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U.S. Consumers Trade Down As Economic Angst Grows

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Spurred by economic worries, American shoppers have quickly decided that cheaper is better. They are trading down to store brands from fancy labels, to small cars from SUVs, and to deep-discounters from full-service stores.

Wal-Mart Stores Inc., which last year returned to its discount roots to try to reverse weakening sales, Thursday reported its best monthly sales gain in four years; it benefited from bargain-hunters seeking deals on the most basic stuff.

Discount stores overall saw sales jump nearly 6% last month, while those of full-price department stores declined. Consumers' use of discount coupons is starting to rebound after a 15-year slide. In June, the lowly Toyota Corolla became the best-selling vehicle in America, a spot held for more than two decades by the beefier (and pricier) Ford F-150 pickup.

Trading down is a common consumer reaction to economic ills. But this time around, the change has come unusually fast and may be touching on the broadest array of goods since the recession of the early 1980s. The combination of historically high fuel prices and soaring food costs, combined with falling housing and stock values and tightening credit, are severely damping the spending habits on which the U.S. economy has long thrived.

The about-face in consumer behavior could bring striking changes to the marketplace, as retailers revamp everything from the size of their stores to the way they stock their shelves, and may force manufacturers to trim niche products in favor of more reliably selling basics.

"There has been a major shift in thinking by shoppers," says Thom Blischok, head of consulting at Information Resources Inc., which tracks spending on consumer goods. "Consumers are moving away from availability, to affordability." Dunnhumby Ltd., a consulting firm that tracks shopping habits for many retailers and manufacturers, says 20% of loyalty-card holders of its U.S. and European retail clients are "radically" reducing spending, according to its analysis of their purchasing data.

The shift challenges a 20-year embrace of ever-pricier exotic foods and a widening array of luxury goods. In the 1980s, Americans warmed to designer labels, Egyptian cottons, and shopping as a form of entertainment.

Now, consumers are pessimistic that their ability to spend will improve any time soon. Two-

thirds of Americans expect the current slump to last for several years, according to the latest Reuters/University of Michigan survey of consumer expectations. Consumer confidence has dropped 38% in the monthly index since its January 2007 peak, and last month 57% of those surveyed reported their financial situation had worsened, the highest figure since the survey began in 1946.

Buying Habits

At almost every income bracket, Americans are changing buying habits and deciding they can live without old favorites. Bob Swanson, a 48-year-old Houston software salesman, drove BMWs for most of the past two decades. But as the price of premium gasoline jumped, he traded his 8-cylinder BMW 540 for a more frugal 4-cylinder Honda Accord that he bought secondhand. "I went from an average of 14 miles a gallon to an average of 24," Mr. Swanson says.



Associated Press

BARGAIN HUNTING: American consumers, like these shopping this week at Wal-Mart in North Little Rock, Ark., are increasingly seeking low prices on basic items, helping drive up discounters' sales.

For instance, in Texas, grocer HEB Inc. has begun stocking up on inexpensive fare -- beans, rice and flats of eggs -- toward the end of the month, as customers run out of money.

Wal-Mart says it is putting more multipack items on its shelves at the start of the month when many customers are flush from being paid, then switching to individual items that require smaller outlays later in the month.

Thursday, the nation's largest retailer reported that U.S. same-store sales for the five weeks ended July 4 rose 5.8%, Wal-Mart's highest monthly increase since May 2004. The big results for the June reporting period were partly attributable to temporary factors benefiting many discount retailers. Federal tax-rebate checks were trickling in, and there were two first-of-the-month days in the period, when many customers get paychecks or government payments and visit stores.

Back to Its Roots

But Wal-Mart also returned to its roots at just the right time. Unlike other retailers, the

Visits to department stores are down 6% this year, down 7% at office-supply stores and down 10% at home-improvement retailers, says market watcher Nielsen North America, which tracks store traffic and spending. But the downturn has proved a boon for retailers at the bottom of the price scale. **Family Dollar Stores Inc.**, a small, discount department-store chain, forecasts same-store gains of 4% to 6% for its fiscal fourth-quarter ending Aug. 30. **Dollar General Corp.**, another discounter, recently reported same-store sales jumped 5.6% for the fiscal quarter ended May 2.

Trying to lure the newly frugal, big retailers and brand-name goods manufacturers are revamping their goods and promotional offers to suit the times, relying on increased efforts to track their consumers' habits.

discounter's less-affluent customers felt the pinch of rising energy and credit woes as early as 2006. Wal-Mart ultimately responded by cutting back on new-store construction and revamping its merchandise. It cut inventories and renewed its focus on reducing prices, just as the economy swooned.

This year, its stores were better equipped for consumers looking to trade down. Wal-Mart also increased advertising spending by 42%, rolling out a campaign that highlighted savings.

Sears Holdings Corp., in contrast, last fall loaded up on clothing, home-goods and holiday merchandise. It was forced this spring to cut back on marketing and discount heavily to clear its shelves. Same-store sales in the quarter ended May 3 fell 9.8% at its Sears stores and 7.1% at its Kmart unit.

Some big-name brands are testing new approaches to try to keep customers. "The reality of the business is you've got to come to the table with an offer," says Bryce McTavish, vice president of retail and sports marketing at MillerCoors, a joint venture of beer makers SABMiller PLC and Molson Coors Brewing Co. One new strategy: Placing lower-priced Coors Light alongside Blue Moon premium beers in store displays, to encourage Blue Moon drinkers who want to economize to stay within the brand. Miller Coors also is weighing offering gasoline cards with purchases as an incentive.

The ability to capture trade-down shoppers will be crucial for some companies. New, cheaper favorites among brands or stores can be formed after as little as three or four favorable experiences, retail experts say.

But unfortunately for some retailers, "the tide is going out," says Credit Suisse analyst Gary Balter. He forecasts retail profits will struggle until "2010 at the earliest," when the current spending weakness should lift. Retailers now losing customers such as **Borders Group Inc.** and **Circuit City Stores Inc.**, both of which reported widening losses compared with a year earlier, won't have relief from slow consumer spending anytime soon, he says.

The next step for retailers and manufacturers is to weed out niche products that don't have mass appeal, says John Rand, a director of retail insights at consultant Management Ventures Inc. Some retailers already are considering dropping suppliers or products that don't generate big sales.

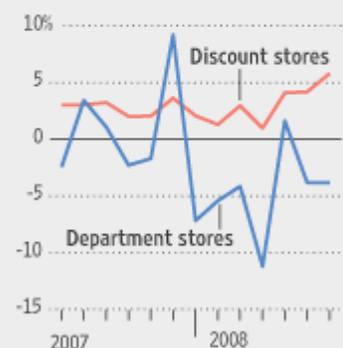
Most at risk are premium-priced items that appeal to convenience over value. Consultants' studies of consumers' food baskets suggest that vitamin waters, 100-calorie snack packages, and children's lunches in a tray are being supplanted by tap water, value-pack snacks and home-made lunches, respectively.

One retail trend already under way may mesh well with the change in consumer habits. Retailers known for their "big boxes" -- **Safeway Inc.**, **Tesco PLC** and **Wal-Mart** -- have or will soon introduce small 10,000- to 15,000-square-foot stores that fit into neighborhoods and contain just a few thousand products.

Pinching Pennies

Full-price department stores have struggled while discount stores have risen

Monthly change in same-store sales



Source: Thomson Reuters

A typical 50,000-square-foot grocery store sells 20,000 items. But most homes buy fewer than 1,000 items a year. Stores that can correctly pinpoint customers' choices will earn higher returns on these smaller spaces.

Electronics chains such as **Best Buy Co.** and **Circuit City** are embracing smaller-size stores as a way to boost margins by shedding goods with slow sales. Such limited-assortment, high-turnover stores may be the next big wave in retailing, says Lee Peterson, a vice president at retail-store consultants WD Partners.

In the meantime, shoppers' eagerness to save shows up in all sorts of ways. Consumers do more one-stop shopping, buying groceries only once a week or twice a month to save on gasoline and by buying in bulk. When they do, they are more apt to stick to a grocery list -- and bring coupons.

Matthew Tilley, director of marketing at Carolina Manufacturers Services, a large coupon processor, says coupon redemptions last year already stopped falling for the first time since 1992, and the company forecasts increases for the rest of this year.

Consumer demand for lower-cost private-label and store brands also is leading retailers to license those brands to competitors to broaden their reach and increase sales. Best Buy now sells its Rocketfish private-label electronics through Japanese retailer K's Holdings. Safeway is selling its O brand of organic foods through restaurant supplier Sysco Corp. and the world's second-largest retailer after Wal-Mart, France's Carrefour SA.

Sales of private-label goods are up sharply, especially for staples with escalating prices. The cost of eggs has risen 33% this year, milk is up 18% and flour nearly 11%, says consulting firm Information Resources Inc. And even higher prices may be coming.

"We haven't yet seen the real impacts of rising commodity costs," says Mr. Blischok, IRI's head of consulting. "We're in a transformation that affects how you spend your money, where you go, what you eat," he says.

IRI's grocery-basket surveys show that sales of prepared foods such as Kraft Foods Inc.'s Lunchables have tumbled. Americans are eating at home more, buying multipurpose medications rather than separate medicines, and choosing a single brand of shampoo instead of one for each family member, IRI studies show.

U.S. premium gasoline sales so far this year are off 12.6%, compared with a just 1.3% decline in regular unleaded sales, according to delivery figures compiled by the U.S. Energy Information Administration.

In some cases, saving money is replacing conspicuous consumption as the object of awe. Linda Butler, a Portland, Ore., homemaker who has used coupons for decades, says that in the past six months she has often been approached in the checkout lanes by other shoppers seeking shopping advice. The 51-year-old homemaker routinely cuts a \$150 grocery bill down to a \$40 outlay through intensive use of coupons.

"People are asking me, how do you do that? Where do you get the coupons?" Mrs. Butler says. She is thinking of setting up classes on how to save money, she adds -- for a fee, of course.