

Retail: navigating the impact of COVID-19

Building flexibility and resilience in the new normal

2020





Introduction

The retail industry is currently in a period of disruption unique in its scale and severity. The global outbreak of COVID-19 has impacted parts of the industry in different ways. While businesses in the grocery sector grapple with supply chain issues, those selling consumer goods and apparel have been challenged by store closures and rapid growth of online sales. Across Saudi Arabia, landlords and retailers have been collectively minimising losses through offering generous incentives to support rental freezes for 1-3 months, along with offering consumer promotions. The acceleration of e-commerce has been notable across the Kingdom.

This report looks at the steps retail businesses need to take to put themselves in the best position for the 'new normal' that will emerge once lockdown restrictions are eased. From liquidity to debt and restructuring, the challenges retailers face are diverse and complex. We also consider implications for employers and how financial planning for the medium and long term will be affected.

We will cover:



Liquidity



Cost management



Debt and restructuring



Preparing for the new normal



What Grant Thornton is doing to help retailers

The challenges posed by COVID-19

The picture for the retail industry at the midway point of 2020 is vastly different than any one of us could have predicted at the end of 2019. The global spread of the virus has brought a temporary halt to all non-essential trading in many parts of the world. The discretionary sector has seen a significant drop in revenue with closed stores. The grocery sector, on the other hand, is dealing with unpredictable demand and a huge increase in demand for online delivery services. Many consumers in Saudi Arabia have relied on e-commerce to purchase both essential and non-essential products, which has led to a huge surge in online sales of up to 300% to 400% for certain brands, compared to pre-pandemic figures. For many companies the sharp economic shock has been exacerbated by operating very tight businesses that carried little cash. Add to this high fixed costs, and it becomes clear many in this sector are in a vulnerable position.

Liquidity

Just like a wide variety of sectors, cashflow forecasting and management has become a serious challenge for many retailers, big and small. An immediate priority over the short to medium-term is preserving cash and increasing liquidity. While government schemes all over the world have allowed businesses to temporarily reduce or defer some of their operating costs, particularly with regards to staff and tax payments, these measures will not go on indefinitely. Retailers that have an established online presence are better placed to adapt their operations and continue to bring in some level of sales. The feasibility of prioritising an online model requires an ability to balance lower profitability per sale and reduced staff with potentially higher operating costs. The extent to which supply chains have been affected will also be a big factor in whether retailers can adapt their processes.

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While the grocery sector has seen an unexpected boost to revenues, this has come with a range of additional challenges. Spikes in demand have caused stock shortages and supply chain issues, as data driven stock planning and merchandising models failed to make it easier to plan what products were needed. Social distancing and increased cleaning have created additional operating costs, but it is the spike in demand for online services that has caused significant pressure. Some brands simply did not have the infrastructure in place to deal with the surge in orders. For shops that are closed or sitting on large amounts of stock that they cannot sell, fixed costs are a serious issue. If they cannot move online, these businesses will need to seek help from the government, lenders or their shareholders.

Cost management

Cost reduction has become an immediate strategic objective across the sector, and we are seeing many businesses looking carefully at their lease and infrastructure costs as well as their physical footprints. For most retailers, the three biggest costs are stock, property and labour.

Many landlords are granting businesses three-month payment holidays, and we may see more flexibility built into the system, such as leases as a percentage of sales. But without revenue coming in there is still uncertainty about how long businesses can operate. For apparel retailers in particular, many of which are sitting on large amounts of unsold seasonal stock, we are already seeing heavily discounted prices. Many other brands will be looking to purchase distressed merchandise at very low prices to sell themselves once their stores are reopened.

For those stores that remain open, COVID-19 has affected almost every part of their supply chains. Social distancing and increased cleaning is, in many cases, increasing costs and slowing processes down, meaning many companies will be looking for profit improvement strategies. In the grocery sector, the need to drive efforts upstream in supply chains could lead retailers to stock less individual brands and instead opt for deeper relationships with particular suppliers. Those with bigger cash reserves will continue to implement automation and self-service solutions, while others could be further incentivised to prioritise these technologies in the medium to long-term.



Debt and restructuring

With revenues flat and many retailers facing a sustained period of depressed demand, finding constructive solutions for debt payments is a major priority. It is important that businesses maintain clear communication with landlords, shareholders, banks and other stakeholders about their ability to operate. Banks may be willing to reschedule debt payments, but only if companies can demonstrate the viability of their recovery strategy. The big concern for lenders when agreeing these kinds of extraordinary measures, or committing to additional lending, is what shape retailers will emerge from the crisis in. For businesses, this means putting together funding proposals for shareholders, using insolvency tools to restructure quickly or even exploring options like bankruptcy protection.

But for those companies that are able to survive into the short and medium-term, it is important to have a viable business strategy in place. COVID-19 could act to speed up the existing trend of retail chains looking to downsize their physical footprints and boost their online activities. But while investors may be looking to pick up brands or acquire capabilities to bring in-house, securing additional physical store space is unlikely to be high on the list of strategic objectives.

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Preparing for the new normal

The disruption caused by COVID-19 has undoubtedly accelerated the shift towards online retail, but it could also have other wide-ranging effects too. If a significant number of businesses decide to retain homeworking as an operating model, the numbers of commuters could reduce as well. This would directly impact the long-established strategy of locating retail stores in and around train stations and other commuter hubs. Apparel brands need to create viable solutions for ensuring that changing rooms align with social distancing and increased cleaning requirements, while consumer goods stores should consider if they are going to allow consumers to pick up and browse their stock. It is uncertain just how much this global public health crisis is going to alter consumer behaviour and whether these changes will extend into the long-term.

Retailers need to ensure their businesses are as resilient and flexible as possible going forward. Lenders and stakeholders need to know there is a working strategy for transitioning from the present disruption to operating in the new normal. This means reducing physical footprints, growing online, creating a multichannel presence and restructuring, but the aim should always be identifying a target market and creating a core group of loyal customers.



Critical considerations for your response

The value chain of the retail industry is highly interconnected with other industry groups and domestic, regional and global economic and social activity. Many of the forces impacting the retail industry are driven by factors outside of its control; this complexity has been highlighted by the impact of COVID-19.

Current market conditions are driving clear liquidity and operational challenges, but can also provide opportunities to those with strong balance sheets and access to supportive lenders and investors. The interconnectivity of the retail industry drives the need for well thought-through, integrated solutions that critically address the needs of multiple stakeholders, particularly where there is separation between asset ownership, the operator and the funders.

We consider the questions on the next page are some of the more important areas to focus on for the industry when looking to assess, protect and restore value – some will be more relevant to your business than others. Grant Thornton can help you to define the next steps in your response.

Key questions to consider





How Grant Thornton's solutions can help you

Our approach in supporting you to assess, protect and restore value in your business starts with helping you to regain control by stabilising the business, whilst developing a robust and realistic turnaround plan. We draw upon our deep expertise across a range of different areas, customised to your specific needs.

Successful turnarounds require the development of a credible plan that has been stress tested against various scenarios, along with a transparent communication strategy that meets the needs of all stakeholders. Building trust, and not breaking promises, will be critical if the plan is to be realised.



Stabilisation, turnaround, and business plan assessment

In the early stages of a turnaround the right support is necessary to create financial stability, assess cashflow and identify opportunities to improve short-term liquidity.

Through independent diagnostic analysis and challenge, we provide stakeholders with a clear understanding of the options available, including strategic and tactical opportunities.

This crucial activity provides comfort and support to management teams and can underpin the credibility of the plan as part of the assessment process of financial stakeholders.

Our solutions

Operational and financial restructuring

Our multi-disciplinary operational and financial restructuring specialists provide support to realise significant business process improvement, implement new business strategies, divest noncore businesses and design new capital structures aligned to the dynamics of the business.

Retail operational consulting

Running a successful bricks-and-mortar retail space involves a lot of behind the scenes activity. Using our specific industry experience, we can help with workforce planning, back of store process efficiency, rostering/labour efficiency, in-store fulfilment of online orders, space optimisation, format development, and store renewal. In order to remain competitive in today's market most retailers are investing in their online offering and our experience includes working with retailers to optimise online capability and support efficient product delivery to the customer, including: online fulfilment; model rollout and optimisation; integration of online into merchandise and store operations; and order management system design and delivery.

Real estate advisory

Our real estate advisory team can help you create a flexible real estate strategy and plan, allowing your business to adapt when it needs to. With the foundation, strategy and plan in place, we will help you optimise your business' efficiency and productivity. Capital raised as a result and in addition to strategic disposals can be re-invested elsewhere and support your business growth. Finding the right space, in the right location, provides a foundation to promote success through your business' operations, people, technology and access to market, enabling you to focus on your business goals.

Debt advisory

We provide specialist advice on the raising and refinancing of debt. Through our deep understanding of the funding landscape and detailed knowledge of the credit process, we devise tailored funding solutions as part of a sustainable capital structure in line with the strategic ambition of our clients.

Exit strategy services

We apply a tailored methodology and fully project-manage and implement the sale or closure of underperforming or non-core corporate entities at maximum value.

Valuations to support asset-backed lending decisions, restructuring and transactions

We provide valuations to support asset-backed financing, including valuing shares and intangible assets, and provide periodic valuations of assets to confirm that the terms of the loan agreement continue to be met. For mergers, acquisitions, restructuring and proposed financial structures, we provide an independent view on value delivering robust advice within the constraints placed by the deal deadlines.

Accelerated M&A

We provide advice and manage transactions associated with the acquisition or disposal of distressed assets or businesses, frequently to short timescales.

Asset recovery and tracing

Asset recovery and tracing normally form part of formal insolvency processes such as liquidations, or are carried out in support of ongoing litigation or fraud investigations. We use specialist approaches to identify and recover misappropriated assets, including those held in offshore trusts, to provide cost-effective value recovery.

Corporate insolvency

Where a business cannot be saved or where a formal insolvency process is required to affect a restructuring, we provide advice and support to distressed companies, their creditors and other stakeholders in order to protect assets and maximise recoveries. In some situations, we take on the role of Chief Restructuring Officer.

Pension schemes solvency

In many parts of the world, we offer a specialist capability to advise corporates and trustees on the solvency of pension schemes.

Enterprise risk management

Our enterprise risk management (ERM) specialists help organisations implement the leading approach to managing and optimising risk. We are able to tailor the approach to our client's individual challenge and create bespoke strategies that work, enabling them to strategically identify, analyse and monitor potential risk to their organisation.

Cybersecurity

Our cybersecurity solutions are designed for clients seeking to address a variety of complex security requirements. We can help organisations assess their security vulnerability, establish or improve their IT security processes and remediate breaches or compliance failures.

Business Process Outsourcing and Shared Service Centres

Increasingly, large organisations are looking to fully outsource their transactional end-to-end finance and accounting processes, leaving them free to focus their finance resources on important strategic business value. We typically commit to reduce costs and/or improve productivity and quality. We also advise organisations on optimising finance and accounting processes, and can take our recommendations through to implementation, whether this involves building a full-scale Business Process Outsourced delivery capability or setting up a Shared Services Centre.

Back office outsourcing

We provide outsourced accounting, payroll, human resource and tax services to domestic SMEs or local branches of international organisations. Our services are managed centrally to deliver a consistent experience for each of our

clients, however widespread their operations. We exploit innovative digital technology to give our clients access to their data round the clock; the same technology gives our large corporate clients access to new and cost-effective offshore platforms. Where our clients face complex tax and payroll challenges, our tax, global mobility and wealth management specialists provide expert, value-adding advice.

Global compliance partnering

Our global compliance partnering solution delivers all local statutory financial reporting, centralised statutory audits, tax compliance (corporate, sales and payroll), payroll administration and local country filings for multinational organisations through a single point of contact. We are the leading adviser to dynamic organisations delivering a solution that improves reporting efficiency and enhances risk management. By providing full transparency, real-time monitoring and highlighting upcoming deadlines, we enable local and central management teams to ensure full compliance at all times.

Financial reporting advisory

We provide clear and practical solutions to address complex accounting and financial reporting issues. We support businesses in navigating the accounting and reporting of government stimulus packages. We're also able to help navigate the accounting and reporting of complex areas including leases, impairment and going concern.

Restructuring tax

Our restructuring tax teams specialise in providing tax advice in all aspects of restructuring scenarios. In particular, this includes advising on the tax aspects of:

- independent business reviews, options reviews and contingency planning
- business restructuring, eg debt restructuring
- mergers and acquisitions
- disposals of trade and assets or wind down of businesses
- corporate insolvencies
- fraud investigations.

Consumers have been compelled to diversify their buying behaviours because of the extended lockdown period, which has given rise to the evolution of e-commerce across Saudi Arabia.

As the notion of convenience, choice and accessibility embeds across the Kingdom, the concept of online buying will surge beyond the pandemic, creating a new way of buying and transacting.

Retailers have an opportunity to innovate their business models, operational practices and to streamline costs in order to leverage the trend further.

Helping your business respond to COVID-19

We are immersed in the retail industry and our professionals are uniquely positioned to assist you in all aspects of the creation and execution of your turnaround plan.

1

You will be working with people who are part of your industry, have a track record of achieving success for their clients, and will bring that experience to your challenges

2

We will take a holistic view of the challenges you face and deliver targeted solutions throughout the various elements of retail value chain including operation, franchising, ownership and funding

3

We will work closely with you to implement performance and working capital improvements and drive effective restructuring strategies. These include providing independent critique of refinancing proposals and acting as a respected bridge between lenders and the senior management team

4

Our experience of effective divestment/investment strategies for investors, funders and corporates will help you identify and maximise opportunities for value creation or protection and to improve liquidity availability if necessary

5

Regardless of the complexity of your group structures, or the international footprint, we have a global network of firms and market-leading teams in all the key offshore financial centres, to be able to advise all leading practices

6

We are at the heart of the development of cross-border restructuring legislation, giving our clients access to leading-edge and best practice restructuring solutions.

“Dynamic organisations can achieve great things with the right support. You need advisers that deeply understand your business, your industry and your wider agenda for growth. Our capabilities, expertise and culture make us perfectly placed to fill that role.”

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