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Large Retailers' Financial Services

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Abstract

Over the last few years, large retailers offering financial services have considerably grown in the financial services sector. Retailers are increasing the wideness and complexity of their offer of financial services. Large retail companies provide financial services to their customers following different strategic ways.

The provision of financial services in the retailers offer is implemented in several different ways related to the strategies, the structures and the degree of financial know-how of the large retailers involved.

Keywords: Large Retailers; Financial Services; Retailing; Supply Models; Global Competition

1. Financial Services and Large Retailers

The retail food market in most developed countries is characterized by hyper-competition and is dominated by a small number of large retailers. Many large retailers have developed extensive customer relationships and have improved their offer by introduction of services with high-added value for customers (Brondoni, 2005; Riboldazzi, 2005). Big retailers are developing different strategies to cope with increasing competition in the merchandise sector and they invest in services innovation, opening their shops to different services which are often not linked to their main activity (Pepe, 2003, 2006). Additionally, over the years, big food retailers have indulged in various diversifications and they have often enlarged successfully these activities.

In particular, during the last decade, the largest retailers have introduced financial services in their offer to face hyper-competition in the retail market and to improve their relationships with customers. To achieve this retailers have exploited different strategies all based on the interaction between retailers and traditional financial companies.

The financial services sector is becoming more competitive. Many companies from different business sectors have entered the market, increasing the level and type of competition. Further, the deregulation in payment system (Payment Services Directive 2007/64/EC) has contributed to opening the financial services

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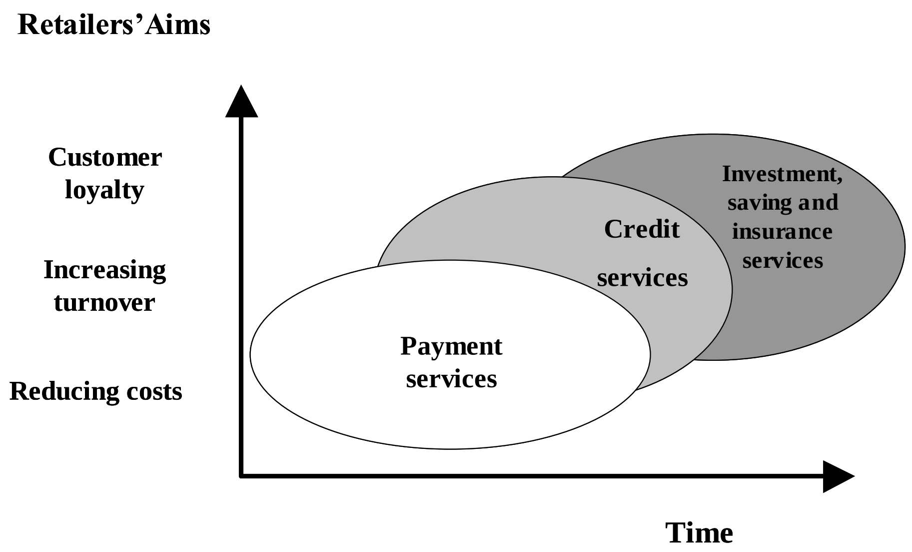
market to newcomers. In particular, among the newcomers, large food retailers seem to possess some special characteristics (Golinelli, 2005; Martinelli and Sparks, 1999; Alexander and Colgate, 2000), enabling them to play a major role in financial services provision. For retailers, in fact, the offer of financial services may provide the opportunity to improve margins (Worthington, 1994), to increase turnover and to build closer relationships with customers.

The evolution of the range of financial services offered by retailers follows a similar path for each different cases (Dafsa, 1995; Gaëlle and Soudan, 1999). At first, retailers offer financial services to safeguard profit reducing operating costs of the payments by debit and credit cards (payment services) (Worthington, 1994). Then, retailers want to support the turnover of the points of sale through credit services in more autonomy from banks. Finally, the financial services are also used in order to cope with the complexity of market dynamics and in order to construct a closer relationship with the customers (investment and insurance services) (Alexander and Colgate, 2000) (Figure 1).

Figure 1: *Financial Services Evolution in Retail Companies*



Often, retailers have enlarged their financial services offer increasing their strategic vision towards a wider target. Indeed, via the use of loyalty cards and credit services, retailers have incorporated complementary services as exclusive promotions. Likewise, they have provided more complex services such as insurance and saving services which are able to join more strongly consumers to the company. In particular, saving and insurance services are used as a marketing tool, to enhance customer loyalty, because these financial services require consumers who entrust their savings to retailers.

In order to satisfy the increasingly diversified financial needs of consumers, retailers activate a process in which consumers communicate their own needs to the service provider, and the provider better understands the consumer's needs. The successful factors for this new kind of financial services offer are a value chain that communicates customer needs and a customer participation in the marketing evolution of services.

More recently, the financial services divisions of large retailers have not been immune to the financial sector woes, reporting a rise in the number of customers defaulting on loans and credit card debt. Nevertheless, grocery retailers aim to take advantage of the poor reputation of banks during the credit crunch, with some enhancing their financial offer and focusing their marketing efforts to increase their brand awareness (Retail Week, 2008).

Indeed, retailers have initially carried out a pure logistical role, favouring the meeting of their own customers with the financial services of the banks. Thus, they have also extended their brand via their financial services, as well as increased the attractiveness of their financial services and corporate image. Although early studies on payment services offered by retailers' brands (Martinelli, 2002) show that retailer branding policies on financial services don't always increase cognitive loyalty in customers' behaviour, most retailers are using their brand to provide financial services in order to support a positive synergies between financial services and corporate image.

2. Ways to Provide Financial Services in Retail Stores

Martinelli and Sparks (1999) argue that a retailer can offer financial services through different partnership with financial operators. Organizational structures to provide financial services are manifold. These partnerships change in relation to the level of the transfer of know-how and the relevance of the financial services in the strategy of the retailer (Risso, 2002).

In particular, it is possible to distinguish three different levels of the transfer of know-how:

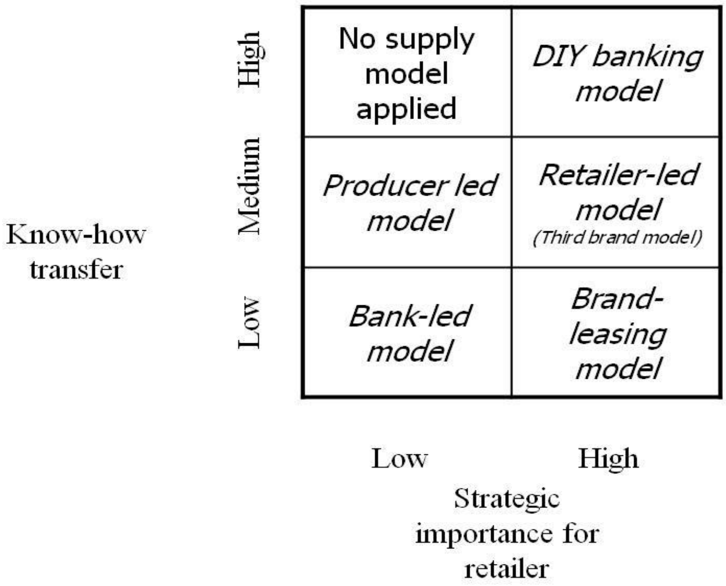
- when the level of know-how transfer between the two sectors is low, retailers and banks enter into simple agreements through which retailers still mainly rely on financial companies to provide financial services;
- when the level of know-how transfer is medium, the agreements turn into a real integration of knowledge between the partners, where retailers learn financial knowledge, on the one hand, and financial companies benefit by techniques of communication and customer information held by retailers, on the other;
- at the end of this process, when a high level of know-how transfer from the financial to the retail sector is achieved, retailers manage financial services directly and by themselves.

Combining the different levels of know-how transfer with the importance given to financial services by retailers, it is possible to identify the diverse solutions implemented (Figure 2).

When a retail company wants to insert financial services in their offer, but it doesn't cover the related risks, it assigns a low strategic importance to the financial offer. In this case, the retail company opts for a reduced interaction with the financial sector and limits itself choosing a financial institution partner to which it rents a part of its sale-surface (in-store banking). This means that the retail company adopts the *bank-led model*, as a lot of USA retailers have done in the 90s.

If the retailer strategy aims to collect a better acquaintance with data and behaviours of the customers, the retailer implements the *producer-led model*. In the producer-led model, the financial services are produced and processed by financial partnership and provided and co-branded through retailer structures.

Figure 2 – *Retailers' Financial Services and Know-how Transfer*



In both models, the retailer cannot be considered as an active actor on the financial services market because it is limited to be a delivery channel of the service in substantial dependency from the financial operator.

Increasing the importance of the role attributed from the retailer to the provision of the financial services, the relations with the financial sector intensify and originate a wider variety of organizational models. If the retailer's strategic vision identifies financial services offer as a way to enhance the value of the customer's relationship and the resources available for these activities are limited – or retailer don't want high interaction with the financial partner – the supply model adopted is the *brand-leasing model*. In the brand-leasing model, the retailer concurs just to use its brand with the bank and all activities are carried out from the financial institution. The bank conceives and develops financial products, sell them through the Internet channel and promotes them by putting advertisements in retail partner stores. In this way, the consumer is strongly attracted to the financial service, although it is an innovative one, because the retailer's brand represents a symbol of trust and familiarity.

When retailers consider financial services in their offer as a valid opportunity of business, they decide to invest resources and to constitute a closer partnership with a bank. This partnership develops a continuous and intense encounter among different knowledge and it is named *retailer-led model*. The services are conceived and developed through mutual interaction between the two partners. The financial offer is provided by an *ad hoc company* – whose control is exercised by the retailer

– utilising the retailer's brand both in the store and on a specific internet site. At the very early stage some retailers used a *third brand model*. They inserted financial services in their offer with remarkable investments creating an organization similar to the retailer-led model but they showed some reservations. In this case, retailers had some doubts on the effective possibilities of the business expansion and they provided financial services with a fantasy brand.

Finally, the retailers become more aware of the importance of financial services in their business operations and they managed to conceive, generate and provide the financial services in perfect autonomy from any other financial operators. The importance of the investments and the transfer of know-how taken from the financial sector are very high. In this case, it delineates the *do-it-yourself (DIY) banking model*. These retailers are, therefore, provider of financial services in full autonomy from banks and they negotiate directly with various financial providers specific financial services as part of their offer.

Every supply model could be suitable to help a retailer to improve his profits, to support the sales growth at point of sale and to permit a strong extension of service activity and the retailer image. Clearly, it depends on the objectives and the involvement of the partnership between retailers and banks. Figure 3 shows possible combinations and solutions linked to the degree of involvement of the retailer and bank partners. When both partners have a high degree of involvement in this business, the partnership is much productive and generates a retailer-led model. At the extreme, it can be identified in DIY banking models, where the bank is only a technical provider and on the opposite side the bank-led model, where the retailer is in a marginal position as a licensee of space. Below the diagonal there is no provision of financial services because the involvement of partners is too limited.

Figure 3: *Supply Models with Retailer and Bank Involvement*

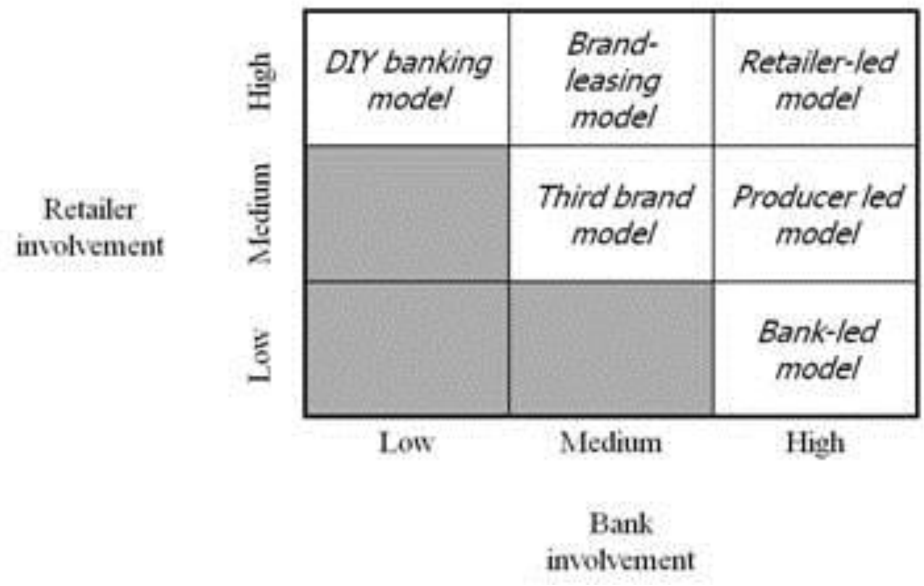


Table 1 shows the marketing mix used to provide financial services in retail store and the different options in relation to supply models adopted.

Is there a right model to provide financial services in retail stores? In analysing some important scenarios, it appears that there is not a one-size fits all solution. If retailer-led models have proved to be the best models to increase effectiveness and efficiency to retailers' financial service offer, the current crisis of the financial system seems to favour the implementation of the DIY banking model. The experiences of Tesco, Auchan and Wal-Mart are significant examples of this pattern.

Table 1: *Supply Models and Marketing Mix of Retailers' Financial Services*

Supply Models	Service Range	Price Competition	Communicational tools	Delivery system	Financial services brand
Bank-led	Wide and simple offer. Nothing link to retailer offer	No competition with other competitors	Traditional. High use of face-to-face contact.	Personal sales and quiet use of direct marketing	Bank brand
Producer led	Opportunity of cross-selling with traditional retailer offer	Quite competition versus traditional financial operators	Strong difficulty to access to communicational tools in the point of sales	Low degree of personal selling and good use of CRM and direct marketing tools	Bank brand and co-branding with retailer brand
Retailer-led	Wide and simple offer. High opportunity of cross selling with traditional retailer offer	High competition versus new and traditional financial operators	Good communicational mix. High capability to use new and traditional tools	Low degree of personal selling and good use of CRM and direct marketing tools	Retailer brand and private label
DIY banking	Wide and simple offer. High opportunity of cross selling with traditional retailer offer	High competition versus new and traditional financial operators	Quite communicational mix. High capability to use new and traditional tools	Strong delay to join other supply model both in personal selling and direct marketing activities	Retailer brand and private label

Source: Risso (2004)

3. The Tesco's Way to Provide Financial Services

The first introduction of financial services in Tesco's offer was in 1997 by a light partnership with the Natwest bank, (third brand model). In 1998, with Tesco Personal Finance (TPF), the financial diversification was stronger and Tesco implemented a retailer-led model, entering into a joint venture with Royal Bank of Scotland (RBS) and using its brand to sign the financial services. This partnership has been a good way to strengthen and expand offer of financial services by Tesco. The retailer-led model adopted by Tesco has facilitated the transfer of know-how between the financial and retail sectors and, simultaneously, the successful creation of financial offer (limited number of products such as savings accounts, insurance and credit cards), which ensures Tesco is able to deliver on its promises to customers.

Recently, Tesco had reached an agreement with RBS to buy its fifty percent shareholding in TPF, converting its financial supply model in DIY banking model. In December 2008, Tesco completed the acquisition of the remaining 50% of TPF from RBS. RBS had been a good partner, and through them, Tesco learned a lot about how to manage a financial services business. The joint venture structure was right for TPF but it had reached a size where Tesco ownership was the most sensible way to run the business and carry it forward.

This was an important move for Tesco, allowing it to build on the success of TPF and eventually offer customers the products they would expect from a full-service retail bank. In this way, Tesco enhances its existing customer base across the 28 simple products offering, but also attracts new customers at a time when many have lost trust in their traditional bank. In this way, Finance and Strategy Director of Tesco said, 'We have a terrific brand and a really good knowledge of our customers and those are things we can exploit when it comes to building the bank to a bigger presence than it is today' (The Grocer, 2008).

All current financial products are available for sale online and, at present, over 50% of Tesco customers choose to buy this way. However, in the same way as customers value the on-line service offered, Tesco understand that many would like to discuss their financial needs with someone knowledgeable. Therefore, Tesco plans to increase its presence for TPF by extending the trial of in-store branches that offer customers the opportunity to talk to specially trained finance advisors in a convenient location. For this reason, Tesco has recently opened six locations in their shops and it has also officially opened the new TPF headquarters at Haymarket in Edinburgh. Tesco Personal Finance has committed to establishing and building its bank from Edinburgh and around 250 members of its staff have already relocated from South Gyle, while the business expects to recruit an additional 200 in 2009 (Creevy, 2009).

4. The Auchan's Experience

In 1983, French international retailer, Auchan, launched its financial division as Banque Accord, utilizing a DIY banking model. Indeed, Banque Accord is a wholly owned subsidiary of the Auchan group. It specialises in financial products and services (payment solutions, savings, insurance, international payment cards, and charge cards), payment technology, online and telephone-based customer relations management, as well as customer relations management in the retail outlets of its partner stores (the Auchan hypermarkets as well as Saint Maclou, Atac, Nocibé, Histoire d'Or, Grand Optical, Pimkie, Leroy Merlin, Norauto,Trésor, Kiabi, Générale d'Optique, Marc Orian, and Alinéa).

To develop its financial services offer at the international level, Auchan, by Banque Accord, has used a *mixed strategy* 'product/country/store'. For countries in which Auchan has a good knowledge of the domestic market, it directly manages the process and offer of financial services via a DIY banking model (Yvernault, 2009). For countries in which the market knowledge is limited, or normative is restricted, Auchan develops a retailer-led partnership.

Indeed, in each new country, Auchan establishes a partnership with leading local firms to search for the lowest possible cost. For each new product or service, it chooses the most highly operational partner to implement better quality solutions and share experiences to carry out a policy of continuous innovation for the stores involved. For example, recently in China, Achuan has launched a credit card issued by Shenzhen Development Bank. With the support of modern data processing technology from GE Money, this card is available for customers to apply for in Auchan stores, assisted by bank staff dedicated to this project (LSA, 2007). To ensure the card benefits to customers (such as credit in coordination with in-store discount and reward policy), Banque Accord has created a Chinese affiliate, Accord Business Consulting (Shanghai) Cy Ltd. Its goal in China is to promote an internationally successful business model using the mass retail channel to distribute financial services while defining the financial services to support the stores success and the needs of stores customers.

5. The Financial Services Offer in Wal-Mart

Also Wal-Mart, the American giant retailer, has increased its offer to financial services. In particular, in 1996, Wal-Mart launched in the USA market a co-branded credit card (Mastercard) with Chase Manhattan Bank and today it has developed a DIY banking model, creating an internal division for financial services offer. Financial services are provided in accordance with many financial services suppliers and Wal-Mart seeks to create an industrial loan company – a banking entity owned by a non-bank – in the USA. Recently, the Federal Deposit Insurance Corporation stalled this attempt (Alaimo, 2007). In 2008, the Canadian branch of Wal-Mart applied to the Minister of Finance to establish a bank under the name Wal-Mart Canada Bank. Since 2007, in Mexico, Banco Wal-Mart has been operative as a bank division, which may be in the black by the end of 2010, offering banking for low-income consumers in branches inside Wal-Mart stores (Progressive Grocer, 2008).

Asda, a UK retailer wholly controlled by Wal-Mart, offers financial services through its own financial division, Asda Financial Services, Ltd. More recently, Wal-Mart has reached a strategic cooperation agreement with the Chinese offline payment provider, Lakala, to provide financial services to people in 80 cities across China. With this cooperation agreement, Wal-Mart will be able to provide its customers with one-stop daily payment services, including credit card repayment, payment of public utilities, and mobile phone recharging.

Wal-mart's 'strategy was to develop more financial services products to complement what [they] are already offering, such as check cashing, money transfers, bill payment and product care plans' (Alaimo, 2007) and it seems to prefer, where possible, a DIY bank model, which assures more control of financial business. Other models, including the retailer-led one, are less utilized and limited to a particular country (i.e. China).

6. Emerging Issues

Financial services within retail outlets are provided in several ways, depending on the different supply solutions adopted. Although all retailers offer financial services by entering into joint ventures with other financial operators, these partnerships can vary in relation to know-how transfer and strategic importance of the activity for retailers.

Retailer-led and DIY banking models appear more suitable than others in creating relationship-building opportunities with customers and in stimulating a stronger awareness in the consumer, who can find in a store a 'useful friend' able to give him or her full satisfaction for various and diversified needs in daily life' (Risso, 2005). At the very early stage, the retailer-led model guarantees the highest degree of marketing innovation and development of the financial offer. Indeed, the partnership led by the retailer produces more intense know-how transfer between retail and financial operators and it allows a better market knowledge of the financial sector for the retailer. Then, DIY- banking models allow retailers the ability to exercise a total control on the management of the financial services, primarily using the retailer brand and developing a complex interaction among financial services, traditional retail offer and corporate brand strategies. The marketing policies connected to these main supply models are highly incisive on consumers and strongly competitive in relation to traditional financial operators. In particular, DIY banking model seem more suitable to achieve these targets in domestic markets where retailers have already obtained deeper market knowledge. The retailer-led model can be applied in introduction of financial services offer in foreign markets.

The process of arrangement of the financial area of the retailer business is still a long one and subject to continuous sharpening. The supply models are daily updated by retail and financial managers involved and they can frequently vary and be significantly improved. At present, there are still wide differences in the provision of the financial services by retailers and it is not possible to consider the phenomenon in a one-size fits all approach. If some retailers achieve profit and extend market share, it is also necessary to specify that not all initiatives are already able to produce profit; in some cases, financial services could represent only promotional tools to stimulate and to support the sales of the retailers.

The advanced strategies adopted in providing financial services' show, as retailers operate on a multi-dimensional approach, to increase their own power and control on different value chains, including the financial services sector. The unexpressed potentialities of retailers' financial services offer can still be important and, as some aspects presented in this paper suggest, financial services are quickly developing in retailer activities. Further, the research focused on strategies and operational tools implemented by large retailers and showed that the provision of financial services by retailers would be desirable. More updated research directed to better understand the consumers' behaviours and the connected retailer business performances would be necessary.

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