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GROWTH AND STRATEGIES OF LARGE, LEAD FIRMS - SUPERMARKETS

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Abstract

Supermarkets are a key route to market for suppliers of food and household consumable products in South Africa. The growth, performance and strategies of the retail industry driven by JSE-listed supermarket chains therefore has important implications for suppliers and, in turn, for the development trajectory of agro-processing and light manufacturing industries. However, costly trading terms and stringent requirements limit the participation of suppliers in supermarket supply chains.

This paper tracks the performance, investment and growth strategies of supermarket chains in South Africa between 2010 and 2016. Key findings reveal that although the formal supermarket industry has grown significantly over the past six years (measured by investments in assets and real turnover), it has remained relatively concentrated with only a handful of main players. Local supermarkets are also expanding their investments into the rest of Africa in search of new markets. The paper further evaluates the implications of supermarket procurement strategies on the ability of local suppliers to participate in supermarket supply chains. It highlights a wide range of constraints that suppliers face in accessing supermarket shelf space. To increase participation of local suppliers, the study recommends better designed and more sustainable supplier development programmes. It also recommends the implementation of a retail code of conduct to curb uneven balances of power and to promote transparency in procurement procedures and trading terms.

L1, L2, L25

List of Figures

List of Tables

1. Introduction

Supermarkets have grown rapidly in southern African countries, largely in the form of foreign direct investment (FDI) by lead JSE-listed South African supermarket chains Shoprite, Pick n Pay, SPAR, Woolworths and non-JSE listed Fruit and Veg City. However, recently, Botswana-owned Choppies Enterprises (also listed on the JSE), has made strong in-roads into southern and East Africa. Large transnational corporations, such as Walmart, have also entered southern African markets through the take-over of South African Massmart (approved in June 2011), and are moving into grocery retail offerings. The formats of supermarkets in South Africa have changed over time, shifting from serving high-end affluent consumers in urban areas to successfully penetrating new markets in lower-income communities. Investments in more efficient procurement and distribution systems have facilitated this spread into low-income rural areas in many countries globally and in southern Africa (Weatherspoon and Reardon 2003).[1]

Why do supermarkets matter and why is it important to track their growth, spread and strategies? The development of supermarkets has important consequences for both consumers and suppliers of food and household consumable products. Supermarkets can offer consumers cheaper prices relative to local independent retailers given economies of scale and global/regional sourcing strategies. Modern supermarkets offer consumers the supplementary service of arranging a wide assortment of products selling concurrently in a convenient setting in a single location with a focus on quality, service, 'one-stop' shopping, and an overall shopping experience (Haese and Van Huylenbroeck 2005; Basker and Noel 2013). Supermarkets have also extended their offering to include a suite of other services, such as financial, cellular and pharmaceutical services as well as serving as payment and purchase points for utilities.

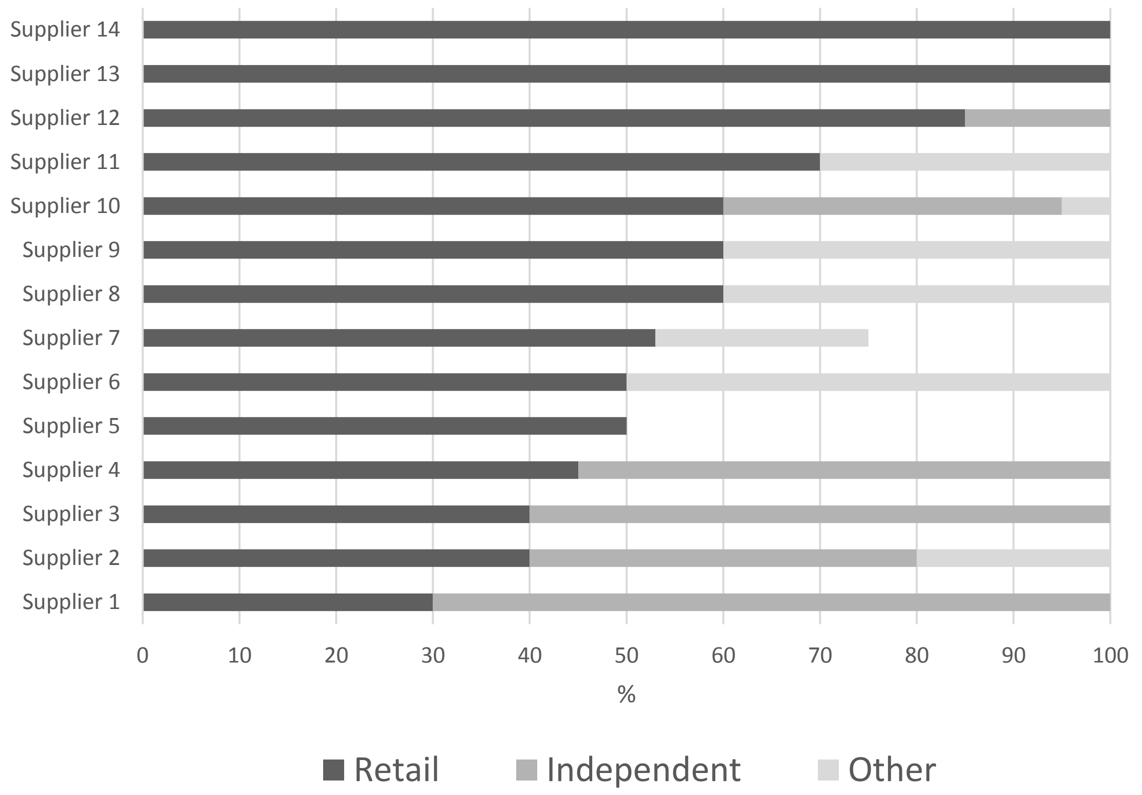
Although the growth of supermarkets has provided wide-ranging benefits to consumers, it has also imposed challenges on the ability of local suppliers to enter and participate in the economy. Supermarkets are a key route to market for suppliers of food and household consumable products. Suppliers sell a large (and growing proportion) of their products through formal supermarket chains (see Figure 1 for selected suppliers). The multinational nature of supermarket chains further opens up much larger regional markets for suppliers providing opportunities for them to participate in the growth process. This allows suppliers to attain the necessary scale to become competitive in national, regional and international markets. Supermarkets therefore have the power to shape value chains and influence growth and investment decisions of suppliers (and linked sectors like transport & logistics). Their procurement

[1] This paper draws from extensive research undertaken for UNU-Wider from three reports under the broad theme "*The Expansion of Regional Supermarket Chains: Changing models of retailing and the implications for local supplier capabilities in South Africa, Botswana, Zambia, and Zimbabwe*", by Reena das Nair and Shingie Chisoro, Centre for Competition, Regulation and Economic Development (CCRED). Full papers references can be found in the reference list.

methods and requirements have important implications for the participation and success of suppliers.

Supermarkets can thus be a strong catalyst to stimulate food processing and light manufacturing industries in South Africa, which is squarely in line with objectives of national industrial policies as well as regional policies such as the Southern African Development Community's (SADC) Industrialisation Strategy and Roadmap, 2015 – 2063.

Figure 1: Proportion of sales by selected suppliers to retail chains, independent retailers and other buyers, 2015-2016



Source: Interviews with selected suppliers of basic food products (such as poultry, dairy, processed foods, maize meal etc.)

Large supermarket chains are often lead firms in global and regional agro-processing value chains. These chains tend to be 'buyer-driven' value chains, where lead supermarkets govern or control the value chain. In these chains, production functions are usually outsourced, while lead firms focus instead on branding, marketing, design and retailing functions (Gibbon and Ponte, 2005). Large supermarkets, retailers, marketers and branded product manufacturers often play a key role in these types of value chains in coordinating decentralised production networks (Humphrey and Schmitz, 2002; Gereffi et al, 2001).

Concerns have been raised that large supermarkets place stringent demands that small and medium-sized local suppliers often find difficult to fulfil given lack of capabilities. This has the effect of excluding these suppliers from important, dynamic, and expanding supply chains (Humphrey 2007). These concerns are exacerbated by the fact that the formal retail industry remains concentrated in South Africa and in the region more broadly. The top three supermarket chains control over 80% market share based on the number of food stores in formal retail (see Table 3 later). Structural and strategic barriers in the retail industry serve to maintain these high concentration levels.[2] Lack of effective competitive rivalry to the major supermarkets chains means that large retailers with market power can engage in anticompetitive behaviour with negative effects on suppliers. Concentrated markets limit suppliers' options and exposes them to potential abuses of buyer power through costly trading terms and other onerous requirements of supermarkets.

It is therefore important to monitor and assess the performance and strategies of supermarkets as large, lead firms that drive value chains. As part of the research for the Industrial Development Research Project (IDRP) Research Stream 1, this report evaluates the growth and performance of lead supermarkets in South Africa over the past five years and the implications of this on supplier development.

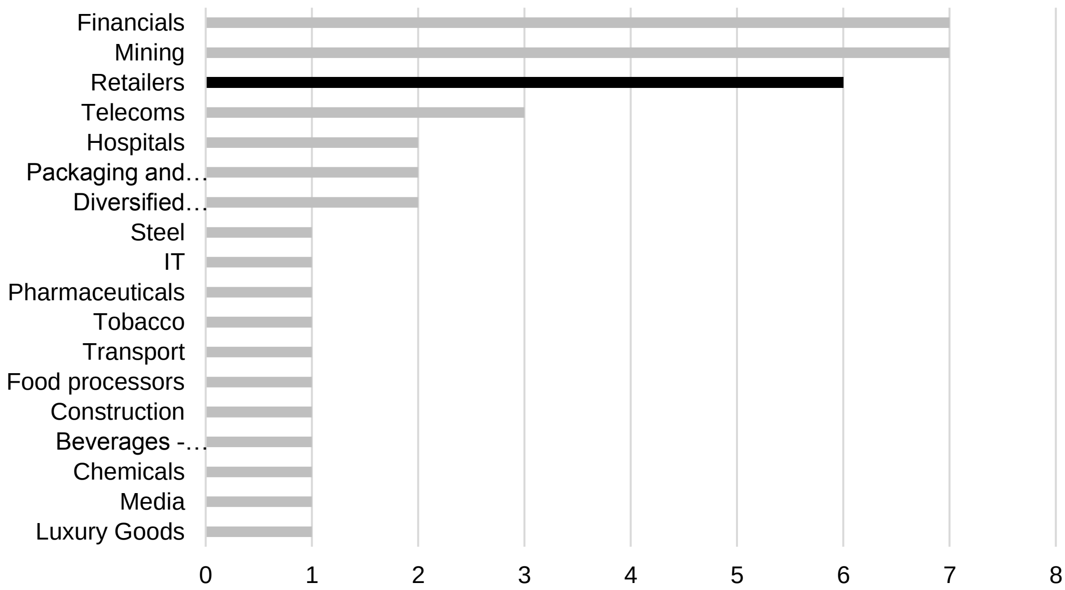
This report is structured as follows. Section 2 looks at the positioning of listed supermarkets on the JSE. Section 3 maps the key supermarket players in South Africa and how they have evolved with respect to formats and offerings. It tracks the growth and performance of these firms using publicly available data sources. Section 4 assesses the impact of the growth of supermarkets on suppliers, drawing on extensive past research undertaken by CCRED. This section also discusses the types of assistance provided to suppliers by supermarkets through supplier development programmes. Section 5 provides preliminary conclusions and policy recommendations for the sector.

[2] For a detailed review of these barriers, see das Nair and Chisoro (2015), https://static1.squarespace.com/static/52246331e4b0a46e5f1b8ce5/t/56dd491740261df5707f9976/1457342749136/CCRED+Working+Paper+9_2015_BTE+Fruit%26Veg+ChisoroDasNair+290216.pdf

2. Positioning of grocery retailers/supermarkets on the JSE

Figure 2 shows that retailers, which include supermarkets, are the third largest sector in terms of number of firms in the JSE Top 40 ranked by turnover, with six firms featuring in the Top 40.

Figure 2: Number of firms by sector in JSE Top 40 (turnover), 2015



Source: I-Net BFA. Note: 2016 data is only available for some companies

Five of the six retailers in the JSE TOP 40 by revenue are supermarkets (the sixth being Steinhoff, a furniture retailer). Turnover for the listed supermarkets has increased significantly between 2010 and 2015 (Table 1).

Table 1: JSE Top 40 by turnover (R billion), 2010 and 2015

	Company	Sector	2015 Turnover	2010 Turnover
1.	Glencore Plc	Mining	2653	1813
2.	BHP Billiton Plc	Mining	636	404
3.	Anglo American Plc	Mining	318	184
4.	British American Tobacco Plc	Tobacco	299	153
5.	SABMiller Plc	Beverages - Brewers	269	131
6.	Sanlam	Financials	239	123
7.	The Bidvest Group	Diversified industrials	205	110
8.	Sasol	Chemicals	185	122
9.	MTN Group	Telecoms	147	115
10.	Old Mutual Plc	Financials	145	70
11.	Steinhoff International N.V.	Retailers	137	48
12.	Richemont SA	Luxury Goods	136	51
13.	Mondi Limited	Packaging and paper	115	55
14.	Shoprite Holdings	Retailers (supermarket)	114	67

15.	Imperial Holdings	Transport	110	54
16.	Massmart Holdings	Retailers (includes supermarkets)	85	47
17.	Vodacom Group	Telecoms	77	59
18.	Datatec	IT	75	29
19.	Sappi	Packaging and paper	75	46
20.	The SPAR Group	Retailers (supermarket)	73	35
21.	Naspers	Media	73	28
22.	Anglogold Ashanti	Mining	67	262
23.	Pick n Pay Stores	Retailers (supermarket)	67	55
24.	Standard Bank Group	Financials	65	38
25.	Barloworld	Diversified industrials	63	42
26.	Anglo American Platinum	Mining	60	46
27.	Woolworths Holdings	Retailers (supermarket)	57	26
28.	Liberty Holdings	Financials	54	22
29.	Aveng	Construction	44	34
30.	FirstRand	Financials	40	18
31.	Barclays Africa Group	Financials	39	23
32.	Kumba Iron Ore	Mining	36	39
33.	Aspen Pharmacare Holdings	Pharmaceuticals	36	10
34.	MMI Holdings	Financials	35	10
35.	Mediclinic International	Hospitals	35	17
36.	Netcare	Hospitals	34	22
37.	Impala Platinum Holdings	Mining	32	25
38.	Telkom SA SOC	Telecoms	32	37
39.	Tiger Brands Limited	Food processors	32	19
40.	ArcelorMittal SA	Steel	31	30

Source: INET BFA. Note: 2016 data is only available for some companies

The firms are also considered in terms of their JSE market capitalisation in 2015/2016. On this basis, Woolworths and Shoprite are the largest supermarket chains in the retail industry in South Africa (Table 2).

Table 2: Supermarket groups ranked by JSE market capitalization as at 03 March 2016

	Market capitalisation as reported in annual reports (ZAR billions)
Woolworths Holdings	74.2
Shoprite Holdings	109.9
SPAR Group	34.5
Pick n Pay Stores	34.4
Massmart Holdings	32.6
Choppies Limited	4.3

Source: INETBFA

3. Growth and performance of key supermarkets in South Africa

As can be seen in Table 3 below, the national market is dominated by three large chains (in terms of store numbers) – Shoprite Holdings, Pick n Pay and SPAR. Woolworths, Walmart's Game and Fruit and Veg City's Food Lovers Market hold most of the balance of the share. Choppies, the newest player is a Botswana-owned supermarket chain that has entered and grown rapidly in the past few years. There are a large number of independent retailers backed by buying groups that are also active in the supermarket industry (not reflected in Table 3). While several these are under the same 'banner' group or name, sponsored by buying groups, they are owned by individuals. These independent retailers are also not listed. We do not assess them further in this study.

Table 3: Number of stores and ownership in South Africa (main chain stores only)

Supermarket (number) – Ownership	Share (based on store numbers)
Shoprite (1284) [3] - SA	31%
Pick n Pay (1280) [4] - SA	30%
SPAR (890) [5] - SA	21%
Woolworths (382) [6]- SA	9%
Game/Walmart (203) - USA[7]	5%
Food Lovers' Market (+100) - SA	2%
Choppies (64) - Botswana[8]	2%
TOTAL	**100%**

Source: Compilation from Annual Reports

Note: This only includes supermarkets and not the other offerings of the holding company, such as furniture, fast food, liquor and pharmacy outlets.

We provide an overview of each of the main supermarkets and map the performance of individual supermarkets over a five-year period from 2010 to 2016.

In general, the supermarket industry is characterised by higher current assets than fixed assets. This is explained by the nature of the retail business, where major assets

[3] Shoprite store numbers comprised of Shoprite, Checkers, Checkers Hyper, Usave and OK Franchise were retrieved from Shoprite 2016 Integrated Annual Report.
[4] Pick n Pay store numbers were retrieved from Pick n Pay 2016 Integrated Annual Report. This report does not differentiate among the different store formats.
[5] SPAR store numbers were retrieved from Integrated Annual Report 2016. The source does not differentiate between the different formats.
[6] This number comprised of Woolworths Food stores was retrieved from Woolworths Annual Financial Statement 2016 pp. 26.
[7] Massmart Annual Report 2016. Comprises 20 Makro stores in South Africa, 57 Cambridge stores in South Africa and estimated that 90% of total regional Game stores (141) are in South Africa.
[8] Massmart Annual Report, 2016

constitute inventory (products on the shelves or stored in warehouses), accounts receivables or debtors and cash and cash equivalents. Capital expenditure typically constitutes a relatively smaller proportion of total assets, and is directed towards purchase of vehicles, investments in distribution centres and new stores.

3.1 Shoprite Holdings

The largest supermarket chain in South Africa in terms of store numbers is Shoprite Holdings. Specialising in foodstuffs and household items, Shoprite was the first supermarket to establish branches in the southern African region. Headquartered in South Africa, it has operations in 14 other African countries.[9] Over and above its 1,514 supermarket stores across Africa, the group has food outlets, furniture stores, liquor stores and pharmacies. Shoprite's main listing is on the Johannesburg Stock Exchange since 1986, in addition to being listed on the Namibian Stock Exchange since 2002 and the Lusaka Stock Exchange since 2003. It is the only South African chain to have multiple listings on stock markets in the continent, an indication of its level of internationalisation (Dörrenbächer, 2000). The company organogram (as well as that for all the other supermarkets) is given in Appendix A.

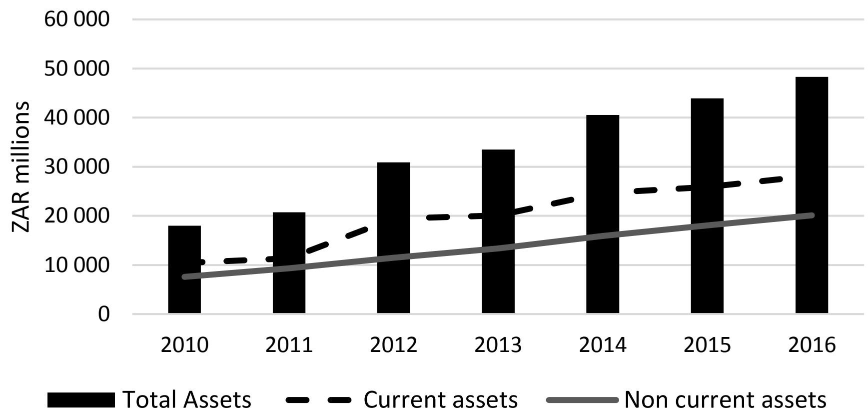
Shoprite Holdings has four core supermarket offerings in South Africa: Shoprite, Checkers, Usave, and OK. It has built a broad customer base catering for the different demographic profiles and set up different store formats to meet the needs of the full spectrum of different income groups/living standard measures (LSM) categories in South Africa.[10] Checkers and Checkers Hyper stores target high-end affluent consumers whereas Shoprite focuses on the broad middle-to-lower end market segments. Shoprite is increasingly extending its offering to lower-income segments by penetrating economically disadvantaged communities through Shoprite Usave. Shoprite Usave is used as a tool to spearhead expansion into the rest of Africa. Further, Shoprite also runs the OK franchise, which caters for smaller convenience-oriented markets located in rural towns, suburbs and neighbourhoods.

3.1.1 Investment trends

Shoprite's total assets grew by approximately 18% per annum between 2010 and 2016 with current assets constituting 60% of total assets (Figure 3).

[9] Angola, Botswana, Ghana, Lesotho, Madagascar, Malawi, Mauritius, Mozambique, Namibia, Nigeria, Swaziland, Uganda, Zambia, and DRC.
[10] LSMs have become the most widely used marketing research tool in southern Africa. It divides the population into 10 LSM groups: 10 (highest) to 1 (lowest). LSMs segment the market according to their living standards using criteria such as degree of urbanization and ownership of cars and major appliances.

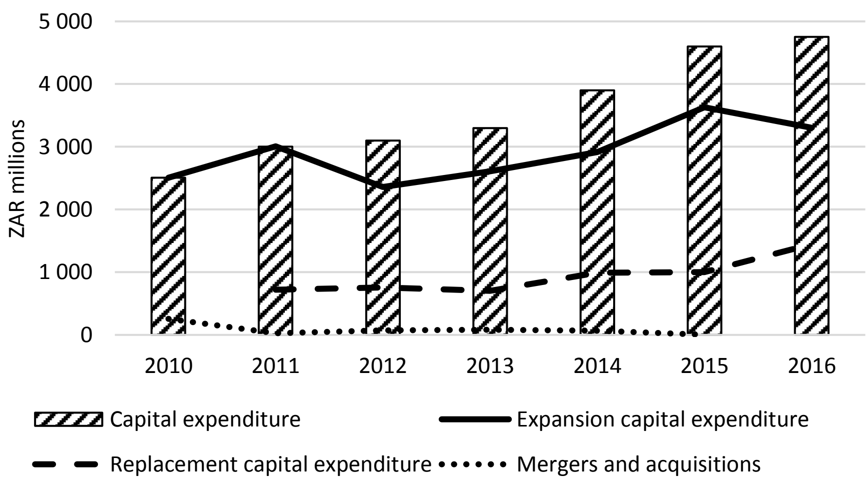
Figure 3: Shoprite Total Assets, 2010-2016



Source: Osiris and INETBFA McGregor

Shoprite's overall capital expenditure grew by a CAGR of 11% over the six-year period mainly driven by expansion capital expenditure (Figure 4). Expansion capital expenditure comprise cash expenditures on land and buildings, distribution centres, new stores and information technology. Shoprite invested significantly in establishing new stores within and outside South Africa. Investments in new stores accounted for 40% of total capital expenditure in 2014 and 2016. Since 2010, the group has embarked on a policy of purchasing vacant land for creating retail space in places where developers cannot be found particularly in economically disadvantaged and underserviced areas, including in countries in the SADC region.[11] The establishment of new stores and acquiring of land fits in with the organisation's rapid organic growth strategy. The group has seen relatively lower levels of mergers and acquisitions in recent years.

Figure 4: Shoprite Capital Expenditure, 2010-2016



Source: Company Annual Reports

[11] Shoprite Annual Reports

Since 2010, Shoprite has extensively invested in a network of advanced distribution centres supported by sophisticated information management systems and transport operations.[12] The group aims to achieve a wide-spread and efficient supply-line to support local and regional growth plans. Information technology and a strong fleet of refrigerated and ambient trucks facilitate the flow of information and movement of products across borders.[13] Between 2013 and 2015, Shoprite's investments in distribution centres and related equipment and vehicles has more than doubled from ZAR228 million to ZAR655 million in 2015 (an increase of 187%, see Table 4) before dropping to ZAR415 million in 2016. In 2015, expenditure on distribution centres (DCs) constituted 14% of total capital expenditure. Shoprite controls its whole supply chain in the region and is over 85% centralised with a 98% service level to all stores in the region. Shoprite's sophisticated and efficient distribution infrastructure in South Africa has helped in keeping prices competitive which has helped the group achieve world-class trading margins.[14]

Table 4: Shoprite Capital Expenditure in Distribution Centres

	Capital expenditure, ZAR millions			
	Dec-13	Dec-14	Jun-15	Jun-16
Distribution centres	137	228	280	379
DC- related equipment and vehicles	91	181	375	36

Source: Annual Reports

Shoprite's growth strategy is to aggressively expand into the rest of Africa while maintaining its strong market leader position in South Africa. Shoprite has been the market leader in terms of keeping up with evolving markets and exploiting opportunities in the region. As of 2016, the group owns 1855 stores in 15 African countries. The capped growth in South African operations might suggest a degree of saturation of home markets. However, regional operations are still underdeveloped accounting for only 14% of the group's overall sales for the period under review.

The main challenges associated with entering regional markets include bureaucracy in the different countries, making it difficult to register a business or acquire land for retail premises.[15] In addition, the long waiting periods at the border posts delay trucks resulting in extended delivery times.[16] However, Shoprite realizes the potential market in the rest of Africa following the high economic growth rates in many countries. Shoprite plans to grow its regional operations through building strong supply chains by making investments in distribution centres. Shoprite's cost competitiveness and dynamic management capabilities have enabled it to respond quickly to evolving

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[12] Shoprite Annual Reports
[13] Shoprite Annual Reports
[14] According to Shoprite CEO, Whitey Basson, '*Heavy investment in distribution and technology has resulted in huge cost savings. We now have the lowest cost structure in the industry*.' (Benetar, 2015)
[15] Shoprite Annual Reports, 2010-2015
[16] Shoprite Annual Reports, 2010-2015

markets have helped the group to tap into new markets as is evident in its success in these markets (see below).

3.1.2 Profitability trends

The profitability of a supermarket is determined by the ability to generate high sales revenue and adopt effective cost control methods. The group's real turnover realised a compound annual growth rate of 6% between 2010 and 2016 (Table 5). In addition, Shoprite's profit margins have improved over the six-year period with a slight decrease in gross profit margins between 2015 and 2016. Overall, Shoprite's growth in real turnover and profitability is mainly due to effective control of costs in all areas of the business and an efficient distribution model.[17]

Table 5: Shoprite Profitability Indicators, 2010 – 2016

	2010	2011	2012	2013	2014	2015	2016
Real turnover (millions)[18]	77 320	78 155	84 767	90 279	94 722	100 361	107 535
Gross profit margin (%)	21.23	22.06	22.56	23.19	23.15	24.70	23.11
Net profit margin (%)	3.36	3.47	3.66	3.88	3.65	3.63	3.72
Return on Equity (%)	38.38	35.43	23.63	23.58	21.58	21.52	22.62
Return on Assets (%)	12.60	12.12	9.74	10.74	9.20	9.39	10.03

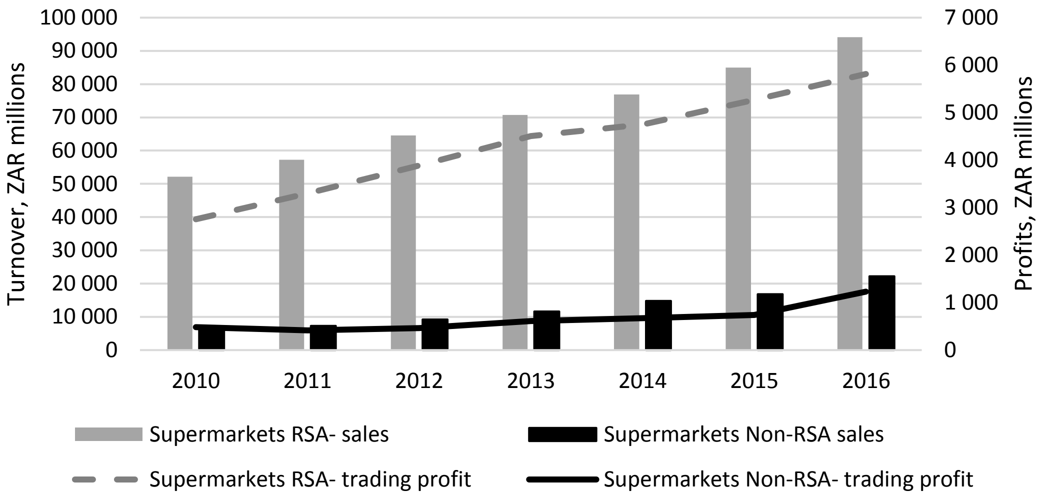
Source: Osiris, INET BFA and annual reports. Nominal turnover adjusted to 2012 constant prices using CPI index. Base year=2012

In terms of supermarket sales and profits, the figure below (Figure 5) shows Shoprite's sales and profits both for their South African supermarkets (excluding all other offerings such as furniture and fast food) and their non-RSA supermarkets.

As is evident, both SA and non-RSA supermarket sales grew, as did profits. Profit and sales growth rates outside South Africa (majority of which is in the rest of Africa) are rising. CAGR of sales between 2010 and 2016 for non-RSA operations were around 21% compared to around 10% for South Africa. Similarly, non-RSA trading profits grew faster than South African operations recording CAGR of 17% compared to 13%. In 2016, non-RSA profits for Shoprite hit the ZAR1billion mark. Shoprite has several 'ownership' advantages in terms of its sheer size, management skills, efficient distribution centres, organisation innovation, ability to integrate into new markets, brand name, ability to access capital and reputation for low prices. Greater returns (relative) outside SA may see even greater investments in Africa in the future.

[17] Shoprite Annual Reports, 2015
[18] Inflation adjusted turnover

Figure 5: Shoprite South African and Non-RSA supermarket sales and profits, 2010 - 2016

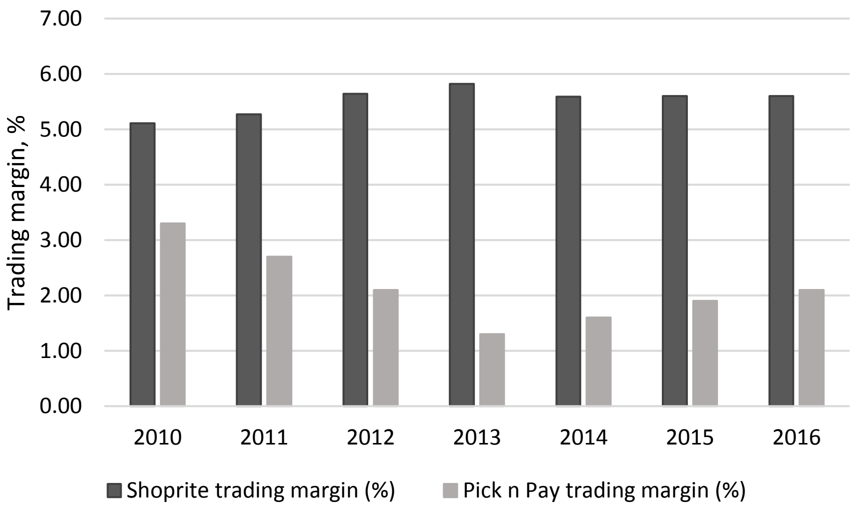


Source: Shoprite's Annual Reports

Shoprite has been the market leader in terms of keeping up with evolving markets, making investments in retail modernisation and exploiting opportunities in the region. It has achieved this through its many ownership advantages. Pick n Pay (below) has largely played the follower role to remain competitive. To be able to tap into new markets, cost competitiveness is important. Shoprite's investments in distribution centres, in addition to dynamic management responding aggressively and quickly to evolving markets, has translated to it offering lower priced products.

Shoprite's trading margins compared to the next biggest player, Pick n Pay, also show its strong market leader position (Figure 6).

Figure 6: Trading margins of Shoprite and Pick n Pay, 2010 - 2016

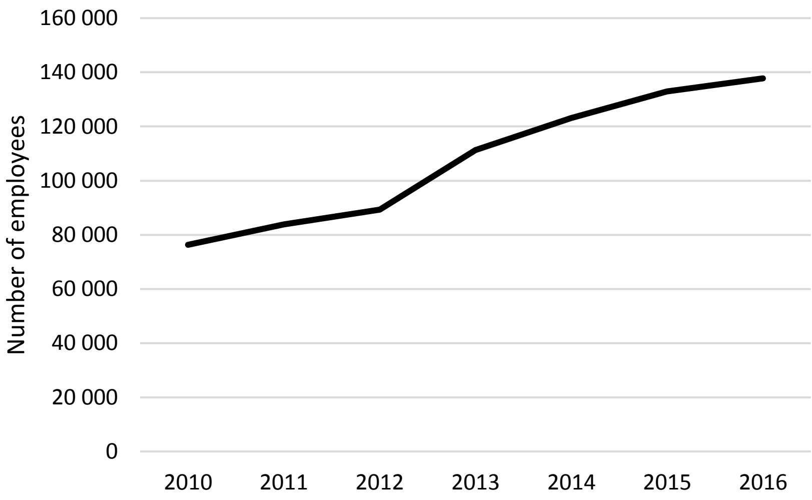


Source: Annual Reports

3.1.3 Employment trends

Shoprite's employment levels in South Africa and the region increased by 81% from 76,318 employees in 2010 to 137,775 in 2016 (Figure 7). The growth in employment is largely attributed to the group's organic growth strategy in South Africa and the region. Shoprite is a key contributor to overall employment in the supermarket industry accounting for approximately 50% of the industry's total employment in South Africa.

Figure 7: Shoprite Growth in Employment, 2010 - 2016



Source: Osiris

3.2 Pick n Pay Holdings

Pick n Pay Holdings, the second largest retailer in South Africa specialises in groceries, clothing, and general merchandise. Pick n Pay supports 1,128 operations across Africa. In South Africa, Pick n Pay operates across multiple store formats, both franchised and corporate-owned. These include Pick n Pay Hypermarkets, Supermarkets, Family Franchise stores and Butcheries. Pick n Pay also recently opened Express franchise stores in collaboration with BP Southern Africa.[19] These are small-format convenience stores located at BP forecourts. Collaborations with fuel companies is something that Shoprite has not yet ventured into.

Like Shoprite however, Pick n Pay is increasingly targeting lower-income consumers, moving away from its traditional, upper-income customer segment. As part of this strategy, it acquired Boxer Superstores in 2002. Currently in Africa, Pick and Pay is only listed on the Johannesburg Stock Exchange (since1981).

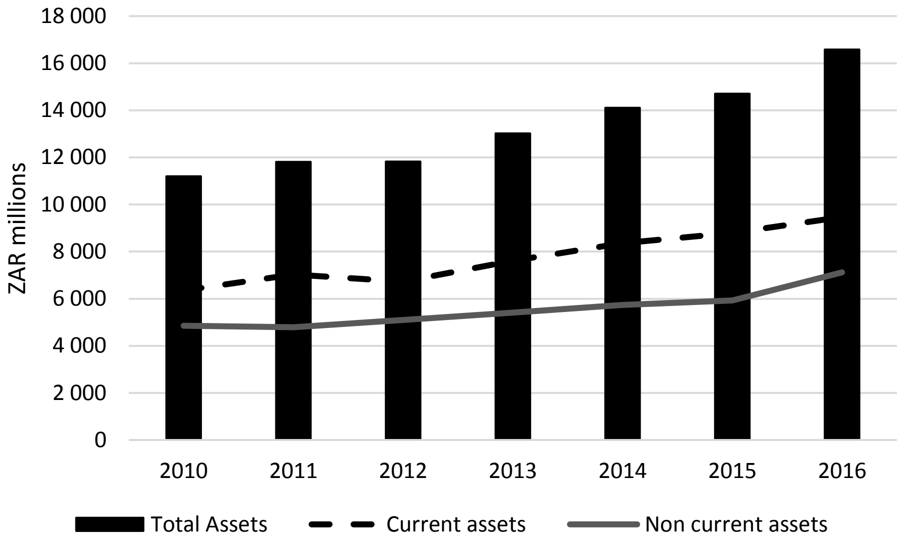
3.2.1 Investment trends

In contrast to Shoprite, Pick n Pay's investment record is a lot less aggressive with total assets having grown by a compound annual growth rate of only 7% between 2010

[19] http://www.shopriteholdings.co.za/OurGroup/Pages/History.aspx

and 2016 (Figure 8). The growth in total assets has been driven by current assets while non-current assets having remained almost constant for the entire period.

Figure 8: Pick n Pay Total Assets, 2010 - 2016



Source: INET BFA McGregor

This marginal growth in non-current assets is reflected in Pick n Pay's capital investments which recorded a compound annual growth rate of only 2% between 2010 and 2015 before increasing to 10% between 2010 and 2016.

Twenty years ago, Pick n Pay's market value exceeded Shoprite's in South Africa. Today, its value is only around a third of Shoprite's. Although turning its profitability around in recent years, Pick n Pay has faced significant growth challenges in South Africa. This has been attributed to its lack of adaptation to the changing South African market and emerging black middle class[20] and general slow pace of retail modernisation and investment, as the relative investment metrics between Shoprite and Pick n Pay clearly reveals.

Admitting these weaknesses, former Pick n Pay CEO, Nick Badminton, highlighted "*Our decision to move to centralised distribution was motivated by changes in South Africa's retail landscape which had seen us fall behind our competitors, who were investing significantly in their supply chains and in improved service to their stores through centralised distribution systems. Throughout the world, the most successful retail groups have unlocked massive value from their supply chains, and most of them have moved away from direct-to-store delivery distribution*".[21] While Pick n Pay more

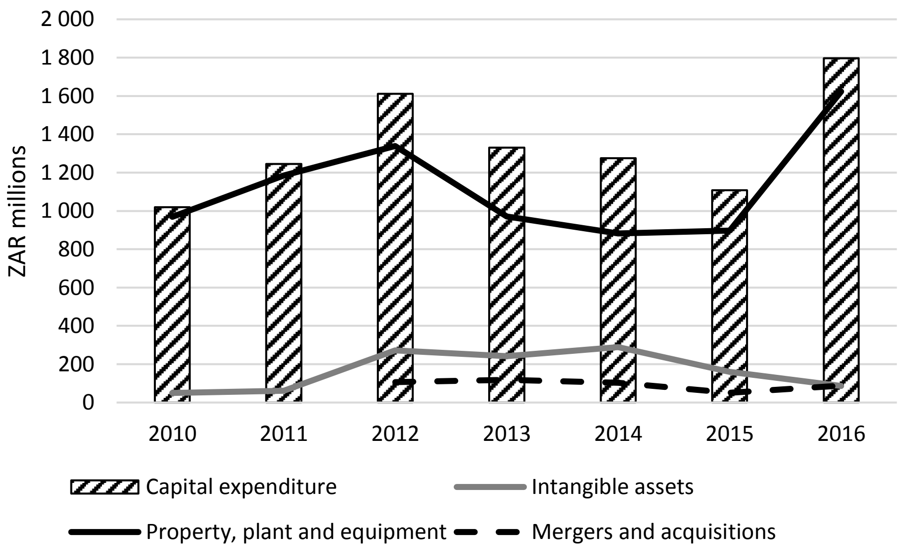
[20] http://www.financialmail.co.za/coverstory/2016/06/03/can-pick-n-pay-regain-its-former-glory, accessed 1 October 2016
[21] http://www.moneyweb.co.za/archive/r628m-distribution-centre-for-pick-n-pay/, accessed 25 August 2015

recently invested over ZAR2 billion in its DCs collectively, these investments were the bare minimum needed to catch up to the rest of the industry, particularly Shoprite.[22]

Poor performance has also been attributed to the group's inability to adapt and respond to changes in the market particularly the emergence of the black middle class. This, and the lack on investments in retail modernisation created a gap between Pick n Pay and Shoprite's performance.[23]

Given this history, the group's capital expenditure in recent years has been focused on growing the group's footprint and improving the overall quality of the supermarket chain. As part of its expansion and restructuring strategy, Pick n Pay has been investing in new stores and distribution infrastructure. As of 2016, the group doubled the number of stores from 794 in 2010 to 1410 stores in 2016 across all formats in nine African countries.[24] The group plans to open further stores to grow the customer base through tapping into new customers in economically disadvantaged communities which exhibit potential. As part of the group's centralised distribution strategy, Pick n Pay invested in its second major distribution centre in Phillipi in Western Cape in 2013.[25] This is over and above significant investments made (R628 million) in its largest DC in Longmeadow in Gauteng in 2010.

Figure 9: Pick n Pay Capital Expenditure, 2010 - 2016



Source: Annual Reports, Cash Flow Statements

[22] According to Shoprite CEO, Whitey Basson, '*Heavy investment in distribution and technology has resulted in huge cost savings. We now have the lowest cost structure in the industry*.' And, '*Through this investment, Shoprite completely out-maneuvered Pick n Pay. The signs were there in 2007 when Shoprite share price started outperforming Pick n Pay at an accelerated pace'* (Benetar, 2015).

[23] http://www.financialmail.co.za/coverstory/2016/06/03/can-pick-n-pay-regain-its-former-glory, accessed 1 October 2016

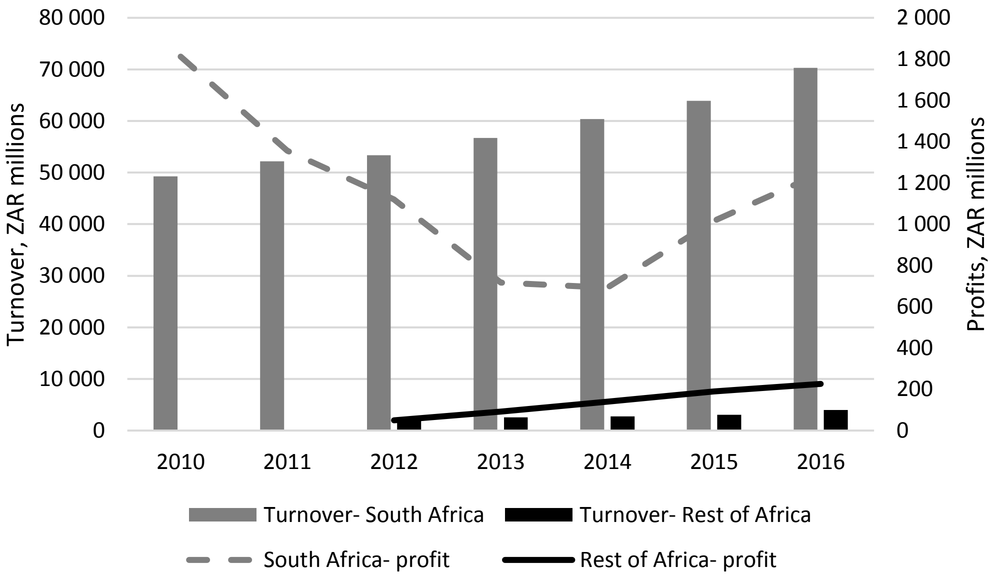
[24] Pick n pay Integrated Annual Report, 2016.

[25] Pick n Pay Annual Reports, 2010-2015

The peak in capital expenditure in 2012 (Figure 9 above), which has subsequently started declining, could be due to several factors including the investments in DCs; the acquisition of the Australian business during the 2011/2012 trading period[26], and the group's restructuring process. Note that the competition authorities in Australia subsequently disallowed the acquisition and Pick n Pay was forced to sell this business. The 2016 spike is likely to be because of the new stores, and re-vamping of existing stores.

As part of its growth strategy, Pick n Pay views the region as the second engine of growth and currently operates in nine African countries. Pick n Pay's regional operations, although off a much smaller base than Shoprite's; recorded a higher sales growth rate of 20% per annum than South African operations (7%) between 2012 and 2016. However, regional operations contribute only 4% to the group's overall sales. Trading profits for the rest of Africa recorded a CAGR of 46% per annum compared to 3% CAGR recorded by South African operations between 2012 and 2016. (Figure 10).

Figure 10: Pick n Pay South Africa and Rest of Africa sales and profits, 2010-2016



Source: Pick n Pay Annual Reports

The group has plans to enter Ghana and Nigeria in 2017. The group's African expansion programme is underpinned by the franchise programme in Botswana, Swaziland and Zimbabwe. However, in 2014 the group closed its franchise operations in Mozambique and Mauritius. As of 2016, the group owns 57 supermarkets in the region and plans to open new stores in Namibia, Zambia, and Zimbabwe. In 2015, the Zambian operations performed exceptionally well while Zimbabwean operations experienced a challenging trading period due to pressures from a deflationary trading environment, increased competition and economic and political instability.

[26] Pick n Pay Annual Reports, 2010-2015

3.2.2 Profitability trends

Table 6 shows a deterioration in Pick n Pay's profitability since 2010 to 2014 before improving in 2015. The depressed financial results are due to an increase in the cost base following the group's long-term transformation strategy which has affected the short-term performance of the business.[27] As noted, in 2010, the group embarked on a restructuring strategy to improve the long-term profitability of the business and regain market share. The restructuring process involved centralisation of the supply chain through investing in distribution infrastructure, centralised category buying, investments in management skills and greater efficiency in the group's operations. Investment in human resources included hiring new senior management from Tescos in UK, to turn around the company. Pick n Pay's structural changes also involved the appointment of experienced non-executive board directors and the closing of 40 unprofitable stores.[28]

Table 6: Pick n Pay Key Profitability Indicators, 2010 – 2016

	2010	2011	2012	2013	2014	2015	2016
Real Turnover	55 405	55 156	55 595	56 781	57 365	58 032	59 207
Gross profit margin (%)	19.58	19.26	19.27	19.65	19.63	20.08	20.27
Net profit margin (%)	2.15	1.51	1.89	0.93	0.92	1.29	1.47
Return on Equity (%)	55.44	36.36	46.32	22.79	21.60	26.42	27.33
Return on Assets (%)	10.62	7.07	9.42	4.23	4.14	5.81	6.42

Source: Osiris, INET BFA and annual reports. Source: Osiris, INET BFA and annual reports. Nominal turnover adjusted to 2012 constant prices using CPI index. Base year=2012

The improvement in profitability in 2016 can be attributed to the fruits of these interventions which resulted in improved operating efficiencies, contained costs, centralisation of the supply chain and investments in customer experience. Centralisation of the supply chain and improvement in procurement activities with suppliers lowered the cost of delivered products both in groceries and perishables.[29] Transition to central category buying benefited customers in terms of better products and better prices while changes to the supply chain resulted in greater product availability, fresher products and less cluttered stores. Throughout 2016, the group achieved greater stability through financial control and working capital management which resulted in consistently stronger cash balances.[30] This allowed the group to repay a significant proportion of their debt which could explain the improvement in the group's return on assets ratio in 2016.

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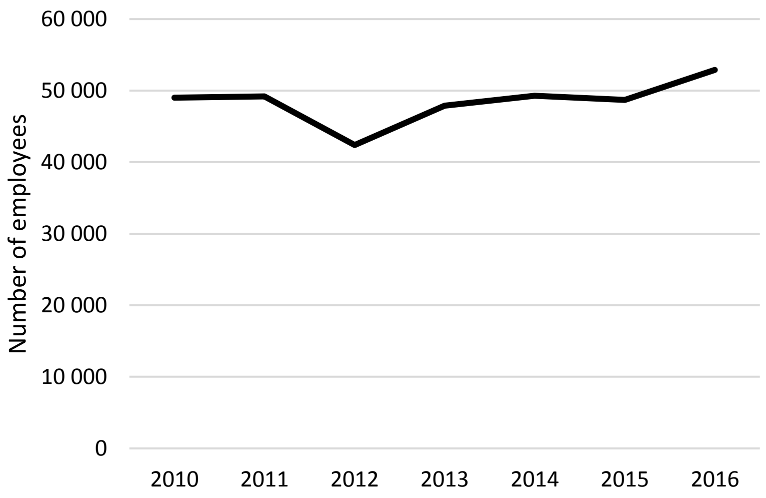
[27] Pick n Pay Integrated Annual Reports (2011, 2013, 2014 and 2015) http://www.picknpay-ir.co.za/annual-reports.php accessed on 21 October 2016
[28] Pick n Pay Annual Reports, 2010-2015
[29] Pick n Pay Annual Reports, 2010-2015
[30] Pick n Pay Annual Reports, 2010-2015

3.2.3 Employment trends

Pick n Pay's employment numbers have remained fairly constant for the 2010-2016 period, although experiencing a dip in 2012 (Figure 11). The group's employment decreased by 0.6% from 49,000 in 2010 to 48,700 in 2015. The dip in employment in 2012 could be due to the forced re-sale of the Australian business during the same year. A further decline in employment between 2014 and 2015 could be due to the closing down of franchise operations in Mozambique and Mauritius in 2014. There are also concerns that Pick n Pay might experience a further decline in employment following the introduction of self-service machines meant to save on costs and improve customer experience.[31] However, in 2016 Pick n Pay in fact created 4,500 new jobs following their store opening strategy of 175 stores.

Figure 11: Pick n Pay Trends in Employment, 2010 - 2016



3.3 SPAR Group

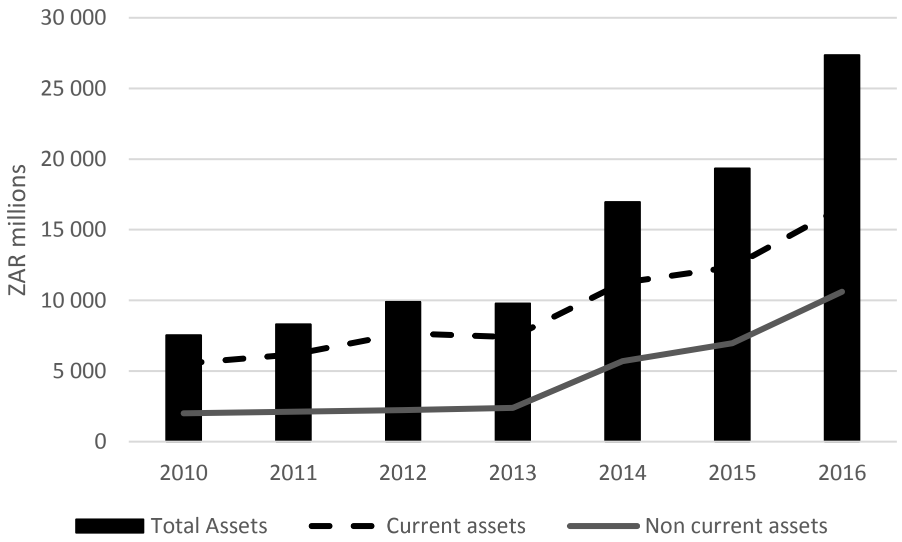
The SPAR Group, the third largest mass grocery retailer specialising in foodstuffs and general merchandise in South Africa, operates in nineteen African countries through a franchise model. The four SPAR Brands are SuperSPAR, SPAR, KwikSPAR, and SaveMor, catering for the full spectrum of income groups. SaveMor is exclusively focused on rural and township markets. It gives the option to existing small-store owners to convert their store into a SaveMor store. SPAR also opened forecourt convenience stores in 2013, SPAR Express, in collaboration with oil company Shell. The SPAR Group listed on the Johannesburg Stock Exchange on 1 July 2004.

[31] http://www.fastmoving.co.za/news/retailer-news-16/pick-n-pay-s-self-service-raises-job-loss-fears-9142, accessed on 21 October 2016.

3.3.1 Investment trends

Although off a smaller base than other retailers, Figure 12 shows limited investments in total assets recording a compound annual growth rate of only 9% per annum between 2010 and 2013. However, in 2014 total assets suddenly increased by 73% following SPAR's acquisition of the BWG Group which owns the SPAR brand in Ireland and the South West of England. The decision to acquire BWG Group was a strategy to find new markets given the challenges of operating in a highly competitive retail environment in South Africa. In 2016, the group further acquired 60% stake in SPAR Switzerland to create scale and expand the geographical operations of the business.

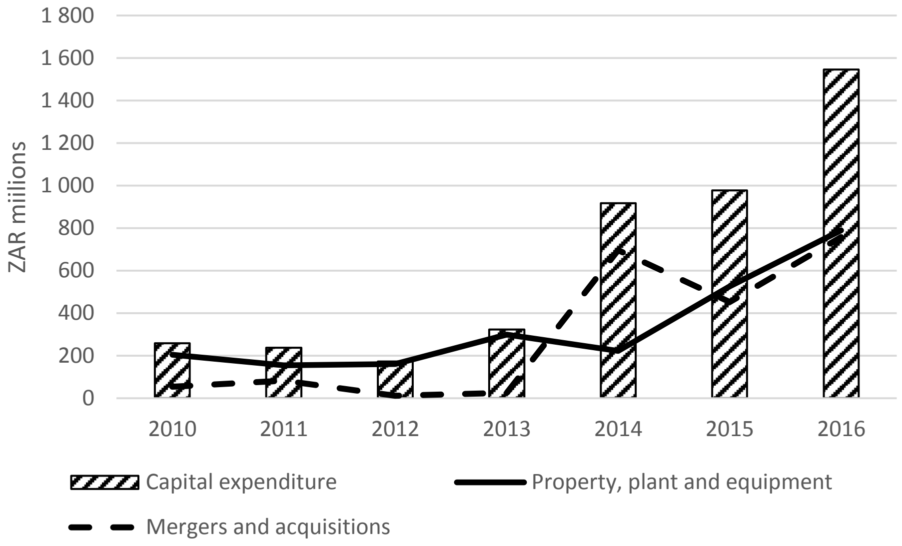
Figure 12: SPAR Total Assets, 2010 - 2016



Source: Osiris and Annual Report data

Figure 13 shows that SPAR maintains very low levels of capital expenditure limited to upgrading distribution centres, new store openings and renovating existing stores. However, the acquisition of BWG Group significantly changed the group's capital expenditure to record a compound annual growth rate of 31% per annum between 2010 and 2015 compared to 8% prior the acquisition. The further increase in capital expenditures in 2016 is due to the 60% acquisition of SPAR Switzerland.

Figure 13: SPAR Capital Expenditure, 2010 - 2016



Source: Osiris and Annual Report data

3.3.2 Profitability trends

Growth in real turnover has been quite low between 2010 and 2013 recording a compound annual growth rate of 5% per annum and is largely driven by the liquor and building material business (Table 7). However, increase in the group's turnover from 49.6 billion in 2014 to 73.7 billion in 2015 is likely to be mainly due to the BWG operations. The acquisition of BWG Group improved the group's turnover to record a compound annual growth rate of 13% per annum between 2010 and 2015.

Table 7: SPAR Key Profitability Trends, 2010 – 2016

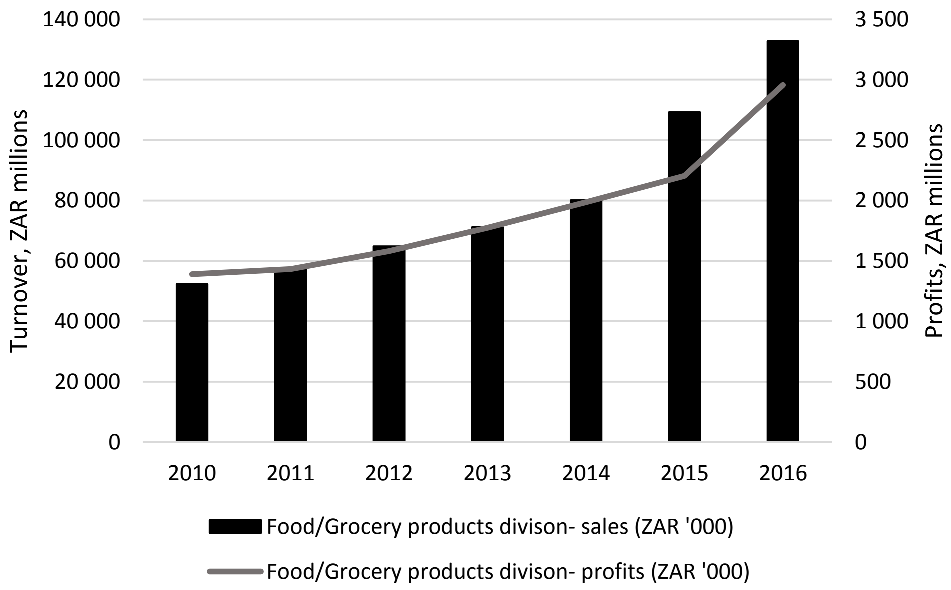
	2010	**2011**	**2012**	**2013**	**2014**	**2015**	**2016**
Real Turnover (R million)	39 550	41 036	43 560	45 390	49 599	72 659	74377
Gross profit margin (%)	9.06	9.29	9.10	8.85	9.45	9.68	10.78
Net profit margin (%)	2.63	2.48	2.45	2.51	2.47	1.94	2.00
Return on Equity (%)	41.87	38.26	37.32	37.39	44.44	42.69	32.16
Return on Assets (%)	12.16	11.47	10.70	12.13	7.86	7.35	6.63

Source: Osiris, INET BFA and annual reports. Nominal turnover adjusted to 2012 constant prices using CPI index. Base year=2012

On average, all the profit indicators have improved over the entire period with the exception of net profit margin which deteriorated particularly in 2015 but shows signs of improvement in 2016. The deterioration in net profit margin could be due to rising costs following store acquisitions, bad debt losses and high diesel prices raising delivery costs. This led the group to introduce a system to monitor fuel utilisation by vehicle at all distribution centres in 2011. SPAR continues to maintain low levels of capital expenditure to improve cash generation and profitability. In addition, according to SPAR, the competitive retail environment driven by increased advertising exposure and aggressive pricing by all the major retailers put SPAR's margins under pressure. This forced SPAR to embark on aggressive advertising and promotions in order to stay competitive in the retail environment.

SPAR's food/grocery sales and profits have also shown significant growth as seen in Figure 14. Sales grew by a CAGR of 17%, while profits grew by 13%. This suggests that there are other, loss making businesses in the SPAR Group aside from food/grocery which have contributed to the declining profit figures in Table 7 above.

Figure 14: SPAR Grocery sales and profits, 2010 - 2016

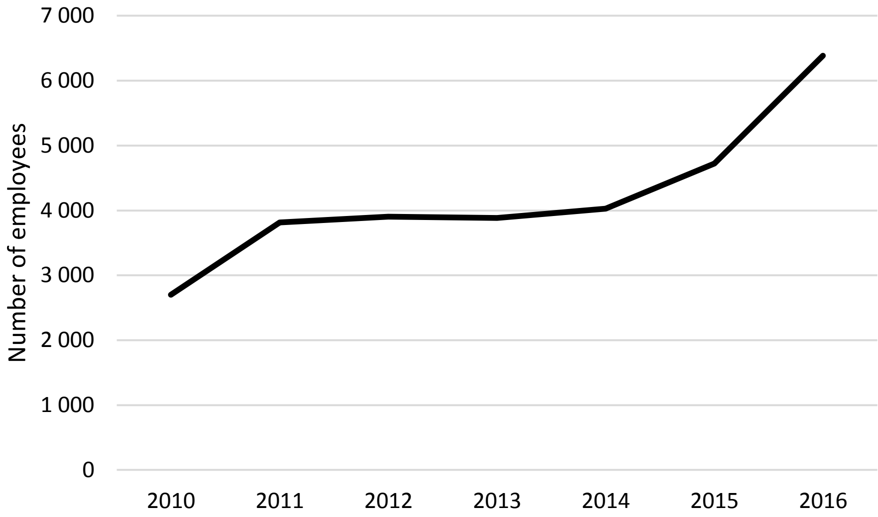


Source: Osiris, SPAR Annual Reports

3.3.3 Employment trends

SPAR's employment numbers have remained stagnant between 2011 and 2013 before rising in 2014 (Figure 15). The increase in employment could be due to the BWG Group acquisition and not necessarily organic creation of employment. However, employment numbers in the figure below appear to be only corporate numbers and not employment of all the individually owned franchises. The further increase in 2016 might be due to the acquisition of Spar Switzerland business in April 2016.

Figure 15: SPAR Trends in Employment, 2010 - 2016



Source: Osiris

3.4 Woolworths Holdings

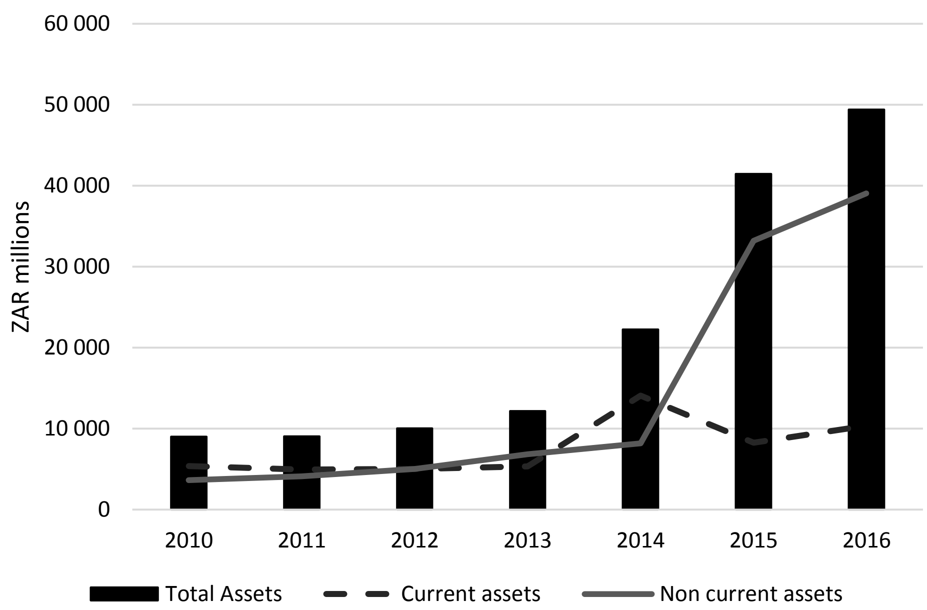
Woolworths Holdings, the fourth largest retail chain in South Africa in terms of store numbers specialises in food and clothing, targeting high income consumers. Woolworths has 1400 store locations in a number of African countries (clothing and supermarkets).[32] The group only has a single brand and format store for its supermarket offering, which emphasizes providing superior quality and product innovation and exclusively targets the high-end, affluent market. Woolworths in South Africa, like Pick n Pay and SPAR, has ventured into convenience stores (Woolworths Foodstop) at Engen fuel forecourts. Woolworths has been listed on the Johannesburg Stock Exchange since 1997.

3.4.1 Investment trends

Like Pick n Pay, Woolworths was not aggressive in investing in total assets until 2013. Assets increased by more than 240% over a period of two years from ZAR12 billion in 2013 to ZAR49 billion in 2016 (Figure 16). This was bolstered by the acquisition of David Jones Limited, the listed Australian department store chain for ZAR21.4 billion in 2014 and buying back of franchise operations in South Africa and the region.[33]

[32] Woolworths Holdings Integrated Annual Report, 2016
[33] Woolworths Holdings Annual Financial Statements, 2015. http://www.woolworthsholdings.co.za/investor/annual_reports/ar2015/whl_2015_afs1.pdf, accessed on 20/10/2015

Figure 16: Woolworths Total Assets, 2010 - 2016



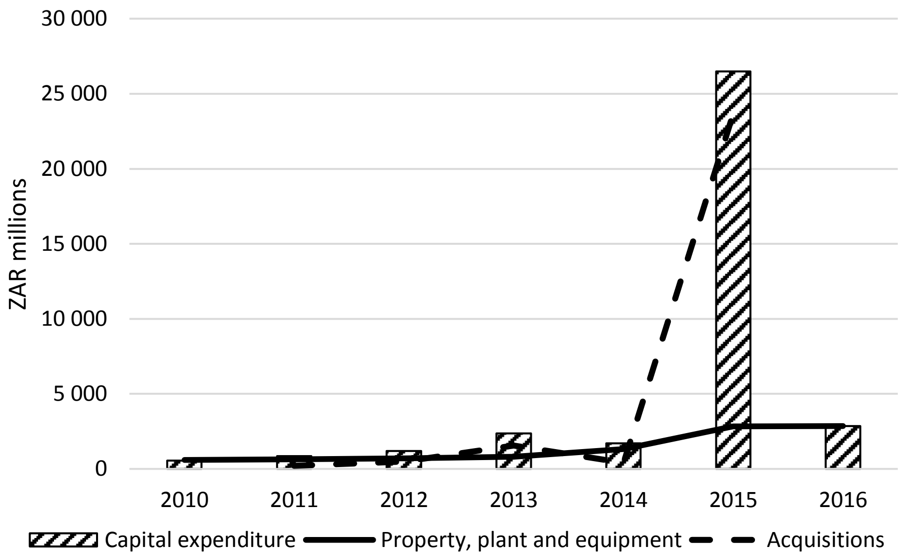
Source: INETBFA McGregor

The low levels of capital expenditure in Figure 17 confirm Woolworths' limited investment in total assets between 2010 and 2013. Between 2010 and 2014, the group's capital expenditures grew by 32% although off a very small base. However, the acquisition of David Jones changed the group's capital expenditures to record a compound growth rate of 116% per annum between 2010 and 2015 before falling back to 32% CAGR between 2010 and 2016.

The low levels of investments could be explained by the group's strategy in earlier years. Since 2010 the group's strategy has been to open fewer but larger stores and extend existing stores.[34] This strategy is quite different from Pick n Pay and Shoprite's strategy of opening smaller format stores in economically disadvantaged communities. The difference in strategies is due to Woolworths' overall focus on the upper income customer group rather than the mass, low income groups.

[34] Woolworths Annual Reports, 2010-2015

Figure 17: Woolworths Capital expenditure, 2010 - 2016



Source: Annual Financial Statements, 2010-2016

The small rise in capital expenditures beginning in 2011 can be also partially attributed to the group's decision to exit the franchise model in South Africa and the region towards a corporate model.[35] As part of this, the group bought back 54 franchise Woolworths stores at a cost of ZAR634 million in 2011 and a further 59 franchise stores in 2012. By 2014 the group had completed buying back 42 franchise businesses in Botswana, Namibia, Ghana, Swaziland and South Africa making Woolworths the full owner of all previous franchises in South Africa and Africa.

In 2013, the group's strategy further appears to have changed from opening a few large stores to opening more stores to increase scale and footprint, covering more geographical areas and offering broader ranges to customers. Building and spreading footprint was part of a strategy to achieve the scale required by the group to defend its current position, gain market share and spread risk. Woolworths also invested in sourcing and synergy improvements and information technology platforms to ensure efficiencies in the supply chain and enhance the group's ability to provide credible offerings to growing operations.

As previously noted, the peak in capital expenditure in 2015 is due to the acquisition of the Australian department store chain David Jones in August 2014. This, in addition to the buying back of franchises, transformed the group to gain significant scale across sub-Saharan Africa and Australasia.[36] Woolworths acquired David Jones to leverage design and procurement capabilities. In addition, the group benefits from scale and

[35] Woolworths Annual Reports, 2010-2015
[36] Woolworths Annual Reports, 2010-2015

efficiencies allowing it to compete with major northern hemisphere retailers entering the markets including the growth of online retailing.[37]

Furthermore, in 2015 the group invested in extensive refurbishments and new stores whilst converting franchise stores to corporate stores. As of 2016, the group has 1400 stores and trades on two continents. The three main groups in Woolworths Holdings are Woolworths South Africa, David Jones and Country Road Group in Australia.

Consistent with Shoprite and Pick n Pay, Woolworths recorded faster growth in Africa than South Africa particularly in Mauritius, Kenya and Zambia. Woolworths primarily operates in South Africa, sub-Saharan Africa and Australia. It closed operations in Nigeria. The decision to close Nigerian operations was driven by the idea that it is a northern hemisphere business with challenges in the supply chain and therefore compromising the group's ability to provide credible and quality offerings to customers.[38] This informs the group's strategy to build scale across the southern hemisphere despite the region contributing a small proportion to the group's overall profits (relative to South Africa). In 2013, the group opened seven new stores in Lesotho, Zambia, Mauritius, Nigeria and Kenya. By 2015, the group had 24 stores in 11 African countries excluding South Africa.

3.4.2 Profitability trends

Woolworths' real turnover grew faster than both Shoprite and Pick n Pay achieving a compound annual growth rate of 13% between 2010 and 2016.[39] Gross profit margin showed year-to-year improvement over the entire period. However, return on equity and assets started deteriorating after 2012 while the net profit margin dipped in 2015 before rising again in 2016 (Table 8).

Table 8: Woolworths Key Profitability Trends, 2010 - 2016

	2010	2011	2012	2013	2014	2015	2016
Real Turnover (millions)	26 421	27 177	28 691	33 572	35 917	49 660	53976
Gross profit margin (%)	33.66	37.23	37.91	38.69	39.22	42.44	45.04
Net profit margin (%)	5.38	6.38	7.16	7.37	7.27	5.51	6.68
Return on Equity (%)	37.04	40.69	45.87	43.74	39.70	21.79	21.88
Return on Assets (%)	13.96	17.99	20.39	21.28	12.39	7.52	8.8

Source: Osiris, INETBFA McGregor. Nominal turnover adjusted to 2012 constant prices using CPI index. Base year=2012

The high profit margins from 2010 to 2014 are attributed to improved sourcing strategy, lower markdowns and good cost control.[40] The group adopted direct sourcing strategies characterised by speed to market and shorter lead times as opposed to

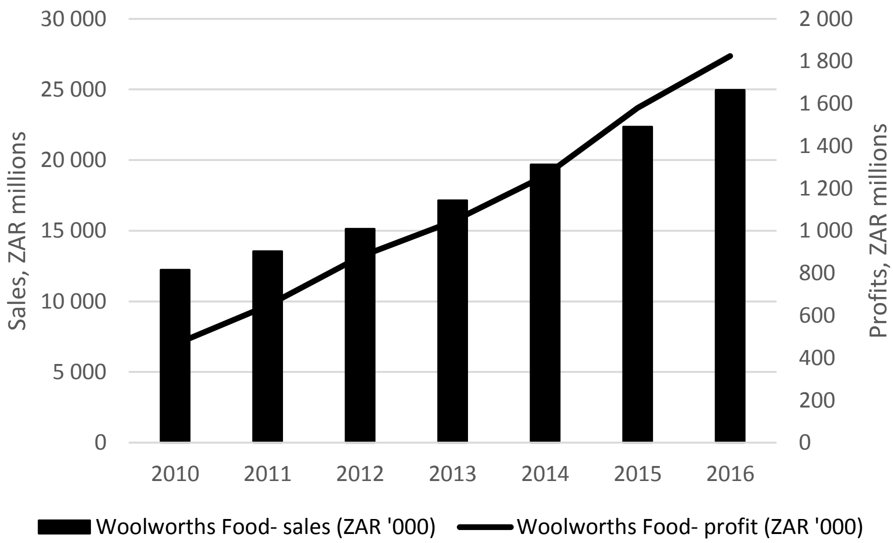
[37] Woolworths Annual Reports, 2010-2015
[38] Woolworths Annual Reports, 2010-2015
[39] Inflation adjusted turnover by the CPI, base year 2012
[40] Woolworths Annual Reports, 2010-2015

using of agents and third parties. In addition, the acquisition of David Jones stores in 2015 increased sales and profit. Growth has been particularly driven by strong performances from non-foods and groceries. In the groceries section, Woolworths Food continues to differentiate on quality, freshness and innovation. In addition, the buy-back of franchises in 2012 improved the group's profitability. Woolworths' strategy to remain profitable appears to be hinged on making existing customers spend more at their stores as opposed to targeting new customers. The group plans to do this through expanding their offering and increasing the size of stores.

However, the group's investments in extensive refurbishments, new stores and purchase of franchise stores in 2015 increased costs putting pressure on the net profit margin. The acquisition of David Jones could have depressed the return on equity and assets in 2015 given the increase in the company's total asset base which has the effect of reducing the above ratios. However, these ratios show signs of improvement in 2016.

Woolworths' food sales and profits grew by a CAGR of 13% and 26% per annum respectively between 2010 and 2016 (Figure 18). This strong performance corroborates the above results and shows that the food division significantly contributes to the group's overall profitability.

Figure 18: Woolworths Food Sales and Profits, 2010 - 2016

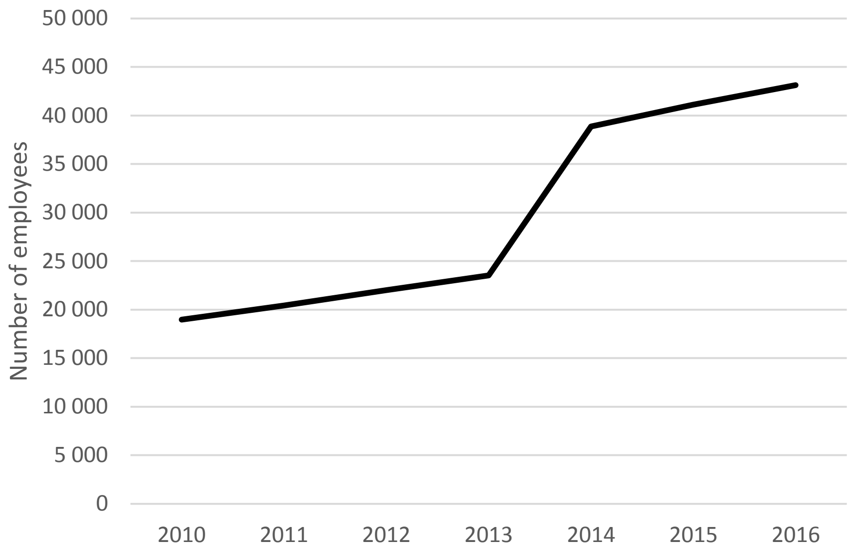


Source: Woolworths Annual Reports

3.4.3 Employment trends

Woolworths' employment figures grew by a compound annual growth rate of 15% between 2010 and 2016 (Figure 19). The group created 26,000 direct jobs in 2013 of which 23,000 jobs are in South Africa. The acquisition of David Jones in August 2014 added a further 7,200 jobs bringing total employment to 38,000 jobs throughout the southern hemisphere. In 2015, Woolworths created an additional 2,700 jobs increasing employment to 41,000 employees. Overall, currently Woolworths contributes to 43,000 jobs across 14 countries.

Figure 19: Woolworths Trends in Employment, 2010 - 2016



Source: Osiris

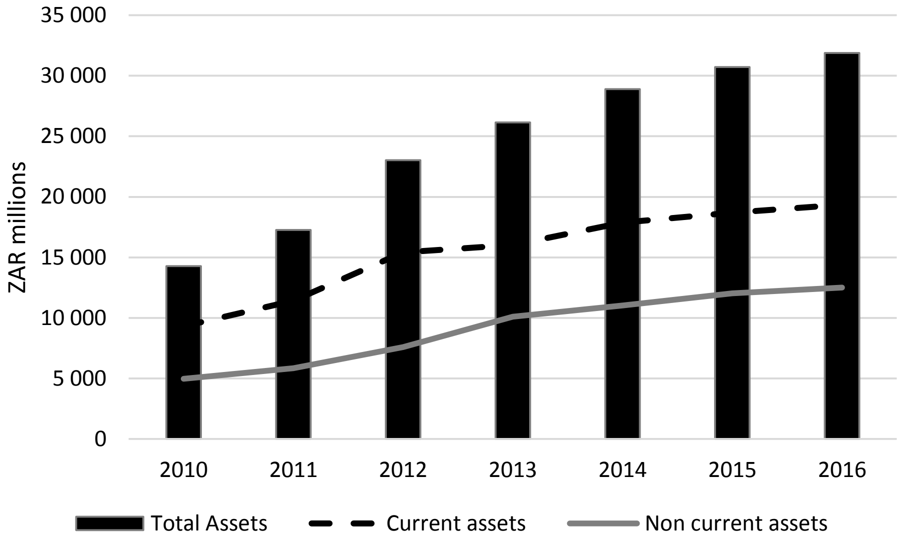
3.5 Massmart Holdings/Walmart

More recently, Walmart-owned Game has branched into food products becoming a retailer of non-perishable groceries and wholesaler of basic foods. This is the typical Walmart format in other countries. Game has the advantage of Walmart's immense global supplier base, allowing it to benefit from lower unit costs. It has however yet to gain traction in southern Africa. Massmart Holdings was listed on the JSE in 2000.

3.5.1 Investment trends

Massmart has maintained a steady growth in total assets recording a compound annual growth rate of 14% per annum between 2010 and 2016 (Figures 20).

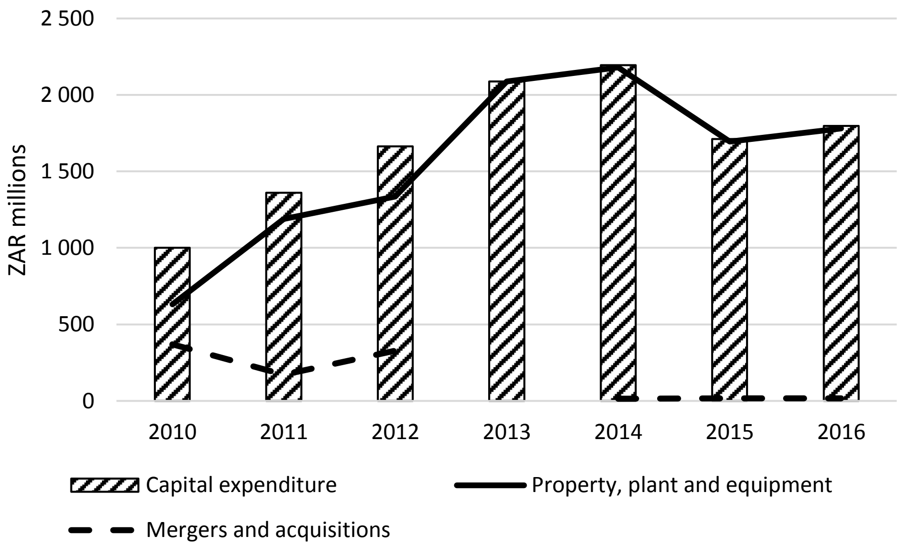
Figure 20: Massmart Total Assets, 2010-2016



Source: Osiris and Annual Report data

Figure 21 shows a steep increase in Massmart's capital expenditure between 2011 and 2013. After Walmart acquired Massmart in 2011, the group engaged in significant investments in new stores, acquisition of stores, distribution centres and capacity to expand its footprint in South Africa and the rest of Africa. However, capital expenditures started declining after 2014 signaling saturation of the expansion strategy.

Figure 21: Massmart Capital Expenditure, 2010 - 2016



Source: Annual Financial Statements, 2010-2015

3.5.2 Profitability trends

Table 9 shows year-to-year improvement in real turnover and gross profit margins between 2010 and 2016. On average, real turnover grew by 5% per annum during the six-year period. However, the high sales growth did not translate into high net profit margins which have deteriorated over the same period. Significant investments in IT systems, new stores and distribution centres between 2011 and 2013 increased expenses leading to depressed net profit margins. In addition, closing of poor performing stores between 2011 and 2012 resulted in once-off costs and inefficiencies. Overall cost pressures remain a major challenge affecting the group's profitability.

Table 9: Massmart Key Profitability Trends, 2010 – 2016

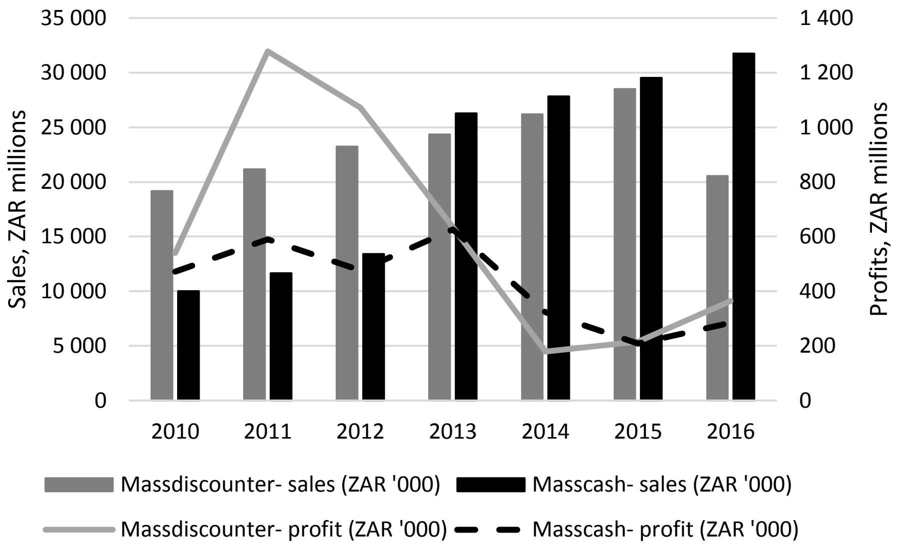
	2010	2011	2012	2013	2014	2015	2016
Real Turnover (R millions)	53 488	56 120	61 363	68 788	70 599	72 659	73 589
Gross profit margin (%)	18.24	18.47	18.61	18.65	18.75	18.99	18.96
Net profit margin (%)	2.38	1.58	1.92	1.78	1.38	1.31	1.45
Return on Equity (%)	33.90	22.12	27.07	24.99	19.54	19.22	22.00
Return on Assets (%)	8.23	5.08	6.15	5.13	3.74	3.62	4.15

Source: Osiris, INET BFA and annual reports, Nominal turnover adjusted to 2012 constant prices using CPI index. Base year=2012

High capital expenditures on new stores and distribution centres increased the net asset value which has led to a decrease in Return-on-Equity from 2011 to 2015 before improving in 2016. Similarly, significant investments in capital assets caused the Return-on-Assets to remain at lower levels.

Masscash and Massdiscounters (covering the group's retail and wholesale operations) show a steep decline in profits after 2013, although sales have grown (Figure 22). Declining profitability in the Massdiscounters division is largely attributed to operational challenges, currency devaluation and the impact of new stores opened in Nigeria between 2013 and 2014. This is estimated to have reduced profit by approximately R40 million. In addition, aggressive competition in the low-income segments has led to investments in new stores, IT systems and brand building with the effect of increasing the cost base. Low sales growth coupled with increasing costs in the Masscash division caused a decline in profits.

Figure 22: Masscash and Massdiscounters Sales and Profits, 2010 - 2016

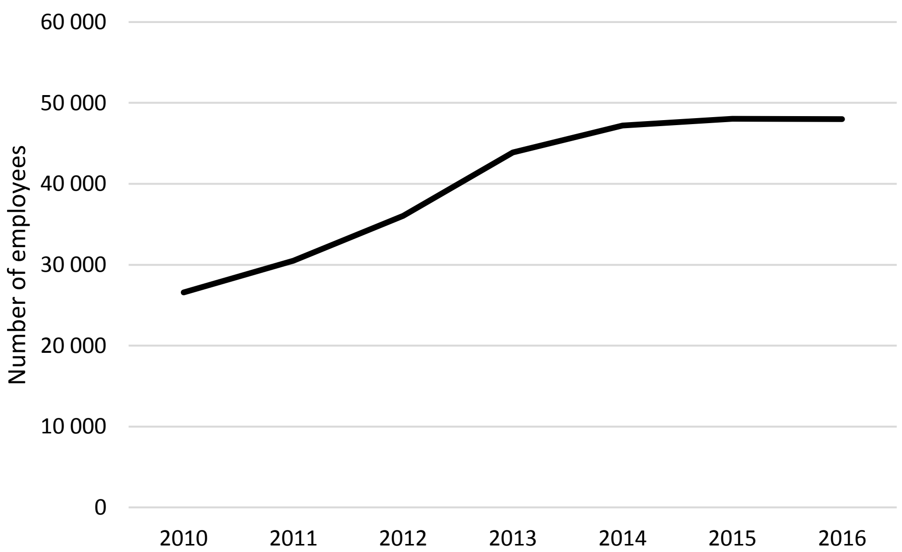


Source: Osiris, Massmart Annual Reports

3.5.3 Employment trends

Massmart's employment steadily improved from 2010 to 2013 before levelling off in 2014 and 2016 (Figure 23). This steady increase could be due to the group's expansion plans after the Walmart takeover increasing the need to invest in extended capacity to service these operations.

Figure 23: Massmart Employment Trends, 2010 - 2016



Source: Massmart Annual Reports

3.6. Choppies Enterprises

While the past trend has been that South African supermarkets have aggressively spread in the region, this is now changing with supermarkets from other SADC countries entering the southern African region. The most successful example of such entry is by Choppies Enterprises.

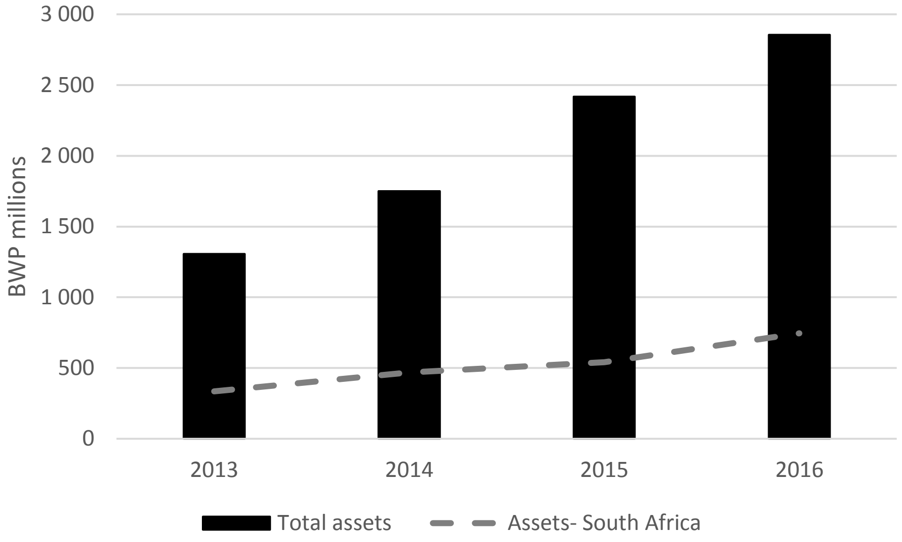
A grocery and general merchandise retailer from Botswana, Choppies has over the last 15 years grown from two stores in Botswana to over 125 stores in Botswana, Zimbabwe, and South Africa. Recently, it has also entered Zambia and Kenya. Choppies' target market is low-to middle-income consumers, but it is attempting to attract middle-to-upper income consumers. It stocks branded international products as well as a wide range of its own private label products. It is also vertically integrated with its own suppliers for certain products such as poultry, sugar and bottled water. Choppies also stocks fresh fruit and vegetables and has a butchery, bakery and takeaway.

Its location in South Africa is mainly in the semi-urban and rural areas in mining towns, locating near transport nodes such as taxi ranks. Formats include compact Superstores, with only a few Hyperstores and small value stores. Choppies has been listed on the Botswana Stock Exchange since 2012 and the Johannesburg Stock Exchange in May 2015, making it the only other supermarket chain other than Shoprite to have more than one listing in Africa.

3.6.1 Investment trends

Choppies is aggressively investing in total assets which recorded a compound annual growth rate of 30% per annum between 2013 and 2016 (Figure 24). On average, South African investments constitute 25% of the total corporate assets.

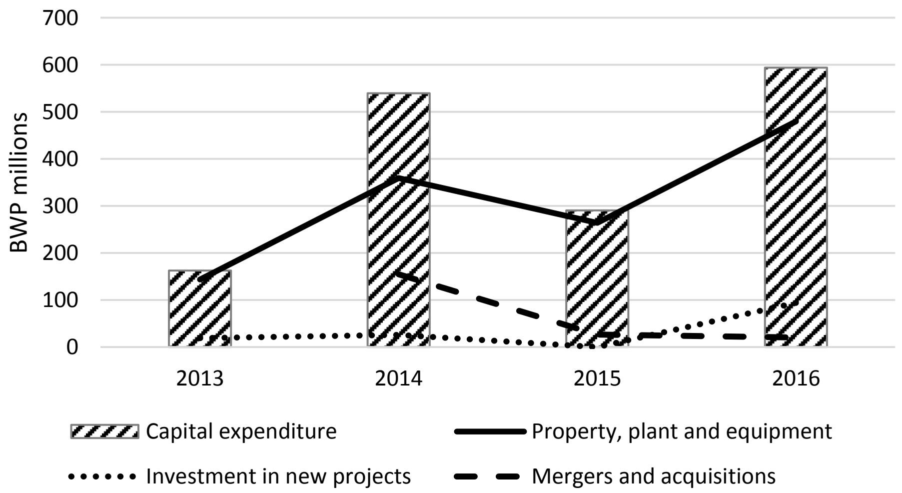
Figure 24: Choppies Total Assets, 2013-2016



Source: Annual Reports, Osiris

Choppies follows an organic and acquisitive growth strategy which is captured by the high levels of capital expenditure in property, plant and equipment and mergers and acquisitions (Figure 25). Since entry in 2013, Choppies has invested in 64 stores in South Africa. In 2015, the group invested in two distribution centres in Rustenburg. In 2016, Choppies acquired 21 Jwayelani stores in Kwazulu Natal and Eastern Cape and invested in a third distribution centre based in Durban. During 2016, capital expenditure was directed to infrastructural developments through strategically located distribution centres and related increases in the vehicle fleet.

Figure 25: Choppies Capital Expenditure, 2013-2016

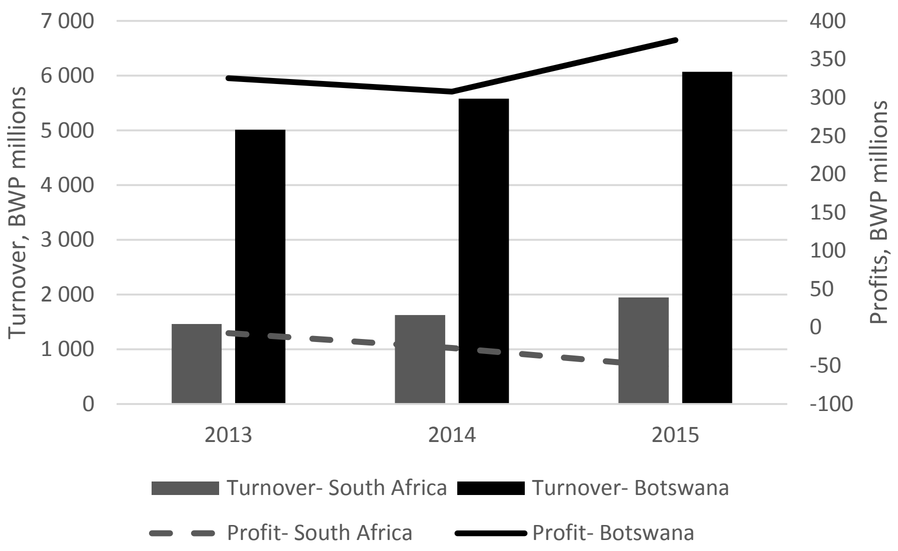


Source: Annual Reports

3.6.2 Profitability trends

South African operations contribute 29% to the group's overall turnover. However, South African operations are not yet profitable incurring substantial losses since 2013 (Figure 26). During this period, the retailer suffered from low sales and reduced footfall. This is mainly as a result of Choppies' strategy to concentrate on mining towns which were adversely affected by drop in commodity prices and electricity shortages between 2013 and 2015. The acquisition of 21 Jwayelani stores in Kwazulu Natal and Eastern Cape in 2016 is expected to contribute positively towards the profitability of South African operations. Investments in centralised distribution centres and improved trading terms from suppliers are also expected to increase efficiency and profitability. Choppies is moving from concentrating on mining areas to expanding into new provinces in order to lessen exposure to mining areas.

Figure 26: Choppies Botswana and South Africa sales and profits, 2013-2016

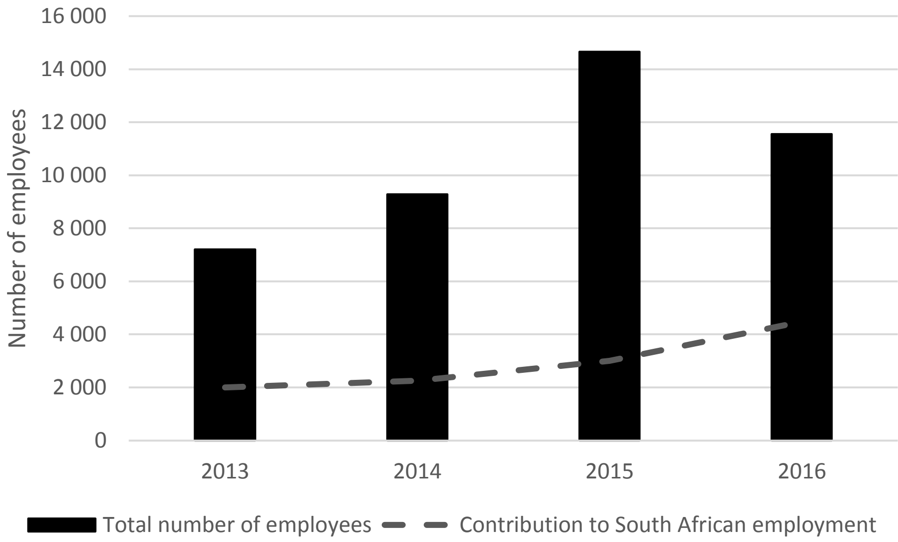


Source: Osiris

3.6.3 Employment trends

Off a low base, Choppies contribution to South African employment increased by 124% from 2,000 employees in 2013 to 4,479 employees in 2016. However, the increase in employment between 2015 and 2016 might be due to the acquisition of 21 operating Jwayelani stores in Kwazulu Natal and Eastern Cape and not necessarily organic growth in employment.

Figure 27: Choppies Employment Trends, 2013-2016



Source: Annual Reports

3.7. Fruit and Veg City Holdings

The fifth largest grocery retailer in terms of store numbers in South Africa is Fruit and Veg City Holdings (FVC). It expanded rapidly since its first store opening in 1993 and by 2007 had around 80 stores nationally. There are now over 100 FVC stores throughout southern Africa. Like the other supermarkets, it has evolved to targeting customers across different income groups, including through its more up-market Food Lover's Market format in affluent suburbs. While also in the grocery retail space, unlike the other major supermarkets, FVC's model is predominantly the sale of fresh fruit and vegetables, with a smaller proportion of other grocery item lines. FVC has also expanded into franchised convenience stores (Fresh Stop stores) through a joint venture with fuel retail company Caltex. FVC further introduced an in-house fast food brand and has diversified into the liquor market. It also has a profitable import and export joint venture primarily of fresh fruit (FVC International).

FVC is not listed on any stock exchange in Africa. In 2007, Pick n Pay sought to merge with FVC. The Competition Commission of South Africa recommended that the Competition Tribunal prohibit the large merger between the two on grounds that it would result in the removal of an effective competitor in the retail market for fresh food. The Commission found that FVC was a growing effective competitor to Pick n Pay and would provide an even greater product offering in the future. FVC showed impressive growth particularly between 2006 and 2012. Turnover more than tripled from R1.6

billion in 2006 to R15 billion in 2015, with a growth rate well ahead of the major listed food retailers.[41] We however do not assess FVC further given that it is not listed.

4. Supermarkets as lead firms that shape supply chains and impact supplier development

4.1. Impact on suppliers

As noted in the introduction, the procurement methods and requirements of supermarkets have important implications on suppliers. Internationally, supermarkets have moved away from spot purchases to adopting specialised procurement agents, dedicated wholesalers, or procuring directly from farmers and processors. This gives them direct influence over pricing, quantities, terms of delivery and product quality. This also has the adverse effect of shrinking the supply base by using only preferred suppliers (see Altenburg et al, 2016) and bypassing traditional wholesale markets (Humphrey, 2007).

Sophisticated centralised distribution centres (DCs) are a key pathway to modern retailing. Globally, large supermarkets chains have shifted from traditional store-by-store or direct store delivery procurement and supply practices, towards using own centralised distribution centres to supply stores in the chain (Reardon and Gulati, 2008). While DCs benefit suppliers by reducing queuing times at multiple stores, allowing more efficient use of transport due to full truck loads, facilitating lower administration costs through single invoicing and allowing less handling of products in the process, they can also limit the possibility of small local suppliers negotiating deals individually with stores.

Large supermarkets are further imposing escalating private quality and processing standards on suppliers (Humphrey, 2005; Boselie, Henson and Weatherspoon, 2003). These standards are over and above country-specific basic legal standards that suppliers have to adhere to. The cost of adhering to private standards and audits is borne by the supplier making it increasingly costly to supply formal supermarket chains. The capabilities of local suppliers (particularly small-scale farmers, small food processors and small producers of household consumable goods) to meet these standards and reach the required scale to compete with imports are important for their sustainability. Marketing of fresh food produce to supermarkets has been particularly difficult for suppliers in developing countries as often the institutional, physical and financial infrastructure support systems are weak (including bar coding, packing houses, cold chains, shipping equipment, credit facilities, standards and certification

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[41] Growth rates of the major listed supermarket chains were reported at about 15% per year between 2006 and 2012, while that of FVC was 20% per year. http://www.financialmail.co.za/business/2012/07/18/fruit-veg-city-grows-market-share, accessed 15/01/2015.

processes etc.). For fresh fruits and vegetables, Sanitary and Phytosanitary (SPS) protocols are also important (Tschirley, 2010). Suppliers are usually responsible for all activities up until the product is delivered to a distribution centre or a supermarket and are solely responsible for the costs of escalating private standards of supermarkets.

Over and above basic legal standards, such as food safety and packaging requirements, in South Africa supermarkets generally require that suppliers meet the minimum Hazard Analysis and Critical Control Points (HACCP) accreditation standards upon which they receive a certificate. In some cases, South African supermarkets impose even higher accreditation standards than HACCP, such as Food Safety System Certification (FSSC 22000) which is an international accreditation. However, in other cases, suppliers are taking it upon themselves to get higher accreditations in order to have a competitive edge over their rivals. Regardless of accreditation, it appears that retailers in South Africa typically send auditors to audit the supplier at the suppliers' cost. Estimates from suppliers are that HACCP can cost as much as R80,000 and FSSC 22000 can cost up to R200,000 per annum, with additional R100,000 annual fees for maintenance. In particular, Woolworths has high private standards and performs regular audits on its suppliers. Woolworths' suppliers are required to farm sustainably under the supermarket's 'Farming for the Future' initiative in addition to other sustainability requirements. In addition to the above, supermarkets require Halaal and Kosher certifications. In the poultry industry, producers are Halaal approved, and abattoirs need to be approved by government.

In addition to private standards, suppliers need to comply with global initiatives in order to access international supermarket shelves. For example, GlobalG.A.P (Good Agricultural Practice), which started as an initiative by British retailers and supermarkets to harmonize local standards and procedures and develop an independent certification system, has grown into a worldwide initiative, with over 100 countries participating in the programme. GlobalG.A.P consists of a set of harmonised standards for fresh fruit and vegetables. It includes food safety, quality, labour and environmental standards (Altenburg et al, 2016). Southern African countries have come up with a stepping stone initiative called 'localg.a.p', a more cost effective solution for suppliers through providing an entry level to GlobalG.A.P certification. Although GlobalG.A.P is regarded as a voluntary certification, it is nonetheless required to access European supermarkets and this comes at a considerable cost to suppliers.

The modernisation of supermarkets and rising standards has therefore placed considerable pressure on suppliers with regards to escalating costs, volumes, consistency and quality of products (Dakora, 2012). Local suppliers often require significant investment in capital, technological, managerial, organisational, and financial upgrades to meet these requirements.

Over and above demanding lower costs and higher standards from suppliers, supermarkets often impose a range of other costs on suppliers through their trading terms. Large supermarket chains in many cases are able to control pricing in their trading terms by controlling elements such as listing fees, rebates, advertising and slotting allowances, promotion fees, payment period terms, settlement discounts and new store openings fees (Reardon and Gulati, 2008). This unilateral control of trading terms is reflective of the buyer power of large supermarkets (OECD, 2015; Clarke et al., 2002). A combination of increasing retail concentration and significant barriers to entry limits the choices that suppliers have in terms of the competing means of distributing their goods in many countries (Dobson, 2015).

Suppliers are required to pay support or listing fees in order to be listed on the supplier database and gain access to supermarket shelves. Slotting fees are generally fixed and independent of the volume of goods sold and hence may not be reflective of costs.[42] Although listing and slotting fees act as a screening device for retailers to stock quality products with low risks of failure on the market, they create additional costs and pass on the risk of stocking new products to suppliers.[43] Listing fees are typically a once off payment which can range from ZAR5,000 - ZAR50,000, but can also be charged as a percentage (estimates provided range from 12-15%) off the product price. Listing fees for till positons (for instance, for sweets and lollipops) can be as high as ZAR 250,000 to ZAR 300,000 for a limited time period.

Access to good shelf space (including in gondola ends during promotions) is also critical for suppliers to successfully sell their products. It is a constant challenge for new entrants to access prime shelf space which is usually taken up by dominant suppliers. The experiences of a new entrant instant coffee producer highlight the challenges associated with securing prime shelf space. Poor visibility on the shelf for the new entrant's product resulted in a drop in sales by 30%. Prior to its position being moved to a less attractive position on the shelf, it had taken 6-7% market share from dominant instant coffee producer, Nescafe Gold. Similarly, access to cooler/refrigeration space is important for suppliers of cold products (such as soft drinks, ice creams, frozen products etc.). There have been numerous competition cases globally that have explicitly recognised the harm to competition of dominant suppliers imposing exclusivity on cooler space.[44] South Africa is no exception. Recently

[42] PricewaterhouseCoopers PwC (2012). Issues and solutions for the retail and consumer goods industries.
[43] Consumers International (2012). The relationship between supermarkets and suppliers: What are the implications for consumers?
[44] Competition Commission of Singapore (2013). 'Coca-Cola Singapore Beverages Changes Business Practices in Local Soft Drinks Market Following Enquiry by CCS'. Media Release, 10 January. Available at: https://www.ccs.gov.sg/media-and-publications/media-releases/cocacola-singapore-beverages-changes-business-practices-in-local-soft-drinks-market-following-enquiry-by-ccs (accessed 21 April 2016); Competition Commission of Mauritius (2013). 'Investigation into the Supply of Coolers to Retailers by Phoenix Beverages Limited and Quality Beverages Limited CCM/INV/019'. Report of Undertakings: Non-Confidential Version. Available at: http://www.ccm.mu/English/Documents/Investigations/INV019-Final%20Report%20of%20Undertaking-NC.pdf (accessed 21 April 2016); European Commission (2005). Commission Decision. Case COMP/39.116/B-2 Coca-Cola. Available at:

in South Africa, a settlement was reached in the SAB Miller/Coca-Cola bottlers merger which included, among other things, an undertaking to allow 10 per cent of Coca-Cola fridge space in small retail outlets to stock competitors' carbonated soft drink products.[45]

Supermarkets also require that suppliers pay advertising discounts off the purchase price for indirectly advertising on behalf of supplier's products when they advertise the supermarket chain. However, not all suppliers are required to pay an advertising fee, especially for those that heavily invest in advertising their brands. Supermarkets prefer suppliers with a brand strategy and who are continually investing in building their brand.

Over and above general trading terms, suppliers usually contribute towards retailers' cost in terms of promotions allowances. Suppliers pay supermarkets to participate in different promotions held by supermarkets such as Back to School, Hey Days, Easter and Christmas promotions. Promotion fees range from approx. ZAR2,500 to ZAR100,000, depending on the scale of the promotion and the size of the outlet. Promotion costs are typically calculated as a proportion of the total invoiced price. For example, approximately 70% of total chicken sales are sold during promotions at a price that is 10% lower than normal price. Suppliers can also run promotions at their own cost in the supermarket premises.

Long payment periods adversely affect suppliers' cash flow and working capital making it difficult to continue production. This leads to additional finance costs as suppliers find alternative sources of working capital. The effects are great for small suppliers without additional reserves to carry out day-to-day operations particularly where they lack quality administration systems that invoice promptly and correctly which results in late payments.[46] Shoprite was pointed out as being particularly aggressive when it comes to errors or queries on invoices.

An assessment of credit periods or credit cycle trends can provide an indication of buyer power of a lead supermarket chain (Figure 28). This measures the average number of days it takes the business to settle its accounts payable to suppliers. As highlighted above, the balance of power in the negotiation of trading terms is often skewed in favour of the lead supermarkets. Supermarkets would try to negotiate as long a payment period as possible as this affects their cash flows. Conversely, suppliers obviously prefer as short a payment period as possible so that they don't face cash flow crunches.

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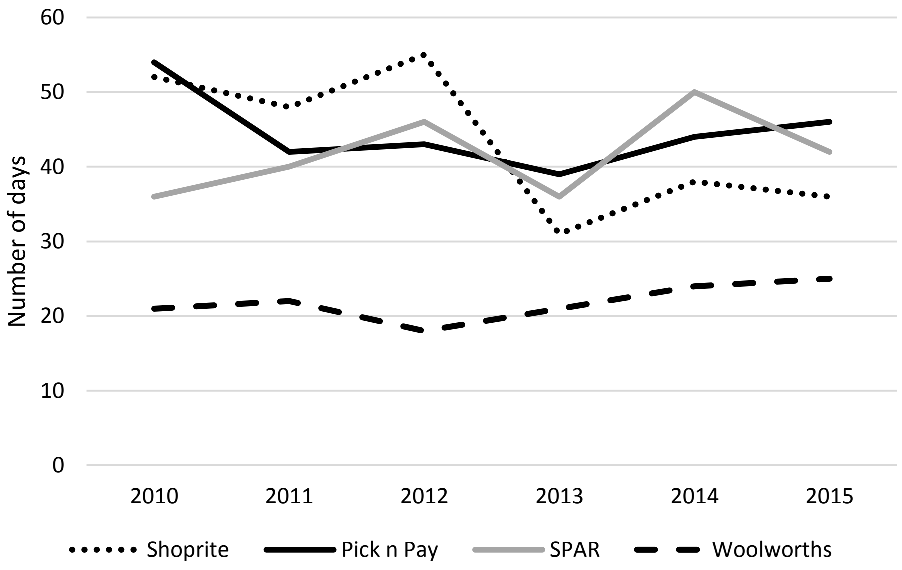
http://ec.europa.eu/competition/antitrust/cases/dec_docs/39116/39116_258_4.pdf (accessed 21 April 2016).

[45] http://www.compcom.co.za/wp-content/uploads/2016/01/SABMiller_AB-InBev_31May16_1530-3.pdf

[46] Consumers International. (2012). The relationship between supermarkets and suppliers: What are the implications for consumers?

Figure 28: Credit periods of supermarkets, 1999 – 2015



Source: Annual Reports

*Notes: Credit Period: (Trade credit / Turnover) * 360*

As can be seen, Shoprite has significantly reduced credit periods for its suppliers, with a sharp decline in 2012. Woolworths has the lowest credit period of the four firms evaluated. Woolworths supplies a wide range of house brands/private labels, forming close relationships with suppliers to produce these goods. These low credit periods may be a reflection of its exclusive relationships with many of its suppliers.

Settlement discounts are also given to supermarkets for paying the supplier within the number of days stipulated in the trade agreement, which varies depending on the supplier. It is commonly 15–30 days from statement and the discount for paying within this period is usually in the range of 2.5–5% off the list price

The cumulative sum of these fees would be administered as a percentage discount off the invoice price that the supermarket pays the supplier. For some suppliers, this can be between 10-15% off the invoice price but this varies between suppliers, and can be significantly higher. This places a significant burden on the margins of suppliers, particularly small suppliers.

Suppliers highlighted that entry of new supermarket chains (like Walmart and Choppies) into South Africa has improved competition allowing them to secure more favourable contracts and trading terms. This emphasises the importance of increased competition between supermarket chains which provides suppliers with alternative routes to market, allowing them to play off one chain against the other during negotiation of trading terms.

Another avenue through which supermarkets can increase their bargaining power against suppliers is through increasing their range of private label or house brand products. There has been growth in private label products in supermarket shelves in South Africa recently. Every major supermarket chain has a range of own brand/private label products.[47] Many suppliers of branded products also manufacture and sell private labels to supermarkets. Supplying house brands is a way in which suppliers can get their products on supermarket shelves. Suppliers can use this as a stepping stone to get onto supermarkets' preferred supplier lists especially for suppliers that have not yet built a brand name. House brands also confer some bargaining power to supermarkets over large, multinational suppliers. However, concerns were highlighted around suppliers being 'forced' into supplying house brands at lower margins than their own branded products and this was used as a tool to negotiate down prices for branded products. For instance, a large poultry supplier expressed its difficulty in supplying a house brand to a supermarket chain, where it was forced to compete with other house brand suppliers of the same product, making it more difficult to negotiate price increases (Ncube et al. 2016).

4.2. Supplier Development Programmes

As highlighted, the growth of supermarkets and modernisation of procurement systems has placed considerable pressure on suppliers. Supermarkets require that suppliers make basic investments in their product before they can start supplying them. These investments include branding (to build brand awareness and loyalty), advertising, sampling, point of sale material, packaging, merchandising and marketing. Such investments ensure that the product sells in the market, which is the suppliers' responsibility. This often requires significant investment in capital, technological, managerial, organisational, and financial upgrades.

Some lead supermarket groups are more active in building these required capabilities through close partnerships with local suppliers than others. Similarly, some key suppliers have successfully entered supermarket value chains on the back of their own investments.

Private sector-led supplier development initiatives

If supermarkets provide support in terms of governance in the value chain, they can transfer skills, knowledge and best practice to suppliers. South African lead supermarkets do offer supplier development programmes. The benefits of these for suppliers will be assessed and a comparison of the programmes across supermarkets

[47] Majority of Woolworths' products are private labels. Shoprite has its 'Ritebrand' and 'Housebrand' ranges in Checkers, which covers around 300 products. Pick n Pay has its 'No Name' brand and is looking to further expand the private label range. Food Lover's Market produces its own house brands 'Freshers' and 'Food Lover's Signature'. SPAR also has its own branded products. SPAR does not allow major suppliers to manufacture its own private label products, thus allowing new and small suppliers to enter the supermarket supply chain.

will be undertaken. In particular, the evaluation will include (but not be limited to) the following:

Woolworths Enterprise Development programme: Woolworths supports existing suppliers to improve their empowerment credentials and supports the introduction of small, medium, black-owned and black women-owned suppliers. The programme provides financial assistance (including shorter payment terms), guaranteed business as well as a package of support that includes mentorship, targeted upskilling and assistance from external experts (Woolworths Holdings Limited, 2010). Black enterprises can access the programme for three-to five-years, after which they should demonstrate that the enterprise has reached a certain level of sustainability.

Pick n Pay's Enterprise and Supplier Development Scheme: This programme assists small suppliers enter the retail market through providing mentorship, guidance and business development support. The programme provides preferential trading terms to small suppliers with a turnover of less than R3 million over a period of 12 months. Such preferential trading terms include 1% cash settlement, 1.5% advertising, 5% rebate, and 7-days payment terms from weekly statement (Pick n Pay, 2015)

SPAR's Rural Hub Model (Mopani District in Limpopo): This initiative is aimed at empowering local small farmers who struggle with meeting the required quality, volumes and consistency needed to supply supermarkets. Funding for the initiative was obtained from the Dutch Government, the Masisizana Fund and the Jobs Fund. The programme involved setting up a Fresh Assembly Point (FAP) which was jointly owned by local farmers and SPAR as the mentor. The FAP assisted farmers in meeting international food safety and quality standards set by Global G.A.P necessary for small suppliers to access larger markets

Shoprite Checkers through Freshmark, its fresh produce distribution arm, embarked on a 3-year programme (2008-2011) to assist 200 small-scale farmers meet Freshmark's minimum food safety and quality standards in South Africa, Swaziland, Namibia and Zambia. Failure by small scale farmers to meet the Global G.A.P standard and the Freshmark Good Manufacturing Practice standard would mean exclusion of small scale suppliers from Shoprite's supply chain. The programme entailed comprehensive training sessions, capacity building, data collection, compliance evaluation, provision of technical support and regular inspections.

Massmart/ Walmart: created as part of the conditions imposed by the Competition Appeal Court in the Walmart/Massmart merger, the merged firm had to set up a Supplier Development Fund (SDF) and make available ZAR 240 million over a period of five years to develop suppliers. The programme has been operating for approximately 4 years. Massmart worked with TechnoServe, a non-profit organisation, to upskill and train farmers to supply fresh produce to its stores, in addition to providing preferential finance terms and inputs. The retailer invested R40 million in smallholder farming to support Massmart's move into fresh produce and grocery market. However, this programme was relatively unsuccessful and has been discontinued due to several setbacks:

- Small farmers were vulnerable to crop disease and weather and could not afford insurance leading to huge crop losses. Massmart ended up covering their costs and purchasing seeds for new crop;
- Massmart entered into pricing agreements with farmers but did not require exclusivity arrangements. The result was that farmers would supply other retailers who offered better prices than Massmart. In the end, Massmart only received suppliers' produce when the market price was low (below the contract price) thereby incurring losses.
- Massmart was required to provide support in terms of farming equipment, logistics, pack houses, extension services (soil science and fertilizers) and carry out significant investment in attaining food safety requirements. Massmart underestimated the cost of these investments and they were not financially prepared to carry out such investments.

There were however some successful initiatives on the manufacturing/processing side of the initiative (e.g. Lethabo Milling, The Noodle Factory, Thistle Bakery and Marble Gold). The Noodle Factory based in Cape Town has been listed with Makro for 13 years supplying an Indonesian noodle brand called Alhami. The firm has started supplying other retail chains such as Fruit & Veg City and Shoprite Checkers.

Lethabo Milling, a maize milling company based in Free Sate received financial assistance as part of the programme. Lethabo received a R1.6 million grant from Massmart towards refurbishing its plant. The support extended to an offtake agreement with Massmart which helped Lethabo further secure a loan from a commercial bank. Lethabo has a guaranteed route to market through supplying Massmart stores in South Africa and has received additional support for training, waived listing fees, fast-track payments (7-day payment period as opposed to 30-day payment terms), and assistance with pricing models. Lethabo Milling is still receiving assistance from the SDF following the challenges brought about by the drought resulting is escalating grain prices. The programme is assisting by providing revolving credit for the miller's operations and assisting with negotiations to secure access to grain supply with Farmwise Grains.

Thistle Bakery based in Kempton Park is a baked goods manufacturer receiving financial assistance from the SDF. Thistle Bakery supplies baked goods under Massmart's Marketside private branding to 32 Game stores.[48]

Massmart discontinued investment in direct farming projects given the difficulties faced and because it was not a market leader in the category of fresh produce. Therefore, it could not influence the end selling price of fresh produce, resulting in a squeeze in profits for products produced by farmers under the programme.

[48] Supplier Development Programme Massmart Report (2015).

Massmart has since shifted its supplier development programmes to focus on building supplies category where it is regarded as a market leader. The current Massmart model focuses on established business that can be up-scaled quickly in FMCG, General Merchandise, DIY and Building, where it makes mutual commercial sense for both Massmart and the supplier. It deals with manufacturers of different building materials ranging from tiles, bricks, doors, nails and ladders. Massmart argues that small suppliers in this category have a greater chance of success because customer demand is more consistent and predictable allowing regular take-off orders with large procurement volumes and wider offering. In terms of household consumables Massmart assists a houseware detergent manufacturer based in Gauteng supplying 70% of its product through Massbuild stores. The supplier was assisted to meet Massmart's ethical sourcing and other requirements.[49]

Other funds from the private sector: Agro-Processing Competitiveness Fund, was set up from the Pioneer cartel settlement. This fund of ZAR 250 million, with substantial co-funding from the Industrial Development Corporation (a development finance institution), offers support to non-dominant agro-processing players in the form of investment support, business support and research grants.

Support from government in supplier development

There are a number of government programmes that offer support to suppliers to supermarkets. Existing funding and support available to small suppliers appears however to involve complicated processes and extensive paperwork. Some of the programmes that will be evaluated include:

- **IDC** support through rebates on capital expenditure (estimates are that around a 15% rebate is obtainable)

- The Wholesale and Retail Sector Education and Training Authority (**W&R SETA**) which aims to facilitate the skills development needs through learning programmes, disbursement of grants and monitoring of education and training. In 2015, the W&R SETA created a central supplier database where suppliers of different products are encouraged to register. Public entities are then required to procure goods, services and/or products from the listed suppliers. This is meant to provide markets for small suppliers through increased government procurement. Whether this had any spill-over advantages into supplying supermarkets will be assessed.

- The Food and Beverages Sector Education and Training Authority (**FoodBev SETA**) which aims to promote skills development in the food and beverages manufacturing sector. This SETA identifies critical and scarce skills through annual reports submitted by employers in the following sub-sectors: Baking,

[49] Supplier Development Programme Massmart Report (2015).

Cereals, Confectionery & Snacks, Beverage Manufacturing, Dairy Manufacturing, Manufacture of Food Preparation Products and Processed and Preserved Meat, Fish, Fruit and Vegetables. It assists with skills gap in the food and beverages sector by awarding bursaries annually for undergraduate and postgraduate studies.

- Government through the Department of Trade and Industry (DTI) runs the Black Business Supplier Development Programme (BBSDP) - a cost sharing grant offered to existing small black-owned enterprises aimed at improving small suppliers' competitiveness and sustainability. For existing businesses only, this programme shares costs with suppliers by extending grants for tools, machinery and equipment. It offers supplier business development and training interventions meant to improve corporate governance, management, marketing, productivity and use of modern technology.

While supplier development programmes by the major supermarkets in South Africa have yielded some positive results, they are limited in scale and scope, and ad hoc in nature. As can be seen, almost all the initiatives of the supermarkets involve small scale farmers and are only for a short duration. As the failure of the Massmart farmer development initiative highlights, in order to be successful it is necessary to have longer term programmes for farmers. All the initiatives also appear to be approached more as corporate social responsibility obligations rather than commercially viable endeavours. In order to have wider and more sustainable impact on developing supplier capabilities, such programmes have to be part of regular, long-term operations of supermarkets.

Suppliers interviewed for past research generally claimed to have little or no support from government. Lack of financial support was a significant concern raised by small suppliers who encounter serious challenges with accessing finance to maintain cash flow and working capital. Lack of access to finance means that suppliers cannot make the necessary investments in their plant, product and brand. Existing government funding and support available to small suppliers involves complicated and extensive paperwork. Suppliers claimed to face considerable bottlenecks forcing them to use consultants at their own expense to try to access such pockets of funding.

5. Conclusions and recommendations

This report has highlighted the central importance of supermarkets as a key route to market for suppliers. The growth, performance and strategies of supermarkets as large lead firms are therefore significant for the development trajectory of agro-processing and light manufacturing industries in South Africa and in the region. It is important therefore to keep track of the growth and to regularly monitor the strategies of supermarket chains.

The report showed that the supermarket industry has indeed grown over the past five years, measured by investments in assets and real turnover. The nature of investments in the retail business appears to be largely through acquisitions rather than organic growth. However, Shoprite appears to be pursuing a strong organic growth model. Growth of South African supermarkets is not only limited to South Africa, but all the chains are expanding rapidly into the rest of Africa. International and regional retailers are also investing in South Africa and slowly gaining market share. This opens up opportunities for local suppliers to increase their scale of production and upgrade their capabilities.

Entry of new supermarket chains that are effective rivals to the incumbents has been relatively slow, leaving the sector concentrated with the top three South African supermarket chains controlling over 80% of the market. Lack of competition limits suppliers' options and exposes them to potential abuses of buyer power. The study highlighted that the use of centralised procurement methods, costly trading terms and stringent private standards puts considerable pressure on suppliers in terms of additional costs, suppressed profits and uncertainty. This limits participation of suppliers, particularly small suppliers, in supermarket value chains and stifles their development.

The report also undertook a preliminary scoping of existing supplier development programmes and government initiatives aimed at increasing participation of suppliers, particularly small suppliers, and the extent to which these have been successful. While supplier development programmes by the major supermarkets in South Africa have yielded some positive results in terms of opening the market to small suppliers, they have not had a major impact on developing a significant number of suppliers and building capabilities to make them sustainable in the long run. The existing supplier development programmes are also limited in scale and scope, and *ad hoc* in nature. Most initiatives involve small scale farmers over short periods of time. Lastly, most initiatives appear to be approached more as corporate social responsibility obligations rather than commercially viable endeavours.

While there are existing government initiatives meant to also financially support small suppliers, such government funding and support involves complicated and extensive paperwork forcing suppliers to use consultants at their own cost to try to access such funding.

With regards to the way forward, we suggest **(i)** on-going monitoring of the growth, performance and strategies of lead supermarket chains in South Africa in order to understand how industrial policy affects strategic investments of firms and where they choose to invest. As undertaken in this report, this can be done by the appropriate sector desk at the dti based on publicly available information; and **(ii)** a range of interventions to encourage competition in the retail sector, to develop local supplier capabilities and to increase participation of suppliers in supermarket supply chains. These recommendations have been raised in previous studies by CCRED.

To foster a **competitive environment for a diversity of retail models**, it is important to open up both retail spaces to rivals and supermarket shelf space for suppliers. This requires active intervention by government, competition authorities, urban planners and supermarkets. Governments can encompass open and flexible retail space in urban planning to ensure a mix of formats through planning policies, opening markets to wider participation and ensuring competition to incumbent supermarkets. This requires municipalities to play a role, possibly under guidance from the dti and the competition authorities. This also requires supermarkets to actively open up shelf space for new suppliers on competitive terms.

To reduce the cost of supplying supermarkets and promote transparency in procurement procedures and trading terms, South Africa could adopt a **retail industry code of conduct**, which could be extended to a regional code of conduct given that it is the same players that largely operate in the SADC region. Such codes as applied in several other countries regulate the conduct of supermarkets towards suppliers by setting minimum standards and obligations for retailers with regard to drafting of supply agreements and various fees included in the trading terms. Namibia recently adopted the retail sector charter in March 2016 aimed at increasing participation of local suppliers through transparent procurement procedures, fair payment terms and rebate provisions. Importantly, the commitment to codes of conduct can help to reduce costs and uncertainty faced by suppliers.

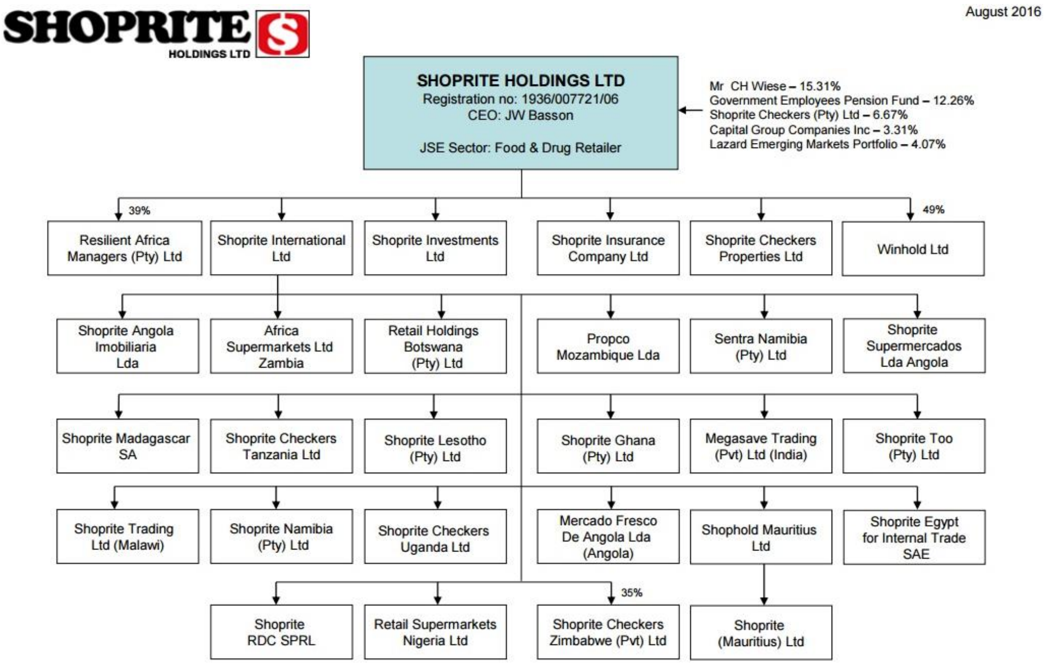
The international experience has also shown that voluntary or mandatory codes of conduct between suppliers and supermarkets are a useful way to control the exertion of buyer power and have been identified as a practical and effective approach in developing countries to level the playing field and reduce information asymmetries between suppliers and supermarkets. For instance, supermarkets in Australia are not allowed to directly or indirectly request suppliers to pay listing fees, shrinkage fees, wastage fees, promotion fees or payment for better positioning of products on the supermarket shelves (enforced by the Australian Competition and Consumer Commission). Only certain exceptions are permitted and any amount paid must be considered reasonable according to predefined criteria. In the United Kingdom, the Groceries Supply Code of Practice stipulates that retailers are required to comply with the Groceries Market Investigation Order of the former Office of Fair Trading which oversees the relationship between supermarkets and their suppliers.[50] In Ireland, there are plans to institute a mandatory Code of Conduct in the grocery sector, to be overseen by the Department of Jobs, Enterprise and Innovation. In Spain, a new act focusing on measures to improve the functioning of the food chain was promulgated in 2013; it uses a mixed model of regulation and self-regulation (through voluntary codes of conduct) to govern commercial relations between the agents in the food chain.

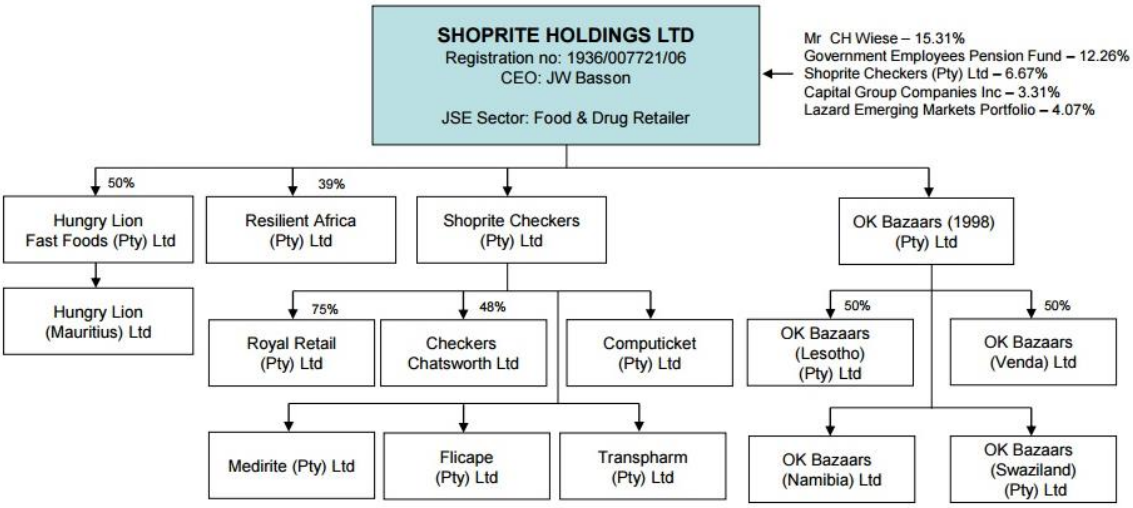
[50] This Code is enforced in the United Kingdom by an independent Groceries Code Adjudicator, set up specifically to oversee the relationship between supermarkets and their suppliers and housed within the former Office of Fair Trading (OFT).

Such measures (a code of conduct or a **retail/supermarket charter**) can be championed by the dti, and harmonized across the region given that it is largely the same retailers that operate in the region. A growing opportunity for suppliers to participate in supermarket chains is through producing house brands or private labels for supermarkets. However, concerns around buyer power being exerted on suppliers of house brands at the expense of their branded product have been raised. Again, codes of conduct covering negotiations of trading terms tailored for house brands can potentially alleviate some of these concerns.

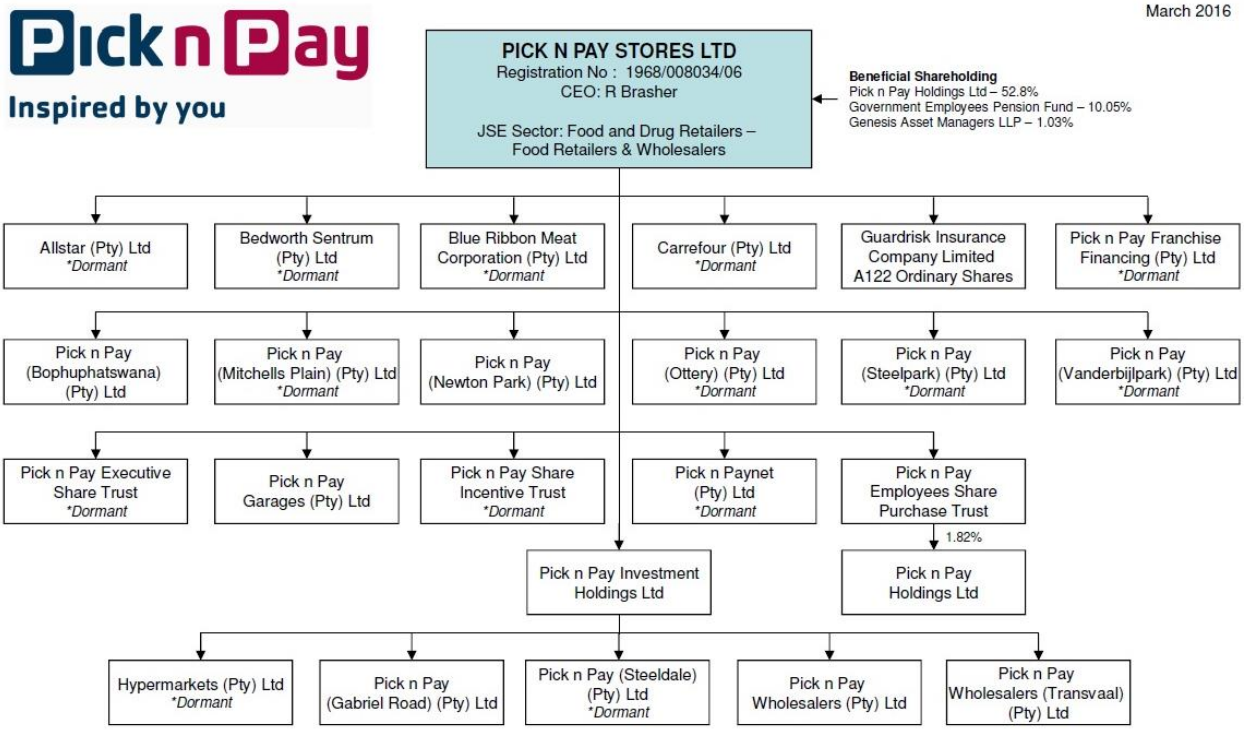
Development of successful **supplier development programmes** requires a much larger, long-term, commercially oriented approach by supermarkets possibly in partnership with the dti. This can be done through the creation of supplier development funds as part of programmes similar to the Massmart/Walmart supplier development programme. Co-funding for such programmes can come from fines levied by the competition authorities in abuse of dominance or cartel matters. Co-funding can also come from existing pockets of funding reserved for black industrialists and small businesses. The critical point is that this funding needs to be channeled appropriately to commercially sustainable business that are mutually beneficial for both the supermarket and the supplier in the long term. For this to happen, the supermarket sector has to be intimately involved in designing and structuring the programmes and in identifying and developing the suppliers qualifying for the support. It cannot purely be financial support without any capability development.

6. Appendix A: Company organograms

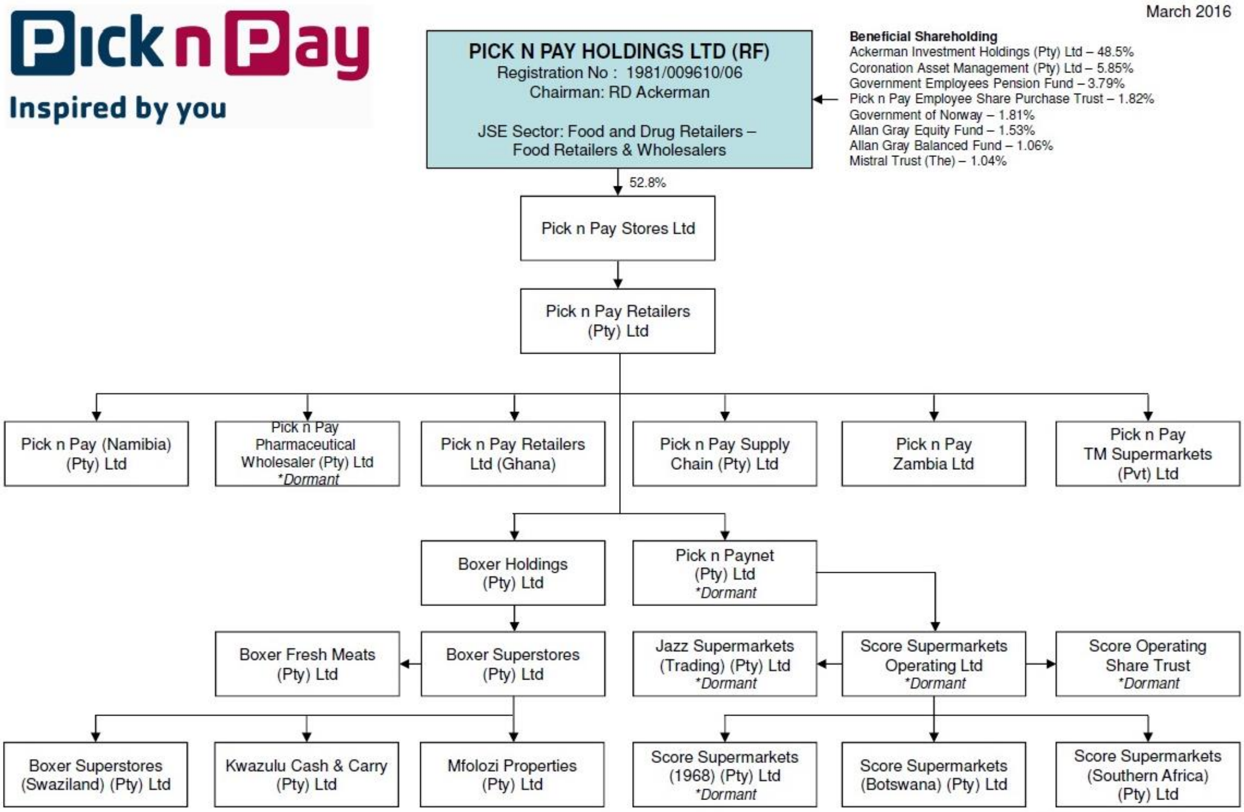


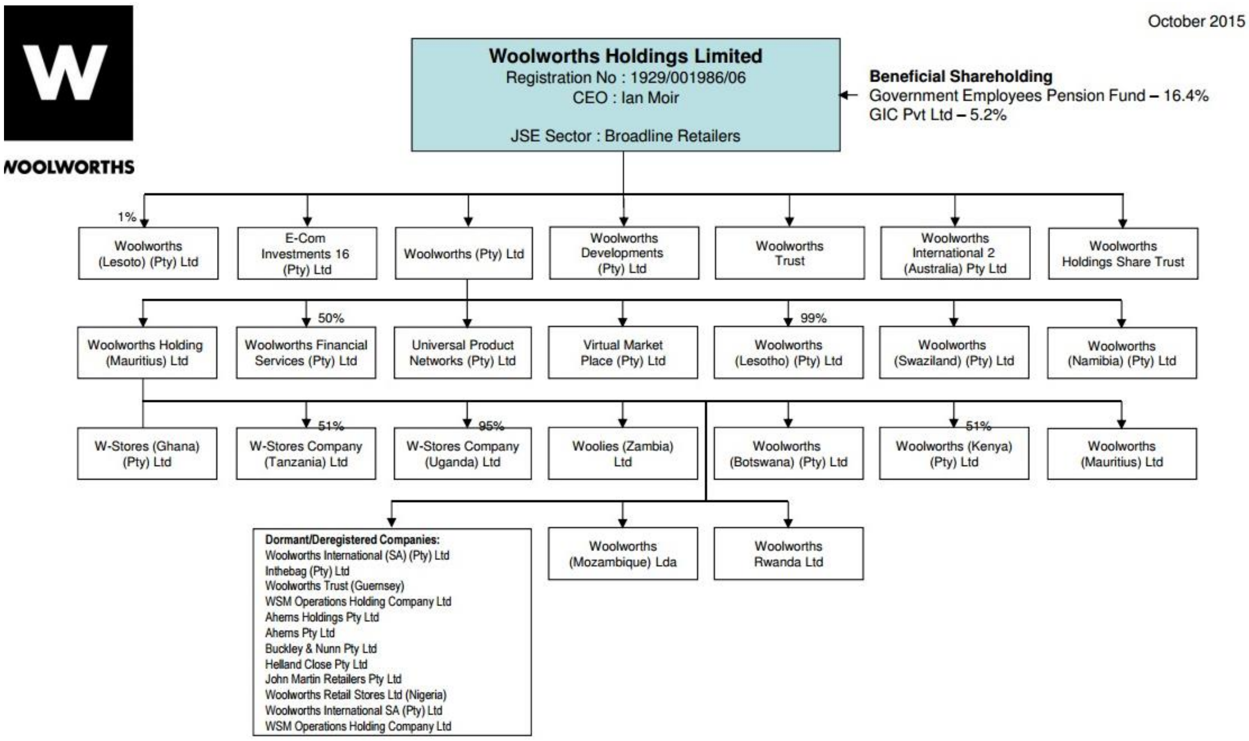


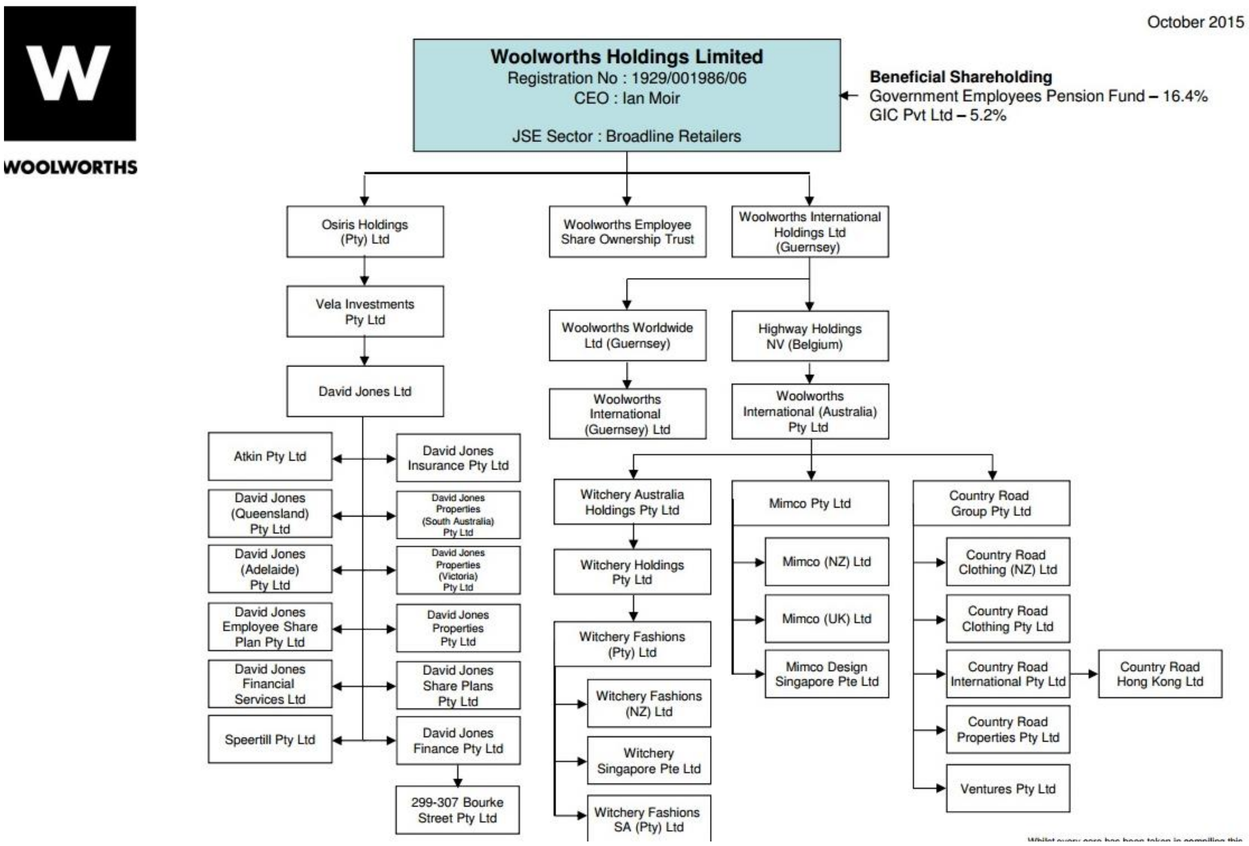
March 2016

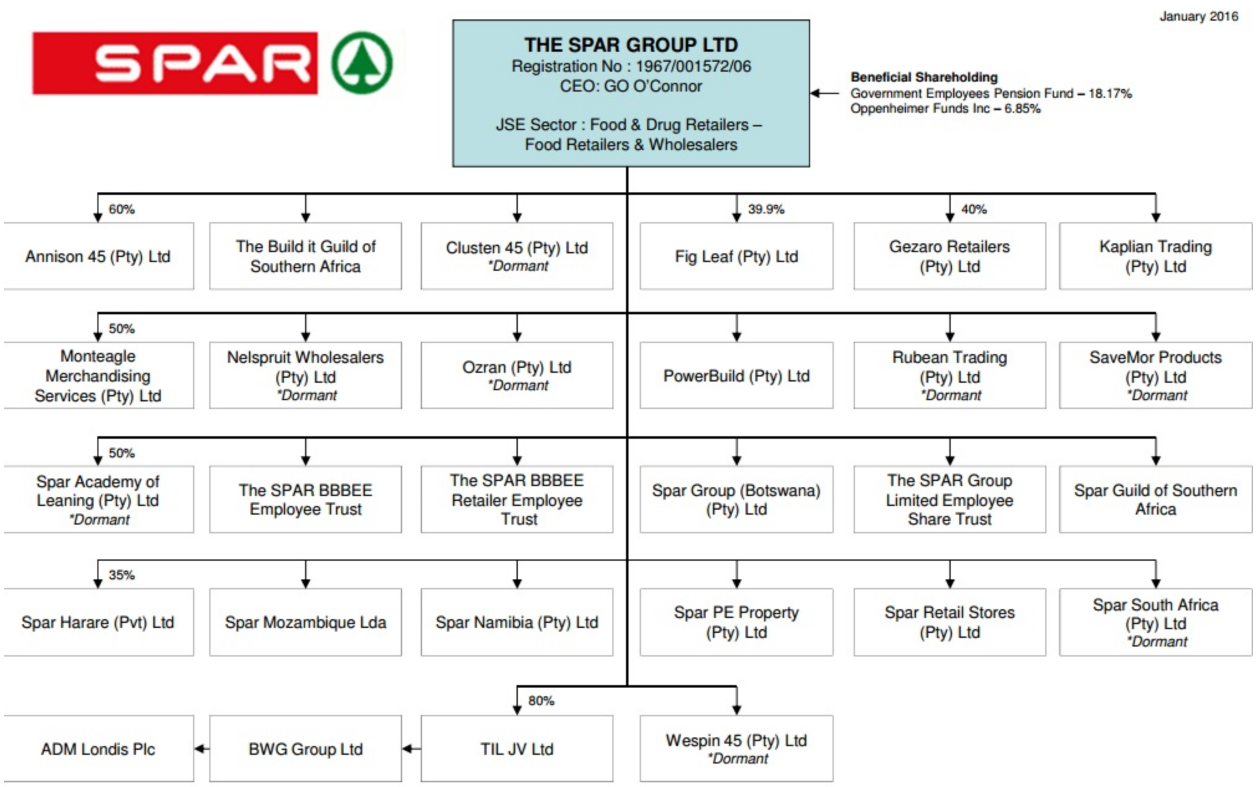


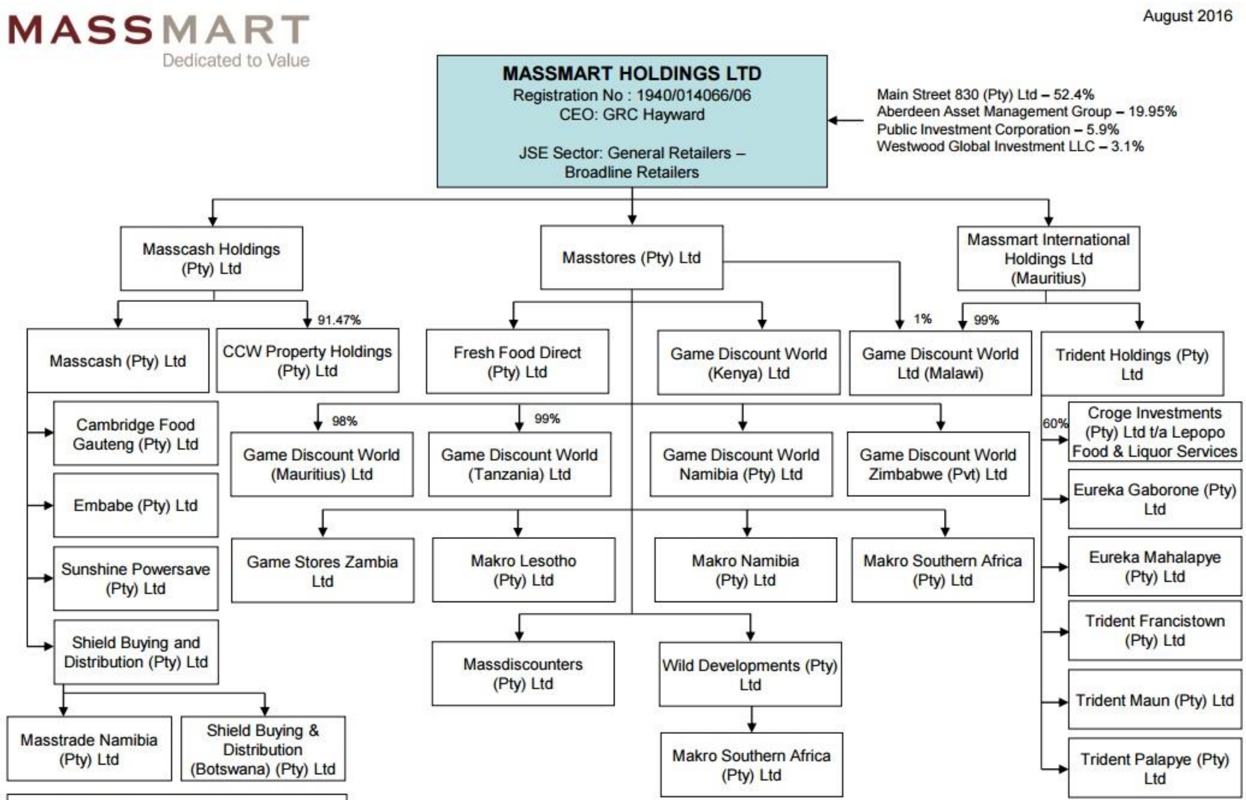
March 2016




WOOLWORTHS
October 2015
Woolworths Holdings Limited
Registration No : 1929/001986/06
CEO : Ian Moir
JSE Sector : Broadline Retailers
Beneficial Shareholding
Government Employees Pension Fund – 16.4%
GIC Pvt Ltd – 5.2%
1%
Woolworths (Lesoto) (Pty) Ltd
E-Com Investments 16 (Pty) Ltd
Woolworths (Pty) Ltd
Woolworths Developments (Pty) Ltd
Woolworths Trust
Woolworths International 2 (Australia) Pty Ltd
Woolworths Holdings Share Trust
50%
99%
Woolworths Holding (Mauritius) Ltd
Woolworths Financial Services (Pty) Ltd
Universal Product Networks (Pty) Ltd
Virtual Market Place (Pty) Ltd
Woolworths (Lesotho) (Pty) Ltd
Woolworths (Swaziland) (Pty) Ltd
Woolworths (Namibia) (Pty) Ltd
51%
95%
51%
W-Stores (Ghana) (Pty) Ltd
W-Stores Company (Tanzania) Ltd
W-Stores Company (Uganda) Ltd
Woolies (Zambia) Ltd
Woolworths (Botswana) (Pty) Ltd
Woolworths (Kenya) (Pty) Ltd
Woolworths (Mauritius) Ltd
Dormant/Deregistered Companies:
Woolworths International (SA) (Pty) Ltd
Inthebag (Pty) Ltd
Woolworths Trust (Guernsey)
WSM Operations Holding Company Ltd
Ahems Holdings Pty Ltd
Ahems Pty Ltd
Buckley & Nunn Pty Ltd
Helland Close Pty Ltd
John Martin Retailers Pty Ltd
Woolworths Retail Stores Ltd (Nigeria)
Woolworths International SA (Pty) Ltd
WSM Operations Holding Company Ltd
Woolworths (Mozambique) Lda
Woolworths Rwanda Ltd


WOOLWORTHS
October 2015
Woolworths Holdings Limited
Registration No : 1929/001986/06
CEO : Ian Moir
JSE Sector : Broadline Retailers
Beneficial Shareholding
Government Employees Pension Fund – 16.4%
GIC Pvt Ltd – 5.2%
Osiris Holdings (Pty) Ltd
Woolworths Employee Share Ownership Trust
Woolworths International Holdings Ltd (Guernsey)
Vela Investments Pty Ltd
Woolworths Worldwide Ltd (Guernsey)
Highway Holdings NV (Belgium)
David Jones Ltd
Woolworths International (Guernsey) Ltd
Woolworths International (Australia) Pty Ltd
Atkin Pty Ltd
David Jones Insurance Pty Ltd
David Jones (Queensland) Pty Ltd
David Jones Properties (South Australia) Pty Ltd
David Jones (Adelaide) Pty Ltd
David Jones Properties (Victoria) Pty Ltd
David Jones Employee Share Plan Pty Ltd
David Jones Properties Pty Ltd
David Jones Financial Services Ltd
David Jones Share Plans Pty Ltd
Speertill Pty Ltd
David Jones Finance Pty Ltd
299-307 Bourke Street Pty Ltd
Witchery Australia Holdings Pty Ltd
Witchery Holdings Pty Ltd
Witchery Fashions (Pty) Ltd
Witchery Fashions (NZ) Ltd
Witchery Singapore Pte Ltd
Witchery Fashions SA (Pty) Ltd
Mimco Pty Ltd
Mimco (NZ) Ltd
Mimco (UK) Ltd
Mimco Design Singapore Pte Ltd
Country Road Group Pty Ltd
Country Road Clothing (NZ) Ltd
Country Road Clothing Pty Ltd
Country Road International Pty Ltd
Country Road Hong Kong Ltd
Country Road Properties Pty Ltd
Ventures Pty Ltd





Please note : This is the best assessment we can make without confirmation from the company.

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