ICL Partner

A Future View of the Grocery Business

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Any time there's an organizational change, the first phrase out of the corporate mouth is "so that we can better serve our customers…" Of course, anyone with a reasonable BS detector will immediately recognize this as code that really means, "our customers are all terribly frustrated with us and reorganizing will deflect some of the heat."

ICL has overhauled its entire organizational strategy over the past three years, and without looking I'm certain we could find that favorite "…serve our customers…" catch-phrase in many of the resulting press releases. But there's a central fact at work here that's a bit unusual — and that fact is that customer orientation has been the primary target of this entire program.

- Reporting wise, we have shifted from a operation of layered management to a matrix allowing rapidly deploying cross-department teams that essentially report only to the customer. The old top management rung (like the Vice Presidents of Whatever) are now viewed as a resource for the customer team leaders.
- Financially, ICL's P&Ls have become a conglomeration of customer-specific P&Ls. All financial reporting is customer–specific.
- Employee compensation is now largely based upon customer satisfaction and success.
- General products and product development organizations have given way to customized, user-specific programs built upon worldwide platforms to minimize individual customer cost while providing virtual customized results.

There are lots of ways to run a company, so why choose this one? ICL resolved to migrate to this philosophy because our customers are in the midst of doing exactly the same thing. For ICL to be successful, we must mirror the mindset of our successful customers as they forge into the future of retailing. The fact is that they expect of us exactly what their customers have learned to expect from them: more… for less.

Another nice phrase, but you probably are thinking "more ***what*** for less ***what***?"

- More quality for less money
- More choice using less time
- More consistency requiring less effort
- More convenience but less risk
- More service for … well, just more service

And just as shoppers' demographics are more diverse, our customers' strategies are more diverse — for example, blending EDLP with a powerful frequent shopping network, an unheard-of combination until recently. Shoppers' lifestyles are more "divergent," whatever that means, just as the demands of our customers seem to be much less homogenous than they were ten years ago. For example, a single “solution” sold in a cookie-cutter way is not going to make the market.

And our several largest prospects moving to **ISS*45*** will use (1) radically different configurations — each one perfectly valid and useful — and have demanded (2) radically different financial proposals — all, of course, constituting a good deal.

And just like their customers, who want to be recognized and catered to as if they were special, our customers, those same retailers, also demand to be treated as individuals.

Like the old jungle saying, “if you want to catch a tiger, learn to be a tiger.” If ICL was going to continue to be successful, we needed to adopt the same strategies as our supermarket customers were using. This wasn’t obvious ten years ago but things have changed radically since then —the markets and their expectations are significantly different. Ok, that’s another wide, generalizing statement, so what does ICL think has changed about the retail market? These factors, for example:

- Consumers have become customers
- Focus on the supply chain has shifted fast to the demand chain
- The old notion of Point of Sale has migrated to Point of Access
- The physical store is still critical, but the “virtual” store is becoming more and more important
- Industrial Technology is still a big deal, but consumer appliances are even a bigger one. This is how you respond to a customer, to the “appliance” frame of mind (grind the coffee beans at home) instead of the Industrial thought (that centered on hauling in another truckload of Folgers off a backhaul).
- Mass merchandising has given way to more and more custom merchandise. And especially, custom merchandising.
- And while all this “micro”– level thinking is taking place, our customers are simultaneously going “macro” at the same time — like the bumper sticker: “Think Locally — Act Globally.”

And the success model for a sustainable, profitable and trusted business is the same for us as it is for our customers. ***Motivated and satisfied employees lead to satisfied customers and that leads to a profitable business***.

So what’s the future of the supermarket business? Well, here are some predictions we think are going to happen. If you think about it, these are all fairly straightforward results of the changes outlined above. Much of this is already starting to show up:

- First, the driving business force has become Merchandising. Not long ago, it was Operations that called the shots, but PoS and Information Technology selections are now made more on the basis of what it can do for customer relationships instead of how many keys are on the keyboard. The mind-set has gone from hard benefits / savings to soft benefits / market share / profit improvement.
- In the same way, plain old “Point of Sale” thinking is shifting to market baskets. The reports that ignite interest today have to do with things like basket analysis and cross-promotion margins instead of PLU movement.
- A supermarket isn’t the old general store. Checkers can’t possibly remember the names of all the customers. But technology can help those shoppers be personally recognized and create the same warm / fuzzy effect. It’s just the same when the woman at the airline counter doesn’t know you from Adam, but when she says “Oh! You’re one of our Executive Platinum members — let’s see if I can get you a better seat…” you don’t really mind that it’s not genuinely personal. You carry

your history on your card. Technically, this grinds down to Loyalty Programs leading to Data leading to Relationship marketing. You market to large numbers of ***individual*** shoppers with targeted coupons instead of mass-marketing to a mass of shoppers reading the Wednesday coupon page.

- Point of Sale will continue to be important, but the supermarket is now starting to become virtual — and it's going to be more and more virtual as time goes on.   The contact a shopper has with the store is much broader than the old model. The store sells to its shoppers not just in the aisles, but more and more with "intimacy:"
  - On the telephone
  - By mail or courier
  - Via FAX
  - At a Kiosk
  - Via a "personal shopper"
  - PC-TV
  - On Smart Cards
  - On the Web (think of the success of "shop-from-work" initiatives)
- These are areas where ICL's Precision Retailing, Interactive Retailing and PoS systems come together with information delivery systems such as **GLOBALabel**. The store of the past just had to "transact." Now, success comes from a cycle of Attract ➞ Interact ➞ Transact, and then you use the transactions to attract all over again. This is the new demand chain, and store technology has to tie these areas together usefully and effectively.
- On the opposite side of the coin, older institutions that went virtual a while back (when was the last time you were actually ***inside*** a bank) are doing just the opposite, becoming brick-and-mortar again, but not in the old way. Now it's inside the supermarket. Coffee shops, fast food, travel services, the post office. Anything that was "virtual" can be found in its "actual" form in the supermarket for additional convenience of the shoppers who are there anyway. This isn't going to stop either. We're entering the retail equivalent of "Everything, All the Time."
- To satisfy customers, store employees have to be knowledgeable and productive from the word "go." This puts new demands on PoS systems to be more complex but simultaneously easier to use. Sorry, the answer isn't to be found in more and better help screens: it's the elimination of the help requirement altogether. And some of the new keyboard technology takes us a giant step in this direction: eliminating unnecessary options (for the moment) is as important as making the actual choices perfectly clear.
- Item pricing will become more and more malleable. The day of "one price for all shoppers" is disappearing fast, especially with the technology now available to manage scaled pricing in-store, on-shelf. Already, it is difficult to know for sure the price of many items until the total key is pressed — just a minimum purchase requirement for a special offer would be sufficient to create this little puzzle. Attempt to automate varying percentage discounts depending upon frequent shopper level, or cross-product promotions to certain shopper segments and you will be presented with a serious technology problem that only advanced software design — including constant background order rationalization processes — will be able to unravel.
- Loyalty programs are coming out of the "green stamp" phase — that is, the old thinking that it was just a promotional tool is dying (or the retailer companies who

thought this way are dying…) If Frequent Shopper is used exactly like green stamps or double coupons — that is, easily duplicable by the store across the street, then everyone will eventually lose equally when everyone has the same program in the zero-sum-game scenario. Effective loyalty programs, on the other hand, are the tools for ***diverting merchandising dollars to the most profitable shoppers*** to increase profits. The strongest retailers are killing their competition by retaining the most profitable shoppers and dumping the unprofitable ones on their enemies.

- There will be more and more variation in the supermarket space, as specific needs for certain types of shoppers are met. We've learned, for example, that a typical shopper will probably buy fewer than 140 different items in a store during an entire ***year*** of visits. If you are the store that delivers those 140 items better and faster and cheaper, you'll earn a disproportionate share of that business. This is why "limited assortment" formats are growing fast and profitably at the same time stores providing great selection are ***also*** tremendously popular, and also very profitable. This seeming contradiction … isn't.
- Some of the variation in stores will take the form of technology. Some of these technologies looked like the road-kill on the information superhighway just two or three years ago, but now the combinations of self-scanning with high-service areas are more common in pilots than ever before. Electronic Shelf Labels may have at last jumped the technology chasm now that the cost and technology problems are finally out of the way. Besides, they're becoming critical for information delivery to selected groups of shoppers. The reward of a virtually checkout-line-free environment may be in the same store — for example, using an in-aisle portable shopper. Or with some amazing ICL technology (still in the lab I'm afraid) you could instantly scan an entire basket by pushing the cart through an electronic "tunnel."
- Critical mass of merchandising and its supporting technology will be essential. The recent continued conglomeration of multi-billion dollar retailers exists to retain not just stock cost advantages. Merchandising "reach" — that is, economies of scale and use of the data network — must be leveraged as well. In the recent wave of conglomerations, notice how the chains on the acquiring end of the deals had superior nationwide operating and merchandising consistency, emblematic of management excellence. How powerful would it be to have 30 – 40 million shoppers all carrying ***your*** card and feeding you data? [1]
- If mass is critical, what about the independent grocer who cannot possibly invest in the massive data warehousing infrastructure required to detail individual shoppers? Of course, independents' typically more efficient operation, local knowledge and higher service levels — something the large chains ***must*** use technology to emulate — will prolong their market base for a some time, but the big guns are getting bigger, and their shopper-specific aim is akin to a techno-guided cruise missile. The affinity marketing programs being pushed toward independents are unfortunately merely a temporary competitive stop-gap, since these may reward frequent shopping but have nothing to do with targeting and retaining the most profitable shoppers.

  But who cares if the independents fold up for lack of merchandising firepower? The great vested interests — and most likely saviors — are the massed dealer community and wholesalers, both of whose survival depends upon a thriving independent grocery community. The best dealers will once again don their consulting hats and create shopper-specific promotional and information systems

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1 I don't know — ask Safeway…

using scaled versions of the big on-line systems. On the wholesaler side, the successful ones will use their mass and competence to create large scale merchandising systems that are second to none of the most advanced chains in their capability and power. These will be marketed to their member stores as a "managed service," perhaps with the consulting services that can go a long way to ensuring independents' success and continued profitability.

The technology requirements to meet these needs are demanding, and very unkind to those who cannot supply the escalating requirements. In a particularly draconian expansion / retraction cycle, the expansion of in-store technology vendors we experienced with PC-PoS will almost certainly continue to shake out most of its temporary participants:

- Use of industry standards is essential. The bar on industry standards, however, is rising with ActiveStore being the most recent and maybe the most powerful standards notion ever presented for the industry. Writing for an off-the-shelf PC database design like FoxPro or B-Trieve was not particularly difficult compared to the rigors of ActiveStore compliance and the high-priced resources required to invent, architect, design, execute and maintain a Windows NT / SQL / ActiveStore complex.
- But these standards are enormously time-consuming for computer hardware, and performance is a continuing battle. Most current systems are slower than their forefathers, and shoppers are less patient than ever. Traditional and simple architectures found in most PoS systems are hopelessly inadequate, especially when ten-year-old software architecture is ported to Windows. The notion, by the way, that ever more powerful PC hardware will rescue inadequate performance characteristics is fatally flawed, unless one agrees that feature / function will be held static…
- The supermarket check-station will need to be featured around the shopper convenience: automatic warnings when more lanes need to be opened. No stoppage of the transaction when manager interaction is required. Automated messages, pagers, cellular calls to on-floor staff when special shopper attention is warranted. In other words, "Shopper ID" will bury "Produce ID" in the scheme of things.
- "Redundant" systems were once a requirement, but many systems today have abandoned or limited Replication, Resiliency and Recovery to the detriment of the shopper. Waiting for the system to come back up with your weekly shopping basket behind 30 other shoppers is the ultimate insult. PoS failures simply cannot be permitted, any more than corrupted or missing basket data can be allowed. Full sign-on, or even hot check files must be available in off-line mode, not to mention wonder of wonders, a full suspend / recall capability. (How do they ***do*** that?) The requirement for supermarkets to evaluate on the basis of architecture as well as features has become essential.
- The systems — and the companies supporting them — must be capable of rapid rollout. In the past, in an "operations-driven" environment, a slow rollout of a chain was fine. Stores were simply retrofitted with new technology when their turns came in the refurb schedule. But a chain cannot unveil a new merchandising system in a geographic area without supporting the same shopper value at all stores. Rollout schedules of up to five stores per day have been necessary to accomplish these ends.
- In line with rapid rollout is the ability to run the software across products. In case after case, major chains have modified their former dual-vendor philosophy, retaining multiple hardware vendors but making a single careful software selection to be operated across all stores regardless of hardware vendor. This provides the necessary competition across the 75% of the investment that is hardware-oriented while dramatically simplifying support and providing merchandising and training consistency across all stores. Furthermore, it enables far faster rollouts (financially in addition to logistically) since existing hardware can often be used.

- New, fresh software is required, and this is more to do with handling future requirements than it pertains to current needs. For example ten-year-old software, ported to Windows, can accomplish many of the PoS-centric functions needed today. But, just as the business commonly requires features today that were not even being considered five years ago, five years ***from now*** the business will need whole complexes of features that no one has thought of yet. The inability to code such important structures — and debug them — over ancient spaghetti code would doom the chain to a massive technology revision years before it would be economically feasible to do so. A valuable question to ask: how many major releases with how many new features did your vendor provide you with last year and ***how difficult was it for you to upgrade to take advantage of them***?
- Technology must be able to knit the entire demand chain, and link it to the supply chain. Vendors who can provide transaction technology, but not demand intelligence or shopper information delivery will be relegated to an ever-shrinking niche without sufficient financial returns for the necessary and constant software re-invention and re-investment.
- And this shakeout will be exacerbated by the ever-increasing hurdles of feature requirements, customization capabilities, performance and industry standardization.

Given this picture of the future of our industry, we have no doubt that the restructuring of ICL — and more important, ICL's relationship to its customers — uniquely positions this company to work for common success with the leading retailers whether nationwide or local.

To your success,

Tony

Tony van Seventer
Director: Supermarket Systems