Grocery profitability outlook – Europe

CxO document

January 2025

Executive summary

- ***Looking back*****: Grocery retail margin are low compared to other industries and have been under pressure. Macroeconomic conditions and industry dynamics have negatively affected hyper/supermarkets over the past 5 years (-0.6pp EBITDA) whereas discounters increased margin (+0.2pp).** Most grocers where able to partly offset the pressure by optimizing gross margins, reducing SG&A and reducing investments
  - Grocery retail EBITDA margins average at 7.1% (2009-2023) compared to 22.9% for non-grocery retailers, 18.5% for CPG, and 15.2% for Euronext 100. On average today, hyper/supermarkets have similar EBITDA margins (6.6%) compared to discounters (6.4%). However, performance varies significantly across grocery retailers (from 4.8% to 9.2% between 2015-23) and hyper/supermarkets experienced stronger pressure over the past 5 years (-0.6pp from 2019-23) compared to discounters (+0.2pp).
  - High inflation has reduced consumer spending, impacting grocery retail volume and value growth, with a 4.5% real decline despite 23.1% nominal revenue growth (22.9pp inflation impact and 4.8pp downtrading). Ongoing industry dynamics such as increased discounter share (+2.2pp), private label share (+3.8pp), and online share (+1.9pp) further challenge profitability, especially for traditional hyper/supermarkets.
- ***Outlook:*** **0.2 to 2.7pp of EBITDA is at risk if no counter measures are taken, as over the next 5 years these trends will continue to pressure margins.**
  - The max EBITDA impact of -2.7pp would make EBITDA margins very thin (~4% on average) especially given 1-2% of revenue is required for renewal CAPEX. Continuation of historical cost optimization (1–1.5pp) will not be sufficient to counter max. trend impact.
- ***Solution:*** **The continued pressure is calling for bolder actions to avoid further profitability erosion. While many grocers are making progress, none fully accelerated their efforts.** Grocers need to do a step change across a set of levers on both growth, operational excellence and transformative change
  - Grocers should build a stronger differentiation to gain market share by focusing on elements that strengthen their value proposition e.g., excel in Fresh or Private Brands, improve their store availability and network.
  - Grocers need to excel in execution and drive profitability to compensate for the negative margin trend and focus on levers to reduce costs e.g., improving end-to-end productivity from supplier to customer (through advanced technologies).
  - Last, Grocers should fund and accelerate their transformation e.g., monetize Retail Media and modernize their IT.

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Grocery profitability in Europe…

1 *Looking back*

… are low and under pressure from macro-economics and industry dynamics

- Grocery retail EBITDA margins are 7.1% on average (2009-23), **significantly below other industries**
- **Hyper/supermarkets faced stronger pressure** compared to discounters
- **Most grocers limited EBITDA decline** through raising prices/negotiating purchase terms, reducing SG&A and lowering investments

2 *Outlook*

… will be at risk if no counter measures are taken

- **Over te next 5 years, pressure on grocers' margins will continue**, especially for hyper/supermarkets
- If no counter measures are taken, **average EBITDA impact could range -0.2 to -2.7 pp for hyper/ supermarkets**
- **Impact of trends could make super/hypermarkets EBITDA margins thin (~4% on average)** with 1-2% of revenue required for renewal CAPEX

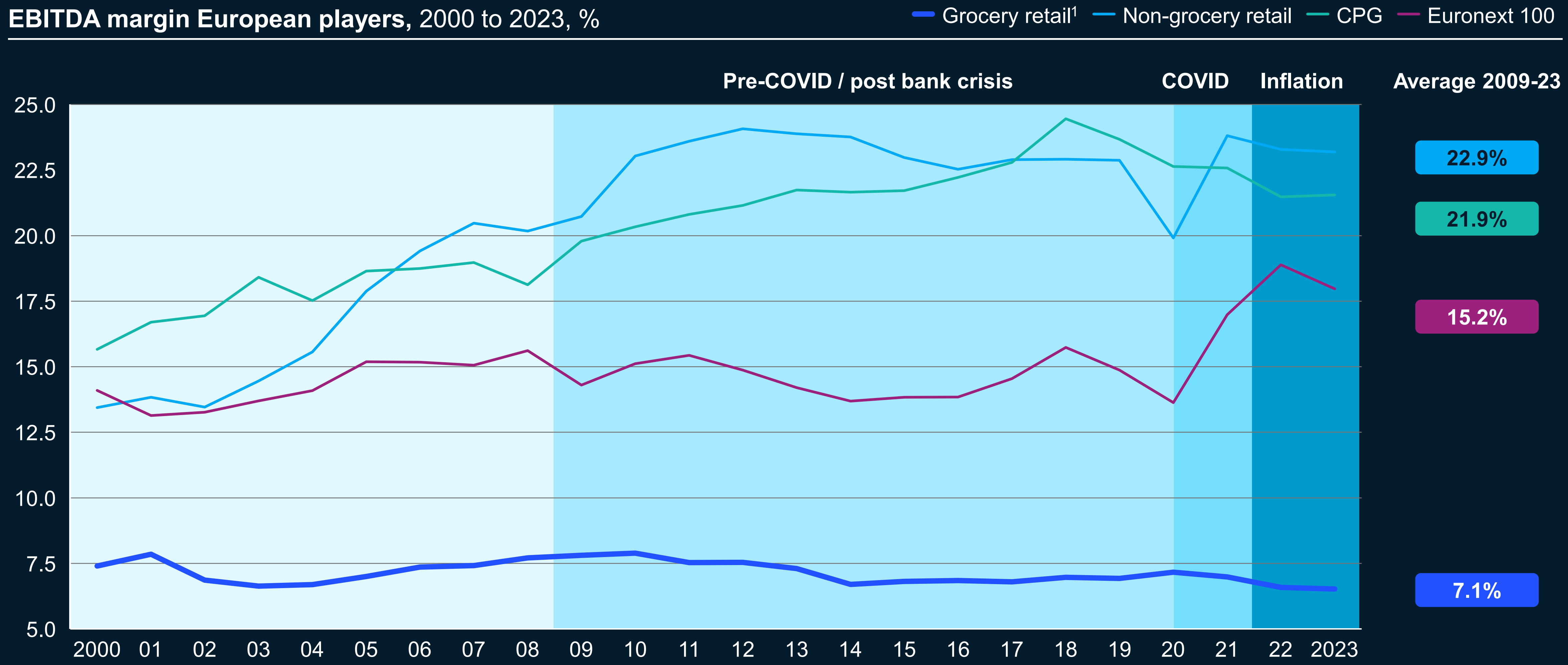
3 *Solutions*

… bolder actions are needed to avoid further profitability erosion

- **Grocers need to do a step change across a set of levers** on growth, operational excellence, transformative change
- **Bolder actions are needed** as historical cost optimization will not be sufficient and impact will heavily depend on the actions taken
- **While many grocers are making progress, none fully accelerated their efforts**

Grocery retail margins in Europe have historically been lower than other industries, averaging 7.1% EBITDA (2009-23)

EBITDA margin European players, 2000 to 2023, %



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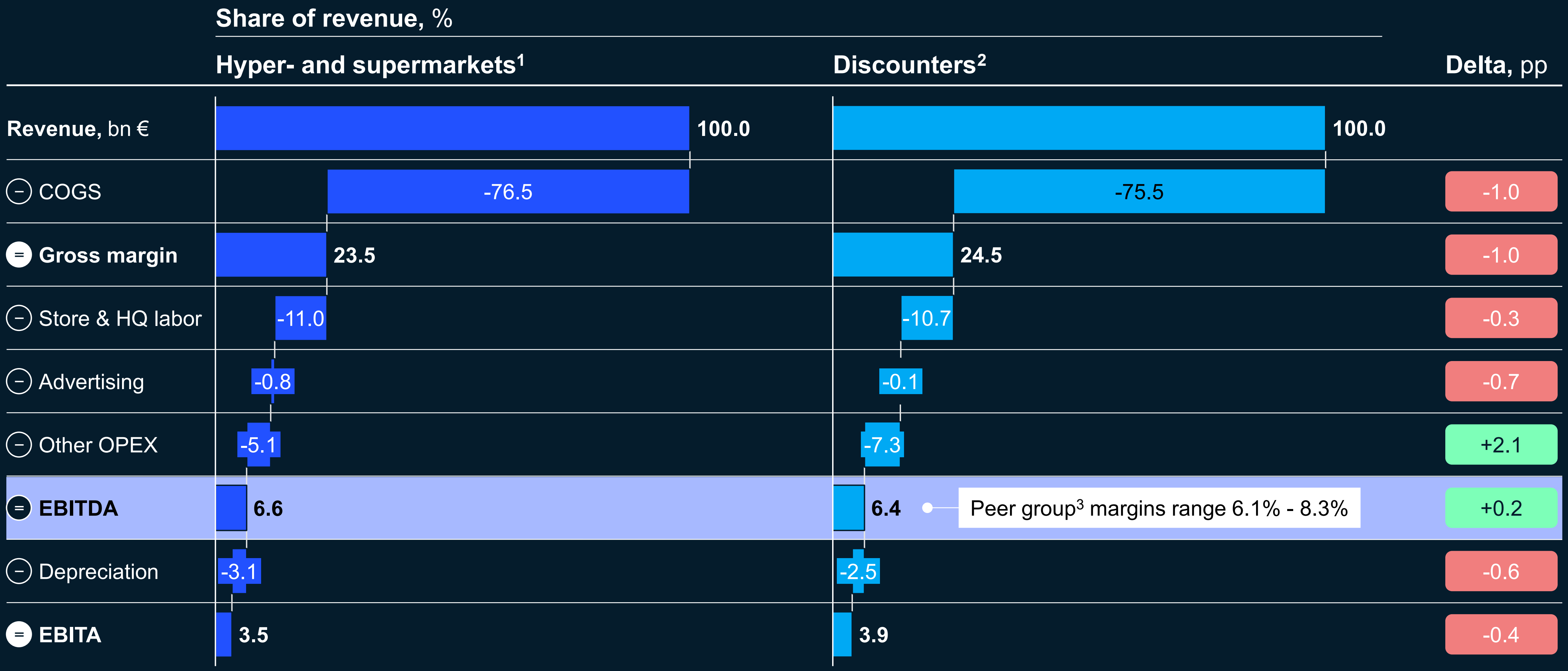
1. Ahold (NLD), LIDL (GER), Carrefour (FRA), Jeronimo Martins (PRT), Metro (DEU), Kesko (FIN), Colruyt Group (BEL), Sonae (PRT), Axfood (SWE), Dino Polska (POL)

Source: McKinsey Value Intelligence Platform, S&P Global Market Intelligence

On average, hyper/supermarkets (6.6%) and discounters (6.4%) have EBITDA margins (2023)

2023 grocery market P&L by type of retailer

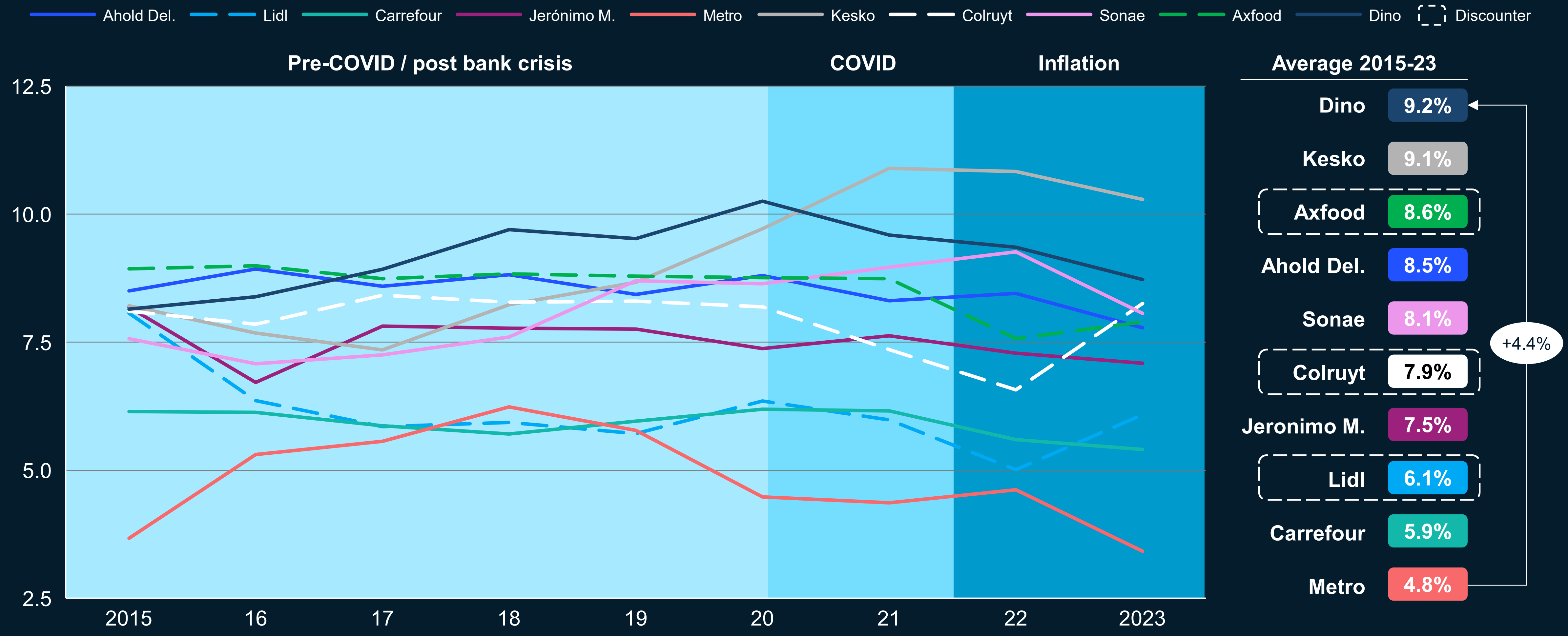


1. Ahold (NLD), Carrefour (FRA), Jerónimo Martins (PRT), Metro (DEU), Kesko (FIN), Sonae (PRT), Dino Polska (POL). Advertisement cost only reported for Carrefour and Jeronimo, equal share of cost assumed for other players | 2. Distribution cost buckets based on expert input | 3. LIDL (GER), Colruyt Group (BEL), Axfood (SWE)

Source: Expert interviews, company financial statements

Performance differs significantly across grocers with average EBITDA margins varying from 4.8% to 9.2% between 2015-23

EBITDA margin European grocers, 2015 to 2023, %



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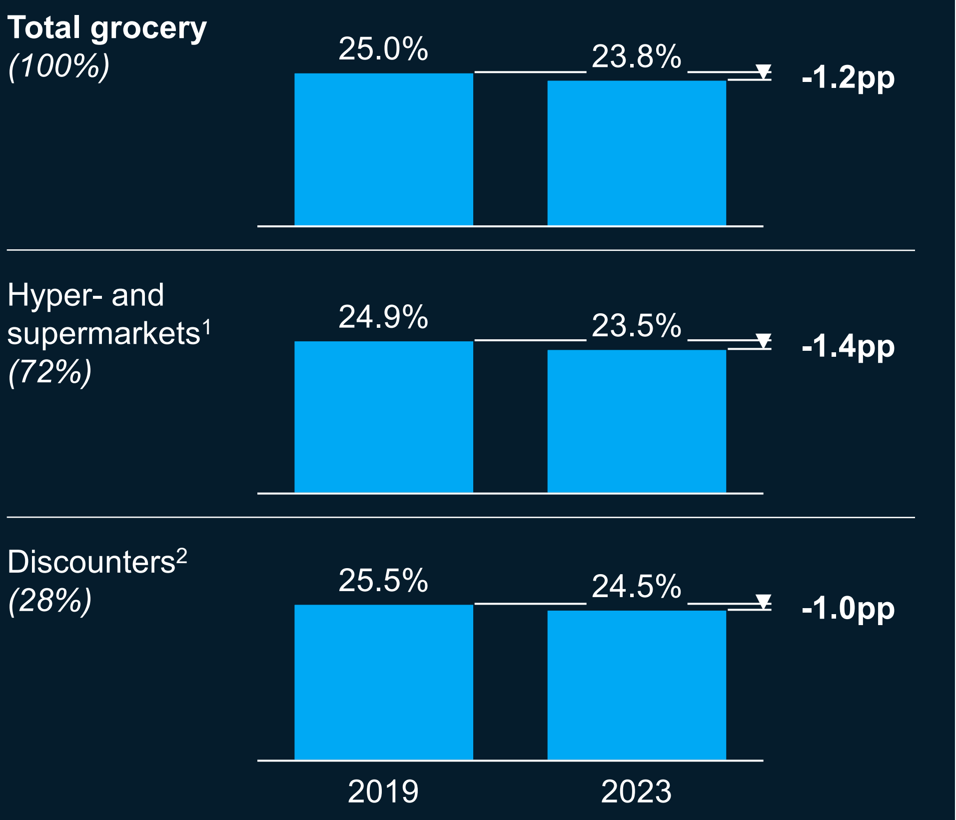
Source: McKinsey Value Intelligence Platform, S&P Global Market Intelligence

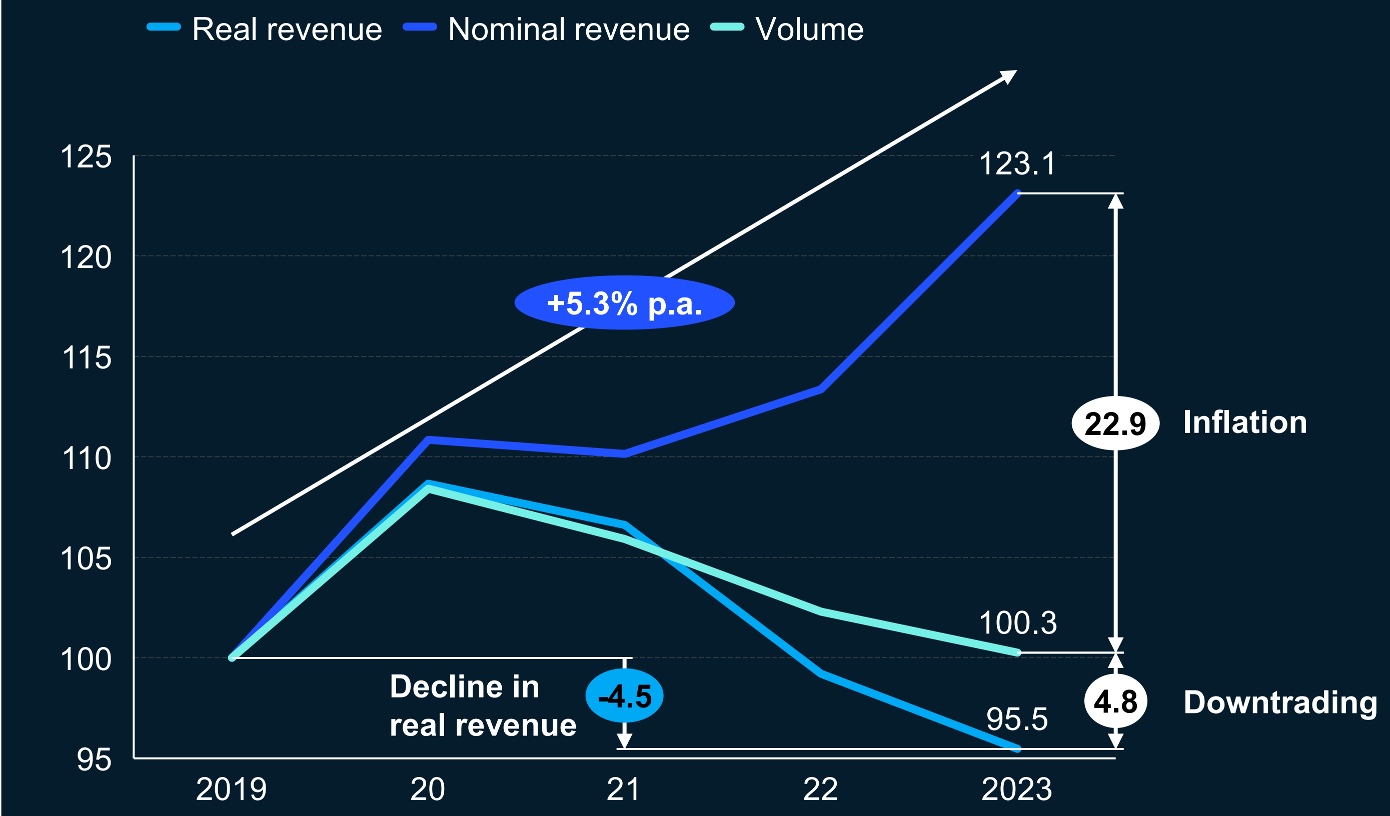
Grocers faced gross margin pressure (-1.2pp) combined with real terms sales decline (-4.5%)

Europe, Grocery retail performance 2019-2023

Channel *(%-share)* **Gross margin, %**



Grocery retail real sales development for EU-10[3]
Indexed (2019 Qx = 100%)



1. Ahold (NLD), Carrefour (FRA), Jerónimo Martins (PRT), Metro (DEU), Kesko (FIN), Sonae (PRT), Dino Polska (POL) | 2. LIDL (GER), Colruyt Group (BEL), Axfood (SWE) | 3. UK, DE, FR, IT, ES, NL, CZ, PL, PT, BE

Source: State of Grocery 2024, McKinsey Value Intelligence Platform, S&P Global Market Intelligence

With declining real sales, especially offline, sales per square meter have also decreased, putting pressure on margins

EU11[1], 2019 constant prices, indexed to 2019, %

x CAGR, %

Driver	Supermarkets	Hypermarkets	Discounters

Real offline sales

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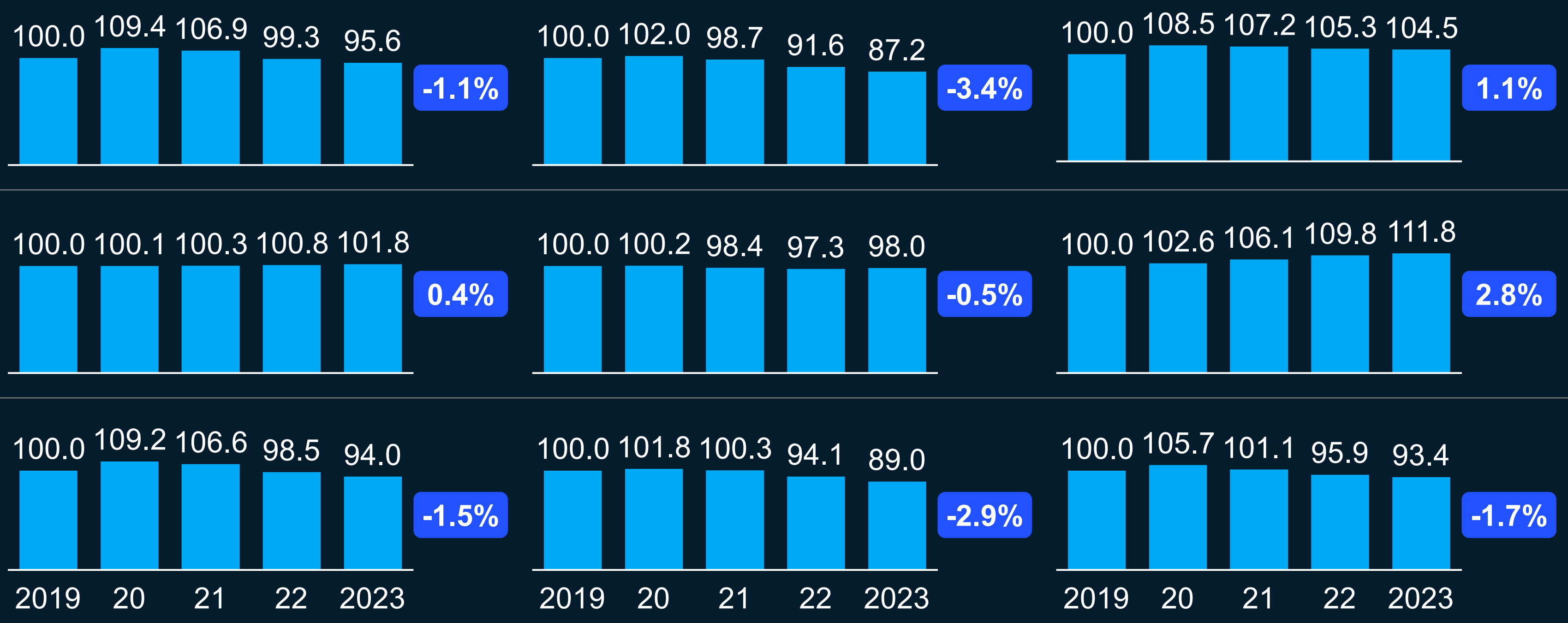
Total sqm

=

Real offline sales per sqm



Real offline sales driven by -7% decline in total offline market (2019–2023) and **shifting market shares**:

- **Supermarkets**: from 36.3% to 36.4% **(+0.1%)**
- **Hypermarkets**: from 20.3% to 18.6% **(-1.7%)**
- **Discounters**: from 19.6% to 21.4% **(+1.9%)**

Conclusion

Decline in supermarket real sales per sqm (-1.5% p.a.) as **lower overall sales (-1.1% p.a.) amplified by increase of total floor space (+0.4% p.a.)**

Hypermarkets saw largest decline in real sales per sqm (-2.9% p.a.) with **sales decline (-3.4% p.a.) only partly offset by reduction in floor space (-0.5% p.a.)**

Decline in discounter real sales per sqm (-1.7% p.a.) due to **increase in discounter floor space (+2.8% p.a.) outpacing the growth in sales (+1.1% p.a.)**

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1. UK, DE, FR, IT, ES, NL (excl. hypermarkets), CZ, PL, PT, BE, SW

Source: State of Grocery 2024, IGD, Eurostat

Margin pressure is the result of both macroeconomic conditions and industry dynamics in Europe, especially for traditional grocers

Historic trend (2019-23)

Macroeconomic

High inflation post COVID-19

High inflation (4.8% p.a. HICP inflation since 2019) impacted **cost structure of retailers.** Retailers passed ~95% of the inflation to consumers, deteriorating margin

Declining consumer spending power

Consumers have become more conscious (saving 15% in 2023 vs 13% pre-COVID19). **Lower spend levels** negatively impacts **volumes** and stimulates **trading down**, providing opportunity for discounters and challenge for traditional grocers

Industry dynamics

Growing share of discounters

+2.2pp share of sales of discounters further **driving down volumes of hyper- and supermarkets** and requiring to offer competitive entry level assortment

Growing share of private label

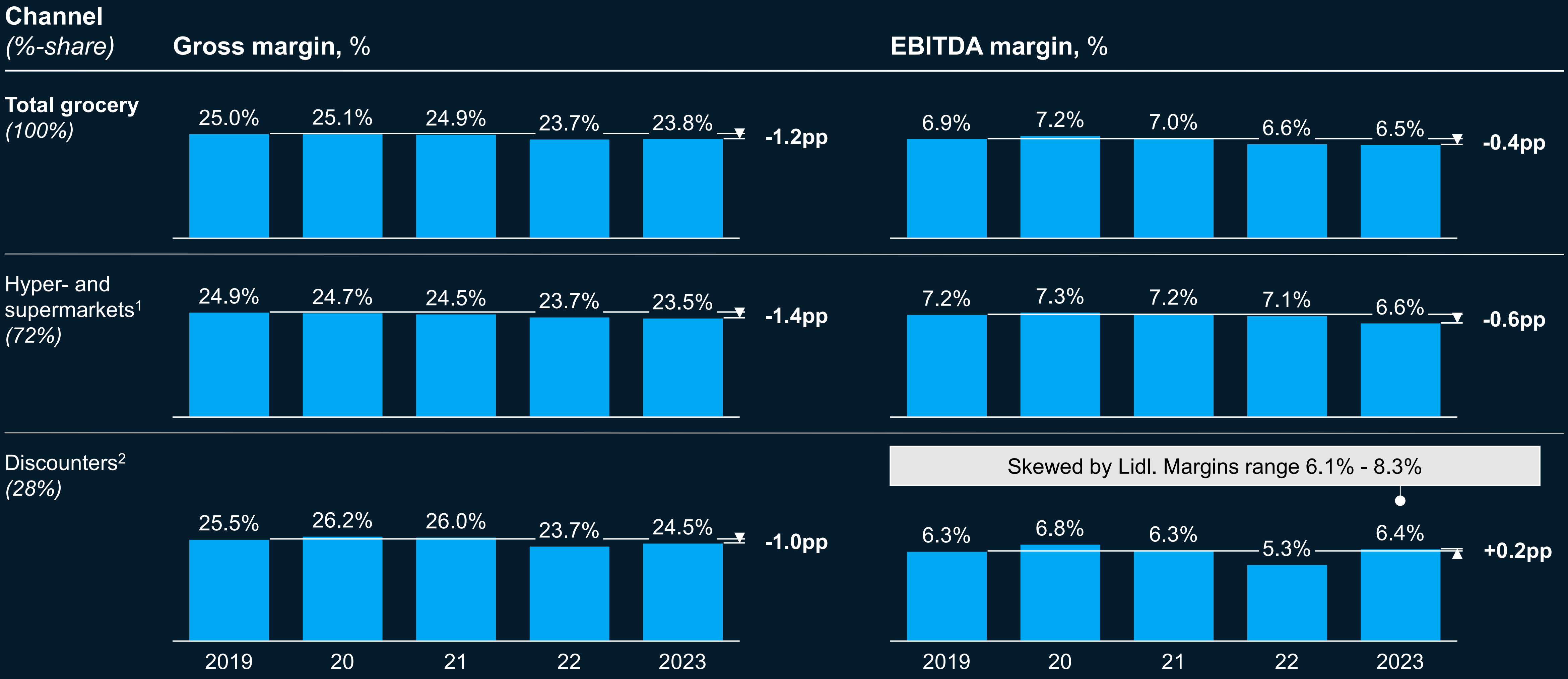
+3.8pp share of sales of private label. **Private label products have a lower price**, but larger gross margin %. Depending on the mix, this results in an EBIT(D)A margin uplift / pressure

Growth of online grocery sales channel

1.9 pp increased online share. **Online channel is margin dilutive** for most traditional players

EBITDA margin of super/ hypermarkets (-0.6pp) shows negative momentum vs discounters (+0.2pp)

Europe, Grocery retail performance 2019-2023



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Source: State of Grocery 2024, McKinsey Value Intelligence Platform, S&P Global Market Intelligence

Grocers limited EBITDA margins decline (-0.4pp) by raising prices/ negotiating purchase terms and reducing SG&A and other costs

🟥 Cost increase / margin decrease 🟩 Cost decrease / margin increase

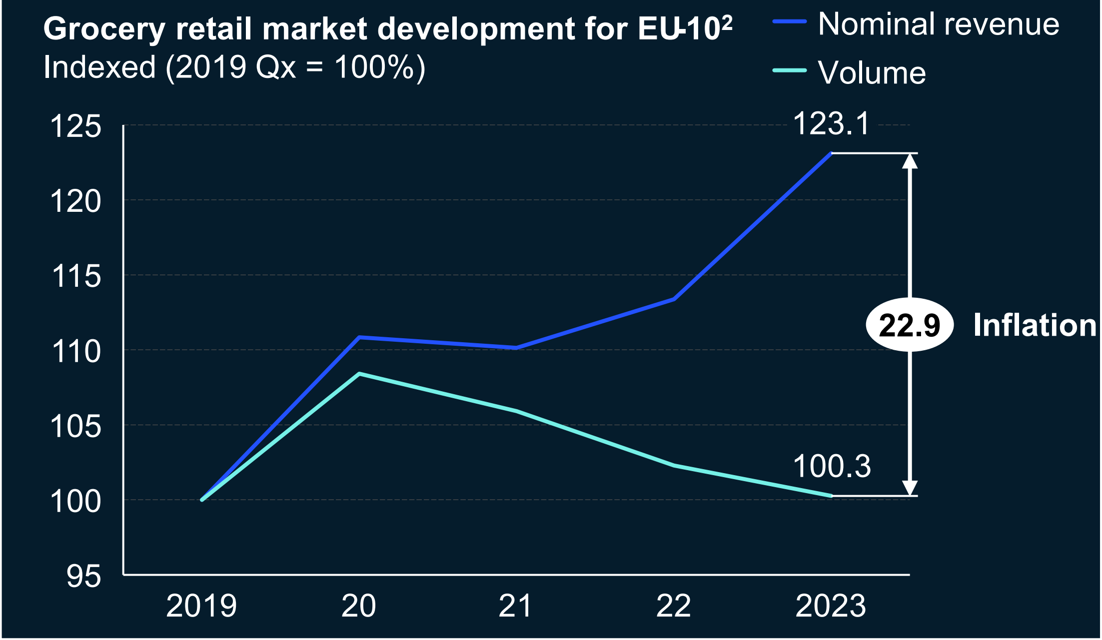
Total grocery P&L[1], as % of revenue

	2019	20	21	22	2023	**Δ 2019-23**, pp
Revenue, bn €	100	100	100	100	100	
⊖ COGS	75.0	74.9	75.1	76.3	76.2	🟥 +1.2
⊜ **Gross margin**	25.0	25.1	24.9	23.7	23.8	🟥 -1.2
⊖ SG&A & other OPEX	18.1	18.0	17.9	17.2	17.3	🟩 -0.8
⊜ **EBITDA**	6.9	7.2	7.0	6.6	6.5	🟥 -0.4
⊖ Depreciation	3.3	3.2	3.2	2.9	2.9	🟩 -0.4
⊜ **EBITA**	3.6	4.0	3.8	3.6	3.6	-

! **2023 CAPEX reinvestment[3]** was at lowest level since 2000, reflected in lower depreciation

⚠ Based on P&Ls of publicly listed grocery retailers, thus skewed towards traditional super/hypermarkets, as major European discounters are privately owned

Despite high inflation, COGS only increased by 1.2pp, meaning that **most (95%) of the inflation was passed to consumers**



Grocery retail market development for EU-10[2]
Indexed (2019 Qx = 100%)

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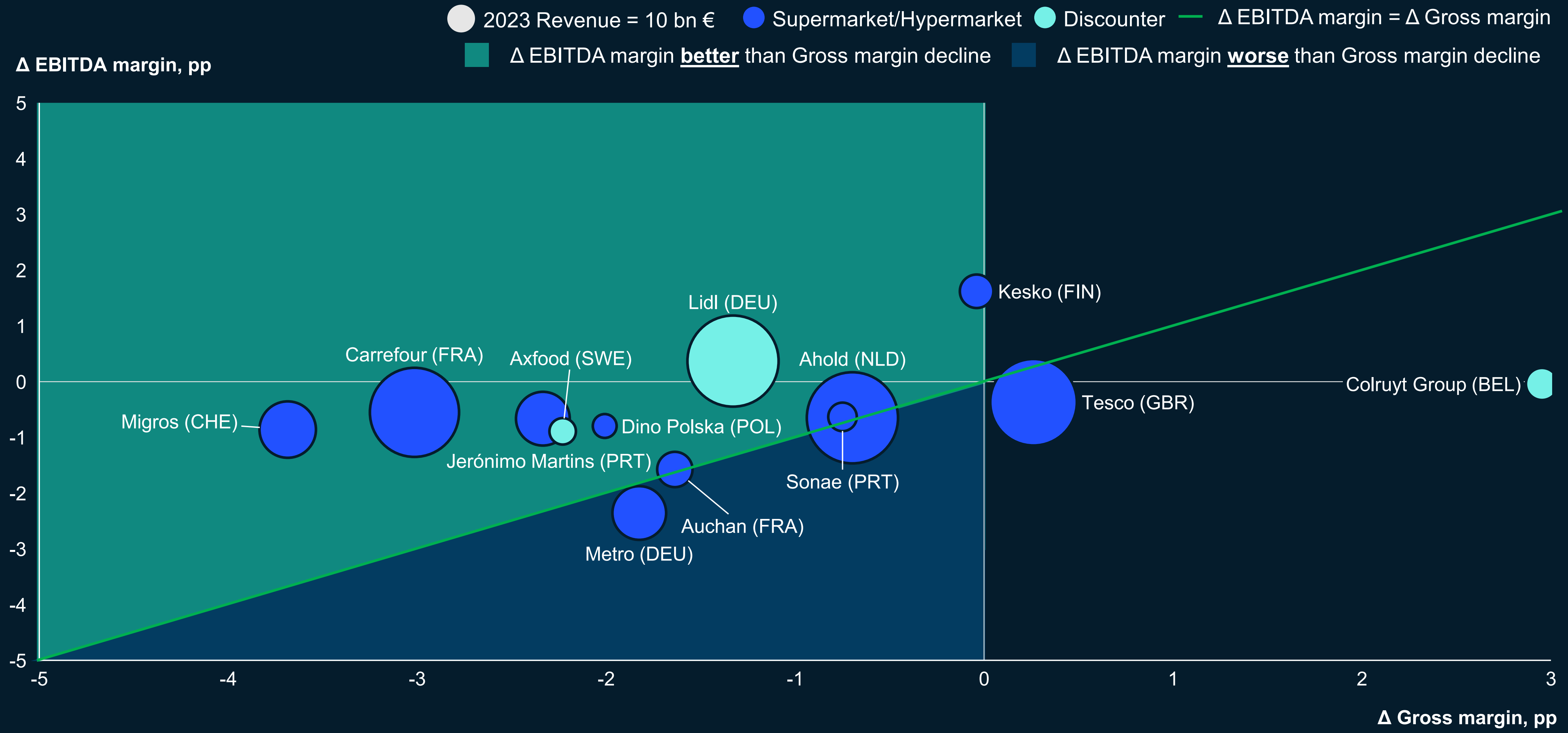
Source: State of Grocery 2024, McKinsey Value Intelligence Platform, S&P Global Market Intelligence

Most grocers partly offset inflationary gross margin decline to limit EBITDA margin decrease

2019-2023 change in margin for grocery retailers in Europe



Source: McKinsey Value Intelligence Platform, S&P Global Market Intelligence

Examples of grocers' actions to raising prices/negotiating purchase terms to optimize gross margins

Ahold Delhaize

- Reopened **price negotiations** across brands in effort to offset inflation
- **Removed Nestlé products** (including Maggi, KitKat, and Nescafé) from its stores **because of increased prices**

"We did have some **tough negotiations with Nestlé** ... it was a place where we said **we just don't take prices** if they're **not acceptable proposals**"

– Natalie Knight, Albert Hejin CFO

colruyt

- Engaged in **purchasing alliances** with European Marketing Distribution (EMD) and AgeCore **to improve its negotiation position** with both private label manufacturers as well as brand manufacturers

“The partnership with EMD gives Colruyt Group access to a wider European network of private label suppliers... [and] will also **improve purchasing conditions**”

- Geert Roles, Colruyt Group, CPO

ALDI

- Launched **various sourcing optimizations** such as jointly sourcing private labels between Aldi Nord and Aldi Süd and unifying the international assortment to boost negotiation power
- **Suppliers are often located near ALDI’s distribution center**, to minimize transportation and operating costs and ensure efficient logistics

TESCO

- **Increased decision power of category managers** over purchasing, pricing and promotions to obtain full product understanding, including cost breakdown and typical margins, benefiting negotiation capabilities

“The resulting product understanding [of increasing Category managers decision power] provides **a substantial benefit in supplier negotiations** for private label and national brands”

- Head of Trading Grocery, Tesco

Source: Press search

Examples of grocers' actions to reduce SG&A and other structural cost items to stabilize EBITA margins

MIGROS

- **Executed a cost restructuring program to create a leaner, more agile organization** with simplified processes and clear roles, reducing 150 full-time positions at Migros Supermarket AG's Zurich headquarters

Carrefour

- Launched a bold cost restructuring plan to **achieve €4 billion in savings** by 2026:
  - **Transferred 39 underperforming French stores** to independent operators to cut operating costs and improve profitability
  - Reduced nearly 1,000 headquarters roles through voluntary departures to streamline operations and lower administrative expenses

TESCO

- Launched cost savings program planned to **mitigate inflation effects** (2022) including:
  - **Savings of £1bn** through GNFR[1], property, store and distribution operations, and central overheads
  - **Removal of counters in 317 stores**
  - **Store conversion** and closure

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1. Goods and Services not for Resale (GNFR)

Source: Press search

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… will be at risk if no counter measures are taken

- **Over te next 5 years, pressure on grocers' margins will continue**, especially for hyper/supermarkets
- If no counter measures are taken, **average EBITDA impact could range -0.2 to -2.7 pp for hyper/ supermarkets**
- **Impact of trends could make super/hypermarkets EBITDA margins thin (~4% on average)** with 1-2% of revenue required for renewal CAPEX

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- **Grocers need to do a step change across a set of levers** on growth, operational excellence, transformative change
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Over te next 5 years, macroeconomic and industry dynamics will continue to put pressure on grocers’ margins, especially for hyper/supermarkets

1. Continued higher food inflation

Food inflation is expected to be **~2.2% p.a.** and will erode retailers’ margins if only **90-100%** of inflation can be passed on to consumers

2. Continued labor market tightness

Wage inflation is expected to stabilize at **~2.5% p.a.**, but at an elevate level compared to historic rates due to tight labor markets. If retailers can only pass **90-100%** of inflation to consumers, margins are negatively affected

3. New diabetes and obesity drugs (GLP-1)

Households with GLP-1 drug users cut overall grocery spending by **~6-11%**, by reducing purchases of calorie-dense, processed foods and snacks. The growing demand for GLP-1 drugs, with the number of users potentially reaching **~4-9%** of the EU population by 2029, could result in further decline in retailers' revenue and profit margins

4. Continued market share erosion to discounters

Discounters are expected to grow their market share by **0.9-3.8pp**, up to **23-26%** of the total retailers market, though at a lower pace than historically

5. Increasing share of private label

Private label share is expected to grow by **3.1-5.6pp** (in line with historic rates) up to **31-33%**. Due to the higher margin of these products, this will positively impact profitability of hyper/ supermarkets

6. Growing share of online

Share of online is expected to increase from 6% to **7-9%**. Online business is still margin dilutive with 5-10pp lower EBITDA margin, but will likely improve over time

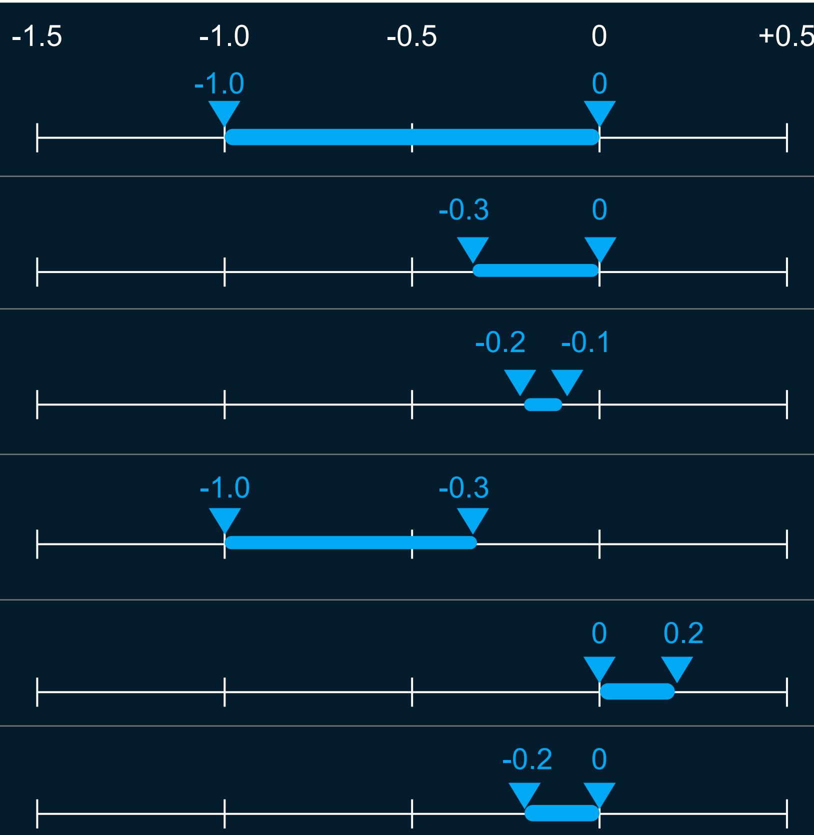
If no counter measures are taken, average EBITDA impact could range -0.2 to -2.7 pp for hyper/supermarkets

The potential profit impact of each trend individually for a normative hyper/supermarket based on the current P&L structure

xx Deep dive follows

			Outlook (2023-29)
Macro-economic	1	**Continued higher food inflation**	**2.2% p.a.** food COGS inflation, with **90-100%** passed on to consumers
	2	**Continued labor tightness**	**2.5% p.a.** labor cost inflation, with **90-100%** passed on to consumers
	3	**Growing adoption of new diabetes and obesity drugs (GLP-1)**	**6-11%** drop in grocery spending among households with GLP-1 drug users
Industry dynamics	4	**Continued market share erosion to discounters**	**+0.9-3.8 pp** growth in discounters share to 23-26%
	5	**Increasing share of private label**	**+3.1-5.6pp** growth in private label volume share to 31-33%, with 5-10pp higher EBITDA
	6	**Growing share of online**	**+1-3 pp** growth in the share of online up to 7-9%, with 3-6pp lower EBITDA

Impact profitability by 2029, EBITDA pp.



Total -2.7pp to -0.2pp

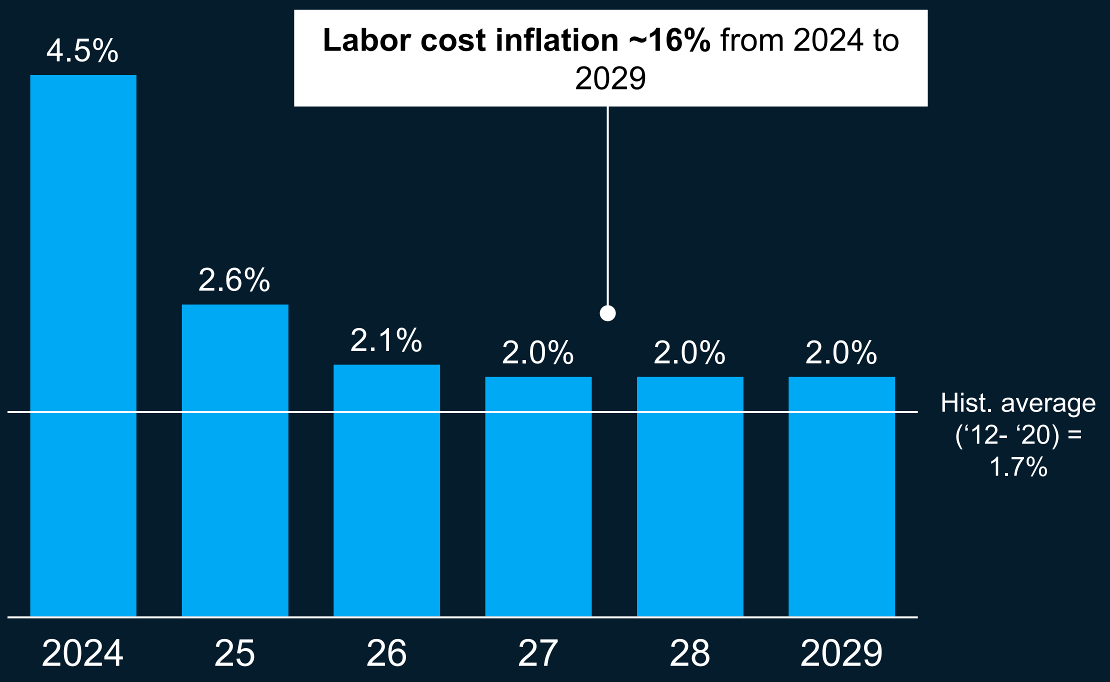
② Labor inflation projected to stabilize above historical average at 2% with peaks of 4.5% and 2.6% in 2024 and 2025

Labor markets in European economies have been tightening since 2010…

Job vacancies per unemployed person

… resulting in a higher than historical labor cost inflation, expected to peak in 2024 - 2025

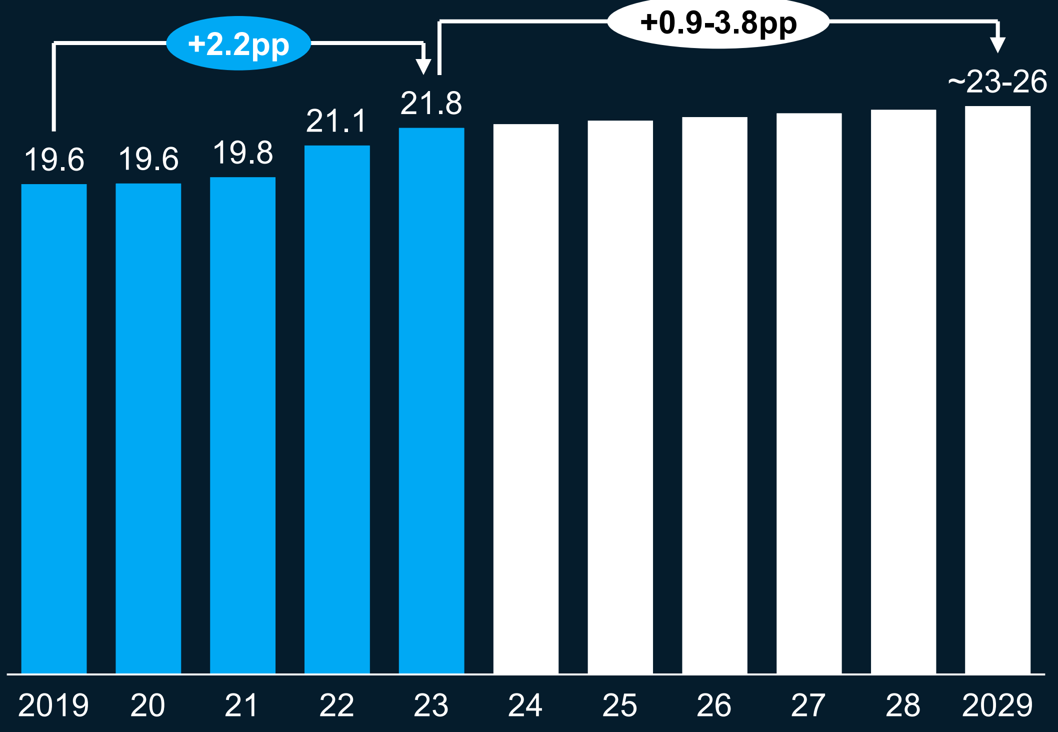
ECB projections labor cost inflation 2024 - 2029, %



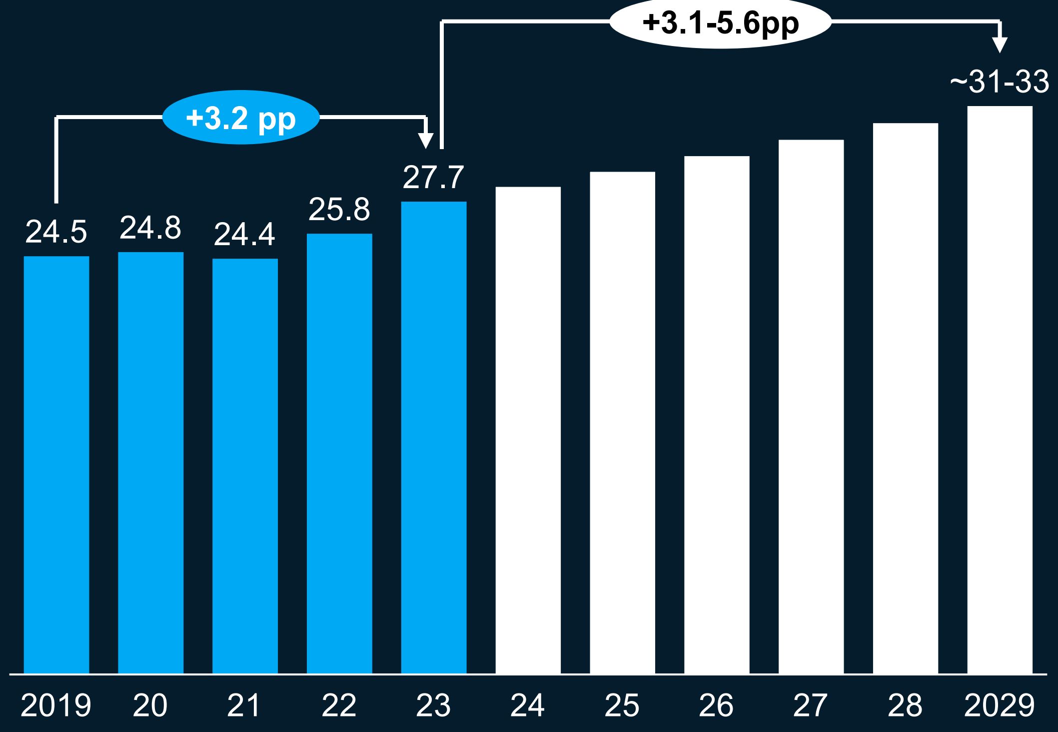
Source: ECB, International Labour Organization, Eurostat, UK Office for National Statistics, Ministry of Health, Labor and Welfare, McKinsey Global Institute analysis

④ ⑤ Discounter share (23-26%) and private label share of hyper/supermarkets (31-33%) expected to increase by 2029

Discounter share of sales[1], EU[2], %



Private label share of hyper/supermarkets volume[3], EU[2]



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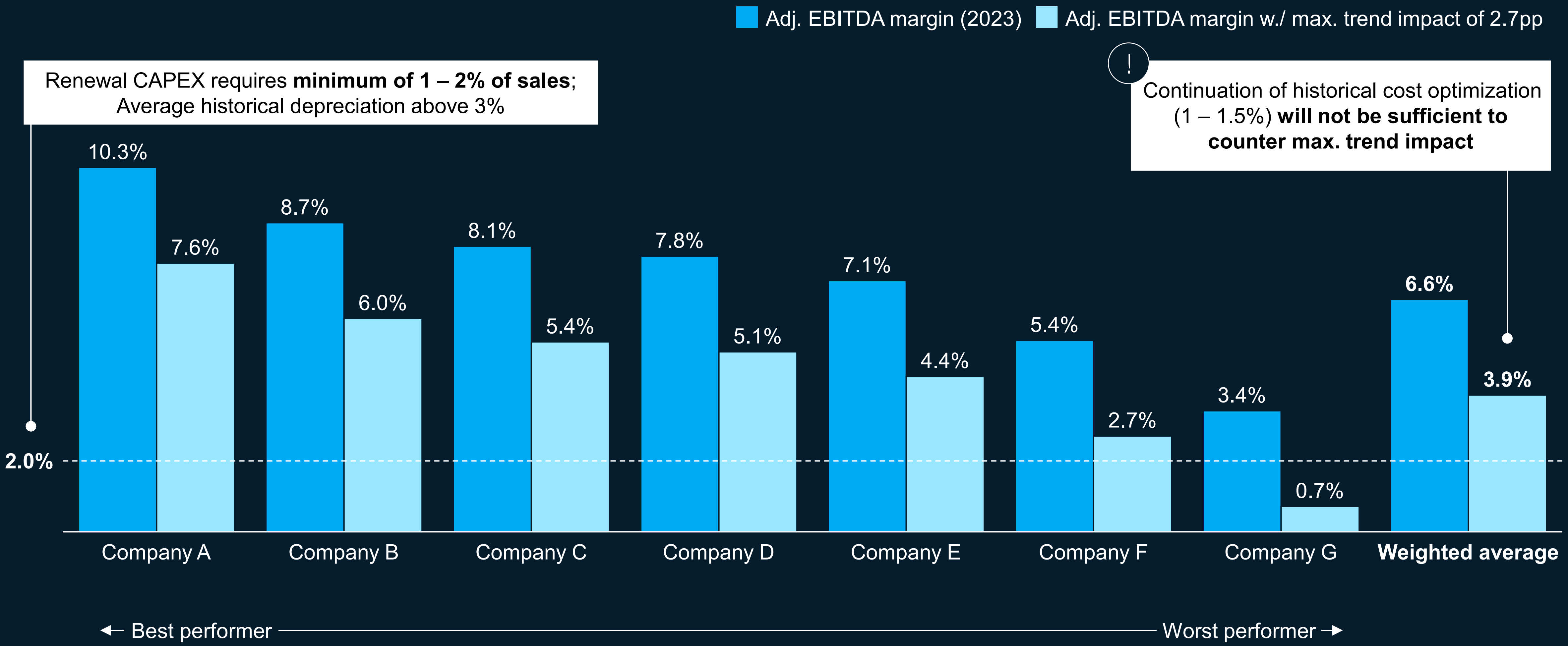
1. Low case 23% share is based on analysis on correlation of average grocery price spread and discounter share growth per country and high case 26% share is based on historic ('19-'23) CAGR
2. UK, DE, FR, IT, ES, NL, CZ, PL, PT, SE, BE
3. Low case 31% share based on extrapolating 2019-2022 growth rate, as the uptick in 2023 likely explained by delayed effect of COVID-induced inflation and high case 33% share is based on extrapolating 2019-2023 growth rate

Impact of trends could make super/hypermarkets EBITDA margins thin (~4%) with 1-2% of revenue required for renewal CAPEX

Trend impact on adjusted EBITDA margin on selected peer group hyper/supermarkets, %



Renewal CAPEX requires **minimum of 1 – 2% of sales**; Average historical depreciation above 3%

Continuation of historical cost optimization (1 – 1.5%) **will not be sufficient to counter max. trend impact**

Source: McKinsey Value Intelligence, McKinsey Analysis

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Taking a future-back perspective, bolder actions across levers needed to avoid further profitability erosion

◔ Potential EBITDA impact xx Deep dive follows

Build stronger differentiation to gain market share

1	Excel in Fresh quality	◔
2	Step-up private label quality and develop private brands	◔
3	Improve store availability and reshape the store network	◕
4	Win on ready-to and food-service offerings	◔
5	Reinvent your loyalty program and promotions	◔

Excel in execution and drive profitability

6	Implement AI-based commercial optimization	◔
7	Drive COGS reduction through negotiation and buying alliances	◑
8	Improve end-to-end productivity from supplier to customer	●
9	Design a zero-based operating model for HQ	◑
10	Automate HQ operations using (Gen)AI	◑

Fund and accelerate your transformation

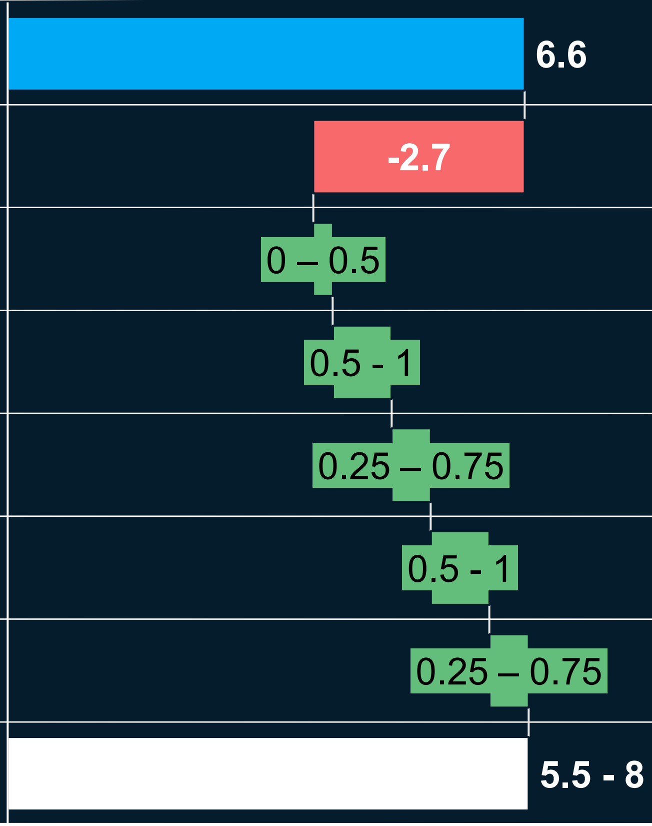
11	Modernize IT, incl. operating model	○
12	Invest in people and talent	○
13	Take sustainability to next level	○
14	Monetize Retail Media	◑
15	Develop your ecosystem	◑

While many grocers are beginning to make progress, none fully accelerated their efforts

Bolder actions are needed to avoid further profitability erosion and to get to sustainable profitability before 2030

Illustration of hyper/supermarket P&L of 2029 based on selected levers

EBITDA hyper/supermarket P&L from 2023 to 2029, as % of revenue



EBITDA 2023[1]	**6.6**	! Without **bold countering measures** the average hyper/supermarket's is set to fall below required EBITDA[2] to cover renewal CAPEX
Max. margin impact of trends	**-2.7**	
② **Step-up private label quality and develop private brands**	0 – 0.5	Assumes **15% volume increase in private label** share at 5 – 10% gross margin premium
③ **Improve store availability and reshape the store network**	0.5 - 1	Assumes store costs of 13 – 18% of rev., **10% store closure,** and **sales recouperation of 50%**
⑦ **Drive COGS reduction through negotiation and buying alliances**	0.25 – 0.75	Based on **0.3 – 1.0% COGS improvement**
⑧ **Improve end-to-end productivity from supplier to customer**	0.5 - 1	Based on **total labor cost reduction of ~5 – 10%** (store 5-10%, DC & warehouse 10-15%)
⑭ **Monetize Retail Media**	0.25 – 0.75	Based on **0.75-1.5% additional revenue at EBITDA margin of 40-70%**
EBITDA 2029	**5.5 - 8**	

Grocers need to do a step change across a set of levers best fitted to value proposition and success to win. Above calculation does not yet include (one off) initial investments. Higher EBITDA improvement requires larger investment

1. Ahold (NLD), Carrefour (FRA), Jerónimo Martins (PRT), Metro (DEU), Kesko (FIN), Sonae (PRT), Dino Polska (POL) | 2. Required renewal CAPEX is 1 – 2% EBITA margin, corresponding to ~4 – 5% EBITDA margin for hyper/supermarkets

Source: McKinsey Value Intelligence

① Wegmans and Albert Hein excel in offering high Fresh quality

Non-exhausive

Wegmans creates “wet market” vibe in its fresh department

Wegmans has focused on **creating the “wet market” vibe** through:

- Focusing on organic, sustainable and small-scale farming
- Highlighting proximity of products
- Generating overall premium feeling

Albert Heijn partners with Vezet to accelerate fresh innovation

Albert Heijn (leader in the Dutch grocery retail landscape) **and Vezet** (producer and distributor of fresh, ready-to-eat vegetables and salads) **do joint development of fresh products and apply “shared warehousing”** in which Vezet manages stocks of AH at DCs, fueled by extensive data sharing to **improve quality and ensure availability of fresh products**

Source: Press search, expert input

2 Stepping up quality of private label & develop private brands to grow to 15% of volume could add up to 0.5% in EBITDA margin

Context & assumptions

Context

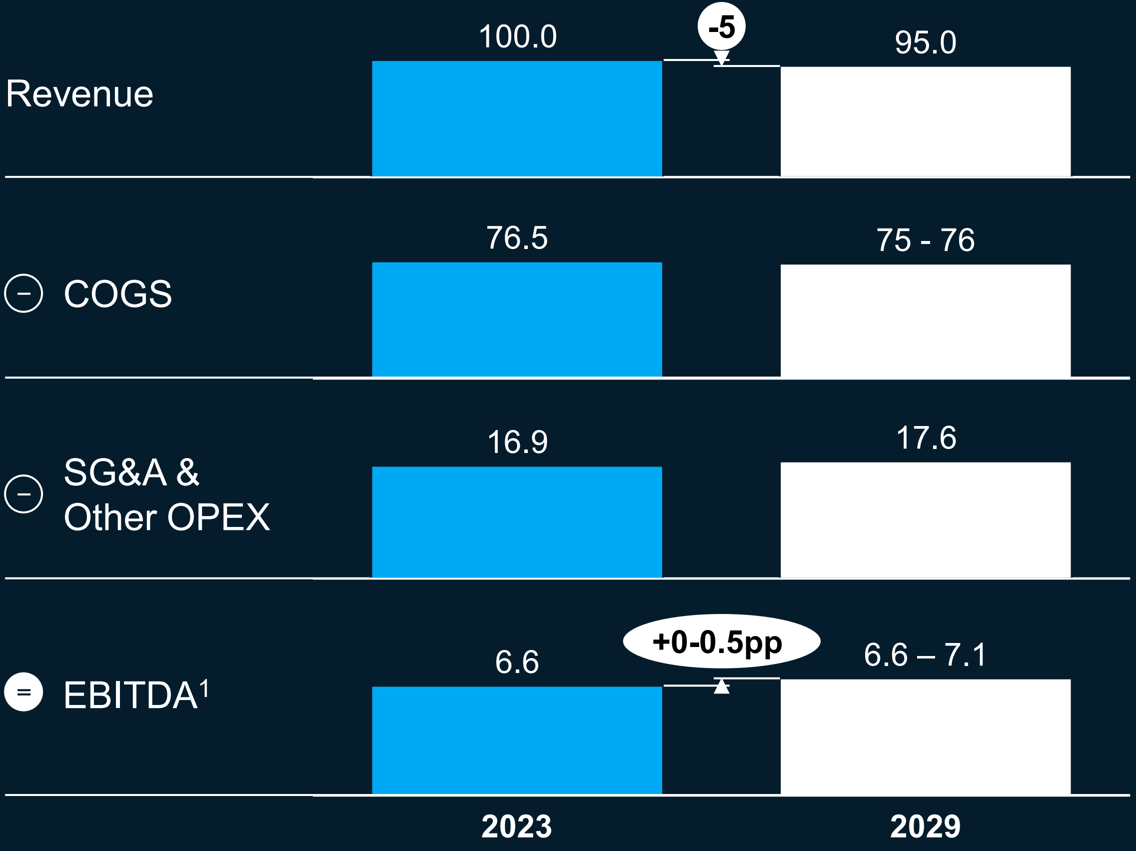
- Private label (PL) and private brands (PB) continue to benefit from consumers' quest for value with **share of sales expanding in every European market** since 2019 (+3.7pp for EU-11)
- **Private label is seen as a brand in itself** – no longer a copy of an A-brand alternative, with **78%** of consumers believing PL products **equal in quality to brands** while **88%** think PL offers **equal or better value for money**
- To win in PL and PB retailers should focus on improving **quality**, **differentiating products** beyond price and entry-level (e.g., brand building, product development), improve **cost efficiencies** (e.g., next-gen sourcing), and **drive scale**

Assumptions

- Increase volume share PL/PB**:** **15%** (accounted for substitution)
- Price discount PL/PB: **25%**
- COGS discount PL/PB: **30-35%**
- Implied GM premium PL/PB: **5-10%**

P&L impact of hyper/supermarkets, % of revenue

Revenue indexed (2023 Revenue = 100%)



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1. 2029 COGS, SG&A & Other Opex, and EBITDA presented as share of 2029 revenue (=100%)

Source: State of Grocery 2024, McKinsey 2024 European Consumer Survey, McKinsey analysis, expert input,

2 Mercadona and Albert Heijn are leading players in Europe in building their private label/brands

Non-exhausive

Albert Heijn differentiated its PL offering with multiple targeted variations

Albert has focused on expanding its private label (PL) and private brands (PB) offering as **49.4% of total food sales in Europe are own brand**[1]

To differentiate its offering beyond price, Albert Heijn introduced various innovative products, PL variations and private brands such as **AH Excellent** (premium), **AH Glutenfree**, **AH Terra** (vegan line with 200+ products), **AH brand ready-to-eat/cook**, **Streeckgenoten** (PB offering local deli meat / near fresh products), **Perla** (PB offering coffee products), **Delicate** (PB offering chocolate

Mercadonas four private brands account for 75% of all sales

MERCADONA

Private brand sales for Mercadona (largest discounter grocer in Spain at 27% market share) **accounted for ~75% of all sales** in 2023

Mercadona achieves most of its sales from its **four, category specific private brands: Hacendado** (food products), **Bosque Verde** (household/cleaning products), **Deliplus** (personal care and cosmetics) and **Compy** (pet care)

Mercadona's 4 private brand logos

HACENDADO

Compy

Deliplus

BOSQUE VERDE

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[1] Presented number is for Ahold Delhaize group of which Albert Heijn is largest player

Source: Company financial statements, press search, Statista

③ Reshaping store networks to close 10% of stores and recouping 50% of sales could add up to 0.5 – 1% EBITDA margin

Context & assumptions

Context

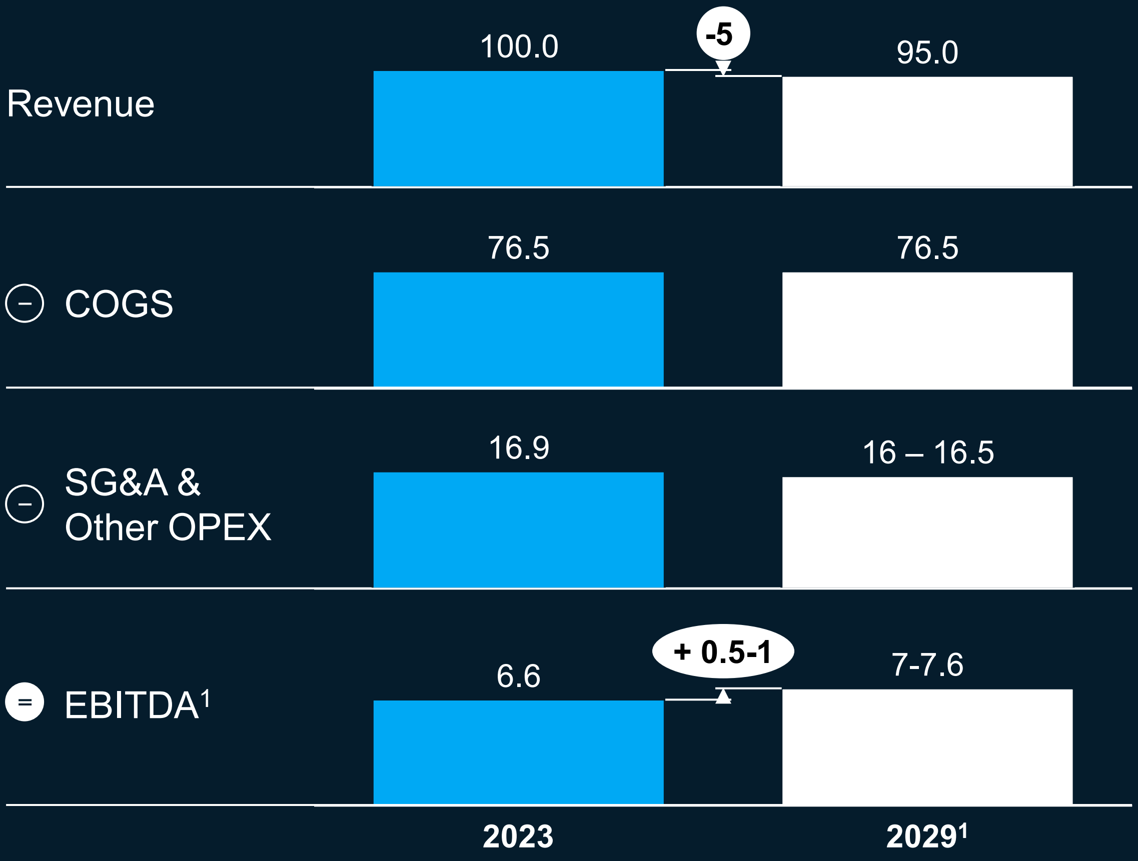
- **Reshaping store networks is a lever for grocery retailers to improve profitability** and consumer experience, with retailers increasingly shifting focus from network expansion to **strategic footprint optimization** balancing efficiency and market presence, **specifically for hypermarkets**
- **Successful store network strategies prioritize right-sizing the portfolio** to reduce overall store costs while potentially **recouping sales** in nearby locations (feasibility depends on store format and country)

Assumptions

- **Share of store closures:** 10%
- **Recouperation of lost revenue:** 50%
- **Store costs as share of revenue:** 13 – 18%

PP&L impact of hyper/supermarkets, % of revenue

Revenue indexed (2023 Revenue = 100%)



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[1] 2029 COGS, SG&A & Other Opex, and EBITDA presented as share of 2029 revenue (=100%)

Source: State of Grocery 2024, McKinsey 2024 European Consumer Survey, McKinsey analysis, expert input

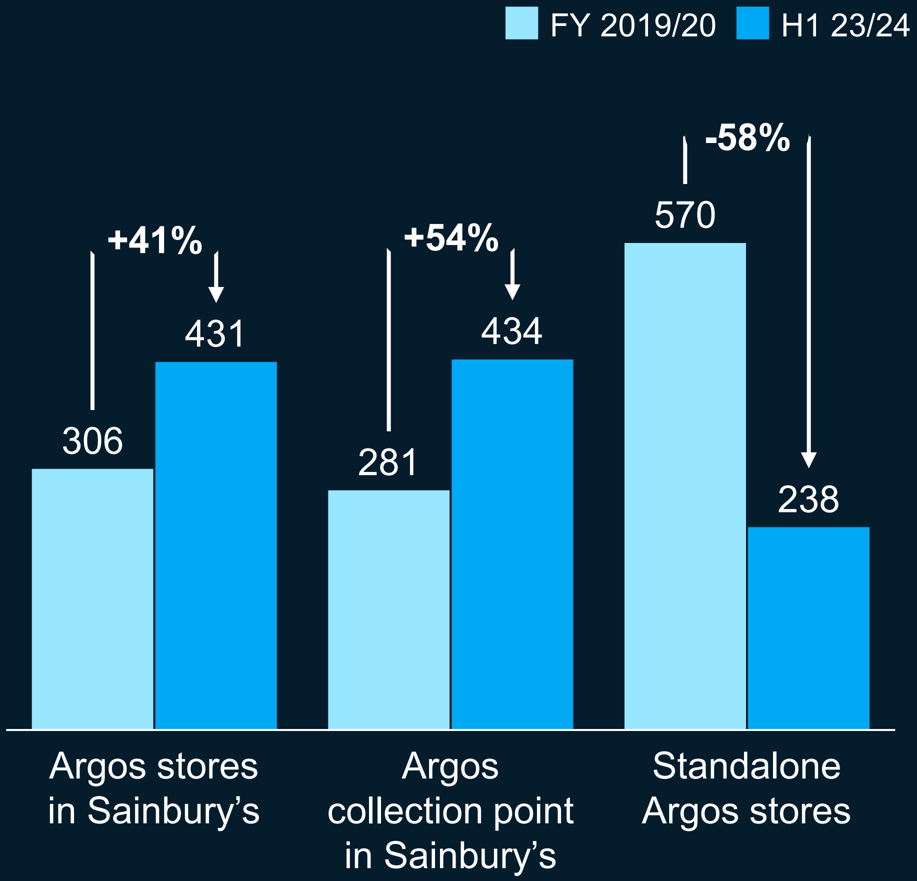
③ Sainbury's drastically reshaped store network and reduced fixed costs with ~3%pp of revenue in 5 years

Context

Sainbury's, the second largest supermarket in the UK, acquired Argos in 2016, a general merchandise retailer

Sainbury's started ~5 years ago to close standalone Argos stores and to incorporate the Argos brand in their supermarket. They are set to close more standalone Argos stores in the future

Rebalanced store network



>3%pp

reduced fixed costs as % of revenue by reducing the standalone store estate and opening more Argos stores inside Sainbury's

Source: Press search, Next Level Sainbury's strategy update February 2024

5 Several retailers launched different types of personalization efforts – with up to 6% revenue increase

Context

European retailers are increasing customer lifetime value across all customers by scaling personalized coupons in a new approach through:

- **Optimizing for long term value** (lifetime) of customer instead of next weeks sales
- **Changing way of working with suppliers** (budgets instead of campaigns)
- **Personalizing everything** (product selection, discount timing, message, discount, channel)
- **Integrating marketing, category management and analytics** teams

Use cases for personalized promotions focus on:

- **Increasing frequency** of client's visits
- **Increasing average basket ticket** with complimentary goods or targeted sales
- **Retaining clients** with decreasing visits frequency

+5 - 6%

In sales versus control group

Source: Press search

7

Driving COGS reduction by 0.3 – 1% through supplier negotiation and buying-alliance activity could add 0.25 – 0.75% EBITDA uplift

Context & assumptions

Context

- Numerous European grocery procurement retailers have **reshaped their assortments and set up** to enhance scale and consolidate purchasing power, securing more advantageous terms after renegotiating with suppliers
- **Optimizing purchasing departments involves varying levels of complexity**, with savings typically increasing as complexity deepens *(deep-dive next)*
- To bring buying activities to the next level top-performers are engaging in **international buying alliances for both assortment and additional services** with full price transparency and knowledge sharing across members

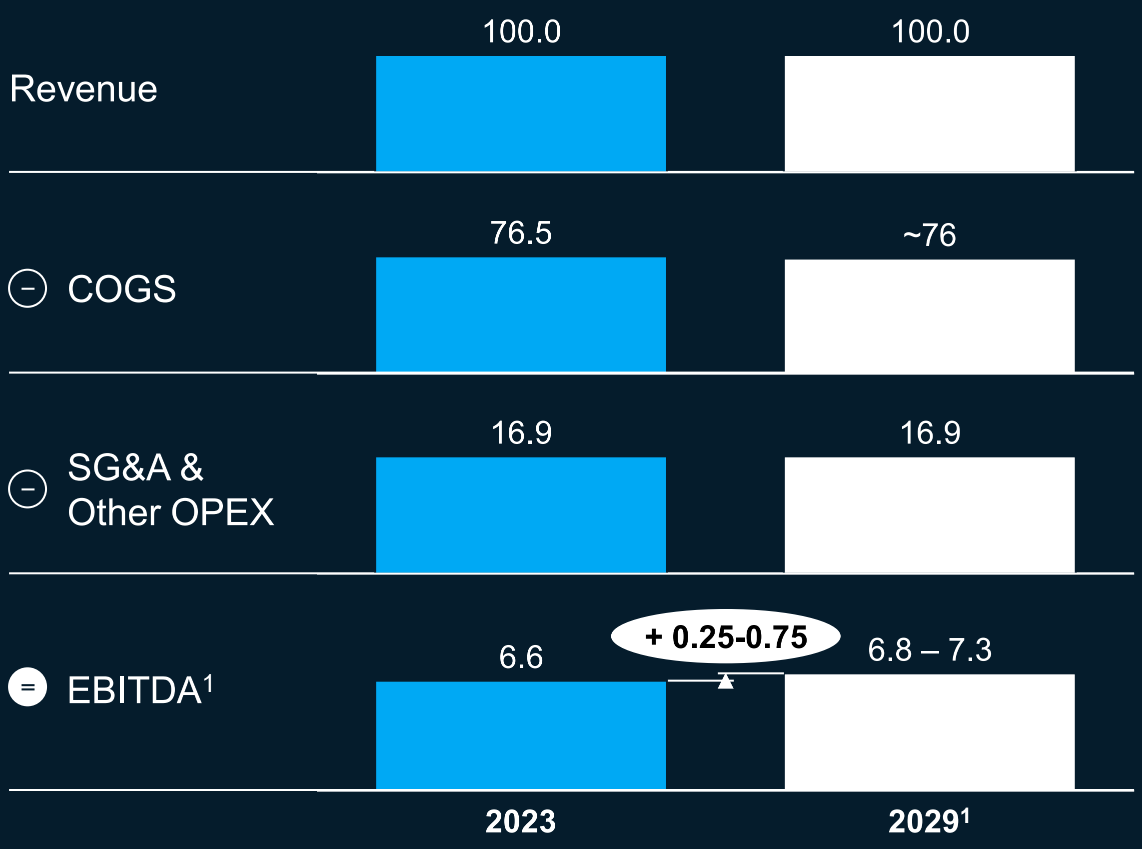
Assumptions

No Change in revenue (savings not priced through)

Decrease in COGS: **0.3 – 1.0%**

PP&L impact of hyper/supermarkets, % of revenue

Revenue indexed (2023 Revenue = 100%)



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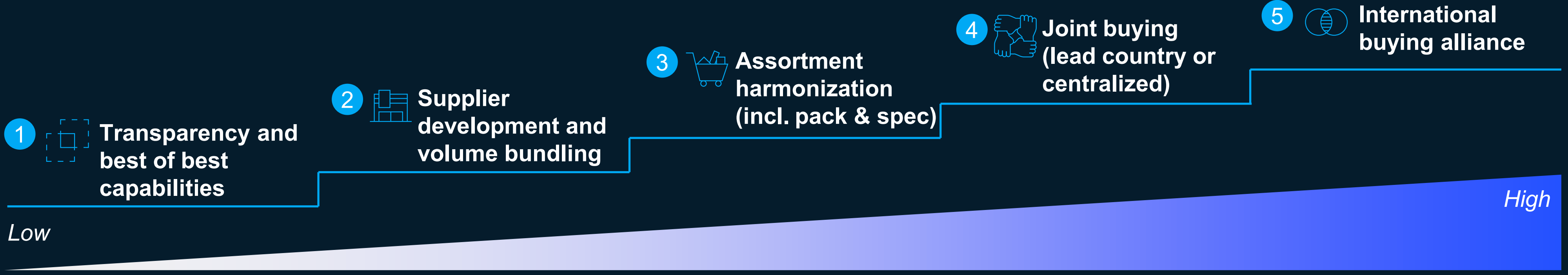
1. 2029 COGS, SG&A & Other Opex, and EBITDA presented as share of 2029 revenue (=100%)

Source: State of Grocery 2024, McKinsey 2024 European Consumer Survey, McKinsey analysis, expert input,

⑦ There are various ways with different levels of complexity for a grocery retailer to drive COGS reduction



Level of complexity	① **Transparency and best of best capabilities**	② **Supplier development and volume bundling**	③ **Assortment harmonization (incl. pack & spec)**	④ **Joint buying (lead country or centralized)**	⑤ **International buying alliance**
Potential value drivers	• Based on joint set of product master data, create transparency on price / full trade terms, clean-sheet for identical and comparable SKUs • AI supported tooling incl. automated-supplier scripts and clean sheet models • At-scale capability building	• Coordinated negotiations with overlapping suppliers for A-brands • Consolidation of ingredient and pack material buying • Harmonization (while balancing dependency and scale) of fresh and own brand suppliers	• Spec and pack harmonization in own brand and fresh • Assortment harmonization between brands • Common database for full SKU details to identify "hidden" overlap	• Full transparency on all price levers • Scale of buying • 3Net/4 Net harmonization at SKU level • Logistics bundling / cost optimization • Value chain re engineering for Fresh assortment	• Leverage scale of joint negotiation of multiple retailers and markets • Full price transparency across members • 3Net harmonization across member retailers • Knowledge sharing on suppliers • Enhanced market intelligence
Inspiration	Walmart LIDL	Walmart		Carrefour REWE	EDEKA

Note : Local brand differences regarding **sustainability** and **franchising** need to be taken into consideration

7 Grocers could join more international buying groups & alliances to further drive COGS reduction

Buying type	Organizations	Members
Integrated Pan-European negotiations *Individual retailer-based negotiations on European level*	LIDL	n/a
	ALDI ALDI	n/a
	Eureca	Carrefour Country organisations
Coordinated negotiations *Alliance-based negotiations of contract terms*	EURELEC TRADING	REWE E.Leclerc Ahold Delhaize
	EVEREST	EDEKA PICNIC Système U JUMBO (further members likely to be chosen from EPIC)
	AGECORE	colruyt CONAD EROSKI coop
	EMD	Globus axfood Casino NorgesGruppen euromadi AMK Woolworths MARKANT SYNTRADE Dagrofa colruyt Kaufland MARKANT SUPER GROS Superunie ЛЕНТА TUKO LOGISTICS ESDitalia euromadi PORT
	Auchan RETAIL FRANCE les Mousquetaires Intermarché	Auchan Intermarché
	ams creating synergy	Ahold Delhaize Musgrave salling group ICA KESKO MIGROS hagar BOOKER Morrisons
On-top international terms *Alliance-based negotiations of additional services*	COOPERNIC	REWE coop Ahold Delhaize E.Leclerc
	EPIC	EDEKA PICNIC Système U JUMBO MIGROS ESSELUNGA Jerónimo Martins

Disclaimer: Consumer pricing at the sole discretion of the retailer

Source: IGD; European Commission, 2020 (Retail alliances in the agricultural and food supply chain), Press search

8 Improve end-to-end productivity through advanced technologies to reduce labor cost with 5 – 10% could give EBITDA uplift of 0.5 – 1%

Context & assumptions

Context

- **Retailers will need to invest in improving end-to-end productivity** to manage rising wages and reduce labor costs (e.g., through automation). **Level of possible efficiency improvement depends on the size, scope and starting point of the investment** and varies across business operations
- **Examples**: digital price tags, advanced inventory forecasting systems, warehouse automation systems

Assumptions

- **Labor cost distribution**: HQ (**10%**), in-store (**70%**), DC/warehouse (**20%**)
- **Labor cost reduction**: in-store (**5 – 10%**), DC/warehouse (**10 – 15%**)

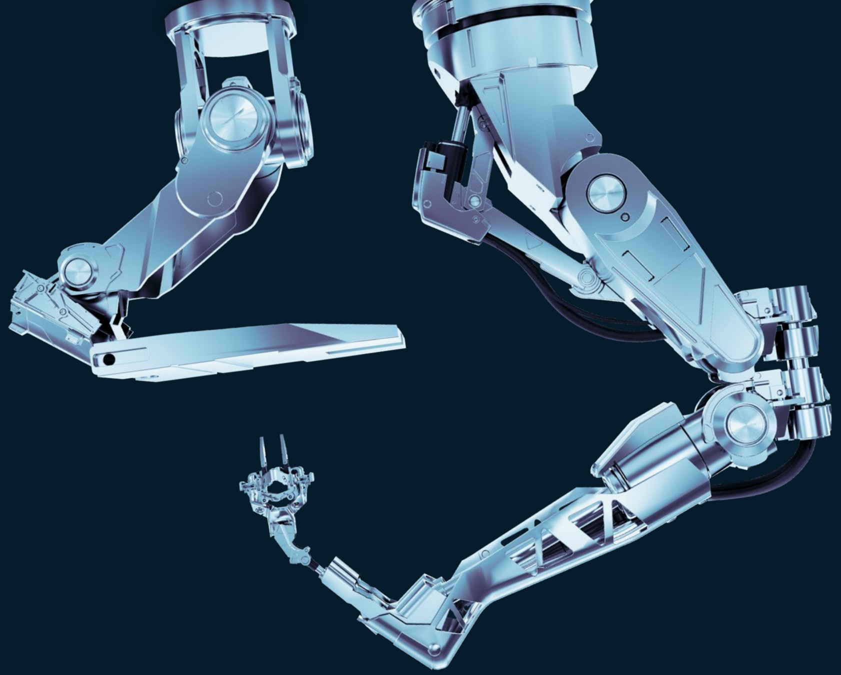
! **Labor need reduction could increase with the scale / boldness of automation** (e.g., up to **40%** in warehouse)

PP&L impact of hyper/supermarkets, % of revenue

Revenue indexed (2023 Revenue = 100%)

This calculation does not take into account the (one off) initial investment, dependent on boldness of investment this can be a large CAPEX investment (g., fully automated warehouse could require up to 5x investment of normal warehouse)

Source: McKinsey analysis, expert input



Utilization of advanced technologies will drastically improve end-to-end productivity

50% of paid workforce activities can be automated with current technology

60% of all occupations can be meaningfully automated (>30% of job activities)

45% of global workers will need some form of reskilling by 2030 to change jobs or upgrade skills significantly

Source: McKinsey

8 Advanced technologies can drastically change the store and warehouse of the future, and improve productivity

Non-exhausive

Grocery store of the future has potential to operate with up to 60% fewer labor hours vs traditional retailer[1]

1. **Back of house**: e.g., automated demand planning, automatic unloader
2. **Centre store**: e.g., Shelf scanning robots
3. **Front-end**: e.g., mobile check-out, just-walk-out-technologies
4. **Management**: e.g., automated ordering, AI service desk
5. **Produce**: e.g., robotic food prep (Breadbot), automated dispensers

The DC of the future has the potential to reduce labor need up to 40%

1. Real-time updates with automated ordering system
2. High-bay system: automated storage and retrieval
3. Drones for quality checks
4. Autonomous vehicles for (un)loading
5. Automated order picking and smart trolleys for best in-store shelving routes

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[1] Might vary depending on starting point of productivity/automation

Source: McKinsey

8 Ocado and Albert Heijn are examples that are using advanced technologies to automate their fulfillment and DCs

Non-exhaustive

Ocado has made significant strides in automating its fulfillment processes

Ocado Retail (an online grocery pioneer with 3B USD of revenue) operations are supported by **Ocado Technology Solutions and logistics services by Ocado Logistics**. Made significant advancements in Customer Fulfillment Centers (CFCs), leveraging advanced technology to optimize their hub/spoke network and ensure accurate stock availability **resulting in rapid delivery scheduling and fulfillment**

Albert Heijn's warehouse robots could result in ~1% EBIT improvement

Albert Heijn opened its new mega distribution center (DC) serving 300 stores using robots to store, retrieve, de-palletize and transport products

Automation offering potential **~1% EBIT improvement[1]**, at **investment of 100 – 300M per center** depending on the level of automation

Vanderlande packing robots

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1. Under assumption that warehouse labor costs equal 2-4% of sales and can be reduced by 20-60%

Source: Company website, IGD Retail, press search

14 Monetizing Retail Media towards 0.75 – 1.5% additional revenue could give an EBITDA uplift of 0.25 – 0.75%

Context & assumptions

Context

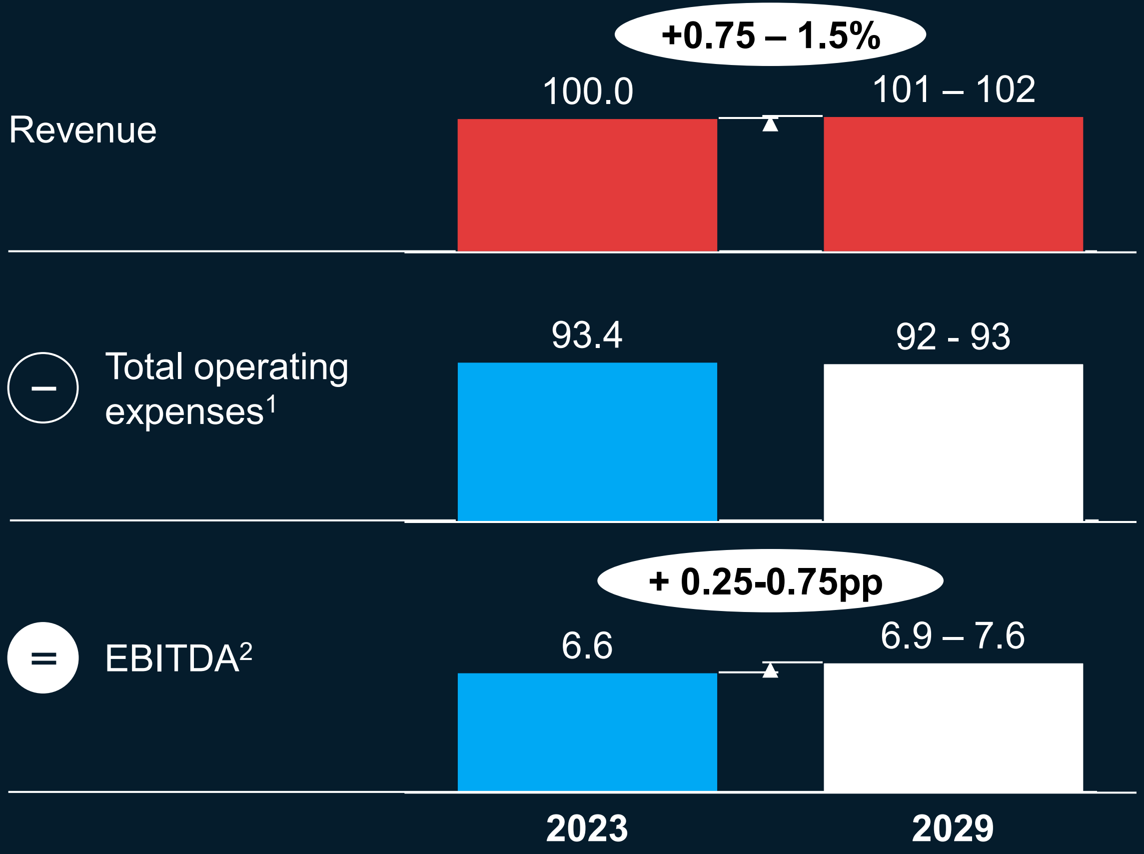
- **Grocery retail has traditionally been a low margin industry** with margin pressure ramping up further in 2023 due to inflation and labor market tightness
- **Monetizing Retail Media (RM) has emerged as driver of profitability with margins reaching up to 70%** within 3 years of launching
- **Impact dependent on (online) scale** (only largest players expected to remain relevant for CPG advertisers), **ability to measure impact for advertisers** (e.g., return on ad spending), and **share of private label** (large share offers lower incentive for CPGs)

Assumptions

- RM additional revenue: **0.75 – 1.5%**
- RM EBITDA margin: **40 – 70%**

PP&L impact of hyper/supermarkets, % of revenue

Revenue indexed (2023 Revenue = 100%)



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1. Includes COGS, SG&A and other Opex | 2. 2029 EBITDA margin and operating expenses presented as share of 2029 revenue (=100%)

Source: McKinsey analysis, expert input

McKinsey & Company

14 Kroger began its retail media business in 2012 – building scale since 2021

Getting Started - 2015

- Getting sponsorship from C-Level
- Strategy 1: building 1P data through 84.51 [they acquired Dunn Humby's US business]
- Strategy 2: building retail media network for activation

Testing Program - 2017

Built new entity Kroger Precision Marketing

Drove testing program in US with multiple CPGs on promoted search and on-site monetization

Leveraged agency to drive the execution & Build out direct selling team

Develop technology infrastructure (PromoteIQ)

Building Scale - 2018-2020

- Expansion Beyond Performance Marketing
- Building Capabilities Beyond O&O
- Agency Trade Desk

10-15%

Uplift on post impression conversion behavior for key CPG advertisers

- Experimentation with Extended Branding Opportunities
- Attribution Solution – launched Stratum

50%+ EBIT

Impact is measured by in-store purchase by exposed audience versus a control group

Building Ecosystem - 2021-today

- Developing End-to-End Brand Journeys
- Private Syndication Marketplaces
- Penetrating the Long Tail
- Building Operational Scalability
- New Product Roadmap

$11B

Digital sales; growing at 52%

$1.2M

84.51 media sales; growing at 35%

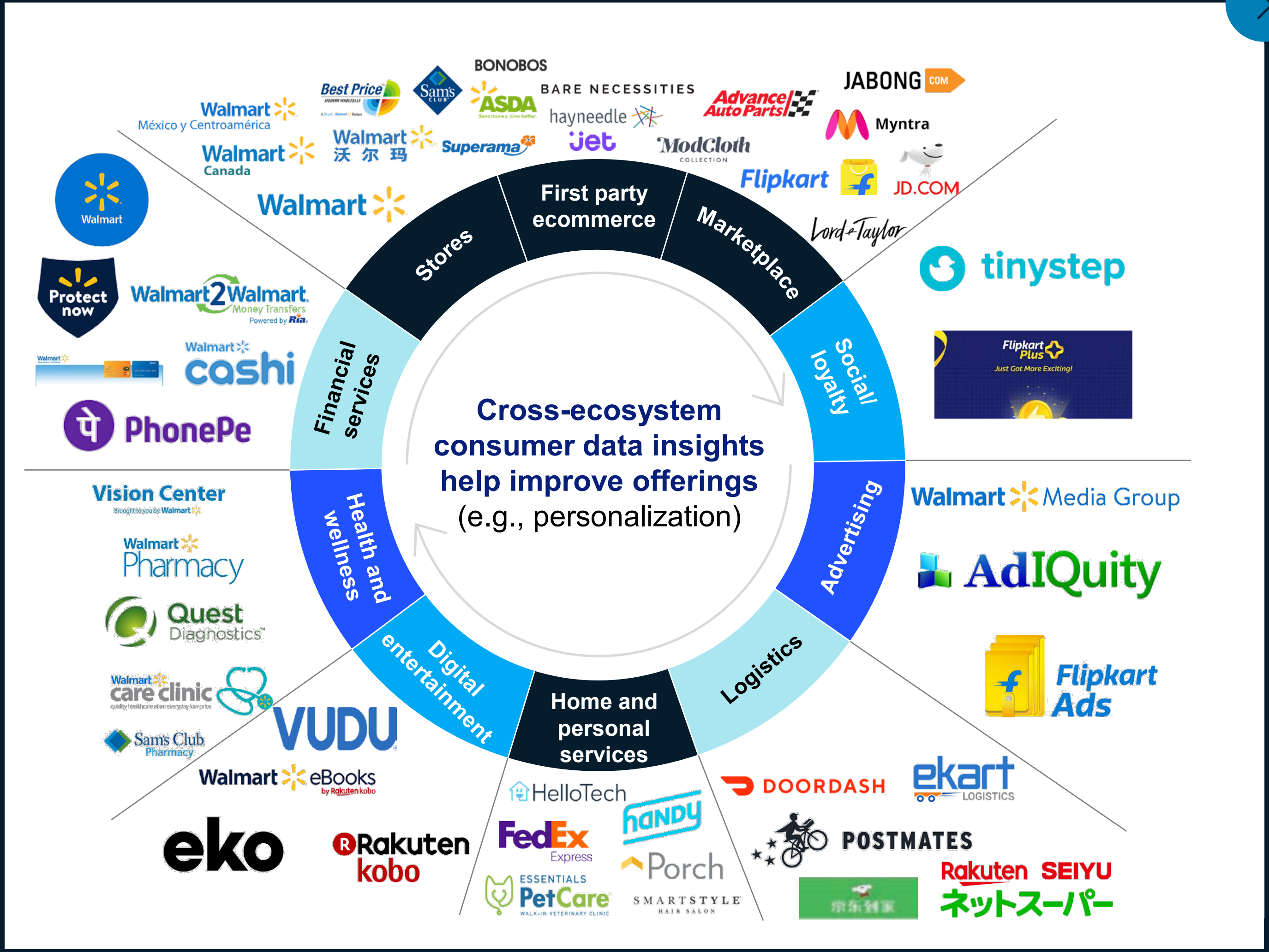
75%

EBIT for media sales

Source: Company website, annual reports, earning calls transcripts, press clippings, KantarRetail IQ

15 Walmart developed its ecosystem by expanding from retail to other sectors (e.g., health) with members spending 2x vs non-members

Walmart Ecosystem



Stores

First party ecommerce

Marketplace

Social/ loyalty

Advertising

Logistics

Home and personal services

Digital entertainment

Health and wellness

Financial services

Cross-ecosystem consumer data insights help improve offerings (e.g., personalization)

Approach & impact

Walmart built an E2E coverage of the retail customer journey, positioning Walmart as a one-stop destination, **leveraging opportunities to cross-sell** across segments (e.g., cross-sell relevant retail products aligned with healthcare needs), and improve offering using consumer data insights

2X	+11M
Member spending vs. non-member (2022)	Members (2022)

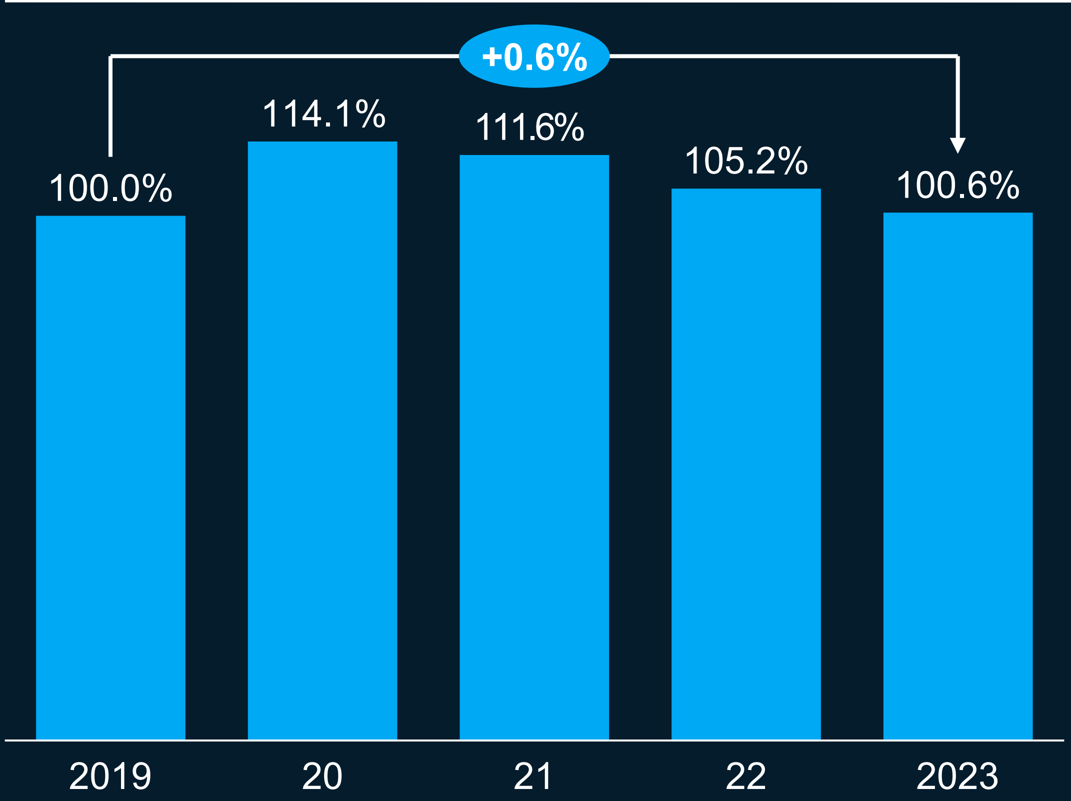
Source: Walmart online presence, expert interviews, press search

Appendix

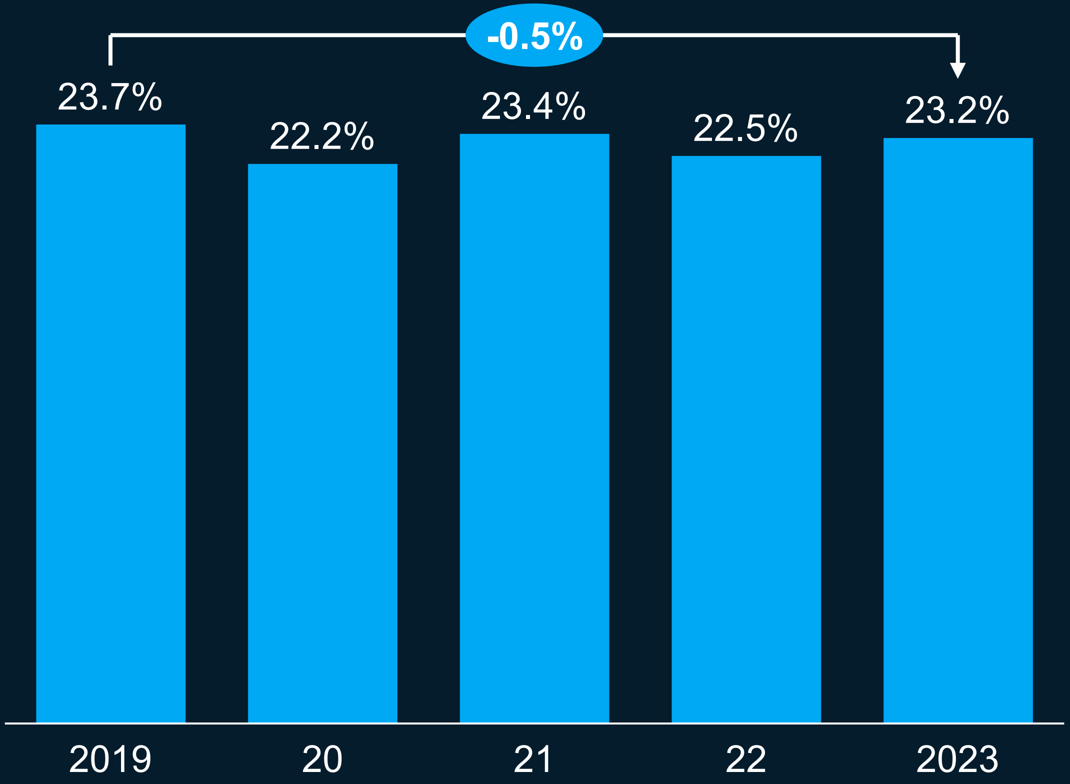
Basket size spiked during COVID, however returned to 2019 levels by 2023, while the promo share declined by 0.5pp

EU11

Basket size, indexed to 2019, %



Promo share, %



Source: State of Grocery 2024

High inflation negatively impacted purchasing power and real household consumption over the last years

Change in real wage, real consumption, savings rate, Eurozone, %

Change of real wages
Percentage change, q-o-q,

Change of real household consumption
Percentage change, q-o-q

Savings rate
Percentage points, quarterly

Real wages (purchasing power) have been declining given high inflation of the last years

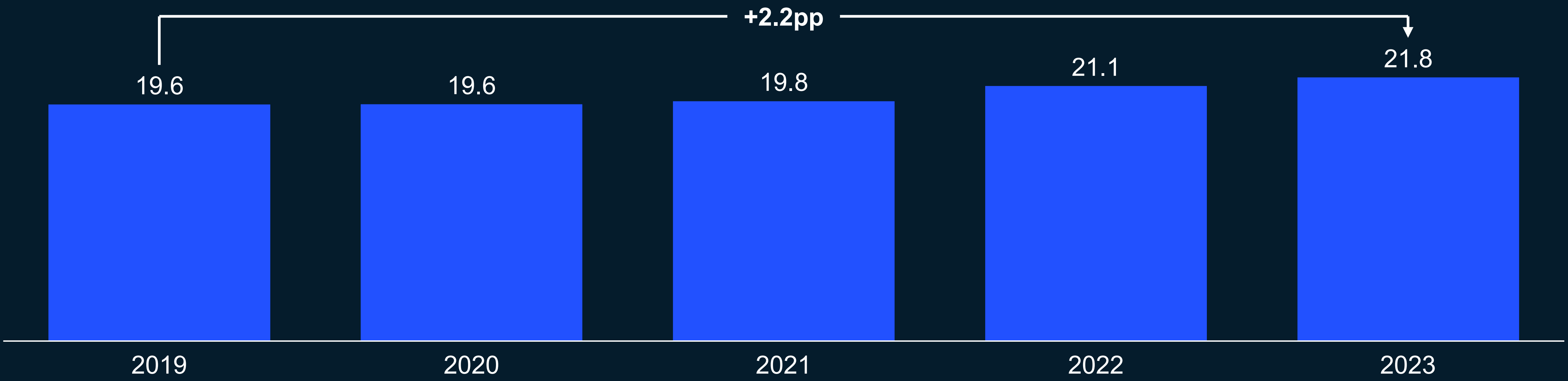
Real household consumption declined drastically after first year of COVID-19, and remains relatively stagnant over the past year

Consumers have become more conscious (savings rate 15% in 2023 vs 13% in 2019), negatively impacting real household consumption

Source: Eurostat

Growing share of discounters (+2.2pp from 2019 to 2023)

Discounter channel share of total grocery EU-11[1], %



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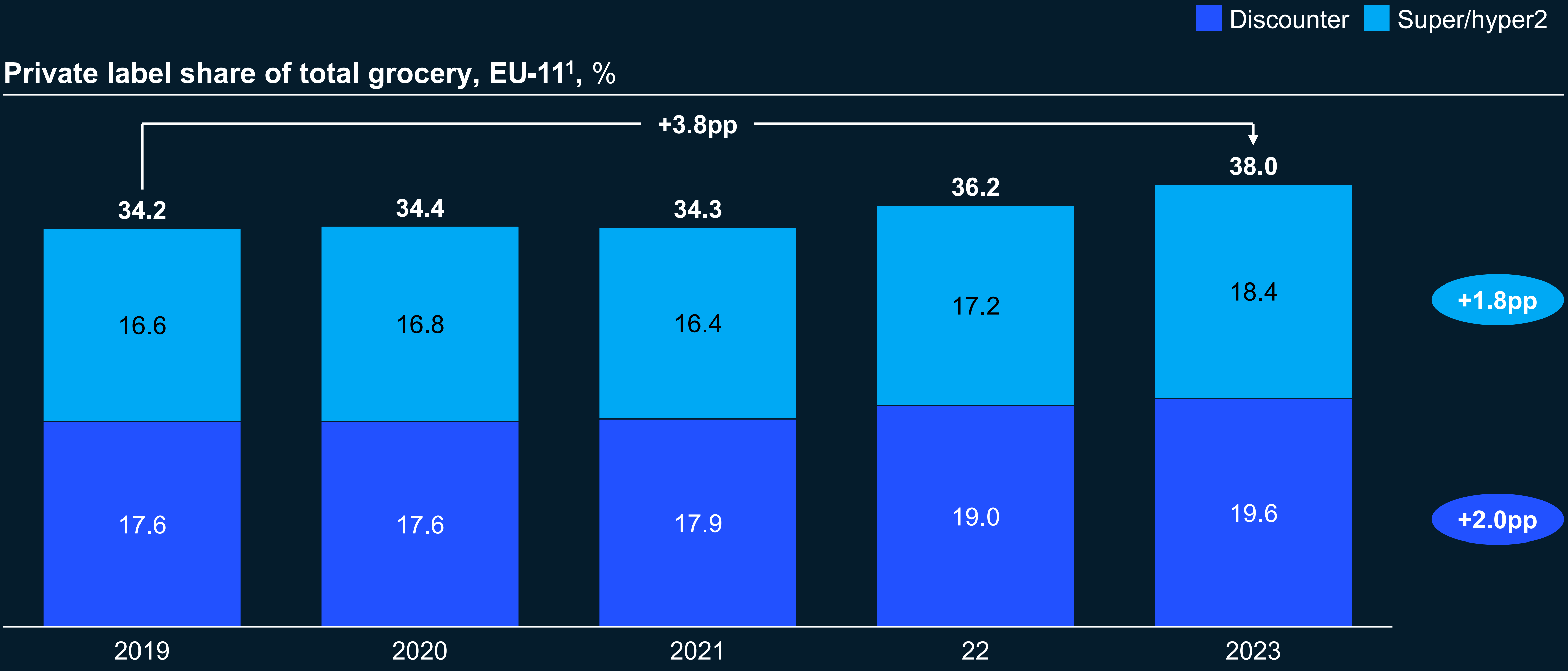
1. UK, DE, FR, IT, ES, NL, CZ, PL, PT, SE, BE

Source: State of Grocery 2024

Growing share of private label (+3.8pp from 2019 to 2023)

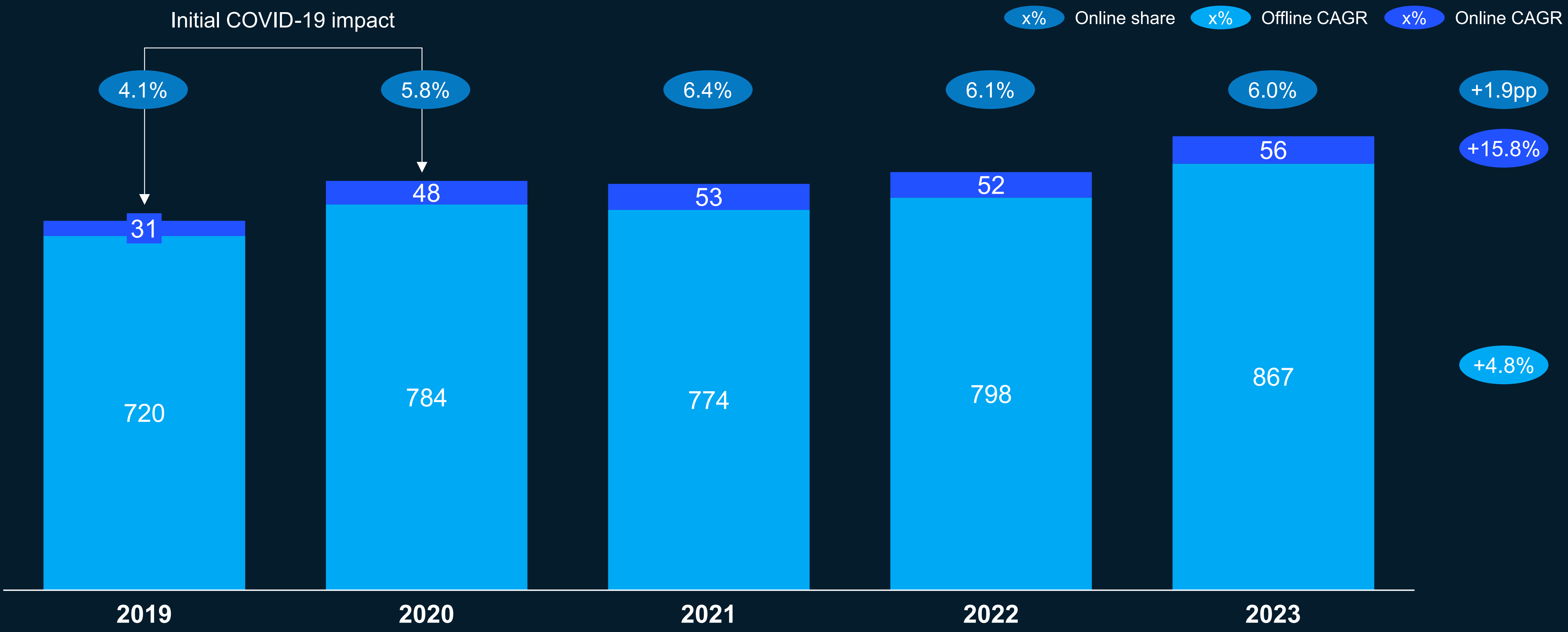


1. UK, DE, FR, IT, ES, NL, CZ, PL, PT, SE, BE | 2. Assuming discounters sell 90% private label

Source: State of Grocery 2024

Online share increased (+1.9pp), resulting in lower margin for hyper/supermarkets, specifically hypermarkets

Offline vs online grocery, EU-11[1], EUR B



1. UK, DE, FR, IT, ES, NL, CZ, PL, PT, SE, BE

Source: State of Grocery 2024, IGD

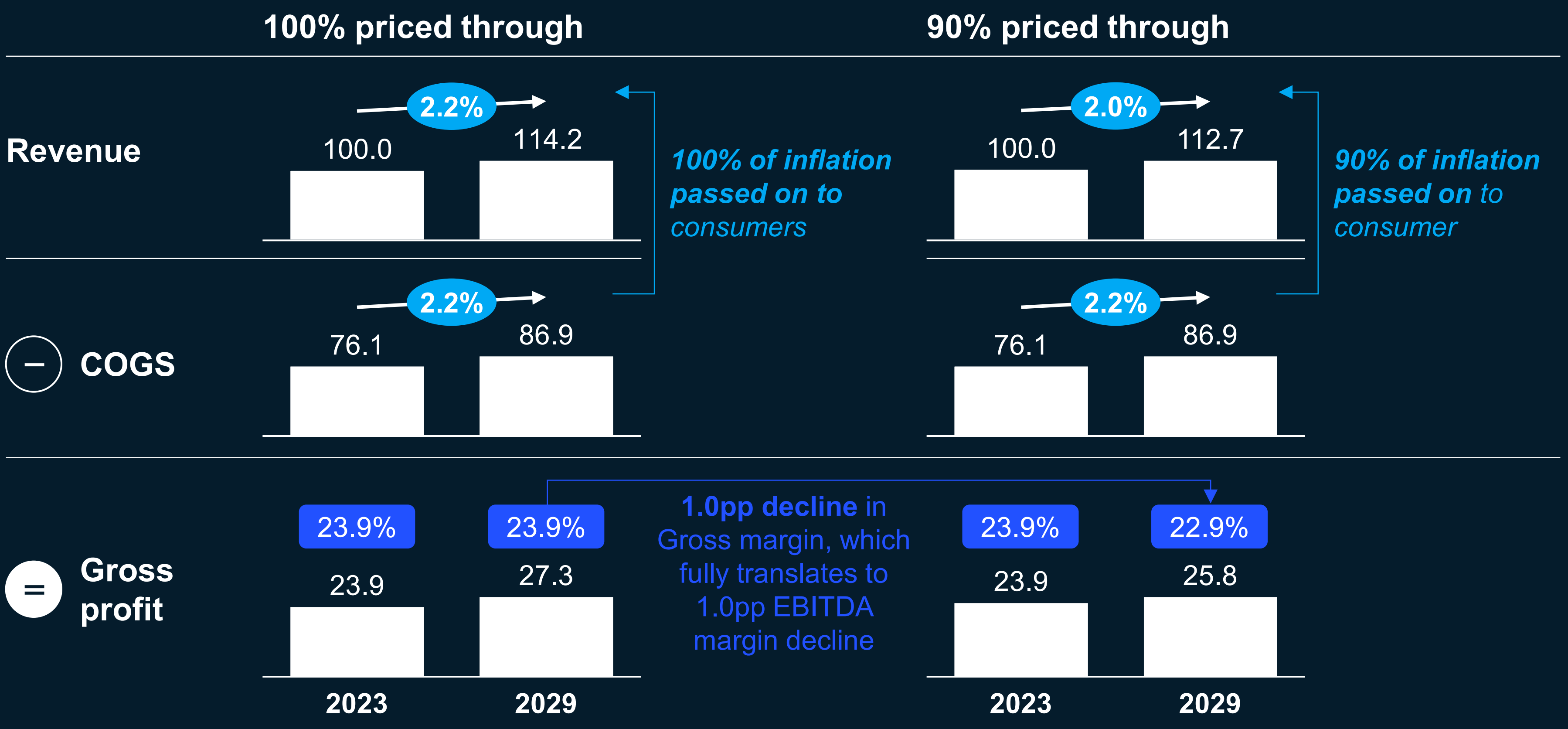
1. If 90-100% of food COGS inflation can be passed on to consumers without affecting volumes, the EBITDA impact is -1.0pp to 0pp

P&L development, %

xx% CAGR, %

xx% Gross margin, %

Indexed (2023 Revenue = 100%)



100% of inflation passed on to *consumers*

90% of inflation passed on *to consumer*

1.0pp decline in Gross margin, which fully translates to 1.0pp EBITDA margin decline

Key assumptions

- **90-100%** of food COGS inflation can be passed on to the consumers without affecting volumes[2]
- 2024-2029 the inflation of COGS will be **2.2%** p.a.[1]
- Revenue growth is entirely due to price inflation, with volumes remaining constant, which means SG&A costs also assumed to remain stable

---

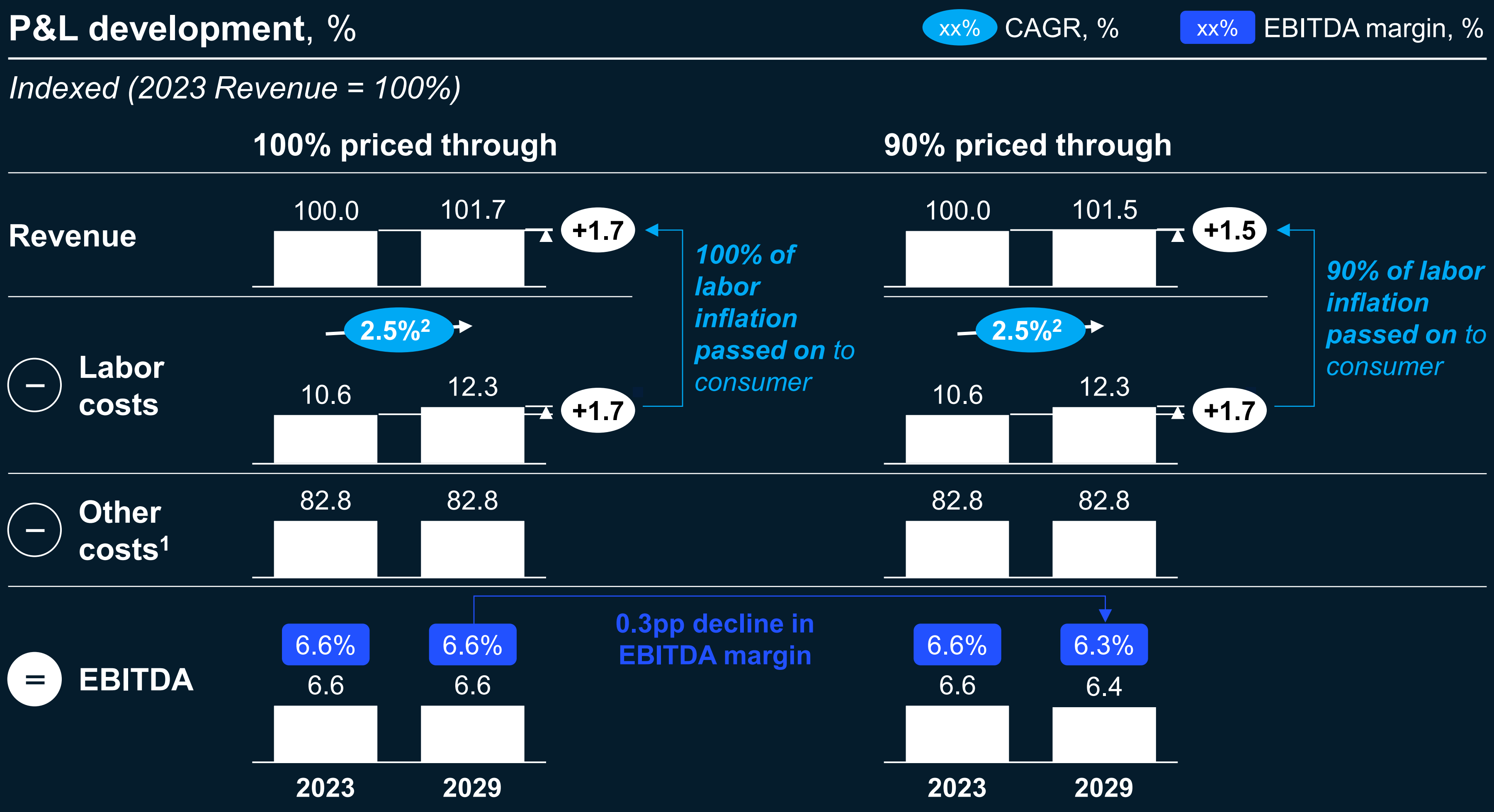
1. In line with ECB food inflation forecast
2. Over the period of high food inflation in 2019-2023, retailers have been able to price through 95% of the ~5% p.a. food inflation onto consumers, while the sale volumes remained stable

Source: State of Grocery 2024, ECB, McKinsey Value Intelligence, McKinsey analysis

2. If 90-100% of labor cost increase due to labor market tightness can be passed on to consumers, the EBITDA impact is -0.3pp to 0pp

P&L development, %

Indexed (2023 Revenue = 100%)



Key assumptions

- **90-100%** of labor cost increase can be passed on to consumers
- Wage inflation peaked at +4-6% in 2023-24 and is expected to stabilize, however at elevated levels (**+2.5% p.a. up to 2029**[2] vs. +1.5% historically) due to a tight labor market and ongoing inflation compensation

1. Including COGS, Logistics, Warehousing and other non-labor costs
2. In line with ECB labor unit cost inflation forecast: growth of 4.5% in 2024, 2.6% in 2025, 2.1% in 2026, then stabilized at 2% p.a., resulting in 2.5% p.a. until 2029 on average

Source: State of Grocery 2024, ECB, McKinsey Value Intelligence, McKinsey Analysis

3. GLP-1 drug users spend 6-11% less on groceries resulting in EBITDA margin decline of 0.1 to 0.2pp

P&L development, %

xx% CAGR, %

xx% EBITDA margin, %

Indexed (2023 Revenue = 100%)

0.2-1.0%[1] drop in volumes depending on the GLP-1 drug adoption rates, translating to 0.2-1.0% decrease in revenues and COGS

SG&A and other costs assumed to stay stable

Key assumptions

- Households with at least one GLP-1 drug user reduce grocery spending by **6-11%**
- **30-40%** GLP-1 drug adoption by 2029 among the people with diabetes (8-10% of the European population)
- **10-25%** GLP-1 drug adoption by 2029 among the people with obesity (16-20% of the European population)

---

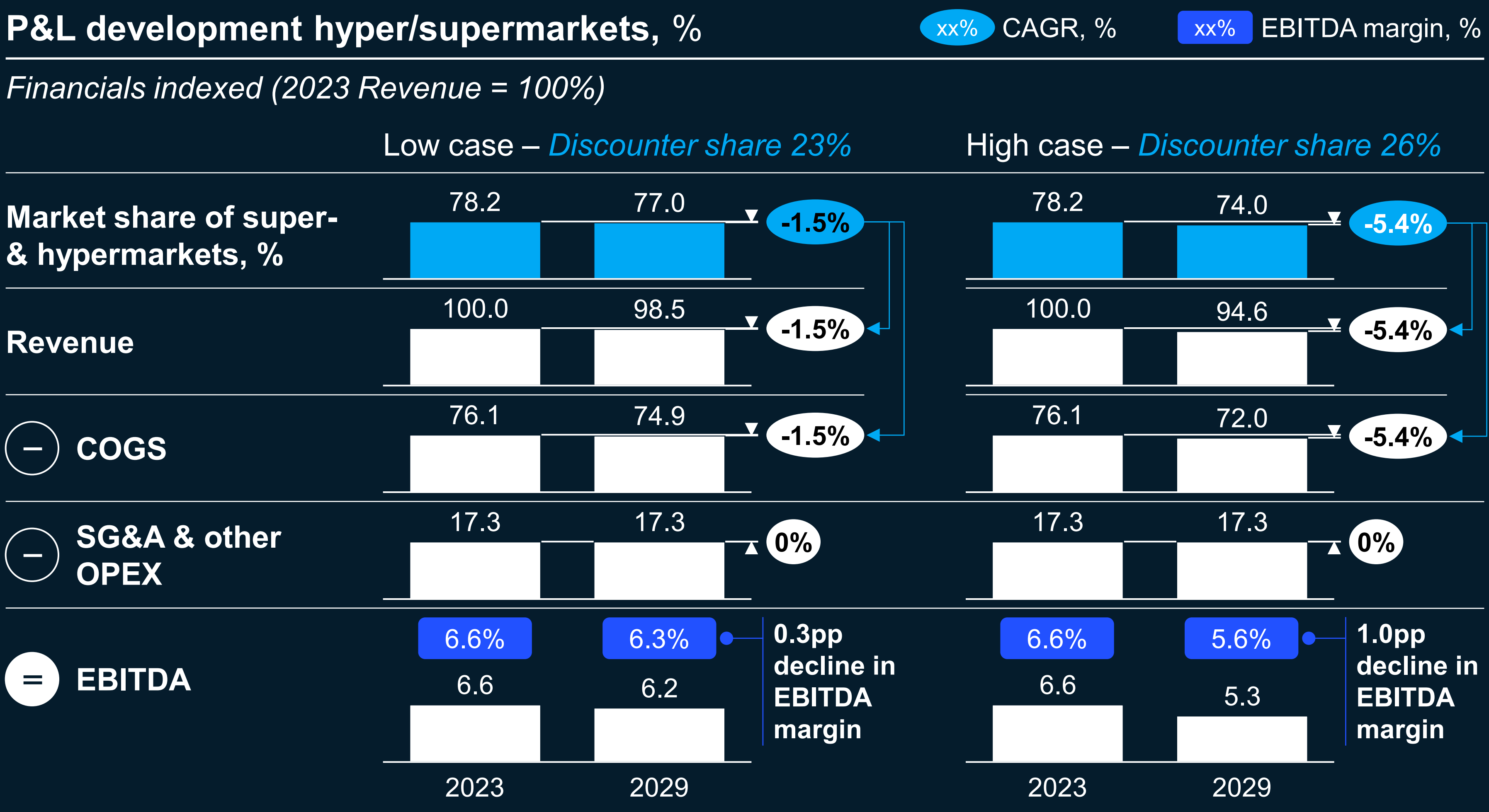
1. 0.2% drop in volumes, assuming -6% in grocery spending for 4% of population (Diabetes - 30% adoption among 8% of population, obesity - 10% adoption among 16% of population)
1.0% drop in volumes, assuming -11% in grocery spending for 9% of population (Diabetes - 40% adoption among 10% of population, obesity - 25% adoption among 20% of population)

Source: State of Grocery 2024, ECB, McKinsey Value Intelligence, McKinsey Analysis, Cornell SC Johnson College of Business Re search Paper, Goldman Sachs Research, J.P. Morgan Research

4. Market share erosion to discounters will negatively impact the EBITDA margin by -1pp to -0.3pp

P&L development hyper/supermarkets, %

Financials indexed (2023 Revenue = 100%)



Key assumptions

- COGS are assumed to develop in line with revenue
- SG&A & other OPEX are expected to stay stable due to relatively high share of fixed costs

Takeaways

- For each 1pp market share loss to discounters, the EBITDA margin of super- & hypermarkets declines by ~0.23pp
- Loss of the market share to discounters is likely to disproportionately impact specific players within certain markets, while having a small effect on others

Source: State of Grocery 2024, ECB, McKinsey Value Intelligence, McKinsey Analysis

5. The increasing share or private label positively impacts EBITDA margin by 0.0pp to +0.2pp

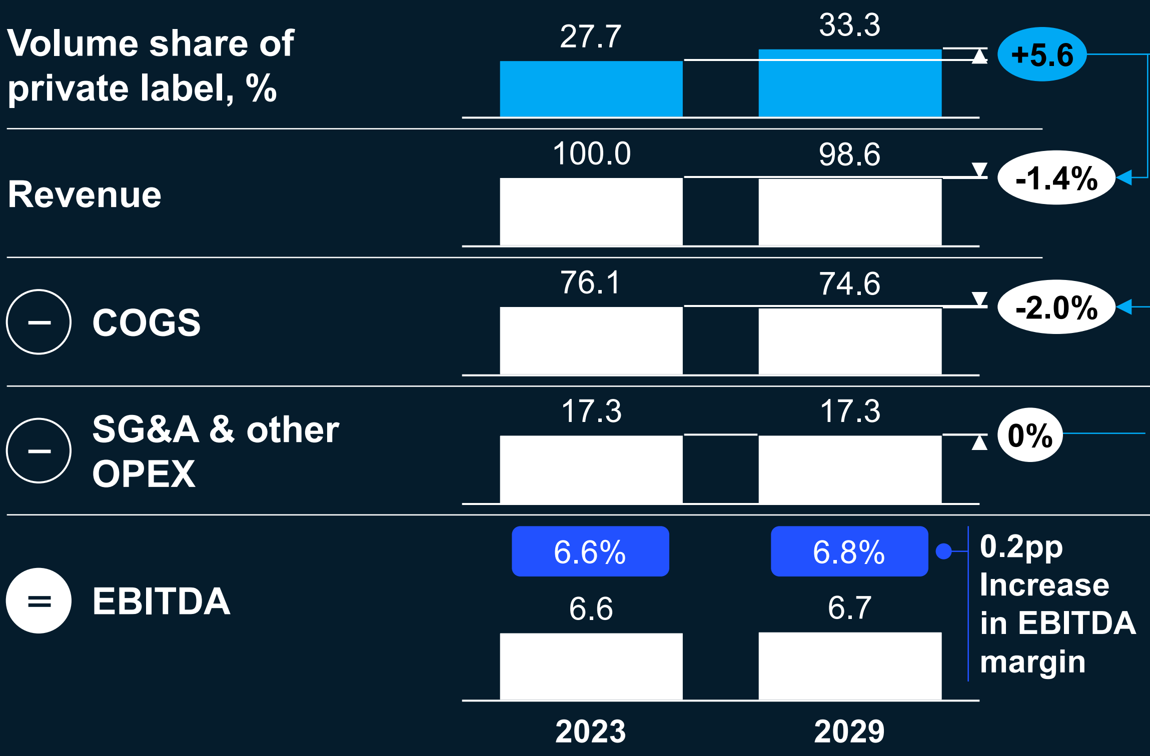
P&L development hyper/supermarkets, %

xx% CAGR, % xx% EBITDA margin, %

Financials indexed (2023 Revenue = 100%)

High case – *Private label share 33%*

Assumptions



× *-25% lower prices*

× *-35% lower COGS, assuming 10% better gross margin of private label*

OPEX are expected to stay stable due to relatively high share of fixed costs

Impact is calculated based on historical focus of super/hypermarkets on low value tier PL. With increasing focus on value-adding PL, effect could potentially increase further

Comment

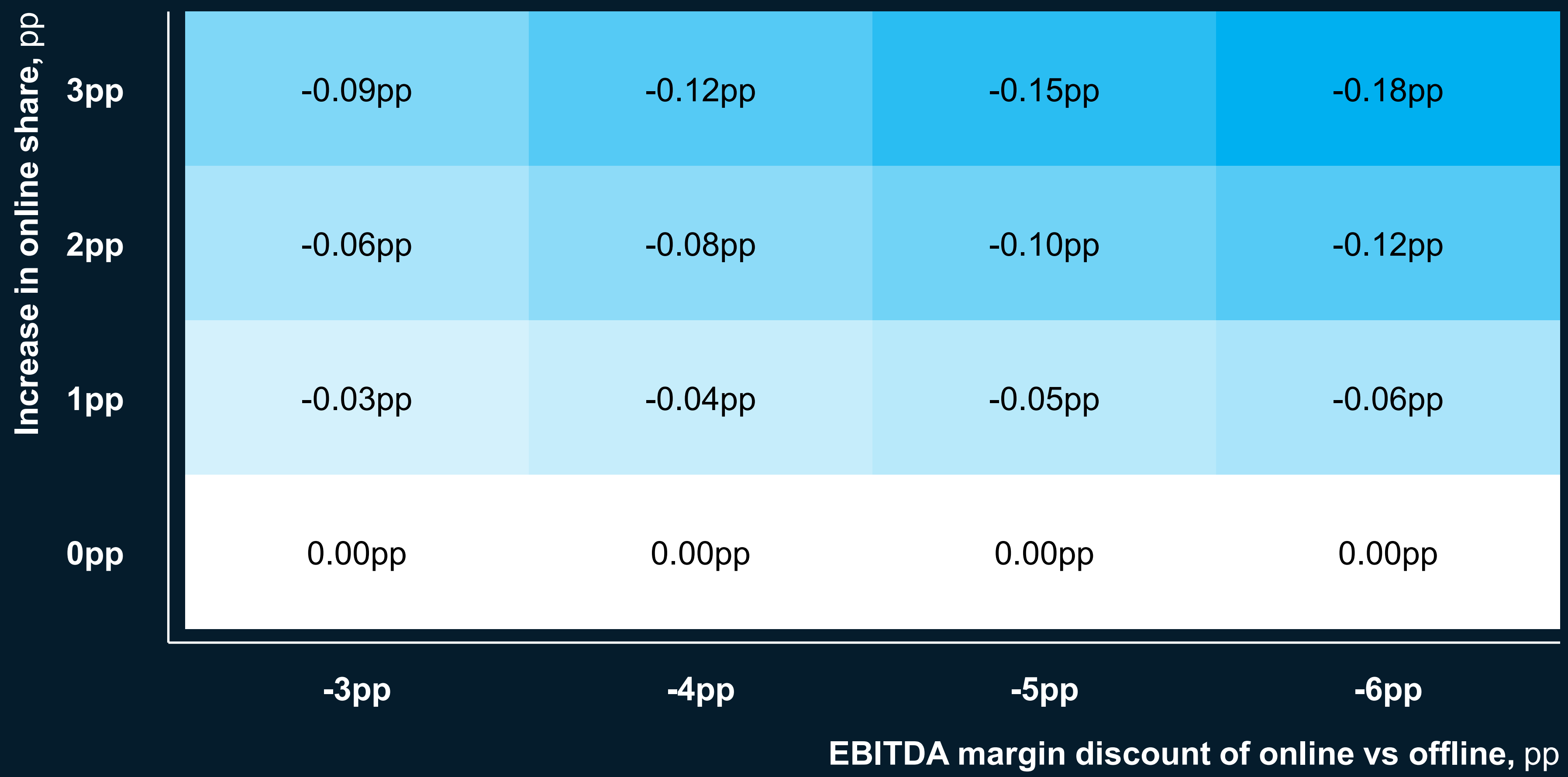
- In low case with 31% private label share by 2029, and assuming a 5% better gross margin of private label, the total impact on the EBITDA is 0.0pp

Source: State of Grocery 2024, ECB, McKinsey Value Intelligence, McKinsey Analysis, Morgan Stanley

6. Online market share is expected to grow from 6% by 1-3pp, resulting in a total EBITDA impact of -0.2pp to 0pp

⬜ Low delta 🟦 High delta

EBITDA margin change of hyper/supermarkets, pp



Increase in online share, pp	-3pp	-4pp	-5pp	-6pp
3pp	-0.09pp	-0.12pp	-0.15pp	-0.18pp
2pp	-0.06pp	-0.08pp	-0.10pp	-0.12pp
1pp	-0.03pp	-0.04pp	-0.05pp	-0.06pp
0pp	0.00pp	0.00pp	0.00pp	0.00pp

EBITDA margin discount of online vs offline, pp

Key assumptions

- EBITDA margin of online grocery is expected to be **3-6pp** lower compared to offline by 2029 (currently 5-10pp)

Source: McKinsey analysis, expert interviews

McKinsey
& Company