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Will the Sainsbury's-Netto tie-up work?

Jean-Paul Sartre famously wrote in a play that "hell is other people". Some might say that if other people are hell, then joint ventures come a close second.

Braving such claims, Sainsbury's recently announced a joint venture with Netto, to launch later this year and reach 15 stores by the end of next.

Apparently, this will bring Netto's systems, infrastructure and low costs together with Sainsbury's UK grocery, sourcing and property expertise in a "compelling customer proposition".

At least some of the new stores will be adjacent to an existing Sainsbury's store, albeit with a separate entrance. All the shops will be branded Netto – hence the compelling customer proposition.

So Sainsbury's is to dabble in discounting, but have it run separately by another discounter.

Not many full-service, quality retail chains have themselves successfully run a discount version. Argyll/Safeway had a discount chain, Lo-Cost, which was run separately.

I remember that whenever Safeway tried to get logistics, buying, IT or any other synergies with Lo-Cost, the latter's costs would always rise because the 'quality' operator started from a higher cost base and had a different attitude towards risk and reward.

It is not so surprising that Sainsbury's is contemplating these Netto stores being so close to its own. When discounters first came into the UK in the early 1990s it became clear that it was better to have one right next to a superstore than to have it a kilometre away.

Sainsbury's and Netto will open the first stores in their joint venture this year

Alongside, they would drive extra footfall, some of which would still come into the bigger neighbour, thereby offsetting some of the attrition. Further away, the effect was just lost sales.

However, questions may be raised about approaching it as a joint venture. Joint ventures always work best when each party brings something sustainably distinctive and unique, yet contributes roughly equally in total.

In this case, both parties are already great retailers with scale, efficiency and skill. Of course, Netto can teach Sainsbury's how to discount and Sainsbury's can give Netto – and the Netto brand – a way back into the UK. Neither of these sound like long-term advantages for the other.

The economics are tough for Sainsbury's. The net margins will be very low for the fledgling discounter, and it will undoubtedly steal significant sales from Sainsbury's.

So Sainsbury's will lose full-margin sales, to be replaced by lower margin discount sales. The discounter will grow sales by gaining share from other grocers, but any resulting profit is then immediately halved because it is shared.

All this and £13m extra investment and £5m to £10m start-up losses this year. At least it is not exactly a Fresh & Easy level of investment.

Sartre's play, by the way, was called *No Exit*, and featured three characters locked in a room for eternity. The point was that there was no way out. And that's the often neglected essential of any joint venture. Make sure there's an elegant exit.

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