

In this issue...

Customers in Control and the New Retail Dynamic

Retailers today face a major inflection point—a profound and dramatic change that is impacting both the way they sell product and communicate with customers. This is a topic with enormous complexity—the explosion of the digital world and its impact on retailing as we know it today and into the future.

Predictably, this topic is getting enormous attention. And, so often, as we have seen historically, the attention is often focused in the wrong place, manifesting itself in the urgent need to create a Facebook page or an app for the iPhone. Too often though, this is being done without a holistic strategy to accompany it, ongoing resources to support the initiative, and ends up creating minimal impact. There are, however, retailers who are placing the right strategic bets and the digital divide threatens to be significant between the have and have-nots.

It has always been our goal at McMillanDoolittle to take the hyperbole surrounding developments in the retail world and do a few things:

- *Simplify them so they make sense with a broader strategic context;*
- *Separate out the hype from the reality—what is real, enduring and important versus what's interesting or gimmicky.*

We'll try to do that now, amidst the swirl of activity surrounding multi-channel commerce, social media, m-commerce, digital media and other ways to reach the consumer.

Hopefully, we will conclude with a sense of what needs to be done now for retailers to position themselves properly for the future.

The Customer in Control

We have been speaking for nearly a decade now about the broader phenomenon of the Customer in Control. Even before the explosion of the digital age, there were some fundamental realities taking place that were impacting retailing:

- *The expansion of choice at retail leads customers to seek and have better options at their disposal. Both from a bricks and mortar and on-line standpoint, there is more and better competition in every category. There is no such thing as a captive consumer anymore.*
- *The advent of the Internet initially put an incredibly powerful tool in the customers' hand—information. The customer can now learn about products; be exposed to almost infinite choices; see how they're rated in an unbiased manner; and understand how they're priced, all without ever leaving their home. And yes, they are increasingly buying goods on-line but the far greater impact today remains on Internet influenced sales.*

- *Two-way communications. First, the power of traditional media has dissipated over the past decades as media fragmentation took place. No longer could a retailer or brand effectively deliver a message through "mass media". More importantly, with the explosive phenomenon of social media over the past few years, the consumer can now talk back-through blogs, social media sites, on-line reviews, You Tube, tweets and the like.*
- *Finally, new generations of consumers are developing profoundly different shopping patterns and ways of communication. They will have been raised in a digital world and will act in a very different manner than the generations before them. While the above trends impact all customers, habits are hard to change and will likely have less impact on older generations of consumers. But, the next generation of consumers is already behaving in very different ways.*

Despite the overwhelming evidence of the move towards Customers in Control, the vast majority of retailers have yet to embrace these changes. They operate largely in a transactional environment, still hoping to dictate to, and manipulate the consumer. Strong words, but unfortunately true.

Some Defining Principles

The real pioneers will be those companies that figure out the new realities of Customers in Control and incorporate new sets of principles as their standard business model.

These principles will include:

- *Encouraging and embracing two way interactions with consumers at all times;*
- *Having more transparency in their business practices;*
- *Developing relationships with consumers that extend well beyond the transaction;*
- *Embracing and integrating multiple ways for customers to interact with your brand-commerce, media and the like.*

Ultimately, this will build trust, loyalty and a relationship with the customer that can be even more enduring than ever before.

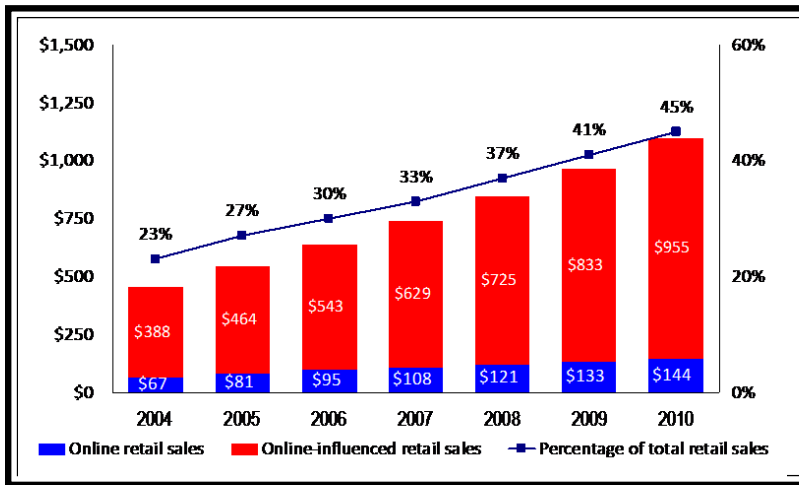
But, it does mean profound change and the need to break through the silos that too often plague retailers. If legacy companies cannot make the change, there are plenty of companies who will gladly step in. In this issue, we will look at some emerging trends and how they will impact retail in the future in the following areas:

1. *Multi-channel retail*
2. *Social Media*
3. *Mobile Applications/Commerce*

Hang on. It's going to be an interesting ride.

Multi-Channel Commerce

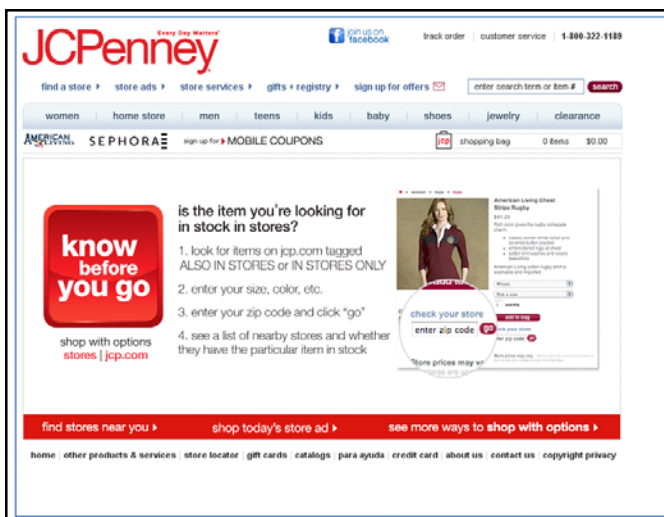
Below is a data slide we've been using quite a bit lately, courtesy of Jupiter. On-line sales continue to grow impressively and at a considerably faster rate than general retail sales. Depending on whose numbers we look at, on-line represents somewhere around 6-7% of total retail sales. And, e-commerce sales will undoubtedly grow even larger as the business and customer base gain in sophistication. While this is clearly significant in and of itself, on-line influenced sales (admittedly a softer measure) represent an even more profound trend. We have seen several sets of numbers, by category and from retailers that suggest that up to half of retail sales are now "influenced" by the Internet.



This means that customers are increasingly using the Internet to research purchases before-hand. Once there, the customer has several options at their disposal, all of which can be influenced by the confluence of bricks and clicks:

- **Ordering on-line.** This is somewhere around 7% of total retail sales and growing at a faster pace than traditional retail. This pace is slowing and does suggest that while enormously important, on-line sales are not going to replace traditional retail anytime soon.

- **Shop on-line and buy in-store.** Many consumers have done the work before-hand and will come to stores ready to buy. Offering real time inventory availability or in-store pick-up creates a major advantage for companies. This can be as simple as JCPenney offering "Know Before You Go" to providing Site to Store services:



JCPenney's Know Before You Go



Walmart's Site to Store

" **Site to Store.** In all new Walmart remodels, Site to Store counters are now prominently placed at the front of the store near customer service. They are even experimenting with drive-thru pick-up stations that allow the customer to never leave their car. This integration with the retail site is allowing companies like Tesco and Walmart to potentially decrease their inventory available in-store and seamlessly move the consumer on-line to make that purchase, with fulfillment occurring either in-store or at their homes. While the infrastructure may be cool, the actual system trails behind. Walmart offers delivery of goods to the store within 7-10 days for regular orders or 3-5 days for customers who sign and pay (\$29) for site to store express. While one potential benefit of this feature is the customer's ability to pick up their order (once it's arrived at the store) when they want to, with the spectacular logistics systems of next day delivery for so many on-line retailers, this offer doesn't cut it.



The Store to Home program at Sears



Order pick-up at chronodrive.com

· **Store to Home.** Conversely, robust store to home programs like Sears utilizes takes active customers and offers them more assortment than a physical retail store could ever offer. While we have had little positive to say about Sears as a retailer in many years, they are truly emerging as a company to watch in the multi-channel space and it may well offer the key to the brand's future.

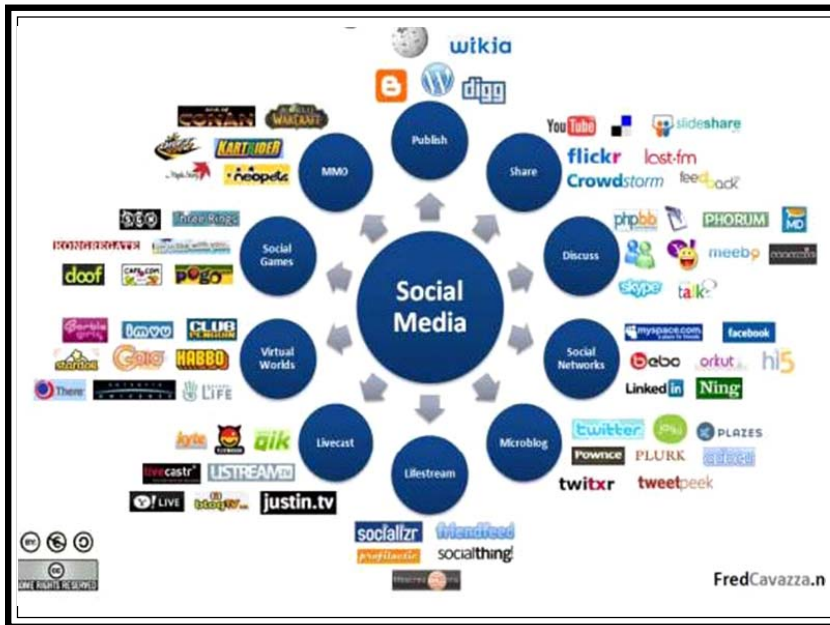
Much More on the Horizon

Still at their infancy, brand new models are emerging that will take all of these notions further. MyGofer by Sears is a physical store test of a pick-up only service that is not terribly meaningful in its own right. But, viewed strategically, what they are really doing is leveraging that technology for broader deployment at all of their stores. And, in fact, that is exactly what's beginning to happen now. ChronoDrive in France allows for customers to order in advance and have products brought to their cars and has been successful enough to begin fairly rapid expansion.

Taken collectively, the multi-channel revolution has very much arrived. And, with the Internet increasingly directly in customers' hands via smart phone devices, the ways to potentially conduct commerce on a mobile device is also very much a consideration for the future.

Social Media

Simply put, there are infinitely more ways that consumers can interact with one another and the companies they do business with today than ever before. The chart below collectively demonstrates the very real power of the consumer's voice today and the outlets available for which they can express it.



If you haven't heard of all of them, that's OK, but each is a phenomenon in its own way. If you're a brand or retailer who is intent on controlling your messages to the consumer, the chart is a sobering reminder of the complexities of such a task.

At the same time, social media also offers an unprecedented opportunity to talk with your customers and engage in a two-way conversation. Not only does this create incredibly powerful real-time customer research and feedback, it also provides some great marketing opportunities.

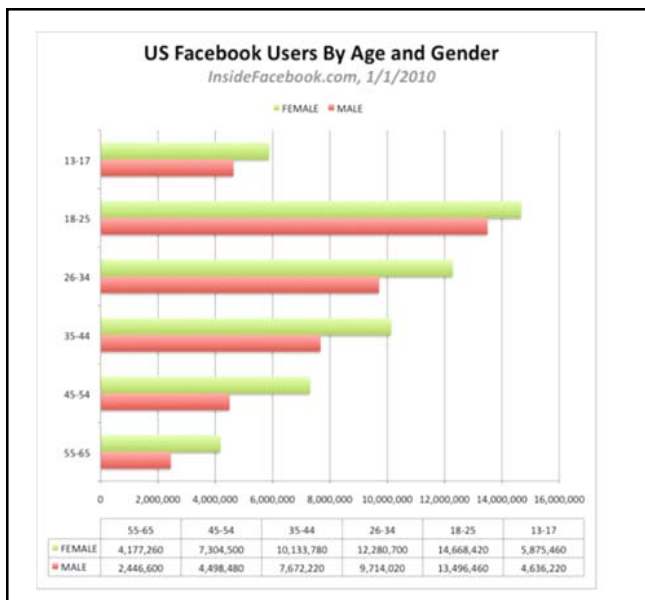
There is a rather huge divide between the social media have and have-nots in retail today. There are companies that have embraced and supported the strategy and have social media pages, YouTube downloads, blogs, community boards for customers and associates, and the like. There are some amazing examples of customer-created content in the form of videos, contest submissions and the like that show real passion towards brands and evidence that social media can truly move the sales needle.

But, before you engage in social media tactics, you better have the following:

- *Something meaningful to say. This includes scheduled activities, promotions, contests, causes, information and other programming that continues to keep customers engaged.*
- *Someone (or some team) in charge of monitoring the back and forth activity.*
- *The fortitude to be ready to respond to what customers are telling you.*

Now, some fun factoids on what's happening:

- *There are now over 100 million monthly active Facebook users. The sheer numbers suggest a mainstream phenomenon. And while the users trend more female than male and younger than older (18-34 year olds represent the sweet spot of registered users), 100 million users clearly transcends a particular demographic.*



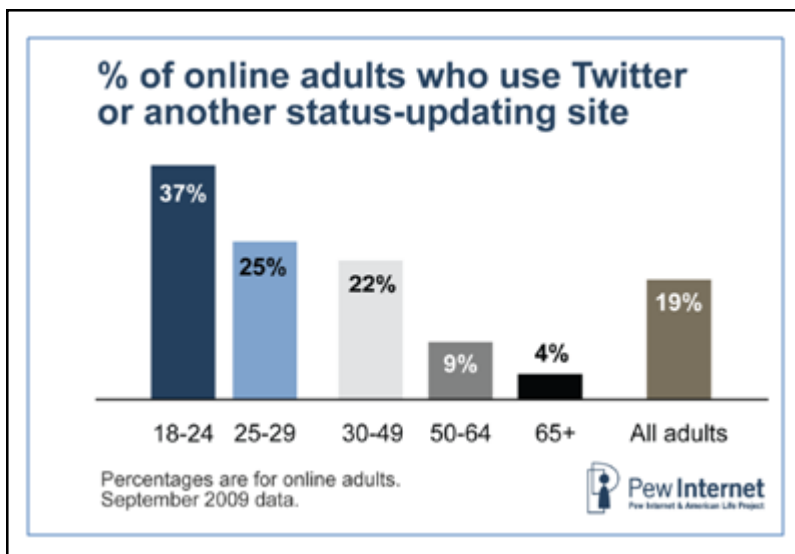
Retailer	Fans
Starbucks	7,024,000
Victoria's Secret	3,196,000
Zara	2,450,000
Nike	2,106,000
Best Buy	1,125,000
Abercrombie & Fitch	1,048,000
Target	1,047,000
Kohl's	986,000
JC Penney	812,000
Outback Steakhouse	706,000
Gap	563,000
In 'n Out Burger	533,000
Life is Good	303,000
Whole Foods	246,000
Aerie	240,000
7-11	232,000
Wawa	161,000
Wegman's	78,000

- Facebook (and there are other sites that have amassed considerable traffic), as a communications tool, is very real today. Retailers of all sorts have amassed a sizable group of fans. Consider the sheer numbers of some of the above retailers' and brands, according to statistics from AllFacebook.com.
- The numbers themselves are rather extraordinary. First, it's notable how many followers Starbucks has relative to just about everyone else. And the number of retailers who now exceed 1 million fans speaks to a consumer willingness to engage with their brands at some level. It is also probably notable to point out who's not on the list. Some of the larger supermarket chains are nowhere to be found, despite the rather obvious overlap with their core consumers. Wegman's, a rather small (by comparison) regional chain is the first supermarket listed. We also note the comparative absence of most hardline retailers here as well. The list is also interesting because it does speak to the "branded" nature of some of the companies. Anecdotally, it does appear that retailers who have cultivated their brands more effectively also have stronger Facebook followings. So, perhaps it's no coincidence that cult brands like In 'n Out Burger and Life is Good well outperform their relative size (if we had a lot more time on our hands, we might develop some fan/revenue dollar kind of metric. It would probably be even more telling than sheer rank order).
- As we have said before, though, it is not just numbers. Having fans but no meaningful interaction doesn't serve much purpose. Whole Foods, as an example, encourages customers to "fan" local stores. This certainly provides the potential interaction with customers at the local level, which is exactly where you would want it. Progressive retailers are using their sites for a few of the following:
 - Polling consumers on key issues
 - Introducing new merchandise
 - Signaling special events and promotions
 - Providing advice on gifting
 - Managing registries
 - Virtual gifting
 - Contests
 - Cause marketing (particularly effective for crises like Haiti)
 - Photo uploads (posing with the brand)
 - Two way interactions--blogs
 - And a lot more

Tweet, Tweet?

Twitter (or micro-blogging) is not as mainstream, reaching just 19% of the adult population today. However, its popularity among younger users suggests that it also must be monitored very carefully and can be a powerful tool for retailers as well.

While Twitter is gaining in popularity, exactly what purpose it serves is not entirely clear...being able to follow the lives of Ashton Kutcher and Britney Spears (numbers one and two respectively among Twitter followers) isn't exactly progressing society forward. However, there are a number of retailers who have amassed an impressive Twitter following and are using this platform as an immediate and inexpensive communications tool. Particularly impressive:



- *Threadless.com (one of our favorites), with over 1.5 million followers.*

- *Starbucks numbers 860,000 and links Twitter and Facebook. Starbucks recently used Twitter to launch their new Frappucino line and you can manage gift cards on Facebook.*

- *Whole Foods appears to be the highest followed retailer with nearly 1.8 million users. Their latest tweet (as this was being written): encouraging the purchase of Whole Trade Guarantee flowers for Mothers' Day. Click further and there is the story of a Whole Foods*

buyer going to Colombia, visiting the farm, visiting the school on the farm that is encouraging education and so on. It is exactly this kind of meaningful interaction that builds the brand and accomplishes something that would be next to impossible in a retail setting.

A Resource Commitment

These sites need active monitoring and a strategy for responding to customers and creating fresh and innovative content. There are plenty of inactive pages, or, the job falls to someone in marketing (who tends to be young and have three or four other things to worry about). Social media needs to be strategized, funded and supported by the organization.

We are increasingly hearing about the new position of Director of Social Media. There will be a lot of innovation occurring here and it will need to be resourced appropriately. The good news: we suspect that social media will be part of a media shift away from traditional means. In the long run, this can be a more cost effective way of meaningfully reaching consumers than mass media ever was.

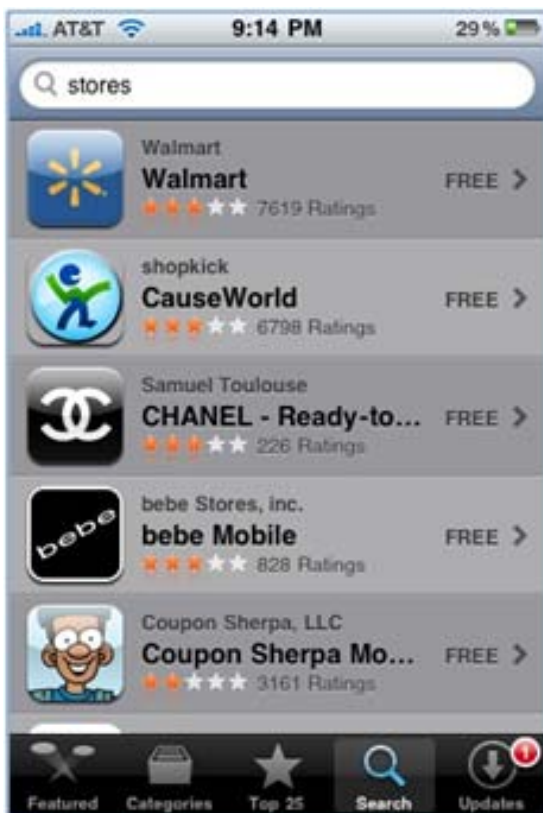
Mobile Media

There's An App for That

Apple has done an extraordinary job of revolutionizing the way we consume media and is very much in the process of changing everything we think about mobility. With over 85 million iPhones sold and over 4 billion apps downloaded so far, it's a bit scary to know that we are merely scratching the surface of what is becoming a global phenomenon. The Apple iPad will have some impact on app usage, already in the hands of 1 million+ consumers. And, of course, Apple is not alone-there are many other smart phones coming on the market that will eventually offer "comparable" capabilities. "Comparable" being the key word because the magic of the Apple brand is their ability to bring function and simplicity together like few tech companies have done before.

Naturally, this is driving more buzz about m-commerce. And, it is not limited to just apps, but extends to texting, mobile optimized web-sites and the like. We have to admit that we cast a somewhat cynical eye on the commerce value of apps today. The ones we have seen so far are driven a bit more around "we got one" than "we have something you might actually use".

Around this time in an in-depth *Retail Watch*, we typically trot out our rusty economics learning and discuss a concept called "bounded rationality". What this says in laymen's terms is that consumers have limits to the amount of information they can process. When exposed to too much, they use filters to limit choices or simply block out further stimuli. With literally tens of thousands of apps available (many are free), retailers will need to develop a compelling reason for a consumer to use their app or it will simply fade into obscurity among so much choice. We've been told that the magic number is five - 5 apps is the number that a person can handle.



Will there eventually be "real" commerce done through mobile applications? Undoubtedly, as the technology continues to improve. Will our phones be self-scanning devices, reading bar codes for information and able to process transactions? Again, we can see a day where this will move well beyond the beta concepts we've seen to date. At the Real Future Store in Germany, the technology already exists (but it was down, of course, during our visit).

Internet Retailer reports 83 mobile apps for commerce and 134 broader mobile commerce sites for retailers. We suspect that number rises daily though there is no clean way to get a read. Type in retail and a variety of pages come up.

As for the apps out there, we do see some things of interest:

- *Virtual catalogs are being published by a number of companies, providing a good way to showcase what's new and links to purchase.*
- *Recipe creators that generate shopping lists have real potential and are being developed by retailers and manufacturers. There is real popularity among calorie counters, restaurant finders and recipe apps, so this is a natural extension.*



An example of a Do It Yourself video at Home Depot

- The basics include a store finder and some sort of gift giving option. Managing registries, gift cards, gift finders and shopping lists are also standards.
- More creative-style mix and match (Gap) or DIY videos (from Home Depot) begin to hone in on the uniqueness of the brands.



Gap's Style Mix and Match

Again, we stress that there needs to be a cohesive strategy behind development that can ultimately drive sales (or at the very least, influence the customer).

We're Just Beginning

Well over a decade ago, we began to chronicle e-commerce, with our first issue debuting in June 1996. Back then, there was little commerce to talk about, as the consumer and technology both needed to catch up.

As we discuss multi-channel commerce, the impact of social media and mobile commerce, we feel that we're at a similar point in time. There's tons of activity, some promising developments but not a lot yet in many of these areas to speak to definitive ROI.

Our advice and caution:

- *Get serious about these areas now or risk falling well behind, particularly with the next generation of consumers who will be the future.*
- *Begin experimenting with what works and what doesn't...*

But, be strategic in how you get there. Fools, indeed, rush in.

RETAIL WATCH

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