What are the secrets of successful retailing and how can retailers survive and prosper in a downturn?

Introduction:

The topic for this White Paper was debated by the KPMG/SPSL Retail Think Tank in October 2007 during a period of increasing pressure on retailers. For Quarter 4 2007, the RTT decided that the outlook was more pessimistic compared to Q3, with downward pressure expected in all three areas considered; Demand, Margins and Costs. This is the first time since the RTT first sat in April 2006 that the members consider that movements in all three drivers will have a negative impact on the overall state of health of UK retail. This is underlined by the latest BRC–KPMG Retail Sales Monitor figures, which show like–for–like growth of just 1% in October, the weakest rise for 11 months. Therefore the issue debated, 'What are the secrets of successful retailing and how can retailers survive and prosper in a downturn?' is considered to be very timely.

Key observations:

- The single most important element of successful retailing is for retailers to know and understand their target customers, how those customers perceive them, what their wants and needs are, and what those customers expect;
- That knowledge needs to be translated into a delivery proposition that encompasses the right product, environment, price/value and service offer;
- The business model must be appropriate to be able to deliver the proposition successfully. This encompasses both the organisational structure and infrastructure and the culture;
- It is the ability of the management culture in a retail organisation to be able to constantly re-evaluate the proposition and the structure that becomes even more critical to a retailers success in a downturn.

What Do We Mean By Successful Retailing and What Differentiates the Winners from the Losers?
The RTT accepts that some elements of successful retailing are extremely obvious; such as strong profitability, growing market share, winning recognition for customer service, value or product; while other elements, perhaps those which underlie the principles by which an organisation works, may be less obvious but are no less vital. In this White Paper the RTT illustrates how these elements fit together to create the climate of success or failure for retailers, mindful that the retail sector is likely to enter a downturn.

1. Know your customer

"The customer is, in a very real sense, a stakeholder in every retailer and, in fact, is the key stakeholder", advises Helen Dickinson from KPMG. Knowing, understanding and responding to your customer is, therefore, the RTT asserts, the single most important mantra in the success factors of winning retailers. In this regard, retailing is no different from any other business; success emanates from delivering what your customers want in a way that is profitable for the business.

The most obvious illustration of the contribution of this customer-focus to retailer success comes by contrasting the consequences of the very different Board appointments made at the top grocery chains in the watershed early 1990s. Many carried on in what was the conventional retail vein of the time, with the appointment of Chief Executives, with buying orientation – putting faith and instilling power in the people responsible for product procurement and price/quantity negotiation. Tesco, in total contrast, through the promotion of Terry (now Sir Terry) Leahy to the Board in 1992 (he became CEO in 1997), began its transition to a 'marketing orientation', building its strategy around really getting to understand its customers and their needs.

The launch of, and on-going commitment to, the Clubcard provides telling evidence of this switch in business focus. Tesco was driven by the desire to gather as much information as possible about the behaviour of its shoppers, harnessing the new found capabilities in EPoS (Electronic Point of Sale) and IT. The "Pile it high; sell it cheap" philosophy of ex-market-stallholder Jack Cohen rapidly gave way to the "Customer is king" mentality. At the time very few would have marked this as a tipping point in British retailing, but hindsight shows us otherwise. Putting the customer at the heart of the business is now accepted as a necessity; 15 years ago in British retailing it was visionary.

Keeping abreast of your customer’s needs on a regular basis is simply not enough now though, particularly as they are so much more knowledgeable than they used to be. The customer and the way he or she relates to individual retailers is evolving continually and the pace of change is ever accelerating. Regular feedback has now been replaced by ongoing,
continuous tracking among leading retailers. Complacency about your customer knowledge is ruinous warns the RTT. There is little loyalty in retailing. If customers don't like what you are selling today and you don't spot it by tomorrow, they'll be voting with their feet the day after. Retailers need to remain on top of the game, putting ever more effort into understanding the continuous changes in their customers' attitudes, desires and behaviour. Sporadic analysis of EPoS data, mystery shopping and holding focus groups with customers was, perhaps, as sophisticated as it got a decade ago. Now, the need to continuously track and understand customers' experiences is a business requisite. The RTT advises that they also need to be acutely aware that segmenting customers in more transient ways, for instance, by lifestyle and by occasion, are just as relevant, if not more so, now than by conventional ways of grouping customers (by socioeconomics etc).

The RTT discussed a number of new trends in consumer behaviour, not least the swelling interest in ethical and green issues (discussed in the RTT's last White Paper; view it at [www.retailthinktank.com](http://www.retailthinktank.com)). It also highlighted another attitudinal trend: "Understanding that the customer wants to be treated with more respect is one of the subtler and yet important recent refinements in the shopper's psyche", commented retail psychologist Tim Denison of SPSL, "Top of the respect agenda is respecting their time. Time is the new money; convenience becomes paramount. Being able to provide easy to reach locations (both bricks and clicks), offer opening hours to suit the modern work–life balance, easy and intuitive navigation around the store/website and quick to pay solutions must all be very carefully considered."

2. The right proposition

An intimate understanding of your customers is a necessary condition of success, the RTT agreed, but it is patently not sufficient in itself. That knowledge needs to be translated into a delivery proposition that encompasses the requisite product, environment, price/value and service offer. The proposition is built under the umbrella of the retailer's brand that serves to provide the "emotional connectivity" with the customer – building affinity, affection and trust, and thereby regular patronage. Ultimately, a proposition that delivers the needs of the customer and identifies with them emotionally through the brand attributes leads to the kind of loyalty and goodwill enjoyed today by only a select few retailers, such as perhaps John Lewis, Tesco and Marks & Spencer.

It's far from true to say, however, that there's a 'one size fits all' solution in terms of the retail proposition; "Look at Sports World/Sports Soccer," comments Paul Clarke of Barclays Retail & Wholesale Sectors. "Despite Mike Ashley upsetting a lot of people in the city, he
does understand his customers. They appreciate the image of it being cheap. It feels cheap. It looks cheap. It is cheap. Not only does that not matter to them, it’s a positive attractor. That is brilliant, because it came at a time when that sector was moving relentlessly upmarket.” However, the RTT believes that it is those retailers who connect with their customers both on a rational basis (product, price/value) and on an emotional level (environment, service, channel, brand) that are invariably examples of successful retailers. Richard Hyman of Verdict Research said; “If you don’t connect with the customer, you don’t sell much. You have to be good at understanding demand – your customers’ demand, which is both explicit and implied.”

Invariably, part of the proposition surrounds price and value, but its role, like every other part of the mix, is always changing. Nick Bubb, of Pali International explains; “People are sated by bargains. They will not buy things in 2007/8 that they don’t need, simply because they’re cheap. Retailers who are successful now and will be successful in a downturn are not necessarily the slash and burn discounters. The rules are changing and it’s foolish sometimes to simply discount in a belief that it will add value. Far better to find exactly what your customers want, which may be items with added perceived value, and then having sourced them, actually add price to match that different perception of value.” The RTT acknowledges that price policy is more about fair pricing than low pricing amongst the leaders. It concludes that there is a considerable psychological cost to retailers if customers discover subsequently that a "bargain" is not the bargain they thought it was when they bought it.

The RTT feel that as customer behaviour is becoming more and more segmented, so there is a growing need to develop multiple formats to their proposition to accommodate the growing disparity. Tesco, yet again, was named as one British success that has achieved this platform, with its various formats – Metro, Express, Extra, – that respond to the various calls of its customers.

3. The right business model
The business model must be right to be able to deliver the retail proposition successfully. In this regard, the RTT refers to aspects of two critical dimensions: i) the organisational structure and infrastructure and ii) its culture.

i) The right organisational structure and infrastructure
RTT members argue that consciously building a structure – and infrastructure – around understanding and developing target customer demand is a good place to start. "Every retailer shares its customers with other retailers, and keeping that in mind should help keep
people focussed. But that's not to say that there is a monopoly on getting the right business model", advises Richard Hyman.

Key to success though is developing an enabling structure that puts customer insight right at the heart of the business; both in a strategic and operational sense. Part of a winning formula is about short decision chains of command. Too much bureaucracy and complexity can strangle the ability to understand and respond quickly enough to the changing needs of the customer. The RTT believes that it is a matter of delivering relevant information to where it is needed in order to satisfy customer demand. Retail is the 'final leg of the relay race' and the interface with the customer its final apotheosis; the moment when that visceral link between the chief executive, the designers, the manufacturers, the teams of buyers, the merchandisers, the marketers, the supply chain, the shop-floor staff and everyone involved is either endorsed or condemned. Too many batten-passing teams, or slow moving team members can impede the speed of delivery and ultimately weaken the linkage between supply and demand.

Collecting, collating, and responding to business information is critical: data must be precise, accurate, timely and focussed to enable management to understand and respond flexibly to trends and changes in market conditions. Management information has generally moved from a good retailers' 'hunch' or 'merchant's nose' to a more precise science significantly enhanced by the data collected through the likes of 'loyalty' cards; detailed real-time analysis of merchandise, channel and epos data; life-time pricing; accompanied shopping; and customer counting and tracking.

The RTT also acknowledges that a structure which incorporates financial soundness, checks and balances is key too to success. According to Paul Clarke, good management requires a strong relationship with its bank, good financial disciplines and decision-making that focuses on cash generative opportunities and optimisation, rather than pure profit. This, he suggests, allows investment in the future, too. Richard Hyman adds that "Investing in demand, in the top line, is how the model and proposition is sustainable".

Integral to the organisational structure is the supply chain management process and infrastructure, which must be able to support quick response and flexibility. RTT members believe collaboration with suppliers is more sustainable than 'muscle'. With the growing importance that customers place on ethical and green issues, good supply chain management processes, accountability and traceability have never been more important to retailers. It is not just a question of efficient logistics, the RTT states; it goes much further.
and deeper into the being of great retail businesses. Furthermore, the RTT acknowledges that suppliers usually have a very good understanding and appreciation of the customer, and can contribute to a retailer's knowledge of the market, if encouraged and supported to do so.

RTT members note that size is not necessarily a success factor: small, nimble, non-traditional retailers (niche, internet, etc) can thrive if they target a specific sector. 'Success is about understanding the target customer and offering a proposition that connects with those needs, whether they be product, price, position or experience-led. Many successful retailers have spotted a particular segment of customer need and created a business and structure to serve it", says Sian Davies of Henley Centre HeadlightVision. Richard Hyman notes that that kind of niche success can be most unexpected too; "Look at the White Company. It's a superb business, but it came from what seemed like a totally barmy idea. It's been beautifully put together and is very sympathetic to its core target market – a real left-field winner.” The RTT feels that perhaps one of the greatest challenges faced by all successful small retailers is how to add scale without losing the ability to deliver the proposition and without losing contact with its life-blood; the customer.

RTT members contemplated whether being privately or publicly held made a difference to success. However they concluded that as long as the structure allows for both a consistent yet evolving long term view and highly-developed commercial astuteness, success can be achieved, regardless of ownership structure.

ii) The right organisational culture
Successful retailers must have a vision of what the future looks like, for their customers and for their proposition. They must not fear putting that vision forward, even if it means frequently changing their model to adapt to customers' and their proposition's changing needs. These are not ingredients of retail success that stem from hard structure or, indeed, infrastructure, but from business culture. Being able to respond to change in an ever-moving marketplace is as much about vision, innovation, creativity and 'can do' attitude as about having the infrastructure and information to react flexibly, the panel believes.

Leadership and empowerment are also at the core of a successful business culture. Whilst much is often and rightly made of the pivotal role of CEOs, the RTT also point to the fact that the most successful retailers treat their staff with as much respect as they treat their customers. Motivated and inspired staff lead to lower churn rates, in turn leading to more
experienced and knowledgeable staff members and to lower training overheads – a virtuous circle. John Lewis’s turnover of staff, for example, is half that of other retailers.

Innovation is hugely important to today's retail arena, and goes hand in hand with vision and leadership as a key aspect of culture, argues the RTT. The fact is that retailers today need to permanently evolve in all areas of the business to reflect the ever changing needs of their customers. Thus the discipline of change management practices needs to be incorporated into the culture of the business. It is a matter of embarking on a journey, but never arriving at your final destination. Critical to success though is insuring that a business doesn’t abandon its core values, as perceived by its customers, as it proceeds.

Innovation and the confidence to innovate, both in the proposition and the business model is important to the customer too and vital for any retailer wishing to keep ahead of competitors who share that customer. The RTT could bring forth a roll–call of many once–great–names who failed to adapt or adapted too slowly and lost market share and impetus and either disappeared or now limp on forlornly, mere shadows of their former selves. The most successful retailers don't wait, either until it's too late or it's almost too late to change their structure, proposition or philosophical orientation. The RTT acknowledges the likes of Tesco and Zara which, “are prepared to ‘do things in a different way’ which has given them ongoing benefits”, states Sian Davies.

Successful retailers have to allow for bravery in their culture too, points out Nick Bubb. They must be able to be aggressive with stores, channels, staff or formats that don't perform and cut them back speedily and efficiently. Similarly they must invest in stores and channels which do perform. Once again, Tesco provides a peerless example of single–mindedly undertaking its due diligence and then wasting no time in trying new locations, new formats or new lines, underwritten by constant evaluation, refinement and evolution of its 'proposition'.

How do the success factors change in a down–turn in the market?

RTT members agree that the fundamentals discussed above are even more important in a downturn in the market, although Helen Dickinson put it more radically than most; "Actually, nothing really changes in a downturn. It's simply that you can no longer hide your mistakes." Given that the RTT considers that the relationship with the customer in all its manifestations is truly key, it believes it is even more crucial for survival and prosperity in a downturn.
Richard Hyman put it succinctly; "When the music stops, any retailer who hasn't focussed on the customer will find themselves without a seat?"

Of all the factors that the RTT considered in its deliberations, members feel that having the right culture to encourage constant re-evaluation of the business model and the fine-tuning of the proposition, to enable the business to evolve seamlessly and effortlessly is of pivotal importance in a downturn.

RTT members also believe that during a downturn, any retailer's proposition might have to be edited more than usual to take into consideration the changing nature of the retail environment and the impact of financial pressures on the target customer. RTT members hold, however, that cutting back on product or service quality in the proposition, is not the way to keep valued customers, and their custom, when markets become more challenging. "It's certainly not a matter of switching out some lights to save on electricity", comments Mark Teale of CBRE.

This is where the right structure and culture, enabling the business to act innovatively and quickly upon new information, facilitating flexible and speedy response to the market is a driver of success. Again, the customer should be at the centre of any choices or changes made: "When in doubt, voting on behalf of the customer has always been the right decision", adds Sian Davies.

Beyond the cultural dimension, the RTT also point to certain aspects of organisational structure that are important in a market downturn. Opportunities to improve cash flow and working capital to allow more flexibility in the operating model will, the RTT believes, help to ride out the expected downturn with the customer base intact when prospects improve. To some extent it's about keeping faith with customers, giving them what they want at prices they'll pay, without compromising your basic proposition, whatever that might be.

RTT members also consider that retailers need to take a hard look at their senior management and staff, and assess whether or not incumbents are both willing and able to respond to changing market conditions. If not, hard decisions may have to be taken by leadership to correct this in order to continue to deliver a successful proposition to the target customer. A shorter decision chain is no bad thing anyway in a downturn so retailers can potentially make some reductions in management which may have four or more positive effects; getting rid of resistance to change, reducing the payroll, shortening the decision chain and, as a bonus, giving younger management an opportunity to prove themselves.
Although the RTT encourages successful retailers to take a long-term view in the face of a downturn, members strongly felt that any major projects including big IT systems programmes, international or regional expansion and entering new market segments should best be avoided if they are felt by management to be defensive moves or 'knee-jerk reactions" as Helen Dickinson calls them. Nothing should in any way take the organisation's attention away from that vital customer relationship.

However, determining whether or not all channels are being fully maximized– and indeed whether or not the right channels are in place or need different emphasis – may be an important consideration. Nick Bubb says; "On line / internet business may be something to be embraced if traditional store footfall declines, though it's not without its cost implications." If the Internet as a channel is a supplement, rather than the main channel to market, RTT members note that it must be consistent with the traditional proposition and all it entails.

At all times, good relationships with key stakeholders: customers, shareholders, financiers, employees, suppliers are important, but become even more so when the going gets tough.

RTT members believes that successful retailers are savvy enough to understand that competitors may be feeling the pressure too, and recognise that some will prosper at the expense of others in a down market. There is no magic pill which will get each retailer through to the other side unscathed and what works for one may well not work for all, however what is vital is the constant measurement, management and evolution of a retailer's offer. Happily many retailers will have the customer-focus, relevance of proposition and business model to succeed. Others, sadly, will fall and perish. Wherever they fall in the great retail forest, new saplings will grow and flourish in the clearings made. Who knows what original propositions they will have, what new retail DNA guides them, what exciting innovations will, literally, be in store?

Date Published: 9/13/2007 5:40 PM

Note to Editors:
The RTT panellists rely on their depth of personal experience, sector knowledge and review an exhaustive bank of industry and government datasets including the following:

Members of the RTT are:
- Nick Bubb – Independent Retail Analyst
- Dr. Tim Denison – Ipsos Retail Performance
- Jonathan De Mello – Harper Dennis Hobbs

info@retailthinktank.co.uk
The RTT was founded in February 2006. It now meets quarterly to provide authoritative ‘thought leadership’ on matters affecting the retail industry. All outputs are consensual and arrived at by simple majority vote and moderated discussion. Quotes are individually credited. The Retail Think Tank has been created because it is widely accepted that there are so many mixed messages from different data sources that it is difficult to establish with any certainty the true health and status of the sector. The aim of the RTT is to provide the authoritative, credible and most trusted window on what is really happening in retail and to develop thought leadership on the key areas influencing the future of retailing in the UK. Its executive members have been rigorously selected from non-aligned disciplines to highlight issues, propose solutions, learn from the past, signpost the road ahead and put retail into its rightful context within the British social/economic matrix.

Definitions: The RTT assesses the state of health of the UK retail sector by considering the factors which influence its three key drivers.

1. Demand – Demand for retail goods and services. From a retro-perspective, retail sales, volumes and prices are the primary indicators. When considering future prospects, economic factors such as interest rates, employment levels and house prices as well as others such as consumer confidence, footfall and preferences are used

2. Margin (Gross) – Sales less cost of sales; the buying margin less markdowns and shrinkage. Cost of sales include product purchase costs, associated costs of indirect taxes and duty and discounts

3. Costs – All other costs associated with the retail operations, including freight and logistics, marketing, property and people
The Retail Health Index – how is it assessed?

Every quarter each member of the RTT makes quantitative assessments of the impact on retail health of demand, margins and costs for the quarter just completed and a forecast of the quarter ahead. These scores are submitted individually, collated and aggregated in time for the RTT’s quarterly meeting. The individual judgements on what to score are ultimately a combination of objective and subjective ones, drawing upon a wide range of hard datasets and softer qualitative material available to each member. The framework follows the example of The Bank of England Agents’ scoring system on economic intelligence provided to the Monetary Policy Committee.

The aggregate scores are combined to form the Retail Health Index (‘RHI’) which is reviewed at that meeting and occasionally revised after debate if members feel it appropriate. The RHI tracks quarter on quarter changes in the health of the UK retail sector and as such provides a useful and unique measured indicator of retail health. The index ‘base’ of 100 was set on 1 April 2006. Each quarter, it assesses whether the state of health has improved or deteriorated since the previous quarter. An improvement will lead to a higher RHI score than that recorded in the previous quarter, and with a deterioration leading to a lower score. The larger the index movement, the more marked the shift in the state of health. The RHI has two main benefits. Firstly, it aims to quantify the knowledge of the RTT members in a systematic way. Secondly, it assesses the overall state of health of the UK retail sector for which there is no official data.

For media enquiries please contact:
Max Bevis, Tank PR

Tel: +44 (0)1159 589 840

Email: max@tankpr.co.uk