

M&A and Capital Markets Activity in the North American Consumer and Retail Sector



Current Scenario

The outbreak of COVID-19 has had a devastating effect on global economies. However, as the COVID-19 curve begins to flatten, economies across the world are starting to recover. Considering the current situation, consumer and retail companies are also preparing to operate in a new economic reality.

According to the U.S. Census Bureau's seasonally adjusted data released on October 16, the retail and food services sales grew by 5.4% on a year-on-year ("Y-o-Y") basis to \$549.3 billion for the month of September 2020. The data indicates that while the economic activities in the U.S. essentials segment are recovering, they are still down in the non-essentials segment.

Figure 1: Y-o-Y Change (%) in U.S. Retail Sales (July–September 2020)



Source: U.S. Census Bureau

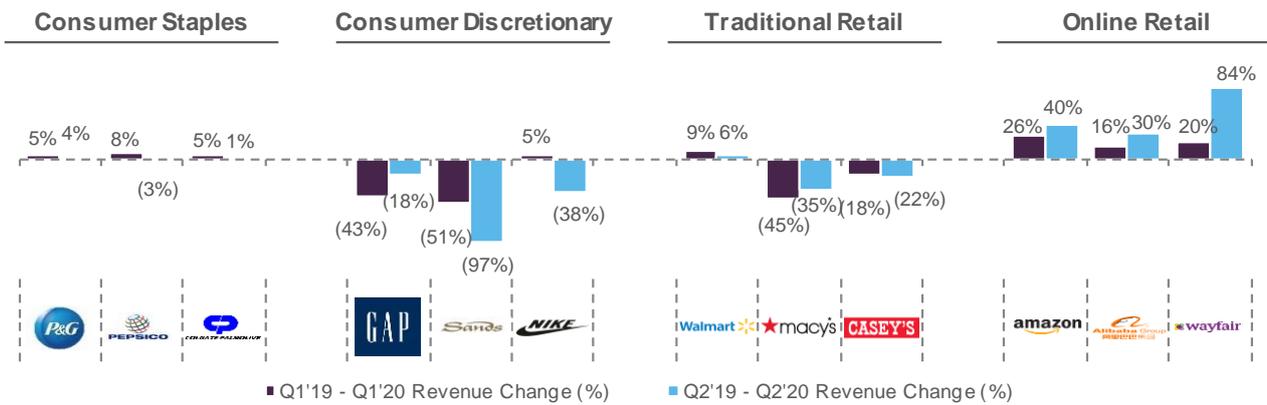
A recent report by the Bureau of Labor Statistics reflects a positive outlook for the consumer and retail sector. It states that the unemployment rate in the U.S., which peaked at 14.7% in April 2020, declined to 7.9% in September 2020. The U.S. retail sector, which had witnessed 2.4 million job cuts in March and April 2020, added back more than 1.9 million jobs between May and September. The retailers added 253,300 jobs in July, 261,200 jobs in August, and 142,400 jobs in September, respectively.

The shift in consumer preference from physical to digital shopping has prompted several online retailers, such as Amazon, to boost hiring. In H1'20, Amazon increased its headcount by approximately 10% to 876,000 people. It recently announced that it will hire 100,000 more people across the U.S. and Canada.

The U.S. government's fiscal stimulus for COVID-19 affected people is acting as a major growth driver for retail spending. The government has spent ~\$250 billion on extra \$600-a-week unemployment benefits (expired on July 31), to help people recover from the effects of the pandemic. The retail sales trends indicate that people spent their unemployment benefits in buying consumer essentials. These trends have been driving growth in the retail sector over the last couple of months. However, we believe that in the absence of these benefits in future, the broader retail recovery would take longer even if the virus is brought under control.

Financial Performance

Figure 2: Revenue Trends of Consumer and Retail Sub-sectors



Source: Company Filings

Revenue from online retail sales surged by 44.4% in Q2'20. It is the highest Y-o-Y growth for any recorded second quarter and the second highest jump for any quarter since the U.S. Department of Commerce started collecting e-commerce data in 1999. Consumers have spent more than 20% of their total expenditure online, marking the highest-ever e-commerce penetration. On the other hand, widespread store closures and consumers' growing preference for home-delivered orders led to a decline of 9.3% in traditional retail sales in Q2'20, compared with 0.6% growth in Q1'20.

The consumer staples segment grew by 1.8% in Q2'20, compared with 4.4% in Q1'20. The dip in growth can be attributed to the fact that people had already over-stocked consumer essentials in Q1'20. Sales of discretionary items continued to be under pressure and declined by 16.4% in Q2'20, compared with 5.3% in the previous quarter. Companies operating in this segment will continue to face headwinds due to COVID-19.

M&A Activities

M&A activities in the Americas (North America, Caribbean, and Latin America) surged by 226% in Q3'20 to \$65 billion, compared with \$20 billion in Q2'20. All sub-sectors of the consumer and retail sector are showing positive trends in M&A deal volume.

Although the crisis is not yet over, cash-backed buyers are tapping into opportunities for transformational deals. Currently, investors are chasing M&A opportunities with firms that have strong capabilities / assets and are expected to recover faster than the others in the post-pandemic era. This implies that organizations that lack the capability to transform in the post-COVID-19 environment or are too expensive for acquirers will become less appealing to investors.

We have observed the following M&A trends in the consumer and retail sector:

- Retailers that have failed to adopt an effective omni-channel model and do not offer unique consumer experience are facing consolidation or filing for bankruptcy.
- Companies are pursuing M&A opportunities to strengthen their supply chain and are sourcing local supplies.
- Investors are looking for deals at distressed valuation to make good use of dry powder.

After the difficult H1'20, the market has witnessed several big-ticket deals in the Q3'20. M&A activity started to rebound in May, as governments across the Americas began relaxing restrictions, and investors and negotiators adapted to remote working.

List of Key M&A deals (YTD basis)

Announced Date	Target	Buyers / Investors	Deal value (\$ million)	Target Industry
08-02-2020	Speedway LLC	7-Eleven, Inc.	21,000	Automotive Retail
09-25-2020	William Hill plc	Caesars Entertainment, Inc.	4,986	Casinos and Gaming
06-10-2020	Grubhub Inc.	Just Eat Takeaway.com	7,300	Online Food Retail
05-11-2020	Coty- Professional & Retail Hair business	KKR & Co. Inc.	2,580	Personal Products
09-15-2020	Kraft Heinz- Natural Cheese Business	Groupe Lactalis S.A.	3,200	Packaged Foods and Meats
09-29-2020	Safe Harbor Marinas, LLC	Sun Communities	2,110	Leisure Facilities
09-09-2020	J. C. Penney Company	Simon Property Group; Brookfield Property Partners	800	Department Stores
06-24-2020	GNC Holdings, Inc.	Harbin Pharmaceutical Group	760	Specialty Retailers
09-14-2020	Scientific Games Corporation	Caledonia Investments	925	Casinos and Gaming
09-22-2020	Boa Technology	Compass Diversified	454	Footwear

Source: Company Filings

Figure 3: M&A Deal Volume (YTD)

(Total Deal Value in \$ billion)



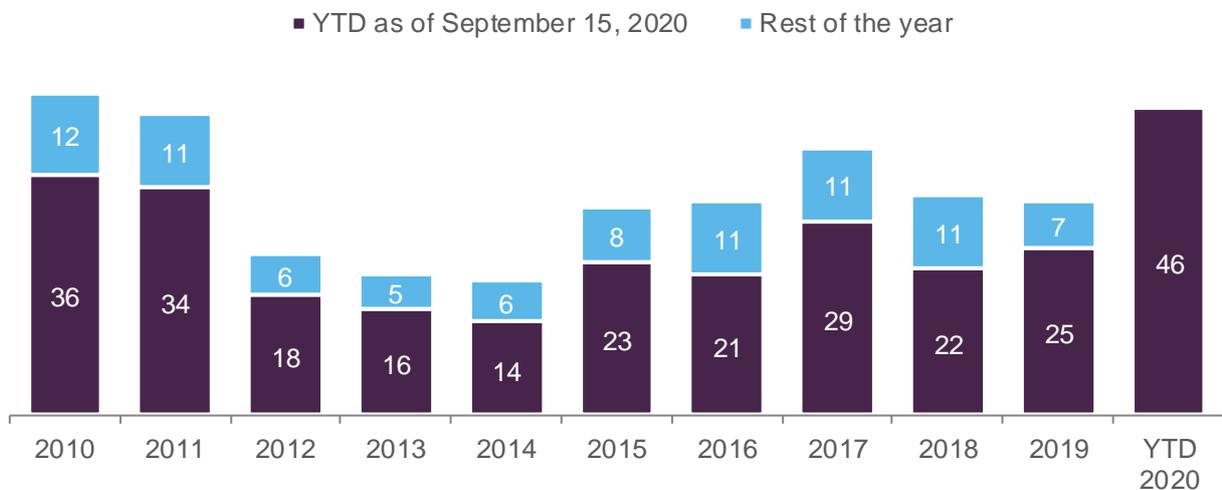
Source: Refinitiv Deals Intelligence

Rising Bankruptcies

Retailers are facing toughest challenges since the global financial crisis in 2009. The COVID-19 pandemic has compelled most traditional retailers to close their stores temporarily / permanently. It has led to a massive dip in customer footfall, forcing retailers to negotiate with other stakeholders to manage unforeseen inventory. The crisis has caused severe liquidity concerns, compelling many traditional retailers to file for Chapter 11 bankruptcy protection.

The U.S. has the highest number of COVID-19 cases in the world. The country is struggling to manage these cases as well as facing a severe pandemic-induced recession. Thus, we expect several companies to file for bankruptcy in the near future. As of September 15, 46 retail companies (each with assets of more than \$1.0 billion) had filed for Chapter 11 bankruptcy.

Figure 4: Bankruptcies Announced in the U.S. Retail Sector



Source: S&P Global Press Releases

Although the pandemic seems to be the apparent reason for the bankruptcy filings, we believe the long-prevailing unsustainable debt structure of retail companies in the Americas is the primary reason that forced them into seeking bankruptcy protection. Many of these companies have now hired advisors to explore debt restructuring options and forge a turnaround.

Capital Market Activities

Figure 5: DCM Quarterly Deal Volume

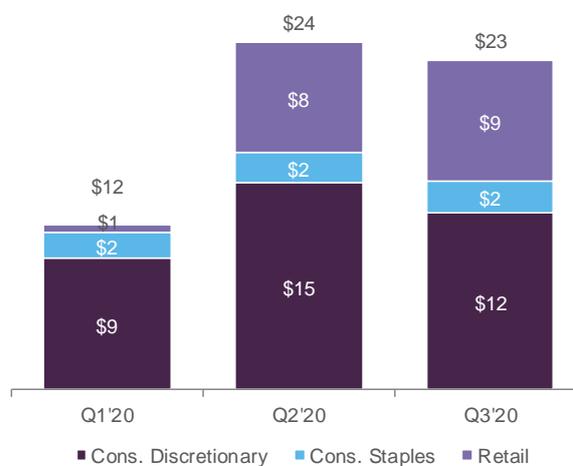
(Total Deal Value in \$ billion)



Source: Refinitiv Deals Intelligence

Figure 5: ECM Quarterly Deal Volume

(Total Deal Value in \$ billion)



Source: Refinitiv Deals Intelligence

The debt capital market peaked in Q1'20, driven by extensive debt-raising and refinancing activities by consumer and retail companies to restructure debt, pay down bank lines, keep their operations running, and raise cash to weather the effects of the pandemic.

Debt-raising activities in the Americas declined by 66% during Q3'20 and was valued at \$112 billion, compared with \$186 billion in Q2'20. The decline was due to the fact that most of the companies already undertook debt raising activities in Q1'20 and Q2'20. In August 2020, 7-Eleven, the largest convenience store chain in the U.S., announced the acquisition of 3,900 Speedway stores for \$21 billion. The company plans to raise \$13 billion in a bridge loan to fund the acquisition.

Equity-raising activity in the Americas inched down by 5% during Q3'20 to reach \$23 billion, compared with \$24 billion in Q2'20. Deal volume in the consumer discretionary and retail segments displayed strong momentum, as companies began raising funds through fresh issue of equity and IPO activity began to rebound during Q2'20.

Albertsons Companies, Inc., a U.S. supermarket operator, closed its \$800 million IPO on June 30, 2020 and began trading on the New York Stock Exchange (NYSE) under the "ACI" ticker symbol. Vroom Inc., an online used-car retailer, made its public debut on June 9, 2020 on the Nasdaq and raised \$467.5 million in gross proceeds.

The companies will, however, continue to experience short-term challenges in raising fresh funds from debt and equity markets, as the current market volatility has caused many investors to stay away from the markets for some time.

The Road Ahead

The world is eagerly waiting for a vaccine against COVID-19. Although there are many candidates under trial, we believe none of them will be made available for public in the next 3 to 6 months. This means that sectors, economies, and industries across the globe will continue to face pressure due to the pandemic. The virus is expected to continue to affect consumer spending and retail sales in the near term. Considering the current status of vaccine development, we do not expect economic normalcy before mid-2021.

The consumer and retail sector will likely grow over the next couple of years, aided by an anticipated rebound in the economy once the pandemic is over. We also expect a rise in per capita disposable income and consumer spending in the post-pandemic era, which will likely fuel the sector's growth.

Moreover, decreasing unemployment rates in the U.S. and improvement in consumer confidence index will likely encourage consumers to spend more. We believe, in order to survive the crisis and ride the growth wave, retailers and manufacturers should collaborate more and adapt to new consumer preferences and behavior, as well as regulations.

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