Upcoming Events

22 Nov: UK Autumn Statement

24 Nov: GfK Consumer Confidence

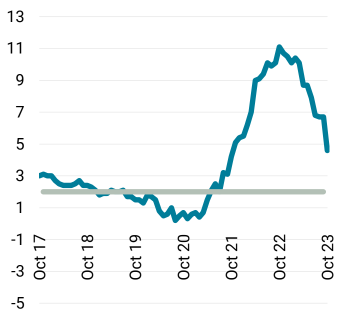
12 Dec: Average weekly earnings

20 Dec: ONS Inflation Data

22 Dec: ONS Retail Sales Data

Chart of the moment

UK Consumer Confidence



Source: GfK, Bloomberg

20 November 2023

Cautious consumers

October's lower than expected inflation and retail sales data casts a shadow on the outlook for the key festive period. We expect consumers to be value-led, with promotional activity and discounting likely to be high through Q4, with company guidance remaining cautious. But it appears there is value to be had in UK consumer stocks, with several takeovers announced in recent weeks.

Retail sales fell to a two-year low last month, as inflation continued to impact customer spending. Sales volumes were 0.3% lower month on month, a negative surprise versus expectations for a 0.4% increase. September sales volumes were also revised lower, to a fall of 1.1% (previously a fall of 0.9%) On an annual basis, sales volumes were down 2.7% versus October 2022, again worse than the minus 1.5% economists had expected. This means sales volumes were at their lowest levels since February 2021, when there were widespread and extensive restrictions to non-essential retail following the Omicron outbreak. Shoppers cut spending on petrol and clothes, with volumes of groceries and household goods also lower (exhibit 1). Persistent inflation has driven a continued divergence between qualities bought (volume) and amount spent (value). Compared to pre-covid levels of February 2020, October sales volumes are down 3.1%, but up a massive 16.9% in value terms, as consumers have had to pay substantially more for less (see exhibit 3). A lacklustre October is likely to add pressure to retailers moving into the key Christmas trading period. We expect significant promotional activity through Black Friday as price-sensitive consumers hold out for discounts.

Online sales values declined 1.2% from September to October, ahead of the monthly fall in the value of total retail, meaning the proportion of sales transacted online fell to 26.6% versus 26.9% a month earlier. The proportion of sales online is broadly consistent YOY versus 26.5% reported October 2022, and remains substantially above pre-covid levels of 19.7% reported in Feb 2020.

UK CPI slowed more sharply than expected in October, down to 4.6% versus the 6.7% recorded for September. This was below than the 4.8% predicted by economists, and the lowest read since October 2021. Inflation has now more than halved from its peak of 11.1% reported in October 2022, understood to represent the highest annual inflation rate since 1981. Lower energy costs were a key contributor to the decline in inflation, along with moderating food price inflation. However, whilst inflation is slowing it remains more than double the BoE's 2% target, with overall price levels now over 20% higher than in January 2021, before factors including supply chain disruption and Russia's invasion of Ukraine caused them to soar.

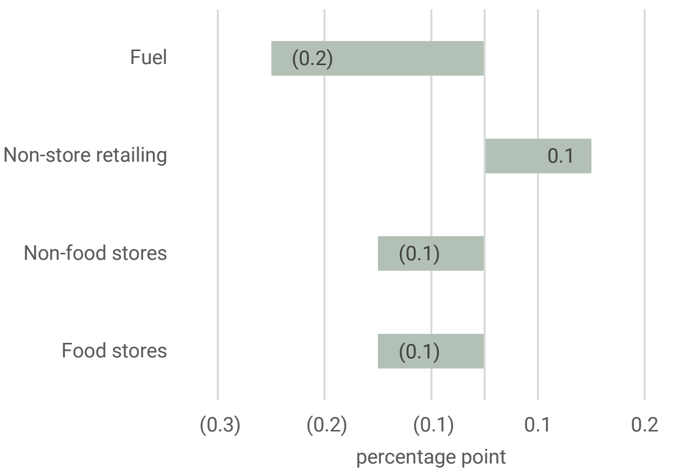
UK wage growth moderated slightly in the three months to September. Regular pay (ex. bonuses) was 7.7% higher YOY in the three months to September, slowing slightly versus the 7.9% increases reported in the previous two ONS releases. Wages have been pushed higher due to a shortage of labour after many workers left the job market during covid and a lower volume of EU workers post Brexit. Adjusted for inflation, real wages were 1.4% higher YOY.

Base rates could fall sooner than previously thought. The weaker than expected sales and inflation data means markets have now almost entirely dismissed the potential for further interest rate rises and have brought forward expectations for the first rate cut to June 2024, a significant move versus the beginning of October when investors did not expect the BoE to lower rates before early 2025.

Chanceller Jeremey Hunt will make his **Autumn Statement** this Wednesday. A coalition of retailers, hospitality and leisure businesses have written to the Chancellor, urging a freeze on business rates and the extension of existing rates reliefs. Business rates in the current year were frozen by the chancellor in last year's autumn statement in a bid to prevent shops from increasing prices on the back of higher tax rates, in turn fuelling inflation. There has also been calls from the retail and tourism sector for the Chancellor to reinstate VAT-free shopping for tourists, and for a review of card fees charged by payment system operators.

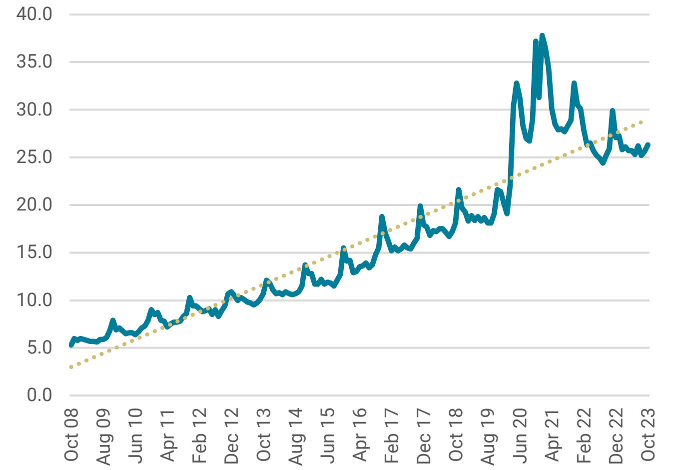
Charts

Exhibit 1: Retail sales contribution MoM



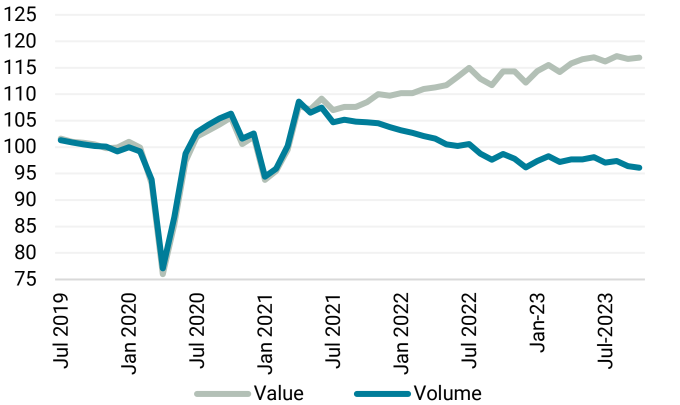
Source: ONS, contribution to monthly growth, volume seasonally adjusted, Great Britain, October 2023

Exhibit 2: Online sales as % of retail sales



Source: ONS

Exhibit 3: Retail sales volume vs. value

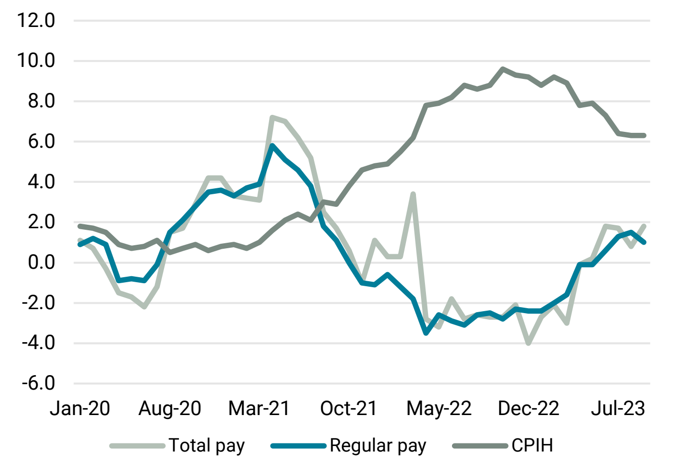


Source: ONS, Bloomberg

Exhibit 4: UK CPI

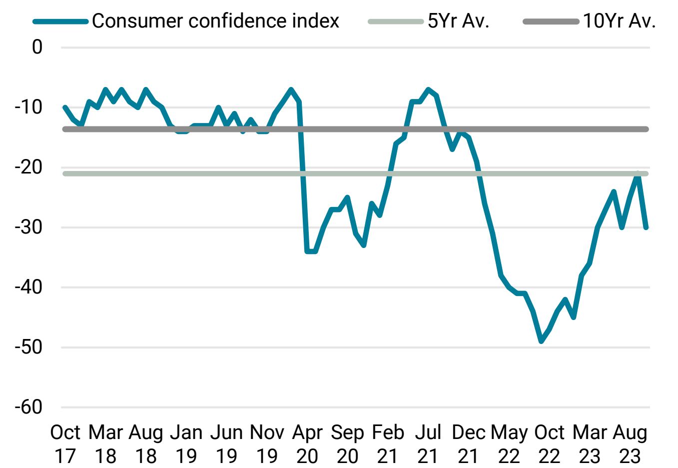
Source: ONS, Bloomberg

Exhibit 5: UK real wage growth (%)



Source: ONS

Exhibit 6: UK consumer confidence index



Source: GfK, Bloomberg

Newsflow

Hotel Chocolat (HOTC) shares soared after it announced a recommended cash acquisition from Mars of 375p per share, valuing the business at a market cap of £534m, a notable premium of 170% above the prior closing price of 139p on 15 November.

City Pub Group (CPC) shares leapt higher after it announced recommended acquisition by Young & Co Brewery, valuing the market cap at £162m, or 145p per share, a premium of 46% to the prior closing price of 99p. Shareholders will receive 198.75p per share in cash and 0.032658 Youngs A shares.

ScS Group (SCS) announced a recommended cash offer of 280p per share, valuing the Group at a market cap of £99.4m. The transaction value represents a premium of c.66% to the prior closing price of 169p. Acquirer Poltronesofà is a leading sofa retailer in Europe, with the ScS deal expanding its footprint into the UK.

Music Magpie (MMAG) shares rose sharply after it confirmed it was in early-stage discussions with BT Group and Aurelius Group over a possible offer to acquire the entire business. The Parties have until 18 December to announce a firm intention.

Fraser Group (FRAS) announced the Disposal of the IP of Missguided to SHEIN. Under the terms of the transaction, SHEIN will acquire the IP and trademarks of Missguided, whilst the Group will retain Missguided's real estate and employees.

Premier Foods (PFD) announced Acquisition of FUEL10K a protein-enriched breakfast brand with a portfolio of granola, oats and drinks products for £34.0m, equivalent to 1.6x projected FY24 revenue of £21m (March year-end). Consideration is funded through existing cash resources with the deal anticipated to be earnings accretive in its first full year.

Marks and Spencer Group (MKS) shares rallied after released its Half-year Report Sales of £6.2bn were +10.8% YOY, with profit rebounding sharply with Adj. PBT of £360.2m +75.3% YOY. Its outlook statement remained cautious, citing erratic weather and higher interest rates as factors that could hit consumer demand in the near term.

ASOS (ASC) released FY23 Results with revenue 11% lower at £3.5bn and Adj. operating profit down 73.1% to a loss of £29.0m (FY22: profit of £44.1m). Net debt of £319.5m is £166.6m higher YOY. It downgraded its outlook for FY24 sales to be down between 5-15% and gave minimal profitability guidance beyond a target to be 'EBITDA positive'. ASOS £500m of bonds now trade at c.60p in the pound implying a yield to maturity of 22.5%- levels that suggest a high degree of default risk.

Next (NXT) released a Q3 Trading Statement with full price sales +4.0% YOY ahead of the 2.0% guided. As a result, full year PBT guidance was increased £10m to £885m. Next continues to assume full price sales for the balance of the year will be lower at 2.0%, reflecting caution for the balance of the year.

Naked Wines (WINE) released a Trading Update and Board Change reducing its outlook for the current year citing weaker than expected trading un the US. Revenue is now expected to fall 12%-16% (previously a fall of 8%- 12%) and Adj. EBIT to be £2m-£6m (from £8m-£12m)**.** Nick Devlin stood down as CEO with immediate effect, with Rowan Gormley assuming Executive Chairman.

Associated British Foods (ABF) the owner of Primark published its Annual Results with Retail revenue of £9.0bn +15% YOY (LFL +8.5%), and Adj. EBIT of £735m down 3% YOY as the business absorbed input cost inflation and higher freight rates. Primark is forecasting sales growth through FY24, driven by increased selling space and LFL growth. Profitability is expected to recover, with EBIT margins to be >10%.

Watches of Switzerland Group (WOSG) released Q2 FY24 Trading Update reported improved Q2 performance with US sales +11% and a good response to its Rolex Certified Pre-Owned programme. FY24 guidance is unchanged. It also published a Long Range Plan setting out a goal of more than doubling sales and profits by FY28 through organic and inorganic growth across UK, USA and Europe.

B&M (BME) released FY24 Interim Results with performance in line and full year EBITDA guidance upgraded. H1 Revenue of £2.6bn is +10% YOY with Adj. PBT of £210m. It has increased UK store estate ambitions and now expects to reach not less than 1,200 B&M UK stores, up from previous guidance of 950 having acquired 51 stores from Wilko in September. FY24 Adj. EBITDA (pre-IFRS 16) guidance increased to £620m - £630m – previous guidance was 'higher than £573m'.

Currys (CURY) reported the Proposed Disposal of Kotsovolos for an enterprise value of £175m on a debt free cash free basis (ex. lease liabilities). The Disposal is aiming to simplify the Group's structure enabling it to focus on its larger markets of the UK & Ireland and Nordics, while simultaneously strengthening the balance sheet.

Revolution Beauty (REVB) released FY24 Interim Results reporting strong recovery in sales +20% YOY to £90.4m and profitability with adj. EBITDA of £6.4m vs. a loss of £7.9m inH1 FY23. Revenue guidance is unchanged at "high single digit percentage growth" implying c.3% revenue growth through H2. EBITDA guidance is upgraded to "low double digit million" vs, previous guidance of "high single digit millions".

Kitwave (KITW) released a pre-close Trading Update confirming a strong H1 performance with positive momentum across all divisions. Trading remains in line with expectations following a significant upgrade in July 2023. In a separate release it announced the acquisition of WLG (Holdings) Limited, which trades as Wolds of Oldham, a composite drinks wholesaler with a turnover of £10.2m in the year to 30 Sep 2022. Consideration was not disclosed but will be funded from existing banking facilities.

Angling Direct (ANG) reported Half Year Results with sales +11.4% to £43.3m (LFL +4.9%). EBITDA of £2.3m is +26.6% YOY. Strong balance sheet with net cash of £17.6m at the 31 July 2023. The Group continues to take market share in the UK and Europe with outlook for the full year unchanged.

Theworks.co.uk (WRKS) released a H1 trading update citing reduced footfall and a resulting slowdown in LFL sales growth as the cause of a downgrade to FY24 guidance. H2 FY24 trading is expected to remain challenging, and consumer spend to be subdued, resulting in the continuation of the increased levels of discounting recently seen across the sector. The Group now expects to maintain a higher level of promotional activity than envisaged at the outset of the year resulting in adj. EBITDA OF £6.0m (previously guided at £10.0m).

Inspecs (SPEC) published a trading update with sales in the 9 months to 30 September +4.6% to £159.1m, with net debt of £21.2m, down £6.4m versus FY22 yearend net debt of £27.6m reported at 31 December 2022. FY23 guidance remains in line with market expectations.

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