Retail Disruptors

The spectacular rise and impact of the hard discounters
EFMI FOOD RETAIL’S

HYPER COMPETITION IN THE WORLD OF GROCERY RETAIL

- CONVENTIONAL GROCERY RETAILERS
  - FOODSERVICE CHANNEL
  - FOOD SPECIALTY STORES
  - ONLINE CHANNEL
  - LOW END (NON-FOOD) RETAIL
  - HARD DISCOUNT
  - THE WALL?
“Retailing is the fine art of separating consumers from their money”
MY VIEW ON RETAIL MARKETS

- Good quality, low price
- Good quality, average price
- Added value, relevant price

Commodity
Mid-market
Specialty
The “wish line”: This is what most people want
MY VIEW ON RETAIL MARKETS

- Organic
- Local
- Convenience
- High quality & good taste
- Fair trade

Graph:
- Commodity
- Mid-market
- Specialty
“Poor people need low prices, but rich people love them”
MY VIEW ON RETAIL MARKETS

The “wish to pay” line
THIS RESULTS IN A ‘BELL-CURVED’ MARKET

Good quality, low price

Good quality, average price

Added value, relevant price

Market size

Commodity

Mid-market

Specialty
MOST HOUSEHOLDS INCOMES ARE LIMITED – AND NOT EVENLY DISTRIBUTED
PURCHASING POWER OF MOST HOUSEHOLDS IS MEDIocre AND STABALAZING

Average income standard household in the Netherlands

<table>
<thead>
<tr>
<th>Soort post</th>
<th>Bedrag netto per maand (in €)</th>
<th>Achtergrond</th>
</tr>
</thead>
<tbody>
<tr>
<td>Inkomsten</td>
<td>2372</td>
<td>Incl. kinderbijslag en kindgebonden budget</td>
</tr>
<tr>
<td>Huur</td>
<td>528</td>
<td>Gemiddelde huur</td>
</tr>
<tr>
<td>Overige vaste lasten</td>
<td>670</td>
<td>Gas, elektriciteit, water, verzekeringen, internet, tv, telefoon, vervoer</td>
</tr>
<tr>
<td>Reserveringsuitgaven</td>
<td>416</td>
<td>Kleding, inventaris, onderhoud huis en tuin, niet-vergoede ziektekosten</td>
</tr>
<tr>
<td>Huishoudelijke uitgaven</td>
<td>592</td>
<td>Voeding, was- en schoonmaakmiddelen, persoonlijke verzorging</td>
</tr>
<tr>
<td>Inkomsten - uitgaven</td>
<td>+ 166</td>
<td>Geen uitgaven begroot voor sociale participatie (gemiddeld 257 euro) of auto (al snel 400 euro)</td>
</tr>
</tbody>
</table>

Development of GDP per capita in EU (purchasing power standard)
SO, MOST MARKETS IN FOOD RETAIL LOOK A BIT LIKE THIS
THE MID-MARKET STILL HOLDS ‘THE BULK’ OF THE SALES

**MID-MARKET**

60-80% OF SALES
When markets mature the ‘Well curve’ becomes more dominant
Arbeidsmarktontwikkelingen in 16 Europese landen
Verandering in procentspunten, 1993-2010 (bron: Goos et al. 2013)
THE WELL-CURVE: POLARIZING CUSTOMERS

- Good quality, low price
- Good quality, average price
- Added value, relevant price

DISCOUNT

DIGITAL

Commodity

Mid-market

Specialty

Growth potential

Average market growth rate
THE WELL-CURVE: POLARIZING CUSTOMERS

- Good quality, low price
- Good quality, average price
- Added value, relevant price

EASY TO SHOP

MORE EXPERIENCE

Average market growth rate
“The rise and impact of the hard discount business model”
Hard discounters distinguish themselves compared to regular grocery retailers as follows:
- Very limited assortment
- Strong focus on private labels
- Small and ‘Spartan-like’ stores
- Unbeatable price quality

In most countries traditional grocery retailers consistently lose sales and margin to hard discounters.
The impact of hard discounters

HUGE IMPACT IN NETHERLANDS

MARKET SHARE ALDI AND LIDL 2000-2018

Bron: Nielsen, 2018
**Future Outlook: Hard Discounters Will Be Quality Discounters**

### Operation ANIKO

**Ontdek de nieuwe Aldi**

ANIKO = ALDI NORD INSTORE KONZEPT

All Aldi-Nord stores in Europe will be remodelled.

Total remodelling cost: EUR 5.2 billion (EUR 1 mln per store)

ANIKO is based on 8 pillars (see next)

<p>| | |</p>
<table>
<thead>
<tr>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>1</strong></td>
<td>Modern stores</td>
</tr>
<tr>
<td><strong>2</strong></td>
<td>Increased choice in vegetables &amp; fruit</td>
</tr>
<tr>
<td><strong>3</strong></td>
<td>In-store oven, freshly baked bread</td>
</tr>
<tr>
<td><strong>4</strong></td>
<td>Fresh meat in standing shelves</td>
</tr>
<tr>
<td><strong>5</strong></td>
<td>Menu suggestions / recipes</td>
</tr>
<tr>
<td><strong>6</strong></td>
<td>More ready-to-eat assortment</td>
</tr>
<tr>
<td><strong>7</strong></td>
<td>More organic and fair trade</td>
</tr>
<tr>
<td><strong>8</strong></td>
<td>Energy saving refrigerators</td>
</tr>
</tbody>
</table>
OPERATION ANIKO: ALL ALDI NORD STORES WILL BE RENEWED

ANIKO-RENEWAL IN NL PER JAN 2019

NUMBER OF STORES REMODELLED PER YEAR/MONTH

- REMODELLED TO ANIKO
- (NOT) YET REMODELLED TO ANIKO

Bron: Inventarisatie EFMI Business School, december 2018
The impact of hard discounters

DISRUPTIVE IMPACT IN THE UK

The spectacular rise and impact of the hard discounters

SOURCE Based on 2017 data from Kantar Worldpanel
The impact of hard discounters

Evolution of market share for major UK supermarkets (Jan-15 vs Dec-18)

- **Tesco**
- **Sainsbury's**
- **ASDA**
- **Morrisons**
- **Aldi**
- **Lidl**

DISRUPTIVE IMPACT IN THE UK: 2015-2018
IS THE US MARKET THE NEXT HARD DISCOUNT BATTLEGROUND?

US STORES

ALDI

2,000+


0 200 400 600 800 1,000 1,200 1,400 1,600 1,800 2,000

Deal extends discount grocer’s market reach into metro New York

Lidl US to acquire Best Market
The unique hard discount business model
THE IMPACT OF ROTATION

• Hard discounter: 2,000 items, Euro 180,000 per store per week, average price per item 1.80 -> rotation 50 per item per week
• Conventional retailer: 20,000 items, Euro 240,000 per store per week, average price per item 2.40 -> rotation 5 per item per week

• With regard to fresh products, what is the impact of the difference in rotation for:
  • Freshness and food waste?
  • Out-of-stock?
  • In-store handling costs?
  • Working capital?
  • Buying office?
THE HARD DISCOUNTER BUSINESS MODEL

Drivers of competitive sustainable advantages

Low cost driver 1: Efficient retail operation
- Low HQ costs
- Efficient warehouse and transportation
- Efficient store operation
- Smart packaging

Low cost driver 2: Knowledgeable and efficient procurement
- National brand as quality benchmark
- Buying large volumes at low prices
- Deep knowledge of supply chain

Low cost driver 3: Efficient financial management
- Low capital intensity
- High sales per m2
- High rotation -> good cash position
- Solid operating income, high ROI
The impact of hard discounters

HUGE PRICE ADVANTAGE HARD DISCOUNTERS

Table 2.4: Price indices of private label in conventional retailers and Lidl in 2016

<table>
<thead>
<tr>
<th>Retailer</th>
<th>Country</th>
<th>Copycat private label conventional retailer</th>
<th>Private label Lidl</th>
</tr>
</thead>
<tbody>
<tr>
<td>Albert Heijn</td>
<td>The Netherlands</td>
<td>69</td>
<td>54</td>
</tr>
<tr>
<td>Tesco</td>
<td>United Kingdom</td>
<td>51</td>
<td>38</td>
</tr>
<tr>
<td>Delhaize</td>
<td>Belgium</td>
<td>63</td>
<td>45</td>
</tr>
<tr>
<td>Carrefour</td>
<td>France</td>
<td>69</td>
<td>51</td>
</tr>
<tr>
<td>Edeka</td>
<td>Germany</td>
<td>81</td>
<td>40</td>
</tr>
<tr>
<td>Carrefour</td>
<td>Spain</td>
<td>75</td>
<td>56</td>
</tr>
<tr>
<td>Tesco</td>
<td>Poland</td>
<td>62</td>
<td>56</td>
</tr>
<tr>
<td>SPAR</td>
<td>Austria</td>
<td>66</td>
<td>40</td>
</tr>
<tr>
<td>COOP</td>
<td>Switzerland</td>
<td>66</td>
<td>37</td>
</tr>
</tbody>
</table>

Average: 67 46

SOURCE: Based on 2016 data from IPLC
The impact of hard discounters

AND QUALITY IS ALSO (VERY) GOOD

<table>
<thead>
<tr>
<th>Dishwasher tablets</th>
<th>Laundry detergent</th>
<th>Diapers</th>
<th>Orange juice</th>
<th>Ground coffee</th>
</tr>
</thead>
<tbody>
<tr>
<td>Aldi</td>
<td>Lidl</td>
<td>Aldi</td>
<td>Sainsbury’s</td>
<td>Aldi</td>
</tr>
<tr>
<td>Lidl</td>
<td>Tesco</td>
<td>Lidl</td>
<td>Lidl</td>
<td>Lidl</td>
</tr>
<tr>
<td>Tesco</td>
<td>Sainsbury’s</td>
<td>Tesco</td>
<td>Morrisons</td>
<td>Sainsbury’s</td>
</tr>
<tr>
<td>Morrisons</td>
<td>Aldi</td>
<td>Asda</td>
<td>Tesco</td>
<td>Asda</td>
</tr>
<tr>
<td>Morrisons</td>
<td>Sainsbury’s</td>
<td>Morrisons</td>
<td>Aldi</td>
<td>Morrisons</td>
</tr>
</tbody>
</table>

NOTE: Which! did not always report the quality rating for every Big Four (Tesco, Sainsbury’s, Asda, and Morrison) retailer.

SOURCE: Based on various issues of Which! (2016, 2018)
THE HARD DISCOUNTER BUSINESS MODEL

Drivers of competitive sustainable advantages

Low cost driver 1: Efficient retail operation
- Low HQ costs
- Efficient warehouse and transportation
- Efficient store operation
- Smart packaging

Low cost driver 2: Knowledgeable and efficient procurement
- National brand as quality benchmark
- Buying large volumes at low prices
- Deep knowledge of supply chain

Low cost driver 3: Efficient financial management
- Low capital intensity
- High sales per m2
- High rotation -> good cash position
- Solid operating income, high ROI

Multiplier

Large store network
THE HARD DISCOUNTER BUSINESS MODEL

Customer value proposition

Multiplier

Drivers of competitive sustainable advantages

Unbeatable price-quality

Large store network

Low cost driver 1: Efficient retail operation
- Low HQ costs
- Efficient warehouse and transportation
- Efficient store operation
- Smart packaging

Low cost driver 2: Knowledgeable and efficient procurement
- National brand as quality benchmark
- Buying large volumes at low prices
- Deep knowledge of supply chain

Low cost driver 3: Efficient financial management
- Low capital intensity
- High sales per m2
- High rotation -> good cash position
- Solid operating income, high ROI
The impact of hard discounters

THE HARD DISCOUNTER BUSINESS MODEL

Figure 2.1 Hard discounter business model

- Limited assortment → Small stores
- Consumer desire to simplify choice → High volume/SKU
- Irresistible value for money → Long-term relations with suppliers
- High quality, low price → High profitability
- Low overhead → Low staffing costs
- Low store investment → Rapid store network expansion
- Incumbent myopia → Uniform format
- Short payback period → Quick return

EFMJ BUSINESS SCHOOL
The impact of hard discounters

Very solid financial performance of HD’s

<table>
<thead>
<tr>
<th></th>
<th>Conventional grocery retailer</th>
<th>Hard discounter</th>
<th>Hard discounter advantage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Revenues</td>
<td>100</td>
<td>100</td>
<td></td>
</tr>
<tr>
<td>Cost of goods sold</td>
<td>(73)</td>
<td>(81)</td>
<td></td>
</tr>
<tr>
<td>(including product loss)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Gross margin</td>
<td>27</td>
<td>19</td>
<td>-8</td>
</tr>
<tr>
<td>Store-related operating costs</td>
<td>(12)</td>
<td>(7)</td>
<td>+5</td>
</tr>
<tr>
<td>- Labour</td>
<td>(8)</td>
<td>(5)</td>
<td></td>
</tr>
<tr>
<td>- Other costs (rent, depreciation, utilities…)</td>
<td>(4)</td>
<td>(2)</td>
<td></td>
</tr>
<tr>
<td>Operating margin (store based)</td>
<td>15</td>
<td>12</td>
<td>-3</td>
</tr>
<tr>
<td>Overhead (SG&amp;A)</td>
<td>(11)</td>
<td>(6.5)</td>
<td>+4.5</td>
</tr>
<tr>
<td>- Central staffing</td>
<td>(3)</td>
<td>(1.5)</td>
<td></td>
</tr>
<tr>
<td>- Logistical costs</td>
<td>(4)</td>
<td>(3)</td>
<td></td>
</tr>
<tr>
<td>- Marketing</td>
<td>(4)</td>
<td>(2)</td>
<td></td>
</tr>
<tr>
<td>Earnings before interest and taxes</td>
<td>4</td>
<td>5.5</td>
<td>+1.5</td>
</tr>
</tbody>
</table>
FINANCIAL PERFORMANCE BIEDRONKA

**Sales & Services**

<table>
<thead>
<tr>
<th>Year</th>
<th>Biedronka</th>
<th>Distribution Portugal</th>
<th>Others</th>
</tr>
</thead>
<tbody>
<tr>
<td>2013</td>
<td>7,703</td>
<td>3,986</td>
<td>140</td>
</tr>
<tr>
<td>2014</td>
<td>8,432</td>
<td>4,033</td>
<td>215</td>
</tr>
<tr>
<td>2015</td>
<td>9,206</td>
<td>4,237</td>
<td>285</td>
</tr>
<tr>
<td>2016</td>
<td>9,781</td>
<td>4,436</td>
<td>404</td>
</tr>
<tr>
<td>2017</td>
<td>11,075</td>
<td>4,609</td>
<td>592</td>
</tr>
</tbody>
</table>

**EBITDA Margin**

- **Biedronka**
  - 2013: 7.8%
  - 2014: 6.8%
  - 2015: 7.0%
  - 2016: 7.2%
  - 2017: 7.3%

- **Pinga Doce**
  - 2013: 5.8%
  - 2014: 5.8%
  - 2015: 5.5%
  - 2016: 5.4%
  - 2017: 5.3%

- **Recheio**
  - 2013: 5.2%
  - 2014: 5.3%
  - 2015: 5.4%
  - 2016: 5.3%
  - 2017: 5.3%
“How does hard discount growth impact conventional retailers?”
The impact of hard discounters
Consumers tend to become more price focussed and less focussed on added value.
Consumers tend to become more price focussed and less focussed on added value.

Consumers tend to evaluate conventional retailers less on price and better on added value.
HARD DISCOUNTERS CAUSE A ‘CONTRAST’ EFFECT

Low price  |  High added value
---|---
Low added value  |  High price
HARD DISCOUNTERS CAUSE A ‘CONTRAST’ EFFECT

Initial sweet spot
HARD DISCOUNTERS CAUSE A ‘CONTRAST’ EFFECT

High added value

Low price

Initial sweet spot

Conventional retailer image

High price

Low added value
HARD DISCOUNTERS CAUSE A ‘CONTRAST’ EFFECT

- High price
  - High added value
    - Conventional retailer image
  - Low added value
    - HD image

- Low price
  - Low added value
    - Initial sweet spot
HARD DISCOUNTERS CAUSE A ‘CONTRAST’ EFFECT

High added value

Low price
- Initial sweet spot
- New sweet spot
- HD image

High price
- Conventional retailer image

Low added value
HARD DISCOUNTERS CAUSE A ‘CONTRAST’ EFFECT

- **High added value**
  - New CR image
  - Conventional retailer image

- **Low added value**
  - Initial sweet spot
  - New sweet spot

- **Low price**
  - HD image

- **High price**
HARD DISCOUNTERS CAUSE A ‘CONTRAST’ EFFECT

- High added value
  - Initial sweet spot
  - New sweet spot
  - HD image
  - New CR image
  - Conventional retailer image

- Low added value
  - Low price
  - High price
HARD DISCOUNTERS CAUSE A ‘CONTRAST’ EFFECT

High added value

Low price

High price

Low added value

Initial sweet spot

New sweet spot

New CR image

Conventional retailer image

HD image

Initial sweet spot

New sweet spot

New CR image

Conventional retailer image

HD image
The impact of hard discounters

EFMI Business school

HD HAVE CREATED THEIR OWN BLUE OCEAN

Figure 6.2 Retail market space map after entry of hard discounters

- "Blue Ocean" vs "Red Ocean"
- Added-Value Image vs Price Image
- Hard discounters (Trader Joe's, Lidl, Aldi, Biedronka, BIM)
- Mainstream retailers
- Warehouse clubs
- Brand discounters
- Proximity retailers
DEVASTATING IMPACT OF HARD DISCOUNT GROWTH IN UK

Tesco reveals 9,000 jobs set to be hit in major restructuring amid 'challenging' market

Tesco said that it hoped to redeploy up to 50% of the staff affected into other customer service roles (Source: Getty)

Tesco has revealed plans to axe up to 9,000 jobs as part of a cost-cutting move that will involve the grocer trimming its head office and closing tens of fresh food counters.
HOW CAN CONVENTIONAL RETAILERS COUNTER HARD DISCOUNTERS?
STRATEGIC OPTIONS CONVENTIONAL RETAILERS

![Diagram showing strategic options for conventional retailers](image-url)
Is TESCO now adopting a downgrading strategy for its main chain?

Tesco is planning to remove 20 per cent of its products from shelves as part of its efforts to regain ground from discount retailers.

As The Times reports, Tesco chief product officer Andrew Yaxley told suppliers last week that the supermarket giant will make swingeing cuts to its product offering, particularly in household departments.

It's the latest such move under chief executive Dave Lewis, who has reduced the number of products on Tesco shelves from nearly 90,000 in 2014 to around 40,000 today.

Tesco enjoys the largest market share of the 'Big Four' UK supermarket retailers, a position that was bolstered by the competition watchdog's rejection last month of a proposed merger between Asda and Sainsbury's.

But in recent years the UK's largest supermarket has lost ground to discount retailers such as Aldi and Lidl, which have expanded rapidly.

Aldi's market share grew to 8 per cent earlier this year, putting it just 2.3 percentage points behind Morrisons, the smallest of the Big Four.

In response Tesco has attempted to cut costs, including through the loss of tens of thousands of jobs.
STRATEGIC OPTIONS CONVENTIONAL RETAILERS?

Coordinated Strategic Responses

- Price Image (Price level, Promotions)
- Added-Value Image (Assortment, Quality, Service, Convenience)
- Defensive strategies
- Downgrading
- Fighting back
- Value-redefinition

JUMBO supermarktien
STRATEGIC OPTIONS CONVENTIONAL RETAILERS

Coordinated Strategic Responses

- High Value improvement
- High Added-Value Image (Assortment, Quality, Service, Convenience)
- Low Price Image (Price level, Promotions)

- Defensive strategies
- Downgrading
- Fight back

JUMBO foodmarkt LEIDSCHE RIJN
HOW RETAILERS CAN CAPTURE MORE VALUE FROM NATIONAL BRANDS?

<table>
<thead>
<tr>
<th>BRAND IMPORTANCE</th>
<th>CATEGORY IMPORTANCE</th>
</tr>
</thead>
<tbody>
<tr>
<td>High</td>
<td>Cell II: Increase slotting allowances</td>
</tr>
<tr>
<td></td>
<td>Cell III: Intensify category management; appoint category captain</td>
</tr>
<tr>
<td>Low</td>
<td>Cell I: Reduce brand assortment</td>
</tr>
<tr>
<td></td>
<td>Cell IV: Exclusive relations with select brand manufacturers</td>
</tr>
</tbody>
</table>

- Cell II: Increase slotting allowances
- Cell III: Intensify category management; appoint category captain
- Cell I: Reduce brand assortment
- Cell IV: Exclusive relations with select brand manufacturers