

1.

We take the view that the “grocery market” should be defined with reference to “grocery products” only. There is just one grocery market. A differentiation between primary shopping (bigger stores), convenience shopping, luxury shopping etc. merely helps to describe how retailers / retail formats distinguish themselves within the grocery market. One may describe these as different segments of the grocery market. They definitely do not constitute markets in their own right, i.e. there is no such thing as the “convenience grocery market”, the “luxury grocery market” or the “discount grocery market”. The distinction is somewhat arbitrary, as a grocery shopper who lives next to a hypermarket would see this as his most convenient grocery shopping provider. Likewise, Tesco’s Finest range constitutes a rather luxurious offer that can easily compete with M&S’s range and equally highly specified products can be found in Lidl’s and Aldi’s discount stores. At the end of the day, it is the need for groceries that drives the consumer and constitutes the market for groceries.

A distinction between primary and secondary shopping therefore merely describes most households’ preference to do a “big shop” every so often and complement this by various other “smaller shopping trips”. This “big shop” does not have to be done in a store of over 1,400m sq. It can be done at grocery discount stores (all smaller than 1,400m sq) or in convenience stores (even smaller than discount stores) or substituted for several small shopping trips to convenience stores.

As to traveling time, the Competition Commission’s assumptions seem to be reasonable, although on the lower end of a reasonable bandwidth and would mostly but not always apply as grocery shopping may be carried out in conjunction with something else, e.g. the journey from or to work, the fitness studio or the hairdresser, whereby the location of something else determines the grocery shopping location (the grocery store not being the “destination” itself but just a side effect).

2.

To answer several key points of this question, we would like to refer to an in house analysis that dates back to January 2006 and was done voluntarily and in confidence in support of a “City Institution” who had asked us to kindly assist them in support of their analytical research. The analysis covers whom we see as our competitors and how we see major aspects of “the grocery market” and should provide a good starting point from where we will expand upon the further aspects of your question.

The UK grocery market actually represents several markets to us, i.e. the grocery market in general, the (hard-) discount sector and specific market segments (e.g. fruit and vegetable, with additional competition from greengrocers, or alcohol, with additional competition from Off Licences) as well as niche areas which direct additional interest towards the main range and generate additional turnover.

Moreover, the UK market is not homogenous, so the competitive environment differs by region (for instance: J Sainsbury is very strong in the South, Morrisons in the North).

The general grocery market has been subject to a significant consolidation process in recent years (takeovers, e.g. Morrisons/Safeway, Tesco/T&S, Sainsbury/Bells, Kwik Save's departure from Scotland, Alldays' receivership and partial absorption by Co-op and the general conversion of formerly independent Co-ops into CWS, etc.). As a result of this concentration, fewer retailers are now claiming ever more market share.

Two of the market leaders, Tesco and ASDA, have been facing natural difficulties to further growing their turnover in core segments (Competition Commission constraints prevented both from bidding for Safeways, planning constraints have been making it more difficult to open new hypermarkets and further competition on price would have not only eroded their bottom lines, but their top lines too, given the sharp price competition already prevalent).

They have instead grown into non-grocery categories like clothing ("George" at ASDA, "Fred & Florence" at Tesco, followed now by Sainsbury's with "Tu") consumer electronics and entertainment products such as CDs and DVDs.

At the same time, traditional non-food retailers have started to integrate small convenience food counters into their stores (e.g. WH Smith, Boots).

Altogether, these developments make it relatively difficult to define the overall UK grocery market, including a definition by overall value, and to analyse precisely companies' respective market share.

It therefore appears inevitable that one must take a view on not only the available quantitative data, also the qualitative changes in the underlying trading formats, product offers, etc., in order to establish the status quo and to reliably predict trends.

The overall "grocery" market, as we would define it, does not comprise of solely groceries, but includes everyday household items (e.g. detergents, tissue ranges, basic body-care products, batteries, bin bags, etc.).

This is widely regarded as a GBP 100-120 billion market p.a., of which about 85% reflects retail sales and ca. 15% other forms of trade (restaurants, contract caterers, canteens, etc.). If we were to take 85% of GBP 110 billion and account for VAT at a rate of around 5%, this would indicate a relevant UK grocery retail market of about GBP 90 billion, net of VAT.

The big four (Tesco, Sainsbury, ASDA and Morrisons) account for around 70% of this market. All the other multiples have a combined share of ca. 25% of the market, with independents retaining a combined market share of around 5%. The other multiples comprise the "luxury brands" M&S (food) and Waitrose (John Lewis Group), the "convenience segment" of Somerfield and Co-op(s), the "discounters" Lidl, Aldi and Netto, and the "frozen food specialists" Iceland and Farmfoods, and a declining number of smaller multiples.

Looking now at the 25% market share belonging to the "other multiples", Waitrose, M&S, Somerfield and Co-op each claim similarly large slices of the grocery market, and their respective "luxury" and "convenience" offers account for about 16% in total.

The three discounters currently claim about 3 % of the grocery market, whilst the other 50 or so multiples share the remaining 6 % (Kwik Save and Iceland being the biggest of those 50, followed by Farm Foods).

Given the current number of less than 900 discount outlets altogether in the United Kingdom (Kwik Save alone had a similar number of stores about 5 years ago), it is instantly clear that market share in different catchments will differ significantly (from 0.2% in Oxfordshire, to approximately 10% in Doncaster, for all the discounters combined.)

Amongst the three discounters, only Lidl can claim a fairly balanced nationwide presence (i.e. broadly reflecting population figures), simply due to an initial location strategy which was not based on distribution costs. The others focused their initial expansion around their warehouses. In consequence, Aldi are slightly underrepresented in Scotland and the South. Netto are particularly strong in the North (100 out of 150 UK stores are in Yorkshire and East Midlands, the North East and the Northwest, with no presence in Scotland and only a handful stores in Wales.

When discussing market shares, one needs to take into consideration the fact that the discounters only offer a limited product range, which is one of the key features of grocery discount.

As a result, sales volumes and market share for product lines stocked by the discounters are generally comparatively high, particularly in categories which are not strongly brand-driven (low share of coffee and nappies, high share of frozen food, tissue ranges, cereals, etc.) and significantly higher than the general market share.

In summary, we see four segments within the grocery market, “the big four” “full range” operators (mainly hypermarkets) but partly and increasingly active within the “convenience segment” (i.e. Tesco Express and Sainsbury’s Local), the “luxury segment” (Waitrose and M&S) and the “discount segment” (Aldi, Lidl, Netto). The frozen food specialists (Iceland and Farmfoods) we would define as part of the convenience segment (frozen meals are a cheap form of convenience food and both operators appear to be “synergising” towards convenience to some extent).

The “big four” are untouchable. They have all got the critical size to run their businesses principally successfully (not talking about stock market expectations).

Tesco are a very good retailer and their permanent desire for significant growth-rates can only be satisfied by innovation (no way to grow sufficiently on the basis of added square footage alone due to the competitiveness of the grocery retail environment in combination with the planning environment and due to a lack of merger opportunities / competition authorities’ constraints). Groceries remain the key to footfall but footfall is now converted into additional turnover in all sort of areas (non-food, financial products, holidays, ...). Based on the obvious synergies, the grocery prices will stay competitive just as to maintain footfall whilst non-food can be offered more competitively than elsewhere, given the existing retailing-infrastructure which can be used at no significant extra costs. Great for the consumer, good for competition, challenging for the others, particularly the likes of Woolworth, HMV, Currys and Argos, just to name a few. Tesco’s offer is very balanced, they have got something for everybody or at least nearly everybody.

ASDA are not as diversified as Tesco. Their USP has long been price and later additionally their cloth range, but Tesco have countered them on both fronts. ASDA have the most homogenous store portfolio amongst the big four.

Sainsbury's are not primarily price focused. They seem to aim for people who are prepared to pay more for shopping at Sainsbury's, in recognition of appreciation of the Sainsbury brand which Sainsbury's promote accordingly. A lot of customers apparently appreciate the location of their Sainsbury's store (in combination with the brand image) sufficiently to settle for comparatively higher prices which makes this strategy worthwhile. Naturally, one would expect to see comparatively less growth from Sainsbury's under these parameters. (One major contributor to their current growth is Sainsbury's Local which still allows for more stores relatively easily, as it appears.)

Morrisons are still in a transition process, trying to fully integrate the operations acquired from Safeway. Given initial problems in getting ex Safeway customers to adapt to Morrisons, Morrisons seem to have incorporated a core Safeway feature into their strategy, this being "High-Low", i.e. very eye-catching offers on the one hand to attract customers to the stores in the first place and communicate great bargains but to recoup this investment by charging high prices for other products, ideally products which are not so much in people's price focus, working on the fact that most customers do not just buy the bargains but a full trolley. In its Northern heartland, EDLP elements still seem to play a more considerable role. Morrisons clearly put a lot of emphasis on their "Market Style" entrée, which they can do efficiently, given their considerable own food production plants.

In quality terms, there is no difference if individual products are compared on a direct basis. Customers' quality perception does obviously depend on not only individual products but range, store layout and service etc. and has got a lot to do with the perceived "image" of the respective retailer.

In terms of range, it appears that Tesco and Sainsbury are offering most "finest style" products, followed by Morrisons and ASDA. In terms of image, Sainsbury's seem to be still ahead of Tesco.

The biggest discrepancy between actual quality and perceived quality image exists in respect of both, the "luxury" retailers and "discount" retailers. Many of Lidl's and Aldi's products are of the same quality as M&S's and Waitrose's but customers perception still widely disacknowledges this matter, although a look at the ingredients lists on the packaging would easily provide enlightenment.

Then again, from a service level perspective (e.g. staff numbers), M&S and Waitrose are still ahead of the competition. This is clearly something that represents value to the UK customer too, and the high prices for mainly interchangeable produce are representing a deterrent for much of the population which others would probably appreciate ("entre nous"-effect).

Aldi are apparently trying to address the "image gap" proactively by means of advertising and merchandising, incorporating a few "M&S-features" into their adverts and stores.

Netto is still comparatively small in size with no truly nationwide presence, not expanding rapidly and do not seem to be taking the same ultimate approach to product quality as

Lidl and Aldi. Netto's offer is far more brand driven and could hardly be maintained if many more stores needed to be supplied (supply chain with quantity constraints, e.g. out of line stock, grey market buying).

We would not expect any major changes in the competitive environment within the foreseeable future.