OliverWyman

RETAIL AND CONSUMER JOURNAL

VOLUME 10

CONTENTS

WELCOME

TO THE 10TH EDITION OF THE OLIVER WYMAN RETAIL AND CONSUMER JOURNAL.

After emerging from the COVID-19 pandemic, the retail and consumer sector was confronted with a new set of major challenges in 2022 and 2023. These challenges include the fallout from inflation and cost-of-living crises in the West, as well as the demand stagnation in many parts of Asia. These factors put pressure on volumes, margins, inventory levels, and costs.

Despite these current challenges, the sector continues to face major long-term shifts. Technological advancements, particularly the rapid rise of generative artificial intelligence are reshaping consumer demand and how companies operate. The emergence of Gen Z and Gen Alpha is introducing a new dynamic to consumerism and talent management. Environmental concerns are also intensifying, leading to the emergence of coalition initiatives and new regulations in the retail and consumer sector. Additionally, recent geopolitical developments have further exposed the vulnerabilities of global supply chains.

While these themes can appear daunting, we remain convinced that there are ample opportunities within every challenge. Those who continue to anticipate, innovate, and transform will thrive more than ever.

This tsunami of change, and how to size the opportunity that comes with it, is the theme of this edition of the Retail And Consumer Journal. We explore the various developments, examine how companies are responding to them, and provide our insights on how to approach these challenges both now and in the future. We hope the shared perspectives will help you stay ahead of the curve and make the most of new opportunities that arise.

We hope you enjoy the reading this edition of the journal.

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DEMAND

INFLATION TRIGGERS SHIFT IN GLOBAL CONSUMER SPENDING

How consumers are adjusting their spending behavior

Jens von Wedel
Sarah Beul
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Inflation has shown signs of easing in recent months, yet consumers worldwide remain apprehensive about their spending power. A June 2023 Oliver Wyman survey of 10,000 consumers in nine countries illustrates that people across the globe still have significant concerns about their ability to pay for essential goods and services, despite a slight improvement in sentiment compared with February this year.

These concerns are widespread in Germany, the UK, France, and the US, with around three–quarters of consumers expressing them. The situation is even more severe in Brazil, Mexico, and the United Arab Emirates (UAE), where that figure is over 90%. As we detail below, consumers adjust their purchasing behavior accordingly.

SHOPPING BEHAVIOR IS CHANGING WORLDWIDE

The fear of inflation is evident in consumers' spending behavior on groceries and essential goods. Across all countries, more than 80% of survey respondents stated that they have adjusted their buying behavior, including over 40% who have reduced how much they buy.

In addition, consumers are particularly on the lookout for cheaper alternatives — more than half of those surveyed reported opting for lower–priced groceries, such as private label goods. The UK stands out in this regard, with two–thirds of consumers indicating they are substituting their regular purchases with cheaper alternatives. Increased price sensitivity has also driven consumers globally to seek cheaper options online (44% of respondents) and actively use coupons (41%) to save money on purchases.

In the Middle East, consumers have adopted an approach to saving money that is not yet as widely common in Europe: 43% of respondents in the UAE reported utilizing bulk orders to reduce prices. This reflects a shopping behavior that we mainly associate with North America, where consumers have long been accustomed to purchasing in larger quantities, benefiting from ample space for storage and significant cost savings from wholesale club retailers.

The bulk ordering continues to show strong momentum in Asia as well, though with a different approach. The model of Pinduoduo is based on a group–buying approach, where consumers can team up with others to purchase products in bulk. As this trend continues to gain traction, it highlights how different regions are embracing innovative ways to leverage bulk purchasing for substantial savings. For Europe, the Asian group purchase model seems a more viable option than the American bulk sizes due to typical limitations on storage room. At this point it is not yet an apparent trend.

Exhibit 1: Changing purchasing behaviors

Source: Oliver Wyman Forum Consumer Survey 2023

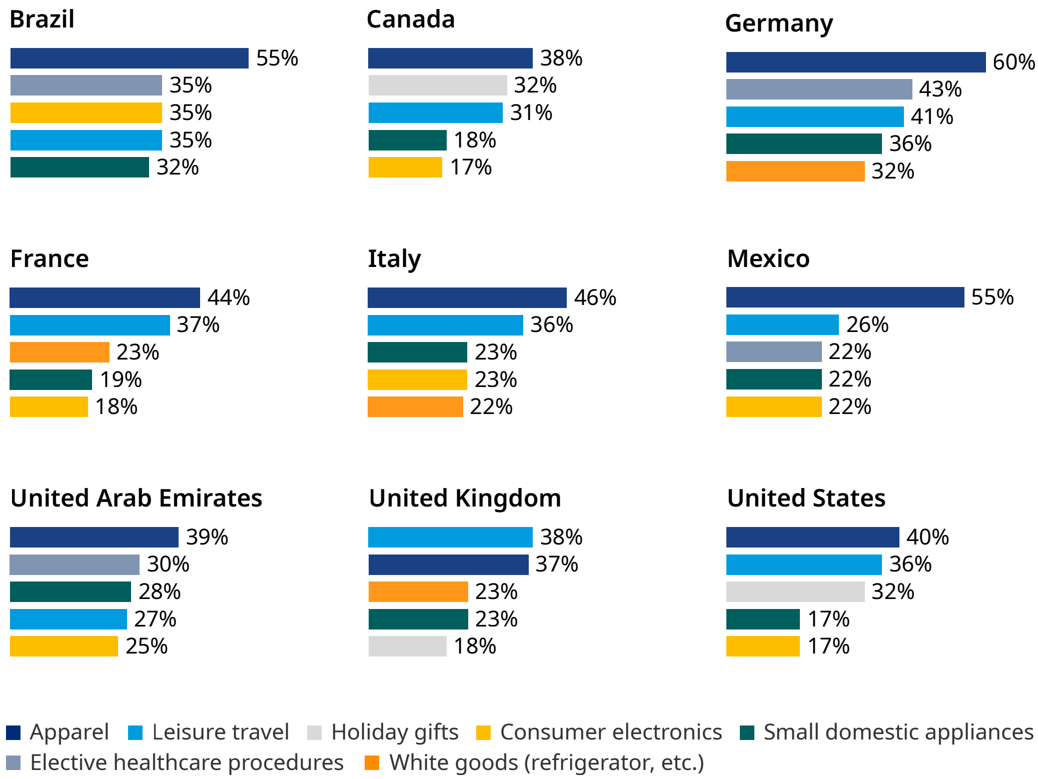
REGIONAL DIFFERENCES IN CONSUMER SPENDING PRIORITIES

Consumers are also adapting their purchases of discretionary goods. While shoppers are willing to accept stronger cutbacks for some product categories due to inflationary concerns, there are exceptions. Interestingly, apparel remains relatively resilient, with nearly half of respondents stating they will continue to spend as before.

Leisure travel is also valued highly. After the prolonged period of restrictions, lockdowns, and uncertainties during the pandemic, many people seem unwilling to accept inflation–driven cuts to their spend on traveling.

Looking at some regional differences: Consumers in North America are less likely to adjust their spending on holiday gifts, while European consumers say they will continue to purchase white goods. Overall, customers are now thinking much more carefully about whether and how much they are willing to spend on furniture, cars, and home renovations and, if necessary, may postpone their purchase to a later point in time.

Exhibit 2: Ranking of non-essential goods during recession



Source: Oliver Wyman Forum Consumer Survey 2023

NEED FOR ACTION FOR RETAIL AND CONSUMER GOODS COMPANIES

Inflation effects on spending will remain severe in the short term, particularly in those categories where consumers are more price–sensitive and willing to adapt their spending patterns, such as furniture, cars, home renovations, and white goods (see Exhibit 2). This challenging economic landscape presents a unique opportunity for retailers and manufacturers that possess superior value–for–money offerings and a commitment to leading cost efficiency. To capitalize on this dynamic, these businesses should proactively undertake a strategic review of their product range and pricing strategies. For instance, they could consider implementing targeted price reductions for a limited period. Retailers could optimize their private label product selection to attract customers who are looking for cheaper options. By embracing such approaches, businesses can position themselves not only for short–term market share growth but also for lasting customer loyalty and competitive advantage.

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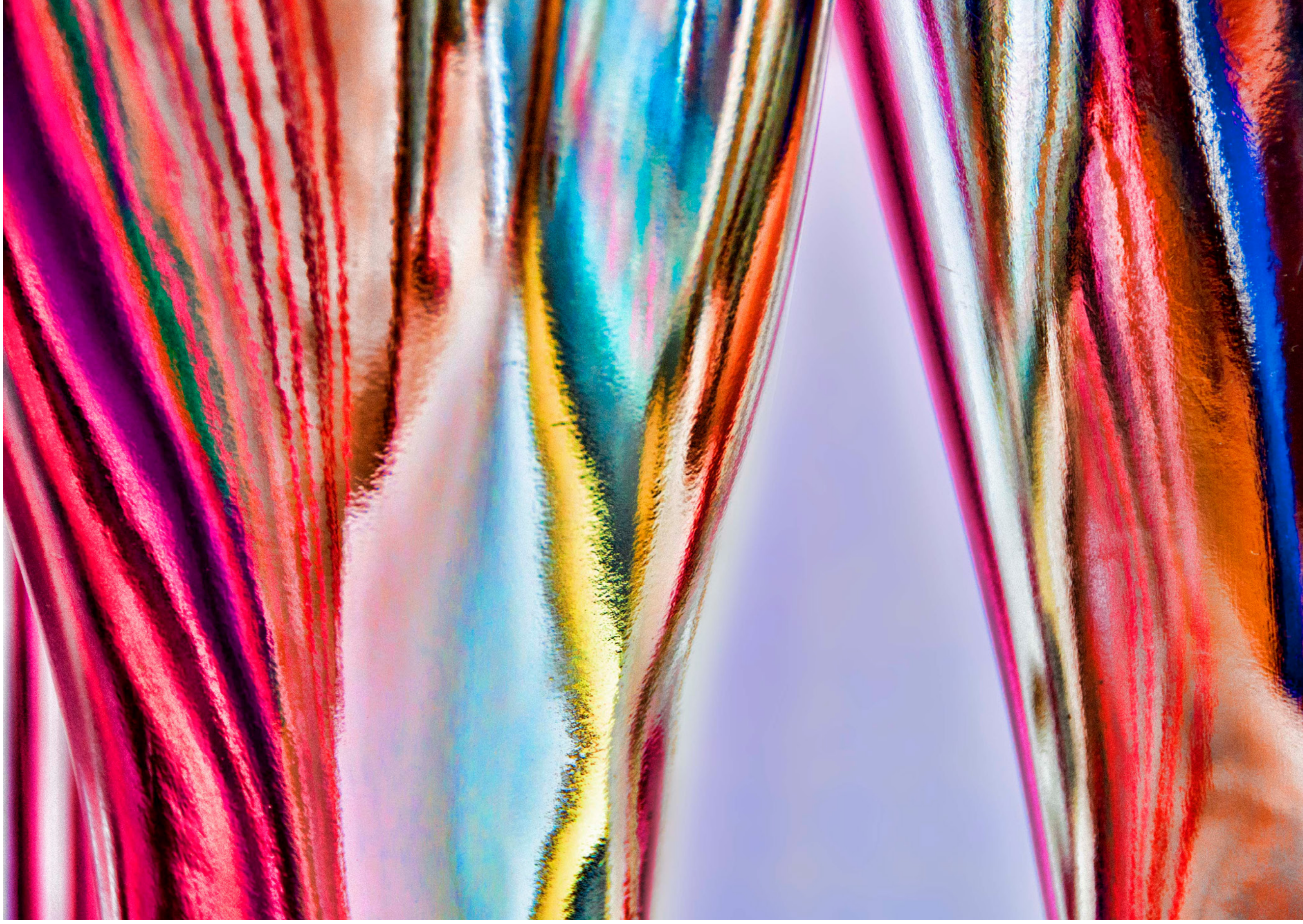


DEMAND

GEN Z — THE GENERATION CHANGING EVERYTHING

Oliver Wyman Forum

Older people sometimes caricature Generation Z as a temperamental collection of "snowflakes" and "strawberries" who personify the excesses of the social media era. But these digital natives are so much more than that. They are emerging from the global pandemic resilient and pragmatic, self–reliant and collaborative. Businesses that dismiss them do so at their peril.

Exhibit 1: Global population of Gen Z

25%	23%	19%	14%
Gen Z	Millenials	Gen X	Boomers

Note: Age group data adjusted to align with Pew Research Center definitions of each generation.
Source: Fitch Solutions

Born between 1997 and 2012, Gen Zers are still coming of age — but they already display fierce independence, passionate activism, and unwavering acceptance of others. They possess a moral compass and a willingness to chart their own paths rather than conform to previous norms. These traits will serve them well as they reshape society, the economy, the workplace, and much more in the years to come.

We spent two years studying this generation. Our research included focus groups and a recent poll of 10,000 adults in the United States and the United Kingdom. While Gen Z is not a monolithic group — far from it — our exhaustive research enables us to connect the dots in new ways on many of the commonly shared views and traits that define this cohort.

While many generations "become their parents" as they pass through life's many stages, the evidence suggests Gen Z will be different. Given the economic, social, and political trauma they have faced in their short lives, many of their values, behaviors, and lifestyle choices are now etched into their DNA. Brands and employers expecting Gen Z to revert to the mean will be surprised when they don't.

Our report dives deeply into what makes Gen Z tick and examines in detail the changes they are bringing. Here is a summary of our most important findings — and how businesses should prepare.

Maybe the older generations sucked it up and [got] on with it. Because it was quite a nice thought, being able to retire and do what you want. But now we're looking at it and our retiring age is moving further and further and further, and we're like, how long is this gonna keep going on for?

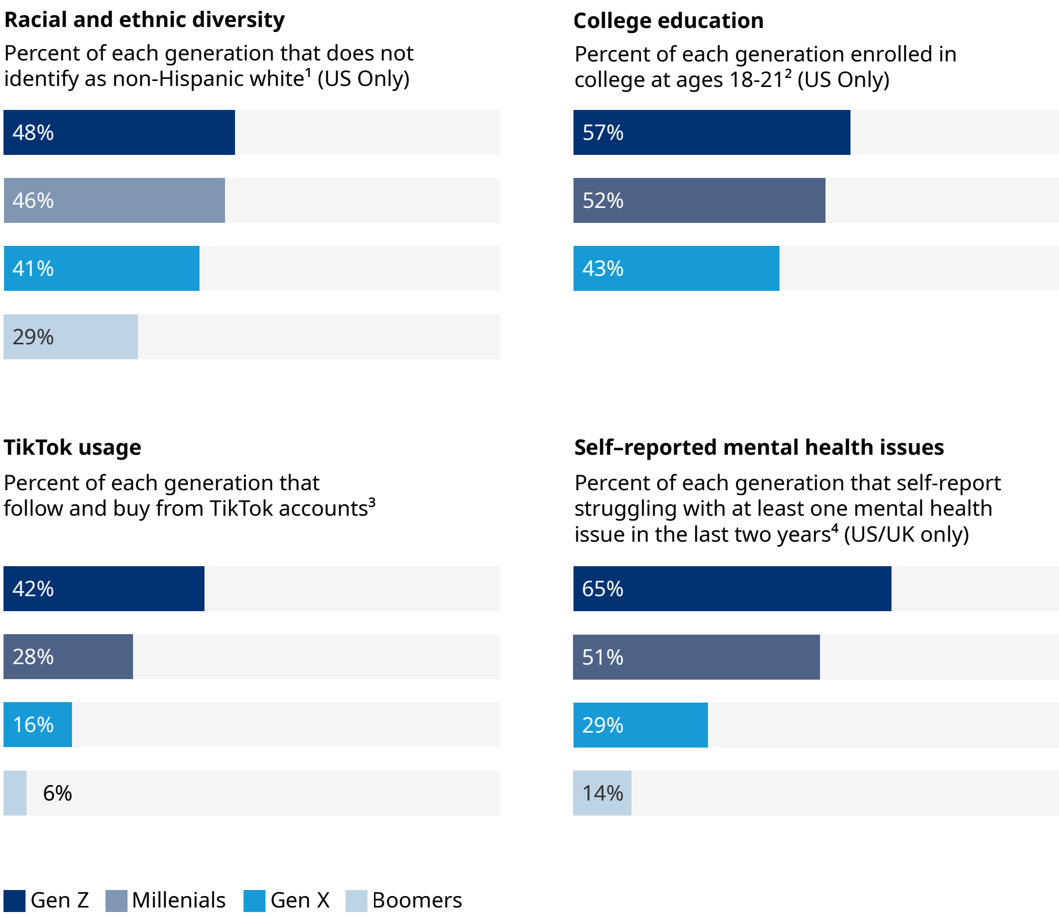
Midlands, UK

WHO THEY ARE

When it comes to identity, Gen Z defies all labels. Its members are spiritual, but not religious. They're realists, and are also optimistic. They embrace gender fluidity and view "situationships" as a practical alternative to defined relationships.

Gen Zers want bosses who understand them — and brands that celebrate their differences and support them in their fight against gender norms, beauty standards, and outright discrimination. To stay relevant, many companies must learn to shapeshift, too, by amending their policies, procedures, and benefits to fit Gen Z's needs.

Exhibit 2: Gen Z is diverse, smart, connected, and struggling with mental health



1. Source: US Census Bureau, Insider Intelligence.
2. Note: Measured in 2018 for Gen Z, 2003 for Millennials, and 1987 for Gen X. Source: Pew Research Center Analysis of US Census Bureau, Insider Intelligence.
3. Source: Klarna, Insider Intelligence.
4. Source: Oliver Wyman Forum Global Consumer Sentiment Survey, September 2020 – present.

WHERE THEY ARE

Gen Zers are the first true digital natives, and it shows in how they choose to stay informed. They may trust print and broadcast news, but 60% get their news from social media and its many influencers and creators, in part because they appreciate multiple viewpoints. They are skeptical and aware of the need to doublecheck what they hear. But they often struggle to distinguish fact from the conspiracy theories, half–truths, and outright lies that pervade social media.

To remain relevant and combat disinformation, media organizations must compete with social platforms through content that is not only informative and entertaining but also relatable. That means partnering with influencers and building up their presence on social media. The same is true for companies that want their story to be heard — and to stick. They should listen first, then understand and meet Gen Zers where they are.

HOW THEY FEEL

Coming out of the pandemic with twice the reported mental health issues as before, Gen Zers have become obsessive about their well–being. And they're managing it on their own terms. Increasingly distrustful of mainstream medicine, Gen Zers are embracing a more holistic approach that gives greater weight to their mental well–being. They track their health with wearables, are trying alt–treatments like CBD, and follow TikTok influencers for medical advice.

Their embrace of alternative medicine reflects a concern that many aspects of mainstream healthcare don't address their needs. Gen Zers are demanding greater attention is paid to the mental health crisis, women's health issues, and the inequalities in access to healthcare. And even those with access to care want better communication with their providers and options that fit their perceptions of self–care.

Over time, Gen Zers' proactive approach is likely to reshape the healthcare industry with their expectations for what care should look like and how it should be delivered. That has implications for the healthcare establishment — and will compel employers to greatly expand the health benefits they provide.

WHAT THEY CARE ABOUT

Gen Zers are throwing their idealism and ingenuity into fights against climate change, income inequality, and other issues. While they disproportionately engage in public protests, Gen Zers also see value in posting on social media or talking with their friends due to the collective impact of these small actions. Yet, they are aware they can't create change alone. Their trust in government and media might be fading, but they believe big institutions have the responsibility to act. They think businesses need to raise their game — and any business that does will have a distinct advantage.

Yes, some corporate leaders are facing a backlash from investors who want them only to focus on the bottom line rather than taking a stand. But if companies don't speak out about issues that matter to Gen Z, they risk losing the next generation of consumers and employees. Gen Zers have a keen eye for performative activism, and issuing a statement that is blatant "greenwashing" won't suffice. Instead, this generation pays attention to substantive commitments of time and money. Giving Gen Zers the volunteer time and financial backing to support their passions are good first moves.

WHAT THEY ARE DOING FINANCIALLY

Watching their parents and older siblings struggle financially has made Gen Zers debt–averse, stressed about money, and determined to manage their finances differently. Gen Z investors are starting younger and, as a group, have a higher percentage of women and people of color. And true to their digital upbringing, they seek community by crowdsourcing investment ideas from subreddits and the flashy influencers on TikTok and Discord.

And yet, they're not sure if they're making the right moves: Gen Zers are 1.4 times more likely to report that "money stresses me out" than older generations — and five times less likely to be disciplined with their spending. While many Gen Zers may not have money today, wealth managers, asset managers, and other types of financial institutions need to play the long game and grab the hearts, minds, and wallets of this next generation of investors. Retooling their products and marketing to reflect Gen Z's diversity is a good start, as is providing more educational and investing content.

HOW TO WIN THEM AS CUSTOMERS

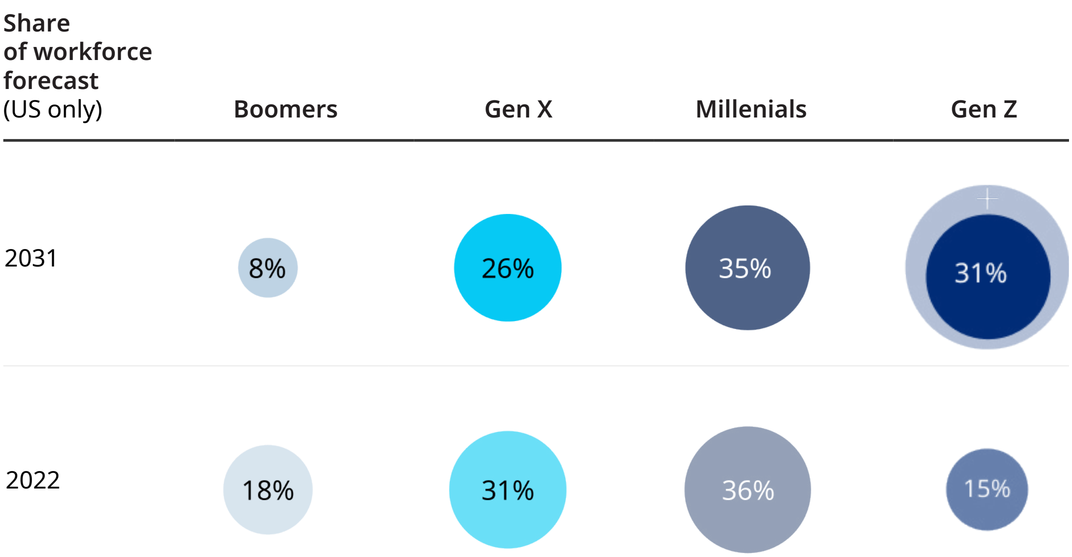
Gen Z has always had a world of online information at its fingertips. As comparison–shoppers, they are frugal, cynical, and can sniff out marketing gimmicks and false claims in a heartbeat. They expect more from companies than millennials do, and won't hesitate to bury companies on social media for their missteps.

Yes, they are a tough sell. But as they fully reach adulthood over the coming decade, Gen Z will become the largest consumer demographic in history. That means brands have no choice other than to learn what Gen Z wants and find ways to be relatable, inclusive, trustworthy, and transparent. Brands need to show authenticity, get "phygital" with the right mix of physical and digital engagement options, and understand that dialogues are the path to transactions.

HOW TO WIN THEM AS EMPLOYEES

While previous generations did whatever it took to climb the corporate ladder, Gen Z isn't about it. The pandemic turned their first jobs into a two-year video call and raised the bar for what they want from their working lives. What many want is to work for globally aware companies that provide the flexibility, autonomy, and work–life balance they seek. And they will #quietquit or #jobhop from employers that don't. A large portion of Gen Zers already are fashioning work for themselves that fits what they want, on their own terms: Today, 45% of them have side hustles.

Exhibit 3: Gen Z is on a path to becoming a leading force in the workplace



Note: Age group data adjusted to align with Pew Research Center definitions of each generation.
Source: US Bureau of Labor statistics

With Gen Z expected to account for nearly a third of the workforce by 2030, employers must raise their game to recruit and retain the best and brightest. Covering the basics — pay, growth opportunities, better worklife balance, transparency — is a start. So, too, is prioritizing their health, offering career optionality and initiatives that help them find personal fulfillment at work, and nurturing their entrepreneurial spirit.

As this report shows, Gen Z is different from even the young millennials who are only a few years older. Timeworn strategies won't work on this cohort — and waiting for them to conform to the old rules is risky for businesses and employers alike. Gen Zers want more — more transparency, personalized attention, democratized information, equitable treatment, and options in the jobs they work and products they buy.

Businesses that became nimbler and more agile during the pandemic should use those same skills to adapt to Gen Z's unique needs. Companies need to be creative and approach decisions more like experiments they can learn from. Given Gen Z's size and clout, employers and brands have no choice but to adapt. The question is whether they will forge ahead to leapfrog the competition — or be leapfrogged. Seizing the moment will help them win over the most consequential generation in modern history.

Read more

WHAT BUSINESS NEEDS TO KNOW ABOUT THE GENERATION CHANGING EVERYTHING

DEMAND

THE RETURN OF CHINESE CONSUMERS ABROAD

What to expect as Chinese tourists return

Imke Wouters
Jacques Penhirin
Kenneth Chow

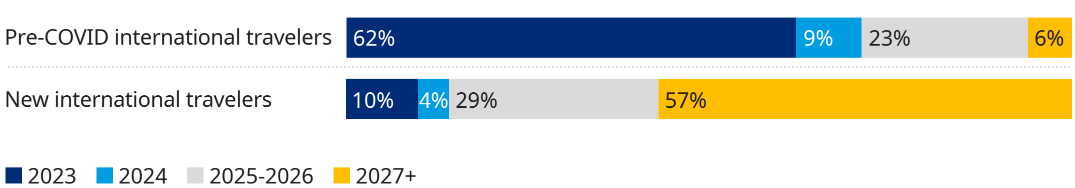
In 2019, Chinese travelers made 155 million outbound trips, and spent a cumulative $245 billion on outbound tourism, an amount greater than the size of New Zealand's total economy. After almost three years of border closure, Chinese travelers are finally coming back. Our survey of 3,495 affluent Chinese consumers, defined as those with a minimum monthly household income of ¥30,000, representing about 5% of China's total population in 2022, sought to understand when and where we would see them again. Additionally, we aimed to determine whether their abundant international shopping habits, particularly for luxury products, would continue.

NO FULL RECOVERY YET AS DOMESTIC TRAVEL REMAINS A POPULAR ALTERNATIVE

Although approximately 60% of experienced international travelers — those who traveled internationally before COVID–19 — have already traveled or are planning to travel in 2023, about 30% plan to wait more than two years before traveling internationally again. While we thought that after three years of border closure, everyone would be wishing to travel internationally again soon, for some the opposite has happened. In fact, 73% ofthe experienced travelers who have decided not to travel internationally in 2023 have made this choice because they prefer to travel domestically, having discovered the attractiveness of traveling at home during the last few years. Taking new international travelers into account, we expect a full recovery of Chinese outbound tourism in the second half of 2024 the earliest.

Exhibit 1: Expected international travel timeline

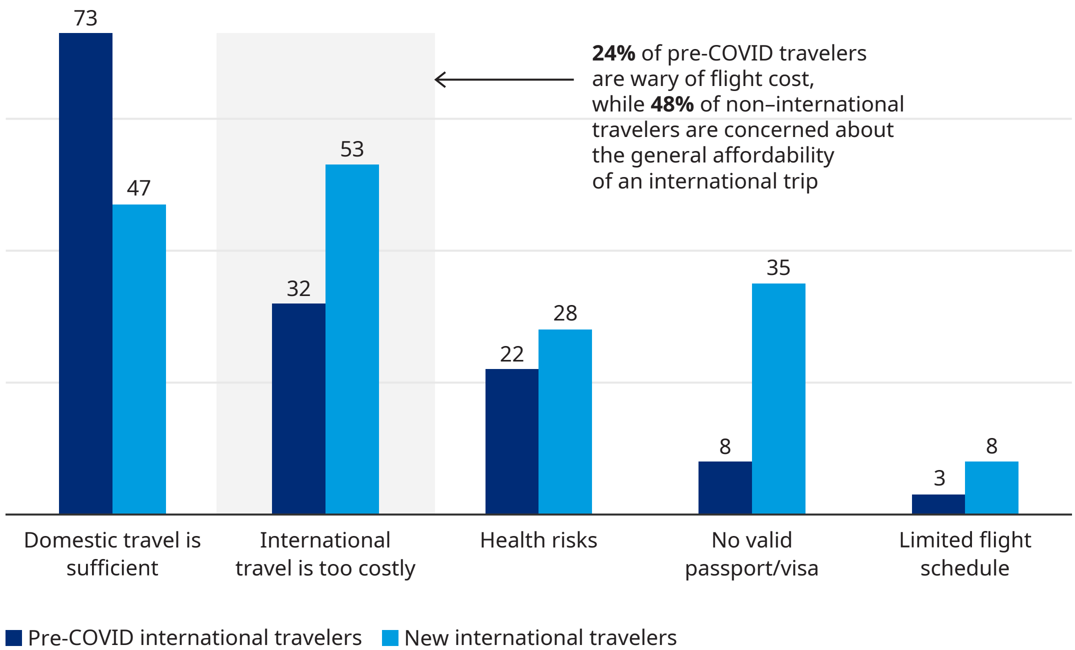
% of respondents



Source: Oliver Wyman's Chinese traveler survey (June 2023)

Exhibit 2: Reasons for deferred traveling plan

% of respondents



Source: Oliver Wyman's Chinese traveler survey (June 2023)

CHINESE TRAVELERS RETURN TO FAMILIAR DESTINATIONS

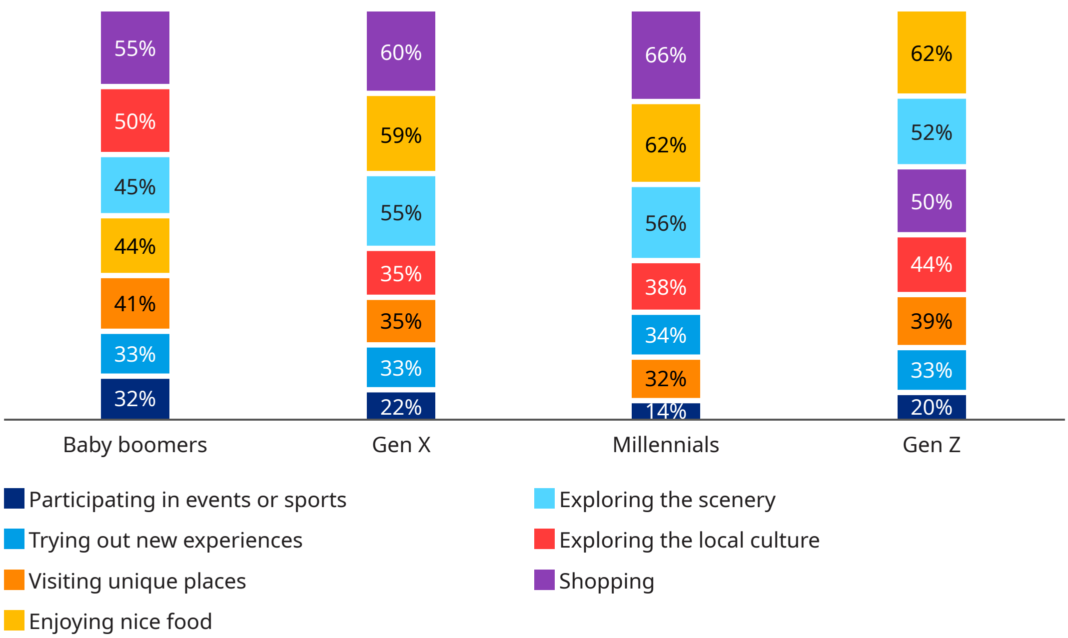
In 2023, the top destinations for Chinese travelers are expected to be familiar places, such as Hong Kong SAR, Western Europe, and Japan. These destinations are top of the list for experienced travelers, with almost 40% of those who have visited Western Europe planning to return this year. We expect an increase in the number of Chinese travelers visiting Europe later this year and expect Japan and South Korea will pick up in tourism significantly during the October holiday now that group tours are allowed.

Chinese travelers are also showing renewed interest in group tours. Contrary to the pre–pandemic sentiment where only 40% traveled in group tours, 52% of surveyed travelers plan to join these tours for their next trip in 2023. This upward trend is observed across all age groups and travel experience.

SHOPPING TOPS REASONS FOR INTERNATIONAL TRAVEL, BUT LUXURY SPENDING STAYS DOMESTIC

Before COVID-19, our surveys revealed the importance of shopping as a reason for international travel declining year-on-year, with exploring scenery becoming the primary motivation. However, shopping has regained its position as the top reason for international travel (Exhibit 3), followed by enjoying nice food. This trend is particularly popular among Gen Z travelers, with 62% of them inciting indulging in gastronomic experiences as their top reason for international travel.

Exhibit 3: Top purposes of post-pandemic international leisure travel by age group
% of respondents, Top 3 choices



Source: Oliver Wyman's Chinese traveler survey (June 2023)

While shopping is the main reason for international travel, the majority of luxury shopping is expected to remain domestic. Chinese luxury shoppers who travel internationally this year anticipate spending 20% of their luxury budget abroad and 80% domestically.

While the Chinese travelers are returning, it takes longer than we expected when the border reopened. Economic uncertainty has also impacted Chinese tourists' luxury spending overseas.

Imke Wouters, Partner, Oliver Wyman

Interestingly, we see a big difference between experienced and new luxury shoppers (those who only started buying luxury products during COVID–19 and so only have domestic luxury shopping experience). Approximately 85% of experienced luxury shoppers expect to revert to shopping overseas now that borders are open, only about a third of new luxury shoppers share this sentiment. These new luxury shoppers also have very high expectations on service levels internationally as they are accustomed to frequent and personal interactions with the sales associates of their core luxury brands domestically. With the luxury market booming in China in 2021, all luxury brands have invested in boosting their offerings in China. Given the wide domestic offerings, Chinese luxury shoppers see less of a need to shop internationally and are now also accustomed to buying luxury products when they want them, rather than waiting to travel. Gen Z represents a significant portion of these new luxury shoppers, and they are looking for new experiences and food rather than shopping.

GEN Z IS THE BIGGEST GROUP OF NEW TRAVELERS

In the last four years, new types of Chinese travelers have emerged. Around 30% of the new travelers in 2023 are members of the Gen Z workforce, who now have a stable income and the means to travel internationally. They care less about shopping and prioritize new experiences they can share on social media. They typically have smaller budgets, so they favour destinations that are close with the aim to maximize the number of experiences they can enjoy in a short time. As they are accustomed to luxury shopping domestically they don't wish to waste their limited travel time on shopping.

Those who are anxiously waiting for the full return of Chinese travelers will have to wait a little longer and be prepared for a new type of Chinese traveler who has higher expectations, given the enhanced traveling and shopping experiences now available domestically.

Read more

WHAT YOU SHOULD KNOW ABOUT THE RETURN OF CHINESE TRAVELERS

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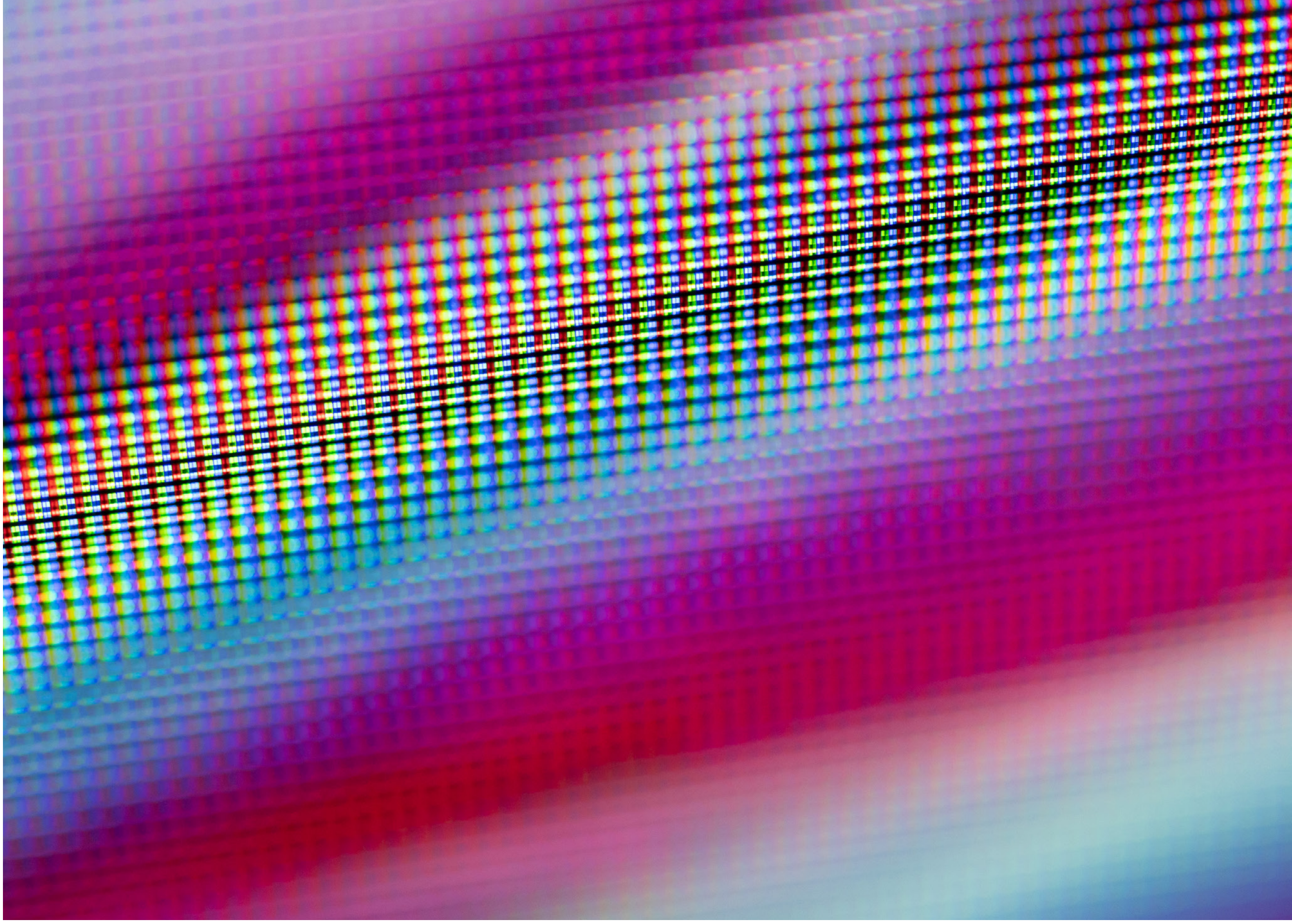


ECOSYSTEM

THE SURGE OF SOCIAL COMMERCE IN CHINA — FROM BIG 2 TO BIG 5

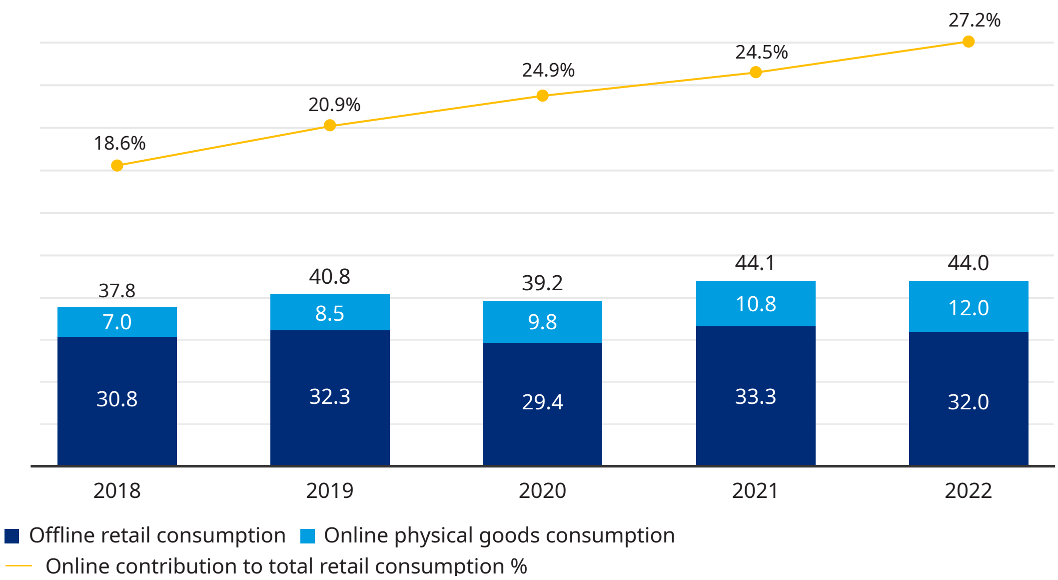
Navigating the evolving digital retail landscape

Jens von Wedel
Dave Xie
Sarah Adelfang

Driven by a confluence of factors, China has emerged as one of the most advanced e–commerce markets in the world. With a population exceeding 1.4 billion, China offers an immense consumer base eager for goods and services. The country's dynamic urbanization and growing middle class have created a preference for a digital transaction, fueling the growth of online retail.

As a result of this evolution, consumption of online physical goods has risen to 12 trillion RMB in 2022 in retail sales value from about 7 trillion RMB in 2018, and now accounts for 27% of China's total retail consumption (Exhibit 1). The market's vast scale, coupled with innovative business models, efficient logistics networks, and an affinity for social interaction, solidifies the nation's position as a vital hub for global e–commerce.

Exhibit 1: China total offline versus online retail consumption, 2018–2022
In retail sales value, trillion RMB



Source: National Bureau of Statistics, Oliver Wyman analysis

A look at China reveals a change in the e–commerce landscape. The longstanding platform dominance of the two major players — Alibaba and JD.com — is increasingly being challenged, driven by the emergence of social commerce. In a short period of time the "big two" have become the "big five", with the addition of challengers Pinduoduo, WeChat mini–program, and Douyin (known elsewhere as TikTok).

While the challengers have experienced rapid growth, the two big players have seen their growth nearly stagnate in recent years. Facilitated by the country's mobile–first mindset, these companies have seamlessly integrated social interactions into the shopping experience, creating new opportunities for brands and retailers. This fusion of social networks and e–commerce has revolutionized how people discover, assess, and purchase products.

Established and emerging players must rethink their strategies to thrive in this dynamic environment. China remains not only an e–commerce pioneer, but also a trendsetter that significantly influences the industry elsewhere in the world, including Europe. So, what conclusions can be drawn about the effects of the shift in China's e–commerce landscape on the European market?

Exhibit 2: Gross Merchandise Value (GMV) evolution of key channels[1]
In billion RMB

	2017	2018	2019	2020	2021	2022E	19-21 CAGR%	21-22 GR%
Tmall and TaoBao (Alibaba)	4,820	5,727	6,589	7,494	7,976	7,500-7,700	+10%	Mid-single digit decline
JD	1,295	1,677	2,085	2,613	3,297	3,482	+36%	+6%
Pinduoduo	141	472	1,007	1,668	2,441	3,100[2]	+56%	36%[3]
Douyin[4]			~50	~500	~800	~1,400	+300%	+70-80%
Overall							+22%	+8-9%

1. Refer to GMV of 2017 – 2021 financial year based on GMV number released by each platform and official data and estimation by company senior management team and broker report; 2. Extrapolated based on PDD Q1–Q3 y–o–y growth; 3. 2022 Q1–3 revenue; 4. Estimated based on broker report.

Source: Annual reports, Broker reports, Expert interviews, Oliver Wyman analysis

UNVEILING THE TRANSFORMATIVE POTENTIAL OF SOCIAL COMMERCE

Pinduoduo (under its international brand Temu) and Shein have emerged as noteworthy disruptors in the European market recently. Notably, Temu stands out from the competition through its customer centricity and advanced data insights, despite still grappling with some operational and commercial challenges.

Unlike established players, these newcomers are not constrained by extensive existing IT infrastructure. The freedom allows them to build fresh data analytics capabilities and seamlessly integrate new technologies such as artificial intelligence. They can also seamlessly tap into underpenetrated marketing channels in social media. This results in a superior ability to attract customers and stimulate demand, especially for low value, nonessential goods.

However, it’s not only social commerce retailers and retail approaches that are benefiting. Many conventional e–commerce brands and retailers have struggled in recent years to operate a profitable customer acquisition funnel through established channels such as search. This has left the leading platforms somewhat uncontested in their growth to take a top position in many Western European markets. Social media creates a new opportunity for brands and retailers to leverage a fast–growing marketing channel.

EXPECTED CONSEQUENCES FOR INDUSTRY LEADER AMAZON

The entry of Chinese competitors into the European e–commerce market will most likely usher in a new era of competition for Amazon. While the US–based company’s biggest competitors have traditionally lagged, the next wave of market entrants is expected to pose a greater risk to its market position.

The competition is coming from two ends of the market. The first is low–budget, no–name products. That’s a reflection on the rising cost for sellers on Amazon , particularly those from China. The Chinese e–commerce competitors have low costs and demonstrate incredible speed and agility in adapting their product portfolios, a combination that is difficult to imitate. Secondly, Amazon has managed to become the go–to destination for product information and research, creating a powerful touchpoint in customers’ journeys. But influencers and opinion leaders on social platforms like Instagram and TikTok are growing their reach in product advice (and advertising). While so far it is mostly left up to brands and retailers to leverage this strength, a more direct “commercialization,” as already witnessed in the Chinese market, would pose an imminent threat for the incumbent market leader.

Still, Amazon’s global expertise and established customer trust can serve as a valuable asset for succeeding in this evolving competitive landscape. Amazon has positioned itself as a trusted player, delivering quality as well as premium customer service (for example, return policies and Amazon Prime). So, while Chinese players are likely to gain popularity among the younger demographic — which is characterized by a strong affinity for e–commerce, more limited purchasing power, and an openness to explore — the older population is likely to remain loyal to Amazon.

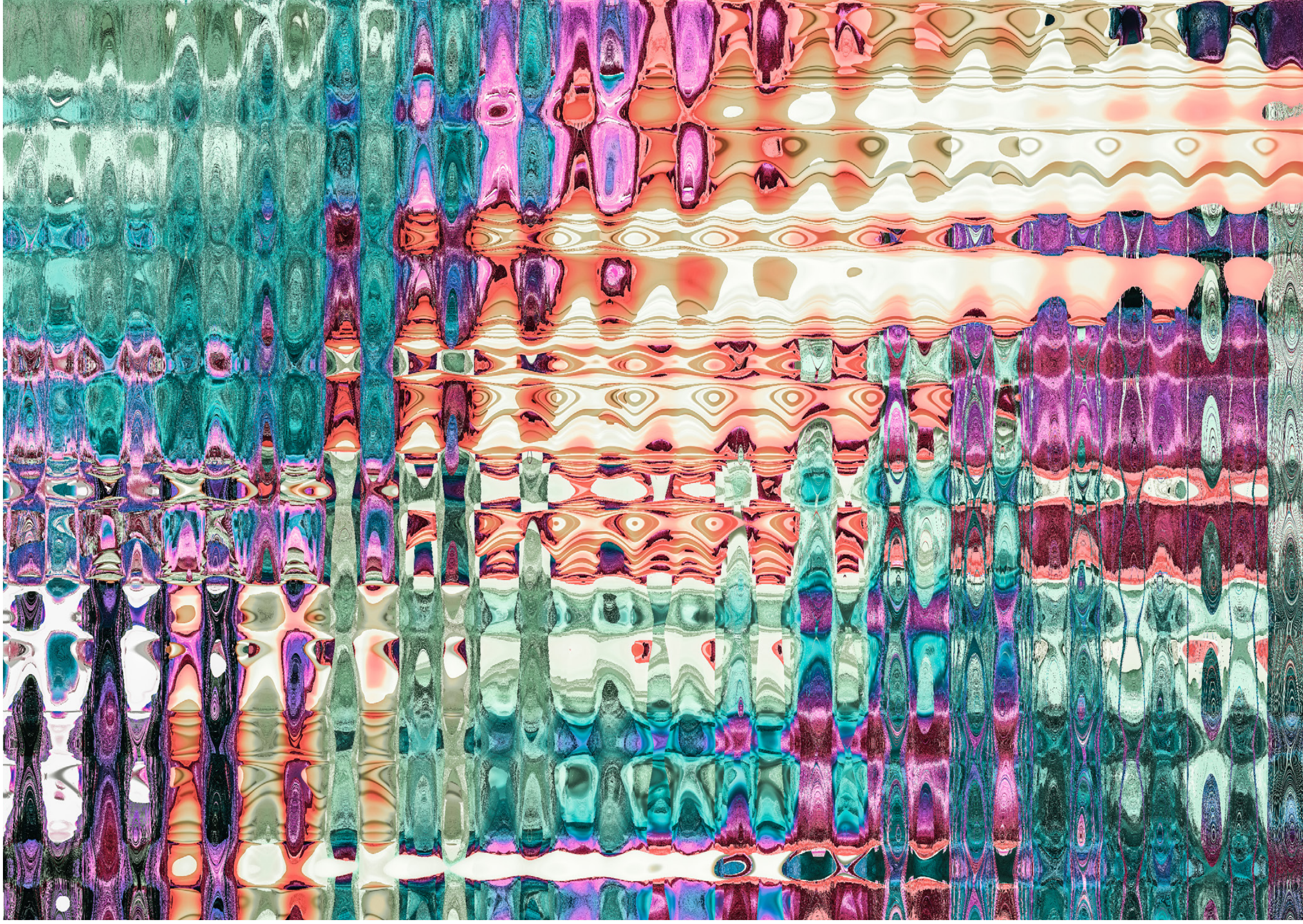
IMPLICATIONS FOR BRANDS AND RETAILERS NAVIGATING THE NEW E-COMMERCE LANDSCAPE

Brands need to prepare themselves to penetrate the new channels, accelerate their retail capability building, and review their strategies. It is important to allocate marketing dollars and e–commerce capabilities appropriately and look out for synergies (category, price, promo) across platforms.

However, capabilities are often transferable across channels . In the past Instagram was the place that brought the influencer economy to life. Tik Tok has quickly taken over and put an even more commercial spin on it. Tik Tok has also become a serious competitor for Google in terms of advertising revenue.

Discussions with manufacturers and retailers clearly show that TikTok is on track to become the most attractive marketing platform for consumer brands. The more fragmented e–commerce landscape is a double–edged sword. On the one hand, brands need to build presence on more platforms, which requires a more even distribution of resources and higher overall investment. And earlier efforts to build differentiated positioning for different platforms based on different segments are likely to be down the drain.

At the same time, this increasing number of options available to customers due to this fragmentation may give them greater bargaining power in terms of traffic, promotion, and consumer data visibility. Brands also need to reflect on how new e–commerce platform opportunities might contrast with the sustainability goals they have set. The agility and speed demonstrated by those platforms, in particular Shein, come with ethical concerns over labor practices and sustainability that could affect brand reputation.



ECOSYSTEM

8 LESSONS TO MASTER PERSONALIZATION IN THE RETAIL INDUSTRY

Leverage personalization to win customer loyalty

Frédéric Thomas–Dupuis
Randall Sargent
Danny Zhang

Customers are increasingly expecting personalized recommendations, offers, and greetings through a seamless omnichannel experience. In fact, according to Salesforce, 73% of consumers expect brands to understand their unique needs and expectations, while 56% expect all offers to be personalized. Globally, 70% of business leaders are boosting investments in personalization, business intelligence platform Statista finds.

However, while many retailers have only recently developed personalization capabilities, and few have truly mastered them, we can learn from the common mistakes observed in the industry.

1. START WITH A COORDINATED VISION

Personalization can mean different things to different people, from personally greeting top customers to personalizing search results on a retailer's webpage to serving up the next best–personalized offer. Without a coordinated vision, efforts can appear disjointed to customers who receive mixed messaging and overlapping deals. As retailers embark on building personalization capabilities, it's important to build consensus around a clear destination so various teams can work towards the same goal.

2. INVEST IN YOUR LOYALTY PROGRAM IN PARALLEL

Personalization requires rich customer loyalty data to make recommendations most relevant. Retailers should focus on driving loyalty sign–ups through in–store signage (for example, QR codes) and campaigns (for example, extra bonus points for creating a profile or downloading the app) in parallel to or in advance of building personalization. In a recent pilot, we found that a combination of personalized communication and in–store signage and kiosks resulted in 14% more new sign–ups. Personalized offers and communication can help drive engagement, but retailers need a strong foundation of customers they can track and reach to reap the full benefits of personalization.

3. PERSONALIZATION IS NOT JUST ADVANCED TARGETING OR SEGMENTATION

True one–to–one personalization requires a complete flip in mindset from the traditional ways of marketing, where a company develops an offer or campaign and then determines the right customer segment to send it to. A better approach is to start with customers and determine through a combination of business rules (for example, what are the priorities and strategic decisions to layer in) and algorithms (for example, collaborative filtering, and propensity modeling) what each should get from a bank of content, offers, and campaigns.

4. OFF–THE–SHELF TECHNOLOGIES ARE (OFTEN) NECESSARY BUT NOT SUFFICIENT

There is no single solution that comprehensively delivers one–to–one personalization. Instead, building a personalization capability requires stitching and tailoring various types of technology together: New machine learning/artificial intelligence algorithms ("the brains") should be built in a flexible and scalable environment and delivered to customers via existing off–the–shelf solutions. In a recent pilot, we leveraged the retailer's CRM software to deliver personalization to customers, feeding it the outputs of algorithms we built that flexibly ranked the most relevant offers for each customer.

5. CURATING EXISTING OFFERS DRIVES SIGNIFICANT VALUE

Many retailers feel that personalization requires multiplying their volume of content, offers, and campaigns. In reality, they can drive substantial financial impact through curation of what they already have. For example, a South American grocer recently launched a personalized digital flyer that led to a 2%–5% increase in customer spend, simply by curating existing offers and content without introducing any new personalized offers or discounts.

6. GENERATIVE ARTIFICIAL INTELLIGENCE (AI) CAN HELP, NOW

Generative AI can help to increase the amount of content, offers, and campaigns without requiring significant additional creative resources. We've tested leveraging generative AI to personalize email greetings to customers, finding that it drives twice as many click–through rates. This new technology requires human oversight and review but can massively accelerate creation.

7. DESIGNATE A CROSS–FUNCTIONAL TEAM

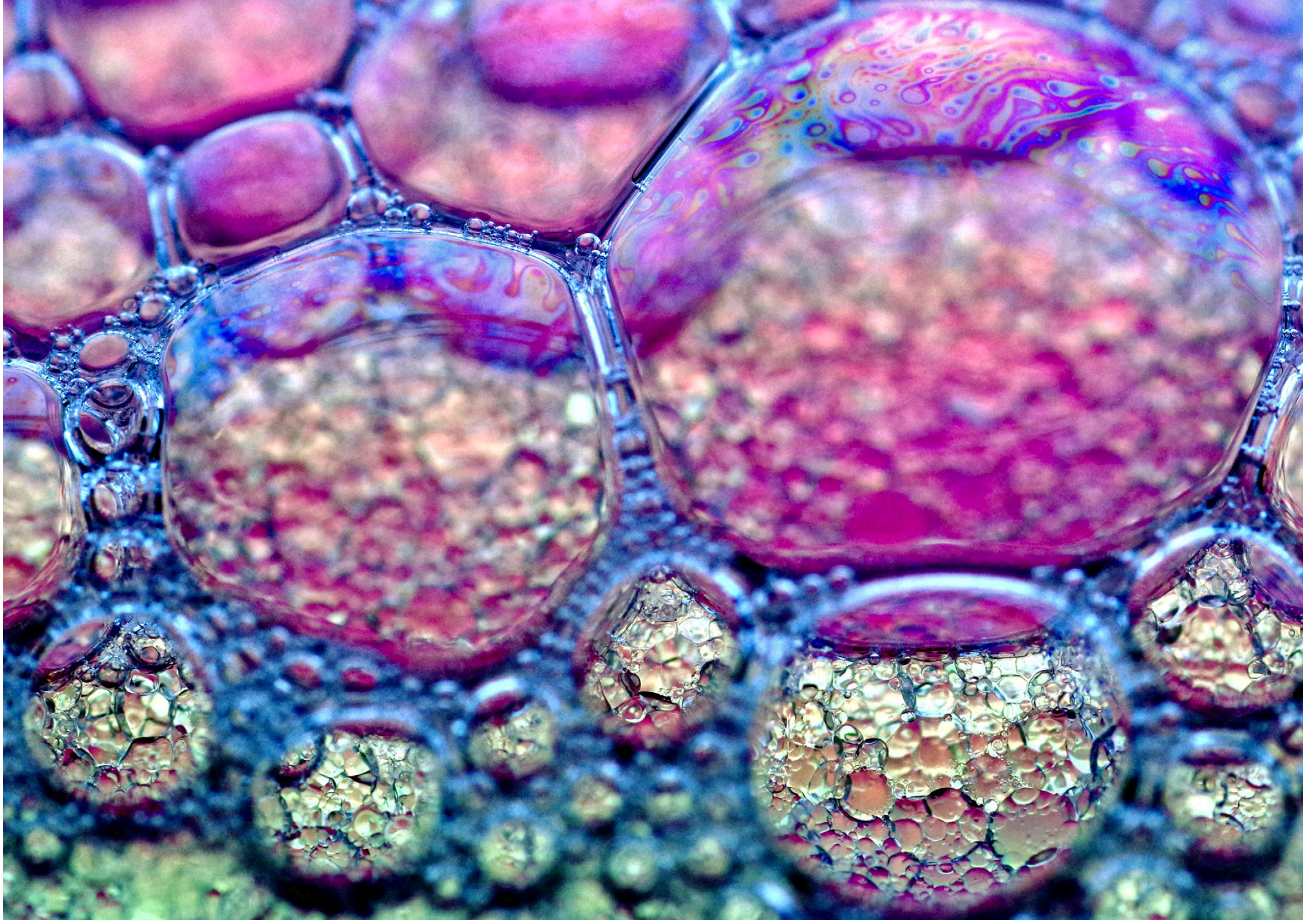
Personalization requires coordination across many parts of the organization, including digital, marketing, merchandising, and IT. We see the most effective organizations creating a small, dedicated cross–functional team focused solely on building and sustaining personalization capabilities and coaching and challenging the rest of the organization to make use of what's available.

8. TAKE ACTION BEFORE EXTERNAL DISRUPTION FORCES YOUR HAND

In jurisdictions around the world, local governments are starting to limit print flyer distribution or ban it altogether for environmental reasons. In other markets, sudden increases in printing and distribution costs can leave retailers stranded. Creating a digital alternative that can be personalized will allow retailers to stay on the front foot.

The rapid advance of technology has opened the doors for exciting personalization opportunities. As retailers develop these capabilities and unveil this technology, it will be important to keep these lessons top of mind.

Additional contributor ***Felix Dumont***



ECOSYSTEM

MIDDLE EAST RETAILERS ARE FOSTERING A WAVE OF INNOVATION

Navigating challenges in the retail landscape

Joe Abi Akl
Sirko Siemssen

Large companies dominating the retail and hospitality sectors in the Middle East are driving ambitious agendas around new customer ecosystems and platform businesses. We recently had the opportunity to discuss these trends with Joe Abi Akl, our newly appointed head of the Retail and Consumer Goods Practice in the India, Middle East, and Africa (IMEA) region.

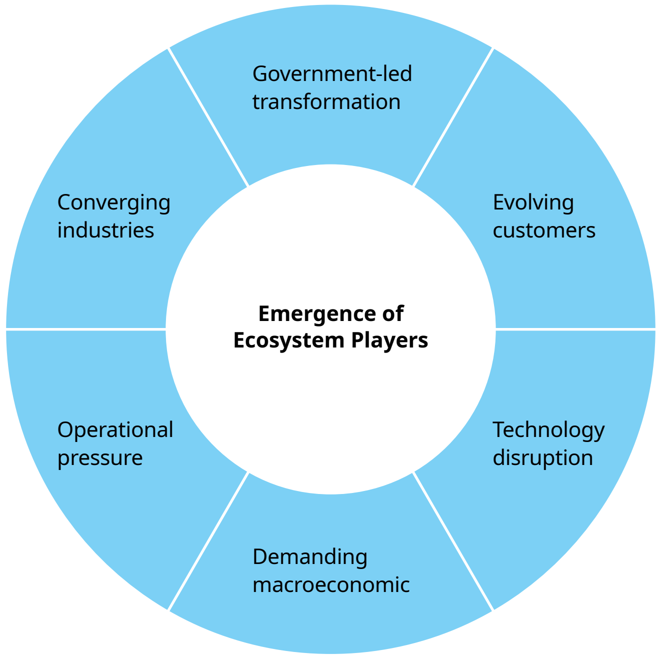
Joe has more than 17 years of experience and recently held key positions at Majid Al Futtaim, a leading consumer and lifestyle conglomerate across the Middle East, North Africa, and Pakistan, where he was instrumental in transforming the business and creating its integrated customer proposition. Joe has also served on the boards of leading startups and on several councils at the World Economic Forum, further enriching his diverse experience in the retail sector. A significant part of his contribution is the establishment of Xsight Future Solutions, a platform anchored in the most comprehensive customer data platform across the region, which has been instrumental in driving transformation and fostering accelerated growth in the region's retail sector.

Sirko Siemsen, global practice leader for Oliver Wyman's Retail and Consumer Goods Practice, spoke to Joe about industry trends, operator challenges, and "build the future" strategies.

Sirko: What excites you about the retail and consumer sector in the IMEA region?

Joe: Everyone knows about the region's strong retail and consumer sector growth in terms of transactions and value. But what I have been focused on are the emerging customer ecosystems (Exhibit 1) and platforms in this region and the blurring industry lines. They are big in ambition, differentiated in terms of customer experience, and effective in driving new income streams — even by global standards. And this is just the beginning: I believe we will see more acceleration of these trends and eventually advanced convergence of retail with entertainment, hospitality, food, banking/payment, communication/media, transportation and travel into a holistic, seamless customer experience across all channels.

Exhibit 1: Trends driving the emergence of regional ecosystems



Source: Oliver Wyman analysis

Why am I confident? Because the region provides a unique combination of demand and supply characteristics. Demand is rapidly growing, driven by a young, affluent population and increasing modernization as well as by more visitors coming to the region. In addition, consumers in the region are used to digital engagement and personalized services. Even after the end of the COVID-19 pandemic, the region is still seeing steady growth in the adoption of digital and omni channels. E-commerce sales are expected to grow at a compound annual growth rate of more than 20% from the current level of US $35 billion. Furthermore, regional customers expect personalized products and services by more than 30% than their global peers and they believe these will significantly influence their in-store and digital experiences.

The supply side deserves special attention, too. We see an ever-growing supply of real retail destinations that builds on the demand growth and delivers genuinely different and experiential shopping experiences. Also, what makes the region different from others is the number of companies active in multiple customer-facing verticals, including different combinations of retail, entertainment, and hospitality as well as real estate development. They are naturally keen to leverage and connect these touchpoints into a holistic customer experience.

The result? This ecosystem approach will have the potential of enabling a revenue pool of $1 trillion across the Middle East North Africa (MENA) region. As Jack Ma said, "I always believe we shouldn't build an empire. Instead, we should build an ecosystem. Every empire will be toppled someday, but an ecosystem is sustainable."

Sirko: What challenges do operators, especially incumbent conglomerates, face in the retail and consumer sector?

Joe: Despite the Middle East's overall opportunity and strategic promise, companies active in the region face significant challenges. The lack of economic integration across the region makes operations complex and difficult to navigate. Retail and consumer companies working in the MENA-region, with its more than 500 million consumers, face varying market dynamics and regulations. Therefore, the Middle East's retail industry remains somewhat fragmented, and many small and midsize operators struggle to tap into economies of scale.

Larger conglomerates, on the other hand, face siloed customer, data, and tech infrastructures. On top of that, given its growth and inherent promise, the region attracts more competition — from both inside the region and from global leaders, including lots of direct-to-consumer businesses. In addition, many family-owned enterprises are also facing questions around governance, the viability of their operating models, and succession as they mature and grow. All these companies are battling for the same customer, talent, and profit pools.

Putting it all together: most operators in the region face three overall strategic needs: 1) Transform and protect the core to deliver on its full potential; 2) Build for the future through the design of winning ecosystems and by tapping into new income streams; and 3) Upgrade capabilities to deliver both.

Sirko: What is an effective approach for enhancing core operations, and developing necessary underlying capabilities?

Joe: Companies should aim for a strategy with three horizons (Exhibit 2). Horizon one is focused on accelerating the core, which is very much about better insights, decisions, and results in all key customer, commercial, and operational areas. Flawless execution and ruthless follow-up are a must to get the bottom-line improvements needed to fund investments into the future. Horizon two is about augmenting and complementing the core by corner stoning into adjacent verticals or partnering with third parties aiming for a broadening of customer touchpoints and relevance.

Very much linked to this is horizon three, which aims at establishing ventures on the foundation of that broadened customer appeal, the extended customer reach, the intensified customer engagement, and the underlying data and insights. Both horizons two and three need to happen in sync, with a strong focus on growth, business cases, the right balance of investing and generating funding, and traction measurement.

Given lead times and the speed at which demand, and supply are evolving, I'm afraid all three horizons need to be addressed now. This in turn requires a clear vision and roadmap, ruthless prioritization, and very tight resource and financial management.

Sirko: In a "build the future" strategy, what are the key success factors to keep in mind?

Joe: First and foremost, this kind of strategy requires commitment from leadership, beginning with a bold vision that extends beyond mere financial targets. Of course, the vision also needs to be relevant to external stakeholders. Developing a magnetic customer platform proposition also requires scaling an ecosystem that expands into new external footprints. In addition, success is predicated upon five further factors:

1. **Developing scalable and integrated digital and analytics capabilities to deliver a personalized customer experience.**
   Personalization is the single most effective lever for scaling, starting with unifying and harmonizing data across all touchpoints and building digital twins of customers, which can be used from process optimization and customer lifetime value maximization to developing common customer engagement platforms around loyalty, payment, and customer value management.
2. **Monetizing existing capabilities and expanding into new adjacent verticals.**
   Companies should pursue diversification opportunities that complement existing businesses. By adopting an asset-light approach, they can drive synergies, deepen customer relationships, and build higher-margin revenue streams across data, digital, and fintech solutions.
3. **Leveraging and enabling the ecosystem.**
   Companies should embrace an open ecosystem mindset by establishing strategic partnerships with engaged customers at the core of the ecosystem. By leveraging external capabilities and actively collaborating with disruptive startups, companies can tap into a wider range of offerings and enhance convenience for their customers. This approach not only increases customer stickiness but also fosters stronger network effects by capturing a more comprehensive and diverse set of customer data. Ultimately, building ecosystem coalitions can attract a larger customer base and drive business growth.
4. **Employing an active portfolio approach.**
   To achieve this requires dynamic capital allocation to balance between a short-term return on investment and experimentation. Companies should remain committed to their long-term visions but embrace adaptability in divesting, investing, and allocating resources to established businesses versus new ventures, while considering the differences in risk, timeframe, success rate, and value creation potential.
5. **Championing talent as a competitive advantage.**
   Companies should adopt a dual approach to human capital: Build the right positioning as an employer of choice to attract talent across the globe, and nurture a learning culture by reskilling, upskilling, and developing future leaders, delivered through internal academies and partnerships with academic institutions. Having said that, innovation can't be confined to a select group. Instead, it needs to be a collective effort leveraging the entire organization and its partners.

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Exhibit 2: Companies should aim for three horizons of a growth-focused transformation

	Horizon 1: Accelerating the Core	Horizon 2: Adjacent Verticals	Horizon 3: Explorative Ventures
Focus	Protect and increase profitability of the core business	Reshape the business and incubate adjacent businesses	Explore options and place selected bets on emerging opportunities
Archetype	"Manager" Efficiency, customer intimacy, incremental innovation	"Entrepreneur" Developing and using IP, exploiting current capabilities, appetite for change	"Innovator" R&D, unfettered experimentation, blue-ocean opportunities
Risk Appetite	Protecting from downside risk	Seeing value in opportunity leveraging existing assets (upside risk)	Investing calculated experimentation (high risk and high reward)
Resource Allocation	Majority	Gradual	Limited
KPIs	Bottom-line, profit, ROI, costs	Top-line, growth, market share	MVP, milestone-based, proof of commercial traction
Mindset	Structure, focus, optimization, governance	Adaptable, creative, evolving, collaborative	Agile, disruptive, challenging, differentiating, testing

Source: Based on IOD Directorship Program

While the adoption of a winning ecosystem mindset is often associated solely with tech giants, I firmly believe that applying this approach and its fundamental principles can prove even more impactful for well-established companies operating in the retail and consumer sectors.

RetailElements
An Oliver Wyman solution

INNOVATION

TECH SOLUTIONS FOR RETAIL MERCHANDISING SUCCESS

The future of retail management is being reshaped

Coen de Vuijst
Dominik Böhler
Alexander Mol

The future of retail management is shaped by technology, providing customers with a personalized, multi–touchpoint shopping experience while accelerating the innovation cycle. However, estimating the pace of change, identifying fads from trends, and making the right technology investments are difficult tasks. With supply chain disruption and inflation impacting customer budgets, retailers must focus on merchandising and sourcing to maintain their competitive edge. Technology can help mitigate the risks of economic and geopolitical factors, as well as the growth of discounters and rising labor and energy costs.

Exhibit 1: Five critical areas of focus for technology in merchandising and sourcing

Priorities		Why do this?
1	Further automate the merchandising levers	• Make better decisions • Free up time and resource by automating
2	Bring an E2E cost view to optimise the business	• Reduce business complexity and operating cost • Win-win with customers by passing on savings
3	Look at your business through a customer lens	• Drive growth with profitable customers • Increase loyalty
4	Build a high-tech innovation function	• Differentiate! Offer products customers cannot get anywhere else
5	Leverage sourcing scale and get more for less	• Best possible prices in branded • Amazing product and price in OL

Source: Oliver Wyman analysis

PRIORITY 1

FURTHER AUTOMATE THE MERCHANDISING LEVERS

Retailers are striving to reduce their reliance on manual processes and spreadsheets by incorporating automation and advanced analytics into their systems. Tech companies that have entered the retail space have successfully implemented highly automated processes that are supervised by humans, which has resulted in lower costs, faster operations, and fewer errors. Retailers must close the automation gap to stay competitive. Automated promotion management, for instance, could include predictive analytics that generate promotions automatically and individualized digital leaflets that combine mass and individualized promotions. Automation can also optimize businesses by integrating insights from price, promotions, assortment, and supplier management. This could reduce personnel requirements and increase efficiency in merchandising and sourcing departments by up to 60%.

PRIORITY 2

BRING AN END TO END COST VIEW TO OPTIMISE THE BUSINESS

In the highly automated world of tomorrow's merchandising and sourcing, strategic goals and daily actions will be closely intertwined, much like an autonomous vehicle, where destination input leads to efficient navigation. To achieve this, specific instructions are essential. Understanding cause and effect is crucial to make informed decisions, including how merchandising and sourcing affect cash flow and the bottom line. Currently, such insights are limited to gross margins or derivatives. Decision–makers need profit and loss (P&L) insights at the product and customer level, accounting for all costs, including cost of goods sold (COGS), supply chain, store labor, waste, marketing, and home delivery. This comprehensive view of the business will allow better decision–making in areas such as macro and micro assortment optimization, supplier negotiations, and customer acquisition and retention.

PRIORITY 3

LOOK AT YOUR BUSINESS THROUGH A CUSTOMER LENS

A true customer perspective becomes increasingly important and personalized promotions and customer segmentation are no longer enough. To achieve true customer centricity, retailers must prioritize the acquisition, development, and retention (ADR) of customers and determine the personalized “best action” for each customer to move them through the ADR cycle. Retailers can use customer insights to improve their business by integrating ADR insights into core merchandising decisions, developing a "personalized next action" capability, and creating customers–for–life through new services like personalized apps for budget management, health, cooking, and sustainability. By focusing on ADR, retailers can build long–lasting loyalty and add meaningful value to their customers' lives.

PRIORITY 4

BUILD A HIGH–TECH INNOVATION FUNCTION

Retailers have an advantage over fast–moving consumer goods (FMCG) companies in building successful direct–to–consumer models. To gain deeper insights into consumers' behavior and unmet needs, retailers should blend human imagination with advanced technology. Behavior data analysis can help identify gaps in customer decision trees and discover latent needs. AI technology can scan external data for untapped trends, while human creativity can enhance insights. Retailers can turn these insights into action by investing in robust product management processes and collaborating with strategic suppliers for research and development (R&D) support. Innovative products can help retailers stand out from discounters, win the battle for customers, and provide offerings that are not found elsewhere.

PRIORITY 5
LEVERAGE SOURCING SCALE, AND GET MORE FOR LESS

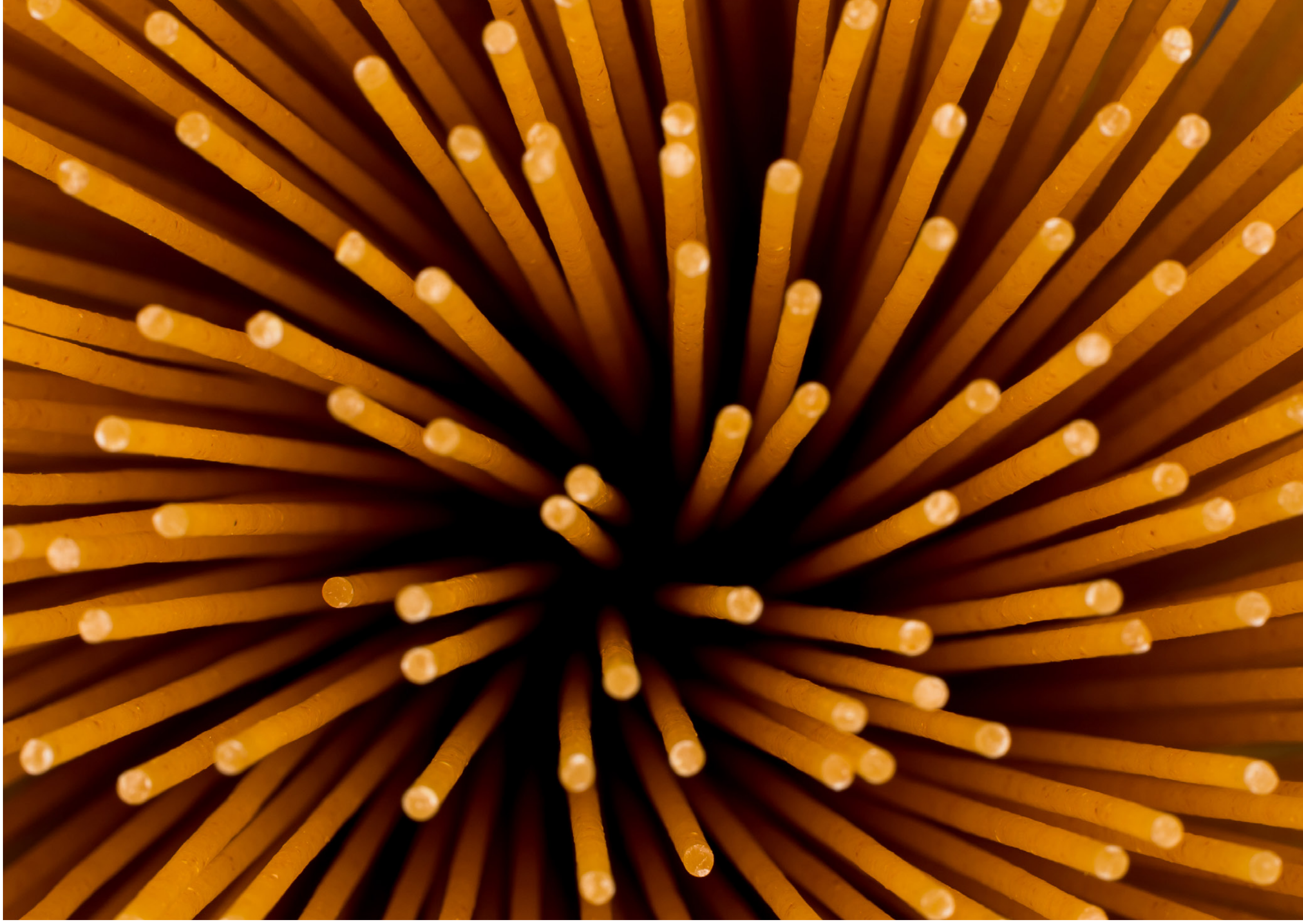
Branded and own–label sourcing require different approaches. Branded sourcing involves obtaining accurate comparisons and standardizing terms to leverage international scale, while advanced technologies like fuzzy matching and interpolation can expand comparisons and counteract price differentiation. Collaborative sourcing involves working with a select group of major suppliers to reduce costs and accelerate new product development. Own–label sourcing requires strategic and collaborative work with suppliers through multi–year agreements, open book arrangements, and value engineering to optimize specifications. Advanced retailers will increasingly utilize cost models based on commodity prices, labor costs, and freight to challenge supplier quotes. The automotive industry offers insight into future retail sourcing with sophisticated cost models and should–cost analyses.

REVOLUTIONIZING RETAIL

Retailers can use technology to improve merchandising and sourcing decision–making, gain granular P&L insights, and offer highly personalized customer experiences. Full–service retailers should leverage technology to support innovation, improve sourcing processes, and transition to more collaborative models. However, to succeed in the digital age, retailers need to recruit and retain a new mix of talent. Retailers should be realistic about what technology to deploy, improve their technology and data foundations, and develop new functionality while improving legacy tech in parallel. Retailers who make technology a core part of their strategy and make the right choices on technology deployment will be the winners in the future tech–driven world.

Read more

FUTURE OF MERCHANDISING



INNOVATION

STRATEGIES TO HELP SOLVE THE PRIVATE LABEL DILEMMA IN RETAIL

The new reality of private label in retail

Sirko Siemssen
Meryem Ben-Goumi
Vikram Dhaliwal
Alexander Pöhl

On top of inflation–induced cost price volatility, retailers are now facing the fallout of consumers shifting to less–expensive channels and product ranges. The latter has cost European retailers more than €700 million of annualized commercial margin already, turning many private label portfolios into liabilities within just 12 to 18 months. As consumer spending may not return to pre–2022 levels for several years, it is critical for retailers to address this challenge seriously and head–on. In our report Addressing The Private Label Dilemma In Retail, we highlight the actions to consider based on our experience working with retailers over the past decades.

At first glance, the growth of private label is good news. As cheaper alternatives to branded products, private label lines should allow to slow the shift to cheaper competitors or channels, while also helping consumers through the cost–of–living crisis. However, the shift puts pressure on retailers' margins also, with volumes flowing to lower– and low–end range products that dilute overall profitability. As a result, while the first wave of challenges rooted in the return to inflation has been difficult to absorb, this second–order effect will create even more challenges.

The strategic intent behind added–value private label lines is clashing with the new reality of crumbling volumes during the cost–of–living crisis. Retailers must decide how to continue winning through private label while improving economics.

Our private label playbook comprises a comprehensive set of recommendations for doing so effectively.

IMMEDIATE ACTIONS TO IMPROVE PRIVATE LABEL MARGINS

Stop the margin erosion and enhance your ability to act based on better control and steering of product–switching dynamics. These are some key steps to follow:

1. **Perform a rapid private label assessment**
   What are the results of mix–changes? What are the underlying switching dynamics? Which internal sourcing capabilities and how can they be improved?
2. **Get systematically on top of private label cost of goods sold and commodity cost opportunities**
   What is the input cost evolution across all private label products? What benefits does AI automation offer in understanding navigating input cost modelling complexities, and providing leverage in negotations with manufacturers?
3. **Run fast–track category resets based on a thorough understanding of consumer product switching behavior**
   How to optimize product allocation, store placement, and pricing to positively impact switching dynamics, prevent slippage, and maintain price perception targets?

PRIVATE LABEL ACTIONS FOR THE LONG TERM

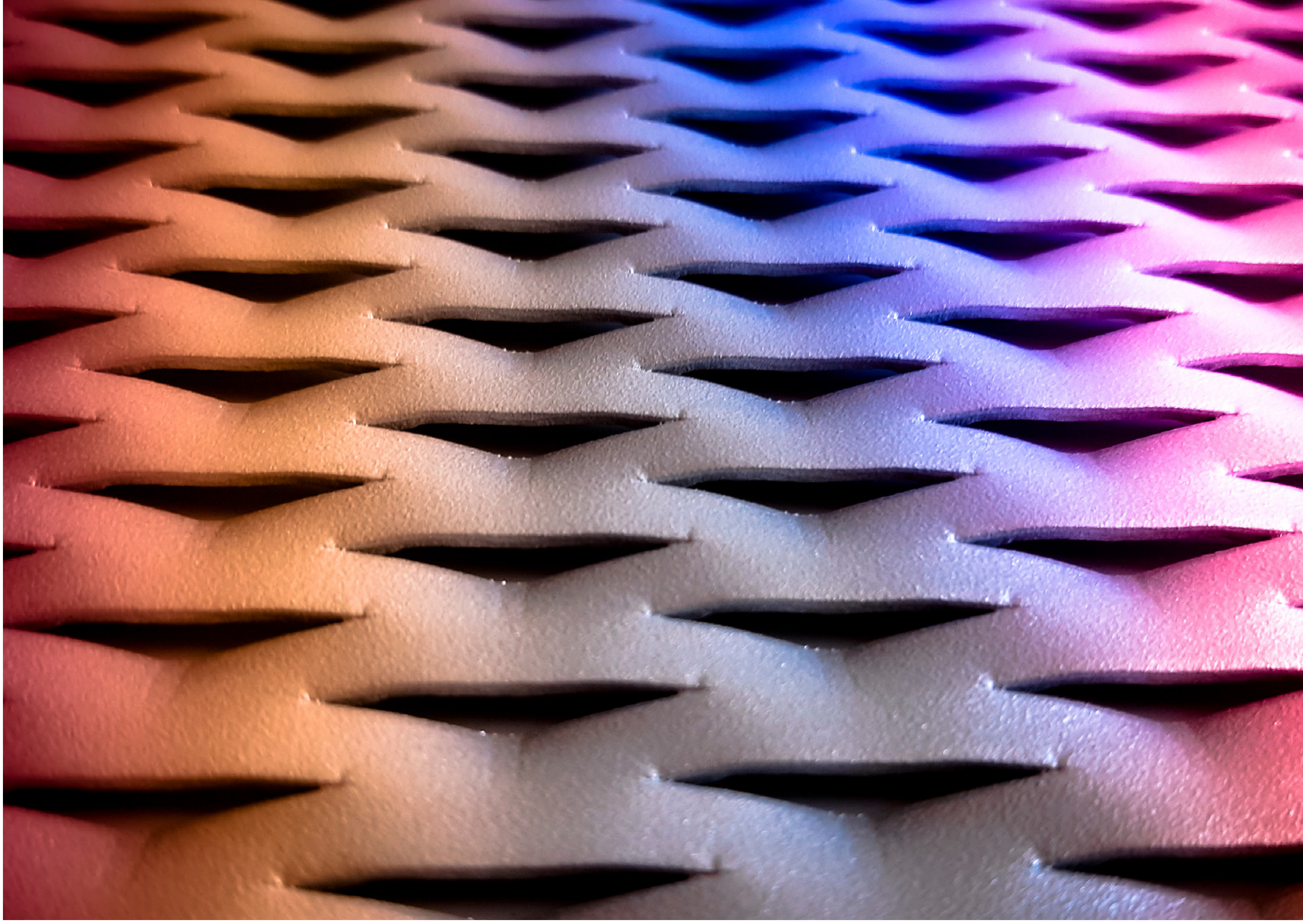
The current crisis is a reminder that the substantial enhancements to private label management capabilities of the last decade are just the beginning. In most cases, there are still gaps in product management and operations capabilities as well as in reaching meaningful scale. Things to consider:

1. **The next private label customer proposition**
   Recalibrate your north star and reposition your portfolio. Consider what you want to grow and focus on. Translate strategy into action by defining operational targets and guidelines at a granular level.
2. **Develop true product cost–management capabilities**
   Move towards a true product company mindset that considers customer proposition, product cost, and supply chain as one.
3. **Get real in terms of scale and focus on volume bundling**
   Combating margin erosion requires a focus on volume bundling through alliances, backed by top–down guidance and incentives to overcome internal resistance.

Since 2022, retailers are mostly reacting to cost of goods sold (COGS) inflation via negotiations and pricing. As the dust settles, it’s becoming clear that retailers face another wave of challenges driven by consumers trading down to the bottom–end of their private label portfolio. This opens gaps in their profitability picture, while the declining volumes in the upper parts of the portfolio raise core strategic questions. The time has come to review assortment and private label propositions, as well as underlying capabilities, to navigate the storm successfully and come out on top.

Read more

ADDRESSING THE PRIVATE LABEL DILEMMA IN RETAIL



INNOVATION

SOLUTIONS FOR DEALING WITH INVENTORY TURNOVER CHALLENGES

How retailers manage inventory in the face of new challenges

Bobby Gibbs
Purav Adiecha

As companies look ahead to the second half of 2023, they face continued macroeconomic uncertainty. One thing they know for sure is that they continue to face interest rates higher than at any point in the last 15 years thanks to 11 rate hikes by the US Federal Reserve since the beginning of 2022. Higher interest rates mean additional attention to cash flow management.

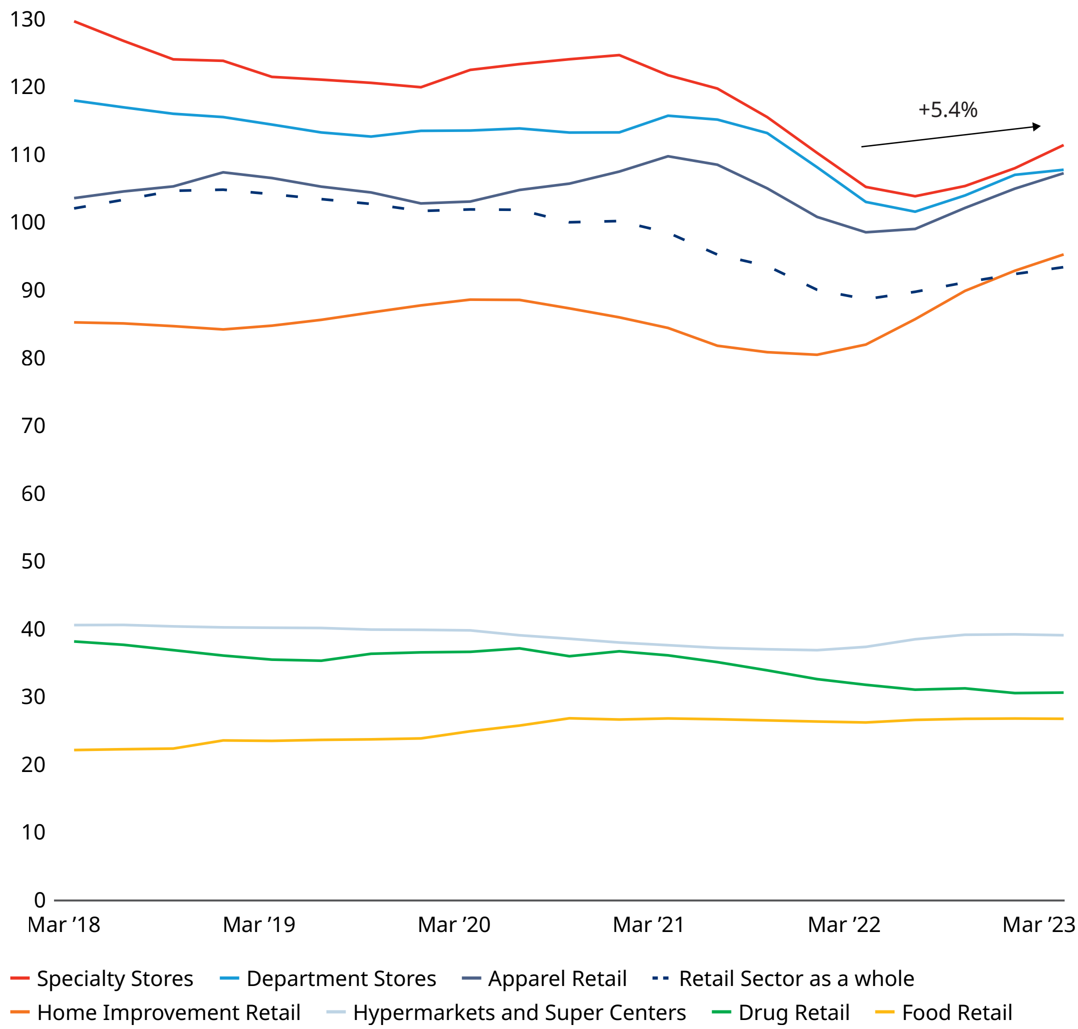
Retailers in many sectors have already suffered from the cutback in consumer spending since interest rates began to increase. This trend may be exacerbated as the Fed is considering raising interest at least one more time before the end of the year. For retailers with high debt loads, an improved working capital position is an essential lifeline. Even for those who have strong balance sheets, the increased carrying cost from the current interest rates could be worth $544 million across retailers in the S&P 1500 Composite.

A KEY MEASURE OF WORKING CAPITAL EFFICIENCY

For any company, there are three key measures of addressing working capital efficiency: Days Sales Outstanding (Accounts Receivable), Days Payments Outstanding (Accounts Payable), and Days Inventory Outstanding. Receivables outstanding are rarely an issue for retailers, as customers typically pay in cash or with credit cards (which have very regular, on-time collections). Retailers can address Days Payments Outstanding (DPO) with the right vendor engagement approach, but these concessions often create a zero-sum proposition when negotiating against vendors. Our experience has shown that the opportunity for savings on Days Inventory Outstanding (DIO) can create more sustainable value.

Some retail sectors require more inventory than others. Inventory levels in retail are generally down since 2018 but have ticked up since last year as shown below. Home improvement retail has seen the greatest increase over this period (approximately 16% year-over-year and 2% annualized since Q1 2018). These retailers are expecting a decline in sales in 2023, which will exacerbate this issue.

Exhibit 1: DIO for select industries within the Retail Sector shows a recent spike in inventory gluts



Source: S&P CapIQ, S&P Composite 1500 data

SOLUTIONS FOR STRUGGLING INVENTORY TURNOVER

Below are some solutions we propose for companies that are struggling with inventory turnover. These solutions have been implemented by Oliver Wyman clients in the past and are based on the experiences of our internal retail experts.

ADD THE COST OF INVENTORY TO MERCHANDISING REPORTING AND INCORPORATE INTO GOVERNANCE

What gets measured gets managed; therefore, incorporating Net Working Capital (NWC) and its drivers into merchandising reports will bring more attention to those metrics from the business. This can be accomplished either by adding these NWC metrics to existing reports or in standalone reports that are more "cash culture"–focused. Key metrics to incorporate include days of inventory outstanding, carrying cost of inventory, inventory on hand, and days of net working capital. Management will then be better informed to take action.

IDENTIFY HIGH-INVENTORY STOCK-KEEPING UNITS (SKUS) FOR DISCOUNT AND SERVICE LEVEL ADJUSTMENT

At nearly every retailer, we see certain SKUs accumulate excess inventory. By starting with those, we can not only unlock quick wins but also find the structural reasons causing this inventory to build up. At this point, management will work to reduce the buildup from two angles:

Flush out stock: Management can expedite the sale of built–up stock through a combination of promotional methods (targeted offers) and changes to planogram facings (movement of slow–moving SKUs to more favorable in–store locations).

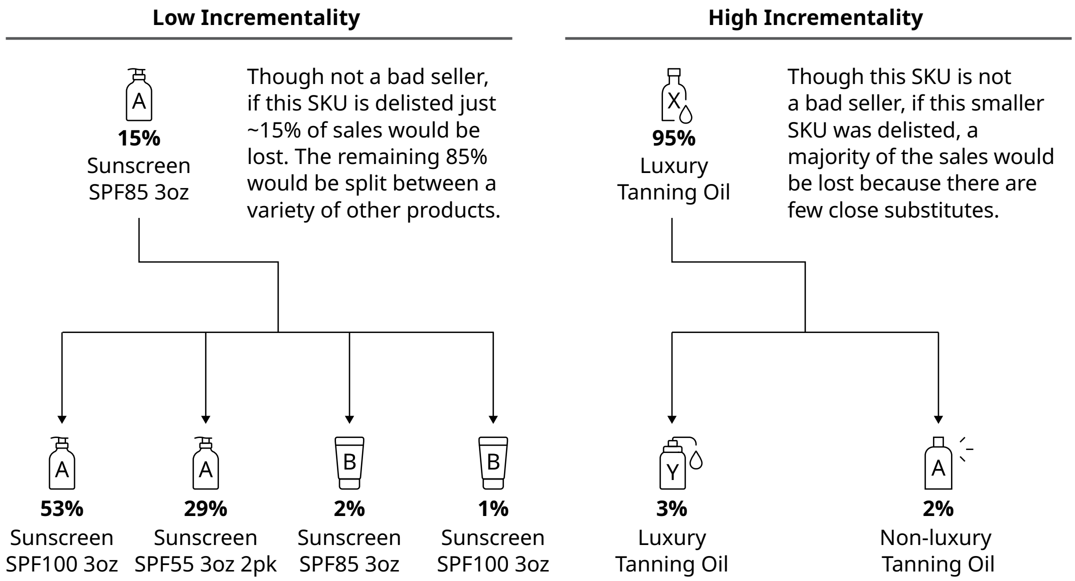
Adjust replenishment: Any recurring orders for the high–inventory SKUs should be reevaluated to reduce either the quantity or frequency of orders.

REDUCED STORE-LEVEL ASSORTMENT THROUGH CLUSTERING

When reducing store–level assortment, it's essential to identify "safe" candidates for delisting — those where a high percentage of lost sales for the specific product would be redistributed among other products in the same "cluster." In the switching analysis example below, the product on the left has near substitutes that would absorb a large percentage of the sales should the product in question be delisted. The same can't be said of the product on the right, which would result in an almost complete loss in sales if the product were removed from the inventory mix.

Exhibit 2: Companies should identify opportunities to reduce SKU counts through an incrementality–based measurement of assortments

Sunscreen lotion switching example



The goal is to ultimately identify "safe" potential candidates for delisting, resulting in an opportunity to flush out inventory

Source: Oliver Wyman analysis

POOL SWITCHABLE ITEMS FOR COMBINED SERVICE LEVELS

Switching analysis can also inform where products should be grouped to pool inventory in setting service levels. For highly switchable products (like the sunscreen on the left above), shared safety stock could service all of the products in that cluster, so that each product does not need its safety stock. By switching from servicing safety stock from the individual product level to the cluster level, the total amount of safety stock on hand is reduced substantially. A customer decision tree can be used to ensure that all products in the cluster are highly switchable.

CASE STUDIES
WHAT THIS COULD BE WORTH

RETAILER WITH MORE THAN $25 BILLION IN SALES (50% PERISHABLES)

The following case illustrates how a large retailer with perishables was able to reduce inventory and simultaneously optimize supplier performance.

Oliver Wyman was engaged to streamline supply chain management processes and governance. Approach and measures taken included:

- Needs–based planning for inventories, which allowed the client to reach optimal service levels
- Specific assignment of SKUs to storage locations to improve the flow of inventory — this improved the readiness of inventory for delivery by 1.4 percentage points for perishables and 1.3 percentage points for nonperishables
- Assortment review and SKU rationalization

These actions allowed the client to achieve **an overall reduction in inventory of 15%** (with an overall cost reduction of $25.2 million), **plus an 80% reduction in process disruptions** for incoming goods. The client then leveraged these wins **to negotiate more variable payment terms** with its suppliers, thereby improving working capital through an additional avenue (payables).

RETAILER WITH MORE THAN $10 BILLION IN SALES

The following case illustrates how a retail client (nonperishables) implemented inventory management solutions on a large scale. The company has a wide product mix (both slow and fast movers) that features both national brands and private labels and more than $10 billion in annual sales. As part of a wider initiative to improve internal capabilities, Oliver Wyman was tasked with reducing working capital in the business.

Solutions the client used to better manage inventory included:

- Governance: The company implemented a uniform set of managerial key performance indicators (KPIs), which gave management a more focused view of which inventories were stuck and should be moved through increased promotion and discounts.
- Clustered assortment: As described previously, Oliver Wyman grouped the client’s products into switchable clusters, which helped with SKU rationalization (and elimination) and created more manageable service levels of safety inventory.
- Supply visibility: The retailer implemented new forecasts and Material Requirements Planning (MRP) systems to better manage the inflow of inventory.

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The client was able to reduce its inventory by 25% by the end of the project while improving inventory availability by 1.2 percentage points and reducing inventory shrink by 2 percentage points. Newly implemented supply controls and KPI dashboards have helped the client ensure that the improvements made have been sustainable.

CONCLUSION: RETAILERS HAVE MULTIPLE OPTIONS WHEN IT COMES TO WORKING CAPITAL

In the face of increased uncertainty and higher interest rates, having more cash on hand or drawing less from a revolver is never a bad thing. For retailers to weather these conditions, they should be equipped with ample liquidity and processes that turn current assets into cash quickly. Inventory reduction and turnover improvement are ways that can have major impacts in this area, and many channels exist for accomplishing them.

***Joshua Korn** contributed to this article*

INNOVATION

STREAMLINING YOUR SUPPLY CHAIN WITH WAREHOUSE AUTOMATION

The secrets of the fully automated warehouse

Dustin Wisotzky
Cornelius Herzog
Christian Jobst

The goal of full warehouse automation might soon be in sight, at least for some.

The idea of automating the warehouse is almost as old as logistics and supply chain management itself. The prime motivation of automation is to increase warehouse productivity and profitability while improving overall efficiency in operations by eliminating human error. Rising labor costs, the challenges of constructing and operating warehouses in highly compact footprints in inner urban areas, and safety and environmental concerns have all fueled continued investment in increased levels of warehouse automation. That journey is now closing in on its end vision for a fully autonomous warehouse that can operate 24/7.

WHERE AUTOMATION IS TODAY

Most warehouses have now automated at least part of their operation. Retailers and fast–moving consumer goods (FMCG) companies often touch level 4 autonomy — where no human intervention is required — for at least some part of their operation. Warehouses at the leading edge deploy advanced hardware and software, where several hundred smart robots are deployed in the warehouse to store and pick goods in a complex, three–dimensional bin system.

It would be incorrect to assume that this level of automation has been achieved in all industries, however. The challenges of warehouse automation are specific to the industry. (See Exhibit 1.) Not only does the current level of automation vary greatly by industry but it can also vary even within the business. For instance, while carmakers and tier–1 suppliers often achieve high levels of automation in picking small components using fully automated systems that shuttle between store locations, these same businesses manage a much lower level of automation when having to handle a component portfolio that varies in size and weight.

As a rule of thumb, it holds true that the larger the item and the more diverse the product portfolio in terms of volume or weight, the more difficult end–to–end warehouse automation becomes.

Exhibit 1: Characteristic levels of warehouse automation by industry

Description

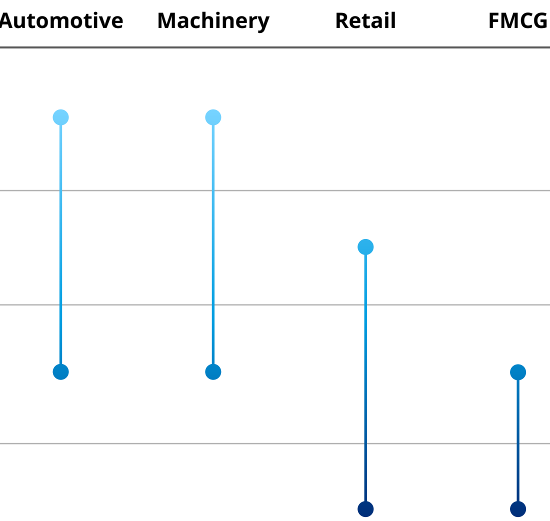
1 Manual warehouse
No automation used in the warehouse. All process steps are conducted by manual labour.

2 Assisted warehouse
Some process steps use mechanization to support manual labor, e.g., roller belts.

3 Partially automated warehouse
A part of the warehouse is automated while other parts use manual labour, e.g., automatic high bay.

4 Highly automated warehouse
Combinations of several automated processes are used, e.g., automatic unloading of trucks and storing to high bay.

5 Fully automated warehouse
No manual labour except for IT/service mechanics in the warehouse.



Source: Oliver Wyman analysis

CHALLENGES ON THE ROAD TO FULL AUTOMATION

Many solutions are now available “off the shelf”. The technology and systems needed to move a pallet automatically from a truck onto a conveyor and then into the storage warehouse in one seamless movement, one that then merges into automatic pallet storage within the warehouse, are readily available. The decreasing price of sensors, e–labels and machine vision systems ensure that the robots, automated machines and the various components of the automated system are all able to communicate with each other seamlessly.

The biggest challenge now facing warehouse operations is that many of these hardware andsoftware solutions are in effect “islands” — and there is no easy way to connect these islands to create a system that is fully autonomous. This is true especially for warehouses where the automation system has evolved over time, a situation more typical than not in most companies. The legacy of piecemeal acquisition ensures that it will inevitably be a major struggle to connect the patchwork of hardware, software, and IT–architecture solutions. This is a challenge full automation has to tackle. Thereby, it is of paramount importance for companies to develop digital supply chain capabilities, where not only the right hard– and software is required but also the right people and an organization that is capable of implementing and maintaining this setup.

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A second important issue is data: Poor data quality or data incompatibility can be the undoing of even the best of automation systems. Connectivity and data are the equivalent of the blood and the cardiovascular system of the autonomous warehouse. The hard truth is that almost all companies today struggle with getting their data right. At every step in the supply chain, it is essential to have accurate, real–time data, including for packing specifications and lot sizes. The data has to be exact in order to enable the machine intelligence to decide how to handle the various items.

GETTING AUTOMATION RIGHT

Compared to a conventional warehouse, a fully autonomous warehouse is more akin to a machine for production rather than being just a place for storage. Ensuring that the autonomous warehouse functions as desired requires the company to think afresh about the role of the warehouse itself — and link seamlessly into all adjacent processes. If the benefits of the autonomous warehouse are to be fully realized, it is necessary for the company to think about reshaping their operating model and accompanying organization, including the processes and IT systems, in order to ensure that they are all fully integrated.

These challenges can make the strategy, design and implementation of warehouse automation appear particularly daunting, especially for large corporations, such as those in retail, automotive or manufacturing, that often have enormous warehousing footprints located at hundreds of different sites.

THE PLACE TO START: TAILORING AUTOMATION TO BUSINESS AND SERVICE REQUIREMENTS

The vision of full warehouse automation is big lure for many Chief Operating Officers (COOs). The benefits are transparent, enabling a significant performance edge and future cost benefits. Yet full automation might not be desirable in all circumstances given the current state of technology. Depending on the industry, partial automation might well yield a more optimal outcome. To establish whether full automation is the right goal fo the business requires developing a full understanding of the company’s business and service requirements.

Customer and service requirements vary significantly between markets, customer segments and product groups. Rather than a one–size–fits–all approach, leading players follow a segmented approach to warehouse automation, tailoring their warehouse designs to the specific needs of individual channels, categories, and order profiles. They are careful to choose the right level of automation and the right technology for each of their segments, ensuring that what is implemented is able to provide the required degree of flexibility for a large spread of order profiles, fulfillment speeds, and scalability.

The answer to warehouse automation is more often than not to adopt a tailored approach, one located in the specific service requirements of the company. By thinking of the warehouse automation challenge in this way, the COO is able to start determining the most appropriate automation strategy for the company. Done right, this will set the road to full autonomy.

Retail**Elements**
An Oliver Wyman solution

SUSTAINABILITY

FOOD RETAILERS NEED TO ACT NOW FOR A NET-ZERO FUTURE

What to keep in mind when crafting transition plans

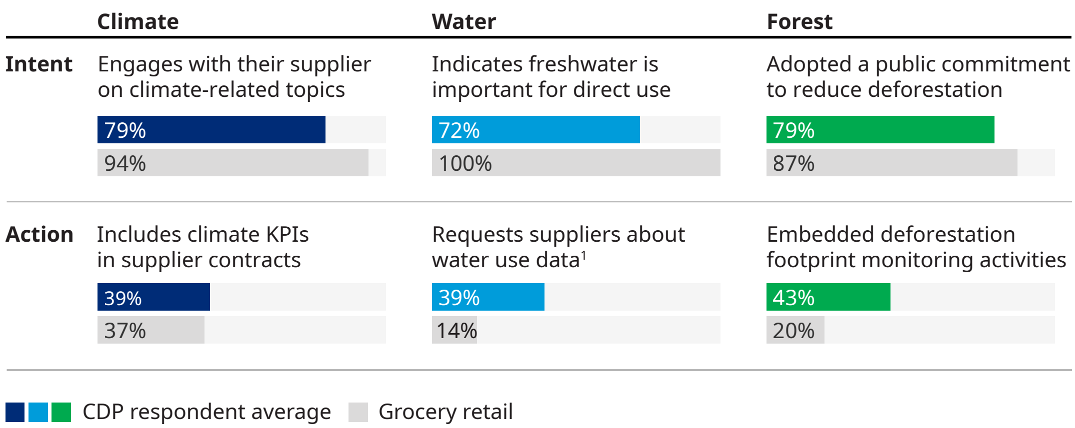
Suzanne van der Meijden
Coen de Vuijst
Julien Hereng

Agriculture and food systems are responsible for 31% of human–caused, greenhouse gas (GHG) emissions and are also among the biggest drivers of water use, land–use change, habitat destruction, and biodiversity loss. That's according to the latest CDP Europe report, which surveyed some 1,500 companies representing around 75% of European market capitalization on corporate efforts to cut emissions. The report is produced by global carbon monitor CDP and consulting firm Oliver Wyman.

While around half of the European companies that filled out the CDP questionnaire reported having 1.5°C climate transition plans, under 5% demonstrated advanced progress in developing ways to connect their transition plans with business plans. According to the report, the food industry has one of the widest gaps between its ambition to cut emissions and its practices.

This year's report featured a deep dive on grocery retail, describing the sector as strong on intent, but failing to translate the desire to cut emissions into action. In this deep dive, we will highlight key conclusions of the CDP report and next steps retailers should take.

Exhibit 1: Food retailers intent and desire to cut emissions into action



1. Respondents indicating that they do not know if they request their suppliers about water use are marked as no.
Source: Oliver Wyman analysis; CDP data; retail sector deep dive

Grocery retailers are among the most value–chain dependent sectors in the economy, with **97%** of their emissions produced upstream in supply chains or downstream with customers. These are referred to as Scope 3 emissions, and for companies, these emissions are among the hardest to quantify and reduce because they are not in the direct control of the manufacturer or retailer.

In practice, most grocers are not yet creating the kind of contractual relationships with suppliers that leverage doing business with them as incentive to cut emissions and protect nature. More than 70% of grocery emissions are being generated by these suppliers. Downstream, too, grocers could incentivize customers to buy products with smaller carbon footprints through pricing, assortment, and promotion practices.

THE KEY STEPS GROCERY RETAILERS MUST FOLLOW TO ACHIEVE CLIMATE GOALS

To make meaningful steps towards closing the delivery gap, grocery retailers need to act now, detailing out how they will achieve their climate goals. For grocers the key efforts are likely to be through departments sourcing products and those merchandising them:

Develop a sustainable procurement strategy:

- Screen the assortment of products and determine how to make it more sustainable by finding new products or new sources of old products that will reduce their carbon footprints. This may require bringing new suppliers onboard with more sustainable operations or in areas that regulate impacts on nature. It also may involve relying more on private label merchandise where grocers have more control.
- Make demands on suppliers about practices deemed acceptable and set targets for reduction of emissions. Be clear about the consequences if suppliers fail to comply, which could involve cutbacks in business with the supplier or the delisting of the supplier
- Monitor the progress of suppliers through clearly structured, regular data exchanges and help the supplier, if necessary, to develop tools to measure progress

Transform merchandising and guide consumers in the right direction. Then leverage the extra efforts in negotiations to encourage suppliers to participate. For instance:

- Provide attractive placement and increase promotion for sustainable products
- Decrease promotions that encourage waste or promote unsustainable products
- Adapt target margins for sustainable products to allow for more of them to be used

RETAILERS SHOULD KEEP THE FOLLOWING ELEMENTS IN MIND WHEN CRAFTING TRANSITION PLANS

- Approach the transformation with both top–down and bottom–up strategies to create a culture of sustainability in which central management and operational staff are all working toward net zero
- Be transparent about the short–term financial implications as well as long–term finance and risk benefits of the transition with stakeholders including financial institutions, shareholders, employees, and even customers
- Prioritize battles and commit only to achievable and meaningful actions — avoid announcing small, token measures
- Bring consumers on board, and keep in mind that readiness strongly differs per geography
- Anticipate that this is an effort that must be sustained over decades and through successive generations of managers to be successful

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As scrutiny of transition plans increases, grocery retailers will begin to feel the heat around emissions and their impact on nature. Being proactive will at least put companies on the right side of the debate.

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STEPPING UP: STRENGTHENING EUROPE'S CORPORATE CLIMATE TRANSITION

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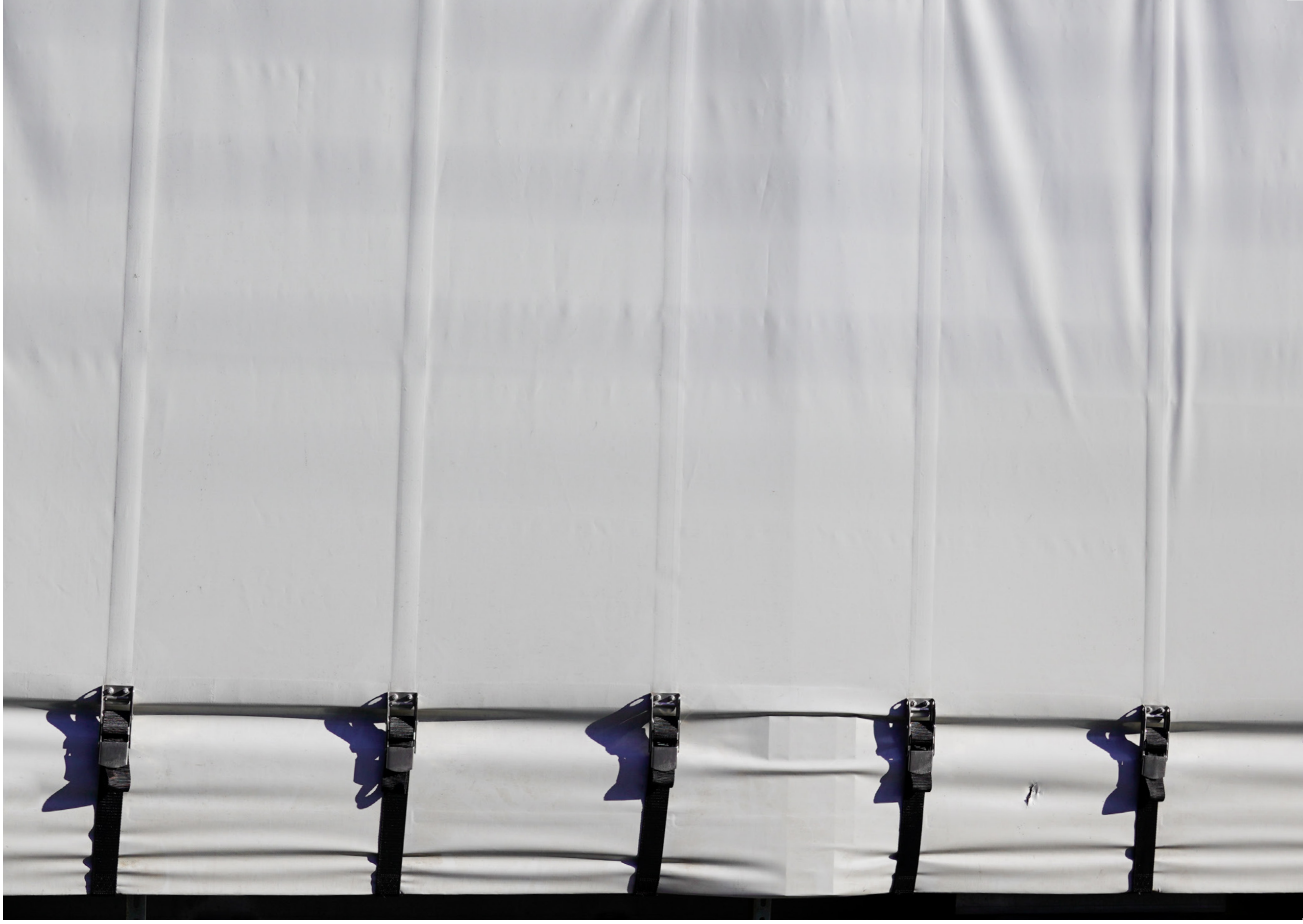


SUSTAINABILITY

DELIVERY DECARBONIZATION PATHWAY

How can e-commerce delivery become carbon neutral?

Mehdi El Alami
Dustin Wisotzky
Florent Gallon
Stefano della Rossa

The breadth of products offered through e–commerce has expanded, and more categories are now available online, from a greater number of vendors around the globe. Online and offline shopping are more closely integrated, and second–hand goods are increasingly popular. More delivery options are available, and related services — such as tracking and rerouting — are becoming standard.

This growing diversity offers customers more opportunity and choice to find what they want. But it also makes it increasingly difficult for both shoppers and retailers to understand the environmental impact of online purchases — and, more specifically, of delivery.

Our previous study of e–commerce, published in 2021, highlighted that in Europe, the environmental impact of e–commerce is positive: Online shopping in Europe generates an average of between 1.5 and 2.9 times less greenhouse gas (GHG) emissions than offline shopping. The study also demonstrated that emissions from both types of shopping vary significantly by product type, country, and — more importantly — customers' locations and purchasing behavior.

The objective of this study is to go to a further level of granularity and focus on delivery emissions — to compare the emissions from various delivery models, to identify the main drivers, and to determine how delivery–related emissions of CO_2 equivalent (CO_2e) can be further reduced. Does home delivery generate higher emissions than pickup–point delivery (PUDO: pick up, drop off)? Does faster delivery result in higher emissions? How can the best technologies available today help reduce delivery emissions? What would it take to reach a 30% reduction in emissions per parcel by 2030 compared to the 2019 level?

Several major parcel operators have committed to at least matching the EU Green Deal target of being climate–neutral by 2050. Among them, the sustainability leaders are aiming to reach net zero by 2040, 10 years earlier. Most initiatives address the entire value chain, encompassing renewable energy sourcing and production, carbon–neutral buildings, carbon–neutral packaging, and zero–emissions transport — and complementing these measures with carbon offsetting.

To substantially reduce delivery–related emissions, resources and efforts will need to be focused on the levers with the greatest impact, and multiple complex solutions will have to be navigated. This calls for a comprehensive assessment of the emissions generated by today's delivery modes and an understanding of possible trajectories to decarbonize these modes.

This new study focuses on six countries, which together account for over 60% of European online sales: France, Germany, Italy, Spain, Sweden, and the United Kingdom. It is based on an analysis of official statistics, our proprietary CO_2e impact model, data made public by delivery operators and confirmed through interviews, and consumer surveys conducted in 2022.

CUSTOMER STANDPOINT: FASTER DELIVERY, MORE DELIVERY OPTIONS, MORE ATTENTION TO THE ENVIRONMENT

Beyond prices, consumers are often faced with three major questions when choosing a delivery option: Do they want a parcel delivered to their home — or to a nearby location where they can pick it up? How fast do they want to get their purchase? And what is the environmental impact of the available options?

Home delivery remains the preferred option for receiving an article purchased online inthe six countries studied. On average, more than 60% of e–shoppers say they favor it.

Fast delivery (in less than two days) is an important decision factor for 45% of e–shoppers and for up to 72% of frequent buyers. Next–day delivery is offered by 70% of the largest European e–stores.

87% of all e–shoppers are keen to change their habits if it can reduce their environmental impact. Their preferred actions are, in order: grouping orders (26%), favoring national shipment (16%), walking to a PUDO location (16%), and choosing an environmentally friendly merchant (16%). The least–popular action, preferred by just 13%, is a delayed delivery if it could reduce delivery emissions.

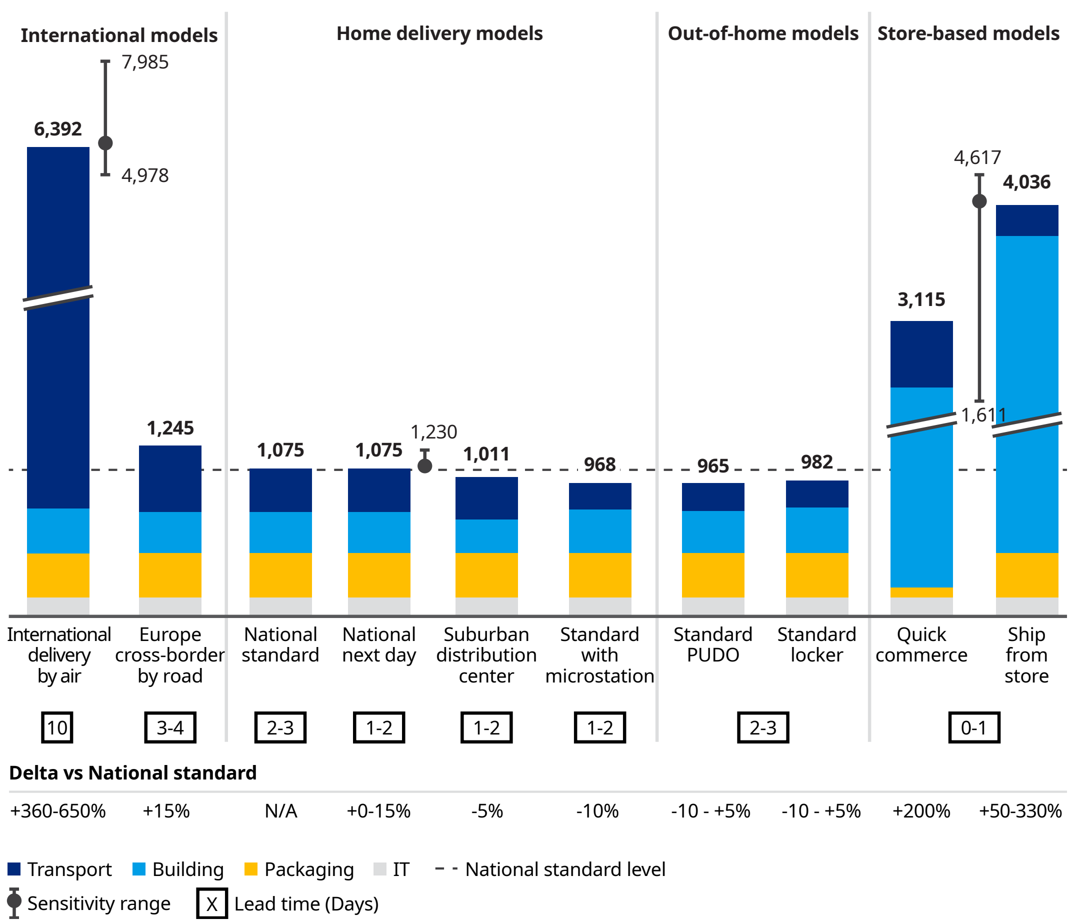
EMISSIONS FROM DELIVERY MODELS: SCALE AND COUNTRY ENERGY MIX MATTER MORE THAN SPEED

Our analysis shows that delivering at home a single, 1 kg parcel through a country’s most common postal system in two days or more generates an average of 1,075 gCO_2e, a measure of the global–warming effect of greenhouse gases in terms of the equivalent quantity of carbon dioxide. Different delivery models were compared to understand the key emissions drivers. The results show that the best way to minimize emissions per parcel is not to reduce delivery speed but to optimize last mile delivery and use the largest possible vehicles in the linehaul and maximize their loads.

The second most important factor influencing emissions is the size and location of buildings — hubs, delivery stations, and pickup points. Buildings’ impact can be even greater than that of transportation, especially in countries that depend heavily on fossil fuels to produce electric power, such as Germany and Italy (500 to 600 gCO_2e per parcel compared to the average of 300 gCO_2e per parcel).

Delivery speed by itself does not drive emissions. When ranking delivery options by lead time for the consumer (the gap between ordering and delivery), emissions form a U–curve: the fastest and slowest options have the highest emissions (see Exhibit 1). The slowest option (international delivery in 10 days or more) has the highest emissions (six times the level of national delivery). National deliveries in one to four days generate emissions ranging between 10% lower and 15% higher than national standard delivery. Same day options can generate emissions up to three or four times higher than national standard.

Exhibit 1: Base case — Emissions by delivery model (gCO_2e/parcel)



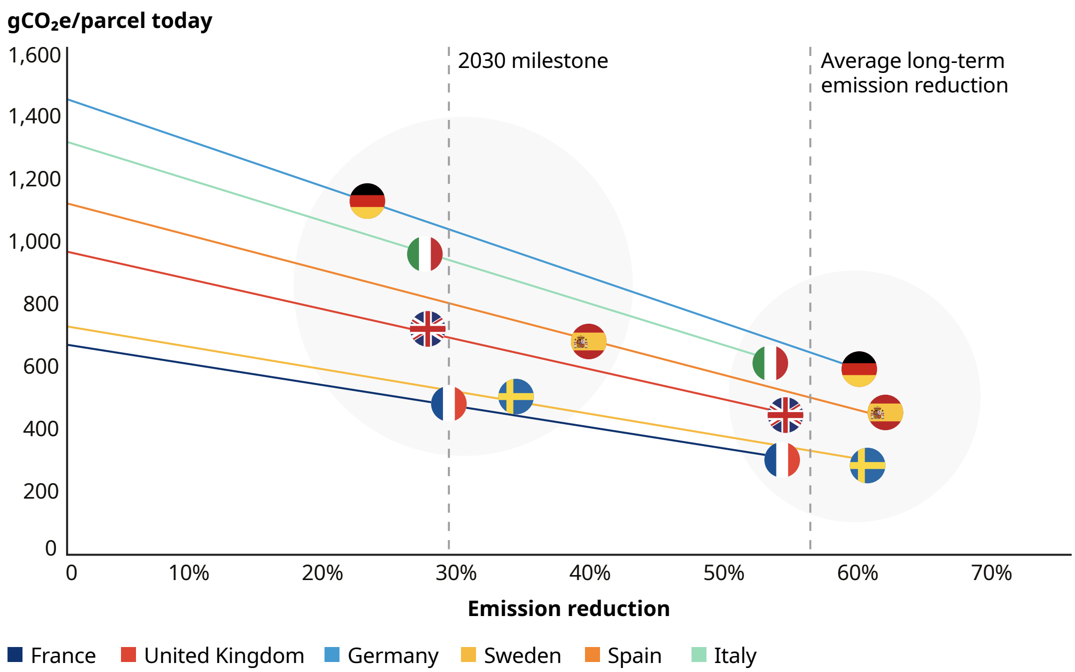
Source: Oliver Wyman 2023

DECARBONIZATION PATHWAY: 30% REDUCTION BY 2030, THEN 60% REDUCTION AT FULL POTENTIAL WITH KNOWN TECHNOLOGIES

Reaching a 30% reduction in greenhouse gas emissions by 2030 would require action on all sources of emissions, through the generalization of today's best practices, the deployment of emerging clean motorization technologies, and the improvement of countries' energy mixes. This 30% goal has been derived from the various targets set by the EU Commission for trucks, vans, packaging, national energy mixes, and other factors.

In the long term, pushing decarbonation drivers to the maximum level technically possible could lead to a reduction in overall emissions of between 55% and 60% to 448 gCO_2e. That would leave 40% to 45% remaining before full carbon neutrality is achieved, through new technologies or infrastructure that is even more energy efficient.

Exhibit 2: Parcel delivery decarbonization roadmap by country (gCO_2e/parcel)



Source: Oliver Wyman 2023

This report is the result of an independent study led by Oliver Wyman. It was conducted over a 12-week period and commissioned by Amazon. The methodology has been defined by Oliver Wyman independently of Amazon. The analysis, conclusions, and projections are those of Oliver Wyman only. The analysis is based on official statistics up to 2021 (unless stated otherwise) and publicly available information. The study does not use any private information from Amazon or other retailers or transport operators. Consumer behavior data is based on proprietary surveys conducted by Oliver Wyman in 2022 across Europe (France, Germany, United Kingdom, Sweden, Italy, Spain).

Read more

DELIVERY DECARBONIZATION PATHWAYS

SUSTAINABILITY

CONSUMER AND HOME ELECTRONICS — GOING FULL CIRCLE

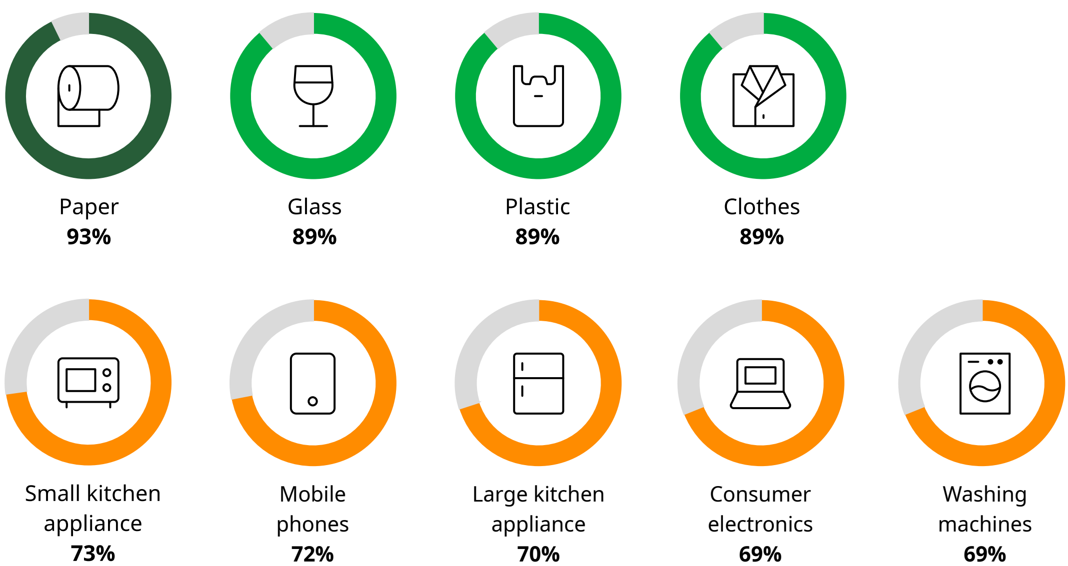
Joint study from GFU and Oliver Wyman

Dr. Martin Schulte

The concept of the circular economy, where materials and products are reused and recycled for as long as possible, is certainly a noble one. However, our latest research revealed that some countries still have work to do to achieve this ideal. Even in Germany, the supposed "world champion of recycling," a third of the country's old kitchen appliances, washing machines, and entertainment electronics — and an even higher share of smartphones — are not recycled. The material value of discarded devices amounts to €5 billion nationwide.

The primary reason for this waste of resources is a lack of awareness about recycling options. In our recent survey, conducted with the electronics industry trade group gfu Consumer & Home Electronics, which involved 1,000 consumers from Germany, the United Kingdom, and France, it was found that one–quarter of the respondents did not know ecologically sensible ways to recycle electrical devices. That was especially true for younger people. Only half of adults under 35 knew how to recycle a large kitchen appliance.

Exhibit 1: Overview of consumers recycling knowledge

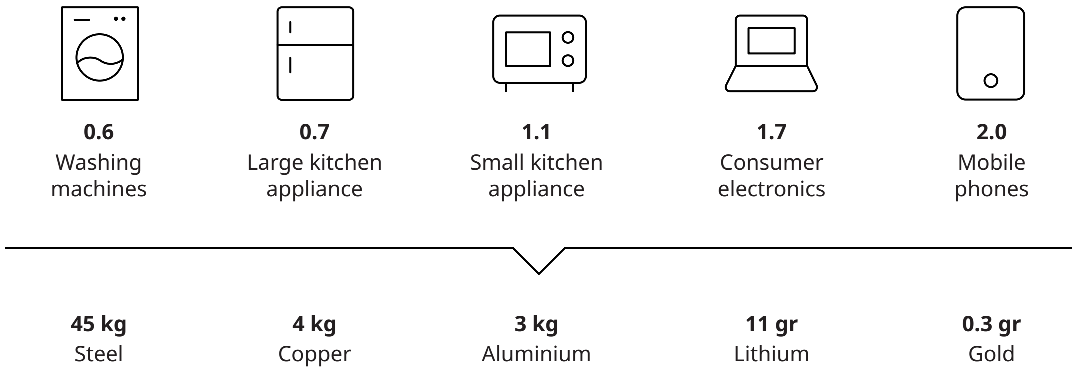


Source: Oliver Wyman Consumer Survey 2023

Germany is a country of bulky waste collection. But there is a lack of implementation when it comes to recycling electrical appliances. At the same time, younger people are taking a more holistic approach to the circular economy by buying refurbished devices or renting instead of buying them.

Dr. Sara Warneke, Managing Director, GFU

Exhibit 2: Number of unused or broken appliances in homes



Plus: Rare earth minerals, such as Neodymium, Cerium, Yttrium and more.

Source: Oliver Wyman Consumer Survey 2023

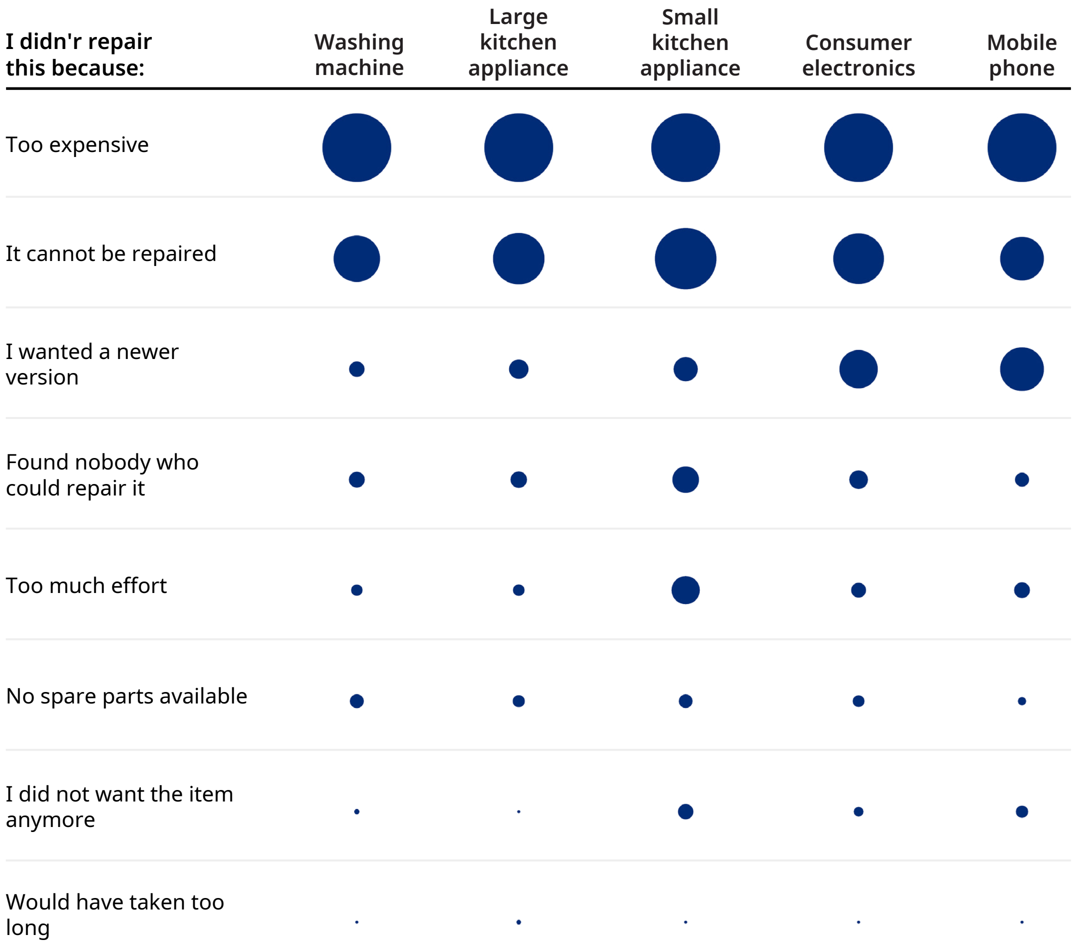
Many e–waste recycling options, including returns to electronics stores, supermarkets, and the original manufacturers, were largely unknown to survey respondents. The results stand in sharp contrast with other categories of materials. Roughly 90% of all respondents knew how to properly recycle paper, plastic, glass, and clothing. To remedy this, consumers need more convenient and free options such as designated recycling points, e–waste collection days, and incentive systems.

A more effective resource utilization in consumer electronics requires greater efforts from manufacturers, retailers, and policymakers alike. Going full circle is in everyone's interest. If the European Green Deal is to be taken seriously, manufacturers need to rethink their product designs.

Dr. Martin Schulte, Partner, Oliver Wyman

In addition to issues with recycling, the study found that consumers get just 22% of their electronic devices repaired. The causes for that low figure are mostly solvable through efforts by legislators and industry to improve product repairability and increase the availability of spare parts.

Exhibit 3: Main reasons for not repairing appliance

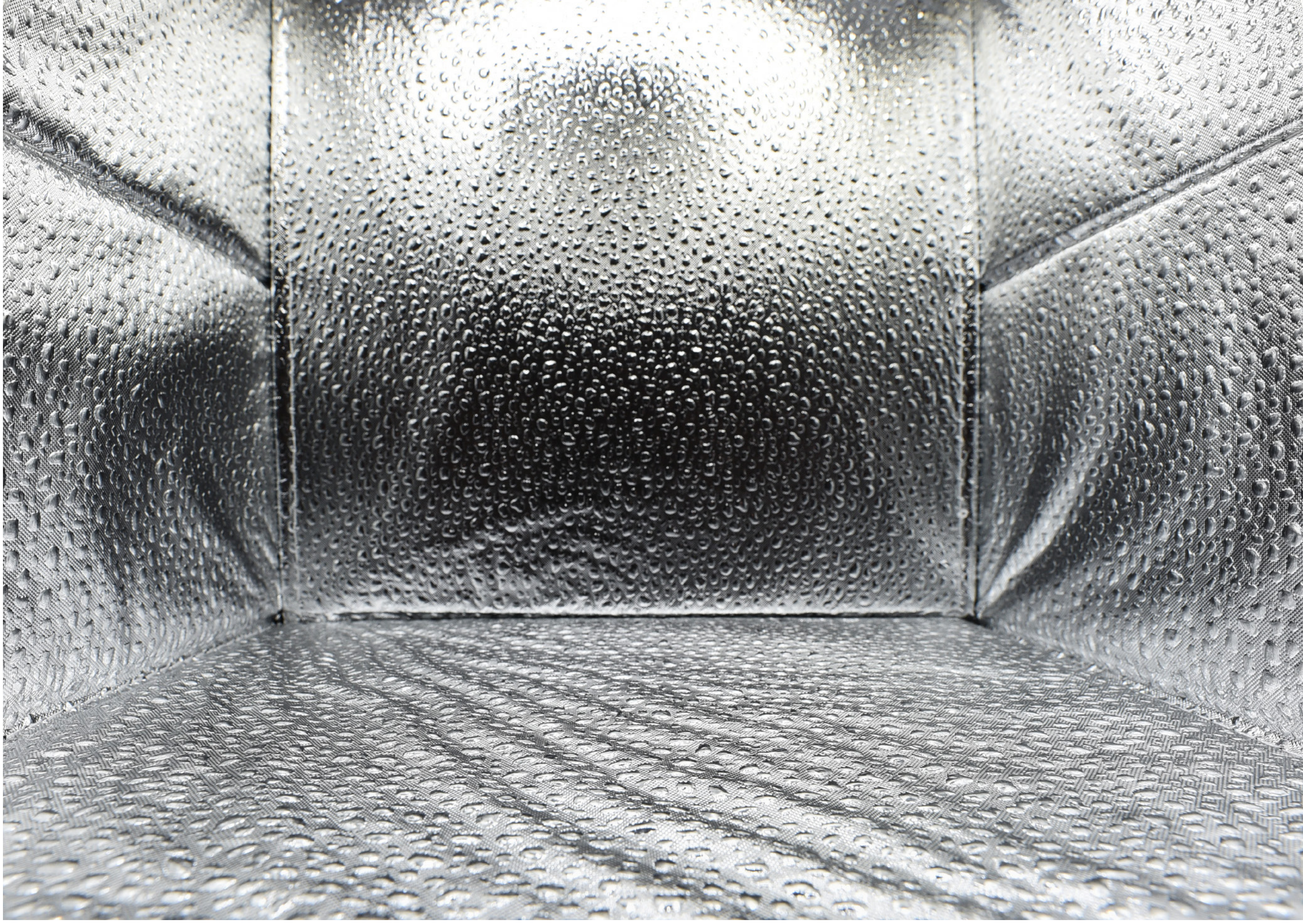


Source: Oliver Wyman Consumer Survey 2023

This is where the EU's Green Deal initiative comes in, with France leading the way as the pilot market for the "repairability index" introduced in 2021. Under this system, manufacturers calculate a score between 0 and 10 to each electronic device, indicating how difficult it is to repair and informing customers about their available repair options prior to purchase. It's been effective. In France, the repair rate stands at 32%, surpassing both Germany (22%) and the United Kingdom (24%). Additionally, there is growing pressure, especially among younger adults, for free returns and improved information about recycling options in general.

Read more

CONSUMER AND HOME ELECTRONICS – GOING FULL CIRCLE



SUSTAINABILITY

4 WAYS TO ALIGN CORPORATE INTERESTS TO SCALE CLIMATE ACTION

The next stage of action for corporate climate leaders

Simon Glynn

Originally published in ***World Economic Forum***

The step change in corporate climate action in the past few years has been extraordinary. Yet we are more than halfway through the critical period between the 2015 Paris Agreement and 2030, and emissions are still rising. Clearly, the world needs to scale up.

For our research report on Climate Action At Scale , launched at Climate Week NYC, we spoke to climate and sustainability practitioners from some of the world's largest corporations on their experiences in making this shift. They recognize that what needs to come next will be qualitatively different from what we have seen so far. In a survey of 200 climate practitioners, half see decarbonization as being a serious challenge — either an “existential threat” or “highly concerning” — by 2030, while a third already see it that way.

They are also clear about what is needed, what they can do and where they depend on others. Here are four lessons we learned:

1. **You can’t act at scale against your interests. Leaders at scaling up are creating the conditions for corporate and climate interests to align**

Doing something because it is the “right thing” is a recipe for incrementalism. Trying to act at scale on that basis creates justifiable resistance, because the pressure to perform commercially is too strong. This resistance fades when a company’s corporate interests and climate interests coincide.

The strongest examples are in B2B businesses that are finding profitable ways to act as decarbonization service providers for their corporate customers. Interests might align for Ball Corporation, for example, if investment in building a circular economy in aluminum displaces the use of competing, less recyclable materials in beverage packaging. Interests might align for Maersk if consumer brands concerned about their own carbon footprints pay a premium for shipping powered by biofuels rather than fossil fuels.

2. **You can’t achieve climate action at scale just by reducing. But you can by building**

Emission reductions are critical, but reducing to zero means doing something differently, not just emitting less. Scale leaders embrace the creative destruction that typically drives transformation and innovation. It’s about renewal: of the business, the industrial sector it operates in and the broader economy. At the core, it’s about new value propositions that companies have developed. These include offerings that grow the share, whether or not at a price premium, of low–carbon solutions at the expense of higher–carbon alternatives, and propositions that save money through operational efficiencies, usually in energy but also in people and materials.

Sodexo, for example, is reducing its Scope 3 emissions by rebalancing the food it serves in clients’ offices, schools and other institutions. It is introducing “low carbon meals”: not plant–based or vegetarian diets, but a shift in the balance of what is on the plate toward less meat and more vegetables. The initiative takes a big investment in the reskilling of its cooks, but it pays for itself in the competitive proposition for corporate clients, and in the shift from animal to vegetable protein, in addition to the decarbonization benefit.

3. Leaders in climate action at scale are adopting new business designs, using new mindsets to earn new rewards

As one practitioner put it: "What we can do a traditional business case for, we've done." To go beyond, leading organizations are open to new ways of thinking — about risk and uncertainty, about what makes a business case and about the capabilities that will matter in the future. We identified a wide range of arguments used to support investments at scale that would not convincingly generate a competitive financial return relative to the baseline of today's business.

Businesses that are moving ahead are instead using arguments based on:

- Competitive differentiation: Positioning to meet new demand from business customers.
- Protecting revenue: Investments to preserve the company's licence to operate as stakeholder expectations change.
- Enabling revenue: Investments without which some of the value–creating visions described earlier would not be viable.
- First mover advantage: Investments to learn, demonstrate and lead.
- Anticipating or influencing regulation: Take action to remain competitive in the face of future regulation or carbon pricing.
- Delegating investments: Impose decarbonization requirements on the supply chain.
- Avoiding stranded assets. Move forward to avoid being left behind.
- Filling the return gap. Structure or fund an investment that gets an innovative solution to a tipping point, making a non–commercial solution commercially viable.

4. Climate action at scale depends on investors, policy–makers and other players for solutions as well as profitability. Companies can't do it by themselves, but they can show the way

In the absence of much pull from the end consumer, which nobody is expecting, these corporate initiatives are built on two insecure foundations: continuing investor commitment and evolving public policy. "Creating the conditions", as we described in the first point, may mean bringing about whole ecosystems, regulatory environments and financing, not just new customer value propositions.

The appetite is strong for a clear policy environment that will make companies' plans for climate action at scale viable, both practically and commercially. Meanwhile, the leading companies we interviewed are not passively waiting. They are positioning themselves, making the moves they can, and working together with business partners, investors and policy–makers to shape a future in which they can scale up their climate transitions.

Read the original piece Here

LEADERSHIP

SECRETS OF EFFECTIVE LEADERSHIP IN TIMES OF CRISIS

How leaders can respond to unexpected events

Michael Lierow

The past few years have sprung plenty of surprises on business leaders – COVID-19, the subsequent supply chain crisis, and then, once everything looked like it had startled to settle down, the massive disruption from the war in Ukraine. The highest inflation for several decades, increased interest rates, and a new international banking crisis resulting from poor bond yields have been poured onto the mix, adding fuel to the fire. And for many businesses what is burning is margin.

These challenges have stretched business leaders. The world has moved from a time where an occasional crisis might be expected to one where continuous crisis management is rapidly becoming the norm. In this article, we explore the personal challenges leaders face during a crisis and the innovative approaches required to lead effectively in these situations.

UNEXPECTED DEMANDS ON LEADERSHIP

In troubled times, as the business environment moves from the familiar to uncharted territory, leaders are called upon to show ingenuity in their responses. Dealing with the complexity and uncertainty produced by a crisis, let alone a whole string of them, demands not only a willingness to show flexibility but also knowledge of how to demonstrate the leadership required. This is both contextual and personal.

Becoming more effective requires increasing the range of your responses. This in turn demands increased self-awareness about how you act when under severe pressure.

To respond appropriately to the unexpected often requires doing something new and untried. In a crisis, nothing is fixed. But without adequate personal preparation, our instincts and habitual actions are always capable of undermining even the best-laid plans. Rehearsal in responding to the unexpected can prepare us for the real event.

CHARACTERISTICS THAT ARE IMPORTANT FOR A LEADER IN A CRISIS

Here are a few suggestions on how to prepare yourself for a crisis drawn from an effective “leadership workout” carried out by a successful COO. The exercises carefully combine our right-brain capacity for sensing and feeling with more left-brain cognitive and analytical approaches.

Become familiar with the unfamiliar: Start by recognizing your comfort zones, as these tend also to be our default options in times of crisis. What is your preferred leadership style when hard pressed? What do you do, what do you say, and what do you not do? What alternative ways of leading might be more effective?

Get comfortable with the uncomfortable: The goal here is to turn our sense of stress and discomfort into our ally. In past crises, what feelings and thoughts distinguished the moments when you have felt, or have actually been, out of your depth? Label this vulnerability for what it is. Recognize how stress affects you physically and label these feelings as your personal "danger signal", the "red flag" that can alert you to impending crisis.

Tune into the stressful moment: The goal is for you to become aware of your danger signals as early on as possible. Once you have identified what happens to you in stressful moments during times of crisis, learn to recognize this feeling in everyday circumstances. What can you do to modify how you respond so as to ensure that the danger signals are of benefit to you and an ally during crisis?

Limber up the agility muscle: The goal is to become more flexible in your leadership responses in changing circumstances. From past experience, what are your own red flags telling you not to do? Practice alternatives. Try out a number of different leadership styles and become familiar with how this makes you feel and how it affects others.

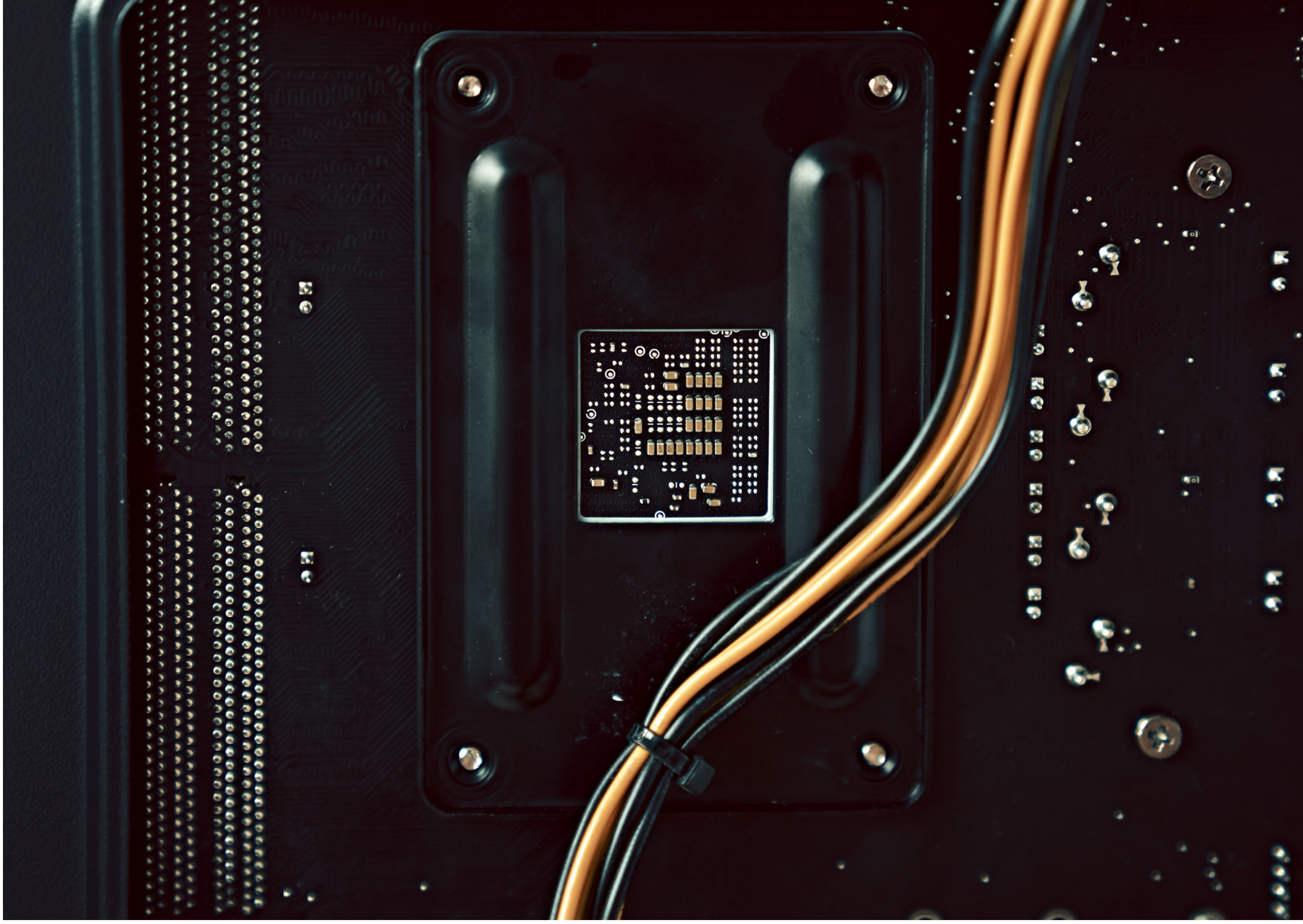
Act expansively when under pressure: Most of us, when under severe pressure. We narrow down our options and revert to well-tried solutions. We need to train ourselves to do the opposite, to open up the solution space during such times by involving others in tackling the challenges. Who is it that you will turn to for extra input during a crisis? Who has complementary skill-sets and can bring a different perspective? What novel approaches are you willing to embrace?

The "leadership workout" will help encourage the practice of right-brain approaches that are unfamiliar to many leaders. This practice is in direct contrast, however, to the impulsive behavior typified by following our "gut instinct". Our first responses are sometimes the wrong ones. The testing of our potential responses prior to enacting them, to establish whether they are appropriate, remains always the first duty of a responsible leader.

For more practical advice on how to effectively lead in times of a crisis, read our in-depth analysis.

Read more

SECRETS OF EFFECTIVE LEADERSHIP IN TIMES OF CRISIS



LEADERSHIP

UNDERSTANDING AI'S IMPACT ON JOB AND INDUSTRY TRANSFORMATION

How the next GPT will reshape our economy

Hunter Williams

In an intriguing twist of historical irony, the product that introduced generative AI to the world is aptly named ChatGPT. Within this context, GPT stands for "generative pre-trained transformer," a term for a class of large language models (LLMs). However, in the annals of science and technology, "GPT" has long held another meaning: "general purpose technology." These are innovations with applications so sweeping that they affect entire economies and civilizations. Examples of GPTs in this sense include the wheel, the printing press, the internal combustion engine, and the internet. The question now arises: will generative AI become another GPT, with similarly far-reaching implications and impacts? If so, how will it affect today's industries, and what can business leaders do to anticipate its impacts?

The impact of AI on various jobs and industries has been a topic of much discussion. Business leaders face hard decisions on how much to invest in deploying AI, where to focus the efforts, and how to manage the risks. For private equity investors and other financial sponsors, understanding how their portfolio is exposed to AI's risk and opportunities is crucial so the right investment decisions can be made and the right guidance given to portfolio companies.

To simplify this complex topic, we believe two dimensions are worth considering: first, the degree to which AI is likely to impact a particular industry, and second, the extent to which total demand in an industry is likely to expand given greater productivity (and therefore lower costs) due to the deployment of AI.

HOW AI WILL IMPACT AN INDUSTRY

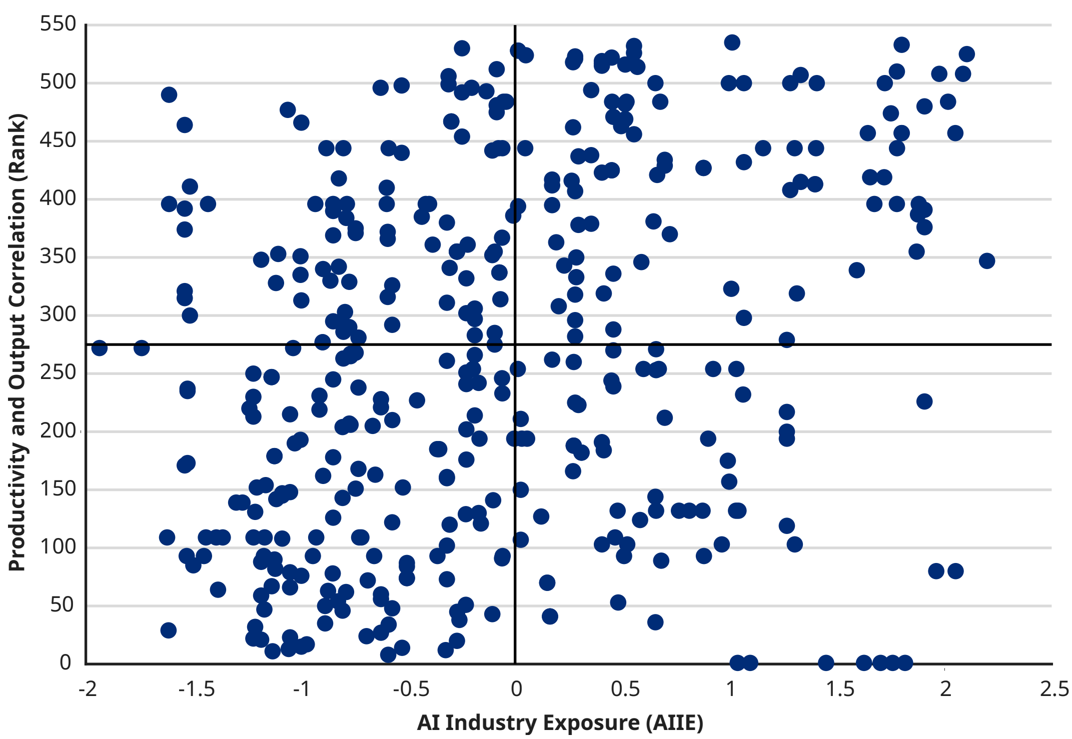
The first dimension has been a topic of extensive academic research, examining the nature of jobs in an industry and their substitutability with AI. While many recent technological innovations have displaced lower earners or more blue-collar jobs — think self-order kiosks at fast food restaurants — generative AI's impact is expected to be greatest on middle-skilled, white-collar jobs. The effects of AI will also be felt in management structures: fewer middle managers will be needed if (for example) 10 AI-turbocharged programmers can soon do the work of 50 today. Some jobs have more "exposure" to the potential impacts of AI than others, and this can be extrapolated to the industry level based on the job mix in a given industry. To quantify these differences, we have leveraged the AI Industry Exposure (AIIE) index, created by Edward Felten, Manav Raj, and Robert Seamans in their academic research first in 2021 and updated it to reflect the impact of LLMs specifically in 2023. Their work found that janitorial services, meat processing, and coal mining (to take three examples) should see less impact from AI while accounting, commercial banking, and legal services will see far more.

But we also need to consider the second-order impacts on industries of "AI shock." How long will enhanced productivity boost margins before being competed away? And what industries will grow most as a result of higher productivity and, therefore, lower costs? Mechanical weaving, for instance, did not just make clothes cheaper; it allowed demand for them to explode. Instead of owning just one set of work clothes and a "Sunday best," a typical worker could afford to have a different outfit each day, leading to today's closets full of clothes that may not even be remembered or worn.

AI-DRIVEN PRODUCTIVITY GAINS AND DEMAND EXPANSION

To estimate how "elastic" an industry is to growth from a positive productivity shock, Oliver Wyman examined the correlation between labor productivity and real output for each industry in the North American Industry Classification System (NAICS) hierarchy from 1987 through to 2019 (to avoid COVID noise). Ranked in descending order from highest to lowest correlation, a higher score on the y-axis can be interpreted as more potential for industry growth in total output due to higher productivity. By plotting industries according to both their expected AI impact and their historical relationship with labor productivity, (Exhibit 2), valuable insights can be gleaned into what might be expected in different industries over the coming decades.

Exhibit 1: Industry-level potential impact of AI on productivity and total output



Source: Occupational Heterogeneity in exposure to Generative AI" by Felten, Raj, Seamans, Bureau of Labor Statistics, Oliver Wyman analysis

Industries on the far left, ranging from dry cleaning to janitorial services, will experience limited direct AI impacts. For these businesses, other levers, such as scale effects and non–AI automation, will be more important for growth and profitability. Executives in these industries need not spend as much valuable time and effort considering the impact of AI, and investors can view them as having a lower "AI beta." Those in the upper left may want to focus more on labor productivity improvements (but not from AI) while those in the lower left are likely to find greater returns from other productivity levers.

However, for businesses in industries on the right side of the matrix, the impact of AI needs to be carefully considered. In the upper right, for an industry where productivity and growth are highly correlated, greater labor productivity will lead, over time, to lower prices and greater demand for those products or services. The size of the pie could grow quickly. Businesses here need to focus on how to rapidly adopt AI to drive productivity and enjoy first–mover advantages, gaining market share and winning more than their fair share of the future growth to come.

Conversely, in the bottom right quadrant, where productivity and growth are less linked, productivity improvements and lower costs may end up shrinking the overall pie as the same amount of work is done with fewer resources. The positive productivity shock can be seen as a deflationary headwind to growth in these saturated or inelastic markets. Many education and healthcare services appear in this quadrant, suggesting AI may help to "bend the cost curve" in these industries that have suffered, for so long, from the Baumol effect — wages rising in jobs that have seen little to no increase in labor productivity, in response to increased salaries in other professions that have experienced significant productivity growth.

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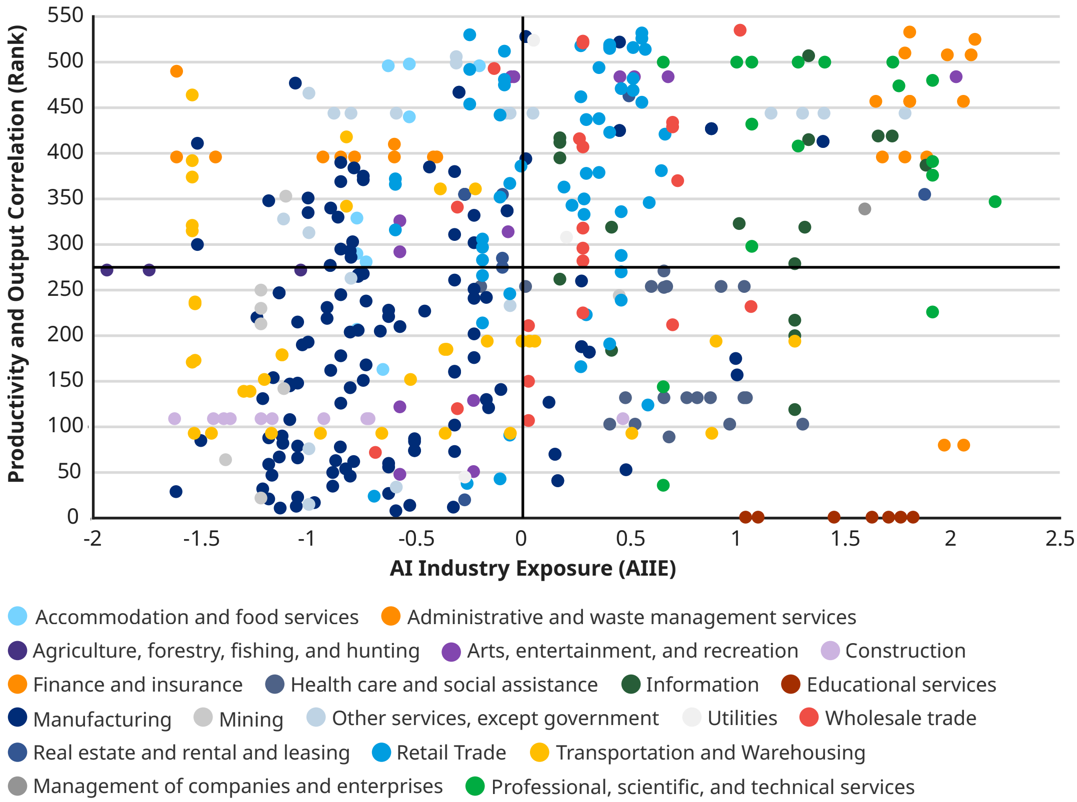
Exhibit 2: Industry–level impact by two digit NAICS classification



Source: Occupational Heterogeneity in exposure to Generative AI" by Felten, Raj, Seamans, Bureau of Labor Statistics, Oliver Wyman analysis

Understanding how your industry or the industries of your portfolio could be affected by AI is one thing; figuring out what to do about it is another. At Oliver Wyman, we are supporting our clients in developing AI strategies, integrating generative AI into their operations, managing the related risks, and helping them redesign work to achieve the optimal combinations of AI, automation, and talent. And we have an interest in getting it right, given our industry (falling into "management, scientific and technical consulting services") sits in the upper right. By staying ahead of the curve and anticipating the far–reaching implications of generative AI, businesses can position themselves for success in a rapidly changing world.

John Lester, ***Sian Townson***, *and* ***David Waller*** *also contributed to this article*

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NAVIGATING THE AI REVOLUTION

LEADERSHIP

TRANSFORM RETAIL EMPLOYEES INTO POWERFUL COMMUNITY BUILDERS

Laure Charpentier

Now more than ever, people are looking for their tribe. They have an increased focus on communicating with others in groups and communities that they are comfortable with, a trend that accelerated when so many were isolated during the pandemic.

This shift also extends to the business world. The more a brand and its salespeople resonate with a customer's culture and what they believe in, the more loyal the customer will be and the more they'll spend. Research from the Oliver Wyman Forum, for example, finds that more than 90% of Gen Z consumers are willing to pay extra for brands that support the causes they care about. Savvy retailers have begun taking advantage by enlisting their employees to build tailored communities around their stores through social media and other outlets. Striking the right tone can provide a significant sales boost, as well as vastly improve loyalty and reduce customer acquisition costs.

WINNING THE TALENT WARS THROUGH COMPANY VALUES

The foundation for improving customer retention in this way starts with a loyal, engaged workforce. Even more than customers, workers want to be aligned with the company's purpose. Employers must clearly communicate what the company stands for and demonstrate a commitment — to environmental causes, civil rights, or other important social and political issues — through real actions. There is 27 percentage point difference in employee retention between companies that provide purpose and meaning in their work and those that do not. Stronger sense of meaning and purpose also has a positive cascading effect on the customer experience.

This helps to build an emotional connection with employees and gives them a sense of belonging. It also fosters a greater feeling of achievement when they can see that their work really matters.

On the flip side, businesses that fail to adequately uphold their values and make meaningful connections put themselves at a considerable disadvantage in the war for talent. Salary raises and flexible schedules are not enough to placate workers as the quiet quitting trend gives way to what business author and former Unilever CEO Paul Polman calls "an era of conscious quitting." For example, more than half of US employees say they would consider resigning if their company's values did not line up with their own, Polman's February 2023 survey finds.

Fortunately, empowering workers to build store-based communities (and even encouraging them to become micro-influencers of a sort) goes a long way toward addressing these difficult labor issues. Not only is it an excellent way to increase their engagement, but it also serves to attract new employees who are energized by the company's purpose and values. Workers who are truly bought in to the message will pass it along to friends and social media followers, which can help attract new hires and lower recruiting spend.

THE BLUEPRINT FOR A COMMUNITY-BUILDING CAMPAIGN

Workers who can serve as the company's "value champions" also will perform their jobs better and be extra valuable as community builders. Finding the right people is usually the responsibility of store managers, who should find staffers that spend a lot of time on social media and are already well-versed in creating content on Instagram or TikTok. Taking on the role doesn't usually come with a direct incentive for salespeople, but it can be a way for them move up the ranks more quickly and get opportunities outside of their regular department.

A large cosmetics chain provides a good model for how to implement a community-building program. The company's stores empower one of their beauty advisors to run their Instagram accounts; that person is responsible for attracting an audience of like-minded clients to the store by making them aware of special offers and inviting them to events. Often the salesperson will bill the store as not just a retail space, but an enjoyable destination for members of the community to gather. A store might throw parties, host product launches, or in the case of the cosmetics company, bring in makeup artists to give clients free makeovers.

In some cases, multiple people from the same store could be assigned as representatives for different communities. For example, one salesperson reaches customers on TikTok who are young and identify as trendsetters, while another focuses on clients who use Instagram and are more interested in self-care products.

The store ambassadors must make themselves highly identifiable. There is no magic bullet for doing so, but perhaps the best way to start is by engaging with clients directly when they're at the store. To help, the store can post signage encouraging shoppers to follow the salesperson on social media.

HOW STORES MAKE COMMUNITY BUILDING SUCCESSFUL

The effort to bring customers together is especially effective in smaller cities that offer fewer opportunities to meet people. Of course, the concept is not to target just any customer; if the salesperson's reach is too broad, the community aspect will get diluted. Finding the right mix is easier for brands whose customer bases are relatively narrow and well-defined. The store can organize its communities in a variety of ways and may designate a different day for each one to be the focus of its events and social media attention. Ideally the parent company will leave the planning to the local stores, which have a better sense of their clientele and foot traffic.

Throughout the process, proper messaging is key. The store manager controls the communication strategy but should give the employee a lot of freedom within it. Again, people will respond only if the salesperson's message resonates well with their convictions and the type of products they're looking for. Among other guidelines, messages should keep the brand highly visible, use language that's properly tailored to the audience, and be mindful of diversity. Whatever the channel, the company's image must be maintained, so the store should designate someone as a community manager to review content regularly.

Several metrics are available to get a picture of how successful a community-building initiative has been. Every store manager needs to check Google comments and ratings. They can also monitor comments on Instagram, TikTok, and other social platforms, and calculate engagement rates of their employees' accounts. Promotions that were specifically advertised to a single community can also be tracked by traffic and revenue.

DEVELOPING CLOSER CUSTOMER RELATIONSHIPS

Many companies are further generating word-of-mouth business by empowering sales representatives to step up their one-to-one interaction with customers. Luxury businesses in Asia have been using this technique for the past few years. Salespeople contact their clients on WhatsApp whenever there's a new product coming into the store, eventually developing more personal relationships akin to real friendships. In China for example, 61% of Gen Z shoppers are in contact with their sales assistant at least twice a month through instant messaging, according to an Oliver Wyman study.

Retailers and brands in large cities in Europe and the US have begun following suit more recently. It seems clear that efforts to develop such connections will only become more personalized and granular in the future. Building this level of client loyalty, the strategy will still depend on the company's ability to first establish a solid bond with its employees mainly from its purpose, value, and ways of taking care of them. From that foundation will come the intended savings in talent or client acquisition costs and bigger numbers at the cash register.

Oliver Wyman is a global leader in management consulting. With offices in more than 70 cities across 30 countries, Oliver Wyman combines deep industry knowledge with specialised expertise in strategy, operations, risk management, and organisation transformation. The firm has 7,000 professionals around the world who work with clients to optimize their business, improve their operations and risk profile, and accelerate their organisational performance to seize the most attractive opportunities.

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