RSR
Retail Systems Research

Making Category Management Relevant In the Age Of The Informed Consumer

Prospective View

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Next-generation category management with advanced analytics and virtualization technologies helps retailers to achieve ***strategic differentiation*** by enabling them to move away from a highly competitive/low differentiating value offer focused on price and convenience and towards offering a ***compelling shopping experience***. Retailers will be able to develop more focused and localized category plans faster, test those plans using customer behavioral insights, roll them out more effectively, establish a platform for better collaboration with supplier partners, and ultimately maximize the profitability and growth potential of each store.

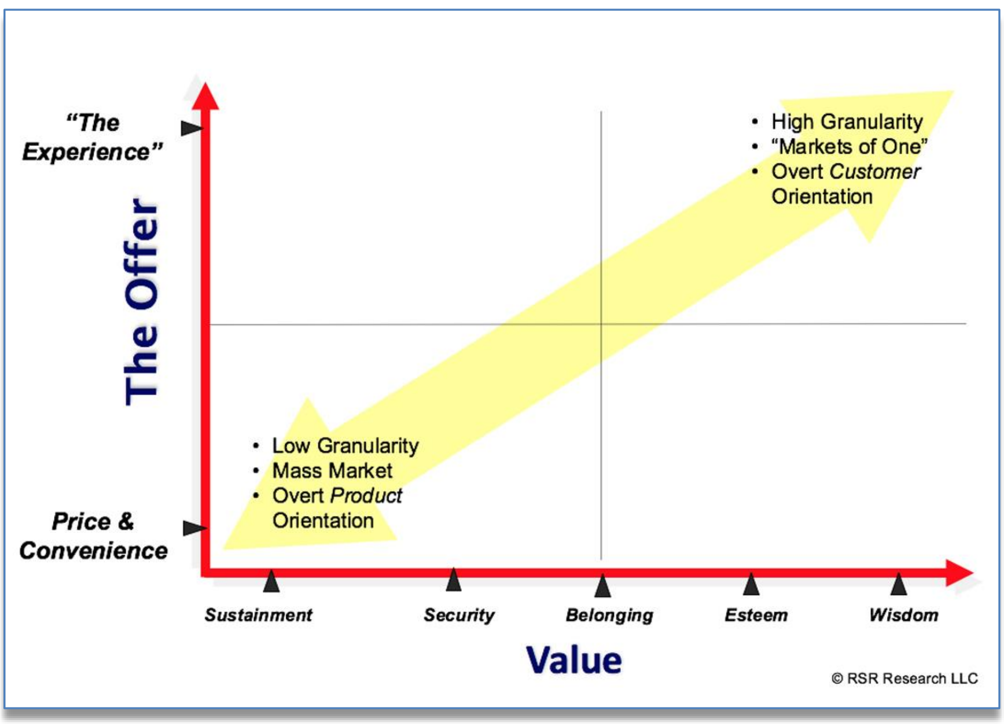
Category Management: Yesterday and Tomorrow

According to the Category Management Association, the objectives of "category management" are "…*to determine the point of optimization in pricing, promotion, shelving, and assortment to maximize profitability and shopper satisfaction."* Those goals are as relevant for fast moving consumer goods (FMCG) and general merchandise (GM) retailers as ever, but yesterday's category management practices are not enough to address the business challenges in today's retail environment.

Let's take a look at the challenges retailers face:

The Value Proposition Has Changed

For FMCG and GM retailers, the market place is increasingly competitive, and segment and channel blurring have devalued price and convenience as primary differentiators. Consider the chart below:



Assortments are most often focused on the basics of modern living ("*sustainment"*) –such as food and beverages, health and beauty items, and household supplies. The level of granularity needed to service one community vs. another is relatively low, and the value being delivered is all about price and convenience. But in today's environment, retailers' prices and the availability of products are transparent to a highly informed consumer community via their mobile devices, and switching costs are perceived as low.

The realities of the new marketplace are borne out by findings in two recent RSR benchmark studies, on pricing practices and mobile strategies. In RSR's April 2016 study entitled ***Pricing 2016: Life Becomes Unmanageable***, responses from FMCG retailers show that the top business challenge is twofold, to grow market share and to stave off competition. The same study revealed that for FMCG retailers, pricing strategies intended to drive top and bottom line results are only "somewhat effective" and that using price to drive customer loyalty is also less than "very effective". In addition, RSR's March 2016 study entitled ***Mobile In Retail: The New Normal*** revealed that for FMCG and GM retailers, competitive price comparisons and price/availability checks are the two most important mobile use cases for consumers. Clearly, price and convenience are table stakes, but not necessarily differentiating.

To overcome these challenges, winning retailers (those who over-perform compared to their competitors) are redefining the value proposition away from focusing solely on low-differentiating value drivers like price and convenience, and towards meeting the needs of a more focused group of customers and in providing a more enjoyable shopping experience *("belonging"*). ***Relevance and the experience*** **are superseding** ***price and convenience*** as the primary demand driver for consumers.

Today, the granularity of the assortment becomes more important, and the total shopping experience is becoming increasingly critical. The difficulty for category planners is that greater granularity has traditionally added complexity: store level assortments are more localized and product adjacencies change, and even the store flow can differ based on the behavioral characteristics of local shoppers.

The Focus of Planning Has to Change

Traditional category management is overtly *product* oriented, and product movement across time and location is used as the proxy for consumer preference and demand. The underlying assumption that retailers and their supplier partners have worked with is that consumers will buy what retailers have to sell them. But as retailers across the globe have learned, consumers are no longer as passive as they were once assumed to be – they don't merely want products at a good price, but solutions to their lifestyle needs. ***It is no longer a question of what retailers and their partners want to sell, but what, where, and how consumers want to buy***.

Demand And Fulfillment Have Changed

For consumers, time is as valuable as money. In the past, retailers assumed that the shopping experience began and ended in the store. The store was physically organized in a manner to maximize every product's contribution to the retailer's category objectives (to build category traffic, sales per transaction, or profits per transaction). But while the store remains an integral part of consumers' shopping journey and the place where most sales transactions are finalized, consumers now use mobile devices to inform their purchase decisions, often outside the four walls of the store. In the store, consumers want to quickly find what they have already decided to buy, without having to wade through aisles of irrelevant items.

To meet demand coming from *outside* of the four walls, winning retailers are offering different fulfillment options to consumers such as instore pickup of online orders and direct fulfillment from the store or DC. But new sources of demand and fulfillment options add even more complexity for category planners to consider, since they also impact store level execution. And most importantly, retailers' ability to deliver the lowest possible cost-of-goods from a "one-size-fits-all" push oriented supply chain is greatly challenged.

Internal Challenges

When it comes to legacy category management processes and technologies, complexity kills speed. FMCG/GM retailers usually carry a high number of products in their assortments (often as many as 75,000 SKU's or more), and inventory turns at a high rate (especially for high velocity categories such as perishables). Even store formats play a role – too many variations of store layout and shelf space design have historically added unmanageable complexity to the planning process.

The speed of the replenishment cycle and sheer number of variables that must be managed, amplified by the limitations of legacy technology, have argued against too much localization. Even when retailers constrained the number of variations, the planning cycle itself was often almost as long as store-level execution of that plan.

The Opportunity: Be Relevant, Be Agile

Given the opportunity, consumers will look beyond "price & availability" to find something more *relevant* to their particular lifestyle needs. Retail Winners understand the implications of this. Consider these findings from RSR's December 2015 benchmark study on Merchandising practices, ***Merchandising 2016: Big Changes Coming***:

- 18% more FMCG/GM Winners rate "localized assortments" as "highly valuable" than under-performing Laggards
- 28% more FMCG/GM Winners rate "integrated assortment and space planning" as "highly valuable" than Laggards
- 13% more FMCG/GM Winners rate "space optimization" as "highly valuable" than Laggards

- 32% more FMCG/GM Winners rate “planogram optimization” as “highly valuable” than Laggards

The days of “one size fits all” assortments are clearly over for consumers. Retail Winners want to respond by offering ***more localized assortments and presentations*** to create a more focused and relevant experience for consumers, while at the same time achieving their sales and profitability goals.

In addition to the *transactional* data used in traditional category management, retailers are learning that to understand demand, they also need insights from new types of *non-transactional* data derived from the digital world; what consumers browse in the digital space, metrics gleaned from online marketing campaigns, and (with the adoption of instore beacons and geo-location data from consumers’ mobile devices) even how consumers browse through the physical store. These new types of data are critically important to retailers today to enable planning for more localized assortments and space plans, and winning retailers are adopting new and powerful data analytics capabilities that promise to deliver new insights from new data faster.

But while the ability to plan localized assortments and space plans is a big improvement over “one size fits all” planning, optimizing assortments and space separately risks undermining both plans. Finally, optimization by itself still does not address how retailers will implement plans quickly and with fewer mistakes that can erode sales and profitability, and ultimately customer loyalty to the Brand.

Model The Store Through The Eyes Of The Consumer

Today’s powerful data analytics coupled with new ***virtualization capabilities*** give retailers the ability to not only *model* category plans, but to simulate store assortments and layouts, and even customer journeys through the store. With ***virtual modeling*** to simulate the physical store, retailers and their category partners can “see” and interact with the store the way consumers would. Merchants and their partners can create and test new merchandising concepts, design new product launches, experiment with alternative assortments and macro store plans, analyze actual performance and adjust plans accordingly. With new data derived from consumers’ “digital” behaviors, the impact of merchandise and marketing plans on sales and profits, the supply chain, and store activity, can be analyzed *before* they are executed.

Most importantly, using next-generation analytics and virtualization technologies as an integral part of category management enables retailers to avoid the arduous, time consuming, and expensive task of rolling a plan out to test stores, observing the results, making adjustments to the plan… and repeating the process as necessary.

Retailers will be able to develop more focused and localized category plans faster, test those plans using customer behavioral insights, roll them out more effectively, establish a platform for better collaboration with supplier partners, and ultimately maximize the profitability of each store. In short, advances in analytics and data virtualization technologies can transform ***the shopping experience***.

The net effect is ***strategic differentiation*** – enabling retailers to move away from a highly competitive and low differentiating "price and convenience" value offer to something that consumers identify as *relevant* to their lifestyles.

Make Next-Gen Category Management Central To Your Planning Process

Retailers who fail to see the implications of customers' ability find what they need anytime and anywhere are putting their Brands at risk. Mobile-enabled shoppers have elevated the need for a new generation of Category Management capabilities. The good news for retailers is that technology is ready to help them address the complexity of managing highly localized assortments in a time of fluid and ever-changing demand.

Rather than viewing Category Management as a discreet optimization process used to extract every ounce of sales and profit from a highly standardized assortment, retailers should implement a next-generation process that is supported by the ability to develop plans based on consumer behavioral insights, that in turn are tested in virtual reality before being rolling out to real stores.

Such an approach should encompass category evaluation and strategy development, macro store planning, inform financial planning, assortment and replenishment planning, and "planogramming". Supply Chain planning will be positively impacted from improved store clustering, resulting in improved item availability even while reducing inventory.

Most importantly, next generation Category Management addresses consumer demands for ***relevance*** and a better shopping ***experience.*** Meeting those objectives will help FMCG and GM retailers achieve ***strategic differentiation*** in today's crowded marketplace.

Appendix A: About The Sponsor

About Symphony RetailAI is the leading global provider of Artificial Intelligence-enabled decision platforms, solutions and customer-centric insights that drive validated growth for retailers and CPG manufacturers, from customer intelligence to personalized marketing, and merchandising and category management, to supply chain and retail operations. Symphony RetailAI is innovating rapidly to drive faster, more profitable decisions through AI, machine learning and voice technologies. We are trusted by over 1200 organizations including 15 of the world's 25 largest grocery retailers, thousands of retail brands, and hundreds of national and regional chains worldwide to help solve their toughest business problems, through AI-powered customer intelligence and retail solutions. More at www.symphonyretailai.com

Appendix B: About RSR Research

Retail Systems Research ("RSR") is the only research company run by retailers for the retail industry. RSR provides insight into business and technology challenges facing the extended retail industry, providing thought leadership and advice on navigating these challenges for specific companies and the industry at large. We do this by:

- **Identifying information** that helps retailers and their trading partners to build more efficient and profitable businesses;
- **Identifying industry issues** that solutions providers must address to be relevant in the extended retail industry;
- **Providing insight and analysis** about a broad spectrum of issues and trends in the Extended Retail Industry.