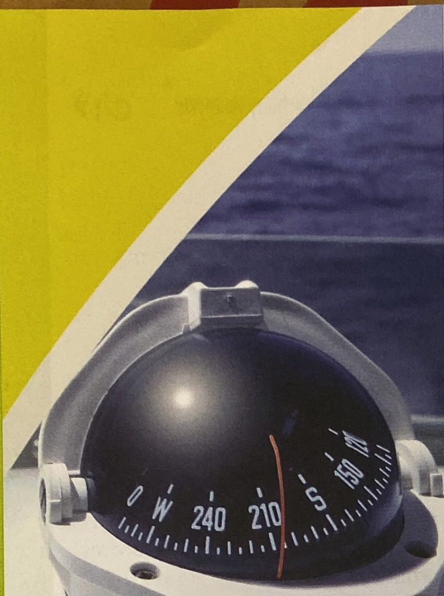
CASE 1

TRADER JOE'S IN 2018



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In the mid 1960's Joe Coulombe owned a chain of "Pronto Market" convenience stores in the greater Los Angeles area, but they were under heavy competitive pressure from 7–11. He began to ponder the idea of opening up a new kind of store—something with more unusual goods for people who had acquired more diverse tastes while traveling, and yearned for flavors they could not get at home. He went on vacation in the Caribbean and came home inspired: he opened up his first "Trader Joe's" (named after himself) in 1967. His store would focus on delivering innovative and hard-to-find foods with prices that would deliver great value. He also made a point of carrying every California wine available. He imbued his new store with a distinctive South Seas theme, by lining the walls with cedar planks, creating displays out of fishing nets, and having employees wear Hawaiian shirts.

The formula was a hit. By the late 1970s, there were twenty Trader Joe's in southern California, and by the late 1970s the chain had attracted the attention of the German Albrecht family, owners of a chain of discount supermarkets called Aldi Nord. In 1979, Theo Albrecht offered to buy Trader Joe's, keeping Joe on to run the business. Coulombe accepted; the Albrecht purchase enabled Trader Joe's to expand more rapidly than it could have otherwise, and Coulombe stayed on to run the company until 1987. He then retired and was succeeded by his friend, John Shields, who expanded the company into Arizona, the Pacific Northwest, and Brookline and Cambridge (near Boston). When Shields retired in 2001, Dan Bane succeeded him, and continued to expand the chain. By October 2017, the company had 473 stores in 43 states, more than 38,000 employees, and an estimated $13 billion in annual sales.

C1-1 A DISTINCTIVE PRODUCT STRATEGY

From the beginning Trader Joe's had a distinctive product strategy. Whereas a typical grocery store might carry 50,000 different items, Trader Joe's carried closer to 4,000, and most products (roughly 80%) bore one of Trader Joe's own brand names (see Figure 1). Many of the names are a fun twist on the name Trader Joe but modified to reflect the nature of the food, such as "Trader Jose's" (for Mexican food), "Trader Mings" (for Asian food), and "Pilgrim Joe" (for New England favorites such as clam chowder). The company focused on gourmet and organic foods, vegetarian offerings, and imported foods, as well as wines and interesting frozen entrees.

Figure 1 Examples of Trader Joe's Branded Items

Trader Joe's is very selective about the products it stocks. Trader Joe's biggest R&D expense is for its top buyers to travel the world looking for new trend-setting items, such as the wildly successful Trader Joe's cookie butter, which is a gooey Belgian spread known as "Speculoos" in its home country. The company does not charge slotting fees to suppliers to get on the shelves—instead it makes them compete to demonstrate they can sell in high enough volumes, and at low enough prices, to keep their spots. Trader Joe's routinely discontinues products that fail to deliver on these dimensions, cutting the 10% worst performers to make room for new items. Customers do not seem to mind the narrower selection—in fact, analysts speculated that customers actually felt *better* about their choices when there were fewer options. Trader Joe's had cultivated a reputation of choosing products very carefully, which in turn, inspired customer faith in the company's offerings. As articulated by a former employee, "If they're going to get behind only one jar of Greek olives, then they're sure as heck going to make sure it's the most fabulous jar of Greek olives they can find for the price."

Trader Joe's also took a fairly strict stance on issues pertaining to the environment, humane practices, and food safety. For example, products sold under the Trader Joe's brand name could not contain artificial colors, flavors, preservatives, or genetically modified ingredients; Trader Joe's eggs could only come from cage-free hens; and Trader Joe's dairy products had to come from cows that were not given artificial hormones. It also announced in 2007 that it would discontinue stocking most products from China due to concerns about inadequate monitoring of food safety.

The carefully curated product line turned out to have big economic advantages: Selling a narrower selection of high-volume products helped to drive down supply costs because each item was bought in higher volumes, enabling Trader Joe's to negotiate deep discounts. At the same time, managing a narrower product line lowered inventory carrying costs, and stocking only items that turned quickly boosted sales per square foot. Trader Joe's stores sell roughly $1,750 per square foot—more than double that of Whole Foods. As a result, many analysts speculated that Trader Joe's was significantly more profitable than a typical grocery retailer (actual profits were unknown as Trader Joe's was a privately held company and did not share its income figures).

C1-2 LOGISTICS AND MARKETING

Most Trader Joe's store locations were leased, and about two-thirds operated out of existing buildings rather than being newly built. The stores ranged from 8,000–15,000 square feet, and were typically opened in non-prime locations (though its Manhattan stores were notable exceptions). From its inception, Coulombe recognized that the stores would fare better in communities that had adventurous and educated people, and thus he targeted college towns and other educated communities.

Rather than working with national or regional distributors, Trader Joe's purchased directly from the manufacturers, which then shipped their products straight to Trader Joe's distribution centers. This process streamlined the distribution process and reduced costs, but also limited where, and how fast, Trader Joe's was able to expand. For example, it took Trader Joe's longer to enter states like Texas or Florida (despite entreaties from customers in those locations who had become familiar with Trader Joe's stores) because they were not easily accessible to its distribution centers.

Trader Joe's spends very little on advertising, instead relying on regional radio advertising, word of mouth, and its newsletter, the "Fearless Flyer." The newsletter is customized by region and offers detailed and witty write-ups of new products that emphasize their authenticity and uniqueness.

C1-3 UNIQUELY FRIENDLY EMPLOYEES

A big part of Trader Joe's strategy and brand image is the friendliness of the experience in the stores. Employees are encouraged to interact with customers, getting to know the names of regulars, and generating a fun and informal vibe. Instead of a PA system, for example, Trader Joe's uses bells where one ding means another register should be opened, two dings means there's a question that needs answering, and three dings means a manager's assistance is needed. Store employees can work in any function in the store, and all are expected to be knowledgeable about the products and be able to make recommendations. If a customer asks a Trader Joe employee about a product, the employee will typically enthusiastically share their own experience with the product, will often accompany the customer to the location where the product is shelved, and may open a package to offer the customer a sample.

Management at Trader Joe's believed that a big part of why people shop in stores is not about the food at all—it's about interacting with people, sharing a smile or a joke, and feeling welcomed. For this reason, Trader Joe's did not offer online ordering, nor did management feel particularly threatened by the growth of online grocery shopping. The Trader Joe's experience was distinctive enough, and fun enough, management believed, that online shopping was not direct competition. However, creating this fun and friendly vibe in the stores had become a growing challenge as the chain grew: how would Trader Joe's ensure that its distinctive store culture of friendly interaction would be retained when stores and employees were being added to the chain quickly? Protecting and reinforcing this culture was a challenge that Trader Joe's management took seriously.

One of the ways Trader Joe's attempted to preserve the employee culture was through its pay policies. When Joe Coulombe founded Trader Joe's, he decided to pay full-time employees the median California family income rather than the much lower salaries typically offered to workers at convenience and grocery stores. Today, store managers and full-time crew members at Trader Joe's are still paid better than typical store employees. According to Glassdoor, a company that gathers pay and benefits information from employees at over 300,000 companies, hourly store employees at Trader Joe's earned an average of $13/hour in 2017, and store managers earned between $52K and $106K. Trader Joe's also contributes 15.4% of employees' gross income to tax-deferred retirement accounts.

C1-4 COMPETITION

The traditional grocery retail industry was mature and had very slim margins. Firms relied on rapid turnover and tight cost control, while also selling premium items such as made-to-order sandwiches, imported cheeses and cut flowers to bolster earnings. Even strongly differentiated grocers like Whole Foods had slim margins (see table below), and industry leaders like Kroger and Albertson's had net margins of 1.55% and 4.00% respectively. This meant there was little room for waste or error in the grocery industry.

Though Trader Joe's has a strong focus on value and many customers were attracted to its stores for its low prices, its emphasis on gourmet and healthy foods caused many people to view the store as being more like Whole Foods than a discounter grocer like Costco or Wal-Mart. Being a lower-cost Whole Foods was a valuable and unique niche position. However, there was growing risk that this particular niche would become more crowded as new alternative grocers emerged. For example, one such competitor was Sprouts Farmers Market. In 2018, Sprouts Farmers Market's 280 stores were primarily located in

Table 1 Revenues and Net Profit Margin at Select US Grocery Retailers, 2017

Grocery Retailer	Gross Revenues ($millions)	Net Profit Margin
Kroger	122,662	1.55%
Albertsons	59,924	4.00%
Publix	34,837	6.58%
H-E-B	23,939	–
Safeway	22,934	–
Whole Foods	16,030	2.85%
Trader Joe's	13,300*	
Wegmans	8,720	–

*Data gathered from Hoovers and 10-K reports. Sales for Trader Joe's are estimated by Supermarket News, accessed October 2, 2018.

the Southwestern states of the United States, but the chain was growing fast. Its business model focused heavily on fresh produce, sold at 20–30% discounts to conventional competitors. Its low cost strategy was simple: whereas conventional grocery stores piled produce high in aesthetically attractive visual displays that connoted abundance, Sprout Farmers Market used smaller "low displays." These displays resulted in far less waste than the nearly 15% of produce that is typically wasted in a grocery store.

Amazon's $13.4 billion acquisition of Whole Foods also presented a further new threat: in addition to providing the convenience of Whole Foods groceries delivered to consumers' doors, Amazon also promised to slash prices on staples like eggs, milk, fruit, beef, and pasta. On many items Whole Foods prices matched, or occasionally even beat those of Trader Joe's. One research study reported that in the first week after the Amazon takeover, Whole Foods gained nearly ten percent of Trader Joe's customers, suggesting serious cause for concern for Trader Joe's management. Whole Foods also had plans to expand its chain of "365 by Whole Foods" stores, which were smaller, stripped-down versions of Whole Foods that would use auto-replenishing technology and order kiosks to reduce labor costs.

C1-5 REMARKABLY SUCCESSFUL, FAMOUSLY SECRETIVE

In 2017, a survey conducted by Market Force Information found that Trader Joe's was ranked as America's third favorite supermarket chain, behind Publix and Wegmans. Perhaps not coincidentally, this was just two spots ahead of Aldi, its lesser known parent. Both chains were praised for their courteous and fast service, and their high quality private-label lines. Trader Joe's success could also be observed in the growth in the number of its stores and its estimated revenues. It was unknown, however, just how much the company earned on those revenues. Was Trader Joe's profitable?

Trader Joe's had always been privately held and famously secretive. It did not reveal its sourcing, and made suppliers sign contracts forbidding them to publicize their relationship with Trader Joe's. There were no signs with the company's name or logo at the Monrovia California headquarters, and management routinely denied requests for interviews from magazines and newspapers. Such secrecy made it hard for competitors to know either what kinds of profits Trader Joe's earned or how it generated those profits. Such secrecy also facilitated suppliers' ability to sell products for a lower cost to Trader Joe's without alienating their other retailers.

Remaining privately held, however, also came at a price. By not franchising or accessing capital through the stock market, Trader Joe's forfeited opportunities to grow faster. Some analysts expressed concern that this left a lot of opportunity for competitors to imitate Trader Joe's business model and product strategy and seize geographic regions that Trader Joe's had left unserved. This left many wondering: How much more profitable was Trader Joe's than other grocery retailers? Should the company be growing faster? And if it did, how could it ensure that its company culture and store culture were preserved?

Sources: www.traderjoes.com; Kowitt, B. 2010. Inside Trader Joe's. ***Fortune***, 162(4):86–96; E. Z. 2014. Trader Joe's doubles its growth rate. ***SN: Supermarket News***, 62(9):24–26; Anonymous, 2014. America's favorite super: Trader Joe's. ***MMR***, 31(9):87. Gustafson, M. 2008. Trader Joe's remarkable journey. ***Private Label Buyer, November 1st, pp 42–46;*** Nisen, M. 2014. The secret to America's most "disruptive" supermarket—fruits and vegetables. ***Reuters***, June 30th; Frias, C, Herring, C, & Reyes, A. 2017. Here's how Whole Foods' new, cheaper prices compare to Publix and Trader Joe's. ***Miami Herald***, August 30th; Clough, B. 2018. 10 quirky things to know about Trader Joe's. ***Fresno Bee***, February 14th; Fickenscher, L. 2017. Whole Foods eats Trader Joe's lunch. ***New York Post***, Octiber 3rd; Dodson, C. 2017. The grocery wars take off. Fast Company, October 1st; Hoovers, 2018; Yahoo Finance 2018.