

natural foods merchandiser's market overview 2008

Editor's note



The numbers are in, and we're happy to report the industry is thriving. Whether their reasons were related to the environment, safety or flavor,

consumers spent at natural products stores last year—especially at the independents,

where sales swelled nearly 12 percent to \$20.9 billion.

Although independents enjoyed double-digit growth, more consumers are buying naturals at conventional stores, as well, to the tune of 12.5 percent growth. Whether it's good or bad news for you, additional mass sales brought the industry to a record \$68 billion—up \$6 billion from 2007.

Amid all the gloomy economic news of late, take a moment to let that number soak in.

In addition to the Overview numbers, in these pages you'll also find interesting data about grocery, supplements, beauty and other departments. Turn to page 32 to learn that vitamin D sales have skyrocketed by 94 percent or to page 38 to find that anti-aging personal care—products sales were flat, which

is surprising, considering all the hype about the category.

Plus, be sure to check out the Market Overview's newest feature: Q&As with five industry experts. It's our way of helping you make the most of the numbers.

—Anna Soref, Editor
asoref@newhope.com

Natural products stores' 2008 sales by category

| | Total sales (M) | Growth | Category as % of total sales | Organic sales (M) | Organic growth | % of category that is organic |
|---|-----------------|-------------|------------------------------|-------------------|----------------|-------------------------------|
| Bakery | \$451 | 6.5% | 1.4% | \$155 | 6.5% | 34.3% |
| Beer/wine | \$738 | 11.0% | 2.3% | \$162 | 12.1% | 22.0% |
| Bulk/packaged bulk | \$1,367 | 7.0% | 4.2% | \$271 | 7.0% | 19.8% |
| Coffee/tea | \$411 | 9.1% | 1.3% | \$290 | 10.1% | 70.6% |
| Dairy | \$1,603 | 9.2% | 5.0% | \$1,208 | 8.7% | 75.4% |
| Fresh meat/seafood | \$1,078 | 12.0% | 3.3% | \$218 | 12.0% | 20.3% |
| Foodservice (deli, restaurant, juice bar) | \$1,238 | 7.0% | 3.8% | \$136 | 5.3% | 11.0% |
| Frozen/refrigerated | \$1,531 | 8.1% | 4.7% | \$419 | 7.5% | 27.4% |
| Nondairy beverages (soy, rice, oat) | \$694 | 5.7% | 2.1% | \$576 | 4.5% | 83.0% |
| Nutrition bars | \$1,031 | 2.0% | 3.2% | \$150 | 16.2% | 14.6% |
| Other beverages | \$609 | 6.4% | 1.9% | \$275 | 8.2% | 45.2% |
| Packaged grocery | \$3,200 | 7.0% | 9.9% | \$1,845 | 7.5% | 57.6% |
| Produce | \$3,899 | 8.3% | 12.1% | \$2,849 | 10.7% | 73.1% |
| Snack foods | \$898 | 6.1% | 2.8% | \$347 | 6.1% | 38.7% |
| Food total | \$18,748 | 7.6% | 58.0% | \$8,903 | 8.8% | 47.5% |
| Herbs/botanicals | \$1,647 | 1.5% | 5.1% | \$76 | 11.9% | 4.6% |
| Homeopathy | \$292 | 4.0% | 0.9% | \$7 | 10.3% | 2.5% |
| Meal supplements | \$253 | 3.5% | 0.8% | \$6 | 17.7% | 2.4% |
| Minerals | \$853 | 8.5% | 2.6% | \$10 | 22.4% | 1.2% |
| Specialty (Ayurveda, glucosamine, EFAs) | \$1,196 | 7.7% | 3.7% | \$51 | 18.8% | 4.3% |
| Sports supplements | \$1,420 | 5.0% | 4.4% | \$8 | 21.1% | 0.6% |
| Vitamins | \$3,574 | 9.4% | 11.1% | \$33 | 12.3% | 0.9% |
| Supplements total | \$9,234 | 6.6% | 28.6% | \$192 | 14.8% | 2.1% |
| Books | \$144 | 3.0% | 0.4% | na | na | na |
| Housewares | \$430 | 17.9% | 1.3% | \$20 | 21.8% | 4.7% |
| Personal care (including aromatherapy) | \$3,220 | 7.1% | 10.0% | \$699 | 11.3% | 21.7% |
| Pet products | \$556 | 10.0% | 1.7% | \$167 | 11.8% | 30.0% |
| Natural personal care/other total | \$4,350 | 8.3% | 13.5% | \$886 | 11.6% | 20.4% |
| Total 2008 | \$32,333 | 7.4% | 100.0% | \$9,980 | 9.1% | 30.9% |
| Adjusted 2007 NFM results | \$30,104 | | | | | |

Totals may not add up due to rounding

Source: NFM/NBJ

Investment roundup

Jane Hoback

The relentless economic downturn continues to take its toll on the naturals and organic industry. With credit markets drying up and the stock market fluctuating, consumers haven't been the only ones pulling back on shopping. The merger and acquisition market, which had slowed to a crawl in the latter part of 2008, came to a complete standstill in the first part of 2009.

As sales dropped, some naturals retailers cut back on new store openings or put expansion plans on hold. Yet despite these dire straits, a few industry experts see glimmers of hope in the coming months.

"For a lot of companies, the goal in 2009 is going to be survival," says Stephen Tardio, managing director of HT Capital Advisors in Chicago. "But there are probably signs of life out there."

Retailing: holding its own

For natural and organic foods retailers, Tardio sees "decent sales growth," of about 5 percent to 15 percent this year. He is seconded by Corinne Shindelar, development CEO of the Minneapolis-based Independent Natural Food Retailers Association, which has 41 members in 80 locations nationwide. "The industry seems to be holding its own."

About five of the group's members are expanding or relocating, and two just opened new locations, Shindelar says. One member, GreenFresh Market in Renton, Wash., closed. "Most of our retailers that had secured financing before the end of the year are moving forward, but those in the planning process that have not secured financing aren't," Shindelar said. "I'm not seeing planning for new locations in 2010."

Sales dipped in the first quarter of 2009, reversed themselves a bit in the second quarter, and are likely to be flat in the third quarter, she said. But, she added, "We have very few members who are experiencing negative store comps."

The National Cooperative Grocers Association, with 111 member co-ops, reports that about 15 percent of its members plan to expand in 2009, down slightly from 2008.

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Key to the charts

N/A: Not available

VMS: Vitamins/minerals/supplements stores

FDM: Food/drug/mass-merchandise stores

Charts provided by: *Natural Foods Merchandiser, Nutrition Business Journal* and the following market research firms: SPINS, based in Schaumburg, Ill., Information resources Inc., based in Chicago; Packaged Facts, based in New York; and Mintel, with offices worldwide.

Phoenix-based Sprouts Farmers Market, which a year ago announced it had increased its growth rate to 15-plus stores a year, said it currently plans to open just 11 stores in 2009. The company operates 31 stores in Arizona, Texas, California and Colorado.

Mike Gilliland, who heads Sunflower Farmers Markets in Boulder, Colo., said that instead of the 12 to 15 stores originally planned, "we'll hit eight this year. And we'll plan eight stores a year here on out until the credit markets loosen up." The company, which operates 24 stores in Arizona, Colorado, New Mexico, Nevada, Texas and Utah, will "do what we can do with our own resources," Gilliland says. "As far as business loans—we've kind of stopped asking."

M&A: at a standstill

The collapse of the credit markets created the roadblock in the merger and acquisition market as well. Natural and organic company M&A activity, which started out vigorously in the first and second quarters of 2008 thanks to cash-rich strategic as well as financial buyers, slowed later in the year, and ground to a halt in the last quarter and into the first part of 2009. Tardio points out that most of the deals in the latter part of the year were already in the pipeline before the economy tanked last fall.

Nutrition Business Journal reported that total M&A activity in the United States dropped 37 percent to \$986 billion in 2008, and initial public offerings fell to a 31-year low.

Tardio notes that during the past six to nine months, "most deals were small and cautious." M&A activity is likely to continue to lag due to the ongoing recession, tight credit, slow growth and poor sales, experts say. Cash will be king. Deals are likely to take longer to complete.

"You can't borrow to buy right now," Tardio says. "That puts financial players on the sidelines. And strategic buyers are having their own problems." Rather than auctions, "a lot of buyers and sellers are talking directly to one another right now," he says.

Valuations have come down, and "there's still a gap between expectations of buyers and sellers in terms of price. In the past, even smaller sellers were looking at [purchase prices of] one times their sales or more," Tardio says. "That's not true anymore." He expects the gap to narrow this year, however.

Looking to sell? Tardio says the investment community is likely to target organic-ingredient suppliers and companies using innovative technologies to produce products that are either organic or have a functional component. Private label will continue to be big. "It seems to be that companies that will be attractive for buyout are those with innovative products rather than me-too products," he says.

Tardio expects deals to get bigger over the next 12 months, "if only because the selling companies have finally grown up a bit and are bigger, and buyers have more cash. But valuations will serve to counteract that a bit."

Jane Hoback is a Denver-based writer and editor.

Average sales

| | Total | Natural products stores | Health food stores | VMS stores |
|---------------------------------|-------------|-------------------------|--------------------|------------|
| Avg. sales 2008 | \$1,475,206 | \$2,855,481 | \$950,424 | \$902,964 |
| Avg. overall net sales change | 9.1% | 11.0% | 7.3% | 1.9% |
| % of stores with sales increase | 67.5% | 74.7% | 69.2% | 59.8% |
| Avg. sales increase | 12.4% | 13.2% | 11.5% | 9.6% |
| % of stores with sales decrease | 30.1% | 21.3% | 28.2% | 39.0% |
| Avg. sales decrease | -10.1% | -6.9% | -16.4% | -9.8% |
| % of stores unchanged | 2.4% | 4.0% | 2.6% | 1.2% |

Source: NFM/NBJ

Business statistics

| | Total | Natural products stores | | | Health food stores | | | VMS stores | |
|--|-----------|-------------------------|---------------------|----------------|--------------------|---------------------|-----------------|----------------|-----------------|
| | | ≤ 2,000 sq. ft. | 2,001-6,000 sq. ft. | >6,000 sq. ft. | ≤1,000 sq. ft. | 1,001-2,000 sq. ft. | > 2,000 sq. ft. | ≤1,000 sq. ft. | > 1,000 sq. ft. |
| Avg. no. of natural products stores under same ownership | 1.9 | 1.6 | 1.8 | 1.8 | 1.5 | 1.7 | 1.9 | 2.4 | 2.5 |
| Avg. retail sq. ft. | 3,196 | 999 | 3,550 | 27,369 | 841 | 1,550 | 5,324 | 867 | 2,238 |
| Avg. linear ft. for natural products | 969 | 641 | 858 | 3,881 | 547 | 793 | 1,675 | 364 | 912 |
| Avg. no. of SKUs | 4,900 | 2,970 | 6,187 | 14,556 | 2,705 | 3,510 | 10,469 | 2,694 | 4,423 |
| Avg. no. of years store has been open | 17.6 | 18.7 | 21.6 | 20.5 | 18.7 | 18.6 | 19.2 | 16.1 | 14.2 |
| Avg. wholesale inventory value | \$118,265 | \$58,860 | \$152,500 | \$490,217 | \$66,748 | \$96,525 | \$161,308 | \$71,940 | \$86,574 |
| Avg. no. of customers per day | 117.7 | 149.1 | 256.3 | 937.9 | 38.7 | 66.3 | 121.5 | 39.9 | 40.1 |
| Avg. sale per customer | \$33.14 | \$24.13 | \$28.76 | \$32.69 | \$33.87 | \$31.71 | \$33.03 | \$38.22 | \$36.04 |
| Avg. no. authorized employee buyers | 3 | 4 | 4 | 10 | 2 | 2 | 3 | 2 | 2 |
| Avg. no. of distributors store works with | 23 | 17 | 25 | 66 | 21 | 21 | 35 | 10 | 24 |
| Avg. annual sales per sq. ft. | \$396.38 | \$553.27 | \$552.17 | \$475.69 | \$254.93 | \$263.89 | \$286.54 | \$409.28 | \$277.68 |

Source: NFM/NBJ

Universe of stores

Independents/small chains

| | # of stores | Sales (M) ** | % of sales | 2008 growth |
|--|---------------|-----------------|---------------|--------------|
| Natural products store ≤ 2,000 sq. ft. | 1,272 | \$580 | 1.8% | 6.0% |
| Natural products store 2,001-6,000 sq. ft. | 2,015 | \$4,623 | 14.3% | 12.6% |
| Natural products store > 6,000 sq. ft. | 968 | \$9,076 | 28.1% | 12.1% |
| Health foods store ≤1,000 sq. ft. | 1,418 | \$351 | 1.1% | 7.6% |
| Health foods store 1,001-2,000 sq. ft. | 1,834 | \$820 | 2.5% | 8.1% |
| Health foods store > 2,000 sq. ft. | 1,518 | \$3,375 | 10.4% | 13.8% |
| VMS store ≤1,000 sq. ft. | 1,705 | \$814 | 2.5% | 10.6% |
| VMS store >1,000 sq. ft. | 1,511 | \$1,227 | 3.8% | 10.8% |
| Total independents | 12,241 | \$20,865 | 64.5% | 11.9% |
| Whole Foods Market | 268 | \$7,724 | 23.9% | -0.7% |
| GNC | 5,280 | \$1,126 | 3.5% | -3.6% |
| Vitamin World | 447 | \$200 | 0.6% | -10.5% |
| Other* | 18,400 | \$2,418 | 7.5% | 5.6% |
| Total natural health food/specialty | 36,636 | \$32,333 | 100.0% | 7.4% |

* Includes co-ops, specialty/gourmet, personal care (Body Shop, Garden Botanica, etc.), gyms, herb shops, mall stands, etc.

** Sales include foods, supplements and other (natural personal care, books, household goods, etc.).

Totals may not add up due to rounding.

Source: NFM/NBJ