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Consumers get frugal, so retailers get creative

By Jayne O'Donnell and Sandra Block, USA TODAY

FOR YEARS, DIETICIANS HAVE urged Americans to practice mindful eating. Eat slowly. Savor every bite. If eating chocolate cake, make sure it's really good chocolate cake. Now, as the country slogs through the worst recession in decades, consumers are increasingly taking a similar approach to spending.

The change shows up every month in retailers' dismal sales. On Tuesday, the National Retail Federation said retail sales are expected to drop 0.5% this year, the first annual decline since the NRF started tracking sales in 1995.

"Most of the consumer behavior we saw in 2008 will continue well into this year," says Rosalind Wells, NRF's chief economist. "Shoppers will be seeking value and trading down to discount and off-price retailers in order to stretch their purchasing power."

Even though spending is expected to increase in late 2009, no one's predicting a return to the devil-may-care shopping from earlier this decade. Now, when consumers spend, they're paying more attention to what they buy. And this shift toward more cautious spending is likely to last.

Sales of furniture and clothing have been plummeting, with retailers in those sectors posting double-digit sales declines. On Monday, Home Depot announced plans to close its 34 Expo design stores, which sell high-end home decor items.

Essentials, such as food, health and beauty aids are selling, but even there, consumers are shifting to less-costly store brands. Consumers are still buying an occasional video game — an industry that's proved to be largely recession-proof — but sales of big-ticket items, such as cars and vacation packages, have fallen off a cliff.

To survive, retailers are battling to convince these new, mindful spenders that their products deliver long-term value, not just empty calories.

"How smart you shop has become a new status symbol," says Eric Gustavsen, co-founder of New York-based branding and design firm Graj + Gustavsen.

While the downturn is cited as the main reason for dreary retail sales, other factors are also at work. Many have realized that

it's not necessary to buy new vehicles or furniture every few years, unless the car dies or the springs give out on the couch. With vehicle sales down 18% last year — the biggest drop since 1974 — it's auto repair shops that are expected to thrive. And after years of recreational shopping, many Americans are starting to realize there's no more room in their closets.

Christine Jonard, 36, of Columbus, Ohio, meets regularly with local mothers to swap clothes and toys for her three children, ages 5, 3 and 1. With the exception of Christmas gifts, she can't



Katherine Motley organized clothing swaps in her community. She's here with six of her seven kids (clockwise from bottom): Alexis, 19; mom Katherine; Zoe, 4; Heather, 14; Evan, 11; Sydney, 5; and Gabrielle, 13.

remember the last time she bought a toy. "We have too much stuff," she says. "Plus, we don't have any money, probably because we have too much stuff."

Katherine Motley, 36, of Phoenix, started organizing clothing swaps in her community about a year ago because she was looking for low-cost ways to outfit her seven children. She says she's spent less than \$100 on clothes in the past year. She believes the interest in swaps will outlast the recession: "People who are like-minded will continue to do these swaps even when the economy recovers."

Speaking before NRF's annual conference this month, Carl Steidtmann, Deloitte Research's chief economist for consumer business, said the spending slowdown was predictable. After a spending boom like the one that occurred

after the Sept. 11 terrorist attacks, he said, "You always see a return to simplicity."

Many consumers still have money to spend, Steidtmann says, "They just don't have the will."

Even high-income shoppers are cutting back, as shown by the sharp drop in sales of luxury items during the holidays, says Jim Harold, retail industry executive for Acxiom, a consulting firm.

Coach, manufacturer of luxury handbags, reported last week that sales at North American stores that have been open at least a year fell 13% during the quarter ended Dec. 27. The company attributed the decline to its decision not to lower prices on its signature handbags at a time when most other retailers were slashing prices.

Luxury shoppers aren't just "looking for deals," Harold says. "They're demanding them."

Consumer spending accounts for about 70% of the economy, up from 66% about 10 years ago, but down from about 72% earlier last year, says Marie Driscoll, director of consumer discretionary retail for Standard & Poor's Equity Research. Driscoll predicts spending will continue to fall until it reverts to being about two-thirds of the economy again.

"We will grow again, but not at the rates we saw before," she says.

HOW RETAILERS ARE TRYING TO SURVIVE:

Highlighting value

"In 2009, the consumer will act rationally," says J.C. Penney CEO Mike Ullman. "They will shop for what they need and less for what they want. And they don't need much."

Cara Putman, 34, of Lafayette, Ind., falls into that category. She's always looked for sales before paying full price for anything. Now, though, she's less likely to make a purchase. What has changed, she says, is a new "willingness to talk myself out of a purchase (and say), 'I don't really need that.' I hope that's a discipline that sticks. And I honestly think it stems more from a desire to streamline and move to simplicity than fears about the recession."

To appeal to customers like Putman, retailers need to convince them that their

brand will make life easier or better, **Gustavsen** says. His firm helped women's fashion line Rafaella come up with a new direction last year that emphasized the clothes' functionality, including two-way stretch and "ergonomic" fabric that moves with the body. The campaign stressed that people shouldn't buy a Rafaella garment "just because it's pretty," he says. Retailers are also looking for ways to stand out from the pack. Along with too many stores, the retail business is crowded with too much merchandise that looks the same, says Macy's CEO Terry Lundgren.

"We need newness, freshness and unique products that will get people interested in buying again," he says.

To compete in this environment, retailers need to go back to their roots, says Janet Hoffman, Accenture's global retail managing partner. That means "knowing their customers and coming up with a unique offer or product, price or, in some cases, service," she says.

Offering better prices

After a holiday season in which many consumers waited until prices were slashed 75% or more to buy, marketers are rethinking pricing strategies. The new directions include adding more lower-cost store brands or products and working with manufacturers to come up with starting prices that products are more likely to sell at.

In response to consumer spending trends, retailers are doing their own buying "with an increased focus on value and price," says Dan Butler, NRF's vice president of store operations and merchandising. Retailers are working with apparel makers and other manufacturers to come up with ways of lowering the cost of products so they can pass savings on to consumers, he says. "It has to be a relevant price for this economy," says Butler.

The response to lower-priced private-label brands in stores has been increasingly positive, with consumers buying 8% more in 2008 than in 2007, according to a report by Sanford Bernstein analyst Ali Dibadj.

"Consumers are figuring out that many private-label products are just as good as branded products — just cheaper," Dibadj says.

Still, style consultant and author Sherrie Mathieson says consumers should remember that sometimes when you pay more, especially with apparel, you're getting higher-quality clothing that's likely to last longer. And she urges her clients to keep that in mind in this economy, when a good suit or dress can be a good investment.

"The modus operandi of shopping wisely will always need to be a mix of trying to get value at a lesser price and knowing when to go for it," says Mathieson.

Emphasizing local ownership

When design firm FRCH planned the redesign of 56-year-old Massachusetts grocery chain Roche Bros. in 2006, it decided to emphasize the local heritage and produce. Customers told store officials in focus groups that those were the two most important reasons they shopped at the stores. That was good news for a store run by the sons of one of the founders that competes against several national chains and discounters including Wal-Mart, which has attracted new customers during the recession.

"It fit right into who we are," says Arthur Ackles, Roche's director of marketing. "We're a local company that's very involved in the community."

The five of 18 stores that have been redesigned highlight the chain's long presence in their areas, including photos at the checkouts that date back to the stores' early years. Since the Wellesley, Mass., store was completely redesigned, the local theme was stressed and product selections expanded last year, sales are up 40% despite the economic downturn, says Ackles.

A survey of independent retailers in a wide range of categories found that sales fell an average of 5% in December, vs. a decline of 9.8% for retail sales overall, according to the Institute for Local Self-Reliance, a non-profit research organization. Retailers in cities that sponsored "Buy Independent/Local" campaigns reported an average decline of 3.2%.

Consumers who patronize local businesses instead of big-box stores are "realizing that cheapness is not the same as value," says Jeff Milchen, co-founder of the American Independent Business Alliance.

Going green

Last week, PepsiCo announced that Carbon Trust, a U.K.-based organization that studies climate change, will certify the carbon footprint of several of its products, starting with Tropicana Pure Premium orange juice. PepsiCo said the certification will provide a benchmark for the company to use in its efforts to reduce greenhouse gas emissions.

A January 2008 survey by Information Resources Inc. found that 70% of Americans are more likely to support companies that are mindful of their impact on the environment and society. The survey predicted the market for sustainable products would grow to \$410 billion by 2010, nearly double its 2005 level.

To attract a piece of that market, online auction giant eBay launched a partnership last year with WorldofGood.com, an online marketplace that offers organic toys, BPA-free water bottles and other products that, the company says, "have a positive impact on people and the planet."

Selling sustainable products doesn't inoculate companies from the recession. WorldofGood doesn't break out separate

revenue, but in recent months, eBay's sales have suffered. The company's net income fell 31% in the fourth quarter.

"Consumers are definitely more cautious in how they're spending their dollars and they're looking for greater value," says Robert Chatwani, general manager for WorldofGood. "We're not immune to that."

In response, the website has been promoting items that are gentle to both the environment and customers' bank accounts. It has made it easier for customers to search items based on price, which provides "more exposure for items that might be more affordable," says Priya Haji, chief executive of WorldofGood.

Anna Moncharsh, 20, a psychology major at Yale University, says she purchased most of her holiday gifts from WorldofGood because she supports its mission and was able to find relatively low-cost items.

"I've always tried to think about what I'm buying, what it's made out of and where I'm getting it from," she says. "And considering the circumstances everywhere right now, I think it's made me more aware of how I choose to spend my money."

Indeed, gone are the days when retailers could convince people they need something they really don't, says Alexi Sarnevitz, who heads global retail strategy for business analytics software company SAS. They need to put their marketing support behind the products consumers really want, he says, and not focus on creating "artificial demand."

"The changes in consumers' psyches are too pervasive," says Sarnevitz.

Gustavsen says people are looking for a "valid reason to buy something."

"If the reason is authentic, even if it's emotional, that's as good a reason as any," he says. "What's out is buying just to buy. I guess that's mindless spending."