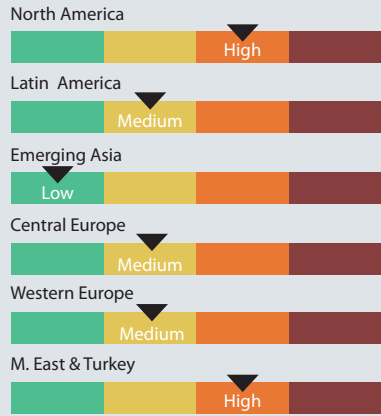




RETAIL

COFACE REGIONAL SECTOR RISK ASSESSMENT



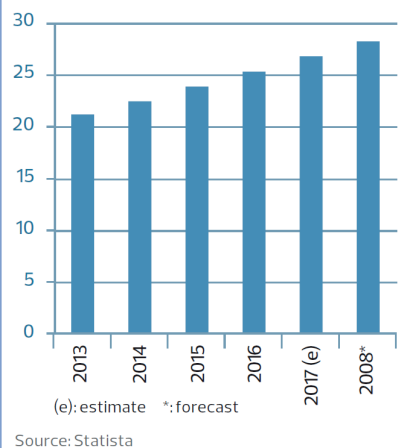
+ STRENGTHS

- Sustained retail sales growth since 2010
- Growth in the Chinese middle class
- Significant urbanisation in Asia and Africa, driving the sector

- WEAKNESSES

- Fierce competition in the sector
- Exponential growth of online shopping
- Vulnerable to economic downturns

GROWTH IN GLOBAL RETAIL SALES (IN TRILLIONS OF \$US)



RISK ASSESSMENT

Driving the retail sector, household consumption is expected to benefit from the continued recovery in the global economy, mainly in Europe but also in the major emerging economies such as Brazil. Global retail sales, including online sales, are expected to continue to grow in 2018, reaching just over USD 28 trillion compared to around USD 26.8 trillion in 2017 (see graph). This growth is likely to be boosted by the rise in e-commerce, whose share of total global retail sales is steadily expanding. The mass retailed products (Including fresh dairy products and self-service) online sales market share is expected to double over the next ten years in the most advanced markets. These should represent 30% of the market in South Korea, 15% in China and 10% in France. In 2025, this type of sale will represent 9% of the retail market, i.e. a turnover of USD 150 billion. The emergence of this new source of competition is putting pressure on the traditional players of the sector.

To cope with these challenges, traditional players are being forced to rethink their strategies, with in including greater segmentation of supply and a move towards concept stores to maximize the customer experience offer. Another underlying trend is the convergence (partly through buy-back operations) of online retailers and traditional sales groups.

DEMAND

The continued recovery in the global economy, which according to Coface projections is expected to grow 3.2% in 2018, should prop up the sector. Household consumption patterns are undergoing major changes. In the advanced economies, these are showing a greater appetite for online purchases. In addition, the “customer experience” aspect is increasingly central to why consumers visit stores. In emerging economies, the growth of the middle classes, especially in China, is supporting demand in the sector.

In fact, despite the ongoing process of rebalancing its economy, Coface estimates that Chinese growth should reach 6.5% in 2018 against 6.7% in 2017. Demand in the sector should remain strong and feed a rapidly expanding middle class. Retail sales increased 10.3% year-on-year between September 2016 and September 2017. However, the increase in household debt, which was estimated at 45% of GDP for 2016, is still a factor to watch.

In Latin America, we note the improvement of the economic situation of the Brazilian giant, with Coface projecting growth at 2.3% in 2018 against 0.7% in 2017. A catch-up effect in household consumption has been observed after two years of recession, plus a recovery in the job market and a return to low inflation. This translates into sales increasing approximately 1.3% over the first nine months of 2017 year-on-year.

In North America, growth in the US economy, expected by Coface to be 2.3% in both 2017 and 2018, should benefit from the resilience in household consumption, in a context of high consumer confidence. Household consumption however is expected to slow in 2018, despite a historically low unemployment rate (4.1% in November 2017). In fact, the consequent increase in the cost of credit will mainly affect the poorest households and will impact their consumption. In addition, households’ room for manoeuvre is particularly limited because of their level of indebtedness, which is still high despite having fallen since the subprime crisis (136% of Total Disposable Income, TDI in Q2 2017), and the fall in their savings rate in the last two years. This slowdown is likely to affect the traditional retail sector, which also suffers of overcapacity.

The economic context in the euro zone is encouraging household consumption and therefore solid demand in the retail sector, with 1.9% growth expected in 2018. This is combined with low interest rates and a high level of household and business confidence.

SUPPLY

The sector continues to be dominated by US world leaders; according to the 2017 ranking (based on 2015 revenue) in the Deloitte Global Powers of Retailing report on the retail sector. Wal-Mart Stores Inc., Costco Wholesale Corporation and Kroger Co (with revenues in USD millions of approximately 482, 116 and 110 respectively) were indeed the three biggest ones. Overall, companies are making significant changes to offerings in advanced economies in order to respond to changing consumer preferences, with in particular the development of “concept / experience stores” where there is an alliance between online retail players and traditional stores. In addition, we are seeing the development of a move towards product premiumization and a global increase in sales in specific segments such as animal products.

In the United States, the sound financial health of the market leader Wal-Mart (which has acquired five online retailers since 2016) masks a sector in great difficulty. Macy’s, Nordstrom, Kohl’s, JC Penny and Sears, which are among the country’s leading brands, reported poor financial results in early 2017.

According to the 2017 Deloitte report, the German group Schwarz Unternehmenstreuhand KG and the French group Carrefour are the two European leaders, with revenues estimated at around USD 94 million and USD 85 million, respectively. Competition from online sales is fierce throughout the region, but the situation remains very mixed. In Italy, the retail trade volume index had increased 2.7% year-on-year comparing December 2017 to December 2016. Business insolvencies in France in the sector had decreased 4% year-on-year in September 2017. In Germany, the sector continues to face structural difficulties linked to low operator profitability and intense competition. It is likely that industry players will be reviewing their plans for expansion in the UK given the Brexit.

In Latin America, businesses in the sector should benefit from the better economic conditions in Brazil and Argentina. Carrefour, which has been operating in Brazil for 40 years, continues to benefit from positive financial results with an increase in revenue of 10% in Q1 2017. The other leading groups in the country are the Brazilian Via Viajero and the French group Casino.

China’s retail sector landscape is very dynamic with some major local players alongside international leaders. Online sales are also very dynamic with Chinese and international giants like Alibaba. The high level of indebtedness in Chinese enterprises, which reached 145% of GDP in 2016, should however continue to be monitored.