A.T. KEARNEY

Growth Opportunities For Global Retailers

The A.T. Kearney 2007 Global Retail Development Index™

Global retail is experiencing an explosive modernization as investment rushes into developing markets. From small proprietors with a mainly local focus, retail's ambitions now stretch worldwide, embracing the latest trends in marketing, distribution and supply. Modern retail grew between 25 and 30 percent in India and 13 percent in both China and Russia. As the wealthiest markets mature, more retailers are pursuing new growth opportunities. They are eyeing countries new to modern retailing, smaller cities (as larger cities become saturated), and customer segments hungry for specialty products. Retailers that can identify the most promising markets will become fierce global competitors—able to saturate the obvious markets and gain first-mover advantage in new ones.

Retailers understand these new realities. Modern retail has been expanding to new markets for a few years now. The trouble is, it is difficult to determine which new market is the most promising one. As one market becomes saturated, is it enough simply to follow the crowd into the next one?

With this in mind, A.T. Kearney developed the Global Retail Development Index™ (GRDI). Now in its sixth year, the GRDI identifies windows of opportunity to help retailers make strategic investments in exciting new markets. It ranks the top 30 emerging countries for retail development using 25 macroeconomic and retail-specific variables *(see sidebar: About the Global Retail Development Index on page 4)*. Figure 1 on page 2 highlights the 2007 findings.

India, Russia and China continue to top the Index. Retailers moved from talking about expansion plans to acting on them in top cities. Woolworth's, Wal-Mart, Supervalu, Euroset and Starbucks all have plans for entering India, joining a handful of single-brand retailers that are already there, including Lacoste, Chanel, Swatch and Omega. In China, the action spreads from tier-one to tier-two cities, where a proliferation of modern retail has begun. Wal-Mart, for example, opened a store in second-tier city Yuxi. This year's GRDI also indicates that several other countries, including United Arab Emirates (UAE) and Vietnam, are cracking open their windows of opportunity in meaningful ways.

Of course, there is more to entering a new market than knowing which cities are hot and

Figure 1

The 2007 Global Retail Development Index™

2007 rank	Country	Region	Country risk	Market attractiveness	Market saturation	Time pressure	GRDI score
		Weight	25%	25%	30%	20%	
1	India	Asia	67	42	80	74	92
2	Russia	Eastern Europe	62	52	53	90	89
3	China	Asia	75	46	46	84	86
4	Vietnam	Asia	57	34	76	59	74
5	Ukraine	Eastern Europe	41	43	44	88	69
6	Chile	Americas	80	51	42	43	69
7	Latvia	Eastern Europe	77	32	21	86	68
8	Malaysia	Asia	70	44	46	54	68
9	Mexico	Americas	83	58	33	33	64
10	Saudi Arabia	Mid. East/N. Africa	65	40	66	35	64
11	Tunisia	Mid. East/N. Africa	60	33	77	37	64
12	Bulgaria	Eastern Europe	62	32	42	68	63
13	Turkey	Mid. East/N. Africa	52	50	57	43	62
14	Egypt	Mid. East/N. Africa	43	37	85	35	61
15	Morocco	Mid. East/N. Africa	59	33	70	37	60
16	Thailand	Asia	71	39	30	55	59
17	Slovenia	Eastern Europe	100	33	13	47	58
18	United Arab Emirates	Mid. East/N. Africa	100	35	33	24	57
19	Croatia	Eastern Europe	73	38	10	70	56
20	Brazil	Americas	53	61	59	18	56
21	Uruguay	Americas	35	41	65	49	56
22	Peru	Americas	42	34	79	34	55
23	Philippines	Asia	41	46	63	37	54
24	Indonesia	Asia	36	40	70	37	52
25	Algeria	Mid. East/N. Africa	25	30	90	35	51
26	Hungary	Eastern Europe	96	36	2	46	51
27	Romania	Eastern Europe	60	31	22	66	50
28	Lithuania	Eastern Europe	75	33	17	54	50
29	Argentina	Americas	31	50	43	54	50
30	Colombia	Americas	44	50	52	26	47

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*

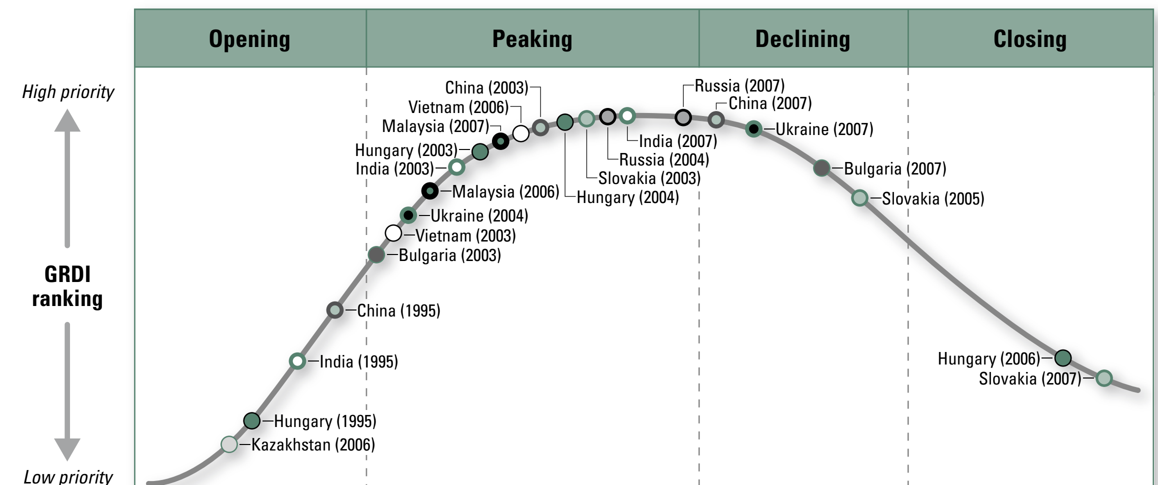
Sources: Euromoney, World Bank, Global Competitiveness Report 2005-2006, A.T. Kearney analysis which ones are not. Our findings further emphasize the importance of understanding the timing of market entry, particularly in terms of consumer readiness. The market might be ripe, but are consumers open to new ideas and willing to accept new products, formats and a "new way of shopping?" There are also significant challenges in entering second- and third-tier cities versus first-tier cities. Retailers soon learn that there's a world of difference between opening a store in Yuxi and opening one in Beijing.

Before we present the GRDI's detailed regional and country results, let's look at how the findings can help retailers identify promising markets. From our analysis, there are three factors that, taken together, can mean the difference between success and failure in a new market. They are: gauging the window of opportunity for entering key cities, understanding consumer readiness, and knowing when and how to move into second- and third-tier cities.

Gauging the Window of Opportunity

The "window of opportunity" measurement we introduced last year continues to be crucial this year. Countries typically progress through four stages—opening, peaking, declining and closing—as they evolve from emerging to mature markets, usually over the course of five to 10 years *(see figure 2)*.

Figure 2
Window of opportunity analysis



	Opening	Peaking	Declining	Closing
Action	Monitor market	Open local office (sourcing, research), test the market and learn	Expedite implementation	No pattern identified
Format of entry	Not applicable	Consider cash-and-carry or convenience formats apart from supermarket	Introduce discount and hypermarkets	Tailor formats to meet specific consumer needs at work
Labor strategy	Not required	Hire and send expatriate employees to location	Scale up operations, increase local hiring, participate in community	No pattern identified

Source: A.T. Kearney

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 Euromoney's country-risk score
- Population size: more than two million
- Wealth: GDP per capita more than $3,000 (GDP per capita 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 risk (25 percent)

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

Business risk (20 percent): terrorism, corruption, crime and violence. 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, pointing to 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): government effectiveness, burden of law and regulations, ease of doing business, infrastructure quality. Zero means the country has poor business efficiency, 100 indicates high efficiency.

Market saturation (30 percent)

Share of modern retailing (30 percent): Zero means the share of retail sales made through a modern distribution format is high and 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 stores (department stores, variety stores, U.S.-style warehouse clubs and supercenters).

Number of international retailers (30 percent): The 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 only include stores predominantly selling food (hypermarkets, supermarkets, discount stores, convenience stores).

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

Time pressure (20 percent)

The time factor is measured by the CAGR (2002 to 2006) of the modern retail sales weighted by the development of the economy in general (CAGR of the GDP and the consumer spending from 2002 to 2006) and the CAGR from 2002 to 2006 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 2005-2006, national statistics, Euromoney and World Bank reports, and Euromonitor and Planet Retail databases.

Generally, companies can use the window of opportunity as a time frame to plan their market entry strategies. Our analysis focuses on the opportunity as applied to grocery retailers, which are typically the bellwether for modern retailing as they serve the broadest consumer segment in a country. The analysis is also applicable to other segments, with some variations and exceptions; we address some of these issues in subsequent sections.

Countries in the opening stage last year have begun moving toward the peaking stage this year. A peaking market is one that is developing quickly and is ready for modern retail, but the advantage of establishing early dominance can be fleeting.

India's window of opportunity continues to be wide for retail investment and development, evident in the spate of alliances and market entry announcements from local conglomerates. Once India's window closes for grocery retailers, there will be little opportunity for market domination in the main cities.

Market saturation in China's and Russia's tier-one cities over the past few years means the window of opportunity is closing, while Vietnam and UAE still offer a few more years of opportunity in the main cities. Latvia remains a solid contender and will probably stay that way for another year or two, as will Saudi Arabia.

Understanding Consumer Readiness

While the window of opportunity concept is relevant as an overall guide, there are instances when consumers are ready to adopt modern retail independently of a market's current state. This is particularly true where there is a very high GDP per capita (Dubai) and in countries with a large population of upper-income earners (India and China). Luxury retailers are discussed in more detail in *How the Rich Are Won* on page 6.

For example, a segment of consumers in India eagerly shop at luxury retailers, as they have been exposed to these goods and have the wherewithal to make purchases. Luxury retailers have entered the country thanks to recently relaxed government regulations. Most observers believe that the government will continue to relax Foreign Direct Investment (FDI) rules in retail beyond single-brand retailers. Smart discounters and warehouse clubs are already planning their entry strategies.

What's interesting about this year's findings is the impact consumer readiness has on modern retail's growth and success. Retailers depend on consumers' willingness to accept modern retail formats and products—if not immediately, at least eventually. How does one determine if customers are ready for modern retail? The following may offer some guidance:

Young, working population with money. Modern retail is most welcome in markets with a large population of young, employed workers with disposable income, a propensity to spend, and a willingness to embrace new formats. These young professionals are "time poor" so will happily pay for speed, choice and convenience.

Older population ready to try something new. As younger consumers become acclimated to modern retail, their families are exposed to it and before long people of all ages begin to embrace its benefits. This is one reason why Russia's modern retail food sector is expected to grow from a 31 percent share of the overall Russian grocery market in 2006 to a 48 percent share by 2011. In contrast, the market share of traditional "Soviet-style" stores is expected to decrease from 21 to 11 percent during the same period.

Influence of Western cultures. In India, modern retail is just 2 to 3 percent of overall retail, but is growing at a remarkable 25 percent per year. The catalyst for this growth, or at least one catalyst, is the Westernization of the culture. Modern retail is taking off in large cities primarily because television shows, movies and Internet sites help shape daily life and offer a glimpse into modern retail's enticements—a vast selection of products (not available at mom-and-pop shops) and the ability to shop in air-conditioned comfort.

Knowing When and How to Move Beyond Tier-One Cities

Knowing when to take modern retail to smaller, second-tier cities represents another important consideration. Retailers that have exhausted growth options in retail-saturated tier-one cities often find new opportunities in tier-two and -three cities. This is the case for most emerging markets and is especially pertinent for the GRDI's leading countries, Russia and China. Both countries have experienced extreme retail growth in their tier-one cities over the past five years. In China, where 75 percent of the middle market is expected to be in tier-two and -three cities by 2017, many retailers are now making their moves into Yuxi, Weifang, Nanchang, Wuhu and Yueyang, helped by FDI deregulation.

How the Rich Are Won

Leading retailers in the luxury goods sector are great examples of acting on the window of opportunity without waiting for consumer readiness. Many of them have entered emerging markets well before consumers were ready. Louis Vuitton opened its first store at the Palace Hotel in Beijing in 1992. Ferragamo entered two years later, while Armani and Hermes, a tad risk averse, didn't open in Beijing until 1998. These companies take a long-term view of their investments, knowing that brand building takes time. While profits are slow in the beginning, the investments will pay off eventually. And by the time the money starts rolling in, they are firmly ensconced in prime locations—occupying space, billboards and hearts.

Indeed, this year, with more than 500 brands and global sales exceeding $200 billion, most of the industry's growth is from emerging markets, especially China, India and Russia. Here the nouveau riche and a growing middle class have access to media, fashion trends, global travel and, of course, credit.

But market potential does not come without pitfalls. In addition to the constant battle with counterfeiters, luxury goods retailers must create synergies between "making" and "selling." Serving large markets such as China and India from regional manufacturing bases makes economic sense, but will it hinder brand integrity and authenticity over the long term? Will creating a tiered product offering and sub-brands to capture less-affluent consumers dilute the brand?

The entry of luxury goods retailers into emerging markets is different from that of the mass market retailers. That's because it carries a sense of a true "cultural exchange." Unlike Europe, where people suffered through wars and depressions, Asian luxury never went out of style and, in fact, inspires how the West defines luxury.

Entering the luxury goods market is not about "taking a new format to those who never experienced it," but rather reinterpreting luxury—respecting the local market definition of luxury and using it to exchange, refresh and evolve the concept of luxury. Smart mass-market retailers will build on the success of luxury retailers by creating "luxury corners" designed to attract these well-heeled patrons. It is a strategy that can be applied successfully to any category, from opulent bathroom fittings in do-it-yourself stores to gourmet foods in hypermarkets.

A retailer should not go into a second-tier city armed with a first-tier city strategy, however. This goes back to our earlier discussion about consumer readiness. Consumers in smaller cities have different needs and requirements. They earn less and so are not willing to pay as much for products and services. The overall strategy should be to customize products and services for these new markets. For example, when Unilever moved beyond Mumbai, it offered the same products but in smaller sizes and at a fraction of the cost.

Is there an advantage to establishing a presence in a major city first before moving into a second-tier city? Our findings suggest that the answer depends on the market and the format. There are definite demographic, economic and social factors that make a tier-one city a safer bet, especially in developing countries. But if the city is already saturated with format competitors (hypermarkets, for example) it may not make sense to move in and risk failure. For example, it may be entirely feasible for grocery retailers to leapfrog the tier-one cities, plan their China market entry strategy around Nanchang and establish regional dominance. Still, most grocery retailers prefer to build a strong brand in tier-one cities first because it makes it far easier to expand once established in this more hospitable terrain.

Then again, the benefits of entering a second-tier city should outweigh the risks. Inadequate infrastructure and lack of exposure to modern retailing may hinder success in tier-two cities. When the infrastructure develops, these smaller cities become attractive targets both for retailers that missed the window of opportunity in major cities and for established retailers looking for growth.

Another drawback to tier-two cities is talent. It is difficult enough to find talented, qualified people in the major cities, so imagine how hard it is to find good people in the smaller cities. Retailers have to be prepared to win the war for talent by tailoring their HR policies to local realities. For more about this, we developed the Retail Labor Index to analyze the labor markets of the leading countries in the GRDI. The highlights are on page 16.

> **Modern retail is taking off** because television shows, movies and Internet sites offer a glimpse into its enticements — **a vast selection of products and the ability to shop in air-conditioned comfort.**

Together, window of opportunity, consumer readiness and movement into second- and third-tier cities represent the future of modern retail. Let's turn now to an overview of this year's findings.

The 2007 GRDI Findings

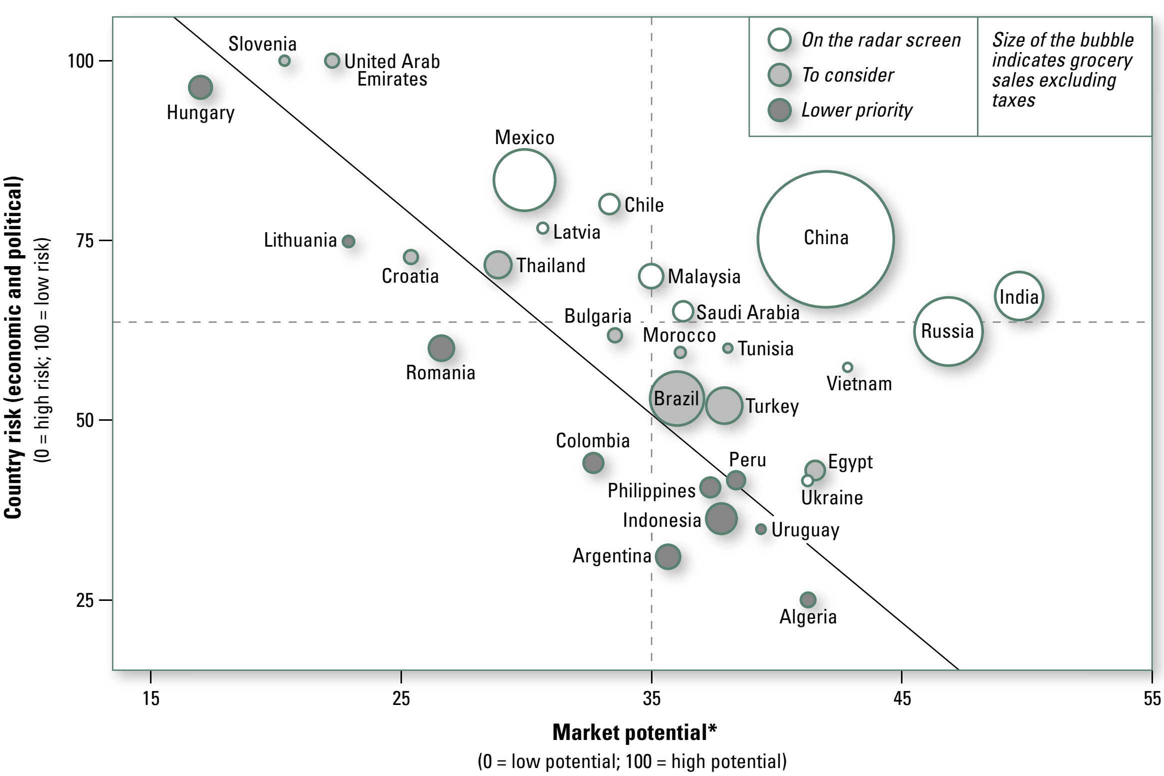
As predicted in last year's GRDI study, the 2007 Index reports impressive retail growth in Vietnam and India. Both had numerous new domestic and global entrants. Wal-Mart, Carrefour and Tesco established a presence in India. Competition in China intensified, further highlighting the urgency for retailers to formulate a "China strategy" to compete with domestic retailers that are more than willing to go head-to-head with foreign entrants *(see figure 3)*. There is a renewed interest in Latin America as more global retailers moved into Mexico, Brazil and Argentina *(see figure 4)*. Russia and Ukraine continue to present exciting opportunities, ranking among the top five countries. More-saturated retail markets, such as the Baltic region, Poland and Hungary, provide opportunities for a new wave of entries based on customized store formats such as discounting. The following offers a closer look at each region.

Asia Welcomes Modern Retail on Many Fronts

Asia continues to be hot. Its promise is coming to fruition as many countries in the region progress from cautious observers to rapid adopters of modern retail. India and China, with their huge populations and roaring economies, are clearly the prime destinations in the region. Smaller

Figure 3

GRDI 2007 country attractiveness



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

Source: A.T. Kearney

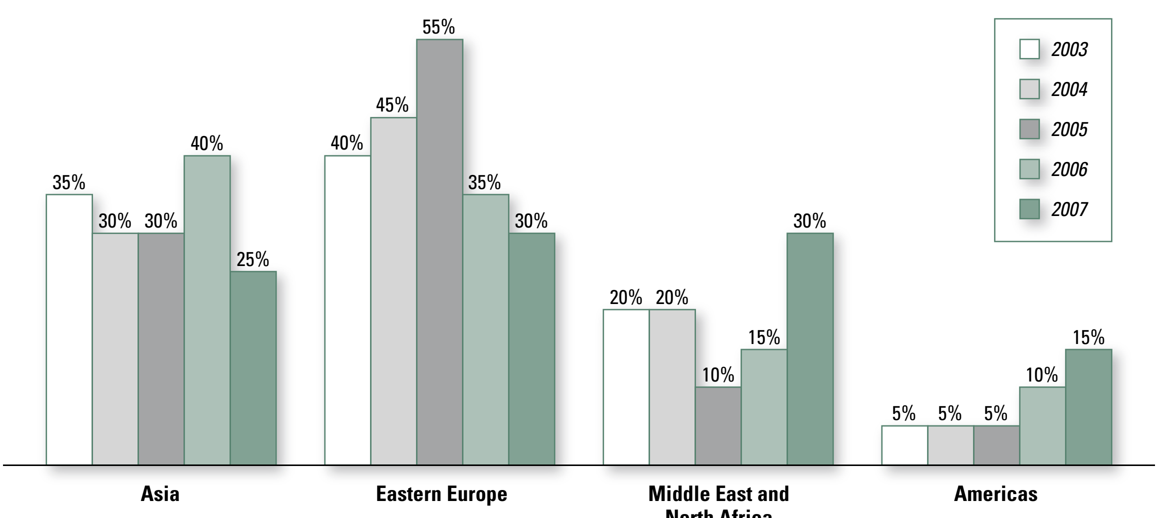
Asian countries—Vietnam, the Philippines and Malaysia—are attracting many global retailers as well.

India: talk turns to action. For the third year, India tops the Index as one of the most attractive countries for global retailers. India's GDP is projected to grow by 9 percent in fiscal year 2007—its highest growth rate in more than 18 years. Projections for 2008 are more than 10 percent, which will likely surpass China's projected rate of growth for the same period. Modern retail, accounting for 2 to 3 percent of the market, is expected to grow at a compound annual growth rate (CAGR) of 40 percent, from $8 billion to $22 billion, by 2010. Overall, India's retail sector is expected to grow from its current $350 billion to $427 billion by 2010 and $635 billion by 2015.

As talk of setting up shop in India turns to action, some retailers face their share of challenges as regulation continues to keep them largely at bay. Under India's current laws, which were somewhat relaxed in 2006, single-brand retailers can own a 51 percent majority stake in a joint venture with a local partner. But the relaxed rules do not extend to multibrand retailers such as Wal-Mart, Tesco and Carrefour, forcing these major companies to 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. Carrefour is engaged in talks with India-based Wadia Group and Britannia to negotiate an agreement that would establish its presence in the market. Essar Group has aggressive plans to open retail outlets in several cities. These industry giants are

Figure 4
Countries "on the radar screen" and "to consider" by region, 2003-2007



Source: A.T. Kearney

in a tight race for the retail leadership position in India.

Local hypermarket retailers are making their moves before the government further loosens foreign investment. Taking their cue from hypermarkets' success in China, local retailers such as Pantaloon Retail, Tata Group's Trent, RPG Group, K Raheja Corp. and Reliance Industries have all taken an early lead, with ambitious expansion plans in place. Meanwhile, Reliance Group and Birla Group have begun to lock up the upstream value chain (for example, farms, logistics and storage) eventually to compete against the likes of Wal-Mart.

> Who will win this retail pitting of wills in India? Will it be the indigenous retailers with their local knowledge or will global powerhouses learn to adapt and compete with their international expertise?

Who will win this retail pitting of wills? Will it be India's indigenous retailers, with their local knowledge, lobbying power and the financial resources to capture the market? Or will global powerhouses, such as Wal-Mart, learn to adapt and compete with their international expertise, Western allure and sophisticated supply chains? The answer will be revealed in the next few years, but regardless, the great Indian "retail gold rush," which we predicted last year, is now underway.

China: modern retail reaches smaller cities. China is a powerhouse that continues to defy its critics. Moving up from number 5 to number 3 in this year's Index, China's strong GDP growth helps maintain its status as one of the fastest-growing economies in the world. In 2006, Chinese GDP grew almost 11 percent and is estimated to grow another 10 percent in 2007. Although its GDP per capita remains low because of China's large population, consumer spending has more than doubled from the mid-1990s and continues to grow rapidly in the large southern and eastern cities.

The retail market grew by 13 percent last year and is expected to grow by 14 percent over the next four years and double by 2010. Fierce competition will likely force retailers to align to gain economies of scale. As is true of many emerging economies in Asia, China's retail sector remains fragmented. The top 100 retailers currently account for about 11 percent of the sector.

High-volume hypermarkets have enjoyed unparalleled success in this market. Wal-Mart, Carrefour and Tesco have all entered via China's tier-one cities. Saturation, however, has caused retailers to look to second- and third-tier cities. Carrefour, which enjoyed approximately 25 percent growth in China last year, will expand into medium and small cities, particularly in northeast and northwest China. Wal-Mart entered Yuxi, Weifang, Wuhu and Yueyang. Additionally, to catch up with Carrefour, Wal-Mart will buy

100 Trustmart stores to expand across 20 Chinese provinces. Thailand-based Lotus Supercenter has begun expansion into mid-sized cities, including Huai'an, Kunshan and Jiangmen.

Domestic retailers are scrambling to launch in second-tier cities or to consolidate their positions before global retailers arrive. Home World, a Chinese retailer operating 58 hypermarkets, has announced plans to increase its store count by 30 percent each year in tier-two cities. Gome and Suning, home-grown electronics retailers, have begun a massive store expansion and increased their presence to second-tier coastal cities.

Vietnam: soon to be barrier-free. Although Vietnam fell one place to number 4 on the 2007 Index, it remains very attractive as one of the fastest growing economies in Asia. This country joined the World Trade Organization (WTO) in 2006 and is proving a tempting target for global retailers. While the Asian bird flu epidemic slowed retail progress, Vietnam enjoys other advantages. The country's relatively large, youthful and highly literate population of 84 million is growing at a robust rate, with 94 percent of its citizens under the age of 65. The population is also shifting to city locations. Vietnam's urban population is expected to increase by 1 million per year for the next 20 years.

Vietnam's greatest barrier—government regulations blocking foreign retailers' entry—may soon cease to exist as entry into the WTO leads to deregulation. The government is expected to allow 100 percent FDI in retail within two to three years. This will put enormous pressure on thousands of mom-and-pop shops (particularly in Ho Chi Minh City and Hanoi) as larger retailers and supermarkets invade this highly fragmented market. Wal-Mart and Carrefour have already announced expansion plans into Vietnam. Casino, Parkson and Metro are in Vietnam, but each holds less than 3 percent of the market share. Meanwhile, domestic retailers are not standing idly by—many are willing to go head-to-head with foreign entrants. The biggest is Saigon Co-op, a state-owned superstore chain and current modern retail leader that operates 13 stores and plans to open more to stay ahead of the foreign competition. Global retailers should formulate their strategies now as Vietnam is peaking in its window of opportunity and may soon decline.

Other Asian markets flex their retail muscles. Malaysia continues to enjoy strong GDP growth (6 percent in 2006) and had a retail sales growth of approximately 8 percent annually from 2003 to 2006. These factors, along with rising personal income and urbanization, have attracted hypermarkets such as Carrefour and Tesco. Wal-Mart may enter Malaysia by acquiring the SHV Makro network. Thailand slipped four places to number 16 on the GRDI. Thailand's window of opportunity is closing as it becomes highly saturated and a pending new retail law will restrict large retailers' prices, operating hours and expansion.

Asian newcomers to the Index include the Philippines, where fiscal reforms and declining inflation have put it in the sights of Wal-Mart, Tesco and Carrefour. The top five current retailers, four of which are local, hold about a 40 percent market share, leaving room for new entrants if they act fast. Another Index newcomer, Indonesia, debuts with recent GDP growth of 5.4 percent—impressive considering its high inflation. A handful of global retailers have entered the market. Carrefour plans to open 10 more stores in Indonesia next year, domestic retailer Matahari plans to add two more hypermarkets to the dozen it opened in 2006, and minimarket chains Indomaret and Alfamart are preparing to open 400 new stores in the next year.

The Middle East and North Africa: A Hot Climate for Retail Growth

The market in the Middle East and North Africa is driven by robust retail expansion, strong GDP and consumers' penchant for a Western lifestyle. Some countries made significant advances in this year's rankings. In fact, this region holds 30 percent of the GRDI's top 20 countries—more than either Asia or the Americas.

United Arab Emirates experiences explosive retail investments. UAE, one of the most modern, sophisticated retail markets in the Middle East, is an extremely attractive market for retailers, led by the "retail Mecca," Dubai. The top five retailers account for 20 percent of the market. Upon completion in 2008, the 9-million-square-foot Dubai Mall will be the largest mall in the world, housing high-end retailers and everyday stores. Gap Inc. opened its first stores in Dubai in 2006 and is set to open 35 more Gap and Banana Republic stores by 2010. In 2006, Boots became the first major international pharmacy chain to open in Dubai. Major hypermarket companies Carrefour, Casino and Spinneys are in UAE, but the country's window of opportunity is still wide open.

With more than 600 supermarkets located in major UAE cities, largely run by small co-ops or private owners, we can expect to see some consolidation in the future.

Saudi Arabia's growth to remain strong. Saudi Arabia is another big mover on the Index this year, advancing seven places to be among the top 10. Its $347 billion economy saw 6 percent GDP growth in 2006 driven largely by high oil prices and exports. GDP growth is projected to slow to 4 percent in 2007 as oil prices and production drop, and will go even lower if political uncertainty continues.

Nonetheless, all forecasts point to strong retail growth in Saudi Arabia as domestic and foreign retailers consolidate through acquisitions, the population continues to grow, and tourism and tax-free status make Saudi Arabia a very attractive market. Hypermarkets are driving most of the retail sales growth. Carrefour plans to open 20 more hypermarkets over the next 10 years, and Casino plans to open 15 more stores over the next three years. Savola Group, a domestic player, is battling its French competitors for market share by opening 10 new hypermarkets by 2010.

Elsewhere in the Middle East and North Africa. Egypt climbed up the Index this year to number 14 as a result of 9 percent retail sales growth. While its mom-and-pop shops are disappearing, hypermarkets are going head-to-head, with Carrefour taking the lead. Domestic retailer El-Hawary is a mild competitor, with Spinneys Lebanon and supermarkets Metro and Shoprite offering further competition. Turkey remains attractive in part due to its recent market reforms and steady GDP growth of 6 percent in 2006. An increasingly urbanized and wealthy population fuels modern retail, where a relatively fragmented market helps create an excellent long-term investment opportunity. Morocco was the biggest mover on this year's Index, advancing 13 places to number 15, due largely to a strong GDP growth of almost 7 percent. Morocco's retail market is in its early stages, with just a handful of retailers, including Metro, Casino, Ahold and Auchan.

Latin America Moves Forward Confidently

Retail in Latin American countries has matured over the years, with opportunities now the ripest. But retailers will have to pay to play here, either through acquisition or by paying a premium for the most desirable locations. The competitive environment is more challenging as Latin American countries move past the crises of the past decade. But as political and economic stability gradually returns, these countries have healthier economies and more retail growth.

Mexico, where Wal-Mart has a lock. Mexico advanced an impressive 10 places to rank number 9 on this year's Index. Mexico's GDP grew roughly 5 percent, marking the country's third straight year of economic growth, but GDP is expected to slow to around 3 percent over the next two years. Modern retail is expected to expand from the large cities, where competition is fierce and markets are becoming saturated, into second-tier cities. Last year, Wal-Mart expanded aggressively in larger cities, moved into 30 new smaller cities, and is now sizing up 370 other cities for future expansion. This aggressive strategy positions it as the market leader not only in Mexico but also in Latin America. Wal-Mart's profits in Mexico are soaring and are expected to increase by more than 20 percent in 2007. Its dominance here makes it difficult for competitors to coexist. Carrefour, for example, sold its 29 hypermarket stores to Chedraui in 2005, deeming them nonstrategic or underperforming.

Brazil, on the rise again. Brazil once again climbed up the Index, rising seven places to rank number 20 this year. Its GDP growth was stable for 2006 at almost 3 percent and should rise slightly more in 2007. At the close of 2006, the Brazilian economy had grown to $711 billion, and a series of interest rate reductions last year helped to increase consumer demand this year. More disposable income has led to a rise in retail sales. Given the size of the Brazilian retail market, long-term retail investment remains attractive, although success is heavily tied to the economy. Over the past several years, global entrants such as Carrefour and Wal-Mart have chipped away at the stronghold national retailers have secured in Brazil. Although both retailers vie for the number-one spot currently held by homegrown leader Companhia Brasileira de Distribuição, there is still ample opportunity for new entrants.

> Success depends on targeting each country's window of opportunity and understanding how consumer readiness loosens wallets — it can mean the difference between a short-lived global expansion plan and healthy retail growth

Chile, an aggressive arena. Chile retains its number 6 position on the Index. Its GDP growth remained stable at 4 percent in 2006, but is estimated to increase by a percentage point or more through the next two years. Retail sales have increased steadily during the past few years, reaching 5 percent growth for 2006 according to estimates. 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.

While the outlook is optimistic, competing here is tough. Supermarkets and hypermarkets are Chilean retailers' main formats in a market dominated by national companies that have managed to drive out international retailers including Home Depot, Ahold, Sears, JCPenney and Carrefour. For global retailers willing to play hard, Chile remains an attractive but challenging investment opportunity.

Latin America's recent Index entries. Colombia ranks last (number 30) on the Index. Its GDP measured the country's highest growth rate in 29 years at almost 7 percent. Casino and Carrefour have captured market share in the country, but Colombia's retail market continues to be dominated by local companies. The top retailer, Almacenes Exito, bought a significant stake in the second largest retailer, Carulla, in late 2006. Uruguay made its debut on the Index this year, fueled by 5 percent GDP growth and a 15 percent rise in retail sales over the past few years. Unlike many of its neighbors, Uruguay has a significant middle class with reasonable purchasing power. Casino is the only major international retailer to enter the market so far. Peru makes its first GRDI appearance with 8 percent GDP growth (compared to roughly 6 percent the year earlier) and retail sales growth of 15 percent over the past six years. The Peruvian retail sector is in the early stages, which might be why so few global retailers have entered. Ahold and Falabella are the only major international retailers in this market. Argentina now enjoys a reviving economy following a recession. Since 2003, Argentina's economy has grown between 8 and 9 percent annually. With the highest per capita income in the region, Argentines prefer discounters and convenience stores to hypermarkets. Global retailers will have to adapt to this environment.

Eastern and Central Europe: Opportunity Awaits

Nine of the 12 Eastern European countries on last year's top 30 Index retained a presence on the 2007 Index. Bulgaria was Eastern Europe's star, advancing nine places to number 12. This region as a whole remains attractive, but the window of opportunity for large-scale supermarket and convenience stores will likely close in the next year or two. The time is potentially ripe for retailers to enter Eastern European markets in categories such as do-it-yourself, consumer electronics and apparel. As we predicted last year, specific formats targeted at niche segments might be available. Multilevel fashion malls and mixed-use centers, which are cropping up throughout Eastern Europe, are expected to be successful. In Warsaw, Złote Tarasy, a 2.4-million-square-foot mixed-use center, will provide space for more than 220 retail stores, including Zara, H&M, Mac and The Body Shop. In Moscow, an even larger mixed-use center, Slava, will be completed by 2010.

Russia's robust retail reaches second-tier cities. Russia remains strong and retains the number 2 position on the Index, which it has held for the past two years. Its $740 billion economy is booming, as is its retail sector. Consumer spending has risen rapidly for the past few years, fueled by an income growth rate of 10 percent last year and 11 percent the year before. More spending by Russian consumers translated into an overall retail sales growth rate of 13 percent last year. Showing no signs of slowing down, retail sales could grow by at least 10 percent in 2007.

Within Russia, Moscow and St. Petersburg account for the lion's share of this spending and retail growth. Ralph Lauren and Debenhams will set up shop in Moscow in 2007, while Starbucks plans to open locations in both cities. As market saturation in tier-one cities increases, some domestic retailers have successfully branched out into second-tier locales. Kazan, Yekaterinburg, Samara, Nizhny Novgorod, Perm, Voronezh, Chelyabinsk and Novosibirsk all have healthy retail investment, with domestic retailers leading the way. Russia's X5 Retail Group has nearly doubled its presence in Yekaterinburg with its Pyaterochka discount store chain, and Paterson invested approximately $35 million to expand its supermarket chain into Tolyatti, Samara, Chelyabinsk, Ufa and Kazan.

A retailer should not go into a second-tier city armed with a first-tier strategy. Consumers in smaller cities have different needs and requirements.

In a move that reflects our concept of consumer readiness, Carrefour entered the Russian market this year via tier-two cities, skipping the saturated major cities after noting domestic movement away from them. Other international retailers are expanding into second-tier cities: Ikea opened a shopping center in Kazan last year and announced plans to expand into Russian cities with populations of more than 1 million people in the coming years. The British do-it-yourself chain Kingfisher opened its first store in Samara.

Ukraine moving from food to other retail. Ukraine continues to be an attractive Eastern European retail market, although it slipped from number 4 to 5 on this year's Index. Estimated at $24.5 billion, the Ukrainian retail market grew by more than 25 percent in 2006. Its retail-sales growth rate, spurred by higher personal income, has exceeded GDP growth for the past several years. Although this record retail-sales growth may not be sustainable, Ukraine's GDP is expected to continue expanding at a healthy clip over the next few years, driven primarily by an underdeveloped organized retail sector.

A majority of the Ukrainian retail market is still composed of family-owned mom-and-pop shops, but many Ukrainians are beginning to prefer shopping in malls and supermarkets. Food retail accounts for almost half of the entire retail market, and, given the highly fragmented food retail market, there are plenty of opportunities for foreign investment. Domestic competition, meanwhile, is heating up. Ukrainian food retailer Furshet, for example, hopes to beat out foreign entrants by nearly doubling its number of supermarkets.

International retailers began to enter Ukraine in the early 2000s. Rewe, Spar and Metro were some of the pioneers. Metro appears to have outpaced the others, expanding aggressively by opening 13 stores in the past three years. Its success demonstrates how lucrative the Ukrainian market can be. Auchan and IKEA are both actively looking for retail space. Italy's King Cross, which builds and operates large shopping centers, is constructing a massive entertainment and shopping center in Lviv, set to open in 2008. The company is already planning to expand into other Ukrainian cities.

Baltic states are crowded. The retail markets in the Baltic states of Estonia, Latvia and Lithuania are becoming highly saturated. Estonia has fallen out of the GRDI top 30, while Lithuania is barely hanging on at number 28. Latvia, on the other hand, remains at number 7, powered by its impressive GDP growth of 12 percent. Latvia is expected to maintain a sure and steady pace over the next two years.

Central Europe: EU membership sparks new interest. Of the five Central European countries on the Index, four—Romania, Hungary, Slovenia and Croatia—slid down the rankings this year. Nevertheless, these markets are still attractive and provide targeted opportunities.

Romania's accession into the EU in 2007, along with solid GDP growth, sparked retailers' renewed investment interest. The country's hypermarket sector is predicted to boom. However, because many of the global retailers already have a stronghold in this market, the window of opportunity will close quickly. Carrefour, Kaufland, Louis Delhaize and Metro have all begun to expand into Romania while Auchan and SPAR opened their first stores in 2006.

Hungary, Croatia and Slovenia, with solid GDP growth rates ranging between 4 and 5 percent and high consumer spending levels, remain viable markets as well. Wal-Mart announced earlier this year that it plans to acquire all of Louis Delhaize's Hungarian stores, which will allow it to slip through just before the window of opportunity for grocery retailing closes. This acquisition will also position Wal-Mart to compete aggressively with the current market leader, Tesco. Merkur, a Slovenian do-it-yourself retailer, plans to open three more centers in Slovenia and six each in Croatia and Serbia in 2007. Apparel retailer Tommy Hilfiger has entered the Croatian and Serbian markets and opened its first accessories store in Croatia in late 2006.

Bulgaria, the fifth Central European country, has risen up the Index rapidly, leaping nine places to enter the top 15 this year. Along with its neighbor, Romania, Bulgaria joined the EU this year, which opens up numerous opportunities for economic growth in this highly fragmented

About the Retail Labor Index

The Retail Labor Index ranks 15 emerging countries on a 100-point scale. A high ranking indicates that a country has a strong labor market. Scores are calculated on the basis of 20 human resources and capital variables. Countries were selected on the basis of their prominence on the GRDI and ranked using three weighted factors:

Talent availability (40 percent). Includes employment potential, availability of scientists and engineers, quality of the educational system, firms offering formal training, permanent skilled workers receiving training, labor regulations a "major or severe" obstacle (variables weight: approximately 16 percent each).

Talent development (40 percent). Includes difficulty of hiring index, rigidity of hours index, difficulty of firing index, rigidity of employment index, hiring costs, firing costs, cooperation in labor-employer relations, ease of hiring foreign labor, willingness to delegate authority and reliance on professional management (variables weight: 10 percent each).

Labor economics (20 percent). Includes pay and productivity, extent of incentive compensation, flexibility of wage determination and production days lost to strikes (variables weight: 25 percent each).

Data and analyses are based on World Bank reports, Global Competitiveness Report 2006-2007 and the International Labor Organization's LABORSTA database.

market. As a result, there will be plenty of opportunities for growth in modern grocery retailing this year. Global retailers such as Carrefour are racing to set up shop, although dominating this market will not be easy, given strong regional retailers such as Kaufland, Dohle and Migros Türk. Like other EU countries (for example, the Baltic states), whose markets rapidly saturated a few years after affiliation with the EU, Bulgaria will enjoy several years of rapid investment and significant retail growth.

2007 Retail Labor Index

Retailers' assessment of expansion opportunities around the globe must include an examination of each country's labor pool. As important as a ready market and consumers are for successful entry or expansion, so is finding a skilled workforce. The A.T. Kearney Retail Labor Index helps executives evaluate labor markets. This Index is based on 20 human resources variables and ranks countries on a 100-point scale *(see figure 5)*. We then plot the Labor Index rankings against

Figure 5

The 2007 Retail Labor Index

2007 Retail Labor Index rank	2007 GRDI rank	Country	Talent availability	Talent development	Labor economics	Retail Labor Index score
		Weight	40%	40%	20%	
1	8	Malaysia	94	92	100	100
2	33	Slovak Republic	100	81	89	97
3	16	Thailand	92	65	82	86
4	1	India	77	81	86	85
5	6	Chile	72	72	97	82
6	24	Indonesia	51	100	89	79
7	7	Latvia	59	73	91	74
8	20	Brazil	73	61	70	73
9	17	Slovenia	71	60	76	72
10	3	China	76	44	85	71
11	26	Hungary	59	62	86	69
12	28	Lithuania	57	62	88	69
13	22	Peru	53	68	82	68
14	19	Croatia	64	47	79	65
15	30	Colombia	51	65	77	65

Legend	Talent availability	Talent development	Labor economics
	0 = low talent availability	*0 = low talent development*	*0 = high cost of labor*
	100 = high talent availability	*100 = high talent development*	*100 = low cost of labor*

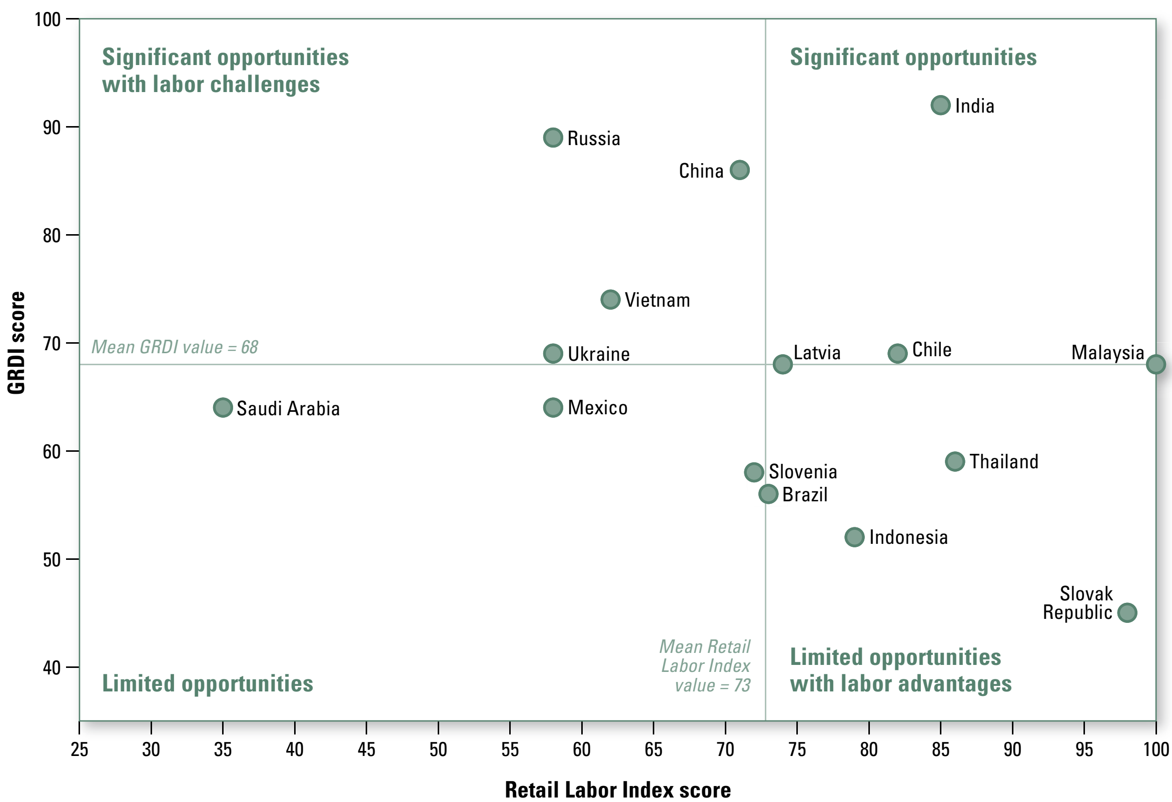
Sources: World Bank reports, Global Competitiveness Report 2006-2007, LABORSTA database, A.T. Kearney analysis the GRDI rankings on a two-by-two matrix *(see figure 6)*. Here, we offer highlights from this year's most promising and challenging labor markets for global retailers.

Malaysia and Chile: bright spots for ample labor. Retailers looking for initial or alternate expansion strategies or risk-hedging plays should consider Malaysia and Chile for their human capital advantages. Malaysia tops the 2007 Retail Labor Index with its young labor pool and one of the region's best education systems and highest literacy rates at 88 percent.

With an urbanized population and strong economic growth, Chile does well on the Labor Index with a highly concentrated labor pool and strong unorganized retail industry converting to modern retail.

India, China and Russia: the going gets tougher. As we noted in 2006 and again this year, India, Russia and China are hot retail markets but continue to face labor challenges. Given their explosive growth in the past few years, these markets have an acute shortage of middle and senior retail management, which is now expensive

Figure 6
Global Retail Development Index vs. Retail Labor Index



Sources: World Bank reports, Global Competitiveness Report 2006-2007, LABORSTA database, A.T. Kearney analysis to employ. Despite their large populations, the supply of qualified talent is limited—and even more so in second-tier cities.

In tier-one cities, the highest salary is no longer the only motivator for these professionals. Surveys from the China Market Research Group (CMR) indicate that the first criterion workers in China now consider is a balanced lifestyle. In second- and third-tier cities, workers still choose salary as their top consideration, followed by job security. Also, retailers need to consider the latent costs of human capital when planning their human resources strategy. These include business disruption costs due to higher attrition rates, losses in brand value, supplier and host government relationship costs, employee morale, expatriate costs and the cost of scarce talent. Primary labor cost is often not the main cost factor. Retailers will need to tailor labor strategies for these different markets—early movers can leverage their knowledge from initial cities to support future expansion.

Shopping for Retail Opportunities

Retailers hope that consumers around the world will accept new ways of shopping when their stores open for the first time. Similarly, retailers must adopt a new way of shopping for global locations if they hope to find receptive markets. Key to that success is targeting each country's window of opportunity, but understanding how consumer readiness loosens wallets is just as important. Finally, as retailers shift from the largest cities to secondary and tertiary locales, an awareness of these new markets' unique opportunities can mean the difference between a short-lived global expansion plan and healthy retail growth now and long into the future.

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