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Spanish Retailer Bucks Trend

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MADRID—Spain's unemployment rate is near 25%, retail sales have declined for 25 straight months and the country is edging closer to an international bailout.

Yet supermarket chain **Mercadona** SA hired 6,500 employees last year, more than any Spanish company, and its sales increased 8% and remain on the rise.

The secret to its success: a German-style recipe for higher productivity that includes flexible working conditions, extensive employee training and performance-linked bonuses—a rare mix in Spain.

As a result, the family-controlled retailer fast is becoming a model in a country urgently trying to rewrite the rules for its economy.

European Pressphoto Agency

'Eliminate anything that doesn't add value,' says Mercadona's Juan Roig.

A decade ago, corporate Germany struck a deal with employees who agreed to work more hours and for wages growing more slowly than productivity. In return, workers won job security, even in lean times. Labor costs fell 1.2%, while productivity rose 9% between 1999 and 2006, according to Deutsche Bank.

But in Spain, easy money lulled companies into accepting rigid labor contracts. Corporate earnings were artificially boosted by inflation, relieving the pressure to keep costs under control. The result: Spanish labor costs rose 23% over the same period.

"The whole country went over the top—including trade unions, businessmen, bankers and politicians," Juan Roig, Mercadona's billionaire owner, said at a company presentation this year.

Southern Europe needs to close the efficiency gap with leaner countries such as Germany. But it won't be easy. Madrid last month said a package to make the economy more competitive would include 43 new laws. If such efforts in Southern Europe fail, the region would face years of stagnant growth—at best.

Mercadona has become a benchmark in Spain, though it will take a while for anyone to copy it, says Luis Simoes, who heads consulting firm Kantor Worldpanel's office in Spain. "Mercadona has invested in its employees for years and years," he says.

The chain had 1,356 stores and 70,000 permanent employees at the end of last year. Profit increased 19% to €474 million ($619 million) on €17.83 billion in revenue. The closely held company doesn't release quarterly figures.

Mr. Roig's drive to make over Mercadona began in the early 1990s. Big international chains such as **Carrefour** SA started raising competitive pressure on Mercadona, which started as a butcher shop in eastern Spain in the 1970s. Mr. Roig decided he needed to offer consistently low prices to compete.

"We had to find a model that would differentiate us from our competitors," he says by email. Among his models was Wal-Mart Stores Inc.

Mr. Roig visited his stores, noticing poorly stocked shelves and managers checking employee bags for stolen items at the end of shifts. He decided that temporary contracts—which then covered about 60% of Mercadona's workers—hurt morale. He curtailed the practice.

Today, about 90% of Mercadona workers have permanent, full-time contracts. At other big Spanish retailers, 60% of employees work part-time, according to the country's General Workers' Union.

Mercadona invests about $6,500 and four weeks of training in each new employee—largely unheard of in Spain. Employees receive an additional 20 hours of training a year. The Spanish government recently followed Mercadona's example by granting all workers a right to 20 hours of training a year.

Mercadona also pays above-average wages and never has conducted mass layoffs. If the company hits certain profit targets, nearly all employees receive a bonus of up two months' salary.

In exchange, Mercadona requires dedication from its employees. They sometimes are called on to help with other jobs around a store, giving the company leeway to adjust to changes in shopper traffic. Workers are trained to keep a close eye on customer needs. When a shopper lingers before a fresh-food shelf, for example, an employee typically offers help in around seven seconds, the company says.

Although Mercadona unions have expressed support for the company, the approach occasionally causes tension. Workers with minor medical conditions face pressure to consult company physicians instead of independent doctors who might authorize longer sick leave, some union officials say. A company spokesman says workers are free to visit any doctor and that under federal law, leave can only be approved by state health-service doctors.

The company also watches costs to the most minute detail. Mercadona worked with suppliers to eliminate the glossy finish on some packaging, an effort to reduce expenses so the savings could be passed on to consumers.

Mr. Roig showed up at a meeting in 2008—shirtless under his jacket—and pinched his waist. "This is surplus fat," he said. "We have to eliminate anything that doesn't add value."

The efficiency drive has helped increase sales per employee 62% since 2004. Annual employee turnover is 5%, half that of Mercadona's peers.

Greater worker productivity allows Mercadona to keep prices in check; it cut them by 10% in 2009 alone. That is paying off as Spanish shoppers tighten their belts.

For example, Mercadona has introduced 64 private-label yogurt varieties in the last two years, at about half the price of branded yogurts. **Danone** SA issued a profit warning this summer when Mercadona undercut prices for the French group's yogurts. Danone said its Spanish yogurt sales fell more than 10% in the third quarter.

The contrast between Mercadona and other retail-industry players is stark. French retailer Carrefour said same-store sales in Spain fell 5.4% in the third quarter.

Mercadona's market share has risen to 21% today from 15% in 2008. And the company is gearing up for a new challenge: exploring expansion outside of Spain, starting in Italy.