Store-based Retailing – Food and Near-food

2

Abstract

Retailers have various ways of meeting customer needs through the organisation and design of their retail outlets. This chapter describes the different types of retail institutions that represent different types of retail strategies for selling goods and services in the food and near-food sector.

2.1 Types of Retail Institutions

From a managerial point of view, understanding the different types of **retail institutions** is important because they have a competitive impact on the retail business. Several types of retail institutions mirror retailer business operations. Thus, each type represents a specific retailing strategy.

Several systems of retail classification have been developed by government institutions to collect and analyse business data more effectively. One of the first classification systems was the **Standard Industrial Classification** (SIC) code, which was developed for the *US Census Bureau* in 1930 and uses special codes (sets of numbers) to identify types of retailers. This served as the basis for the further development of international classification systems such as the UN's **International Standard Industrial Classification of all Economic Activities** (ISIC), the NAICS (**North American Industrial Classification System**) or the NACE (**Nomenclature statistique des Activités économiques dans la Communauté Européenne**) in the European Union (see Fig. 2.1)

Under these classification schemes, retailers are assigned hierarchical codes based on the types of products and services they sell. However, retailers selling the same category

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G - Wholesale and retail trade; repair of motor vehicles and motorcycles G47 - Retail trade, except of motor vehicles and motorcycles	
G47.1 -	**Retail sale in non-specialised stores**
G47.1.1 -	Retail sale in non-specialised stores with food, beverages or tobacco predominating
G47.1.9 -	Other retail sale in non-specialised stores
G47.2 -	**Retail sale of food, beverages and tobacco in specialised stores**
G47.2.1 -	Retail sale of fruit and vegetables in specialised stores
G47.2.2 -	Retail sale of meat and meat products in specialised stores
G47.2.3 -	Retail sale of fish, crustaceans and molluscs in specialised stores
G47.2.4 -	Retail sale of bread, cakes, flour confectionery and sugar confectionery in specialised stores
G47.2.5 -	Retail sale of beverages in specialised stores
G47.2.6 -	Retail sale of tobacco products in specialised stores
G47.2.9 -	Other retail sale of food in specialised stores
G47.3 -	**Retail sale of automotive fuel in specialised stores**
G47.3.0 -	Retail sale of automotive fuel in specialised stores
G47.4 -	**Retail sale of information and communication equipment in specialised stores**
G47.4.1 -	Retail sale of computers, peripheral units and software in specialised stores
G47.4.2 -	Retail sale of telecommunications equipment in specialised stores
G47.4.3 -	Retail sale of audio and video equipment in specialised stores
G47.5 -	**Retail sale of other household equipment in specialised stores**
G47.5.1 -	Retail sale of textiles in specialised stores
G47.5.2 -	Retail sale of hardware, paints and glass in specialised stores
G47.5.3 -	Retail sale of carpets, rugs, wall and floor coverings in specialised stores
G47.5.4 -	Retail sale of electrical household appliances in specialised stores
G47.5.9 -	Retail sale of furniture, lighting equipment and other household articles in specialised stores
G47.6 -	**Retail sale of cultural and recreation goods in specialised stores**
G47.6.1 -	Retail sale of books in specialised stores
G47.6.2 -	Retail sale of newspapers and stationery in specialised stores
	G47.6.3 - Retail sale of music and video recordings in specialised stores
G47.6.4 -	Retail sale of sporting equipment in specialised stores
G47.6.5 -	Retail sale of games and toys in specialised stores
G47.7 -	**Retail sale of other goods in specialised stores**
G47.7.1 -	Retail sale of clothing in specialised stores
G47.7.2 -	Retail sale of footwear and leather goods in specialised stores
G47.7.3 -	Dispensing chemist in specialised stores
G47.7.4 -	Retail sale of medical and orthopaedic goods in specialised stores
G47.7.5 -	Retail sale of cosmetic and toilet articles in specialised stores
G47.7.6 -	Retail sale of flowers, plants, seeds, fertilisers, pet animals and pet food in specialised stores
G47.7.7 -	Retail sale of watches and jewellery in specialised stores
G47.7.8 -	Other retail sale of new goods in specialised stores
G47.7.9 -	Retail sale of second-hand goods in stores
G47.8 -	**Retail sale via stalls and markets**
G47.8.1 -	Retail sale via stalls and markets of food, beverages and tobacco products
G47.8.2 -	Retail sale via stalls and markets of textiles, clothing and footwear
G47.8.9 -	Retail sale via stalls and markets of other goods
G47.9 -	**Retail trade not in stores, stalls or markets**
G47.9.1 -	Retail sale via mail order houses or via Internet
G47.9.9 -	Other retail sale not in stores, stalls or markets

Fig. 2.1 NACE codes – examples. (Eurostat 2015)

of merchandise are not necessarily direct competitors. These classification schemes, therefore, are mainly used for data collection and statistical analysis to provide insight into the development of the various retail institutions at a national or international level. For retail managers, the more strategic aspects of the different types of retail institutions are crucial. Therefore, classifying retail institutions based on the characteristics of the strategies they employ to sell goods and services is important for **strategy development** and competitive analysis. These types of retail institutions are referred to as **retail formats**. Retail formats are specific configurations of retail marketing mix that are maintained consistently over time (e. g., type of store design and atmosphere, merchandise offered, services provided, pricing policy, type of location, approach to advertising and promotion, etc.).

2.2 Theories of Retail Evolution

2.2.1 Overview

There are a number of theories to explain the present structure of the retail industry and predict the future development of current and new retail formats. In this context, the **wheel of retailing** and the **retail lifecycle** are two particularly important theories.

2.2.2 The Wheel of Retailing

The **wheel of retailing** (McNair 1931) is a well-established framework for explaining developments in retail institutions. The theory suggests that retail institutions go through cycles during their development (see Fig. 2.2). The theory is that as low-end retailers upgrade their strategies to increase sales and profit margins, new forms of low-price (discount) retailers take their place in the market.

The **wheel of retailing** describes institutional changes that occur when new competitors enter the market. In its initial form, the wheel of retailing consists of a three stage cycle (McNair and May 1978; Brown 1988; Berman and Evans 2013, pp. 143–145):

- According to the wheel theory, retail innovators often appear as low-price operators. Thus, the cycle begins with retail institutions starting off with **low prices** and **low service levels**.
- The second phase is **trading up**. Retailers who wish to expand their business and attract more customers enhance the quantity and quality of merchandise they handle, provide more services and open outlets in more convenient locations. This leads to an increase in operating costs and prices and thus offers opportunities for new competitors to enter the market with low-price strategies.
- The third phase sees **increased competition** for services of all kinds and a convergence of retailers' marketing mixes as they mature. They become vulnerable to new competitors entering the market with low prices.

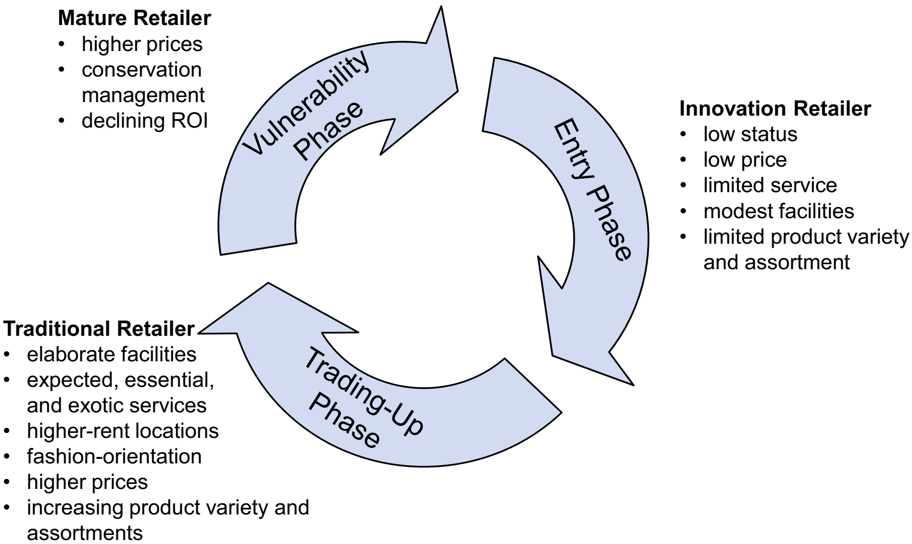


Fig. 2.2 The wheel of retailing

The wheel of retailing describes a circular retail format development process of alternating trading up and dissolution of retail formats due to a competitive environment, characterised by innovators entering the market as low-price competitors.

2.2.3 The Retail Lifecycle

The retail lifecycle is a succession of identifiable stages that a retail format goes through over time (Berman and Evans 2013, pp. 146–148):

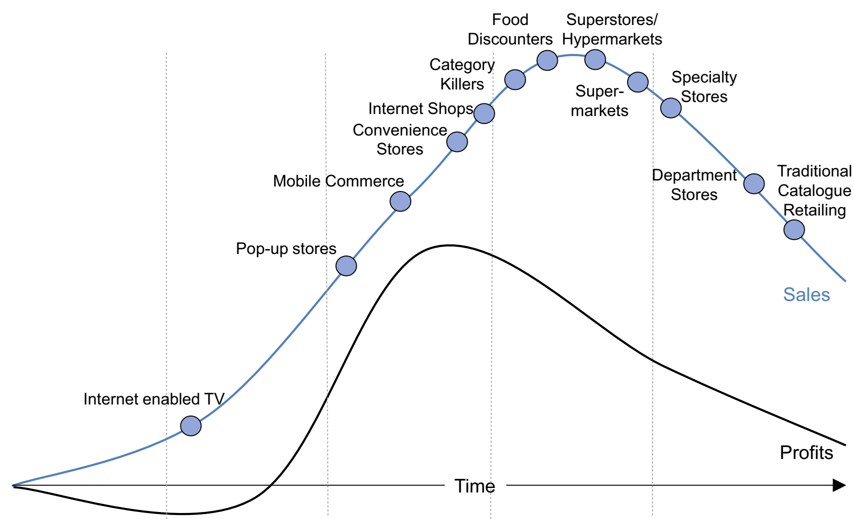
- In the **development stage**, the new format is introduced to the market. It is different from existing retail institutions' strategies, as at least one element of the marketing mix is altered in the new format.
- In the **introduction phase**, sales and profits are low, but growing. Costs and risks are high because long-term success is not assured at this stage.
- The **growth phase** is characterised by the rapid growth of both sales and profits. Existing companies expand their markets and new competitors employing the same retail format enter the market. Towards the end of this stage, growth acceleration begins to decline and cost pressures may emerge.
- The next stage is **maturity** of the retail format, brought on by market saturation, which in turn is caused by a high number of firms using this retail format and competition from new formats. Sales growth declines and profit margins may have to be

reduced to stimulate sales. Once maturity is reached, the main goal is to prevent the business from declining and to sustain profits for as long as possible.

- In the final stage, **decline**, sales volumes decline and prices and profitability shrink. Companies can try to avoid decline by **repositioning** their retail format, but many companies abandon the format altogether and introduce new formats to keep their customers or attract new ones.

Fig. 2.3 illustrates the characteristics of these five stages and indicates the stages which current retail formats have reached in Western or developed countries, including the United Kingdom, France, the United States or Germany.

In the context of the retail lifecycle, **store erosion** (Berger 1977) is defined as a reduction in a retail company's appeal and ability to attract customers over time because of changes in the company's internal and external conditions. In a **dynamic environment**, new retailing formats that meet new customer needs render existing retail formats obsolete. In order to avoid decline and survive, retail companies must adapt to changing marketplace conditions and **reposition** their retailing concepts.



	Development	Introduction	Growth	Maturity	Decline
Sales	low/growing		rapid acceleration	high, levelling off	dropping
Profitability	negative to break even		high yield	high/declining	low to break even
Positioning	concept innovation		special needs	broad market	niche
Competition	none		limited	extensive/ saturation	intensive/ consolidated

Fig. 2.3 The retail lifecycle. (Adapted from Berman and Evans 2013, p. 146; Zentes et al. 2005, p. 34)

2.3 Store Formats in Food and Near-food Retailing

2.3.1 Overview

Over the past few decades, food retailing has undergone substantial changes. **New competitors from general merchandise retailing** have entered the market by expanding their assortments and selling **food** and **near-food articles** (i. e., articles of daily use such as health and beauty aids, cosmetics and hygiene products). But, in most cases, traditional food retailers also carry merchandise outside their traditional lines of food and near-food items (i. e., general merchandise) and offer other kinds of services. These developments indicate that it is difficult to precisely allocate retail institutions to either food or general merchandise retail formats. This section will present the formats of superettes, conventional supermarkets, superstores, combination stores, hypermarkets and supercentres, convenience stores, food discounters, drugstores and warehouse clubs. Table 2.1 provides an overview of the characteristics of the most important retail formats.

Food retailing store density is relatively high in most countries.

Fig. 2.4 presents the density of retail stores of different sizes in European countries. While larger store formats are growing more relevant, stores below 1000 m^2 dominate in all country markets by store numbers. These play an important role in proximity retailing, among others.

2.3.2 Superettes

Superettes, **minimarkets** or **minimarts** are very small store formats (smaller than 400 m^2) that offer a limited assortment of food and related items of daily and short-term requirements. These formats have been under pressure for a while, even though these were once the traditional neighbourhood store format for food retailing. However, they remain important in some markets, such as the Asia-Pacific region.

Because of its long trend of dwindling market share, many retailers in Western markets have written off **superettes** and streamlined their store chains. However, thanks to the efforts of retail chains such as *EDEKA* or *REWE*, which have supermarkets but also operate superettes, this retail format is experiencing a resurgence. These retailers have changed the positioning of their small store formats by using trading-up strategies in their retail marketing mix. This strategy of positioning superettes as a form of neighbourhood-oriented proximity retailing – not to be mistaken with convenience stores – in **neighbourhood locations** or in cities, with modern in-store designs, revamped assortment strategies and usually lower prices, has made this store format relevant again.

Because one of the main problems with superettes in the past was store productivity, many retailers have also changed the **ownership structure**. In most cases, they now operate their superettes as franchise systems or voluntary chains to guarantee their profitability (see Chap. 7).

Table 2.1 Selected characteristics of store-based formats in food retailing. (Adapted from Berman and Evans 2013, p. 150; Levy et al. 2014, p. 42)

	Superettes	Conventional Supermarket	Superstore	Hypermarket	Convenience Store	Hard Discounter
Size (m^2)	100–399	400–1000	1000–5000	5000–30,000	200–400	500–1500
SKUs	20,000	20,000–30,000	30,000–40,000	40,000–150,000	1000–3000	700–1500
Merchandise	Small to medium breadth and depth of assortment; average quality; manufacturer and store brands	Extensive breadth and depth of assortment; average quality; manufacturer and store brands	Full assortment of supermarket items, plus health and beauty aids and general merchandise	Extensive breadth and depth of assortment; full selection of supermarket and drugstore items, and general merchandise	Medium breadth and low depth of assortment, average quality	Medium breadth and low depth, heavy use of store brands (up to 90 %)
Percentage Food	90 %	75–90 %	60–80 %	60–70 %	90 %	80–90 %
Prices	Average/competitive	Average/competitive	Competitive	Competitive	Average to above average/high	Very low
Atmosphere and Services	Average	Average/good	Average	Average	Average	Low
Location	City or neighbourhood	City or neighbourhood	Community shopping centre or isolated sites	Community shopping centre or isolated sites	Neighbourhood, city or highly frequented sites	Neighbourhood, traffic-oriented
Promotion	Little to moderate	Use of newspapers, flyers, coupons	Heavy use of newspapers, flyers, coupons	Heavy use of newspapers, flyers, coupons	Little to moderate	Heavy use of newspapers and flyers

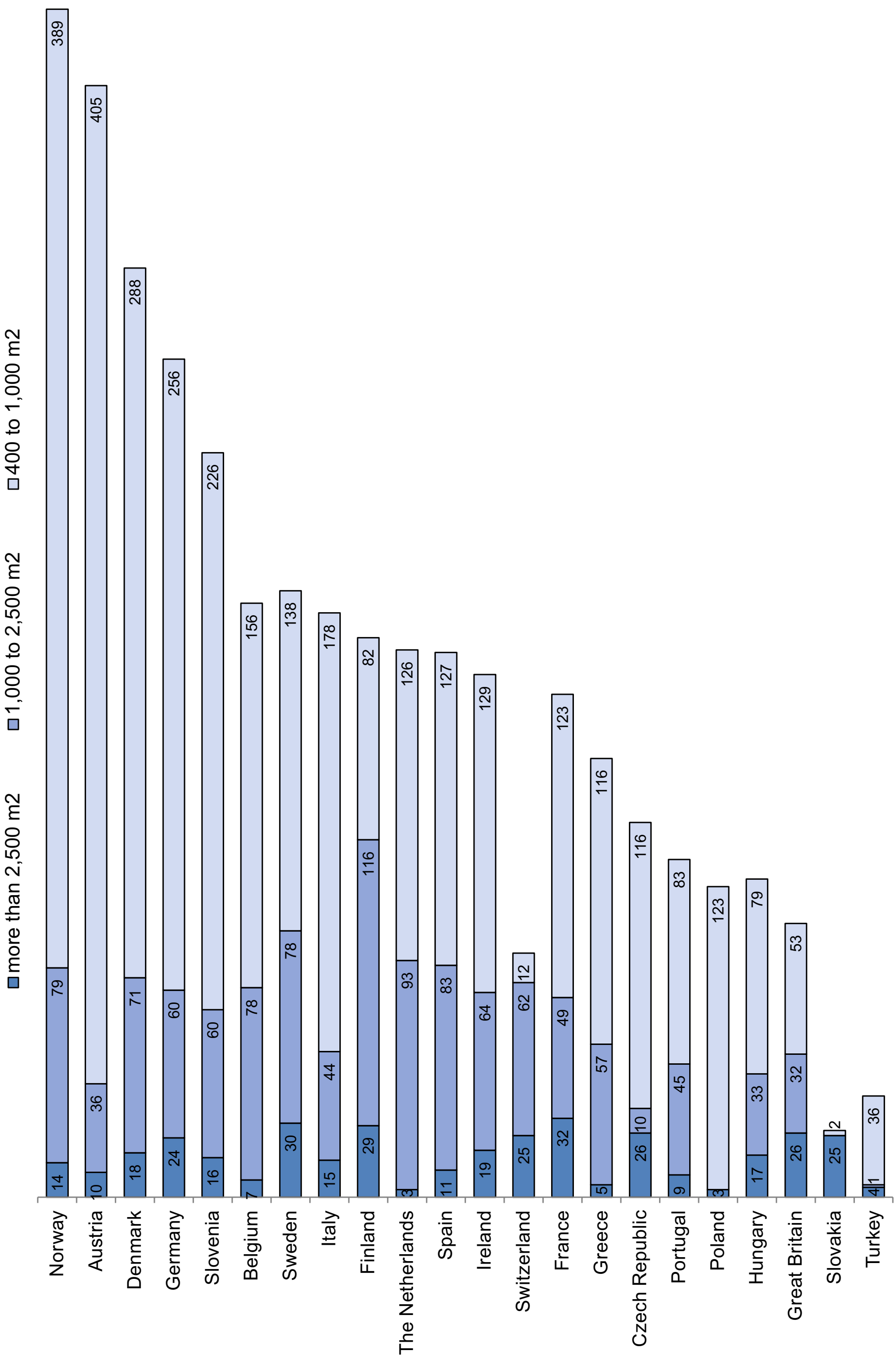


Fig. 2.4 Number of stores per 1 million inhabitants in Europe in 2013. (Nielsen 2014)

2.3.3 Conventional Supermarkets

Conventional supermarkets are self-service stores that carry a wide range of **food items** (mainly groceries, meat and produce), including fresh food (e. g., fruits and vegetables) and related items. The share of general merchandise offered in this retail format is limited to between 10 and 25 %, including, for example, health and beauty aids and products (Berman and Evans 2013, p. 152).

Supermarkets are usually located in city or neighbourhood locations with sizes between approximately 400 and 1000 m². Important players that use this format include *Sainsbury's*, *EDEKA*, *REWE*, *Ahold* or *Intermarché* in Europe and *Kroger* and *Albertson's* in the USA.

This has traditionally been the main retail format for grocery shopping and has accounted for the majority of sales in food retailing for several decades. However, it faces **intense competition** from new formats offering more convenient shopping facilities, more product lines and more varied assortments or lower prices as a result of lower operating costs (Levy et al. 2014, pp. 42–43).

Companies such as *REWE* or *EDEKA* have successfully **repositioned** their supermarkets and thus improved their competitive positions by emphasising freshness and high quality assortments, introducing medium- to high-level store brands and improving store atmosphere in order to provide a better **in-store shopping experience**.

2.3.4 Superstores

Food-based **superstores** are larger and more diversified than conventional supermarkets. Their size varies between 1000 and 5000 m², with expanded services such as a deli, bakery, seafood counter and general merchandise sections (Berman and Evans 2013, pp. 152–153). They are **"true" food stores** with a share of general merchandise ranging from approximately 20 to 40 %, but also offer consumers expanded **one-stop shopping** possibilities.

Combination stores, as they are sometimes known, are a similar store concept. They tend to be larger than superstores (up to 9500 m²) and offer a higher share of general merchandise (from 25 to 50 % of sales). These stores combine food and general merchandise, thus offering a higher level of one-stop shopping for consumers than superstores (Berman and Evans 2013, p. 153).

This combination of food and general merchandise in superstores and combination stores yields operating efficiencies and cost savings, mainly because non-food items tend to have higher margins. Superstores and combination stores usually follow either a **high-low pricing strategy** (HiLo), which means that they are very promotion-oriented (e. g., intensive advertising or distribution of flyers), or an **everyday low-price strategy** (EDLP) using few promotions and selling their merchandise at fixed low prices (see Chap. 13). Superstores and combination stores can be located in city or neighbourhood locations as well as in isolated sites or in shopping centres and oriented towards customers travelling by car. Important players that operate superstores or combination stores include *Intermarché*, *REWE, Tesco* or *Albertson's*.

2.3.5 Large Retail Formats

Over the past few decades, large retail formats have gained market share in grocery retailing. These large-scale retail formats are also referred to as "big-box retailers".

While this trend has developed similarly worldwide, specific formats have developed in different countries. **Hypermarkets**, which originated in France, are the largest of these. Their size ranges from 9000 to 30,000 m² (e. g., *Carrefour* and *Auchan*). The German **"SB-Warenhäuser"** (e. g., *Metro's Real* format or *EDEKA's Marktkauft* format) tend to be smaller, with sizes starting at 5000 m². While these European formats have a larger share of food items, ranging from 60 to 70 %, in the USA **supercentres** (e. g., *Walmart, Kmart, Target*) range from 14,000 to 21,000 m² and carry a broader assortment of general merchandise. Thus, the share of general merchandise is higher, ranging between 60 and 70 % (Levy et al. 2014, p. 45).

These large retail formats usually follow an aggressive, promotion-oriented **low-price strategy**. The stores are generally located in isolated sites or found near to or integrated into shopping centres. The architecture is usually cost-oriented, with a simple store design and **function-oriented** store atmosphere. As these large retail formats offer a broad assortment of food and general merchandise and thus provide **one-stop-shopping** opportunities, customers usually buy more. These store formats have a greater market area than smaller store formats (e. g., supermarkets), meaning customers are willing to drive further. These stores, therefore, provide substantial parking facilities. Because of their low operating costs and the combination of food with higher margin general merchandise, which allow for **aggressive pricing strategies** and increased shopping convenience (e. g., in terms of a broad and deep assortment), over the past few decades large retail formats have gained market share mainly at the expense of conventional supermarkets. However, some countries (e. g., France) seem to have reached a saturation point, and hypermarket operators are searching for ways to modify the format to maintain market share.

2.3.6 Convenience Stores

Convenience stores ("c-stores") are usually in easy-to-access locations, such as heavily frequented areas or urban neighbourhood locations. They open long hours (up to 24 hours, depending on local or national legislation). The stores are small and facilities are limited, with an average atmosphere and average service level. Convenience stores can be operated as standalone units (e. g., *Tesco Express*, *7-Eleven*, *Auchan, Coop Pronto*), but are often coupled with petrol stations (e. g., *Shell Shop*s, *BP* or *Aral Stores, Esso Shops*).

The focus of convenience stores is on **ease of shopping**. They offer fast shopping, allowing customers to pick their merchandise quickly and check out quickly (Levy et al. 2014, p. 46).

The **very limited assortment** of these stores is food-oriented. Convenience stores thus also offer "mental convenience", as the limited assortment enables customers to make their choices quickly (Berry et al. 2002). A high proportion of sales are impulse purchases, mainly in areas such as snack foods, soft drinks, beer and wine, tobacco products or newspapers and magazines. The average transaction in convenience stores is small, and the products are often consumed shortly after purchase. Prices in convenience stores are usually above average.

2.3.7 Hard Discounters

Hard discounters in food retailing usually follow a very aggressive **everyday low-price strategy**, with prices up to 20 to 30 % below those of conventional supermarkets. They offer a small selection of items and, therefore, are also referred to as **"limited-line stores"** or **"limited-assortment stores"** (e. g., Berman and Evans 2013, p. 153). A typical *Aldi* store, the best-known example of this format, carries about 1080 stock-keeping units (SKUs). The basic assortment consists of food items with a high rate of turnover in few size options and brands are offered per product category. Other prominent examples of internationally successful hard discounters are the German *Lidl* and *Carrefour's Dia*.

The stores are characterised by their "no-frills" approach, meaning that, for example, there are almost no services available (no helpdesk, no sales staff in attendance, etc.) and store design and atmosphere are very simple and cost-oriented. Often, products are sold out of boxes (**"box stores"**) or cut cases and are presented on pallets. Food-based hard discounters often carry a limited range of manufacturer brands and rely heavily on **low-price store brands** (see Chap. 12). Thus, prices vary between different retailers.

Discounters often complement their assortments with a weekly or semi-weekly changing selection of **general merchandise**, sold at very low prices and heavily promoted via newspaper advertising or flyers distributed to households. These items come from a variety of product categories (ranging from personal computers and furniture to home accessories) and often have no association with the regular merchandise carried by the retailer. Such items are offered in order to increase store traffic, and non-food items (in some cases produced exclusively for this purpose) usually have a higher margin than food items.

Hard discounters are usually located in easily accessible **traffic-oriented and cost-oriented locations** with a focus on low occupancy costs, e. g., neighbourhood locations or periphery sites with adequate parking facilities. Because of their aggressive pricing strategies, the different types of convenience they offer (e. g., "mental convenience" because of the limited assortment and quick shopping because of the small store size) and location strategies, hard discounters have grown consistently over recent decades. They often play an important role in **proximity retailing**.

2.3.8 Drugstores

Drugstores are specific types of specialty stores that focus on beauty, health and personal grooming merchandise (Levy et al. 2014, p. 54). In addition, these stores often sell categories such as food items, magazines or newspapers, stationery, toys or gifts. Depending on governmental healthcare policies, in some cases **pharmacies** are associated with drugstores and sell prescription pharmaceuticals in addition to over-the-counter (OTC) medicine. The product categories sold in this store format are similar to food items in some respects, mainly in terms of shopping frequency and purchasing patterns **(near-food items)**. In some statistics, drugstores are therefore classified as food store formats.

Compared to traditional specialty stores, drugstores tend to be more aggressive on price and apply pricing strategies such as everyday low-price (EDLP) strategies or promotion pricing. Important players include *Boots*, *Walgreens*, *Rite Aid*, *A.S. Watson* or *dm-Drogeriemarkt*.

Drugstores are often located in city or shopping centres, but are now increasingly found in local neighbourhoods or isolated sites. Thus, they play an important role in **proximity retailing** and usually offer a high degree of **shopping convenience** via their location strategies, small store sizes and speedy checkout facilities.

2.3.9 Warehouse Clubs

Warehouse clubs are a food retail format developed in the USA and later introduced into countries such as Spain and France. However, the format is not prevalent worldwide. Warehouse clubs sell their products to both end-users and small- to medium-sized companies. Business members typically represent less than 30 % of the customer base, but account for approximately 70 % of sales. **Membership** is required and customers are charged an annual fee. The largest warehouse clubs in the USA are *Costco* and *Sam's Club* (*Walmart*).

This type of store is characterised by **low prices** for a limited assortment comprising half food and half general merchandise. The stores are very large (9000 m^2 or larger) and are located in secondary sites (i. e., in low-rent districts). Store architecture and design are very simple and cost-oriented, characterised by a simple interior, concrete floors and wide aisles (Ogden and Ogden 2005, p. 104).

Items are usually presented on pallets. This type of store offers fast-moving, high-turnover merchandise, thus minimising holding costs. Warehouse clubs concentrate on special purchases from popular brands. Often, products are sold that are sourced from manufacturers in special circumstances (e. g., overruns, returns, etc.) (Berman and Evans 2013, p. 160).

The warehouse club format resembles **cash and carry wholesalers** (e. g., *Metro Cash & Carry*), which also require membership. Even though membership is restricted to companies and these outlets focus on **business-to-business trade**, end users also frequently purchase at these stores.

2.3.10 Non-store Formats in Food Retailing

While most food retailing occurs via store formats, there are several **non-store formats** through which consumers can purchase groceries and related products. For example, **remote ordering** channels, such as traditional catalogues or Internet shops, can be used to distribute merchandise. While these formats are generally gaining in importance, the share of groceries offered through mail order channels remains limited (see Chap. 4).

For fresh merchandise (e. g., farm produce, bakery products, meat or fish), **market stands** or **truck and van sales** are traditional modes of distribution mostly used by small producers to reach their customers as a specific form of direct selling or implemented by retailers as specific methods of **proximity retailing** in rural areas. Because of the close and personal contact with their customers, these vendors often have high retention rates among their customer base. However, the costs associated with direct selling are very high and, therefore, so are the prices. **Vending machine retailing** is another alternative. Merchandise such as snacks and soft drinks are stored in a machine and dispensed to customers who pay via cash or card. Vending machines are usually placed at convenient locations with high traffic (Levy et al. 2014, p. 72). Vending machines have undergone several innovative developments recently. For example, new types of **kiosk vending machines** provide customers with product displays and information on the merchandise and electronic systems track inventory and cash, thus reducing stock shortages or malfunctions.

2.4 Conclusion and Outlook

The food retailing landscape has changed dramatically over the past few decades. While the relevance of these diverse store formats in food retailing differs around the world (see Fig. 2.5), **competition** has increased due to various factors, including mergers and acquisitions and the internationalisation of retail companies. In addition, the main retail formats in this sector have also changed as a result of these developments, **technological progress** and responses to changes in customer behaviour.

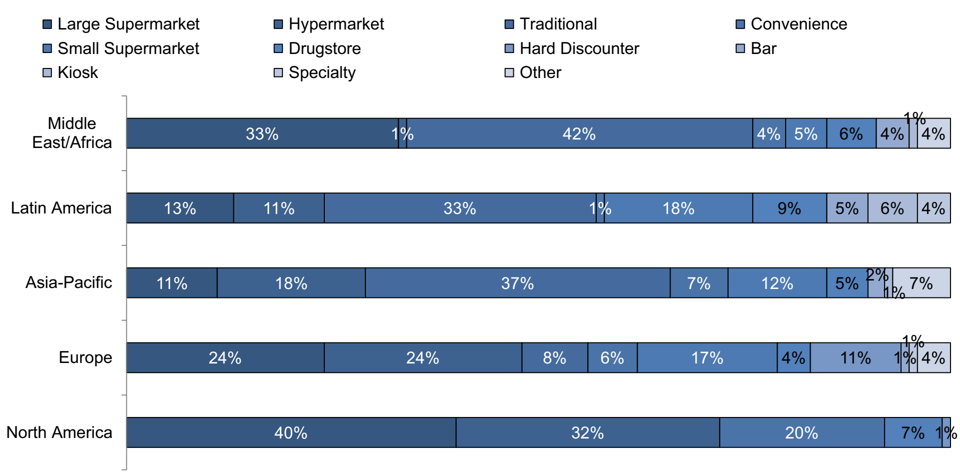


Fig. 2.5 Regional share of trade by retail format. (Nielsen 2014)

Even though new non-store retail channels have been developed due to new developments in information and communication technology, **brick-and-mortar store formats** remain the most important channels for selling groceries. Still, new store formats which gain market share spur important developments. The most important in this context is the increase in discount-oriented retail formats such as large retail formats (e. g., hypermarkets) and small, food-based hard discounters. *Convenience stores* are also becoming more important.

In order to remain competitive in the mature business of food retailing, more and more retailers are carrying merchandise which falls outside their traditional assortment. This phenomenon is referred to as **"category migration"** (Zentes et al. 2005, pp. 52–55) or the "blurring" of retail formats (Fox and Sethuraman 2010, p. 246; see Chap. 12). For example, food discounters offer general merchandise as special offers in weekly or semi-weekly promotions to generate store traffic and improve profit margins. Another important trend is that food retailers are extending their regular assortment to increase sales and margins. For instance, hard discounters have extended their basic assortments in recent years by adding fresh meat and frozen food.

Further Reading

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- Morschett et al. (2005). Perception of Store attributes and overall attitude towards grocery retailers: The role of shopping motives. *International Review of Retail, Distribution and Consumer Research*, 15(4), 423–447.
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2.5 Case Study: Lidl and Kaufland

2.5.1 Profile, History and Status Quo

Both *Lidl*[1] and *Kaufland* are part of the *Schwarz Group*, the biggest European retail chain. With over 79.3 billion EUR in revenue in 2014, the group surpassed competitors such as *Carrefour* and the *Metro Group* (Handelsblatt 2015b). Both *Lidl* and *Kaufland* are based in Germany with headquarters in Neckarsulm. However, as a result of their international

[1] Sources used for this case study include the companies' websites www.lidl.com and www.kaufland.com, various annual and interim reports, presentations and the explicitly cited sources.

activities, only 34 billion EUR of their 2014 revenue came from Germany (Lebensmittel Zeitung 2015).

The roots of the Schwarz Group date back to 1930, when Josef Schwarz began to invest in the small company *Südfrüchte Großhandlung Lidl & Co*. Immediately after his initial investment, the former fruit vendor was transformed into the wholesale market *Lidl & Schwarz KG*, offering a wider range of foods and goods. After the end of World War II, Schwarz and his partner started to rebuild at once and were able to reopen a few years later.

When Dieter Schwarz, son of Josef Schwarz, began to take over the family business in 1973, he decided to open the first discount store, with a new name that no longer reflected his own. Thus he took the name of his fathers' former business partner. *Lidl* was introduced in Ludwigshafen, Germany, and was an immediate success; just four years later, the chain had 30 different stores. At first, Schwarz was uncertain about the chain's future, so not all of these were discounters. It wasn't until the late 1970s that he decided to concentrate on discount stores with his *Lidl* brand.

After *Lidl* developed into a pure discount store, Schwarz introduced *Kaufland* as an alternative to this philosophy. In 1984, he opened the first self-service superstore under this new brand, the beginnings of another success story. After the first store opened in Neckarsulm, *Kaufland* grew rapidly. After the fall of the Berlin Wall and German reunification, Schwarz was eager to implement his West German brand in this new market. In the late 1990s, the first East German *Kaufland* store opened its doors to new customers, followed by many others. Today, *Kaufland* operates over 635 stores in Germany and employs over 80,000 people. With over 60,000 products on its shelves, *Kaufland* is one of the leading full-range retailers in Europe.

Early on, Schwarz decided to develop both chains separately from each other in order to avoid cannibalism between the two formats and to gain market share by targeting a larger group of potential customers. Therefore, *Lidl* and *Kaufland* differ in a number of key ways (see Table 2.2) and can be defined by the elements relevant to their specific target group. Even though some of the initial standards have been altered, both formats still occupy distinct positions. While *Lidl* is positioned as a typical food hard discounter, *Kaufland* displays some elements of a hypermarket, albeit with a clear emphasis on cheaper prices, smaller

Table 2.2 Characteristics of *Kaufland* and *Lidl*. (Adapted from DIWG/STIWA 2012, FAZ 2015)

	Kaufland	Lidl
Size (m^2)	3000–5000	800
SKUs	60,000	1600
Prices	Low/average	Low
Merchandise and Services	Fresh meat, fresh cheese, bakery, few non-food items	Bakery, few non-food items, store and manufacturer brands
Location	City or neighbourhood, traffic-oriented, large parking availability	City or neighbourhood, traffic-oriented

store sizes and a smaller share of general merchandise than the typical hypermarket. Thus, *Kaufland* is an example of a large-scale discounter (see Table 2.2).

2.5.2 International Activities and Distribution Network

Ever since their successful launch in Germany, both divisions of the company have also been very active internationally. In 1998, *Kaufland* began its international expansion by opening a store in the Czech Republic. Recently, the highly saturated German market has made *Kaufland's* successful growth heavily reliant on European expansion (German Retail Blog 2014). Today, *Kaufland* operates in six foreign markets and plans to enter Serbia as a seventh in the near future. The company has supported its international expansion by installing 17 distribution centres all over Europe to ensure on-time delivery to all of their 1200 branches. Unlike competitors like *Auchan* or *Carrefour*, *Kaufland* rarely enters another market by acquiring an existing chain. Although they have indicated interest in acquisitions at several points, the *Schwarz Group* has so far relied on its strong growth potential (German Retail Blog 2014). In recent years, *Kaufland* has been the most active full-range retailer in terms of expansion, which is partly the basis for their latest financial success compared to their major competitors.

Lidl first entered foreign markets in 1989 with a store in France. Since then, *Lidl* has been extremely active in international expansion, and is now active in 26 European countries with 9875 stores (Planet Retail 2014). These expansions have mostly met with great success. *Lidl* is particularly successful in France, where it currently holds the largest market share of any discounter, operating more than 1500 stores in total. In some cases, *Lidl* has made an exception from their strategy of always implementing their own structures when expanding, by acquiring competitors in countries such as Bulgaria and Romania, where they acquired stores from their competitor *Tengelmann*. *Lidl* relies on numerous distribution centres that each deliver to around 60 stores in their area (Tengelmann 2010).

2.5.3 Economy forces Change

Although initially designed to cater to very different demands and therefore different kinds of customers, *Lidl* and *Kaufland* are growing closer. As a full range retailer, *Kaufland* has always sold product categories that *Lidl*, as a pure discounter, did not offer. But due to recent trends and developments, *Lidl* and other discounters have had to change their appearance to ensure their survival.

After a noticeable decline in the early 2000s, discounters such as *Lidl* are now regaining market share. One of the main reasons for this new prosperity is the expansion of their range of goods. By adding a higher share of higher quality fresh products and selling them at a higher profit margin, they have been able to improve performance. In their current strategies, *Kaufland* and *Lidl* both sell freshly baked pastries, meat and other high quality organic products in their stores. Nowadays, only 40 % of revenue comes from lower priced categories and products (FAZ 2014). Adding to those developments, service has also become more important to discounters. An improved focus on service is another reason behind *Kaufland's* and *Lidl's* recent success (Handelsblatt 2014).

Lidl and *Kaufland* have made significant changes to their assortments of wine, meat, bread, vegetables and fruit. Nowadays, *Lidl* carries over 20 different coffee products and offers meat from animals butchered just 48 hours before hitting the stores to ensure freshness.

By adding well-known premium brands to their offerings while other, bigger chains concentrated on cheaper products offered as private labels, *Kaufland* and *Lidl* were both able to garner a lot of attention and market share in the early 2000s. In recent years, however, their competitors have closed this gap and also introduced higher quality products onto their shelves. A famous example of this fierce competition is *Lidl's* partnership with *Coca-Cola*. *Lidl* was the first discounter to offer this brand to their customers. However, after *ALDI* and other competitors also introduced the brand into their assortments, a price war began, and intense competition forced these companies to sell *Coca-Cola* products at extremely low prices (Die Welt 2014).

Following this trend, *Kaufland*, *Lidl* and competitors introduced their own premium brands to better cater to their customers' demands and secure higher profit margins (Genios 2015). These recent developments brought *Lidl* and *Kaufland* even closer. With *Lidl* expanding their products and therefore sales, they are not as clearly separated as when Schwarz first established his retail brands in the 1970s. Since both are still performing well financially, the oft-feared cannibalism of market share has not been a major issue so far. Nevertheless, both companies are keen to use synergies to get ahead of other competitors. Initial attempts such as the *Bonback* bakery that delivers to both *Lidl* and *Kauf-land* have proved very successful, and the CEOs of both brands are eager to widen this cooperation (Planet Retail 2015). With rising interest in their new products, *Lidl* will be forced to create more production facilities to meet higher demand. They currently only have three food production facilities under their own control and are therefore strongly reliant on outside suppliers (Planet Retail 2015).

As *K2020*, *Kaufland* is rebuilding its brand and revaluating its products and store quality. In the coming years, many stores will either be upgraded to meet modern standards or be closed. Only those that provide added customer value will survive the *K2020* initiative. As well as offering newer, fresher and locally produced products, this will also mean implementing a modern style for *Kaufland's* interior design: factors that used to be unimportant. Non-food products such as bicycles, folders or other supplies will no longer be part of their product line, reducing store size and increasing efficiency. Frank Lehmann, CEO of *Kaufland*, predicts that at least 24 of their German stores will close because they will not meet these new standards (FAZ 2015).

In 1997, *Lidl* established a website (www.lidl.com) where they started to offer products not sold in their stores. In addition to the weekly special offers in their stores, *Lidl* customers can find another set of promotional offers online that often complement the in-store offers. In addition to these online purchase options, both *Kaufland* and *Lidl* customers can find

Fig. 2.6 Lidl's "Good Quality" campaign. (Lidl 2015, https://www.lidl-lohnt-sich.de)

additional information on products, special offers and stores on the companies' websites. Customers can further engage through special recipes and competitions. Each country or market has a unique website that follows an overall design template but varies in content and products displayed. These websites are also an example of further cooperation between the two retail brands, as both are operated by the same service department at the Neckarsulm headquarters (Planet Retail 2015).

2.5.4 Rebuilding a Brand – "Lidl lohnt sich"

As mentioned above, *Lidl* and *Kaufland* have both undergone a series of changes to their appearance and product assortment. *Lidl* was especially keen on softening their earlier discount-driven image. Faced with declining sales and a growing trend for convenience and naturally grown products, they were forced to act. Therefore, they started a new communication initiative in the late 2000s that focused on high quality products. Through new slogans and an alternative look and feel to their stores, they began to move away from their earlier price-driven image.

Previous *Lidl* advertisements focused on their cheap prices and had almost nothing in common with the new marketing approach, as shown in Fig. 2.6. In general, this new imagery is keen to convey the newfound quality of *Lidl* products. In addition, the products chosen for these advertisements are not part of the discount markets' usual product lines. With the addition of freshly baked pastry and finer wines in particular, *Lidl* is trying to reach new customers who are less price-sensitive than their former clientele. Given the huge number of stores, it took until early 2014 to implement a bakery section in all of their European subsidiaries. Because of the targeted new look and feel of the *Lidl* retail brand, the general appearance of their stores will also change in the coming years. These changes will be visible both inside and outside the stores.

The store depicted in Fig. 2.7 is a new concept that represents the best-case scenario for a *Lidl* store. Their new design has been specifically built to be as energy-efficient as possible, complementing the more natural and high quality focus of their general communications. *Lidl* is currently working on implementing energy norm ISO 50001 in all of their stores, reducing CO_2 production and costs through lower energy consumption. By the end of 2015, all of *Lidl's* German stores are supposed to be ISO 50001 certified. However, the model store is obviously not suitable for every circumstance, particularly within cities and highly populated areas.

Fig. 2.7 Lidl store. (Lidl 2015, http://www.presseportal.de/pm/58227/2976929)

Furthermore, *Lidl* has made and will continue to make significant changes to their stores' inside appearance. Their employees will be responsible for transforming the stores to better match those shown in the advertisements. The changes will have a major effect on the price tags, signs and shelves used within the stores. In addition to these physical changes, employees have received special training to better understand and communicate *Lidl's* new image and philosophy.

2.5.5 Conclusion and Outlook

To ensure further growth in the near future, *Kaufland* has declared an interest in taking over a few stores from the former competitor *Tengelmann* in Germany (Handelsblatt 2015a). With over 400 potential stores located in the south of Germany, this acquisition would greatly boost *Kaufland*'s market share in that region. The German cartel office has yet to approve this acquisition, as it could lead to a monopolistic situation in the region. In addition, *Kaufland* has recently announced plans to further invest in reshaping their existing branches. Seeing as their initial store design and set-up can no longer cater to current customer demands and standards, they are forced to respond to these pressures. During their rapid growth in the early 1990s, *Kaufland's* focus was mainly on expanding as fast as possible to secure the perfect spots for their stores. Now, *Kaufland* CEO Frank Lehmann plans to invest in these stores' atmospheres as well (German Retail Blog 2014).

Given the highly saturated European markets, opportunities to secure further growth are limited. *Lidl* is therefore planning to set up stores in the US and enter a new market. As with all of their international activities, *Lidl* plans to adjust their format to better suit American customers, while trying to remain loyal to *Lidl's* established standards, visions and philosophies. The quality-oriented communication approach will be part of this next stage, and further steps will be taken to gain additional shares in all markets in which *Lidl* is currently active. Initial plans to enter the US market with 100 stores during 2015 had to be cancelled, since the US situation differs significantly from that of *Lidl's* home market. Establishing the necessary supply chain is the main challenge to overcome before starting operations in the US (Planet Retail 2015). Competition from *ALDI*, their arch rival, which started its US operation in the late 1970s, has given *Lidl* another challenge to overcome. With planned annual investment of over 600 million USD in the US market, *ALDI* will almost certainly be able to obtain further market shares in this highly competitive market (Planet Retail 2015).

Schwarz Group CEO Klaus Gehring also showed interest in increasing synergies between the two growing retail brands, despite formerly operating them as completely separate departments. As discussed above, they have already started using similar production facilities and delivering goods to one another. Gehring wants to build upon this experience and try to merge areas such as administration or equipment procurement. These ideas are vastly different from *Schwarz Group's* early days, when speed was often more important than efficiency. In the near future, both companies will use currently overlooked synergies to ensure a steady growth in revenues (German Retail Blog 2014).

Questions

1. *Lidl* is planning to enter the US market in the next few years. What are likely to be the biggest obstacles to overcome when entering this unknown market?
2. *Lidl* and *Kaufland* are growing closer. What advantages and disadvantages will this have?

- See the companies' websites.
- See Planet Retail (2014).

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