



UK Back-to-School Retail Preview 2017: Inflationary Pressures Set to Boost Discount Channels

- 1) We see the pressures of higher inflation fueling an acceleration in market-share gains for discount and value retailers such as Primark and B&M.
- 2) Online retail sales now account for over one-quarter of nonfood sales, and Amazon will be a key back-to-school destination for the 30% of Brits that now have Prime membership.
- 3) In what has now become an annual event, Aldi and Lidl have launched ultralow-priced school uniform ranges, with each chain offering an entire outfit for £3.75.

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We see the pressures of overall inflation on shoppers' wallets this year fueling an acceleration in market-share gains for discount and value retailers.

UK Back-to-School Retail Preview 2017

Back to school may be an important time for students, but it is a crucial event for retailers. The period is one of the biggest revenue opportunities of the year—some reports note that it is the second-biggest seasonal event after Christmas.

Higher inflation levels should support spending growth for back-to-school categories this year. Yet, we see the pressures of higher overall inflation on shoppers this year fueling an acceleration in market-share gains for discount and value retailers, from Aldi and Lidl to Primark and B&M. We also see the structural shift to e-commerce boosting Amazon and other pure-play retailers.

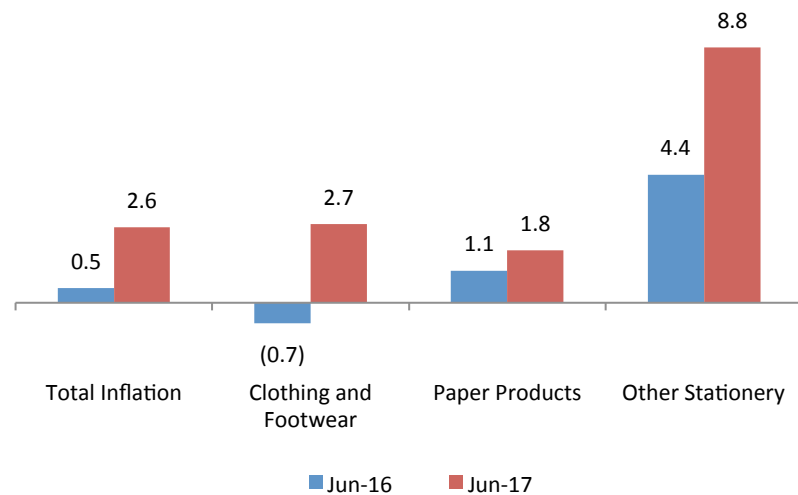
What Will Drive Spending in 2017?

1. Higher Inflation Set to Prompt Renewed Migration to Discount Stores

Average price rises are now outstripping average income growth, and we see the ensuing squeeze on shoppers' spending power as fueling a flight to discount this back-to-school season.

Figures from the Office for National Statistics (ONS) reflect the inflationary burdens which have trickled into retail this year. Below, we chart inflation in total and for selected relevant back-to-school categories. The jump in inflation in stationery and apparel is likely to buoy total growth in these categories.

Figure 1. Consumer Prices Inflation for Selected Categories, June 2017 vs. June 2016 (%)



Source: ONS

We expect discount retailers to be the key beneficiaries ahead of back-to-school 2017.

School uniforms are a major part of the back-to-school budget, accounting for an estimated 58% of spend, according to 2014 data from retail research and consulting firm Conlumino. Therefore, higher inflation in apparel suggests opportunities for value retailers to attract price-conscious shoppers.

This acceleration in the discount segment is borne out by recent results from discounters Primark and B&M: revenues at Primark grew 21% year over year in the first nine months of 2017, and UK comparable sales at B&M surged 7.3% in 1Q18.

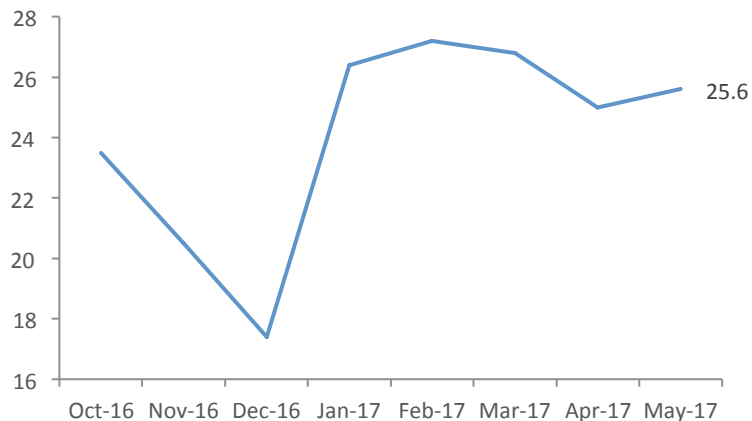
Moreover, data from Kantar Worldpanel has indicated an acceleration in sales growth rates at Aldi and Lidl: in the four weeks ended June 18, Aldi grew sales by 16.2% and Lidl by 18.8%. Aldi and Lidl are once again offering ultralow-priced uniform ranges this year, as we discuss below.

We expect the discount retailers mentioned above to be key beneficiaries ahead of back-to-school 2017.

2. One-Quarter of Nonfood Sales are Now Online, Providing Rich Pickings for Amazon

Year over year, online retail sales continue to grow share of retail, and online-only retailers will once again almost certainly grow share of back-to-school spend this year. Online retail sales now account for over one-quarter of nonfood sales, according to our analysis of ONS data. Given back-to-school shopping spans stationery, apparel and electronics, this season's back-to-school spend could see a similar online/offline split.

Figure 2. UK: Internet Retail Sales as a Proportion of Total Nonfood Sales (%)



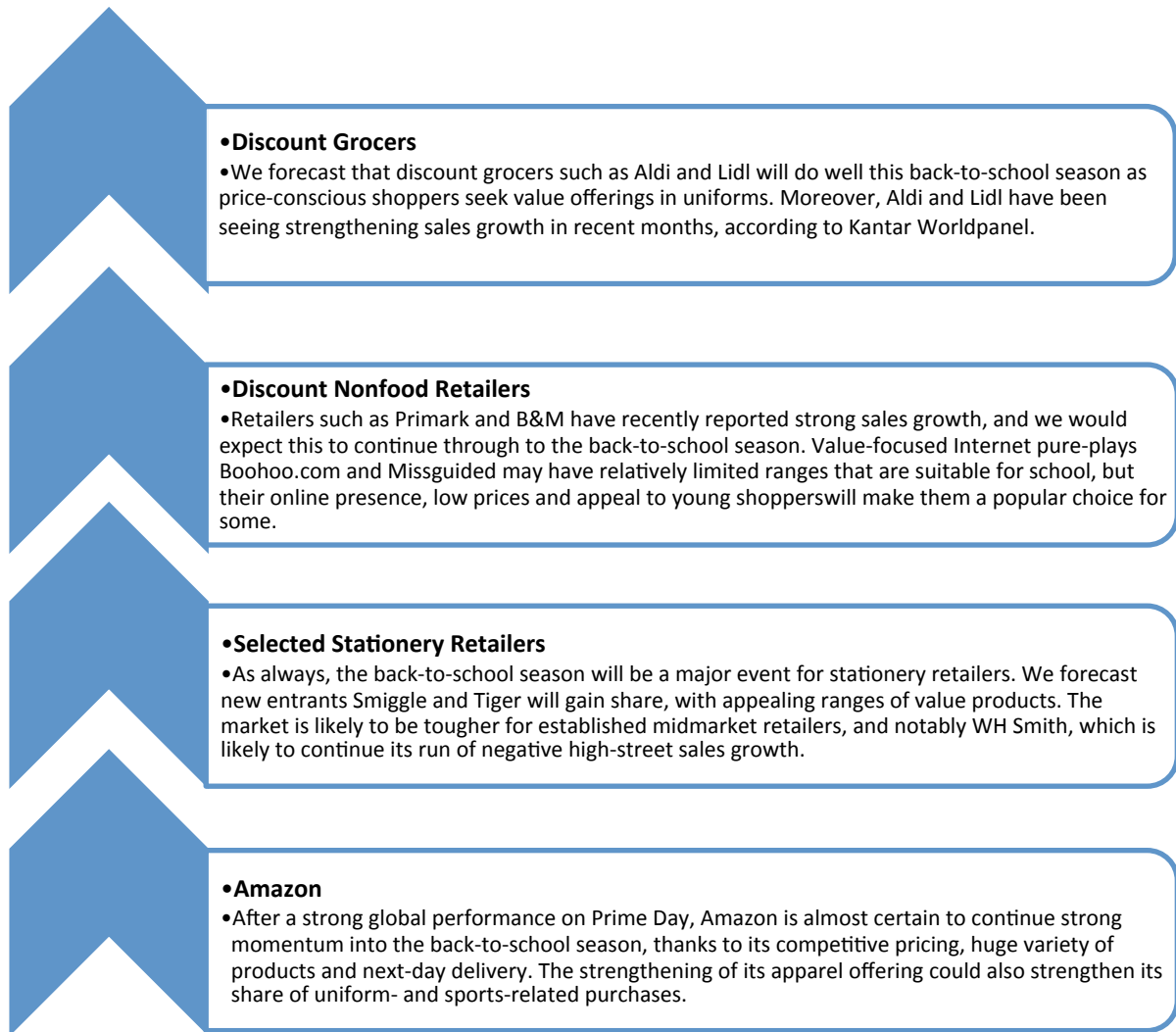
Source: ONS/FGRT

Amazon enjoyed a 26.5% share of UK Internet sales in 2016.

In apparel and footwear, some 24% of sales are now online, according to February 2017 data from Kantar Worldpanel. In consumer electronics, we calculate e-commerce captures around half of all sales, based on data from Statista. So, in these two major back-to-school categories, e-commerce will be a significant channel.

Amazon is likely to be a key beneficiary of the structural shift to e-commerce. The retailer enjoyed a 26.5% share of UK Internet sales in 2016, up from 25.5% in 2015, according to Euromonitor International. In the UK, some 30% of adults now have an Amazon Prime membership, according to a survey by Retail Week and ICM—and for these shoppers, the free, fast delivery will be an incentive to turn to Amazon for back-to-school purchases.

Figure 3. Likely Winners for Back-to-School 2017



Source: FGRT

Back-to-School Category Review

School uniforms, sports kits, stationery and electronics are the major back-to-school categories. We review these categories' prospects below.

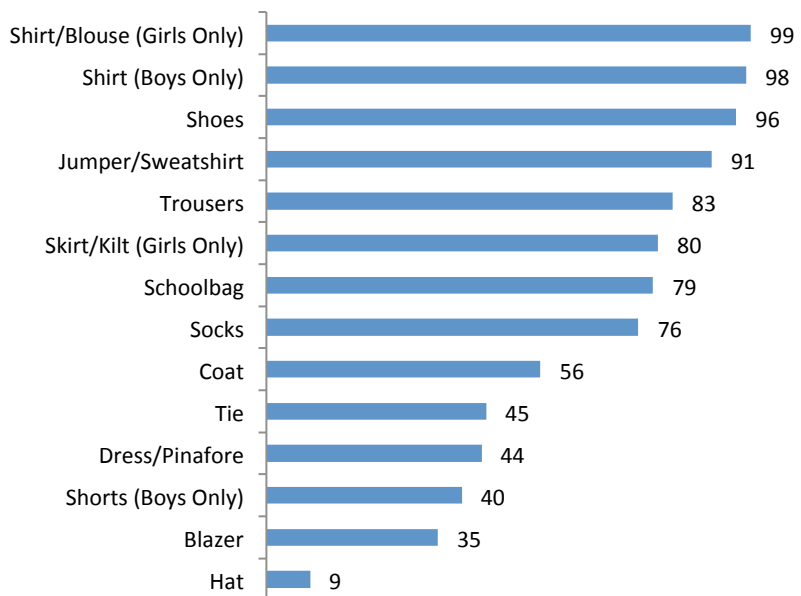
Uniform and Sports Kit

School uniforms is a major expense. Fully 99% of UK parents or carers said that their child's school requires children to wear a uniform, according to a survey by the Department for Education in 2015. And 94% said they are also required to purchase sports apparel. In fact, 50% of parents were expected to buy at least nine items of uniform for their children.



Source: iStockphoto

Figure 4. UK: Proportion of Parents that Are Compelled to Buy Each Category of Clothing (%)



Source: Department for Education, Cost of Uniform 2015

The average cost for an entire school uniform in the UK was £213 in 2015.

The Department for Education estimated that the average total cost for an entire school uniform was £213 in 2015. Moreover, some 21% of schools require parents to buy uniforms from designated specialist shops, and this greatly restricts the ability for them to trade down in core items such as school jumpers, ties and blazers. In fact, only 17% of parents could buy all of their child's school uniform at any shop (down from 22% in 2008), with 62% stating they could buy items from a combination.

For those parents that could shop anywhere, the cost of the entire uniform was considerably lower, at £189.

For the 79% of shoppers who are free to buy uniforms from any store, strong price competition in supermarkets will be highly beneficial. In what has now become an annual event, Aldi and Lidl have launched ultralow-priced school uniform ranges, with each chain offering an entire outfit—two polo shirts, a sweatshirt or jumper, and trousers or pleated skirt—for £3.75. However, for Aldi this is an increase from last year's price of £3.44, showing the inflationary pressures in apparel. This is the same price as last year for Lidl, but it increased prices modestly last year.

With 8.3 million children of school age in 2016, even the lower average spending figure of £189 yields a potential £1.8 billion spending on uniforms. We think this total looks improbably high, and that many shoppers will likely be spending much less than £189 per year, and that some parents will not buy an entire new uniform each year.

The average cost of a sports kit was £88 in 2015, and for those who could purchase from any shop, the total was lower, at £63.13, according to the Department for Education. For 8.3 million school-age children, that suggests a potential total spend of £727 million.

Stationery

Value growth in stationery may be supported by raised inflation.

In recent years, stationery has been a slow-growth category, as tech has replaced some of its functions. This year, value growth in stationery may be supported by raised inflation, which we charted earlier. However, [as we have reported elsewhere](#), there is increasing demand for stationery as a desirable purchase, and growth opportunities have shifted from everyday essentials to desirable, relatively affordable “luxuries.” This has been supported by the increase in newer entrants such as Tiger, Typo and Smiggle. This season, we, therefore, expect basic stationery items to be supported by higher inflation and a degree of “treat” purchasing for more premium lines.



Source: www.smiggle.co.uk

Electronics

One potential hit to retail spending on electronics will be the demands made by schools for parents to lease or purchase electronics through designated companies. Increasingly, schools are asking parents to equip children with electronics such as iPads for classroom use, we have seen a rise in specialized leasing schemes for electronics. The risk to retail is that these schemes switch spending from retail to wholesale.

Many schools have launched programs which lease hi-spec equipment, accessories and insurance to parents under a centralized system, with costs reaching up to £785 per child in some cases. We see this as negative for the retail sector for two reasons: 1) it

may have a knock-on effect to other categories, as many parents will be reluctant to spend big on other back-to-school categories; and 2) these purchases will remove an element of spending from electronic stores, and switch it to wholesale suppliers.

Moreover, this year, inflationary pressures in other categories may squeeze some consumers' willingness to splash out on new electronics.



Source: iStockphoto

Discount grocery retailers, mixed-goods discounters and value apparel stores are likely to be among the winners this year.

Key Takeaways

- We expect raised inflation, which is now outpacing average earnings growth, to prompt an acceleration of market-share gains for discount retailers this back-to-school season.
- Discount grocery retailers, mixed-goods discounters and value apparel stores are likely to be among the winners this year.
- Amazon will gain from the structural shift to e-commerce, its vast product offering and the beneficial effect of Prime memberships.



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