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SPOTLIGHT ON REINVENTING RETAIL

The Future of Shopping

Successful companies will engage customers through “omnichannel” retailing: a mashup of digital and physical experiences. *by Darrell Rigby*

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Spotlight



ARTWORK Rachel Perry Welty
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It's a snowy Saturday in Chicago, but Amy, age 28, needs resort wear for a Caribbean vacation. Five years ago, in 2011, she would have headed straight for the mall. Today she starts shopping from her couch by launching a videoconference with her personal concierge at Danella, the retailer where she bought two outfits the previous month. The concierge recommends several items, superimposing photos of them onto Amy's avatar. Amy rejects a couple of items immediately, toggles to another browser tab to research customer reviews and prices, finds better deals on several items at another retailer, and orders them. She buys one item from Danella online and then drives to the Danella store near her for the in-stock items she wants to try on.

As Amy enters Danella, a sales associate greets her by name and walks her to a dressing room stocked with her online selections—plus some matching shoes and a cocktail dress. She likes the shoes, so she scans the bar code into her smartphone and finds the same pair for \$30 less at another store. The sales associate quickly offers to match the price, and encourages Amy to try on the dress. It is daring and expensive, so Amy sends a video to three stylish friends, asking for their opinion. The responses come quickly: three thumbs down. She collects the items she wants, scans an internet site for coupons (saving an additional \$73), and checks out with her smartphone.

As she heads for the door, a life-size screen recognizes her and shows a special offer on an irresistible summer-weight top. Amy checks her budget online, smiles, and uses her phone to scan the customized Quick Response code on the screen. The item will be shipped to her home overnight.

This scenario is fictional, but it's neither as futuristic nor as fanciful as you might think. All the technology Amy uses is already available—and within five years, much of it will be ubiquitous. But what seems like a dream come true for the shopper—an abundance of information, near-perfect price transparency, a parade of special deals—is already feeling more like a nightmare for many retailers. Companies such as Tower Records, Circuit City, Linens 'n Things, and Borders are early victims—and there will be more.

Every 50 years or so, retailing undergoes this kind of disruption. A century and a half ago, the growth of big cities and the rise of railroad networks made possible the modern department store. Mass-produced

automobiles came along 50 years later, and soon shopping malls lined with specialty retailers were dotting the newly forming suburbs and challenging the city-based department stores. The 1960s and 1970s saw the spread of discount chains—Walmart, Kmart, and the like—and, soon after, big-box “category killers” such as Circuit City and Home Depot, all of them undermining or transforming the old-style mall. Each wave of change doesn't eliminate what came before it, but it reshapes the landscape and redefines consumer expectations, often beyond recognition. Retailers relying on earlier formats either adapt or die out as the new ones pull volume from their stores and make the remaining volume less profitable.

Like most disruptions, digital retail technology got off to a shaky start. A bevy of internet-based retailers in the 1990s—Amazon.com, Pets.com, and pretty much everythingelse.com—embraced what they called online shopping or electronic commerce. These fledgling companies ran wild until a combination of ill-conceived strategies, speculative gambles, and a slowing economy burst the dot-com bubble. The ensuing collapse wiped out half of all e-commerce retailers and provoked an abrupt shift from irrational exuberance to economic reality.

Today, however, that economic reality is well established. The research firm Forrester estimates that e-commerce is now approaching \$200 billion in revenue in the United States alone and accounts for 9% of total retail sales, up from 5% five years ago. The corresponding figure is about 10% in the United Kingdom, 3% in Asia-Pacific, and 2% in Latin America. Globally, digital retailing is probably headed toward 15% to 20% of total sales, though the proportion will vary significantly by sector. Moreover, much digital retailing is now highly profitable. Amazon's five-year average return on investment, for example, is 17%, whereas traditional discount and department stores average 6.5%.

What we are seeing today is only the beginning. Soon it will be hard even to define e-commerce, let alone measure it. Is it an e-commerce sale if the customer goes to a store, finds that the product is out of stock, and uses an in-store terminal to have another location ship it to her home? What if the customer is shopping in one store, uses his smartphone to find a lower price at another, and then orders it electronically for in-store pickup? How about gifts that are ordered from a website but exchanged at a local store? Experts estimate that digital information already in-

Idea in Brief

A decade after the dot-com implosion, traditional retailers are lagging in their embrace of digital technologies.

To survive, they must pursue a strategy of omnichannel retailing—an integrated sales experience that melds the advantages of physical stores with the information-rich experience of online shopping.

Retailers face challenges in reaching this goal. Many traditional retailers aren't technology-savvy. Few are adept at test-and-learn methodologies. They will need to recruit new kinds of talent. And they'll need to move away from analog metrics like same-store sales and focus on measures such as return on invested capital.

Traditional retailers must also transform the one big feature internet retailers lack—stores—from a liability into an asset. They must turn shopping into an entertaining, exciting, and emotionally engaging experience. Companies like Disney, Apple, and Jordan's Furniture are leading the way.

fluences about 50% of store sales, and that number is growing rapidly.

As it evolves, digital retailing is quickly morphing into something so different that it requires a new name: omnichannel retailing. The name reflects the fact that retailers will be able to interact with customers through countless channels—websites, physical stores, kiosks, direct mail and catalogs, call centers, social media, mobile devices, gaming consoles, televisions, networked appliances, home services, and more. Unless conventional merchants adopt an entirely new perspective—one that allows them to integrate disparate channels into a single seamless omnichannel experience—they are likely to be swept away.

An Industry Stuck in Analog

Why will digital retailing continue to grow so fast? Why won't it peak sometime soon, or even implode the way it did the last time around? Anyone who has shopped extensively online knows at least part of the answer. The selection is vast yet remarkably easy to search. The prices are good and easily compared. It's convenient: You can do it at home or at work, without using gasoline or fighting to park. Half of online purchases are delivered free to U.S. consumers—up 10 percentage points over the past two years. Many returns are free as well. Product reviews and recommendations are extensive. Little wonder that

the average American Customer Satisfaction Index score for online retailers such as Amazon (87 points) is 11 points higher than the average for physical discount and department stores.

The advantages of digital retailing are increasing as innovations flood the market. For instance, Amazon has already earned valuable patents on keystone innovations such as 1-Click checkout and an online system that allows consumers to exchange unwanted gifts even before receiving them. Digital retailers drive innovation by spending heavily on recruiting, wages, and bonuses to attract and retain top technical talent. They were also among the first to utilize cloud computing (which dramatically lowers entry and operating costs) and to enhance marketing efficiency through social networks and online advertising.

Customers are out in front of this omnichannel revolution. By 2014 almost every mobile phone in the United States will be a smartphone connected to the internet, and an estimated 40% of Americans will use tablets such as the iPad. If you doubt whether consumers are ready for technology-driven retail solutions, find a “dumb” video display in any public location and look for fingerprints on the screen—evidence that people expected it to be an interactive touchscreen experience.

Meanwhile, traditional retailers are lagging badly. Online sales account for less than 2% of revenue at

Amazon's five-year average return on investment is 17%, whereas traditional retailers average 6.5%.

Walmart and Target. Nor are traditional retailers pioneering digital innovations in other channels, such as mobile shopping and call centers, or seamlessly integrating these technologies in their most important channel—physical stores.

It's not surprising that these retailers are bringing up the rear. As a consultant, I often walk through stores with senior retail leaders whose knowledge of physical retailing is impressive: They know precisely where a fixture should be, exactly how lighting is likely to affect sales, and which colors work best in which departments. As a group, however, they are shockingly subpar in computer literacy. Some retail executives still rely on their assistants to print out e-mails. Some admit that they have never bought anything online. Technophobic culture permeates many great retail organizations. Their IT systems are often old and clunky, and knowledgeable young computer geeks shun them as places to work.

Retailers tend to focus on the wrong financial metric: profit margins. If a change dilutes margins, it's bad. But Bain's research shows that retailers' stock prices are driven by return on invested capital and growth rather than by margins. Amazon's five-year operating margin is only 4%—far below the 6% average for discount and department stores. But with faster inventory turns and no physical store assets, Amazon's return on invested capital is more than double the average for conventional retailers. As a result, Amazon's market value, \$100 billion, is roughly equivalent to that of Target, Best Buy, Staples, Nordstrom, Sears, J.C. Penney, Macy's, and Kohl's combined.

Conventional retailers haven't had great experiences with breakthrough innovation. They are most comfortable with incremental improvements and with following the well-known dictum "Retail is detail." Too many store reinvention programs have launched with great fanfare, only to

Technophobic culture permeates many retailers, and young computer geeks shun them as places to work.

But it isn't just computer illiteracy that holds traditional retailers back. Four other factors are at work as well.

Retailers were burned by e-commerce hype during the dot-com bubble. Many created separate online organizations to maximize valuations. The separate organizations targeted different customer segments, inhibited collaboration, and created serious frictions and jealousies. When the predictions of dot-com domination proved wildly optimistic, overpriced acquisitions began failing, and store organizations smugly celebrated. A decade later, real collaboration between retailers' store and digital operations remains rare.

Digital retailing threatens existing store economics, measurement systems, and incentives. Traditional retailers live and die with changes in same-store sales, in-store sales per labor hour, and compensation systems based on such metrics. That was fine when online sales were 2% to 3% of revenues, but the whole system falls apart when that number reaches 15% to 20%.

die unceremonious deaths. Propose a more novel approach and retailers will ask why, if it's such a good idea, nobody else is doing it.

Retailers tend to believe that their customers will always be there. But as customers grow more comfortable with omnichannel shopping, they grow less tolerant of what they encounter in stores. Sales associates are hard to find. When you find one, he or she doesn't know much about the merchandise. Stockouts are frequent, checkout lines long, returns cumbersome.

An omnichannel world, in short, represents a major crisis for traditional retailers. Customers are passing them by. Online players are gaining. To keep up, existing retailers will need to create an omnichannel strategy—and pick up the pace of change.

Redesign Shopping from Scratch

The first part of any such strategy is facing reality. Retailing executives must acknowledge that the new technologies will get faster, cheaper, and more versatile. They need to forecast the likely digital density

How Fast Is Your Industry Moving Online?

Online competition increases predictably as online prices, selection, convenience, and customer trust improve relative to physical stores. Here's how three industries scored for key drivers (1=low; 5=high). Try this yourself: If your total is between 30 and 35, digital capabilities are or will soon be a strategic priority for your firm. If it's below 30, you should focus on developing digital tools to build traffic, enhance in-store experience, and increase basket size before competitors do.

	BOOKS	APPAREL AND ACCESSORIES	GROCERIES
PRICE			
PRICES OFTEN LOWER ONLINE (DELIVERED)	5	3	1
DIGITIZED PRODUCTS CREATE LOWER COSTS	5	1	1
VALUE OF PRICE COMPARISONS	5	3	2
SELECTION			
VALUE OF BROAD ASSORTMENTS	5	4	3
VALUE OF CUSTOMIZATION	2	3	1
SEARCHES IN STORES OFTEN FUTILE	4	3	2
CONVENIENCE			
RESEARCH AND INFORMATION INTENSITY	5	3	2
WEB TOOLS TRUMP STORE EXPERIENCE	4	2	2
EASE OF DELIVERY AND RETURNS	5	3	1
TRUST			
RELIABILITY OF PRODUCT DESCRIPTIONS	5	2	2
FRUSTRATION IN STORES	4	4	2
TRUST IN ONLINE RETAILERS	5	3	1
TOTAL	54	34	20

in their categories and prepare for the effects. What should I do differently today if I believe that 20% of our sales will soon come from digital retailing—and that 80% of our sales will be heavily influenced by it? Should we be opening any new stores at all? And if so, how different should they be? How should we adjust to a world of greater price transparency? What happens when traffic-building categories shift online and no longer pull customers into our stores?

Situations like these call for start-from-scratch, across-the-board innovation. In the book *Idealized Design: How to Dissolve Tomorrow's Crisis...Today*, coauthor Russell L. Ackoff recounts a similar turning point at Bell Labs in 1951. The vice president in charge of the labs asked a group to name the organization's most important contributions to telephonic communications. The VP pointed out that each one, including the telephone dial and the coaxial cable, had been conceived and implemented before 1900. He challenged the group to assume that the phone system was dead and had to be rebuilt from scratch. What would it look like? How would it work? Soon Bell's scientists and engineers were busy investigating completely new technologies—and came up with concepts for push-button phones, call waiting, call forwarding, voicemail, conference calls, and mobile phones. Retailers need the same start-over mentality.

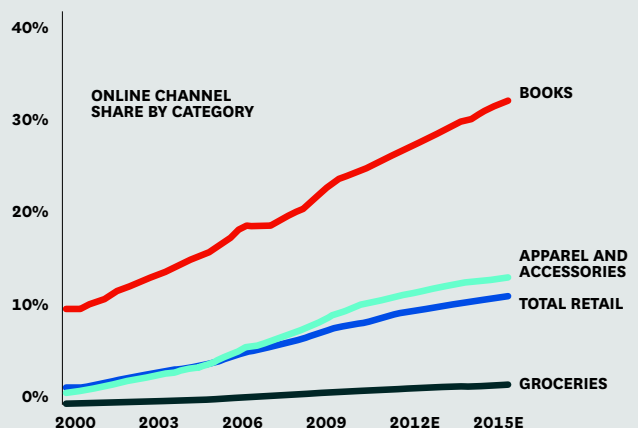
The design specifications of omnichannel retailing are growing clearer by the day. Customers want everything. They want the advantages of digital, such as broad selection, rich product information, and customer reviews and tips. They want the advantages of physical stores, such as personal service, the ability to touch products, and shopping as an event and an experience. (Online merchants take note.) Different customer segments will value parts of the shopping experience differently, but all are likely to want perfect integration of the digital and the physical.

The challenge for a retailer is to create innovations that bring the vision to life, wowing those customers and generating profitable growth. Let's see what this might mean in practice.

Pathways and pain points. Retailers traditionally defined their job with three simple imperatives: Stock products you think your target customers will want. Cultivate awareness of what's in the store. When prospective customers enter the store, make it enticing and easy for them to buy. The job in an omnichannel world is more complex. Products themselves can more easily be customized to the

The Threat Threshold For Physical Retailers

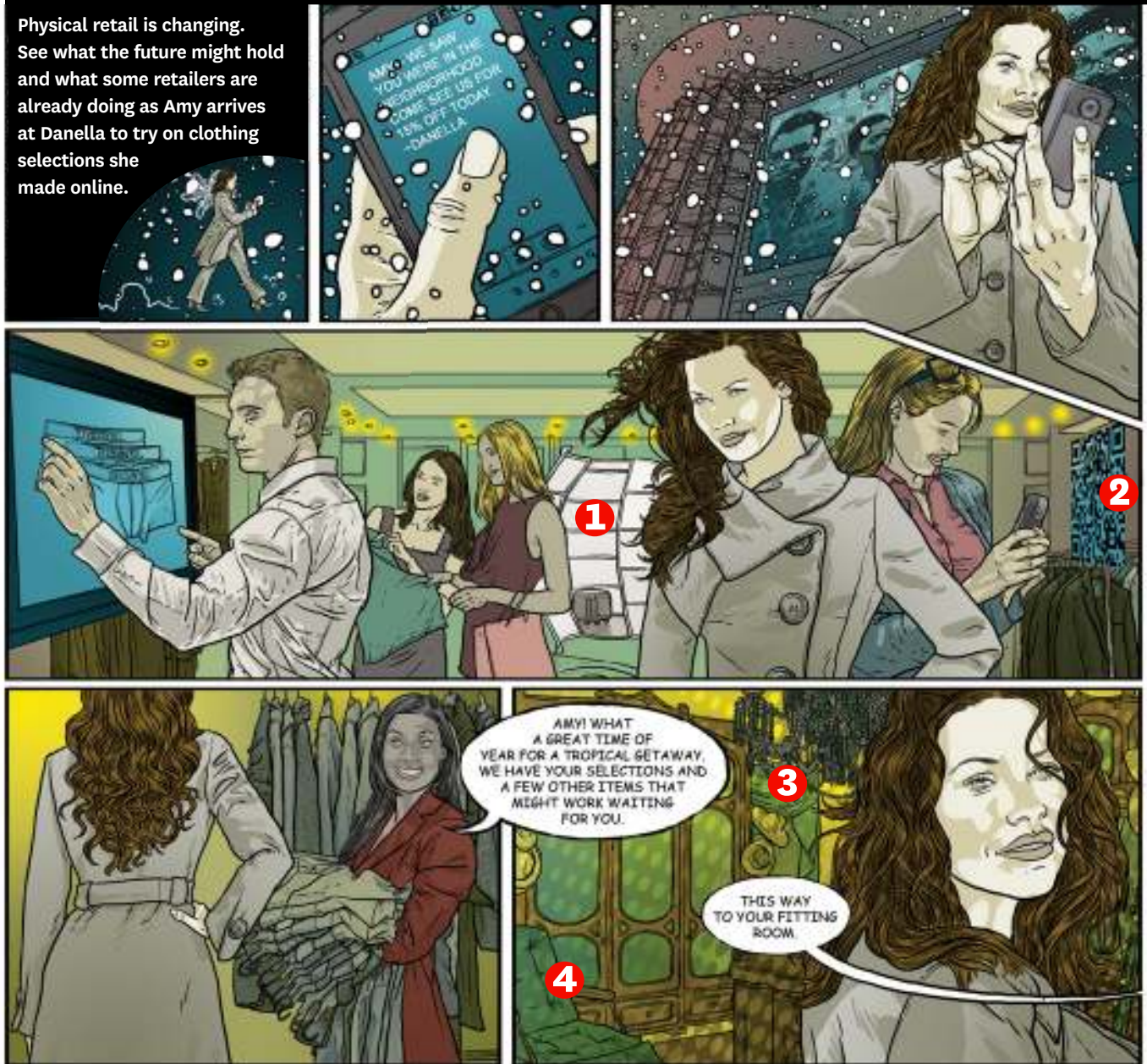
As e-commerce sales for U.S. retailers climb, store-based companies face treacherous landscape ahead. In books, the path above 15% digital penetration first brought consolidation; then Borders closed stores, filed for bankruptcy, and liquidated. The largest store-based retailer, Barnes & Noble, lost money in fiscal 2011 and struggled to raise additional funding. Physical retailers of music, videos, and consumer electronics face similar challenges. Even apparel and accessories, once considered too experiential to sell online, could approach tipping points in the next five years.



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The Near Future of Physical Retail

Physical retail is changing. See what the future might hold and what some retailers are already doing as Amy arrives at Danella to try on clothing selections she made online.



preferences of individuals or small groups. Shoppers' awareness depends not solely on company-generated marketing efforts but also on online expert reviews or recommendations from friends on Facebook and Twitter. The shopping experience includes not just visiting the store but searching for various vendors, comparing prices, quick and hassle-free returns, and so on.

Retailers today have a variety of precision tools that they can apply to discrete parts of these shopping pathways. Consider the job of creating awareness, which in the past relied mostly on mass-market advertising, promotions, and the like. Today marketers can send coupon codes and offers to customers'

1 Pop-up dressing rooms: Old Navy, Bloomingdale's

2 Smartphone-enabled product demonstration videos: Macy's

3 Highly designed fitting rooms: Ann Taylor

4 Fitting room seating area: Macy's, Nordstrom

mobile devices. They can optimize search terms and location-based promotions. They can provide targeted offers to customers who check in to stores through external platforms like Foursquare. The list of possibilities is getting longer by the day.

Using such tools at each point in the pathway, retailers can identify sets of targeted customers defined by (increasingly) narrow parameters and create appealing interactions. Earlier this year, for example, the UK retailer Tesco studied its South Korean operation, known as Home plus, to determine how it could increase grocery sales to time-starved Korean consumers. The answer: Bring the store to the consumers at a point in the day when they had

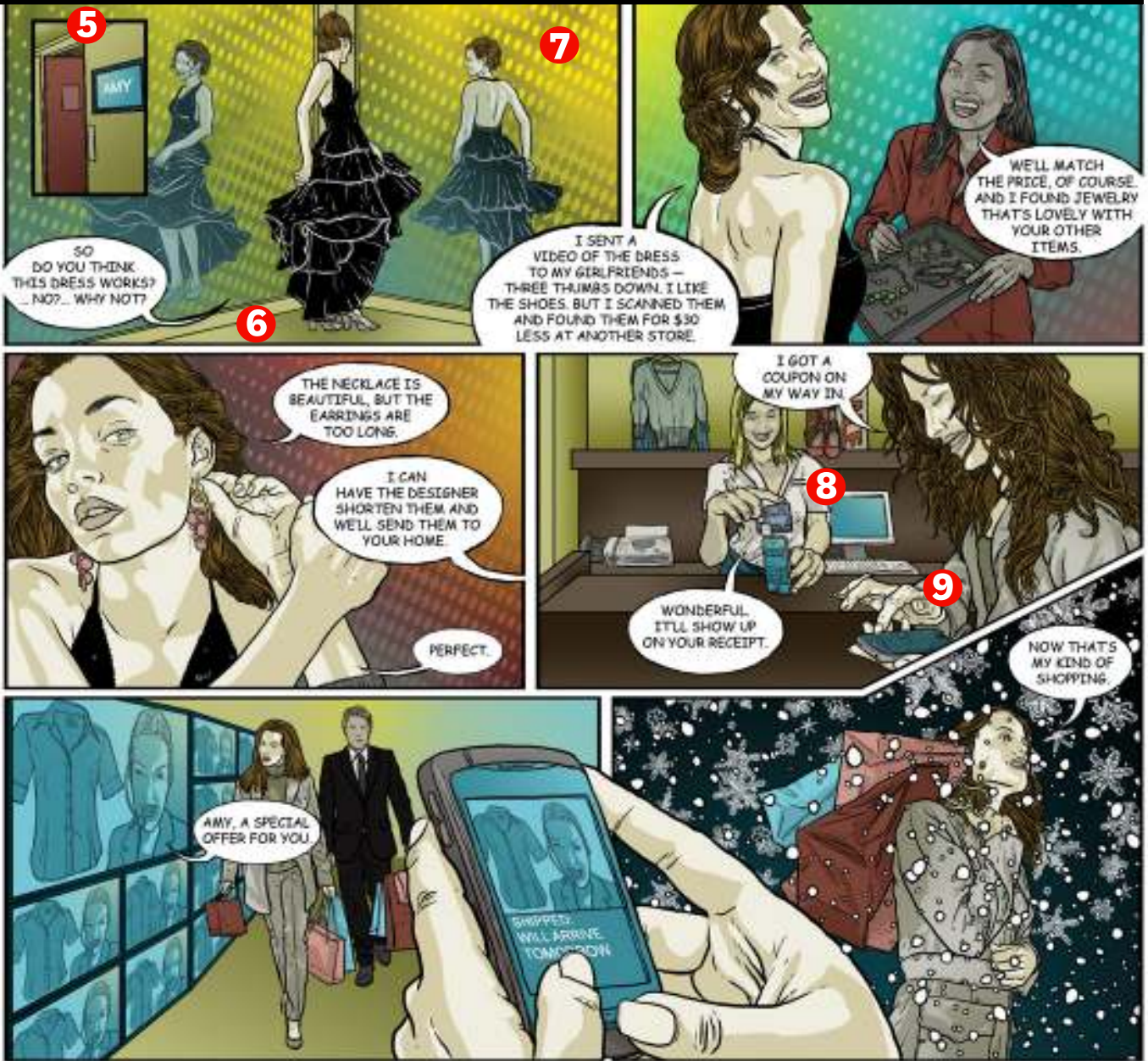


ILLUSTRATION: JAN FEINDT

time on their hands. In a pilot program, Home plus covered the walls of Seoul subway stations with remarkably lifelike backlit images of supermarket shelves containing orange juice, fresh vegetables and meat, and hundreds of other items. Consumers wanting to do their food shopping could simply scan each product's Quick Response code into their smartphones, touch an on-screen button, and thereby assemble a virtual shopping cart. Home plus then delivered the physical goods to the shopper's home within a few hours. According to Tesco, more than 10,000 consumers took advantage of the service in the first three months, and online sales increased 130%.

- 5 Name on fitting room door:** Anthropologie, Banana Republic
- 6 Fitting room with space for groups:** Anthropologie
- 7 In-room camera with 360-degree views:** Jeanswest (Australia)
- 8 Mobile checkout:** Sephora, Apple
- 9 Electronic receipt:** Sears, Kmart, Patagonia

Omnichannel retailers can devise different ways of wowing each target segment. Some segments can be served much the way they were in the past. Others will require more imagination and innovation. Disney, for example, is reimagining its retail stores as entertainment hubs with a variety of interactive displays that will entice all segments of the family to visit more often and stay longer. But retailers will have to devote resources to this search for innovations along the customer's pathways. The trick will be to identify each segment's unique paths and pain points and create tailored solutions rather than the one-size-fits-all approach that has characterized much retailing in the past.

Bringing Digital and Physical Retailing Together

Omnichannel retailing is the way forward for retailers seeking to satisfy customers who increasingly want everything. They want the advantages of digital—such as nearly limitless selection, price transparency at the click of a mouse, and personalized recommendations from friends and experts. They also want the advantages of physical stores—such as face-to-face interaction with store personnel, products available for trying on or trying out, and the social experience of shopping as an event. Different customers will value parts of the shopping experience differently, but all are likely to want perfect integration of the digital and the physical.

ADVANTAGES OF DIGITAL

RICH PRODUCT INFORMATION

CUSTOMER REVIEWS AND TIPS

EDITORIAL CONTENT AND ADVICE

SOCIAL ENGAGEMENT AND TWO-WAY DIALOGUE

BROADEST SELECTION

CONVENIENT AND FAST CHECKOUT

PRICE COMPARISON AND SPECIAL DEALS

CONVENIENCE OF ANYTHING, ANYTIME, ANYWHERE ACCESS

ADVANTAGES OF PHYSICAL

EDITED ASSORTMENT

SHOPPING AS AN EVENT AND AN EXPERIENCE

ABILITY TO TEST, TRY ON, OR EXPERIENCE PRODUCTS

PERSONAL HELP FROM CARING ASSOCIATES

CONVENIENT RETURNS

INSTANT ACCESS TO PRODUCTS

HELP WITH INITIAL SETUP OR ONGOING REPAIRS

INSTANT GRATIFICATION OF ALL SENSES

The experience of shopping. Traditional retailers have suffered more than they probably realize at the hands of Amazon and other online companies. As volume trickles from the stores and sales per square foot decline, the response of most retailers is almost automatic: Cut labor, reduce costs, and sacrifice service. But that only exacerbates the problem. With even less service to differentiate the stores, customers focus increasingly on price and convenience, which strengthens the advantages of online retailers.

If traditional retailers hope to survive, they have to turn the one big feature that internet retailers lack—stores—from a liability into an asset. Stores will continue to exist in any foreseeable future—and they can be an effective competitive weapon. Research shows that physical stores boost online purchases: One European retailer, for instance, reports that it captures nearly 5% of online sales in areas near its physical stores, but only 3% outside those areas. Online and offline experiences can be complementary.

The traditional store, however, won't be sufficient. For too many people, shopping in a store is simply a chore to be endured: If they can find ways to avoid it, they will. But what if visiting a store were

exciting, entertaining, emotionally engaging? What if it were as much fun as going to the movies or going out to dinner—and what if you could get the kind of experience with products that is simply unavailable online?

This is hardly beyond the realm of possibility. Jordan's Furniture, a New England chain, achieves some of the highest furniture sales productivity in the country by using themed "streets" within its stores, a Mardi Gras show, an IMAX 3-D theater, a laser light show, food courts, a city constructed of jellybeans, a motion-simulation ride, a water show, a trapeze school, and special charity events. Cabela's and Bass Pro Shops not only have some of the highest-rated websites; they also have some of the most engaging physical stores. These kinds of store experiences are expensive to create. Might digital technology improve the customer experience in stores more cost-effectively?

In fact, it is already doing so. Digital technology can replace lifeless storefront windows with vibrant interactive screens that change with the weather or time of day and are capable of generating recommendations or taking orders when the store is closed. It can allow customers to design products or assemble outfits and display their creations in high-visibility locations like Times Square. It can create engaging games that attract customers, encourage them to stay longer, and reward them for cocreating innovative ideas.

Digital technology—in the form of tablets, for example—can also give sales associates nearly infinite information about customers, describing the way they like to be treated and creating precise models of their homes or body types that enable perfect choices. It can change pricing and promotions accurately and instantaneously. It can provide customized recommendations. Virtual mirrors accelerate and enliven the dressing room experience by connecting customers with trusted friends. Technology can eliminate checkout lines, capture transaction receipts, file rebate claims, and speed returns. It can give a call center operator full access to a customer's purchase and complaint history.

My objective here is not to enumerate every possible innovation. Rather, it's to illustrate how the opportunities for digital technology in stores, mobile devices, call centers, and other channels are just as abundant and viable as they are for websites. Moreover—and this is key—retailers in many categories can link these channels and technologies to create an

omnichannel experience with stores that is superior to a purely digital retail strategy.

One task is to apply these innovations early enough, frequently enough, and broadly enough to change customer perceptions and behaviors. Adopting successful innovations three years after competitors do is unlikely to generate much buzz or traffic. Of course, many digital innovations will fail, and the effects of others will be hard to quantify. So a second task is to upgrade testing and learning skills to 21st-century levels. It was hard enough to gauge the effects of pricing changes, store-format upgrades, or newspaper versus TV ads in the old world. (Remember John Wanamaker's famous lament that he knew he was wasting half his advertising budget but didn't know which half?) An omnichannel world makes those test-and-learn challenges look like child's play.

Integrating innovative ideas with the base business, in contrast, requires collaboration, compromise, and detailed planning. It's a bit like putting a satellite into orbit. Send it too far from the core and it will drift aimlessly into outer space, wasting money and squandering opportunity. Launch it too close to the core and gravitational forces will overwhelm it, causing it to crash and burn. So mobilizing an organization to both develop and integrate omnichannel innovations is challenging. But it can be done.

One approach is to create separate formal organizational structures but coordinate key decisions—something most retailers failed to do the first time around. Apple launched its online store in 1997, midway through the dot-com bubble. When it began opening retail stores in 2001, the company established its online and offline channels as

Leading-edge retailers are testing digital and physical innovations using clinical-trial-style methodology.

Retailers must now try to assess the effects of paid search, natural search, e-circulars, digital displays, e-mail campaigns, and other new techniques and third-party innovations such as SCVNGR, a location-based social network game—and must gauge those effects on both physical and digital channels (which include mobile apps as well as the internet).

Leading-edge companies such as PetSmart and the UK pharmacy chain Boots have begun applying science to this task: They are testing digital and physical innovations with clinical-trial-style methodology, using sophisticated software to create control groups and eliminate random variation and other noise. All this is costly, but it's hard to see how retailers can avoid doing more of it.

The Omnichannel Organization

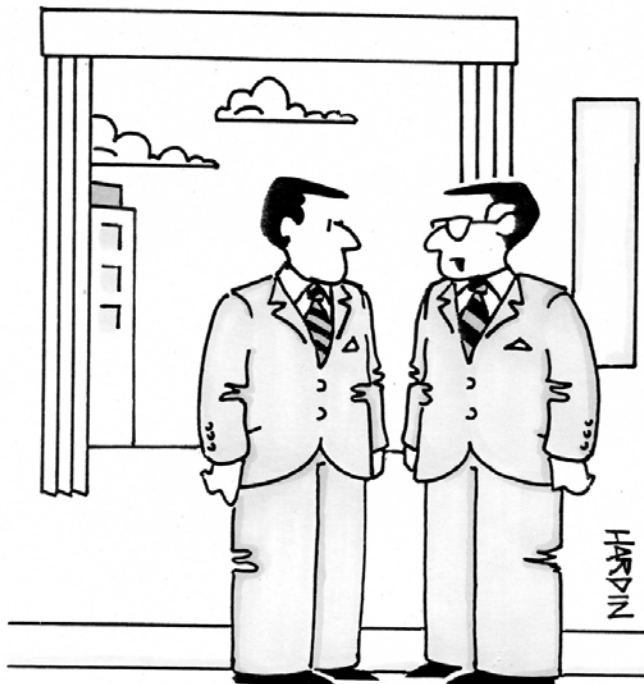
How can retailing companies organize themselves around an omnichannel strategy? Historically, mobilizing an organization to develop and integrate breakthroughs that threaten the base business has been one of management's greatest challenges. Disruptive innovation requires a separate team that has autonomy, a distinctive set of talents, different knowledge bases, and a willingness to take bold risks.

wholly separate organizations, each challenged to maximize sales without worrying about potential conflicts. At first, collaboration between the units was limited largely to coordinating merchandise assortments, new product release dates, and pricing policies. Fortunately for Apple, its innovative products and unparalleled service trumped its lackluster channel integration. Over time, however, customers began to expect more from a preeminent technology company. Apple increased the level of collaboration, enabling cross-channel returns and using its often frenzied product releases to experiment with new systems for checking a store's inventory or reserving items online for purchase in the stores. When Apple revamped its physical stores in 2011, it replaced information cards near demo products with iPads, which provide extensive information and product comparisons in much the way the online site does. The iPads also give customers information on omnichannel support options, and they can page an in-store specialist for further assistance.

Innovative organizations also need to attract and retain innovative people—imaginative, tech-savvy, often young individuals who spin out new ideas every day. Retailers haven't appealed to many of these

innovators in recent years. Now that they must compete with the likes of Amazon and Google, they will have to upgrade their recruitment efforts. They may find some of the people they need buried deep within their own organizations. Others they will find in creative centers such as New York and San Francisco, or around college campuses.

In the past, big retailers have had difficulty hiring innovative people and luring them to headquarters operations in Arkansas or Minnesota or Ohio. And they have had little success creating autonomous disruptive groups and linking those groups to their core operations. But the same technologies that are driving omnichannel strategies can help solve both problems. Desktop videoconferencing, mobile applications, social networks, collaborative groupware, shared knowledge bases, instant messaging, and crowdsourcing not only help Amy shop; they also help Sheldon and Rajesh work together—wherever they may live—and integrate their ideas with their employer's existing capabilities.



"I started as just another 'yes-man,' but eventually my talents were recognized and I became a full-fledged sycophant."

The department-store company Macy's may be showing the way here. In February 2009, when Macy's consolidated its U.S. divisions into New York, it conspicuously left a digital team in the heart of Silicon Valley. Since then Macys.com has started to add 400 people to its existing team of 300. To attract and retain talented technologists, the division launched its own recruiting microsite touting its enviable location, fashion glitz, and unique blend of entrepreneurial ingenuity and business acumen. It rapidly expanded its participation in the social media most favored by desirable recruits. It studied the characteristics of its most successful executives and then developed professional training programs in communication skills, time management, effective negotiations, and financial expertise so that recruits had opportunities for advancement. It capitalized on the local network of technology entrepreneurs, venture capitalists, and leading-edge software and hardware providers not only to identify talent but also to catalyze collaboration and new ways of thinking. These organizational strategies have helped Macy's woo and energize technology stars, increase its e-commerce revenue growth to more than 30% a year over the past two years, and attain the top spot on the 2011 L2 Digital IQ Index for specialty retailers.

For most companies, making changes like these is a tall organizational order. Move too slowly and you're in danger of sacrificing leadership and scale, just at a time when market share is shifting rapidly. Move too quickly, however, and you may not have adequate time for testing and learning. The time-honored rule of the judicial system sets the best course: with all deliberate speed. Retailers need to test and learn quickly but refrain from major moves until they know exactly what they hope to gain.

IS IT ALL WORTH IT? A successful omnichannel strategy should not only guarantee a retailer's survival—no small matter in today's environment. It should deliver the kind of revolution in customer expectations and experiences that comes along every 50 years or so. Retailers will find that the digital and physical arenas complement each other instead of competing, thereby increasing sales and lowering costs. Ultimately, we are likely to see more new ideas being implemented as customers and employees propose innovations of their own. In today's environment, information and ideas can flow freely. Retailers that learn to take advantage of both will be well positioned for success. ♡

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CARTOON: PATRICK HARDIN

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Challenges and Opportunities

Interview with John Rossi, Global Head of Consumer Goods Consulting, Wipro

What are the biggest challenges in retail and ecommerce for consumer goods manufacturers?

For many years, the consumer goods manufacturer, whether the company sold soda or cereal or sporting goods, has not known the actual shopper or consumer; their retail partner did. They might know generally that their typical consumer was a 50-year-old man, who prefers salty snacks over sweet candy. But they did not know the individual or the household. The retailers do know that, since most have been gathering the information for years via loyalty cards or other ways of accumulating data. But the retailer, who is dealing with many different manufacturers, doesn't always share that information.

So manufacturers must play catch-up on the one-on-one level with the consumer. They must create a better business proposition for the retailer so they will share the information. Retailers are not accustomed to doing that because, until now, their collaboration has been mainly focused on the manufacturer providing advertising and promotion dollars to reach a mass audience.

But we need a better model. There is no reason these manufacturers shouldn't be marketing to the shopper and final consumer, or at least their household. Using enhanced marketing techniques, including direct-to-consumer marketing, they will start to gain data that allows them to eventually sell via ecommerce. The apparel industry has been doing it for years via the web and their own stores; the rest of the consumer goods (CG) industry can learn and follow this lead.

The challenge is, how far does a consumer goods manufacturer try to go? Should I go direct-to-consumer? Should I focus just in marketing, or do I want to go all the way to ecommerce? If I go to ecommerce, should I use a company like Amazon, sell via my retail partner's website, or build my own branded ecommerce capability? Companies have to decide where they want to be on the continuum and how fast they want to go.

There is already proven direct-to-consumer and ecommerce in the apparel and footwear industries. For instance, if I am selling jeans, I may have my own stores, but I also sell those jeans through other retail channels, including online. We are starting to see luxury goods companies take a similar approach. The personal care companies and the food and beverage companies are selling online via retail partners (e.g., Amazon, Drugstore.com, Walmart.com to name a few), but very few are selling online via their own websites or mobile apps.

How can manufacturers balance virtual shopping with their retailer's desires for in-store experiences?

The retailers are already moving down the road to the harmonious, all-channel experience. Of course, it is easier for them; they have thousands of stores. So if I buy something at Macy's in Chicago or online, but need to take it back at Macy's in Orlando, they can easily make the exchange. It's more difficult for consumer goods companies that don't have that opportunity, since they sell through multiple retail channels and would need to determine who has ownership of their returned goods. Is it the CG company, the retailer who sold the product, the retailer accepting the exchange or return? It's cumbersome, but will be figured out over the next few years.

Today, the manufacturers have to start to understand how to interlock all these various experiences. On the front end, if a manufacturer is going to do direct-to-consumer marketing, should they have a collaborative relationship with the retailer and develop programs with them, or should they do it on their own? Or should they do both? The best answer depends on the manufacturer's business strategy.

It is very hard for a manufacturer to get to a seamless experience, since today, the consumer can't buy from one chain and return to another. But what if the manufacturer could allow the consumer to buy at one place and then, with the proper receipt, return it directly to the manufacturer? The manufacturer could also work with an aggregator, which might make this seamless. Amazon and Drugstore.com have figured out a model, for instance, so that a tube of toothpaste can be cost-effectively delivered to my house. So a consumer goods manufacturer could collaborate with the aggregator, provide some margin, and use this model to create a more seamless environment. However, this may not reduce the manufacturer's cost, since these aggregators are really just an additional channel requiring their own margins to remain in business. Many CG manufacturers will be creating an additional channel—their own. It's worked for apparel, footwear, and luxury brands; it'll work for beverages, food, and personal care. But first, they want to better understand the individual shoppers and consumers.

Manufacturers should look at different approaches. For instance, the CG company might create their own loyalty program, using a phone app, so that no matter where a consumer buys a product, the company can know what was bought and by whom. The CG company would learn if the shopper is buying multiple products

from their company in different places—for instance, shampoo at one store, toothpaste from another, and makeup from a different channel. With that kind of information, a CG manufacturer could begin to market products like that directly to the household. This becomes more interesting.

It appears from our experience, if the CG manufacturers start with helping their retailers' programs on the marketing end, that gives them access to data, and it puts them on a quicker path for direct-to-consumer. There are some segments with quicker opportunities. Nike owns their own stores, but you can also buy their similar—if not identical—products at a department store or a sporting goods store. Nike has a nicer ecosystem that enables them to create a seamless experience faster. For them, it is probably more of a business decision about how far and how fast to push that seamless experience.

Among those CG companies that own their own stores—and there are plenty of them—too often they treat online and retail as separate entities. Maybe they need to treat their own stores as test-and-learn centers for consumer behavior and new product introductions. It's common to spend more than \$1 billion on new product introductions. Why not introduce it first into their own channel, then test acceptance of the items before a nationwide rollout? Many are missing out on opportunities to better understand their shoppers, their consumers, and increasing the likelihood of new product successes. With an industry average of new product failures between 60 and 80%, using your own stores and ecommerce for test-and-learn seems like a no-brainer.

Where should CG companies start in developing—and investing in—their strategies?

The big question for many companies: Are we going to go into marketing to consumers at an individual brand level or a company level? Obviously, companies like P&G, Nestlé, and Unilever own many brands under one umbrella. So far, many of the “multi-brands under one roof” companies have gone brand by brand, product by product, to the consumer. Many agencies are involved, many channels of information are created, and there are a lot of inefficiencies.

We need to create a holistic platform for all our brands so we can know more about the consumer. When companies have a common technology and common platform, they can give a 360-degree view of shoppers for the entire company. This is a big hurdle, but an important step forward. Getting alignment is difficult since so many CG companies allow brands to make autonomous decisions best for their brand even if counter to the overall company goals. But soon they will have to start looking at this from across the organization if they want to best understand their shoppers and consumers at an individual level.

Technology will play a key role in understanding the shopper and consumer. Today, when you have dozens of agencies helping with brand marketing, each uses technologies that they are comfortable with and know. They are not taking advantage of the CG

manufacturer's power. The CMO should be pushing the envelope to harmonize technologies so we get better data that can be used holistically to gain a 360-degree view of their shoppers and consumers. In many companies, the IT department may not be informed or involved in these consumer-facing areas, but we have to be better at this. We need to have marketing and IT taking this on together from day one. [Making] proper consumer and shopper information readily available to the entire enterprise will be the largest strategic investments over the next few years. What ERP was to business transformation in the 90s, consumer information “hubs” will be for the mid-10s.

An important adjacency for CG manufacturer's consideration is building their own loyalty programs. To date, companies that have done this are seeing decent internal results on increasing sales thanks to understanding the individual shoppers and consumers. As they get this data, companies also have to ask if they want to focus on the individual or the household. For some, it might be a shorter jump to get to the household. For instance, if you have hundreds of brands and you are able to understand where households are already buying some of your products, you have the opportunity to convert them to buy more of your brands on a regular basis. You can also identify the household that might be buying your paper towels but not your facial tissues, or your shampoo but not your conditioner. Households use a lot of both; by having this information, cross-selling becomes much easier.

Those first movers are gaining market share and getting a better chance to gain consumers' loyalty. Taking it a step further, if I can deliver to the consumer's door, I can convert a household to a regular subscription service. A subscription service that is direct from the manufacturer to the consumer's doorstep is a logical next step for purchases like toothpaste or dog food. If you tie it into their usage patterns, it becomes a predictive replenishment, and that becomes almost guaranteed income.

Other CG companies with fewer brands also may have to get out there to survive. Stores aren't getting larger, but aisles are getting wider. Retailers are almost real-estate agents as it relates to the use of shelf space. So if you are a smaller company, it is becoming more difficult to get shelf space unless you are providing very high margins, so it is crucial to spend more on promotions and marketing to gain new shoppers. Promotional spending is now above 20%, up from the low teens where it was just a few years ago, and we know of a few companies admitting that their trade spend is now over 30% of gross revenues.

Direct-to-consumer makes a lot of sense in better understanding your exact shoppers and consumers; having better visibility into your promotional spend and its effectiveness; and providing better balance in the CG manufacturer/retail partner relationship. Some CG companies are investing heavily in figuring it out—they'll be tomorrow's winners. Wipro is helping many companies figure it out.

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