

Finding Upside in the Downturn: Merchandising Best Practices podcast series Segment: Three of five

Hi, I'm Kelly Allen. What are some of the issues and trends impacting retailers and consumer product groups today? And what strategies can help them stay ahead? Today you're going to listen in as IBM World Wide Distribution Executive, Patricia Waldron, talks to Brian Hume. Brian is president and founder of Martec International, a leading retail consulting and training practice. Here, Brian talks about the different ways basket analysis can help retailers understand and better serve their customers.

Patricia Waldron: So, there are tough challenges in the market and I think we all agree that retailers in general are monitoring their organization more closely and re-forecasting more frequently and we have talked about some ways that they are doing it. What are some even more valuable techniques that retailers can use to make the most of information in a tough economy?

Brian Hume: Well, the first challenge for a lot of people is actually to realize that a trend has changed or a new trend has shaped up; people are usually pretty good, if there is a trend going on, they are pretty good usually at following it and where people pull down is recognizing that the trend changed. And one of the very valuable processes or techniques is the thing that everybody refers to as basket analysis and you can do basket analysis whether or not you have got any other kind of supporting programs like frequent shopper or customer loyalty programs. Everybody can use basket analysis and the key thing there is you measure how the basket is changing all the time and how that basket changes all the time will tell you a lot about your customers' changing tastes and priorities. So, if you look back over the history and say, what proportion of my customer baskets included brand A for example and how is that changing and you know are we seeing a bigger share of the baskets switching into brand B which might be the more value price brand as a for instance; but by using this approach of basket analysis, you can learn a lot about how your customers are reacting and if you do it in the right way, you can get some early warning signals so that you can kind of factor that into your planning. Now, if you also have some kind of a frequent shopper program or some kind of a customer loyalty program and you can collect the basket level data and link it to individual consumers, then you can run a customer segmentation analysis and divide all your customers into individual segments or types; in practice, for most people, you ideally group your customers into somewhere between three and about six or seven segments; statistically, you might want a dozen or 15, but actually what we found through experience is that as a business most businesses can't manage more than about seven or so, six or seven or so. But then, you can take your six or seven customer segments, you can look at how the basket mix is changing individually in each of those segments, and then you can say "Okay, this change varies by segments; now let's develop reaction strategies that are tailored to each segment." So, you might see for example in different segments different degrees of cannibalization, different degrees of halo effect, you might see different switching between brands, between products, ingredients and that kind of thing and if

you have got that basket analysis and you can view that by customer segment, then you can develop much more detailed strategies to respond in the best way.

Patricia Waldron: So, Brian, that is great to understand a little bit more about basket analysis and utilization of CRM and customer segmentation. How do retailers get started on that?

Brian Hume: Okay. Well, there are a couple of answers to that. The first thing is that the basket analysis can be somewhat daunting, especially if you start on the basis that I am going to analyze every single customer basket that we transact every day of the year, every week of the year, and so on and you end up with a phenomenal number of baskets and a phenomenal workload. They don't actually need to do that. There is an 80/20 process at work here like so many other things in retail and like so many other things in life in general. So, you could take a sampling exercise and say for example let me take all the baskets at the end of week 12 and then again at say week 25, week 26, then again at say week 39, and so, every quarter we could take a sample of the basket and then we could analyze how that basket makes changes. We can rank products individually based on their sales performance best to worst, so we can pick out our top scoring products and we might sell say 30,000 different products in our store, but we will rank them and the top 300 products will account for a huge share of our sales and then we will look at say that top 300 products and we will say "Now, let's look at those in the basket and see what things they drag along with them" and rather than attempt to do the whole thing for every single product and we have 30000 of them. So, you can go a long way by taking intelligent samples and doing the analysis of intelligent samples and in fact there were some companies that believed that you shouldn't ever do the 100% sample, because the incremental value you get isn't worth the incremental work content to do it. So, that is one thing and the second thing is you can actually, as long as you can identify the customer and you can assign the customer to a type, you can do a lot to understand that type of customer by just running things like workshops with your own store managers, area managers, individual buyers, and so on. And we have done this a number of times, We have a thing in Martec we call the customer game and if you, for example, if this is something you get interested in, if you approach your Cognos representative, we will gladly send you a free copy of the game. And what the game says basically is you get a group of 20 people in the organization that deal with the shop end of the business, usually out of the stores, they go and they cut photographs out of the local newspapers and the magazines and each individual aims to get five or six photographs of people they think are their typical customer, you put them all on the wall, so you end up with maybe a 100 photographs on the wall, you get the people to sort them into clusters, you end up with maybe five or six clusters, and you end up with a few outliers who doesn't seem to fit anything. So, you push the outliers to one side, you look at the five or six groups that you end up with, you take a flip chart, you take group one, and you say give me a name for a typical person in group one and somebody calls out a name and usually, it is pretty obvious to most people in the group that that name is representative of those people and then you start to build up on the flip chart the lifestyle of that person and then when you have done that exercise, you can go back and say "So, if I am in the fashion business, let me now ask you what are the things that this person would wear to work? What are the

things they would wear when they go out for a social on a Friday night or go out to something on a Saturday?" and you can start to say "Do we carry those kind of things in our product mix?" If you were in the grocery business, you would say "What does this person eat for breakfast and maybe they don't even eat breakfast at all," right, and then you start to say "Do we carry the right things in our assortment? What kind of income has this person got? Can they afford the kind of products we sell? Do we need to be at different price point? What kind of promotional strategy? And you can start this without spending a fortune on frequent shopper programs and actually, we very often say to people that have got frequent shopper programs, start with a game and it will give you a baseline and you could say "Now, let's go to the database and let's see if we can validate some of this in the database using the volume data examples. So, there are ways you can work your way into this. It doesn't need to start life, being horrendously expensive, it doesn't need to start life being horrendously complicated; you can get an awful lot of the value by doing some relatively simple things.

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