Executive Summary

In virtually all of RSR's recent research, the evidence is compelling that the retail industry is at a critical "reset moment", the likes of which we haven't seen since the adoption of store-level barcode scanning in the 1980's. That technology-driven change was all about perfecting the mass merchandising model – and especially the supply chain. But this reset moment (which is also technology-driven – by virtue of the mass adoption of smart mobile) has forced retailers to service consumers’ new digitally enabled anytime/anywhere shopping behaviors. That in turn is causing retailers to think about how to move beyond a pure “push” oriented supply chain that assumes the store as the only destination for inventory.

Key findings

• Retailers understand that omni-channel customer behaviors are bringing new pressures on supply chain, but they have not fully connected the dots between their business challenges, like the changing pattern of consumer demand, and how their digital strategies impact these supply chain-driven challenges, for example, as digital channel growth remains a high priority.

• Retailers are reaching for the brass ring when it comes to their opportunities: targeting fulfillment from the most profitable location as their primary omni-channel fulfillment opportunity. However, without increased visibility across their network, their ability to achieve this goal is doubtful.

• While retailers acknowledge that major changes need to come to supply chain, they are not necessarily best-positioned to invent a new supply chain model, particularly when it comes to cross-functional involvement. For many retailers, there may be too much marketing involvement and not enough from the CFO.

• The largest retailers are looking to big technology investments to assist their supply chain transformations, but their smaller counterparts are under-estimating what technology - particularly in a cloud-enabled, third-party environment - can do for them.

BOOTstrap Recommendations

Addressing enterprise-wide inventory visibility is a prerequisite to true omni-channel enablement. Focus first on inventory “holes”, and work towards real-time updates of the perpetual inventory from transactional systems.

Fulfilling online demand in the stores must be considered as part of the forecast. Demand from the digital selling channels also affects store-level merchandise planning.

Realigning operational departments to be less channel specific is a smart tactic. But that means that line of business executives must collaborate more when it comes to designing the overall customer experience in an omni-channel context. The top supply chain executive should include Store Operations and eCommerce leaders, as well as the CFO, in developing the design for the next-generation supply chain.

Retailers must look beyond the logical “four walls” of the business when thinking about the supply chain, involving key trading partners in discussions about how to provide “endless aisle” assortments and drop-ship options to consumers.

Small and medium sized businesses need to look at commercially available on-demand supply chain solutions as an alternative to capital intensive investments in supply chain technology.
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Research Overview

Why Supply Chain Execution? Why Now?
Omni-channel is evolving and maturing. Retailers, as RSR discovered in our latest benchmark on omni-channel strategy, are turning from envisioning the future of digital-enabled shopping towards making that vision a reality.

However, for all the work that has been done, and for all of the future that has been envisioned, one particular function of the retail business has been held apart: the supply chain.

Changing the supply chain is time consuming, resource intensive, expensive, and risky. And though most retailers have grappled with how digitally-enabled consumer shopping behaviors are changing, most of what they have done to respond resulted in a thin layer of omni-channel veneer, and a supply chain unchanged - isolated and protected at all costs.

Like a pressure cooker locked down too tight, however, the forces acting on supply chain are only building greater pressure, from shifting consumer behaviors to demands for omni-channel service. And those forces won’t be easing up any time soon. While the retail supply chain has been designed and refined to serve one channel only - stores - most retailers are looking to other channels, channels that only increase retailers’ need to become more seamlessly omni-channel: retailers in this benchmark report that the primary channel of focus for future growth is eCommerce, followed by mobile. Stores take only third place on the list (Figure 1).

Figure 1: Eclipsing Stores

The more sales that are driven through digital channels, the more pressure there will be on supply chain to move away from efficient, store-oriented fulfillment towards flexible "buy anywhere/get anywhere" inventory strategies.

The net result? The retail supply chain as it currently exists was designed to support a cost structure and a business model that is rapidly becoming obsolete: a store-only model. Given the

Source: RSR Research, December 2013
supply chain’s relative isolation from omni-channel transformation to date, are retailers aware of the pressure that is building? Do they have a plan to address it? What might that plan be?

That is exactly what we set out to discover with this report.

**Defining Winners and Why They Win**

RSR’s research always focuses on a category of retailers we call “Retail Winners”. Our definition of Retail Winners is straightforward. We judge retailers by year-over-year comparable store/channel sales improvements. Assuming industry average comparable store/channel sales growth of **five percent**, we define those with sales above this hurdle as “Winners,” those at this sales growth rate as “average,” and those below this sales growth rate as “Laggards.” It is consistent throughout much of RSR’s research findings that Winners don’t merely do the same things better, they tend to do different things. They think differently. They plan differently. They respond differently.

**The Future Looms Larger for Retail Winners**

As we noted earlier, retailers generally report in this survey that their growth plans for the next three years will be shaped by eCommerce first, then mobile, then stores. But Retail Winners have a different priority - by far, they place more importance on mobile commerce (Figure 2).

*Figure 2: Doing More - A Winning Behavior*

The argument could be made that mobile commerce has seen small investments in the past, so to say that Retail Winners are focusing on it now as a priority is merely making up for lost time. However, whether this is true or not, mobile has a side effect: impact on stores. The first time stores saw consumers bring their smartphones with them to shop at the shelf, was the moment when the store operations team woke up to the reality of omni-channel - that activities online could not be isolated from stores. That stores could no longer remain isolated from the digital world.

And, as we will see in this report, Retail Winners are not prioritizing digital channels in a vacuum. Because they are working harder than their peers at building the connections between channels, they also see more clearly the impact these investments will have on the underlying infrastructure that makes omni-channel possible - most particularly supply chain.
Methodology

RSR uses its own model, called the “BOOT Methodology℠,” to analyze Retail Industry issues. We build this model with our survey instruments. Appendix A contains a full explanation of the methodology.

In our surveys, we continue to find differences in the thought processes, actions, and decisions made by retailers who outperform their competitors and the industry at large – Retail Winners. The BOOT model helps us better understand the behavioral and technological differences that drive sustainable sales improvements and successful execution of brand vision.

Survey Respondent Characteristics

RSR conducted an online survey from October-December 2013 and received answers from 84 qualified retail respondents. Respondent demographics are as follows:

- Job Title:
  - Executive/Senior Management (C-Level or VP) 36.8%
  - Middle Management (VP / Director / Manager) 39.5%
  - Individual Contributor 18.4%
  - Other 5.3%

- 2012 Revenue (US$ Equivalent)
  - Less than $50 Million 19.7%
  - $51 - $249 Million 9.8%
  - $250 - $999 Million 13.1%
  - $1 - $5 Billion 4.9%
  - Over $5 Billion 27.9%

- Products sold:
  - Fashion/Short Lifecycle 31.1%
  - Seasonal 9.8%
  - Basics/Replenished Items 16.4%
  - Durable goods 11.5%
  - Consumer electronics 18.0%
  - Perishable goods 13.1%

- Headquarters/Retail Presence:
  - USA 50.0% 55.3%
  - Canada 5.3% 34.2%
  - Latin America 2.6% 21.1%
  - UK 10.5% 18.4%
  - Europe 21.1% 39.5%
  - Middle East 2.6% 18.4%
  - Africa 0.0% 7.9%
  - Asia/Pacific 7.9% 28.9%
• Year-Over-Year Sales Growth Rates (assume average growth of 5%):
  Better than average (Retail Winners)  41%
  Average  38%
  Worse than average (Laggards)  21%
Business Challenges

The 3 C's of Supply Chain: Consumers, Consumers, and Competitors?

Retailers identify three primary business challenges facing supply chain these days: changing consumer expectations (primarily that consumers demand a more seamless experience), the impact of those changing expectations on the business (as their changing shopping patterns drive new demand patterns that retailers have to respond to), and finally, competitive pressure to get faster - faster order-to-delivery cycles, faster commit-to-ship cycles, even faster shipments (Figure 3).

Figure 3: Three Clear Challenges

None of these business challenges will ease up any time soon. But hidden in these priorities is the basic challenge of bringing supply chain into the overall omni-channel strategy: the cause and effect of all of these competing priorities. The pattern of demand has changed because for most retailers, digital channel growth outpaces store growth. Consumers expect retailers to provide a more seamless omni-channel experience - and a great deal of that experience means bringing more of the digital experience into stores, through capabilities like "endless aisle".

Retail Winners appear more likely to understand the interplay of these causes and their effects. They place the same order of priority on the business challenges impacting supply chain, but they are more broadly focused - the better to be able to understand the impact of cause and effect (Figure 4).
Figure 4: Consumer Expectations Impact Many Retail Strategies

Winners are more realistic than their peers, when it comes to the linkage between two particular areas - first, that consumer expectations will ultimately drive towards digital channel growth, which in turn will place new pressures on supply chain. And second, that while competitive pressures are forcing shorter order-to-delivery cycles, much of that expectation is being placed on the supply chain side of that cycle, rather than just focusing on trying to speed a shipment once it's out of the distribution center.

Among revenue bands, the smaller retailers (less than $250 million in revenue) stand apart from the rest of their peers: only 39% report feeling the pressure from consumer expectations, vs. 85% of those retailers with $1 billion or more in revenue. And small retailers place significantly more emphasis on expected changes to consumer behavior due to changing internet tax laws (31% vs. 0% of peers).

**Reality Check**
Retailers are expecting big changes as a result of new consumer shopping behaviors and competitive threats, but how ready are their supply chains to respond? Not very.

Sixty percent of respondents report that they provide direct to consumer fulfillment from a stand-alone DC today, the most widely implemented of all of the customer order fulfillment processes that we evaluated in this study. Outside of ship-from-store direct to consumer, which 49% of respondents reported as being implemented or in the process of rolling out, most every other capability had approximately one-third or less of respondents reporting the capability in place or even on its way (Figure 5).
What makes for an even more cautionary tale, however, is the number of disconnects that exist within this data. For example, retailers appear to be making a lot of progress fast in enabling ship-from-store (the 49% noted above), but only 37% report they have or are in the process of getting online visibility to in-store inventory. How can retailers confidently promise in-store inventory to customers if they can’t confirm that it’s really there?

Another disconnect: only 50% of retailers are convinced that ship-from-store is valuable vs. 74% who believe that picking in-store inventory for in-store pickup is valuable. And yet, 49% report ship-from-store in progress, vs. only 36% for in-store inventory for in-store pickup. And neither of these capabilities is truly possible without visibility into store inventory (which only 37% have in process). Retailers can’t reasonably promise what they don’t know they have in stock.

**When Supply Chain is a Differentiator - and When It Should Be**

Larger retailers ($1 billion or more in revenue) place more value than peers on some capabilities that one would expect to be typical to larger retailers over smaller, for example direct-to-
consumer fulfillment from a DC, online visibility into in-store inventory, and in-store inventory pick for consumer in-store pick-up. However, they also place much more value than smaller retailers on the ability to ship-from-store direct to consumer, in-store purchase for fulfillment from online distribution, and same-day shipping - all capabilities that smaller retailers, with their flexibility, could potentially value as differentiators, but for some reason don't (Figure 6).

**Figure 6: Small Services That Could Look Big**

<table>
<thead>
<tr>
<th>Order Fulfillment Processes</th>
<th>$1B+</th>
<th>$250M-$1B</th>
<th>Under $250M</th>
</tr>
</thead>
<tbody>
<tr>
<td>Direct to consumer fulfillment from our DC</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Online visibility into in-store inventory</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>In-store inventory pick for consumer in-store pick-up</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Same-day ship</td>
<td>33%</td>
<td>45%</td>
<td>62%</td>
</tr>
<tr>
<td>Ship from store direct to consumer</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Ship to store from &quot;Direct&quot; DC for consumer in-store pick-up</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>In-store purchase of online inventory for shipment direct to consumer</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Same-day delivery</td>
<td>33%</td>
<td>46%</td>
<td>55%</td>
</tr>
<tr>
<td>In-store reservation of inventory for consumer in-store purchase</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Store-to-Store transfer for pick-up in-store</td>
<td>0%</td>
<td>22%</td>
<td>38%</td>
</tr>
<tr>
<td>Drop ship from vendor direct to consumer</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Drop ship from vendor direct to store</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Source: RSR Research, December 2013

Smaller retailers are much more interested in enabling dropship from a vendor direct to consumer or to the store. At one level this makes sense - smaller retailers won't have the leverage with the vendor or the physical space to carry the full line that a vendor might offer. Dropship theoretically allows a small vendor to offer a breadth of line without all of the inventory risk. But smaller retailers should also be more flexible than their larger peers, and they won't have the scale to negotiate favorable shipping rates from a direct to consumer distribution center, which means that
ship-from-store should be easier to deliver, without much more incremental shipping costs than what they already offer consumers.

Why wouldn’t smaller retailers pursue services like ship-from-store that larger retailers struggle to offer, not only from a process perspective, but also from a cost perspective? It appears that smaller retailers are thinking like large retailers in anticipating costs, without thinking through the differentiating customer service benefits.

**Breaking Out of Traditional Thinking**

The biggest business challenge of supply chain these days is old-school, traditional thinking. Classic supply chain concepts like the bullwhip effect or multi-echelon optimization don’t need to be tossed out the window with the arrival of omni-channel retailing. However, these concepts have in the past been developed to solve only one retail problem: getting inventory from a source to a store. After that, home delivery services for big ticket items aside, it was mostly up to marketing to get it from the store to the consumer's home.

Not including online visibility to in-store inventory, there are eleven ways to get merchandise from a source to a consumer listed in Figure 6, above. And that list is by no means exhaustive. Marrying eleven-plus ways to fulfill an order in an omni-channel world together with a supply chain designed to move product in one direction only is a monumental challenge - it’s no wonder retailers have avoided this challenge for as long as possible.

The bad news: transforming supply chain may very well be as painful and expensive as retailers worry that it will be. The good news: the retailers who successfully navigate this transformation will not only enjoy flexibility and speed advantages at a competitive cost of business, they will have developed key differentiating services and offerings for their customers, as we will explore in the next section.
Opportunities

Connecting the Dots Part 1: The Opportunities

This study finds that retailers’ top three opportunities for supply chain to contribute to the success of their omni-channel businesses are: optimize fulfillment based on the most profitable inventory opportunity, redesign the supply chain to be more cross-channel, and improve cross-channel forecasts. But the differences by performance are significant (Figure 7).

Figure 7: Different Pains, Different Priorities

Lagging retailers' top priority is to redesign their supply chain to be more cross-channel. But what does that really mean? Ideally, they would like to optimize fulfillment based on the most profitable location, but only half as many Laggards as Winners also identified rethinking how revenue and costs are allocated in cross-channel fulfillment - a key component of understanding the most profitable location. Laggards are also more than twice as likely as Winners to rate smaller, more localized inventory footprints in stores as an opportunity, but Winners are half as more likely to prioritize re-optimizing warehouse flow between store and eCommerce order profiles - something that would seem to be an important first step on a journey to smaller inventory profiles in stores.

Source: RSR Research, December 2013
Winners are taking what appears to be a more sensible approach to prioritizing opportunities: their number one objective is to prioritize fulfillment based on the most profitable location. Right behind that priority, they realize they must understand the costs involved in how they source inventory today. Consistent with their awareness of the need for speed as a supply chain business challenge, they are also turning to more forward stocking locations to enable faster fulfillment, and right alongside that goal, they know they will need to re-evaluate how they forecast in order to accommodate a more distributed fulfillment network.

The fascination with more local distribution centers is driven primarily by larger retailers - 44% of retailers with $1 billion or more in revenue, vs. 14% of mid-sized retailers and 23% of smaller peers. Anecdotally, this appears to be a direct reaction to the competitive threat of Amazon. And while much has been made in the public domain about the opportunity for stores to serve as "already built" local distribution centers, the reality is that store-based retailers have not fully determined if stores alone will be enough. They may need their own investments in local distribution in order to make competing against Amazon in speed of fulfillment a reality.

**Connecting the Dots Part 2: The Process Gaps**

When it comes to operational challenges, retailers' top three challenges are: the supply chain is not designed for current or projected volumes of direct-to-consumer shipments, current warehouse flow is not optimized for current or projected volumes of direct-to-consumer shipments, and what to do with online inventory returned to stores.

But as with the opportunities, we see enormous differences by performance (Figure 8, below). Both Winners and Laggards agree that supply chain is not designed for current or future volumes of direct-to-consumer shipments. But Laggards appear frozen in panic mode - they are the primary driver for making "warehouse flow issues around current or future volumes of direct-to-consumer shipments" such a highly rated challenge. They also fret more about what to do with online inventory returned to stores.

Winners have very different priorities when it comes to acknowledging and grappling with their operational challenges, and their priorities fall directly from the opportunities they perceive. Yes, their supply chain is also not designed for current or future volumes of direct-to-consumer shipments, but next on their list is to rethink their forward positioning of inventory. This ties to their reported challenges around increasing the speed of their consumer order-to-fulfill cycles, as well as the need to respond to competitive speed - which they acknowledge by placing "direct to consumer shipments are not fast enough" third on their list.

Near the bottom of Winners' list of challenges is dealing with online inventory returned to stores. While no one wants to write that inventory off, at the same time anecdotal evidence supports that retailers who make it easy for consumers to return to store - no matter where the inventory came from - are gaining offsetting benefits, by driving incremental traffic to stores that result in incremental spend.
Figure 8: Panic vs. Reaction

<table>
<thead>
<tr>
<th>Top 3 SCE Operational Challenges</th>
<th>Winners</th>
<th>Others</th>
</tr>
</thead>
<tbody>
<tr>
<td>Our supply chain is not designed for the current/ projected volume of direct-to-consumer shipments</td>
<td>44%</td>
<td>50%</td>
</tr>
<tr>
<td>We need to rethink our forward positioning of inventory to compete with online pureplays</td>
<td>27%</td>
<td>39%</td>
</tr>
<tr>
<td>Direct to consumer shipments are not fast enough</td>
<td>27%</td>
<td>39%</td>
</tr>
<tr>
<td>We don’t have good visibility into how demand flows through our selling channels</td>
<td>23%</td>
<td>33%</td>
</tr>
<tr>
<td>Tracking labor &amp; shipment costs across cross-channel fulfillment</td>
<td>13%</td>
<td>33%</td>
</tr>
<tr>
<td>Current warehouse flow is not designed for current or future volumes of direct to consumer shipments</td>
<td>22%</td>
<td>33%</td>
</tr>
<tr>
<td>Marketing promotions cause unintended consequences on supply chain</td>
<td>17%</td>
<td>0%</td>
</tr>
<tr>
<td>What to do with online inventory returned to stores</td>
<td>22%</td>
<td>43%</td>
</tr>
<tr>
<td>We haven’t figured out how to align incentives for sales credit for cross-channel sales.</td>
<td>22%</td>
<td>27%</td>
</tr>
<tr>
<td>Pressure from store operations to prepare “shelf-ready” shipments that cut store labor requirements</td>
<td>0%</td>
<td>13%</td>
</tr>
</tbody>
</table>

Source: RSR Research, December 2013

Connecting the Dots Part 3: The Results

When the perceived opportunities are combined with the operational challenges, what is the net result on retailers' inventory strategies? In past supply chain and merchandising research, RSR predicted that as retailers adjusted their local store inventory profiles, both to try to capture some of the inventory leverage opportunities that omni-channel fulfillment offers as well as to adjust the assortment to be more localized, there would be natural pressure to increase inventory - to carry a shallower depth of a broader range of SKUs.

That appears to be coming to pass. Both Winners and Laggards now struggle with a double-whammy of too much slow-moving inventory and too many out of stocks (Figure 9, below). It's bad to be out of what's selling, and it's probably worse to be overstocked in inventory that is not selling. But both problems at the same time means the money that might have been spent to stock back into what's selling is trapped in the inventory that isn't moving.
The big difference between Winners and Laggards is that Winners are more likely to be able to see where their inventory plans have gone wrong. While more than half of Winners still report struggling with inaccurate inventory in stores, that's nothing compared to Laggards' 74%.

However, given Laggards' lack of interest in visibility noted above, this outcome can hardly be unexpected. Laggards report being challenged by issues that visibility plays a critical role in solving, but at every level - the business challenge level and the opportunity level - visibility takes a back seat to responding to the latest fire or competitive threat.

Visibility is key to retailers' ability to actually enable the kinds of omni-channel fulfillment processes they see as opportunities. But "visibility" is a very broad topic - where are the real gaps?

We asked retailers to specifically identify the types of visibility that are valuable to them, as well as how much of each type of visibility they actually have. The results continue to tell a tale of poor visibility.

System-wide visibility - the broadest kind - is not surprisingly the most valuable. But less than half of respondents report that they have "a lot" of system-wide visibility (Figure 10, below). DC available inventory - where inventory is theoretically the easiest to keep accurate - is where visibility is greatest.
Retailers reported that their top opportunity was to fulfill inventory from the most profitable location. But according to the findings in Figure 10, the only place they have relative confidence in their inventory visibility is in the DC. Retailers have some confidence in store inventory levels, but only 25% of respondents have shelf-level visibility within the store - a key component of in-store pick for in-store pick-up. The direct side of the business is no better: less than half of respondents report that they have a lot of visibility into the online channel's available inventory.

**Visibility: The Opportunity That Enables All Others**

The good news is that under those averages, some progress is being made - primarily by Retail Winners. Winners and their peers track well in achieving a lot of visibility for DC available inventory, and even system-wide visibility and inbound to DC inventory, though at much lower rates. However, Winners are pulling away in two notable locations: store inventory levels, and online channel available inventory. If retailers hope to achieve "profitable promising" of inventory to consumers, no matter where it might be located, visibility into those locations where inventory is stored will have to improve. Winners appear to be taking a step-wise approach - overall store inventory before shelf-level, for example, but at least they are working the visibility problem.

Resolving the organizational and process issues that increased visibility will undoubtedly raise - that is a different topic altogether.
Organizational Inhibitors

The problem inherent in any proposition to redesign the supply chain is that the best retailers’ profitability is closely tied to the operational excellence of the supply chain. Whereas the right assortments, prices, and promotions are keys to triggering top line revenue, cost of goods is the next biggest variable in generating the gross margins needed that pay for retailers’ operations while still delivering something to the bottom line. It is for this reason that the legacy supply chain design has moved from merely being a challenge to omni-channel enablement to becoming a true inhibitor to moving forward in an omni-channel world. The question is not so much can consumer demands for multiple fulfillment options be met, but can they be met profitably? That’s the big “if”.

In RSR’s 2012 study on supply chain execution, we saw that the top organizational inhibitor to retailers’ aligning the supply chain to new omni-channel selling capabilities was a supply chain design that is not optimized for omni-channel fulfillment (55%). In this year’s study that stumbling block has come much more into focus – now 63% of responding retailers say that’s their #1 organizational inhibitor to making progress on the challenges and opportunities they see. What that means comes much more clearly into focus when we examine the other highly ranked inhibitors. Whereas “lack of confidence in inventory accuracy” rated as a top inhibitor for only 19% of respondents last year, this year the response more than doubled (44%). That doesn’t mean that perpetual and actual inventories are hopelessly out of sync however; only 19% of retailers in this study indicated that as a problem. It goes back to “visibility” – while local inventories might be well managed locally, the lack of visibility across the enterprise to fulfill cross-channel orders has become a major issue.

Facing Up To Reality

When examining top organizational inhibitors, there are two stories; Winners know they need to change, while their lesser-performing rivals are still trying to figure out if such a big change is inevitable (Figure 11, below). While the overall response shows that “a supply chain design that is not optimized for omni-channel fulfillment” is the top inhibitor to an effective to omni-channel strategy, Retail Winners see that most clearly (40% more than others). Winners also have much more clarity about other stumbling blocks than do average and lagging performers. For example, over twice as many over-performers as others indicate that they don’t have the right metrics or incentives in place to measure cross-channel performance. On the other hand, almost 20% fewer Winners are worried that they don’t have top-level support to drive a cross-channel strategy.

So, many Winners have the leadership focus, and they are very aware of the need to change – and that in order to act effectively they need to put metrics in place to help determine the scope and impact of those changes. For others there still seems to be a question of “if” the challenges can be met.
Mid-Tier Stress

Earlier in this report, we observed that retailers with less than the equivalent of $1B in annual revenues are struggling to see the value associated with certain omni-channel processes. Why that is comes into more focus when we asked them to identify top organizational inhibitors (Figure 12, below). To start, mid-tier retailers feel much more strongly that their current supply chain design stands in the way than even Winners do (86% compared to 75%). But they also identify a big roadblock to addressing that issue; mid-tiered retailers feel most strongly that lack of coordination between supply chain, merchandising, and marketing is a top inhibitor (survey responses show that this is particularly true for fast moving consumer goods and general merchandise retailers).

This finding is important because a key to omni-channel success is for key line-of-business (LOB) leaders to work together to design a consistent customer shopping experience across the enterprise. Left to their own devices, line of business executives will fall back to what they know has worked in the past. For the supply chain executive, that means procuring and distributing product in the most efficient way possible, sacrificing needed flexibility in the process. Mid-tier
retailers apparently see these two inhibitors in a kind of “deadly embrace” – the supply chain is not designed to meet emerging requirements, but the line of business executives that could address the issue don’t work every well together. And although the mid-tier feels less strongly than their competitors that “top level support for a cross-channel strategy” is an issue, that support apparently doesn’t extend to the supply chain.

Figure 12: The Mid-Tier Lament

<table>
<thead>
<tr>
<th>Top Inhibitors By Tier</th>
<th>Overall</th>
<th>$250M-$1B</th>
<th>$1B+</th>
</tr>
</thead>
<tbody>
<tr>
<td>Our supply chain is not designed to support omni-channel fulfillment</td>
<td>63%</td>
<td>68%</td>
<td>86%</td>
</tr>
<tr>
<td>Lack of coordination between supply chain, merchandising, and marketing</td>
<td>42%</td>
<td>44%</td>
<td>57%</td>
</tr>
<tr>
<td>Lack of confidence in inventory accuracy</td>
<td>44%</td>
<td>43%</td>
<td>40%</td>
</tr>
<tr>
<td>We don't have the right metrics or incentives to measure cross-channel supply chain efficiencies</td>
<td>28%</td>
<td>29%</td>
<td>28%</td>
</tr>
<tr>
<td>Lack of active top-level support for a cross-channel strategy</td>
<td>29%</td>
<td>35%</td>
<td>40%</td>
</tr>
</tbody>
</table>

Source: RSR Research, December 2013

Where Winners Really Stand Out
If the notion is accurate that the entire industry – Winners and Laggards and everyone in between – is at a pivotal “reset moment”, then it stands that no one performance group can claim to have it all figured out. Today’s Winners could be tomorrow’s Laggards if they don’t see the need to change, and visa versa. While this study clearly shows that most retailers are in the same boat when it comes to realignment of the supply chain to serve an omni-channel selling environment, it also shows that Winners are far more sensitive about the need to do something about it.

And so it’s no surprise that Retail Winners are far ahead when it comes to remediating today’s organizational inhibitors (Figure 13, below).
Very clearly, Winners see that viewing the omni-channel agenda as either a customer-facing or a supply chain issue, isn’t enough. They understand that it’s about the whole operational model – how they plan, buy, sell, and manage their businesses. Winners also better understand that one key to operating in this new consumer-driven environment is metrics and incentives. When it comes to metrics, Retail Winners know that they can’t afford to ignore signals coming from consumers themselves in their digitally enabled paths to purchase, to respond quickly when consumers demand it – and to do it profitably. As to incentives, it’s the old adage – “you get what you pay for”. More Winners than others understand the importance of the right incentives - although it’s clear from the data that more retailers of all stripes need to pay attention to how employees are incentivized to support omni-channel execution.

Average and under-performing retailers, on the other hand, are looking for a champion – they want the top of the company (presumably the CEO) to “make it so”. This result reflects what we
saw earlier regarding organizational inhibitors – Winners aren’t worried about top-of-company support, but other retailers are.

**A Particularly Tough Sell?**

Not everyone agrees that a fundamental realignment of the supply chain to be non-channel specific is a great idea. Specifically, many of those retailers who sell fast moving merchandise – food and basics - show much less interest in pursuing that approach than the overall response group (Figure 14). These retailers’ supply chains are highly verticalized, built for maximum efficiency and speed.

*Figure 14: Seeing The Issues Differently*

![Chart](image)

Overcoming Inhibitors - Food & Basics

Source: RSR Research, December 2013

But while food & basics merchants don’t place nearly as much emphasis on realigning the supply chain to enable cross-channel fulfillment, they aren’t tossing out the idea of cross-channel *ordering*. They just want to see an ROI for the proposal. And, these retailers are more interested than the general response group and Winners in improved analytics that will help them monitor supply chain activity and respond to real-time conditions.
The bigger question for these retailers might be, how to service direct-to-consumer and online orders for in-store pickup? The answer to that comes into focus when we go back and examine their view of the overall challenges and opportunities associated with omni-channel. Food & basics retailers feel more strongly than any other group that consumers expect retailers to provide a more seamless omni-channel experience (81% compared to 67% overall), and that one way to respond to that expectation is with more forward inventory locations for same-day delivery (44% compared to 34% overall) as well as with greater investments in mobile/m-commerce (78% compared to 70% overall).

In other words, many food & basics retailers don’t foresee an opportunity to fulfill customer orders from geographically distant locations. Instead they see the probability of consumers ordering online for local pickup in a store or direct delivery from a nearby local fulfillment location. While that may trigger a re-think of inventory visibility and omni-channel order management, it doesn’t necessarily trigger a fundamental change in the overall physical supply chain design.

**Who’s Driving This Thing?**
To no great surprise, the VP of Supply Chain is the top influencer for supply chain decisions today, but our respondents want to see more line of business executives involved (Figure 15).

*Figure 15: More Cooks In The Kitchen*

The Supply Chain executive has the biggest say by far in decisions that effect S/C design and performance, but our survey respondents clearly feel that the head of Store Operations or COO should have as much influence, and that the VP of Merchandising, eCommerce head, and (significantly) the CFO should be involved as well. However, the VP of Marketing should have less influence, according to our survey takers. This response may be reflective of the current state of affairs. For many, the CMO is “the new kid on the block” and is having a lot of influence.
over the overall omni-channel strategy discussion. But in the end, the CMO’s role is demand generation and customer acquisition/retention, while the others have to (quite literally) deliver the goods. Our survey respondents want more of the executive team involved in next-generation supply chain design. In this context, the emphasis on the CFO is interesting and appropriate; supply chain is where “profitability” comes from, and challenges to it threaten profitability. So our respondents seem to be saying, "let’s make sure that the decisions we make about supply chain alignment help ensure our future financial too!"
Technology Enablers

The omni-channel agenda, at its essence, is all about the speed with which information can get to the people who want or need it. In the case of consumers, it’s about getting access to content about products and services available and community feedback about those choices. For the marketing executive, it’s about getting the right value message to the right consumer at just the right moment. For store employees, it’s all about getting up-to-the-second information about the customer’s context in order to assist in the sale. And for the supply chain, it’s all about how well supply is meeting demand in the real world, as it’s happening. And where it’s happening.

Nowadays, virtually all information is digital. So the technology overlay to the physical supply chain is vital to retailers’ ability to manage the flow of goods, even in fairly small operations. For big organizations, it’s absolutely central to the strategy.

Bigger and Better?

Earlier in this report, we made the point that if retailers hope to achieve “profitable promising” of inventory to consumers, then visibility to those locations where inventory is stored will have to improve. In this study, big retailers (those with greater than the equivalent of $1B in annual revenue) clearly are saying that they plan to invest to make that kind of visibility real. But whereas larger retailers have achieved a high level of visibility to DC inventory, they have been much less successful in achieving store level visibility (Figure 16). And (perhaps surprisingly), big retailers in particular show an inability to see “enterprise-wide” inventory visibility, even if they can see DC and store inventories separately.

*Figure 16: Impaired Vision*

<table>
<thead>
<tr>
<th>Types of Supply Chain Visibility</th>
<th>$1B+</th>
<th>$250M-$1B</th>
<th>Under $250M</th>
</tr>
</thead>
<tbody>
<tr>
<td>DC available inventory</td>
<td>80%</td>
<td>63%</td>
<td>67%</td>
</tr>
<tr>
<td>Store inventory levels</td>
<td>60%</td>
<td>44%</td>
<td>56%</td>
</tr>
<tr>
<td>Online/Direct channel available inventory</td>
<td>56%</td>
<td>44%</td>
<td>44%</td>
</tr>
<tr>
<td>Inbound to DC inventory or orders</td>
<td>60%</td>
<td>38%</td>
<td>56%</td>
</tr>
<tr>
<td>System-wide inventory visibility</td>
<td>67%</td>
<td>36%</td>
<td>56%</td>
</tr>
<tr>
<td>Inbound to store inventory or orders</td>
<td>50%</td>
<td>33%</td>
<td>56%</td>
</tr>
<tr>
<td>Store on-shelf inventory levels</td>
<td>28%</td>
<td>33%</td>
<td>33%</td>
</tr>
<tr>
<td>Visibility into vendor dropship inventory</td>
<td>13%</td>
<td>8%</td>
<td>0%</td>
</tr>
</tbody>
</table>

*Source: RSR Research, December 2013*
It stands to reason then that big retailers see the value of enterprise-wide visibility most clearly, and that is exactly the case (Figure 17). These retailers put the greatest value on two things: real-time updates to inventory from transactional systems and enterprise-wide inventory visibility. Although the two aren’t necessarily related, taken together they help to deliver real-time visibility across the entire enterprise – the best-case scenario for companies that want to be able to commit products to sell without either the risk of over-inventoring or customer dissatisfaction from out-of-stocks, or (worse yet) backorders.

**Figure 17: Winners Have a Different Value Emphasis**

More of the larger retailers also see value in advanced sourcing algorithms for locating the optimal inventory for customer order fulfillment. So not only do the big retailers see value in real-time inventory updates and visibility across the enterprise to enhance their ability to commit to

<table>
<thead>
<tr>
<th>Technology Investments: Value</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Real-time updates to inventory from transactional systems</strong></td>
</tr>
<tr>
<td><strong>Enterprise-wide inventory visibility</strong></td>
</tr>
<tr>
<td><strong>Distributed order management/customer order management</strong></td>
</tr>
<tr>
<td><strong>Cross-channel specific supply chain analytics</strong></td>
</tr>
<tr>
<td><strong>Sourcing algorithms for locating the optimal inventory for customer order fulfillment</strong></td>
</tr>
<tr>
<td><strong>Store perpetual inventory management</strong></td>
</tr>
<tr>
<td><strong>System-based methods of capturing missed sales opportunities due to local out of stocks</strong></td>
</tr>
<tr>
<td><strong>Parcel shipping management systems to identify real-time customer shipping costs</strong></td>
</tr>
<tr>
<td><strong>Employee-facing mobile devices for assisted selling and order capture and fulfillment in stores</strong></td>
</tr>
<tr>
<td><strong>Supplier drop-ship management system</strong></td>
</tr>
<tr>
<td><strong>Item-level RFID</strong></td>
</tr>
</tbody>
</table>

Source: RSR Research, December 2013
sell, they also see value in fulfilling in the most profitable way (and using technology to guide them in that goal).

What About SMBs?
Omni-channel supply chain doesn’t have to be a “big boy’s” game, but that is hard to tell from responses in this survey. SMB (small and medium business) retailers (those with less than the equivalent of $250M in annual revenue) don't see nearly as much value in technology enabled omni-channel supply chain capabilities as do their larger competitors. As a matter of fact, only one (parcel shipping management systems) is clearly favored by SMBs more than other respondents.

Why is this? Whereas supply chain automation and optimization may have been the exclusive domain of retailers who could afford expensive technology solutions in the past, nowadays there are a number of credible on-demand solutions available at reasonable cost, and virtually no capital requirements. It may be as simple as this: SMBs are the most disaggregated of all retail segments, and getting information to them about available and affordable technology options is very difficult. But to borrow a phrase, “there’s a lot of money being left on the table”. More than that, “service and selection” – the very things that made it possible for SMBs to thrive in the days of the 20th Century channel masters, now can be made available to anyone in the digital domain. And that means that big retailers can and probably will be able to offer that kind of differentiated value too.

Easier Said Than Done
As Figure 18 (below) shows, retailers overall have a long way to go to match the reality to the perceived value of technologies to support an omni-channel strategy. As expected, enterprise-wide visibility is top-of-mind and top-of-spend. At the other extreme, RFID continues to languish, the result of the industry-wide black eye it got in the mid-2000’s from all the hype associated with case-pack and pallet tagging.

Interestingly, Winners fare significantly better in the “Implemented/Rolling Out” column with a couple of capabilities – “Distributed order management/customer order management”, (50%), and “Parcel shipping management systems” (36%). This is indicative of the “newness” of the omni-channel supply chain challenge – it’s a whole new game.
Summing It Up

While retailers may agree that it’s a whole new omni-channel world, what that means from a technology perspective hasn’t necessarily been thought through. Not only does buy anywhere/get anywhere challenge the traditional operational model, it also challenges traditional notions of the technology portfolio. There are many ways to reduce the “friction” that exists between operational systems that interact with each other at the data level. Some retailers may find it more expedient to move from batch-style updates between distributed transaction systems, while others choses to “re-centralize” key databases to enable 360° of visibility. Still others may choose to use commercially available on-demand solutions to replace some or all of their legacy systems.

However, the key point is that “visibility” is the prerequisite to success for an omni-channel selling company, for inventory, customer, and product information. And for supply chain, it all starts with knowing where inventory is, in something approaching real-time. As this study reveals, there are no real Winners or Laggards yet – the competition has just begun.
BOOTstrap Recommendations

While there’s a tremendous amount of focus right now on the customer-facing side of the retail operational model, retailers are only beginning to think about the implications of buy anywhere/get anywhere retailing on the supply chain side. The fundamentals still are the same – retailers need to match supply with demand in a way that builds sales and profitability. What has changed is that “demand” (the customer) will not necessarily go to where the supply is. The “supply” must also be able to go to where the customer is – and that challenges some of the most basic assumptions built into the push-oriented legacy retail operational model.

While it’s still early days, Winners are (once again) showing the way for the industry to follow. This study highlights some of those ways:

You Can’t Drive If You Can’t See

Winners are leading the way in developing two important capabilities: enterprise visibility into store inventory levels and online channel available inventory. These are essential in order to achieve "profitable promising" of inventory to consumers. But retailers don’t have to “boil the ocean” – a step-wise approach will help your company to get started:

• Focus first on where your inventory holes are, for example shelf-level in the store
• Work towards something approaching real-time updates from transactional systems to the perpetual inventory (if technology constraints prevent true real-time, think about intra-day exchanges of data)
• If accuracy isn’t good enough for 100% “commit to sell”, think about “minimum available to sell”
• RFID? The technology seems to be an almost perfect fit for omni-channel if it’s directed toward in-store accuracy, and it is showing great promise in apparel. But other priorities come first.

Digital Channel Growth Needs To Fold Into Planning

Those large percentage increases on a small base of cross-channel activities are about to start adding up to real inventory challenges. For example, the U.S. Department of Commerce estimates that 94.5% of all retail sales still happen in a store (2012) but that's down from 98% just a few years ago. And that doesn’t gauge activities like buy online/return in-store. As the shift piles up, fulfilling online demand moves from a rounding error in store plans to something that must be forecasted and managed on its own. And forecasting demand for online is not as simple as treating the channel as a flagship or extra-large store - demand comes from a much larger base of consumers spread across a much larger geography than any store ever must accommodate. Planning merchandise in that situation is far more complex than the already complex requirements for planning at individual store levels.

Bring in the additional complications of demand coming through one channel yet fulfilled by another channel, and planning for demand becomes even more complex - retailers have not even begun to scratch the surface of the implications of new types of fulfillment on merchandise planning.
**Organization & Process First, Technology Second**

Winners don’t see the omni-channel agenda as either a customer-facing or a supply chain issue, it’s about the whole operational model. To that end, they favor realignment of operational departments to be less channel-specific. They also know that keys to operating in this new consumer-driven environment are new metrics and realigned incentives.

Overall respondents to this study express a strong desire for more of the executive team to be involved in defining the next-generation supply chain design, and not leaving it to the top Supply Chain executive. That makes sense, and aligns well to RSR’s advice about addressing omni-channel retailing – design the total Brand Experience across all channels, and then determine the impact to line of business operations to support the new design.

Once those operational impacts have been determined, then address technology enablers.

**Get Used To Thinking “Outside The Box”**

Buy anywhere/get anywhere isn’t just about the consumer experience, it’s an opportunity to rethink the entire supply chain. It's about whether you can get to every available inventory item in your entire system, whether at a trusted vendor, in a returns process, in a shipment to a DC or on a shelf. Yes, this requires giving up some supply chain efficiency in the short term, which Retail Winners have already agreed is an important priority. However, when it comes to supply chain transformation, true Winners will have two key elements to their supply chain capabilities: total flexibility to reach into any inventory anywhere in the supply chain, delivered at costs comparable to the highly efficient supply chains of today.

**Everyone Can Play**

What many retailers, particularly in the SMB space, don’t seem to realize is that there are many technology options open to them that didn’t exist even five years ago. Net-native commercial solutions sidestep traditional capital requirements and in-house technology expertise requirements. This is as much a to-do for the technology community as it is a “learning” for retailers – everyone has a play.

But it is also important for SMB’s to realize that tier-one retailers, who in the past have dominated with rationalized assortments and highly optimized push-oriented supply chains, can also play the “differentiation” card by developing “endless aisle” and dropship strategies with their vendor partners too, expanding their offering in significant ways. Chances are the tier-one retailers have other, bigger issues, and that creates a window of opportunity for the SMBs.
Appendix A: RSR’s BOOT Methodology™

The BOOT Methodology™ is designed to reveal and prioritize the following:

- **Business Challenges** – Retailers of all shapes and sizes face significant external challenges. These issues provide a business context for the subject being discussed and drive decision-making across the enterprise.
- **Opportunities** – Every challenge brings with it a set of opportunities, or ways to change and overcome that challenge. The ways retailers turn business challenges into opportunities often define the difference between Winners and “also-rans.” Within the BOOT, we can also identify opportunities missed – and describe leading edge models we believe drive success.
- **Organizational Inhibitors** – Even as enterprises find opportunities to overcome their external challenges, they December find internal organizational inhibitors that keep them from executing on their vision. Opportunities can be found to overcome these inhibitors as well. Winning Retailers understand their organizational inhibitors and find creative, effective ways to overcome them.
- **Technology Enablers** – If a company can overcome its organizational inhibitors it can use technology as an enabler to take advantage of the opportunities it identifies. Retail Winners are most adept at judiciously and effectively using these enablers, often far earlier than their peers.

A graphical depiction of the BOOT Methodology™ follows:
Appendix B: About RSR Research

Retail Systems Research ("RSR") is the only research company run by retailers for the retail industry. RSR provides insight into business and technology challenges facing the extended retail industry, providing thought leadership and advice on navigating these challenges for specific companies and the industry at large. We do this by:

- **Identifying information** that helps retailers and their trading partners to build more efficient and profitable businesses;

- **Identifying industry issues** that solutions providers must address to be relevant in the extended retail industry;

- **Providing insight and analysis** about a broad spectrum of issues and trends in the Extended Retail Industry.