

The future of retail: How to make your bricks click

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No, the brick and mortar store is not dead. Here's how to use physical stores to your advantage in the digital age.

This is no easy time to be a brick and mortar retailer. Across the U.S., sales within physical stores are at a standstill, while those of online retailers zoom along at double digits. Between 2008 and 2013, e-commerce sales grew ten times faster than in-store retail. (Exhibit 1) What's more, the digital world continues to infiltrate the four walls of traditional stores, where shoppers are armed with smartphones and an entirely new set of expectations.

At the same time though, the future for brick and mortar stores doesn't have to be as dreary as it looks. The concept of a physical store, whether at malls, downtown districts or shopping centers, is not going away any time soon. In fact, in 2020, more than 80 percent of U.S. retail sales will still happen within the four walls of a store.

The retailers who thrive in the next decade will be those that reimagine and redefine their stores for the digital age. Brick and mortar retailers have enormous opportunity to leverage the distinct benefits of old fashioned, in-person shopping in ways that digital sites can only dream about. Tomorrow's winners will be those who are able to transport the digital world into their stores in a manner that delights customers, builds loyalty and generates brand value.

Why digitize your physical stores?

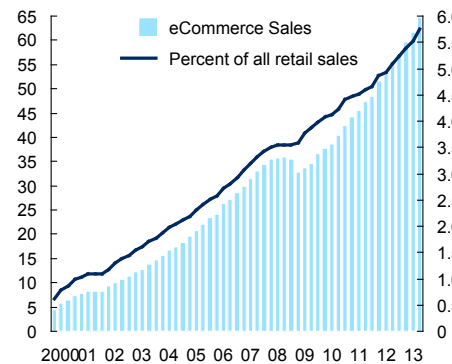
It is essential for stores to digitize in order to meet the increased customer expectations now a reality in an always-on, whatever-you-want world. More than 60 percent of Americans have a smartphone and 80 percent of these consumers are "smartphone shoppers"—they use their phones to help them shop while in a store, most often to research product reviews, specifications and compare prices.

Exhibit 1:

In US, e-commerce continues strong growth in both dollars and share...

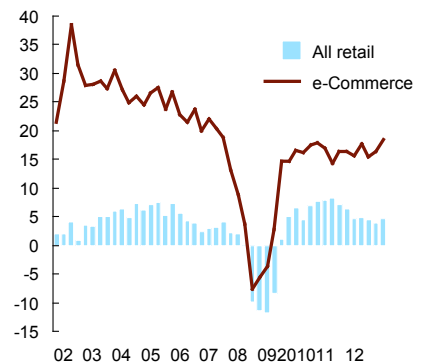
US E-commerce sales¹

\$ Billion, seasonally adjusted; Right axis percent



Sales Growth

Compared to same quarter in previous year



¹ Excludes travel, tickets, and financial services

SOURCE: US Census Bureau; team analysis

The various interactions consumers have with digital media and digital platforms have rewritten the arc of the consumer decision journey, causing shoppers to become accustomed to a much greater level of convenience, choice and accessibility. The use of a variety of online-only features—such as personal recommendations, product reviews from other customers, huge product assortments and availability, and 1-click everything—has afforded shoppers the power to make purchasing decisions much more on their own terms. When the doors swing open to the temperature-controlled confines of a store, shoppers bring many of these expectations with them. (Exhibit 2)

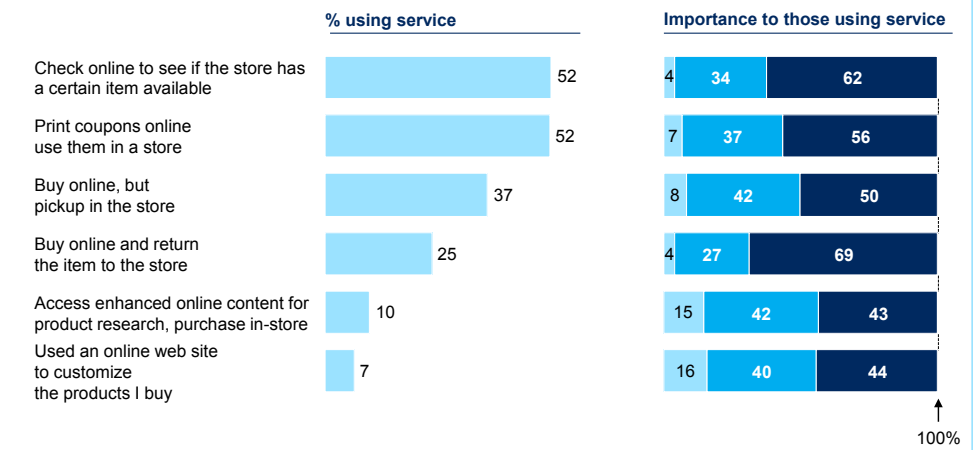
Exhibit 2:

Integrated on- and offline services going beyond multi-channel

Not important
Somewhat important
Important or extremely important

Importance of multichannel functions among survey participants

% of respondents; N = 4,877



SOURCE: iConsumer 2013 – RT16aa, RT16bb

Two decades after Netscape and Amazon were founded, more and more industries are approaching the tipping point where digital is becoming the “new normal.” (Exhibits 3 and 4) This is the point at which traditional retailers must become advanced incumbents in order to survive. To do this they must effectively compete with online-only players by evolving into integrated digital enterprises. Laggard incumbents, or those who do not successfully innovate, simply will not survive.

Exhibit 3:

While grocery and household products have remained solidly in store, nearly all other categories have rapidly digitized in last 5 years

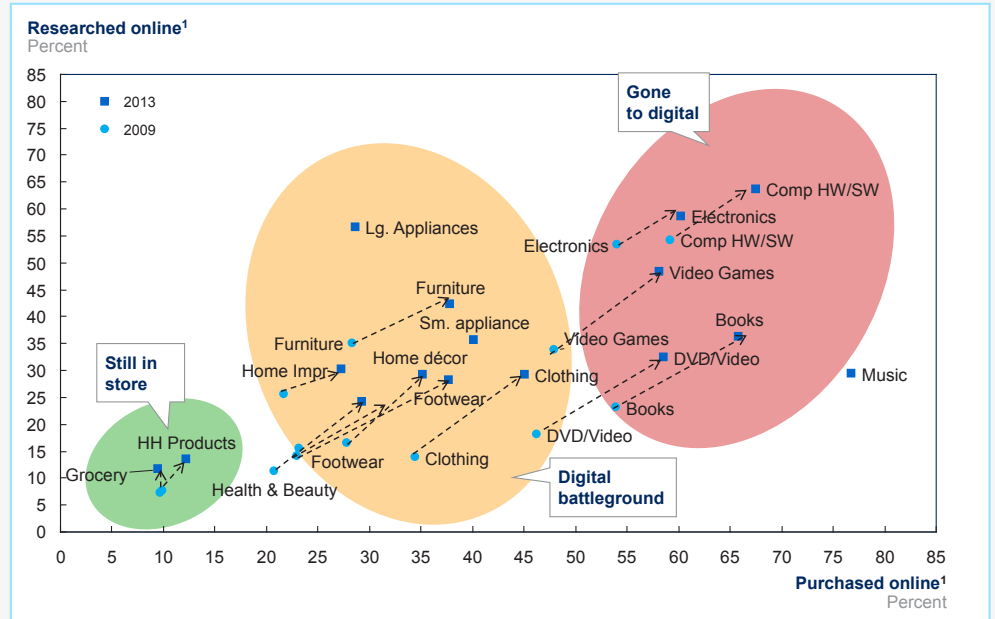
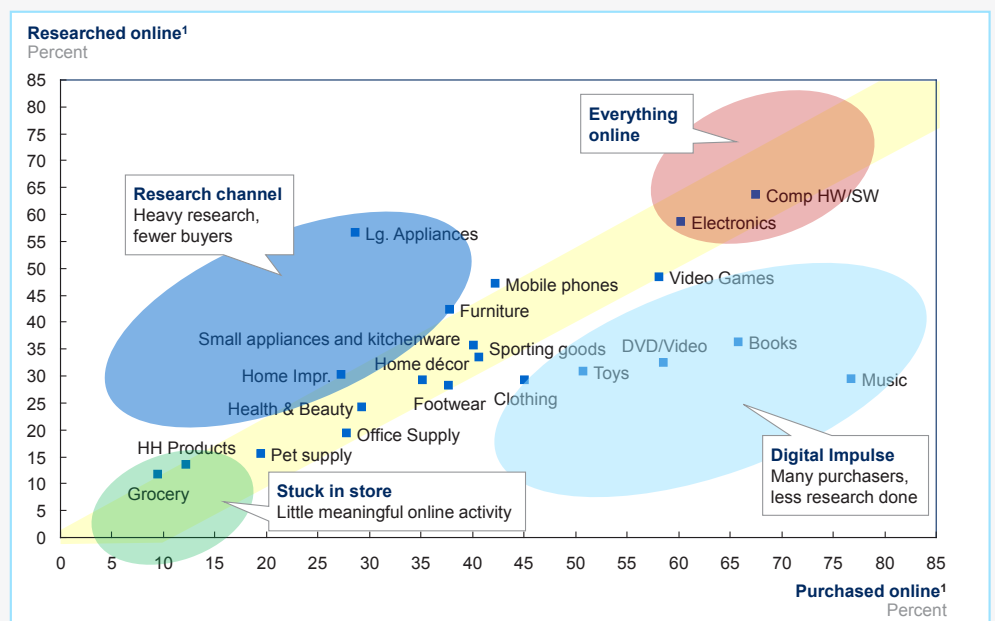


Exhibit 4:

... and online channel has developed as “impulse” vs. “research” channel for certain categories



What does it take to make your bricks click?

By uniting traditional advantages with key success elements of the digital experience, brick and mortar retailers have the opportunity to offer consumers an experience surpassing that of online sites. Brick and mortar stores, for instance, can provide the sort of visual navigation and tactile experience that will be hard, if not impossible, to ever replicate online. This holds true not just for electronics or other online-savvy product categories, but also more traditional ones like clothing and large appliances. Nearly one-quarter of apparel shoppers say that digital touch points are the most influential factor in the initial consideration phase of their consumer decision journey. By marrying offline strengths with digital advantages along three main areas, a wide range of retailers can see significant sales impact, a higher conversion rate for customer promotional efforts, and a reduction of inventory days on hand.



Merchandising—Avoid lost sales and improve the in-store shopping experience

Retailers have great potential to optimize their in-store product offerings in a way that enhances interactions with customers. In our experience, an expansion of both the range and presentation of merchandise can double sales.

To expand the range of products, well-placed iPads or interactive shelves offer customers a nearly unlimited selection of items—providing shoppers with added convenience. For retailers, the endless shelf strategy provides enhanced sales, particularly if there are products being offered that aren't readily available elsewhere. At Amazon, for instance, a large category of niche

books that cannot be stocked by physical bookstores represents a substantial portion of the site's book sales. While these niche books represent just 2 percent of all the titles Amazon sells, they account for 37 percent of the site's total book sales, helping to boost category sales by 60 percent.¹

In addition to substantially expanding product offerings, interactive shelves can also give shoppers access to helpful and valued product features. Sephora, for instance, uses iPads to provide access to deep product content, such as whether a particular lotion gave a rash to anyone with a certain skin type. Customers can bring products to the iPad for scanning, which allows them to see additional information, read product reviews, or add the item to their shopping list. These features are also available as a mobile app that's been downloaded over 1.1 million times.² Such expanded product information also has a potential sales impact. In restaurants that have tested digital menus, access to additional details about the restaurant's food and wine selections have led to a 20 percent increase in wine consumption.³

Digital technologies hold great promise for improving the presentation of store merchandise. Apparel retailers, for instance, can drive customer excitement by using 3D scanning technologies to create virtual fitting rooms that allow shoppers to see what specific items might look like on them. This technology records a customer's dimensions and contours, features questionnaires on style preference and clothes the customer already owns, and then creates a personalized profile that is accessible in all stores and online. Customers can do a virtual try-on of garments for a quick comparison and also share the images with their social network to get instant feedback from friends. In pilot programs, virtual dressing rooms result in more than a 50 percent increase in conversion rates for first time buyers and a 30 to 50 percent reduction in product return rates vs. online.⁴ Customers may also continue online try-ons at home, and perhaps at the store window during closing hours. Some leading-edge retailers have experimented with interactive mirrors and facial recognition technology installed in shop windows to allow virtual after-hours shopping.

Virtual fitting rooms can be coupled with a personal digital assistant that makes recommendations based on information given by the customer, the customer's purchase history, and current sales within the store. Burberry, for instance, has taken an innovative approach to digital merchandizing by using RFID e-tags to provide customers access to

¹ The Longer Tail: The Changing Shape of Amazon's Sales Distribution Curve," by Erik Brynjolfsson, Yu (Jeffrey) Hu and Michael D. Smith, 2010

² All company examples come from news articles and other public reports, unless otherwise noted.

³ Aptito

⁴ NCR and TechValidate survey

additional information about its products. Scanning an item in front of a “magic mirror” will call up details on how the product was crafted, along with suggestions for additional items it could be paired with.

Innovative start-ups are reinventing the store experience to provide ultimate convenience. A Tokyo startup called teamLab has pioneered virtual mannequins that are triggered when a customer removes a clothes hanger from the rail. Customers can then see models displayed on a video screen nearby in their chosen garment. In an example that illustrates how less is more, Seattle-based Hointer has launched a fully automated men’s clothing store that allows customers to shop quickly with the help of their smartphones. Rather than displaying a whole rack of clothes, Hointer features just one of each item. To select the item in the size they want, shoppers scan QR codes using their smartphones. Items are then delivered to their changing room using German robotic technology. The apparel can be purchased while the shopper is still in the fitting room by swiping a credit or debit card on a tablet kiosk. In addition to the streamlined digitized experience, this model also reduces the need for shelf and floor space and opens up new modes of attractive product presentation.



Marketing—Using digital data to reach shoppers

When existing customers enter a store, they are often eager, typically at an unconscious level, to be wowed by a compelling brand experience. It is important that retailers seize upon this opportunity, and digital technologies offer many new and strategic ways to do this. Retailers can, for instance, give shoppers who enter a store their own personalized offer of the day. After identifying existing customers, specific offers could be sent to their phone or displayed at a welcome terminal that also gives product info, online reviews and a Facebook/social product finder. The purchase of the product on offer would be enabled through a 1-click check-out

with the customer’s information already filled in. The customer could then choose immediate carry out or delivery “when you get home.” This sort of marketing effectively combines the store’s haptic brand experience with the benefits of the targeted and personalized promotions found online. New customers can also be engaged by this system and offered quasi-personalization through a back-end process of identifying their statistical twins.

Macy’s for instance, has partnered with Shopkick to install iBeacon transmitters throughout several of its stores. In this trial, customers who enter a store with the Shopkick app installed on their phones will be alerted to various rewards, deals, discounts and product recommendations. The technology enables shoppers to be shown products they had previously “liked” while browsing the web, when in the vicinity of that product in the store. It is important that this type of precision marketing be done correctly in order to avoid alienating shoppers. If executed with finesse and relevance, these campaigns can be very effective.

The Guatemalan shoe store Meatpack certainly found that to be the case. In order to avoid losing customers to competition, the company introduced an app that pushed warnings to customers’ cell phones whenever they entered the store of a competitor. The app then immediately offered timed discounts counting down from 99% until they reached a Meatpack store. According to the retailer, this app managed to steal at least 600 customers from the competition over the course of a week. What’s more, the bold idea also won the brand a lot of free publicity.

Other retailers are using digital technology to enhance their marketing efforts within various aspects of store real estate. For instance, adidas has introduced interactive storefront windows where bypassers can discover and explore products that are displayed in the window. Via a touch screen, a URL and a personal pin code, desired items can be saved directly to a customer's phone. This technology has drawn a significant number of shoppers into the store, with 25 percent of those who try it entering the store afterward, and 90 percent of bypassers watching while the storefront was used by someone else.⁵

The key variable to effective marketing will be the creative and strategic use of customer data. An example of how companies have used digital technologies to create compelling, personalized customer offers is airlines. One U.S. carrier, for instance, had a process for managing and executing multiple targeted micro-campaigns. These travel promotions were segmented by loyalty status but lacked any deeper segment orientation, and the destination offers were largely generic. It was only when the airline started leveraging its rich historical flight data that they were able to drive incremental trips. It did this by segmenting customers based on how they buy, how they fly, and how they engage with the airline and its partners. Drawing from this, the airline started offering individual recommendations based on algorithms that determined what destinations a customer had the highest propensity to fly. These "Next Place to Fly" offers communicated highly relevant and personal recommendations to customers along with the more standard discounts. As a result, the airline experienced a 6X boost in its booking response rate from these offers.⁶



Operations—Optimizing inventory

By digitizing operations, retailers have the opportunity to combine the immediacy of store purchase/pick-up with the supply chain excellence of online. The buy-online-pickup-in-store feature (BOPS) both enhances customer satisfaction and increases traffic and cross-selling in physical stores. For shoppers, it is becoming an expected feature—37 percent say they have used BOPS, with about half of those rating it as "important" or "extremely important." The ability to buy online and return to the store is slightly less utilized (25 percent of shoppers) but highly valued by 69 percent of those who use it.

For retailers, BOPS can be a sales tool. When customers see that products are available for purchase or pick up in stores, they are more likely to visit and perhaps do additional shopping in those stores. One national U.S. retailer that's a pioneer in BOPS, for instance, saw a 1.8 percent net sales increase after their BOPS implementation. Online sales declined by 1.8 percent when some customers decided to close their transactions after seeing the product available in stores. But this was more than offset by a 3.6 percent increase in offline sales due to the transfer of online sales to physical stores and cross selling from the additional traffic in stores.⁷

The supply chain excellence and real-time inventory data that BOPS requires also improves stock management and increases inventory turnover. Apple's inventory days on hand, for instance, has declined from 7.5 in 2008 to 3.4 in 2012, a drop of 55 percent.

⁵ <http://www.mediapost.com/publications/article/219668/tapping-the-smartphone-for-interactive-window-shop.html>

⁶ McKinsey pricing practice

⁷ "Integration of Online and Offline Channels in Retail: The impact of Sharing Reliable Inventory Availability Information," by Santiago Gallino & Antonio Moreno, 2012

Physical stores, too, can benefit from optimized inventory management. Pushing low stock turn products to the online channel can cut down on inventory and improve working capital. Gap is doing this with a new feature called 'Ship From Store.' The option lets online shoppers buy directly from store inventory, accessing items that might otherwise go to markdown. The feature allows Gap stores to keep their shelves stocked with the right items while also meeting the growing inventory fulfillment demands of the company's e-commerce channel.

The path ahead

Retailers who digitalize all steps of the customer journey are awarded with higher revenues and greater operational efficiency. Yet today, no stores combine all these elements for digitizing the in-store experience and engaging customers in omni-channel journeys. There is significant future potential. Digitization should be done gradually, first rolling out basic features and then testing new and more fundamental digital concepts through pilots in selected stores. Ultimately the end goal is an integrated, fully clickable and personalized in-store experience—the sort that customers have come to expect in the 1-click online age.

<http://mckinseyonmarketingandsales.com/focus/consumer-and-shopper-insights>

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