

Do large retailers displace small informal retailers? The case of a Pick n Pay store in KwaMashu, Durban, South Africa.

Thabani Thaddeus Madlala, Thabani@tips.org.za

Trade & Industrial Policy Strategies (TIPS), Pretoria, South Africa.

Abstract

South Africa is characterised by high unemployment and a relatively small informal sector. This paper generates better insight into the economic relationship between the formal and informal sectors of the South African economy. It investigates whether or not the development of large retailers displaces small informal retailers. The study focuses on current and former owners of informal grocery shops “spaza shops” in a township of KwaMashu, Durban. The analysis revealed that the impact of a large retailer is highly localised, with the greatest impact being on shops adjacent to the mall. Within this radius, most informal shops experience lower consumer volumes and are forced to adjust marketing strategies. These shops typically respond to supermarket entry by diversifying commodities.

Keywords: informal sector; grocery shops; large retailers; agglomeration economies.

1. Introduction

The persistence of high level of unemployment is widely recognised among one of the major socio-economic challenges for South Africa. The Quarterly Labour Force Survey (QLFS) results for the second quarter of 2015 show that 25.0% of the labour force is unemployed (Statistics South Africa 2015). While this high unemployment rate has numerous roots such as lack of demand for labour by possible employers, poor education system and lack of productivity (National Treasury Department 2011; Department of Labour 2013), the weakness of the South African informal sector plays a key role in explaining this trend. The informal sector is indeed an important component in expanding economic participation. However, little attention has been paid to its role in fostering growth and creating employment. It is a neglected component of the economy and has not been recognised in the formal system of law. In an address to the National Council of Provinces in 2003, the former South African President Thabo Mbeki made the following statement:

The second economy (or the marginalised economy) is characterised by underdevelopment, contributes little to GDP [gross domestic product], contains a big percentage of our population,

incorporates the poorest of our rural and urban poor, is structurally disconnected from both the first and the global economy and is incapable of self-generated growth and development (Valodia and Devey 2010, 134).

Furthermore, the country has a relatively small informal sector employment compared to other developing countries, particularly Sub-Saharan African countries (Kingdon and Knight 2004; Valodia and Heintz 2012; ILO 2013). Among the reasons for this is a growing competitive formal sector.

This paper contributes to the understanding of the competitive behaviour of informal sector enterprises in a growing economy. In South Africa, the formal sector dominates the informal sector. The QLFS results for the second quarter of 2015 show that the formal sector accounted for over 10 thousand of employees, while the informal sector accounted for over two thousand (Statistics South Africa 2015). The critical issue to be examined is whether the expansion of formal sector stimulates or displaces the informal sector. In this situation, the paper focuses on the character of competition between large retailers and their smaller counterparts, informal grocery shops. The questions raised include: Are there any links between large retailers and small grocery shops? If so, how are these two sectors linked? Do shop owners lose markets for their goods as a result of the entry of large retailers? If so, what are the dominant reasons for these changes? How do small grocery shops respond to the entry of large retailers?

The paper specifically focuses on the behaviour of informal shops in the KwaMashu area, in Durban, South Africa. It sheds light on whether and how informal shops adapt to competitive conditions. Given the limited prior research, the paper does not intend to present a definitive position, but highlights interesting findings from primary research.

The paper proceeds as follows. Section 2 gives a brief literature review on large-scale retail development in South Africa and theoretical framework. Section 3 provides the methodological framework. Section 4 presents the findings from the study area and gives an analysis and interpretation. The final section concludes with recommendations and summarises the main findings.

2. Review of extant literature

2.1 Large retail development in emerging markets in South Africa

Commercial development has transformed the geographic structure of retailing. Since democracy, the South African retail grocery industry has seen the construction of a new retailscape. Large retailers which tended to locate in more suburban settings have also moved to second economy areas, i.e. township and rural areas. The South African Council of Shopping Centres (cited in Ligthelm 2008) and the South African Cities Network (2010) indicate that over 160 retail centres had been developed in second economy areas by 2009. This growth is expected to continue. Most often the anchor tenants in these shopping centres are national grocery chains which offer goods that are the same or similar to that offered by informal retailers. Several studies explore factors that influence large-scale retail development. It is argued that commercial development in second economy areas is driven by the economic upliftment of inhabitants moving from a lower- to middle-income class. For instance, Tagg, Tustin and Strydom (cited in Ligthelm 2008) indicate that the Black South African middle class increased from 2.8% to 10.5% between 1998 and 2008. The consequent increase in consumer spending has caused large retailers to increasingly focus on market expansion strategies in emerging markets, forming inbound shopping.

Other studies point out that formal industry competitiveness may drive large retailers to seek new markets. It is recognised that retailing is one of the toughest and most competitive sectors. According to Terblanche (cited in Mathenjwa 2007, 11), “retail business environment is becoming increasingly hostile and unforgiving, with intense competition from domestic and foreign competitions”. As a result, large retailers have started to target non-urban settings. One should take note that the development of industrial clusters is one of the focus areas in the municipal documentation. For instance, the eThekweni Municipality (cited in DPLG and Business Trust *n.d.*) indicates that the development of formal nodes and corridors attempts to bring economic opportunities closer to local communities and provides the establishment and opportunities for informal retailers to conduct businesses.

2.2 Linkages between formal and informal economic activities

In contrast to Mbeki's pronouncements (quoted above), it has been theorised in the literature that informal sector firms are linked to formal sector firms. This is explained via theories such as structuralism. The structuralist perspective argues that the informal sector is a conduit used by formal sector firms to produce and distribute goods and services, and is an inherent part and by-product of a new emergent mode of production (Bose 1974; Weeks cited in Moser 1978; Moser 1978; Castells and Portes 1989; Skinner 2005; Chen 2007; Valodia and Devey 2012). Additionally, structuralism argues that the nature of the relationship between these sectors can be a *benign* or *exploitative* one. Considering the nature of the production system through which they are linked is vital to understand the linkages between these sectors. Some scholars have shown that the nature of the linkage varies according to the nature of the production system. Chen (cited in Meagher 2013), for instance, explains that there are three broad structures to mapping formal-informal sector linkages in the economy:

“Open markets” involving direct exchange linkages between formal and informal firms; “subsectors” which focus attention on supply, labour and production linkages across formal-informal boundaries...; and “global value chains”, which examine linkages between lead firms and subcontractors extending across national borders (Chen cited in Meagher 2013, 6).

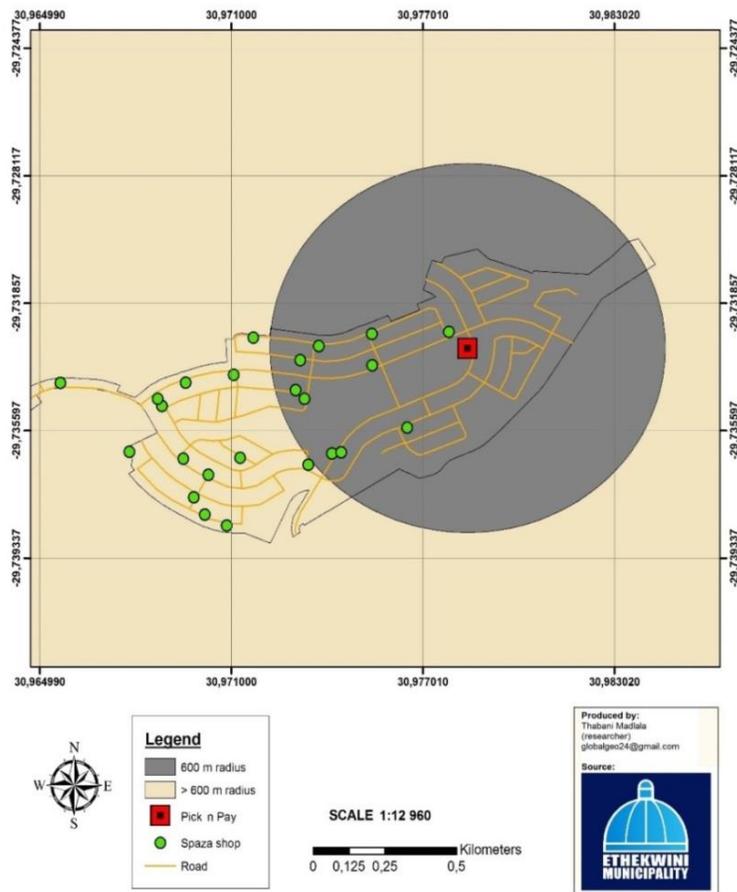
3. Research methodology

In order to understand the impact of large retailers in emerging markets, a sample of informal grocery shops located in KwaMashu, Durban, was interviewed. The study area is within the boundary of the eThekweni Municipality, which the municipality manages through a single administrative unit known as INK (Inanda, Ntuzuma and KwaMashu) Nodal Economic Development Project (DPLG and Business Trust *n.d.*). A shopping centre was opened in May 2013 and houses a national chain store Pick n Pay.

In 2014, a year after the opening of the store, interviews and surveys were conducted with current and former shop owners. Prior to the fieldwork, individual meetings were held with some of the local participants to introduce the research and acquire their participation. Purposive and snowball sampling procedures based on locality size were adopted. This fieldwork was undertaken with the local participants in two phases. The first phase occurred between March and April 2014. The aim during this phase was to produce rich and detailed information regarding the market in the area.

The second phase took place in July 2014, two months after the first phase. During this period the purpose was to observe changes in the market that had occurred after the first phase of the research. The sampling allowed for the selection of respondent businesses in concentric circles around the shopping centre with the application of geographic information system (GIS). Figure 1 confirms distance categories that were selected. The various residential blocks included in each of these distances were selected using the distance measure on a map created by the eThekweni Municipality Corporate GIS (2014). This approach allows a measurement of the impact of the store development on informal shops by distance from the centre. A total of 24 active and five inactive shop owners were interviewed across the distance categories.

Figure 1: Sampling plan, KwaMashu, Durban



Source: eThekweni Municipality (2014)

3.1 Strengths and weaknesses of the study

This study provides some interesting insights of informal retail employment in a growing South African economy. It is important, however, to note some of the limitations of the study. The study findings cannot be generalised to the entire business market because of the relatively small sample size. Furthermore, the study was carried out among informal grocery shops, which excludes other types of businesses in the informal sector. It would be advisable to conduct a similar study in an alternative area that may portray a somewhat different socio-economic structure. Also, such a study should preferably include other business sectors in addition to the retail sector addressed in this paper.

4. Study findings

Participants in the study were asked several questions on the impact of the Pick n Pay store on surrounding shops. These questions ranged from perceived small business mortalities to more exact questions on the decrease or increase in consumer volumes, stock movement, profitability and product range of existing individual shops.

4.1 The impact of large retail development in emerging markets

Descriptive statistics confirm a generally negative impact of the store on the surrounding informal shops. Table 1 below shows that the larger segment in close proximity to the centre indicated a dramatic decline in consumer volumes, stock movement and profitability since the opening of the store. Table 2, on the other side, shows that the larger segment far from the centre experienced only a slight decline. However, it is not known how these businesses performed prior to the entry of the store. Their performance might have been poor then too, which means that one cannot be definitive in the findings. The results of the study suggest that although there have been changes in the small business market, the negative effect of large retailers is more severe in the case of businesses in close proximity to the retail node.

Table 1: Perceived impact on business performance after the development of Pick n Pay (within 600 m) – March to April 2014

	Stock size		Profits		Customers	
	Number of shops/ shopkeepers	%	Number of shops/ shopkeepers	%	Number of shops/ shopkeepers	%
Increased in large amount	0	0	0	0	0	0
Increased in small amount	0	0	0	0	0	0
The same	1	10	1	10	1	10
Decreased in small amount	2	20	2	20	2	20
Decreased in large amount	7	70	7	70	7	70
Total	10	100	10	100	10	100

Source: Field Survey (2014)

Table 2: Perceived impact on business performance after the development of Pick n Pay (above 600 m) – March to April 2014

	Stock size		Profits		Customers	
	Number of shops/ shopkeepers	%	Number of shops/ shopkeepers	%	Number of shops/ shopkeepers	%
Increased in large amount	0	0	0	0	0	0

Increased in small amount	0	0	0	0	0	0
The same	3	21.43	3	21.43	3	21.43
Decreased in small amount	8	57.14	8	57.14	8	57.14
Decreased in large amount	3	21.43	3	21.43	3	21.43
Total	14	100	14	100	14	100

Source: Field Survey (2014)

Having lost market sales of products in their businesses, participants were asked to determine which type of products were most affected. Most shop owners indicated that they had lost sales in bread. Table 3 shows the differences in price of commodities in the informal shop sector and the chain store. The evidence confirms that there exists a competitive product market between informal shops and large retailers. One of the participants, particularly close to the store, stated that “Sales of loaves of bread declined significantly and most end up expiring as very few customers purchase from me, resulting in financial loss. As a result, I no longer order many cases [trays] of bread from a wholesale bakery. Sometimes I buy few loaves of bread at Pick n Pay”. As shown in the table, the price of a white loaf of bread, for instance, from Pick n Pay was R5.99 compared to R10 from informal shops; a price difference of R4.01. This finding indicates that the impact of the store on some shops has resulted in significant losses of sales of perishable foods and has led to some businesses limiting or severing linkages with their suppliers. Other participants indicated that they

have lost market sales of refrigerated products. For instance, one reported “I do not stock fresh-milk anymore. Instead, I stock long-life milk as it requires no refrigeration”. The participants further indicated that the dominant reasons for the changes resulted from a duplication of products in the area, price differences, increased levels of competition and decreased consumer volumes.

Table 3: Price comparison between informal grocery shops and a Pick n Pay store in KwaMashu – March to April 2014

Food product			Spaza shops (average)	Pick n Pay	Other large retailers (Shoprite)
Item	Weight/Mass	Brand	Price	Price	Price
1. Rice	500g	<i>Aunt Caroline</i>	R8	N/A or DNS	N/A or DNS
2. Rice	1kg	<i>Aunt Caroline</i>	R12	N/A or DNS	R10.79
3. Maize meal	1kg	<i>Ace</i>	R8.50	R6.79	R6.99
4. Maize meal	5kg	<i>Ace</i>	DNS	R28.99	R31.99
5. Fresh milk	500ml	<i>Clover</i>	R6	R8.29	R7.99
6. Fresh milk	1l	<i>Clover</i>	R12	R11.99	R11.99
7. Half-dozen eggs	-	No brand	R9	R8.99	R9.99
8. Half-white loaf	-	<i>BB Bakeries</i>	R5	DNS	DNS
9. Full white loaf	700g	<i>BB Bakeries</i>	R10	R5.99	R9.19
10. Half-brown loaf	-	<i>BB Bakeries</i>	R4.50	DNS	DNS
11. Full brown loaf	700g	<i>BB Bakeries</i>	R9.50	R5.49	R7.99
12. White sugar	250g	<i>Huletts</i>	R4	N/A or DNS	N/A or DNS
13. White sugar	500g	<i>Huletts</i>	R7	R6.49	R6.99
14. Soft-drink	330ml	<i>Coca-Cola coke</i>	R7	R7.49	R6.99
15. Soft-drink	2l	<i>Coca-Cola coke</i>	R17	R13.99	R14.89

Source: Field Survey (2014)

* Note: N/A – not available at the time of data collection

DNS – does not stock

g – gram

l – litre

kg – kilogram

ml – millilitre

Although there is a competitive market between informal shops and large retailers, the majority of the participants reported no change in the number of shops in their immediate vicinity. However, those who reported a decline stated that “two to three shops” had been shut down since the opening of the store. Out of the five former shop owners interviewed, it was established that three shut down their businesses before the opening of the store. Their reasons were lack of business planning, employee-theft, and finding new employment. This indicates that the opening of the store had no direct or indirect role in the closure of these businesses. However, one of the participants went out of business due to loss of customers after the store opened.

During the second phase of the field research, some changes were observed in the shop sector. One of the most important findings was the discovery of new shops surrounding the centre. The finding indicates that new entrants locate in a favourable position to large retailers to take advantage of passing traffic. These results reflect the importance of nodal integration. Another discovery was that prices of commodities were almost the same between these sectors. For instance, a loaf of bread (white) had increased to R10.40 from Pick n Pay compared to R11 from informal shops. It was also observed that none of the shops documented in the first phase had shut down.

4.2 Links between large retailers and small grocery shops

Although most of the participants indicated that the opening of the store had no benefit for their businesses, some indicated slight benefits. Reasons given by these participants who indicated positive effects included:

“When people [consumers] find that Pick n Pay is closed [after trading-hours], they tend to buy small products from me”; “I used to source goods such as loaves of bread from large wholesalers but now I purchase them at Pick n Pay because they are cheaper; and “Pick n Pay benefits my business as I do not have to hire a vehicle to get some goods at wholesalers. Instead, I purchase some products at Pick n Pay as it is closer to my shop”.

The findings suggest that a large retailer can draw in consumers from surrounding communities and that small businesses may benefit from the exposure and to foot traffic. This shows that there

is some recognition of the positives that can be gained by being around large retailers which are already drawing the desired customers as well as save time and costs.

4.3 Competitive response from informal shops to large retailers

Participants were also asked if they had included new products or services in their business since the opening of the store. Very few indicated that they had done so. Given that there are few incentives to improve business performance; one can conclude that the majority of these entrepreneurs made few dramatic adjustments to their competitive strategies and were either unwilling or unable to enact a competitive response. The businesses that adopted a competitive strategy to fight the store tended to focus on other commodities or extend their markets to sustain competitive advantage. These businesses have thus decisively shifted away from being general shops.

Although informal shops cannot compete with large retailers on price, some have assessed their strengths and weaknesses, and committed to a competitive strategy by providing merchandise mix where there is little direct competition. Some of the participants reported:

“I have now introduced towel sales in my business, offering something different from Pick n Pay”; and “I have become a part-time tailor, producing such products as common shirts and dresses as well as sewing embroidery designs on fabric”.

Take-away food business is another industry which has emerged in the informal shop sector. For instance, one of the participants opened a small take-away business in addition to her business – selling “Russian sausages” and “potato fries”. According to this participant, her intention is to build strong relationships with many of her key customers over time, which will further protect her from competitive threats.

Some shops have competed in a narrowly defined market segment with specialised offerings or in niche marketing, focusing on specific groups of consumers and the specific needs and wants of these groups. For instance, two of the participants reported that they focus on children as a niche market and have become reliant on a relatively small market. They offer products such as sweets,

chips, and biscuits for this market segment. Responses to market demand included “easy to sell”, “sells fast” and “goods always in demand”.

Additionally, the informal shops have slight advantages because they have longer trading hours compared to large retailers. Most participants indicated that they trade between “7 am and 8 pm”, whilst the store is open from “8 am to 6 pm”. Furthermore, the participants allow customers to purchase goods on credit as a strategy to keep them loyal.

5. Discussion and conclusion

It is important to keep in mind that an entry of a large business reshapes the economic geography of grocery retailing and this is supported by scholars who place the findings in a broader academic discourse and contributes towards the existing literature in development economics.

5.1 Differences and similarities in results and conclusions in relation to other studies

Previous studies have been conducted on the impacts of large retailers on local labour markets. The findings of the present study confirm the argument made by Ligthelm (2008) about the adverse effects of large retailers on the local labour markets of small retailers. He argues that small retailers surrounding large retailers suffer a larger loss in market share compared to those further away. The findings of the present study show that the entry of a new large store significantly impacts only those rival small businesses that operate in close proximity to a large store. Rival small businesses outside a certain radius are not significantly affected by the entry of a large store.

This paper also confirms the findings of Valodia, Davies, Altman, and Thurlow (2007), who assess the importance of the geographic concentration of industries as a source of agglomeration economies. The finding implies an increase in retail employment with new shops attributable to the opening of the chain store. The concentration of these new businesses is evidence for the existence of agglomeration economies. Although it is hard to predict, there is likely a possibility that new shops might be harmed over the long-term in the absence of clear business strategies. However, this anecdotal evidence requires better understanding and is something that will have to be addressed in future studies.

The paper has also confirmed that the entry of a chain store impacts on spatial and temporal scale in the labour market – involving interactions of businesses in a decreased spatial-temporal scale.

As the store located closer to local businesses, some were able to overcome the barrier of the time and space separation, which formerly separated and isolated individual businesses. A growing preference from shop owners for goods sourced from the large retailer, situated nearby, over wholesalers (located far away) was noted. This has reduced dependence on long supply chains and the cost of moving goods. It could also be argued that the presence of the large retailer has significant impacts on time savings. Distance, therefore, plays a critical role in determining the distribution of ideas and interaction.

5.2 Recommendations and policy implications of the empirical findings

Commercial development of large retailers is one of the government's strategies to address unemployment in South Africa. There is a belief that if a large store is opened in the trade area it is going to capture a considerable amount of trade or perhaps change zoning status in order to attract small businesses. The government focuses much on large industries which is hoped to contribute to gross domestic product. Little attention has been paid to a competitive market that exists between large retailers and their smaller counterparts. The findings of this study suggest that government needs to carefully weigh the costs and benefits of associated with the development of large businesses. It is therefore recommended that there should be a broader understanding of spatial competition in dynamically evolving industries.

Additionally, the participants were requested to make suggestions of what the government could do to improve the relatively small informal sector enterprises in the area. They reported that the government should make efforts to assist small businesses in financial and business planning through appropriate development plans, and establishing special institutions and programmes to assist informal enterprises as they do formal ones.

5.3 Conclusion

This paper has provided some evidence to support two important predictions of the structuralist perspective. The first is that there are linkages between formal and informal sector firms in the labour market. The case of KwaMashu shows that a Pick n Pay outlet has minimal linkages with informal shops in terms of easy access to market and product distribution. The second contribution is that informal businesses may be exploited by the capitalist structure of mass merchandisers as direct competitors in a competitive environment. As is evident in the present study, large retailers

and informal shops compete within the same product market. The results indicate that informal shops struggle to compete on price with larger chains. More importantly, the results indicate that the entry of a new large store significantly impacts only those rival small businesses that operate within a tight radius of the large retailer site and these small businesses in the trade area lose a comparable amount of trade. It is considered that the government sector needs to weigh the costs and benefits of commercial development in secondary economy areas as well as provide special institutions and programmes to assist small informal businesses.

References

Bose, A.1974. *The informal sector in the Calcutta metropolitan economy*. Geneva: International Labour Office.

Castells, M and Portes, A. 1989. World Underneath: The origins, dynamics and effects of the informal economy. In A. Portes., M. Castells and L. Benton. (eds). *The informal economy: Studies in advanced and less advanced developed countries*. Baltimore: Johns Hopkins University Press.

Chen, M. 2007. Rethinking the informal economy: Linkages with the formal economy and the formal regulatory environment. Working Paper No 46. United Nations, Department of Economic and Social Affairs, New York. http://www.un.org/esa/desa/papers/2007/wp46_2007.pdf

Department of Labour. 2013. *Job Opportunities and Unemployment – in the South African Labour market 2012-2013*. <http://www.labour.gov.za/DOL/downloads/documents/annual-reports/job-opportunities-and-unemployment-in-the-south-african-labour-market/2013/joboppreport2013a.pdf>

eThekwini Municipality. 2014. <http://citymaps.durban.gov.za/internetwebsite/index.html>

DPLG and Business Trust. n.d. *Inanda, Ntuzuma, KwaMashu (INK) Nodal Economic Development Profile*.

http://www.durban.gov.za/Documents/City_Government/IDP_Policy/01%20INK_narrative.pdf

ILO. 2013. *Women and men in the informal economy: A statistical picture*. Geneva: International Labour Office. http://www.ilo.org/wcmsp5/groups/public/---dgreports/---stat/documents/publication/wcms_234413.pdf

Kingdon, G and Knight, J. 2004. Unemployment in South Africa: The nature of the beast. *World Development*. 32 (3): 391-408. http://ac.els-cdn.com/S0305750X03002407/1-s2.0-S0305750X03002407-main.pdf?_tid=3a21430e-0d38-11e4-b16c-00000aab0f26&acdnat=1405549767_33188f22b382de856a8a4285770da8f5

Ligthelm, A. 2008. The impact of shopping mall development on small township retailers. *South African Journal of Economic and Management Sciences*. 11(1): 37-53. <http://www.sajems.org/index.php/sajems/article/viewArticle/376>

Mathenjwa, A. 2007. *The impact of Jabulani shopping mall on small township businesses and their response* (Unpublished master's thesis). University of Pretoria.

<http://upetd.up.ac.za/thesis/available/etd-03232010-153852/unrestricted/dissertation.pdf>

Meagher, K. 2013. Unlocking the informal economy: A literature review on linkages between formal and informal economies in developing countries. WIEGO Working Papers.

<http://wiego.org/publications/literature-review-linkages-between-formal-and-informal-economies-developing-countries>

Moser, C. 1978. Informal sector or petty commodity production: Dualism or dependence in urban development? *World Development*. 6 (9-10): 1041-1064.

National Treasury Department. 2011. *Confronting youth unemployment: policy options for South Africa*. Pretoria: National Treasury.

<http://www.treasury.gov.za/documents/national%20budget/2011/Confronting%20youth%20unemployment%20-%20Policy%20options.pdf>

Skinner, C. 2005. Constraints to growth and employment in Durban: Evidence from the informal economy. Research Report 65.

<http://wiego.org/sites/wiego.org/files/publications/files/Skinner-Constraints-Growth-Employment-Durban.pdf>

South African Cities Network. 2010. Retail centres and township development: A case study.

http://www.sacities.net/images/stories/2011/Publications/TTRI_Case_study_Retail_Centres_and_Township_Development_2010.pdf

Statistics South Africa. 2015. *Quarterly Labour Force Survey: Quarter 2:2015*. Pretoria:

Statistics South Africa. <http://www.statssa.gov.za/publications/P0211/P02112ndQuarter2015.pdf>

Valodia, I., Davies, R., Altman, M and Thurlow, J. 2007. *Exploring economic behavior in South Africa's informal economy, especially in relation to the formal economy*. Cape Town: Human Sciences Research Council.

Valodia, I and Devey, R. 2010. Formal-informal economy linkages: What implications for poverty in South Africa? *Law, Democracy & Development*. 14 (n.n): 133-158.

http://www.idd.org.za/images/stories/Ready_for_publication/valodia_devey-new.pdf

Valodia, I and Devey, R. 2012. The informal economy in South Africa: debates, issues and policies. *Margin: The Journal of Applied Economic Research*. 6 (2): 133-157.
<http://mar.sagepub.com/content/6/2/133.full.pdf+html>