Retailing Beyond Borders

NEW RETAIL! New markets, Partnerships & Business models

Rabobank

Foreword

Dear participant, 18 January 2019

We would like to thank you for your presence at the congress today. We trust that the presentations and discussions have fully energised you to go out, take the opportunities and deal with the challenges in the retail sector.

The 'Anton Dreesmann Leerstoel voor Retailmarketing' Foundation - supported by a group of leading retailers in the Netherlands - has chosen Rabobank as its partner to host and co-organise its annual congress. The partnership started in 2011 and has been prolonged several times since then. We appreciate the opportunity to share our knowledge and views on the retail sector with you and hope to further strengthen our relationships.

The subject of today´s 'Retailing Beyond Borders' congress, was 'NEW RETAIL! New markets, Partnerships & Business models', a key theme for the retail sector.

We have written a report on the congress theme, in close cooperation with Frank Quix of Q&A Consultancy. The key points of the report are:

- market growth will be a limited driver for the sector going forward; retailers must focus on gaining market share in an increasingly competitive market; this becomes more difficult and requires new strategies
- the traditional value chain changes into a value wheel with different players gaining access to the consumer; the value wheel offers new opportunities for retailers via new partnerships
- not all retailers will profit from the value wheel; a distinctive formula and cooperation capabilities are key.

The report is based on a combination of desk research, an online survey among Dutch retail executives and discussions with various retail executives.

Like many retailers in their respective markets, Rabobank strives to be the leader in the Dutch banking market. We are a knowledge-driven bank, serving a wide range of corporate customers active in all sectors in the Netherlands. Our industry analysts cover continuously all relevant sectors in the Netherlands, including food retail and non-food retail. We have a wide portfolio of banking products, sector knowledge and experience in the retail sector.

Rabobank is dedicated in supporting the strategy of retailers. Rapidly changing market circumstances ask for a partner that knows your business.

We look forward to welcoming you again at next year's event here at Rabobank.

Kind regards,

Jos Voss
Sector specialist non-food retail

Jeroen Wortman
Sector banker non-food retail

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Sector specialist non-food retail

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MANAGEMENT SUMMARY

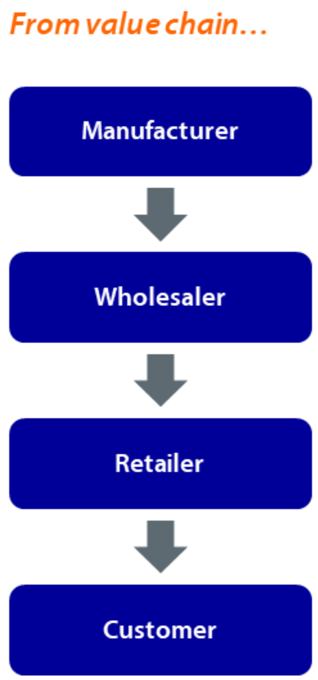
Retailers must focus on getting a bigger piece of the cake and this requires new strategies

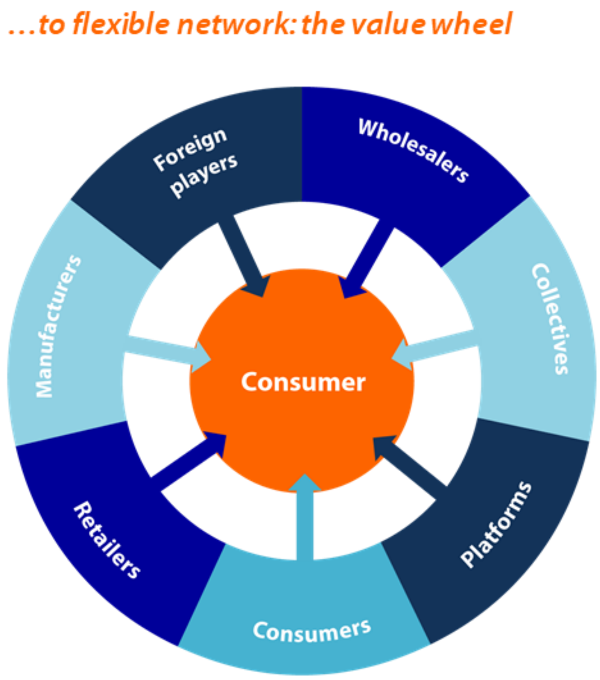
Although growth is slowing down, there is still a quite broad based growth of private consumption in the Netherlands and other (European) countries, which is, of course, positive for the retail sector. However, in the medium to long term market growth will be modest at best (around the rate of inflation). This expectation has not only a macro-economic foundation (economic risk, historical economic swings), but there are also structural market developments that will depress growth. To name a few: ageing of population (older people tend to buy less), moving from product ownership to availability and the increasing number of one person households. In addition: consumer expectations become higher and higher and competition is heating up from various angles. This combination of higher consumer expectations and increasing competition leads to a market standard that is continuously moving up. To use a metaphor: more competitors are fighting for a piece of the cake that is only growing modestly and it becomes more difficult to get a piece since consumer expectations are constantly increasing. If the cake is not growing (very much), you must get a bigger piece. This becomes more difficult and requires new strategies.

Traditional value chain becomes a value wheel, offering various new opportunities for growth

In the traditional value chain (producer-wholesaler-retailer-consumer) the retailer is the single point of access to the consumer. This traditional value chain is changing since other supply chain partners (e.g. producers/brand owners) are trying to get direct access to the consumer and new players enter the retail arena from, for example, the leisure and publishing sectors. Technological developments and changing consumer expectations are supportive for these players in getting a position in the retail sector.

This leads to a value wheel with the consumer in the heart of the model and multiple ways to reach the consumer. This value wheel can be a threat for retailers (more players grab a part of the market), but this threat can be turned into an opportunity via new partnerships with new and existing players, giving access to new markets, new products/services and new business models and leading to improvements of the retail operation, the retail formula and the customer journey.





In our vision, these new partnerships can support various business goals for the retailer:

- *Profit from the benefits of international expansion, with a lower risk profile.* Together with online platforms, international expansion becomes more feasible and less risky. The retailer can also take a stake in an international retailer in order to profit from the benefits of international expansion and as a stepping stone for cooperation
- *Improve/expand the quality of the retail formula and the product/service offering.* Opportunities include: category management via cooperation with other retailers, designing a new and better customer journey by combining the strengths of two retailers and finding new partners to increase the consumer offering
- *Grow and optimise the portfolio of touchpoints with consumers.* Partnerships with 'unusual suspects' like consumer collectives offer opportunities to broaden the number of touchpoints with consumers. Joining forces with other retailers, wholesalers and producers/brand owners offers opportunities to optimise stock levels and stock availability
- *Help partners in realising their objectives and build new business models.* Retailers can help brand owners, wholesalers and communities of consumers to achieve their goals and objectives. This opens the way to new business models
- *Grow from retailer to (online) platform.* Opportunities include: supporting C2C platforms by adding 'security and confidence' and growing from category leader to category platform.

Retailers who see the opportunities of the 'value wheel' and act accordingly will profit and be rewarded with a larger piece of the cake.

Not everyone will profit; retailers have to bring something extra to the table

We see two Key Success Factors for profiting from the opportunities of the value wheel.

First, the retailer has to be top of mind for the partners in the value wheel. This implies that the retail formula has to be distinctive on at least one of five value attributes:

(i) special Product, based on unicity and a vertically integrated model
(ii) Price proposition or perception
(iii) Service proposition, based on expertise of staff
(iv) Access to a wide consumer base via multiple touch points
(v) Experience, based on store environment.

Also smaller retailers can get a distinctive value proposition, based on e.g. a niche offering, customer knowledge or exceptional service.

The second Key Success Factor regards the cooperation capabilities. The retailers must be prepared to see former 'enemies' like producers/brand owners and competitors as possible cooperation partners. Furthermore, they must have the (cooperation) capabilities to turn these opportunities into partnerships. In our vision, the retail sector has some serious way to go on this road towards cooperation. According to our online survey, retail executives are more positive on their cooperation capabilities.

In addition to these two KSFs, it is important that retailers are prepared to experiment and not be afraid to fail.

Not all retailers will score well on the previously mentioned KSFs (formula, cooperation). They need new impulses coming from new management, new ownerships and/or new staff. Fresh blood from outside the retail sector can be supportive.

The value wheel contains many valuable opportunities and these opportunities will rise to the surface. The 'only' thing retailers have to do is grab these opportunities!

1 INTRODUCTION

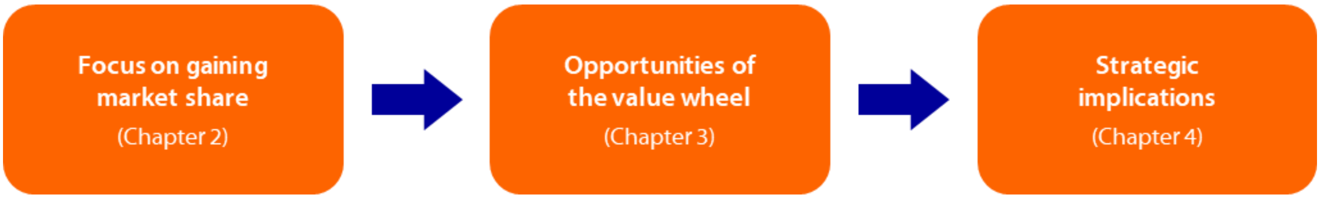
The quick and fundamental changes of the retail sector are more important for the future than the swings in the economy. Economic growth will at best be a limited driver for the sector while the structural changes will be quite disruptive.

One of these fundamental changes is the end of the traditional value chain supplier-wholesaler-retailer-customer. The retailer is no longer the 'single point of supply' for the customer. Various other players like suppliers, (online) platforms and collectives have gained direct access to the customers and they will increase in their efforts going forward. Is this a threat for the sector or can this threat be turned into an opportunity? This line of thinking has inspired us to write a report with the 'value wheel' - as successor to the traditional value chain - as its central theme. In our opinion this value wheel contains many opportunities for the retail sector to 're-invent retail ' and find new markets, partnerships and business models.

In this report we will elaborate on three key messages:

- Market growth will be a limited driver for the sector going forward; retailers must focus on gaining market share in an increasingly competitive environment; this becomes more difficult and requires new strategies
- The traditional value chain changes into a value wheel with different players gaining access to the consumer; the value wheel offers new opportunities for retailers via new partnerships
- Not all retailers will profit from the value wheel; a distinctive formula and cooperation capabilities are key.

This report is based on a combination of desk research, an online survey among Dutch retail executives and discussions with various executives of Dutch retailers. We have summarised our findings in three blocks.

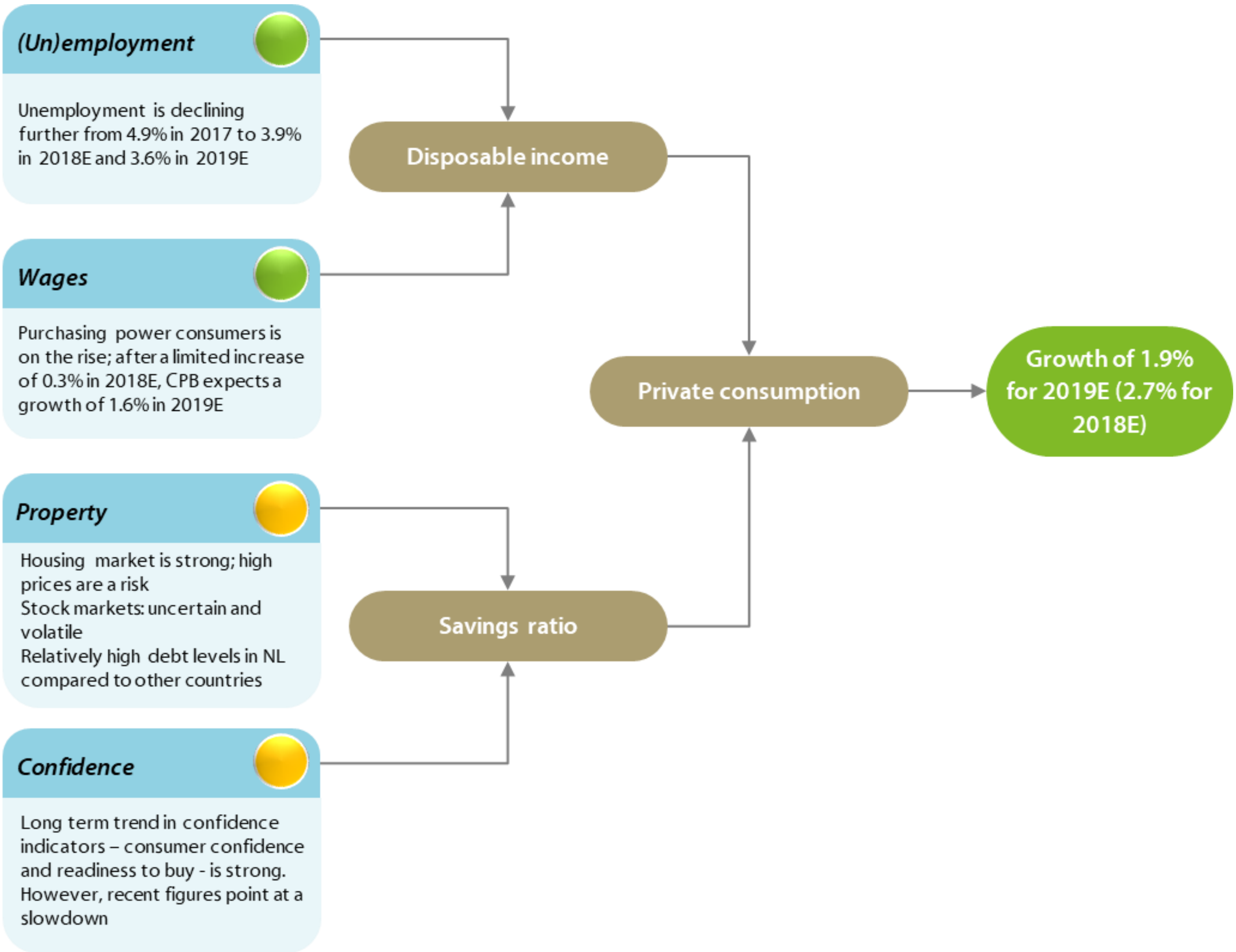


2 IF THE CAKE DOES NOT BECOME MUCH LARGER, GET A BIGGER PIECE

2.1 The economy gives limited support to market growth

Although growth is slowing down, we still see a further growth of private consumption in 2019 and 2020. Private consumption is the part of GDP that is the most important for the retail sector. This expected growth is quite broad based with all four engines of private consumption contributing: higher employment, increasing procurement power of consumers, favourable housing market and still high consumer confidence.

Figure 1: Estimated 2019 private consumption in the Netherlands



Source: Rabobank, Dutch statistical office CBS, Dutch bureau for Economic Policy Analysis CPB
Note: Traffic signal (red, yellow, green) indicate the prospects for the various parts

We see private consumption growing in other European countries too. This is of course positive for the retail sector. However, in the medium to long term, we expect that the growth of the market will be modest (around the rate of inflation) and that this will not be a growth driver for the sector. This expectation is not only based on economic clouds on the horizon (Brexit, possible trade war because of increasing import tariffs, financial and political situations in some European countries), the various risks that threaten future growth (including the high financial leverage of Dutch households, uncertainties on interest rates and pensions and the geo-political situation) and economic logic and history (what goes up must come down: after years of growth there will always be years of decline). Apart from these economic issues, we see some structural changes affecting the growth potential.

2.2 Some structural changes will depress market growth

The retail sector is changing fundamentally because of demographic changes, increasing consumer expectations (driven by and enabled by technology) and increasing competition. These structural factors will depress market growth in various ways. Here are a few examples:

- The population is ageing and older people tend to buy fewer products (they already have all the products they need) but spend more on services (healthcare, assistance for housekeeping or maintenance of house and garden)
- People see that they do not have to own all the products they need. Availability is more important than ownership. This trend is driven by various factors including economic considerations (e.g. electric drills are used for a limited time only during their lifecycle), financial motives (ownership requires upfront investments) and sustainability (increasing the lifetime of the products which is positive for the environment). All in all, other business models (rent, sharing, pay for use) are positive for consumers but will depress demand and market growth
- There is a growth in the number of one person households. For these households, costs of living and food are relatively high which will depress their spending power in other categories like fashion, consumer electronics and personal care.

Consumer expectations become higher and higher, driven by ongoing technological developments, and competition is heating up from various angles. This has multiple effects. Firstly, price is often used as a competitive weapon. The lower price becomes the norm and all retailers have to comply, leading to a downward trend in pricing and pressure on margins. Secondly, in order to comply with consumer expectations, retailers continuously have to invest in technological developments (e.g. Artificial Intelligence, voice recognition, robots, drones) leading to higher capex requirements, higher operational costs and possibly pressure on margins. Finally, the combination of higher consumer expectations and increasing competition leads to a market standard that is continuously rising. 'Excellent service' becomes the standard and is less valued and rewarded. Consequently, retailers have to find new ways to 'excel'. For example: same day delivery used to be a premium service with extra charges. As more and more retailers offer this service and offer this 'for free', the premium service becomes 'standard' and 'free' becomes the norm.

Competition from international online players like Amazon and Alibaba is a point to watch for the Dutch retail sector in particular. We often hear and see the question 'Will Amazon come to the Netherlands?' This is a quite odd question since Amazon is already here. According to Twinkle, Amazon has sales of EUR 230m in NL and is the #7 online player in the market. This sales level is generated with relatively little effort and delivery takes place from Germany and the UK since Amazon still has no warehousing in NL. Until now Dutch players have some advantages over Amazon like free delivery and shorter delivery times. If Amazon pays a little more attention to the Dutch market, these advantages can disappear quickly. A comparable threat is coming from Alibaba. The Chinese giant is planning to build a new DC in Liège (Belgium) which will lead to an improvement of its customer proposition (shorter delivery time).

2.3 Focus on gaining market share, not on market growth

The situation can be summarised by this metaphor: more competitors are fighting for a piece of the cake that is only growing modestly and it becomes more difficult to get a piece since customer expectations are constantly increasing. If the cake is not growing (very much), you must get a bigger piece. This becomes more difficult and requires new strategies. Head to head competition on price is a dead end street. This leads to a race to the bottom and the fight for the lowest price can be won by only a few players. It is a smarter strategy to find new ways to reach new and existing consumers and to get a larger piece of the cake. New partnerships and business models provide various opportunities in this direction.

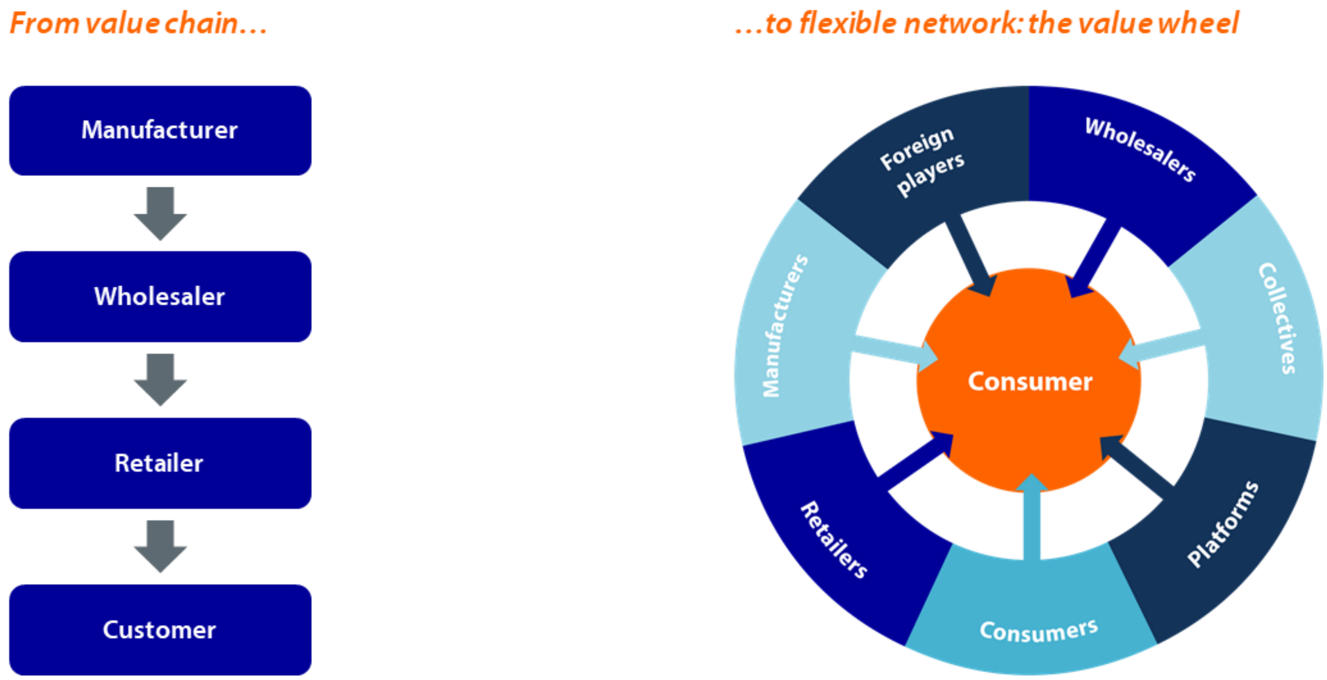
3 FROM VALUE CHAIN TO VALUE WHEEL: NEW OPPORUNITIES FOR GROWTH

3.1 Evolution of the value chain

3.1.1 In the traditional value chain, the retailer is the single point of access to the consumer

The traditional value chain is pretty simple and straightforward. Producers/brand owners supply the products (possibly via wholesalers) to retailers. The wholesalers take care of various tasks including bulk breaking (break up large volumes into smaller volumes for the various retailers), logistics (from producer to the DC of the retailer) and financing. The retailer sells the product to the consumer. For the retailer, this traditional supply chain is relatively favourable as they are the 'single point of access' to the consumer. The 'monopoly' gives them a competitive edge since the other supply chain partners are dependent on them in order to reach the end-user and to get information on customer preferences and customer behaviour.

Figure 2: The value chain becomes a flexible value wheel



Source: Rabobank, Q&A Consultancy

3.1.2 However, there are various points of access: the value wheel

Due to various factors, the traditional value chain has changed. Other partners in the supply chain such as producers, brand owners and wholesalers try to get direct access to consumers in order to build their brands and obtain valuable consumer insights. Consumers become more and more internationally oriented and have an open mind towards the offerings of international retailers. New players enter the retail arena, coming from e.g. the leisure or publishing sector, in order to leverage their consumer base.

This new playing field is enabled by two developments. Firstly, technology makes it possible to reach consumers from each and every desired direction. In the 'old days' a bricks-and-mortar store base was necessary in order to get access to consumers. Now there are all sorts of channels (including internet, mobile, social media) and they are available for everyone, with no or limited borders. Secondly, consumers love the fact that they have more choice and for them the consumer relevance of their 'supply partners' is key and their supply chain position is totally irrelevant. This is illustrated by the global list of most valuable brands, drafted by Brand Finance. The top 15 of this list contains three retailers (Amazon, Walmart, Alibaba) with Amazon and Alibaba being technology companies, active in (mainly) online retail and partly serving as a platform for others. 5 out of the top 7 run platforms as a (part of their) business model.

Figure 3: Top 15 most valuable brands, world wide

#			*Type of company*	*Brand value 2018 in USD million*
1		Amazon	Retailer	150,811
2		Apple	Manufacturer/brand owner	146,311
3		Google	IT company	120,911
4		Samsung	Manufacturer/brand owner	92,289
5		Facebook	Media company	89,684
6		AT&T	Telecom provider	82,422
7		Microsoft	IT company	81,163
8		Verizon	Telecom provider	62,826
9		Walmart	Retailer	61,840
10		ICBC	Bank	59,189
11		China Construction Bank	Bank	56,781
12		Alibaba	Retailer	54,921
13		China Mobile	Telecom provider	53,226
14		Wells Fargo	Bank	44,098
15		Mercedes-Benz	Manufacturer/Brand owner	43,930

Source: Brand Finance

We see the value chain changing into a value wheel, with the consumer at the heart of the model. There are now multiple ways to reach the consumer. Each of the players in the wheel can reach the consumer directly or can form alliances with partners to do this together.

3.2 Will retailers profit or suffer from the value wheel?

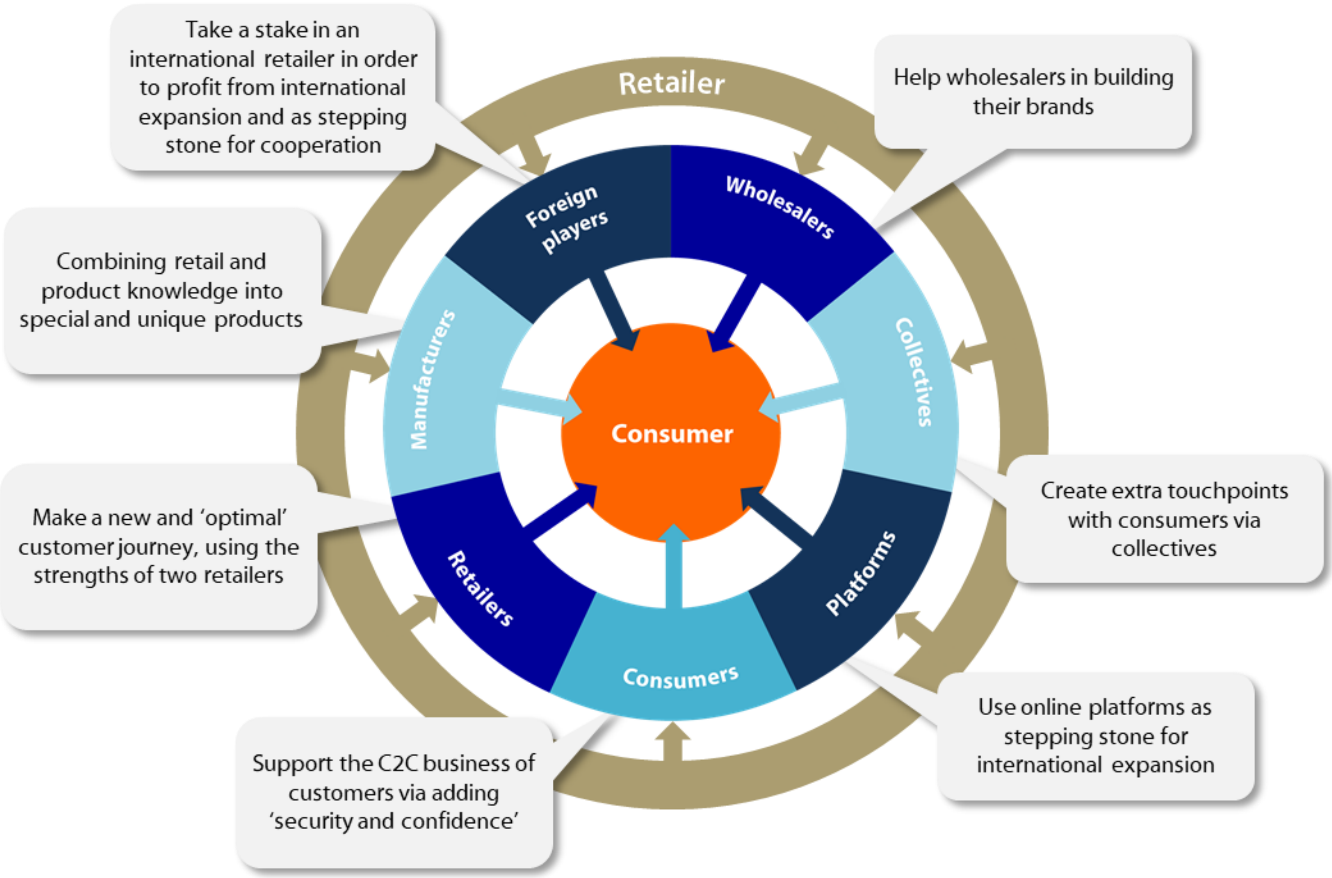
There are two ways to look at the value wheel. It can be seen as a threat since other players eat away market share. A more positive way, is to consider it as an opportunity. Through partnerships with others it is possible to find new opportunities for growth (new markets, new products/services, new business models) and to improve the quality of the retail operation, the retail formula and the customer journey.

These new partnerships, within the framework of the value wheel, can contribute to the following business goals for retailers:

- Profit from the benefits of international expansion, with a lower risk profile
- Improve/expand the quality of the retail formula and the product/service offering
- Grow and optimise the portfolio of touchpoints with consumers
- Help partners in realising their objectives and build new business models
- Grow from retailer to platform.

We will discuss these goals and opportunities in the next chapters and illustrate them with examples.

Figure 4: Examples business opportunities from value wheel



Source: Rabobank, Q&A Consultancy

3.3 Profit from the benefits of international expansion, with a lower risk profile

3.3.1 Together with online platforms, (international) expansion becomes more feasible

International expansion is a logical option for retailers who want to extend their market reach. This is especially applicable for retailers who have a Dutch home market since the Netherlands is a small and mature country with an increasingly competitive retail environment. Figure 6 shows that many foreign countries are more attractive from the perspective of growth of private consumption.

In the traditional way of international expansion - entering new countries alone and on a greenfield basis - the strategy is no walk in the park and requires much time, management effort and money. The retail brand has to be built in the new country, a dense bricks-and-mortar store base is necessary, the retail formula often has to be adapted to local consumer preferences and market circumstances (depressing the efficiency and therefore the profitability) and solutions have to be found for getting access to various resources such as suppliers, staff, management and logistics.

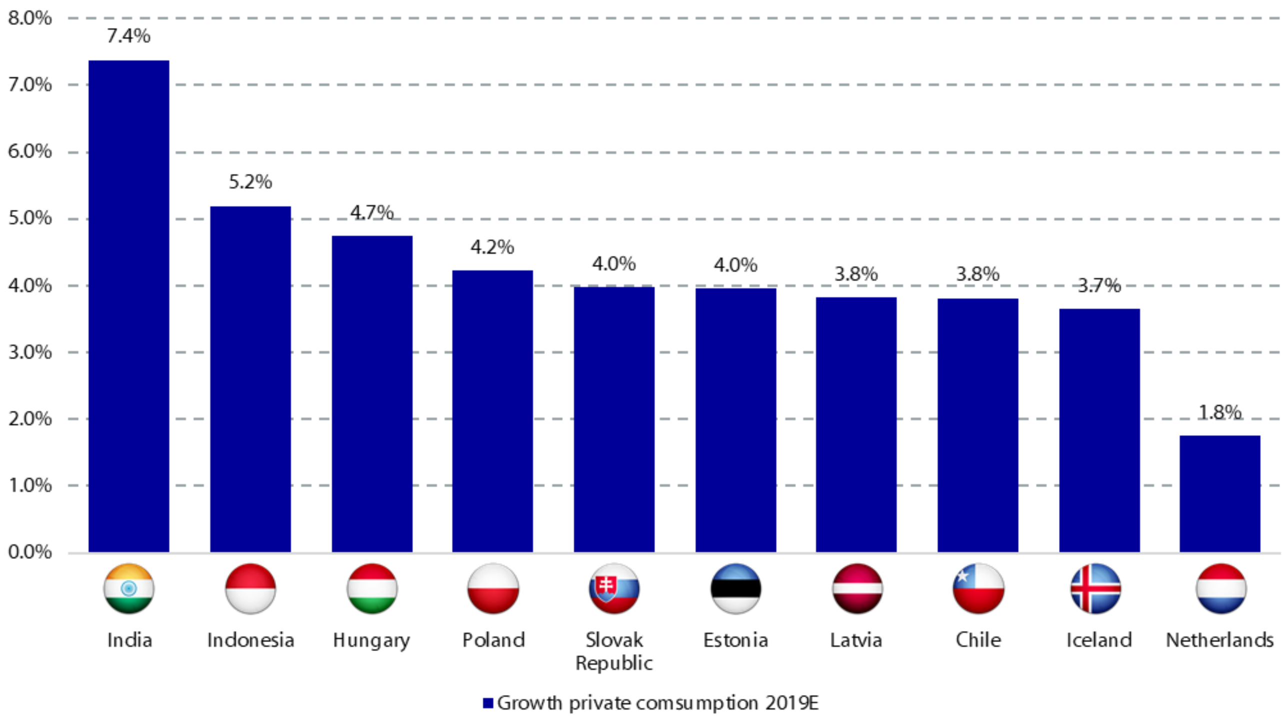
International expansion via online platforms is easier in many ways. The retailer can profit from the consumer relevance of the platform, no investments are needed in a store network or in own online operations and the platform takes care of the necessary resources. Of course there is a price tag attached to the cooperation as the online platform takes a part of the margin. The other side of this coin is that the retailer can save on capex, marketing spend and operational costs and that the risks of the international expansion are lower. Online market places become more and more important. According to Internet Retailer, consumers spent USD 1.55 trillion in the top 75 online market places in 2017, a growth of more than 30% compared to 2016. Figure 5 contains the top 5 online market places with three players from China and two from the US. In China almost 75% of all online sales was realised by the two most dominant platform owners in 2017.

Figure 5: Top 5 online market place

		GMV 2017 in USD bn	***Country***	
Taobao		428	China	
Tmall		340	China	
Amazon		155	US	
E-Bay		87	US	
JD.com		87	China	

Source: Internet Retailer
Note: GMV is the Gross Merchandise Value, the total value of goods sold in the market place. Sales of the marketplaces' own products are not included in this ranking

Figure 6: Prospects growth private consumption



Source: Estimates OECD, November 2018

Via online platforms retailers can access countries that are attractive but difficult to penetrate on a greenfield basis. We will illustrate this statement using the Global Retail Development Index (GDRI) of AT Kearney. This research and consultancy firm makes a yearly ranking of countries that are most attractive for international expansion by retailers. The ranking is based on a combination of four factors: market attractiveness, country risk, market saturation and time pressure, resulting in a GDRI index. The top 10 contains two very large countries (China and India) and large countries are attractive for retailers because of the large market potential and the fact that the costs of international expansion can be earned back more easily via the huge customer base. However, entering these large and complex markets without the help of partners is virtually impossible and cooperation with an online platform offers a way out. This is why retailers like Costco, Aldi and H&M have chosen to enter China via Tmall, the online platform of Alibaba. Burberry cooperates with online platform Farfetch to sell its merchandise in 150 countries. Starbucks and Alibaba have closed a deal with both online and offline dimensions. Starbucks' merchandise is sold via Tmall and Taobao, platforms of Alibaba. Starbucks opens outlets in Hema, the Chinese supermarket chain of Alibaba. Walmart uses the Japanese online platform Rakuten to strengthen its position in Japan. Both retailers have opened a new, dual branded online shop for this purpose: Walmart Rakuten Ichiba Store.

Figure 7: Top 10 most attractive countries for international expansion

#			GRDI score	Population in millions
1		India	71.7	1,329
2		China	70.4	1,378
3		Malaysia	60.9	31
4		Turkey	59.8	80
5		United Arab Emirates	59.4	9
6		Vietnam	56.1	93
7		Morocco	56.1	35
8		Indonesia	55.9	259
9		Peru	54.0	32
10		Colombia	53.6	49

Source: Report AT Kearney

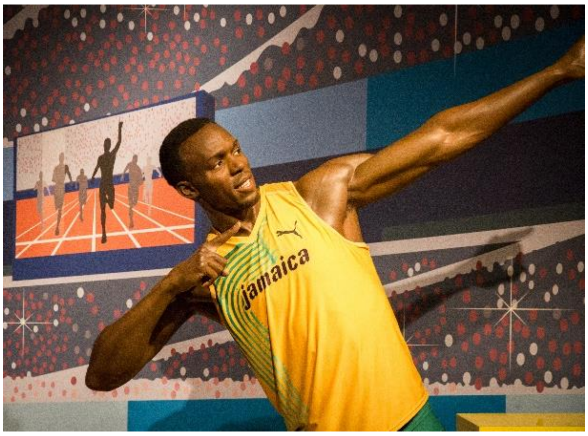
3.3.2 Take a stake in an international retailer

There is another option to profit from the benefits of international expansion without bearing the full risks of an autonomous international expansion strategy: taking a stake in an international retailer. CECONOMY (owner of MediaMarkt and Saturn) has a stake of around 24% in another international consumer electronics retailer, Fnac Darty. The main strategic consideration for CECONOMY was Fnac Darty's strong position in France, one of the few major European markets where CECONOMY is not active. Via Fnac Darty CECONOMY gets financial exposure in France. Taking a stake can become more than a financial investment. It can become a stepping stone for further cooperation. After buying the stake in 2017, CECONOMY and Fnac Darty announced in 2018 plans for cooperation in a European Retail Alliance. This new platform aims at cooperation in various business areas including private label sourcing, innovation and data analytics. Recently however, CECONOMY announced that it will put the cooperation on hold in order to focus on various operational issues.

Taking a stake in another retailer and building a cooperation model on top of it, is a quite defensive move and time will tell if it will be successful. Another example apparently turned out to be not successful. In 2001, UK based DIY retailer Kingfisher bought a 25% stake in Hornbach with a twofold strategic rationale: (i) getting an indirect interest in the German DIY market (ii) defensive move against US giant Home Depot who could have used Hornbach as a stepping stone for European expansion. However, in 2014 Kingfisher sold its stake in Hornbach and found other ways to enter the German market. Now, Kingfisher has around 20 stores in Germany.

3.4 Improve/expand the retail formula, product/service offering and customer journey

3.4.1 Move from generalist to specialist can be very rewarding



In sports, it is well known that it is more rewarding to be a specialist than a generalist. Take athletics as an example. Usain Bolt is a world famous specialist on the 100 metres. In 2009 he set the world record at 9.58 seconds. His 2018 income is estimated by Forbes to be USD 31m and he has more than 18 million followers on Facebook. Kevin Mayer from France is the world champion decathlon (athletic event consisting of ten different athletic disciplines). His best time on the 100 metres is 10.55 seconds, around 1 second slower than Usain Bolt. He has around 133,000 followers on Facebook and although we have no income estimate, it is probably much, much lower than Usain Bolt's. Both athletes have talent and have to work hard, but it obviously pays to be a specialist.

Back to the retail sector, we see many retailers playing the decathlon: doing every retail discipline themselves. It is probably better to focus on a limited number of disciplines in which they can excel truly and to seek cooperation on other aspects. There are more and less far-reaching forms of cooperation. A relatively simple form is summarised by us as 'category management'. More far-reaching is the model in which players design together the best customer journey, based on the strengths of each of these players. We will elaborate on both models.

3.4.2 Category management: outsource certain product categories

Category management is well known in the food retail sector. Supermarkets give the responsibility for a certain product category to a supplier: the category captain. This captain is responsible for the composition of the assortment in their category. Supermarkets are quite complex stores with many products in many product categories. Category management helps retailers in managing this complexity. Also in non-food we see complexity increasing as the boundaries between the non-food sectors (fashion, DIY, living etc.) are blurring and retailers have to handle more and more product categories. Therefore, category management is making inroads into the non-food sector. We see various examples. Department store de Bijenkorf outsources the books category to specialist AKO, part of publisher Audax. Household store Blokker offers 50,000 book titles via its website. Composition of the assortment and the fulfilment is handled by specialist store Paagman. Albert Heijn cooperates closely with the specialist V&D Concepthouse for its assortment of school supplies.

3.4.3 Design the best customer journey together

A more far-reaching cooperation model is the development of a new customer journey, based on the strengths of the partners. In such a model, the customer journey is analysed and for each step the strengths and weaknesses of the cooperation partners are assessed. Based on this analysis and assessments, it is decided which of the partners will execute which part of the new customer journey. Consequently, processes, procedures and IT systems will be combined in order to build this new customer journey.

We see the cooperation between consumer electronics retailer BCC and online retailer Wehkamp as a good example of this model. In this cooperation, both partners use their strengths to play a certain role in the new customer journey. BCC has expertise in the consumer electronics category and a physical store network. The strengths of Wehkamp are in online, logistics (its new, highly automated and efficient DC in Zwolle) and in the service proposition towards customers. Based on these complementary strengths a new customer journey is designed, built and implemented. The cooperation has multiple stages and phases. In a next phase, new combinations of capabilities, knowledge and expertise can be made in order to further improve the customer journey. We can imagine for example that the financing proposition of Wehkamp will be made available to BCC customers, that BCC outsources its fine-meshed logistics to the homes of consumers to Wehkamp and that Wehkamp uses the stores, knowledge and staff of BCC for special and 'private' workshops for its customers on themes like Internet of Things (IoT) and smart homes.

3.4.4 Find new partners in order to improve/expand the retail formula and product offering

The value wheel contains numerous opportunities to improve/expand the retail formula or the product offering.

Finding new suppliers and adding products to the assortment

Convenience store Primera saw some interesting developments in the market for mobile phone devices and subscriptions. The specialised telecom stores focus more on the larger cities and the high end of the market with the more expensive devices and subscriptions. Smaller cities and the 'standard' assortment (cheaper devices, often with prepaid packages) are not attractive enough for brand owners. Kijkshop was active in the 'low end' part of the market that needs less service/advice, but this retailer was forced to close all its stores. Primera partnered with various suppliers of mobile devices, prepaid packages and accessories in order to increase its product offering. The partnership has started with a pilot in a limited number of stores and will be rolled out further after proven success. For the suppliers the large and dense store network of Primera (> 500 stores, also in smaller cities) is attractive as this is complementary to its existing sales channels.

Leverage customer bases and product offerings

Energy supplier Essent has opened shops-in-shops in 36 of the 70 BCC stores in the Netherlands. In these shops-in-shops Essent customers can get advice on e.g. energy savings and new energy contracts. The cooperation can be extended towards other product categories like solar panels and smart home solutions. This shop-in-shop cooperation goes beyond the traditional shops-in-shops like in fashion, where department store owners offer parts of their retail space to fashion brands. In this case, we see multiple benefits for both partners. BCC gets access to the customer base of Essent and can align its product (and service) offering with the advice of Essent. For Essent, the shops-in-shops open opportunities to deliver added value to its customers (not only advice, but also corresponding product and service offerings; one-stop-shop) in a commodity (energy) market.

Adding technology to the retail formula

Technology plays an important role in the improvement of the customer journey and therefore in the quality of the retail formula. Retailers can seek cooperation with technology providers in order to keep their formulas up-to-date in this respect. An example is the cooperation between Intersport and Alibaba. In addition to the existing online shop on Alibaba's Tmall platform, the sport retailer and the technology giant developed a co-branded store in Beijing. This store is loaded with technological features that will make the customer journey more convenient, including interactive shop-windows, smart mirrors based on artificial intelligence that can provide (product) information to customers and virtual shelves offering an 'endless' assortment. Ocado is another example. Ocado is not only an online supermarket, but the company also sells its technology platform to other retailers who want to move from the traditional 'bricks-based' model to an omnichannel model. Kroger (US), ICA (Sweden) and Casino (France) have joined forces with Ocado to obtain the technology platform.

Combining retail and product knowledge into special and unique products

IKEA and Sonos (specialist in home sound systems) have set up a cooperation in order to integrate the knowledge and technology of Sonos into the product offering of IKEA. This cooperation has benefits for both the retailer and the brand owner. Sonos gets access to the preferences of the customer base of IKEA (and can align its product offering with these preferences) and obtains a huge platform for its products. IKEA can make better products for its customers and can use the strength of the Sonos brand name for its marketing ('Sonos technology inside').

Stretch the scope of the formula via new partners

Retailers can stretch the scope of their formula from B2C to B2B or C2C via new partnerships. The Dutch local book store Van der Velde, with seven stores active in the northern part of the Netherlands, has found a new market for its books: the public libraries. New book titles are delivered directly to the libraries who get a newer assortment in this way, which is more attractive for its members. Libraries traditionally buy their books via a central service organisation, but this takes 3-4 months to get new titles on the shelves. We can imagine that this example will be followed by more book stores and libraries. A C2C example is IKEA. The furniture retailer offers its customer in Sydney the opportunity to hand in their used IKEA furniture in exchange for store vouchers. IKEA assesses the products against predefined quality criteria. In this way, IKEA can get a share of the already existing second hand market for IKEA furniture. The company partners with its customers (who are now both customer and supplier) and adds confidence to the products via its brand name and quality checks. As a bonus, IKEA strengthens its CSR image.

3.5 Grow and optimise the portfolio of touchpoints with consumers

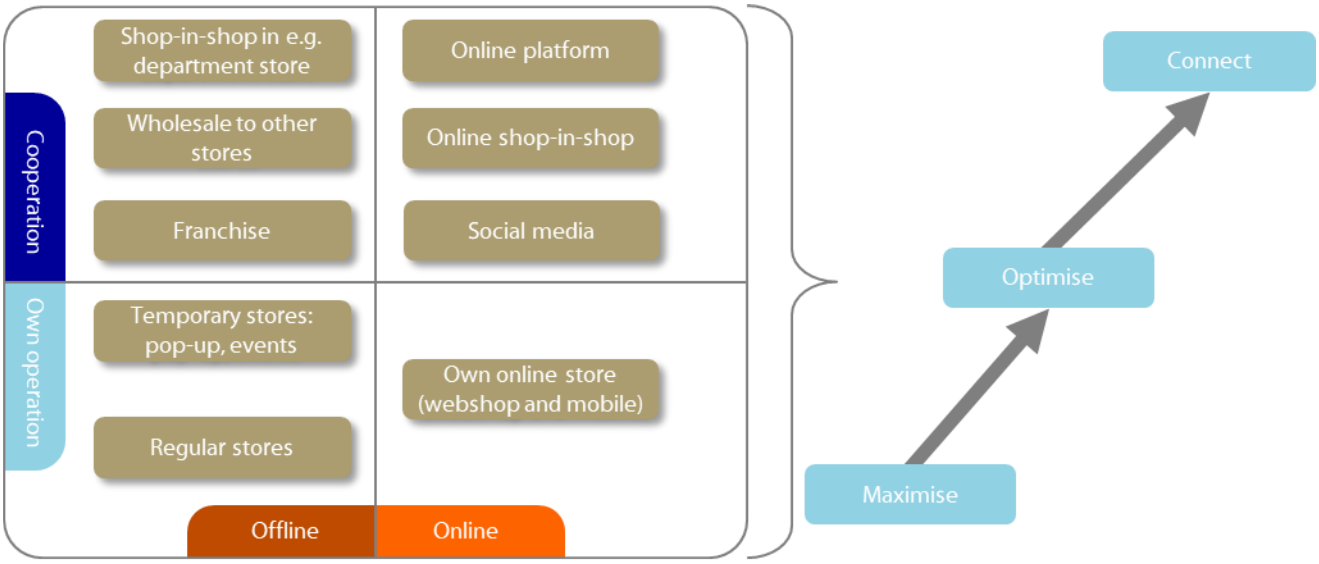
Retailers and brand owners usually sell their products via a combination of touchpoints with consumers, both online and offline and both company owned and owned by third parties. The composition of this combination differs per retailer and depends on various factors.

In countries where it is difficult to do business on your own (for example, because of political and cultural circumstances) it can be wise to team up with a local partner, acting as a master franchiser. For larger cities, own flagship stores are useful, although their profitability is perhaps below par due to the high rental levels, the huge investments in the store fittings and the staff that are necessary for such a store. These flagship stores play an important role in the brand building and the low financial contribution is therefore not much of an issue.

In smaller cities however, flagship stores are not rational and multi-brand stores or franchise stores are more suitable. A strong (international or local) online platform can be a valuable addition to the own webstore.

This combination of touchpoints has to be managed as a portfolio. In this management, we distinguish three phases: maximise, optimise, connect.

Figure 8: Portfolio of touchpoints: Maximise, Optimise, Connect



Source: Rabobank

In the first phase, maximise, new partnerships can play an important role

Figure 8 already contains a number of examples of partnerships. There are also partnerships possible with some 'unusual suspects'. In particular, 'collectives' can become an important source for new partnerships. Collectives are communities of people with the same interests, objectives and/or concerns. Dutch examples include: ANWB (Royal Dutch Touring Club; association of 4.4 million members with various interests in all kinds of mobility), KNVB (Dutch Football Association with 1.2 million members, playing football) and Consumentenbond (association of consumers; around 0.5 million members; acting as an organised interest group for their members and other consumers). These collectives offer retailers (and other providers of products and services) access to a huge customer base via a variety of communication channels including magazines, websites, newsletters, events and e-mails. Retailers can offer special products ('product only available for members') or special prices and discounts ('only for members'). They can also create extra touchpoints, together with the collectives. For example: webstore with the brand name of the collective, fully operated by the retailer. In this way, the retailer grows their portfolio of touchpoints.

In the optimisation phase of the portfolio, the retailer reviews the composition of the portfolio

In which parts do we have to grow? Which parts can be downsized in order to make room for new areas?

Connecting the portfolio is the final part in which the retailer removes all borders between the touchpoints in order to give the consumers an 'integrated shopping experience'

Consumers can easily switch and travel between all touchpoints. They can get inspired by a social media site of the retailer, touch and feel the product in a store (either company owned, franchise or shop-in-shop), order online via the Amazon platform and return to another store if the product does not meet expectations. Each and every touchpoint knows the customer and offers the same products, information and conditions.

Besides offering a more convenient customer journey, this 'connecting phase' can bring another benefit: stock optimisation. In many traditional value chains, high stock levels are a major issue. The key point of this issue is that each and every partner in the value chain (manufacturer, wholesaler, brand, retailer) makes their own decisions on the necessary stock levels. To make it worse, every individual retailer in the retail network of a certain country makes their own decisions, based on the expected behaviour of their own customers. The combination of all of these decisions leads to a sub-optimal (too high) stock level because every part of the chain takes only their own customers into account. If all the supply chain partners took the perspective 'How to service the total customer population with one combined stock', this would lead to lower total stock level. In this 'one stock concept' the 'optimal' total stock level is determined, based on various data regarding sales expectations, production and replenishment planning and lead times. This 'optimal total stock' is split between the various touchpoints of the retailer (and/or brand) and is available for all customers in a country. So the demand of a customer of store A can be fulfilled from the stock of store B or the online platform C or the central DC of the retailer (and/or the brand). If all the touchpoints are connected and operate with one integrated stock, many benefits can be reaped: lower stock, higher stock turnover, lower risk of obsolete stock, higher product availability for customers. However, implementation of this model is no walk in the park. Many issues have to be solved in order to build such a model, including connecting IT systems, sharing data and financial settlements.

A fully vertically integrated retailer can take the lead in the implementation of the mentioned 'one stock model'. In a model that is not (fully) vertically integrated, the wholesaler can take a leading role in this respect. The wholesaler is the linking pin between manufacturer/brand owner and retailer and can prove its added value in this way.

3.6 Help partners in realising their objectives and build new business models

Retailers can help other players in the value wheel to meet their goals and objectives. They can build new business models around this. In this way, competitors can become partners. We see various opportunities in this area.

Help brand owners to integrate forward

Many brand owners want to integrate forward towards retail for multiple reasons: (i) get direct access to information on customer preferences and buying behaviour (ii) capture extra margin (iii) build their brands.

Large brands like Apple, Nike and Adidas are perfectly capable of doing this on their own. Other brands can use the help of retailers. Brand development and retail are quite different ballgames, requiring different skills and capabilities. Retailers have these skills and capabilities and can leverage them to brand owners. The Dutch high-end fashion retailer Oger operates a mono-brand Corneliani store in Amsterdam for this Italian brand owner. The Dutch multi-brand shoe retailer Nelson exploits around 40 mono-brand stores for the Danish shoe brand Ecco.

The cooperation has benefits for the brand owner (using the retail skills and capabilities of the retailer instead of 'buying' them), but also for the (multi-brand) retailer: (i) access to extra customer information that can be leveraged to the multi-brand operation (ii) closer cooperation with the brand owner (iii) extra sales and margin.

Retailers can even build new business models around the concept of helping brand owners. Shops-in-shops are a well-known example and we see (smaller and larger) variations on this model. B8ta is a store for electronic gadgets that does not earn its money via selling products but via offering store space and staff to brands. STORY in New York is a retail concept that takes the point of view of a magazine, changes like a gallery and sells things like a store. That means that every four to eight weeks, STORY completely reinvents itself - from the design to the merchandise – with the goal of bringing to light a new theme, trend or issue. STORY cooperates with brand owners for building the theme, trend or issue and can derive its profits from two sources: the consumer (selling products) and the brand owner (selling 'space' in the 'magazine').

Help wholesalers building their brands

The traditional role of the wholesaler of unbundling large volumes of the brand owners into smaller volumes for individual retailers is under pressure. Both brand owners and retailers are increasing their scale and are able to do business directly, helped by internet and other communication technologies. For the logistics role, the wholesaler has to compete with specialised logistic service providers.

In order to counter the pressure in the supply chain, wholesalers are integrating backward to producer/brand owner via the development of what they call 'brands'. However, consumers perceive these 'brands' to be (private) labels in reality, with less brand value than real brands. The wholesaler can seek cooperation with its retailers to add value to these labels and lift them towards brands. Retailers can do so in various ways, e.g. by giving the labels a more prominent place on their virtual and/or physical shelves and building a brand experience around the products. We see the Dutch shirt producer/wholesaler Van Winkel Fashion as an example. Van Winkel offers various shirt brands to multi-brand fashion retailers, including Ledûb, John Miller and Blue Crane. The company offers a made-to-measure Ledûb shirt programme to consumers in cooperation with its dealers (retailers). Consumer and retailer can design a tailor-made shirt, using the website and (3D design) software of Van Winkel. In this way the value of the Ledûb brand is strengthened, both for the consumer and for the retailer.

Help communities of customers.

Retailers can help their communities of customers in various ways. Fulfilling their needs for inspiration and information is an example. Supermarket Jumbo has acquired the website 'Smulweb' that enables customers to share recipes, tips and advice on food. In this way, commodity products like food are enriched with information, thereby increasing their value for customers. Another way to help customers is to combine their buying power towards suppliers. Building a community of energy consumers and getting 'the best deal' for them from an energy supplier is an example. Retailers can also organise reversed auctions for their customers. The customers pre-order a 'special and exclusive' product displayed on the website of the retailer, e.g. a book or a work of art that is produced in a limited collection. The retailer orders the products at the supplier, based on the pre-orders of the customers. The customers have the perception of an 'exclusive and special deal' and the retailer has a risk-free business model as they only buy what has already been sold.

3.7 Grow from retailer to platform

Many retailers already sell their merchandise on platforms like Amazon, Zalando and bol.com, but there are opportunities to become a platform themselves.

Support C2C business of the customers

Customers like to trade with other customers (C2C) but like to avoid the risk of not getting paid or not getting the product.

A retailer can add 'security and confidence' to the C2C trade by building a trade platform. The platform adds value via various measures like the screening of advertisements, providing tips and information on 'safe trading' and letting the platform members share knowledge, reviews and experiences. The platform can also play a direct intermediary role between seller and buyer. Marktplaats (part of eBay) has a service called 'Gelijk Oversteken' ('Crossing roads at the same time'). Via this service, the buyer pays not directly to the seller but to a holding account of Marktplaats. The seller sends the product using a track-and-trace service. After confirmation of receipt by the buyer, the money is released from the holding account and transferred to the seller’s account.

Category leaders can become platforms

Via the Amazon platform consumers can buy IKEA products. Sellers are either IKEA themselves or third party traders trying to profit from pricing differences between countries, In our opinion, IKEA can build a platform by themselves, not only selling IKEA products (new and second hand) but also other products in the (broad) category 'home related products'. IKEA is top of mind for customers in this category and can leverage this consumer relevance towards a platform. Such an own platform has various advantages: (i) IKEA customers get a much wider choice (ii) IKEA gets sales and margin that is now captured by others like Amazon. We note that this option is not that straightforward and is not suitable for everyone. The retailer has to be absolutely top of mind in its category. In addition, it requires 'courage' since the retailer must be prepared to sell products of its competitors and view former 'enemies' as 'partners'.

3.8 Profit or suffer? It is a matter of choice!

Will the retailer profit or suffer from the 'value wheel'? In our opinion, this is a matter of choice. Retailers who do nothing will probably suffer as a part of their sales trickles away to other players in the wheel. To paraphrase a well-known saying: "If you always do what you have always done, you will get less than before". However, retailers who see the opportunities of the 'value wheel' and act accordingly will profit and be rewarded with a larger piece of the cake.

4 STRATEGIC IMPLICATIONS FOR THE SECTOR

4.1 Not everyone will profit; retailers have to bring something extra to the table

Although suffering or profiting from the value wheel is a matter of choice, not everyone will be able to make the more favourable choice. We see two Key Success Factors for retailers:

(i) The retail formula that has to be sufficiently distinctive from competition in order to become a preferred partner for other players in the value wheel

(ii) Capabilities in order to make cooperation with others work.

We will examine these two factors in more detail. Retailers with insufficient scores on these KSFs, need fresh impulses via new management, new staff and/or new owners.

4.2 Retailer has to become top of mind partner, based on 'something special'

The potential cooperation partners in the value wheel can choose from a wide variety of retailers. They will pick a retailer that is distinctive from other retailers since he can bring 'something special' that other cannot bring. This 'something special' has to be embedded in the retail formula and can be based on at least one of the five value attributes:

- A special product that cannot be offered by another, based on unicity and a vertically integrated model in which the retailer controls the supply chain
- Good price proposition or good price perception, based on scale and/or sourcing capabilities
- Service proposition, often based on the expertise of staff, that is recognised by consumers who are willing to pay for this service
- Access to a wide customer base via multiple touchpoints, both online and offline
- Stores that are appreciated by customers due to their high Experience character.

Figure 9: Examples of retailers being distinctive on the five value attributes

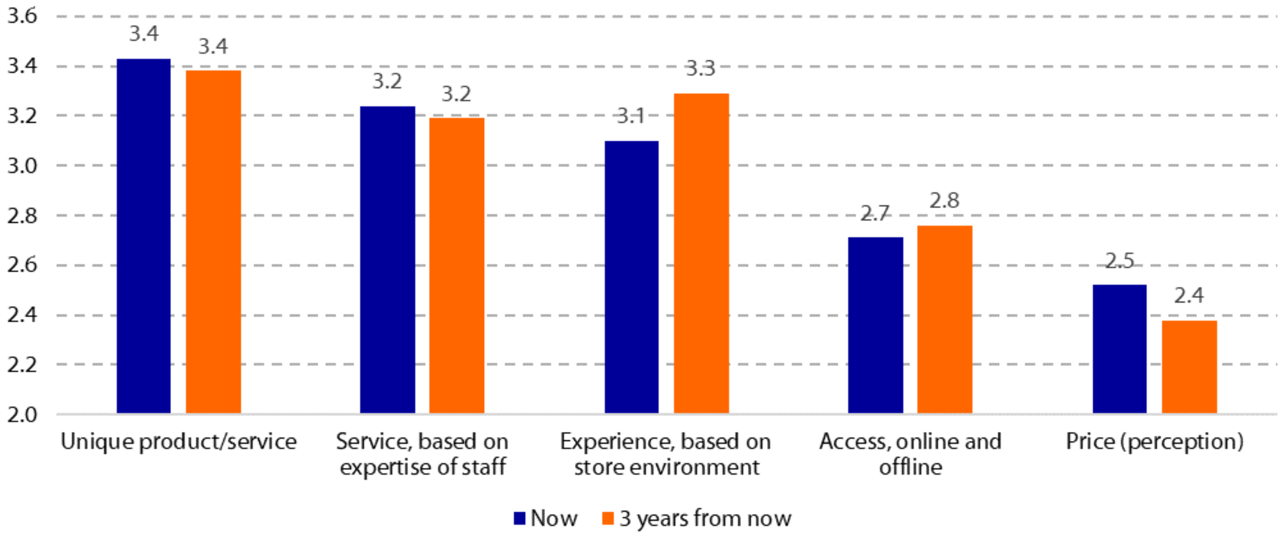
Unique product	RITUALS...	Rituals is a fully vertically integrated retailer with its own, unique products. The company makes its personal care products special by connecting them to 'stories' and 'rituals' that are rooted in the Asian culture and traditions.
Price (perception)	ACTION VERRASSEND VOLLEDIG, VERBAZEND VOORDELIG	Action is a non-food discounter with a strong price perception. The assortment is changing permanently. Customers know that what is now in store, can be sold out next week. This makes them 'greedy'.
Service, based on Expertise of staff		Apple uses its store and staff to provide service and information to its customers. In the Apple stores, people can learn about their Apple device and about all possible applications. In order to support these learning experiences, Apple stores offers workshops for people of all experience levels. In these workshops, customers can explore everything they can do on their Mac, iPad or iPhone.
Access	hunkemöller	Hunkemöller makes its products available via a wide portfolio of touch points including its international store network, own webshop and online platforms.
Experience, based on store environment	Globetrotter << NEUE HORIZONTE >>	Visiting the Globetrotter store in Cologne (specialised in outdoor equipment) is really entertaining. Visitors can try-out the products by really experiencing an outdoor activity. There is e.g. a climbing wall where the hiking shoes can be tested in a real-life environment. In the basement, there is a pool where customers can work with canoes and scuba dive equipment. Furthermore, Globetrotter offers a year-round agenda with events, theme days, readings and trainings. In the store, customers can explore the different areas and 'dwell time' is encouraged with cafés and a restaurant.

Source: Rabobank, based on model of Crawford and Matthews

Figure 9 contains some examples. Although these examples are bigger, international players, being distinctive is also possible for smaller players, e.g. retailers active in a niche or 'local heroes' who are strong in their market area based on a combination of a strong local brand, heritage, entrepreneurship, customer knowledge and excellent service. Via cooperation with online platforms these niche players or local heroes can get access to other markets. Their niche positions or strong local market positions make them attractive for online platforms.

Via an online survey, we asked (Dutch) retail executives to rank the five value attributes for their formula. The most important value attribute was given a '5' and the least important attribute a '1'. We asked them to make a ranking for the current situation ('now') and for the expected situation 3 years from now. The results are summarised in figure 10. It is remarkable that the 'Unique product/service' gets such a high score. In our opinion it becomes increasingly difficult to become and stay distinctive on this attribute since the market is very transparent (and transparency will increase still further) and products and services are available 'everywhere', both online and offline. Unique product and service offerings are only possible in market niches that are defendable for a limited period of time. We are positive on the high scores for Service and Experience. As explained in our 2017 report 'Working on Transition', these attributes provide the best opportunities for physical stores. Also the relatively low score for Price is positive as the battle for the lowest price can be won by only a few players.

Figure 10: Ranking of the five value attributes



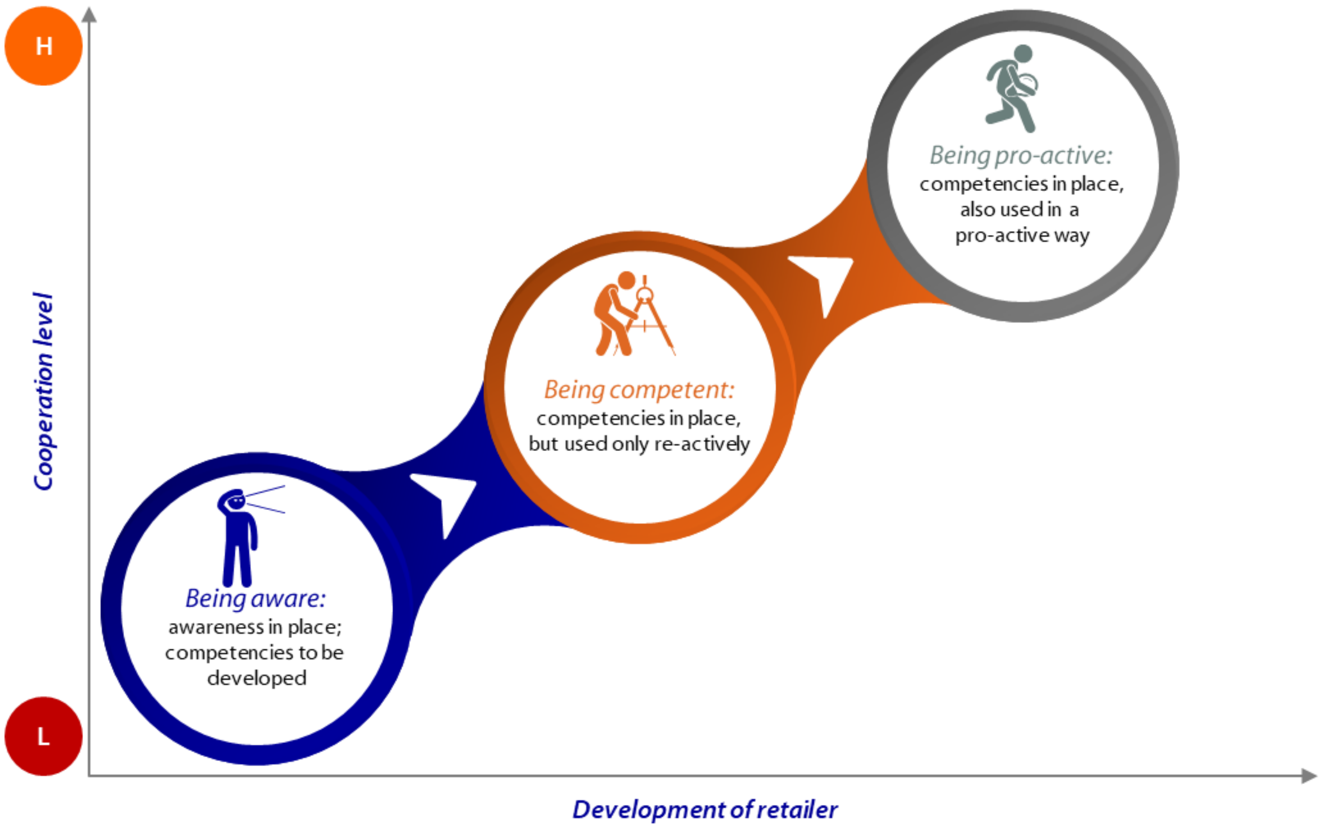
Source: Rabobank and Q&A Consultancy, based on online survey among retailers

4.3 Cooperation capabilities

Cooperation is the 'magic word' in the exploitation of the opportunities of the value wheel. Therefore, retailers need capabilities on cooperation in order to capture opportunities. In the development of these opportunities, we recognise three stages.

In the first stage *'Being aware'* the retailer recognises the opportunities of cooperation and feels the need to develop capabilities in this area. In *'Being competent'* the retailer is able to cooperate. This ability has two dimensions: external and internal. The external dimension has to do with managing the relationship with the cooperation partner. This includes: looking at 'shared interests' instead of 'own interest', real understanding of the claims, concerns and issues of the partner, ability to grant a 'fair share' of the results to the partner instead of hunting for the 'maximum share'. There is also an internal dimension since cooperation can also have consequences for the internal organisation. If, for example, two retailers combine their customer journeys into one new customer journey, like in the previously mentioned cooperation between BCC and Wehkamp, this has consequences for the operations of the retailer. The retailer must be able to understand and manage these consequences. In the *'Being pro-active'* phase, the retailer is constantly looking for new and unexpected opportunities for cooperation and is always prepared to use their competencies in order to capture these opportunities.

Figure 11: Three stages of development of cooperation

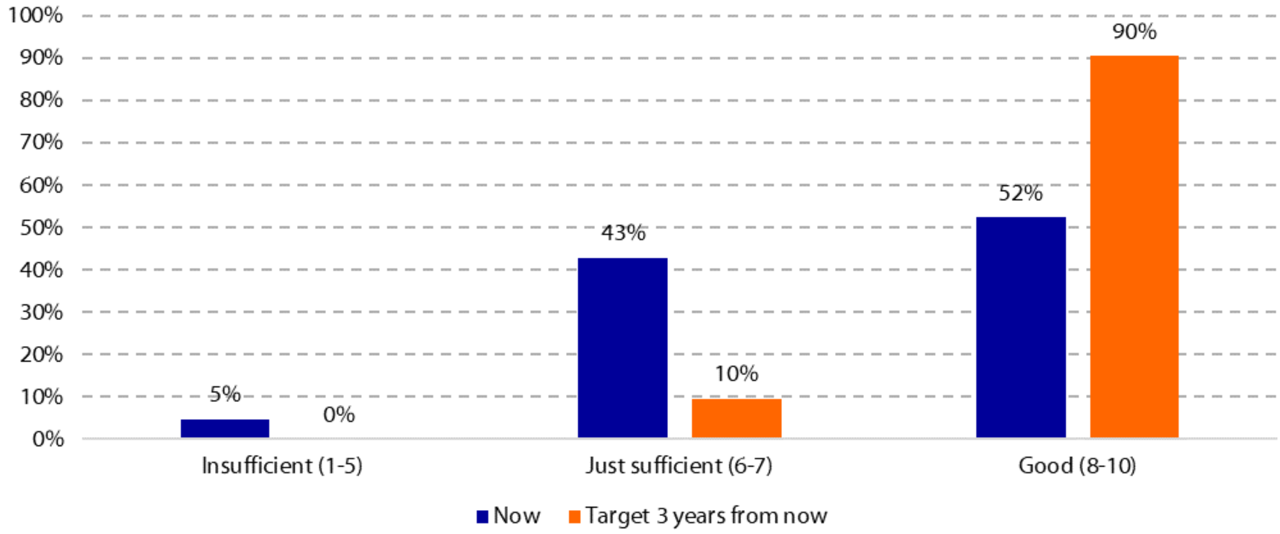


Source: Rabobank

In our opinion, the retail sector is in the early stages of development of cooperation capabilities. Retailers are used to fighting various wars with different enemies. There is the 'war on the customer' with the competitors. Since competition is coming from various angles now, this war has become more complex. The 'war on the margin' is fought with the supplier and sometimes even the customer plays a role in this war since the customer likes to capture a part of the margin via negotiating discounts. The landlord is the enemy in the 'war on the rent'. Turning from the 'war mode' into the 'cooperation mode' provides a different perspective on these 'enemies'. Via cooperation with competitors new markets can be conquered. Joining forces with suppliers opens the door towards a larger market, which is far more compelling than dividing an existing (and maybe declining) market. The landlord can help the retailer in increasing traffic, enabling him to generate visitors and sales. Taking a different perspective on all these stakeholders - seeing them as valuable cooperation partners and not as enemies - will not be easy for retailers and this will take time.

Our cautious view on the cooperation capabilities of the retailers is not endorsed by the retail executives that have participated in our online survey. They are quite positive on their cooperation capabilities. We have asked them to assess the cooperation capabilities of their organisations on a scale of 1-10. Besides the assessment of the current capabilities we have asked a target for three years from now. In figure 12 we have summarised the results, using three levels: capabilities are insufficient (1-5), just sufficient (6-7) and good (8-10). Since cooperation is of eminent importance and this importance will increase even further because of the concept of the value wheel, we see 'Good' as the threshold for the sector. According to the retailers more than 50% meet this threshold now and this share will increase further towards 90% within 3 years. If the respondents are right, this is positive for the sector. However, we prefer to be more cautious and think that there is a lot of work to be done in this area.

Figure 12: Assessment of cooperation capabilities of retailers

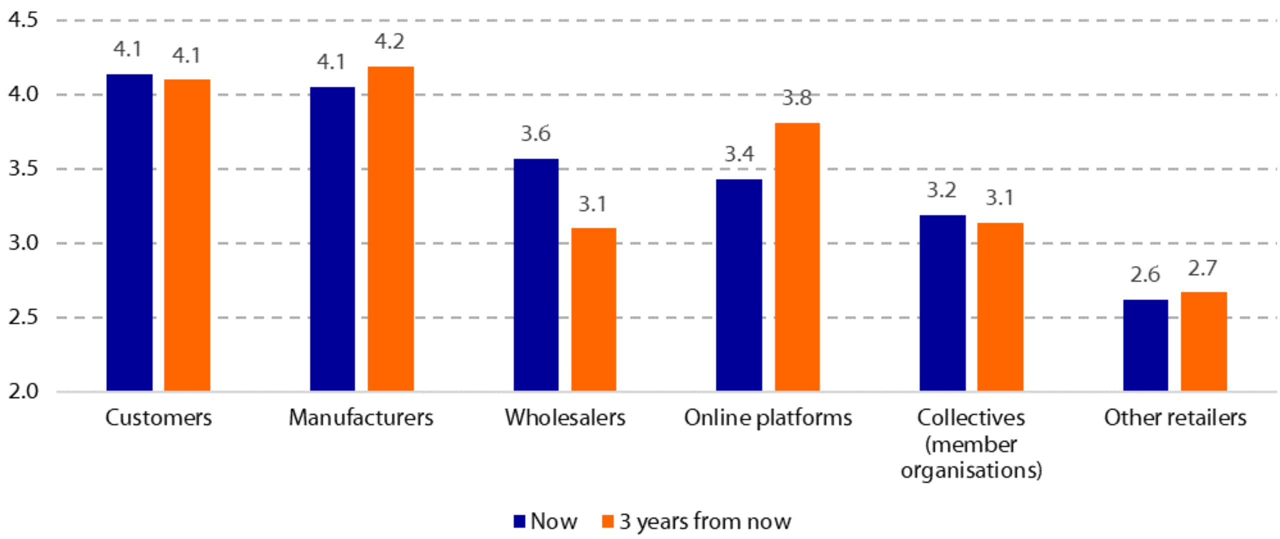


Source: Rabobank and Q&A Consultancy, based on online survey among retailers

We asked the retail executives in an online survey to rank six possible cooperation partners out of the value wheel (customers, manufacturers, wholesalers, online platforms, collectives, other retailers) on the probability that they would seek further cooperation with them. The most probable partner was given a '6' and the least probable a '1'. They have assessed both the current situation and the expected one three years from now. Figure 13 contains the results. The most important conclusions in our view are:

- The customers get relatively high ranking which is positive since they are not an obvious partner while cooperation with them has many possibilities
- The high scores for the 'obvious' cooperation partners manufacturers and wholesalers indicate a conservative stance of the retailers: a preference for the traditional supply chain partners
- Online platforms become more popular as cooperation partner (increase from 3.4 now to 3.8). This is positive as these partners can give a boost to the national and international market presence of retailers
- It is still difficult for retailers to see other retailers as cooperation partners instead of competitors. In our view, there is much potential in cooperation with competitors, but this seems still a bridge too far for retailers.

Figure 13: Ranking of possible cooperation partners

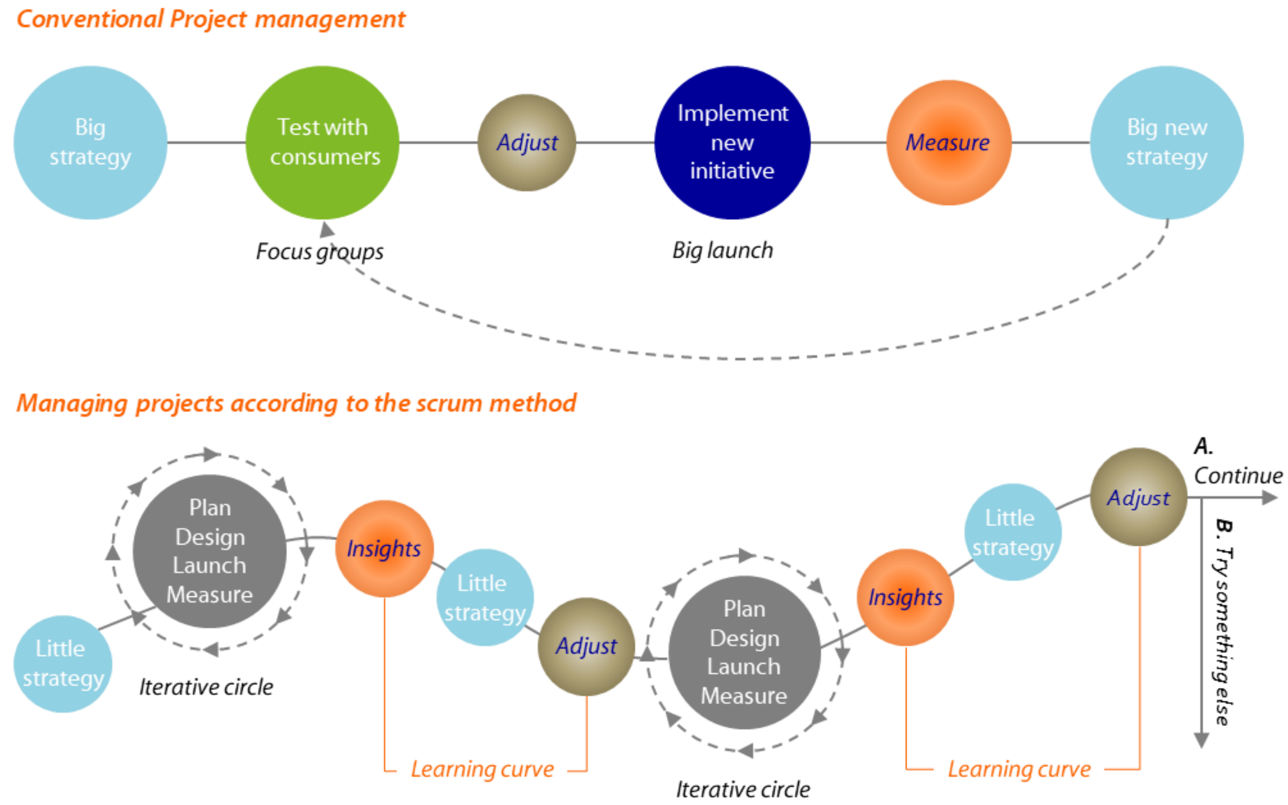


Source: Rabobank and Q&A Consultancy, based on online survey among retailers

4.4 Prepared to experiment and not afraid to fail

Building 'perfect answers' on the challenges of today's retail environment is hardly possible. Circumstances change quickly and 'yesterday's' answers are too late and do not fit with the questions of 'tomorrow'. To paraphrase a former retail executive: "Better 80% on time than 100% too late". Experimenting, making small steps and continuously adapting plans and strategies are the way forward. The 'scrum method' can be helpful in managing and executing projects (see figure 14).

Figure 14: From 'big bang' to small learning curves



Source: Rabobank

4.5 New impulses, new perspectives

Not all retailers will score well on the key KSFs of their retail formula and their cooperation capabilities. These retailers need new impulses coming from new management, new ownerships and/or new staff. Here are some examples of retailers who have profited from a variety of new impulses:

- Hunkemöller was part of retail conglomerate Maxeda until 2010 when the chain was sold to a financial investor. In 2009, a new CEO had come aboard: Philip Mountford. Management and the new owners made some drastic changes to the brand identity. The focus moved from 'price' to 'product and experience' and the Benelux retailer became an international fashion brand. The company more than doubled its number of stores from >400 in 2010 to nearly 900 (in 25 countries) in 2018
- The living decoration retailer Kwantum was part of Macintosh Retail Group until 2015. In 2014, Macintosh had decided to focus on its Shoes division. The company was already in financial trouble at that time (which has ultimately led to the bankruptcy in December 2015). The combination of the focus on shoes and the financial difficulties had of course a negative impact on the investment possibilities of Kwantum. In November 2015 Kwantum was sold to financial investor Gilde. Under the new ownership, Kwantum was able to invest again and build on its formula. In 2017, Gilde bought Leen Bakker from Blokker Holding as a first step towards a multi formula strategy
- The founders of Action, who opened the first store in Enkhuizen in 1993, recognised that they could only grow the company to a certain level. For example, they lacked knowledge, expertise and experience for a sizeable international expansion. In 2011, they sold their company to financial investor 3i. The new owner brought new management on board and the company grew from around 250 stores in 2011 to 1,095 stores (in six countries) in 2017.

With respect to the cooperation capabilities, we think that the retail sector can use some fresh blood from outside, from sectors that are more familiar with cooperation. In team sports for example, cooperation is necessary for success. "Players can win matches, but teams win championships". Cooperation is also essential in the automotive industry. Customers cooperate closely with their suppliers in the design of new components and are located in each other's neighbourhoods in order to enable just-in-time delivery.

4.6 Grab the opportunities of the value wheel!

Some of the strategic options we have described in chapter 3 are relatively easy to realise while others will require more resources in terms of management attention and money. All options have to compete with other strategic opportunities for scarce and valuable resources. However, in our opinion the value wheel contains many valuable opportunities and these opportunities will rise to the surface. The 'only' thing retailers have to do is grab these opportunities!

COLOPHON

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