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Retail trade

«When sales are doing badly here, they do well somewhere else»

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Internationalisation of distribution becomes an important matter in times like the present, characterised by a steep downfall of domestic consumption together with fierce competition. Never before was the sentence more true that says: «When sales are doing badly here, they do well somewhere else».

Some years ago, it was enough to have testimonial presence at half a dozen culturally similar countries in the vicinity to show that a retail concept could go international. Today, overdependence on the market of origin is considered a stigma that, combined with local adverse conditions such as a reduction in sales, puts credibility in jeopardy.

Compared with manufacturing companies, those in distribution are particularly complex and face a hard task on their way to internationalisation. Dawson & Mukoyama (2003) identified some causes proving this assertion. For instance, retailers have their assets scattered, especially if their geographic spread is big, whereas industrial companies have maximum efficiency when concentrating them. This obliges to pay more attention to spatial and cross-border coordination of systems, which are tighter as distribution companies go international.

Another difference highlighted by these authors are the involvements of unequal cost structure when expanding abroad, especially complications due to operating with different currencies. More essentially, transnational activity demands sensibility towards and adaptation to the local culture that is not highlighted as strongly when talking of activities of industrial and service companies.

Internationalisation of retailing through commonly accepted generalisations

Scope and institutions

Setting up and managing distribution channels is indispensable in competition between retailers. This competition has extended its scope from the local to the international and more recently the global level.

Attention paid by academic literature to internationalisation of retailing produced its first systematic pieces of work in the 1950s. They were descriptive studies of the big US companies as they were expanding around the world (e.g. Sears & Roebuck in Cuba in the 1940s).

During the 1970s and 1980s, and still within this descriptive emphasis on the characteristics of formats, innovative detailed literature and its struggle in conquering foreign markets produced pieces of work focusing on the distinction between local, international and global trade and its implications on standardisation or adaptation to new target markets (e.g. Salmon & Tjordman, 1989).

Transnational activity demands sensibility towards and adaptation to the local culture that is not highlighted as strongly when talking of activities of industrial and service companies.

In the 1980s, the world's biggest retail formats were the object of study. A brief overview over these firms shows that they are essentially US companies that based their sales on high-turnover consumer products (HTCP) or at least depended on such sales together with others. This research highlighted cross-border domination of the supply chain. Wal-Mart, Target and Kroger were some examples focused on in those years.

Towards the 1990s, the focus of academic literature moved to management and the scope of retail activity in the globalisation process, its causes and effects.

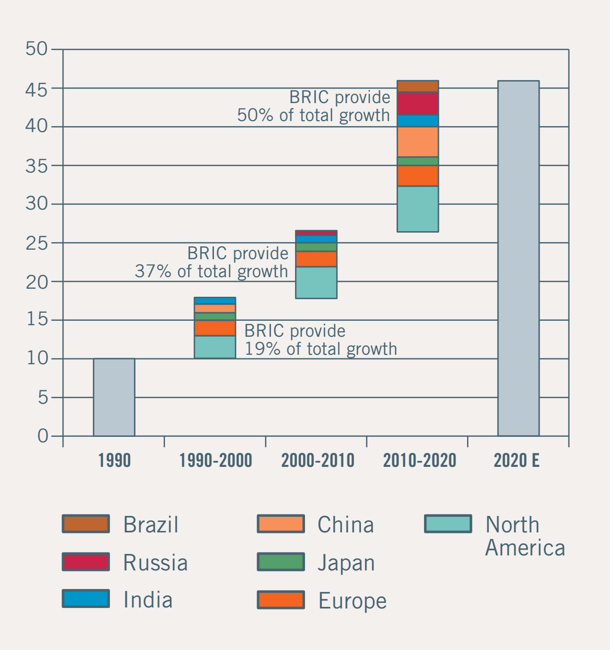
Today, the academic interest has moved into the same direction as that of the consumer, and the focus on supermarkets and their logistic systems has been replaced by the study of global distributor brands like consolidated H&M, DIA, Inditex, Amazon, IKEA and Mango or those that have started this process at a firm pace, like Sand, Intimissimi, Next and Uniqlo, among which there are many from Catalonia: Tous, Rosa Clarà, Desigual, Custo, Pronovias, GAES, Punt Roma, Castañer and Sita Murt, to name some. They are smaller in size than the supermarket chains studied in the 1980s and more heterogeneous as to their country of origin, but they have clear and very differentiated concepts, powerful brands and a footprint in dozens of countries.

The evolution of the industries, the reasons, the decisions of giving priority to any given countries and the role played by the different access modes and formats in the expansion process will be the main focus in this century.

The Catalan company Mango is among the already consolidated global distribution brands.

As to geographic variety, graph 1 shows that the future of retail belongs to other regions than today, not based on the current size but on their potential growth. This graph shows the importance of retailing in the big emerging powers in the future as opposed to apathy in mature industrialised markets. It also shows the more modest but also more accessible opportunity of small emerging markets, particularly the closest ones.

Graph 1. Growth of the share in global expenditure



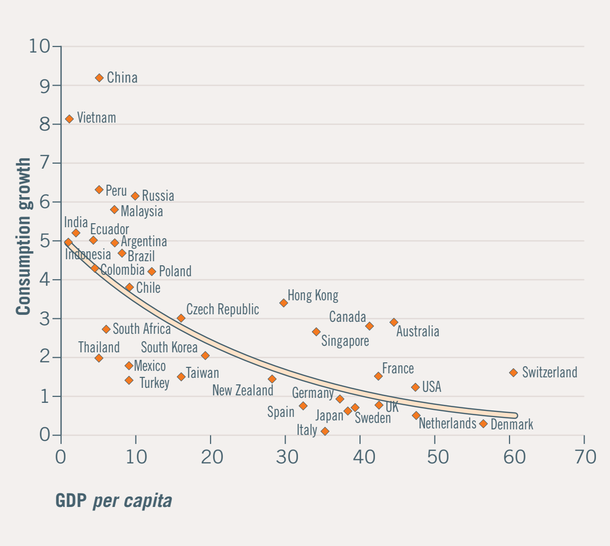
Source: The Goldman Sachs Group, INC (Nov. 2009). «Europe: Retail».

▲ The graph shows that the future of retail belongs to other regions than today.

The decreasing function as the GDP (Gross Domestic Product) develops is determined by two ratios. In the ordinate, it is annual consumption growth measured between 2006 and 2010 (estimate), while the abscissa shows a second ratio, GDP per capita. This function shows the scarce growth margin promised by advanced economies. Spain belongs to the least attractive cluster, combining low growth with medium GDP per capita.

This graph does not break down the consumption growth variable in the ordinate. Behind low growth of Spanish consumption (as can be seen, not much worse that that of the EU-15) lies a high unemployment rate, considerable family debt, stocks resulting from fifteen years of uninterrupted consumption growth – in the form of newer durable goods (apparel, furniture, personal information devices and cars) – and a return to savings rates unheard in the last two decades. Spaniards behave increasingly like Northern Europeans, but with less available income.

Graph 2. GDP per capita (2008) and growth of consumer expenditure



Source: The Goldman Sachs Group, INC (Nov. 2009). «Europe: Retail».

▲ Spaniards behave like Northern Europeans, but with less available income.

Graph 2 shows the share of the big emerging countries in consumption growth, which can impose some increasingly far, complex and risky expansion demands on Spanish retailers. It is no surprise that some most striking distribution formulas in this decade have come from retailers having entered markets with a high country risk (Inditex with Stockman to enter the Baltic states and Russia) or even an enormous one (Inditex with Tata to serve the Indian market from 2011).

Opportunities

Another variable to which literature on retailing pays attention says that solid presence in the domestic market is an indispensable requirement for successful international expansion, which is justified by two reasons (Alexander & Quinn, 2002). Firstly, «it contributes to learning and developing management skills» and secondly, «it creates a membership network for potential candidates».

Solid presence in the domestic market is an indispensable requirement for successful international expansion, although there are exceptions.

Of course, there are exceptions: Desigual carried out its international expansion together with local one, supporting one another, especially in its wholesale trade.

Consulted studies (e.g. Kacker, 1985) classify causes for expansion in two big motivation groups: push and pull. When a retailer finds a small domestic market or one going through deep recession in consumption or subject to tight regulatory pressure, they can feel pushed to expansion. Ahold to South America and Jerónimo Martins to Eastern Europe are examples of HTCP retailers pushed outside their country due to the size of their markets of origin (Netherlands and Portugal respectively). However, when Carrefour opened its first hypermarket in Catalonia, Pryca in El Prat outside Barcelona, it was our country as a market what pulled them over.

The attractiveness of a country based on its pull effect is determined by its size, current or potential income of its residents and cultural proximity to the country of origin. Low salary costs, an attractive real estate branch and absence of competition were the main causes of the internationalisation of Carrefour. There is no doubt that for most European retailers, especially Spanish ones, push factors will dominate over pull ones in 2010.

A second concept in studying internationalisation opportunities is graduality. As early as in 1977, Johanson & Vahlne stated that retailers follow an expansion pattern by which expertise and know-how add on with each entry into new markets requiring increasingly complex formats and being culturally or geographically more distant from the country of origin.

Thus, Spanish companies go to neighbouring markets like Portugal (GAES and Tous) or France (Inditex) first. Central and South America is then usually the next step in internationalisation (GAES), which has the burden of distance but the advantage of cultural proximity. There is a very positive image of Spanish brands in Latin America, which explains why Mexico was the first market on the way towards internationalisation at Tous (being currently their second biggest market), Massimo Dutti and Inditex within twenty years and more recently at Punt Roma, or that Argentina is so for GAES. The second biggest market for DIA is France, and 25 years after opining their first shops in Barcelona, Brazil will become the third.

Confirmation of this graduality and the risk of ignoring it becomes apparent in an overview of recent expansion of five Spanish retailers sharing their international ambition but with a difference in age (Mango, Zara, Tous, GAES and Desigual) and branch.

Zara, for instance, opened 137 shops in 2006, of which only 20% were domestic openings. In 2008 they opened 159, of which only 14% in Spain. In 2009, Japan, Latvia, Lithuania, Poland, UAE, Thailand, Lebanon, Serbia and Russia were the main destination countries of this expansion (as well as other less exotic ones like Italy and Belgium). Shop closures in that year concentrated on Spain, France and Greece, some of its oldest markets.

Mango opened in its turn 134 new shops in 2008 (205 in Spain). The UAE, Estonia, Norway, Azerbaijan, Romania, Portugal, Iran and Iraq were their destinations. Only 8% were local openings in 2009, the remaining 92% being spread over Belarus, Georgia, Iraq, New Caledonia, Kazakhstan, Korea, Turkey, China, the Philippines and Japan.

Tous opened only 16% of its new shops in Spain in 2009, but openings abroad are still mostly in geographically or culturally close destinations. America was among its most active markets in 2009.

GAES is still developing the Spanish market as a priority, with 75% of its openings in 2009.

DIA opened more than half of its shops in Spain in 2006 but less than 20% in 2009. Desigual went from opening 71% of its shops in Spain in 2007 to 13% in 2009. 2008 was divided equally between the local and the foreign market, showing a retailer with an aggressive expansion but still with some potential in its domestic market, thus deviating from graduality as suggested by Johanson & Vahlne.

Managing competencies

Apart from the impact of the skills of managers in distribution companies, their causes have also been explored by academic literature. What is more beneficial, having managers with international experience to ensure success or the effects of this experience on the skills of the management in its fulfilment, no matter the geographic scope of the market? Are these competencies of managing teams the cause or the effect of internationalisation?

The most internationalised European retailers are those focusing on high-turnover consumer goods (HTCP).

Authors conclude that it is much more important to have a management able to tackle internationalisation beforehand than management of internationalised companies being more competent, and that the only benefit increasing in the course of expansion is the relatively powerful position vis-à-vis the suppliers, which is higher than that of companies focusing on the local market only.

Without determination, competence and tangible commitment of the management there is no way forward. The biggest distraction is a munificent local market. The most internationalised European retailers are those focusing on high-turnover consumer goods (HTCP). Operators like Carrefour, Metro, Ahold, Tesco and Auchan are clear examples. There is no Spanish retailer in this group of internationalised pioneers, although DIA, a discounter belonging to the Carrefour group, has its headquarters, its whole management and most of its 4000 discount shops in Spain, from where it operates in fifteen countries in America, Europe and Asia.

A study by Myers & Alexander (1996) justifies the contribution of manager ambition to this process as it looks into the different attitudes of executive managers at fifty of the then biggest HTCP retailers from France, Germany, Italy, the Netherlands, Spain and the United Kingdom. This study stated that in 1995, French retailers were convinced of the internationalisation opportunities of their business. Germans were as well, but only in neighbouring markets (Austria or Belgium) they could serve from Germany. The British and Dutch had limited confidence, while Italians and Spaniards had not international expansion among their priorities.

At that time, Spanish and Italian managers were rather concentrating on the opportunities in domestic markets. The French were the most determined. So it can be concluded that determination of managers and their commitment in tackling ambitious challenges were rather the cause than the effect of internationalisation. Without talent at their service, it would be better to stay at home and languish.

Entering the same markets as all competitors is a risk factor.

The main problems with international expansion are related with haste. The first is «sheep herd» behaviour in selecting markets, entering the same as all competitors. This occurred with the textile branch in the Greek market in the last three years – a country very attractive a priori for Spanish retailing but that turned out to be so culturally close to the domestic market that it has exactly the same problems. The second problem is haste in choosing the access mode besides the country, and underestimation of its risk premium.

A well-known case is Ahold and problems arisen from their entry within just 16 months, between 1997 and 1998, to Brazil, Argentina, Chile, Peru, Paraguay and Ecuador (a couple of years before, Ahold pulled out of a project to enter Spain in partnership with Caprabo and later, almost in this century, its big independent project in Spain with Supersol).

Underestimating integration difficulties, the need of raising debt or not paying enough attention to the quality of acquisitions in case this is the pattern chosen to enter a market, causes massive value destruction leading a company to bankruptcy.

Access modes

Distributors with an international view have several ways to enter a market: export (through wholesaling, licensing or concessions), franchising, acquisition of domestic operators, mergers and direct introduction or organic development.

Examples of Spanish companies within each mode are the following: wholesaling (Castañer in Italy), organic development (Tous in the US and UK), franchising (Mango and GAES) or concessions, merger with a local retailer (Sephora and El Corte Inglés) or acquisition, or partnerships (Inditex with Tata in India, with Stockman in Finland to enter the Baltic states and later Russia and with Percassi in Italy, or Nespresso with the Daurella family to enter the Catalan market).

Export, the first step in the internationalisation process of a brand, is beyond the scope of this article. It is about developing a strong international brand and enter markets through what Treadgold (1988) calls «low control» mechanisms like wholesale to local distributors, licensing or opening corners and concessions at other retailers. This is the model of Nike, Nokia and Punto Blanco, with occasional verticalisation of their distribution.

Global franchises are one of the most popular schemes for international expansion. Master/area, joint venture, direct and indirect investment are the four franchise modes. When indicating the reasons for which companies adopt these patterns, Alexander & Quinn (2002) state first that «most work required to expand operations in the foreign market is born by the franchisee, which reduces that of the franchiser».

Another reason they add «is local contribution as it understands the market better than their principal and is in a better position to handle cultural, language and bureaucratic issues».

A third reason often used by Spanish companies is dampening the country risk and having leverage resources and the franchisee's commitment. However, reduced perfection or absence of follow-up and monitoring systems has led to conflict, mistrust and reorienting this pattern among Spanish operators.

There are two access modes: the online and the multiple channel.

The online channel is an excellent mechanism for internationalisation. Examples of global retailers with a growing market share in Spain are Amazon.com and Vente-privee.com. Privalia is an example of a Catalan company with a strong, fast-growing footprint in the rest of Spain. Their managers assert that turnover was at around 60 million euros in 2009, and in March 2010 they announced the opening of their second international portal in Mexico.

A new academic opinion developed during the 1990s (Buchanan, 1992; Nueno & Quelch, 1998) that began to be implemented and stated the superiority of the vertical distribution model pioneered by manufacturers of renowned brands, recovering control over their channels as they withdrew distribution from franchisees, concessionaires and multibrand retailers and opened their own shops, taking the sole responsibility over their expansion and internationalisation. This was a successful strategy and is perhaps the reason why it was imposed, perhaps by imitation, on modes combining direct and indirect channels. However, progressive expansion becoming less close and more complex and more recently global recession in consumption, increasing real estate and communication costs and the size of the big global markets have sometimes meant that the feasibility of international expansion turned out to be impossible without a strategy encompassing indirect wholesale trade (through department stores and specialist shops) and with direct sale through controlled (virtual or physical) channels. This is the multiple channel thesis and the most frequently adopted pattern by Spanish companies, combining wholesale trade at department stores or independent retailers with opening standard shops and franchises run by operators. Mango has areas under concession in Falabella shops in Chile and shops in malls and own shops in the United States. Tous uses the same scheme in Chile and the US (Macy's) with areas under concession in department stores and own shops or in partnership with local partners. Adolfo Domínguez has corners in Palacio del Hierro in Mexico City, and Castañer sells through Colette, multibrand shops, Galeries Lafayette and three own shops, all of which in Paris.

Adding an online channel to an existing distribution system is a double-edge sword as it destroys value in 30% of cases.

One of the first strategies to add to a consolidated distribution system is the online channel (under brand control), which can become a double-edge sword. A study by Geyskens, Gielens & Dekimpe (2002) shows that adding an online channel to an existing distribution channel destroys value in 30% of cases (the distributor's share value drops).

Some recent PhD thesis tackles this challenge, although related to adding sales points with brand products from past seasons or with defaults (outlets) to the existing consolidated system. Results are not conclusive, basically due to the current market situation. Tous, for instance, has an online shop serving exclusively the US market and relaunched in 2010 to supply more markets. Other national operators come back on outlets as a core scheme (such as Ralph Lauren in Spain) ore just another channel (Desigual, Mango), while some use more aggressive methods (Lefties from the Inditex group has an urban outlet with a chain and brand of its own and just moved its headquarters from León to Tordera in Catalonia).

Conclusions

Catalan companies have been late in their international expansion and often turned out to be overdependent on the domestic market. In the absence of any causes to push them abroad, their focus on a munificent and empathic market and maturity of close markets has reduced their motivation to open to the world.

During the last two decades, both manufacturers and distributors in industrialised countries were more successful in exporting through internationalisation of their shops than through the products sold. Spain, and particularly Catalonia have produced many success stories that share the following factors, among others:

– They are centralised and do not fully dominate local procurement, which keeps them out of certain areas (e.g. HTCP) and restricts expansion to rigid concepts and patterns hardly adaptable to local specificities.

– They hardly adapt to consumer tastes in the host country.

– They followed a pattern based on opening few shops in many countries (sprinkler) rather than penetrating less markets («oil drop» expansion).

Current opportunities for them are complex by scale and affinity:

– Polarised, emerging and small markets, like the twelve latest accession countries, the total size of which (e.g. textile) hardly doubles that of the Spanish market, which amounted to 17 billion euros in 2009, or too large (BRIC), fragmented or culturally far attractive markets for the future.

– Liabilities largely surpass short-term return and require carefulness in the absence of local partners or capital suppliers.

The most common recommendation by academic literature, adapting practices and processes according to the cultural character of the host country (Dawson, 1994), has been by and large ignored by Spanish domestic champions, concentrated and based on as well as being a hostage of very differentiated product concepts. Inditex features an extremely centralised model and Tous, GAES, Pronovias, Rosa Clarà and Punt Roma have neither local subsidiaries nor often specific country managers (GAES being an exception there). Some of their managers assert that this adaptability and empathy requirement can be catered for from the headquarters. When taking decisions between centralising and relinquishing sales beyond the target segment on the one hand and the risk of diluting a multilocal success model on the other, adapting it to each of the dozens of markets they operate in, they prefer the former.

Relatively late access of Spanish distributors means that the geographically or culturally closest markets feature either places with deep rooting or other multinational or global retailers having entered them many years ago. This exposes latecomers to the complexity of emerging markets. Retailers wishing to enter there need to do the double task of developing a consumption pattern while seizing market quota, which means bigger obligations in terms of time and investment. They are thus required to adjust the ambition to the size of upcoming challenges. To Starbucks, developing a market in Spain ensuring turnover and business at all times of operation is a requirement forcing to seize a share able to live up to strong investment done so far. For a medium-sized distributor, markets demanding big efforts in passing the message can be difficult to tackle. This warning is particularly relevant for manufacturing companies in a verticalisation process that tend to think that industrial rules (scale vs. adaptability) are still valid in their expansion as distributors.

Potential expansion markets are becoming ever less attractive, farther, more complex and risky.

«When sales are doing badly here, they do well somewhere else», but the effects of good performance in the latter markets are visible in those having entered them by attraction rather than by force. Talent and commitment of managers able to tackle this challenge is neither improvised nor bought, even less with increasing demand, and potential expansion markets are becoming ever less attractive, farther, more complex and risky. Internationalisation of distributors is a double-edge sword: there is nothing making a model more credible to public opinion, particularly financial institutions. Likewise, there is nothing like failing in this challenge to turn this credibility into mistrust and put the model in jeopardy.

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