GROCERY HEADQUARTERS.com
September 2008

COVER STORY

Rough seas

By Richard Turcsik

Can supermarkets successfully navigate in turbulent economic times?

The roster of major companies filing for bankruptcy over the past year reads like a who's who list of corporate America: Bennigan's and Steak & Ale restaurants; IndyMac Bank; Sharper Image; Bombay Co.; Linens 'n Things; Steve & Barry's; Frontier Airlines; Mervyn's; Boscov's; the Lillian Vernon catalog; and even Las Vegas' Tropicana casino. Skyrocketing gas and other energy costs, the home mortgage fiasco, rising inflation, a plummeting dollar, and consumers who are just plain scared make it easy to see why the list is growing daily.

Supermarket chains have been noticeably absent from that list—so far. And to stay off it, they have to do far more than embrace the old adage that "people have to eat," because by no means are traditional supermarkets immune from this economic maelstrom. "Today's economic environment is the most challenging I have experienced in my 30 years in retail," John Mackey, CEO of Austin, Texas-based Whole Foods Market, said recently in a conference call with analysts, where he discussed his company's 31% drop in net income for its latest quarter.

Not only do many expect this recession to be far more turbulent and prolonged than past downturns, but supermarkets also have to face a slew of competitors fighting for a piece of the ever-shrinking consumer budget. Traditional supermarkets are battling for a share of the food dollar with a host of outlets, ranging from the overbuilt "fast casual" restaurant industry to Wal-Mart Supercenters, Costco, Trader Joe's, Aldi, Save-A-Lot, dollar stores, as well as drugstores such as CVS, Walgreens and Rite Aid, which are increasingly using grocery items as loss leaders.

While unemployment remains relatively low, $4 a gallon gas prices have prompted most consumers to drastically cut back. WSL Strategic Retail, a New York-based consulting firm, has been tracking rising gas prices for more than two years. "All along we saw a consistent percentage of shoppers saying they are going to have to cut back and spend less when they shop because of gas, but when we did our last survey in May, the numbers just jumped up with quantum leaps," says Candace Corlett, president.

"Clearly a lot of people who were in the middle were horrified by gas prices and home heating bills, but were still managing," Corlett says. "Those folks are now trembling. They have thinner wallets and have to look at price points. We're talking about households in the $75,000 to $100,000 range who now have to cut back too."

TARGETING RESTAURANTS

That's a golden opportunity for supermarkets to seize upon the chance to woo those consumers who have cut back on dining out.

"I see a very strong opportunity for supermarkets," says David Rogers, president, DSR Marketing Systems, Inc., Northbrook, Ill. "People are going all the way from the restaurant back to home meal preparation. All levels of the supermarket can benefit because if you are a high-end grocer, like Harris Teeter, Fresh Market or Whole Foods, you're going to be in the restaurant substitution business, especially if you can convey a value presentation with prepared foods and take-home meals," he says.

A good way for supermarkets to do that is by using their websites, says Rich Tarrant, founder and CEO of MyWebGrocer, based in Colchester, Vt. "Giving consumers the ability to peruse the items that are on sale on your website, and building a shopping list from that is clearly an area that will help people manage their budgets, and can help retailers differentiate themselves within the current environment," he says.

Tarrant suggests retailers offer meal suggestions and recipes on their websites, and set it up so just a click of the mouse adds those ingredients to a shopping list. "Anything you can do to make that easier for the time-pressed consumer naturally gives you some assistance in combating other retailers who maybe don't make it that easy for consumers," he says.

San Bernardino, Calif.-based Stater Bros. is going after the restaurant business by teaming with MARTmenu, a Port Clinton, Ohio-based web-based service that lets consumers plan weekly menus through a supermarket's website.

"Our original thrust was to provide a competitive alternative to the Applebee's, Olive Gardens and Red Lobsters of the world that were taking stomach share from the supermarket industry," says Doug Falls, CEO and founder. "But with the economic downturn people are pulling back and doing less restaurant dining and more dining at home. We decided to position ourselves to take advantage of this market opportunity."

Operating under the MENUbutler name at Stater Bros., MARTmenu offers consumers recipes from seven different types of cuisines: Homestyle Grill, Seafood, Bistro, Asian, Mexican, Italian and American Grill. Consumers register once and are sent e-mails with easy-to-prepare recipes for main dishes, two side dishes and dessert. Ingredients are set according to the number of servings selected by the customer, and the printed recipes are store specific, showing what aisles the ingredients can be found on, based upon the store where the consumer shops.

According to Falls, of consumers using the service, most pick a main dish, 86.8% pick one side dish, 55.6% pick a second side dish and 69% pick a dessert. "That's a good way to build market basket size," Falls says. "A main dish runs about $10.83, side one $10.22, side two around $6.53, and the dessert $10.43."

MENUbutler sends consumers three e-mails a week, with the third being the value meal, using recipes incorporating what is on sale at Stater Bros. that week. "This way the consumer can go through and pick recipes based on what they can save," Falls says.

AFFORDABLE FOOD SUMMIT

On the East Coast, Stop & Shop is helping customers weather the recession by hosting Affordable Food Summits in its stores. To date, two summits have been held in New York, one in New Jersey and others are being planned for New England. "These are essentially panel discussions," says Rob Keane, a spokesman for the Quincy, Mass.-based grocer. "We have some local politicians, economists and our own consumer advisor gives advice to customers as to what they can do [to save money]," he says. "Some of the advice our consumer advisor gives is how to plan meals and base your shopping list on what's on sale that week and how to plan your meals accordingly."

The events are held in open areas set up on the selling floor to allow for maximum exposure and participation, are free of charge, and advertised to shoppers via in-store signage and bag stuffers.

Whole Foods has teamed with *Mambo Sprouts*, a Collingswood, N.J.-based marketing service that promotes natural and organic foods. "We're trying to increase the basket size of what people are buying at conventional supermarkets and at Whole Foods we're taking it a step further," says Mathew Saline, Mambo Sprouts' founder and CEO. He adds that while things are tough, "supermarkets are not at a point of crisis, like General Motors."

But there is concern that as consumers tighten their belts they will cut back on pricier organic items. "People are going to be more careful of what they purchase, and I think we're all going through some angst as to what is important to spend on and what is not," Saline says. That's why *Mambo Sprouts* has developed *The Whole Deal* for Whole Foods. It's a marketing program incorporating a newsletter, coupon books, online coupons and budget recipes with an online component where customers can upload their own tips on hot to enjoy a healthy Whole Foods lifestyle while sticking to a budget.

"With *The Whole Deal*, Whole Foods wants people to know that they have many items and many ways to shop their store as a value proposition," Saline says. "People tend to shop Whole Foods in an experienced kind of way, meaning it's a wonderful place, you try new products, and the next thing you know, you spend twice as much money as you originally thought.

"But now people are paying much more attention to what they are putting in their cart," Saline continues. "Because of that, Whole Foods wants to tell people that they can put together inexpensive recipes, combine private label and national brand products, and save a lot on a meal."

BIG MIDDLE CHAINS

One problem facing traditional retailers in this current recession is that Wal-Mart, Costco, BJ's, Save-A-Lot and Aldi have already carved out niches catering to shoppers who are watching their pennies, says Richard J. George, Ph.D., professor of food marketing at the Erivan K. Haub School of Business at St. Joseph's University in Philadelphia.

"The key to the 'big middle' chains is to provide some value options for customers," George says. "It may mean taking a stand on the top 50 consumer products—things like Cheerios, Scott tissue, Heinz ketchup and things like that which can differentiate you in terms of strength in the market and recognizing that times are tough," he says.

Corlett of WSL Strategic Retail says supermarkets can win back shoppers by cutting prices on "luxury" items, such as Haagen-Dazs ice cream. "Retailers should focus on the things that people are sacrificing and make them loss leaders," she says.

Sales can be won back in other ways, too. Corlett's research shows that 32% of women are now baking instead of buying premade desserts. "Reintroduce people to the brownie mix and cupcakes," she says. "Cupcakes have had a resurgence, just by themselves as a fashion statement. Retailers can show people how to make cupcakes. They already know how to make a tuna casserole; show them how to make cupcakes."

Tarrant says retailers promoting online shopping can increase their sales in the high-margin HBA and non-foods categories. "Customers who use the online channel consolidate their purchases back to the retailer and are not doing multiple stops," he says. "They may pay a service fee, but they've saved time by eliminating having to go to more outlets. In a time where a cup of coffee is $3, to save an hour and 20 minutes in a store, particularly if you are a young mother with kids, is a very easy value proposition to justify even in tight times."

George suggests retailers reevaluate their use of end caps. "Get rid of the soda for a month and put up the ingredients for a meal there—everything you need for a good value meal that is easy to prepare, like spaghetti and sauce," he says. "People don't want to compromise on time, they don't want to compromise on quality, but they do have a financial restraint. So the mid-tier chains should do some sharp value pricing on some key items and don't get beat on that," he says.

Retailers can improve sales by paying closer attention to where products are located in the store, says Art Hammer. He's principal of QualPro, a Knoxville, Tenn., firm that uses Multi Variable Testing (MVT) to help retailers improve their sales by gauging where sales are originating.

One suggestion: don't put a table full of doughnuts up front by the checkout lanes. "The cashiers will brag that they see customers taking stuff off of it all the times and the stock boys will say how many times they have to stock it, but when you look at the numbers you'll find the bakery department's actual numbers are falling," Hammer says. "What's happening is that people are getting their sweet tooth taken care of with a small sampling of product at the checkout and never get back to the actual bakery department to see all the fresh-baked breads, pies and all of these other things."

Hammer has another tip: bake throughout the day. "For efficiency and productivity stores may bake all of the bread over an evening shift, but our tests found that when it is spread out over the whole day, the bakery employee productivity might not be there, but that aroma of the baking bread spreads across the store, and total store sales go up," he says.

Retailers can also improve sales by stepping up the customer service.

"During times like this, retailers need to get back to the basics of trying to create a relationship with the consumer that is simply based on trust," says Glenn Llopis, president of Glenn Llopis Group, LLC., based in Irvine, Calif., and author of the upcoming book Serving Serendipity. The days of consumers going to Bristol Farms for produce, Ralphs for paper towels and Stater Bros. for bottled water are over, Llopis says. "Shoppers used to shop around and cherry pick, but with gas prices and the economy where it's at, the one-stop shopping destination is critical."

Now's a good time to implement SKU reductions, Llopis says. "Consumers want the shopping experience to be fast, simple, economical. Now more than ever, retailers should consider a strategy like McDonald's has with its value menu. Retailers need to simplify what they are selling. Instead of trying to focus so much on new products, let's give consumers what they want and start servicing them like we used to because right now consumers don't want a lot of change."

Retailers can use the recession to regain customer loyalty, says Tom DeCotiis, a marketing expert and author of Make it Glow. "The bad news is that waiting until times are tough in order to earn the loyalty of your customers smacks of closing the barn door after the horses are gone," he says. "However, it is especially true that in hard times our need for comfort and caring peak. It may be contrary to conventional wisdom, but at these times genuinely caring service is worth at least as much as a few cents off your grocery bill."

Consumers have been substantially trading down throughout 2008, and supermarkets need to address that phenomenon to win back sales, says Bill Bishop, president of Willard Bishop Consulting, based in Barrington, Ill.

“Stores can do more with their internal signing and price communication to let customers know that they have some trade-down opportunities,” Bishop says. “Highlighting comparisons with the national brand and private label would be one way,” he says, noting that an increasing number of retailers are adding second tier private labels with names like Value Time.

“It is not so much a generic as a second tier that’s a lower quality than a first tier,” Bishop says. “Some retailers don’t want to draw attention to these labels because they don’t want to trade down people, but we’re in a world where people are looking for those. It is worth your while to draw attention to them because you’d be better off with a half-loaf than none at all,” he says.

“In a recession there are some customers who need to have more control over their budget. They can’t afford to spend as much as they were spending so some of them will turn to store brands because of the price differential,” says Brian Sharoff, president of the Private Label Manufacturers Association in New York.

In the inflation-charged ‘70s generics—inexpensive, lower quality private label items in “no frills” plain packages—were all the rage, but Sharoff doesn’t expect them to raise their heads this time around. “At most generics were about 2.5% of unit market share, and that lasted only for about a year and a half.

“The amount of time, effort and money that retailers have to spend to create a generics program with such meager results, I think, makes it pretty clear that very few of them are going to try and do something like generics again,” Sharoff says. “You’re more likely to see retailers trying to offer budget alternatives, and I think Aldi and Save-A-Lot and companies like that are going to be very aggressive with their marketing and that will be matched by traditional retailers.”

Top brands really need to step up their efforts, experts agree. “Choosing the less expensive brands really puts the onus on our favorite brands, which tend to be the premium priced brands, to demonstrate value,” says Corlett. “They need to tap into the other values that are driving shopper now—the desire to be healthier, to manage obesity, to prevent disease. This is a rare opportunity in our culture when people are primed for prevention and retailers need to tap into that value,” she says.