

Whole Foods Market, Inc. (WFM) Memo

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Company Description

Whole Foods Market, Inc. is a chain of over 350 organic supermarkets that operate in the United States, Canada and the United Kingdom. They sell a variety of food and household items including produce, meat, vegetables, seafood, spices, bakery, catering, vitamins, clothing, books, floral items and specialty products such as beer, wine and cheese. Focused on providing their customers with the highest quality products, they stress the importance of not only fresh and organic foods, but also an in-store experience unlike any other grocery chain. They produce their own brand of all-organic products called "365" that is meant to allow for people of all economic classes access to organic foods. With over 80,000 employees, Whole Foods is about more than just grocery shopping, it is about "pursuing a healthy lifestyle".

Thesis / Key Points

- **Rise of the healthy eating/organic trend:** Over the past few years, American consumers have been becoming more health conscious as obesity rates have risen and healthy eating has become a hot-button issue. As this issue has come to the front line, Americans have started buying more and more organic products, as they believe that these foods are healthier. Especially as the economy has started to turn around, consumers are finding more cash in their pockets to pay for these more expensive organic products. The market was valued at \$57.5 billion in 2010 and is expected to grow to \$104.7 billion by 2015. Last year, the organic products sector of grocery reached 13% growth across all retail chains. As this market continues to grow, WFM will benefit because it is the first and most well-known "certified organic" retailer in the country. All of their products are 100% organic and because consumers are aware of this fact, WFM will most likely be the first place they turn to when looking to buy healthy.
- **Incredibly strong brand awareness and loyalty:** WFM currently operates in somewhat of a niche and within that niche they have incredible loyalty from their customers. They target people looking to eat healthy (and those who can afford to pay for the more expensive products) and aim to be the "go-to" place for those consumers. So far, they have succeeded in this mission as they are absolutely the number one national retailer of organic products. Most of their customers either do all of their shopping at Whole Foods, or they come to WFM for specific reasons but always look to Whole Foods when those needs arise. These loyal customers seek out the WFM stores, and consistently say that they are willing to travel farther to a Whole Foods even if a normal supermarket is closer to them. In addition to the loyalty of their customers, they have an excellent image among American consumers. They are not seen as a purely profit-seeking corporation as most other large grocery chains are because their products are of high quality and they consistently receive positive press about their corporate governance. WFM is usually an excluded when other grocery companies are getting ridiculed by the press about issues such as pesticides and the wages of their workers on farms. In fact, they have actually been praised in the past for engaging in agreements promising to ensure that anyone handling their food will receive proper wages and care. Additionally, they were named "World's Best Retailer" by World Retail Congress in 2013.
- **In-store experience unlike any other:** Another unique quality about the WFM stores is what comes with the shopping experience. The first thing you notice when you go into the store is the presentation of the foods. Unlike a supermarket such as Kroger where the food is jammed into aisles with harsh lighting and linoleum floors, WFM's stores are friendly, welcoming, easy to navigate and attractive. Rather than boring signs labeling the food, there are hand-drawn chalkboard designs explaining where the food is from and what has gone into bringing it here, plants of all kinds line the tops of shelves, the aisles are wide and easy to navigate, and the presentation of the products helps customers see the array of choices they have. All of these things help the shopper realize that care and thought was put into bringing their food to the store. In addition to normal shopping, the WFM stores offer easy to-go and buffet-style food options in the form of a dining hall or restaurant. This provides shoppers with the opportunity of taking home already-made organic meals. This feature became so popular in stores that now most stores have seating areas so that people can stop in and just grab a meal even if they aren't looking to do all their grocery shopping. To top it all off, the staff at the Whole Foods Markets are exceptional. They are incredibly knowledgeable about the food and the stores and they are amazingly friendly. They have been known to memorize the names and orders of frequent shoppers in order to make them feel more "at home" and welcome in the stores.
- **Becoming more price-conscious:** In order to stay competitive and continue to grow, WFM realizes it needs to adjust its prices to attract new customers. They set a goal of opening 1,000 stores and have started some initiatives to generate the growth in consumer base needed to reach this goal. A few years ago in response to their higher than average prices that gave them the nickname "Whole Paycheck", they created their "365" brand, whose slogan is "Certified organic products at everyday great value prices". This brand is owned and operated by WFM, giving them more control over the pricing and thus allowing the cost-conscious shopper to buy organic products in their stores. Over the past year, WFM has begun making efforts to appeal to these shoppers by offering coupons on their website and in-store as well as beginning a series of "budget friendly recipes". They offer these recipes in-store and online along with "money saving tips" with ideas for how to prepare cheap meals during different seasons using products found in the Whole Foods stores. In the coming year, they plan to continue this appeal to the price-conscious shopper by instituting a rewards program. They currently have no loyalty program or rewards card, and in 2014 they are planning on starting both. The plan is to have the programs run similarly to programs found in larger supermarket chains. In addition to the rewards programs, WFM realizes that competition is increasing from the larger supermarkets as they begin to open their own organic sections and brands. They are also opening a test store in Detroit that will be specifically targeted to the lower-class shopper in order to explore the possibility of opening entire stores for this demographic.

Misperception

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13%. Comparable-store sales are now forecasted to increase 5.7%-7% whereas before they were expected to increase 6.5%-8%. After this release, investors lost a lot of confidence in the stock and shares fell almost 10% as a result as hasn't fully recovered. WFM executives blame these decreases on cannibalization created by the many new store openings in Q4 2013 and 2014, but investors fail to see that this cannibalization is most likely short-term. This has happened to WFM's stores in the past but has generally fixed itself after a year or two. When first opened, many Whole Foods stores compete with themselves because they are usually in similar areas and attract similar customers. However, this rarely lasts as the stores then begin to attract new customers within a year and ultimately increase growth for the company in the long run.

- **WFM can't compete with larger supermarkets:** Investors are also concerned about the rising competition from larger supermarkets such as Kroger who are beginning to establish their own organic product lines and eating into WFM's customer base. They worry that WFM's price point is not able to compete with the cheaper supermarkets. What they fail to see, however, is the current and future plans that WFM has in place in order to decrease their prices. Many investors don't mention their 365 brand, which is actually at the same price point as many of the supermarkets' organic lines, as well as their plans to begin a rewards program and their other efforts to appeal to the price-conscious shopper. They also seem to discount the fact that WFM has established itself as the #1 place to buy all-organic products and that will be incredibly hard for the supermarkets to compete with.

VAR

- **Shopper loyalty:** On the busy grocery-shopping day on the Wednesday before Thanksgiving, I went to my local Whole Foods in Chicago to talk to shoppers about their Whole Foods experience. I asked them if WFM was their grocery store of choice, and if so why and if not, then what brought them to the store that day. Of the 30 people surveyed, 19 said they did most or all of their grocery shopping at WFM. Almost every single response to the "why?" question mentioned the importance of organic, fresh and healthy foods and that Whole Foods was the best and most trustworthy place to get those products. A few also mentioned they appreciated the fact that WFM seemed to actually care about what they put in their stores and they weren't just there to get the customers in and out. One woman said, "They actually care about the quality of what goes on their shelves and that matters because nothing is more important than what you put inside your body." The 11 that didn't shop regularly at WFM said that they were there for one of two reasons: one, because WFM provided a specialty product that is hard to find at other stores, or, two, because they were using WFM to cook their Thanksgiving dinner. A few of these shoppers said that while they didn't shop at WFM on a weekly basis, they were using their organic Turkeys and other "Thanksgiving foods" to make a healthier dinner. One mother said "I had heard good things about their turkeys, so I figured why not try it? So this year I bought everything here." The customers that were looking for more specialty products such as spices or gluten-free products, said that when they needed these items they almost always came to WFM. Reasons for this were the selection and variety of what would normally be specialized products at supermarkets as well as the fact that they tended to be cheaper at WFM than at other specialty stores. Every shopper asked had a supermarket grocer that was closer to their home than the WFM store.
- **Creating a unique in-store experience:** (more about this in the exhibits) I also talked to the manager of my local store about how he creates such a unique environment. He says that it absolutely starts with the staff, and when hiring he looks for a specific type of person that will love their job and use that to make the shoppers feel welcome. He then said that the next most important thing is store atmosphere. He pointed out the presentation or "plating" of all the food items as well as the extensive information about all of the products. He said that "the goal is to not hide anything from the customers. We have great products and we want to show them off." To him, creating a friendly and welcoming store is incredibly important to gaining and keeping customers.

How It Plays Out

- My prediction is that the WFM stock will recover in the later parts of 2014 as the cost-conscious initiatives kick in and the cannibalization effects of 2013 wear off of their new stores. This will most likely lead to better than expected 2014 results. They also intend to continue store growth into next year, with plans to open around 35 stores. These new store openings will also help increase revenues. If all goes well WFM should be a \$70 stock, which would be an appropriate time to sell.

Risks / What Signs Would Indicate We Are Wrong?

- It is possible that the recent decrease in stock price was a proper adjustment to what the price of the company should be. If this is the case then WFM's share price will probably not increase as much as we would like in the coming months. There is also a chance that WFM will not succeed in competing with the larger supermarkets because of their image and price point, in which case they would lose market share and the share price would most likely drop. If either of these things were to happen and WFM were to drop below \$50, we would need to reevaluate our position.
- A current attractive aspect of WFM is the fact that it has high margins, and these margins are at risk as it tries to lower some prices to attract a new demographic. If WFM doesn't succeed in changing their image and bringing in new customers at this price point, then their revenues could take a hit causing stock prices to drop.

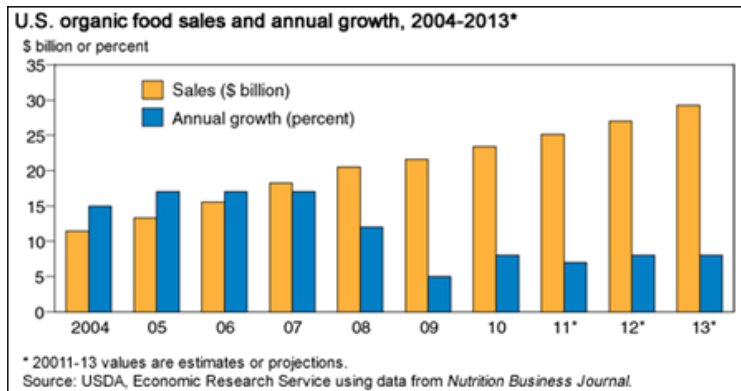
Signposts / Follow-Up

- We should continue to monitor the revenues generated by WFM as they are a great indicator of whether or not their business strategies are working. It is also worthwhile to track profit margins, as they will most likely be affected going forward. WFM also operates with little to no debt and keeping track of that going forward could be good insight into the shape

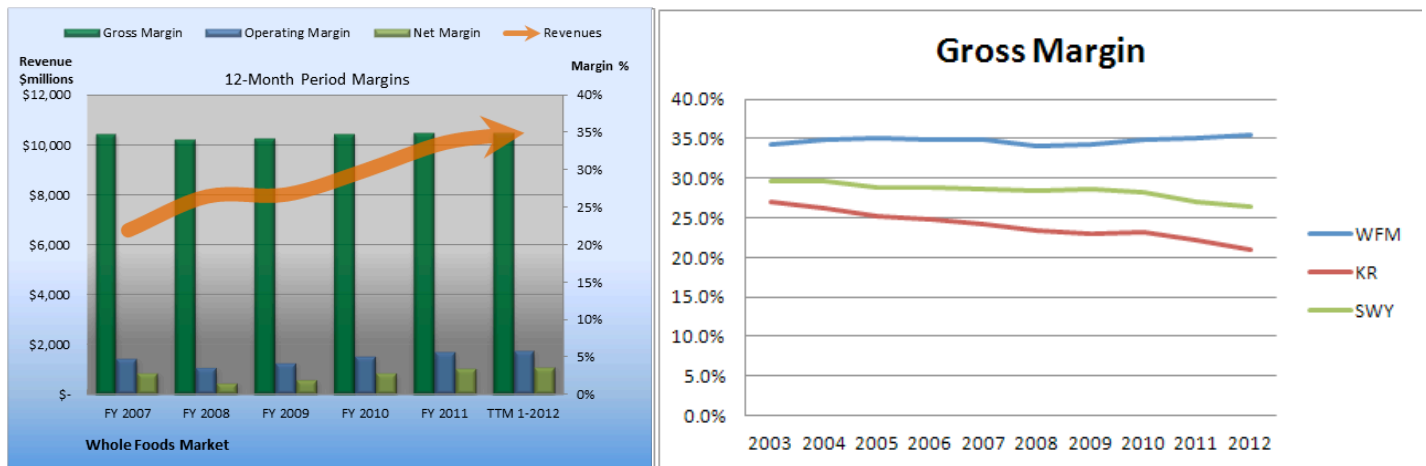
Important Company Financial Data

Current Price (12/3/13): \$56.69	Operating Cash Flow: 1.01B
52wk Range: 40.70-65.59	Total Debt: 27.0M
P/E (ttm): 38.56	Revenue: 12.92B
Forward P/E (1yr): 28.49	EPS: 1.47
Div. & Yield: .48 (0.9%)	Market Cap: 21.11B

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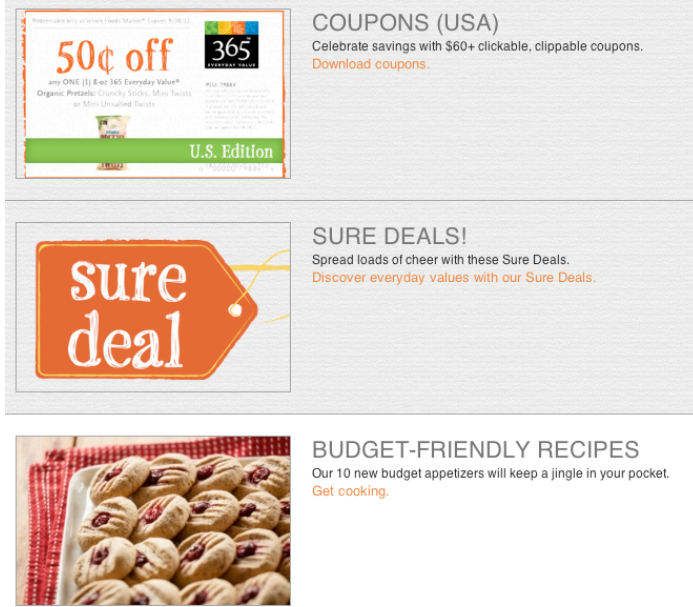
The organic food industry is growing in the US and as the #1 organic food provider in the nation, WFM will benefit from the growth and attention the industry is generating



WFM's margins have consistently been impressive and above their competitors'

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Attracting the Price-Conscious Shopper



COUPONS (USA)
Celebrate savings with \$60+ clickable, clippable coupons.
[Download coupons.](#)

50¢ off
any ONE (1) 8-oz 365 Everyday Value® Organic Peanut, Country Sliced, Tofu Tosses, or Mini Unsweetened Tosses.
U.S. Edition

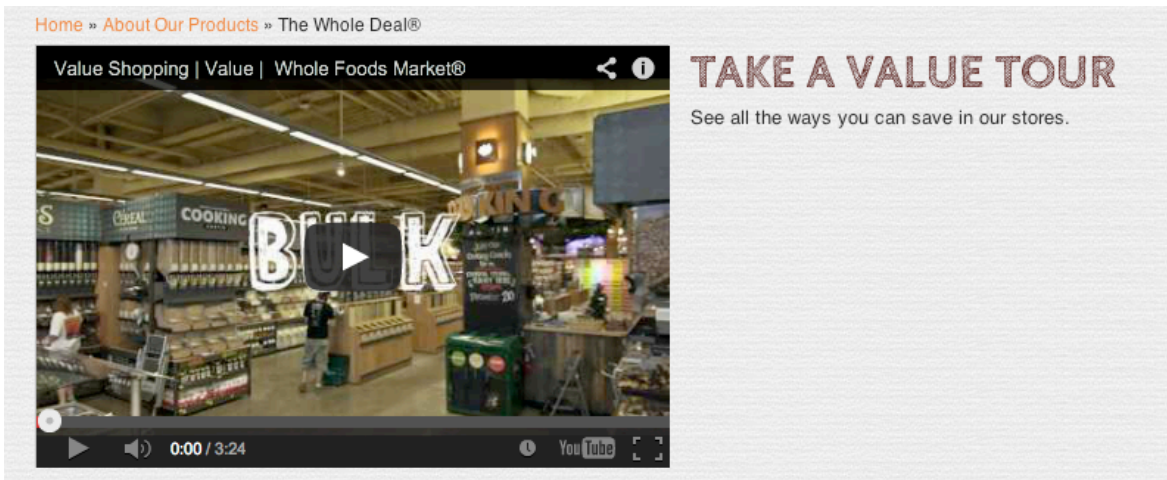
sure deal

SURE DEALS!
Spread loads of cheer with these Sure Deals.
[Discover everyday values with our Sure Deals.](#)

BUDGET-FRIENDLY RECIPES
Our 10 new budget appetizers will keep a jingle in your pocket.
[Get cooking.](#)



WFM is beginning to make moves in order to attract lower-income consumers. The pictures above to the left and below are shots from their website, where they have entire pages on how to save in stores through recipes and coupons, and even a video on how to properly “value shop”. The image above to the right is a sign from my local store advertising their 365 Value brand. Signs like these were all over the stores, pointing shoppers to the places where they could find deals.



Home » About Our Products » The Whole Deal®

Value Shopping | Value | Whole Foods Market®

TAKE A VALUE TOUR
See all the ways you can save in our stores.

0:00 / 3:24

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Creating the In-Store Experience like No Other



WFM Stores are not like other supermarkets—they aim to be more friendly and welcoming. The aisles are wider, the lighting doesn't hurt the eyes, there are plants everywhere and more is offered than just food. Taken in my local store, the pictures to the right and left showcase the variety of products sold in WFM stores. In addition to food, they also offer organic/fair trade clothes and organic body products.



The variety seen at any WFM is incredible. For any given product, even specialty products, they have a better variety than any other store, but at competitive prices.



WFM stresses the importance of understanding where their food comes from, and they do everything they can to provide their shoppers with as much information as possible about their products as seen in the middle picture. To the left, the buffet is seen where shoppers can have one meal or bring home a fresh-cooked, organic dinner for the week. On the right is a “Lifestyle Center” found in some stores. In this room, Whole Foods stores will host events for private parties where they teach guests to cook and they will host workshops for the public to teach them about healthy eating and cooking.

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