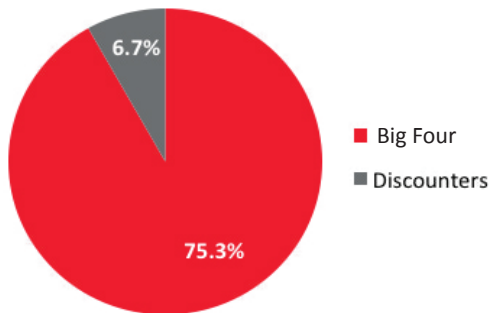


DISCOUNTERS ON YOUR DOORSTEP: WHICH GROCERS ARE MOST VULNERABLE TO DISCOUNTER GROWTH?

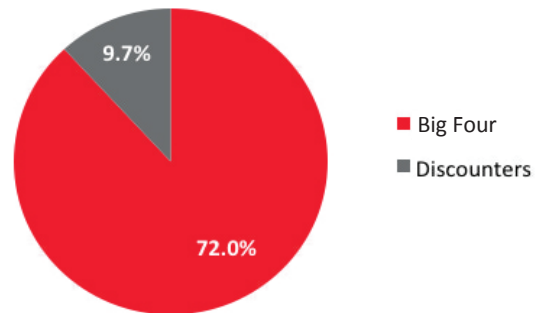
STATE OF THE MARKET

Undoubtedly, the headline news story within the grocery sector in 2015 has been the continued rise of the German discounters, Aldi and Lidl. Whilst their growth figures have slowed slightly from their highs of 20%-30% in 2014, market share analysis from Kantar for the twelve weeks ending 16th August 2015 demonstrates their continued strong growth, with Aldi increasing sales by 18% and Lidl growing by 12.8%. Recent reports suggesting that Lidl is now looking for almost 300 new sites within the M25 provides firm evidence that the growth of the discounters is set to continue. Naturally, this growth has come at the expense of other grocers, with the chart below epitomising the extent to which the Big Four of Tesco, Sainsbury's, Asda and Morrisons have been impacted by the discounters:

Market share (12 weeks to 18 Aug 2013)



Market share (12 weeks to 16 Aug 2015)



Source: Kantar

The above chart encapsulates that it is the Big Four who have been most affected by the growth of the discounters. Whilst a number of other reasons have also played a role in the Big Four's struggles, undoubtedly it has been the discounters who have been the main beneficiaries of the Big Four's loss in market share. Given Aldi and Lidl's continued success, and their well-documented ambitious opening plans, understanding which of the main grocers is currently at risk and who is most vulnerable in the future is crucial when anticipating how the sector will develop over the next five years.

DISCOUNTERS ON YOUR DOORSTEP

CACI's grocery catchment model and database, ProVision, enables us to understand which grocers are competing against Aldi and Lidl most frequently.

When looking at this analysis, first and foremost it is clear why it is the Big Four grocers who have suffered the most from the discounters' success. The average number of discounters within 1 mile and a 5 minute drivetime of the Big Four is substantially higher than for the Co-op and Waitrose, suggesting that it is typically the Big Four that Aldi and Lidl are most frequently competing against.

Retailer	Average Number of Discounters (1 Mile)	Average Number of Discounters (5 Minute Drivetime)
Asda	0.74	6.18
Co-op	0.38	4.27
Morrisons	0.72	5.10
Sainsbury's	0.62	5.64
Tesco	0.66	4.98
Waitrose	0.45	4.38

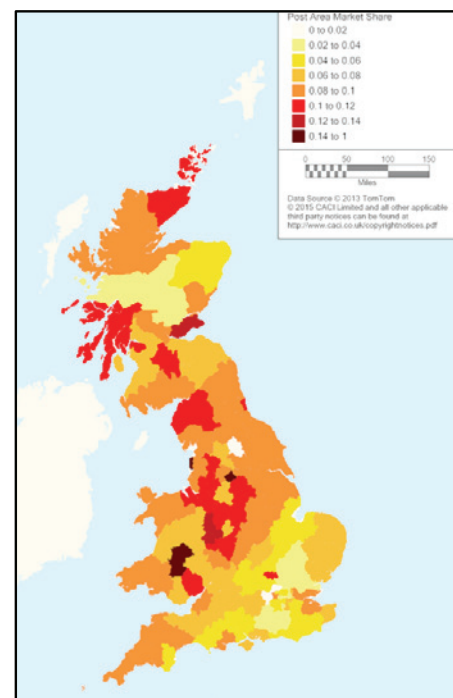
Source: CACI's ProVision

It is Asda and Morrisons who are most likely to be competing 'head-to-head' against a discounter within 1 mile. If we then look at a wider catchment (5 minute drivetime), Asda again has the highest number of discounters on average within 5 minutes, but Sainsbury's also features highly as being more likely to have a discounter in its catchment. Based on these figures, Asda and Morrisons currently look to be the most vulnerable geographically in relation to the discounters. This is relatively unsurprising given that ProVision tells us that the highest areas of combined market share for the discounters is in the Midlands and the North of England, where Asda and Morrisons are particularly prominent.

EXPANSION OPPORTUNITIES FOR THE DISCOUNTERS

ProVision also enables us to understand market share for all supermarket brands in the UK. By analysing the 'white space' for the discounters, i.e. areas where they currently have low market share, it is clear that a large number of these opportunities are concentrated in London and the South East.

Whilst Sainsbury's currently finds itself with large numbers of discounters within a 5 minute drivetime, they are also finding themselves competing head-to-head (within 1 mile) on a relatively infrequent basis. However, given the opportunities for Aldi and Lidl in London and the South East, Sainsbury's heartland, it is fair to say that the cases where Sainsbury's finds itself competing head-to-head with the discounters is likely to increase significantly over the next few years.



Combined Aldi and Lidl Market Share (Postcode Areas)

Source: CACI's ProVision

WILL SHOPPERS REMAIN LOYAL?

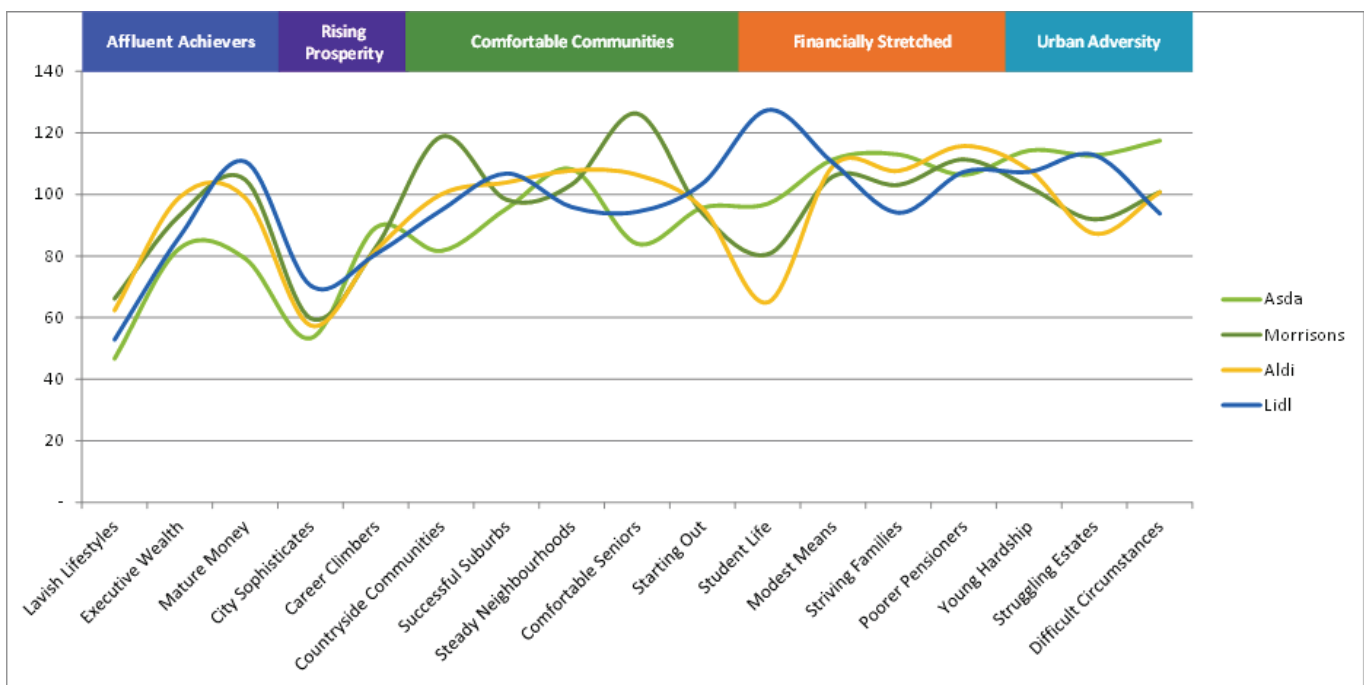
Whilst analysing the Big Four's geographic proximity to the discounters is crucial to understanding vulnerability, it is equally important to take into account which grocers' customers are most likely to also shop at Aldi and Lidl. Using a combination of CACI's Ocean database and TGI market research data, combined with our geodemographic segmentation, Acorn, we can analyse which grocers' customer profiles have the closest correlation with Aldi and Lidl's.

Retailer	Customer Profile Correlation with Aldi	Customer Profile Correlation with Lidl
Asda	67%	69%
Co-op	71%	44%
Morrisons	88%	48%
Sainsbury's	-84%	-52%
Tesco	-41%	-13%
Waitrose	-75%	-75%

Source: CACI's Ocean & TGI Market Research

As the table above shows, Morrisons' customer profile bears the closest resemblance to Aldi's, whilst Asda's Acorn mix is similar to both Aldi and Lidl's. Sainsbury's and Waitrose both have more affluent customer bases, hence the reason for the negative correlation with Aldi and Lidl's profile. However, the ongoing improvements to Aldi and Lidl's offer and ranges, along with the potential growth of both discounters in London and the South East, means that Sainsbury's in particular may find more of their customers jumping ship to the discounters in the future.

By comparing Asda and Morrisons' Acorn profiles with the discounters' customer bases, we can understand which consumer groups are most under threat from the discounters.



Acorn Profile Comparison | Source: Ocean & TGI

Whilst Aldi and Lidl have earned many plaudits and made huge strides in improving their offer and widening their appeal, the core of their customer base is still the middle to lower income groups who also are more likely to shop at Asda and Morrisons. In particular, Asda and Morrisons are competing strongly with the discounters for the Acorn groups Successful Suburbs, Steady Neighbourhoods, Modest Means and Poorer Pensioners. These are Acorn groups for whom price and value are crucial factors in determining where they shop, and with these segments constituting over a quarter of the UK population, the successful retention of these customers will play a key role in Asda and Morrisons' fortunes over the coming months.

ROUND UP

In summary, based on a combination of customer similarities and territory encroachment, Morrisons and Asda currently look to be most at risk from the discounters' ongoing growth. Whilst the progress of both discounters is taking its toll on all of the Big Four, Asda's recent sales release, which announced their worst sales performance in history, combined with the 47% drop in pre-tax profits experienced by Morrisons, provides a strong indication that it is these two retailers who are bearing the brunt of the discounters' growth. Undoubtedly, the ability of these brands to close the gap in price with the discounters without sacrificing product quality will be crucial in retaining customers. However, whilst Morrisons and Asda are currently most vulnerable to the discounters' ongoing growth, the extent and spatial distribution of Aldi and Lidl's new opening programmes will help to determine whether other grocers, and Sainsbury's in particular, are likely to be impacted more in the future.