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Retail Supply Chain Reboot:

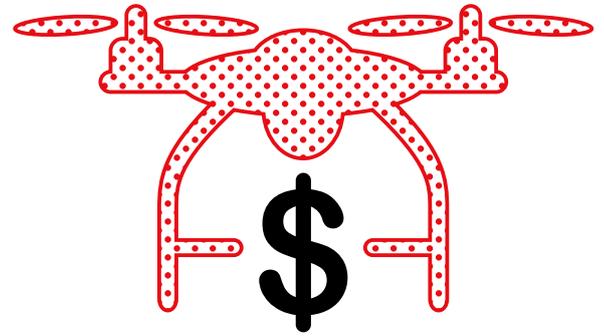
Agilely Facing the Unknown

by Mirko Martich

Are retailers winning the customer experience battle but losing the profitably war?

As more companies increase their investments in supply chain logistics to offer the seamless customer experience consumers crave, some aren't acknowledging the unusually high levels of uncertainty they face today. Lacking the ability to anticipate multiple scenarios or the agility to deal with them effectively, retailers could find themselves on the wrong side of fast-moving and costly logistics trends.

Investing heavily in supply chain logistics



Retailers are investing strongly in this area, with leading players worldwide already announcing plans to boost their supply chain performance:

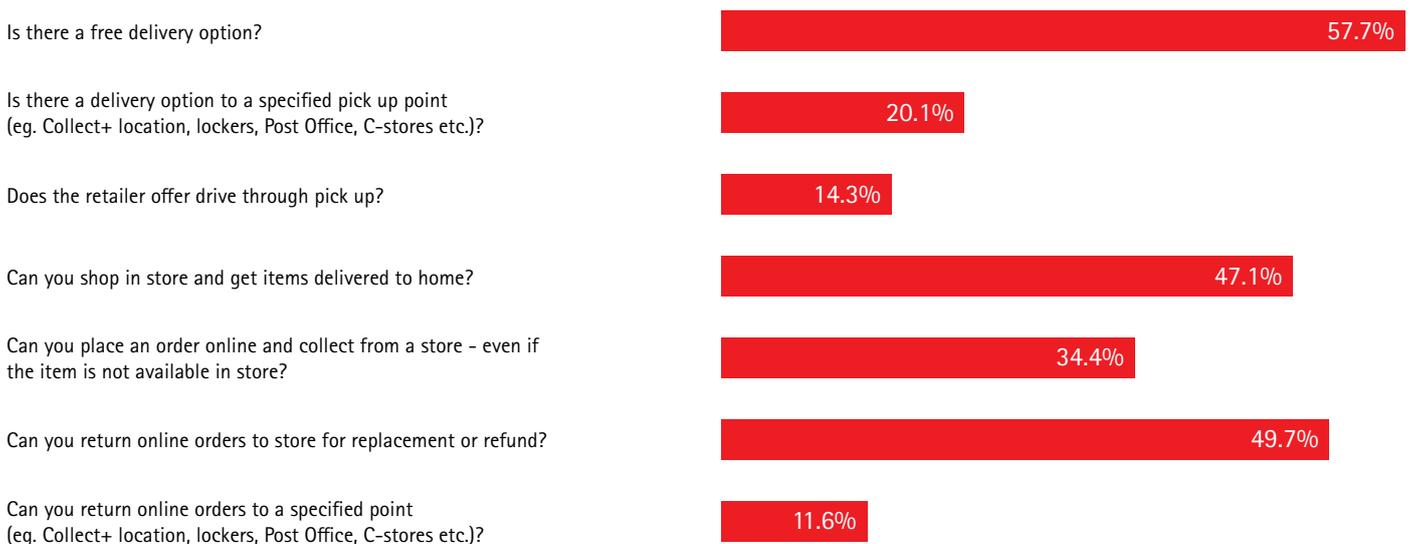
- John Walden, CEO of Argos, a UK based retailer, recently stated that as online shopping grows, customers are increasingly expecting faster, cheaper and more convenient fulfillment.¹
- Home Depot, a US based retailer, plans to make major capital investments to bolster its supply chain, technology, e-commerce platform and warehouse technology system.²
- Amazon entered into a strategic partnership with the Shanghai Free Trade Zone to replicate the massive regional distribution centers it has in the US and Europe.³

Customers are driving most of this spending. Accenture surveyed roughly 10,000 consumers in 13 countries and found that 89% are interested in ordering out-of-stock items via their mobile phones when shopping in stores.

Likewise, 35% shop online prior to visiting stores to see if the product they want is available, and 92% want retailers to send real-time promotions to them while shopping. Other Accenture research reveals that 63% of consumers say consolidating their orders is very important, and 25% are using "click-and-collect" services (i.e., consumers buy online and collect the purchase at a local store) more than they did a year ago.

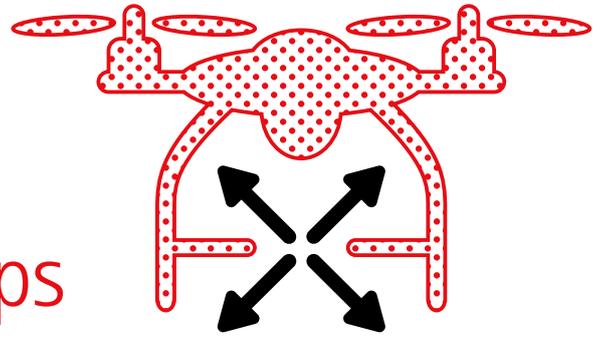
The industry's response to these findings has included a flurry of fulfillment investments and experiments. Accenture's 2015 Seamless Retail Survey benchmarked 189 retailers across 12 countries (Figure 1). It revealed that nearly 60 percent of respondents offered a free delivery option, almost 50% allowed consumers to return online purchases to stores, and nearly 15 percent already had drive-through product pickup services. What's more, over half of all retailers provided next-day deliveries, and increasing numbers offered a variety of specific delivery options.

Figure 1: Accenture retailer benchmarking results regarding fulfillment options



Source: Accenture 2015 Seamless Retail Survey Benchmarking - Base = 189 retailers across 12 countries

The next challenge: closing growing cost gaps



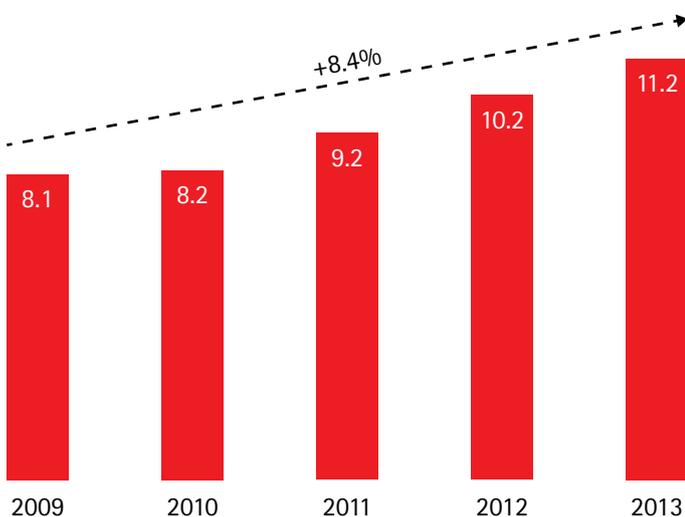
Many retailers realize the industry needs to make significant investments in supply chain performance to remain competitive. They understand their options for supporting consumer needs in this area, and know where to spend money to achieve these goals. Despite this knowledge, closing current gaps in logistics performance remains difficult due to the challenges inherent in scaling up the new approaches. The reality is that retailers globally are making these investments to support what is often a small part of their business: in some cases, only 10 percent or less of a retailer's total sales originates online. What happens when that amount expands significantly?

Clearly, cost pressures will intensify going forward. In November 2014, Credit Suisse published a report⁴ on e-commerce retail and logistics. The researchers studied 40 retailers, and all but one offered some sort of free ground-shipping option. The report also noted that in 2015, Federal Express and UPS in the US are changing the way they calculate package costs and introducing price increases. These moves will have a major impact on retailers, which often charge less for home deliveries than they actually cost. In fact, delivery costs already show up as a snowballing expense on the income statements of even the best retail players. For example, Amazon's net fulfillment costs as a percentage of sales have risen at an 8.4 percent annual rate over the past four years, from 8.1 to 11.2 percent (Figure 2).

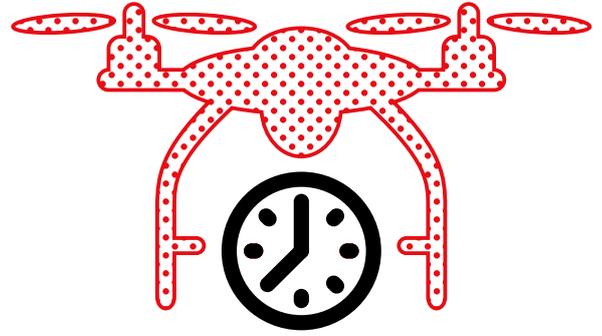
Alternatives to home delivery also pose challenges. One large retailer recently estimated that if its click-and-collect program grows as planned, it will soon require two to three trailers full of goods parked outside each of its stores to fulfill customer orders. Several French and UK retailers such as Carrefour, Auchan, Tesco and others have already set up drive-through operations, and many North American retailers are moving in a similar direction, including Walmart, which is testing its first click-and-collect center in Bentonville, Arkansas.

While retailers can attempt to transition customers away from free shipping to the click-and-collect option, it's still expensive. For example, grocers need to assemble orders quickly that employees have picked and stored in ambient, chilled, and frozen areas within the store. For most retailers, click-and-collect requires sales staff to spend time picking items in the store instead of selling, and collection areas can tie up valuable sales floor space. Alternatively, shipping the ordered items from distribution centers requires different "pick-and-pack" operations and store delivery frequencies in order to match customer pickup schedules. What's more, up to half of traditional mail-order catalog orders end up as returns; online players will likely see similar results.

Figure 2: Amazon's net fulfillment costs as a percent of sales



Source: Amazon annual reports



How scenario planning can help

In the face of these challenges, retailers need to reassess their supply chains entirely. For this reason, we believe that simply investing more money in new capabilities and running a higher-cost supply chain to create a seamless customer experience will likely be a money-losing proposition for many players. Instead, retailers should employ tools that can guide them both in the timing of initiatives and the outlays required to achieve an optimum balance of speed, scale, complexity and cost.

Scenario planning can help retailers reimagine their supply chains with the right scale, cost and rollout timing while ensuring profitable growth as consumer behavior evolves. This approach makes sense today because it helps teams to address the changes affecting future store sizes, locations, and assortment needs.

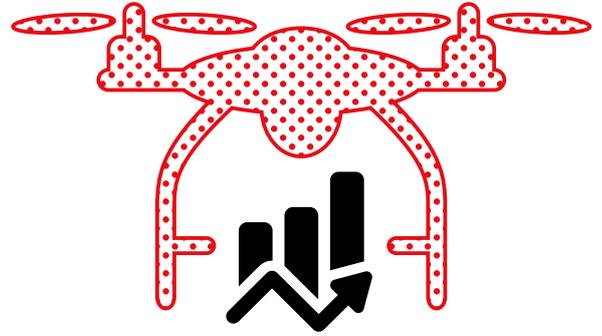
How does it work? Suppose planners at a global mass-market retailer develop three possible scenarios for the company's online business over the next five years, based on consumer research and experience-based insights. The three scenarios provide a low, medium and high estimate of how disruptive different levels of online sales will be for the company. Each scenario examines the impact additional online sales will cause across three typical shopper "missions" (i.e., stocking up on regular purchases, filling in missing items, and "browsing" and other online buys).

In scenario one, which assumes the lowest percent of online sales (e.g., just over 15%), the impact would be manageable. In essence, the retailer would have to find creative ways to maintain its low prices while dealing with challenging but not overwhelming levels of seamless fulfillment. At the other end of the spectrum, scenario three envisions a world where up to 25% of sales originate online. This scenario has a far greater impact on the number of consumers who stock up via subscriptions, use click-and-collect pickup centers, or want scheduled deliveries. If this scenario happened, the company would have to reinvent its supply chain completely, investing heavily to deliver millions of seamless transactions each month.

Useful in situations where high levels of uncertainty exist, scenario planning helps leaders to engage in "what-if?" simulations and work out their consequences across the entire supply chain. Defining the right approach for the company's specific situation will play a critical role in its success in developing a balanced logistics program going forward. We believe the industry is reaching a tipping point in this regard, and that retailers are investing in supply chain improvements because management clearly understands consumer behavior is changing, and that they could fall behind if they fail to act now.

Done right, scenario planning can help to justify the tens (if not hundreds) of millions of dollars retailers are spending to improve supply chain performance. In addition to improving customer satisfaction and competitiveness, experience shows it can have a meaningful impact on a retailer's bottom line. Other benefits include:

- Getting people into stores and/or online, driving loyalty with subscription services and generating additional sales with impulse purchases delivered at the customers' convenience.
- Fulfilling orders from the "optimal" locations (e.g., overstocked stores), enabling retailers to sell more products at higher margins.
- Reducing the total cost to serve by integrating store, distribution center and e-commerce operations, and eliminating redundant distribution, transport, handling and inventory costs.
- Optimizing returns and ensuring the company processes items and puts them back out on sale (where relevant) as quickly as possible.



Key enabler: Gaining greater agility

The insights scenario planning generates won't make a difference if the organization lacks the ability to adjust its supply chain strategy quickly enough to realize the benefits of the new plan. That's why most retailers should also focus on improving their organizational agility. Growing numbers of retail leaders recognize this shortfall: a 2014 Retail Week report⁵ showed that fully a third of surveyed retail executives rated agility as one of their top three supply chain challenges. And another 40 percent believed that adapting their supply chain to achieve target multichannel performance was their most pressing priority – only 12 percent said the same in 2013.

Accenture's research and experience suggest that leading players tend to do several critical things right when it comes to boosting supply chain agility. Successful agile players:

Actively build seasoned, diverse leaders and management teams.

Ensure that managers up and down the organization have full accountability and the right competencies to handle a diverse set of circumstances.

Speed up decision making. Establish a culture attuned to making critical decisions at speed. Doing so can help to ensure that those decisions are tuned to market conditions.

Invest in and make more use of data and analytics to run the business. Leaders understand the competitive value of deeper insights and knowhow and willingly access many sources of data – not just their own – to obtain those insights.

Prioritize strategic decisions. Distinguish between the decisions that affect everyday operations and the bigger decisions that concern the company's strategic direction.

Prepare their ecosystem to act quickly. They arm their business ecosystems – suppliers, customer, and a range of third-party partners – with the resources, information, and tools needed to take decisive, well-orchestrated action. Consequently, they can quickly measure the results and course-correct when needed.

Retailers are making big investments in supply chain innovations, but often lack a way to make sense of their future store-level logistical needs. Scenario planning offers a fact-based way for leaders to simulate likely changes in consumer behavior regarding product pickup and delivery, enabling them to base future investments on the most cost-effective services that help meet customer needs. However, unless retailers augment their scenario planning efforts with agile organizational capabilities, they could end up building a supply chain for today's retail "battle" that quickly becomes obsolete in tomorrow's fast-changing war for customers.

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