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**REPORT FROM THE COMMISSION
TO THE EUROPEAN PARLIAMENT, THE COUNCIL, THE EUROPEAN
ECONOMIC AND SOCIAL COMMITTEE AND THE COMMITTEE OF THE
REGIONS**

**Retail market monitoring report
“Towards more efficient and fairer retail services in the internal market for 2020”**

SEC(2010)807

1. INTRODUCTION

This Commission report on retail market monitoring results from the work launched in early 2009 in line with the new market monitoring policy approach presented in the 2007 Communication on “A single market for 21st century Europe”¹. The retail sector was chosen for this market monitoring exercise because of its economic significance for the European Union (4.2% of the EU’s GDP, 17.4 million employees and 20% of European SMEs²), and, in particular, its close links with a multitude of upstream and downstream markets.

Retail services encompass a wide variety of forms (shops, electronic commerce, open markets, etc.), formats (from small shops to hypermarkets), products (food, non-food, prescription and over-the-counter drugs, etc.), legal structures (independent stores, franchises, integrated groups, etc.), locations (urban/rural, city centre/suburbs, etc.). The analysis in this report covers all these variants, with a particular focus on grocery retail services, given their economic importance³. This complexity cannot be reduced to a simple dichotomy between small shops and supermarket groups. Indeed, the strategy of the large retail groups over recent years has been one of diversification, from small neighbourhood or village shops to hypermarkets, by way of medium-sized stores such as supermarkets or discount stores. In this Report the term “retail services” is used for all these forms.

Based on an in-depth analysis, this report and the accompanying Commission staff working document present a first assessment of the issues affecting – or likely to affect – from an internal market perspective the economic, social and environmental performance (for example, in terms of innovation, competitiveness, productivity, employment, contribution to tackling poverty, social inclusion (of disabled people in particular), tackling climate change, and in terms of ethical and social responsibility) of companies active in the retail sector⁴. The identification of the issues raised in this report is based on the various economic principles and public interest objectives that are at the heart of the internal market in order to contribute to smart, sustainable and inclusive growth in the Union.

In the light of these conclusions, the Commission will, in a second phase and in the context of the relaunch of the internal market announced in the Europe 2020 Strategy⁵, define measures which could be taken to improve the smooth functioning of the Internal Market in this sector whilst respecting the principles of subsidiarity and proportionality as well as the other fundamental objectives of the European Union. The aim is to help companies operating in the retail sector of the EU to make the best use of the internal market freedoms in order to stimulate the growth of their

¹ COM(2007) 724 “A single market for 21st century Europe”.

² The retail service sector has 3 700 000 SMEs, compared to 2 300 000 in industry, or 63% more. Eurostat, SBS, 2005 and 2007. The “Small Business Act” for Europe (COM (2008)394 final) is a key element of European SME policy.

³ It represents around half of total retail sales. Euromonitor International 2007.

⁴ Explanations of the analyses in this report can be found in the Commission working document on retail services in the internal market, July 2010.

⁵ Communication from the Commission “EUROPE 2020 - A strategy for smart, sustainable and inclusive growth”.

services and promote innovation, whilst respecting the objectives of economic, social and territorial cohesion, together with worker, consumer and environmental protection. Retail services that are smart, sustainable and inclusive, henceforth defined as “fair”, can contribute directly to the success of the Europe 2020 Strategy.

2. THE HORIZONTAL NATURE OF RETAIL SERVICES

Retail services act as a link between a multitude of upstream and downstream markets, making it a key player in the European economy. In the downstream markets, retailers interact with consumers. To the extent that the retail sector determines consumers’ access to a wide choice of consumer goods, including basic household goods and groceries, the operation of the retail market has a direct impact on the quality of life of citizens. It is thanks to the services provided by retailers that many consumers have access locally to products from other Member States and third countries, thus benefitting in a very real way from the internal market. Retailers can become a driving force in the adoption of sustainable growth paths thanks to their responsiveness to consumer behaviour and their interaction with consumers. In the upstream markets, retailers often interact across borders with a wide range of players, in particular wholesalers and suppliers, employees, commercial property services, transport companies, logistics services, providers of payment systems, advertising and marketing agencies, security companies, energy suppliers, and waste collection and recycling services.

Any developments in the retail sector thus automatically have knock-on effects in other economic sectors and on their respective actors. Therefore, any policy response seeking to resolve an identified problem should take into account the horizontal nature of retail services by giving due consideration to potential impacts along the retail supply chain. It should be based on drawing a balance across the various economic freedoms and public interest objectives that are inherent to the smooth functioning of the Internal Market.

3. A RETAIL SERVICE GROWTH PATH THAT HAS GIVEN RISE TO SIGNIFICANT SPILL-OVER EFFECTS

The modernisation of the retail sector since the 1960s, with the dawn of retail groups, has contributed significantly to combating inflation. It has offered consumers, including during periods of economic downturn, greater choice at competitive prices allowing them to reallocate a growing share of their income, traditionally used for satisfying basic daily needs, to the consumption of an ever broader range of goods and services, which, in turn, has stimulated innovation and economic growth.

The search for and benefits of economies of scale and scope have transformed the business models of today’s retailers. Concentration across the borders of the internal market and vertical integration have jointly given certain retailers considerable negotiating power, allowing them to negotiate low prices. This bargaining power has, in turn, led to the European consolidation of manufacturing, logistics and commercial property service sectors, whose main players seek to attain equivalent flexibility and bargaining power in their respective supply chains in order to meet the demands of retailers. Even if European retailers have, at aggregate level, achieved lower productivity growth over the past decade than their counterparts in the United States,

their growth and the waves of horizontal and vertical integration have contributed to making the retail sector more efficient and to lowering inflation. Moreover, greater competition, in particular because of the rise of European discount stores and budget-price own brands, has reinforced this trend, ever pushing retailers to become even more efficient in order to curb the erosion of their margins.

Although this has increased competition, squeezed margins and increased competitiveness throughout supply chains, it has not been without impact on small independent shops, local authorities, small agricultural producers, small and medium sized manufacturers, employees and isolated or socially disadvantaged consumers. At times it has been to the detriment of the EU's objectives of environmental protection and social and territorial cohesion. Moreover, the analysis has found that the economic performance of the sector has not achieved its full potential in the EU, in particular from the internal market perspective. This report and the accompanying Commission staff working document highlight the various problems that have been identified as impeding, or likely to impede, optimum performance of the retail sector in the internal market, from the point of view of the various actors upstream and downstream of the supply chain: consumers, retailers, suppliers, employees and future generations.

4. MORE EFFICIENT AND FAIRER RETAIL SERVICES FOR CONSUMERS IN THE INTERNAL MARKET

An internal market for retail services which is more efficient and fairer for European consumers must offer them, wherever they live, access to the widest choice of retailers and high quality products at competitive and affordable prices, in accordance with the objectives of smart, sustainable and inclusive growth pursued by the EU. It must also offer access to reliable, transparent and comparable information on retail service offers throughout the EU, so that consumers can make better-informed choices, and have confidence that wherever they shop in the EU their consumer rights will be upheld.

The analysis identified the following problems:

The first concerns the accessibility and range of retail outlets. The proximity of shops offering essential goods and services, in particular grocery shops, is of growing importance to the elderly (17% of the EU population is already 64 or older) and disabled people (15% of the EU population), the socially isolated and those who live in sparsely populated areas, and those 9% of EU citizens who cannot afford a car⁶. The need to keep rural areas vibrant, to which aim local shops contribute, and to restrict the use of cars for environmental reasons will make this issue ever more pressing.

However, the number of small local grocery shops (with fewer than 10 employees) fell by 3.7% between 2004 and 2009. This trend is also being felt in other subsectors of the retail sector because of the increasing polarisation of sales outlets in either city centres or purpose-built out-of-town shopping centres. Moreover, consumer surveys⁷

⁶ Eurostat News release 77/2009, 28 May 2009, Living Conditions in the EU.

⁷ IPSOS consumer satisfaction survey, on behalf of the European Commission, 2008.

show that those living in towns with fewer than 10 000 inhabitants are less satisfied than average with the choice of shops to which they have access. It would appear that, despite initiatives in the Member States to control the growth of commercial retail development, the lack of territorial cohesion in this respect is worsening, although the recent trend for retail groups to establish small neighbourhood shops in towns and rural areas has mitigated this to some extent. Electronic commerce could help to counter the negative aspects of these trends and keep pressure on prices in both electronic commerce and shops, but, overall, its turnover is small, accounting for more than 2% of total retail service sales in just four Member States⁸ and on-line sales in the grocery retail sub-sector are even lower. How to improve access to shops and promote the development of electronic commerce in the EU are key questions. A detailed market study on price differences in electronic commerce has already been launched.

The analysis also highlighted considerable price differences within the internal market, suggesting that the internal market is still fragmented. For example, the price of food and non-alcoholic beverages is, on average, 28.4% higher in Belgium than in the Netherlands⁹. For certain common pharmaceutical products sold over the counter (OTC), the price difference can reach a factor of one to five¹⁰. In the clothing retail sector, it is surprising to note that prices in Ireland, France and the UK are below the EU average whilst those in the Czech Republic and Slovakia are considerably higher than average¹¹. Several factors such as differences in average household disposable income or VAT explain certain price differences, whilst other factors connected to competitiveness, the regulatory framework or commercial practices such as territorial supply constraints or obstacles to parallel trade¹², also play a role. The nature and respective weight of the factors explaining price differences, however, is difficult to define precisely. Furthermore, better consumer information on retail offers beyond their local shopping area, including offers in other countries, could also help to reduce these disparities.

National competition authorities and consumer associations have shown how retailers apply different prices across local shopping areas depending on the level of competition within those areas¹³. The finding that consumers are dissatisfied with the availability of sources of independent comparative information on retail offers reinforces this analysis. It appears that one of the reasons for this situation could well be the lack of growth of such services offering transparent, accessible, comparable, high quality information to consumers on retail service offerings beyond their own local and national market, in particular for electronic commerce.

The difficulties associated in offering such information services, whether commercial communications or independent information services, are central findings of this identified market malfunctioning.

⁸ Euromonitor International 2007.

⁹ For more information on the differences in food prices within the EU, see the Communication on “A better functioning food supply chain in Europe” (COM(2009)591 final).

¹⁰ IMS health, November 2009.

¹¹ Eurostat Statistics in focus 50/2009.

¹² See COM(2009) 591 final, quoted above.

¹³ UFC “Que Choisir” [Which?], 3 April 2008, and report of the UK Competition Commission, 30 April 2008.

5. MORE EFFICIENT AND FAIRER RETAIL SERVICES FOR OPERATORS IN THE INTERNAL MARKET

An internal market for retail services that is more efficient and fairer for EU retailers must allow those that are competitive, whatever their size, to coexist and grow on the market, in particular by way of innovative, efficient and sustainable strategies, notably by using its cross-border dimension. The analytical work carried out so far has identified a series of problems impeding the retail sector from exploiting its potential in the EU.

Firstly, major restrictions on entry to the retail market remain a subject of concern as they limit local competition and create obstacles to the achievement of the internal market for retail services. Some of them, such as bans on new outlets based on economic impacts on local competitors, are being done away with by the implementation of the Services Directive¹⁴. Nevertheless, current fragmented national, regional and local commercial planning frameworks, in conjunction with different rules on property and land ownership as well as a European commercial property development market which could give rise to malfunctioning at local level are other factors likely to dissuade parties from entering certain markets. In border areas – home to 35% of EU citizens¹⁵ – a lack of coordination between national legislations is particularly likely to distort competition. Certain Member States have developed good practices which could be applied in others. All the relevant public interest objectives must be taken into account, in particular the need to reconcile the interests of retailers with environmental protection or spatial planning (e.g. by maintaining sufficient access to shops offering essential goods and services).

Secondly, retailers sometimes mention the existence of obstacles to sourcing from companies established in other Member States. Such a situation could be explained, for example, by a decision on the part of a manufacturer to allocate customers to its various subsidiaries depending on their geographical location (intra-group decision). It could also be the result of contractual requirements imposed by producers on their wholesale or retail customers. If proven to exist, this phenomenon could help to explain the cross-border differences in price levels mentioned above. The capacity to engage in parallel importing is further restricted by different national regulatory frameworks, for example, on different language requirements for food labels¹⁶. Thirdly, despite European-level harmonisation of the rules governing commercial practices towards consumers, such as advertising, marketing and promotional practices¹⁷, certain remaining diverging national rules on commercial communications, in particular sales promotions, impede the development of efficient, and potentially cross-border, communication strategies by large retailers and by SMEs in border regions, electronic commerce, etc.¹⁸ In particular, selling and reselling at a loss are of importance for the economic models of retailers selling

¹⁴ Directive 2006/123/EC of 12 December 2006 on services in the internal market.

¹⁵ European Commission (DG Regio) Working Paper on Territories with Specific Geographical Features (02/2009).

¹⁶ Directive 2000/13/EC on the approximation of the laws of the Member states relating to labelling, presentation and advertising of foodstuffs. See also the proposal for a regulation of the European Parliament and of the Council on the provision of food information to consumers (COM(2008) 0040 final).

¹⁷ Directive 2005/29/EC of 11 May 2005 on unfair commercial practices.

¹⁸ Green Paper on Commercial Communications in the Internal Market (COM(1996) 192 final).

durable goods, notably textiles. Yet, the various national regulations imposing restrictions on selling at a loss, with the aim of protecting small retailers, appear to have not always been effective in this regard. Similarly, differing restrictions on sales periods have been criticised for leading to unfair competition between border regions.

Other identified problems include the continuing lack of a sufficiently competitive internal market in payment systems, the need for access to more efficient logistics networks and services and the coexistence of differing regulatory frameworks for: franchising, which may prevent the growth of purchasing networks of small retailers, consumer rights, shop opening hours or the collection and recycling of waste.

6. MORE EFFICIENT AND FAIRER RETAIL SERVICES FOR SUPPLIERS IN THE INTERNAL MARKET

An internal market for retail services that is more efficient and fairer for suppliers must allow them to sell products which are competitive in terms of price and quality and/or innovative in a sufficient quantity to make their investments worthwhile. It should provide suppliers with information on consumers' demand patterns so that they can adapt their supplies so as to better respond to changing needs and trends, in particular for more ethical products. It should thus promote an economy based on innovation which enhances efficient resource allocation, is greener and more competitive, encouraging economic, social and territorial cohesion. The analysis identified two problems preventing a transition to more efficient and fairer retail services for suppliers in the internal market:

Firstly, where they occur, tensions in the contractual relations between companies may curb suppliers' ability to make sufficient margins to make their businesses viable and to make necessary investment in product innovation. Certain contractual requirements applied directly by retailers or their central purchasing groups on their suppliers or by suppliers on primary producers could, in some circumstances, be considered unfair and likely to curb the growth and even the viability of certain competitive companies. On occasion, structural inefficiencies of intermediaries in the food supply chain could contribute to asymmetrical price transmission, price rigidity and unfair contractual conditions being imposed on primary producers¹⁹. Moreover, insufficient protection of branded product innovations against unfair practices such as slavish imitation could sap innovation in this sector.

Although certain national laws on unfair contractual terms between enterprises exist, they vary widely between Member States, which can lead to barriers fragmenting the internal market, distorting competition or increasing the risk of circumvention. In any event, the effectiveness of such rules is often curbed by the fear of retaliatory measures if infringements are reported. Relations between parties in the supply

¹⁹ Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions – Food prices in Europe (COM(2008) 0821 final).

chain, which can sometimes be unfair and unjust, are a policy problem for which the work of the Food Supply Chain Forum seeks to bring a first response²⁰.

Another important tool is the continued application of competition rules against anti-competitive practices which may affect the smooth functioning of the supply chain – to the detriment of consumers – and ensure fair competition conditions for all economic operators in the retail sector.

Secondly, even though the growth of quality control schemes and in particular accounting for social and environmental performance, is to be welcomed, small companies in particular cannot always afford to apply them due to their often national coverage, their proliferation, the lack of transparent and comparable information about them and their relatively high implementation costs. The absence of an independent frame of reference for such quality control schemes that would result in greater transparency and comparison across them whether for products and/or services, in particular their environmental and social criteria, are therefore key hindrances to achieving the potential of the internal market for retail services.

7. MORE EFFICIENT AND FAIRER RETAIL SERVICES FOR EMPLOYEES IN THE INTERNAL MARKET

An internal market in retail services which is more efficient and fairer for employees must help to improve both working conditions and productivity. As well as being one of the EU's main employers, the retail sector is often the entry point into the labour market for many young (30% of employees are under 30 years of age), low-skilled or unskilled people. The retail sector also relies heavily on part-time work (30% of its workforce) and is also the sector with the highest proportion of female employment (60%)²¹. Nevertheless, the analysis shows that a more efficient and fairer retail market is still sought by employees, for four main reasons.

Firstly, despite the minimum standards laid down in European law, labour law differs widely between Member States. These variations are compounded within Member States by sectoral collective agreements that can differ by type of shop, sub-sector of retail services or number and category of workers employed. This has led to different economic models in the retail sector. New entrants have often to adapt their existing business model to be able to compete with incumbents. The fierce price competition that tends to prevail in the retail sector implies that wage costs often come under pressure, and working hours are often difficult to reconcile with family life. However, certain retailers take a competitive stance by offering good working conditions, constructive social dialogue and training so that their staff remain loyal and effective in customer relations.

The second problem is linked to the informal economy which, although difficult to gauge, has a negative impact on working conditions in the retail sector, in particular in small and micro-enterprises, where effective enforcement of legislation and collective agreements is more difficult. While it is legitimate to want to reduce red

²⁰ Pursuant to the proposal made in the Communication on “A better functioning food supply chain in Europe” (COM(2009) 591 final).

²¹ Eurostat, Labour Force Survey 2007.

tape for small firms of this kind, it is also vital to ensure that they do not cut corners on working conditions, in particular as far as health and safety are concerned.

Thirdly, given the diversity of working conditions in the retail sector, it is often difficult for consumers to know about the social responsibility of particular retailers and thus to make an informed choice about where to shop.

Finally, whilst the retail sector's ability to absorb low-skilled workers is often emphasised as a positive characteristic, the associated down-side is that it may be more difficult for this sector to quickly adopt new technologies. The lack of ICT skills undermines the sector's productivity. The high proportion of SMEs in this sector renders it difficult for it to invest sufficiently in continuous vocational training.

Improving working conditions, combating the informal economy and maintaining employment levels and competitiveness by better matching the needs of retailers and the skills of workers are therefore major challenges.

8. MORE EFFICIENT AND FAIRER RETAIL SERVICES FOR FUTURE GENERATIONS IN THE INTERNAL MARKET

An internal market in retail services which is more efficient and fairer for future generations must also fully account for its environmental impacts. It must be a gateway to the offer of a wide range of more environmentally-friendly and/or fair trade products, allowing "fair" firms, including those based in non-EU countries, to gain access to the internal market. It must also be based on lower energy consumption and on efficient logistics and waste collection and recycling systems. Competition within the sector must not only be gauged on economic factors but also on social, ethical and environmental ones.

The retail sector has a significant environmental impact, as a result of both its day to day operations and the consumer travel that it generates. The retail sector requires a great deal of energy for shop lighting, refrigeration, heating/air conditioning, etc. It also generates and recovers significant amounts of waste (advertising flyers, packaging, food waste, electrical and electronic products). Insufficiencies and differences in collection and recycling systems are a problem. The sector also contributes considerably to the volume of commercial traffic. Most deliveries are still made by road, even though other forms of transport, such as inland waterways and rail, are starting to be used. Moreover, inefficient transport and delivery of goods in urban areas has a negative impact on congestion, pollution and quality of life. The delivery of goods in urban areas is a major constraint on the sustainable development of the retail sector. In line with the principle of subsidiarity and the respective competences of the European Union, the Member States as well as regional and local authorities, the Commission will examine how to design an integrated policy, encompassing the planning of urban mobility infrastructures, including the use of smart transport systems (ITS) and vehicles with innovative technology adapted to the needs and constraints of cities.

Furthermore, until recently, the environmental impact of retail, such as the societal costs generated by the CO₂ emissions associated with logistics, were not entirely incorporated into the sector's costs. Certain retailers are now trying, at times thanks to incentive measures, to meet some of the afore-mentioned goals by reducing the

external impact of their activities. The lack of common rules and a European-level method of analysing the lifecycle of products so as to measure their environmental impact remains a problem. On this last point, insufficient coordination at European level of national initiatives could lead to the risk of further fragmentation of the internal market²².

9. CONCLUSIONS AND NEXT STEPS

This report has identified, on the basis of a thorough analysis performed by the Commission in consultation with all the stakeholders in this area, a certain number of problems having – or likely to have – a direct impact on the performance of the retail sector, from an economic, social or environmental point of view, the resolution of which could help the sector to navigate the transition towards a more efficient and fairer internal market in retail services.

1) The following problems were identified as affecting – or having the potential to affect – the performance of retailers in terms of accessibility (lack of cohesion between the location of shops compared to existing home locations and means of transport) for all EU citizens to a varied range of competitive retail services respecting the requirements of sustainable development:

- a lack of efficiency and diversity across commercial planning rules together with malfunctioning of the commercial property market have an adverse impact on where retailers choose to establish shops and accessibility for consumers;
- insufficient development of electronic commerce in the internal market, as a result of a series of obstacles (cross-border postal services, means of payment, poorly functioning systems of redress, etc.);
- underdevelopment of commercial communications and independent information services (for example, internet price comparison sites, including cross-border ones, or comparative tests of products and services) probably resulting from persisting differences across national consumer protection and unfair competition rules and from difficulties in comparing across quality control systems for goods and services and their respective environmental or social criteria.

2) The following problems have been identified as hampering, or likely to hamper, the optimum growth of operators, in particular their ability to invest and innovate with regard to the quality of products and services offered:

- a lack of rules governing unfair commercial practices and contractual relations between the various parties in the supply chain and/or poor application of the rules where they do exist;
- a lack of transparency of quality control systems and associated difficulties in their crossborder use.

²² The retail forum created by the European Commission in 2009 aims to reduce the ecological footprint and disseminate good environment practices in the retail supply chain.

3) The following problems have been identified as affecting working conditions, labour productivity, employment levels and competitiveness in the retail sector:

- differences in working conditions caused by differences in labour law and collective agreements applicable to retail services;
- the negative impact of the informal economy on working conditions;
- a lack of consumer information on the social responsibility of retail service companies;
- a mismatch between the skills needs of companies and those of staff in the retail sector.

4) The following problems have been identified as having the potential to impede the transition to a more sustainable retail sector:

- high energy consumption, considerable levels of waste production, significant contribution to commercial traffic flows and congestion in urban areas;
- insufficient consideration of environmental costs in the retail supply chain (logistics, energy efficiency of shops, marketing and communications, etc.), in particular where sufficient incentives are not made available;
- lack of a common life-cycle methodology for evaluating the environmental impact of products and services sold.

Measures to respond appropriately to these problems and European policies which could be launched as a consequence will be presented in the Commission Communication on relaunching the internal market, planned for the autumn of 2010. Given the horizontal nature of the retail sector, any resulting measures will take the fullest account possible – in their design, in the consultative/negotiation processes that will be used for their adoption and in their subsequent application – of all the various objectives of the Treaties, while fully respecting the principles of subsidiarity and proportionality.

The Commission calls on all interested parties to submit their responses to this report by 10 September 2010, to the following address:

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