

SWOT analyses

Discussion and analysis of
three major UK retailers

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COMPANY SNAPSHOT

BOOTS



Boots is the UK's largest chemist chain and employs almost 75,000 staff. The retailer has close to 2,500 pharmacy-led health and beauty outlets, which includes 624 Boots Opticians. A vital piece of the company's strategy is its Boots Advantage Card, which is thought to be the world's largest smartcard loyalty scheme, with more than 17 million active holders in 2012.

In June, parent Alliance Boots entered into a strategic partnership with Walgreens, the largest drugstore operator in the US, to create a global, pharmacy-led, health and beauty business. Walgreens has invested £4.3bn in cash and shares to acquire a 45% equity interest in Alliance Boots and will acquire the remaining 55% within the next three years for a full merger.

As a result, Stefano Pessina, who has been executive chairman of Alliance Boots since July 2007, will now be on the board of directors of Walgreens, while four directors from the US company have joined the Alliance Boots board. Alex Gourlay, chief executive of the health and beauty division at Boots, believes there is potential to leverage Walgreens' 7,890 US stores to increase sales of its popular own-label ranges, from No7 to Botanics.

In the year to March 2012, Boots saw UK sales dip 0.2% year on year to £6.7bn, with Boots Opticians contributing £332m. However, retail trading profit increased to 5.2% to £750m, with its trading margin rising to 11.2%. International trading profit growth was significantly more than domestic, with a 16.7% rise to £63m. During this period the group reported a 2.4% decline in sales of retail health products to £891m, while beauty and toiletry sales increased 2% to £2.2bn.

On a strategic front, Boots this year has overhauled its consumer website and launched its 'order online, collect in store' concept, available in nearly all its UK stores. Also, in August the retailer launched an extended food offer in partnership with Irish food retailer Musgrave. Launched initially in 11 stores, this new convenience food offer focuses on 'food to go', 'food for later that night' and 'fresh top up'.

WALGREENS HAS INVESTED £4.3BN IN CASH AND SHARES TO ACQUIRE A 45% EQUITY INTEREST IN ALLIANCE BOOTS

Stats for year ending March 2012

UK sales
£6.71bn
(includes Boots Opticians)

UK operating profit
£750m

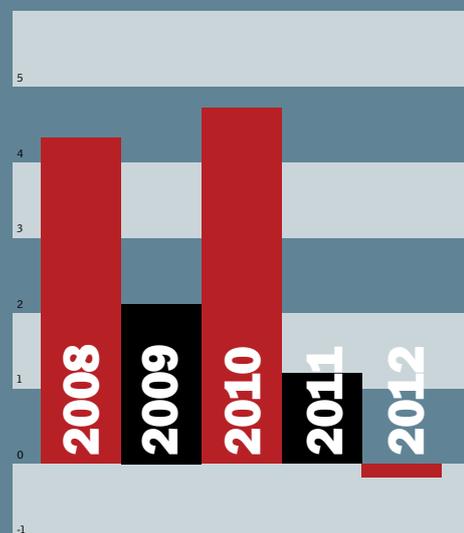
UK stores
2,477

UK employees
74,851
(Chemist / retail employees)



UK sales change (%)

Sales growth



● UK sales change (%)

SWOT ANALYSIS

BOOTS



▲ STRENGTHS

- **Biggest chemist chain in the UK** Boots has more than 2,500 chemists shops in this country alone, including the Alliance community pharmacies, giving it a dominant share of a big and resilient market.
- **Ethical image** Boots is one of the most trusted brands in UK retailing, reflecting a strong heritage and the ethical image derived from its pharmacy operations.
- **NHS pharmacy footfall** The Boots' dispensing business drives significant footfall from customers picking up prescriptions and seeking advice, giving invaluable pick-up trade opportunities
- **Own-label brands** Boots owns several highly regarded and long-established brands such as No7 in beauty, Soltan in suncare and Botanics in toiletries, many of which are manufactured at Boots' own factory on its Nottingham HQ site.
- **Powerful loyalty card** Launched back in 1997, the Boots Advantage Card is a powerful tool for rewarding customer loyalty (collecting four points for every £1 spent) and one of the biggest and best loyalty card schemes in the UK.
- **High margins** Boots the Chemist is not as profitable as it was 10 years ago, when EBIT margins were 14% to 15%, but it is still a double-digit operating margin business.

▼ WEAKNESSES

- **Mature** Boots is so dominant that it will find it hard to grow its UK market share further.
- **Clinical store design** The downside of having the pharmacy business is that many of the stores are rather clinical in their ambience and in-store fixturing is often quite basic.
- **Weak non-core sales** Outside its core beauty, healthcare and toiletries business, Boots struggles to hold its sales in so-called 'Lifestyle' categories like photographic, electricals, beauty care and baby.
- **Boots Opticians** Despite the economies of scale from the Dollond & Aitchison merger, the Opticians business still struggles to make money and find a position in the market relative to competitors such as Specsavers.
- **High street base** Although the pharmacy business has to be close to its customers, the decline in many high streets relative to out of town and online shopping leaves Boots' big high street presence a little exposed.
- **Pharmaceutical regulations** With NHS budgets under pressure, the remuneration for dispensing prescriptions is subject to Government regulation and oversight.

▲ OPPORTUNITIES

- **Services** Although somewhat discredited by Boots' poorly executed foray into wellbeing services 10 years ago, the provision of healthcare services for consumers remains an opportunity, given Boots' ethical image.
- **Synergies** The merger with the pharmaceutical wholesaler Alliance Unichem and the more recent deal with US drugstore giant Walgreens provides scope for buying economies.
- **Product development** The increasing interest in personal health and wellbeing provides plenty of potential for Boots to provide useful new products such as anti-ageing treatments.
- **Third-party sales** As well as contract manufacturing in toiletries, Boots has further potential to sell its key product brands, such as No7 cosmetics, to overseas retailers and websites.

▼ THREATS

- **Discounters** Although the Superdrug drugstore chain has failed to make much impact on Boots in recent years, there are strong discount competitors such as Bodycare, as well as the incursion by 'pound shops' into branded toiletries.
- **Supermarkets** All the big supermarket chains have considerably improved their cosmetics and toiletries departments in recent years, as well as opening pharmacies in some cases, and the power and convenience of 'one-stop shopping' at supermarkets is a constant threat to Boots' core business and customers.
- **Strategic direction** Having been subsumed into the Alliance Unichem empire of Stefano Pessina, a consummate dealmaker, and then into private equity ownership by KKR, Boots UK has not lost momentum. But there is a risk that the recent merger with the Walgreens business in the US will drag the business downmarket in its focus and that Boots UK doesn't get the investment that it needs.

Nick Bubb, Sept 18, 2012

KEY PEOPLE

Executive chairman

Stefano Pessina

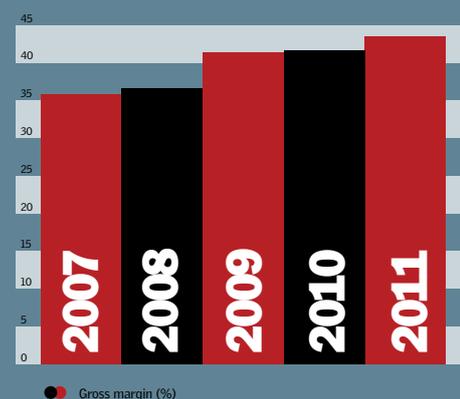
Group finance director

George Fairweather

Chief executive, health and beauty

Alex Gourlay

Operating performance



● Gross margin (%)

COMPANY SNAPSHOT

HOME RETAIL GROUP



Home Retail Group owns Argos, the UK's high street and catalogue retailer, and Homebase, the second largest DIY specialist chain*. Argos has almost 750 stores, employing more than 30,000 staff, while Homebase has more than 340 edge-of-town superstores, with about 19,000 employees. Home Retail also owns the Habitat brand, which includes the UK website and three London stores, and stocks its products in store and online at Homebase.

Sales at Argos and Homebase have declined in three of the last four years, with the rate of deterioration accelerating in the financial year to February 2012. During the period, Home Retail's sales totalled £5.49bn, of which Argos generated £3.87bn and Homebase £1.51bn. Both businesses suffered like-for-like sales declines of 8.9% and 2% respectively. At Argos, laptops and tablets sales grew, but the decline in the consumer electronics market, particularly TVs and video games systems, more than offset this rise. On the whole, group operating profit plummeted 67% to £84.7m.

In the half-year to September, sales at Home Retail fell 1% to £2.53bn. During this period, operating profit at Argos totalled £3.3m on sales of £1.68bn, with like-for-likes up 0.6%. Multichannel participation increased to account for 51% of total revenues, with the check-and-reserve option accounting for 30% of overall sales. Homebase generated sales of £787m, down 6.2% on a like-for-like basis, as operating profit fell to £24.5m. This was mostly due to poor weather conditions affecting sales of its seasonal products and the difficult market conditions in big-ticket categories.

During this time, Homebase launched a new store format in Aylesford, Kent, which featured an upgraded kitchens offer, including an installation service, and several new product lines. Also, internet sales participation rose by 25% year on year, while its reserve-and-collect sales increased 31%. In July, Homebase relaunched its website and in October it rolled out a mobile-optimised site.

In the same month, Argos managing director John Walden, who joined in February, revealed the retailer's new five-year strategy, which includes £300m of investment, to position Argos as a digital retailer. The scheme will move the Argos catalogue from the lead channel into a 'supporting role'. Walden also said the retailer will position the focus of its stores on the collection of product and customer service for sales that will "increasingly be managed online or through mobile". Argos also aims to relocate or shut about 75 shops (10% of the estate) in the next five years.

*In terms of most recent annual sales

ARGOS' NEW FIVE-YEAR STRATEGY IS TO POSITION IT AS A DIGITAL RETAILER



Stats for year ending February 2012

UK sales
£5.49bn

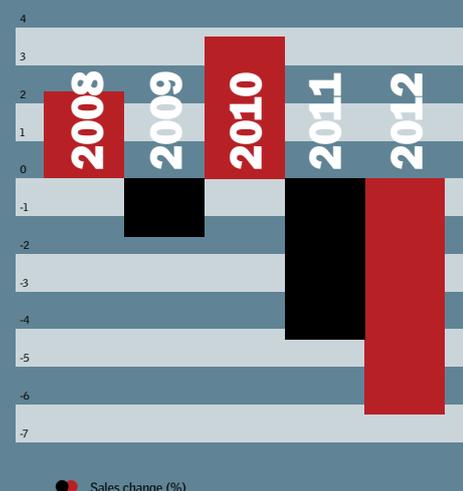
UK operating profit
£84.7m
(excludes central services and financial services)

UK stores
1,089

UK employees
49,688



Sales growth



SWOT ANALYSIS

HOME RETAIL GROUP



STRENGTHS

- **Key player in non-food** UK home and general merchandise retailer Home Retail Group has a 10% share of the market and leadership positions in many product categories.
- **Well-known brands** Argos and Homebase are among the best known brands in UK retailing, and the group also owns some strong own-label brands, such as Habitat in furnishings, Bush and Alba in consumer electronics, Chad Valley in toys and Schreiber and Hygena in furniture.
- **Multichannel pioneer** Argos was the first major retailer to develop a click-and-collect approach to online retailing and still claims to be the leading multichannel retailer in the country.
- **Synergies** Since the acquisition of Homebase in 2002, the group has been able to achieve significant synergies in buying and sourcing, particularly via the direct import and direct sourcing of common furnishing and furniture products from the Far East.
- **Tight cost control** The group has a very strong record of delivering significant organisational and infrastructure changes to reduce operating costs, particularly in the distribution and supply chain, to offset underlying cost inflation.
- **Strong cash generation** Despite the recent pressures on profitability and dividend cover, Home Retail has a good record on working capital control and cash generation. It also still has net cash on the balance sheet as well as a significant receivables loan book.

WEAKNESSES

- **Cyclical markets** Home Retail's strongest markets are the ones under the greatest cyclical pressure from the prolonged UK recession and the housing market downturn, notably big-ticket furniture and furnishings and DIY, as well as video games.
- **Mass-market customer positioning** The typical Argos customer is very exposed to the job insecurity and credit availability constraints of the mass-market demographic.
- **Structural change** As well as cyclical pressures, the inexorable process of structural change in the marketplace is also swamping Argos, as the competition (eg, Dixons) catches up with its multichannel expertise and offers more compelling products and stores, with Argos tied to its costly twice-yearly catalogue and promotional leaflets and self-service showroom approach.
- **Profitability pressures** Profits have collapsed alarmingly in recent years, despite tight cost control, with EBIT margins heading to well below 2% this year. If multichannel participation has grown to be now nearly half the Argos total business, in sales terms, what does that say about the trends in the other half of the business? Homebase too, is not as profitable as its DIY rivals.
- **Over-spaced** Argos justifies a portfolio of 750 expensive stores on the grounds that it needs them for its click-and-collect service, but there remains pressure to downsize.
- **No credible overseas exposure** Home Retail has avoided making loss-making overseas acquisitions, but it has also failed to reduce its dependency on the UK market.

OPPORTUNITIES

- **New products** The Habitat brand re-launch should help increase customer loyalty and Argos has shown it can sell new technology, in the form of booming sales of tablet PCs and e-readers.
- **A new pair of eyes** The new US managing director of Argos, John Walden, is very experienced in US multichannel retailing and brings a fresh approach to the chain's challenges.
- **Homebase differentiation** Homebase has a differentiated position at the 'softer' end of the DIY, gardening and home enhancement market and its prototype store in Aylesford shows its potential to be a stronger business.

THREATS

- **Outdated business model?** It is telling that the catalogue showroom store format has died a death everywhere else in the world, except in the UK. In the US, the discount stores such as Walmart and the online giants such as Amazon destroyed the convenience and range advantage of the catalogue showroom chains many years ago, so time is not on Argos' side.
- **Excessive cost control** Home Retail claims that its tight cost control has not affected customer service standards, but this may be hard to maintain if staffing ratios continue to be pruned.
- **Excessive discounting** Both Argos and Homebase rely heavily on regular sales and price-cutting, but this inevitably undermines customer confidence in initial pricing and encourages them to wait for the next promotional event.
- **Competition** Both of Homebase's principal competitors, B&Q and Wickes, are well-managed, while Argos faces myriad specialist and generalist competition, from Dixons and DFS, to Amazon and Apple.

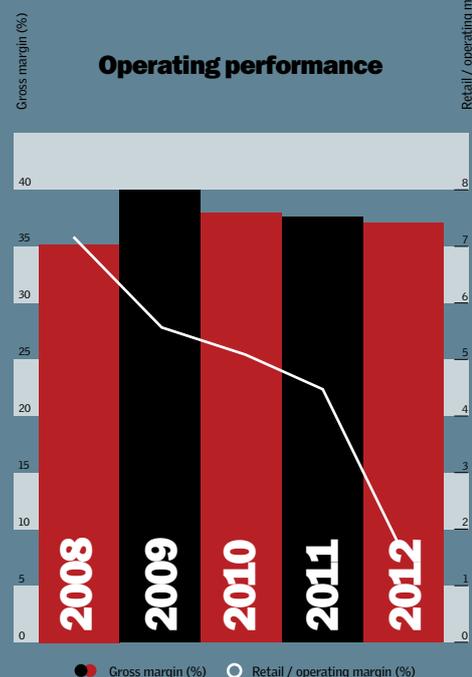
Nick Bubbs, Sept 17, 2012



KEY PEOPLE

Chief executive officer
Terry Duddy

Group finance director
Richard Ashton



COMPANY SNAPSHOT KINGFISHER

KINGFISHER

Kingfisher is the UK's leading DIY retailer employing about 27,000 full-time employees. In the UK, the group has nearly 360 B&Q DIY superstores, which includes 29 former Focus stores, and a rapidly-expanding chain of 215 Screwfix trade counters. The group is one of the UK's most international retailers with extensive overseas DIY interests centred round retailers Castorama and Brico Dépôt, as well as B&Q. It has more than 950 stores in eight countries in Europe and Asia.

Overseeing these operations is group chief executive Ian Cheshire, whose recent changes to the board include the promotion of chief executive of B&Q and Kingfisher UK Euan Sutherland to chief operating officer. Also, group finance director Kevin O'Byrne was appointed divisional chief executive of B&Q, with Karen Witts, previously at Vodafone, announced as a replacement.

Kingfisher had a strong performance in the year to January 2012 as it totalled group sales of £10.83bn, 60% of which were generated overseas. The group's domestic sales remained flat at about £4.34bn for the period, though B&Q UK and Ireland's retail profit increased 10.9% to £238m.

However, group sales fell 3.3% to £5.48bn in the first half of the year to July, with like-for-like sales falling 2.8%, while retail profit dropped 14.7% to £403m. Kingfisher blamed wet weather in the UK and northern Europe for "significantly" impacting footfall. During this period the UK was particularly hard hit as retail profit plunged 20.2% to £145m and like-for-like sales dropped 5.5%. The wet weather also meant seasonal product sales fell 7%, forcing the retailer to slash prices to clear stock.

Making up for lost ground this summer, B&Q is set to launch a series of multichannel initiatives next year, including in-store kiosks and an overhauled website. The group has also launched a property review and has begun to sublet store space for the first time to retailers including Asda, as it looks to reduce its footprint as multichannel sales grow. At Screwfix, Kingfisher rolled out its first own-brand range of clothing targeting tradesman and the "serious DIYer".

KINGFISHER IS ONE OF THE UK'S MOST INTERNATIONAL RETAILERS WITH MORE THAN 950 STORES IN EIGHT COUNTRIES



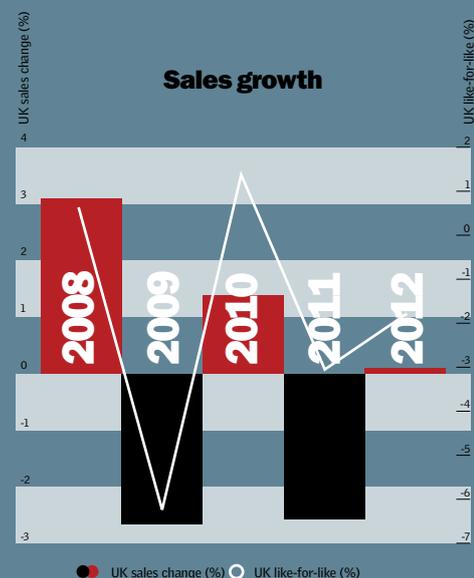
Stats for year ending January 2012
Figures include both B&Q and Screwfix

UK sales
£4.34bn

UK operating profit
£271m

UK and Ireland stores
572

UK employees
27,047
(full-time only)



SWOT ANALYSIS KINGFISHER

KINGFISHER

STRENGTHS

- **Market leader** Kingfisher is the market leader in DIY retailing in Europe, via the dominant brands of B&Q in the UK and Castorama in France and Poland. It is the third largest DIY group in the world.
- **Management** Since becoming chief executive in January 2008, Ian Cheshire has given Kingfisher a strong sense of direction and delivered a step-change in operating performance, driving a strong recovery in UK profitability.
- **Synergies** In the past, Kingfisher did not have the structure and culture to maximise the opportunity to leverage its scale, but it is now fully focused on a comprehensive programme of direct sourcing of products and developing common brands across the group.
- **Strong cash flow** Kingfisher is cash generative and has a strong balance sheet, a function of its high operating profitability, strong working capital control and freehold property ownership.

WEAKNESSES

- **Vulnerable to external influences** DIY is a market whose underlying fortunes are very tied to activity in the housing market and the pressures on mortgage and credit availability make the outlook problematic.
- **China** The B&Q business in China is still not profitable and the business continues to struggle to find the right store format for the market.
- **Estate size** B&Q is a relatively mature business and, with so many big out-of-town stores, it may have to downsize its physical footprint as the DIY market becomes more multichannel.
- **Influence of weather** Seasonal outdoor products are an important business in the first half in northern Europe, particularly for B&Q, making Kingfisher exposed to the vagaries of the weather.

OPPORTUNITIES

- **Direct sourcing** The increasing proportion of direct sourcing will add considerably to gross margins, particularly as Kingfisher develops its global 'super-brands' in sectors such as gardening (Verve), outdoor leisure (Blooma), cooling (blyss), garden and power tools (MacAllister/Performance Power) and trade workwear (Site).
- **International expansion** Russia could be "the next Poland", in the sense that this small but fast growing chain of 19 stores (versus a target of 60) can mature into a highly profitable division for the group (such as Poland).
- **The 'trade' market** There is a good opportunity to grow the group's share of the 'trade' market, mainly via the fast-growing Screwfix chain in the UK and the well-established Brico Dépôt chain in France.
- **Product innovation** By focusing on product innovation and making the shopping process easier Kingfisher can grow its business.
- **Store format** Castorama is developing an attractive new store format, which focuses on stock availability and self-service, with DIY lesson workshops, elements of which have been transported to B&Q UK.

THREATS

- **Exchange rates** With most of its business overseas, Kingfisher is a natural beneficiary of sterling weakness in terms of the translation of non-UK earnings, but the recent strength of sterling (against the Euro and Polish zloty) has worked the other way, undermining group profits.
- **Risk of common product ranges** The push to develop common product ranges, in the quest for sourcing efficiencies, could back-fire if local consumer tastes and preferences get overlooked.
- **French economy** France is an important contributor to group earnings and though the Castorama business and the DIY market has been resilient, the near-term outlook for the French economy is not promising.
- **Competition** Kingfisher has significant DIY competitors in France and the UK, eg, Leroy Merlin, Wickes and Homebase, which could increase their differentiation and effectiveness and exploit any weakness in Kingfisher's operations.

Nick Bubb, Sept 14, 2012

KEY PEOPLE

Chairman

Daniel Bernard

Group chief executive

Ian Cheshire

Group finance director

Karen Witts

