Deloitte.

Retail Globalization
Navigating the maze

Contents

Introduction

Over the past decade, a growing number of globally minded retailers have reduced their dependence on their home markets, where sales have stagnated in recent years, and made expansion into more attractive foreign markets a priority growth strategy. However, globalization requires a substantial investment of time, money and resources. As retailers have moved into unfamiliar and unpredictable territory, many have faced serious setbacks, failing to fully appreciate the unique challenges posed by different economic, political, and cultural environments. Proper due diligence into the obstacles as well as the opportunities will help retailers set and achieve realistic goals for increased sales and profitability as they tap into new growth markets.

Deloitte has identified six key aspects of globalization that can create roadblocks for retailers contemplating international expansion. The first two deal with assessing risk, both the organization's threshold for risk and the risk posed by the growing power of local competitors. The next two issues – the need for strategic localization and an assessment of market entry methods and market attractiveness – are critical considerations for strategy development. The last two topics address people and power issues through human resource development and enterprise governance.

Experience has taught us that going global is more than the liberalization, modernization or "westernization" of markets. While globalization involves the diffusion of products and practices, information and ideas, it must be grounded in the specific culture of consumption in each local market.

This report illustrates not only the potential pitfalls, but also the promise of globalization. Looking back has the advantage of learning from the mistakes of the past. Looking ahead, the case for globalization is compelling. While there are no easy answers, for many retailers, going global represents the best path to long-term growth and, eventually, profitability as well.

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Navigating retail global expansion

Managing the risk/reward tradeoff

Every retailer that has expanded into foreign markets or has even thought about it knows only too well – globalization adds layers of complexity to every aspect of doing business, creating greater risk exposure. Merchandising, marketing, store operations, real estate, human resources, reporting requirements, tax policy – all must be reevaluated in light of a new consumer culture, competitive set, or regulatory environment. In addition, economic uncertainty, political instability, currency fluctuations and other macro-environmental factors beyond the retailer's control add to the risk of doing business in foreign markets. Before a retailer can decide what role, if any, international expansion will play as part of its overall growth strategy, it is important to evaluate and manage the company's threshold for risk across these multiple dimensions.

There are several key issues that deserve specific attention as companies consider their appetite for risk. Among the most important are realistically managing return on investment expectations; ensuring brand integrity; and assessing the retailer's corporate global leadership capacity, functional capabilities and resources. These issues are under the retailer's control, but without careful consideration they can become stumbling blocks to successful globalization.

Payback expectations: Take the long view

International sales have contributed to growth for most of the world's leading retailers. However, return on investment has not always followed – at least not as quickly as expected. Different countries are in different stages of maturity with regard to economic and retail development and pose different levels of risk. As a result, different timelines for payback will be experienced. In emerging markets, where a host of country-specific hurdles can impede progress, it can take years simply to break even. Payback delays can result from protectionist governments, poor infrastructure development, the condition of the local supplier market, and bureaucratic red tape or corruption.

Protectionism: Even as governments open up their retail sectors to foreign direct investment, they are often actively helping local retailers to modernize and remain competitive through protectionist policies and financial support. For example, foreign retailers have complained about Vietnam's application of an Economic Needs Test (ENT) requirement before allowing them to open a second retail outlet. The Malaysian government has designated retailing as a National Key Economic Area. Federal and local authorities are striving to achieve a balance between modernity and convenience and the sustainability of the small, local retailers. They are assisting local players in developing new, large format outlets through commercial loans or acting as an equity partner via government-linked investment companies (GLICs).

Infrastructure deficiencies: A well-developed infrastructure, including transportation, power supply, and information and communication technology, is key to large-scale retail development, but in many emerging markets this is not always up to par. An otherwise attractive market can be hampered by difficulties and delays resulting from under-developed infrastructure.

An efficient distribution system, for example, depends on a well-developed and well-connected transportation system, from port to railway to highway. A transportation network that is poorly connected means that goods have to be warehoused while in transit, leading to substantially higher costs and more waste, especially with regard to perishable goods when there is a lack of cold storage infrastructure. The lack of a robust IT network with real-time communication linking stores and suppliers makes it difficult for retailers to manage their supply chains.

Lack of control over supply chain: Over the past 20-30 years, the balance of power between retailers and manufacturers with home markets in Western Europe and North America has tilted decisively away from suppliers in favor of large retailers as the retail industry consolidated. Enormous buying power has allowed retailers to exert a great deal of control over product specifications, pricing, logistics, inventory management and other aspects of the supply chain. This, in turn, has become a competitive advantage for some of the world's largest retailers.

The nature of the supplier-retailer relationship in emerging markets is often quite different. Purchases are often made from thousands of small, relatively unsophisticated local suppliers. Several layers of distributors may exist between the manufacturer and the retailer, and each layer receives a markup. There is often little or no collaboration between vendor and retailer. Disparate systems and data formats add to the complexity.

As the retailer expands nationally, logistics can become even more challenging because few distributors can supply nationwide. Localized assortments, therefore, require relationships with multiple vendors of similar goods. In some cases, retailers may choose to source locally simply to avoid the high cost of transportation and storage.

Another issue involves low fill rates from vendors, which can make it difficult to implement effective merchandising programs. Moreover, small suppliers enjoy a certain power over foreign retailers, as they often have an option to supply other major retailers. Finally, there may be government rules about local sourcing for certain products. This lack of control over the supply chain can create inefficiencies and add unanticipated costs of doing business in developing markets.

Red tape and corruption: Multilayered, inefficient, and at times seemingly arbitrary government bureaucracy is another issue that can cause projects to be delayed, sometimes for years. Occasionally, in addition to red tape, foreign retailers may have to navigate approaches to business that are at odds with their corporate values. A morass of regulatory challenges or a lack of transparency in government regulation makes some countries, like India or Russia, difficult markets to enter and can make taking a local partner a near necessity.

For all retailers, profitability, rather than growth, eventually must become the priority in foreign investment. As these issues illustrate, however, retailers will need to take the long view. They must be willing and able to make long-term commitments and potentially sustain prolonged losses before realizing any gains. This will likely be even more daunting for smaller enterprises with fewer resources and less capacity to manage complexity and bureaucracy.

Missed ROI expectations in developed markets

While the constraints of doing business in emerging markets can make payback times uncertain, missed ROI expectations can also occur in developed markets. One reason is underinvestment. Entry into a strategically important market involves the commitment of significant resources, which entails increased risk. Retailers unwilling to invest sufficient resources to achieve economies of scale will often need to adjust their payback period. Payback delays in developed markets also result from overly aggressive revenue assumptions, which may result from a misalignment with market needs or poor execution leading to lower-than-expected consumer adoption.

Ensuring brand integrity

Because retailers sell products to the end consumer, they must be careful to ensure the utmost integrity of their "brand." This is an issue that all retailers need to pay attention to, but it is critically important for single-brand retailers where the retailer *is* the brand.

A burgeoning middle class in emerging markets, growing media penetration, and worldwide marketing of brands have led to a convergence of consumer aspirations that has increased the demand for foreign brands around the globe. As retailers expand outside their domestic market, it is important that they protect against potential devaluation of their brand assets. This requires that they understand, plan for, and monitor the many potential risks to brand integrity that could result from foreign activities up and down the value chain, including manufacturing standards and product safety, working conditions, and sales tactics. For example, despite having strict ethical standards, a number of high-profile retailers have seen their brand reputation damaged at least temporarily in recent years by revelations, or simply accusations, of working with unscrupulous suppliers that use child labor, fail to pay a living wage, or otherwise exploit workers.

For all retailers, product safety violations and counterfeiting pose a serious risk to the "brand." Globalization increases that risk as retailers become dependent upon extended supply chains using multiple vendors. Food retailers, in particular, will need to expand their tracking and tracing capabilities to ensure food safety. As international retailers look to source products faster and at lower cost, it is critical that they also make product quality and safety a priority.

Capability assessment

The ability of corporations to run global operations is another critical risk assessment factor. A retailer's globalization potential depends on an honest assessment of its corporate global leadership capacity, functional capabilities, and resources.

Successful foreign operators usually have a leading position in their home market and strong liquidity. But success also requires corporate leaders with an enormous capacity to learn and adapt, the willingness to embrace different cultural perspectives, and a high tolerance for frustration and uncertainty. The ability to galvanize large and increasingly diverse groups of people to work together toward a common purpose is another critical global leadership skill. As a business expands internationally, areas such as strategy development and talent management become more complex, requiring a further refinement of leadership skills.

The globalization of retailing activities can also be an execution challenge, stretching an organization's functional as well as leadership capabilities. Finance, information technology and human resources – not to mention the more retail-specific activities of merchandising, marketing, store operations and logistics – must now be carefully orchestrated and coordinated across multiple disparate markets.

A key component of global strategy development requires the retailer to determine to what extent its competitive advantage is based on firm-specific functional capabilities and whether or not they are easily transferable to other global locations. If the organization underestimates the internal capabilities and resources needed to operate in a new environment, it can pay a steep price, including expansion delays and/or financial overruns, while it scrambles to align its competencies and workforce with the organization's global objectives. Finally, the right global talent pool means not only having the appropriate skills and resources to manage the global expansion, but also that resources are available to focus their attention on the company's global ambitions.

An unintended consequence of focusing the organization on global expansion is the potential impact it can have on the core business. A retailer must always be cognizant of protecting the core business while exploring growth opportunities. Too often, we see retailers pulling critical resources to focus on achieving global growth without a plan to protect its base business.

Because misaligned or insufficient leadership skills, functional capabilities or available resources can threaten global expansion strategies, having a clear understanding of the organization's capabilities – and then identifying and filling talent and leadership gaps – is critical to success.

The growing power of local competitors

Over the past two decades, the ability of foreign retailers to bring leading-edge practices to relatively unsophisticated markets has resulted in a migration from traditional retailing to modern, organized retail formats in developing markets around the globe. However, as the transformation of the retail sector progresses in these markets, many strong national and regional players also have emerged across formats and product categories. One obstacle that is often underestimated when foreign retailers assess the opportunity in emerging markets is the growing power and sophistication of the local competition, which is often stronger than it may appear.

Local retailers, quite naturally, have a better understanding of local consumer culture. They have already secured the best retail locations. They have well-known local brands and a history with local consumers. They may also benefit from protectionist initiatives and restrictions placed on large multinational players. In addition, many local retailers are focused almost entirely on the local or national market and, therefore, have greater flexibility than their foreign rivals to tailor company strategy specifically to that market. At the same time, they quickly learn how their global counterparts operate and copy their best practices.

In addition, many domestic retailers in emerging markets have used the recession to restructure their operations and are now gearing up to expand rapidly – not only nationally but regionally in a trend that is shifting the global retail landscape. During the next few years, there will likely be a wave of consolidation in emerging markets among both local and foreign retailers as they attempt to deepen their market penetration in order to secure or fortify a leadership position. This will make it more difficult for any new entrants to penetrate the market.

The need for strategic localization

Retailers' close and personal relationship with consumers makes for a complex business – especially if those consumers are scattered around the globe. Consumption is a sociocultural process as much as it is an economic interaction. Therefore, in addition to understanding the demographic characteristics of the population, such as age, income, and family size and structure, retailers need to be responsive to local culture and traditions, tastes, preferences and shopping habits, which can be quite different from one country to another and sometimes within a single country.

How often do consumers shop? Do they travel by car or bus? What are their expectations for quality and freshness? What colors do they prefer? What is the average size for clothes and shoes? Are there psychological barriers for prices of certain products? What is the consumer's definition of "value"? Understanding the needs of diverse consumer groups is not easy. And the growing power of local competitors who possess this detailed market knowledge makes the need to develop a strategically localized identity in foreign markets all the more critical.

At the same time, while every market is unique, the tastes and preferences of consumers from around the world are becoming more similar. Increasingly, consumers everywhere want the same things—the things they have heard about or seen on the Internet or in the movies. This has resulted in the emergence of global markets for many standardized consumer products such as consumer electronics, entertainment and media, and fashion apparel and accessories.

While the extent of localization depends in part on the type of product offered (e.g., commodity items versus luxury goods), "acting local" goes beyond products and sourcing. Strategic localization also involves localization of merchandising (including packaging and display), store layout and ambience, marketing and promotion, formats and brands, site selection, staffing and customer service—the entire value proposition needs to be re-evaluated to determine its viability in a different cultural and competitive environment.

The tradeoff between localization and standardization is a balancing act. Many retailers have found that a global standardization strategy often does not elicit sufficient response from local consumers. At the same time, extensive localization means costs will inevitably increase. Global businesses must also strive to ensure that localization does not mean the loss of corporate identity.

The tradeoff between localization and standardization is further complicated because retailers typically pursue global expansion in order to leverage the strengths of their core business at home. However, simply bringing the best of their world to a new world is not sufficient. Retailers require a strategy that reflects the pre-existing market structure and the needs of local consumers as well as the competitive advantages that the retailer can offer. The power of the retailer's domestic advantages, such as a more efficient supply chain or a unique brand, can be overestimated, while the extent to which retailers will need to adapt to the local market is underestimated.

There is no perfect entry strategy

In addition to the degree of localization required to succeed in a given market, retailers need to decide what method of market entry will allow them to best adapt to local market conditions. In fact, the two issues are intertwined: the more different the market, the greater the need for adaptation, the greater the risk, the less likely retailers are to go it alone.

There are five primary routes for retailers to enter a foreign market: wholesale distribution, licensing, franchising, joint venture, and owned expansion (greenfield and/or acquisition). A set of parameters –ranging from the required level of investment and time to payback to internal capabilities, knowledge of the market, ensuring brand integrity and human resource requirement – drives the selection of entry method. Essentially, the choices represent a tradeoff between speed and control, risk and reward. Therefore, the selection of ownership model for entering and operating in a new market requires a careful assessment of the operational, organizational, and financial impact of each option.

Foreign retailers can enter a market as a ***wholesale distributor***, supplying products to local retailers and institutional customers such as hotels and restaurants or other businesses for resale or use.

Some foreign retailers choose to distribute their branded products to consumers through a ***strategic licensing agreement*** with a domestic retailer. This gives the domestic company the right to sell the brand through its own stores, enter into shop-in-shop arrangements with other retailers, or distribute the brand to its franchisees.

Many retailers prefer ***franchising*** rather than licensing to expand quickly and to better maintain the integrity of the brand by imposing strict guidelines on how the product is merchandised and marketed. Franchising allows for great potential variation in the level of control that the retailer has over the entire business concept and method of doing business, relinquishing primarily the front-end competence in the marketplace to the local operator.

To retain even more control, retailers may opt to enter into a ***joint venture*** agreement with a domestic player. Compared with a wholly owned venture, combining capabilities and resources with a partner can reduce time to market. Other benefits include the opportunity to learn from the joint venture partner and share the risk. As with franchising, choosing the right partner – ideally one with complementary resources, skills and assets – is critical. Different cultures and management styles can sometimes result in poor integration and cooperation.

Owned expansion provides the most control, though it is usually the most time-consuming way to enter a foreign market. Although this mode of entry can be the most lucrative, it can also be the most risky given the size of the investment required and the cultural, political, economic, legal, regulatory and labor considerations, not to mention the financial implications of going it alone. As a result, owned expansion is sometimes used as the second phase of a company's market entry strategy once the overall market risk has been determined.

Successful global retailers have entered different markets in different ways. Some retailers use multiple methods even within the same country in an effort to cater to individual geographic areas and optimize the local opportunity. There is no one rule of thumb. The right choice depends on many factors, not the least of which is the company's risk profile.

Market potential vs. ease of expansion tradeoff

When contemplating a new market entry, retailers also face a tradeoff between market potential and ease of expansion. Retailers naturally are attracted to developing markets, such as the BRIC countries, based on their sheer size and economic growth, along with a significant relaxation of restrictions on investment. In addition to a burgeoning middle class, these markets boast lower retail saturation levels, increasing urbanization, growth of retail space, and greater Internet penetration – all leading to increasing retail sales per capita.

Despite the potential of emerging markets, retailers may miscalculate their own individual market prospects by focusing too much on macroeconomic factors while underestimating the operational difficulties of doing business in these markets. In order to assess a market's overall attractiveness, market potential must be balanced against possible pitfalls. This requires careful assessment of a market's cultural, political and regulatory environments and their implications for strategy, risk management and ROI. Key considerations should include real estate, tax policies, security and privacy standards, and labor laws.

Real estate: The age-old retail adage, "location, location, location" is as important in Mumbai, São Paulo or Beijing (not to mention second and third tier cities) as it is in Paris, London or New York. As retailers expand their global footprint, the ability to secure strategically important retail locations at reasonable prices is critical.

The impact of globalization on retail real estate has driven prices up and made prime locations harder to find. Although the emergent middle class in developing markets, with their pent up demand, has boosted retail real estate activity, there still is inadequate local capacity in many markets. As a result, there has been a rapid increase in prices. On the other hand, continuing economic challenges in the United States and other developed countries have created opportunities for foreign retailers to enter mature markets and find great locations in malls or other shopping areas that were unavailable or unaffordable prior to the downturn.

Tax policies: From a tax perspective, globalization – especially if it involves mergers, acquisitions, partnerships or joint ventures with other companies – creates complexity. New markets can impose tax regulations that could impair a retailer's ability to take advantage of business opportunities. Therefore, companies should be aware of and prepare for the tax and legal environments in the new jurisdictions that they serve in order to sustain their growth. Failure to do so could result in fines, penalties or delays in getting goods to customers.

As rents climb in emerging markets, the question of leasing versus buying is being raised. Generally, retailers entering a foreign market focus on the core business and do not tie up their capital in real estate that could be more productively used elsewhere in the business. Buying real estate can be a risky bet if the retailer lacks strong knowledge of the local market.

However, landlords are becoming more sophisticated, making it more difficult for foreign retailers to get especially favorable leasing terms. In some markets, developers have become more reluctant to sign long leases with hypermarket and other big-box operators, preferring instead smaller boutique and high-end stores that add to the "brand cachet" of their properties. As desirable retail real estate becomes increasingly limited and expensive, foreign retailers are reconsidering the strategy of leasing. So far, the plan to develop and own retail space has been limited to a few big-box retailers, whose slim profit margins and large-scale land requirements make them particularly rent-sensitive. For example, in 2010, Wal-Mart and IKEA began for the first time to buy land in China to develop some of their stores.

Performing tax-related due diligence enables maximum efficiency from an operational and ROI perspective and may reveal unforeseen tax costs. Efficient tax structuring and planning can be designed to create more flexible structures that allow a retailer's business to grow and be modified, minimizing unnecessary tax expenditures; automate tax compliance and reporting processes; and analyze different supply chain and selling structures to maximize direct and indirect tax efficiency.

Security and privacy: While the Organization for Economic Co-operation and Development (OECD) developed its Guidelines on the Protection of Privacy and Trans-border Flows of Personal Data as far back as 1980, many countries still have no data protection rules at all. Where legislation does exist, it's typically a hodge-podge of different approaches. Even where common standards have been developed, as in the EU, they are often complex and inflexible.

In an era of increasing globalization, the lack of global privacy standards has two potentially damaging consequences. First, it results in the loss of effective privacy protections for individuals. How can consumers be certain their data is safe, wherever it might be located? For retailers at home and abroad, the unlawful or unethical collection, storage and management of customers' personal information can destroy consumer trust.

Second, it creates uncertainty for business, which can restrict economic activity. How does a company, especially one with global operations, know what standards of data protection to apply in all the different markets where it operates? Privacy rules – no matter how well designed – that differ from one country to another require companies to treat customer data differently, which can become not only burdensome, but costly.

Labor laws: Employment systems and work habits differ from country to country. Although labor laws in emerging markets, like restrictions on working hours or use of part-time labor, are being modified and liberalized to suit a more modern retailing context, they still can act as constraints on business and should, therefore, be a consideration in market selection. Global retailers' labor practices must be malleable and respond to local labor laws and institutions, including restrictions on hiring and dismissals, working conditions, dispute resolution, collective bargaining and social security systems. Key issues to be addressed include work organization, skill development, staffing arrangements and remuneration systems.

First steps: Familiarity breeds comfort

As these issues demonstrate, market attractiveness depends on much more than size and growth. Taking "baby steps" into a similar market, especially one close to home, is a lower cost, risk averse strategy. For retailers inexperienced in international expansion, ease of market entry may be reasonable tradeoff for market potential – at least until they get their feet wet – because it reduces uncertainty. Even Wal-Mart moved first into Mexico, followed by Canada.

In addition to market proximity, ease of entry is facilitated by cultural and demographical similarities – including such things as language, consumer shopping habits and preferences, and family size and structure – as well as a similar competitive set. Tactical similarities also make doing business easier than in other, more "foreign" countries – for example, a similar regulatory environment and labor practices. In some cases, there are historic ties between countries, such as Germany and Austria or the United States and Puerto Rico, that pave the way.

Close geographic proximity provides specific benefits. Physical proximity supports supply chain and distribution efficiencies and also makes it easier to use a single regional infrastructure (e.g., headquarters and administrative operations). Brand equity often seeps across common borders based on shared media outlets and cross-border shopping. A successful track record tends to reinforce this approach to international expansion. Many U.S. retailers, for example, have successfully made their first international foray into the Canadian market.

Hedging bets – online retailing

Internet retailing is the fastest growing retail channel – globally and on a national or regional basis. It has emerged from the recession stronger than ever, boosted by an increase in the number of Internet connections, increased use of credit cards, and a large and growing population of consumers that spend considerable time online and are comfortable with e-commerce. For these reasons, some retailers view online retailing as the best way to connect with international customers for the first time.

Online retailers benefit from the ability to interact with consumers and learn about their specific needs and wants, sometimes as a precursor to eventual brick-and-mortar retailing. This allows them to build customer relationships and assess the market opportunity without first incurring the expense of creating a physical presence in the market. It also provides greater flexibility for retailers to adjust the offering to various customer groups. An online-only presence in foreign markets allows retailers to efficiently manage supply chain activities like order processing, inventory handling, delivery, and promotion. In other words, for some retailers, investment risk, brand exposure, and operational challenges can be mitigated through international online retailing.

However, challenges still exist. Despite rapid growth, personal computer and Internet access are still limiting factors to wider adoption in developing markets. Product delivery and transaction system infrastructure deficiencies also temper wider use of online retailing. Even in markets where the infrastructure is well-developed, like Canada, it can be difficult for e-retailers to keep their "timeless delivery promise" due to the very long distances.

The human resource challenge

Retailing is one of the largest sources of employment in most countries. However, the supply of trained employees with an understanding of the retail business is often inadequate compared to the needs of organized retailing –especially in emerging markets. Meeting the talent requirements of an international company also demands greater attention to management staffing needs by recruiting and retaining people who are willing to travel extensively or serve as expatriates. For these reasons, finding and retaining good people is one of the biggest headaches faced by global retailers – at both the corporate and local levels.

In general, HR initiatives become increasingly complex and can have a greater impact on the organization's top-line growth and bottom-line profitability as companies move outside their traditional geographic markets.

At home or abroad, an organization's reputation or "brand strength" is critical for the recruitment and retention of customers and employees alike. People want to work for companies that are growing, that provide opportunities for advancement, and that are good corporate citizens in the communities in which they operate. But the war for talent in high-growth markets is escalating. Without employee trust and loyalty, large multinational retailers risk becoming training grounds for a developing country's retail management.

Retailers should aim for local management in foreign markets. Companies that hire mostly local talent will improve their chances of long-term success. Local operators have knowledge of local consumers and culture that expats don't have. They are often well-connected in the local business community and have contacts with government authorities. And they can navigate local ways of working. In addition, they typically foster greater loyalty within the organization than do foreign managers. Foreign retailers must make a commitment to local talent development if they hope to outperform local competitors.

While excessive reliance on expatriates is discouraged, in the early stages of expansion, expats, who understand company culture and processes, are needed to manage entry into new markets and ensure compliance with the company's core values and principles. Proper rotation of expat managers is also important to keep them from becoming desensitized to unacceptable conduct.

Developing the organizational and governance structure

Enterprise governance is the last topic for discussion here, but it should be considered early on by retailers planning an international expansion strategy.
For retailers operating across geographies, it's not only where you operate, it's how you operate. The governance structure, starting with the selection of home office location, has important implications for the organization's overall cost structure, processes and controls, knowledge management activities, taxation and financial reporting requirements. The key is finding the right balance between centralization and localization to support the retailer's expansion strategy, including the eventual size of the international business, the character and mix of markets to be entered, and the local ownership models to be employed. The governance structure, therefore, must be dynamic, evolving to support the retailer's expansion over time.

Determining which functions will be performed at what level of the organization in each country or region will depend on the strategic importance of each market and the capabilities of the local resources. It should also take into account the need to balance a strong organizational culture with local cultural differences and create a sense of community across the organization. The strength of an organizational culture depends on a uniform and universal set of core values that are shared throughout the organization. This is important because a strong culture tends to enhance employee commitment and loyalty toward the organization.

A strategic assessment of centralized versus localized support activities requires balancing the cost structure with the need for localized autonomy and decision-making. This will lead the organization to select from a spectrum of local presence options (for example, shared services, core local services, etc.). The need for global versus local talent will also depend on the nature of the business. Food retailing, for example, is inherently local, while designer apparel can be managed across borders. Ultimately, successful global expansion requires building scale, and the delegation of decision-making and accountability needs to reflect that.

Tax implications: Global expansion is driven by business and operational objectives; however, the home country and local country tax treatment of those operations must be considered to avoid inefficiencies and additional charges. Retailers must consider the tax impact on all aspects of a company's operating model and the associated value chain. This includes design, procurement, manufacturing, development of relevant intellectual property, and selling channels.

Proper supply chain planning can use arm's length transfer pricing guidelines, applied to a center-led business model (i.e., the Principal Operating Company ("POC")), as well as customs and other indirect tax planning, to embed tax efficiencies into a company's operating model. The result is a business with an organically low effective tax rate. However, it is critical that the substance of the decision-making actually take place in the location of the POC.

Several different operating models lend themselves to the retail industry--franchise, joint venture (JV), and corporate-owned. The franchise model can be very lucrative as it is all margin; but there is less opportunity for U.S. tax deferral as compared with the other two models. The JV or the corporate operating models can be employed with similar benefits, with preference depending on desire for control at the ownership level.

Even the determination of the geographic location of the headquarters can be tax driven. Many cities will offer tax incentives to attract companies to bring their headquarters, employees, and income to that region.

Financial reporting implications: Global expansion requires reconciliation of different accounting policies (local GAAP, U.S. GAAP, IFRS). For example, inventory costing and lease accounting may be recorded differently across standards.

However, convergence of accounting standards is gaining momentum. Reporting under IFRS will be allowed or required for most public companies in the United States and around the globe within the next few years. Many international retailers have already adopted IFRS. Some of the benefits that have been derived from this shift include increased transparency and consistency of financial information, more efficient use and availability of global resources, streamlined internal controls, additional access to capital, simplified cross-border M&A transactions, and opportunities for improved cash management and income tax planning.

The potential benefits of transitioning a multinational organization to a single set of accounting standards do not come without a cost, however. Conversion to IFRS will require a significant commitment of specialized resources in order to properly analyze and plan implementation. Companies must assess and create policies with a global understanding of the processes and goals of the entire organization, train the appropriate people in the organization (often across cultural and language barriers), and implement appropriate information systems and operational processes.

The time to act is now

The issues presented here highlight two realities of retail globalization: First, it requires a substantial investment of time, money and resources. And second, getting it right is not easy. As retailers raise their exposure in global markets, they will need strong risk management skills to navigate the maze. The cost of managing these risks will complicate the achievement of profitable growth.

That said, as mature economies stagnate, global expansion is becoming crucial to long-term growth for more and more retailers. Old markets have become saturated, and new ones must be found. But attractive markets are becoming increasingly crowded. Many of the world's biggest retailers have already set up shop, and they are determined to defend and fortify their positions. Competition from domestic retailers is intense. Despite the many inherent problems and risks, postponing an international growth strategy is no longer a viable option. The bottom line is that the easy growth is over, and there is no going back. The time to act is now.

Many of the world's biggest retailers have already set up shop, and they are determined to defend and fortify their positions.

Retail Globalization case studies

As a leader in the retail industry, Deloitte marshals the local experience of practitioners at member firms around the globe and takes a multi-disciplinary approach to help numerous retailers on their successful globalization journeys – whether they are just planning it or have already started.

Case study 1: Global fashion jewelry and accessories retailer

The Deloitte member firm in the U.S. helped a privately held fashion retailer develop its long-term international expansion strategy and create a corresponding operating model for its franchise business. The retailer lacked a sustainable franchise operating model to support current operations and future growth.

Deloitte was also engaged to assist in defining the retailer's global operating model as well as the design and implementation of a pan-European organization to support its expansion plans.

Activities

- Reviewed current methods of entry, benchmarked leading specialty retailers' practices – including operating and merchandising models, and made recommendations by market.
- Developed a franchise operating model which included organizational structure, roles and responsibilities for all customer facing functions, a deep-dive assessment on required supply chain changes, and a review of IT implications.
- Identified and prioritized markets to enter.
- Identified and vetted potential franchise partners.
- Modeled pro-forma financial benefits.

Benefits

- Identified opportunities to add +$150M in EBITDA over 10 years.
- Defined road map detailing which markets to enter and when to enter them.
- Developed crisper operating model with clear integration points between North America and Europe.

Case study 2: Canadian restaurant chain

Deloitte Canada was engaged by a major international quick service restaurant chain to assist with strategic planning related to its international expansion plans. The client required Deloitte's assistance with the identification of high priority countries for entry, including the development of business cases and preliminary market entry plans for each key identified market.

Activities

- Assessed the company's internal readiness and capability for international expansion across functional areas.
- Assessed the brand implications for internationalization.
- Reviewed competitors' experience with international expansions.
- Facilitated a global market entry analysis and filtering process to identify three priority markets with the highest potential for success based on pre-defined criteria.
- Developed a business case for international expansion, including the preparation of a detailed five-year financial model outlining the required investments and profit potential from entry into each of the short-listed markets across a variety of assumptions and scenarios.

Benefits

The core project team worked closely with Deloitte member firm industry specialists in each of the top six most attractive markets to prepare detailed country profile and market entry assessment reports to assist with reviewing the candidate markets for entry.

Case study 3: North American fashion retailer

The Deloitte member firm in the U.S. assisted a fashion retailer in assessing the Chinese market and size of the opportunity, expansion options, and in the development of a market expansion strategy.

Activities

- Sizing the market opportunity, in aggregate and by city.
- Understanding market characteristics.
- Determining scope and pace of expansion by city
- Selecting method(s) of entry/expansion and partners.
- The team developed market intelligence through on-the-ground primary data collection and secondary research.
- Analysis of Deloitte proprietary data (e.g., Deloitte's Survey of Chinese Consumers) and extensive secondary research.
- Interviews with industry association leaders, industry analysts, and former executives of competitors' China businesses.
- U.S. and China store scans of competitor pricing and assortment.
- City visits to tour shopping center locations and store formats.

Benefits

- An assessment of the China opportunity size and market landscape (encompassing consumers, competitors, real estate, regulations).
- Recommendations on methods of entry and partner selection considerations.
- Prioritization of top cities for entry, including estimated store count by city, pacing/trajectory of expansion, and projected revenue.

Case study 4: European denim brand

The client was evaluating an acquisition of a mid-level jean brand in Europe. As part of its potential post-acquisition growth plan and exit strategy, it wanted to assess the potential retail opportunities for the brand in China. Specifically, it wanted to understand how to enter the Chinese jeans market, how to distribute product, the retail potential/consumer spend, and forecast potential margins of a build-out strategy.

Activities

- Reviewed China jeans' market size and potential growth, customer demographic and competitive environment.
- Assessed the market opportunities in first and second tier cities. Profiled key competitors' China business model, distribution model and geographic coverage strategy.
- Conducted a survey of 1,080 participants to understand current and future category spend patterns.
- Offered client's China entry strategy suggestions and evaluated its EBITDA in China in next five years.

Benefits

- Designed China entry plan and business model, including plans developing business in tier 1, 2, and 3 cities in five years based on competitor benchmarks.
- Provided Revenue and EBITDA projections.

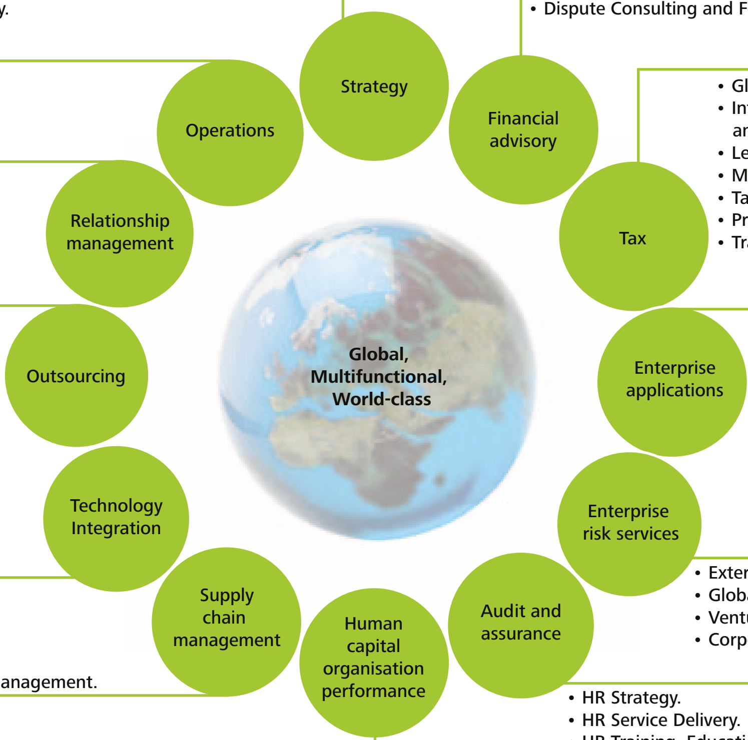
Deloitte's Global Retail Expansion capabilities

Regardless of where you are in your global expansion journey, Deloitte is well-positioned to assist with any issues. Deloitte has a demonstrated track record of delivering "executable strategy" with experience ranging from deal and market evaluation to development of a multi-year expansion strategy.

The Deloitte difference	
A focus on executable strategy	• Known for developing strategies that turn into results. • A pragmatic approach built with an eye on implementation. • We accompany our clients all the way through implementation.
A global presence	• Deloitte member firms are present in more than 150 countries. • We have helped leading retailers and consumer businesses scale their operations globally.
Enterprise-wide, multi-disciplinary competencies	• Have the depth and breadth of experience to cover the many functions of a retailer. • We manage multi-disciplinary engagements across the globe with confidence. • We add value with a unique blend of tax and risk skills.
Extensive multi-channel, multi-brand retail expertise	• Deep experience in merchandising, marketing and store operations. • We have managed complex, global, strategic engagements for multi-branded, multichannel retailers.

Deloitte's Integrated Global Retail Expansion offerings

Deloitte is uniquely positioned to assist retailers across the multiple functions required for expansion into new markets:



- Business/Management Strategy.
- Brand management and strategy.
- CFO and CMO Services.
- Corporate and Competitive Strategy.
- Customer and Market Strategy.

- Store Operations.
- Back-Office Support.
- Process re-engineering.
- Store 3.0.

- Contact Center.
- Service Effectiveness.
- Market Effectiveness.
- Channel Management.
- Sales Effectiveness.
- Customer Experience/Service.

- Business Process Outsourcing.
- Application Management.
- Outsourcing Advisory Services.

- System Integration.
- IT Strategy.
- Information Management.
- Architecture and Infrastructure.
- Enterprise Business Integration.
- Technology Advisory.
- Global Service Offering.

- Supply Chain Strategy.
- Lean Operations.
- Logistics and Distribution.
- Sourcing and Procurement.
- Product Innovation and Lifecycle Management.

- Corporate Finance.
- Transaction Services.
- Reorganization Services Valuation.
- Dispute Consulting and Forensic Analytics.

- Global Employment Services.
- International Tax expansion and divestiture.
- Lead Tax Services.
- M&A.
- Tax Management Advisory Services.
- Private Client Advisors.
- Transfer Pricing.

- Enterprise Software Package Solutions
- SAP
- Oracle

- Capital Market Services.
- Regulatory Consulting Services.
- Internal Audit.
- Security and Privacy Services.
- Control Assurance.

- External Audit Services.
- Global Offering Services.
- Venture Capital Related Services.
- Corporate Governance Services.

- HR Strategy.
- HR Service Delivery.
- HR Training, Education and Learning.
- HR BPO Advisory, Technology.
- HR Organization and Design.

Representative methodology and tools

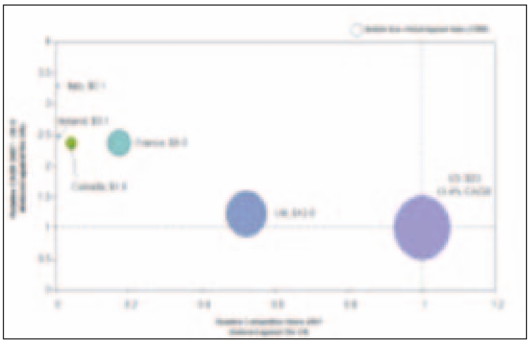
Deloitte's methodology and approach can address the broad range of operational considerations and complexities that retailers may face in their global efforts, from strategy to execution.

Growth strategy	Operational strategy	Implementation
Develop a cohesive and executable long-term international strategy • Expansion strategy. • Market strategy. • Financial and operating targets.	**Define the global operating model** • Customer-facing functions. • Back office functions. • Key enablers.	**Detail the steps, resources, and investments required to realize goals and targets** • Overall implementation roadmap. • Market-specific action plan. • Tax, audit, and compliance.

Our tools include:

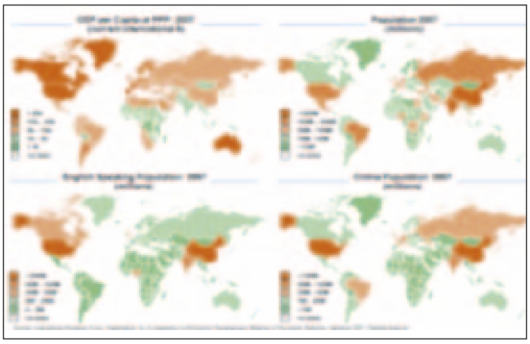
Market sizing graphs to identify the most promising geographies for future growth across several key dimensions.

Online apparel market size and targeted countries



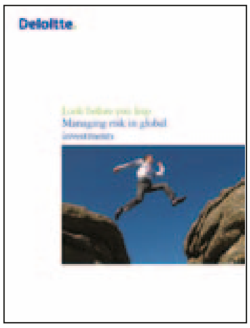
Global assessment to measure key growth and opportunity metrics tailored to the business's target customers.

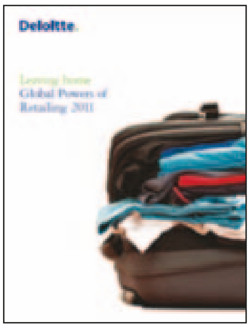
Global assessment of key metrics

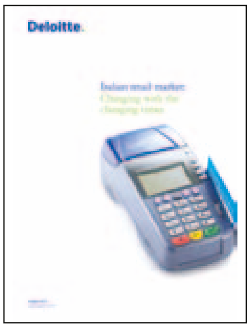


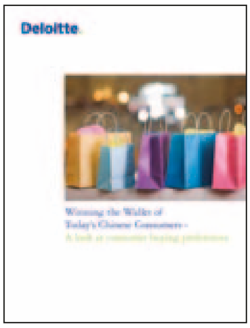
Deloitte’s eminence and perspectives on Global Retail Expansion

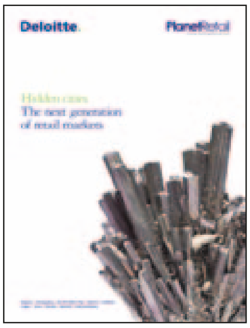
Professionals at Deloitte member firms around the world gather and organize the knowledge and experience of engagement teams that have worked with retail companies engaged in global expansion. In the spirit of knowledge sharing, Deloitte continues to develop provocative and relevant publications that address the issues that matter most to retail executives. A sampling of our eminence includes the following:

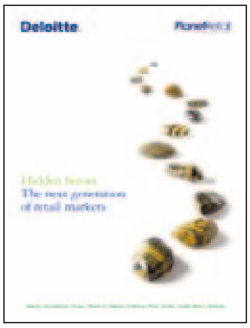












The Deloitte member firm network

With a strong network operating in countries throughout the Americas, Europe, and Asia Pacific, Deloitte’s Consumer Business specialists combine deep industry experience and understanding of regional markets to help companies around the world succeed wherever they operate.

Deloitte member firms serve 79% (or 75 companies) of the 95 Fortune Global 500® CB companies, including:

- 17 of the top 20 retail companies.

- All of the wholesale and distribution companies.

Clients in the retail industry include:

- Alliance Boots
- Delhaize Le Lion
- El Corte Ingles
- Fonciere Euris/Casino
- Groupe Jean Coutu
- Grupo Gigante
- Home Depot
- Inditex
- Jeronimo Martins
- Metro
- PPR
- Sainsbury
- Sears Holdings Corporation
- Soriana
- TJX Companies
- Wolseley
- Woolworths Ltd.

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