RETAIL COMPETITION

Book Chapter

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INTRODUCTION

Forty years ago, a consumer who wished to purchase a prescription medication in the United States and many western countries would have probably walked into a local drug store. Today, a customer can fill prescriptions at any number of drug stores (e.g., Walgreens or CVS), supermarkets (e.g., Kroger or Albertson's), mass merchandisers or supercenters (e.g., Wal*Mart or Target) in town, not to mention mail-order providers (e.g., AmeriCan Meds 1-800-469-0955) and online pharmacies (e.g., www.Drugstores-Online.com). The option to purchase goods in so many different formats and channels is symptomatic of the heightened intensity of retail competition in today's consumer goods market, driven by discerning consumers with heightened expectations and widely-varying tastes, and rapid technological advancements that facilitate effective distribution of products and provision of retail services.

First, in many product categories, consumers now have the option to purchase from different retail formats. A retail format consists of a group of retailers that offer a common variety of product categories to consumers. Formats which have emerged in recent years, including mass merchandisers, supercenters and warehouse clubs are collectively known as *non-traditional formats*; while formats that with a longer history such as grocery, drug and department stores are referred to as *traditional formats*. Thus, retail formats compete with each other to attract consumers and this competition is referred to as *Between-Format Competition*.

Second, retailers within each format (e.g., CVS and Walgreen drug stores) compete with each other to obtain a higher share of the market, a phenomenon termed as *Within-Format Competition*.[1] Within-format competition reflects the traditional notion of retail competition, between stores of the same format. By definition, these stores offer a similar variety of

[1] Analyzing competition between and within formats is a modification of intra- and inter-type competition (see Miller, Rearden and McCorkle 1999 for an overview)

merchandise. For example, all department stores sell primarily apparel and goods for the home; all supermarkets sell perishable and dry grocery products along with health and beauty items; all warehouse club stores sell a broader variety of products, including food, packaged goods, apparel and durable goods. While the variety of products is very similar within a format, prices, category assortments, and store location strategies can differ in somewhat significant ways.

The focus of this chapter is to discuss these two types of retail competition – Within-Format Competition and Between-Format Competition, identify key trends, offer some insights and predictions about the future, raise pertinent issues, and promote ideas for future research. The chapter is organized as follows. Researchers have identified many factors that influence a consumer to purchase goods from a particular store, i.e., store patronage (Arnold, Tigert and Ma?). Of these, the following four broad retailer factors appear to be of paramount importance from the standpoint of retail competition.[2]

- *price* – Prices of items within and across categories, may change from week to week when implementing a promotional strategy
- *variety* – Breadth or number of categories typically carried by the outlet
- *assortment* – Depth or number of items within a category[3]
- *store location* – Where the retail store is located its store and how this affects consumers' cost of shopping

Retailers compete along one or more of these factors to garner their share of the market. Accordingly, we organize our presentation along these four dimensions. For each dimension, we first discuss the consumer trends related to that factor. We then draw on these insights, and other pertinent research, for understanding current trends in Between-format and Within-format retail competition, making predictions about the future, and raising competitive issues.

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[2] Quality of goods primarily relates to manufacturing and hence not considered here as a retail factor.
[3] The terms assortment and variety are used in the indicated manner following Levy and Weitz (p. 39).

RETAIL PRICE COMPETITION

Consumer Trend: Increasing Emphasis on Value

A weaker global economy, decreased consumer confidence (especially since the 9/11 terrorist attack), proliferation of alternate retail outlets, and the availability of price information on the Internet have all resulted in elevated consumer price consciousness. Consumers exhibit this price consciousness by purchasing on deal, shopping across stores and formats in search of bargains, patronizing discounters, and purchasing more low-priced private label products.

At the aggregate market level, consumers' emphasis on value can also be understood from the household income distribution. The distribution of US household incomes in the year 2000 is shown in Figure 1. The distribution is highly skewed: although the average income is $??,???, the median household makes less than $40,000 and more than 58% of US households earn less than $50,000 per year. Most households, therefore, do not have substantial disposable income and therefore tend to be price sensitive. Moreover, high-income households buy no more in most categories (e.g., toilet tissue, detergent, salty snacks) than low-income households. In fact, because high-income households spend more time outside their home for work, eating, and entertainment, they may actually buy fewer grocery items. As income levels continue to polarize, with more people taking lower-wage service jobs, this elevated level of price sensitivity is likely to persist in the near future, at least with respect to frequently purchased consumer goods.

Within-Format Price Competition

<u>Trend – Greater price competition within format:</u> Trends in consumer behavior and retail technology, both point to increased price competition across stores within a retail format. As discussed above, consumers are exhibiting greater price sensitivity when purchasing goods from retail outlets. In keeping with this consumer trend, retail technologies that reduce cost of operation to the retailers, and thus the retail price to consumers, have emerged. Automated check-outs reduce labor costs. Cross-docking, a technology-enabled activity, delivers goods directly from the manufacturers' warehouse to the retail store, obviating the need for retail warehousing, thus reducing inventory and storage costs. Sophisticated supply chain management systems such as Collaborative Planning, Forecasting and Replenishment (CPFR) can significantly reduce supply costs. Radio Frequency Identification (RFID) technology is improving product tracking significantly. Unlike bar codes which must be passed in front of a scanner, RFID tags can be read remotely by a device up to 60 feet away, reducing the time and labor needed to take inventory and facilitating faster stock replenishment when inventory levels are low. For example, according to one Sainsbury (U.K.) manager, RFID tags have reduced the receiving-function time from two and half hours to 15 minutes.[4]

Through adoption of these cost-saving technologies and other strategies, stores within a format are competing intensely on price; the one with the lower price will gain higher share. The phenomenal growth of Wal*Mart is a testament to the consumers' desire for low prices. To cater to the mass market of value-conscious customers earning relatively low income (less than $50,000), retailers now focus on offering low prices, in lieu of high service or premium products.

Issue – EDLP vs. Hi-Lo Pricing. As discussed in the previous section, consumers are becoming more price conscious and hence desire lower price. To offer value to customers, supermarkets generally use one of two pricing strategies: (1) frequent promotional discounts, known as HiLo pricing, or (2) everyday low prices, commonly abbreviated as EDLP. On average, EDLP stores offer lower prices than HiLo stores, but discounting by HiLo stores allows opportunistic shoppers to pay lower prices there compared to EDLP stores. By offering

[4] For more details on these technologies, see Sethuraman and Parasuraman (2005)

temporary discounts, HiLo supermarkets can price discriminate between opportunistic shoppers, who are willing to invest time and effort searching for bargains, and those who are not. Consumers who have low opportunity costs of time and/or enjoy greater benefits from searching for low prices will gather information from different supermarkets and may even shop at multiple stores. They gather information about weekly price deals by studying feature advertisements of competing retailers (Urbany Dickson and Kalapurakal; Urbany, Dickson and Key) and may even be willing to visit multiple stores to take advantage of price deals at each store, a practice known as cherry-picking (see Fox and Hoch 2005 for a detailed description of cherry-picking). A recent industry study finds that one-third of US households shop at multiple grocery stores in an average week (Food Marketing Institute 2003, p. 20).

One implication of price search is that consumers can be influenced to switch stores by retailer advertising (Urbany, Dickson, and Kalapurakal 1996, Briesch, Chintagunta and Fox 2004), though evidence suggests that promotions in only a few categories have a measurable impact on store traffic (Walters and Rinne 1986; Kumar and Leone 1988; Walters and MacKenzie 1988; Grover and Srinivasan 1992). Another implication is that cherry-pickers are not necessarily unprofitable customers, despite their higher price sensitivity. In fact, shoppers spend as much at their favorite store when they cherry-pick as when they visit only one store (Fox and Hoch 2005). However, cherry-pickers are far less likely to be profitable for other stores (not their favorite), which they visit primarily to hunt for bargains.

Most supermarket visits are to HiLo stores, but our knowledge of price competition between EDLP and HiLo stores can be enhanced by understanding who shops at EDLP stores and why. EDLP retailers require scale economies to support their low prices, so they operate larger (more square footage) but fewer stores in a geographic market (to draw customers from a larger trade area) compared to HiLo retailers. For most shoppers, visiting EDLP stores therefore involves more travel than visiting nearby HiLo stores. EDLP stores are also more time consuming to shop because of their larger footprint. Shoppers are loyal to EDLP supermarkets for one or more of the following reasons: (1) low opportunity costs of time – shoppers are willing to spend more time shopping, perhaps because they have lower wage rates or fewer time constraints; (2) greater benefits from shopping at low-priced EDLP stores – the lower prices found at EDLP stores can be applied to the needs of a larger family (Bell, Ho, and Tang 1998; Briesch, Chintagunta, and Fox 2004); (3) big basket shopping – infrequent shoppers buy a large basket of goods when they visit a supermarket (Bell and Lattin 1998), so the lower prices available at EDLP stores are effectively magnified by the big basket;[5] (4) Brand loyalty – brand-loyal shoppers are unwilling to buy whatever brand a HiLo retailer offers at a discount as a substitute for their preferred brand, limiting their ability to be opportunistic. The competitive implications for EDLP retailers are straightforward:

- EDLP retailers are more likely to be successful in markets where consumers have a higher opportunity cost of shopping and/or can apply low EDLP prices to a big shopping basket. Attractive markets for EDLP retailers have the following characteristics: high wage rates, a high incidence of working women and single-parent families, bigger families and larger average basket sizes.
- Urban areas, where basket size is limited by the transportation constraints are less attractive for EDLP retailers.

A substantial segment of shoppers switch between EDLP and HiLo supermarkets, depending on the purpose of their shopping trip (Fox, Metters and Semple 2003). Because they do not shop at consistent intervals (Kim and Park 1997), these shoppers sometimes stock up and sometimes simply fill in between major trips (Kollat and Willett 1967; Frisbie 1980; Kahn and

[5] Big basket shoppers also have less flexibility to delay purchases, which prevents them from changing the timing of their purchases to accommodate the deal schedules of HiLo retailers.

Schmittlein 1989, 1992). If the basket of goods they intend to purchase is sufficiently large, they will be willing to travel to a less convenient EDLP store; if the basket is not large enough, they will choose a more convenient HiLo supermarket (Bell, Ho and Tang 1998). Do shoppers switch between EDLP and HiLo retailers? A recent study finds that shoppers switch between EDLP and HiLo stores 15% of the time—about half the rate that they would switch if stores were chosen strictly at random (Briesch, Chintagunta and Fox 2004). The competitive implications of switching between EDLP and HiLo supermarkets focus on the shopping trip. The more often consumers shop, the more likely they are to choose a HiLo store; the less often they shop, the more likely they are to select an EDLP store. EDLP supermarkets can influence consumers' shopping frequency by providing incentives for big basket shopping, basically volume discounts, using frequent shopper programs or other, less targeted, means.

[Ed. Do you want to summarize some key takeaways from EDLP-HiLo here? Punchlines?]

Between-Format Price Competition

Prediction: Mass Merchandisers will keep price low and enjoy a widening price advantage. Mass merchandisers, though they do not all use an EDLP strategy, offer lower average prices than other formats on common items. In fact, a recent study of market basket prices showed that Wal*Mart offers 10% lower prices than supermarkets overall (reference???; other statistics reported about prices and promotion come from Fox, Montgomery and Lodish 2004). Drug stores offer prices similar to supermarkets, though slightly higher, on comparable items. Because they are less reliant on promotions, mass merchandisers make a smaller proportion of their sales on discounted items than supermarkets, which make a smaller proportion of their sales on discounted items than drug stores. In other words, mass merchandisers offer lower prices but fewer promotions, drug stores offer higher prices but more promotions, with supermarkets in between the two.

The only available study bearing on price competition between formats shows that mass merchandisers could increase revenues by raising their overall price levels, while supermarkets and drug stores would lose revenues by raising prices (Fox, Montgomery and Lodish 2004). Interestingly, they find that both mass merchandisers and supermarkets could increase revenues by offering more promotions, but drug stores would be better served by reducing promotions. Why do mass merchandisers keep their prices low, despite the revenue they could gain by raising prices and the already substantial gap between their prices and those of other formats? The mass merchandiser business model depends heavily on scale and it associated cost advantages; the greater the scale, the greater the cost advantage. Preserving and extending this advantage is critical to their long-term success. To date, mass merchandisers, particularly Wal*Mart, have maintained an almost single-minded focus on cost efficiency. Moreover, by using their capital to build supercenters, Wal*Mart and Target have shifted their product mix toward lower-margin grocery products in pursuit of higher store traffic and sales volume. The investment in supercenters is a credible commitment to maintain low prices. There is no reason to believe, given the obvious success of this strategy, that these mass merchandisers will raise their prices in the foreseeable future.

Trend – Small-store formats are becoming more cost-efficient and can offer increasingly lower prices. "Big box" retail formats such as mass merchandisers, supercenters, and hypermarkets are not the only retailers undercutting traditional formats on price. Dollar stores (such as Dollar General and Family Dollar) have rapidly become profitable purveyors of general merchandise in the US, while hard discounters have made inroads selling groceries in

Europe. These formats operate large numbers of small stores which are located closer to consumers. By using flexible logistics, information technology and effective centralized management of inventory and personnel, however, they are able to match the cost structures of operators of larger stores (Metters and Ketzenberg 2000). Metters, Ketzenberg and Gillen (2000) argue that “tightly linked networks of small stores … can actually enjoy the same scale advantages as those of superstores.” Wal*Mart obviously agrees, having announced plans to roll out its own small-store format offering products at the same prices found in its supercenters.

RETAIL ASSORTMENT COMPETITION

Consumer Trend: Not Too Little and Not Too Much!

When assessing consumer preferences for product assortment, it is important to understand that more is not necessarily better. Deeper retail assortments (stocking more items per category) increase the time and effort consumers must expend when purchasing in a category (Baumol and Ide 1956) and are more likely to cause consumers to become confused or frustrated. On the other hand, deeper assortments give consumers a wider range of items to choose from, increasing the probability that they will find the item they want. However, retailers incorporate the items with broadest appeal into the assortment first, so each additional item added will appeal to fewer and fewer shoppers. The benefit of adding additional items therefore diminishes as the number of items in the assortment grows. How deep retail assortments should be depends on balancing consumers’ benefit in finding what they want and the costs incurred in finding it. Research on this topic has focused on grocery stores, with mixed implications for retailers. A number of studies show that reducing category assortments has little or no negative impact on sales in those categories (Information Resources, Inc. and Willard Bishop Consulting 1993; Dreze, Hoch and Purk 1994; Broniarczyk, Hoyer and McAlister 1998; Boatwright and Nunes

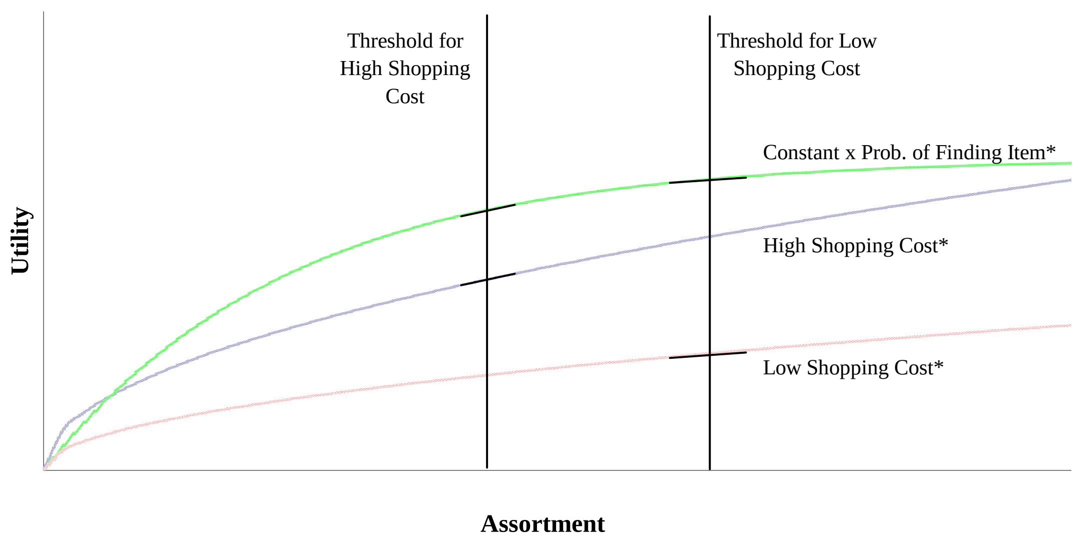
2001). More recent studies focus on how assortments affect patronage (Fox, Montgomery and Lodish 2004; Kadane et al. 2004; Briesch, Chintagunta and Fox 2004). These studies find that assortment reductions affect where customers shop, and that the primary cost of assortment reduction is likely to be the loss of store visits, not category sales. The relationship between assortment and patronage at a store is probably concave, with preference for that store increasing in assortment up to a maximum level, beyond which preference remains constant or decreases. Is the relationship in fact concave? Is there a threshold point above which consumers dislike deeper assortments? What is that threshold? Does it vary across consumer segments and/or product categories? These are important questions for future study.

Within-Format Assortment Competition

Trend – Tailoring assortment to meet local market conditions. Retailers of the same format also compete on product assortments. It is well-known that retailers modify the size and composition of their assortments based on the demographics of households in their trade areas. For example: grocery stores in markets with larger Hispanic populations offer more authentic Mexican food items; drug stores in markets with more elderly populations carry larger assortments of incontinence products while drug stores in markets with more families with young children will carry larger assortments of diapers; and department stores in trendier urban markets offer more haute couture fashions. The practice of customizing assortments for individual stores is known as micro-marketing. To the extent that it can be pursued cost effectively, micro-marketing is a valuable competitive weapon. However, because micro-marketing is inherently ad hoc, we will not present a detailed discussion in this chapter. We will focus instead on how the size of assortments systematically affects within-format competition.

As discussed earlier, the assortment size that consumers prefer reflects the tradeoff between their benefit from the availability of more items and the cost they incur when shopping a larger assortment. Because consumers' opportunity cost of time drives their cost of shopping, consumers with different opportunity costs will prefer different assortments (Briesch, Chintagunta and Fox 2004). To illustrate this point, figure 3 shows the difference in assortment sizes preferred by two shoppers, one with low shopping costs, the other with high shopping costs. Consumers with low shopping costs (because they have low opportunity costs of time) prefer larger assortments. Consumers with high shopping costs (due to high opportunity costs of time) prefer smaller assortments. Linking opportunity costs to demographics, the implication is that stores with higher wage rates, more working women, and more single-parent households in their trade areas should offer smaller product assortments.

FIGURE 3
Shopping Costs and Assortment Response



* The cost curves conform to Baumol and Ide's (1956) assumption that costs are a constant function of the square root of the number of products in the assortment. Also per Baumol and Ide, the probability of finding the most preferred item increases with the number of products in the assortment and asymptotes at one.

Between-Format Assortment Competition

Prediction: High assortment/high price and low assortment/low price formats are likely to be most successful. Each format sells a different variety of categories, but they also offer many different assortment levels within categories. As a result, categories which are sold in two or more formats are likely to have larger or smaller assortments in each. For example, the assortment of carbonated beverages in a warehouse club store is less than one-tenth the size of the carbonated beverage assortment in the average supermarket.

There is evidence that shoppers' preference for assortment varies by format but is highly correlated with the actual assortment levels offered. In packaged goods categories for example, supermarket assortments are generally twice as large as mass merchandiser assortments, which are generally twice as large as drug store assortments. Consistent with actual assortments, consumers' exhibit the highest preference for assortment in supermarkets, with deeper assortments increasing both the probability of patronizing a store and the amount spent there. Consumers are least sensitive to assortment levels of drug stores, perhaps because drug stores sell packaged goods primarily as a convenience for consumers (Fox, Montgomery and Lodish 2004).

Not surprisingly, larger families and households with lower incomes are more likely to shop at mass merchandisers (Fox, Montgomery, and Lodish 2004; Singh, Hansen and Blattberg 2004). Yet these households should also prefer larger assortments because of they have lower opportunity costs and higher benefits to search. Across formats, then, it appears that the desire for low prices supercedes the preference for larger assortments. This is consistent with the relative importance of price and assortment in peoples' choice of grocery stores (Arnold, Ma, and Tigert; Arnold and Tigert; Arnold, Oum, and Tigert: Briesch, Chintagunta and Fox 2004).

Interestingly, a recent study finds that individual shoppers' preference for assortment and sensitivity to price are highly negatively correlated, so that the more sensitive they are to prices, the less they value larger assortment, and vice versa (Briesch, Chintagunta, and Fox 2004). For retailers, this finding means that high assortment/high price and low assortment/low price formats are likely to be most successful.

Prediction: Retailers will segment markets based on the purpose of the shopping trip. Preference for assortment seems to be more dependent on the purpose of the shopping trip than preferences for other factors such as price and location [Ed. Is this true? I would think location preference is more likely to vary based on shopping trip. Why not just make and absolute statement instead of a comparison?] When stocking up, shoppers prefer stores offering larger assortments because the benefits of searching can be applied to a bigger basket of goods. On quick trips to fill in between stock-up trips, shoppers prefer stores with smaller assortments because of the higher opportunity cost of shopping. Thus, stock-up trips are more likely to be made to supercenters and supermarkets (Singh, Hansen, and Blattberg 2004), while quick trips are more likely to be made to convenience and drug stores—the purpose of the trip dictates shoppers' preference for assortment. In the future, retailers will segment markets based on the purpose of the shopping trip, not just customer-specific factors (e.g., demographics) or market-specific factors (e.g., urban/suburban/rural). A shopper may therefore be in the target segment on some trips, but not on other trips. Wal*Mart's new Neighborhood Market format is an example of just that; its small-footprint stores attract quick trips while Wal*Mart's supercenters are positioned for stock-up trips (Wal-Mart 1999 Annual Report).

Prediction: Supermarkets will not decrease assortments substantially, despite industry initiatives to do so. Trip-specific assortment preferences have additional implications for the competition between supermarkets and non-traditional formats, particularly supercenters. If supermarkets are to mount an effective defense against these formats, they must compete for consumers' stock-up trips, which represent a disproportionate volume of sales. If supermarkets were to cut their assortments substantially, they would risk relinquishing those stock-up trips to supercenters, warehouse clubs, and mass merchandisers. The lower costs touted by industry initiatives like Efficient Consumer Response and Category Management do not justify this risk. Thus, supermarkets will not make substantial assortment reductions, at least not in the foreseeable future.

RETAIL LOCATION COMPETITION

Consumer trend: Balancing Convenience and Costs

Store location, perhaps the longest-term decisions that a retailer makes, has long been considered a primary driver of retail competition (see The Legacy of Harold Hotelling 1978 and Brown 198? for detailed discussions of store location). Convenience is generally acknowledged as the most important factor in consumers' store choice decisions (Arnold, Ma, and Tigert; Arnold and Tigert; Arnold, Oum, and Tigert; Briesch, Chintagunta and Fox 2004). Stores located closer to the consumer are more convenient, and are generally preferred by consumers. However, in order to locate its stores close to consumers, the retailer must offer a large number of stores, each serving a small number of consumers. Thus, scale efficiencies are lost, and convenient stores are not able to offer prices as low as less convenient outlets. In other words, spatial convenience often comes at a cost. Retail properties themselves have cost implications, affecting pricing strategies and margins. For example, Wal*Mart's inexpensive rural store sites are an important component of its low cost structure. Consumers' store choice decision represents a balancing act between paying high prices for goods in more convenient outlets and low prices for goods in less convenient outlets.

Within-Format Location Competition

Trend: The need for agglomeration. Shopping convenience is multi-faceted, with the shopper's proximity to the store an important factor. Another factor is one-stop-shopping, which is discussed under product variety. A third convenience factor is agglomeration—locating stores near one another—which allows "virtual" one-stop-shopping. By agglomerating stores, consumers are afforded two distinct benefits: (1) They can fulfill different purposes on a single shopping trip, such as dropping off their dry cleaning, visiting a restaurant or café, doing their banking, shopping for apparel and also for food. This is known as multi-purpose shopping, and is a foundation for agglomerating stores in shopping malls and retail centers. (2) Consumers can also search across similar stores to maximize the value or quality of the product(s) they purchase. The second consumer benefit provides the rationale for locating stores of the same format near one another. In practice, this is quite common, as evidenced by "restaurant rows," "motor miles," etc.

Why would stores of the same format locate near one another? Competition between like stores is in some measure offset by mutual benefit both stores enjoy from being located near one another. The benefit is largely in the form of store traffic. Consumers prefer to travel to an agglomeration of retailers so they can search and compare, even if they must travel farther to do so. In other words, retail agglomerations become destinations for shoppers. Research suggests that such agglomerations have winners and losers. One study finds that specialty retailers should try to enter agglomerations before their competitors do (Miller, Rearden and McCorkle, 1999). Another study suggests that retailers with lower market shares benefit from locating their stores near competitors, while those with higher market shares do not (Fox 2001). Both studies point to the conclusion that <u>within-format competition for store locations is essentially a zero-sum game</u>. Gains by one retailer due to location advantage will result in losses for another retailer with less advantageous location (?). Therefore, retailers must attempt to be a first-mover in selecting an advantageous location. [Ed. Can you clarify the zero sum game and its implications?]

Between-Format Location Competition

<u>Trend – Large store formats such as supercenters being located closer to consumers in urban markets</u>. Spatial convenience—the proximity of stores to consumers—is specific to each format (Fox, Montgomery and Lodish 2004). Drug stores typically have high market penetration, so each store serves a small trade area. Grocery stores have only slightly lower market penetration, serving somewhat larger trade areas. Mass merchandisers, supercenters and warehouse clubs all have substantially lower penetration levels, and stores of these formats serve proportionally larger trade areas.

Recall that the purpose of a shopping trip dictates which format the shopper will visit. If the shopper is buying a big basket, then price looms larger than spatial convenience; if a smaller purchase is planned, then spatial convenience is relatively more important than price (Bell, Ho and Tang 1998). While consumers always prefer more convenient locations, this preference is therefore stronger for drug stores than grocery stores, and stronger for grocery stores than mass merchandisers (Fox, Montgomery and Lodish 2004), supercenters or warehouse club stores. Location preference is also becoming stronger among consumers in urban areas, fueled by commuting difficulties due to traffic congestions, and the availability of alternate shopping outlets closer to home. From a retailer’s perspective, the concentration of consumers in urban areas and the demise of less successful retailers and retail formats make room for growing successful retail formats such as supercenters to locate their stores closer to their target market.

Trend: Retailers are moving off the mall. Malls have prospered because locating stores near one another offers shoppers a different type of convenience. This convenience, the ability to satisfy multiple purposes on a single trip and search across stores efficiently, makes the mall a shopping "destination." Yet malls are falling out of favor with consumers (McKinsey report; other references????). Consequently, retailers are shifting their stores off the mall. Examples include JCPenney, which has announced that it will shift many stores to off-mall locations, and Sears, which announced that it will close more of its mall locations to open new stores on Kmart sites off the mall (this was touted as a primary reason for Kmart's purchase of Sears). Why the trend off the mall? In part, because one-stop-shopping can be accomplished more efficiently in emergent large-store formats such as mass merchandisers and supercenters. Furthermore, the lower prices offered by these emerging formats have reduced the consumer's return to price search.

RETAIL VARIETY COMPETITION

Consumer trend: One-Stop-Shopping equals Time-Saving!

Shopping convenience has several aspects, including spatial convenience, transactional convenience, and one-stop-shopping convenience. One-stop-shopping enables consumers to be efficient by buying everything they need in a single store. Annual surveys (conducted by AC Nielsen??) in 1995 and 2000 reveal that 36% to 44% of respondents feel that one-stop-shopping convenience is very important to their shopping decisions. Moreover, an AC Nielsen Homescan study (2002) finds that 63% of respondents agree that they are "constantly looking for new ways to get the household chores (like shopping, cooking, cleaning) done faster."

Between-Format Variety Competition

Trend: Growing popularity of broad-line retail formats. Retailers facilitate one-stop-shopping by offering a broad variety of product categories. For example, many consumers can now buy bananas, beer, frozen entrees, detergent, shampoo, blue jeans, television sets and computers at the same store where they can fill prescriptions, get their nails manicured and their hair cut, do their banking, rent a video , and eat a hot meal. The growing popularity of broad-line retail formats, such as mass merchandisers and supercenters (a supercenter includes a both a mass merchandise store and supermarket under one roof), combination grocery and drug stores, as well as warehouse clubs, is a testament to consumers' increasing desire for one-stop-shopping.

OTHER TRENDS IN RETAIL COMPETITION

Trend: competition between formats is for store visits, not for customers. Stores of different formats offer a different variety of categories, yet the categories often overlap. The catalyst of competition between formats has been the emergence of hyper-efficient mass merchandisers, in particular Wal*Mart, which carry an exceptionally broad variety of products. Mass merchandisers, and the supercenter format they pioneered[6], offer packaged goods categories in common with supermarkets and drug stores, apparel and home categories in common with department stores, and overlap with the offerings of most category killers. As a result, mass merchandisers and supercenters compete with supermarkets, drug stores, department stores and category killers for many purchases. Because of Wal*Mart's well-publicized cost advantage (which is also enjoyed, to a lesser extent, by other mass merchandisers), this competition has prompted many to sound the death knell of these other formats. Although predicting the demise of these formats is premature, there is evidence to support their concern.

[6] The supercenter format, modeled on Carrefour's hypermarket format, incorporates a mass merchandise store, a full service grocery store and several additional services including pharmacy, restaurant, automotive and vision care.

This evidence includes (1) the dramatic inroads that Wal*Mart's supercenters have made in grocery sales in the last decade—Wal*Mart now sells more grocery products than any retailer in the world and 22% of US shoppers now claim to shop regularly at supercenters (Food Marketing Institute 200?), (2) recent high-profile bankruptcies of category killers such as K-B Toys and Toys 'R Us, as well as (3) the general malaise among department store retailers. More specifically, a recent study finds that a supercenter opening cost a nearby supermarket 17% of its business, primarily because customers made fewer visits to the supermarket (Singh, Hansen and Blattberg 2004).

This study highlights the important point that competition between formats is for store visits, not for customers. Most consumers who patronized the supercenter continued to shop at the supermarket, albeit less frequently. Another study shows that the more mass merchandisers a household visits, the more grocery stores it visits as well (FML). Thus, for people who shop in multiple formats, a visit to a mass merchandiser is not a substitute for a visit to a grocery store.

Trend: Retail sectors are consolidating, with fewer, larger firms remaining. In response to the growing competitive threat from mass merchandisers, retail sectors are consolidating. This consolidation is due more to acquisition than organic growth. The underlying rationale is that larger retailers will have the scale necessary to reduce costs in order to compete with mass merchandisers. Examples of consolidation in US retail sectors include grocery, with Kroger, Safeway and Albertsons now comprising x% of sector sales, home improvement, with Home Depot and Lowe's now responsible for x% of sector sales, and office supplies, with Office Depot, Office Max and Staples representing x% of sector sales. A cautionary note … for consolidation to be successful, the remaining firms have to effectively exploit their new-found scale to reduce costs. This requires centralizing operations, in particular the buying function, and negotiating concessions from their suppliers.

Trend: Retail formats are blurring. Consistent with consumers' growing preference for one-stop-shopping (Messinger and Narasimhan 1997), traditional retail formats increasingly offer a wider variety of product categories. In general, retailers add categories that will increase store traffic. Examples include convenience stores and supermarkets offering fresh prepared foods for immediate consumption, supermarkets and mass merchandisers dispensing gasoline, grocery stores dispensing ethical drugs by adding pharmacies, and bookstores opening coffee bars. Because only a few categories can effectively drive store traffic, traditional formats also find themselves with more and more categories overlapping, a phenomenon known as format blurring.

Two Final Issues

Two final issues are highly germane to predictions about the future of retailing:

(1) Given Wal*Mart's remarkable size—over 7 1/2% of all US retail purchases are made at Wal*Mart stores (reference???)—and phenomenal history of growth, what does the future hold for this retail giant? More specifically, what will drive Wal-Mart's future growth or will its growth slow or stop? In the near-term, the answer is clear. Wal*Mart's capital expenditures will be focused on supercenters through 200?, at which point

Must take advantage of its operational efficiencies, must be sufficiently material to allow for meaningful growth

Assumes no major regulatory constraints (moreso in US than international)

(2) Will major retailers continue to "internationalize," exporting successful formats and operations to other countries?

Summary of Trends and Predictions

Put figure (sort of like figure 1) in here.