Shifting Expectations, Borrowed Equity and Retail's Real Estate Problem

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IT'S NO SECRET THAT THE U.S. IS "OVER-STORED,"

with two times more square footage of retail space per capita than anywhere else in the world[1]. Retailers with prime real-estate positions are facing hard questions in an era where store and mall closings are an everyday occurrence.

Brands with otherwise successful product lines are also in danger because of commitments they have made for their physical stores. Recently, Jamie Salter, CEO of Authentic Brands Group, who runs stores like Aéropostale, Juicy Couture and Nine West, recently said "they have a rent problem" when talking about distressed brands. He recalled a story where he was speaking with one of his major mall partners, General Growth Partners (GGP), and they asked him to "please stop closing stores." He asked them to attract more buyers and/or lower the rent, but they said they couldn't. His response was "...then I can't stop closing stores." Given the headlines of the past few years and prognostications around the "death of the mall," this exchange isn't too surprising even when talking about strong, legacy brands.[2]

Additional pressure has fallen onto anchor stores with the highest square footage, which have traditionally drawn traffic that helped a mall's other stores. The death of traditional anchors like Sears reveals that sometimes this pressure can be too much, and that the stores that remain when an anchor leaves, along with the malls themselves will have to change or end up closing as well. For brands and retailers, there is a real question of where, what size and how when it comes to bringing their offering to market in such a volatile environment.

Complicating the conversation further, and maybe not as well reported, is that some malls are doing very, very well proving they have a future. Many of these strong performing malls continue to see year-over-year growth, along with their tenants. There has also been success from data-fueled direct-to-consumer brands who are selectively opening stores to great traffic over the past year. And, while shopping traffic numbers have stayed somewhat stagnant at those malls and stores, those shoppers are actually spending more per person and per visit than in the past. The shoppers who are there are ready to buy.

So, the problem facing retailers today is multifaceted and one solution isn't going to help everyone. But some of these stores are starting to aggressively change, adapt and innovate in hope of repurposing and reinvigorating their real estate, changing it from a liability to an asset.

It is also helpful that sales-per-square foot, which used to be the primary metric of success, has been tempered by a number of creative attribution models which take into account the new ways that shoppers are discovering, buying and fulfilling orders from stores. Paula Price, Macy's new CFO, pointed to this new type of success measurement and the reality that not every tactic has a direct way to measure ROI. Much of their recent success has come from an attitude that says, "if it just makes sense for the customer, we are going to do it." Macy's is also measuring success by customer instead of store, as they have realized their best shoppers "shop at least 2 different stores and online."[5]

As retailers and brands rethink their market strategies, a new type of partner is needed whom deeply understands the evolving consumer and how to meet their changing expectations. WONGDOODY and Infosys are focusing on bringing this type of solution to the market, creating human-centric experiences powered by technology. Our combined point of view and capabilities are focused on four major trends driving retail into the future:

- Borrowed Equity
- Repurposing of Stores
- Innovative + Flexible Spaces
- Omnichannel Experiences

BORROWED EQUITY

Retailers are focusing on shopper insights to help guide them in thinking of new ways to utilize their real estate. For instance, 69% of shoppers expect to see new merchandise when visiting a store, and will come back more often if they feel it will happen.[7] At the same time, DTC brands are realizing that e-commerce penetration by category is limiting to the type of growth they desire. While they build up deep reservoirs of data and huge followings online, they are looking for retail outlets of their own. This convergence sets up the notion of borrowed equity very nicely.

Target is really pushing the notion of borrowed equity and has even gone as far as investing $70 million in Casper to back up its belief. In addition, a spokesperson said that the company is "aggressively" seeking out new digital brands to bring into stores in every category. Aside from Casper, the company now sells formerly online-only brands including Harry's, BarkBox, Quip and Native.[6]

Macy's has taken an even more aggressive push, investing in b8ta and giving prime real estate in some of its stores to the innovative retailer that helps bring small, startup and digital-only brands to physical retail. The large retailer has also recently made Rachel Shechtman its Chief Experience Officer after the purchase and assimilation of her popular Story store concept. These Story installations read like a magazine where all of the merchandising of products is centered around a specific theme. The richly experiential spaces are helping redefine the image of Macy's, according to its Chief Digital Officer, Naveen Krishna.

Borrowed equity also helped Ulta grow 14.1% last year on the backs of digitally native brands like Kylie and Morphe with their huge social followings.[8] Showfields in NYC is a store completely dedicated to leveraging the audiences of its 4 floors of digitally native vertical brands, while Neiman Marcus allocated an entire floor in its new Hudson Yards flagship as flexible space for the very same thing. Even drug and specialty retailers are getting in on the act, with the likes of Birchbox and Walgreens or, Banana Republic and Cos Bar.

Borrowed equity is a solution to multiple problems, as it delivers on new customer expectations while allowing retailers to utilize their existing assets in new and different ways. This trend will redefine existing retailers for years to come and is part of a larger repurposing aimed at addressing the real estate problem head-on.

> ***We have helped clients like Ulta revamp consumer interaction experiences online to better match with and connect online and offline experiences. Moving their e-commerce to a new platform and the experience overhaul helped Ulta.com grow by 53% and increased downloads of the mobile app to more than 750,000.***

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REPURPOSING OF STORES

As changing consumer expectations have driven people toward Amazon, with 73% saying it is where they go when they are ready to buy, stores of all types have had to repurpose their real estate.[9] This repurposing of stores has made huge, successful strides over the past few years and even helped to create a competitive advantage for those doing it right.

The notion of changing your store into a fulfillment center is one of the most dramatic shifts powering this trend. Best Buy started fulfilling online orders from local stores in an effort to turn their business around in the age of Amazon. Target is the most recent beneficiary of this strategy, as they recently reported that 75% of their online sales are now fulfilled by local stores. Utilizing traditional retail properties in this way also plays right into BOPIS and curbside, which are rapidly gaining popularity with shoppers.

Dick's Sporting Goods has also shifted the use of its real estate to boost business. As their online sales have grown to nearly 23%, they are still looking to open new stores and malls are pretty happy about it. Their status, primarily as anchor tenants, means they (usually) have entrances to the outside that allow for things like BOPIS and curbside delivery, plus large storage space to house inventory for both the store and online orders.[10]

With the growing influence and percentage of online orders and BOPIS, returns are also on the rise. Aside from fueling a rapidly growing marketplace of third-party vendors willing to help with returns, it has made retailers rethink their spaces in response. Amazon is also no stranger to returns and made a really smart move in partnering with Kohl's and its retail footprint as drop-off locations. It's a smart move by Kohl's as well, generating a new traffic source to its real estate. Amazon-owned retail locations, specifically Whole Foods, will start to roll out return servicing as well. Finally, Nordstrom's Men's Store in NYC is testing kiosks in the store for self-service returns.

Retailers are getting smart with their real estate and repurposing it to create a competitive advantage out of a liability. However, not all retailers are going to be able to survive this way. With high rents and long commitments, malls need to start acting creatively to change the conversation.

INNOVATIVE + FLEXIBLE SPACES

When it comes to retailers like Authentic Brands Group, their stores need and want malls to do better, but they are in more of a unique situation as an "interior" store. Their ability to flex their space and create the types of experiences that consumers now expect will require a number of shifts in format, structure and digital integration.

An interesting company called Convene has just purchased an anchor store in NYC's high-profile Brookfield Place and will have 73,000 square feet, with plans to convert it into a venue for conferences, corporate meetings and cultural gatherings. That means about a quarter of the 300,000-square-foot mall will pivot away from retail when the new event venue debuts in November of 2019.3

This notion of creating more diversity of usage in malls, to complement retail, is at the heart of new strategies by companies like WeWork, which has developed its Made by We concept in NYC. This complementary approach combines coworking space with innovative retail spaces and concepts that aren't tied to traditional rent structures and sales-per-square-foot metric. Billed as a "town square" for mission-driven projects and small businesses, Made by We will be another consideration for brands and retailers to consider in the expanding universe of innovative and flexible tenant spaces.[4]

The continuing trend is toward pop-ups, made legitimate by retailers like Nordstrom and J.Crew, which lend themselves to flexible, short-term leases. Malls are now looking at dedicating space to pop-ups and adjusting normal structures to accommodate them. Pop-ups are great for retailers and brands to test concepts, merchandising and even product development, which can only help retail as a whole. Amazon recently closed 87 of its pop-up stores, but only after gaining a tremendous amount of data which helped it to focus on its next generation of physical retail, including the 4-star and Bookstore concepts.[11]

Finally, malls and retailers alike are helping to drive participation, traffic and engagement for their retail partners through innovative digital, omnichannel experiences.

Taking experiences powered by revamped technology and using them to connect and fulfill human expectations is how retail and brands will succeed in the future.

OMNICHANNEL EXPERIENCES

The notion that shoppers lose trust in retailers when they have different experiences in different channels and are more likely to return to those providing them has been a reality since e-commerce entered the scene. However, new shopper expectations transcend this continuity alone and desire an actual connection of the multiple channels where they discover, try and transact. The technological hurdle at the heart of connecting experiences is inventory transparency. This real-time exposure of inventory across channels allows for BOPIS and the utilization of stores for e-commerce fulfillment mentioned earlier. It also powers numerous "endless aisle" executions in stores.

Connecting accounts and prior purchases is also of great use to consumers and retail operators alike but presents numerous technology hurdles. This is true especially when empowering human retail associates with information to better help them provide needed context in the moment and to fuel personalization outside of a retailer's website or app.

Walgreens is a great example of what can happen when all of these systems come together. Because they offer prescriptions, there is even more need for integration and two-way communications. Utilizing Walgreens' online and mobile tool set, shoppers can see inventory, create BOPIS requests, and order and fulfill prescriptions while being directed to the nearest store. In the store, associates are now connected with devices to better help them navigate more than 100,000 SKUs with shoppers and allow them to see past-purchase history and current order status.

Another retailer setting the gold standard for omnichannel is Starbucks, who was able to eclipse 11% of purchases via mobile-order-pay, and increase participation in its loyalty program, gathering data to better service consumers across the ecosystem. To cap it all off, almost 1-in-3 transactions happens via mobile payment, setting the standard for retail of all types.[12]

> ***Adidas, an Infosys and WONGDOODY client, is a leader in creating omnichannel experiences powered by technology. By building a Salesforce Commerce Cloud (formerly DemandWare) deployment, we were able to create more inventory transparency connecting online and offline globally, driving 200% YoY growth on key shopping days while setting the stage to increase loyalty via in-store and online experiences.***
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> ***We have created similar functionality for retailers like Hudson's Bay, driving more than 20% increase in store orders, and consumer brands like Beats by Dre and Starbucks, powering their omnichannel feedback survey.***

THERE IS NO ONE-SIZE-FITS-ALL SOLUTION TO MEET CHANGING CUSTOMER DEMAND.

LET'S GET STARTED TOGETHER

In today's retail environment, a couple of things are becoming clear. First, there is no one-size-fits-all solution to meet changing customer demand. Second, and maybe more importantly, technology "transformation" is important, but only part of the equation. Taking experiences powered by revamped technology and using them to connect and fulfill human expectations is how retail and brands will succeed in the future.

WONGDOODY and Infosys create partnerships which deliver across the spectrum of experience powered by technology, and help create data-driven, authentic brand experiences unique to the needs of our customers. We would love to talk more to get started on the next evolution of retail.

ABOUT STEVE

Steve White helps our clients navigate the rapidly-changing retail environment as the leader of WONGDOODY's Retail Innovation practice and is an active voice in the evolving retail conversation as a committee member for the National Retail Federation, frequent speaker and contributor.

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