GERALD EDELMAN

INDUSTRY UPDATE
QUARTER 3
YEAR 2020

Coronavirus

Industry exposure

How will different industries respond to the coronavirus?

The extent to which businesses have been impacted by the pandemic has very much depended on the sectors they operate in. By identifying the different risk factors and how they affect different industries allows us to see those sectors and businesses most at risk because of the coronavirus, as well as those that are benefitting.

The coronavirus pandemic has had a significant impact on the UK economy. Lockdown restrictions are easing, but subdued consumer confidence is continuing to impact sales and the UK economy has entered its deepest recession since records began. In the three months to June 2020, GDP fell by 20.4%.

The extent to which businesses have been impacted by the pandemic has very much depended on the sectors they operate in. Businesses have been exposed to: **social distancing measures, working from home, supply chain disruption and international trade disruption**. These factors have had a considerable impact on some sectors. Therefore, understanding each industry's exposure to these elements is key to predicting how businesses will respond to the pandemic in the medium term.

Most to least affected industries

Very High	Less affected
Air transport Manufacturing Estate agents	Road transport Financial and professional services

High	Beneficiaries
Construction Sports facilities Accommodation and food services Retail	Online retailing Online food/grocery delivery Technology

Very high risk industries

Manufacturing | Estate agents | Air transport

Manufacturing has been severely impacted by the coronavirus because it is highly sensitive to disruption in international trade. Reduced consumer demand worldwide due to the closure of stores, reduced disposable income, and high levels of uncertainty have also had a negative impact on the industry. In the three months to July 2020, the CBI Industrial Trends Survey reported **the fastest rate of decline in manufacturing output since records began.**

Manufacturing is also a labour-intensive industry, which means working from home policies has reduced, and in some cases halted, production. The UK government is encouraging manufacturing workers to return to work under new social distancing guidelines. Despite this encouragement, many factories will be operating at a reduced capacity, limiting their output potential. Furthermore, with labour representing a high proportion of costs in an industry facing significant revenue decline, over **53% of manufacturers have stated they will be making redundancies in the next six months to reduce costs** (Make UK survey). This is expected to worsen as government support schemes, such as the Coronavirus Job Retention Scheme, end.

The **property and estate agent industry** is another sector at very high risk due its close relationship with the overall health of the economy. Demand for rental properties and, in particular, the purchase of properties is significantly affected by key macroeconomic variables. Higher unemployment (estimated to reach 9% in 2020), lower confidence, and lower economic growth are expected to reduce consumer demand. Despite record low interest rates of 0.1%, **Knight Frank expects residential property sales to drop by 38% in 2020 compared to 2019 levels.**

The **air transport industry** is also amongst the industries that have been worst hit by the coronavirus due to its reliance on international mobility. International travel restrictions have been implemented worldwide. **At Heathrow Airport passenger traffic fell by 96.2%** over the three months to June 2020, compared to the same months in 2019. Whilst many countries have begun lifting travel restrictions, the industry is heavily exposed to changes in government policy. This includes the introduction of new quarantine measures imposed on travellers returning from selected countries. Furthermore, the implementation of social distancing regulations, which include reducing the number of passengers on each flight, is expected to continue to depress passenger numbers going forward.

In anticipation of a sustained decline, British Airways has announced the grounding of their fleet of Boeing 747, with Virgin Atlantic ending its operation at Gatwick airport. In further bad news, **EasyJet, Ryanair, Virgin Atlantic and British Airways are amongst the largest airlines announcing significant job cuts**, of 4,500, 3,000 and 12,000 respectively. This comes after Virgin Atlantic reduced their staff by 3,150 in May 2020.

High risk sectors

Accommodation and food services | Sports facilities | Retail | Construction

The **accommodation and food services** industry saw almost no revenue during April and May 2020 due the UK's lockdown. Many of these businesses were able to reopen from 4 July, but strict social distancing measures remain in place. This will limit customer numbers and make it increasingly difficult for many establishments to remain profitable.

Recent government comments also suggest that, in the event of a severe coronavirus flare-up, schools will be prioritised over hospitality services. Pubs and restaurants therefore face the risk of future lockdown restrictions and further losses of revenues.

The full effect of the coronavirus on the industry is expected to be felt once the government furlough scheme ends. **Over 60% of the workforce in the sector was on furlough between 15-28 June**, according to ONS figures. As businesses take on employee costs alongside a shortfall in revenue, large-scale redundancies and business closures are expected.

Sports facilities, gyms, leisure centres and indoor pools were permitted to reopen on 25 July. However, strict regulations are now in place. Social distancing measures limit the number of customers on the premises, constraining revenue. The number of people returning to the gym is also expected to be low, heavily impacting the industry. During lockdown, many gyms offered online training and coaching programmes, however this has not been sufficient to sustain industry income. **Revenue for the current year is expected to decline by 27.6%.**

The **retail sector**, which had already been struggling due to the growing popularity of online shopping and high rent and rates costs, has been severely impacted by the coronavirus. The sector has suffered from high levels of supply chain disruption and social distancing measures.

A reduction in manufacturing output is expected to reduce inventory, inflating purchasing costs and adversely affecting margins. Clothing supply is at risk, with an estimated 18.9% of total imported clothing originating from China.

Rising costs is expected to occur alongside decreasing revenue. Whilst some retail stores were able to adapt to a surge in online shopping following the closure of all non-essential stores, the volume of **retail sales fell by 18.1% in April from the previous month**, and 22.6% when compared to April 2019 (ONS). Household goods, fuel sales and clothing have been the most exposed sub-sectors.

Whilst ONS data shows that the reopening of retail stores on 15 June saw a spike in demand, recent payment data from July suggests that sales have trailed off since the start of July.

Social distancing regulations on stores are likely to have a longer-term impact on the whole sector, with lower levels of footfall and a move towards increased e-commerce sales. Significant numbers of physical shops are expected to close once government support schemes finish, with many retailers such as John Lewis and M&S announcing significant job losses.

Output in the **construction industry** is forecast in a 'best-case scenario' to fall by 25% in 2020 (Construction Products Association). Following some uncertainty over the classification of construction workers under 'essential' and 'non-essential' businesses, the UK government encouraged construction firms who had not yet reopened to return to work on 10 May. BuildUK estimates that 86% of construction sites in England and Wales were open in the week following. Despite this, building site closures and social distancing measures are expected to have **brought work on 220,000 new homes to a standstill,** with the HIS Markit UK Construction PMI falling by 8.2 in April 2020. This represents the steepest contraction in output on record.

Growth in the industry is expected to resume from 2023. However, the recovery is reliant on the UK economy picking up due to the close link between construction and the demand within the property market. Accordingly, the longer the overall economy takes to recover from the pandemic, the more affected the construction industry is expected to be.

Less affected sectors

Road freight transport | Financial and professional services.

The **road freight transport industry** is not expected to be significantly affected by the coronavirus. As 'essential' businesses, the industry was able to continue trading, remaining broadly exempt from international travel restrictions.

The industry is exposed to lower industry demand from major importing countries and non-food retailers; however, the downstream demand from food retailers has significantly increased. This has been driven by supermarkets and other food retailers expanding their orders. **Food demand is expected to mitigate the lower demand in other areas**, such that industry revenue is expected to remain similar to previous years.

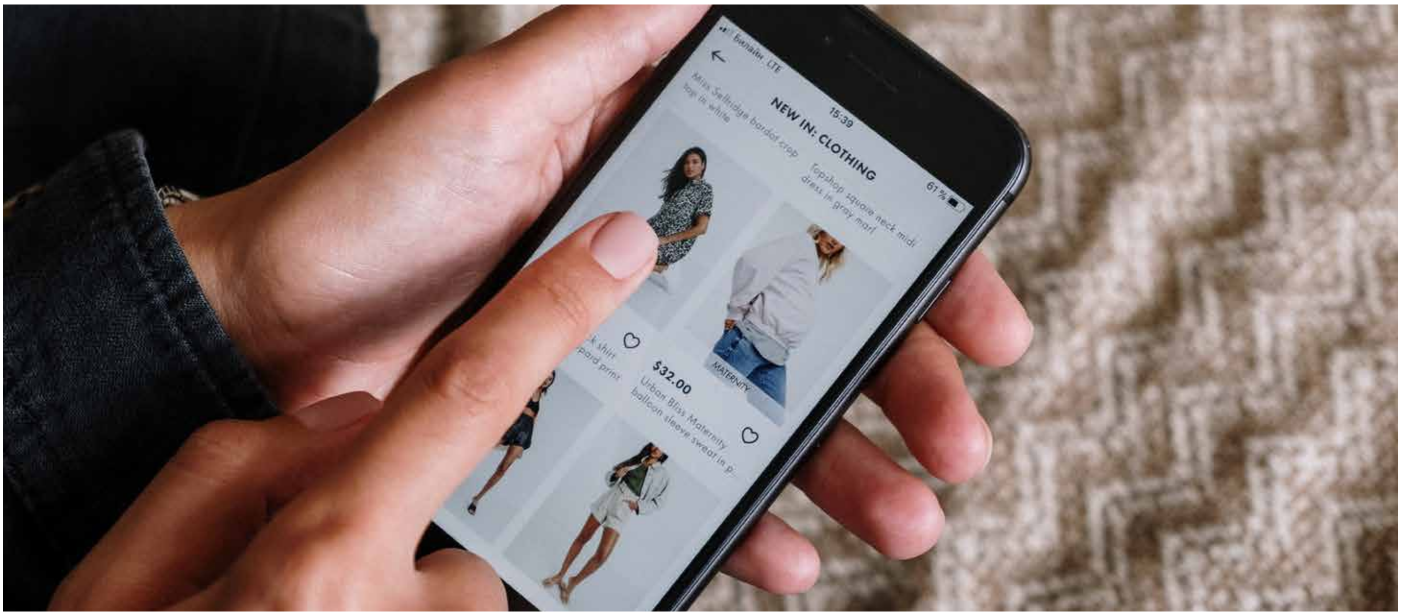
Financial and professional services are not forecast to experience a severe impact from the outbreak of the coronavirus and UK lockdown. These industries benefit from the ability to work remotely, with many firms looking to adopt working from home policies going forward.

Whilst a reduction in the number of businesses, and therefore clients, is expected to negatively affect industry demand, this impact is expected to be short term. Industry revenue is forecast to bounce back from 2021, which is reliant on a UK economic recovery this year.

The sector has also seen an increase in demand from businesses trying to understand the full impact of the coronavirus on their operations, which is expected to offset the declining demand for consultancy services.

Lower business expenditure in the short term will limit the demand for non-essential financial services. However, financial services may benefit from higher volumes of corporate transactions in the second half of the year as distressed companies are acquired by those who have continued to trade strongly throughout the pandemic. The legal sector is forecast to benefit from a rise in insolvencies, increasing advice over redundancy procedures from employers and employees alike, and disputes resolution relating to supply chain disruptions.

The Law Society reported a **30% increase in enquires and requests to draw up wills** in April 2020. This is expected to help the industry off-set any negative impacts to revenue.



Beneficiaries

Online retailing | Online food and grocery delivery | Certain technology businesses

Online food delivery and online grocery delivery platforms are among the sectors set to 'benefit' from the outbreak of the coronavirus. Both sub-sectors were classified as essential by government guidelines, allowing them to operate during the initial UK lockdown. Low exposure to social distancing disruption meant that operations were able to continue as normal. Both sub-sectors have experienced a boost in sales at the beginning of the outbreak, with consumers substituting dining out with takeaway and home-cooked meals.

Takeaway demand was also boosted by the difficulty that many consumers had in booking grocery delivery slots during the early stages of the pandemic. In response to higher demand, supermarkets such as **Tesco and Sainsbury's increased their delivery slot numbers by 200% and 75% respectively** in May 2020. This trend of increased home delivery of groceries and pre-prepared food is expected to continue in the medium term, as consumers remain wary of visiting restaurants and supermarkets.

Online retail stores benefit from low labour requirements and limited international trade exposure. During the UK 'lockdown', the industry saw their sales as a percentage of total retail sales increase from 19% in February 2020 to 32.8% in May 2020. Whilst this figure fell slightly in June to 31.2%, the forecast closure of many physical retail stores will sustain online sales in the long term.

A recent survey by Channel Advisor showed that **42% of customers will shop online more frequently post-lockdown**, suggesting a permeant change in the way that people shop.

Many **technology businesses** have benefited from the pandemic as they are able to offer digital solutions to assist people with new ways of working and living. As businesses have adapted to, and adopted, new working from home policies, the **demand for tech services has increased significantly and is likely to be sustained going forward**. An obvious example is the increase in reliance on video conferencing, which has become indispensable to remote workers. The soaring demand for the services offered by tech businesses has driven an 'unprecedented' rise in the value of many tech businesses, particularly large US tech stocks such as Apple, Amazon and Microsoft. The share price of Apple, for example, has doubled in the 21 weeks since its March 2020 low and means that the Company was recently crowned the title of the first US company to breakthrough the $2 trillion value mark.

Gerald Edelman services

Our teams are fully functional and able to help you navigate through these unprecedented times, by providing a range of services, including:

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- Business valuations
- M&A
- Corporate Finance

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Formed in the late 1940s, we have established ourselves as one of the leading mid-tier businesses in the UK. We deliver a wide range of financial and strategic business advice, working closely with our clients to help them achieve their aspirations.

Today, we remain committed to business and have a philosophy and an aspiration to deliver genuinely exceptional experiences to our clients and others. We have 17 partners and approximately 140 employees. Ranked 51st in the Accountancy Age Top 50+50 Accountancy Firms 2019 and 51st in the Accountancy Top 75 firms 2019, Gerald Edelman is well placed to service the differing needs of our clients – no matter how large or small.

Gerald Edelman is not *just* an accountant. We strive to break away from the term ‘accountant’, thinking beyond compliance and identifying ourselves as a ‘client’s first port of call’.

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