

## **Introduction**

### **Company Goals**

With the idea of opening a supermarket that exclusively serves natural foods, Whole Foods Market (WFM) envisioned many goals for its community. WFM's main goal is to offer products that are environmentally sustainable in the long run (WFM, 2013). The firm believes everyone should take responsibility to contribute to the sustainability of earth in order to provide an inhabitable place for generations to come. Thus, WFM has continued to seek innovative ways to further sustainable living through strict procedures in product selection and its strong advocacy of organic and local farmers (WFM, 2013). Sustainable eating is further emphasized through healthy eating regiments on the company's website informing customers of the benefits of healthy eating for themselves as well as the environment. Although WFM's public ownership requires the firm to maintain a traditional corporate structure focused on growth in terms of wealth and profits, it differentiates itself in terms of wealth distribution. In alignment with WFM's goals to "give back" to communities, a minimum of 5% of annual profits are distributed to numerous communities and non-profit organizations regularly (WFM, 2013).

### **Brief History**

WFM, once a small natural foods supermarket, has now become an international leader in the natural foods industry. The firm began its operations in 1980 in Austin, Texas with 19 employees. In the 1990s, driven by its success, WFM acquired numerous natural foods supermarkets. Acquisitions such as Wellspring Grocery of North Carolina, Bread & Circus of Massachusetts and Rhode Island, Mrs. Gooch's Natural Foods Market of LA, Bread of Life of Northern California and others contributed to the expansion of WFM all across the US. Along with a successful initial public offering in 1992, WFM expanded into Canada in 2002 and the UK in 2007 (WFM, 2013). As of 2012, WFM had 73,000 members, 335 store locations with 322 in US, 7 in Canada, and 6 in UK, and \$12 billion in net sales (WFM, 2013).

## **Current Situation**

### **Products**

WFM is a supermarket chain that prides itself on providing the highest quality of natural and organic products. As a result, WFM products are “minimally processed, largely or completely free of artificial ingredients, preservatives and other non-naturally occurring chemicals” (WFM, 2013, p.12). Suppliers are required to be third party certified or rated on sustainability to meet WFM’s expectations. For example, in early March, WFM publicly announced that all its suppliers must clearly label products that contain genetically modified organisms (GMOs) by 2018 or begin sourcing non-GMOs (Robb & Gallo, 2013). Such initiatives and criteria demonstrate WFM’s dedication to its promises through transparency.

### **Market Share**

The grocery retailer market in North America is highly fragmented. In the last five years, WFM’s market share in North America has increased from 0.8% in 2009 to 1.1% in 2012 (Euromonitor International, 2013). Currently, the industry’s leader Walmart has a significant lead at 23.2%, while Kroger and Safeway, the industry’s second and third, respectively, hold only 6.7% and 3.4% (Euromonitor International, 2013). This indicates the importance of price in attracting and maintaining consumers in the grocery industry.

### **Financial Performance**

Annual financial data in the recent years indicate a strong financial growth for WFM. Assets have grown, while long-term debt was decreased to \$24M in 2012 from \$929M in 2008. Average weekly sales per store grew by almost 20% since 2008, despite the emergence of 60 new stores within the same period. Operating margin has also increase from 3.0% in 2008 to 6.4% in 2012, signaling increased efficiency and economies of scale. The financial strength of WFM’s is further reflected on earnings per share, which has grown by almost 68% within the past five years.

**Table 1: Whole Foods Market, Inc. Summary Financial Information**

	Sept. 30, 2012	Sept. 25, 2011	Sept. 26, 2010	Sept. 27, 2009	Sept. 28, 2008
<b>Consolidated Statements of Operations Data <sup>(1)</sup></b>					
Sales	\$ 11,698,828	\$ 10,107,787	\$ 9,005,794	\$ 8,031,620	\$ 7,953,912
Cost of goods sold and occupancy costs	7,543,054	6,571,238	5,869,519	5,276,493	5,246,468
Gross profit	4,155,774	3,536,549	3,136,275	2,755,127	2,707,444
Direct store expenses	2,983,419	2,628,811	2,376,590	2,146,626	2,108,679
General and administrative expenses	372,065	310,920	272,449	243,749	270,428
Pre-opening expenses	46,899	40,852	38,044	49,218	55,554
Relocation, store closure and lease termination costs	9,885	8,346	11,217	31,185	36,545
Operating income	743,506	547,620	437,975	284,349	236,238
Interest expense	(354)	(3,882)	(33,048)	(36,856)	(36,416)
Investment and other income	8,892	7,974	6,854	3,449	6,697
Income before income taxes	752,044	551,712	411,781	250,942	206,519
Provision for income taxes	286,471	209,100	165,948	104,138	91,995
Net income	465,573	342,612	245,833	146,804	114,524
Preferred stock dividends	—	—	5,478	28,050	—
Income available to common shareholders	\$ 465,573	\$ 342,612	\$ 240,355	\$ 118,754	\$ 114,524
Basic earnings per share	\$ 2.55	\$ 1.96	\$ 1.45	\$ 0.85	\$ 0.82
Weighted average shares outstanding	182,401	175,221	166,244	140,414	139,886
Diluted earnings per share	\$ 2.52	\$ 1.93	\$ 1.43	\$ 0.85	\$ 0.82
Weighted average shares outstanding, diluted basis	184,444	177,279	171,710	140,414	140,011
Dividends declared per common share	\$ 0.56	\$ 0.40	\$ —	\$ —	\$ 0.60
<b>Consolidated Balance Sheets Data</b>					
Net working capital	\$ 1,125,443	\$ 573,783	\$ 413,647	\$ 371,356	\$ (43,571)
Total assets	5,294,216	4,292,075	3,986,540	3,783,388	3,380,736
Long-term debt (including current maturities)	24,122	17,905	508,698	739,237	929,170
Shareholders' equity	3,802,469	2,991,305	2,373,258	1,627,876	1,506,024
<b>Operating Data</b>					
Number of stores at end of fiscal year	335	311	299	284	275
Average store size (gross square footage)	38,000	38,000	38,000	37,000	36,000
Average weekly sales per store	\$ 682,000	\$ 636,000	\$ 588,000	\$ 549,000	\$ 570,000
Comparable store sales increase <sup>(2)</sup>	8.7%	8.5%	7.1%	-3.1%	4.9%
Identical store sales increase <sup>(2)</sup>	8.4%	8.4%	6.5%	-4.3%	3.6%

<sup>(1)</sup> Fiscal year 2012 was a 53-week year and fiscal years 2011, 2010, 2009 and 2008 were 52-week years.

<sup>(2)</sup> Sales of a store are deemed to be comparable commencing in the fifty-third full week after the store was opened or acquired. Identical store sales exclude sales from relocated stores and remodeled stores with expansions of square footage greater than 20% from the comparable calculation. Stores closed for eight or more days are excluded from the comparable and identical store base in the first fiscal week of closure until re-opened for a full fiscal week.

Note. Adapted from "2012 Annual Report," by Whole Foods Market, 2013, *Annual Stakeholder's Report 2012*, p.29. Copyright 2013 by the Whole Foods Market.

## **Current Strategy**

### **Expansion**

Domestically, WFM has expanded through the acquisition of rival companies since the 1990s. Recently, the company acquired Wild Oats Markets in 2007 for \$700 million, which was financed through a five year term loan agreement (WFM, 2013). WFM is one of the largest public food and drug retailers in the US with a total of 335 stores in US, Canada, and UK. In 2012, WFM opened a record number of 25 stores with 79 stores in development (WFM, 2013). Furthermore, 45 new leases were signed to continue this steady growth strategy in hopes of achieving 1,000 stores in the US in the future (WFM, 2013).

### **Differentiation Strategy**

WFM is a food retailer differentiated through a broad product selection of high-quality natural and organic products (WFM, 2013). Differentiation strategy is "an integrated set of actions taken to produce goods or services (at an acceptable cost) that customers perceive as being different in ways that are important to them"(Hitt et al, 2009, p.148). In order to keep a broad base of loyal customers, the company differentiates itself with sustainable natural products and high dedication to surrounding communities unlike any other in the grocery industry (WFM, 2013).

### **Transnational Strategy**

WFM has adopted a transnational strategy to pursue international expansion in Canada and UK. Transnational strategy focuses on putting the same weighted priority on local and international markets to optimize flexibility and balance. WFM entered the Canadian and British market through wholly owned subsidiaries (WFM, 2013). Despite the high capital investment of such method, it allows WFM to control the quality of its products to ensure consistency in its brand image internationally. Aside from the expectation of high quality products, WFM's local managers are given autonomy in regards to supporting and engaging their respective local communities to be in alignment with WFM's focus on "giving back" to its local communities.

## Environment

The grocery industry, in general, is characterized by intense rivalry and a high threat of substitution, forcing firms in the industry to find ways to differentiate their brand and product offerings. The recent consumer push for health and environment conscious product offerings has allowed companies like WFM to differentiate itself based on this sociocultural dimension. On the other hand, in recent years, there has also been a large push for convenience from consumers who prefer to purchase all retail items from one store (Euromonitor, 2012). This provides a difficult challenge for grocers like WFM because they are forced to compete with large chains like Walmart, who can and do provide a wider array of products.

As a company, WFM's reputation for quality is among the top in the industry, drawing heavily on local suppliers to strengthen the value of their supply chain. In turn this creates value for their target customers, who tend to have a higher willingness to pay more for quality products, based on their mid to upper class income bracket (Whole Foods Market, 2013). Its higher prices do, however, provide an interesting opportunity for competitors. The supermarket chain, Trader Joes, provides similar product offerings to WFM, but it is priced significantly lower and often operates in the same market, representing a potential threat for WFM's growth (Datamonitor, 2008).

On a larger scale, WFM must be cognizant of the potential problems they may face as a higher cost retailer amidst economic uncertainty. Despite the optimistic outlook of the American economy it remains volatile due to the fragility of many EU nations (Valetkevitch, 2013). During economic uncertainty, consumers tend to move to low cost retailers, drawing crucial business away from companies like WFM (Hitt, et al., 2009). The grocer must also remain cognizant of government regulations surrounding the qualification of nature and organic products, which may positively or negatively affect WFM. Finally, it is pertinent for WFM to pay particular attention to opportunities for global expansion as certain international markets begin to push for healthier and more organic food options.

## **Strategic Challenges**

### **Heavy Saturation in the US Market**

Currently WFM receives 96.8% of its sales solely from the US market with its 322 stores.

Although WFM has continued to observe growth in net income in the recent years, this high dependence on only one market may hinder the companies' growth. For example WFM's growth in 2009 during the economic recession in the US was negative. Failure to diversify across different markets will expose WFM to the volatility of the American economy.

### **Further International Expansion**

In terms of further global expansion, location is the most important factor for WFM to consider. Different countries have different culture, preferences and tastes. Despite the success of wholly owned subsidiaries in Canada and UK, WFM may have to adjust its strategy to enter new markets. In addition, regulatory standards regarding natural and organic foods along with the prospective country's taxes, tariffs and exchange rates will have to be considered. Furthermore, increasing brand awareness in prospective countries may require large initial marketing expenditure and time.

### **Intensive Competition**

The grocery retailer industry is highly fragmented among local, national, and international players operating as natural food stores, online retailers, and etc. The competition in the market is quite intensive with lower cost competitors in comparison to WFM. Walmart, the market leader has established economies of scale and advantageous relationships with its suppliers allowing it to dramatically lower its prices unbeatable by any competitor. Furthermore, Trader Joe's has emerged as a more affordable option to WFM. Posing a serious threat for WFM in the nature foods industry. There is a definite need for WFM to consider the capabilities of Trader Joe's and its potential in comparison to WFM.

## **Global Economic Conditions**

Economic conditions greatly affect consumer confidence and their willingness to spend. Due to the current volatility in the American market and the pessimistic outlook of the Canadian and European markets, the consumer confidence index has also been volatile. For example, the American consumer confidence has yet to recover to its 2007 levels, while the Canadian consumer confidence index has dropped to 2009 levels (Trading Economics, 2012; Argitis, 2013). This poses a tough challenge for WFM because it has positioned themselves at a high price point due to the high quality and sustainability of their products. As a result, during these economically uncertain times, consumers may opt to purchase from lower priced retailers.

## **Government Regulations**

WFM is subject to various federal, state, and international laws and regulations regarding its products or its industry. WFM will need to comply with provisions regulating health and sanitation standards, as well as the food labeling, equal employment, minimum wage, and necessary licensing for food and alcohol beverages. Recently following the horsemeat scandal in Europe, loop holes in the European food legislation has prompted some critics to push for changes regarding food labeling in Europe (Manthorpe, 2013). Changes such as these may affect the operating costs of WFM or its suppliers, which will have an impact on the net income of the company (WFM, 2012).

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