The Future of Retail

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Challenged, but not broken

The Future of Retail
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Is traditional retail broken? Many people think so, pointing to shuttered shops, town centres bereft of shoppers, and deserted malls. The Covid-19 pandemic, they argue, merely accelerated a trend that was already underway, stretching back 20 years: the rise of e-commerce, exemplified by e-tailers such as Amazon, Zalando, AO World, Boohoo, Zappos, and Asos.

Traditional retail is certainly challenged. There's no mistaking that. But there's a world of difference between 'challenged' and 'broken'. E-commerce's rise isn't unstoppable, and nor is e-commerce without risk. While traditional retailing isn't necessarily a comfortable place to be right now, neither is e-commerce retail, either: ask any online retailer competing with Amazon.

The paper you're reading discusses the various issues and challenges faced by retailers in both the physical and online worlds, talking to leading experts for insights and industry perspectives. Better still, it highlights specific and actionable strategies enabling each to compete more effectively. Finally, it points to the skills likely to be necessary in order to compete in this brave new retail world.

In short, if the future of retailing—physical, online, or both—is close to your heart, then I believe that this paper is essential reading.

Professor Omera Khan
Executive Strategic Advisor
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Founded in 1778, British retailer Debenhams was famed for its multi storey department stores, almost two hundred of which were once to be found spread across the UK.

As recently as 2011, the company was valued at £1.6 billion. No longer: in January 2021, the business was sold for just £55 million—and the purchaser wanted only the Debenhams brand, not the 118 remaining Debenhams stores, or any of their employees. The stores would be closed, and their employees would lose their jobs.

The buyer? Manchester-based online fashion retailer Boohoo, founded as recently as 2006, and which has a stock market value of £4.4 billion. Days later, a similar fate befell billionaire Philip Green's collapsed Arcadia fashion chain, and its Topshop, Topman, Miss Selfridge, and HIIT brands. Again, the buyer—online fashion retailer Asos—wanted just the brands, not the physical stores or their employees, paying £265 million for the brands, and £30 million for on-hand inventory. The following month, Boohoo snapped up the remainder of Arcadia, paying £25.2 million for the chain's venerable Dorothy Perkins, Wallis, and Burton brands. Again, the 214 shops were to be closed, and their 2,450 employees made redundant.

True, Arcadia had been slow to embrace e-commerce, and had initially been dismissive of the rise of 'pure-play' online retailers. But Debenhams, noted the Financial Times, was one of the top ten retail websites in the UK, with 300 million visits and £400 million of sales in the year to August 2020. Integrated into Boohoo's operation, a revitalised Debenhams was expected to prosper again, said observers —but only as an online business.

Yet even if the detail of the narrative differs from retailer to retailer, and country to country, the bigger picture is clear. Something significant is convulsing the world of retail. Paradigms that reliably worked for

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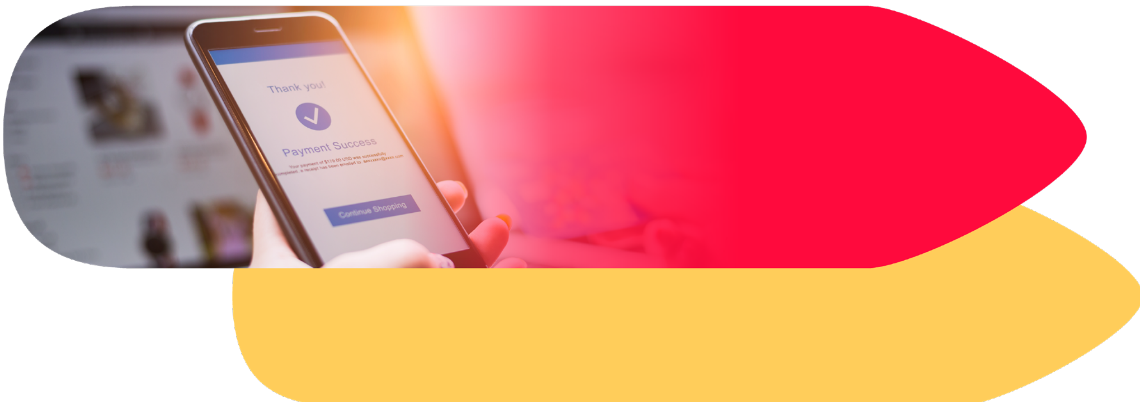
And signs of that revolution are everywhere. In America, Sears once had over 3,500 stores, and was a fixture in countless malls across the country. A January 2021 article in business magazine Forbes struggled to identify the number currently trading, but estimated it at just over 60. Sears, like Debenhams, is another operator of department stores. So too are Neiman Marcus, J. C. Penney, and Germany's Galeria Karstadt Kaufhof, which also declared bankruptcy. Maybe, then, it is solely department stores that are troubled?

Alas, no: legions of niche stores have also vanished, or been forced to declare widespread store closures, or filed for bankruptcy, too, across Europe and North America. Germany's McTrek outdoor chain, the UK's electrical retailer Comet; America's Toys R Us, Brooks Brothers, J. Crew, and Guitar Center; the list is long, and growing. And for every retailer that simply collapsed and vanished, it is clear that many, many more are troubled, and shrinking, with stretched balance sheets and tiny



What's going on?

It is tempting—but mistaken—to start with the most obvious manifestation of the revolution that is taking place in retail: the rise in e-commerce, exemplified by the emergence of retailers such as Amazon, Zalando, AO World, Boohoo, Zappos, and Asos.

But to do that is to confuse cause and effect. E-commerce sites such as these wouldn't exist—or wouldn't have grown in such a spectacular fashion—if they didn't address some basic consumer needs that traditional bricks-and-mortar retailing either didn't meet, or didn't meet very well.

The real starting point, then, is the consumer. **What is it that today's consumer wants, and how—and why—has that changed from what yesterday's consumer wanted?** This, it turns out, is a question that is very straightforward to ask, but tantalisingly difficult to answer.

One thing is clear, stresses retail logistics veteran Neil Ashworth, non-executive chair at retail fulfilment service provider Selazar: the changes in retail that are underway at present aren't something new, but go back over 50 years, although the pace of today's change is far faster. The death of 'over the counter' grocery retailers, the emergence and growth of self-serve supermarkets and petrol stations, the rise of hypermarkets, the decline of department stores, and the emerging rise of convenience retail: these are driven by deep-seated changes in consumer behaviour and expectations.

What is it that today's consumer wants, and how—and why—has that changed from what yesterday's consumer wanted?

"Back in the 1950s, choice was constrained, and people lived the same way, and looked the same, and ate the same things. **Today, consumers want to be far more individualistic, and their expectations about choice and range and quality are far more demanding.** Arguably, Tesco's rise to prominence in the UK market was driven by catering to this demand, serving the vast group of 'the middle' and by winning the race to put down property to meet it," he observes.

In much the same way, consumers increasingly want an individual experience: shopping as a form of entertainment, shopping as an experience—so-called 'experiential commerce'—and shopping as a form of social interaction. Generation Z, and most millennials, view retail stores very differently from previous generations, notes Patrick Van Hull, industry thought leader at supply chain software company Kinaxis, and a keen observer of the American retail market.

"So far, especially in America, experiential commerce has generally been an urban phenomenon, but now it's moving out into the suburbs, and into even rural environments," he explains. "If you're competing with Amazon, it's difficult to differentiate yourself on price, so you have to do it some other way: service, providing an experience, and entertaining."

Ashworth agrees. In the UK market, he notes, large out-of-town retail park electrical retailers—in the front-line when it comes to competing against price-focused e-commerce retailers such as AO World and Appliances Direct—are having to focus more on experiential commerce in order to differentiate themselves, a trend which he sees only accelerating.

"Walk into a large appliance store in the United States to buy a cooker or a range or a refrigerator, and you're being sold to by trained chefs. They've realised that people don't just want to own the appliance, they also want to own the outcome: the meals that you prepare with it. A video from an e-commerce store, viewed on your laptop, just doesn't compare."

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Neil Ashworth
Non-executive Chair Selazar

And essentially, argues Tony Mannix, chief executive of Clipper Logistics, a retail-focused logistics provider with specialisms in fashion and non-food retail, experiential commerce is simply a ratcheting-up of a long-running trend—a continuation, in other words, rather than something new.

"Despite the Covid-19 pandemic, the consumer hasn't changed: they still like to shop. They like seeing things, and enjoy being sold to. Look at what happened in the summer of 2020, after the first lockdown eased: people flocked to stores such as Primark and IKEA, because they liked the retail environment and the experience of shopping there. Queues of over an hour were commonplace, and at some stores, shoppers arrived before 6am for a 9am opening."

That said, notes Van Hull, it is too simplistic to see the world of retail as a single entity, responding identically to identical pressures. Likewise, it can be dangerous to generalise too much about consumers: there will always be products, and situations, and individual consumers, "where the requirement is simply to go into the store, grab what is needed, and get out."

The trick, then, is for retailers to be able exploit that requirement—hence, of course, the rise of the modern-day convenience store. To maximise success in such a scenario, he stresses, it is not just the physical retail environment that needs customising to consumers' expectations, it is also very often the products: in grocery, for instance, the focus is on ease, convenience, and goods that ready-packed, pre-chilled, appropriately-sized and portioned.

Perhaps more than anything, though, it is consumers' expectations regarding choice and speed that are impacting most on retail. Today's consumers don't just want a wider selection to choose from, as well, they demand near-instant gratification once that selection has been made.

Flexibility, agility and responsiveness have never been more important.

"The days of 'please allow 28 days for delivery' have long gone," says Clipper Logistics' Mannix, bluntly. In physical retail, he notes, the move towards ever-larger stores—on both sides of the Atlantic—was about achieving an optimum combination of choice and speed: a wide range to choose from, and the promise of being able to carry it away there and then. Flexibility, agility and responsiveness have never been more important.

Ashworth agrees. British home goods retailer John Lewis—which, although arguably less-differentiated in the market than formerly, has still largely managed to sidestep the carnage taking place in the department store sector—is often touted as a retail success story. It isn't, he argues—instead, the firm should more properly be regarded as a supply chain success story.

"John Lewis realised that when on average you're selling less than an item per store per week, the nearest whole number is zero. So you replenish only on sale, and not to some pre-determined layout guide or inventory-holding formula such as 'case quantity plus two'. Doing that allows you to eliminate in-store storerooms, freeing up space. But the shelves start to look bare, after a while. So you put in narrower shelves, which frees up more space, which you fill by offering a broader range, or whole new product lines. And finally, you establish 'close-support' warehouses, which can replenish sold items very, very quickly. The result is like-for-like sales growth, at a time of shrinking sales elsewhere in the market. You are also able to serve the home shopper from the same facility, thereby improving the return on investment"

Speed has a cost—a cost to both the consumer, and the retailer.

That said, speed has a cost—a cost to both the consumer, and the retailer. For a physical retailer, a consumer's speed expectations can't be met if their demand hasn't been forecast accurately, and the item is out-of-stock. Grocery retailing led the way, says Delia Vazquez, Senior Lecturer in Retail Marketing at the UK's University of Manchester: because food is perishable, inaccurate forecasts carry a cost both in terms of lost sales (if demand has been under-estimated), or discounted or thrown-away products if demand has been over-estimated.

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Tony Mannix
CEO Clipper Logistics

Zara-style fast replenishment based on actual sales short circuits this, but again, at the cost of setting up such a supply chain, and the arguably higher costs of near-shored manufacturing.

Fast fashion is another example, she adds: with long supply chains stretching to Asia, both lost sales and discounting are endemic. Zara-style fast replenishment based on actual sales short circuits this, but again, at the cost of setting up such a supply chain, and the arguably higher costs of near-shored manufacturing.

Nor is speed costless for the e-commerce retailer, especially at the extremes. To offer same-day deliveries, special-purpose supply chains are required, points out Michael Huth, Professor of Logistics at Germany's Hochschule Fulda University of Applied Sciences.

"High-speed fulfilment capabilities cost money in terms of local warehouses and 'last mile' delivery capabilities," notes Huth. "It's also necessary to invest in superior forecasting techniques—perhaps using artificial intelligence—in order to better forecast demand, and fine-tune the stocked range."

Amazon, for instance, is building a network of smaller warehouses located close to cities, holding a reduced range of items—typically, just over 100,000 or so—with a guaranteed delivery of under five hours. Amazon Prime Now, long-established in major conurbations on both sides of the Atlantic, offers two-hour deliveries on groceries and similar items, from a range that is 20,000-strong. Ultimately, report those close to the company, the goal is to increase both the size of these stocked ranges, as well as the number of such warehouses: a September 2020 report from Bloomberg, for instance, spoke of 1,000 suburban warehouses spread across the United States.

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Professor Michael Huth
Hochschule Fulda University of Applied Sciences

The promise of e-commerce

E-commerce made it possible to stock—and sell—the remainder of the range: the so-called 'tail', stretching all the way down to items that sold far less frequently, but which cost little to stock in vast warehouses located in inexpensive industrial parks.

In October 2004, tech magazine Wired published an article by its editor-in-chief, Chris Anderson. Two years later, in July 2006, the thoughts contained in that article saw the light of day again, in Anderson's book The Long Tail: Why the Future of Business Is Selling Less of More, which was promptly shortlisted for the Financial Times Business Book of the Year Award.

Stripped to its essentials, the premise of The Long Tail was simple: e-commerce, and e-commerce stores such as Amazon, made it possible for retailers to stock many, many more items than any physical retailer could. In books, music, videos, and many other categories, physical retailers were forced to concentrate on the best-selling items—those that turned over reasonably quickly, and could justify their expensive shelf space on premium retail sites in town centres and shopping malls. E-commerce made it possible to stock—and sell—the remainder of the range: the so-called 'tail', stretching all the way down to items that sold far less frequently, but which cost little to stock in vast warehouses located in inexpensive industrial parks.

Better still, the 'tail' was arguably more profitable: whereas physical retailers competed fiercely among themselves to sell the bestsellers, hacking into profit margins by cutting the price, this wasn't so necessary with respect to the 'tail': consumers were simply happy to find the item on sale at all. And even better, recommendation engines made it possible to proactively mine the tail so as to bring it to the attention of consumers who might not otherwise have been aware of it.

Anderson provided a compelling example of the tail in action: a little-known book published in 1988 called Touching the Void, in which British mountain climber Joe Simpson related a harrowing account of near-death in the Peruvian Andes. Soon forgotten, the book largely disappeared from sale, despite good reviews. But a decade later, Into

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Thin Air, another book about a mountain-climbing tragedy, by climber and writer Jon Krakauer, became, as Anderson puts it, "a publishing sensation".

Online reviews on Amazon noted its similarities to Touching the Void, prompting purchases of it, leading to Amazon's recommendation engine pointing out to customers that 'people who bought Into Thin Air also bought Touching the Void'. By 2004, related Anderson, Touching the Void was outselling Into Thin Air by more than two to one. Better still, Amazon began promoting the sale of both books as a packaged pair. Not bad for a book that was originally almost out of print.

As consumers, we perhaps now take all this for granted. But as retail, logistics, and supply chain professionals, we see things slightly differently. We see e-commerce creating a whole new business model, a whole new competitive paradigm. Initially conceived as a way of profiting through disintermediation—cutting out wholesalers, physical retailers, and other intermediaries—and selling directly to end-consumers, we see now e-commerce rewriting the rules of retailing, offering a hugely extended assortment, but also attractive pricing and delivery times.

Fast fashion and consumer electronics, the long tail simply comprises a broader assortment: no one wants to buy last year's fashions, or a five-year-old television model.

Freed from the constraints of having to be located in consumer-friendly locations—town centres, shopping malls, and retail parks—e-commerce retailers also find themselves unshackled from the high costs of such locations: a warehouse can be built anywhere that land is cheap, transport access good, and labour is available. Nor does an e-commerce retailer's IT operation need to be co-located with the warehousing operation: again, this can be located where it best makes sense.

But not every e-commerce retailer is able to exploit 'long tail' capabilities in the same way—and therein lies the weakness in e-commerce retailing. For retailers such as Amazon, the long tail it offers embraces both a wide assortment of contemporary items as well as older items that no longer sell as strongly. But in—say—fast fashion and consumer electronics, the long tail simply comprises a broader assortment: no one wants to buy last year's fashions, or a five-year-old television model. In such scenarios, a competitive stance involves building an ever-larger assortment, at the cost of an ever-larger inventory. Zalando, for instance, presently stocks 3,000 brands across its European operations, and has announced an intention to increase that to 6,000 brands.

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The brand is the product, and competition is largely price-based.

Consequently, as a rule of thumb, the lower the importance of the long tail to the business model, then the more important that disintermediation and pure price-based competition become. Worse, factors that help physical retailers in the fight against pure price-based competition often don't apply in the e-commerce world, and so become irrelevant to consumers: forget convenient locations, easy parking, physical proximity, and personal service, for instance. Hence, for e-commerce retailers such as Boohoo and Asos, the more important it becomes to have distinctive brands, preferably brands that are exclusive to the e-commerce retailer themselves, in order to blunt the margin-sapping impact of price competition. But achieving that is often easier said than done: in popular online categories such as consumer electronics, mobile phones, books, DVDs, music, and games, the brand is the product, and competition is largely price-based.

E-commerce is no sinecure: it is easy to fail, and many e-commerce businesses do fail, especially if they have yet to build-up scale.

In short, sums up e-commerce expert Arnd Huchzermeier, Professor of Production Management at Germany's WHU Otto Beisheim School of Management, despite giving the appearance of being unstoppable, the reality of e-commerce is very different. Notwithstanding the attractions of the e-commerce business model—the long tail, no need to build up a chain of expensive physical stores, and the potential ability to reach many more customers than is possible with the footprint of a physical presence—e-commerce is no sinecure: it is easy to fail, and many e-commerce businesses do fail, especially if they have yet to build-up scale. As with Amazon's early days, profitability requires scale—fixed costs are high, and many may not achieve that scale before running out of cash.

"Traffic to e-commerce channels is very fragile, with consumers very ready to switch allegiance and shop elsewhere: a lot of companies underestimate the difficulties, and don't understand how easily they could find themselves without customers," he warns. "They need strong fulfilment partners, strong sourcing skills, and strong systems to deal with issues such as returns, fraud, and counterfeit products. And the required investment IT infrastructure is growing all the time—not just in terms of customer service, the customer online experience, and fulfilment, but also in data analytics and predictive modelling."

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WHU Otto Beisheim School of Management

Shaping a competitive response

How should retailers respond, then? What can physical retailers do to fight back against the onslaught from the e-commerce world? What can e-commerce retailers do, to better secure their own survival and eventual prosperity? How can both sets of retailers better address the weaknesses in their own particular retail models? And, intriguingly, are there any stratagems that benefit both physical retail and e-commerce retail?

One thing is clear: there is no silver bullet. That said, e-commerce's agenda is perhaps easiest to outline, if not actually achieve. And several strategies do suggest themselves.

The first is to blur the distinction between the online and physical worlds, in particular through joint ventures and tie-up with physical retailers. While that sounds perverse, the logic would be to piggyback on physical retailers' existing logistics networks so as to offer more of an omnichannel offering, in particular for reverse logistics. The attraction to the physical retailer from such tie-ups is twofold, says Selazar's Ashworth. First, they would see additional footfall, with potential customers visiting their stores for the purposes of (say) returning an item, but potentially making purchases while there. Second, their logistics networks would see higher utilisation, and a contribution towards fixed costs from the e-commerce retailer.

Second, e-commerce retailers can go even further in terms of 'final mile' logistics and fulfilment. Amazon's strategy in this area is well-known; doubtless, other retailers will follow, argues Hochschule Fulda University's Huth. While same-day deliveries are an untapped opportunity for most e-commerce retailers, he notes, delivering such a capability is expensive. That said, lock-up boxes and collection points are arguably easier to implement, and just as attractive an option to a perhaps broader category of consumer: not everything is required immediately.

Third, data. Again, companies such as Alibaba and Amazon are leading the way, points out the University of Manchester's Vazquez. Today, she notes, she is no longer teaching students about the power of social media in marketing: instead, she is teaching about AI, machine learning, process mapping, and interpreting data to better understand consumer needs and build better customer offers. It is no longer enough to simply be a retailer, she argues: companies will have to acquire these data skills, or partner with others who possess them.

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And fourthly, brands. Building distinctive brands differentiates e-commerce retailers, delivering loyal customers through making their websites 'sticky'. But building distinctive brands costs money, and takes time.

Hence the attractiveness of buying brands, instead—especially at a discount. As we have seen, Boohoo picked up failed Arcadia Group's Topshop, Topman, Miss Selfridge, and HIIT brands, to add to a collection of acquired brands that already included Karen Millen, Coast, Oasis, and Warehouse. But by adding Debenhams, Dorothy Perkins, Wallis, and Burton—bought at 'fire sale' prices—Boohoo was able to bring its offering to a whole new demographic: older, arguably wealthier customers. Starting from scratch might have taken years. Buying the brands—together with their headquarters brand-support and design teams—delivered the same thing at a stroke.

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What of physical retailing? As with e-commerce, several strategies suggest themselves.

First, as with e-commerce, physical retailers could make better use of customer data, argues the University of Manchester's Vazquez. It is sometime forgotten, she points out, that what enabled UK grocery retailer Tesco to overtake its competitor J. Sainsbury—the UK's then dominant grocery retailer—in the 1990s was Tesco's Clubcard loyalty programme. The ability to reward customer loyalty was simply a fringe benefit: the key thing about Clubcard was its ability to link electronic point-of-sale data to identifiable customers, about whom the retailer could build up an increasingly complete picture of their shopping habits, interests, and personal family circumstances.

The three-month experiment that led to Clubcard's inception—an experiment carried out by specialist analytics firm Dunnhumby—culminated in a presentation to a stunned Tesco board of directors. The reaction of Tesco chairman and former chief executive Lord MacLaurin is widely quoted.

What scares me about this is that you know more about my customers after three months than I know after 30 years," he reportedly told the husband and wife team who had founded and led Dunnhumby.

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Second, physical retailers could establish their own e-commerce operations, notes Hochschule Fulda University's Huth.

"In Germany, a lot of retailers are still not prepared to create an online shop," he observes. "And that's not just smaller, family-owned stores: even quite large firms have been slow to develop viable, working online operations."

That said, there are risks with this strategy, notes Jim Spittle, a former retail supply chain director, chair of the UK's NHS Supply Chain, past president of the Chartered Institute of Logistics and Transport, and an advisory board member and external examiner at Cranfield School of Management.

"Margins are thin, and the costs are high—not just picking, packaging and delivering, but also the circular economy and returns processes. E-commerce is certainly more convenient for the savvy shopper, but for the retailer, price competition, quality, and reputational risks are the dangers to watch. Counterfeit goods are a problem area, and one that is becoming larger."

Third, physical retailers possess insights and strengths not shared by online retailers, points out Clipper Logistics' Mannix: they physically 'touch' their customers.

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Jim Spittle
Chair NHS Supply Chain

"They know their customer in their own brand environment," he stresses. "They're not just meeting demand, as an online retailer does: they can urge a customer to try a product, or try-out an item of clothing for size or look, and so they have an opportunity to upsell, and influence. Online retailers struggle to do all those things. Physical retailers need to go back to their roots, emphasising the customer service they can offer, and exploiting their physical environment and presence."

And fourthly, physical retailers can exploit their brand and values to appeal to a growing number of consumers who are not primarily price-driven when choosing between retailers, but instead prefer to buy from brands that they perceive as sharing their own values and agendas.

"Going forward, it is likely that issues such as sustainability and social responsibility are going to be much more important," says Kees van der Vleuten, a former Royal Philips Electronics Supply Chain Executive, and now Managing Director and Chief Operating Officer of advisory firm KC MT Services. **"Consumers increasingly want to buy from ethical, sustainably-driven retailers. As e-commerce retail is often price-driven, a brand offering based around values can be a competitive differentiator."**

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Upskilling for the future

And what of the skills necessary to implement these various strategies? As always, so-called 'soft' skills are an important element. Leadership skills, change management skills, persuasion skills, influencing skills, and collaboration skills: most observers point to soft skills as the key to unlocking the changes that competing in the new retail landscape will call for.

"Physical retailers, especially, need a very different mindset," sums up Clipper Logistics' Mannix. "They're used to competing on the High Street, not in the warehouse, or through data analytics."

"Up until recently, retailers' focus has been on traditional retail skills, rather than on supply chain management," adds Hochschule Fulda University's Huth. "That's now changing: supply chain skills are becoming more important. But as supply chain management itself evolves, those skills are changing, too: IT skills are becoming more important, for example. At the moment, supply chain management education is often very business-focused, rather than IT-focused."

'T-shaped leader' has value when considering skill sets

Data analytics is another area where there is an imbalance, notes the University of Manchester's Vazquez. Look at industry leaders such as Amazon, she stresses: at present, few retailers—either physical or online—have anything like the skills required to compete with the industry's leaders in retail analytics. What is called for, she adds, is a significant amount of upskilling in most areas of data analytics.

Going forward, it's going to be much more important to have knowledge of things other than simply retailing or supply chain management.

Finally, the notion of the 'T-shaped leader' has value when considering skill sets, observes KC MT Services' van der Vleuten.

"Going forward, it's going to be much more important to have knowledge of things other than simply retailing or supply chain management," he concludes. "The key thing is to learn about other things, as well: learn about IT, learn about finance, learn about data analytics, learn about sustainability. Leaders need to know about retailing and supply chain management, of course, but they also need to acquire skills in these other areas, as well. In short: learn, learn, learn."

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