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2019 - Retail's gap year

Retail Forecasts February 2019

Public Executive Summary

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Deloitte Access Economics

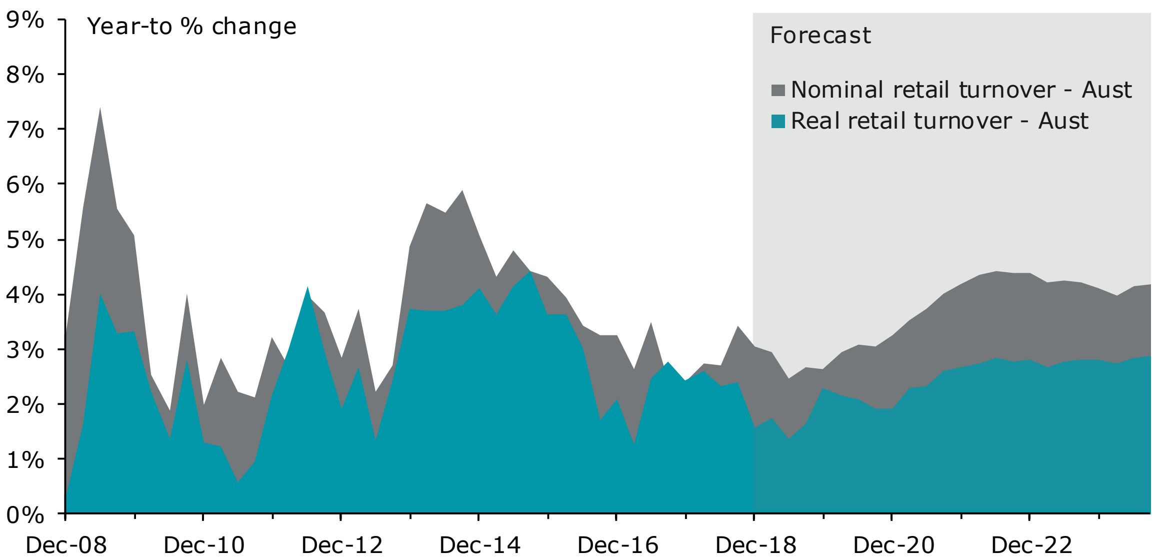
National Outlook

Australia's retail sector has been sustaining a reasonable rate of sales growth in an unconventional way – not so much from income growth, but leveraging off consumers' willingness to spend. That willingness to spend has been supported by very strong asset price growth, creating a massive windfall for one set of consumers. But for another (largely separate) set of consumers they have been associated with a significant lift in debt commitments. In recent years both cohorts have run down their rate of savings from labour income, to support consumer spending at a faster pace of growth than it rightly should have achieved, given the economic fundamentals.

Retail sales weakened in 2018, with real retail turnover expanding 2.2% over the year. Housing gains have dried up and there are question marks over the sharemarket as well. Labour income growth is good, but not good enough yet to avoid some damage to retail growth in the absence of an excuse to run down savings further. And when overall net wealth is heading downwards, it provides a fairly strong incentive to be more prudent with your cash. That leaves 2019 as retail's gap year - nursing a hangover before getting ready to move ahead in a year's time.

Why will 2020 retail sales be better? Primarily because the asset price trauma is expected to have largely worked through, which will leave labour income growth as the key underlying driver once again. There is upside pressure to wages, particularly in pockets of hot demand such as infrastructure and digital, and this is expected to continue building through 2019, providing a stronger platform for retail spending as we head into 2020.

Chart 1: Nominal and real Australian retail turnover



Source: ABS Cat 8501.0, Deloitte Access Economics

Key changes since last issue

The Australian economy slowed more than expected in December, with quarterly growth of just 0.2%. Weakness in the housing market weighed heavily on construction activity, and consumption remained under pressure. The flow of weaker data leading up to the quarterly result prompted the Reserve Bank of Australia to moderate its stance on future monetary policy changes, indicating a rate hike was now just as likely as a rate cut. The central bank maintains its outlook for growth and inflation, but noted that this is dependent on the ongoing strength of the labour market.

Economic and retail trends

A **slowdown in the global economy has commenced** after a robust period of growth as the drivers of growth start to splutter. While the US economy was benefiting from the 2017 tax cuts, with stronger job growth and wages in 2018, the boost to activity is likely to be short-lived. US growth is easing back as higher interest rates and exchange rates take hold, and rising trade tensions weigh on business sentiment. Meanwhile, the slowdown in China's economy has accelerated more recently, despite increased monetary and fiscal stimulus measures.

The **Australian economy is showing signs of weakness heading into 2019**. Construction activity has pulled back, driven by declines in the housing market, and private consumption remains constrained by subdued income growth. Exports continue to perform strongly, especially in the gas and coal sectors, but this has not translated into any major lift in investment activity. Overall, economic growth is anticipated to drift lower over the coming year.

Overall consumer spending growth over the past five years has averaged 2.5% per annum – but growth is household disposable income has only averaged 1.9% per annum. That difference is a fair chunk of change. Many retailers have only survived the last few years because **we have lived beyond our means**. This is reflected in the household savings ratio, which ended 2018 at 2.5%.

The **Federal election** will deliver a sugar hit to consumers to help get through what would otherwise be a more constrained income environment. It does look like, at this point in time, the 2019-20 Federal budget is heading towards a surplus. But with a Federal election now only weeks away there are likely to be lots of raids from both sides of politics on a pretty modest pot. The government has already proposed personal income tax cuts. Beyond that there is speculation of straight cash handouts, mimicking the response to the GFC in 2008-09. Both of those avenues would translate very quickly into higher rates of retail and other consumer spending, and would no doubt be gratefully received by the sector.

The retail sector ended 2018 on a weak footing, and anecdotal evidence suggests this has continued into 2019. **Foot traffic was down** an average 3.8% through January, and while the shift to online spending accounts for some of the weakness, there is also indications of weaker underlying demand. Real retail turnover growth is expected to slip from 2.2% in calendar 2018 to a more modest 1.6% growth in 2019, before lifting back to 2.2% growth in 2020.

And while 2019 will be tougher overall, it's also **not going to be a uniform picture across components of spending.** Retail's worst year over the past decade was not during the GFC (when massive cuts to interest rates and some government stimulus supported the sector) – it was in 2011 as the sugar hits faded. During that year, sales at department stores and clothing retailers went backwards, while catered food sales also suffered a blip following a couple of years of strong growth, with the more discretionary element of these offerings being hit. Consumer durables and more discretionary spending may be similarly hit during 2019.

But, like all good gap years, there is also the **opportunity to use the time well to set oneself up for success in the future**. In the case of retailers, this 2019 gap year is not just about survival (though that is clearly important). It can be used to become more competitive, including strengthening connections with customers and streamlining operations, so that when broader market growth does return, retailers are in a position to take best advantage of it.

The rise of debt - buy now, pay later

What is it?

Buy now, pay later is a payment system where the payment is either delayed or payed off in instalments. It sometimes requires a deposit or upfront payment. The offering is operated by retailers and service providers, such as Afterpay, Certegy Ezi-Pay, and zipPay.

The service is usually used on non-essential items such as clothing, technology, electronics, software, personal care items, furniture, homewares, and appliances. While the average purchase using this form of payment is relatively low at just under $200, increasingly buy now, pay later is available for more expensive products.

In general, the fee for using this service is paid by the retailer rather than the consumer. However, any late payments are paid by consumers, and these fees are increasing as a share of total revenue, sitting at 12% in June 2018.

Who is using it?

Between 2015-16 and 2017-18, the number of users increased from 400,000 to 2 million, or 10% of the adult population. In addition, the number of transaction increased from 50,000 to 1.9 million over the same period.

Buy now, pay later is most popular for spending on pets and animals (18% of online payments), and fashion (15% of online payments). The average consumer is young, with 60% of users aged between 18 to 34 years. Many are employed part-time or unemployed, and more women use the service compared to men.

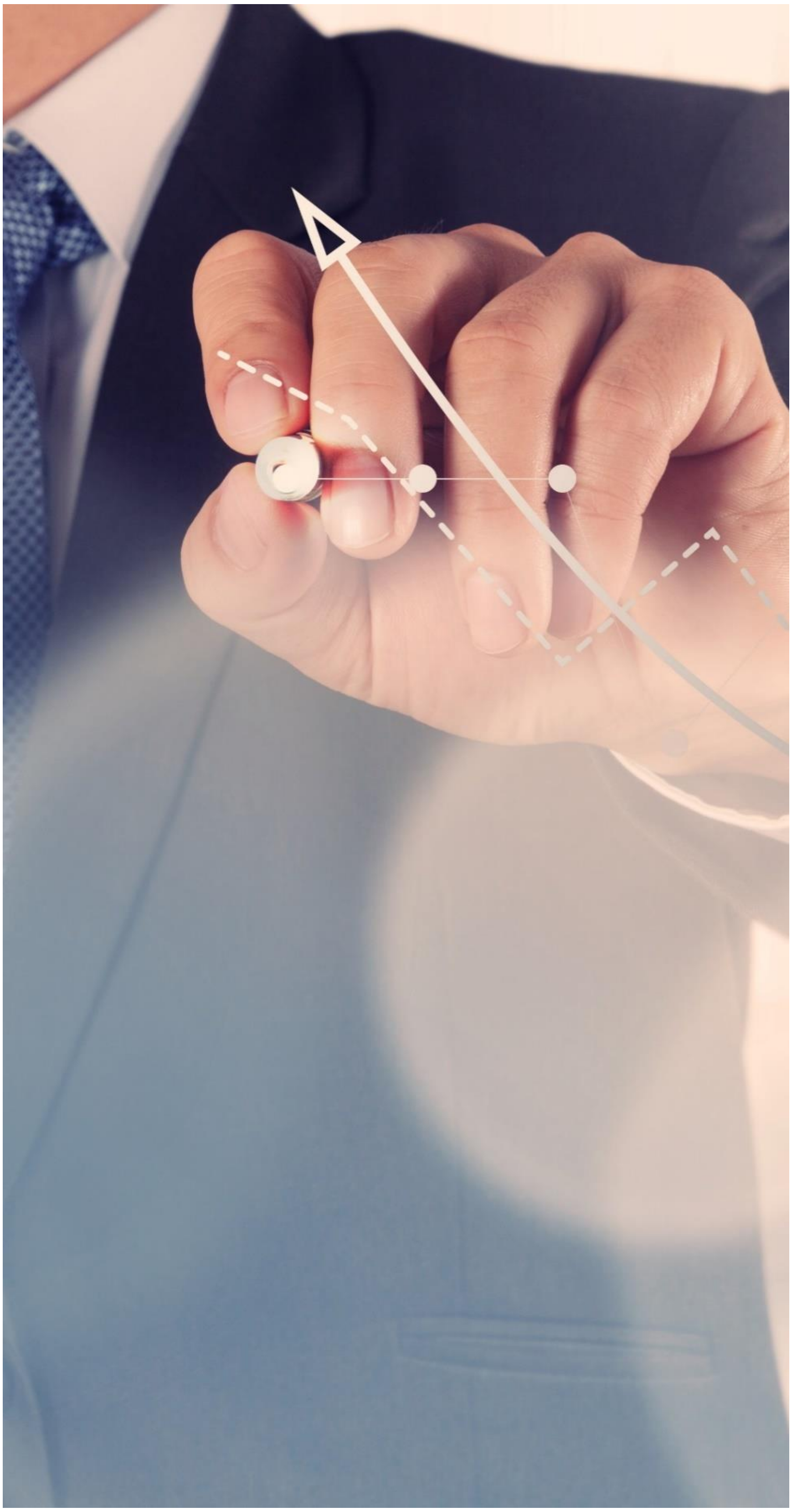
How does it impact spending behavior?

Research by ASIC indicated that 81% of users surveyed felt they could by more expensive items than they were otherwise able to, 70% felt they could be more spontaneous with their purchasing habits, and 64% felt they could spend more than they normally would.

While people using the service can spend more in the short-term, there is a risk that debt can build up if payments are not made on time, causing a reduction in spending in the long run and contributing the financial stress. Also, excessive spending in the short-run increases vulnerability in the event of an economic shock. Around 10% of transactions incur a missed payment fee according to ASIC research.

Some concerns have been raised that while providers help customers manage their obligations, there is little done to check the customer’s ability to service the debt by examining income or existing debt requirements. This could potentially increase the riskiness of this type of lending, creating problems down the track if household finances change.

What is Retail Forecasts?



Retail Forecasts, produced quarterly, provides detailed analysis of current retail sales and consumer spending, and the important economic drivers which influence them.

Included are National retail forecasts, retail category forecasts and State retail forecasts, as well as the broader income and non-income influences of retail spending.

An annual subscription includes four quarterly reports plus Excel spreadsheets including 10 year forecasts and charts.

The accompanying Detailed Consumer Spending provides ten year forecasts of detailed Household Final Consumption Expenditure categories and detailed Retail Sales categories.

Contact us

We are happy to respond to any inquiries in relation to the publication or our forecasts.

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Report with retail forecasts data:
$2,799 for an annual subscription or $1,399 for a single issue.

Report with retail forecasts data and detailed consumer spending forecasts: $9,899 for an annual subscription or $4,949 for a single issue.

Our retail forecasting and analysis capabilities

Retail forecasts and analysis are a key focus of our macroeconomics practice.
Deloitte Access Economics specialises in research of the movements of key drivers in the Australian economy. By combining this wealth of knowledge with research on consumer behaviour and the retail market, we can analyse current retail supply and demand characteristics, forecast future movements and make informed recommendations for retail development, investment and strategy. At Deloitte Access Economics, we draw on our highly reputable research into key drivers of retail demand to provide insights to clients. These drivers include the following:

- **Consumer behaviour:** Consumers' changing preferences and needs
- **Consumer sentiment:** How consumers react to economic changes
- **Household income and debt:** Current and future insights on disposable income
- **Population and socio-demographics:** How the population is likely to change over time
- **Technological influences:** The effect of technology and the internet on retail
- **Macroeconomic influences:** How the economy at the state, national and world level affects the retail market.

Our project experience

Deloitte Access Economics has delivered a range of insights for the retail sector, including:

- Economic contribution work for a number of major retail stakeholders
- Competition policy analysis for major retailers
- Price and productivity analysis at a category level for major retailers
- Analysis of Australian online retailing for major stakeholders in the retail sector
- Mobile Nation: opportunities and strategies for retail for Australian Mobile Telecommunications Association
- Monthly economic briefs for a major retailer (ongoing work over several years)
- Monthly retail trade briefs for a major retail stakeholder (ongoing work over several years)
- Commentary on key drivers of retail sector performance, delivered to a number of clients as reports and/or presentations
- Economic outlook commentary, as it relates to the retail sector.

Our core capabilities

We can forecast retail turnover

- Retail turnover forecasting, at national, state or regional level if required, based on ABS, Household Final Consumption Expenditure and MarketInfo categories

We can analyse a specific product or place

- Regional economic profiling and forecasting, with a focus on retail
- Consumer product pricing, competition and performance analysis
- Shopping centres and retail precinct competition and performance analysis
- Economic impact analysis for major retail developments or decisions

We can contextualise retail trends using our economic knowledge

- Commentary on retail performance, growth and trends within an economic context
- Consumer behaviour and consumption habits analysis
- Digital influence analysis of retail and consumer products
- Retail trends analysis and forecasts, in terms of both supply and demand trends

Drawing on the above, we can help with forward planning

- Network planning for retailers and centre owners
- Strategic planning for retail sector decision-makers
- Scenario planning for retail sector decision-makers

Our publications

Below are examples of Deloitte’s recent published retail research. Please click the icons to see more on each publication.

CFO Sentiment Edition 5
Solid on outlook, positive on risk

Retailers’ Christmas Survey 2018
Spending your way through Christmas

Global Powers of Retailing 2018
Transformative change reinvigorated commerce

Meaningful brands
Connecting with the consumer in the new world of commerce

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