Emerging Opportunities For Global Retailers

The 2008 A.T. Kearney Global Retail Development Index™

The credit crunch that began in the United States and quickly spread globally has slowed retail growth and added to the financial stress of retailers worldwide. U.S.-based retailers in particular are grappling with lower same-store sales in their home markets, while the weak U.S. dollar is fueling inflation in Asia, consternation in Europe and Japan, and serious worries in general. That is especially true in China, which has more than $1 trillion in U.S. dollar-denominated sovereign reserves. As a result, emerging markets have retrenched, but not to such a degree that their overall growth has been endangered. That larger growth story remains very much intact.

Transformation is the watchword for retailers as economic turbulence continues into 2008. The economic conditions make for a tougher operating environment, but they are also among the most compelling reasons for the move toward a more global market. In fact, despite the setbacks in the United States and Europe, GDP growth across India, China and Russia is still expected to top 8 percent in 2008. This makes the retail opportunity in emerging economies more compelling (less than 10 percent of these markets are well-organized). For global retailers, the message is clear: Even when faced with tough economic conditions in their home markets, they can realize continued double-digit same-store sales growth and profits in their emerging markets. This kind of growth creates a powerful incentive for large retailers in developed countries. Pursuing expansion into new markets appears to be the best means to further diversify their customer and operations bases, and deliver continued growth and shareholder returns.

For these reasons and others discussed in this paper, 2008 will likely emerge as a landmark year for visionary retailers, those that have already begun entering emerging markets. It will allow them to muscle through the current economic turmoil and become truly differentiated from the competition. In turn, their performance will encourage other large retailers to expand or continue expanding in emerging markets. Failing to do so could not only constrain future earnings, but also cause retailers to miss large windows of opportunity.

Figure 1

The 2008 Global Retail Development Index™

2008 rank	Country	Region	Country risk	Market attractiveness	Market saturation	Time pressure	GRDI score	Change in rank compared to 2007
1	Vietnam	Asia	57	34	67	99	88	+3
2	India	Asia	29	39	78	93	80	–1
3	Russia	Eastern Europe	31	52	50	90	72	–1
4	China	Asia	36	50	45	82	67	–1
5	Egypt	MENA	22	34	90	64	66	+9
6	Morocco	MENA	26	36	80	68	66	+9
7	Saudi Arabia	MENA	49	40	63	50	62	+3
8	Chile	Latin America	44	52	45	58	60	-2
9	Brazil	Latin America	23	60	60	54	60	+11
10	Turkey	MENA	20	53	59	64	58	+3
11	Mexico	Latin America	38	59	40	56	57	–2
12	Algeria	MENA	15	34	90	50	55	+13
13	Malaysia	Asia	40	44	43	61	55	–5
14	Peru	Latin America	17	34	82	54	55	+8
15	Indonesia	Asia	13	41	71	61	53	+9
16	Bulgaria	Eastern Europe	28	32	42	79	51	–4
17	Ukraine	Eastern Europe	42	40	38	60	51	–12
18	Tunisia	MENA	29	34	76	41	51	–7
19	Colombia	Latin America	17	49	56	57	50	+11
20	United Arab Emirates	MENA	61	37	32	45	48	–2
21	Latvia	Eastern Europe	36	32	27	73	45	–14
22	Romania	Eastern Europe	27	30	21	85	43	+5
23	Slovenia	Eastern Europe	65	28	12	58	43	–6
24	Thailand	Asia	30	39	33	61	42	–8
25	Macedonia	Eastern Europe	13	20	74	53	41	NA
26	Philippines	Asia	14	46	76	24	41	–3
27	Guatemala	Latin America	13	15	87	41	40	NA
28	Argentina	Latin America	3	51	42	59	38	+1
29	Honduras	Latin America	4	13	91	45	38	NA
30	Lithuania	Eastern Europe	37	34	17	64	37	–2

Key: *On the radar screen* · *To consider* · *Lower priority*

Legend:

Country risk	Market attractiveness	Market saturation	Time pressure
0 = high risk	*0 = low attractiveness*	*0 = saturated*	*0 = no time pressure*
100 = low risk	*100 = high attractiveness*	*100 = not saturated*	*100 = urgency to enter*

Sources: Euromoney, World Bank, Global Competitiveness Report 2006-2007, *A.T. Kearney analysis*

Note: MENA = Middle East and North Africa

This is a snapshot of the findings and analyses in the 2008 A.T. Kearney Global Retail Development Index™ (GRDI). Now in its seventh year, the GRDI ranks the top 30 emerging countries for retail development. We analyze 25 macroeconomic and retail-specific variables to help retailers conceive successful global strategies *(see sidebar: About the Global Retail Development Index on page 7)*. Figure 1 highlights the 2008 findings.

In addition to the annual country rankings, this year A.T. Kearney introduces the Retail Apparel Index. This analysis of emerging market opportunities in the apparel segment begins on page 16.

Gauging the Window of Opportunity

The "window of opportunity" measurement introduced in 2006 remains a valuable tool for retailers as they develop global growth strategies. It identifies the points at which new retail markets begin demonstrating a pattern of organized retail, and when they will respond most favorably to innovative marketing approaches and management techniques.

Before the window of opportunity opens, investments in a new market can bog down due to myopic regulations, uninterested consumers and incapable supply chains. But all of that changes once regulators begin to understand the economic power of organized retail. Consumer shopping patterns begin to favor the formats and offerings global retailers can provide, and ancillary service providers arrive to take advantage of secondary or parallel opportunities.

The window of opportunity begins to close once regulatory barriers to entry become less onerous, and when many global competitors have already entered—having snapped up the best real estate and captured consumer mindshare. There may be additional opportunities in organized retail after this point, but only for retailers with the most innovative approaches.

Markets typically progress through four stages as they evolve from emergence to maturity, usually over the course of five to 10 years. These stages are: opening, peaking, declining and closing *(see figure 2 on page 4)*.

The 2008 GRDI analysis finds more countries now entering the opening and peaking stages, leading to a broader playing field and emphasizing the need for global retailers to evaluate these markets for areas of focus. The peaking stage is becoming more crowded as countries recognize the growth potential of—and consumer demand for—organized retail. New additions to this stage include Saudi Arabia, Morocco, Algeria, Egypt and Jordan.

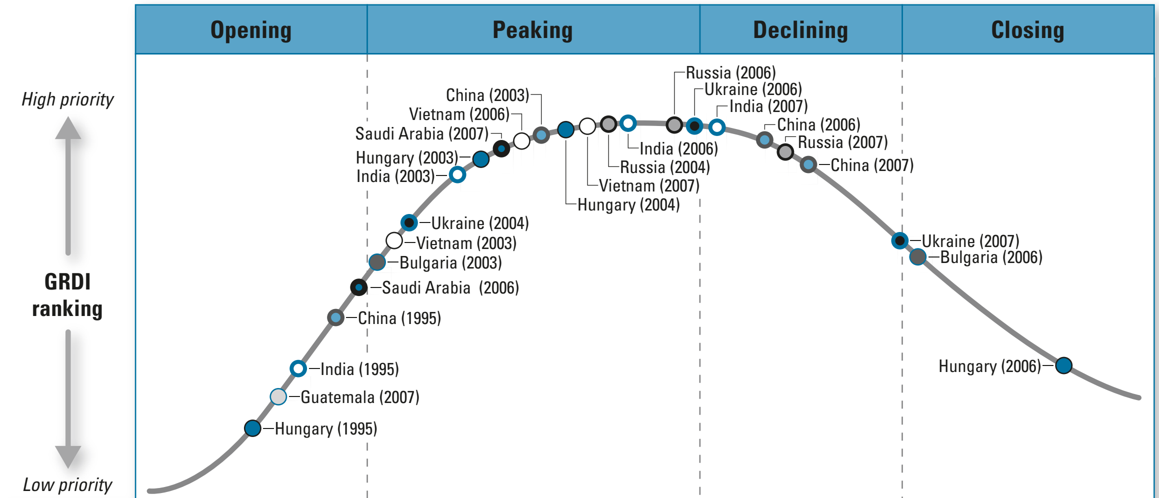
In the declining and closing stages, tier-two and -three cities (along with innovative formats) provide excellent opportunities. Apparel, electronics and entertainment are still strong growth areas in countries such as Hungary and Bulgaria.

The timeline for moving through the stages varies with the market. Generally, larger and more restricted markets will take longer—up to 10 years—to move from emerging to closing. Smaller, less regulated markets typically make the transition within three to five years. For example, Bulgaria and Algeria may rise and fall through the stages more quickly, but India, Russia and China will be viable longer. That said, we expect a decline in new market opportunities in larger countries over the next few years, particularly in major metro areas.

The 2008 GRDI Findings

As expected, Vietnam has become an attractive market and is drawing interest from large regional retailers. According to our 2008 GRDI, Vietnam remains among the most exciting opportunities, along with Morocco and Egypt.

Figure 2
Window of opportunity analysis



	Opening	Peaking	Declining	Closing
Action	Monitor markets and conduct consumer research	Identify local partners and real estate locations; establish pilot stores and the supply chain	Increase market entries to capture market share	Determine leadership status (profitability) in the segment
Format of entry	Consider minority investment in local retailer	Consider supermarkets, hypermarkets, cash & carry and convenience stores	Consider discount, warehouse stores and apparel	Move to wave-two formats, including EEO, DIY and specialized apparel*
Labor strategy	Identify skilled labor pool for market	Hire and train local talent and balance the expatriate mix	Change balance from expatriate to local staff	No pattern identified

Source: A.T. Kearney

**EEO refers to entertainment, electronics and office retailing; DIY is do-it-yourself*

For its part, India has had an unparalleled year. Its organized retail industry grew by more than 25 percent, with new entrants coming in across all formats and categories. In the grocery category alone, the top five firms had a combined store growth exceeding 50 percent. Specifically, Casino opened the first of 25 Le Marché stores it plans to open in India this year, while competition in China and Russia intensified as more retailers moved into the smaller, less competitive cities.

However, the credit crunch and higher cost of capital will make large-scale expansion on multiple fronts more difficult to sustain.

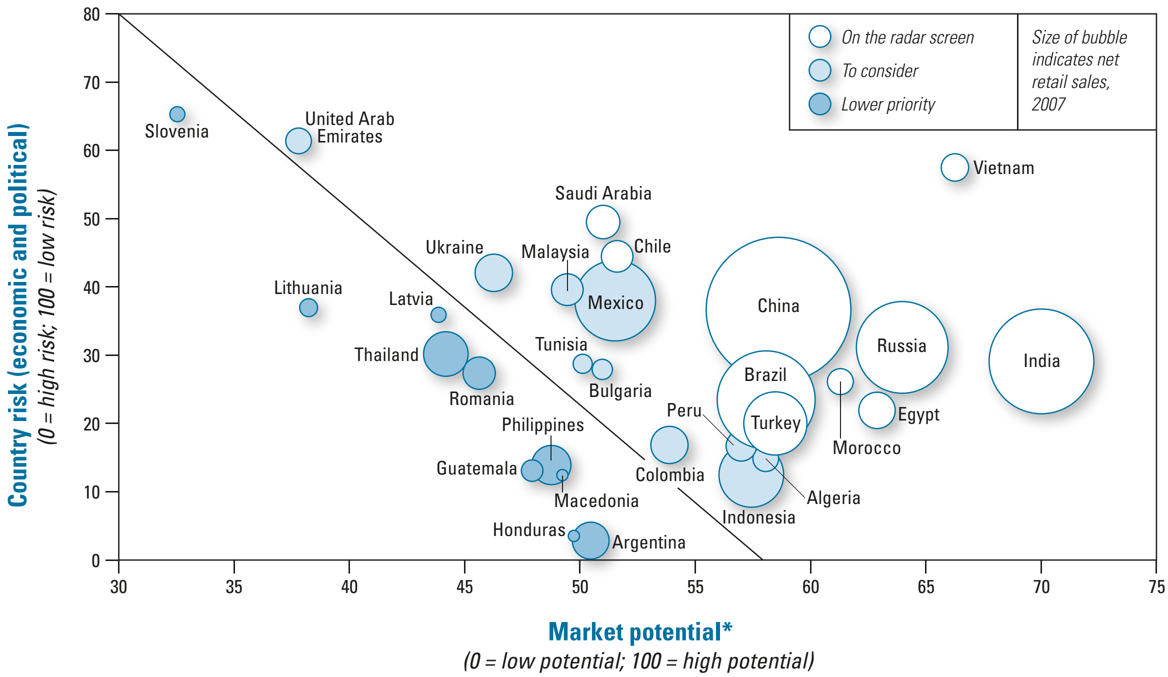
The relative market attractiveness for the top 30 countries in the Index is depicted in figure 3. The following offers a closer look at the current conditions underlying each region.

Asia Grows Up

Asia turned a corner this year. Despite the stumble across most developed markets, including the United States, Japan and Europe, Asian markets held their own. The region continues to see strong GDP growth, which is likely to top 7 percent in the coming year. In this year's Index, Vietnam steals the spotlight from the regional powerhouses, India and China. Although a much

Figure 3

GRDI 2008 country attractiveness



* Based on weighted score of market attractiveness, market saturation and time pressure of top 30 countries

Source: A.T. Kearney

smaller market than its two neighbors, at a mere $20 billion, the relative absence of competition and impressive GDP growth make it an attractive entry market for global retailers.

Vietnam: the shackles are off. Vietnam, with the perfect mix of opportunity and timing, tops the list as the most attractive opportunity for 2008. The regional progress of organized retail in the Philippines, Thailand and Malaysia has helped introduce Vietnamese consumers to modern retail. Additionally, the opening up of the Vietnamese economy has encouraged global retailers to capitalize on the opportunity. The official "arrival" of the Vietnamese market occurred with the entry of Dairy Farm and Best Denki, joining the METRO, Casino and Parkson groups in Vietnam.

With its recently deregulated retail markets, a stable political base and a robust economy, Vietnam will lead the other Asian mini-tigers this year with a GDP growth rate exceeding 8 percent. Although it is one of the few remaining single-party Communist countries in the region, its leaders are attempting to replicate China's economic success. The government is undertaking a broad-based privatization program. It will soon remove restrictions on 100 percent foreign ownership of retailers, and it recently launched a program to develop wholesale and retail real estate throughout the country by 2010. Given this ongoing economic reform and plans for attracting more foreign direct investment, its retail market is poised to take off.

The Vietnamese consumer is another reason to expect strong growth in the retail sector. With 79 million people under the age of 65, the country is fairly young. The opening of the economy, therefore, has resulted in a huge increase in consumer spending—more than 75 percent from 2000 to 2007. Also, the country is becoming more urban and concentrated. More than 1 million people a year are expected to migrate into two of its large cities, Ho Chi Minh City and Hanoi. With rising living standards, more consumers are switching from traditional, open-air wet markets to modern retail—tempted by a broad range of products, a more comfortable and hygienic shopping experience and less haggling.

In modern retailing, Ho Chi Minh City and Hanoi are Vietnam's most important cities. Ho Chi Minh City, with its nearly 8 million people and numerous middle- and upper-class consumers, will likely experience the most retail development from both local companies and foreign investors. Hanoi is perhaps five years behind Ho Chi Minh City in retail development. Among its more than 3 million people are civil servants and expatriates looking for a modern shopping experience.

Traditional mom-and-pop stores and wet markets still dominate, with the top five organized retailers owning less than 3 percent of the market. In Ho Chi Minh City alone, there are more than 6,000 mom-and-pop stores and more than 2,000 wet markets, the latter being a major source for grocery and personal care goods. Shoppers trust the freshness of the products they buy in wet markets, knowing they come directly from the field or wholesale market each morning. These markets also offer convenience, location, variable pricing and familiarity as consumers have developed relationships with the sellers. Convenience is especially important as the Vietnamese tend to buy their produce daily.

With its interesting mix of culture, growing middle and upper classes, and significant expatriate and tourist communities, Vietnam is also becoming an attractive entry market for global luxury retailers. Between January and April 2007, almost 450 Mercedes-Benz cars were sold, plus cars of other luxury brands. People are buying up luxury goods to increase their status. Gucci, Luis Vuitton, Cartier, Roberto Cavalli, Dolce & Gabbana, Burberry, ESCADA, Rolex, Clarins and Shiseido have established a presence in Vietnam.

India: a maturing market climbs the rankings. India continues to be among the most attractive countries for global retailers. At $511 billion in 2008, its retail market is larger than ever and drawing both global and local retailers. While GDP is projected to grow by more than 8 percent in fiscal year 2008, projections for 2009 are a more modest—at least by Asian standards—7 percent.

Organized retail, which still accounts for less than 5 percent of the market, is expected to grow at a compound annual growth rate (CAGR) of 40 percent, from $20 billion in 2007 to $107 billion by 2013. India's overall retail sector is expected to rise to $833 billion by 2013 and to $1.3 trillion by 2018, at a CAGR of 10 percent.

Consequently, as a democratic country with high growth rates, India's retail market opportunity is unchallenged. Consumer spending has risen sharply as the youth population (more than 33 percent of the country is below the age of 15) has seen a significant increase in its disposable income. In the past four years alone, consumer spending rose an impressive 75 percent.

But challenges have emerged that could potentially slow the pace of growth for new global

About the Global Retail Development Index

The annual A.T. Kearney Global Retail Development Index ranks 30 emerging countries on a 100-point scale—the higher the ranking, the more urgency there is to enter a country. Countries were selected from a list of 185 based on three criteria:

- Country risk: more than 35 in the Euromoney country-risk score
- Population size: more than 2 million
- Wealth: GDP per capita more than $3,000 (GDP per capita threshold for countries with populations of more than 35 million is more flexible due to the market opportunity)

GRDI scores are based on the following four variables:

Country and business risk (25 percent)

Country risk (80 percent): political risk, economic performance, debt indicators, debt in default or rescheduled, credit ratings and access to bank financing. The higher the rating, the lower the risk of failure.

Business risk (20 percent): business cost of terrorism, crime and violence, and corruption. The higher the rating, the lower the risk of doing business.

Market attractiveness (25 percent)

Retail sales per capita (40 percent): A score of zero indicates that the retail sector (total annual sales of retail enterprises excluding taxes) is still underdeveloped. A score of 100 indicates that the retail market is already mature, indicating an opportunity.

Population (20 percent): A zero indicates the country is relatively small, representing limited opportunities for growth.

Urban population (20 percent): Zero means the country is mostly rural; 100 indicates the country is mostly urban.

Business efficiency (20 percent): Parameters include government effectiveness, burden of law and regulations, ease of doing business and infrastructure quality. Zero means the country has poor business efficiency, while a score of 100 indicates high efficiency.

Market saturation (25 percent)

Share of modern retailing (30 percent): A zero indicates a large share of retail sales made through a modern distribution format within the average Western European level (200 square meters per 1,000 inhabitants). Modern formats include stores predominantly selling food (hypermarkets, supermarkets, discount stores and convenience stores), and mixed merchandise (department stores, variety stores, U.S.-style warehouse clubs and supercenters).

Number of international retailers (30 percent): The total score is weighted by the size of retailers in the country: three points for tier-one retailers (among the top 10 retailers worldwide), two points for tier-two retailers (within the top 20 retailers worldwide) and one point for tier-three retailers (all others). Countries with the maximum number of retailers have the lowest score.

Modern retail sales area per urban inhabitant (20 percent): A zero means the country ranks high in total retail area per urban inhabitant, close to the average Western European level. Modern formats are stores predominantly selling food (hypermarkets, supermarkets, discount and convenience stores).

Market share of leading retailers (20 percent): A zero indicates that the market is highly concentrated with the top five competitors (local and international) holding more than 55 percent of the retail food market. A 100 indicates the market is still extremely fragmented.

Time pressure (25 percent)

The time factor is measured by the CAGR (2002 to 2007) of modern retail sales weighted by the development of the economy in general (CAGR of the GDP and consumer spending from 2002 to 2007) and the CAGR from 2002 to 2007 of the retail sales area weighted by newly created modern retailing sales area. Results are from zero to 100, with 100 indicating that the retail sector is advancing quickly, thus representing a short-term opportunity.

Data and analysis are based on the United Nations Population Division Database, the World Economic Forum's *Global Competitiveness Report 2006-2007*, national statistics, Euromoney and World Bank reports, and Euromonitor and Planet Retail databases.

entrants—stifling regulations, soaring real estate costs and fiercely competitive domestic retailer groups. In addition, shopping mall projects are running into resource constraints that are delaying completions and disrupting many retailers' entry strategies.

Global retailers, hungry to enter this market, continue to be frustrated by restrictive government regulations. Under India's current laws, which the government relaxed somewhat in 2006, single-brand retailers can only own a 51 percent majority stake in a joint venture with a local partner.

Such relaxed regulations do not extend to multibrand retailers such as Wal-Mart, Tesco and Carrefour, which must operate through a franchise or cash-and-carry wholesale model. Accordingly, Wal-Mart recently joined forces with Indian telecom giant Bharti Enterprises. Bharti will own retail shops under the Wal-Mart franchise, and Wal-Mart will operate the logistics, procurement and storage activities. These giants are in a tight race for the retail leadership position in India. In the past couple of years, numerous retailers, including the SPAR Group, Carrefour, Marks & Spencer and Nautica have entered the market. Earlier entrants, including Wal-Mart and METRO, have plans for a blitz across the country. Wal-Mart in particular plans to expand rapidly across northern India. Tesco and Kroger will feel additional pressure as the situation grows more competitive.

Local hypermarket retailers are moving aggressively to get ahead of further loosening of foreign investment regulations. Taking their cue from the success of hypermarkets in China, local retailers such as Pantaloon, the Tata Group's Trent, RPG Enterprises, K Raheja Corp. and Reliance have all taken an early lead due to ambitious expansion plans. Seasoned businesses such as Reliance and Aditya Birla are locking up the upstream value chain (farms, logistics and storage) to better their positions once they begin competing directly with the likes of Wal-Mart.

As the retail industry in India matures, companies are pursuing new business models. For example, Reliance restructured and is now pursuing joint venture opportunities with international retailers such as Office Depot, Marks & Spencer and Neiman Marcus. The industry is also beginning to consolidate, with Aditya Birla acquiring Trinethra Superretail, the Wadhawan Group acquiring small regional retailers, and Actis investing in the supermarket chain Nilgiris.

Even as global firms prepare to enter India, some warning signs have emerged. Inflation is soaring (7 percent), real estate costs are prohibitive and the costs to acquire, train and retain workers have increased as more lucrative work opportunities emerge. Although the workforce continues to grow rapidly (with more women and farmers entering), it cannot keep up with the growth across all business sectors in India.

Still, large retail outlets hold a strong appeal for customers even though they place India's 4 million to 6 million mom-and-pop shops at risk. This is causing concern over the pace of change and could be another speed bump on the road to India's 1.2 billion consumers.

China: opportunities abound in smaller cities and innovative formats. China's countryside is turning into the next competitive retail battleground. Although China drops from third to fourth place in this year's Index, its strong GDP growth keeps it among the fastest growing economies in the world. Last year, Chinese GDP grew at more than 11 percent, outdoing all estimates. The growth rate in 2008 is expected to be a still impressive 10 percent.

The Chinese market remains highly fragmented. Retail chains are growing in the larger cities, but small, independent, subscale retailers cover the countryside. Less than 5 percent of the grocery market is serviced by the top five organized grocery retailers.

Hypermarkets still remain the primary growth format. Supermarkets currently have a significant presence but growth is slowing as hypermarkets and convenience stores, occupying opposite ends of the format spectrum, are replacing them. In some areas, despite the large format, the wildly popular hypermarkets are generating higher sales per square foot than the more dense supermarkets. Last year alone, Carrefour and Wal-Mart opened more than 50 new hypermarkets. On the other end, Tesco opened its first convenience store in Shanghai and plans to open five more of its Legou Express stores by the end of the year. Discount stores are also taking off, and this format will see strong growth in 2009.

Smaller cities, west and south of Beijing and Shanghai, are seeing strong growth as well. For example, Carrefour has opened a store in Urumqi in China's westernmost Xinjiang region, and Wal-Mart opened its 100th superstore in December in Loudi, in the Henan province. Currently, nearly 40 percent of Carrefour's stores are in secondary regions in China, and this trend will only get stronger in 2008 with increased competition in these secondary markets.

Middle East and North Africa: Retail Growth Arrives

The Middle East and North Africa (MENA) region is the hottest market for modern retail growth today *(see figure 4 on page 10)*. More than a third of the top 20 GRDI countries hail from this region. The strong euro and the power of the "petro-dollar" are the main reasons behind the recent retail growth in Morocco, Tunisia, Saudi Arabia and Algeria. The six nations of the Gulf Cooperation Council (GCC) are expected to earn $9 trillion by 2020, most of which will be reinvested over the next decade in local economies.

In India, seasoned businesses such as **Reliance and Aditya Birla are preparing** for the day when they begin **competing directly with the likes of Wal-Mart.**

Saudi Arabia alone is building seven economic cities. For example, within the next eight years, King Abdullah Economic City is expected to have more than 2000 factories and a population of 2 million.

Saudi Arabia: the kingdom embraces retail. Saudi Arabia moves up in the GRDI rankings this year to number 7. Its GDP grew by more than 7 percent in 2007 and it is projected to grow by approximately 9 percent in 2008. This puts it squarely in the Asian tiger league. With oil prices topping $100 per barrel, the country is poised to grow exponentially in consumer spending. Additionally, its sizable population of 24 million, increased tourism and tax-free status make Saudi Arabia attractive to retailers with expansion plans.

The Saudi market is the largest, most populous and the richest in the Gulf region. Despite a majority of small to medium-sized towns where retail is mainly in the hands of outdoor markets and *baqalas* (neighborhood stores), modern outlets are attracting Saudi shoppers, especially in cities such as Riyadh, Dammam, Jubail and Jeddah.

However, the retail sector is fragmented and unorganized. With more than $49 billion in sales, the top five retailers control less than 7 percent of the market. Casino and Carrefour have a presence in the country, but together they operate fewer than 35 stores. Plans are to double this number over the next few years. Domestic competition is strong, with local retailers such as Panda and Al Othaim Commercial Group hurrying up their expansion plans to strengthen their presence before more global retailers arrive. As a result, new merchandising, products and know-how are all making their way into the market.

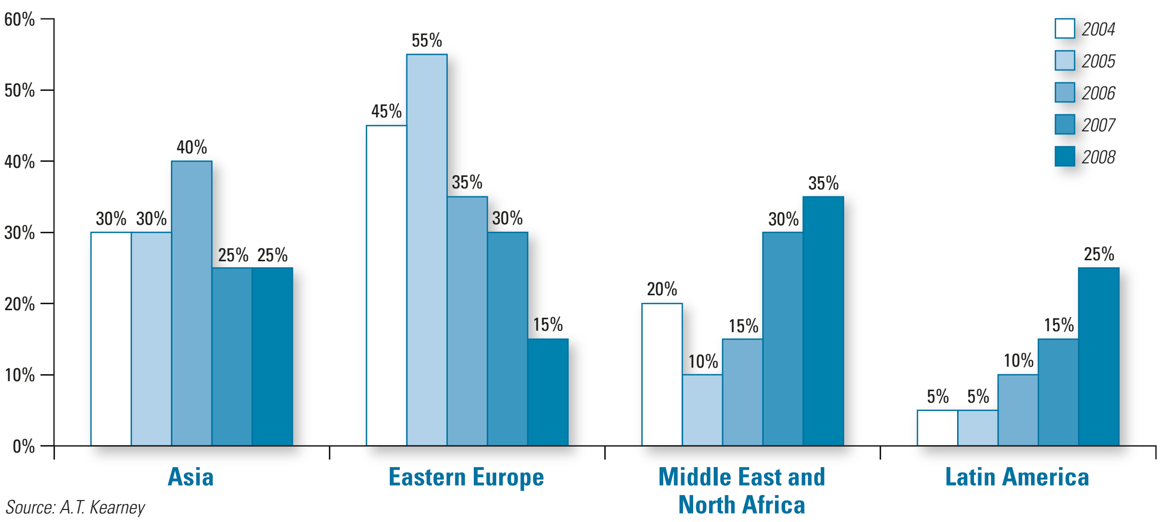
Hypermarkets are the most successful retail format in Saudi Arabia. Because real estate is inexpensive, the large-scale formats are becoming more popular. However, with more real estate locations being snapped up for outlets and malls, the race is intensifying.

Egypt, Morocco and Algeria: North Africa joins the party. In North Africa, three countries—Egypt, Morocco and Algeria—are experiencing strong economies, with 6 percent average growth projected for 2008. Morocco and Algeria, in particular, are benefiting from tourism and trade with Europe. Both countries are also relaxing domestic restrictions, encouraging foreign investment and experiencing more stable political and economic environments.

Egypt leads in economic development due to its continual economic reforms and investments in infrastructure. Tourism is a major growth driver, as is the stronger euro. But then,

Figure 4

Countries "on the radar screen" and "to consider" by region, 2004-2008



Source: A.T. Kearney

the Egyptian economy has been showing above-average growth over the past 10 years; in 2008, GDP growth is expected to top 7 percent. Egyptian retail consists largely of traditional outdoor markets, outlets and small neighborhood stores, with organized retail accounting for less than 1 percent of the market. Although Egypt's total market size is smaller than that of India or China, its lack of consolidation and the limited presence of organized retail make it an immense opportunity for market entrants. Hypermarkets are already in Cairo and Alexandria (situated in larger shopping malls), opened by Carrefour via its regional franchise partner, Majid Al Futtaim Group. The first domestic-style hypermarkets are emerging, opened by Spinneys and Seoudi Group. But their efforts are being hindered by structural and regulatory problems, including partisanship within business and government circles. Despite these challenges, Egypt remains one of the top retail opportunities in 2008.

Morocco, with more than 30 million people, is a regional powerhouse due to its location, favorable European trading relationships and tourist attractions. GDP growth is projected to reach 6 percent for 2008. These are still the early days of modern retail, however, as Morocco's retail sector is currently dominated by small corner shops and outdoor markets. Modern retail accounts for less than 3 percent of the market. The tax-free trading on the streets keeps prices low, which benefits shoppers and allows farmers and producers to operate free from government regulations. In larger cities such as Casablanca, modern supermarkets have been emerging within the past five years (mainly operated by independents) and attracting customers with higher quality goods and lower prices. This trend is accelerating. Until recently, European retailers, including METRO, Casino and Auchan, operated via joint ventures with a local company, such as Auchan's venture with ONA. They are now beginning to notice Morocco. With the exception of ONA and Hanouty, most domestic competition is still relatively small and independent, creating an entry opportunity for large global retailers.

Algeria, with the slow but sure return of political stability and economic recovery, is expected to achieve 5 percent growth of its economy in 2008. Historically, Algeria has not been open to foreign investors and it is a difficult place to do business. The retail market is fairly underdeveloped and in the hands of independent stores and street markets. Domestic competition is not well-developed; Algeria has only one retailer, Blanky, which is struggling to operate successfully. In the coastal towns, corner stores and small independents are the major form of retailing. Given Algeria's colonial past, French retailers have an inherent advantage in gaining political support. They also will have the better understanding of customer preferences and an easier time attracting and training a workforce. Carrefour, which is the only global retailer in the country (opening its first store in 2006), plans to expand to 20 stores over the next 10 years.

Latin America Matures

Retail in Latin American countries has matured over the years, so now second-wave opportunities are the ripest. Latin America also offers a wider range of targeted countries than before, with five countries in the GRDI top 20, up from only one in 2005.

Trends in overall GDP and retail sales growth in the region have been promising due to rising prices for commodities and favorable demographics. Spiking oil prices are benefitting the region and have led to increased foreign investment by two of its major countries, Brazil and Venezuela.

The developing countries have relatively young workforces, with Latin America's working-age population projected to grow through 2020.

Retailers will have to pay to play in Latin America—by being forced to pursue acquisitions or paying a premium for the most desirable locations—as the environment is still challenging. While Latin American countries have moved past the crises of the past decade, the threat of another crisis always looms large. Still, political and economic stability have gained traction, which means all of these countries have healthier economies and retail growth.

As Brazil's economy expands, an emerging **middle class will provide ample opportunities** for domestic and international entrants to **capitalize on the country's newly created wealth.**

Brazil: retail is on the rise again. Brazil has once again climbed up the Index, rising 11 spots to rank at 9th place this year. Brazil is by far the dominant economy in Latin America, accounting for slightly more than half of the continent's total GDP. Growing at more than 4 percent in 2007, Brazilian GDP is strong and projected to increase at a similar rate in 2008.

Much of that growth has resulted from the consistent and liberal policies established by Brazil's current president, Luiz Inácio Lula da Silva. The election of this leftist in 2002 was initially met with skepticism, and resulted in an unprecedented fall in the Brazilian real. However, da Silva instituted policies that brought about a boom in foreign direct investment (roughly a 100 percent increase in 2007). This foreign direct investment, combined with fewer government controls over prices and growing disposable income, have fueled a dramatic increase in retail sales—rising at a 17 percent CAGR since 2004.

Growth in both GDP and retail sales should continue to be supported by favorable demographics. With more than 190 million people, Brazil is the fifth-largest market in the world and has the second-largest population in the Western hemisphere behind the United States. The Brazilian population is also young—more than 60 percent is under the age of 29.

The retail market is not very concentrated. The top five retailers own roughly 25 percent of the market and no retailer owns more than a 10 percent share. Large international chains such as Carrefour and Wal-Mart plan to expand their formats and challenge the national retailer, Companhia Brasileira de Distribuição, for the number-one spot. Hypermarkets, mostly targeted at lower-middle-income customers, continue to dominate the landscape, while department stores offer additional consolidation opportunities. The few department stores that operate in the country target the large low-income segment. As the economy continues to grow, an emerging middle class will provide ample opportunities for domestic and international entrants to capitalize on the country's newly created wealth. That said, Brazil still possesses the largest wealth disparity in the region and an ever present threat of crime.

Chile: an attractive, yet aggressive arena beckons. Chile drops one spot to number 7 on the 2008 Index. Its GDP growth was stellar at roughly 6 percent in 2007 and is expected to top 5 percent in 2008. Disposable income is also on the rise. As Chile continues to recover from the economic crisis of 1999, and as Chileans become wealthier, the retail market will continue to grow and modernize.

Chile is among the most politically and economically stable and liberalized countries in Latin America, which makes it a low-risk destination for retailers. Retail sales have increased steadily over the past few years, with an estimated 5 percent growth rate for 2007. Although Chile enjoys the highest retail sales per capita of any Latin American country, its sales still lag significantly behind those of developed nations. The diverse economy, low corruption rates, minor wealth disparities and all-time high government surpluses make for a very attractive target.

Although the outlook is optimistic, competing in Chile is tough. The retail market is one of the most sophisticated and competitive environments in the region. The sector is fairly concentrated, with the top five companies accounting for approximately 60 percent of sales. Supermarkets and hypermarkets are the main formats in a market dominated by national competitors. These are the same national retailers that have managed to drive out international companies, including Home Depot, Ahold, Sears, JCPenney and Carrefour. For global retailers that are willing to play hard, Chile remains an attractive investment opportunity.

Colombia: new stability opens up a promising frontier. Colombia moves up an impressive 11 spots to 19 in the 2008 rankings. Political reform and stability led to an impressive GDP growth rate of almost 7 percent in 2007, and a projected 5 percent growth rate for 2008. Retail sales have also increased in the past decade, reflecting a 12 percent CAGR since 2004.

Colombia has long been one of the most dangerous countries in the world. Between 1948 and 2008, the country enjoyed just seven years of peace during lulls in its ongoing civil wars. The Colombian drug trade has provided the main financing for both past and present rebels. The country's current president, Álvaro Uribe Vélez, is a conservative who plans to end the long-term cycle of drugs, corruption and war. Through his hard stance and strong U.S. support, he has gained the upper hand against the drug traffickers and guerilla armies. This newfound stability has resulted in a much needed increase in foreign investment.

Retail in Colombia is comprised primarily of small, domestic mom-and-pop shops that offer additional services such as open credit and are located in close proximity to homes. Although the small shops have proven to be tough competitors, large companies do have some presence in Colombia, with the top five companies owning 35 percent of sales. Hypermarkets, which target the middle and upper classes, are also increasing their presence in the country, with Almacenes Exito, majority-owned by Casino, as the clear leader. Carrefour, the second-largest retailer in the country, is planning to invest heavily in Colombia through 2010.

Concerns remain, however, as the country is struggling to end 60 years of conflict. If President Uribe can achieve peace in his country, we can expect rapid diversification and economic growth fueled by an influx of foreign investment.

Eastern and Central Europe Present A Daunting Challenge

This year, Eastern Europe slips in the Index as countries in MENA, Asia and Latin America overtake them in the rankings. Soaring inflation, rising fuel costs, political uncertainty and regulatory challenges led to the fall of markets such as Ukraine, Latvia, Bulgaria and Lithuania. The former Soviet bloc faces economic challenges from free markets and unbridled growth in the recent past. How they deal with these hurdles will determine the attractiveness of these markets over the next few years.

Russia: robust retail reaches second-tier cities. Russia slips one place on the Index this year to number 3. Record high prices for crude oil and natural gas, its main exports, and strong domestic demand are contributing to a booming economy, making it the bright spot in an otherwise challenging region. GDP growth estimates have been revised upward from 6.5 to 7 percent. Russia is also expected to join the World Trade Organization (WTO) this year. That will give it access to foreign markets and help diversify its exports. It is also expected to retain its political stability, as former president Vladimir Putin was confirmed as prime minister earlier this year. The booming economy supports income growth and strong consumer spending. Some 60 percent of this spending is focused on retail sales. A large portion of the population (38 percent) is within the 15 to 39 age bracket, boding well for added consumption and spending.

While Moscow and St. Petersburg remain the most favored retail destinations in Russia, retail continues to expand to second-tier cities and industrial regions. Faced with sluggish growth in domestic markets, foreign retailers continue their entry and expansion into Russia. South Korea's Lotte opened a department store in Moscow at the beginning of 2007. Carrefour plans to open its first two stores there by the end of 2008 and add five more stores in 2009. While its first store is expected to open in Moscow, the additional units will be located mainly in regional and second-tier cities. Despite sluggish global sales—weighed down by the impact of a slowing global economy—IKEA remains positive about continuing its expansion into Russia. It is committed to making this capital expenditure, having opened stores in Novosibirsk and Rostov-on-Don. IKEA plans to open two more stores during its 2008 fiscal year in Krasnodar and Samara. Wal-Mart has named an executive, Dr. Stephan Fanderl, as President of Wal-Mart Emerging Markets—East. He will explore expansion into Russia and other neighboring markets. German retail and tourism group Arcandor's retail chain, Karstadt, plans to open several outlets in Russia's main cities.

Market saturation, increased domestic consumption and higher disposable incomes are leading retailers to expand into industrial cities such as Yekaterinburg in the Ural Mountains region, Novosibirsk in western Siberia, and the densely populated areas of Nizhny Novgorod and the central Volga region. X5 Retail Group, Russia's largest supermarket chain, has exercised its option to buy the Karusel hypermarkets for up to $970 million as it seeks a bigger share of Russia's consumer boom in the regional cities of Nizhny Novgorod, Yekaterinburg and Volgograd. METRO, the largest cash-and-carry operator in Russia, has opened about 30 outlets and has expanded into central and southern Russia and the Urals.

Russia, however, remains a tough place to do business in. Licensing presents potential issues, as do opaque real estate costs and inflation, which is still hovering at more than 7 percent.

Ukraine: competition increases for investments. Ukraine slips from 5th to 17th place in the GRDI rankings. It faces several problems—poor infrastructure, bureaucratic red tape, ongoing political instability and soaring inflation (17 percent). At issue are increasing money supplies and high fuel costs. Russia, the main supplier of Ukraine's oil and gas, has increased fuel prices by 400 percent since 2005.

Most of the country's retail markets are also still protected by high tariffs. These will have to be removed ahead of any WTO membership. A booming Russian economy and the benefits of European Union integration for other Central and Eastern European countries are also diverting precious foreign investments. International retailers from Western Europe are investing and expanding, but mostly in business-friendly Russia and Bulgaria.

Many retailers have slowed their plans. REWE, which entered Ukraine in 2000, has only opened 10 BILLA supermarkets, while Auchan will not open its first store until the summer of 2008. Even METRO, which has 18 cash-and-carry stores, is likely to slow expansion. However, Ukraine remains on the radar screen for many retailers, especially those that seek markets adjacent to Russia. Its geographic proximity to Western Europe is also a plus.

Food accounts for roughly two-thirds of total retail sales in Ukraine. While retail sales remain strong in Kiev, Dnipropetrovsk, Donetsk and Odessa, it could take some time before regional cities can provide a truly attractive investment zone for international grocery retailers.

With limited competition from cautious foreign competitors, domestic retailers are seizing the opportunity—even though most are regionally focused. Amstor and Velyka Kyshenia, the leading hypermarket operators, almost doubled their number of stores in 2007 and continue to expand.

Baltic states: retail is struggling. The recent retail frenzy in the Baltic states has abated as these countries face spiraling inflation. Latvia has the distinction of having the highest inflation rate in the European Union at 16.8 percent, a 12-year high. In Lithuania, which is the largest Baltic state, inflation is at 11.4 percent. This has adversely affected retail sales, especially in major spending categories. At this point, the Baltic state consumers are weary shoppers.

This explains why Latvia drops 14 places in the Index to 21 and Lithuania barely hangs on at number 30. Still, Marks & Spencer, in a joint venture with COMS, will expand on its current 13 Marks & Spencer stores in the region, opening stores in the Czech Republic, Slovakia, Latvia and Lithuania. Marks & Spencer intends to open 30 more stores in these markets and perhaps enter Estonia.

> For global retailers, the message is clear: **Companies can continue growing** sales and profits in emerging markets **even when faced with tough economic conditions at home.**

Rimi Latvia and Maxima, the two existing retail chains in Latvia, continue to dominate the domestic market since they face limited new competition. The Rimi Baltic Group (Rimi Latvia's parent company) now operates 215 stores in the Baltic region with 56 stores in Lithuania, 94 in Latvia and 65 in Estonia. The dominance of these two companies offers tremendous market power in dealing with producers and suppliers.

The Retail Apparel Index

Within this year's GRDI, we introduce the A.T. Kearney Retail Apparel Index. This Index isolates emerging market opportunities in the apparel segment from the larger global retail picture. The analysis evaluates more than 30 apparel markets to identify the top 10 countries in terms of market size, growth prospects and consumer affluence *(see figure 5)*.

The Retail Apparel Index is comprised of market indicators (55 percent) and growth indicators (45 percent). Market indicators include total clothing sales and imports, total and youth population, and clothing sales per capita. Growth indicators include total clothing sales, compound annual growth rate (CAGR) in clothing imports and clothing sales per capita, population growth and CAGR of GDP per capita. Within each metric, a country is assigned points based on its value on the metric against the largest in the sample. For example, China has the largest total clothing sales at $93.5 billion, so it scores 100 points in this metric. Brazil has $76 billion in total clothing sales, so it scores 81.4 points (76 divided by 93.5 times 100).

Brazil: fashion forward and fragmented. Brazil tops the 2008 Retail Apparel Index due to the country's total expenditures on apparel, higher per capita spending on the sector, and level of clothing imports. Brazil is among the world's fastest growing clothing markets, increasing at more than 7 percent a year. Total sales

Figure 5
The Global Retail Apparel Index, 2008

Rank	Country	Absolute market size	Growth prospects	Consumer affluence	Score
1	Brazil	45	33	42	48
2	China	74	22	36	47
3	India	57	37	31	47
4	Turkey	29	37	59	46
5	Chile	22	47	44	46
6	Romania	21	54	34	45
7	Argentina	21	44	39	41
8	Thailand	22	25	57	40
9	Russia	52	22	39	39
10	United Arab Emirates	31	42	28	38

Source: A.T. Kearney *Note: Scores are rounded* in the clothing sector have exceeded 30 percent over the past five years.

The Brazilian population is young, with more than 60 percent under the age of 29. The young Brazilian consumer is fashion conscious and ready to devote a significant portion of income to apparel. Apparel sales on a per capita basis are remarkably high at $402 per person—six times more than the average Chinese consumer spends. Also, Brazilian consumers use more credit when buying apparel than their emerging-market counterparts. Private retailer cards generate 46 percent of all apparel sales in Brazil today—as much as the United States and the United Kingdom generate individually. Indeed, clothing retail leaders Riachuelo and C&A have issued more cards (13 million and 16 million respectively) than Visa and MasterCard. Credit is a very profitable business line.

Although Brazil is the sixth-largest apparel manufacturer in the world, its domestic production is insufficient to fulfill local demand, so the country imports significant amounts of apparel. Imports exist despite tariffs and the longer supply chains to low-cost sourcing hubs such as China.

Brazil's domestic retail market is highly fragmented. Smaller, local retailers account for more than 60 percent of the market. Domestic retailers, including Riachuelo, Renner, Pernambucanas and Marisa, dominate the organized mass market landscape. These retailers do not have the economies of scale, broad base of suppliers or operating efficiencies of the large chains. The upper class is served by only a few multinationals, including Mango, Miss Sixty and Zara. The Brazilian retail industry records lower profit margins due to small, fragmented, subscale and dispersed competition.

Despite few barriers to entry, only a handful of global apparel retailers are operating in the country today—a situation that will not last for long. To succeed in Brazil, major retailers would be wise to develop new capabilities in credit management, local product sourcing and innovative marketing. They should also marry their operational and scale efficiencies with attractive credit services and local merchandizing. As the credit markets widen, and consumers mature over the next few years, the environment will become consolidated and flooded with global competitors.

China: a strong tier-two story. Brazil only narrowly edges out China and India in the Retail Apparel Index, despite the fact that both countries have much larger populations. China has the third-largest retail apparel market in the world, valued at $93.5 billion. Only the United States ($232 billion) and Japan ($100 billion) are larger. Still, organized apparel retail forms a small portion (17 percent) of total apparel retail in China compared to the United States (85 percent). Apparel retailers are primarily concentrated in China's tier-one cities, such as in Shanghai, where apparel sales in department stores and malls account for an estimated 65 to 70 percent.

Among all the apparel segments, key areas such as women's apparel will be responsible for much of the growth over the next few years, especially as urban fashion trends begin to shape tastes and influence personal style. Much of the rise in apparel sales is due to an emerging affluent middle class in the cities. This group regularly buys mid- to low-end apparel for daily needs, and buys one to three mid- to high-end pieces every year for special occasions. Price is the most important criterion in these purchase decisions, followed by quality, brand, fit, design and the shopping environment. Online purchases account for some of the growth, with apparel and bags among the leading categories.

For retailers, there are several nuances that require a better understanding of Chinese customers in local markets. For instance, the average apparel size is different in China than in other countries, and even within the country, there are size differences among consumers in the north and south. Climates across the country vary widely, requiring region-specific entry and management strategies.

Among the biggest challenges for international retailers is affordability. Spending on apparel is $70 per capita annually, which is significantly lower than in most other countries. Locals can afford to spend about 25 percent of what foreigners spend on apparel. Even premium customers in China generally spend only about 50 percent of what foreign visitors spend.

Several large international apparel retailers, including Etam, Giordano International and Mango, are currently operating in China. With average annual sales of $300 million, Etam operates more than 2,400 sales outlets in China alone. Giordano, which operates under multiple brand names, operates more than 1,700 stores worldwide, with 820 stores in China. The company plans to open 50 additional stores in China.

These retailers are facing growing competition from domestic competitors. For example, the Wuhan Hanshang Group, headquartered in Hubei Province, has sales of $65 million. It is a diversified conglomerate, providing tourism, exhibition and related services.

India: open for business. Apparel is India's second-largest retail category (behind food and groceries), representing 10 percent of its retail market. Projected to reach $37 billion for 2008, apparel will be among the highest growth categories, with a CAGR of between 12 and 15 percent.

In 2008, organized retail will represent roughly 20 percent of the total apparel market. This is expected to reach 35 to 40 percent by 2013. This rapid growth is supported by the burgeoning Indian middle class. Mean annual disposable income is growing at more than 6 percent CAGR; consumer spending is expected to increase 8 percent per year, faster than the United States, the United Kingdom, Japan and China.

Other factors supporting these brisk growth rates include more apparel-focused shopping malls, continued penetration of credit cards, organized apparel retailing in tier-two and -three cities, the popularity of ready-to-wear clothing and Western fashions for women.

Still, India's apparel market is highly fragmented. The top seven competitors represent less than 10 percent of the total market. Customers tend to be loyal to a specific retailer—Shopper's Stop, Westside and Pantaloon—instead of any particular apparel brand. This has led to a thriving private label apparel market for ready-to-wear clothes and more competition. However, brands such as Benetton, Louis Philippe, Van Heusen and Esprit are capturing a strong following among Indian consumers.

There is a flurry of activity across all price points, with new concepts and brands being launched almost every month. Madura Garments joined Peter England People, a mass market family store modeled after Gap and Old Navy. Discounter Koutons has opened nearly 1,000 stores in the past few years.

A key challenge for apparel retailers in India is to induce customers to purchase quickly, which means sales promotion tactics are important, including end-of-season sales, festival promotions and special events.

Under India's current laws, single-brand retailers can own a 51 percent majority stake in a joint venture with a local partner. But these rules do not apply to multibrand retailers such as Wal-Mart and

Carrefour. The trend is toward further loosening such regulations, opening up the market to global apparel retailers. However, local companies are fortifying their positions for the pending assault.

Foremost among these local firms is the Future Group, with sales of $845 million. It has more than 5 million square feet of retail space in roughly 450 stores across 40 cities. Its principal formats include Pantaloon, a department store chain, and Big Bazaar, a hypermarket chain. Shopper's Stop is another strong domestic competitor with 1.5 million square feet of retail space across 88 stores in 12 cities. The group plans to have 6 million square feet of retail space by 2011.

A Landmark Year for Retailers

This year is shaping up to be a turbulent one for global retailers—the credit crunch may have started in the United States, but it has quickly spread around the globe, creating financing woes for existing and expanding retailers. Although the European markets have fared better so far, this scenario cannot last long given the turmoil across the Atlantic. As a result, 2008 will be a landmark year for visionary retailers that differentiate their companies from the competition by expanding into new emerging markets. For large mass market retailers, the message is simple: Expand or perish.

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