BUSINESS TRANSFORMATION

LESSONS FOR EMERGING MARKETS

FOUR ACTIONABLE INSIGHTS FOR RETAILERS

In parts of North America and most of Western Europe, the retail sector has reached a saturation point. Opening new stores in these markets does not lead automatically to an increase in bottom line results. Under these conditions, retailers have had to change their approach to maintain year-over-year growth on sales and profitability, for example, by becoming more cost efficient and wringing greater profits out of the same volume of sales, or by investing in commercial capabilities to enhance like-for-like sales. (See our report "The Rise and Rise of Cost Reduction.")

Meanwhile, in developing economies, some retailers are following in the footsteps of those original retail pioneers, mirroring the same pattern of rapid growth and expanding real estate. Innovation and local customization are thriving in places like China and India, but also in lesser-known markets like Kazakhstan and the Czech Republic.

But the world is not the same place as it was when the likes of Tesco, Carrefour, Walmart, and Edeka made their first billions. With globalization and digitalization, markets are maturing in a very different consumer environment, where they are both hindered and helped by the internet, international competition, and collaborations.

For retailers in emerging markets and those mature retailers looking to expand on the international stage, here is a simple guide to the step you can take.

BIGGER ISN'T ALWAYS BETTER: SMALLER FORMATS CAN WIN, TOO

In countries like France and the UK, retailers grew rapidly by building huge real estate portfolios of giant out-of-town hypermarkets, and then raced to buy up space on the high street to offer convenience formats in every neighborhood. While there is some demand for super- and hypermarkets in emerging markets, the fastest-growing format is the smaller convenience store size, of under 3,000 square foot.

In Russia, this scenario is being played out by Pyaterochka (owned by X5), Magnit, and Dixy, all of which are pushing out a vast number of discount-style convenience stores that offer low prices and target small but frequent shoppers. The approach has lent itself to rapid expansion, because the stores are small, light on capital expenditure, and easy to open, with a basic product range. Between 2012 and 2016, the three main retailers collectively opened over 13,000 new stores, more than doubling the number of modern retail stores in Russian grocery.

Small formats are also hugely successful in India, where most of the populations' grocery needs are served by small local stores; and in Poland, the discount format Biedronka – a banner of Portuguese retailer Jeronimo Martins – is leading the market. These smaller formats are nimble enough to win share from the international behemoths of hypermarket retailing by tailoring themselves to serve local demand and having adaptive supply chains.

ONLINE IS A NECESSITY, NOT AN OPTION

In the West, most of the big retailers had a strong physical presence before adding an online channel into the mix. Retailers in emerging markets will likely not have this luxury and will have to adapt themselves accordingly. For example, in China, Alibaba, JD, and Yihaodian built their own logistics networks supporting their online businesses – an expensive choice, but one that gives them full control of the end-to-end customer experience.

Similarly, shoppers in the more remote places outside Kazakhstan's main cities are keen to adopt online shopping opportunities, if the technology and infrastructure can be provided to support it. Retailers in Kazakhstan have proven to the rest of the world that cash-on-delivery is a viable payment solution for online orders. Lack of flexible payment options is often a barrier to people who are not able to access banking services or who prefer to pay in cash, for whatever reason, such as distrust of online payment systems. (For more on this, see "Digital Equality: Three steps to better serve low-income consumers online.")

In developing countries, mobile phones and tablets have leapfrogged desktop computers and laptops in enabling people to get online. Meanwhile in developed countries, use of mobiles and tablets to access the internet is increasing, particularly among people with lower incomes. Successful retailers are investing in excellent mobile shopping sites that are customized to browsing and making purchases on a small screen.

In India, the grocery market alone is worth over $650 billion. But this huge consumer market is regulated by laws aimed at limiting competition from international retailers. However, regulations in India do permit foreign businesses to operate via online marketplaces, allowing consumer goods to go where stores cannot. Businesses taking advantage of this, like UK clothing retailer MISSguided and US brand The North Face, are helping customers become familiar with their brands, so as internet access grows and infrastructure challenges decline, they will be well-positioned to win market share. Those who are watching and waiting for legislation to change are already a step behind.

CONSOLIDATION SHOULD ALWAYS BE ON THE TABLE

Consolidation will always be a feature in retail. Such consolidation may be on a small scale and local, as in the case of the Future Group in India bringing local, family-owned stores (kiranas) – currently serving 98 percent of the country's grocery needs – into their Aadhaar (rural) and KB's Fair Price (urban) franchises. Or it may be national, as we are seeing in Poland, where a highly competitive and fragmented market – the top five leading grocers account for less than 50 percent of the market – is being shaped by those retailers who are actively pursuing a strategy of integrating franchise concepts and local banners.

Merger activity in Poland will continue in the coming years, driving centralization and efficiency. In such retail environments, the winners will likely be those businesses that actively drive consolidation early on and can quickly and efficiently integrate businesses to streamline commercial and operational activities like category management, purchasing, or logistics.

In mature markets, we also expect to see more mergers and acquisitions, as shown in the Netherlands. Two national companies combined when Jumbo bought C1000, and more recently, Albert Heijn merged with Belgian supermarket Delhaize. In addition to national and international consolidation, it is important for retailers to keep an open mind about cross-sector acquisition and merger, such as UK grocer J Sainsburys' purchase of general merchandise retailer Argos. It may prove to be a canny way to future-proof their business in the face of a local market, confronting falling grocery margins, loss of share to hard discounters, rising food inflation, and fickle consumer confidence.

DON'T FORGET THE BASICS

In the end, success in retail comes down to customer satisfaction with prices and product offering. To meet these expectations, a retailer must have strong commercial capabilities. In particular, they should consider reducing complexity and cost in their operations.

For example, promotions are becoming a retail plague in the Czech Republic. Over the past years, the fight for customers and market share has led to a flood of promotional activities by almost all the supermarkets in the country. In the Czech Republic, we see half of the sales made will be products on promotion, rising to 80 percent for some categories – like poultry or beer – during certain times and in certain stores. The grocers may believe they are positioning themselves as the low-cost option, but the result is that customers no longer trust the original shelf prices and will only make purchases on promotion. This is driving a vicious cycle of more and more promotions that damage the business.

Pricing, promotions, and product assortment are among the most powerful levers that a retailer can use to improve financial performance. It is therefore essential to manage them actively, and to ensure senior management retains visibility and control of key decisions. With dozens of buyers making hundreds of decisions every day, the stakes are high, with millions riding on choices made by relatively junior personnel. Ensuring that corporate strategy is cascaded down into individual product categories and that the buying teams have the tools they need to make the right decisions can transform a retailer's financial performance.

CONCLUSION

The cornerstones of successful grocery retail are the ability to adapt to new and changing environments and developing the right formats and related capabilities in a cost-effective way. To succeed in emerging markets, domestic and international retailers should not only look to customize their businesses to the specific challenges and opportunities of each region, but also be open to learning new ideas from markets and experiences half a world away.