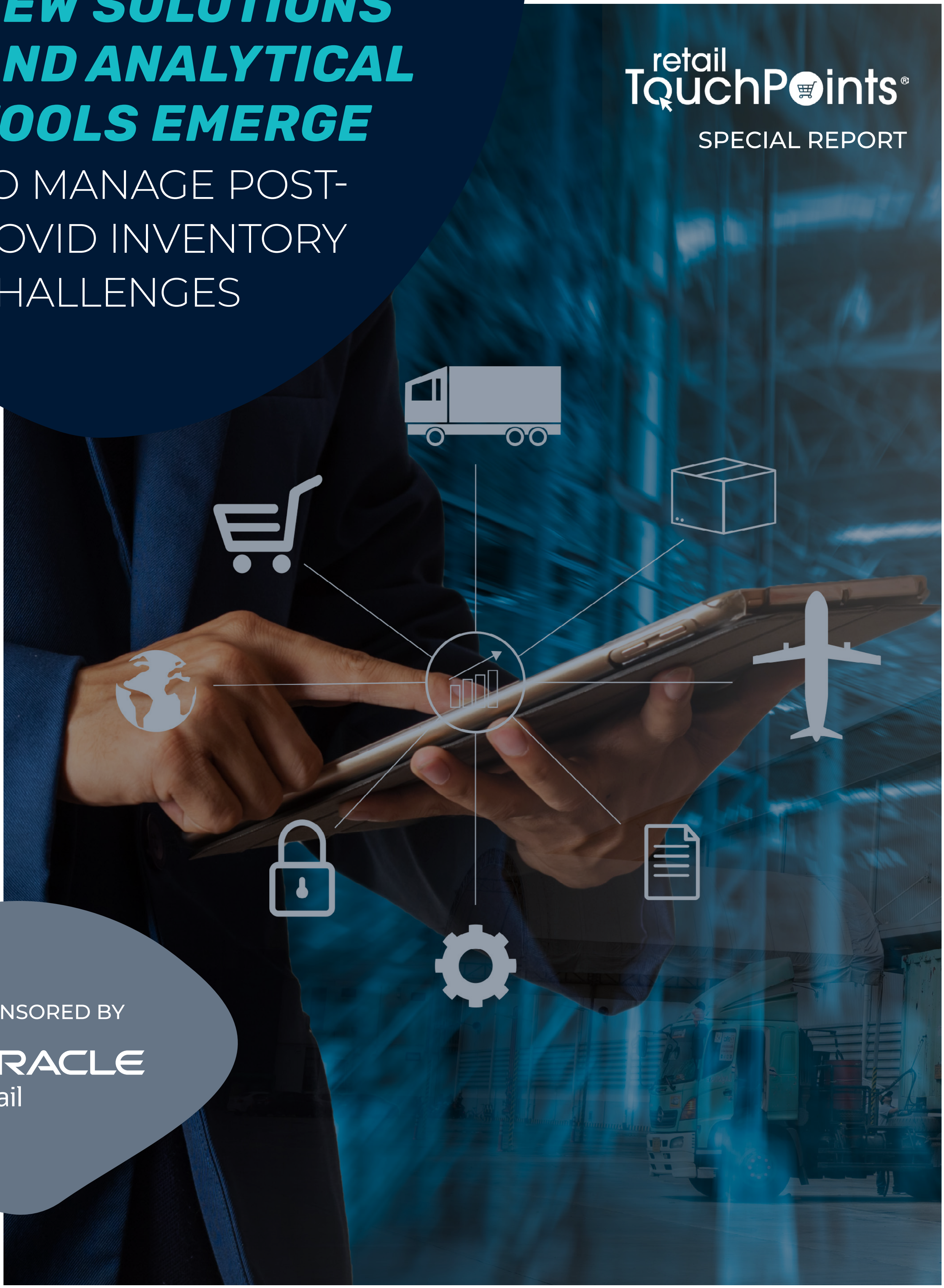
NEW SOLUTIONS AND ANALYTICAL TOOLS EMERGE TO MANAGE POST-COVID INVENTORY CHALLENGES



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SPECIAL REPORT

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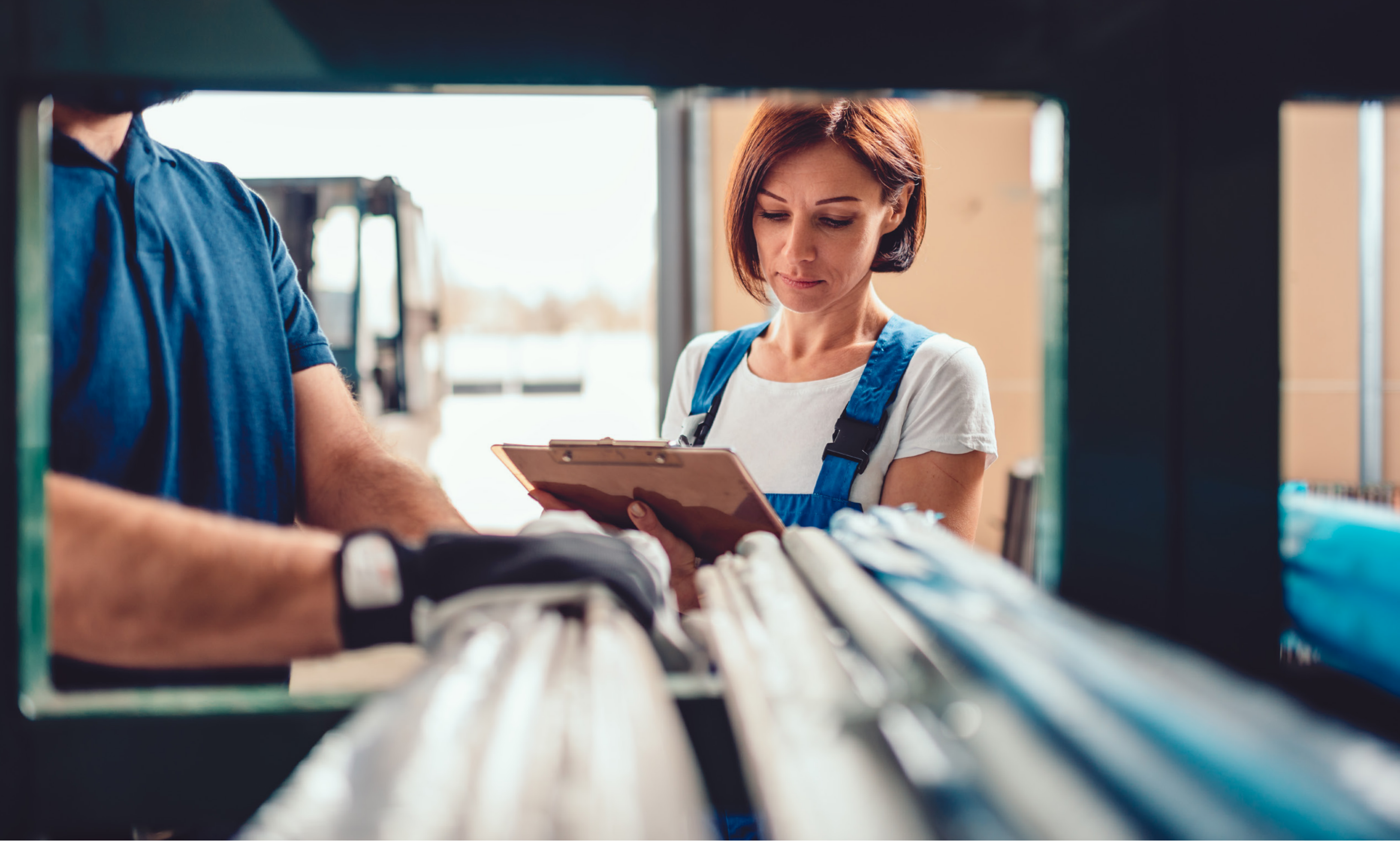


INTRODUCTION

The sudden onset of COVID-19 had many retailers scrambling to address short-term inventory issues. Panic buying stock-ups left many retailers without enough paper products, cleaning supplies and non-perishable foods to meet suddenly spiking demand. The photos of bare, cleaned-out aisles flooded the internet last spring, and retailers across the globe had to rapidly shift their inventory and supply chain strategies for both the short and long term.

On the other end of the spectrum, shuttered non-essential retailers were left with seasonal product that they had no way of getting into shoppers' hands. Many immediately pivoted to ecommerce as well as BOPIS and curbside models to salvage sales, but these didn't address deeper changes in consumer behavior that the pandemic accelerated.

To brace themselves for future shocks such as other viruses, political conflicts or climate emergencies affecting supply sources, retailers are considering longer-term strategies to protect themselves — and their customers — from the worst effects. This *Retail TouchPoints* Special Report will look at how retailers can adjust their inventory and assortment strategies to adapt to times that are still in the process of changing, including:

- Targeted, smarter assortments;
- Analyzing more granular consumer demand data to inform highly localized inventories;
- Using ecommerce to satisfy "long tail" demand; and
- More resilient supply chains that emphasize flexibility and diversification.

ADJUSTING STRATEGIES FOR A LESS PREDICTABLE, MORE ECOMMERCE-HEAVY ENVIRONMENT

Even before the pandemic-propelled ecommerce surge, brands already were experimenting with tweaking in-store inventory to better align with localization efforts, using more precise store planograms at a granular level. After dealing with the store assortment challenges induced by COVID-19, retailers spanning categories from apparel to grocery have had to level up their approach to inventory even more.

As ecommerce growth continues, many retailers are fulfilling these orders from stores themselves, meaning that they'll need to carry more inventory to meet the rising demand. "Our research indicates ecommerce growth will continue, and the volume of orders fulfilled from stores will continue to do so as well," said Mike Griswold, VP of the **Gartner Supply Chain Practice** in an interview with *Retail TouchPoints*. "**Retailers should be aggressively reviewing their assortments and be more deliberate with SKU rationalization efforts.** Over-assorted companies will find it difficult to effectively manage inventory levels and fulfill ecommerce orders efficiently."

The acceleration of ecommerce also presents an opportunity for retailers to make use of "precision planograms/assortment to be made available **on the physical as well as the virtual shelf**," said Sameer Anand, partner in the Strategic Operations practice of global management consulting firm **Kearney** in an interview with *Retail TouchPoints*. "The key to that precision of assortment is mining the data to truly understand who the consumer is, what they are shopping for, with what frequency, and their response to advertising, promotions and ecommerce delivery modality offers."

By harnessing the power of their consumer data, retailers can then use that information to form their initial category/assortment plans for store and ecommerce channels, and then use existing forums to collaborate with the brands that are also bringing deep insights on consumers — both online and in physical stores. It's also essential to recognize the specific role the store plays for its customers, whether that's as an experience hub, a quick replenishment point or a node for delivery to home. Aligning the type of stores with consumer insights in an integrated manner across channels, merchandising and supply chain is needed to define the assortment strategy at a granular level, Anand explained.

When it comes to the products themselves, in addition to the traditional categories such as perishable food, menswear, home appliances, etc., retailers need to apply category distinctions such as:

- Consumption at home versus away from home;
- Essentials that consumers may "stockpile";
- Modality of purchase (in-store, ship-to-home from store, ship-to-home from distribution center); and
- Supply limitations on the brand side resulting in products being on allocation.

Using a category scoring process — which could encompass going all the way down to SKU level — based on the dimensions outlined above can then allow for **segmented strategies for inventory levels**. For some categories, like those with long-tail SKUs or products purchased in larger pack sizes, it may make more sense to designate them as ship-to-home directly from the supplier, Anand said. Items such as disinfectants might call for higher safety stock levels because of demand and supply volatility, while categories like fresh produce will need a higher replenishment rate while consumers are still in the "at home" mode.

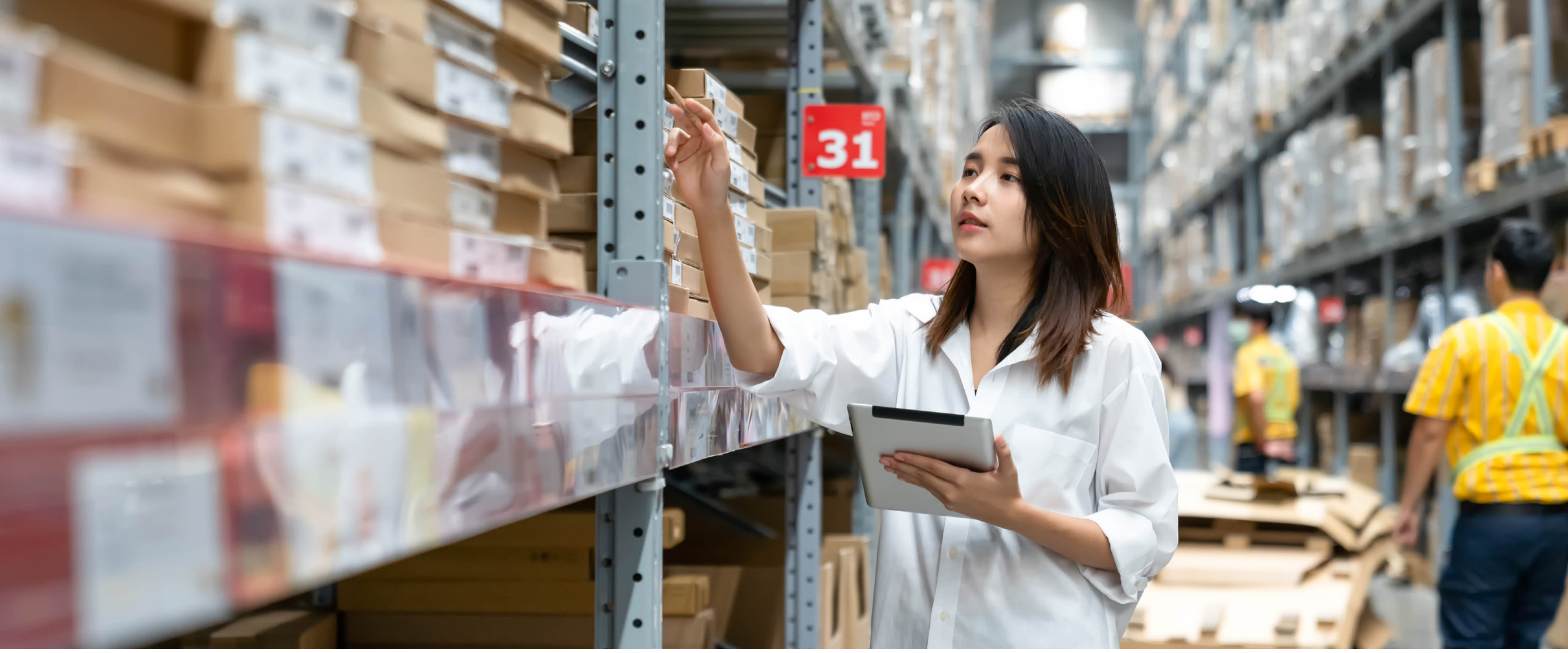
DETERMINE HOW MUCH RISK 'INSURANCE' YOU NEED

The need for supply chains to be more resilient and agile in order to deal with disruptions is greater than ever before. "Our data reveals CSCOs [Chief Supply Chain Officers] believe they will deal with **five to nine disruptions per year**," Griswold said. "Supply chains need to be more agile, especially in areas of demand planning, inventory acquisition and positioning."

Establishing processes such as sales and operations planning that provide early visibility into demand and supply challenges is crucial for the long term. "The sales and operations execution process (S&OE) provides the mechanism to ensure inventory is available as well as positioned in the appropriate nodes of the supply chain," Griswold said.

So what effect will future risks — caused not only by viruses and climate disasters but also rising ecommerce penetration, political risk and social unrest — have on inventory, and how can retailers protect themselves? Or, as Anand puts it: "How much 'insurance' does a retailer need to 'buy'?" That all depends on the risk profile of the retailer. Much like buying insurance, it comes down to an assessment of the likelihood of an event and its impact.

Retailers should "do a similar examination across the brand/retail value chain, i.e. a stress test, and get a view on vulnerabilities and the depth of those under various uncertainty scenarios," said Anand. "[This] will provide a view of what needs to be addressed, [followed by] internal debate on confidence level and affordability related to what needs a fix."



While each brand's risk threshold will be different, there are several strategies retailers can apply for the long term, including:

Collaborative retailer/brand partnerships powered by data and technology. Focus on the insights and actions that lower cost to serve, improve agility and drive growth across ecommerce channels.

Investments in software applications that improve visibility, transparency and predictability across the integrated supply chains. "In our conversations with channel and supply chain executives across brands and retailers, they have reiterated that knowing how much of the product is going to be available by geography and timing has been a high priority 'ask' to calm down the consumers," Anand said.

Automation of physical infrastructure as well as process. Labor costs will continue to rise, so the ability to do more with less, whether in corporate functions (e.g. through robotic process automation tools) or operations (like automated DCs to handle pallets) is growing.

Bolstering precision analytics across the end-to-end value chain. Precision at geo level is the key, Anand emphasized, whether it applies to assortment, inventory levels, inventory deployment or dynamic changes to flow paths multiple times a year.

"There is a desirability vs. affordability trade-off to consider given that all these investments add up," said Anand. "That's where we see retailers looking for new sources of value (e.g. data monetization, shared supply chains, network commercialization) to fund these omnichannel and resiliency-driven supply chain transformations."

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POST-COVID INVENTORY STRATEGIES:
Q&A WITH GREG FLINN, ORACLE RETAIL

Retail TouchPoints: **How will post-COVID inventory/assortment decisions differ from prior to (and during) the pandemic?**

Greg Flinn: The long-standing practice of simply looking at historical data to drive assortment decisions was turned on its side due to the short- and long-term shutdown of physical locations and digital presence. Pre-COVID data suggests that business casual was an important category that showed ebbs and flows over time. However, with the shift to work from home, this historical data is virtually meaningless, as seismic shifts have occurred across product categories, from business casual to (ath)leisurewear in this case.

To ensure that they are accurately identifying the right opportunities, retailers should look to use available web data gathered during brick-and-mortar shutdowns to identify category opportunities by geographic region, to drive assortment and inventory decisions. While the thought process remains the same when it comes to creating compelling assortments and placing the inventory in the right place at the right time, the **historical data should be cleansed** to optimize its utility.

RTP: **What new factors will retailers need to take into account?**

Flinn: COVID has given rise to new customer journeys. BOPIS, BORIS, etc., have been around for a while, and new journeys — such as curbside pickup and returns — are emerging as more critical than ever for retailers to facilitate. This presents an opportunity to evolve the curbside experience and deliver a seamless contactless experience for the customer using mobile POS. Retailers must figure out how to create mobile “stores” to highlight additional products a customer may want, using purchase history or suggesting an alternative product to turn a return back into a sale.

For example, if a customer wants to return a handbag curbside, while the reasons for the return may not be known, presenting other options via a store-on-wheels could be beneficial. It could help keep the customer engaged, provide customized service, maintain the sale and, ultimately, deliver an unforgettable user experience. Although loss prevention issues have to be addressed, providing options to customers while sitting in their vehicle will create a significant opportunity for any retailer to create an in-vehicle experience.

RTP: **What longer-term strategies can protect retailers from the worst impacts of future inventory shocks, such as other viruses or climate emergencies affecting supply sources?**

Flinn: The idea of a narrow supply chain network is likely a thing of the past. Agility is key for retail success and resiliency amid disruption. Retailers must take the time to identify regions that need additional fulfillment locations and areas that need more brick-and-mortar stores to serve as customer-facing experiences. Having a well-established network of inventory holding locations and having the ability to shuffle inventory quickly across the network will make coping with future inventory shocks more manageable.

Additionally, retailers must identify categories of products where they can control production and distribution, enabling them to shift more quickly as the demand shifts. Household paper products, such as toilet paper, tissue and paper towels, serve as a great COVID example. Based on the demand for those paper products during the COVID pandemic, instead of relying on someone else's production schedule and only procuring what was allocated to each retailer, taking on the production of specific categories means retailers can more quickly respond to massive demand shifts. For this reason, COVID saw the rise of demand for private-label and own-brand products, particularly in grocery, where grocery retailers could have met the increased consumer demand with ease and without relying on third-party suppliers. As we found, consumers will not tolerate out-of-stock inventory: **63% of consumers** we surveyed confirmed they would not wait to try another brand or shop elsewhere.

RTP: **What supply chain strategies should retailers be considering as they relate to inventory and assortment?**

Flinn: Although opening physical locations seems counterintuitive in a pandemic, our **research** also showed that there would continue to be a desire by consumers to shop at a traditional brick-and-mortar store. The decreasing price in real estate suggests an opportune time to open new stores in markets where web data supports the demand and available customer base, or to use retail space as a dark store where inventory is used to fulfill orders. This approach speeds up the delivery times to those areas further away from the central warehouses.

Furthermore, real-time allocation of available inventory will ensure that inventory is sent to the locations that need it most now, versus pre-allocation that often results in non-trending stores getting unnecessary inventory — creating additional expenses as that merchandise gets touched multiple times throughout the **supply chain**.

From an assortment point of view, while working to maintain truly unique assortments versus the competition, retailers must focus more on the core items within an assortment, ensuring depth in those items, and focus less on the fringe items, decreasing the breadth of the assortment. Assortments will always need fringe items, but in the future, owning less of those fringe items and moving those inventory dollars to the core items will increase sell-through and margins.

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RTP: **What tools/solutions will be most valuable to retailers in this area?**

Flinn: A robust **forecasting solution** with built-in AI will be critical in quickly identifying demand, fulfillment and return patterns as the business evolves. Understanding where and when — the demand will occur, an order will be fulfilled and a return will happen — sets retailers up to place the inventory optimally by location, thereby saving on inventory holding costs, shipping expenses and costs associated with taking returns.

Planning solutions will be necessary to set the appropriate guardrails around unconstrained forecasts, making the distribution of open-to-buy dollars across products and locations much more efficient. Additionally, cloud solutions that help identify relevant offers at the customer level will drive inventory productivity and increase margins.

RTP: **What else should retailers be considering as they rethink assortment, inventory and supply chain?**

Flinn: As demand shifts seismically across product categories, retailers must incorporate customer data in every decision they make. Retailers must also understand how the customer mix is changing and understand how the traditional core customer might no longer be a significant portion of the business. Analyzing history by customer, planning by a customer and managing inventory by the customer will highlight quickly emerging customer groups, high-margin customer groups and declining customer groups. Creating **assortments**, managing open to buy, and allocating with specific customers in mind cannot be overlooked and must be incorporated into any end-to-end planning and supply-chain-management process.

Greg Flinn manages Oracle Retail's planning and optimization applications from an evolutionary and go-to-market point of view, which includes solutions such as merchandising financial planning, and assortment and item planning. Flinn leverages more than 20 years of retail merchandising planning experience from the Neiman Marcus Group, where he was leading the team's Oracle Retail implementation of planning and merchandising solutions.

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USING GRANULAR, LOCATION-SPECIFIC CONSUMER DEMAND DATA TO CRAFT ASSORTMENTS

As retailers analyze customer data using a combination of micro-segmentation of consumer preferences and service, the results allow them to pivot their approach and inform physical store assortments. The various ecommerce models deployed in specific geographies, and how these complement the offering, also need to be taken into account. Assortment decisions can affect key indicators such as margins and customers' perception of convenience.

"Are [retailers] looking to serve the long tail, which might be high margin on a relative basis, exclusively through online orders?" Anand said. "Are they providing pickup services? Keep in mind the demographics of that specific postal code and **the premium on convenience that consumers are willing to pay**. Can the consumer demand be shaped to be comfortable with **24-hour** order-to-delivery on some categories, while it's **four to eight hours** for other categories? The assortment decisions in a physical store should be addressed with these considerations."

Of course, retailers also need to factor in product sales when focusing on assortment decisions. Today, there's a wealth of data, from sources such as the store's own POS to popular ecommerce purchases in the market area that the physical store serves.

"Successful companies balance the art and science of determining store-specific assortments," said Gartner's Griswold. "Utilizing this data and aligning assortment with customer and stores leads to lower markdowns, higher inventory productivity and more full-price sales."

Another trend that gained momentum due to the pandemic is retailers converting select locations into "dark stores" or micro-fulfillment centers. However, approaches can vary as retailers experiment with what's still a relatively new concept.

For example, one brand may be using its physical store as an experience hub with an emphasis on fresh (think produce or prepared meals), while the rest of the customer's order is fulfilled quickly and efficiently at a dark store next door. However, a different retailer might view the dark store more as an extension of the regular store, housing high-velocity items in a location designed to maximize ease of picking and fast replenishment. In the former example, there would be a significant reduction in assortment at the customer-facing store, whereas in the latter case the assortment might not change as drastically. "There is no single answer, so start with the 'Shape of Demand,' understand the role of various modalities in delighting the consumer and then determine assortment in that context," Anand advised.

THE ADVANTAGES OF LOWER OVERALL INVENTORY LEVELS

As retailers focus on heavy investments, driven by omnichannel requirements and building resiliency, they also are looking at new sources of value. This is where assortment comes in: lowering inventory levels — without compromising on service levels — can free up cash flow for investment in other priorities. "Well managed inventory levels in the age of **increased personalization and tailored planograms** on one hand, and limited DC storage space on the other hand, allows for managing supply chains while **limiting the increased cost to serve that would happen otherwise by virtue of additional node/storage space**," said Anand. As a bonus, the right levels of inventory also result in reduced out-of-stocks and, consequently, bolster the brand's perception among consumers.

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Jessie is a retail expert, design lover and storyteller. She has never turned down an invitation to go shopping — in the name of research, of course.