AN OVERVIEW OF HOUSEHOLD CONSUMPTION AND EFFECTS OF CRISIS ON RETAIL TRADE IN CROATIA

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Abstract
Indicators of private or household consumption are the basic indicators of the conditions in the national economy and the basic indicators of economic deprivation. This paper will discuss the data on household consumption available in the official statistics in Croatia. Also, it will discuss the data on the structure of personal consumption from which undoubtedly is obvious that in times of crisis majority of population is oriented to satisfaction of basic needs. On the other hand, retail is an industry that responds to the economic crisis faster than other industries because it is directly linked to personal consumption. Thus, due to the reduced consumption in households, indicators of business activity in the retail trade shows a negative effect not only through the reduction of generated income, but also through changed way of behavior of the majority of consumers, which consequently leads to changes in the retail structure. Specifically, it is clearly visible that the sales formats with the lowest margins occupy an increasing share of the market. Therefore, in this paper change in the retail trade is analyzed as well.

Keywords: consumption, crisis, poverty indicator, retail, Croatia

Topic Groups: Social sciences and business; Industry, area or region specific studies

INTRODUCTION
The global economic crisis, which reached its highest intensity on a global level achieved in period 2008-2013, had affected all aspects of economic activities. In the sector of distributive trade the most obvious consequences are: the loss of purchasing power of citizens, changes in consumers’ purchasing behavior and, consequently, changes in the business strategies of individual companies in the sector.

Although, many scientists dealt with the problems of the economic crisis measurements and effects of global economic crisis, there is a scarcity of papers dealing with the impact of the economic crisis on individual industries, and, especially, in the markets of the newer members of the European Union.

As reduced consumption have a direct detrimental impact on retail trade, this paper will focus on the retail trade in the newest EU member state – Croatia. In the paper we will describe how
the reduction and restructuring of household consumption during the economic crisis is affecting the retail trade in Croatia.

The paper is divided into two sections. The first is based on publicly available official statistics and explains the movement of household consumption and the structure of household in Croatia. While the second part of the paper explains the changes caused by the economic crisis the two levels: (1) changes in consumer behavior, and (2) changes in the structure of retail trade. The second section is based on secondary data retrieved from official statistics, but also from research papers treating various topics related to retail industry in Croatia.

**THE STRUCTURE OF HOUSEHOLD CONSUMPTION IN CROATIA AS AN INDICATOR OF THE ECONOMIC CRISIS**

Available data gathered in The Household Budget Survey conducted by Croatian Bureau of Statistics show that the average annual consumption expenditures per one household are decreasing due to deep economic crisis taking place since 2008 (see Table 1). Contemporarily, one household in Croatia spends less than 10000 euros per year for final consumption.

**Table 1: Average annual consumption expenditures per one household in Croatia**

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<td>Consumption expenditures in HRK</td>
<td>76,188.00</td>
<td>75,167.00</td>
<td>74,941.00</td>
<td>-1,247.00</td>
<td>-1.64%</td>
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<tr>
<td>Consumption expenditures in EUR</td>
<td>10,024.74</td>
<td>9,890.39</td>
<td>9,860.66</td>
<td>-164.08</td>
<td>-1.64%</td>
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*Source: CBS (2012a)*

Moreover, the official statistics relentlessly shows an extremely unfavorable structure of personal consumption in Croatia where from 2008 to today an increase in the share of food and non-alcoholic beverages in total consumption is observed. This share is now around 32%. Thus, one third of the average household budget in Croatia serves merely to meet the most basic needs of life i.e. foodstuff and non-alcoholic beverages. Second in importance are housing expenditures and energy (with a note that the index does not include the rent) which also in the same period increased share in the average household budget and today is around 15% of the average household budget. Shares of individual product groups in total consumption of households in Croatia are shown in Figure 1.
If we sum up the two mentioned indicators, we can conclude that in Croatia almost a half of the average household budget is spent on food and housing expenditures and in most households there is a little room left to meet some secondary or tertiary needs. All this tells us that the average household in Croatia focused on mere survival, with fewer acquisitions of goods such as, for example: household appliances, consumer electronics, branded apparel and footwear, furniture and services in the field of hospitality and education.

In Figure 2 the share of the most basic life necessities in Croatia and in some selected EU countries is shown. Based on Figure 2, we can conclude that the Croatian household, compared to the newer EU member states is, in fact, in a very difficult situation. While in the average Austrian, Slovenian and even the Hungarian household, after obtaining food and paying housing costs (excluding rents and loans) remains between 60 and 70% of the household budget, for the average Croatian household it remains little more than half out of which the household has to purchase the clothes and shoes, to pay transportation costs, to pay medical services, and to pay costs for their children's education.

Furthermore, according to CBS (2012a) data, to households in Croatia almost no space remains for long-term investment. Official data shows that for this purpose is allocated up to 7% of total expenditures in the household. While, for instance, in Slovenia the long-term investments are 9.72% of the total household expenditures, in Austria 10.31%, and the Czech Republic 8.36% (according to OECD.Stat data). We have to point out that there are some
doubts regarding the methodology of CBS, but in this paper we will not get into debate on CBS methodology, but we will use available CBS data as is.

**Figure 2**: Comparison of the share of the basic necessities in household consumption in 2011

![Graph showing share of basic necessities in household consumption](image)

*Source: For Croatia – CBS (2012a); for other countries – OECD.Stat (2015); own compilation*

According to all the displayed data, we can argue that the personal consumption reached a bottom and there is no space for its further decrease in Croatian households because majority of Croatian households focuses on the satisfaction of basic needs. In addition, the analysis of poverty indicators is telling us that Croatia, compared to other selected countries, is in a very unenviable position because it has high rate of poverty risk, which further reinforces the negative trends in personal consumption of households (see Figure 3). Unfortunately, due to the economic crisis taking place across EU, the risk of poverty is getting deeper and deeper (see Figure 4).
Moreover, data of the Independent Trade Union surveys in Croatia are not encouraging because they claim that the average wage in Croatia can cover only 80% of monthly living expenses, and the pensions can cover only around 60% (CITU, 2013). And if this situation continues, there a significant number of households will be brought to a situation that basic needs cannot be satisfied.
EFFECTS OF CRISIS AND REDUCED CONSUMPTION ON RETAIL TRADE IN CROATIA

A change in final consumption and ongoing and long-term economic crisis together with the problem of deepening poverty in given geographic market puts many challenges in front of retail companies. In advance we will describe some of challenges for retailers in Croatia. We will explain two levels of changes: (1) microlevel focusing on changes in consumers’ behavior and (2) macrolevel focusing on consequential changes in retail structure in Croatia.

Changes in Customers’ Behavior

A large proportion of citizens in Croatia are negatively influenced by ongoing economic crisis. Basic economic indicators (CBS, 2009 and 2014b) show that unemployment rate grew from 13.2% in 2008 to 20.2% in 2013. At the same period average wages remained almost the same (in 2008 average net wage was 5178 kunas or 681 EUR, while in 2013 average net wage was 5178 kunas or 726 EUR; which means that annual growth was only 1.3%). At the same period consumer prices grew continuously (see Table 2). Taking all of this into account, relatively, customers are getting poorer and poorer.

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<th>Table 2: Chain indices of consumer prices in Croatia</th>
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Source: CBS (2012b, 2014b)

When the Maslow pyramid is discussed in retail management and retail marketing literature, then it is always in relation with markup possibilities. Counting on a high number of customers trying to satisfy their basic needs i.e. economy of scales, and due to high number of retailers serving similar purposed i.e. increased competition, retailers will apply lower markups in product categories serving to customers’ basic needs. While to product categories which are promoted to serve higher level of customers’ needs (according to Maslow’s pyramid, see Figure 5), the focus will not be on price competition but on qualitative values, and therefore, in those product categories retailers will usually apply higher retail markup rates. The higher retail markup rates combined with a large number of consumers that are actually purchasing products, the higher profitability of retailer is generated as a consequence.
Figure 5: Maslow’s pyramid of needs

Deficit in satisfaction of basic needs

Source: adapted according to Maslow (1943)

In the time of recession when customers are focused on low level of needs and where are a decreasing number of customers that can afford satisfaction of higher levels of needs, not only profitability of retailers is directly affected, but also their revenues are brought to a question. And a large number of retailers are brought into a vicious cycle of lowering business activities. There are several relationships in retailing system which can contribute to the depth of the crisis at a certain marketplace and understanding of them can be of a great importance when retailers are searching for a way to survive. In Figure 6 the simplified model is given showing that layoffs and wage decrease at a certain market will, inevitably, lead to the pressure on retail prices and retailer will have to make corrections of markup rates. As markup rates in retail serve to cover operating costs, retailer will be forced to think how to lower this costs which in most cases means that he will decrease wages to his workers and/or layoff some of his workers and in that way in local market crisis is increasing and a contribution to pressure on retail prices is made.

Moreover, lower markup prices and reduced number of financially stable customers brings us to situation of lower revenues and lower profitability. Low profitability is a new pressure to cut operating costs and retailers is brought to a new situation of deciding on wages and/or layoffs. On the other hand, when retailer is facing a low profitability, he is forced to rationalize his supply chain, and, unfortunately, rationalization of supply chain often means a mere pressure on suppliers to cut input prices. This after some time, on suppliers’ side, will lead to new layoffs and/or wage decrease. And the consequence will be a new pressure on retail prices.
But, the tragedy of the vicious spiral effect is that low profitability means a low possibility to invest into activities that can bring structural changes. Therefore, a deep recession is deepening more and more if some external impact isn’t made at some point. That external impact can be: a government intervention into labor market; innovation impulse to change procedures, services, products; availability of financial support from financial institutions or investor for structural changes etc. But in this paper external impacts are not in our focus.

There are various actions taken by retailers in order to survive in the market and in order to keep profitability above zero values. Some of them are searching and applying new channels to communicate with customers so they are applying multichannel principles throughout implementation of channels with low transaction costs, others are applying innovative techniques in supply chains and intensively are searching for logistics effectiveness in strategic cooperation with suppliers, and some of them are intensively promoting private labels in order to gain overall control on all aspects of merchandize. And some research results (see in Petljak, Stulec and Renko, 2011) show that in time of recession there is a respective growth of private labels in the average consumer basket. This brings us back to the fact that customers are searching for products with the price as low as possible.

This fact is empirically supported by Anic (2010). His research results on consumers in Croatia show that the high proportion of price-sensitive consumers are those with lower incomes and lower levels of education. Moreover, when concerned for their own financial situation, consumers become even more price-sensitive. When they make decision in which

**Figure 6: Impact of Recession on Retail – Vicious Circle(s) of Retail in Recession**

![Diagram of Impact of Recession on Retail](source: own work)
store (of the foreign retailer) to purchase in, they tend to prefer the price-oriented retailers, while this is not the case when they are deciding on locally owned retailers. In addition, price-sensitive consumers show a great loyalty to a couple of preferred retailers, but they are spending less money per one purchase in stores of their preferred retailer.

We have to point to other facts regarding contemporary customers that influence and change retail strategies all over the world. Ridderstrale and Nordstrom (2007) claim that contemporary customer is “a mother of all dictators!” because he/she wants to satisfy his/her individual need with personalized products or services and he/she is completely aware that it is possible in terms of a real time. This is the consequence of a growing competition in all markets all over the world. Customers have a huge possibility to instantly get substitutes of products, services, retail outlets, and retail channels and so on. Moreover, he/she is not afraid to intensively use information technology in all phases of purchasing. Prior purchasing, he/she is collecting information, comparing prices, then he/she is deciding how to purchase within the traditional or online store or even combining those two. At the end, after purchasing, he/she share information on products, services, retail outlets, retail experiences throughout social media, but also he/she is searching for additional support regarding the usage of purchased products or services. So, actually retailers are facing very well informed, involved and disloyal customers and they have to predict it in their retailing strategies.

Another thing to take into consideration in a future development in retail is an increased awareness of consumers of sustainability concepts in retailing. As some studies shows, in Croatia consumers react positively on corporate social innovations applied in retail outlets and, consequently, retailers in Croatia apply a wide spectrum of initiatives in the field of corporate social responsibility (see Renko et al., 2010 and Sutic et al., 2012). For instance they make various donations to local communities, they provide products to socially endangered population during the Christmas and Easter season, they introduce environment-friendly shopping bags, they organize events in order to promote healthier lifestyle, etc.

**Changes in the Retail Structure**

Due to all previously described changes on micro level, on macro level we can observe that the retail structure is changed as well. In Figure 7 the structure of retail market is shown. It is obvious that winners in the time of recession are hard discounters because their market share doubled from 2008 till 2013. In the same period, the share of hypermarkets grew as well but only for 7% in given five years. In such environment, small shops and supermarkets are two retail formats which in the crisis suffered the most. In given period small shops lost 9% of market share, while supermarkets lost 6% of market share. All in all, we can conclude that consumers are turning to shopping formats which offer a larger variety of products combined with lower markups and, thus, lower prices.
Moreover, Knego and Knezevic (2012) explain problems that small retailers are facing in Croatia due to economic crisis, those are: (1) significantly lower labor productivity measured by gross turnover per employee compared to medium-sized and large retailers, (2) lower inventory turnover ratio, which increase the cost of financing inventories and increase operational costs, (3) unfavorable conditions due to inability of obtaining the benefits of economies of scale,(4) low gross margin and low markups which shrinks their possibility of investment in technological modernization of their retail outlets, and (5) as a result of all previously mentioned problems, they have to offer higher prices comparing to larger retailers. All those problems are deepening in the situation of market concentration and increased internationalization of retail market so we can expect even harder situation for small retailers in the near future. So, in the future they will have to make significant changes in their overall business strategies trying to differentiate not by prices but by quality of service, personalization of assortment to narrow niches, by redesigning layout of shops, choosing more favorable locations, finding strategic partners at supply side and so on. For instance, Knego, Vouk and Petljak (2014) give some suggestions regarding location and layout that can be applied by small retailers in order to survive at the market.

We have to point out that, according to data in Figure 7, there was a significant growth in “other formats” of retail. This category includes: traditional marketplaces of local community, door to door retail, vending machines, TV sales and e-commerce. Unfortunately, at the moment we do not have a detailed insight into the structure of the other category and in future research this category should be scrutinize more in order to see which format Croatian consumers are converting to: are they turning back to their local marketplaces or do they prefer e-commerce as a new retail channel?

In addition to mentioned changes, there is one new format that is situated between traditional retailing or traditional food supply chains and final users of food within a socially endangered population, and that is a social supermarket. The first social supermarket in Croatia was opened in Split in 2009.
Social supermarkets have the main purpose to serve those groups of customers which have low income or which are unemployed. Holweg and Lienbacher (2011) define social supermarkets as food oriented retailers selling food to a restricted group of people living in or at risk of poverty. Maric (2013) claims that social supermarkets are social innovation which comprises social responsibility of associated individuals with an aim to show social solidarity towards socially vulnerable persons or families towards collection and distribution of goods that are collected from individual donors, large retail chains and/or other companies. Therefore we can say that in the very essence, they are nonprofit organizations which base their activity on volunteerism and charity and if they generate any profits they use them to promote charitable activities. At the moment, there are more than 15 social supermarkets operating in Croatia and on monthly level there are new initiatives taking place in this field of operation.

Holweg and Lienbacher (2010) explain that social supermarkets can be positioned as a linkage within reverse logistic systems trying to reduce food waste and to redistribute food surpluses which occurs in the traditional food supply chains.

Maric and Knezevic (2014) explain that social supermarkets, as a retail format, are of similar size as conventional supermarkets or as convenience stores and that they are serving a local community in narrow geographic area, offering food as a key part of merchandize. But their assortment is much narrow and shallow comparing to mentioned retail formats because it heavily depends on collected donations within a certain period. If they are not organized in order to distribute goods for free, then their pricing policy is comparable to hard discounters, because they offer significantly lower prices comparing to other retail stores (what is an analogy to the policy of EDLP – Every Day Low Prices). Therefore, at some markets there is observed collision between hard discounters and social supermarkets because, to some point, they are targeting similar group of customers or users. So in the near future this is the topic to pay attention to in further retail research.

CONCLUSIONS

The ongoing economic crisis had a detrimental impact on household consumption in Croatia. In period 2008-2013 unemployment rate grew, but average net wages almost remained almost at the same level. Moreover, at the same period consumer prices grew continuously. The household consumption in absolute values reduced and changed in structure. At the moment, almost a half of the household budget is serving to satisfy the most basic needs.

This brings many challenges in front of retailers operating in Croatia because their profitability is directly affected and often they are caught in a vicious cycle of lowering business activities. On the other hand, consumers are becoming more and more price sensitive and conscious regarding purchasing, which can lead retailer to implementation of policies oriented towards cutting prices and cutting operational costs, and that means speeding up in the vicious circle.

In the paper we have pointed out that retail formats oriented towards a larger product variety at lower prices are gaining the marketshare in situation of economic crisis. Both, the hypermarkets and hard discounters grew in market share in Croatia since 2008, while supermarkets and small shops suffered the most. Another thing that we brought attention to, are social innovations that in the future could have an impact on retail revenues if the crisis
continues, and those are social supermarkets as a form of food distribution to socially endangered citizens.

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