Industry Top Trends Update

Retail and Restaurants

Going from bad to worse

Sarah Wyeth
New York
sarah.wyeth@
spglobal.com
+1 212 438 5658

What's changed post-COVID?

Risks for retailers and restaurants increased dramatically. The COVID-19 pandemic and unprecedented economic shutdown to contain it forced retailers and dine-in restaurants to temporarily close their doors and pivot to digital channels. Consumers, wary or unemployed, limited spending to basics. Grocers and other retailers deemed essential—such as Walmart Inc., Target Corp., Loblaw Cos. Ltd., and Dollar General Corp.—have benefitted.

The hardest hit subsectors are mall-based retailers and casual dining. The shutdown and lingering fears of the coronavirus are likely to weigh on foot traffic to indoor malls and restaurants. Department stores and typical mall-based apparel retailers face the double whammy of being less relevant in consumers' new homebound life.

The sector was already struggling amid secular pressures. Competition for share of wallet, bargain-hunting, conscious consumerism, and the shift to less profitable e-commerce contributed to an annual spec-grade default rate of 10% since 2017.

Increased focus around social risks include health and safety. As retailers and restaurants reopen, they will bear extra COVID-19-related costs of implementing measures to ensure a safe workplace and product.

What is the likely path to recovery?

For many, there won't be a recovery. Defaults and bankruptcies increase every week. With around one quarter of our ratings in the 'CCC' category, the 2020 default rate will easily double relative to recent years.

Essential retailers will be followed by restaurants and nonessential retailers in the recovery. Grocers' higher volumes will likely absorb elevated safety and e-commerce costs. Quick-service restaurants, well-suited to social distancing and a weak economy, should stabilize in 2021. Dine-in restaurants and discretionary mall-based retailers are unlikely to recover until 2023 and beyond.

What are the key risks around the baseline?

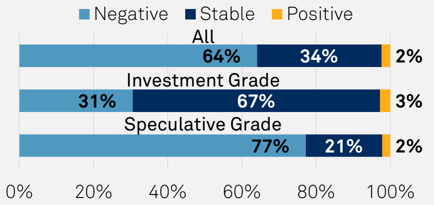
Those that survive face a choppy, nonlinear road to a new normal. Regional hotspots of COVID-19 cases are likely to force retailers and restaurants to reinstate temporary closures and/or capacity limitations. Where in-person sales are permitted, health and safety costs will pressure margins. Ramping up efficient digital capabilities is imperative.

Reverting to shareholder-friendly activity too soon could delay credit quality recovery. Many issuers have tapped debt markets to bolster liquidity. Elevated share buybacks or dividends, funded with excess cash or otherwise, before the operating environment and earnings have recovered could pressure ratings further.

Latest Related Research

- COVID-19 Will Shape The Future Of Retail, May 27, 2020
- Shakeout In Retail, Restaurant Sectors Begins With J. Crew, May 4, 2020
- Impact Of The Coronavirus Likely To Drag U.S. Retail And Restaurants Ratings Down Further, April 24, 2020

Outlook Distribution



Ratings Statistics (YTD)

	IG	SG	All
Ratings	36	102	138
Downgrades	6	38	44
Upgrades	0	8	8

Ratings data as of end-June, 2020

COVID-19 Heat Map

COVID-19, Recession, and O&G Impact

Retail Essential	Low
Restaurants	High
Retail - Non-essential	High

Potential Neg. Long-Term Industry Disruption

Retail Essential	--
Restaurants	Yes
Retail - Non-essential	Yes

2020 Estimates v. 2019

Revenue Decline	EBITDA Decline	Incremental Borrowings
Retail Essential		
No decline	0% to 10%	<5%
Restaurants		
10% to 15%	25% to 40%	>10%
Retail - Non-essential		
15% to 25%	>60%	>10%

2021 Estimates v. 2019

Revenue Decline	EBITDA Decline
Retail Essential	
≥2019	≥2019
Restaurants	
≥2019	≥2019
Retail - Non-essential	
10% to 20%	20% to 30%