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Staying Afloat on the Retail Wave

In this time of relative retail buoyancy, retailers can still find themselves in financial difficulty. **James Stewart** and **Kevin Winterburn** examine why.



Arguably, the retail market in Australia has never been more challenging. We have now seen 15 years of record economic growth, a very strong stock market, high housing prices – and strong retail growth, particularly since 2001. Yet even in this time of relative retail buoyancy, retailers (even major retailers) still find themselves in financial difficulty. There are three key reasons why retailers get into serious trouble, or even fail.

- 1 **Failure to reinvent the brand;**
- 2 **The inability to create and sustain a winning product offer; and**
- 3 **A failure to understand and implement basic retail principles.**

1 The Failure to Reinvent

The retail lifecycle of many retailers is already short. And its getting shorter because...

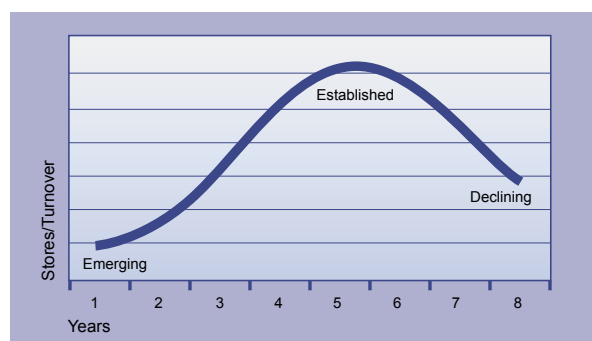
- **Consumers change** (their tastes, preferences and habits).
- **New competitors enter the market** (presenting consumers with an ever expanding array of choice).
- **Society evolves more quickly than anticipated** (highlighting which brands are in step with the times – and which have dated).

A retail lifecycle essentially consists of three phases; **Phase 1** – is the time it takes to develop and launch a retail brand/concept, the development phase.

Phase 2 – is the point in time when the business reaches financial maturity (sometimes correlating with market saturation).

Phase 3 – is the time when a business' rate of growth and performance begin to falter and then almost invariably decline.

The key challenge for retailers today is not only to reach the top of the lifecycle curve as quickly as possible, but then to stay there by continually fine-tuning or reinventing the brand to stave off Phase 3.



In the last seven years we have seen the collapse of a number of iconic Australian retailers:

- The Sportsgirl/Sportscraft Group (1999);
- Harris Scarfe (2001);
- Collins Booksellers (2005); and
- Lincraft (2005) and Gowings (2005).

Each of these retailers have a rich history and, at one time, was a leader in its chosen field. Each either failed to differentiate itself in a relevant way and/or failed to move with the times. More astute brands have worked hard to stay relevant and attractive.

McDonalds has spent the last three years undertaking a major brand repositioning exercise. By 2002 McDonalds was struggling for the first time. It incurred its first loss since 1954. McDonalds' research found that after 20 years at the top of the fast food business, it had failed to retain a whole generation of children who had grown up eating Big Macs and fries. These customers (now adults) had moved on because they wanted healthier options and greater variety.

In 2003, McDonalds changed its core strategy away from growing stores to growing customer visitations.

Achieving this involved a dramatic change in brand image and product offering – to reposition the brand as being for adults (not just children) and for those who wanted healthier meals rather than the traditional hamburger and fries.

In 2005, McDonalds' turnover was up 33% on 2002 (to over US\$20 billion). Over the same period profits were up 191% to US\$2.6 billion. Significantly, this result was achieved while holding total restaurant numbers virtually constant (at 31,890 worldwide)*.

Good retailers, big or small, need to continually reinvent their brand to stay relevant to their customers.

Did you know...

- Myer Melbourne is the second largest retail store (in size) in the world. It ranks second to only Macy's, New York
- In 1985 Department Stores held a 7% market share of total retail spend in Australia. By 2005 that share had shrunk to under 4%.
- Department stores in the US shopping centres usually own their retail space. In Australia, the converse is increasingly the case.
- Regional shopping centres in the US do not, usually, include supermarkets or food courts in their tenancy mix. Again, it's the opposite here.
- The world's largest retailer, WalMart, had annual sales growth in 2005 (USD 30 billion) that was larger than the total turnover of Coles Myer in that year.

2 Product Balance

In retail, product is **everything**. No degree of operational excellence will save you if your product and product mix are not right. Underperforming retailers typically offer product which:

- Fails to make a statement (or, more accurately, a statement that brings the brand promise to life);
- Lacks differentiation; and
- Lacks balance (in terms of basics, fashion and highlight items).

Ongoing success in retail is all about product reflecting the brand's positioning in the market. More specifically, success requires that there is a strong focus on product which:

- Captures the imagination (including the emotional needs) of the target customer;

*Source: McDonalds 2005 Annual Report

- Is consistent with (and expressive of) the retailer's brand positioning and theme;
- Meets optimal quality parameters; and
- Is carefully priced to reflect both economic and emotional value.

If product lacks relevant differentiation it usually indicates a retailer that's content with a 'me too' business strategy.

Peter Williams (the former CEO of Selfridges of London, the English icon) asks the seminal question "given there is so much stuff for people to buy, why shop with you?"

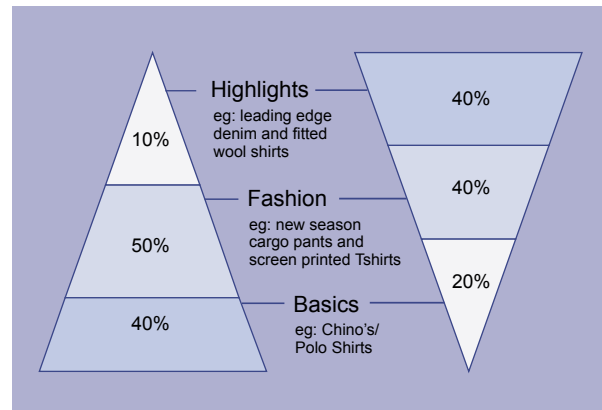
Any retailer who can't answer this question convincingly is in serious trouble because she/he can only fight the competition on convenience and/or price, strategies that almost invariably lead to lower profitability over time.

Card & Gift Stores: An Example

Symptoms of Product Losers	Symptoms of Product Winners
<ul style="list-style-type: none"> • Attend the same gift fares 	<ul style="list-style-type: none"> • Resource independently
<ul style="list-style-type: none"> • Buy from the same importers and wholesalers 	<ul style="list-style-type: none"> • Source globally
<ul style="list-style-type: none"> • Are selling agents for the card companies 	<ul style="list-style-type: none"> • Are buying agents for their card customers

Another key to success is product balance or mix. A balanced product mix means the retailer has got the right proportions between the **basics** (which are the backbone of a business and should be in-stock all the time), the **seasonal** fashion items (that provide product 'newness' to the offer and freshness that prompts a higher frequency of customer visits) – and the **highlights** (that strengthen the aspirational pull of the brand).

In your typical men's fashion retailer, for example, a balanced stock mix may look something like the pyramid on the **left**.



Many retailers (and particularly those under financial stress) tend to get their stock balance wrong, as per the pyramid above on the **right**. This often occurs as a result of the drive for **cash flow** overtaking the drive for **profit**.

A retailer with an 'unbalanced' stock mix is usually displaying one of the **first symptoms** that something is **seriously wrong**.

3 Retail Execution

Running a retail business well is the third prerequisite for success. A sound understanding of basic retail principles – and a relentless commitment to their execution on a day-to-day basis is the key. Among the most important of these principles are:

Sales Forecasting

One of the biggest, and most common, mistakes we see is a very understandable one. It's over-optimism. Many retailers are simply unrealistically optimistic in their sales and profit forecasting, particularly when it comes to new stores or new brands.

When these overly optimistic forecasts can't be achieved discounting usually follows (to clear stock) which puts pressure on the cost of doing business and profit.

A common mistake many retailers make when forecasting sales is to adjust their sales target to produce a 'good-looking' sustainable, occupancy cost percentage. Instead they should adjust the occupancy cost in anticipation of the likely outcome.

Forward Order (OTB) Planning

A lot of retailers argue that stock turn is the single, most important contributor to retail profit. Forward order planning (open to buy – OTB) is the key to achieving both stock turn and gross margin outcomes. It's the tool good retailers use to identify how much product they want and when they want it (to achieve their sales and margin targets).

In spite of this, it's amazing just how many retailers have inadequate or no forward order planning procedures.

Product Mix Planning

Having the right amount of stock won't work unless the mix of that stock is also correct. Both are required to achieve budgeted margins. Getting those essential 'level' and 'mix' questions right involves the use of product planning tools that help determine the correct product assortment (categories and range). Without the effective use of planning tools (product family tree, category planning, range assortment planning), the assortment mix can quickly become unbalanced and put severe pressure on sales and margin targets.

Margin Planning

Good retailers are sophisticated enough to calculate both their **first margin** (initial or full selling price less Cost of Goods ('COGs')) and their **final gross margin** (initial price – less markdowns – less COGs).

The widespread, and growing, use of **discounting** as a marketing tool means it's essential for retailers to plan for promotional markdowns and the markdown required to clear distressed stock.

Event Planning

Few successful retailers are brave (or silly) enough to just open their doors and wait for things to happen. Nothing very much happens in retail unless you make it happen. Good retailers **plan** activities to drive sales. Such activities or events can include:

- Calendar events (eg: Valentine's Day);
- Advertising;
- In-store promotions;
- E-mail communication;
- Window displays;
- In-store visual presentations; and
- Store staff incentives.

Staff Rostering

Finally, store wages are the biggest, single controllable expense at store level.

Retail is a game of percentages and every percentage saved on operating costs goes straight to the bottom line.

All successful retailers know this, so it is surprising that so many retailers have only a rudimentary knowledge of how to roster staff properly. Effective rostering can significantly reduce the percentage of labour costs to sales. Staff rostering should cover full timers; part timers; casuals and should be matched to peak traffic times to meet customer demand.

4 Summary

In this article we have covered a lot of ground discussing brand, product and operational issues. The lessons learnt from all that experience can be condensed into what we consider are the five characteristics of successful retailers.

Successful Retailer Characteristics

- A tight focus on their target market(s) and product offer. Such a tight focus enables them to differentiate themselves from their competition and to update/reinvent themselves on-time;
- The understanding and skills to communicate their brand story and product offer clearly, strategically, and in a timely fashion;
- Excellent product planning and stock management skills;
- Strong management information platforms that enable performance benchmarking on a weekly (or even daily) basis; and
- People chemistry. People with the right skill sets, an appropriate organisational structure and the right culture to get everyone singing off the same song sheet!



James Stewart,
Partner & Group Retail Practice
Leader, Melbourne
phone: 0419 305 807
email: jstewart@melb.fh.com.au



& Kevin Winterburn
Retail Specialist, Melbourne
phone: 0419 877 250
email: kwinterburn@melb.fh.com.au

For more information about our Retail Services please contact:

Sydney: John Melliush
+61 2 9286 9999
john.melliush@syd.fh.com.au

Melbourne: James Stewart
+61 3 9600 4922
jstewart@melb.fh.com.au

Brisbane: Will Colwell
+61 7 3831 4833
wcolwell@qld.fh.com.au

Adelaide: Martin Lewis
+61 8 8100 7600
mdlewis@sa.fh.com.au

Perth: Martin Jones
+61 8 9214 1444
mjones@perth.fh.com.au

New Zealand: Brendon Gibson
+64 9 307 7865
brendon.gibson@ferriers.co.nz

Asia: Rod Sutton
+852 2820 5600
rsutton@fh.com.hk

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