

THE OLIVER WYMAN

**RETAIL & CONSUMER  
JOURNAL**

VOLUME 7

# FOREWORD

Welcome to the 7th edition of the Oliver Wyman Retail & Consumer Journal. While it is a truism that change is the only constant in life, what has been astonishing over these past seven years is the magnitude and scale of the change. A glance at the table of contents of past Journals makes clear just how big a transformation we have lived through. What is so striking are not the topics themselves – customer satisfaction, pricing, assortment, purchasing, costs, operations, logistics, and software. No, what is striking is the emergence of new realities, which have fundamentally changed the game – and in retrospect were not so easy to predict. We have chosen these new realities as the focus for this year’s Journal.

Smartphones existed seven years ago, but the use of handheld devices to shop and pay wirelessly for everything, everywhere was not a reality. It is today. The integration of mobility with shopping has been revolutionary. And the integration of payments into the shopping experience will prove to be equally revolutionary. “Payments in Retail” provides insight into what has happened, what is likely to happen, and how retail and consumer companies need to react.

The internet has been with us for 30 years and continues to be a primary driver of change and disruption. For decades, suppliers and retailers have battled for margin within a relatively static country-by-country, market-by-market trade terms framework. But that framework is rapidly being dismantled. Price transparency for consumers, aided by legislation, has driven cross-border shopping to levels never seen before. Retailers, too, have identified arbitrage opportunities across markets and are exploiting them. Trade terms are the battlefield, and price convergence the likely outcome. “Cross-Border Arbitrage” assesses the current state of play.

Data mining has become critically important to companies wishing to optimize their value proposition to millions of customers. And it has often proven much more effective than consumer research not only in understanding buying behavior but also, crucially, in creating a tailor-made customer offer. But data mining has its limits: While it provides incredible detail on existing customers for existing offerings, it is less good at predicting future behavior. “Social Listening” provides a new and fascinating insight into the mind of the customer – and may well one day make traditional customer research obsolete.

The world of hard and soft goods has changed dramatically as well. In the past, most luxury companies focused on brand and exclusivity, and less so on building a direct relationship with the customer – traditionally the USP of the retailer. That is changing. Online shopping has emerged as a threat, and one that must be met. For luxury players, e-commerce represents not only a defensive move but also a potential game changer. “The E-Commerce Upside” explains why.

As grocery stores continue to evolve, so does the way we shop. Traditional supermarkets are embracing a new information age for groceries – one that focuses on technology while still making the most of its customer. At the same time, supermarkets still need to keep the in-store experience compelling for customers, but that means changing their model profoundly. “Revolution in the Aisles” looks at how grocers are changing the game via technology, while “Fighting for the Future of the Supermarket Industry” deep dives into how grocers must solve holistically for a multitude of risk, strategy, and people challenges in-store.

Despite the change and uncertainty revolving around the supermarket, one thing has not changed. Freshness is still an enormously important driver of success – for many even more important than price. Leaders in fresh outperform and create true separation from competitors, especially the online variety. But what leadership in fresh means, and how to achieve it, are still challenging questions. Our multi-country consumer research provides some interesting and thought-provoking answers.

Another new reality has taken place with astonishing speed – the emergence of China not only as a source of supply and an enormous pool of consumers (not news), but also as a leader in retail and consumer innovation. Whereas seven years ago, Chinese executives might have looked to the West for best practice, now it is the West making the study visits. Integrated supplier, retailer, and payment ecosystems, driven by artificial intelligence and machine learning, may well represent the future for us all. Our tour of China takes a closer look.

We round off this edition of the Retail & Consumer Journal with the thoughts of two chief executives who have enjoyed long and storied careers. They provide their take on the state of retail and consumer, as well as what they see happening going forward.

I wish you interesting reading!



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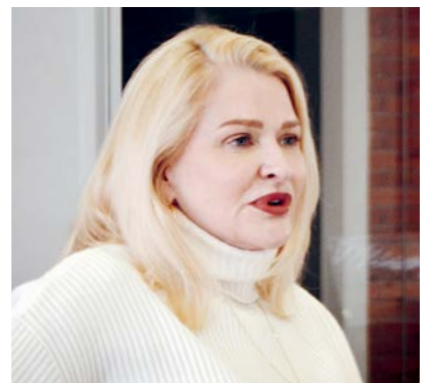
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# PAYMENTS IN RETAIL

THE FUTURE OF SHOPPING WILL BE SHAPED  
BY RETAILERS PROVIDING AN INTEGRATED,  
STREAMLINED PAYMENT EXPERIENCE

Ensuring a seamless and enjoyable customer journey has always been a focal point for retailers. Until recently, the standard journey was well covered: Go to the store, browse the merchandise, and select a product for purchase. However, the payment experience – albeit central to the journey – has long been neglected, with retailers generally choosing to outsource the responsibility to banks, largely due to its complexity. While making payments may seem run-of-the-mill and seamless to many customers, complexity arises as shopping channels, technology, issues with types of payment, and consumer preferences evolve rapidly.

Retailers are beginning to develop strategies around integrating payments into their value proposition. While some still see payment as a process to be optimized from a technical and cost standpoint, implementing the right payments strategy is an opportunity for retailers to gain a real strategic advantage.



## A SEAMLESS PAYMENT EXPERIENCE IS THE DIFFERENTIATOR THAT AMAZON, UBER, AND WECHAT ALL HAVE IN COMMON

Have you ever wondered what business trait Amazon, Uber, and WeChat have in common? All of them have harnessed the untapped power of the payment experience in enhancing the customer journey, and have based their success on it.

**AMAZON** is leading the way in using payment as a strategic control lever. The company offers countless forms of payment, checkout is fast and seamless, and payment is secure. The Amazon payment experience is a differentiator: For the same product at the same price, users will often choose Amazon for its 1-Click button ordering. In addition to using payment as a pillar of its value proposition, Amazon has further used payment as a loyalty tool to expand its business and to capture larger market share and profitability.

**Amazon Prime Reload:** This offers 2 percent cash-back to Amazon Prime customers when they load money from a bank account or debit card into their Amazon prepaid account.

**Amazon Prime Rewards Visa Signature Card:** This is a relaunch of the Prime Credit Card, targeted at Amazon Prime customers to encourage loyalty. Card users are entitled to 5 percent cash-back for purchases made on Amazon and 1 percent to 2 percent cash-back on purchases at other retailers.

**UBER** has frictionless payment capabilities that are the most powerful assets of the centralized customer journey platform. A cashless experience for car transportation was the differentiator that formed the foundation for Uber's success among drivers and users. More recently, Uber has expanded its payment and service offerings outside of its core application.

**Uber digital payment:** Uber accepts various digital payment methods including PayPal, Alipay, WageWorks commuter credit, and Apple Pay. It also uses its underlying payment platform (among other synergetic assets) to develop Uber Eats, a restaurant marketplace app, which successfully entered an already competitive market by offering a well-proven and seamless payment experience.

**Driver Instant Pay:** Uber has enhanced its payment experience for drivers as well. The Instant Pay solution allows drivers to get paid up to five times per day, helping to address their short-term liquidity concerns. For a small fee, this service allows cash to be taken out with an Uber debit card or personal card.

**WECHAT** has transformed itself from a basic instant messaging and social media platform to a holistic ecosystem that connects people, services, and businesses. The company's swift rise to success can be attributed, in no small measure, to the introduction of WeChat Pay, a digital wallet that allows users to make mobile payments and send money between contacts. WeChat Pay contains numerous payment capabilities and offerings, which have significantly affected how people use and interact with the application.

**Peer-to-peer payment:** Users who provide bank account information can transfer money into a friend's WeChat Wallet balance. Recipients can then pay it into their personal accounts or use the funds for other purchases through WeChat.

**Commercial transactions:** Consumers can now use the app to pay bills, order and pay for a cab, and purchase goods online. Companies use WeChat Pay in four ways: in-app payment, QR code payment for desktop websites, e-commerce for owned channels, and quick pay for in-store purchases.



Thanks to its unique payment experience and offerings, WeChat has grown from roughly 400 million users in 2014, when it introduced WeChat Pay, to around one billion registered users today, 800 million of whom use WeChat Pay.

## UNFORTUNATELY, MOST RETAILERS FAIL TO OFFER A SEAMLESS PAYMENT EXPERIENCE TO THEIR SHOPPERS

Retailers have generally been very attentive to providing a differentiated and enjoyable customer experience, but have neglected the payment dimension. For customers, the payment experience is poor, making the checkout process underwhelming at best. The “VWO eCommerce Cart Abandonment Report 2016” has shown online cart abandonment rates as high as 60 percent to 80 percent, and the magnitude of missed sales is massive (Exhibit 1). The same holds true for physical stores, where the use of EMV (Europay, Mastercard, Visa) chip cards and slow point-of-sale hardware terminals cause a poor purchasing experience, affecting customer satisfaction and, ultimately, store traffic.

Exhibit 1: Getting payments wrong has a high cost

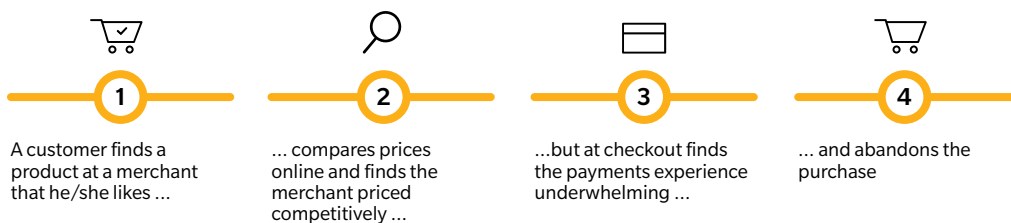
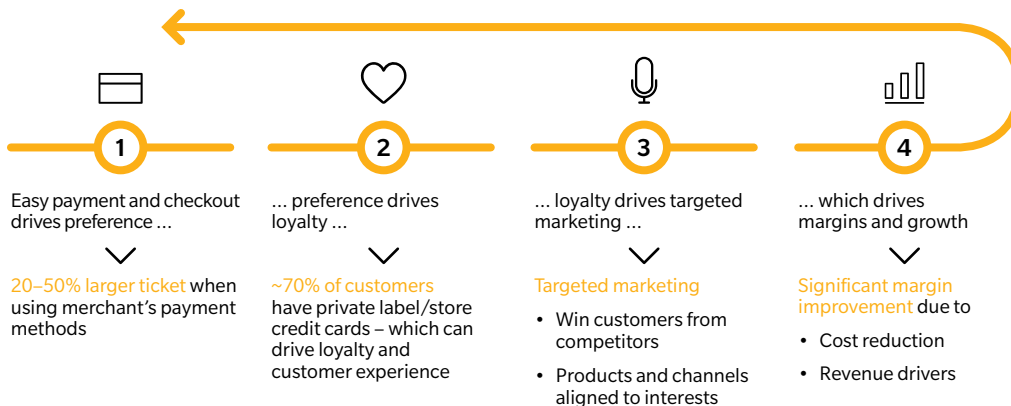


Exhibit 2: Getting payments right boosts sales and loyalty



Source: Oliver Wyman analysis, Morgan Stanley Research

# PAYMENT IS A CRUCIAL AND LARGELY UNTAPPED OPPORTUNITY FOR RETAILERS TO INCREASE REVENUES AND IMPROVE PROFITABILITY

Creating a payments strategy that enhances the consumer experience can simultaneously develop loyalty and grow revenues, as well as optimize margins (Exhibit 2). How?

## LEVERAGE PAYMENTS AS A LOYALTY TOOL TO DEVELOP CLIENTS

Payments can serve as a hook for retailers to drive penetration and go beyond the typical loyalty construct. Key questions for retailers on using payments as a loyalty tool include:

- How can payments protect my customer relationships while enhancing customer experience and my brand?
- How can I offer a differentiated rewards value proposition using payments?
- How can I exploit payments data to deliver customized offers to customers?

An effective way for retailers to drive revenues is to integrate rewards management into the payment and checkout process, and to create personalized services that can help drive loyalty. Publishing relevant offers, coupons, and messaging linked to consumers' payment preferences and shopping patterns will optimize the return on advertising expenditures.

For instance, Uber launched a new branded credit card in 2017 with Barclaycard. It enables customers to receive cash back for Uber-related purchases, including Uber Eats, encouraging more spending on Uber's platforms. Similarly, Uber has partnerships with American Express and Visa that encourage cardholders to use Uber to gain credits.

## USE PAYMENTS TO GENERATE ANCILLARY REVENUES

As a starting point to generating growth through payments, retailers should look for ways to create unique checkout solutions for customers consistent with their brand. These can take different forms as shown in Exhibit 3.

Referring to our previous best-in-class players, Amazon developed financial services enabling it to drive more revenues: For unbanked or underbanked customers, Amazon Cash offers a prepaid account that can be used for purchases on Amazon.com. Customers can preload cash (without any fees) to their Amazon accounts through several participating retailers.

On top of ancillary revenues, a strong payments infrastructure is critical in an omnichannel era where players must offer an integrated and seamless cross-channel shopping journey, including pick-ups and returns. Different payment platforms for physical and online operations complicate reconciliation, inventory, and refunds, and obscure the true cost of payments.

**Exhibit 3: Revenue drivers for retailers using payments**

OPPORTUNITIES	DESCRIPTION	BENEFITS
<b>Alternate forms of payments</b>	Enabling global customers to pay as they prefer	<ul style="list-style-type: none"> <li>• Higher cross-border sales</li> <li>• Higher conversion/ lower abandonment</li> </ul>
<b>Contextual commerce</b>	<ul style="list-style-type: none"> <li>• Ability to purchase when/where you want</li> <li>• Use single sign-on for easy check-in</li> </ul>	Easier user exchange leads to seamless checkout
<b>Financial services</b>	Linking payments to: <ul style="list-style-type: none"> <li>• Credit (installment loans/ POS financing)</li> <li>• Other value-added services (e.g. DCC)</li> </ul>	<ul style="list-style-type: none"> <li>• Higher customer spending power</li> <li>• Opens up fee income possibilities</li> </ul>
<b>Targeted surcharging</b>	Charging a fee for more expensive forms of payments or in certain markets	<ul style="list-style-type: none"> <li>• Ancillary revenue stream</li> <li>• Manage acceptance costs</li> </ul>
<b>Proprietary forms of payments</b>	Payments mechanisms designed to drive higher purchases (e.g. co-brand/PLCC)	<ul style="list-style-type: none"> <li>• Enhanced loyalty and spending</li> <li>• Lower payments costs</li> </ul>

Source: Oliver Wyman analysis

## MANAGE THE TOTAL COST OF PAYMENTS

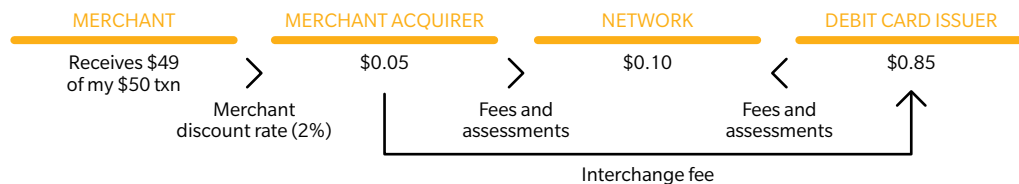
The illustrative scheme in Exhibit 4 shows the economics for the participants in a 50 US-Dollar credit card purchase and is subject to significant variability depending on:

**Geography:** National regulations have an impact on interchange fees and customers' preferred payment types, such as cash, debit card, and credit card. How can retailers standardize processing fees in different jurisdictions and reduce the overall cost?

**Cross-border or domestic commerce:** International transaction fees can cost up to eight times as much as domestic because of factors such as dynamic currency conversion and VAT refunds. Are there ways to reduce costs resulting from international transactions?

**Brand or type of card:** Interchange levels vary by provider (such as Visa), tier (gold or silver, for example), and type (corporate or other). How can retailers optimize relationships with vendors and card issuers to minimize these interchange fees?

Exhibit 4: Payment fees breakdown per type of players in the payment value chains



Source: Oliver Wyman analysis

A more effective approach to capture greater value from this value chain for a merchant consists of:

- Systematically breaking those costs down as per the above structure and building internal cost reference to challenge them individually. Such internal knowledge should, for example, establish that switch fees between the acquirer and the network typically range from one cent to five cents for a PIN debit operation in the United States.
- Approaching the market in a consolidated way, as acquirers and networks typically grant discounts for large-volume clients, which can reach 1 percent to 2 percent of the transaction value.

Retailers that have addressed these costs have achieved savings as high as 10 percent, and the results of some sustained initiatives have been even better.

# THE PATH FORWARD


The payments space has been undergoing significant transformation in recent years. From being viewed as a cost of doing business, it has become a key enabler of an integrated and seamless shopping experience that provides a unique competitive advantage. Leading companies such as Amazon, Uber, and WeChat have made significant investments to implement successful payments strategies. These companies are shaping the future of shopping through an integrated, streamlined payment experience.

To offer their customers the best possible payment experience, retailers need to ask themselves the right questions in building their strategy:

- What are my customers' needs and how can an improved payment experience help to fulfill them?
- How can I use payment to enable seamless, personalized interactions with my customers? What value-added services can I offer?
- What is the right way to think about my own proprietary forms of payment versus third-party forms of payment?
- How do I arrange finance and get organized to radically enhance my customers' payment experience?
- Which partners or providers are best suited to support my journey?
- How do I strike the right balance between fraud management and customer experience?
- What implications do the global trends in data protection have for my payments strategy?

**We believe the time for retailers to act is now. Payments can be a key tool in increasing revenues and growing overall businesses, while providing opportunities to reduce operating costs. However, deriving increased value from payments requires careful thought and execution, and finding the right partners when necessary.**





# CROSS- COUNTRY ARBITRAGE

A MULTIBILLION-DOLLAR THREAT  
TO THE CONSUMER PACKAGED  
GOODS INDUSTRY

For decades, consumer packaged goods (CPG) companies have run their go-to-market and trade spend through national subsidiaries. This has allowed adaptation to the local environments: It also did no harm, as long as the retailers on the other side focused merely on their markets. But that game is changing – and changing fast.

Companies such as Amazon simply refuse to play the traditional game. The company systematically assesses trade terms throughout Europe and buys at the absolute lowest price across markets. Amazon is not alone – others are doing it too. Retailers are becoming more sophisticated, forming international buying alliances that allow them to cherry-pick across markets and cut prices further. Adding to the CPG headache, consumers are also buying internationally, enabled by the internet and regulatory changes. Our research indicates that the resultant arbitrage risk for CPG companies is up to a fifth of total market size. The threat is substantial and, for some, existential: It is a race for superiority, accelerating all the time.

## A RADICALLY DIFFERENT RETAIL LANDSCAPE

The retail landscape is undergoing radical change – and with it, trade-spend requirements. Retailers, under pressure from e-commerce and discounters, are becoming more sophisticated so as to survive the onslaught of e-commerce and discounters. With online sales exploding, even legacy brick-and-mortar retailers are seeing more and more of their sales move online and they are putting greater emphasis on that part of their business. Even smaller retailers are gaining greater visibility into price differentials, thanks to marketplaces.

Retailers in particular are besieged by the spread of e-commerce and rise of discounters. Furthermore, price comparison engines provide consumers with increasing transparency on price levels at different retailers, which has intensified competition.

International retailers like Amazon and the grocery discount retailers have built up sophisticated cross-border buying capabilities. And retailers are now following suit, consolidating purchasing in their own international operations, as well as joining retail alliances and buying groups. Sourcing is becoming more professionalized and internationalized: A series of cross-border mergers and acquisitions has helped retailers optimize their sourcing in key segments including food, beauty and healthcare, and consumer electronics.

### **CROSS-BORDER ARBITRAGE EXPOSURE**

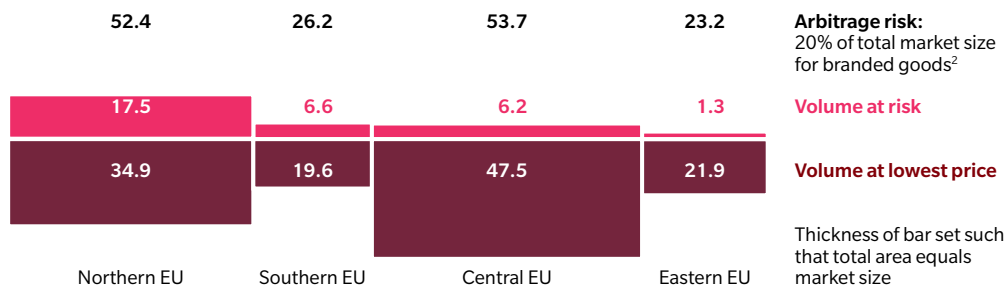
One reason retailers are able to profit from international sourcing is the inability of many CPG companies to manage pricing internationally due to their lack of a systematic mechanism for pricing across markets. Historically, CPG makers have operated their businesses on a market-by-market basis: So, the sales organization in Germany, for example, only focuses on German retailers, while the Netherlands is served by a separate sales team. As a result, different sets of conditions and prices apply to the two countries.

This has given rise to a growing risk exposure for branded goods. The arbitrage risk from retailers sourcing products at lower prices in different markets is 20 percent on average for branded goods (Exhibit 1). For grocery, that amounts to a commercial risk exposure FOR SUPPLIERS of more than 30 billion euros in European markets alone, according to an Oliver Wyman analysis of several fast-moving consumer goods categories.



**Exhibit 1: 20% of branded consumer revenues may be at risk from cross-border grocery retail purchases**

MARKET SIZE AND ARBITRAGE POTENTIAL PER REGION OF SEVERAL PRODUCT CATEGORIES<sup>1</sup> in BN €



1) Spirits, confectionaries, soft drinks, homecare

2) 18% total market size inclusive own label

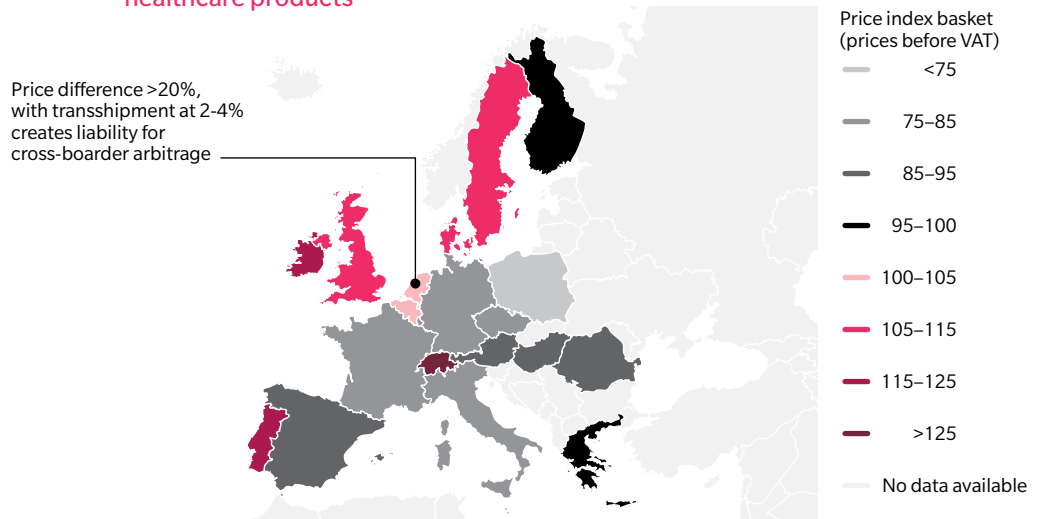
Source: Euromonitor, Oliver Wyman analysis

## THE CHALLENGE OF THE SOPHISTICATED CONSUMER

In addition to cross-border sourcing arbitrage risk, there are challenges posed by the differences in consumer prices. Price comparison portals and deal sites provide a new level of market transparency, while mega-platforms like Amazon legitimize those prices and accelerate their changes. This threatens the effectiveness of promotions and domestic pricing models. On average, prices of a range of identical consumer products can be 1.5 times higher in some European markets than in others. Beauty and healthcare products, for example, are over two-thirds more expensive in some European markets than in others (Exhibit 2).

An army of small- and medium-sized businesses has sprung up, leveraging these arbitrage opportunities by shipping goods across markets, thus creating price conflicts. In addition, price-matching algorithms, such as Amazon's, have pressured retailers to match prices outside the markets they operate in. If any product becomes available online for a lower price – sometimes as a result of uncoordinated international pricing by manufacturers – other retailers quickly have to match this.

## Exhibit 2: Cross-country comparison of consumer retail prices for select beauty and healthcare products



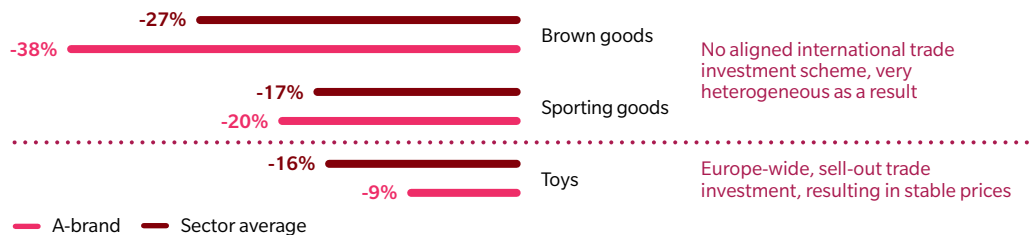
Source: Retailer websites, Oliver Wyman analysis

## TARGETING THE A-BRANDS

The price pressure is particularly intense in the more expensive product categories, such as consumer electronics and spirits. To compensate for the margin loss, retailers demand additional discounts of various kinds from consumer goods companies. Discounting comes with its own set of challenges, as brand perceptions are threatened if consumers get used to cheaper prices for certain products. Mass-market brands – or “A-brands” – are prime targets: As retailers like to promote them aggressively to create traffic, cross-border price imbalances trigger price erosions especially quickly (Exhibit 3).

## Exhibit 3: A-brands are especially vulnerable to price erosion, Example Germany

### 6-MONTH PRICE EROSION



Source: Retailer websites, Oliver Wyman analysis

# TRADE-SPEND MANAGEMENT: A SIX-STEP PROGRAM

CPG companies need to get their act together and understand how they are making their money and where they are making it. But doing that calls for fundamental transparency allowing them to see and know what their products sell for in one market versus another – something they are currently in the dark about. Many CPG companies lack transparency around how much an article sells for in one market versus another: A six-pack of beer may sell for 25 percent less in the UK than in France, posing a considerable arbitrage risk to the CPG maker. While some consumer goods companies are wrestling with and dealing with these challenges, there is no silver bullet. But our work has seen the emergence of a powerful tactical framework and toolkit to help companies regain the initiative: Effective measures include offering a portfolio of differentiated products for different markets; harmonizing prices and trade conditions throughout Europe; and more closely managing the retailer relationship. All of these initiatives depend on a strong and consistent trade invest management scheme, which must include both fundamental capabilities and specific measures (Exhibit 4).

Exhibit 4: Holistic international approach to improved trade spend



Source: Oliver Wyman

# SIX FUNDAMENTALS FOR MANAGING TRADE INVESTMENT

## 1. END-TO-END TRANSPARENCY

Transparency is a key enabler of successful trade-spend management. But many manufacturers with international operations lack a comprehensive overview of 3net prices – the prices of goods after recurring discounts – paid for their products in different markets. The main problem: Trade terms differ from market to market, as do conditions for offering these terms. In France, for example, promotional discounts are capped by law, so other discounts are used to compensate. In Spain, unconditional permanent price reductions tend to be far higher than in other southern European markets.

**Step One: Achieve a standardized, comprehensive view of the discounts that retailers are being given across all markets.**

## 2. A HARMONIZED TRADE-INVESTMENT GRID WITH PAY-FOR-PERFORMANCE:

Trade-spend management is a complex process with multiple objectives – and it is usually iterative, so constantly needs updating. A harmonized trade-spend grid is a basic requirement. The grid should be harmonized so that trade conditions in different markets are represented in a common language, making comparisons easier.

Best-in-class consumer goods companies operate with a central platform that collates trade spend across different markets and channels. This transparency improves decision-making at all levels, and helps with reporting. A large part of current trade-spend consists of unconditional discounts: Prices are reduced for a particular retailer – for example, because of its size – irrespective of how that retailer then proceeds to sell the goods.

But it is smarter to offer discounts with provisions – making them conditional upon presenting the products in a certain way or meeting volume targets. So, when central and local teams allocate funds for different customers, they can define pay-for-performance objectives, which should fit the manufacturer’s broader strategic objectives. Mechanisms will be needed to enforce pay-for-performance agreements in a coherent, consistent manner. The CPG maker might, for example, dispatch staff to check that retailers are meeting the conditions. The proportion of discounts offered with and without stipulations will vary greatly between markets. In some cases, those terms may be ineffective and not lead to better collaboration – if, for instance, a sales target is too easy to achieve, or if a retailer has to display at least three products of a brand, when it is already displaying five.

**Step Two: Develop a harmonized, unified trade-investment grid that presents and compares trade conditions in different markets in a straightforward way.**

### 3. ACTIVE STEERING AND GOVERNANCE:

A governance structure will be needed to ensure active management of trade spend in individual markets. Local organizations will have to keep track of performance and feed information back to a centrally maintained data platform. Guidelines should be set for the allocation of trade spend in different channels and markets – both physical and online, and including the internationally operating retailers. The allocation will depend on several factors. One is corporate strategy, where the manufacturer wants to grow. Others are a brand's contribution and market performance, namely where a product's main growth is happening. A trade fund allocation tool can be a great asset in determining optimal trade allocation.

**Step Three: Establish a governance structure for overseeing trade spend in different markets.**

## INTERNATIONAL TRADE-SPEND MANAGEMENT CAPABILITIES

### 4. CREATING AN INTERNATIONAL TRADE-SPEND ORGANIZATION

Grocers are increasingly participating in international buying alliances. Others, such as Lidl and Amazon, are operating a similar system in their own organization. Alliances with more than five members have historically focused on negotiating discounts based on their large combined volumes of a manufacturer's products. Recently, however, even smaller alliances of two to four retailers – EURELEC and Envergure, for example – have started to negotiate product prices.

Consumer goods companies, too, need a more coordinated approach. This should have a central team that collects and analyzes trade-spend data in order to produce insights on different markets and channels. The central trade team will help to standardize trade-spend structures, definitions, and processes. It will also be responsible for allocating funds to different markets and channels based on their strategic objectives. And it will provide parameters – such as maximum prices – for local teams when they are negotiating with local customers. The central team will get increasing responsibility for managing international clients and buying groups, while local teams negotiate with local retailers.

**Step Four: Create a centralized trade-spend team to align terms and coordinate cross-country trade investment.**

## **5. A STRATEGY FOR INTERNATIONAL KEY ACCOUNTS AND BUYING GROUPS**

Once a central team has been established, it will be in a position to leverage insights across markets and deal with international clients and buying groups. The insights can be used to allocate trade spend based on growth potential and the channels the retailer is active in, and how these contribute to strategic objectives. Prices across markets and channels can be standardized to varying degrees. They can be fully harmonized across markets, or they can be made consistent within pricing corridors so that any price differentials are so small that it will not be worth transshipping products across borders.

**Step Five: Develop a growth-driven strategy allocating trade spend for key accounts and buying groups.**

## **6. A TOOLKIT TO MITIGATE INTERNATIONAL PRICE ARBITRAGE**

The first step to deal with international price arbitrage is to establish which product areas are at risk. Once the largest threats have been identified, mitigation measures can be selected that best fit the company, brand strength, and positioning. An array of different levers is available in three groups (Exhibit 5). The first group is related to selective distribution, which includes design variants: Several A-brand product manufacturers offer larger pack sizes to Lidl than to other retailers, for example. A second group is pricing policy: In one cashback example in the Netherlands, Heineken offers a free glass of beer in a bar to shoppers who buy a crate of beer in a Dutch supermarket. The third group, retailer management, includes establishing a strategy to deal with Amazon Marketplace and the like: This can be done either through dedicated programs for premium products or by engaging in strategic partnerships with a few selected marketplace sellers.

**Step Six: Create a toolkit for improving price consistency by identifying the biggest threats and potential mitigation levers.**

Exhibit 5: Consumer goods companies can pull many levers to improve price consistency

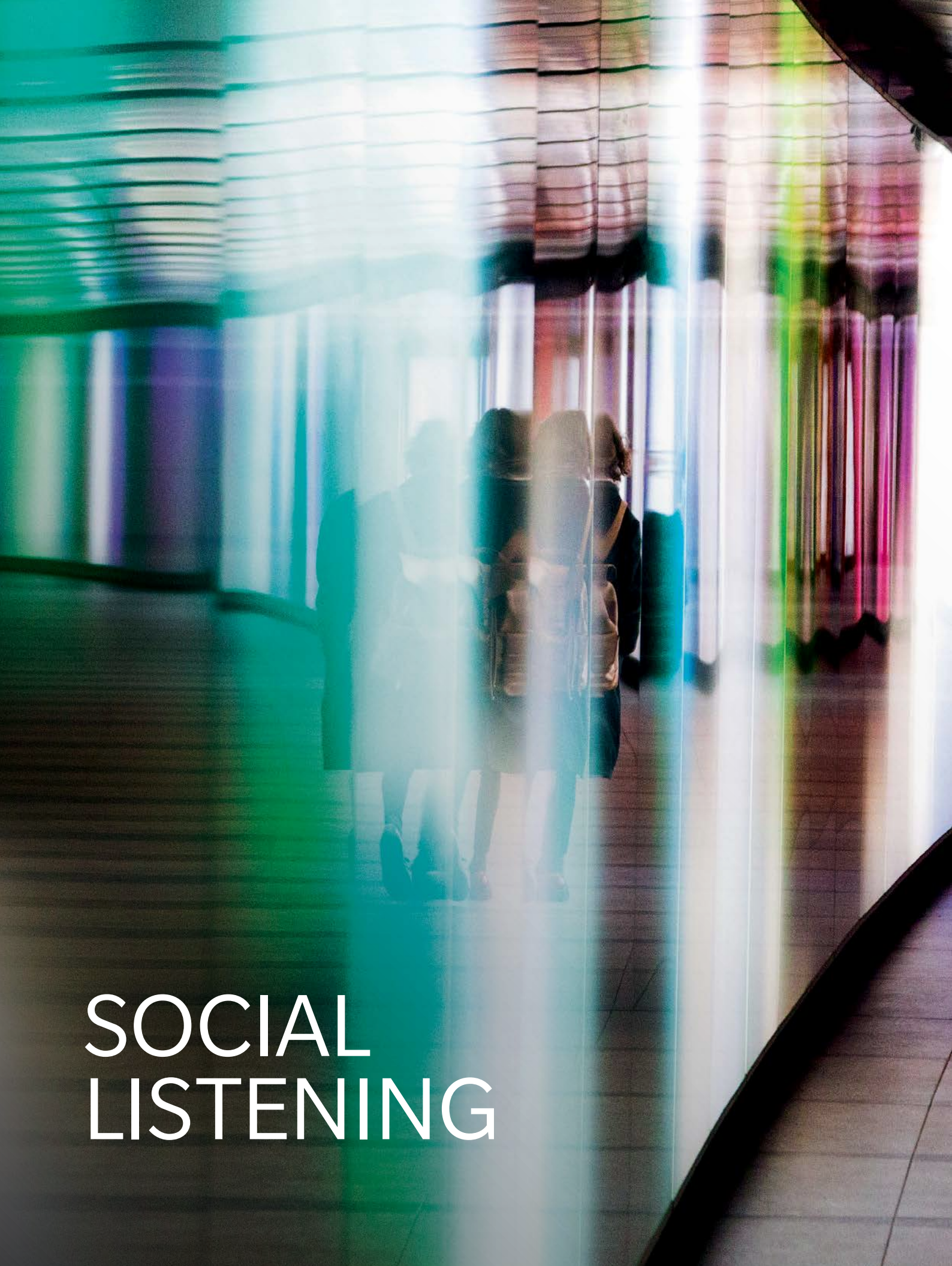
SELECTIVE DISTRIBUTION	PRICING POLICY	RETAILER MANAGEMENT
<b>Bundles</b> Bundling of products with complementary services	<b>Rebalanced margin alignment</b> Trade spend reflecting margin expectations, particularly with multichannel clients	<b>Marketplace strategy</b> Whitelisting of marketplace retailers  Active support of marketplace retailers, e.g., through selective distribution concepts
<b>Design variants</b> Retailer-specific variants differing in non-functional specs (e.g., EAN, design)	<b>P4P-linked trade investment</b> Link of (amount of) trade investment to retailer counterparts, including distribution quality	<b>Selective marketing support</b> Preferential platform-specific marketing investment (e.g., AMS) on specific resellers only
<b>Exclusives</b> Functionally different product variants given to single retailers only	<b>Selective cashback</b> Cashback offer to end consumer, if products bought through selected channels	<b>Margin pool monitoring</b> Ongoing complaint tracking of prices together with suitable response mechanisms
<b>Smart distribution</b> Distribution of entire product ranges through subset of channels only	<b>Selective additional services</b> Selective spend of non-cash measures, e.g., supply-chain services, PoS promoters	

Source: Oliver Wyman

## RETAILERS ARE MOVING FAST AND MANUFACTURERS NEED TO AS WELL

Product manufacturers need to build new capabilities to deal with the increasing internationalization and sophistication of retailers’ operations. There is no single formula, but the starting point is to create transparency in trade spend as a way of understanding where a manufacturer is vulnerable and where opportunities lie. There are numerous tools that can help combat the threat: It’s up to each manufacturer to figure out the ones that will work and to use them effectively.

In some cases, they will have to make trade-offs. If, for example, a manufacturer harmonizes prices across the EU, its products will end up being relatively pricey in some countries. It will then have to figure out the optimum balance between margin stability and volumes. Whatever manufacturers decide, they will need to act fast. If they don’t, retailers will outsmart them, and large areas of their business will be at risk.



# SOCIAL LISTENING





## THE REVOLUTION IN UNDERSTANDING WHAT YOUR CUSTOMERS REALLY WANT

Companies have traditionally relied upon consumer surveys, focus groups, and research reports to figure out what people think of their products or services. But these approaches have several shortfalls. Sample sizes are limited and subject to bias. The studies take time to organize and the results quickly become dated. Moreover, what people say often differs from what they do, like when they complain about discount airlines but then use them all the same.

Social listening provides an alternative that is enabling companies to tap into much richer consumer insights that are generated in real time. Every day, hundreds of millions of people talk publicly on social media about where they have been, what they have bought, and their good and bad experiences. Or they just express their feelings and opinions. This information is a gold mine for consumer-facing industries, including retail, consumer goods, retail banking, insurance, and healthcare. But so far, most companies have not turned this information into value.

In our experience, companies can gain a competitive advantage by analyzing what consumers say on social media because they can obtain better insights at a fraction of the cost and then act on them at lightning speed. Social listening is increasingly informing the new product development, marketing, operations, and international expansion of consumer product companies. It can also aid early crisis management and help spot potential corporate acquisition targets. Put another way, social listening can be turned into the map in a treasure hunt.

Until now, social listening has mostly been limited to public opinion monitoring. For example, it is used to count the number of times a brand is mentioned – “buzz” – and whether the content is positive or negative – “sentiment.” But this monitoring tends to yield only standardized or aggregated metrics, which seldom lead to actionable business decisions.

Recently, advances in machine learning have made smart analysis of natural language content possible, as well as the monitoring of pictures and videos. In our experience, the new techniques have been very effective in enabling companies to investigate a wider range of consumers’ feelings and follow different aspects of their lives. We have seen how their preferences can be mapped and updated immediately, as can the ways in which customers connect with and influence each other.

## Exhibit 1: What can go wrong when analyzing source posts

DIMENSION	WARNING SIGNS	ACCURACY RATE
<b>Content of post</b>	<ul style="list-style-type: none"> <li>• Too sales-driven</li> <li>• Overly positive – likely to be promotional</li> <li>• Weblinks are added to the posts (depending on destination of the address)</li> <li>• A large volume of identical or similar posts in a short time</li> </ul>	<p><b>50%</b></p> <p>Rules-based classification/filtering</p>
<b>Author</b>	<ul style="list-style-type: none"> <li>• A company’s official account</li> <li>• An identified KOL/influencer/tribe leader</li> <li>• Very few connections</li> <li>• A brand-new account</li> <li>• Has posted identified fake posts or promotional posts in the past</li> <li>• Always posts at a similar time of the day or else very randomly (showing, perhaps, no discernable sleep pattern)</li> </ul>	<p><b>90%</b></p> <p>Machine-learning approach</p>

Source: Oliver Wyman analysis

Machine learning can also overcome the problem of “unclean” data. Companies often buy social media data from a vendor, but many of the source posts do not actually come from consumers; instead, they have been written by the brand’s marketing agency, e-commerce sellers, or robots. In fact, we discovered in one case that more than nine out of 10 posts provided by a data vendor had not actually been written by consumers. Such posts are typically overly positive and give a false impression of a brand’s health. Machine learning can analyze accounts and their content in order to filter out such fake posts (Exhibit 1).

We are only beginning to scratch the surface of how these machine learning advances will enable social listening to eventually rewrite the rules for consumer product companies. But already, we are seeing social listening overturn how consumer product companies develop, market, and package their products. We have seen multiple examples of how social listening can help consumer companies.

## GENERATING CONSUMER INSIGHTS

Social listening can uncover hidden links between consumer markets that are heavily influenced by others, as consumers take cultural or fashion cues from places they feel an affinity for. Analysis of social media posts, for example, shows that the Indonesian cosmetics market is now more heavily influenced by trends in Thailand than from France or Japan. It also points to the products and brands concerned, as well as the reasons for the link. For example, one Instagram post about a face powder read: “Best seller in Thailand! Super fit for my skin color.” Another referred to a product’s sun protection factor.

## HOW TO IDENTIFY A TRIBE THAT IS IMPORTANT TO A PRODUCT CATEGORY

### WHAT IS A TRIBE?

Users are connected with each other (follow each other)

They exceed a minimal level of engagement

There are one or more common themes in their engagements/discussions

### EXAMPLE OF AN IDENTIFIED TRIBE OF NEW MOMS

Each node represents one user



Each link represents a connection between two users:  
Thick link = strong connection

Large, hollow nodes are tribe leaders; the size of their nodes is proportional to their advocacy potential

Source: Oliver Wyman analysis

These comments indicate that Indonesian users of cosmetics see similarities with Thailand in climate and people's skin color, and that they feel that products popular in Thailand will be right for them. Makeup manufacturers might therefore want to consider taking products that work in Thailand and launching them in Indonesia, perhaps also using their popularity in Thailand as part of an Indonesian marketing campaign. Indeed, in makeup our work suggests that product manufacturers could increase their return on investment in Indonesia by up to 20 percent by identifying and partnering with the most-promising brands in Thailand.

We have seen how comments on social media can also help develop new versions of products. For example, a manufacturer can often double its rate of hit products from, say, one in 10 to one in five with better consumer information, halving the cost of developing also-ran products. Social listening thus brings manufacturers closer to consumers, enabling them to make customized, small-lot products for specific groups.

### MAKING TRIBAL MARKETING EFFECTIVE

Analysis of social media interactions is also making tribal marketing much easier and more precise, by locating groups with tastes and needs in common on, say, Twitter or Weibo, its Chinese equivalent. By tracking and measuring the connections between a group of new mothers, for example, marketers can map their tribes and identify leaders – the members who are best-connected with the others. These will likely have significant influence on the tribe's preferences in baby products and other categories they might be drawn to.

Social listening can answer crucial questions about tribe leaders: Do their posts usually get replies? Are they retweeted? Do their photos show them using particular combinations of makeup, accessories, and apparel? In other words, how do the tribe leaders widen interest in the brand? And does the resulting expression of interest lead to retweets and actual purchases? (See Sidebar.)

Once tribes with a strong affinity to a product category have been identified, a brand can then build connections with the leaders, for example by sending them exclusive product previews and samples or inviting them to events. The leaders might then turn these into posts, generating interest in their community about the brand and its latest products. These marketing techniques complement mass advertising campaigns with celebrities and key opinion leaders (KOLs) who are paid for their services. This combination of social listening and tribal marketing can generate a return on marketing spend between 20 and 50 percent higher than traditional advertising.

## IMPROVING OPERATIONS

Consumers often talk on social media about their interactions and experiences with brands, products, and services – such as how bad the packaging is or how poor the delivery was. However, it is tricky to turn such comments into actions. Simple aggregations of the appearances of key words, such as “packaging,” are not useful, since they don’t indicate whether the specific complaint is leakage or unclear instructions on a bottle. They also won’t help establish whether an issue is confined to a particular batch or is a recurring problem. Without such details, it is impossible to take any action that might improve a manufacturer’s operations (Exhibit 2).

But techniques such as natural language processing, machine learning, and image recognition are now helping to identify more precisely what is being said. They can then suggest the right actions. For example, if one social media post complains that a bottle is hard to carry because it is large and made of glass, that information could prompt a manufacturer to study the potential of smaller bottles made of different materials. If other posts praise some foundation makeup for being long-lasting and hiding pores effectively, these qualities might be considered as themes for future advertisements.

Exhibit 2: Social listening – using posts to improve operations or product innovations

DIMENSION	WARNING SIGNS	KEY PHRASES CAPTURED BY NLP <sup>1</sup> ALGORITHM	BUSINESS ACTIONS TO CONSIDER
<b>Packaging</b>	I received it as a present. It might sound silly, but the ease of use of the pump is my favorite thing about this product. As we all know, getting cream out of a typical container with a lid is a pain! The lid and the container get greasy every time after use ...	<ul style="list-style-type: none"> <li>Ease of use of the pump</li> <li>✘ Typical container with a lid gets greasy and is a pain to use</li> </ul>	<p><b>Operations:</b> Introduce pump feature to more products</p> <p><b>Marketing:</b> Use the pump feature more in advertisements for this product</p>
<b>Product quality</b>	The pen has a sharp tip and is easy to draw with. I can draw round my eyes without any blur. But the pen got blunt after a couple of weeks, and now it is as bad as other pens!	<ul style="list-style-type: none"> <li>Sharp tip is easy to draw with</li> <li>No blur</li> <li>✘ Tip gets blunt after a couple of weeks</li> </ul>	<p><b>Operations:</b> Investigate the use of other materials to make the tip last longer</p>

1) Natural Language Processing

Source: Oliver Wyman analysis

## CATCHING TROUBLE EARLY IN LISTED COMPANIES

A less obvious use case for social listening is the early identification of troubled listed companies. Many serious problems – accounting scandals, accumulation of unsustainable debt, and misconduct by senior executives – are preceded by early signs, such as employees talking on social media or in news articles. These might not stand out themselves enough to attract attention at first. But the right techniques can provide clues to help regulators step in and mitigate damage. We have found several examples of accounting scandals, where preceding signs were later identified that could have led to action at an earlier stage.

## THE FUTURE OF SOCIAL LISTENING

In practice, these and other social listening use cases will often be combined. A retail bank launching a greenfield digital unit, for instance, can use social listening to identify and quantify customer pain points, segment potential customers, and inform product design. After launch, influencers can be sought out and targeted and the brand perception tracked in order to optimize products and services continuously.

Still, though social listening techniques have been around for over 10 years, very few companies are making the most of them. That's not because of a lack of material to work with: Publicly available social media data – all of which has been posted with explicit user consent – can be provided by the social media platforms or via third-party data vendors. Instead, the main barrier to making social listening useful has been the quality of the data, which are usually too aggregated to provide significant insight into consumers, or else are based on social postings that include large numbers of fakes. Moreover, obtaining clean data that inform business decisions is not easy. It can require natural language recognition in different languages and advanced techniques to analyze social media accounts and their contents automatically and effectively.

Soon, however, these techniques will be common in consumer-facing industries, and those companies that neglect them will find it hard to catch up. By contrast, product manufacturers that learn how to understand consumers in actionable ways – and to test their reactions in real time – will have a huge advantage.

Typically, we have found, the first step is an audit of the company's current capabilities – its access to data and the analytics techniques it uses – plus the business value they generate. This takes only a couple of weeks and reveals which new social listening techniques will be most effective and the value they can potentially unleash. The company can then carry out an upgrade, revamping the underlying analytics and developing new business use cases for social listening. This usually takes between three and six months – after which smarter business decisions follow immediately. In our experience, commercial benefits follow in just a few weeks.



# THE E-COMMERCE UPSIDE



## LUXURY BRANDS: TURNING THE E-COMMERCE THREAT INTO AN OPPORTUNITY FOR GROWTH

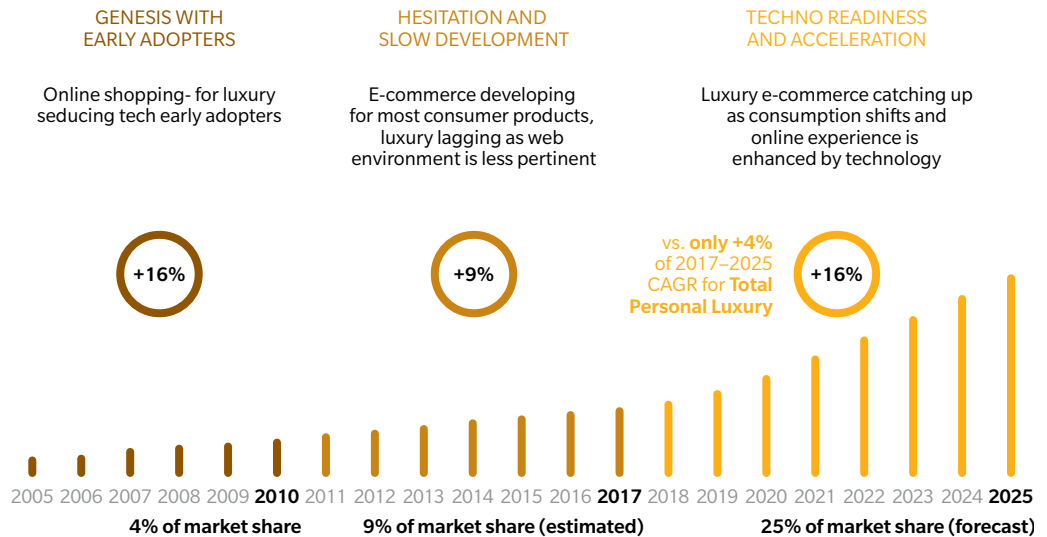
Following the introduction of e-commerce platforms in the early 2000s, luxury brands saw quick adoption by customers. However, product sales through e-commerce channels did not grow as fast as anticipated. We believe e-commerce penetration of the luxury goods market is likely to increase soon and could reach 25 percent by 2025. The challenge for luxury brands is to participate in the growth of e-commerce and protect market share, while maintaining brand positioning. To succeed, luxury brands will have to deliver an outstanding customer experience, seamlessly combining traditional offline channels and e-commerce.

# E-COMMERCE IN LUXURY IS FINALLY STEPPING UP

## E-COMMERCE PENETRATION IN LUXURY BRANDS HAS INCREASED SLOWLY UNTIL RECENTLY

Embraced initially by early adopters and pioneer brands like Hermes, online shopping for luxury goods grew at a 16 percent annualized pace from 2005 to 2010 (Exhibit 1). But following that initial burst, growth slowed to single digits between 2011 and 2017 as consumer interest waned.

**Exhibit 1: Online personal luxury goods market<sup>1</sup>**  
 Historical 2005-2017 and forecasted 2018-2025, US\$ billion



1) Personal luxury goods includes designer ready-to-wear and haute couture, luxury eyewear, designer shoes, luxury leather bags and other small leather goods, luxury jewelry, luxury timepieces, super premium fragrances and super premium makeup and skincare

Source: Euromonitor, Goldman Sachs Equity Search, Oliver Wyman analysis

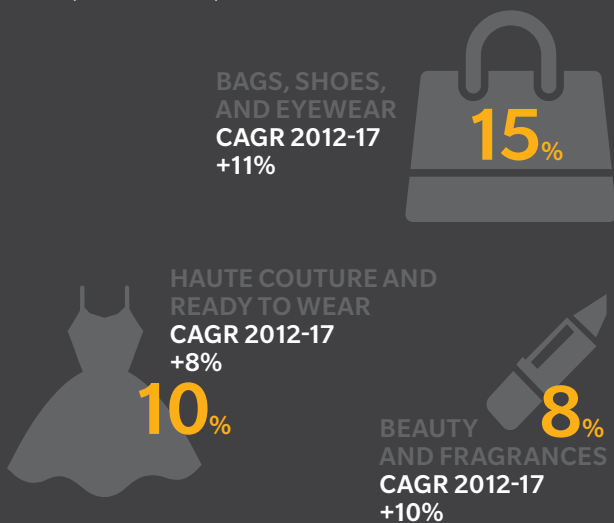
Despite the below-average performance of the online channel for luxury goods, a deeper look reveals a nuanced picture, with different penetration rates across various product categories and regions. Accessories (bags, shoes, and eyewear) generally tend to be the most popular items purchased online, given the absence of fit concerns. But that may be changing (page 35). There is also a wide divergence of e-commerce penetration between different regions: As of 2017, China, the Americas, and Europe have penetration rates of 20 percent, 13 percent, and 8 percent, respectively.



# PENETRATION RATES ACROSS VARIOUS PRODUCT CATEGORIES AND REGIONS

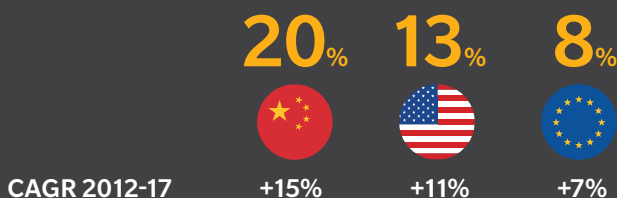
## SHARE OF ONLINE RETAILING – PER CATEGORY OF PRODUCTS

VALUES AS A PERCENT OF MARKET VALUE 2017 (ESTIMATED)



## SHARE OF ONLINE RETAILING – PER MARKET

VALUES AS A PERCENT OF MARKET VALUE 2017 (ESTIMATED)



Source: Euromonitor, Oliver Wyman analysis

Accessories (bags, shoes, and eyewear) are the most likely luxury goods to be purchased online, as the category enjoys freedom from fit concerns, with e-commerce capturing a 15 percent share of sales and growing at an 11 percent per year average annualized pace between 2012 and 2017. On the other hand, timepieces and jewelry have seen less success in e-commerce channels, with market penetration only reaching 5 percent, as consumers prefer to purchase these higher-priced items through other channels. Some categories previously considered unsuitable for online retail are expected to improve their penetration, as pure online players with innovative retail concepts enter the space. Beauty Pie, which sells luxury beauty products at factory prices through a subscription-based service, is one example of a new, innovative online player.

Geography has played a role. Disparities in penetration rates can also be observed among different geographic regions, with China leapfrogging the US in 2012 to become the most penetrated global market for luxury retail. Based on 2017 statistics, China, the Americas, and Europe have penetration rates of 20 percent, 13 percent, and 8 percent, respectively. China was initially slow to go online, but e-commerce channels have grown rapidly since the end of 2016 after the growth in mobile phone technology helped expand internet access to more than half the population. Alibaba and Tencent-JD.com dominate China's e-commerce marketplace, and companies like Alipay and WeChat have made mobile payments seamless for consumers. With 95 percent of purchases made through mobile phones, the e-commerce market in China has been able to engage customers through mobile platforms and lower barriers to purchasing online. With China leading the way, we anticipate other regions will catch up and drive the online luxury market growth.

## **FOUR DRIVERS ARE PROJECTED TO POWER THE ANTICIPATED RISE OF LUXURY E-COMMERCE**

### **Increased penetration of internet technology and availability of e-concessions**

Luxury e-commerce has been made simpler and more seamless through increased accessibility of internet technology. Growth in high-speed fixed and mobile networks, together with cybersecurity solutions, has broadened online channel use. Luxury brands can sign e-concessions agreements with online marketplaces and multibrand platforms to benefit from a department store-like online environment.

### **Variety and convenience**

Because there are no shelf constraints online, variety and choice are practically unlimited; plus, the rise of premium delivery and fulfillment services allow for fast shipping, home delivery, and facilitated returns. Attention to packaging and delivery has vastly improved, with “white glove” services delivery and use of fine packaging adding to the appeal of luxury e-commerce.

### **Enhanced customer experience online**

The maturing of internet technology, along with the entry of new pure players and the digital development of luxury brands, has helped revolutionize the online customer experience. The introduction of innovative solutions leveraging artificial intelligence and machine learning, such as predictive algorithms that create profiles of user preferences, enables luxury brands to establish intimacy and create an exceptional and personalized experience for the customer. Mobile apps have enriched this experience by supporting the online channel while complementing offline channels. Additionally, the rising influence of social media sites – such as Facebook, Twitter, and Instagram – is playing a critical role in the evolution of online shopping, especially among younger generations.

### **Consumption shifts**

Internet retail has been considered an arena more suited to low- to mid-priced brands for a long time. Recent evolutions have changed this situation, and consumers are now demonstrating increased willingness to purchase luxury goods from online platforms, especially if authenticity is guaranteed. The luxury consumption shift toward digital is also a generational shift, as Millennials and Generation Z, familiar with digital platforms, will represent a larger share of the addressable luxury market, with increasing earnings over time.

# THE DEVELOPMENT OF PURE E-COMMERCE PLAYERS IS BOOSTING LUXURY E-RETAILING

The rise of online-only platforms, which account for almost 55 percent of online luxury retailing, under various business models, has driven online luxury retail (Exhibit 2). From multibrand e-retailers that buy products from brands to resell, to online marketplaces that provide online platforms to brands without holding inventory, the new e-commerce players have advanced and reshaped the online luxury market. These new players provide consumers with access to a wide selection of brands and products and allow buyers to compare different offerings on a single platform.

Consequently, brands are building partnerships with luxury e-commerce platforms to benefit from the e-commerce upside and complement in-house competencies. For example, **Burberry has partnered with luxury platform Farfetch to expand Burberry’s online sales reach from 44 countries to 150**, including Mexico and Brazil and countries in Southeast Asia. Farfetch offers around-the-clock delivery within two to seven days, free returns, and a pickup service. In 2017, LVMH launched 24 Sèvres, a multibrand e-commerce site. **24 Sèvres features more than 150 labels**, including 20 from LVMH’s own stable, **targeting 75 markets worldwide**.

In Asia, brands can get access to large customer bases and adapt to new purchasing behaviors by joining a network such as Alibaba’s. Burberry and Lancôme have opened Tmall storefronts, which are part of a network of services interconnected by the Alipay integrated payment solution. In October 2018, Richemont announced a strategic partnership with Alibaba to bring the online luxury retail offering of Yoox Net-à-Porter (YNAP) to Chinese customers. Alibaba is to provide technology infrastructure, marketing, payments, and logistics to support the joint venture (JV), while YNAP is to make use of its strong relationship with leading luxury brands.

Exhibit 2: Share of online luxury retailing by types of retailers



Source: Oliver Wyman analysis

# TO BE ON THE WINNING SIDE OF THE E-COMMERCE REVOLUTION, LUXURY BRANDS MUST TACKLE EIGHT CHALLENGES

Along with its opportunities, e-commerce poses challenges that luxury brands must address and cannot afford to overlook, both for their brand equity and market position (Exhibit 3). We have identified eight key challenges, ranging from risk mitigation tactics to strategies for tapping into e-commerce growth.

Exhibit 3: Eight challenges for luxury brands



Source: Oliver Wyman analysis

## DEFEAT COUNTERFEIT AND PREVENT BAD EXPOSURE

Already subject to counterfeit items and reselling, luxury brands need to be even more vigilant to prevent criminal behavior through e-commerce channels that could contribute to the proliferation of fake products and unlawful reselling.

Online sales through third-party online platforms have been a thorn in the side of many luxury brands. Chanel recently won a multimillion-dollar trademark infringement lawsuit against more than 25 Amazon sellers peddling branded knock-off goods (such as fragrances and handbags) on the e-commerce platform.

Careful control over e-commerce channels applies not only to counterfeit detection but also more generally to any product misrepresentation likely to hurt brand equity. Luxury brands need to select the right e-commerce platforms to fit their needs and maintain close oversight of their distribution network.

In a famous case involving counterfeit goods, Coty discovered that one of its resell partners, Parfümerie Akzente, was selling its products on third-party e-commerce websites without its consent. The case was referred to the European Court of Justice who ruled in favor of Coty, finding that luxury goods companies can prohibit their authorized distributors from selling goods on third-party internet platforms, as:

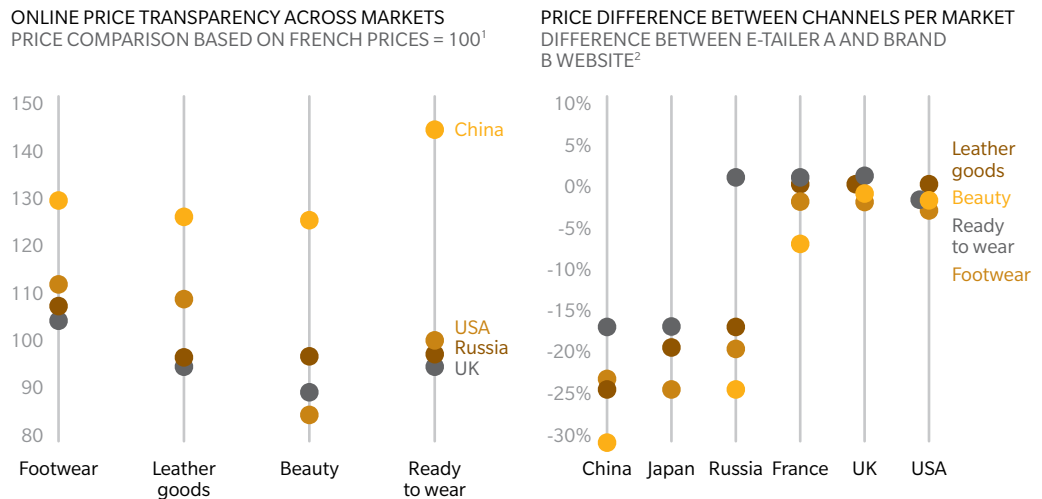
**“The quality of luxury goods is not simply the result of their material characteristics, but also of the allure and prestigious image, which bestows on them an aura of luxury. That aura is an essential aspect of those goods.”**

## DEFEND MARKET SHARE AND AVOID CANNIBALIZATION BY SOLVING THE ONLINE LUXURY PRICING EQUATION

Although price is the primary motivating factor for buying luxury goods online, premium consumers also value fair prices, something that can be easily ascertained, given the high degree of price transparency on online platforms (Exhibit 4). Shipping costs and delays (if there are any) will likely not justify for a consumer a price discrepancy for the same product across multiple channels. Some luxury brands, such as Dior or Cartier, display different assortments to avoid easy comparison: for example, the launch of special online editions like the Panthère de Cartier watch, which has just extended its exclusive partnership distribution with Yoox Net-à-Porter Group, or products/categories available only in stores, like the Dior Ready-to-Wear offer.

Managing economics and profitability across online platforms has become a real challenge for luxury brands and is becoming more complex when coping with multiple geographies. A strong online pricing strategy is key to being successful in e-commerce.

### Exhibit 4: Significant price differences between regions and channels are visible online



1) Data scraped from Luxury Brand B country websites as of May 18, 2018

2) Data scraped from E-tailer A and Luxury Brand B websites as of May 18, 2018

Source: Oliver Wyman analysis

## ATTRACT NEW CUSTOMERS AND DEVELOP CROSS-SELLING

Building holistic customer intelligence to improve intimacy is a powerful way to attract new customers and develop cross-selling opportunities. For luxury brands to better know their customers and create unique customer experiences and offers, brands need to gather enough relevant consumer data across various sources and then exploit them by creating consistent links and harnessing the power of analytics (Exhibit 5). Burberry uses big data and artificial intelligence (AI) to drive sales. Using its customer 360 program, Burberry collects voluntarily shared data through loyalty and rewards programs, customer purchase history, and social media activity to offer personalized product recommendations online and in-store. Diane von Furstenberg, which adopted Qubit Aura, an AI-powered product recommender based on user behavior, attributes 11 percent of revenue being driven by personalization.

Exhibit 5: Examples of data sources and information that brands can leverage



Source: Oliver Wyman analysis

## LEVERAGE SOCIAL MEDIA

Nowadays, a significant share of purchases are influenced by consumers' digital experience, and most online customers turn to social media for help with buying decisions; the luxury goods industry is no exception to the growing influence of social media on online purchasing. Some luxury brands are keenly aware of the power of social media and have made significant investments: Burberry, for example, dedicates at least 60 percent of its marketing budget to digital media. Luxury brands are using influencers to promote their products, with significant impact being seen in China, thanks to "key opinion leaders." Watchmaker Jaeger-LeCoultre's brand awareness more than doubled after its campaign featuring the internet celebrity Papi Jiang was posted on its Weibo and WeChat accounts. However, leveraging social momentum to drive social awareness and sales requires companies to target the platform that will generate the highest returns on investment in terms of engagement and broadened brand exposure, without losing sight of the other types of platforms where competitors could become predominant. And recent misadventures from Prada show that social media is a dangerous space for luxury brands.

## DELIVER THE ULTIMATE EXPERIENCE

The key to delivering a great customer experience is to combine physical footprint with a well-executed online strategy to provide a premium omnichannel experience. This means mastering five must-haves that are essential to transposing the luxury brand universe onto the online world:

- 1. Offer user-friendly navigation.**
- 2. Display functional product pages.**
- 3. Ensure a flawless payment experience.**
- 4. Personalize the experience** a notch above the rest in terms of both technology and know-how – from personalized content based on client preferences and latest research/ activity or access, to premium services for high-value customers.
- 5. Transport and inspire consumers** with editorial content and storytelling that elicits an emotional response, providing customers with the images, fashion events, and gift ideas to inspire them.

Beyond online must-haves, the luxury experience should integrate both offline and online channels in a complementary way. New technologies are contributing toward revolutionizing the “phygital” experience, and many luxury brands have begun to take advantage of them. Fred House reinforces the in-store experience through digital with its initiative L’Atelier FRED. In its Parisian flagship store, the jewelry house invites its customers to design a completely personalized version of its emblematic Force 10 bracelets among the multitude of combinations, using a case composed of a screen and a table. The “phygital” experience goes further, with a smartphone app to capture the specific color of an object or photo and to use it for the bracelet.

Dior’s virtual reality runway-show headset and Selfridges’s augmented-reality concept stores bring unique and interactive customer experience to their stores. Farfetch’s Augmented Retail program encompasses several technological changes, such as customer recognition, an RFID-enabled clothing rack, a mobile payment experience, and a data-collection platform to connect information and services. Chanel signed a strategic partnership with Farfetch (where the luxury brand has taken a minority stake) and plans to use the platform’s know-how to work on digital innovations linked to customer services.

Running an online channel also means luxury brands must be able to offer reliable delivery services that ensure consistently high-end packaging and customer care. In June 2017, JD.com launched a new premium logistic “white gloves” service, where couriers in suits and white gloves deliver packages in electric cars as opposed to scooters. Through this new offering, JD.com aligns its service with its luxury standards to offer a consistent customer experience and compete against other well-positioned players such as Tmall.



# DEFINE THE RIGHT E-COMMERCE MODEL FOR YOUR LUXURY BRAND

The online luxury goods market is finally taking off, with competition accelerating and complexity intensifying. Luxury brands need to define a clear digital strategy and make the right decisions to benefit from growth opportunities and to protect their market share and brand equity. Beyond simply taking the online ecosystem and environment into consideration, digital strategy involves the much broader and greater “phygital” consumer experience: the immersive and visionary experience that the luxury brand is best capable of providing. Brands will have to skillfully reconcile offline and online channels to revolutionize not just e-commerce but the physical store experience as well, which will remain the main ambassador for luxury brands.

Most luxury brands have started to explore e-commerce and are testing different approaches, trying to find the right model. To determine the right e-commerce model, luxury brands need to start with three sets of questions:

## **1. Definition of market needs**

- What are your local customers’ motivations to buy online?
- What is the current online market offer per geography? What is the competitive landscape?
- In each market, what are your customers’ preferences in terms of choice and services?

## **2. Definition of platform(s)**

- Is your brand awareness strong enough to generate traffic through your own e-commerce site?
- What degree of control do you wish to maintain of your brand expression?
- What go-to-market paths should you combine?
- What partners do you believe can provide the right trade conditions?

## **3. Definition of operations**

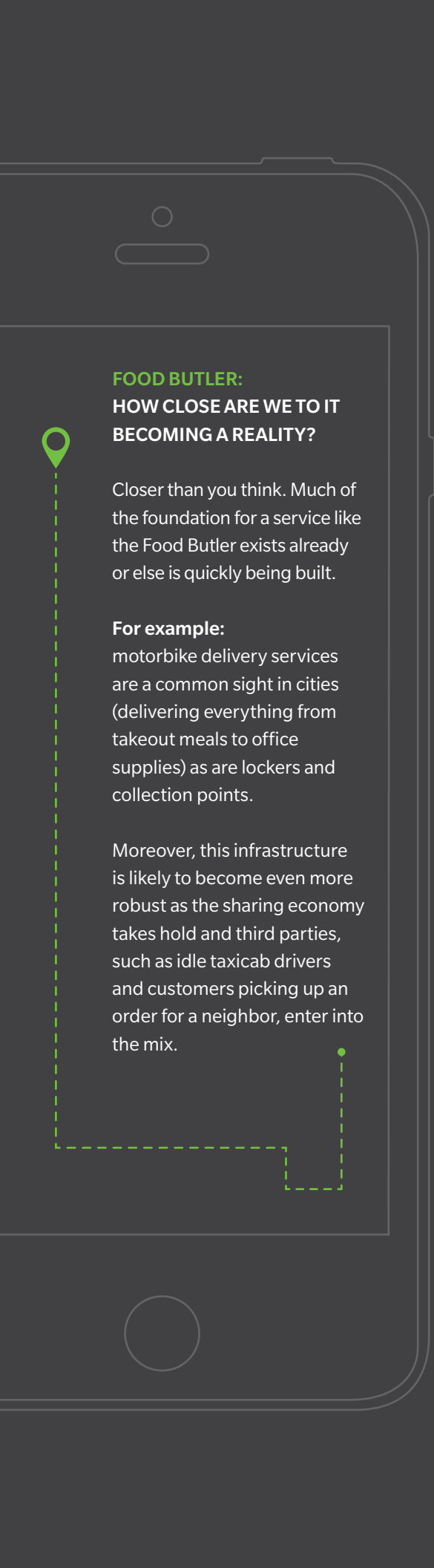
- Do you have the relevant scale to manage operations internally?
- What core activities should be kept in-house to ensure quality?
- Is there any advantage in leveraging e-commerce players’ scale and expertise?





# REVOLUTION IN THE AISLES

HOW THE GROCERY STORE  
OF THE FUTURE WILL FOREVER CHANGE  
THE WAY WE SHOP FOR FOOD



**FOOD BUTLER:  
HOW CLOSE ARE WE TO IT  
BECOMING A REALITY?**

Closer than you think. Much of the foundation for a service like the Food Butler exists already or else is quickly being built.

**For example:**

motorbike delivery services are a common sight in cities (delivering everything from takeout meals to office supplies) as are lockers and collection points.

Moreover, this infrastructure is likely to become even more robust as the sharing economy takes hold and third parties, such as idle taxicab drivers and customers picking up an order for a neighbor, enter into the mix.

The year is 2028 and Helen Martinez doesn't shop the way her parents did. Like them, she buys almost all her food and household items from The Fictional Food Store – but unlike them, she no longer needs to go to a store. Instead, she signs up for regular deliveries with the supermarket's Food Butler app. This offers shoppers maximum control with minimum hassle. Parameters include the degrees to which a food basket is healthy, adventurous, or inexpensive. Ms. Martinez has indicated that her family consists of two adults and two children – one of whom is allergic to gluten. Food Butler then auto-populates her shopping lists, plans her family meals, and figures out the lowest-cost delivery options. "I don't have to think about menus and meals," she says. "Fictional Foods sends them to me."

Fictional Food's attraction to shoppers like Ms. Martinez explains why it has become a grocery success story. The company has just grabbed a 20 percent share of the US and European grocery markets, cementing its position as one of the five big grocers outside China. But two decades ago, digital technology and the rise of online shopping threatened to put traditional supermarkets like Fictional Foods out of business.

What made the difference? Unlike other traditional grocers, Fictional Foods embraced a new information era for groceries as it witnessed the rise of Amazon in the sector. It focused on technologies that would help it to pull ahead of old rivals. It also made the most of its customer relationships, enabling it to compete with digital natives even when nearly half of food is delivered to people's homes. Some sign up for regular deliveries, taking advantage of discounts available for a subscription service. Others outsource the complexity of planning, as Ms. Martinez does, by setting parameters. "On the surface, Fictional Foods is a grocery business," said Dave Shultz, global head of retail at Corporate Bank. "But look under the hood, and you see that it is actually an information business."

## THE MCDONNELL REVOLUTION

In 2018, Fictional Foods was a traditional store-based grocer under attack with operations in Germany, the Netherlands, and parts of the US. One threat came from discount supermarkets. But the greater menace was online food shopping, which prompted forecasts of the slow death of supermarkets and their replacement by the giants of e-commerce. Amazon had become serious about food with its purchase of Whole Foods Market and, soon after, it became – after Apple – the world’s second trillion-dollar company in terms of market value.

That year, Jason McDonnell took over as Fictional Foods CEO and started a revolution. On Monday, October 8, staff arrived at the company’s head office and found three-quarters of their desks had been removed – to illustrate how much less central support digital retailers were operating with. Hundreds of products were dotted around the office with 30 percent price reduction stickers – to indicate the kind of prices Fictional Foods needed to offer. And each manager was given an iPad with a mock-up of the first version of the Food Butler app – to indicate where the future lay.

To cut costs in stores, Fictional Foods first reduced staff numbers at checkouts by allowing customers to scan items, either at the exit or while shopping. Ordering and warehouse operations were automated. And the center of each store, which traditionally consisted of stacks of packaged food and household products, was converted into an array of icons and barcodes, so that shoppers could simply click for home delivery or to have their purchases waiting at the exit. Fictional Foods also consolidated its suppliers to a handful with which it had deep relationships. This enabled it both to reduce costs through long-term contracts and to develop new products jointly. Within a few years, Fictional Foods had cut its retail prices by an average of about 10 percent.

The company quickly grasped why online grocery shopping would not be an automatic success and why it would be challenging to square with traditional supermarkets. Many food products need to be kept at specific temperatures and delivered fast, but home delivery can be prohibitively expensive outside densely populated cities. Fictional Foods developed a system to cater efficiently to customers with different profiles in different locations – as well as for the same customers at different times when they have different needs.

Regional fulfillment centers serviced larger home-delivery orders and those containing specialty items unavailable in most physical stores. Smaller baskets and click-and-collect orders were serviced by stores. Options included: delivery within an hour by motorbike; lockers and collection points; and mobile vans touring neighborhoods that customers can locate on Food Butler and place an order with. Fictional Foods also started to use third parties, from taxis to customers picking up an order for a neighbor. “When online grocery shopping first went mainstream, it wasn’t that convenient,” says Caroline Smith, grocery expert at the consumer organization, Consumer Watchers. “Fictional Foods has managed to set up a system that can serve regular planned deliveries but also short-term unplanned needs. This was a major unlock.”

## FOOD AS AN INFORMATION BUSINESS

In 2025, Fictional Foods accelerated the use of information in its operations in order to understand its customers' behavior better: where they will be when, and what they are likely to want to buy. Predicting these behaviors helps satisfy customers more efficiently and offer products and services at lower prices. Fictional Foods even let customers vote through Food Butler for less-common products to be added to their local outlet. Fictional Foods began to use big data analytics to predict the characteristics of new products that consumers would purchase if they existed.

The model depended on the ability to leverage vast quantities of customer data – which in turn depended on the availability of such data. In 2021, Fictional Foods started to buy up other retailers, including one grocer dominant in most European countries and in most regions of the US. Often it acquired the number two player in a market: Battered by e-commerce competition, these were cheap in the early 2020s. Fictional Foods then introduced its products, digital operating practices, and low prices. Most importantly, it integrated the acquired businesses into its system of stores and fulfillment centers. This system was set up for each region based on customer characteristics, population density, and competitor profiles. In many cases, these also-rans turned into regional market leaders. “Fictional Foods worked out that their huge amounts of customer data were one of the few advantages they had over us in the late teens and early twenties,” said one retired Amazon executive. “We were watching and trying to keep up.”

The company's innovation leader service offers suppliers insights into global consumer purchasing habits, enabling these suppliers to optimize their product offerings for different countries and consumer segments. In return, Fictional Foods gets better terms from the big brands, as well as innovative new products and promotions to pass on to consumers. In Germany, Fictional Foods is testing a service that lets customers commit to products over long periods, enabling manufacturers and farmers to plan further ahead. One project is the world's largest organic chicken farm, underwritten by three-year customer subscriptions. “We find that empowering customers can unlock great new ways to do things,” said Ms. Huygens.

In the industry, Fictional Foods has become known for the flow of information and suggestions between customers, suppliers, and fulfillment services. A customer chooses a health rating on Food Butler so that it can recommend appropriate food, while also taking into account the customer's recent orders and ratings of previous meals. Suggestions and discount offers are relayed via Food Butler so that customers will go to the branch where the product range best matches their preferences.

When a delivery comes to a neighborhood, customers there are invited to make an order and are offered a discount. Large subscription-based orders earn significant price cuts when they are coordinated with neighbors' orders. Some customers scan products at home as they use them: Fictional Foods then calculates when they might be ready to replenish their fridge and

suggests a delivery for a time when the customer is likely to be home. Fictional Foods thus influences customer behavior to achieve a transparent, intelligent supply chain that makes fulfillment more efficient and less costly, and this magic lifts the economics of the whole business. “We have signed up for four new meal suggestions a week, which are deliberately adventurous,” said Jens Stoltz, who lives in Munich with wife Tanja and their two children. “The prompts then provide us with extra surprises.”

Earlier this year, Fictional Foods took its use of IT to a higher level with the launch of its Premonition forecasting system. Traditionally, retailers forecast the demand for products in each store and then place orders with suppliers and send the products to the right stores. Premonition forecasts what an individual customer might want, even if they are not yet aware of it themselves. If a customer is walking down a road near a mobile delivery unit, Premonition can suggest a recipe kit to buy and take home based on past choices – even if the customer had not actually been thinking of what to buy for dinner. “It can even help customers eat better by preemptively suggesting a healthy dessert when it knows a customer is at risk of ordering a quart of ice cream,” says Kimberly Robinson, the mathematician behind the system. “Premonition probably knows more about customers than they do themselves.”

On her Food Butler, Ms. Martinez has set her cost-consciousness level at nine out of 10 and both cooking time and healthiness at six, while she chooses a seven for how experimental she wants her meals. She gets discounts on regular subscription items and also from coordinating delivery slots with her neighbors. “All this saving means I can let Food Butler book me and my husband a dinner every month at a local restaurant,” she said. “It surprises me with a different selection each time.”

But the biggest surprise of all has been the fact that Fictional Foods, once a hidebound traditional supermarket, is at the head of the pack in redefining groceries. That’s because McDonnell was one of the few CEOs who recognized that the innovations implemented by Amazon after its purchase of Whole Foods in 2017 just scratched the surface of digital grocery shopping.

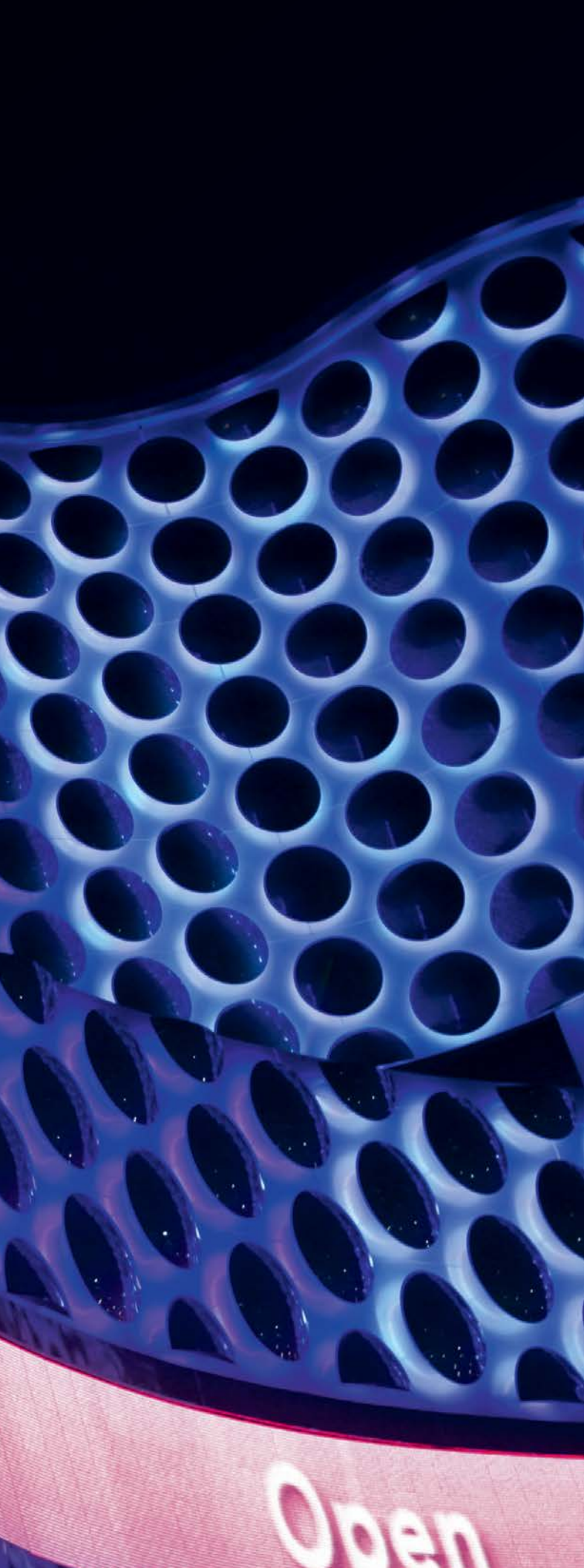
Ten years ago, that was not an obvious direction for the industry. Concerns over privacy and misuse of data were generating a public backlash against the gathering of individuals’ data by big corporations. This led to pressure for privacy regulations that might have derailed parts of Fictional Foods’s current business model.

But McDonnell saw that many aspects of IT – such as supplier management and warehouse and store operations – would still be applicable whatever the public thought of using their data. And in the end, the public was convinced that safeguards on data use would prevent meaningful compromise of their privacy. Most people saw the benefits of letting a grocer get to know them through data.

# FIGHTING FOR THE FUTURE OF THE SUPERMARKET INDUSTRY

Open





Authored by MMC Retail and Wholesale Industry Group

## **RISK, STRATEGY AND PEOPLE – DELIVERING VALUE FOR THE CUSTOMER OF TODAY AND TOMORROW**

The battle for the food dollar spend of today's consumer has never been more challenging. Doomsday predictions abound regarding traditional supermarkets' ability to survive the competitive threats posed by online retailers, at-your-door delivery from restaurants, prepared food offerings from convenience stores, and the appeal of meal-kit companies. The online and brick-and-mortar worlds are each seeking to find the right balance between the two to satisfy a consumer palate that is more diverse and demanding than ever. Surviving and thriving means delivering the right combination of value, convenience, choice and a compelling experience that creates and sustains repeat customers. A successful supermarket CEO will need to effectively and holistically solve for a multitude of risk, strategy, and people challenges.



## **DIGITIZATION AND AUTOMATION WILL FUNDAMENTALLY SHIFT THE LABOR AND STAFFING MODEL FOR SUPERMARKETS**

When shopping for food, customers globally are seeking an array of on-trend products they can purchase through a variety of channels and experiences – from rich immersion and advice to online to grab-and-go. Shoppers are also more adventuresome than ever before in selecting brands, giving a boost to private brands and diminishing the demand for nationally recognized products. These changing needs and wants exceed the limits of what can be found in a traditional supermarket and, as a result, supermarkets and other grocery retailers are rapidly changing to keep up with their customers.

The changes in product assortment and the need to deliver the new consumer experience will also cause food retailers to change their labor model profoundly. Labor is a high fixed cost for supermarkets and carries annual wage and benefit increases. However, technology will provide ways to cut costs, operate better and smarter, and eliminate certain tasks entirely. For example, forecasting errors will be reduced by machine-learning algorithms, making stock management easier. Center store products will be bought online or from virtual shelves. Smarter tools and automation will massively reduce back-office work. Streamlining and digitization mean managers won't have to work through long paper lists and daily reports. The new checkout experience will also minimize hassles such as cash management.

Repeat product purchases will be delivered to customers efficiently via personalized online orders supported by either delivery or curbside pick-up. As such, supermarkets will rely less on labor for stocking, display, and checkout activities. In a complete rethink of the store layout, the backroom will house the center store assortment and serve as a picking area. Some online orders will be picked here for home delivery or in-store pickup. The checkout line will be eliminated, replaced by one-click payment, scan-and-go systems, and/or self-checkout terminals. As a result, we predict that the utilization of manual labor will drop by approximately 40 percent over the next five years.<sup>1</sup>

## **SUCCESSFUL SUPERMARKETS MUST ENHANCE AND CUSTOMIZE THE CUSTOMER EXPERIENCE IN PHYSICAL STORES**

Food retailers have a unique opportunity to respond to changing consumer trends to acquire and retain customers, but these changes also carry a significant amount of risk for incumbent supermarkets. How do they fund all of the required changes? How fast can they embrace these changes? At what pace will their customers give them credit for responding to their needs? How do they win against their traditional players while also staying competitive against new entrants such as Amazon/Whole Foods, hard discounters such as Aldi and Lidl, specialists like Trader Joe's, clubs such as Costco, and mass merchants such as Walmart?

1) MMC RWIG Supermarket Task Force

Customers will vote with their feet and wallets to reward the retailers who best deliver on their wide range of needs and wants. Successful supermarket operators are reconfiguring their stores to attract and retain customers. Recognizing that customers are demanding “new” (expressed as “authentic,” “local,” “sense of purpose,” “good for me,” “country of origin,” or “good for the planet”) and have high expectations for a great experience, retailers must consider which of the following strategies to pursue:

- Deliver seamless online/in-store experiences
- Allocate space for sit-down meals
- Source products from local vendors
- Create/feature more private label lines
- Personalize offers and prices

... YOU BETTER START  
SWIMMIN' OR YOU'LL  
SINK LIKE A STONE,  
FOR THE TIMES THEY  
ARE A-CHANGIN'



## HOW CAN FOOD RETAILERS GET AHEAD IN THE RACE FOR THE CUSTOMER?

In 1963, Bob Dylan penned lyrics that should be reverberating within the board rooms of every food retailer today, “Then you better start swimmin’ or you’ll sink like a stone, for the times they are a-changin’.” Although evocative, the lyrics prescribe neither the direction in which to swim nor the pace.

Here are five suggestions:

- **Understand why customers** are demanding healthier foods to provide far greater insights into how to curate a private label offering rather than relying on traditional consumer research.
- Be willing to take **more risks – and be able to intelligently manage them.**
- Find ways to increase your **decision-making speed.** Faster decisions combined with more experimentation will increase the yield when taking risks.
- Employ **fewer but higher-performing people** on your staff. Grocery retail is becoming a sophisticated sport – your team members need to be able to compete.
- **Lower costs**, not only for traditional reasons but mostly to fund the investments you will need so you can carry out the above four exercises.



## DEVELOP A COMPELLING EMPLOYEE EXPERIENCE ALIGNED TO YOUR CUSTOMER

When an employee enjoys being at work, it is demonstrated in their engagement and contributes to their performance, which in turn increases store revenue and lowers in-store labor costs. The challenge is creating an employee experience that matches the customer experience. How can supermarkets elevate their employee experience?

NEARLY 80 PERCENT OF ALL AMERICAN EMPLOYEES ARE CATEGORIZED AS LIVING PAYCHECK TO PAYCHECK

**Talent.** With the new digital era comes a new breed of jobs. Rather than manage only the internal workforce, the best companies will establish and manage an extensive talent ecosystem. Workforce analytics help optimize needed labor maps and transition issues, moving from the current state to the desired, future state.

**Skill dynamics.** Given the speed of innovation, companies need to target talent not only with the specific technical skills required but also with data analytics. Consumercentric competencies must be identified and then acquired or developed.

**Competitive pay.** In these times of fewer roles and static pay, new compensation platforms will be needed to engage, retain, and reward staff for the right skills and behaviors, including increased focus on retaining those employees with customer-facing roles.

**Career pathing.** Tomorrow's jobs do not exist today. The introduction of digital technology means that many supermarkets are eliminating roles. Career maps must be adapted to respond to leaner and flatter organizational structures.

**Choice.** Like the customer purchasing online and in-store, employees appreciate additional choices with their benefit options. Nearly 80 percent of all American employees are categorized as living paycheck to paycheck, with limited savings.<sup>2</sup> When faced with unforeseen expenses, which are typically tied to medical or health issues, many will look to loans, such as from a savings plan (401k) or other means to access needed capital to help with unexpected expenses.

Developing and implementing a workforce rewards strategy to elevate the employee experience will produce team members who can compete in the new grocery retail environment, ensuring their supermarket can succeed.

## THE OPTIMAL DEPLOYMENT OF CAPITAL TO INTELLIGENTLY MANAGE AND FINANCE RISK IS CRITICAL IN THIS NEW WORLD

Margins are tight and more pressured than ever in this fight for the consumer's food dollar. Pennies matter. Successful supermarket operators will utilize fact-based decision-support tools and analytics to understand their risk-bearing capacity and allocate capital – through risk retention, risk mitigation, and risk transfer – to optimize their spend and protect their balance sheet.

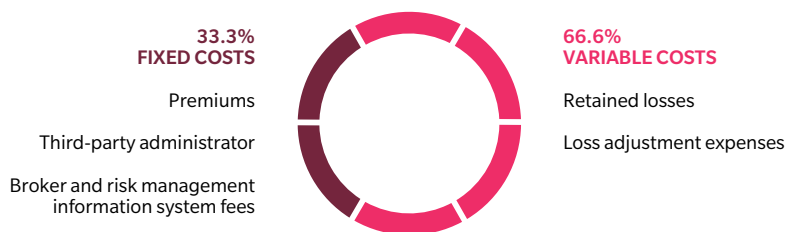
2) CareerBuilder survey, 2018

Employee and customer injuries (i.e. variable costs) are the largest component of a supermarket's total cost of risk (TCOR). Grocers who identify loss drivers, develop strategies to reduce and manage claims, and execute their strategy in a consistent, disciplined manner have a tremendous ability to positively impact their selling, general, and administrative expenses (SG&A) line. As both supply chain and consumer platforms rely more heavily on technology and e-commerce, the threat of system interruption (by malware, ransomware) and theft of confidential information (customer, employee, pharmacy) become greater and potentially more devastating to both financial results and your brand.

Consumer demand for locally sourced and prepared foods creates additional liabilities from a product contamination and foodborne illness standpoint. How supermarkets respond before the event (recall procedures, indemnification agreements with suppliers) and after (customer and regulatory authority interface, crisis response) will shape how your company is viewed by the community.

Supermarkets must determine the best approach to meet growing consumer demand for home delivery and BOPUS (buy online, pick up in-store) availability. Companies who undertake delivery on their own expose themselves to increased and previously unknown liabilities. Those who utilize third-party providers need to pay careful attention to the indemnification and insurance provisions of their contracts with these providers.

### Supermarket total cost of risk (TCOR)



## THE RISKS AND CHALLENGES DEMAND A KNOWLEDGEABLE, EXPERIENCED BUSINESS PARTNER

The disruptive, hyper-competitive nature of today's food retailing environment requires innovative solutions from a partner with unparalleled industry experience, deep resources, and analytical decision-support tools. The Marsh & McLennan Companies are the partner of choice for more than half of the Supermarket News Top 75 Retailers & Wholesalers, assisting them with their human capital, risk, financial, operation strategy, and brand reputation challenges. We deliver executable strategies designed to reduce costs, improve operational performance, minimize volatility, grow top line revenue, and protect the balance sheet.



# TAKING FRESH TO THE NEXT LEVEL

Oliver Wyman's latest survey of more than 17,000 consumers in 14 different countries shows that "Fresh is key." Fresh is an important card that grocers can play to attract high-value customers and to differentiate themselves from other players – even more so from online competitors.

For this reason, taking the fresh food departments – from bread to meat to fruit – to a higher level is essential. Quality is no longer enough to enable retailers to stand out. To face this challenge, they need a more personal and emotional approach as well as new tools.

Exercising greater control over the supply chain is imperative. To become Fresh Champions, retailers need to excel in every element of the fresh value chain, guaranteeing high standards "from farm to fork."

## FRESH IS KEY ...


... for traditional retailers to attract high-value customers, differentiate themselves from other players, and win against online competitors.


**Fresh Products Guide The Choice of The Main Store** – For 59 percent of the consumers interviewed, the quality of fresh products (which include meat and cold cuts, fish, fruit and vegetables, bakery, cheese, and ready meals) is the most important criterion for selecting their main grocery store. As many as 70 percent of consumers continue to return regularly to the store they consider best for this category of products. At the same time, stores that fail to offer high-quality products risk losing their customers: 53 percent of all shoppers are willing to change stores if they are not satisfied with the offer of fresh products.


**Better Fresh Leads to More Traffic and Larger Baskets** – Satisfied shoppers of fresh products visit the store 7 percent more than dissatisfied customers and spend 24 percent more. Furthermore, excellence in fresh products also supports sales in other categories: On average, an increase of 1 euro in fresh spending can lead to an increase of 1.47 euros in total sales.

**Fresh Is A Crucial Element of Differentiation** – 32 percent of respondents perceive a significant difference in the quality of fresh products among the various chains. For non-fresh products, this percentage drops significantly to 20 percent. This depends on the market: While only 19 percent of Dutch customers and 22 percent of UK customers perceive differences in the quality of fresh products among retailers, the number more than doubles for Russia (54 percent).

### CUSTOMER SURVEY RESULTS

 **70%** mainly shop at the store they consider as "best place for fresh"

 **24%** bigger baskets from customers satisfied with fresh

 **7%** more frequency from customers satisfied with fresh

### IMPORTANCE OF PRODUCT CATEGORIES FOR FRESH SATISFACTION<sup>1</sup>

 **28%** Fruit and vegetables

 **20%** Meat and cold cuts

 **13%** Cheese

 **13%** Convenience food (fresh only)

 **10%** Bread and pastries

 **7%** Fish

<sup>1</sup>) Correlation, category satisfaction vs. fresh satisfaction

### Quality Is Not The Only Element That

**Matters** – The fact that customers may struggle to perceive differences in fresh food quality among retailers does not mean that quality no longer matters. On the contrary, it is still by far the most important factor defining customer satisfaction (see graphic); it has simply become the norm, especially when it comes to the visual appearance of products. A common misconception is that quality is defined by looks for fruit and vegetables and by expiry date for meat. While this is not completely wrong, our survey highlights the importance of taste: It is already the main factor determining quality for meat and bread and is becoming more and more significant for fruit and vegetables (as the graphic shows). Retailers should ask themselves what they are doing for customers to experience superior taste both in the store and at home.

### Retailers Can Impress With An Assortment

**Tailored to Their Customers** – Globally we see assortment becoming an increasingly important driver of customer satisfaction. Customers focus on different elements depending on geography. For example, consumers in German-speaking countries care more about local than seasonal assortment, and vice versa in English-speaking countries. The importance of categories also varies between countries. Additionally, preferences depend on the demographic in each store's immediate vicinity. Retailers will have to make sure they understand what customers want in each of their stores and adapt the assortment to their individual needs, while trying to ensure as much exclusivity as possible.

QUALITY



ASSORTMENT



## WHAT DETERMINES CUSTOMER SATISFACTION WITH

... FRUIT / VEGETABLES



... MEAT / COLD CUTS



QUALITY

35%

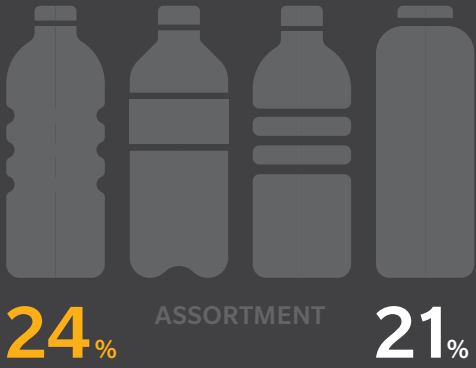
32%\_Appearance

29%\_Taste

17%\_Size and shape

THESE COUNTRIES HAVE DIFFERENT PRIORITIES FOR FRUIT AND VEGETABLES





31%

- 32%\_Taste
- 29%\_Appearance
- 17%\_Product specification

THESE COUNTRIES HAVE DIFFERENT PRIORITIES FOR MEAT AND COLD CUTS



QUALITY

ASSORTMENT

**Customers Seek an Emotional Connection –**

We can observe a much stronger correlation between satisfaction and product presentation in North America (over 20 percent) than in Europe (around 10 percent), especially in the fruit and vegetable category. Leading US retailers are aware of this and use theatrical presentations to connect emotionally with their consumers. We expect this to become an area of focus for European retailers (with a more cost efficient approach) too, in the future.

But the most important element in connecting with shoppers is human interaction. Under tight cost pressure, retailers struggle to give their employees enough time to interact with customers. In particular, service counters can make a huge difference. They create the atmosphere of a specialty store and make shopping a pleasant experience.

**Leverage Technologies –**

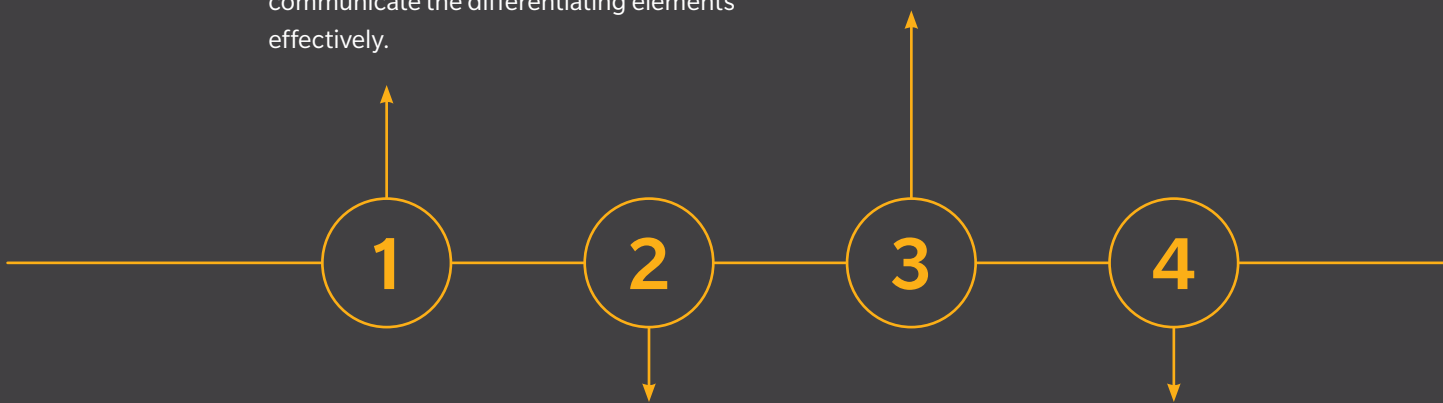
New technologies provide retailers with many opportunities to strengthen their offer to customers while keeping complexity and cost under control. For example, a state-of-the-art ordering system that uses machine-learning technology and provides intuitive tools will secure better availability and reduce waste, while allowing employees to spend more time with shoppers. Another example is a modern assortment tool that creates individual planograms for stores, containing all the favorite products of each store’s local customers while limiting the assortment to a minimum that avoids waste and ensures freshness.

# KEY SUCCESS FACTORS FOR A FARM-TO-FORK TRANSFORMATION

**Maximum product quality (and effective communication)** – Expand the range of certified products; offer products with the highest standards; control and guarantee the quality of the products along the entire supply chain with processes and systems; communicate the differentiating elements effectively.

**Best freshness available at any time –**

Implement advanced forecasting methodologies and intuitive tools for ordering and production planning, for reducing lead time (from producer to shelf), and for selecting pack sizes that guarantee product freshness.



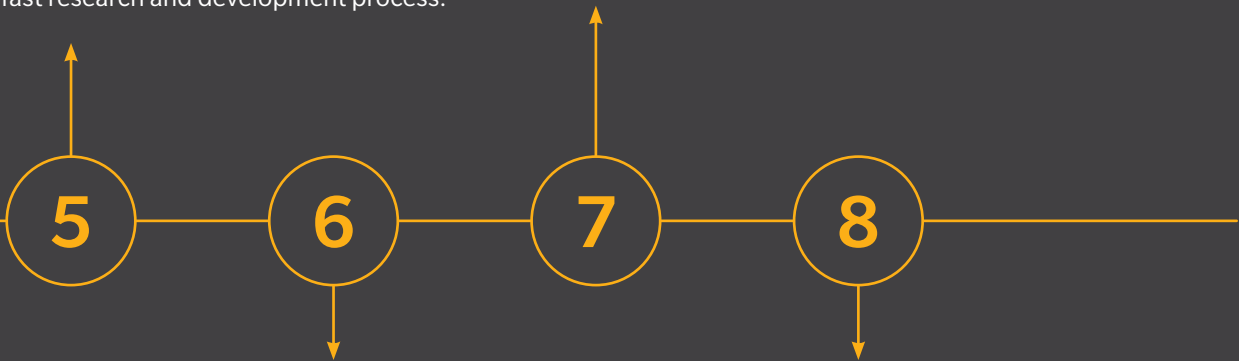
**Assortment definition based on local needs** – Adapt the assortment to specific local needs, including seasonal products from local producers; allocate space and choose volumes for each product based on demand.

**Excellent presentation and counter service –**

Adapt counters and the gastronomy offer to the growing demand for a differentiating shopping experience, while also improving customer service with in-house initiatives (tastings, cooking classes, and so on) and other resources (such as catering); leverage a customer-oriented sales force.

**Product and service innovation as a differentiating element** – Establish a culture of continuous innovation together with a rigorous culture of quality and customer centrality; adapt the assortment according to customers' changing needs (for example, by offering ready meals); structure an efficient and fast research and development process.

**Optimization of in-store activities** – Have plans in place for staffing and product replenishment depending on customer frequency, ideally leveraging intuitive tools for managers and associates; define indicators to monitor sales performance; identify the best practices to apply to other stores.



**Integrated supply chain management and verticalization** – Integrate the supply chain, with transparency on inventories and quality, and cooperate with suppliers (through data sharing, partnerships, verticalization, and so on); the supply chain should ensure traceability and quality standards, and enable access to scarce resources and exclusive products (such as organic and artisan produce, and regional specialties).

**Invest in attracting the best talent** – Define a strategy that is effective in attracting and recruiting people with the appropriate skills; invest in initial and periodic training and in incentive schemes for retaining talent.

In summary, our experience suggests that a significant step forward in the fresh food category cannot be achieved simply by partially optimizing some key functions (such as purchasing or the supply chain). It requires a holistic approach – from farm to fork – in which the entire system focuses on ensuring maximum customer satisfaction and on driving gains in the short and long term. Starting this transformation requires resources and perseverance but it pays off: Fresh Champions achieve more traffic and larger baskets, and stand out in the market as top players. They manage to retain customers and create a positive halo effect, strengthening their brand. This is how Fresh Champions can protect and increase their market share.

# AI: NOT JUST FOR ONLINE STORES

TRADITIONAL STORES CAN BOOST MARGINS  
BY UP TO 10 PERCENTAGE POINTS





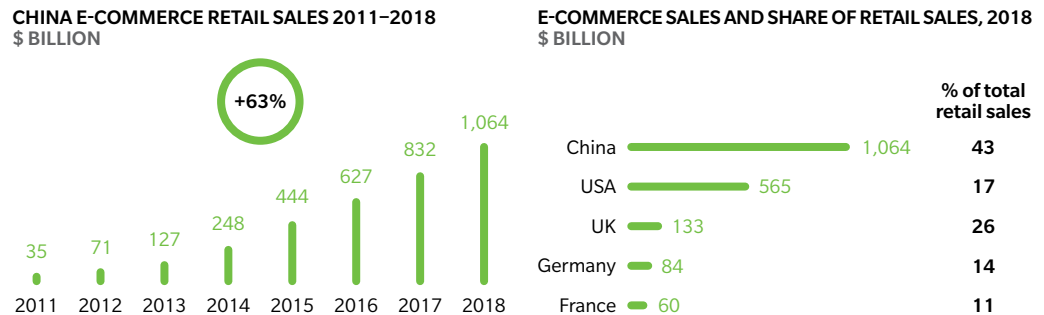
# FIGHTING BACK WITH ARTIFICIAL INTELLIGENCE

The visible difference between online and traditional retail is the presence or lack of a physical store. The more-significant divide could be online retailers’ massive accumulation and use of data.

When someone buys a T-shirt in a physical store, the retailer simply records the item, its price, the date and time of the purchase, and how the customer paid. When someone buys the same T-shirt online, the retailer will know all of the above and... the purchaser’s name, email, billing address, even the neighborhood where he or she lives. The online retailer will also know and record the purchaser’s size, product preferences, and items rejected during the search that led to a final choice. In addition, the retailer may also learn what other products are commonly bought at the same time, and may even get the buyer’s social media profile, if this was used to link to the shopping site. If the item was a present, it may also have been possible to gather many of the same details about the recipient.

As retail moves into the artificial intelligence (AI) era, online retailers have a significant head start. Their current processes have allowed them to gather data by default, amassing data gold mines from each component of the online ecosystem. Understanding the value of this information, they have for years been using analytics to optimize processes in all aspects of retail: demand generation, the purchasing decision, payment, and fulfillment. AI in the future will take the use of analytics beyond mere task automation and into realms of decision-making and problem-solving – at first by providing support, and later evolving the ability to perform these tasks automatically. Such capabilities could accelerate further the online erosion of physical retail – a potentially existential threat. Without concerted action by traditional bricks-and-mortar players, the already significant online retail digital advantage will only widen, increasing the pain that high-street retailers have suffered in recent years.

**Exhibit 1: China e-commerce growth**



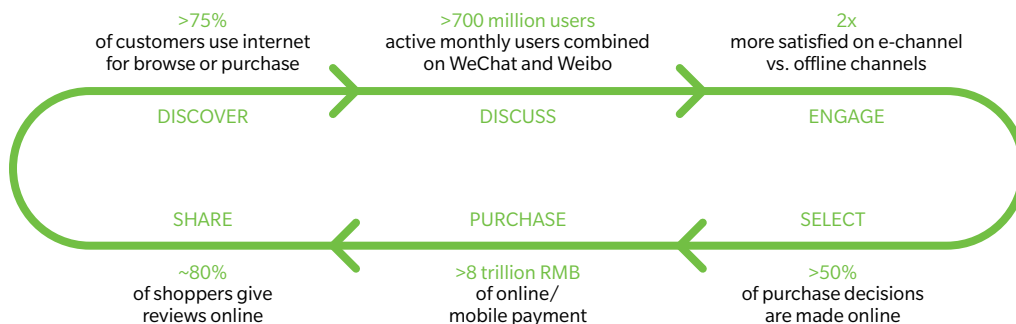
Source: Euromonitor

For a glimpse of the possible consequences, look at China, which has shot to the global forefront of online retail, with e-commerce accounting for over 40 percent of retail sales in 2018 (Exhibit 1). While the equivalent figure for the United Kingdom was 26 percent, online sales were far less significant in other major markets: 17 percent in the United States, 14 percent in Germany, and 11 percent in France.

Linked to this rapid online-driven digitization is the rapid emergence of digital-native retail giants such as Alibaba and JD.com. They have been buying – as well as developing themselves – units to cover every link in the chains of retail activity, including digital payment apps, delivery companies, and social media units to generate demand (Exhibit 2). Most that is most concerning for traditional retailers, the online empires are buying up chains of brick-and-mortar stores, complementing the digital efficiency of their online businesses with physical-store characteristics: Customers can seek advice from store assistants and see products before buying them. As a result, there is a growing sense of urgency among Chinese retail companies about digitization and AI. In a recent survey there, more than three out of four executives said the industry would see “real disruption” from AI in the next five years.

But there is still hope. Our recent experience indicates that physical retail, by aggressively embarking upon ambitious AI programs, can not only meet this threat but also change the game in terms of economics. By doing so, we have seen some physical retailers improve margins by up to 10 percentage points. In operations, the gains come from smarter in-store processes, back-office automation, and better supply chain management. Commercial decisions have been improved through superior management of categories, suppliers, prices, and promotions. If only some of these improvements are made, financial improvement can still be dramatic, especially when seen against a starting point of traditionally razor-thin average net profit margins.

Exhibit 2: Typical online journey of a Chinese consumer



Source: Oliver Wyman analysis

# WHAT CAN AI DO FOR RETAILERS?

In the past, AI was often considered a tool that only technology companies were capable of exploiting. In China, retailers wanting to use AI usually aligned themselves to one of the two retail empires. Now, any company willing to invest may access the benefits of AI, giving them the potential to boost margins significantly.

The most basic AI algorithms can perform repetitive tasks that previously needed human intervention. These include the ability to scan a paper invoice to extract numbers and the items they refer to, and voice assistants' recognition of commands in human voices to perform basic tasks.

A smarter level of AI uses a combination of data and logical reasoning to make informed decisions. AI needs data – unlike a human, who can make decisions based on experience. But, given data, an AI-equipped computer can go far beyond what humans are capable of: It can process greater quantities of data of a larger number of different types and do this much faster. The more data an AI system has, the more remarkable are the tasks it can perform, which is why online retailers are now ahead in their application of AI. But traditional retailers can also mine data assets related to shopping habits, such as those they have gathered from loyalty programs.

Far from being in the realm of science fiction, AI is happening now. We think AI can help retailers both to increase their sales and reduce their costs, boosting margins in operations by up to 4 percentage points, and on the commercial side by up to 6 percentage points (Exhibit 3). However, these figures represent just the basic potential for improvements that are achievable over the coming five years or so. Longer-term possibilities include the creation of personalized experiences for customers, forecasting potential sales of a new product, and robotics to automate physical tasks.

Exhibit 3: Summary of potential margin uplift from AI

OPERATIONAL PROCESSES	In-store automation	+2-3 pp
	Back-office automation	+0.5 pp
	Supply chain management	+1-1.5 pp
COMMERCIAL DECISIONS	Category management	+1.2 pp
	Price and promotion management	+1.5 pp
	Supplier management	+1-4 pp
<b>TOTAL</b>		<b>+7.2-11.7 pp</b>

Source: Oliver Wyman analysis



# OPERATIONAL PROCESSES

AI can replace or support workers in repetitive, low-value tasks such as shelf replenishing, freeing up staff to provide top-quality service: They can operate delicatessens, offer tastings, and answer customer questions, giving the store a human touch that will encourage people to return.

## IN-STORE AUTOMATION

Frontline staff in retail stores are preoccupied with four mundane tasks: replenishment, check-out, repackaging, and store maintenance. AI tools can help at least with the first two of these. Automatic checkout goes beyond the self-checkout systems common in supermarkets, as it recognizes items placed in a basket without the customer or a staff member having to do anything. The simplest systems register when a customer removes items from shelves and then deducts the total from a digital payments system. Some retailers are now rolling out systems based on radio-frequency identification (RFID), which uses electromagnetic fields to automatically identify and track tags attached to objects. More advanced systems register purchases using cameras combined with image-recognition software. The first stage of shelf replenishment is to predict demand. AI tools can run calculations on factors such as weather changes and thus forecast changes in demand and inventory requirements for clothes and beverages in real time. Trends in clothes and makeup products – and the combinations they are bought in – can be anticipated by examining popular Instagram accounts. Predictions will improve over time, as the system learns from its previous attempts at prediction.

+2-3 PP  
MARGIN

The next stage, stacking shelves, can be time-consuming if a staff member must rummage through boxes looking for the right items and figuring out where they fit on a shelf. But AI can instruct a warehouse exactly where to stack boxes in a truck so that they are automatically unloaded in the right order. Human shelf stackers then don't have to search or think so much. Depending on the retailer, in-store automation could contribute between 2 and 3 percentage points to the company's margin by making possible a smaller, tech-enabled frontline workforce.

## BACK-OFFICE AUTOMATION

A number of back-office tasks can be automated using AI-based tools. Invoices can be read by machines and then paid without the need for human action, even when they are on paper and do not conform to any particular format. Early mistakes can be part of a learning process, as the system constantly improves itself. Business performance can then be calculated and updated in real time, rather than just at the end of set periods.

+0.5 PP  
MARGIN

This advanced level of automation will drive a reduction in the headcount of entry-level accountants and other back-office staff, and also enable senior management to react faster to changing business conditions. As back offices at headquarters typically account for around 1 percent of a retailer's costs, there is a high chance that AI can raise the company's margin by 0.5 percentage points.

## SUPPLY CHAIN MANAGEMENT

+1-1.5 PP  
MARGIN

Many players have already digitized their largest distribution centers, so the flow of stock from factory to distribution center to retailer is automated: Orders are placed automatically, and robots move pallets around warehouses. Other retailers have outsourced many of their distribution operations to specialists.

AI can further reduce supply chain costs. In the past, humans made decisions over the best way to transport goods, namely whether to do a single large shipment in a large truck or make several smaller deliveries, and whether to make direct deliveries to stores or go via a large, regional distribution center. Now, digital analytics can figure out the cheapest, quickest routes and take into account a wider range of factors than a person can.

While supply chain costs are generally equivalent to just 2 to 3 percent of sales, AI in this area could potentially boost a retailer's margin by around 1.0 to 1.5 percentage points.

## COMMERCIAL DECISIONS

AI can churn through data in a fraction of the time of a human being and far more accurately. Head-office staff can then devote their time to decisions that only humans can make – those involving intuition and emotion, such as aspects of stores' location, design and presentation.

## CATEGORY MANAGEMENT

+1.2 PP  
MARGIN

Decisions on the products to offer within a category have been mostly guided by the gross revenues and margins they generate. AI can help make smarter decisions by analyzing past transactions to see the propensity of customers to switch between products in the same category. If a product can easily be substituted for a lower-cost equivalent, then the retailer can make the switch and earn a better margin. For example, boxes of tissues come in multiple

brands that offer relatively small differences in quality. By analyzing purchase data from a sample of customers in this category, retailers may be able to identify brands with lower brand loyalty and replace them with a private-label version to earn a better margin. In our past projects, the newest, state-of-the-art algorithms to make better product choices yielded increases of up to 6 percent in like-for-like sales, boosting the company's overall margin by 1.2 percentage points.

## PRICE AND PROMOTION MANAGEMENT

Most retailers still design their promotions around intuition and negotiation with the product makers. However, promotions have complex effects. A special discount on Brand A shampoo will likely boost a retailer's sales of both that shampoo and other related Brand-A products – now and in the future. But the promotion will come at a cost and might also hurt the retailer's sales of Brand-B products. AI can help reveal the true impact of promotions. Doing so starts with measuring the impact of a promotion against a more accurate baseline that incorporates seasonality. In some cases, retailers will identify promotions with a negative overall impact – that is, when the promotion does not lead to other sales that compensate for the costs. Our past projects indicate that a sophisticated promotion algorithm can increase the company's margin by 1.5 percentage points over the course of one or two years.

+1.5 PP  
MARGIN

## SUPPLIER MANAGEMENT

Contracts with suppliers, containing buying terms and conditions, are usually based on factors such as products' historic margin performances. AI can sift through data on different variables to provide evidence of what drives this performance, as well as the commercial importance of the supplier to the retailer and vice versa. It can thus help retailers to manage suppliers systematically and suggest the best negotiation tactics. There are significant variations in the effectiveness with which different retailers manage their suppliers. We think applying AI in this area could increase a retailer's margin by 2 to 4 percentage points.

+1-4 PP  
MARGIN

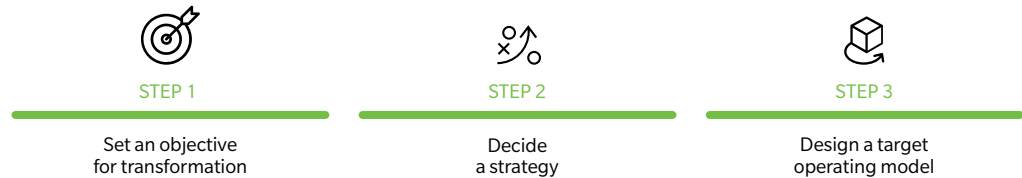
## HOW TO GET STARTED WITH AI

Nearly half the executives responding to our Chinese survey said they are willing to invest up to 5 percent of sales in AI<sup>1</sup>. However, there's a common belief that introducing AI capabilities to a business is complicated. Technical challenges include obtaining data of sufficient quality, writing the code, and generating actionable output.

1) Of the 27 respondents, 41% answered "between 1 and 5%," 7% answered "5-10%," and 4% answered ">10%"

The simplest way to start is to ask the right questions, work with an experienced partner to develop the right technical tools, and be aware of challenges involved in training and hiring a workforce to work with AI. We suggest a three-step process (Exhibit 4).

#### Exhibit 4: Three steps to an AI future



Source: Oliver Wyman analysis

## STEP 1: SET AN OBJECTIVE FOR TRANSFORMATION

Retailers have limited resources, so they must pick the areas in which to deploy AI. The most important factor is the organization’s “crown jewels” – that is, the special capabilities that give it a competitive advantage and that it would not want to outsource to a third party. These distinguishing capabilities should already be clear from a retailer’s overall corporate strategy and the dynamics of the markets it operates in. They are candidates for investment in AI, so that the organization can double down on its core expertise and set business objectives for the results.

The critical questions are:

- What are the crown jewels that need to be protected and developed?
- What kind of impact could AI have on them?
- What are the business objectives for AI?

## STEP 2: DECIDE A STRATEGY

The business objectives decided in Step 1 should be the basis for a strategy to use data and AI.

The critical questions are:

- What is the right AI strategy for the organization?
- What is the right corresponding data strategy?
- Should the organization build or buy its AI capabilities?

We believe there are four sets of capabilities that retailers should consider for their AI strategy, as well as the six, more-specific, solutions suggested previously in this report:

**Commercial effectiveness:** Excellence in a retailer's core trading functions, such as its product range and management of suppliers, prices, and promotions.

**Operational efficiency:** Superior management of supply chains – that is, logistics planning, warehousing, and transportation – and labor resources.

**Product development:** Accurate targeting of consumer demands.

**Experience innovation:** Knowing customers well enough to deliver a personalized experience throughout their shopping journey.

For a premium retailer of fresh products, the key might be to select the best natural products and make sure they get to shoppers in the best possible state. A value retailer might optimize pricing and promotions to enhance its competitive advantage. Both will need to understand marketing analytics and stock the right products for their respective sets of customers.

## STEP 3: DESIGN A TARGET OPERATING MODEL

In an AI-enabled organization, the “machine” takes over some tasks from the workforce, and it is common to fear that humans will simply be replaced by AI. However, we firmly believe that machines will never completely replace existing occupations and job categories. Instead, there are more likely to be task substitutions, as workers are freed up from old tasks to focus on new ones. In the United States, one new high-tech position should create 4.9 supporting positions, according to a World Economic Forum (WEF) study. Globally, AI will result in a net gain of 58 million jobs between 2018 and 2022, the WEF estimated.

What will change are the skill sets required by humans who work alongside AI processes. When retailers consider their target operating model, they should be concerned less with how many of their workforce they will need to let go, and more with the changes in the work they need their staff to do.





# CHINA'S APPAREL BATTLE:

## ONLINE VERSUS OFFLINE

The surge in e-commerce can give the impression that apparel shopping in China is moving completely online. However, physical stores have important roles to play now and in the future. To investigate the state of China's apparel market, Oliver Wyman asked 3,000 Chinese apparel shoppers detailed questions about their shopping habits. The results show that, while the apparel market is changing rapidly, the reality is far more complicated than many current perceptions.

## PERCEPTIONS OF THE MARKET

### **ONLINE SALES IS THE CHANNEL OF THE FUTURE**

Today, 99 percent of adults in Chinese cities have purchased apparel online. In addition, 50 percent have purchased a particular fast-fashion brand both online and in a physical store. As a result, the online share of apparel sales doubled from 20 percent in 2012 to 40 percent in 2017. So it is natural for fashion brands to shift their resources and efforts to online operations.

### **COMPETING ON PRICE AND PROMOTIONS IS NECESSARY TO WIN ONLINE**

China's e-commerce giants boosted online sales by creating shopping festivals named after dates, such as 11/11 and 6/18. However, these have evolved into promotion drives that take place almost every month, and at least half of online sales now involve some form of promotion mechanism. But are they always a recipe for success?

## THE REALITY OF THE MARKET

### **CONSUMER BEHAVIOR IS HIGHLY FLUID**

Our research shows that customers move between channels according to preference and convenience. By contrast, many apparel brands and retailers maintain separate organizational silos for their online business and physical stores. This choice to silo can result in propositions that often compete with, rather than complement, one another.

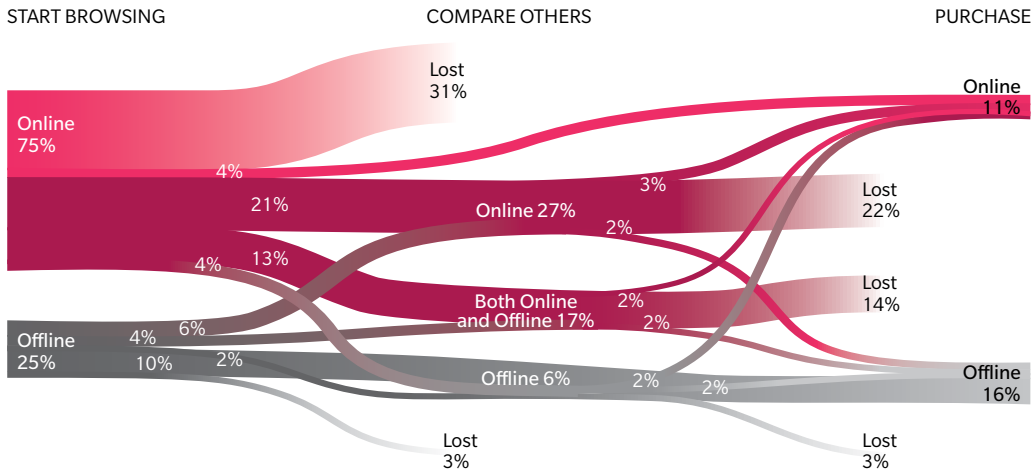
Three-quarters of shopping journeys for branded apparel start online and 40 percent of visitors to physical stores have first researched products online. The online channel dominates consumer research and comparison, accounting for two-thirds of engagements (Exhibit 1).

Online and offline activities are now highly connected at the decision-making stage, so most shopping journeys have more than one stop. As comparing and researching products online requires minimal effort, 75 percent of consumers go beyond the product they initially search for and look at other brands or in physical stores.

The wider choice available online has resulted in something that may be counterintuitive – lower brand loyalty. Key opinion leaders (KOLs) play the role that fashion magazines used to in driving the top of the brand funnel – where consumers become aware of a product and start to consider it. However, for someone to then actually buy the product, they also need to feel that the brand is “for me” (Exhibit 2).



**Exhibit 1: Customers follow a complex and meandering on-and offline journey towards a final purchase**



Source: Oliver Wyman 2018 consumer survey, Oliver Wyman analysis

**Exhibit 2: Key opinion leaders (KOL) behavior**

**NUMBER OF KOLS FOLLOWED**

**2.7** Number of KOLs regularly checked

**1.8** Number of KOLs that trigger purchase in PGM

**REASONS FOR PURCHASING BASED ON KOL RECOMMENDATION**

**51%** His/her recommendation attracts me

**37%** The products look good when the KOLs wear it

**41%** The product she/he recommends fits me well

**34%** I use this as a channel of fashion information

**40%** His/her recommendation will make me look good

Source: Oliver Wyman 2018 consumer survey, Oliver Wyman analysis

## MANY CUSTOMERS STILL PREFER TO SHOP OFFLINE

Offline channels play an important role at the purchase stage, accounting for 60 percent of all transactions. Offline conversion is almost 4.5 times as high as online. Moreover, while consumers buy 43 percent of their unbranded apparel online, when branded apparel has a physical retail presence they buy between 80 and 85 percent of it offline.

This “stickiness” within the offline channel reflects a continuing desire to touch and feel a fabric, look in stores for mix-and-match inspirations, and try on apparel to avoid the hassle of return and exchange. So, when they have a choice, consumers go to the offline channel as part of the shopping journey for branded products. The offline channel also contributes value through engagement that leads to online sales – and this is relatively more important than the online contribution to offline sales. While 15 percent of offline purchases begin online, 22 percent of online purchases have their origins offline. Similarly, with price comparison, 25 percent of offline purchases have involved online comparison but 30 percent of online purchases have involved offline comparison (Exhibit 3).

## FIVE LESSONS FOR APPAREL COMPANIES

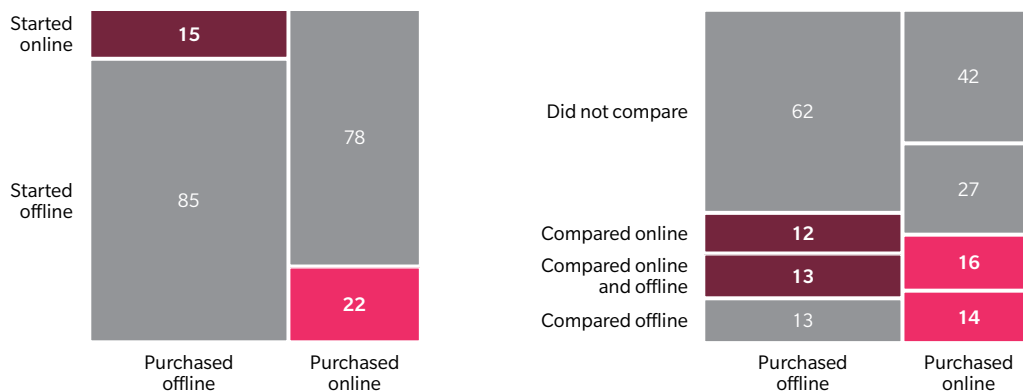
### 1. BE CONSISTENT ACROSS PLATFORMS

Though there is no one-size-fits-all model for organization, selling to omni-channel consumers calls for a joined-up approach that integrates e-commerce with the company’s other activities. Under Armour China, for example, has a standalone e-commerce team. But to ensure alignment with the company’s strategic principles, activities such as online merchandising and promotion are planned by a manager who reports to the heads of both the e-commerce and merchandising divisions. Consistency is also needed in the proposition brands offer online and offline. Uniqlo’s online ranges are the same as its offline, while Zara’s are twice as big to provide online customers with greater choice. Both companies maintain consistent listed prices online and offline. They also have a disciplined approach to promotions; Zara’s online and offline promotions are completely aligned.

Some brands position themselves differently online and offline, but there is a danger that consumers can lose track of what the brand stands for. Other brands offer inconsistent promotions in different channels. In both cases, the heavier, more-frequent online promotions have failed to boost sales and have instead led consumers to wait for the next promotion.

Our consumer research suggests that successful brands focus not merely on promotions or low prices but also on the overall value proposition – one that consumers recognize and acknowledge. The average selling price – including online sales – of strong brands such as Zara and Uniqlo was stable or rose slightly in 2017 and 2018 (Exhibit 4). Consumers are attracted by strong brand identity, reasonable prices, and good value.

**Exhibit 3: Importance of online vs. offline engagement compared to sales in the other channel, in %**



Source: Oliver Wyman 2018 consumer survey, Oliver Wyman analysis

**Exhibit 4: Performance of leading Tao brands**

RANK 2015	BRAND	2017 SALES (MILLION RMB)	GROWTH 2015-17	RANK 2017	CHANGE IN RANK
1	Hstyle	1,063	49%	5	-4
2	ONLY	1,577	82%	2	0
3	VERO MODA	1,531	79%	3	0
4	Uniqlo	1,607	99%	1	3
5	ZARA	1,358	109%	4	1
6	Inman	406	22%	18	-12
7	Ochirly	844	78%	6	1
8	LETIN	703	83%	9	-1
9	ELF SACK	417	46%	17	-8
10	Liebo	437	51%	15	-5

Tao brand for female apparel

HSTYLE	INMAN
<p>Opened 1<sup>st</sup> offline store in May 2018 focused on in-store experience</p> <ul style="list-style-type: none"> <li>• Displaying products only and not for sale</li> <li>• Featuring fancy architecture, and augmented reality interaction</li> </ul>	<p>Tested water in opening offline stores since 2015</p> <ul style="list-style-type: none"> <li>• Have opened about 400 stores offline now</li> <li>• Selling same newly launched SKUs at same prices offline and online</li> <li>• Offline sales reached 300 million RMB in 2017</li> </ul>

Source: Shengyicanmou, Oliver Wyman analysis

## **2. RECOGNIZE AND TAKE ADVANTAGE OF THE EMERGING NEW ROLE OF PHYSICAL STORES**

Flagship stores are more important than ever, as online shopping has taken away some of consumers' time and brands need to stand out more to win sales. Flagships should include a strong element of experience to let consumers bond with the brand. For example, Adidas opened its RunBase on Shanghai Xuhui Riverside to offer exceptional service to runners – including high-quality hardware, cutting-edge technology, the latest fashion, and training sessions.

However, there is now less need to place stores in primary locations. Instead, a strategy combining a flagship store with service centers might be more practical. In Japan, for example, Muji and Uniqlo both host iconic flagship stores in prime locations, supplemented by smaller, more-practical formats in shopping streets – and even in railway stations and airports. So brands should actively think about the roles stores play in the consumer journey, and rebalance their investments in location, store environment, and services.

Service models, too, can be varied to boost conversion rates. North American menswear brand Bonobos started in 2007 using an e-commerce model. It later set up Guideshops: A customer can book an hour-long, personalized visit where a guide shows them different products to try on – with no queuing for fitting rooms or checkouts. The average order size in these stores is twice that of Bonobos' online orders, and customers are more likely to make repeat transactions and less likely to return products.

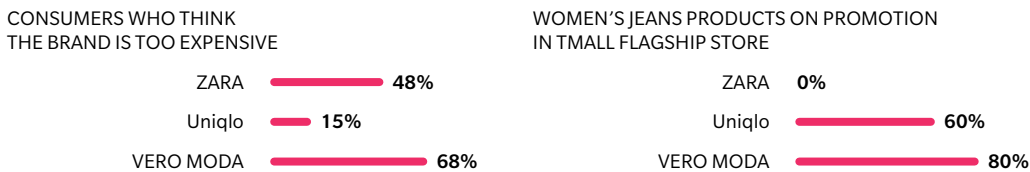
## **3. FOCUS ON ASPIRATIONAL PRODUCTS**

More space for aspirational items, such as bold colors and non-traditional prints, encourages customers to try clothes on. To create the appropriate impression, stores may need to reduce space dedicated to basics, instead directing consumers to order them online. For many brands, this will mean smaller stores that are easier to navigate. Any savings on rent can be reinvested in upgrading the store experience and increasing staff numbers, both of which would increase conversion rates.

However, online-only brands are now losing share, and increasingly competing on pricing and using promotions. Hstyle ranked number one among female apparel brands in 2015 but fell to number five in 2017; Inman was in sixth place but fell to 18th. Realizing an online proposition is not enough on its own, they both have started to experiment with physical stores to let consumers better experience their products (Exhibit 5).

Many brands that started online have also expanded offline to increase exposure and improve conversion rates. NEIWAI, an online-centered underwear brand established in 2012, has started to roll out a handful of experience centers to secure its position in the hearts and minds of consumers. The centers showcase different occasions on which to use the underwear.

## Exhibit 5: Value perception vs. promotion participation



Source: Oliver Wyman 2018 consumer survey, store check in July 2018, Oliver Wyman analysis

## 4. GET HEAVILY INVOLVED IN SOCIAL MEDIA

Key opinion leaders (KOLs) and media platforms can drive traffic through online platforms and social media – something that is now essential for success in apparel retail. There are plenty of successful examples of brands that have leveraged KOLs and platforms, both in apparel and in other industries. In cosmetics, for example, most trends are started by KOLs on social media. However, online marketing programs are becoming more expensive, especially with highly popular KOLs. So it is essential to measure their effectiveness and direct investment to the most valuable channels. Libeika is a fashion icon who posts mix-and-match recommendations on WeChat. Her conversion rate was once as high as 25 percent. After accumulating millions of fans, in December 2017 she launched a flash sale of products from her own apparel brand on her WeChat mini-program. Most products had an average selling price between 200 and 400 yuan, and the event achieved sales of 1 million yuan in just seven minutes.

## 5. USE ONLINE DATA TO UNDERSTAND CUSTOMERS BETTER

Innovative strategic approaches are needed to capture consumer data by channel, analyze it, and turn it into meaningful segment insights. Social listening is one way to hear what consumers think about your brand and find out about their experiences with it – good and bad. For example, scraping all the Weibo posts and comments related to Nike since January 2016 can help to identify key discussion points and how they have been evolving. Data from Dianping.com, for example, can be used to identify pain points in consumers' recent shopping experiences and to pinpoint problem stores so that prompt action can be taken.

**While online sales are growing rapidly, it's tempting to believe that this is the future. But offline shopping is still very much part of the whole sales picture, and is here to stay. The buying behavior of consumers is complicated, straddling online and offline channels which may be used for different parts of the shopping journey. To understand these subtleties within the apparel market, the China experience provides clear lessons for the rest of the world.**

# DIGITAL MEDIA PLAYS INCREASING ROLE FOR CHINESE TRAVELERS

The surge in outbound Chinese travelers over the past decade has had an impact on a variety of industries around the world. The travelers have both benefited and challenged retailers, consumer goods brands, the travel sector, and hospitality services alike. They have had an effect on outlet stores outside London, on German department stores, and on airport duty-free stores worldwide – as well as on every major hotel chain and airline.

Over the past year, Chinese travel has become increasingly social and digital, according to Oliver Wyman's latest survey of the subject. Independent travelers, who are comfortable using digital tools in their daily lives, are going online to plan their trips and share their experiences.





Chinese outbound travel has gone through dramatic changes over the years we have been following and describing it, since our first survey released in 2016. Outbound travel used to be dominated by organized tour groups. But today many Chinese are “free and independent travelers.” Luxury purchases – including buying for others, either for resale or on someone else’s behalf – once drove world-leading per-pax spend. But this too has faded as a wider range of Chinese people travel abroad and as luxury products become less expensive and more available at home.

Chinese consumers have leapfrogged shopping formats that are mainstream elsewhere and taken up mobile e-commerce, mobile payments, and social shopping with gusto. So it should come as no surprise that Chinese travelers are also highly social and digital. Our report, based on a recent survey of 2,000 outbound Chinese travelers, demonstrates this shift and shows its implications for business.

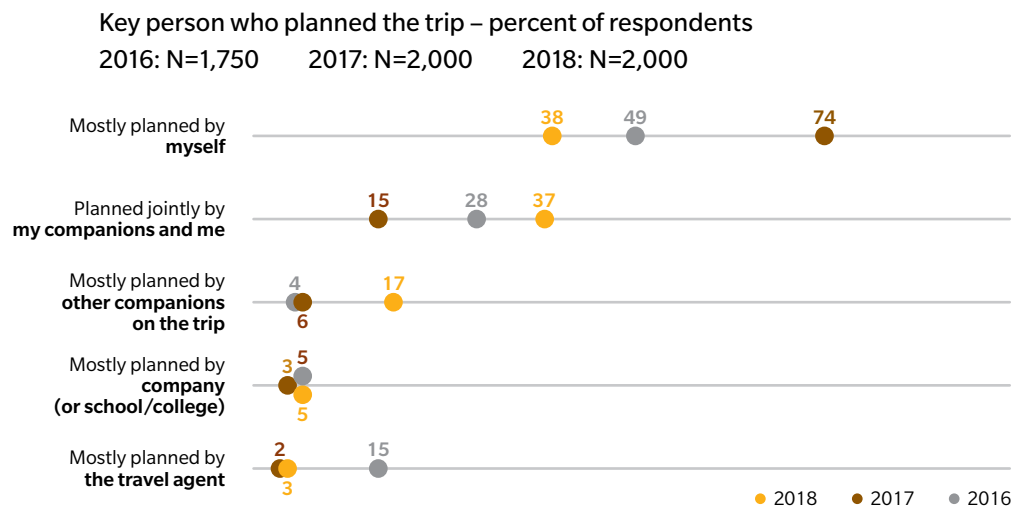
The number of outbound trips by Chinese travelers in 2018 reached 140 million, according to the China Tourism Academy – a 13.5 percent increase over 2017. That rise – slower than in previous years – was driven in roughly equal parts by the greater number of Chinese able to travel and by individual travelers’ increasing number of trips, our research suggests. The average traveler in our survey reported taking 2.1 outbound trips per year, an annualized increase of 6 percent. Meanwhile, the share of outbound Chinese from Tier 1 cities reached its lowest level since we began tracking it, reflecting a wider base of travelers.

Travelers' destinations and purposes are also changing. While destinations such as Hong Kong remain common, the trend in recent years has been towards more-distant overseas trips. Chinese travelers are increasingly comfortable traveling farther afield: When they were asked where they planned to visit in the next 12 months, Iceland broke into the top 15 destinations of interest. As travel becomes more frequent, trips are shortening, with the average duration falling by more than one day.

There was a strong increase this year in the share of people traveling with their spouses, extended family, and – in particular – friends. As a result, the average group size rose about 10 percent over the previous year. This was reflected in the way trips were planned as well. Up until now, the clear trend has been from professional-planning to self-planning. In 2018, however, more than one-third of respondents reported jointly planning a trip with their companions. That implies that the growing social aspect of Chinese travel begins before departure, during the planning stages (Exhibit 1).

When Chinese people travel with friends and family, they primarily seek memories: Sightseeing and recreation-and-entertainment were the most frequently cited reasons for a trip (Exhibit 2). According to 53 percent of our sample, “the most important part of a good holiday is to enable me to experience luxury that I can’t have back home”.

**Exhibit 1: Chinese travelers are increasingly planning their trips socially**



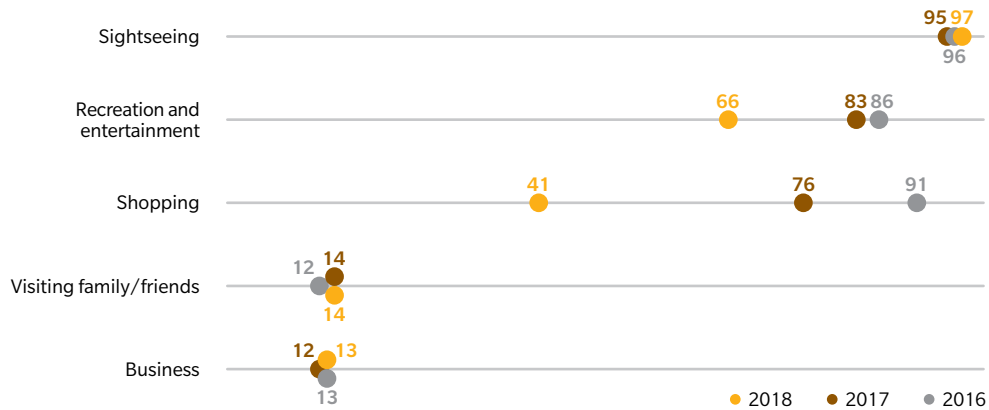
Question: Who planned the itinerary?

Source: Chinese Traveler Survey 12/2015, Chinese Traveler Survey 3/2017, Chinese Traveler Survey 11/2018, Oliver Wyman analysis



**Exhibit 2: Chinese travelers travel less for shopping and more for sightseeing, particularly for city views/local culture**

Trip purpose comparison 2016, 2017, 2018 – percent of respondents  
 2016: N=1,750    2017: N=2,000    2018: N=2,000

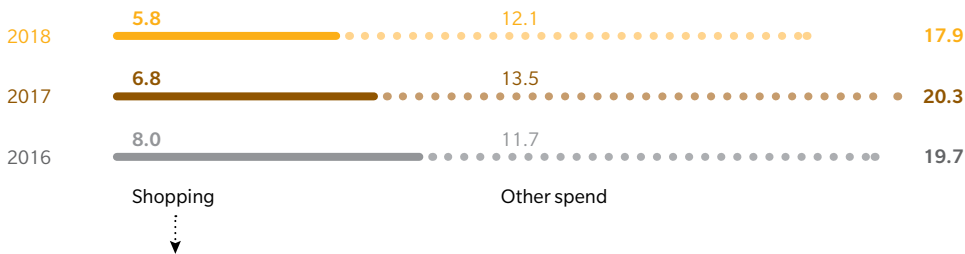


Question: What was the primary purpose of your last trip (rank up to three)? – Top three purposes

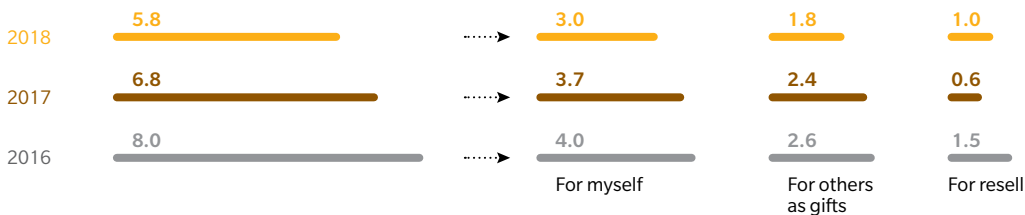
Source: Chinese Traveler Survey 12/2015, Chinese Traveler Survey 3/2017, Chinese Traveler Survey 11/2018, Oliver Wyman analysis

**Exhibit 3: Average trip spend decreased along with shopping spend**

Average shopping spend as share of trip budget – K RMB  
 2016: N=1,750    2017: N=2,000    2018: N=2,000



Trip purpose comparison 2016, 2017, 2018 – percent of respondents,  
 2016: N=1,750    2017: N=2,000    2018: N=2,000



Question: How much did you spend on this trip to (Generated Location) in each of the following categories?

Source: Chinese Traveler Survey 12/2015, Chinese Traveler Survey 3/2017, Chinese Traveler Survey 11/2018, Oliver Wyman analysis

## BYE-BYE “MAI-MAI”

Chinese travelers were once known to “mai, mai, mai” (“buy, buy, buy”) while abroad, but the once-central role of shopping in Chinese travel has been fading. For the first time in our survey, fewer than half the respondents cited shopping in their top three reasons for traveling overseas, and only 7 percent cited it as number one. For the second year running, Chinese travelers reported spending less on shopping year on year. The share of a trip’s budget devoted to shopping fell below one-third, with decreases in the amounts spent on shopping for resale, for other people, and for the travelers themselves (Exhibit 3). For some destinations, however – including Italy, Macau, and Korea – shopping still plays a large role.

The shopping that does take place while traveling is increasingly concentrated in duty-free and tax-refunded channels: Our sample reported spending more than 50 percent of their shopping budgets in these. Local brands and products are increasingly a focus of shopping while abroad, with one-third of respondents saying they choose to shop where they can find many local brands and products, a significant increase over the previous year.

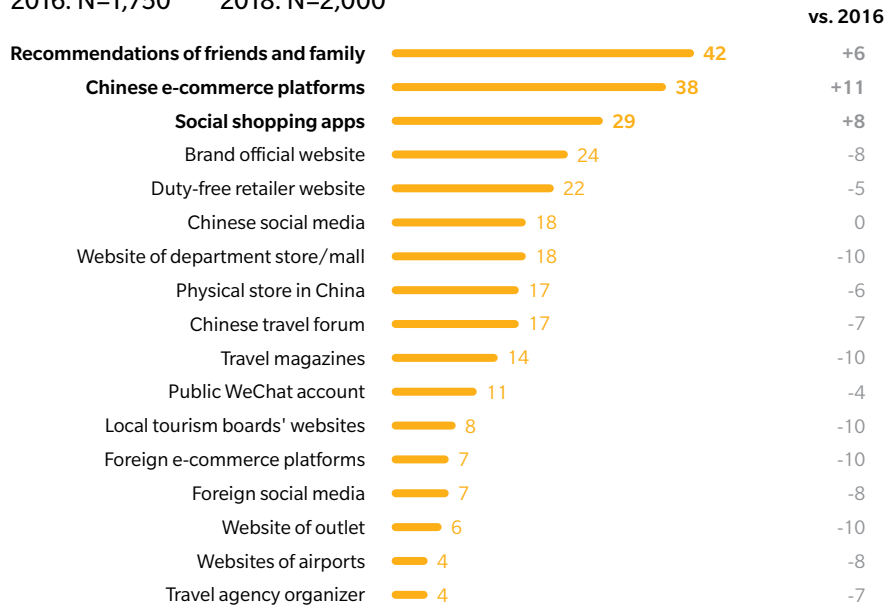
Social factors are key to deciding what people buy and where. As Exhibit 4 shows, recommendations from friends and family, review-driven Chinese e-commerce platforms, and social-shopping apps were the three most-cited sources of information for shopping while abroad.

**Exhibit 4: Shopping influenced by social recommendations and digital sources**

Sources of information, 2018 – percent of respondents

2016: N=1,750

2018: N=2,000



Question: Before your trip to (Generated Location), which of the following information channels did you consult to decide what to buy?

Source: Chinese Traveler Survey 12/2015, Chinese Traveler Survey 11/2018, Oliver Wyman analysis

# A TASTE FOR TRAVEL

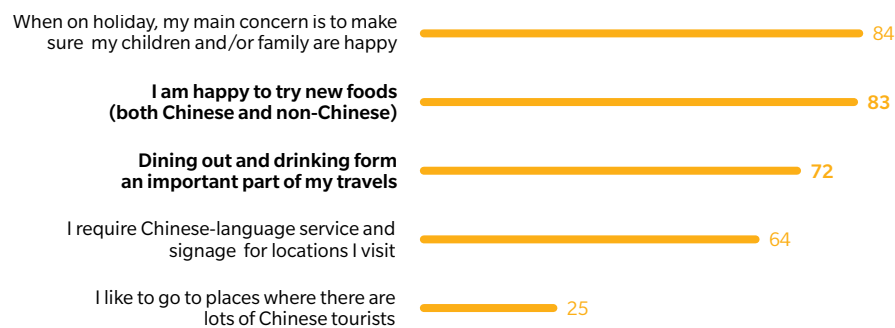
If shopping no longer drives Chinese tourism, what does? The answer is social experiences. Sightseeing and recreation are the most-cited reasons for travel (Exhibit 5). A key need for Chinese travelers while abroad is to create “shareable” memories – for example, photos of an authentic local meal or of the traveler and their companions in front of a well-known tourist destination.

## Exhibit 5: Chinese travelers seek out more authentic experiences

### Food and beverage (F&B) preferences while traveling overseas

2018 – percent of respondents

2017: N=2,000    2018: N=2,000



### F&B overseas travel description by agreement, 2018 – percent of respondents

N=2,000



Source: Chinese Traveler Survey 3/2017, Chinese Traveler Survey 11/2018, Oliver Wyman analysis

Food plays a central role in Chinese culture, so it is not surprising that it plays an important role in travel as well. About 70 percent of our sample agreed that “dining out and drinking form an important part of my travels.” What has changed, however, is the level of openness to local food: In 2018, 83 percent reported being willing to try new types of food, including non-Chinese. Travelers in our sample were far more likely to seek out authentic local cuisine than to stick with familiar Chinese eateries. The share saying they try to eat like the locals as much as possible exceeded the share preferring Chinese food, and that gap increased a net 20 points over 2017. Consistent with the trend toward digitally enabled “social” travel, online restaurant reviews were a key source of information for choosing where to eat, cited by 57 percent of travelers in 2018, up from 46 percent in 2017.

## PLANNING

Just as China has different services from the rest of the world for e-commerce, social media, and search, it also has its own online travel agents and aggregators. These are dominated by local players Ctrip, Fliggy, and Qunar.

Two-thirds of respondents said they used Ctrip to book flights and hotels, with Alibaba’s rebranded Fliggy platform taking the number-two slot. Direct bookings on official airline websites increased, as they improved their Chinese versions and Chinese consumers became more familiar with them.

Price, while still the number-one factor for choosing a booking platform, lost ground to other factors, including the provision of travel information and guides – which rose 32 percentage points – and the convenience of a one-stop service.

Airlines should note that Chinese travelers choose an airline primarily on price, the convenience of flight schedules, and its on-time record. While around 60 percent of travelers are aware of loyalty and mileage programs, these were the least-cited reason for choosing an airline, and their utilization is low. Travelers were five times as likely to say they used the programs but didn’t choose their airline based on them than to say they chose an airline because of its loyalty program.

Loyalty programs are similarly unimportant for hotel accommodation; they were the factor least cited as a reason for a particular choice. Chinese travelers book based upon location, reputation for cleanliness garnered from online reviews, and value for money. Chinese travelers take particular note of the hotel Wi-Fi and amenities offered – things like shampoo and soap: 40 percent said these have a strong impact on their impression of a hotel.

# HOW TO REACH CHINESE TRAVELERS

Marketing to Chinese travelers requires a specific, localized approach, given that they are digitally savvy, make frequent use of social media, and listen to others' opinions. As Chinese travelers rely heavily on word of mouth and online reviews, it's important for businesses to be present on the right platforms, to monitor and manage their profiles, to head off early issues that could generate negative word of mouth, and to create ample opportunities to generate positive word of mouth.

Sites like Mafengwo are key sources of advice for travelers, especially for dining and shopping. Online travel agents are widely used to book hotels and flights. For generating positive word of mouth, nothing beats WeChat, the dominant Chinese social media and messaging platform, which has plenty of opportunities for sharing. English has already adopted the word "Instagrammable"; businesses targeting Chinese travelers should learn the Mandarin equivalent, "晒" (shai).

**The opportunity presented by outbound Chinese travelers has rightly attracted the attention of a wide variety of businesses. These range from department stores to outlets, from the luxury houses of New York and Paris to Scotland's distilleries – and they of course also include airlines and hotel chains. Making the most of this opportunity requires up-to-date insights into and understanding of Chinese travelers and their motivations, as well as a concerted strategy that leverages local platforms and digital media. Does your organization have in place what it needs to attract today's Chinese travelers? And tomorrow's?**



# WHO WILL HOLD THE POWER?

## FUTURE TRENDS IN THE GROCERY SECTOR

Marc Poulin, former CEO of Sobeys, was interviewed by James Bacos, Retail & Consumer Goods Senior Partner, in a wide-ranging and freewheeling discussion about the current state of the retail grocery sector – and more importantly where it is headed.

**James: Last we spoke, Marc, you had just completed “The Retail Revolution,” which sought to project what will happen in retail over the next decade. Have you seen your predictions and expectations come true? Given the benefit of hindsight, do you have any second thoughts? Or is there something you wish to dial back and say, “Perhaps I wasn’t right” ?**

**Marc:** My general feeling is that our premise is still valid, and that the retail world is moving in the direction we identified. But that (the retail revolution) is less on pace and is developing more slowly than I expected.

*At the same time, we’re seeing it happen. I can talk about the grocery field. Since the study, there have been commitments by various players towards building their own platforms. They may not have been implemented, but they’re on the way. Kroger and Sobeys with Ocado are good examples. They’re building the facilities right now and the launch of either one will probably be in spring 2020. Once you get a few big large-scale players coming into the fray, we will see the acceleration we were talking about.*

*When you talk about elements or blockers, I think the biggest blocker is that some of the executives are not addressing it with the urgency they should. Another source of delay lies with economy and the consumer, both of which are pretty healthy in most markets. Because of that, grocery retailers may not feel the pressure as much since their traditional business is healthy.*


*But if we hit a recession, it’s going to be interesting. People will feel the pressure then because the business will not be performing well. At the same time, you’ll lack the resources to do what needs*

*to be done. I think the retailers who are not moving on that front or are moving slowly may get flat-footed.*

**James: Do you think there’s a risk there will be a major shakeout in five years? Or do you think it will take ten years for that to happen?**

**Marc:** I think it’s more of a five-year span. Yes, there is a major risk. I’ll give you an example: on the one hand, we see Kroger entering the state of Florida with one of their fulfillment centers, a market they’re not in currently; on the other hand, we have incumbent grocers who have historically steered clear of the internet.

*It’s going to be an interesting clash. There’s no way that incumbents will be able to get the technology they will need to compete fast enough if they wait to see if the customer reacts favorably to the new offering. Plus, if the economy goes into a recession or slows down, which everybody expects, then it’s going to hurt bad and it’s going to hurt fast. A brick-and-mortar retailer does not need to lose a lot of sales to have its bottom line impacted significantly. It’s always difficult to time*



the markets and to anticipate when these things will happen. Obviously, the jury is still out on whether the bets will pay off. But one thing we do know is that the technology keeps on moving and becoming more and more sophisticated.

**James: North America, particularly the United States, remains a fragmented regional market. There are some players that are purely national, but many are not. Do you see a place in the market for regional players, or is scale plus technology going to be the ticket to success, and the smaller players won't be able to play?**

Marc: What's going to save the regional players, in my mind, is that most of the e-commerce and online technology is going to be available to them as a service, either from technology players or big players who operate in another market and are willing to sell their technology.

So, yes, the regional players will be able to compete. They won't have the same profitability as the ones who developed the technology but, on the basis of their brick-and-mortar strength, they'll be able to remain in the game.

Instacart is an example of a technology that many players didn't have to develop. But it's something that a lot of grocers switch towards, at a relatively low cost. You see that model taking hold in other areas, too. We hear of many players who are developing analytics platforms that people can buy and put to work. To be honest, it's a good thing. A lot of those regional grocers don't have either the scale to do it on their own or the capabilities culturally to do so.

What's going to be interesting is the really small players who I believe will survive, as they may not need all that technology. The bigger regionals, on the other hand, may become too dependent on the technology providers if they don't do things on their own.

The key for any player will be to develop true competitive advantage with the way the retailer interacts with the customer, technology enabled or not.

**James: My colleagues in China are of the opinion that the Alibabas and Amazons – or other technology providers of the world – are going to be the tail that wagged the dog.**

**Ultimately, they'll be integrating into brick-and-mortar. Ownership and strategy will be led by technology, rather than purchasing, and it'll be a completely different world.**

**What do you think? Is that complete science fiction or will it happen?**

Marc: I don't think it's complete science fiction. At the end of the day, whoever controls the relationship with the customer is where the value is going to come from.

In the brick-and-mortar world, value was created by the daily interactions in the store. But in the new world, even for brick-and-mortar retailers, value lies in the data and the ability to use that data to create a better shopping environment for the customer.

The physical fulfillment of that value is not as important as it used to be. It's the data technology element that's important. That's why the technology player will have a bigger hand in the customer relationship and be able to extract more value from it.



I would say the technology player will get more and more control over the retailer, because that's where the value is being created. At the same time, huge players, such as Alibaba with Hema, will be tempted to use that power and deliver the brick-and-mortar experience themselves.

The key is: How do you create that relationship with the customer? That's where the value will reside. That's why I think the regionals will embrace those technology players. They will be successful if they can be creative in using the data to create more intimate relationships with their customers.

It's going to have to be in a very strategic relationship. For example, Kroger took shares in Ocado, which was smart, because you're going to get married for the long term with your technology partner. You'll have to find ways to influence the way your partner develops in the future.

**James: You've said power lies with the person or the company that controls the customer relationship. That power is derived from driving satisfaction and loyalty.**

**My own view is that I haven't seen much innovation in terms of driving satisfaction and loyalty. Analytics and looking at customer and card data have been around for a long time, but I have yet to see a dramatic change in the customer experience. What do you see as dramatic changes in the experience and the way customers shop over the next few years?**

Marc: I think it's going to come. But you're right: Customer experience is the area where there hasn't been much change.

In our model, we talked about three types of blockers or elements: fulfillment, delivery, and the interface, which is the customer interaction and everything else. Fulfillment is an area where we're seeing a lot more options. Delivery will move along on its own, based on technology and other developments.

The interface, however, hasn't really moved forward in many cases. Partly, it's cultural. A lot of the technology-driven players are steered by engineers, not marketers. They don't yet understand how to bring value to the equation.

But it's there for the picking. The reality remains that online players keep improving on the experience front. Artificial intelligence capabilities are making it happen.

For example, there's a firm based in Montreal that is focused on helping the pure e-commerce players by driving better use of the data and interfaces. Helped by artificial intelligence, they achieve pretty good results.

The brick-and-mortar retailers are slowly losing the race because the online retailers keep building their capabilities. Brick-and-mortar players are not investing enough of their resources and, at some point, it's going to be difficult to catch up.

**James: Let's switch gears. Up to now, we've been talking about the proverbial elephant in the room for brick-and-mortar grocery retailers: It's technology, disruption, and an aspect of their business that they don't know.**

**Sometimes, though, when you're looking at the elephant in the room, you may be missing a second elephant**



**standing behind the first. That second elephant, it seems to me, is the trend around the sustainability of the business model in a fundamental sense: the fact that you're bringing mangoes from Brazil every day to Canada. It's the idea of a carbon footprint and the costs associated with the modern world that are now starting to be paid in the form of climate change.**

**My sense is that this is beginning to be important to the consumer. Certainly, that's the case in Europe. But I'm wondering whether or not you think we might see a return to a different kind of grocery sale in North America. What's happened over the past 20 years has been an explosion of availability: A generation ago you couldn't simply walk into a retail grocer any day of the year and get a fresh mango. But if the mango you buy in a store comes with a label laying out its carbon footprint, will that have an influence over shopper behavior?**

Marc: I see this trend moving in increments. You're talking about the mangoes. I haven't had the feeling

that consumers are willing to give up the availability of the mango yet.

I don't know if it was the case in your life, but my grandparents tell me that they had an orange once a year, at Christmas. It was a big thing for them. Will the world revert to that? I think you'll need more economic cues than just a good feeling about it.

That said, I don't think you can run the business the way you used to without taking those externalities into account and at least looking at how you can address it. The notion of food waste is becoming more important. People are more aware of these things. In that regard, there's going to be a lot of pressure on being efficient from a systems point of view.

The notion of being able to distinguish what's important to which customer is going to be key. On the issue of climate change, you have segments of the population that are very passionate about it and very involved and segments who couldn't care less.

In the past, the brick-and-mortar response to polarizing topics such as

climate change was "Let's create a concept around that". There would be stores that would do things as usual, and there would be others that would be more like Whole Foods.

But, given the current data and technology capabilities, it doesn't have to be a concept. It just has to be a different offering to a different community and can actually be driven from a single infrastructure.

In that regard, again, the online players are more flexible than the brick and mortar guys. You could have an Amazon that speaks a different language to a more eco-sensitive customer than to a Donald Trump follower who may be indifferent to climate change.

To be able to speak a little bit differently to diverse groups of customers as a result of your knowledge of the customer is going to create opportunities for players that have that ability.

**James: Marc, you've given us much to mull over. Thank you for taking the time to talk with us. We appreciate it.**

Marc: It's always a pleasure.

# THE RACE FOR DATA

## DIGITIZATION IN THE GLOBAL FASHION INDUSTRY

Sharen Jester Turney served as president and CEO of Victoria's Secret for a decade before her departure in 2016, and led the company to record revenues of nearly \$8 billion.

Since then, she has served as an adviser to leading global fashion brands, helping them master an increasingly dynamic and challenging business environment. She shared her views on the state of the sector with Oliver Wyman's Martin Schulte.

**Martin:** *Sharen, as an expert in the fashion industry, what would you say has changed over the past 10 or 15 years?*

*Sharen:* Back then it was all about design and sourcing. Those two ingredients determined the success of a label. Spending was directed towards expansion, building new stores and expanding geographically into new countries, and less investment went toward backbone operations, such as IT and robust processes. Fashion used to be a sector driven by the designers. Much of that has changed, with analytics playing a growing role in complementing the creative parts.

**Martin: Can you expand on that a little?**

Sharen: In the past, there was a clear correlation between a product or brand's level of fashion and what a consumer had to pay for it. Players like Inditex have changed this and have democratized fashion. As a consequence, fashion is less of a differentiator to stand out from the crowd. Today, the mobile phone and other tech gadgets have partly replaced fashion in that regard. And of course, the role of e-commerce and mobile commerce has raised the bar for everyone in the sector.

**Martin: You've touched on digitization – what's the challenge for fashion players?**

Sharen: Many companies have a catch-up game to play. Capabilities in pricing and promotions – and I mean real promotions, not markdowns – are underdeveloped in our sector. So are classic category-management skills. Digitization provides a lot of options to help with these issues. To be fair, the fashion sector is more challenging than other retail sectors, given the increased number of and ever-shorter length of fashion cycles. There is very little continuity in what we sell, making time-series analysis difficult. Yet, most fashion retailers and verticalized manufacturers sit on a treasure trove of unused sell-out data.

**Martin: Are there some examples?**

Sharen: Sure. Our industry needs to learn how to cope with the sector challenges I mentioned above. One approach is to consequently identify products via their product attributes, allowing you to see patterns across several fashion cycles in terms of price elasticity, for example. Or take the example of RFID to track products across the value chain, to optimize stock levels and sell-through performance.

**Martin: Can digital tools help us with consumer insights and trends – to understand needs or predict the future?**

Sharen: Good point. In particular, on the consumer front there are myriad tools available that are already widely used by the beauty and cosmetics sectors, but less so by our sector. Things like social listening and the exploitation of weak signals from across messenger services, social media, and moderated communities are rich sources of insights. For example, a lot of these signals point to strong growth in the resale and secondhand market for fashion, partly driven by consumers' growing concerns about sustainability.

In addition, I see new and playful approaches emerging for trend research on the back of digitization, such as in gamification. It is not difficult to have the consumer play with a brand's app and have her rank trends or upcoming style options, for some kind of reward, of course.

**Martin: How can the CEO of a textile chain overcome these challenges?**

Sharen: I would advise them to find someone to help navigate the required changes and to lay out a clear digital agenda and roadmap. Otherwise, it is very easy to lose track of direction. Plus, I would advise them to constantly self-disrupt themselves. I like to say that "you have to fire yourself every year" to question your very personal behavioral patterns. If you want to make change happen, you must find a simple, to-the-point way of communicating. That is the only way to make this transformation happen.

**Martin: What's your outlook for the sector as a whole?**

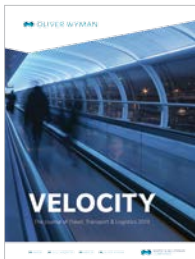
Sharen: The sector will continue to bifurcate into globally operating powerhouses and agile, highly capable niche brands. We will see the middle ground continue to collapse.

That said, I suspect we'll see the pendulum swing toward individual niche brands – or powerhouses able to mimic those brands – soon. Consumers today are over-retailed, over-choiced, and over-penetrated with the same brands globally. Highstreets and shopping centers across the globe look mostly the same. Consumers long for individuality and feeling special; this is a deep-rooted desire. This will naturally lead to a counter-reaction, as we have seen many times before in retail.

**Martin: Thanks very much for your time, Sharen.**

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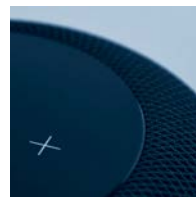
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