

Instructions and Explanation - Rural Grocery Profit Simulator

The number one consideration when opening a small-town rural grocery store is, can we attract enough business to be profitable? Positive cash flow is essential, even for non-profits or cooperative stores, as funds will be needed for repairs to building and equipment, technology upgrades, and replacement of equipment as it wears out or becomes obsolete.

Estimating Market Size

The first step in analyzing profit potential will be to determine how much revenue we can create. This starts by looking at the size of our market and making some assumptions and estimates with regard to spending patterns. We will consider the population of our own town (the town where the store will be located), then add to that the rural population that falls within the store's market area (the rural population for whom our store is closest), and finally add the population of the other towns in our market area.

To begin the analysis, we will first enter the basic information about our store and town. Next, to determine the geographic footprint of our market we will look for the closest stores in each direction surrounding our location. This is the first step in our Rural Grocery Profit Simulator. We will then assume that the residents who live closer to our store will be potential customers of our store, and those that live closer to the neighboring store will not be considered potential customers. For example, to the west the nearest store is 10 miles away. Splitting the distance in half we assume that the residents within 5 miles of our location are potential customers. Those more than 5 miles from the store are assumed to be customers of the store in the neighboring town.

In our exercise you will enter the distance to the closest store in each direction (north, south, east, west). It is possible that there could be more than one store in one direction, just as it is possible there could be no stores in another direction. If there is more than one store in a quadrant, simply use the closest store in your calculation. If there is no store in a quadrant, determine the closest store in any direction and enter that distance in the space provided.

Next, we will develop an estimate of rural residents who reside in our market area. We will do this by calculating the percentage of the county that our market represents. For example, if the county were 100 square miles and our market is 20 square miles, we can see that our market will represent 20% of the county. The population and size of your county should be easy to find in Wikipedia or at the county's website. Enter these where requested and the program will calculate the percentage of the county that is within our market.

As we continue, we will enter the names and population of all towns in the county, as follows:

- List all towns in the county and their population. Check the appropriate box for the towns that are in your market. To add another town, select the "Add new town" button.
- If a town is only partially within the county, estimate the population living within the county and enter this amount next to the town name.
- If a town is in your market but outside of the county, list this town and select "In Market" and "Outside County".

The last step in estimating the market size will be to consider how our market residents will use the store. We realize that most residents will not purchase all of their groceries here, and some will buy very little in town. We also realize that those who live close to the store are more likely to shop here than

those who live farther away. To account for this we will look at residents of the town, residents of the other towns in our market, and rural residents within our market. Each of these will have a percentage of shoppers who will use our store as their primary grocery, others who use the store as a secondary option, and some who visit only rarely.

To begin we have assigned default values to all of these, but you are free to change them as you see fit, by double-clicking on the field you wish to change. For those who live in town, we have assumed that 50% will do their Primary shopping in our store, 40% will use the store as a Secondary option, and 10% will shop here only Rarely. For rural residents and those who live in other towns in our market, we have assumed fewer customers will consider this to be their Primary store. If you make any adjustments to these percentages, keep in mind that the percentages must add across to 100 for each category (your town, Rural Market, and Towns in Market).

After completing these steps, you will have accounted for each resident within your market area. Each will be recognized as being either a regular shopper, a sometimes shopper, or a rare shopper. We are now ready to take a look at revenue.

Estimating Revenue

The first step in estimating revenue is to determine per capita spending on groceries. Using data from two reputable sources we have calculated this figure and there is nothing for you to do in this step. You then will have the opportunity to adjust prices to current levels. For example, if the per-capita spending shown here is for calendar year 2022 and it is now 2024, you may want to increase per-capita spending by a certain percentage. You can estimate a percentage based on your general knowledge of price increases during this time, or you can go online and search for the data. One location where you can obtain a twelve-month inflation figure is at the Bureau of Labor Statistics website (link included below). Be sure you look for the “Food at Home” figure. <https://www.bls.gov/news.release/cpi.nr0.htm>

You may also want to make a second adjustment to per-capita grocery spending, this time based on your location. We provide a link to Missouri Economic Research and Information Center where you will find a map, updated quarterly, where each state is assigned an overall cost index. A little farther down the page you will find a chart showing a cost index for several spend categories. You will of course want to look for your state’s index in the Grocery category. The link is: <https://meric.mo.gov/data/cost-living-data-series>. Enter this figure in the appropriate field.

Earlier we identified our Primary, Secondary, and Rare shoppers. We identified a certain percentage of residents as Primary shoppers, but we realize even the Primary shoppers, on average, will not spend all of their grocery dollars at our store. Therefore, we need to estimate the percentage of groceries these customers will purchase in our store. We have pre-filled this field and made an initial assumption that Primary shoppers will purchase 60% of their groceries at our store. We have then estimated that Secondary shoppers will spend 25% of their grocery dollars here, and Rare shoppers 5%. Again, these percentages can be adjusted as you see fit. The three percentages do not need to add to 100% in this case.

Estimating Expense

Since one of the largest expenses of grocery store operations will be related to the purchase or rental of a physical location, we begin by identifying ownership of the building. The program offers three possible ownership models. Scenario 1 looks at costs (depreciation) when the building housing the store is

owned by the business. Scenario 2 is when the building is not owned by the grocery business, with monthly rental paid to the owner.

Scenario 3 considers a common practice where the building is owned by a related party holding company that is typically owned by the same individual(s) who own the store. In this instance the grocery will typically pay monthly rent to the holding company, but the rent charged may not always be market rate. Thus, it may be a more accurate reflection of financial results to calculate depreciation as if the grocery owned the building. Choosing Scenario 3 will route to a depreciation calculation. Alternatively, if you believe rent expense is a more accurate reflection of financial performance in your situation you may choose Scenario 2.

Once you have selected the appropriate scenario you will be asked to enter amounts spent on various depreciable assets. Line 1 will ask about either the cost of the building if owned, or Leasehold Improvements if rented. The remaining nine lines will be the same regardless of ownership. You will enter (estimated) amounts to be spent on various improvements or equipment, and the program will calculate depreciation based on typical "Useful Lives" of the particular asset class. You can override the useful lives used if necessary. You may also add Miscellaneous Assets in the spaces provided at the bottom of the list.

Next you will be asked to add rental costs either for the store itself (if applicable), or for other structures or equipment that may be leased. Monthly rent is entered, and the program calculates annual rent.

Due to the cash requirements that are typical when opening a grocery store, it is likely that financing will be needed. In the next step you are asked to enter anticipated loan amounts and interest rates.

Finally, we look at the other expense categories that will impact bottom line. We set the Gross Margin to a default value of 25%, meaning Cost of Good Sold defaults to 75% of revenue. This figure, and all of those that follow, can be adjusted by the user. Salaries and Operating Expenses are entered as a percentage of total revenue based on peer averages. Officer Compensation defaults to a conservative annual value of \$40,000.

To Keep in Mind

If the store is close to a larger town that has a full-service grocery or has a Wal-Mart or other superstore, these factors can reduce the percentage of residents shopping at the local store and therefore results of this exercise are less likely to be accurate. Such factors can be addressed by, for example, reducing the market area of the quadrant or quadrants near to the store in question. Or you could reduce the percentage of Primary shoppers for your store.

This program does not take into account the purchases made at your store by individuals who live outside of your market area. Generally, it is expected that these sales will not be a large percentage of sales and will not significantly impact results. Regardless, be aware of this caveat.

The results of this model are based on a number of assumptions and estimates. While in many instances the results can help to determine the likelihood of success of a new grocery store, actual outcomes may significantly differ from those calculated here. It is therefore possible the results may be reasonably accurate for one community and not as accurate for another. There are a number of default values in the program that can be changed by the user. This allows for experimentation by users as they compare results based on different entry values.