Customer Loyalty & Private Label Products

KPMG Global Consumer Markets

Foreword

Retailers are facing increasing pressure from all fronts. The competition is getting tougher, customers are more discerning and demanding, and the traditional barriers between products and services are disappearing. On top of this, the phenomenal growth of e-commerce is increasing customers' expectations for more competitive prices and 24-hour service. To keep ahead, retailers need an increasing range and depth of expertise in customer management. KPMG's Global Consumer Markets group, in partnership with the Oxford Institute of Retail Management (OXIRM) has undertaken research across Europe into retail trends and the impact of customer loyalty.

There have been many recent developments in loyalty schemes, with varying degrees of success. The loyalty of customers, who can switch freely between retailers, has been influenced by several factors including:

- advances in technology – magnetic/chip cards, card scanners, falling data processing costs – enabling millions of daily purchases to be analysed, tracked and rewarded;
- decline in store numbers and the accompanying increase in store size;
- moves out of town by stores, leading to a decline in shopping frequency;
- increase in store size via out of town developments permitting an increase in the range of categories stocked;
- increased usage of private label, as both a store loyalty builder and a ready alternative to branded products, reducing the customer's resistance to switch brands;
- inclusion of pharmacies, post offices, dry cleaners and petrol stations creating the facility for "one stop" shopping and providing traffic store generators.

This report confirms that customer loyalty is complex and covers many retail strategies and operations. We believe that the findings, published here, will provide valuable insight to retailers, who are looking to introduce, or already have, private label products.

KPMG is one of the world's leading professional service organisations, with over 103,000 staff in 159 countries. We have a deep industry orientation, focused on anticipating and meeting our clients' needs. KPMG brings lasting and measurable benefits to our clients through the delivery of integrated solutions that combine business strategy, industry-focused people, the latest processes and technology.

OXIRM links sound academic scholarship to the practical needs of retail and related service companies. OXIRM is a leading centre for retail management education, with an active programme of high quality applied research, based at Templeton College, the graduate College of business at the University of Oxford.

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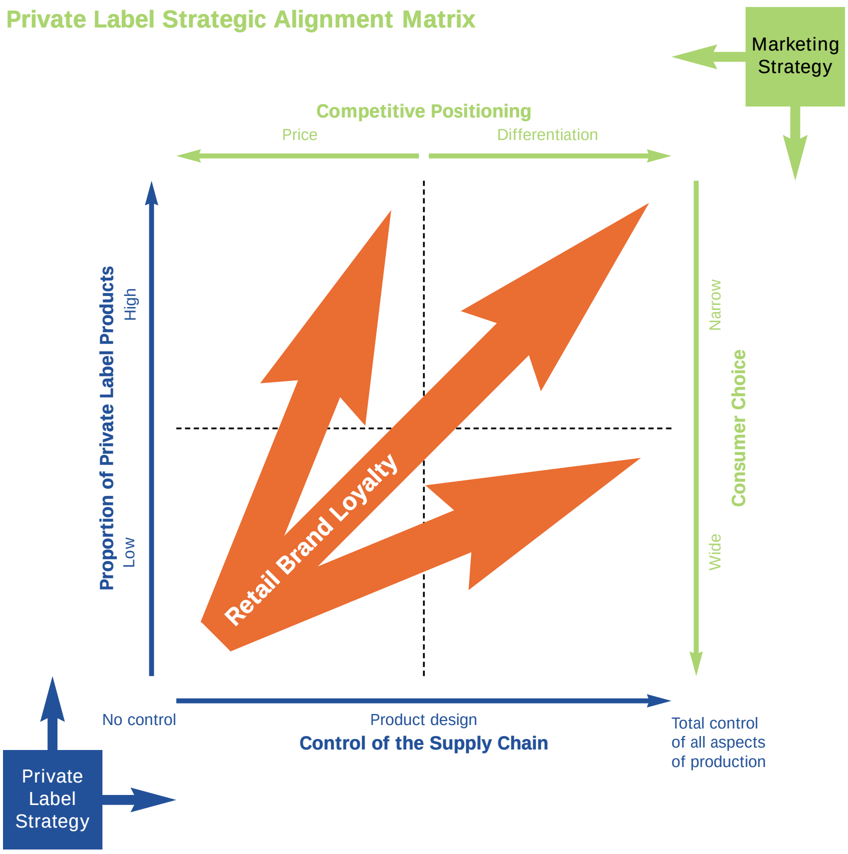
1 Executive summary

Customer loyalty cannot be built in a day. Increasingly it is built through longer term customer relationships with a valued brand. Private label products[1], we find, play an important role in developing a retail brand. As part of KPMG's series of research reports on customer loyalty, this report focuses on the role of private label.

Successful private label development is the result of harmonised strategies and effective implementation, which are specific to each individual retailer and product category. We believe there are several routes to success.

High performing retailers align their private label strategy with their overall marketing strategy. By identifying the strategic focus – and then delivering relevant product and service benefits to the customer – true loyalty to the retail brand can be established.

Private Label Strategic Alignment Matrix



[1] Private label is any product with a retailer-owned name on it.

The *Private Label Strategic Alignment Matrix* is an effective tool to help retailers measure and evaluate the consistency of their private label and marketing strategies. How it is developed and used to build brand loyalty is explained in greater depth in the main section of this report.

To implement a successful private label strategy, we believe retailers need to:

- ensure any private label strategy is aligned with overall marketing strategy by seeking a focused positioning in the *Private Label Strategic Alignment Matrix*;
- ensure high standards of quality control (pre-transaction) and customer service (post-transaction) are maintained. Trust is fundamental for shoppers to accept private label products and services. Accepting private label also establishes additional trust in the retailer's ability to meet consumer needs reliably; and
- ensure relevant products and services are developed under private label. Certain products are less suited to private label development. It is easier for the retailer to encourage the consumer to try frequently purchased, low value private label products relevant to the retailer's core range, rather than infrequently purchased, high value products outside the retailer's core range.

Electronic retailing has special relevance for private label. There is more opportunity to switch between e-tailers on the Internet than between conventional 'bricks and mortar' retailers. Established private label can allow web-based retailers to offer unique products, so helping to trade on factors other than price, deter shopper promiscuity and secure lasting and profitable customer loyalty.

This report includes case studies based on research and collaborative reviews of seven major European retailers with substantial private label products: Aldi, Asda (George clothing), Boots the Chemist, Decathlon, Marks & Spencer, Migros and Tesco.

2 Private Label, retail branding and loyalty

A brand differentiates products and services, and strong brands stand out from the competition. They are less prone to substitution and generate high levels of loyalty.

Private label products contribute to retail brand differentiation, and their positioning reflects the value of the brand. They are not perceived as being interchangeable with similar private label products in other retailers (unlike manufacturer branded products, which are the same regardless of the retailer). 100% manufacturer branded products means that retail differentiation can only be achieved by service related factors, such as location and atmosphere.

A retailer can achieve differentiation through a large (but not necessarily exclusive) portfolio of private label products. As consumers usually visit with the intention of buying, and not simply for the experience, this is important. Service adds to the differentiation, and together with a unique product range, results in a strong retail brand. The extent to which this differentiation is seen as relevant by consumers can be measured in terms of: economics (price premiums and market share), attitude (consumer perceptions) and behaviour (consumer loyalty).

Customer loyalty is therefore the result of an affinity with a valued brand. As retail brands can be tangibly enhanced by the development of private label products[1], many retailers use private label as an important tool.

This report provides a strategic framework with which to analyse a retailer's private label development and identifies the critical issues in implementation. The methodology for this report is briefly discussed in Section 7.

An Overview of Private Label

There are many definitions for the term private label, including own brand, store brand, retailer brand, own label, among others. The term used in this study is private label, and is defined broadly as:

"any product with a retailer-owned name on it"
(Davies[2], 1990)

A private label product can be anything from a basic commodity product, such as tinned tomatoes, to an innovative retailer brand with relatively high quality and price. The term is used as a general name for all retailer-owned product names, regardless of their level of sophistication. Private label is initiated by the retailer and the onus for the development, manufacturing, marketing and distribution of private label products is on him, though often in close co-operation with suppliers. As this may require considerable resources, smaller

[2] Davies, Gary (1990): The two ways in which retailers can be brands. Working paper. C2, Oxford Institute of Retail Management.

or independent retailers may join together to source products. Products supplied in this way tend to be commodity products, such as fresh fruit, or simple, low-cost products.

Private label products can be classified as follows:

Store brands carry the retailer's name, but no additional sub-brand. For example, Tesco's standard store brands.

Store sub-brands carry both the retailer's name and a sub-brand. For example, Tesco's Finest range.

Generic brands have a name independent from the store name. For example, Euroshopper's range of products. These are not named store brands; they can be used across differently named stores and chains.

Individual product brands are owned by the retailer and are treated by the company like individual brands. For example, Aldi uses individual product brands. The retailer's name may be visible in the background but is not emphasised.

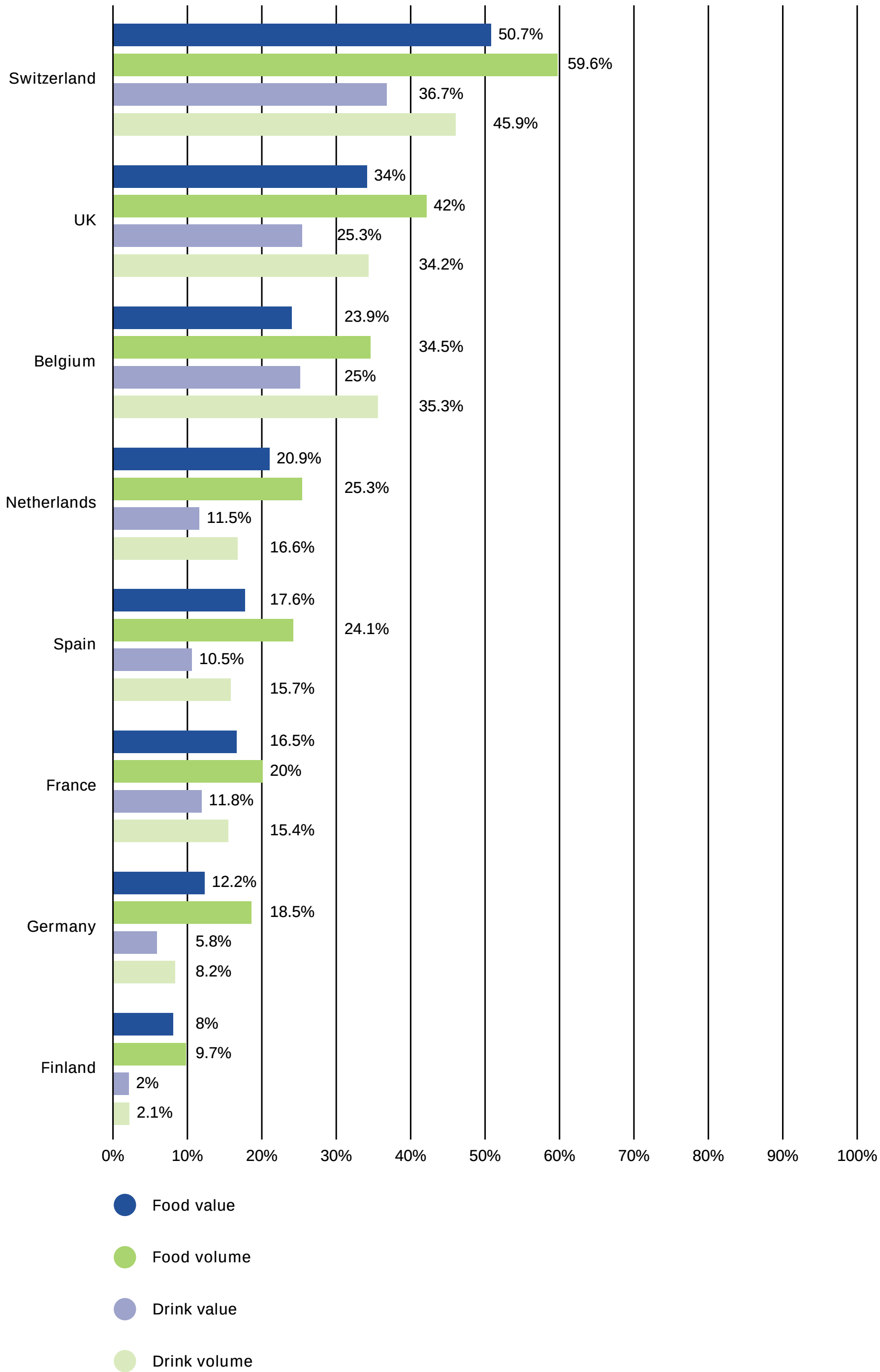
Exclusive products are not, by definition, private label products, but possess some similar characteristics. For example, Migros in Switzerland has a number of exclusive agreements with suppliers (for example, with Del Monte).

Many retailers employ more than one type of private label. A grocery retailer may have store brands for the majority of private label lines, and store sub-brands for the more upmarket ranges and aspirational products or for the more low-price commodity ranges like Asda's Farm Stores or Migros' M-Budget.

Private label penetration[3] varies significantly across European grocery markets, as shown opposite.

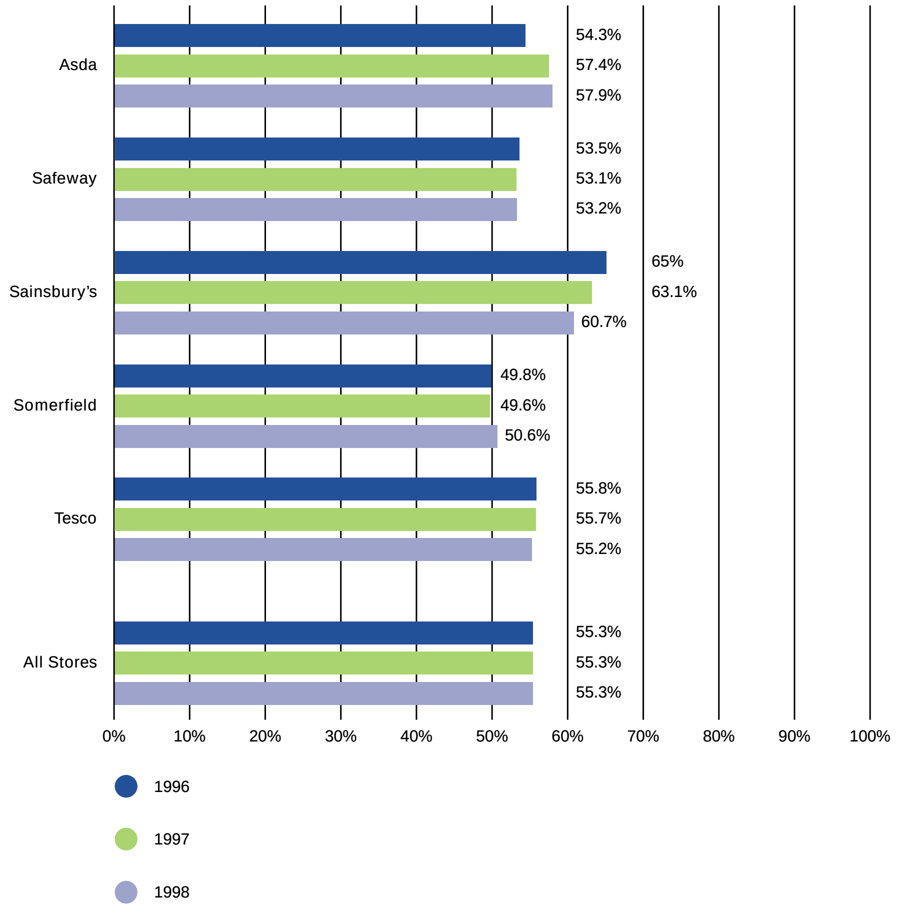
[3] The data describing private label penetration across different countries is often inconsistent (see Appendix A for details).

Private Label Share of Sales by Country, in 13 Food and 7 Drink Categories[4]



[4] Source: ACNielsen (1998): International Private Label Retailing – Indicators and Trends. Note: The figures are simple averages. The German figure excludes Aldi, which almost exclusively stocks private label product. With Aldi included, the German penetration can be estimated to rise more than 10 percentage points.

The Major UK Food Retailers' Private Label Share of Sales[5]



The most penetrated markets in food retailing are the UK and Switzerland, in others such as Italy and Norway the penetration is still very low. In many cases, the actions of one or two retailers within a country have a significant impact on country averages. For example, in Switzerland and Germany, Migros and Aldi respectively have very high private label penetration and a significant market share, which greatly impacts national private label market share.

There are markets where nearly all the key players have developed their private label similarly, such as UK food retailing, as shown above.

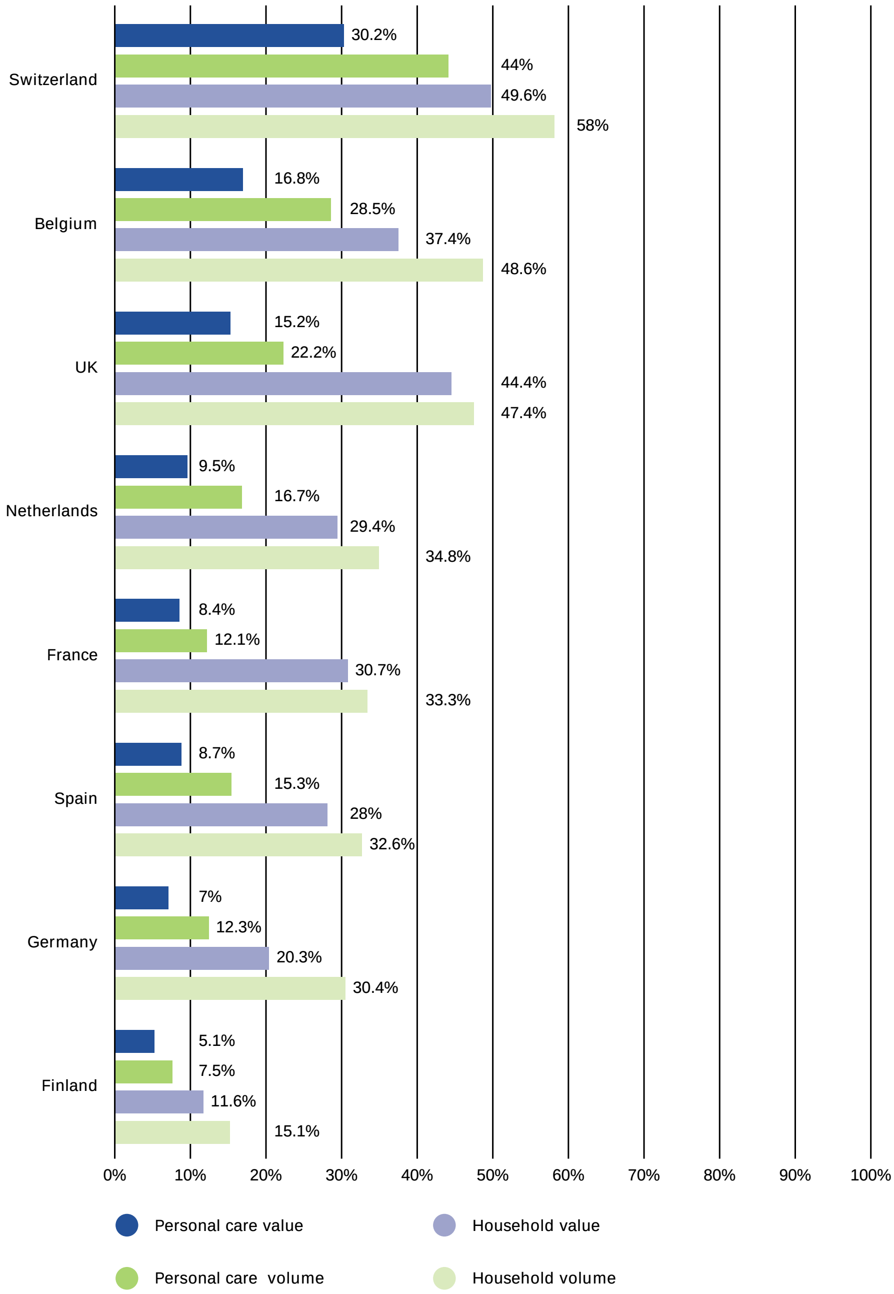
In the UK grocery sector, one of the major reasons for a high level of private label penetration is the fresh and chilled product categories, as it is difficult for branded manufacturers to handle these very short shelf life products. For example, private label penetration in the chilled ready meals category is around 95% in the UK (*Mintel: Own Label Food, November, 1998*).

Private label exists in most product categories in non-food retailing, such as clothing, electrical products and DIY. Relevant statistics for general private label penetration are unavailable, because of the fragmented nature of non-food retailing. The exception is the large grocery retailers that operate both in food and non-food retailing. The main non-food areas are toiletries and household products (see opposite).

In the grocery non-food sector, the private label offer may appear similar, but at a cheaper price. For example, Sainsbury's Wash and Shine or Tesco's Two in One compared to Proctor & Gamble's Wash and Go shampoo. Retailers are also entering new non-grocery related categories, such as CD-players and books.

[5] Source: ACNielsen, State of the Nation 1998. Note that accounting for Somerfield's acquisition of Kwik Save would reduce their 1998 figure to around 39%. Kwik Save's figures for 1996-98 are 20%, 21% and 26% respectively.

Private Label Shares by Country, Personal Care and Household[6]



In the non-grocery sector, many retailers are specialised and serve a narrower niche in the market. Sometimes the niche can be very narrow, such as Tie Rack. Most DIY, cosmetics, sports goods retailers and department stores sell a mixture of both private label and manufacturer brands.

Where private label does exist in non-grocery retailers, 100% private label is more common and the border between the manufacturer and the retailer is not as well defined. Some manufacturers have vertically integrated down the supply chain and opened retail units in order to distribute their private label products, such as Benetton. Some retailers have increased their control up the supply chain, for example Marks & Spencer.

[6] Source: ACNielsen (1998): International Private Label Retailing – Indicators and Trends.

3 What are the commercial implications of Private Label?

Retailers have different commercial objectives for their private label products and use different types of ranges for different purposes. In an Institute of Grocery Distribution survey[7], UK food retailers were asked what the role of own brands in a particular category should be. The most important roles were:

1 improve profitability;

2 build and maintain consumer loyalty;

3 reinforce market position;

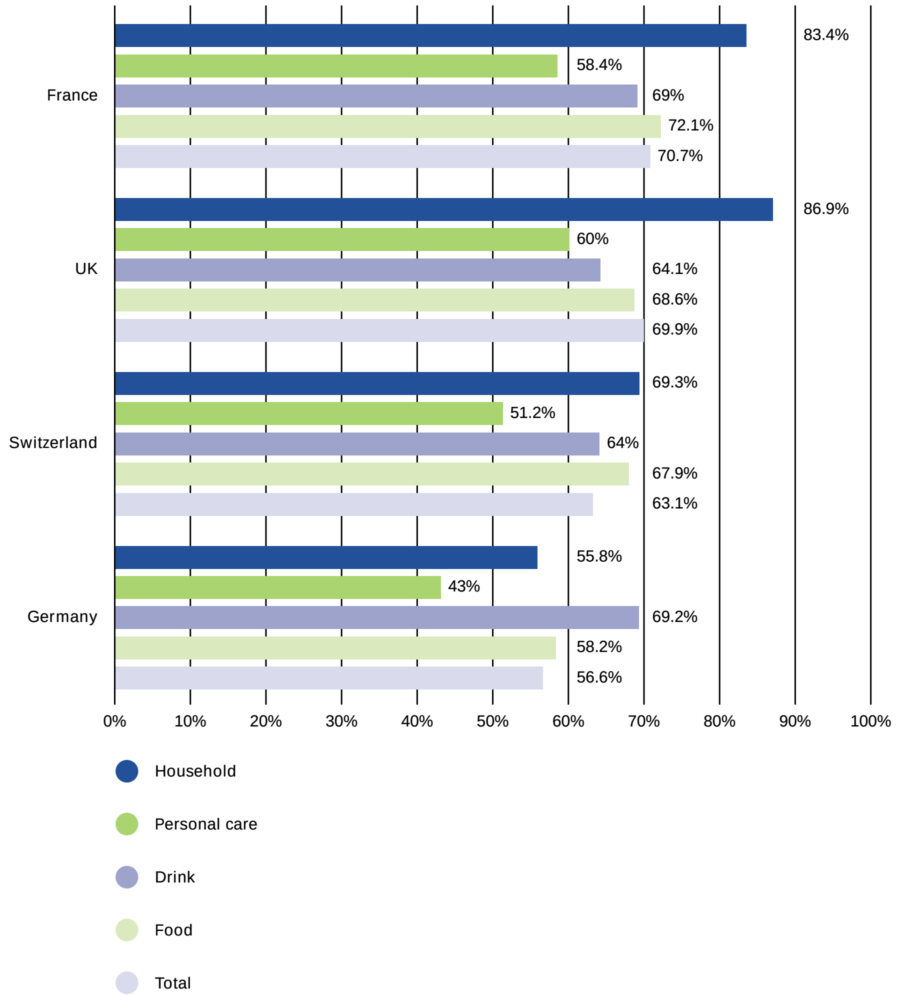
4 increase consumer choice;

5 match products more precisely to retailers' customers.

Others included: the enhancement of store image, better control of supply chain and product quality and differentiation from competitors. Private label can also play an important role in building the wider retailer brand.

[7] Institute of Grocery Distribution / Mary McGrath (1995): The Changing Face of Retailer Brands. IGD Business Publications, Watford.

Price Index, Private Label vs Manufacturer Brands (=100)[8]



Improve Profitability

According to ACNielsen, private label prices are generally at least 20% to 40% cheaper than manufacturers' brand prices, as shown above.

Private label products are not necessarily of comparable quality with the manufacturer branded products. Lower quality "budget" product lines and higher quality private label products may be included.

Consumer buying prices are still generally lower for private label products even when "budget" product lines are excluded, as shown in the next table, where private label products are, on average, 14% cheaper than the manufacturer branded product lines.

[8] ACNielsen (1998): International Private Label Retailing – Indicators and Trends. NTC Publications LTD, Henley-on-Thames.

Prices of Manufacturer Brands compared to Private Label (PL) Tesco and Sainsbury's in the UK[9]

Product *Brand*	**Brand price (£)** *Tesco* *Sainsbury's*	**PL price (£)** *Tesco* *Sainsbury's*	**Price Index (£)** *Tesco* *Sainsbury's*
Baked beans (420g) Heinz	0.31 0.25	0.23 0.23	74% 92%
Washing powder (E3) Persil	2.39 2.39	1.99 1.75	83% 73%
Dog food (400g) Pedigree chum	0.45 0.45	0.41 0.42	91% 93%
Cornflakes (500g) Kellogg's	0.99 0.99	0.79 0.89	80% 90%
Instant coffee (200g) Nescafe Original	3.25 3.25	2.65 2.79	82% 86%
Soft drink (2l) Coca-Cola	1.29 1.29	0.69 0.95	53% 74%
Tea bags (160) Tetley	2.99 2.99	1.69 2.19	57% 73%
Diapers Pampers	5.65 5.65	4.99 4.99	88% 88%
Canned tomato soup (300g) Heinz	0.37 0.41	0.37 *(290g)* 0.37 *(295g)*	103% 92%
Tomato ketchup (1.14kg) Heinz	1.46 1.46	1.43 1.29 *(1kg)*	98% 101%
Cat food (400g) Whiskas	0.47 0.47	0.43 0.43	91% 91%
Toilet tissue (x2) Andrex	1.07 1.79 *(x4)*	0.95 1.69 *(x4)*	89% 94%
Sanitary towels (x14) Always	1.59 1.59	1.25 1.69	79% 106%
Fish fingers (x10, 300g) Birds Eye	1.49 1.49	2.15 *(x20, 600g)* 1.25	72% 84%
Frozen peas (2lb) Birds Eye	1.29 1.29	1.29 1.19	100% 92%
Squash (1l) Robinson's	0.79 0.79	0.65 0.75	82% 95%
Mean average			
Adjusted	1.64	1.33	86%

[9] Tesco and Sainsbury's stores in Oxfordshire (23.11.1999). The products in the table are well-known brands, all appear in ACNielsen's list of Top 100 UK Grocery Brands and are known value items as stated in Checkout, December 1998: The Top 100 Grocery Brands. Price index figures have been adjusted (where relevant) to take account of differences in weight.

Prices compared in this table are of products that may *appear* to be similar, though in reality they may differ, not only between the manufacturer branded product and the retailer branded product, but also between the different retailers' products.

Prices of both manufacturer brands and private label are similar in the two stores. An example of the excluded "budget" product lines (which may have been included in the ACNielsen survey) is a can of baked beans, which could have been purchased for £0.10 (10p) from the Sainsbury's Economy or Tesco Value ranges. It is also worth noting that these prices may vary considerably over time. A similar OXIRM survey in January 1999 showed a 22% difference in price between private label and manufacturer branded goods.

Despite the fact that private label products are usually priced lower than manufacturer brands, they generally carry larger profit margins, though gross profits may be similar. Key Note estimates that in grocery, margins are generally 5% higher[10]. Corporate Intelligence on Retailing (now Retail Intelligence) explain that "although in percentage terms own-label is more profitable than branded goods, in cash terms the gross profit is the same on average"[11]. Laaksonen states that "the margins of own brands can be 5-20 % better than the margins derived from the leading brands"[12]. Profit margins may therefore vary significantly across different retailers and product categories.

Private label products may be cheaper to produce for a number of reasons, including:

- where private label uses the manufacturer brands as the benchmark it might be seen as capitalising upon some of the original product development and marketing;
- manufacturers may produce private label at prices that reflect only the direct manufacturing costs – in order to fill excess production capacity;
- if the manufacturer's sales force and distribution channels are not used, the retailer's buying price can be reduced;
- if the retailer has enough (marginal) buying power, it might be able to negotiate a reduction in the manufacturer's profit margin.

The following example illustrates how a retailer's buying price for private label product might be up to 25% lower than the perceived comparable manufacturer branded product.

An Example of the Costs Avoided with Private Label[13]

	Manufacturer Brands	Private Label
Raw materials	35	35
Packaging material	12	12
Manufacturing costs		
- variable	9	9
- fixed	5	-
Research & development	3	-
Sales force	4	-
Advertising & promotion	9	5
Transport & distribution	5	2
Other costs	10	10
Operating profit	8	2
Retail Buying Price	**100**	**75**

[10] Key Note Market Report (1997): Own brands. Key Note, Middlesex. Seventh Edition.

[11] Corporate Intelligence on Retailing (1998): Own-label in the UK - The Grocery Trade Poised for Change. Corporate Intelligence on Retailing, London.

[12] Laaksonen, Harri (1994): Own Brands in Food Retailing Across Europe. Oxford Institute of Retail Management.

[13] Source: OXIRM on the basis of manufacturer annual reports and company accounts.

This example shows how costs can be reduced for private label, although the cost structure will vary between different manufacturers and products.

Private label products may also help retailers increase margins indirectly, by reducing the reliance on a particular manufacturer, enabling tougher negotiations on price.

Providing a low price private label product may reduce pricing pressures on manufacturer branded products, and by stocking differentiated products, in terms of size and specification, direct price competition can be avoided. This means more risk for the retailer, especially in terms of product development. By stocking only private label product, this risk becomes fundamental to business success, as poor product development may seriously impact consumer loyalty.

Consumers will then turn to the competition's products, rather than other products within the same retailers.

Profitability results from a combination of factors – the actions of retailers, consumers and manufacturers (as well as accounting principles). This makes direct comparisons between retailers, product categories and/or countries difficult. However, what is clear is that private label may be a means to improve profitability, both directly and indirectly.

Build and Maintain Consumer Loyalty

The ability of private label to build and maintain consumer loyalty has been discussed extensively (for example, see Corstjens[14]). To obtain loyalty, it is necessary to have a unique offer. A distinctive private label range that matches the needs of the retailer's customers can provide this.

In the UK, ACNielsen studied[15] shopping habits in different grocery stores. The importance of "good quality own label" varies from 3% in Somerfield to 7% in Sainsbury's; the average being 5%. Private label also influences other attitudes, such as "good range of products", "low prices" and "value for money". Private label appears most important to "new families", young couples with small children.

An ACNielsen Homescan survey in the UK, highlights the reluctance of private label buyers to change store:

[14] Corstjens, Judith and Corstjens, Marcel (1995): Store Wars. The Battle for Mindspace and Shelfspace. John Wiley & Sons Ltd, Chichester.

[15] ACNielsen: State of the Nation 1997.

Attitudes of the Own Label Buyer[16]

Percentage agreeing with statement	Branded Buyers (<20% private label spend)	Own Label Buyers (>80% private label spend)
"The economy will get much better in the next 12 months"	11.0%	24.0%
"I like to shop at different stores to get the best prices"	42.7%	28.8%
"I know which store offers the lowest price on my usual brands"	46.3%	20.2%
"When my favourite product is on promotion I stock up on it"	36.6%	56.7%
"I shop around a lot of different stores for special offers"	20.7%	11.5%
"I find out about new products from TV adverts"	53.7%	32.7%
"I have bought a new product after seeing it on TV"	41.5%	23.7%

The table suggests that private label buyers are more store loyal and not as easily influenced as brand buyers. They are not as price-oriented as has been thought, as they don't tend to switch stores to obtain the lowest prices.

Reinforce the Retail Brand

A brand is unique, consistent in quality and offers something of value to the consumer. The advantages of a retailer brand has been described as twofold[17]:

1. Differentiation, helping the retailer to move away from price competition.
2. Consumer loyalty, by establishing a reputation for reliable quality (see previous section).

A retailer can achieve brand differentiation either from the uniqueness of the products through retailer-made or controlled product specifications, or from the uniqueness of the total offer. For example, Aldi differentiate on the grounds of cost leadership so the price of Aldi's exclusive products is more important than any other innovative, distinctive element.

The brand franchise may be extended to other products or services. The relationship between private label and the retailer brand is mutually supportive: as private label helps to build the retail brand and the brand supports private label sales.

In fact, private label can play a crucial part in building the retail brand.

Increase Consumer Choice

Consumer choice is increased through private label. Some categories, such as chilled ready meals, are so dominated by private label – because of the very short shelf life – that private label is a must if the retailer wants to offer a competitive range.

Many retailers offer a range of price and quality alternatives within a category by creating differently positioned private label products. For example, Tesco has its budget Value range, Healthy Eating, normal Tesco-brand and "restaurant-quality" Finest-range to cover many different price-quality options.

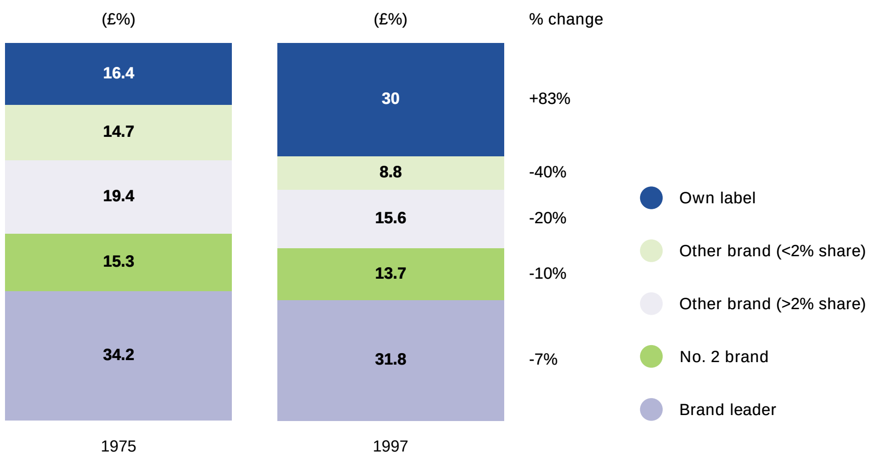
[16] Source: J. Sargent (1997): Own label: taking stock in 1997. Original source: ACNielsen Homescan Survey.

[17] Gary Davies (1990): The two ways in which retailers can be brands. Working paper, C2, Oxford Institute of Retail Management.

Private label products also increase choice by providing alternatives to manufacturer brands. Retailers can use the increasing amount of information they have on customers and their shopping habits, through scanning and loyalty cards, to develop new, customer-driven products. This customer knowledge can give retailers a competitive edge (see next section).

However, if the private label product is very similar to an existing one, it can be argued that private label may decrease consumer choice. And as private label products generally take market share from secondary and tertiary brands, rather than from brand leaders, as the following diagram illustrates, the result can be to drive smaller manufacturer brands out of the market. This also decreases customer choice.

The 'Average' Market Structure (1997 vs 1975) in the UK[18]



Match Products to Customers' Needs

During the past few years, the vast amounts of data retailers have been able to gather on customers has increased significantly, due to sophisticated scanning and loyalty schemes. Electronic commerce also enables retailers to store information on customers' buying habits and preferences, allowing companies to develop products to match customers needs and offering cross-selling opportunities.

Armed with relevant information, retailers can use private label to tailor products and services to their consumers. For example, Boots recognises that customers buying at airports prefer smaller sizes and different ranges of products to those buying in out of town stores. They also know that people who buy rolls of film also tend to buy picture frames and related goods, so they can arrange displays accordingly, or offer special linked purchase deals.

[18] Source: Taylor Nelson Sofres

4 What is the right Private Label strategy?

Case studies covering seven major European retailers have been analysed to construct a strategic framework for private label development (see Section 7 for case study details).

As private label is a key component of the retailers' overall strategy, it is sometimes hard to separate private label success and the general success of the retailer. What is clear is that there are many types of successful private label strategies.

Competitive Positioning

A strong company culture is a common feature among all the retailers studied. Founders or senior executives have set out the company's business principles, and the retailers have aligned their strategy to these. The trading strategies and routes to differentiation are varied, but clearly distinctive. Within most of the case study retailers (with the exception of Tesco), the basic strategy has remained nearly unchanged from the very early years. Tesco, as an exception, provides an example of how a retailer can evolve from being a seller of manufacturer brands only, to a leading developer of private label products.

For all of the retailers studied, private label has been, and is, an important means of putting the distinct corporate strategy into action. It is not just a way to increase margins (important though this is) and it is possible to carry out too much private label development. For example, it can be argued that Sainsbury's have actually reduced their private label development in recent years. Private label is thus utilised to achieve competitive advantage – to build the retailer brand. For example, in Migros, private label has been employed to reflect company values of health, high quality and ethics.

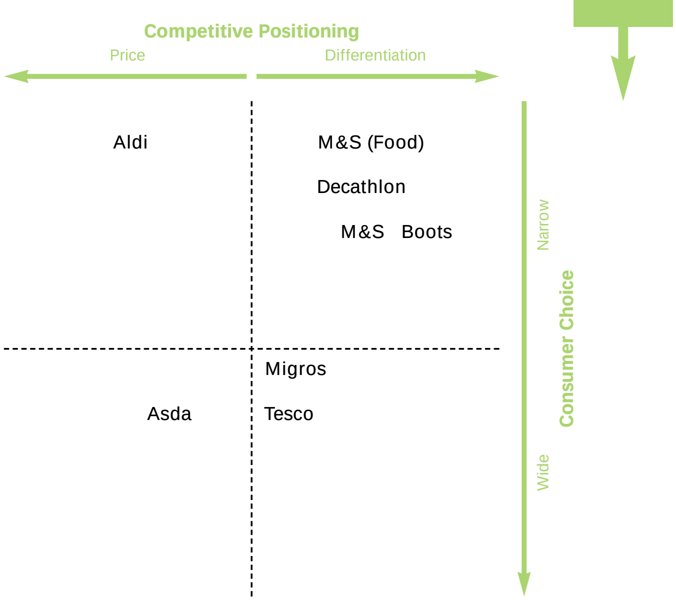
Private label is therefore an essential element of the overall retail marketing strategy, which could be simply defined as cost or differentiation. This price/differentiation forms the framework developed here for evaluating private label strategy.

What is the right Private Label strategy? (continued)

Private Label Strategic Alignment:
Stage One – Competitive Positioning

This model will be developed further throughout this section.

Private Label Strategic Alignment:
Stage Two – Consumer Choice



Consumer Choice

In the generalist market, consumers still prefer manufacturer brands in many product categories. According to Mintel[19], in a consumer attitudes survey undertaken by BMRB, 41% of the sample of 964 housewives in the UK (where leading food retailers claim around 50% of sales on private label) agreed with the statement: “For some products, only branded foods will do”. By not stocking all manufacturer brands, retailers risk damaging their image as a competitive retailer. Manufacturer brands provide authority as well as choice to consumers. In the case of Decathlon, fashionable brand names, such as Nike, are important to the retailer’s overall image.

In Asda, the George range is marketed strongly, but the brand name is not visible on garments when worn. The range aims to be a generic family clothing brand, and Asda deliberately chooses not to target the most label-conscious teenagers , so restricting consumer choice.

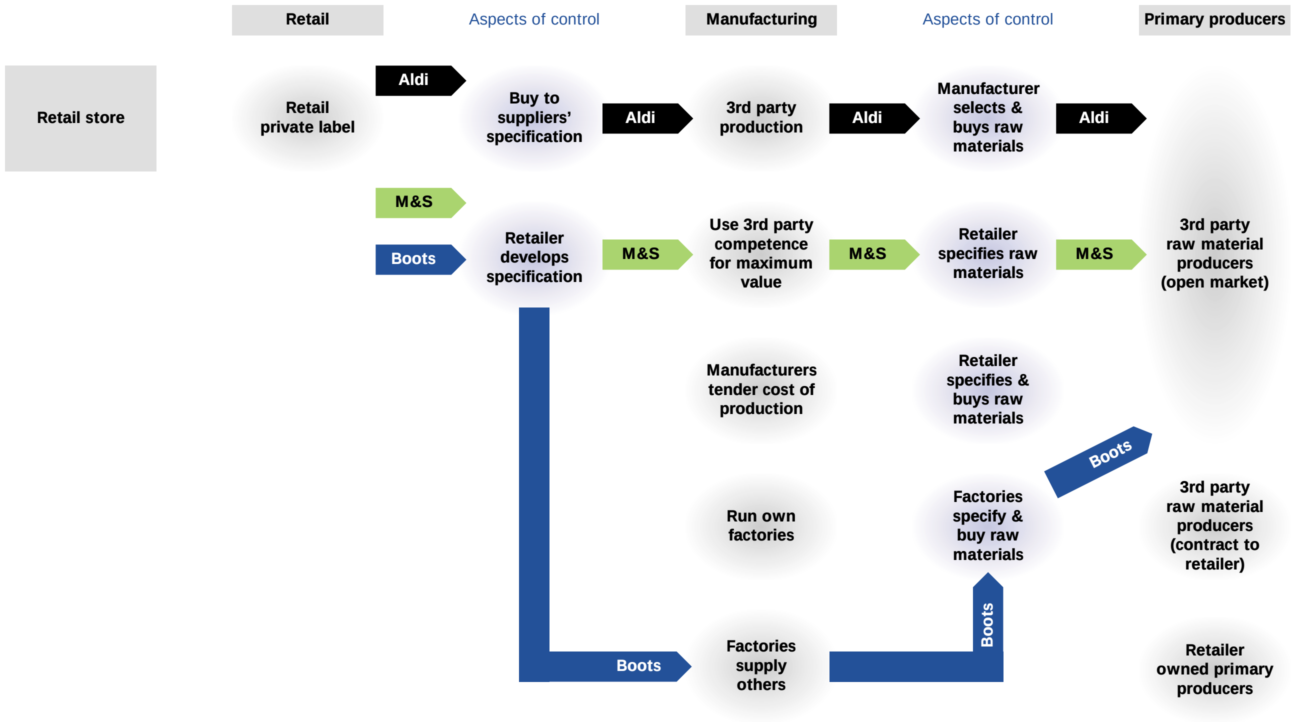
Retailers must therefore select products for private label development which suit their target consumers. This then forms the second axis of the model.

[19] Mintel Marketing Intelligence: Own Label Food, November 1998. Mintel International Group Limited, London

Control of the Supply Chain

The three major stages in the retail supply chain are retailing, manufacturing and primary production. When a retailer introduces private label, there are several different options for managing each of these stages, as illustrated below.

Private Label Supply Chain Options and Examples of Retailers' Choices

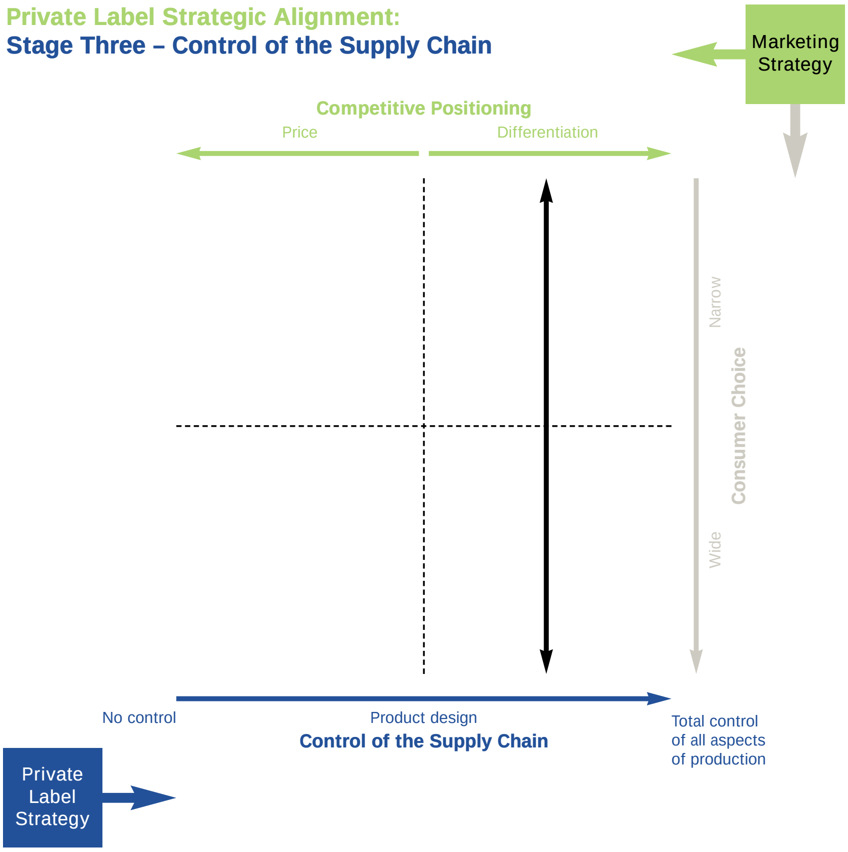


A key decision in private label supply is whether the retailer or the supplier develops the product specification. Retailers may take advantage of manufacturers' product development and may only want to buy a finished product at the lowest possible price. This is often the case with basic, low-price private label products. This requires very little resource from the retailer, though it may not give any real point of differentiation other than price. But, by developing the product specification, a retailer may achieve differentiation and therefore (non-price based) competitive advantage. This demands much greater expertise, resources and risk from the retailer. Retailer-designed product specifications may also provide competitive advantage through the freedom to select suppliers and more directly control cost and quality.

Retailers vary their approach with different products, depending primarily on their overall marketing strategy for that category. Most retailers take more than one approach and the examples shown are not exclusive.

In the case of many commodity products (such as some grocery products), the brand leader often defines product standards. Retailers cannot match brand leaders in terms of innovation, research and development, and promotional support. Retailers therefore take a cost-driven approach, reliant on the supplier's product design.

Private Label Strategic Alignment:
Stage Three – Control of the Supply Chain



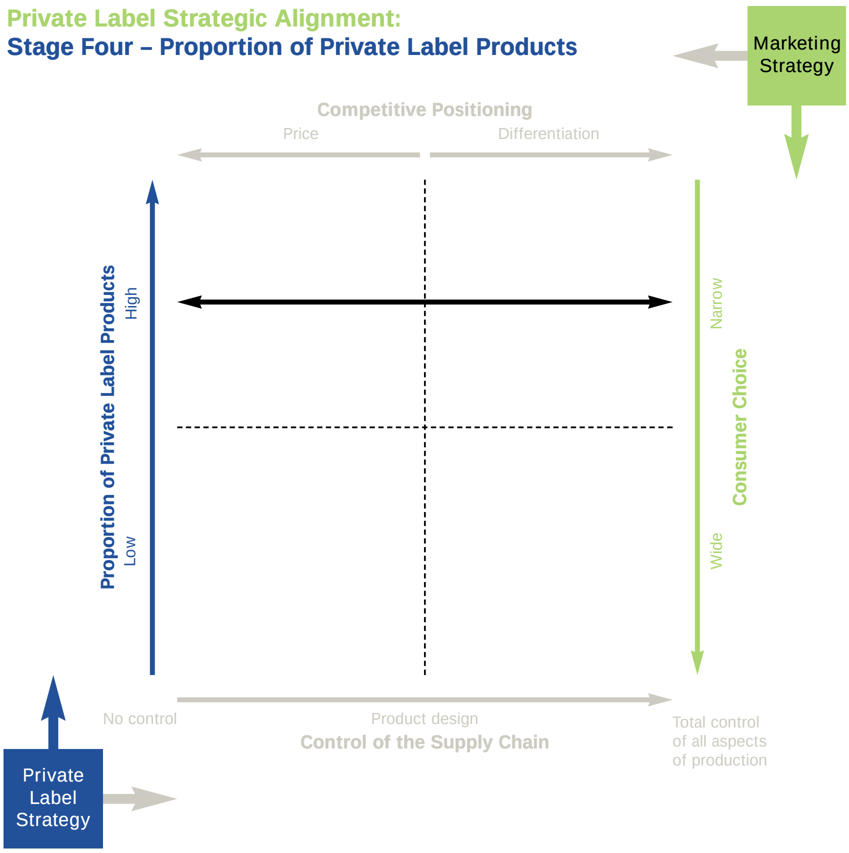
If a retailer's image relies on the particular characteristics of a product, then it must be unique. This can be achieved by retailer-made product specifications. Control of the supply chain may be varied, either via production control (e.g. Boots, Migros), by strict supplier selection, partnership and control, (e.g. Marks & Spencer, Decathlon), or by contracting product design to a competent third party with secured exclusivity (e.g. Asda with George).

The sourcing of private label is sometimes regarded as a process of shopping around for spare capacity and lowest prices in the short term. This is the case for some retailers and buying groups, especially with budget ranges, such as the AMS Euroshopper range. However, in their relations with suppliers, the retailers we studied prefer long-term partnerships and close co-operation with information sharing "for both partners' benefit".

In practise, this often means geographical proximity, which contributes to easier supplier control with shorter response times. When expanding overseas, retailers are generally keen to seek local suppliers in the new markets. The high interest in product quality, as well as private label's contribution to building the retailer brand, increases the preference for long-term supplier relationships .

Control of the supply chain is therefore an essential element in successful private label development. The level of control is variable, and should be relevant to competitive positioning. But it stands to reason that if a retailer wants to create a unique product and unique service to gain differentiation in the market, the level of control of product design and manufacturer must be high. This is illustrated above.

What is the right Private Label strategy? (continued)



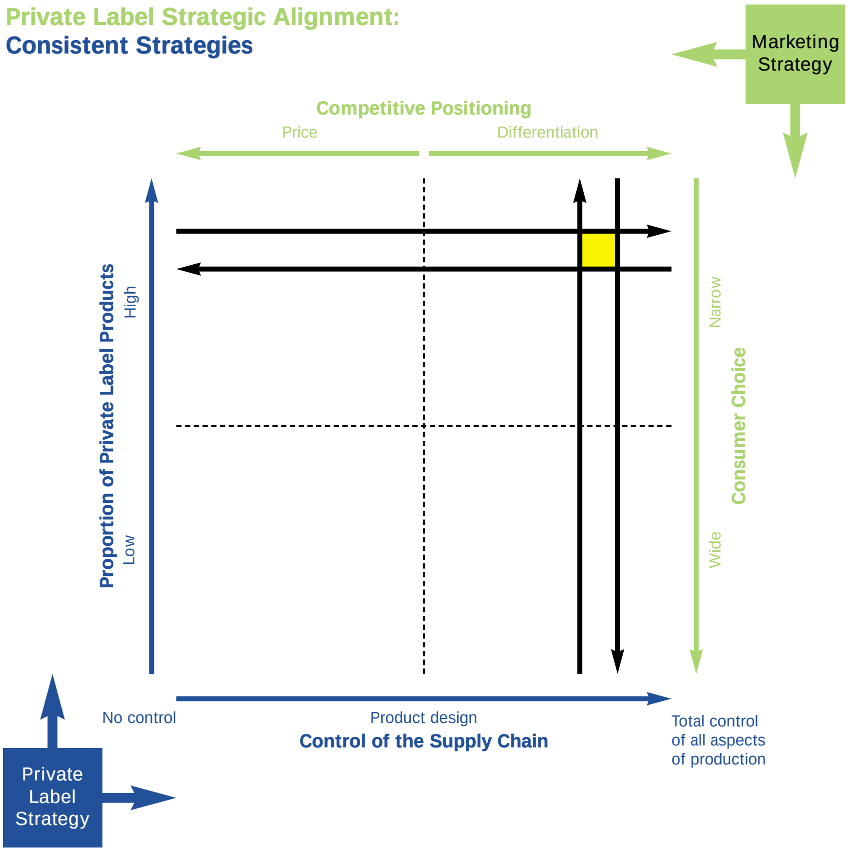
Proportion of Private Label Products

A total commitment to private label brings rewards as well as risks. It means there will be no benchmark in-store for the consumer comparisons. There would be no need for numerous similar products, simplifying the ranges on offer, and allowing more efficient space management, thus reducing costs. This is an important objective of Aldi's to help achieve competitive advantage. Product packaging and merchandising can be more co-ordinated, leading to a clearer brand image, differentiation and greater brand loyalty.

However, saturation of private label penetration, particularly within the UK food sector, has been evident. For example, Sainsbury's private label penetration has reduced recently, apparently to avoid consumer choice becoming too restricted. Thus, "natural" limits on private label penetration appear to exist depending on the consumer choice offered within the overall marketing strategy, as illustrated in this model.

[19] Mintel Marketing Intelligence: Own Label Food, November 1998. Mintel International Group Limited, London

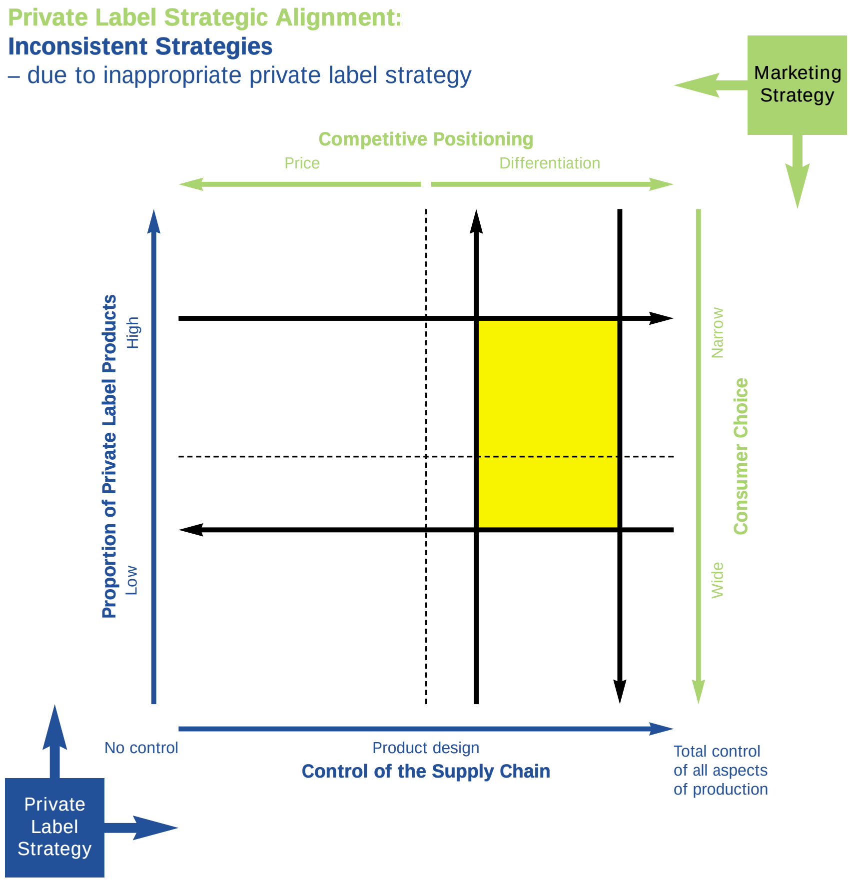
Private Label Strategic Alignment:
Consistent Strategies



Evaluating Private Label Strategies

Using this analytical framework, it is possible to evaluate the consistency of a retailer's private label strategy. A consistent strategy appears as a small area on the framework, while an inconsistent strategy covers a large area.

For example, a retailer with an overall marketing strategy based on a highly differentiated product range (and hence offering limited customer choice) has a consistent private label strategy if there is a high proportion of private label product over which he exerts a high level of design and manufacture control. This would be represented as above.



One example of an inconsistent strategy for this retailer would be if the private label objectives did not align with the overall marketing strategy (see above). Inconsistency may occur through incorrect private label development and/or through a change in the overall marketing strategy.

5 How does Private Label strategy affect retail brand loyalty?

In building loyalty to the retailer brand, many retailers choose to use the store brand as an umbrella brand. This creates marketing synergy between the store name and the private label's product name. The retailer's name on the label can increase the trust towards the products and encourage the consumer to buy. Recently, Asda added the Asda brand name to its Farm Stores range, to bring more trust to the range, as well as strengthening the Asda price positioning.

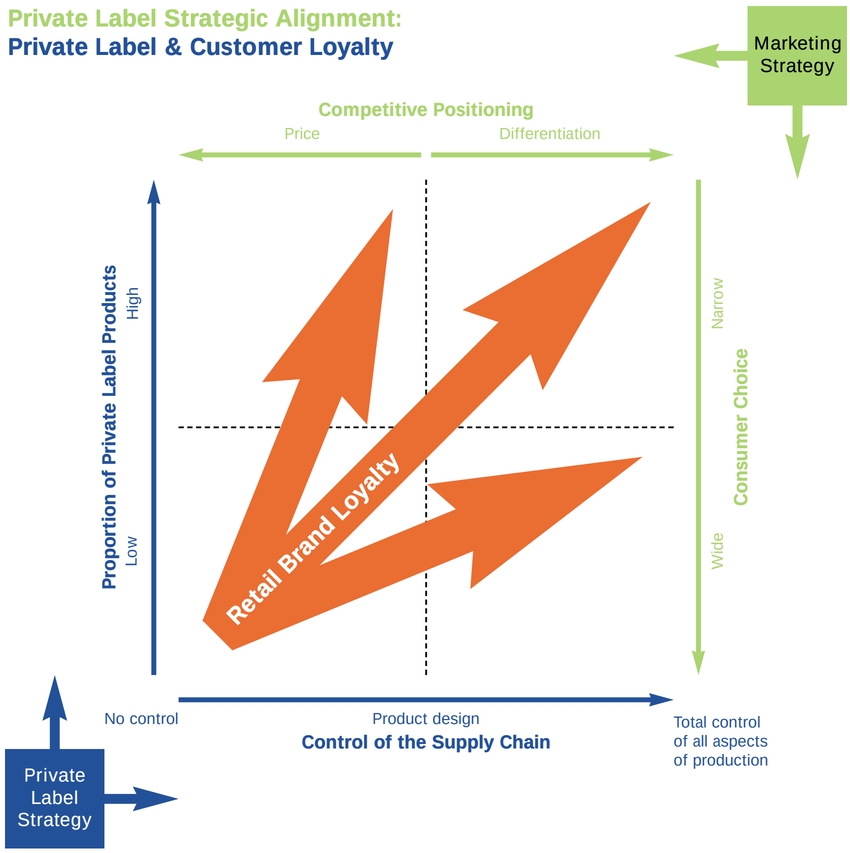
All of the retailers we studied, regardless of their pricing strategy, put heavy emphasis on the quality of their private label, within the limits of their general strategy and price positioning. None would just take the cheapest alternative available, but instead aim for the best combination of price and quality that fits their company strategy.

With the exception of Marks & Spencer, which still has an almost total commitment to private label, all the retailers would stock a branded product if they failed to source a private label product of similar quality. For example, in confectionery where manufacturer brands are very strong, Aldi stocks selected lines from several major brands, such as Mars chocolate bars, because there are no products of similar quality available in the private label market.

To maximise brand loyalty, it is important for a retailer to manage the quality of private label products throughout the range. Retailers must therefore consistently deliver the same quality of private label product. This is especially true in the case of store brands, where there is a strong association between private label products and the retailer. If the retailer has different names for each product, for example Aldi, the ability to convey values of originality and consistency may be reduced. But the consequences of poor product development, low sales and subsequent risk to brand loyalty are also reduced.

As retailers become more highly differentiated and focused, brand loyalty tends to increase, though the relevant potential market may decrease. What is important is to maximise brand loyalty within the overall marketing strategy adopted by the retailer. This can be illustrated in the private label strategic alignment model as follows.

How does Private Label strategy affect retail brand loyalty? (continued)



6 How should Private Label strategy be implemented?

Private label strategies can only be implemented successfully by gaining the consumer's trust in the retailer, and the private label products themselves. The acceptance of private label creates further trust in the retailer's ability to reliably meet consumer needs. Consequently, high standards of quality control (pre-transaction) and customer service (post-transaction) is vital.

The leading UK retailers, with high levels of private label product, enjoy a high level of consumer trust and this continues to increase, as the following table shows.

Company	1994	1997
Boots	78	83
M&S	73	83
Sainsbury's	59	74
Tesco	52	71
ASDA	46	67
Safeway	45	64

% Trusting Companies to be Honest and Fair in the UK[20]

Similarly, retailers are well trusted, even compared to many well-established manufacturer brands, as well as other institutions and professionals, as the following table shows.

Institution/brand	% Trusted
Your GP (Doctor)	85
Kellogg	84
Cadbury	83
Heinz	81
Nescafe	77
Rowntree	74
Your bank	72
Coca-Cola	65
Your church	64
The police	62
Your Member of Parliament	28

Top Brands and Institutions in the Trust Stakes: % Trusting the Following to be Honest and Fair[21]

[20] Source: Henley Centre Planning for Social Change 1998

[21] Source: Brand Strategy July, 24, 1998. Original source: Henley Centre Planning for Social Change 1998

The case study retailers have several ways of reinforcing consumer trust and therefore loyalty towards their private label products. Refund policies aimed at quality assurance are common. Examples of these are Marks & Spencer's "No Questions Asked" refund policy as well as Aldi's "No Quibble Guarantee". Decathlon offers one-year (or more) warranty on all Decathlon products. All Boots brand products are covered by a two-year guarantee. Tesco prints on its private label products that: "We are happy to refund or replace any Tesco product which falls below the high standard you expect. Just ask any member of staff."

Private label product information, such as nutritional information, written on packaging or provided elsewhere in-store exceeds legal requirements and is often found to be more extensive when compared to manufacturer brands. Many retailers produce information leaflets, such as Tesco's healthy eating guide, featuring their private label products, or Boots' medicine guides.

It is often easier and quicker to alter lower volume, private label product specifications than higher volume, manufacturer branded products, in response to changing consumer preferences. For example, some food retailers have been quicker than branded manufacturers to exclude Genetically Modified ingredients from their products, following recent consumer concern.

The unit price and retailer competence influences the amount of trust a consumer needs when making a purchasing decision. This relates to the retailer's core competence. Where the unit price is low the consumer is more inclined to try a private label product, since the consequences of the decision proving unsatisfactory are small. New private label products are also more likely to be successful if they are considered close to the retailer's core competence. Therefore retailers can move transitionally into new product areas. For example, retailers may initially offer loyalty cards or credit before moving to a more comprehensive range of financial services, as we have seen with many leading grocery retailers.

For some products, it is not so much a question of trust in technical elements, but rather social credibility in these niche markets. This is particularly true in high fashion markets. In these and similar upmarket product categories, a generalist retailer's regular store brand may be regarded as being too downmarket. For example, Asda usually puts its logo clearly on the front label of products, but on wine it uses hand-written text to distinguish or mask (depending on your point of view) the Asdawine logo.

Finally, while some customers may only trust branded products, this does not necessarily stop successful private label development. According to consumer research, many customers of Marks & Spencer believe that they never purchase private label products and that only branded ones will do[22]. This is despite the fact that M&S only sell their own private label products.

[22] Mintel Marketing Intelligence: Own Label Food, November 1998. Mintel International Group Limited, London

7 Methodology

This research was carried out through extensive secondary research and primary research during the second half of 1999 through the use of retailer case studies. The primary sources of information are company interviews, company documents (statistics, memorandum, annual reports etc.) and observation. The focus of the study is on Western European retailers and markets.

The Case Study Retailers

Retailers were selected because of the significance of private label to their overall marketing strategy and as they represent different approaches to its development. The chosen discriminators include: the retailing area, the frequency of purchase, the role of private label within the retailer, the use of fascia name, the share of sales of private label, the level of involvement in product design, the degree of vertical integration and the market sector.

Aldi

Aldi is a very well-known example of a successful German discounter with a very high (99%) share of sales for private label. It only operates a single store format with small stores and a very limited product range with individual names for each private label product. It competes on price, and mainly stocks food, but also has short-term non-food offers.

Aldi offers its customers a unique combination of price and quality. However, the consistency and total commitment throughout all operations to reducing costs has been something that competitors have found very difficult to copy, and the strong company culture created by Aldi's founder brothers probably plays a significant part in Aldi's success. Aldi is totally focused on its pricing strategy and private label is an essential tool to pursue this strategy. Aldi expects its suppliers to undertake product development. Total control and a uniform way of operation throughout the company results in better efficiency, less complexity and provide Aldi with the basis for its competitive edge.

Asda Clothing (George)

Asda is a major UK grocery retailer. It has strongly increased its private label offer in recent years and has a private label share of grocery sales of around 50%. It also stocks a wide selection of non-food items, such as clothing, leisure and household goods. One of the major non-food ranges and the main focus in this report is Asda's successful clothing range called George, which forms the major part of Asda's clothing offer and is managed totally separately from the main Asda brand.

Asda has been very innovative with George. By contracting the product design to a high profile fashion professional and his team, Asda appears to have achieved differentiation and therefore competitive advantage. In addition to well designed products and a range that aims to match the needs of its customers, it can be argued that George also gained credibility, often lacking in supermarket clothing, as a result of the high profile of Mr George Davies (the company's founder and Managing Director).

Boots the Chemist

Boots the Chemist is a good example of a successful private label non-food retailer. In its product mix, both private label and manufacturer brands have their own important roles, the shares being around 43% and 57% respectively. Boots has also successfully used sub-branding and has exported its own branded products along with its stores. Boots is involved in manufacturing, has a strong company brand and very high consumer trust, especially in the company's core areas of health and beauty.

Boots' brand image has been developed over more than 100 years. In addition to producing unique products, vertical integration with their own factories reinforces the authority of the Boots brand. Boots gives a full refund on products the customer wants to bring back and gives a two-year guarantee to all Boots private label products.

Decathlon

Decathlon is a French sports retailer. It stocks both manufacturer brands (45% of sales) and private label (55% of sales). The private label products are in product categories that include some of the most advertised manufacturer brands in the world. Decathlon has a number of differently sized stores, either specialising in one sport or offering a wide range of all sports-related merchandise. The majority of its stores are in France, with current expansion to other European markets.

Private label is used in Decathlon as a tool to create an uniquely wide product range in its specialist area, with various price and quality choices for the customer. The depth, innovation and quality of the product range combined with supporting product information and knowledgeable staff help give Decathlon and its private label ranges credibility. The retailer's investment in product development and quality control plays an important role in the success of private label products in both fashionable sports clothing and more technical specialist equipment.

Marks & Spencer plc

Marks & Spencer is one of the most famous private label retailers in the world. The company has been in the forefront of private label development for decades and in many aspects, can be seen to have had great importance in influencing the development of private label in the UK and later, through its international expansion, in other parts of the world. In the past, M&S has also been very successful in both its food and non-food offer. It sells its own generic brands and has a reputation for good quality and value for money. It does not own any factories but is closely involved in product development and quality control at all stages of the supply chain.

M&S has achieved very high levels of trust from its customers, which appears to have been achieved through heavy involvement in the supply chain, strict quality control and a very flexible refund policy. By investing in product development and strong supplier relationships, M&S has been able to form a unique product range that aims to offer value for money.

Migros

Migros is the market leader in food retailing in its home country of Switzerland. Migros serves a mass market with many differently sized store formats and a wide range of products. It also has an exceptionally high private label share of sales (around 95% in food). Migros is an example of a vertically integrated retailer, operating in a relatively small market. In addition to food, it also has a wide range of non-food products as well as other services.

Migros is an exceptional retailer in many respects. It's unique company principles, set in the early years by the founder of the company, and a wide range of business activities combined with a very dominant market position sets it apart from most other retailers. Migros is unique in having an extremely high private label penetration, even though it is a generalist grocery retailer with a wide range of products. This has been made possible through the massive vertical integration of the company. In addition, private label has an important role in Migros by making the company principles alive in the form of products – thus reinforcing Migros' market positioning.

Tesco plc

Tesco has the highest market share in UK food retailing. Private label is thought to have been of great importance in building its success and retail brand. It operates many store formats and has a number of differently positioned private label sub-brands though always in conjunction with the Tesco name. Private label share of sales at Tesco is around 50%.

Tesco is a generalist retailer with a wide range of products especially in its main business area, food. Private label has an important role in Tesco by creating a range that gives customers more choice in terms of different product varieties and price. However, brands still have an important role in its ranges, leading innovation and in creating an attractive total offer for Tesco's customers. Tesco aims to achieve synergy in marketing by using the store brand across all its store formats, services and private label products.

Technical Note

Statistical data on private label is variable. A common statistical measure of private label is its share of sales in a product category, country or retailer. The most usual sources of data are EPoS-scanning and consumer panels conducted by market research organisations. However, the lack of standard definition for private label within the retailing industry creates much variation when comparing private label shares between retailers, categories and countries.

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This research was conducted by Dick Bell, Richard Cuthbertson and Satu Koskinen from OXIRM for Emyr Williams and Richard Clarke from KPMG.

For further details contact:

Emyr Williams
emyr.williams@kpmg.co.uk

KPMG
8 Salisbury Square
London
EC4Y 8BB
http://www.kpmg.co.uk

Telephone: +44 (020) 7311 8696
Facsimile: +44 (020) 7311 3311

For further information, please contact KPMG's Global Consumer Markets group in the following offices:

UK
David P Clifford
+44 (020) 7311 8962

Ireland
Robert Dix
+353 (1) 410 1390

Sweden
Per Gustafsson
+46 (8) 723 9358

Finland
Wilhelm Holmberg
+358 (9) 693 93 692

Austria
Peter Humer
+43 (732) 6938 2212

Norway
Eivind Lonheim
+47 2207 2263

The Netherlands
Ton Oudejans
+31 (20) 656 7580

Spain
Valeriano Perez
+34 (-) 9145 63400

France
Patrick Petit
+33 (1) 556 87 080

Italy
Salvatore Sanna
+39 (080) 524 3203

Germany
Johannes Siemes
+49 (221) 207 3248

Belgium
Karel Van Oostveldt
+32 (3) 825 2025

Central & Eastern Europe
Stephen Young
+36 (1) 270 7100

Asia Pacific
Tim Mason
+61 3 9288 5568

Americas
Mark Larson
+1 312 665 1488

For further information, please contact KPMG at:

KPMG International Headquarters
Burgemeester Rijnderslaan 20
1185 MC Amstelveen
The Netherlands
Tel: +31 (20) 656 6700
Fax: +31 (20) 656 6777
Web: www.kpmg.com

Austria
Schwarzenbergplatz 16
A-1010 Vienna, Austria
Tel: +43 (1) 506 32
Fax: +43 (1) 506 32/60 00
Web: www.at.kpmg.net

Belgium
Avenue du Bourgetlaan 40
B-1130 Brussels, Belgium
Tel: +32 (2) 708 43 00
Fax: +32 (2) 708 43 99
Web: www.be.kpmg.net

Denmark
Borups Allé 177
Copenhagen, Denmark
Tel: +45 (38) 18 38 18
Fax: +45 (38) 18 38 19
Web: www.kpmg.dk

France
21 rue Dumont d'Urville
F-75116 Paris, France
Tel: +33 (1) 56 89 60 00
Fax: +33 (1) 56 89 60 10
Web: www.fr.kpmg.net

Germany
Traubenstrasse 44-45
10117 Berlin, Germany
Tel: +49 (30) 2068 0
Fax: +49 (30) 2068 2000
Web: www.kpmg.de

Hungary
XIII Váci út 99
H-1139 Budapest, Hungary
Tel: +36 (1) 270 71 00
Fax: +36 (1) 270 71 01
Web: www.hu.kpmg.net

Ireland
Russell Court, Stoke's Place
St Stephen's Green
Dublin 2, Ireland (Republic)
Tel: +353 (1) 410 18 00
Fax: +353 (1) 412 18 88
Web: www.kpmg.ie

Italy
Via Vittor Pisani 25
20124 Milano, Italy
Tel: +39 (02) 67 64 31
Fax: +39 (02) 67 64 36 03
Web: www.kpmg.it

The Netherlands
Rijnzathe 10
3454 PV De Meern, The Netherlands
Tel: +31 (20) 658 1658
Fax: +31 (20) 658 3658
Web: www.kpmg.nl

Norway
Brynsveien 12
0667 Oslo, Norway
Tel: +47 22 07 22 07
Fax: +47 22 72 42 82
Web: www.no.kpmg.net

Russia
Ul Staraya Basmannaya, 38/2 bld. 1
Moscow 107066, Russia
Tel: +7 (502) 937 44 77
Fax: +7 (502) 937 44 00/99
Web: www.ru.kpmg.net

Spain
Edificio Torre Europa
Paseo de la Castellana 95
Madrid 28046, Spain
Tel: +34 (91) 456 34 00
Fax: +34 (91) 555 01 32
Web: www.es.kpmg.net

Sweden
Tegelbacken 4A
SE-111 52 Stockholm, Sweden
Tel: +46 (8) 723 91 00
Fax: +46 (8) 10 52 58
Web: www.kpmg.se

Switzerland
Badenerstrasse 172
Ch-8004 Zurich, Switzerland
Tel: +41 (1) 249 31 31
Fax: +41 (1) 249 23 19
Web: www.kpmg.ch

United Kingdom
8 Salisbury Square
London EC4Y 8BB, United Kingdom
Tel: +44 (20) 7311 1000
Fax: +44 (20) 7311 3311
Web: www.kpmg.co.uk

Africa
South Africa
KPMG Crescent, 85 Empire Road
2122 Parktown, South Africa
Tel: +27 (11) 647 71 11
Fax: +27 (11) 647 80 00
Web: www.kpmg.co.za

Middle East
Bahrain
5th Floor, Chamber of Commerce &
Industry Building
Manama, Bahrain
Tel: +973 22 48 07
Fax: +973 22 74 43

Designed by IDP Design Consultants 020 8658 8858

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