Different Is Good: FreshDirect Redefines the NYC Grocery Landscape

https://www.freshdirect.com/browse.jsp?id=about_overview

For an example of the relationship between technology and strategic positioning, consider FreshDirect. The New York City–based grocery firm focused on the two most pressing problems for Big Apple shoppers: selection is limited and prices are high. Both problems are a function of the high cost of real estate in New York. The solution? Use technology to craft an ultra-efficient model that makes an end-run around stores.

The firm's "storefront" is a Web site offering one-click menus, semi-prepared specials like "meals in four minutes," and the ability to pull up prior grocery lists for fast reorders—all features that appeal to the time-strapped Manhattanites who were the firm's first customers. (The Web's not the only channel to reach customers—the firm's iPhone app was responsible for 2.5 percent of sales just weeks after launch.) R. M. Schneiderman, "FreshDirect Goes to Greenwich," *Wall Street Journal*, April 6, 2010. Next-day deliveries are from a vast warehouse the size of five football fields located in a lower-rent industrial area of Queens. At that size, the firm can offer a fresh goods selection that's over five times larger than local supermarkets. Area shoppers—many of whom don't have cars or are keen to avoid the traffic-snarled streets of the city—were quick to embrace the model. The service is now so popular that apartment buildings in New York have begun to redesign common areas to include secure freezers that can accept FreshDirect deliveries, even when customers aren't there. L. Croghan, "Food Latest Luxury Lure," *New York Daily News*, March 12, 2006.

The FreshDirect model crushes costs that plague traditional grocers. Worker shifts are highly efficient, avoiding the downtime lulls and busy rush hour spikes of storefronts. The result? Labor costs that are 60 percent lower than at traditional grocers. FreshDirect buys and prepares what it sells, leading to less waste, an advantage that the firm claims is "worth 5 percentage points of total revenue in terms of savings." P. Fox, "Interview with FreshDirect Co-Founder Jason Ackerman," Bloomberg Television, June 17, 2009. Overall perishable inventory at FreshDirect turns 197 times a year versus 40 times a year at traditional grocers.E. Schonfeld, "The Big Cheese of Online Grocers Joe Fedele's Inventory-Turning Ideas May Make FreshDirect the First Big Web Supermarket to Find Profits," *Business 2.0*, January 1, 2004. Higher **inventory turns** mean the firm is selling product faster, so it collects money quicker than its rivals do. And those goods are fresher since they've been in stock for less time, too. Consider that while the average grocer may have seven to nine days of seafood inventory, FreshDirect's seafood stock turns each day. Stock is typically purchased direct from the docks to fulfil orders placed less than twenty-four hours earlier.T. Laseter, B. Berg, and M. Turner, "What FreshDirect Learned from Dell," *Strategy+Business*, February 12, 2003.

Artificial intelligence software, coupled with some seven miles of fiber-optic cables linking systems and sensors, supports everything from baking the perfect baguette to verifying orders with 99.9 percent accuracy.J. Black, "Can FreshDirect Bring Home the Bacon?" *BusinessWeek*, September 24, 2002; S. Sieber and J. Mitchell, "FreshDirect: Online Grocery that Actually Delivers!" *IESE Insight*, 2007. Since it lacks the money-sucking open-air refrigerators of the competition, the firm even saves big on energy (instead, staff bundle up for shifts in climate-controlled cold rooms tailored to the specific needs of dairy, deli, and produce). And a new initiative uses recycled biodiesel fuel to cut down on delivery costs.

FreshDirect buys directly from suppliers, eliminating middlemen wherever possible. The firm also offers suppliers several benefits beyond traditional grocers, all in exchange for more favorable terms. These include offering to carry a greater selection of supplier products while eliminating the "slotting fees" (payments by suppliers for prime shelf space) common in traditional retail, cobranding products to help establish and strengthen supplier brand, paying partners in days rather than weeks, and sharing data to help improve supplier sales and operations. Add all these advantages together and the firm's big, fresh selection is offered at prices that can undercut the competition by as much as 35 percent.H. Green, "FreshDirect," *BusinessWeek*, November 24, 2003. And FreshDirect does it all with margins in the range of 20 percent (to as high as 45 percent on many semiprepared meals), easily dwarfing the razor-thin 1 percent margins earned by traditional grocers.S. Sieber and J. Mitchell, "FreshDirect: Online Grocery that Actually Delivers!" *IESE Insight*, 2007; D. Kirkpatrick, "The Online Grocer Version 2.0," *Fortune*, November 25, 2002; P. Fox, "Interview with FreshDirect Co-Founder Jason Ackerman," Bloomberg Television, June 17, 2009.

Today, FreshDirect serves a base of some 600,000 paying customers. That's a population roughly the size of metro-Boston, serviced by a single grocer with no physical store. The privately held firm has been solidly profitable for several years.

Even in recession-plagued 2009, the firm's CEO described 2009 earnings as "pretty spectacular," P. Fox, "Interview with FreshDirect Co-Founder Jason Ackerman," Bloomberg Television, June 17, 2009. while 2010 revenues are estimated to grow to roughly $300 million.R. M. Schneiderman, "FreshDirect Goes to Greenwich," *Wall Street Journal*, April 6, 2010.

Technology is critical to the FreshDirect model, but it's the collective impact of the firm's differences when compared to rivals, this tech-enabled strategic positioning, that delivers success. Operating for more than half a decade, the firm has also built up a set of strategic assets that not only address specific needs of a market but are now extremely difficult for any upstart to compete against. Traditional grocers can't fully copy the firm's delivery business because this would leave them **straddling** two markets (low-margin storefront and high-margin delivery), unable to gain optimal benefits from either. Entry costs for would-be competitors are also high (the firm spent over $75 million building infrastructure before it could serve a single customer), and the firm's complex and highly customized software, which handles everything from delivery scheduling to orchestrating the preparation of thousands of recipes, continues to be refined and improved each year.C. Valerio, "Interview with FreshDirect Co-Founder Jason Ackerman," *Venture*, Bloomberg Television, September 18, 2009. On top of all this comes years of customer data used to further refine processes, speed reorders, and make helpful recommendations.

Competing against a firm with such a strong and tough-to-match strategic position can be brutal. Just five years after launch there were one-third fewer supermarkets in New York City than when FreshDirect first opened for business.R. Shulman, "Groceries Grow Elusive for Many in New York City," *Washington Post*, February 19, 2008.