What Is the Retail Disruption Investment Opportunity?

- The retail sector is undergoing a massive transformation as consumers move online and away from in-store shopping.
- COVID-19 may have accelerated these trends as store closures are estimated to reach new records.
- For legacy retailers, the adoption of online shopping doesn't solve all problems, and the distinction between online and bricks-and-mortar retail is still one worth making.

ONLINE RETAIL—Early, incessant, and accelerating change

For many consumers, pandemic life has probably included a steady stream of deliveries as many bricks-and-mortar stores were forced to temporarily close or set capacity restrictions, or as shoppers opted for online shopping over in-person interactions. However, the shift from bricks-and-mortar retail to online shopping was taking place long before COVID-19, and for investors, it's a transformation that may represent a compelling investment opportunity. The long-term trends driving retail disruption include:

EASE

More than a quarter of consumers in the U.S. make an online purchase at least once a week.

MILLENNIALS

65% of millennials, the largest generation in the U.S., say they prefer to shop online rather than in-store.

BANKRUPTCIES

Over 100 retailers, including JC Penney and Sears, have filed for bankruptcy since 2015.

STORE CLOSURES

Despite a few retailers opening stores, 2019 saw a record-breaking 9,300 store closures. Current predictions for 2020 are more than double that number.

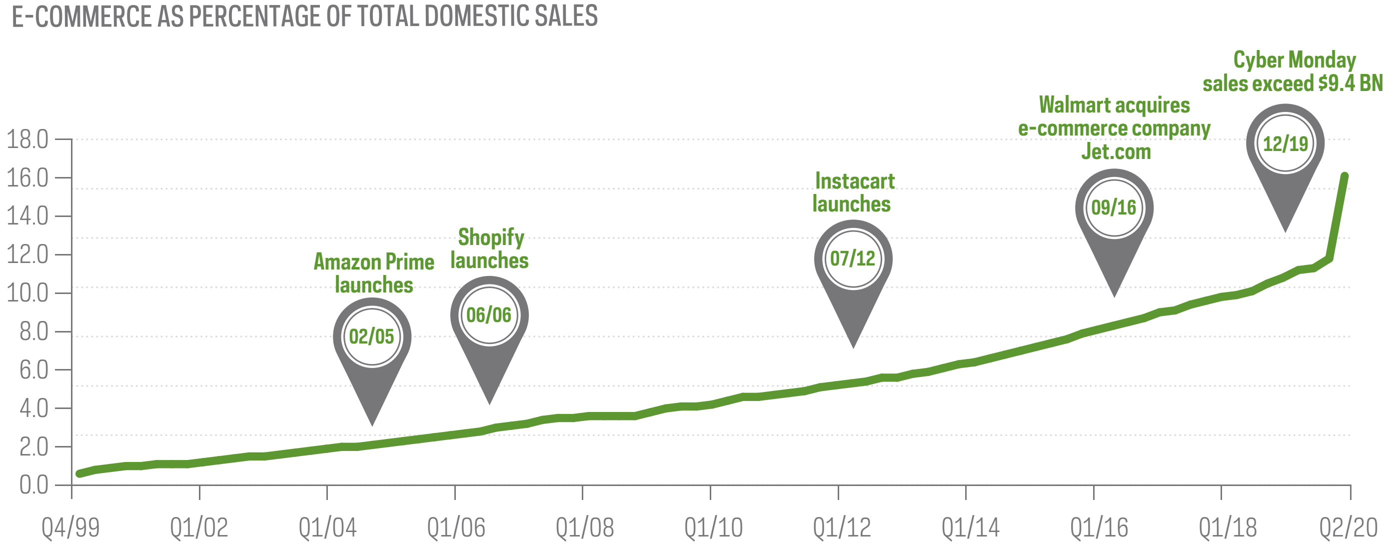
In addition to these long-term secular trends, there are several emerging behaviors that may continue to put pressure on traditional retail, especially as Generation Z, the first truly digital generation, gains buying power.

THE RISE OF GEN Z BUYING POWER

- U.S. smartphone purchases make up just over 5% of total online retail, but that number is increasing.
- Social media and influencer culture are beginning to shape online shopping habits.
- Instagram's in-app purchase feature is predicted to generate $10 billion revenue in 2021.

Given this backdrop, it might come as some surprise that before COVID-19 hit, bricks-and-mortar was still responsible for an overwhelming majority of U.S. retail sales. Online retail's march has, however, been incessant and accelerating, with its penetration increasing nearly three times as fast in the second half of the 2010s compared to the first half, yet still accounted for only 11% of total retail sales in the U.S. at the end of 2019. The pandemic lockdown further accelerated this trend, as the second quarter of 2020 found e-commerce rising to about 16% of total U.S. retail sales.

Figure 1: Online Retail Market Share



STORE CLOSINGS AND BANKRUPTCIES—Adding pandemic fuel to the retail fire

While online retail has grown, many malls have emptied and stores have closed, even during what—until recently—was a strong U.S. economy. The pandemic has, of course, intensified the rate, with recent predictions putting 2020's store closure rate at more than double that of 2019—which was already a record-breaking year.

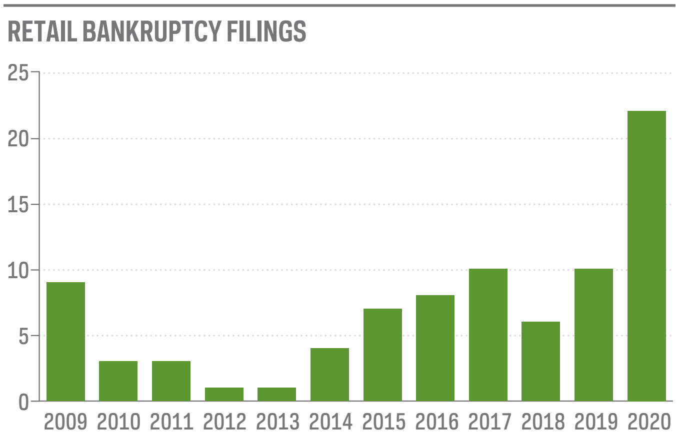
Store Closures
2020: 25,000*
2019: 9,300
2018: 5,844

*expected

A permanent acceleration?

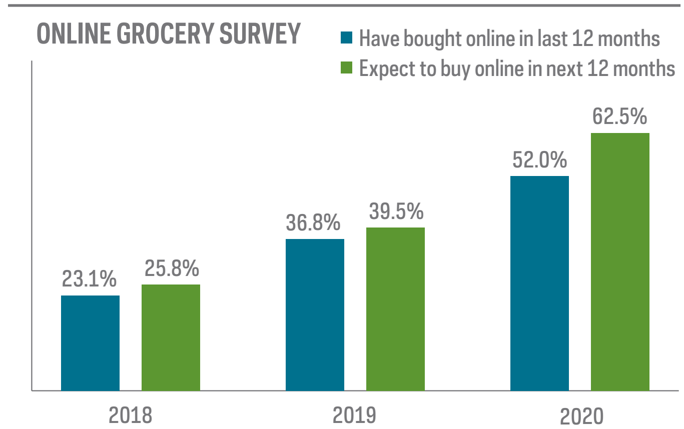
It is tempting to chalk this up to a temporary impact of COVID-19, but there are signs that the pandemic is in fact accelerating an existing long-term trend and furthering opportunities for e-commerce growth. One glaring example: e-commerce food and beverage sales increased over 100% in the second quarter of 2020 from the first quarter, and more than 220% over the second quarter of last year. Groceries, specifically, are online retail's least-penetrated category, accounting for less than 3% of the category spend in 2019. Coresight Research forecasts an increase of 40% in online grocery sales in 2020, on top of 22% growth in 2019. And remember, grocery stores were considered essential businesses and open during the entire lockdown period.

Figure 2: Bankruptcies



Data represents filings from 1/1- 8/6 for each year shown above.

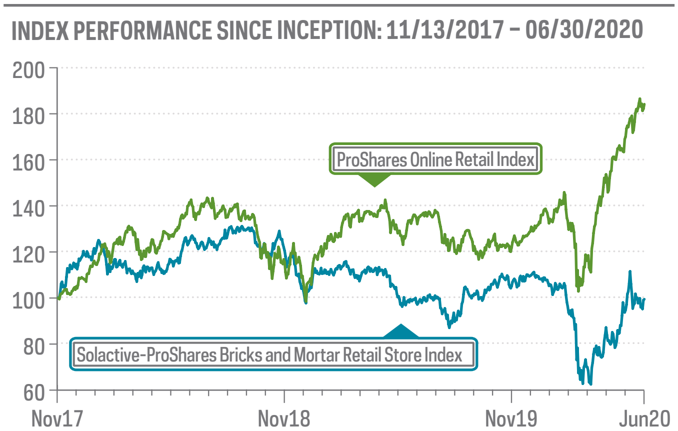
Figure 3: Online Grocery Survey (Coresight Research)



New habits may very well stick around in a vaccinated post-pandemic world. Chewy, the rapidly growing pet e-commerce retailer, noted this in their Q2 earnings release...

> "We believe the increased demand levels we are experiencing are here to stay and reflect an acceleration of e-commerce adoption that is not likely to return to pre-pandemic levels."
>
> — Chewy, Inc.

Figure 4: ProShares Online Retail vs Solactive-Proshares Bricks and Mortar Index Performance



ONLINE VS. BRICKS-AND-MORTAR RETAIL— A distinction (still) worth making

A look at the top-ten online retailers shows Walmart as a solid number two, and several other legacy bricks-and-mortar players such as Home Depot, Best Buy, Macy's, and Target make the list as well. Has the line been blurred to such an extent one can no longer isolate online and bricks-and-mortar retail for investment purposes? Let's start with the basics:

- The Solactive ProShares Bricks and Mortar Retail Store Index has over 40 constituents (as of 6/30/20).
- The index includes companies that receive at least 50% of their revenue from retail operations and 75% or more of their retail revenue from in-store sales, making them highly exposed to the shift to online retail.

The basics are clearly reflected in performance. The Solactive-ProShares Bricks and Mortar Retail Store Index has dramatically underperformed the ProShares Online Retail Index.

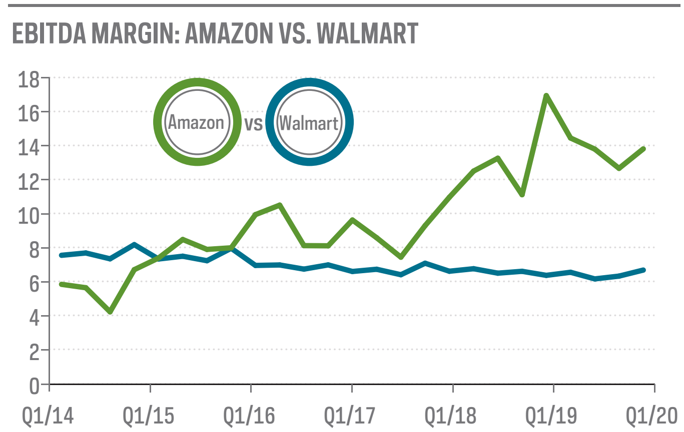
Even for those legacy bricks-and-mortar companies that are having some success in online retail and creating an "omni channel" model, the future may not be so bright. Over the last several years, as Walmart has successfully grown its online business to the coveted second-place position, its margins have declined.

Meanwhile, as Amazon continues to grow, its margins have expanded, serving as a reminder of the performance challenges facing even those bricks-and-mortar retailers who are having online success. Legacy cost structures, bloated footprints, and multiple distribution platforms all pose long-term profitability challenges. It's another key reason that, indeed, the distinction between online and bricks-and-mortar retail is still an investment distinction worth making.

Figure 5: Amazon vs Walmart Margins

E-commerce sales in billions (estimated)			
	2017	2018	2019
Amazon	$177.87	$232.89	$280.52
Walmart	$15.04	$20.95	$28.8

Sources: Amazon, Statista, Amazon Annual Reports, 2020. Walmart, TREFIS 2020.



EBITDA: Earnings before interest, taxes, depreciation and amortization.

THE RETAIL DISRUPTION OPPORTUNITY

ProShares offers three ETFs that enable investors to tap into the long-term trends of retail disruption. Explore the suite of products.

CLIX

PROSHARES LONG ONLINE/SHORT STORES ETF (CLIX)

Lets investors potentially benefit from both the potential growth of online companies and the decline of bricks-and-mortar retailers through a long/short construction.

ONLN

PROSHARES ONLINE RETAIL ETF (ONLN)

Tracks retailers that principally sell online or through other non-store channels.

EMTY

PROSHARES DECLINE OF THE RETAIL STORE ETF (EMTY)

A dedicated short fund designed to benefit from the decline of traditional bricks-and-mortar retailers.

Sources: eMarketer, ("Millennials shopping preferences") March 2019; Statista ("global e-commerce penetration rate") July 2020; Episerver, Reimagining Commerce 2020 ("weekly online shopping"); eMarketer, April 2019 ("mobile retail e-commerce"); CNBC ("Instagram's new e-commerce feature"), April 2019; CNBC ("Retail Store Closures 2018 and 2019") March 2020; Bloomberg ("Bankruptcy chart, expected 2020 store closures"), August 2020; CB Insights ("List of bankruptcies") July 2020; Coresight Research, number of retail store closures; Retail Dive ("Running list of retail bankruptcies"), July 2020; Coresight Research U.S. Online Grocery Survey 2020.

As of 6/30/20: ONLN and CLIX allocations to Amazon 24.08%, 24.08% and Chewy 4.07%, 4.07%. CLIX also has short side allocations to Walmart 2.15%, Target 2.15%, Macy's 2.27%, Best Buy 2.21%, Home Depot 2.19%. EMTY index holds Macy's 2.27%, Best Buy 2.21%, Home Depot 2.19%, Walmart 2.15% and Target 2.15%. Holdings are subject to change.

Any forward-looking statements herein are based on expectations of ProShare Advisors LLC at this time. ProShare Advisors LLC undertakes no duty to update or revise any forward-looking statements, whether as a result of new information, future events, or otherwise.

Investing is currently subject to additional risks and uncertainties related to COVID-19, including economic, market and business conditions; changes in laws or regulations or other actions made by governmental authorities or regulatory bodies; and world economic and political developments.

ProShares EMTY seeks a return that is -1x the return of an index (target) for a single day, as measured from one NAV calculation to the next. Due to the compounding of daily returns, EMTY's returns over periods other than one day will likely differ in amount and possibly direction from the target return for the same period. Investors should monitor their holdings consistent with their strategies, as frequently as daily. For more on correlation, leverage and other risks, please read the prospectus.

Investing involves risk, including the possible loss of principal. These ProShares ETFs are non-diversified and entail certain risks, which may include risks associated with the use of derivatives (such as swap agreements, futures contracts and similar instruments), imperfect benchmark correlation, leverage and market price variance, all of which can increase volatility and decrease performance. EMTY seeks short exposure and should lose money when its index rises. CLIX's short positions are not intended to hedge the portfolio in market downturns, but rather to allow stocks with unfavorable outlooks to contribute to performance. Short positions lose value as security prices increase. Investments in the consumer discretionary and retailing industries are subject to risks such as changes in domestic and international economies, interest rates, competition and consumer confidence; disposable household income; consumer tastes and preferences; intense competition; changing demographics; marketing and public perception; and dependence on third-party suppliers and distribution systems. Investments in smaller companies typically exhibit higher volatility. Smaller company stocks also may trade at greater spreads or lower trading volumes, and may be less liquid than stocks of larger companies. ONLN and CLIX invest in international investments, which may involve risks from: geographic concentration, differences in valuation and valuation times, unfavorable fluctuations in currency, differences in generally accepted accounting principles, and from economic or political instability. In emerging markets, many risks are heightened, and lower trading volumes may occur. Please see their summary and full prospectuses for a more complete description of risks. **There is no guarantee any ProShares ETF will achieve its investment objective.**

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