

Grocery Outlet: Bargains On Brands

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This unique chain helps find homes for the ‘problem products’ of 2,500+ manufacturers. It also helps shoppers stretch their food budgets.

“We try to keep the categories full, but when I go home at night, I don’t know where the next 70,000 cases are going to come from for the future week’s sales. I just keep filling slots by category and stay connected to our suppliers,” says Rachel Dent, refrigerated foods buyer at Berkeley, Calif.-based Grocery Outlet.

We’re mid-way through a tour of the extreme value closeout chain’s store in Redwood City, Calif., and it’s hard for us to fathom how these people run a thriving \$650 million business and stay calm amid such unpredictability. After all, with product here today and gone tomorrow, how do you set planograms, or plan promotions?

“We don’t,” answers frozen food buyer Diana Curtis, matter-of-factly. “It’s impossible to have real planograms. We have a recommended roadmap, but you can’t have strict rules.”

As this begins to sink in, Steve Wilson, the vp of purchasing, points out that “Only about 80% of what we sell are closeouts or over-runs. The rest is fast-moving product that is made-to-order for us as a customer convenience. Since we don’t have slotting fees and all, our buyers love to discover new, smaller manufacturers and help them gain early distribution. If a manufacturer calls us today, we negotiate today and take delivery next week.”

Back when we bumped into Curtis at the Western Frozen Food Convention in February and agreed it would be fun to do a cover story on the chain “someday,” we had no real idea what to expect. But here are a few things we didn’t expect:

- Refrigerated foods do about \$90 million annually, or a little over 14% of sales at the chain’s 125 stores. Frozen foods, at about \$105 million, account for 16%+ of sales.
- That strong volume comes off low SKU counts. In the frozen/refrigerated warehouse run by Versacold in Modesto, Calif., there are typically about 350 items in frozen food, and from 280-300 in refrigerated. In the stores, of course, there’s a somewhat higher variety as items work their way through the system.
- Average basket is \$21-\$23, depending on the time of the month.
- The 40-year-old chain has no debt, and an AAAAA credit rating.

Zero predictability

Okay, now that we have your attention, let's get back to what intrigues us most: how to run a business that has such an utter lack of predictability. Wilson credits his seasoned staff (Dent, for example, has 28 years experience with Grocery Outlet) and explains that he sees the constant uncertainty as constant opportunity.

“That’s the beauty of our business,” he says. “We tell shoppers to stock up on products they like, because it may not be there tomorrow. Our focus is on bargains on brands you trust. It’s a treasure hunt all the time.”

More than 2,500 manufacturers rely on Grocery Outlet to make problem merchandise go away. In discussing mutual friends in the industry with Curtis, Dent and Wilson, it’s clear that the partnerships and friendships run deep.

Curtis and Wilson nod in agreement when Dent says “Perhaps the hardest thing we have to do when working with a manufacturer is to say no, we can’t take something. We take as much as we can as often as possible, and that really connects them to us.”

It’s a constant guessing game. If you take in too much today from one manufacturer, you can be sorry tomorrow when another manufacturer calls with a huge closeout that you can’t touch because of insufficient space.

All purchasing is done at corporate headquarters. Stores, with the exception of three that are company-owned, are owned and operated by local entrepreneurs – generally husband and wife teams. They have the autonomy to pull products that are right for their local demographics – something that is necessary considering the differences between stores in, say, National City, Calif., and Bellingham, Wash.

Prices are typically 40% to 50% less than those found in conventional retailers, Wilson says. Comparisons and savings are printed on tags at the shelf, but “We don’t compare our values up against Safeway or Albertson’s,” he notes. Instead, he says, it seems more appropriate to compare prices with extreme value retailers in the area, without naming them. Savings are printed out on receipts, which encourages shoppers to come back for more.

It’s about value

The buyers used to be hesitant to stock items that sold for more than \$3.99, but now many items sell for \$4.99 and \$5.99 and even higher. “It’s about value, really,” Dent says. “We never buy cheap for cheap’s sake – we are not trying to hit a specific price point, but to provide the customer with obvious savings.”

The merchandise mix has evolved significantly over the past few years in ways other than price. “Fortunately, we recognized six or seven years ago that we weren’t convenient,” Wilson acknowledges. “People used to just do their treasure-hunting here before going somewhere else to finish their shopping. Now, you can get your milk, meat, produce and

staple items here and still do your treasure hunting at the same time. We don't want to go too far on this, because we want to maintain our branding statement, which is saving people money. So we minimize the number of SKUs of these staple items. We show the best value we can on them, but it's not quite the same 40% or 50% savings."

Although there are no real planograms, headquarters staff makes recommendations to the stores about product placement, often based on longish inventories or products close to code, and the resulting need to move it out quickly.

As we begin walking through the frozen food department, Curtis notes that endcaps focus on high-ring, high-visibility branded items. Hispanic foods, she says, are a strong and emerging category, with items from Ruiz Foods extremely popular.

"To Diana's credit," Wilson says, "we'll probably do somewhere north of \$3 million in the Hispanic segment this year, and on few SKUs. We had hardly any sales here a few years ago."

Schwan's stars

The frozen pizza category is also strong – with Schwan's as a strong strategic partner. Red Baron items are usually closeouts, but "Schwan's also has a regular goods program for us," says Curtis. "When pizza closeouts from other brands temporarily dry up, Schwan's makes fresh items to order."

Further down the aisle we notice strong representation in organics. Closeouts of natural and organics have done well in the past because shoppers saw the huge savings vs. stores such as Whole Foods. Comparisons were easy – there are 17 Grocery Outlet stores within a one-mile radius of Whole Foods units.

"Now we're pursuing this on a larger scale and trying to get product that's made for us, where we can do a dead net program and increase our offerings because customers are looking for that now, and we can give them a really good value," says Curtis.

Wilson adds that "Our typical customer is 34- to 38-year-old woman, with two or three kids and a take-home income of around \$40,000-\$45,000. The incomes for Whole Foods shoppers are significantly higher, but people are always looking for value and a treasure hunt."

He does not believe Wal-Mart's entry into the organic market will cause any supply problems. In fact, Wilson says, the move may create excess supply, since Wal-Mart is reportedly not doing as well with organics as it had hoped. Suppliers who expanded capacity to meet expected demand from Wal-Mart may now be looking to dispose of inventory. "If that happens, we'd like to be the first call they make," Wilson says.

Sometimes, it's hard to know why a product misfired. One example is a discontinued vegan eggplant parmagiana from Rosina, which Grocery Outlet shoppers loved. One of them told Curtis that it was one of the only vegan products her kids would eat.

We pass by Tony's Pizza Twists, which Curtis jokingly describes as "the love of my life," and move on to product from long-time partner Dreyer's Ice Cream. She calls one discontinued item – Blisscotti ice cream sandwiches – "an absolute gem."

Grocery Outlet stocks many quart-size ice cream products, which are not always the best sellers in conventional retail. It also gets excess inventory from most major ice cream brands.

Yet private label shows up store-wide. Near some Pot O'Gold ice cream made for Grocery Outlet are facings of orange ice cream bars made for Pathmark, the East Coast retailer. What gives?

It happens a lot

"It happens a lot with cancelled orders, or things discontinued in midstream and the manufacturer needs a home for it," Curtis explains. "We make a point of not embarrassing the manufacturer or the retailer. So we don't advertise them or make a big deal out of it – we move them discreetly, priced to move quickly and get them out of the system. We're not here to rub anybody's nose in anything; we just want to get rid of problems for people and move on."

The pie and desserts section, next to ice cream, has Chef Pierre prebaked pies with labels explaining minor imperfections, alongside Mrs. Smith's product. At this peak selling period, Mrs. Smith's is a made-to-order supplier since closeouts are not plentiful enough to keep the pie category in stock.

Our tour continues on to the refrigerated department, along the back wall. Dent explains that this store – with 72 feet of open multi-decks – is larger than the average Grocery Outlet, which has about 48 feet. But this store has higher volume than most, so it can handle the product required to fill up the space.

Although it is about 11 o'clock on a Wednesday morning, we are surrounded by shoppers eager to check out the sausage, bacon and lunchmeats at the start of the lineup. Most shoppers begin their search of the refrigerated cases here, where the higher-ring items are.

Shoppers take their time. Even though the SKU counts aren't high, there seem to be many choices in this treasure hunt. The two-pound bacon, the upscale Hormel maple peppered bacon, or the No. 3 ends and pieces bacon? There's also a good assortment of lunchmeats.

“We do in the neighborhood of 7,000 to 8,000 cases a week of lunchmeats in all our stores, and that is our biggest category next to dairy,” says Dent. It’s also the hardest category to keep in stock, she adds. Although sales have nearly doubled in the past five or six years, industry consolidation has affected sources of closeouts, so Dent has to fill back in with made-to-order items.

As we move further along, we see a popular item: end-pieces from salami and pepperoni from Sara Lee’s Gallo Salame, sold under a second label called Roma. It’s on the shelf here at two pounds for \$7.

“It is an amazing value,” Dent says. “Endpieces may not be as pretty as what you might normally see in a refrigerated case, but we can’t keep this item in stock. Once the customer takes it home and sees the quality, they come back for more.”

Another success story: Chicken of the Sea crab claw meat in a one-pound refrigerated can for \$7.99. Sales of the item top \$100 per week in each store. Sokhom Sar, a refrigerated and frozen food buyer who works with both Dent and Curtis, had a hunch it would sell, and took a chance on it.

Taking a chance

“At a conventional retailer, this would never have happened,” Wilson says. “They’d want something for the space, and marketing money, but Sokhom just took a chance and bought 100 cases. He figured he’d watch the POS sales for a couple weeks and if it sold, we’d continue to buy it and if it didn’t, no foul – just move on to the next item.”

Milk – all fresh and made-to-order – was added as a convenience about six years ago, based on customer requests. The company is careful to limit the SKUs and facings since most profits come from closeouts. But then again, milk brings in more customers, who then spend more.

4 lbs. hot dogs: \$1

Moving along, we notice four pounds of hot dogs on sale for \$1, and notice that it is dated to expire this very day. “In a refrigerated case, you have nowhere to go once it runs out of shelf life, it goes to the garbage can,” says Dent.

Products with three or four days left on the “sell-by” date are marked down at least 50%, to make sure it sells. Only about 1.5% of refrigerated inventory gets marked down for this reason, however, and about 1% has to be thrown away.

“As a closeout refrigerated buyer, my biggest challenge is to buy just enough for the stores, to make sure it sells before the code,” says Dent. “But we give stores leeway, based on their experience, to mark things down to make sure they go out of the system without having to be thrown away.”

The last-minute markdowns aren't all bad. Many shoppers buy refrigerated product that is close to code and freeze it when they get home. And the markdowns help generate added excitement in the stores.

The cheese category, the second highest-dollar generator in refrigerated foods, is a destination for treasure hunters. Although products such as cheddar, sliced Swiss, cream cheese and shreds may always be in stock, there is constant churning in specialty cheese, the fastest-growing segment in refrigerated foods.

An elderly customer brushes past our photographer and complains, to nobody in particular, that "There's no yogurt again." Dent says yogurt is a difficult category because it is growing so rapidly and closeouts are scarce. It's not a good made-to-order item because it is already low-priced and often deeply discounted by other retailers.

"When manufacturers are shorting conventional stores on yogurt, they're not likely to have product for us," Dent says. "But we can move anywhere from 14,000 to 20,000 cases a week, when we can get it. Right now, we are in stock about half the time, and when people see it, they load up."

While the store is always in stock on eggs, opportunistic buying means there may be mostly large eggs one week and medium another. Brown eggs are popular, especially in the Northwest, where organic items are also fast-sellers. The limited selection we see today includes five-dozen packs at \$4.29 – popular with restaurants, and big families. The store indexes high on Hispanics, who are heavy users of eggs.

And so our tour ends. For a longer version of this story with details that would not fit here, go to www.rffretailer.com, and click on the cover of the magazine.