Retail Management

Block

2

RETAIL STRATEGY

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Our E-mail id: cwfeedback@icfaiuniversity.in

Centre for Distance and Online Education (CDOE)
The ICFAI Foundation for Higher Education
(Deemed-to-be-University Under Section 3 of UGC Act, 1956)
Donthanapally, Shankarapalli Road, Hyderabad- 501203

BLOCK 2: RETAIL STRATEGY

This block, *Retail Strategy*, emphasizes the different strategies that should be adopted by a retailer in the competitive market environment. This block consists of 4 units.

Unit 4 - *Retail Market Strategy:* This unit pays attention to aspects like price, location, merchandise purchasing, operations, logistics, market research, service and communications that should be taken care by the retailers. The necessity for systematic planning with the limited financial and human capital available at the end of every planning process is discussed. The need for re-planning periodically to help a retailer in strategic positioning is also emphasized in this unit. In addition, key strategies and implications for modern Indian retailing are explained.

Unit 5 - *Financial Strategy:* This unit covers the elements of financial strategy faced by a retailer through a discussion on financial documents, namely, the income statement and the balance sheet. How a retailer should set his/her financial objectives is re-looked at and an analysis of Strategic Profit Model is also examined in the process.

Unit 6 - *Store Location and Site Evaluation*: Every retailer would opt for locational advantage of his store. There are various factors that should be considered for identifying the store location. The four-step process of analyzing alternative trade areas, determining the most beneficial type of location, selecting a general site, and selecting a specific site by a retailer are explained in this unit. Omnichannel retailing – objectives, benefits and relevant implementing strategies for retailers are also emphasized in this unit.

Unit 7 - *Retail Organization and Management:* The steps involved in designing and structuring a retail organization, the various levels of management and their respective roles and responsibilities, the different types of stores in the retail industry, and the various forms of ownership like sole proprietorship, partnership and corporation are the topics that shape this unit.

Unit 4

Retail Market Strategy

Structure

“Marketing strategy will impact every piece of your business and it should be tied to every piece of your business.”

- Brandon Andersen, Chief Strategist at Ceralytics and Chief Digital Officer

4.1 Introduction

Whether you’re just setting up shop or been running your store for decades, acquiring new customers and keeping the ones you already have are paramount. The good news is that there are more than enough ways to market your business.

In this era of globalization and increasing competition, retailers are showing a keen interest in formulating well-designed strategic plans that could attract and retain customers by understanding and catering to their needs and changing interests. An effective strategy enables the retailer not only to stay in the market, but also to grow and prosper.

The strategic plan of a firm should be formulated by assessing the external environment affecting the working of the firm and capitalizing on the opportunities available after assessing its own strengths and weaknesses.

However, no strategy can be effective, if it is not implemented properly. Therefore, retailers should take steps to implement the strategy effectively and monitor it from time to time. This unit focuses on developing effective strategies for firms in order to establish themselves in the market and gain competitive advantage.

4.2 Objectives

After reading through this unit, you should be able to:

- Define a retail market strategy that gives an understanding of a retail format
- Restate the evolution of various theories and learn to anticipate the changes in the retail environment
- Determine the target market to ensure the choice of the right retail format while functioning in the industry
- Differentiate the various retail formats that assist a retailer in building a sustainable competitive advantage
- Evaluate the factors contributing to sustainable competitive advantage to achieve strategic positioning
- Discuss the nature of strategic planning to acclimatize to future challenges
- Evaluate the stages of retail planning process that assures the vision and mission of the organization

4.3 Definition of Retail Market Strategy

It is important for a student of marketing or someone pursuing his career in the marketing field to first know what retail market strategy is. It helps him identifying business opportunities and focus his attention on the target market. A retail market strategy is a statement, which defines the orientation of the firm in terms of the target market that it wishes to cater to, the retail format that it proposes to build, and the retail mix variables that it chooses to gain decisive competitive advantage and sustain its position in the retail market. The retail format takes into consideration factors like the nature of the merchandise, assortments, the services offered, the objectives of the promotional campaigns, pricing, store design and visual merchandising, location and number of stores, etc. To formulate a good market strategy, the retailer should first understand its target market and its retail format.

Example: Westside's Commitment to Serve a Compelling Range of Fresh Fashion

Westside, one of the best retail brands in India, is owned by Trent and is a part of the Tata Group. Westside has set a benchmark in its offerings to customers.

Contd….

Westside opened its 200th store in April, 2022 in Mumbai. The new store has a well laid-out store with latest collection. It also offers marquee brands like Zudio, Star Bazaar and so on. Westside has positioned itself as a compelling range of fresh fashion brand steadily.

Source: (April 4, 2022). Westside's Commitment to Serve A Compelling Range Of Fresh Fashion. Retrieved from https://www.livemint.com/brand-stories/trent-ltd-chairman-mr-noel-tata-unveils-westside-s-200th-store-in-borivali-11649076794937.html. Accessed on 01-07-2022.

4.4 Prominent Retail Management Theories

Retail market formats have evolved and matured over a period of time. To understand this cycle of retail format, the student of retail management should necessarily know the genesis of the various theories that evolved due to the changing retail environment.

Pradhan (2010) classified the various theories associated with retailing into three categories:

1. **Environmental:** deals with the retailer strategy with respect to changes in the retailing environment.
2. **Cyclical:** deals with the retail theory that caters to periodic changes that follow a specific pattern of phases.
3. **Conflictual:** deals with the retail strategy with respect to the level of competition at the marketplace.

4.4.1 Environmental Theory

Based on the Darwinian principle of "*Survival of the fittest",* this theory posits that every retailer needs to monitor continually the changes that are taking place in the retailing environment. The above changes can take various forms viz. political, economic, social, technological, environmental, and legal. According to this theory, the profitability of a retailer depends significantly on his ability to adapt successfully to the changing environment. Retailers, who quickly and positively adapt to the changing environment, gain from the changes attaining competitive advantages over others.

Example: Apple Portraying "Survival of the Fittest"

Apple Inc. (AAPL) found on 1st April, 1976, offers innovative range of products. Apple in 2022, is a leader in innovation and manages to set trends with each product it launches on the market, and this has been proven time and time again, revolutionising the technological world. Apple occupies third place after Walmart and Amazon on the Fortune 500 List for 2021, in terms of revenue. Apple offers path breaking products in the range of desktop, laptop, tablet, and smartphones. Despite having a growing number of competitors Apple continues to be a dominant player in the sector.

Source: (January 7, 2022). Who Are Apple's Main Competitors in Tech? Retrieved from https://www.investopedia.com/ask/answers/120314/who-are-apples-aapl-main-competitors.asp. Accessed on 01-07-2022.

4.4.2 Cyclical Theory (The Wheel of Retailing and Accordion effect)

The cyclical theory consists of the Wheel of retailing and Accordion effect. “Wheel of Retailing” is one of the most prominent retail management theories. The theory suggests that new retailers (innovator) often act as low priced operators following a low cost-low profit margin structure, offer unique customer-specific merchandise, which helps them to attract customers from the established players in the market. Building on their initial success, these retailers tend to expand their business by offering greater variety & assortment of merchandise, opening retail stores at expansive locations, and improving their level of customer service quality. However, doing so leads to an escalation in their overall cost structure and they trade upon the focus based on which they established themselves in the market. The above loss of focus creates a vacuum for new retailers to enter the marketplace who repeat the process followed by the focal retailer. The focal retailer then in turn becomes vulnerable to losing its customers to the emergent discounted players following low cost structure. The Wheel of Retailing has been criticized on its generalizability.

“The Accordion Effect” explains the evolution of stores from specialty retailing, then widening the variety & assortment of merchandise offering by adding new classes of products. The accordion effect classifies retailers into two categories viz. (i) retailers with “closed accordion” (narrow assortment of merchandise), or (ii) “open accordion” (wide and deep assortment of merchandise). Both the Wheel of Retailing and The Accordion Effect together are termed as Retail Cyclical theory.

4.4.3 Conflict Theory

This theory deals with the level of competition that exists in the marketplace between retailers operating through similar formats or belonging to same broader retail category. The underlying premise of this theory is that nothing in this world is fixed or sacred and always lends way to others when faced with a decline. According to this theory, retailing evolves through a dialectic process whereby two opposite retail formats combine together to create a new format. According to this theory, a retailer passes through a series of phases when faced with competition. In the first phase, the retailer experiences a shock when faced with the challenge. In the second phase, it may retreat and subsequently attempts to sabotage the success of its competition. When unsuccessful, the above retailer admits defeat and looks for new avenues to offer better products and services.

4.4.4 Retail Life Cycle

Similar to the “Product Life Cycle”, every retail organization passes through four stages of innovation, growth, maturity and decline. The evolution of a retail organization through the four stages is termed as "*Retail Life Cycle*". The four stages are:

a. ***The Innovation Stage***: The retail organization focuses on experimentation in order to build competitive advantage through convenience and other means against established players. It faces limited competition. It experiences moderate profitability and this stage may last up to five years from its inception.

b. ***The Growth Stage***: The retailer enjoys a rapid rise in sales and profitability. However, a few competitors emerge at the marketplace trying to replicate its success. In such a scenario, having gained some experience, the retailer tries to pre-empt the market by establishing its leadership. The duration of this stage ranges from five to eight years. However, the retailer starts to feel pressure on its existing cost structure towards the end of this stage.

c. ***The Maturity Stage***: The retailer experiences intense competition at the marketplace, especially from the innovative new entrants. This leads to a decline in the growth of its sales and profitability. It forces the retailer to rethink his market strategy and reposition himself to include the change of retail format and merchandise mix.

d. ***The Decline Stage***: The retailer loses his competitive edge at the marketplace. The management of the organization decides the extent to which it is worthwhile to continue doing business. This stage is characterized by negative sales and high overhead expenditures.

4.5 Target Market and Retail Format

A retail strategy cannot be formulated in isolation or by considering the aspirations and resources of the organization alone, which form the internal environment. The external environment such as customers and competitors should also be considered as they impact its formulation. Retailers should not only satisfy the needs of the target market, but also perform better than the competition. The retail format should be so chosen that the retailer is in a position to provide the retail mix that its target customers look for.

Traditionally a 'market' was considered as a place where buyers and sellers met to bargain and exchange products and services. However, in the modern marketplace, the sellers and buyers do not need to meet one another. Customer can directly place orders with the retailer through the retailer's web site using the Internet and make payments online.

Hence, a 'retail market', in present times, refers to a group of customers who have common or similar needs, which can be collectively addressed by a retailer who chose to cater to the same group or customer segment.

Thus, the retail format chosen is based on the target group (any customer segment based on the demographics, lifestyle, buying situation, benefits, etc.) that the retailer wishes to cater. Departmental stores, specialty stores, discount stores and hypermarkets are some of the retail formats. Within each product segment like apparel, groceries, toys, etc., a retailer can choose a different target market. For instance, the same retailer can target high-income customers for its apparel section while it may target middle-income customers for its grocery section. Thus, each retailer can choose a different retail mix.

Example: Shoppers Stop - the Large Store with a Huge Set of Brands

Shoppers Stop is a top apparel, fashion and beauty retail company established in 1991 by the K. Raheja Group at Mumbai, India. In 2022, the company announced the launch of four new department stores in Jaipur, Jodhpur, Lucknow and Mumbai. The store in Mumbai was launched at the Chhatrapati Shivaji Maharaj International Airport. Further, one more outlet of SSBeauty, which is a luxury beauty store, was launched in Mumbai.

Shoppers Stop has positioned itself as a bridge to luxury brand with impeccable customer shopping experience with offline and online shopping experience. At the same time the company has invested ₹ 40 crore in digital technology to enhance customer experience. With omni-channel strategy, the retailer is offering social shopping with seamless experience from discovery to check-out. All of the stores of Shoppers Stop are linked to Shoppersstop.com. This has created a unique advantage for Shopper Stop with a huge set of brands.

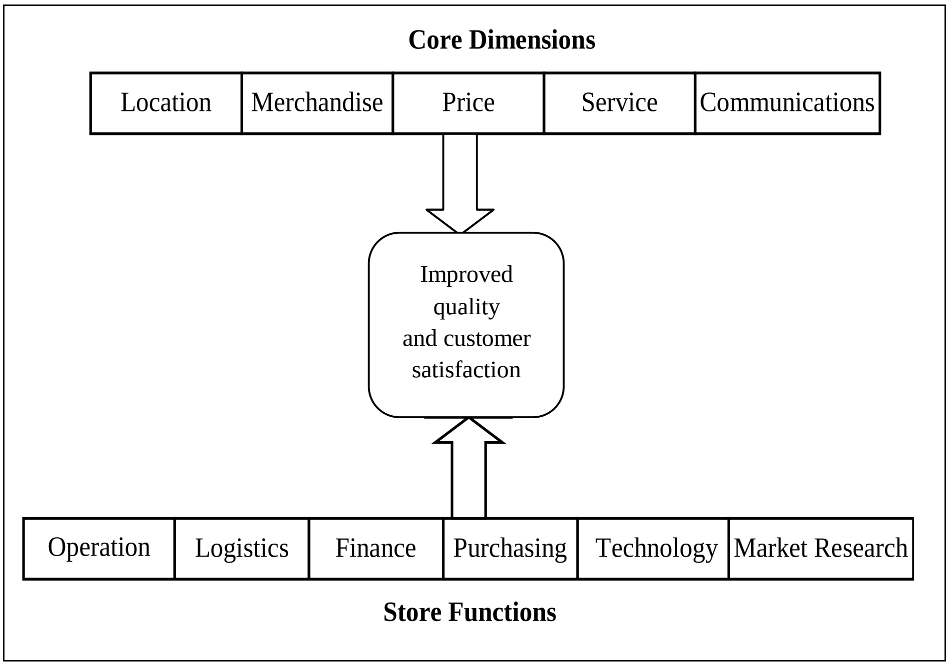
Source: (February 21, 2022). Shoppers Stop Opens Five New Stores. Retrieved from https://www.livemint.com/companies/news/shoppers-stop-opens-five-new-stores-11645442098993.html. Accessed on 04-07-2022

4.6 Building Sustainable Competitive Advantage

After establishing the retail format and defining the target market, the retailer should formulate a retail strategy that would help it differentiate its store from its competitors. The retail strategy is chiefly guided by the five dimensions: price, location, merchandise, service and communications. Customers form an opinion of the store based on these core dimensions. The core dimensions are supported by everyday store functions, i.e. operations, purchasing/logistics, market research, financing and technology. The pictorial representation of all the influencing dimensions and functions can be seen in Figure 4.1.

The effect of each of the dimensions can be understood by a careful examination and analysis of the retailer's position with regard to that of its competitors. Thus, the dimensions that influence the business most and win over the competition should be given utmost importance.

Figure 4.1: Positioning the Retail Store



Source: ICFAI Research Center.

4.6.1 Location

Many customers and retailers have realized the benefits of competition. Healthy competition encourages them to perform better and provide better bargains for the customers. However, some retail markets and locations are so appealing that they lure too many operators, thus resulting in too many competitors competing for a limited market. With so many players aspiring for a small market share, each retailer would eat into the sales volume of another. As a result, none of them would enjoy the benefits.

Very few retailers have the drawing power that would make the customer travel an extra mile only to visit the store. Location of a retail store determines the customer traffic to the store and the customer traffic for an area broadly remains the same irrespective of the existence of a particular store, unless the store itself has high crowd-drawing power. Hence, location strategy of stores with low drawing power is aimed at attracting the customer traffic that is directed to a particular location.

The presence of a number of stores in a particular locality can prove beneficial due to the increase in customer traffic. By taking competition in good spirit and making efforts to address the unfulfilled needs of customers, all retailers can make considerable profits. Retailers can sell complementary products in their stores, so that the customers view that location as a complete shopping area and attract more customer traffic.

Example: Delhi's Chandini Chowk: A Lucrative Shopping Destination

Delhi's Chandni Chowk sees a massive number of four to six lakh daily footfall. This is quite high when compared to the total combined footfall from major malls in Delhi-NCR, as stated in a report of JLL (Jones Lang LaSalle Incorporated). Shahjnabad redevelopment has further accelerated the growth of local economy and increased number of tourist footfall. Well organized and authorized commercial space will spur various national and international brands to invest in Chandini Chowk who were aspiring since long to venture into this Asia's largest wholesale market.

Source: (June 29, 2022). Daily Footfall In Chandni Chowk Bazar More Than Total Footfall Of Major Malls In Delhi NCR: Report. Retrieved from http://timesofindia.indiatimes.com/articleshow/92525146.cms?utm_source=contentofinterest&utm_medium=text&utm_campaign=cppst. Accessed on 04-07-2022

4.6.2 Merchandise

Merchandise mix refers to the total range of products that a store offers to its customers. The merchandise being offered by a store determines the perception of the customers with regard to the store. It is not necessary for retailers to follow low-price and bargaining patterns if they maintain unique merchandise.

The identification of the stores is often linked to the merchandise they offer. Retailers can cater to the needs of their target customers and retain their identity by formulating a detailed merchandise plan.

Retailers also differentiate themselves from others based on the merchandise they offer by creating in-house brands of merchandise. This concept is highly popular in the UK and to an extent in the US. In India, this type of store branding is limited to apparels and groceries. Retailers like Shoppers' Stop stock other brands along with their own, while Westside sells entirely its own brands. Other than national brands and store brands, proprietary brands are on the rise in the US. Proprietary brands help the retailers establish a strong store image, create loyalty and realize more profits. The merchandising strategy adopted by a store can be examined by mapping the store's assortment with the offered variety[1]. Some retailers like Walmart and Kmart prefer to offer their target customers a large variety of products, though with shallow assortments while some other retailers like Toys 'R' Us prefer to keep deep assortments with less variety. Retailers have to make a choice between maintaining a wide variety or deep assortment because opting for both would increase the inventory costs undesirably, making the firm uncompetitive. However, some big retailers like Sears and JC Penney manage to equip their stores with both wide variety and deep assortments.

[1] Variety of products refers to the number of different products being stored by the retailer while assortment refers to the depth of the product line or the choice offered within the product category.

4.6.3 Price

The relative strategic positioning of a retailer can be determined by its margin-turnover proportion. It is very difficult for a retailer to achieve high turnover and high margins simultaneously because if it increases the price, its customers will drift away to other retailers. Similarly, it is not possible for a retailer to sustain in the marketplace (in spite of low margins) if it has a low turnover. This leaves the retailers with only two choices -- either to maintain a high turnover by keeping low margins or to keep higher margins in spite of the low turnover. Wal-Mart is a good example of the former, while JC Penney adopts the latter practice.

Generally, retail stores, due to their low turnover, try to maintain profits by keeping high margins on the products they sell. Discount retailers try to attract customers by keeping low margins, and making profits through high turnover.

However, these pricing strategies have their disadvantages. Some retailers, who choose to maintain high margins sometimes, do not realize any profit due to low turnover. At the same time, retailers who aim at high turnover through low margins may sometimes need to sell the merchandise at lower margins as their customers get used to discounts and sales and tend to postpone the purchase until another sale.

4.6.4 Service

The kind and extent of service appropriate and feasible for each store would be different and should be determined by the managers in a particular store. The quality of both the basic and associate services (gift-wrapping, mailing, etc.) being offered by the retailer is important.

Retailers need to spend considerable amounts of money to offer good customer service. These amounts are justifiable only if the high service being offered results in some kind of payoff for the retailer. The payoff could be in the form of retained customers, or in the form of increased sales. However, retailers should always ensure that their service strategy is aligned with their market strategy. Retailers should identify specific service areas according to their market strategy. This will provide a differential advantage to the retailer.

4.6.5 Communications

The retailer should determine well in advance, the level of service he wishes to provide for particular merchandise. If a retailer chooses to provide service, which involves high costs for low-priced merchandise, it would not provide any advantage to the retailer. Likewise, if a retailer does not provide good service for high-priced items, customers would not be satisfied and this would work in favor of the competitors. However, if a retailer selling high-end merchandise provides good/superior service, customers would be delighted and would become loyal customers for the retailer. Thus, the retailer can gain strategic advantage over its competitors by offering good customer service. However, retailers selling low-priced merchandise need not necessarily provide additional or a wide variety of services. Such retailers can minimize service costs by providing just basic services and keeping the customers happy both price wise and service wise.

The market strategy of a retailer would be incomplete and ineffective if no effort is made to reach out to the potential customers. While designing the communication policy, a retailer must take care of four strategic dimensions: reach, frequency, content and personalization. Reach refers to the number of people who see an advertisement at least once. Frequency is the average number of times that a customer sees the advertisement. Content refers to the image the retailer wishes to project. Personalization is the ability to provide customized communication to customers through direct mailers or telephone using customer database.

Activity 4.1

A retail organization incorporates three components in its retail strategy: Selection of target group, positioning and differentiation, and implementation of the strategy with the support of a judicious marketing mix. Visit a departmental store and a specialty store (selling footwear) and study the differences in the strategy and its implementation in both the store formats.

Check Your Progress - 1

1. Which of the following is a strategy that defines the orientation of the firm in terms of the target market that it wishes to cater to, the retail format that it proposes to build, and the retail mix variables that it chooses to gain decisive competitive advantage and sustain its position in the retail market?
    a. Retailers strategy
    b. Retail market strategy
    c. Marketing strategy
    d. Retail format strategy
    e. Marketing mix strategy

2. Which of the following is referred to as a group of customers who have common or similar needs, which can be collectively addressed by a retailer who chose to cater to the same group or customer segment?
   a. Retail Market
   b. Market
   c. Retail outlets
   d. Target market
   e. Retailers market
3. Which of these options given below gives the least suitable description of a retail market?
   a. Both buyers and sellers meet to transact.
   b. Group of customers who are interested in the offer from the retailers and order it online.
   c. A place where buyers and sellers meet to bargain and exchange products and services.
   d. A location where retailers spread out their merchandise with a view to selling the same to customers.
   e. A place where customers meet to plan their future purchases.
4. Retailers, apart from holding branded items, also create their own brand for sales in their stores. What is this type of brand called?
   a. Domestic brand
   b. In-house brand
   c. Licensed brand
   d. Own brand
   e. Labelled brand
5. Which of the following denotes the services like home delivery, mail orders, babysitting, gift wrapping, check cashing, etc. offered by retailers?
   a. Additional services
   b. High-end services
   c. Basic services
   d. Associated services
   e. Low-end services

4.7 Achieving Strategic Positioning

After examining the factors that help build competitive advantage, we need to understand the concept of strategic positioning. When Apple Inc. entered the smartphone market, nobody would have thought that it would quickly make a deep dent in the market share of Nokia that produced low cost mobile phones with standard features specifically designed for the Indian consumers, and Samsung that was gradually side-lining Nokia through its smartphones. Ideologically it positioned itself as operating system and user interface company instead of another hardware company. It used its hardware as a tool for delivering its user interfaces, services or apps. Despite quoting premium prices for its smartphone products, its strategic positioning of 'user interfaces as a form of content' helped it grab the attention of customers and acquire the leader position in the smartphone market. To sum up, 'strategic positioning is a process of perceiving new positions that woo customers from established positions or draw new customers from the market' (Michael Porter). The supporting dimensions mentioned earlier (i.e., operations, purchasing / logistics, market research, financing and technology) also help the retailer in strategic positioning. Let us consider each of these factors separately and evaluate/analyze how each of them lends a strategic advantage to the firm.

4.7.1 Operations

The day-to-day functions in a retail outlet (staffing, maintenance and general management) should be carried out efficiently. The appearance of the stores should be appealing and the store personnel should provide good service, which is consistent with the strategy and image of the store.

Example: Operations at McDonald's

McDonald's is an America-based multinational fast-food chain with quick service restaurants. The crew members are directly responsible for food preparation, customer care and serving the food while maintaining cleanliness and hygiene. Every guest has to be treated in a friendly way while ensuring purity and cleanliness. The crew is responsible to create a warm and friendly ambience.

Source: (October 2, 2022). What Does A McDonalds Crew Member Do. Retrieved from https://www.zippia.com/mcdonalds-crew-member-jobs/what-does-a-mcdonalds-crew-member-do/. Accessed on 04-07-2022

4.7.2 Purchasing/Logistics

Retailers today are trying to exploit the purchasing and logistics distribution channels in order to gain competitive advantage. The image of a store primarily depends on the kind of merchandise and the availability of stock. Thus, it is essential for retailer to stock the right kind of merchandise that the consumers would seek and buy.

The decisions regarding logistics also play a significant role in helping the retailer achieve competitive advantage. One such logistics decision is cross docking[2].

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[2] The distribution system wherein the merchandise is pre-packed by vendor in the quantity required by the store, thus requires limited or no interim storage. Cross docking is explained in greater detail in chapter 17.

Cross docking does not only help retailers reduce their inventory and logistics costs, but also helps them reduce the lead times, thereby gaining a competitive advantage. Better control over the retailer's distribution channels helps the retailer reduce the cost and provide better service to its customers.

4.7.3 Market Research

It is important for a retailer to have a good understanding of the customers' expectations, needs, wants and behavior. The merchandise in the store should reflect the customer's choice and not the retailer's interests and assumptions. To understand the customer, the retailer should conduct market research programs from time to time. The changing preferences and trends in the market can thus be tracked, analyzed and used to the advantage of the business.

4.7.4 Financing

The importance of financial planning is often underestimated by many retailers. Short-term debt financing often causes problems to the small retailers. The retailers should give due consideration to the return on debt and equity. By planning the finances of the firm properly, retailers can have enough capital for financing various store operations.

4.7.5 Technology

In small retail stores, technology plays a supporting role, but for large retailers with multiple stores, technology plays a very important role. In fact, the use of technology is now considered a strategic decision. Technology enables smoother and hassle-free communication between the store managers and the top management. Technology provides vast amounts of information to all people concerned, which can be used to manage the store more efficiently. For example, efficient use of such information by store managers can help reduce inventory costs.

4.8 Nature of Strategic Planning

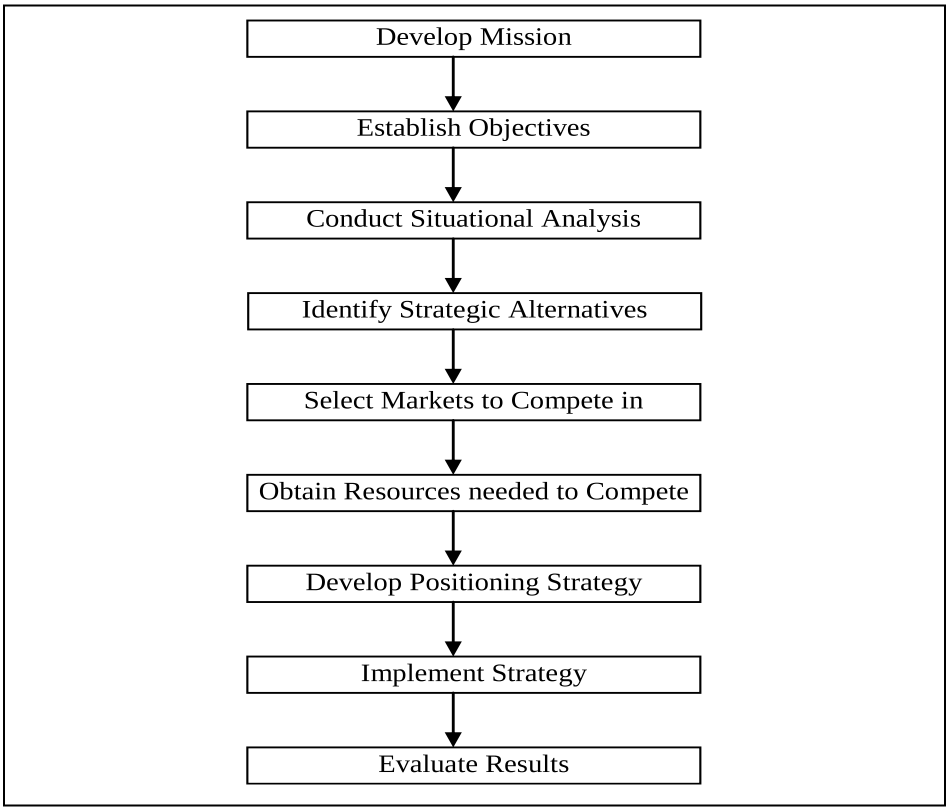
Strategic retail planning is the process by which a retailer plans the future actions of a firm by anticipating the change in environment and business patterns. It helps the retailer to anticipate the opportunities and threats that the retail firm may encounter and take suitable and timely action. Strategic planning is futuristic in nature and tends to prepare the firm for future challenges.

Window-driven planning is a strategic initiative that involves predicting the customer's demands, tastes and preferences so that the merchandise can be made available in the stores right in time, i.e., before the customers move away to the competitors' stores or before their preferences change again. This helps the retailers gain maximum advantage from the fads prevailing at a particular point of time. Depending on the nature of the opportunity (window), the retailers can choose whether to respond to it. Retailers generally respond to either those opportunities that are expected to last for a long period or those that are small but attract large number of customers. Time plays a crucial role in window-driven planning. It is essential for the retailer to identify opportunities in time. If he fails to do so, he loses competitive advantage. However, before taking up new business opportunities, it is important to analyze the situation well.

Strategic planning requires a coordinated approach and therefore all departments of retail organization should be well coordinated. Horizontal information sharing[3] should be encouraged. This would ensure that each group would have an understanding of what the rest of the organization is doing or is planning to do. Vertical information sharing[4] is also essential as it generates interest in all employees of the store. It can help reduce inconsistencies between lower-level planning and upper-level planning.

Strategic planning is generally done annually. However, with increasing competition, there is growing need to take up strategic planning more frequent. Moreover, due to changes in customers' buying patterns, economic and business dynamics, the retailer may need to re-plan its strategies. However, irrespective of the frequency of planning, strategic plans should be comprehensive and realistic.

Figure 4.2: Retail Strategic Planning Process



Source: ICFAI Research Center

[3] Information sharing is among all the departments and store groups.

[4] In vertical information sharing, the top management takes inputs from the employees who are in direct contact with customers like salespersons.

Some retailing strategies adopted by retailers are immediacy merchandising, which involves lowering the prices of products to facilitate fast movement of merchandise and relationship retailing, in which the retailer tries to attract and retain its customers by building a long-term relationship with them by special promotional offers, discounts, etc.

Example: Chick-fil-A – Purpose Well Planned by the Founder

Chick-fil-A is one of the largest American fast food restaurant chains and the largest specializing in chicken sandwiches. The founder of Chick-fil-A, is Truet Cathy, who since inception of the venture-based business on Biblical principles in 1982 set the Corporate Purpose which has guided the operations of the venture. Chick-fil-A holds its purpose at helm of all its affairs guiding the business and work. "To glorify God by being a faithful steward of all that is entrusted to us. To have a positive influence on all who come in contact with Chick-fil-A."

Source: (June 8, 2020). Our Culture and Values Chick-fil-A. Retrieved from https://www.chick-fil-a.com/careers/culture. Accessed on 04-07-2022

4.9 Retail Strategic Planning Process

The success of a retail strategy depends as much on its actual implementation as it does on how well it is designed to meet the needs of the customers. In order to sustain and grow in the highly competitive market, retailers should plan their retailing strategies carefully.

The various stages of the planning process are depicted in Figure 4.2. A detailed study of these stages has been provided below:

4.9.1 Developing the Mission

The mission of a retail firm reflects the basic purpose of its existence. A carefully developed mission statement includes such details as the products and services to be offered, scope of business, target customers, growth plans, the kind of customer service to be provided, and the attributes for competitive advantage. There is often a more detailed mission statement provided to the employees of the retail firm than the one that is publicized outside the firm. The mission statement distinguishes the retail firm from others, reflects the values that the firm believes in and provides a sense of direction to the retail personnel.

The mission statement reflects the philosophy of the top management and guides the corporate culture. The stakeholders can gain an understanding of the firm's philosophy by looking at its mission statement.

The mission statement of a firm is the foundation of the whole planning process and hence, should be precise and reflective of the firm's attitudes and philosophy. Moreover, the plans in the subsequent planning stages should be consistent with the mission statement.

4.9.2 Establishing Objectives

After the basic purpose of existence of the retail firm is known, retailers decide the objectives of the firm. The objectives are the formal statements of what the firms seek to achieve in terms of sales volume, profitability, market share, quality levels, etc. Although profit is the prime objective for the existence of the firms, some firms incorporate social objectives as well. This helps them establish a good image in the community.

Objectives are set for the short-term as well as the long-term. Short-term objectives are generally set for short periods (one to two years) while the long-term objectives are set for longer periods. The long-term objectives are not as specific as the short-term ones, but they include the strategic dimensions of the retail firm. In retailing, the long-term objectives do not stretch beyond five years owing to the highly fluid market dynamics.

Objectives should be time-specific, measurable, attainable and indicative of the business priorities. If the objectives are specific and measurable, they motivate the employees to perform better. Similarly, objectives that are not attainable discourage/ frustrate the employees. However, objectives would not serve their purpose unless they are reviewed and evaluated periodically.

4.9.3 Situational Analysis

Before implementing a strategy, a retailer should have a clear understanding of the internal and external environments. Therefore, the retailer should conduct a thorough analysis of the strengths and weaknesses of the firm and assess the opportunities and threats in the environment. The assessment of the internal and external environments is known as 'situational analysis' or 'SWOT analysis'. It helps the firm make maximum use of the existing assets of the firm and take adequate measures to correct the weaknesses.

The supply of timely and accurate information has enabled the retail firms to take more efficient and appropriate decisions. The information about the external environment and the analysis of upcoming trends by experts round the globe are very useful for the retailer.

Strengths and Weaknesses

Strengths and weaknesses are internal to the firm and can be largely controlled by the management. The financial resources, physical assets, management skills, sales force, merchandise, employees' attitude toward the company, etc. are examined to identify the strengths and weaknesses of the firm. While strengths can be optimally utilized to achieve the firm's objectives, strategies can be developed to overcome weaknesses by employing an external consultant with an expertise in weak areas or by training the store personnel or by studying similar cases in other firms.

The retailer can also make use of the information collected from employee surveys, customer complaints, accounting reports, focus groups, customer surveys, supplier surveys, etc. to assess the strengths and weaknesses of the firm more thoroughly. It also offers a critical analysis of the various practices followed by the retailer like maintaining vendor relations, designing ad campaigns, the kind of merchandise being offered and the HR practices being followed.

While assessing the strengths, the retailer pays maximum attention to the financial performance of the firm. The retail managers regularly and completely monitor the financial aspects of the firm like the costs incurred, profits, sales, assets, liabilities and net worth. Most firms limit their internal assessment to the analysis of the financial statements and reports and do not pay heed to other functional areas of marketing, purchasing & logistics, human resources. However, this should be avoided.

One of the major strengths to retailers could be the operational efficiency it has achieved over time. Operational efficiency is the ability of the firm to cut costs as the volume increases. The efficiency achieved due to high volumes that a firm churns is referred to as 'scale economies'. As the retailer gains experience in retailing, it becomes more efficient in all its operations - be it purchasing, handling or selling. Operational efficiency is certainly a factor that gives the retailer an advantage over its competitors due to the lower operating expenses it incurs. Such retailers (like Walmart) often pass on a part of these savings in operating expenses to their customers, thereby attracting more customers.

The relationship with suppliers is a factor that should be given due consideration while assessing the firm's strengths and weaknesses. Due to the improvements in technology, suppliers today have greater access to information regarding the retailers. Hence, while assessing the strengths and weaknesses of the firm, their opinions should be given due consideration. Similarly, it is important to consider the customers' perceptions of the firm's strengths and weaknesses.

Opportunities and Threats

Opportunities and threats are the factors external to the firm over which the retailer has little or no control. A firm is a part of a much bigger sphere, i.e., the business environment, the social environment, the natural environment, economic environment and the political environment. Hence, the firm needs to keep track of the external environmental constraints and responsibilities before taking any internal business decisions. The knowledge of existing rules and regulations and upcoming trends in the legal, economic, social, and technological areas can help the retailer determine favorable changes that could be grabbed as opportunities as well as unfavorable changes that could pose a threat and need to be kept under check.

Economic Conditions

The economic situation prevailing in the country determines the purchases that consumers make and the amount of money they are ready to spend. In times of economic downturn, it becomes difficult for a retailer to register any year on year sales growth. In such times, rather than attempting to induce the customers to spend more, the retailers should make efforts to gain a larger share of the market using innovative strategies. It can also do so by venturing into new markets. Weak and uncompetitive retailers are pushed out of business when the economic conditions are challenging. When economic conditions leave little or no chance for sales growth, it is referred to as 'stagnant economy'.

However, some retailers not only manage to sustain their operations under economic pressure but also manage to grow. As customers tend to cut their purchases and the amounts spent during tough times, discount retailers take advantage of the situation and attract customers from specialty and high-priced retail stores, registering sales growth. Thus, even hard times provide an opportunity for some retailers, though sometimes at the cost of other retailers.

Technological Developments

Technological innovations have had a tremendous impact on the way businesses are run. Telemarketing and e-marketing have made it possible for retailers to sell their merchandise to customers without even meeting them face to face. Technology has made transactions more simple and convenient. Credit cards have efficiently replaced cash transactions. Customers can transfer money from their account directly into the retailer's through 'Electronic Funds Transfer'.

Technology has enabled vendors and retailers to keep a track of their own as well as each other's inventory levels and schedule the selling/ manufacturing/ distribution activities accordingly. By holding minimum inventory, both vendors and retailers can save on the cost incurred in maintaining a huge inventory and can utilize the funds for other purposes. Moreover, retailers can place their orders instantly and vendors can deliver them in a few days. Thus, the order fulfillment that once took weeks now takes only a few days.

Technological changes can also be observed in the way shopping is done. Using kiosks, customers can learn about the product features and the benefits that it offers. The advent of Smart Carts has made shopping a pleasant experience. Smart carts are shopping carts equipped with technology that helps them track the contents added to the cart and total the amount of the purchases automatically with every element added to the cart.

Competitive Environment

With globalization, there has been considerable increase in competition. The number of stores is constantly increasing while the sale per store is decreasing.

Although retailers are trying to woo customers using all means, the sales have continued to decline. The retailer should be widely aware of the competitive environment and assess its competitors' moves on a regular basis.

Assessing Competition

Assessing the competition forms a critical part of the strategic planning process. Knowing the competitors helps the retailers to position themselves and gain competitive advantage. Retailers can gather information about their target customers online or through the physical environment. Some of the basic questions that the retailers would need to answer are:

Who are the consumers?

While defining the target and secondary consumer segments the following attributes should be checked:

- Gender (male, female)
- Age segments (children, teenagers, young, old)
- Socio-economic level (low, lower middle, upper middle, high)
- Taste level (classic, classic update, contemporary, leading edge)
- Interests (sports, hobbies, cars, house they own)
- Geographic reach (neighborhood, town, city, state, country, global)

What are the options?

Once the retailer knows his target customers, he needs to consider the options available and select the best option on the basis of the following parameters:

- ➢ Product – National brands or private labels, exclusively or widely available, wide variety or deep assortment
- ➢ Pricing – Regular, clearance only, everyday low price, discount every day, lowest price guaranteed
- ➢ Positioning – Niche or dominant player in a category, discount, classic or contemporary
- ➢ Service Level- Service offered is self-service, full-service or assisted self-service. On the Web, service can be relatively full-service defined as multi-access (i.e., fax, phone, and e-mail), 'live' service representatives round the clock and year or assisted self-serve via e-mail on weekdays and working hours.

Where to sell?

A retailer needs to understand the customer expectations and choose the channels to reach its target customer

- ➢ Traditional Stores – street, mall, urban, secondary markets, shop/kiosk within a store, direct Marketing through catalogue, mailings, telephone, fax, e-mail
- ➢ Online – within India, International

Why should the consumer shop here?

The retailer should be able to define clearly, the unique advantages that it provides to its customers over its competitors. Some of these have been listed below:

- Exclusive products
- Wide assortment in a specific category
- Lowest prices on national brands
- Satisfaction guarantee on purchases for a specific period (Ex: up to one year)
- Specialized information, tips and linkages that are useful for customers and encourage them to make return visits to the site
- High degree of convenience

How to trace competitors?

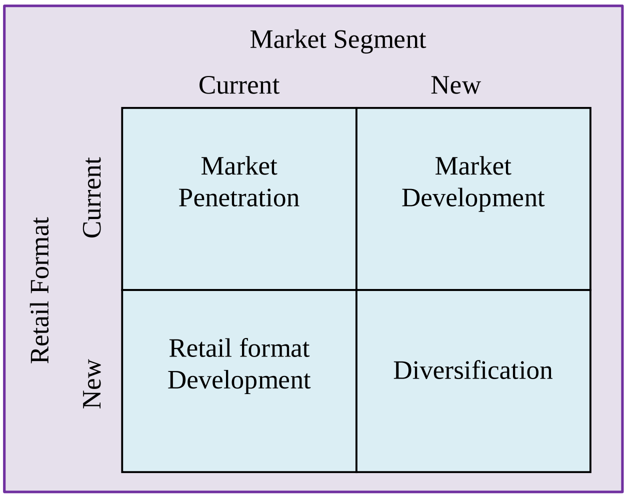
A retailer can conduct basic market research (i.e. track who its competitors are, what their strengths and weaknesses are, what kind of bargains they are offering to their customers, etc.) by employing any of the following methods:

- Listening to its current and potential customers, family and friends
- Taking vendors' opinions on the best retailers and best e-retailers for the same offerings as the retailers'
- Attending trade shows and sessions organized by other retailers and e-retailers
- Keeping itself updated with regard to fast growing product categories, changes in Internet industry, etc., through articles in trade publications, magazines and retail web-sites
- Learning the changing lifestyles of customers and changes in their spending of disposable income so that the retailer can stock merchandise according to their reallocation of expenditure
- Surfing the Net for global competitors and successful strategies (through search engines)
- Touring the newest malls and unique stores in trendy neighborhoods

4.9.4 Identifying Strategic Alternatives

The result of situational analysis forms the basis on which the retailer evaluates the strategic alternatives. The four strategic alternatives that a retailer considers are market penetration, market development, retail format development and diversification as shown in Figure 4.3.

Figure 4.3: Major Strategic Alternatives



Source: ICFAI Research Center

Example: Walmart Won't Lose Grocery Market on Price

Walmart, the US grocery retailer is known to compete on basis of price. Walmart holds 18% of US grocery market as on 2021. In 2022, deep discounter grocery stores like Aldi, Lidl also performed well amidst looming recession. Walmart chose to work with its suppliers to keep price low for its customers to ensure it continues to hold low prices as long as possible.

Source: Souza, K. (July 04, 2022). The Supply Side: Walmart says it won't lose grocery market share to dollar stores in recessionary period. Retrieved from https://talkbusiness.net/2022/07/the-supply-side-walmart-says-it-wont-lose-grocery-market-share-to-dollar-stores-in-recessionary-period/. Accessed on 04-07-2022

The retailer may also refine its existing strategies for productivity improvements. Let us now look into the role of each alternative that shapes the retail strategy.

Market Penetration

Market penetration helps the firm compete in the existing market segments with existing format by a strong market presence. Market penetration defers the firm's saturation point and builds on the existing strengths of the firm like thorough knowledge of the merchandise, huge databases about customers and their preferences. This strategy is adopted by retailers who intend to concentrate on the existing market segment and helps the retail firm increase its: number of customers, quantity purchased, and purchase frequency.

Increasing the Number of Customers

An increase in the number of customers results in more sales and increased profitability. The number of customers can be increased by opening new stores, making the existing stores more attractive, modifying the offerings of the existing stores by reviewing the merchandise, adding more brands, allocating more space to certain merchandise like apparel, etc. To increase the market penetration and maintain market share, retailers add more stores. The retailing mix variables can be used to attract the customers by:

- Offering the lowest prices in the existing market area
- Offering a wide variety of consumer goods from groceries to decorative items
- Providing better service and facilities to customers like parking facilities, convenient shopping hours and location, wide variety, systematic arrangement of merchandise, shopping carts, single-floor stores or direction signs for the different sections of merchandise at frequent locations.

Increasing the Quantity Purchased

Retailers try to create a retail atmosphere that lures consumers to buy more. They spend substantial amounts to create such an atmosphere. This is generally done by improving the layout of the stores. Some retailers have set up fast food joints and coffee parlors to increase the customers visiting the stores, thereby resulting in increased purchases.

Another approach to increase the quantity purchased is to adopt cross selling. In cross selling, salespersons from one department try to sell complementary products from the same or other departments, thus increasing the overall purchases in the store. For example, a customer who purchases a lipstick can be persuaded to buy the matching lip-liner.

Increasing Purchase Frequency

Stocking a wide variety of merchandise in the stores all through the year creates an impression among the customers that they would easily get what they are looking for. For example, the wide variety of toys offered by Toys 'R' Us all through the year assures the customers that they would have a good choice of toys even when they come to exchange the toys later. Toys 'R' Us registers round the year sales for video games and toys in the low to medium price range. Furthermore, high impulse buys like hobby kits and die-cast toys ensure high customer traffic at the stores.

The purchase frequency can also be increased by offering discounts on selected products at particular times. The discounts lure the customers to purchase the product that is presently being offered even if they did not intend to buy the product earlier.

Market Development

Market development is a bold strategic shift that involves more capital and is more risky than market penetration. Market development strategy can be executed by reaching new market segments or by expanding the existing markets.

Reaching New Market Segments

Retailers, especially food retailers try to tap new segments in existing markets by offering 'something more' to the existing merchandise/items. For instance, by adding low calorie, non-fried items to its menu, the food-chain retailer, McDonald's has attracted the nutrition conscious customers to its outlets. Coffee chains offering sandwiches and other food items, fast food restaurants adding soups and doughnuts to their menu are good examples of strategies retailers adopt to broaden the existing product lines and attract new customer segments.

New market segments can also be targeted by opening up new outlets at non-traditional locations like hospitals and railway stations. The toy retailer, Toys 'R' Us has expanded its offerings by adding a 'Baby Boutique'. The baby boutique sells high-end nursery items, thus reaching a new segment of expectant parents.

Market Expansion

Market expansion based on geographic spread is a strategy that has been successfully adopted by retailers for a long time. A store concept that succeeded at one place is generally expected to work at other places. Such a strategy is most often followed by franchise retailers. Retailers even go in for cross-border expansion when their home market is saturated. For example, the Spanish retailer Zara, which, a decade ago had its operations only in Spain and a few stores in Portugal, now has stores all over the world. Retailers can also go for market expansion by catering to new markets. For example, a retailer could expand by introducing low-priced merchandise in the same store. The market expansion can extend to establishing an online store. Many grocery retailers have realized the importance of an online presence for penetrating deeper into the existing markets, developing individual customer relationships and increasing the return on investment.

Retail Format Development

Retail format development is done either by introducing a new retail format or by polishing/developing the retail format that is in existence presently. The retail format may be developed either to adapt to a particular geographic dynamics or because it is convenient to adopt. For instance, the limited menu offered by food retailers like McDonald's outlets in big stores is a form of retail format development.

Another form of retail format development is to introduce new forms of selling like electronic or catalog retailing to improve the convenience to the customers or to attract new customers.

Diversification

Diversification is an overall shift in focus. A retailer can enter into new markets with an entirely new retail format. The diversified retailer serves new customer groups by offering products or services that it had never offered before. For instance, Toys-R-Us' entered the kids' apparel market with its Kids-R-Us chain. This is an example of diversification into a related area.

Productivity Improvement

By adopting this strategy, retailers aim to improve productivity. Firms generally go for productivity improvement strategy when they are in the mature or decline stages of the lifecycle. The main objective of firms in mature or decline stages will be to extract as much profits as possible from the existing formats and markets by refining their existing strategies (without making any further investments). For example, in areas where Walmart reaches saturation, it closes down its smaller stores in surrounding towns and opens regional "Superstores" that offer groceries, auto repair, and other services. Retailers can increase the productivity by undertaking cost reduction, increasing merchandise turnover or prices and margins.

Cost Reductions

When trying to achieve improvements in productivity through cost reductions, retailers try to implement self-service schemes to reduce the labor requirements. Some other ways for reducing costs are reducing the store hours, making better use of the part-time helpers and cutting on customer services. The emergence of sophisticated technologies helps retailers in cost reduction planning by providing information on individual contributions of each of the items in the merchandise towards the total profitability of the firm. The merchandise can, thus, be planned according to the merchandise movements. This helps cut down inventory costs without compromising on the availability. Technological innovations also help cut costs. For example, using electronic data interchange with suppliers saves costs by eliminating the need for paper-based transactions.

Increasing Merchandise Turnover

Better merchandise mix results in increased merchandise turnover and increased turnover, in turn, results in improved productivity. The merchandise mix can best be improved by having access to real-time information from the point-of-sales terminals. The retailer can thus ensure the right merchandise mix that not only helps in protecting its desired/established image, but also improves the productivity through increased customer satisfaction. Some retailers encourage store managers to introduce certain items on a trial basis so that they gain an understanding of changing market demands. Another way to improve the merchandise mix is to broaden the mix. This is done by storing a broad variety of items in the merchandise.

Increasing the Prices and Margins

While formulating productivity-based strategies, retailers need to pay special attention to the aspects of prices and margins of the merchandise. The retailers cannot afford to raise the prices of all products they offer because doing so would compel the loyal customers to withdraw. However, the retailer can select a few low-visibility items or items that are not purchased often, and retain higher margins on those items or the retailer can simply add high-margin items to its merchandise as superstores do. Retailers can also charge certain sums for installations or deliveries based on the total purchase amount.

Selecting the Target Markets

After evaluating all the strategic alternatives, the retailer selects the one that promises maximum profit and offers the best scope for growth. Then, the retailer would need to select the target market that it wants to cater. The retailer should first segment the population and identify the target markets.

Segmenting the Market

A *market segment* refers to a group of customers whose needs will be satisfied by the same retail offering because they have similar needs and go through similar buying processes. Retailers define and determine each group of people who have some common attributes. These attributes could be demographic in nature, i.e., based on age, income, occupation, etc. or based on psychographics i.e., the activities, interests, opinions, etc. Basically, retailers use demographics for segmentation, while they use psychographics to supplement the demographic segmentation.

While segmenting the markets, the retailer should ensure that the market segments are:

Measurable: The segments should be identifiable and quantifiable.

Accessible: The marketing efforts should be directed towards the selected segment and the marketing efforts should have a positive impact and produce the desired outcome.

Economically Viable: The chosen market segment should be big enough to be economically viable for the retail firm to focus its marketing efforts on them.

Stable: The selected attributes of segmentation should be reliable indicators of market potential.

While developing the market strategy, depending on the products offered, the retailers can perceive customers in one of the following ways:

Similarity: The retailers perceive that the consumers are all similar and that a standard product will satisfy the needs of most of the customers. Though age, needs, income, preferences, etc. differ among various customers, the basic premise is that these attributes do not influence the purchases they make. For example, all the convenience stores primarily focus on providing convenience to the customers by offering a good merchandise mix, wide variety and good assortments. They assume that all customers look for convenience while shopping. They do not look into the differences in thinking that may exist in a few customers, for whom convenience may not be the primary concern.

Differences-similarities: The market demand is influenced by the differences and similarities in consumer preferences. Customers are grouped based on these differences (or similarities) and then the retailers to focus on their target customers, use the aggregate of these groupings as the base. For instance, young fashion-conscious women in mid-income group could be segmented for an apparel retailer.

Uniqueness: Every customer is different from the other and this difference is what makes a customer unique as an individual. Hence, a standard product cannot appeal to all the customers alike. However, customers with somewhat similar preferences can be included in one segment and retailers can make tailor-made offers for such groups.

Target Markets

Target markets are the market segments that the retailer wishes to serve. Market positioning of a retailer reflects the kind of image the retailer wants to establish among its target group and the group of retail firms with which it wishes to compete and coexist. When trying to build an image in target customers' minds, retailers should look into the attributes that constitute the image of the stores. These attributes vary along the different age groups.

Target Market Selection

To finalize the target market, the retailer first takes the entire market into consideration. The size of the market as a whole is considered along with the different customer segments that it could serve or who would be interested in the retailer’s offerings are short-listed. Then, the segments that the retailer could best appeal to and serve most effectively are chosen as the possible target markets.

These possible target markets are evaluated further to finalize the target markets. Evaluation is done based on attributes like future growth potential. These are shown in the Table 4.1. Final target markets are thus selected based on the best match of these attributes with retailer's interests.

Each of the attributes is given a certain weightage and each possible target market is rated against it. The product of these weights and ranks gives the total score for each possible target market. This score enables the retailer to evaluate the attractiveness of each target market objectively and select the final target market(s).

After finalizing the target market, the retailer focuses on developing strategies to draw customers by in-depth study of their behaviors, values, motives and expectations. The retailer also tries to understand the decision making process of the customers.

The following Table illustrates the method of market attractiveness evaluation

Table 4.1: Market Attractiveness Evaluation

Factor	**Weight (a)**	**Potential Target Markets**					
		Young Professionals		**Teens**		**Middle Age**	
		Rating (b)	Score a × b	Rating (c)	Score a × c	Rating (d)	Score a × d
Future growth potential	25	7	175	9	225	5	125
Present style	15	6	90	6	90	8	120
Investment required	5	7	35	7	35	6	30
Strength of competition	15	7	105	7	105	8	120
Ability to meet the needs of market	15	8	120	9	135	6	90
Profit potential	25	5	125	6	150	4	100
Total Score	**100**		**650**		**740**		**585**
Rating is in a scale of 1 to 10 where 1 is very unattractive and 10 very attractive							

Note: *Parameters of evaluation based on more than one source.*

Compiled from various sources by ICFAI Research Center

Obtaining Resources Needed to Compete

The retailer can choose to enter the retail business either by starting a new firm, by acquiring an existing business, by entering into partnership with an operating firm, through a joint venture with a successful retail chain abroad or through franchising. The decisions regarding obtaining the resources depend on the way the retailer chooses to enter the retail business. If the retailer chooses to acquire an existing firm, it may not need to arrange physical resources, as they are already available. The retailer can thus focus his entire attention on acquiring financial and human resources. Financial and human resource planning should be in line with the firm's overall strategy. These have been explained in the subsequent units.

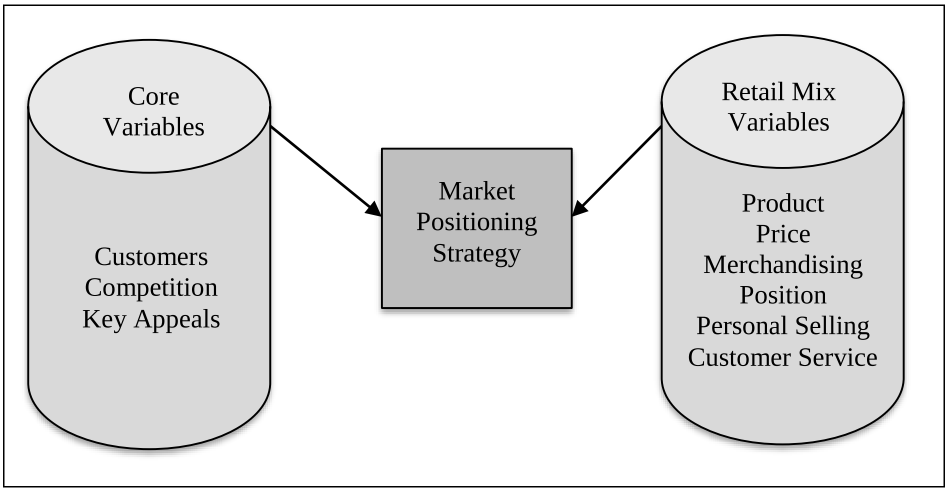
Once the necessary resources have been obtained, the firm needs to position itself in the market. Through positioning, the retailer tries to create a strong image of the firm in the minds of the target customers and thus invoke the kind of response that the retailer desires. Positioning should be such that the consumers should be able to distinguish clearly the retailer's stores from that of the competitors'.

Developing a Positioning Strategy

In these days of intense competition and diminishing differentiation among various retail firms, the importance of positioning has increased. Retailers use 'Positioning Map' to understand the position of other firms in the market place. A positioning map is a two-variable map drawn based on some selected attributes. For example, for apparel retailers the two attributes would be fashion vs. assortment, for departmental store they would be quality vs. price. The positioning map gives the retailer a clear picture of the relative positioning of the firm with regard to its competitors. Thus, retailer can decide whether to reformulate its positioning strategy or to improve the existing strategy. Repositioning can be done by broadening the assortments, re-pricing, etc.

The various variables that affect the market positioning of a retail firm are depicted in Figure 4.4.

Figure 4.4: Market Positioning Strategy



Source: ICFAI Research Center

There are two types of variables: core variables and retail mix variables. Both sets of variables together form the positioning strategy for the retail firm. The retailer takes certain decisions with regard to the retail mix variables, some of which are:

Product: Decisions relating to the width, depth and assortments, brands (company brands or store brands or generic brands), selection of suppliers, choice of inventory levels

Price: Decisions regarding the store's pricing policy in relation to market prices, price adjustments, price levels

Merchandising: Decisions regarding the store design and layout, presentation of the merchandise

Promotion: Decisions concerned with the allotment of budget for advertising, sales promotions, public relations

Personal Selling: Decisions on the number of salespersons employed, training, compensation

Customer Service: Decisions of the services to be offered return and exchange policy, credit policy

Strategy Implementation

The efforts undertaken by the retailer in thinking, researching and planning can be futile if the strategy is not implemented properly. The implementation process involves developing action plans and assigning the ownership, establishing critical paths and linking the action plans to operating plans. The main objective of all these strategies is to create value for customers.

The practices of the firm should be customer-oriented. The merchandise sold should be attractive and advertising and promotions should appeal to them. Salespersons and other store personnel should be knowledgeable and friendly.

Evaluating Results and Controlling Operations

The effectiveness of a strategy can be known only by measuring the performance of the implemented strategy. Once the plan is implemented, it is essential to monitor the various activities to determine how effective the plan has been. If the objectives are not achieved as targeted, a re-analysis needs to be done either by revamping the strategy (if the problem is found to be with improper planning) or by re-implementing the plan (if the implementation was not carried out properly).

Periodic evaluation of the strategies implemented, will help the retailer in understanding their suitability in the changing market situations so that it can revamp its strategies at an early phase. The overall aspects of the plan, i.e., the merchandising plan, financial plan, pricing plan, distribution and sales support plan, human resources plan should all be considered while evaluating the firm's strategy. The merchandising plan, financial plan, pricing plan, advertising and promotional plan, information systems plan, distribution plan, human resources plan should all be reviewed. Such an overall evaluation guarantees that the changes in individual plan that are made periodically do not disrupt the overall strategy of the retail firm. It also helps the retailer plan the individual variables in a way that would strengthen the overall competitive strategy.

Strategy for Modern Indian Retailing: Key Implications

The Indian retail industry has experienced high growth in the last couple of decades and has now moved towards the concept of modern retailing. The market penetration of organized retailing has increased from 6-8 percent (in 2005-06) to 8-10 percent in 2018-19. Many factors have catapulted the growth of organized retailing. These include: (i) a growing and robust economy; and (ii) a rise in retail expenditure across India through the internet coupled with the smartphone revolution. The above factors have forced retailers to rethink their market strategy, keeping the following changes in mind:

- Retailers need to provide a frictionless interactive shopping experience to customers through technology-oriented retailing. Today, the customers have access to information related to their purchase and want control over their shopping process.
- The level of competitive intensity is increasing at an increasing rate after the advent of well-funded e-commerce players and the emergence of hyper-local regional retailers leading to consolidation of the industry.
- Retailers need to focus on setting higher standards of customer service and shopping experience centered around the development of experience stores interconnected with other operating channels such as mobile applications, websites, and interactive kiosks.
- Retailers will need to emphasize on value-added services (e.g., installation, insurance, warranty, as well as maintenance and repair) as a critical point of differentiation in a growing hypercompetitive business environment.
- Retailers need to curate, localize as well as reimagine their value proposition by building on product exclusivity, social media presence (as a selling and customer service platform), and content marketing.
- Retailers and vendors need to display improved supply chain collaboration in the wake of economic changes since the introduction of the Goods and Services Tax (GST). Consequently, they need to re-engineer their supply in a way to minimize tax incidences and maximize their benefits of access to a cohesive market.
- With e-commerce becoming a primary retail channel, retailers must reassess their security measures aimed to minimize online frauds as the Indian Companies Act, 2013, has highlighted the need for greater responsibility assumed by the board of directors of firms towards ensuring accountability towards implementing and maintaining a vigil in this regard.
- Retailers need to become customer-focused from product-focused by adopting a renewed approach towards human resource management. They should implement technology-oriented training programs to equip their employees (especially frontline employees) in specialized areas such as merchandising, customer service, inventory management, and supply chain management.
- There is a steady increase in retail consumption among the Tier-II and Tier-III Indian cities. Moreover, the exponential growth of internet users, coupled with sales of smartphones, also led to retailers expanding their investments with higher confidence in the above cities.

Therefore, retailers are adopting the following six-pronged approach to attain profitability in today's dynamic and hyper-competitive Indian retailing industry.

1. Retailers are making continuous endeavors to understand the ever-evolving customers' needs and preferences. They have appointed chief customer officer (CCO) who is responsible for understanding the changing customer needs and preferences. The responsibility of the CCO is to customize the product assortment to be maintained at the stores keeping in mind the local market dynamics.
2. Retailers are developing a customer-centric value proposition harnessing the collective intelligence of their customers in terms of their opinions about the retailers and its marketing mix elements (such as their product assortment, customer service, pricing, promotion, and location). Retailers are moving beyond quality towards inculcating innovation while designing their value proposition aimed at providing better shopping experience to their customers.
3. Retailers are attempting to integrate the shopping experience of customers across various touchpoints (both offline as well as online). Consequently, they are taking leverage of the digitalized connectivity to bridge their offline with online businesses. Furthermore, they are taking advantage of technology in streamlining their supply chain management to attain a competitive advantage.
4. Retailers are increasingly institutionalizing analytics in their organization and developing a data-driven culture in their decision making. They are using the above approach in building an operating model with analytics at the heart of their decision making. The above approach aims to improve their bottom line by enhancing the assortment mix, optimizing inventory management, and streamlining their supply chain.
5. The digital world presents a gamut of privacy and security risks associated with people, processes, and public relations. Furthermore, retailers are putting in place the process of monitoring brand-related communication with the public at large, especially on social media. It may originate officially from the organization or its employees in their capacity on behalf of their organization. It is important because social media is becoming a powerful communication tool that can enhance or deteriorate the brand image of an organization.
6. Retailers are accelerating their investment in modern technologies (e.g., cloud-based technologies) as they consider it as a source of competitive advantage. Despite their short lifecycle, they realize that the return on investment (ROI) on technological solutions is long term. However, Indian retailers are still in the process of recruiting and training employees who could enable their organization to identify and solve issues using new-age retail technologies.

To conclude, the above discussion outlines the critical success areas which a retailer needs to keep in mind while designing their retail strategy in the contemporary Indian scenario. It outlines significant factors that will shape the business model of retailers in a flexible way that is agile to the changing dynamics of the Indian retailing landscape. The above factors will help retailers to leverage technological advancements to their advantage in a way that helps them convert market intelligence into actionable knowledge. It will enable retailers to create a demand chain, thereby evolving their organization from being product-centric to customer-centric. It also helps retailers in adapting their business models to overcome various challenges posed by the dynamic and hypercompetitive Indian retailing industry. These changes could be across the different elements of their retail mix, such as store formats, communication channels, assortment mix, supply chain management, and human resource policies. The above changes will help retailers to provide an interconnected, seamless, and superior shopping experience to their customers, thereby boosting their ROI and building their competitive advantage.

Activity 4.2
Visit a leading mall in your city and evaluate the location of the mall based on the following parameters: Nature of site, traffic attracted by the location, characteristics of the traffic, neighbourhood and characteristics of neighbourhood, competition in the proximity and its influence on the profitability of the mall, nature of the target audience like affluence, education level etc., expected profitability of the mall etc.

Check Your Progress - 2

6. Which of the following planning initiatives is a strategic initiative that involves predicting the customer's demands, tastes and preferences so that the merchandise can be made available in the stores right in time, i.e., before the customers move away to the competitors' stores or before their preferences change again to Immigration?
   a. Market planning
   b. Retail planning
   c. Customer driven planning
   d. Window-driven planning
   e. Window planning

7. Which of the following reflects the philosophy of the top management and guides the corporate culture?
   a. Departmental goal
   b. Personal Goals
   c. Organizational objectives
   d. Organizational culture
   e. Mission Statement
8. While segmenting the markets, the retailer should ensure certain aspects that the market segments should be. Which of the following are correct?
   a. Measurable, accessible, stable and economically viable
   b. Measurable, accessible and economically viable
   c. Measurable, accessible, and stable
   d. Accessible and economically viable
   e. Measurable, accessible, stable and identifiable
9. There are two types of variables for retail firm positioning strategy: core variables and retail mix variables. Both sets of variables together form the positioning strategy for the retail firm. Which of the following are the elements of core variable?
   a. Customer, competitors, and key decisions
   b. Customer, competitors, and key customers
   c. Customer, competitors, and key segments
   d. Customer, competitors, and key markets
   e. Customers, competitors, and key appeals
10. What are the variables considered by a retail firm for its positioning strategy?
    a. Product, price, and merchandising position
    b. Personal selling and customer service
    c. Product, price, merchandizing position, personal selling, and customer service
    d. Product price and customer service
    e. Product, price, place, and promotion

4.10 Summary

- The importance of formulating a retail strategy is understood by all small and big retailers. To build a competitive advantage that can be sustained, retailers need to pay special attention to aspects like price, location, merchandise, service and communications.

- Operations, purchasing/ logistics, market research, financing and technology, which determine the strategic positioning of the firm are also equally important. In this chapter, we discussed how each of these factors affects the firm's image.
- To utilize the limited human, financial and physical resources optimally, retailers should have a well-planned strategy.
- Thus, retailers should follow a systematic planning process for formulating and implementing the strategy. All the efforts of retailers are directed at the customers. Therefore, they should take every care to ensure that the customer gets the right impression and image of the stores.
- Periodic reviews and evaluations will help the retailer to take corrective actions either by re-planning the strategy or by implementing it more effectively.

4.11 Glossary

Market Segment: It refers to a group of customers whose needs will be satisfied by the same retail offering.

Merchandise Mix: It refers to the total range of products that a store offers to its customers.

Merchandising: It means decisions regarding the store design and layout, presentation of the merchandise.

Mission Statement: It reflects the philosophy of the top management and guides the corporate culture.

Retail Market Strategy: It is a statement, which defines the orientation of the firm in terms of the target market that it wishes to cater to, the retail format that it proposes to build, and the retail mix variables that it chooses to gain decisive competitive advantage and sustain its position in the retail market.

Retail Market: It refers to a group of customers who have common or similar needs, which can be collectively addressed by a retailer who chose to cater to the same group or customer segment.

Situational Analysis: The assessment of the internal and external environments is known as 'situational analysis' or 'SWOT analysis'.

Strategy Implementation: Developing action plans and assigning the ownership, establishing critical paths and linking the action plans to operating plans by a retailer.

Target Markets: It is the market segments that the retailer wishes to serve.

4.12 Self-Assessment Test

1. Define retail market strategy.
2. Explain the core dimensions of retail positioning strategy.
3. Explain the various steps of retail strategic planning process.
4. What are the various variables that affect the market positioning of a retail firm? Explain.
5. A retailer faces competition on a daily basis in the market. What are the various methods employed by retailers to trace competitors in the market?

4.13 Suggested Readings/Reference Material

1. Giri Arunangshu and Chatterjee Satakshi, “Retail Management: Text & Cases” Paperback, PHI Learning Pvt. Ltd., 2021.
2. Swapna Pradhan, “Retailing Management: Text and Cases”, McGraw Hill, Sixth Edition, 2020.
3. Barry Berman, Joel R Evans, Patrali Chatterjee and Ritu Srivastava, “Retail Management”, Thirteenth Edition Pearson Education, 2017.
4. Gibson G. Vedamani, "Retail Management”, 5th edition, Pearson Education, 2017.

4.14 Answers to Check Your Progress Questions

1. (b) Retail market strategy

A retail market strategy is a statement, which defines the orientation of the firm in terms of the target market that it wishes to cater to, the retail format that it proposes to build, and the retail mix variables that it chooses to gain decisive competitive advantage and sustain its position in the retail market.

2. (a) Retail market

A group of customers who have common or similar needs, which can be collectively addressed by a retailer who chose to cater to the same group or customer segment, are referred as retail market.

3. (e) A place where customers plan their future purchases.

A Market is a place where buyers and sellers meet to bargain and exchange products and services. All options, except e, give a suitable description of a market. Option e, which states that market is a place where buyers plan their future purchases is not a suitable description of a market place. Buyers could do the planning in any place.

4. (c) In-house brand

The own brands of merchandise of a retailer is termed as in-house brand.

5. (d) **Associated services**

Services like home delivery, mail orders, babysitting, gift-wrapping, check cashing, etc. are referred to as associated services. It is an extension of the basic service provided to the customer.

6. (d) **Window driven planning**

Window driven planning is a strategic initiative that involves predicting the customer's demands, tastes and preferences so that the merchandise can be made available in the stores right in time i.e., before the customers move away to the competitors' stores or before their preferences change again.

7. (e) **Mission statement**

The Mission statement reflects the philosophy of the top management and also guides the corporate culture.

8. (a) **Measurable, accessible, stable and economically viable**

While segmenting Retailer should ensure that the market segments are: *Measurable, Accessible, Economically Viable, and stable*

9. (e) **Customer, competitors and key appeals**

There are two types of variables for retail firm positioning strategy: core variables and retail mix variables. The core variables consist of three elements, i.e. customer, competitors and key appeals.

10. (c) **Product, price and merchandising position, Personal selling and customer service.**

There are two types of variables for retail firm positioning strategy: core variables and retail mix variables. The retail mix variable consists of Product, price merchandising position, Personal selling and customer service.

Unit 5

Financial Strategy

Structure

"The budget is the key to a successful financial future."

- Benjamin Franklin

5.1 Introduction

Business firms operate for profits and good financial future. Budget is the key for sound financial planning for any organization. Sales budgets aid the sales department to spend properly on potential requirements.

The income statements and balance sheets of all retailers contain information regarding the performance of their stores. However, only a few retailers take the time to understand and analyze these financial figures to measure the performance of their retail stores. Retailers who take time to study these figures are able to develop business models and generate more profits than other retailers who operate in similar environment. This is because these retailers focus their resources on areas, which are most important for profit generation. By doing so, they earn a higher return on investment.

Retailers use various financial ratios like gross margin, net profit margin, asset turnover, and financial leverage to measure the performance of their stores. The strategic profit model, a comprehensive framework based on all these ratios, can be used to understand the ability of various financial strategies to achieve a retailer's profit objectives.

In this unit, we will examine the strategic profit model and two important financial documents, the income statement and the balance sheet. We will then discuss how a retailer can measure the performance of his store using the strategic profit model. The performance objectives of retailers and the various performance measures used by them will also be discussed.

5.2 Objectives

After reading through this unit, you should be able to:

- Discuss the mathematical relationship involved in a Strategic Profit Model to understand the financial components revolving around a business
- Relate the different elements of income statement that enable business operations
- Explain the elements of a balance sheet that relates to the overall performance of the company
- Construct performance objectives that underlines the goals to be set for top management
- Evaluate performance measures that helps in reviewing strategic plans.

5.3 Strategic Profit Model – An Overview

Generally, most businesses operate on the premise that they need to get a good return on investment. Operating results such as sales and profits are measures that depend on the level of psychological value created for customers: the greater the perceived consumer value, the stronger the competitive advantage, and the better the strategy.

Example: Strategic Profit Model Components @ Avenue Supermarts

Example: Avenue Supermarts Limited scored the highest net profits, around 11.65 billion Indian rupees, in the financial year 2021. Due to the COVID-19 pandemic lockdowns, many companies incurred losses. Aditya Birla Fashion and Retail Limited witnessed losses of around 6.5 billion rupees.

Financials of Avenue Supermarts for FY 2021 are:

- Total Assets =13,655.97 crores
- Net profit = 1165.3 crores
- Net worth = 12,305.28 crores
- Net Sales at ₹ 7,303.13 crore

Strategic Profit Model Components can be calculated as given below:

a) Net Profit Margin = Net Profit / Net Sales = 1165.3/7303.13= 0.1595

Inference: The above net profit margin calculation infers that for each 1 rupee revenue earned by Avenue Supermarts it earns ₹ 0.159 in net profit.

Contd….

b) Asset Turnover = Net Sales / Total Assets = 7303.13/ 13,655.97 = 0.5347

Inference: The above Asset Turnover ratio of Avenue supermarts show that the efficiency of the company's assets in generating revenue or sales is good.

c) Financial Leverage = Total Assets / Net Worth = 13,655.97/12,305.28 = 1.1097

Inference: The above Financial Leverage ratio of Avenue supermarts is more than 1 which shows that it could be quite risky for the company.

d) RONW = Net Profit Margin x Asset Turnover x Financial Leverage = (0.1595 X 0.5347 X 1.1097) x 100 = 9.46 %

Inference: The above RONW indicates that for every Rupee of equity in 'books,' Avenue Supermarts. generated a 9.46 % return.

Sources: Avenue Supermarts Ltd. Annual Report (20-21),
i) https://www.moneycontrol.com/financials/avenuesupermarts/consolidated-balance-sheetVI/AS19#AS19 &

ii) https://economictimes.indiatimes.com/avenue-supermarts-ltd/balancesheet/companyid-45987.cms (accessed on 16/9/22).

The retailing business is no exception. Though retailers adopt different strategies, they pursue the same financial goal, i.e., earning a good return on investment. The strategic profit model (SPM) is a tool for planning and evaluating the financial performance of retailers. It combines information from the income statement and balance sheet into a single, comprehensive framework. The strategic profit model establishes a mathematical relationship among net profit margin, asset turnover, and financial leverage. By so doing, it arrives at two important performance measures for return on investment- return on assets and return on net worth. This model regards return on net worth as an important indicator of the performance of a firm. Return on net worth measures how much income was generated on the investment made by the owners of a firm. It therefore shows how much value a company has created for its shareholders.

The performance ratios required to calculate the return on net worth are net profit margin, asset turnover, return on assets, and financial leverage.

Different components of the model are:

Net Profit Margin = Net Profit / Net Sales

Asset Turnover = Net Sales / Total Assets

Return on Assets (ROA) = Net Profit / Total Assets

Financial Leverage = Total Assets / Net Worth

Return on Net Worth (RONW) can be calculated as follows:

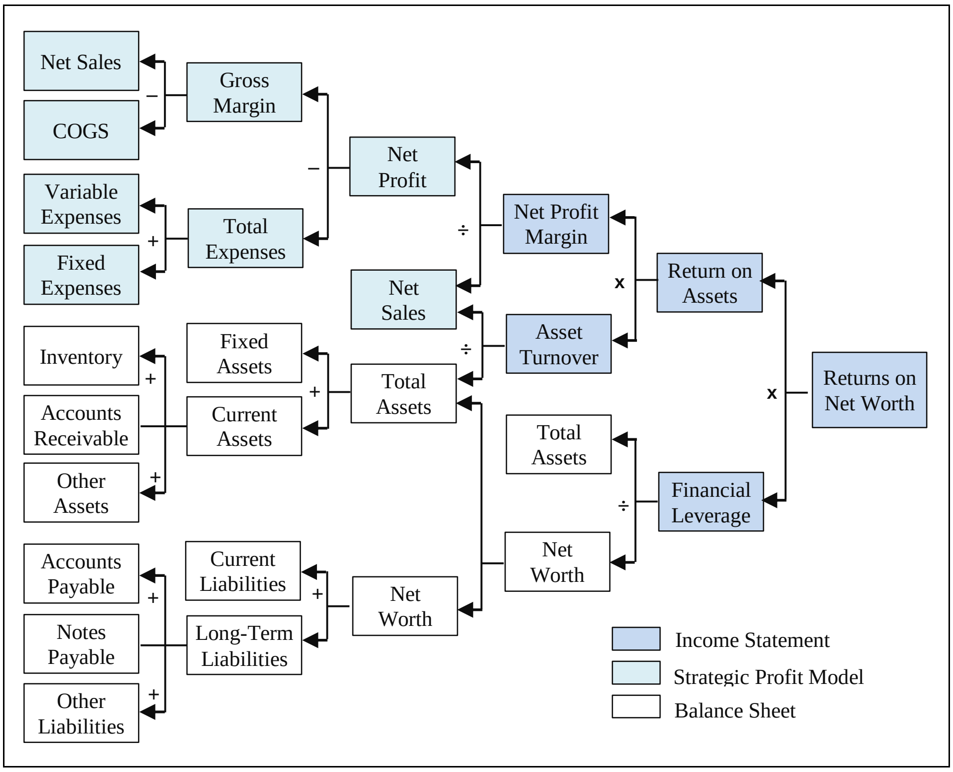
RONW = Net Profit Margin x Asset Turnover x Financial Leverage

= Return on Assets x Financial Leverage

(Return on Assets = Net Profit Margin x Asset Turnover)

Figure 5.1 gives a graphic representation of SPM. The various performance ratios shown in the strategic profit model can be calculated from the financial documents (income statement and balance sheet) prepared by retailers. While the profit margin can be derived from data provided by the income statement, asset turnover and financial leverage can be derived from data provided by the balance sheet.

Figure 5.1: Understanding the Strategic Profit Model



Source: ICFAI Research Center

5.4 Income Statement

An income statement, a type of financial statement, gives the profitability level of the retailer for a given year. It furnishes the overall picture of sales and cost of goods sold. Based on this statement, a firm can plan to either increase sales or reduce cost of goods sold or formulate a strategy for a combination of both to gain a realistic look of future profits. The income statement is one of the important financial statements prepared by retailers to keep track of the performance of their retail stores. It summarizes the financial performance of a company for a given accounting period (usually one year). The statement shows how much revenue the company earned through its operations, and the expenses associated with bringing in that revenue. The difference between the revenue and the expenses reflects the profit earned by the company. Thus, the statement shows how profitable the organization is. The income statements can also be broken down - by division, by department, by branch, and by geographic segment; thus, giving the retailer detailed information on the performance of each micro unit of the firm. The data can be compared with industry benchmarks to give the retailer an idea of the firm's position with reference to its competitors. Table 5.1 shows income statement of a hypothetical store ABC Ltd.

Table 5.1: Income Statement of a Fictitious Company ABC Ltd. (₹ in '000s)

Net Sales	578,269
Less: Cost of Goods Sold	350,421
Gross Margin	227,848
Less: Operating Expenses	141,544
Less: Interest Expenses	6,423
Total Expenses	147,967
Net Profit Before Taxes	79,881
Less: Taxes	31,438
Net Profit After Taxes	48,443

Source: ICFAI Research Center

Sales

The total revenue received from the sale of merchandise is known as gross sales. Net sales are arrived at by subtracting the returns and allowances from the total revenue received. The term returns refers to the value of the merchandise that has been returned by customers (Goods are returned either because they are defective or because they did not satisfy the customer). The term allowances refer to the additional discounts and price reductions that are given to customers by the retailer. Thus, Net Sales = Revenue received – Returns – Allowances.

Sales are an important indicator of the performance of a firm. Sales figures, which all retailers strive to increase, show how active a firm is in the marketplace. If sales are higher than those achieved in the previous year, the firm is on growth path. If sales are less than those achieved in the previous year, the firm is in trouble. To stem the decline in sales the retailer must take corrective measures or change its present strategy.

Cost of Goods Sold

The cost of goods sold includes the direct cost associated with manufacturing/ procuring the merchandise for the store. These costs include transportation costs and costs that are directly related to producing or purchasing the goods. Simply put, it is the price paid by the retailer to produce or acquire goods for sale.

Gross Margins

The gross margin refers to the difference between net sales and the cost of goods sold. It is also expressed as a percentage of net sales.

Gross Margin = Net sales – Cost of Goods Sold

Gross Margin % = Gross Margin/Net Sales

$$\text{Thus ABC Ltd. gross margin\%} = \frac{227{,}848}{578{,}269} \text{X100} = 39.4\%$$

The gross margin indicates the profitability of a company. It shows how much money is available for providing a profit and covering the retailer's expenses. Thus, a high gross margin indicates high revenues and the financial ability to improve the business operations (like marketing, new product development). Retailers can use gross margins to compare the performance of two product lines or stores. A higher gross margin also implies that the store is efficient in procuring and selling merchandise.

Expenses

There are two major types of expenses, interest and operating expenses. Interest expenses refer to interest payments that have to be paid periodically for financing provided by lenders like banks. Operating expenses refer to expenses incurred by stores for their day-to-day operations.

There are three main categories of operating expenses: selling expenses, general expenses, and administrative expenses.

- Selling Expenses include salaries of sales staff, commissions etc.
- General Expenses include rent, utilities, and other miscellaneous expenses.
- Administrative expenses include salaries of staff other than salespeople and expenses like office supplies, postage etc.

Usually expenses of department stores are higher than the expenses of discount stores and warehouse clubs. This is because department stores are located in prime areas where rent and other expenses are high. In addition, to providing a high level of customer service, department stores incur expenses for retaining experienced sales persons and maintaining a good store ambiance. The expenses of discount stores are lower because they are located in less expensive areas, and they offer minimal customer service.

Net Profit

The term net profit is more popularly known as "bottom-line" in business circles. It is derived by subtracting the cost of goods sold and expenses from net sales. Net profit can be expressed either as before taxes or after taxes.

Some analysts are of the opinion that profit before taxes should be considered for decision making, as taxes are not in the control of the retailer. However, generally, profit after taxes is considered for decision making as that is the amount, which a retailer is left with for distribution to shareholders, for reinvestment in the company or for repayment of any debt.

Net profit = net sales – cost of goods sold – expenses

The net profit margin is expressed as a percentage of net sales:

Net profit margin % = Net profit/Net sales

$$\text{Net profit margin\% of ABC Ltd. is} = \frac{48{,}443}{578{,}26} \text{ X100=8.38\%} \longrightarrow \textit{eqn 5.1}$$

A company must make a profit to survive and compete in the marketplace. The net profit is one of the key indicators of a company's financial performance. If a company shows low profits or losses, either the company's costs are exceeding its revenues or it is not achieving an adequate volume of sales. Thus net profit acts as a yard stick for gauging the performance of the company. The net profit margin is one of the components of SPM.

Example: Income Statement of Adidas-Sports Retailer

In 2021, Adidas revenues recorded a growth of 16% on a currency-neutral basis to € 21.234 billion from € 18.435 billion in 2020.

- Sales of its products increased across all segments/markets with EMEA, North America, and Latin America being strong markets for it with double-digit improvements.
- Net sales by product category of Adidas are: Footwear sales increased by 13%, Apparel revenues increased by 20%, accessories and gear sales increased by 22% in 2021.
- The gross margin of Adidas increased by 0.7 percentage points to 50.7%,
- Its Royalty and commission income increased 41%, and other operating expenses of Adidas decreased 4.7% points
- Its operating margin increased by 5.3 % points to 9.4%.
- Its Net income from continuing operations increased hugely by 223%, and
- Net income attributable to shareholders increased by 390%.

Contd….

(Please refer the table below):

1. Net sales by segment in million pounds (€)[1]			
	2021	**2020**	**Change**
North America	5,105	4,519	13%
EMEA	7,760	6,308	23%
Latin America	1,446	1,035	40%
Asia-Pacific	2,180	2,083	5%
Greater China	4,597	4,342	6%
Other Businesses	145	149	(3%)
Total	**21,234**	**18,435**	**15%**
2. Net sales by product category in million pounds (€)			
	2021	**2020**	**Change**
Apparel	8,710	7,315	19%
Footwear	11,336	10,129	12%
Accessories and Gear	1,187	991	20%
Total	**21,234**	**18,435**	**15%**
3. Gross Margin			
The gross margin of Adidas increased by 0.7 percentage points to 50.7% form 50.0% in 2020			
4. Royalty And Commission Income			
Adidas Commission income and Royalty increased 41%			
5. Other Operating Expenses As A Percentage of Sales			
As a percentage of sales, other operating expenses of Adidas decreased 4.7% points to 41.9% from 46.5% in 2020			
6. Operating Margin			
Operating margin increased by 5.3 % points to 9.4%			
7. Net Income From Continuing Operations			
Net income from continuing operations increased hugely by 223%			
8. Net Income Attributable To Shareholders			
Net income attributable to shareholders increased by 390%			

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Source: Adidas (2021). "INCOME STATEMENT", https://report.adidas-group.com/2021/en/group-management-report-financial-review/business-performance/income-statement.html (accessed on 16/9/22).

5.5 Balance Sheet

While the income statement provides the results (revenue and expenditure) of a store's business operations for a particular period, the balance sheet indicates the financial status of the store at a particular point in time (usually at the end of the year). The balance sheet consists of three components: assets, liabilities and owner's equity (net worth). It gives a snapshot of the firm's financial position. In short, it is the report card of a retailer with which he can generate funds or avail loans from investors and credit institutions. The balance sheet is based on a simple concept, i.e., in order to acquire assets, a firm (retailer) must pay for them with either debt (liabilities) or with the owners' capital (shareholders' equity). Thus, in a balance sheet, assets should balance with the liabilities and owner's equity:

Table 5.2: Balance Sheet of fictitious company ABC Ltd. (₹ in 2014)

ASSETS	Amount in lacs (₹)
Current Assets	
Cash	232
Marketable securities	147,566
Accounts receivable	3,523
Inventories	66,528
Others	5,270
Total Current Assets	**223,119**
Total Fixed Assets less Depreciation	129,039
Total Assets	**352,158**
LIABILITIES	Amount in lacs (₹)
Current Liabilities	
Accounts Payable	15,244
Accrued Expenses:	**Nil**
Payroll and Payroll related	2,771
Worker's Compensation	5,534
Due to Shareholders	1,655
Others	3,613
Total Current Liabilities	**28,817**
Long Term liabilities	**3,698**
Total Liabilities	**32,515**
Owner's Equity	
Common Stock	156,154
Retained Earnings	163,489
Total Owner's Equity	**319,643**
Total Liabilities and Owner's Equity	**352,158**

Source: ICFAI Research Centre

Assets = Liabilities + Owner's equity

Assets are the items owned by the firm (retailer) that have an economic value and they are expected to produce some economic benefit to the firm. Assets include land and buildings, equipment, inventory, cash, patents, and accounts receivables. Liabilities are the obligations that the firm owes to outside parties. Liabilities include bank loans, debts to suppliers, and debts to employees. Owner's equity is the difference between the assets and liabilities. It generally includes the amount of capital the owners invested plus the profits that have been reinvested in the firm.

Let us examine the elements that constitute the assets, liabilities, and owner's equity. Please refer Table 5.2.

5.5.1 Assets

Assets represent everything owned by the firm that has value and the resources available to the firm that can be used for generating revenue. Assets can be divided into two types based on their level of liquidity. Current assets refer to those assets, which can be converted into cash within a short period; fixed assets are those assets, which cannot be converted into cash within a short period. For retailers, current assets determine the survival of the firm. In retail business, current assets form a major portion of the total assets, while fixed assets like buildings and fixtures constitute a minor portion of the total assets.

Current Assets

In retailing, current assets are calculated as follows:

Current assets = Accounts receivables + Merchandise inventory + Cash + Other Current Assets

Accounts Receivables

Accounts receivables refer to the amount that is due from customers. Receivables arise because the company sells goods to customers on credit (apart from cash sales). If a company insists on cash sales only, it may lose customers to competitors who offer credit sales. Thus, from the marketing and customer service point of view, it is important to provide credit sales. However, having a large amount of accounts receivables is also not advisable since the proceeds of the sales are blocked in these receivables and this affects the retailer’s ability to invest in other productive activities.

Some retailers, e.g. Sears and J. C. Penney, offer credit to their customers through their own credit card system. These stores charge the customer lower interest rates for providing credit. Such a credit card system has its advantages: It ensures the loyalty of the customers towards the stores and earns interest income for the retailer (the retailer charges interest for giving credit).

If not managed properly the receivables can strain the financial position of the retailer. Cash, which is a scarce resource, is being locked up in the receivables, thus decreasing investment opportunities. Moreover, there is a high risk of receivables becoming bad or irrecoverable. Stores should take preventive measures to reduce the financial burden arising due to receivables. One such measure is factoring. Factoring, also known as "cash for receivables," is the conversion of accounts receivables into immediate cash by the outright purchase of its receivables at a discount by financial services companies called factors. Factoring enables retailers to receive cash for the value of accounts receivables within a short period. The factor will assume the responsibility of recovery of the receivables. Therefore, not only will retailers be relieved of the collection of the receivables, they will also not have to deal with the risk of the receivables becoming bad. Another option for dealing with the receivables is to accept third party credit cards like Visa card and Master card. By accepting such cards, retailers are completely relieved of the process of offering credit from their own resources. In India, the system of third party credit cards is more prevalent than "own card system". Retailer should also encourage cash sales through discounts on cash purchases.

Merchandise Inventory

This is the most important asset from a retailer's point of view. It constitutes the major part of the total assets of any retailer. For ABC Ltd., it constitutes nearly 20% of its total assets.

$$\text{Inventory to Assets ratio} = \frac{\text{Inventory}}{\text{Total Assets}}$$

$$\text{For ABC Ltd., Inventory to Assets ratio} = \frac{66{,}528}{352{,}158} \text{ X100} = 18.8\%$$

Inventory Turnover

Inventory turnover refers to the ratio of net sales to average inventory.

$$\text{Inventory Turnover} = \frac{\text{Net sales}}{\text{Average Inventory}}$$

$$\text{[Where Average Inventory} = \frac{\text{Inventory}}{\text{(1-Gross Margin)}}$$

For ABC Ltd. Average Inventory = 66,528 ÷ 0.61 = 109,062]

$$\text{For ABC Ltd., Inventory Turnover} = \frac{578{,}269}{109{,}062} = 5.3 \longrightarrow \textit{eqn 5.2}$$

The inventory turnover indicates the speed at which the inventory is moving out of the stores. It is used to evaluate the efficiency of an organization in managing its investment in inventory. The inventory cycle usually consists of ordering of inventory, stacking in the store, and selling to customers. The inventory turnover refers to the number of times (on an average) inventory sold in a year. If the inventory turnover is six, it indicates that, on an average, the retailer turns over or sells his inventory every two months. For ABC Ltd., the inventory turnover is 5.3, implying that inventory is sold every two and half months (approx.). Discount stores and wholesale clubs have a higher inventory turnover than department stores. This is because wholesale clubs stock the most common commodities (like groceries) at competitive prices. Such commodities sell quickly and lead to high inventory turnover. In addition, the product mix is limited in wholesale clubs, thus leading to lower inventory. Department stores carry all types of goods, including specialty goods, which slow down inventory turnover. To cater to a wide range of customers, department stores have a wide product mix, which makes it difficult for the retailer to have proper inventory control.

Cash and Other Current Assets

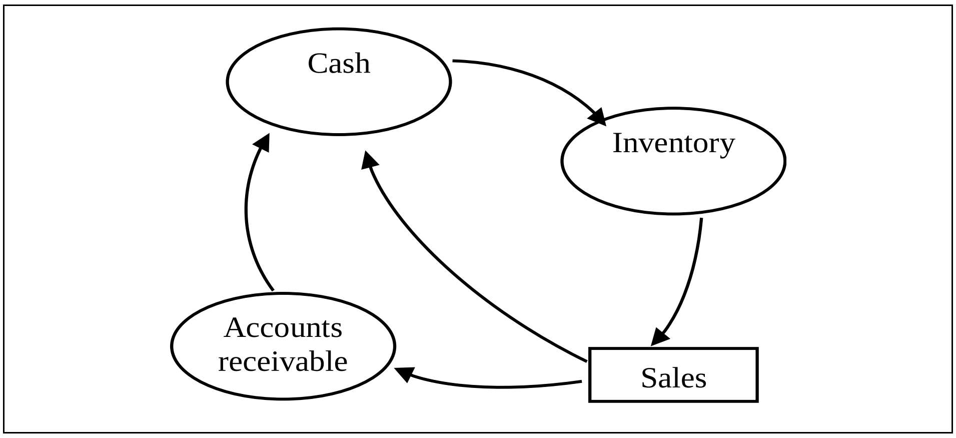
Cash includes money in hand, marketable securities like treasury bills, and money in bank accounts to which the retailer has ready access.

Other Current Assets consist of prepaid expenses and other miscellaneous assets. Prepaid expenses refer to expenses paid in cash and recorded as assets before they are used or consumed, e.g., insurance. The insurance premium is paid prior to the receipt of the benefit. Prepaid rent is also an example of a prepaid expense.

Operating Cycle

Cash invested in retail businesses takes various current asset forms (inventory, accounts receivables) before it is converted into liquid cash (which includes profits). This cycle of cash-inventory-sales-accounts receivables-cash is known as the operating cycle or the current asset cycle. Figure 5.2 depicts the relationship between various current assets in an operating cycle. Retailing businesses aim at making profits by selling goods and services. In this process, retailers invest cash for procuring various goods, which would be later sold to customers for cash or on credit. Cash received from the sales along with the cash that was collected from accounts receivables will be used to purchase the inventory. The profitability of the retailer depends on the productivity of various current assets (i.e. inventory, accounts receivables, and cash) and the number of times cash is rotated in the operating cycle. Inventory is a key asset for retailers. The inventory should be maintained at an optimal level to minimize the possibility of excess inventory or no stock. While accounts receivables are necessary for retailers from the marketing and customer service point of view, steps should be taken to minimize the risk of receivables becoming bad through factoring, use of third party credit cards, etc.

Figure 5.2: Relationship between Current Assets in an Operating Cycle



Source: ICFAI Research Center

Fixed Assets

Fixed assets represent those assets, which require more than one year to be converted into cash. They include buildings, furniture and fixtures, equipment, land etc. Fixed assets will have a limited useful life. Over the years, the values of these assets depreciate or reduce. This reduction is factored as depreciation while assessing the value of fixed assets.

When assessing the value of a fixed asset, its cost is spread over the useful life of the asset. The value of the fixed asset is arrived at by subtracting the depreciation from the cost of the asset. [Buildings will have useful life of 25 years whereas fixtures and equipment will have a useful life between 2-5 years.]

Asset Turnover

Asset turnover refers to the ratio of net sales to total assets.

$$\text{Asset Turnover} = \frac{\text{Net sales}}{\text{Total Assets}}$$

$$\text{For ABC Ltd. Asset turnover} = \frac{578{,}269}{352{,}158} = 1.64 \longrightarrow \quad \textit{eqn 5.3}$$

This ratio measures how effectively managers use their assets. If the asset turnover is high, the retailer is using assets efficiently. Though retailers attach more importance to current assets than fixed assets, they should not overlook the role of investment in fixed assets. When deciding to invest in any fixed assets, they should evaluate how much sales can be generated from the proposed investment. For example, if a retailer wants to set up new fixtures in a store, he must examine how much increase in sales can be achieved through the proposed investment.

5.5.2 Liabilities and Owner's Equity

Liabilities refer to items that a company owes to creditors and suppliers. On the balance sheet, liabilities are generally broken down into current liabilities and long-term liabilities. Owner’s equity, however, includes the amount of capital the owners invested plus any profits that the retail firm reinvested in the firm. Let us now examine each component of liabilities and owner's equity.

Current Liabilities

Current liabilities refer to debts that need to be paid within one year. Non-payment of these liabilities may lead to insolvency of the retailer. Some of the common current liabilities of a retailer are accounts payables, notes payable and accrued expenses.

Accounts Payables

The amount owed to vendors or suppliers of merchandise is referred to as accounts payables. Vendors offer goods to retailers on a credit basis. Retailers take advantage of such offers to control costs. Vendors give credit for a period, depending on their relationship with the retailer, the financial status of the firm, the value of the consignment, and the credit history of the retailer. By using bargaining skills and developing an understanding of the market, a retailer can get goods at best terms. Since credit is generally interest free for the period the credit is given, it is cheaper than the short-term loans that are provided by financial institutions. If utilized properly, the retailer can save a substantial amount in the form of interest savings. Thus, accounts payable is one of the important forms of short-term financing.

Notes Payable

The current liabilities, which a company owes to financial institutions, are referred to as notes payable. It includes the principal and interest payable to lenders like banks within one year.

Accrued Expenses

Accrued expenses occur when expenses are recognized before cash is paid. Accrual accounting requires expenses incurred during a period to be recorded in that period even if the cash is paid later. Assume that a company advertised during December 2021 but has not received a bill or paid for the advertisement, which cost ₹ 50,000. The advertising costs incurred during the year 2021 must be recorded as an expense for that year, even if the payment is made in a later period. Hence, an advertising expense of ₹ 50,000 is accrued on December 31, 2021. Since a payment of ₹ 50,000 must be made in the future, a liability is recognized for this amount.

Long Term Liabilities

Long-term liabilities refer to obligations that will be paid after one year. They include bonds, mortgages on real estates, and long-term loans.

Owner's Equity

Owner's equity represents the share of the owner's investment in the business. In accounting framework it is given by

Owner's equity = Total Assets – Total Liabilities

Two common elements of owner's equity are

- Common Stock
- Retained Earnings

Common Stock

This type of stock is issued by most corporations. Owners of common stock have certain benefits and rights. They have the right to vote to elect the members of the board of directors and they are entitled to a share in the profits of the company in the form of dividends.

5.5.3 Retained Earnings

Retained earnings are a part of profits that are not paid as dividends to shareholders but are retained to reinvest in the business. The percentage of earnings that should be retained and the percentage that should be distributed to shareholders depend on the growth potential of the company. If the firm has opportunities for growth, a major portion of the earnings should be reinvested to earn high returns for the shareholders. If opportunities are few or nil, it is prudent to distribute the earnings as dividends among the shareholders.

Financial Leverage

One of the important ratios, which determine the extent of share of owner's investment in assets, is financial leverage.

$$\text{Financial Leverage} = \frac{\text{Total Assets}}{\text{Owner's Equity}}$$

$$\text{For ABC Ltd. Financial Leverage} = \frac{352{,}158}{319{,}643} = 1.10 \longrightarrow \quad \textit{eqn 5.4}$$

This ratio measures the extent to which a retailer is using outside finances (debt) in its capital. It indicates the total asset value in relation to the value of owner's equity. The leverage ratio of ABC Ltd. is 1.10. This indicates that for every ₹ 1.10 in total assets, the owners put up ₹ 1.00 and outsiders put up the remaining ₹ 0.10. That means the greater the ratio, the higher the level of outside financing.

Too much debt may result in the insolvency of a firm as liabilities may exceed the paying ability of the firm. A low financial leverage ratio indicates the inefficient use of alternative sources of financing by the firm.

Asset turnover and financial leverage are two performance ratios that are derived from the balance sheet of a firm. These ratios form a part of the SPM framework.

Example: Balance Sheet of Future Retail Ltd. @2021

The Balance sheet of Future Retail Ltd. for 2021 shows the total assets to be at INR 12028.72 crores which also equals to the sum of liabilities and owners' equity at INR 12028.72 crores. The three components' assets, liabilities and owner's equity can be analyzed for Future retail Ltd. for the year 2021 as given in the table 5.2.

(Replace table 5.2 in SLM with this table)

Table 5.2: Balance Sheet of Future Retail Ltd. for 2021 ₹ (in Crores)

Particulars	Mar'21
Liabilities	12 Months
Reserves & Surplus	1060.77
Share Capital	138.38
Net Worth	1199.15
Unsecured Loan	.00
Secured Loan	10829.57
TOTAL LIABILITIES	12028.72
Gross Block	7566.75
(-) Acc. Depreciation	725.22
Net Block	6841.53
Capital Work in Progress	73.94
Inventories	3995.89
Investments	114.42
Cash and Bank	68.68
Sundry Debtors	405.12
Loans and Advances	7385.73
Total Current Assets	11855.42
Current Liabilities	6777.64
Provisions	78.95
Total Current Liabilities	6856.59
NET CURRENT ASSETS	4998.83
Misc. Expenses	.00
TOTAL ASSETS	12028.72

Source: Economic Tines (March, 2021), "Future Retail L Balance Sheet", https://economictimes.indiatimes.com/future-retail-ltd/balancesheet/companyid-45395.cms (accessed on 16/9/22).

Check Your Progress - 1

1. Which of the following are the performance ratios required to calculate the return on net worth?
   a. Net profit margin
   b. Asset turn over and returns on asset
   c. Return on investments
   d. Financial leverage
   e. Net profit margin, Asset turn over and returns on asset & Financial leverage
2. Which of the following formula is represented correctly?
   a. Net Profit Margin = Net Profit / Total Investment
   b. Asset Turnover = Net Sales / Total Assets
   c. Return on Assets (ROA) = Net Profit / Total Sales
   d. Net Profit Margin = Net Sales/Total Assets
   e. Inventory turn-over = Net sales/ Total inventory
3. Which among the following is derived by summating Accounts Receivables + Merchandise Inventory + Cash?
   a. Liquid assets
   b. Currents assets
   c. Firms reserves
   d. Total assets
   e. Fixed assets
4. Which of the following term indicates accounts payables, notes payable, and accrued expenses?
   a. Debt
   b. Long term liability
   c. Current liability
   d. Expenses
   e. Accrued expenses
5. Which term is popular as ‘bottom line’ in business circles?
   a. Net profit
   b. Net loss
   c. Net expenses
   d. Assets
   e. Liabilities

5.6 The Strategic Profit Model

In the previous sections, we examined the income statement and the balance sheet. We also studied the important performance ratios derived from these statements. As some of these ratios are interrelated, examining them in isolation can be confusing. Moreover, it is difficult to compare the performance of a retailer with that of other retailers using individual ratios because different firms employ different strategies and consequently have different operating characteristics. The strategic profit model combines the different performance ratios- net profit margin, asset turnover, and financial leverage to give a single comprehensive framework for easy and accurate comparison. In other words, it provides a visual format of assessing a firm's profitability. The strategic profit model gives two important returns on investment measures, return on assets and return on net worth.

Return on Assets = Profit Margin x Asset Turnover

Return on Net Worth = Return on Assets × Financial Leverage

5.6.1 Return on Assets

Return on assets is the combination of profit management and asset management. It is given by

Return on Assets (ROA) = Net Profit Margin x Asset Turnover

$$= \frac{\text{Net Profit}}{\text{Net Sales}} \times \frac{\text{Net Sales}}{\text{Total Assets}} = \frac{\text{Net Profit}}{\text{Total Assets}}$$

By

Using the results of eqn 5.1 and 5.3 in the above equation, we get

$$\text{ROA} = 8.38 \times 1.64 = 13.7\% \rightarrow \qquad \textit{eqn 5.5}$$

The ROA is 13.7% for ABC Ltd. In other words, for every rupee invested in assets ₹ 0.13 returns are generated. This ratio is important for measuring the economic viability of a firm. It determines how much profit can be generated from the retailer's investment in assets. When investing in assets, a retail firm should evaluate whether the returns exceed the investment and give far greater returns to satisfy the firm's objectives.

Example: Return on Assets @ Avenue Supermarts

Consider the Avenue Supermarts Limited data given above and Return on Assets can be calculated as given below method.

Contd....

a) Net Profit Margin = Net Profit / Net Sales = 1165.3/7303.13= 0.1595

Asset Turnover = Net Sales / Total Assets = 7303.13/ 13,655.97 = 0.5347

Return on Assets (ROA) = (Net Profit Margin x Asset Turnover) x 100

= (0.1595 X 0.5347) x 100

= 0.0853X 100 = 8.53%

OR

(Net profit/ Total Assets) x100 = (1165.3/13,655.97) x 100

= 0.08533x 100

= 8.53%

Sources: Avenue Supermarts Ltd. Annual Report (20-21),
i) https://www.moneycontrol.com/financials/avenuesupermarts/consolidated-balance-sheetVI/AS19#AS19 &

ii) https://economictimes.indiatimes.com/avenue-supermarts-ltd/balancesheet/companyid-45987.cms (accessed on 16/9/22).

5.6.2 Return on Networth

The owners of a business are more concerned about this ratio.

Return on Net Worth = Return on Assets x Financial Leverage

or

Return on Net Worth = Profit Margin × Asset Turnover × Financial Leverage

$$= \frac{\text{Net Profit}}{\text{Net Sales}} \times \frac{\text{Net Sales}}{\text{Total Assets}} \times \frac{\text{Total Assets}}{\text{Net Worth}} = \frac{\text{Net Profit}}{\text{Net Worth}}$$

RONW is a combination of three ratios, profit margin, asset turnover and financial leverage

From eqns 5.4 and 5.5 the calculation for ABC Ltd. is

RONW = 13.7 x 1.10 = 15.07%.

By measuring the return on net worth, a retailer can decide whether a strategy is worth pursuing. ABC Ltd.'s RONW is 15.07%. If ABC Ltd. plans to open a new music store chain and the projected return on net worth is less than what the company currently earns (15.07%), the company should consider alternative investment options. Return on net worth is the combination of three ratios, profit margin, asset turnover, and financial leverage. Improving each of these ratios can have positive effect on the return on net worth.

5.6.3 Improving Financial Performance

Now let us look at how the strategic profit model can be used as tool for assessing the performance of a retailer and how the model can be used to improve the financial performance. Generally, there are three paths to improve financial performance

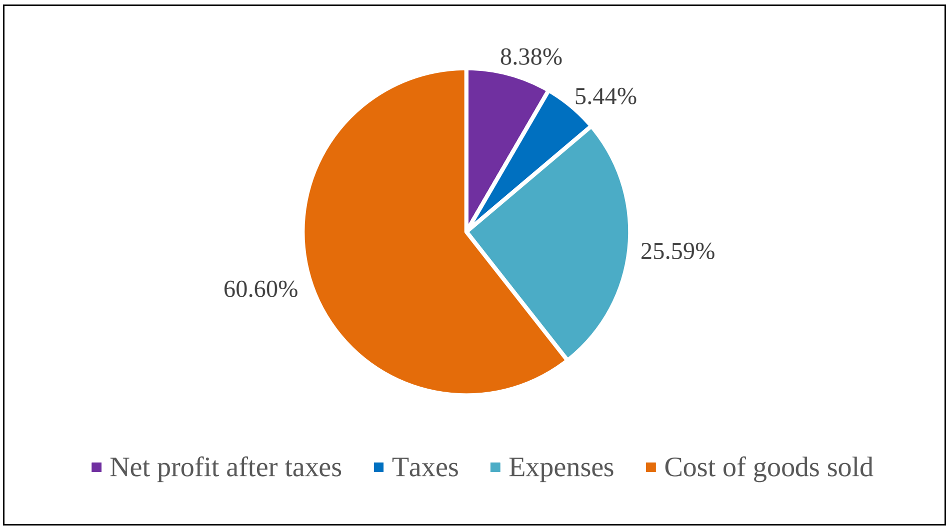
- Profit Management.
- Asset Management
- Debt Management

Let us examine each of these methods in detail.

Profit Management

Profit management is one of the most important components of the strategic profit model. The net profit margin is used to evaluate how well a company is controlling its costs in relation to its generation of revenues. Profit management is an essential task for all retailers. The focus of profit management is sales productivity and expense control.

Figure 5.3: Profit Margin of the Fictitious Company ABC Limited



Source: ICFAI Research Center

Figure 5.3 provides an overview of the components that affect the profits of ABC Ltd. The pie represents the total sales revenue of ABC Ltd. The net profit is the slice of the pie that remains after slicing out parts of the pie for the cost of goods sold and the total expenses of ABC Ltd. Hence, the net profit margin depends on the cost of goods and the operating expenses. In the figure, the net profit margin is 8.38%. This indicates that, on an average for every rupee of sales, ₹ 0.083 net profit is earned.

The chart shows the components of profit management. Any changes in the values of net sales, cost of goods sold, and expenses can bring about change in the net profit margin. The profit margin can be increased by increasing sales, and keeping expenses constant; or bringing down expenses, without changing the level of sales or; by increasing sales as well as bringing down expenses.

Let us examine how management can increase sales. Management can bring about an increase in sales by increasing the prices of goods. But, increase in prices may hurt the sales volume. Only the prices of selected merchandise should be increased so that there is no decrease in sales volumes. The prices of items (luxury goods) for which the demand is not very price sensitive should be increased. Although an increase in sales is a good measure of marketing success, a retailer can gain from the increase only if sales outpace expenses. This can be done by increasing sales without incurring a corresponding increase in expenses. However, in reality, an increase in sales is always associated with an increase in expenses.

Table 5.3: Impact of Sales on Profit Margin (fictitious company ABC Ltd.)
Amount in ₹

	Present Scenario	**4% Increase in Sales without Corresponding Rise in Expenses**	**4% Increase in Sales with Corresponding 2% Rise in Expenses**
Net Sales	578,269	**601,399**	**601,399**
Less: Cost of Goods Of Sold	350,421	350,421	350,421
Gross Margin	227,848	250,978	250,978
Less: Operating Expenses	141,544	141,544	**144,374**
Less: Interest Expenses	6,423	6,423	6,423
Less: Total Expenses	147,967	147,967	150,797
Net Profit Before Taxes	79,881	103,011	100,180
Less: Taxes	31,438	40,586	39,471
Profit After Taxes	48,443	62,425	60,709
Net Profit Margin	8.38%	10.38%	10.09%

Source: ICFAI Research Center

In the Table 5.3, we see the impact of a change in sales on profits.

From the third column of Table 5.3, we can see that a 4% increase in sales without a corresponding change in expenses brings about an extraordinary increase in profits from 8.38% to 10.38%. Data in the fourth column shows that even if there is a corresponding 2% increase in expenses there is a comparable increase in profits because the increase in sales outpaces the increase in expenses.

Profit can also be increased through cost control. Cost of goods sold includes the cost of merchandise, transportation costs and other costs that are directly related to producing or acquiring merchandise that is for sale.

The reduction of cost of goods sold depends on the management's buying skills and the ability to reduce transportation costs. Management can negotiate with vendors for favorable terms like volume discounts and product discounts. Product discounts, volume discounts are deducted from the cost of goods sold. Big retailers like Walmart can negotiate with vendors for favorable terms. Costs can also be reduced considerably by managing transportation effectively. The management can cut transportation costs by studying cheaper alternate shipping means. It can consider closer suppliers for easy and cheaper transportation.

Table 5.4 shows the impact of a 2% reduction in costs on the profit margin, other factors remaining constant. Here, a 2% reduction in the cost of goods sold contributes to a 0.73% (9.11-8.38) increase in the net profit margin. Thus, through tighter cost control, retailers can increase their profit margins.

An increase in profits can also be generated through a reduction in operating expenses. Such expenses should be brought down without tinkering with the image and overall profitability of the concerned firm. Under certain circumstances measures like lowering of wages and salaries, laying off employees, and eliminating free home delivery services may harm the image and hence the profitability of the firm. Lowering of wages and salaries, and laying-off quality employees may de-motivate employees. De-motivated and dissatisfied employees may have a negative impact on sales as well as customer relations. And if the company stops providing value added services like free home delivery, then it may not live up to customer expectations. Thus, those services and expenses that have a direct impact on the customers need to be maintained, and in some areas, retailers can decrease costs by exploring alternatives to improve efficiency. For example, lighting expenses can be reduced by installing the latest energy saving lighting systems without compromising on the ambiance of the stores.

Table 5.4: Impact of Reduction of Cost of Goods Sold on Profit Margin (fictitious company ABC Ltd.) Amount in ₹

	Present Scenario	**Reduction of 2% in Costs of Goods Sold**
Net Sales	578,269	578,269
Less: Cost of Goods Of Sold	350,421	**343,412**
Gross Margin	227,848	234,856
Less: Operating Expenses	141,544	141,544
Less: Interest Expenses	6,423	6,423
Less: Total Expenses	147,967	147,967
Net Profit Before Taxes	79,881	86,889
Less: Taxes	31,438	34,234
Profit After Taxes	48,443	52,654
Net Profit Margin	8.38%	9.11%

Source: ICFAI Research Center

The Table 5.5 shows the impact of a reduction in expenses on the profit margin. A 3% reduction in expenses results in a 0.44% increase in the profit margin.

Table 5.5: Impact of Reduction in Expenses on the Profit Margins of a fictitious company ABC Ltd. Amount in ₹

	Present Scenario	3% Decrease in Expenses	3% Reduction in Expenses Coupled with 4% Increase in Sales
Net Sales	578,269	578,269	**601,399**
Less: Cost of Goods Sold	350,421	350,421	364,437
Gross Margin	227,848	227,848	236,961
Less: Operating Expenses	141,544	**137,297**	**137,297**
Less: Interest Expenses	6,423	6,423	6,423
Less: Total Expenses	147,967	143,720	143,720
Net Profit Before Taxes	79,881	84,127	93,241
Less: Taxes	31,438	33,146	36,737
Profit After Taxes	48,443	50,981	56,504
Net Profit Margin	8.38%	8.82%	9.4%

Source: ICFAI Research Center

If there is an increase in sales as well as a decrease in expenses, a considerable increase in profits occurs. The fourth column in Table 5.5 shows this change.

Profit management is thus an important tool for improving the profitability of a retailing firm.

Asset Management

A retailer can improve financial performance through effective utilization of assets. Asset management is a key component of the strategic profit model. A common measure for assessing the asset management is the asset turnover ratio. It indicates the sales generated in relation to the amount invested in assets.

From eqn. 5.3, we know that the asset turnover of ABC Ltd. is 1.64. This indicates that for every rupee invested in assets, ₹ 1.64 worth of sales are generated. The key to asset management is to utilize resources optimally in order to generate sales volumes and profits. The asset turnover ratio of a firm cannot be compared meaningfully with that of other firms in the industry because retail firms adopt different strategies for asset management. For example, discount stores and warehouse clubs have higher asset turnover ratio than department stores and specialty stores.

Cross industry comparisons of financial performance require that asset productivity be measured in terms of profits. This can be achieved through the return on assets (ROA) ratio. The ROA combines two ratios, net profit margin and asset turnover. Therefore, it combines two components of the strategic profit model to give a common measure for an easy and comprehensive analysis of the financial performance of a retailer. We have already discussed ways to improve profit margin performance, which would also improve return on assets. So let us focus on how we can improve upon the asset turnover to increase the return on assets. One way to improve the asset turnover is to increase the sales without making a corresponding increase in investments in assets. Another way is to reduce assets while keeping sales constant. The current assets constitute major part of assets for any retailer. Effective control of current assets can reduce the assets base without causing a decline in sales. Cash, inventories and accounts receivables are the key current assets. Of these, inventory represents a sizable investment for a retailer. Therefore, inventory control is a major step in asset management. Inventory control not only affects asset productivity, but also sales productivity and the financial stability of the retail entity.

From eqn. 5.2 for ABC Ltd., inventory turnover is 5.3. This indicates that the inventory is moving out of the store every 2 ½ months (approx.). Excessive inventory can tie up too much cash, thus affecting the financial stability of the firm. If the level of inventory is very low, then no stock or stock out situations can occur which will affect the profit of the firm through lost sales opportunities. Therefore, the firm must strive to achieve an optimal level inventory.

To achieve better inventory performance, retailer must

- Buy in proper quantities.
- Tie up with fewer suppliers for easier management.
- Invest in inventory control systems, which can give accurate information, resulting in better monitoring of inventory.
- Remove slow moving items from the product mix to reduce inventory-carrying costs.

Cash is an important component of current assets. Firm must have optimal cash in hand to meet emergency and short-term needs. Too much cash in hand can make firms forego opportunities for investment in merchandise, hampering their growth prospects.

Accounts receivables must be regularly reviewed to ensure that they are not going bad. While providing, credit is important from point of view of customer satisfaction, retailers must ensure that it does not have a negative effect on their asset position.

Debt Management

Return on assets is a good measure of how effectively retailer is using the firm's resources. A more effective measure of performance is return on net worth or owners' equity. The leverage ratio is the link between return on assets and return on net worth. It explains the owner's contribution in the firm's investment. In other words, financial leverage ratio reflects the extent to which a firm has financed its assets with debt. It is computed as follows:

$$\text{Leverage ratio} = \frac{\text{Total Assets}}{\text{Net worth}}$$

The leverage ratio for ABC Ltd. is 1.10. Thus, we can infer that for every ₹ 1.10 worth investment in assets, owner's contribution is ₹ 1 and debt is ₹ 0.10. Increase in debt increases the return on net worth of the retailer. The reason is owners need to invest less funds from their resources and can utilize more outside funds and thus owners can get more returns with less investment. Before deciding on financial leverage, the retailer should examine some aspects. He should evaluate the financial position of the firm and determine whether the debt option will increase the RONW. If yes, the retailer must determine the level of debt the firm can afford. High debt may burden the balance sheet and increase the risk of financial instability.

Another aspect is the interest rate scenario. If the interest rates charged by lenders are higher than the return to the owners, additional debt will reduce the return on net worth. Under such circumstances outside financing is not a viable option. There are three types of financing: short-term financing, intermediate, and long-term. Short-term financing refers to funds that retailers can borrow for less than one year. The retailer uses short-term loans for purchasing merchandise for the next festival season or repaying dues to suppliers etc. Intermediate loans are usually offered for a period of more than one year but less than five years. These funds are used for refurbishing stores, buying new equipment and fixtures, etc. Retailers generally secure long-term loans for periods longer than five years. These loans are used by retailers to buy fixed assets like buildings and land.

Of late, attracting FDIs (Foreign Direct Investments) is one of the ways of attracting funds for retail operation.

Activity 5.1 The Strategic Profit Model uses return on assets as the basis for assessing a firm’s profit margins. Using Strategic Profit Model compare a wholesale Club and a Departmental store to explain which path both the retail formats would adopt to increase profit margins.

5.7 Setting Performance Objectives

Setting performance objectives is the first and most important part of any strategy planning process. A clear set of objectives will help the organization focus on the changes that need to be made to achieve those objectives. Some guidelines for setting objectives are given below:

- Objectives should be clear and specific
- Objectives should be measurable
- Objectives should be realistic and attainable
- Objectives should be time bound

For example, financial objectives can be:

- "To achieve sales growth of 35% for the year ending 2023"
- "To generate profit of 20% on the investment of ₹ 50 crores for the year 2023-2024"

Setting objectives for a retail firm requires a combination of top-down and bottom-up approaches to planning.

The top-down approach involves setting of overall goals by top management. These goals are then narrowed down to store levels.

In top-down planning, top managers set the overall strategy based on their analysis of changes in external environmental factors such as economy, competition and consumer trends. Based on the overall strategy the organizational objectives are set. Then these objectives are broken down into specific objectives at various merchandise category levels and store levels.

The objectives set for the merchandise category level determine the width of category, depth of the assortment, the product availability, the level of customer service, the floor area, and the location within the store. Once the broad objectives are set for a merchandise category, the merchandise manager makes decisions regarding each item of merchandise within a category. These objectives are further broken down to set goals for category managers and buyers.

The store level objectives are used to set the performance objectives of the regional store managers. The regional store managers in consultation with the store managers set performance goals for each individual store.

Thus, in the top-down approach, organizational objectives are broken down until performance goals are set for the department level.

The bottom- up approach complements the top-down approach. In the bottom-up planning approach, lower level managers propose the objectives. These estimates are passed onto higher level. They flow up to the top management. Based on these estimates the overall objectives are set by the top management.

But, frequently there are differences between the objectives that are set by top management and those set by lower level employees. To iron out such differences top management should negotiate with managers at the operational level and arrive at a solution that is acceptable to both parties.

How best a strategy may be, the organization will not get the desired results if the employees who have to implement those strategies are not motivated and are not accountable for their actions.

Accountability measures the progress and the results of the strategy that has been implemented. It involves the setting of guidelines, regular monitoring and periodic review of the progress. Monitoring and review enables retailers to compare the progress with the objectives and identify the reasons for the differences between the actual and proposed results.

Every manager at each level of the hierarchy should be made accountable for the objectives that are set for that level. Managers should not be made accountable for factors that are beyond their control. Suppose the profit target for a certain department is 20%. If top management decides to cut prices in response to competitive pressures, the profit margins may decrease. The concerned department may not achieve the profit target due to this change in policy. Thus, when assessing the performance of each operational level, top-management should consider all aspects that affect the performance to ensure a fair assessment of performance.

Example: Performance Objectives @ ITC

ITC is the one of the most valued Indian companies with focus on economy, society and environment. ITC's performance management system reflects MBO (Management By Objectives) to strengthen accountability and drive performance. ITC has clearly defined objectives with the result areas aligned to its Business Plans. Its assessments are based on outcomes that are measurable and serves as a strong base to drive and sustain high performance.

The objectives or goals of ITC based on Performance at the enterprise level are as given below:

- To Sustain the company’s position as one of India's most valuable corporations
- To achieve leadership in each of the business segments within a reasonable time frame

To achieve a Return on Capital Employed (ROCE) in excess of the Company's cost of capital, at all times

Source: ITC Sustainability Report 2022, https://www.itcportal.com/sustainability/sustainability-integrated-report-2022/ITC-Sustainability-Integrated-Report-2022.pdf (accessed on 21/9/22)

5.8 Performance Measures

A proper performance measurement system adopted by a firm is one of the ways of having track on the progress of business. Performance measures are used to measure the performance and evaluate the progress of strategic plans. Since numerous factors influence the performance of a firm, no single measure can give a complete picture of its performance. Multiple measures should therefore be used to assess the performance (Refer Table 5.6). The selection of measures depends on the level at which performance is measured and the resources that are controlled on that level.

Table 5.6: Examples of Performance Measures used by Retailers

Output	Input	Productivity
Net sales	Inventory level	Return on assets
Net profits	Cost of goods sold	Return on net worth
Gross margin	Expenses	Asset turnover
		Inventory turnover
		Gross margin return on investment
		Gross margin return on space
		Gross margin return on labor
		Average bill size
		Conversion ratio

Source: ICFAI Research Center

Types of Performance Measures

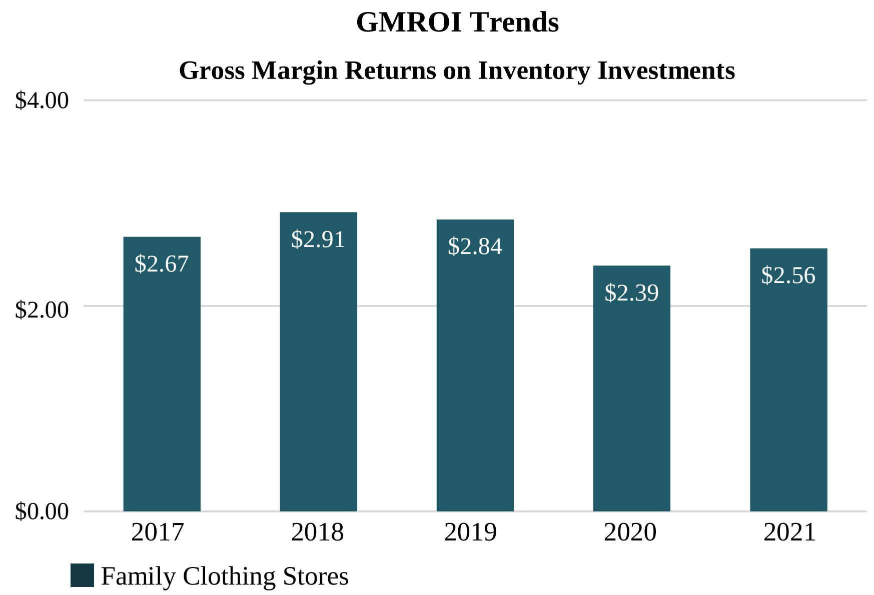
Retailers use a host of performance indicators to measure growth, efficiency, etc. The most common measures are input, output, and productivity measures.

Input measures identify the amount of resources needed to provide a product or service. For retailers, inventory, and cost of goods sold are examples for input measures. Output measures track the results of company activities. Sales and net profit are the key output measures used by retailers. Productivity measures assess the output achieved in relation to the inputs used. Return on assets and return on net worth are the key productivity measures that are used by retail businesses. Some productivity measures, like the average bill size, and gross margin ratios are unique to the retail industry.

Generally, to estimate the popularity of stores, managers count the number of people who visit the store. In retail jargon, the number of people who visit the stores are referred to as "footfalls". Footfalls are linked to sales to get the conversion ratio. The conversion rate is given by the number of sales receipts as a percentage of footfalls. Thus, the conversion ratio determines rate at which visitors turned into customers. If the ratio is 20%, it indicates that 20% of the total number of visitors purchased goods from the stores. The average bill size is arrived at by dividing total value of sales receipts by number of sales receipts. These ratios help retailers gauge their performance and develop plans for improving these measures to make the firm more productive.

Example: Performance Measures-GMROI of Family Clothing Stores of North America

Example: The Retail Owners Institute is a reputed institute for making the basics of retail financial management easy and readily available to retailers. The Retail owners institute conducts research in retail industry especially in North America. The following chart shows the GMROI of Family clothing stores for the last five years. The GMROI is ranging from a minimum of $ 2.67 (in 2017) reached to a maximum of $2. 91 (in 2018) then started decreasing from 2019 & 2020 where it reached the lowest of $2.39 and again started rising to $2.56 in 2021.



Source: Clothing Accessories Stores Retail Benchmarks, 2021, https://retailowner.com/Benchmarks/Apparel-Accessories-Stores/Clothing-Accessories-Stores# (accessed on 21/9/22).*

Activity 5.2

What makes the financial strategy of retail different from that of the other businesses? What specifications and factors impact financial strategy in retail business? Explain giving examples from the industry.

Check Your Progress - 2

1. Generally, there are three paths to improve financial performance. What are they?
   a. Profit management, asset management and equity management
   b. Profit management, current asset management and debt management
   c. Profit management, Asset management & Debt management
   d. Profit management, liability management and equity management
   e. Financial management, Liability management and debt management
2. Which of the following must be done by a retailer to achieve better inventory performance?
   a. Buy in proper quantities
   b. Tie up with fewer suppliers for easier management.
   c. Order adequate quantity to benefit the supplier
   d. Invest in inventory control systems and remove slow moving items from the product mix.
   e. Network the warehouse with stores in various locations and ensure replenishment of inventory as and when required.
3. A retailer can improve financial performance through effective utilization of assets. Asset management is a key component of the strategic profit model. A common measure for assessing the asset management is the asset turnover ratio. Which of the following indicates the above mentioned scenario?
   a. The sales generated in relation to the amount invested in clearing debt
   b. The sales generated in relation to the amount invested in assets.
   c. The sales accumulated in relation to the amount invested in assets.
   d. Increasing profits with minimum assets.
   e. Minimizing assets to the maximum extent possible to maximum returns.
4. For which of the following, the retailer should ensure that it is measurable, accessible, stable and economically viable?
   a. Segmenting
   b. Positioning
   c. Targeting
   d. Marketing
   e. Expanding

5. Return on net worth (RONW) is a combination of three ratios. What are they?
   a. Profits, assets and liability
   b. Profit, assets and financial liability
   c. Profit margin, asset margins and financial leverage
   d. Profit margin, asset turnover and financial leverage
   e. Profit margin, asset turnover and financial strength

5.9 Summary

- In this chapter, we understood the elements of a financial strategy. We examined two important financial documents: the income statement, and the balance sheet. We saw how they are important for retailers in evaluating financial performance.
- Later, we analyzed the strategic profit model and examined its components. The strategic profit model uses return on net worth as key performance measure for evaluating financial performance.
- Through an example, we saw how using the SPM could improve the financial performance of a retailer.
- We then discussed the way in which financial objectives are set. The setting of financial objectives requires a combination of top-down and bottom-up planning approaches.
- Finally, we looked at the various measures used by retailers for measuring performance.

5.10 Glossary

Asset Turnover: Asset turnover refers to the ratio of net sales to total assets.

Assets: Assets represent everything owned by the firm that has value and the resources available to the firm that can be used for generating revenue.

Balance Sheet: The balance sheet indicates the financial status of the store at a particular point in time (usually at the end of the year). The balance sheet consists of three components: assets, liabilities and owner's equity (net worth).

Fixed Assets: It represent those assets, which require more than one year to be converted into cash. They include buildings, furniture and fixtures, equipment, land etc.

Gross Margin Return on Investment (GMROI): GMROI measures the gross margin on each rupee invested in inventory.

Gross Margin Return on Space (GMROS): GMROS measure is used by store managers to determine the margins generated for each square foot area of space.

Income Statement: It is one of the important financial statements prepared by retailers. It summarizes the financial performance of a company for a given accounting period (usually one year).

Inventory Turnover: Inventory turnover refers to the ratio of net sales to average inventory.

Operating Cycle: Cash invested in retail businesses takes various current asset forms (inventory, accounts receivables) before it is converted into liquid cash (which includes profits). This cycle of cash-inventory-sales-accounts receivables-cash is known as the operating cycle or the current asset cycle.

Strategic Profit Model (SPM): It is a tool for planning and evaluating the financial performance of retailers.

5.11 Self-Assessment Test

1. What do you understand by strategic profit model? Explain its various components.
2. Define balance sheet: Explain its importance in planning financial strategy of the firm.
3. Explain the various paths to improving financial performance.
4. Explain the guidelines used for setting performance objective.
5. Explain the term GMROI, GMROL, GMROS.

5.12 Suggested Readings/Reference Material

1. Giri Arunangshu and Chatterjee Satakshi, "Retail Management: Text & Cases" Paperback, PHI Learning Pvt. Ltd., 2021.
2. Swapna Pradhan, "Retailing Management: Text and Cases", McGraw Hill, Sixth Edition, 2020.
3. Barry Berman, Joel R Evans, Patrali Chatterjee and Ritu Srivastava, "Retail Management", Thirteenth Edition Pearson Education, 2017.
4. Gibson G. Vedamani, "Retail Management", 5th edition, Pearson Education, 2017.

5.13 Answers to Check Your Progress Questions

1. **(e) Net profit margin, asset turnover and returns on assets and financial leverage**

   The performance ratios required to calculate the return on net worth are net profit margin, asset turnover, return on assets, and financial leverage

2. **(b) Asset Turnover = Net Sales / Total Assets**

   Net Profit Margin = Net Profit / Net Sales, Asset Turnover = Net Sales / Total Assets, Return on Assets (ROA) = Net Profit / Total Assets, Inventory turn-over = Net sales/ Average inventory. Hence, except for option c, all other options are incorrect.

3. (b) Current assets

Current assets = Accounts receivables + Merchandise inventory + cash + other current assets

4. (c) Current liability

Some of the common current liabilities of a retailer are accounts payables, notes payable and accrued expenses.

5. (a) Net profit

The term net profit is more popularly known as "bottom-line" in business circles. It is derived by subtracting the cost of goods sold and expenses from net sales.

6. (c) Profit management, Asset management & Debt management

Generally there are three paths to improve financial performance i.e., Profit Management, Asset Management, Debt Management.

7. (c) Order adequate quantity to benefit the supplier

To achieve better inventory performance, retailer must

Buy in proper quantities, tie up with fewer suppliers, invest in inventory control systems and remove slow moving items from the product mix and link and network warehouse with various branches.

Except for option c, all other options support higher inventory turnover and performance.

8. (b) The sales generated in relation to the amount invested in assets

This is the common measure for assessing the asset management in the asset turnover ratio.

9. (a) Segmenting

It is an important objective of a retailer.

10. (d) Profit margin, asset turnover and financial leverage

RONW is a combination of three ratios, profit margin, asset turnover and financial leverage.

Unit 6

Store Location and Site Evaluation

Structure

> "*You walk into a retail store, whatever it is, and if there's a sense of entertainment and excitement and electricity, you wanna be there.*"
>
> - Howard Schultz, an American businessman and author and chief executive officer of the Starbucks Coffee Company.

6.1 Introduction

Opening a new retail location is a significant investment for your organization. Make sure you are making the right decision by evaluating new locations with sound techniques.

Location is a top priority for all businesses. For the retailer, location means being at the right place at the right time. Whether it is the first store or the hundredth store, retailers must spend time and money on the process of store location and site evaluation. This is because location cannot be changed easily once a store has been established. Moreover, the choice of store location has a profound effect on the entire business life cycle of a retail operation. Location helps retailers gain a competitive advantage, as it is a unique asset. Once a site has been selected and occupied by a retailer, it cannot be used by any other retailer. Location is one of the few strategic advantages that competitors cannot imitate easily. To be precise, location and site selection comprise the most strategic and crucial decisions made by retailers.

In the last five years, organized retailers in India have had a lot to cheer about. The prices of real estate have come down significantly in many Indian metros, because of which supply of property is expected to go up. However, the complexity of selecting a location increases when there is a dearth of prime properties available at reasonable prices. Selecting a store location involves evaluating a series of trade-offs concerning the cost and value of the site for a specific retailing format. The selection of a store location depends on the type of retailer, the kind of store being set up, the type of merchandise that would be sold, the price at which it would be sold, the type of customers being targeted, the expectations of customers in terms of price, service, and convenience, and the financial strength of the retailer. The retailer's image and constraints will help limit the number of store locations being considered. Once the store concept has been determined, the retailer can shortlist and consider those locations that are in tune with the image of the store.

6.2 Objectives

After reading through this unit, you should be able to:

- State the importance of location decision that has an effect on the business life cycle of the retail operation
- Probe the factors that define Market Area Analysis that ensures generation of sales
- Inspect the trade areas that provides vital information of expanding the business units in an economical way
- Identify the techniques of analyzing the trade area to attract maximum customers
- Evaluate the potential Site Location of a retail business that gives easy accessibility that ultimately helps the busies to grow
- Debate on the various types of Site Locations to decide on the right one that would generate profits

6.3 Selecting the Store Location

Firms require visibility and exposure to their target markets. Store location decides these two parameters for a retailer. When selecting a location, the retailer must analyze regional and local markets to determine the area that seems to offer the highest market potential. Such an assessment is called market area analysis. Demographics, business climate, and the level of competition are considered during market area analysis. Then the retailer must examine specific areas within those market area, which is called trade areas. Trade areas refer to the areas from which most of the customers are drawn. The process of selecting trade areas is known as trade area analysis. Finally, the retailer must select the most suitable site within the preferred trade area, i.e., the one that satisfies the firm's objectives and meets customer needs. The process of choosing the best site is known as the site selection process. In this chapter, we will examine each of these steps in detail.

Example: Ye at Times Square Gap to Dress the World

In July, 2022, Kanye West, the Hollywood artist also known as Ye launched his brick-and-mortar retail store with Yeezy Gap products. The Times Square Gap store in New York City is selected for the purpose as it would be perhaps the most iconic and at the middle of a major commercial hub. The store is strategically located in city offering a nexus of tourism and transit, ideal for Ye's aspiration to dress the world.

Source: Tashjian, R. (July 20, 2022). Ye Brings His Vision for Gap to Times Square. Retrieved from https://www.harpersbazaar.com/fashion/designers/a40667837/kanye-west-gap-stores/. Accessed on 22-07-2022

6.4 Market Area Analysis

Many retailers like Shopper's Stop, Raymond's, Pantaloons, Titan, and Food World have successfully established stores at key locations in different states of India. The international fast food giant, McDonald's, has successfully identified suitable locations in many countries. The best regions are those that generate the highest demand or sales for a retailer.

A market area analysis consists of regional area analysis and local area analysis. The retailer must analyze regional differences across domestic or international markets. After selecting a particular region, the retailer has to analyze one or more local markets within that region. After identifying some promising market areas, the retailer should estimate their sales potential to choose the market area with the highest sales potential.

6.4.1 Factors affecting the attractiveness of Market Areas and Trade Areas

When analyzing market areas, a retailer must assess various environmental and market conditions, to identify the market area that matches the firm's objectives and strategy. Although market area analysis is distinct from trade area analysis, the factors that make market areas and trade areas attractive are the same. Let us examine some of the important factors for selecting the market area. (Table 6.1 lists the major factors that influence the selection of a market area or trade area.)

Table 6.1: Factors Affecting the Attractiveness of Market Areas and Trade Areas

Factors Affecting the Attractiveness of Market Areas and Trade Areas	
Demographics	• Total size and density • Age distribution • Average level of education • Percentage of population having own houses • Occupation distribution • Trends

Contd.....

Proximity to supply sources	• Cost of delivery • On time delivery • Number of manufacturers and wholesalers • Availability and reliability of product lines
Economic Base	• Dominant industries or companies • Employment rate • Total Income and per capita disposable income • Growth forecasts • Economic and seasonal fluctuations • Access to credit and financial facilities
Competition	• Number and size of the competitors present • Availability of transportation • Long term versus short term outlook • Saturation levels
Store Locations and its availability	• Number and type of locations • Availability of transportation • Own versus leased locations • Costs of occupancy and operation.
Regulations	• Licensing procedures • Operational procedures • Minimum wages prevalent • Zoning • Tax structures

Adapted from various sources by ICFAI Research Centre.

Demographics

Demography refers to the study of population characteristics. The various demographic variables that retailers have access to are consumer's age, gender, income, education, family background, and occupation. In India, different types of information on the population can be obtained from studies conducted by research organizations such as NCAER, ORG-MARG, IMRB, and A.C.Neilsen, etc. Demographic variables can be used to identify target markets for retailers. The analysis of demographic changes help retailers to track consumer trends. Demographics studies thus provide retailers with information that help them locate and define the required customer base.

Economic

All businesses operate in an economic environment and many of their decisions are based on economic factors. Retailers must examine the following factors in detail:

- Per capita income
- Interest rate
- Employment rate
- Business cycles

The higher the per capita income, the higher the spending power of the consumers and the lower the interest rates the easier it is to set up stores (due to the availability of cheaper funds, at low interest rates).

In India, the IT boom during the 1990's led to an increase in the population of the upper middle class and the upper class, especially in South India where many IT companies are based. This encouraged retailers to set up stores in cities like Bangalore and Hyderabad.

Cultural

Culture has a significant impact on the way consumers shop and the goods they purchase. Different people hold different values and lead different lifestyles. These differences affect their shopping preferences. Moreover, consumers like to be comfortable in the environment in which they buy goods. To provide a comfortable shopping environment to consumers, retailers should understand the culture and language of their customers. In a country like India where multiple languages are spoken, retailers should hire employees who are fluent in the regional language where the store is located. Since Indian culture is made up of several distinct subcultures, retailers should understand the various aspects of culture that would influence their locational decision.

Demand

The demand for a retailer's goods and services has a significant impact on the retailer's store location. Not only should customers be interested to buy the goods, they should also have the purchasing power. Demand is a function of the population and the purchasing power of the consumers living in a location, which the retailer is targeting. Population and income statistics can be obtained from the published sources of information like census data. These statistics help retailers compare populations and determine the one, which would be able to purchase the merchandise carried in their stores. The characteristics of demand determine whether a retailer should sell high-priced goods – like durables, furniture, jewelry and electronics or low-priced goods like apparel, toys, and groceries. During the early 1990's when the Indian economy was liberalized, many multinationals overestimated the demand and entered the Indian market with high expectations. Many of these firms later retreated from the Indian market because of poor sales.

Infrastructure

The nature of the infrastructure required, depends on the basic framework of the business. Different types of retailers require different types of channels to deliver goods and services to customers. The distribution of goods is highly dependent on existing infrastructure such as highways, roads, railways, and airways (depending on the transportation used). Legal infrastructure like laws, rules and regulations, and technical infrastructure like computerization, communication, and power distribution, also influence store location. The quantity and quality of infrastructure varies significantly across countries and regions. Retailers, whose operations depend heavily on computerization and telecommunications, should not consider those areas that do not meet their minimum specifications of these criteria.

Example: Tesla Shifting Focus On Cheaper Locations, Remote Managing of Test Drive Fleet, And Delivery Centers

In 2021, Tesla the car makers implemented a major change in its retail strategy. The company moved from showrooms in posh locations and fancy malls to cheaper locations. It hosted a fleet of remote test drive cars and delivery centres. The money saved from rent of those posh locations showrooms would be spent on delivery centres located at more affordable areas. Also delivery centres would be combined with service centres called "Tesla Centres".

Source: Lambert, F. (July 28, 2021). Tesla (TSLA) Launches Major Shift in Retail Strategy: Cheaper Locations, Remote Working, And More. Retrieved from https://electrek.co/2021/07/28/tesla-tsla-major-shift-retail-strategy-cheaper-locations-remote-working/. Accessed on 07-07-2022.

6.4.2 Estimating Sales Potential

After identifying some promising market areas, retailers should measure the sales potential of these areas. An accurate appraisal of sales potential is necessary to determine the amount of inventory to be procured, the number of employees needed, and the expenditure required. Retailers generally use population statistics to determine the sales potential. The factors that determine the sales potential of an area are area sales activities, and level of competition.

Area Sales Activities

The sales potential can be determined using sales activity index. The sales activity index (SAI) is a measure of an area's per capita retail sales in relation to the per capita sales for the entire country. It can be calculated as follows:

$$\text{SAI} = \frac{\text{Area's Percentage of India's Retail Sales}}{\text{Area's Percentage of India's Population}}$$

The SAI should be used with caution, as a high SAI coefficient does not always imply high sales potential. Factors like non-area resident buying, and corporate sales may inflate the SAI.

Level of Competition

Competition varies from nation to nation and region to region. In some areas, the competition is stiffer than in other areas. Generally, the level of competition increases with the level of industrialization of a country.

The level of competition in a region has an impact on the merchandise decisions of a retailer. A retailer should have a thorough knowledge of both its direct and indirect competitors in the market, the goods and services offered by them, and the consumer perception of these stores. Depending on the level of competition, market areas can be classified into saturated, under-stored or over-stored market areas. A saturated market area has optimum number of retail stores to meet customer demand. In these areas, customers are offered a good range of goods and services and retailers are able to make good profits. Since customers are attracted towards these areas because of the variety of merchandise offered, retailers who can offer a superior retail format to customers in terms of merchandise, prices or service choose these areas. An under-stored market area has very few stores, which offer goods, or services that satisfy the needs of the population. Any retailer establishing a store offering the right products in such an area would certainly have a first mover advantage. The initial success of Wal-Mart can be attributed to its strategy of opening stores in small towns that were comparatively under-stored. An over-stored market area has more retailers than are required to meet customer demand. As a result, some of the retailers are unable to make sufficient profits.

Some forms of competition increase the chances of success of retailers. For instance, if a store is located near an anchor store it will be able to draw the crowd that visits the anchor store. Such a location would not be an advantage if the people visiting the anchor store did not constitute the target segment of the store. Small retailers usually perform well when they are located near large stores, but only when they sell merchandise that complements the merchandise sold in the large store. Large stores, on their part need to carefully evaluate the number of competitors offering similar merchandise, or merchandise those customers who tend to compare before making a purchase decision. The degree of competition in a location is measured with the help of the index of retail saturation.

The index of retail saturation (IRS) measures the level of demand in a particular market on the basis of the population, consumer expenditure, competing retail space and a particular product or product area.

The index of retail saturation can be calculated as follows:

$$\text{IRS} = \frac{\text{POP} \times \text{EXP}}{\text{CRS}} = \frac{[\text{Demand}]}{[\text{Current Retail Selling Price}]}$$

IRS - Index of retail saturation in area for products

POP - Population in area that is likely to buy the products

EXP - Per capita retail expenditure in area on products

CRS - Current retail space (sq. ft.) in area selling products

IRS measures the level of demand in a market, that the retailer expects to break into or the demand that is, perhaps, already attained. The IRS provides an index of the attractiveness of the trade area for a specific product line or product category. The higher the index, the better the retailer's chances of success and a low index indicates that the area is saturated with similar competitors. In a saturated market area, the volume of retail equals the amount being consumed by the population. In an over-stored market area the volume of retail exceeds the volume required by the population, and in an under-stored market area, the volume of retail is insufficient for the potential customers. After selecting a suitable market area, the retailer must identify a specific trade area.

Activity 6.1

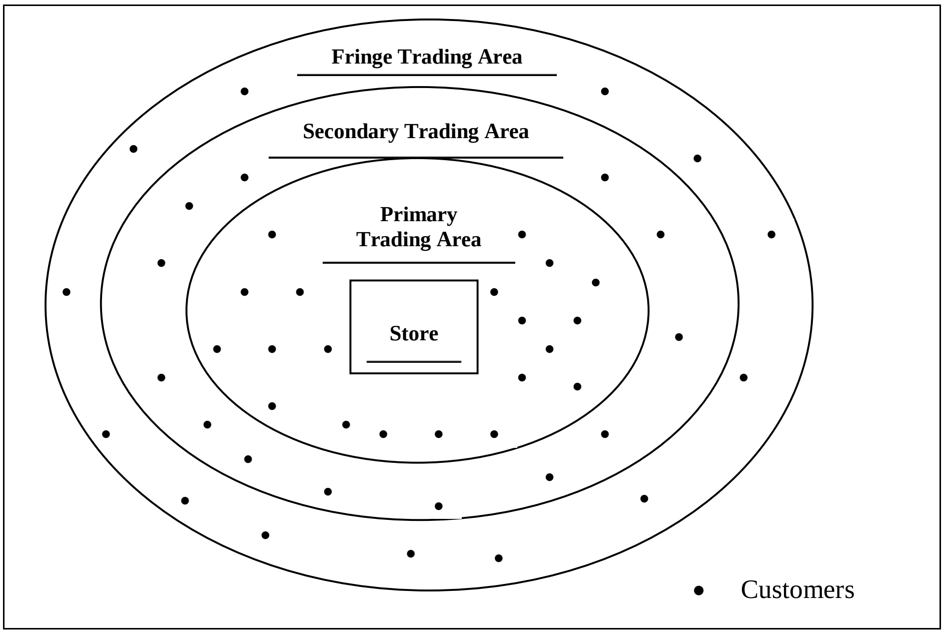
You may have noticed that many stores prefer a location in a shopping center or a shopping mall as against setting up a free-standing store wherein the retail brand exclusively occupies the building. Giving a suitable example, list out the advantages of locating a store in a shopping center as against setting up a free-standing store.

6.5 Trade Area Analysis

Trade area analysis provides retailers with vital information such as store patronage, local market opportunities, competing businesses, and barriers that would dissuade consumers from visiting the site.

A trade area is a geographical area containing the customers of a particular firm or group of firms for specific goods or services. A trade area can also be defined as a district, whose size is generally determined by the boundaries within which it is economical, in terms of volume and cost, for a retailer to sell and/or deliver a good or service.

Figure 6.1: Parts of Trade Area



Source: ICFAI Research Center

The first step in trade area analysis consists of describing and analyzing alternate trade areas and deciding on the most promising one (Refer Figure 6.1). Once a trade area has been selected, it should be examined on a regular basis to keep track of changes occurring in the area.

6.5.1 Size and Shape of Trade Areas

Every trade area consists of three parts: primary, secondary and fringe. The primary trade area contributes 50% to 80% of the store's customers. This area is nearest to the store, has a higher percentage of customers, and contributes the highest per capita sales. The secondary trade area provides another 15 to 25 percent of the store's customers. This trade area is situated beyond the primary trade area and the customers in the area are dispersed more widely than in the primary trade area. A fringe trade area consists of all the other remaining customers. These customers are the most widely dispersed. Fringe trade areas usually contain out shoppers, who travel great distances to patronize a particular store.

A retail store could have a primary trade area of three kilometers, a secondary trade area of seven kilometers, and a fringe trade area of nine kilometers. The greater the primary and fringe trade areas, the better it is for the retailer[5]. A diagram of the parts of trade areas is given in Figure 6.1. In practice, trade areas do not take the concentric pattern shown in the figure. They adjust according to the environment.

[5] Edward M.Mazee, Identifying the Key Factors in Retail Store Location, Journal of Small Business Management, Jan1972, p18.

A number of different factors determine the size and shape of trade areas. Some of them are:

- Store type
- Store size
- Merchandise type
- Location of competition
- Housing patterns
- Travel time

Store Type

Two types of stores in the same shopping mall can have trade areas of different sizes. One store might offer a better product assortment; have heavy promotions, and a stronger image. Such a store, referred to as a destination store, has a much larger trading area than a competitor with a less unique appeal does. Some outlets do not have a trading area of their own and even do not have their own traffic. Such outlets are dependent on customers who are pulled towards the area for some other reasons. For example, restaurant at a shopping mall or a florist in the lobby of a hotel depend on the customers pulled to the shopping mall or hotel. Such store is referred to as a parasite store.

Store Size

The size of the trade area of a store is influenced by the size of the store itself. The trade area tends to increase with the increasing size of the store, but this increase may not be in proportion to the increase in the size of the store. This relationship between the size of the store and the size of the trade area can be attributed to the assortment of goods and services offered to the customer. For example a hypermarket like More mega mart, which provide a large assortment and variety of products under one roof, have larger trade area, whereas supermarket like Ratnadeep which have a smaller store size and carry less merchandise have smaller trading areas.

Merchandise Type

The type of merchandise offered by a retail store also affects the size of the trade area. Merchandise can be classified as convenience goods, specialty goods, and shopping goods.

Convenience goods refer to products that customers buy frequently, such as fruits, vegetables, groceries. These are purchased from neighborhood Kirana stores and roadside stalls. Thus, in such cases, the trading area is small. Other types of convenience goods, such as staple foods like rice and dal and groceries like soaps and detergents, require little pre-purchase planning. These goods are generally bought on a monthly basis. Super markets like DMart are main locations for such purchases. The trading area for supermarkets is larger than the trading area for Kirana stores.

Shopping goods are bought less frequently than convenience goods. These goods include clothing, and electronic goods. Since the investment in such goods is high, customers are willing to spend time comparing products in a number of different stores before purchasing. Stores selling such shopping goods have a relatively large trade area.

Specialty goods possess unique characteristics, but require a considerably high investment and time, for example, cars, two wheelers, and luxury goods. Customers buy such goods only after a lot of pre-purchase searching and planning. Stores carrying such type of goods have a greater trading area than shopping goods stores.

Location of Competition

The number of competing stores in an area and the distance between the stores also influence the trading area. Two types of competition take place: inter-store competition and intra-store competition. Intra-store competition refers to competition between two retailers selling similar merchandise. In such cases, trading area is often reduced for each. Suppose, Nilgiri’s and Reliance Fresh were located in the same area, customers could choose to go to either one of the stores. As a result, the trade area of each store would shrink. Inter-store competition or competition among retailers selling dissimilar merchandise increases the range of goods and services offered at a particular location. If Shopper's Stop, Titan, Archie’s and Barista were located in the same area, customers would benefit from the availability of a wider range of goods and services. Consequently, customers from greater distances would be pulled to these areas thus expanding the size of their trade area. In addition, a new store's entry into a particular location can affect the size and shape of the trade area of the established stores at that location.

Housing Patterns

The trade area of a retail store is influenced by the housing patterns of the people in a region. People in urban areas generally reside in multi-unit housing structures close to prime commercial areas. In suburban areas, people live in individual houses that are spread out geographically. In such areas, the retailer has to pull consumers from greater distances to generate a sufficiently high sales volume.

Travel Time

This refers to the time taken by the customers to travel to retail stores. With regard to travel time the greater the distance between their point of origin to the store (destination point) the greater the travel time and the greater the trade area.

Check Your Progress - 1

1. For which of the following analyses, a marketer carries out regional area analysis and local area analysis?
   a. Market analysis
   b. Market area analysis
   c. Trade area analysis
   d. Both Trade area and Market area analysis
   e. Trade analysis
2. There are many factors, which affect both market area and trade area. Which of the following is not a factor affecting both?
   a. Demographics
   b. Regulations
   c. Psychographic
   d. Economic base
   e. Competition
3. All businesses operate in an economic environment and many of their decisions are based on economic factors. Which of the following is not the part of economic factors that should be examined by retailers?
   a. Per capita income
   b. Employment rate
   c. Business cycles
   d. Social environment
   e. Interest rate
4. Which of the following measures the level of demand in a particular market based on the population, consumer expenditure, competing retail space and a particular product or product area?
   a. IRS
   b. SAI
   c. CRS
   d. EXP
   e. Both SAI and CRS
5. Which among the following terminologies provide retailers with vital information such as store patronage, local market opportunities, competing

businesses, and barriers that would dissuade consumers from visiting the site?

a. Store analysis

b. Market Analysis

c. Market area Analysis

d. Trade area analysis

e. Customer Analysis

6.5.2 Measurement and Definition of the Trade Area

The process of measuring and defining a trade area is one of the important components of retail store location analysis. The objective of measurement and definition is to determine the trade area that has the highest probability of attracting customers within the selected market area.

Retailers use a variety of techniques to define a trade area. The most popular methods are gravity models, trend analysis, analog models and regression models. Geographic Information Systems (GIS) are also widely used to measure and analyze trade areas. With advances in computers, GIS applications have become very sophisticated. At the same time, they have become cheaper, thus leading to an increase in the use of GIS by the retail industry. Globally, mapinfo.com and Tactician are the major companies that develop and market GIS software applications.

Defining the Trade Area of an Established Store

The size, shape and characteristics of an established store's trade area can be defined accurately and easily. The trade area can be measured with the help of either secondary data (store records) or primary data (by conducting a special study). Store records can provide the addresses of customers who bought the goods and services on a cash or credit basis. Using these addresses primary, secondary and fringe trade areas can be described in terms of the

- Frequency of shopping at a particular retail outlet by people from different geographic locations
- Average billing amount at an outlet by people from a particular geographic location
- Presence of an outlet's credit card holding customers in a particular geographic location

Though it might be easy to obtain information on the customers having/using credit cards, the retailer should not arrive at any conclusion until the information on cash customers is also included. Analysis of only cash customers or only credit customers might result in overstatement or understatement of the total number of customers from a particular area. The retailer can also gather primary data to get a clearer picture of the store's trade area. To obtain demographic and lifestyle data of its customers the retailer can conduct a primary research on its own or with the help of a market research firm. Primary research can be done through in-store surveys. Using an in-store survey, the researcher undertakes a sample within the store, with the interviews being conducted in proportion to the store sales on each day of the week. Sample sizes need to be optimal to allow for analysis of results by potential geographic areas from which people will visit the stores. The results of an in-store survey can be tabulated to indicate which geographic areas provide what proportion of the customers. Irrespective of the manner in which the trade area is defined, the retailer should consider the time bias, since customer inflow varies with time like shopping centers near parks and entertainment centers have a heavy influx at night and weekends, whereas the stores in main centers have more customers during festivals and special occasions.

Once the trade area has been defined, the retailer must map the locations and density of customers in the trade area, either manually or through GIS. In the manual process, a paper map representing the area surrounding the store is used. Colored dots or pins are placed on the map to indicate population densities, income levels and other related factors. After this has been done, customer locations and densities are indicated, then primary, secondary and fringe trade areas are marked along with their pin/zip codes. GIS integrates all the important customer information with other sources of information like the census data, and develops digital maps representing primary, secondary and fringe trade areas.

Defining the Trade Areas of a New Store

A new retailer planning to set up a store in a well-established trade area can define its trade area in a manner similar to that of an established store. The process of defining the trade area of a new store would differ, when the trade area has less well-defined purchasing and traffic patterns. The potential trade areas of a new store should be analyzed frequently by examining the opportunities offered by the market, existing customer profiles, and traffic patterns.

There are four commonly used methods for delineating the trade area of a new store.

- Trend Analysis
- Analog Models
- Regression Models
- Gravity Models

Trend Analysis

Trend analysis involves predicting the future based on the past, analyzing government and other data pertaining to predictions regarding the location of the population, automobile registrations, housing development, public transportation, etc. Consumer surveys are also used to collect information on the time and distance people are ready to travel for different possible retail locations and the features that pull the consumers to the store. Based on the data the new store trading area is determined.

Analog Model

This is the most popular and simplest trade area analysis model. It estimates the potential sales of a new store on the basis of the revenues of existing stores in identical areas, the competition at a prospective location, the expected market share of the new store at the proposed location, and the size and density of the primary trade area of the location.

Regression Model

This model develops a series of mathematical equations representing the relationship between the potential sales of the store and the various independent factors of each location. The regression model helps retailers examine the impact of independent variables on the potential sales of a new store: the size of the population, average income levels, number of households, competitors close-by, transportation problems and traffic patterns.

Gravity Model

These models are based on the fact that people tend to shop at stores that are closer and more attractive than their competitors are. They take into consideration factors like distance between the consumers and the competitors, distance between the consumers and a particular store location, and the image of the store in the consumer's mind. Reilly's model and Huff's model are two important gravity models used by retailers.

Reilly’s Law of Retail Gravitation

Inspired by the formula for gravity, Reilly proposed[6] that "two cities attract the retail trade from an intermediate city or town in the vicinity of the breaking point in direct proportion of the population of the two cities and inversely proportional to the square of the distance from these two cities to the intermediate town". Simply put, a customer will travel a distance to shop depending on the population of the shopping area and the distance between areas. Reilly's model suggests that greater shopping center mass (size) increases consumer utility, thus increasing the gravitational pull of a center; and that distance to the center decreases consumer utility, which exponentially decreases the gravitational pull of the center.

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[6] William J. Reilly, Methods for the Study of Retail Relationships, University of Texas Bulletin 2944 (Austin: University of Texas, 1929; reprinted, 1959).

It is given by

$$\frac{T_a}{T_b} = \frac{P_a}{P_b}\left(\frac{d_b}{d_a}\right)^2$$

Where T_a and T_b represent the proportion of trade drawn to the centers A and B

P_a and P_b represent the population sizes of cities A and B

d_a and d_b represent the distance from the intermediate town to cities A and B.

The original model has been reformulated in order to determine the position of an intermediate area where trade becomes split between two competing centers.

$$D_{ab} = \frac{d}{1+\sqrt{\frac{P_b}{P_a}}}$$

Where,

D_{ab} = Breakpoint of A

d = distance between A and B

P_a = Population of city A

P_b = Population of city B

This formula determines the point of indifference between two cities or locations, in order to determine the trade area of each location. The point of indifference refers to the geographic breaking point between two locations at which consumers would be indifferent about shopping at either location. According to Reilly's law, the majority of the consumers would be pulled towards the larger location because of the greater availability of merchandise and facilities, which would make the increased travel time worthwhile.

Based on this formula, a city (A) with a population of 12,00,000 population attract people from twice the distance that to a city (B) with a population of 3,00,000. If there was a distance of 15km between the cities, the point of indifference for the bigger city (A) is 10 km and for the smaller city (B), it is 5 km.

d = 15 Km

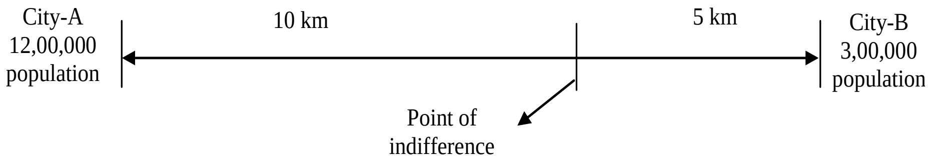
Pa= Population of bigger city (city A) = 1200000

Pb= Population of smaller city (city B) = 300000

Substituting these values in the formula, we get

$$D_{ab} = \frac{15}{1+\sqrt{\frac{3,00,000}{12,00,000}}}$$

$$= 10 \text{ km}$$



So, city A, as can be noticed above, pull people from a distance of 10km, whereas city B can draw only those people who reside within 5km. Suppose, a builder owned shopping centers in City A and City B. He can charge a higher rent for shopping space in city A than for shopping space in city B, and according to Reilly's gravity model, shopping space in city A will draw more customers than shopping space in city B.

Reilly's law is based on two major assumptions:

- Two competing areas will be equally accessible from a major road
- Retailers in two areas are equally competitive

Other factors that affect customer preferences are ignored or held constant. Reilly's law of retail gravitation has made a significant contribution to the analysis of trade areas. The data required by the model is easily available and inexpensive to collect. Retailers can integrate Reilly's law with other tools to find out whether the trade area being considered is the most appropriate.

In spite of the advantages it offers, Reilly's law of gravitation also has two major limitations:

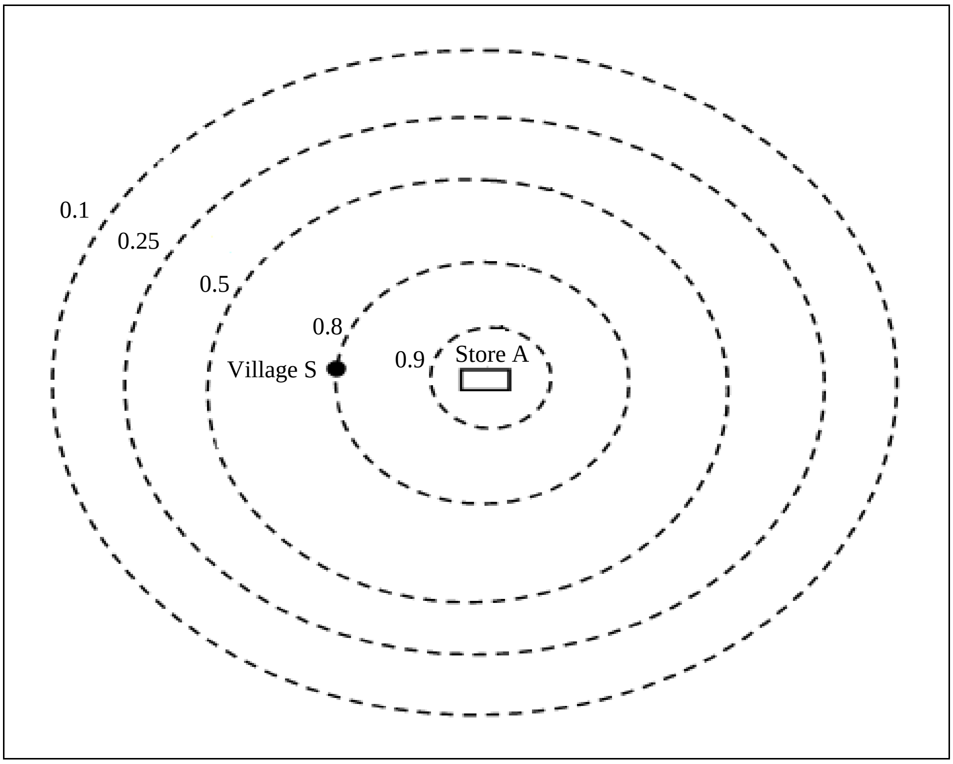
- The distances measured are limited to the major roads; they do not consider streets. Many people would travel short distances along the streets, which might not be taken into account.
- The exact distance to a store might not be in agreement with the consumer's perception of distance.

Huffs Law of Shopper Attraction

Huff's Law of Shopper Attraction is a gravity model (Huff, 1964) similar to Reilly's law. It can be used to define a store's trade area. Huff's law was developed in an attempt to overcome some of the limitations associated with Reilly's model. It is based on the assumption that not everyone within a trade area will travel to the store or shopping center. Huff's model provides a series of probabilities of consumers choosing to visit one center as opposed to another in terms of the attractiveness of each center (measured by floor space) and a deterrence factor (measured by traveling time to the center). That is, it gives the probability of how likely it will be for a customer to travel to a particular store/shopping center.

Huff's model enables the probability values for a series of areas to be calculated and plotted on a map for easier analysis. The simplest way of interpreting Huff's model is to think of it as a geographical map representing the contours of demand around a store. Figure 6.2 shows the contours that stretch out from a store (like the contours of route map). Each contour in the figure is given a probability value. This value indicates the likelihood of a consumer within that area shopping at that store instead of traveling to a different location. Since a consumer living in the village S would go to shop at store A, 80 percent of the time, the 0.8 contour crosses village S.

Figure 6.2: Contours of Customer Demand



Source: ICFAI Research Center

Huff's model takes into account the pulling power of store A relative to the total pulling power of all other stores in the region. The pulling power of a retail store depends on the size, distance and types of products it offers. Therefore, three factors are used to calculate probability contours:

*The size of the stores in the regio*n: Large stores attract more consumers than small stores because they offer a wider selection of goods.

The time taken to travel to each store: Stores located in remote areas tend to be less attractive than those located close by because of the time consumed by traveling and the inconvenience of doing so.

The type of product: People are prepared to travel further for certain types of products (like quality furniture) than for other types of merchandise. The type of product being purchased has an influence on the way consumers balance the attraction of store size against the inconvenience of traveling a long distance to a store.

Huff's model helps in identifying the number of shoppers from surrounding towns or cities that may shop at a particular site or location. This model might also take into account the percentage of potential customers that would like to travel through the area to patronize retailers in other shopping centers in the locality. These percentages are included in the calculation.

Huff's law of shopper attraction defines trade areas on the basis of the product assortment (desired by the consumer) offered at different shopping locations, time taken to travel from the consumer's residence to alternative shopping centers, and the sensitivity of shopping to travel time. The product assortment variable is measured by total area (sq.ft.) of selling space a retailer expects all other firms at a shopping location to assign for a particular category. Sensitivity towards the kind of shopping describes the purpose of the trip – for restocking or for shopping and the type of goods or services being sought (like furniture, apparel or groceries).

Huff's law of Shopper Attraction can be given as

$$P_{ij} = \frac{\dfrac{s_j}{(T_{ij})^{\lambda}}}{\displaystyle\sum_{j=1}^{n} \dfrac{s_j}{(T_{ij})^{\lambda}}}$$

Where,

P_{ij} = Probability of consumer's traveling from home i to shopping location j

s_j = Square feet of selling space in shopping location j containing a particular

merchandise category

T_{ij} = Travel time from consumer's home i to shopping location j

λ = Parameter used to estimate the effect of travel time on different kinds of shopping trips

n = Number of different shopping locations

λ is usually determined with the help of research or a computer program. The application of this formula is illustrated by the following example:

A company manufacturing cosmetic products is planning to set up a leased department at a retail store at a specific shopping location. The company is studying three prospective shopping locations A, B and C. All the retailers in these areas are expected to assign 600, 350 and 250 total square feet of store space respectively in their stores to the company's cosmetic products. Potential customers reside 13 minutes from location A, 6 minutes from location B and 9 minutes from location C. From the research conducted earlier, the company estimated the effect of travel time to be 2.

$$P_{iA} = \frac{(600)/(13)^{2}}{600/(13)^{2} + 350/(6)^{2} + 250/(9)^{2}} = 21.7\%$$

$$P_{iB} = \frac{(350)/(6)^{2}}{600/(13)^{2} + 350/(6)^{2} + 250/(9)^{2}} = 59.4\%$$

$$P_{iC} = \frac{(250)/(9)^{2}}{600/(13)^{2} + 350/(6)^{2} + 250/(9)^{2}} = 18.8\%$$

Therefore, the probability of consumers shopping for cosmetic products at location A is 21.7%, at location B is 59.4% and 18.8% at location C. If 100 people reside 6 minutes from location B, then 59 of them will shop there.

To determine the overall trading area for location B, similar calculations should be done for consumers living 5, 10, 20, 25 minutes away and so on. The number of consumers at each distance who would shop there must be added. This will enable all the stores at location B to estimate the total market, size of trade area, and primary, secondary and fringe areas for a specific product category.

Huff's law can be applied only after taking into account the following factors:

- If more selling space is added for a particular product category at a location, the percentage of population residing at every travel time who shops at the store increases.
- The probability of consumers shopping at a specific location depends mainly on the influence of travel time (for that specific product category).
- Huff's model is highly product specific, so it gives different trade areas for different product categories.
- The variables in the model are difficult to calculate. For example, travel time should be converted to distance in miles for the purpose of mapping. Moreover, travel time depends on the type of transportation used.

Example: Amazon Go and Amazon Fresh Retail Stores Measure Trade Using Store Analytics

Amazon launched physical Store Analytics that help companies fetch aggregated and anonymized understanding about the performance of their products. Amazon Go and Amazon Fresh, hosts the technology at the Amazon retail stores in USA.

Contd….

The technology provides a sneak peek into how customers search for a product, consider and purchase them. This would facilitate more streamlined decisions to promote products and create their ad campaigns. The data driven analytics help companies understand their products better and refine their supply over time.

Source: Zboraj, M. (June 29, 2022). Amazon Launches Physical Retail Store Analytics. Retrieved from https://www.progressivegrocer.com/amazon-launches-physical-retail-store-analytics. Accessed on 07-07-2022.

6.6 Site Evaluation and Site Selection

A wrong site location would lead to business failure. Site evaluation, hence, is of utmost importance to gauge sales potential, accessibility, increasing footfalls to the store that would eventually become potential sales to the firm, and most importantly conforming to legal aspects before raising the building. It helps a retailer to select the evaluated site(s). Site selection is a way of visualizing the firm’s business and its target market. The two important questions: What to sell? For whom to sell? are answered by site selection. What, do you think, might have made Shopper's Stop locate its store at Andheri, M.G.Road-Chembur and Bandra West in Mumbai, Begumpet and GVK One in Hyderabad, Ashok Nagar – Magrath Road in Bangalore, Indira Palace- Malvia Nagar-Jaipur, Ansal Plaza – Khelgaon Marg in Delhi, The Great India Place in Noida or Harrington Road – Chetpet in Chennai?

After identifying a particular trade area, the retailer must select a site for the store. To do so, the retailer must carry out a site evaluation and selection process (Refer Table 6.2).

Table 6.2: Advantages and Disadvantages of Various Retail Locations

Locations	Advantages	Disadvantages
Isolated Store	• Low rents • Lack of competition • Operational flexibility • Good parking space	• Promotion driven • Hard to attract customers
Central Business District	• Easy accessibility • Good assortment of products and services • High pedestrian traffic	• High rents • Parking problems • Traffic congestion

Locations	Advantages	Disadvantages
Secondary Business District	• Decent product assortment • Proximity to residential areas	• Parking problems • High rents
Neighborhood Business District	• Low rents • Good parking facilities • Less congestion • Long working hours	• Limited assortment of goods and services • Limited traffic
Planned Shopping Center	• Good product assortment and services • Ample parking space • High suburban population • One-stop shopping center • Sharing of common costs	• Land-lord imposed regulations • High rents compared to isolated locations • Competitive environment • Domination by large anchor stores

Source: ICFAI Research Center

6.6.1 Types of Locations

The retailer can choose from three types of locations: the isolated store, the unplanned business district, and the planned shopping center. The number of customers visiting a store and the business generated by that store depends on the location of the store. (See Table 6.2 for the advantages and disadvantages of various locations.)

Isolated Store

The isolated store is a freestanding retail outlet situated on either a street or a highway. Stores of this kind do not have any retailers in their vicinity with whom they have to share consumers. The isolated store location is not suitable for small retailers as customers would not be willing to travel to small stores, which do not offer much variety and have a shallow assortment of merchandise. But, large retail stores like Wal-Mart and Giant can afford to select an isolated location, as they are capable of pulling and retaining consumers.

The Unplanned Business District

Unplanned business districts are retail locations in which two or more stores are situated either together or closely in a manner that the total arrangement in that particular district was not planned in the initial long range planning. The stores are situated depending on what suits them best, but not based on the district.

Consequently, in a particular area all the stores may sell similar or related products. Unplanned business districts can be categorized into four types

- Central Business District
- Secondary Business District
- Neighborhood Business District
- String

Central Business District

A central business district (CBD) is the traditional center for retailing in a city. It is the largest area for shopping in a city. A CBD has a high concentration of department stores and large offices; railway and bus stations; entertainment facilities like pubs, clubs, and cinemas; and a town hall. Generally, main roads converge into a CBD resulting in a high level of pedestrian and vehicular traffic. Real estate is very expensive in a CBD.

CBDs usually pull in consumers of all classes and ethnic groups from the whole city. A CBD contains at least one major department store and a group of specialty and convenience stores. The arrangement of stores in a CBD does not follow any specific format. Usually, early entrants occupy the central part. Table 6.3 lists the CBDs present in major Indian cities.

Though CBDs are known for retailing activities, overall sales of outlets located in CBDs has been decreasing substantially compared to sales of outlets located in planned shopping centers. This has happened because many residential areas have shifted to the suburbs. In many major cities, most of the people in middle and upper income groups have moved to the suburbs, where they are provided with planned shopping centers. Table 6.3 gives a macro view of CBDs in select cities of India.

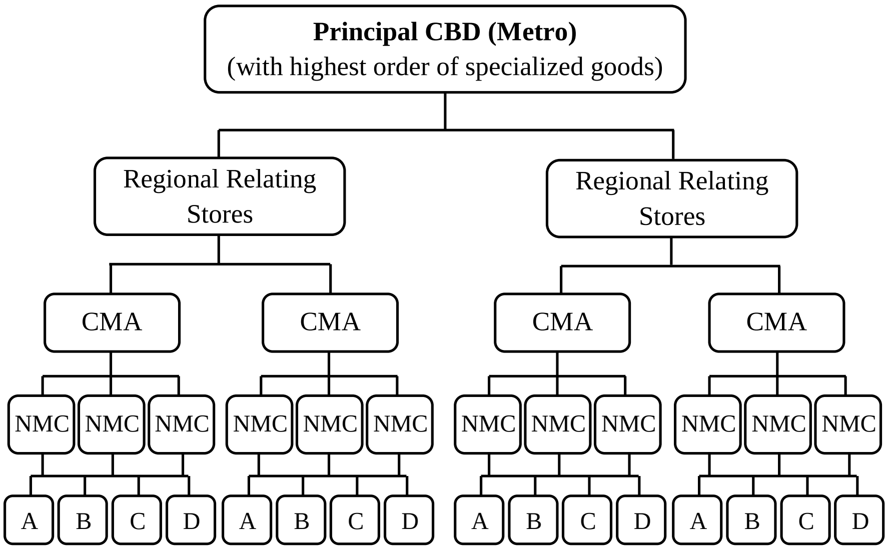
Table 6.3: Central Business Districts (CBDs) in Major Indian Cities

City	Central Business Districts
Mumbai	Colaba Causeway, Fort/Churchgate, CBD Belapur, Nariman point and Kemps Corner in South Mumbai Linking Road in North Suburban
Bangalore	M.G.Road, Brigade Road
Delhi	Connaught Place
Hyderabad	Begumpet, Banjara Hills, Somajiguda, Panjagutta, and Abids
Chennai	Anna Salai, Nungambakkam High Road, Armenian St., Cathedral Road, Egmore, T-Nagar and Alwarpet

Sources: (i) ICFAI Research Center; (ii) Ishar Judge Ahluwalia, Ravi Kanbur, Mohanty P.K. (Edited), "Urbanisation in India: Challenges, Opportunities and the Way forward", Sage Publications, 2014

Figure 6.3 depicts the hierarchical order of Central Business Districts (CBD)

Figure 6.3: Hierarchical Order of CBD



Note: CMA = Community Marketing Areas

NMC = Neighbourhood Marketing Centres

A, B, C, D = Convenience Shopping Goods Stores

Source: ICFAI Research Center

Usually, consumers are more aware of unplanned business districts and planned shopping centers than isolated stores. As a result, stores at unplanned business districts and planned shopping centers generate a major chunk of retail sales.

Secondary Business District (SBD)

A SBD is an unplanned shopping center in a city, which is generally bounded by the junction of two major streets. Big cities like New York in the US, London in the UK or Mumbai in India usually have many SBDs, each containing at least a mini department store, a variety store, and some big specialty stores apart from many small stores. The significance of this type of shopping location has been increasing because of the expansion of cities over large geographic areas. Stores located in an SBD are small outlets, which offer a limited variety of products with a shallow assortment. In addition, they have a smaller trade area than that of the stores in CBDs. However, they offer greater proportion of convenience goods than stores in CBDs.

Neighborhood Business District (NBD)

An NBD is an unplanned shopping center that caters to the convenience shopping and service needs of a particular residential area. An NBD typically consists of a small grocery store, stationery store, a bakery, a restaurant, a vegetable store etc. NBDs are usually situated on the main streets of residential areas.

String

A string is an unplanned shopping center, consisting of a group of retail outlets, generally offering similar or related products, situated along a street. Car accessory stores and jewelry stores are often found in a string.

The Planned Shopping Center

A planned shopping center consists of a set of architecturally similar commercial establishments constructed on a site which is owned and managed centrally, operated and designed as a single unit, has a balanced tenancy, and has access to good parking facilities. Generally, a planned shopping center contains one or more anchor stores along with a variety of smaller stores. Balanced tenancy helps the stores in a planned shopping center complement each other in the quality and the range of products offered and thus help them cater to the overall needs of the population in the trade area. To ensure balanced tenancy, the management of a planned shopping center stipulates the proportion of total space that each type of retailer may occupy, specifies the product lines that each of the different retailers may sell, and specifies the type of retailers who can obtain unexpired leases for stores in that shopping center. There are three types of planned shopping centers: regional shopping center, community shopping center and neighborhood shopping center.

A regional shopping center is a planned shopping center catering to a geographically dispersed market. It usually consists of at least one big department store and 50 or more small retailers. Regional shopping centers offer a very broad and deep assortment of products and services that are aimed at enhancing the shopping experience of consumers. A typical regional shopping center's target market consists of around 1,00,000 people, residing or working at half an hour's driving distance from the shopping center.

The ground floor is completely devoted to food. The food court offers six types of cuisine, including Indian, Lebanese, Chinese, Italian and others. McDonald's also has an outlet here. Crossroads has a rooftop car parking facility on the Teflon retractable roof (Asia's largest, outside of Japan), apart from the basement parking facility with a capacity of about 150 cars.

Community Shopping Center

A community shopping center is a medium sized planned shopping center consisting of a branch of a department store, a variety store, a category killer store, and many more small stores. It caters to the needs of consumers coming from one or more populated residential areas located close-by. This type of center offers a moderate assortment of both shopping and convenience products and services. A community shopping center usually serves about 20000 to 100000 people residing or working within a 10 to 20 minute driving distance from the shopping center. Establishing a community shopping center requires long range planning.

Neighborhood Shopping Center

A neighborhood shopping center is a planned shopping center, which aims at providing convenience products that meet the daily needs of customers in a particular neighborhood. Such a center has a supermarket or a drugstore, which would be the largest store in the neighborhood. The other stores in the neighborhood shopping center are a bakery, a dry cleaner, a stationery store, a barber store, a beauty salon, a grocery store, a hardware store, and a restaurant. A neighborhood shopping center offers convenience goods and services to customers residing or working in the immediate vicinity. It typically serves 3000 to 50000 people who are located within a 15 minute driving distance. A neighborhood shopping center is planned carefully with balanced tenancy when developed initially. However, with the passage of time, the planned aspects of this shopping center may disappear and the prospective new occupants of the store may face very few restrictions.

After identifying different types of locations, the retailer must select a location for its store. The decision to situate a store at a particular location is based on the strategy adopted by the retailer and a proper analysis of the strengths and weaknesses of every alternative location. Once the merits and demerits of the available alternatives have been analyzed, a broadly defined site for setting up the store can be identified. A retailer takes two decisions at this juncture, i.e., defining the general location type and identifying specific site at such a location.

Example: Google Opens First Physical Store in New York

Google in 2021, opened its first physical retail store in New York City. The store would offer a variety of Google products at display and for sale like Google phones, smart home devices and many more. The store offers an opportunity for customers to understand how the products work and interact with experts on how to best use Google products.

Source: Gartenberg, C. (May 20, 2021). Google is Opening its First Physical Retail Store This Summer in NYC. Retrieved from https://www.theverge.com/2021/5/20/22445472/google-first-physical-retail-store-chelsea-nyc-summer-2021. Accessed on 07-07-2022

6.6.2 Choosing a General Location

The general location type could be like a "site on a highway in an isolated location" or a "neighborhood shopping center." Once the general location has been defined, the retailer has to identify the specific site in a city/region that matches the predefined site location, like a site on MG road in Bangalore.

6.6.3 Assessing Site Evaluation Criteria

Retailers should conduct extensive analysis to assess every general location and the specific sites present within them. Selecting the site for a retail store is as critical as the selection of a retail area, particularly for stores that depend on the traffic patterns of customers for generating business. In any area, the best site for a specific store is referred to as the 'one hundred percent' location. As different types of retailers require different types of locations, a location that is 'one hundred percent' for a particular retailer may not be the best location for another type of retailer.

Generally, a retail site is evaluated based on the sales potential and the cost of doing business at that site. The following factors must be considered when selecting a site:

- Sales potential of the site
- Access to the site
- Access for pedestrians
- Synergies from nearby stores
- Leasing and occupancy terms
- Nature of the site
- Legal and political environment

The *sales potential* of a site is determined by demographic, economic and competitive factors and the strategies through which the retailing firm wishes to create a competitive advantage. When evaluating the sales potential, a retailer should also consider the growth potential for a store in that prospective location.

Accessibility to the site refers to the ease with which a customer can approach or leave a store located on a specific site. This depends on road patterns, their condition, the number of traffic signals on the way to the site in the primary trade area, parking facilities etc.

Pedestrian accessibility refers to the ease with which pedestrians can navigate their way towards the store or walk through the mall. This depends on the congestion on the roads, the congestion within the mall where the store is located, and visibility of the store.

The *synergies* that a store can derive from being located next to other stores also play a crucial role in site selection. Complementary retail stores at a particular shopping center help each other. When all the stores in a shopping center have similar strategies for retailing in terms of merchandise assortment, quality, prices, services and the shopping environment, they derive a cross shopping benefit.

The terms of *lease and purchase contracts* have a significant impact on a retailer's site selection decision. The occupancy rate in the immediate or surrounding locality is also a critical factor. For instance, a low occupancy rate at a particular shopping center can increase the retailer's negotiating power, as the real estate developer would be eager to fill the vacant space. But, a low occupancy rate can also be an indication of poor access and poor market variables. If the low occupancy rate does not indicate poor economic viability, it can attract unwelcome competitors.

The *legal and political environment* also has an influence on site selection. In India, the setting and development of retail outlets is governed by a set of regulations. These regulations can vary from state to state and city to city. Every state has its own development control regulations that determine the location of retail stores, space needed to be left, the height of the building, the permissible floor space, the availability of parking space in relation to the floor space, the presence of fire protection systems and the standards of structural safety. Evaluating the legal and political environment before locating in a foreign country is important, as the future operations of multinational retailers are more vulnerable to the political changes.

The nature of the site and its surrounding areas must not be ignored, whether it is open land or an already existing structure. The physical specifications and features of the site must be in accordance with the needs of the retailer. Many factors are critical to the retailer's business plan: traffic flow during the day time, number of cars that can be accommodated in the parking space and, most important the room for expansion. A site, which is functional today, might not be functional later with the growth of the business.

6.6.4 Multi-Attribute Weighted Checklist

Most of the retail outlets integrate all site evaluation factors with the help of management's judgment. At the ground level, a checklist for all significant factors is prepared and the site is evaluated according to the degree to which the site meets the desired characteristics.

Table 6.4: A Multi Attribute Weighted Checklist

Attribute	Management Importance	Existence				Score = importance Δ existence			
		Shopping Center	CBD	Isolated Location	Strip Mall	Shop-ping Center	CBD	Isolated Location	Strip Mall
Traffic Flow and Accessibility									
Access of Vehicular traffic									
Access to Pedestrian traffic									
Availability of mass transit									

Attribute	Management Importance	Existence				Score = importance Δ existence			
		Shopping Center	CBD	Isolated Location	Strip Mall	Shop-ping Center	CBD	Isolated Location	Strip Mall
Retail Competition									
Number of stores in the area									
Competitiveness of other retailers									
Possibility of joint promotions with local retailers									
Site Characteristic									
Number of parking spaces available									
Visibility of the site									
Compatibility of neighboring stores									
Cost Factors									
Easy terms of lease/rent agreement									
Basic rent payments									
Length of lease									
Local taxes									

Attribute	Management Importance	Existence				Score = importance Δ existence			
		Shopping Center	CBD	Isolated Location	Strip Mall	Shop-ping Center	CBD	Isolated Location	Strip Mall
Operation and maintenance cost									
Restrictive clauses in lease									
Total						xxx	xxx	xxx	xxx

Source: ICFAI Research Center

Table 6.4 gives a model multi-attribute weighted checklist that can be used for evaluation of sites. The left side column displays certain attributes, which the management considers important. The top row comprises a list of possible sites. Each attribute is given weightage (from 1-5) according to its importance for a proposed store. Then each attribute is assigned a number, depending on the extent to which the attribute is present at each of the sites mentioned. The final score for each attribute at a particular site is arrived at by multiplying this number with the weightage given by the management. The sum of the total scores of all the attributes gives the total score of each site. Thus, to take a decision with respect to the setting up of a store, the management can select the site with the maximum score.

Omnichannel Retailing: Blurring the Boundaries between Retail Channels

The advent of the internet and smartphones has questioned the relevance of store location and site selection in retailing. As a consequence, many physical retailers (e.g., Walmart) are venturing actively into the online space. Similarly, many online retailers are also planning to start their operations into the physical space (e.g., Lenskart). Retailers are operating with a combination of different types of channels while dealing with their customers. Accordingly, they can be classified into three broad categories, i.e., multichannel retailers, cross channel retailers, and omnichannel retailers. They define multichannel retailing as a set of retailing activities related to selling merchandise and services through more than one channel where a retailer does not integrate any of the retail mix elements (e.g., product, price, promotion) across channels. They define cross-channel integration as a set of activities concerned with selling merchandise and services through more than one channel where a retailer integrates more than one element of the retail mix, but not all. According to them, omnichannel retailing is a set of activities related to selling merchandise and services where a retailer integrates all the retail mix elements across all the available channels.

The main objective of omnichannel retailing is to provide a seamless shopping experience by integrating all the existing retail channels. Empowered by the centralized data management system, omnichannel retailers enable their customers to use different channels simultaneously during their shopping journey from need identification until product purchase. Recent industry reports indicate a rise in the number of internet users (through smartphones), which has provided them with greater control over their shopping process, want their retailers to be available on both store-based as well as offline channels, and provide a seamless shopping experience to their customers. Omni channel retailing centers around two key points: (i) customers can initiate channel integration process across all the touchpoints (e.g., accessing product-related information on the website and making the transaction inside the physical store); and (ii) retailers have complete control over the integration of various touchpoints.

Both physical stores and online channels have their advantages as well as disadvantages. Physical stores provide customers with an opportunity to touch and feel the products before making their purchase as well as provide a stimulating social entertainment experience. Online retailers enable customers to access a wide variety of assortment mix, product-related information, personalized offerings, and communication. Industry experts are observing a rising trend among customers accessing the internet through their smartphone. Nevertheless, most retailers provide mobile applications with minor updates of the retailer's existing website to accommodate the small screen of the smartphone. The seamless shopping experience requires retailers to work on four key operating areas, i.e., inventory management, purchase management, order fulfillment, and real-time review of operations. Hence, omnichannel retailers may gain competitive advantages by adopting the following strategy:

i. **Identify the various touchpoints used by the customers during their shopping journey**: It will help the retailers understand the customer preferences about their shopping needs but is also the touchpoint where they fulfill those needs. Consequently, retailers will be able to reach the customers at the right time, in the right place, and with the right offering.

ii. **Make the inventory visible across all the channels**: Through channel integration, retailers can optimize their inventory at hand, at the same time, increase the stock availability to meet the omnichannel demand. However, it requires retailers to control their inventory management systems, including purchase order, stock counts, inventory shipping details, by bringing it on a single platform.

iii. **Build automated operations**: Retailers need to automate their retailing operations to ensure that their retail mix elements work in sync with each other. It will not only allow retailers to bring efficiency into their operations but also provide a single view to their customers, thereby improving their cash flows as well as customer shopping experience.

The above measures will help a retailer in (a) continuously track their customer preferences, and (b) provide a customized solution to satisfy their needs.

There are various challenges that a retailer has to encounter while implementing an omnichannel retailing strategy. Below are the significant challenges faced by retailers while implementing an omnichannel retailing strategy:

i. **Overcoming the barriers of advanced technology requirements:** Retailers need to adopt an advanced warehouse management process to streamline their inventory movement across channels. It is because inefficient inventory management leads to an increase in inventory costs. Store-based retailers need to efficiently move their merchandise from distribution centers (DC) to retail outlets where the bulk breaking takes place. On the other hand, internet retailers need to store the merchandise at their DCs for a considerably more extended period (bulk breaking takes place at the DC), leading to higher inventory holding costs.

ii. **Engaging customers across channels**: Retailers need to map out the customer shopping process from need identification until the actual purchase. It is critical because the shopping behavior of customers has increasingly become complex wherein they research a product online and then makes a purchase in a physical store (webrooming); alternatively, they research a product in a physical store and buy it online (showrooming). Hence, retailers must use their various touchpoints effectively to engage their customers throughout their shopping journey and maintain consistency in their communication across the channels (e.g., brand-related information and pricing policy).

iii. **Managing Channel Conflicts**: Many conflicts may arise during the process of channel integration. Retailers have a separate organization structure for each of the above channels, which increases the challenge of providing seamless customer shopping experience. Similarly, the information systems required by physical stores are more merchandise oriented, whereas that required by online retailers is customer-centric. Hence, retailers need to ensure a smooth flow of information across the channel wherein the channels need to complement each other rather than acting as a substitute. Hence, retailers should address the above potential areas of channel conflict to make its omnichannel strategy effective.

Omnichannel retailing is gaining prominence across the globe due to its advantages. Researchers find that omnichannel retailing enhances customer loyalty, improves customer retention, enhances customer lifetime value, and acts as a potential source of competitive advantage.

Activity 6.2 Places like Anna Salai in Chennai, Nariman Point in Mumbai, Connaught Place in Delhi etc. are well known Central Business Districts. Choose a CBD in your city or a well-known CBD in India and evaluate the CBD in terms of various parameters that measure market attractiveness. What are the advantages of locating a store in a CBD?

Check Your Progress - 2

6. A number of different factors determine the size and shape of trade areas. Which of the following is a factor used to determine the same?
   a. Store type & Store size
   b. Merchandise type & Location of competition
   c. Housing patterns & Travel time
   d. Store proximity
   e. a, b, & c
7. Which of the following is referred to as the time taken by the customers to travel to retail stores?
   a. Travel time
   b. Visiting Time
   c. Reaching time
   d. Shopping time
   e. Transaction time
8. There are four commonly used methods for delineating the trade area of a new store. They are Trend Analysis, Analog Models, Regression Models. Which is the fourth one?
   a. Gravity models
   b. Digital model

c. Market analysis

d. Area analysis

e. Both a & b

9. Un-planned business districts are retail locations in which two or more stores are either situated together or closely located in a manner that the total arrangement in that particular district looks as if it was not a long range planning. Un-planned business districts can be categorized into four types. They are Central Business District, Secondary Business District, Neighborhood Business District. Which is the fourth one?

   a. Local Business District

   b. Tertiary Business District

   c. String

   d. Area Business District

   e. Primary Business District

10. Generally, a retail site is evaluated based on the sales potential and the cost of doing business at that site. Which of the following factors must be considered when selecting a site?

   a. Sales potential of the site & Access to the site

   b. Access for pedestrians & Synergies from nearby stores

   c. Leasing and occupancy terms, Nature of the site & Legal and political environment

   d. Political environment only

   e. Sales potential of the site & Access to the site, Access for pedestrians & Synergies from nearby stores and Leasing and occupancy terms, Nature of the site & Legal and political environment

6.7 Summary

- Retailers desire to set up their outlets in the best possible locations. The optimum store location for a retailer is based on many factors like the type of industry, the product category being sold, and the degree of competition.
- Retail stores are located where the opportunities offered by the market are at a maximum. Retailers usually go through four-step process to select a store location: a) analyzing alternate trade areas; b) determining the most beneficial type of location; c) selecting a general site and d) selecting a specific site.
- A trade area refers to the geographical area from which retailers attract customers. When two or more shopping centers are situated close to each other, then their trade areas would overlap.

- Every trade area consists of three parts, primary, secondary and fringe. The size and shape of the trade area depends on the size of the store, the type of the store, competitor's placement, and the time taken to travel to the store. Reilly's Law and Huff's model help retailers define their trade area.
- Globally, retailers use geographic information systems to analyze and delineate their trade areas. Three major factors that help retailers analyze their trade areas accurately: the characteristics of the population, the characteristics of the economic base, the competition and the level of retail saturation.
- There are three types of locations that a retailer can consider for locating its store, i.e. – isolated store, un-planned business districts and planned shopping centers. Important factors that are considered when selecting a site are sales potential; accessibility; pedestrian traffic; terms of occupancy and the legal and political environment. The retailer must go through all these steps of location and site evaluation to find the "one hundred percent location".

6.8 Glossary

Central Business District: A central business district (CBD) is the traditional center for retailing in a city. It is the largest area for shopping in a city.

Demography: It refers to the study of population characteristics, such as age, gender, income, education, family background, and occupation.

Index of Retail Saturation (IRS) measures the level of demand in a particular market on the basis of the population, consumer expenditure, competing retail space and a particular product or product area.

Isolated Store: The isolated store is a freestanding retail outlet situated either on a street or on a highway. Stores of this kind do not have any retailers in their vicinity with whom they have to share consumers.

Neighborhood Business District (NBD): An NBD is an unplanned shopping center that caters to the convenience shopping and service needs of a particular residential area.

Sales Activity Index (SAI): It is a measure of an area's per capita retail sales in relation to the per capita sales for the entire country.

Secondary Business District: SBD is an unplanned shopping center in a city, which is generally bounded by the junction of two major streets.

Trade Area Analysis: It provides retailers with vital information such as store patronage, local market opportunities, competing businesses, and barriers that would dissuade consumers from visiting the site.

Travel Time: This refers to the time taken by the customers to travel to retail stores.

Trend Analysis: Trend analysis involves predicting the future based on the past. It involves analyzing government and other data pertaining to predictions regarding the location of the population, automobile registrations, housing development, public transportation, etc.

6.9 Self-Assessment Test

1. What do you understand by market area and trade area analysis? Explain the factors affecting the attractiveness of market area and trade area analysis.
2. Explain the terms- sales area index and index of retail saturation.
3. Explain the Huff law of shopper's attractions.
4. Differentiate the term CBD and NBD.
5. Site selection is the key to a successful retail operation. Explain the factors which must be considered while selecting a site for a retail store.

6.10 Suggested Readings/Reference Material

1. Giri Arunangshu and Chatterjee Satakshi, "Retail Management: Text & Cases" Paperback, PHI Learning Pvt. Ltd., 2021.
2. Swapna Pradhan, "Retailing Management: Text and Cases", McGraw Hill, Sixth Edition, 2020.
3. Barry Berman, Joel R Evans, Patrali Chatterjee and Ritu Srivastava, "Retail Management", Thirteenth Edition Pearson Education, 2017.
4. Gibson G. Vedamani, "Retail Management", 5th edition, Pearson Education, 2017.

6.11 Answers to Check Your Progress Questions

1. (b) Market area analysis

A market area analysis consists of regional area analysis and local area analysis.

2. (c) Psychographics

Market area and trade area are affected by, demographics, economic base, regulations, proximity to supply source, store location and its availability and competitions.

3. (d) Population Growth

All businesses operate in an economic environment and many of their decisions are based on economic factors. Retailers must examine Per capita income, Interest rate, Employment rate and Business cycles in great detail.

4. (a) IRS

IRS measures the level of demand in a particular market on the basis of the population, consumer expenditure, competing retail space and a particular product or product area.

5. (d) Trade area analysis

Trade area analysis provides Retailers with vital information such as store patronage, local market opportunities, competing businesses, and barriers that would dissuade consumers from visiting the site.

6. (e) a, b & c

A number of different factors determine the size and shape of trade areas. Some of them are Store type, Store size, Merchandise type, Location of competition, Housing patterns and Travel time

7. (a) Travel time

The time taken by the customers to travel to retail stores called travel time.

8. (a) Gravity model

There are four commonly used methods for delineating the trade area of a new store. They are Trend Analysis, Analog models, Regression Models and Gravity models.

9. (c) String

Unplanned business districts can be categorized into four types. They are Central Business District, Secondary Business District, Neighborhood Business District and String.

10. (d) Sales potential of the site & Access to the site, Access for pedestrians & Synergies from nearby stores and Leasing and occupancy terms, Nature of the site & Legal and political environment

Generally, a retail site is evaluated based on the sales potential and the cost of doing business at that site. The factors which must be considered when selecting a site are Sales potential of the site, Access to the site, Access for pedestrians, Synergies from nearby stores, Leasing and occupancy terms, Nature of the site and Legal and political environment.

Unit 7

Retail Organization and Management

Structure

"A workplace filled with and driven by employees with positive attitudes attributes to service excellence and team success."

- Ty Howard is founder, CEO and editor in chief of the online magazine, Motivation, one of America's most requested motivational keynote speakers.

7.1 Introduction

The management of people in any retail organisation creates inevitable opportunities, costs and stress for all those who are involved.

A retail organization is a formal collection of people and other resources to accomplish a set of goals. Retail organizations use various resources like people, merchandise, machines, money, information and stores to cater to the needs of their target customers. Retail establishments should design an organization structure that helps them achieve their goals in an effective and efficient manner.

The organizational structure depicts an organization's managerial, administrative, and operational relationships. It also represents the authority, responsibility, and accountability of the store personnel working at various levels of a retail organization. A retail organization structure, groups various activities in the retail store for better administration and control.

The organization structure differs from store to store. It depends on various factors: the number of retail outlets and their size, the nature of the merchandise, the breadth and depth of the merchandise offered to the customer, the level of customer service, the positioning of the store etc.

The organization structure determines how well a retail store can function efficiently and effectively in a given competitive environment by satisfying the needs of its target market segment. Retail organizations can use various structures depending on the goals of the organization and its approach to store management. This unit discusses the various aspects of designing an organization structure and managing a retail store to serve the needs of its customers efficiently and effectively.

7.2 Objectives

After reading through this unit, you should be able to:

- Define the set of organizational objectives that enables efficient retail planning
- Sketch the Organizational Design that helps in establishing the roles and responsibilities of every stakeholder in the retail business
- Narrate the various forms of retail organizations that ensures hierarchical clarity to the employees when in retail business
- Familiarize with the different classifications of Organization Structures that helps in assimilating the areas of responsibilities of the internal stakeholders of the firm
- Discuss the legal forms of a retail organization that advices on the liabilities and debts applicable to a retailer

7.3 Designing a Retail Organization Structure

A well-defined, clear design of an organizational structure spells out the individual responsibilities and the chain of command followed by the business unit. It plays a crucial role for executing successful business plans. A retail organization structure helps in identifying the reporting relationships and decision-making authorities in a particular retail organization. It also describes the flow of information and communications in an organization. Thus, designing an organization structure is essential for ensuring the smooth functioning of a retail store. Before deciding on the structure, a retailer should define the objectives of the retail organization and identify the various organizational tasks that are required to achieve those objectives.

7.3.1 Defining Organizational Objectives

Organizational objectives are the important ends towards which an organization's and its employees' efforts are directed. A well-defined set of objectives would help a retailer answer the following questions: what is the retail store planning to achieve? How would the store achieve those ends? In which direction is the store heading? Apart from helping the retailer answer these questions, organizational objectives also set guidelines for developing a retail plan.

Generally, every retail organization has three levels of objectives (Refer Table 7.1):

- Strategic objectives
- Operational or administrative objectives
- Functional objectives

Table 7.1: Tasks Performed in a Retail Firm

Strategic Management Tasks	Develop a strategy, identify the target market, determine the retail format, and design organizational structure, select locations.
Merchandise Management Tasks	Buy merchandise – Locate vendors, evaluate vendors, negotiate with vendors, place orders. Control merchandise inventory – Develop merchandise budget plans, allocate merchandise to stores, and review open-to-buy and stock of position. Price merchandise – Set initial prices, adjust prices.
Store Management Tasks	Recruit, hire and train store personnel, plan work schedules, evaluate performance of store personnel, maintain store facilities, locate and display merchandise, sell merchandise to customers, repair and alter merchandise, provide services such as gift wrapping in delivery, handle customer complaints, take physical inventory, prevent inventory shrinkage.
Administrative Management (Operations) Tasks	Promote the firm, its merchandise and services – plan communication program, develop communication budget, select media, plan special promotions, design special displays, manage public relations.

Contd....

	Manage human resources – develop policies for managing store personnel, recruit, hire, train managers, plan career paths, keep employee records. Distribute merchandise – locate warehouse, receive merchandise, mark and label merchandise, store merchandise, ship merchandise to stores, return to merchandise to vendors. Establish financial control – provide timely information on financial performance, forecast sales, cash flow, profits, raise capital from investors, bill customers, provide credit.

Source: ICFAI Research Center

Strategic Objectives

The top managers of a retail organization formulate its strategic objectives. These managers have expertise in different fields: human resource management, finance, accounting, management information systems, distribution etc.

Operational Objectives (Administrative)

On the basis of the strategic objectives, middle level managers formulate the operational objectives of a retail store. These managers are called administrative/ operational managers.

The operations manager handles the merchandising and store management activities in a retail store. He implements the strategic plans of the organization with the help of the administrative staff.

Functional Objectives

Front line managers are responsible for achieving the functional objectives of a retail store. The functional objectives are task specific and are related to store functions like merchandising, sales, logistics etc.

Identifying Organizational Tasks

To achieve organizational objectives, a retail store has to entrust various tasks to its employees. Organizational tasks vary from one retail store to another.

Example: Takeya Delivers Exemplary Customer Service Objectives Through Smile Campaign

In 2020, Takeya, a comprehensive discount store in Tokyo, Japan launched the "Smile Campaign" to boost its exemplary customer service objective. The campaign targeted to make staff appear more customer friendly.

Contd….

The "Smile Campaign" goal was simple: to "deliver a smile through the masks." Amidst Covid times the masks were designed to aid employees to make people laugh and bring a little bit of joy to the store environment bringing customer delight.

Source: Zlotnick, R. (August 25, 2020). Japanese Store Employees Wear 'Smile Masks' to Make Them Seem Friendlier. Retrieved from https://www.distractify.com/p/japanese-store-smile-masks. Accessed on 07-07-2022

7.4 Principles of Retail Organization Design

Retail organizations should follow certain principles when designing the organization structure to avoid duplication of work and ambiguity in the line of authority. The organization structure developed around such principles (listed below) would clearly explain the functions and responsibilities of each employee in an organization.

Retail store management involves various tasks concerned with strategic management, merchandise management, store management, operations management and promotion management. Managers should use various principles to classify employees into groups and allocate the responsibility of completing tasks. Some of the principles that retailers use when designing a retail organization structure are

- Specialization and departmentalization
- Line of authority and responsibility
- Unity of command
- Span of control

Specialization and Departmentalization

Once a retail organization identifies the activities that are necessary to achieve its objectives, it must split those activities into specific tasks that can be performed by individual employees. This division of labor into small, specific tasks and the assignment of specific tasks to individual employees are called specialization. Job specialization allows individual employees to concentrate on a particular task. By specializing in some activities, employees can improve the quality and speed with which they serve the customer.

After assigning tasks to employees, a retail manager should group the tasks into small sets. Employees performing certain tasks can be grouped together into units or departments. Many retailers use departmentalization to enhance productivity. Some of the ways in which employees are divided into groups are discussed below:

Departmentalization by Function involves grouping of jobs that relate to the same organizational activity. For example, all employees performing tasks concerned with merchandise management are put in one department.

Departmentalization by Product involves grouping of jobs that relate to a particular product or service. A retailer may group employees into departments like apparel, home furnishing, footwear etc.

Departmentalization by location involves grouping of jobs that are performed in a geographic area. A chain store may consider each of its retail stores, warehouses etc. as separate departments.

Departmentalization by customer involves grouping of employees on the basis of the customers they serve.

Example: Pantaloons Leverages on Departmentalization to Host a New Shopping Experience

Pantaloons is a leading fashion retailer in India. In late 2020, Pantaloons decided to reposition itself as a "Progressive Style Partner". Visual Merchandising (VM) experts at the store played an important role highlighting 'what's hot'. New shopping experience is provided adding new cosmetics and lifestyle departments with new look and feel. Lifestyle department was added to provide for home needs products arranged by category.

Source: (March 17, 2021). Pantaloons – A New Experience for A Progressive Style Partner. Retrieved from https://mag.euroshop.de/en/2021/03/pantaloons-a-new-experience-for-a-progressive-style-partner/. Accessed on 08-07-2022

Authority and Responsibility

For the efficient functioning of the store, employees should be given the authority and responsibility to perform tasks without any assistance from senior officials. The store manager is responsible for maintaining service standards, while the sales manager is responsible for ensuring that customers receive prompt service. These managers can perform well only when they are given complete authority and responsibility to carry out their specific functions.

Store personnel working at various levels of the organization may share a 'Line relationship' or a 'Staff relationship'. Line relationships exist between employees working at various organizational levels. Here the manager has direct control over his immediate subordinates. Staff relationship is advisory in nature.

Unity of Command

According to the principle of unity of command, employees (in a retail organization) should be answerable to only one immediate superior for a particular task at any given point in time.

The efficiency of retail store employees decreases when they have to report to or follow the instructions of more than one supervisor. By implementing unity of command in a store, management can help employees perform better.

Span of Control

The efficiency with which a store supervisor/manager handles his subordinates decreases when the number of subordinates increases beyond a particular level. Hence, every retail organization should determine the optimal number of subordinates a manager can handle efficiently. The principle of span of control gives guidelines for determining the number of subordinates a superior should control, depending on his position within the organization and the nature of the tasks being performed by his subordinates. These guidelines are based on the following principles:

- Supervisor's span of control becomes narrow when employees' tasks are ambiguous and not standardized.
- Supervisor's span of control broadens when employees and the supervisor are competent.
- Manager's span of control increases when subordinates work at a single location.

7.5 Forms of Retail Organization

A retail store designs its organization structure in a way that ensures its smooth functioning. An appropriate organization structure is one that helps a retail organization understand and meet the requirements of its target market.

In a retail organization, the structure or design should be communicated to employees. An organizational chart can be used for this purpose. Organizational charts/maps help employees to understand the formal relationship between the various departments of the organization.

Prior to designing the organization structure, a retailer should decide on

- The number of hierarchical levels required in the organization for its successful and efficient operation.
- The classification of various tasks into different areas and the number of such areas required.

7.5.1 Levels of Organization

The number of levels in a retail organization equals the number of positions separating the highest official (CEO) from the lowest employee (sales personnel). Retail organizations adopt two types of organizational structures, flat organizational structure and tall organization structure.

Flat Organizational Structure

In a flat organizational structure, there are one or two management levels with a wide span of control. This type of organizational structure is commonly used by independent and small retailers to reduce operational costs. A flat organizational structure ensures speedy redressal of employee grievances. The number of employees reporting to a manager is higher compared to a tall organizational structure.

Vertical or Tall Organizational Structure

In a vertical structure, there are many organizational levels. This type of organizational structure is commonly found in department stores and chain stores. There are some drawbacks to a vertical organization structure. In a vertical organization structure, the rigid structure is the major drawback. In addition, there is no direct communication between managers and subordinates. The presence of many layers of management makes it difficult for an organization to take quick decisions regarding the provision of goods and services that meet the changing needs of the customers.

Example: Zappos Believes in Holacracy

Zappos.com is an online shoe and clothing retailer company based in United States. Zappos discarded traditional management hierarchy and adopted philosophy of "holacracy,". In holacracy the company is self-managed by every employee. There is a hierarchy but it's composed of a series of "circles," or teams. The focus in the structure is on the work and not on the role. Employees are encouraged to speak up their thoughts, insights and ideas about ways to do work.

Source: Corcoran, M. (June 30, 2020). What Zappos, Google, and Bridgewater Can Teach Us About the Importance of Speaking Up. Retrieved from https://neuroleadership.com/your-brain-at-work/zappos-google-bridgewater-teach-about-speaking-up/. Accessed on 08-07-2022

7.5.2 Organizing by Areas of Responsibility and Task

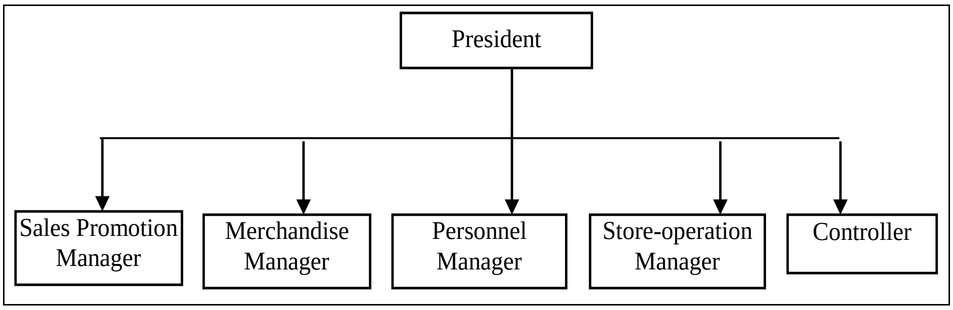
An organization can be structured according to the way in which tasks and responsibilities are assigned to employees. For designing an organization structure based on tasks and responsibilities, retailers can use one of the following approaches:

- Functional approach
- Geographic approach
- Product approach

Functional Approach

In this approach, jobs are grouped according to functional areas. The functional areas of a store are store operations, buying and selling of merchandise, promotional activities, recruitment and training of store personnel etc. Generally, small retailers use a two function (merchandising and store operations) organization structure. They add some more functions in the structure as the business grows. Figure 7.1 shows a functional organization chart.

Figure 7.1: Functional Organization Chart

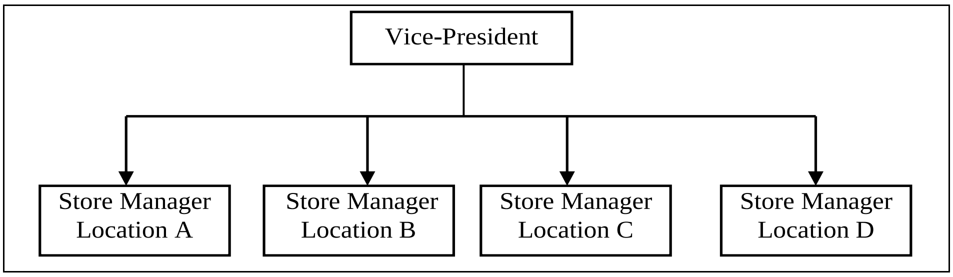


Sources: ICFAI Research Centre

Geographic Approach

In this approach, work is allocated on the basis of the geographical location of the organization. Chain stores use the geographic approach to allocate work to achieve economies of scale. Depending on the geographical location, the organization decides on the levels of hierarchy and the degree of specialization required for a particular store. Figure 7.2 depicts a geographic organization chart.

Figure 7.2: Geographic Organization Chart

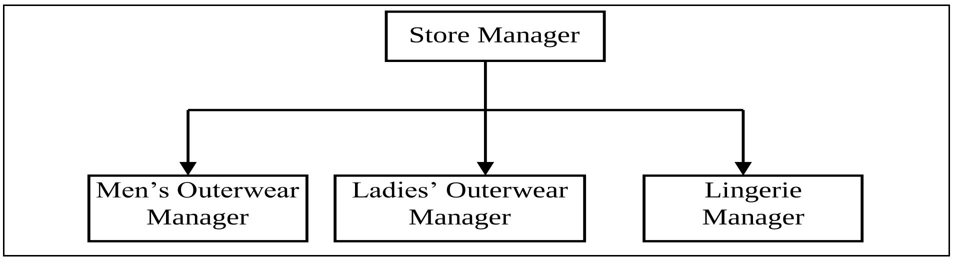


Sources: ICFAI Research Centre

Product Approach

In this approach, a retailer organizes the store according to the products he sells. This organization structure is designed to satisfy the needs of the customers buying these products. Figure 7.3 provides the product organization chart of an apparel-retailing store.

Figure 7.3: Product Organization Chart



Sources: ICFAI Research Centre

Activity 7.1
Take the instance of a well-known fashion store like Pantaloon and a departmental store like Big Bazaar. How is the departmentalization done in these stores and what is the difference in the departmentalization structures between the two? **Answer:**

Check Your Progress - 1

1. Generally, every retail organization has three levels of objectives. What are they?
   a. Strategic objectives, Operational or administrative objectives, & Functional objectives
   b. Strategic objectives, Operational or administrative objectives, & Personal objectives
   c. Operational objectives, administrative objectives, & Functional objectives
   d. Administrative objectives, Functional objectives, Organization objectives
   e. Strategic objectives, Corporate objectives & Functional objectives
2. Retail organizations follow certain principles when designing the organization structure to avoid duplication of work and ambiguity in the line of authority. Which of the following principles does the retailers use when designing a retail organization structure?
   a. Specialization and departmentalization
   b. Line of authority and responsibility
   c. Unity of command & Span of control
   d. Line of authority, responsibility and principal of scalar chain
   e. Specialization and departmentalization, Line of authority and responsibility, Unity of command & Span of control

3. Store personnel at various levels of the organization may share a 'Line relationship' or a 'Staff relationship'. In line relationships the manager has direct control over his immediate subordinates while staff relationship is ___.
   a. Competitive in nature
   b. Authoritative in nature
   c. Advisory in nature
   d. Cooperative in nature
   e. Informal in nature
4. The employees of an organization are answerable to only one immediate superior for a particular task at any given point in time. The organization is following which of the following principles?
   a. Unity of purpose
   b. Scalar chain principal
   c. Unity of direction
   d. Unity of command
   e. Unity of Authority
5. Which of the following features of a vertical organization help in bringing greater control?
   a. Many layers in the organization.
   b. Various levels of decision making.
   c. No communication between managers and subordinates.
   d. Communication between managers and subordinates.
   e. Timely supply of high quality materials to manage inventory.

7.6 Retail Organization Structures

An organization structure furnishes clarity and guidance to resolve both human resource issues and inter-departmental issues that may arise during the operation of the retail unit. Retailers can be classified into three major groups based on their size and nature: independent retailers, department stores and chain stores. Various retail organization structures used by different retailers are discussed below. Figure 7.4 and Figure 7.5 depict the organization structures of McDonald’s and B & G Metro respectively.

7.6.1 Independent Store Organizational Structure

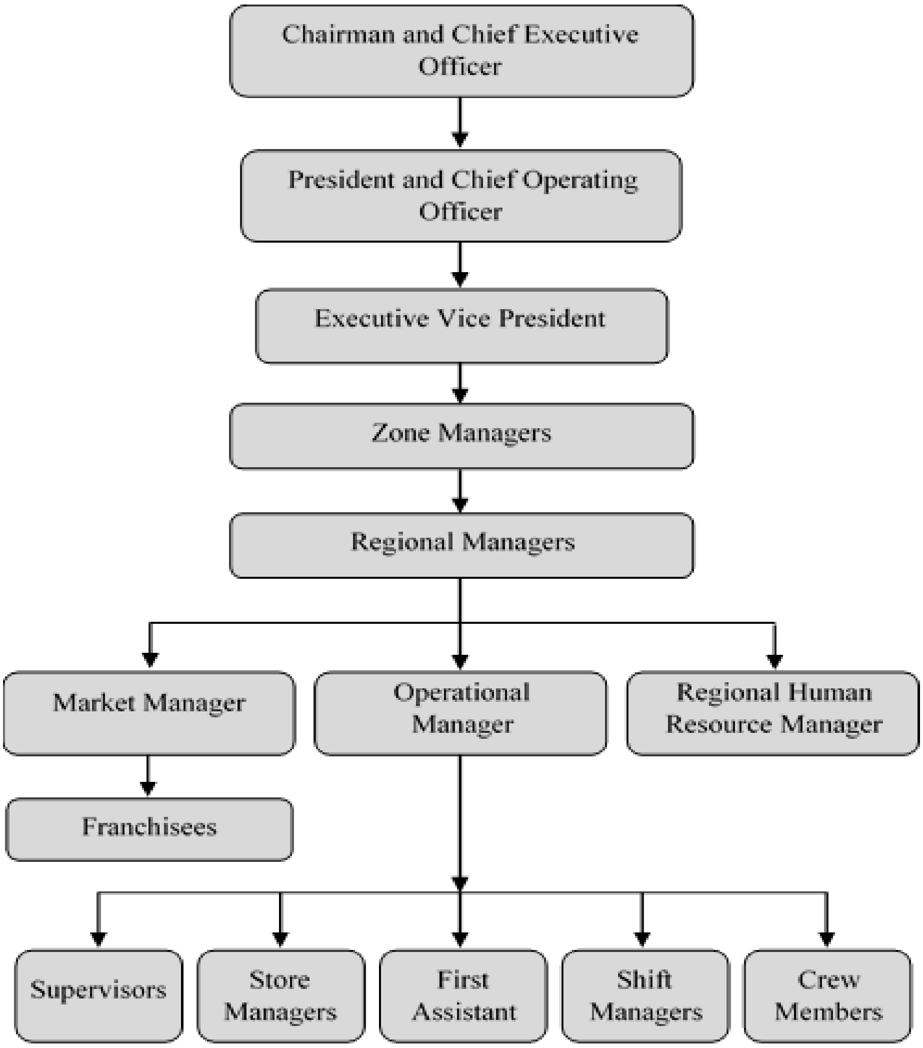
An independent retailer establishes a store with very few employees. All the activities of the retail store are managed by the owner himself.

As the store expands, the retail owner hires a few more employees. The coordination and control of the business is easy as the owner manager allocates the works to his employees and monitors them personally. As sales increase, the retailer (owner) hires supervisors who have specialized in the field of merchandising and operations. Even at this stage, critical store management activities like planning, execution and control are carried out entirely by the owner. He also controls the financial activities of the retail store.

The merchandise manager is responsible for developing, procuring, controlling, pricing, promoting and selling the merchandise in the store.

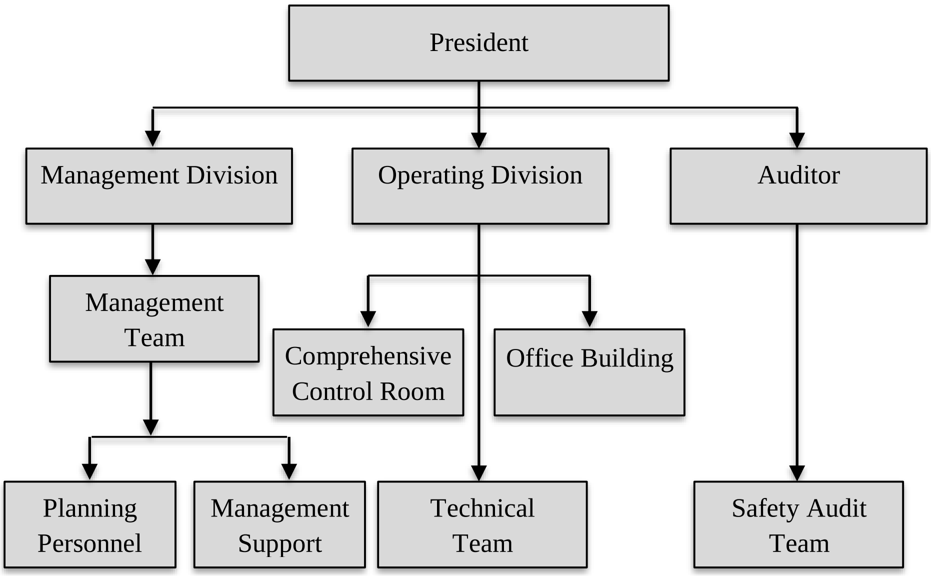
The operations manager is responsible for recruiting and supervising store personnel, planning information systems, designing and maintaining store facilities, and ensuring the store security.

Figure 7.4: A Typical Organizational Structure like McDonald's



Source: ICFAI Research Centre

Figure 7.5: Organizational Chart of B & G Metro



Source: ICFAI Research Center

7.6.2 Department Store Organizational Structure

Department stores have more complex and taller organizational structures than independent stores. Traditionally, department stores were family-owned businesses and the entire store was supervised by the family members. The organization structure and the executive positions in such stores were designed to accommodate the family members in the store. Gradually, with advances in technology and increase in competition, the organization structure of these stores changed. Most modern department store organization structures are inspired by the functional organization structure proposed by Paul Mazur in 1927. This organization structure is popularly known as the Mazur plan.

Mazur Plan

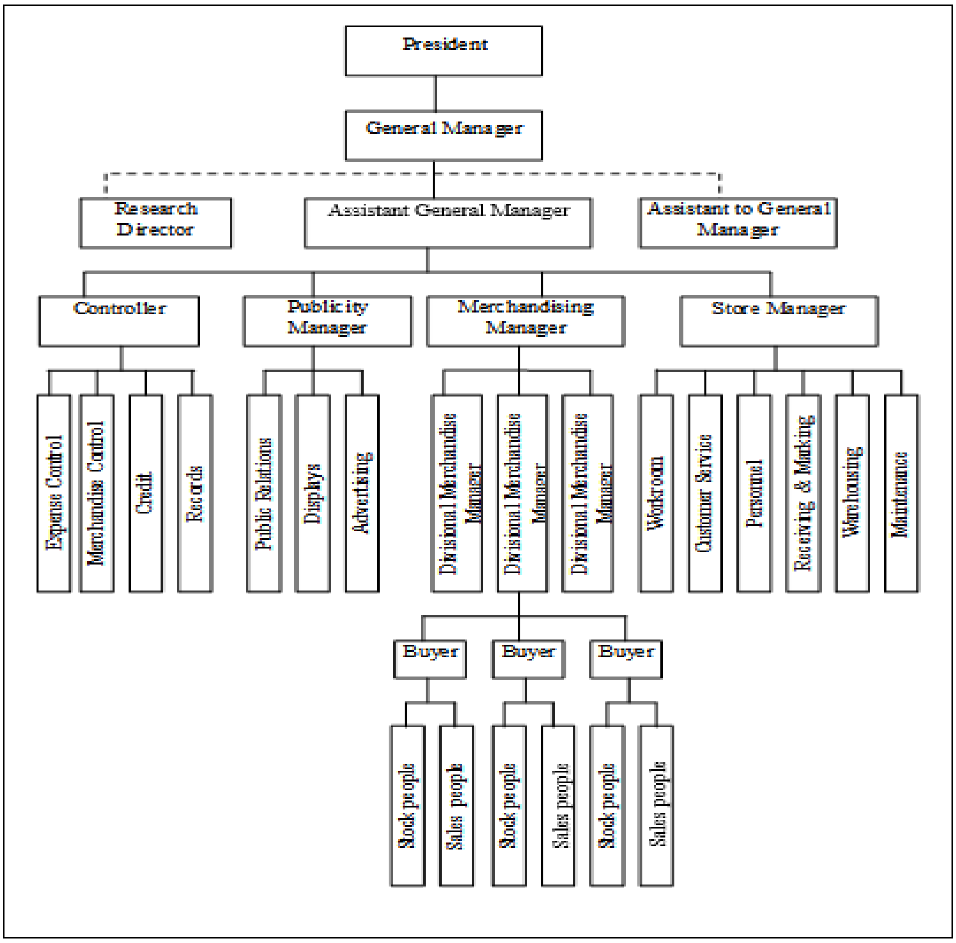
The Mazur plan divides all retail activities into four functional divisions/areas: finance (accounting and control), merchandising, promotion, and store operations (Figure 7.6 depicts a basic Mazur organization plan for department stores). Each division is handled by a manager. The responsibilities of the different managers are given below.

The finance manager is responsible for the efficient management of a firm's assets. He should also ensure adequate working capital for the smooth functioning of all the divisions in the retail store. The finance manager is also responsible for

- Designing and updating various accounting and control systems.
- Preparing budgets for physical inventory, merchandise and expenses of a retail organization.
- Preparing financial reports for the various stakeholders of the firm, like top management, government agencies and trade organizations

The merchandising manager supervises the buying and selling activities of the retail organization. He also has to ensure that quality, fashion, assortment, and pricing of merchandise are in line with the overall retail strategy of the firm. He has to coordinate all the activities of the retail organization e.g. regarding finance, promotion and operation.

Figure 7.6: Basic Mazur Organization Plan for Department Store



Adapted from Paul Mazur, "Principles of Organization Applied to Modern Retailing", New York: Harper & Brothers, 1927

The general merchandising division plays a central role in a retail organization as it carries out activities that are aimed at satisfying the customer.

The promotion manager is responsible for all the promotional activities of a retail organization. These activities include advertising, sales promotions, interior and window displays, public relations and publicity. He is also responsible for collecting feedback from customers and passing it on to the marketing wing, which handles advertising for the retailer.

The physical operation of a retail store comes under the jurisdiction of the retail operations manager. He is responsible for the development and maintenance of facilities; customer service and assistance; credit and collections, procuring, checking, marking and stocking of incoming merchandise; store security and general store keeping. Sometimes an operations manager acts as a proxy personnel manager, handling activities like recruitment and training and evaluation of store personnel.

Modifications to the Mazur Plan

Even though many retailers used the Mazur plan to design their organizational structures, they believed that it had some shortcomings. With the increase in the scale and complexity of retail store operations and the evolution of independent stores into chain stores, retailers felt that the Mazur plan required some modification. Consequently, two types of modifications were made:

- Functional Modifications
- Geographic Modifications

Functional modifications to the Mazur plan changed the number of functional divisions. In the modified Mazur plan, an additional functional division was added to the existing four divisions. The new functional division could be personnel division or distribution or real estate and construction or catalog operations. Further, the buying and selling functions (which were earlier handled by the general merchandise manager) were separated. The reasons in favor of separation of the buying and selling functions are given below:

- The skills, talents and training required for buying and selling are very different. Salespersons should have good communication skills whereas merchandise buyers should have good bargaining skills to succeed in their respective fields.
- Buying activities take more time than selling activities. If one person were handling both functions, he would be away from the store for a long time. Moreover, if he focuses on buying activities, he will not be able to spend sufficient time on selling activities.
- Efficient handling of consumer feedback takes time and requires the manager’s undivided attention. The store manager who is involved in many other activities cannot do justice to any single activity. The general merchandise manager who plays the roles of buyer, salesperson, and customer care executive cannot do justice to any of these roles.
- Flexibility decreases when a single person handles all the buying and selling functions and responds to consumer feedback. Efficiency and flexibility increases more when these functions are divided between two persons.
- The arrangement of merchandise in the store should facilitate the selling function.

Although many retailers favor the separation of the buying and selling functions, a few experts oppose this separation. Some of the arguments that support the clubbing of the buying and selling functions are given below:

- To understand customers better, the buyer should also handle the selling function. In other words, a single person should handle both the buying and selling activities in a retail store.
- If a single person handles both the buying and selling of products, customer satisfaction will increase. This is because the buyer would procure merchandise on the basis of firsthand information about the tastes and needs of customers.
- Performance evaluation of various departments will be simplified if the buying and selling functions are carried out by the same person.
- The bundling of buying and selling functions would eliminate the conflicts that arise between the selling and buying personnel when both the functions are separated.

Geographic modifications to the Mazur plan became necessary with the increase in the scale of retail operations of department stores and the establishment of outlets in different geographic locations. Retailers had to modify their organization structure to cater to requirements of stores operating in different locations. The Mazur plan can be modified based on one of the following approaches:

- Main store approach
- Separate store approach
- Equal store approach

The relevance of geographic modifications increases with the growth of retail organizations.

Main store approach: In this approach, the main store or the parent organization controls the operation of the branches. Functions like merchandise buying, promotion, personnel management, and operations are carried out by the same managers in the main store for all the branches. These managers operate from the main store. For example, in the main store, the store activities are handled by four divisional heads – the finance manager, the general merchandise manager, the promotion manager and the operation manager. These same managers will control the activities in the branches also.

The managers at the parent organization (main store) are responsible for all the activities in the branches. In the branch stores, sales activities are looked after by the branch sales manager, who reports to the sales manager at the main store. In the main store approach, branch stores are regarded as sales divisions of the main store.

This type of approach for designing the organization structure of a department store is advisable only

- When it is in the initial stages of growth
- When the markets in which these stores operate are similar and when all the stores sell the same range of merchandise
- When the branches are located close to the main store. The geographical distance between the parent and the branch stores should be such that the management and the supporting staff can access and supervise the branch stores easily

Separate store approach: In this approach, each branch is treated as an independent operation within the organizational structure. In other words, there is no main store that controls the operations of the branches. All the functions (merchandising, finance and operational activities) are carried out separately by each branch.

The separate store approach is adopted by department stores only

- When there are many branches, say five or more
- When the size of all the stores is almost the same

Advantages

The separate store approach has the following advantages:

- Every store in the retail organization has a greater degree of freedom over its operation
- The stores can offer customized products as each store can take its own decisions

Disadvantages

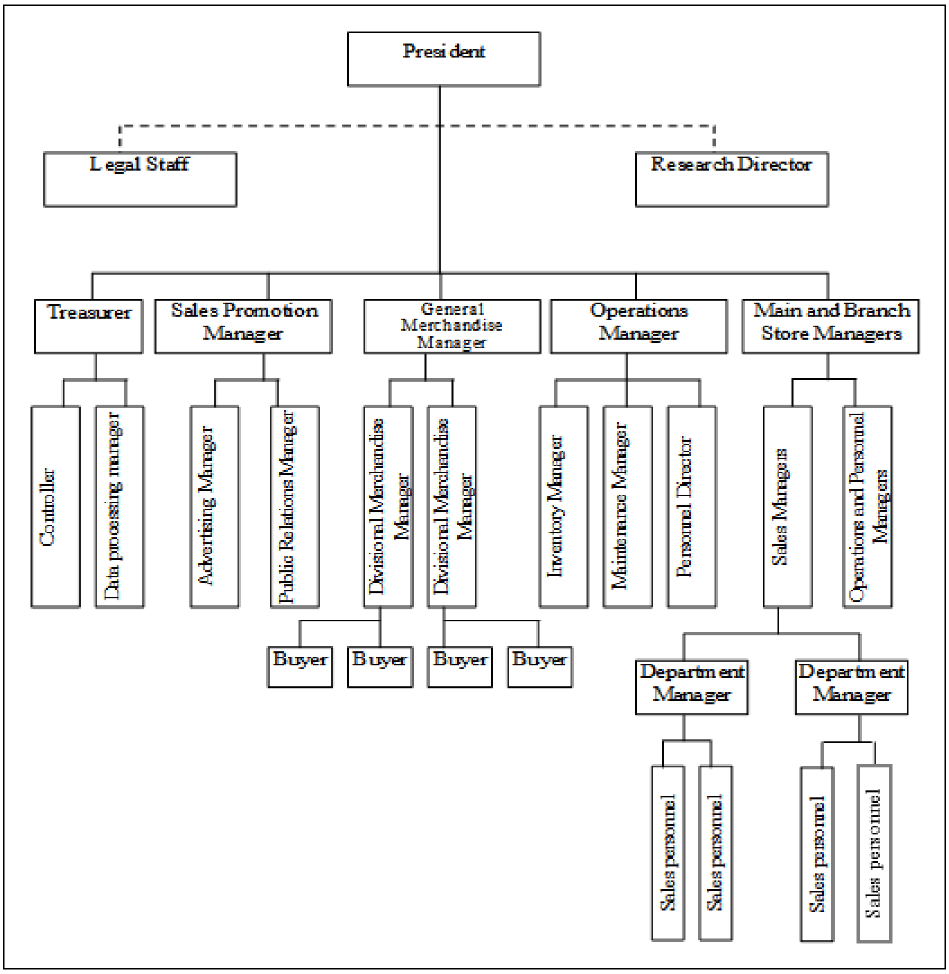
The disadvantages of the separate store approach are listed below:

- Diseconomies of scale in buying arise because each store has to buy its own merchandise and other supplies
- Increase in operational costs due to employment of more people in each department
- Difficulty in maintaining a consistent image across all branches
- Difficulty in achieving coordination between the stores

The main store approach is not responsive to local needs, but the separate store approach is costly and difficult to manage. Therefore, a new approach, called the equal store approach, was developed.

Equal store approach: In the equal store approach, all the managerial functions are centralized and controlled by headquarters. Managerial functions like finance, merchandising, promotion and operations, are directly controlled by headquarters for all the branches. Figure 7.7 depicts an equal store organization structure used by many chain stores. This approach has two unique features:

Figure 7.7: Equal Store Organizational Format (used by chain stores)



Source: Extracted and adapted from Berman Evans, "Retail Management: A Strategic Approach", Chapter 11, 13th Edition, 2017.

Separation of buying and selling activities: Under the Mazur plan, both functions are handled by the general merchandise manager. But, in this approach, the merchandise manager handles the buying function alone. The selling activities are decentralized and carried out by managers at individual stores.

Equal treatment: All stores (branches and main store) are treated equally as basic sales units of the retail organization.

Thus, the equal store approach has the advantages of both the main store and the separate store approach. Centralized buying generates economies of scale while the separation of functions allows individual stores to cater to the needs of the individual target markets.

7.6.3 Chain Store Organizational Structure

The size, geographic spread, local markets, product mix and operating mix vary from store to store in a retail chain store organization. Three factors have an impact on the organization structure of a chain store organization:

- Centralization
- Specialization
- Standardization

Centralization refers to the degree to which authority for taking retailing decisions is delegated to corporate managers rather than to geographically dispersed regional, district, and store managers. A retail organization is said to be centralized when all policies and decisions regarding the operating and merchandising activities of its constituents are taken by headquarters or the home office.

Many chain stores adopt centralized decision making to keep transaction and overhead costs low. Some chain stores found that increased centralization could lead to slower decision making. Therefore, these stores explored various ways to achieve a balance between centralization and the need to meet local needs.

Walgreens, the retailer giant from the US has a strategy of focusing on giving a great customer experience rather than concentrating on the location as the only way to satisfy their customers.

Specialization differentiates chain store organizations from other store formats. Chain stores group tasks into a number of specialized functions, which are greater in number than those specified in the basic Mazur plan. Specialized store functions include distribution, marketing, real estate and construction, personnel and industrial relations along with the four basic functional divisions finance, merchandising, operations and promotion.

A high degree of **standardization** for merchandising and operations is another special feature of chain store organizations. Standardization, in the case of chain stores, refers to the consistency of the merchandising and operating procedures practiced by geographically dispersed retail stores. Chain stores have effective monitoring and control systems for gathering information to achieve standardization. Chain stores use standardization as a tool to convey a consistent image.

Example: IKEA's Standardized Stores

IKEA organizes its retail outlet by a "maze-like" structure. It offers store designed to put customer's emotions and senses into overdrive. IKEA's store layout is a "fixed path" design.

Contd…

This design has a particular path for customers to follow and leads in one direction within the store. In most of the stores, customers get to explore only about 33% of the merchandise on offer. The fixed path approach ensures that customers explore most of the products and also stay longer at the store.

Source: Clinehens, J. (January 2, 2021). The Gruen Effect: How IKEA's Store Design Makes You Buy More. Retrieved from https://medium.com/choice-hacking/the-gruen-effect-how-ikeas-store-design-makes-you-buy-more-27316f330385. Accessed on 08-07-2022.

7.7 Legal Forms of Retail Organization

The ownership of a business depends on the size of the business, requirement of capital and the methods used for protecting the owners from liabilities. As the organization grows, the form of ownership also changes. Legally, there are three types of ownership:

- Sole proprietorship
- Partnership
- Corporation

Sole proprietorship

Sole proprietorship is a common and simple form of ownership. In this type of ownership, the store is completely owned by a single person.

There are no formal legal requirements to set up a sole proprietorship firm. Only a license is required from the local jurisdiction (like municipal corporation or health department). A person starting a store using this method need not fulfill any other legal formalities other than complying with the laws governing the type of business the person is setting up. This method thus allows a retailer to set up a retail organization quickly with minimum costs. Here, the owner has the complete authority in decision-making and is entitled to all the profits from the retail operations. Many Kirana stores in India are sole proprietary business entities.

Partnership

When two or more persons come together to start a business, based on the agreement mutually agreed upon between the partners, then the business is called a Partnership. Here, all partners take part in decision-making. They share the profits on the basis of the agreement made at the time of formation of the store. But the Partnership Income Tax is paid by the Partnership.

There are two types of partnerships- general partnership and limited partnership. In a general partnership, all partners have equal authority and responsibility for the management of the business; and so on the liability of partnership debts. In a limited partnership, more than one member may finance the business, but only a few members will manage the operations of the retail store. Those who are not part of managing the operations, generally, are also not accountable on the liability of partnership debts.

Example: Hero and Cholamandalam Partnership for Electric Vehicle Sale

Hero Electric in May, 2022 partnered with Cholamandalam, an Investment and Finance Company to offer retail finance for sales of its two-wheelers electric vehicles. The partnership will provide an opportunity for Hero to harness on the widespread network of Chola present across the country.

Source: (May 30, 2022). Hero Electric partners with Cholamandalam to offer retail finance. Retrieved from https://www.thehindubusinessline.com/companies/hero-electric-partners-with-cholamandalam-to-offer-retail-finance/article65475480.ece. Accessed on 08-07-2022

Corporation

It is a legal business entity authorized by the law to operate as a single person, even though it may consist of a number of stakeholders.

An individual or a group can select any of the above ownership patterns for starting a retail organization. The ownership pattern should be selected based on various factors like the scale of operations, desired level of risk and liabilities, capital, and skills required to manage the retail organization. In general, a Corporation enjoys tax advantages as the income and profits earned can be distributed between the corporation and the owner (if a Corporation is formed by Sole Proprietorship) / owners (if a Corporation is formed by Small Business Partnerships).

Activity 7.2

Give two examples of retail stores that have effectively used Vertical Integration to have greater control over product, demand, and information flows in the organization.

<u>Check Your Progress - 2</u>

6. Which of the following is a plan which divides all retail activities into four functional divisions/areas i.e. finance (accounting and control), merchandising, promotion, and store operations?
   a. Organizational plan
   b. Mazur Plan
   c. Bohra Plan
   d. Mazur Plan
   e. Retail Organizational plan

7. The ownership of a business depends on the size of the business, requirement of capital and the methods used for protecting the owners from liabilities. Legally, there are three types of ownership in a business. What are they?
   a. Sole proprietorship, Partnership, Corporation
   b. Sole proprietorship, Partnership and Cooperation
   c. Sole partnership, Partnership, Corporation
   d. Sole proprietorship, Partnership, Cooptation
   e. Proprietorship, Partnership, Corporation
8. Which of the following term denotes when two or more persons come together to start a business, without incorporating it?
   a. Joint venture
   b. Corporation
   c. Partnering
   d. Partnership
   e. Business deal
9. With the increase in the scale and complexity of retail store operations and the evolution of independent stores into chain stores, retailers felt that the Mazur plan required some modification. Consequently two types of modifications were made. What are they?
   a. Functional Modifications & Geographic Modifications
   b. Functional Modifications & Operational modification
   c. Functional Modifications and Organizational modification
   d. Organizational modification and operational modification
   e. Organizational modification and Demographical modification
10. Which of the following is called as a legal business entity authorized by the law to operate as a single person, even though it may consist of a number of stakeholders?
   a. Cooptation
   b. Corporation
   c. Sole proprietorship
   d. Sole Ownership
   e. Ownership

7.8 Summary

- An organization is a formal structure of roles and positions put in place to achieve some specific goals
- The structure of a retail organization defines the role of employees and the way in which the organization functions. This unit discussed the steps involved in designing an appropriate retail organization structure to enhance a store's ability to serve its target markets
- To design an effective retail organization structure, managers/ owners must define store objectives, identify the tasks, classify the tasks and jobs; and assign responsibilities and authority to various positions, and define the relation between them
- Organizations can have flat structures or vertical (tall) structures. A flat organization structure has only one or two levels of management, whereas a vertical organization has more than two levels of management
- Independent stores, department stores and chain stores use different organization structures to facilitate their operations
- Department stores use the basic Mazur plan with some modifications to design their organization structure. This chapter also described various forms of ownership like sole proprietorship, partnership and corporation

7.9 Glossary

Centralization: It refers to the degree to which authority for taking retailing decisions is delegated to corporate managers rather than to geographically dispersed regional, district, and store managers.

Corporation: It is a legal business entity authorized by the law to operate as a single person, even though it may consist of a number of stakeholders.

Flat Organizational Structure: In a flat organizational structure, there are one or two management levels with a wide span of control.

Functional Objectives: They are task-specific objectives formulated by Front Line Managers.

Mazur Plan: The Mazur plan divides all retail activities into four functional divisions/areas: finance (accounting and control), merchandising, promotion, and store operations.

Operational Objectives: They are strategic objectives formulated by middle-level Managers.

Sole Proprietorship: In this type of ownership, the store is completely owned by a single person.

Span of Control: The principle of span of control gives guidelines for determining the number of subordinates a superior should control, depending on his position within the organization and the nature of the tasks being performed by his subordinates.

Tall Organizational Structure: In this form of retail organization, there are multiple levels of organization.

Unity of Command: An employee (in a retail organization) should be answerable to only one immediate superior for a particular task at any given point in time.

7.10 Self-Assessment Test

1. What are the various tasks performed by a retail organization? Explain.
2. A retail organization has three levels of objectives. Elucidate these levels of objectives.
3. What are the various principles that retailer uses when designing a retail organizational structure?
4. Explain the term unity of command and span of control.
5. Explain different types of retail ownership.

7.11 Suggested Readings/Reference Material

1. Giri Arunangshu and Chatterjee Satakshi, “Retail Management: Text & Cases” Paperback, PHI Learning Pvt. Ltd., 2021.
2. Swapna Pradhan, “Retailing Management: Text and Cases”, McGraw Hill, Sixth Edition, 2020.
3. Barry Berman, Joel R Evans, Patrali Chatterjee and Ritu Srivastava, “Retail Management”, Thirteenth Edition Pearson Education, 2017.
4. Gibson G. Vedamani, "Retail Management”, 5th edition, Pearson Education, 2017.

7.12 Answers to Check Your Progress Questions

1. (a) Strategic objectives, Operational or administrative objectives, & Functional objectives

Generally, every retail organization has three levels of objectives. These levels are Strategic objectives, Operational or administrative objectives, & Functional objectives.

2. (e) Specialization and departmentalization, Line of authority and responsibility, Unity of command & Span of control

Retail organizations follow certain principles when designing the organization structure to avoid duplication of work and ambiguity in the line of authority. Principles that retailers use when designing a retail organization structure are: Specialization and departmentalization, Line of authority and responsibility, Unity of command & Span of control.

3. (c) **Advisory in nature**

Store personnel working at various levels of the organization share a 'Line relationship' or a 'Staff relationship'. In line relationships, the manager has direct control over his immediate subordinates while staff relationship is advisory in nature.

4. (d) **Unity of command**

According to the principle of unity of command, employees (in a retail organization) should be answerable to only one immediate superior for a particular task at any given point in time.

5. (e) **Timely supply of high quality materials to manage inventory**.

In vertical structure there are many organizational levels. In a vertical organization structure, the rigid structure is the major drawback. This results in no direct communication between managers and subordinates. It makes difficult for an organization to take quick decisions. However, there can be greater quality and inventory control and this is a big advantage.

6. (b) **Mazur Plan**

The Mazur plan divides all retail activities into four functional divisions/areas: finance (accounting and control), merchandising, promotion, and store operations. Each division is handled by a manager.

7. (a) **Sole proprietorship, Partnership, and Corporation**

Legally, there are three types of ownership: Sole proprietorship, Partnership, and Corporation.

8. (d) **Partnership**

When two or more persons come together to start a business, without incorporating it, the business is called a partnership.

9. (a) **Functional Modifications & Geographic Modifications**

With the increase in the scale and complexity of retail store operations and the evolution of independent stores into chain stores, retailers felt that the Mazur plan required some modification. Consequently, two types of modifications were made: These modifications are Functional Modifications & Geographic Modifications.

10. (b) **Corporation**

Corporation is a legal business entity authorized by the law to operate as a single person, even though it may consist of a number of stakeholders.

Retail Management

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