

## **POUNDLAND / 99P STORES MERGER INQUIRY**

### **Summary of hearing with Morrisons on 23 June 2015**

#### **Background**

1. Morrisons was a national supermarket chain with 514 stores, of which 150 were convenience stores. Morrisons said that a couple of years ago it had set out a clear intent to move into the convenience and online channels as other supermarkets were moving in these directions. Morrisons said that the convenience sector allowed it to move into locations with a smaller footprint and a smaller population target, and to achieve growth. Morrisons said that the online channel gave it reach beyond its current physical estate into different parts of the country.
2. Morrisons said that its convenience stores primarily focused on its fresh food offering and that initially, roughly half of these stores' space was reserved for fresh food. It felt that this made its convenience stores unlikely to attract the same kind of shoppers as Poundland or other single-price point (SPP) retailers, which offered primarily ambient household and health and beauty products.
3. Morrisons said that while at a general level it was conscious of discounters' impact on the market, at a precise level, Poundland and other SPP retailers had not influenced its thinking. Morrisons did not have a particular strategy around the £1/99p price point and would price products at £1 where the market benchmark indicated this was the appropriate price.
4. Morrisons said that it was moving increasingly towards specific price points rather than percentage discounts as a means of attracting customers. These offerings would be communicated using large boards stating the price points in store. Morrisons said that it was increasingly pricing products at whole pound price points as it felt that customers were no longer as comfortable that percentage discounts offered good value.
5. Morrisons said that its turnover had been following the same trend as other supermarkets in the past couple of years, and similar to them had experienced declines in sales per square foot. Morrisons thought such declines were now potentially slowing.

6. Morrisons said that several different elements of its trading strategy had been designed to address these declines, for example its online and convenience offerings. It has also tried to simplify its promotional offers, reinvigorate its own brands and reduce the number of products on its shelves.

## **Morrisons' offering**

7. Morrisons said that its individual stores had limited autonomy to set trading parameters. Its ranges, pricing, marketing and store layouts were determined centrally. To a limited extent, local management defined staffing levels, and there was some discretion on the choice of promotional offers. Morrisons received a great deal of feedback from store managers and would provide short term support with promotional activity if a competitor had opened in the vicinity. Morrisons expected local store managers to notify head office if local conditions were likely to affect business, so that stock levels could be adjusted accordingly.
8. Morrisons said that through using various databases it would become aware of any new openings of Poundland or 99p Stores in the same areas as its stores. Morrisons would not adapt its offer or create any specific promotions or marketing to respond to a new opening by Poundland or 99p Stores. A centrally led response would more typically be made for another supermarket's opening (Asda, Tesco, Sainsbury's and possibly M&S Simply Food), where the materiality of the impact on Morrisons would likely be higher.

## **Competition**

9. Morrisons said that in terms of competition with discount retailers, it was more focused on Aldi and Lidl than Poundland, and that it had become more conscious of these retailers in the past two to three years. Morrisons had responded to a general downward movement of market prices, which was driven by discount stores generally. One example of this was its 'I'm Cheaper' campaign, when it moved prices on a large number of staple goods, specifically core products that it sold to a large number of its customers. This was a direct response to feedback that people were buying these items at Aldi and Lidl. This campaign largely focused on fresh produce, but also included some own-brand grocery food items.
10. Morrisons was not aware of Tesco's brand outlet initiative, but said that most big retailers would consider creating a 'bargain zone area' from time to time. Morrisons said that this was a response to situations where the customer demographic was particularly focused on price. This was sometimes designed for clearance goods and sometimes to gather a range of different goods

together for sale at a specific price point. Morrisons said that this was normally done to help the perception of value offered by a retailer. Morrisons was not aware of any of its competitors responding to Poundland and 99p Stores' offerings, but thought they all were very focused on price.

11. Morrisons did not specifically benchmark prices against Poundland and 99p Stores, but said it was possible that their prices influenced the general market and thus Morrisons' pricing indirectly. Morrisons said that the main reason it did not monitor or respond to Poundland and 99p Stores' prices was because their product ranges did not overlap greatly. Morrisons said that the largest areas of overlap were in health and beauty products, and that there was some limited overlap in some other non-food items, crisps and biscuits, and pet food. It did however benchmark Asda (on a weekly basis), Aldi and Lidl.
12. Morrisons was not aware of any specific past initiatives where it had launched different pack sizes in order to sell more products at the £1/99p price point. It was also not aware of any instances where Poundland or 99p Stores had responded to anything it had done.

## **Customer behaviour**

13. Morrisons said that every major retailer had a different view of different groups of customers and how they shopped. Morrisons divided its customers into those who had extremely busy families and were prepared to pay a bit more to get everything they needed from one shop, and those who had the time to plan their shop, visiting several different retailers to take advantage of as many offers as possible. Morrisons thought that the habits of highly price-conscious shoppers had spread much further through the population since 2008, and that UK customers were very price-aware.
14. Morrisons thought few customers of Poundland or 99p Stores would purchase the majority of their weekly shopping at these stores, simply because they sold virtually no fresh food. Even the most price-conscious customers would therefore normally have to visit another retailer such as Morrisons. Morrisons said that the way in which it used segmentation was to divide the whole customer body into groups and then target within those groups. It sought to understand the characteristics of each group, and then based its decisions on product ranges on this. For example for older, affluent 'empty-nest' customers, who tended to be fond of its counters, it would ensure that its counter product ranges were attractive to them. It noted that its price-critical customers, typically older or single-parent families, would tend to shop for certain items at a discount store such as Aldi, Lidl or Poundland in search of a better deal.

15. Morrisons said that its low price commitments were focused on a selection of products that Morrisons sold in a relatively large number of baskets. There was limited overlap with Poundland and 99p for these products, but significant overlap with the other big multiples.
16. Morrisons thought that customers shopping for a large family would tend to seek value from buying products in larger pack sizes, but was unsure of the extent to which unit equivalent prices (UEP) affected customers' shopping decisions. Morrisons compared the UEPs of like-for-like products with other retailers to check whether these were being sold more cheaply elsewhere. Morrisons said that its cheapest item in a product category also needed to match the cheapest item offered by Aldi in the same range in absolute terms.
17. Morrisons was aware that other supermarkets had dedicated sections of their stores to SPP products. It thought that this was a strategy employed on a cyclical basis and that it was not unique to the current period. Morrisons said that Asda in particular had offered SPP products a lot in the past. Morrisons said that it would potentially also explore the use of SPPs or round price points (at £1, £2 etc) in the future. Morrisons thought price deflation would continue across all retailers although the pricing of goods.
18. Morrisons showed a much greater propensity to split its basket far more frequently across a far greater range of retailers.

## **Entry and expansion**

19. Morrisons had no confirmed plans to open any new convenience stores and that this was down to a number of factors, including the difficulty of finding profitable sites. Morrisons said its expansion strategy would very much depend on how its new chief executive wanted to take the company forward. Morrisons would not specifically look for high street locations similar in size to Poundland's or 99p Stores', and said its focus was on finding profitable sites. Its convenience stores could range in size from 1,500 to 10,000 square feet. Morrisons felt the main barriers to entry and expansion would be locating suitable sites and financing their development.
20. Morrisons said that it was difficult to estimate the cost of setting up a new store and that there were no pre-determined timescales for opening one. It said the timing was very dependent on the local authority granting planning consents and the outcome of negotiations with landlords or site owners.
21. Morrisons said it was difficult for it to know what barriers existed for potential new VGM retailers as its criteria for a site to be viable were very different from theirs. Morrisons said that VGM retailers were able to successfully occupy

sites that Morrisons could not make profitable. It considered the barriers to entry for a new SPP like Poundland to be low, because it would have a wider choice of suitable sites. Morrisons said it was very unlikely that it would respond to the significant expansion of VGM retailers now or in the future.

22. Morrisons thought all VGM retailers and supermarkets could be considered to operate in a market primarily driven by value. It thought that customers had an expectation and habit of looking for value, and larger retailers were now somewhat pinned in, in terms of their pricing, by Aldi and Lidl. Morrisons did not think this situation would change. It felt that customers were showing an increasing willingness to split their shopping across a number of retailers and that this behaviour was now well-established.

### **Effects of the merger**

23. Morrisons was not in a position to comment on how the competitive dynamics of the high street might change following the transaction.