

ALDI IN AUSTRALIA: WHAT WILL BE THE IMPACT?

May 2000

Aldi will become a small but significant player in the Australian market

OVERVIEW

- I. Aldi is the world's lowest cost grocery retailer**
- II. The United Kingdom provides an excellent model for the development of Aldi in Australia**
- III. The arrival of Aldi in Australia will have a focused impact, felt mostly on key line pricing and by Franklins**

I. Aldi is the world's lowest cost grocery retailer

- **Ia. Aldi acts as a category killer in core grocery lines**
- **Ib. Aldi has a low-cost logistics and operational system that works on a 12% gross margin**
- **Ic. Privately owned Aldi has a long investment horizon and plenty of patient capital**
- **Id. There are few threats to Aldi or the limited assortment store. Aldi is immune to competition, even from WalMart**

Ia. Aldi acts as a category killer in core grocery lines

- **Aldi is a limited assortment discount grocery store, a format characterized by a high turnover on a narrow range of grocery items in a small space**
- **The main appeal of limited assortment stores is low prices**
- **Packaged grocery accounts for almost 50% of a German Aldi store's turnover and 50% of an American store's SKU mix**
- **In Germany, over 70% of German households shop at Aldi, mostly for basic staples**

Aldi is a limited assortment discount grocery store...

TYPES OF DISCOUNT FORMATS

<i>Format</i>	<i># of Items</i>	<i>Key Points</i>	<i>Examples</i>
Limited Assortment	600-1000	Tightly controlled selection Focus on packaged groceries Emphasis on low costs 10-20% cheaper	Aldi, Netto, Lidl, Norma, Save-A-Lot
Discount Supermarket	1000-3000	More flexible product selection More fresh, chilled and frozen 5-10% cheaper	Kwik-Save, Plus, Penny
Extended Range Discount	3000+	Full product selection Discount perception	Franklins No Frills, Food Giant, Colruyt Le Clerc, Intermarche,

...a format characterized by a high turnover on a narrow range of grocery items in a small space

U.S. STORE FORMAT DEFINITIONS

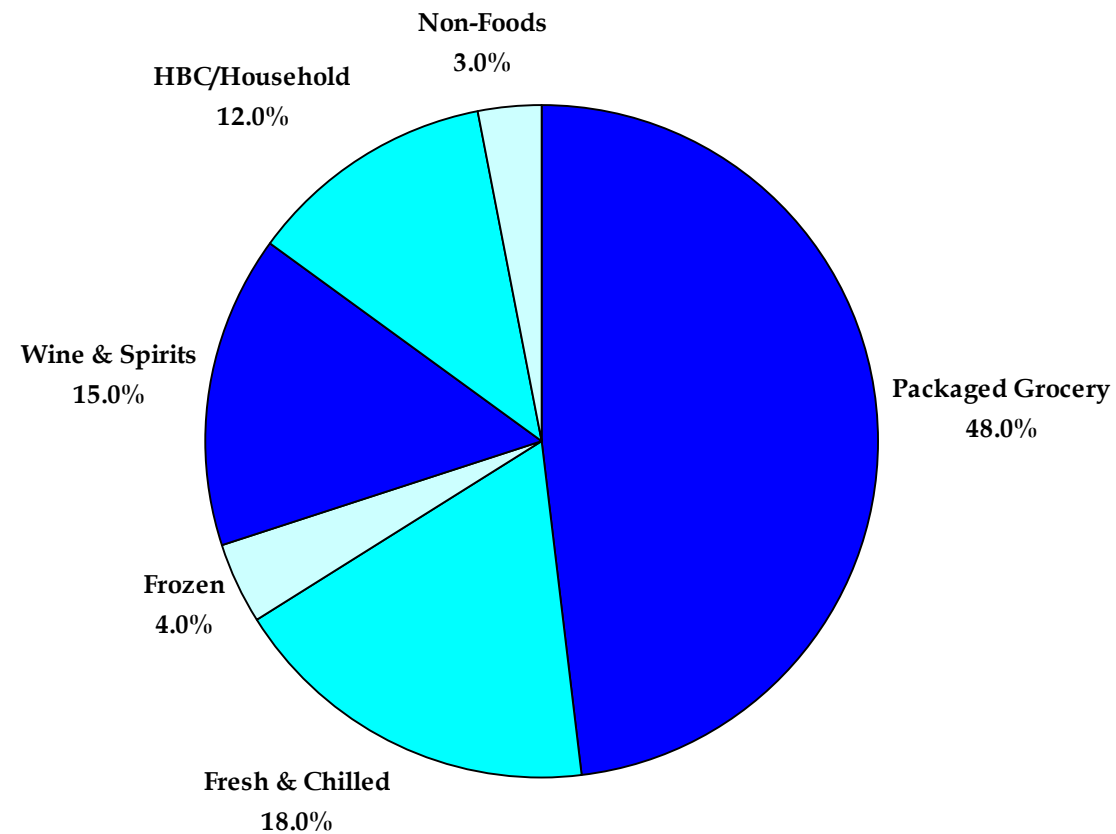
<i>Format</i>	<i>Total Area (sqft.)</i>	<i>Weekly Sales (US\$)</i>	<i>Number of Items</i>	<i>Weekly Sales per sqft.</i>	<i>Weekly Sales per item</i>	<i>GM/HBA/ Non-Foods % of Sales</i>
Conventional Supermarket	22,500	\$141,500	15,000	\$6.29	\$9.43	8%
Superstore	41,500	\$297,500	23,000	\$7.17	\$12.93	13%
Food/Drug Combo	53,500	\$385,000	29,000	\$7.20	\$13.28	18%
Wholesale Club	111,000	\$632,400	4,000	\$5.70	\$158.10	60%
Convenience Store - traditional	2,500	\$11,300	3,100	\$4.52	\$3.65	7%
- gas station	1,900	\$8,300	2,300	\$4.37	\$3.61	8%
Limited Assortment	8,000	\$62,500	800	\$7.81	\$78.13	6%

The main appeal of limited assortment stores is low prices

- **“Our market niche is price.”**
 - **Tony Eisenhut, Aldi US Vice President September 1996**
- **“There has always been a segment of the population that is attracted to low prices, but it’s a bigger segment of the population today. I think limited assortment is here to stay.”**
 - **Don Marsh, Chairman, Marsh Supermarkets, October 1994**
- **“The format definitely is growing because it has an extraordinary price proposition. There isn’t too much other than price that recommends it. The supercenter is probably going to be more impactful just because of its absolute size, but I think there is going to be strong growth in the limited assortment format, too. No one wants to overpay for groceries. And if the limited-assortment stores offer is acceptable to you, then you’re overpaying if you’re going somewhere else.”**
 - **Willard Bishop, Bishop Consulting, October 1994**
- **“The worse off people are, the better off we are.”**
 - **Anna Albrecht, mother of Aldi owners Karl and Theo**

Packaged grocery accounts for almost 50% of a German Aldi store's turnover...

ALDI RETAIL SALES BY CATEGORY IN GERMANY
(Percent of Sales)



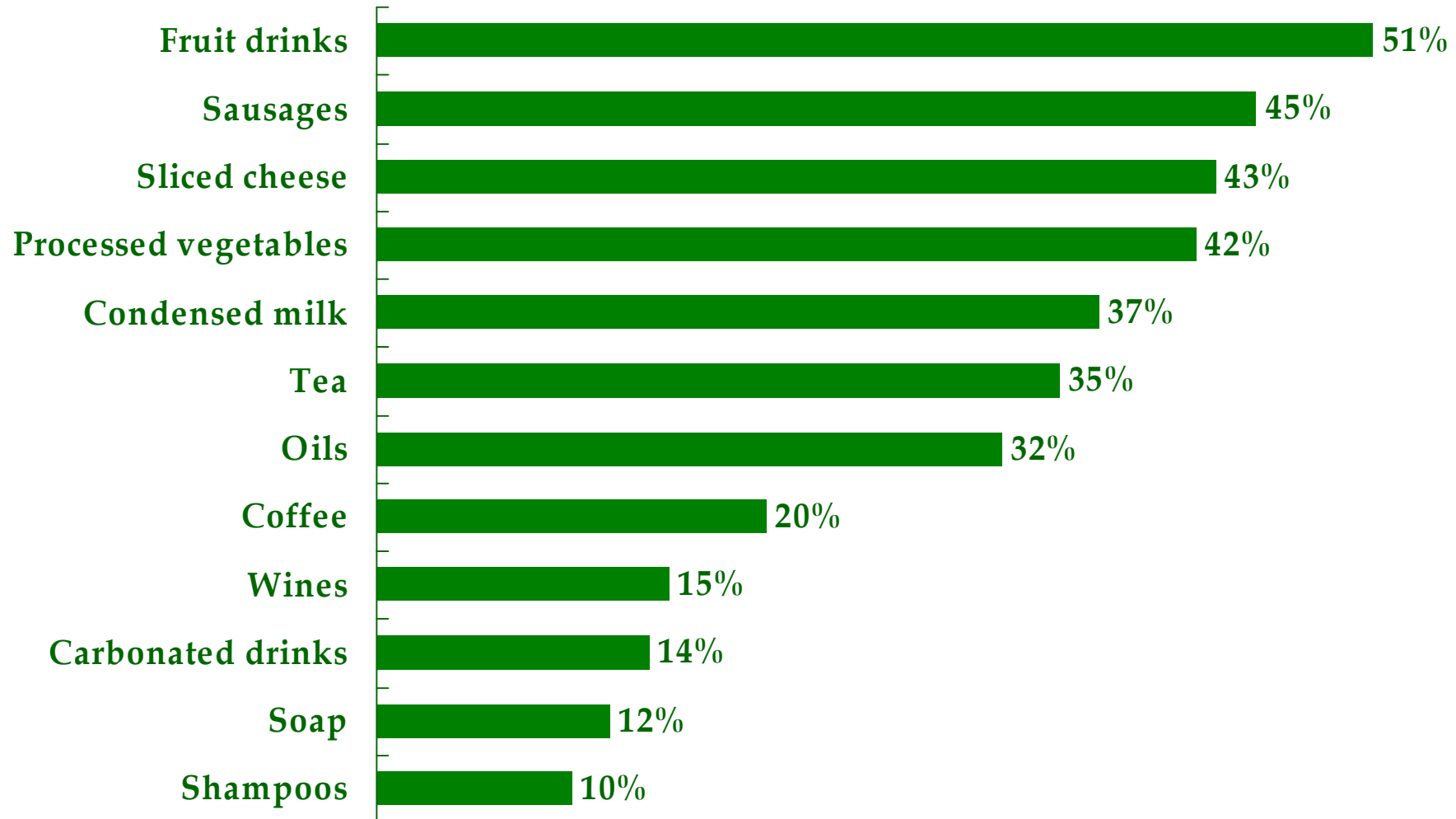
... and 50% of an American store's SKU mix

ALDI U.S. ASSORTMENT BY CATEGORY

Grocery		# of SKU's	Perishable		# of SKU's
293 50%	Baking supplies	36	Bacon & Deli meats	26	209 36%
	Beverages	39	Bread & bakery	26	
	Candy & gum	23	Dairy products	38	
	Canned fruit	14	Produce	27	
	Canned vegetables	21	Frozen food	92	
	Canned meat & fish	13	Non-foods		# of SKU's
	Cereals	24	Baby needs	3	82 14%
	Condiments	29	Health & beauty aids	28	
	Cookies & snacks	37	Household	18	
	Desserts	8	Paper products/plastic bags	23	
	Pasta	6	Pet supplies	10	
	Prepared foods	31			
Soup	12				

In Germany, over 70% of German households shop at Aldi, mostly for basic staples

ALDI MARKET SHARE IN WEST GERMANY
(% of total German sales; 1990 data)



Ib. Aldi has a low-cost logistics and operational system that works on a 12% gross margin

- Shopping at Aldi is not always a pleasant experience
- Aldi operates on a 12% gross margin and a 2% net margin

Aldi has a system that delivers the lowest possible cost of goods sold

Aldi has a streamlined checkout and store labor system that minimizes payroll costs

Aldi keeps site occupancy costs low by buying its store sites and having a basic store fitout

Aldi controls SG&A, Distribution and other costs ruthlessly

- Low priced, high quality private label is the key to Aldi's strategy
- Aldi sticks to its basic store format and offering religiously

Shopping at Aldi is not always a pleasant experience

- **“The facilities looked to me as if the place had been bombed just a day or two before.”**
 - **Advertising Age**

- **“At Aldi, costs are ruthlessly controlled. A shopper could starve to death waiting for an employee to answer a question. The stores don’t advertise; they aren’t even in the phone book. Unlike warehouse chains, Aldi does not require its customers to buy by the case. Checks and coupons are not accepted, and customers bag their own groceries - and bring their own bag if you don’t want to pay Aldi 4 cents for every bag. There are no stock boys because there are no shelves to stock. Goods are sold out of special, easy-to-open cartons. The guy wheeling the pallet of canned vegetables to the sales floor is probably the store manager. Aldi stores carry only about 600 items (most grocers have 10,000), so cashiers memorize prices and move faster than scanners.”**
 - **Forbes, February 1993**

- **“Its very depressing. People charge around the shelves to get out as soon as possible.”**
 - **Fiona Gilmore, Michael Peters & Partners Design Consultancy**

Aldi operates on a 12% gross margin and a 2% net margin

ALDI PRO FORMA STORE PROFIT & LOSS STATEMENT
(1995 U.S. market estimate)

	<i>Percent</i>	<i>Weekly</i>	<i>Annually</i>
Sales	100.0%	\$120,000	\$6,240,000
Cost of Goods Sold	88.0%	104,400	5,428,800
Shrinkage	0.5%	600	31,200
Payroll	3.0%	3,600	187,200
Occupancy	1.4%	1,680	87,360
SG&A, Distribution & Misc.	5.1%	7,320	124,800
Net Profit	2.0%	\$2,400	\$124,800

Aldi has a system that delivers the lowest possible cost of goods sold

- **Private label accounts for 90-95% of sales**
- **Aldi operates on a true net cost basis and requires no additional trade spending of any kind**
 - No slotting fees**
 - No introductory allowances**
 - No promotional discounts**
 - No volume allowances**
 - No gifts, golf tournaments, event funding, voluntary donations, etc.**
- **Aldi warehouses and delivers 100% of its items, including milk and bread, eliminating the need for direct store delivery and regional warehousing on the part of vendors**
- **Aldi stores do not require in-store sales representative, marketing or merchandising support**

Aldi has a streamlined checkout and store labor system that minimizes payroll costs

- **Aldi employees are paid well but are non-union where possible**

Employees are paid over the industry average and receive performance bonuses

“Aldi once had trouble with a Belgian trade union and shut three stores rather than compromise in negotiations.” Supermarket News, June 1992

- **Stores operations are designed to minimize labor**

Stores have between four and six full time employees

Checkout operators memorize 600 PLU item codes instead of scanning

Checkout operators average 42 items/minute vs. 15/minute in supermarkets

Average order size is 35 items; total cashing time per item 1.44 seconds

Store management is limited to a store manager who works six days, writes the order and operates a checkout

Stores have limited opening hours (56 hours per week coverage in the U.S.)

- **Product is displayed in the shipping box, on the shipping pallet, which is unloaded from the truck to the store floor by the truck driver**

Reducing handling and labor: total replenishing time per item 2.83 sec.

Eliminating backroom inventory and restocking

Aldi keeps site occupancy costs low by buying its store sites and having a basic replicated store fitout

- **Aldi attempts to buy all of its sites freehold to eliminate rent costs and rent increases**
- **Aldi tends to build from scratch rather than takeover an existing property**

Estimated U.S. cost to build of US\$50/sqft. or \$450,000 for a 9000 sqft. site

Total U.S. store fitout cost is estimated at US\$115,000 (fixtures, freezers, etc.)

Aldi stores are not remodeled; the store format has not changed in 15 years

Shopping carts require a coin deposit decreasing theft and reducing labor costs

- **“The company buys cheap land on city outskirts and builds cheap warehouses.”**
 - **Hoovers Food Industry Guide**
- **“Aldi situates its smaller than average stores mostly in farm towns or blue-collar, immigrant or low-income neighborhoods - Aldi likes dealing with big working-class families that eat at home and eat heartily. Stores are located away from costly real estate such as strip malls. They generally measure 8,000 square feet, one third the size of a typical grocery store..”**
 - **Forbes, February 1993**

Aldi controls SG&A, distribution and other costs ruthlessly

- **Aldi does not advertise other than through a fortnightly price-list flyer**
- **Aldi has a world-class logistics system**

The lack of promotions or specials ensures an even off-take from suppliers, who deliver just-in-time in predictable volumes

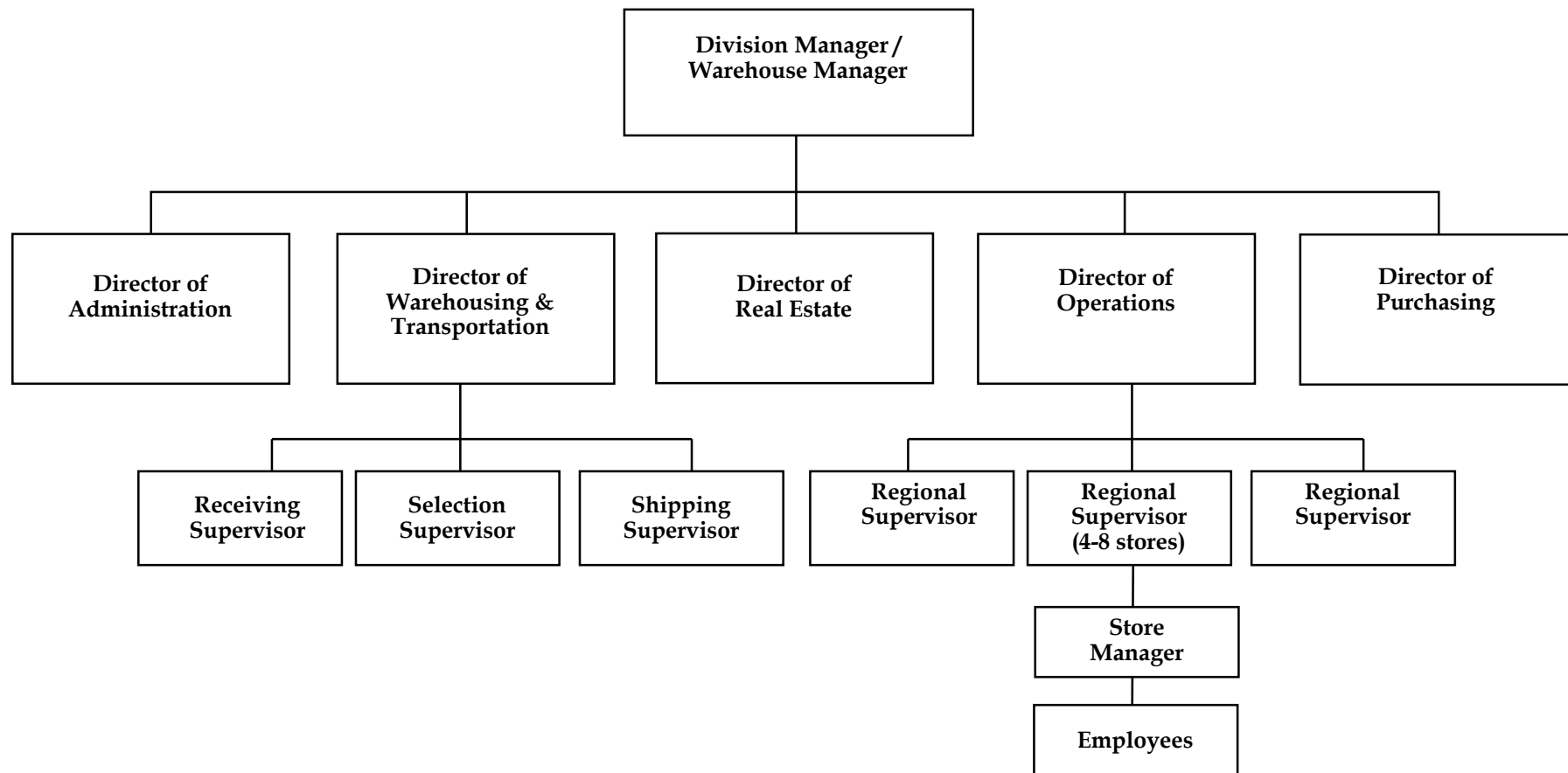
90% of product (by volume) is directly cross docked at the warehouse without entering inventory

Stores turnover their inventory weekly (52 times a year)

- **Aldi's lean management structure is built around the division, which represents the 30-60 store area serviced by a warehouse**
- **"Each Aldi division or warehouse is made up of an uncomplicated corporate structure that facilitates communication, recognition and advancement. All promotions are from within our organization."**
 - **Aldi Recruitment Brochure**

Aldi's lean management structure is built around the division, which represents the 30-60 store area serviced by a warehouse

ALDI MANAGEMENT STRUCTURE



Low priced, high quality private label is the key to Aldi's strategy

- Suppliers are attracted by Aldi's reputation for straight dealing**
- The huge volume Aldi moves through a very narrow range of items attracts even firms that traditionally do not supply private label**
- Aldi has its own product specifications and demands top quality**
- Aldi private label packaging is not "cheap and nasty"**

Suppliers are attracted by Aldi's reputation for straight dealing

- **"Once a price has been fixed, Aldi adheres to it relentlessly. Neither seller nor Aldi itself are allowed to rework prices, which gives security to suppliers as long as they abstain from speculation on low commodity prices during initial negotiations. This unique loyalty has helped some suppliers to grow with Aldi over the years.**

Approximately 70% of each own brand is supplied by a single manufacturer who often enough is also a producer of national brands. The discounter tends to buy from smaller manufacturers to achieve a strong position in price negotiations - with some of these smaller companies Aldi accounts for more than 30% of sales. On the other hand, Aldi wants to keep independent from suppliers and suppliers are not allowed to depend wholly on Aldi."

- **Private Label International, Fall 1995**

- **"Renowned for straight dealing and speedy payments, Aldi can also be demanding - insisting on consistently high quality and prompt delivery of goods."**

- **Irish Times, November 1999**

- **"[Aldi] works closely with manufacturers to help design own-label products that are cheaper to transport, stock and sell."**

- **The Economist, May 1993**

The huge volume Aldi moves through a very narrow range of items attracts even firms that traditionally do not supply private label

- Aldi German sales work out to an average of 30 million Euros for each SKU

- “Cereal maker Kellogg is to make cereal for somebody else, breaking with years of tradition. It has signed a deal with Aldi to supply five cereals under the store’s brands: Schoko Chips, Schoko Flakes, Honey Nut Flakes, Honey Balls and White Flakes.”
 - BBC News, February 2000

- “It emerged last year that several international giants, including Nestle and Unilever, have long been supplying non-name products to Aldi - news that came as no surprise to many Aldi regulars who noticed an uncanny similarity between many of their discount favourites and major branded products.”
 - Irish Times, April 2000

Aldi has its own product specifications and demands top quality

- **“The key to Aldi’s unrivaled loyalty in Germany is the fact that low prices are accompanied by consistently high quality so that, for example, Aldi champagne wins high marks in blind tastings and their sunscreen is believed to be the best on the market.”**

- **Irish Times, April 2000**

- **“What our customers want, and what we provide, is guaranteed top-quality products at the lowest possible prices. Aldi does not and will not sell generics, because the quality isn’t up to the high Aldi standards.”**

- **Dan Gavin, Aldi Springfield Division Manager, October 1994**

- **“I just want to share with you my absolute delight with your products and prices!! I have always shopped in a situation of “tight budget” and want to commend you for the obvious concern with quality that your company upholds. I am always amazed at the quality of the food I purchase somewhat feeling I’m “taking a chance,” considering I do not know the brands. Each product I have tried has not only proved to be an adequate product in quality, but actually been very fine indeed.”**

- **Recky Mondy, Aldi Customer Letter, Cornell University Aldi Case Study**

Aldi's private label is sold under a number of "controlled" brands that consumers do not perceive are owned by Aldi

- **"Aldi has a number of different labels that are its private label. Our research shows that consumers believe this is a national brand label from another area of the country."**
 - **Willard Bishop, Bishop Consulting, June 1992**
- **"Aldi follows the German custom of not using its name for its own brands, so quality defects will not backfire on Aldi's reputation."**
 - **Private Label International, Fall 1995**

Aldi private label packaging is not “cheap and nasty”

SAMPLE ALDI BRANDS



Aldi sticks to its basic store format and offering religiously

- **“At Aldi the customer is not king. We are providing not service, but mass production.”**
 - **Karl Albrecht, Aldi Co-owner**

- **“Our phenomenal growth has been achieved by our adherence to a very single minded Company philosophy: we offer the customer a carefully selected range of high quality exclusive own label brands at heavily discounted prices. What’s more, these discounted prices are guaranteed week in week out.”**
 - **Aldi UK Website, April 2000**

- **“Aldi has been successful by ignoring the siren call of retail experts to diversify, to broaden its range of products, and to use focus groups, market research and sophisticated advertising. Orders are determined, not by what suppliers are offering at favourable prices at any given time, but by what customers want.”**
 - **Irish Times, November 1999**

Ic. Privately owned Aldi has a long investment horizon and plenty of patient capital

- **The company is the eighth largest retailer in the world, with 1998 sales of US\$35 billion**
- **Aldi is legendary for its secrecy, refusing to release any financial or operational information to the media . However, this desire for secrecy has created a convoluted ownership structure**

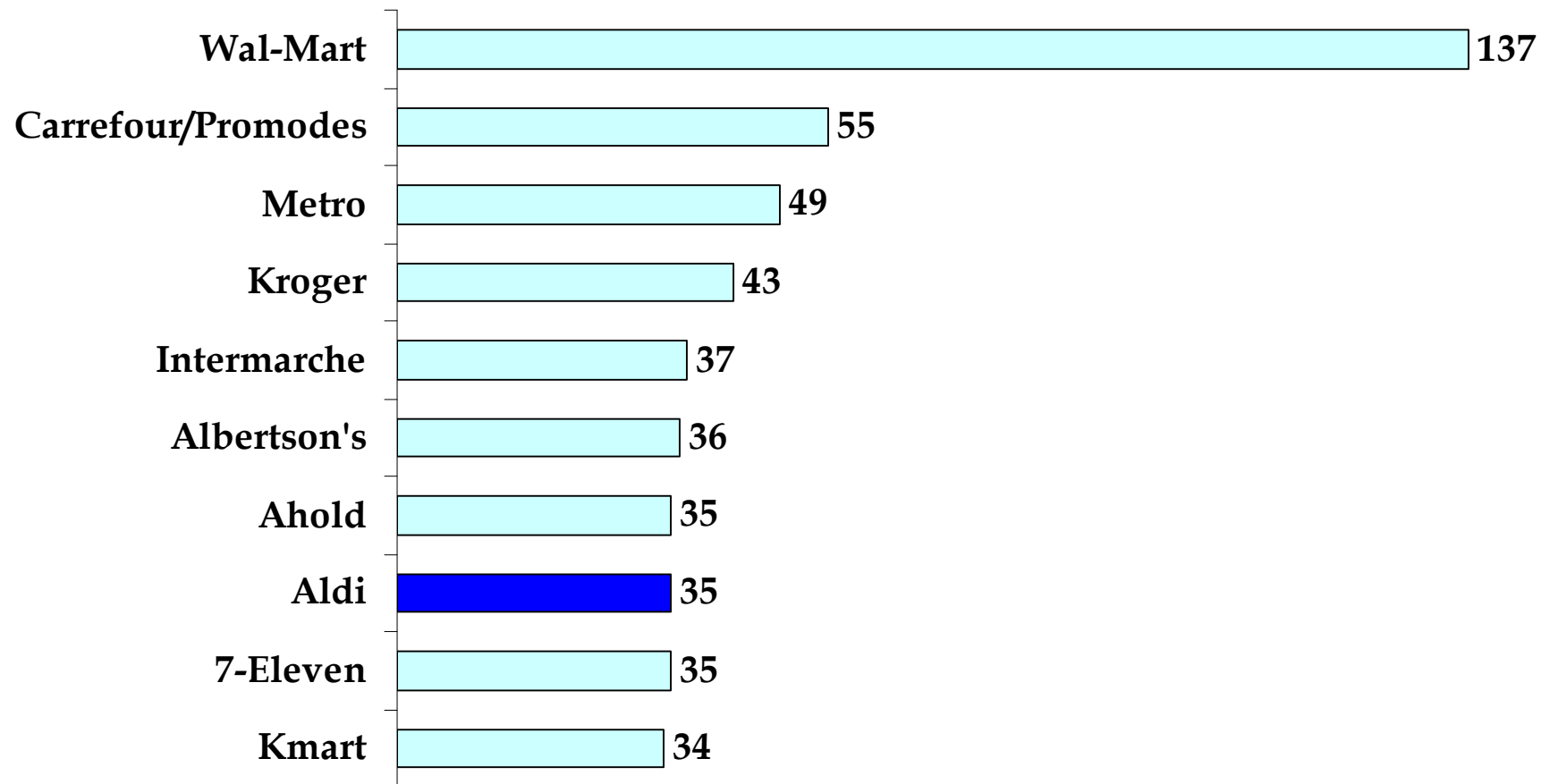
Aldi's global empire is split into two organizations, Aldi Nord and Aldi Sud, with Aldi Sud leading the expansion into English speaking countries

The division of Aldi into two parts reflects the division of the company by the two brothers

- **The Albrecht family is investing in Aldi for the long run**

The company is the eighth largest retailer in the world, with 1998 sales of US\$35 billion

10 LARGEST GLOBAL RETAILERS
(1998 Sales; US\$ Billions)



Aldi is legendary for its secrecy, refusing to release any financial or operational information to the media...

- **“The company goes to remarkable lengths to prevent public disclosure of its activities whether financial (sales, let alone profits) or physical (store numbers and foreign openings). The research organization Nielsen was for many years excluded from even visiting Aldi stores, a rejection almost unique among major food retailers in Europe. This penchant for secrecy was reinforced by the abduction in 1971 of Theodore Albrecht - he was eventually released, reportedly on the payment of a DM7 million ransom.”**

- **Corporate Intelligence on Retailing**

- **“That Aldi has grown so large worldwide - while attracting so little notice - is a tribute of sorts to Aldi’s strict policy of maintaining absolute secrecy about its business. Aldi founders Karl and Theo Albrecht live a reclusive life and have not been seen in public for many years. One result of this policy - whether intended or not - is that Aldi often creeps up on the competition with its low-tech operation, catching the competition unawares.”**

- **Supermarket News, June 1992**

However, this desire for secrecy has created a convoluted ownership structure

- **“Aldi’s lean management structure combines topdown hierarchy with a high degree of decentralization. Aldi North and South both consist of around 25 legally independent organizations, each of which consists of approximately 50 outlets. This decentralization has one reason in German Law: from a certain size upward, German companies are under the legal obligation to disclose their results and consult with unions. To avoid this Aldi founds a new company whenever the number of outlets would bring the company within the range of the disclosure law.”**
 - **Private Label International, Fall 1995**

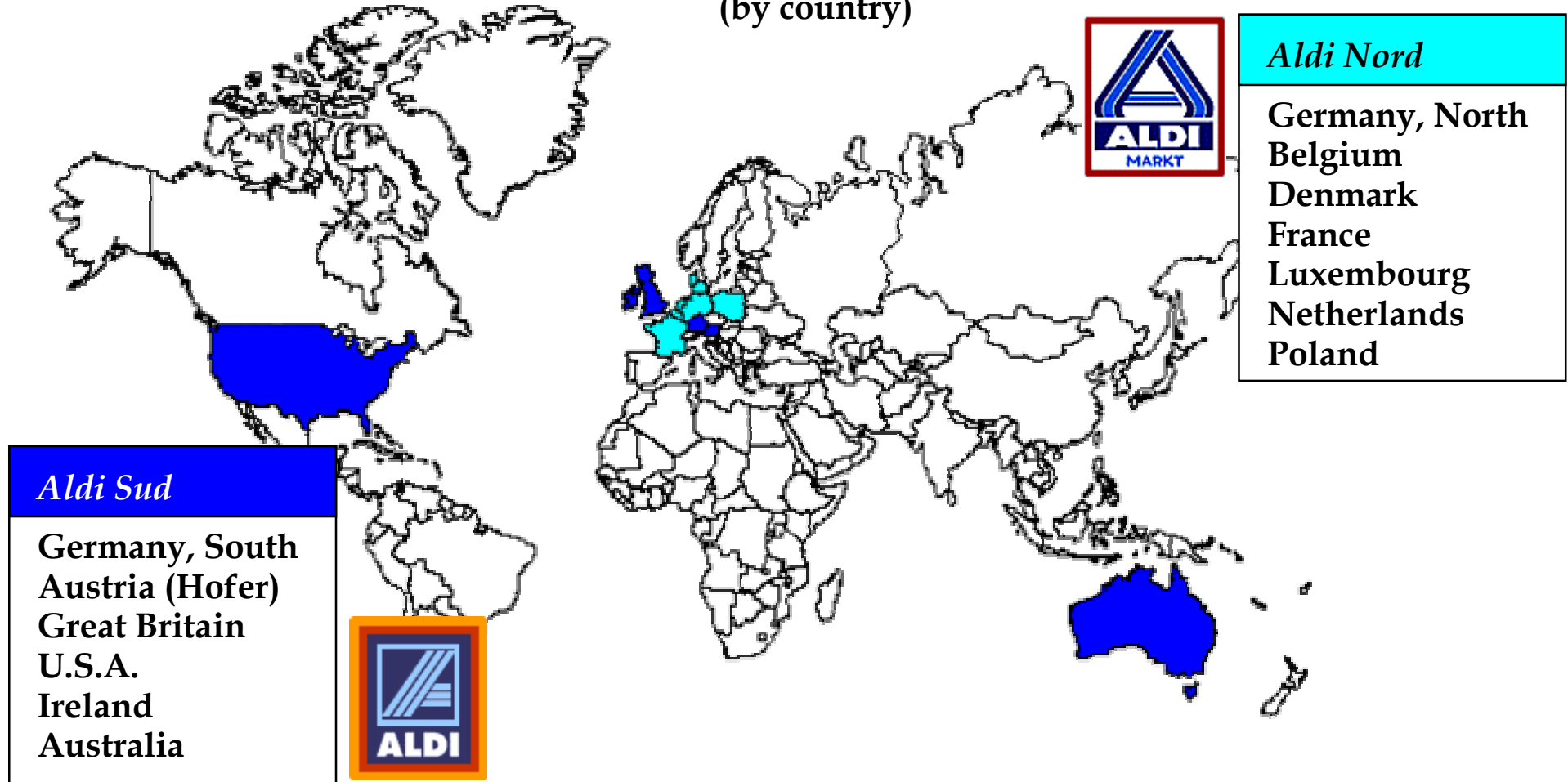
- **“Aldi North and Aldi South are not groups in the traditional sense. Technically, Aldi’s business activities are controlled by a number of family foundations, which enjoy a greater amount of secrecy and entrepreneurial freedom in Germany.”**
 - **Private Label International, Fall 1995**

- **“The group is tightly controlled. Aldi Einkauf, based in Mulheim, is a private company that oversees the operations of Aldi Nord and Aldi Sud. Ultimate control remains entirely with the Albrecht family and is vested through Albrecht KG, a private family foundation.”**
 - **Corporate Intelligence on Retailing**

Aldi's global empire is split into two organizations, Aldi Nord and Aldi Sud, with Aldi Sud leading the expansion into English speaking countries

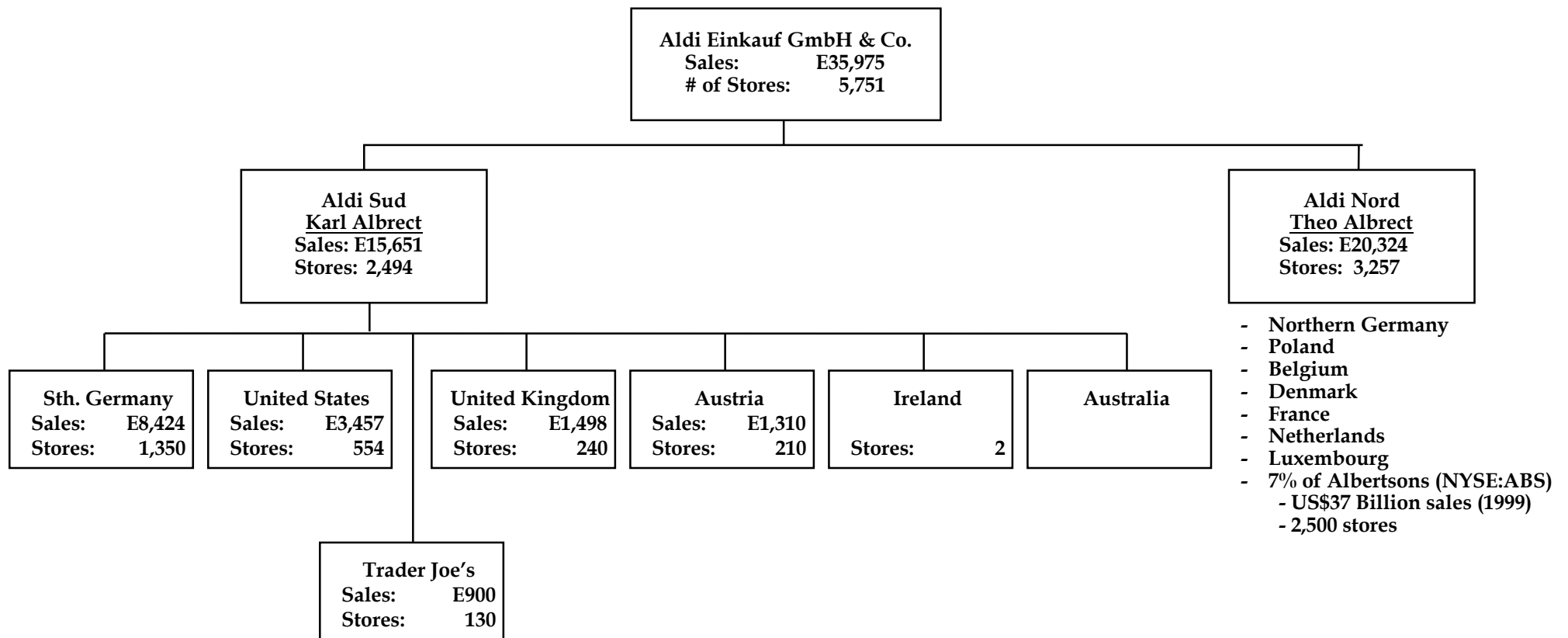
ALDI GLOBAL OPERATIONS

(by country)



The division of Aldi into two parts reflects the division of the company by the two brothers

ALDI EINKAUF GMBH & CO
(Euro; millions)



The Albrecht family is investing in Aldi for the long run

- **“Internationalization has not always yielded fast profits for Aldi. In Denmark, it was reputed to have taken 10-12 years to achieve a profit, indicating a willingness to take a very long view on matters of market penetration. A private company, Aldi is still run by the brothers Karl and Theodore. This partially explains its resilience and willingness to pursue very long term goals.”**
 - **Peter McGoldrick, Irish Marketing Review, 1993**

- **“The Albrecht family doesn’t really control Aldi anymore, the second generation of the family can’t touch it. The company is run by independent trusts that have one goal: to grow the business. As long as I grow market share year in, year out, I have a job.”**
 - **Tim LeBeau, President Aldi USA, March 1992**

Id. There are few threats to Aldi or the limited assortment store...

ALDI SWOT ANALYSIS

<i>Strengths</i>	<i>Weaknesses</i>
<p>Simplicity of operations Cost efficient Powerful price points Private label sourcing Price edge over other retailers Understands economics of business Deep pockets of parent company Low breakeven stores Parasite stores feed off supermarkets</p>	<p>Manual systems used Limited assortment, limited appeal Minimal perishables, marginal quality Dependent on well trained cashier</p>
<i>Opportunities</i>	<i>Threats</i>
<p>Expand into other markets Increase market penetration Continue to improve quality Tap into institutional markets Hold tight to lowest cost positioning</p>	<p>Other limited assortment who understand the business and can operate better</p>

... Aldi is immune to competition, even from WalMart

- **“Wal-Mart or any other competitor’s activity doesn’t really influence ours. We have our own focus, our own agenda and we prefer to get on with that.”**
 - **Trevor Coates, Managing Director, Aldi UK/Ireland, March 2000**

- **“Aldi offered prices 24% below Sam’s Club [WalMart’s Warehouse Club Operation] on a market basket of 301 comparable items.”**
 - **Supermarket News, Oct 1994**

- **“Aldi sells only high-volume items, mostly canned produce, paper goods, snacks, frozen food. Limiting the range in this way and selling most under its own label means that Aldi can cut prices even below Wal-Mart, the low-cost benchmark.”**
 - **Forbes, February 1993**

II. The United Kingdom provides an excellent model for the development of Aldi in Australia

- **IIa. Aldi reshaped consumer price perceptions and the retail environment**
- **IIb. Existing supermarket chains responded somewhat successfully in a number of ways**
- **IIc. Supermarkets started a market wide price war in a small range of basic grocery items**
- **IId. The shakeout that followed drove marginal players out of business**

IIa. Aldi reshaped consumer price perceptions and the retail environment

- Aldi generated a lot of publicity when it entered the U.K. market
- Aldi grew its U.K. stores numbers 36% per year for ten years
- Aldi's main European rivals followed it into the United Kingdom
- Aldi and Netto offered significant price savings against conventional supermarkets
- Aldi did this by having ownership that was willing to take a long term view

Aldi generated a lot of publicity when it entered the U.K. market

- "MAYHEM FROM TWO SHOPS"

- The Grocer (UK), June 1990

- "The arrival of Euro-competition, specifically the German discount chain Aldi into the UK, has sent waves across this calm pond. We have seen grocery discounting for over two decades, most noticeably personified by the Kwik Save chain. Why, then, the considerable consternation when one more discount store was opened in Birmingham in February 1990? Could it have been another case of British xenophobia? Alternatively, does Aldi have a particular track record and characteristics that merit this level of concern?"

- Peter McGoldrick, Irish Marketing Review, 1993

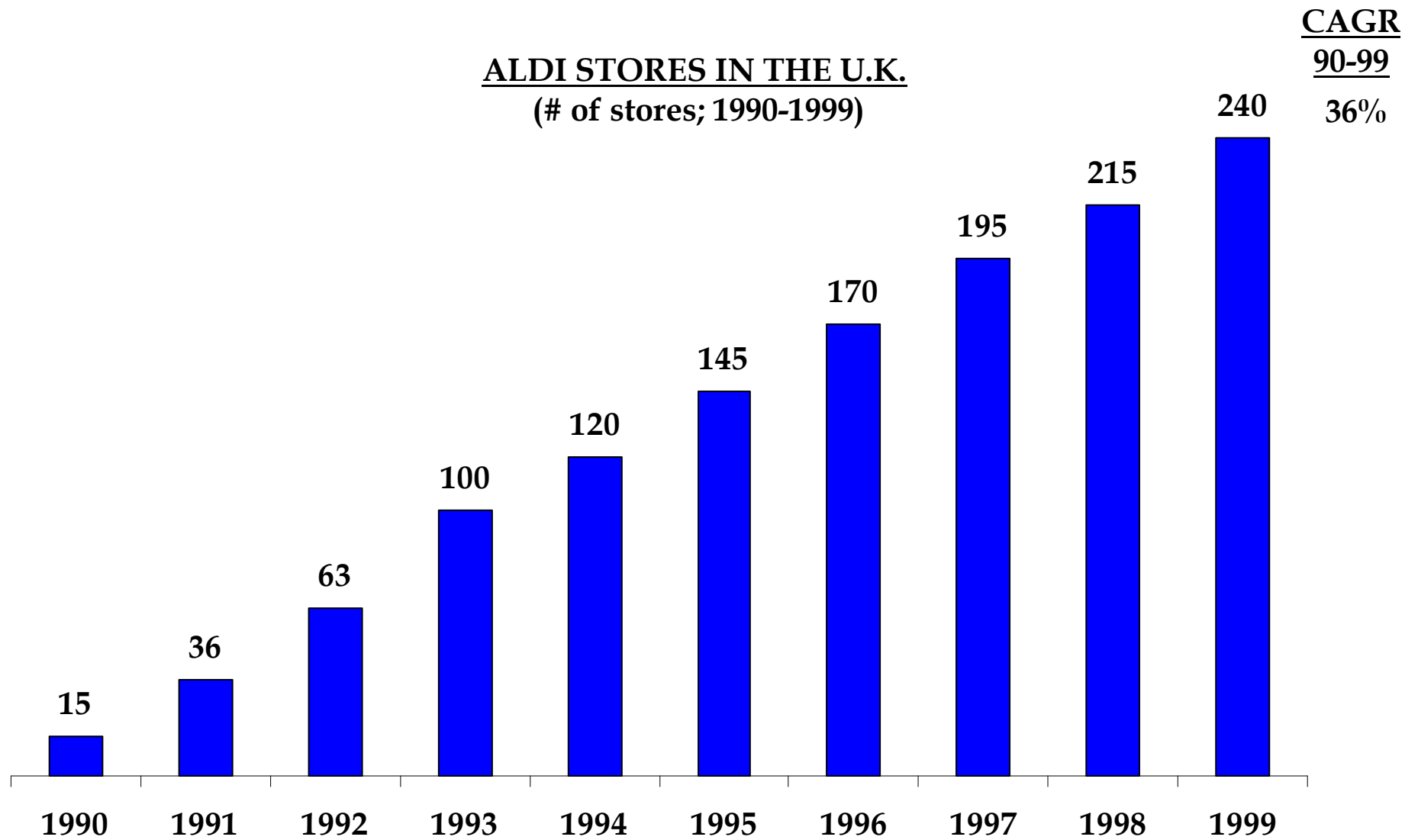
- "By reintroducing the "very low" price concept to a market which had been moving in the direction of one-stop quality superstores, Aldi and Netto have had a destabilizing effect disproportionate to their numbers. Their advent coincided with the recession and gave the impression among consumers that they might be paying too much for their food."

- International Journal of Retail & Distribution Management, Jan 1994

- "When Aldi first came to the UK, armed with its policy of total silence and firm intent, the speculation was rife. How could such a price cutter survive in the UK jungle, after all, operators have diversified their inventories, moved up-market, used technology and ended up with startling net margins. And that obviously is what attracted Aldi used to 2% back home. Aldi is the maverick, the store that could upset the apple-cart especially if inflation takes a firmer grip. Its effect on trading methods and profitability could be startling."

- The Grocer (UK), June 1990

Aldi grew its U.K. stores numbers 36% per year for ten years



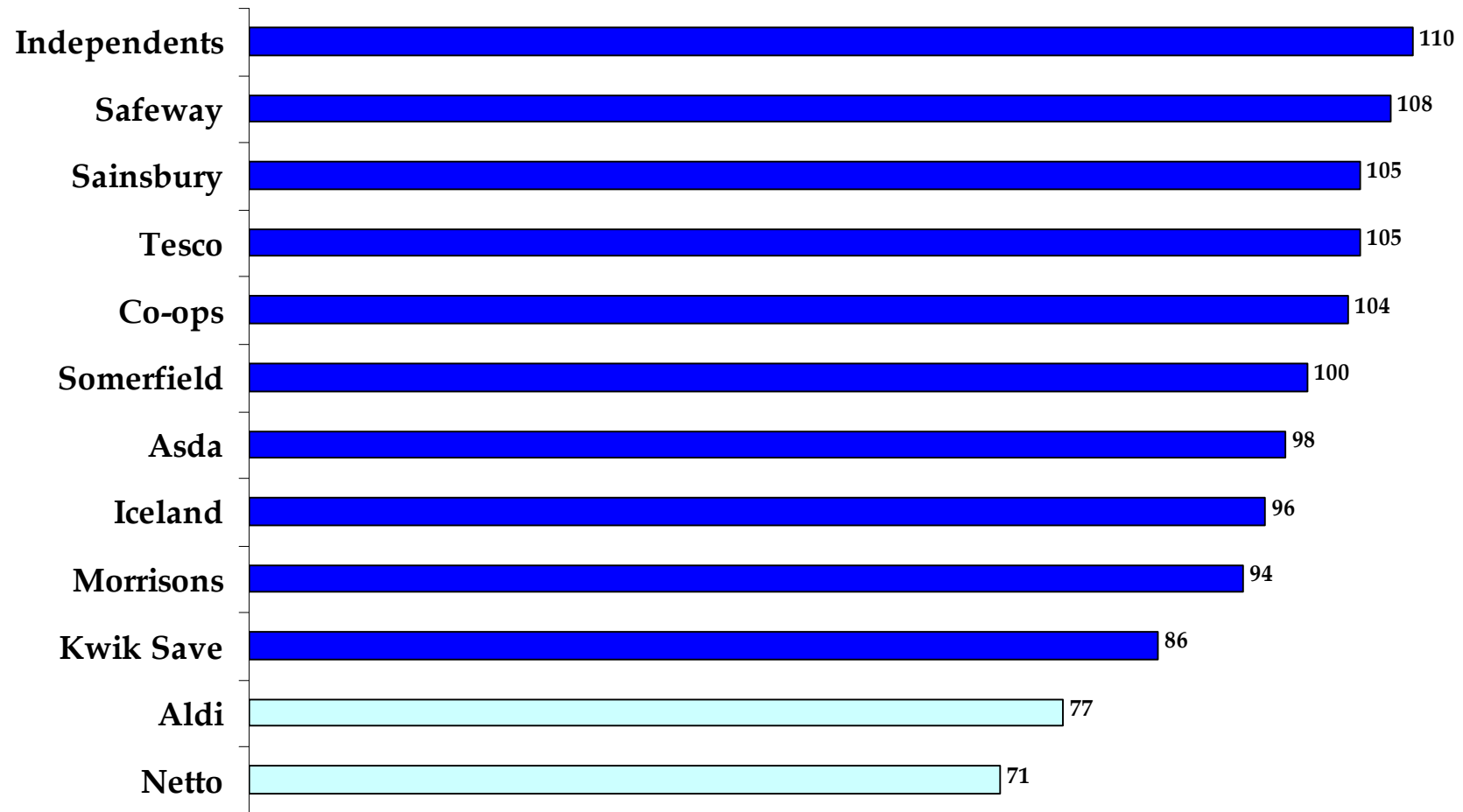
Aldi's main European rivals followed it into the United Kingdom

EUROPEAN DISCOUNT GROCERY FORMATS IN THE U.K.

<i>Facia</i>	<i>Parent Company</i>	<i>99 World Sales (US\$B)</i>	<i># of Outlets (1/1/2000)</i>		<i>First U.K. Store Opened</i>
			<i>World</i>	<i>U.K.</i>	
Aldi	Aldi Einkauf GmbH	\$35.0	5,751	240	Apr 1990
Netto	Dansk Supermarked	\$?	683	119	Dec 1990
Lidl	Lidl & Schwarz Stiftung	\$11.3	3,000+	118	Nov 1994

Aldi and Netto offered significant price savings against conventional supermarkets

RELATIVE PRICING STRUCTURE OF U.K. RETAILERS
(Relative Price Index; 100=Average)



Aldi did this by having ownership that was willing to take a long term view

KEY POINTS OF DIFFERENCE: DISCOUNT VS. SUPERSTORE

<i>Variable</i>	<i>Limited Assortment</i>	<i>U.K. Food Superstore</i>
Average number of items	650	23,000
Stockturns (times per annum)	40/50	23/26
Net Margin	2%	7%
Asset Turnover (times per annum)	7	3
ROCE (Net Margin X Asset Turnover)	14%	21%

IIb. Existing supermarket chains responded somewhat successfully in a number of ways

- High end stores attempted to distance themselves from the price end of the market through larger selections, new products, and better service**
- Supermarkets attempted to reduce the price differential by offering a limited range of low-price private label products under a second label**
- Major chains also launched shopper loyalty club cards**

High end stores attempted to distance themselves from the price end of the market through larger selections, new products, and better service

- **“The superstores have upgraded their service (shorter queues at Sainsbury’s and Tesco, self-scanning at Safeway), improved their ancient facilities (the increased availability of cheap petrol for example), and launched loyalty schemes amid a blaze of publicity.”**

- **Super Marketing, April 1995**

- **“Sainsbury, aware that it has never been the cheapest supermarket, is not aiming to win the price war, instead stressing what it sees as other strong selling points, such as exotic and organic foods. It is also widening the benefits of its loyalty card and focusing on store revamps. One trial will see trolleys with cup holders - for people to drink coffee as they shop.”**

- **BBC News, August 1999**

Supermarkets attempted to reduce the price differential by offering a limited range of low-price private label products under a second label

- **All of the major chains launched a line of low-priced private label products**

- **“Tesco’s Value lines were followed by Safeway’s Savers and Sainsbury’s Essentials. Kwik Save fought back with its No Frills range. Many discounted products make a loss, but that is judged worthwhile in the fight to regain customers. Tesco estimates its Value line brings in an extra half-million people a week.”**
 - **The Independent, January 1995**

- **“Everyone agrees the death knell for discounters was sounded with the introduction of Tesco’s Value budget range in July 1993 and Sainsbury’s Essentials for the essentials which followed. Own-label budget ranges, which now include Safeway’s Savers and Sommerfield’s Basics, have grabbed a 5 to 6% share of total packaged grocery sales and 10% to 12% in volume.”**
 - **Super Marketing, April 1995**

All of the major chains launched a line of low-priced private label products

U.K. VALUE OWN LABEL BRANDS

<i>Chain</i>	<i>Value Brand</i>	<i># of items (1995 data)</i>
Sainsbury's	Low Price Essential	120
Tesco	Value	136
ASDA	Farm Stores	250
Safeway	Savers	120
Somerfield	Basics	100+
Kwik Save	No Frills	130
Iceland	Super Value	12

Major chains also launched shopper loyalty club cards

U.K. SUPERMARKET LOYALTY SCHEMES

<i>Chain</i>	<i>Loyalty Scheme</i>
Sainsbury's	Sainsbury Card
Tesco	Clubcard
Safeway	ABC Club

IIC. Supermarkets started a market wide price war in a small range of basic grocery items

- **The price fight began with the legendary “Baked Beans War”**
- **The price war quickly spread to other basic grocery lines**
- **The overall effect was to lower consumers price expectations for a narrow range of core products**
- **“The opening of an Aldi or a Lidl with fewer than 700 lines would not itself force a nearby Sainsbury’s or Tesco store with 20,000 lines to cut its prices. But it could force a local Somerfield or Asda to react and that could have a knock-on effect for the other multiples. And as both Asda and Somerfield have become more price-sensitive, the price war could spill out of the more traditional areas of packaged grocery and into, for instance, toiletries.”**
 - **Super Marketing, January 1995**

The price fight began with the legendary “Baked Beans War”

- **“Baked beans, the unsung hero of British cuisine, are setting the pace in the marketing war billed as the sale of the century. In some stores they are now so cheap that management has to impose a quantity restriction, presumably to avoid a customer stampede. The craze for knock-down prices has infected even upper-crust supermarkets like Sainsbury’s.”**
 - **The Guardian, October 1994**
- **“Britain’s biggest supermarket chains have introduced baked bean rationing because of a 3p-a-can price war. Shoppers at Tesco, Asda and Kwik Save were yesterday limited to four tins to prevent other retailers from stocking-up and re-selling them. The bean feast began last month when the big chains cut the prices of their own brand baked beans to 5p in the face of tough competition from the discount stores Aldi and Netto.”**
 - **The Independent, April 1996**
- **“The baked beans war intensified with a 1p a tin promotion launched by Milbank Foods.”**
 - **Financial Times, April 1996**
- **“The multiples have the discounters on the back foot. If they can curtail Aldi and Netto’s store growth, that will be a job well done.”**
 - **Paul Smiddy, Retail Analyst, Nomura Securities, November 1994**

The price war quickly spread to other basic grocery lines

- **“U.K. food retailers are coming under increasing pressure from the Three Horsemen of the Discounting Apocalypse: German discounters Aldi, Netto and Lidl. Our estimate is that they currently have about 1% of the retail market between them. They wanted to grab market share very quickly by driving down the price of items such as milk, bread and butter, forcing the superstores to respond.”**
 - **Richard Perks, Verdict Research, April 1996**

- **“The price of butter has plummeted as the supermarket giants battle to crush the discounters. The move follows the baked beans price war earlier this autumn when the price of a 14oz can fell as low as 5p in some stores. Similar activity is taking place in the frozen turkey market.”**
 - **Marketing Week, November 1994**

- **“A bread war has broken out in Britain’s supermarkets as retailers jostle to offer the cheapest white loaf in the country. Shoppers can now snap up their white sliced for as little as 7p after an intense round of price cutting by the major chains.”**
 - **BBC News, February 1999**

The overall effect was to lower consumers price expectations for a narrow range of core products

- **“Prices of basic groceries in some supermarkets have fallen by 17% over the last two years. The stores have slashed prices to compete with discount chains, resulting in a savings of £357 a year on a weekly basket of essentials.”**

- **Daily Mail, October 1994**

- **“It is a publicity stunt by the big majors who are facing pretty stiff competition from big discounters like Aldi and Netto. In the long term there will be a gradual narrowing of prices between the majors and the discounters and that will be the real good news, not the one off promotional specials like this.”**

- **Jack Winkler, Food & Health Research UK**

- **“The likely outcome is that retailers will polarise into those who trade on price, such as Aldi and Netto, and those who trade on quality, such as Marks & Spencer and Sainsbury, with precious little room in the middle, either for brands or for retailers.”**

- **Marketing, July 1993**

IId. The shakeout that followed drove marginal players out of business

- **“I expect the shakeout to continue. There are far too many discount fascias in the market and the major players will win. Things are pretty tough at the bottom end of the market.”**

- **Clive Vaughan, Verdict Research, February 1995**

- **‘Extended range’ discount grocer Kwik Save was the major casualty**

Kwik Save was squeezed between Aldi and the full service supercenters

Dairy Farm appointed two ex-Franklins managers, Graeme Seabrook and Graeme Bowler, in succession to run Kwik Save

Aldi and Netto beat Kwik Save by having a much higher turnover per square foot

Kwik Save was taken over by Somerfield which plans to convert, sell, or close all stores

- **Smaller, poorly financed discount formats were also driven out of business**

Kwik Save was squeezed between Aldi and the full service superstores

- **“Kwik Save used to be cheap and cheerful. Now it’s even cheaper, but not so cheerful. Prices are down but so are profits. The chain is seen as being caught between the superstores and the full-blooded discounters.”**
 - **The Guardian, May 1995**
- **“Kwik Save is paying the price for straying from its roots. As a discounter of a limited range of basic branded goods it had a distinct appeal. That has been blurred as the group tried to emulate the supermarkets by doubling its product range to over 4000 lines, building larger, more expensive stores and introducing own-label goods. This has allowed pure discounters such as Aldi and Netto to undercut it, while the big supermarkets have retaliated from on high by cutting prices on the typical Kwik Save shopping basket. Kwik Save is being horribly squeezed in the middle.”**
 - **The Financial Times, May 1996**
- **“Kwik Save has no future unless it can establish clear points of difference versus its competitors, the limited assortment stores and the superstores.”**
 - **NatWest Securities, July 1995**

Dairy Farm appointed two ex-Franklins managers, Graeme Seabrook and Graeme Bowler, in succession to run Kwik Save

- **“Aldi will not undersell us on merchandise. Our policy is to be very competitive and we will move our prices down if we have to.”**

- **Graeme Seabrook, July 1989**

- **“Graeme Bowler is the tough, pugnacious, opinionated Australian who will either humiliate Britain’s leading food retailers in a prolonged and bitter price war, or fall flat on his hard-nosed face. Mr. Bowler is Chief Executive of Kwik Save, Britain’s leading discounter. Critics claim Kwik Save, trapped between the increasingly price conscious Sainsbury, Tesco and Safeway and Continental narrow-range super-discounters, such as Netto and Aldi, is heading for trouble.”**

- **The Guardian, May 1995**

- **“The food retailing environment has changed dramatically over recent years. Competition has become increasingly fierce from superstores and continental discount groups, which have encroached on Kwik Save's traditional customer base, both geographically and through aggressive pricing. The resultant setback to the company's financial performance is an indication that Kwik Save needs to adapt more quickly to the changing demands and rising expectations of our customers. In February, with the help of Andersen Consulting, the group began a comprehensive review of all its business operations.”**

- **Kwik Save Press Release, November 1996**

Aldi and Netto beat Kwik Save by having a much higher turnover per square foot.

U.K. DISCOUNT SECTOR

<i>Format</i>	<i>Average Store Size (sqft.)</i>	<i>Sales per sqft per annum (UK £)</i>
Aldi	6,000	£900
Netto	6,000	£750
Kwik Save	6,500	£440

Kwik Save was taken over by Somerfield which plans to convert, sell, or close all stores

- **“Although the deal is being billed as a merger, Somerfield is making a recommended offer for Kwik Save, which has been struggling in a fiercely competitive market and has seen sales fall and its year pre-tax profits slide to £73.7m from £90.3m. Kwik Save shareholders will receive seven Somerfield shares for every six Kwik Save shares they own. Following the deal, Somerfield investors will own 62.5% of the enlarged group.”**

- **Financial Times, February 1998**

- **“Britain's fifth-biggest retailer ran into trouble after it bought Kwik Save in February last year. It has been badly hit by a new wave of aggressive price campaigns by the market leader, Tesco, and by Asda, which is owned by US discount giant Wal-Mart. Somerfield has now announced that 350 Kwik Save stores it had already said did not fit into its restructuring plans will be offered for sale as a going concern. Somerfield branded store like-for-like sales were down 1.4% while at Kwik Save sales were down 16.2%.”**

- **BBC News, November 1999**

- **"It's not quite clear when or how things are going to improve."**

- **Ian Macdougall, Analyst, Williams De Broe, March 2000**

Smaller, poorly financed discount formats were also driven out of business

DISCOUNT GROCERY SECTOR CONSOLIDATION IN THE U.K.

<i>Fascia</i>	<i>Parent Company</i>	<i>First Store Opened</i>	<i>Outcome</i>
Kwik Save	Dairy Farm Intl. (25%)	1965	Taken over by Somerfield Stores to be sold or closed (?)
Shoprite	Shoprite	1990	Bought by Kwik Save
Ed	Carrefour	Jan 1993	Bought by Netto
Penny Market	Budgens/Rewe JV	Jul 1993	Format discontinued 4 stores sold to Lidl
LoCost	Argyll/Safeway	-	Sold 123 stores to Spar Sold 101 stores to Co-op

III. The arrival of Aldi in Australia will have a focused impact, felt mostly on key line pricing and by Franklins

- **IIIa. The entry of Aldi into the Australian market will cause a lot of sound and fury**
- **IIIb. Aldi will attract price sensitive shoppers from lower socio-economic groups**
- **IIIc. These shoppers will primarily come from Franklins and independent supermarkets**
- **IIId. Aldi will restructure market-basket pricing, causing a number of lines to be sold at true net cost**

IIIa. The entry of Aldi into the Australian market will cause a lot of sound and fury

- **“In any new market you go into you are going to challenge the establishment. Established and very strong retail groups are anxious to protect their position. Aldi has established a bit of a reputation of becoming involved in price wars and disputes.”**
 - **Trevor Coates, Managing Director, Aldi UK/Ireland, March 2000**
- **“Aldi is worrying supermarket retailers, especially in NSW. The main fear is that increased competition might spark a price war and hurt margins.”**
 - **Australian Financial Review, October 1999**
- **“German supermarket group Aldi received a shot across its bows from Coles Myer’s chief executive Mr Dennis Eck concerning its imminent move into Australia. He said Coles was committed to “punching” its competitors.”**
 - **Australian Financial Review, October 1999**

IIIb. Aldi will attract price sensitive shoppers from lower socio-economic groups

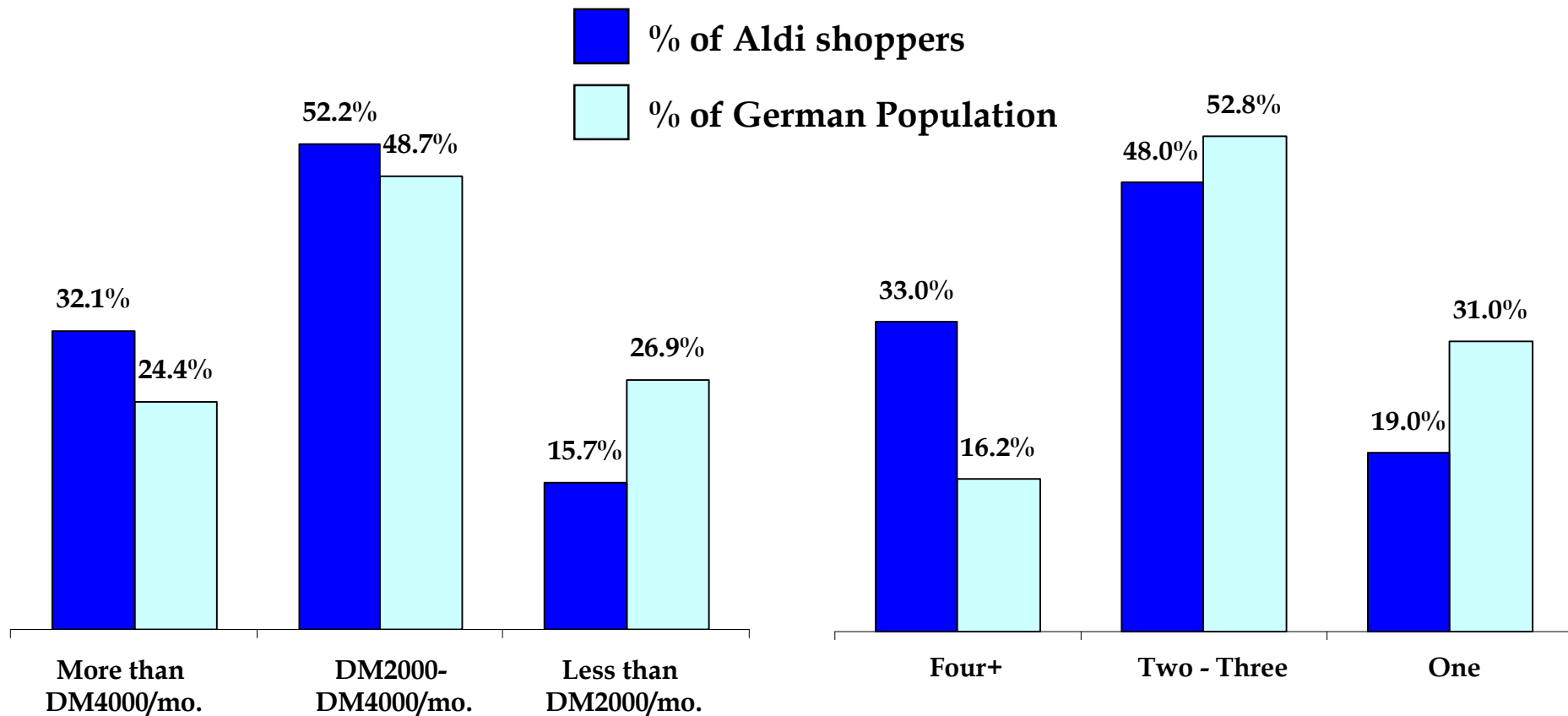
- **In Germany, Aldi attracts a relatively larger percent of large, medium to high income households**
- **In the U.K., Aldi attracted older, more down market shoppers living alone**
- **In Australia Aldi will attract price sensitive shoppers from lower socio-economic groups**

In Germany, Aldi attracts a relatively larger percent of large, medium to high income households

ALDI DEMOGRAPHICS IN GERMANY
 (% of income vs. % of Aldi shoppers)

Household Income

Household Size



In the U.K., Aldi attracted older, more down market shoppers living alone

ALDI DEMOGRAPHICS IN THE U.K.

<i>Demographics</i>	<i>Aldi Shopper</i>	<i>Average U.K. Shopper</i>
Average age	45.6	44.3
Older than 65	20%	16%
Single/living alone	23%	15%
C2 D E income group	70%	59%
Reasons for store choice: (all mentioned)		
Convenience	24%	76%
Facilities	22%	32%
Price	91%	32%
Range	8%	16%
Quality	10%	12%

In Australia Aldi will attract price sensitive shoppers from lower socio-economic groups

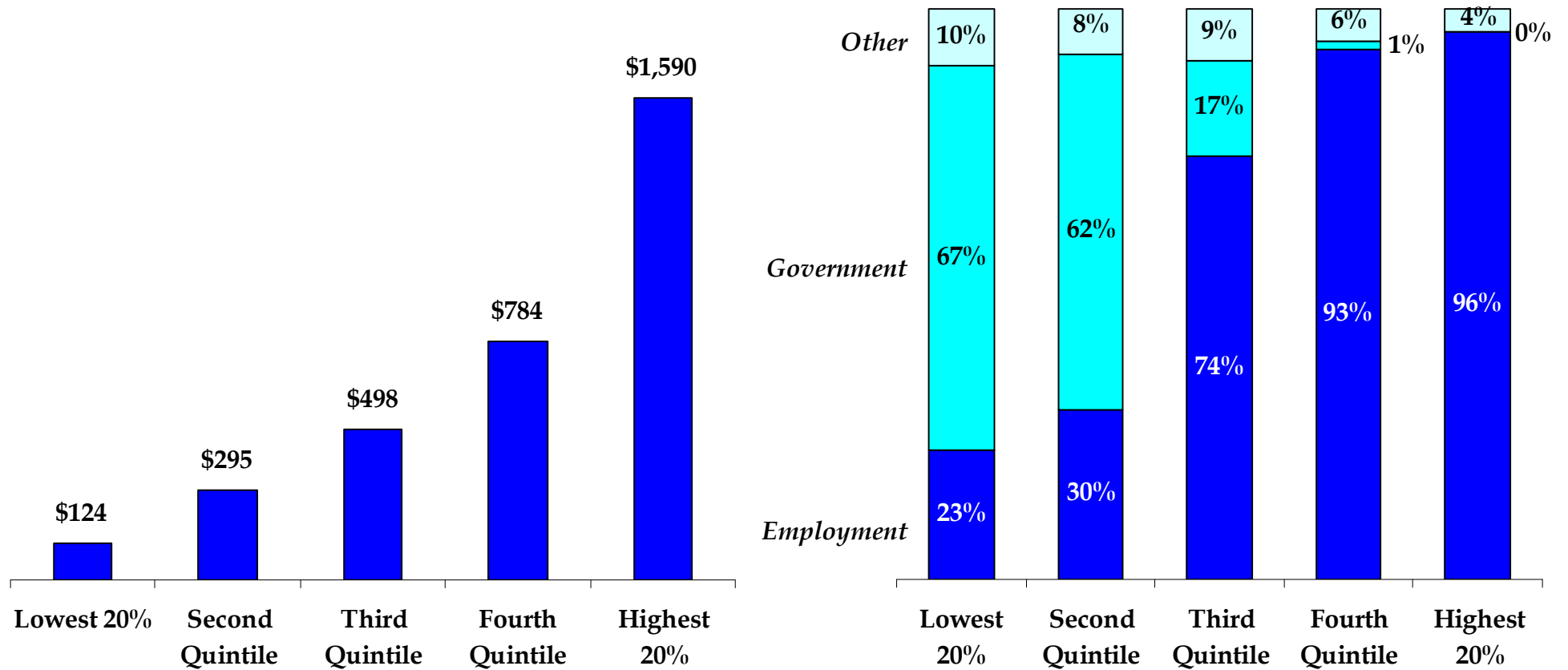
- **There is a strong base of available customers for Aldi in Australia**
- **In Australia, poorer people spend more of their income on food**
- **“Unquestionably, its formula appeals to the most economically stressed segment of our society. No matter what happens to our economy, there is always going to be 20% or more of the population that is going to find Aldi pretty attractive.”**
 - **Willard Bishop, Bishop Consulting, June 1992**

There is a strong base of available customers for Aldi in Australia

HOUSEHOLD INCOME DISTRIBUTION
(Australia by quintile¹)

Average Gross Weekly Income

Source of Income



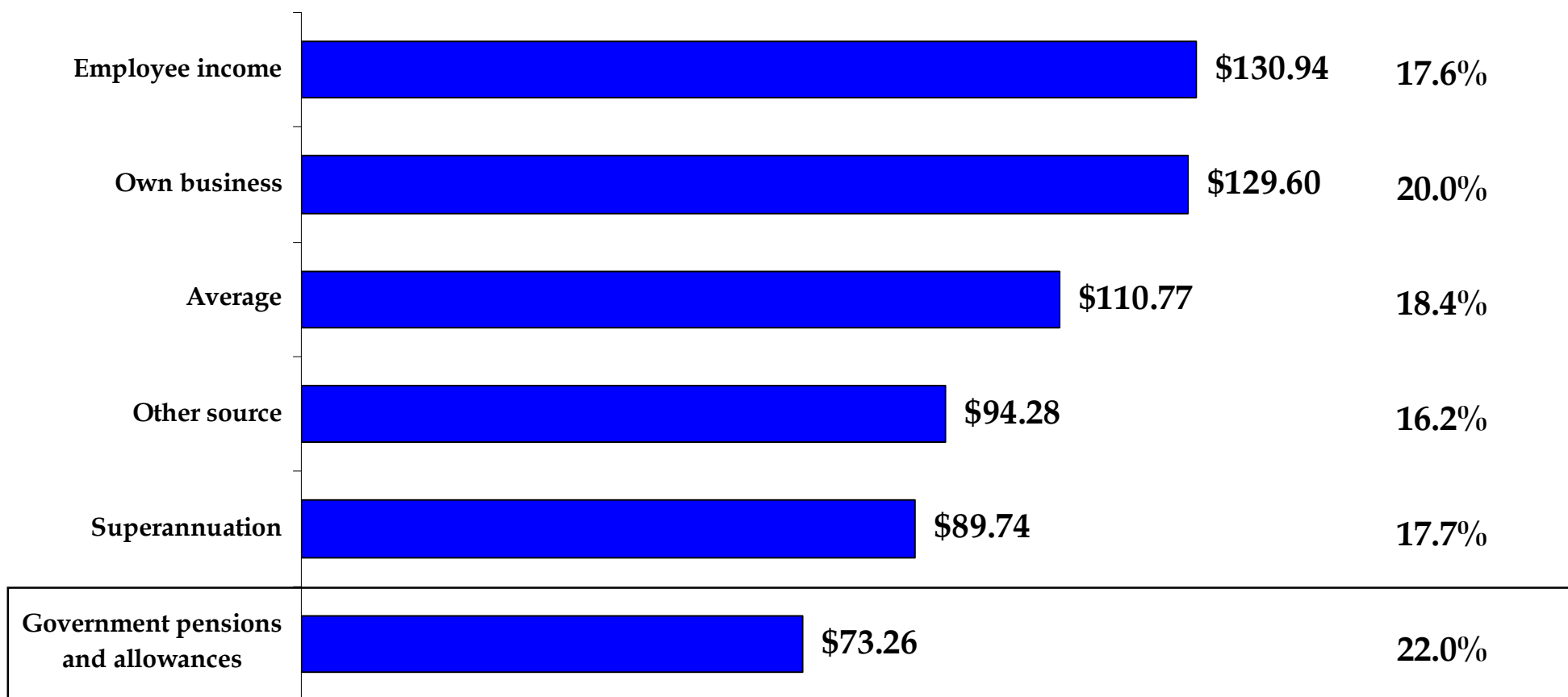
In Australia, poorer people spend more of their income on food

HOUSEHOLD EXPENDITURE ON FOOD¹

(\$; % of total expenditure)

Weekly Expenditure on Food

% of Expenditure

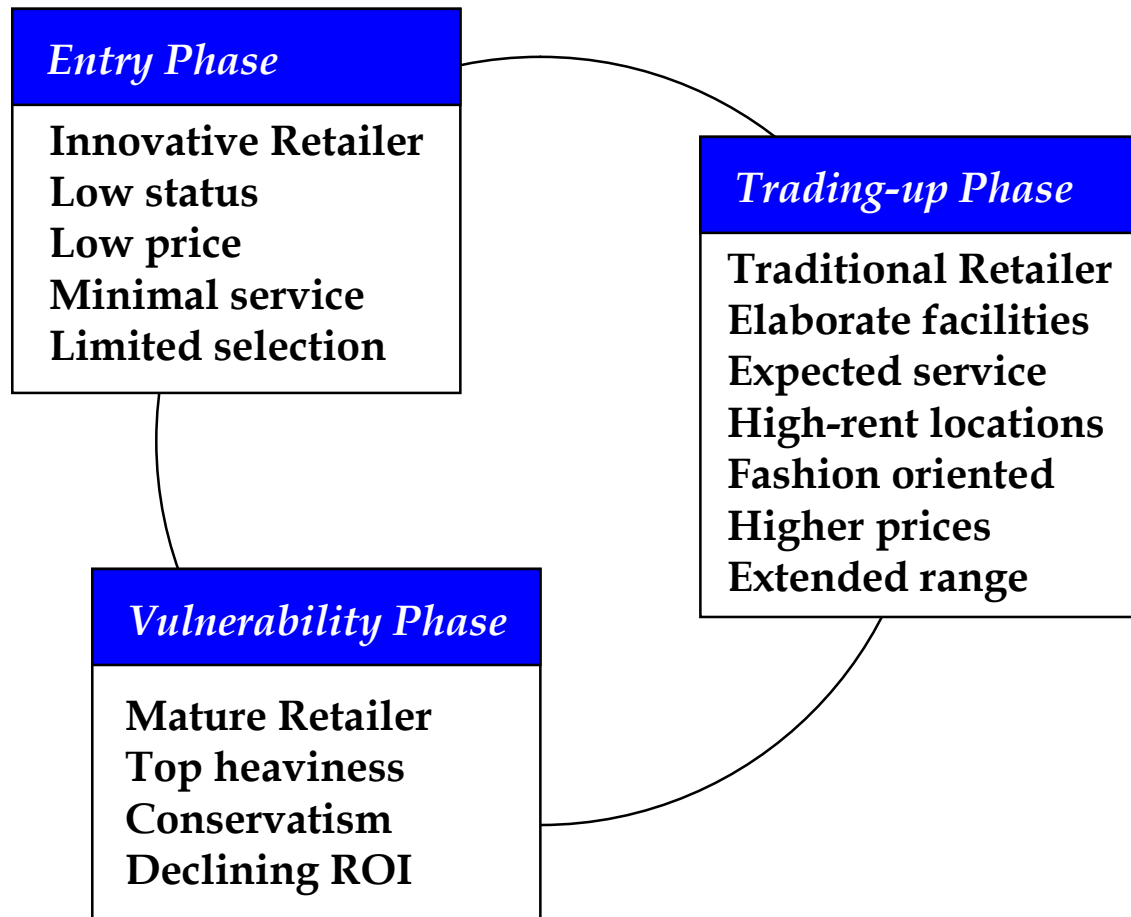


IIIc. These shoppers will primarily come from Franklins and independent supermarkets

- The “Wheel of Retailing Theory” appears to apply in Australia**
- Aldi will open a large number of stores very rapidly**
- The competitive impact of an Aldi store opening is felt most clearly by weaker players**
- We project that Franklins and Independents will be squeezed between the increased Aldi at the price end of the market and Woolworths and Coles as quality one-stop shops**

The “Wheel of Retailing Theory” appears to apply in Australia

THE WHEEL OF RETAILING



–“The company is shedding its format of selling a narrow range of mostly dry goods at cheaper prices in small outlets, instead turning Franklins into an outlet more like rivals with an emphasis on fresh food. This switch in strategy may leave Franklins vulnerable with the expected arrival later this year of German discount chain Aldi, which plans to target Franklin’s traditional market”

–Sydney Morning Herald, January 2000

Aldi will open a large number of stores very rapidly

- **The limited assortment model requires scale in purchasing to achieve lowest cost price; therefore, Aldi will roll out stores very rapidly to gain scale**
- **Aldi grows by building distribution centers, then fills in the area surrounding it with stores**

“Aldi builds up distribution capacity before it expands. It wants to have capacity in place before rolling out more stores.”

- David Shriver, Analyst, NatWest Securities

In the United States, Aldi has spread from its base in the midwest

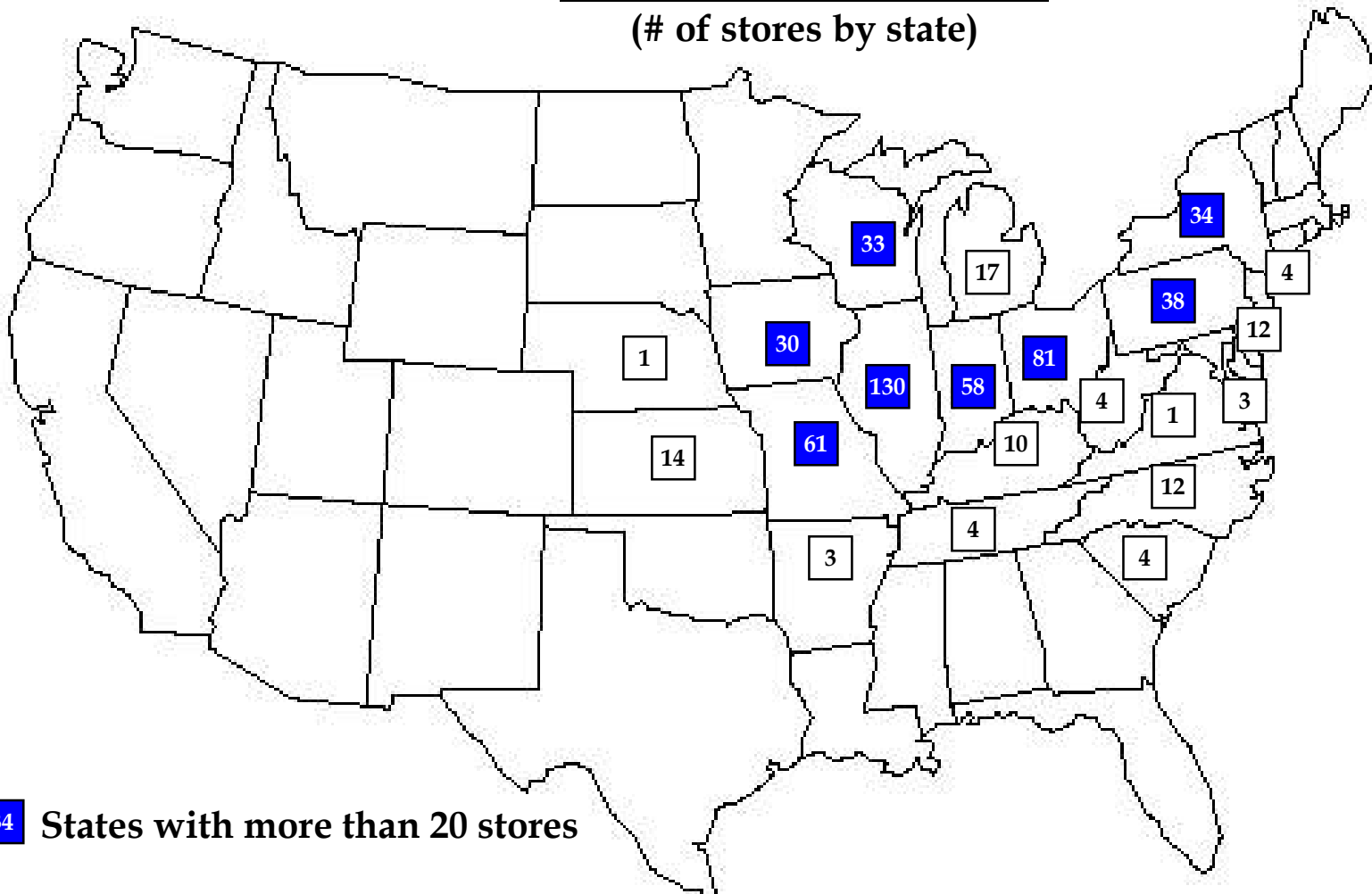
In the United Kingdom, Aldi has built a national network, but has concentrated in the depressed middle and north of the country

- **By 2005, we project 200 Aldi stores in four eastern states supported by four distribution centres**

In the United States, Aldi has spread from its base in the midwest

ALDI STORE LOCATIONS

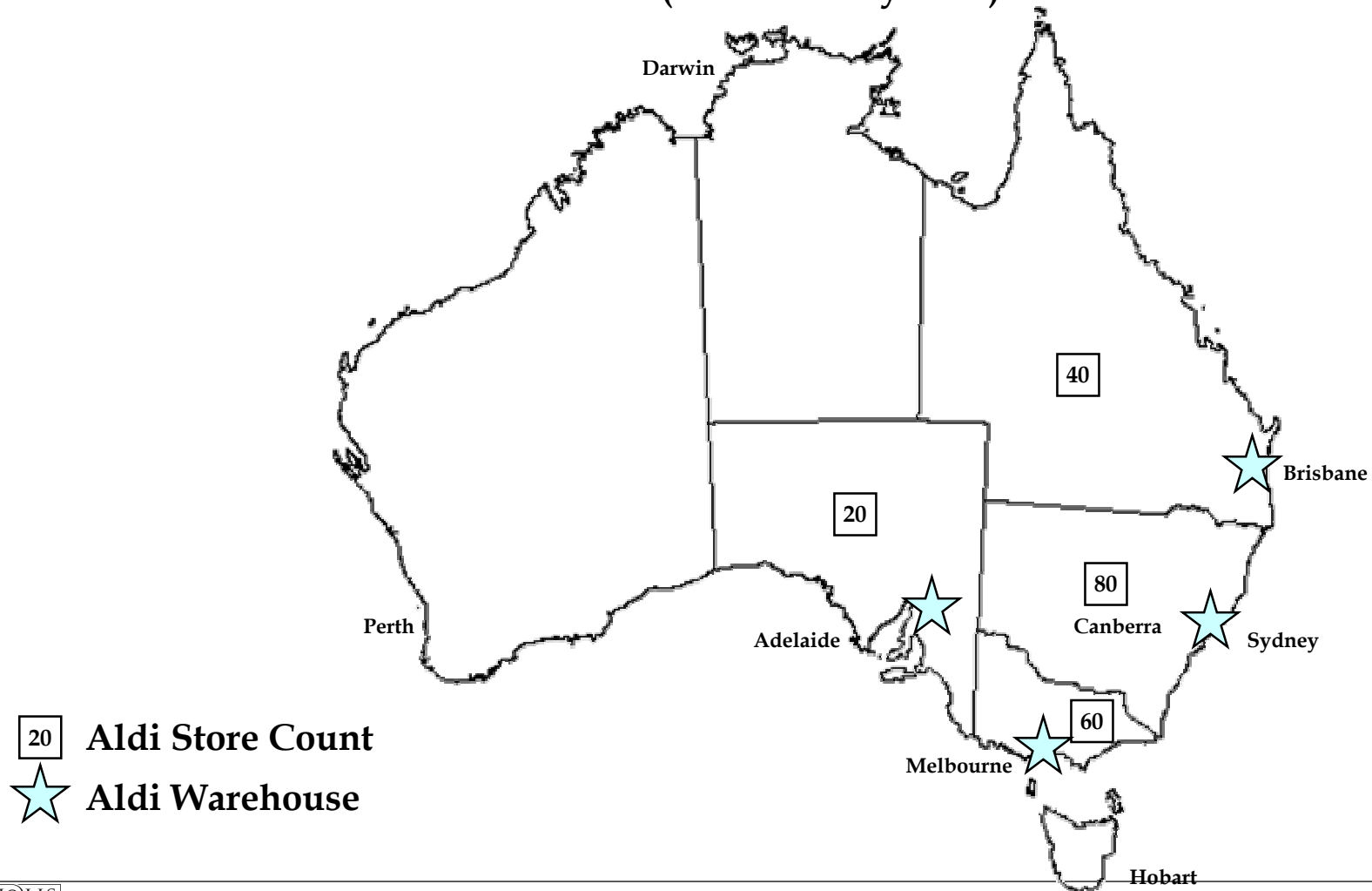
(# of stores by state)



34 States with more than 20 stores

By 2005, we project 200 Aldi stores in four eastern states supported by four distribution centres

PROJECTED ALDI STORE LOCATIONS 2005
(# of stores by state)

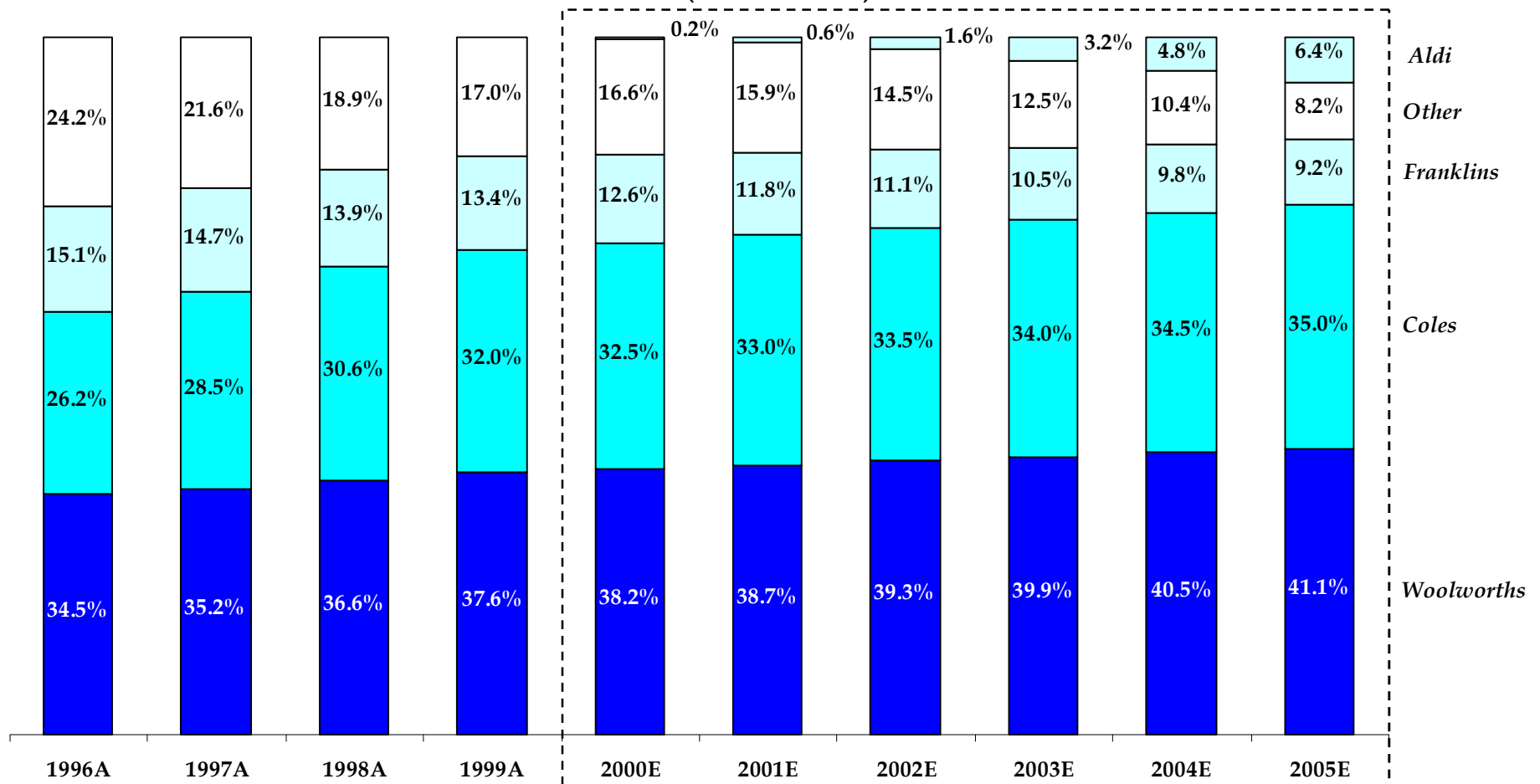


The competitive impact of an Aldi store opening will be felt most clearly by weaker players

- **“Aldi’s impact is primarily felt in small rural towns where there was not much competition, and in those areas their presence can be felt. Although they do operate in the cities, Aldi’s real strength is in rural areas where they give the local IGA a real run for their money.”**
 - **Supermarket News October 1990**
- **“The smaller, independent grocers suffered the most in the Netherlands.”**
 - **Peter McGoldrick, Irish Marketing Review, 1993**
- **“They search for less than prime locations and like to be in rural, blue-collar and/or low income neighborhoods.”**
 - **McMillan/Doolittle, February 1995**
- **“They’ve taken the cream off the top. They don’t kill anyone, but they do tend to make things on the lower end a little more competitive.”**
 - **Roger Alswager, Roundy’s Supermarkets, July 1994**

We project that Franklins and Independents will be squeezed between the increased Aldi at the price end of the market and Woolworths and Coles as quality one-stop shops

2000-2005 AUSTRALIAN GROCERY MARKET SHARE
(% of Sales)



IIIId. Aldi will restructure market-basket pricing, causing a number of lines to be sold at true net cost

- Australian supermarkets will pressure suppliers not to sell to Aldi, a move which will backfire**
- In Australia, as elsewhere, Aldi will sell a number of lines at unbelievably low prices**
- Perceptions in the food industry of Aldi and its impact in Australia are off the mark**

Australian supermarkets will pressure suppliers not to sell to Aldi...

- **“A lot of pressure was brought to bear on our suppliers in the UK to stop supplying Aldi, and when that happened I had a lot of product withdrawn from sale. Fortunately, with our connections and buying power in Europe we managed to overcome that.”**
 - **Trevor Coates, Managing Director, Aldi UK/Ireland, March 2000**

- **“We intend to talk to our suppliers if [Aldi] have lower costs so we are on a similar footing.”**
 - **Dennis Eck, Chief Executive, Coles Myer**

...a move which will backfire

- **“Certain retailers are being accused of telling certain suppliers that if they trade with Aldi they better watch out. And Aldi, rather cleverly, has informed the Office of Fair Trading that it has read such reports, and without accusing anybody, has suggested that the OFT might like to have a quick peep at what might be going on.”**
 - **The Grocer (UK), June 1990**

- **“Dear Customer, Stocks of Felix cat food are unavailable as the supplier, Quaker Oats, has refused to supply Aldi. In our opinion they consider we are selling too cheaply to you, our customer. Please accept our apologies for any inconvenience and rest assured that we will not be deterred from our policy of quality and lowest prices.”**
 - **Aldi In-store notice, UK market, 1991**

- **“Claims that Aldi was selling branded products below cost as a loss leader were investigated by the Office of Fair Trading and rejected in 1991. Nonetheless the market leaders in the food retailing sector have seen Aldi’s large discounts as a threat to their established position.”**
 - **Euromonitor 1992**

In Australia, as elsewhere, Aldi will sell a number of lines at unbelievably low prices

- **Aldi has demonstrated an ability to deliver on low prices**
- **Likely categories for a price war include:**
 - Bread and biscuits (white bread, buns, crackers)**
 - Beverages (juice, coffee, tea and soda)**
 - Canned fruit, vegetables and meals (including beans and spaghetti)**
 - Dairy (milk, butter, cheese)**
- **“Aldi uses a system that could be called “everyday loss leader.” For example, Aldi has been selling a series of corn, peas and beans at close to cost for about 10 years. When you talk to competitors, they will say, ‘Aldi sells it at retail cheaper than we can buy it. You don’t find every item marked up 10% or 11%. Some are probably marked up a lot less. They do that with their vegetables, they do it with their breads.”**
- **Willard Bishop, Bishop Consulting, June 1992**

Aldi has demonstrated an ability to deliver on low prices

ALDI PRICE ADVANTAGE

ALDI VS. JEWEL

(Chicago Conventional Supermarket)

<i>Category</i>	<i># of items</i>	<i>% ALDI Advantage</i>
Bread & bakery	13	51%
Candy & gum	11	31%
Canned goods	31	46%
Cereals	17	49%
Condiments	21	49%
Cookies & snacks	26	54%
Dairy	13	44%
Frozen	32	35%
Health & beauty	13	54%
Household	14	48%
Deli meats	22	44%

ALDI VS. SAM'S CLUB

(WalMart's Warehouse Club Store)

<i>Category</i>	<i># of items</i>	<i>% ALDI Advantage</i>
Grocery	181	28%
Non-edibles	34	27%
Dairy	20	12%
Frozen	35	4%
Deli	7	22%
Produce	9	29%
Health & beauty	15	35%

Perceptions in the food industry of Aldi and its impact in Australia are off the mark

- **“You can’t go into an environment where successful people have been operating for 30, 40, 50 years and expect to do it successfully in a very short time. We are a different formula. We will be successful as well but that takes some time. Eventually we’ll get our stores... because we are very long-term players.”**
 - **Michael Kloeters, Managing Director, Aldi Australia, April 2000**
- **“First, nobody in Germany believed that Aldi would be a success until it was too late. Everyone in Germany was thinking along the lines of one-stop shopping and service, taking for granted rising demand and increased spending power. Given lower growth, there will always be groups in a society with a need for lower prices and time to shop around - pensioners for example. Second, it should be remembered that the tendency to trade up in retailing automatically increases costs and that creates a niche for a discounter. This poses a real threat for the existing retail trade.”**
 - **Konsulten Studierejse, 1976**
- **“One thing is certain, Aldi has thrown a scare into the whole food industry and consequently into many brand marketers. They all tended to smile patronizingly at Aldi years ago, but now they are feeling the consequences.”**
 - **Advertising Age**

Australian food retailers and manufacturers should act not react to Aldi's arrival

KEY RECOMMENDATIONS

Retailers

Reduce Aldi's psychological price impact

- **Launch a value line of private label now**
- **Price this line at true cost on key items**

Avoid controversy and media coverage

- **Be careful in pressuring suppliers**
- **Be careful in site approval petitions**

Focus on perishables

- **Emphasize what Aldi lacks**
- **Create a point of difference**

Manufacturers

Produce private label for Aldi

- **Aldi is an honest and loyal customer**
- **Aldi can take Australian products to their operations in Europe and America**
- **Someone will do the business**

Develop a clear cost structure message

- **Explain true dead net cost to retailers**
- **Explain how their actions increase costs**
- **Lower prices now on key lines**

Invest in new product development