Western European Retailers | At cross-roads between revolution or evolution | Four strategies are possible | What could be the future growth path of your company?
WESTERN EUROPE HAS BECOME A PATCHWORK OF RETAIL STORE FORMATS — DIFFERENT STRATEGIES NEEDED
REVOLUTION OR EVOLUTION?

Today, Western European retailers are facing their biggest challenge yet. In mature markets with near-zero population growth, the economic crisis has eroded the little consumer purchasing power that was left and, secondly, competition has become cutthroat. The top three retailers in the UK, France, Belgium, Germany and the Netherlands control between half and three-quarters of the market. Shareholders are seeing their value dissipate. Carrefour’s 2011 share performance, for example, was down 37%. Western retailers need to find their way back to growth.

In our recent study "Revolution or Evolution", Roland Berger Strategy Consultants and EFMI have mapped out four strategies for growth. Whether they take an evolutionary or a revolutionary approach, retailers will have to raise their game at home, change the game in existing markets and break new ground if they are to stay on – or return to – the path towards growth.

THE CONQUEST OF GROWTH

Since the industrial revolution, retail concepts have been introduced, pursued and abandoned in a continuous quest for new and faster growth. As a result, Western Europe has become a patchwork of store formats. Supermarkets hold sway in the Netherlands, Belgium and the United Kingdom; discount is king in Germany; and in France, hypermarkets still dominate the retail landscape.

But in light of today’s stagnating markets, growth seems out of sight for many retailers. As markets mature, autonomous growth is slowing. Competition authorities are not likely to allow M&A-driven growth in most Western European markets and this will hurt their profitability per square meter as well. Ahold and Tesco, for example, have shares of 34% and 31% in their respective home markets and will probably be denied the full acquisition of competitors. Belgian, German and French market leaders have lower market shares and may be able to take over some smaller competitors, but their scope to grow is limited, too. As a result, major retail players are reviewing their growth strategies. Though much will depend on economic performance overall, discounters and convenience stores are expected to gain some market share this year as all major players are investing in convenience store concepts, e.g. Carrefour City and Tesco Express.

And while many supermarkets will reverse downwards trend through store reshaping, hypermarkets will face rough waters.
But growth is not impossible. Revolutionary and evolutionary approaches are within reach. Our growth matrix distinguishes four growth strategies: retailers can circle the wagons at home, strike out abroad with existing concepts, change markets by importing new concepts to either home or new markets, or pioneer entirely new retail models.

**THE RETAIL GROWTH MATRIX**
From short term focus to long term strategy

1. **RETAIL FORTRESSES – DEFEND AND EXPAND HOME MARKETS**
At home, retailers will need to raise their game to defend and expand market shares. They should rethink old retail models (what we call “Retail 1.0”), rebalance their revenue mix, be consistently creative in marketing and really get under their customers’ skin. Margins and sales will profit from one (or more) of the following actions.

- **Reshaping formats** is a way to provide customers with a more up-to-date shopping experience. Carrefour is reshaping 92 European hypermarkets into “Carrefour Planets” that are user-friendlier and more practical. This trend is also being seen in supermarkets.

- **Private label products**, our analysis shows, can realize up to 25% higher margins at 15% lower retail prices, growing profits rather than revenue. As consumers spend more and more money on private label products, these also allow retailers to differentiate and cater to a wide range of needs. Tesco offers a fine example with its Tesco Finest, Tesco Organic and Tesco Value lines.

- **Creative marketing actions** generate free publicity and positively influence sales. In the Netherlands, Albert Heijn (AH) has had a string of successes. Its football card campaign (allowing young fans to collect and trade league players, but also to create cards of themselves in their favorite jerseys) gave both short-term sales and the chain’s image a tremendous boost. AH followed this with similar campaigns using animals (in partnership with the World Wildlife Fund), fairytale characters and the Muppets.

- **Customer-centric retailing** enables the marketing department to adapt the marketing-mix according to the likes, dislikes and wishes of the customer it is basically further segmenting your client base in your merchandising. Knowing your customer is becoming ever more essential.
All retailers are likely to follow Switzerland’s lead in private label. In the end, 45% of all products, from value to organic to super premium, will be private label.

2. NEAR AND FAR – EXPLORE NEW MARKETS WITH OLD IDEAS

To find growth abroad, retailers may want to cross oceans. Emerging countries in Asia and Latin America have seen high GDP growth which has led to the introduction and socioeconomic expansion of grocery stores. The influx of first-time customers in such regions will drive substantial retail growth for years to come.

Closer to home, Central and Eastern Europe provide opportunities to further capitalize on proven formats. Hypermarkets, the most popular format in these regions, are expected to continue to grow, aided by innovations like the compact stores set up by Kaufland. Discounters will also gain share. By contrast, convenience stores will lose ground in Central and Eastern Europe, as will supermarkets, which compared to Western Europe have a significantly smaller share (27% vs. 43% in 2012).

Some Western retailers have already succeeded in applying long-tested retail ideas in new markets. Tesco’s 371 stores are realizing significant growth in Poland, as are Carrefour’s 54 hypermarkets and supermarkets in Romania. Interestingly, Western retailers have yet to penetrate the Ukraine, an interesting retail market, despite the recent removal of most entry barriers. But why bother setting up shop far from home? Rather than “think global, act local”, Western retailers are learning to think local to succeed – and we’re seeing that in many cases, that means giving up on scale-related benefits. Carrefour in China, for example, is having to decide if merely gaining another local business without any real global synergy makes any strategic sense. Ahold sold its Asian stores when it realized these stores contributed next to nothing to economies of scale. Nowadays, Ahold’s primary focus is on expansion close to home, in Belgium and Germany.

Carrefour has successfully grown in emerging China by sourcing 85% of its products locally, empowering store managers to make judgment calls and customizing formats to local conditions.

3. UPGRADE THE GAMEBOARD – RESTRUCTURE THE MARKET

To find growth at home or in neighboring countries, retailers need to change the market structure itself. One cannot expect to conquer these mature markets with a “me too” format that has long been used by domestic competitors with dominant market shares. To enter and grow, retailers must change consumers’ attitudes to shopping. From the 70’s onwards, Aldi and Lidl were able to export hard discounting because it was un-
known outside Germany and brought about a fundamental change in consumers’ buying habits. Ahold’s convenience stores have been a success because they were the first of their kind in the Netherlands. These format developments will reinvent the market and the rules on which it plays.

Ahold’s AH to go was the real first convenience store in the Netherlands. Typically found in high-traffic areas such as train stations, and with extended opening hours, it realizes 11% return on sales. Ahold plans to export the formula to Germany and Belgium.

Non-food is another example of format and channel development that changes the structure of the market. Tesco Direct has become a major non-food player (25% of total sales, with typically higher margins) and Tesco.com has rapidly become the largest online grocery store in the world (GBP 3.1 bn revenue expected in 2012). To achieve these great results Tesco created nothing new. It merely introduced existing concepts that were new to its market – and did that really well.

4. CHANGE THE GAME – PIONEER NEW RETAIL MODELS

“Innovation distinguishes between a leader and a follower.” An avid innovator, the late Steve Jobs never tired of stressing the need for gamechangers (the essence of what we call “retail 2.0”). Prime examples in retail include Tesco Korea’s virtual subway stores and Auchan’s “click and drive-in supermarkets” in France.

The world’s second busiest commuters saw their waiting time transform into shopping time with the new ability to shop for daily essentials in the subway using smartphones. Online sales skyrocketed by 130% and helped Home plus become South Korea’s number one online retailer.

In France, consumers drive in to collect their purchases at existing stores (Auchan Drive) or pick-up points (Chronodrive.com). Top Chronodrive.com stores generate EUR 20 m sales per year and Auchan aims to expand it locations by more than 250%, from today’s 28 drive-ins to 100.

Innovation makes a strong case for expanding abroad or even overseas. Emerging markets may be ideal locations to initiate radically new retail models because legacy formats and infrastructure are less developed in such areas. Retailers can seek out the surroundings most suitable for and receptive to retail innovation. Once developed and fine-tuned, these concepts can be imported back home to spurn new growth.

Online retailing is an example of a gamechanger that has opened up the world to many retailers. Though Europeans have been slow adopters of online shopping – compared to the US, the online share of total retail is relatively low (3.4% vs. 4.6%) – e- and m-commerce are on the rise. The proportion of Europeans who bought something online doubled to 40% last year. In 2012 alone, the online market in Europe will grow by 16%.
And the European Commission has made a single online market a priority. Such a move would put 500 million consumers in play. The most exciting emerging market for Western European retailers may be right on their doorstep. Another example is Apple who built flagship stores with extremely high turnover per square meter very rapidly.

**HERE BE DRAGONS: THE TWO SIDES OF RETAIL GROWTH STRATEGIES**

But there is a catch. If emerging markets are fertile ground for retail innovation, they are also home to local retailers who know their customers much better than Western entrants. And local retailers are quickly becoming more sophisticated. Being the first or most successful innovator abroad is far from guaranteed.

Western retailers must also protect their own home markets from pure play competitors like the UK’s Ocado, Brazilian market leader B2Winc.com (USD 4.0 billion in revenue in 2010) and Chinese Yihaodian.com (USD 464 million in revenue in 2011). For these foreign competitors, the entry barriers are low. They must solve the cost problem of the last mile, but unlike traditional expansion there is little necessity to build (or acquire) a brick-and-mortar network in Western markets. Either way, Western retailers need to be careful with their strategies in both their home markets and their markets abroad and have to think how to be disruptive instead of just following major online players.

An online grocery retailer without physical stores, Ocado, continues to grow by an average 21% per year and it is becoming increasingly profitable. The company has operated in the UK since 2002 and was listed there in 2010. It has not announced any plans to enter other European markets... yet.

**THE REVOLUTION WILL BE EVOLUTION**

To seize growth, retailers must continuously reinvent themselves at home and abroad. Whether to squeeze home markets for growth, expand to emerging markets far away, change mature markets closer to home, or create new market opportunities, retailers need to introduce new or new-to-the-market propositions: labels, marketing, formats and channels.

However, retailers should think first how to integrate new, innovative technology into their current business model before just opening another web-shop without adding any profits to the current business model. Looking closely at their own capabilities and overall strategies, retailers can evolve themselves in the line of lasting, and much needed, growth.

We found four strategies for growth in our study as shown in our retail growth matrix. From short term focus to long term strategy. Evolution or revolution: What will be the future growth path for your company?
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