Bankwest Future of Business: Focus on Supermarkets

2018
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Key insights

Foreword

Understanding factors impacting your industry, and how other businesses in your industry are performing, can be a great gauge for how your business is tracking.

The Bankwest Future of Business: Focus on Supermarkets Report is designed to give you a snapshot of the current and expected future state of your industry, which could help you plan and spark ideas. The report covers Australia’s supermarkets and grocery stores, providing insight on grocery and specialised food retailers, summarising trends based on statistics from IBIS World, the Australian Bureau of Statistics and other reputable sources.

The large industry players continue to compete and drive down prices for Australian groceries, with consumer prices for food and non-alcoholic beverages declining by 0.7% in the year to September 2017 compared to Australia’s Consumer Price Index (CPI) growth of 1.8%. Having enjoyed a duopoly for many years, major supermarkets Coles and Woolworths now face one of the most fiercely competitive industries due to the rapid growth of international retailers competing for a share of the $100 billion industry. Discount retailers Aldi, Costco and Kaufland are all rapidly growing their market share.

The grocery price war has also made it difficult for the smaller businesses in the sector, with the number of grocery retailers employing fewer than 20 staff declining by 10.6%. However, opportunities remain for smaller operators to diversify into more specialised markets where such operators are thriving.

Australian supermarkets and grocery stores are projected to experience annualised revenue growth of 1.8% in the five years to June 2022. Technology and big data will become increasingly important as companies seek to better understand their customers and offer greater convenience. However, success hinges on their ability to provide customers a seamless digital experience and maintain a high level of trust in these channels.
Industry overview

Supermarkets and grocery stores across Australia continue to compete on price, with the largest Australian supermarkets battling for a share of the $100 billion market.

Establishments

Australia’s large supermarket chains dominate the market in terms of revenue. Smaller players are finding it hard to remain competitive in the grocery and supermarkets industry, with 10.6% of supermarket and grocery stores with less than 20 employees exiting the market in the year to June 2016. However, this was not the case for specialised food retailers, with the number of stores employing less than 20 employees rising by 3.8%, compared to a 7.5% decline in stores employing more than 20 staff.

Change in number of Australian supermarkets and grocery stores (June 2015–2016)

<table>
<thead>
<tr>
<th></th>
<th>Jun-15</th>
<th>Jun-16</th>
<th>Yearly change</th>
</tr>
</thead>
<tbody>
<tr>
<td>Less than 20 employees</td>
<td>2,631</td>
<td>2,351</td>
<td>-10.6%</td>
</tr>
<tr>
<td>20 employees or more</td>
<td>7,079</td>
<td>7,194</td>
<td>1.6%</td>
</tr>
</tbody>
</table>

Source: ABS 8165

Breakdown

The product range offered by Australia’s industry giants has evolved during the last five years, with the expansion of private food label goods, organic food and healthy options, and an increased focus on convenience fuelling demand for ready-to-eat meals and pre-cooked packaged meals.

Source: IBIS 2017
What’s driving industry growth?

The entrance to the Australian market of international retail giants has increased competition among supermarkets and grocery stores. These new entrants are competing heavily on price in a bid to grow market share. Food and non-alcoholic beverage prices have risen slowly, growing by just 4.0% in the five years to September 2017, compared to a 9.4% rise in Australia’s CPI.

Food and non-alcoholic beverage CPI vs All Group CPI (2012 – 2017)

Price competition has allowed some supermarkets to grow their market share and ultimately benefited Australian shoppers.

How are industry players competing?

- Woolworths $1 billion investment into reducing grocery prices is expected to fuel sales growth
- The entrance of AmazonFresh is anticipated to increase price competition during the next five years due to lower prices and strong negotiating power
- Sticking to generic name brands to drive lower prices relative to other market players

Three trends shaking up the grocery market

Gluten free - Increased number of Australians avoiding wheat by opting for gluten-free options without formal diagnosis of celiac disease

Gourmet – National rise in preference for premium foods has increased among certain customers, supporting the $896 million industry

Organic - The $2 billion organic food industry accounts for $26 spending per person, with this figure likely to increase among millennials and those with young children
Spotlight on Australia

International grocery retailers have challenged local supermarkets on price, with profits declining across the industry. Cannibalisation is now a real concern for the sector, with an estimated 80.0% of supermarkets facing competition from a same-brand store within 10 minutes' driving distance.

Australia has the second highest proportion of grocery shoppers preferring to use self-checkout, with 52.0% of Australians liking the convenience self-checkout provides.

47% find self-checkout simple to use
54% would prefer a larger bagging area
44% could not find an attendant when needing assistance

Market share of Australia’s supermarkets and grocery stores

- **Woolworths**: 36.8%
- **Westfarmers Limited**: 16.2%
- **Metcash (IGA)**: 10.9%
- **ALDI**: 8.6%
- **Other**: 7.5%

Source: IBIS 2017
Spotlight on Western Australia

Perth has the lowest CPI for food and non-alcoholic beverages across all Australian capital cities. Perth consumers spent 1.0% less in September of 2017 compared to the previous year.

Food and non-alcoholic food and beverage CPI (September 2017)

Prices for Perth fruit and vegetables saw the largest decline in the year to September 2017, declining by 6.9% in the year to September 2017. Changes in Perth grocery prices, likely driven by the entrance of Aldi and the local economic environment, included:

- **Bread and cereals**: 1.6%↓
- **Meat and seafoods**: 0.2%↓
- **Dairy**: 1.4%↓
- **Fruit and vegetables**: 6.9%↓

The price of an average grocery basket in Western Australia has declined by 5.1% across Australia’s two largest retailers.

### Average price:

<table>
<thead>
<tr>
<th>Year</th>
<th>Average price</th>
</tr>
</thead>
<tbody>
<tr>
<td>2015</td>
<td>$177.7</td>
</tr>
<tr>
<td>2016</td>
<td>$168.6</td>
</tr>
</tbody>
</table>

Source: ABS 6401
What does the future hold?

Technology and innovation essential for cost competitiveness

New technologies that help contain costs will be essential for supermarkets and grocery stores’ sustainability of low prices. Additionally, businesses will increasingly target their customers through digital platforms to improve the customer experience and offer greater convenience.

- Digital price tickets allowing for live pricing changes
- Focus on data to better understand customer preferences
- Faster delivery systems giving customers greater convenience
- More focus on online channels encouraging customers to purchase online

Customer likelihood of purchasing groceries online

<table>
<thead>
<tr>
<th>Percentage</th>
<th>Average grocery buyer</th>
</tr>
</thead>
<tbody>
<tr>
<td>3.1%</td>
<td>Bought groceries online in last 4 weeks</td>
</tr>
<tr>
<td>28.7%</td>
<td>Would consider buying groceries online in next 12 months</td>
</tr>
</tbody>
</table>

Source: Roy Morgan 2016

How are supermarkets responding to competition?

Major players Coles and Woolworths are focusing on quality through private label products to fend off competition from international giants Aldi and Costco²

Coles’ ‘everyday value’ strategy aims to permanently reduce the shelf prices of approximately 4,100 products³

Grocery chains are expected to open fewer stores, instead focusing on refurbishment driving sales growth

Providing ‘click and collect’ shopping options allowing customers to order at home and pick up in store

² Canstar Blue, 2016
³ AFR, July 2017
What challenges does the industry face?

Grocery stores have invested heavily in self-checkout, reducing expenditure on wages. However, this has created a new challenge of theft as reduced employment has meant less supervision of customers. The cost of retail crime is estimated to be $4.5 billion per year.

**Challenges:**

- Depersonalisation of the shopping experience
- Identifying effect technology has on theft
- Creating better processes to manage theft

The decline in the number of smaller supermarkets and grocery stores reveals the difficulty in maintaining business growth amid intense price competition. Smaller stores in areas of strong competition may need to rethink their value proposition and focus on niche customer segments by offering highly specialised products. The number of Australian grocery companies is expected to shrink by 1.4% in the five years to June 2022, while establishments will rise by 1.0%.

Other challenges for smaller operators include:

- Rise of online-only grocery ‘dark stores’
- Smaller scale limits ability to invest in technology to collect and leverage data insight
- Lower supplier bargaining power

Consolidation among the mainstream grocery stores and supermarkets creates opportunities for smaller operators to diversify into high growth niche and higher priced markets. The Australian organic market is expected to reach $2 billion revenue in 2018.

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2 Inside Retail Australia, June 2017
Where do the opportunities lie?

The rise of ‘dark stores’ that sell groceries only to online customers highlights an opportunity for supermarkets to reduce operational costs and provide greater value-add delivery services.

Research by Nielsen suggests continued growth in online grocery shopping among Australian shoppers.

- **20.1%** growth in Australian online grocery sales
- **24.0%** have ordered groceries online in the past
- **55.0%** are willing to purchase online groceries in the future

Technology will not only be used in facilitating customer purchases, major supermarkets will look to further leverage data to:

- Better understand their customer
- Retain customers and improve loyalty
- Track purchase history
Continued automation and use of self-service checkouts will see lower skilled jobs and employment decline by 2.5% in the five years to June 2022. However, grocery stores will increase employment in skilled trades, marketing and business intelligence, which will see industry wages rise by 15.0% during the period.\(^3\)

Forecasted industry growth

Revenue is projected to rebound after a modest 0.6% decline in the year to June 2017, growing by 9.3% in the five years to June 2022.

Actual and projected supermarket and grocery store revenue (2008-2023)

Over the next five years, the supermarket and grocery store industry will experience:

- **1.0%** rise in establishments
- **1.4%** decline in businesses
- **2.5%** decline in employment

Source: IBIS 2017
Sources


Atipaldi, R. Grocery e-commerce: The 20-20-20 opportunity, Nielsen Australia, November 2016

Australian Organic, Australian Organic Market Report 2017

Choice, Supermarket Price Survey 2017

Cloutman, N. Supermarkets and Grocery Stores in Australia, IBISWorld, October 2017

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Mitchell, S. Aldi's fresh new format a 'game changer': Morgan Stanley, Australian Financial Review, September 2017

NCR, Self serve checkout: A global consumer perspective, 2014
At Bankwest, we know that Business Banking is about more than just financial solutions.

We provide banking solutions to many of Australia’s leading businesses, including those in supermarkets and grocery stores. Whether you require straightforward banking or a more customised solution, our team of experienced banking specialists can help.

Speak to one of our Business Banking Specialists today. Call us on 13 7000.