The Economist

Food retailing in Europe

The Germans are coming

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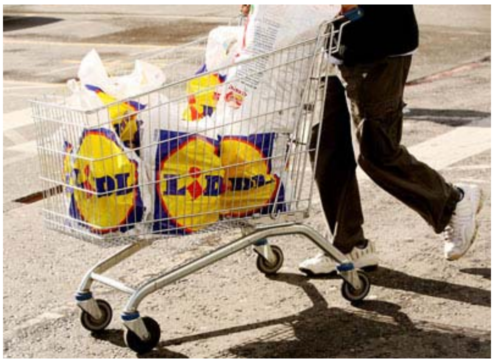
Germany's "hard discount" model of supermarket retailing is spreading in Europe



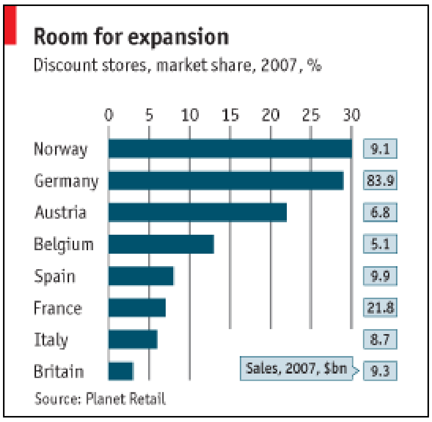
Guardian News & Media

IT IS as far from the charming ideal of French farmers' markets and small family-owned shops as you could imagine: strip lights glare down on a narrow range of products in ugly packaging, displayed in cardboard boxes piled on the floor and on low shelves. But sales are booming at the new Lidl discount supermarket in south-west Paris. Previously, the German chain stuck to the suburbs, where poorer folk live, says Fatouh Mourad, the store's manager. But rising food prices and widespread concern about "pouvoir d'achat", or purchasing power, in France, has given Lidl the confidence to push inside the city's limits.

As economic prospects worsen across Europe, discounters such as Lidl—and Aldi, another German chain—are taking market share. They generally charge some 30-50% less for groceries than ordinary supermarkets. In France, according to TNS, a research firm, discounters increased their market share to 11.2% in the second quarter of this year, up from 10.5% a year ago, whereas the share fell at Carrefour, the world's second-largest retailer. In Belgium a local discounter, Colruyt, is gaining share at the expense of Carrefour and other pricier chains. Dutch shoppers too are trading down to discounters, says TNS, and in Britain, where Aldi and Lidl struggled for years, they are now the fastest-growing grocers.

Discounters affect prices well beyond their own stores. "There's a massive global price-war in food retailing, much of it provoked by the gains by Aldi and Lidl and other discounters," says ***James Amoroso***, a food-industry consultant. Tesco, the world's fourth-biggest retailer, is fighting an all-out price war against Lidl in Ireland, and Belgium's Delhaize recently slashed prices in response to discounters. Carrefour, too, is under pressure to cut prices.

But can the discounters can hold onto their gains? Tesco's finance director recently suggested that they were merely having a "moment in the sun". He was quickly contradicted by the head of buying for Aldi in Britain, who pledged to open a store a week and win a tenth of the market (it has 2.9% now). In Germany, the heartland of discounting, cut-price operators have some 30% of the market, according to Planet Retail, a consultancy (see chart), and shopping at Aldi and Lidl is the norm for rich and poor alike. The two firms doubtless reckon they have a shot at replicating that position elsewhere.



They may well succeed, at least in some markets. "It's the best business model for retail in the world," says Philippe Suchet of Exane BNP Paribas in Paris. Discounters stock a fraction of the goods that a normal supermarket offers, resulting in fewer suppliers, a high volume of purchases and sales, and massive economies of scale. "You would find 16 brands of tomato ketchup in a normal big supermarket," says Paul Foley, managing director of Aldi in Britain. "In my store you will find a choice of one." Discounters mostly sell their own private-label goods, which are more profitable than branded goods, where the brand owner takes a big cut, and also more efficient—having bar codes in exactly the same place on every product, for instance, says Mr Foley, means faster checkouts.

Aldi and Lidl, which dominate the world of discounting, have annual sales estimated at €43 billion ($64 billion) and €35 billion respectively, compared with €102 billion for Carrefour. They are privately owned and can take a long-term approach to expanding abroad. New stores cost little to open and generate rapid sales, says Jürgen Elfers, retail analyst at Commerzbank in Frankfurt, so the discounters can expand during hard times more rapidly than any other kind of retailer.

The two firms are intensely secretive and say little about their expansion plans, but new stores are opening all the time. They are expected to expand quickly in France now that a law designed to keep discounters out has been changed. Lidl is poised to go into Switzerland, and in a rare interview last year its chief executive said it wanted to tackle America. (Aldi is already present in both markets.)

Lidl recently caused a fuss in Dublin, when it bid for a site on fashionable Grafton Street: critics complained it would lower the tone. But Lidl may not be so out of place, since middle-class people are changing their shopping habits to buy at least basic items at hard-discount stores. Five years ago in Britain, says Mr Foley, a quarter of his customers were well-off shoppers; now half of them are. Economic worries are part of the reason for that, of course, but Aldi appeals to middle-class shoppers because it manages to produce goods of surprisingly high quality at a low price.

What should perhaps worry conventional supermarkets most, in fact, is that the discounters have proven themselves adept at moving upmarket, even as they retain most of their efficiencies. In many markets, for instance, Lidl now stocks a limited range of branded goods alongside its cheaper own-label items. In Britain Aldi used to be known for tinned and packaged foods, but has introduced fresh and delicatessen products. In Germany Lidl even tried to buy a chain of organic supermarkets until an outcry scared it off. But there is a limit to the range of products discounters can stock while maintaining the efficiency of their model, cautions ***Mr Amoroso***.

In recent years the German discount model has experienced only one big setback. In March Lidl pulled out of Norway after four years of trying to establish itself. Rema 1000, a local discounter, will take over Lidl's stores there. Executives at the posher kind of supermarket must be longing to know how the Norwegians did it.