

Ring the register

Key growth strategies for retail CEOs

*Results of PwC Canada's
Retail Consulting Services
CEO Study (2011)*





Key findings

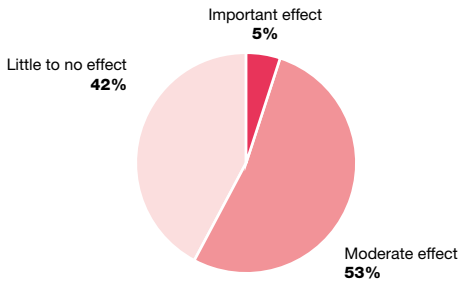
With the objective of understanding what steps retail CEOs are taking to drive profitable growth given the current economic environment, PwC Canada's Retail Consulting Services recently conducted a study of CEOs of 21 North American chain retailers in the specialty sector (90%) (including apparel, jewelry and footwear) and department store sector (10%). The study was conducted during October and November 2011.

The findings from these interviews and our comments based on our industry experience are not meant to be representative or projectable for the entire domestic or international retail market. Retailers will have to assess the merits of these findings in the context of their own personal circumstances.

Retailers are back in growth mode, despite economic conditions. Growth strategies are being driven by “organic” opportunities like international and e-commerce strategies versus the flurry of deal activity witnessed prior to the recession. Organic growth strategies that retailers are most focused on include international expansion, e-commerce solutions, and product and price innovation centered on private label and exclusive collections. Study respondents were increasingly focused on growth strategies that helped to differentiate them in a sea of sameness, thus providing a more compelling proposition for their customers to keep them coming back again and again in the quest for new and exclusive fashion and value.

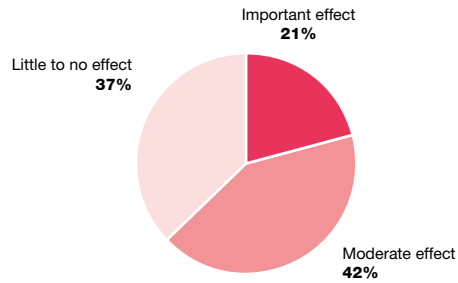
One hundred percent of the retail CEOs surveyed acknowledged that the real “game changer” is the move to seamless multi-channel integration that includes e-commerce, brick and mortar, m-commerce and social media. Some CEOs commented that “control has shifted from retailers and brands to the consumer” in this game changing paradigm.

Retail CEOs were asked to rank the impact of the following economic issues on their businesses.



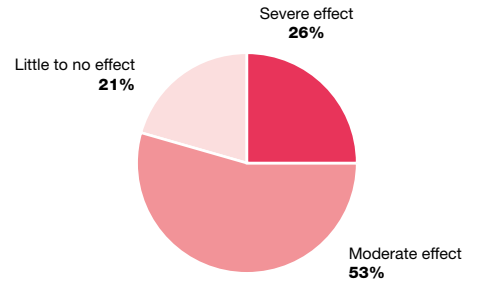
1. General Inflation, including gas

5% of retailers said general inflation, including gas prices, is having an important effect on their business, while 53% said it had a moderate effect, with 42% claiming it has little to no effect.



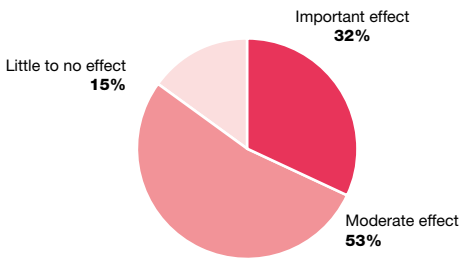
2. Higher product prices

21% of participating CEOs said higher prices for products their company sells have had an important impact on their business, while 42% said it had a moderate effect, with 37% claiming it has little to no effect.



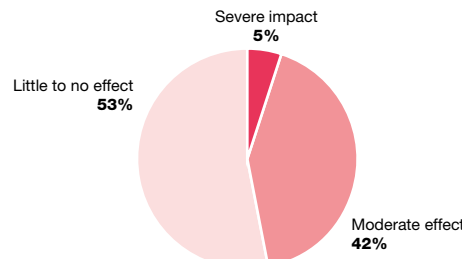
3. Unemployment

26% of retailers noted that unemployment has had a severe effect on their business, while 53% said it had a moderate effect, with 21% claiming it has little to no effect.



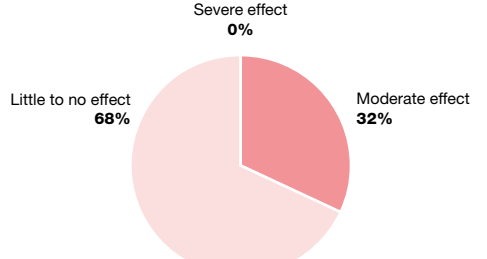
4. Consumer Confidence

32% of respondents said that consumer confidence has had an important effect on their business, while 53% said it had a moderate effect, with 15% claiming it has little to no effect.



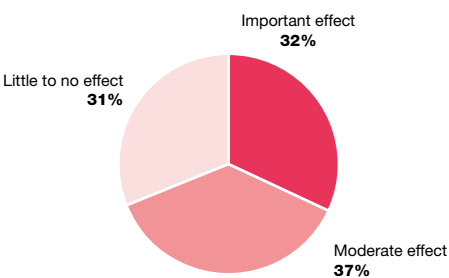
5. Stock Market Performance

5% of those surveyed said that stock market performance has had a severe impact on their business, while 42% said it had a moderate effect, with 53% claiming it has little to no effect.



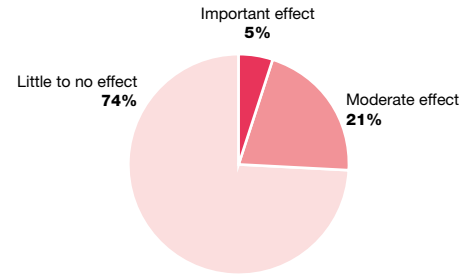
6. Government "gridlock"

None of the retailers surveyed said that government "gridlock" has had a severe effect on their business, while 32% said it had a moderate effect, with 68% claiming it has little to no effect.



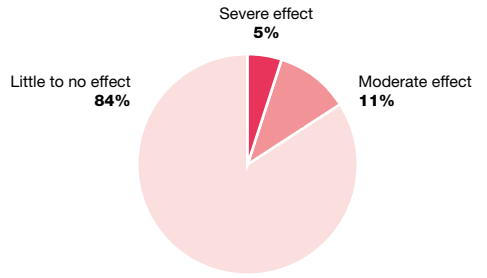
7. Housing Crisis

32% of retailers said that the housing crisis has had an important effect on their business, while 37% said it had a moderate effect, with 31% claiming it has little to no effect.



8. U.S. debt and deficit

5% of those surveyed said that the U.S. debt and deficit has had an important effect on their business, while 21% said it had a moderate effect, with 74% claiming it has little to no effect.



9. European debt and deficits

5% of respondents said that the European debt and deficit has had a severe effect on their business, while 11% said it had a moderate effect, with 84% claiming it has little to no effect.

Economic environment

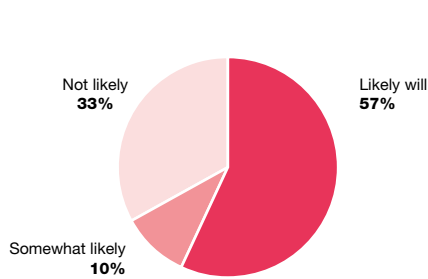
The CEOs indicated that the issues that impacted their businesses most severely were unemployment, consumer confidence and the housing crisis, with the combination of these factors having the most severe impact on sales. One CEO described the impact of consumer confidence as in the following, “if my customers don’t feel good, then they are going to spend much less money on apparel”.

The impact on businesses was particularly severe in markets where housing and construction was most impacted, such as Florida, Arizona and California. Interestingly, most retailers surveyed indicated that higher commodity prices and the weaker US currency – which led to increases in cost of goods sold and hence selling prices in the range of 4-10% – were reported as having had little impact on sales volumes for most retailers. Another CEO described the impact of this issue as being significant for his customer as “the

moderate customer does not have the ability any longer to refinance her home to finance retail spending as she has far less equity value in her home”. Retailers selling big ticket items on credit explained, “We are experiencing higher than usual credit decline rates and have had to develop more innovative credit strategies in order to mitigate the loss of that credit-dependent customer. While these strategies cost us and that customer segment more, the overall ROI was positive as we minimized the loss of that revenue.”

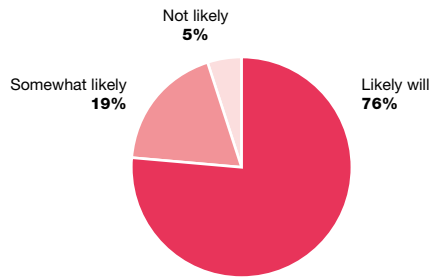


CEOs were asked to rate the following growth strategies as they relate to their business.



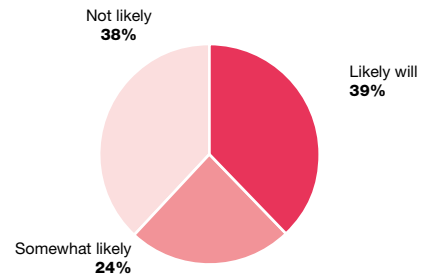
1. International Markets

57% of survey participants will increase penetration of international markets (either directly or through license or franchise partners) as part of their growth strategy, while 33% said they are not likely to do so, with 10% only somewhat likely to do so.



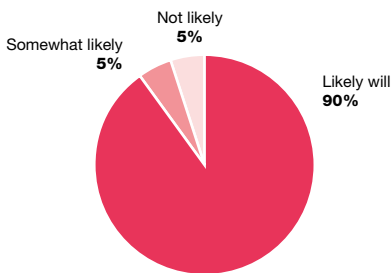
2. Stores

76% of retailers will likely introduce new stores or store concepts and/or undergo extensive store renovations as part of their growth strategy, while 5% said they are not likely to do so, with 19% only somewhat likely to do so.



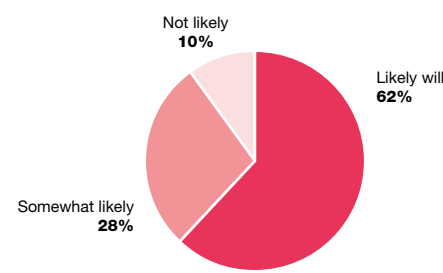
3. New brands/nameplates/divisions

38% of those surveyed will introduce new brands/nameplates/divisions as part of their growth strategy, while 38% said they are not likely to do so, with 24% only somewhat likely to do so.



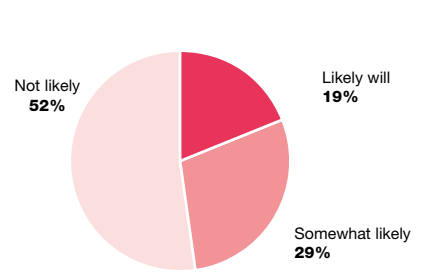
4. E-commerce

90% of respondents will increase their use of e-commerce as part of their company's growth strategy, while 5% said they are not likely to do so, with a further 5% only somewhat likely to do so.



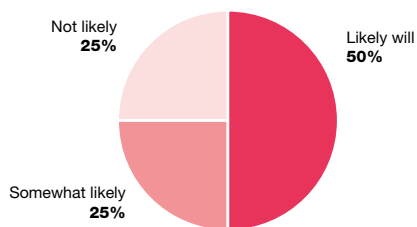
5. Social Networks

62% of retailers will increase their use of social networks as part of their company's growth strategy, while 10% said they are not likely to do so, with a further 28% only somewhat likely to do so.



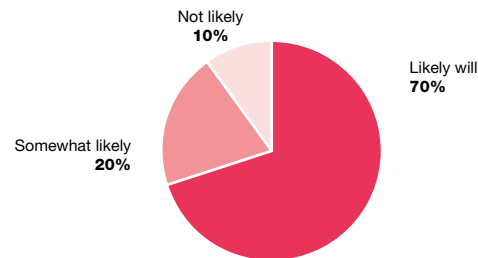
6. "Traditional" media

19% of survey participants will likely increase their offline marketing practices through "traditional" media as part of their growth strategy, while 52% said they are not likely to do so, with 29% only somewhat likely to do so.



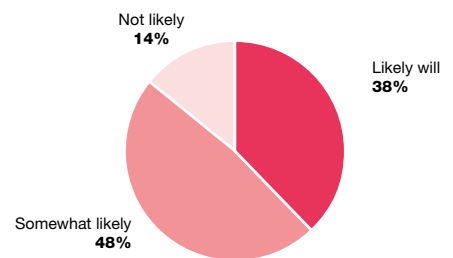
7. Merchandise categories

50% of those surveyed anticipate they will introduce additional merchandise categories as part of their growth strategy, while 25% said they are not likely to do so, with 25% only somewhat likely to do so.



8. Private label programs or exclusive collections

70% of respondents will increase their use of private label programs or exclusive collections as part of their growth strategy, while 10% said they are not likely to do so, with 20% only somewhat likely to do so.



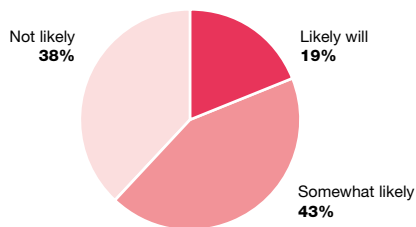
9. Higher-margin categories and lines

As many as 38% of survey participants will likely trade up to higher-margin categories and lines as part of their growth strategy, while 14% said they are not likely to do so, with 48% only somewhat likely to do so.

Growth strategies

Almost without exception, CEOs interviewed were very focused on top line growth of their businesses and had invested considerable effort in developing clear growth strategies.

International market expansion was a high priority for 57% of retailers surveyed, while e-commerce was a high priority for 90% of retailers surveyed. Greater use of exclusive merchandise collections as a key tool in increasing differentiation and in providing more value in the way each retailer's customer defined value was a priority for 70% of retailers. One CEO commented that "no retailer can be the best at everything. We believe in partnering with the best resources, whether as suppliers, licensee or joint venture, as a key pillar in our quest to provide a compelling reason for customers to keep coming back to our stores, rather than spending additional time on online websites. Customers will not keep coming back if there is nothing new or special in the store." While 19% of retailers surveyed enhanced their assortment strategy to include additional emphasis on opening price points, as many as 38% of retailers



10. Opening price points

Only 19% of survey participants will increase their emphasis on opening price points as part of their company's growth strategy, while 38% said they are not likely to do so, with 43% only somewhat likely to do so.

surveyed felt that was not a productive strategy unless customers considered low prices to be the value they were searching for.

Another CEO described "we are working tirelessly to replace commodity brands that can be found in numerous retailers and to fill our stores with exclusive fashion brands that the customer cannot get anywhere else, but at very compelling price points. We feel strongly that making sure we have the right brands and value of our merchandise is much more crucial than adding low cost opening price points."

For the most part, retailers surveyed added additional categories when they had identified gaps in assortment based on customer needs, not just to broaden assortments. E-commerce emerged as the highest priority, with 90% of those surveyed treating it as a key growth strategy.

The jury was out on social media. While 62% of CEOs surveyed said it was very likely they would increase investments in social media, there were mixed feelings on how and where the investments in this area would be made to drive ROI. Significant concerns were expressed by CEOs as to how to monetize investments in social media.

More than 50% of CEOs said they would not increase investment in "offline" marketing. While they continued to see TV, radio and newspaper brand marketing as important, many had shifted focus to database marketing to deepen share of wallet from existing customers, and to online marketing and social media.

Surprisingly, 76% of CEOs interviewed were increasing focus on investing in new store concepts, adding stores and more store renovation than in recent years. There was a lot of discussion about "brand refreshes" to enhance the way in which the brand would be articulated to their particular customers.

One CEO commented that "while it seems we are doing a lot more renovation this year, we are coming off of a three year cycle of little to no investment following the start of the recession in 2008, so we are still playing catch-up". Another said, "You cannot invest in everything. We know we are far behind in investing in e-commerce but we chose to invest in international expansion and it now makes up more than 15% of our business and we expect it to get to more than 33% in five years. For us, it is more important than e-commerce. We know it is likely different for many other retailers. Our brands extend well to certain international countries and we are very strategic as to where we are expanding, and so far it is working well for our business."

Retailers were asked how important acquisitions will be to their business in achieving their growth strategies.

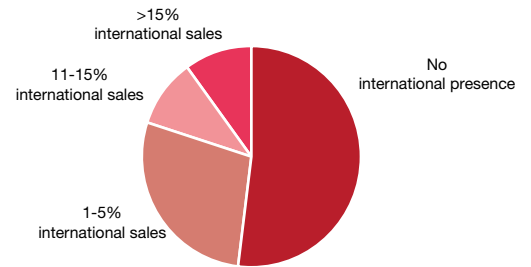
More than 60% of CEOs interviewed are growing organically, with less than 20% likely to grow by acquisition. Many of those who are planning to grow by acquisition are doing it opportunistically, by buying groups of stores out of bankruptcy or divestitures from other retailers, but only when the locations make sense for their customer base and are available at the right price.

- 19% of retailers felt acquisitions will be very important in achieving their company's growth target.
- 19% of retailers felt acquisitions will be somewhat important in achieving their company's growth target.
- 62% of retailers felt acquisitions will not be important in achieving their company's growth target.

International sales

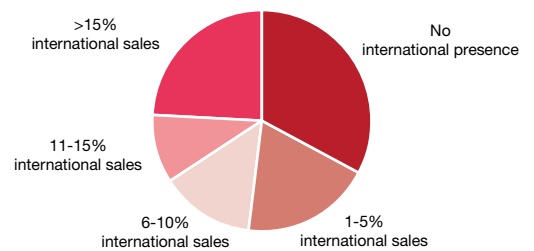
When asked how important international sales are and would continue to be to their businesses, CEOs responded in a very divergent fashion. While more than half of retailers surveyed have no international presence today, one third still expect to have no international presence in five years. On the other hand, 24% of retailers surveyed expect to have more than 15% of their sales coming from international markets in five years, up from 10% today. The retailers that indicated they would not expand internationally responded this way largely because the concepts were not sufficiently differentiated or transportable internationally and/or they felt they had significant available domestic expansion opportunities; and that international expansion would be a distraction with lower returns than domestic expansion.

For those retailers surveyed who are expanding internationally, there was a shift towards franchise or licensee models rather than employing their own capital internationally. These exceptions appeared to be in countries where such brand expansion was easier to manage.



Current international sales

- 52%** no international presence.
- 28%** 1-5% international sales.
- 0%** 6-10% international sales.
- 10%** 11-15% international sales.
- 10%** greater than 15% international sales.

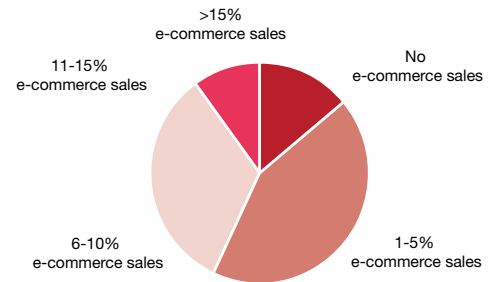


Projected International sales in five years

- 33%** no international presence.
- 19%** 1-5% international sales.
- 14%** 6-10% international sales.
- 10%** 11-15% international sales.
- 24%** greater than 15% international sales.

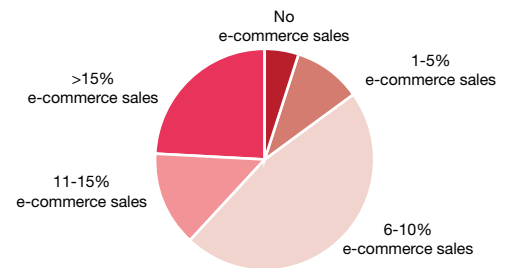
E-commerce

E-commerce is the single biggest growth driver for the majority of the CEOs interviewed as can be seen from the sharp increase in anticipated e-commerce sales relative to bricks and mortar stores below. Thirty-eight percent expect e-commerce sales to be in excess of 10% of total sales in five years, compared with 10% today. Current e-commerce growth rates for CEOs interviewed ranged from 5-20 times greater than bricks and mortar, with the greatest percentage gains coming from retailers whose e-commerce operations were less than five years old. Some CEOs commented that they were now looking at their different channels (stores, online and catalogue) in a more integrated manner than previously, when the channels had all been optimized individually. One interviewee commented, “Our websites are being revamped to reflect the synergies available to provide more seamless cross-channel shopping opportunities for our customers. We are also broadening assortments on our website and making more than 75% of our inventory available on our website as well as in our stores”.



Current e-commerce sales

- 14% no e-commerce sales.
- 43% 1-5% e-commerce sales.
- 33% 6-10% e-commerce sales.
- 0% 11-15% e-commerce sales.
- 10% greater than 15% e-commerce sales.



Projected e-commerce sales in five years

- 5% no e-commerce sales.
- 10% 1-5% e-commerce sales.
- 47% 6-10% e-commerce sales.
- 14% 11-15% e-commerce sales.
- 24% greater than 15% e-commerce sales.



Industry game changers

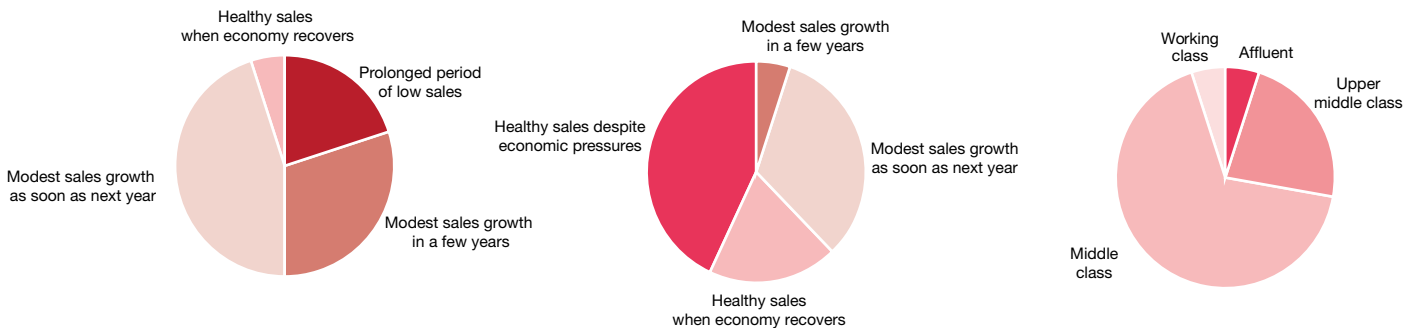
Ten years ago, e-commerce changed the way retailers do business. Retailers were asked what they see as the retail industry's future "game changers" and how they would effectively compete for the next generation of consumers growing up in a digital/mobile world.

One hundred percent of CEOs surveyed believed that seamless, easy cross-channel integration was the key game changer today and would continue for the next few years. Some CEOs commented that "control had started to shift from the brands to the consumer who now has the ability to research, browse, tweet, comparison shop, and transact and pay online while in the store and are now in the always connected paradigm, as opposed to when we want them to shop. Customers want the information and the solutions when and how they want it today and we have to give it to them." There was a strong feeling that mobile smartphones are going to change the dynamic of the retailer and the consumer significantly, with the consumer gaining much more control. Accessibility and understandability will be critical to this seamless cross-channel integration. More personalized, customized two way dialogues will become important to this digital, mobile customer generation.

Expectations

The results of this question were interesting; with most retailers feeling that the broader retail industry would grow modestly at best for the next 1-2 years, while feeling at the same time that their own company's sales and profits would grow at a healthy rate. It was challenging to determine if this was just optimism or whether this was rooted in reality. CEOs indicated that they had well defined tactical customer growth initiatives.

Customer demographics



Revenue expectations for the overall retail market over the next ten years

- 20%** a prolonged period of low or no sales gains and increased margin pressure.
- 30%** modest sales growth and margin improvement, but not for another few years.
- 45%** modest sales growth and margin improvement, as soon as next year.
- 5%** healthy sales and margin growth, but not until macroeconomic conditions improve in the general economy.
- 0%** healthy sales and margin growth, even as external financial pressures persist

Revenue expectations for the respondents own business over the next ten years

- 0%** a prolonged period of low or no sales gains and increased margin pressure.
- 5%** modest sales growth and margin improvement, but not for another few years.
- 33%** modest sales growth and margin improvement, as soon as next year.
- 19%** healthy sales and margin growth, but not until macroeconomic conditions improve in the general economy.
- 43%** healthy sales and margin growth, even as external financial pressures persist.

The typical customer of the surveyed retail CEOs

- 5%** affluent or wealthy
- 23%** upper middle class, "comfortable"
- 67%** middle class, "budget conscious"
- 5%** working class or unemployed, with a limited or fixed budget

For more information about our 2011 Retail CEO Study,
please contact:



Alain Michaud
.....
National & Eastern Canada
Retail & Consumer Leader
.....
514 205 5327
.....
alain.michaud@ca.pwc.com



Swati Patel
.....
GTA & Central Canada
Retail & Consumer Leader
.....
416 947 8292
.....
swati.patel@ca.pwc.com



Calle Johnson
.....
Western Canada Retail &
Consumer Leader
.....
604 806 7774
.....
calle.johnson@ca.pwc.com

The firms of the PwC network provide industry-focused assurance, tax and advisory services to enhance value for clients. More than 161,000 people in 154 countries in PwC firms across the PwC network share their thinking, experience and solutions to develop fresh perspectives and practical advice. In Canada, PricewaterhouseCoopers LLP, an Ontario limited liability partnership, and its related entities have more than 5,700 partners and staff in offices across the country. See www.pwc.com/ca for more information.

"PwC" is the brand under which member firms of PricewaterhouseCoopers International Limited (PwCIL) operate and provide services. Together, these firms form the PwC network. Each firm in the network is a separate legal entity and does not act as agent of PwCIL or any other member firm. PwCIL does not provide any services to clients. PwCIL is not responsible or liable for the acts or omissions of any of its member firms, nor can it control the exercise of their professional judgment or bind them in any way.

PricewaterhouseCoopers has exercised reasonable professional care in collecting, processing, and reporting of this information but has not independently verified, validated, or audited the data to verify the accuracy or completeness of the information. As such, PricewaterhouseCoopers gives no express or implied warranties, including, but not limited to, any warranties of merchantability or fitness for a particular purpose or use.

www.pwc.com/retail-consulting