The Economist

Furniture shops

The secret of IKEA's success

Lean operations, shrewd tax planning and tight control

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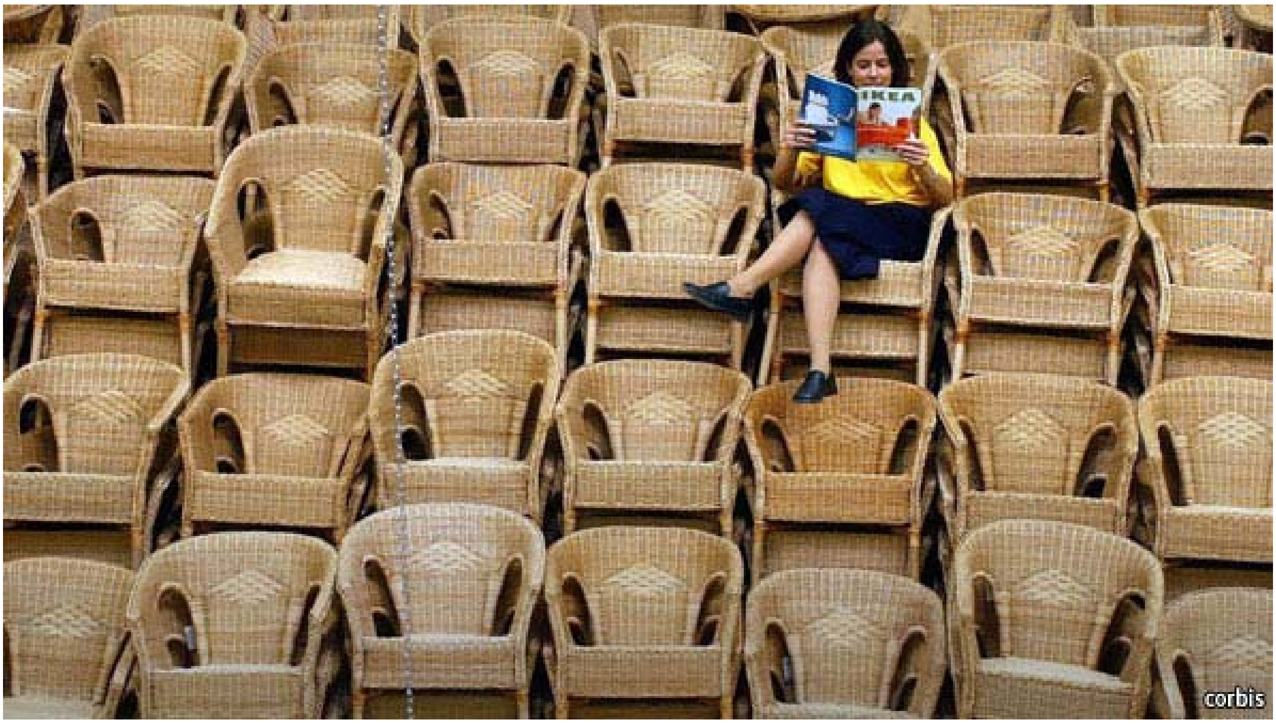


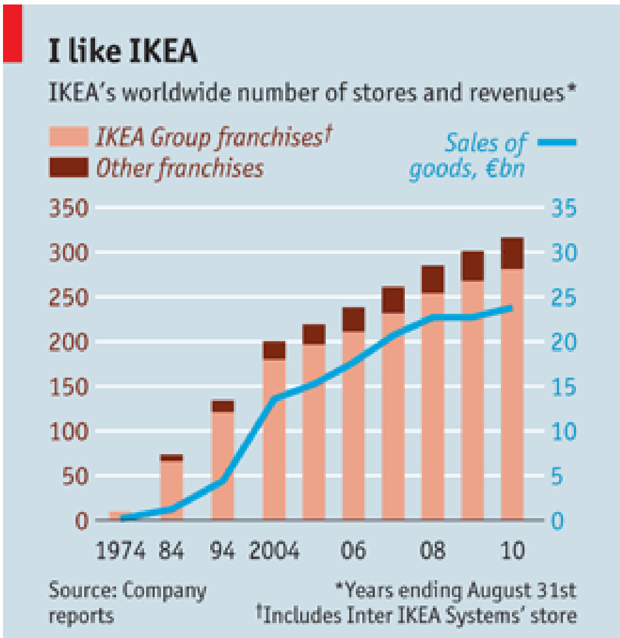
THE paragraphs below are arranged randomly; you will have to assemble the finished article yourself.

Just kidding. But if you shop at IKEA, you are no doubt familiar with the hassle and frustration of assembling its flat-pack furniture at home. Millions of customers endure it, for two reasons: IKEA's products are stylish and they are very, very cheap.

“We hate waste,” says Mikael Ohlsson, who took over as chief executive of IKEA Group in September 2009. He points proudly at a bright-red “Ektorp” sofa. Last year his designers found a way to pack the popular three-seater more compactly, doubling the amount of sofa they could cram into a given space. That shaved €100 ($135) from the price tag—and significantly reduced the carbon-dioxide emissions from transporting it.

Thrift is the core of IKEA's corporate culture. Mr Ohlsson traces it back to the company's origins in Smaland, a poor region in southern Sweden whose inhabitants, he says, are “stubborn, cost-conscious and ingenious at making a living with very little”. Ever since Ingvar Kamprad founded IKEA in 1943, the company has tried to allow “people with limited means to furnish their houses like rich people”.

IKEA presents itself as a green company with a social mission. Mr Ohlsson boasts of its charitable work and its aim to use only renewable energy. He says he wants his “co-workers” to be happy, honest and inclined to think for themselves. He is proud that 40% of the company's 200 top managers are women.



Business is good (see chart). In the fiscal year 2010, IKEA's sales grew by 7.7% to €23.1 billion and net profit increased by 6.1% to €2.7 billion. Conforama, Habitat and other rivals do not come close. IKEA's strong brand and low prices helped it to weather the downturn, even though 80% of its sales are in crisis-hit Europe. In 2010 its sales rose by 8.2% in Spain and 11.3% in Italy. The firm is doing well in Bulgaria and Romania and planning to expand further in central and eastern Europe.

Thrifty Germans are IKEA's best customers, accounting for 15% of sales. It has become part of German culture: in 2009 a Hamburg theatre staged an opera about it, “Wunder von Schweden” (“Miracle from Sweden”), a biography of the “furniture messiah” set to Swedish folk tunes.

Yet behind IKEA's clean image is a firm that is very Swedish, secretive by instinct and, some say, rigidly hierarchical. All six members of the supervisory board are Swedish. (Mr Kamprad, at 84, is a senior adviser.) Over the years the company has been accused of using child labour in Asia and of buying feathers plucked from live geese. Journalists revealed that Mr Kamprad had backed a Swedish fascist group in his youth; he apologised in an open letter.

More recently, IKEA has had problems in Russia, where it has 12 stores. Having campaigned against corruption and even frozen its investments there for a while to protest against poor governance, last year IKEA was itself involved in a scandal. It had to sack two senior executives in Russia for allegedly turning a blind eye to bribes paid by a subcontractor to secure electricity supplies for its St Petersburg outlets.

When damaging news breaks, IKEA has an admirable habit of coming clean. But the firm's ownership structure is opaque. Critics grumble that its set-up minimises tax and disclosure, handsomely rewards the Kamprad family and makes IKEA immune to a takeover. The parent for IKEA Group, which controls 284 stores in 26 countries, is Ingka Holding, a private Dutch-registered company. Ingka Holding, in turn, belongs entirely to Stichting Ingka Foundation, a Dutch-registered, tax-exempt, non-profit-making entity, which was given Mr Kamprad's IKEA shares in 1982. A five-person executive committee, chaired by Mr Kamprad, runs the foundation.

The IKEA trademark and concept is owned by Inter IKEA Systems, another private Dutch company. Its parent company is Inter IKEA Holding, registered in Luxembourg. For years the owners of Inter IKEA Holding remained hidden from view and IKEA refused to identify them.

In January a Swedish documentary revealed that Interogo, a Liechtenstein foundation controlled by the Kamprad family, owns Inter IKEA Holding, which earns its money from the franchise agreements Inter IKEA Systems has with each IKEA store. These are lucrative: IKEA says that all franchisees pay 3% of sales as a royalty. The IKEA Group is the biggest franchisee; other franchisees run the remaining 35 stores, mainly in the Middle East and Asia.

One store in the Netherlands is run directly by Inter IKEA Systems.

After the airing of the polemical documentary on Swedish TV, Mr Kamprad retorted that “tax efficiency” was a natural part of the company's low-cost culture. Yet such diligent efforts to reduce the firm's tax burden sit uncomfortably with IKEA's socially conscious image. Mr Ohlsson is trying to defuse criticism of IKEA's opacity by providing more information on its finances. Last year the firm published detailed figures on sales, profits, assets and liabilities for the first time ever.

Mr Ohlsson argues that IKEA is more competitive as a privately owned company. Instead of sweating to meet the quarterly targets the stockmarket demands, it can concentrate on long-term growth. Mr Ohlsson plans to double the pace of store openings in China, where IKEA already has 11 outlets. Undeterred by the firm's headaches in Russia, he plans to open perhaps three more stores in the Moscow area in the next few years. Mr Ohlsson hopes to move into India when the retail market opens up there. He even sees room for expansion in Britain. An Englishman's home is his castle, and castles need furniture.

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