

## William Blair Funds investing for the future: The Global/Local Challenge of Online Groceries

Tyler Chamberlin Ph.D.

### Introduction:

The global COVID-19 pandemic has forced billions of people into their homes and out of retail stores. The result has been a massive shift towards online shopping which has hugely benefited e-commerce companies. In addition to being one of the world's most valuable companies, Amazon is now also the world's most valuable brand<sup>1</sup>, having expanded from books to almost everything consumers want to buy. Well, almost everything. For a company like Amazon, that seeks to make life more convenient for consumers, developing an online grocery always seemed like a natural fit, and they have long coveted this valuable, if competitive, global market. But success in this market has proven elusive, both for Amazon and other would-be online grocery retailers. One of the key questions surrounding, what most expect will be a robust online market for groceries even when the current pandemic passes, is whether the online world of groceries was likely to be more international or even global when traditionally, grocery retailing had remained dominated by domestic competitors.

### The Grocery Business:

Food is a necessity of life, and big business all around the world. For around a hundred years now, grocery stores in most highly developed countries, such as Canada, the US and the UK, have been dominated by large "cash and carry" stores where customers picked what they wanted off of shelves and then lined-up to pay for them. Stores were large, and got larger over the years, and could easily sell over 50,000 individual items. Change occurred but not all that rapidly with the introduction of private label brands, such as President's Choice for example, and new offerings were added and removed as consumers tastes changed and evolved.

But despite a fairly standardized customer experience, grocery retailing remained a largely domestic business. In Canada, the major players were Loblaw, Sobey's and Metro but since the mid-2000's Wal-Mart has also had a strong presence in groceries<sup>2</sup>. When Wal-Mart entered the market there was great concern that the world's largest retailer, at least at the time, would be able to out-compete its Canadian rivals. The same sort of concerns were held by British grocery store chains when Wal-Mart bought the ASDA chain of grocery stores in 1999<sup>3</sup>.

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<sup>1</sup> Abboud, Leila (2019). "Amazon clinches top spot in the world's most valuable brand ranking", *Financial Times*, June 11<sup>th</sup>.

<sup>2</sup> Shaw, Hollie (2014). "Walmart Canada gaining ground in retail food fight", *Financial Post*, Nov 13<sup>th</sup>.

<sup>3</sup> Cowe, Roger; Buckingham, Lisa and Martinson, Jane (1999). "Wal-Mart swallows Asda", *The Guardian*, June 15<sup>th</sup>.

Grocery retailing has proven remarkably resilient to foreign competition. Of course people's tastes for specific foods differed from one country to the next, but given that the business models were the same it was surprising that companies had been able to be successful in their international operations. Where companies have had at least some success, as Wal-Mart has in Canada and the UK it has usually required them to acquire an existing domestic player and then expand or evolve the product offerings. But while Wal-Mart now holds about 12% of the Canadian market<sup>4</sup>, disappointment with their progress in the UK market (where they operate under the Asda brand) led to a proposed merger with domestic rival Sainsbury's, a merger that was eventually rejected by the UK government on the grounds that it would create too large a competitor<sup>5</sup>.

Efforts by the British grocery chain Tesco were largely unsuccessful and required the company to pull back from their attempt to penetrate the US market in 2013<sup>6</sup>. Just recently, it was announced that the company had sold its Polish stores, it's largest market in Europe outside of the UK, for £181m (about \$307m CDN) to a discount chain out of Denmark<sup>7</sup>. Earlier this year, it sold its chain of over 2,000 stores in Thailand and 74 in Malaysia for \$10.6B (USD)<sup>8</sup>. It has also announced that it was ending it's 20% share of a Chinese jointventure<sup>9</sup>.

With these experiences in mind, there was much excitement, and concern amongst established competitors, when Amazon bought the premium American grocery store chain Whole Foods in 2017. Whole Foods had already started to slowly expand into both Canada and the UK and with Amazon's pioneering success in on-line commerce it seemed that revolution, as opposed to evolution, might finally be upon the grocery business.

#### Online-Retailing of Groceries:

Groceries presented a set of new logistical challenges, even for a dominant on-line player such as Amazon. First is the issue of the sheer number of products that customers expect to choose from in a grocery environment, over 50,000 at least. Would online delivery necessitate a reduction in product offerings? The second challenge is the perishability issue. Many groceries need to be kept refrigerated and cannot be just left on people's doorsteps. Urgency is a third challenge, as many

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<sup>4</sup> Shaw, Hollie (2014). "Walmart Canada gaining ground in retail food fight", *Financial Post*, Nov 13<sup>th</sup>.

<sup>5</sup> Eley, Jonathan; Walker, Owen and Pickard, Jim (2019). "Sainsbury's takeover of Asda blocked by UK's competition regulator", *Financial Times*, April 25<sup>th</sup>.

<sup>6</sup> Finch, Julia and Walsh, Fiona (2012). "Tesco's American dream over as US retreat confirmed", *The Guardian*, December 5<sup>th</sup>.

<sup>7</sup> Nilsson, Patricia (2020). "Tesco quits Poland in further retreat from overseas ambitions", *Financial Times*, June 18<sup>th</sup>.

<sup>8</sup> Reed, John & Eley, Jonathan (2020). "Tesco agrees \$10.6bn sale of Thai and Malaysian operations", March 9<sup>th</sup>.

<sup>9</sup> Ibid.

customers are looking to receive their products today, if not immediately. Two days is convenient for most Amazon purchases but delivering today is a new challenge. Did these last two challenges require a new technological solution? If so, it would appear that a company like Amazon, that was already developing its own delivery technologies, would be in a much better position to succeed.

The Situation in 2020:

Most the largest players in the grocery business had begun selling products online and offering either in-store pick-up or home delivery, albeit typically only in select urban markets. When the COVID-19 pandemic hit in early 2020, retailers of all products scrambled to find new ways to get their products into the hands of customers. In-store or curbside pick-up was a much easier solution for stores but avoiding going to stores appeared to be what customers really wanted. The ways in which companies had chosen to go on-line with their deliveries varied significantly.

In Canada, both Wal-Mart and Loblaw have partnered with a US-based company called Instacart which has both an app and 'boots on the ground' delivery service. In the UK, Amazon is providing delivery services for the established grocery store chain Morrisons, despite their ownership of Whole Foods. It was thus not yet clear whether delivery would end up being a service provided by established retailers or by new specialized technology companies. Finding the right partner company could mean success and an early advantage for firms operating within markets that remained largely domestic but developing the "last-mile" solution to grocery delivery could be the basis upon which a global grocery retailer might finally be developed into a dominant player in multiple markets internationally.

William Blair Funds LTD:

William Blair & Company is an American investment bank and financial services company headquartered in Chicago. The company was established in 1935 and has almost \$100B USD in assets under management. Their International Growth Fund looks to invest into companies that are likely to experience growth in the next couple of years, over and above what is expected for the industries in which they are operating. In other words, they are looking to select the companies that are best positioned to out-perform their competitors.

As a new investment analyst with William Blair, you have been asked to look at the market for on-line groceries and to select one company from either the United States, Canada or the United Kingdom which you believe is well positioned to out-perform over the next few years in this market. The company can be an existing grocery retailer such as Loblaw, Wal-Mart or Morrisons, or one of the app developers such as Instacart or an online retailer such as Amazon. You will want to consider the business model

of the company (how they make money), the market(s) in which they operate, and the likelihood of success of their approach to on-line grocery shopping compared to the others being developed.