Greentailing and Other Revolutions in Retail

Hot Ideas That Are Grabbing Customers' Attention and Raising Profits

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Published by John Wiley & Sons, Inc., Hoboken, New Jersey.
Published simultaneously in Canada.

Library of Congress Cataloging-in-Publication Data:

Stern, Neil Z.
Greentailing and other revolutions in retail : hot ideas that are grabbing customers' attention and raising profits/Neil Z. Stern, Willard N. Ander.
p. cm.
Includes bibliographical references and index.
ISBN 978-0-470-28858-0 (cloth)
1. Retail trade–Management. I. Ander, Willard N. II. Title.
HF5429.S734 2008
658.8'7–dc22

2008012263

Printed in the United States of America.

10 9 8 7 6 5 4 3 2 1

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Preface

> You say you want a revolution.
> Well, you know we all want to change the world.[1]
>
> —*The Beatles*

Symbolically, we chose to begin writing *Greentailing and Other Revolutions in Retailing* on November 23, 2007. That day was better known in retail circles as "Black Friday," the day after Thanksgiving, and the supposed start of the holiday shopping season. It received the name Black Friday years ago for also being the day that retailers finally begin to reap profits after losing money for the majority of the year. For many years, it was also the biggest shopping day in terms of overall sales, with cash registers merrily ringing away. Though Black Friday has long since lost its distinction as the biggest shopping day (procrastinating shoppers have turned the weekend before Christmas into the biggest shopping period), sales on Black Friday for 2007 were still estimated to be well over $10 billion.

Retailers are no longer content to simply wait for Black Friday to kick off the holiday season. Many retailers simply blur the lines between holidays, with Christmas products for sale even before Halloween ends. With the holiday season so important to retailers, the sooner they can get sales, the reasoning goes, the better. Nor, seemingly, can they wait to open their doors. A quick perusal of the dozens of holiday ads spread out in front of us show that 4:00 AM seems to be the "right" time to start sales. If you're not an early riser, no problem—most stores also managed to stay open until midnight. And more stores still offered promotions that kept them open during the holidays for days *and* nights. For those customers sleep deprived enough to show up at those early bird sales, fantastic bargains awaited: 42" HD plasma TVs were being sold in some stores for under $1,000—the same item was well over $5,000 just two years ago. Vacuum cleaners were being sold for $25 and brand name jeans for $9. Could there be any truer indication that America's frenzy for the pursuit of more for less continues unabated?

Indeed, a simplistic but startlingly accurate view of retailing over the past 100 years or so reveals that almost all retail innovation can be directly traced to the retailer's constant quest to determine ways to sell products for less, and the consumer's eagerness to embrace this philosophy. And, by selling products for less money, we entice consumers to buy more. This has meant wondrous innovation on both the supply and demand side of the equation. From a supply standpoint, sophisticated logistics and distribution, enormous advances in technology help to manage the business in a smarter manner, and the globalization of sourcing has helped keep costs (and subsequent prices to the consumer) low.

From a demand side, there has been a constant evolution (and sometimes revolution) from a format standpoint. The development of the self-service supermarket (along with the development of the shopping cart) and the invention and evolution of the discount store and the Internet have changed the way Americans shop. New formats have come along, all figuring out a way to sell more, for less. The Supercenter (the combination of food and general merchandise in one enormous box) allowed companies like Wal-Mart to sell a broader range of products for even less money. The creation of the Wholesale Membership Club, typified by concepts like Sam's Club and Costco, created an awesomely efficient way to sell select items in large quantities at unbelievable prices. Dollar stores like Family Dollar and Dollar General focus on imported goods and extremely low cost of operations to achieve their savings. And the European notion of a hard discount store (typified by companies like Aldi) bring together private brands, extremely limited range, and a low-cost store to achieve great savings. The consumer has reaped a windfall of savings, and retailers who have figured out how to sell for less have experienced exponential growth.

While not all innovations in retail have focused on price, it has certainly been a prevalent theme. While exploiting fashion, providing outstanding service, offering an expanded range of products, and selling or manufacturing high-quality merchandise have all shown that available niches exist in all facets of retailing, the notion of bigger and cheaper has been hard to shake. Margins have been reduced in just about every retail business, from food to apparel to electronics. Similar products cost less now after inflation than they did decades before, and consumer buying power has increased. The consumer has had it very good, demanding more for less, and more often than not, getting it.

In our first book, *Winning at Retail*, we extensively documented what amounted to an empirical look at retail success and our theory behind why some retailers win and others lose. We called it the "-Est Theory for Retail Success." The -Est theory derives from the word "best," and essentially says that a retailer must be best—superior to all others—at one core proposition that's important to specific customers. Retailers must strive for this, the notion of owning one key element, rather than attempting to be great at everything for all customers. -Est retailers devote themselves with laser-like focus to their core customer proposition, what we call their "-Est position." They commit employees from top to bottom of their organization to that position. They communicate their -Est position to customers, and execute it relentlessly at the store level. -Est retailers also base strategic and day-to-day operational decisions on their -Est position.

Wal-Mart was cited as the quintessential example of one core -Est element—cheapest. Everything Wal-Mart did for its first 40 years of doing business was focused on enhancing its position as the low-price leader. With its "Always Low Prices," Wal-Mart won with customers. The other -Est positions that win with customers are: Big-Est, having the largest assortment of one merchandise category; Hot-Est, having the right products just as customers begin to buy them in volume; Easy-Est, having service that makes shopping easy; and Quick-Est, having service that makes shopping quick.

We defended the theory by documenting successful retailers' adherence to these basic principles. It took a very rational viewpoint of consumer behavior, suggesting that retailers could be classified into one general area. And hindsight has thankfully proven the theory. But, as with any theory, questions certainly lingered and we engage in many debates, in countless facets of the retail industry, on whether the theory still holds. We are often asked the following:

- Does the notion of an -Est work in every category?
- What about occupying more than one -Est position? Isn't it better to have two or three -Ests rather than one?
- Can an -Est position go away?
- Aren't there multiple facets of an -Est like hot?
- What about quality? Surely there are retailers who win by having the best-performing stuff?
- What about the emotional aspects of connecting with a brand? There seem to be many examples of brands that win not for rational reasons alone but by creating a very real relationship with the customer.

In the very real nuances of positioning a retailer, all of these questions are valid and all need to be accounted for in an increasingly complex and competitive retail world. While we stick to our guns on the need to differentiate and not be everything for everybody, we acknowledge the need for further examination of a retailer's positioning.

It's difficult to argue with the notion of selling products for less. Wal-Mart's mission has long been built under the concept of allowing ordinary people the opportunity to buy more products. It turns out that the execution of this very simple and very pro-consumer positioning strikes at the very core of our social fabric. Manufacturing jobs have all but deserted America as companies have sought to source goods cheaper elsewhere. The deflation of many products has been achieved through cheap global sourcing. What about competitive wages for workers? What about health benefits for employees, as retailing makes up a huge chunk of American jobs? What about protecting smaller retailers without access to the economies of scale of the bigger players? And what about smaller manufacturers (or even bigger ones) who must constantly attempt to take costs out of their products to live up to the relentless cost pressures from retailers? These are all significant issues that the country (and retailers) are dealing with today and challenge the idea that lower prices for consumers is always the best thing for society as a whole.

We have always been proponents of a basic economic stance: "The customer is boss." Or consumers vote with their wallets. One of the inevitable responses that consumers will give in focus groups is nostalgia for the old days. They loved the service at the local hardware store or the intimacy of shopping in town. Well, if consumers liked it so much, how come they switched their spending dollars to Home Depot and away from Bob's Hardware? Again and again, what consumers say and what they do seem to be two very different things.

There is mounting evidence, however, of impending change. Wal-Mart, with its incredible historic growth, has been slowing down of late and has not been able to produce the phenomenal growth that at one point seemed inevitable. Whether it's growing consumer resentment over Wal-Mart's social practices or simply poor execution of retail fundamentals, the retail giant is no longer as successful (or feared) as it once was. While far and away still the largest and most formidable retail organization in the world, its future growth no longer feels as certain. If bigger was better, that surely couldn't happen. Home improvement titan Home Depot is struggling to maintain its customer base and the largest department store chain, Macy's, is also limping along of late.

There is also considerable evidence that the consumer is changing and success can no longer be as easily measured in the simple, rational dimensions of price or having an ample abundance of products. Perhaps big, one-size-fits-all formats are no longer the right formula for success?

And perhaps consumers will begin voting with their values as much as their dollars.

Greentailing and Other Revolutions in Retailing seeks to catalog those changes that are occurring in retail today. They might be revolutions, providing new ways to connect with customers and drive business. This is not a manifesto for going green. We are pragmatic practitioners of the fundamental goal of retail strategy—if it doesn't drive long-term success and profits, don't bother. This is not about feeling good or generating positive public relations but driving sales and profits. We delve into the notion of Greentailing and the implications it's having right now on retailers and suppliers. We look at the key consumer demographic and behavioral changes that are creating the opportunities for new ways to reach consumers. We explore the dynamics of new ways to win with consumers, breaking away from traditional brick-and-mortar, product-driven approaches. And, we tackle the issue of who owns the customer and the changing dynamic between retailer and supplier.

You say you want a revolution? *Greentailing and Other Revolutions in Retailing* may not change the world, but hopefully it will at least encourage people to think about retailing in a whole new way.

INTRODUCTION

What's Going to Revolutionize Retailing in the Future?

The future is already here. It's just unevenly distributed.
—*William Gibson*

William Gibson, the great British science fiction writer, is famous for taking reality as we know it, and with just the slightest shifts, creating a futuristic vision of the world. Although his stories explore an unknown future, they are steeped with enough reality to be plausible. Somewhere, in the hundreds of thousands of existing stores, millions of product on the shelves, and untold dreams in the heads of entrepreneurs, the vision for the future of retailing is already taking shape. It will likely be built on common trends and themes we see today, with that slight "shift" that creates the revolution. As Gibson intimates and we preach, the future is already here, it is just not easy to collect it in one tidy place. We know real change is going to happen; getting there, profitably and fast, is sometimes a very different story.

Every year, hundreds of new concepts and tens of thousands of new products are ambitiously introduced into the marketplace. Very few manage to succeed. Some are bankrolled by multibillion-dollar corporations with reams of data and research. Others are formed on a shoestring budget, operating out of a garage or the trunk of a car. We have been tracking, reviewing, and participating in the development of new concepts for over 20 years at McMillan|Doolittle. We would venture to say we have probably seen more new ideas—realized or scrapped on the drawing board than just about anyone. We trade on this experience to hopefully have a higher batting average of hits versus misses. We are constantly monitoring the retail scene to try to answer some of the fundamental questions:

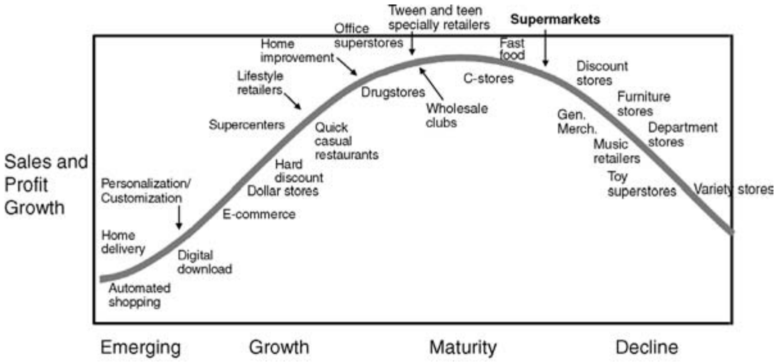
- Why do some concepts work and others fail?
- Why do some ideas, like the notion of Greentailing suddenly seem to be taking hold after nearly two decades of gestation?
- What other ideas are going to revolutionize the retail landscape?

Most importantly, we often first need to answer the question, who cares? Why is there an obsession with developing new ideas or innovation? If you have a successful concept or product line, what's wrong with running with what you have and making the occasional tweaks along the way? The answer is simple—do you want to be in business 10 years from now?

For a number of reasons, the world of retailing is changing faster and more dramatically than ever before. It is not enough to simply get it right once; winners must continually stay on top of their game or risk an even quicker obsolescence than ever before. With the customer voting daily, the need to stay on top is vital. And there is certainly still an advantage for the retailer or supplier who gets there first. It is always easier to make changes when you're on top than when you're fighting for survival at the back of the pack.

COMPRESSED LIFE CYCLE

It's no secret that retail has been consolidating. There have been more mergers than ever before, consolidating retail power among fewer companies. At the same time, there have been more bankruptcies, with weaker retailers dropping out of the race. Just as importantly, we've also seen the life cycle for stores squeezed. In the past, the retail life cycle looked like a typical bell curve. There's a period of development for an emerging concept, followed by a period of rapid growth, then maturity as the curve flattens, and then eventually there's a decline. That cycle still exists, of course, but it's been significantly compressed as new retail concepts grow, mature, and decline faster than ever:



The Retail Life Cycle

Are consumers simply more fickle than before? We don't think so. The abundance of great choice has made them realize that better alternatives do exist. They are simply not as loyal to any store or brand.

The cycle is compressing in part because of the globalization of communications. Ideas can spread almost instantaneously, thanks to the Internet. While good ideas once were able to remain regional and somewhat obscure, that's no longer the case. Ideas and best practices now spread internationally, often in a matter of days, as traditional barriers and borders begin to disappear. When Tesco "secretly" opened its long-awaited entry into the U.S. market called Fresh & Easy, it was a matter of hours before significant intelligence (and lots of opinions) flooded the Internet. Ideas no longer incubate in relative obscurity because they are exposed quickly on an international stage. There is little that is proprietary to a retail concept that has its doors open to the public. They are easy to replicate but hard to run successfully.

The other big squeeze on the life cycle is the high-risk, high-reward influence of venture capital and public markets. Retailers have greater access to funds than they did in the past, both from private and public sources. However, that money comes with strings attached—the expectation of fast growth. As e-commerce showed, the battle for "first-mover" advantage and critical mass has often become the top priority. Getting there first, and with scale, requires a concept to move fast. The result of these activities is a compressed retail life cycle that forces new concepts to come of age quickly. It also puts pressure on older formats and established retailers to innovate, or risk idly sitting by while a fast-moving new concept takes away customers. Staying on top is harder than ever before, and the monthly report card of same-store sales often shows how quickly one's fortune can change. Even before the ink dried on our first book, *Winning at Retail*, some of our "success" examples were beginning to experience hard times.

As proof of the compressing life cycle, we looked at the history of various retail formats. Variety stores like Woolworth and Ben Franklin were the nation's first mass retailers. They are dead now, after about 50 years of existence. Department stores are also about 50 years old and now are clearly in a state of decline, in the process of consolidation rather than rapid growth. Yes, department stores are still important, but discount stores now outsell department stores by about a 4 to 1 ratio, with most of that change occurring in the past 20 years. Discount stores themselves were hatched around 40 years ago. And in just 40 years, they've reached a level of maturity where even the nation's number three discount store, Kmart, is fighting for survival. Meanwhile, the leaders Wal-Mart and Target have both become grocers as a way to continue expanding, and both are trying to figure out new ways to maintain their dominance. The category killer sector, including stores like Home Depot and Toys"R"Us, have been around for 30 years or so. (Note: Toys"R"Us actually was started over 50 years ago, but not in the category killer, large-chain format of today.) These "biggest" type retailers are also mature, and various sectors within this category appear to be in decline. E-commerce retailing, with all its hype and irrational exuberance, matured in less than a decade to the point where many start-ups were forced out of business and growth rates will soon be approaching 10 percent to 15 percent annually rather than the 50 percent to 100 percent growth of the past.

Life cycles are shrinking so dramatically that it's nearly gotten to the point where investors, retailers, and retail suppliers should begin to think about stores the same way investors think about dance clubs or trendy restaurants. Those types of businesses are notorious for being big moneymakers for two or three years, then either limping along for a time or simply going away. The investment strategy is to get in fast, make lots of money, then get out. While retail may never move quite as fast as hip restaurants and night clubs, the lesson is plain: In today's market, stores must be able to adapt to new market conditions very quickly. Successful companies then need to be judged not only on their ability to get it right once, but also on their ability to innovate and change as consumers and competition dictates. And they must be able to do so in a high-pressure environment, where separating out the fads from long-term trends is extremely difficult. Getting out may be just as important as getting in—there have been several notable plugs pulled of late (The Gap's Forth & Towne or Finish Line's Paiva) where the trend was there but the companies themselves were not able to capitalize on it.

The trick, then, is to maintain a solid position on the growth side of a retail life cycle. This may mean developing a new format to participate in a growing market or radically revamping an existing one to maintain relevancy. In a world where it is increasingly difficult to find a one-size-fits-all format, it might mean doing all of the above—looking for a new concept for growth while retooling an existing one.

What are the common ways that retailers lose their way? We have identified four classic patterns:

1. *Innovative new competition:* Competition truly has to be accounted for on a local level. Customers shop the stores in their trade areas. A retailer simply has to be the best in its marketplace to succeed. In the absence of better competition, a retailer can succeed in its market, temporarily. But, eventually, a better competitor will come along and supplant that retailer's existing position. That retailer can come from the next town, region of the country, or increasingly, from another part of the world. Even more daunting, he or she may come to market in the form of an e-commerce competitor, or a