FORUM
2015

RETAIL

+ Lifting-The-Barriers Roundtable

Preliminary Paper

ATKearney

CARI CIMB ASEAN RESEARCH INSTITUTE

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About CARI

The CIMB ASEAN Research Institute (CARI) was established in 2011 as a member of CIMB Group. CARI prides itself on being the first independent, transnational research institute dedicated solely to the advancement and acceleration of the ASEAN integration agenda. CARI was designed to pursue research and to promote thought leadership in support of an integrated ASEAN Community. CARI seeks pragmatic solutions and policy recommendations to address challenges in ASEAN integration and connectivity. CARI's headquarters is located in Kuala Lumpur but the institute has a regional presence.

ASEAN
BUSINESS
CLUB

About ASEAN Business Club

A fully private sector driven initiative of ASEAN's leading businesses coming together to support economic integration while providing a platform for networking. The ABC creates an avenue for ASEAN's businesses to engage with global regional leaders. The club's vision is ASEAN: Open for Business.

About A.T. Kearney

A.T. Kearney is a leading global management consulting firm with offices in more than 40 countries. Since 1926, we have been trusted advisors to the world's foremost organisations. A.T. Kearney is a partner-owned firm, committed to helping clients achieve immediate impact and growing advantage on their most mission-critical issues. We continue to live by the principles established by our founder Andrew Thomas (Tom) Kearney and his belief that "our success as consultants will depend on the essential rightness of the advice we give and our capacity for convincing those in authority that it is good."

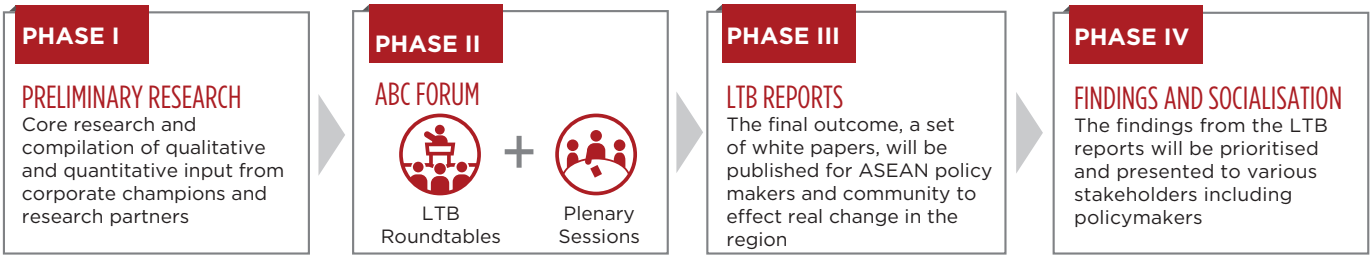
PREFACE

The Lifting-The-Barriers Initiative (LTBI) is a year-long research exercise designed in conjunction with the ASEAN Business Club (ABC) Forum. The overall objective is to conduct sector based research with the purpose of identifying bottlenecks and barriers to trade and ASEAN economic integration.

The LTBI in 2013 and 2014 have yielded 13 reports for 11 sectors, namely 1) Financial Services, 2) Capital Markets, 3) Connectivity, 4) Aviation, 5) Infrastructure, Power and Utilities, 6) Healthcare, 7) Legal and Tax, 8) Automotive and manufacturing, 9) Minerals, Oil and Gas, 10) Retail, 11) Food and Beverage Industry. The LTBI 2015 continues to highlight five key sectors covered in 2013 and 2014, with the addition of the tourism sector which is one of the twelve priority integration sectors (PIS) of the ASEAN Economic Community Blueprint.

The Lifting-The-Barriers reports have been widely referred to by ASEAN policy makers and stakeholders. The ASEAN Chair of 2015, the Right Honourable Prime Minister Dato' Sri Najib Razak, publicly cited the LTB reports as being a useful guide for Malaysia's stocktake exercise to identify the gaps between ASEAN aspirations and the reality in the business sector, in anticipation of the pronouncement of the ASEAN Economic Community later this year.

The LTBI has four phases, each playing a unique role in helping achieve the wider objective. Details of the initiatives are:



Phase I:
Phase I of the LTBI involves core research and seeks to identify the existing barriers in each sector to assist in understanding the challenges faced by different segments of the industry. We also study the AEC obligations and impacts on businesses and the industry as a whole.

Phase II:
Phase II convenes around the sector based "Lifting-The-Barriers Roundtables" at the ABC Forum. The roundtables serve as a platform for different stakeholders to deliberate on the future of their sector and of ASEAN as a region.

Phase III:
Phase III consists of the production of the final outcome of this exercise, the Lifting-The-Barriers Reports, white papers delivered to the relevant regulatory bodies to effect real change and accelerate ASEAN integration efforts. This phase will consolidate materials from Phase I and Phase II. The Reports summarise the industrial insights and ideas discussed at the Roundtables.

Phase IV:
Phase IV is the socialisation of key findings from the LTBI. This phase involves the distribution and presentation of the key findings to the relevant regulatory bodies as well as to other industry stakeholders. The 2014 LTB Reports were distributed to over 1000 companies and corporate entities as well as presented to various ASEAN government bodies and institutions.

DISCLAIMER:

This is a discussion paper intended to inform and facilitate debate for the ASEAN Business Club Forum on the 14th of May 2014. It is not for submission, distribution or for any other purpose for which it was not intended. No citation or quotation is to be extracted from this report without the express consent of CIMB ASEAN Research Institute and the relevant Research Partner

TABLE OF CONTENTS

1 Executive Summary 2
2. Part I: Retail Innovation Landscape 2
3. Part II: ASEAN and Retail Innovation 4
4. Part III: Barriers to Retail Innovation in ASEAN 6

EXECUTIVE SUMMARY

Innovation in retail has been accelerating for the past couple of decades across the globe, expanding and improving retailers' products and services and significantly enhancing the level of interactions with consumers. As retailers are focused on further driving consumer experience and creating more value, we expect the pace of Innovation to pick-up even more in the coming years.

Although most ASEAN countries have engaged in the path towards "retail modernity" over the last years, retail innovation in ASEAN is today still in the early stages of development. The penetration of new products, services and platforms such as private labels and e-commerce are indeed still low compared to more developed markets.

Driving innovation in ASEAN represents a unique opportunity to take the retail industry to the next level, improving the retail experience for consumers, facilitating the emergence of regional players, homogenising the retail space across countries and helping drive ASEAN markets integration.

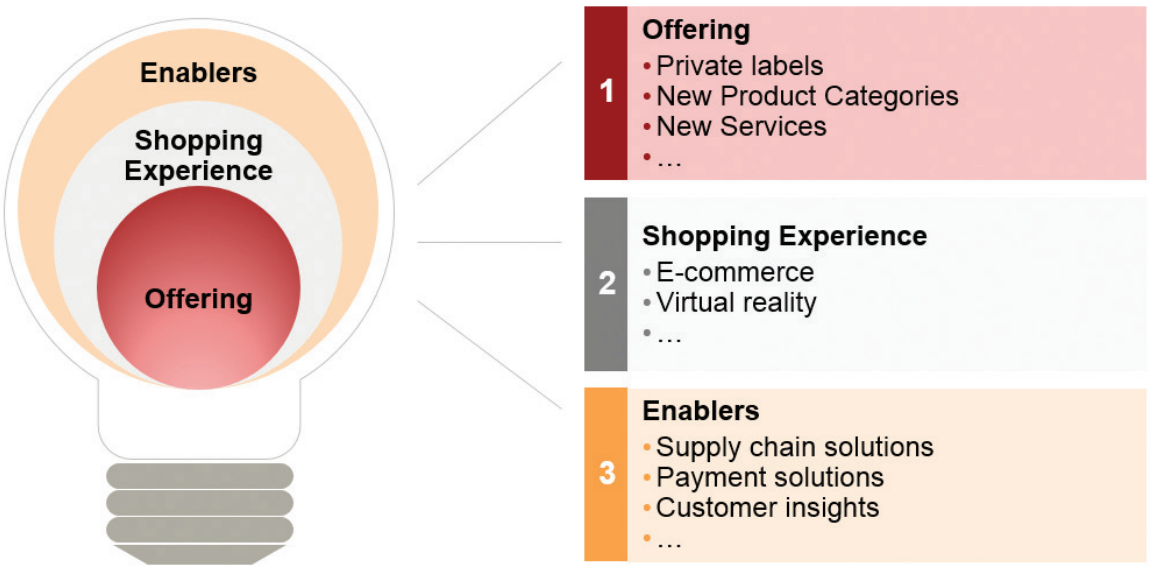
However, there are barriers to the development of retail innovation in ASEAN that need to be overcome, including market readiness, lack of scale, access to financing for innovators, integration of talent, insufficient infrastructure capabilities and cumbersome regulations. In order to fully unleash the potential of retail innovation and capture impact for the region, these barriers need to be addressed and overcome.

This paper will aim to provide an understanding of the landscape of retail innovation opportunities and asses the current status of retail innovation in the region. It will specifically highlight potential barriers and the role of key stakeholders in overcoming those barriers, leveraging inputs from the Lifting-The-Barriers Roundtable.

PART I: RETAIL INNOVATION LANDSCAPE

The different types of innovation in the retail space can be grouped into 3 buckets: Offering, Shopping Experience and Enablers.

Figure 1. Retail Innovation Landscape



Source: A.T. Kearney

1. Offering

Some of the most visible innovations in the retail space are down to the new products and services which have been progressively launched over the years by retailers across the globe.

Retailers have first looked at creating their own store-label brands, directly competing with the branded products that they were distributing. Those own-store-branded goods also known as private label goods really started taking-off in the 1990s. In what started as a retailer's low-cost & low-quality substitute for known brands, private labels now have significantly increased in quality, delivering to consumer needs across wider price points. They have even become a key differentiator for some retailers in terms of good quality offering with lower prices, positively affecting the retailer's image.

Retailers have also looked at expanding their offering to become more competitive and drive consumer loyalty, getting into new product categories and expanding into new services. For example, major retailers such as Tesco have expanded their businesses into financial services (Tesco Bank) and telecommunications (Tesco Mobile).

2. Shopping Experience

One of the key innovations in the consumer interaction space has certainly been the growth of e-commerce, which has been revolutionising not only the retail business but also how FMCGs develop, market and distribute their products. E-commerce gained scale in the 1990s as an alternative way of engaging the customers from the traditional brick-and-mortar store format and to provide more convenience. Over the past two decades, it has grown steadily, making up 7% of the global retail industry in 2014, or around US$1.5 trillion. The global e-commerce market is expected to grow between 15 and 17% per year to reach US$2.4 trillion by 2017 and more than US$7 trillion by 2025. Growth in the developed markets will be driven by the increase of wallet and basket size while growth in the developing regions is expected to be fueled by digital adoption and the increased penetration of shoppers.

More recently, the retail space has also seen the emergence of "Virtual Reality" (VR) innovations providing consumers with a more tangible in-store experience. Virtual reality could be the next frontier for retail, with most of the VR applications currently still under development. Different retailers ranging from fashion apparel companies or furniture providers to automotive and grocery retailers have launched several initiatives into the virtual reality space, in an effort to merge the physical and digital world. These initiatives also served as a differentiating factor for the retailers, helping create a buzz that further showcases their brand image. Several applications implemented by retailers include VR stores recreating the in-store experience; VR fitting rooms used by apparel retailers to allow quick and hassle-free fittings; and VR mirrors to enables shoppers to try the look of different eyeshadows and lipsticks without applying them to the skin.

3. Enablers

Significant innovation has also occurred over the past years on the back-end and operational side of the value chain. Innovations have specifically enabled retailers to optimise processes and be more cost efficient whilst improving service levels. The majority of retailers are leveraging "big data" to analyse past buying behaviors and predict trends which enable them to optimise stocks or manufacturing orders. Some retailers are also using Radio Frequency Identification (RFID) technologies which enable them to track merchandise from the manufacturer, providing a more accurate view on stock levels.

Major innovations have also been introduced in the area of payment solutions, making payment easier and more convenient for consumers. From Near Field Communication (NFC) "tap to pay" wallets or aggregator mobile payment applications that consolidate all cards to hands-free payment via beacon technology, innovations are numerous and are expected to keep the pace as new technologies development accelerates.

With the rise of mobile applications and social media, retailers have also found ways to improve the shopping experience using technologies, including QR codes, navigation technologies/smartphone applications or smart trolleys which synchronise the shopping list and identify promotions.

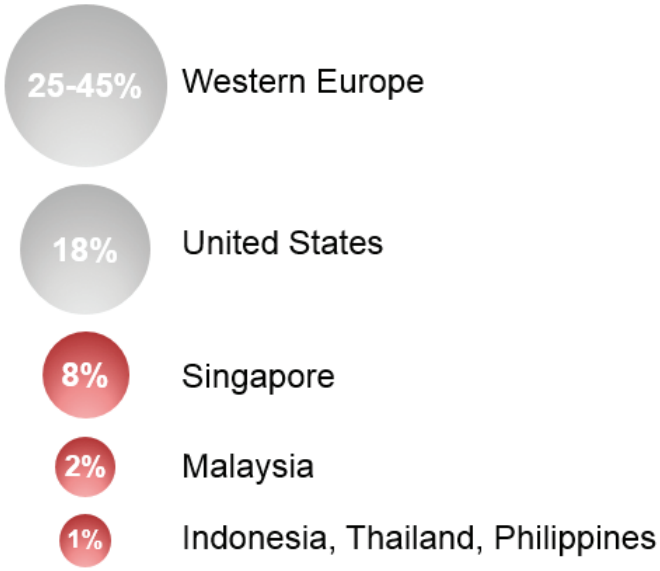
PART II: ASEAN AND RETAIL INNOVATION

1. Where is ASEAN Today?

Although most ASEAN countries have engaged in the path towards "retail modernity" over the last years, retail innovation in ASEAN is today still in the early stages of development. The penetration of new products, services and platforms such as private label and e-commerce are indeed not at the level observed in more developed markets.

Private label penetration in ASEAN is still relatively low (see Figure 2), with most countries except Singapore, being at 2% or lower retail penetration vs. 20-30% in more developed countries. As modern retail markets in the region mature, private label penetration is expected to accelerate and catch up with the rest of the world. A recent study from Nielsen confirmed the consumer pull; with consumers across ASEAN perceive private label goods more favorably and are starting to view them as a viable alternative to known brands.

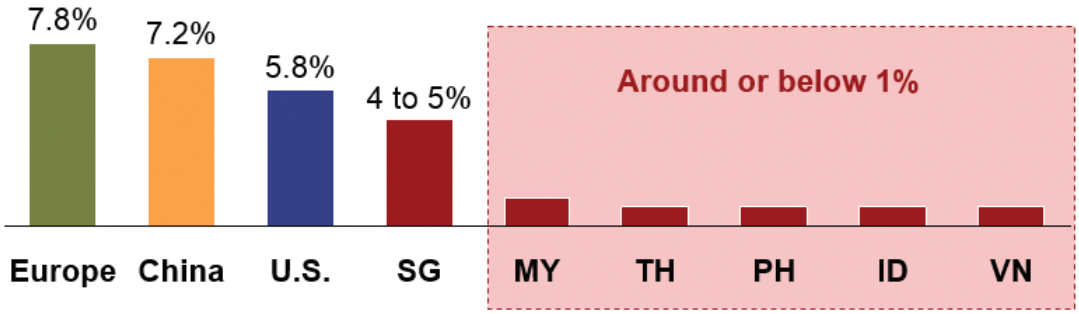
Figure 2. Penetration of Private Label Products in Retail



Source: Nielsen, *The State of Private Label Around the World, November 2014*

As shown in Figure 3, e-commerce is relatively strong in Singapore in terms of percentage of retail sales made online (at 4-5%, compared to US, China, and Europe's rate of 6-8%); however, the 2nd most mature country of the ASEAN-6 is quite far behind (at around 1%)

Figure 3. E-Commerce Sales as % of Total Retail Sales



Source: Frost & Sullivan, *High Growth and Consolidation Expected in Southeast Asia's eCommerce Market, July 2014*

As shared in our previous report, the ASEAN region is expected to be one of the world's fastest growing markets for e-commerce in the next few years, with an expected annual growth of about 25%. Cross-channel integration has already started to develop, with bricks-and-mortar stores are now investing in their multi-channel offering in order to stay competitive. This trend is increasingly developing in Indonesia, Thailand and the Philippines, where the growing number of online shoppers have prompted retail brands to offer innovative services such as online gift registries or in-store pickup or delivery services.

2. A Unique Opportunity for ASEAN

Driving innovation in ASEAN represents a unique opportunity to take the retail industry to the next level, improving the retail experience for consumers, facilitating the emergence of regional players, homogenising the retail space across countries and helping drive ASEAN market integration.

Figure 4. Benefits of Retail Innovation to Key Stakeholders

Source: A.T. Kearney

Driving innovation in the retail space is expected to deliver broad benefits to all stakeholders.

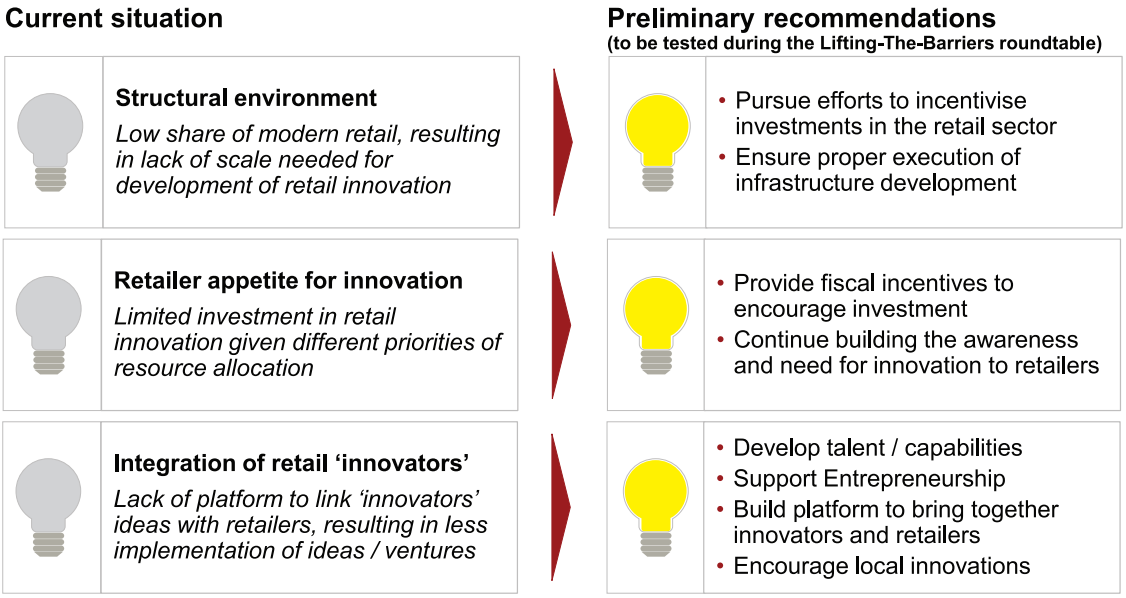
First, **consumers** would enjoy an improved retail experience, a broader menu of products (e.g. from across ASEAN), better products and lower prices. **Retailers** are expected to strengthen their offering and grow, giving to some of them the scale to expand across the region. Investing in innovation can also serve as a platform to build the company brand and image. At the **country** level, ASEAN would benefit from a more dynamic retail industry to reach their national growth and development targets. And finally, higher GDP and regional homogeneity in the retail space are expected to help drive **ASEAN market integration**

[1] *Lifting the Barriers to e-Commerce in ASEAN, 2014*

PART III: BARRIERS TO RETAIL INNOVATION IN ASEAN

However, there are barriers to the development of retail innovation in ASEAN that need to be overcome. Those include market readiness, lack of scale, lack of access to financing and talent, insufficient infrastructure capabilities, and cumbersome regulations. In order to fully unleash the potential of retail innovation and capture the full impact for the region, these barriers need to be addressed and overcome.

Figure 5. Key Barriers to Innovation in Retail

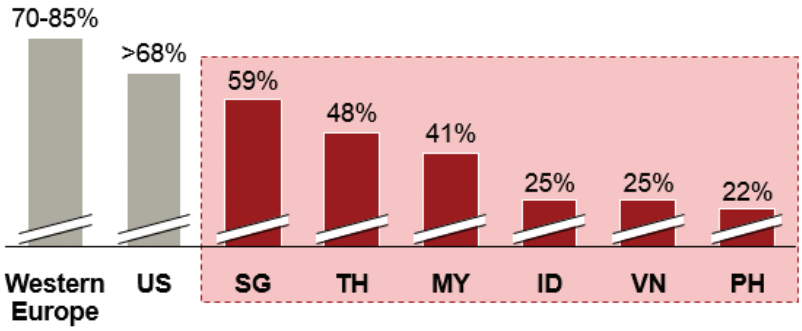


Source: A.T. Kearney

1. Structural Environment

Given the lower share of modern retail in ASEAN at around ~20-40%, excluding Singapore, compared to 70-85% level in the US and Europe and the still dominating cultural adherence to traditional mom-and-pop stores in rural areas, many retailers may not yet have the scale relevant to warrant investing in and adopting retail innovations.

Figure 6. Modern Retail as % of Total Retail Sales (2014)



Source: Planet Retail, *Country profiles reports, 2014*

There are examples of initiatives across the region to help drive the penetration of modern retail. The Vietnamese government is investing significantly to convert traditional wet markets into modern trade centers and upgrade traditional grocery retailers to ensure higher standards of hygiene and food safety. Countries such as Indonesia have also put infrastructure as a top priority on their agenda and various government initiatives throughout the region have been underway to develop toll roads, ports and railways.

However, there are still some opportunities to improve the structural environment through putting in place policies that incentivise investments in the retail sector (e.g. tax subsidies and tax exemptions for local and international retailers seeking to invest in ASEAN countries) and through helping to ensure that infrastructure development initiatives are carried out.

2. Retailers' Appetite for Innovation

Most of the major retailers in ASEAN have announced plans for new store openings in the coming years (see figure 7). To name a few, strong expansion plans have been announced in Indonesia by Hypermart, Indomaret and Alfamart. Many leading foreign retail chains have also expanded their branches in the region over the years. The upcoming ASEAN Economic Community (AEC) should drive local retailers' cross country expansion approach as illustrated by the investments of Alfamart in the Philippines and Central Group in Vietnam.

However, more can be done to further drive retailers' appetite for innovation in the region on coordinating innovation development efforts amongst smaller retailers and building partnerships with international retailers that can bring retail innovations into the region. To illustrate, Singapore has taken the initiative to develop a Retail Innovation Center for Enterprises (RICE) in 2014. The institution aims to educate retailers by acting as "one-stop service" information on the latest technological solutions (mobile apps, management software, payment solutions, etc…). This initiative is the first of its kind in ASEAN and paves the way for further promising retail innovation developments in the region.

To encourage more investments in retail innovation, governments can also provide various fiscal incentives in the form of tax reductions, or exemptions and subsidies for innovation-related technology and classify these types of investments in a separate class. This would incentivise more companies to transfer knowledge into ASEAN and develop the retail innovation industry in the region.

Figure 7. New Store Opening Plans at Major Retailers

Country	Retailer	Recent announced plans
Malaysia	G-Express	+ 500 stores by 2020
Indonesia	Hypermart	+ 20 new stores in 2015
	Alfamart	+ $166Mn in 2015 in stores expansion and DCs
	7-Eleven	+ 2,500 new stores by 2025
	Lotte	+ 4 malls by 2018
Philippines	Philippines Seven Corp	+ 500 7-Eleven outlets in 2015
	All-Day	+ 100 new convenience stores
	Robinsons	+ 10 stores by end of 2015
Vietnam	Vingroup – Ocean Retail	+ 24 shopping centers in 2015
	Aeon	+ 20 shopping malls by 2020
	Berli Jucker	+ 205 convenience stores by 2018
	Nguyen Kim	+ 30 stores by 2019

Source: Desk research, Corporate websites

3. Integration of Retail 'Innovators'

There is still a relatively low level of exposure of the ASEAN retailers to the retail innovators either because promising ideas do not get sufficient support or resources or simply because avenues to interact with retailers are lacking.

In Singapore, the Infocom Development Authority (IDA) launched FutureSchools@Singapore, designed to encourage innovation and entrepreneurship in schools. This program equips students with the skills needed to be effective workers and citizens in the globalised and digital world. IDA industry partners will also use FutureSchools to experiment and commercialise the most promising new ideas.

Within the region, developing incubators for retail innovation would provide a platform for ideas. However, as the next step to take the idea to implementation, governments need to link these innovation ideas to the retailers, by holding trade fairs or other retail innovation-related conventions, or creating avenues of communication between innovators and retailers.

AN INITIATIVE BY

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