retailthinktank
KPMG | Ipsos Retail Performance

Is the weather an excuse for retailers' poor business models and risk management?

- *Do retailers cry wolf too often when hit by weather extremities?*
- *Optimism faces a 'Big freeze' as the Christmas season approaches*

Part I: Executive Summary

Introduction

It is often said that retailers are a bit like farmers - always complaining about the weather. But while it's not so surprising that the weather is so important to farmers' lives, given the need for the right amounts of rain and sunshine to grow crops, the case for retailers is less clear cut.

It is undeniable that periods of extreme weather can have a significant impact on an individual retailer's performance. From market point of view, a company is only ever as good as its recent sales figures, so any shift in the timing of consumers' spending patterns precipitated by the weather will be a cause for concern. Retailer's preoccupation with the weather is an inevitable consequence of a preoccupation with short-term trading.

"Extreme conditions certainly can have a profound impact on shopping activity in situations when it prevents people from reaching the shops, but retailers are often too quick to call on the weather to explain away periods of abnormal store trading," says Tim Denison, Director of Retail Intelligence at Synovate Retail Performance.

The KPMG/Synovate Retail Think Tank met in October to consider whether the weather is a justifiable explanation for poor retail performance or an excuse for poor business models and risk management.

"Indian Summer" blamed for early discounting

In the run up to the all-important Christmas trading period cash flow and stock rotation schedules are particularly tight, with retailers eager to make the most of limited shop floor space. At these critical times, retailers often dread the weather forecasts as any departure

from the normal seasonal cycle often results in consumers postponing purchases, bringing planned purchases forward, or in the worst case not making the purchase at all.

Helen Dickinson, Head of Retail at KPMG, said: "There is no doubt that the weather does impact retail performance. We see this most starkly in periods of extreme or unexpected conditions such as the country grinding to a halt in December last year due to adversely snowy conditions or the Indian summer in late September this year."

"As a result sales will be gained or lost and once forgone, a significant proportion of it will not be regained given the discretionary, 'of the moment' nature of so much of our shopping activity."

Therefore September's unusually warm weather will have tested retailers' careful Autumn planning as the already reluctant consumer was tempted away from the high street by the sun. Retailers tried to contend with this by introducing snap promotions and deep discounting over the following weeks to encourage shoppers to part with their cash, but this reduced margins already under considerable pressure from rising costs.

Weather variations in the UK

What is fair to say is that abnormal extremes of weather are unhelpful to retailers. If it is too hot when the weather is meant to be cold, or vice versa, it can make life difficult, particularly for apparel, DIY and gardening retailers.

Nick Bubb says: "That is why companies that sell weather-sensitive or weather-protective goods, but who always seem to find the weather too dry/too wet/too cold or too sunny, are always held up as examples of whining retailers. To avoid ridicule when talking to the City about trading trends, retailers are usually best advised not to mention the weather."

Food retailers, on the other hand, have more scope to flex their range and are less susceptible to weather patterns due to the shorter term level of stockholding and more responsive supply chains.

This is one reason why the weather should balance out in terms of its overall impact on overall retail sales, as business lost by non-food retailers can be gained by food retailers – which is what happened during the 'Indian Summer' at the end of September.

For seasonal products, both the start and peak of unit sales can vary by six weeks from one year to the next, curtailing or protracting the sales window. This can culminate in either significant missed sales opportunities caused by failing to have sufficient products in the stores at the right times, or serious over-stocking if the buying season turns out far shorter than the selling season. The phasing of stock, clearance strategies, the resonance of media plans, and ultimately the sales and margins made on seasonal goods can all be compromised by sustained spells of unseasonal weather.

Matters however become more contentious when weather conditions are linked to consumer's sentiment to shop, for example, blaming a 'wet' Saturday for poor trading. As the weather is significantly different from one year to the next on 75% of the days (source: Planalytics), there is a strong case to be made to treat the effect of everyday weather variations on retail over a trading year as a constant. Over the longer term our climate is reasonably predictable and the weather does not fundamentally affect consumers' ability to spend.

There are, therefore, some good reasons why the weather can contribute to short term variations in individual retailers trading performances, though retailers seem all too ready to blame sales dips on the weather and rarely attribute sales spikes to it. Its impact is overplayed too heavily and too often, and rarely over the course of a year should it be considered anything other than a 'business as usual' factor. It does not have any major impact on overall aggregate retail sales across the market over the course of any particular year.

Weather just an excuse or a mask for underlying business issues?

So is weather just another excuse for poor performance? For retailers weather is a major variable and undoubtedly affects the way consumers spend money with a particular type of retailer over a short period of time. It is a perfectly legitimate explanation for both good and poor performance as what might be unfavourable weather for one retailer might be good for another.

What British retailers will be hoping for now is that forecasts of an early 'big freeze' later this month are correct, ensuring careful plans are not disrupted and that shoppers are encouraged to get into the festive spirit early and start spending on winter clothing, seasonal food and presents.

In the UK, variations in weather are a constant aspect of the trading environment. But while UK retailers are well aware of this, new entrant foreign retailers are sometimes surprised by the impacts of weather changes on demand and costs. The longer supply chains often associated with foreign retailers mean that replenishment responsiveness may be slower; exacerbating the problem of weather-related fluctuations in stock movement and causing further cost increases.

John Dawson of University of Edinburgh, said: “As inventory systems have changed from forecast driven supply chains to consumer driven demand chains, so the impact of weather becomes more evident. But logistic responses are not always able to respond timeously and so demand is not met or, even worse, product arrives too late to catch the weather-related demand. Costs and demand are affected by variations in weather.”

A greater focus on supply chain management and forecasting is only one aspect that needs to be addressed for retailers looking to outwit the weather. A better merchandising and buying strategy will most certainly beat these short-lived weather blips. Retailers with robust forward planning and risk analysis will even be able to take advantage of these weather extremities.

Allowing a greater deal of flexibility as well as autonomy at store level, especially among the regions that experience these weather variations, can also help in managing the fluctuations caused by weather.

Retailers who don’t have sophisticated systems in place to cope with weather extremities don’t need to panic however. They should utilize the tools they already have in place. For example, the online offering should be exploited instantly when hit by adverse weather. Marketing and communications through online should be increased to shift seasonal stock.

In addition, retailers can take advantage of changing weather by luring customers into stores and increasing footfall during these periods. Sometimes the simplest steps can be the most effective. If you’ve ever dashed into a warm store during a downpour or been tempted by a water dispenser during a ‘hot spell’, you will know that this is an opportune time to target customers with your stock offerings whatever the weather – so long as the merchandising reflects the weather outside.

Another key trick to beating these rather abrupt weather variations is by retailers working to shorter and more flexible cycles. Fast fashion retailers have got it right and don’t stick to rigid plans throughout the year. It’s imperative to forward plan but those strategies need to be flexible enough to incorporate and adapt to a sudden change in consumer behaviour.

The business models currently being practised by many retailers are far too stiff to take advantage of consumer patterns. If retailers can start to work towards a more flexible model, then underlying issues faced by retailers during short-lived weather blips can be successfully overcome.

Weather changes, particularly the extreme events that are the most disruptive from a retail perspective, can be widespread or local, forecast or unexpected, and long or short-term in duration. The varied forms of weather events have different impacts on demand and costs. A forecast widespread long period of extreme cold has one set of impacts. An unexpected local heavy rainstorm and flash flood have quite different impacts on demand and costs for the retailer. Very few of these weather events should be viewed as having an unanticipated impact on demand and costs.

Conclusion

Retailers who have a plan and anticipate the risks of extreme weather changes will ensure that their stock is shifted during these periods. What is more, they will be able to ensure that their staff can get to and from work and that opening hours are adjusted to accommodate the customer. Many food retailers, for instance, get this spot-on and have good forecasting systems in place, especially on seasonal goods. For them, having the right stock at the right time is always key, given the short life cycle of many product lines. They have better forecasting models than many in the non-food sector and they have greater flexibility to pull forward stock at short notice.

For non-food retailers, it can be a double-edged sword. They don't have enough 'general' stock to work from and can't sell the stock they have at high margins. Transitional stock is also hard to get in on short notice.

To counter this, non-food retailers need to be more creative and have more autonomy at store level, especially at a regional level. Continuing to build more flexibility into the business and forecasting model is the focus for improvement.

The extent to which weather can be used legitimately to explain unanticipated changes in sales reduces every year. Forecasting the weather has improved. More and more retailing is undertaken in atmosphere controlled shopping centres and online, rather than on High Streets. Non-weather related volatility has increased so management systems should be better prepared to cope with such volatility. But it is still surprising how many times weather is used as a way of 'explaining' why sales are lower than forecasts had suggested.

Without doubt the weather can have an impact on consumer demand in general and for specific items. Weather also affects a retailer's costs but given that the weather, and its variability, is always present, effective retail management should be able to be responsive to the changes in weather, even turning them into a competitive advantage. After all, as far as the British weather is concerned, the motto 'expect the unexpected' is as fitting as it gets.

Part II: In detail – Individual views of the RTT members

Nick Bubb: "The weather across the UK is very different, but it is, literally, the same for everyone"

In the long term, over a season or indeed over a year, the weather should balance itself out, so "the weather" can never be a long-term excuse for underperformance. That is why companies that sell weather-sensitive or weather-protective goods, but who always seem to find the weather too dry/too wet/too cold or too sunny, are always held up as examples of whining retailers. To avoid ridicule when talking to the City about trading trends, retailers are usually best advised not to mention the weather.

The weather across the UK is very different, but it is, literally, the same for everyone and gone are the days when there were regional chains, based in say Scotland or London, who could buck the national trend. Most big retailers are national chains and they have to take the regional rough with the smooth, in terms of weather patterns.

What is fair to say is that seasonal or abnormal extremes of weather are unhelpful to retailers, so that if it is too hot when the weather is meant to be cold, or vice versa, it can make life difficult, particularly for apparel retailers. In the Spring/Summer season the weather is meant to be dry and sunny in the UK, not wet and cool, and in the Autumn/Winter season the weather is meant to be cool and wet, not hot and dry.

Food Retailers have more scope to flex their range and are less susceptible to weather patterns. Indeed, that is a reason why "the weather" should balance out in terms of its impact on overall retail sales, as business lost by Non-Food retailers can be gained by Food Retailers, as for example happened during the recent "Indian Summer" heatwave at the end of September.

But, by and large, the weather should only shift the timing of planned consumer spending by a few days, which is why any perception of "whining" from retailers about "the snow" in December last year was disproportionate. It was easy to point to individual days of trading in December wiped out by road disruption etc, but there was time to catch up for most retailers, not least given the comparison with snow disruption in early January 2010. In the round, given how helpfully frosty the weather was in November 2010, few clothing retailers can have had any real cause for complaint about "the weather" at the end of last year. As usual, retailers who had a compelling product offer enjoyed perfectly good Christmas trading and did not go around complaining about the weather…and yet it seems several retailers who had a bad time covered up the structural causes for their poor trading by blaming "the weather".

Helen Dickinson, KPMG: **"**The best retailers really are prepared for the unexpected**"**
There is no doubt that the weather does impact retail performance. We see this most starkly in periods of extreme and/or unexpected conditions – the country grinding to a halt in December 2010 due adversely snowy conditions or the Indian summer of late September 2011. Indeed there will be sales lost (or gained for that matter) as a result and once forgone, a significant proportion will not be regained given the discretionary, 'of the moment' nature of so much of our shopping activity. However, year in, year out, there will always be anomalies and one-offs and therefore at a market level it has little overall effect on overall retail sales.

It's a different story from an individual retailer perspective. When monitoring sales patterns on a hourly, daily or weekly basis the swings and roundabouts can indeed be stark and its part of the skill of strong retailers to forecast well and build in the flexibility in their offering and supply chain as well as to understand the factors driving their performance and to respond to continually changing conditions both in the short and longer term.

The best retailers really are prepared for the unexpected. They are getting the valuable insight from the mountains of data that they collect and interpreting it wisely. Their suppliers, logistics arrangements and store staff are sufficiently flexible to respond to fast moving conditions in an efficient and reliable way.

The issue comes in reporting – whether internal or external. Yes, the weather may well be a significant factor when assessing short term performance. But often its consequences can mask more serious underlying problems in product, supply chain or other areas of efficiency of operations.

From an external market perspective pointing to weather as a driver of performance should be used with caution. We are already in an environment where "wolf" may have been cried one too many times and cynicism has kicked in. Used too often it will it will at best sound like an excuse and at worst be interpreted as hiding some more serious problem. It's time to ensure honesty and bring back the credibility to how weather patterns are really affecting retail businesses.

Neil Saunders, Conlumino: "The link between weather and demand is documented and undeniable"
The British obsession with the weather isn't just confined to polite conversation; it's a favourite mitigating factor of many a retailer. Too hot, too cold, too much snow, too little rain the lexicon of excuses is seemingly endless. But how valid are such justifications? There are at least two factors in favour of retailers' who point to the weather to explain performance.

The first is that the weather, in all its forms, genuinely does have an impact on underlying consumer demand. A searing summer is likely to boost sales of salad, outdoor furniture and barbeques just as wash out summer will depress them. Equally, exceptionally bad weather and our seeming inability to cope with meteorological extremes, does have the potential to depress footfall or hamper internet deliveries, which in turn affects demand. The link between weather and demand is documented and undeniable.

The second factor is that British weather is genuinely changeable. While, on the whole, we are fortunate to escape extremes, we do have great short term variability in our weather patterns which makes it difficult for retailers to accurately forecast the shape of demand. Certainly, forecasting tools do exist and are employed by most large retailers selling products subject to weather-related shifts, but they are far from being totally accurate and can still leave even the best of retailers on the hop.

While the above points are both valid, it has to be said that weather does not have a huge impact on overall aggregate demand; some products may be affected more than others, but weather does not fundamentally affect consumers' ability to spend. So there are limits as to how much the weather can be used as an excuse. Moreover, over the long term our climate is reasonably predictable so weather excuses are much more valid to explain away a bad season, than they are to explain a poor year or couple of years of trading.

The bottom line is that retailers have a responsibility to be honest about the weather, and that includes pointing out when it has helped drive a strong performance as well as a weak one. Retailers also have a responsibility to build tolerance into their merchandise, sales and margin plans to account for weather variability. Just as wise person will carry an umbrella even on a clear day, a wise retailer will have a plan for the inevitable shifts and fluctuations in our weather.

Tim Denison, Synovate: “Retailers are quick to call on the weather to explain away periods of abnormal store trading”

Why does British small-talk invariably start with the weather? The explanation is pretty simple: the UK has one of the most changeable daily weather patterns in the world, making it a ready topic of conversation. Take a recent week; at its start we were basking in temperatures approaching 30˚C, making news headlines, but nearing its close the rain was descending and temperatures had tumbled to their October norm.

Retailers are quick to call on the weather to explain away periods of abnormal store trading. Extreme conditions certainly can have a profound impact on shopping activity in situations where it prevents people from reaching the shops. At the height of the winter snowstorms last year, for example, 22% fewer shopping trips were made in the 4 days between 29th November and 3rd December compared to the previous year (source: Synovate Retail Performance). It resulted in lost sales that retailers never fully clawed back in the run-up to Christmas. The opportunity to buy online does now help cushion the impact of inaccessibility caused by extreme weather. Over that same week last year, John Lewis reported internet sales up by 45% year-on-year.

This argument however, fails to hold up for seasonal products; the weather conditions when consumers start and stop buying seasonal lines. Both the start and peak of unit sales can vary by 6 weeks from one year to the next for seasonal products, curtailing or protracting the sales window. This can culminate in either significant missed sales opportunities caused by failing to have sufficient product in the stores at the right times, or serious over-stocking if the buying season turns out far shorter than the selling season. The phasing of stock, clearance strategies, the resonance of media plans, and ultimately the sales of and margins made on seasonal goods can all be compromised by sustained spells of unseasonal weather.

There are, therefore, some good reasons why the weather can contribute to variations in trading performances, though retailers seem all too ready to blame sales dips on the weather and rarely attribute sales spikes to it. To my mind its impact is overplayed too heavily and too often, and rarely over the course of a year should it be considered anything other than a 'business as usual' factor.

Richard Lowe, Head of Retail & Wholesale, Barclays Corporate: "September's unusually warm weather will have tested retailers' careful planning as the already reluctant consumer was tempted away from the high street by the sun"
Most retailers will define weather as bad when a season is delayed or unusually hot or cold for the time of year so while most of us were enjoying September's Indian summer, the unusually warm weather was a cause for concern for the high street as consumers bought ice cream and sun cream instead of winter coats and woolly jumpers.

Retailers, particularly fashion retailers, work months in advance planning and ordering stock in anticipation of the seasons, which are broadly predictable – warm in the summer and cold in the winter. This year the seasons have been turned on their heads with an April heat wave, a wet summer and the 29 degree-highs of late September challenging retailers in an already difficult market.

In the run up to the all important Christmas trading period cash flow and stock rotation schedules are particularly tight with retailers eager to make the most of limited shop floor space. Any departure from the normal seasonal cycle, as we have seen, often results in consumers postponing or bringing planned purchases forward, or in the worst case not making the purchase at all.

So September's unusually warm weather will have tested retailers' careful planning as the already reluctant consumer was tempted away from the high street by the sun. We can expect to see many retailers trying to contend with this by introducing snap sales and deep discounting over the next couple of weeks to encourage shoppers to part with their cash. This in turn will reduce margins which are already under considerable pressure from rising costs.

So is weather just another excuse for poor performance? For retailers weather is a major variable and Britain's unreliable weather, undoubtedly affects the way consumers spend money. In my view it is a perfectly legitimate explanation for both good and poor performance as what might be unfavourable weather for one retailer might be good for another.

What British retailers will be hoping for now is that forecasts of an early big freeze later this month are correct, ensuring careful plans are not disrupted and that shoppers are encouraged to get into the festive spirit early and start spending on winter clothing, seasonal food and presents.

Mark Teale, CB Richard Ellis: "There is little evidence that the weather has much overall impact on aggregate annual sector sales levels"
Shopping activity clearly is affected by weather conditions. If it is pouring with rain or snowing, we are less likely to want to go shopping or, at least, prefer to go shopping in covered centres. Conversely, if it is sunny, High Street shopper footfall levels are apt to increase. As unseasonal weather can (and does) suppress/increase sales in the short term, it is understandable if retailers periodically maintain that their sales levels have been impacted by the weather. Niche traders, with seasonal offers, are particularly vulnerable.

There is however little evidence – to date at least – that the weather has much overall impact on aggregate annual sector sales levels. Or rather that there are so many other factors affecting sector sales levels that it is rarely possible, even following prolonged periods of drought or lengthy bouts of unsettled weather , to credibly attribute aggregate sales change to the weather. Whatever the broader concerns regarding climate change might be, there is little evidence that any changes in weather conditions in the UK over the last few years have impacted much on shopping behaviour.

What is changing shopping behaviour, and indeed has resulted in an 18% reduction in shopping frequency since the mid 1990s, is market share shifts to (one-stop) out-of-town trading facilities and the reduction in trip level due to the concentration of shopping activity in larger markets. The latter, by increasing shopping access costs, is steadily reducing shopping frequency. Fuel price inflation is exacerbating the problem (as is the internet, parking cost inflation etc).

Whether the decline in shopping frequency matters is a moot point. The shopping frequency reduction has occurred over a period that has seen a very substantial increase in consumer spending. Average trip spends have increased significantly as a result. Trip levels are already pretty thin in the early days of the week, particularly in out-of-town markets. Staffing levels are an issue where throughput levels are heavily concentrated in only part of the week (often Friday, Saturday and Sunday). But apart from that, from the property perspective, it is the aggregate profit contribution of occupiers cumulatively over time that matter, not short term spending fluctuations whether or not due to the weather.

John Dawson, University of Edinburgh: “Very few weather events should be such as to have an unanticipated impact on demand and costs”

As inventory systems have changed from forecast driven supply chains to consumer driven demand chains so the impact of weather becomes more evident, but logistic responses are not always able to respond timeously and so demand is not met or even worse product arrives too late to catch the weather related demand. Costs and demand are affected by variations in weather.

Weather changes, particularly extreme events which are the most disruptive from a retail perspective, can be widespread or local, forecast or unexpected, and long or short-term in duration. The varied forms of weather events have different impacts on demand and costs. A forecast widespread long period of extreme cold has one set of impacts an unexpected local heavy rainstorm and flash flood have quite different impacts on demand and costs for the retailer. Very few of these weather events should be such as to have an unanticipated impact on demand and costs.

The extent to which weather can be used legitimately to explain unanticipated changes in sales gets less year by year. Forecasting the weather has improved. More and more retailing is undertaken in atmosphere controlled shopping centres rather than on High Streets. Non-weather related volatility has increased such that management systems can cope better with such volatility. With these reductions in the role of weather it is surprising how many times weather is used as a way of ‘explaining’ why sales are lower than forecasts has suggested.

Without doubt the weather has an impact on consumer demand in general and for specific items. Weather also affects the costs of a retailer but given that the weather, and its variability, is always present, effective retail management should be able to be responsive to the changes in weather, even turning them to competitive advantage. In explaining the unexpected, retailers too often see no enemy but winter and rough weather.

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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

- Martin Hayward – Hayward Strategy and Futures
- Maureen Hinton – Conlumino
- James Knightley – ING
- Richard Lowe – Barclays Retail & Wholesale Sectors
- David McCorquodale – KPMG
- Martin Newman – Practicology
- Mike Watkins – Nielsen

The intellectual property within the RTT is jointly owned by KPMG (www.kpmg.co.uk) and Ipsos Retail Performance (www.ipsos-retailperformance.com).

First mentions of the Retail Think Tank should be as follows: the KPMG/Ipsos Retail Think Tank. The abbreviations Retail Think Tank and RTT are acceptable thereafter.

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.

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