Open for Business in Canada, Target Now Fighting for a Retailing Edge

Description

By Christine Conway

Target (NYSE: TGT) has come to Canada, and in the first quarter its first 24 stores produced $86 million in sales. The big-box retailer plans to open 124 stores by the end of 2013.

Target dwarfs the local competition in size (its market cap is $46 billion, versus Loblaw's $14 billion and Shoppers' $12 billion), and so its move into the Canadian market is obviously a game changer for the competition. The acquisitions we've seen of late — between **Sobeys** and **Safeway** and now **Loblaw** (TSX:L) and **Shoppers Drug Mart** (TSX:SC) — are a strategic way to stave off such competitive threats.

Fighting old retail battles

Target and Loblaw will be chasing the same customer: price-sensitive consumers with limited household dollars. Some of the key ways these retailers try to capture as many consumer dollars as possible is through loyalty programs, access to a pharmacy, and, of course, smart real estate in the form of well-placed physical locations.

Rewards programs are used aggressively to create customer loyalty, but come at a cost to the bottom line. Target has its REDcard program as a debit card or Mastercard. This in-store only card gives a 5% discount on purchases, excluding pharmacy. In Target's 2013 first-quarter report, the penetration of sales through the REDcard program in the U.S. was 17.1%. The discount cuts into gross margins, but leads to increased purchases. In the company's first-quarter conference call, Target CFO John Mulligan said that the company continues to "see households increase their spending more than 50% on average when they begin using a REDcard."

Loblaw, too, has a loyalty card structured either as a debit or Mastercard. Its President's Choice Financial awards points based on dollars spent; those points can be redeemed for future purchases.

These loyalty programs not only incent customers to spend more in-store; they collect massive amounts of data about the shopping habits of their faithful patrons. This data can then be used to help the retailers place produce and sell more effectively to their existing customers.

In-store pharmacies have long been another tactic to attract customers. With an aging population and a consumer desire for all-in-one convenience, the pharmacy is a smart way of getting customers through the door. For this reason alone, acquiring Shopper's Drug Mart will potentially expand Loblaw's market.

If Target follows the same model it uses in the States, most stores will have a pharmacy component. Target's U.S. pharmacy is combined into its "health, beauty & household essentials" category that accounts for 25% of revenue.

In an attempt to gain a firm handle on market share, Loblaw wanted more storefronts and access to a wider market. What better way than to buy into a successful brand? Shopper's has 1,237 stores and various offsets across Canada, although half its stores are concentrated in Ontario.

Success around the corner?
For the time being, Loblaw's reach will far exceed Target's, but the novelty of a major force in retail should help Target get traffic through its doors.

It remains to be seen if Target's successful U.S. model will allow it to steal market share here in Canada. But it has a valuable loyalty program and its pharmacies represent a major convenience for consumers. Plus, Target has been compared with the value-conscious **Wal-Mart** in a lot of pricing comparisons. Put it all together and you get a picture of a company well on its way to establishing its presence in the Canadian market.

The Motley Fool recently released a new stock research report, "A Top Canadian Small Cap for 2013 — and Beyond." To download your FREE copy of the report, simply click here now!

Christine Conway does not own shares of any stocks mentioned in this story.

CATEGORY

1. Investing

TICKERS GLOBAL

1. NYSE:TGT (Target Corporation)
2. TSX:L (Loblaw Companies Limited)

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