

# Chain Reaction

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Last month, *The Wall Street Journal* published an article entitled, “Not Copying Wal-Mart Pays Off For Grocers,” the theme of which was that U.S. supermarkets have finally turned the corner and figured out effective ways to fend off Wal-Mart and grow their businesses on a non-price basis.

“After years of decline brought on by fighting Wal-Mart Stores, Inc., on price,” noted the *Journal*, “the nation’s grocery chains are on the mend.”

To support its point, the *Journal* cites the fact that sales at supermarkets open at least a year grew four percent between 2005 and 2006—the biggest increase in five years, according to TNS Retail Forward.

*Progressive Grocer* also lends support to the idea of a supermarket comeback in its *74th Annual Report of the Grocery Industry*, noting that according to its research, total grocery sales were up 4.3 percent in 2006 following a 4.7 percent increase in 2005—obviously significant improvements over the no-growth years of the early 2000s.

Sounds good, right? Hmm...

Before we encourage you to sell all of your Google stock to invest in U.S. supermarkets, we would urge a deeper look. The fact is that underneath these growth figures still lies a nest full of core issues that continue to plague supermarkets in general and do not promise to abate in the near future. Specifically:

- According to the U.S. Department of Commerce and TNS Retail Forward, supermarkets’ share of total U.S. food, drug and mass sales has plummeted from 48 percent in 1992 to 28 percent through 2006—and is forecasted by Retail Forward to drop *another* two points to 26 percent by year-end 2011.
- Over the last five years (2001-2006), food-at-home spending increased 5.9 percent, but supermarket industry sales increased only 2.9 percent—indicating that someone else is consistently stealing its chickens.

- During this same period, supercenters grew at an average annual rate of 15.7 percent—most coming from Wal-Mart, which along with SAM’s and Neighborhood Markets, now does approximately \$134B of total U.S. food sales, according to Retail Forward. To put a dimension on this, \$134B is twice the size of Kroger (\$66B) at the end of 2006 and approximately 27 percent of total 2006 U.S. Retail Food sales (\$499B).

- Meanwhile, consumers continue to leave the supermarket channel in droves. Nielsen reports that between 2001 and 2006, annual trip frequencies per household to U.S. supermarkets declined from 72 to 62, which—when multiplied by 115MM households—mean a loss of approximately 1.15 billion total trips.

In addition, this migration appears to be actually accelerating. According to Retail Forward, between 2005 and 2006, the number of shoppers making a monthly trip to conventional supermarkets dropped from 60 percent to 52 percent while weekly shoppers dropped from 37 percent to 31 percent.

- To top this off, the future doesn’t appear to look much brighter.

Versus a compound annual growth rate of 2.9 percent between 2001 and 2006, Retail Forward forecasts supermarket-industry sales growth at only 2.7 percent between 2006 and 2011—equivalent to an anemic 0.6 percent annual growth rate in 2000 real dollars.

The issue for most (not all!) supermarkets is that despite years of experiencing great pain (26 filed for bankruptcy over the last decade), most persist in doing the same things that got them into trouble in the first place.

## FILLING THE PRICE GAP

Based on a 2007 survey of 302 executives representing the nation’s top supermarket chains on the subject of “Most Effective Solutions for Dealing with Competitors,” *Progressive Grocer* reports that more than 31 percent still think that “pricing and

**How Wal-Mart is changing the supermarket business and why it means more work for you.**

promotion” is the answer, while only 21 percent think that differentiation is the answer.

These results indicate how hard it is in this industry to change behavior. It is *precisely* because of years and years of attempting to compete on price with Wal-Mart and the other value discounters that supermarkets have allowed themselves to become so eviscerated.

Simple mathematics—a five-minute exercise—would tell any of these folks that one cannot compete on price when one’s operating expenses are higher than the gross margins of one’s leading competitors.

The challenge in this situation is not to drive oneself into bankruptcy by continuing to compete on price, but to find ways to make the shopping experience sufficiently rich and exciting that one’s customers conclude that the difference is worth it.

There is recent, ample, highly visible evidence of what true differentiation can do to fill the Wal-Mart/value discounter versus supermarkets “price gap.” As anyone following this industry already knows, two public supermarkets that have broken out of the pack are Kroger and Safeway—the latter still somewhat unproven because of the lack of Wal-Mart competition in California.

Nevertheless, these folks have led the way by focusing on becoming relevant to their specific shoppers—Kroger, through Dunnhumby, and Safeway via its Lifestyle Store conversions and focus on health-and-wellness. Rather than offer cookie-cutter solutions wherein everything is the same in every store, both Kroger and Safeway have done the research and taken the time to segment and configure their stores based on *local* shopping behavior and proclivities. The results for both have consistently exceeded industry same store sales increases *every quarter* since Q1, 2005, while simultaneously increasing profits steadily.

#### RELEVANCE ROCKS

The key to these successes has been relevancy. By working with leading suppliers—and by actually investing their own “shekels” in research that enables them to establish a dialogue with their respective shoppers—both Kroger and Safeway have apparently managed to find ways to differentiate effectively on a non-price basis, *while simultaneously lowering costs!*

One of the results of this strategy is that—not surprisingly—a whole raft of supermarkets has recently followed suit and developed their own versions of shopper segmentation protocols, each of which attempts to define and clarify shoppers into

different “pods,” each based on what these retailers have found out to be their customer’s primary shopping motivations or need states.

Ahold, for example, now divides its shoppers into six different classifications—*urban seekers, traditionalists, quick fixers, good lifers, deserving diners* and *budgeters*—while Food Lion has divided its shoppers into eight classifications—*golden years, dinks, getting by, comfortably carpooling, babies and bills, wealthy elite, savvy singles* and *country living*.

Whether these retailers actually utilize these segmentations to reconfigure their stores and/or merchandising practices remains to be seen (some cannot even effectively get a display up on time).

However, the message to suppliers is that most will expect suppliers to align their distribution, assortments, new item introductions and program recommendations with each of these retailers’ newly-defined shopper segmentation protocols.

In practice, this means that one could be asked to assort and promote differently in two different stores owned by the same supermarket only six miles apart. To assess the marketing community’s reaction to this prospect, *Reveries.com* surveyed the subject in April.

Results from 143 respondents representing 135 companies were surprisingly positive, indicating that most *welcome* the prospect of retailer guidance on what will and will not work best for their brands in specific stores, even at the risk of increased complexity.

- Forty-nine percent—about half—believe that the emergence of retailer segmentation policies will have a “significant” or “major” impact on the way they do business at present.
- When asked to list what retailer shopper segmentation protocols will cause them to do differently, the number-one ranked response (45 percent) was “ensure that all future promotions, new item introductions and category management assortment recommendations align with the new retailer-defined shopper segmentation cluster.”

Another 41 percent said, “require greater internal collaboration” while—importantly—33 percent said, “Change new item forecasting procedures to better align new item distribution targets with retailer shopper segmentation models.” (*see table*).

- Cited by 65 percent as the most beneficial effect of retail segmentation protocols is “better targeting of products and promotions,” while another 45 percent look forward to “improved collaboration with key retailers.”

**What has the emergence of retailer shopper segmentation caused your company or client to do — or plan to do — differently, if anything?**



SOURCE: Reveries.com

- As far as downsides are concerned, 69 percent feared “increased complexity of logistics and execution” — but based on the accompanying verbatim comments, none views this as a hard stop.
- The department expected to be most impacted by the emergence of retailer segmentation protocols is customer marketing/shopper marketing (46 percent), followed by brand marketing (19 percent) — the latter in recognition of the fact that it will no longer be possible for marketers to use a broad brush when forecasting, planning new item introductions or promotion programs.

On an open-ended basis, the survey also asked: “What else do you anticipate will be the impact of retail segmentation requirements on your company, client or business?” Following is a representative sample of the verbatim responses:

*“Adapt or face extinction.”*

*“Retailer-specific shopper insights versus brand-specific shopper insights.”*

*“Our research on retailers will need to reflect the way they view their consumers.”*

*“Building new capabilities in knowledge and insights to work with key customers to truly understand their segmentation strategies.”*

*“The need for marketing organizations and their partners to become more involved with data and targeting — something that has not been the key driver for retail promotions.”*

*“Fewer Saturdays with my kids.”*

Moral of story: It looks like suppliers may finally have a basis for true partnering with supermarkets — defined as working together to *market* to the mutual shopper at a time when *both* are focused on the same objective (*i.e.*, “relevancy”) — something for which we can all be grateful to Wal-Mart. ■



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