COMMENTARY: RETAIL STRATEGIES

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The Road to Consumer-Centric Retailing: Lack of Consumer Demand Preferences the Biggest Pothole

by Kevin Sterneckert

AMR Research recently completed a study to understand the trends in the merchandising decision areas of assortment management and space planning. We worked with 150 retailers to gain a perspective on the challenges, key value drivers, timing, and intended investment budgets in these two key areas across the specialty hardline, mass merchant, department store, and fast-moving consumer goods (FMCG) and softline segments.

Retailers recognized the need to improve their understanding of consumer demand. Even though many continue to use e-mail and Microsoft Excel to make assortment and space decisions, I sense a change in the wind—expect continued migration away from the traditional blocking-and-tackling tools to technologies that allow retailers to sense and shape demand. One reason for this could be that the dramatic shift in the economy, coupled with the emergence of a far more discriminating consumer, has caught many retailers unprepared for this new environment. They're expected to make new investments in these areas over the next 12 months as a result.

Each retail segment uses slightly different terminology to define assortment management and space planning. In this article, assortment management includes assortment planning and category management as used by apparel and FMCG companies, respectively. And while most apparel retailers aren't currently planning space allocations at the store or SKU level, there's a movement by many to determine macro-space allocations beyond historical techniques.

What are the challenges of assortment and space merchandising decisions?

Retailers reported current capabilities fall short of true consumer-centric retailing. They determine assortment and space decisions from a financial perspective and don't include consumer demand inputs in their decision process (see Figure 1).

However, retailers agreed the single largest objective is to have the ability to include consumer demand preferences in the planning process. The gap between performance and importance here illustrates the lack of current capabilities found in installed applications and the absence of functionality in a majority of the products available.

The study unveiled an interesting disagreement between business and IT leaders when asked about consumer demand insights. The gap between importance and delivered capabilities is smallest in the minds of IT leaders (13%), especially when compared to marketing (40%) and other business areas (30%), which believe there's still much more to do.

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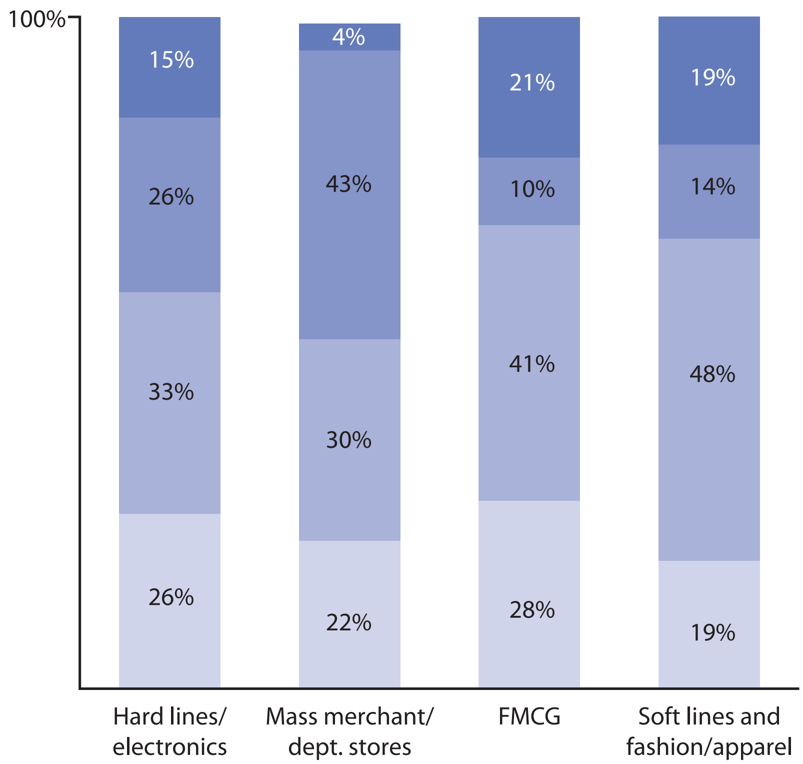
Figure 1: Process maturity



Level 1: We record the merchant decisions and forecasts and use as a guide throughout the buying process.

Level 2: We receive top-down corporate goals and objectives. All decisions are intended to deliver on these objectives.

Level 3: We receive top-down corporate goals and objectives and combine these with bottom-up planning through item planning activities.

Level 4: We examine consumer insight data along with syndicated sources to determine the bottom-up objectives. This is combined with corporate objectives to deliver a localized assortment and space allocation plan.

Q. Which of the following gives the best general description of your company's assortment management and space planning process?
N = 100 U.S. retailers

Source: AMR Research, 2009

Why are retailers improving their assortment and space management tools?

Idealistically, improvements to the assortment management and space allocation process should make organizations more consumer centric and thus more viable. But study results show there's a significantly more powerful reason for these improvements—profit. Investments in assortment management and space planning should enhance overall profitability and reduce stock levels. In fact, many respondents indicate these benefits are indeed very real.

Retailers also reported a significant improvement in on-shelf availability exceeding pre-project estimations. Although not entirely unexpected, the significant benefits opportunity indicates that sound assortment and space processes can play a significant role in on-shelf availability performance.

> *There's an improved understanding that SaaS and hosted applications provide a secure, reliable, and potentially less expensive alternative to the on-premises approach.*

Similar objectives can be seen through investments in space planning. However, most retailers understand improvements in space allocation will have a more granular impact on their businesses. Our study corroborates this, suggesting that, when compared to assortment management projects, space-planning initiatives are more likely to impact sales per square foot and reduce inventory levels.

When will leading retailers improve their assortment and space capabilities?

The answer to this question is a simple one: right now. Many retailers plan to make new investments in assortment and space tools within their next budget cycles. This translates to a large number investigating the capabilities of available products. Although the economy has changed the way companies invest in technology, assortment and space inquiries continue to bubble to the top of our inquiry lists, signaling a desire by many AMR Research clients to increase their investments in these tools.

Even though increased spending in key areas is anticipated, specific initiatives will vary between U.S. and European retailers. Expect to see heavier investments in assortment management by European retailers to take advantage of planning and size/pack optimization technology, which was an area pursued heavily by U.S. retailers in the past 12 months. Conversely, expect to see higher interest from U.S. retailers for inventory, allocation, replenishment, and order management, primarily based on higher maturity by our European counterparts (see Figure 2 on the next page).

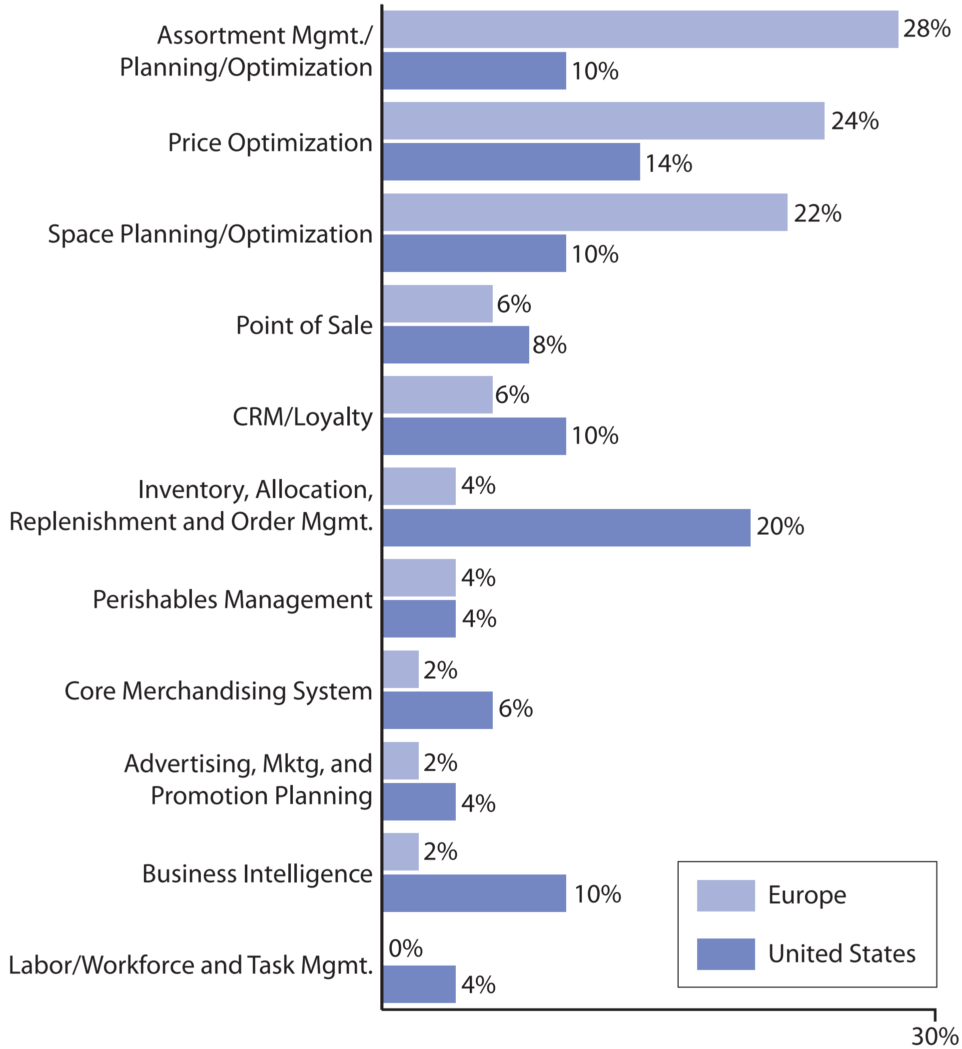
How will retailers improve their merchandising capabilities?

U.S. and European retailers agree budget approvals require significant business case justification and must satisfy three criteria:

- Demonstrate how the project impacts your company's income statement and balance sheet.
- Include a reasonable implementation plan that demonstrates improvements within 12 months. (European retailers reported they expect benefits within 9 months.)
- Create an organizational change management plan embraced by your business sponsors. Don't pretend Excel and e-mail will cease to exist in the assortment and space process. Create a transition plan instead that recognizes reality and charts a path to a post-Excel and e-mail platform.

More than 42% of retailers surveyed indicated they prefer best-of-breed technology for assortment and space, delivered either through software as a service (SaaS) or offsite hosting. This represents a significant shift from the traditional retail model of all applications sitting behind the firewall. It stems from an improved understanding that SaaS and hosted applications provide a secure, reliable, and potentially less-expensive alternative to the on-premises approach.

Figure 2: Europe vs. United States—consumer-centric merchandising technology priorities



Q. Q. Which is most important over the next year?

N = 50 European retailers / 50 U.S. retailers

Source: AMR Research, 2009

Don't forget your business value

Over the past 18 months, I've advocated infusing consumer demand insights into retailer merchandising decision processes. Although this research confirms many retailers embrace this perspective, the adoption pace is lagging behind, leaving significant business value on the table. U.S. and European retailers agree that improvements in assortment planning and space management capabilities accelerate consumer-centric merchandising proficiency, leading to profit improvements, reduced stock levels, and improvements in product availability.