DISCOUNT STRATEGY IN FOOD RETAILING

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Discusses the recent trend to discounting in supermarkets and its "real" effect on the food distribution system.

Very lately the food retailing scene is experiencing a new trend. National and regional supermarket chains are converting their stores into discount food stores. These converted stores are promoted as discount and cut-rate outlets for food, related items, and health and beauty aids. Examples of such conversions are Lucky Stores of California, Stop and Shop of Boston, Penn Fruit of Philadelphia, and of course, A&P and its WEO operations. This development has not run its course and even as this article is being written, chains are going discount in different parts of the country. In analyzing this trend, this report first summarizes some of the major reasons for this movement, then identifies certain effects. It also recommends a very desirable approach to studying food discounting.

In the early 1930's the pioneer supermarkets enjoyed a significant cost advantage compared with the then conventional type of food stores. This was possible mainly because of the supermarket's low overhead costs, its emphasis upon self-service instead of upon clerk-service and its operations close to full capacity. Every resource at the disposal of the supermarket was used fully with the sole objective of maximizing both sales and total profits. A bulk of the savings in cost was passed on to the shoppers in the form of conspicuously low prices which in turn helped the supermarket to attract the high sales volume required to operate at or near full capacity.

They were doing so well since their arrival and up to the middle 1950's that supermarket chains were perhaps the most glamorous investments in the stock market and possibly the most sought after ventures. Between the years 1950 and 1960 the total sales of supermarkets doubled.[1] They had almost saturated the urban areas to the extent that there was a feeling of "overstoring". Increasingly they began to compete with each other. Stores began to get larger and fancier. They increased their newspaper advertising to tell shoppers of their distinctive offerings. To add to their distinctiveness stores began to try trading stamps and other promotional appeals.

The final outcome of all these developments was that the supermarkets of the late 1950's and early 1960's were burdened with added overhead costs leading to a profit squeeze. Supermarket chains ceased to be attractive investments in terms of both growth of capital and return on investment. Not only that, a majority of the new supermarket units built since 1958 did not attain their anticipated sales volume.[2] This resulted in excess and idle capacity. From there on the supermarket clearly was not the epitome of retail efficiency on which it prided itself. This naturally led to profit erosion and forced the chains to look for ways and means to improve their sales and profit performance.

To consider a specific example, most families do their major food shopping near the weekend. Perhaps the institutional practice of designating Friday as the weekly payday is one of the important reasons for the concentration of food shopping near the weekend. Instead of trying to spread their sales over all the days in a week, supermarkets, however, nurtured this tendency for years by offering and emphasizing weekend specials. As a result, people were conditioned to shop for food during the latter part of the week. To cater to these large crowds of shoppers, the stores became larger in size with several check-outs and other facilities necessary to make their shopping as pleasant as possible. The trouble, however, was the fact that many of these check-outs and facilities were lying idle during the earlier part of the week and the chains apparently were not concerned about this situation until it become a serious problem. Of the several possible alternatives open to the chains, the most promising one was to go back to the basic philosophy of the pioneer supermarkets--low margins with high sales volumes, everyday low prices--to increase both total profits and the capacity utilization of the plant, namely the store and all the customer facilities. As we know now, these very same chains are advertising in the Sunday newspapers (instead of the Wednesday or Thursday issues), advising their prospective shoppers of the "low prices" and "specials" that are good for the entire week, not just the latter part of the week.

The effects of going discount can be many fold. In summary, however, a majority of the chains experience the following developments.

1. Total sales do increase but sales by day of the week do not change appreciably in the short run. If the so-called bargains are not perceived as real bargains, the sales volume goes back to the earlier levels.

2. The total cost of promotion increases in spite of the savings involved in dropping of stamps and other give-a-ways.

3. The first store to go discount in an area has the edge over others in enlarging its trading area. Subsequent discounters are looked upon as imitators by shoppers.

4. The speed and the harshness with which competitors retaliate often decide the durability of the early gains of the first discounter in a trading area.

5. Profits in the early periods after going discount tend to go down. There is no assurance or evidence that they necessarily go up later in the case of all discounters.

6. Some of the prerequisites to successful conversion are excess capacity, large size stores, good locations, prior experience in non-food discounting, ability to finance a conversion program, and lead time from competition prior to retaliation.

There are some severe limitations to activities in this area. First is the fact that food has a relatively low price elasticity. Small reductions in prices do not bring about increased purchases from individual families. The average American housewife has a definite idea of how much she should spend on food. She usually accommodates short run increased needs in volume of food by trading down in terms of the cuts of meats or brands of groceries. In other words, discount prices per se do not induce increased consumption by individual families. Any increase in the sales volume is attained by increasing one's market share in his own trading area and by attracting shoppers from competitors' trading areas. Second, even if the price elasticity of food were greater than one, there is a natural limit on how much a person can eat. This factor works as a natural ceiling on the amount of food purchased by individual families. Shrewd discounters have found a way to get around these two limitations by offering more non-food and HABA items at discount prices, so that even if a family spends the same dollar amount on food items, it spends in the food store some or all of the money that normally would have gone to the neighborhood drugstores and hardware stores. In this new arrangement, the food store is better off in terms of increased sales volume and at the same time, the family is within its budget, and perhaps even a little better off because of the discounted prices on non-food items at the food store.

Not much has been published on discounting of food. Those reports[3] that do examine this topic, invariably restrict themselves to examining prices before and after going discount. This researcher believes that in buying goods from an American retail institution one really buys a total package, a "bundle" of which price is only a part. Examples of other variables are physical product, variety, assortment, promotion, store location, customer service, store exterior, store interior, and store personnel. Further, in the absence of list-prices and manufacturers' suggested retail prices, food discounting should be viewed as a manipulation not of price alone but of several variable aspects of "bundles" offered to thousands of prospective shoppers.

Marketing strategy defined in simple terms consists of identifying a target-market and developing a marketing mix to appeal to that target-market. This is the basic concept of marketing--consumer-oriented activities in business. One problem, however, in developing and implementing a marketing strategy in food retailing is that market segments in food retailing are not sharply definable. The weekly food baskets of the same shopper are subject to several influences, both subjective and objective. The time-proven weapon among competitors in food retailing, for that matter all forms of selling, is the development of some differential advantage that will attract prospective buyers.

A successful discounter develops differential advantages in terms of lower prices and the fact of being the pioneer in lowering prices, publicizes these facts, and keeps hammering that message constantly. By restricting his competition to prices and promotion, the discounter in effect looks upon shoppers who prefer and seek lower prices to anything else as his target-market. His promotional activities enable him to accomplish this objective by enlarging his area of patronage. He maintains the loyalty of his clientele by constantly manipulating the variables in the "bundle". In other words, a discounter increases his productivity by developing an institutional concept of an efficient store--the old-fashioned supermarket--and translates this idea into a real institution at the right time and the right place.

Unfortunately, this trend is now going against the retailers' own interest under the disguise of competition. Many discounters, particularly A&P, have gone for twenty-four-hour operations, with crews working overtime on a <u>regular</u> basis. This decision increases operating costs more than proportionately for the added hours a store is open. This researcher hopes that someone will undertake a simple project to convince the industry that the marginal benefits of additional sales and prestige derived from the increased hours of operation may not be worth the marginal costs involved in manning and operating the store during those additional hours. With all the problems they have these days, food retailers, however, are in no mood to listen to any advice.

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[1] "36th Annual Report of the Grocery Industry," <u>Progressive Grocer</u>, April 1969, p. 68.

[2] "Facts About New Supermarkets Opened in 1960", Chicago, The Supermarket Institute, 1961.

[3] See for example, Martin Leiman, <u>Food Retailing By Discount Houses</u>, Market Research Report # 785, U.S.D.A., Washington, D.C., 1967.

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