



How can grocers survive inflation without making the customer pay the price?

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After the roller coaster ride of the last two years, grocers hoped that 2022 would be relatively smooth and predictable. Unfortunately, that's not the case. With higher food, gas, and energy prices, inflation soared to 9.1%—higher than it's been since 1981.¹ In September, food at home prices were up 13%. While this rate was still at a historical high, it was also the first decrease in growth in 15 months.² But even with this slight ease, challenges remain. Grocers are still grappling with supply chain disruptions and labor shortages that are now complicated by inflation.³

In the extremely competitive grocery industry, with traditionally small margins, grocers must balance staying financially healthy without alienating customers by passing on too many price increases.

Just as inflation is affecting grocers, it is also impacting their customers and how they shop. Consumers have cut back on spending. For example, in March, 61% of U.S. adults surveyed primarily bought daily essentials, such as food and healthcare.⁴ At the same time, consumers bought more groceries online than they did the previous month—perhaps as a way to keep track and control costs.



Consumers are still looking for value as they adjust their spending habits. A recent McKinsey study predicts that not only are customers looking for value, but they also want to eat healthier.⁵ When they shop, they still expect the convenience of omnichannel shopping, and many are concerned about sustainability.

But the higher food prices are taking a toll on how consumers view grocery stores. Gallup's research found that consumer perception of grocery stores dropped significantly in 2022, a 14% decrease from 2021.⁶ When grocers pass on higher prices to customers, they risk customer loyalty and trust, which affects both the acquisition and retention of shoppers short and long term.

Bottom line: despite the challenges both consumers and grocery stores face, when consumers grocery shop, they still expect convenience, variety, and value. This can be difficult for grocery stores at any point—much less when inflation is rising. However, there are ways grocers can re-examine their processes to meet the business and consumer needs, with an emphasis on value. With operational and marketing tweaks, grocers can implement strategies that will streamline their businesses and give them an advantage for now and in the future.





Economic instability continues to rattle the grocery industry

Used cars. Chicken. Beef.⁷ The price increases for those items were initially subtle. But soon, inflation was evident as seemingly unrelated events like supply chain shortages and the war in Ukraine led to historic price increases. By June 2022, the price of food at home increased 11.9% over the previous year, with butter and milk leading the way, with year-over-year increases of 16% and 15.9%, respectively.⁸

Fortunately, the most recent forecasts suggest that inflation is receding, but a possible recession is looming even as that happens. Whether it's higher prices or smaller budgets, consumers feel the squeeze as they try to make do with less.

“The biggest impact of inflation on customer loyalty and the lifetime value of the consumer is if they start changing stores to shop by price,” explained Rob Wilson, Managing Director at L.E.K. Consulting. As a senior member of L.E.K.’s consumer and retail sector and head of the North American food and beverage practice, Wilson advises clients on growth strategy and other critical business issues. Grocers already see differences in foot traffic. “In certain areas, consumers are shifting to more value-oriented locations. If they stick and shift a portion or their whole basket to another retailer, it’s the worst-case scenario.”

Wilson said that although most consumers are affected by rising prices, value-oriented ones are most likely to change how they shop.

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Consumers expect more than competitive prices

Even though consumers are willing to shop for the best prices, they still expect grocers to offer more than low prices. Deloitte reports that 84% of consumers still consider health and wellness when purchasing fresh food, including more personalized nutrition.⁹ 55% of consumers still say they're willing to pay more for foods that contribute to their health.



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In addition to lower prices and healthy foods, consumers expect grocers to continue with the conveniences that started during the pandemic, such as online shopping, curbside pickup, and delivery.

Earlier this year, McKinsey reported that consumers expect a consistent value proposition, regardless of whether they shop in-person, online, or in-app.¹⁰ In fact, using a store app while shopping in person is increasingly essential. McKinsey also pointed to socially conscious customers who expect grocers to commit to sustainability.

With customer expectations for convenience and personalization fueled by technology and sustainable practices, all while maintaining competitive pricing, grocers may feel stuck between a rock and a hard place.

But grocers can use operational and marketing strategies to help keep inflationary pricing in check while building a better customer experience.



Redefining “value”

When customers think of “value,” they often think of the lowest price. And it’s hard to stay financially solvent when constantly competing on price. But value can mean much more, said Kevin Kincaid, Executive Vice President, Lead Client Partner at PureRED. “Total value needs to represent not just price but convenience and personalization,” he said. These aspects can be bundled into a full-value offering for consumers navigating uncertain times.

With that perspective on value, grocers can look at areas in operations and marketing where they can streamline processes to cut costs and increase efficiency.



Review supplier pricing

Grocers are fighting supplier prices, asking them to justify their increases. Kroger and other chains have asked brands to prove price increases are necessary and say they may stop carrying products or change suppliers if the prices aren't held in check.¹¹ In an age when supply chain disruptions also squeeze grocers, this may feel like a risky move. However, grocers can always look for better vendor negotiations, Kincaid said. "Any way that retailers can get more creative in how they negotiate their buys with their vendors so that they're able to absorb or potentially minimize the passing of that cost to consumers is worth considering."

Wilson confirmed that most retailers require justification for increases. "We're hearing more and more that it's harder to get retailers to accept price increases." A new supplier may offer lower prices, he said. This could be a short-term fix, he warned. "Some suppliers might drop prices to get their foot in the door and raise prices later."

Revamp offerings of convenience

During the pandemic, grocery delivery boomed when many people worked from home. But that was an expensive endeavor for retailers. Wilson said the home delivery option is less essential as people return to the office. "The definition of convenience changes. Maybe it's more convenient for me to schedule a pickup on the way home from work than to have it dropped off on my doorstep." Wilson added that if grocers can entice customers to use curbside, it's a significant cost saving for the retailer and one many consumers are willing to absorb.

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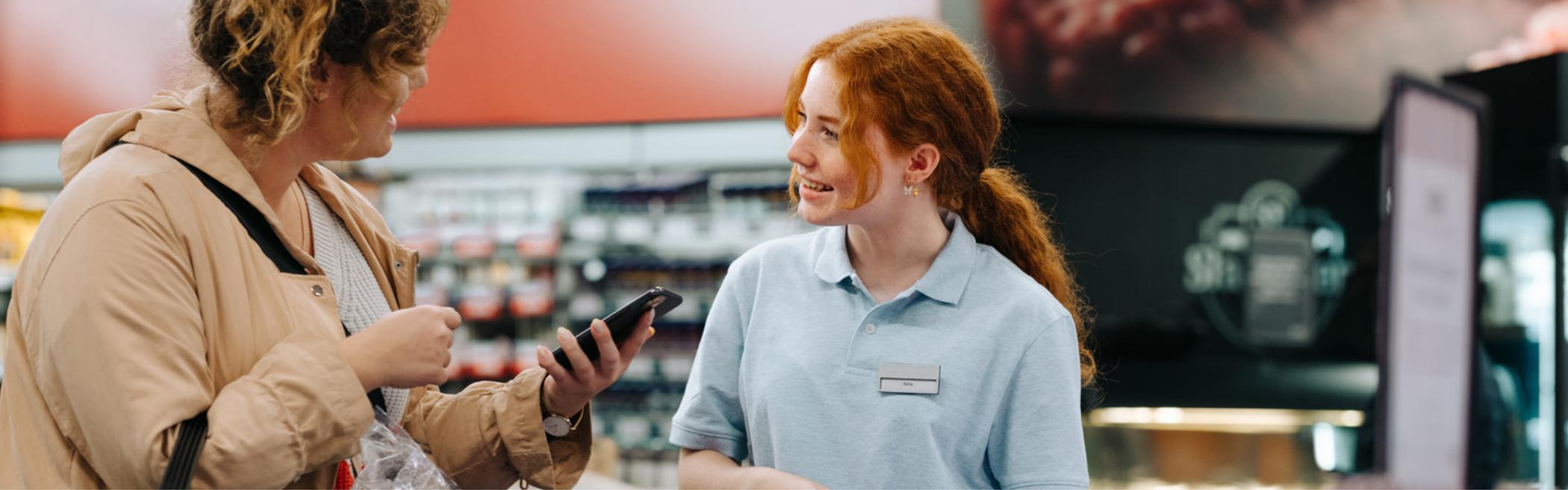
Rob Wilson, Managing Director at L.E.K. Consulting



Offer less, not more

Stockouts are a lose/lose/lose proposition. Suppliers lose because they can't fulfill orders. Grocers lose because they don't have the products on shelves. And customers lose when they can't find their favorite items at the store. Grocers used to try to offer consumers multiple choices for many occasions. Now, however, to reduce stockouts, the focus is on producing the most popular SKUs. "One of my clients just focuses on chocolate and vanilla pudding," Wilson said. "Forget about strawberry and banana or the other five flavors."

This streamlined approach creates a win/win/win. "It helps the consumer because it helps keep costs down. It helps the retailer not to have stockouts and lose the customer to a competitor. And it helps the supplier because they can keep the lines running longer without having to do so many changeovers for the different flavors, and those costs can ultimately be passed on."



Offer selective differentiation

In a National Grocer Webinar, IGA CEO John Ross said now is the time to “double down on differentiation,” adding that “differentiation is the weapon that grows share, even when times are tough, and shoppers are looking for a deal.”¹²

In the same webinar, Tim Lowe, President of Lowes Foods, said independent grocers could stand out by helping shoppers rediscover the fun of cooking at home while saving money. Grocers can help customers save money, discover the “thrill of cooking” restaurant meals at home, or learn how to stretch one protein into multiple meals.

Streamline processes

Wilson said that companies are looking at all of their operational processes to become more efficient. This exercise is necessary at any time, especially when budgets are tight. “Grocers are accelerating a lot of pre-existing initiatives and ideas toward a more efficient and automated supply chain. Automation doesn’t just help grocers save money. It also helps increase capacity.”

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Look at new perspectives in marketing

Grocers overlook how marketing can decrease costs while still benefiting revenue.

One challenge Kincaid's client had was the rising cost of distribution fees attributed to direct and shared mail pieces out to customers. "PureRED worked with this retailer to identify different substrates and sizes of communication fulfillments that would enable the retailer to reduce their costs from a printing and distribution perspective while still being able to get communication pieces out to consumers about their weekly promotions and offerings."

Kincaid said that changing some of the client's substrate and page sizing enabled them to reduce the press and printing size for consumers.

Kincaid said PureRED also worked with a retailer to eliminate the need for print ads and move to a digital offering that allows them to present their best offers to their customers in a one-to-one capacity instead of a more expensive mass circular.

Beyond the savings from changes in marketing material, grocers can gain when marketing is personalized and integrated into their day-to-day life. Kincaid said that expectation is different from ten years ago when customers were wary of companies having their personal information. "Now, it is the cost of doing business to be able to know your consumers, know what they care about most, and deliver a personalized experience for them. And the next step in that is being able to provide personalized offers, not just personalized content that is tailored."

Grocers have faced many economic changes, and those challenges are likely to continue. As they manage these changes, marketing and operational strategies can help them continue to add value to their customers.

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