



The impact of modern retail on choice and innovation

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The Commission study on the EU retail sector

- **Motivation for the study:**

- ***Complaints*** at national and EU level argue that large retailers impose detrimental conditions on food suppliers (food manufacturers and farmers) and that this reduces their means to invest, thereby decreasing choice and innovation.
- ***Nobody really checked such negative long term effects*** of retailers' practices on consumer welfare

- **Objective of the study: deliver quantitative evidence**

- Provide facts about the evolution of concentration at the different levels of the supply chain
- Identify the possible (positive and negative) drivers of choice and innovation: concentration factors, imbalances, economic environment, socio-demographics, shop characteristics, shop opening, etc

- **Method of the study**

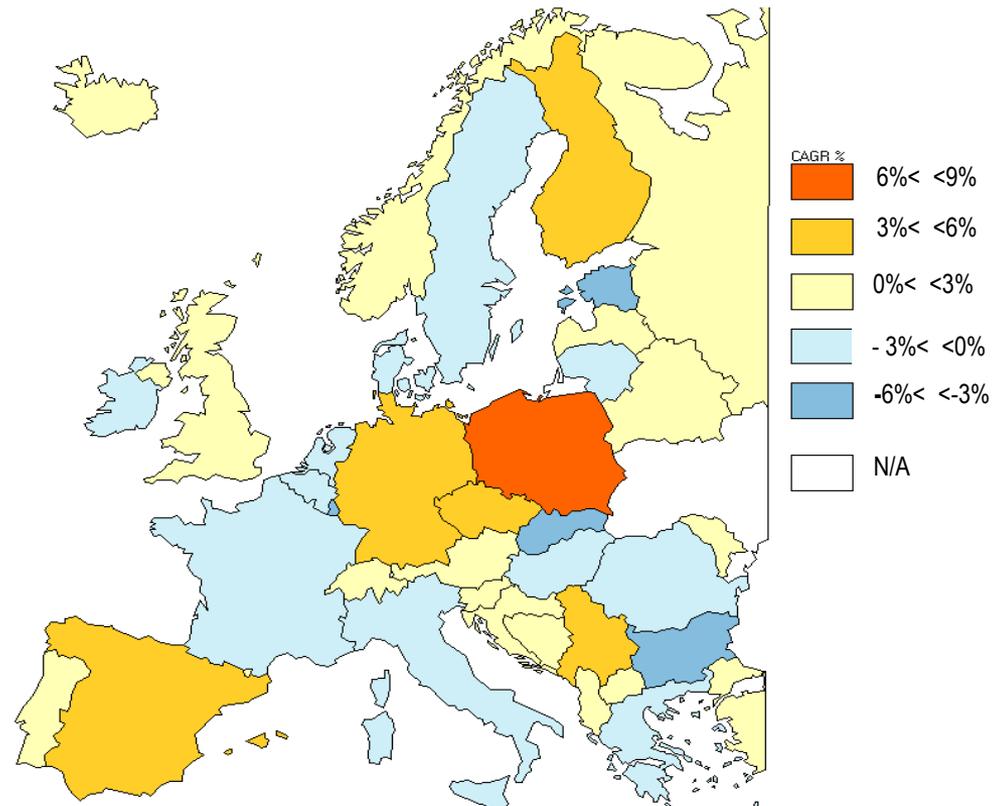
- Construction of a comprehensive database on a representative sample for the EU, containing more than 100 local areas in 7MS: various situations of areas and local retail concentration, various situations of supplier concentration and imbalances between retailers and suppliers at national level, etc
 - *Caveat: only moderately concentrated national retail markets were covered*
- Detailed data on choice and innovation on retailers' shelves, more than 100,000 different products, covering 23 product categories, 2004-2012;
- Econometric analysis: choice/innovation vs possible drivers

Main conclusions of the Commission Retail Study

(1) The concentration of modern retailers at wholesale level

- Retailer concentration (including both modern retailers and traditional retail shops) has increased overall, due to the increasing share of modern retail.
- Concentration of modern retail at national level has decreased in a majority of EU Member States (16 out of 26 reviewed).

Evolution of modern retail concentration across Europe
(at national level)

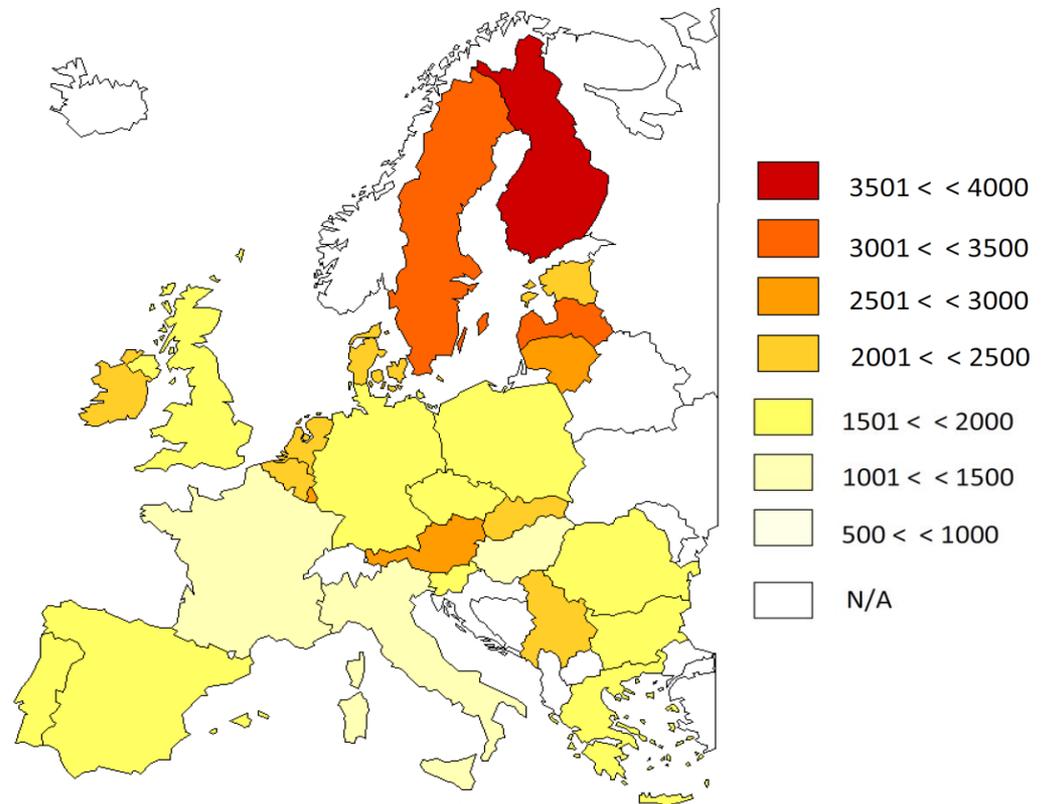


Main conclusions of the Commission Retail Study

(1) The concentration of modern retailers at wholesale level

- Most EU member states have low-moderately concentrated modern retail sectors (below 2500)
- The Nordic and Baltic countries have highly concentrated retail sectors (above 2500)

HHI of Modern Retail sector (2012)

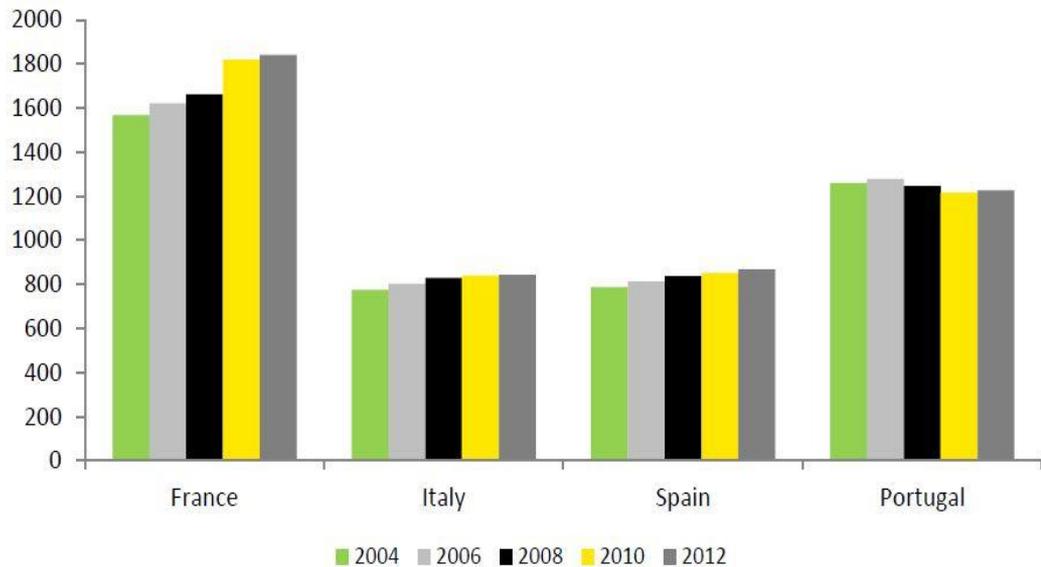


Sources: Planet Retail, EY analysis.

(1b) The situation of modern retail at retail level

- The types of modern retail vary between Member States
 - Proportion of discounters, supermakets and hypermarkets
 - The sales area of the different formats
- Retail concentration varies at local level

Figure 102: 2004-2012 data set: Average sales area of supermarkets per MS (national level) – in m² for 4 MS sample (source: EY analysis based on © Planet Retail)



(2) The concentration of suppliers at wholesale level

- The market structure of suppliers varies widely between product category and member state, from low concentration (green) in some to high concentration (red) in others.

Concentration of top 3 suppliers, by product and member state

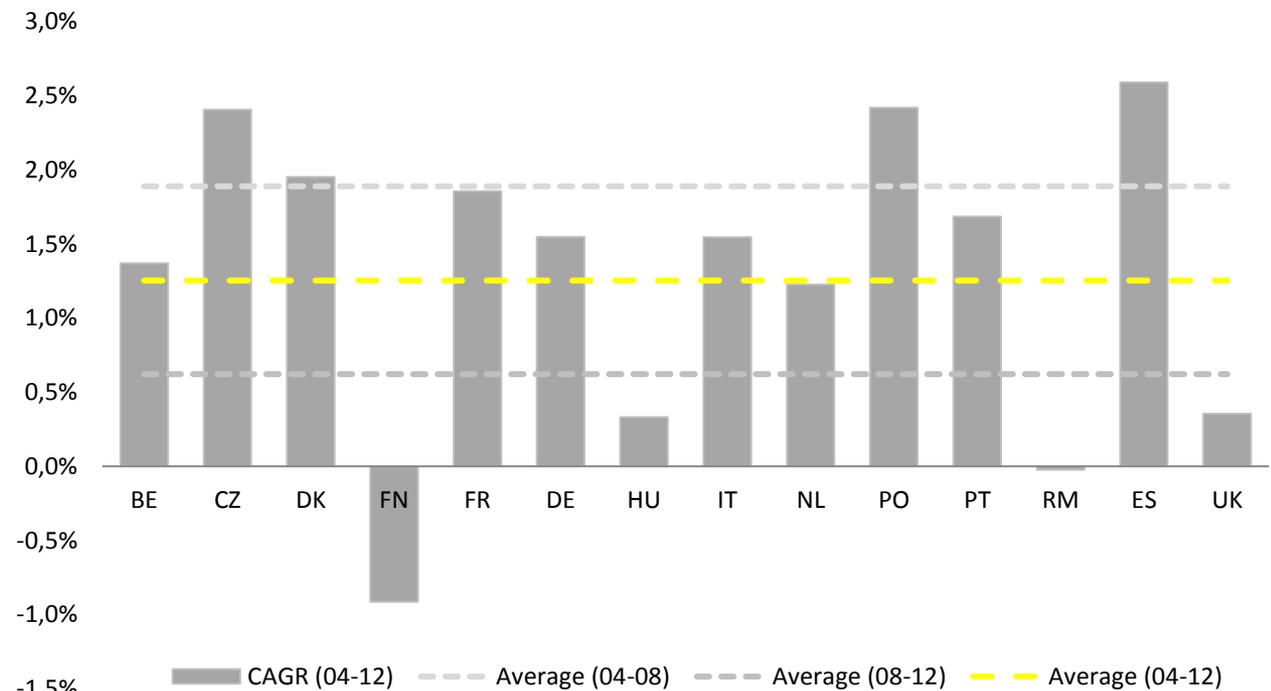
Product Category	FIN	DE	ROM	CZ	POL	NL	FR	HUN	BE	IT	POR	UK	SPA	GER	Average
Baby food	90%	91%	80%	74%	89%	79%	77%	74%	81%	83%	79%	64%	64%	78%	79%
Coffee	74%	64%	76%	62%	66%	73%	72%	70%	69%	56%	65%	59%	74%	42%	66%
Cereals	47%	57%	54%	71%	65%	47%	72%	42%	61%	83%	64%	56%	51%	44%	58%
Yoghurt	77%	81%	75%	43%	61%	41%	70%	50%	48%	60%	47%	55%	65%	34%	58%
Ice Cream	86%	57%	54%	42%	50%	78%	60%	62%	55%	22%	67%	44%	65%	47%	56%
Soft drinks	56%	59%	74%	49%	40%	40%	68%	49%	63%	52%	46%	59%	75%	41%	55%
Tea	70%	62%	59%	39%	55%	73%	56%	61%	47%	48%	54%	55%	46%	44%	55%
Chocolate	67%	53%	63%	71%	39%	47%	45%	49%	59%	61%	48%	67%	49%	45%	54%
Mineral water	70%	68%	52%	66%	45%	61%	72%	38%	58%	59%	31%	49%	31%	24%	52%
Biscuits	72%	60%	34%	81%	66%	42%	59%	60%	39%	51%	30%	38%	40%	41%	51%
Butter/margarine	67%	79%	48%	42%	29%	57%	40%	53%	47%	43%	56%	73%	32%	29%	50%
Frozen pizzas/starters	44%	48%	33%	55%	56%	75%	53%	66%	49%	54%	40%	39%	24%	53%	49%
Frozen ready cooked meals	58%	58%	86%	67%	43%	48%	29%	34%	56%	57%	40%	30%	37%	39%	49%
Savoury snacks	53%	56%	66%	49%	47%	50%	43%	43%	64%	31%	45%	44%	46%	40%	48%
Milk	83%	69%	45%	38%	54%	41%	42%	48%	26%	41%	51%	18%	38%	15%	44%
Fruit Juices	57%	58%	56%	46%	64%	36%	44%	43%	22%	50%	42%	30%	38%	24%	43%
Desserts	62%	72%	39%	33%	36%	49%	33%	43%	40%	56%	43%	25%	40%	21%	42%
Edible oil	34%	29%	51%	46%	58%	42%	48%	56%	35%	34%	47%	28%	26%	26%	40%
Frozen vegetables	44%	32%	33%	47%	45%	44%	35%	28%	41%	46%	31%	42%	27%	42%	38%
Cheese	72%	62%	50%	44%	40%	25%	42%	59%	19%	19%	43%	16%	29%	20%	38%
Canned vegetables	33%	18%	48%	47%	68%	53%	41%	19%	38%	14%	20%	43%	28%	24%	35%
Ham	53%	47%	34%	45%	56%	4%	28%	42%	24%	17%	42%	13%	27%	19%	32%
Bread	55%	43%	11%	22%	5%	13%	7%	2%	5%	7%	8%	47%	9%	20%	18%
Average	62%	58%	53%	51%	51%	49%	49%	47%	46%	45%	45%	43%	42%	35%	

Sources: Euromonitor Passport, EY analysis. Based on 2012 data.

(2) The concentration of suppliers at wholesale level

- However supplier concentration per member state (averaged across product categories) has **increased** over 2004-2012 in 12 of 14 MS analysed.
- Similarly, supplier concentration per product category (averaged across member states) has **increased** over 2004-2012 for almost all categories.

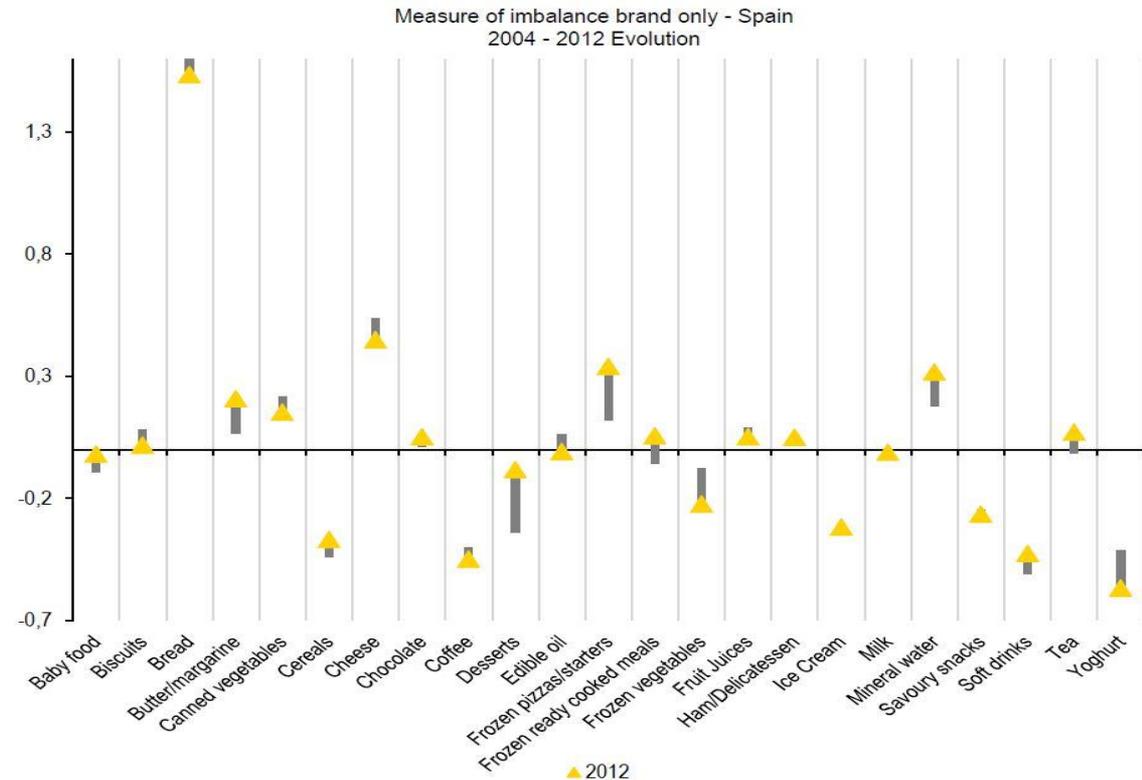
Evolution of supplier concentration (HHI brands only), 2004-2012



Source EY analysis based on Euromonitor International, CAGR of HHI

(2) Imbalances between retailers and suppliers

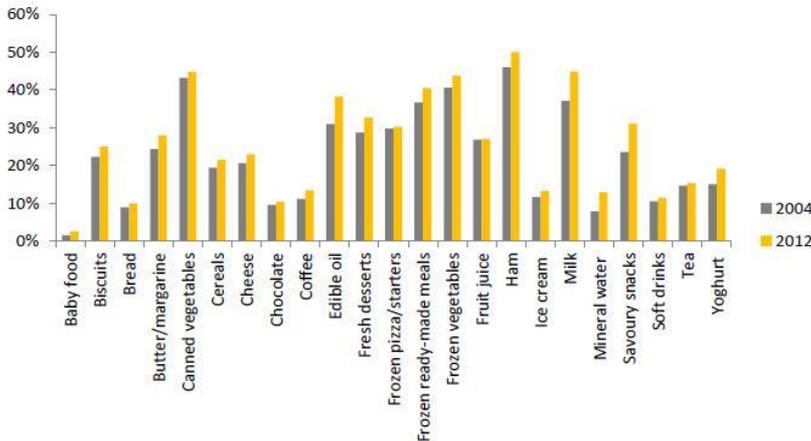
- The ratio of concentration of retailers and brand suppliers varies per state and per category
- The retail side of the market is not always the most concentrated side. In a sample of 14MS and 23 categories there were as many situations where suppliers were stronger than retailers.



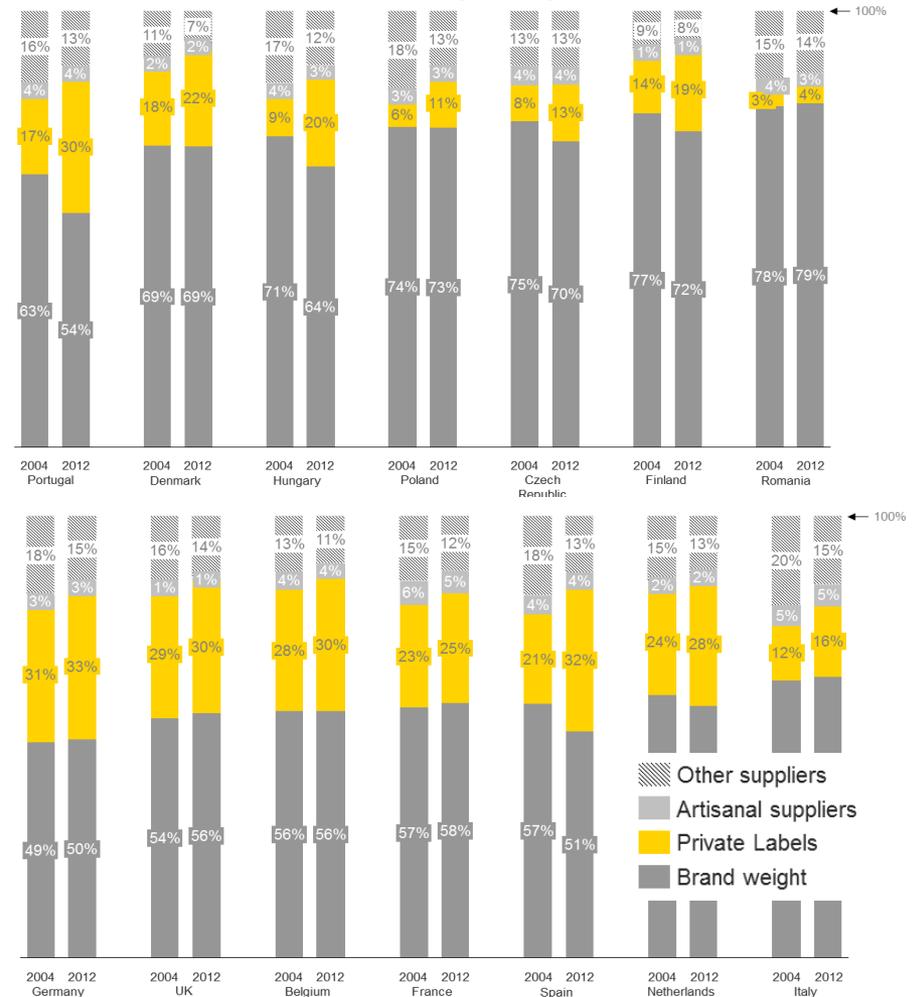
Private labels and brands

- Varied situations per member state and per category
- Brands continue to dominate in value of sales (50%-80%)

Figure 113: Percentage of private label sales share by product category - average across 14 MS (national level) (source: EY analysis based on © Euromonitor International)



Market share in edible grocery market

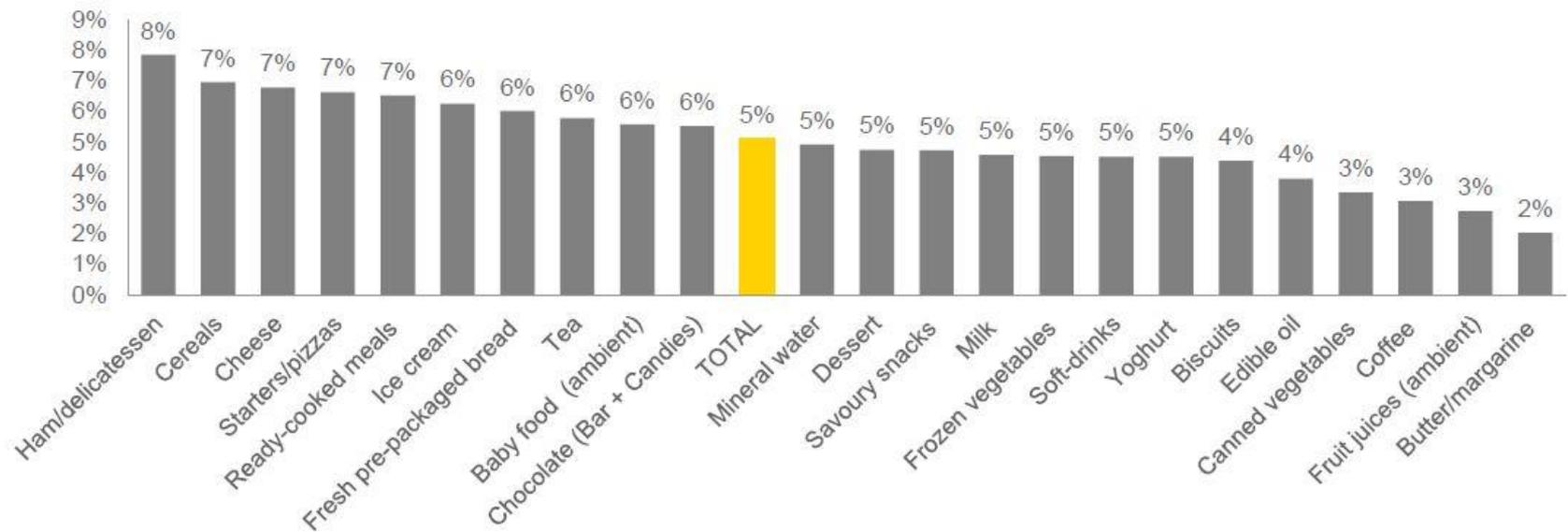


(3) Has choice on retailers' shop shelves declined in Europe?

- No!
- Choice in local retail shops increased over the last decade, both in terms of the number of different products and different brand suppliers, and in all product categories
- A slowdown could however be observed since 2008.

Per product category

Annual growth of total number of EAN by product category 2004-2012



(4) Has innovation on retailers' shop shelves declined in Europe?

Caveats before answering

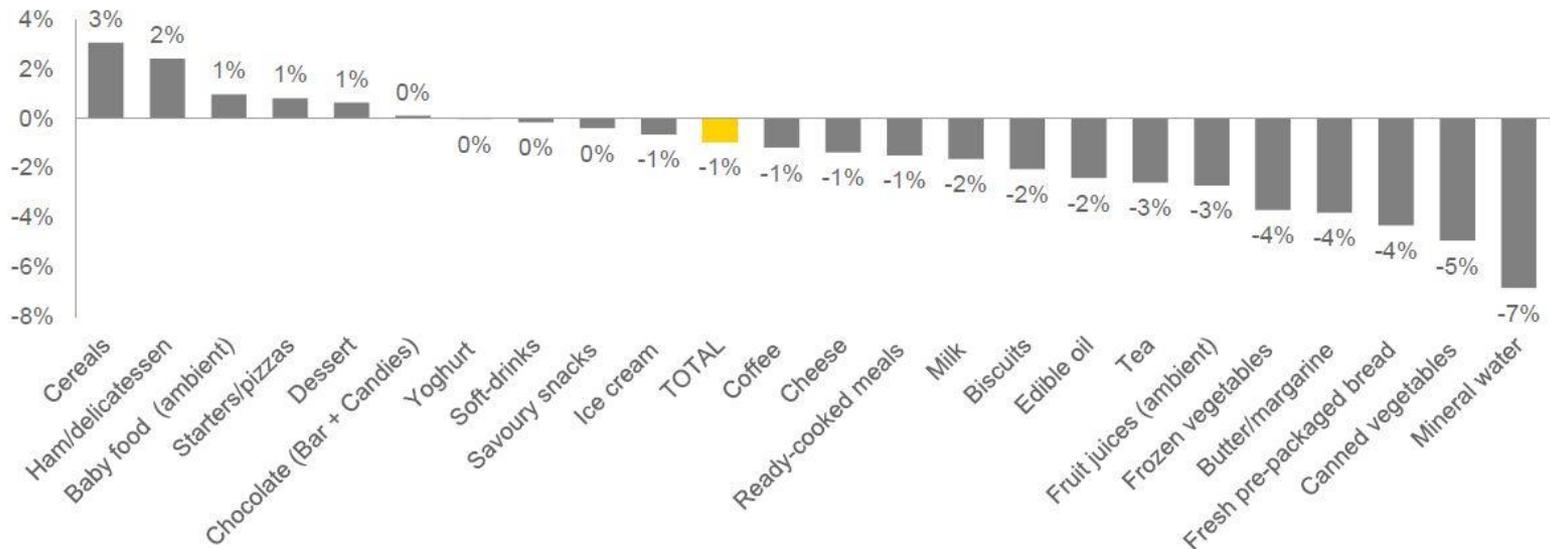
- No universally accepted definition of innovation
- Study measured different dimensions
 - The universe of new EAN codes (excl. Promotions)
 - Categories according to Mintel
 - Packaging innovations
 - Range extensions (e.g. new flavours)
 - New formulations (e.g. change of ingredient)
 - New products

(4) Has innovation on retailers' shop shelves declined in Europe?

- Yes!
- Innovation increased until 2008; since then a decline in the innovation rate can be observed for most product categories.

Per product category

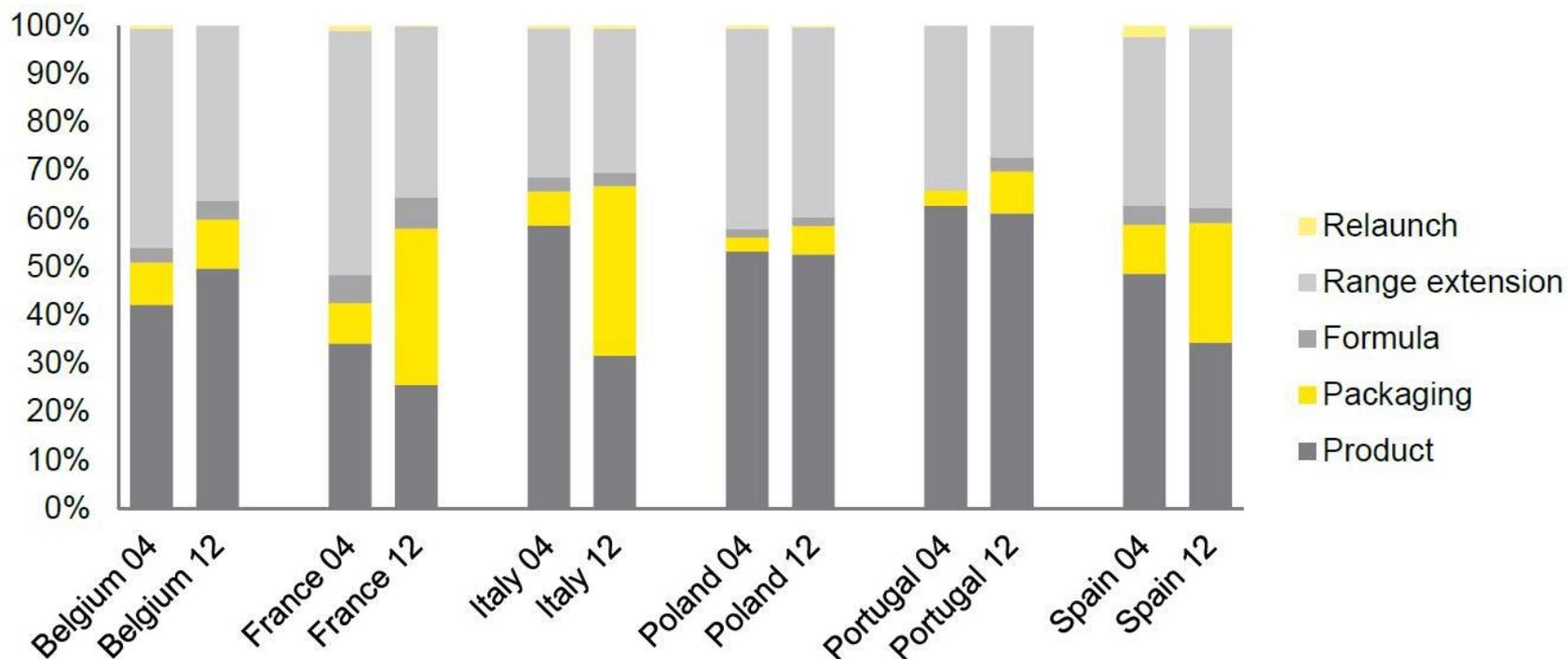
Annual growth in number of new EAN codes by product category 2004-2012



(4) Has innovation on retailers' shop shelves declined in Europe?

- Trend towards more packaging innovation

Figure 51 : 2004-2012 data set: Proportion of types of innovations by MS (local level)
(source: EY analysis based on © Mintel GNPD and © Nielsen Opus)



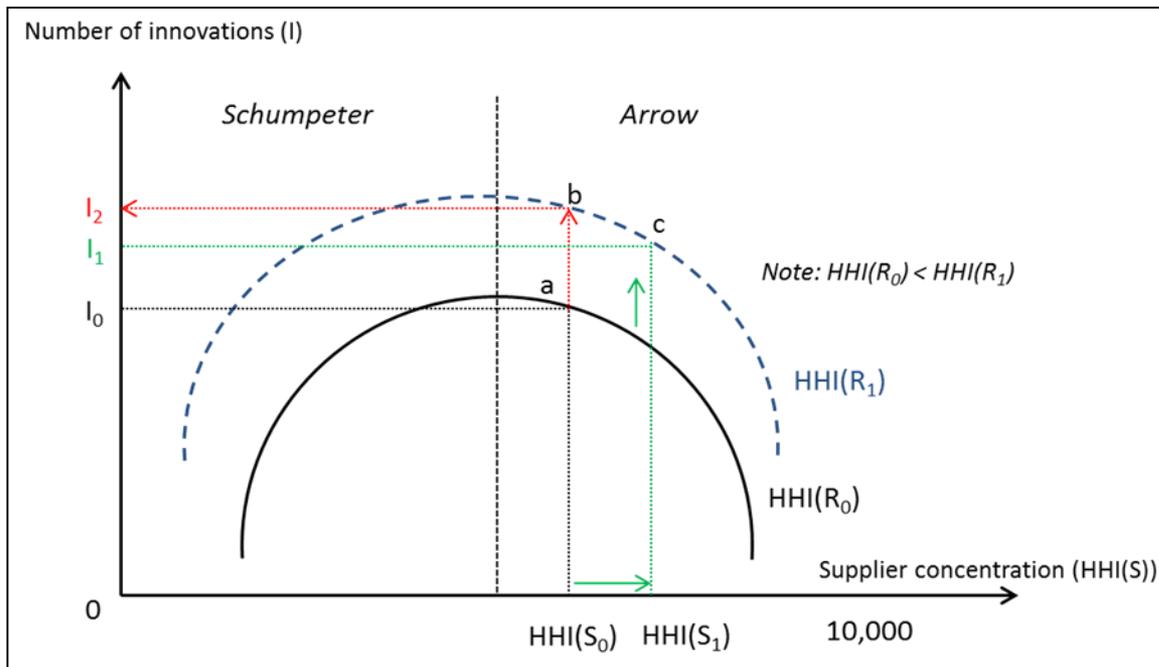
(5) What are the main likely drivers of choice and innovation?

(note: result of econometrics in moderately concentrated national retail markets)

- Positive drivers:
 - The **opening of a new shop** in local consumer shopping areas
 - The **expansion of modern retail outlets** in terms of floor space
 - The **size of the product category**
 - For innovation: An **increase in the relative wholesale concentration of retailers** vis-à-vis their suppliers
- Negative drivers:
 - The **economic environment** since 2008, measured by the local unemployment rates and local GDP/capita
 - For innovation: higher levels of **supplier (wholesale) concentration (at national level)**
 - For innovation: The proportion of **private labels** in the product assortment, measured as the proportion of PL products in EANs and new EANs by shop and product category.

Key result concerning retailers

Increased wholesale concentration of retailers relative to suppliers appears to be good for innovation in moderately concentrated national retail markets



Source: The Commission's modern retail study – A. Renckens/P. Chauve analysis

Are there competition issues?

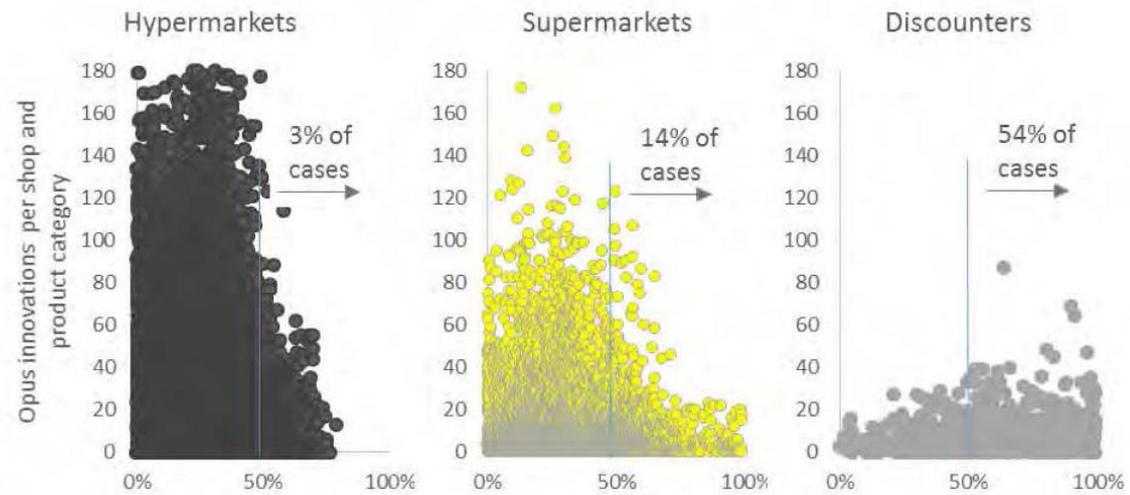
- Is there a problem in highly concentrated national retail markets?
 - To be investigated by the relevant national authorities
- Are private labels a problem for innovation?
 - To be developed (see after)
- Retailers in buying alliances may actually not pass on benefits (e.g. lower prices) when they do not face competition downstream
 - Italian case: Centrale Italiana
 - Norwegian case: Norgesgruppen/ICA

How do private label products impact on choice and innovation?

(note: in moderately concentrated retail markets)

- Graphical analysis of the **relationship between choice/innovation and private label penetration** suggested a non-linear relationship exists, distinct from the linear relationships found for other drivers. This motivated a refinement to the analysis concerning the specification of the relationship between PL share and choice/innovation.
- Including the square of private label share in the regression suggests there is a **significant negative non-linear relationship between innovation and PL penetration** (decrease is larger the higher the share of PLs).
- No significant relationship with choice however.

Innovation and private label share



Source: Figure 154 from Modern Retail Study

Possible explanations why PL penetration is associated with less innovation (*follow-up Study*)

- *Assortment effect theory*: PL products may be less innovative than brands by nature, and replacing brands with PLs on the shop shelf therefore leads to a less innovative range of products;
- *Consumer choice theory*: the study results may be driven by consumer choices and retailers may be simply giving consumers what they demand. Alternatively, consumers may not easily switch between shops, giving retailers little incentive to maintain an innovative product offer;
- *Crowding-out effect theory*: increased PL penetration may reduce brands' incentives to innovate, e.g. because they cannot get the scale required to make innovation profitable, or because retailers use PLs to engage in practices such as marketing copycat products that reduce brand incentives to introduce innovation.
- *Missing piece theory*: the PL variable used in the study may capture the effect of an unexplained variable not included in dataset, such as variation in stocking policy at store-level that is not measured by retailer format.

What's your view?

*Thank
You
For
Your
Attention!*



Useful links

- **DG Competition study**, "*The economic impact of modern retail on choice and innovation in the EU food sector*" (October 2014):
http://ec.europa.eu/competition/sectors/agriculture/retail_study_report_en.pdf
- **European Central Bank**, "*Retail market structure and consumer prices in the Euro Area*" (December 2014): <http://www.ecb.europa.eu/pub/pdf/scpwps/ecbwp1744.en.pdf>
- See also **European Central Bank**, "*Within- and cross-country price dispersion in the Euro Area*" (November 2014):
<http://www.ecb.europa.eu/pub/pdf/scpwps/ecbwp1742.en.pdf>

European Central Bank work on market structure and prices

The European Central Bank has carried out a project on consumer prices (as part of its work to understand inflation mechanisms).

They have published several studies using a comprehensive AC Nielsen scanner dataset covering 9 member States across 45 food product categories over 2009-2011. The studies look at differences in price levels across the Euro Area and their drivers.



After controlling for income levels, VAT, unemployment, population density and business cycle, the studies find significant impacts of concentration and competition on prices:

- **Downstream retail competition (i.e. lower local retail concentration) is associated with lower prices for the end consumer**
- **Higher retail concentration in the procurement market (including buyer groups) is associated with lower prices for the end consumer (welfare-enhancing).**
- **Concentration of suppliers has a large impact on price differentials across EU countries – lower concentration of suppliers is associated with lower prices.**