

OMNICHANNEL OPERATIONS

BRANCHING OUT IN THE NEW RETAIL ECOSYSTEM



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While e-commerce sales accounted for just 8% of retail sales in the US in 2013 and 2014, cross-channel retail contributes to more than half of total sales today, a tipping point in omnichannel retail.¹

At its core, omnichannel retail is about a gradual but important shift in consumer behaviour. Today, consumers increasingly expect to discover, search, buy, pick-up, and return items seamlessly from various physical and digital access points.

Both established companies and start-ups have made significant investments in building omnichannel capabilities. For all players, omnichannel requires a dramatic and fundamental shift in mentality from cost-centric, largely hidden supply chains to front-and-centre, customer-centric operations. As customers' expectations are evolving, retailers are testing a series of initiatives, including:

- More **access points**: online, mobile, stores, drives, lockers, pick-up and drop-off points, parcel shops
- More **delivery options**: after-hours, week-end delivery, time slots
- Shorter **lead times**: pick-up within 2 hours, same-day delivery
- **Flexible delivery points**: at train station for commuters, work place
- More in-store and drive-through **pick-up services**: reserve online, self-collect, pick-up in drive, endless aisles, etc.
- **Seamless experience** across access points and channels

This paper presents a new way of thinking about the operational implications of omnichannel retail and two steps retailers should take to survive and win in the new world:

1. **Focus on four plays** – that will drive customer-centric operations
2. **Think and build agile** – design your organisation and infrastructure to be flexible, innovative and one that embraces change rather than runs from it

¹ Source: Forrester Research.

1. FOCUS ON FOUR KEY PLAYS

While almost every retail process is or will be impacted by omnichannel, we believe that there are four key strategic “plays” that are critical to support the transformation in the eyes of the consumer: dynamic network design and order fulfilment; existing asset utilisation; owning the last mile delivery; and integration with suppliers.

DYNAMIC NETWORK DESIGN AND ORDER FULFILMENT

The growth of new services will force retailers to develop dynamic networks. To fulfil orders faster, they could leverage or combine their existing distribution centres (DCs), platforms, and stores with third-party providers.

Beyond traditional DCs, retailers are increasingly relying on a more diverse set of models to accommodate different combinations of product range, CAPEX requirements, pick-pack-ship volumes, access points, and lead time (Exhibit 1).

Exhibit 1: Dynamic network design and order fulfilment

APPROACH	RATIONALE	USE CASE
Store picking	<ul style="list-style-type: none">Offering a broad range of SKUs within two hours with minimal investment	<ul style="list-style-type: none">Click-and-collectShip-from-store
Dark store	<ul style="list-style-type: none">Higher picking productivity on a narrower range, for pick-up or delivery within two hours	<ul style="list-style-type: none">Click-and-collectSame-day home delivery
Fulfilment centre	<ul style="list-style-type: none">High picking productivity on a broad range of SKUs for next day deliveryCan be dedicated to online or shared with brick-and-mortar operations	<ul style="list-style-type: none">Home delivery
Drop-shipping	<ul style="list-style-type: none">Expanding range to SKUs not sold in store by partnering with suppliers and wholesalers	<ul style="list-style-type: none">Home deliveryEndless aisles
Fulfill from supplier's DCs	<ul style="list-style-type: none">Cut costs and inventory by shipping very high-volume products straight from the supplier	<ul style="list-style-type: none">Home delivery

UTILISE EXISTING ASSETS BETTER

Physical stores come with high capital and human costs, putting retailers at a disadvantage against their leaner online competitors. However, stores could also become a key advantage. By using these physical assets as platforms for supply chain services – such as order fulfilment, pick-up and drop-off points, returns, ship-from-store, lockers – retailers could get ahead of the race to provide customers with fast and local services.

With current systems, processes, and layout, in-store picking productivity for grocery products rarely exceeds 40–60 items picked per hour – compared with 180–300 in a fulfilment centre or dark store. Yet we believe retailers will close part of the productivity gap through advanced inventory management, improved fulfilment systems and technologies, and picking methodologies. This would provide them with a vital competitive advantage against online pure players.

OWN THE LAST MILE

Delivery costs and services are important for customers choosing where to shop online. This has turned the last mile into one of the most powerful ways to differentiate in the market.

Exhibit 2: New players competing to own the last mile

HOME DELIVERY



- UberRUSH
- Deliv
- Postmates
- Peapod
- UberRUSH
- Google Express
- Instacart

COLLECTION POINTS



- Collect+
- Amazon.co.uk
- Curbside

LOCKERS



- Amazon.com
- ByBox

Traditional delivery companies have for decades built hub-and-spoke infrastructures and offered customers fixed delivery times. This model will increasingly become irrelevant.

Online leaders such as Amazon and Google have invested more aggressively in last-mile innovation than retailers and are shaping the way suppliers and transportation companies redesign their operations. Reflecting on how this affects their own business model, retailers will have to consider three options to innovate in this space:

- Build their own proprietary delivery capabilities where they have volume and density
- Leverage new solutions offered by start-ups such as Deliv', Collect+, and Instacart (Exhibit 2)
- Push their traditional suppliers to innovate more and rethink delivery models

Our article "Disruptive Logistics: The New Frontier for E-commerce" discusses these challenges in greater detail.

INTEGRATE WITH SUPPLIERS

As part of Amazon's Vendor Flex programme, P&G allowed Amazon to set up fulfilment operations within its own warehouses in the US to reduce transportation costs and speed up delivery. While supplier-managed inventory and other collaborative projects have existed for decades, this partnership is among the first for online operations. Target's alleged reaction to this partnership (moving P&G products to less-prominent places in their stores) emphasised the importance and complexity of supplier-retailer partnerships both online and offline.

Suppliers are making considerable investments in direct-to-consumer capabilities and partnerships. Given the scale required to serve consumers, we believe that it will be in both suppliers' and retailers' interest to better integrate and collaborate to achieve the critical mass required to best serve clients. Areas of focus will include:

- End-to-end **distribution** approach, drop-shipping
- Integrated **planning** and forecasting, leveraging big data
- Real-time visibility on **inventory** and orders
- Real-time **replenishment**
- Differentiated **packaging** for online versus in-store

2. THINK AND BUILD AGILE

Traditionally, retailers have laid out and executed expansion plans over several months or even years. However, with rapidly evolving consumer tastes and technology, this approach comes at a cost. It is becoming more difficult to predict what the landscape will look like in two to three years, much less define and plan for an unknown end state.

Not only will consumer needs continue to evolve, but omnichannel will likely mean different things to different consumers in various markets and sectors. For example, in grocery retail, click-and-collect accounts for over 90% of online orders in France but has only recently started to take off in the US.

If the only constant is change, then building flexibility and evolution into the organisation and infrastructure is paramount. To be agile, retail operations will need to:

- Think of the end state as an evolving target and adopt a continuous improvement mindset
- Focus more on incremental steps and sprints rather than a marathon, where it is better to make progress frequently and tangibly in weeks and months, rather than years
- Use meeting customer needs as the primary measure of progress
- Plan for experimentation and failure, fail quickly and cheaply
- Place a high value on simplicity, speed, and nimbleness
- Constantly reflect on progress and be faster, simpler, and more efficient

New and innovative approaches to systems and technology are also necessary in an agile organisation. Omnichannel presents a radically different set of challenges to retailers which require solutions incompatible with most legacy systems and technologies. For example:

- The product, inventory, customer, and order data are visible across every channel and to each stakeholder
- Real-time decision making
- Orchestration of multiple stakeholders such as suppliers, third-party logistics providers, transportation companies, ecommerce platform, ERP, etc.
- Enhancing services and productivity through technology: picking technologies and automation, in-store kiosks, etc.

How can retailers evolve their systems to enable customer-centric omnichannel operations? Walmart is showing one possible way: it has made 15 acquisitions since 2010. These cover areas such as online communities, search and discovery, predictive intelligence, and cloud-based services for e-commerce and operations. Meanwhile, other retailers are re-thinking the role of IT and service operations to bring them from behind the scenes to the front lines (as described in our report “The New IT Horizon”).

CONCLUDING REMARKS

The rapid growth of e-commerce is reshaping the retail ecosystem and the balance of power between consumer product brands, retailers, online players, wholesale distributors, and logistics groups. There is a fundamental shift in the way consumers shop, thereby increasing complexity for retailers. Retailers risk losing customers, cash-flow, and control of key elements of their value chain.

To survive and win in this context, we believe retailers need to shift their operations from cost-centric to customer-centric, focus on the right “plays”, and become more agile and innovative to hit a constantly moving target.

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ABOUT OLIVER WYMAN

Oliver Wyman is a global leader in management consulting that combines deep industry knowledge with specialised expertise in strategy, operations, risk management, and organization transformation.

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