MULTICHANNEL MERCHANT
OPERATIONS SPECIAL REPORT

Seismic Shopping Shifts Bring Evolution to Operations

By **Tim Parry**

Shift happens. And right now, there's a seismic shift in how U.S. consumers shop.

Retailers are vying for time on their customers' screens across all their devices before, during and after a purchase, per The State of Retailing Online 2017 report released in January by the National Retail Federation's Shop.org division and Forrester.

Forrester estimated direct online sales totaled 11.6% of total U.S. retail sales ($394 billion) in 2016, but digital touchpoints impacted an estimated 49% of total U.S. retail sales.

Consumers are no longer just going to the store and buying what they need, and that is changing the way retailers do everything from fulfilling and shipping orders to communicating with and satisfying their customers.

As Sophelle CEO and Founder Doug Weich put it, consumers don't differentiate between shopping channels the way retailers do: They just want to shop and pick up their order at their convenience.

After years of being told by ecommerce analysts and experts that "this is the year of mobile," mobile commerce is finally here, and it's taking the traditional retail model with it.

"Every time there's a major disruption in any industry you tend to not see the best operators in the old model emerge in the new model," says Jason Goldberg, Senior Vice President of Content and Commerce at digital consultancy SapientRazorfish. "Now that we have this huge digital disruption we're all living through, there are new players."

Is Omnichannel Profitable?

So far, 2017 is shaping up to be the year of the shrinking store landscape. While chain stores such as Family Christian Stores and The Limited are shutting down for good, department stores such as JCPenney (up to 140 locations), Macy's (68 announced in January), Kmart (108) and Sears (42) are significantly downsizing their store footprints.

While many pure-play ecommerce companies are experiencing dramatically increased fulfillment costs, JCPenney Chairman and CEO Marvin Ellison says he's pleased with the double-digit growth of jcpenney.com, and with how leveraging brick-and-mortar locations is enabling the company to offset the last-mile delivery costs.

Ellison said he believes the future winners in retail will be the merchants that can create a frictionless interaction between stores and ecommerce, while leveraging physical locations to minimize the growing operational costs of delivery.

At first, this might look like a classic retail cost-cutting exercise to maintain profitability in a tough trading environment and appease stockholders. But Columbus Consulting International Principal Stuart Aldridge said it appears there is more to it than that.

Aldridge said JCPenney's decision to also close two distribution centers could easily be interpreted as part of a review of the distribution mechanics in response to fulfilling online business. He added that the decision to

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shake up product categories suggests that JCPenney is aware of the shifting nature of its customer base, both in desires and demographics.

"The department stores are feeling the full force of the Amazon effect," Aldridge said. "I would expect more announcements of this kind [by other store retailers] in the next 18 months."

Closing two of its distribution centers is a key strategic move because it will allow JCPenney to take advantage of omnichannel fulfillment methods such as ship from store and buy online, pickup in store, while also integrating store inventory to expand its online assortment.

Exposing store inventory online can result in higher online sales, increased foot traffic, improved store inventory turns and reduced carrying costs by leveraging stores to fulfill online orders with items sitting on their shelves, Sophelle's Weich added.

But can omnichannel initiatives be profitable? According to MCM Outlook 2017 survey results, 45% of merchants said their omnichannel business was in the black in 2016, while 12.5% said it lost money; the rest (42.5%) said it was a break-even proposition.

By effectively leveraging its in-store inventory, actively promoting more click-and-collect sales, and routing more orders to ship-from-store, OrderDynamics CEO Nick McLean said JCPenney has a momentous opportunity to significantly boost margins and bounce back.

"Several of our clients have already shown improved margins by increasing their ship-from-store capabilities, and closing distribution centers profitably," McLean said. "With the right order management technology, this could be a boost for JCPenney."

Shipping From Store

Omnichannel fulfillment has thrown a wrench in the works for merchants of all sizes, as consumers are dictating how and when they want to receive orders they have placed online. And that's not just for online orders earmarked for pickup in store, but for customer orders destined for delivery at as fast a pace as can be offered by Amazon.

But this increasingly popular fulfillment method requires sophisticated coordination between your retail commerce technology and in-store associates, making it challenging to implement and maintain. In fact, if you don't plan properly, ship from store can interfere with the in-store customer shopping experience.

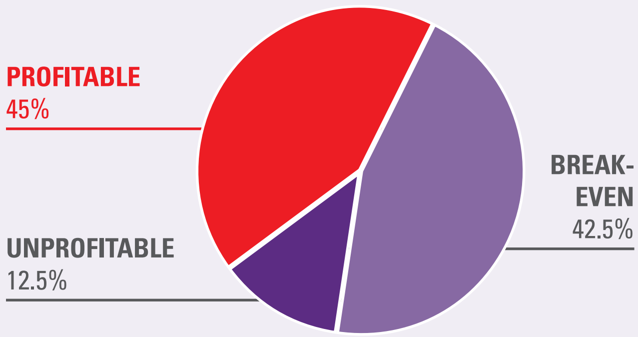
Because of the geographic coverage of the store locations, when you do ship from store, you'll often have a lower zone so therefore a cheaper package with regards to the distance that has to travel. And the package may even reach the recipient before the guaranteed delivery date, said LJM Consultants partner Thomas Andersen.

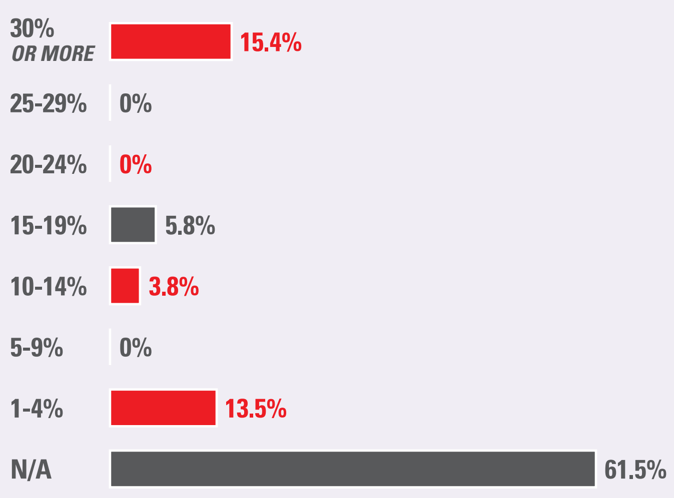
"You may have two stores that are only 15 miles away from the shipping address, whereas if you shipped from the distribution center, you might be shipping from three or four states away," Andersen said. "So that gives the shipper a big advantage."

But ship from store is not easy, Andersen said.

"You have a more sophisticated network to manage because you have packages moving from all kinds of different places," Andersen said. "You have employees that are packing and shipping those packages that aren't necessarily as well-versed as someone that's in a distri-

If you were an omnichannel business in 2016, were these operations:





What percent of orders placed online were fulfilled in-store for in-store pick up?

bution center. So you may lose some efficiency there, and [store employees] are more apt to make some kind of mistake than someone that does it [in a distribution center] all day every day."

The majority of MCM Outlook 2017 respondents (81%) said they fulfill ship from store orders during business hours. Half of respondents said they use employees whose hours are dedicated solely to ship from store.

Having removed the silos of separate store and online channels and shifting to a single shared inventory, many companies now see new silos emerging, said Robin Gray, a principal with Columbus Consulting International.

The ship-from-store capability allows retailers to easily respond to customers and better manage inventory. However, when the decision of which unit to sell from which store is a supply chain function, it can work in conflict with the allocation function, causing unintended stock-outs and harming the experience of the in-store customer.

To best meet the needs of both the online and in-store customer, allocation needs to be fed the information necessary to meet the combined demand, Gray said.

BOPIS Keeps Growing

Buy online pickup in store (BOPIS) is seeing great growth. In fact, 15.4% of MCM Outlook 2017 survey respondents said that 30% or more of their online orders were fulfilled in store for pickup during 2016.

Walmart's 29% ecommerce sales growth during the fourth quarter of 2016 can be directly attributed to its integrated offering. Over the holidays, its "Pickup Today" service grew by more than 27% year-over-year.

In 2016 approximately 75% of all JCPenneys' online orders touched a physical store, Ellison said during its fourth quarter earnings call. He added that even with a reduced store count, JCPenney is competitively positioned to deliver a differentiated department store model that meets the expectations of a digital world with an inspiring, tangible shopping environment.

But are retailers doing BOPIS right? Your retail store operations can have the greatest state-of-the art omnichannel inventory management system on the planet. But if you don't have the people and process in place to make magic happen, you're going to fail to deliver your customer an exceptional BOPIS experience.

According to a 2016 JDA consumer survey before the holiday season, retailers are still figuring out how to streamline the process and manage mounting customer expectations.

"The department stores are feeling the full force of the Amazon effect. I would expect more [store closing] announcements in the next 18 months." —Columbus Consulting International Principal Stuart Aldridge

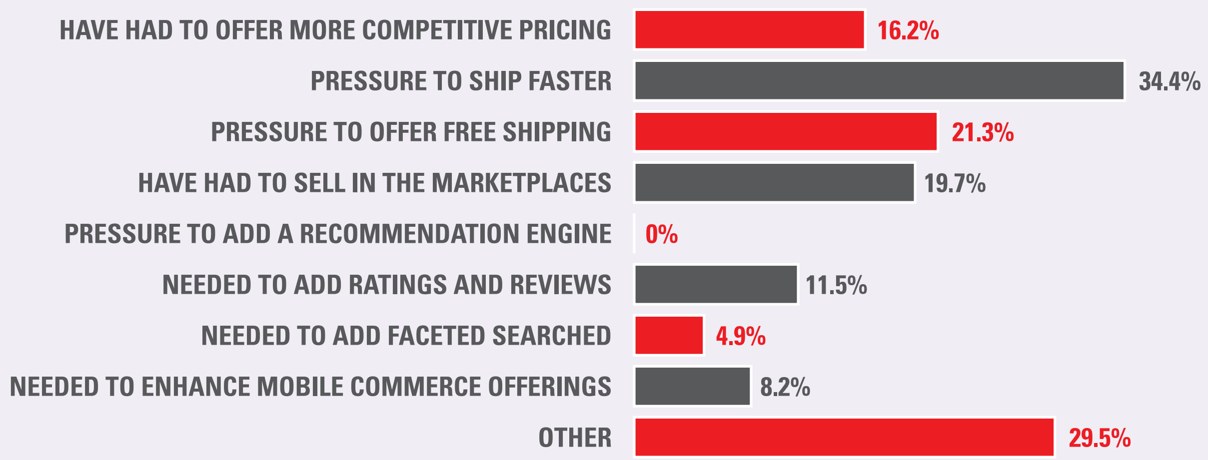
Forty percent of the respondents who have leveraged BOPIS in the last 12 months have experienced a problem. Of those problems, staff-related issues seem to be most predominant, with 22% of respondents reporting that store associates took a long time or were unable to find their order, and 15% reporting a lack of dedicated BOPIS staff to assist with pickups.

Changing Free Shipping Thresholds

Amazon and other ecommerce giants have made free shipping a virtual necessity to keep the customer satisfied. Per the MCM Outlook 2017 results, 21.3% of respondents said the effect of Amazon on its business includes the pressure to offer free shipping incentives.

And in 2017, ecommerce giants are changing the free-

What percentage of orders placed online in 2016 were fulfilled for in-store pickup?



shipping game by lowering their free shipping thresholds. In February, Walmart made waves by announcing it would lower its free two-day shipping minimum order value to $35. Three weeks later, Amazon quietly lowered its free shipping requirements from $49 to $35.

So Amazon's non-Prime members can enjoy free shipping, but Amazon did not specify whether they would receive expedited free shipping, or if it would take longer for those orders to be delivered.

With an average 42% of online orders shipping free last year, per DynamicAction, retailers have no choice but to keep a close eye on their customers' expectations to receive purchases without additional fees.

"The fact that Amazon released this free shipping threshold reduction with no fanfare displays that the pressure the vast majority of retailers have felt from Amazon over the past few years is beginning to go both ways," said DynamicAction senior vice president of global marketing Sarah Engel. "The fact that Amazon didn't outright match Walmart's free shipping timeline shows their continued commitment to the recurring revenue Prime model."

Focusing on free shipping over expedited shipping is a calculated move, as consumers in 2016 displayed a desire for free shipping over getting their packages quickly, Engel said. While Engel's figures show that orders using free shipping were up 1% year-over-year in 2016, orders using express shipping were actually down an average 55% in North America.

While Pier 1 CEO Thomas Toomey said on a recent earnings call that the company shifted a portion of its promotional spend away from discounts and towards shipping offers, Boot Barn CEO James Conroy pointed out on a recent earnings call that free shipping just erodes profitability a bit more.

Free shipping offers may not be a reality for all merchants, and that's not just because of promotional budgets or shipping costs. Merchants need to look deep into their operations and determine ways to keep their parcel shipping costs down.

Tim Parry is a freelance writer and a former Managing Editor of Multichannel Merchant. @RealTimParry