Merchandising the Right Product, the Right Place, at the Right Time

> *"Innovation is not the product of logical thought, although the result is tied to logical structure."*
> Albert Einstein

Merchandising brings together the understanding of customer behavior with product strategy and operational implementation. With so many channels and choices for consumers Merchandising is the critical focal point where your retail business and competitive ability are differentiated. This focal point brings together both internal considerations such as supplier relationships with external ones such as matching assortment profiles to various customer segments and locations. As a result, various inputs from Marketing, Finance, Customer Service and Stores and Channels come together and both influence and support the Merchandising function.

The precise definition of Merchandising will depend upon the specific context and may include working with channel strategy, assortment approach, selling and buying, promotions, stock management, and space management, but it will certainly involve how to sustain and amplify customer activity within the retail environment. The types of objectives are likely to include defining the assortment that meets customer expectations, adding value through merchandise augmentation and achieving product financial objectives. Merchandising will determine the depth, breadth and availability of the merchandise offer that aligns with overall retail strategy. Category management strategies will be supported with assortment suggestions that customers can identify with and respond to favorably.

At a marketing level, Merchandising also recognizes and manages product life cycles, ensuring that products or brands are allocated the right space, display and resources at different life cycle stages. New product innovations traditionally enter the business as "introductions" which, if successful, experience a "growth" phase and then move toward a more stable "mature" phase and then gradually into a "decline" phase. Product and market changes of a shorter time frame also require management, as in seasonal and fashion-related situations. Today's faster product-to-market cycles are giving retailers greater opportunity to implement more frequent and shorter seasons, offering customers fresher merchandise more frequently. There is more flexibility to add new product lines, bring in private labels and adjust the retail proposition to customers' evolving needs.

At a financial level, Merchandising will look at managing the buying budget and how product margin expectation contrasts against actual performance. These buying budgets will need to be aligned with sales targets such that appropriate buying commitments can be determined accurately. Without the understanding of future sales expectations, it would be difficult not only to manage stock, but also to offer the "open to buy" flexibility required in dealing with suppliers and product availability. Dealing with suppliers is not limited to supply commitments, but broader sourcing considerations such as supplier service, capability, innovation, product quality and increasingly social or "green" responsibility.

Merchandising represents the implementation focal point of the retail business, an interaction overlap between Marketing, Finance, Procurement, and Stores and Channels. The ability to execute on these various functional objectives is a difficult balancing act that determines retail success. Three significant barriers can prevent Merchandising from delivering the right product, the right way at the right time:

Barrier 1: ***Insufficient information to develop and execute a customer-centric merchandising approach***

Merchandising is looking to translate various inputs of retail strategy into a meaningful implementation framework. But to do so requires access to the finer detail of these inputs. At the most crucial level, customer shopping behavior and expectations must be distilled into identifiable and differentiated customer targets. Ways of reaching these customers through visual themes and effective messaging must be understood. Delivering on various product gross margin targets requires constant monitoring. If there are serious concerns around protecting profitability, these margin targets may be fixed, although it is more likely that higher margins will be achieved through a flexible margin policy that is well executed. This still requires working within defined pricing strategies and product characteristics that align with overall brand and/or channel strategy. All these inputs will support sourcing choices as well as considerations such as space management for stores and inventory allocations for channels.

Consistently balancing these multiple inputs around the appropriate merchandising offer is complex. Without the right information support, the approach relies more on human intuition. While this may be successful, it misses the opportunity to optimize the offer. Ever since the efficient consumer response (ECR) and customer-centricity initiatives came into being, managing the supply chain efficiently against the various consumer demand drivers has become a key concern of Merchandising. The science to support business optimization relies on information sweet spots to target the consumer in the most profitable manner using the various tools available to Merchandising. Today, success is increasingly decided in the detail, with Merchandising relying on these inputs to generate higher value to the business.

Barrier 2: ***Merchandising lacks the integrated business process information needed to develop a comprehensive and targeted approach***

Merchandising decisions affect and rely on Marketing, Finance, Customer, Stores and Channels, and other functional departments. Without appropriate visibility, departmental barriers may get in the way and stymie the merchandising process. By adhering to a single set of business goals and financial drivers and monitoring performance, combined with appropriate accountability, you can improve the process from strategy definition to alignment on priorities to engaging Finance, so the value drivers are understood and considered in any forecast.

Barrier 3: ***Inability to identify, measure and analyze the drivers of Merchandising success***

Retailers typically define success by sales or profit growth within a given time period. Measuring financial performance—sales, markdowns, costs, margins and turns—is vital, but interpreting only these metrics may lead to missed opportunities. It is important to measure the drivers that impact *these same sales and profits. From a Merchandising perspective, does allocating more shelf space or improving displays lead to higher sales, margins or cross-selling? How do color and size profiles vary across channels and regions, and what is the impact on lost sales?*

Merchandising depends on timely action. The sooner you know, the better. These metrics should let you know when to take action to protect profits. For example, quickly identifying slower moving goods enables merchants to implement a smaller early markdown or cancel merchandise on order. Accurate and insightful information on trends and performance are more important than perfection and indecision. Managing risk is part of the merchandising process, and may actually assist in understanding trends, drivers and their impact on the top and bottom line. Failures, when quickly discovered and corrective action is taken, can generate learnings and become stepping stones to success. Merchandising should look to understand what drives success and failure.

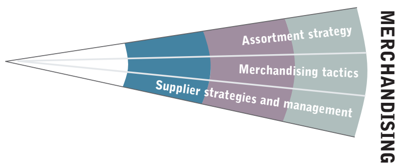
No amount of planning guarantees success. Making the “go or no go” decision requires information sweet spots to allow the business to decide how to resolve the issue through more resources, new offerings or pricing—while minimizing lost revenue, profit erosion or lost competitive advantage.

From a "Black Art" to a Consistent and Targeted Process

Merchandising combines many cross-functional requirements, distils various inputs, identifies trends, balances risk and learns from failures, such that it can define and implement a Merchandising proposition that customers respond to. Accurate information is a key enabler of this process.

Merchandising combines three key decision areas with associated information sweet spots:

- **Assortment strategy** ➔ What are the right products, presented in the right way, that meet customer demand?
- **Merchandising tactics** ➔ What is the right way to position, present and adjust your merchandise offering, and what is the impact of these tactics?
- **Supplier strategies and management** ➔ How do you align your retail strategy with suppliers, and how are expectations managed



Assortment Strategy

Assortment strategy is a critical decision area that correctly interprets the retail strategy and translates this into a proposition that meets customer demand. The right products are given the right profile in terms of a broad or deep assortment and are customized or localized for channels and store profiles, clusters or regions to entice the right customer in the right way. Traditionally specialty stores or category killers offer depth, while discounters, superstores and club stores offer breadth. *What is the ideal product range and selection choice for targeted customers? How does this approach impact your stock requirements?*

GOALS	METRICS	DIMENSIONS
Cost of Goods ($/%)	Sales ($/%)	Fiscal Month
GMROI ($/%) (Gross Margin Return On Inventory Investment)	Product Cost Increase ($/%)	Year
CMROI ($/%) (Contribution Margin Return On Inventory Investment)	Gross Profit ($/%)	Quarter
	Contribution Margin ($/%)	Month
	Inventory ($)	Week
	Inventory Days (#)	Organization
	Inventory Days Cover (#)	Division
	Aging Inventory Days (#)	Channel
	In-stock Positions (#)	Store
	Out-of-stock Positions (#)	Department
	Sales by Price Point ($/%)	Organization Code
	Price Adjustments ($/#)	Region
	New Product Sales ($/%)	Region
	Category Sales ($/%)	Territory
	Assortment skus (#)	Locality
	Own Brand SKUs (#)	Product Hierarchy
	Shrinkage ($/%)	Product Category
	Rebates ($/%)	Product Group
	Products on Promotion ($/#)	Product Line
	Supplier Performance Score (#)	Supplier/Vendor
	Supplier Delivery Lead Days (#)	Vendor/Merchant
		Supplier/Manufacturer
		Price Tier

FUNCTION	DECISION ROLES	PRIMARY WORK	CONTRIBUTORY	STATUS
Merchandising	Executives	•		
	Professionals	•		
Store/Channel	Executives			•
	Professionals		•	
Marketing	Executives			•
	Professionals		•	
Customer Service	Executives			•
	Professionals		•	
Supply Chain	Executives			•
	Professionals		•	
Finance	Executives			•
	Professionals		•	

Decisions regarding the merchandise quantities and types of inventory needed across these same assortment profiles will also be evaluated. A well executed assortment strategy will increase sales, stock turn and profits. You should be able to quantify how the various buy units impact financial performance and ensure that these same units easily move along the supply chain. This is a just-in-time process where the stock-keeping unit (SKU) arrives at the right time at the various supply stages and with a timely shipment to the store. The balance between meeting the customer demand in a timely manner without over-stocking or out-of-stock situations is finely tuned. Seasonality will be considered, along with how quickly the suppliers can respond to new trends. The faster a retailer can identify and adjust to changing customer demand with a “new” and “right” proposition, the higher the financial reward.

Merchandising Tactics

This decision area is concerned with the tactical implementation of any assortment strategy. *What are the channel, space and presentation implications for a given product range or category? How do these align with the pricing and promotional strategies? Are the on-line and in-store displays communicating effectively the customer proposition? Is a store remodel, re-prioritizing the environment or visual cues of certain assortments needed—where, how, why? How are various price points managed and displayed in practice?*

GOALS	METRICS		DIMENSIONS
Merchandising Cost ($)	Sales ($)	Outlets (#)	Fiscal Month
Merchandising effectivness Score (#)	Unit Sales (#)	Number of Product Firsts (#/$)	Year
Transaction Value ($)	Traffic (#)	Average Price ($)	Quarter
	Transactions (#)	Average Market Price ($)	Month
	Markdowns ($/%)	Price Change ($)	Week
	Visual Displays (#)	Price Point Breaks ($)	Organization
	Space Allocations (#)	Promotions (#)	Division
	Placements (#)	Promotions ROI ($/%)	Channel
	Sales per sq. feet/meter ($)	Store Development Initatives (#)	Store
	Selling Space (sq. feet/meter)	Store Upgrades ($/#)	Department
	Profit per sq feet/meter ($)	Square feet/meter per Outlet (#)	Org. Code
	Changes in Visual Merchandising (#)		Region
	Changes in Space Allocation		Region
	Merchandising Activities (#)		Territory
	Merchandising Activities per Outlet (#)		Locality
			Product Hierachy
			Product Category
			Product Group
			Product Line
			Price Tier
			Placement Type
			Merchandising Type

FUNCTION	DECISION ROLES	PRIMARY WORK	CONTRIBUTORY	STATUS
Merchandising	Executives	•		
	Professionals	•		
Store/Channel	Executives			•
	Professionals		•	
Marketing	Executives			•
	Professionals		•	
Customer Service	Executives			•
	Professionals		•	
Supply Chain	Executives			•
	Professionals		•	
Finance	Executives			•
	Professionals		•	

The practical execution of what needs to occur in-store is directly linked to the goal of generating increases in average transaction values and visit frequency. Augmentation opportunities to increase the customer spending within a category or potentially cross-category will be considered. By placing appropriate merchandise at the appropriate location with the right visual information, retailers will look to maximize customer spend profiles. Service requirements and space options will also be assessed to support these goals.

Understanding the impact of various merchandising activities is an important success factor. Successful retailers measure and monitor what works and use these insights to re-assess future merchandising tactics—ending the disconnect between corporate strategy and field execution.

Supplier Strategies and Management

Channel, store profile and assortment strategy will influence the approach and balance of this decision area, and the types of suppliers selected—local, national or international. Off-shore sourced merchandise will carry certain increased risks, such as political risks, and the continuity and consistency of supply will need to be managed closely. *What is the nature of your supplier relationships? How do these suppliers meet or satisfy your customer needs? Is the focus on centralized control or a more partner-based strategy to encourage creative supplier input and innovation?*

GOALS	METRICS	DIMENSIONS
Unit Costs ($)	Sales Growth ($/%)	Fiscal Month
Change in Unit Costs (%)	GMROI ($/%) (Gross Margin Return On Inventory Investment)	Year
Supplier Performance Rating (#)	CMROI ($/%) (Contribution Margin Return On Inventory Investment)	Quarter
	Quality Performance Score (#)	Month
	Supplier Initiative Score (#)	Week
	New Product Initiatives ($/#)	Organization
	Supplier Preference Score (#)	Division
	Claims ($/#)	Channel
	Inventory ($)	Store
	Inventory Days (#)	Region
	Aging Inventory Days (#)	Region
	Local Supply ($/%)	Territory
	National Supply ($/%)	Locality
	International Supply ($/%)	Product Hierarchy
	Supplier Discount ($)	Product Category
	Supplier Discount (%)	Product Group
		Product Line
		Supplier/Vendor
		Vendor/Merchant
		Supplier/Manufacturer
		Price Tier

FUNCTION	DECISION ROLES	PRIMARY WORK	CONTRIBUTORY	STATUS
Merchandising	Executives	•		
	Professionals	•		
Supply Chain	Executives		•	
	Professionals	•		
Store/Channel	Executives			•
	Professionals		•	
Marketing	Executives			•
	Professionals		•	
Customer Service	Executives			•
	Professionals		•	
Finance	Executives			•
	Professionals		•	

A critical requirement is to manage costs (price/margins), stock and lead time, or delivery expectations, but other considerations such as quality performance, product exclusivity, innovation and customization, and availability may also be defined in your supplier strategy. Supplier performance across the whole supply chain will be part of the scoring that will benchmark and influence the negotiation of future relationship expectations. Other issues include overall reputation, competency and ability to deliver on specific requirements, such as private label.

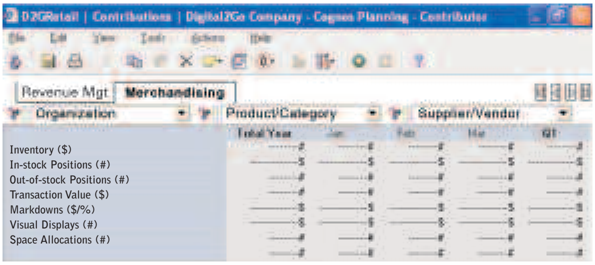
Beyond the "control" side of the relationship, the retailer will be looking for expert advice and creative suggestion of how to differentiate the value proposition. Suppliers bring another dimension or market knowledge and competitive comparisons to merchandise managers, providing market trends or related feedback from a different perspective, which can help in positioning or repositioning the retail strategy.

Assortment Strategy

Cost of Goods ($/%)
Product Cost Increase ($/%)
Inventory ($)
Inventory Days Cover (#)
In-stock Positions (#)
Out-of-stock Positions (#)
GMROI ($/%) (gross margin return on inventory investment)

Merchandising Tactics

Merchandising Activities (#)
Merchandising Cost ($)
Merchandising Effectiveness score (#)
Transaction Value ($)
Markdowns ($/%)
Visual Displays (#)
Space Allocations (#)
Placements (#)
Sales per sq feet/meter ($)



Dimensions

Fiscal Year/Month/Week
Region/Territory
Organization
Product/Category
Supplier/Vendor
Price Tier
Placement type
Merchandising Type

The Assortment Strategy and Merchandising Tactics decision areas illustrate how the Merchandising function can monitor its performance, allocate resources and set plans for future financial and operational targets.