

Determining the business impact of retail store openings on a sales and distribution company

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ABSTRACT

The retail environment is experiencing some difficult challenges lately. Consumers are under threat due to the current economic situation in South Africa with rising inflation and increasing utility costs such as water and electricity. This scenario has an affect the consumer's disposable income that affects what they spend with retailers. Sales growth for retailers is ultimate, what the industry is all about. The sales growth in the past is not as desirable lately, and retailers are seeking other ventures to get growth. They are targeting to increase their footprint into South Africa as a way to seek growth. New retail stores in South Africa is increasing rapidly. South Africa is one of the six biggest countries with a number of retail stores and shopping centres but on the other hand, have one of the highest unemployment rates in the world. Retailers among themselves are very competitive, and the biggest retailers are trying to get a market share of the industry. With the store openings, retailers try to achieve that. It is evident that five years ago Pick n Pay was the largest retailer in South Africa, but Shoprite has captured market share through the years and is now the leading retailer in South Africa with 27% market share. Increasing in the number of retail stores affect companies that need to service the retailers. With increasing of stores comes increasing costs. Sales growth from new store openings is not sufficient to cover costs and with retailers' strategies to continue increasing footprint, will have an unfavourable effect on sales and distribution companies when it comes to their profitability and future. Over the past five years from 2011 to 2016, retailers increased their footprint dramatically. Retailers such as Shoprite have increased store openings by 40.9% over the five-year period and Pick n Pay by 29.4% over the same period. This shows that retailers were aggressive to obtain growth, but results show a different story. This study will determine what effect the store openings have for a sales and distribution company.

Keywords: Retail environment, consumers, store openings, cost increasing, growth, profitability.

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LIST OF ABBREVIATIONS

Abbreviation	Description
ABC	Activity-based costing
Clicks	Clicks Group Holdings
CPI	Consumer Price Index
DC	Distribution Centre
DSD	Direct Store Delivery
EDI	Electronic Data Interchange
FMCG	Fast-moving Consumer Goods
GDP	Gross Domestic Product
IT	Information Technology
JSE	Johannesburg Stock Exchange
LSM	Living Standard Measures
Massmart	Massmart Holdings
NDD	Nominated Delivery Date
NOD	Nominated Order Date
Pick n Pay	Pick n Pay Holdings Limited
ROE	Return on Equity
SACSC	South Africa Council of Shopping Centres
Shoprite	Shoprite Holdings Limited
Spar	Spar Group Limited
ULP	Unleaded Premium
UPD	United Pharmaceutical Distributors
VAT	Value Added Tax
Woolworths	Woolworths Holdings Limited
YOY	Year on year

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CHAPTER 1: NATURE AND SCOPE OF THE STUDY

1.1 INTRODUCTION

The main focus of this study is to determine the impact that retail stores' openings have for an entity in the industry of a sales and distribution company.

The data that was used is a company ("The Company") that is in the Fast-moving Consumer Goods (FMCG) industry and distribute clients' products to all major retailers in South Africa, as well as neighbouring countries of South Africa. They are also responsible for the in-store executions for their clients' products in the retail stores that means, for instance, merchandising and packing of shelves. "The Company" earn percentage commission based on the total sales to the customers from their clients they represent. Each year there are agreements signed between the Company and the retailers that are mandated by their clients.

The past years "The Company" are in the top 10 of Clicks Group Ltd from a supply point of view and the other five customers they are ranging in the top 50. "The Company" is also responsible for the sales and merchandising of these customers for their portfolio of products. They will have merchandisers that will make sure that shelves are packed according to specification, and sales representatives will make sure that there is enough stock in the stores.

All companies in this day and age are looking for cost-effective solutions to be viable in the future. If one takes a look at GDP for South Africa, it was 3.3% for the quarter of June 2016 (Trade Economics, 2016) together with increasing inflation at 6.2% means that businesses are under pressure to show growth. In the retail sector of South Africa, the consumers are also under pressure due to inflation and thus have a direct impact on the retail industry. Consumers are not spending as much as anticipated initially and can be seen that the year on year sales only increased by 0.8% for quarter 2 of 2016 (Trade Economics, 2016).

According to the retail and consumer products outlook when competition increases from retail sectors, companies are driven to introduce more efficient supply chains and technology improvements to reduce the cost of doing business. It was also raised that inflation will put more pressure on consumer goods companies to cut cost on supply chains and operations to achieve volume growth that can succeed the fixed costs (Fouche 2012:6).

Due to the above, a company that services these retail stores becomes increasingly difficult to make a profit due to rising costs. The six biggest retail customers in South Africa are currently Shoprite Holdings Limited (Shoprite); Pick n Pay Holdings Limited (Pick n Pay), Spar Group Limited (Spar), Clicks Group Limited (Clicks), Massmart Holdings (Massmart) and Woolworths Holdings Limited (Woolworths). Lately, the retail customers have become more aggressive with their new store developments to assist with growth in their businesses and to get the consumers to their store rather than their competitors. According to the Corporate Retail Channel Report the total store universe for these customers are Shoprite Holdings with 2,549 stores, Pick n Pay with 1,333 stores, Massmart with 412 stores, Spar with 2,033 stores, Woolworths with 1,395 stores and Clicks with 689 stores (Corporate Retail Channel Report, 2017a).

Retailers have become more aggressive with its new store openings to enable them to get the significant growth in the markets. According to Corporate Retail Channel Report, the total number of new store openings were 353 during the 2015 financial year and 361 new stores in 2016. Total planned new store openings for 2017 are Shoprite Holdings with 194, Clicks with 25, Massmart with 58 and Woolworths with 24 new stores which are planned. Pick n Pay and Spar did not yet give an indication yet of new store openings in 2017 (Corporate Retail Channel Report, 2017a)

As a business, merchandisers have to service the new retail stores still. Some retailers charge you a distribution rate to have your stock in their distribution centres (DC), but it is a well-known fact that retailers often only want fast-moving consumer products in their DCs but still want the other products in the store. Furthermore, there are other operating expenses, for example, salaries that have a major impact on an organisation if a new retail store opens. As described, this fact makes it difficult to service these stores financially if new stores open, for instance, in the outline areas and have a direct to store delivery to

them. Table 1.1 below shows how the total number of retail stores from 2011 to 2016 expanded for the six customers in this research only.

Table 1.1: Store Counts from Retailers (2012-2016)

	FY2012	FY2013	FY2014	FY2015	FY2016	5-year Net New Stores	5-year Change
Shoprite	424	453	503	566	577	153	36%
Checkers	167	173	185	201	202	35	21%
Checkers Hyper	28	29	31	36	37	9	32%
Usave	259	299	327	348	355	96	37%
Pick n Pay Hyper	20	20	20	20	20	0	0%
Pick n Pay Corporate	174	185	200	215	226	52	30%
Pick n Pay Franchise	282	287	277	288	289	7	2%
Pick n Pay Express	9	17	21	46	80	71	789%
Boxer Superstore	99	113	123	125	138	39	39%
Game	107	121	130	137	139	32	30%
Makro	16	19	19	19	20	4	25%
Masscash Wholesale	79	77	73	70	68	-11	-14%
Mascash Retail	28	47	47	51	52	24	86%
Superspar	295	305	313	329	329	34	12%
Spar	439	432	427	425	425	-14	-3%
Kwikspar	134	136	135	131	131	-3	-2%
Savemor	17	28	28	32	39	22	129%
Woolworths Foods	366	365	374	409	410	44	12%
Woolworths Franchise	300	296	297	317	321	21	7%
Clicks	402	442	464	486	496	94	23%

Source: Trade Intelligence Master Data, respective retailer's financial results, 2016a

It is a constant battle to keep costs to a minimal due to the aggressive approach from retailers to have bigger market share than their counterparts and thus increase their footprint in South Africa with new store openings. The sales growth out of the new retail store openings is not sufficient to cover the variable and fixed costs for an organisation. The above background has a direct impact on companies such as "The Company" when it comes to new store openings.

1.2 PROBLEM STATEMENT

This study examines the impact of cost factors (distribution, salaries, advertising and debt collecting) on a sales and distribution company's profitability due to an increase in new retail store openings in South Africa that need to be serviced.

For a sales and distribution company to service current and new retail store involves:

- Appointment of merchandisers to pack the shelves of the products the organisation represents in the trade;
- Sales representatives need to call on an additional store for order and inventory levels;
- Distribution to the specific retail store if not in DC; and
- Travel costs.

For all these costs above an organisation needs to evaluate the impact that costs will have in its business. The concern for these organisations is all well if retail stores increase and the total sales of the products also increase together, but lately the total sales growth that the consumers show, do not warrant the new stores due to the fixed costs a business has only increased, and one would imagine the sales, which is directly linked to the commission of the business, do not grow as anticipated. The consumer does not spend more now that a store is closer to his/her work or house but now just shifts its favourable customer store to the closest shop now rather with another retail chain.

According to Makhala (2016), the independent analyst Syd Vianello stated that retailers' new store openings need to slow down and rather concentrate on using existing space efficiently and tough times like these the retailers will become more aggressive with promotional spend in a bid to lure consumers into their stores.

These factors together with all new retail store openings will have a direct impact on costs and margins for a sales and distribution company. They will have to operate sufficiently, effectively to maintain competitively, and to achieve in store objectives from the basket of products that they are responsible for. Costing and planning are of high importance to still trade profitably for an enterprise.

1.3 OBJECTIVES OF THE STUDY

The objectives of the study are divided into primary and secondary objectives.

1.3.1 Primary objective

The primary objective was to determine the cost factors that have an effect on the profitability of a sales and distribution company in the retail sector of South Africa due to the increase in retail stores that needs to be serviced.

1.3.2 Secondary objectives

The primary objective is achieved by the following secondary objectives:

- The market share of the six biggest retailers in South Africa.
- Determining which factors have an impact when new store openings occur and as such:
 - New store openings have not sufficient growth in sales to be viable for operating costs.
 - Total universal sales growth of retailers do not increase with new retail store openings; consumers only spend now at stores closer to their home or work or switch to other retailers.
 - Salary costs of field workers in the retail environment.

1.4 SCOPE OF THE STUDY

1.4.1 Field of study

The study falls into the FMCG industry, specifically on retailers in the food and grocery sector as well as the health and beauty sector. It emphasises how retailers grow their footprint in South Africa and with the expansion of footprint, it does not bring in more sales for retailers.

1.4.2 Geographical demarcation

The retailers that were focussed on are, as mentioned above, the six biggest retailers in South Africa. The six retailers will be focussed only in South Africa and not the retailers' export markets. This study also takes into account the data collected by "The Company" that is operating across South Africa with all the retailers. "The Company" is a national entity which is operating across all the provinces of South Africa.

1.5 RESEARCH METHODOLOGY

1.5.1 Literature study

Establishing a thorough theoretical background is essential to the problem statement as mentioned above. Detail and analysis of theories related to factors that will have an impact in this study need to be addressed in detail.

The main focus of a literature study is to gain knowledge of the industry as well as the determining factors. Knowledge gathered from the literature study was used for analysing the data that were collected.

Sources that were used for the literature study is:

- Academic books;
- Journals;
- Internet;
- Financial Statements;
- Industry Reports; and
- Previous dissertations.

1.5.2 Empirical study

This section explained what the research approach was that used and detailing the activities in conducting the specific research.

1.5.2.1 Overall research design

The quantitative research approach was used in this study. Data will be in the form of secondary data. Data of “The Company” will be used as internal data to analyse the costs for a sales and distribution companies to services retail stores and the effect it has on the profitability of a company. Furthermore, data from the six biggest retailers were collected and analysed through their financial statements that needed to be published as these are listed entities on the Johannesburg Stock Exchange (JSE).

1.5.2.2 Population and sampling method

A secondary analysis was based on financial reports of the six biggest retail customers in South Africa, namely Pick n Pay, Shoprite, Clicks, Woolworths, Masscash, and Spar. All of these companies are listed entities on the Johannesburg Stock Exchange (JSE) and will, therefore, have their financial reports available for research. The financial reports will be studied and used in the research to determine the financial results of the entities and their growth on new retail store openings. Data of “The Company” and retailers are based on results across South Africa within all provinces.

1.5.2.3 Data collection

External and internal secondary data were collected and used in the analysis. According to Lancaster (2015:81) internal secondary data is data that are already available in the organisation from financial, sales and marketing data. Data of “The Company” were used as internal data to analyses of the costs for a sales and distribution companies to services retail stores and the effect it has on the profitability of a company. This takes into account DCs and store deliveries to the retailers.

According to Lancaster (2015:80), external data is data that were collected and prepared outside the organisation like published financial reports. Thus, financial reports of the six

biggest retailers were collected for my research as a published external secondary source. The six biggest retailers are Pick n Pay, Shoprite, Woolworths, Massmart, Spar, and Clicks.

Financial results were obtained from the retailers' website or the published results after three months after year-end as prescribed by the listing requirements of the Johannesburg Stock Exchange and Section 30 of the Companies Act (71 of 2008) (SA, 2008). Furthermore, trade and industry publications were also used to collect data.

1.6 LIMITATIONS OF THE STUDY

The limitations of this study are that it focuses only on the six major customers in South Africa; they are Shoprite, Pick n Pay, Woolworths, Massmart, Clicks, and Spar. The study excludes all other retailers such as Dis-Chem, wholesalers, independent and wholesale pharmacy groups, speciality retailers (Edcon) and Tier-two retailers (for example Smash, Shield, and others). The study also focuses only on the fast-moving consumer goods sector and health and beauty sector within those specific retailers. It also excludes informal trade such as informal shops in townships and corner shops. "The Company data" referred to in this study only focuses on the six biggest retailers mentioned above.

1.7 DIVISION OF CHAPTERS

This study was organised and laid out in the following matter.

- Chapter One: Introduction to the research problem, the importance of the study and the background of the study
- Chapter Two: The review of existing literature on the cost factors and sales growth of retail stores.
- Chapter Three: Presentation and analysis of the results from data
- Chapter Four: Conclusion and recommendations based on all data collected.

CHAPTER 2: LITERATURE STUDY

2.1 INTRODUCTION

For the past few years, the retail sector is undergoing major changes and will keep changing due to the current financial situation in South Africa. The consumers are under threat, and thus it has a direct impact on spending in the retail channels. The retailers are also not willingly let margins go and pass it onto manufacturers. Distribution of product to retailers become more difficult to manage, because some deliveries will go to their distribution centres and other direct to the stores. With the strategic view of retailers on increasing their store universe even more in the future, have huge implications for manufacturers. The manufacturers are then, for instance, the sales and distribution companies. Retailers face intense competition nationally where competitors offer the same merchandise and compete by price, quality, or speed to the market. It is common to find that some retailers have evolved business models that give the consumer a better shopping experience (Wallace, 2017). South Africa has the sixth largest number of shopping centres globally, according to the South Africa Council of Shopping Centres (SACSC). The total floor area consists of over 23 million square meters consisting of more than 2,000 shopping centres. With the continuing opening of malls, strategies from the retailers are seeking opportunities to gain more market share in the fiercely competitive market (Chibaya, 2016). According to the Kloppers (2016), the increase in shopping centres with new stores will affect the smaller shops. Over time the smaller shops will start feeling pressure and will start to struggle for future growth. In the 23 million square meters of shopping space, Gauteng province has the largest and Northern Cape the lowest. Below is the breakdown per square meter, per province, from the highest to the lowest (Klopper, 2016):

- Gauteng – 10,298,782 square meters;
- Western Cape – 3,492,642 square meters;
- KwaZulu-Natal – 3,097,443 square meters;
- Mpumalanga – 1,540,473 square meters;
- Eastern Cape – 1,337,697 square meters;
- Limpopo – 1,212,060 square meters;

- North West – 984,307 square meters;
- Free State – 808,956 square meters; and
- Northern Cape – 273,821 square meters.

According to an independent analyst, Chris Gilmour, the retail market is deteriorating by the day and retailers will find it difficult because of margins that are already low. They will have to be incredibly innovative, and it is going to be all about gaining market share. Shoprite has only a few stores in high earning areas but plans to open a further 23 stores in wealthy areas. Checkers is increasingly challenging Pick n Pay, and Woolworths' dominance in some areas and Massmart had entered the fray, taking on Shoprite through the Cambridge brand, which focuses on the lower Living Standard Measures (LSMs). The uncontrolled retail environment, which is the Spaza shops, is estimated to take over some of the bigger retailers' market share. The uncontrolled retail environment grew from 45% in 2015 to 53% in 2016 (Shevel, 2017).

The Clicks Group and the Dis-Chem Pharmacies growth in the channel are expected to be driven mainly by the expanding presence of stores through the opening of more stores and the acquisitions and conversions of independent pharmacies into their chains in the years to come. Pick n Pay had the largest market share between 2003 and 2007, but could not keep up to date with Shoprite Group's expansion and increasing competition from other retailers. According to Euromonitor International, factors that influence this include high operational costs, outdated systems, lack of investments in centralised distribution. Retailers such as Woolworths, Pick n Pay, and Checkers have continued expanding, but the question should be asked if it is effective in the South Africa context (Chibaya, 2016).

In 2016 return on equity (ROE) were 51.6% for speciality retailers whereas grocery retailers came in at 22.3%. The grocery retailers have a 62% market spend whereas the speciality retailers had a 23% and the remaining 15% is for clothing retailers (Mashego 2017). The following factors have a direct effect on retailers and for the sales and distribution company that will affect their margins:

- Retail spend continues to remain fragile;
- Store growth has been marginal as new shopping centres impact trading density;
- Rising inflation and slow moving like sales and volume along with marginal store growth; and

- Rising interest rates and currency depreciation will further strain consumers' disposable income.

According to Muller (2017a) two of the JSE's largest mall owners, Growthpoint Properties, and Hyprop Investment, recently reported a slowdown in the trading density growth in their retail portfolios. The CEO of Growthpoint, Norbet Sasse, said that consumer spending at a number of their malls in Gauteng had been diluted due to the opening of new centres such as the Mall of Africa and the extension of Menlyn Park. Furthermore, he stated that it is becoming more difficult to grow turnovers given the fact of the oversupply of retail space. Over the last decade it has been rolled out at an incredible pace and some listed retailers like-for-like growth was impacted by the expansion of their stores (Mclachlan, 2016).

2.2 COSTS STRUCTURES

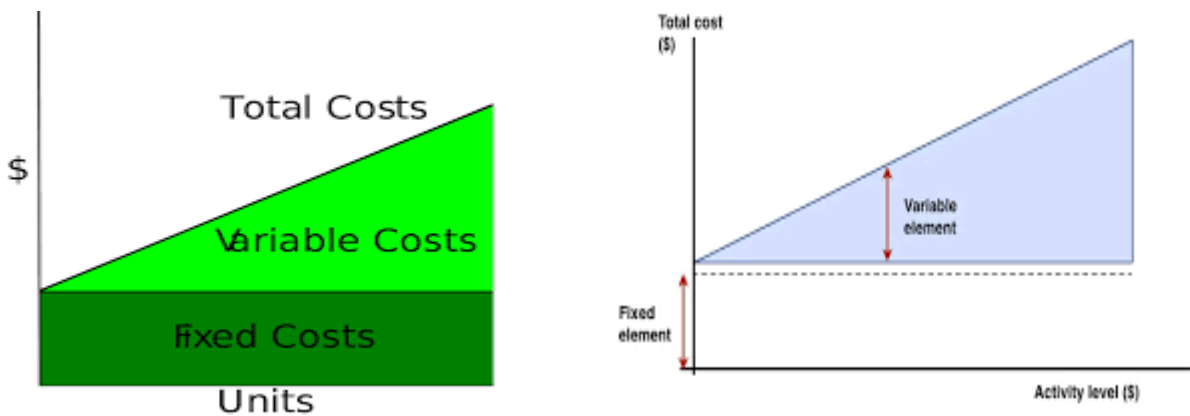
2.2.1 Variable and fixed costs

Costs behaviour means how costs will react or respond to changes in the level of the business activity. If for instance, the level of activity level rises and falls, costs can rise and fall as well, or remain constant for the period. Costs can be categorised as variable or fixed (Seal et al., 2015).

Variable costs are costs that vary in total in the direct proportion to changes in the level of activity. Fixed costs are a cost that remains constant in total regardless of the changes in activity (Seal et al., 2015).

Figure 2.1 below shows the difference between variable and fixed costs.

Figure 2.1: Cost Comparison



Source: *Management Accounting – Study Guide, 2016*

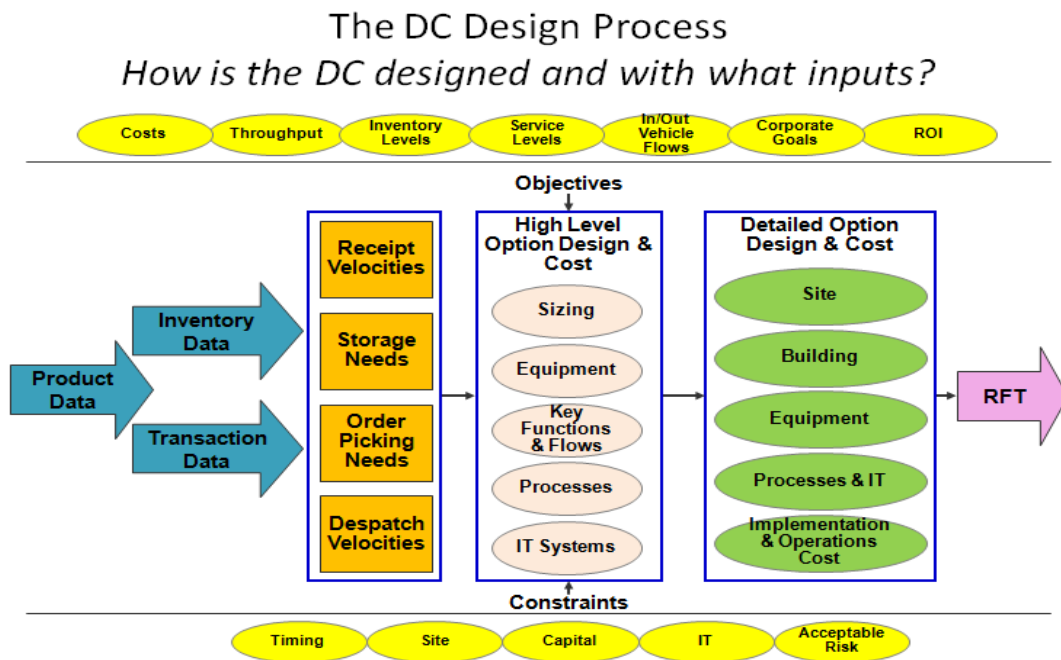
There are businesses that have a greater proportion of variable costs, and those businesses have lower risks. Businesses with more variable costs in lieu of fixed costs are less sceptical to sudden changes in sales volume. Variable costs rise and fall in a relationship with sales, which have a lower breakeven point then (McMahon, 2011).

For the research cost factors for a sales and distribution company, will have an impact on the organisation when a new retail store opening happens. Costs need to differentiate between fixed and variable so that it can be applied to the projected theory of profitability for an organisation.

2.2.2 Centralised distribution

Centralised distribution can be referred to move de-centralised or multi-centralised centres to one central distribution point (Benetar, 2015). Distribution costs are defined as costs incurred to deliver a product to the end user for an organisation. All the retailers have DCs across South Africa. If an organisation is accepted in their distribution centres, the retailers will deliver it to all the stores and will charge the organisation a percentage of the sales that were disseminated from their DC. If an organisation product is not accepted in the DCs, it should deliver the products to the individual store. The delivery to the individual store is known as Direct Store Deliveries (DSD). DSD actual rate is around 8%, and suppliers for retailers were prepared to give in the region between 4-6% of a distribution allowance to make it worth the while for retailers.

Figure 2.2: DC design process

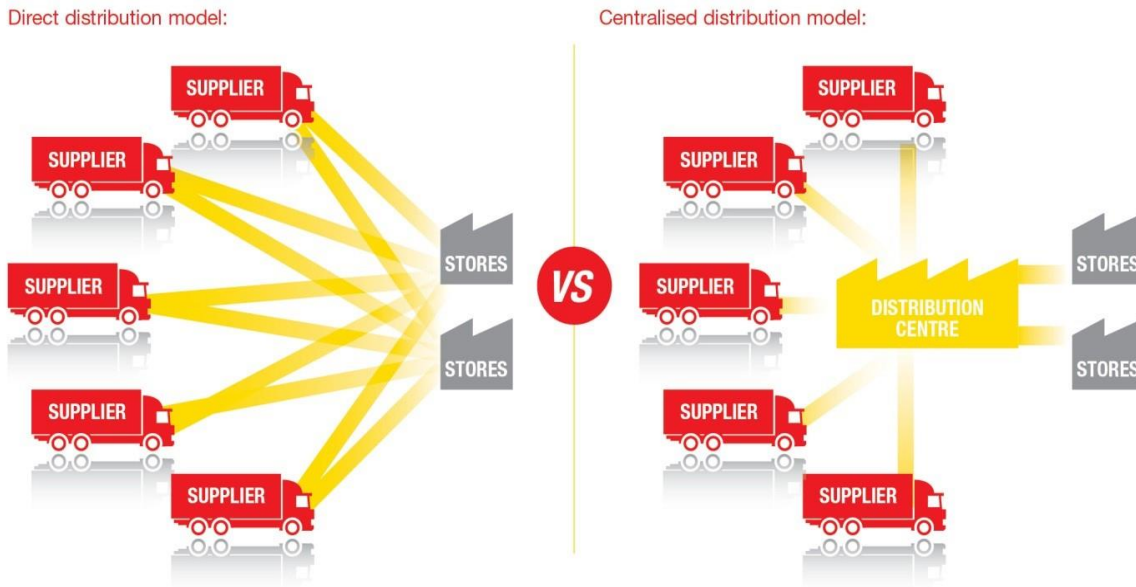


Source: Logistics Bureau, 2016

According to Stubbs (2011) retailers, for the past few years have had a massive strive toward central distribution centres. All the major retailers have their distribution centres in the hub of each province. The opening of centralised distribution happened to better compete with expected increases in supply chain efficiencies. On the cost side for retailers' factors such as the following played a big role:

- Reducing Inventory;
- Optimising transport;
- Providing better controls through more comprehensive management; and
- Better on-shelf availability.

Figure 2.3: DSD model vs DC Model



Source: Shoprite Holdings, 2016

In a business where margins are already close to the bone, cost management and innovative thinking are now very important to succeed. Through centralised distribution, it also means retailers have less congestion at stores back door. It is also great from a delivery point of view because suppliers have a single delivery point instead of multiple deliveries. For some suppliers, they would still want to go with the DSD route. This allows them flexibility on distribution models. The DC Model allows for reducing costs if the stock is managed correctly. Larger carriers have larger product offerings to retailers, but a lot of big suppliers are struggling to offer a level of customer service that is needed. Value-adds become very important in times like these where you can offer a variety of products to the retailers from the supplier point of view (Durham, 2013).

2.2.3 Remuneration costs

According to the Basic Conditions of Employment Act (No. 75 of 1997) from the Department of Labour remuneration are defined as any payment in money, made or owing to any person in return for that person working for any other person (SA, 2016). Furthermore, the merchandisers are governed through a minimum remuneration as per the Government Gazette that is published each year. Employers will have to pay the

prescribed minimum wage as per instructed in the Sectorial Determination for the Wholesale and Retail Sector.

Table 2.1: Merchandisers' Salaries

	Minimum wages for period 01/02/2017 - 31/01/2018				Minimum wages for period 01/02/2017 - 31/01/2018			
	Area A				Area B			
	Bergrivier, Breede Valley, Buffalo City, Cape Agulhas, Cederberg, City of Cape Town, City of Johannesburg Metropolitan Municipality, City of Tshwane, Drakenstein, Ekurhuleni, Emalahleni, Emfuleni, Ethekewini Metropolitan Unicity, Gamagara, George, Hibiscus Coast, Karoo Hoogland, Kgatelopele, //Khara Hais, Knysna, Kungwini, Kouga, Hessequa local authority, Lesedi, Makana, Mangaung, Matzikama, Metsimaholo, Middelburg (Mpumalanga), Midvaal, Mngeni, Mogale, Mosselbaai, Msunduzi, Mtubatuba, Nama Khoi, Nelson Mandela, Nokeng tsa Taemane, Oudtshoorn, Overstrand, Plettenbergbaai, Potchefstroom, Randfontein, Richtersveld, Saldanha Bay, Sol Plaatjie, Stellenbosch, Swartland, Swellendam, Theewaterskloof, Umdoni, uMhlathuze and Witzenberg				Metropolitan and local municipalities not listed in Area A.			
	Less than 27 hour a week	More than 27 hours per week			Less than 27 hour a week	More than 27 hours per week		
	R.p.h	R.p.h	R.p.w	R.p.m	R.p.h	R.p.h	R.p.w	R.p.m
Merchandisers	R 19.66	R 18.98	R 854.33	R 3,701.82	R 17.13	R 16.45	R 740.35	R 3,207.97

Source: Department of Labour, 1997

Remuneration costs in a sales and distribution entity are their biggest line expense. These sales and distribution companies' employ these following employees (a short description of their job specifications follow):

- Merchandisers – Packing of products from their suppliers on shelf and making sure sufficient products are in the stock room
- Sales Representatives – Taking orders at store level were they still can influence orders (Listed Retailers cannot be influenced and order per their system). Stocktake at store level
- Territory Supervisors – Outlining areas where they fulfil a role like the sales representatives.
- Regional Sales Managers – Working closely with their suppliers and making sure sales targets are achieved on a month-to-month basis.
- Order Clerks – Capturing of orders
- Office Staff – General work specifications.

According to the Government Gazette, merchandisers will have a 7-8% salary increase for the period 1 March 2016 – 28 February 2017 and to employ a sales representative it will cost an entity between R15,000 – R20,000 cost to the company to service those stores. This is excluding travel costs for an organisation.

Merchandisers for a sales and distribution company is mainly blue-collar workers, and their payroll is made up by most of the merchandisers. Merchandising is a very costly function in retail, especially if you consider the human capital element of merchandisers. When there are “out of stocks” in the retail store, it is mainly a blame game between retailers and suppliers; retailers blame their suppliers and merchandisers whereas, on the other hand, suppliers blame the retailer (Durham, 2013). According to Fore Good’s Leron Varsha merchandising should be managed by retailers where the turnover is not sufficient. On the other hand, at large stores, retailers do not have the expertise to merchandise the products correctly. The cost for merchandising is pegged at 4% of turnover (Durham, 2013).

If competitors of manufacturers have the same product that competes against each other for market share, they will not be using the same merchandising company. They view it as a conflict of interest and is afraid that one will get preferential treatment over the other. This makes it more challenging that if you are providing a service of merchandising, you cannot take on new business, even though it is difficult to give preferential treatment above the other. The reason for that is big retailers have a set outlet spacing, and you cannot control it.

South Africa has one of the highest official unemployment rates in the world, 25%, and is one of the unequal countries with a Gini coefficient of 0.69. Thirty-two percent (32%) of total income is received by the wealthy 4% in South Africa while 66% of households only receive 21% of the income. It is estimated that over half of people living in South Africa do so on an income of less than \$1.25 (R15.85) per day (Anon, 2015).

Local suppliers are struggling to maintain competitiveness against international rivals, and could be one of the following:

- Relative high local wages;
- Labour unrest; and
- Inflexible labour policies.

During 2011, average wages rose at about twice the inflation rate, and that proved challenging for suppliers and manufacturers (Fouche & Wilkinson, 2012).

The remuneration of staff can have a negative impact on an organisation if a new retail store opens and that specific new retail stores do not get significant growth from the products.

2.2.4 Trading costs

For a supplier such as from a sales and distribution company, they have cost to sell their product to the retailers. Sometimes these costs can add an extra burden to the consumers if a middle way is not found with suppliers and retailers and the consumers will feel the effect through price increases. These costs include the following:

- Retailers' price strategy;
- Confidential Rebate;
- Allowances (Distribution, Advertising and other); and
- Discounting.

- Retailers' price strategy

Retailers will have a price strategy when goods are purchased from suppliers. One of the strategies will be a markup on goods purchased. When a supplier wants to sell their products to the retailers where consumers can buy it from, the retailers will sell the products at a markup to cover the retailer's cost. Two key elements to understand the costs associated with pricing are that these elements are the cost of goods and amount of operating expense. Cost of goods includes shipping and warehousing whereas operating costs involve overheads, payroll, and rent.

The markup on costs can be calculated by adding a pre-set profit margin or percentage (Hudson, 2017).

This strategy is most common in the South African retail environment. The retail environment, however, uses more than one retail pricing strategy due to competition and that pricing is one of the central aspects in the retail sector (Competition Commission of South Africa, 2002).

- Confidential rebate

Confidential rebate is a discount that a supplier and retailer negotiate each year, and the rebates are based on a percentage of the sales each month. These confidential rebates are meant to cover the retailer's shelf space and listing fees just to name a few. Most retailers feel that the confidential rebates is a sound and ethical practice and cannot forgo these rebates because it is already built into their supply chain and operations. Confidential rebates can be as high as 15-18% and thus have a negative impact on a small supplier that want their goods to be sold to the consumer (FPMC, 2003). According to Harrilal the confidential rebates is used by some retailers to have more power and can be seen as exclusivity fees and are only for the privilege to have the manufacturer products in store (Harrilall, 2009).

- Allowance

Allowances include distribution, advertising and other such as data or swell allowances. These are based on a percentage of monthly sales and will, for instance, be used to do advertising in-store, or if products are in the retailers DC, they will then charge you a DC allowance to deliver it to the individual stores.

- Discounting

Discounting include settlement discount and discount that suppliers give retailers that are negotiated yearly between the parties. Settlement discount allows the retailers to pay early their monthly purchases of the supplier and because of that, the supplier gives them a discount on the total payable amount. These settlement discounts can be in the region between 2-3%. Normal discounting form part of the natural way of dealing with retailers.

Discounting can include when a product is at a special price to the consumer, the price variance between the normal selling price and the price that is on the shelf is treated as a discount. These discounts will be passed onto the supplier and have to come off their margins (Hudson, 2017).

2.2.5 Information Technology costs

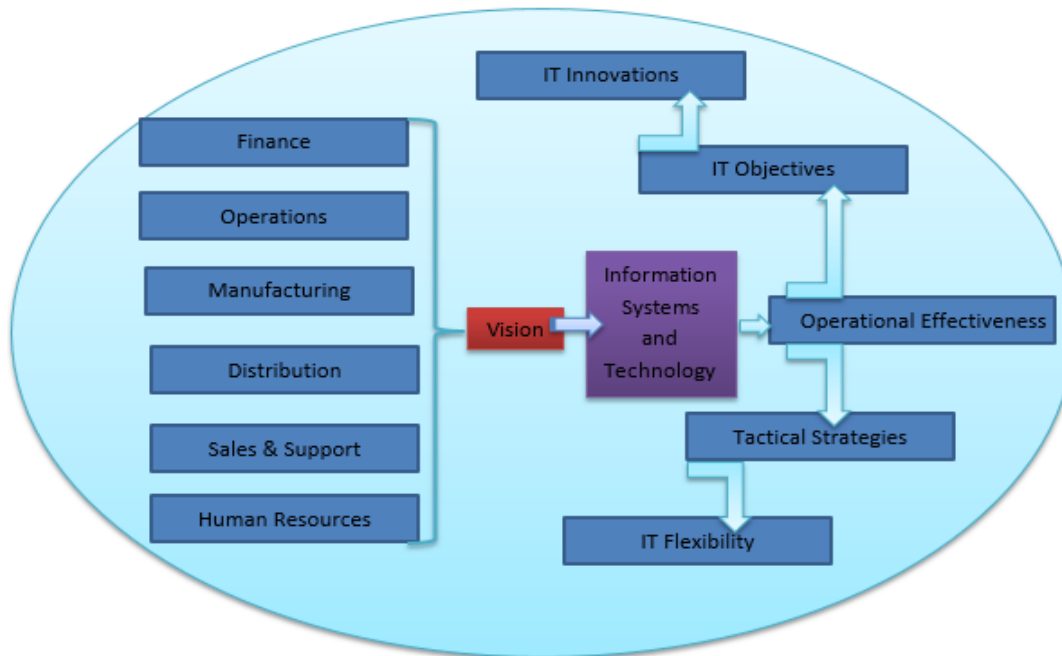
According to Daintith (2009), Information Technology (IT) is the study, design, development, application, implementation, support, or management of computer-based information systems. Information Technology can be anything relating to the operating environment within the retail sector. Information and technology are critical in today's highly competitive market.

There are multiple reasons in the retail environment why IT needs to be transformed:

- Increase company ability to enhance speed and flexibility;
- To collect and analyses customer data; and
- Work effectively.

IT can speed up processes and deliver cost benefits to the company, but the implementation and upkeeping are big costs for suppliers. The figure below shows what IT involve when it is planned correctly.

Figure 2.4: Information Technology Systems: Planning and Implementation



Source: Reworked information

2.3 SOUTH AFRICAN CONSUMERS

Living Standard Measures (LSM) is done by the South African Audience Research Foundation and is a unique means of segmenting the South African market. LSM data provides valuable insight into a consumer of South Africa. With the ever-growing population in South Africa, the retailers can target the LSM group for turnover growth (Corporate Retail Channel Report, 2016b).

LSM is a market segmentation tool that segments an individual or market, based on the status of socio-economic factors (De Jager, 2004). Living, according to the Corporate Retail Channel Report (2016b), indicates that there are the higher LSMs which are a growing population that allows the retailers for growth (Corporate Retail Channel Report, 2015). The South African Population is concentrated in the LSM 4-7 Groups. Table 2.2 below shows the breakdown per LSM group per province in South Africa.

Table 2.2: LSM per province in South Africa

	LSM 1 - 3	LSM 4 - 6	LSM 7 - 10	Contribution to population
Gauteng	2.10%	40.00%	57.90%	26.30%
KwaZulu-Natal	15.90%	54.00%	30.10%	18.80%
Eastern Cape	25.00%	51.60%	23.40%	12.10%
Western Cape	0.70%	36.00%	63.40%	11.80%
Limpopo	11.80%	79.50%	8.70%	9.60%
Mpumalanga	8.10%	60.60%	31.30%	7.60%
North West	11.00%	68.60%	20.40%	6.70%
Free State	5.90%	62.20%	31.90%	5.20%
Northern Cape	7.40%	58.00%	34.60%	2.10%

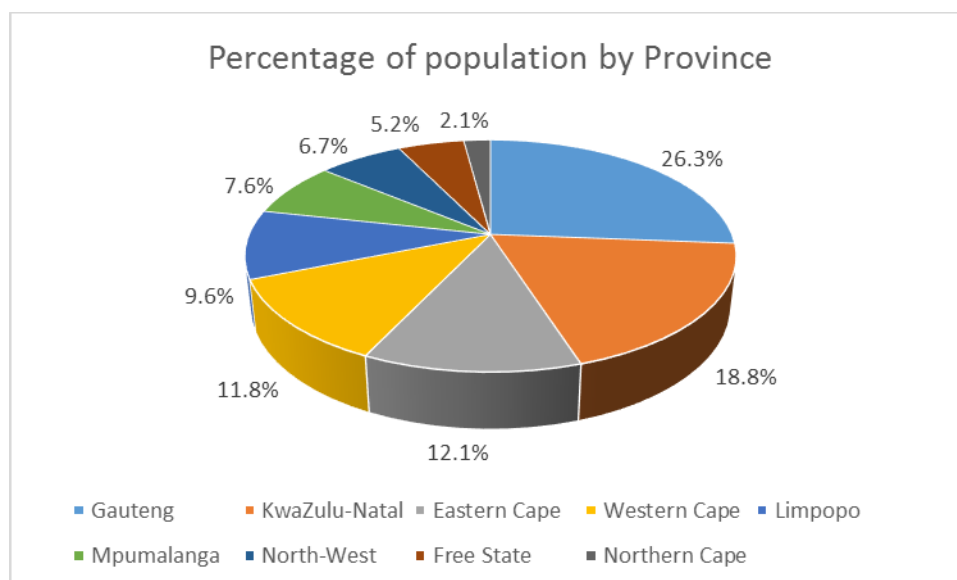
Source: SAARF AMPS 2015B

Gauteng, KwaZulu-Natal and the Eastern Cape have the highest population in South Africa, followed by the Western Cape. According to Corporate Channel Report, Gauteng and Western Cape are the richest provinces with the highest concentration of LSM 7 – 10. The retailers can be differentiated by LSM group for the purpose of this research to verify where the majority of consumers shop and of which race is the consumer population.

The Gauteng and Western Cape provinces are the only two with net increases in migration compared to the decrease from other provinces. The migration is mainly coming from LSM groups 1-5. These aspects create development for retail development but need to identify which markets have to be targeted. Research that was conducted shows the LSM 8 is showing rapid growth (21% per year since 2006) with a comparison to the lower end of the market (Prinsloo, 2016).

The different LSM groups have prompted local retailers to focus closely on how they want to position their brand against specific income brands. For the upper LSM groups is where there is a clear aspiration drive to increase spending. There is a constant migration from lower LSM scores to higher ones, with benefits that flow to the retailers (Fouche & Wilkinson, 2012).

Figure 2.5: Percentage of population by Province



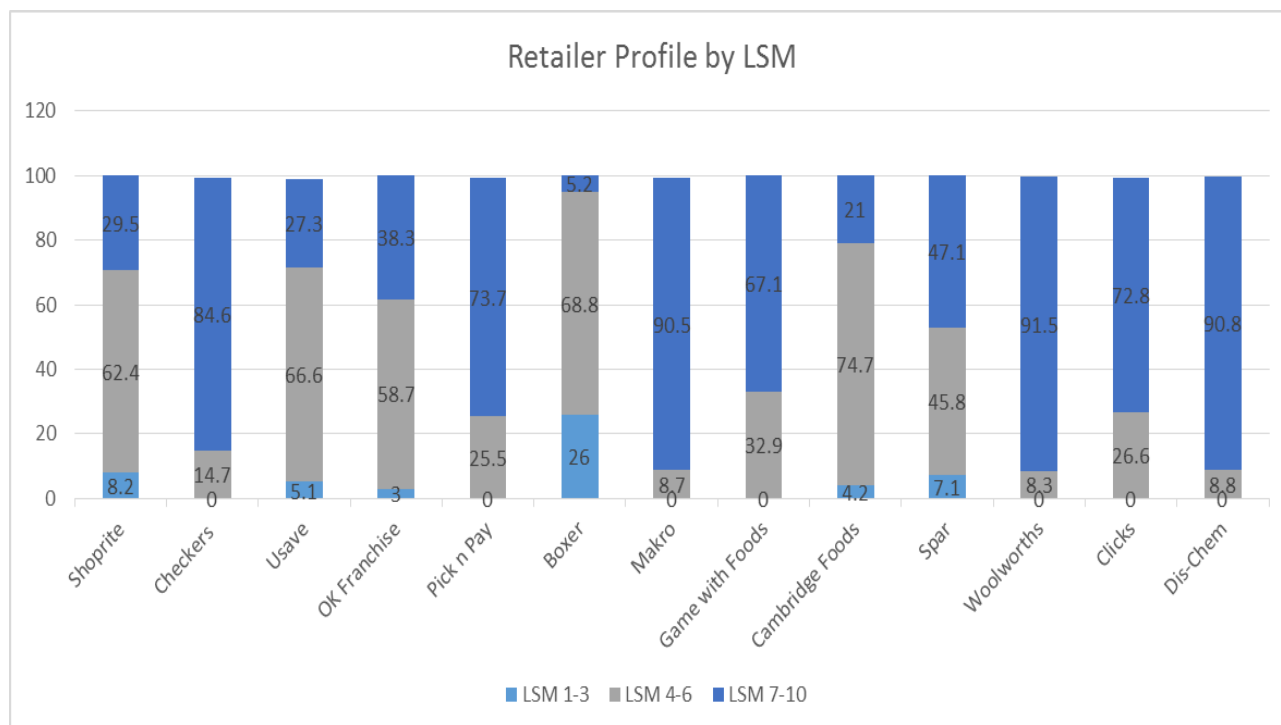
Source: SAARF AMPS 2015B

The growing middle-class population was assisted by receiving government grants. With increases in this group retailers target broad spectrum LSMs and can assist with growth for the retailers. Shoprite, Pick n Pay and Spar service a wide range of LSMs and holds the highest penetration across all LSM groups (Corporate Retail Channel Report, 2016b).

The following is evident from the LSM groups in 2016:

- South African population is concentrated in LSM 4 – 7 group;
- LSM 1 – 3 continue experiencing declines; and
- LSM 7 – 10 increasing 5-year trends is encouraging as it indicates that more consumers have money to spend at retailers.

Figure 2.6: Retailer profile by LSM

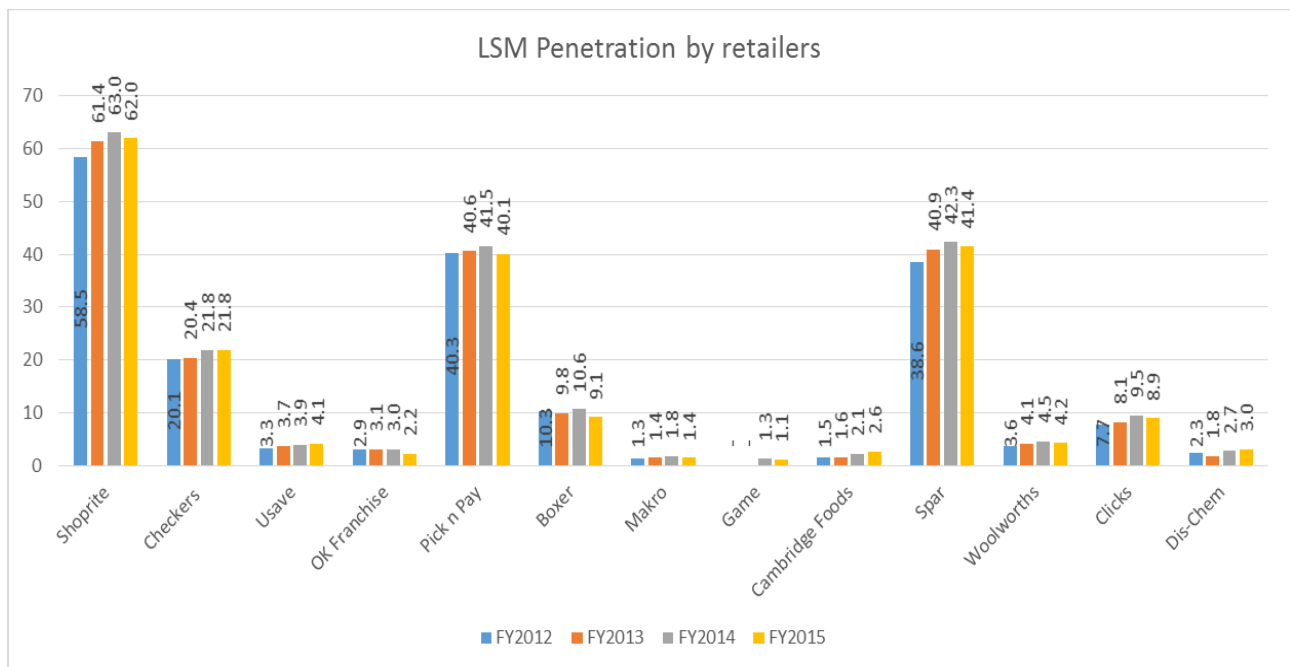


Source: Trade Intelligence, 2016b

Penetration refers to the percentage of shoppers in the total population who shop at each retailer. Shoprite Holdings is the biggest retailer in South Africa with the largest footprint of stores across various brands. Shoprite, with 62% penetration is concentrated in the LSM 4-6 representing 62.4% of the shoppers. Checkers is enjoying 21.8% of South Africa consumers and is concentrating for the LSM 7 and upwards.

Massmart caters for all LSM with their different chain of stores. Game has zero penetration in the LSM 1-3 but then Cambridge target middle and lower LSMs with almost 80% of their shoppers being LSM 6 and lower. Spar has the second highest penetration in the South African retail market with 46% of their consumers falling into the LSM 4-6 and 47% LSM 7 and higher. Pick n Pay has the third largest penetration of consumers, and the majority of their customers fall into the LSM 7-10. Woolworths' strategy is to cater for high earning consumers, and thus their majority of customers fall into LSM 9-10. Clicks focus on health and beauty and only consists of 8.9% penetration of 70% of the customers being at LSM 7-10 (Corporate Retail Channel Report, 2017).

Figure 2.7: LSM penetration by retailers



Source: Trade Intelligence, 2017

According to Pearson (2017) the current economic situation in South Africa, recently the technical recession, have consumers and retailers in a spin. Consumer spending will affect retailers and recently revealed that consumers are actively doing pre-shopping to see where they can save on costs. Furthermore, consumers are recently more focussing on broadsheet in newspapers and online advertising to compare retailers pricing for their benefit and to save on costs. In stores, consumers have decided to substitute some product or downscaling on product choice.

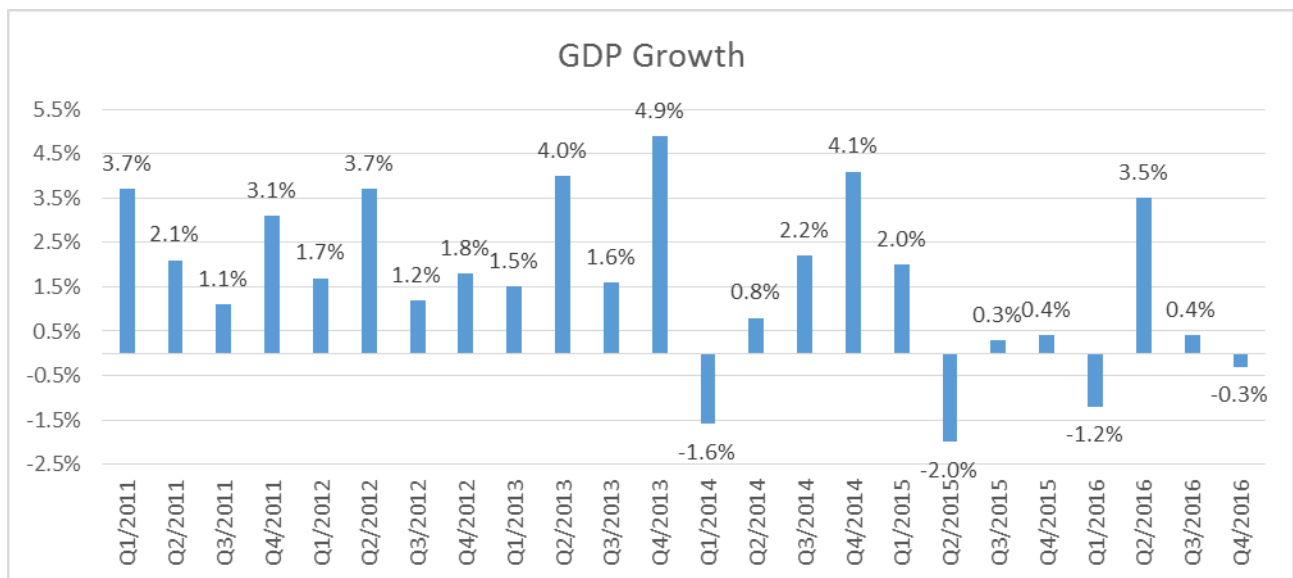
It is also revealed that best brands in the market are rather not purchased and consumers will rather choose cheaper brands. Many consumers are starting to buy brands they normally would not have considered to save some hard-earned money. Furthermore, consumers will still buy single units rather than bulk for immediate savings. This has to do that consumers can then buy another product they need with the money rather than to buy bulk and only have one item (Pearson, 2017).

Consumer shopping habits are shaping the retail environment in a new direction. It is evident that there is a proliferation of new malls all targeting the same market, but struggling to attract consumers to their stores (Anon, 2017). Over the past decade, the new retail stores added to the market grew at a much quicker pace than retail sales.

Until a year ago it was always the lower and middle class that was under strain, but lately one sees that the upper-income levels also are under pressure due to increase in taxes and electricity and eroding their disposable income (Muller, 2017b). These have a direct impact on overall sales in comparison to the number of new stores that are opening. The consumer just shifts their retailer due to pricing or location, but the overall sales do not show the desired growth.

The common measure to calculate a state of a nation's economy is the Gross Domestic Product (GDP). GDP is the total market value of all goods and services produced in a country in a specific time frame. It is measured against the previous period. If the GDP is higher in comparison to the previously measured time, then it shows that economy is doing better (Ashanti, 2012). GDP growth in 2014 was at 1.6% and slowing down in 2015 to 1.3% recorded. In the first quarter of 2016, the GDP was reported at -1.2% that had alarm bells sounding for a possible recession. Quarter 2 and 3 had a slight recovery of 3.5% and 0.3%. However, the last quarter of 2016 showed a -0.3% GDP again (Corporate Retail Channel Report, 2017).

Figure 2.8: GPD growth 2011-2016



Source: Trade Intelligence Economic Indicators Report, 2016

The unemployment rate also has a direct impact on suppliers and retailers of South Africa. This indicator is the most concerning for South Africa with the employment rate sitting at the end of 2016 at 26.5%. The employment rate in South Africa reached an eight-year high in quarter 4 of 2016 at 27.1%. If one considers the expanded definition of unemployment,

which includes discouraging workers no longer seeking employment, it will be at 35.6% for quarter 4 of 2016. Educational restrictions are one of the key concerns. Legislations and restrictive laws often make employers wary for the hiring of staff, but the most important factor is the economy of South Africa. The margins for all employers, including retailers and suppliers, is under threat and sometimes lead to staff retrenchments to save costs (Corporate Retail Channel Report, 2017).

2.4 RETAIL ENVIRONMENT

2.4.1 Types of retailers

The retail environment is very competitive in South Africa with a continuous price war between the specific retailers as well as prime store locations. The recent entry of Walmart in South Africa will even increase competition. As competition increases, they are being driven to introduce better and more effective supply chains.

The front-runner in the retail space is still the Shoprite group (PWC, 2012). As mentioned earlier the six biggest retailers in the formal trade have over 80% of the market. The six biggest retailers are Shoprite Group, Pick n Pay, Spar, Massmart, Clicks, and Woolworths.

Shoprite has 14 distinct brands across South Africa and is split up into five different segment units. These are:

- Shoprite (Shoprite, Usave, and Medirite);
- Checkers (Checkers and Checkers Hyper);
- Furniture (House and Home);
- Franchise (OK Foods and Grocer, Sentra and Friendly Supermarket); and
- Fast Food (Hungry Lion).

Shoprite's position as the number one retailer appears unassailable. They still grow significantly in difficult circumstances. One of their strategies is to develop further in Africa. However, the Shoprite group can expect some changes in the years to come due to a possible controlling stake that Steinhoff International wants to buy in Shoprite and retiring of key top-level management (Corporate Retail Channel Report, 2017). Shoprite has

continued to increase stores resulting in a growth of 26% on stores since the fiscal year 2012. Recently store growth has slowed down due to competition and focussing more on expanding in Africa.

The Total Group opened a net of 103 stores in South Africa in 2016 with a total footprint growth of 4.9% since 2015. These total of stores is across the Shoprite Group. The retail aspects of Shoprite will be focussed on. Shoprite Supermarkets opened 36 new stores in 2016; Checkers opened nine new stores, Pharmacy segment opened four stores, whereas Usave opened 16 new stores in South Africa for a total of 65 new stores in South Africa. For their planning of 2017, Shoprite is planning to open 52 new supermarkets in South Africa, and furthermore 23 franchise stores to give a total of 78 new stores in 2017 (Shoprite Holdings, 2016).

Pick n Pay group is managed through two divisions consisting of the South Africa division and Africa Division. Pick n Pay had a dominant consumer base in the early 2000 but was gradually overtaken by Shoprite. They were once the biggest retailer in South Africa. According to Laing, Pick n Pay in 2017 decided to offer severance pay to cut down on costs. It is estimated that around 3,500 people were put on early retirement or retrenchment. This was done to cut down on costs and making a positive impact on operating costs. People will be employed on tougher terms when new store openings incur (Laing, 2017). They have achieved reasonable results over the years but is in a three-part turnaround strategy by their CEO, Richard Basher. Pick n Pay to have its own corporate stores (52%) and franchise stores (48%) whereas Shoprite does not have any Franchise store that is trading under the name "Shoprite". The South Africa division of Pick n Pay consists of the following:

- Corporate (Pick n Pay Hypers and Supermarkets);
- Franchise (Pick n Pay Supermarkets); and
- Boxer (Boxer Supermarkets)

Pick n Pay group opened 168 new stores in fiscal 2016 with a growth of 4.4% in 2016 compared to a 2.5% in 2015. In the retail aspect of South Africa, Pick n Pay Corporate opened 11 new stores in 2016 and currently have 226 supermarkets and 20 Hypermarkets in South Africa. Pick n Pay franchise only opened one new store with a total of 289 Supermarkets. The majority of the store openings are for clothing and liquor. The Boxer supermarkets opened 24 new stores in 2016 (Pick n Pay Holding, 2016).

Spar Group is a South African listed entity and showed good growth from 2014, largely due to the 80% stake acquisition of BWG Group that enable them to operate across other countries. Spar retail consists of Spar (426 stores), Superspar (335 stores), Kwikspar (129 stores) and Save Mor (42 stores). Spar retail opened 19 new stores across South Africa for the fiscal year 2016. Spar does not give any indication on planned new stores (Spar Group Limited,2016).

Massmart is a South African-based, globally competitive regional management group. They are reliant on high volumes and is the second largest distributor of consumer brands in South Africa. Their focus and strategic direction, however, did not change, the continual improvement and growth of core business. Massmart is among the retailers the most programmatic, celebrating success quietly (Corporate Retail Channel Report, 2017). Massmart Group consists of the following group structure:

- Massdiscounters (Game);
- Masswarehouse (Makro);
- Massbuild (Builders Warehouse); and
- Masscash (Jumbo Wholesalers, CBW, Cambridge, and Rhino).

Massdiscounters opened two new stores in 2016. Game has 118 stores. Masswarehouse only opened one new store. The Masscash business that consists of wholesalers closed down four stores and opened six new stores. The Masscash group is planning to open 27 new stores in their retail and wholesale section, excluding their Massbuild business (Massmart Holding, 2016).

Clicks is a retail and healthcare specialist that has been listed on the JSE since 1996, in the Food and Drug Retailers section. Clicks group continues to hold its own, even in the difficult economic situation. This is mainly due to their loyal customer base. The new listing on the JSE from Dis-Chem will be led that Clicks feels some competitive pressure (Corporate Retail Channel Report, 2017). The Clicks group consist of Clicks retail and Clicks Distribution. Clicks retail and pharmacy stores whereas Clicks distribution is the business segment were United Pharmaceutical Distributors (UPD) distribution sits in their company.

Clicks group consist of 689 stores as at the fiscal year 2016. Clicks retail opened 25 new stores in 2016, a growth of 5.1%. The total number of stores for Clicks retail is 475 in South Africa. Clicks CEO, David Kneale, stated that their objective is to open between 20 – 25 stores each year. It is evident through their Capex budget for 2017 of R557 million for new stores and refurbishments (Clicks Group Ltd).

The Woolworths group has been listed on the JSE since 1997, and their strategic view is to cater to the high-end consumer. Woolworths is operating not only in South Africa but also in Australasia and sub-Sahara African countries. The Woolworths group consists of the following:

- Woolworths (Woolworths Clothing, Woolworths Food, and Woolworths Foodstop);
- Country Road (Country Road Clothing); and
- David Jones (David Jones clothing).

The Woolworths group opened a net of 58 stores in 2016. Woolworths Food, consisting of 30% of the stores, have 410 stores in total. New stores for the food section in the fiscal year 2016 were 10. Woolworths is planning to open 39 new stores in 2017, and Woolworths Food is planning for the next three years to increase their footprint by 20.1%. The food section of South Africa is planned to open eight new stores in 2017, 12 in 2018 and four in 2019 (Woolworths Holding Ltd).

2.4.2 Retail sales

The Bureau of Market Research (2014) shows that available data from household income growth is under pressure where household expenditure growth exceeds its income and have a direct impact on the growth of the retail trade sector of South Africa (2014:12). South Africa's economic growth, and more particularly, the retail trade sales have a direct link to international economic conditions that have an impact in South Africa. According to trading economics, the retail YoY were only up by 0.8 percent in July 2016 and whereas in October 2015 it was also only 4.0 percent up. This shows that retail sales growth do not increase in double digits with new retail store openings.

It is estimated that the corporate retail in South Africa was worth R430,9 billion in the fiscal year of 2015 which represents an increase of 13.1% in the market. In 2014 fiscal year, it increased by 9% to 2015 (Corporate Retail Channel Report, 2017).

The growth rate in the retail sector has been declining. Year on year sales growth, but yearly price increases from retailers account for half of the growth. There is a major change in the spending intentions amongst consumers. Food inflation has been on the rise and has a direct effect on spending of the consumers. The tightening of the consumer's belts has also been one of the factors for not achieving anticipated growth. There is a continuing battle with independent and branded retailers, but the independent retailers are losing ground on the major top six retailers (Durhman, 2011). The major retailers are also pushing for store openings in the township or lower geographical areas. Where a few years ago these consumers had to travel to go to big stores or buy from the informal trade (spaza shops) but lately the retailers are opening a store and getting more penetration from consumers.

According to Durham (2011), retailers are driving strategies more than ever to get the anticipated growth. They follow the following three strategies:

- Evolving Infrastructure

Retailers are seeking profit from infrastructure and move towards central distribution rather than DSD. Another venture they are starting to develop is the online shopping, even though it is still in the early days. Consumers, however, still want to go to shops and seek alternative pricing from different retailers.

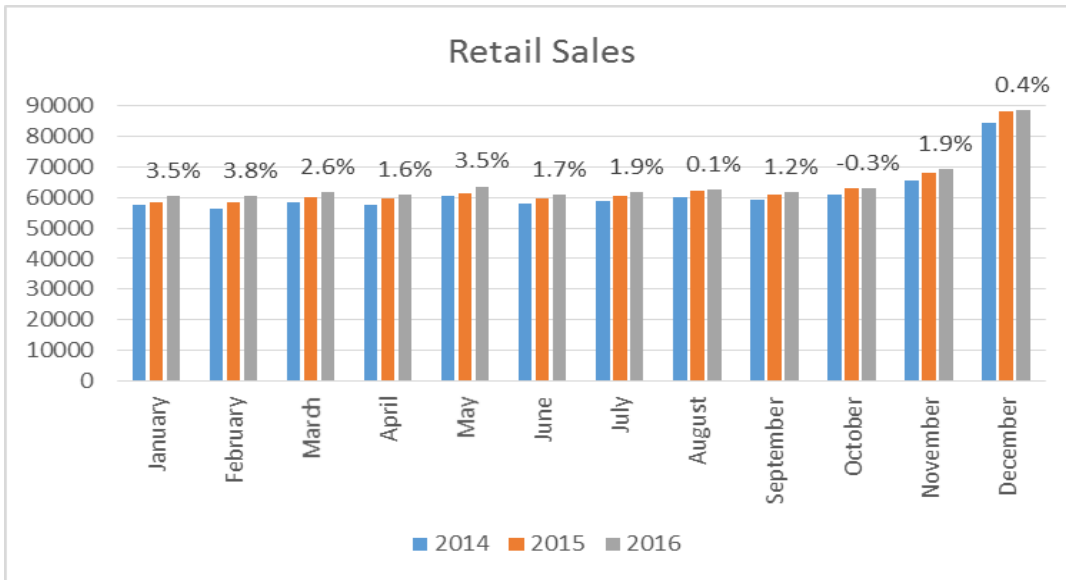
- Effective Consumer targeting

Retailers also realised that they need to cater for all consumers and not focus on one buying group. South Africa is just too diverse, ranging from culture, regional and religious lines.

- Customer loyalty

Retailers all launched new marketing platforms to get consumers to their stores. For example Pick n Pay launched smart shopper, Clicks have Clicks Clubcard where one can earn points, and Shoprite started first to get children motivated that their parents' shops at their stores to get Stickies. Loyalty programs will just become more important for retailers to attract consumers.

Figure 2.9: Retail Sales growth (2014-2016)



Source: Stats SA, 2017

The above figure shows that retailers' growth is not where they want it at. Together with the yearly price increases that retailers take, it is painting a bleak picture. The table below shows the real growth of retailers including new store openings.

Table 2.3: Real Growth Comparison for Retailers

Real Growth Comparison FY2016							
Retailer	Financial Period ending	Total Turnover Growth	Like-for-Like Growth	Growth from Net new stores	Internal inflation	Real Growth	Real Like-for-Like Growth
Shoprite Group	June 2016	14.4%	5.5%	8.9%	3.5%	10.9%	2.0%
Shoprite SA Supermarkets		10.9%	4.2%	6.7%	3.9%	7.0%	0.3%
Pick n Pay Group	Feb 2016	8.2%	3.8%	4.4%	3.1%	5.1%	0.7%
Pick n Pay South Africa		8.4%			5%	3.4%	
Spar Group Wholesale	Sep 2016	23.8%			6.2%	11.0%	
Spar Group Retail		8.2%	7.9%	0.3%	6.2%	2.0%	1.7%
Woolworths Group	June 2016	16.4%					
Woolworths Food		11.9%	5.7%	6.2%	6.7%	5.2%	-1.0%
Clicks Group	Aug 2016	9.5%					
Clicks Retail		12.8%	9.8%	3.0%	4.3%	8.5%	5.5%
Massmart Group	Dec 2016	7.7%	5.4%	2.3%	6.7%	1.0%	-1.3%
Massdiscounters		5.3%	1.5%	3.8%	4.8%	0.5%	-3.3%
Masscash		7.5%	7.9%	-0.4%	9.3%	-1.8%	-1.4%
Masswarehouse		11.0%	7.6%	3.4%	6.5%	4.5%	1.1%
Massbuild		5.6%	1.7%	3.9%	9.3%	-3.7%	-7.6%

Source: Trade Intelligence, respective retailers' financial results, 2016

The table above shows that the retailer's price increase through inflation was between 5-7% average and that total growth of new store openings were low thus give a real growth percentage for retailers between 0-2% on average. The real like-for-like growth shows that the suppliers will struggle to keep up with costs if retailers just keep on opening new stores that they have to service.

According to Ruddick like-for-like is when new stores that were added will not be included, meaning a retailer only measure stores that were open a year ago. Retailers are finding themselves in between two scenarios, change in consumer behaviour and expectations. There is a greater demand for value and a stronger fight for consumers (Ruddick, 2016).

This will assist the researcher to establish the overall growth of the retailers after taking into account the new retail store openings. This will further assist to determine if the cost factors can sustain the new retail store openings with the growth achieved for an organisation.

2.5 MARKET SHARE

According to Naidoo (2011), market share is the portion of total sales a company claims to have in a particular market over a specific period and relative to the industry size. The retailers are in a constant battle for market share. It is estimated that the market is about R220 billion worth. One of the main strategies for retailers to get the market share is to widen their store footprint in South Africa so that consumer can rather buy from them than their competitors.

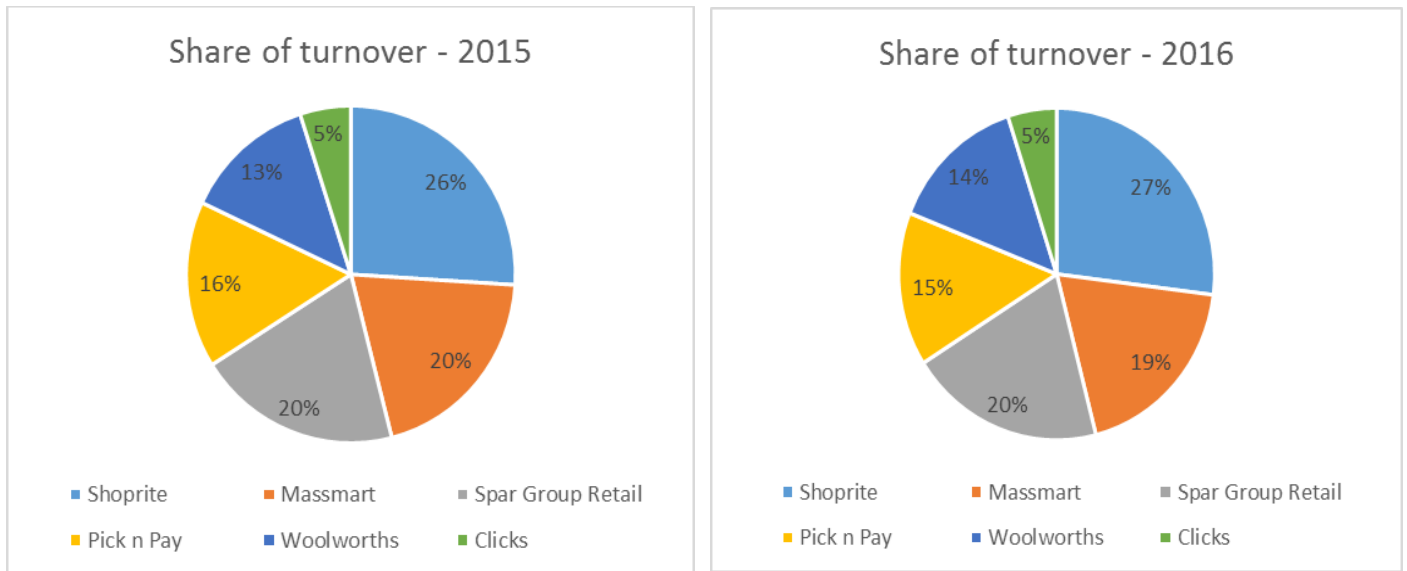
Value of the retail market is not determined by how big or small the percentage size is, but rather what exactly the market is. The market is defined as the area within the competitors are trying to get involved with or trying to lure consumers to their stores. The share is what it means in value or volume.

Market share is calculated by measuring the percentage of sales or percentage of volume (Ryder, 2016). Higher market share puts retailers at a competitive advantage. Companies with higher market share sometimes get better prices from suppliers because they have such a big market and consumers buying from them. If a retailer has a bigger market share, it can increase their buying power.

The degree of transparency of information in the retail sector of South Africa is to investigate the market share that retailers hold in the market. It is important that size and the percentage of market share that retailers hold is understood since competition in the retail sector plays such a big role in the determination of market fairness (De Jager, 2016).

For the past financial year's results, the current market share of the six big retailers can be seen in Figure 2.10 below.

Figure 2.10: Retailers' Market Share



Source: Respective retailers' financial results

Shoprite is the largest retailer in South Africa with a 27% market share in 2016. Spar market share is constant year-on-year; this has to do with their 7.9% increase in turnover in 2016. Massmart, which is the third biggest retailer in South Africa. Pick n Pay's market share declines each year. In 2014 it was 18% and decreased in 2015 to 16%. Their market share is currently at 15% of the total retail sector. Woolworths' market share increased from 13% to 14% in 2016 and largely due to the turnover growth of 15%. Clicks market share is only 5% constant between the two years (Corporate Retail Channel Report, 2017).

The market share of the retailers assisted in the research study to establish which objectives the retailers have and why is the drive so strong among the different retailers about its market share in the industry.

CHAPTER 3: PRESENTATION AND ANALYSIS OF RESULTS

3.1 INTRODUCTION

According to Bressand *et al.* (2014) retailers found it difficult to extract growth. In most markets, they are facing fierce competition, and opening new stores is no longer a safe way to grow the business. Like-for-like growth has been flat or declining in some cases. It is even more difficult for sales and distribution companies to still service these stores with continuing increase of new store openings. Sales are not sufficient to offset the companies' costs.

In this chapter the impact of new store openings has for a sales and distribution company was investigated. Before any conclusion can be reached on the profitability and feasibility of such a company, it is necessary to calculate different costs that are involved in servicing all these retailers with its increase in market share through store openings.

Furthermore, the data used is a company that is currently doing all these work for the retailers. Each element will be evaluated which include merchandising salaries, distribution fees, trading costs, and the overall impact of retailers buying behaviour.

The financial results of the six biggest retailers that have more than 80% of the retail market, will be analysed, and then "The Company" data of their annual sales will be evaluated and compared with the costs involved in servicing these stores.

3.2 METHOD OF RESEARCH

According to Bryman *et al.* (2014:100) research method is a technique to collect data. It may be in the form of various instruments which include questionnaires developed by the researcher and structured interviews. There are also other research methods to be used such as observation, interpretation of documents and secondary data.

Furthermore, case study design involves severe analyses of one or more cases which the researchers aim to obtain richer data (Bryman *et al.*, 2014:100). The difference of case studies, in comparison with other designs, is that the focus is on the understanding of a bounded situation or system. The following criteria were investigated in this study:

- The increase of retailers' footprint in South Africa – Each year retailers are opening new stores, and their strategic overview is to continue with this trend. South Africa has one of the highest numbers of retail space allocated in the world but also have the highest unemployment rate. It was investigated if store openings are for gaining market share or have a specific plan for consumers.
- Costs involved for companies servicing the retailers – The costs for companies servicing retailers, continue to increase year-on-year. Retailers have huge buying power over their suppliers and pass their yearly price increase on to the suppliers. With the new store, openings come at additional costs, but growth is not there to cover those costs. An investigation into which costs are involved and what impact it has for such entities gave answers.
- Retail growth – Retail is a challenging environment with a lot of hurdles. Consumer spending is under threat and with consumer disposable income decreasing due to living standards increasing, consumers do not spend what they used to with retailers. Retailers are seeking for growth from other ventures such as store openings. Retail growth is declining, and it was investigated how growth would be sustainable from rising costs.

This study will focus on secondary data that was collected from the six biggest retailers in South Africa as well as internal secondary data. Secondary data is used in this study for comparison of the criteria mentioned above.

3.2.1 Case study

The six retailers that have more than 80% of the retail market need analysis to highlight their growth over the periods. The six retailers are:

- Shoprite Limited;
- Pick n Pay Group Limited;
- Spar Group;
- Massmart Holdings Limited;
- Clicks Limited; and
- Woolworths.

Each retailer was evaluated, and the results of the growth and the total store counts are shown below.

3.2.2 Financial Overview and Store Counts

- Shoprite Holdings Limited

Shoprite group's turnover has increased for the year ending 30 June 2016 by 14.4%. The current retail environment is very challenging and with a GDP growth average of 0.7% for Shoprite's financial year end of 2016. Their growth in total retail sales was low at only 3.3% and with food sales even lower at 0.8% growth. The volatility in the currency also saw currency declining by the value of R12.30 to the dollar in June 2015 to R15.07 to the dollar in 2016 adding to the high inflation (Corporate Retail Channel Report, 2017). The average Consumer Price Index (CPI) for Shoprite internal food inflation was at 3.5% whereas the average food CPI was at 7.2% for 2016. The internal CPI inflation was the lowest that it has been since 2011. See figure below of the turnover of Shoprite per division.

Table 3.1: Turnover for Shoprite Group

R' m		
Division	2016	Increase % from 2015
	R 130,028	
SA Supermarkets	R 94,167	10.9%
Non SA Supermarkets	R 22,246	32.6%
Furniture	R 5,207	15.3%
Other Operating Segments	R 8,408	12.8%

Source: Shoprite Holdings Limited, 2016

Shoprite is continuing with its strategy to open new stores and thus resulting in store number growth of 26% since the 2012 financial year. Because Shoprite has the biggest market share of all retailers, it gives them a slight advantage when negotiating with suppliers. It gives them bargaining power. Although the store openings declined somewhat, Shoprite will continue to improve their quality of stores. They will also focus on expanding their footprint further in Africa. For this research, it will only focus on the stores in the formal retail sector of South Africa due to “The Company” that it will compare data with, which is also only in the formal retail sector.

Table 3.2: Shoprite Store numbers

Division	SA	Non SA	Total
Shoprite	439	138	577
Checkers	233	6	239
Usave	292	63	355
Pharmacy	130	38	168

Opened in 2016	Planned in 2017
36	52
9	0
16	23
4	0

Source: Shoprite Holdings Limited, 2016

- Pick n Pay Holdings Limited

Pick n Pay had a difficult year, especially with Shoprite taking market share away from them. Also, the consumers' disposable income shrunk because of the rise of household debt to an increase in petrol prices. The drought experienced in 2016 had a massive impact on Pick n Pay's results and placing further constraints on the consumer.

Against these challenges, they delivered their strongest turnover growth in six years with an 8.2% growth with a balanced approach with store openings that gave a 4.4% sales growth for year-end 28 February 2016. Pick n Pay like-for-like growth also improved to 3.8%. However, the GDP growth was only at 0.3% for Pick n Pay, and their internal CPI came out at 5%. However, Pick n Pay year on year growth for only their retail section were at 3.4% whereas food at 0.9%. See figure below of the turnover of Pick n Pay per division.

Table 3.3: Pick n Pay Turnover

	R' m	
	2016	Increase % from 2015
Group Turnover	R 72,446	
Pick n Pay South Africa	R 69,301	8.4%
Pick n Pay Africa	R 3,145	3.8%

Source: Pick n Pay Holdings Limited, 2016

Pick n Pay has a slightly different stance to Shoprite when it comes to store openings. They only opened 11 stores in 2016. Their big drive is at the Boxer chain that is part of the Pick n Pay group. It can be seen below in the total of 26 Boxer stores that opened in 2016. Pick n Pay is very wary of opening new stores due to its financial difficulties they have experienced the last few years. Pick n Pay do not give any indication how many stores they opened in 2017. This research focuses only on the stores in the formal retail sector of South Africa due to "The Company" that it will compare data with, and which is also only in the formal retail sector.

Table 3.4: Pick n Pay Store numbers

Division	SA	Non SA	Total	Opened in 2016
Pick n Pay Corporate	246	57	303	11
Supermarkets	226			11
Hypermarkets	20			0
Pick n Pay Franchise	232	57	289	1
Boxer	203	5	208	26

Source: Pick n Pay Holdings Limited, 2016

- Spar Group Limited

Spar retail delivered a good solid performance for the year ending 30 September 2016. The total growth was at 23.8% but the acquisition of BWG Group in 2015 assisting with the group growth. This is evident through the 32% of the total turnover from international currency. The average CPI over the financial period was 5.9%, and internal inflation of Spar was at 6.2%. This assisted with the total turnover growth as well. Furthermore, this shows that Spar caters for the higher earning consumer. Their year on year increase in retail trade sales was at 2.59% over the period, and their increase in food retail sales were 2.27%. See figure below of the turnover of Spar per division.

Table 3.5: Spar Turnover

	R' m	
Division	2016	Increase from 2015
Group Turnover	R 90,689	
Spar	R 49,615	8.9%
Build it	R 6,908	11.6%
Tops	R 5,177	0.12
BWG Group	R 23,100	
Spar Switzerland	R 5,889	

Source: Spar Group Limited, 2016

Spar does not have a corporate footprint. All the stores are franchise holders of the Spar Group. Spar retail section new store openings have not opened many stores in 2016. Their biggest drive was at Tops and Build It where they had opened 36 and 28 stores, respectively. The data of the “The Company” consists of stores in the formal retail sector of South Africa. Resultantly, only in the formal retail sector footprint is analysed.

Table 3.6: Spar Store numbers

Division	SA	Non SA	Total	Opened in 2016
Total Spar	890	127	1017	5
Superspar	335	14	349	6
Spar	426	65	491	1
Kwik Spar	129	48	177	-2

Source: Spar Group Limited, 2016

- Massmart Holdings

Massmart had a good result if one takes into account the retail difficulties that consumers are experiencing. Group turnover has increased by 7.7% for the year ending 31 December 2016. The real like-for-like growth experienced a decrease of 1.3%. GDP growth for Massmart during this period was at 0.3%. Their total retail growth for the year was low at 3.4%. The rand volatility against the currency fluctuations once again saw Massmart not finding the desired growth on turnover. Their Masscash and Massdiscounters segments, however, experienced better growth rate on margins of their sales growth rates. See figure below of the turnover of Massmart per division.

Table 3.7: Massmart Turnover

Division	R' m	
	2016	Increase from 2015
Group Turnover	R 91,249	
Massdiscounters	R 20,544	5.3%
Masswarehouse	R 26,270	11.0%
Massbuild	R 12,687	0.056
Masscash	R 31,748	7.5%

Source: Massmart Holdings, 2016

Massmart group have in total 412 stores excluding the franchise and buying groups. A strategic focal point for them is to expand their footprint in South Africa and opening stores where they can make some sustainable profit. One of their strategic viewpoints is in stores that do not give them the desired return on investment. Through 2016 it could be clearly see through stores that they have closed.

Their strategic view on expanding their footprint in South Africa can be seen through their planned store openings the 2017 financial year. They have been planning to open 23 new stores, and 20 of those comes from the franchise division. For this research it will only focus on the stores in the formal retail sector of South Africa due to “The Company” that it will compare data with, is also only in the formal retail sector. See below the retail footprint of stores that will be used in this research.

Table 3.8: Massmart Store Numbers

Division	SA	Non SA	Total	Stores opened in 2016	Stores planned in 2017
Game	118	23	141	2	2
Makro	20	0	20	1	1
Masscash	111	12	123	2	20

Source: Massmart Holdings, 2016

- Clicks Group Holdings

Clicks Group Limited presented good results for the year ending 31 August 2016. Their group’s turnover increased by 9.5% and showed the best results of all the six retailers when one takes into consideration the like-for-like growth. Their like-for-like growth was 5.5% for the year ending 2016. Clicks growth in total retail trade remains low at 2.7% with their retail food sales even lower at 1.29%. Clicks retail sales for the year is up by 12.8%. CPI for the period was at 5.8% and Clicks internal inflation were at 4.3%. It is interesting to note that their internal inflation in the fiscal year 2013 was 3.4% and three years later, at 4.3%. It is clear that they increased their internal inflation because their brand becomes more known, and their market share increases. This emphasises the dominance in the health and beauty retail section of South Africa. Clicks’ strength is their innovation and value ranging in retail and is observed through the market share they increased in some core categories. See figure below of the turnover of Clicks per division.

Table 3.9: Clicks turnover

Division	R' m	Increase from 2015
	2016	
Clicks Group	R 24,171	
Clicks	R 15,543	13.5%
Musica	R 906	1.2%
The Body Shop	R 191	0.145
UPD	R 11,055	6.1%
Intragroup	-R 3,524	0.136

Source: Clicks Group Limited, 2016

Clicks Group has a total 689 of stores. The Clicks retail division is 72% of the group store footprint. The Clicks group currently have 36 stores outside South Africa. Clicks want to continue their dominance, especially with Dis-Chem Limited growth, in the health and beauty retail sector of South Africa. Dis-Chem were listed on the JSE in 2016, and the competition between these two retailers will be massive in the next two years. They cater to the same consumer in South Africa and want to protect their market share. Clicks planned store openings in 2017 are between 20-25, and they will continue to open so many each year. In expanding their footprint, small pharmacies will close down due to consumers rather shopping at the bigger retailer. This research study only focuses on the stores in the formal retail sector of South Africa due to “The Company” that it will compare data with, and who is also only in the formal retail sector. See below the retail footprint of stores that were used in this research.

Table 3.10: Clicks Store Numbers

Division	SA	Non SA	Total
Clicks	475	36	511

Opened in 2016	Planned in 2017
25	25

Source: Clicks Group Limited, 2016

- Woolworths Holdings Limited

Woolworths’ dominance is a result of their LSM 8-10 targeting market. It is the high earning consumer, although for them lately the economic situation also changed their buying habits.

The Woolworths group sales increased by 15% for the year ending 30 June 2016. The total food segment increased by 11.6%. It is their fourth year that Woolworths achieved double-digit growth. Woolworths is maintaining their strategy on food sales to the upper LSMs of the market and their clothing, and general goods are still focused on the middle LSM. For the fiscal year ending 2016, the average CPI was at 7.20%. Woolworths' internal inflation was at 6.70% for the year. See figure below for the turnover of Woolworths per division.

Table 3.11: Woolworths Turnover

Division	R' m	Increase from 2015
	2016	
Woolworths Group	R 65,004	
Food	R 24,956	11.6%
Clothing & GM	R 13,701	9.6%
Logistics	R 515	0.16
Country Road	R 10,647	17.2%
David Jones	R 15,185	25.2%

Source: Woolworths Holdings Limited, 2016

Woolworths Group has a total of 410 stores. This includes their Africa Footprint of 21 stores. Woolworths, as like many other retailers, has a strategy to increase their footprint of the store in South Africa. They have detailed three-year planned store openings, for 2017, 2018 and 2019 fiscal year. Overall, they want to open 40 stores each year over the following three years. Woolworths opened ten new Foods stores in South Africa reflecting a 3.3% store growth and 9.3% trading space growth (Trade Intelligence, 2017). This study only focused on the stores in the formal retail sector in South Africa due to "The Company" that it will compare data with, and which is also in the formal retail sector. See below the retail footprint of stores that were used in this research.

Table 3.12: Woolworths Store Numbers

Division	SA	Non SA	Total
Food	389	21	410

Opened in 2016	Planned in 2017
10	8

Source: Woolworths Group Limited, 2016

3.3 COST TERMS

It is crucial that the reader of this study understand the costing terms that will be discussed in the case study application. The following costing abbreviations will be used and are important to note that all data (in Rand Value) in this case study is exclusive of VAT (Value added tax) and at Net Invoiced Price.

- **Net Invoiced Price** – Net Invoiced price is the price that is given to the supplier after agreed discount is given. Discount will be agreed annually and will differ from retailer to retailer. Thus, in short, the supplier will sell to the retailer at amount X and will then take the discount that is agreed beforehand, and the calculated price. The net invoice price is also being used by retailers to calculate their trading terms cost.
- **Sales and merchandising cost** – This is a cost that a supplier will pay a sales and distribution company to pack the shelves, making sure product labels are correct, negotiating better shelf space and make sure sufficient stock is at store level where the supplier products are listed at the retailers. Furthermore, the sales and distribution company will be capturing orders of their (supplier) products if an order is received from the retailers. The cost is based on a percentage of sales for a supplier's product.
- **Distribution cost** – This is a cost that will have to get paid to the logistics provider for the warehousing of stock and delivery to the retailers. It is common in the South African environment that suppliers use a logistics service provider for warehousing and delivery. Some blue-chip companies such as Aspen and GSK, use a logistic service provider to deliver their goods to retailers and warehousing of their stock. These logistic service providers get the best cost-effective solution and make use of economies of scale from the different manufacturers. All manufacturers will share a warehouse, and the logistics service provider will deliver one load to retailers with all the different manufactures products on. This cost has also calculated a percentage of sales that gets delivered by the logistics provider on behalf of the supplier to the retailers.

- **Trading costs** – These are costs that the retailers charge to the suppliers on a monthly basis. These costs are also based on a percentage of total sales that the retailers buy from the suppliers. It includes the following:
 - This is for distribution if the supplier's products are in the specific retailers DC;
 - Confidential discounts; and
 - Allowances.

3.4 ANALYSIS OF THE EFFECT OF STORE OPENINGS ON A COMPANY

Each cost element is evaluated separately, to analyse the effect that store openings have on a sales and distribution company, and a conclusion was reached for each different element to determine the effect it has on a company.

3.4.1 Remuneration costs

3.4.1.1 Evaluation of costs

As discussed earlier in the research, a sales and merchandising company will have to service their clients' products in the specific retailers. It is thus crucial to get economy of scale for such entities to make it profitable for them to continue in future.

Their majority of remuneration costs will be in employing merchandisers to pack the shelves. As noted in my literature study, an average fee charged for those services to their clients is around 4%. There are other costs such as office staff, order clerks, and sales representatives as well in such an organisation. All products on shelves in the retailers in South Africa are not done by themselves. They have merchandising companies that pack the shelves of their portfolio of clients' products. Inside the six biggest retail stores it is noticeable that many supplier companies are frequently busy to pack products on the shelf. These retailers do not do it themselves. Some smaller retailers, however, do it themselves.

Retailers get upset when products are not packed out on the shelf in their stores. They feel that they will lose customers if the stock is not packed out or if they run out of stock on specific lines. Merchandising companies will sometimes let their merchandisers roam between stores, especially if the stores are located in a shopping centre and are close by. It just depends on how big a specific store is and how busy a shopping centre is. It is a norm that merchandisers “will average five stores”. For this research, five stores per merchandiser were used.

A sales representative can get to more stores because they will have access to transport. In this study, an average of 15 stores was called upon.

See below table of the data collected for “The Company” and how much income is generated from stores.

Table 3.13: Analysis of Merchandising Cost

Retailer	Sales for full year			Growth Percentage	
	2016	2015	2014	2016	2015
Shoprite	R 113,324,446.35	R 114,627,319.52	R 96,595,218.11	-1.1%	18.7%
Pick n Pay	R 74,665,514.26	R 59,302,906.53	R 53,157,104.76	25.9%	11.6%
Spar	R 43,788,097.26	R 43,049,786.75	R 40,209,917.51	1.7%	7.1%
Massmart	R 14,327,443.28	R 16,908,298.73	R 14,641,620.11	-15.3%	15.5%
Clicks	R 209,447,102.47	R 192,912,630.39	R 155,025,224.02	8.6%	24.4%
Woolworths	R 10,327,900.80	R 6,981,482.86	R 6,123,352.15	47.9%	14.0%
	R 465,880,504.42	R 433,782,424.78	R 365,752,436.66	7.4%	18.6%
	Merchandising Fee @ 4%				
Retailer	2016	2015	2014		
Shoprite	R 4,532,977.85	R 4,585,092.78	R 3,863,808.72		
Pick n Pay	R 2,986,620.57	R 2,372,116.26	R 2,126,284.19		
Spar	R 1,751,523.89	R 1,721,991.47	R 1,608,396.70		
Massmart	R 573,097.73	R 676,331.95	R 585,664.80		
Clicks	R 8,377,884.10	R 7,716,505.22	R 6,201,008.96		
Woolworths	R 413,116.03	R 279,259.31	R 244,934.09		
	R 18,635,220.18	R 17,351,296.99	R 14,630,097.47		
	Overall store counts				
Retailer	2016	2015			
Shoprite	1094	1029			
Pick n Pay	681	643			
Spar	890	885			
Massmart	249	244			
Clicks	475	450			
Woolworths	389	379			

Retailer	Income per store	
	2016	2015
Shoprite	R 4,143.49	R 4,455.87
Pick n Pay	R 4,385.64	R 3,689.14
Spar	R 1,968.00	R 1,945.75
Massmart	R 2,301.60	R 2,771.85
Clicks	R 17,637.65	R 17,147.79
Woolworths	R 1,061.99	R 736.83

Source: "The Company"

If one evaluates the table above, it is evident that the income per store is low and that it is so for the full year. As discussed, the store opening is only specific to the retail aspect per retailers, and for this research, no attention was given to the entire store universe because that falls outside the retail aspect.

The six biggest retailers opened a total of 148 new stores in 2016. If only merchandisers were appointed to service these stores, it would cost a sales and distribution company R547,869.36 (148 store X R3701.82) a month if one works on the minimum wage for a merchandiser company. That would equal to R6,574,432.32 a year if one had to employ a merchandiser for each store. This does not even take into account any administrative staff or sales representatives. If you use the norm that merchandiser can cover on average five stores, it will then cost an entity R109,573.87 (148 store / 5 x R3701.82). That equals to R1,314,886.46 a year. This is a massive cost for an organisation to absorb to maintain the profit goals for the organisation.

As per Table 3.13 that sales for "The Company" to retailers only increased by 7.4% from 2016 to 2015. The sales growth is not sufficient to sustain the structures needed to maintain a good level of service to the stores. Also, the yearly growth in sales must sustain the current structure needed. As per Table 3.13, the total income for the year per store is R31,498.38. That equals to R2,624.86 per month per store of the retailers if all stores are calculated as a total. As discussed earlier and you work on that a merchandiser can cover on average of five stores and a sales representative on 15 stores average, the total average cost for the entire structure will be as follows:

- Merchandisers – R2,796,687.17 (3778 stores / 5 per merchandisers X R3,701.82) per month. Yearly cost is R33,560,246.02 (R2,796,687.17 X 12); and

- Sales Representatives – R5,037,333.33 (3778 stores / 15 per sales representative X R20,000 CTC) per month. Yearly cost will be at R60,448,000.00

As per Table 3.13, the total income from retailers will be R18,635,220.18. As noted, the economy of scale is very important to such an entity, and it needs to get more clients also to offset the cost of the structures. If for this study you estimate that you can get ten more clients' income of the size of "The Company", a sales and distribution company will earn approximately R186,352,201.77 (R18,635,220.18 X 10).

Compared to the total earnings with the two levels of cost structure, the two levels of remuneration structures are 50% of your total sales. This does not even take into account the higher level of remunerations structure such as management and the regional sales manager and as well as the administrative staff.

If the store openings continue, and as the study shows that 7.4% growth of the company sales from 2015 to 2016 and to consider that 148 stores opened, it is not viable to service these stores at a satisfactory level. Planned stores' openings for 2017 are opening 176 stores. To put the 176 stores into perspective, it will cost the organisation the following additional for 2017:

- Merchandisers monthly salary cost of R130,304.06 (176 stores/5 X R3701.82). That is R1,563,648.77 (R130,304.06 X12)
- Sales Representative monthly salary cost of R234,666.67 (176 stores/10 X R20,000 CTC). This is R2,816,000 a year.

This shows that it will cost the organisation an additional R4,379,648 in remuneration structures. This is not even considering your current salary staff annual salary increases. Your merchandiser's salary increases are governed by the published Government Gazette and are on average 2% above CPI. Thus, an additional 7% salary increase will be absorbed by the organisation. With retail trade sales increases only by 3%-5% annually (Trade Intelligence, 2017) and with the table in 3.13 the retail sales for "The Company" only increased by 7.4%. Thus, bringing the new store openings under scrutiny on how this cost will be absorbed.

3.4.1.2 Conclusion on remuneration structure

As explained above the costs of opening new stores have a direct impact on an organisation that services these stores. The yearly sales growth does not justify the cost that is involved with new store openings. If one evaluates the like-for-like growth as per Table 3.3, the growth is also not sustainable for retailers. Shoprite had like-for-like growth of 2% but increased their store openings with 65 new stores in 2016 and plans to open 75 more stores in 2017. Clicks had the best like-for-like growth of 5.5% and Massmart the worst of negative 1.3%.

It further shows that with retailers opening new stores, the consumer easily changes their preferred retailer. It also shows that the retailers are more aftermarket share than the total sales growth. The store openings have to slow down. Otherwise, the retail environment will only get tougher by the day.

3.5 DISTRIBUTION AND TRADING COSTS

3.5.1.1 Evaluation of costs

The distribution and trading cost will be evaluated together for a reason being that these costs go hand in hand together. This is because if retail stores open and one are not in the retailers DC, one will incur distribution cost to the DSD. On the other hand, if one is in the retailers DC, one will incur trading cost such as distribution allowance for the fact that the retailer delivers your stock to the individual store on one's behalf.

As mentioned earlier, a sales and distribution company will not always have their own warehousing and fleet but would rather use the logistic service provider to deliver their stock to the retailers to make use of economy of scale and to save on costs. The retailers are starting to become more aggressive with their efficiencies in the organisations. Especially in this time when consumers are under constraint and have a direct impact on them. According to Campbell-Young (2013), the changes in the retail space let the retailers focus more on the supply chain and cherry pick products that can be in their DC. Furthermore, Campbell-Young states that an international trend of companies is to focus on lines and suppliers that are most effective for their business. In previous years, they could absorb a certain amount of inefficiencies when it came to slow-moving products.

Due to the economic climate, this cannot be dealt with anymore and need to be ruthless when it comes to slow-moving product lines. Cherry picking can be defined as taking the best and leaving the rest.

Some retailers' cherry-pick the products of the sales and distribution companies that can go into their DC but will not accept slow moving product lines. Retailers, however, would still like to offer the slow-moving lines to their consumers, and a sales and distribution company would then have to deliver it to the individual stores.

This makes it difficult to a sales and distribution company because it can happen that some of their portfolio of products are in the retailers' DC and some not. It makes it difficult for these companies, not only because it is a disruption on their side when it comes to being effective and efficient but will increase their costs to get the product at the retailers.

Table 3.14: Sales per delivery method

Sales per Retailer per delivery Method						
Retailer	2016			2015		
	DC	DSD	Total	DC	DSD	Total
Shoprite	R 87,608,694	R 25,715,753	R 113,324,446	R 84,373,869	R 30,253,450	R 114,627,320
Pick n Pay	R 25,513,798	R 49,151,716	R 74,665,514	R 8,202,261	R 51,100,645	R 59,302,907
Spar	R 43,631,587	R 156,510	R 43,788,097	R 42,506,165	R 543,621	R 43,049,787
Massmart	R 9,061,750	R 5,265,693	R 14,327,443	R 4,204,464	R 12,703,835	R 16,908,299
Clicks	R 209,447,102	R 0	R 209,447,102	R 192,912,630	R 0	R 192,912,630
Woolworths	R 10,327,901	R 0	R 10,327,901	R 6,981,483	R 0	R 6,981,483
	R 385,590,833	R 80,289,672	R 465,880,504	R 339,180,873	R 94,601,552	R 433,782,425

Percentage of sales per delivery method						
Retailer	2016			2015		
	DC	DSD	Total	DC	DSD	Total
Shoprite	77.31%	22.69%	100.00%	73.61%	26.39%	100.00%
Pick n Pay	34.17%	65.83%	100.00%	13.83%	86.17%	100.00%
Spar	99.64%	0.36%	100.00%	98.74%	1.26%	100.00%
Massmart	63.25%	36.75%	100.00%	24.87%	75.13%	100.00%
Clicks	100.00%	0.00%	100.00%	100.00%	0.00%	100.00%
Woolworths	100.00%	0.00%	100.00%	100.00%	0.00%	100.00%

Source: "The Company"

Woolworths and Clicks are the only retailers that, if they list one of the products at their stores, it goes immediately into the DC. Spar is also fully DC operated, even though the data suggest that 1.26% and 0.36% in 2015 and 2016 respectively are still DSD.

Those percentages are due to out of stocks and asking the retailer to deliver directly. It is not of material value. The biggest issue that is currently prevailing is at Shoprite, Pick n Pay and Massmart. The major concern here is that the service provider charges you as a sales and distribution company a fee calculated on sales value, and so does the retailers. One can argue that a sales and distribution company has to negotiate a better rate from their service provider. The solution is that it can be negotiated if all retailers are in the DC and will only have certain deliveries to all the main provinces for the retailers. The following needs to be calculated to draw a compelling conclusion:

- Total DC Costs; and
- Total DSD Costs.

DC Costs

The data shows, in Table 3.13, that the total DC deliveries would be a value of R385,590,833. Retailers would charge the supplier a distribution fee for delivering stock for all of the individual stores for the specific retailer. The norm for a distribution allowance is in the region of 5%-6% on sales to the retailers. For this calculation, we will be using the average of 5.50%. The total costs retailers will charge suppliers is R21,207,496 ($R385,590,833 \times 5.50\%$) and on the sales, that went via DSD will not be charged. For a sales and distribution company, this will be equal to R1,767,291 per month. As discussed earlier a logistics service provider for the suppliers will also charge a percentage fee for warehousing the stock and delivering it to the retailer's DC centre.

Logistics service providers work on two costing structures normally. A percentage fee on sales or activity-based costing (ABC). Through experience in the industry, it is the best cost-effective way to work on a percentage fee on sales rather than activity-based costing. The reason for that is they do not have a dedicated facility for only one supplier but multiple suppliers, to get the economy of scale. The norm in the industry is also approximately 5%. For this study, 5% is set as the norm and used in the calculations.

Discussed above, the service provider will also charge you as a supplier 5% for deliveries to the retailer's DC. Thus, the cost involved will be R19,279,541 ($R385,590,833 \times 5.00\%$) average for the year and equals to R1,606,628 a month. For a sales and distribution company, for deliveries to the DC will in total cost them R40,487,037 ($R21,207,496 + R19,279,541$) a year for deliveries.

DSD Costs

For the DSD the suppliers will only have to pay their logistics service provider. The involved cost will, as described above, also be calculated at 5%. Thus, in total it will be R4,014,484 ($R80,289,672 \times 5.00\%$) for a year. The DSD is normally the biggest cost to the logistic service provider because it is the outlining areas in South Africa and does not get economy of scale from other suppliers in their warehouse. The reason for that is other suppliers could be in the DC in totality, or some products are and do not need to be delivering to those stores.

So, the total cost you pay to the logistics service provider will be R23,294,025 ($R19,279,541 + R4,014,484$) per year and the retailers a total of R21,207,496 as a DC allowance each year. The total distribution cost element for such a supplier will then be R44,501,521 ($R23,294,025 + R21,207,496$) a year and equals to 9.55% of the total sales.

3.5.1.2 Conclusion on distribution and trading costs

Because the retailers are cherry-picking on which products they want to take into the warehouse, this gives the suppliers an extra burden of costs. The costs will only increase, and suppliers can expect rate increases from their service provider if stores keep on opening in South Africa. If you had, for instance, some products in Shoprite that they do not want to take into their warehouse, your logistic service provider would have to deliver 65 new stores in and around South Africa. Where they work on a percentage of sales and the sales only increased overall by 7.4% as per "The Company" data, is not covering those costs for DSD deliveries.

Assume that all products of "The Company" were in the DC and would then have paid the retailers a total of R26,623,428 ($R465,880,504 \times 5.50\%$) and they can negotiate with the logistics service provider for a rate decrease to 3.84% to get to the total distribution cost of R44,501,521. It will be dependable to get the rate down to 3.84% due to the complexity and cost factor for them.

The supplier will have to become more like the retailers and be hard on the DC of all products intake. Retailers cannot have the bread buttered on both sides that they do not want to take the product into DC but still want it on offer to the consumers.

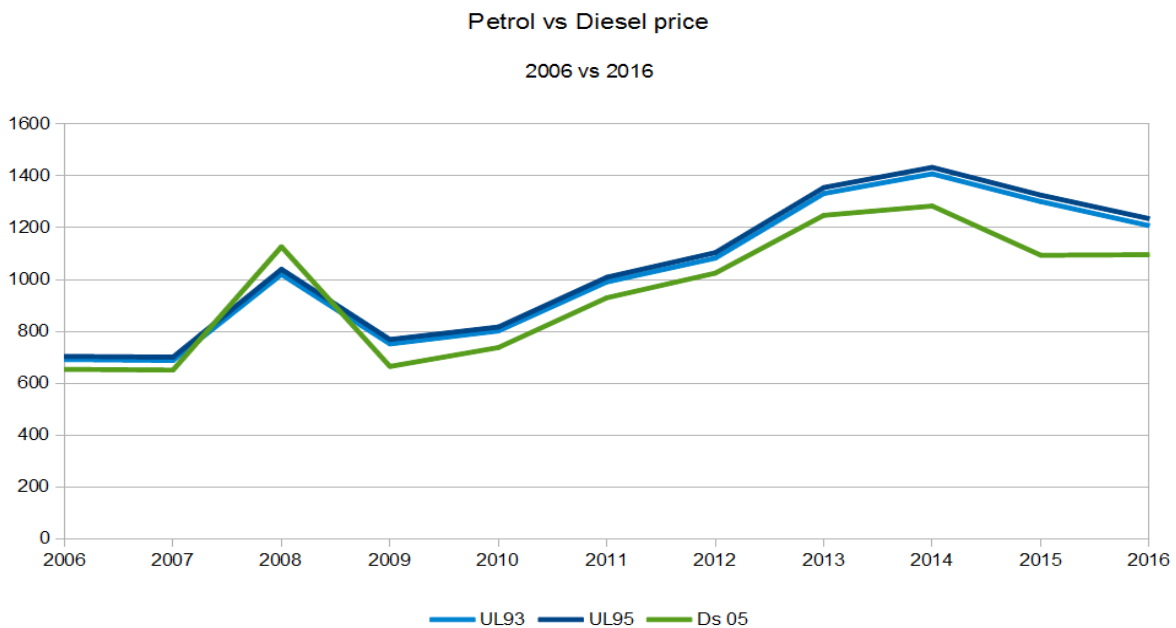
Sales and distribution companies will have to make a hard call and delist those products if retailers do not want to have all the products in their DC.

3.6 ADDITIONAL CONCERNS

3.6.1 Other costs that have an effect

There are many other costs that also affect the retail store openings. These costs are, for instance, travel costs and IT costs. As a sales and distribution company, one has to give one's sales representatives, territory managers and regional sales managers fuel cards to get to the stores that they need to service. This is extra costs that will have an impact on a company's profitability. Below figure just shows how much the price of petrol increased from 10 years ago. If one evaluated only from the end of 2015 when it closed on R12.40 for a litre of 95 unleaded premium (ULP) to R12.85 per litre of 95 ULP in 2016, it is a 4% increase in a year's time. From the 148 stores that opened in 2016, these stores have to be visited by the above staff and the extra costs of expense have to come from an increase in sales. It was evaluated throughout this study that retailers' sales growth did not assist with the additional cost that a company had to take on.

Figure 3.1: Fuel History of South Africa



Source: *Businesstech, 2016*

IT costs also have an impact if new stores open from retailers. The following is just some actions that are involved when new stores open:

- Setup of ordering platform, if franchise store, for example, EDI (Electronic Data Interchange), electronic download,
- Setup of new NDD (Nominated delivery date) and NOD (Nominated ordering date).
- The opening of an account and delivery details on the IT system.

IT cost must be calculated what it is for an organisation. It is sometimes difficult to calculate an organisation's return on investment for IT due to that fact that there is not always a direct income stream link. IT investment could be essential for a business's survival. There will always be new development when the new store opens in the retail environment. Technology is constantly changing. If changes are required from the retailer front, a sales and distribution company needs to adapt and keep up to date with all new developments.

3.7 CONCLUSION

The following conclusion can be derived from the evaluation above:

- The study shows that the overall retail market for the six major retailers were low and did not achieve the desired growth in sales. Shoprite achieves overall an average growth of 17.9%, Pick n Pay an average of 6.1%, Spar 10.8%, Massmart 7.4%, Clicks 9.8% and Woolworths an average of 15.9% sales growth in 2016. The study shows, however, that real like-for-like growth was very low. This is due to inflation and annual price increases. Growth from new stores was very low - between 6-8% - even if one takes into account only at new stores that were opened. Shoprite increased their store footprint from 2012 to 2016 by over 26%. The increase shows their dominance in the retail environment and the overall market share.
- Real like-for-like for retailers as mentioned earlier, were very low with some retailers reporting negative growth. This should be alarming for retailers if their real like-for-like growth is negative. Thus, meaning that although overall growth from new stores increased, some of the sales grew negatively in the year.

For a sales and distribution company which is reliant on sales, if real like-for-like growth is low, they will not be profitable due to increase from operating expenses such as salaries and other administrative costs. Real like-for-like growth for retailers for their financial year ending in 2016 was not as desirable. Shoprite came in 2.0%, Pick n Pay at 0.7%, Spar at 1.7%, Woolworths -1.0%, Clicks 5.5% and Massmart at -1.3%.

- The sales of the retailers of the data increased by 7.4% whereas the store footprints across South Africa increased by 148 stores. The costs to service these retailers only increase year by year, and the sales growth does not justify the store openings. Overall, retail sales were also low throughout the year, and consumers just switch to other retailers for convenience. The total size of the market does not increase; consumers just shift where they buy their monthly supplies from. Consumers do not buy more if more retail stores open. In fact, consumers are starting to cut down on costs due to their available disposable income.

For a sales and distribution companies, their biggest expense is their salary costs and distribution costs. With salary costs, the majority of the staff is merchandisers. The salaries of merchandisers are governed by Government and are on average 2% above CPI. For every store that is opening in South Africa, a merchandiser needs to be placed in the store or change which they are responsible for. Sales growth is not sufficient to make it profitable for a company if taking into account all these costs.

Sales and distribution companies need to find alternative measurements to be efficient and profitable. Sales and distribution companies will survive, but their profitable sustainability is not all guaranteed. They will in future have no other option but to acquire other smaller entities and try to get better economy of scale to cut down costs and to grow their entities. Other options could be to go into partnership with other similar entities. It is a known fact that retailers have significant power of manufacturers and that they control the industry. Shoprite has the biggest market share in the retail sector and can assume that they will also hold the strongest power. As a sales and distribution company, it cannot dictate to the retailers regarding store openings but should, however, be more effective when it gets planned.

Retailers also started a few years ago with their centralised distribution to be more effective and see a way to generate more profit for their organisations. It could be just a matter of time when they start the same when it comes to in-store merchandising. If the likes of Shoprite and Pick n Pay to want to do their own merchandising, it could spell the end of the road for sales and distribution companies function of merchandising. The retailers will just pass those costs onto the manufacturers and can generate some profit margins for the group. However, the basic principle for a successful enterprise is to stick to what you are good at. These retailers are good at providing a product of choice at a good quality to the consumers. Those functions will just be at more risk to the retailers and have a risk of not managing it correctly and be out of stock in stores. They will lose their consumers and alternatively more market share.

Now that it has been determined what the effect of store openings have on the profitability of a sales and distribution company, the overall effect can be determined.

CHAPTER 4: CONCLUSIONS AND RECOMMENDATIONS

4.1 INTRODUCTION

In the past decade, retailers have become more aggressive in the South Africa retail environment with expanding their footprint, with the opening of new stores. It is starting to become at the stage where it is more difficult for manufacturers or suppliers that service the retailers, to be profitable (refer to par. 3.4). Their increase in stores also does not give the desirable growth that is needed for the retailers itself, or the manufacturers. South Africa has the six highest largest number of shopping centres globally according to the South Africa Council of Shopping Centres (SACSC) (Chibaya, 2016). This fact is concerning when you take into consideration South Africa unemployment is one of the worst in the world, in the bottom ten.

The increase in store openings has to start slowing down due to consumers buying power and their available disposable income. This is not even starting mentioning the retailers increasing their costs. This expansion of their footprint is becoming more about market share than it is for providing a service to the consumer. Merchandising is becoming a nightmare for sales and distribution companies due to rising costs in the opening of new stores when the overall sales growth does not justify it. It cannot be profitable in the future if this trend is continuing.

The market share of retailers, especially the big six retailers, is becoming more and more and something has to give in. For manufacturers, such as sales and distribution companies, it is starting to become very expensive to get their products into the hands of consumers due to costs. Furthermore, the retailers are becoming more aggressive with front and back margins. In reality, the consumer will be negatively impacting on costs and will feel it with yearly inflations creeping up.

4.2 CONSEQUENCES OF THE INCREASE IN COSTS TO TRADE WITH RETAILERS

Based on the trend of store openings by South African retailers, it is evident that it will continue in the future and will have major consequences for a sales and distribution company. The store openings will continue due to the challenges between the retailers for market share. Sales growth is not increasing because consumers are struggling. Upon the literature study and analysis that were done in Chapter 2 and 3, we can see what negative effects it will have on a sales and distribution company.

4.2.1 New model for in-store merchandising

The effect that store openings have on the merchandising aspect is huge. Sales and distribution companies cannot continue to be profitable in the future. The economy of scale for such entities is crucial but is also starting to have a negative effect on the industry.

Competitors are starting to cut their rate when it is average around 4% for that aspect to around 2 – 3% just to gain new clients. This cannot be sustainable for the industry. In the past year alone, numerous similar entities closed their doors due to these circumstances. Competitors cannot compete due to those services at these kinds of rates for the reason that your initial investment for infrastructure when gaining a new client, cannot off-set at those rates. The fixed cost alone for salaries, especially pertaining merchandisers, will not be enough. The economy of scale is important but not at these kinds of ventures.

Confidentiality with manufacturing will also need to change. Manufacturers do not want to use a direct competitor merchandising company for the reason that they feel that the one will give preferential treatment to the other when it is competing for shelf space. Entities that provide a merchandising function is starting to close down, and there are just so many that can provide those services. Manufacturers need to find a middle ground so that merchandising companies can get better economy of scale through representing more similar competitors in the retail stores. This can then assist with the growing number of store openings that are planned in the next three years.

The current model in retail for food and the health and beauty section, the growing number of stores is not cost effective for the entities. It cannot sustain the current model. To annually employ an average of 148 merchandisers will cost R6,547,432 only on merchandisers, that will equal to the average of R163,685,800 (R6,547,432 divided by the average commission of 4%) year sales to only offset the merchandisers' fixed costs. This is not taking into account again of other employment titles or other operating expenses. The real like-for-like growth from retailers is also not where they want it to be. The retailers put a lot of faith into new store openings, but with new store openings, their other stores have decreased in sales. The assumption can be made that if a new store opens closer to consumers home, the consumer would rather go to the new store than the one he/she previously went to. So with new store openings, the existing stores are losing customers.

There is a risk that retailers can target to put their own merchandising infrastructure in place. Retailers are always looking ways to improve margins in their organisation, and they might think to have their own merchandising infrastructure, can generating more profit and can then pass the cost onto the suppliers. This would not be ideal for retailers due to the reason that they are not specialised in that field and would, in fact, have an extra burden for them to manage as an organisation. Centralisation of distribution was their main focus for the past few year and will continue with to be. This idea is maybe not for the near future but definitely at some point in the time.

4.2.2 Fully centralised distribution

As discussed in Chapter 3 retailers are sometimes cherry-picking which products of a manufacturer will go into DC or not. If for whatever reason it might have, not being included into DC, the retailer would normally still want it in their stores, but the manufacturer will have to deliver it to its individual store. Also, it was discussed that due to cost savings, manufacturers are using a logistic service provider to benefit from economy of scale to the warehouse and distribute a variety of manufactures products to retailers on behalf of them.

As per par. 3.5 stated that if your entity's products are partly into DC and other DSD, then it is not effective and is costing your organisation profit margins. This is probably the retailer's power in the sector that forces you to do it partly but is not effective.

Margin wise a sales and distribution company should then decide to delist the products that the retailers do not want to have in their DCs. This is not short-sighted, but it will be beneficial to an organisation to have everything into DC and then negotiate better rates with the logistics service provider. This will make your organisation a better lean operation and take complexity out which now is costing the organisation margin.

The sales that could be lost through delisting can be recovered through better operational strategies for the organisation. More focus can be channelled towards getting stock levels right and getting service deliveries close to 100% accuracy through taking out the complexity for partially being in the DC.

4.2.3 Reducing of trading costs with retailers

Cost of trading with retailers has starting to increase over the years. Even though with trading costs is it calculated on the percentage of sales to retailers. This is back margin. The front margin is where retailers take a markup on the products that you as a manufacturer sell to them. It is estimated that total margin for the retail environment is in the region of 40%. This is substantial, and for manufacturers, it is becoming more difficult to have the desired margins for their organisation. It can be assumed that due to the six biggest retailers' market share, they have the power that can afford you as a manufacturer to get your product to the consumer.

Retailers are also steadily increasing the back margins to offset their costs lately. This comes back to retailers not getting the desired sales growth out of the consumer and still increasing their footprint. Trading costs need to decrease to allow for a more competitive market and assisting consumers to buy more. Neither the retailer nor the manufacturer is willing to move on margins, and ultimately it is the consumer that feels the pain. It is, however, they that do not get growth out of their business.

Retail landscape needs to change in the future to make it viable. There is maybe an opportunity now for a competitor to go up against the big six retailers and to take market share away from them. Especially the online shopping will grow more in future and can be an adventure for manufacturers to look into. They will then ultimately be able to supply consumer's products without having back margins from retailers. According to Mahlaka (2016a), South Africa was poised to top 1% online sales of all retail sales in 2016, the first time since the inception of e-commerce. It does not say much, but when you look at figures, online shopping by customers is poised to grow to R47 billion in 2017 from R28.8 billion during 2015 (Mahlaka, 2016b).

Smith (2017) reported that during 2016 online sales grew to R37.1 billion. In an interview conducted with customers, online spending is budgeted to continue with respondents saying they will increase their online spending in the next 12 months, citing the convenience of shopping online, planning to save more money and changes in disposable income as the reasons for the expected increase (Smith, 2017). Some of the savings can be invested in to cover costs related to the delivery of goods to the consumer's doorstep.

4.3 OBJECTIVES

The objectives of this study consisted of a primary and some secondary objectives.

The primary objective was to determine the cost factors that have an effect on the profitability for a sales and distribution company in the retail sector of South Africa due to the increase in retail stores that needs to be serviced.

Secondary objectives were to investigate:

- The market share of the six biggest retailers in South Africa; and to
- Determine which factors have an impact when a new store opening incurs and as such:
 - New store openings do not have sufficient growth in sales to be viable for operating costs;

- Total universe sales growth of retailers do not increase with new retail store openings, consumers only spend at stores closer to their home or work or switch to other retailers; and
- Salary costs of field workers in the retail environment.

The study concluded that the new store's openings are not viable for a sales and distribution company. The costs that are involved in servicing the retailers' new store openings are just increasing and cannot be sustainable. This study further concluded that retailers show minimal growth and worrying real like-for-like growth that shows that store openings cannot continue. Store openings will continue in future and retailers have aggressive roll out strategies in place. This study shows the competition between the six biggest retailers is about market share. To be the first movers, retailers rely on overall sales growth with the expansion of their footprint, but the current store structure of specific retail group sales is decreasing and cannot be sustainable.

Profitability for a sales and distribution company make an organisation vulnerable in the current retail environment. It is clear that the retail environment in the future will be challenging and will have a major overhaul coming up to withstand the consumers that are struggling and have less disposable income. It is suggested that further studies need to be conducted in the overall retail market with other sales and distribution companies' data to confirm the assumptions made in this study.

4.4 RESEARCH RECOMMENDATIONS

- This study only focused on retailers that are in the FMCG as well as the health and beauty sector. Further studies should be conducted on the entire retail sector to determine the overall effect.
- This study was done with data from the six biggest retailers in South Africa, namely, Shoprite, Pick n Pay, Spar, Massmart, Woolworths, and Clicks. A further study should be conducted in the overall space that includes other retailers such as Dis-Chem, Wholesalers, Pharmacy Wholesalers and Tier 2 retailers.

- This study was done using sales data from “The Company”. “The Company” is currently trading with the six biggest retailers and has been over 20 years in the industry. Other similar entities should be analysed further to see if store openings have a similar effect on their profitability and future existence.
- The effect what consumer idea is regarding the expansion of store openings is worthy of investigation. The study should be conducted to see if a consumer will shop more if a store is located closer to the one they normally shop or does whether or not it has an effect. This will give better insight from a consumer’s point of view.
- The effect that store openings have on other smaller retailers. The study should be conducted what effect it has when the six biggest retailers expand their footprint and how many smaller retailers cannot continue to compete against the big six. This will give an insight on how many have to close their doors and what happened to those consumers.
- The effect on what costing can be saved if the confidentiality between manufacturers are letting go so that they can merchandise two similar products that compete with one another other. This will show the effect what economy of scale can do.
- The effect of health and beauty retailers such as Clicks and Dis-Chem have on smaller pharmacies. Clicks and Dis-Chem offer a variety of products, and not only cater on health but also beauty. Lately, it is also going into the groceries section. The smaller pharmacy will be forced to close and can be seen lately with all corner pharmacies the past few years that have been closing.

4.5 CONCLUSION

The retail environment is a challenging sector and is dependable on numerous factors. The economic conditions and future growth of South Africa are also not looking promising which have a direct impact on consumer disposable income. Consumers do not have the same disposable income as what they had previously, and that has a direct impact on retail sales. Retailers want to generate sales growth out of store openings, but this has a direct impact on sales and distribution companies. There are many factors involved when retail stores open. Retailers force such entities to increase their costs in their organisations through the fact that they need to service these stores.

If it is not profitable anymore for such entities. Growth in sales is the most important future factor for retailers, and their growth is not where it should be.

Real like-for-like growth is small growth digits and in some cases negative. Store openings are still going to increase from a retailers' point of view but are about market share. Sales and distribution companies cannot stay afloat if this continues into the future. Unfortunately, the only suggestion is that retailers need to evaluate their strategies for new store openings or sales and distribution companies need to look into more diversification of their services to be able to continue in the future. With this trend continuing, you will see more companies closing down.

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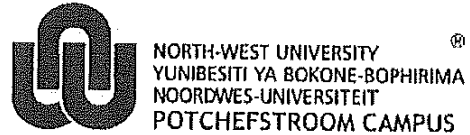
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APPENDICES

Appendix A: Declaration



SOLEMN DECLARATION AND PERMISSION TO SUBMIT

1. Solemn declaration by student

I,

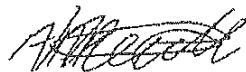
declare herewith that the mini-dissertation entitled,

which I herewith submit to the North-West University, Potchefstroom Campus, in compliance with the requirements set for the

degree is my own work, has been language-edited in accordance with the requirements and has not already been submitted to any other university.

I understand and accept that the copies that are submitted for examination become the property of the University.

Signature of student:



University number:

Signed at in this day of 2017 .

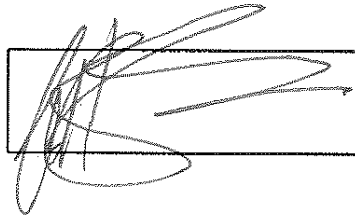
PLEASE NOTE: If a thesis/dissertation/mini-dissertation/article of a student is submitted after the deadline for submission, the period available for examination is limited. No guarantee can, therefore, be given that (should the examiners' reports be positive) the degree will be conferred at the next applicable graduation ceremony. It may also imply that the student would have to re-register for the following academic year.

2. Solemn declaration and permission to submit by supervisor/promoter

The undersigned declares:

- The student is hereby granted permission to submit his mini-dissertation: **YES/NO**
- That the student's work has been tested by me for plagiarism (for example by TurnItIn) and a satisfactory report has been obtained: **YES/NO**

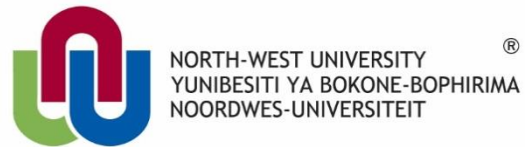
Signature/Supervisor/Promoter:



Original details: Marijke Ackema\10512187) C:\Users\10512187\Desktop\SOLEMN DECLARATION AND PERMISSION TO SUBMIT.docx
26 April 2017

File reference: 7.1.11.3.2/3

Appendix B: Ethical Clearance



13028073

BREEDT, ADP MR

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North-West University

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South Africa 2520

Prof CJ Botha

Tel: (018) 299 1672

Email: christoff.botha@nwu.ac.za

16 March 2017

ETHICAL CLEARANCE

This letter serves to confirm that the research project of **BREEDT, ADP** has undergone ethical review. The proposal was presented at a Faculty Research Meeting and accepted. The Faculty Research Meeting assigned the project number **EMSPBS17/03/06-01/23**. This acceptance deems the proposed research as being of minimal risk, granted that all requirements of anonymity, confidentiality, and informed consent are met. This letter should form part of your dissertation manuscript submitted for examination purposes.

Yours sincerely

A handwritten signature in black ink, appearing to read 'CJ Botha'.

Prof CJ Botha

Manager: Research - NWU Potchefstroom Business School

Appendix C: Editor's letter



Dynamic Language &
Translation Specialists

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CC No: 1995/017794/23

Tuesday, 24 October 2017

To whom it may concern,

Re: Letter of confirmation of language editing

The dissertation **Determining the business impact of retail store openings on a sales and distribution company** by ADP Breedt (13028073) was language and technically edited. The referencing and sources were checked as per NWU referencing guidelines. Final corrections remain the responsibility of the author.

Antoinette Bisschoff

Officially approved language editor of the NWU since 1998
Member of SA Translators Institute (no. 100181)

Precision ... to the last letter