

**Exchanges at Goldman Sachs with Jennifer Davis and Vishaal Rana
Hosted by Jake Siewert, Global Head of Corporate Communications
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Jake Siewert: This is Exchanges at Goldman Sachs where we discuss developments currently shaping markets, industries, and the global economy. I'm Jake Siewert, Global Head of Corporate Communications here at the firm.

Today, we're going to talk about state of consumer retail sector and how consumer retail companies are poised to navigate the post-pandemic era, God willing. To do that we're joined by Jen Davis, Head of Retail Investment Banking, and Vishaal Rana, a Managing Director in the Consumer Retail Group in the Investment Banking Division here at Goldman Sachs. Jen, Vishaal, welcome to the program.

Jennifer Davis: Thanks for having us, Jake.

Vishaal Rana: Thanks for having us.

Jake Siewert: All right, Jen, let's start with you. We're obviously at a critical juncture as the economy starts to reopen or has reopened in many places. And vaccines continue to roll out broadly. What does this turning point mean for retail and the companies you're covering?

Jennifer Davis: Yeah, it's a tremendously interesting time. So, I think it's a great time to be talking about all of this. Look, not surprisingly, the retail sector has continued to massively evolve over the last 12 months. E-commerce volumes grew as much in the first quarter of 2020 as they did in the prior ten years, which is just incredible for us.

So, when we think about that critical inflection point, Jake, that you asked about, the turning point means that retailers can really start thinking now more offensively versus defensively, which is where they were a year ago.

What we're seeing is that leading retailers are embracing this opportunity to win new customers by leveraging lessons they've learned from the last year and investing in strategies to serve customers well, wherever, and whenever they want to shop. You have customers who are expecting, you know, a seamless omnichannel experience overall. Their journey evolves. It may start online. It may stop in the store. It may, ultimately, end again online. And so, really retailers need to be ready to pivot

and serve customers where they want to be served today.

Jake Siewert: So, Vishaal, as Jen mentioned, consumer preferences have been reshaped by the pandemic and shifted pretty dramatically. So, how has a more consumer-first approach transformed the landscape of retail? And how can new entrants benefit from the shift?

Vishaal Rana: Yeah, look, consumer first is the right word, Jake. I mean, historically, traditional retailers and Wall Street analysts have been focused on, you know, a metric called same-store sales. So, what is the change in performance over an individual period for a store network? And today, while same-store sales are still really important for most of our retail clients, as Jenn mentioned, consumers are more nimble in their shopping patterns. Some go to the store. Some buy on a mobile device. Some have a subscription. Nearly everyone has all of these things.

So, look, new metrics have been introduced. Average order value. Average customer spend per year. Customer retention rates. These were all historically just, quote, direct to consumer metrics that have now permeated to more traditional brick and mortar retailers as well.

So, if you're a new entrant, it's easier than ever to put up an online storefront, right? So, e-commerce enablement companies like Shopify, they help create a storefront. They manage the payment. They manage back office. I mean, frankly, the fact that Shopify is one of the most successful technology companies in the world is a proxy for how new entrants are benefiting from this new environment.

And so, I think the idea and the proliferation of new brands selling directly to the consumer has clearly been a multi year trend. That isn't going away. And is going to be accelerated through consumers wanting newness all the time.

But look, there are really challenges still for new entrants. Right? The cost of customer acquisition is really high. And for that to be beneficial for that new entrant over time it requires a lot of scale. And I think that gets to a little bit of why there's been some resiliency with a lot of traditional retailers because they actually have that scale.

Jake Siewert: So, Jen, at the onset of the pandemic we saw a lot of companies that you cover accessing the capital markets to

raise debt, in many cases just for their own survival and to get through it. But not long after that we saw a pretty big shift in the capital markets towards growth and innovation. Talk about advising your clients through those valleys and peaks, as it were.

Jennifer Davis: Yeah, it's amazing to me, again, just the change in 12 months where a year ago it was advising our clients whether they were drawing down entirely on their revolvers. They were issuing new credit facilities and new revolvers purely to have liquidity on their balance sheets. And they were unsure about, you know, how deep the trough would be. And now, literally within 12 months, you've got still incredibly low borrowing costs. You've got debt markets and equity markets that have been extremely attractive across the board. And I think you've seen a complete shift towards really tapping those markets for opportunistic and offensive purposes.

Here we sit in April. And in the last three months, in our sector we've seen IPOs of Petco, Poshmark, Doc Martins, Doordash, Airbnb, thredUP, just to name a few within the larger consumer retail sector. It really shows the attraction of the equity markets and how all of those debt and equity options are available to our clients.

I think the other thing that's happened as a result of that, Jake, is just an incredible growth in M & A because CEOs are much more confident in the recovery at this point and can think about funding M & A. You've got M & A volumes that are up 100 percent year over year, which is incredible when you think about a year ago we were just starting the pandemic.

I think the other thing we'd be remiss to not mention but has dramatically impacted the sectors that Vishaal and I cover is the growth in the SPAC market. The SPAC market has been, you know, close to 20 percent of global M & A volumes. And in our sector that tends to be more small and midcap transactions. It's been almost half of US M & A, between 1 to 5 billion dollars. And so, again, you're seeing just this incredible attractiveness and appetite from investors to invest in this sector.

Jake Siewert: So, talk a little bit about differentiation within the sector. Obviously, some stay-at-home businesses have benefited dramatically. But they're poised to see a little bit of a drop off. And how about reopening businesses? And what are they looking at right now?

Jennifer Davis: And not surprisingly, right, the stay-at-home last year, whether it was anything related to home, home improvement, sporting goods, sports equipment, at-home fitness, food delivery, cleaning, center of store, grocery all took off last year. And you saw a real dampening in terms of restaurants, travel and leisure, branded apparel and accessories, when people other than athleisure, you know, wear to work and wear for special occasions, all of that dropped off dramatically.

Now what you're seeing is really a 1-2 punch that those sectors that had really been the reopening businesses and had taken a pause last year are starting to dramatically recover as people are seeing the reopening cadence happening. But you're still seeing strength in the stay-at-home categories. And I think that's really being driven by the incredible consumer stimulus that's been put into the economy by the government. When you think about, you know, the \$1,400 stimulus added on top of the 600 put in consumers' pockets in December, that coupled with a high savings rate through last year means that consumers have a big checkbook to still spend this year. And so, despite the pivot from stay-at-home to reopening names, you're still seeing relative strength across the board.

Jake Siewert: So, a lot of discussion even before the pandemic about the future of brick and mortar. Now, as we enter the post-pandemic era, what is the fate of brick and mortar, particularly as direct-to-consumer is not just rising, but tending to dominate? Vishaal, let's start with you.

Vishaal Rana: As Jen referenced earlier, e-commerce has been on a tear for multiple years now. It's been rapid in growth. Call it 15 to 20 percent year over year. And 2020 saw unprecedented volumes in terms of consumers being able to buy from vendors directly. And US retail sales were huge, right? It's, like, over 4 trillion dollars. And so, there's a lot of dollars to go around between direct-to-consumer concepts and brick and mortar retailers.

Now, when you think about e-commerce growth, what's interesting is that, look, Amazon's always been the highest percentage of both e-commerce value and a disproportionate amount of its growth. What's interesting, in 2020 is that while the absolute dollars of growth for Amazon were tremendous, its total overall contribution stagnated a bit. You know, mainly because of the rise of traditional brick and mortar concepts being more relevant online. So, Target, Walmart, Costco, Kroger. You sort of name large retailers that have traditionally been getting to

consumers via their store footprint, they've been able to figure out a way to have a more seamless shopping experience for their customers.

So, on the fate of brick and mortar, to your question. Look, the demise of many shopping malls has been well documented. But believe it or not, there are still numerous unit growth stories out there in retail. Value retailers, certain restaurant concepts. You noted direct-to-consumer companies are dominating. A great number of them now have a brick-and-mortar footprint themselves. And the reason for that is that these are really efficient customer acquisition vehicles. They're great marketing. They give you control over your cost versus being beholden to paying search engines or to social media companies where often the formula on how you pay for advertising can change.

So, I think the punch line on the fate of brick and mortar is expect a continued focus on seamless commerce. So, you know, what is the ubiquity of your store in any different form, whether it is physical, online, mobile, whatever it may be? That's kind of the fate. What is more difficult and obvious is being a pure play only brick and mortar retailer, of which I think there are very few left. I'm not sure you could name a whole lot that are, at least, of scale.

Jake Siewert: So, Jen, how about your perspective on this? It's obviously a changing world. My wife and I drove by a mall the other day and had to explain to our four kids what a mall was. So, what's your perspective on the fate of brick and mortar?

Jennifer Davis: Yeah, I think it's a great question, Jake. I'm not surprised to hear of that conversation you had to have with your kids. And I would, you know, echo and underscore a lot of what Vishaal said. The reduction in retail square footage is not new news. Right? Last year, retail chains closed about 8,700 stores in the US after shuttering 9,800 in 2019. So, you're talking, you know, close to 19,000 stores being closed. And when you talk about malls, there are external estimates out there that say a quarter of the country's malls will close by 2023. So, I fully agree with Vishaal. It's not going away entirely. It's going to be a reduced store footprint. And this kind of omnichannel, all in one experience is going to be something that all retailers and brands will need to address.

What they're doing is evolving to be more experiential or more convenient. So, you've got retailers adding things like virtual

fitting rooms. Hosting live stream shopping events. Allowing shoppers to make virtual appointments with sales associates and stylists. Really, malls and stores need to evolve to give customers a fun destination reason to come in to shop on one hand. Or a super convenient way to shop on the other.

And I think, Vishaal talking about Target and Walmart are great examples of that. They've been, you know, two retail behemoths investing very heavily in this in terms of buy online, pick up in store. Or using their stores today to be e-commerce fulfillment centers.

I think the other thing that retailers are doing to evolve from a brick-and-mortar standpoint, Jake, is really thinking about personalization. It's been interesting to me, there was a McKinsey study recently that said that 100 percent of top quartile retailers cited omnichannel personalization as a top five priority. But only 15 percent of retailers have actually implemented personalization across channels. So, the ability to meld that online and offline experience will be critical to the bricks and mortar success going forward too.

Jake Siewert: Well, to your point about malls evolving. My 12-year-old son had read about the indoor wave pool at American Dream Mall. And he's very excited to check that out one of these days. Not to mention the indoor skiing.

Jennifer Davis: Exactly. The family destination of fun.

Jake Siewert: Exactly. So, we may find ourselves in a mall before long.

Vishaal, let's continue on the topic of direct-to-consumer. There's been an evolving narrative around both the power not danger of user and customer data. How do you think that narrative will play out in retail? And how will the continued intersection of consumer and tech inform strategic activity around the industries?

Vishaal Rana: The customer data topic is going to get increased scrutiny. I think there is a lot of literature on this already over the last few quarters. And the focus on big technology and where they are with owning customer data is of enormous importance to the government. And for retailers, you know, look, there's been an evolution. Right? In traditional brick and mortar retailers, the retailer used to get point of sale data which would help them understand what was bought, which store.

Help them manage inventory. And the evolution today is that big technology, including big retailers, obviously, have far more information that is potentially helpful as they think about marketing and chasing new customers. But to your observation, Jake, it is likely to get more scrutiny.

But overall, you know, a broader question on technology and retail, the impact of strategic activity. We think it's going to continue. At a starting point, retailers have focused largely on building out their own technology capabilities. That's the first point. Right? They have built out proper e-commerce, you know, websites. They have built out a proper back office. They have tried to create their stores into distribution centers if necessary. So, billions of dollars have been spent by retailers to sort of catch up to the Amazon impact over the last ten years.

On strategic activity, look, there have been some parties who have done a lot, like, you know, Walmart obviously made a huge investment in Flipkart in India. That's an example of looking at the distribution channel in an emerging market and saying that's the right way to go. And I think where you're going to see retailers probably spend more dollars on the M & A side, maybe, around last mile as technologies emerge that are going to be helpful for their own distribution as their distribution becomes much more, as we talked about earlier, seamless oriented. How can they do that? So, Instacart became a huge company on its own by helping retailers do that. Are there other things out there that retailers will invest in or purchase, potentially, to enable their experience from an e-commerce perspective? And I think we're going to see some of that.

What's a little bit less clear is traditional brick and mortar retailers buying, so-called, D to C companies. I think that's been sort of a mixed bag to date so far mainly because the companies tend to be quite different in their approach, and tend to be quite different in terms of the cultural aspects of each of those companies.

Jake Siewert: So, obviously, technology was a huge accelerant during the pandemic. Another thing that really saw a big uptick was all things sustainable. How do you see technology and sustainability colliding in retail? And how do you think this focus on climate, in particular, will have an impact on the industry over the next few years? Jenn, why don't you start on that.

Jennifer Davis: Yeah, look, most retailers and brands today understand the link between doing good and bottom-line impact. 80 percent of retailers believe that company actions matter to consumers. And 64 percent believe those actions affect purchase decisions. And so, companies are aware of these facts. They're evolving their business models to address it.

A great example is the fashion industry. They're responsible for large biodiversity impacts across the value chain, including generating up to 10 percent of global carbon emissions and 20 percent of global industrial water pollution. So, companies, what we're seeing them doing is really using technology to address these major issues. There are examples where they're implementing a digital strategy from supply chain to customer experiences using RFID and blockchain DNA tagging to help with traceability, transparency, and material recovery. We've got companies like Inditex who are partnering with universities like MIT to research initiatives into the circular economy and really talk about using technology to address sustainability and recycling with textiles. So, I think, you know, companies are embracing the "doing well by doing good" philosophy and investing heavily to address those.

The other big impact that we've seen as a result of the focus on sustainability is the growth of the resale in the rental market. And so, we've seen companies like The RealReal and Poshmark and thredUP, as I mentioned, you know, having IPOs in the past couple of years.

The resale market last year grew at 25 times the rate of the broader retail sector. And it's supposed to grow to twice the size of the fast fashion industry by 2029. And so, consumers are really voting with their wallets in terms of companies that they're spending money with and recognizing the impact of sustainability on their purchase decisions.

Jake Siewert: So, Vishaal, your take on the intersection between technology and sustainability in retail today?

Vishaal Rana: Yeah, look, I think well captured by Jen. I think the two things I'd add, number one, it's a board level focus. Okay? Like many things that have evolved over the last ten or 15 years, board are paying enormous amount of attention to sustainability, the impact on climate, and, importantly, whether or not their company is well positioned. You know, some of that comes from because it's the right thing to do, as consumers want of it. And some of it is because there's an enormous amount of

ESG capital that has been raised. And the markets have spoken. And the markets are saying, "Hey, large public corporate in the retail space, if you want us to participate in your equity story through us investing, we'd like to see metrics. We'd like to sort of see progress along sustainability goals that you have outlined." And so, we think the retail community is going to need and is being quite thoughtful on this, especially on this area of creating sort of closed loop sustainability system. You know, meaning making sure that, you know, whatever products are used or consumed are being traced in a way that the retailer understands where they're coming from and is able to sort of control it a bit.

So, I think that this topic is of enormous focus. And you should expect a combination of investors along with boards that are seeing where their consumer is to continue to focus on it.

Jake Siewert: All right. Well, Vishaal, Jenn, thank you very much for joining us today for this great discussion.

Jennifer Davis: Thanks so much for having us.

Vishaal Rana: Thanks, Jake.

Jake Siewert: That concludes this episode of *Exchanges at Goldman Sachs*. Thank you very much for listening. And if you enjoyed this show, we hope you subscribe on Apple Podcasts and leave a rating or a comment.

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