

September 2008

Small-Market Retailers Show Big-Market Growing Pains

According to data from the August 2008 Aberdeen Group report *The Complete Mantra of Driving Holiday Selling through 2008, 2009 and Beyond*, 55% of leading retailers see the need to "counter competitive selling strategies" as their top holiday pressure. This Aberdeen retail Research Brief drills down to smaller, Tier 3 retailers (retailers with annual revenues of less than \$50M and hereafter referred to as "smaller retailers"), to see if they feel the same pressures as leading retailers, and explore and delineate the issues affecting the readiness of smaller retailers for a successful holiday season.

To determine their holiday readiness, several questions were asked of these smaller retailers: "What capabilities and technologies are you able to leverage from Tier 1 (over \$1B in annual sales) and Tier 2 (\$50M - \$1B) companies?" And, "If you were unable to use their capabilities and technologies, what was the next best proper course of action?" In other words, how Tier-specific are retail capabilities and enabling technologies?

The final context in answering how smaller retailers can make the most of their modest IT budgets is how they attempt to accomplish their IT goals given the current economic downturn. Salvaging a profitable holiday season this year, and preparing for future years of holiday success, requires the determination and establishment of clearly defined operational underpinnings.

Holiday Pressures, Strain, Opportunity, or All Three?

A leading consumer electronics retailer recently revealed that holiday traffic at their chain was 450% that of non-holiday traffic. This spike in customer volume puts an inordinate strain on retailer's systems. Conversely, it also presents retailers with a golden opportunity to make sales and margin goals they never would have achieved without this added traffic and incentive to buy.

As we are in the midst of a global economic downturn, it is imperative that retailers identify the pressures most specific to their specific segment. Due to the macroeconomic environment in which all retailers operate, some pressures will be the same for completely disparate groups. Such is the case with the top two pressures between Best-in-Class retailers and smaller retailers as reflected in Figure 1. Both groups are nearly tied when indicating their top two pressures: competition (38% for Best-in-Class, 35% for smaller retailers) and comp (meaning this years' sales over last years' sales from the same store; 31% for Best-in-Class, 29% for smaller retailers).

Research Brief

Aberdeen's Research Briefs provide a detailed exploration of a key finding from a primary research study, including key performance indicators, Best-in-Class insight, and vendor insight.

Recommendations For Action

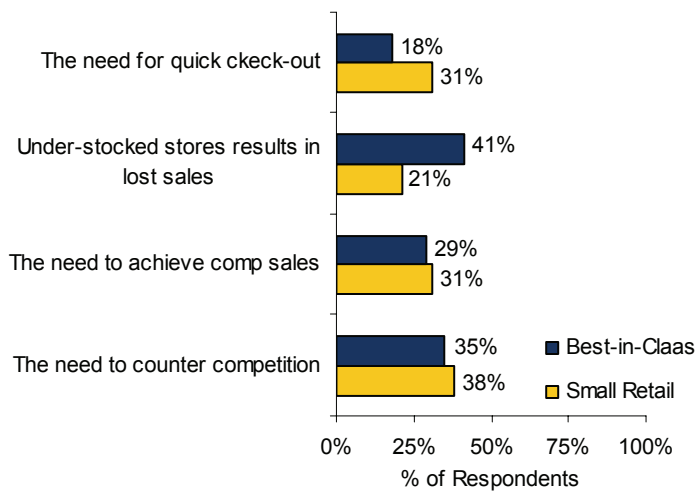
- ✓ Conduct systems diagnostics before peak season by an independent third party
- ✓ Don't skip steps when moving along the maturity model (e.g. premature use of Web 2.0)
- ✓ Make having a master data repository a top of mind priority

Microeconomic pressures also play a role. Best-in-Class stores have more sophisticated forecasting tools and supply chain networks; use of which opens them up to a greater depth and breadth of analytical issues needing resolution. The result is Best-in-Class retailers place increased pressure and expectations on themselves to deliver the correct stock in the correct amount to the correct location at the correct time (41% for Best-in-Class, 21% for smaller retailers). Since smaller retailers do not yet have the financial wherewithal or infrastructure for such efficient merchandise flow, their pressures focus on actual, measureable, financial impact: customer throughput at the point of sale.

"If a thunderstorm knocks out your power and keeps your customers at home, there's not a whole heck of a lot you can do. But if a similar store opens up in your strip mall, you've just got to take steps to deal with that."

~ Tom Walla, Partner,
Hobbytown USA

Figure 1: Sales, Inventory and Service - Paramount Pressures



Source: Aberdeen Group, August 2008

Best-in-Class Companies

Aberdeen used four key performance criteria to distinguish Best-in-Class companies (Top 20%) from Industry Average (Middle 50%) and Laggard organizations (Bottom 30%):

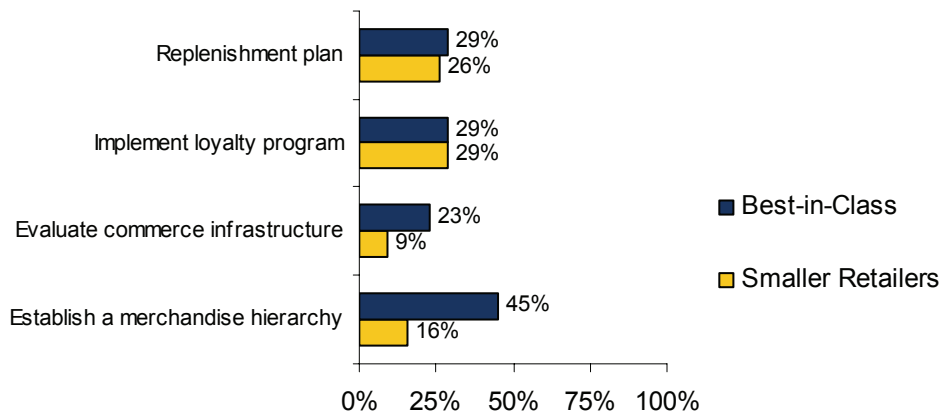
- ✓ Average sales comp
- ✓ Average gross margin
- ✓ Conversion rate increase
- ✓ In-stock performance

Holiday Action Plan for Smaller Retailers

Actions are the retailer's response to the pressures they perceive as most dire. As Figure 2 indicates, Best-in-Class and smaller retailers are once again almost exactly tied in two of their shared strategic actions: replenishment and loyalty. Both of these are traditional, key tenets of a retailer's successful holiday plan.

The other two (commerce infrastructure and merchandise hierarchy), however, differ markedly in that they are part of a "new wave" of actions of which forward-thinking retailers are availing themselves. Commerce infrastructure diagnostics has quickly emerged as a new, enterprise-wide best practice, measuring bandwidth capacity, traffic spike scalability, and "pre-peak systems triage." And establishing a merchandise hierarchy based on customer affinity and preference is clearly an advanced action well beyond the means of most smaller retailers (only 16%), but a functionality enjoyed by nearly half the Best-in-Class retailers (45%).

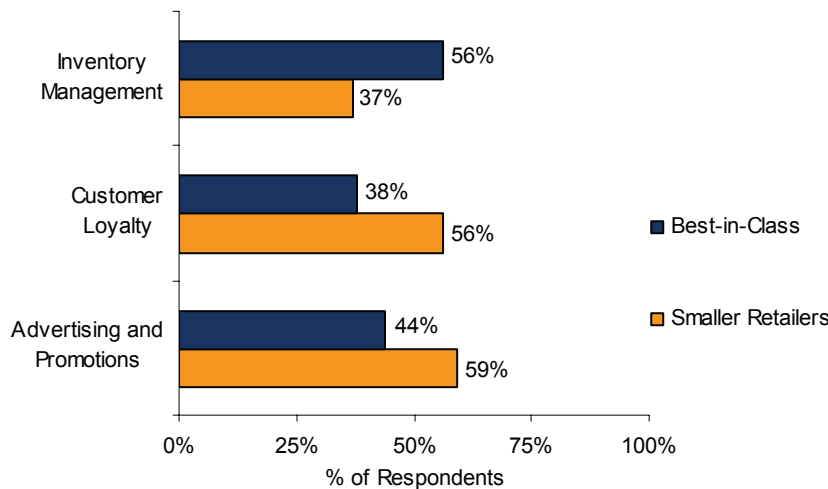
Figure 2: Top Strategic Actions - Small Retailers and Best-in-Class



Source: Aberdeen Group, August 2008

Supporting their strategic actions, all retailers have a plethora of choices when it comes to spending their holiday investment. As indicated in Figure 3, smaller retailers prefer to spend holiday investment dollars on the most straightforward, customer-facing applications of advertising and loyalty. Best-in-Class retailers also spend a considerable portion of their holiday funds in these areas, though not to quite the same extent. This is because Best-in-Class retailers also invest functional holiday dollars on internal-facing applications as well as external-facing ones. Inventory management is a Best-in-Class favorite (56% for Best-in-Class to the smaller retailer's 31%), as is replenishment (31% to 26%) and store operations, such as store planning, planograms and in-store communications (25% to 11%).

Figure 3: Top Functional Areas of Holiday IT Investment



Source: Aberdeen Group, August 2008

Recommendations for Smaller Retailers

The following are key recommendations for smaller retailers heading into a potentially very tough holiday season in 2008, with additional recommendations for bolstering success in 2009 and beyond:

- **Perform a comprehensive health-check of your enterprise.** Go through each sales channel and have an independent third-party check for vulnerabilities. Examples include evaluating any bandwidth changes due to new releases; integration costs between disparate applications; a thorough review and determination of the correct level of exactitude on SLA's - for Best-in-Class, some applications may be deemed "mission critical" and worthy of the cost of 24 x 7 support, while others are considered less inherently essential, and can suffice on the less costly option of overnight batch processing, once system functionality is restored. But remember; you won't be the only retailer seeking these pre-holiday check-ups and services, so don't wait until Thanksgiving!
- **Don't bolt web 2.0 functionality to the site prematurely.** While appealing, "immersive" customer-facing applications such as social networking, dynamic content, search tools, personalization, and online comparison shopping tools certainly are useful in the proper context, you have to have reach that context in order for such a move to make sense. In other words, make sure your architectural platform is fundamentally sound and integrated across all commerce channels. Your business will be far better off if you eschew 2.0 applications in favor of more fundamental infrastructure upgrades, channel integration, enterprise-wide inventory visibility, and efficient, demand-driven replenishment.
- **If you sell only through brick and mortar, your 2008 efforts should focus on short-term, tactical wins;** customer throughput at the register, use of handhelds and other mobile tools to bring information and productivity out onto the selling floor, and providing self-service tools such as kiosks to cross-sell and up-sell.
- **If you sell only through brick and mortar, your 2009 efforts and beyond should focus on specific business process pain points,** determining which enabling technologies will assuage or eliminate them, and construct an implementation roadmap based upon need, value, and cost.
- For all retailers, but especially those selling through multiple channels, **every effort should be made to construct a data repository for merchandise, customer, and data information storage and management.** By providing a "single view" of these data types, you support improved utility, flexibility, and opportunity across the entire enterprise. Forty-four percent (44%) of smaller retailers report having this functionality now, with 33% more planning to construct such repositories within the next 12 months. Best-in-Class retailers are even more enthused, with

"Moosejaw's goal is to sell the finest outdoor, surf, skate and snowboard products in the world and have as much fun as possible while doing it. (Crossview) knows that loyal customers receiving a consistent experience will lead to larger order sizes, more frequent purchases, and the viral spread of its brand story."

~ Jeffrey Woolf, COO,
Moosejaw, Inc.

57% reporting they have this functionality now, and 27% more plan to have it within the next 12 months.

- **If you sell through several different channels, make sure inventory is adjusted accurately and in real-time.** Retailers have a number of ways in which online orders are fulfilled. For one Tier 1 office supply retailer, once an order is placed and the payment recognized, fulfillment can come from a number of different locations: from a Distribution Center (DC); from a scaled-down DC-like structure known as a fulfillment center, or even from a nearby store. Each of these fulfillment choices has varying degrees of paperwork associated with the sale, and varying times before the disparate inventory silos finally get reconciled with the master Inventory "system of record."

Table 1: Vendors that can Help Assist Scalability Issues of Holiday

Company	Industry Focus	Sample Customers
www.accenture.com	Professional services company with deep expertise across a number of businesses, including retail.	Staples, Pep Boys. Has 17 focused industry groups in five operating groups. This industry focus provides a thorough understanding of industry evolution, business issues and applicable technologies
www.adobe.com	An on-demand rich media platform. Can streamline dynamic content to any channel and enhance the online shopping experience.	Mercedes, Kodak, Louis Vuitton
www.akamai.com	26,000+ servers help ecommerce retailers deliver reliable, fast, scalable performance.	1-800-Flowers, Marks & Spencer, Blockbuster, Pacific Sunware, others
www.aldata-solutions.com	Exclusive retail industry focus. Their Core Retail Suite includes merchandising, sales, replenishment, logistics and store operations	Customer base mostly in Europe, but N.A. clients include Price Chopper, McDonald's, and Trader Joe's.
www.atg.com	A leader in ecommerce web content, including Web 2.0 and other immersive technologies which benefit retailers.	Chico's, Scotts Lawn Care, T-Mobile, Casual Male, others
www.crossview.com	A vendor specializing in multi-channel integration, order management and fulfillment, and providing a consistent, uniform shopping experience at each customer touchpoint.	Moosejaw Industries, Sam Ash Music, Dave's Bridal, Sony Style, Integrity media, Barney's, Vanity Fair
www.epicor.com	Like JDA, Epicor has assembled a fairly complete, end-to-end retail suite of applications, including those from Epicor, NSB and CRS.	Aeropostale, American Eagle Outfitters, Ann Taylor, Zales

Company	Industry Focus	Sample Customers
www.islandpacific.com	Now going under the moniker of Island Pacific Merchandising System (IPMS), they are a leading merchandise planning vendor for the small and mid-tier specialty market. Out of the box system-wide functionality appeals to smaller retailers.	Customers include Brookstone, Samsonite, and Lily Pulitzer.
www.JDA.com	An end-to-end, retail-specific enterprise suite, capable of providing nearly all functionality growing retailers need.	5,500 customers across all retail verticals. Accounts include Ace Hardware, Jones Apparel, Stride Rite, Coach, and many others.
www.microsoft.com	A major player for all sized retailers, Microsoft has made a concerted effort of late to penetrate the all-too-often overlooked SMB market. Special areas of focus include store systems, real-time analytics and supply chain.	Lehigh Safety Shoes, H-E-B Grocery, Clarke (CPG) Distribution

Source: Aberdeen Group, Month 2008

For more information on this or other research topics, please visit www.aberdeen.com.

Related Research	
Responsive Customer Loyalty ; June, 2008	The Mantra for Driving Holiday Sales ; August, 2008
The Changing Dynamics of Retail Promotions ; February, 2007	Technology Strategies for Multi-Channel Integration ; April, 2008
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