

Consumer & Retail Sector Reference

Industry Special – Sector-Specific Reference

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Supplement to the G2G Complete Reference. No duplication.

I. UK & European Retail Landscape

The UK retail market is characterised by extreme consolidation, with the Big Four grocery chains controlling 67% of grocery spend. Combined with Aldi and Lidl, the Big Six represent approximately 82% by volume. Convenience stores, led by Tesco Express, represent the fastest-growing channel. The non-food segment has been decimated by e-commerce. Out-of-town retail parks remain under structural pressure. Private equity interest in retail includes CVC's interest in Pets at Home, Apollo's pursuit of Boots, and Blackstone's stake in Selfridges, typically targeting mature cash generative businesses with property upside. European retail presents distinct dynamics: Germany has strong private label penetration; France has regulatory constraints; Italy is fragmented. Omnichannel maturity varies significantly with Carrefour and Tesco leading. Property value underpins significant value creation with Tesco's revaluation and Sainsbury's sale-leaseback. Inditex demonstrates the power of vertically integrated fashion retail with rapid design-to-shelf cycles and real-time demand responsiveness. Notable PE-backed transactions include Boots LBO by KKR (2007), which extracted significant dividends through leveraged buyout. M&S remains a periodic activist target given property optionality. Sainsbury's-Tesco merger was blocked (2019) on competition grounds. Current capex in bricks-and-mortar remains depressed relative to pre-2008 levels, with retailers prioritising omnichannel investment and supply chain automation. Market consolidation has created significant bargaining power with suppliers, enabling retailers to demand slotting fees and rebates.

The regulatory environment constrains further consolidation in UK grocery, reflecting antitrust scrutiny. Strategic positioning in non-food (clothing, home, beauty) requires differentiation against pure-play e-commerce. Channel strategy evolution from store-centric to omnichannel requires significant capex and operational complexity. Customer data becomes increasingly valuable; retailers with 10M+ active customer relationships can monetise through insights and targeted marketing. Supply chain resilience emerges as competitive differentiator post-COVID disruptions. Sustainability requirements (plastic reduction, carbon neutrality) drive cost inflation without corresponding pricing power. Pension liabilities constrain strategic flexibility for legacy retailers. Real estate optionality creates hidden value for property-rich retailers like Tesco and Sainsbury's with significant store ownership. Franchisee model expansion in convenience and food-to-go enables capex-light growth but creates franchisee profitability risk if economics deteriorate.

The rise of discounters represents structural market share shift rather than cyclical event. Aldi and Lidl have demonstrated that limited SKU (1,400 vs 40,000), private label focus, and ruthless cost control enable superior returns. Traditional supermarket response via private label expansion and convenience format only partially offsets share loss. E-commerce penetration in grocery (25-30% of sales) is accelerating, driven by demographic shift toward younger consumers and convenience preference. Omnichannel execution capability differentiates winners from losers; retailers unable to seamlessly integrate inventory, pricing, and customer experience face share loss to pure-plays and discounters. Geographic concentration risk in UK property represents long-term headwind as retail footprint contracts and prime locations consolidate. Inflation in labour costs (5-7% annually) outpaces pricing power, compressing margins unless offsetting COGS reduction achieved. Technology capex requirements for omnichannel, data analytics, and supply chain visibility create barrier to entry for smaller players.

LFL Analysis: Volume Decline 1-3% YoY, Masked by Price Inflation 0-5% | Volume Loss to Online 3-5% Annually

Space Productivity: High Street Conv. 40-60 per sq ft, Hypermarket 15-25, Discount 20-30 | Marginal Site 30-40% Lower Density

II. Like-For-Like Growth & Space Productivity

Like-for-like (LFL) sales growth decomposition into price and volume is critical for understanding market share dynamics. Volume typically declines 1-3% annually in mature UK retail, masked by price inflation of 0-5% depending on promotional intensity. During inflationary periods (2021-2024), retailers with pricing power (premium/luxury) achieved LFL growth through price whilst discount players captured share through volume. Conversely, recessionary periods see volume collapse partially offset by defensive private label switching and channel shift to discounters. Nielsen/Kantar basket analysis provides granular insight by product category, revealing where share is lost to competitors, online, or alternative channels. Share loss in health & beauty to Amazon and Boots.com, in clothing to ASOS/Shein, and in electricals to Currys.com represent structural headwinds. E-commerce cannibalism is underestimated by most retailers; pure-play online penetration is 5-8% of traditional grocery by volume, directly reducing supermarket customer frequency and basket size.

Space productivity measured as sales per square foot varies dramatically by format and geography. High street convenience stores generate 40-60 pounds per sq ft annually versus 15-25 for hypermarkets. Airport and travel retail generates 200+ per sq ft reflecting captive audience and premium pricing. Discounters achieve 20-30 per sq ft through high inventory turnover and limited variety. Premium formats (Waitrose, M&S Food) generate 25-35 per sq ft through higher unit prices and selective customer base. Marginal space productivity is critical; the 50th unit in a town may generate 30-40% less revenue density than the 1st. Cannibalisation analysis quantifies new store opening impact on neighbouring existing stores; typically 10-30% of new store revenue is cannibalised from adjacent locations, a factor often underestimated in management projections. Dead mall analysis reveals that many retailers operated stores with single-digit ROIC; systematic rationalisation by Morrisons and Sainsbury's unlocked material value.

Inventory productivity directly impacts working capital and space utilisation efficiency. Fast-moving grocery (fruit, vegetables, dairy) require high velocity and low inventory (2-3 weeks of cover) whilst clothing requires seasonal build and clearance cycles (4-6 weeks peak, 1-2 weeks off-season). Excess inventory ties up cash and forces markdown, directly compressing gross margin. Supermarkets typically maintain 6-8 weeks of total inventory; specialty retail 8-12 weeks. Recent supply chain disruption (COVID, container costs, port congestion) forced retailers to either over-order (excess inventory) or under-order (stock-outs and lost sales). Best-in-class retailers use advanced demand forecasting, promotional calendars and supplier collaboration to optimise inventory levels simultaneously with space productivity. Store clustering analysis identifies geographic cannibalization hotspots requiring remediation through store repositioning, format conversion, or selective closure. Store format evolution from large hypermarket to smaller neighbourhood formats reflects changing consumer shopping patterns and cost structure evolution.

Like-for-Like Decomposition: $LFL \% = (\text{Volume } \% \times \text{Vol Mix}) + (\text{Price } \% \times \text{Price Mix})$

Space ROIC: $4\text{-Wall EBIT} / \text{Store Capex} + \text{Working Capital} = \text{Target } 15\text{-}25\%$ for Growth Stores

III. Gross Margin Analysis & Markdown Dynamics

Gross margin is the primary lever of profitability, determined by intake margin, shrinkage, markdown, and private label mix. Intake margin varies by category: produce (5-15% gross margin) versus luxury goods (40-50%), with promotional goods potentially trading at cost or negative margin to drive traffic. Retailers achieving 25-30% gross margin (Tesco, M&S) operate higher private label mix and strong vendor negotiation. Discounters operate at 18-22% through low-cost sourcing and limited private label. Gross margin bridge analysis isolates margin drivers and flags deterioration sources. For example, Sainsbury's margin compression (2019-2020) reflected category mix (growth in low-margin grocery versus higher-margin non-food), promotional intensity (price wars with Aldi/Lidl), and shrinkage (logistics centre theft spike). Category-level margin analysis reveals which departments (produce, meat, deli, bakery) are margin destroyers versus generators.

Markdown dynamics critically impact seasonal P&L in fashion retail. Markdown waterfall progression: full price (60-80% of season), first markdown (20-30%), final markdown/clearance (50-70% off), off-season write-off. Seasonal mix means poor Q4 performance directly flows to Q1-Q2 losses. Sell-through rates vary significantly: leading brands (Zara, Next) achieve 85-90% at full price versus legacy retailers (Debenhams, Boohoo) at 60-70%, necessitating deeper markdowns. Mark-up curve determines markdown absorption ability; retailers with high mark-ups (luxury) absorb better than those with tight mark-ups (discounters). Promotional velocity (frequency and depth) reflects competitive intensity and demand weakness; increasing promotional cadence signals margin pressure and potential demand destruction as consumers learn to wait for discounts. Promotional calendar optimisation reveals overlap and conflicts; retailers often run conflicting promotions destroying incremental volume benefits.

Shrinkage (inventory loss, typically 0.5-2% of sales) results from controllable factors (pillage, till fraud, administrative error) and uncontrollable factors (waste, spoilage). Fresh food retail suffers higher shrinkage (2-3%) due to perishability. Fashion suffers from theft and security tag removal. Serious shrinkage problems signal either operational issues or control failures requiring material intervention. RFID tagging, loss prevention associates, and CCTV reduce shrinkage 20-40%, though capex is substantial. Full-price mix (% of sales at retail price versus promotional price) directly drives profitability; retailers tracking declining full-price mix signal deteriorating margin and demand, major red flag for investors. Private label mix, when done well, expands margin 3-8% of sales (PL typically 3-5% higher margin than branded) and strengthens retailer negotiation with suppliers; however, quality perception risk and consumer brand preference limit PL penetration.

Gross Margin Bridge: $\text{Opening Margin} +/- \text{Category Mix} +/- \text{Promotion} +/- \text{Shrinkage} = \text{Closing Margin}$

Full-Price Mix Tracking: $\% \text{ Revenue at Retail Price vs Promotional Price} | \text{Declining Mix} = \text{Demand Pressure Red Flag}$

IV. Working Capital & Inventory Management

Retail working capital is typically negative (favourable) as suppliers grant 30-60 day payment terms whilst consumers pay at point of sale. Cash conversion cycle (CCC) = Days Inventory + Days Sales Outstanding minus Days Payable Outstanding. Strong retailers achieve 5-15 day negative CCC (cash benefit), whilst distressed retailers slip to positive

10-30 days (cash drain). Tesco historically achieved near-zero CCC through massive bargaining power; recent supply chain inflation forced modestly positive CCC as supplier terms tightened. Inventory management remains critical; weeks of cover (inventory value divided by weekly COGS) of 6-8 weeks optimal for grocery, 8-12 weeks for specialty retail. Aged inventory analysis (% of inventory >6 months old) flags operational issues and obsolescence risk; excess aged inventory requires deep markdown destroying margin. Seasonal working capital swings are material; fashion retailers build inventory 15-30% above average in Q3 (pre-Christmas), requiring funding of 50-200M+ depending on size, creating Q4-Q1 cash swings. Supply chain disruption (COVID, port congestion, strikes) forced inventory build of 15-25%, materially impacting 2022-2024 working capital and net cash position. Inventory rationalisation (SKU reduction, DC consolidation, demand-sensing automation) is primary PE value creation lever; reducing inventory 10-15% whilst maintaining service levels unlocks 100M-500M cash for debt paydown. Vendor-managed inventory and consignment arrangements shift working capital upstream to suppliers, particularly beneficial for capital-intensive items (furniture, electricals, footwear). Collaborative demand planning with major suppliers, using POS data and forecast sharing, reduces demand whiplash and inventory buffering.

Supplier concentration risk is material; if key suppliers face disruption, working capital shock is immediate. Shrinkage inflation (growing faster than sales inflation) signals control failures and organised retail crime; a 0.5-1% shrinkage spike consumes 30-50% of EBITDA growth. Seasonal peaking requires structured working capital facilities; seasonal revolver size of 500M-1B+ is typical for major retailers with careful covenant management to avoid technical default during peak inventory seasons. Fashion retail is particularly exposed to working capital volatility; poor Q4 demand (after major inventory build) forces liquidation consuming cash and destabilising liquidity. Treasury optimisation through supply chain financing partnerships enables working capital efficiency gains of 5-15% without compromising supplier relationships.

CCC = Days Inventory + DSO - DPO | Negative CCC = Working Capital Benefit; Target Negative 5-15 Days

Inventory Days = (Inventory Value / COGS) x 365 | Grocery 42-56 Days, Fashion 56-84 Days, Specialist 60-90 Days

V. IFRS 16 & Occupancy Economics

IFRS 16 (implemented 2019) revolutionised lease accounting by recognising lease obligations as liabilities and corresponding right-of-use (ROU) assets. For retailers with significant store leases, IFRS 16 increased assets and liabilities by 200-400%, materially impacting balance sheet metrics. A retailer with 2B rent obligations now records 2B+ ROU asset and 2B+ lease liability; adjusted EBITDA (adding back lease expense) increased 15-25% overnight, critical adjustment for debt covenant and valuation multiples. Occupancy cost ratio (total rent expense divided by sales) typically ranges 8-15% for grocery (lower in urban prime locations, higher in secondary locations) and 12-20% for specialty retail. Lease maturity profiling is critical; retailer with 70% of leases maturing in Years 1-3 faces significant refinancing risk and rent increase exposure.

Store-level four-wall P&L (revenue minus direct COGS, labour, occupancy costs, excluding corporate overhead allocation) is primary driver of individual store economics and renovation/closure decisions. A store with 20M revenue, 25% gross margin (5M), 2M labour (10%), 2M rent (10%), and 800K variable overhead generates 200K four-wall EBIT (1% margin). Once allocated corporate overhead (5-8% of sales), store breaks even or loses money, driving closure. Conversely, convenience store with 8M revenue, 28% gross margin (2.24M), 1.2M labour (15%), 800K rent (10%), and 400K overhead generates 240K four-wall EBIT (3%), viable after overhead allocation. Rent benchmarking across portfolios reveals significant variability; prime high street locations with 50M+ sales may pay 8% rent whilst secondary locations with 8M sales pay 12-15%.

Sale-leaseback of owned properties (Sainsbury's Nectar property sale, Tesco monetization) is common financing tool; retailers sell stores to property funds and lease back, monetising embedded value (10-20B for major retailers) to delever debt and fund capex. Lease negotiation (rent holidays, percentage rent, expansion options, break clauses) is material during downturns; during COVID-19, major retailers renegotiated 1,000+ leases extracting material reductions and flexible terms. Landlord concentration risk is material; major pension funds and property companies controlling UK retail real estate can exercise pricing power post-recovery. Lease extensions and break clause exercise require careful timing and commercial negotiation; retailer waiting until 12 months before expiry loses leverage versus negotiating 3-5 years ahead.

Occupancy Cost %: Total Annual Rent / Annual Sales = % | Target 8-12% Grocery, 12-18% Specialty

Four-Wall EBIT: Revenue - COGS - Labour - Rent - Direct OH = Store Profit Before Corporate Allocation

VI. E-Commerce & Omnichannel Economics

E-commerce represents 25-30% of UK grocery, 50-60% of fashion, and 70-80% of consumer electronics. Online contribution margin (gross margin minus fulfilment cost) is negative for most grocery; grocery e-commerce operates at -2 to +3% margin versus +5-8% for store, reflecting fulfilment cost of 1-2 per 10 basket. Customer acquisition cost (CAC) in e-commerce is 15-40 for digital acquisition (Facebook, Google, affiliate) but much higher (50-150) for paid search in competitive categories. Customer lifetime value (CLV) for repeat retail customers is typically 3-5x CAC, meaning CAC payback occurs in 6-18 months for loyalty customers. Return rates in fashion e-commerce are 20-40% (versus 5-10% in-store), directly impairing online margin; luxury and apparel return rates are highest (35-45%), electronics 15-25%, groceries 1-3%.

Return logistics cost (reverse logistics, inspection, re-stocking, final disposition) consumes 10-15% of returned value, making returns economics dire. Some retailers (Shein, Boohoo) accept near-total loss on returned items to drive volume; others (Zara, Next) limit returns window and charge restocking fees. Fulfilment model selection (ship-from-store versus distribution centre versus dark store) fundamentally impacts economics. Ship-from-store has zero marginal capex but high labour inefficiency and variable cost (0.50-1 per order). Automated dark stores (Tesco's partnership with Ocado) have high capex (20-40M per site) but low variable cost (0.10-0.20 per order) and faster delivery (2-4 hours). Ocado IPO (2010) pioneered dark store economics; post-pandemic, dozens of retailers deployed dark stores, likely creating excess capacity as demand normalizes.

Click-and-collect (C&C) economics are superior to home delivery; margin is 1-3% (versus -2-3% for delivery) as consumer absorbs logistics cost. C&C drives store traffic and impulse purchase (15-25% of C&C customers browse in-store), offsetting reduced deliverability. Subscription models (Amazon Prime, Sainsbury's+) add 5-15 monthly recurring revenue per subscriber, materially improving CLV and retention; Prime members spend 2-3x more. However, subscription churn (15-30% annually) is significant risk; acquiring replacement for 1M churned members at 40 CAC costs 40M annually. Omnichannel integration (unified inventory, pricing, customer data) requires significant capex and operational complexity; legacy retailers struggled, losing share to pure-plays (Asos, Next) with unified systems.

Online Margin: Gross Margin % - Fulfilment % - CAC Amortisation % = Online Profit

Dark Store Capex: High Upfront (20-40M) + Low Variable (0.10-0.20 per order) vs Store (0.50-1.00)

VII. Brand Value & Private Label

Brand valuation uses relief-from-royalty (RFR) method: brand value equals net present value of hypothetical royalties if brand independently owned. For 1B revenue retailer with Tesco/Sainsbury's brand, implicit royalty is 3-5% (30-50M annually), resulting in NPV (at 10% WACC, 10-year terminal) of 200-300M. LVMH brands (Louis Vuitton, Dior) operate implicit royalties of 20-25%, reflecting 10-15x higher intangible value. Brand value drivers are consumer awareness, pricing power, loyalty, and geographic reach. Brands facing structural headwinds (declining NPS, share loss, margin compression) suffer valuation collapse; Boohoo's brand value halved post-scandal, reducing implicit equity value by 500M+. Private label penetration varies significantly; UK grocery achieves 35-40% by value (Tesco up to 45%), driven by quality improvement and conscious consumerism.

Private label margin is 3-8 points higher than branded (PL 30-32% versus branded 25-27%) because retailers bypass supplier markup. However, PL growth cannibalises branded, causing supplier margin pressure and potential delisting; Nestlé and P&G have repeatedly threatened delisting against aggressive PL pricing. Co-packing arrangements (outsourcing PL manufacturing) reduce capex but create supply concentration risk and quality inconsistency; multiple retailers sourcing from same manufacturer risks reputational contagion. Brand contribution analysis quantifies profit attributable to branded versus PL; sophisticated retailers model volumes, pricing, margin and promotional intensity separately. Exclusive brands (Sainsbury's Taste the Difference, M&S Collection) command 10-20% premium versus standard PL, driving differentiation in commoditised categories.

Brand extensions into adjacent categories (Tesco Clubcard into financial services, M&S into home insurance) have low penetration (2-5% of customers) but high margin (20-30% if successful), creating optionality requiring significant capex. Licensing revenue (third parties using brand for credit card, insurance, travel) generates high-margin recurring revenue (10-15% of licensing partner revenues at 5-8% take-rate); however, reputational risk (poor third-party service damages brand) requires careful partner selection. Private label quality standards and category exclusivity drive retailer margin enhancement; Waitrose's exclusive suppliers and M&S Food heritage enable premium pricing and higher margins than standard grocery.

RFR Valuation: Brand Value = Annual Revenue x Royalty % / (WACC - Growth %)

PL Penetration: UK Grocery 35-40% Value, 25-30% Volume | PL Margin 300-700 bps vs Brand

VIII. Grocery & Supermarket Economics

The Big Four UK grocery retailers (Tesco 27%, Sainsbury's 16%, Asda 14%, Morrisons 10%) control 67% of grocery spend. Tesco (65B revenue) is diversified conglomerate spanning food, F&F, telecoms, financial services, property; scale advantage yields 8-10% EBITDA margin. Sainsbury's (32B revenue) is pure-play grocery with financial services; 5-7% EBITDA margin reflects pure-grocery exposure and smaller scale. Asda (19B revenue, private equity-owned by Zuber Issa & TDR Capital since 2020) carries leveraged balance sheet (4B+ net debt) and pursues aggressive cost-cutting. Morrisons (16B revenue, acquired by Clayton Dubilier & Rice, 7B EV, 2021) is most exposed to discount disruption but has higher EBITDA margin (6-8%). Discount format disruption (Aldi 15B, Lidl 12B, combined 15% share) fundamentally altered grocery economics via limited SKU (1,400 versus 40,000), high velocity, private label focus (90%), real estate efficiency (6-8% rent versus 10-12%), and labour optimisation.

Aldi's logistics efficiency (central warehousing, regional distribution, direct-to-store) achieves 2-3% distribution cost versus 6-8% for supermarkets. Supermarket response is two-fold: defend value perception (Tesco Finest private label, budget ranges) and execute cost reduction (supply chain automation, private label expansion, store rationalisation). Loyalty programmes (Nectar, Clubcard) generate significant customer data and drive repeat and wallet share; Tesco's Clubcard database (15M+ active members) is leveraged for targeted marketing, reducing CAC versus national advertising. Fuel margin is <1% but drives traffic and basket size (+5-10 per transaction); fuel loss-leading during price wars (2015-2017) compressed grocery margin as retailers cross-subsidised. Fuel cap (government-imposed margin limits) was avoided post-Brexit but remains political risk.

Financial services arms (Sainsbury's Bank 10M+ customers, Tesco Bank 5M+) generate 15-25% pre-tax margins through deposit spreads and product cross-sell. However, capital requirements (8-10% Basel III) tie up 500M-1B+ per retailer; recent exits (Tesco sold c.50% to Barclays, 2019) reflect capital intensity versus retail returns. Pension liabilities are material; Tesco's defined benefit scheme carries 2-3B liability, Sainsbury's 1-2B, materially impacting cash flow. Property portfolio assets are material; Tesco owns c.70% of stores (5-8B asset value), Sainsbury's c.60% (2-3B), enabling sale-leasebacks to unlock value for deleveraging. Property optionality creates hidden value; underutilised stores can be repurposed (residential conversion, restaurants), creating value beyond grocery NAV. Structural headwinds include online grocery cannibalism (3-5% volume loss annually), Amazon Fresh disruption, premiumisation pressure, and sustainability costs.

Big Four + Discounters = Big Six: 82% of Grocery Market | Grocery Margins 25-28% Gross, 7-10% EBITDA

Supermarket vs Discounter Economics: Supermarket 25-28% Margin, 8-15K SKU | Discount 18-22% Margin, 1.4K SKU

IX. Fashion & Apparel Economics

The fast-fashion model (Inditex/Zara, H&M, Boohoo) fundamentally differs from traditional apparel through rapid design-to-shelf cycles (2-4 weeks versus 6-9 months traditional), low inventory holding, and high velocity sell-through. Zara operates 200+ design studios globally, refreshing 10,000-15,000 SKUs annually versus competitors' 3,000-5,000; agility enables Zara to pivot to trends within 4-6 weeks. Zara's vertical integration (owns 80% of production; competitors 20-30%) enables supply chain control and quality consistency, supporting premium pricing (35-60 versus H&M 20-40). Gross margins for Zara average 55-60% (retail) versus 45-50% for H&M, reflecting pricing power and operational efficiency. Seasonal buying calendars (Spring/Summer buy Feb-Apr, Autumn/Winter buy Aug-Oct) require significant inventory build; major retailer might build 15-20% above annual average in Q3, consuming 100M-300M working capital.

Boohoo's online-only model (15% initial gross margin, now 25-30%) prioritizes volume and customer acquisition over margin, operating at near break-even EBITDA (2-3% versus Zara 8-10%), creating leverage sensitivity. Size curve management is critical; garment manufactured in 5 sizes with demand distribution requires balanced production; over-producing mispriced sizes leads to excess inventory and forced markdown. Fabric sourcing, cost control and sustainability drive apparel margins; 30 retail price breaks down approximately: fabric 4-5 (15%), labour 2-3 (10%), logistics 1-1.5 (5%), marketing 3-4 (12%), overhead 3-4 (12%), margin 12-15 (40-50%). Labour cost inflation (5-15% per year) and sustainability requirements (2-4% cost) compress margins unless offsetting gains achieved.

Vertical integration (Inditex owns 40+ factories) enables supply cost reduction by 3-5% versus outsourcers but requires capex and operational complexity. Most apparel retailers outsource 70-90% of manufacturing to specialist CDMO providers, creating supply concentration risk; factory closure can destroy Q4 sales plans. Returns logistics is critical friction point; returning 30 item via reverse logistics costs 2-4, incentivising some retailers to absorb costs whilst others charge restocking fees. Returns rate variance (outerwear 25-30%, dresses 35-40%, shoes 30-35%) requires category-specific strategies. Seasonal sell-through targets are 85-90% at full price for premium (Zara, Next) versus 70-80% for mid-market, directly driving markdown waterfall and P&L outcomes. Exclusive distribution and wholesale partnerships drive apparel economics; wholesale discount is typically 60%, yielding lower retailer margin (44%) versus direct-to-consumer (60-70%).

Apparel Unit Economics: COGS 15%, Labour 10%, Logistics 5%, Marketing 12%, OH 12%, Margin 40-50%

Sell-Through Targets: Premium 85-90% Full Price, Mid 70-80%, Discount 60-70% | Markdown Waterfall 3-4 Tiers

X. Restaurants & Food Service

Restaurant unit economics vary by format (fine-dining, casual, quick-service). Typical casual dining restaurant (3-5M revenue, 120 seats, 1.5 covers per seat per shift) operates: food cost 28-32%, labour 28-32%, occupancy 10-15%, other variable 5-8%, fixed overhead 3-5%, yielding 5-15% EBIT. Casual dining chains (Nando's, Wagamama, Zizzi) achieve 10-15% EBIT through supplier scale, labour efficiency, and fixed cost leverage; private restaurants operate 2-8% due to limited scale. Quick-service restaurants (McDonald's, KFC, Subway, Pret) operate higher covers (2-3 per seat per day) and lower labour (18-22%), yielding 15-25% EBIT pre-ent at franchise level. Franchisee unit economics (QSR: 2-3M revenue, 40% to franchisor, 600-900K franchisee EBIT = 20-30% ROI) exceed corporate store economics. Like-for-like covers (customer counts) decompose into frequency and average spend, both critical metrics; cover decline is worse than pricing decline (volume loss not covering fixed costs).

Daypart analysis (breakfast, lunch, dinner, late-night) reveals economics variance; breakfast generates 35-40% of daily sales at 35-40% margin whilst evening generates 25-30% at 15-20% margin (higher waste on unsold perishables). Delivery aggregator dynamics (Deliveroo, Uber Eats, Just Eat) have fundamentally altered restaurant economics; aggregator commission (15-30% of order value) compresses restaurant margin by 400-800 bps. A restaurant earning 15% EBIT sees margin collapse to 6-12% when 25% of orders are aggregator. Customers acquired via aggregator have 50-60% repeat rate versus 70-80% for direct channels, reducing CLV. Aggregator orders represent 30-50% of restaurant volume in urban markets, making them economically unavoidable. Some restaurants respond via premium pricing on aggregator (+10-15%) or ghost kitchens (low-rent, delivery-only operations yielding 20-30% higher margin).

Ghost kitchen economics: 500-800K revenue per kitchen (versus 2-3M restaurant), 2-3M annual rent (versus 300-600K), 4-6 revenue streams (multiple brands per location), 20-30% EBIT; however, quality and brand fragmentation risk requires careful execution. Franchise economics in restaurants have changed; Subway (2,500+ UK locations) faced franchisee bankruptcy waves (2015-2020) as lease costs, supplier costs, and labour inflation eroded unit economics; recent turnaround included lease renegotiation and delivery integration. Location productivity is paramount; restaurant adjacent to train station generates 30-50% higher covers than suburban location; failed locations (leased at premium for peak demand) destroy franchisee equity. Lease negotiation flexibility is critical during downturns; many restaurants successfully renegotiated leases during COVID-19 obtaining rent holidays and flexible terms.

Casual Dining: 4M Revenue, 28-32% COGS, 28-32% Labour, 10-15% Occupancy, 5-15% EBIT

Aggregator Commission: Restaurant 15% EBIT - 25% Commission = 6-12% EBIT | 30-50% Volume Mix

XI. Luxury & Premium Positioning

Luxury retail (Hermès, Louis Vuitton, Rolex, Burberry, Gucci) operates on fundamentally different economics than mass-market retail. Gross margins reach 70-85% (versus 25-30% for grocery), reflecting pricing power, low promotional intensity, and minimal discounting. Pricing power stems from inelastic demand (high-net-worth individuals relatively insensitive to price), scarcity (production quotas), and heritage (brand value accumulated over decades). Hermès Birkin bag (retail 5-15K, waiting list 2-5 years, resale 10-30K) exemplifies luxury economics; artificial scarcity maintains pricing power and brand preference. Directly operated stores (DTC) are preferred for luxury, controlling 60-80% of sales versus wholesale 20-40%; DTC margin of 65-75% versus wholesale 40-45% drives brand preference and customer relationship control. Wholesale partnerships are selective; each represents 2-5% of brand sales but drives traffic and prestige positioning. Geographic mix is critical; Asia has grown from 15% to 30-40% of luxury revenue, driving capex in Chinese cities; however, political and regulatory risk create margin volatility.

Premium brands (Coach, Burberry, Hugo Boss, Mulberry) operate at gross margin of 55-70%, higher than mid-market but lower than ultra-luxury. Premium positioning enables pricing power versus mid-market (20-30% premium) but requires heavier marketing and store investment. Coach's turnaround (2017-2020) exemplified premium repositioning: raising entry-level pricing, closing wholesale channels, expanding flagship stores, increasing marketing spend. This strategy compressed revenue (down 15-20%) but expanded margin 500 bps. Burberry's turnaround (Marco Gobetti, 2017-2022) similarly involved 40% stocktake burn (destroying excess inventory), wholesale reduction (closing 200+ doors), and repositioning toward cool/aspirational, driving EBIT margin from 15% to 25%. Authenticity and heritage are critical; counterfeiting risk is material (50-60% of Hermès and Louis Vuitton sales globally are counterfeits), requiring supply chain transparency and authentication technology (NFTs, blockchain).

Aspirational luxury (tier below ultra-luxury, accessible to upper-middle-class: Ted Baker, Reiss, Jigsaw) operates at 45-55% gross margin; this tier has been squeezed between mass-market premiumisation (Zara, Uniqlo) and true luxury, creating structural valuation pressure. Direct-to-consumer shift (20-30% of sales to e-commerce) requires capex for logistics infrastructure but yields 60-70% margin versus 45-50% wholesale. However, DTC inventory risk is asymmetric; excess inventory consumes retailer balance sheet and margin through forced markdown. Luxury sector dynamics create opportunities for PE-backed consolidation and positioning; recent valuations reflect quality of portfolio brands, DTC penetration, and emerging market growth optionality. Regional strength varies significantly; Asia exposure (China especially) is material risk given political sensitivity to luxury positioning.

Luxury Margins: Ultra 70-85%, Premium 55-70%, Aspirational 45-55% vs Mass 25-30%

DTC vs Wholesale: DTC 65-75% Margin, Wholesale 40-45% | Asian Exposure Risk Given Political Sensitivity

XII. Valuation & Comparable Analysis

Retail valuation multiples vary significantly by subsector, driven by growth, margins, capital intensity, and competition. Grocery multiples range 5-7x EBITDA (reflecting 5-7% EBITDA margin, low growth, defensive stability); Tesco historically trades 6-8x, Sainsbury's 5-7x depending on momentum and debt levels. Specialty retail (apparel, homewares, footwear) trades 6-10x EBITDA; growth retailers (Boohoo pre-scandal 8-10x) command premium versus legacy (M&S 5-7x). Luxury multiples are 12-20x EBITDA, reflecting 15-25% EBITDA margins and brand intangibles; LVMH trades 15-20x, Hermès 18-25x. Discounters are rarely public; Ocado IPO (2010) trades 5-6x EV/Sales despite negative earnings, reflecting dark store platform optionality. Food-to-Go trades 8-12x EBITDA; Nando's parent private (valued >10x EBITDA in acquisitions), McDonald's franchisee 10-12x. Valuation bridge analysis is critical; if Tesco trades 6.5x and Target (US) trades 6x EBITDA despite Target's 20% higher margin, spread reflects UK regulatory/lease risk. EV/Sales multiples (1.5-2.5x grocery, 3-5x specialty) are useful for loss-making retailers (IFRS 16 distorts EBITDA).

Sum-of-the-parts (SOTP) valuation is critical for diversified retailers (Tesco food/F&F/financial services/property; Sainsbury's grocery/financial services; M&S clothing/food/property). SOTP approach (grocery 5x EBITDA, F&F 7x, financial services 12x, property NAV, sum and deduct net debt) often yields higher equity value than blended multiple, highlighting optionality from unlocking undervalued segments. Tesco's property monetization (sale-leaseback of 1,000+ stores, 2-3B cash) was valued as 15-20% hidden value. Franchise models command premium multiples due to capital-light, recurring revenue characteristics; Domino's franchisee trades 15-18x EV/EBITDA versus 11-13x corporate-owned, reflecting capital efficiency. Omnichannel retailers (Next, Asos, Zalando) trade 8-12x EBITDA despite lower net margins (3-5%) versus bricks and mortar, reflecting growth and working capital benefits. Pure-play e-commerce (Boohoo, Shein, Farfetch) trade extreme multiples when growth sustained (10-15x revenue

growth justifies 5-8x EV/Sales even at negative EBITDA), but compression severe when growth slows.

Comparable selection requires careful sector definition; comparing Tesco (70% grocery) to Sainsbury's (85% grocery) is appropriate; comparing either to Next (pure apparel, 60% online) is misleading without adjustment. Geographic arbitrage creates valuation variance; UK grocery trades cheaper (5-7x) than US grocery (6-8x) reflecting UK regulatory burden, lease cost, and competitive intensity. Currency effects can temporarily distort multiples for multinational retailers; Inditex (Zara parent) gets 60%+ revenue from international, creating currency hedging requirements and reported earnings volatility. Activist investor engagement often targets valuation multiples, arguing for SOTP structure, dividend increases, or strategic M&A; these campaigns generate 15-30% total return through price appreciation as multiples re-rate on operational improvements.

Multiples by Sector: Grocery 5-7x, Specialty 6-10x, Luxury 12-20x, Discounters 7-9x | EV/Sales 1.5-2.5x Grocery

SOTP Structure: (Seg1 EBIT x Multiple1) + (Seg2 x Multiple2) + Property NAV - Net Debt = Equity Value

III. Private Equity Value Creation

Private equity acquisition of retail targets operco/propco structures to unlock value. Typical LBO acquires 2B EBITDA retailer at 6x (12B EV, 10B debt, 2B equity), then separates property (3-4B NAV) into propco, selling bonds to refinance opco debt and extract 1-2B dividend to sponsors. Post-separation, opco deleverages via EBITDA growth while propco generates stable rental yield (4-6%). Store rationalisation is primary EBITDA lever; closing 10-15% of stores (low-ROIC, high-occupancy-cost locations) unlocks 200-500M annual EBITDA with minimal capex or customer disruption, as remaining stores capture closed store sales and reduce overhead. Private label expansion (shifting 5-10% of sales to PL, capturing 300-500 bps margin improvement) adds 50-150M EBITDA for mid-cap retailer. Supply chain optimisation (DC consolidation, automation, SKU reduction) yields 2-4% COGS reduction, 100-300M EBITDA uplift.

Omnichannel investment (dark stores, click-and-collect, unified inventory) requires capex but improves customer retention and margin through reduced delivery cost. Data monetisation (customer data licensing, advertising partnerships) generates 20-100M annual high-margin recurring revenue for large retailers with 10M+ customer base. International expansion (replicating model in new markets) requires significant capex but offers growth upside and multiple expansion. Bolt-on M&A is common (Sainsbury's Argos, Tesco F&F, Carrefour Dia), providing immediate revenue/EBITDA uplift, leverage paydown, and strategic optionality. Synergy quantification (shared logistics, procurement scale, overhead absorption) assumes 10-20% cost reduction on acquired COGS and SG&A. 300M revenue bolt-on at 8% EBITDA (24M) with 15M synergies yields 39M EBITDA (1.6x multiple compression).

Management incentivisation (roll-overs, earnings, options) is critical; misaligned management (seeking liquidity exit versus PE sponsor seeking 5-7 year value creation) has destroyed value (Morrisons acquisition 2021 saw management contracts renegotiated post-close). Leverage is critical constraint; retailer with 5-6x total leverage has minimal debt paydown capacity; sponsors must engineer EBITDA growth or propco refinancing to delever. Recent retail PE valuations remain elevated (5-7x despite margin pressure and online cannibalism); sponsors rely on significant operational leverage to achieve return targets, creating risk if economy deteriorates or online penetration accelerates.

EBITDA Value Bridge: Entry EBITDA + Store Exit + PL Expansion + Supply Chain + Omnichannel + Bolt-ons = Exit

Propco Dividend: Property NAV (3-4B) → Bond (3-4% yield) → Opco Debt Refinance (4-5%) → Sponsor Dividend

IV. Due Diligence Red Flags

Declining like-for-like sales (negative LFL for 2+ consecutive years) signal structural headwinds and potential further deterioration. Tesco's LFL decline (2011-2013, avg -2%) led analyst downgrades; subsequent recovery (2013-2019, avg +2%) validated repositioning. Rising inventory relative to sales (inventory days increasing 2+ weeks YoY) signals demand softness and obsolescence risk; Boohoo's inventory spike (2020, +25% on flat revenue) foreshadowed Q1 2021 markdown disaster. Occupancy cost ratio creeping upward (8% to 10%) with flat revenue signals lease renegotiation failure or store mix deterioration toward lower-productivity locations. Customer concentration risk (top 10 customers >40% of sales) is material in B2B retail; losing major customer can destroy 5-10% of revenue. Pension liabilities (gross underfunding >50% of equity value) consume cash and constrain strategic flexibility.

Promotional dependency (high discount frequency, limited full-price mix) signals brand weakness and margin compression; Debenhams' spiral into administration accelerated as increasing promotional intensity (70% at discount) destroyed margin and equity value. Capex underinvestment (capex <80% of depreciation) signals deferred maintenance, store ageing, and competitive disadvantage; retailers deferring renovations 2-3 years see customer defection. Supplier concentration risk (>50% of COGS from top 5 suppliers) creates negotiation risk and supply disruption exposure; food retailers sourcing 80%+ from Nestlé/P&G face margin pressure. Shrinkage inflation (growing faster than sales inflation) signals control failures and organised retail crime; 0.5-1% spike consumes 30-50% of EBITDA growth. Lease maturity cliffs (30%+ maturing within 2-3 years) create refinancing risk; landlord pricing power demand creates 100-150 bps occupancy cost jump.

Labour cost inflation outpacing pricing power (wage inflation 5-7% versus pricing 2-3%) compresses margin 100-200 bps annually; 5B retailer with 20% labour cost sees 100-200M annual margin erosion without productivity gains. Technology debt accumulation (aging POS, fragmented omnichannel, poor data integration) creates capex liabilities and competitive disadvantage; legacy retailers' inability to execute seamless omnichannel (Debenhams, BHS) contributed to failure. Customer NPS decline (dropping 5+ points YoY) is leading share loss indicator; retail turnarounds (Tesco CEO Dave Lewis, 2014-2019) are announced with NPS recovery roadmaps. Store returns showing negative ROIC or cash flow, increasing frequency of store closures, and declining traffic indicate fundamental demand deterioration.

Red Flags: LFL < -2% (2yr), Inventory +2-3 weeks YoY, Occupancy > 11%, Shrinkage > 1%, ROIC < 5%

Structural Issues: Pension >50% Equity, Capex <80% Depreciation, Supplier Conc >50%, Labour Inflation > Pricing

XV. UK Grocery Deep Dive: Market Structure & Economics

Tesco commands ~27% UK grocery market share, making it the clear leader with approximately GBP 60 billion in UK sales. Its Clubcard loyalty programme captures data on ~80% of transactions, enabling targeted promotional efficiency and a retail media business (Tesco Media & Insight Partners) generating estimated GBP 100-200m revenue at high margin. Tesco's property portfolio includes substantial freehold estate valued at ~GBP 12-14 billion, creating opco/propco optionality. Booker (wholesale arm, acquired 2017 for GBP 3.7bn) adds B2B distribution serving independent convenience stores and catering. Tesco Bank provides financial services cross-sell. In DD for grocery M&A, the key analysis is market share stability by format: Tesco's share is most vulnerable in convenience (competition from Co-op, discounters) and least vulnerable in large-format supermarkets where scale advantage in range and parking is defensible.

Aldi and Lidl have been the structural disruptors of UK grocery, growing combined share from ~5% in 2010 to ~17-18% by 2024. Their model is fundamentally different: limited assortment (1,500-2,000 SKUs vs. 25,000-40,000 in a Tesco Extra), ~90% private label, minimal staffing levels (4-5 staff per store vs. 15-20 at traditional grocer), no loyalty cards, simple store format with low fit-out cost (GBP 5-7m vs. GBP 15-25m for a traditional grocer), and aggressive pricing (15-25% below Big Four on comparable basket). Their growth has compressed sector margins: UK grocery EBITDA margins fell from 6-8% (2005) to 3-5% (2024) partly due to discounter pricing pressure. Asda under TDR Capital ownership is attempting to bridge the gap through Project Future (convenience, online, price investment), but faces execution risk.

Fuel margins are a significant but volatile contributor to grocery profitability. UK supermarket fuel generates ~GBP 20-40bn collective revenue but at very thin margins (1-3 pence per litre, compared with 5-8p/l at independent forecourts). Supermarkets use fuel as a footfall driver (loss leader or near-break-even) rather than a profit centre. In financial analysis, always strip out fuel from LFL calculations to see underlying food performance. GSCOP (Groceries Supply Code of Practice) regulates the relationship between large retailers and suppliers in the UK; the Groceries Code Adjudicator can fine retailers for breaching the code. Key GSCOP risks in DD: retrospective cost-price changes, delay tactics on supplier payments, delisting threats, and forensic accounting of supplier rebate arrangements.

XVI. Fashion, Apparel & Luxury Specifics

Fast fashion operates on compressed design-to-shelf cycles: Zara's vertically integrated model achieves 2-3 week cycles from design to store (vs. 6-9 months for traditional fashion). This speed allows Zara to test trends in small batches, read real-time sell-through data, and reorder winners quickly while minimising markdown risk on losers. The model requires proximity manufacturing (Zara uses Spain, Portugal, Morocco, Turkey rather than Far East), higher per-unit production cost offset by lower markdown cost, and sophisticated demand-sensing analytics. In DD for fashion targets, benchmark the design-to-shelf cycle time, first-price sell-through rate, and terminal markdown depth against Zara as the gold standard. Next plc (UK) achieves an impressive 70%+ full-price sell-through rate through disciplined buying, rapid in-season trading, and an effective outlet channel.

Luxury retail (LVMH, Kering, Hermes, Richemont) operates under fundamentally different economics: gross margins of 65-75%, EBITDA margins of 25-40%, pricing power that exceeds inflation, and brand heritage that creates multi-generational consumer loyalty. Luxury valuation is driven by organic revenue growth (target 6-10% pa), geographic diversification (especially exposure to China, which represents 30-40% of global luxury demand), directly operated store (DOS) mix vs. wholesale (higher DOS = better margin control and brand experience), and category diversification (leather goods, watches, beauty, wines/spirits). Key luxury metrics: average selling price (ASP), revenue per square metre in DOS, comparable-store sales growth, and client acquisition cost. Hermes trades at 45-55x forward P/E reflecting unmatched brand desirability and pricing power; LVMH at 20-28x; Kering at 12-18x (more cyclical fashion brands).

Size curve management is a technical but commercially critical aspect of apparel retail. A size curve specifies the quantity of each size (XS through XXL) ordered per style, based on historical sales data by category and market. Incorrect size curves lead to over-stocking in unpopular sizes (creating markdowns) and stock-outs in popular sizes (lost sales). Best practice: analyse sell-through by size at SKU level, adjust size curves quarterly, and use post-season residual stock data to refine future buys. Return rates in online fashion are 25-35% (vs. less than 5% in-store), and the primary driver of returns is fit/sizing issues. Bracketing (customers ordering multiple sizes and returning the wrong ones) inflates CAC and destroys online unit economics. AI-powered size recommendation tools (e.g., True Fit, Fit Analytics) can reduce return rates by 3-5 percentage points.

XVII. Restaurants, QSR & Food-to-Go

Restaurant and quick-service restaurant (QSR) economics centre on four-wall unit profitability. A typical QSR unit generates GBP 800k-1.5m revenue with 30-35% food cost, 25-30% labour, 8-12% rent, and 8-15% EBITDA. Managed restaurants carry all costs on the operator P&L; franchised restaurants pay 4-6% royalty plus 2-4% marketing fund contribution but bear their own P&L. Franchise models are capital-light for the franchisor (franchisee funds capex) and generate high-margin recurring royalty income. Key metrics: average unit volume (AUV), same-store sales growth (SSSG), restaurant-level EBITDA margin, new unit payback period (target less than 3 years), and unit closure rate (should be below 2-3% per annum).

Delivery aggregators (Deliveroo, Uber Eats, Just Eat Takeaway) have transformed the restaurant sector since 2015. Aggregator commission rates of 25-35% of order value compress restaurant margins significantly; a restaurant with 65% gross margin before delivery loses 25-35 percentage points to the aggregator, leaving 30-40% gross margin on delivery orders vs. 65% on dine-in. Many restaurants are delivery-unprofitable but participate to maintain customer relevance and incremental revenue. Ghost kitchens (delivery-only kitchens with no customer-facing space) reduce rent costs by 40-60% but are entirely dependent on aggregator platforms for order flow, creating platform dependency risk. DD for restaurant chains must model the channel mix (dine-in, takeaway, delivery) and the margin profile of each channel separately.

Daypart analysis breaks down revenue by time of day: breakfast (6-11am), lunch (11am-2pm), afternoon (2-5pm), dinner (5-9pm), late night (9pm-close). QSR profitability depends heavily on utilising the fixed cost base across multiple dayparts. McDonald's breakfast launch in the UK added ~15-20% to daily AUV by unlocking the morning daypart. In DD, analyse revenue per trading hour by daypart, identify underutilised dayparts, and model the revenue uplift from menu innovation targeting weak periods. Labour scheduling optimisation (matching staff hours precisely to demand curves) is a primary PE value creation lever in managed restaurant businesses, typically delivering 100-200bps of margin improvement.

XVIII. Consumer Retail Glossary

Achieved Margin: Gross margin after shrinkage, markdown, promotions. **Aspiration Luxury:** Accessible upper-middle-class segment. **Category Management:** Supplier collaboration optimizing assortment. **Click-and-Collect:** Online ordering with in-store pickup. **Concession:** Brand shop-in-shop, 10-15% rent. **Daypart:** Time-of-day revenue/margin analysis. **Direct-to-Consumer:** Direct brand selling, eliminating wholesale. **Dark Store:** Automated delivery warehouse. **DPO:** Days Payable Outstanding (supplier terms). **Four-Wall P&L:** Store-level profit excluding corporate OH. **Ghost Kitchen:** Delivery-only, low-rent kitchen. **Intake Margin:** Vendor markup pre-markdown. **Loyalty:** Customer rewards program. **Markdown Waterfall:** Progressive price reductions. **Occupancy Ratio:** Rent as % of sales. **Private Label:** Retailer-branded, 3-8% higher margin. **Relief-from-Royalty:** Brand valuation method. **ROIC:** Return on Invested Capital. **Sale-Leaseback:** Sell property, lease back. **Sell-Through:** Full-price units sold / received %. **Shrinkage:** Inventory loss (0.5-2%). **SKU:** Stock Keeping Unit (product). **Vertical Integration:** Brand manufacturing ownership. **VMI:** Vendor-Managed Inventory. **Weeks of Cover:** Inventory value / weekly COGS.