WHITE PAPER

Managing Fulfillment in Omni-Channel Retailing –

How to use technology to enable your omni-channel strategy

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MANAGING FULFILLMENT IN OMNI-CHANNEL RETAILING – HOW TO USE TECHNOLOGY TO ENABLE YOUR OMNI-CHANNEL STRATEGY

Introduction

Have you ever been presented with a new "opportunity" from the sales and marketing team? Perhaps it is an opportunity that will generate more sales for the company (that's a good thing, right?) but at the same time, it is an opportunity that is a bit ahead of it's time when it comes to the supply chain (okay, here's where it gets interesting).

This, of course, is a rhetorical question. Supply chain operations teams are often presented with new challenges, whether in the form of a new customer, a new compliance requirement, or a new product introduction, among many others. While most operations minded people relish these challenges, there is also something to be said about up-front collaboration amongst the teams when determining how to go after the new opportunity.

An opportunity that has been at the forefront of supply chain executive's minds over the last decade has been the expansion of retail sales into a robust omni-channel environment. As is too often the case, companies, not wanting to lose a single sale, have opened up new channels without enough consideration to how they were going to fulfill those orders.

Fulfilling orders that originate directly from the customer is a much different proposition than replenishing brick and mortar stores. For starters, the order size is very small, often a single unit. These orders are then shipped directly to the customer rather than in bulk to the store. Say goodbye to bulk shipping rates through truckload carriers and hello to higher rates through parcel shippers. If these basic elements are not addressed in the supply chain, the resulting new business will be less than profitable.

As with any new concept, there have been leaders and laggards when it comes to developing an omni-channel retailing strategy. The stories of Amazon.com and Borders Group provide a great example of companies in the same industry with two very different outcomes (see box on page 3). The good news is that even the laggards (at least the ones that are still around) have an opportunity to be successful. Technology is a great enabler in solving the problems that omni-channel retailing presents.

This white paper will take a closer look at the trends in omni-channel retailing, the key challenges that it presents to supply chain operations, and how technology can ensure that profitability is maintained as new sales channels are pursued. If you are a supply chain executive that is new to the world of omni-channel retailing, or if you have been at it for a few years but are looking to get better, then read-on.

Single-channel commerce: going the way of the dinosaurs

"It's just the reality of life in three to five years' time," said Mark Bolland, CEO of UK retailer Marks & Spencer. "For our type of business, if we're not international or multi-channel enough, we do not have a clear future." – Yorkshire Post

Retailers have had it easier than the dinosaurs. Whereas the dinosaurs may have ultimately been doomed by a sudden catastrophic event such as a large asteroid, retailers have had well over a decade to formulate and implement an omni-channel retailing strategy.

While it is true that multi-channel retail has existed for decades (think JC Penney catalog), the myriad of options available to customers today create a much more complicated execution problem. Moreover, this is a train that not only has left the station but one that continues to gain steam.

For the last several years, tough economic conditions have led to a lot of uncertainty in retail. Despite this uncertainty in the overall market, omni-channel retailing has stood out with its consistent growth. Leading this growth is the e-commerce segment.

According to a study performed by Forrester and published by eMarketer.com, U.S. retail e-commerce sales are expected to reach $362 billion by 2016 and are expected to continue to grow at double-digit rates (see chart 1). Global sales are expected to reach nearly $1 trillion dollars in 2013.

If the sheer growth of e-commerce isn't enough to gain the attention of retailers, then perhaps additional data around shoppers in this segment will. By 2015, it is expected that the number of on-line shoppers will exceed 200 million in the U.S., representing over 90 percent of all Internet users. Not only is the number of shoppers increasing, the amount spent by each shopper is also expected to increase from $1,207 in 2012 to $1,738 by 2016. One need not be a math genius to see what is driving the overall growth.

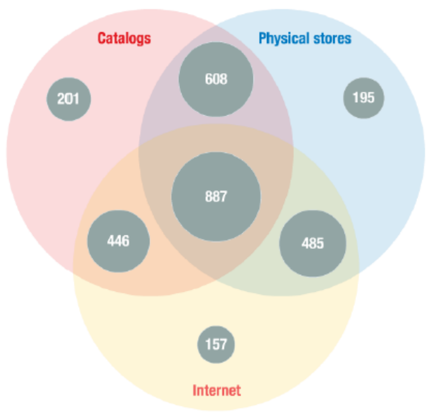
A final statistic to drive the point home; according to a McKinsey analysis published by Aberdeen, the dollars spent by multi-channel shoppers is significantly higher than those that rely on a single channel (see chart 2).

Therefore, by selling through multiple channels retailers not only take advantage of high growth areas, but they also gain access to customers that tend to spend more money.

There are several factors driving these phenomena. According to Forrester, to drive sales, retailers are improving their web sites and service offerings, using more aggressive marketing and discounting techniques, and introducing loyalty programs for on-line shoppers. As these influences attest, the response to changing customer preferences has been lead by the sales and marketing side of the business.

The back-end fulfillment side of things has been slower to adapt, partially due to the uncertainty of where it was all headed. Supporting this point is a survey from MultiChannel Merchant's MCM Outlook 2012-13 for Operations and Fulfillment. In that survey, 59 percent of companies indicated that they employ an order management system while only 41% use a warehouse management system. While advancements have been made on the front end (e.g. improved web site design and leveraging technology to manage the incoming orders), there remains much room on the back-end fulfillment side to improve operations.

Average annual dollars spent per customer by channel (apparel example)



Source: Aberdeen; interviews; JC Williams Group; McKinsey analysis

In a world that is rapidly moving to omni-channel retailing, it is critical that retailers adopt the right strategy or face the possibility of extinction. For those that are moving down this path, it is also imperative that they include their supply chain operations when developing and refining their strategy.

An illuminating example from the world of book retailing :
Rewind the clock to 1994 and a startup retailer called Amazon was incorporated in the state of Washington. Its primary business was to sell books over the Internet to provide access to a wider range of titles than could be stocked in a bricks and mortar store.

About the same time, Borders Group was reestablishing itself as an independent company having been divested from K-Mart. Borders was growing quickly and expanding internationally. It's sales were $1.6 billion in 1995 and they introduced a new large format, 30,000 square foot store that exceeded the footprint of rival Barnes & Noble.

In 1998, Borders launched an online sales channel but never was able to reach profitability in that division. This led them to forge an agreement with Amazon to co-brand a web site for their online sales channel. Under the agreement, Amazon would own all aspects of the arrangement (including the inventory) and Borders would get a "finders fee" for business that came to the site from Borders.com.

Many analysts see this agreement with Amazon as the beginning of the end for Borders. Rather than keep ownership of a segment of the market that was growing very quickly, Borders chose to outsource to a competitor and focus on their bricks and mortar business.

In September 2011, Borders closed its last remaining stores and officially became a defunct company. Today, Amazon continues to thrive and has introduced innovations such as the Kindle to drive further sales and more firmly establish the Internet as a primary selling and delivery channel for books. Would Borders still be operating today if they had re-tooled their business model to match the industry trends? Amazon has been able to build a profitable on-line business so odds are, Borders could have been successful too with the right strategy and execution.

Is your supply chain ready for omni-channel retailing operations?

"To build a profitable online business companies must integrate it seamlessly with their bricks-and-mortar operations. Many keep them separate, increasing the risk that they fail to communicate or work together properly." - The Economist

The above highlights a fundamental objective for companies as they move into omni-channel retailing operations. It is crucial that the new businesses integrate seamlessly with existing operations. The operations of all business units must be considered holistically to ensure that actions for one do not negatively impact another. While this may seem logical, in practice, it is easier said than done.

As the number of channel options for purchasing goods has increased, so have the customers' expectations when it comes to product availability ("I want it now"), the variety of options (can you say SKU proliferation) and the price they are willing to pay to have goods shipped directly to their home ("$0 seems a bit steep, doesn't it…what else can you do for me?").

These rising expectations contribute to the many challenges that supply chain operations face when implementing omni-channel fulfillment. While the list of challenges is quite long, for the purposes of this discussion the focus will be on a few key areas.

First, consider order management. With orders originating from multiple channels, there will be demand against existing and planned inventory from multiple sources. If there is no visibility across these order pools, there is a good chance the inventory will be over allocated and lead to out-of-stocks and the possibility of a lost customer. A retailer can compensate for this by having dedicated inventory for each channel, but that will carry a very high cost.

When it comes to handling online orders, retailers face another productivity sapping problem. By their nature, these orders are very small, often for only a single unit. Additionally, they often come with unique handling requirements such as gift-wrapping. Without the proper technology, it will be very costly to fulfill these small orders while meeting all of the unique requirements.

A familiar problem in retail operations that is heightened in an omni-channel environment is SKU proliferation. Today, customers are accustomed to finding exactly what they want and usually will not accept substitutes. In a bricks and mortar store, a customer is somewhat of a captive audience. It is not always easy to jump in the car and head to a different store if they don't find what they want so they may opt for a substitute. By contrast, when shopping online, a potential customer can easily click on another store to find exactly what they are seeking.

To stay competitive, retailers must provide access to a wider assortment of items than they may have historically. To address this issue, the retailer has options. These options have trade-offs that must be considered. If they choose to stock additional items in their assortment, they will have the increased carrying cost of inventory as well as the challenge of forecasting the demand for the additional items across channels.

Alternatively, the retailer can rely on a third party to fulfill some of their items but then are faced with the challenge of integrating with the third party's systems to have visibility to item details, availability, and shipping times. They also may be competing for access to this inventory with other retailers under this scenario.

Whichever path (or likely combination of paths) the retailer chooses, there will be risk. Should an item not be in stock when a customer wants it, they will lose a sale and quite possibly a customer. Brand loyalty is hard to come by and retain in the online marketplace.

They last major challenge we will consider is the compressed order cycle time. In the ecommerce world, not only do customers expect to get exactly what they want, but they also expect to get it fast without paying a lot to do so. With a lot of retailers offering low cost or even free, expedited shipping, it is a huge challenge to contain costs while meeting the customer's expectations.

While companies have been making good progress in implementing their front-end omni-channel retailing strategies, there is still a lot of work to be done on the back end. It can get overwhelming in a hurry when one tries to profitably manage all of the moving parts. It is easy to see why the operations side has been lagging the customer facing side. Growing the top line through multi-channel sales is great, but if the back-end activities cannot be performed effectively, the bottom line will suffer. It's that old dilemma that retailers face—over-deliver and the costs become untenable, under-deliver and there is a risk of losing a customer.

Leveraging technology to solve the challenges

"These rapidly changing business strategies among retailers have direct impacts on existing and future supply chain management strategies. Inventory management will take on new dimensions for optimizing both physical store and online fulfillment requirements with multi-tier optimization an essential component. Sourcing and transportation strategies need to balance the needs for lowest cost with newer dimensions of customer service and inventory visibility needs. Investments in required new technology and systems will have to be evaluated with criteria that support a combination of brick and mortar outlet, online fulfillment and logistics service center needs." - Infosys

For those new to the world of omni-channel retailing, the challenges are certainly daunting. The good news is that technology exists to address these challenges. Just as retailers use technology to improve the customer facing side of the business to drive top line sales, retailers that are successful in this arena also leverage technology to ensure that the bottom line is healthy as well.

Supply chain execution systems (SCE) exist that have the functionality that retailers need to be successful. There are three central areas where a best-of-breed SCE will ensure that operations are streamlined and that customer expectations are met: warehouse management, transportation management, and trading partner integration. Overlaying all three are visibility tools that provide all parties in the chain with the information they need to make proactive decisions.

Warehouse Management

A warehouse management system (WMS) ensures that the operation is set up for success from the very beginning of the process flow in the DC. If errors or delays occur on the inbound side, they will carry forward to downstream activities, potentially leading to customer disappoints.

A WMS enables the introduction of optimal receiving processes that will support the needs of omni-channel retailing including visibility of inbound goods, tailored processes by channel or client, improved “dock to stock” timeframe and maximized use of storage locations. The WMS will identify goods that are needed immediately for outbound orders and facilitate receiving directly to a pick location.

Moving downstream in the process flow, small order fulfillment optimization is critical to the success of omni-channel retailing operations. Without the ability to batch these orders to be able to wave and pick them en masse, the costs would simply outweigh the benefits of the sales.

The WMS facilitates an accelerated shipping process that meets the needs of omni-channel retailing. The WMS will be able to systematically integrate and batch orders from multiple sources, tailor the waving and picking process by channel or client, optimize the picking and packing process for small orders, and eliminate redundancy of effort for larger orders—all while maintaining the appropriate priority levels for each transaction.

In short, a WMS will ensure that the operations maintain efficiencies, control costs and most importantly, achieve service level goals that are so important in an omni-channel environment. Without a robust system to manage these complexities, operations cannot expect to be successful.

Transportation Management

A transportation management system (TMS) is required to address the next principal challenge of omni-channel retailing: how to ship the large influx of small orders cost effectively, while maintain the appropriate service level commitments.

To meet these objectives, the TMS will employ rule-based algorithms to identify the best mode of transportation for each shipment. When possible, shipments will be consolidated so that they can be moved closer to the final destination more economically. These systems will be integrated to the carriers’ systems and work in conjunction with the WMS to manage the workflow so that the shipments are ready when the truck backs up to the door.

In addition to managing the outbound shipments, the TMS will manage the inbound shipments. This will provide the operation with a number of benefits including visibility to what’s coming for planning purposes, the lowest possible freight rates, ability to evaluate the carriers and create charge backs when requirements are not met, and the reduction or elimination of charges from the carrier due to unexpected circumstances.

Trading Partner Integration

Trading partner integration and enablement is another fundamental area that will drive business efficiencies in omni-channel retailing operations. Trading partner integration will assist the business in optimizing information and product flows. Of primary importance with this function is the automation of business transactions through electronic communications. These business transactions include purchase orders, invoices, advanced shipping notices (ASNs), inventory statuses, item master updates, planning/scheduling data, transportation updates and a host of others. This information is exchanged quickly and systematically between trading partners so that no time is wasted sifting through documents, e-mails or other non-efficient methods of communication.

Equally important as the speed of the transactions is the accuracy. With established ties between the retailer and their trading partners, these transactions can be relied upon to be accurate. Therefore the operation can perform activities like ASN receiving in conjunction with a WMS to simplify the work. This accelerates the overall dock to stock process ensuring that the product is available when the customer comes looking for it.

As companies expand their product assortments to gain more market share, trading partner integration becomes a key enabler. As companies outsource the fulfillment of the extended assortment to suppliers and other third parties, the performance of data synchronization between systems becomes crucial. The retailer must have accurate product information as well as precise information on availability and lead times to be able to provide the information to their customers.

In addition to solving the complexities of data synchronization, trading partner integration enables key execution tasks associated with third party fulfillment operations. These include sending and receiving orders, communicating fulfillment status information, creating retailer specific packing slips, providing shipment status information and the inclusion of return shipping labels. Without trading partner integration tools, these essential third party fulfillment tasks would be unmanageable.

The final piece of the puzzle is visibility. This is the piece that ties it all together from a systems perspective and helps to ensure that the right products are available when they are needed and that all customer service level commitments are met. One failure in this environment can lead to the permanent loss of a customer. Brand loyalty is not as prevalent in the online shopping world of so unless customer expectations are met or exceeded with every transaction, there is always a chance they will leave and never return.

Conclusion

There is no longer any debate; retailers must have an omni-channel retailing strategy or they will cease to exist. Whereas retailers that have pursued such strategies have done well on the front-end, customer-facing side of the business, the back-end fulfillment operations have lagged.

The challenges with omni-channel fulfillment operations are formidable. The good news is that proven technology is readily available so that companies can go after new business and do so profitably.

Omni-channel retailing is all about the execution. With the right systems in place, retailers can deliver near flawless execution to their customers to ensure that they keep coming back in the future.

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