Food Retailing Review

The State of the Food Retailing Industry


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Food Retailing Review

The Business Environment

- Complex business environment
  - Greater external influences on day-to-day business
- The economy is driving:
  - Changes in consumer behaviors
  - The need for further efficiencies internally
  - Changed marketing, merchandising and promotional strategies
  - The need for greater cooperation throughout the supply chain

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What Are the Major Changes?

- High food-at-home inflation
- Roller coaster fuel and gas prices
- Credit liquidity crisis
- Unemployment rising
- House prices and sales in the pits
- Stock market collapse
- Population shifts
- Weak dollar
- Emerging nations

- None of these are short-term issues

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Consumers Are Feeling the Pinch

- Consumer confidence continues to decline leading to reduced consumer spending
- Changing…
  - ❑ Shopping patterns
  - ❑ Food consumption patterns
  - ❑ Purchasing decisions

- Implications for the entire food channel

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Changing Shopping/Eating Habits

- Eat out is down
  - ❑ 1.2 times per week
  - ❑ Decreases across the board, even Generation Y
- Home-cooked meals are up
  - ❑ 4.9 meals per week
  - ❑ No firm definition of “prepare” or “home-cooked”
  - ❑ Real chance for food retailing to take back mealtime
    - Cooking at home = eating healthier
    - Cooking at home = saving money
    - Cooking at home = family mealtime

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However, at Least Half of Shoppers…

- Cook more and eat out less (71%)
- Buy fewer luxury items (67%)
- Purchase more store-brand items (60%)
- Eat more left-overs (58%)
- Take fewer trips
- Engage in money-saving behaviors pre-trip and inside the store
  - Coupons
  - Bulk
  - Private label

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How Shoppers Pick the Primary Store

- Very important factors

	2007	2008
High-quality produce	77	75
Low prices	64	73
Clean, neat store	75	72
High-quality meat	73	72
Convenient location	61	66
Items on sale/promotions	55	66

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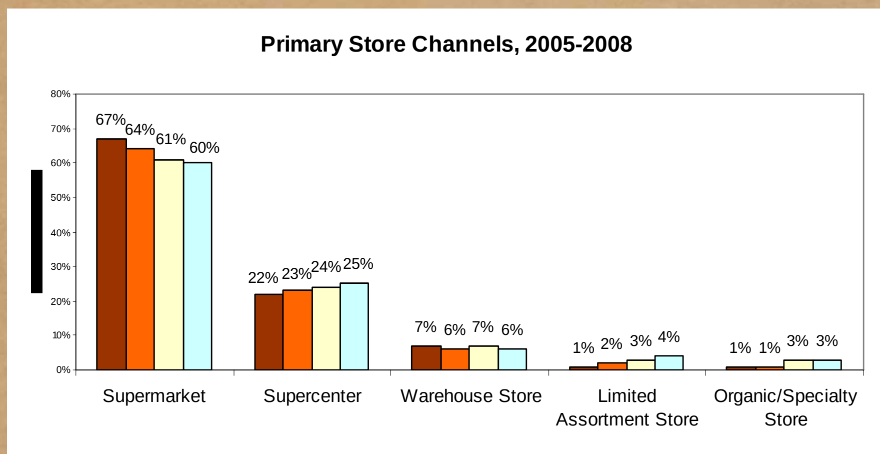
Increased Focus on Price and Value



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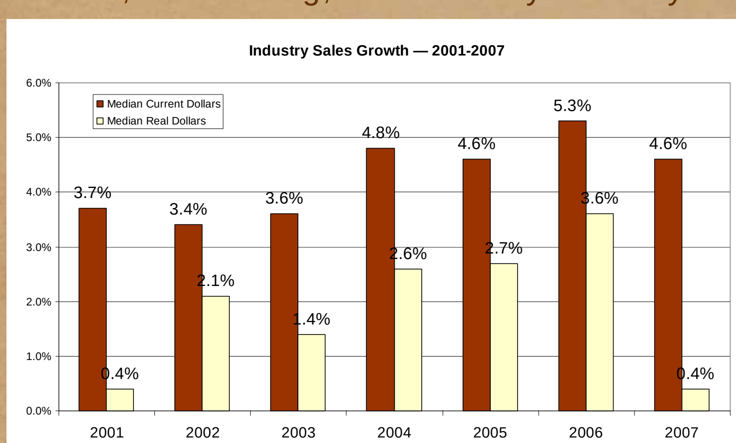
Industry Performance

- Sales, while strong, were virtually offset by inflation



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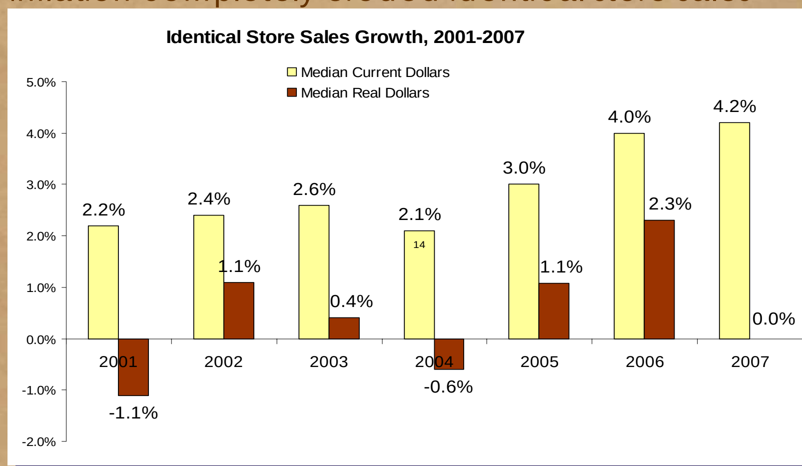
Identical Store Sales

- Inflation completely eroded identical store sales



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Net Profits

- The industry's median net profit for 2007-2008 dropped slightly to 1.84%
  - ❑ 2006-2007 was a 38-year record at 1.91%
- 2007 was still a banner year
  - ❑ Profit was driven by operating results
  - ❑ Companies lowered their long-term debt levels
  - ❑ Reduced inventories
- Many retailers struggled in 2008
  - ❑ Profit expectations down

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Economic/Profitability Outlook

- Outlook for overall industry less positive for 2009

	Level of Optimism About Company's Profitability Outlook		
	2006-2007 %	2007-2008 %	2008-2009 %
Very Optimistic	39	30	28
Somewhat Optimistic	50	56	51
Not Too Optimistic	11	12	18
Not Optimistic at All	0	2	3

- Challenged by consumer money-saving behavior
  - Trading down
  - Substituting
  - Eliminating

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Success in Today's Market

- Growth in value-based formats
  - Supercenters
  - Warehouse clubs
  - Limited assortment stores
  - Dollar stores

- Those who set themselves up for success. Profit leaders typically are companies that…
  - Spent less on salaries, benefits, supplies and other expenses
  - Have lower debt levels
  - Reinvest in their companies

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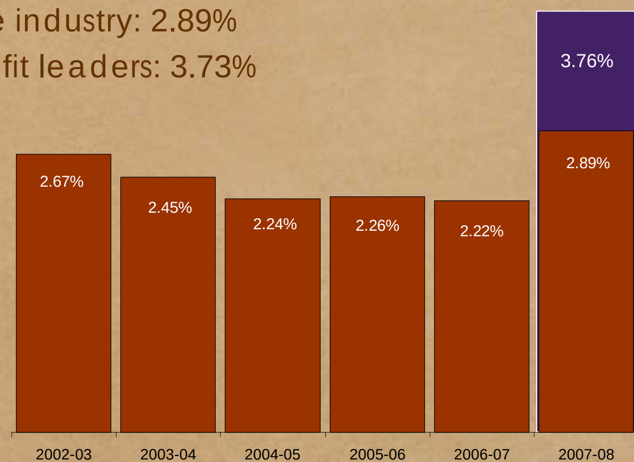
Capital Expenditures

- The industry: 2.89%
- Profit leaders: 3.73%



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What keeps our CEOs awake at night?

- The FMI worry index tells all

2004
7.0 Competition
6.4 Interchange fees
6.2 Healthcare
5.9 Staffing, hiring, retention
5.6 Energy costs
4.9 Technology investments
4.4 Local/national economy

2008
7.9 Energy costs
7.7 Healthcare costs
7.5 Competition
7.4 Interchange fees
7.2 Local/national economy
7.1 Food safety
6.7 Staffing, hiring, retention

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Energy Costs

- Retailers spend 1.5% of sales on energy
- For 81.5 percent of retailers energy costs increased in 2007 compared with 2006
  - Median increase of 7.0%
  - Increase of 8.4% in 2006
  - 95.8% expect a cost increase over 2008
- Increase in store operations: 90.5% by an average of 7.9%
- Increase in transportation: 90.0% by an average of 9.5%
- Increase in warehousing costs: 78.9% by an average of 5.0%

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Energy Costs

- 66% have not passed on increases in energy costs to shoppers
- Ways to lessen the impact of rising energy costs:

	Implemented %	Rate of Success, Scale 1-10
Minimize Leakage on Refrigeration Systems	95.2	7.2
Lower Store Lighting Costs (LED, Lowering Lights, etc.)	90.2	7.1
Adjust Store Temperature to Save on Store Heating/Cooling	88.5	5.5
Create More Energy-Efficient Store During Remodels or New Construction	85.2	7.4
Re-engineering Store Delivery Frequency	75.4	5.3
Improved Warehouse Operations	61.7	5.7
Product Packaging Innovations (Item, Case, Pallet)	60.7	4.6
Improve Manufacturer Backhaul Program	59.0	5.1
Implement Alternative Energy Sources (Solar, Wind, etc.)	57.4	3.4

Competition

- Once highest concern, but now surpassed by costs of doing business
- Top competitive worry remains local competition from other supermarket operators
  - Supercenters and new supermarkets follow
- Retailers continuously adapt their product selection to better meet customer needs
  - Increased focus on private label, including multiple-tiers and organic products
  - Greater focus on health and wellness and online shopping
  - Median of 3,450 new items added each year

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Differentiation Techniques

- Emphasis on perishables universally cited as top tactic used to differentiate
  - Also most successful strategy
  - Organic merchandising growing in use and success
  - Private label and health and wellness programs are other important strategies
- Positioning and differentiation will be ever more important as consumers are changing their purchasing habits

Other Trends to Watch

- Sustainability
  - Retailer focus on green practices that can positively impact the bottom line
  - Reusable shopping bags catching on big
- Health and wellness
  - While healthfulness is often second to price and time, eating better is a clear priority
  - 88% of retailers feel this is an area of competitive advantages
  - Nutrition programs
  - Whole health concept

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