

# How To Compete In The Natural Products Marketplace

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I came into this business at an early age, working in my parents' health food store, which they purchased in 1960. Things have changed considerably since then. Products that once were available exclusively in health food and natural product stores now are available in more than 20 different retail channels.

In the early days, the drug stores, doctors and supermarkets were looked on as the profit-driven capitalists catering to the unenlightened masses. We members of the natural nutrition movement had the truth, and the truth had set us free to convert the world to a better way of life through healthful foods and supplements.

Back then, the retail outlets all contained "health food store" in their titles, and we used only two keys on our cash registers: "taxable" and "non-taxable." We worked hard, pulling converts off the street one at a time as they walked by, curious for information about a particular vitamin or supplement that they heard might help them with a condition that they had.

Although we did not understand it in those days, at our very roots we were a knowledge-and solution-based industry, and this is a driving principle that remains with us to this day.

The fact that eating natural and organic foods improves one's health, and that natural supplements provide relief from symptoms more safely and economically than drugs were the truths that drove our industry's growth. In spite of declarations from the mainstream medical community and conventional food industry that all this health stuff was pure poppycock, mounting scientific evidence was proving otherwise.

## When Price Wasn't King

In my early years in the business, there were few sales, deals or discounts. When it came to a one's health, results were what counted, not price. This is another principle that has remained with us to this day. Or has it?

The rising popularity of natural products-so-called complementary and alternative medicine-driven by consumer testimonials and good science, has brought us to a point where both the medical community and food industry no longer could ignore the fact that natural products sales had been enjoying continued "healthy" double-digit growth. In our view, if these products had not been living up to the claims being made for them-that they could improve health or relieve symptoms-the mainstream outlets never would have felt threatened with a loss of market share. But that is precisely what did occur.

Afraid that if they stayed on the natural product sidelines they would miss the gold rush to natural products, drug stores, supermarkets,

mass merchandisers, club stores and dozens of other distribution outlets have attempted to join the playing field, seeking membership in the "private" club. Some have been successful. Most have not. Those that have succeeded understand that the core natural products consumer who frequents health and natural products markets is an educated, affluent, value- and knowledge-driven customer-not one of the masses who make up the bulk of the mainstream's customer base.

Numerous research studies have reported that consumers want to eat more healthfully and are interested in using alternative natural remedies. Nevertheless, our cash registers are telling us that more consumers are thinking about buying organic foods and natural supplements than actually are purchasing them.

Herein lies the dilemma: there are three groups of consumers:

1. There is a core group of educated and value-driven consumers who purchase products primarily from natural product stores.
2. There also exists a larger, more peripheral group of consumers who, on the one hand, tell us that they want to eat better and that they support the concept of organic foods and supplements, but, on the other, simply are not committed to paying a premium price for these premium products. Most of these consumers frequent conventional outlets. For this group, price is an important decision-making factor in moving natural products through mainstream channels.
3. The last group consists of those consumers who make their food purchases without giving any thought to health or nutrition. This group is highly motivated by price and sees little value is spending extra for healthy foods, let alone natural or organic products.

## How Natural Is Natural?

A business that sells natural products must understand the difference between the "natural" consumer and the "truly natural" consumer. The core natural product consumers, the "truly natural," view their purchases through a "total wellness" window. They are committed to consuming primarily organic and natural products and supplements. Quality, benefits and knowledge drive their purchases.

Peripheral natural product consumers view their purchases through a "healthy" window. They see "low-fat," "low-salt," and "reduced-calorie" products as healthy, but probably not essential. Although they tell researchers they are health-oriented, they are not committed to a "total wellness" program.

Overlay this discussion with a value-price analysis covering the general population, and the road map becomes clearer. This analysis

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reveals that those consumers in the younger age groups (20-35) are more price-driven and less value-oriented, than those consumers in the older age groups (40 and above). The value and price influence lines move in opposite directions with the 20-year-old being the most price-driven and least value-concerned, and the over 55-group being the most value-driven and least price-sensitive.

If you are a natural product store owner trying to determine how best to compete among the other 20-plus distribution channels, your first question has to be, "Who are my customers?" Do more of them fall into the educated, affluent, value-driven, total wellness, over-40 age group-or are more of them in the younger, budget-conscious, peripheral group?

The experience of the average natural products store is that the top 30% of customers deliver 75% of sales, while the bottom 30% of customers account for only 3% of sales. Yet that bottom 30% often are the vocal minority-the first ones to tell you that they can purchase a product more cheaply in another store. Meanwhile, overall, they purchase the least from your store. If you make the mistake of lowering your prices just to attract these bottom shoppers, you give up crucial margin needlessly on between 70% and 90% of your sales.

There also is another factor to consider before lowering prices: if you simply are attempting to respond to competition from mass market, drug and discount stores, then you should first get to know who their customers are. The typical customer at these outlets falls into the peripheral, price-driven group. Few truly natural consumers shop in mass, drug or discount stores for their natural foods and supplements. In fact, the nation's 30,000 supermarkets have coexisted quite well with natural product stores, not by taking market share from them, but by servicing a different customer.

Meanwhile, the 4,000-store GNC chain has done a good job of attracting younger crossover consumers and introducing them to supplements. Many mainstream consumers made their first "natural" supplement purchase at a GNC store.

Inadvertently, this very strength of GNC actually led it into a heap of trouble. Here's what happened: most of GNC's customers are demographically similar to Wal\*Mart shoppers. Thus, when that retailing giant and other mass market stores began stocking more natural products, GNC saw it as a serious threat. This prompted the firm's announcement last summer that it was lowering prices on 40 products.

Wall Street's reaction-based on the theory that lower prices mean lower profits-drove GNC's stock into the tank, and many other supplement stocks were pulled along with it.

## Just Another Price Competitor

In many respects, Internet merchants are simply electronic versions of the mail order, catalogue, or price-oriented mass marketers. And, therefore, although the Internet relies on new technology, the competitive pressures it brings to bear are, in many respects, no different from those natural products retailers have faced for years.

A close examination of the Internet "boom" reveals the following: first, the category of websites that attracts the greatest number of visitors is sex and pornography. This may be a sad commentary on the morals of Internet users, but it hardly is a shocker to many. The category with the second largest Internet audience is health and health-related issues, and that, legitimately, may be considered a surprise.

In fact, this statistic has important ramifications for the natural products industry. It suggests that each day more people are using the Net for information on personal health issues, and demographics confirm that this will continue to be a growing trend.

From an e-commerce perspective, the non-perishable nature of many natural remedies surely lends itself to Internet ordering and delivery. But the big question remains as to how much, if any, sales of natural products will be lost by traditional retailers.

Forgetting for the moment the recent near-industry-wide sales-softening, which has been identified as a natural correction of an over-explosive market, the industry has experienced impressive growth during the past seven years. During this period, multiple channels of distribution for natural products have opened. Products that were available only in natural food stores now appear everywhere, including drug stores, discounters, club warehouses, mass marketers, supermarkets and the Internet. Mainstream manufacturers have invested tens of millions of dollars into the introduction of new natural product lines. Hundreds of millions have been invested in the Internet distribution channel.

Happily, so far, the effect of increasing the distribution channels and product offerings has been to further expand the market. The increased presence of natural products in all these new venues has fueled a public awareness that never had been seen before. As a result, sales have climbed throughout the entire industry. So the initial impression-that these new markets would take business away from traditional natural product stores-has not proved true. Indeed, the continual ringing of cash registers at natural products outlets is telling us just the opposite.

Internet pricing may be of some concern, but remember that consumers have been able to purchase supplements discounted at 20%-30% through mail order catalogues for 25 years. During this period, the mail order channel has captured only 4% of the supplement market. Will an Internet-placed mail-order capability cause market share to be lost from traditional retailers-or simply grow the entire market as we have experienced with other new distribution channels in the past? This, of course, is the big question. So far, most Internet supplement sales have migrated from the mail order channel and not retail storefronts.

## Amazon's Shortcomings

Internet projections, most recently, have started to be trimmed to more realistic proportions. Observers-if not investors-are beginning to gain perspective. For example, it hasn't gone unnoticed that after five years was the leading online retailer, Amazon.com was still

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hundreds of millions of dollars away from making a profit. Even more important, sales of books by all Internet retailers combined were roughly 3% of total book sales. The fact that bricks-and-mortar book retailers have been able to maintain 97% market share in the face of all the hype about Amazon over five years is a pretty good indication that they are going to be around for a long time.

Nevertheless, regardless of the level of market share captured by the e-tailers, it would be the height of stubborn folly to deny that they represent potential competition at the very least. Therefore, prudence dictates that traditional retailers should formulate a strategy for competing with these cyber rivals, just as they have for dealing with the likes of CVS, Safeway, Kmart, mail-order houses and multilevel marketers.

So how do we best compete? By learning all that we can about the needs and desires of our customers and crafting our businesses in such a way that we meet the strongest concerns of our highest spending, most loyal patrons. Specifically, here are some steps we should be taking:

- Market and merchandise to attract the “eagles.” These are the educated, affluent, time-starved consumers for whom quality, selection, knowledgeable service and convenient location are most important. Eagles will not drive across town to buy something at a lower price. They do not have the time. Eagles prefer to talk face-to-face with someone they trust about their health needs and supplements, rather than look for the cheapest product, drive to a discounter across town, or click through dozens of 30-second-to-load web pages.
- Use monthly specials and power stacks to project a good price image, and give faithful customers added value. Straight line discounting does little to drive top line sales, and erodes the bottom line.
- Seek out quality-efficacious products with good science behind them-and use “sell-the-solution” marketing rather than price promotions.
- Position your store and its personnel-through your newsletter and health columns submitted to local newspapers-as experts in their field and a ready source of nutrition information for your community.
- Begin your own research on how to use the Internet for communication between you and your customer. The Internet can be a powerful tool to drive customers back to your store. ***Check out LivingNaturally.com.***
- Incorporate a category management strategy into your everyday operations to eliminate the slow sellers and increase the facings of better sellers.
- Continue to watch the market. Make changes when you see a new trend appearing-and remember that a shift is not necessarily a trend.

## More Big Stores

Seven years ago, it was estimated that the U.S. market could support approximately 200 natural products supermarkets over 15,000 square feet in size. Today, the market probably could support twice that many.

Although demographic trends point to continued growth in our industry, we are still only 2% the size of the conventional grocery industry, and organic produce represents only 1% of all produce sold. As I see it, we have miles of potential at all levels.

The successful selling of natural products is an art. A national survey of the natural foods market released by The Henry A. Wallace Institute for Alternative Agriculture found that while almost half of mass market grocery retailers increased their natural foods offerings, fewer than 20% claimed success.

Natural foods will continue to appear through dozens of distribution channels. Some will do it right. Others will not. Regardless of the overall number of outlets, however, there always will be a place for natural product retailers who have good marketing and merchandising savvy, as well as the love, commitment and passion for these products. This is something that mass marketers most often do not provide.

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