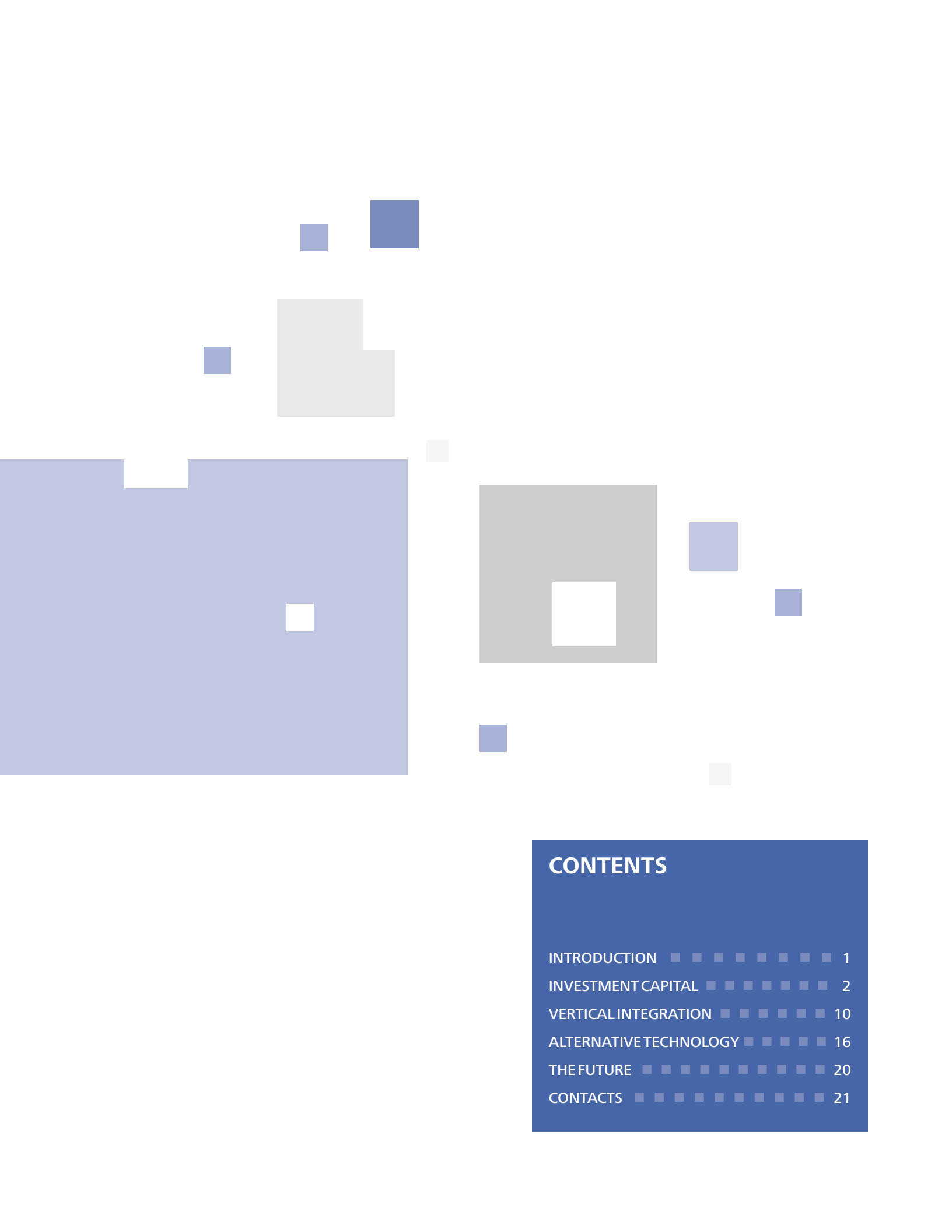


Disruption in retail

From product to pixels





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INTRODUCTION

Deloitte and the Retail Council of Canada (RCC) recently undertook a study aimed at uncovering how technology is supporting and driving disruption within retail.

While previous studies by Deloitte and the RCC explored the evolution of the omni-channel and the use of social media in retail, the focus in 2015 has shifted to the overwhelming impact of technology on the retail environment.

Technology and retail are growing closer than ever, with the evolution of retail being driven by the consumer. Faster, better, cheaper has to be achieved at all costs, but how? Retailers are looking to technology for the answers.

Whether it is the vertical integration of the supply chain that is made possible by improved system interfaces or the seamless online, mobile and in-store shopping experience that consumers expect, the desired results cannot be achieved without technology.

WE CONDUCTED INTERVIEWS WITH RETAILERS TO UNDERSTAND HOW THEY ARE USING TECHNOLOGY TO BRING DISRUPTION TO THE RETAIL LANDSCAPE. SPECIFICALLY, THE FOCUS IS ON:

- How is disruptive retail innovation being financed?
- How are retail companies and technology disrupting the flow of goods and information from concept to consumer?
- How is alternative technology disrupting retail?

THE FINDINGS CONFIRM THAT RETAIL IS AN EVER-EVOLVING INDUSTRY. HOWEVER, FASTER SERVICE, BETTER QUALITY AND RICHER EXPERIENCES ARE NOW BEING ACHIEVED BY:

- Looking outside the organization for technology innovation or for funds to innovate in-house
- Using technology in new ways to improve the customer experience and to educate staff
- Improving the communication and volume of data flow within the retail organization
- Improving the communication and volume of data flow with suppliers

We found that technology disruption in the retail sector will favour those who are willing to accept it and those who are willing to change to better serve the new breed of technology-savvy consumer.





INVESTMENT CAPITAL

Investment capital for retailers? In the past, venture capital has not typically backed retail, so why is venture capital now available for retailers? Who is venture capital being made available to, and why? When we posed these questions to retailers and to sources of capital, we were very intrigued with the answers.

Technology in retail is seen as the big disrupter. With more purchases through eCommerce, there will be a dramatic shift in where consumers buy, and risk capital wants to play. It wants to back the start-up retailers that are dramatically shifting markets.

And brick-and-mortar retailers are also taking on the challenge.

“eCommerce is going to continue to grow as consumers get more comfortable ordering online. Consumers will increasingly use stores for more inspirational purchases, and will tend to order regular basics online for the

convenience,” says Paul Hazra, Vice President – Corporate Services, Overwaitea Food Group. If retailers want to survive the disruption, investing in technology to improve the online customer experience, improving logistics and inventory management, and increasing employee engagement in-store are considered key.



FUNDING FOR TECHNOLOGY IS HOT!

Currently, as retailers search for creativity and disruption, there is significant capital available. However, there is a catch, as highlighted by Brooke Harley, Founder, Campfire Capital: *“Tech-driven players are getting looked at by tech venture capitalists. Retail start-ups leading with a value proposition involving technology are more likely to secure funding than retail start-ups leading with a value proposition involving product or brand.”*

We found that there are two prominent capital powers at play – venture capital funding of retail companies presenting themselves as technology companies, and traditional retailers investing in in-house research and development. There are also traditional retailers currently sitting on the sidelines; they’re waiting to buy the technology disruption that will eventually become mainstream.

“There is no advantage to being behind when it comes to technology. Technology is not a matter of if – it’s a matter of when.”

Gary Sorenson
Chief Operating Officer and
Executive Vice President,
H.Y. Louie Co. Ltd.

Specifically, traditional brick-and-mortar retailers are allocating their technology budget in the following ways:

INTERNAL RESEARCH & DEVELOPMENT (R&D) GROUPS

- Retailers are keeping the technology spend internal. And, by creating core product teams focused solely on innovation to deliver a compelling product for the consumer, they are taking a “design first” approach. All operational responsibilities are removed from these teams; they are forced to think long term, disruptive and out of the box.

INTERNAL CAPITAL SPEND ON TRADITIONAL IT

- Retailers are increasing their IT budget, including additional spending for software, staffing and upgrading knowledge of existing personnel.
- We noted a shifting focus on budget allocation (e.g., decreases elsewhere in the organization in order to fund IT).
- There is also a shift in the expectations of franchisees versus corporate investment and spend requirements. For example, although corporate may supply a cloud-based software product, franchisees may need to pay for hardware like tablets.

EXTERNAL CAPITAL SPEND

- Venture capital is being made available to technology companies building disruptive software that will either improve the customer experience or improve back-office operations and efficiency.
- Many of these companies will become the target of traditional retailers that have not invested in innovation internally.



SO, WHERE ARE COMPANIES INVESTING THEIR TECHNOLOGY DOLLARS?

1. CONSUMER ONLINE EXPERIENCE

The operational complexities required to support the online shopping channel impact all aspects of a retail organization, from merchandising to marketing to warehouse management, and especially delivery. In short, investments are required to succeed and increase market share as much as they are required to defend existing market share. An effective user-friendly online experience protects your market share, entrenching the consumer with your offering. Consumers have to be able to shop whenever, wherever they are and the experience has to be exceptional on a laptop, tablet and especially mobile phone.

We noted that capital investments in technology to support the online experience can be grouped into the following categories:

Personalizing the online experience:

- **User-friendliness of the eCommerce platform** – the platform has to provide an excellent user experience, regardless of the device used
- **High-quality product photography** – the online image of the product needs to exceed expectations, as the visual experience is replacing all of the other senses
- **Look and feel of the website** – the website is replacing the look and feel of the sales floor, including the product presentation and the placement
- **Knowing what you're selling** – the user interface should be driven off the product requirements, e.g., zooming in on a picture of a container of coffee is not as essential as being able to zoom in on an engagement ring or a piece of clothing
- **Proactive data analysis** – mining data and using it before the shopping experience to make the online experience more relevant for the customer during the transaction, rather than after it, is more efficient for the retailer, it enhances the consumer experience and, in turn, it increases the likelihood of a completed sale

Understanding the consumer in-store and online:

- **Integrating digital and in-store analytics** – understanding what customers are looking at online and making it readily available in the store
- **Consumer loyalty program analytics** – using historical data to predict future buying patterns and inventory levels, and to understand the success of marketing campaigns
- **Enabling consumer identification and tracking across channels** – investing in technology that allows the retailer to track and understand buying patterns across channels
- **Opening doors to new markets** – based on the consumer base that has been identified by analytics, driving compelling product stories through effective and targeted communication

“People are ready for something new. Mediocre is not allowed anymore. Capital is being made for start-ups as they are celebrating new ideas and new ways to do things, this could lead to potentially leap frogging the others in the sector.”

Lyndon Cormack
Managing Director, Herschel Supply Co.

“Once we aligned the furniture that was most often browsed online with what was available in the store, we saw a significant jump in sales.”

Arash Fasihi
Chief Executive Officer,
Cymax

“Our predictive analytics provide leading indicators to anticipate demand, versus traditional sales data (lagging indicator). We connect this data signal directly to the manufacturer to empower them to put their products where the demand will be.”

Joseph Thompson,
VP of Marketing, BuildDirect

2. SYSTEMS AND PROCESSES

We found retailers are investing in back-office systems and processes that provide clear information on inventory availability and location. Technology has been, and will continue to be, relied upon to increase efficiencies with order management, in-store merchandise management, and timely deliveries from warehouses to stores and consumers, as well as deliveries directly from stores to consumers. *“Snapshot inventory, profit margin and inventory turns are vital software functions,”* says Ed Des Roches, President, Plum Clothing.

As retailers move away from case deliveries to delivery of individual products (“eaches”), traditional inventory management processes and systems cannot keep up. Many retailers are limited by outdated systems and lack of system integration, which makes it difficult to execute timely and efficient business decisions. Retailers are looking at the following investments to get the right product in the right channel, at the right time and at the lowest cost:

“Traditionally, there were three buckets of investment – technology, infrastructure and marketing – and these were clearly separated. But now, technology evolution has merged the three buckets, blending operations and the impacts of the investments.”

Aaron Gillespie
Vice President, COBS Bread

Back-office system integration

- Enables transparency and data flow between head office, sales offices and all selling channels, providing one cohesive set of data
- Improves the flow of information between stores and head office, which then supports process efficiencies (e.g., return processes, inventory levels)
- Ensures technology supports up-to-date item records and accurately represents what is available across all inventory access points

Vendor management systems

- Enable integration with vendors and/or manufacturers, driving visibility into key performance indicators such as sell-through, stock-outs and consumer demand
- Provide visibility with vendors and/or manufacturers, and support a mutual understanding of consumer behaviour in relation to vendor incentive programs and customized consumer incentives

Order management systems

- Enable efficiencies throughout the order fulfilment process, enabling process decisions that optimize labour productivity
- Support in-store picking with low volumes, as product is on a shelf or hanging on a rack; also support operational analysis of critical mass, as well as the need to move to dedicated distribution centres for eCommerce

Online delivery systems and processes

- Enable visibility of online buying patterns in order to forecast demand, and to improve communications with suppliers
- Manage key performance indicators such as inventory turn and return rates, and enable comparisons of performance across channels
- Support understanding delivery/shipping fees as well as the cost of distributing products, and enable conducting sensitivity analysis to better understand optimal fees

3. EMPLOYEE ENGAGEMENT

Despite large investment dollars going to technology, many retailers still feel that their employees are their biggest asset, and they are looking for ways technology can help employees interface and engage with consumers.

“We focus part of our technology investment in enabling our employees on the store floor. Providing them with the right information, in an easily accessible format significantly improves the speed and ease with which they can serve our members,” says David Labistour, Chief Executive Officer, MEC.

Interaction between employees and consumers, whether it is on the sales floor, on the phone or online via chat, will always be part of the business of retail. While there continues to be stiff competition and competing priorities, resulting in pulling investment back from staffing, people will always be at the heart of the business. *“Although the weakest part of the retail supply chain is often face-to-face interaction with customers, some companies have got it right. It pays to continue to invest in people and in personal interactions,”* says Paul Wilson, President, Spence Diamonds.

While consumers conduct significant research digitally, a certain percentage of purchases continue to be in person and, should an issue arise with an online purchase or with product quality, consumers will no doubt continue to communicate their unhappiness via phone, social media or in person in-store.

During the study, we noted retailers focusing their investments in technology that supports employees in the following three areas:

- **Information at their fingertips** – Employees should not have less information about the products than a customer walking through the door, so an investment needs to be made in technology that allows employees to easily look up product information, availability and selection. Technology should also enrich the experience by providing employees with insights from the point of sale, such as sales per hour (SPH), average basket size (units) and average transaction (\$). If an employee is serving a return customer, information on the customer’s recent purchases could also be useful.
- **Communicate across the organization** – Employees need access to relevant regional and online information. Customers should not have to tell employees what’s happening on the eCommerce site.
- **Train employees** – Employees should be trained and well versed in using the in-store tools, as well as the eCommerce platform. This will empower employees and allow them to better support customers, whether customers complete their purchase in the store or online.

“Personal growth on the sales floor can come from staff training and the power of analytics, especially for small companies that can be very flexible. The information that sales associates need is easy to find. With some guidance, insights and product knowledge, a seemingly transient workforce can become lifelong employees,” says David Goldman, President, Boys’ Co.



RETURN ON THE TECHNOLOGY INVESTMENT

Since our first retail study in 2012, Return On Investment (ROI) has been a key question when it comes to retailers and technology. It continues to be a key focus for retailers; however, we've noticed a shift, as this question was less difficult for retailers to answer in our 2015 study than in previous studies. eCommerce is seen as a store – the capital outlay is normally less than a brick-and-mortar store, but the potential upside is significant because customers are not confined to a geographical area. Retailers are also allocating some intangible value to their online presence, since it is seen as a method to protect and grow the brand.

We found that retailers are commonly measuring ROI by:

- Trial and error, piloting a small change and then measuring changes in revenue, customer service and store efficiency
- Using specific online metrics such as the number of unique visits, customer conversion and shopping cart abandonment to understand profitability
- Comparing the eCommerce investment to the cost of building out a brick-and-mortar store and funding store operations

Within the U.S. and Canada, the venture capital appetite for technology investment and ROI definition significantly varies. Historically, cash flow was the main focus for investment in retail. Now, there is investment in technology companies that improves the vertical integration of retailers, as this is seen as the real disruptor to the industry.

This shift doesn't mean retailers are comfortable with the investments. Challenges retailers are facing include:

- Difficulties defining the ROI on technology investment, as they find it difficult to correlate increased store sales with the investment in an online presence
- Issues stating a clear ROI that meets senior leadership expectations; store investment is a known entity with a known investment and a clear estimation of sales, while online sales are still unproven, making ROI difficult

In summary, the retailers that are ahead in this space determine ROI mostly through solid analysis, but the analysis is augmented by imagination and an ability to take a leap of faith.





VERTICAL INTEGRATION

As the change in funding and the interest in venture capital firms show, vertical integration is the new frontier in retail. But what does this mean for non-vertically integrated retailers? Why the shift? Where should they look to integrate? How does vertical integration play with existing supplier relationships? How are brands reacting to the shift?



TECHNOLOGY'S ROLE IN VERTICAL INTEGRATION

Retailers have spent significant time and effort building their existing supplier relationships, and being able to leverage these relationships enables retailers to integrate more efficiently. This allows both parties to better predict the right inventory, increase turnover, and execute strategic plans that benefit the retailers and their suppliers.

One way retailers are doing this is by investing in technology that allows retailers to share data with suppliers in a timely manner. Technology is most certainly needed for visibility into production as well as for tracking manufacturing through shipping, at warehouses, and during distribution and order fulfilment. Accurate estimates are very important, not only to meet the demands of the consumer, but also to hold suppliers accountable.

"Worldwide inventory is key. People come into the store to interact. If you can support this through the use of technology by getting the right inventory into their hands at the right time, then that is success. The customer's time is precious."

Dave Andru
Head of Finance and Growth Management,
Kit and Ace

Relationships for retailers are inherent in the technology they invest in, as core business execution depends on it. It is the demand for speed and accuracy that dictates the system needs, and communication and data accuracy are integral throughout the supply chain in order to:

- Manage quality assurance pertaining to raw materials and finished goods
- Accurately forecast and communicate expected demand to supply chain partners
- Allocate and replenish inventory in a geographically centralized manner in order to satisfy local demand

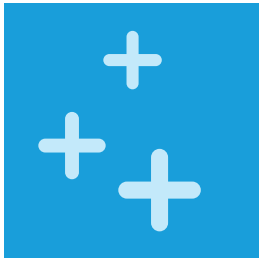
The relationships in the supply chain don't stop at the store but, more importantly, we noted that technology needs to be used to measure consumer loyalty, based on in-store and online experience:

- Customer Relationship Management (CRM) systems enable consumer data to be analyzed and synthesized, the tracking of customer preferences, and a general understanding of, and intimacy with, each consumer
- Customer loyalty programs enable retailers to reward repeat business, and provide customized services to consumers in-store and online

With relationship requirements spanning end to end in the supply chain, how are retailers and brands managing these capabilities?

"We have to be responsive to what the customer is asking and looking for, and be careful not to over-curate pre-emptively. Personalization involves understanding the customer, because they choose what they want."

Kyle Vucko
Chief Executive Officer, Indochino



RETAILERS' REACH

To improve their vertical integration, retailers are taking as much control as possible, reaching back into their supply chain as well as reaching forward into customers' homes. Specifically:

- **Reaching back** – We noted that more and more retailers are reaching back into their supply chain to create and manufacture private labels in an effort to reduce price comparisons with large online retailers and to improve the offering to the customer. Customers often tout “selection” as being key; however, there is a segment of the market that values a curated offering over the lowest price. Retailers can target this market with a well-thought-out private label that offers quality products.
- **Reaching forward** – Retailers are well versed in managing the in-store experience, but how well versed are they in managing the delivery to the customer or the in-store collection experience? The termination of the purchase interaction is not when the customer leaves the store, as in the past, but rather when the package arrives at the customer's home. These are new elements of customer interaction that should be well planned and executed. Retailers should be using data to become more relevant to their consumers and their ever-changing needs. The ultimate retailer's reach into a customer's home is online groceries. The products, especially produce, need to be as good as, or better than, you would pick for yourself. The customer is trusting the retailer to select products and to judge quality on their behalf.

“Integrate into a customer's life by being as close to the customer as possible, and by making it as convenient as possible.”

Peter van Stolk
Chief Executive Officer, SPUD

ONLINE GROCERY

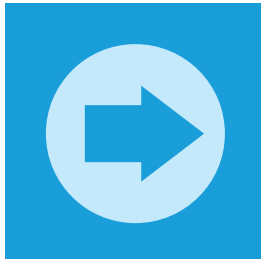
While delivery services for apparel and hardline goods continue to increase and become the norm, we found throughout our study that the grocery landscape is continuing to adjust to the new norm of online shopping, with deliveries or click-and-collect (either in-store or through a valet service). While Canada continues to lag in this segment, there are many grocery retailers that are changing the face of grocery shopping, again bringing as much control as possible into their supply chain. An online customer with the potential for repetitive weekly orders provides online grocery retailers with a significant opportunity to increase brand loyalty and monthly spend.

What does that mean for broader eCommerce?

“As customers get more comfortable buying groceries online, there will be a continued further growth spurt in other online specialty food products like chocolates,” says Peter Higgins, President, Purdys Chocolatier.

“We provide restaurants with the ability to reach forward and interact with customers like they have not been able to do and technology is enabling that.”

Ryan Spong,
Chief Executive Officer, Foodee



BRANDS REACHING FORWARD

While retailers are taking as much control as possible, so too are brands. The desire, and the requirement, to provide an end-to-end experience for the consumer is pushing brands that traditionally have not previously gone directly to the consumer to do so now. Brands are opening more retail stores and they are also selling directly to consumers online. This creates a number of challenges for retailers, especially if the brands offer discounts on the merchandise online and the same discount is not offered to retailers.

Brands are also aiming to control the in-store experience of the brand, with interactive in-store displays, product placement and an endless aisle. Retailers are considering this carefully, but they are more likely to accept this willingly if the interactive displays enhance the store experience, rather than intruding upon it.

Brands are also working with retailers to create new partnerships for inventory. Endless aisles in stores support the movement towards the development of a “drive-through” world, where the retailer doesn’t have to have everything the consumer wants – just a way to get it to them as soon as possible, with little or no incremental cost to the retailer or consumer.

“You can’t get away with retail being just a transactional space any more. Customers want an experience. Retailers need to make their experience memorable – even before it starts and after it ends.”

Anne Forkutza,
Creative Strategist, iQmetrix





ALTERNATIVE TECHNOLOGY

Alternative technologies that we explored included alternative payment channels, 3-D printing, interactive in-store displays, wearables, foot traffic analysis and, of course, drones. Depending on the type of retailer and the products sold, the answers in this section varied greatly. However, one thought that was common is summarized well by Clint Mahlman, Executive VP and Chief Operating Officer, London Drugs, who says, *"There is no value in technology just for the sake of technology. To be valid, there must be real value to the customer."*

Technology needs to improve the customer experience, improve efficiency or increase basket size. *"Show the connection of how I am going to buy. Am I coming back? Am I buying more? Is it just entertainment? It's a gimmick until you connect the dots,"* says Brian Kerzner, President, Rocky Mountain Chocolate Factory.



ALTERNATIVE TECHNOLOGY

We found four alternative technologies that have gained traction in the market, with some retailers having implemented pilot programs:

MOBILE WALLETS/PAYMENTS

Although most retailers we interviewed have not activated mobile payment options, they are following this innovation closely. Mobile payment functionality is being considered by retailers when new software or hardware is purchased. Integration with loyalty programs and CRM systems, as part of mobile payment rollouts, is a key consideration.

“Merchant payment systems will be most disruptive. Consumers are going to expect retailers to accept any type of payment method they want. POS systems need to be constantly updated so they can accept any payment method.”

Darren Hawrish
President, Native Shoes

ENDLESS AISLE

Retailers are looking for ways to bring the endless supply that is available online, as well as the online brand experience, into the store. Endless aisles allow retailers or brands to extend the supply of products and options to customers who have made the effort to visit the store. They allow retailers to more effectively manage precious shelf space without running the risk of losing the sale because the new product is not on the shelf in the customer's favourite colour. The endless aisle has immense possibilities, but it is not without pitfalls. As mentioned in the vertical integration section above, brands are reaching further into stores, wanting to control the whole customer experience. But what happens when the brand wants the endless aisle to connect to their own website instead of to the retailer's? How does the sale get tracked, and how does the retailer get compensated? Who owns the inventory and manages the deliveries?

SMARTPHONE-BASED TRAFFIC ANALYSIS

Retailers are exploring ways to use smartphones to understand the movement of customers outside and inside stores. Understanding what percentage of foot traffic is captured at different parts of the day would allow retailers to put strategies into place to increase in-store traffic at the appropriate times.

PRODUCT INFORMATION BEACONS

Beacons allow retailers to bring some of the online experience into the store and allow customers to use their smartphones to easily look up product details. For example, a beacon associated with a mannequin allows the customer to scan the beacon and obtain all the product information about the mannequin's outfit.

We also discussed a number of technologies that retailers did not think provide adequate returns at the moment but may do so in the future, specifically 3-D printing, drone delivery services, futuristic changing rooms, and elaborate interactive in-store displays (other than those that support endless aisles).

WHAT IS AN ENDLESS AISLE?

An endless aisle uses in-store tablets or displays that allow customers to order products that are no longer in stock or that are not sold in the store. The customers then have the product shipped to their homes or shipped to the store for pickup at a later date.

WHAT IS A PRODUCT INFORMATION BEACON?

Beacons are small pieces of hardware that retailers can place anywhere in a store. They pinpoint the location of a consumer's smartphone that has a retailer's app. Beacons use Bluetooth® Low Energy wireless networking technology, which is common on all newer smartphones.

THE FUTURE

Customers are not going to become less demanding, and the competitive landscape is not going to become less fierce. Embracing the disruption that technology is bringing is key to a retailer's survival, but each retailer needs to figure out where it makes the most sense to play. Is it online, mobile, in the supply chain or in-store? Should the technology reduce interaction with staff or improve the quality thereof? The answers to these questions depend on the sector that a retailer is in and understanding what customers want.

The two insights that we'd like all readers to take away are:

1. Retailers can't ignore the changing consumer.
2. Retailers should not get distracted by 'shining' new technology without understanding the value it brings to them and their customers.

How will you respond?

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