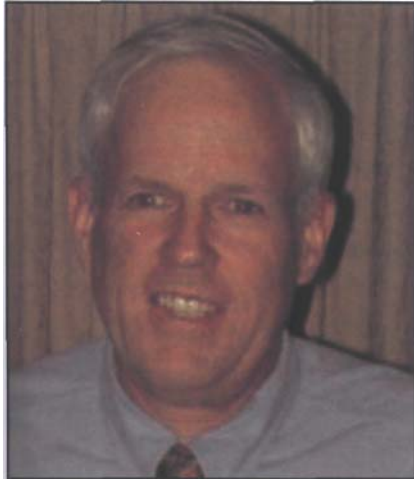


Keynote Address to California Avocado Society Annual Meeting 1999

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Introduction by: Mark Affleck

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When I think of an annual meeting I start by thinking about - why. Why come? What do you do when you are there? What are you looking for? What's the purpose? And invariably I come up at the end of that thought process with a couple of things: 1) to check in on "the today" - on the things that are happening right now in our world — the trends, techniques, tips, programs and the like, and 2) to check what is on the horizon for the future. I believe that any meeting can rally an industry to come together and say: "How am I doing?" And it only works if you challenge the things you are doing now with an eye on tomorrow. You know, when I think about that, it's really what I do for a living. You pay me to see the future. I don't get paid to respond to anything. If I'm responding, I'm gone, I'm late.

There is no such thing as "on time." There is early or late. And that means that the only way you can be early and the only way you can make moves that are transformative is to take a look at what is happening on the other side of

the hill. I mean, that is just the way it is. If you stop to extrapolate that, and build scenarios, you would say: "Well, Mexico is in now and will be in some more later. And what are the impacts of that? Where should we market our fruit? What should we do now in order to be successful down the road?"

So, we've had this run since 1988 of major success with the dollars. But it's still a

challenge. It always feels like you have one foot in the grave and one foot on the good side. It's an interesting way to manage, but I've only known that. I've only known managing in times of record revenue and near extinction. And when you think about it, and I've told others this, that when I say that I am glad about that, it is because every single minute of every single day of every month of every year we are forced to look ahead to see what is coming. But that's the easy part. Most people don't do it, but that's the easy part. So do that.

Here's the hard part. What do we do? What are the strategies? What needs to be done? What money needs to be spent? What needs to be changed? What needs to be challenged — even if it's painful, and that's the hard part. And so, luckily, fortunately for me, and I hope good for you, our board has come through and let me do those kinds of things.

One of the ways we do it is to take a scan of what is happening out there in the world and that's exactly what we are going to do now with the keynote speaker. I want to congratulate Bob Coleman, the Avocado Society Board, Carl Stucky, Peggy Mauk and others for thinking ahead like this and bringing in such a speaker. It demonstrates that you are thinking ahead, that you do want to know what is happening in the market place, that you do know that there will be major impacts and transformative change down the road.

And so, how do you look to the future? Well you start exploring. You start building scenarios. It is all driven by information and you have to open up your own insular wall and let the other light in. And that is what we are going to do today.

It is my pleasure to introduce Bob Reynolds as our keynote speaker today. We are very fortunate to have him with us. He is one of America's top strategic thinkers on fruit marketing. He has a wide range of experience across many different areas of business. He founded his consulting firm, "Reynolds and Associates," in 1987 and quickly became recognized as an expert in food and consumer marketing in the U.S. and Canada. Clients are spread across the food-marketing spectrum. Listen to this list: produce, meat, seafood, wine. It's like a picnic, right? Produce, meat, seafood, wine, sounds like a picnic to me. Grocery retail, government agencies and information technology — that's the breadth of experience he has.

Before forming his own firm, Bob was CEO of the Wine Growers of California, a top executive with Safeway and General Foods, and a chief strategist in the California attorney general's office. Before starting his career, he earned a Master of Science degree in agricultural economics from the University of California, Davis. Not a bad school! You can see that our keynote speaker today is uniquely qualified to paint a picture of the food marketplace of which our industry is a part. Bob will tell us about the future of the retail grocery business, consolidation, Internet shopping, technology, marketing, and much more. Listen carefully. I know you'll come away with a new and deep understanding of the changes and challenges erupting in the food market. Ladies and gentlemen, Bob Reynolds.

KEYNOTE ADDRESS

First of all, I know nothing about avocados except that I like to eat them.

I do know quite a bit about grocery stores and so I'm going to talk about grocery stores instead of avocados. I'm really not going to talk much about selling avocados in grocery stores; I'm going to talk about what is going on in the grocery store business and its natural extension, such as how you sell avocados.

What is this business that we call the retail business, the grocery retailing business? We have this core marketing challenge, and that is selling real products to real consumers. That is what I really love to think about doing. The whole marketing process is actually about getting something into the consumer's hands. In order to do this, in this business, we have to go through the retail process. We have to do a two-stage sell; one to sell to the retailer, and when we get that done, then we have to sell our produce to the consumer.

Now, I hope that you heard me clearly. It's that we have to sell our product to the consumer through marketing channels. The job gets started when we start selling to the retailer. So, it is not as if it is their job, it is our job.

Well, how do people shop? Let's just do a little quick turn around this whole grocery-marketing concept. First of all, how many in this group are regular retail grocery shoppers? You ought to be out there every week doing some real shopping because you learn a tremendous amount about the marketing process. Most shoppers are under time pressure. They are most often oriented toward the next meal. Forget this idea of shopping for the next month. Also, they would rather be doing something else. I hate to shop! They are looking for meals, not ingredients. If you are an ingredient seller, you've got a problem these days. Unless you are selling a solution to the meal problem, you have an uphill battle.

Most shoppers, not all, but most shoppers go to the store with a vague idea about what they want but they don't have a list. They make many of their decisions in the store. Many of their meal decisions are inspired by what they see in the store. Brand and size decisions are essentially all made in the store and many pre-trip decisions are changed once they get into the store. People buy much more than they ever plan to buy in the store when they get there — two or three times as much as what they intended to buy when they get there. Those extra buys are usually in response to promotions in the stores. Now, much of it is about how products look. In the produce department, what do we do? Remember, we pick the item up, we look at it, and we smell it. Few people realize how much the nose is involved in the produce department and the meat department. It doesn't happen when you are buying tires. In these peripheral departments, shoppers are exposed to thousands of great ideas. So they have lots of opportunity to buy other produce items along with yours. A third of what you buy in the food store is Tide, and cake flour, and batteries, and film, and all the other kinds of things. Those other products are a challenge for you because they are going after the same share of the consumer's wallet as your fruit.

There is a simple maxim in the grocery business called the "see-sell" imperative. You have to "see" it in order to be able to "sell" it, and if it looks good, people will buy it. If it

doesn't look good, they won't buy it. You can't buy it if it is not on display, and they won't ask for it because there are thousands of things out there that look good that they will buy — that they can buy.

The backstage people, the people that make decisions as to what goes on the shelves, are sometimes thought of as bean counters or order takers. This was partially true when information was less accessible. There was little sales data available back when I worked at Safeway, 16 or 17 years ago. When we wanted to find out how much Tide we had sold in all our operations, guess where we had to go find out? We had to go ask Proctor and Gamble. We didn't know which markets weren't doing well. The brand sellers like Proctor and Gamble, the people who controlled this product, were the people who had the data. They had the data and they ran the marketing programs. The retailer didn't spend a whole lot of time worrying about inventory and supply. The brand sellers controlled the information — they controlled the intellectual horsepower. Retailers executed the brand marketing programs that were generated by the brand marketing people. Retailers talked with each other about market shares, but their main concern was to build new stores to keep up with population growth and to execute marketing programs well. The whole idea was about growth. Well times are changing. They really are changing in the grocery business.

We're going to be talking about some of the ways that change is being driven. Here are some of the "change drivers;" that is, some of the things that are happening now, and some of the things that are going to happen in the future: 1) consolidation of retailers — consolidation is very big right now, 2) the explosion of information in the grocery business, and 3) the realization by retailers that their shelf space has value. They are "renting" shelf space, if you will, in order to get an additional return on their investment. 4) Productivity and efficiency are important. We will also look at 5) the elimination of needless costs, 6) new promotional businesses, and 7) the role of the power vendors. Regarding power vendors, you need to know who your competitors are for a share of the consumers' wallet, and I don't care if it is Tide or Gallo wine. One thing I do know about the avocado business is that avocados are not a staple food — it is a luxury product. You are competing for the extra dollars that are left over in the wallet once all the staples have been purchased.

Consolidation in the business has been a huge topic over the past 18 months, especially over the last year. I used to talk of the great "explosion" of consolidation. But really it is an "implosion" — a coming together of the grocery business into a lot fewer hands.

What are some of the big examples? The Kroger Corporation is now the biggest grocery retailer in the U.S. and is headquartered in Cincinnati. Remember, that is halfway across the country. The Kroger Corporation is now the proud parent of Fred Meyer, a retail group up north, as well as Ralphs here in this southern California market, Smiths in Salt Lake City and so forth. Then we have Albertsons taking over American Stores. American Stores is Luckys in this area. Then there was Safeway business here. Safeway, of course, is the parent of Vons in this market place. And the list goes on and on of mergers and pending mergers. It is big business and a lot of big bucks are involved. Lest you think that this is an American issue, the same thing is happening overseas, in Canada and elsewhere.

Let's take a look at one series of consolidations. About 1988 or so, a fellow named Ron Burkle, a finance specialist, acquired the Alpha Beta stores that were cast off in the Lucky merger with Alpha Beta. Mr. Burkle began his stake in the southern California market place with about 38 stores. Well, Ron Burkle is a name you are going to hear more about. Over the next several years he acquired more of these California grocers. A major acquisition in 1994 and 1995 was the Ralphs / Food for Less deal where a common ownership was engineered by — Ron Burkle. Alpha Beta disappeared at that time along with such venerable names as Boys and others. Then QFC acquired Hughes while Fred Meyer acquired Smiths. Ralphs acquired QFC/Hughes, with the Hughes name disappearing in southern California. Then Fred Meyer acquired Ralphs. The Deputy Chairman of the Executive Committee of Fred Meyer coming out of that deal was — Ron Burkle.

Finally, Kroger acquired Fred Meyer. We have all those name plates of super markets, all owned by Kroger, which is headquartered in Cincinnati. Guess where you have to go to get a major marketing campaign going with any of those name tags? You can't go down to Compton anymore to find out what goes on. The major decision-makers and the discussions concerning major marketing directions are going to be in Cincinnati at the Kroger Corporation.

Well, what is Kroger? They have about \$43 billion in sales in about 2200 supermarkets in 31 states. They have over 300,000 employees, give or take a few. And guess who is the Chairman of the Executive Committee — Ron Burkle. This is the fellow who acquired some Alpha Beta stores 12 years ago. It shows what somebody can do when they have the financial resources and business acumen.

Here is a result of all this consolidation. In 1987 the market share of the top ten U.S. grocers was 28.4%. In 1999 the Wall Street Journal said that the top ten grocers control 52.1% of the grocery business. That is a huge change. That is a doubling of the share of business controlled by the top ten players. What are some of the implications of that? Well, there are a lot bigger firms doing different things and controlling great big chunks of the business. There are a lot fewer alternatives for people like you in the avocado industry to sell to, so you can then sell to consumers down the line. Who are the top ten now?

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| 1) Kroger | 6) Ahold |
| 2) Albertsons | 7) Fleming |
| 3) Wal-Mart | 8) Winn-Dixie |
| 4) Safeway | 9) Delhaize |
| 5) Supervalu | 10) Publix |

Special mention needs to be made about someone that wasn't even in the grocery store business seven years ago — the Wal-Mart Supercenter. Has anybody seen a Wal-Mart Supercenter? If you want to know how groceries may be sold in the future in great portions of this country, look up a Wal-Mart Supercenter. You don't have any in California. You need to go to Texas, or Oklahoma, or Arkansas. The big Wal-Mart stores have added about one third more floor space to diversify their offerings.

There are alternative retail groups vying for consumers such as Internet commerce. The one we're going to talk about is Webvan dot com, a Bay area enterprise. It is the brainchild of Louis Borders who founded Borders Books. Their CEO is George Shaheen who came from Anderson. They have a 300,000 square foot automated warehouse in Oakland. They have a huge investment in this facility and they have talked about a one billion-dollar deal with Bechtel to build facilities in 26 U.S. markets. They have substantial venture capital behind them and are headed for a big IPO (initial public stock offering), even though their pre-opening losses amount to \$33.5 million. If their IPO goes as well as expected, they will be raising up to three hundred million dollars.

So let's go shopping on the Webvan dot com WebPages on the internet. Now where do you think we would find avocados? Can anyone guess? Is there anybody outside this room who really thinks an avocado is a fruit? Let's try salad fixings. They show two different kinds of avocados and they are both Hass. One is about to be ripe, and one is ripe. So they can be ripe in three or four days or ripe for tonight. Say we want some avocados and a few other things. After we have selected our grocery items we can specify a window of delivery — when do we want our order delivered? One of the things that Webvan dot com does is deliver within a half-hour window so you don't have to be around forever. This is the special difference between what they are doing and what anybody else has ever done with their delivery based shopping enterprise. After selecting the date and time of delivery, we then give them our credit card number and so forth. I have tried this grocery service and have had very good results and results that weren't so good. What is also special about this service is that they charge you absolutely nothing for delivery. I can't figure out how they do it but they charge you nothing for delivery.

There are other web shopping services that you might want to look at. The oldest is an outfit called Peapod. Homegrocer dot com is a new group under Amazon dot com. Another new company is Webhouse. It has not been launched yet, but is tied to Priceline. Priceline is the internet travel service where you offer what you want to pay for airline tickets and hotel rooms. I can't see how that would work in the grocery business, but that is their model. And then there are some captive systems tied to retailers. Albertsons has one although not live in this area. Schuncks in St. Louis has one, as does Hannaford in Boston and Raley's in the Sacramento area.

The interesting thing with dot com businesses is that nobody is making any money. They are losing money hand over fist with this process, but they are staking out new territory. Sales levels are not huge. The combined sales of Webvan dot com, for all the things they are doing in the Bay area is about three good grocery stores, maybe four. They are missing the impulse sale and last minute shopping for the next meal. You can't order it at 3 o'clock and get dinner ready at 6. It doesn't work that way. You have to be thinking further ahead than this evening's dinner.

Most of the traditional retailers are taking a defensive stand regarding e-commerce. They are looking into it, but they are not in it. They would much rather have people in their grocery stores pushing carts and buying all of the wonderful things on display.

The power of information is driving a great deal of change in the grocery business. Every time you go through the checkout, a huge amount of information is accumulated

about what you buy, when you bought it, and at what price. This is very, very valuable information that we didn't have at all 15-20 years ago. When coupled with things like the club cards of Vons and Ralphs, a database of very valuable information is built. This means that a whole new breed of decision-makers are now working at the management level at the grocery stores. There used to be a whole set of intuitive managers in the grocery business. I call them "old fudds" because they are the kind of guys who did their job real well, didn't have to think a lot about data analysis, and just wrote up orders. They are being replaced by bright young people who probably went to school while working in a grocery store — it's what we call the "retail scholarship." Nobody is giving any money away, but the flexible hours and all those kinds of things were perks that led them to have the grocery business in their blood. They also have the intellectual horsepower to go with it and a huge information resource in order to figure out what sells, where, and how quickly. It was different when I came into the business in 1970-71. You would hardly believe that you are in the same business. The transition has been away from the intuitive way of doing business. I know because I've lived in the business for 35 years. It is now based on the empirical. I can go look at the data, and I'm smart enough figure out what those data mean and I can put it into play.

Category management is the buzzword in business these days. We don't have buyers anymore in the grocery business, we have category managers. They are responsible for the profitability of the items assigned to their care. They are also responsible for determining how produce is arranged on the floor and other logistics involved in the whole category management process.

More importantly now, the retailers are recognizing a new value in this information, and they are making money by selling it down the street. So don't go ask a retailer to share some of that information for free because they want to sell that information for a profit. The organizations that have done a good job of developing their information are the firms that are on the acquisition side of the ledger. There was a firm up in Montana with a computer system that had horrible problems. Simply put, their computers weren't going to work and they were going to have to invest somewhere around 10 to 12 million dollars to get back to where they needed to be. Instead of doing that, they went shopping for a suitor. Albertsons acquired them so they were able to avoid the investment. So information technology is driving a lot of what is going on.

The control of information in the grocery business leads increasingly to the control of commerce. It is also very important these days to understand that producers need to have a lot more than great products. Great products are just the starting points for getting this grocery marketing process going. It is also necessary to have a program that sells the product to the customer who sells it to the consumer. You have to realize that the customer and the consumers are not the same people. Customers are the retailers like Safeway, Ralphs, and Albertson's. Your consumers are the people that are going to buy and eat your product. Your job is not done when the sale is made to the retailer. You are responsible for getting good information into the hands of the consumers, meeting the consumers in the store with product positioning and with increased advertising of one sort or another.

Power vendors have been leading the way for how groceries are now marketed. The people who are making the decisions on how produce is going to be sold are the people

who have been paying attention to the methods of the "power vendors." They have noted the kind of advertisements, promotions, allowances that all these kinds of products employ based on the data that has been gathered in the marketplace over the past 10 or 12 years. These power vendors buy a lot of services to support the programs to sell their products. These are people like Nabisco who stock every package of cookies and crackers with the Nabisco label on it that you see in the store. Power vendors are leaving the old style programs with incentive buys and dollars off per case for a set period of time. Now we have a shift to what are called "pay for performance" kinds of deals. The difference here is "pay for . . ." The money goes to the retailer for pushing products based on what gets sold to consumers. This is a far more useful method of inducing movement than the old "incentive to buy" methods.

So what does this mean to the growers of produce commodities? Produce is behind the curve. The science of selling has evolved from the experiences of the vendors that sell their products in the "center" of the grocery store. Produce information systems are sadly lacking, but that is changing. If you pick up an avocado in the market you will see a sticker with a PLU or price lookup code. This number identifies the produce item for the checker. They don't have to guess what kind of apple, or how big a bunch of carrots it is. This is a great stride over what had gone on before. Everybody else in the store has had UPC or universal product codes for some time. That's the bar code that identifies where it came from, who the seller was and all those kinds of things. UPC gave us a great deal more information. Very little has been known on item profitability in produce. Ask a produce seller how much money they are making in their department on avocados, oranges or apples and they don't know because they don't have the information. The produce business is simply going to have to adapt to the systems that have been developed by the grocery power vendors.

So what are some of the building blocks for a good marketing operation? In short, it's data. We need to analyze the data to know how to control when and where it is sold, where it came from and how to generate additional profitability. It is technical expertise. It is the ability for a commodity representative to walk into a produce operation and say: "If you do ABC&D, you'll make much more money in your produce department." And he or she can tell you why and show data leading to information, which lead to decisions that will generate more demand and profitability. It is vendor leadership. It's not enough to expect the retailer to know how to do the things that are good for marketing your product. The important thing is that the vendor is going to have to tell the produce retailers how the job gets done — to step in there and teach them how to use the tools. It is going to take a new breed of produce marketing people.

Here are some points in summation. People are obviously still shopping for groceries. You will see some Internet shopping in your area. There are going to be fewer and bigger firms doing all sorts of things to squeeze out profits. They will be searching for profits to pay down their debt as soon as possible. Marketers will need to be armed with tons of information. Those who have the ability to buy some of this information will be ahead of the curve. The programs that have been pioneered in the "center of the store" are going to be used to search out profit potential throughout the store. This should create beautiful produce operations that will have to produce proven profits.

Finally, here are bullet points that encapsulate the major trends of the grocery business:

- Bigger organizations — fewer headquarters
- Cash hungry — lots of new debt
- Less responsive — more layers
- New people — lots of testing — uncertainty
- Struggles for positions of influence
- New marketing programs
- New buying procedures
- Emphasis on Private Label
- Lots more management "by the numbers"

The Selling Function:

- Fewer places to sell — further away
- Fewer — but better people needed
- More technology — systems
- Relationships less important
- More direct selling
- Tougher for small brands — regional brands
- Uncertain broker role
- More in-store support required

As for the seller:

- Study
- Persistence
- Patience
- Programs
- Price
- People
- Service
- There is no "Magic Bullet"