

# Game Changer Part 1

Prospects for the retail sector appear to be going from bad to worse, with far reaching implications. *Carter McNabb* predicts

**I**N THE 2010-11 financial year, according to Deloitte Access Economics, retailing posted its worst result in 20 years, with little prospect for significant improvement in the near future. While this is worrying in itself, reports such as this often overlook two key points.

Firstly, the retail downturn is not just an economic phenomenon; bricks and mortar retailers are now engaged in a losing battle with online competitors with lower cost operating models.

Secondly, changes in the retail sector have direct, measurable impacts on logistics service providers.

Analyst reports for listed logistics providers show they remain captive to a soft retail environment, and must now find strategies to invigorate EPS (earnings per share) growth, currently limited to about 6-8 percent.

Despite this, many bricks and mortar retailers are still looking skywards for the 'good times' to return. Needless to say, they aren't going to. This doesn't mean there won't be retailing 'good times' in the future, but the reality is, retail survivors will be pioneers who acknowledge the certainty of online shopping; substantially lower prices, the virtual collapse of national borders and a strong Aussie dollar.

According to Morgan Stanley Research, of the approximately \$60 billion in Australian retail market sales growth over the last six years, about \$10 billion was internet derived.

The United Kingdom and United States study reveals internet retailing has accounted for 19-39 percent of the growth in the industry since 2005. In comparison, Australian online retail has taken just 9 percent of growth. Since Australian internet retailing is far less mature than that of the US and UK, experience in these markets is relevant.

It is estimated over the next four years, \$13 billion of the likely \$50 billion growth in retail sales will be internet derived. In other words, internet retailing's share of the growth will be close to 27 percent.

The same study's market analysis demonstrates prices are between 19-64 percent cheaper online. High labour and rent costs play a big part in this premium in our view, and will be key drivers for more online retailing.

Growth in bricks and mortar sales are likely to slow to less than 4 percent over the next four years but at the same time, online sales are expected to grow in the order of 20 percent a year. The impact will be greatest in non-food categories, but this means we are talking about radical change in 48 percent of total retail sales.

Also, leakage offshore remains a topical issue given the ability for offshore retailers to bypass import duties and GST on goods under \$1,000. Australian retailers

are at a 10 percent price disadvantage in electronics and nearer to 15 percent in clothing.

As ever, retailers who read the markets and are agile enough to take advantage of the unavoidable changes will need supply chain partners to match their new strategy. During the next couple of issues, I will look at some of the options for retailers and the characteristics of their 'new reality' supply chains.

## GOING MULTI-CHANNEL

Even though there are distinct benefits in operating a retail inventory completely external to Australia's high real estate and labour markets, most retailers of the future will retain a floor space while adding an online presence. Their challenge will remain to offer attractive prices in the online world without cannibalising bricks and mortar stores.

Multi-channel retail expands the number of channels for customers to buy and receive goods and the mixture of options the customer has for ordering and delivery; for example, order online and pickup in store. While customers can take advantage of lower prices, they can also enjoy the pleasure of 'me time' shopping.

**“Many retailers are still looking skyward for the ‘good times’ to return.”**

Developing a multi-channel strategy can be daunting, particularly for retailers 'forced into it' by falling sales revenues. Many try out online retailing in addition to their existing businesses but most trials have three characteristics, which almost guarantee failure.

These include a lack of funding, senior management commitment and the failure to integrate supply chain and logistics providers into the solution.

The need to reduce inventory costs will push such retailers to create a common pool of stock for both operations and integrate the distribution operations for their bricks-and-mortar stores and direct-to-consumer businesses.

This approach provides both benefits and challenges.

On the plus side, selling online, depending on the level of the Australian dollar, enables retailers to develop markets overseas, which is especially valuable for quality or niche product lines. Depending on the product this can increase the selling season for seasonally influenced ranges.

But with two groups of consumers, stock-turns could increase. A common pool of inventory serving two quite different demand and replenishment models



increases the complexity of forecasting demand, management of discount cycles and the whole 'cost to serve' model.

In addition, the efficiencies of online retailing are complicated and may be lost depending on transportation pack sizes and the need to repack and redistribute at high Australian labour prices before on-shipment to retail stores or individual consumers.

Logistics providers, internal or third-party logistics (3PL), will also have to change their game. Logistics support for an internet trader, however committed, can be more intense or can morph into a different part of the market. Some retailers are servicing their online clients through Australia Post or other parcel carriers. This growth has caused capacity problems for the international carriers, such as UPS.

Will it create a problem or an opportunity for your business? Other traders are developing or finding 3PLs capable of servicing the last mile; still others are exploring more socially innovative options; for instance

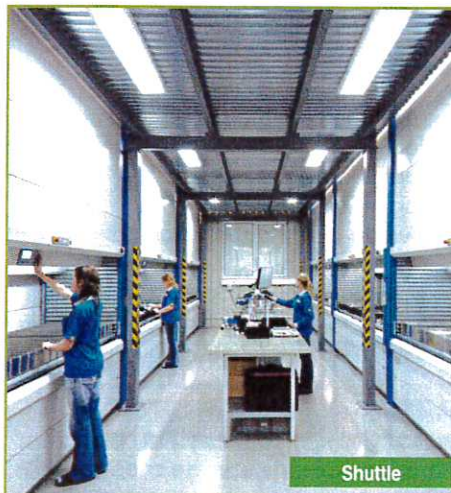
having customers collect goods either from the shop or from local 'depots' such as convenience shops.

These changes create opportunities to shape and service a new market where the 'handover' becomes a retailer's value-add, not a customer's role. And then there is the increased demand for reverse logistics when the 'dress doesn't fit'.

As the retail environment changes forever, so does retail logistics. Opportunities abound for the fleet of foot; those logistics services companies that understand the new market and strategise to win. ||

Next issue: Navigating your way from multi-channel to cross-channel retail

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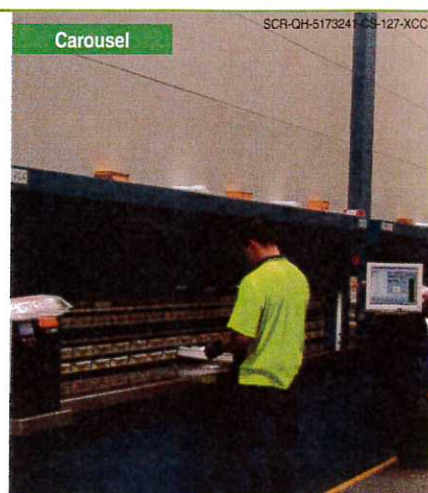
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