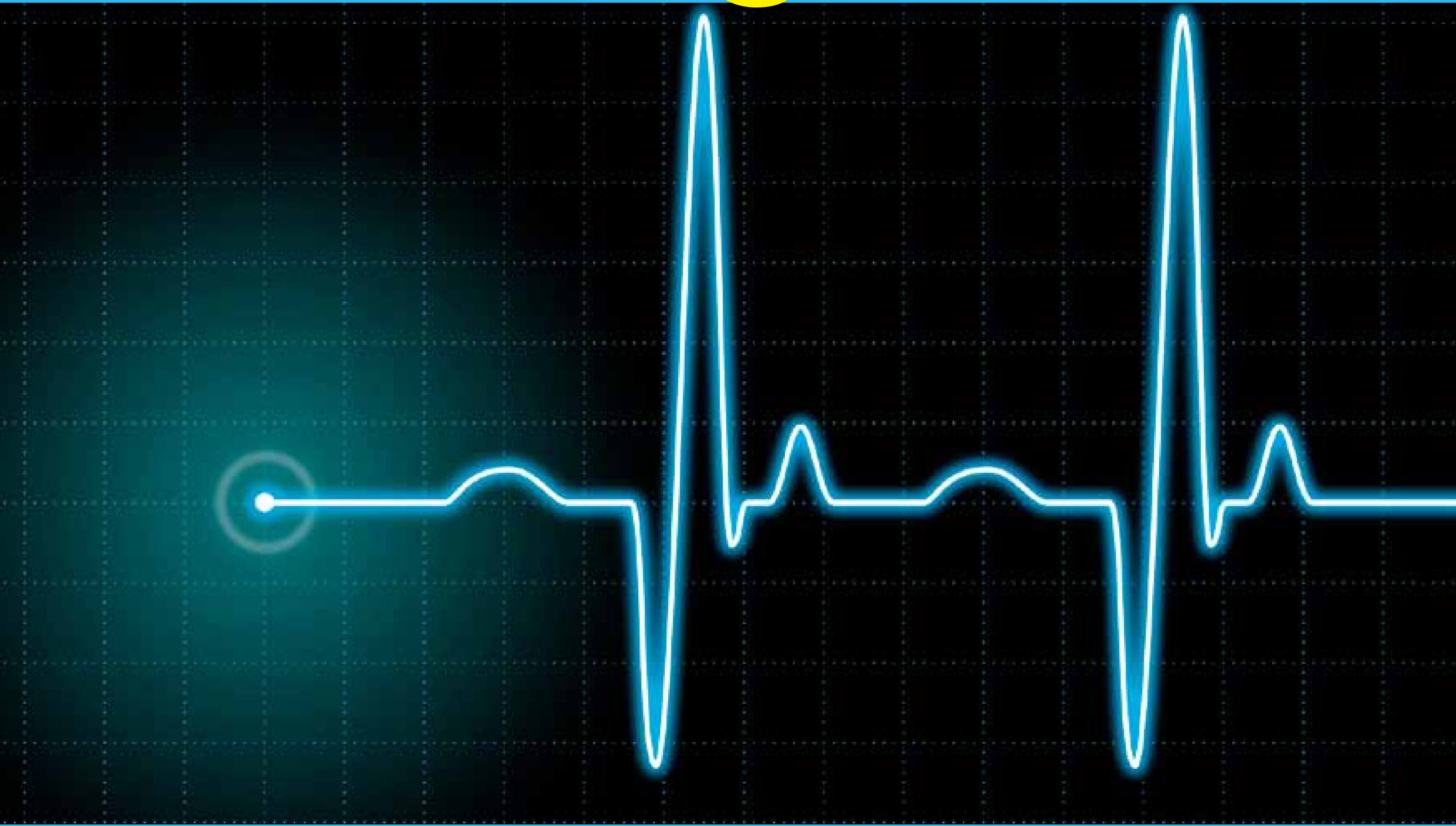
BREAKTHROUGH Insights

First Half 2010

The Pulse of Retail Recovery



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The spring of 2010 was indeed a fascinating time to be studying the retail marketplace, as the global economy—fueled largely by developing markets and a sporadic recovery in the US and Europe—continues to recuperate. At no time in recent history has **rethinking** been more important: reassessing the markets, channels, strategies, and structures that have driven past success. Kantar Retail has been rethinking our core offer as well, particularly how we combine the great work of our four legacy companies into an integrated whole.

As we all move into the 2012–2014 strategic planning horizon and button down operating plans for 2011, we encourage you to consider a few attributes of the rethinking process—innovation, repositioning, and precision—featured in this issue of *Breakthrough Insights*.

Innovation – Growth in this environment will come from innovation—but not just innovative products. New markets, new areas of focus, and new ways of doing business will be essential for growth. Conversely, many of us will find that many of our traditional "growth wells" have dried up to some degree, forcing even more differentiated strategies. Key examples:

- Our assessment of US and European economic indicators is the business case for innovative approaches, as the economic recovery remains uneven and unpredictable. Expect more of this type of insight from Kantar Retail's research model: how the economy is fueling retailer strategy and behavior in 2010 and beyond.
- Our view of forward-looking forecasting techniques will be critical. To get 2011–2014 right, companies must retool their forecasting to use more forward-looking views and less "drag and drop" extrapolation of the past.
- New markets become more critical. Kantar Retail's groundbreaking research on retail in developing economies explains how modern trade functions in many of the world's high-growth markets. Also, we examine changes in the Russian marketplace that should hopefully make multi-national commerce easier. In 2010 we will be accelerating our coverage of some key markets for growth—notably China—as we seek to adapt to the changing growth footprint of the global retail landscape.
- The rapid growth and evolution of the online grocery channel in the UK is symptomatic of the major shifts we all should consider, as retail sales and marketing increasingly digitizes. A key theme in this overview is the **decreasing** role that retailers are playing in framing the shopper's decision process, as pricing and product information becomes more readily available for third-party sources.

Repositioning – Though Walmart isn't "all of retail," we are seeing notable strategic changes that we highlight in this issue: the innovation and retooling of Walmart's Project Impact and the shift in strategic emphasis at Sam's Club. Critical is the need for retailers to find **non-sales growth pathways to increasing return on capital**. In the US, Europe, and Japan, this type of conversation will become the dominant theme of retailer/supplier relations. It will require a major retooling of suppliers' vocabulary and thought process, as so many of our tactics, skills, and incentives are aimed at top-line growth first—an approach that will not be sufficient for best-in-class retailer partnership.

Repositioning is also happening at a shopper level. With an in-depth look through Kantar Retail's ShopperScape™, we examine shopper attitudes and behavior in a critical segment of the retail marketplace: the US consumer electronics industry. Re-engineering communication and marketing against a more pragmatic, prudent, and cautious consumer will be a major theme of our 2011 marketing program development.

Precision – Increasingly, retailers will find it more difficult to grow with a one-size-fits-all philosophy and will aim to develop more refined, targeted approaches to much of their core work. In this issue we focus on trade spending and promotion: an eye-popping look at the levels and nature of trade funding along with a summary of our trade promotion survey. One core retailer requirement that comes out of this survey is the need for shopper insights to fuel trade promotions, and Kantar Retail shares some thoughts on how to successfully achieve this. More broadly, we discuss how vendor criteria are shifting at key retailers and how suppliers must raise their game to win.

Finally, we hope you enjoy a conversation with the leader of Kantar Retail's Americas Insights Team, Mary Brett Whitfield, as she shares her vision on how our research team will continue to grow and deliver the best insights in the retail industry.

Innovation, repositioning, and precision. If your work in 2010 is not more skewed to these three areas than it has been in the past, keep the rethinking process going. Otherwise, you may be missing significant opportunities to grow sales and profits.

Bryan Gildenberg

Chief Knowledge Officer, Kantar Retail

The Evolution of Private Label

Assessing Retailers' Strategic Motives

By Lauren Story / Originally published on January 11, 2010

Private label has taken on a central role at retail over the last several years, making up approximately 17% of total CPG spending and over one-fifth of CPG products purchased. As wallets continue to tighten and price inflation mounts, shoppers are increasingly looking for ways to save money. Today, private label products are the solution for shoppers looking for quality products at an affordable price. Kantar Retail anticipates that increases in private label spending will continue in the foreseeable future, as retailers invest heavily in not only private label expansion but also private label brand development.

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Using Kantar Retail's private label framework, we review six leading retailers' private label strategies: Target, Walmart, CVS, Loblaw, Costco, and Safeway. We also analyze the motivation behind specific private brand products at the respective retailer, providing insight into how suppliers can defend against the rise of private label.

Private Label Framework

Kantar Retail's private label framework assesses products along two dimensions: the retailer's "motivation" for the product line and the brand equity, or "power," that supports it (Figure 1).

Motivation: The Horizontal Axis

Lines developed for mainly financial reasons simply aim to grab sales share and tend to mimic national brands. Comparatively, lines with branded imagery let retailers build differentiation and develop relations with customers.

Power: The Vertical Axis

Store brands that mimic national brands are considered "reflective," as they depend on national brands to provide customer assurance of the category. In contrast, "incandescent" brands can stand alone using the respective retailer's brand equity.

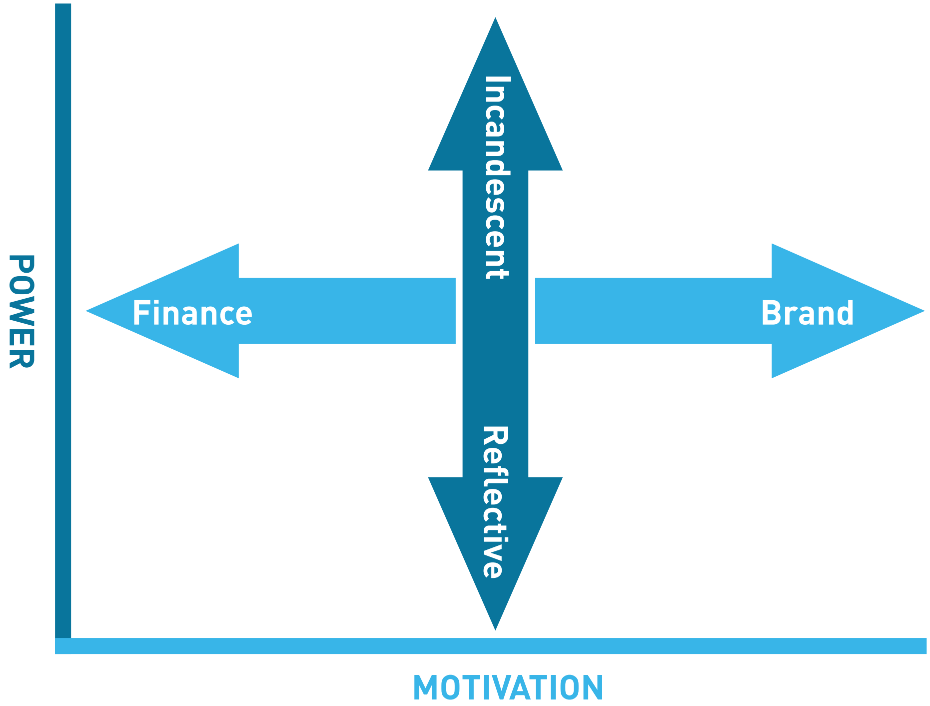

Figure 1. Private Label Framework / Source: Kantar Retail research and analysis

Target Delivers on Brand Promise While Appearing Less Reflective

Target leverages its private label portfolio to gain margin, enhance its brand equity, and strengthen guest loyalty. The retailer's private label portfolio can be seen across the building, from edible grocery to housewares. The relaunch of Target's "wave and bullseye" collection to the new "up & up" brand represents Target's increased desire to grow brand equity while diverting from the reflective look and feel of the "wave and bullseye" reminiscent of national brands.

Target has leveraged "up & up" to satisfy both components of its brand strategy, "Expect more, Pay less." On the "pay less" side, up & up is a cheaper, trade-down alternative, offering a savings of approximately 30% against branded items. Interestingly (and somewhat paradoxically), Target's ubiquitous bullseye is missing from the up & up packaging, allegedly because the retailer didn't want to cheapen the brand by associating it with low prices. In any case, up & up's quality, new packaging, and design conveys Target's "expect more" positioning.

Walmart Pushes into Lower-Right Quadrant with Launch of Great Value

In the past, Walmart's private label strategy has been financially motivated. This has started to change with the relaunch of its Great Value line in March 2009. As the largest food brand in the US, in terms of both sales and volume, Walmart's Great Value

Retailers in Transition

Target houses numerous private label brands with varying degrees of motivation and power. For example, Target's higher-end edible grocery brand, Archer Farms, resides in the upper-right quadrant, offering innovative products with a strong brand identity, while the new up & up brand represents the transition of its predecessor, the "wave and bulls eye," from the lower-left quadrant to the lower right. At least in the consumables area, recent investments in the retailer's private label portfolio represent a more brand-centric strategy.

Walmart offers a host of private brands that have historically focused on financial motivations, residing in the lower-left quadrant. The recent launch of Great Value and continued private label investments suggest a transition to the lower-right quadrant with an increased focus on brand development.

CVS has historically been focused on purely reflective store brands intended to grow margin. However, recent investments in private label suggest a dual movement toward a more incandescent and brand-oriented private label strategy, positioning the retailer closer to the middle of the framework. CVS's private label will continue to be financially motivated while focusing on developing brand equity specifically in health and beauty categories.

Harnessing Brand and Power

Loblaw, Costco, and **Safeway** reside in the upper-right quadrant of the private label framework. These three retailers have created private brands that successfully convey brand identity in an innovative way while maintaining appeal to shoppers.

line represents an estimated 16% of the retailer's grocery sales. The retailer updated this grocery line's packaging for a consistent white-and-blue brand appearance across its products, thus building a recognizable product portfolio. Although still reflective of national brands, Walmart's range of leading consumables offerings is starting to build a unique brand presence.

CVS Operates Financially Motivated Private Label Strategy Wrapped in Brand Strategy

CVS is devoted to driving margin in the front store, as front-end sales make up only approximately 18% of the total CVS Caremark business. Private label plays a leading role in enabling the retailer to grow margin, making up 16% of front-end sales with over 3,500 store brand products. Blade, a men's personal care product, is one of the many recently launched private label products that, while still clearly mimicking a national brand, appears less reflective and has more of a brand feel. Recently, CVS has been investing in more appealing packaging, intended to create a brand story that will more effectively connect with shoppers. This departure from a purely reflective private brand represents an upward movement on the private label framework.

CVS has also leveraged multiple marketing and promotional vehicles including ExtraCare to grow the Blade brand. The recent investments in brand development mark a shift away from a strictly financial private label strategy. While CVS appears to be transitioning to a more incandes-

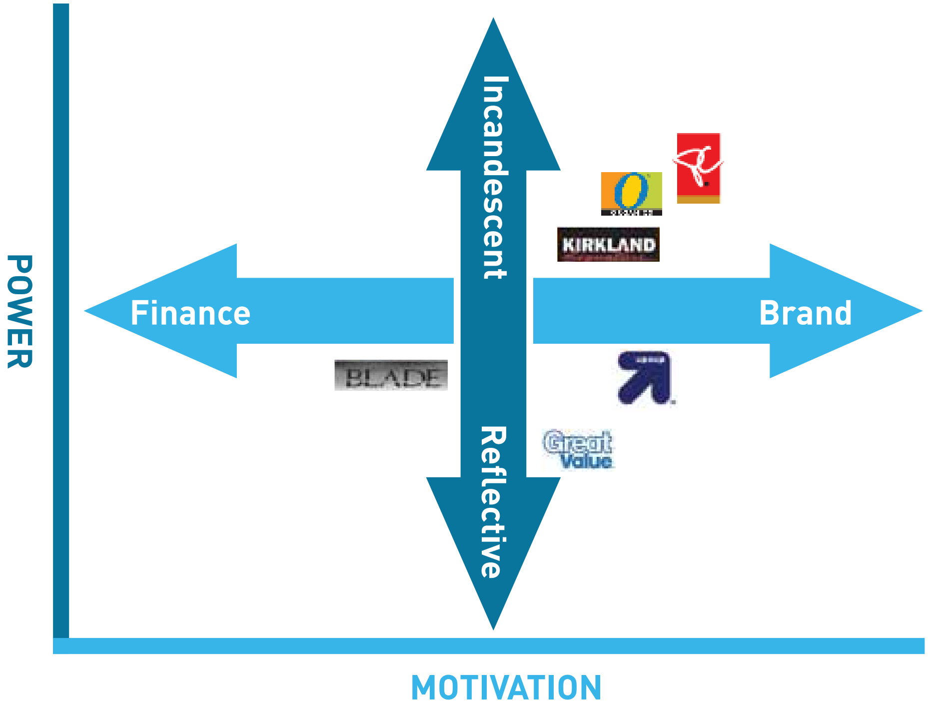

Figure 2. Private Label Dynamics in Retail / Source: Kantar Retail research and analysis

cent and brand-oriented strategy, finance will continue to be the retailer's main motivator. CVS will invest in private label products to leverage brand with the ultimate goal of gaining margin.

Loblaw Represents Private Label Best Practices Internationally

Kantar Retail considers Canada's largest retailer, Loblaw, to be the archetype of what a great private label strategy would look like to the US grocery industry over the next five years. President's Choice, Loblaw's primary control label, is by far the largest brand by sales in Canada according to ACNielsen.

President's Choice has maneuvered to where it is today because it has been managed nationally as a standalone brand, in the same way suppliers manage their own brands. This has created an enormous emotional connection with Canadians, and it has allowed Loblaw to leverage its control labels in a way not many retailers can—to drive discretionary trips.

Loblaw does not manage its control labels through a purely financial lens, and the retailer has stated it is not looking to aggressively expand penetration. Loblaw understands that shoppers come to the store for PC products, even making an additional trip just for those additional four or five items. Loblaw's motivation is to drive total category profit. If a private label SKU can enhance the category, Loblaw is very willing to inject a new PC product to enhance the category's appeal to shoppers, and thus increase dollars for the category.

Costco Delivers on Quality and Price, Generating Trust Among Shoppers

Costco has a unique private label strategy that relies on one brand, Kirkland Signature, which accounts for approximately 19% of sales in categories across the building. Costco has been so successful in this capacity because it has developed a brand that can stand alone—given its strong foothold in quality and ability to

	Private Brand		Suppliers	
	Strengths	Weaknesses	Opportunities	Threats
up & up	Guests' current propensity to trade down to private label	Marketing push started too late, so confusion about the brand remains among guests Some of the participating categories (e.g., baby food and house cleaners) aren't complementary, which may impact cross-category sales	up & up prices are sometimes too low on selected items, which could potentially cheapen the entire collection in guests' eyes and thus elevate the brand's equity Develop co-promotion with out-of-category branded SKUs	Target is pleased with up & up's success and plans to add even more items to this collection in 2010, making shelf space increasingly premium
Great Value	Walmart's over 130 million weekly shoppers gives wide visibility Recently relaunched brand Increased consumer research (e.g., Great Value Round Table)	Brand equity still lagging Share of sales penetration relatively weak Many shoppers (i.e., Brand Aspirationals) have tended to be brand conscious	Develop co-promotions with complementary Great Value categories Generally, Great Value required presence of national brands for its value proposition	Increased shelf space for Great Value taking from national brands Increased Great Value promotions may divert opportunity Second- and third-tier brands may face rationalization
Blade	Broad assortment across multiple categories Innovative packaging and scents Low-price, high-value offering Targets a specific shopper segment	Still somewhat reflective of national brand	Co-branding, some of which is already being seen at the shelf Realize where Blade is lacking in personal care and reallocate resources	Preferential shelf and promotional treatment Expanding product line Margin preservation: elevating category economics
President's Choice	Emotional brand connection to Canadians Wide assortment through brand extensions (Blue Menu, Organic) Established standalone brand with equity separate from Loblaw	Loblaw struggling with internal capabilities and processes Weapon for fighting Walmart on price erodes margins Competition-matching of tiers of product has eroded uniqueness	High-end innovation where there is limited Blue Menu or Organic presence Realize a category is saturated with private label and rededicate resources Loblaw prefers to match lowest tier of private label to comparable off-brand product	President's Choice introduced into category that lacks healthy, organic, or premium SKUs Complete cut of branded SKUs from category and replaced with President's Choice Loblaw will flood a category, forcing out brands with little warning
Kirkland Signature	Strong brand equity with a loyal following Broad range of offerings High-margin brand for Costco Equity allows Costco to market as upscale and even to displace national brands	National-branded member loyalty: If Costco over-rationalizes branded SKUs in favor of Kirkland Signature, members may choose to opt out of a category purchase in favor of their national brand preference at another outlet	Co-branding with Costco Innovation in categories where there is limited Kirkland Signature In select cases, dual brand with Kirkland Signature on the same SKU	Increasing shelf space Continued traction among Costco members
O Organics	Broad exposure across multiple categories Third-party distribution Pillar of Ingredients for Life brand message Sells at a higher average rate than the average of items in the store	High overall price perception at Safeway Organics viewed as a discretionary spend for shoppers	High price perception creates opportunity for lower-priced natural/organic alternatives Natural/organic items are targeted at a limited segment of the shopper base	Third-party distribution creates competition beyond Safeway's store base Gross margin driver for Safeway Broad exposure across categories extends Safeway's private label presence

Figure 3. Private Label SWOT / Source: Kantar Retail research

deliver on price, which has in turn garnered members' trust.

At first glance, Costco's private label strategy appears to be financially driven: The retailer's private brands are twice as productive as the national brand equivalent on a sales-per-club, per-SKU, per-week basis and generate margins between 13% and 15%. In reality, Costco leads with quality, instilling a sense of trust in the brand while providing savings of at least 20% compared to leading national brands. Costco will only offer a private label alternative where it feels Kirkland Signature can offer a comparatively unique quality.

Safeway Private Label as a Lifestyle Solution: Driving the Brand Message

In recent years, Safeway has pared down its overall private label assortment from 70 brands down to a suite of approximately 14 "power brands" that stretches across the full merchandising ladder. Despite such a wide array of SKUs, Safeway's private label strategy is a key pillar of the larger "Ingredients for Life" brand message that Safeway introduced in 2004. Safeway's private label items are meant to be more than just products. Rather, they are viewed as "lifestyle solutions."

O Organics, an organic dry grocery line launched in 2005, has become one of the stalwarts in Safeway's private label portfolio. The line currently consists of over 400 SKUs, all of which are USDA-certified organic. Given its success, Safeway extended the line in 2007 to include products for babies and toddlers. The motivation behind O Organics is primarily brand driven, as it is found in a number of categories and is well aligned with Safeway's larger Ingredients for Life brand message given its organic status.

How Can Suppliers Defend Against Private Label?

As private label continues to take a greater amount of shelf space and a larger share of wallet, it will become even more important for suppliers to understand the retailer's private label strategy and the motivation behind comparable private label products (Figure 2). Additionally, suppliers may benefit from assessing private label competition by identifying where the strengths and the weaknesses in the brand lie as well as the opportunities and threats that exist (Figure 3).

Retailers are constantly evaluating their private label offerings, looking to capture shopper trust and develop brand equity. Understanding retailers' private label strategies and aspirations will be key for suppliers defending against private label. Shelf space remains at a premium, as private label continues to expand and retailers look to optimize their assortment to offer a clear value proposition. Suppliers appealing to the retailer's private label motivators while identifying and responding to private label opportunities will gain a cutting edge with the retailer.

Today's value-conscientious shopper is increasingly trusting of store brands that offer innovative yet affordable solutions. While it is important to understand the retailer's private label motivators, it is essential not to lose sight of the shopper who is focused on both affordability and quality.

The Status of Walmart's Project Impact

By Robin Sherk / Originally published on April 9, 2010

Walmart's Project Impact is well underway, with over half of its US Supercenters due for remodeling by the end of October 2010. As management is proving flexible in its tactical implementation, the retailer is generally happy with its performance to date. Rollout of the overarching plan is even set to intensify. Eduardo Castro-Wright, Walmart's Vice Chairman, explained in February 2010 that Walmart US is "escalating the next phase of Project Impact." At Walmart's investors meeting in October 2009, a new senior management scorecard was announced to explicitly direct the team's focus on developing "Growth," "Leverage," and "Returns," underscoring Project Impact's core aims of improving sales and enhancing profitability.

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Here, Kantar Retail evaluates the performance of Walmart's Project Impact across functions, as a new fiscal year unfolds under the strategy's implementation. Assessing Project Impact's performance and adjustments to date, we detail the status of its financial and merchandising, operational, and marketing efforts; examine areas poised for further refinement and those that appear engrained; and provide suppliers a perspective on unfolding opportunities and considerations.

Financial and Merchandising – "Win, Play, Show"

Overall, Walmart had solid returns for the fiscal year ended January 31, 2010, with free cash flow up over 20% to reach USD 14.1 billion. Although figures were not broken out for Walmart US, Castro-Wright described the segment as delivering "a very strong free cash flow performance." Moreover, Walmart US's operating profits were the most it has ever reported, climbing 5.2% to reach USD 19.52 billion for the fiscal year. Though the retailer is still concentrated on containing its costs, the latest quarter saw its operating expenses grow less than the rate of sales growth. Walmart US's returns were further aided by gross margin gains and inventory declines.

- **Gross margin increased 73 basis points (bp) for the fiscal year.** This change was attributed to better merchandise and markdown planning, labor productivity, and "price optimization."
- **Inventory decreased 7.6% for the fiscal year versus a sales increase of 1.1%.** This reduction equated to USD 1.8 billion of less inventory in the retailer's stores and distribution centers over the course of the year.

While returns were strong, Walmart's sales growth softened toward the end of the year: In the fourth quarter, Walmart US's operating income rose 5.6% compared to a net sales decline of 0.5%. Comparable-store sales (comps) declined 2.0% in the fourth quarter and 0.2% for the fiscal year. Both external and internal factors drove this decline.

- **Deflation, particularly in grocery and consumer electronics:** Castro-Wright explained that the swing between the inflation experienced in 2008 and deflationary pressures in 2009 impacted the retailer's comps performance "more than 300 bp." This pressure likewise drove down the retailer's average ticket.
- **Store traffic concerns:** While traffic for the fiscal year was up 1.3%, Walmart US reported "a slight decrease" in fourth quarter traffic. In March 2010, Chief Operating Officer Bill Simon explained that some of the "Win, Play, Show" assortment refinements cost the retailer the shopper's trip, even though the SKUs removed weren't high-velocity items.

Efforts to bolster Walmart's near-term sales performance are already underway. While Simon explained that on the whole the retailer's new assortment efforts have "driven some of our growth," he recognized concern with this loss of trips. Specifically, the retailer acknowledged that customers demanded certain slower-moving, infrequently purchased items to satisfy their shopping needs. To address this, Walmart has already responded by adding back about 300 branded SKUs. Given that the average Supercenter

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carries about 142,000 SKUs, this adjustment of less than 1% to the assortment stands as a refinement to the retailer's established "Win, Play, Show" merchandising strategy.

Operational – "Fast, Clean, Friendly"

Walmart is generally satisfied with the performance of its Project Impact remodeled stores. In March 2010, the retailer's leadership explained that relative to its control group, the remodeled stores experienced a 125–150 bp sales lift, a 6–8% reduction in inventory, and customer experience score gains on "every metric" they evaluate. Reviewing the latest quarter, Castro-Wright reported that Walmart US saw its "highest customer satisfaction scores ever." With such results, the retailer not only reasserted its timeline for Supercenter remodels but also accelerated components that enhanced its performance. At the same time, Walmart refined components of the strategy that were apparently hampering sales.

Figure 1. Pallets by the Store Entrance of Walmart Supercenter
Source: Kantar Retail store visit, New Hampshire

- **Accelerating clean Action Alley rollout:** By the end of its first quarter, Walmart will have removed pallets from the main "Action Alley" aisle in the stores on the waiting list to begin Project Impact conversions. The retailer explained that customers liked the uncluttered shopping experience. As it helps Walmart to reduce store inventory level, this move also encourages shoppers' movement across departments and down the aisles.
- **Refining clean Action Alley standards:** Walmart has shown flexibility in its standards for clearing the Action Alley, allowing pallets back for certain promotional events. The retailer is also allowing pallets in at peak times, such as on weekends, and in key locations, such as by the entrance (Figure 1).
- **Adjusting endcaps to counterbalance:** The retailer announced plans to focus on the use of "bulk, high-capacity" endcaps, which basically hold the quantity of a pallet. Simon explained that these offer a "much clearer price impression" and a "much more hard-hitting product presentation" relative to its traditional endcaps.

- **Adding more branded displays:** Walmart is apparently acknowledging the importance of national brands' equity: Kantar Retail has noticed an increasing amount of suppliers' signage and in-store display material in recent months. Such promotions showcase that Walmart sells the key products that its shoppers value. As Simon acknowledged in March 2010, "we are a house of brands."
- **Mitigating Project Impact remodel interruptions:** Admitting that traffic declined more than anticipated as stores underwent remodeling, Simon detailed that the retailer now plans to implement a "hard relaunch" with area advertising and "local merchandising initiatives" to communicate that the store is refreshed and encourage shoppers to return.

Marketing – "Save Money. Live Better"

Walmart continues to assert its brand mission, as the company intensified promotion of its messages in 2009. Kantar Media recently listed Walmart as one of the top 10 ad spenders in the country, assessing that its measured ad spending rose 35% over the prior year. Walmart's annual report, released March 30, 2010, detailed that its advertising costs hit USD 2.4 billion in its last fiscal year. Castro-Wright detailed that Walmart US media presence enhanced markedly through "higher co-op advertising spending" over the year. Through the retailers own efforts, and by joint efforts with suppliers, Walmart continues to reinforce both aspects of its message.

- **Save money with Rollbacks:** In March 2010, Simon reasserted that their "brand position requires us to serve the customer by having the lowest price." He detailed plans to increase the intensity of Rollback advertising to focus "more on longer-term" promotions, particularly on "key" food and consumables. This emphasis represents a shift away from the weekly deals touted throughout the 2009 holiday season.
- **Offering targeted value:** Punctuated deals are still present, but efforts such as Walmart.com's "Beauty Value Week" are more refined, as they also encourage use of its website and online ordering service.
- **Live better, entertain the family:** Walmart is taking a bigger stake in promoting wholesome, at-home "family moments" such as by 1) jointly creating a made-for-TV film, *Secrets of the Mountain,* as part of an extension to its Family Night campaign and 2) coordinating a "retail-tainment" effort with DreamWorks to promote its new family-friendly film, *How to Train Your Dragon*. The wide-ranging effort includes offering themed Happy Meal books at select in-store McDonald's, setting up a Viking ship for a two-day event in New York's Times Square, and an array of exclusive merchandise across categories.
- **Enhance environment, added goals:** Furthering its global environmental efforts, Walmart unveiled targets to reduce the greenhouse gas emissions throughout its supply chain by 20 million metric tons by the end of 2015. This, in effect, sets self-assigned standards to reduce emissions in advance of potential nationally or internationally imposed regulation.

Kantar Retail Point of View

Walmart's management is focused on fostering growth and leveraging its resources and capabilities to drive better returns. This requires a delicate balance. It appears that the scale has recently tipped toward enhancing profits, as gross margins rose, inventory decreased, and management focused on remodeling more of its Supercenter base. At the same time, Walmart's sales growth began to stagnate, and visitation started to fall. With Project Impact as its anchor, the retailer is now recalibrating to stabilize this turn.

Its leadership has demonstrated a willingness and ability to adjust the implementation of Project Impact. Several refinements are already underway across the strategy, including:

- Bolstering branded merchandise assortment in select areas,
- Re-examining in-store displays and suppliers' brand presence,
- Shifting clean Action Alleys and readjusting pallet placements, and
- Communicating longer-lasting Rollback messages.

These changes, at least in the near term, may represent an acknowledgement of suppliers' equity and ability to bolster sales. Kantar Retail anticipates that such responsiveness to consumer feedback and performance data will continue to guide Walmart's modifications to its unfolding approaches.

Looking further ahead, Walmart will continue to search for the optimal balance between efforts that leverage its resources and those that drive growth forward. Walmart's initiatives for longer-term returns include its new global sourcing efforts to reduce the cost of making its private label goods, continued Project Impact store remodeling, and the implementation of its January 2010 reorganization to streamline teams and processes for greater efficiencies. Growth efforts will include further refining its brand and price leadership promotions and exploring new avenues, such as developing its multi-channel and online presence and adding smaller, Project Impact–oriented formats such as High-Efficiency Prototypes. The mixture of

> The mixture of both near- and long-sighted efforts indicate that Walmart is positioning to be a competitive retailer that resonates with shoppers now and in the years ahead.

both near- and long-sighted efforts indicate that Walmart is positioning to be a competitive retailer that resonates with shoppers now and in the years ahead.

The following table outlines the near-term implications of Project Impact's status for suppliers:

Walmart's Position	Supplier Implication
With Project Impact as its anchor, Walmart's senior leadership is working to develop growth and leverage resources to enhance the company's returns.	Recognize and communicate internally that, in spite of some adjustments, Project Impact is "here to stay." Acknowledge the role of your product portfolio, understanding its position within Walmart's objectives for driving sales growth and enhancing profits. ("Win" categories are its vehicles of growth, whereas "Show" categories are kept for profitability.) Identify whether internal growth and profitability targets align accordingly.
Facing declining fourth quarter traffic, Walmart added back about 300 items to capture lost trips.	Examine internal research to identify which assortment items may jeopardize differing shopping trips to Walmart. Recognize that Walmart's adjustment does not mean an end to its SKU rationalization efforts, understanding the limits have tightened for new product introductions.
Inventory levels in the stores and distribution centers continued to decline.	Be vigilant against out-of-stocks, as such reductions intensify the need for precision. Identify and anticipate factors, such as changing promotional events that may impact demand for your category.
Clean Action Alley is rolling ahead, with flexible reductions in pallets and new "bulk, high-capacity" endcaps.	Plan for lasting reductions in pallet placement opportunities, while acknowledging that select occasions are likely to emerge. Develop new ways to entice shoppers to the shelf, such as through mobile apps and online messages, cross-category communication, or innovative shelf presentations. Examine the opportunities and adjustments needed to best leverage the bulk endcaps. Connect with warehouse club teams for package presentation and display style ideas.
Focusing on Rollbacks and reasserting its price leadership position.	Anticipate that Walmart will seek to limit its cost of goods sold to drive price positioning. This will likely include an unwillingness to accept price increases when faced with inflationary pressures or further probing into the full supply chain to search for means to bolster efficiencies.
Taking "bigger bets" by co-developing and intensely promoting family entertainment options.	Expect rising demands for advanced planning and further internal coordination across sales, marketing, online, and insights groups to develop and align with Walmart's increasingly sophisticated efforts. Acknowledge that family-friendly, "at-home" entertainment themes are a well-engrained facet of Walmart's "live better" messaging.

Potential Game Changer

Sam's Club Is Poised to Compete, Details Its Wide-Ranging Strategy

By Robin Sherk / Originally published on March 1, 2010

In October 2009, Sam's Club senior management introduced a new strategic direction for the business at Walmart's annual meeting for the investor community. The transformative go-to-market strategy swept across merchandising, operations, and marketing functions. Under Chief Executive Officer Brian Cornell, the organization's vision is aligned to make "Savings Simple" for members, leverage consumer and member insights to make investment decisions, and support "fewer, bigger, and better" initiatives. This article provides insight into why Sam's Club adopted this approach, what it entails, and maps out the anticipated impact for supplier partners.

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Why Is Sam's Club Changing?

Sam's Club had to address its historical marketing, merchandising, and operational challenges. In addition, the retailer recognizes the prospects for building new growth and leveraging its resources and Walmart's capabilities to drive better returns. Here, Kantar Retail outlines key challenges and areas of opportunity:

Expenses Outpacing Sales – Over the past several years, Sam's Club has become less profitable: Operating expenses have increased at a faster rate than sales. Tepid sales growth coupled with weak membership growth have failed to offer sufficient leverage for rising running costs. In short, Sam's Club has identified a need to re-evaluate operating expenses, processes, and standards to achieve greater club efficiencies.

Inventory and SKU Productivity – Sam's has historically achieved lower levels of SKU productivity than its primary club competitor, Costco (Figure 1). Despite several contributors to this gap, a significant opportunity to achieve higher productivity through more thoughtful and relevant merchandising remains. Traditionally item-centered, Sam's offering has been giving members a bit of everything rather than focusing on categories with stronger potential. Sam's reassessment of the overall product mix was needed 1) to better align it with growing member demands and 2) to enhance the resonance of its offering.

Membership Growth and Retention – Membership renewals have also been a challenge. The lead club competitor, Costco, gets approximately 90% of members to stay year over year. Sam's Club, in contrast, is estimated to receive renewals from about 70% of its base. To build and retain its base, Sam's endeavored

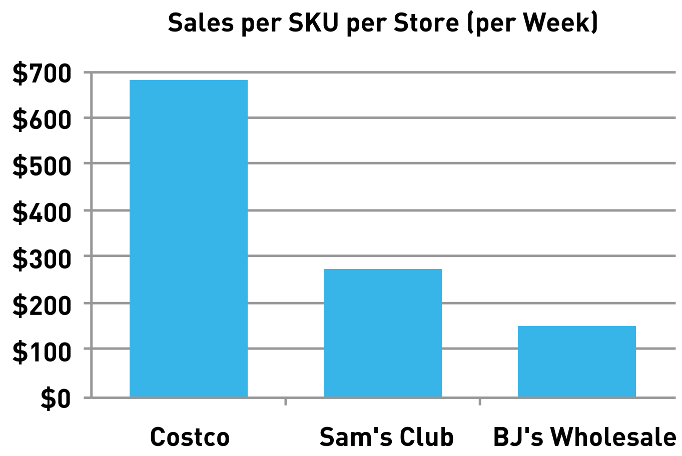

Figure 1. Comparison of Club Channel Inventory and Club Productivity
Source: Company reports, Kantar Retail analysis

to better attend to its various member segments' needs in an effort to drive its top line and enhance member loyalty.

Member's Value Proposition – Sam's has lacked a clear, consistent, and differentiated member value proposition. To better attract new members, bolster resonance and share of spending with current members, and attract Plus membership upgrades, Sam's had to develop and effectively communicate the unique value that its membership provides.

What Is Sam's Response?

Addressing these challenges and building the business further required a comprehensive strategy to reach across its functions. Broadly speaking, senior leadership's plans to leverage its member insights and Walmart's resources. The team has clearly set out the business's direction and simplified its approach. The following sections examine Sam's novel merchandising frameworks, its redefined marketing initiatives, and its operational and club redesign initiatives. The goals across these efforts are 1) to increase the club's productivity and efficiency and 2) to offer a stronger member experience and value proposition. Developing both of these objectives should drive its membership, share of members' wallet, and marketplace growth.

I. Merchandising

New Category Framework

Previously, Sam's Club was a strictly item-level merchant. This is no longer the case. Linda Hefner, Sam's Club Executive Vice President (EVP) of Merchandising, explained that Sam's analyzed its categories "on the basis of how we can meet member needs," as well as the customary assessments of sales and growth opportunity. The retailer is working to add assortment relevance and focus to its offering by introducing a unique, "member-centric" category framework.

Using its member and consumer insights, Sam's in its new approach divides the categories based on two criteria: relevance and differentiation. Relevance refers to whether members buy the item as a necessity, whereas differentiation refers to whether Sam's can bring a unique proposition to the marketplace. These two notions provide the axes for considering Sam's four-box framework of category classifications (Figure 2).

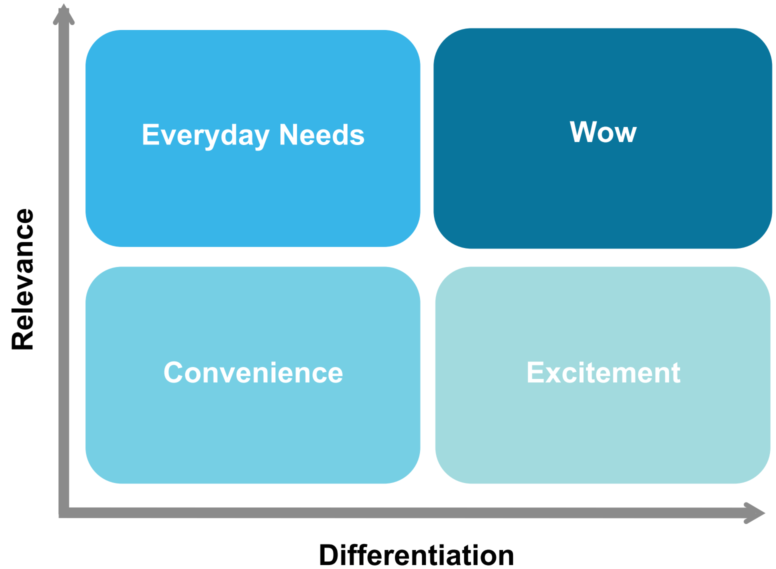

Figure 2. Sam's Club Member-Centric Category Framework
Source: Company presentation

- **Wow –** These categories have a high degree of relevance with members, and Sam's recognizes the opportunity to provide a distinct proposition. Examples of "wow" categories include Fresh, Baby, and Health & Beauty.
- **Excitement –** Sam's sees strong prospects to provide a unique offering, but the items are of less necessity to its members. Instead, such offerings as Seasonal and Electronics provide a sense of newness in the club.
- **Everyday Needs –** These items are "must buys" for members, but Sam's does not assess that it has strong differentiation in the marketplace within this category. Examples of "everyday needs" include Office Supplies and select household necessities.
- **Convenience –** Here, the offerings are not considered particularly relevant, and Sam's does not regard itself as differentiated competitively. Offerings such

as Sporting Goods and Furniture will not be of particular focus for the club, and they will likely face SKU rationalizations.

Using this framework to clarify the assortment means that in-club merchandise allocations are poised to change. Overall, the number of SKUs within Sam's Club will remain the same. General merchandise categories—including Sporting Goods, Apparel, Seasonal, Furniture, Movies/DVDs, and Large Appliances—will lose space. This area will go to categories in consumables, including Meal Solutions, Produce, Meats, Bakery, Baby, Over-the-Counter medicine, and Health & Beauty Aids. This shift of allocations aims to "accelerate Sam's Club share growth" with members in more profitable, productive categories.

New Buyer Scorecard

To aid merchandise selection within this new framework, Sam's Club also introduced a new criteria for its buyers to scorecard against. Hefner explained the goal is to develop a "best practice approach for assessing merchandise value in a very consistent way across all categories." The value of an item is to be evaluated in terms of its perceived benefits to

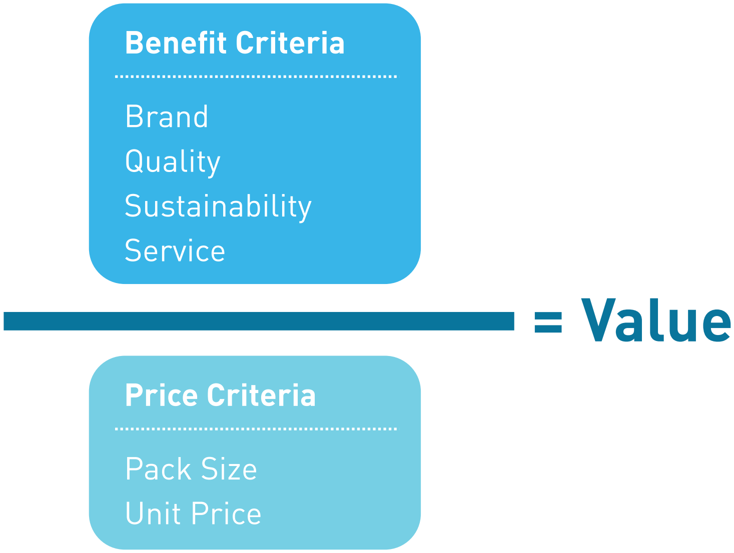

Figure 3. Sam's Club Buyers' New Value Criteria / Source: Company presentation

members versus its price. Both the benefits and price are multi-faceted concepts. The dimensions are outlined in Figure 3.

Furthermore, once the value proposition of an item is assessed, Sam's will benchmark it relative to other offerings in the marketplace. This will include within-channel and cross-channel competitors. As Hefner explained, this "more rigorous approach ensures we deliver on our promise to make the best choices for our members." Delineating its value criteria and implemented evaluation policies shows that Sam's is adding structures that develop its inventory's relevance and quality standards to drive assortment resonance with its members.

II. Marketing

In 2009 Sam's Club replaced its previous tagline, "It's a big deal," with a more direct mission statement: "Savings Made Simple." This new tagline matches the overall tone of its new go-to-market efforts, as Cornell had explained that "simplicity is at the heart of our strategy." It also shifts the focus of the value proposition from a "big" pack-size "deal" to a more sophisticated offer for clear, accessible, and

Previous Logo

Current Logo

Savings Made Simple

Figure 4. Sam's Club Old and New Logo Presentation
Source: SamsClub.com, Kantar Retail research

convenient "savings." Along with this new message is a more refined logo and presentation, which is featured in clubs, online, and in marketing communication (Figure 4). In sum, the appeal presented in Sam's message has developed.

Sam's Club explained that its new message speaks to three types of members: 1) Advantage members who shop the club for their family and personal needs; 2) Business members who go to Sam's for their company (may include restaurant owners, local convenience store operators, or office managers); and 3) "cross-over" shoppers who go to Sam's to meet both business and personal needs. Sam's message must resonate across these members' demands.

The retailer has also articulated three targets for its communication around "Savings Made Simple," depending on the audience's level of association with the retailer:

1. **Attract new members.** For those unassociated, Sam's seeks to build its base across both Advantage and Business memberships. Examples of such tactics include offering fractional memberships for club trial and demonstrating its value proposition.
2. **Retain current members.** To encourage renewals among current members, the retailer reiterates the savings that Sam's provides. One approach is to promote its "Savings Made Simple Study," which tells users how much they save shopping at Sam's versus other retailers.
3. **Encourage upgraded memberships.** For those already loyal to Sam's, the goal is to attract upgrades to Plus memberships, which are sold at the more profitable cost of USD 100. Sam's bolstered its value proposition in 2009 with the introduction of its personalized coupon program: e-Values. This unique offering uses new technology to apply customized discounts to members' cards automatically.

Across these communication objectives for its various memberships, the retailer clearly stated its purpose. Cindy Davis, Sam's Club EVP of Membership, Marketing, e-Commerce, effectively summarized: "Our goal is to expand baskets, to increase our share of wallet with our existing members, as well as build member loyalty."

III. Operations

Sam's Club is also re-evaluating its clubs to drive efficiencies. The retailer set a series of near-, mid-, and long-term initiatives to build the club's labor productivity while enhancing the members' experience. This includes efforts to reduce inventory, enhance scheduling and processes, and re-evaluate the work areas in the clubs.

Nearer-term initiatives—such as its new 5S Program to "sort, straighten, sanitize, standardize, and sustain"—are already being reinforced within the club's communication to staff. To support the broad range of efforts, Sam's has instigated a new innovation team, led by Ami Spivey. Sam's Club EVP of Operations, Ignacio Perez, explained that the initiatives are expected to reduce labor hours 6–8% over the next five years.

In the fall of 2009, Sam's Club began testing a redesigned layout, dubbed "Project Portfolio," in 10 of its clubs. The changes include rearranged department locations, adding space to the focus "wow" areas such as Health & Wellness and Fresh. The retailer added a new center aisle, improved display adjacencies, and enhanced sightlines to aid in-club navigation. Signage, lighting, and merchandise presentation were also enhanced, bolstering the experience and assortment appeal.

Still in the testing phase, a club-wide implementation of this redesign has yet to be set on a public timeline. Cornell explained that the company is serious about the efforts, shifting capital spending plans from new clubs into remodels. He also pointed out the efforts are meticulously strategic: "transforming insights into action." Hefner said that after the initial results of the pilot remodels are assessed, "we plan to roll it out to the rest of our clubs." Moreover, Sam's closed 10 of its underperforming clubs in January 2010, allowing future remodel efforts to focus on locations with better potential. Suppliers should anticipate that Sam's Club will roll out a redesign of its base over the next several years.

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Kantar Retail Point of View

Kantar Retail views this array of changes at Sam's Club as game changing. Introducing a clear strategy to rally behind, the company is positioned to address the long-standing challenges facing its organization and to build new opportunities. Its assortment is being rethought and refined; its communication is being polished and targeted; and its clubs are being re-evaluated and redesigned. Sam's Club is taking wide-ranging action, distinguishing its position under Walmart's portfolio. Senior leadership asserts this position, as Cornell chose to describe the business as "the ninth largest retailer in the United States" and said that "going forward, you should expect us to run this business like a top 10 US retailer." This is a revitalized Sam's Club that is poised to compete.

Implications of Sam's efforts on suppliers are likewise wide-ranging and significant. The following table summarizes the key areas for suppliers to consider:

Action by Sam's Club	Impact	Supplier Implication
Implemented a new go-to-market strategy, reaching across functions.	Many of the previous conventions for working with Sam's will adjust.	Communicate Sam's new direction internally, allowing teams to plan for shifts both in working with the retailer and its competitors' responses. Anticipate a heightened focus on member and consumer insights, across approaches to pallets, SKUs, and marketing proposals.
Announced a member-centric category framework, based on relevance and differentiation.	Sam's is rethinking its approach to its assortment, looking across the club and prioritizing particular departments.	Recognize where your categories stand within Sam's new framework, anticipating assortment opportunities or edits. Proactively identify which SKUs may be candidates for addition or deletion to prepare for potential adjustments.
Introduced a new buyer scorecard to standardize evaluation of products.	Sam's is working to bolster the value proposition of its assortment, heightening its focus as a "buying agent" for members.	Delineate your assortment's benefits and position on the scorecard, and consider it relative to competitor retailers' offerings. Anticipate pallet and assortment expectations to increase, especially in "Wow" areas, as Sam's seeks to develop its assortment's proposition.
Clarified marketing message, "Savings Made Simple," with focus to attract, retain, and upgrade memberships.	Sam's has heightened attention on its own brand image and communication to engage members.	Consider ways that your offering or promotional programs may align with Sam's message and objectives. Evaluate the opportunity Sam's nascent eValues program may offer. Anticipate that, as Sam's brand sophistication increases, its developing campaigns may require broadened resources or planning times.
Remodeling clubs, adjusting departments, and adding a center aisle.	Sam's is focused on driving efficiencies and improving members' experiences. New club openings will slow.	Map where your categories and products are likely to fall in the new club layouts, recognizing new adjacencies and in-club sightlines. Anticipate opportunity for in-club promotional space, given the added endcap facings created by the new center aisle. Understand Sam's new club expansion is set to slow: re-evaluate your sales growth expectancies for the retailer.

2010 Americas Events Calendar

KANTAR RETAIL

Q3

Mexican Retailing Forum — Mexico City

Jul 6 Best Practice In Global Retailing Trends: The Latin American Response (PM)
Jul 7 General Session
Jul 8 Negotiation Skills To Maximize ROI

Walgreens Workshop Series — Chicago, IL

Aug 3 Winning In Today's Retail Ecosystem (PM)
Aug 4 Walgreens Workshop

CVS Workshop Series NEW — Providence, RI

Aug 10 Winning In Today's Retail Ecosystem (PM)
Aug 11 CVS Workshop

Safeway SuperSession NEW — Oakland, CA

Aug 31 Winning In Today's Retail Ecosystem (PM)
Sep 1 Safeway Workshop
Sep 2 Negotiation Skills To Maximize ROI (AM)
Shopper Marketing (PM)

East Coast Grocery SuperSession NEW — Tampa, FL

PUBLIX, DELHAIZE

Sep 14 Winning In Today's Retail Ecosystem (AM)
Compact Formats (PM)
Sep 15 Publix Workshop
Sep 16 Negotiation Skills To Maximize ROI (AM)
Shopper Marketing (PM)

Target/Supervalu SuperSession — Minneapolis, MN

Sep 21 The Compact Grocery Store & The Save-A-Lot Strategy (PM)
Walmart's Project Impact: Assessment and Implications for Target (PM)
Sep 22 Finding Success At Supervalu
Partnering With Target
Sep 23 Negotiation Skills To Maximize ROI

Q4

Canadian Retailing Forum — Toronto

Oct 5 Best Practice In Global Retailing Trends (10am-3pm)
Oct 6 General Session
Oct 7 Negotiation Skills To Maximize ROI (AM)
Shopper Marketing (PM)

Strategic Outlook Conference — Chicago, IL

Oct 19 General Session

Future of Category Management Forum — Chicago, IL

Oct 20 General Session

Strategic Outlook Conference — New York, NY

Oct 26 General Session

Online/Multichannel Workshop Series NEW — San Francisco, CA

Oct 26 Online/Multichannel Workshop
Oct 27 Social Media/Digital Marketing (AM)
Session TBD (PM)

Strategic Outlook Conference — Rogers, AR

Nov 2 General Session

Walmart SuperSession — Rogers, AR

Nov 3 Sessions TBD
Nov 4 Sessions TBD

Year-End Forum — Atlanta, GA

Dec 7 Breakouts TBD
Dec 8 General Session
Dec 9 Breakouts TBD

Kantar Retail Tel: 1.800.370.3261 or 1.617.588.4100 Fax: 1.617.499.2723 Web: MVI-Worldwide.com

KANTAR RETAIL

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Retail Insights /

Superior breadth and depth of analysis — Comprehensive insights delivered through articles, forecasts & data reports, slide presentations, photos, and special reports covering the leading retailers, channels, markets, and key retail topics globally.

Accurate and actionable insights — Our research delivers an implications-focused point of view that enables our clients to grow their businesses through more effective business planning and execution.

Shopper Insights /

Primary data and unique, in-depth research — Shopper motivations, in-store behaviors, and the purchasing decision process to develop strategies to maximize ROI and improve in-store execution.

Forward-looking point of view — Get smarter about what makes shoppers tick and align with growth opportunities.

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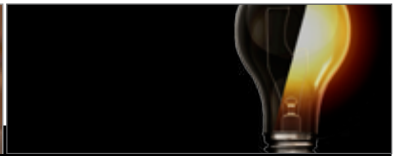
Frequent access to our experts — Hear real-time, actionable insight from Kantar Retail experts, addressing everything from key customer strategies to the trends that are shaping an evolving retail marketplace.



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Vendor of the Year Checklist Ten Requirements for 2010

By Jennifer Halterman / Originally published February 2010

Near-term growth for many retailers will be driven not so much by expanding with new stores but more so by discovering untapped pockets of growth: catering to new shopper segments, offering unique solutions, delivering innovative products, and more. As retailers search for growth opportunities and greater efficiencies that drive productivity and profitability, they will demand more and more from their manufacturer partners. Here, Kantar Retail provides a top 10 requirements checklist to help vendors think about what they must do to align more closely with retail customers in 2010 and beyond.

1. Help penetrate new consumer segments.

Manufacturers that can help retailers identify untapped growth opportunities—such as going after unique shopper demographics, capitalizing on hot trends, and considering new formats to serve unmet shopper needs—will be well positioned. The opportunity exists, for instance, for manufacturers to partner with retailers to create in-store destinations that cater to specific shopper segments. H-E-B recently launched a Men's Zone area in select San Antonio, Texas stores with the assistance of P&G. The dedicated aisle features 500+ products and includes five touch screens that provide grooming tips and product advice. Blue lighting captures shoppers' attention, as does the overhead flat-screen TV featuring sports programming.

2. Customize the offer.

Manufacturers must understand retailer-specific economics in order to appropriately customize product programs that align with an individual retailer's financial levers and metrics. In addition, retailers will demand specialized programs to differentiate themselves from the competition. They will increasingly expect vendors to partner on micro-merchandising initiatives related to penetrating new consumer segments with, for example, ethnic products, multi-lingual signage, and packaging tailored to community needs or smaller pack sizes for urban areas. Manufacturers working with Walmart to launch Hispanic concept Supermercado de Walmart will likely be the first called on when Walmart decides to roll out the concept. Target, which is planning to test a smaller format concept aimed at dense urban markets, will look to its vendor partners to help determine how to best meet specialized urban needs.

> Relationships between retailers and vendors are becoming and will continue to be ever more complex, as some retailer growth initiatives take on a more granular focus.

3. Streamline communications.

Relationships between retailers and vendors are becoming and will continue to be ever more complex, as some retailer growth initiatives (such as multi-format and micro-merchandising efforts) take on a more granular focus. Retailer/vendor organizational structures must align so that information flows through the most critical, and preferably few, touch points. This will allow more efficient and accurate dissemination of information, ultimately saving both parties time and money. A "one-voice" approach will generate a consistent message that can be expressed across teams: advertising, logistics, marketing, packaging, etc.

4. Explore more solutions selling.

Retailers are placing more emphasis on shopper solutions rather than just on products. Manufacturers should look for ways to align products within a larger solutions story that retailers want to convey. An example is the rising number of retailers, including Target and Walmart, attempting to transcend beyond the perception of health care products seller to that of integrated health and wellness solutions destination. The latest to join the fray is Giant Eagle, which is testing an expanded health and beauty care (HBC) offer in a select number of stores. In addition to featuring a broader assortment of products, stores now have a nutritionist to conduct classes on food preparation and dieting tips. Manufacturers should look for opportunities to partner with a retailer like Giant Eagle to sponsor such classes, another vehicle in which to promote their products.

5. Create unique connections with shoppers.

Direct-to-consumer touch points that drive product awareness will be critical, as shoppers try to digest the exorbitant number of media messages they encounter every day. Walmart Smart Network in-store displays allow manufacturers to deliver targeted messages at the point of sale. For this unique medium, vendors will be expected to deliver custom content and work to integrate the message with Walmart's larger marketing plan (e.g., price rollbacks, health and wellness, and sustainability). Vendors are also finding new ways to bring their messages directly into the home. Some leading manufacturers—including Clorox, Kraft, and SC Johnson—are teaming with at-home marketing company House Party to sponsor brand parties. Shoppers sign up at HouseParty.com to host an event. If selected to host, the shopper receives a party pack featuring product samples, coupons, and more.

6. Leverage new technologies.

The growing popularity of smartphones enables anytime access to information and allows shoppers to compare prices, read reviews, and buy—all while standing in the aisle. Moving forward, retailers and manufacturers must think about investing in the latest mobile tools and applications and even more about the broader issue of mobile customer engagement: They must assess how mobile tools can be better leveraged inside the store to both enhance the shopper experience and drive customer loyalty.

7. Take the lead on category management.

Shelf space is up for grabs as retailers re-evaluate assortments, rationalize SKUs, and rein in inventory-related costs (e.g., supply chain, backroom, stocking, markdowns, etc.). In addition, intensified private-brand penetration is pressuring national/name brands. Manufacturers that demonstrate capabilities to work with retailers to assort and grow the entire category (not just a product or brand) are more likely to be lauded as strategic partners than left on the cutting room floor.

8. Be a good green partner.

Sustainability will remain a top retailer agenda item. Manufacturers must commit to investing in green products, packaging, and processes. In many cases, sustainable business practices help lower costs: Reduced packaging, for example, typically translates to a lower carbon footprint and decreases supply chain expenses. Walmart holds vendors to a sustainability scorecard to help the retailer attain its long-term environmental goals: be supplied by 100% renewable energy, create zero waste, and sell products that sustain people and the environment. Walmart Canada is holding a Green Business Summit to bring manufacturers and competitors together to share business initiatives that are "good for the planet and good for the bottom line."

9. Drive innovation—in products, pricing, promotions, packaging.

Innovation is critical to new growth. However, the real advantage comes from not only making better versions of existing products but in delivering unique products and solutions and better product experiences as well. Manufacturers that focus on innovation will secure their position on the shelf because retailers are more likely to view them as partners in growth. Additionally, retailers will look to manufacturers to collaborate on backroom efforts (such as supply chain initiatives) to help cut costs from the system.

10. Express value beyond price.

As the economy starts to show signs of improvement, manufacturers must start thinking about how they can help retail customers redefine value that revolves around more than just price. From the shopper perspective, value means getting more for the money, and "more" means different things to different shoppers: convenience, selection, quality, quantity, service, etc. Redefining value will help manufacturers and their retail partners better align themselves for long-term growth.

Kantar Retail Point of View

Increasing retailer demands—around analytics, customization, solutions selling, supply chain efficiencies, sustainability, communications, etc.—means exceedingly complex relationships for vendors to manage. This complexity translates into a rising cost to serve. Going forward, it will be critical for manufacturers to analyze, quantify, and prioritize retail customer accounts—in other words, manage customer account portfolios much like they manage product and brand portfolios—based on growth potential, profitability, and return on investment.

Trade Transformation

A Shopper-Centric Approach

Contributed by Todd Bortel, Mike Urness, and Ginny Valkenburgh

Trade promotion is a USD 176 billion annual business, but for years it has been considered a "necessary evil" in the world of consumer packaged goods. Companies sought to trim the fat around trade promotion by optimizing their budgets and programs. Optimization became the singular goal of trade practice in the 21st century, as CPG manufacturers worked to make their trade spending as efficient as possible.

Even industry leaders believed that optimized trade promotion was synonymous with successful trade promotion. In the words of one President of Sales at a major US manufacturer, "Our trade spending is under control. We have reduced our spending by 20% in the past three years. We have a first-rate system to track performance. We are in great shape."

However, trade partners who believe that optimization alone will support their success are sorely mistaken. Efficiency is a *sine qua non* of today's trade, but the real frontier lies with the shopper. CPG companies must consider how they can reach shoppers along the Path to Purchase™. They must influence the shopper as she chooses the outlet, shops the store, and ultimately selects which products to buy. The new challenge in trade promotion will be learning how best to steer one's organization along this shopper-driven retail marketing path.

This will be no easy feat. Shoppers are reacting to economic conditions by making fewer trips and cutting costs. Traditional trade promotion has become less relevant, as retailers focus increasingly on price.

To address these new challenges, manufacturers must partner with retailers along the entire Path to Purchase™. Manufacturers can maximize trade productivity by pursuing two complementary paths:

1. **Ensure your trade house is in order.** Learn from the leaders to establish solid fundamentals. Model trade activities after best-in-class organizations to improve trade productivity (Figure 1). This year's leading performers in trade promotion include Kraft, Procter & Gamble, General Mills, PepsiCo, and Unilever. These manufacturers distinguished themselves through their solid execution, clear promotion strategies, and well-trained workforces.
2. **Set your organization on the path to shopper-driven trade promotion.** Commit to market with the retailer and develop capabilities to influence the shopper along the whole Path to Purchase™ (Figure 2).

Four major strategic pillars underpin Path to Purchase™ marketing:

1. **Insight visibility.** Possession of unique consumer insights will enable manufacturers to initiate appropriate planning conversations with their trading partners.
2. **Collaboration.** Manufacturers must collaborate with retailers to broaden their frame of reference beyond the category. A broader view will make the manufacturer more valuable to the retailer and will result in wins for both parties.
3. **Marketing capabilities.** Manufacturers must stay abreast of the latest technology to

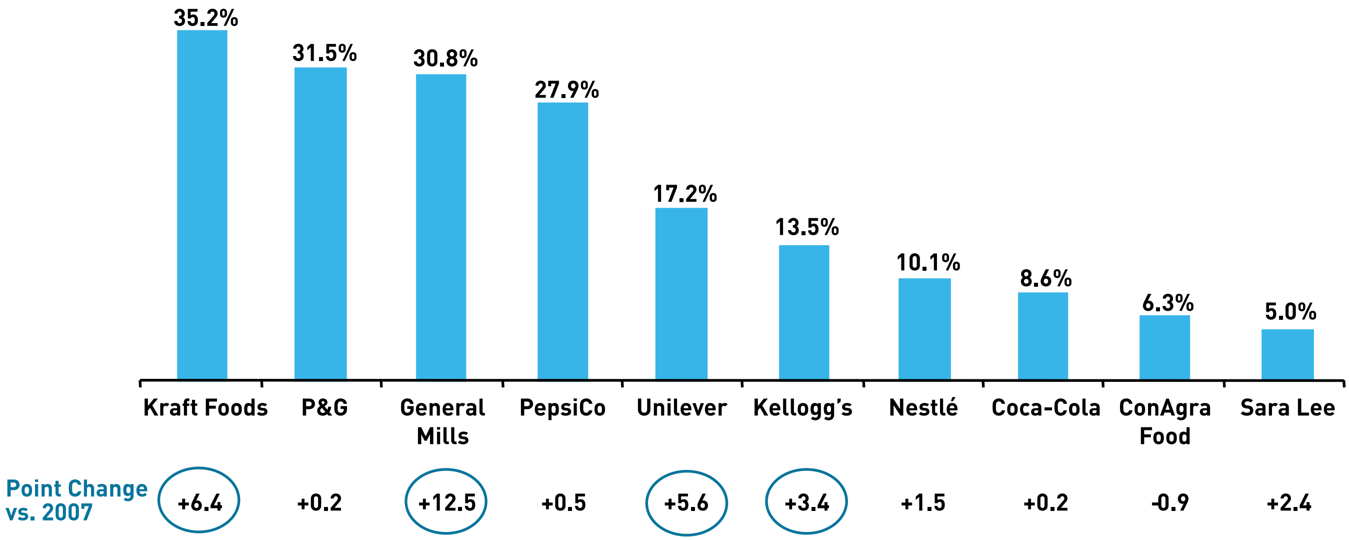

Figure 1. Best Manufacturers at Trade Promotion: % of Retailers Ranking Manufacturers in Top Three

Source: Kantar Retail Trade Promotion Study 2010

The new challenge in trade promotion will be learning how best to steer one's organization along this shopper-driven retail marketing path.

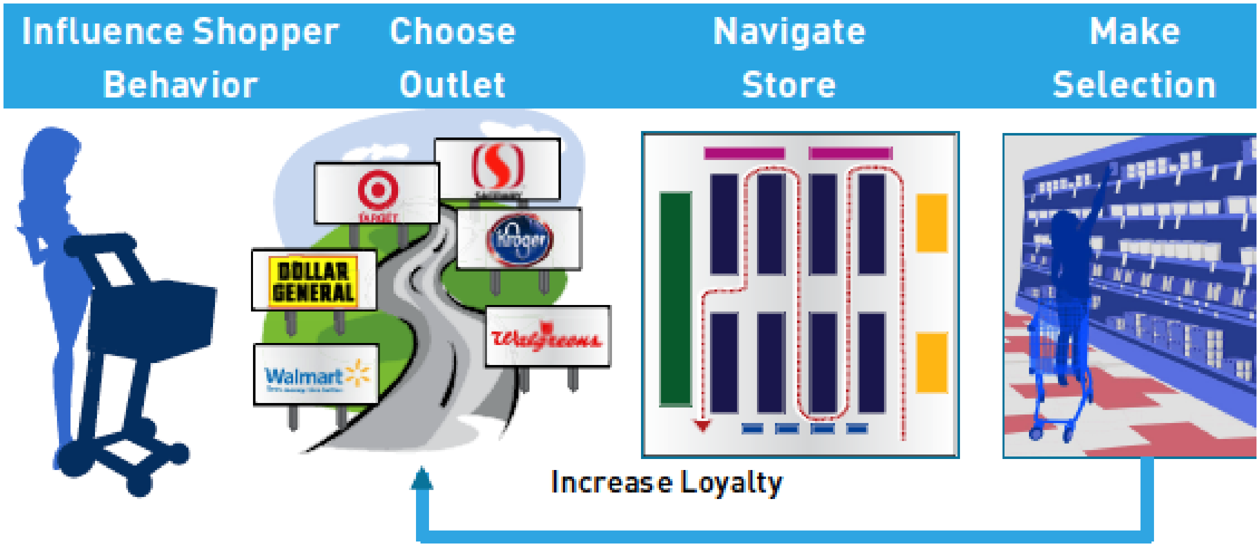

Figure 2. Path to Purchase™ Marketing / Source: Kantar Retail Trade Promotion Study 2010

woo consumers. Marketing capabilities are fundamental to shopper-driven trade.

4. **Funding reallocation.** Price dollars and shopper marketing dollars must be used as effectively as possible.

If manufacturers manage their trade house correctly, there will be more collaboration between trading partners. This will ensure that the largest part of the manufacturer marketing budget is put to effective use.

"Trade Transformation: A Shopper-Centric Approach" is the 13th industry report on Trade Promotion Spending and Merchandising, now produced under Kantar Retail. The study is based on more than 250 responses from a broad scope of retailers and manufacturers. It is designed to establish a definitive position on the key issues surrounding trade spending from both a manufacturer and a retailer perspective. If you wish to learn more about the Trade Promotion Merchandising and Spending Industry Benchmarking Study, please contact Ginny Valkenburgh at 203.834.2800.

Mary Brett Whitfield

Taking Her Team to New Heights *By Elizabeth Lee*

As a retail expert, Mary Brett Whitfield knows a thing or two about shopping behavior. In fact, she leverages this knowledge to her family's advantage in Columbus, Ohio. In that market, "Kroger and Giant Eagle give gas discounts based on grocery spending," she says. "At Kroger, you can get the maximum discount if you spend $750 or more in a month. With two teenage boys, we often spend that much. Once we hit the mark, we switch to Giant Eagle."

Whitfield was perhaps always meant for the business of knowing about retailers and shoppers. After all, she has been immersed in the industry since childhood. Her father was a co-founder of Management Horizons, the predecessor company of Retail Forward and a pioneer in applying strategic consulting principles to the retail industry. Retail Forward is—as of January 1, 2010—one of four companies that form Kantar Retail. "I grew up visiting stores with my dad. We actually spent part of every vacation checking out new retailers," she says.

After obtaining a bachelor's degree in economics and an MBA, Whitfield began her career in 1989 at Pier 1 Imports/Fort Worth, Texas, in the market research department, where her responsibilities included designing surveys and moderating focus groups. Two years later, she landed a position in the market research division for Pearle Vision in Dallas. In 1993, she was recruited to join Management Horizons, which by then had been acquired by Price Waterhouse.

With a body of work that spans market positioning and consumer behavior to financial analysis, Whitfield's analytic experience is varied and rich. Yet, Whitfield values the perspectives of her colleagues. "My approach is that I don't assume that my thinking is better than anyone

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else's," she says. "I consider all opinions and suggestions as equal to mine because I know I have smart people working for me." Whitfield's humility about her 22 years of experience belies the enthusiasm she has for retailing. "I'm passionate about helping people understand how consumer behavior and changing competitive dynamics in the retail landscape have the potential to impact their business," she says.

"For me, it starts with the consumer. You have to understand what she's thinking, what she's looking for, and how she approaches shopping. Once you understand that, it becomes significantly easier to help retailers and suppliers know how to position themselves in the marketplace—how to think about marketing positions, location decisions, and assortment." Noteworthy is Whitfield's easy use of the pronoun *she*. After all, "women make around 80% of buying decisions," though Whitfield—the mother of Max, 16, and Kevin, 15, and wife of 25 years to Michael—emphasizes that she doesn't use herself as a focus group.

Today, Whitfield leads the newly integrated Americas Insights Team for Kantar Retail. In this role, Whitfield has the exciting challenge of combining the broad yet deep insights of the legacy Retail Forward and legacy MVI teams. She describes Retail Forward as "fact-based" and "forward-thinking." "We look at the world from a consumer and shopper point of view. We want a deep understanding of her behavior, which is rooted in the macroeconomic environment: what's happening in the economy and how it affects consumers. We combine the three worlds—shoppers, the environment, and stores—to help our clients be forward-thinking." While the strengths of MVI and Retail Forward are very different, Whitfield says, they are also very compatible. According to Whitfield, the many benefits of the combined offer include:

- **Focus –** "One of greatest strengths of the legacy MVI business is its deep knowledge and understanding of specific retailers. Retail Forward's traditional approach is to understand what is happening across the landscape, particularly with shoppers. When you combine the organizations, you have a much more complete, more robust understanding of what's happening in the retailer marketplace."
- **Forecasting –** The combined teams now have economists who can offer "a more informed, fact-based perspective." Whitfield says: "Economists who are able to interpret what's happening in the economic environment as far as what it means to retailers and others in the retail industry are pretty unique."

I'm passionate about helping people understand how consumer behavior and changing competitive dynamics in the retail landscape have the potential to impact their business.

- **Coverage –** The combined teams also complement each other as far as their respective retail sector coverage. Retail Forward has subject matter experts in areas, such as apparel and home improvement, that have not historically been a focus for MVI. Likewise, Retail Forward can leverage "a deeper understanding of the key account retailers as well as a database that is 'second to none' in understanding retailers on an individual basis."
- **Consulting –** Kantar Retail is not limited to retail analysis, Whitfield explains. "With the integration of the four companies, we have the consulting component to help companies act on the insights we provide. We have people with the skill sets and experience to take the insights to execution."

The accessibility to these combined resources saves clients time, Whitfield says. "Our clients are focused on their direct competitors and have jobs that require them to focus on their brand or what's happening in their stores. But, there's a lot happening with other stores, brands, and shoppers. We look across the entire retail landscape—like the consumer does."

The Kantar Retail integration doubles the size of the Americas Insights Team, and Whitfield has high expectations for the group. "The ability to collaborate with more people with differentiated experience and perspectives will strengthen the quality and relevance of the insights," she says. "The goal is to become the trusted advisor on a broader, deeper set of issues to manufacturers that sell to retailers as well as the retailers themselves."

She says that Kantar Retail's ability to help clients—from insights to implications to implementation—is critical. "In the current economic environment, many companies are planning and acting in survival mode, but eventually the recession is going to end. The retailers who have not been planning for the recovery will be left behind. Our insights can position companies to thrive—not just survive."

The retailers who have not been planning for the recovery will be left behind. Our insights can position companies to thrive—not just survive.

KANTAR RETAIL

Shopper Insights

As shoppers continue to change at an unprecedented pace—the need for rich and timely insights has never been greater. Kantar Retail's Shopper Insights answers key questions about shopper behavior:

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- Which stores are shopped regularly – who's winning and who's losing?
- What categories did shoppers buy? How does it compare to the past year?
- Who shops specific retailers' stores, websites, and/or catalogs?
- What do shoppers spend on key merchandise groups? Where do they spend the most and why?

For More Information, Please Contact

CustomerService@mvi-insights.com / 1.617.588.4100

Shopper Insight analysis, data reports & the ShopperScape™ database Get a fact-based point of view of shoppers' future intentions to spend, their perceptions of household financials, and which retail venues are sought for the variety of merchandise groups. The ShopperScape™ monthly, online survey is balanced to be representative of the US household, giving you access to data for:

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- Spending behavior at 200 retailers
- Purchasing behavior at 70+ categories in seven category groups

Shopper Webinar Series Gain critical insight into shopping behavior in the food, drug, and mass retail channels. Hear forward-looking, expert insights into shopper motivations, in-store behaviors, and purchasing decision processes that allow you to know what makes shoppers tick and how to align yourself with where the growth is. Powered by the proprietary ShopperScape™ monthly survey, the series provides insight into what factors are influencing shopper behavior right now.

KANTAR RETAIL

ShareGroups

Kantar Retail's ShareGroups bring together non-compete companies to have an open conversation regarding our common challenges and opportunities.

- Share real-life examples of Best Practices that provide relevant, actionable insights
- Brainstorm and Problem Solve on the key items that we are struggling with to help create strategies that will address them
- Promote new thinking that will improve execution against our challenges and opportunities

We have ShareGroup teams that focus on specific channels — Mass, Warehouse Club, Drug, and Grocery. We also have two teams focused on Shopper Insights.

For More Information, Please Contact

Steve Meehan at 1.800.370.3261 ext. 4173 or 1.817.235.0172
Steve.Meehan@KantarRetail.com

Team-Generated ShareGroup Areas of Discussion

Top of Mind — Updates on the Economy, Industry, Channels, and Retailers

Client Best Practices — Talent Acquisition, Team Structure, Speed to Market, Supply Chain Leadership, Training and Skill Development, Strategic Management of Trade Spending, The Team Leader as General Manager, Tools for Consumer and Shopper Solutions

Retailer Trade Practices — In-store Execution, Health & Wellness Initiatives, Top to Top Best Practices, Sustainability & Carbon Footprint Needs and Demands, Customer Segmentation

Problem Solving and Brainstorming — ShareGroup members openly discuss our challenges seeking the team's advice and guidance on move-forward strategies, tactics, must haves, and watch outs

Team Member Case Studies — In-depth sharing of successful programs and processes to offer innovative ideas and strategies that should prove valuable to other ShareGroup team members


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Recession Alters CE Shopping Behavior
New Frugal Mindset Sticks

By Dina Roldan / Originally published March 2010

Consumer electronics shoppers changed their behavior considerably during the recession and are likely to maintain new habits as the economy gradually improves. Most shoppers are limiting CE spending by making do with what they already own and/or delaying purchases. When they do buy something, many CE shoppers look only for the best deals when choosing a retailer; for instance, many are shopping Walmart's CE department more frequently. With a new frugal mindset, most CE shoppers will not revert back to past conspicuous consumption habits. Rather, the limiting and deal-seeking behaviors of the recession will give way to pragmatic, mindful choices in the recovery—even among more affluent shoppers.

Figure 1. Changes in CE Shopping Behavior, by Generation

Notes:
Respondents shopped for CE products in the past year, whether a purchase was made or not.

Gen Y members of the ShopperScape™ database are between 18 and 28 years old.

Source: ShopperScape™, January 2010

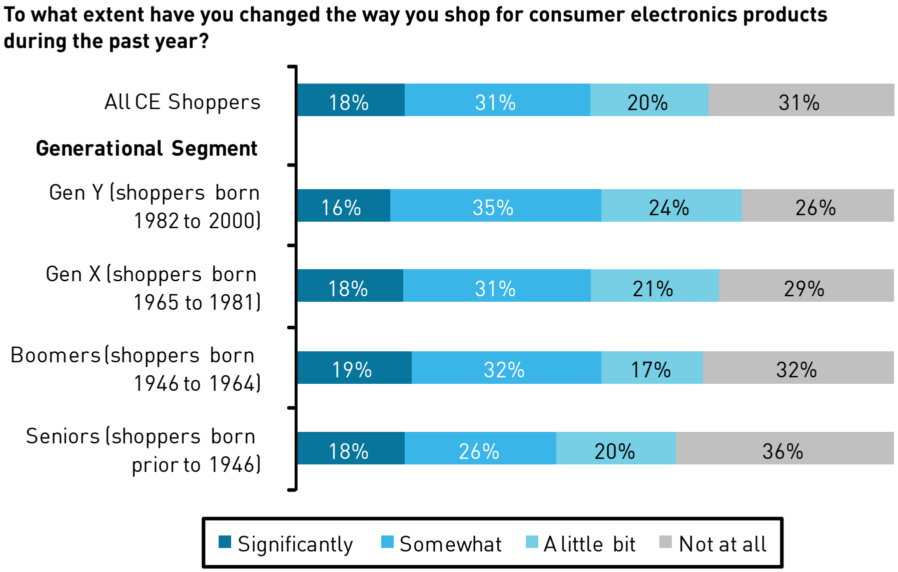
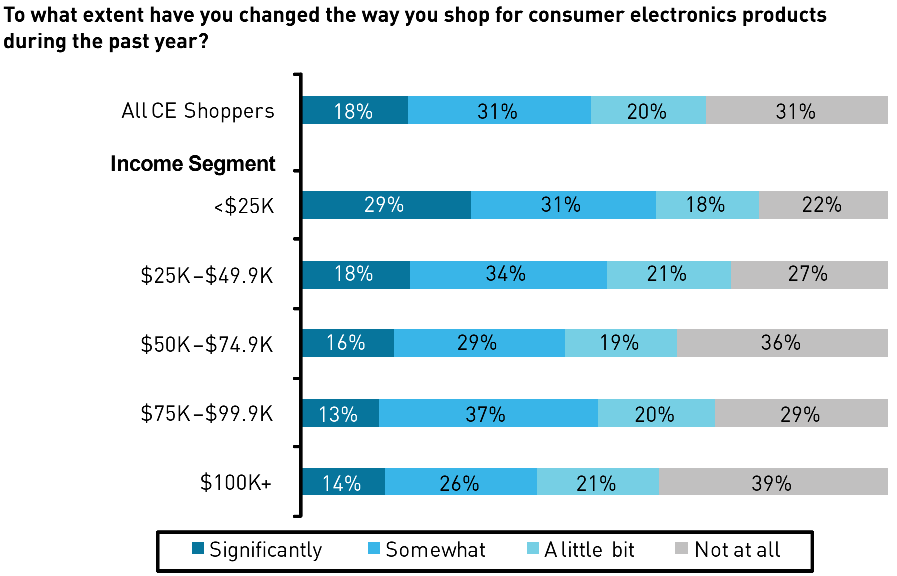


Figure 2. Changes in CE Shopping Behavior, by Income Segment

Notes:
Respondents shopped for CE products in the past year, whether a purchase was made or not.

Source: ShopperScape™, January 2010



Recession Prompts Big Behavior Changes

The recession has had a major impact on most CE shoppers; 69% have changed their shopping behavior to some degree (Figure 1). The overall effect has been more pronounced on younger and lower-income shoppers, but the intensity of the reaction has been strongest among Boomers. Seventy-five percent of Gen Y shoppers—who tend to be the most technologically advanced but the least financially stable—say they've changed their CE shopping behavior. A significant but noticeably lower share (64%) of Seniors—the least technologically savvy but most financially secure—report changing their shopping behavior. With concerns about finances as retirement looms, Boomers are more likely to report they have "significantly" changed their behavior than the other generational segments.

More than three-quarters (78%) of shoppers with household incomes of less than USD 25,000 report a change in behavior, compared with 61% of shoppers with household incomes of USD 100,000 or greater (Figure 2).

With concerns about finances as retirement looms, Boomers are more likely to report they have "significantly" changed their behavior than the other generational segments.

Making Do with What They Own

The most prevalent change among CE shoppers is "limiting" behaviors: 57% reported they are making do with what they own; 42% are delaying purchases until it's absolutely necessary; and 33% are buying products only with cash. Other limiting behaviors (that a quarter of CE shoppers have adopted) include sticking to a firm budget, waiving warranties, waiting longer to replace an item that can't be repaired, and buying lower-priced CE brands.

Deal-Seeking Particularly Prevalent

Many CE shoppers are changing how and where they shop, especially as they search for competitive prices. Nearly 40% of CE shoppers are shopping around more to find the best deals and/or to compare prices online, and 35% use advertised specials or sales to determine what brands to buy. Nearly a quarter shop Walmart more frequently for CE products than they had in the past, a shot across the bow of Best Buy, the remaining national electronics specialist.

Gen Y Concerned About Cash; Boomers Worried About Fiscal Health

Overall, CE shoppers (37%) indicate they have changed their behavior due to a combination of the following reasons: saving money, concerns about their current household financial situation, and

About 75% of each of the generational segments expect to maintain their new behaviors in the future.

concerns about the recession's future impact on their household (Figure 3). Having accumulated little wealth, Gen Y shoppers buck that overall pattern and are more concerned about current cash flow than the other household finance reasons tracked. In contrast, Boomers and Seniors— underscoring the disparate impact on their wealth from the housing slump and stock market falloff during the recession—are more worried about overall household fiscal health than the younger cohorts.

New Behaviors to Stick Across Generations

The recent economic downturn will have a lasting impact on CE shopping behavior. Most (77%) CE shoppers say they will not revert back to past shopping habits even when the economy and their personal finances improve. A small minority (6%) report they are somewhat or extremely unlikely to continue with their recessionary shopping behavior. Despite the differences across generational segments in terms of recession behavior changes, there are no significant differences among them with regard to expected CE shopping behaviors: About three-quarters of each of the generational segments expect to maintain their new behaviors in the future.

Overall, what is the main reason you have changed the way you shop for consumer electronics products during the past year?*

	All CE Shoppers	Gen Y (shoppers born 1982 to 2000)	Gen X (shoppers born 1965 to 1981)	Boomers (shoppers born 1946 to 1964)	Seniors (shoppers born prior to 1946)
My household's current financial situation	18%	17%	20%	19%	14%
Concerns about how the recession will affect me/my household in the future	8%	5%	9%	9%	6%
Trying to save money	31%	46%	33%	27%	23%
Some combination of the three reasons above	37%	28%	33%	41%	48%
Some other reason	5%	4%	5%	4%	10%

Figure 3. Main Reasons CE Shoppers Changed Behavior

** Among shoppers who have changed the way they shop for consumer electronics products during the past year*

Note: Gen Y members of the ShopperScape™ database are between 18 and 28 years old.

Source: Kantar Retail ShopperScape™, January 2010

Kantar Retail Point of View

Savvy CE retailers can succeed in the face of a tough environment if they can create a compelling hook to draw in recession-weary shoppers and then close the sale. Retailers can create a sense of urgency and excitement with limited-time deals, offer generous incentives and competitively priced bundles, and differentiate with exclusives. For example,

- Newegg.com creates excitement with frequent limited-time "Shell Shocker" promotional deals.
- Sony's Trade-In Program may entice shoppers who are "making do with what they own" to trade in old electronics for credit on new purchases. In addition, this program can help Sony up its green quotient with shoppers.
- Apple is a master of creating hype and a sense of exclusivity. It enables customers to pre-order online and reserve its latest gadgets—such as the new, "magical" iPad—before they launch. Not only are customers ensured to get the latest technology but Apple can better gauge demand for its latest electronics as well.
- Best Buy is gauging demand by querying customers about the features they want in a laptop and then teaming up with Dell, Sony, and Toshiba to create the "coolest new experiences."
- Walmart has found success in its Project Impact stores with new displays and cheaper prices on gaming consoles and software (Figure 4).

In a category that quickly takes on the characteristics of a commodity business as new features and functionality migrate to mass-market price points, CE retail innovations must occur at least as quickly as product innovations. Otherwise, shoppers will go somewhere else to make a purchase.

Figure 4. Walmart CE Display at Project Impact Store
Source: Kantar Retail store visit

About Kantar Retail ShopperScape™
The Kantar Retail ShopperScape™ database is a unique source of information about shopping behavior based on a monthly survey of 4,000 nationally representative households. The extensive survey measures a wide range of shopping behaviors and attitudes. Survey respondents are the self-designated primary shopper for their households. Surveys are conducted online using the TNS 6th dimension access panel. For details on how to access the complete database and other ShopperScape™ reports available, contact Katherine Clarke at 614.355.4009 or Katherine.Clarke@KantarRetail.com.

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The Role of Shoppers in Promotions

Contributed by Jacqui Keery / Originally published on May 20, 2010

In the last decade, UK sales volumes on promotion have dramatically increased: Retailers and suppliers have adopted a policy of using promotions to bring in new shoppers and to encourage all shoppers to buy more. Promotions, however, are an over-used and often incorrectly used tool.

"It is one of the most shortsighted of policies possible to try to succeed by winning those customers who buy on price and seek the cheapest deal. They are unreliable." *– Peter Ehrenberg*

"The easiest new customers to acquire by promotion are typically the least loyal." *– Ogilvy Study, London*

The Macro Environment

Shopper perception of value has altered and is, arguably, a permanent consequence of the recession. Bargain hunting has become a socially acceptable approach to shopping. In fact, shoppers now take pride in flaunting their "Primark" shopping bags and how "little" they paid for a particular item. Some may argue that this shift in attitude and behaviour would advance the cause for promoting even more frequently and deeper; however, such a view is shortsighted.

An in-depth examination of shopper attitudes toward value reveals that retailers and suppliers alike must essentially redefine the term *promotion* and review the type of mechanic they employ. Along with forcing a re-evaluation of value, shoppers are more deliberately avoiding accumulation of waste, which begs the question of why suppliers and retailers continue to adopt BOGOFs and multibuys as mechanics. Are these types of mechanics even relevant in a society with an increasing number of single households and aging couples with no or only one child? The reality of the changed macro environment means that a new approach to the design and implementation of promotions must be adopted.

The Commercial Reality

The commercial reality of the cost of promotions paints an even more sobering picture of the need to overhaul the approach to promotions. Promotions are like the cocaine of the brands marketing world. They are a tempting quick fix to boost market shares and block competition, but—like most quick fixes—the lasting effect is negative and merely requires more of the same to maintain the status quo.

Pressure to promote (from retailers, the competition, and internal brand volume targets) will not go away, but brands must reduce the frequency and depth of promotions to help restore profitability and brand equity. Many well-known brands sell over 70% of their volume on deal, leaving them weak and vulnerable to cheaper alternatives.

To help reduce the "promotional crutch," brands must look to smarter marketing and activation at the point of purchase to deliver stronger sales.

Think Shopper

To reverse the situation of increasing promotions/declining brand and category equity will not be easy. Rather, it requires deep understanding, insight, and strategic and commercial planning. It begins with the end in mind: The Shopper. Often, suppliers are

Value is very dependent on perception, and there are many ways to communicate value.

so caught up in the commercial world of trading discussions that shoppers, who actually buy into the promotion, are completely overlooked: who they are, what their needs are, and why they would buy into a promotion. Is value unnecessarily being given away? The answer involves changing the go-to-market model and thinking “shelf back.” As brand managers will recognise, it is a complete change in the view of the retail world.

Today, accessibility to understanding shopper behaviour and types is better than ever. Tesco is widely known for using its Clubcard to track shopping habits and segment shoppers just as much as, if not more than, a loyalty mechanic to reward loyal shoppers. How much do suppliers take advantage of this? This does not have to equate to hugely expensive in-depth studies. Up-front thinking of the types of shoppers who buy into brands, and what they logically might want from promotions, is a huge step forward from the blanket approach of supporting BOGOFs once a quarter because “that’s what we did last year.”

Do suppliers and retailers know that a large proportion of the UK’s wealth is in the over 50s shopper group? Do suppliers and retailers acknowledge this when planning promotions? Do these shoppers want to load up their larders on BOGOFs and multibuys? Based on a common-sense understanding of such shoppers and their needs, the answer is “probably not.” Value is very dependent on perception, and there are many ways to communicate value. The over-50s group is more interested in health, convenience, inspiration, and quality. The types of shoppers who buy into the “larder-loading” promotions are not brand loyal and, frankly, eat into the bottom line. They drive a short-term volume increase but do not drive the more important, longer-term brand metrics of loyalty, penetration, frequency, and weight of purchase. Put simply, they cost the brand money.

Promotions, however, are not all doom and gloom. When used correctly and linked to shopper insights and clear objectives, promotions can be a positive tactic used to build brand and category equity.

The Shared Challenge

Understanding shopper behaviour through shopper insights is one-half of the equation. Implementing changes in the store, a shared responsibility of the retailer and supplier, is the other half.

Still, promotions are a good short-term profit generator for the retailer. To influence retailers to *want* to change the promotional mix, a strong category vision and strategy that illustrate the case for change—and the ultimate prize via total category growth—is essential.

Strategic Promotions

A strong category vision and strategy provide the framework to plan and implement strategic promotions. A strategic promotion aims to positively impact shopper and consumer behaviour, whereas "transactional" promotions purely provide the shopper with a price incentive to purchase. Examples of strategic promotions may be on pack coupons, which encourage repeat purchase or gifts that build brand equity. The measure of difference is in the objective: Is it driving a positive consumer-behaviour change or just short-term volume?

Kantar Retail recommends that an absolute minimum of one in 10 promotions implemented should have a strategic purpose. This approach marries the realism of the demand from customers for transactional volume driving with the necessity for longer-term, equity-building promotions.

Transactional Promotions

Let us not leave the impression that transactional promotions must always be detrimental. Much headroom exists to achieve the same volume results but with much more efficiency. Simple analysis will demonstrate the optimal point at which to achieve volume and profit. Deal buyers look for a strong deal, but the deal must not always be as strong as 50% off. Reducing the discount offered and strategically planning the promotion's timing to maximise the volume driven can achieve significant savings back to the bottom line.

Shopper Marketing

Ultimately, the key to driving brand and category equity is in broader thinking about the total promotional mix and shopper marketing plan—ensuring the right shopper is targeted, in the right store, at the right time and using the right media to communicate the right message. Best-practice shopper marketing plans deliver the strategic context of the total category vision.

Key Takeaways

- As the platform for a strategic approach in challenging times, shopper insights are critically important.
- The development of a category vision is essential to sell a promotional plan to a retailer.
- Promotions must have clear objectives in identifying the desired behaviour change and the group of shoppers to target.
- Deep, price-led promotions are in reality bought mostly by "deal-hunting" shoppers who are not brand loyal.
- A balance of equity building and transactional promotions must be achieved to begin reversing the trend of declining brand and category equity from consistent over-promoting.

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A Taste of the Future

The Online Grocery Market in the UK

By Olli Hellmann / Originally published on April 22, 2010

Online grocery is not just another retail channel emerging, as it has truly revolutionised the way consumers shop for food. For suppliers, web-based technologies and strategies employed by retailers represent never-before-encountered challenges. If suppliers want to succeed in the online retail world, they must develop solutions to these challenges. Here, Kantar Retail looks at the most dynamic online grocery market in Europe, the United Kingdom—particularly the innovations retailers have implemented in recent years to stay ahead of the competition and consequent implications for suppliers. These insights will also be highly valuable for future strategic planning in other markets where online grocery is not as developed as it is in the UK.

Online Retail Models

Grocery retailers all over the world have developed different ways of integrating the growing opportunities provided by the Internet into their sales strategies. Broadly speaking, three different retail models can be distinguished: 1) the shopping trip starts online and finishes in a brick-and-mortar store; 2) the shopping trip starts in an offline shop, but the purchase is made online; or 3) the whole shopping trip takes place in the virtual world (Figure 1).

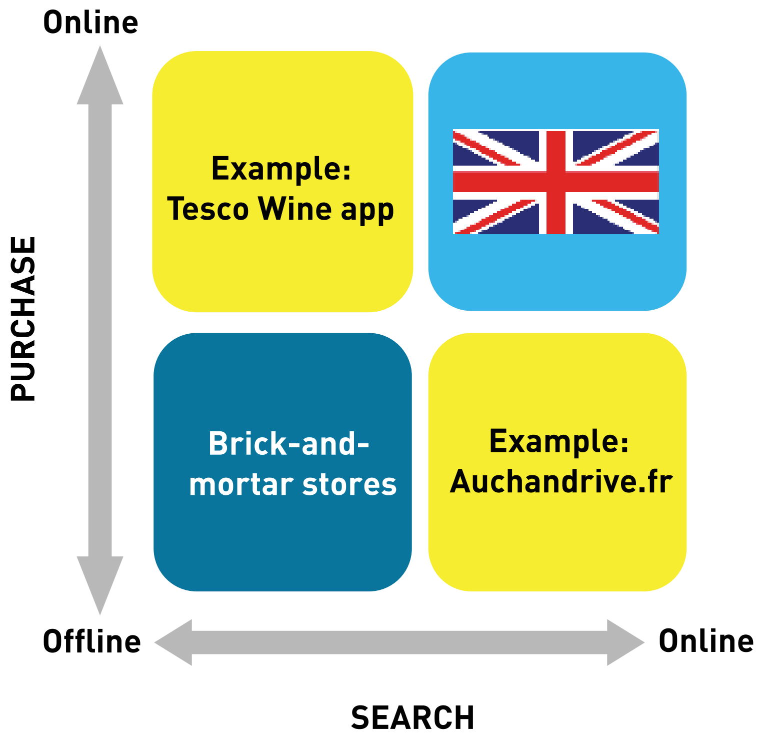

Figure 1. Online and Offline Retail Strategies / Source: Kantar Retail research and analysis

Model 1: Shopping Trip Starts Online, Finishes in Brick-and-Mortar Store

Recently, this model has been attracting a lot of attention from French grocery retailers. Auchan, Leclerc, and Système U have launched concepts that allow shoppers to choose their groceries online and then pick their order up in stores or special drive-in facilities. In two of its hypermarkets, Auchan has been testing the Keyshopping scheme, which lets shoppers create a shopping list online and print a store map with all the shopping items located before heading to the offline store.

Model 2: Shopping Trip Starts in Offline Shop, but Purchase Is Made Online

So far, this model has only been of limited interest to grocery retailers. One of very few examples is Tesco's Wine Finder app for the iPhone. After taking a photo of any wine bottle label, shoppers receive tasting notes and information about that particular wine. The application will direct the user to "Tesco Wine by the Case" at Tesco.com/wine, so customers can buy their selection directly from their mobile phone.

Model 3: Whole Shopping Trip Takes Place in Virtual World

This is the dominant model in the UK online grocery market, and it is the focus of this article. The shopper never sets foot into a conventional store; every step of the shopping trip is virtual.

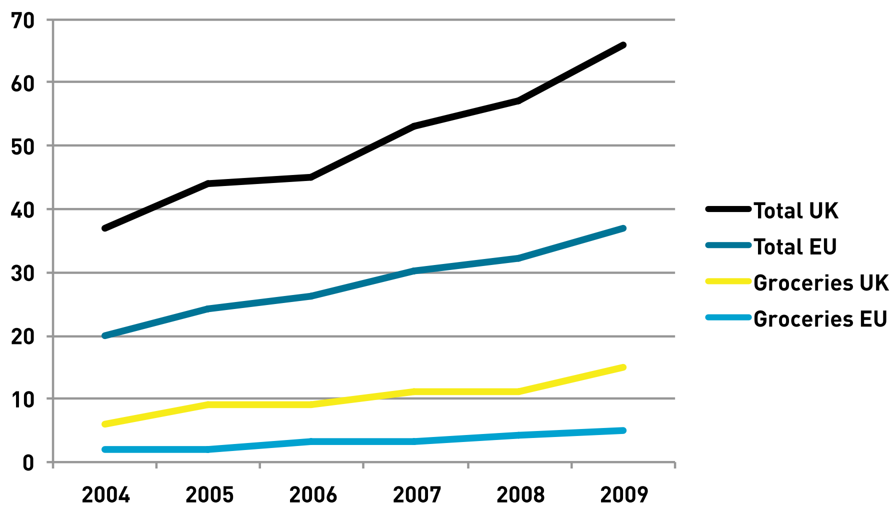

Figure 2. Consumers Who Made a Purchase over the Internet in Previous 12 Months
Source: Eurostat

The UK's Move Toward Universal Broadband Access

According to Eurostat, the UK has one of the highest Internet penetration rates in Europe. In 2009, 77% of households had Internet access, which is considerably higher than the 65% EU-wide rate. Of those households with Internet access, 90% had a broadband connection, a significant increase from 69% in 2006. The proportion of households able to access the Internet, however, varies between UK regions: The highest level is found in London, and the lowest proportion is recorded in Scotland. Moreover, access to the Internet is less widespread among certain social groups, such as low-income classes, older people, and ethnic minorities.

In March 2010, the UK government announced a tax on telephone landlines to help pay for the expansion of Internet services to rural areas and socially marginalized groups. The goal is to provide 90% of the country with access to super-fast broadband by 2017.

Europe's Most Dynamic Online Retail Market

Partly due to the well-developed broadband infrastructure, British consumers have become the most prolific online shoppers in Europe. In 2009, 66% of British adults had bought goods or services over the Internet in the previous 12 months, compared to only 37% on average in other EU member states (Figure 2). Denmark followed in second place with 64%. Sweden and the Netherlands shared third place with 63%.

According to a study on Internet usage conducted by the Office for National Statistics, the most often cited reason for shopping online is convenience. British consumers also like the fact that they can buy products that are not available in their area. Furthermore, price perceptions play a role, as many people think that online stores offer better prices than more traditional retailers. A common explanation for why people decide not to shop online is simply that they prefer the experience of shopping in person. In addition, many consumers are deterred by concerns about payment security and identity theft.

In 2009, the most popular items to buy online were films and music (50%), followed by clothes and sports goods (49%), and household goods (for example, furniture or toys). Groceries were a less common purchase (22%), but women were twice as likely to purchase groceries than men (30% compared with 15%). Age is another factor, with younger people (25–44 years old) more disposed to buying groceries online than the 45–54 or the 55–64 age brackets (28% compared to 22% and 19%, respectively).

Overall, this means that—in 2009—15% of Brits had ordered groceries over the Internet in the previous 12 months. This makes the UK the most active online grocery market in Europe, well ahead of Germany (9%) and Denmark (6%). Although the online channel still accounts for a very modest share of the retail grocery market, this share continues to rise. In 2004, the online sector contributed just little more than 1% to overall grocery sales. By 2009, the rate increased to 2.2%. The market was worth GBP 3 billion, having grown at a compound annual growth rate (CAGR) of almost 22% between 2004 and 2009 (Figure 3).

Online Retailers and Their Strategies

In the UK, most of the leading online grocery retailers are the major food retail groups with brands that are very familiar to shoppers. The first of these retailers to launch an online grocery retailing business was Tesco in 2000. An estimated 250,000 grocery deliveries are made by Tesco.com per week, making Tesco the undisputed leader of the UK online grocery market with a 52% share of sales. The other three larger players are Sainsbury's, ASDA, and Ocado—each holding around 15% market share (Figure 4). Waitrose just started an online delivery service in 2009, generating about GBP 25 million in its first year. Waitrose is closely tied to Ocado (the latter sources its supplies from Waitrose) and has agreed not to expand its online business in the Greater London area, Ocado's main geographical focus of operations, through 2014.

Founded in 2002 as an online-only retailer, Ocado is the only larger Internet grocer that operates exclusively from a warehouse. All other retailers run their online shopping service primarily from their brick-and-mortar stores, with staff picking items selected by online shoppers from the supermarket shelves. However, some major investments have been made recently, as retailers are trying to make their online logistics more efficient. For example, Tesco opened a new online order processing facility in Kent in 2008; ASDA is piloting a new

	2004	2009	2014E	CAGR '04-'09	CAGR '09-'14E
Total	98,791	137,726	175,690	6.9%	5.0%
Online	1,124	3,027	6,110	21.9%	15.1%
Share online	1.1%	2.2%	3.5%		

Figure 3. UK Grocery Market in GPB Million / Source: Kantar Retail database

	2004	2009	2014E	CAGR '04-'09	CAGR '09-'14E
Tesco	719	1,581	2,094	17.1%	5.8%
Sainsbury's	153	503	1,198	26.9%	18.9%
ASDA	140	486	1,859	28.2%	30.7%
Ocado	107	451	953	33.3%	16.2%
Total	1,124	3,027	6,110	21.9%	15.1%

Figure 4. Major Online Grocery Retailers in GPB Million / Source: Kantar Retail database

Kantar Retail expects the UK's online grocery market to reach a value of GBP 6.1 billion by 2014 ... given that convenience is a main driver for shopping over the Internet, online will steal share from conventional supermarkets.

"virtual store" near Leeds; and Sainsbury's has heavily invested in IT enhancements.

Driving Traffic

All retailers have been working very hard on driving more shoppers into their online stores. In particular, they have been focusing on the specific strengths of the Internet vis-à-vis shopping in conventional channels. One area that has received a lot of attention is convenience. Following are examples of retailer efforts to make shopping online easier and less time-consuming than in conventional channels:

- Ocado launched an iPhone application in summer 2009, allowing consumers to shop on the go.
- Tesco linked its loyalty card database to its web store, meaning that products consumers buy regularly in a brick-and-mortar store will automatically be saved to their online "favourites" list.
- On the Sainsbury's website, shoppers can add all ingredients for Jamie Oliver's recipe ideas to their virtual shopping basket with a single mouse-click.

Advertising Low Prices

Retailers have been fiercely promoting the price savings consumers will achieve when shopping over the Internet.

- Tesco and ASDA launched the "switch-and-save" option: Whenever a shopper picks a product, the website will suggest a comparable, cheaper item.
- Ocado offers "Internet Only Prices" on Waitrose own-label products and labels products with "Tesco Price Match" if they are not more expensive than in Tesco brick-and-mortar stores.
- Ocado was the first of these retailers to abolish delivery charges—on orders over GBP 75 and made during "quieter" time slots.

Promoting Sustainability

Retailers have found ways of selling online grocery shopping as an environment-friendly alternative to shopping in conventional brick-and-mortar stores.

- Tesco introduced the bagless delivery in 2007, using only reusable plastic boxes, and it offers a "green delivery" option, highlighting delivery slots with a delivery already scheduled in the shopper's local area.

- Ocado praises itself for running all of its delivery vans on recycled vegetable oil.

In addition, the four big players in online grocery have extended their online business to non-food products, including categories such as clothing, electrical appliances, and furniture. Tesco started the trend in 2006 with Tesco Direct, followed by ASDA in October 2008 and Sainsbury's in July 2009. Even Ocado now stocks a growing selection of non-food products, such as cookware and toys.

Independent Price Scrutiny

Driven by the rapid growth of the online grocery market, a variety of third-party products has emerged to help the consumer take full advantage of the virtual shopping world. One very popular website is MySupermarket.co.uk, which allows shoppers to compare the price of their virtual trolley across all four major online supermarkets in real time.

Shoppers can then pick the cheapest retailer and will be taken directly to the checkout of that particular online store.

Also increasingly popular are voucher websites offering discount codes for web retailers, such as VoucherCodes.co.uk or MyVoucherCodes.co.uk. Finally, through the rapid penetration of smartphones, shoppers are now able to access the Internet in conventional offline stores. With the latest smartphone applications, such as RedLaser or ShopSavvy, shoppers can scan the barcode of any product using the built-in camera, and the phone will then search for cheaper offers on the Internet.

The Future of the UK Online Market

Kantar Retail expects the UK's online grocery market to reach a value of GBP 6.1 billion by 2014. Although growth is likely to slow down in the future due to the sector maturing, the online channel will still grow faster than the overall grocery market (Figure 5). In particular, given that convenience is a main driver for shopping over the Internet, online will steal share from conventional supermarkets. Other convenience formats, on the other hand, are likely to remain largely unaffected by the rise of web grocers.

The growth of the online grocery channel will be driven by consumers trying to save more and more time on their weekly food shop, consumers becoming more Internet savvy, further advancements in technology, and the expansion of the high-speed broadband network. At the same time, the established online grocers will continue to refine their strate-

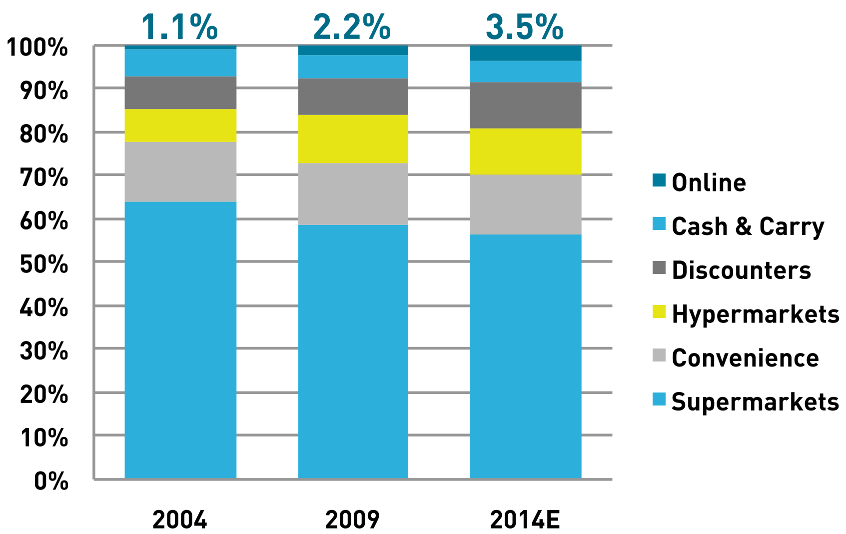

Figure 5. Share of Grocery Sales by Retail Channel / Source: Kantar Retail database

gies and optimize their logistics processes. Tesco is very likely to retain its leading position in the market, but other retailers will close the gap (Figure 4). Ultimately, the battle will be won by those most successful in attracting consumers who are not yet doing their grocery shopping online or only do so infrequently.

A possible threat for established online grocers could come from other retailers launching an Internet food shopping service. Two larger UK retailers without a web store are Morrisons and Marks & Spencer. While there seems to be space for further market entries, much will depend on whether these two retailers will be able to shoulder the immense financial investment of setting up an online delivery service. A third player to watch out for is Amazon, one of the world's leading online retailers. In the United States, Amazon sells dry foods through its main website and in 2007 launched AmazonFresh, an online grocery service covering certain areas of Seattle, Washington.

What remains to be seen is whether the current model of Internet retailing will be able to withstand the fierce price competition in the channel. The ongoing price war in the grocery market is likely to escalate in the virtual world. If Amazon enters the UK grocery market, this will probably shake up pricing for bulk dry foods. One possible option for UK online grocers to cut costs could be the French model of "ordering online but picking up in the store." Online newcomer Waitrose already offers this option to shoppers. If this model proves to be more profitable, other retailers may follow suit.

Supplier Implications

Although online still accounts for only a small share of sales in the overall UK grocery market (2.2%), this share is growing rapidly (3.5% by 2014). Other online grocery markets outside the UK are forecasted to grow, particularly in continental Europe. Suppliers are thus given an exciting opportunity to grow alongside a dynamic new channel, but they must follow the trend of online grocery shopping very closely and prepare to face new challenges.

One challenge is the intense price competition in the online retail market, which will be even tougher than in conventional grocery channels. Using third-party products, consumers can compare prices in real time and then pick the cheapest offer—an option not available in the conventional channels. In the UK, retailers are already fighting a fierce price war, which has now spilled into their virtual stores. Web grocer Ocado, for example, has been trying to match the prices of market leader Tesco, while supermarkets have continued to keep promotion levels high—for various reasons, one of which is to discourage shoppers from moving online. Price competition in the online channel raises a number of questions for suppliers:

- What special promotions/discounts do they want to offer online? Do they want to offer the same promotions/discounts online as conventional retail channels?
- Which parts of the product range do suppliers want to expose to the demanding price pressures in the online retail world? Considering that the online channel is mainly used for large weekly shops while other channels will be used primarily for top-up shops, do suppliers want to sell the same product offer online and offline?

A second challenge for suppliers arises from the fact that Internet shopping is largely driven by customer convenience (time and effort). Features of grocery web stores, such as favourite lists or the option to shop on-the-go with mobile phones promote a habitual shopping behaviour. Shoppers could be less inclined to try new things but might tend to stick to brands they have bought before. In other words, online retail technologies help to maintain consumer loyalties: good news for brands that already find themselves in the virtual shopping basket but a challenge for brands that still sit on the virtual shelf. The latter must work much harder than in the conventional shopping channels to encourage purchase trial.

Online purchase loyalties could become even stronger if web retailers combine price and convenience. One striking example of where the online retail market could be heading is Amazon's "Subscribe & Save" scheme in the US, which gives customers 15% off and free shipping on grocery items if they sign up for auto-replenishment. Getting onto consumers' virtual shopping lists now is vital for suppliers, as changing consumers' purchasing habits could become increasingly difficult in the future. This is particularly true in the current economic climate, which has prompted consumers to re-evaluate their brand loyalties for the next decade.

Last but not least, the growing trend of shopping groceries over the Internet will have profound implications for branding—both for supplier brands and retailer brands:

- Since point-of-sale marketing is not an option in the online grocery channel, retailer brands must communicate their emotional and rational benefits to consumers before they enter the virtual store. Online, packaging will be less important as a marketing tool since shoppers cannot touch the product or interact with it. Instead, breaking through the clutter will become more dependent on other touchpoints. Ironically, packaging could gain increasing importance on conventional shelves as a memory aid for consumers' next online shop.
- Grocery retailers will find it increasingly difficult to develop a strong emotional bond between their brand and consumers. Shopping groceries is a much less personal interaction than visiting a brick-and-mortar store, where the retailer has a much stronger influence on the shopper's mood. Again, the decision to shop online is primarily driven by functional factors such as price and convenience. This undermines emotional bonding between the consumers and the brand, as consumers are likely to switch to whichever online retailer can objectively score highest on these points.
- In the online world, supplier brands may have an advantage over retailer brands, since the brand's benefits communicated through marketing can be experienced when consuming the product. The role of the retailer, on the other hand, could be limited to delivering these brands to the consumer's front door.

In sum, while online retailers control powerful tools to influence shoppers' shopping lists, they are highly vulnerable to price attacks from competitors, since building an emotional bond with shoppers is very difficult. Suppliers, on the other hand, must rely heavily on retailers to get onto consumers' shopping lists, but they are in a much better position than retailers to develop an emotional connection between their brand and consumers. Both sides thus need each other, which opens new opportunities for establishing fruitful partnership relations.

Russia's Trade Law Marks First Attempt to Regulate Commercial Policy

By Vadim Khetsuriani / Originally published on February 11, 2010

On February 1, 2010, the first Russian law regulating modern grocery trade development and the business relationship between suppliers and retailers took into effect. To align with the new trade law requirements, grocery suppliers and retailers now have six months to draft and sign new contracts of supply. The law clearly presents an opportunity for both parties to develop a new set of business requirements from the partners and renegotiate the contracts. It is essential for suppliers to understand the risks and to take the lead in building new pay-for-performance principles. In this article, we highlight the most important clauses in Russia's first law to regulate modern grocery trade and commercial policy development between suppliers and retailers.

First and foremost, the law limits the ability of retailers and suppliers to include conditions and compensations for these conditions in the main contract of supply—apart from the volume bonus. This means that if before the total bonus (usually a percent of the invoice product cost) was agreed upon in exchange of volume and other services that retailers render to suppliers (such as shelf space, promo, listing, etc.), putting other conditions besides the volume in the main contract of supply is prohibited. This bonus (which can now be clearly called a "volume bonus") is also limited to 10% of the invoice cost of the products. Other compensations for services must be agreed upon outside of the main contract of supply and as part of an additional agreement.

Most importantly, the agreement on compensation for other services cannot influence the decision on the main supply contract agreement, and additional service contractual provisions cannot be used as a counterpart of the main supply contract. This part of the law is perhaps the biggest change to the commercial policy, and it creates new risks and challenges for suppliers. Clearly, this clause is not limiting retailers' ability to generate "back margin" for retailers. However, it "dilutes" the value of the bonus in the main supply contract. For example, if last year a supplier was paying an 8% bonus for volume and other services, written in the contract of supply, this year the retailer can still keep the 8% bonus but cannot commit to anything but volume in the contract.

Other services must be agreed upon separately, which gives retailers an opportunity to charge separate fees and thus increase the total back-margin generation. In addition, if the retailer was paid a bonus above 10%, the additional amount will have to come in a separate agreement. (For example, if the retail was paid a 14% total retro bonus last year, 4% will have to come in a separate agreement this year.) Retailers now have an opportunity to use the clause of limiting the retro bonus to 10% to either demand the additional 4% on the invoice or to develop a new price list for services, increasing the cost of these services to compensate for the limit in the retro bonus.

Figure 1 summarizes retailer margin levels and the likely opportunities for retailers to renegotiate better conditions, which suppliers should keep in mind.

Margins	Example	Description	What Will Likely Happen
1 Net	5%	Front margin, enabling retailers to lower prices without risk of "selling below cost"	Will increase by retailers that were paid more than 10% on the 2 net
2 Net	10%	Volume bonus only according to new law	If was below 10%, can be pushed to reach 10% limit
3 Net	4%	Services such as promo, distribution, shelf, etc.	Will increase by retailers that were paid more than 10% on the 2 net

Figure 1. Retailer Margin Levels and Opportunities

Source: Kantar Retail research and analysis

Using the example on the previous page as a hypothetical retailer margin structure, we can conclude:

- Retailers that did not "sell" enough services to suppliers because the amount they were getting in 2 net (retro bonus) was above 10% will likely increase the cost of services, increase the number of services offered, or both. Clearly, the objective will be to maximize the cost of services to compensate for the limit of the 2 net retro bonus to 10%.
- Tracking the completion of services will become more important for suppliers for two reasons:

1. The cost of services or the amount of services offered will likely increase. Suppliers must negotiate the services carefully to determine what exactly they would like to purchase and what services are measurable and valuable for their brands' distribution.
2. If suppliers pay for the services to retailers but do not have proof that the services were rendered, they will have a difficult time allocating these costs as expenses for a tax deduction. Since these services are not part of the main supply contract, the government needs more "proof" that these services were rendered to allow suppliers to recognize these costs as "expenses."

- While the pressure on the front margin is not directly linked to the new law, retailers can still use the new law as an opportunity to ask for lower invoice prices, especially if they were getting a retro bonus above 10% last year.

Another significant regulation from the new trade law is the directive of payment days for grocery products, as shown in Figure 2.

This regulation poses some risk to suppliers, in particular:

- If a supplier was paid below the payment day's limit maximum, retailers will use the law as an opportunity to renegotiate terms and get the maximum extension for payments. Suppliers must develop strong quantitative arguments to negotiate such payment extensions; without it, retailers will use the law as an "excuse" to extend payment terms.
- If suppliers are to be paid more regularly by retailers in light of the new regulation, this can result in shrinkage of space that this supplier was taking on the shelf. Not being able to compensate the product inefficiencies with longer payment terms, retailers will choose to delist the slow-turning assortment or cut the number of facings of these products on the shelf. In addition, the new law complicates the agreement process between retailers and suppliers on assortment: It prohibits the ability to envisage a fee for changing the assortment of food products.

Product Expiry Dates	Payment Days Maximum Limit by Retailers to Suppliers
From within 10 days	Within 10 working days
From within 30 days inclusive	Within 30 calendar days
From within more than 30 days + alcoholic products made in Russia	Within 45 calendar days

Figure 2. Payment Days for Grocery Products

Source: Kantar Retail research, published text of the new trade law

The implication for suppliers from the regulation of payment terms is clear: Suppliers need to measure the stock rotation more effectively and on a regular basis in order to review it with retailers. Stock turns should be used as a common target to ensure that retailers maintain their working capital efficiency, and suppliers in term will be able to maintain their shelf space—backed up by the certain agreement on replenishment. This may result in higher logistics costs, as some suppliers will be forced to deliver the products more frequently so as not to overstock retailer systems.

Finally, the law has some strategic growth regulations for retailers that will affect suppliers' business. Retailers have been imposed a ceiling on market share in constituent entities of the Russian Federation and/or municipalities of 25%. While the ways of measuring market share within the set boundaries are yet to be developed by the government, this market share limit does not allow retailers to continue to grow in their "home regions" organically or by acquisitions. For retailers such as Magnit (which has a very high market share in some of southern cities of Russia) and for X5 (which has a high market share in Moscow and St. Pete), this limit means that—in the long term—growth must come from outside of the "home territory." This puts the following constraints on retailers, which will have a long-term effect on the supplier community:

> If suppliers are to be paid more regularly by retailers in light of the new regulation, this can result in shrinkage of space that this supplier was taking on the shelf.

- Large retailers will engage in regional acquisitions more actively, which can have a negative effect on their operating efficiencies, particularly logistics costs. Retailers will push for higher logistics fees from suppliers to compensate for these inefficiencies.
- With acquisitions or organic growth outside of "home regions," retail networks will collide and competitive pressures will increase. In the likelihood of increased competition, the pressure will probably remain on price (that in turn will be transmitted onto suppliers). If retailers will uncover trading term inconsistencies between them and their potential acquisition targets, this will cause rounds of negotiations when retailers will try to align conditions. This will be an issue for some suppliers that have big inconsistencies and lack a logical framework in how much they spend on services with retailers.

Kantar Retail Point of View

Russia's first trade law presents several key factors. Along with the top-of-mind issues discussed here, other regulations within the law give power to the government to control prices *for certain types of socially important food products* and to regulate the commercial policy on those products. This section is still a "work in process" because the list of "socially important food products" has not been announced yet. The law is also set to develop frameworks for disclosing information on conditions of counterparts selection by retail networks and suppliers (and essential terms and conditions of contracts between them), although the actual practice is not clearly set yet.

What is certain is that the law as is has a lot of ambiguities and will be revised by the government in the coming years. However, this law marks the first attempt of the government to regulate the commercial relationship in the modern grocery industry.

To align with the law in its current context, suppliers and retailers are given six months to renegotiate their agreements. It presents opportunities for both parties to improve trading terms. Suppliers should be proactive and:

- Analyze their current trading terms' structure and foresee the possible scenarios of change and risks/"gaps" that retailers can take advantage of.
- Develop new frameworks of paying for services and clear, consistent rules for capturing the services rendered to avoid tax issues.
- Develop valuable counterparts—which should be presented as effective "selling stories" to retailers—aimed at helping retailers develop categories, bring shoppers back to the stores, and develop shopper loyalty.

In the context of Russia's economic crisis and the depressed shopper demand, retailers need strong supplier brands in their stores more than ever. Private label capacity in Russia is not strong enough to attract shoppers. Given that brands play a vital role in retailers' success, suppliers should approach renegotiation of the contracts with a clear and concise framework of pay-for-performance principles and to do so with a positive attitude of joint business planning and winning with the shopper. The new law is an opportunity for suppliers to re-evaluate what they have been paying for and to agree with retailers on effective ways of engaging with the shoppers and developing categories. Such an approach should ease the tension of negotiations and result in more strategic partnerships being built between large FMCG suppliers and leading grocery chains.

In the context of Russia's economic crisis and the depressed shopper demand, retailers need strong supplier brands in their stores more than ever.

Retailing in Emergent Markets

Contributed by David Marcotte and Jim Leonard, Kantar Retail; Gwen Morrison, WPP – The Store; and Sonia Misak and Christina Vuleta, Futures Company / Originally published January 2010

An excerpt from "Retailing in Emergent Markets: Strategic Foundations & Best Practices," this article features a framework for assessing the pace of change in emergent markets, typical market drivers and disruptors, and best-in-class retail responses to serving a diverse, highly dynamic local shopper base.

Figure 1. Six Retailers on Four Contents Involved in This Study / Source: Kantar Retail research and analysis

Abandon all preconceptions.

The best way to approach an emergent market is with openness and a sense of discovery. Looking for absolutes will most likely lead to frustration rather than enlightenment. Though some characteristics tend to hold true across markets, most—by their very nature—defy predictability.

International retailers often arrive in emergent markets because their home retailing market is saturated, and growth requires stealing market share from the competition. That isn't typically the case in emergent markets, which is part of their appeal. In emergent markets, growth depends primarily on attracting both occasional shoppers and repeat customers for whom contemporary malls and stores are a relatively new experience. The key challenges involve reaching these customers, educating them about organized retailing, and helping them smoothly transition to what for them is a new way of shopping.

Growing a retail business requires a proposition that appeals to potential customers at all income levels and operators who are willing to take a long-term view of retail market development. Wealth exists in emergent markets but, until recently, has been concentrated in a narrow band of the population. Most emergent markets now include a rising middle class.

An Open Mind

To a great extent, success in an emerging market depends on an open mind. It's not like dropping another store into a city in a developed market, which is usually an exercise in leveraging existing capacity. While the retailer makes some commitment to the local community, generally in the form of additional jobs, the expansion is strictly about business.

There's no reason to enter an emergent market without an expectation of increased revenue or profit, of course. That is the main motivation. It's easier to succeed as a new entry, however, if profit does not remain the only motivation. Once in an emergent market, the retailer becomes part of a dynamic effort to improve the lives of the nation's people. Through products sold and services offered, successful retailers understand the current state of development and help customers move it forward. Three initial insights to guide this process are:

1. **Everyone who walks into the store is a potential customer.** This retail aphorism especially applies in emergent markets where retailers must understand how to turn customers, from all income levels, into shoppers.
2. **Retailers must become part of the local retailing landscape.** Being perceived as the local outpost of an international retail chain is less likely to work.
3. **Customers recognize when a retailer sincerely cares about their community.** They will reward caring retailers with their patronage.

The Shopping Environments

Retailing in emergent markets divides into two separate trades: the fragmented and the organized. Most consumers typically shop both.

The Fragmented Market

The traditional, or fragmented, market comprises the many ways that consumers have historically purchased goods (Figure 2). It's retailing in the purest sense of the term. Shopping at the local outdoor "wet market" is a daily event. Products are on display, but access to them often requires the help of the merchant. Price is determined by direct negotiation between buyer and seller.

The assortment is limited and availability isn't assured, but sometimes the products are unique. Credit is offered. In fact, because people are often paid daily, their cash is limited, making credit mandatory. This credit is usually "book credit" whereby the retailer keeps a written record of purchases. Retailer profitability sometimes depends more on the credit terms than on the sale price.

Figure 2. Typical Fragmented Retail (Soweto, South Africa)
Source: Kantar Retail market visit

Figure 3. Pick n Pay Hypermarket (Soweta, South Africa)
Source: Kantar Retail market visit

The Organized Market

The organized retail market consists of malls and stores that specialize in certain categories or include multiple departments such as hypermarkets. The stores are usually part of a chain within a larger retail or holding company (Figures 3 and 4).

Merchandise is available for browsing in store environments that often are self-service and provide other value-added services, such as banking, that can make the store not just the location to obtain products but also a destination.

Pricing is fixed. Product range can be extensive with predictable availability. Retailers maintain credit programs, but profitability depends more on margins. Credit helps drive sales by making merchandise affordable. It also feeds databases with customer information used for marketing.

Figure 4. Beijing Hualian Group (BHG), China
Source: Kantar Retail market visit

Not "either/or"

It'd be logical to expect that the entrance of retail chains wielding the advantages of technology and economies of scale would be followed by the disappearance of small shops. This conclusion could reasonably be drawn from a casual glance of retailing in North America or Europe. It'd be wrong, however, when applied to emergent markets. At least in the near term, organized retailing isn't superseding traditional retailing in these countries. The organized and traditional markets coexist side by side. Shoppers move fluidly back and forth. Both options serve the needs of the emergent market consumer—but in different ways.

An emergent market is in transition. People shift easily between daily life as it has been and life as it's becoming. They may visit local merchants in their

Figure 5. Convenient Locations, Biedronka (Poland)
Source: Kantar Retail market visit

village but also shop in the superstores that they pass during their commute for work in the city. The most convenient, or most flexible, format often wins out (Figure 5).

Consumers may enjoy the broader selection in the organized trade, but they need the traditional trade to survive for several reasons. First, the shops sometimes provide products that are unavailable in the organized trade, a wider range of fresh options, or even the option to buy goods in very small (affordable) increments unavailable or impractical in the organized trade. Second, the shops are convenient. Third, the local merchants offer credit. Finally, consumers enjoy ongoing relationships, often friendships, with retailers in the fragmented trade.

Place

Place is an important concept for understanding emergent markets. With various distinctions, place emphasizes how complex these markets are and organizes the multiple facets into a comprehensible whole.

- **Geography:** Is the market primarily urban or rural? Are there expansion opportunities to neighboring countries?
- **Culture:** What are the major holidays? What special foods and other items are needed for their celebration?
- **Government:** How stable are the politics? How extensive are educational and other programs that can impact retailing?
- **Location:** How available is public transportation? Can the customer walk to the store from home, or is the store a place to stop during the work commute?

Drivers of Change

To understand retail development in emergent markets, we focused on three drivers: the consumer/customer, retail or business consolidation, and disruptors/escalators. The interaction of these drivers can be complicated but form a useful framework for explaining the shape and speed of development in emerging markets.

The Costumer

Emergent market consumers are shifting more spending to the organized market for several reasons.

- **Demographic shifts:** People move from rural areas into cities where modern stores are located.

- **Disposable income:** Government programs, such as improvements in education, increase household spending.
- **Product availability:** Retailers in the organized trade expand the range of available products.
- **Price:** Economies of scale make item pricing more affordable in the organized market.
- **Trip aggregation:** Traditional daily shopping becomes inefficient as more women enter the workforce.
- **Product quality:** International retailers and their suppliers raise quality consistency.
- **Shopping experience:** Beyond filling basic needs, recreation becomes a reason to go to stores.

Consolidation

Several factors drive consolidation of the modern trade.

- **Access to capital:** As the emergent markets become more stable economically, they attract increased international investment.
- **Information systems:** Installing state-of-the-art information technology provides a competitive advantage.
- **Supply chain:** Organized retailing will benefit from improvements in infrastructure and advancements in technology.
- **Wholesale structures:** Retailers in the organized market operate from their own distribution centers and depend less on the wholesalers that serve the traditional trade.
- **Homogenous customer base:** In many of these markets, the populations are less ethnically and racially diverse than in North America or Europe, which have higher rates of immigration. Consequently, diets and other product needs are fairly consistent. This sameness perfectly suits the chain-store approach.

Disruptors/Escalators

Emergent markets are much more unpredictable than developed markets.

- **Taxation and duties:** In some Latin American countries, duties on products are collected at state lines. Efforts to avoid those payments can make distribution more circuitous and less efficient.
- **Election cycles:** Some markets have democratic and dependable elections. Others do not. Regardless, in emergent markets, elections and political disruptions can have a greater, longer impact on retailers.
- **Economy:** Inflation, short-term funds, currency value, and external exchange rates are sometimes difficult to control.
- **Legislation:** Government intervention to stimulate the economy or to shape the society is common in all markets. The decision for China to stimulate consumer spending on home goods and consumer electronics in early 2009 is a good example of a positive disruption.

The Customer

In all markets, developed or emergent, customers are on a journey. In developed markets, we think of this journey as upward mobility. Customers see more and want more because they assume that more is always possible, that the future will be better. In emergent markets, until recently, the future looked no different than the present and the past. Individuals primarily focused on fulfilling basic needs to maintain life with food, shelter, and clothing or to cope with death by providing ritual funerals. Today, their concerns go beyond basics to include health care, education, and the acquisition of goods and services to not only sustain life but also make it better. People are changing their behavior: saving and spending in ways that match their aspirations for a better future.

Helping the customer move along this journey first requires understanding the realities of the customer's current existence: how much and how often they are paid, who in the household controls spending, and where they live in relationship to the closest store. Emergent market consumers have become keenly aware of prices and extremely resourceful as shoppers. Where, what, and how much they buy are influenced by many aspects of how they live.

Affordability

Retailers in emergent markets must reach out to low-income consumers because the middle class alone is too small to support a substantial business. The upper class is just as likely to spend away from the country as within. Low-income consumers provide immediate revenue, and the prospect of future growth and growing aspiration for a better future can propel these individuals into a growing middle class—on which the organized trade depends for large-scale growth over the long term. Retailers should consider:

- Does the customer have cash or need credit, which is typically more available in the traditional market?
- Who controls the money? In some markets, bank accounts may be shared by the entire household.
- What is the flow of money? In emergent markets, the ability to purchase constantly fluctuates according to when and how people are paid.

Proximity

Whether a consumer shops in a traditional or modern store can depend on which store is more conveniently located. City dwellers would normally enjoy more access to organized retailing, but villagers working in the city might shop in a modern store situated along the commuting route. In an urban area, where shoppers might walk to a store, the amount purchased would be restricted to the size and weight that could be carried. The availability of refrigeration at home, either owned or shared, also influences the purchase.

Community

Shopping, especially in rural areas, tends to be more communal than in developed markets. To save money, members of a village might combine funds to purchase commodities in bulk. The South African supermarket Pick n Pay has a format called Boxer, a hybrid cash and carry/grocery format, that serves this bulk purchase requirement (Figure 6 and 7).

Similarly, villagers might share the price of a taxi to visit an urban store if the total cost for the trip, including purchases and transportation, saves money. Time to make the journey to shop and greater assurance of product availability in the urban store would also influence this trip.

Customers might need an item only found in the organized trade because, as the emergent markets develop, customers require more than basic items. For example, women are now more likely to be in the workforce and require ready-made, inexpensive meal solutions.

It's increasingly important to offer some affordable luxury that addresses the customer's desire to live a better, more pleasurable life and to offer products that encourage shoppers' aspirations (Figure 8). Frequent purchasing, however, may remain beyond reach for some time.

Figure 6. Boxer's Market Environment
Source: Kantar Retail market visit

Figure 7. Boxer Bulk Packs
Source: Kantar Retail market visit

Entering the Organized Market

Customers from lower incomes first visit the organized market out of curiosity and for recreation. They are not traveling to a mall or hypermarket to buy a loaf of bread. They buy fresh bread locally at the bakery in their neighborhood. More likely, they're visiting the hypermarket to spend a day out with family.

The retailer's proposition—some combination of high value and low cost—raises the customer's expectations. The retailer's challenge is to move the customer from simply an observer seeking to be entertained to a shopper buying for basic needs. Plaza Vea is a good example of a retail banner coping with the mass of entertainment-oriented shoppers and working to get them to make an initial purchase (Figure 9). A shopper who can be persuaded to buy basic items is more likely to return on a frequent, if not daily, basis. Once that shopper visits the store regularly, the provision of credit enables the trade-up in merchandise from strictly basic needs to more aspirational merchandise (Figure 10).

Getting shoppers to buy basics sometimes requires helping them overcome their intimidation with the large stores and educating them about self-service and other big-store characteristics. Pay cycles can also pre-determine shopping patterns and trade-offs between needs and wants. The process of moving customers into the organized market requires many interrelated initiatives including:

- Providing an experience that fulfills the need for recreation.
- Getting the basic assortment of products and prices correct in an affordable set of transactions.

Figure 8. Aspirational Merchandise, Magazine Luiza (Brazil)
Source: Kantar Retail market visit

- Offering a relevant credit program.
- Adding value to become a one-stop shopping location or solution.
- Becoming a community-oriented venue by moving the cultural center of an area to the store via events and meetings.

Shopping as Leisure

Shopping as entertainment or leisure is a new pastime in emergent markets. Families filling stores and malls on weekends are a good indicator of a growing middle class enjoying the central perquisites of middle class life: disposable time and money.

The scene looks familiar to anyone who's strolled the malls or superstores of any developed market, but three chief concerns exist for emerging markets:

Figure 9. Plaza Vea Neighborhood Format, Peru
Source: Kantar Retail market visit

1) getting to the venue, 2) feeling safe while shopping, and 3) returning home safely. Because relatively few people in emergent markets can afford to own cars and public transportation is limited, malls and major stores are usually located near population centers and bus lines; some retailers even provide bus service. In areas where crime is a concern, the merchants provide effective and appropriate security, making the venue a safe, comfortable place where people socialize or enjoy a sense of community.

Connectivity

Nearly three-quarters of the world's four billion mobile phones are now used in emergent markets. Wireless technology arrived early and spread quickly in emergent markets, compensating for the lack of land lines and the inefficiencies of national postal ser-

Figure 10. Credit Options, Magazine Luiza (Brazil)
Source: Kantar Retail market visit

vices. The presence of extensive wireless technology enables retailers to transmit marketing messages to the mobile phones of customers.

Income isn't a barrier to owning a mobile phone. To saturate their markets, the major mobile phone providers have designed products that are affordable even to people living in poverty. They have aggressively introduced mobile phones through the rural village equivalent of Tupperware parties.

Suppliers

In the traditional market, suppliers and retailers enjoy long-standing relationships that smooth some of the bumps in an inefficient distribution system.

International suppliers can play an important role in improving processes and expanding product assortment in emergent markets. They can leverage the expertise they bring from developed markets by partnering with local suppliers, but it's not that easy for many reasons—especially logistics. Reliable delivery is a challenge when few distribution centers exist, and the roads generally are poorly maintained and clogged with traffic.

Meanwhile, retailers in the organized market remain the main educators of local suppliers. The retailers are attempting to close the gap between their systems and the lack of process sophistication among local suppliers. Areas of focus include quality assurance, product movement, in-store activities, and electronic communications and payment/EDI (electronic data interchange) standards. Retailers entering or operating in emergent markets understand best practices. However, implementation of best practices—especially in collaboration with suppliers—often presents the greatest challenge.

The full report, "Retailing in Emergent Markets: Strategic Foundations & Best Practices," is a result of an 18-month groundbreaking research study sponsored by the Coca-Cola Retailing Research Council Latin America. The global study examined the evolution and interplay between traditional and organized trade retailing and retail best practices across a range of emergent markets: China, Brazil, Peru, South Africa, Poland, and Turkey. Fieldwork included store audits as well as interviews with shoppers, store managers, retailer executives, and market analysts, ultimately producing a common set of "strategic pillars" or operating foundations common in many transitioning economies. To request an Executive Summary of this comprehensive report, contact Jim Leonard at 617.588.4105 or Jim.Leonard@KantarRetail.com.

2010 EMEA Events Calendar

KANTAR RETAIL

Kantar Retail believes that the only successful way for manufacturers to grow in the modern retail environment is by engaging with their retail customers in a collaborative, value-added business partner basis. Our calendar features training workshops and forums across a variety of markets and retail channels, all designed to enable our clients to build such relationships with those retail organisations that are driving growth across the EMEA region.

Q3

Auchan & Metro Russia Workshops — Moscow

Sep 21 Business Planning for Auchan
Sep 22 Business Planning for Metro C&C
Geographical coverage – Russia

CEE SkillBuilders™ & Channel Workshops — Warsaw

Sep 27 Retailer Financial Models
Sep 28 CEE Discounter Channel Workshop
Geographical coverage – Central & Eastern European

Spain Retail Forum NEW — Madrid

Sep 30 Spanish Retail Trends Overview
Geographical coverage – Spain

Q4

Lidl & Metro Global Workshops — Dusseldorf

Oct 13 Selling to Lidl STREAM
Geographical coverage – Europe

Oct 14 Business Planning for Metro Cash & Carry STREAM
Geographical coverage – Global

Carrefour Global Workshop — Paris

Nov 16 Business Planning for Carrefour STREAM
Geographical coverage – Global

Buying Groups Workshop — London

Nov 30 Buying Groups Workshop
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Getting It Right

Forecasting Retail Sales

By Frank Badillo / Originally published on April 13, 2010

In January 2009, Kantar Retail laid out a US forecast for 2009 that in retrospect is particularly insightful when you consider what was happening at the time.

- Retailers and suppliers were bracing themselves for a free-fall in consumer spending in the wake of reports for the just-completed holiday of 2008. Retail sales had fallen for the first time in the 40+ years that the government had been collecting sales in a similar manner.
- Consumer confidence was sinking toward its low point, which was reached the next month in February 2009. Feeding the pessimism was an ongoing string of negative economic reports, starting with an employment report showing the biggest prior-year job loss since World War II.
- The only thing growing was the number of dire forecast scenarios, including a prediction by the International Monetary Fund in January 2009 that the *world* economy would see its worst performance since World War II.

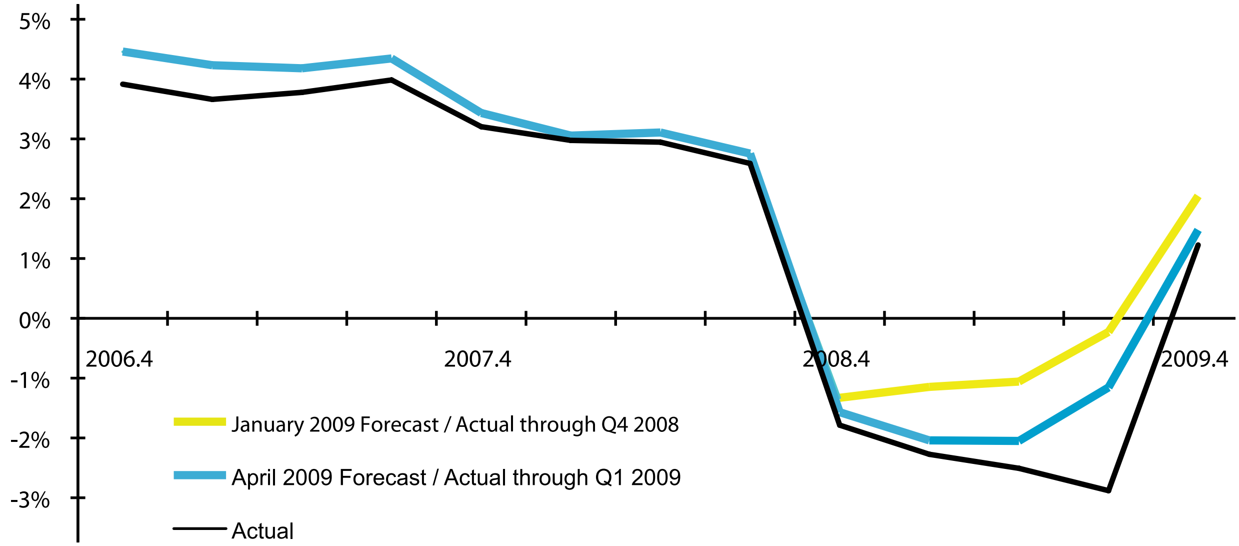

Figure 1. Nominal Retail Sales Excluding Auto & Fuel Channels (quarterly % change year-to-year, not seasonally adjusted)
Note that the pre-2009 gap in the history of the data series is a result of downward data revisions by the government since the initial forecasts.
Source: US Department of Commerce, Kantar Retail

In the middle of this uncertainty, Kantar Retail issued a forecast that proved correct in predicting that retail sales growth would return in the fourth quarter of 2009—as well as predicting the broad pattern that clients should expect. Exact numbers were off, but the forecast clarified that this wasn't the most important point. In the words written at the time:

"What's most important about this forecast is the pattern, not the absolute numbers. The declines may turn out to be more or less, but either way what should be expected is a pattern of weakness that finds a bottom in the first three quarters of the year. And then, if certain factors fall into place, the first signs that things are getting better should emerge by the end of the year."

Perhaps just as notable, the forecast identified two of the "certain factors" that indeed helped confirm over the year that the expected pattern was emerging: 1) the consumer expectations component of the consumer confidence index and 2) initial unemployment claims.

The Forecast Against Actual Sales Performance

The most accurate part of the forecast—and perhaps most contentious given the negative trends at the time—was the projection that year-to-year nominal growth would re-emerge in the fourth quarter of 2009 (Figure 1). Getting the intervening quarters right proved more difficult for a number of reasons worth revisiting: government data revisions, the impact of two successive years of government economic stimulus, and the degree of downward price pressure. In assessing these issues, it becomes clearer that the forecasts were most accurate in inflation-adjusted or volume terms.

Fourth Quarter 2009

In the end, the year-to-year growth that re-emerged in the fourth quarter of 2009 turned out to be 1.2%

for retail sales excluding the auto and fuel channels. The initial forecast in January 2009 had pegged that growth at 2.0%. A forecast update in April of 2009 (after the first quarter data was in) was much closer to the mark at 1.5% growth. Clearly, having another quarter of data—with some, but not all, of the eventual government revisions—helped better gauge the bottom and recovery pattern that would emerge.

Government Revisions

A half percentage point of the difference between the January 2009 forecast and the 2009 actuals is a result of government data revisions. The government originally reported a fourth quarter 2008 decline of -1.3% for retail sales excluding the auto and fuel channels, which was key to determining the starting point for the January 2009 forecast. Months later, the fourth quarter 2008 decline was revised downward to -1.8%. That downward revision of 0.5 percentage points was the bulk of the difference between the initial forecast and the actual for the fourth quarter of 2009.

Effects of Economic Stimulus

The bigger discrepancy between forecast and actual for the second and third quarters of 2009 partly reflect the difficulty of accounting for two rounds of government economic stimulus (the 2009 round under President Obama and the 2008 round under President Bush). In the end, the 2009 economic stimulus provided no apparent benefit to retail sales in the expected second and third quarter time frame. Instead, there was a negative impact from the 2008 economic stimulus. With difficult comparisons to prior-year periods boosted by economic stimulus and without the benefit of new stimulus, growth in the second and third quarters of 2009 sagged.

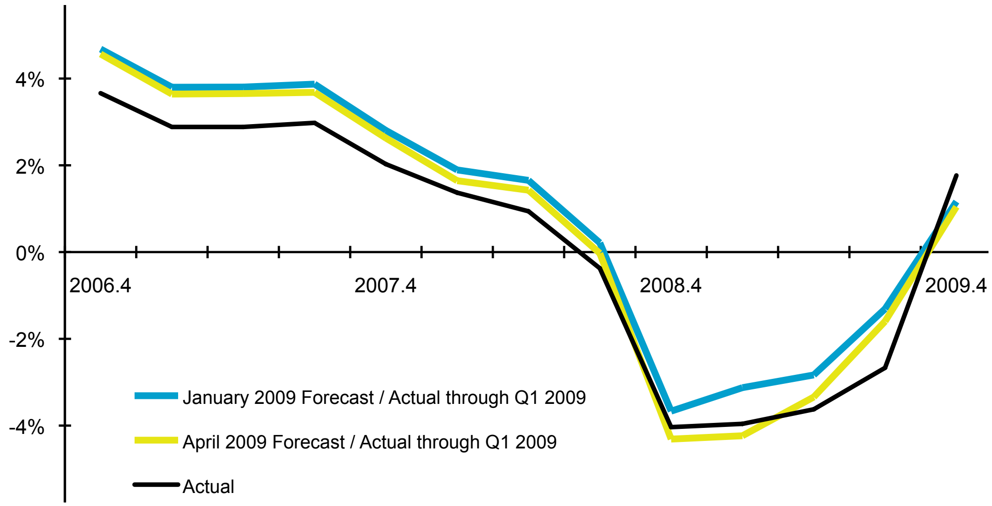

Figure 2. Inflation-Adjusted Retail Sales Excluding Auto & Fuel Channels (quarterly % change year-to-year, not seasonally adjusted)

Note that the pre-2009 gap in the history of the data series is a result of downward data revisions by the government since the initial forecasts.

Source: US Department of Commerce, Kantar Retail

Inflation-Adjusted Forecasts

The 2009 forecasts turned out to be closest to the mark in inflation-adjusted or volume terms (Figure 2). At an annual level, the January 2009 forecast was half a percentage point high, and the April 2009 update was almost exactly on target in inflation-adjusted terms. (The update forecasted a 2.0% decline in inflation-adjusted sales, and the actual was a 2.1%

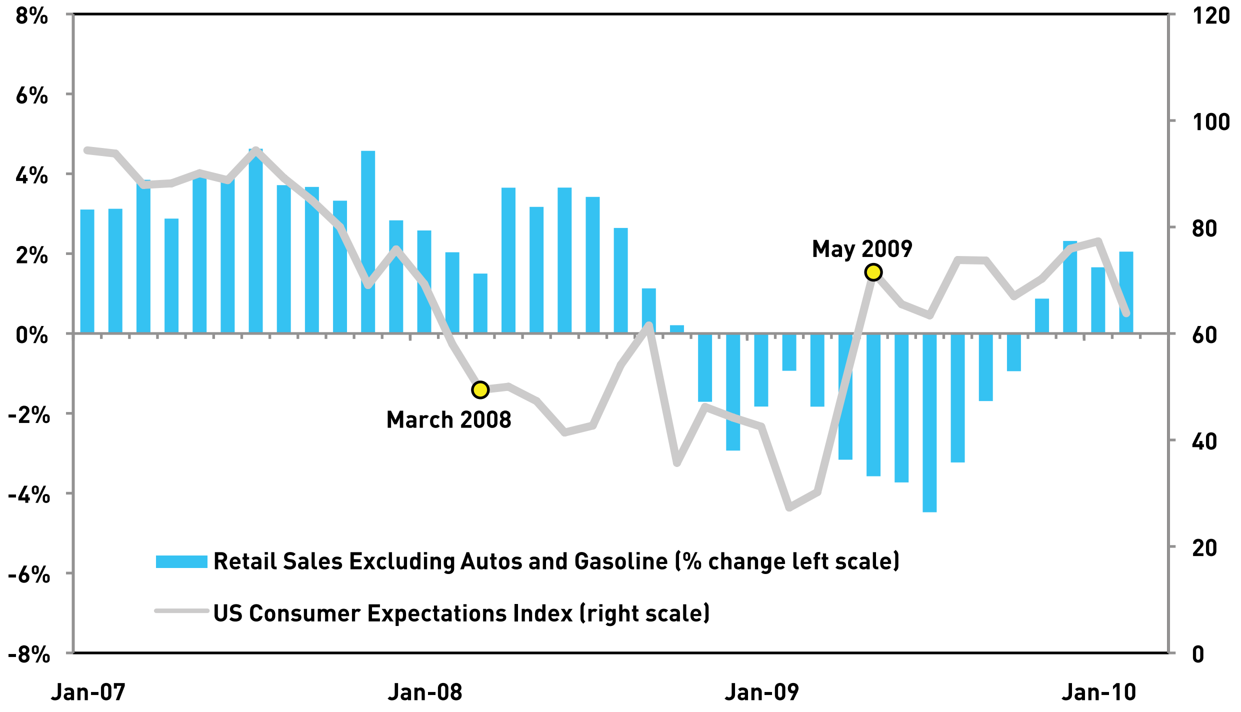

Figure 3. Consumer Expectations & Retail Sales Excluding Autos & Fuel / Source: Conference Board, US Department of Commerce, Kantar Retail

decline.) What this means is that most of the forecast error was a result of price-cutting that proved more severe than forecasted. The impact of price deflation on nominal sales growth was most severe between the second and third quarters, when there was a shift from 1.2% inflation in the second quarter to -0.2% deflation in the third quarter for the combined channels. Therefore, stepped-up price-cutting also explains why nominal sales growth sagged in the second and third quarters.

Consumer Expectations as Check on Forecast

The analysis that accompanied the January 2009 forecast argued that it was important to look beyond the top-line consumer confidence measure to understand why spending was declining so precipitously and to understand when it would begin to bounce back. In particular, the analysis focused on the "consumer expectations" component of the confidence index, which has proved to be a better leading indicator of turning points in retail sales than the overall index (Figure 3).

The consumer expectations index tumbled toward exceptionally low levels at least nine months prior to when retail sales began to post top-line declines. Conversely, the consumer expectations index began its modest bounce-back some seven months before retail sales began to grow again. This bounce-back in consumer expectations became most pronounced in May

2009, which provided some post-forecast confirmation that the expected pattern was occurring and that positive growth would re-emerge in the coming months.

Jobless Claims as Check on Forecast

Also providing confirmation that the expected pattern was emerging over 2009 was the trend in initial unemployment claims, which the January 2009 analysis identified as another leading indicator of a year-end bounce-back (Figure 4).

From their peak in March 2009, initial unemployment claims began a steady decline that foreshadowed the return of GDP growth in the third quarter of 2009. This is the pattern that has been evident in previous recessions, where a let-up in unemployment claims from their peak is followed by GDP growth within one or two quarters.

Final Thoughts

An important dimension of the Kantar Retail forecasts of early 2009 proved to be the supporting analysis. Identifying and relying on key leading indicators such as consumer expectations and unemployment claims—as well as leveraging shopper insights from Kantar Retail's monthly ShopperScape™ survey—verified that the forecast path was on track. As sales growth sagged in the second and third quarters of 2009, this provided some confidence to stick close to the initial forecasts. As a result, no one came closer than Kantar Retail to forecasting the path to the modest recovery in retail sales that occurred by the end of 2009.

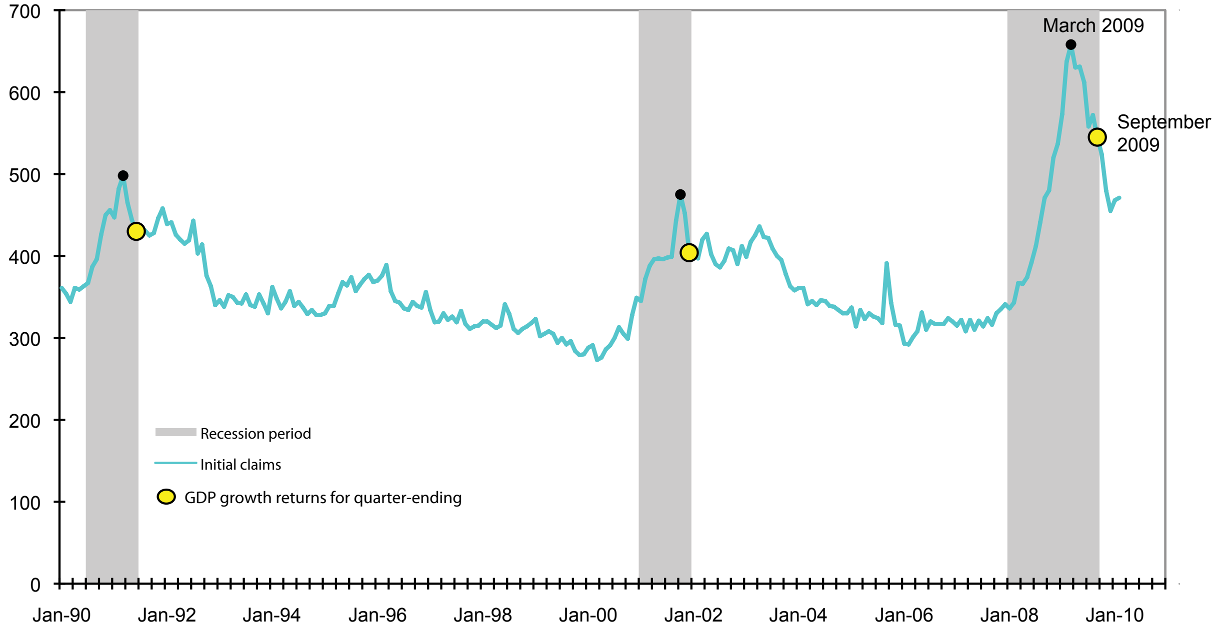

Figure 4. Unemployment Claims (seasonally adjusted, weekly average for month in thousands)
Source: US Department of Labor, Kantar Retail

The Threats to a U.S. Recovery

By Frank Badillo / Originally published on April 16, 2010

It hasn't taken long for the biggest threats to an economic and retail recovery to make their presence felt in 2010.

Kantar Retail has cautioned about the two-fold threats to a US recovery: 1) unexpected shocks that trigger another round of fear in the global markets and 2) the unwinding of the Fed's intervention in the financial markets. Both threats have gained momentum in recent months.

Greece and, to a lesser extent, China have been the source of the unexpected shocks. Financial markets are worried whether the debt woes of Greece will ripple across the countries that use the euro. Also, concerns have grown that China's moves to tighten credit and dampen inflation pressures will extinguish a global recovery led by emerging markets.

Meanwhile, concerns have also mounted as the Fed has begun to explain and carry out its plan for reversing its monetary expansion. A key milestone was crossed without major incident on March 31 when the Fed ended its purchases of mortgage-backed securities. Still, some concern and risk remain: If private buyers don't fill the void going forward, then long-term interest rates will rise and new mortgages will be tougher to come by.

These threats likely represent the first of a number of hurdles to an economic and retail recovery in 2010. However, the threats should be surmountable and the recovery should remain on track. The right trends continue to emerge in business investment and the job market, among other drivers of the recovery. In addition, the government's new jobs stimulus package as well as the lagging effects of last year's economic stimulus should ensure that the recovery is not derailed in the coming months.

Following are some further insights into the outlook and economic events of recent months.

Greece and Deficit Worries

In the longer term, the predicament faced by Greece and the eurozone countries will have more positive than negative repercussions for the United States. The recognition that the euro bloc is vulnerable to the woes of its weakest members—and needs to be ready to bail them out—ultimately makes the euro somewhat less attractive to investors relative to other currencies, including the US dollar. Any factor that helps boost the dollar ultimately helps dampen inflation in the United States (by making foreign goods more affordable). These disinflationary currency effects are important, as the US dollar otherwise faces downward pressure in the months and years ahead in the wake of the Fed's monetary expansion.

In the short term, however, the concerns about Greece's burgeoning budget deficit also draw attention to the growing deficits in the United States (as well as other countries). As long as the US deficits continue to worsen and worries grow about the government's ability to finance them, pressure on interest rates will rise in the near term. If severe, increasing interest rates could threaten the emerging recovery.

While concern about the recent deterioration in the US deficit is warranted, there's reason to believe the problem—and the interest rate side effects—will abate as the economy improves (Figure 1). The US

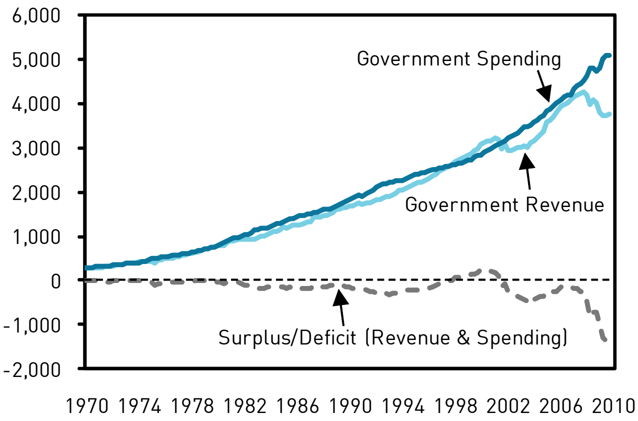

Figure 1. Government Revenue, Spending, and Surplus or Deficit (billions of dollars, seasonally adjusted at annual rates)

Source: US Bureau of Economic Analysis, Kantar Retail deficit has worsened of late primarily because the decline in jobs—and payroll tax cuts included in the economic stimulus—have resulted in a sharp decline in tax revenue since the end of 2007. As revenues bounce back with employment, the deficit will begin to narrow thus causing worries to recede. To remain dormant, however, the revenue improvement must be matched by a government commitment to curb the deficit spending. The stepped-up spending was sound policy to help pull the economy out of recession but becomes bad policy if sustained. While it's hard to count on Congress to reduce spending, the latest anti-deficit rhetoric and upcoming mid-term elections should move spending in the right direction and also ease the interest rate worries in the longer term.

The China Wildcard

China remains one of the biggest wildcards in the global economic recovery. That point was reinforced by the early-year jitters generated by China's move to limit lending in an effort to curb inflation pressures. To be sure, it would be good for the global economy if China were to successfully moderate its robust growth. That growth paused only briefly in the wake of the global financial crisis before surging in response to China's economic stimulus and renewed international investment in China. Among other things, tempered demand for fuel and other commodities by China would ease potential inflation pressures, as demand slowly recovers elsewhere in the world.

It's another story if China fumbles its handling of its economy. If it tightens too much, declining demand from China could push other countries back into recession. Tightening too little or too late perhaps would expose speculative bubbles in real estate or other markets that burst, thus creating a new shock

As long as the US deficits continue to worsen and worries grow about the government's ability to finance them, pressure on interest rates will rise in the near term.

to global financial markets. It's unclear just how high the China risk is. What is clear is that China has often been able to avoid problems because it is able to control the economy and society in ways that other governments cannot.

The Bernanke Factor

The monetary tightening predicament remains greatest, however, for Ben Bernanke and the Federal Reserve. Their moves in the first months of the year were the first in a series that are likely to roil markets and raise uncertainty through the end of the year, if not longer. In February, the Fed raised a bank lending rate (the discount rate, not the more important Fed Funds rate). That occurred about a week after the Fed laid out its broad plan for reversing its monetary expansion and a day after the Fed released minutes from its January meeting that specifically cited the discount rate as the first step in its plan.

The succession of events was enough to send ripples through asset markets. Get used to it. Business and consumer confidence will be subject to ups and downs, as the markets try to anticipate the Fed's every move over the course of the year. Of particular interest is the timing of an increase in the Fed Funds rate, which stands at 0.25%. The increase probably won't happen until the second half of the year, after sustained job growth has returned.

In the meantime, the Fed has survived its first steps without major consequences, including its decision to end its purchases of mortgage-backed securities on March 31. The coming weeks and months will prove critical, however, to determining whether the Fed's plan ultimately will be successful—as Kantar Retail assumes in its baseline retail forecasts—or whether the Fed stumbles and either sends the economy back into recession by tightening too quickly or causes a spike in inflation (and a drop in the dollar) by tightening too slowly.

Investment Leading Bounce-Back in Jobs

In reversing its monetary expansion, the Fed is responding to growing signs of recovery (with fourth quarter investment growth among the recent signs). Business investment grew at a double-digit annualized rate in the fourth quarter from the third quarter (Figure 2). Investment was boosted, in part, by business tax provisions from the economic stimulus package. From here, it's likely that investment growth will be driven primarily by the profits reported by an increasing number of firms in their latest quarter. Investment growth will also be sustained by Congress's extension of the investment deductions from the stimulus package that had expired on December 31 (although a provision allowing accelerated depreciation of investment property was not extended into 2010). Further sustaining investment growth should be the mounting evidence of rebounding consumer demand in the face of low, if not declining, inventories.

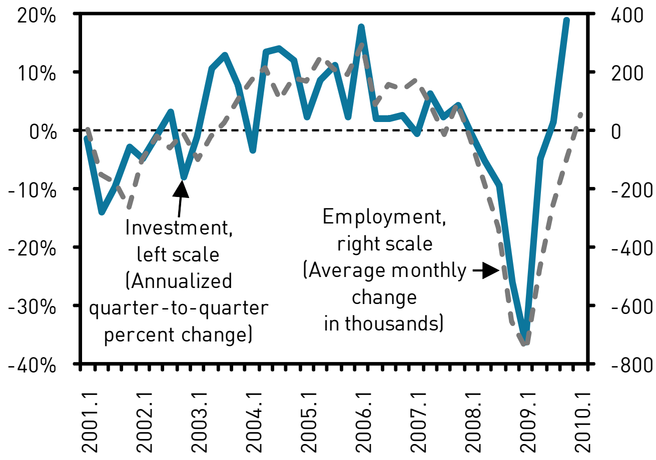

Figure 2. Business Investment and Employment

Source: Bureau of Economic Analysis, Bureau of Labor Statistics

As investment growth is sustained, employment growth typically follows, and March may prove to be the tipping point toward sustained job growth. With the 162,000 jobs added in March, the first quarter ended with clear job growth. If the job turnaround is sustained in the coming months, then this should generate the income growth that helps lift second-half growth in consumer spending and retail sales.

Lagging Let-Up in Unemployment

While job growth returned in March, the unemployment rate has not shown ongoing improvement. It held steady for the first three months of the year and remained only slightly below the peak of 10.1% reached in October (Figure 3). The jobless rate reflects the persisting drag on the consumer economy that is keeping the bounce-back in household spend-

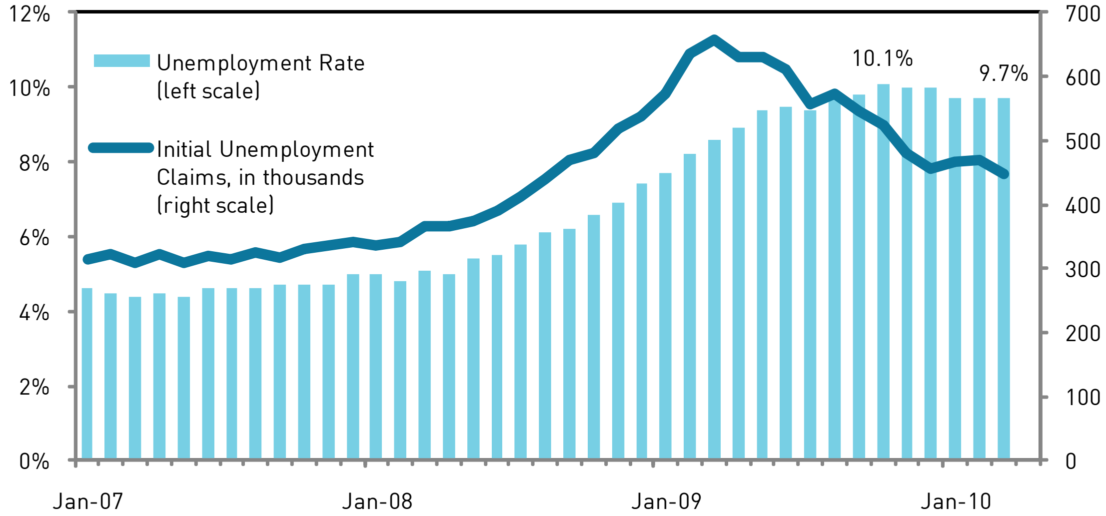

Figure 3. Unemployment Rate & Unemployment Claims

Source: US Bureau of Labor Statistics

ing modest and retail sales growth below average. At the same time, it's important to recognize that the unemployment rate is a lagging indicator. It's usually one of the last job market measures to turn around. The better leading indicator is unemployment claims. That trend is signaling—based on past patterns—that the unemployment rate will also be showing improvement in the months ahead.

Consumer Confidence Holds Steady

It will probably take evidence of both subsiding unemployment and sustained job growth for consumer confidence to take the next step in its recovery. Consumer confidence through March remained in the narrow band in which it has been since May 2009, when it was led higher by a step up in the Consumer Expectations component of the index (Figure 4). That improvement in consumer expectations roughly coincides with the fall-off in new unemployment claim filings over the

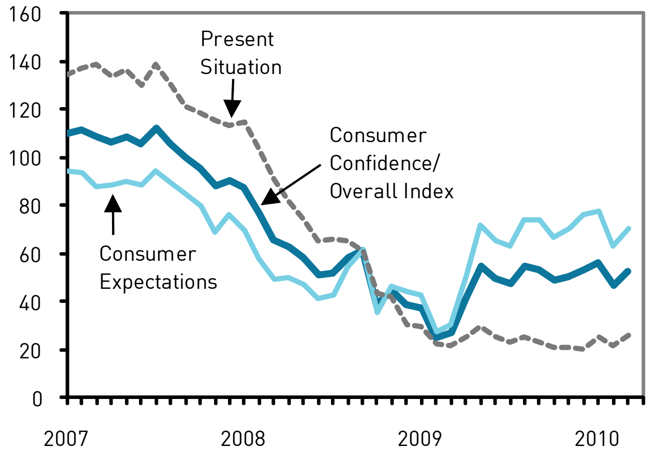

Figure 4. US Consumer Confidence Index (seasonally adjusted, 1985 =100)

Source: Conference Board

past year. While the Present Situation component of the index remains near its lows, the March data may provide a very faint sign of improvement. March's Present Situation measure edged higher for the second time in three months, reaching its highest reading since last May.

Jobs Bill Boost

The jobs trend and consumer confidence should be kept on an improving track by the USD 18 billion jobs bill passed by Congress in mid-March. The initiative gives companies two incentives to hire and retain unemployed workers: the companies do not have to pay Social Security taxes for the remainder of 2010 for those workers, and the companies get a USD 1,000 tax credit for each worker that remains on the payroll for at least one year. The jobs bill should end up reinforcing job growth that should be taking root in the months ahead, given recent trends.

Lagging Stimulus Effects

The jobs bill is essentially a second government economic stimulus package, albeit a much more modest one. This new stimulus follows a 2009 stimulus package that is delivering a lagging boost to the economy in 2010. According to recent estimates, only one-third of the USD 787 billion stimulus from 2009 has been paid out. As a result, the emerging economic recovery should be sustained to some extent by initiatives from last year's stimulus, including another year of payroll tax cuts, infrastructure projects that turned out not to be "shovel ready," and remaining entitlement spending. While the stimulus efforts should ultimately ensure that the economy recovers, there is also a risk that a second package could generate stronger-than-expected growth by the end of the year. That, in turn, could make the Fed's monetary tightening plan even tougher to implement beyond 2010.

Interest Rates and the Housing Market

The Fed's move to stop buying mortgage-backed securities did not result in a feared surge in long-term interest rates. Nevertheless, the uptick in rates by tenths of a percentage point at the start of April pushed the 10-year Treasury bond rate to pre-financial crisis levels near 4%. While these levels remain low by recent history, they still generate some foreboding that mortgage rates will be headed higher

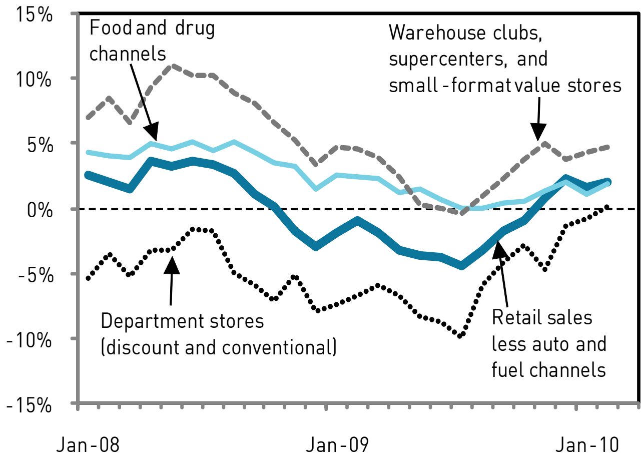

Figure 5. Retail Sales Measures: Food, Drug, and Mass Channels (percent change year-to-year, seasonally adjusted)

Note: Food and drug channels include supermarkets, drugstores, and foodservice (i.e., restaurants).

Source: US Department of Commerce

at some point. The good news at the moment is that there is no upward pressure on interest rates from inflation, which remains subdued based on the latest consumer price data excluding food and fuel.

Over the next year, however, the threat of inflation ultimately will lead interest rates higher. This will create a challenge for a recovery in the housing and home goods markets in 2010 and into 2011. So far, existing home sales have rebounded primarily because of federal mortgage credits. Building starts and sales of new homes have shown only meager signs of recovery. Therefore, the housing market will be hard pressed to lay the foundation of a solid recovery in the face of rising interest rates and the expiration of the mortgage credit in April. All this reaffirms that home goods will continue to lag in the retail sales recovery that will be led by the other retail segments.

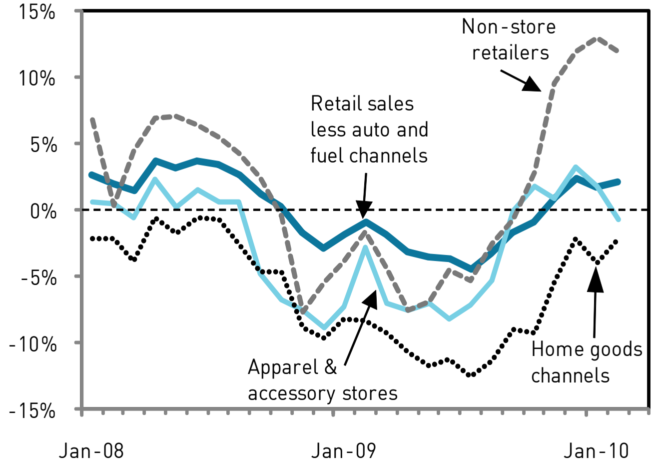

Figure 6. Retail Sales Measures: Apparel, Home Goods, and Non-store Channels (percent change year-to-year, seasonally adjusted)

Source: US Department of Commerce

Retail Sales Trends

The stimulus efforts should help sustain a rebound in retail sales growth that continues to be led by non-store retailers as well as value-oriented retailers. The combined warehouse club, supercenter, and small-format value store channel has been growing at about a 4% rate or better since October 2009, reaching 4.7% growth in February (Figure 5). That compares to the about 2% pace for retail sales excluding the auto and fuel channels. Lagging slightly with growth between 1% and 2% are the combined food and drug channels. Lagging more significantly with flat or declining sales are the combined discount and conventional department store channels, although the persisting declines are steepest among the conventional department stores.

With double-digit growth beginning in December, the non-store channel (which includes online and catalog retailers) is outpacing all of retailing (Figure 6). After a strong December, apparel and accessory stores have seen growth tail off, slumping to slight declines in February—though company-reported same-store sales have held up better. The combined home goods channels have continued to lag all retail channels, posting declines ranging from -2% to -4% through February 2010. The home goods channels should be the last to see positive growth return over the course of 2010, depending on improvement in the housing and mortgage markets.

Key Indicators Suggest Fragile Recovery for Europe

By Himanshu Pal / Originally published on February 26, 2010

Three years back, not many had expected that the mortgage crisis that started in a few US states would one day spiral into one of the worst global economic crises since the days of the Great Depression in the 1940s. What made the economic events of 2008 historic was the global (Americas, Europe, Asia Pacific) and pan-industry (financial services, manufacturing, retail) impact of this crisis.

Europe had been one of the worst affected by the economic crisis—something which we at Kantar Retail have reflected on in our previous articles and discussions. In our last article on European Economic Indicators (published 2 November 2009), we considered whether "the worst is over." From a 20,000-feet review, one would believe that the worst is in fact over, especially considering the economic data released by European statistical organisations that suggest that all major economies are out of recession. This article explains that, although the European economy has recovered, the recovery is fragile and the optimism could be short lived.

Europe Trudges Its Way Out of Recession ... Barely

Many people would have sighed with relief as the UK (Europe's second biggest economy) trudged its way out of recession with 0.1% quarter-on-quarter growth during Q4 2009. However, the GDP growth for the Euro Area (EA) and the European Union (EU) grounded to a near halt with just 0.1% growth versus Q3 2009 (Figure 1), due to the stagnation in Germany (Europe's biggest economy) and contraction across markets such as Greece, Spain, the Czech Republic, Italy, Cyprus, Latvia, Hungary, and Romania.

News regarding the state of the Greek economy and its impact on the European economy has been extensively spoken about—from massive public spending and spiralling public debt, fraudulent accounting and reporting practices, to ever-increasing fiscal deficit. Further, there are growing fears regarding the economic health of Spain (Europe's fifth biggest economy), Portugal, and the Baltic countries (Latvia, Lithuania, and Estonia).

While Portugal struggles to contain rising unemployment, Spain is struggling to combat rising public debt, fiscal deficit (that now stands at 11.4%), unemployment (19%), and collapsed property market and consumption expenditure (heavily reliant on credit) due to the financial downturn. The situation in the Baltic countries (Latvia, Lithuania, and Estonia) is even more distressing with year-on-year GDP decline in the range of 9% to 18%—worst among all EU member states (Figure 2). The decline follows the withdrawal of foreign investment, reduced exports, and deep cuts in public spending—with the latter aimed at lowering the budget deficit to retain the rescue aid from the International Monetary Fund (IMF), the EU, and other lenders.

With talks of a multi-billion EU bail-out plan for Greece—and the possibility of similar future action in the offing for Spain, Portugal, and the Baltic economies—the key question is: Who would source this funding/bail-out package? According to recent news, the package is likely to be funded partly by the European Central Bank and the IMF, along with possible loans and guarantees by Germany and France. The move is likely to further exert pressure on

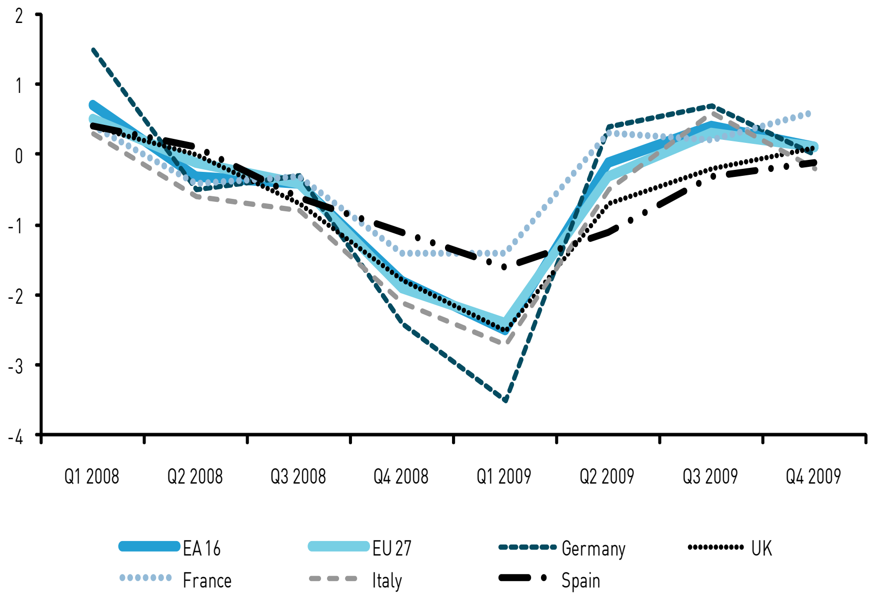

Figure 1. GDP Volume Growth (% change versus previous quarter)
Source: Eurostat

the two key European economies that are already combating rising fiscal deficits on the back of huge domestic stimulus packages. Further, if Greece defaults on the loans extended to it by various banks and financial institutions, it could spark off a "Domino Effect" across Europe with other fragile economies crashing down as well. Another critical piece is the planned austerity drives by governments in Greece, Spain, and Portugal as a result of the mounting pressure from the European Central Bank and other member states to cut down public spending and reduce fiscal deficit. This could very much skittle out the credit availability as well as depress consumption and investment activity in these countries, thereby undermining the overall EU recovery.

It's important to recognise the intrinsic relationship between GDP growth and the consumer and business variables that impact retail sales. Indeed, it's a vicious cycle whereby an improvement in economic situation prompts consumers to spend more (with reduced propensity to save), which in turn means increased retail sales that prompt retailers to invest and expand more thus creating more employment. More employment means increased domestic output (GDP) and more consumer confidence propelling another wave of increased spending—and it goes on and on. Unfortunately, it works the other way around as well: If the economic situation worsens, it triggers off a spiralling downward trend. We at Kantar Retail believe it's important to look at each market separately, as it's not only difficult to paint a uniform picture for the whole of Europe, but doing may also present a slightly misleading picture.

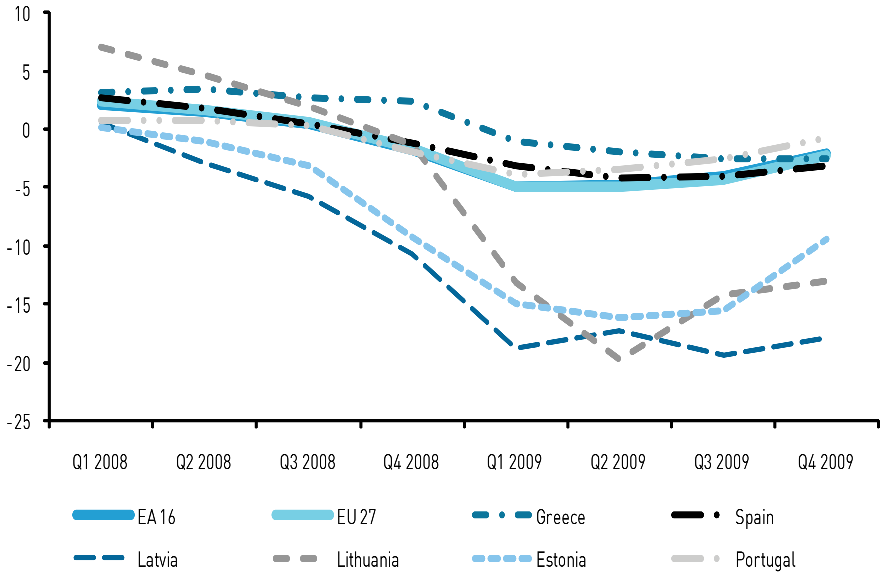

Figure 2. GDP Volume Growth (% change versus same quarter in the previous year)
Source: Eurostat

Rising Unemployment

Unemployment rates increased in both the EA and the EU during Q4 2009. While the EA experienced an unemployment rate of 10% in December 2009 versus 9.8% in September, the EU witnessed the rate increase to 9.6% in December from 9.3% in September 2009. Notable is that the current unemployment rates are the highest both in the EA since August 1998 and in the EU since January 2000. Eurostat estimates that roughly 23.012 million people are unemployed in the EU, with the number of unemployed increasing to 163,000 in December 2009 alone.

Back to Inflationary Conditions

Both the EA and the EU witnessed a return to inflation during Q4 2009, after a quarter of deflation in Q3 2009: All major economies registered an increase in prices (Figure 3). The EA experienced a 0.9% increase in prices during December 2009 (average of 0.43% during Q4 2009), and the EU experienced an inflation rate of 1.4% in December 2009 (average of 0.96% during Q4 2009). On the other end, Ireland, Estonia, and Latvia continued to experience deflation with prices declining 2.7%, 2%, and 1.3%, respectively, during December 2009. We expect deflationary conditions to continue in these economies at least during Q1 2010.

Recovery Boosts Consumer and Retailer Confidence

Interestingly, the modest recovery in Europe has been greeted with cheer among consumers and retailers alike, with both consumer confidence and retail confidence index in Q4 2009 improving versus Q3, Q2, and Q1. Although the consumer confidence index in the EU continues to be in the negative, it improved to -14.3 in December, as compared to -16.7 in September and -31.8 in February. Similarly, the retail confidence index in the EU improved to -6.4 in December, versus -10.9 in September and -24.5 in February. Most of the cheer comes from consumers and businesses that continued to feel more confident about the economy after a torrid Q4 2008 and Q1 2009: They started spending relatively more as compared to last year. The outlook for Q1 2010 looks promising with the consumer and retail confidence index for the EU further improving to -13.1 and -3.3, respectively, in January 2010.

As highlighted earlier, consumer and retailer confidence has an intrinsic relationship with retail sales. Even more important to understand is the fragility of consumer and retail confidence in the current economic scenario. An apt example is Greece in Q4 2009: the economic scenario worsened; the already weak consumer confidence plummeted; and, consequently, retail sales fell.

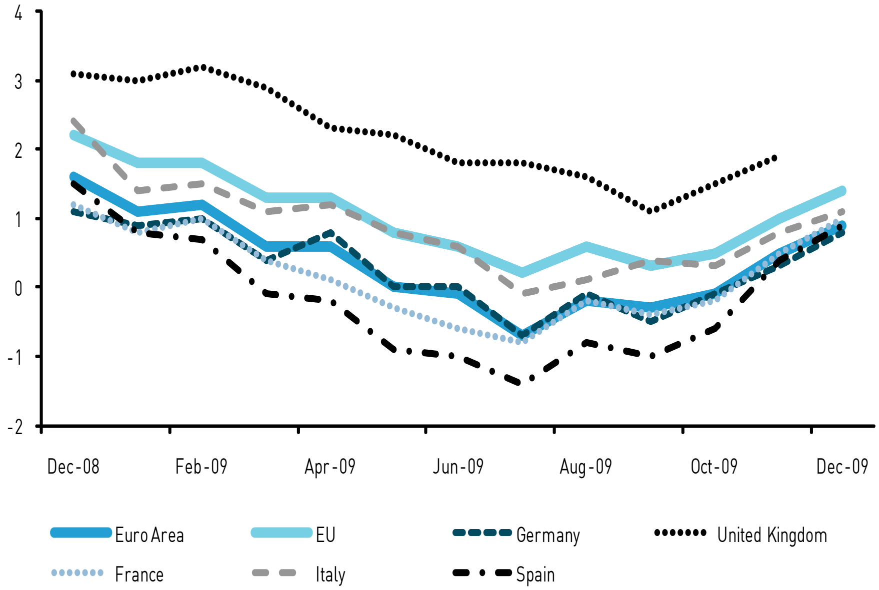

Figure 3. Inflation

Source: Eurostat

What About Retail?

Consumers and retailers are feeling relatively better and more confident about the economic prospects as compared to Q4 2008 and Q1 2009. This confidence has started to percolate its way through to the retail sales volumes, which continue to improve with each quarter.

Although retail trade volume in the EU continued to decline with a roughly 0.9% year-on-year drop in Q4 2009, it fared better versus the year-on-year decline of 1.6%, 1.9%, and 2.7% in Q3, Q2, and Q1 2009, respectively (Figure 4). Greece, Slovenia, Slovakia, and the Baltic countries were the worst performers during Q4 2009, further emphasizing the negative impact of the prevailing economic crisis.

Recessionary conditions generally prompt consumers to be more frugal and iterate their buying behaviour through trading down, trading out, and deferring purchases of certain product categories, especially discretionary spending products, such as consumer electronics, furniture, etc. In contrast, the demand for certain necessity products, such as food remains relatively stable. This trend is clearly evident in the retail trade volume data for Europe and suggests a stronger year-on-year growth in food sales versus non-food categories. While the total retail sales declined 1.6% year-on-year in December 2009 (as compared to -2.8% and -2.1% in September and June 2009, respectively), the sales of food, drinks, and tobacco products improved 0.1% year-on-year in December 2009 (as compared to -1.9% and -1.6% in September and June 2009, respectively). As expected, non-food sales fared worse vis-à-vis both overall and food retail sales, with sales declining 2.2% year-on-year in December 2009 (compared to -3% and -1.5% in September and June 2009, respectively).

We believe that the food sales will continue to improve during Q1 2010, while non-food sales will continue to remain weak in Q1 2010 and recover in Q2 2010. The economic recession in Europe has also brought about a marked change in the way retailers approach consumers—with increased emphasis on aggressive pricing and value orientation, optimized merchandise mix with greater shelf space and promotion for private label range, direct marketing efforts, and interest-free financing schemes to capture a growing share of trips and expenditure in a declining market.

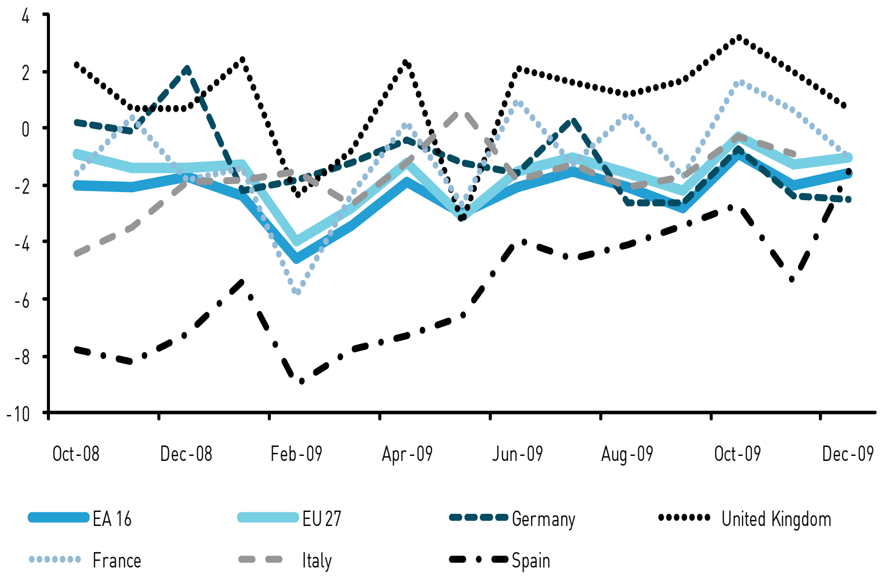

Figure 4. Retail Trade Volume (year-on-year)
Source: Eurostat

Kantar Retail Point of View

We believe that the recovery road ahead—at least for H1 2010—will be tough. Governments of member states must cautiously tread a fine line between public spending and managing fiscal deficit and public debt.

The European economy has undeniably recovered from the virtual bloodbath of Q4 2008 and Q1 2009, primarily due to the efforts of governments to infuse funds to bail out financial institutions and increase consumption spending. Mainly propelled by strong monetary and fiscal policies and recovering industry and trade, the performance—never mind the modest growth—of advanced economies, such as Germany, the UK, and France, makes such a recovery evident.

In spite of this, Kantar Retail suggests that the current economic situation is still fragile and recommends "cautious optimism." We believe that the recovery road ahead—at least for H1 2010—will be tough. Governments of member states must cautiously tread a fine line between public spending (to support the momentum of increased consumption and investment) and managing fiscal deficit and public debt. Two key factors—the ability of economies such as Greece, Spain, and Portugal to reign in their public debts and fiscal deficits and the efficient, continued monetary support to banks and financial institutions by governments of key economies such as Germany, the UK, and France—will influence the outcome of H1 2010.

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