

Jan DeLyser  
Vice President, Marketing  
California Avocado Commission

## **Avocado Pricing at Retail**

Few topics generate more heated debate amongst growers, suppliers, and retailers than retail produce pricing. Some believe the relationship between the grower and the buyer is the same regardless of the economy, but current conditions add fuel to the debate about the spread between farm gate price and the price at retail. The past 12 months have dealt a heavy blow to the production side of agriculture with unprecedented increases in input costs and uncertain availability of water. Conversely, retailers also face rising operating costs and are challenged to differentiate themselves with consumers in an exceptionally competitive marketplace.

Bruce Peterson, former head of Wal-Mart perishables, alluded to the many misconceptions concerning retail pricing in his presentation, *The Short Course on Produce Marketing*, given at the University of California, Davis in April, 2009. He said some producers think there should be a one-to-one correlation between the FOB cost and the retail price. He cautioned that each retailer has their own strategy when it comes to enticing consumers into the store, and he emphasized the importance of marketers and producers understanding the objectives and unique challenges that retailers face.

### **California Avocado Commission**

The California Avocado Commission (CAC) is an organization that is focused on creating demand for California avocados while

generating value throughout the marketing channel from grower to consumer. CAC often finds itself in the role of moderator of this debate. CAC works for the California avocado grower, and with the sellers and the buyers, to entice consumers to purchase California avocados in season. Each link in the marketing chain relies on the next for long-term viability. A detailed look into retail pricing structure follows and provides insight into those strategies.

### **The Target Consumer**

Traditionally, CAC has defined avocado consumers as light users (up to 12 avocados per year), medium users (between 13 and 36 avocados per year) and heavy users (37 or more avocados per year). During the 2008 season, the “Super Avocado User” was identified as the consumer purchasing more than 120 avocados per year. The super user tends to be more male, more affluent, younger and more ethnically diverse than the traditional target consumer of women age 25-54, by 40 percent. By expanding the consumer target, CAC sharpened its focus on consumers who entertain at home and cook for fun. This change proved timely with the economic down turn. According to the 2008 Avocado Tracking Study by Cooper Roberts Research, the super user group tends to be eco-conscious, scoffs at traditional gender roles, has a thirst for knowledge of new cultures, takes pride in buying American, and prefers fresh foods rather than canned and frozen foods. Also, this consumer has an appreciation for the “Hand Grown in California Avocados” marketing theme with key attribute ratings for demonstrating premium quality, better taste, fresher products, food safety, environmental responsibility, and fair labor practices.

### **California Avocados at Retail**

The produce department continues to be a growth area for retailers. This is in contrast to the long-term decline in profitability for the general grocery items found in the center of the stores. The produce department provides unique opportunities for retail differentiation. The “freshness” of the produce department is often used to help establish a distinct brand position for a supermarket chain of stores.

Avocados are a very productive category in the retail produce

section. They are versatile and provide opportunities for secondary displays. Produce departments may feature bulk displays of large and small avocados, bagged avocados, or seasonal varieties such as Lamb Hass, Pinkertons, Reeds, or other varieties. Because of their versatility, avocados rank high as an ingredient in recipes, generating valuable incremental sales of other produce items and non-produce items such as tortilla or corn chips. These unique qualities, combined with their strong growth in sales, position avocados as a high-profile item at retail, particularly with produce personnel.

### **Increased Shopping Basket Potential Grabs Retail Attention**

The purchase of avocados by consumers often leads to the purchase of other complementary food items. This increases the average cash register ring of avocado purchasers at retail. Information from A.C. Nielsen Homescan 2007, indicates a 69 % increase in consumer spending at retail when avocados are in the shopping basket. The Homescan research states that a typical shopping basket with avocados will average \$66 per trip while one without is \$39. Additionally, avocados continue to increase in sales and productivity in 2009, one of only a handful of produce categories to do so.

**Avocado users spend more money per grocery visit**

- There is an increased spend of 69% when avocados are in the shopping basket
- Average consumer spend per grocery trip
  - Shopping basket with avocados: \$66
  - Shopping basket without avocados: \$39

Source: A.C. Nielsen Homescan 2007

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### **Avocado Retail Promotion**

The definition of retail promotion has a number of meanings and depends on several factors. Frequently, feature ads are used as a measure of promotional activity. Feature ads are useful tools, particularly when large volumes of avocados need to be moved in a timely manner and foster a strategy of a steady pull through the produce market that keeps momentum active. CAC's retail research shows that a well-constructed strategy of feature ads will generate increased sales. CAC's retail data program provides an invaluable opportunity for CAC's merchandisers to communicate to retailers specific performance information at market level, compare their experience with that of competitors, and highlight the retailer's prior performance. It is not CAC's practice to provide specific pricing recommendations to retailers. However, the business review process leads the way to strategic discussions resulting in fact-based decisions regarding timely promotion to insure a strong pull strategy (marketing and sales working together to create demand that pulls the product through the marketing channels) for California avocados versus a push strategy (a result of supply exceeding demand and requires pushing out the product at discounted prices to keep inventories in check).

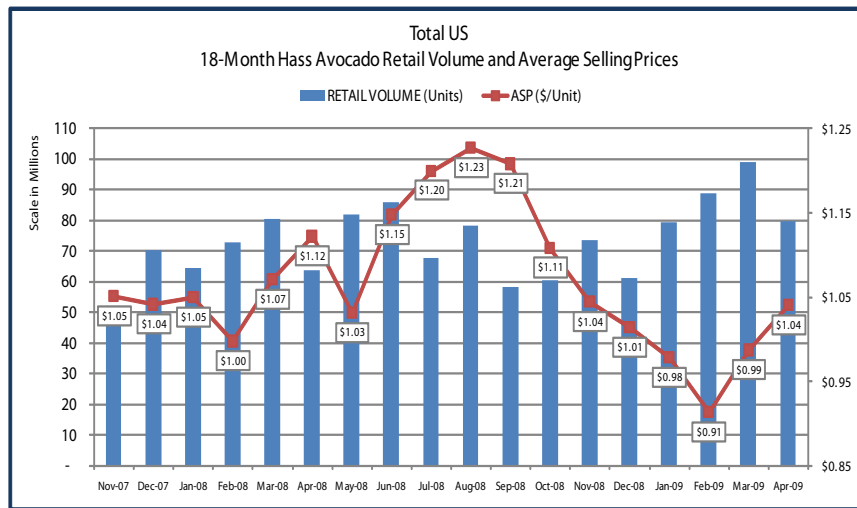
Maintaining well-stocked, prominent locations in the produce department with in-store promotions is a key measure of promotional success in lighter crop volume years. CAC's programs work hard to generate awareness of California Avocados to create demand and a strong consumer "call-to-action" for purchase in season through radio advertising, in-store activity such as in-store radio broadcast, point-of-sale signage, themed bin displays, grocery cart ads, magazine print ads targeted to our heavy/super user demographic, and fitness center ads. The power of the integrated marketing campaign generates retail promotional confidence. In a short crop year, it's important to demonstrate the value of promotional impact based on availability. A feature ad or in-store promotion at \$1.69 has perceived value to the consumer when the everyday price is \$1.99 or higher.

The information above sets the stage for why avocados have the attention of retailers. What follows is a survey of the factors that influence retail produce pricing.

## Margins

Retailers work with two margins: the margin of an item going into the store called Initial Mark Up (IMU) and Gross Margin (GM). We'll focus on Gross Margin.

GM is figured differently in various companies. It is based on total department sales figures for a calendar month, or a 28-day period. GM is generally the gauge used to evaluate the performance of retail produce managers.



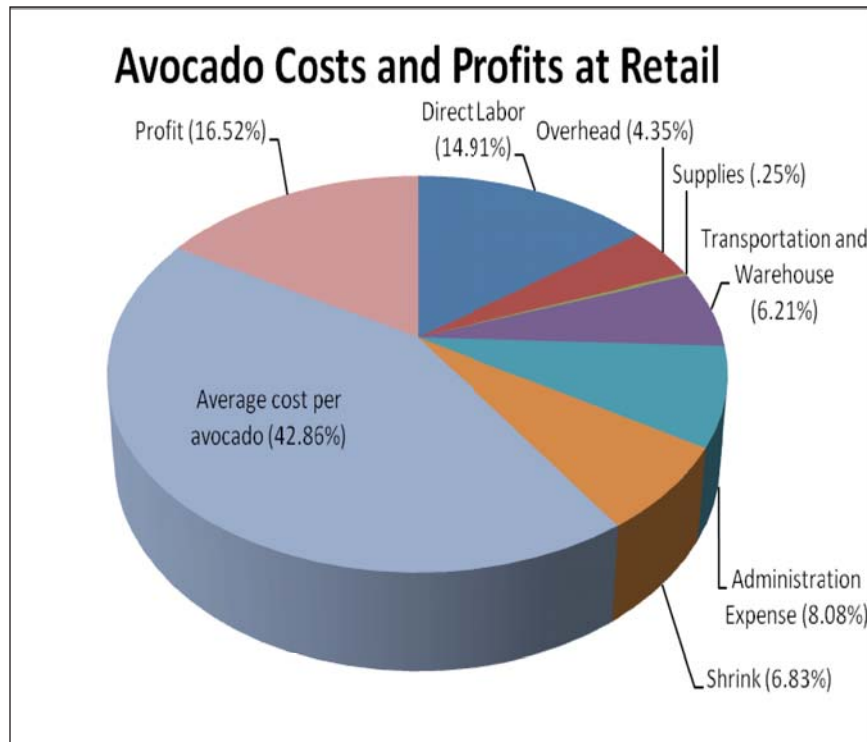
### A Hypothetical Gross Margin

- Retail Sales \$100,000
- Cost of goods delivered to the distribution center (DC) \$ 46,000
- Initial Markup (IMU) \$ 54,000
  - The Cost of warehouse, receiving, put away selection, and transportation to the stores is usually around 112% of cost of the produce item. In this case, the cost could be 10% or \$ 4,600
    - IMU after warehouse and transportation \$ 49,600
  - Shrink is the value of the product that is not saleable. This varies from retailer to retailer. The Produce Marketing Association reports it to be between 6-7% of retail sales. We will use 7% or \$7,000
    - GM dollars after shrink and warehouse costs is \$42,600
    - GM percentage after shrink and warehouse costs is 42.6% of total costs
  - Direct labor generally ranges from 10-12% of total costs

- Fringe benefits generally range from 5% to 8% of total costs
- Supplies generally range from 1% to 3% of total costs
- Direct labor, fringe benefits, and supplies are deducted from GM on the chain's Produce Contribution Report reducing the profit to between \$26,400 –\$20,400 or 26.4% – 20.4%

**An Actual Retail Example**

2008 Average Retail Price: \$1.61



**Costs:**

Direct Labor	\$ .24 (14.91%)
Overhead (personnel, store mgrs, porters)	\$ .07 (4.35%)
Supplies (bags, stickers, etc.)	\$ .004 (0.25%)
Transportation/Warehouse	\$ .10 (6.21%)
Administration Expense	\$ .13 (8.08%)
Shrink	\$ .11 (6.83%)
Average cost per avocado	\$ .69 (42.86%)

Profit: \$ .266 = 16.52%

### **Concluding Thoughts**

The debate regarding retail pricing will undoubtedly continue, and there will be times when the point-of-purchase pricing will be out of sync with the farm gate value. The great news for the avocado industry is that the “California Avocado Grower” marketing campaign, combined with strategic promotions, continues to positively impact avocado movement in the produce market during the California avocado season. Additionally, the referential consumer price point in season remains over \$1.00. And, that bodes well given the continued increase in demand, even in difficult economic times. Retailers have embraced the avocado category for the value it represents, not only in avocado category sales, but with the dollars it generates in complementary sales.