Paris, 6th March 2023

ANNOUNCEMENT

Private labels: the future of luxury department stores?

Research suggests that moving upmarket their private labels could be a way for department stores to kill two birds with one stone: increase profitability and recognition in the eyes of customers. Thanks to business rationalization and the ability to deal with CSR complexity, tapping into the competitive advantages of private labels could be a strategic move for the department store's business model.

On average, the private label business represented 16% of total IADS members' turnover in 2022, up from 9% in 2019. This increase stems from the pre-pandemic efforts to improve this product category, and the impact of Covid-19, which nudged price-conscious customers to switch from national brands to private labels.

Aware that this part of their business could be improved and can contribute to regaining productivity points, IADS members constantly re-evaluate their private labels: **El Corte Inglés** reduced the total number of labels with the ambition to transform them into brands (**Sfera** and **UNIT** in the young fashion segment are good examples), **El Palacio de Hierro** launched a 5-year plan combining brand recognition ambitions and new organisation, while **Galeries Lafayette** and **Manor** doubled down on targeting specific categories (for instance, the home category, or mono-product segments such as cashmere or men's shirts).

Although there is no one-size-fits-all strategy or internal organisation, all companies pursue the same goals: review their business organisation, move towards more sustainability, revise price points to improve margins, and contribute to the retailer's brand recognition. This is why the IADS dedicated its 2022 Academy research program to this strategic topic, as private labels are key in department stores' economic equation.

Private labels' supply chain objectives: deliver, de-risk, re-deploy… and dilemmas

Last year, the IADS identified the supply chain as the most critical topic for private labels. 2022 brought a number of new uncertainties (war in Ukraine, energy shortage, Covid-19 impact in China…), resulting in a longer production lead time. As a result, late deliveries were an issue for the Spring-Summer season, for instance, some companies only received 70% of their expected stock by March 2022 compared to 90% in 2019. The answers were swift: materials were pre-booked well in advance, production planning started earlier (which saved 2 months on the overall schedule), and reliance on Chinese suppliers was reduced, sometimes by up to 6%, in favour of Southeast Asian countries (+6%) and the Euromed zone (+1.5%).

Interestingly, nearshoring redeployment in the Euromed zone remains shy. Taking into account production and shipping, delays are reduced by up to 8 weeks, which considerably improves operations. However, this comes at a price: production costs can vary by as much as +3% when switching from China to Euromed, while they can decrease by -4 to -8% in other Southeast Asian countries. Given the rise in the cost of materials, additional product costs obviously raise the question of the retail price point and how much customers are ready to pay for these brands.

Sustainability and private labels: the compliance complexity

In Europe, the constant and complex changes in regulation add costly difficulties to the compliance process. As shown in France with the AGEC law (anti-waste and circularity law), enforced since the 1st of January 2023, providing transparency and traceability is really complex, and this affects private labels in the same manner as international brands.

For all members, the goal is to pursue already engaged sustainable efforts and increase the share of sustainable products, knowing that reaching full transparency is the biggest challenge and expectation from customers. The ambition is to reach 100% sustainable collections by 2024 or 2025 (**Go for Good** already accounts for 68% of **Galeries Lafayette's** private label products), while also pursuing other structural efforts, such as reducing the amount of packaging used.

When it comes to social compliance, it is all about auditing, de-risking and teaming up: **Breuninger** helps its suppliers become 'BSCI-compliant' (Business Social Compliance Initiative), while **Galeries Lafayette** audits its suppliers' production facilities and teams up with third parties such as Emmaüs.

In any case, finding the right way to clearly communicate sustainable and social efforts as well as legal information remains a headache. Initiatives such as QR codes tagged on each product and linking to the website are on the way, however, once again, all these efforts come at a price when it comes to production costs.

Raising the price point: an obligation, or a strategic choice?

In order to maintain viable margins, private labels retail prices increased in line with the general price inflation. However, this opened the debate of going premium to be able to justify a new price point. Across the board, motivation is different: some department stores see it as a way to compete with some international brands, while others are pre-empting the high-quality basics segment. In the US, **Target** is a good example of this strategy, as the price is no longer the primary factor for customers when buying private labels, but rather quality and value for money. In addition, the IADS Academy's research argues in favour of brand premiumization by showing that high discount rates did not improve sell-through. In other words, price point is not a sales argument for private labels as important as initially believed. As a matter of fact, among the IADS members' private labels roster, it appears that the ones with the highest gross margins have better sell-through rates.

The debate remains open, as many questions around private labels still need to be answered: how can the price limit be gauged? Is premiumization a question of upgrading the brand itself, or targeting a new audience? How can retailers create a strong brand identity that can co-exist with the overall company brand without dedicating too much overhead and resources? Indeed, unlike **Marks & Spencer**, one of the business cases analysed by the IADS Academy, not all department stores have a namesake private label brand. Also, in the case of Target, promoting awareness of its private labels usually goes hand-in-hand with opening shop-in-shops and conducting advertising campaigns, which can prove to be very costly, and risky.

Conclusion: private labels have everything department stores need to keep going and growing

Since Covid, supply chain disruptions have continuously impacted the private label business. After dealing with the cost increase for raw materials and transportation, most members are now trying to anticipate production lead time and favour near-importing to reduce their dependence on Chinese suppliers. Such a major shift implied increased costs, and by extension, increased retail prices.

While the efforts in CSR are continuing, they create an additional and major extra value to the private labels supporting brand awareness and attracting customers. Going further, the IADS Academy's overarching theme centred around the importance of transforming private labels into real, independent brands. Department stores have a reputation and resources, so they benefit from competitive advantages provided they are able to overcome internal price resistance, (based on the traditional belief that private labels are competing on low price points), and, by extension, align priorities, investments and scale across all departments (general management, private label teams, merchandising and marketing departments, stores and space allocation).

Despite the difficulties private labels are facing, they have a generous margin level when compared to other business models that can be found in department stores. For that reason, **private labels remain a key competitive advantage** that could prove to be very profitable provided they receive the right amount of investments and attention.

About IADS

The IADS is the only expert platform dedicated to the department store format in the world. Its uniqueness lies in the close relationships between its member CEOs and organisations, making it a very powerful asset for decision-making at the highest level.

Today, the Association gathers leading department stores around the world, all key players in their respective markets, and represents more than €26bn cumulated annual turnover, achieved through more than 360 stores with 190,000 associates in 19 countries.

Its permanent members include Centro Beco (Venezuela), Beijing Hualian Group (PRC), Breuninger (Germany), El Corte Inglés (Spain), El Palacio de Hierro (Mexico), Galeries Lafayette (France), Lifestyle International Holding (Hong Kong), Magasin du Nord (Denmark), Manor (Switzerland), SM (Philippines), The Mall Group (Thailand), and close ties are also knitted with other companies.

The wide variety of business models and cultures represented provide the Association and its members with a richness in the exchange which is valuable for the solutions and thought-provoking debates that it generates. The Association is also very close to its members' business questions and issues and actively contributes to problem-solving processes, which makes it a truly unique format in the retail association world.

About the IADS Academy

The IADS Academy programme, a 27-year-old tailor-made mentoring workshop open to our members' high potentials only, promotes cooperation and future orientation. Over the years, the IADS Academy has trained 180+ executives from 28 companies in 21 countries, some of whom reached top positions in member and non-member companies (within IADS members, 4 CEOs, and outside the Association, 2 CEOs and 2 COOs in 2023).

Press Contact: IADS, Christine Montard, press@iads.org, +33 6 45 47 45 14