



January 1994

## **New Competition in Food Retailing**

By

Rod Hawkes

Department of Agricultural, Resource, and Managerial Economics, Cornell

Today, grocery store and supermarket operators face direct competition for consumers' food dollars from a broad array of alternative retailers. Among the most aggressive suitors are mass merchants (such as Wal-Mart or Kmart), drug store chains, wholesale club stores, convenience stores, limited assortment stores, and supercenters.

Traditional lines between types of retailers are becoming blurred as supermarkets and grocery stores have expanded into higher profit general merchandise products while general merchandise retailers have expanded into food products which generate higher customer traffic. Some of these alternative food retailers currently operate in New York State while others are rapidly on their way to entering this market. New Yorkers are familiar with most of these alternative retail formats and are increasingly relying on such outlets for their food purchases.

Two of these supercenters and limited assortment stores do not currently operate in New York State but will be opening here in the near future. Supercenters combine a complete supermarket and a full-line discount department store under one roof with common checkout aisles. These huge stores are being developed by Kmart and Wal-Mart, with both companies projecting rapid expansion in both number of stores and sales by the end of the 1990s. Kmart has already announced plans to develop supercenters in the Buffalo and Albany areas. Wal-Mart's initial expansion is concentrated in the southern states and it is not likely to open supercenters in New York as soon as Kmart will.

Limited assortment stores represent the other end of the spectrum in terms of size and selection. These small stores are about one tenth the size of supercenters. As the name implies, limited assortment stores do not attempt to compete with supermarkets on variety and selection, typically offering less than 1,000 products. Usually, limited assortment stores offer only one size and one brand of each product. These stores stock mostly private label or store brands which rival or surpass national brands in quality and performance. The main attraction of limited assortment stores for consumers is very low prices.

The US food distribution system has been proudly held up to the world as an example of efficiency. Americans spend far less of their disposable income for food than citizens of any other nation. Although the price of food tends to increase each year with inflation, the relative cost of food--as measured by the percentage of disposable income spent on it--continues to decline.

Supermarkets have traditionally taken some credit for the efficiency of the system, taking pride in delivering high quality food at low prices. However, due to lower cost structures and technological sophistication, most of the alternative retail competitors are providing food and grocery products even more efficiently than supermarkets have in the past. Supermarkets are responding to the new competition by re-examining their own systems and operations. Faced with low inflation, limited population growth, and intensified competition, supermarket operators must focus on reducing costs rather than increasing margins as a means of raising profits on a relatively static sales base.

One indication of the extent of alternative format competition with supermarkets is the percentage of items purchased at other retailers which could also be purchased at supermarkets. A 1992 Nielsen Market Research Survey of retail sales trends highlights changes in market shares of supermarkets and alternative food retailers across 292 major supermarket product categories. Between 1991 and 1992 supermarkets lost market share in 63 percent of the 292 product categories while alternative retailers lost market share in less than 20 percent of product categories. In fact, in 20 of the 292 product categories, supermarkets share of sales declined by 5 percent. The product categories in which supermarkets lost market share represent all supermarket food and non-food departments. Supermarkets only gained market share in 16 percent of the 292 categories while drug stores, mass merchants, and other non-food stores each gained market share in more than half the product categories. Convenience stores and wholesale

club stores saw their shares of the majority of categories remain unchanged. Clearly, mass merchants, drug stores and other non-food stores are aggressively challenging supermarkets for consumers' food dollars with market share growth in over 50 percent of supermarket product categories.

Despite the onslaught of aggressive new competitors, supermarkets still command the lion's share of the consumer's grocery dollar and have some strategic advantages over each of the other types of retailers. The overall effect of alternative retailer competition is likely to benefit the supermarket industry in the long run as responses to new competitors make supermarket operators more efficient and profitable. Consumers should be the big winners as the range of food shopping choices expands and increased competition lowers food prices.