

ATKearney

On Solid Ground: Brick-and-Mortar Is the Foundation of Omnichannel Retailing



ATKearney

Executive Summary

Digital retailing is capturing headlines and inspiring spirited debate as retailers plan how best to invest for future success. But beyond the headlines, physical stores remain the foundation of retailing, evidenced by the fact that 90 percent of all retail sales are transacted in stores and 95 percent of all retail sales are captured by retailers with a brick-and-mortar presence.

According to the Omnichannel Shopping Preferences Study—the latest addition to A.T. Kearney’s ongoing study of the evolution of omnichannel commerce—physical stores are clearly customers’ preferred shopping channel and a place where the most significant consumer and retailer value continues, and will continue, to be created.

It is important to acknowledge that shoppers actually find physical stores appealing—especially when we read all the hype about online and digital. Stores provide consumers with a sensory experience that allows them to touch and feel products, immerse in brand experiences, and engage with sales associates who provide tips and reaffirm shopper enthusiasm for their new purchases.

The store plays a crucial role in online purchases, as two-thirds of customers purchasing online use a physical store before or after the transaction. In these cases, the store makes a significant contribution to converting the sale, even though the transaction is eventually registered online. In other words, the source of value creation (brand building, product awareness) is distinct—or decoupled—from the place of value capture (sales transaction). This is particularly important for retailers, as they consider resource allocation decisions across channels to ensure that the true value the physical store creates is accounted for properly.

The future of retail is solidly anchored in the brick-and-mortar channel. With customer satisfaction at the core of retailing, successful retailers will do their part to provide consumers with the ability to shop when and where they want. And it’s been proven that having multiple channels is good for business.

The debate should not be a question of digital or physical. Successful retailers understand how each customer touch point adds value (as defined by the customer) and develop omnichannel strategies—with stores as the foundation—that maximize customer satisfaction and profitability.

Key Facts and Figures

95 percent of all retail sales are captured by retailers with a brick-and-mortar presence

Two-thirds of consumers who purchase online use the store before or after the transaction

The value of stores for customers and retailers is far greater than the sales that are captured within them

Physical stores help retailers drive online sales

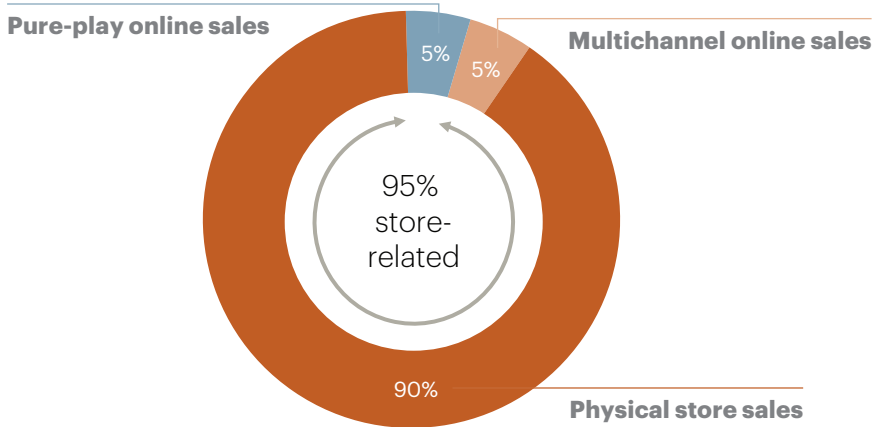
It’s not physical or digital; it’s physical with digital. Having multiple channels is good for business

Introduction: The View from the Store

In what some believe to be an era where high technology holds almost all the answers for retailing, physical stores are quietly evolving through the integration of digital innovations, ultimately vying to offer consumers a true omnichannel retail environment.

However, while innovation is always exciting, it is important to remember that today 90 percent of all U.S. retail sales still occur within the four walls of a physical store (see figure 1). And, even in this day and age of smartphones, social media, and same-day delivery, retailers with a brick-and-mortar presence collectively sell more on their websites than pure online players. Why? Because shopping is a journey, whether online or in the real world.

Figure 1
Total U.S. retail sales (2013)



Source: A.T. Kearney analysis

The Shopping Journey

Every product purchase can be seen as a shopping journey, beginning with product discovery and leading to trial and test, purchase, delivery or pickup, and, in some cases, to returns. Participants in the study were asked to report their preferences across each stage of this journey (see sidebar: About the Study on page 3).

Consumers select channels based on a broad range of criteria, from physical convenience to brand loyalty to the desire to be entertained or surprised. As a result, how and where consumer value is created and captured depends on the consumer's preferences. However, irrespective of who the consumer is and what she or he is buying, the study finds that physical stores remain the cornerstone of the consumer's shopping journey.

Think of a consumer who goes to a store to learn about or try a product and then decides to purchase it through the retailer's website. Now imagine another who learns about that same product through online reviews, and goes to the store to check dimensions and purchase it. In the first example, the consumer's experience in the physical store is integral to winning the

About the Study

The importance of traditional retailing is reinforced by A.T. Kearney's Omnichannel Shopping Preferences Study, which asked more than 2,500 U.S. shoppers about their shopping preferences and behaviors. The research protocol used the following birth year segmentation as the foundation for its cohort analysis. Teens: 1995–2001; millennials: 1980–1994; generation X: 1965–1979; baby

boomers: 1950–1964; seniors: born before 1950. As part of the research protocol each respondent was allowed to provide input for multiple categories; categories included in this study are apparel and accessories, health and beauty, furniture, jewelry, computer and electronics, and sporting goods. This report summarizes the findings of the study, input from a variety of retailers and property

developers, and A.T. Kearney retail sector analysis.

The Omnichannel Consumer Preferences Study is the newest in our series of breakthrough research in retail innovation. This independent survey of consumers and retail executives was funded by, and completed in cooperation with, leading U.S. shopping mall real estate developers.

purchase, thus creating value during the first two stages in the shopping journey. In the second case, the store plays a role in both creating and capturing value.

The emergence of multiple channels has introduced—more dramatically than at any other time in the history of retailing—a decoupling of the source of value creation from where value is captured, with crucial implications for all omnichannel retailers.

Decoupling Value Creation from Value Capture

Value is created at multiple steps along the customer's shopping journey as the decision to make a specific purchase is informed, supported, and reinforced. Value is captured when the purchase is tendered. Put another way, value creation is a precondition to value capture. If the shopper isn't convinced a transaction has sufficient value, she or he will not make a purchase.

While value can be captured through both physical and digital channels, the study finds that most consumers prefer engaging with physical stores irrespective of where the final value capture takes place. In two-thirds of the instances when consumers indicate a preference for online purchases they still rely on physical stores for other important steps in their shopping journey—an example of the decoupling of value between channels. Perhaps not surprisingly, this preference for stores is even more pronounced for high touch-and-feel categories, such as apparel and accessories: the physical store is involved at various stages along the shopping journey in 71 percent of online sales. The same percentage also applies to more standardized categories, such as consumer electronics. The research supports the scope of this decoupling effect and demonstrates how and why sales are becoming increasingly channel-agnostic.

The decoupling phenomenon requires that successful retailers develop effective value creation and capture tracking technologies and systems to track shopper engagement beyond "sales." Without such systems in place it may be too easy for some retailers to begin to downplay the contribution their physical stores make toward a successful shopping journey. As retailers develop the ability to better track the value created and captured by their physical stores, the power for focusing in-store investments that drive additional benefits for the retailer and its consumers will be more apparent.

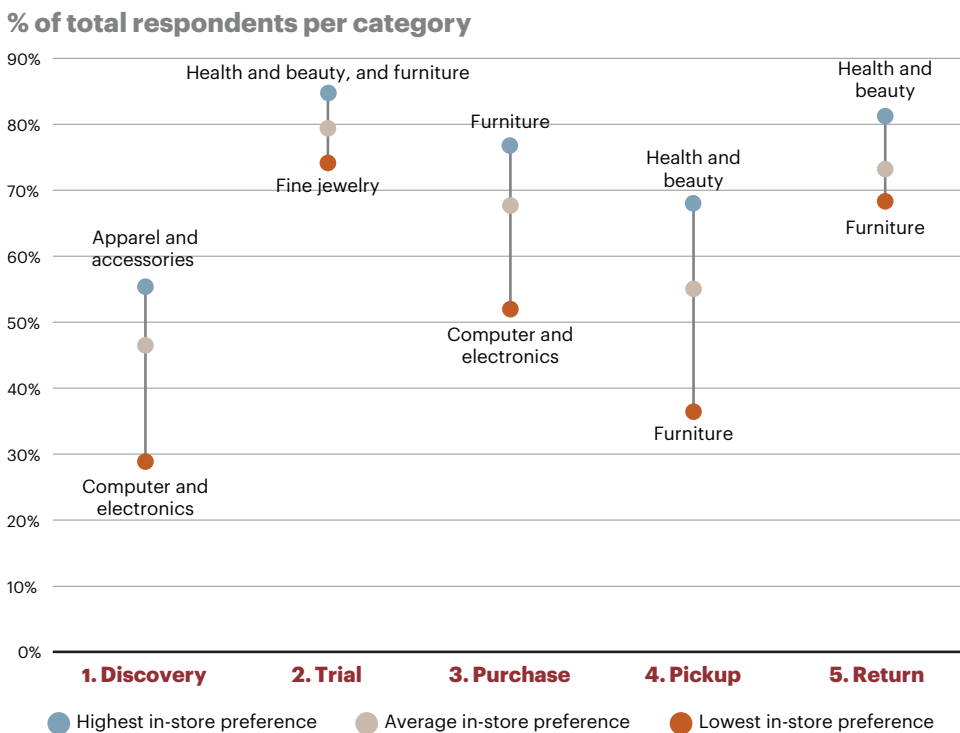
Brick-and-Mortar Is the Future of Modern Retail

While most consumers shop multiple channels, their channel preferences vary by age, purchase category, and stage in the shopping journey. Consumers differ sometimes significantly. But when they explain their channel choices, they consistently state the importance of convenience, which is supported by the immediacy stores provide to consumers.

By examining each step of the shopping journey, retailers can see how channel preference differs by category and demographic cohort, and understand why developing an integrated omnichannel experience is pivotal to retail success.

To better understand how this works, let's look at the five steps of the shopping experience (see figure 2).

Figure 2
In-store channel preference by step in the shopping journey



Note: For survey question "Do you prefer to [INSERT STAGE] [INSERT CATEGORY] online or in a physical store?" n = 2,504 respondents and r = 8,518 journeys
 Source: A.T. Kearney Omnichannel Shopping Preferences Study, 2014

1. Discovery

Discovery is the only stage along the transactional journey where shoppers prefer online for a select few categories. However, the majority of consumers prefer in-store discovery for key retail categories such as apparel and accessories, health and beauty, and furniture.

For these categories, in addition to convenience, consumers identify stores as the preferred destination for exploring new products with a broad selection of choices.

2. Trial and test

When it comes to product trial and test, respondents indicate a clear preference for physical stores.

For high touch-and-feel categories including apparel and accessories, health and beauty, and furniture, respondent preference for in-store trial and testing is as high as 85 percent. Even for standardized categories such as consumer electronics, trial and test preferences are in the 76 percent range—shoppers don't really know the difference between LCD and LED; they choose what looks better to them. Immediacy, ease, and accuracy of testing are all cited as reasons for preferring in-store trial.

3. Purchase

A.T. Kearney finds that when it comes down to making a purchase, stores are preferred in the majority of cases.

For purchase, consumers find that stores offer immediacy and accessibility that cannot be replicated through other means. For categories such as fine jewelry, electronics, furniture, and sporting goods, consumers additionally value stores for their better customer service, which they believe is not available online.

In-store pickups offer a sense of reliability and trust that consumers don't find online.

4. Delivery or pickup

The study establishes that, overall, consumers prefer in-store pickup over home delivery, but preferences vary by category. Of all the categories, in-store pickup is most popular for health and beauty and fine jewelry products. In-person, in-store pickups exclusively offer a sense of reliability and trust that consumers don't find online and through home delivery, in addition to the obvious benefit of being able to take goods home immediately.

5. Returns

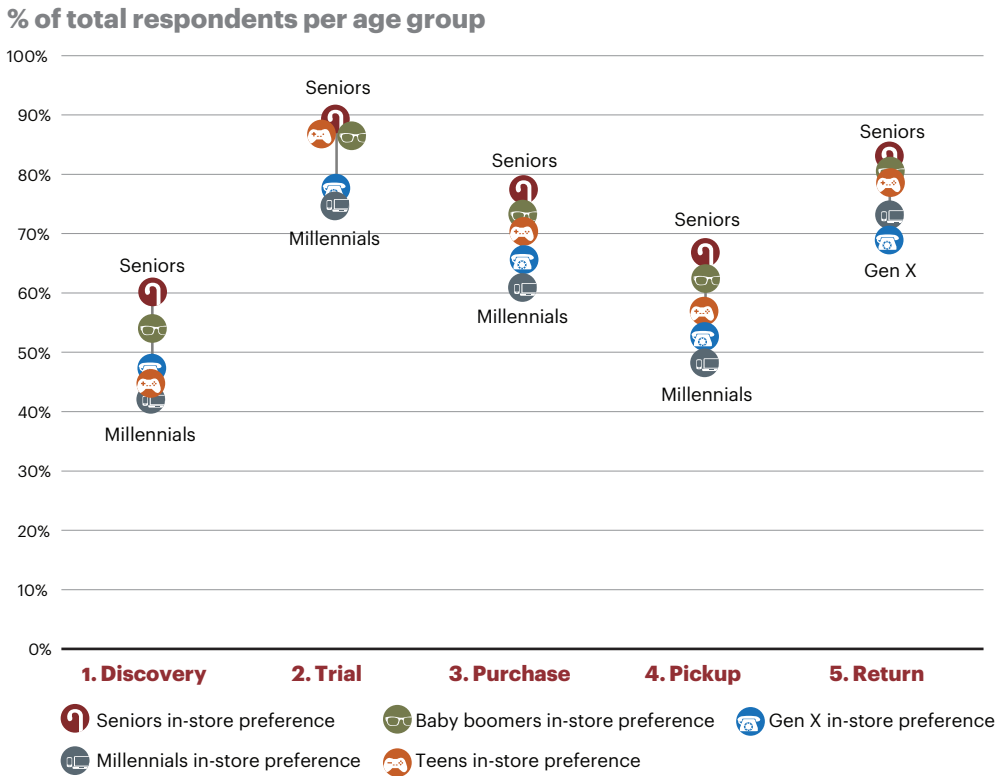
Across all product categories, physical stores are vital centers for product returns, even for purchases made online. In fact, after trial and testing, returns is the stage in the shopping journey where consumers demonstrate the highest preference for physical stores over online shopping. This clear preference for in-store returns is a product of the desire for accessibility, immediacy, and time efficiency, which translates to a behavioral pattern of returning products to the nearest store. And this is great news for physical retailers. For online pure-plays, returns are a dead-net cost; for a brick-and-mortar store, a return is a potential new sale.

The respondents seem to be saying that a retail channel's unique characteristics determine which role it does—or can—play along their individual shopping journey. But other factors, including demographics, also shape preferences.

Generational Poles and Parallels

Regardless of age, stores are generally preferred across the shopping journey, although where and how consumers interact with stores differs by age group (see figure 3).

Figure 3
In-store channel preference by step in the shopping journey



Note: For survey question “Do you prefer to [INSERT STAGE] [INSERT CATEGORY] online or in a physical store?” n = 2,504 respondents and r = 8,518 journeys
 Source: A.T. Kearney Omnichannel Shopping Preferences Study, 2014

Interestingly, teens’ overall preference for physical stores is one of the highest, and greater even than that of millennials and generation Xers. This is a critical fact for retailers and other branders eager to engage customers early in their lives in hopes of building lifelong relationships. Meeting teens where they prefer to shop requires a trip to a physical store.

More than any other age group, millennials prefer using multiple retail channels, be they digital or physical. And when they visit a physical location, their preference is for trips designed to accomplish multiple goals. Nonetheless, the majority of millennial customers prefer stores for trial and test, purchase, and returns.

Across all categories, seniors prefer physical stores to online shopping. Baby boomers’ channel preferences are more closely aligned with those of seniors, with a demonstrably higher preference for brick-and-mortar stores. Boomers and generation Xers cite a variety of pragmatic reasons for preferring shopping in the physical channel, from accessibility and time efficiency to better product selection.

The Bottom Line: It's Not Physical or Digital— It's Physical with Digital

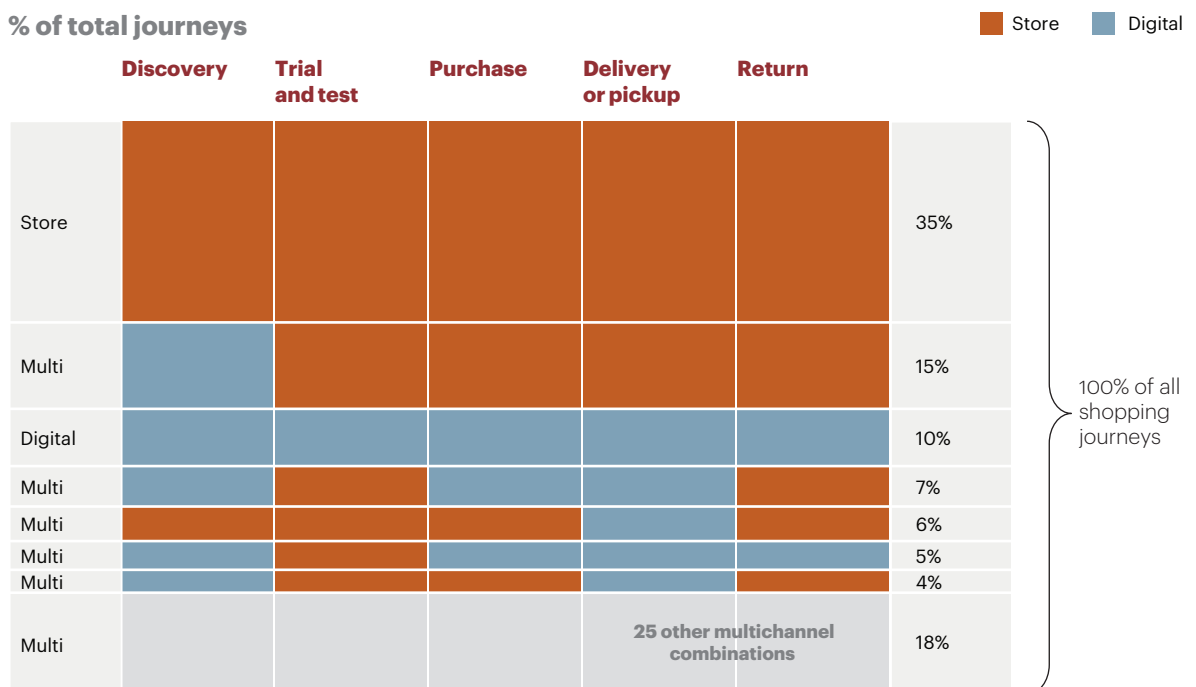
As we have seen from the study results, most shopping experiences are journeys that span multiple channels. As illustrated by figure 4, consumer channel preference varies by stage in the shopping journey, although the most common preferred shopping journey is exclusively store-based for each stage. Fifty-five percent of consumers prefer to use both stores and online throughout the entire journey. Of the 30 possible multichannel journeys, the most common is one in which online is used solely for initial product discovery and the store is preferred for trial, purchase, pickup, and returns.

Viewing retail strategy through the lens of two separate—and at times competing—channels hinders retailers' ability to create a seamless, end-to-end customer experience.

Clearly, a strategy based on leveraging the appeal of the physical store supported by digital is the best formula for capturing the maximum number of sales, building sustainable customer loyalty, and creating opportunities to cross-sell.

Not only are consumers engaging multiple channels throughout the journey, one-third of consumers use more than one channel simultaneously at any given stage in the journey—for example, price checking on a smartphone while in a store. Understanding the consumer's desire for a seamless shopping experience, progressive retailers are devising innovative strategies for maximizing channel value.

Figure 4
Store, digital, and multichannel shopping journey preferences



Note: For survey question "Do you prefer to [INSERT STAGE] [INSERT CATEGORY] online or in a physical store?" n = 2,504 respondents and r = 8,518 journeys
Source: A.T. Kearney Omnichannel Shopping Preferences Study, 2014

The Benefit to Retailers

There's a lot of profit potential in an omnichannel customer offering, which connects a strong store base and digital channels. The potential is driven by three factors: increased shopper loyalty, sales lift, and the opportunity for cross-channel sales. Let's begin by looking at loyalty.

Understanding the Multi-Channel Shopper, a 2011 study conducted by the Verde Group and the Jay H. Baker Retailing Center at the University of Pennsylvania's Wharton School, found that multichannel shoppers are more loyal and spend more than single-channel shoppers. It also showed that brand loyalty is directly correlated with retail channel usage. The more channel opportunities a retailer offers, the more channels a customer shops. And, the more channels a customer shops, the more loyal the customer.

Internet retailers are seeing value in physical stores and are **rapidly expanding their physical footprint.**

The same study showed that multichannel consumers are 15 percent more likely than single-channel consumers to recommend a retailer and that the average spend of three-channel consumers is more than twice that of single-channel shoppers. And then there are those sales lifts, difficult to achieve in the world of single-channel physical retailing.

Even companies that were the darlings of the digital retail boom—Internet retailers such as Bonobos and Warby Parker—are seeing value in physical stores and are rapidly expanding their physical footprint. These click-to-brick retailers report e-commerce sales lifts of three to five times in the built-out markets. This is, at least in part, explained by the fact that retailers report that up to 70 percent of their online consumers live within a physical store's trade area.

There is also a growing advantage of multiple channels: the presence of stores increases value to e-commerce sales and vice versa. The value of a retail strategy that operates multiple channels has been demonstrated by studies that found 23 percent of consumers purchase more items when picking up an online order from stores. Retailers also report that up to 20 percent of consumers who return an online purchase in store make an additional purchase.

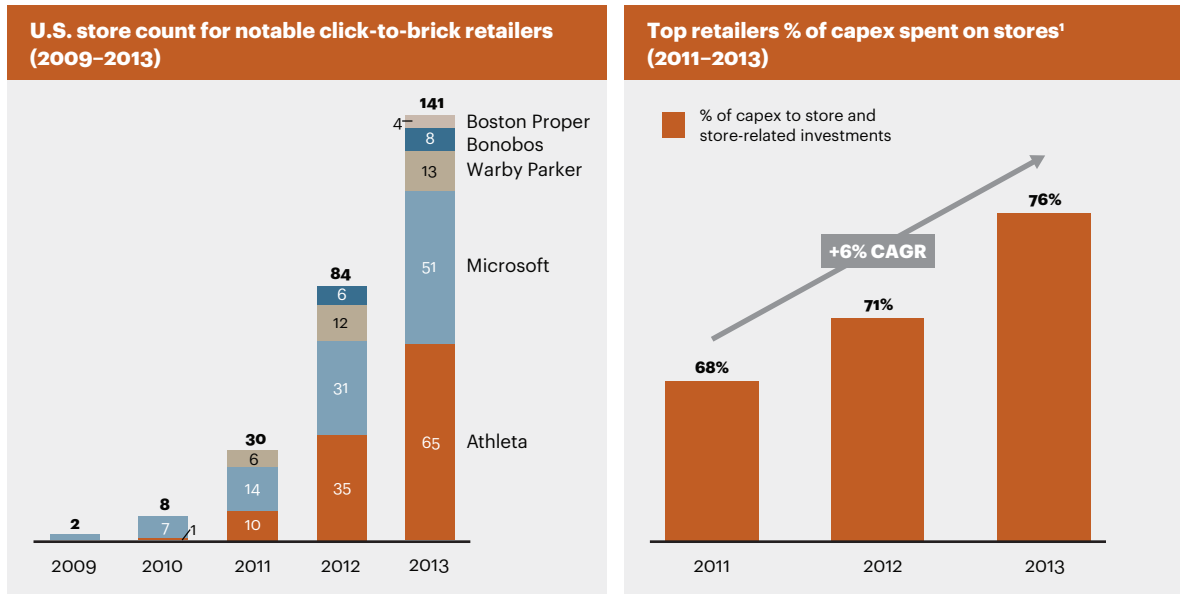
Stores are Just Good Business

Recognizing the benefits of cross-channel retailing, many click-to-brick retailers are beginning to invest heavily in physical stores, or, as in the example of eBay's kiosks in San Francisco and New York, at least in a physical interface. Previous pure-play dot-coms such as Athleta and Boston Proper have now moved into the physical space, and even Amazon.com has experimented with pop-up stores.

The store count for five click-to-brick retailers has grown by more than 140 locations over the past five years (see figure 5 on page 9).

While some traditional retailers are adjusting their store portfolio in the face of changing shopper preferences, others, such as Restoration Hardware and Burberry, are expanding their

Figure 5
Retailer investments in physical stores

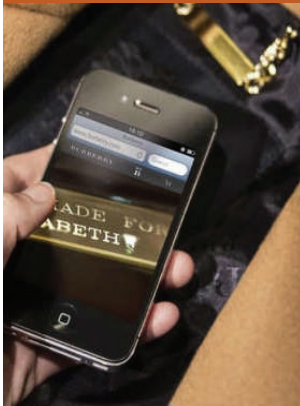


¹Top retailers includes a sample of: Nordstrom, JCPenney, Foot Locker, Neiman Marcus, Williams-Sonoma, Zales, Abercrombie & Fitch, and Limited Brands. Sources: Bloomberg, retailer websites, annual reports; A.T. Kearney analysis

footprints and reinvesting in physical assets (see Burberry case example below). Fast-fashion retailers including H&M and Uniqlo are aggressively looking for new markets, and an increasing number of traditional stores are staging new services such as Macy’s store fulfillment and Gap’s Reserve In Store.

An A.T. Kearney analysis of Bloomberg data and leading retailers’ annual reports found top retailers with multiple channels are spending 76 percent of their capex on store experience and offerings, a 6 percent CAGR increase since 2011 (see figure 5).

Case Example: Burberry’s Digitized Stores Offer a Seamless and Inspiring Shopping Experience



Burberry’s flagship store on Regent Street in London showcases how the luxury retailer is integrating multimedia technologies to provide customers with a seamless in-store shopping experience. Upon entering the store, customers see full-length screens with audio-visual content, live streaming hubs, and mirrors, allowing customers to explore products they see models wearing. When a customer approaches a piece of clothing, RFID tags attached to these items activate and display information about the article of clothing. Burberry has brought innovations into the Burberry Beauty Box. Customers can place products on RFID platforms and see how those products look on them through a projected image. Customers who find what they want can also check out at portable point-of-sale systems that each sales associate carries, further creating a seamless and memorable shopping trip, minimizing annoyances, and increasing satisfaction.

Sources: Luxury Daily, The Telegraph; A.T. Kearney analysis

Whatever the strategy, format, or channel, the future of retailing will be characterized by consumer-centricity as operators continue to capitalize on emerging opportunities to better serve the customer demands for “anything, anytime, anywhere.”

Parting Thoughts

Over time, retailers will continue to integrate physical and digital resources and incorporate new platforms and devices as they build an enhanced shopping experience in response to their customers’ desire for retail solutions that deliver anything, anytime, anywhere, anyhow.

Tomorrow’s consumer will also demand increasingly customized fulfillment of preferences, from convenience and access to exploration and relaxation.

Will online shopping continue to grow? Of course.

Will physical stores remain the cornerstone of retailing? Of course.

Successful retailing has always been—and will continue to be—based on providing the greatest number of consumer options possible and creating the most value on the customers’ terms. And, in the future, that will require physical stores supplemented by digital capabilities, and retailers with the skill to get the most from each channel.

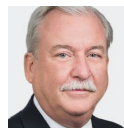
Retailing has come a long way since the prehistoric moment when one human tentatively bartered with another. What may have begun as a simple one-on-one exchange of bright feathers for a polished stone has evolved into what would have seemed like science fiction only 50 years ago.

For all the change we have seen, the basics of retailing remain the same. There is always a buyer, a seller, a product or service, and some location where value is exchanged. And, based on the research, it would seem that shoppers prefer—and will continue to prefer—a robust variety of shopping options, anchored by a physical store.

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The signature of our namesake and founder, Andrew Thomas Kearney, on the cover of this document represents our pledge to live the values he instilled in our firm and uphold his commitment to ensuring "essential rightness" in all that we do.

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