

Shopping Optimized

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At a recent Grocery Manufacturers Association conference, Publix CEO Ed Crenshaw said that successful SKU reduction programs need to maintain a focus on the shopper. As reported by *Supermarket News*, Crenshaw also made it clear that store brands need the same scrutiny as national brands when it comes to SKU reduction decisions.

Walmart is also redefining the roles of individual categories in its stores and rethinking the depth and breadth of product assortment choices. As part of this role re-definition, Walmart is reconsidering the role of national brands for some of its categories.

Putting the shopper at the center of retail assortment decisions.

For example, if the category is not considered a significant profit-builder and is somewhat ancillary to the needs of Walmart's customer base, that category becomes a prime candidate for reduced shelf space and significant SKU reductions, along with brand rationalization.

In some categories, retailers are figuring out that national brands are not always the drivers of the category and are looking to reduce the number of national brands on the shelf significantly, while expanding the presence of their own more profitable store brands.

In April 2009, it was reported that Walmart was

considering reducing the amount of space it provided branded manufacturers like Coke and Pepsi for Dasani and AquaFina bottled water brands. Margins in the bottled water category are low and leveraging Walmart's private label brand would only enhance category margins.

We have seen this same phenomena play out across other categories within Walmart, as well as at the major drug chains that historically have carried a vast array of over-the-counter drug products. Drug-chain retailers are beginning to recognize that too much variety creates a sea of shopper confusion at the shelf.

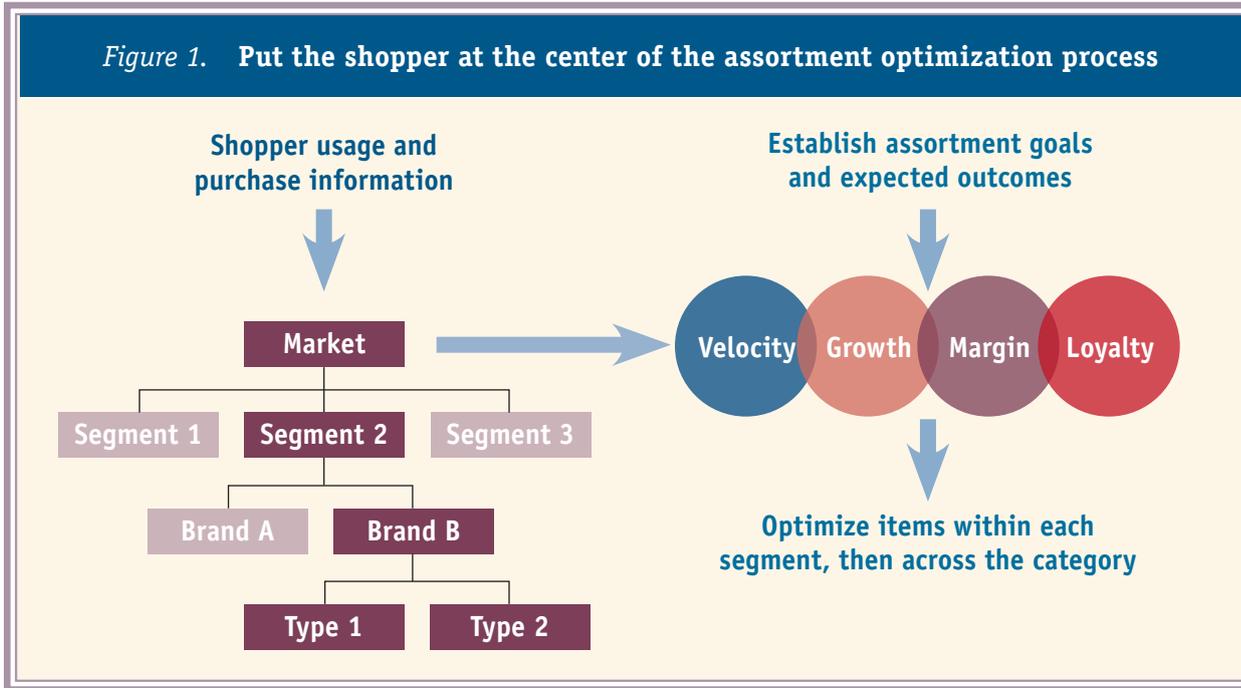
The premise of reducing shopper confusion and eliminating non-productive SKUs makes an incredible amount of sense, but carries considerable risk if not managed correctly.

We know from previous assortment studies that shoppers will travel great distances for better selection in certain categories, while convenience is more critical in others. (*How Does Assortment Affect Grocery Store Choice?* Richard Briesch and Edward Fox of Southern Methodist University, and Pradeep Chintagunta University of Chicago, January 2008).

If the SKU or brand rationalization process is not managed appropriately, retailers could lose shoppers and significantly reduce category volume. Publix CEO Ed Crenshaw also noted that discontinued items — not high prices or lack of front-end service — are the number-one shopper complaint.

For retailers, discontinuing items with high shopper-loyalty risks driving the shopper to a competitor's store. For manufacturers, the risk is that every retailer picks a different SKU rationalization approach. Consequently, they lose control of their internal portfolio rationalization process, which causes supply chain and manufacturing efficiencies to spiral out of control.

Figure 1. Put the shopper at the center of the assortment optimization process



SOURCE: Henry Rak Consulting Partners

START WITH THE SHOPPER

So, what is the right approach to SKU, line (forms and sizes) and brand rationalization? What is the best way to reduce the risk of lost and confused shoppers and maximize returns? The right approach starts with understanding how the shopper organizes the category into distinct segments based on usage and purchase behaviors (see figure 1).

When shoppers arrive at the shelf, it is essential to understand how they organize their needs and make purchase decisions. Understanding these behavioral dynamics will provide valuable insights that define both shelving and assortment principles.

In the case of adult analgesics, consumers may think about usage based on whether they have a headache or body pain. From that starting point, how do shoppers make their purchase decisions? What is most important: brand, form (liquid or pills) or size? Are there other attributes that are important to them, like convenience or flavors?

Once the way the shopper uses the product and makes purchase decisions has been defined, then organizing principles for SKU, line or brand rationalization can be established.

Which approach has the optimal impact on the category and the shopper must be determined. Simply eliminating the bottom 20 percent of SKUs based on velocity may not necessarily reduce confusion at the shelf. In fact, it could potentially result in low-velocity/high-loyalty SKUs being discontinued, which could cause shoppers to choose an alternate store.

For example, organic products tend to have

relatively low retail movement but high loyalty among shoppers. Eliminating the bottom 20 percent does not always reduce shelf confusion because all the sizes, forms, flavors that may be redundant tend to be retained.

However, eliminating the bottom 20 percent may identify the brands that are least incremental to the category and provide a good start towards brand rationalization.

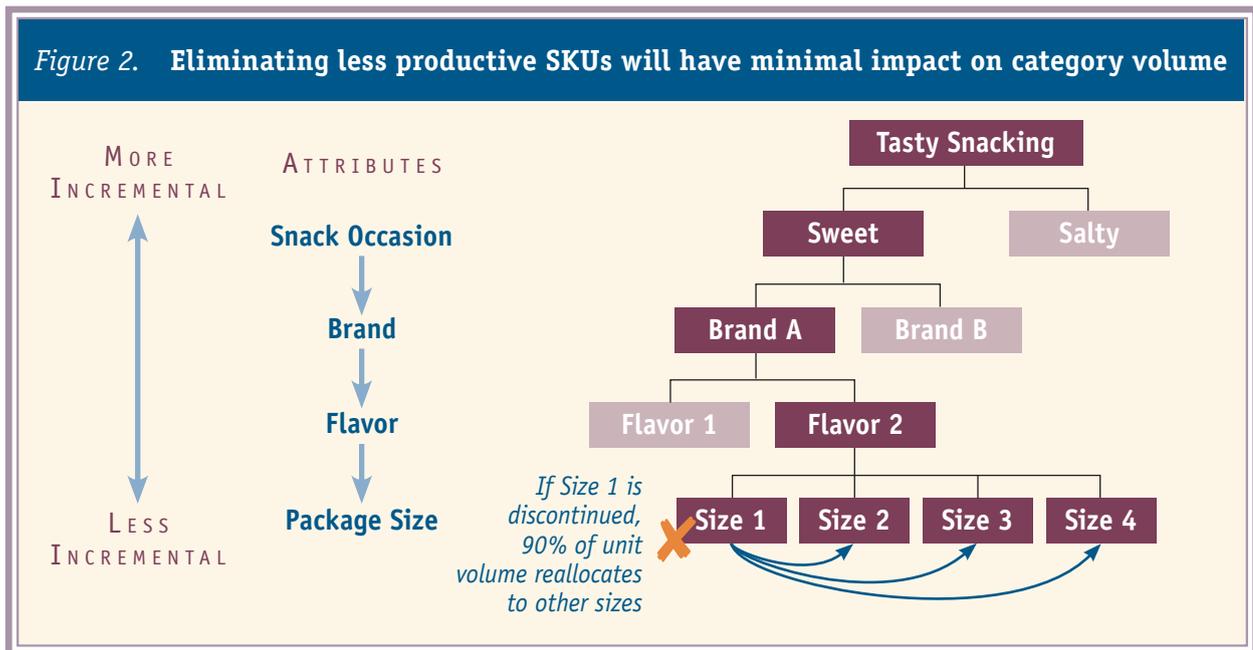
The approach and tools chosen for SKU rationalization must be able to identify which products are truly incremental to the category's growth and which are redundant based on actual shopper choices. Those SKUs that are redundant will reallocate their volume to similar SKUs when deleted and will not hurt category volume (see figure 2).

It is also important to understand the overall productivity of each of the shopper segments. By comparing the dollar sales to unit volume, it can be determined which segments are candidates for growth versus which may need to be rationalized. As retailers begin to make product add-and-delete decisions, it is critically important to understand where the product volume flows when items are added or deleted.

Clearly, not all volume falls away when an item is deleted and not all volume is incremental to the category when a new item is added. Given that, it is important to understand how the shopper makes choices when the item they had previously purchased is no longer available. It is equally important to understand where new items will source volume when added to the product mix.

In some cases, the new product may be filling

Figure 2. Eliminating less productive SKUs will have minimal impact on category volume



SOURCE: Henry Rak Consulting Partners

an unmet shopper need and provide an incremental purchase in the category. Understanding shopper switching behavior and the transferable volume flow is accomplished through usage- and purchase-based market-structure analysis, along with tools that identify detailed switching behaviors based on alternative SKU choices.

TRUE SHOPPER SATISFACTION

When it comes to brand rationalization, retailers must look at the number of brands that truly satisfy shopper needs. When looking at a category like dry packaged desserts, which includes iconic brands with dominant market share like Jell-O, you have to believe that most likely there are no more than two or three brands that satisfy shopper needs.

In more complex categories, like upper respiratory and allergy medication — with many ailment symptoms like cough, cold and flu — a distinct set of brands in each category segment most likely satisfy shopper needs.

These needs dictate that a somewhat broader set of brands is required, but maybe not as many as are represented on the shelf today. As these products are examined for deletion, it is important to understand shopper loyalty, and which brands, forms, sizes and SKUs would cause shoppers to leave the store if they were not readily available.

The range of assortment depth can vary by channel based on how shoppers value the depth of assortment. In the grocery channel, allergy products may be more of a convenience purchase, and depth of assortment may not be as critical. However, in the drug channel, allergy is a destination category where the depth of assortment is valued and expected.

Even when depth of assortment is valued, considerable room for brand and SKU rationalization still exists, but great care must be taken to understand SKU/brand incremental value and loyalty.

SKU, line and brand rationalization should not be a one-time event, but rather an ongoing process to capture the latest segment trends. The benefits, if done correctly, are an improved shopping experience, increased distribution on core SKUs, and greater category volumes with fewer SKUs.

This leads to improved gross-margin return-on-inventory investment (GMROI) for retailers. Manufacturers and retailers need to collaborate on this process to ensure that all low performing SKUs are viewed equally — including both national and store brands. This collaboration works best when real category-level margin and profit data are incorporated as part of the output results.

The end-game is to reduce shopper confusion, improve category metrics like revenue and GMROI, and satisfy shopper choices at the category segment level.

This is not a one-time event, but an ongoing, evolutionary process that requires a shopper lens on the category and the appropriate tools to discern item effectiveness and incremental category growth. ■



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