

Wal-Mart's founder Sam Walton once said: "Most of the values and the rules and the techniques we've relied on have stayed the same the whole way. Some of them are such simple common-sense old favourites that they hardly seem worth mentioning."

ALDI founders Karl and Theo Albrecht would have agreed with Sam Walton on this - and many other core principles and techniques. Sam was obsessed with detail. So were the Albrecht brothers. At Wal-Mart they say: 'We are different'; ALDI says much the same. Sam Walton declared 'we think small' and referred to his 'simplicity concept'. Simplicity is one of ALDI's guiding principles too. Wal-Mart makes a habit of trying things out to see if they work; trial and error is the ALDI way too. Sam Walton and his managers knew that there is no magic formula for success, but that numerous small things

contribute to it. ALDI shares this conviction: retail is detail: paying attention to all the success factors over decades. That is the art, and that is no secret.

Finally, Sam Walton had one guiding principle: "I'm sure you're sick to death of it," he said. "But I'm going to say it again and again anyway: the secret of successful retailing is give the customer what they want." ALDI concurs with this guiding principle, 100%. But there is one way in which ALDI and Wal-Mart are poles apart.

Wal-Mart offers customers everything they want to find under one roof at low prices. ALDI offers only a very limited range. Consider these numbers:

- ALDI sells 700 items, generating a turnover of US\$44 billion
- Wal-Mart sells 100,000 items, generating a turnover of US\$300 billion

Is ALDI really that special?

OVERVIEW

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Hard discounters represent a major challenge to Europe's mainstream retailers and manufacturers. But many still fail to understand the secrets of their success

This translates into:
ALDI turnover per item: US\$63 million
Wal-Mart turnover per item: US\$3 million.

Every single one of ALDI's items generates high volumes of sales. Many of Wal-Mart's do too. But many other Wal-Mart items sell at a much lower rate. The similarity of ALDI's sales profile creates simplicity; Wal-Mart's diversity creates complexity. This results in completely different strategies, organizations and cost structures. As we'll see, even the most astute business commentators still underestimate the importance of this difference. But first, let's revisit ALDI's guiding principles.

What makes ALDI tick?

ALDI was born out of a poverty regime of post-war Germany when hard times and enforced frugality demanded the avoidance of waste. The end result of this 'poverty regime' was the ALDI concept. This was not a sudden invention. Albert Einstein once described his way of working as 'I grope my way forwards'. That's what Karl and Theo Albrecht did too. They literally groped their way forward to their sales system, which can be summarized by these five points:

- a limited product range,
- goods which reflect basic consumer needs,
- easily handled goods in terms of

- operational requirements,
- best possible qualities - measured against leading brands
- the lowest possible sales prices.

A limited product range

ALDI's success is the success of setting voluntary limits. For decades ALDI North kept its product range down to 600 items. At present this figure has presumably grown to 700. ALDI South today still sells 650 items.

Formerly, ALDI only sold items in what is called the dry product range. Refrigeration or special handling were not necessary. Today, the equipment and logistics necessary for refrigerated and frozen goods present no problems. The personnel do not require any special background knowledge about ALDI products either.

When you have just 600 items, each item is an individual and can be treated as such by everyone all the way up to the top management. "People know" each individual item personally when there are only 600. Even starting from 2,000, and certainly when the range goes up to 20,000 items, managers at other retailers must resort to blunt instruments of quality assurance and product range control. All business systems, the organization, communication, even the scope and type of business of meetings are

There is no magic formula of success, but numerous small things contribute to it – paying attention to small details over decades.

determined by the number of items in the product range. Even Tengelmann with some 15,000 items must do nearly everything differently than ALDI. This cardinal difference has not been properly appreciated, even by business economists.

ALDI's limited number of items enables it to profit from those consumers who like their products simpler, more durable, cheaper and plain, and who are tired of being confronted with new products. The enormous variety of products on offer today is quite a burden for customers. Today, many customers are glad on occasion to do without the enormous selection, if they can be sure that the spontaneous choice from the shelf is a sensible one. ALDI relieves its customers.

Focusing on basic consumer needs

Ultimately in retailing, success is not decided by 'buying power' and purchasing expertise. It is decided by marketing: the ability to truly focus on customer needs. If investment in purchased inventory (i.e. if the value of purchased goods, the purchase price), is seen as a cost factor, then it is by far the largest cost category in retailing. 60 to 80 percent is very common. But it would be wrong for companies to conclude they have made a decisive contribution towards business success if they secure respectable purchasing prices.

ALDI's success is not based on purchasing - as many competitors believe - but on sales, on sales and close-to-customer policies: ALDI does not always get the best purchase prices in comparison with its competitors.

Too many companies give too little thought to core questions. More important than the question of purchase prices is something else:

*"Why should customers shop in my store?
Why should the customer select my product?"*

This question - the core question for all marketing and corporate strategy - applies in all companies and institutions, from carmakers to hotel chains to symphony orchestras. It is simply a question of strategic direction, of a company's concept.

However, many companies content themselves with vaguely worded statements such as "we want to offer good products at reasonable prices", which is not an adequate answer. Many more companies indulge in all sorts of activities and practices which have nothing really to do with customer demand. Take the attempt to tempt customers with special discounts.

Purchasers and vendors meet and work out their annual programs.

The enormous variety of products on offer today is quite a burden for customers. Today, many customers don't want enormous selections.

Producers want to boost one item in particular, and retailers comply in exchange for a special payment. Or else, if a vendor wants to place a new item on retail shelves, he must come up with something imaginative to get retailers' approval. Since retailers are always in need of money, they demand that manufacturers pay a certain sum to get their item listed. Since retailers support this item in a number of ways - they present it on their shelves - money must be paid. These amounts are then put into the funds for outstanding achievements of the purchasers. How can they prove how successful they were? Whether any specific purchasing price can be called a success is anybody's guess. Perhaps too much was paid. But if the purchaser by the end of the year has saved up a nice pile of money, then it is a success. Such sums are even included in the annual budgets. But the advertising expense benefits reveal nothing about whether the purchase price is generally "appropriate". And of course the vendors include such extras in their budgets in advance.

Retailers' lack of real customer focus shows up time and time again in the many ways they seek to compensate for their own lack of conceptual creativity. Some examples are: manufacturers being required to pay contributions to make sure that an item already in the product

range will not be eliminated; manufacturers paying if they want a new item put on the shelves; and sales interruption remuneration. If non-delivery or late delivery (missing items in the shops) cause sales losses, compensation is claimed. But since the causal relationship is very difficult to prove and quantify, retailers go so far as to demand lump payments as compensation. That's on top of conventional discounts such as cash payment discount, quantity-related discount, campaign discounts, promotional bonus, media-related remuneration and so on. Thus, despite what is called the demand power of retailers, the retailers become the sales departments of the manufacturers.

The consequences of such a retail policy are simple:

- High advertising expense benefit + weak mission = modest success
- Low advertising expense benefit + strong mission = major success

But manufacturers aren't much better. They feel compelled to give in to retailers, afraid that they might lose their business contact. But the real reason is that often their products are similar to the point of being interchangeable, and the use value they have for the consumer is not very distinctive. In short, they have failed to answer the basic question: 'why should

Retailers' lack of real customer focus shows in the ways they compensate for their lack of creativity, via listing fees and over-riders for example.

the retailer have this product on his shelves?' All this is a product of poor leadership and organization, and poor use of employee creativity.

Another example of this general lack of any overview is aggressive manufacturer promotional campaigns whose shop displays and eye-catchers clash with the store's layout and upset business organization, quite apart from the usual over-supply of items which, after the campaign, end up in the store's back rooms or are somehow squeezed onto the regular shelves. Such developments - which have continued for decades - result from mistaken ideas about what the real success factors in retailing are, and these have also led repeatedly to mistaken "explanations" of ALDI's legendary success.

ALDI does not pursue this sort of "discount policy". The purchase price is stated as net/net - after subtracting all the discounts which have no interest whatsoever for the purchaser. ALDI buyers concentrate on essentials, specifically, their customer needs, on their company's most immediate mission. Vendor conditions do not play any role at all in the product range strategy (while at ALDI's vendor-oriented competitors this is often the only "strategy" they have).

Of course all drive hard bargains. But what most experts mean by "purchaser power" is in fact "vendor power": the ability to achieve high sales figures. Vendor power is not the result of purchaser power, although purchaser power in this context can provide support. The main factors of purchaser power are different: sales concept, products, qualities, prices, locations, marketing.

Easily handled goods

It is often argued that "sales psychology" is the basis for ALDI's decisions regarding merchandise placement. The interiors are kept so simple on purpose simply to create the illusion of being cost conscious. This is wrong. ALDI does not focus on appearances. ALDI's focus is on costs and, in addition, making the customer an honest offer, without any "show". Customers are not supposed to believe ALDI is low-price. ALDI is low-price. The purpose is not to suggest this. It is a fact which customers experience when they themselves compare prices. Decorating the interior of an ALDI store involves no other criterion than the use of purposeful, durable and low-cost materials. Shelves, lanes, and - if possible - even the length and width of the store itself should be determined solely in terms of logistics (box size, pallet size, the maneuvering space needs for forklifts and similar matters).

Vendor conditions play no role in ALDI's product range strategy. For many competitors vendor conditions are the only 'sales' strategy they have.

In retailing it is common to place high-price items or items with larger margins at eye-level, or the poorly calculated items like sugar down low so that it is difficult for customers to pick them or even to find them. At ALDI, on the other hand, merchandise is placed on shelves and pallets in the stores solely in response to logistic considerations. Appearance is not a factor. In the framework of finely tuned ordering procedures, shelf space and position are determined by weekly needs, item characteristics and delivery frequency.

For ALDI, rational sales are more than a mere slogan. When you enter an ALDI market you can see what it means. Sugar, flour, beverages, milk, laundry detergent and other items are presented for sale, untouched, on the same machine-loaded pallets as they were shipped out by the manufacturer. All the other items are put on pallet once and moved to their position in the store. At that point it is usually just a matter of opening the box and the merchandise is ready for sale. None of ALDI's employees need to unpack individual packages or decorations. ALDI did not introduce refrigerated items, for example, until the refrigerator cases and the cardboard boxes matched its requirements. The cases had to have enormous capacity and boxes had to be the right size so that they could be placed

neatly into the cases without any wasted, leftover space.

The ordering procedure itself is the simplest one imaginable. As at Toyota and other Japanese manufacturers who use kanban systems it is based on: "If it leaves, replace it."

Quality comes first

ALDI always strives for lower costs, but never at the expense of quality. Everything ALDI sells is benchmarked against leading branded products. As a principle, when different qualities are involved, purchase price differences are not the sole factor in the decision-making process. A higher purchase price is accepted for higher quality.

Nearly 95 percent of all the items on ALDI's shelves are private-label, which however are often made by well-known brand makers such as Bahlsen, De Beukelaer, Blendax, Trumppf, Nestlé or Unilever. No one else has pursued this policy so fanatically. Vendors know the ALDI quality requirements. They must meet them. The best raw materials and excellent processing are expected. Since the vendors do not have long-term contracts, ALDI can also immediately terminate business relationships without the need for interminable legal wrangles. Nevertheless, ALDI has rarely proceeded

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so strictly that a vendor's existence was endangered. This is why ALDI is not interested in making vendors dependent on its order quantities. Often an additional vendor is tapped in advance.

Private labels require confident, knowledgeable consumers: quality and price as rational arguments against the irrational "brand" idea. ALDI customers do not need labels to boost their feelings of personal adequacy. Consumers are very well capable of judging quality themselves, independent of brand advertising campaigns. Product value has the priority.

There is hardly a competitor of ALDI who carries out such extensive quality controls, at least in the course of my professional life. When it comes to freshness, ALDI can hardly be beat. Its rapid transport and distribution system makes it practically impossible for competitors to offer fresher wares. Reliable, uniformly perfect quality was and remains decisive for ALDI's success - more important than any specific distribution system. A distribution system can be watched, analyzed and copied. Such a fanatic and no-compromise quality policy, however, requires a specific corporate culture and this requires people who think, feel and act accordingly.

The lowest prices anywhere

Of course the company's basic principle is to sell products at prices lower than anywhere else, in contrast with many other retailers whose goal is to get the highest possible prices without endangering the company's competitiveness. This pays in terms of the company's standing in the eyes of the customers.

No one disputes the fact that ALDI sets prices in the food retail trade. The market price is determined by ALDI. If the purchase price drops, ALDI nearly automatically lowers its sales price. ALDI achieves its best values for prices by cost cutting in all areas - with the exception of wages and salaries which generally are among the highest but, due to the high productivity of staff, generate the lowest personnel costs. Higher wages are as much a part of 'lower cost' as anything else: creating a low cost structure depends on the extent to which the company's management and its employees are prepared to and capable of working on details.

ALDI is also never stiff-necked or short-sighted in its quest to reduce costs. For example, it never gave an "order" to reduce cost category X by a certain percentage. Cost reduction was never forced. The basic ideas of value analysis

A distribution system can be copied. But ALDI's fanatic quality policy requires a specific corporate culture and people who feel and act accordingly.

play more of a role. When value analyses are conducted certain business units or cost units are examined against the background of their significance or necessity for business operations. What is not needed can be eliminated. The yardstick for cost management must always be the strategy of the company. Caution must be urged against cutting off the "strategic branch" on which you are sitting. If, for example, customer assistance is one of the company's important strategic approaches, then any personnel cuts in this area must be carefully thought-out. In recent years department stores have faced this predicament: cut high personnel costs to the detriment of customer assistance? ALDI also faces these dilemmas: how to avoid long lines at the cash registers when these lines are frequently only temporary?

Dealing with vendors: consistent and fair

ALDI could not have achieved its current success without close working relationships with its suppliers. So how do ALDI's five guiding principles translate into the way it manages supplier relationships?

In contrast to a view often expressed in the trade, ALDI does not conclude any long-term agreements with vendors as a

matter of principle. Many believed ALDI would sign such agreements to bind vendors and somehow suck them dry. Wrong. For ALDI the only thing that counts is that vendors continuously supply high qualities, and of course, the prices must also always be competitive.

If anything is below par, there are very simple sanctions. The vendor who previously supplied, say, 20 distribution centers of an ALDI Group, loses perhaps 5 centers. Only in extreme cases - and these all involve quality-related questions - does he lose them all. This principle of distribution center allocation also enables ALDI to test out new vendors and expand their ordering.

Nor is there any intention of making any vendor completely or even substantially dependent on ALDI. This may seem like a good idea: it means the retailer can exercise greater influence on vendors or depress their prices. But this would also make ALDI dependent on fluctuations in quality, internal problems of all kinds in the vendor's business up to and including capacity breakdowns. Even a collapse caused by the vendor himself could easily be blamed publicly on ALDI. Under these circumstances it is essential to make use of an intelligent alternative.

For retailers it is basically more interesting if the vendor market is made

Many companies indulge in all sorts of activities and practices which have nothing to do with customer demand. Special discounts, for example.

up of a large number and variety of companies. Each company can only exist over the long term if their profit margins are wide enough, so it simply does not make any sense to drive a partner into insolvency or - one step in that direction - to kill his appetite for business. This has been one of the most important issues on the agenda between manufacturers and retailers for many years. Here too, ALDI has had a positive impact, in addition to its inflation-braking effect on the economy.

The company is a fair partner:

- A price - once it has been agreed to - is not open to 're-adjustments'
- No discounts are demanded afterwards
- No unjustified complaints are made
- Vendors are not 'sucked dry'.

Improved and more successful negotiations

A number of ideas can be deduced from ALDI's relationships with its vendors for generally improved relations between retailers and manufacturers. The current negotiating practices could be loosened up and focus more on the facts. Putting on the pressure and playing poker are not the best approaches if people want to continue working together in the future. A good guideline for successful negotiating is offered by the Harvard Concept whose most important principle is that negotiations are successful when both

partners would like to continue to engage in business in the future as well.

The points I have listed below are from my experience the most important for successful negotiations with vendors:

- Drop what is known as the annual conferences. The end of the year is an accidental and random date. Issues should be handled as they arise and negotiations should not have to start under the pressure of a deadline. Manufacturers and retailers could agree to periodic meetings for specific product categories.
- In fact, every "annual conference" is a strategic conference. The purchaser holds discussions autonomously, bearing sole responsibility for their outcome once management and purchasing have defined their strategic and tactical positions. He makes the final decision alone.
- Purchasers must not be given target margins before they enter negotiations, but rather conceptual ideas (e.g. replacement of vendors, items or similar matters). A clear distinction must first be made between concepts and conditions.
- Nearly every vendor's sales can be increased by 20 to 50 percent. The question is whether this is really wanted and how to go about it. At issue are the concepts, alternatives and options.

It simply does not make any sense to drive a supplier into insolvency or – one step in that direction – to kill his appetite for business.

**Top of the list of cultural values at ALDI is asceticism. Doing without.
Here is an ALDI doing-without checklist.**

- ✓ 1. No staff to relieve management of intellectual work
- ✓ 2. No controlling department to provide direction
- ✓ 3. No external market research
- ✓ 4. No work with management consultants
- ✓ 5. No budget forecasts
- ✓ 6. No scientifically cleaned statistics that reveal all
- ✓ 7. No scientific analysis techniques for all questions related to supplying the market
- ✓ 8. No customer surveys
- ✓ 9. No ISO 9000 or TQM
- ✓ 10. No sophisticated system of terms and conditions to squeeze supplier prices
- ✓ 11. No differentiated price policy by sales area or store area
- ✓ 12. No differentiated product mix from store to store
- ✓ 13. No complicated calculation methods for setting prices
- ✓ 14. No games involving qualities to optimise profits
- ✓ 15. No highly complicated engineering for logistics
- ✓ 16. No product placement in stores based on psychological analysis of shopper behaviour
- ✓ 17. No luxury in the offices, no top-of-the-range company cars
- ✓ 18. No public appearances
- ✓ 19. No publicity
- ✓ 20. No acceptance of gifts from suppliers
- ✓ 21. No acceptance of invitations to dinner from suppliers

Asceticism – or doing without – is the most important core characteristic of ALDI. It is top of the list of cultural values. It goes with simplicity.

- Sales always have priority ahead of margins. It is familiar knowledge that costs and profit, in the end, can only be covered by margins. But the basis of any business with a customer is sales. The main thought of the purchaser and vendor must focus on the interests of the customer, the consumer - anything else is short-sighted.
- Purchaser, vendor and conditions must never be allowed to determine the product range.
- Conditions must not lead to pressure on volumes and quantities. The principle must be: the customer (who moreover makes his own selection) makes up his own mind. Quantity scales and discount rates rarely make sense.
- No agreements should be reached which, at a later date, can only be adhered to by turning them inside out.
- Find logistics cooperation and rationalization models. ECR Europe can be a source of ideas.

Long before an item is on the shelf in an ALDI market, the course is plotted to obtain the best prices for enormous quantities. Negotiations are conducted which go beyond the usual limits of procurement negotiations. The goal is to realize a conception which is appropriate for ALDI's large-scale purchases. Because ALDI purchasers want more than to get a good price. Their goal is to conclude

contracts in such a way that the incidental effects can be turned into purchase advantages. The ways and means of doing this are many:

- A manufacturer with long-term, major orders, can be encouraged to modernize his production lines, to rationalize the manufacturing process.
- Elsewhere a vendor who sells most of his production to ALDI is convinced to drop advertising, on condition of a guarantee of purchase.
- But also less significant agreements - such as the agreement that deliveries can always take place in full trailers - make for additional purchase advantages.

So it is not the purchasing conditions alone which determine ALDI's relations with its vendors. A company which produces private labels needs the confidence of the contractor. This is usually developed over years of business interaction. In the beginning, however, there is of course always a sort of "coaching" by ALDI. This involves good quality levels and their precise definition, package designs and sizes, as well as questions related to the vendor's capacity, his ability to assure hygienic and reliable production processes.

Many new vendors already know what ALDI expects. They ask colleagues and

Negotiations should focus on facts. Playing poker and putting on pressure is no good if people want to continue working together in the future.

they prepare themselves for a completely different sort of business relationship than is otherwise customary in the trade. One really important point remains - and all ALDI vendors will confirm this: renegotiations during which attempts are made to upgrade conditions for deliveries which have already been made do not occur. ALDI is interested in the continued existence of their capable vendors. The relationships in these cases are nearly symbiotic. But to some competitors thoughts like these are foreign.

Summary

Companies should be capable of developing their own business principles in line with their own cultures. ALDI has succeeded in doing this. Although ALDI kept an eye on the competition, the competition was never a source of “benchmarks” for ALDI’s own practice. ALDI has always set its own course. Many specific elements of ALDI’s business model can be copied. But there is one thing that others find very hard to copy: a fanatical and no-compromise corporate culture focused on consumer value and supported by people who think, feel and act accordingly.

Further reading

This article is an edited extract from the author’s book *Bare Essentials: the ALDI way to retail success*, Cyan/Campus, 2004

ALDI always set its own course. Many specific elements of ALDI’s business model can be copied. But its fanatical corporate culture cannot.