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Store Brands: Driving Growth and Building Loyalty



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1. STORE BRANDS' STRATEGIC ROLE IN A RETAILER'S PORTFOLIO

To say grocers, retailers, and wholesalers experienced extremes over the last 24 months would be an understatement; a significant dip in revenue in the earlier stages of the pandemic followed by a healthy recovery, and now enduring the storm of inflation and rising commodity prices. **Now consumers are feeling the pinch of inflation** and nowhere does the cost increase hurt the wallet more than groceries. Double digit percentage increases from CPGs (e.g. Dairy products 10 – 12%) are now being passed through, impacting the consumer's ability to purchase the product and brands they usually enjoy, but cannot due to the impact of inflation.

Store brands now have a new opportunity to gain additional share vs. national brands. As consumers continue to stock up on pantry essentials as well as healthier and elevated premium offerings, **price increases from national brand products paved the way for consumers to try and/ or build a relationship with store brands.** The value, quality, and uniqueness of store brands products increased store brands' share of wallet with existing customers. In a news worthy shift, customers first chose store brands due to availability and then became repeat shoppers driven by quality and value. We believe these trends are here to stay and now is the time to capitalize on the tailwinds that emerged over the past 24 months by rejuvenating and reinvesting into programs.



“Driven by creeping inflation and supply chain disruptions, the future of private labelling seems to have arrived just about everywhere...”

Retailers are making big bets to continue winning in store brands

Over the past decade, 10+ retailers have built \$1B+ store brands. All the while, store brands growth has surged, increasing in size by 12% while on track to surpass national brand growth within the next 5 years. The growth of store brands is not going to stagnate anytime soon – 70% of retailers generating more than \$1 billion in revenue are seeking to invest, broaden, and diversify their supply chains in order to grow their store brands division.

While home furnishings, home décor, sporting goods, apparel, and other retail verticals are seeing a renewed interest in store brands, **grocery is the leading vertical where store brand is winning, with 56% of consumers purchasing store brands.** The store brands offerings of the shelf today bear little resemblance to the products of five years ago. Grocers have increased their total product offerings and most supermarkets today offer at least one store brand option in nearly all relevant product categories.

Historically, store brands has been focused on high-velocity national brand equivalent (NBE), but the game has changed. Consumers are now expecting national brand or better (NBB) quality while still realizing value. **Having a strong portfolio of NBB products across most edible and non-edible categories are now table stakes for retailers.**



The role of store brands is also evolving – grocers are realizing store brands is not only a volume play but allows for margin capture from the store perimeter. POS data affirms store brand offerings are expanding beyond the center store to align closer with consumer purchase frequency. Leading national grocers such as Albertsons, Kroger, and ALDI have moved well beyond center store NBB offerings. These grocers are continually launching and refreshing multiple differentiated brands within each value tier, including \$1B+ organics, free-from, and premium brands. As lifestyle habits change, natural, organic, and premium products are predicted to be a driving factor in store brands revenue and margin growth. These are clear areas to focus on for exponential and fast-paced growth. The time is now to make the investment in store brands.





Exhibit 1. Sampling of Private Label Portfolio across select retailers



Source: A&M analysis, Company websites

The graphic above (**Exhibit 1**) demonstrates how leading grocers have been innovating in premium spaces at a rapid pace, including high-grade packaging and quality ingredients. Most notably, Kroger and Albertsons have invested heavily in building out their premium, organic products, and natural/ free-from/ plant-based products with best-in-class success. Kroger's private label brand Simple Truth brought in ~\$3 billion in sales, and Albertson's Organics brand has generated ~\$1B+ in revenue. Even traditional low-cost grocers such as ALDI are infiltrating the premium tier, giving further evidence that grocers are fighting for consumers across tiers to effectively manage the volume-margin mix as low-margin Opening Price Points (OPP) are now expected.

Exhibit 2. Select grocer approach to product line tiering

| Well established across key food and non-food categories | | Growth engines | | |
|--|-----------|---|---|-------------------------|
| | OPP & NBE | Natural/Free-From | Organics | Premium & Super Premium |
|  | ✓ | <ul style="list-style-type: none"> Simple Truth – over \$3B in sales; expanding in plant-based products 660 Private Label products launched in 2020, 60% (~390 SKUs) in Simple Truth or Private Selection Transitioning national brand slotting to make room for Simple Truth | | |
|  | ✓ | | <ul style="list-style-type: none"> O Organics brand is ~\$1B in revenue and growing ~800 new private label products planned over next few years Expanding private label into prepared meals, innovating on plant-based products | |
|  | ✓ | | <ul style="list-style-type: none"> Target's private label brand - Good & Gather crossed over \$2B sales 600 new products added to Good & Gather portfolio in 2020, including into Good & Gather Signature Plan to add 30 new products in Good & Gather Plant-Based in 2021 | |
|  | ✓ | | <ul style="list-style-type: none"> Moving into upper-middle class demographics since 2019, remodeling and expanding store count Expanding organic, vegan, produce, and more elevated product lines Pushing for 100% sustainable packaging by 2025, continued waste reduction | |

Source: A&M analysis, company websites



Five Questions for grocers to answer

- Have our consumers switched to store brands during the pandemic?
- Which product categories are must-win and which ones are ripe for evolution?
- What is the value of getting this right?
- Where do we start to re-energize store brands program?
- What new capabilities do we need to lead?

In this article, we present a path forward for grocers to WIN through store brands



2. EVOLVING CONSUMER PERCEPTION OF STORE BRANDS



The effects of rising inflation and the COVID-19 pandemic have generated shifts not only in the product selection of consumers and what they elect to purchase, but consumer behaviors themselves. The pandemic presented an unprecedented time within grocery, when fear-prompted panic-buying caused delays within supply chains and ultimately led to a lack of access to many national brand products in-store. As we move into the post-covid world with inflation risks, we believe the momentum behind store brands is consistent and here to stay.

“While 53% of shoppers have intentionally purchased store brands products in the past year, the availability of store brands products has also played a role in addressing global product shortages ...”

We also learned that consumers are eating healthier now than they were at the start of pandemic, with a renewed focus on health and wellness goals. Lifestyle choices are also broadening (Keto, Paleo, etc.) and are top of mind for consumers, offering various pathways for store brands to win. **Ingredient quality and sustainability (packaging, sourcing, etc.) are seen as the next big trends** as product claims are now three times more likely to influence the purchasing habits of premium store brands consumers.

Private brands will need to respond to these consumer trends with an increased selection of organic, eco-friendly, free-from, and plant-based products that are aligned with consumer lifestyle preferences.

Evolving Consumer Preferences

The ease of obtaining and the affordability of store brands products compared to national branded products led more customers to purchase store brands as an alternative during the pandemic. Compelling product quality has had consumers expanding their horizons and embracing more store brands offerings. As these consumers notice that store brand quality is equal or better to that of a national brand, it is clear that consumers are willing to make the switch to store brands.

Multiple consumer surveys indicate that the “top reasons to purchase store brands products include lower price (60%) and having quality just as good as national brands (56%)”. It’s no secret that consumers are now loyal to store brands brands; not only are their products less expensive, but they are equivalent to national brands in terms of quality and provide an outstanding value per dollar. In a recent survey conducted by Alvarez & Marsal (A&M), **four in ten consumers indicated they believe the quality of store brands has improved over the past year, and one in three of these shoppers are purchasing more store brands grocery products than one year ago**. Many individuals who switched to purchasing store brands during the pandemic are going to continue to do so, with “33% planning to buy more store brands than pre-pandemic, and 13% lean towards buying much more”

Source: A&M 2021 survey, 2021 Shopper Experience Index, Statista, Numerator



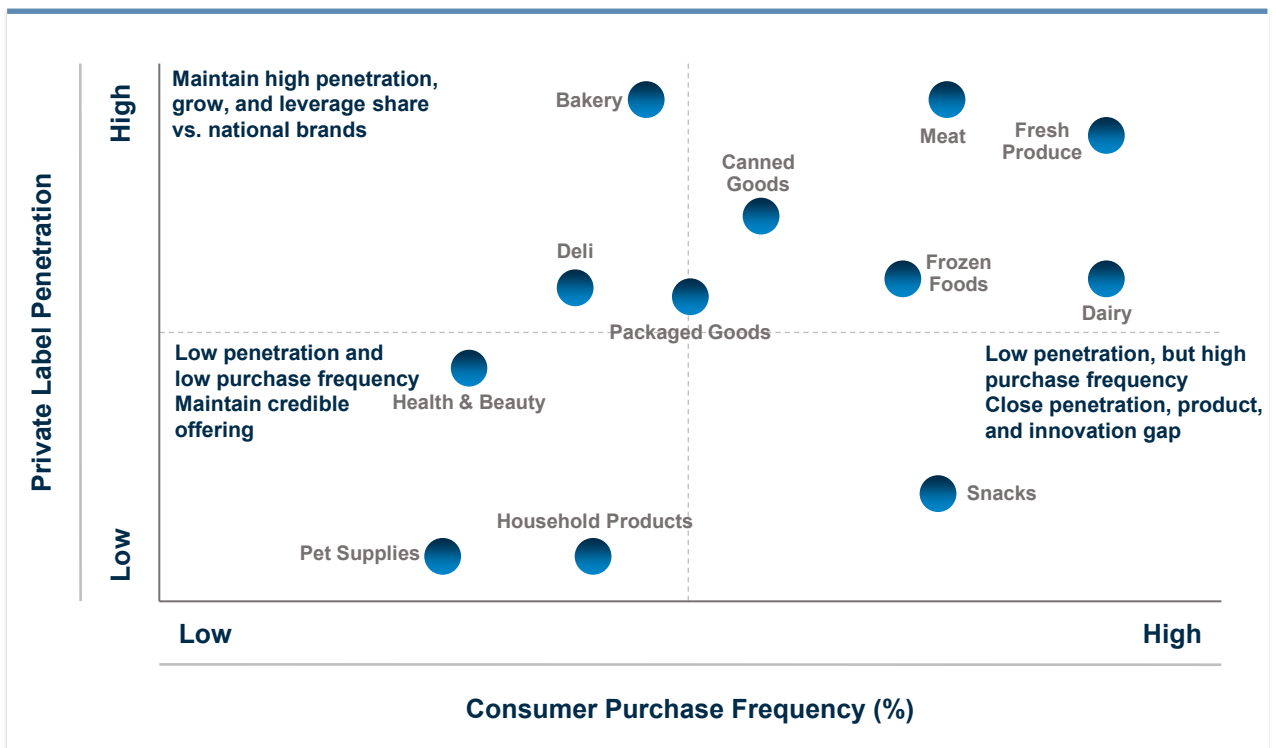


In a recent study by A&M, the majority of consumers surveyed believe the private label brand and the grocery store are equally important when deciding where to shop

A&M analysis of syndicated data across select categories shows assortment choices grocers should make in growing their product lines and categories.



Exhibit 3. Select Categories, Private Label Penetration vs. Purchase Frequency



Source: A&M analysis, FMI, Consumer Insights, Company websites

Our analysis of syndicated and consumer survey data indicates the following approach to select categories:

A

Center Store Packaged Goods such as cereal and oatmeal – have become table-stakes categories. Consumers directly compare national brands such as Post and Kellogg's while evaluating value

B

Center Store H&B/ pet supplies – high margin but very hard to execute due to food packaging requirements, brand recognition/ affinity of consumers. Apart from Target's recent foray into pet food, others have taken a wait-and-watch approach

C

Perimeter including bakery, deli, fresh produce/ meat – these hard to execute categories present tremendous opportunity in their role as traffic drivers

D

Frozen/ Refrigerated – Margin generating categories along the perimeter are also becoming key battle ground categories. Proliferation of private label in the cheese aisles in Kroger, Target, Jewel-Osco and several other grocers point to this trend

CHEESE AISLE

Meijer Example



- ~60%+ of the assortment is dedicated to private label natural cheese
- Kraft Heinz divested natural cheese partially due to competition with Private label

PAPER PRODUCTS SHELF

Albertsons Example



- Open Nature (natural) top and Signature (NBE) middle shelf placement. Value Corner (OPP) bottom shelf placement
- ~40%+ assortment is private label

Source: A&M analysis

Survey data confirms consumer affinity towards private label products as being similar or better quality and hence delivering value.

Current consumer lifestyle trends are shifting towards sustainable and healthy products, offering grocers the latitude to penetrate select categories that are likely to boom in the near future. Albertsons CEO recently noted, “Our Private Label is a key component in driving customer loyalty and satisfaction,... 100% of most loyal customers have Private Label products in their baskets....The Private Label customer is incredibly valuable to us as well...these shoppers make 16 more trips a year and spend over \$560 more during that same timeframe” (Winsight Grocery Business).

The store brands market is tried and tested and offers grocers the opportunity to implement an immediate go-to-market strategy. **A&M analysis indicates this store brands grocery to be a \$100B opportunity, so the real question every retailer should be asking themselves is – Why haven’t we addressed this space sooner?**



CASE STUDY

KROGER: KNOCK-OUT PRIVATE LABEL PERFORMANCE



The Journey

Kroger did not always generate over \$30B in annual private label sales, own a network of dairy, meat, and bakery plants that manufacture ~40% of its own brands, or its own data analytics firm – it has been a decades-long journey focusing relentlessly on the product, following data, and putting the customer first.

Following the release of 'Simple Truth' in 2012, Kroger's CEO stated, "One of our fastest-growing departments is Natural Foods. Our customers told us they want organic and natural products that are easily identified and affordable, so we launched them."

Kroger continues to act in-line with consumer preferences, "...Digital and fresh matter to our customers, and we have continued to invest and grow our capabilities in both areas, leading to significant share of wallet gains in both digital and total food at home."



How Kroger Led

- Built an ecosystem of in-house manufacturing sites and contract manufacturers
- Developed world class analytics and consumer tasting programs
- Optimized the assortment to feature private label
- Uses all-in landed cost view
- Innovated – Murray's Cheese shop, premium and plant based offerings, etc.
- Had consistent CEO agenda and support



Evidence and Results

- \$30B+ in private label sales
- 1 in 4 products purchased by customers are Kroger brands
- Current portfolio of brands: \$3B+ Simple Truth brand and Simply Organic \$1B+ in revenue
- Private label sales penetration of ~30%
- Private label margin contribution of ~23%

Source: A&M analysis, Company publications

3. THE VALUE OF GETTING IT RIGHT WITH STORE BRANDS



The shift from branded to private label grocery products will likely continue and accelerate as there are tangible benefits to capitalizing on these trends. Average private label dollar share for traditional grocers is ~20% and leading national grocers, namely Kroger and Albertsons are nearing 30% and pushing boundaries by targeting ~40% private label penetration. **Growing overall private label penetration from 20% to 40% represents a ~\$100B opportunity in the \$500B US grocery market**, but what is the additional unlock by achieving these increased penetration targets?



Increased Profitability and Working Capital to Fund the Future

Cross-category gross margins for private label grocery products averages ~35% compared to ~20% gross margins for branded products. Simply put, grocers will generate additional profits by making private label growth a strategic priority. Additionally, the lower acquisition cost of private label product improves free cash flow and reduces working capital. This creates the opportunity for grocers to fund the near future and compete with leading national chains through initiatives such as:

- Strategic Investments in value added services, technology, and e-commerce
- Product and packaging innovation to align with evolving consumer trends
- Fund future private label growth through re-investing in high levels of own brand promotions and/or pricing



Capture Customers and Drive Category leadership

Multiple consumer surveys including A&M's survey shows the strength of a private label brand is as important as the store itself. Growing own brands through improved penetration ultimately increases store traffic and consumer loyalty. Capturing these customers and their loyalty to store brands is an enabler for expanding beyond traditional private label categories and into those with higher margins, and provides the ability to drive innovation and disruption within categories (e.g., Kroger's plant-based meat products).



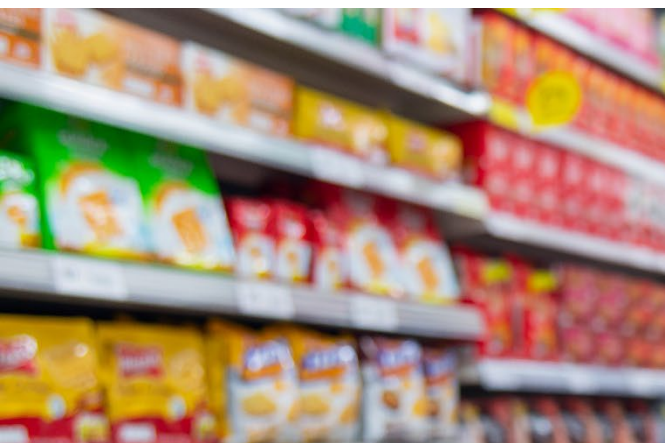
Increased Leverage with Branded Manufacturers

Mature and robust private label programs create the opportunity to improve leverage with branded manufacturers. Private label grocers, however, must be willing to convert additional facings to private label. This value can be captured in the form of negotiating better wholesale prices, increased trade fund rates, and increased allowances in categories where private label is strong.



Operational Excellence & Supply Chain Resilience

Growing private brands and strengthening supplier relationships can improve supply continuity, on-shelf rates, and supply chain efficiency (e.g., higher volume items). Even as pandemic impacts on supply chains begin to diminish, supply chain resilience will continue to be a focus for grocers who need to focus on delivering on their customer promise. Private brands thrived during the pandemic and will continue to be a mechanism to maintain supply chain resilience and supply continuity.



“Retailers are trading slotting fees for better margins and customer loyalty...”

4. EXECUTING STORE BRANDS AS A GROWTH ENGINE

A&M CASE STUDY: ACCELERATING A WHOLESALE DISTRIBUTOR'S BOLD STRATEGY TO WIN IN PRIVATE LABEL



Situation:

- Grocery wholesale distributor with \$10B+ revenue and 3,000+ stores
- Maintained multiple private label brands across the portfolio, from opening price point through organic and premium



Challenge:

- Private label brand program was under evolution with low brand penetration, premium and organic programs at the early stages of development
- Brand architecture had overlapping value propositions
- Aimed to achieve wholesale private label penetration of ~25%+
- Increasing product cost due to inflationary pressure while maintaining quality



How did A&M help

- Conducted primary market research to understand brand perception and opportunities across the architecture
- Helped define the overarching strategy
- Deployed assortment optimization approach for select categories
- Integrated a framework for PL category leadership
- Ran RFP to drive value capture during 2021 (2-4% improvement in an inflationary environment)
- Designed a comprehensive private label strategy plan with glidepath to increase sales by ~35-50%

In our experience, the pathway to win in private label centers around balancing two key elements – **pragmatic strategy and disciplined execution**. This also serves as the building block for a holistic reinvention framework (**Exhibit 4**) by creating immediate impact to fund the program and establishes the near term and longer-term roadmap.



Exhibit 4. A&M framework: Store Brands Strategy and Execution





Source: A&M

When embracing a case for change or the reinvention of private label brands, grocers are faced with tough questions - what's the starting point, how to start, and what are the goal posts. The indicative questions on the following page can help a grocer determine the starting point in their journey.



Indicative Key Questions for Strategy and Execution *(not exhaustive)*

| | | |
|---|--------------------------|---|
| STRATEGY  | Positioning | <ul style="list-style-type: none"> What is the key value proposition for each brand in the portfolio? Are category roles (Traffic, Margin, Basket) well defined? |
| | Price & Promo | <ul style="list-style-type: none"> For KVI and OPP items, are price points defined and differentiated? How can owned brand promotional effectiveness be improved? |
| | Product | <ul style="list-style-type: none"> What is the right mix between OPP, NBE, natural, and premium? Is there pruning opportunities to reinvest into whitespaces? |
| | Placement | <ul style="list-style-type: none"> Do all regions/ divisions carry adequate penetration of products? Can Planogram placement be improved for owned brands? |
| EXECUTION  | Platform | <ul style="list-style-type: none"> Do tools exist today to compare dead net pricing for name brand and store brands? Is most category manager's time spent collecting data or analysing and acting? |
| | Process | <ul style="list-style-type: none"> Is the store brands team setup and enabled to act as a leading CPG? Is the category management fully integrated across name brand and store brands? |
| | Procure | <ul style="list-style-type: none"> Does a defined sourcing calendar with RFP cadence/ targets exists? Do store brands mega suppliers view you as a strategic long-term partner? |
| | People | <ul style="list-style-type: none"> Is the role of the core merch. team and support functions clearly defined? Are merchants acting as buying specialists or overall category leads? |

Source: A&M analysis

To begin executing, we recommend a simple 3-step approach to accelerate growth and drive value capture.



01

DIAGNOSE

Diagnostic study to identify strength and gaps in the portfolio



02

PRIORITIZE

Prioritize top areas for strategic definition and unlock immediate value through sourcing market events



03

SCALE

Integrate and execute against strategic priorities

Working through this process, the actionable outcomes include a well-defined go-forward strategy, development of internal capabilities to drive store brands growth, and the strengthening of execution muscle to drive the program forward.

There are strong industry tailwinds for continued store brands growth, but grocers must continue to manage supply uncertainty and the impact of rising commodity prices on margins and shelf price while delivering on growth targets. Now is the time to act with a (re)invigorated, end-to-end store brands strategy to navigate near term oscillations and establish the longer-term roadmap to capture the minds and hearts of the consumer.





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WE CAN HELP!

We bring consulting and operational experience in Retail and Consumer Goods across functional areas such as strategy, operations, supply chain and commercial functions. We have lived through these challenges and have firsthand experience.





CONSUMER AND RETAIL GROUP

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With over 5,000 people across four continents, we deliver tangible results for corporates, boards, private equity firms, law firms and government agencies facing complex challenges. Our senior leaders, and their teams, leverage A&M's restructuring heritage to help companies act decisively, catapult growth and accelerate results. We are experienced operators, world-class consultants, former regulators and industry authorities with a shared commitment to telling clients what's really needed for turning change into a strategic business asset, managing risk and unlocking value at every stage of growth.

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