



## Leverage actionable insights to **increase competitiveness** in U.K.'s retail industry

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Combating tough economic conditions, declining consumer spending, and ever-increasing competition in the U.K. grocery market



### Key Facts (2007 estimates)

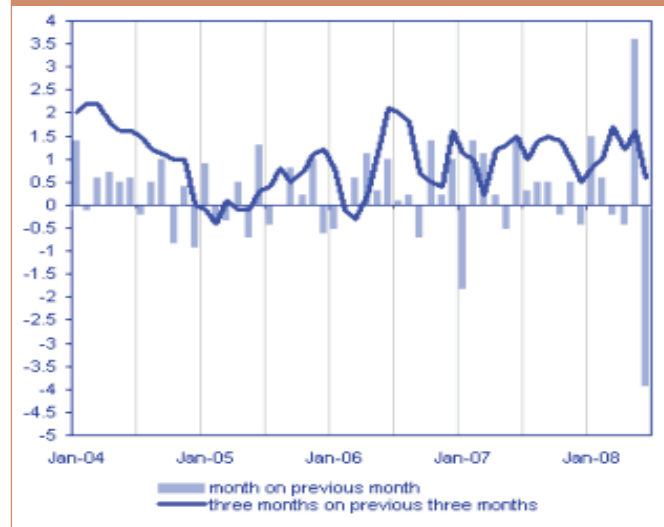
- GDP: USD 2.756 trillion
- GDP growth (real): 2.8%
- Inflation: 3%
- Population: 60.77 million
- Formal retail sales: GBP 265 billion
- Formal retail sales growth: 3.8%

Source: <http://www.statistics.gov.uk/>

Source: <sup>1</sup>British Retail Consortium

When the United Kingdom's National Statistics Office announced a 3.6 percent increase in monthly retail sales volume during May 2008, it came as an unexpected and pleasant surprise to many, especially considering the weakening British economy. However, the joy was short-lived as retail sales volume plummeted 3.9 percent in June 2008 (down 2.2 percent on an annualized comparison), and like-for-like sales value declined 0.9 percent<sup>1</sup> during July 2008, vis-à-vis same period last year; resurfacing concerns pertaining to the health of U.K.'s retail market (valued at close to GBP 265 billion<sup>1</sup> during 2007).

Retail Sales Volume in the United Kingdom (Jan' 04 - June '08)



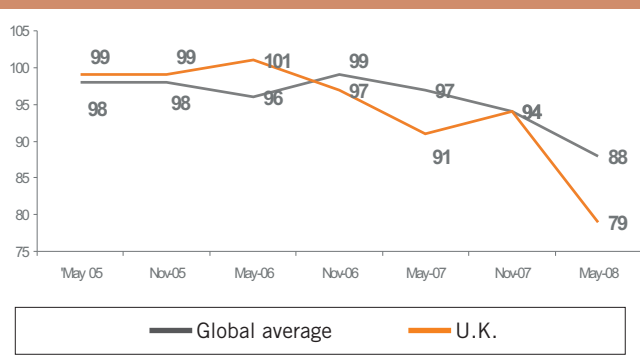
Source: National Statistics Office



Some of the factors that have adversely impacted the country's retail market include

- **Reduced liquidity** as a result of
  - Crisis in the U.S. banking, financial services industry, which spilled across the Atlantic to the United Kingdom within weeks of hitting the U.S. financial services alone accounts for close to 8 percent of U.K.'s GDP directly, while BFSI and related businesses contribute roughly 30 percent to the GDP. The mortgage crisis adversely impacted the credit availability (both corporate and consumer) with banks resisting and at times unwilling to lend, thereby reducing liquidity
  - Rising oil prices triggering an unprecedented increase in global commodity prices including those in the U.K. Higher inflation rates have reduced the consumers' basket volume even if the value remains the same (prolonged high-inflationary conditions may drive consumers start diverting funds for future contingencies)
  - Declining currency with the GBP declining for 18 successive months of decline vis-à-vis the Euro. This has put immense pressure on imports
- **Consumer confidence** has plummeted to 79 during May 2008 (the lowest since 2003), as compared to 94 during November 2007, and 91 during May 2007, as a result of factors such as rising fuel costs (propelling price rise across all major product categories), and falling property prices. This trend is shown in the following chart

U.K.'s Consumer Confidence Index versus global average 05-08



Worst hit by the economic downturn has been the non-food sector (including household goods, textile, clothing and shoes), which has experienced a strong decline in sales. This is underscored by

- **Declining same-store-sales or like-for-like sales** for non-grocery retailers such as Homebase and B&Q (specialty home goods retailers)

- **Weak sales experienced in non-grocery categories** by Tesco, the U.K.'s largest retailer.

In stark contrast, food and grocery retailing (accounting for more than 40 percent of total retail sales in the U.K.) continues to grow with close to a 6.5 percent increase during June 2008. Although a part of this growth can be attributed to food inflation (currently running higher than average retail price inflation), it is also attributable to the low substitutability of food and related products in the daily shopping basket, and the increasing percentage of people in the age group of 65+ years (who are generally less likely to purchase the latest fashion and technology products). This trend is shown in the following chart

Retail and Food Inflation in the United Kingdom (1993-2008)



Source: National Statistics Office

### Case Study

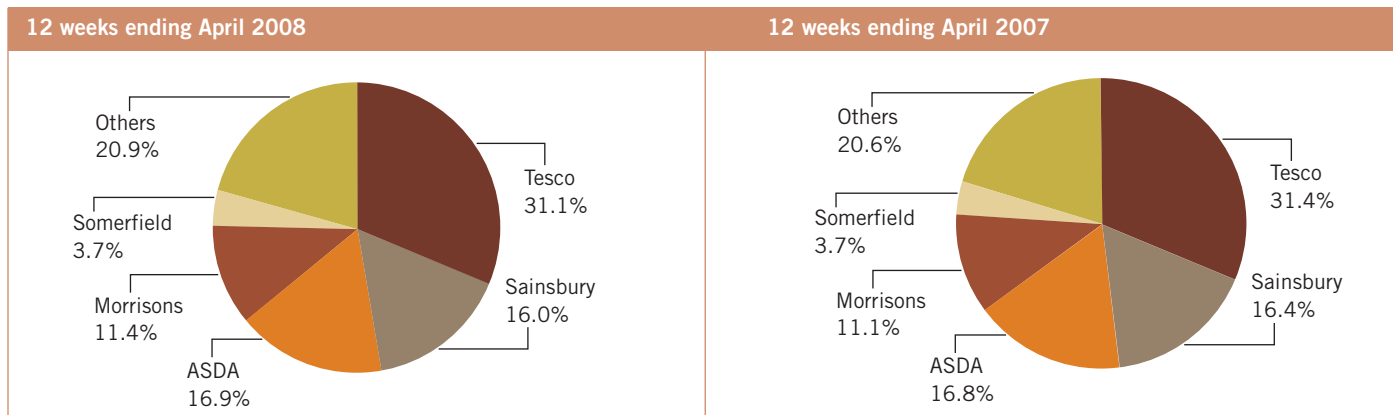
WNS helped a leading U.K. based grocery retailer understand consumer attitudes and behaviour regarding health and nutrition; thereby facilitating decision making with regards to merchandising, new product development and in-store communications. The solution delivered by WNS included

- Defining 13 product categories based on a typical household basket
- Developing a unified score based on 5 nutritional metrics using Principal Components Analysis
- Segmenting customers using CART decision trees based upon product consumption data and respective nutritional profiles for around 50,000 products
- Developing scores for unclassified products.

Based upon the analysis drawn from WNS's study, the grocer is developing new products under its private label offering.



**United Kingdom food and grocery market - Key players and market share**



Source: TNS Global

Moving over to the supply side, the U.K. grocery market comprised close to 55,540 retailers<sup>2</sup> during 2007, which can be classified into supermarkets and superstores (accounting for roughly 73 percent market share<sup>3</sup>), convenience stores (20 percent share), and traditional 'mom-and-pop' stores (approximately 7 percent market share).

The market is highly consolidated with the top 5 players (Tesco, Sainsbury, ASDA, Morrisons, and Somerfield) accounting for roughly 79.1 percent of the market share<sup>4</sup> for the 12 weeks ended April 2008, down 30 basis points from 79.4 percent during the same period in 2007. (Please refer to the above exhibits for comparison)

However, with declining consumer confidence, and curtailed spending, the competition among retailers is getting fiercer with retailers adopting an array of strategies to attract customers. These strategies can be broadly classified under five buckets

- Moving to a multi-format strategy
- Increasing mergers and acquisitions
- Consumer-oriented merchandising
- Flexible pricing
- Increasing use of business intelligence tools for greater consumer insights.

These are described in the following paragraphs.

**Multi-format strategy**

Changing consumer lifestyles and shopping behavior (smaller household size, time constraints, and growing health consciousness encouraging shoppers to buy in smaller quantities resulting in frequent but shorter shopping trips) have prompted retailers to adopt a multi-format strategy (operating multiple formats such as discount stores, superstores, online, and convenience

stores in the same market. These formats can be broadly differentiated in terms of store size, merchandise and customer mix). This trend is evident from the increasing number of big box retailers venturing into multiple retailing formats (such as convenience, online, and specialty), thereby giving retailers a wider presence (across consumer groups and geographies) and ability to customize the store size and layout according to local economics and consumer shopping needs.

A good example of a multi-format strategy is that of Tesco (the largest U.K. retailer). Tesco has rolled out a robust multi-format strategy in order to cater to a varied consumer base (up market and value-seekers), and shopping needs (low-value and more-frequent shopping trips versus high-value/bulk and weekly/monthly shopping trips). For example, the retailer has positioned Tesco Express (a convenience store) to address immediate shopping needs while Tesco's Extra, Metro and Supermarket stores are primarily focused on addressing the demands of weekly shopping trips and stocking a combination of premium and discounted products.

The retailer has also forayed into the home goods and utility segments through the launch of its Tesco Homeplus (sells home goods, apparel, consumer electronics, cosmetics, and very limited groceries) in 2005, and Dobbies (a garden center) in 2007. However, Tesco's biggest coup was the launch of Tesco Direct (catalogue business for the non-grocery segment) in 2006, which has helped the retailer not only supplement tesco.com (online business for groceries) but also provide a differentiating edge compared to its competitors. The fact that ASDA plans to launch ASDA Direct (replicating Tesco Direct) in October 2008 shows the importance retailers are attaching to format strategy. However, Tesco and ASDA are not the only retailers in the U.K. to adopt a multi-format strategy, as shown in the following chart

Source: <sup>2</sup>Reuters (Primary source: National Statistics Office) <sup>3</sup>Food and Drink Economics Branch - Defra 2006 Report <sup>4</sup>TNS Global National Statistics Office)



**Key grocery retailers in the U.K. - Formats**

Retailer	Supermarket	Hypermarket	Convenience	Discount	Online	Other
Tesco	Tesco Tesco Metro	Tesco Extra	Tesco Express T&S One Stop	Tesco	Tesco.com Dobbies.co.uk	Tesco Direct HomePlus
ASDA	ASDA	ASDA Wal-Mart Supercenter		ASDA Essential	ASDA.co.uk	ASDA Living George
Morrisons	Morrisons					
Sainsbury's	Sainsbury's Sainsbury's central		Sainsbury's Local		Sainsbury's. co.uk	

Source: WNS Research

Only Morrisons has a single format strategy, which they have maintained for some time. However, the retailer is now exploring the possibility of opening small box stores to address the changing shopping needs of consumers.

**Mergers and acquisitions**

Mergers and acquisitions have always been a core strategy for growth, be it in any geography, phase of industry life cycle, or fragmented or consolidated marketplace. With organic grocery growth in the United Kingdom becoming more difficult due to insignificant growth potential in an untapped consumer base, declines in consumer spending, and ever increasing competition, many retailers are resorting to inorganic route to growth as a key go-to-market strategy. Not only does this strategy help retailers rapidly develop economies of scale, but also enables them to acquire customer base and real estate, two components that are of premium value in the U.K. retail industry at present.

Recent examples of mergers and acquisitions in the U.K. retail marketplace include

- Proposed acquisition of Woolworths Group by Baugur Retail Investment Group
- Co-operative Group's acquisition of Somerfield for GBP 1.56 billion
- Sale of 10 Sainsbury's convenience stores to Co-operative Group
- Morrisons' acquisition of Safeway.

**Consumer-oriented merchandising**

U.K. retailers have realized that they must approach the marketplace in new and different ways to capture consumer attention. This has led retailers to move away from the traditional merchandising or product mix strategies that they followed for decades. Each component of merchandising - be it sourcing, in-store positioning, private label-national brand mix, or product promotion - is based upon what best suits consumer requirements.

For example

- Both Morrisons and ASDA have moved to a high local (from within U.K.) sourcing model
- Retailers such as Morrisons, Aldi and Lidl are restructuring their stores by increasing the selling area offering non-grocery products (such as health and beauty)
- Retailers are closely monitoring and evaluating their strategies pertaining to private labels, aiming to strike the right chord with customers. Some examples include
  - At one end of the spectrum, Tesco is developing more premium product lines such as exotic fruits or products offered through Tesco Finest, especially in the southeast U.K.-to attract affluent customers who currently prefer shopping at Waitrose or Sainsbury's. On the other hand, it plans to launch a new private label offering named 'Tesco Standard' in the autumn of 2008, aimed at value-seeking customers in order to effectively compete against the discount chains
  - Morrisons has a range of private label initiatives, which include further strengthening its organic own-brands and premium private label offerings 'The Best' and adding a new private label line called 'Food Fusion' aimed at reinforcing an up-market positioning
  - ASDA plans to reduce SKU levels by 10 percent and stock more category leaders/brands with high brand equity and customer acceptance.

**Case Study**

WNS is currently assisting a US based specialty office supplies retailer to identify customers (from the retailer's total customer base of 24 million) for its promotion (mail coupon booklets) campaign, and decide which coupon offers should be sent to each identified customer category. WNS' solution encompasses

- Selecting customers with maximum purchases in the promoted product categories during the past 12 months
- Identifying buyer offers based on the products bought by identified customers
- Identifying associated products that are sold with the buyer offers using market basket analysis
- Assigning coupon offers for associated products to complete the coupon book.



### Flexible pricing

Improving price perception has become a key area of focus for grocery retailers, with almost all chains aggressively developing and executing price promotion campaigns. To illustrate

- In June 2008, while Tesco reduced the price of 3,000 items by 50 percent, ASDA and Morrisons reduced the prices of 10 key value items (including bread, milk, and eggs), and 2,000 other items, respectively
- In January 2008, Aldi launched a price promotional campaign called 'The A List' wherein it lowered the prices of 38 key products by 50 percent. The retailer carried out a similar campaign in March 2008 (called 'Price Turnaround') wherein it lowered the price of 100 products by 15 percent compared to 2006 prices. In both cases, the campaigns have been backed up with strong in-store promotions highlighting the new prices as compared to the old prices.

### Increasing use of consumer insight

With the business environment becoming increasingly dynamic, the need for quick decision making based upon real-time data has become extremely critical. To this end, leading retailers are now deploying a range of business intelligence tools. These tools use information (including retailer-specific data such as category and brand-wise sales, customer footfalls, promotion responsiveness, etc.; and market specific data such as demographics, market competition, and regulatory framework) gathered from primary (market research and field surveys) and secondary (web-based) research and use sophisticated statistical and analytics models to provide key insights and answers to strategic and operational questions. Some of these insights and questions revolve around

- **Place** - Market entry and exit; customer identification, segmentation, and targeting; store location analysis; identifying and managing store locations
- **Product** - In-store merchandise mix, managing private label products, in-store product assortment; inventory management
- **Price** - EDLP versus premium pricing; price sensitivity across customer segments and product categories; sales productivity optimization; margin management; price positioning/architecture
- **Promotion** - Mode and channel for promotion (in-store through fliers, discount coupons, etc., or use of mass-media such as radio, television, newspaper, etc.); effectiveness and customer responsiveness to promotional campaigns and loyalty schemes

- **Competitive intelligence** - Competitive mapping (in terms of place, product, price, and promotion); acquisition target identification and evaluation
- **Supply chain management** - Vendor/supplier management based on performance of their products and services.

Some business intelligence tools used by U.K.-based retailers include

- Clubcard intelligence used by Tesco to track spending activities of over 13 million households that shop in its stores to proactively manage merchandising and promotional activities
- 'Self Serve' a business intelligence application used by Sainsbury's that captures and analyzes sales data (up to 40 million transactions a day) to help the retailer and its suppliers to track sales performance of its products, as well as analyze shopping behavior.

### Conclusion

With the demand-side economics (including economic environment, consumer confidence and spending) in the U.K. not likely to improve in the next few years, retailers must deploy a use a combination of strategies (some of them discussed in this article) to succeed in the marketplace. Is there one single strategy that can be adopted across the board? The answer is 'not really'. For example, competing through heavy price cuts and discount promotions may not be the best strategy for a premium, up-market retailer, as compared to offering more differentiated products and services. Similarly, inorganic growth (through mergers and acquisitions) may not be feasible for all retailers because liquidity issues and resultant low return on investments. The impact and efficacy of any strategy pertaining to either pricing, mergers and acquisitions, or multi-format offerings will vary across retailers and will ultimately depend upon the retailer's ability to proactively and effectively map and understand

- Underlying and underserved **consumer needs** - whether they revolves around price, product variation, or convenience
- Evolving **competitive landscape** - go-to-market strategy of competitors (targeted consumers, product categories, pricing, and mode of promotion)
- Retailer's own **past performance** - efficacy of retailer's promotion, pricing campaigns and formats
- **Market opportunities** - entering/exiting geographic and consumer markets; potential merger and acquisition targets.



In short, the success mantra for retailers lies in gaining better and faster insights pertaining to market, consumer, self and competitors and then using these insights to develop and execute business strategies.

Identifying and developing these insights to define and sharpen their strategy is impacted by the paucity of talent, time, and analytical expertise. Successful retailers have recognized the power of outsourcing this capability to develop actionable insights.

## Case Study

WNS helped a leading US mattress company to develop an assortment of bed series at 'store group' level to maximize sales. WNS' solution included

- Grouping stores by sales (historical) using store characteristics, geographic and demographic factors, and competitive landscape
- Creating time-series models to forecast sales for each store group, for each bed series using bed assortment data, demographics, store characteristic, and competitive landscape
- Comparing future sales mix assortment with current assortment and suggesting changes.

Based upon the results obtained from WNS' study, the retailer is adjusting the planograms for its nation-wide stores.

## About WNS

WNS is a leading global business process outsourcing company. Deep industry and business process knowledge, a partnership approach, comprehensive service offering and a proven track record enables WNS to deliver business value to some of the leading companies in the world. WNS is passionate about building a market-leading company valued by our clients, employees, business partners, investors and communities. For more information, visit [www.wns.com](http://www.wns.com).

## About The Author

Himanshu Pal, a business development manager at WNS Research and Analytics Services, also supports MVI, a retail research and consulting firm supplying breakthrough retail insight, analysis, and thought leadership via its European office in London.

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