



Envisioning the Future of

Integrated Retailing®

The Hottest Trends
at the Intersection
of Technology
and Merchandising

July 2007

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Consumer Behavior

What's most important to consumers?

Well, we all know that consumers weigh the attributes of price, quality, selection, product features, service, convenience, shopping experience, and provider knowledge. What might not be fully appreciated, however, is that according to a recent comprehensive survey by Gartner, consumers rank “making products easy to return” as the second most important service in the apparel segment, and third most important service in the department store segment. (“Having products in stock” is the No. 1 service requirement in all segments, by an overwhelming margin.)



Ask Dr. Roger

Will consumer spending hold up through the year?

Yes, by every indication, consumer spending will continue to grow through the rest of the year and beyond. Economic, employment, income and spending growth, although not spectacular, are all in positive territory. Any declines in the value of home equity are marginal and by no means permanent; the overall drag on the economy from the housing industry should decline in coming months (Moody's). Leading indicators, including new orders for consumer goods, are rising.

The resiliency of the US economy and American consumers are again trumping all predictions of doom and gloom. We have weathered the worst. The run-up in gas prices has hurt, but the effect has not been profound or lasting. Consumer sentiment may be restrained, but is not gloomy. There is no hint of recession anywhere on the horizon: economic conditions are good, equity markets are strong.

What this means for retailers: be prepared for breakouts – sudden explosions of consumer desire and spending for goods and services in high demand. As always, we counsel following trends, not fads, but anticipation and foresight are also rewarded!

How best to do this? Contact us for customized information!



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Considering that on average, across the retail industry, 9% of all sales result in merchandise returns, **returns management thus becomes a major front on the strategic battlefield.** This represents a particularly delicate challenge for retailers: most returns are perfectly legitimate, and customers expect their return transaction to be handled as smoothly, pleasantly and quickly as the original sale, yet fraudulent returns are a serious problem. (Some estimates put industry-wide returns fraud as high as \$16 billion per year.)

This challenge is compounded by the fact that most consumers now expect retailers to provide a **fully integrated, real-time multi-channel shopping environment.** Consumers want and expect to be able to buy merchandise through one channel – catalog or online, say – and return at the retail store. Most retailers do not yet offer these options; according to Gartner, only 18% fully coordinate planning of the fulfillment process across channels, and only 16% do so for returns management.

What's the solution?

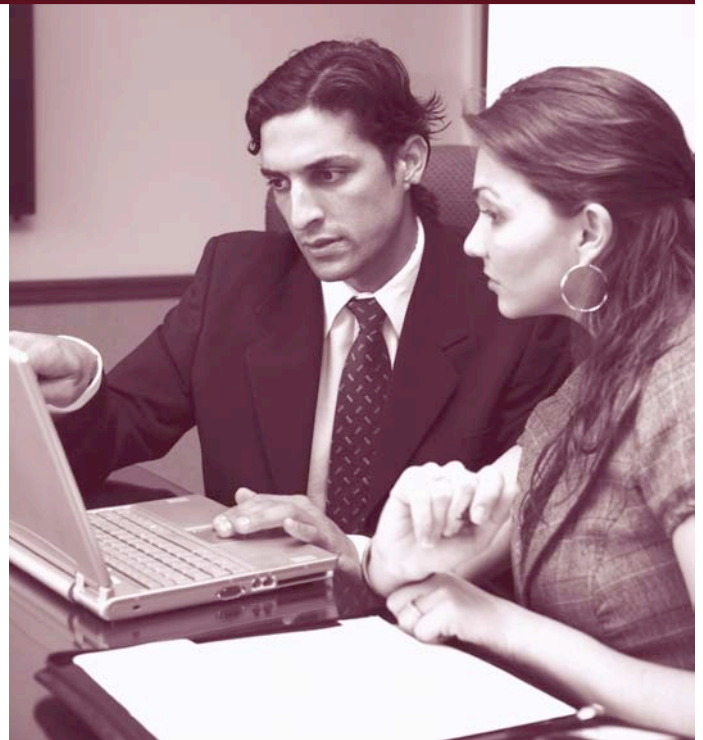
There are many types of fraud:

- Return of Stolen Merchandise
- Fraudulent Tenders
- Wardrobing
- Price Arbitrage
- Over-Refunding Legitimate Purchases

An enterprise-wide solution would require:

- Centralized, Real-Time Sales Updates
- Accurate Return Price
- Cross Channel Returns
- Simplified Employee Compliance
- Speed

Technologies and processes that make it easier for customers to return products through any



channel should move up the list of IT priorities. One firm that provides such software is **Epicor/CRS.** Its Returns Management application features:

- Transaction Repository
- Ease of Data Search
- Correct Price, Tax and Tender
- Centralized View Across Multiple Stores
- Multi-Channel Transactions for Improved Customer Service
- Ease of Use

The most immediate and quantifiable benefit of implementing a returns management system is a reduction of loss due to returns fraud (industry-wide, 9% of returns are fraudulent). **But a cross-channel returns capability, properly communicated to the customer base, would in and of itself constitute a differentiating competitive advantage, and provide potential for increasing both volume and loyalty.**

[For more information: www.crsretail.epicor.com]



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Business Strategies

Will department stores remain competitive?

Very much so, if they become true multi-channel retailers, with feature-rich web sites that are integrated into store environments and operations. True, department stores accounted for only 7% of non-automotive retail sales in 2004, down from 11% a decade earlier (A.T. Kearney). But the department store format, when updated, is still quite relevant to the shopping needs, wants and habits of the 21st century consumer.

Macy's multi-channel strategy, to take an industry leader's example, involves committing hundreds of millions of dollars to its stores, web site and distribution operations. According to Peter Sachse, chairman of **Macys.com**, the web site is far more than a selling channel – it's the online hub of the Macy's brand, a source of information, comparison shopping and consumer reviews, and a driver of traffic to stores.

Macy's multi-channel strategy starts from a good place: company research shows 98% awareness of the Macy's brand among women 25-54 with incomes of \$35,000 or more, and 63% of its \$22.4 billion in sales last year were in women's apparel, shoes, lingerie, accessories

and cosmetics. Further, the best Macy's customers shop both online and in stores: their multi-channel shoppers spend 20% more in stores than their average in-store shopper, and 60% more online than the average **Macys.com** shopper.

A key part of the company's strategy is to build Macy's as a national brand. In order to reach and convert its best customers, Macy's has increased its spending on online marketing and advertising, on catalog and Internet fulfillment (logistics and distribution), and on upgrading the web site to make it more appealing and more closely tied the Macy's stores and brand image.

One great feature (as per our item above): an Easy Returns link on the Macy's home page that clicks through to a page explaining how goods ordered online can be returned in stores or by mail.

Will online "pure-plays" remain competitive?

Profitable growth will become harder for purely Internet retailers which are not selling digital products and services exclusively. The theory of "The Long Tail" holds that there is cumulative profit in carrying an infinite supply of infrequently bought merchandise. But even bookseller **Borders**, after letting Amazon handle its online sales for 7 years, now realizes its future depends on having multiple integrated channels of its own.

So **Borders** is this month launching **bordersstores.com** as a marketing web site, which will evolve early next year into **borders.com** with e-commerce functionality. **Borders** sees its web site as much more than just a store: it's a brand vehicle, a merchandise vehicle, a marketing vehicle, a customer relationship tool and a consumer research tool. Visitors will be able to search a local store's inventory online, review books, reserve a book, and then pick it up at that store. Once in the store, customers will be able to access their accounts at any in-store kiosk.





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In other words, **Borders'** strategic plan for revitalization brings the store to the Web and the Web site to the store, **a winning strategy in our view. Borders** will integrate its customer loyalty program, customer service, fulfillment and analytics across channels. It will open digital centers in **Borders** stores that will enable customers to interact with and purchase new digital products and services (in-store or online).

So multi-channel is a retailing must?

Absolutely. Multi-channel capability drives customer service, relationships, value and loyalty. It will become increasingly difficult for any retailer to grow profitably in one channel alone.

Actually, it may make more sense to say "merged-channel" rather than "multi-channel," **which for too many retailers actually means "multi-silo-ed."**

A true merged-channel approach is a shock to the retail system. Everything is affected: incentives, organiza-

tion, marketing, metrics. How are customers using each channel for shopping, comparing, buying? If a shopper researches online but buys in-store, which channel gets credit for the sale? Has the shopper received a catalog or email? A true merged-channel retailer would use technology in all of its channels to be collect and analyze such data. Management would then be able to make informed decisions about inventory, staffing, pricing, promotions, etc.

A true merged-channel retailer presents a consistent, seamless experience to the consumer, and provides a unified view of the enterprise, products and consumers to the retailer. Both customer and retailer benefit greatly when such a relationship is established, maintained and strengthened.

Connecting Technology

Who is providing the technology?

Borders Group Inc. has contracted with several leading technology vendors for the new multi-channel platform it is launching next year. **Sterling Commerce** will provide order management and fulfillment for the Web site. Customers will be able to buy online and pick up or return in-store, or go to a store, find what they are looking for in the inventory at another store and order that item to be delivered to their home.

Omniture Inc. will provide the analytics side of the equation, giving the ability to tie together specific offline events. **IBM's Sales Center for WebSphere Commerce** will provide the customer service application. Sales Center is a customizable cross-channel solution that enables contact agents to work with multiple stores, orders and customers simultaneously, view cross-sell and promotional information, find and compare products, and view product availability as well as view or take control of the customer cart.





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Customer Service

What is customer-centricity?

At **Best Buy**, customer-centricity means treating each customer as a unique individual, meeting their needs with end-to-end solutions, and engaging and energizing employees to serve them. Increasingly this means delivering integrated solutions to consumers, as well as innovative products and services.

By listening to customers and employees more closely, **Best Buy** is benefiting from new ideas that in the past would never have reached corporate headquarters. Through employees that regularly engage with customers, the retailer has discovered several growth opportunities. Those with the highest potential include **small-business customers, new services offerings, and international growth**, which together accounted for a total of \$230 billion in company revenue last year.

Best Buy invites input from approximately 120,000 sales associates in over 1,150 stores in the US, Canada and China, tapping into the one million hours they spend daily with customers. From this input **Best Buy** has segmented its customer base into basic lifestyle groups. The purchasing officer is identified for each segment and an associated purchasing index is developed. Data is collected and analyzed, and intelligence extracted for product development and redesign, new business model development, and new service offerings.

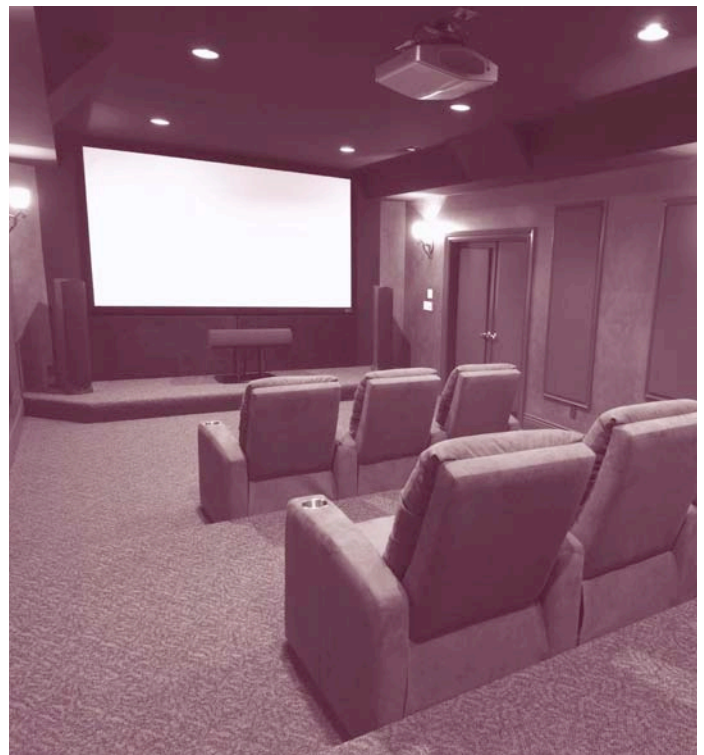
The results are impressive, and are there for everyone to see. **Best Buy** has 40% of its US stores operating under the consumer-centric model. The number of Geek Squad agents has grown to 5,000 and home theater installation services were brought in-house to provide a better and more consistent customer experience. **Membership in the Reward Zone customer loyalty program has reached 7.2 million**

and as a result, **Best Buy** has learned more about customer purchase patterns than ever before.

Best Buy is developing an extraordinary core competence by gathering and synthesizing customer intelligence. This is allowing the retailer to advance collaboration with suppliers, while also building a huge competitive private label business for itself.

The consumer electronics (CE) industry is immense (projected to reach \$200 billion by 2010), growing rapidly (20% growth 2005-2010), highly innovative (20,000 new products a year), very competitive (net margins are still only about 2% to 4%), and consolidating (in 2005 the top three retailers – **Best Buy, Wal-Mart and Circuit City** – accounted for 48% of the North American market, a 33% increase over 2001). It will take great strategy and excellent execution to be a winner in this market.

Customer-centricity is **Best Buy's** primary competitive business strategy. It means innovative products and services, targeted markets, integrated solutions, and merged-channel execution. **It's a winning strategy.**





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Entertainment Retailing

Experiential tourism

L.L. Bean plans to develop a 700-acre outdoor adventure center near its flagship store in Freeport, Maine, with the goal of creating a national recreation destination. Visitors might hike, bike, golf, cross-country ski, or go kayaking, seal watching or fishing in nearby Cisco Bay. Then they could eat and stay the night on the property.



The company also hopes these visitors would stop by the flagship store and buy products and services to help them enjoy the activities. The overarching goal, the company says, “is to expand our relationship with our customers, and enhance the customer experience.”

As a concept, Bean envisions a “family-friendly outdoor adventure attraction with lodging amenities under something similar to a theme park operating mode.” The lodging facility could be branded as L.L. Bean, or could be independently or nationally branded with a Bean reference. Outdoor-oriented amenities and facilities are critical, of course, to fit with the L.L. Bean brand image and support retail sales.

Is this a savvy move?

Very much so. Roughly 3 million people walk through the Freeport stores every year, making L.L. Bean Maine’s second-most popular tourism destination behind Acadia National Park. In recent years, Bean has branched out into recreation through its Outdoor Discovery Schools, where customers take lessons for activities like fly-casting or kayaking. **These activities are very popular, and Bean has found they generate good customers who buy products.**

Creating a destination adventure center such as the one being discussed – where people can stay and participate in these and other outdoor activities – takes the formula to a higher level, and would propel Bean from being a store, mail-order retailer and a brand into a full-fledged outdoor experience. Bean is on a fast track to make the project happen: it plans to pick finalists early next month to submit proposals for how to develop the project, and wants to see the theme park operating within three years.

Bean operates seven full-price retail stores and 14 outlets on the East Coast. It plans to open 35 more full-price stores within five years, and future stores also could be linked to outdoor adventure centers in other states. **Experiential tourism is a trend with staying power – people increasingly want to combine leisure, travel, learning and family vacation time – and adding retail to the mix is a brilliant gambit.**

Still, the project represents a major undertaking and expansion of strategic direction for Bean, a family-owned company with net revenue last year of \$1.54 billion, an increase of 4.6% over 2005. In-store retail sales shot up 14% as the company continued to open stores, but for the first time L.L. Bean’s web site produced more revenue than its stores or catalogs. The web site recorded 73 million visits in 2006, an increase of 13% over 2005. L.L. Bean remains a big catalog retailer, mailing more than 300 million a year.



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Communication Strategies

How should retailers use direct marketing?

They should follow the lead of **Williams-Sonoma** (parent of **Pottery Barn**), which will supercharge its use of database marketing this year in an attempt to take customized, direct-to-consumer appeals to a level never done before in retailing. The company's advanced marketing platform is being used to create new appeals uniquely framed for email customers vs. retail customers, frequent shoppers vs. newcomers, and other profiles.

Williams-Sonoma is another retail industry leader executing a multi-channel strategy. It is opening stores – the company will open five **West Elm** and two **Williams-Sonoma Home** units this year, including a super-sized **West Elm** store in downtown Washington, D.C. that will twice the size of existing stores (40,000 sq. ft. vs. the usual 20,000). But e-commerce will

exceed \$1 billion this year, contributing over 25% of total corporate revenue.

Over one-third of new **Williams-Sonoma** customers are acquired through its web sites. When the company sent an email to customers who had browsed for a particular item, response was nine times that of typical email offers. When the company targeted an offer to customers who had already bought an item in **Pottery Barn's** Chesapeake furniture collection, response jumped to 18 times the norm.

Targeted email will increasingly be recognized as one of the most efficient, productive and profitable methods of direct marketing any multi-channel retailer can undertake.



Merging Operations

How important is in-store pickup?

It's becoming a major point of competitive differentiation. Well-known pioneers include **Circuit City**, **CompUSA**, **Wal-Mart**, **Best Buy** and **Sears**, but even smaller multi-channel players like **Bombay Co.** are providing in-store pickup for web orders as part of an overall strategy to improve customer service and increase profitable growth. To stay ahead of the curve, some retailers have even begun adding perks such as reserved parking spots, special checkout lines and in-store signage directing consumers to the pickup area.

Wal-Mart has launched a program that offers free shipping to customers who purchase items online and have them shipped to one of the company's stores instead of their homes. Shipments for site-to-store customers will arrive on the same trucks as other deliveries. Once employees scan the items, customers will receive e-mails notifying them that their purchases have arrived.





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According to a survey the company sent to customers who used the service during a trial period, about half of them spent an additional \$60 in Wal-Mart stores when they went to pick up their online purchases. Customers who use the service already are among Wal-Mart's most loyal; the trial-period surveys also showed that two-thirds of site-to-store customers shop weekly at Wal-Mart stores. CompUSA says customers who buy online and pick up in stores spend 35% more than customers who shop only in stores.

Some retailers offer in-store pickup of web orders across most categories; others limit the service to items that can be carried out of the store. Wal-Mart's service allows customers access to thousands of items that only are available online; top-sellers have included an LCD television and children's furniture. The service also helps the retailer's sustainability efforts (see the June issue of *Integrated Retailing*), because consolidating shipments permits the company to put fewer trucks on the road, using less fuel and fewer cardboard boxes.

Radio Shack launched its ship-to-store program in 1,300 company-owned stores last November. Their aim is to get online shoppers to stores for up-selling and cross-selling. Radio Shack plans to roll out the

program to 3,400 franchises this year. Besides avoiding shipping fees, customers can use the service to purchase products like hot video games before they are available in general release.

In-store pickup of items ordered online is a service multi-channel retailers will need to offer and expand to stay competitive, please consumers, and grow profitably.



Upcoming Appearances

Shopper Insights in Action

Integrated Retailing is a media partner with the 7th annual **Shopper Insights in Action Conference**. Presented by the **Institute for International Research**, the conference unites retailers, brands and industry experts to share research practices and actionable case studies that turn insights into winning retail strategies.

The conference is scheduled for July 11-13 at the Chicago Marriott Downtown on the Magnificent Mile. Agenda and registration information is available at <http://www.iir.com> and <http://www.shopperinsights.com>. As a reader of *Integrated Retailing*, you are invited to attend the conference at a discount; use priority code XM1915REM.

Hispanic Boom 2007

Dr. Roger Selbert keynoted the **2007 Hispanic Boom** conference, presented by the **Strategic Resource Institute**, in Los Angeles last month. An audio recording of the presentation, plus an interview with Dr. Roger, are available for listening or podcast at <http://www.hispanicmpr.com>. Scroll down to "Hispanic Projections." The power point presentation that accompanied the presentation may be requested; email roger@integratedretailing.com.

