Old Dog, New Tricks

Battling price perception with a warehouse in Bozeman

BY KELLY WISEMAN

There are plenty of unwelcome emotions that accompany us through our days in retail, like stress or maybe even a little anger. But nothing quite starts the day like that twinge of outright fear in the pit of your stomach the first time you see negative sales growth for the week or month. You wonder if you did something wrong, if the bottom is about to fall out of your world, what the impact will be on staff. Negative sales growth is not the most evil force in the universe, but it does tend to keep a lid on wages and can cause a serious and rapid drain of cash. In other words, it stinks.

In Bozeman, Mont., our wave of negative sales began before the national recession, with the arrival of a large and somewhat flashy competitor in November of 2007. Our rolling monthly sales growth went from a positive 8 percent to negative 2.5 percent in a month, and in the toughest part (we hope) of the recession, we experienced a stomach-gnawing negative 10.5 percent.

We did a lot of things to keep the store profitable, like cutting unnecessary expenses, slashing labor (including painful layoffs), and so on. But one of the key elements was to attack a problem that many co-ops share: the perception that our prices are too high.

We operate in a very competitive environment. In a town with a population of about 35,000 (plus 10,000 nonresident Montana State University students), we have six major supermarkets, three natural food stores, a few smaller independents, and a very competitive locally owned warehouse grocer just down the street that regularly slots in natural brands at about a 25 percent margin. They even have a nifty slogan that they run in our only local newspaper twice a week: "Where you don't have to be wealthy to eat healthy." Ouch.

Food service is a big part of what we do, 23 percent of sales. A few years back, we put in a large (4,800-square-foot) commercial kitchen and bakery in a building two blocks from the store. We have a few small trucks and regularly haul bread, pizzas, salads and bakery items from the Central Kitchen (CK) over to the store. We also buy our milk directly in multiple pallets weekly and deliver to the store from the large cooler at the CK. So we do have a few years of experience under our belt in the trials and tribulations of moving food between buildings. Our good fortune is that it is only two blocks, hardly a long haul.

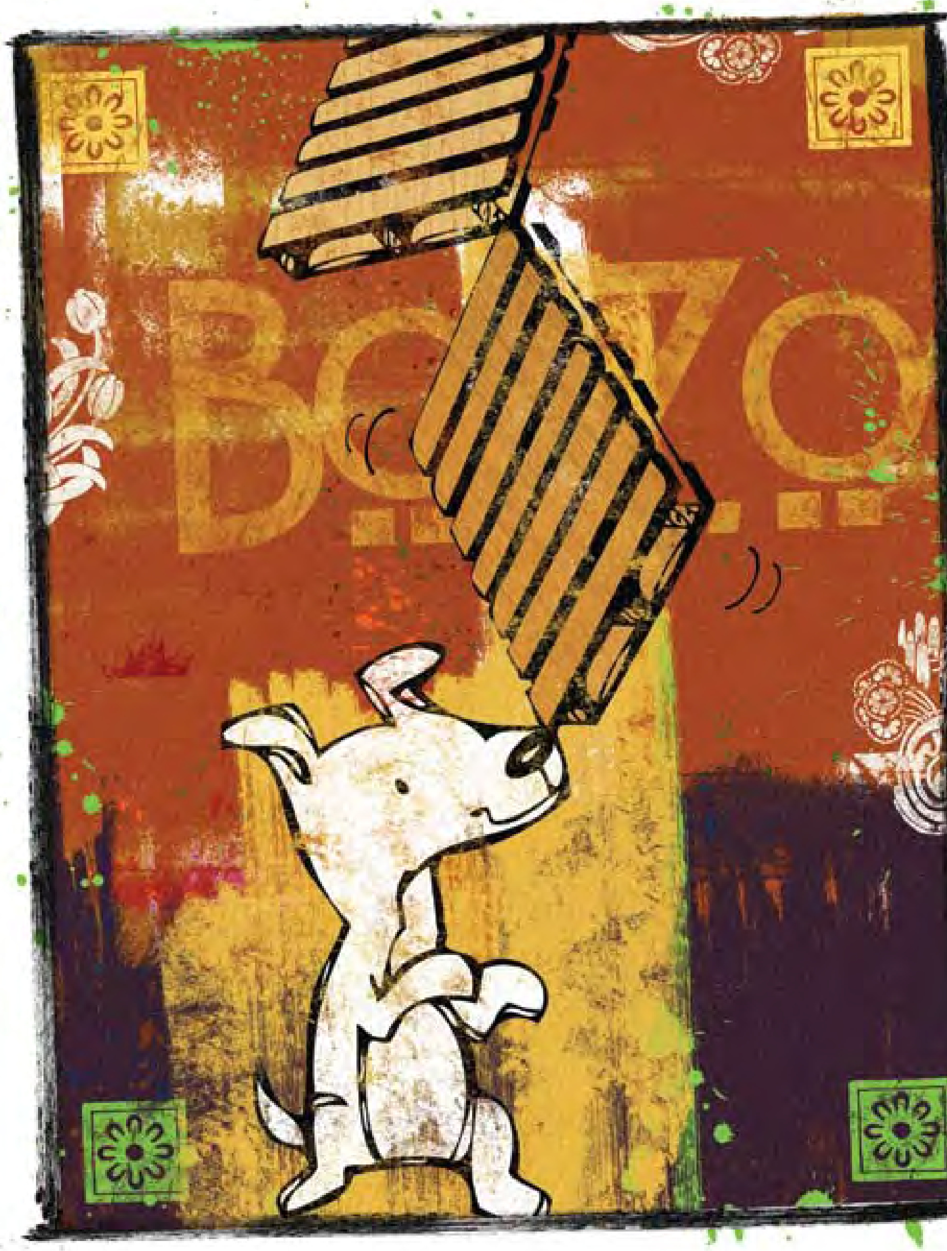

ILLUSTRATION BY KEN DAVIS

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In the middle of the sales downturn (summer of 2008), the remaining half of the CK building, an additional 4,800 square feet, became available to rent. We declined taking on the additional space until our landlord offered to wave the first year's rent and give us a good deal for nine more. We agreed to add 4,800 feet to our occupancy costs because we wanted to do what some of our competitors can do: buy lots of stuff on sale and keep it on sale. It was a big step for us because we have always kept our grocery inventory lean and mean. Now we were going to add 90 pallets to the mix.

Building a warehouse

The easy part about a warehouse is that it doesn't have to look pretty, there is very little staffing, and you hardly have to heat the thing. Our vision was to have a space big enough to hold about 10 ▶

pallets of grocery and 10 pallets for food service—paper goods and flour for the bakery, mostly. Since the place has a fairly low ceiling (it's a former video store) we decided to forgo shelving and instead just slot pallets on the floor. For tools, we bought an electric forklift, which we only rarely use, and a manual pallet jack, which does almost all of the work. Since one of our delivery trucks has a lift gate, as does distributor UNFI's truck, we did not even need a loading dock, just an overhead door.

High on our list of concerns for this project was the very likely possibility of inventory getting out of control and bloated, thus draining cash. So, using our Catapult POS system, we created a process that continually tracks inventory and is pretty simple to use. On Mondays and Thursdays, a grocery buyer places a purchase order by 11:00 a.m. I print the PO, build and wrap pallets of goods, then commit the purchase order to a tracking spreadsheet, which adjusts the inventory. As new product comes into the warehouse from the distributor, we post the invoice to the same spreadsheet, adding to the "On hand" page real costs, quantities, and the date of arrival. This way, our grocery team can always see, in real time, an accurate count of all 165 SKUs (current tally) on hand, what we paid for them, and the current retail price.

The scale of our Central Warehouse is small enough for one person to do all the work of receiving and slotting new product, adjusting the inventory sheet, and building pallets for delivery to the store twice a week. This work takes about six to eight hours a week, depending on the range of product the grocery team orders in. At our level of sales ($12 million/year) we generate about four pallets per week from the CK to the store.

As I write this, our grocery warehouse inventory is $40,000, with an additional $12,000 of body care inventory. In the last eight months since we started, our cash position has actually improved. In part, this is because we have added no significant staffing (my salary is already paid for) and already have a trucking system in place. The other reason our cash position is improving is because, with a warehouse, we have more ways to make money.

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Margin gain

Much of what we buy is just regular monthly deals offered by UNFI, though we also buy some items direct (paper goods, mostly), and broker buys are not uncommon. We generally get between 20 and 25 percent off for large deals, sometimes more, and we now have the advantage of picking and choosing what monthly deals to continue, sometimes for months on end. And the very good news is that we were able to lower prices (more stuff on sale all the time) and actually increase gross margin at the same time.

Prices went down, profit went up. *Catch 22*'s Milo Minderbinder would be proud.

The trick is what we call "pocket margin," which is the difference between the first month's retail sale price and the newer, slightly higher sale price that we set to sell out the remaining inventory. For the customer it's a deal, because food and goods are still cheaper for months on end than regular pricing. Plus there is the added and critical benefit to our grocery margin of reloading shelves, at reduced cost, right before the item goes off sale. So, on over a hundred SKUs at a time, we have cheaper food at a higher margin.

The proof of this thing is in the numbers: in the first six months our grocery margin jumped two full points and sales turned from negative 1 percent to a positive 6 percent. In fact, we are now using the margin gain from the warehouse to drop the margin goal for the produce department about 10 percent, something our members appreciate very much.

Telling the story

Somewhere in the middle of the sales downturn, when our growth was about negative 8 percent, we decided to change our marketing plan. We scrapped the bi-monthly newsletters and all elaborate ads. We went instead to daily, reverse type, strictly bold message ads in our local paper. In exchange for a long-term commitment we get great placement, and we can change these impact ads in just a few minutes. So the folks around town started seeing and remembering the price-related messages that were in the front section of the hometown rag each and every day, and sometimes twice a day.

Sometimes we tried to be department-specific: "*Over 100 Wines Under 10 Bucks*"; sometimes we just mentioned the new price of organic greens: "$1.99"; occasionally, we would put in something funky just to get their attention and remind them who we are. My fave: our Valentine's Day seafood department ad: "*Nothing Says Love Like Crabs*."

At the same time, we ramped up our web presence, jazzing up our site, getting a Twitter presence, and sending out weekly food e-news. We also offered web-based coupons, in-store member special coupons, and were very grateful to have a good selection of NCGA and UNFI coupons.

Moving on

Now that the boom cycle in our little Western town is over, our goal is to remain sensitive to the economic hardship that surrounds us while remaining loyal to the mission and values that built the house in the first place. In the deli, we will still create great and at times elaborate salads and entrees, but we also offer rice and beans, at a minimal price, at all times. Our grocery buyers remain unshaken in their commitment to how and by whom food is grown, but they also now have a keen eye for volume deals, closeouts, and even the humble but meaningful free fill. We do not hesitate to offer cheap food at a lower margin as part of our "Basics" program, and we keep a close watch on the competition.

We no longer believe the old adage that you can't change the public's perception of pricing. We seem to be doing exactly that, though only time will tell to what extent. In Bozeman, we believe it can be done. It takes some hard work, maybe a little serendipity, and a dash or two of humility in admitting that maybe we should have been doing this all along. ■