

Industry Report: Supermarkets

Introduction

Decreased consumer spending and a sluggish national economy have taken a relatively minimal toll on the supermarket industry over the past 12 months. While credit woes and bankruptcy filings have challenged commodity retailers of all kinds, the Food Marketing Institute (FMI) reported that supermarket sales exceeded \$535 billion in 2007. Sales growth can be partly attributed to consumer's cutting back on restaurant spending. Industry leader Wal-Mart reported second quarter 2008 same store sales increases of 4.5% as shoppers aiming to save on gas costs frequent one-stop superstores. Meanwhile, The Kroger Company reported same store sales increased 5.8% over the first quarter of 2008 while smaller regional businesses such as Southern California-based Stater Brothers also posted comp. store sales increases over the first half of the year. In addition, niche stores selling natural and organic foods continue to add new store locations in an increasingly health-conscious marketplace.

Industry Outlook

Discount pricing strategies within large format, big box stores containing grocery departments, such as Wal-Mart Supercenters, Target and Costco, have put a strain on smaller, regional grocers. Additionally, consolidation within the marketplace is likely to affect the industry. Top-tier supermarket chains that increase their store base through the acquisition of smaller companies may struggle to absorb what they have bought while also defending their market share against discount department store chains and other low-cost operators. Experts predict that price points for staple items such as bread, eggs and milk will continue to climb due to rising energy costs and increased consumer demand. Finally, due to relatively thin profit margins and stringent operating requirements, technological advances will continue to be added conservatively. New solutions such as faster checkout machinery will need to quickly demonstrate positive results through increased profits and/or reduced operating costs.

Appraisal Factors

Based on recent liquidations and appraisal experience, Tiger Valuation offers the following factors for consideration when dealing with a supermarket chain or grocery store.

- **Inventory augmentation** – Supermarket traffic is driven by high-turnover perishable goods, such as dairy, meat and produce. In most cases, perishable goods must be replenished in order to preserve a balanced product offering during a going-out-of-business (GOB) event. Accordingly, liquidators need to ensure that they maintain relationships with vendors in order to augment the sale with key perishable items, which achieve higher gross recovery values than general merchandise. The proportion of replenishment goods received from company-owned distribution centers versus third-party vendors should also be monitored closely. Recovery values would be adversely affected if core perishable inventory is not properly augmented or if normal restocking patterns are disrupted.
- **Customer prescription lists** – For grocery stores that also contain pharmacies, the locations' script lists could be valuable assets. These lists are usually auctioned to competing pharmacies prior to a liquidation sale. The valuation of script files is typically predicated on gross margins, sales history, turnover rates and proximity and diversity of competing pharmacies.
- **Store type** – The supermarket industry is made up of a wide variety of different store concepts, including conventional locations, superstores, warehouse and wholesale clubs and convenience stores. The grocery inventories of warehouse chains and specialty stores generally have the highest recovery values because they stock fewer SKUs and, thus, have a less complicated expense structure than the more traditional grocery store model.
- **Staffing** – Payroll costs and employee benefits can be significantly higher for supermarket GOB events than other retail formats because employees often belong to a union. Liquidators can save on staffing expenses by eliminating non-essential departments, such as bakery and deli counters, as the sale progresses. Operating costs can be further trimmed as inventory is sold down, allowing the liquidator to collapse space by condensing goods into fewer aisles and selling unused fixtures.

Conclusion

According to FMI, just over 50% of every \$100 spent at grocery stores is used to purchase perishables, making the augmentation of goods such as dairy, meat and produce essential during a supermarket GOB sale. Turnover of perishable products can exceed 50 times per annum. As a result, in a liquidation sale lasting several weeks, properly replenishing perishable goods will net higher recovery values than simply selling down existing store inventory. Other important considerations include the value of customer script lists, the type of store being liquidated and staffing issues.