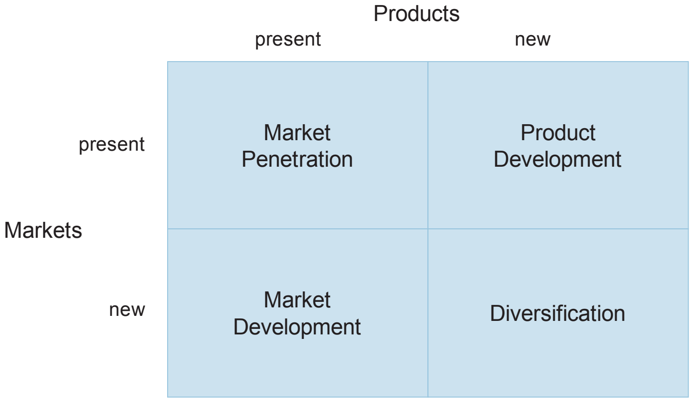
7 Growth Strategies

The aim of this Chapter is to introduce the alternative routes to company growth for retailers. Ansoff's matrix, as a strategy tool, is introduced. Outlet multiplication, cooperation and mergers & acquisitions are considered to be the basic alternatives for expanding the retail store network.

7.1 Growth Options

Almost all retailing activities start as independent, single outlet operations. Compared with other business sectors, such as manufacturing, entering into retailing by opening a retail store is relatively easy and does not require high capital resources. The desire to grow business and increase value is often a fundamental objective from the very beginning. For retailers, among other benefits, sales growth provides benefits through purchasing from suppliers in large quantities and from economies of scale in operations (e.g. IT, logistics, and administration) (Ogden/Ogden 2005, p. 92).

Figure 7.1 Alternative Routes to Company Growth – The Ansoff Matrix



		Products	
		present	new
Markets	present	Market Penetration	Product Development
	new	Market Development	Diversification

Source: Ansoff 1988, p. 109.

For decades, strategic management has analysed alternative routes to company growth. The Ansoff matrix (also called the product-market matrix) is a well-known categorisation of growth strategies (see **Figure 7.1**). It consists of four separate strategies, depending on **what** products and services are offered and **to whom** they are offered (Ansoff 1988):

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- With present products and in present markets, growth can be achieved by **market penetration**. Higher sales from existing markets can either be obtained by attracting current non-customers, who either do not buy products in the offered categories at all or who buy them from competitors. Alternatively, the loyalty of the existing customers of the retailer can be improved and the value of their shopping baskets increased.
- **Product development** is characterised by offering new products to existing markets. This can be done by providing the existing customer base with new product categories in existing stores (see Chapter 11). Apparel stores expanding into selling shoes would be a good example. *Amazon* increasing its product offer from media products into general merchandise such as fashion or even food is another example.
  Considering that the retailer's "products" are its stores (see Chapter 9), product development in retailing often means introducing new retail formats in existing markets (see Chapters 2, 3 and 4). Store retailers starting to offer their products on the Internet or supermarket retailers opening convenience stores are examples of product development.
- A current product offer can be targeted to a new customer segment, often in a new geographic area (**market development**). Regional retailers expanding their traditional store formats into other regions or national retailers expanding into new countries attempt to increase revenue for the company with this strategy. This strategy will be discussed in more detail in the Chapter on internationalisation.
- **Diversification** entails offering new products to new markets. Within diversification, there are a number of strategy sub-types: horizontal diversification, vertical diversification and conglomerate diversification:
  - **Horizontal diversification** refers to diversification into a related business field on the same level of the value chain as before. In the case of a retailer, this is the case if the company opens up stores (or acquires stores) that are dedicated to new product categories. The German food retailer *REWE* that operates home improvement stores (*toom*) is a typical example. This example shows that the distinction between the strategy type "product development" is blurry since offering new products (or new retail formats) often attracts new customer segments as well.Another example of horizontal diversification would be the attempt by *Tesco* to open up a new store format, a small format neighbourhood store called *Fresh & Easy*, in California.
  - **Vertical diversification** refers to a move into the business on the level of customers (forward diversification) or suppliers (backward diversification). Since retailers are usually the last commercial stage in the value chain, forward diversification is seldom. Backward diversification, however, i.e. taking over activities that have traditionally been carried out by the suppliers, is a frequent strategy. As shown in Chapter 1, retailers now often operate manufacturing facilities in which they produce their own products. The case study to this Chapter, *Migros*, is an excellent example of this strategy type.

- Finally, **conglomerate diversification** refers to the offering of new products or services to new markets that are unrelated to the core business of the company. A number of retail companies (e.g. *Tesco*, *Migros*, *Auchan*) are active in banking. This is not entirely unrelated because customer credit cards, financing, etc. for the retail process can be handled via these banks as well. Some retailers have entered into the travel and tourism market, e.g. the *REWE Group* or *Casino*. Other retailers have entered wholesale markets. For example, the Swiss retail group *Coop* is now Europe's second largest food wholesale company after it acquired a 50 % stake in the *REWE Group*, a large food wholesaler that operates cash & carry markets and delivery services. A prototype of conglomerate diversification is the Virgin Group. Originally started as a record store and owning *Virgin Megastores*, the company now operates *Virgin Airlines*, *Virgin Finance* and many other unrelated businesses (see Morschett/Schramm-Klein/Zentes 2010).

Because diversification often leads retailers beyond traditional retail markets, the management literature warns of the dangers when the core competence of a company lies in other fields. As the example of *Tesco's Fresh & Easy* – as well as others – has shown, inexperience in two fields – in the market and in the product – often leads to low performance.

In almost all cases (except for the diversification to other levels of the value chain), growth strategies for retailers can take two basic forms:

- Enhancing sales in existing retail outlets
- Enhancing sales by enlarging the outlet network.

Most retailers' statistics, therefore, differentiate between revenue changes in existing stores (also called comparable store sales growth or like-for-like) and changes in the scale of operations owing to opening or acquiring new stores. The latter is the focus of this Chapter, because the establishment of new stores is the most important growth route for retailers. For example, *IKEA* entered Poland in 1991 and now operates eight large stores in the country; in 2005. *Federated Department Stores* (now called *Macy's*) added 400 department stores to its store network in the USA, while *Fressnapf*, a Germany-based pet supply retailer, was founded in 1989 and now controls a store network of about 1,150 stores in twelve 12 European countries, thereof almost 800 in Germany. *Inditex* entered Germany in 1998 and now operates 72 outlets under the *Zara* and the *Massimo Dutti* banner in this country. *Tesco* entered Eastern Europe in 1994 and now operates about 730 stores in four countries. These examples also indicate the most important options for outlet growth:

- Organic growth: *IKEA*'s large surface area stores in Poland – as in most other countries – were established through organic growth.
- Joint ventures: *Inditex's* market entry in Germany was realised in a Joint Venture with the German retail group *Otto*.
- Franchising: most of *Fressnapf*'s growth in Germany comes from attracting new franchise partners, who open outlets under the *Fressnapf* brand.

- Acquisition: *Macy's* growth in 2005 was the result of the acquisition of the *May* company and the conversion of these stores into *Macy's* department stores.
- Mixed strategies: *Tesco* entered most Eastern European markets with small acquisitions, buying a few stores of regional retailers or, as in the case of the Czech Republic and Slovakia, from US retailer *Kmart*. Then, many new stores were opened via organic growth but if the opportunity to purchase additional stores emerged, the company used it, for example in Poland where it acquired the stores of a German retailer who left the country.

7.2 Organic Growth through Outlet Multiplication

The direct establishment of their own new outlets is usually the primary method for retailers to expand their businesses (Zentes/Morschett 2002, p. 173). This is also called organic or internal growth. The resulting chain stores operate multiple retail stores under common ownership and usually engage in some level of centralised decision-making. Large retail chain stores comprise up to several thousand stores.

Advantages of Outlet Multiplication

Opening new branches offers the advantage that the retailer's concept can be transferred to the new store right from the beginning. The location decisions and store layout and all attributes of the new store can be tailored to the existing strategy. Store managers are company employees, which enables activities to be monitored closely and decisions to be made centrally. Risk is limited as expansion is gradual. By opening up outlets, necessary adaptations can be identified early and new outlets can then be modified during the process. Furthermore, financing is sequential, i.e. the existing outlets contribute with their cash flows to the financing of the new outlets.

Constraints of Outlet Multiplication

At the same time, considerable financial resources become successively tied up in the store network. The opening of branches requires substantial capital investment, which is a major constraint to growth. In many markets, organic growth is slow because of zoning restrictions, planning permission, the search for sites, including the acquisition and development of the premises and so on. This entails the risk that the critical mass is not reached fast enough and other retailers with similar concepts, but not similar constraints, expand faster. This problem particularly affects retailers that require large sites for their outlets, e.g. category killers and hypermarkets (see Chapter 10), because approval for these sites is restricted in many countries.

Another drawback is the loss of flexibility over time. Many chain store operations are slower to respond to changes in consumer demand and other situational factors because of bureaucracy and the decreasing motivation of employees that are typical of larger businesses. Tailoring the assortment to the specific local needs is often easier for independent retailers than it is for large chain stores (Ogden/Ogden 2005, p. 93). However, modern retail information systems increasingly allow combining centralised decision-making with locally adapted marketing, including a locally adapted merchandise mix or prices.

7.3 Cooperative Arrangements

7.3.1 Joint Ventures

While the variety of cooperative arrangements is wide, joint ventures are clearly among the most popular forms of alliances. Since joint ventures are not retail-specific, they are only outlined briefly here. A joint venture is formed when two or more parties decide to undertake economic activity together and create a new enterprise as a legal entity in order to pursue a set of agreed goals. The parties agree to contribute equity and share the revenue, expenses and control of the enterprise (Morschett/Schramm-Klein/Zentes 2010, p. 286; Sternquist 1998, pp. 133-139). For example, when the Spanish *Inditex Group* entered Germany in 1998, it did so in a 50:50 joint venture with the German *Otto Group*. The joint venture operated the *Zara* stores in Germany.

Combination of Resources

A major advantage of forming a joint venture is the combination of the resources of two companies. Both companies bring financial and management resources, know-how, store outlets or other assets to the deal. Especially when a retailer enters a new retail or service sector or a culturally distant foreign market, the market knowledge of a joint venture partner is valuable and can facilitate expansion. In the example of *Inditex* and *Otto*, *Inditex* owned the retail brand and had the operating model for fast fashion, while *Otto* had the knowledge of the local market and better insights into location selection in Germany.

Risk Reduction

Another benefit of joint ventures is the reduction of risk for each company by splitting the risk between the participating companies. The larger the retail company, the more likely it is to expand on its own, because it can more easily afford the expenses and absorb the risk in this case.

Coordination Costs

The major drawbacks of joint ventures are the high coordination costs, because two independent partners with potentially conflicting objectives have to work together. Opportunism may emerge if one of the companies can gain a profit at the expense of the other. Thus, managing a joint venture is more complex than is managing a wholly owned company. Full control over the strategy of the joint venture is lacking because all decisions have to consider the interests of all participating companies. As a consequence, the stability of joint ventures is often considered to be rather low.

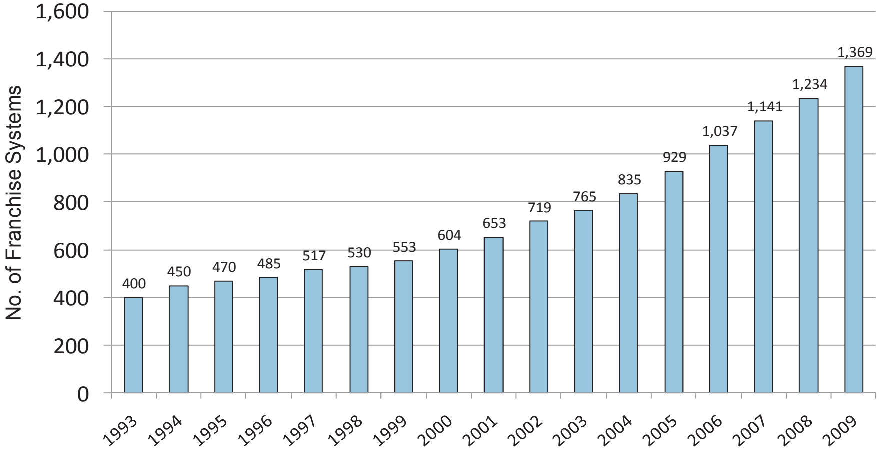
7.3.2 Franchising

While the fast food chain *McDonald's* is the most often cited example of a franchise system, many well-known retailers also operate as franchise systems. *Benetton*, *The Body Shop*, *Fressnapf/Maxi Zoo*, *OBI* and *7-Eleven* are examples.

Franchising is defined as a contractual agreement between two legally and financially separate companies, the franchisor and the franchisee. The franchisor, who has established a market-tested business concept, enters into a relationship with a number of franchisees, typically small business owners, who are allowed to use the franchisor's brand and must operate their business according to the franchisor's specified format and processes. The franchisor provides ongoing commercial and technical assistance. In return, the franchisees typically pay an initial fee as well as fees (royalties), which average about 5 % of gross sales, plus some advertising fees (Inma 2005, p. 29).

According to different national franchise associations, the franchising sectors in different country markets have reached considerable sizes. In France, there are about 1,400 franchise systems, in Germany about 960 and in the United Kingdom about 850. On average, each franchise system has between 40 and 50 franchise outlets, but the largest often exceed 1,000. All statistics show that franchising is growing continuously (see, for example, **Figure 7.2**).

Figure 7.2 Franchising in France



Source: Fédération Française de Franchise 2011.

Division of Tasks

A fundamental characteristic of franchising is that it always involves two separate and independent companies that assume distinct roles and a strict division of tasks in order to achieve a joint objective. Since the franchisee owns its own business, it is entitled to all profits that are generated. Franchising thus combines the benefits of a large, efficient retail system, including economies of scale in procurement, logistics, national advertising, IT systems and administrative activities, with the strength of an independent entrepreneur who manages the outlet, including customer contact and supervising store employees (Zentes/Morschett/Neidhart 2003). The common brand enables all participants in the franchising system to benefit from the advertising and goodwill generated by each outlet. From the consumer's perspective, it is often impossible to detect the difference between franchising and own branches.

Forms of Franchising

There are two main forms of franchising (Sternquist 1998, p. 123):

- Direct unit franchising is the basic form. In a unit franchise, the franchisor grants the franchisee the right to engage in a single franchised business operated at a specified location.
- In a master franchising agreement, the franchisor grants the master franchisee a set territory, and within this territory the master franchisee is allowed to establish unit franchises.

Sources of prospective franchisees can vary:

- Often, start-up entrepreneurs are targeted. Their inexperience makes the franchisor’s business package relatively more attractive.
- In **multi-unit** franchising, successful franchisees are allowed to open new branches. This strategy is a type of organic growth within a franchise system. The number of outlets per franchisee, however, is often strictly limited because multiple franchise outlets diminish some of the advantages of franchising.
- **Conversion franchising** occurs when a franchisor adds new franchisees to the system by recruiting existing independent retail businesses (Hoffman/Preble 2003). Store owners may affiliate with the franchise system to take advantage of the brand and other components of the operating system.

Advantages for the Franchisee

For the franchisee, there are a number of benefits compared with a non-franchised independent business. Upon opening the franchise store, the franchisee enjoys instant goodwill in the market because it can use an established brand name, exploit a tried-and-tested business concept and carry out standard operating procedures.

It also receives comprehensive information on the business concept before starting, including information on necessary investment and likely profits. It obtains training and support, and financing is usually easier since belonging to the franchise system provides the franchisee with access to financing that would otherwise not be available as easily. From the perspective of a bank, it is easier to give credit to a franchisee since it can provide a business plan that has been based on the example of existing franchisees.

Advantages for the Franchisor

For the franchisor, as a growth strategy, franchising also has considerable benefits (Berman/Evans 2010, pp. 108-111; Zentes/Morschett/Neidhart 2003):

- Franchising allows for rapid growth of a retailing company. Especially when the success of a concept depends upon rapid market coverage, franchising is a way of multiplying a concept without the usual financial constraints. Franchisees also finance the investment for establishing stores.
- Motivation of franchisees is high, because they manage their own stores.
- Franchisees have knowledge of the local markets; customer and employee contact of franchisees is direct and personal.
- Written franchise agreements require the store owners to keep to stringent operating rules set by the franchisor.

Disadvantages for the Franchisor

One major disadvantage for the franchisor is that it has no direct hierarchical control over the franchisee. The franchisee is an independent contractor, not an employee. Franchisees can harm the overall reputation of the franchise if they do not maintain company standards. Changes in the franchisor's strategy may be slow to implement because franchise contracts usually run for three to five years and substantial changes are only possible through changing the contracts. If competition between different outlets occurs, it leads to conflicts (stronger than in own outlets since the profit is shifted from one franchisee to another). Also, franchisees may join to restrict the influence of the franchisor and attempt to change the rules. Another drawback is that under European law, the franchisor is not allowed to fix the final consumer prices for products. Accordingly, the marketing and management of a franchise system is more complex than it is for a truly uniform and hierarchically managed system of company-owned stores.

Often, the dynamics of the balance between the benefits and drawbacks of franchising leads to a change in the use of this growth strategy during the life cycle of a retailer. The resource scarcity that motivates retailers to embrace franchising as a growth strategy in the expanding stages of their life cycles lessens as the system becomes more established and growth rates decline. The costs associated with managing a complex franchise system gradually outweigh the benefits associated with the resources provided by franchisees. Consequently, over time franchisors tend to buy back franchises and increase the number of company-owned stores (Oxenfeldt/Kelly 1969). However, over the past few years the opposite development has also been occurring. Since, for many chain stores, operating small stores with low turnovers in certain market areas is not profitable in the form of company-owned stores, and the higher motivation in manager-owned stores has often proven capable of making a store profitable, some large chains have started to spin-off certain retail outlets and transform them into franchised stores. Smaller supermarkets and convenience stores are typical objects of such transformations (Zentes/Morschett/Neidhart 2003, p. 227).

Plural-Form Networks

Often, franchising is not used as an exclusive company strategy, but franchisors also own a substantial number of retail outlets themselves. The complexity of managing such plural-form networks is higher than that of managing monolithic systems of own stores or franchises. Synergies can be drawn from applying two different growth strategies simultaneously in the company, such as higher franchisor flexibility when deciding on new store openings. At the same time, the risk of conflict throughout the network is substantially higher and the management culture required to manage a franchise system of independent store owners is often different from the culture needed to manage a chain store (Cliquet 2000).

7.4 Mergers & Acquisitions

Companies also have the option of external growth, namely expanding by acquiring resources from other companies. Expansion through mergers & acquisitions (M&A) involves the consolidation or purchasing of existing retail companies or retail outlets. It can, in the case of diversification, also refer to the purchase of companies in other sectors than retailing. In a **merger**, two companies are combined and at least one of them loses its legal independence. In an **acquisition**, one company acquires a majority interest in another or takes over certain assets (stores) of another company. The term acquisition is often restricted to a full takeover. The legal independence of the acquired company can remain intact (Zentes/Swoboda/Schramm-Klein 2006, pp. 278-281).

M&A have played a major role in structural changes in the retailing sector over recent decades and they constitute a well-established growth mechanism (Burt/Limmack 2001). For example, in 1999 *Carrefour* merged with *Promodès* to form the largest European retail company and the second largest worldwide. In 2005, the merger of *Sears* and *Kmart* into *Sears Holding* created the US's fourth largest retailer. In 2006, the *Metro Group* took over 85 *Walmart* stores in Germany, expanding its own *Real* hypermarket network of 330 stores by a quarter. The Austrian *XXXLutz*, the second largest furniture retailer in the world after *IKEA*, bought five furniture chains in Germany. The largest acquisition, *Mann Mobilia*, added seven stores to the company's network. In 2011, *ASDA* took over the store network of *Netto* (Dansk) in the UK, giving it the possibility to establish a chain of small supermarkets. A list of similar examples would be long.

Advantages of M&A

M&A allow rapid expansion by overcoming the bottleneck created by the difficulty of establishing and developing adequate retail locations, which can take years from site selection to finally opening a store (Burt/Limmack 2001, p. 4). Within a short period of time, an acquisition makes an entire bundle of resources available to a company. Especially when first-mover advantages are pursued in a new market, this can be a critical success factor (Meyer 2001, p. 359). Since the customer base of the acquired retail company may be preserved, market share in a new market is gained quickly. Thus, with M&A a company has a substantial turnover in a new market from the very beginning, which may help pay for the investment.

After an acquisition, either the integration process comprises a change in the brand name of the outlets or the original retail brand of the acquired retail outlets is retained. The latter is often the case, when the acquisition is used to expand into other retail sectors or formats. A food retailer entering the DIY market, or a supermarket company acquiring a discount chain, for example, could be well advised to keep the acquired chain's established retail brand. The acquired company's existing resources – management expertise, personnel, sites and so forth – focus on its established field of business; thus, an objective of an acquisition is to exploit the know-how and dedicated assets of the acquired company.

Disadvantages of M&A

However, integration costs following an acquisition can be high. An incompatibility of company strategies, capabilities, resources and cultures often results in an insufficient exploitation of existing potential for synergies. The takeover and associated cultural change in the acquired company may also result in a brain drain and the loss of significant management skills. Also, in many markets it is difficult to find suitable takeover candidates. Successful retailers are, in most cases, not available for acquisition and less successful retailers often have retail locations, stores and premises that are not attractive enough for acquisition. Adequately evaluating the value of a retail company before an acquisition is, however, not an easy task and the real value and quality of the acquired company can often only be assessed correctly after the acquisition (Burt/Limmack 2001, p. 4). For example, in Germany *Walmart* faced the problem that the store network acquired for market entry was unfavourable and, over time, other targets for takeover were not available on the market. The option of further expansion through acquisition may also be limited by antitrust laws, as the example of *Safeway* in the United Kingdom illustrates. In already highly concentrated markets, the acquisition of other outlet networks by the largest players is often not approved by authorities.

In summary, acquisition is a fast growth strategy when adequate takeover objects are available, but the associated risk is substantially higher than it is with organic growth.

7.5 Minority Investment in Retail Companies

Owing to the difficulties associated with full-scale acquisitions, acquiring a minority stake in another retail company is also a frequently pursued strategy. For example, *Kingfisher* bought a 21 % stake in the German DIY retailer *Hornbach* and supports *Hornbach*'s national and international expansion, for example by providing funds. In 2004, Hong Kong-based *A.S. Watson* purchased a 40 % stake in German drugstore chain *Rossmann*.

Acquiring the partial ownership of another retail company involves similar advantages and disadvantages to the acquisition strategy in general. However, successful retail companies generally prefer another company buying an equity stake in their company to being fully acquired. Equity participation by a larger company can add resources that support its further expansion. Furthermore, the strategy can be useful in situations where full-scale acquisitions are difficult because of the particular market conditions or government control. At the same time, the remaining equity stake of the initial company reduces the risk of a brain drain (Zentes/Morschett 2002, p. 174), since the established management team of the acquired company often retains control, frequently only supplemented by additional management capacity from the acquiring company. The risk of overestimating the value of the acquired company is reduced because the acquiring company achieves full transparency over business processes and results, facilitating a potential full acquisition after a certain period.

7.6 Reduction Strategies and Withdrawal from Markets

While most companies focus on growth, some authors point out that strategic planning and analysis should also include the strategic withdrawal options from certain product or geographical markets. Sometimes closing down or divesting (selling-off) the unprofitable parts of a business or those that do not match the current strategy can help the retail company as a whole (see also Chapter 8).

For example, in 2002 *Fressnapf*, the European market leader in pet food and pet supplies, closed down its online shop (which it reopened in 2010). In 2006, *Walmart* withdrew from Germany after accumulating losses since its market entry in 1997. *Netto Dansk* left the UK in 2011 by selling its outlets to *ASDA*. In 2005, *OBI* sold its DIY stores in China to a competitor *Kingfisher*. Even though *OBI* operates about 500 DIY stores internationally and has sales of more than six billion EUR, it decided strategically that the future investment needed to ensure success in this huge market would be too high. At the same time, the company announced the opening of 100 new stores in Europe over the next five years. It is noteworthy that *Kingfisher* itself announced in 2009 to divest a third of its stores in China because they did not promise to return a profit or because they did not fit the future strategy in the country. In 2010, *Carrefour* announced it intended to sell off all of its hypermarkets in Thailand to *Groupe Casino*. *Saturn*, usually an internationally successful electronics retailer, announced at the beginning of 2011 that it would sell its stores in France to a competitor.

These examples demonstrate that in retailing, growth strategies are closely connected to withdrawal strategies. Withdrawal is not always the result of failure in a country, even though it often is. Other reasons include a change in corporate strategy, a change in external conditions, the necessity to generate cash to strengthen operations in the home country or low future expectations concerning the specific retail format.

Generally, divestment reveals that the retailer expects a better opportunity for investment and growth elsewhere. Retailer portfolios, with respect to their stores, store formats and country markets, are often reassessed, and a strategic withdrawal from one market often provides the starting point for expanding into other markets or for opening additional stores in the remaining markets.

7.7 Conclusion and Outlook

Growth continues to be highly relevant for the success of a retail company but, at the same time, it is more difficult to achieve because of several factors. These include the power of large retailers and the crowding out of independent retailers and small chains as well as the already high and increasing level of concentration in many retail markets combined with market saturation in many product categories.

Flexible growth strategies, therefore, become more important. Retail companies usually do not use these strategies in isolation but in combination, as the example of *Tesco*'s internationalisation or the description of plural form networks illustrated. If a retail company wants to enter a completely new country or establish a new store format (e.g. a food company entering into electronics retailing), then an initial acquisition helps achieve critical mass quickly. From that point on, the company can grow by establishing new sites and opening stores. Furthermore, as has been shown in the context of the increasing concentration in retailing, companies then often make a major step forward by acquiring smaller chains that leave the market.

Larger, divisionalised retail store groups with different retail formats often implement different growth strategies for different formats and/or markets. For example, *Carrefour* operates its hypermarkets in most parts of the world as own outlets, while it franchises its system in the Middle East (United Arab Emirates, Egypt, Saudi Arabia) to the *Majid Al Futtaim Group* that operates a number of large *Carrefour* hypermarkets in the region. The difficult market conditions in this region and the local knowledge of its franchise partner are the probable reasons for this strategy. Most of *Carrefour's* convenience stores all over the world are franchised, and the expansion of supermarkets stems at least partly from franchised outlets, while there is also a substantial number of own outlets. Concerning the Balkan region, *Carrefour* established a joint venture in 2010 with the Greek company *Mari-*

nopoulos to open stores in Bosnia, Slovenia, Serbia and Croatia and other countries. This is a typical picture of retail companies that use different growth strategies over time and which tailor these strategies to the retail format and specific situation.

Further Reading

HOFFMAN, R.; PREBLE, J. (2003): Convert to Compete: Competitive Advantage through Conversion Franchising, in: Journal of Small Business Management, Vol. 41, No. 2, pp. 187-204.

7.8 Case Study: Migros[1]

7.8.1 Profile, History and Status Quo

The origins of the Swiss retail group *Migros* date back to 1925 when Gottlieb Duttweiler founded *Migros* as a limited company in Zurich, Switzerland. His vision was a sales organisation without intermediate trade, aiming to create a direct **bridge** from manufacturer to customer. At the beginning, he started his company with five Ford T trucks used as mobile retail shops and only six articles of everyday essentials, including coffee, rice and soap. Shortly after the company's founding, the mobile retail shops offered their goods in 293 destinations across Switzerland and the assortment of goods increased. The early success of Duttweiler's corporate strategy was based on his pricing; partially he sold goods with a price reduction of 40 % in comparison with his competitors. This was achieved by focussing mainly on private labels. Only a year later, *Migros* opened its first store in Zurich. In spite of everything, *Migros* struggled for economic survival in its early years. During the Second World War, Duttweiler decided to change *Migros'* limited company structure into regional cooperatives and founded the *Migros* cooperative alliance. Nowadays, the alliance consists of ten cooperatives.

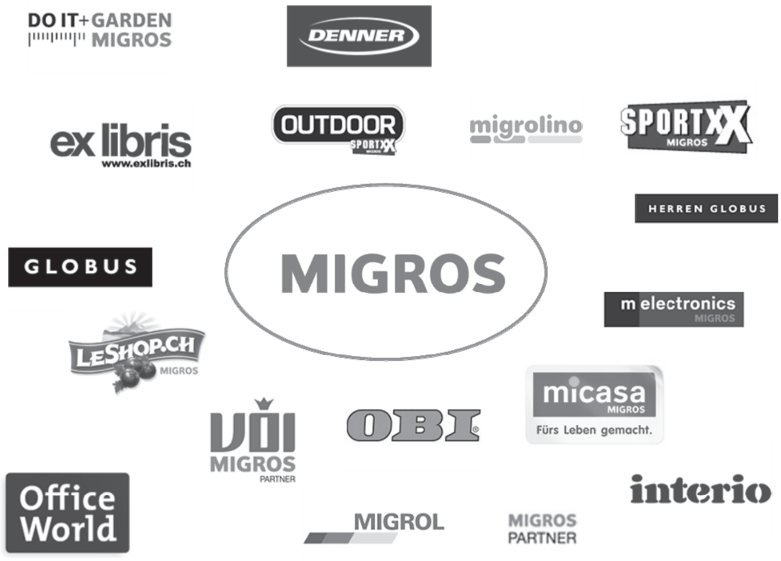
To reduce waiting times and deal with the increasing number of shoppers, *Migros* opened Switzerland's first **self-service store** in 1948. A specific feature of *Migros*, based on the dreams of its founder, are its social values, e.g. social capital, education for everyone and the abandonment of selling alcohol and tobacco.

Nowadays, *Migros* is the biggest retailer in Switzerland, holds a market share of 20.4 % and has approximately 61,700 employees and a group volume of 24.9 billion CHF in 2009. The company concentrates on five business segments: cooperative retail business, trade, industry, wholesaling and travelling. The cooperative retail business with its grocery stores is the core business of *Migros*.

[1] Sources used for this case study include the website http://www.migros.ch and various annual and interim reports, investor-relations presentations as well as explicitly cited sources.

In Switzerland, *Migros* operates many different retail formats: supermarkets, hypermarkets, category specialist stores such as *Micasa* and *Ex Libris*, department stores, restaurants and convenience stores. **Figure 7.3** shows the portfolio of the retail business of *Migros*.

Figure 7.3 The Portfolio of the Retail Business of Migros


DO IT+GARDEN MIGROS
DENNER
ex libris
www.exlibris.ch
OUTDOOR
SPORTXX
migrolino
SPORTXX
MIGROS
HERREN GLOBUS
GLOBUS
MIGROS
m electronics
MIGROS
LESHOP.CH
MIGROS
micasa
MIGROS
Fürs Leben gemacht.
VOI
MIGROS
PARTNER
OBI
interio
Office World
MIGROL
MIGROS
PARTNER

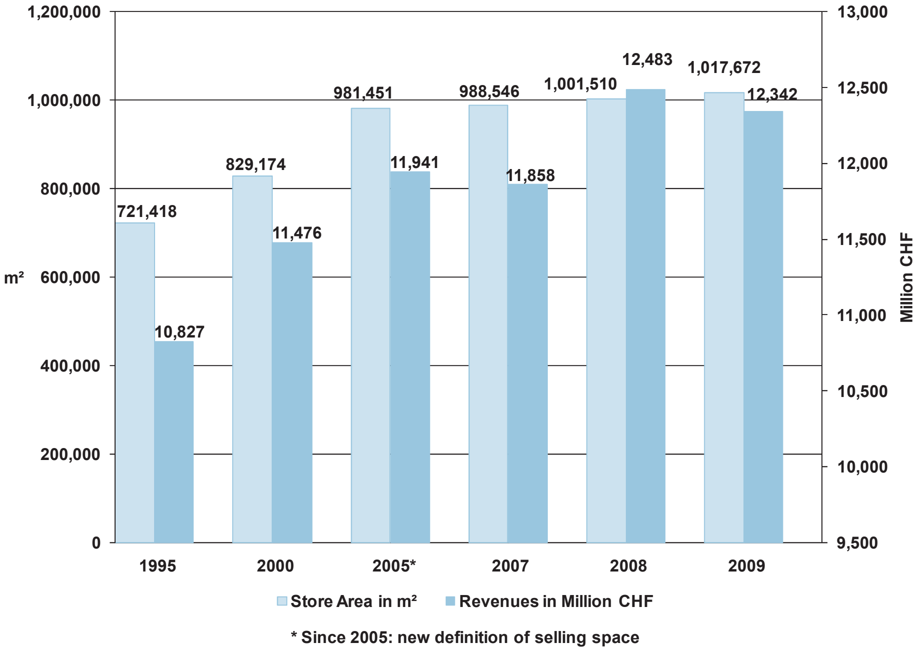
Source: Migros 2011.

7.8.2 Organic Development in Selected Fields in Recent Years

As shown in this Chapter, organic growth – usually through outlet multiplication – is a primary method for a retailer to expand its business. However, *Migros* forces the renovation and expansion of its consisting branch network as well. This practice can be seen as a form of risk reduction, whereby a proven concept is transferred to new stores. Between 2000 and 2009, the sales area of the company's grocery retail formats (*Migros* MMM stores can be defined as hypermarkets, the MM stores as large supermarkets and the M stores as small supermarkets) increased from 829,174 m^2 to 1,017,672 m^2, an increase of 23 %; the selling space of the whole retail business grew from 964,792 m^2 in 2000 to 1,265,059 m^2 in 2009, which was equivalent to an increase of 31 % (GfK 2010, pp. 109-114). Since 2000, the total number of grocery retail stores has remained steady during a continuous process of store closures and new store openings. This indicates that the average store size has increased.

It is noteworthy that *Migros'* organic growth in grocery retailing is becoming difficult. While the company increased its sales space by 23 % from 2000 to 2009, sales volume only increased by 7.5 % in the same period, as is evident in **Figure 7.4**. This comparison also reveals that one important productivity measure – sales per square metre – has deteriorated over the past decade. Furthermore, it can be seen that revenues have dwindled since 2009 because of the adverse circumstances in *Migros'* core business, e.g. increased competition. This negative sales trend also has an effect on productivity: the average revenue per square metre is declining in all three supermarket formats (Gfk 2010, pp. 119-121).

Figure 7.4 Revenues and Expansion of Store Areas in the Grocery Retail Formats of Migros (M, MM, and MMM)



Source: IHA-GfK 2003, p. 87; GfK 2010, p. 113.

7.8.3 Cooperative Growth and Buying Stakes

Cooperation is another growth strategy. The most popular forms of alliances to grow are **joint ventures,** which combine the resources of at least two companies to reduce the business risk for both parties. *Migros* also uses this strategy to grow. In 2008, *Migros* established a joint venture with the mineral oil group *Shell* to run its **convenience stores** in the petrol stations of *Migros* and *Shell* as well as rail stations and to expand the branch network under the revived brand *Migrolino*. In 2009, *Migros* and *Shell* owned 217 convenience stores and the development of this joint venture exceeded expectations. *Migrolino* stores carry a similar assortment to other convenience stores, including alcoholic beverages. They also sell *Migros* store brand products. *Migrolino* and *Shell* remain independent companies and a merger of the particular chains of petrol stations is not planned. An example of the low stability of joint ventures is the failed joint venture *Cevanova* between *Valora* and *Migros*, which was the predecessor of the joint venture with *Shell*. It existed from 2000 to 2008 and operated 95 convenience stores under the retail brand "*avec*" in petrol and rail stations. After the breakup, the shops were divided among the former joint venture partners, but the brand rights stayed with *Valora.*

Another popular form of cooperative arrangements is **franchising,** which involves two separate and independent companies with distinct roles and a strict division of tasks. An example of this type of growth strategy is the partnership between the German DIY chain *OBI* and *Migros*. In Switzerland, *Migros* is the exclusive partner; the regional *Migros* cooperatives run the *OBI* stores with their own staff. *OBI* offers widespread assortments in the category groups of construction materials, DIY, habitation, gardening and pets with more than 80,000 articles. After the beginning of negotiations in 1997, the first *OBI* store was opened 1999 in Basel. Nowadays, *OBI* and *Migros* run ten stores in Switzerland. In the midterm, an expansion up to 15 to 20 stores in Switzerland is planned.

In 2009, *Migros* bought a stake of 49 % in the German *Gries Deco Company* with its retail brand *Depot*. Even though different in detail, this approach was rather similar, from the perspective of *Migros*, to the establishment of a joint venture because the strengths of different companies are combined and the interests of different partners still have to be considered. The brand *Depot* sells home accessories, gifts and smaller items of furniture. The strengths of *Depot* are the presentation of varying worlds of living and emotional stagings of products. The products are produced under the instructions and ideas of *Depot.* In 2010, *Depot,* with the concept and market knowledge of *Gries Deco* and the fresh capital influx by *Migros,* opened 71 new locations. The volume of trade reached 200 billion EUR, in comparison to 2009, this was a surplus of 70 %, after a surplus of 35 % in the previous year (Bender 2011). *Migros* was the preferred partner of Christian Gries, manager and co-proprietor of *Depot*. Furthermore, both parties expect a long-term relationship with dynamic growth. In 2011, five new stores in Switzerland and 70 new locations in Germany are planned (FAZ 2011). *Migros* also believes that there is a great potential between its own subsidiary firm *Interio* and *Depot*. Both entrepreneurial concepts will be adapted similarly, and synergy effects will be realised. Furthermore, it is notable here that a stake regularly has other aims than M&A. A stake initially appears to be more like a partnership on an eye level, whereas M&A is the assimilation of a company.

Another example of growth by acquiring a stake is the online retail channel *Migros LeShop. LeShop* was founded by Christian Wanner and three partners as a start-up in 1997, and it started selling food online in April 1998. *Migros* entered into a strategic alliance with the company in 2003. After a few years of successful cooperation, *Migros* bought 80 % of *LeShop* in 2006, which was later stocked up to 90.5 %. The management team of *LeShop*, in particular the managing director and co-owner, remain in charge and it maintains a high level of autonomy within the *Migros* group.

In 2010, *Migros LeShop* held a market share of 67 % in food online shopping in Switzerland. The online supermarket provides a large assortment of *Migros* private labels and – different from *Migros* grocery stores – also stocks a large selection of manufacturers' brands. It also sells wine, beer and liquor. *Migros LeShop* delivers the products directly to the customer's front door and aims at young families and working mothers, which appreciate the simplicity as well as the saving of time. *Migros LeShop* has about 50,000 regular customers; 91 % of them are repeat buyers. The revenues of *Migros LeShop* are constantly growing **(see Table 7.1**). Furthermore, a robust growth in online grocery retail for the next years is forecasted (GfK 2010, p. 338).

Table 7.1 Revenues of Migros LeShop between 2000 and 2010 in Million CHF.

Year	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
Reve nues	6	11.5	12.8	15.2	32.6	47.1	64.5	92.3	112	132	151.1

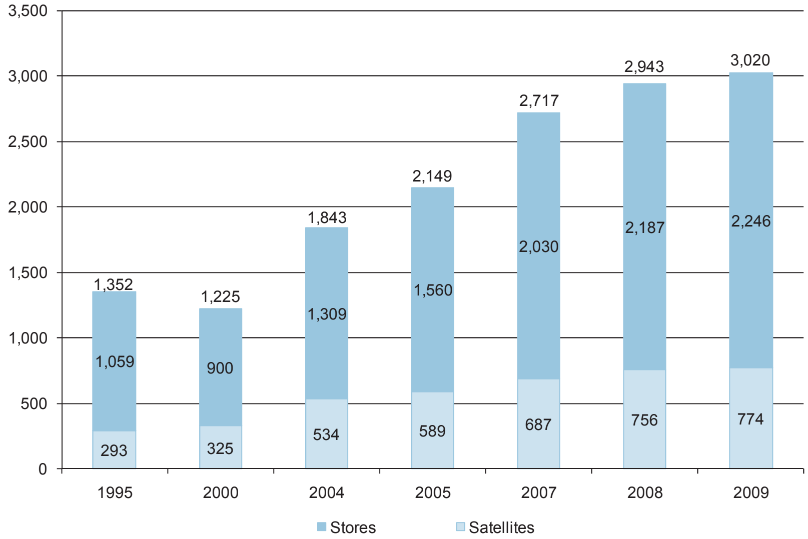
Source: Migros LeShop 2011.

7.8.4 Mergers & Acquisitions

Expanding by acquiring other companies is another option to grow. This enables a company to gain an entire bundle of resources and, furthermore, rapid expansion. *Migros* recently used this strategy to grow. In 2007, it acquired a 70 % stake in the Swiss discounter *Denner*. This stake was bulked up to 100 % in 2009. *Denner* is the number three in the Swiss retail trade and the leading discounter in the country. It is noteworthy that a major part of *Denner*'s sales stems from alcohol and tobacco. In fact, *Denner* stores have often been co-located with *Migros* stores so *Migros* customers that could not buy these products in *Migros* due to the founder's principles could still easily buy them at the same shopping trip, at the *Denner* next door.

The former owner of *Denner*, the Gaydoul family, sold the retailer to save its long-term competitiveness in a market with intensified competition because of the market entry of the German discounters *Aldi* and *Lidl*. *Denner*, a discounter who only sells in Switzerland, would probably not have had the necessary purchasing volume on its own to compete with these two foreign discounters. Despite *Denner's* expansion plans, the Gaydoul family was afraid that the growth of the retailer would stagnate and decided to sell *Denner* to create a long-term solution for the company. *Migros* took this chance and entered this market segment. Before, *Migros* was not represented in the discount sector with its own stores.

Figure 7.5 Development of Sales of Denner from 1995 to 2009 in Million CHF



Source: GfK 2010, p. 169.

Following the decision of the Swiss competition commission, *Denner* remains an autonomous company with its own brand presence. After the bulk up of the stake at the end of 2009, the former *Ex-Libris* managing director Peter Bamert became the head of the discounter. In 2009, *Denner* generated revenues of more than three billion CHF, an improvement of 2.6 % in comparison with the previous year. With this growth, *Denner* exceeded the total retail market, which realised a growth of only 0.5 %. Overall, *Denner* has maintained its position in a difficult market environment. At the end of 2009, *Denner* ran 752 stores, 437 stores of which were autonomous and the 315 remaining stores are so-called "*Denner-Satellites*", which distributes the *Denner* products, but ran by independent merchants (GfK 2010, pp. 166-169). **Figure 7.5** shows the development of the sales of *Denner*.

However, an acquisition has a higher risk than does organic growth: integration costs can be high and the possibility of incompatible company strategies, resources and cultures is always there. The **takeover** of *Denner* has also produced hurdles for *Migros*. According to the competition commission, *Denner* cannot be fully integrated into *Migros* Company, e.g. both companies cannot buy goods together for resale. Another problem is the frictions concerning the growth strategy of *Denner*. As a result, the CEO of *Denner*, Peter Bamert left the company after only one year as CEO even though he had increased revenues and forced the expansion of *Denner* (Tagesanzeiger 2011).

7.8.5 Migros Industry

Migros not only operates as a retailer, but also operates in other fields. This **diversification** initially aimed to reduce the cost of goods sold, to secure supply and to reduce risk. However, it has developed into a central pillar in the strategy of *Migros*. *Migros Industry* delivers primarily to *Migros* channels such as *Migros* grocery stores, *Denner*, *Migrolino* or *Migros LeShop*, as well as third-party customers domestic and abroad.

In previous years, *Migros Industry* expanded its market position. In 2010, *Migros Industry* generated revenues of 5,316 billion CHF, up 2.5 % despite a tough economic context. The focus of business operations was Switzerland but also Germany, England and France. For example, the largest manufacturing companies, *Chocolat Frey* and the cosmetics producer *Mibelle*, produce different store brands for the German retailers *REWE*, *EDEKA* and *dm-Drogeriemarkt*. *Migros Industry* employs 10,049 employees in Switzerland. In 2009, *Migros* reinvested 151 million CHF in projects aimed at the growth and rationalisation the industry sector. The companies of *Migros Industry* are shown in **Table 7.2.**

Table 7.2 The Companies of Migros Industry

Product Field	Company
Meat/Poultry/Fish	Micarna, Mérat, Favorit
Dairy Products/Cheese	Elsa, Mifroma, Dörig, Mifroma France
Bread/Cakes and Pastries/Pasta/Rice/	Jowa, Midor, Riseria, Jowa France
Chocolate/Coffee	Chocolat Frey, Delica
Convenience/Beverage	Bina, Aproz, Gastina
Near-food	Mibelle, Mifa, Hallam Beauty
Wholesale Business	Scana

Source: Migros 2011.

Migros Industry is a driving force of growth within the cooperative. Therefore, *Migros* forces an expansion in the industry sector, domestic and abroad. The focus lays on a strengthening of marketing force in the main markets and on an upgrade of assortments. Furthermore, the dependency of brand manufacturers can be reduced and *Migros* cooperative can obtain more favourable buying conditions.

7.8.6 Summary and Outlook

Company growth is essential for retailers. As shown in this case study, *Migros* does not focus on only one growth strategy, but uses different strategies in combination, depending on the business segment and distribution channel. The most obvious part of the diversification strategy is the backward diversification with *Migros Industry*.

In the grocery channel, *Migros* cooperative makes use of a strategy of organic growth. Instead of increasing the number of outlets (which would be difficult in a rather saturated market with zone restrictions), it does so by growing the outlet sizes of its M, MM and MMM stores. The disadvantage of this strategy is the relatively slow growth, the decreasing productivity of the sales area and a loss of flexibility over time.

Another growth strategy has also been used to realise market entry in the discount sector. In order to gain a strategic size in this market sector, especially against the background of the market entry of German retailers *Aldi and Lidl*, *Migros* decided to buy the Swiss discounter *Denner* to realise a rapid expansion. *Migros* also used the possibility of cooperation to grow, for example by establishing *Migrolino* convenience stores in a joint venture with *Shell*. Similarly, it bought stakes in interesting companies such as the *Gries Deco Company* and *Migros LeShop* to develop new market segments. All these growth strategies can be seen as a part of diversification and risk spreading in different branches. It is noteworthy, however, that the expansion strategy watered down the principles of the founder because *Denner*, *Migrolino* and *Migros LeShop* now sell alcoholic beverages and tobacco products.

In the future, *Migros* will continue its strategy of diversification and growth. Nevertheless, this strategy concentrates on Switzerland with regard to retailing. This geographical restriction on one core market could cause disadvantages concerning international competitors that push into the Swiss market. Only *Migros Industry* has an international position and is likely to increase internationalisation (Morschett et al. 2009).

Questions

1. Discuss the consequences for a company which arises of a poor organic growth. What are the problems?
2. Which problems can emerge with acquisitions?
3. What are the advantages and disadvantages of joint ventures?

Hints

1. Consider Chapter 8 concerning the possibility of acquisitions.
2. See Chapter 8 as well concerning the relevance of joint ventures.