# The Rise and Fall…and Rise Again of Private Label in Canada

*Kevin Grier, Senior Market Analyst*
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Private label (PL) market share in Canada has trended lower in recent years, according to Nielsen MarketTrack data. This is unanticipated for a number of reasons, one being that it is contrary to expectations for consumer behaviour during a recession. More importantly, the lower PL trend runs counter to the experience and practice at many grocers and manufacturing firms in Canada. Meanwhile, the direction and trend in PL has important implications for companies across the food chain in Canada. For these reasons, it is worth taking a look at why private label share in Canada may have declined in recent years. It is also important to examine where private label's share may be heading in Canada over the next several years.

As a starting point, private labels are defined as retailer-owned brands. They are sometimes called store brands or controlled labels. They are only available at a particular retailer, and typically in multiple categories. The Progressive Grocer *Glossary of Grocery Industry Terms 1995* defines PL as "a product label or brand owned by a wholesaler or retailer for a line or variety of items for exclusive distribution." This contrasts to national brands, which are available at all retail outlets. PL products have existed for decades, but have only been gaining share and importance in Canada over the past twenty years. The growth and development of private label in Canada has been led by Loblaw with their President's Choice and No Name brands.

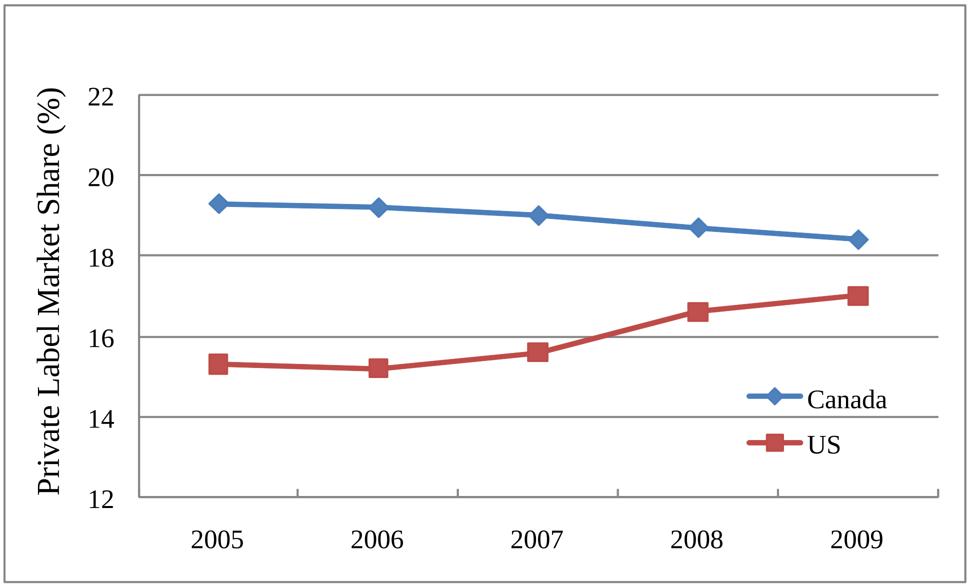
## Private Label Status and Trends

Sobeys Inc, of Stellarton, Nova Scotia, recently issued a media release extolling the virtues and growth of PL in Canada. Following are some of the points raised by Sobeys, based on a consumer trends poll:

- More than 80% of Canadian grocery shoppers say they purchase PL brands
- 49% of Canadian shoppers purchase PL brands frequently and 34% say they sometimes purchase them
- 58% of Canadians who purchase PL products frequently say they are less expensive and offer their families greater value
- 48% of frequent PL buyers said they feel the products are comparable, or better, in quality than national brand names
- PL brands are most popular in Quebec and Ontario, with 54% and 51% respectively saying they purchase them frequently

Despite these results, Nielsen data show that PL's share has plateaued or is in decline. Figure 1 shows PL's share of total market dollars over the last five years in the US and Canada.

**Figure 1: Private Label Market Share**




**Source: Nielsen MarketTrack, National All Channels, 52 weeks to December 19, 2009, Excludes Random Weight Fresh; US: ScanTrack**

Not only is the Canadian trend surprising, but most in the industry do not even agree that it is declining. The trend is not within the experience of many in the industry who instead see that their shares of PL are expanding. That said, there are factors at work that can explain the trend.

## <u>US is Understandable</u>

The US growth in private label penetration is not surprising. For one reason, their market had been quite underdeveloped with regard to PL, relative to Canada and Europe. However, it was only a matter of time before major US retailers began to expand and build-up their PL programs. Another big reason for the growth in the US is that the recession has been deeper and more challenging than in Canada, beginning in the fourth quarter of 2007 and peaking in 2009. Consumer surveys have repeatedly shown over the past year that US consumers are switching to PL in order to save money during difficult times. This may have driven a significant increase in PL distribution in retail. Retailers felt they needed PL to show consumers they were responding to the recession and helping out.

In fact, there have been huge changes in the dry grocery and perishable sets in US grocery stores, due to the increase in private labels. This is particularly the case at Wal-Mart and Costco, followed by Kroger. A visual appraisal suggests that at least one-third of the sets at Wal-Mart Supercenters are PL now, whereas three years ago they may have had 5-10% of space in the same categories. It is also notable that there were no major marketing initiatives for PL in the US. Instead, they just quietly found their way onto store shelves. One other trend that may have helped is that many of these retailers, led by Costco and Tesco, saw that consumers were prepared to accept fewer brand choices in a set. Many tertiary brands were culled to make room for the growth in PL shelf space and SKU's. Of course, Wal-Mart has recently admitted that there is a limit to what can or should be culled.

There are two key noteworthy points regarding PL's in the US and Canada. Both relate to the fact that the two markets are significantly different as they relate to PL and national brands. The first is that national brands have tended to be stronger in the US than in Canada, or conversely private label is more developed in Canada. This could be due to higher relative incomes in the US. It could also be due to the fact that Canadians developed a taste for PL in the more challenging economic circumstances of the 1990's. Perhaps the simple answer is that Canada is the home of Loblaw, the leading North American force behind PL. Whatever the reasons, the two markets remain dissimilar.

The second point of interest, as shown on Figure1, is that the PL share is trending differently in Canada vs. the US. While the US trend might be easy to understand, it is the Canadian direction that is of particular interest, as explored below.

**<u>Pricing Differential</u>**

The Nielsen data show that PL's dollar market share in Canada has declined in each of the last five years from about 19.3% in 2005 to 18.4% in 2009. Data from earlier periods, which are not directly comparable, suggest that PL share may have peaked in Canada around 2003 or 2004. This, of course, means that the national brand share has been increasing. Table 1 shows the 2009 breakdown in PL and national brand shares by dollars, tonnage and units. It also shows the change from 2008.

**Table 1: Private Label Compared to National Brands**

| | Private Label | | National Brands | |
|---|---|---|---|---|
| | 2009 Market Share % | vs 2008 | 2009 Market Share % | vs 2008 |
| **Dollars** | 18.4 | 4% | 81.6 | 5% |
| **Units** | 18.7 | -2% | 81.3 | 1% |
| **Tonnage** | 24.3 | -3% | 75.7 | 1% |

**Source: Nielsen MarketTrack**

As can be seen in Table 1, while PL dollars increased by 4% last year, the national brands increased by 5%. On a tonnage and unit basis, PL declined while national brands increased modestly. By any measure, during 2009 PL slipped while national brands gained.

As noted earlier, the decline in PL market share is surprising for a number of reasons related to the nature and relative price of PL. For example, one reason for the unanticipated trendline is the fact that PLs are less costly than national brands. Depending on the category and the product, national brands can cost anywhere from 15% to two times more than PL at retail. In fact, given the widely varying classes or tiers of PL and national brands at retail now, it is probably not even wise to generalize about the price spreads between PL and national brands. That is to say, for an upscale or first tier PL offering, the differential will be less than that of a more generic offering. Loblaw's President's Choice and No Name are the most familiar examples of upscale and generic, respectively, although all leading grocers have tiers of PL. The two main tiers at Metro are "Selection" (lower) and "Irresistible" (upper). Overwaitea's upper end brand is the "Western Family" while its lower or second tier is called "Value Price."

Of course, there are variances in tiers between national brands such as Heinz and French's mustard, or Delissio and McCain's frozen pizzas. There are even national brand tiers within the same company. For example, within the Procter & Gamble diaper offering there are Pampers and Luvs. One is premium, the other is budget.

Table 2 shows various product offerings and prices at Loblaw's Zehrs banner, Metro and Sobeys in Ontario as of July 2010. The table shows the wide variation in prices between national brands and PL, depending on the tier of PL or national brand.

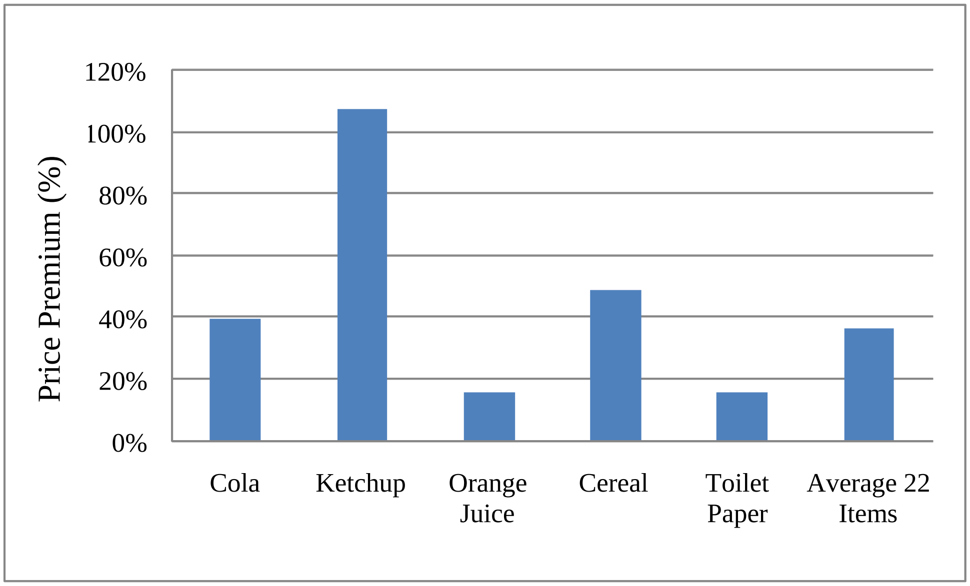
**Table 2: PRIVATE LABEL AND NATIONAL BRAND PRICE COMPARISONS, ONTARIO, JULY 2010**

| | ZEHRS | | | | METRO | | | | Sobeys | | |
|---|---|---|---|---|---|---|---|---|---|---|---|
| **Product** | **Brand** | **Price** | **unit** | **Product** | **Brand** | **Price** | **unit** | **Product** | **Brand** | **Price** | **unit** |
| Detergent | Presidents Choice | 7.29 | 1.9kg | Bacon | Selection | 3.49 | 500 g | Salad Dressing | Compliments | 1.99 | 475 ml |
| | Tide | 9.39 | 1.8kg | | Maple Leaf | 4.49 | 500 g | | Kraft | 2.50 | 475 ml |
| | | | | | | | | | | | |
| Toilet Paper | Presidents Choice | 6.79 | 8 rolls | Toilet Paper | Irresistible | 5.49 | 8 rolls | | | | |
| | Royal | 7.79 | 8 rolls | | Cashmere | 6.39 | 8 rolls | | | | |
| | No Name | 3.49 | 12 rolls | | | | | | | | |
| | | | | | | | | | | | |
| Cola | Presidents Choice | 3.99 | 12 cans | Cola | Selection | 3.49 | 12 cans | Cola | Compliments | 3.99 | 12 cans |
| | Coca Cola | 5.49 | 12 cans | | Coca Cola | 5.49 | 12 cans | | Coca Cola | 4.99 | 12 cans |
| | | | | | | | | | | | |
| Ketchup | Presidents Choice | 1.79 | 1 litre | Ketchup | Selection | 1.99 | 1 litre | Ketchup | Compliments | 1.99 | 1 litre |
| | No Name | 1.79 | 1 litre | | Heinz | 3.99 | 1 litre | | Heinz | 3.99 | 1 litre |
| | Heinz | 3.99 | 1 litre | | | | | | | | |
| | | | | | | | | | | | |
| Pasta Sauce | Presidents Choice | 2.49 | 700 ml | Pasta Sauce | Irresistible | 3.49 | 700 ml | Soda Crackers | Compliment | 1.99 | 450 g |
| | No Name | 1.49 | 700 ml | | Selection | 1.79 | 700 ml | | Premium Plus | 2.99 | 450 g |
| | Prego | 2.99 | 700 ml | | Prego | 2.99 | 700 ml | | | | |
| | | | | | | | | | | | |
| Tomato Paste | No Name | 1.19 | 369 ml | Orange Juice | Irresistible | 5.79 | 2.84 l | Pancake Mix | Compliments | 2.99 | 905 g |
| | Hunts | 1.59 | 369 ml | | Tropicana | 6.69 | 2.63 l | | Aunt Jemima | 3.79 | 905 g |
| | | | | | | | | | | | |
| Cereal (flakes) | Presidents Choice | 3.59 | 750 g | Cereal (O's) | Selection | 5.99 | 1.3 kg | Cereal (O's) | Compliments | 3.99 | 575 g |
| | Kelloggs | 4.99 | 750 g | | Cheerios | 9.39 | 1.3 kg | | Cheerios | 5.79 | 525 g |
| | | | | | | | | | | | |
| Pancake Mix | Presidents Choice | 2.59 | 905 g | Cereal Bars | Selection | 2.79 | | Cereal Bars | Compliments | 2.99 | 300 g |
| | No Name | 2.39 | 905 g | | Kellogg | 3.49 | 295 g | | Kellogg | 3.49 | 295 g |
| | Aunt Jemima | 2.99 | 905 g | | | | | | | | |

**Source: George Morris Centre, July 2010**

Given the variance in pricing differentials, as shown in Table 2, it is obviously difficult to generalize about pricing between national brands and PL. Nevertheless, a comparison of 22 of the items in Table 2, between the first tier PL and the national brand, shows a national brand premium of about 36%. Figure 2 shows the premium for five products and the 22-product average.

**Figure 2: National Brand Price Premium over PL, July 2010**




**Source: George Morris Centre**

Notable in Table 2 and Figure 2 is the huge premium that Heinz ketchup retains over PL. Meanwhile, Heinz has managed to retain its share of the market over the years. This is testimony to the equity and loyalty a national brand can enjoy.

With the variances noted, however, it remains apparent that PL offers savings, sometimes substantial. Furthermore, while there is room for argument, there is little difference in quality between most high-end PLs and the leading national brands. Given the costing differential, it is particularly interesting that, during recession and periods of high unemployment, PL is not growing. In other words, the US performance conforms more to pre-conceived ideas of behaviour during a recession. The fact that the Canadian recession was shorter and less damaging might explain the difference, in part.

## PL Benefits to Grocers

Another note of interest is that the decline is not a grocer-driven strategy. That is, Canadian grocers are not de-emphasizing or cutting back on PL offerings, shelf space or merchandising support. If anything, the offerings and support are increasing. Evidence of such is the fact that Sobeys is introducing several hundred more PL lines over the next 18 months. In this regard, it is worth recalling why grocers favor PL:

1. The margins are usually better for grocers on PL than they are for national brands. Again, it is prudent not to generalize about the magnitude of the margin difference as it varies greatly between categories and between grocers. The differences in margins within the store, of course, are due to the nature of the competition in the category. In some categories where national brands margins are already tight, the PL offering will have less of a differential. Differences between grocers or banners will be due to the

strategic purpose or importance the grocer or banner places on PL.  As such, the margin differential in favor of PL can vary from just a few cents on an item to as much as two times the national brand margin, despite the fact that PL sells for less.

2. PL gives grocers leverage in the market with national brand manufacturers.  Grocers know what it costs to produce the product and they know what is happening in the commodity markets.  PL provides a realistic threat to national brands in terms of delisting and spacing.  It also provides a counterbalance to keep manufacturer costs in line.
3. PL provides grocers with a "destination" product line.  It gives grocers the opportunity to offer products that are available only at their stores.  Of course nobody has done this better than Loblaw's PC brands, and their ongoing efforts with green products and Blue Menu items.  They can drive consumer loyalty and brand equity for the retailer.

As a result of the two or three key private label strengths, grocers learned the proper balance between national brands and PL.  They learned about the value of brands and the consumer equity that the brands in the category held.  For example, grocers learned that tier two and tier three national brands had little or no consumer equity.  Those brands could be swept away without a loss of consumer demand.  As well, the loss of those brands resulted in an increase in the margins afforded by their PL replacements.  The categories were clarified and simplified for both consumers and retailers.  In summary, from grocers' perspectives, store brands have helped them control their own destinies and develop better consumer focus and delivery.

This allows for the argument that a decline in private label share is not due to retailers pulling back on their efforts, at least not intentionally.  However, it is without doubt that Loblaw drove PL share and development in grocery retail in Canada.  It was like a business cult where everything they did was to strengthen the PL shares.  Like most businesses there is a life cycle, and PL's business cycle at Loblaw needed to be reinvented to stay on top.  Given the stress and change at Loblaw during the past three or more years, there was less emphasis on PL.  Based on media reports, it appeared that the focus over the last few years was on cost cutting, price matching and logistics, which helped eat up operational budgets.  The new management teams have not placed the same emphasis on PL.  It is also logical to assert that Loblaw's lack of drive or support has been reflected through their competitors.  The assertion, therefore, is that a lack of emphasis at Loblaw can partially explanation the lack of PL growth across Canada.  This argument would apply not only for Loblaw itself but for its impact on other grocers.

## National Brands Fight Back

Another reason for the lack of growth in PL in Canada has to be the push back coming from the national brand manufacturers.  National manufacturers like Kraft and P&G are not sitting back waiting to lose market share.  They are fighting back with trade promotion and consumer promotion dollars.  By all accounts, the national brand manufacturers are pumping more money to retailers to keep shelf space, to lower prices and to merchandise their products.  From a practical perspective, they are waging a price war with PL for shelf space.  Retailers report that basket size is up and trips are down which makes it all that much more important for manufacturers to get their brands out front.

Also of note is that PL penetration in Canada is already quite high. In Europe, PL market share is generally measured at around 25%, and is much higher in some countries than others. While low compared to Europe, Canada's share is relatively high. As such, the growth potential might be somewhat limited in Canada. In addition, shoppers who did feel income pressure could just as easily be swayed by promotions on national brands, rather than trade down to PL.

Other factors of influence:

- Deflation in other categories frees up the food budget to a certain extent. Consumers have not been pressured to purchase lower-priced PL because overall price levels have remained low.
- As Wal-Mart grows their food business in Canada, which is by any account inevitable due to their expanded Supercentre presence, overall PL penetration would decrease since their PL program is weaker in Canada. Within this context, as of now, most analysts view Wal-Mart's PL offerings in Canada as very tepid or uninspired. The simple arithmetic of this combination means that overall Canadian PL share is going to lag, at least until Wal-Mart gets serious about PL in Canada.
- The same trend holds for ethnic stores, which are the source of most of the growth in the grocery industry in Canada. Ethnic stores are not big on PL. Given that they are growing, this suggests PL share would be under pressure.

## Looking to the Future

As noted, industry participants are astounded that private label share overall in Canada is down, especially as most see their PL businesses growing. The unanticipated trend is also a surprise as it relates to the expectations for PL behavior in a recession, and the fact that the positive components of PL are still well-entrenched and operable.

Moving forward, however, watch for the trend to reverse and for PL share to increase. The reasons for this forecast are as follows:

- As evidenced by the Sobey announcement, all grocers are going to sharpen their private label programs across the country. Now that management change seems to have subsided at Loblaw, their efforts are likely to be refocused on PL. In addition, while Wal-Mart's PL efforts in Canada are not yet very strong, they are more focused in the US. It is reasonable to assume that, once they get their Supercentres growing in Canada, they will increase their PL emphasis here, as in the US. In other words, the positives of PL are going to drive further growth and the programs will become more sophisticated.
- National brands are staving off PL by reducing price gaps. In other words, they are not building brand equity, they are fighting on price, which is not a long term strategy for growth. Most academic research shows this is a low return on investment. However, Ad Age April 12 on the other hand, contains research that shows leading manufacturers such as Kraft, Kellogg and P&G are among manufacturers holding their own with PL by emphasizing the value of their brands in ways beyond price. The Ad Age article goes on to say that marketers are more likely to succeed against PL through improved products or marketing better aimed at consumer segments, retailers and localities prone to switching to

PL. About 80% of package players in the past year, according to Ad Age, have assigned executives specifically to combat PL.

The bottom line is that brand marketers need to win back consumers with quality and added product merits. This is a tall order and one that only the top food manufacturing companies will be able to deliver on. Looking to the next few years, watch for private label's market share to solidify and begin to slowly increase. Going back to a Nielsen share ranking of 20% within the next five years is likely.

This has ramifications for the entire food chain in Canada. It means that manufacturers of PL products will see a growing market and opportunities. National brand manufacturers will need to devote increased investment dollars into product improvement and development. It also means that national brand manufactures will continue to see entrenched and more sophisticated PL competition. This, in turn, means that retailer leverage will continue to grow in terms of shelf space allocation, merchandising and pricing. Finally, it means that in addition to Wal-Mart, another factor will be at work keeping Canadian food price inflation in line.

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