

***RESTRUCTURING OF THE RETAILING SECTOR AND THE
SUPERMARKET SEGMENT***

***Angela Maria Medeiros M. Santos
Luiz Carlos Perez Gimenez****

****Respectively, Manager and Engineer of the Automobile Industry,
Commerce and Services Department of the BNDES.
The authors would like to thank the intern, Carolina Barbosa Matos, and
the librarian, Arthur Garbayo, for their assistance.***

Abstract

The Brazilian retail sector is currently undergoing important changes that are culminating in a process of internal restructuring of both companies and the sector as a whole. In addition, due to an ongoing process of increasing organization and implementation of information technology, the sector has adopted a new form of relationship with suppliers, and has developed a wide range of knowledge regarding the habits of different consumers. The availability of this data, in conjunction with the concentration of the sector, is increasing the power of retailers relative to producers, in accordance with the worldwide trend toward the transfer of power in the productive chain, from industry to retail.

Restructuring of the Sector

Within the retail sector, the restructuring of companies in various segments has been observed. This process has the objective of adjusting and adapting the same companies to conditions of increased competition resulting from the well-known transformations in the Brazilian economy that took place at the start of the current decade.

A number of the more typical companies of the various segments, that have restructured their operational and financial structures, as well as their range of merchandise, are notable for having adopted some of the following measures:

- a transfer of stockholder control;**
- the closing of less profitable or unprofitable outlets, and the upgrading of existing outlets;**
- debt restructuring and negotiation**

- professionalization of management, that has traditionally been in the hands of families;
- a search for a more solid capital base, for example, through securitization of receivables as an alternative form of financing;
- increased use of commercial automation and information technology;
- perfection of knowledge of the end client;
- a change in the relative emphasis on operational versus financial profits;
- revival of planning tools, as well as the perfecting of tools for comparing and controlling costs.

Of particular relevance have been the changes to the economy that followed the implementation of the Real Plan. For companies that were already in the process of restructuring themselves, currency stability leveraged sales. Also of particular note were those companies that detected the need to make changes to their strategic positioning, or that decided to invest in methods and processes that would boost operating efficiency, and increase overall competitiveness, deciding on, and complementing such measures in the middle of the financial crises or economic recessions of recent years.

For companies that were already encountering difficulties due to administrative or operational shortcomings, the accompanying increase in competition exposed their inability to make rapid changes, most notably in shifting their operational focus, as well as in adapting to the newly competitive environment. Some of these experienced major financial imbalances, with traditional companies such as Casa Centro (household appliances), Casas Pernambucanas (textiles) and Mesbla

(department stores) pushed into bankruptcy or into seeking protection from their creditors.

The most adversely affected companies were the traditional department stores that suffered a certain loss of identity due to their frequent attempts to change, as well as their lack of operational definition. The measures that such companies took to change direction were the transfer of stockholder control and the restructuring of their debts, with this process entailing changes in operating methods and market positioning.

At the same time, a number of these prepared growth plans, expanding through acquisitions and associations. This trend is due to the conjunction of two factors:

- the sale of companies in difficulties, or that are disposing of assets to address the need to concentrate on their core business or to redefine their focus of activity; and**
- benefits from acquisition or association, that create synergies, lead to increases in market share, and the entry into markets where the former companies had significant shares, well-established operations and a strong brand.**

Examples of this process include:

- The acquisition of the Brastel and Prosdócimo networks by Lojas Arapuã during the 1980s;**
- The acquisition of the ‘Lojas Garson’, ‘Só Dinheiro’, ‘Ultralar’ and ‘Columbia’ networks as well as individual outlets of the ‘Tamakavi’ and ‘Ponto Forte’ networks by Casas Bahia.**

- **The acquisition of the department stores ‘Mappin’ and ‘Mesbla’ by the Vigor Group;**
- **The acquisition of the ‘Lojas Buri’ chain by the Ponto Frio chain.**
- **The acquisition of a number of the ‘G. Aronson’ chain outlets by Eletro (Pão de Açúcar Group).**

The restructuring of the Brazilian market is also being driven by an onslaught from the leading global retailers, most notably from Europe, whose home markets are already close to saturation, and who have decided to operate in other markets, attracted by the growth potential of emerging economies. In general, companies have adopted the models used by leading companies to increase their own efficiency, while companies entering the market have undergone an apprenticeship with regard to the difficulties of transplanting and implementing closed models to other markets with different cultural backgrounds and consumer preferences, and have found it necessary to make certain adjustments.

In addition to supermarkets, the arrival of foreign companies has also occurred in new segments, such as apparel (with the entry of J.C. Penney), bookstores (with the acquisition by Fnac of Ática’s megastores), and building materials (with the entry of two large companies, Leroy Martin and Castorama).

At present, the sector is undergoing a process of restructuring, with a view to providing continuity to the processes mentioned above. It must nevertheless be stressed that the economic policy measures adopted to curb demand, such as the raising of interest rates, and the increase in bad debts, have had a significant

impact on retailers, even if to different degrees, and have made it necessary for the sector to make a permanent strategic adjustment.

Changes and Internal Restructuring of Retail Companies

The aspects mentioned above, the growth in competition and the changes in behavior and habits of consumers have been fundamental in promoting significant changes in retailing. The growing competition between outlets with the same format, as well as between different types of store, have obliged companies to introduce cost reduction programs, and measures to rationalize operations, as well as to differentiate their services in order to attract more customers.

The modifications observed nevertheless cover a search for greater operating efficiency, as well as improvements in the management of companies, in ways that allow them to obtain sustainable comparative advantages that are increasingly centered on cost structures, product quality, and quality of services offered, rather than on selection of products and prices, which tend to be very similar.

These advantages are principally based on:

- **A correct definition of the mix of products, a vital factor for the profitability of companies;**
- **Combination of services in a form that is evident to the consumers, offering more for less;**
- **Information technology as an element of increasing importance in the retail chain, as well as a support to distribution;**

- **The deployment of new systems, tools and techniques, such as inventory management, management by category, *Electronic Data Interchange (EDI)*, *benchmarking* etc.;**

and

- **The concept of partnership and the exploitation of synergies between the activities of different agents in the value-added chain: producers, distributors, retailers and end customers.**

Special emphasis must be placed on the computerization of the sector, which is incorporating increasing levels of information technology, that is in turn providing greater knowledge on product flows, and efficiency gains in the producer-retailer chain, considering the degree of integration between companies that is possible through the use of computer networks. The accelerated introduction of this technology is redefining commercial operations, inventory volumes and logistical flows, as well as leading to an increasing degree of integration between industry and retailing.

EDI, for example, is one of the forms of integration between companies, that replaces commercial documents between suppliers and retailers, such as purchasing orders, invoices, embarkation documents, notice of receipt, etc. Another instrument is the *Efficient Consumer Response (ECR)*, by means of which, suppliers and distributors share information and work together to increase the efficiency of the whole chain, reducing costs and overall inventory, as well as providing better service to customers, for example, through a more suitable selection of merchandise.

Its principal tools are:

- The use of EDI to exchange documents between suppliers and supermarkets;

- Issuing of invoices by computer (CAO), based on information collected at points of sale;
- Use of Activity-Based Costing (ABC) to identify, analyze and allocate costs of activities carried out within the company, eliminating those that do not add value;
- Adoption of continuous and automatic replacement of inventory; and
- Management using product categories as strategic business units.

A relevant aspect is the change in the habits of Brazilian consumers, related, for example, to the desire for healthier products, a higher proportion of food consumed outside the home, and an increase in purchasing of semi-processed products. Another point to be considered is the greater segmentation of consumers and family types, with products being created to cater to this diversity.

These are important changes, since business now focuses on satisfying the desires and requirements of customers. Concepts such as customer loyalty building, and of the value attributed by consumers to the cost/benefit relation of purchases, are being exploited more heavily by retailers.

On the subject of internal restructuring, it is important to highlight the fundamental role of logistics, currently a major concern among retailers, which is also closely linked to advances in information technology. Many retailers have invested in distribution centers, with a view to centralizing purchases and achieving greater efficiency in their logistic systems.

Impact on the Sector

The impact of these changes is greater on account of the high degree of heterogeneity within the sector, which is characterized by the variety of store formats – many of which are operated at regional level, are family-owned, and are not stock exchange listed – as well as by different standards of management. It is therefore necessary to note that only the large companies that are the leaders in their respective sectors have been demonstrating such behavior.

Notable among the effects of such processes is the growth of concentration in certain segments, a greater presence of foreign companies, the adoption of more modern practices, and changes in the relationship between retailers and suppliers. The wave of restructuring is not limited to one sector, but applies to the main branches of retailing, such as supermarkets, department stores, and retailers of household appliances.

The major Brazilian retailers are already of fundamental importance for industry, although growing concentration in the principal retail segments could become a greater concern for industry, as a result of the concentration of sales in a small number of companies with regional/national coverage, and their consequent ability to pressure suppliers.

A greater degree of organization of companies within the sector, as well as the suitable use of information on patterns of consumption, combined with this concentration of the sector, places retailers in a privileged position with regard to suppliers. This power is being exploited by retailers, for example, to import products and launch their own brands, whose sales are growing within Brazil, even if they still represent only a small share of the market. For retailers, own

brands increase the profitability, most notably of low-margin products, in addition to reducing their dependence on the few suppliers that dominate the market.

With the aim of reducing dependence, but at the same time, broadening the range of products offered, retailers may develop local suppliers, and bring others from outside the country. In the latter case, they may start by importing to test the market, and subsequently install a factory. Importing is also an important escape route for own brands, most notably in segments where the underlying industry suffers from capacity shortages.

For suppliers, retailers' own brands may represent a higher level of utilization of their installed capacity, in addition to offering an easier way for smaller companies to enter markets controlled by oligopolies, as well as benefiting industries without brands, industries that lack distribution, and industries looking to establish Brazilian operations. For medium-sized suppliers, this allows better programming of production, guaranteed sales and lower marketing costs. In the light of retailers' own brands, however, traditional suppliers are being obliged to reinforce the value of their own brands.

Some of the large retailers also have the capacity to attract industries to Brazil, since they may offer economies of scale due to their purchasing volumes, and thus create greater competition among existing suppliers.

In addition to the changes resulting from the retail sector's attempt to increase its power over suppliers, in terms of buying power, suppliers are being affected by the

changes that retailers are implementing. This fact is particularly notable among supermarkets, since this is the most advanced segment in terms of introducing new working and organizational practices. Growing computerization, new methods of control and management of inventory, space and product categories also impose requirements on suppliers to invest in computerization and automation.

The principal groups have also been adopting measures to increase their operating efficiency, and maintain the profitability of sales, such as re-examining margins, reducing costs, more hard-line negotiations with suppliers and a redefinition of their product range. The sector has moved towards greater contracting to third parties of non-essential activities, as well as establishing logistical partnerships with their suppliers, and improvement of planning of inventory and purchasing.

This partnership is still incipient, and implies modifications in processes of organization, such as investments by suppliers to a degree that varies, in general terms, with their size. On the other hand, this process also demands better prediction by retailers of demand, and more efficient planning of purchasing, as well as a larger transfer of information on consumer habits, and increasingly efficient installations for unloading goods.

Within Brazil, the supermarket segment has been the most affected by these transformations, since it is facing ever increasing competition, and hence a growing need to increase productivity. Such transformations include increasing concentration within the sector, an increasing presence of international companies, as well as of global suppliers, and increased diversity of consumer behavior.

Supermarkets in Brazil

Within Brazil, there is a trend towards concentration. In 1997, the 20 largest supermarket and hypermarket chains accounted for 60% of the revenues of the 300 largest companies, while in 1994, this figure stood at 57%. The two largest chains, Carrefour and Pão de Açúcar, accounted for 26% of the revenues of the 300 largest companies in 1997, while the 5 largest and 10 largest represented 40% and 49% of these total revenues respectively (Table 1).

Table 1
Degree of Concentration of the Supermarket Sector within Brazil

	1994	1997
Revenues of 2 largest as % of Total Revenues	26	26
Revenues of 5 largest as % of Total Revenues	37	40
Revenues of 10 largest as % of Total Revenues	47	49
Revenues of 20 largest as % of Total Revenues	57	60

1998 projections show changes in the ranking of the 10 largest chains, due principally to the growth of the Carrefour, Pão de Açúcar and Sonae groups. It is estimated, for example, that Carrefour should grow by some 25% relative to 1997, due to the acquisition of 23 supermarkets from Lojas Americanas. Growth of around 40% is expected for the Pão de Açúcar group, following a number of acquisitions such as the 'Rede Barateiro' network. The major surprise in the ranking is the appearance among the five largest groups of the Portuguese retailer, Sonae, which acquired control of Companhia Real de Distribuição, of 85% of Cândia Mercantil and of Mercadorama (in the state of Paraná). The main mergers and acquisitions carried out last year are presented in Table 2.

Table 2
Mergers and Acquisitions in Brazil – 1997-98

DATE	MERGER/ACQUISITION
End-1997	Sonae acquires all the shares of Companhia Real de Distribuição
End-1997/1998	Pão de Açúcar acquires Freeway, Millo's and outlets from the Mambo, Ipcal and SAB chains
December 1997	Carrefour buys Eldorado
December 1997	Jerônimo Martins buys Sé from the Garantia group
April 1998	Garantia buys Abastecedora Brasileira de Cereais (ABC)
June 1998	The Pão de Açúcar group buys Barateiro
June 1998	ABC acquires five outlets from Serra e Mar
August 1998	Sonae acquires 85% of Cândia
September 1998	Comptoirs Modernes negotiates the acquisition of Lojas Americanas' supermarkets
November 1998	Sonae acquires Mercadorama
December 1998	J. C. Penney acquires control of Renner's capital
January 1999	The Pão de Açúcar group buys the Peralta chain

Source: Gazeta Mercantil.

One of the causes of this restructuring is the accelerating internationalization of hypermarkets and supermarkets, in which the need to expand and achieve a global scale of operations occurs in conjunction with the saturation of the large international retailers' home markets.

Brazil is highly attractive as a destination for new chains, since it has a large market into which new consumers may enter, a successful record by the international chains that are already established here, poor ability to compete among the existing players, and legislation that does not restrict the entry of large retailers. The share of foreign capital within the sector, most notably of European companies, has increased in line with the entry of the large chains into the Brazilian market (Table 3).

Table 3

International Supermarket Chains with a Brazilian Presence

GROUP	COUNTRY OF ORIGIN	YEAR OF ENTRY
Carrefour	France	1974
Sonae	Portugal	1989
Wal-Mart	USA	1995
Royal Ahold	Holland	1996
Jerônimo Martins	Portugal	1997

European groups continue to be the most favorably disposed to invest in Brazil in the short term, most notably the Auchan, Casino, Metro and Pinault-Printemps groups, that could establish operations in the near future.

Strategies

The strategies of hypermarkets and supermarkets vary on a number of points, even if such groups have a common objective of at least maintaining their share of the market, with this implying a drive to expand and increase productivity on a continuous basis.

The strategies of international groups, in particular, depend on their respective national cultures. Carrefour bases its strategy on distribution, while Wal-Mart lays emphasis on logistics and information technology. The large British retailers base their strategies on relationship marketing and own brands. Brazilian groups have adopted a little of each of these models.

In the face of the new challenges to which they are being exposed, Brazilian supermarkets and hypermarkets are investing to increase their ability to compete. While acquisitions and the opening of new outlets have occurred, a study carried

out by the Brazilian Supermarkets Association (Abras) in 1998, shows that the majority of Brazilian companies intend to grow by investing in their own stores.

Since investments in modernization and expansion are capital intensive, stock market listings and associations with foreign companies are starting to be seen as suitable strategies.

A trend towards expansion has been observed among the large groups, which are seeking to dominate regional markets and consolidate their market positions, as well as to increase their bargaining power with suppliers. At present, foreign and large Brazilian companies are expanding by building new outlets, and by acquiring small- and medium-sized chains. In the latter case, the combination of the levels of management and information technology and the lags in professionalization and undercapitalization makes such companies attractively valued targets for mergers and acquisitions.

For foreign companies, penetration of foreign markets through mergers and acquisitions is more attractive than organic expansion, since it accelerates the process of understanding markets and consumer habits. Within the sector, the expansion of Carrefour, Pão de Açúcar, Sonae, Wal-Mart and Jerônimo Martins has been particularly notable.

Such companies have also attempted to exploit their higher rate of store visits, or greater customer penetration rate than that of specialist retailers. In this way, hypermarkets have created new departments to sell a range of products including apparel, household appliances, personal computers, peripherals and supplies, and

have begun to use specialized sales staff, financing of sales and periodic workshops. Supermarkets have in turn sought to give greater emphasis to their own specialty - perishable goods. Both formats have attempted to become 'category killers' (highly specialized stores) in certain products.

With regard to store formats, some groups have adopted single formats, while others have adopted a multi-format approach in an attempt to cover the whole market with different retail concepts. At the same time, a trend has been perceived towards format diversification, with Wal-Mart, for example, starting to build 4,000 m² supermarkets.

The search for greater efficiency by companies involves human resources, logistics, building of customer loyalty, relationship marketing, category management, quality, ease of payment, partnerships with suppliers, own brands, services, variety and rotation of products, and the installation of round-the-clock stores. Some of these aspects are discussed below.

Logistics

With the growth of both companies and competition between them, logistics has become fundamental for hypermarkets and supermarkets, as have the associated issues of centralization versus decentralization and information technology.

The 'whether to centralize' issue revolves around the decision to build large distribution centers, which many large retailers have taken. In the 1970s, the most common model was decentralized sourcing. Today, there is a discernible trend towards centralizing distribution, even if there is as yet no dominant model.

A number of companies work with a mixed model, in which outlets are supplied from a central warehouse for certain kinds of products, while others are delivered directly by suppliers. Such suppliers tend to have more efficient distribution networks than retailers, and tend to deliver to stores, with some even having their own distribution centers, principally in the Northeast.

Technology and Automation

With the new competitive conditions within the sector that followed economic stabilization, the principal Brazilian companies have begun to invest in new technology more intensively. The large retailers began to automate their operations and introduced new tools such as EDI and category management.

In general, a store may be said to be automated when it has a computerized checkout. In addition to this innovation, however, the implementation of information technology also entails the reception area, the finance department, inventory and receipt of goods, as well as other sectors. According to Abras, around 60% of sales are already made at automated checkouts. An Abras survey of 650 companies carried out in 1998, indicated that use of technology is at the following stage:

- process automation, that covers optical scanners at checkouts, automated payments and receipts, automation of delivery of goods and ordering, is, on average, in the process of being implemented;
- process automation is occurring from the outside inwards. That is, starting with checkouts;
- the use of optical scanners at checkouts and automated payments and receipts, is at the most advanced stage;

- the use of technological tools is still incipient, and the majority of companies are in the ‘to be implemented’ stage;
- technological tools that are currently being implemented include warehouse management software, category management, space management, EDI and information systems; and
- category management software is at the most advanced stage.

Since it represents a new process, the majority of companies that are obtaining information through information technology are still learning to use the available data.

Relationships with Suppliers

Purchasing policy, new working and organizational practices, and the computerization of supermarkets and hypermarkets are leading to new patterns of behavior towards suppliers.

Among the current changes are the formation of partnerships between supermarkets and suppliers, as well as the agreement of long-term supply contracts. Such partnerships cover the replacement of products by the supplier’s employees, the sharing of information for new product launches or promotions, the definition with the retailer of forms of display of the products within supermarkets, monitoring of inventory levels, manufacturing of own brand products, etc.

This relationship generally takes different forms, which are chosen according to the relative power of the supplier and the retailer. The latter will analyze suppliers

to determine the best price, the forms of payment and the service that these offer. At the same time, a number of new factors are being observed with increasing frequency, such as punctual deliveries, guarantees of product quality, and a broadening of the services offered. Such points are being introduced gradually, and represent, depending on the product or the supplier, a significant change.

In seeking to boost profitability, retailers have sought to optimize and diversify their sourcing of merchandise. Among the methods available to retailers that reduce the power of suppliers and also differentiate their products are importing, the offer of own brands, and the development of suppliers mentioned at the start of this study.

Category Management

Category management refers to the more efficient distribution of sections in hypermarkets and supermarkets, in accordance with consumer preferences, and the maximization of revenues, as well as the display of products on the shelves, with a view to understanding the thought processes of consumers at the moment of buying, and thereby attracting them.

The benefits of category management include: the measurement of value of each supplier to the consumer; the measurement of profit on each brand; improvement of store organization and image to attract more consumers; increased impulse, convenience and complementary purchases; as well as permitting the analysis of the supply chain, predicting the necessary logistics and the cost of supply.

Building Customer Loyalty

Supermarkets have realized that among the many variables, customer loyalty is diminishing, implying a need to increase spending on advertising, as well as to devote more attention to the expectations of consumers. This process is causing the segment to wake up to the urgency of carrying out regular surveys of consumers, and of introducing frequent client programs. The launch, for example, of a smart card by a medium-sized supermarket chain in the suburbs of São Paulo (D'Avó Supermercados) built customer loyalty, and in parallel, a 26% increase in sales.

The gaining of customer loyalty is the result of a major effort to satisfy him or her, and involves not only rational but also subjective criteria, such as, for example, the display of large quantities of goods, credit and different forms of payment.

Information generated by checkouts make it possible to know each store customer and devise frequent client programs. Within Brazil, there are already examples such as the one mentioned above, even if no company is believed to have introduced a consistent customer loyalty building program, purely by analyzing data from sales points.

Conclusion

The retail sector is currently undergoing important changes that are culminating in restructuring processes, with a larger presence of foreign companies, and a greater degree of dominance by large groups.

The changes that have occurred and the restructuring that has been carried out so far, are already affecting the principal segments of retailing, although the supermarket/hypermarket segment is the most advanced in this process.

The adoption of more modern practices and 'organization of production' aims to guarantee market position under new conditions in which competition reinforces the importance of management within companies, as well as its ability to devise strategies and improve the efficiency of the supplier-retailer chain.

Implementation of information technology, modern methods of process organization and sourcing policy are some of the salient points that are leading, for example, to a new model of relations with suppliers, greater emphasis on logistics, management and training of human resources.

The principal groups have been adopting measures to increase their operating efficiency and to maintain the profitability of sales, and have tended to outsource non-essential activities to third parties, and establish logistical partnerships with their suppliers, as well as planning inventories and purchasing levels more effectively.

The implementation of these changes is occurring in different ways, but their combined effect is changing the profile of retailing within Brazil.