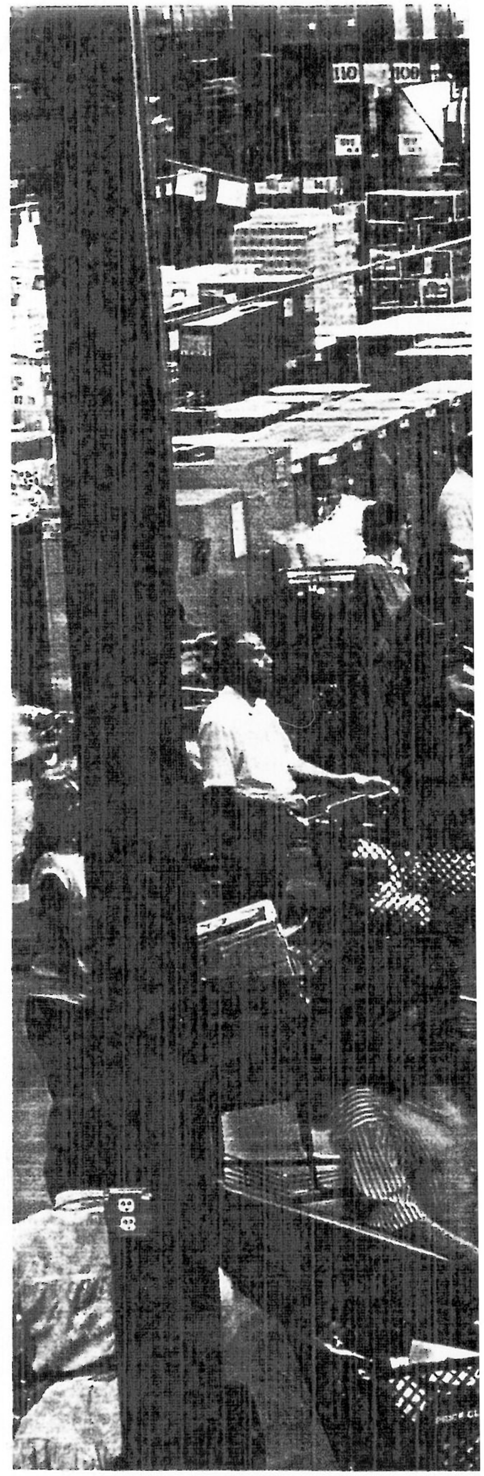
They Get It For You Wholesale

Sol Price, left, and his son Robert at a warehouse on Morena Blvd. in San Diego – the first Price Club.



Sol Price and his warehouse clubs have sparked a revolution in the retail trade.

By Cathryn Jakobson

LIKE A GIANT MATCHBOX LYING ON its side, the warehouse in Burbank stretches long, low and white toward the rough foothills of the San Gabriel Mountains. It stands in a neigborhood of body shops and small factories, its identity announced only by a small, red-lettered sign: Price Club.

The fluorescent lights are wildly bright inside a cavernous space the size of two football fields. It is hot, crowded and noisy. Demonstrators hawk toasted garlic bread and pepperoni-stuffed calzone. Children scream and hundreds of oversized carts hurtle past merchandise stacked on steel shelves 18 feet high. Long lines stretch toward 35 checkout counters. The selection is limited — types of refrigerators, one brand of garbage — and the customers invited to join the club pay an annual $25 membership fee.

So what draws the crowds? Bargains. With modest markup above cost, the club caters every shopper's dream of "getting it wholesa

Some 10,000 people a day — the owners of b nesses as well as bargain-hunting families — upon Reebok Newport Classic athletic shoes $32.99 instead of $46.95, the suggested retail p or a combination Goldstar color television an videocasette tape recorder, $399 instead of $5 a discount store.

Life imitates television. The comparison sh pers of "The Price Is Right" meet the impulse shoppers of "Sale of the Century." A woman w ing a self-satisfied grin loads her cart with six reproduction Louis XIV dining-room chairs w needlepoint seats. "I've been looking for these

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OTOGRAPHS BY BILL BALLENBERG

years," she gloats, "and here they are, for $125 each." Another woman says, with a sigh: "I stand in the aisles anticipating turns in my life. I think, 'I might someday *need* a snowblower.' "

Price Club, founded in 1976, is the pioneer of the burgeoning warehouse business. "It's the greatest revolution in retailing in the past 10 years," says Stephen F. Mandel Jr., a retail-business analyst for Goldman, Sachs & Company. With more than 40 warehouses in the United States and Canada, Price Club leads the pack; in the fiscal year ended last August, the company reaped profits of about $95 million on more than $4 billion in sales. But the competition — from such warehouse operations as Costco — is growing.

Sol Price, the feisty, 72-year-old founder of the empire that bears his name, occupies an office overlooking the San Diego harbor. The furnishings include a Naugahyde couch, but that comes as no

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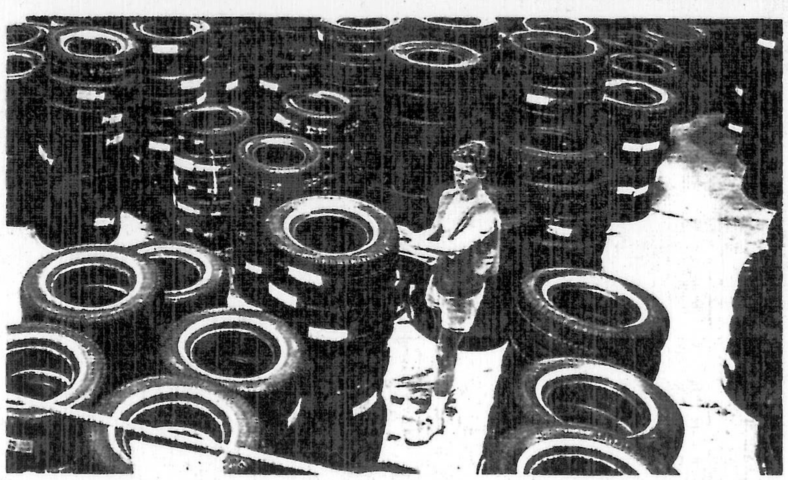

Above, a warehouse in Fairfax, Va.; Price Club is expanding its East Coast operations.

Left, tire display at the warehouse in Fairfax.

PRICE CLUB

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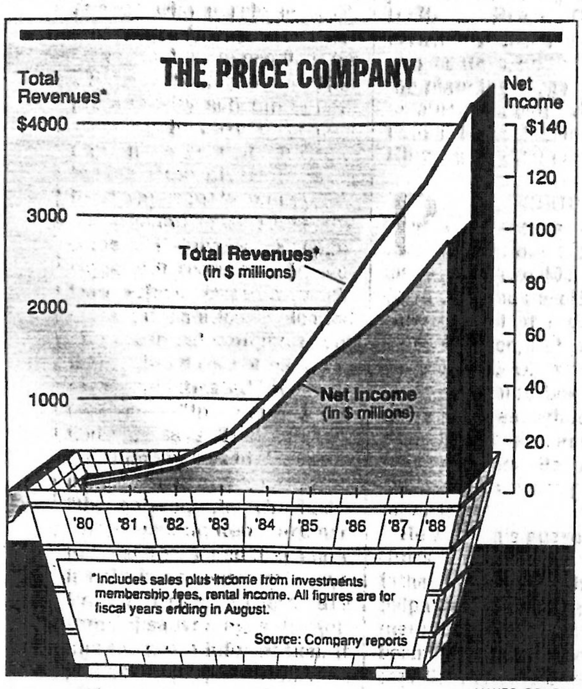

HAYES COHEN

surprise. Price Club management is frugal down to its socks. The company's annual report is a slim white volume with no photographs. It is mailed out with the fourth-quarter report and the proxy statement, to save money on postage. "The richer people are," says Sol Price, referring to some of Price Club's members, "the more they like to save." Price estimates his personal wealth at $250 million to $300 million.

His father, a manufacturer of women's coats and suits, moved from New York to San Diego when Sol Price was 13. Price earned a law degree from the University of Southern California and practiced law until he was 39. In 1954, he and several partners raised $50,000 and launched Fedmart; a year later he abandoned the practice of law for retailing.

Fedmart, which was set up for Government employees, offered a wide range of products — small appliances, housewares, liquor, clothing — at a deep discount and charged a membership fee, $2 a family, to add a sense of exclusivity. Manufacturers and local merchants were outraged because the store was ignoring the fair-trade laws that established a minimum price at which most goods could be sold. Newspapers refused to carry Fedmart's advertisements; the

refused its application for membership.

"Fair-trade laws were enacted in the depth of the Depression," Sol Price says. "They were a way for Congress to protect merchants — so they would know they wouldn't be undercut. In the 50's there was no longer a reason to have the laws, except that big department stores liked them."

After World War II, the Two Guys stores in New Jersey started selling appliances at deep discount; Korvettes followed suit with a wider range of merchandise. Manufacturers, eager to increase volume, supplied discounters like Fedmart and Korvettes in spite of the fair-trade laws (which stayed on the books in some states until 1975, when they were repealed by an act of Congress).

Fedmart's sales for the first year were $4.5 million, more than four times greater than expected. By 1974, Fedmart had become a 45-store chain with sales of more than $300 million.

The next year, Hugo Mann, a German retail magnate, bought two-thirds of Fedmart for more than $20 million. Sol Price stayed on as chief executive, expecting to participate in the company's growth. "There was so much romance to it," he says. "I thought of that money, all the expansion that would happen

Less than a year later, Mann sent Price packing. Price's sons — Robert, 33, and a senior vice president, and Laurence, 29, who was in charge of purchasing — quit their jobs. Within seven years, Fedmart, suffering heavy losses, was liquidated.

Price was 59 when he was ousted from Fedmart. He took to strolling through San Diego, chatting with grocery-store owners, restaurateurs, the people who ran newspaper and candy stands. He discovered a gap in the retail marketing network, just waiting to be filled.

At the time, owners of small businesses could either deal with four or five wholesalers or they could go to cash-and-carry operations with limited stock and pay higher prices. Price was convinced that, if he could keep prices down and yet put everything a small-business customer needed under one roof, he would have a winning formula. "It was just one of those great ideas that no one had latched on to," says Stephen Mandel.

PRICE INVESTED about $800,000 of his money and raised $1 million from businessmen in the San Diego area. He also sold $500,000 worth of stock to Fedmart employees who joined him in his new venture, the Price Company. Robert Price was appointed president and chief executive officer. Larry Price, unhappy about reporting to his brother, bowed out.

To qualify for membership in Price Club, customers had to show proof of business activity such as a professional license or a resale permit. The proprietor of a bar could shop there for cigarettes to stock his shelves and toilet paper to stock the bathrooms. (Price Club has no way of knowing whether businesses buy for resale or for their own use.) A doctor could buy office stationery. So could a housewife doubling as an interior decorator. Price duplicated the membership concept he started at Fedmart, but he increased the fee.

"We thought of it as a sort of speak-easy," says Robert Price. "We tried to create a mystique." Price Club opened on the edge of San Diego in 1976. The first year was grim, with losses of $750,000 on sales of $16 million.

"We couldn't figure out what had gone wrong," says Sol Price. "Was it the membership fee? Did we have the

A customer offered a solution: Let Government employees join the party. In short order, invitations were also extended to utility and hospital employees and to the members of certain credit unions and savings deposit clubs — the kind of people unlikely to bounce checks. But Price Club would not accept credit cards. "It's against my religion for people to go into debt to shop," says Sol Price. Eventually, the retail customers also had to pay a membership fee.

"It was unimaginable, this idea that you could charge people to shop," says Michael Exstein, vice president of equity research for Shearson Lehman Hutton. But it worked. Retail customers flocked in. Today they account for 35 percent of sales volume.

Price Club went public in 1980. Its stock hit a high of 55¾ in 1986, dropped to 23½ after the 1987 crash and now trades at about 42.

MY FATHER-IN-law is dangerous in there," says one club member. "He buys things he'll never use up, like 12 rolls of film, a case of motor oil, 10 rolls of masking tape. My mother-in-law tries to keep him out of Price Club, as a matter of policy."

Why do people, once inside the warehouse doors, experi-

'IF THE DEPARTMENT STORE IS THE WIFE, WE ARE THE MISTRESS.'

ence a dry-mouthed, glassy-eyed desire to buy in quantity? Why do members spend an average of $125 each time they shop? "Finding a bargain is exciting," says Avijit Ghosh, associate professor of marketing at New York University's Leonard N. Stern School of Business. "It makes you feel smart, like you know something someone else doesn't know." People who "save" $100 on a VCR end up spending it on videotapes.

The urge to shop wholesale cuts across cultural and economic boundaries. In the Burbank Price Club parking lot, BMW's and Mercedes-Benzes are parked alongside

trucks.

Traditionally, says John A. Quelch, a professor at the Harvard Business School, retail customers choose their stores on the basis of location, a wide assortment of goods, service, ambiance and price. Department stores and specialty stores may offer those advantages, but they charge between 35 percent and 65 percent over manufacturers' prices. That left the door open for the discount stores.

"The early K Marts and Korvettes were very bare bones, very price-oriented," says Avijit Ghosh. But gradually, in an effort to lure department-store customers, discounters added fancy displays and increased their advertising budgets. Large discount chains began marking up their goods 15 to 35 percent.

Enter Price Club with margins of generally less than 10 percent over cost. Its warehouses carry goods that would never be found on the shelves of a K Mart — Courvoisier cognac and Baccarat crystal. And Price Club, unlike such off-price retailers as T. J. Maxx and Marshalls, does not offer unpopular lines of goods, seconds and out-of-season stock.

While the average discounter carries about 50,000 different products, Price Club carries about 3,000. Price buys in great quantity, by the truckload rather than by the gross.

Packaging is outsized, too. Rice comes in 10-pound bags, peanut butter in 32-ounce jars. Smaller items are packaged in "multi-packs" — 12 bottles of apple juice kept snug under a veil of shrink-wrap. Nothing is sold for less than $2.

The formula is clear and simple: High volume at low markup produces profits. Goods turn over more than 20 times a year — about 7 times as often as at K Mart.

EVERY SEVEN DAYS, merchandise worth an average of $2 million moves into each Price Club warehouse. Some manufacturers — especially those in electronics, office equipment and clothing — are at first wary of selling to warehouse clubs for fear of offending regular customers. "If the department store is the wife," says Sol Price, "then we are the mistress. Whenever they can, they try to sell us the second line."

So a portion of Price Club's inventory comes through the

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gray market from foreign distributors who ship American merchandise back to the United States. Price also buys from diverters, third parties who purchase stock from manufacturers and retailers and try to peddle it for whatever they can get. That process adds substantially to the price the warehouse must pay. In the view of Sol Price, buying from diverters is "a hard way to make money."

Merchandise is ordered by some 75 buyers. Keeping track of it requires a Herculean effort. Once a week, sales information is loaded into a central computer, but Price Club does not have the most sophisticated inventory controls. "In our warehouses," says Ted Wallace, the company's chief operating officer on the East Coast, "the only people who know where specific items are are the managers, and they know it only from memory." Says Robert Price: "There are some disadvantages to getting too much information. It just sits on people's desks."

The company makes substantial demands on its 11,000 employees, but there are compensations. The wages and benefits are generous and advancement can be swift — from broom pusher to manager in five years. Efforts to bring in outside managers often backfire. "There's a fairly high mortality rate," says Ted Wallace. "Only about 20 percent have lasted. You have to be initiated slowly into the Price Club culture to be able to work here."

Almost from the beginning, Price has bought, rather than leased, the buildings that become warehouses. The company also buys the land on which to construct its centers. According to Robert Price, at least 25 percent of Price Club's properties — those sites that have land in excess of the club's needs — is acquired by partnerships formed by the Price Company and real-estate entrepreneurs. Price's partners develop the property, find additional tenants and return at least half the rental income to Price Club. The properties owned by Price are carried on its books at more than $400 million.

By setting up shop in out-of-the-way locations, Price pays rock-bottom prices for its real estate. By leasing space to other retailers, Price generates extra revenues — an estimated $9 million a year in 1990 — and increases the flow of shoppers. "I'm not fazed by having potential competitors in a development with us," says Sol Price. "Retailers who say 'no' to this are kind of stupid, because it means that the competitor is going to locate three blocks away and you are not going to get the traffic." Price Club has created a dozen such shopping centers, and more are in the planning stage with such tenants as Levitz Furniture, Longs Drug Stores, Burger King and AMC theaters.

PRICE CLUB HEADquarters is a nondescript, one-story building in San Diego, 10 miles from downtown and the office of the chairman of the board, Sol Price. His son, Robert, the 46-year-old C.E.O., works in a linoleum-floored box of an office just big enough for a desk, a couple of chairs and a set of filing cabinets. He habitually wears slacks and a sports shirt to work.

He keeps his guard up at all times, but especially when his father is around. There is a palpable push and tug between them. "Robert has always been shy and standoffish," says Sol Price. "He needs to be more sensitive to other people." Along with many of the company's other employees, Robert Price has attended Dale Carnegie training seminars; he says they have helped him. But a Wall Street analyst, accustomed to leisurely telephone chats with company officers, complains that Robert Price is still impatient: "He gives you five minutes." These days, another company executive takes analysts' calls.

When he does relax, Robert Price confides that he dropped out of law school at the University of California at Los Angeles after a month and that he dropped out of the Peace Corps after two months. He is about to start his 15th year of piano lessons and would like to practice more, he says wistfully, but he doubts the shareholders would appreciate it.

Sol Price has his own complexities. He often talks about ethics in general, and about his own business ethics in particular. The family's charitable trust has contributed to the San Diego Symphony and the Old Globe Theater, and has donated $2 million to establish a student center at the University of California at San Diego. Yet he is widely known as a man who takes no prisoners, in business or in his personal life.

He has had a long-running feud with his younger son. In 1978, Larry Price returned to the fold and began opening tire-installation centers at Price Club warehouses. He leased the necessary space from the Price Company, and borrowed money to finance the business. By 1985, he had about 20 centers. Three years ago, the company canceled the leases on those centers. Sol Price says his son was not an efficient manager. Larry Price, in turn, calls his father "a control freak" who canceled the leases because he wanted to dictate the relationship between Larry Price and his former wife and their children. Larry Price filed for arbitration in 1985. He was awarded $3.7 million.

With the assistance of Marvin Mitchelson, the well-known divorce lawyer, Larry Price is suing his father for an additional $100 million. Why Mitchelson? "This is not a business dispute, it's a divorce," Larry Price says.

"You do the best you can with your children," says Sol Price. "But you can't go through life eating your heart out because everything does not go perfectly."

THE WAREHOUSE INdustry, with $15 billion in sales this year, is now the fifth-largest form of mass merchandising in the nation, behind supermarkets, discount stores, department stores and drugstores. Price Club has inspired a number of imitators, including Sam's Wholesale Clubs (a division of Wal-Mart with 100 warehouses, primarily in the South and Midwest) and Pace Membership Warehouses (with 40 warehouses throughout the United States).

One company that Price Club perceives as a threat is Costco, co-founded by Jim Sinegal, a former Price Club executive, in 1983. Seattle-based Costco has 50 warehouses and earnings in fiscal 1988 of $14.5 million on sales of about $2 billion. The company has moved beyond Price Club into the vending of fresh meat and seafood; it also has a large produce department. Its warehouses are concentrated on the West Coast, sometimes in Price Club s backyard.

In California, warehouses seem natural. Almost everyone drives and has plenty of storage space at home. Warehouses make less sense where land is expensive and hard to come by, where zoning regulations are fierce, where the traffic is heavy and the home storage space limited. New York City comes to mind.

Price Club made a bid to penetrate the New York marketplace in 1987 by offering to buy a dozen discount stores operated by TSS-Seedman, but the deal fell through. The club does have 14 warehouses in the East, spread thinly from Virginia to Quebec, including one in Edison, N.J., and another in Smithtown, L.I. Yet another is due to open in Babylon, L.I., next spring. Robert Price would like to open 7 to 10 new warehouses a year.

Some Wall Street analysts are dissatisfied with the pace of Price Club's expansion. Last September, the company announced the appointment of Ted Wallace as head of East Coast operations. He will, as Robert Price puts it, "make decisions without sending everything back to San Diego first. That was slowing us down."

AT INGRID'S, A GERman restaurant near Price Club headquarters, Robert Price orders a turkey-and-avocado sandwich and talks about his company's future. He allows that there has been some discussion about accepting credit cards — Costco now issues its own — but no decision has been made.

The larger question, though, is how far the company can go to attract retail customers without alienating its wholesale clientele. Retail customers boost volume, but Price Club believes that wholesale customers are more loyal. "We're still wandering around on the question," he says. "It's under constant review."

Six years ago, Sol Price was stricken with Bell's palsy while in Europe trying to get a good buy on an antique prayer rug. The condition has paralyzed the left side of his face. Price says he will "get out of the loop," step down as chairman of the board next year and pass control of the company to his son Robert, Giles Bateman, the chief financial officer, and Richard M. Libenson, chief operating officer.

"I'm proud of the boys," he says. "I wouldn't like to be Milton Petrie," a reference to the chief executive of Petrie Stores, a large retail chain. "He's got all the money and power, and nobody coming up behind him, ready to take over."

But Price has not departed yet. "Sol still plays a major role," says Stephen Mandel. "Real-estate decisions don't get made without his say-so. He is the person who makes sure that things are done right. He has stature and presence, and no one would dream of standing up to him, because he won't tolerate it."

As usual, Sol Price has the last word: "I'm like a junkie," he says. "I can't quit cold." ∎