

Whole Foods Market – To Be or B2B

by Samuel Sen for Professor Linda Bailey (Fall 2001)

Jeff looked at his watch. It was Monday and he knew he would have to leave for home soon from the office. He had been spending a lot of time working on Whole Foods Market's (WFM's) B2B strategy and many key questions still remained unanswered. WFM's CIO, Mike Clifford had assigned him an urgent B2B project on short notice and Jeff was running out of time.

Business

WFM based in Austin, Texas, is the largest chain of natural and organic food supermarkets. The mission of WFM is to improve the health, well-being and healing of both people and the planet.

At the end of fiscal 2000, the company had \$1.8 billion in sales and operated 117 stores in 22 states. Each store averaged 27,000 square feet and \$17 million in annual sales. The company employed around 18,500 people, 15,400 of them full time employees¹. The key financials of WFM are provided in [Exhibit 1](#).

The company opened its first store in Austin in 1980; between 1991 and 2000 WFM witnessed a CAGR in sales of 39%. A large part of the growth is attributed to the acquisition of regional organic supermarket chains.

The natural products offered by the company include:

- Natural and organic foods and beverages
- Dietary supplements
- Natural personal care products
- Natural household goods
- Educational products

Business Process

WFM has 131 retail locations. Stores are spread over 8 regions: Northern Pacific (NP), Southern Pacific (SP), Southwest (SW), Mid West (MW), North East (NE), Mid Atlantic (MA) and the South (SO).

Typically, WFM established its initial presence by making acquisitions in each region. The company then worked slowly at converting the existing store brand name into Whole Foods. Thus, in some regions, WFM stores retain the name of the acquired chain.

Each region operates fairly independently running their marketing and promotions.

"WFM does not have a standard store design. Instead, each store's design is customized to fit the size and configuration of the particular location and community in which it is located" (from WFM annual report for FYE September 24, 2001).

Each store manages its own purchasing and stocking and has about 20,000 SKUs. Stores are supplied either directly through third-party suppliers or through WFM's own warehouses. Third-party suppliers are used mainly to provide fresh produce whereas WFM's warehouses stock and supply private label and non-perishable items.

WFM has about 10,000 suppliers, the bulk of them being small regional companies or individuals. There are very few large national suppliers that control any sizeable part of the company's purchases. Buyers, who visually monitor inventory levels on a continuous basis, do purchasing at the store level.

The WFM culture is one of entrepreneurship and fierce independence. The company promotes individual decision-making and also provides considerable opportunities to individuals or local management to run their own businesses. Business units are empowered to make most of the operating decisions required to run their units. The culture is also very informal as reflected in the casual and friendly atmosphere of the company's offices. The company values the balanced lifestyle of its employees and rarely requires overtime hours.

Technology

WFM uses a central financial management and accounting system from Peoplesoft. This system is available to all accounting personnel in the stores, warehouses and regional offices. The system consolidates the company's financial reporting, and makes all vendor payments. Currently, Peoplesoft is the only enterprise-wide system used at WFM.

Stores have a stand-alone Point of Sale system called RBX. This system is used to scan and record product sales and also maintains the item master with the latest product prices. The POS system allows store managers to monitor what has been sold. However, there is no central inventory system at the store level for tracking which items have been purchased. Buyers order new products largely by visual inspection (or physical count). Most orders are placed by phone and faxed, though some stores have MSI machines, which are handheld instruments that relay orders through a modem. Stores load sales and purchase information through a custom made application onto Peoplesoft. Peoplesoft does not keep track of item-wise inventory at a store level. As a result, physical inventory levels are not tracked at the store level.

WFM has seven company-owned distribution centers. Three of them run an application called EXE which tracks inventory at the distribution center. The other four run their own legacy software applications for inventory--a result of acquisition.

Five of the eight regional centers also have a system called CIX, which is a product master database for the region. It provides a regional view of the RBX product master. The data variables, however, are different in each of the regions. For example, one region uses 18 digits for unique tracking of UPC codes. The others may use the standard of 13 or 14 digits. The MA and SO regions do not use CIX and use their own application. Book value currently prohibits replacement.

IS organization

The IS organization led by Mike Clifford, CIO, has a matrix structure. Each region has an IS coordinator who reports to the business unit as well as to the CIO. At the head office, WFM has five groups reporting to the CIO ([Exhibit 2](#)):

- Strategy & Planning group
- National Infrastructure Team
- Supply Chain Automation Team
- Business Systems Team
- Retail System Team

The director of each of the five head office groups has a business partner with whom they work (e.g., the Supply Chain Automation Team works with the Vice President of Purchasing). There are around 80 people working at a national level in IS. The regional IS coordinators typically have 6-8 people reporting to them.

Requests for new technology support stem from the businesses. IS planning is done on a quarterly basis where directors plan projects with their business partners. The regional coordinators are responsible for the day-to-day support of the businesses. The IS structure, like the rest of WFM, is

decentralized with operational responsibility residing at the regional level. Past efforts at centralization have not been very effective due to WFM's entrepreneurial culture.

Large implementations in the recent past

The company had decided a few years ago to install an ERP system. They had chosen Peoplesoft as the platform and had utilized the services of a large big five consulting firm. However, they faced major implementation issues with Peoplesoft. The project took longer to implement than originally envisaged. This left a very bad feeling within WFM about large-scale implementations as being not only time-intensive but also very costly. The company actually disengaged the consulting firm prior to completion.

B2B initiative

While the advantages to B2B may be obvious with WFM's 10,000 suppliers, CIO Mike Clifford was not convinced. Adopting any system always comes at a cost and would the cost justify the benefits of a new system? According to Mike, B2B could potentially reduce purchasing costs by 2% on average but what would be the cost of implementing such a system. To further study B2B applications for WFM, Mike called on Jeff Zon, Director of IS.

Jeff plunged into a study of B2B implementation at WFM. Jeff knew that any B2B effort would need to have the following implications for WFM:

- Build capabilities within WFM IT. In the past, all programming and infrastructure projects were implemented by a patchwork of consulting organizations.
- Develop a shopping list of B2B products, which could then be evaluated for their suitability for WFM.

As Jeff studied the fascinating world of B2B, he knew he had to answer key strategic questions:

- Should they build a B2B system or purchase a shrink wrap (packaged) solution?
- Should they hire a consultant or conduct the study internally?
- Should they implement on a company wide basis or begin with a small pilot program and progressively implement site by site?
- Should they look at implementing all suppliers to a store or a subset of suppliers?
- Organizational structure...?

Build vs. Buy

After a few weeks of research, Jeff concluded that there were 2 broad ways for implementing B2B-- WFM could either become a member of a B2B exchange or develop their own B2B system tied to its own suppliers. The second approach seemed to be more applicable as there were no credible B2B exchanges in the grocery industry.

In building their own B2B system, WFM had basically 3 options:

- [Shrink-wrap Software](#)
- [Electronic Data Interchange \(EDI\)](#)
- [Custom Application](#)

Shrink-wrap Software

Jeff was aware of several vendors selling B2B software. A few of them were Ipnnet and Bak-Tek. Both these vendors offered an ASP model where they would also host the application.

Using shrink-wrap software would cut down the development effort. However, most of the software also required that the suppliers have certain installations on their IS. The fee structure was quite economical to WFM--it involved a small upfront (or onetime) license fee and a monthly usage fee. Total cost of ownership was expected to be under \$100,000 (indicative). Most applications also collected a monthly fee from the suppliers. The investment involved in this option was not very large and it also had the advantage of offering a ready-made solution from vendors experienced in the field. WFM could choose vendors who had a proven track record in the industry and who would be able to deliver a time tested robust solution.

Electronic Data Interchange (EDI)

EDI involved exchanging information between suppliers and WFM in standard EDI formats, over secure Value Added Networks (VANs). The installation of EDI for WFM would be quite easy through established EDI vendors. There was also a perception that EDI was more secure as it operated over proprietary networks. EDI, however, also required smaller suppliers to have EDI-compatible information systems, which would ensure that they could communicate order information between WFM and themselves. In addition EDI had the following characteristics:

- It cost about 25 cents for 1000 characters--each order would be around 1000 characters.
- Both WFM and the supplier would be charged by the EDI service provider.
- Suppliers would need to be connected to the VAN to receive EDI messages.

A few of WFM's suppliers were already using EDI. These suppliers insisted that WFM become a part of their VAN in order to transact with them. So far, WFM had resisted joining their VANs. The EDI option would generally cost more than the shrink wrap solution. However, the EDI solution would provide a very high level of security. Security was important to WFM not only for itself but also to provide comfort to its suppliers. With the number of Internet frauds increasing daily, this solution would definitely be attractive to any security conscious organization. A lot of large organizations did not mind paying the extra cost of EDI in exchange for the security benefits.

Custom Application

Jeff figured that building an XML and email based B2B system would be quite simple for WFM. It would involve employing a developer and purchasing some hardware and software. A simple email-based system could be developed where a purchase order could be generated by WFM and sent to the supplier via e-mail. The supplier, upon receipt of the email would accept the purchase order and then fill out an invoice form (which could be a standard form attached to the email) and return it to WFM. This standard invoice form would then be integrated with WFM's financial system.

In this method, the entire supplier needed was email access, which was fairly common even among smaller suppliers.

The other advantage of building in-house is that it would build B2B capabilities and also allow the IS team to experiment with several different new products while building the system. A homegrown solution would probably cost less than \$ 100,000 (indicative) as well.

There remained several pitfalls, however, to this approach. The first was the question of how robust of an application could the IS team develop? While developing a homegrown solution would not be difficult, could it compare with that of other vendors who have already developed and tested robust systems over time? In a way, this approach was also like "re-inventing the wheel." Second, would this method be cheaper than existing off-the-shelf solutions? Third, how much security could WFM achieve in such an application given that information was being transmitted over email.

Using Consultants

Jeff wondered whether he should call in experienced B2B consultants to help them in understanding the B2B opportunities. The advantage would be that consultants would already have experience in the B2B area and would be able to arrive at the best solution without much experimentation. However,

hiring a consultant would be expensive. In addition, employing a consultant would mean that the WFM team might not get enough hands on experience in scouting the B2B marketplace.

Implementation Methodology

Jeff wondered what kind of implementation methodology WFM should follow. After developing the initial application, Jeff could either test it on a small number of stores or actually implement nationwide with all the stores at one time. The "Big Bang" theory had been successful in a few instances where there was a burning need for revolutionary change. Also, the big bang approach would ensure that everyone was on board at the same time. Running two simultaneous systems was potentially dangerous as human tendency was to resist change and criticize the new system.

In addition, Jeff also needed to focus on which suppliers to include in the B2B implementation. WFM's suppliers clearly fell into categories. The smallest category was large nationwide suppliers. These were sophisticated companies, some of whom had their own EDI systems. These companies had already been asking WFM to take part in their EDI. This of course came at a cost to WFM. A majority of the suppliers, however, were smaller companies who had only a basic technology infrastructure e.g. PCs connected to the Internet, typically through dial up. And then, of course, there were really small suppliers who did not have any computing facilities whatsoever.

Organizational Structure

Jeff wondered who should really be on the B2B implementation team from WFM's side. Should the team include a few of the IS regional managers? Should the team include the buyers from the stores? Should there be a steering committee of regional managers with only central IS people doing the development? Should they pass on the costs to their suppliers to use the shrink-wrap and EDI options?

With all these choices, Jeff felt that he had more questions than answers. As he packed up for the day, his closing thoughts as he left the office were on the final answer. He knew there would be much ambiguity through the entire process. At some stage, however, he would need to cut through the ambiguity and make some difficult decisions.

Exhibit 1

Key Financial Highlights

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	2001	2000	1999
Sales	2,237,231	1,838,630	1,492,519
Cost of goods sold	1,482,477	1,205,096	985,000
Gross Profit	789,784	633,534	507,519
Net Income (Loss)	67,880	(4,831)	42,155
Total Assets	829,171	760,399	655,463
Accounts Payable	50,468	49,985	45,829

Exhibit 2

