerably less certain.

Constrained consumer spending

Another difficult year is predicted for SA retailers as our economy comes under additional pressure. The extended lockdown restrictions are likely to further dampen consumer spending, predominantly relating to discretionary goods and services, and this could have a knock-on effect given that the SA economy, as well as employment security, is largely driven by consumer spending. Most analysts now expect retail activity to only recover to 2019 levels by 2022/23.

The upcoming retail trading updates set for release later in January are expected to confirm this concerning situation and are widely touted to include largely disappointing festive season trade figures, as consumers were still reeling from the financial impact of the first wave of Covid-19 infections in the fourth quarter of last year.

Once again, the hardest-hit sector is likely to be discretionary retailers who will undoubtedly report a less-than-festive holiday season, with sales figures well below the usual market expectations for that time of the year.

Unsurprisingly, one of the main results of these pressures has been an increasing preference by retail consumers for value purchases over premium goods. This has been especially evident in the clothing category, where value players such as Mr Price and Pepkor have generally performed better than their mid-market and premium competitors.

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Food retail: a mixed bag

The food sector is expected to show a slightly different trend, with participants in the mid-market to premium food segments expected to surprise on the upside. The reason for this is that food retailers exposed to middle- and upper-income customers, such as Checkers, Woolworths Food and Spar, are likely to have benefitted from many of these consumers staying at home instead of travelling, or even eating out, over the holiday season.

On the other hand, value food retailers may very well disappoint in terms of recent performance, having experienced volume declines, margin pressures, or both. Purchases by low-income consumers are anticipated to decline, due to difficulties in absorbing the financial shocks of lower earnings and rapidly rising food inflation, evidenced by the marked SA Food CPI increase to 5,8% for October to November 2020, from the 4,4% seen between January and September 2020.

Ultimately, the circular relationship between retail sales, consumer spending and employment in SA means retailers are unlikely to be able to 'sell' themselves out of the situation in which they now find themselves. For many, doing business the same way they always have been is not an effective way to achieve sustainable profitability going forward.

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Data to drive efficiency and engagement

The ability of any retail operation to survive and thrive – not just during the current or future Covid-19 waves, but well into the future – now depends significantly on its ability to collect and leverage customer data to understand its customers and meet their fast-changing needs.

Artificial intelligence (AI), the internet of things (IoT) and robotics are key to all of this, because they present retailers with a means to enhance efficiencies, drive meaningful customer engagement, manage inventories, optimise staffing needs and increase sales via online channels easily.

Despite all these economic challenges, retailers who used the period between the Covid-19 waves to adapt and pivot their businesses, and shift their focus to meaningful operations and supply chains, have the potential to see it through the second wave and offer value in the long term, particularly since many of them now present investors with compelling entry opportunities.

We believe that the January trading update will highlight these potential winners across the retail sector, which are likely to include such stalwarts as Mr Price, Pepkor and Woolworths. Provided investors do their due diligence and are prepared to be patient, there is still value to be unlocked in the SA retail sector.

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