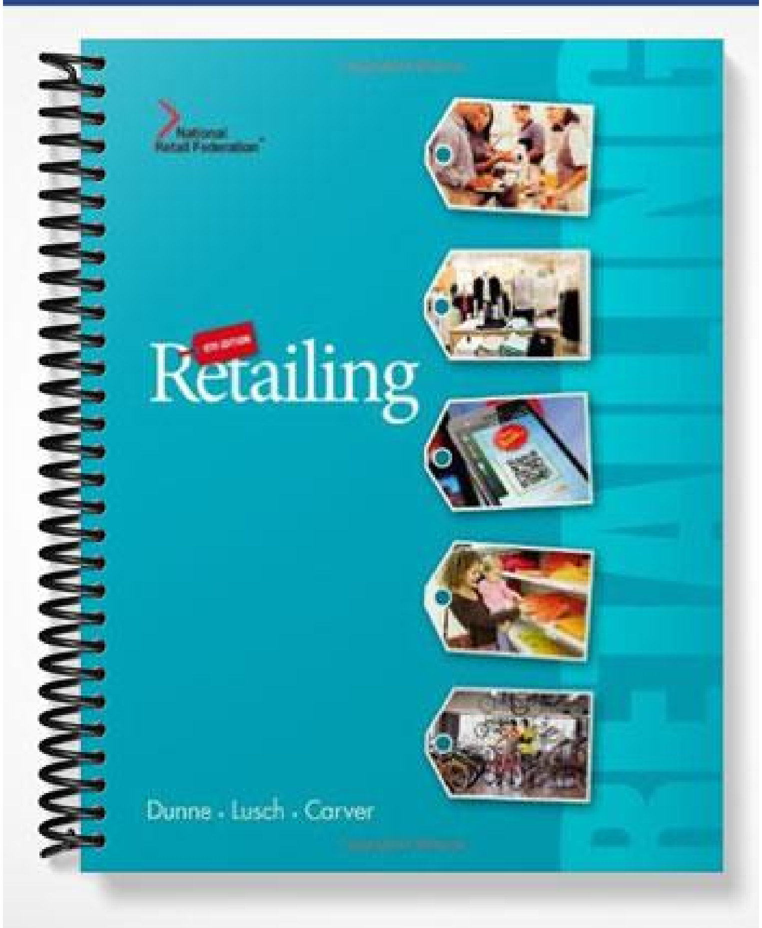
SOLUTIONS MANUAL



Chapter 2

Retail Strategic Planning and Operations Management

OVERVIEW:

In this chapter, we will explain the importance of planning in successful retail organizations. To facilitate the discussion, we introduce a retail planning and management model that will serve as a frame of reference for the remainder of the text. This simple model illustrates the importance of strategic planning and operations management. These two activities, if properly conducted, will enable a retail firm to achieve results exceeding those of the competition.

LEARNING OBJECTIVES:

After reading this chapter, you should be able to:
1. Explain why strategic planning is so important and be able to describe the components of strategic planning: statement of mission; goals and objectives; an analysis of strengths, weaknesses, opportunities, and threats; and strategy.
2. Describe the retail strategic planning and operations management model, which explains the two tasks that a retailer must perform and how they lead to high profit.

CHAPTER OUTLINE:

I. Components of Strategic Planning

In most endeavors, a well-defined plan of action can mean the difference between success and failure. A clearly defined plan of action is an essential ingredient in all forms of business management. This is especially true in the highly competitive field of retailing, where consumer demand continues to be relatively soft.

Planning is the anticipation and organization of what needs to be done to reach an objective. However, it is difficult to know in advance of each upcoming season what styles, quantities, colors, and sizes the customers will want. Superior planning by retailers enables them to offset some of the advantages their competition may have such as a good location. Success for all retailers, large and small, is generally a matter of good planning and then implementing that plan.

When there is a lot of change and turbulence in the retailer's environment, it may be especially important to be proactive in terms of strategic action. For instance, several retailers have chosen to "jump with both feet" into the digital world and overlook the short-term potential of cannibalizing one's in-store sales. In 2010, JCPenney became the first retailer to place its entire product catalog online within Facebook. While these retailers may not be sure about the eventual role social media or the Internet may play within their respective industries, each has realized that if they don't plan for the future and take strategic actions today, they risk becoming "forgotten retailers of another era."

Strategic planning involves adapting the resources of the firm to the opportunities and threats of an ever-changing retail environment. Through the proper use of strategic planning, retailers hope to achieve and maintain a balance between resources available and opportunities ahead. Strategic planning process consists of four components:

- Development of a mission (or purpose) statement for the enterprise
- Definition of specific goals and objectives for the enterprise
- Identification and analysis of the retailer's strengths, weaknesses, opportunities, and threats—referred to as SWOT analysis
- Development of strategies that will enable the enterprise to reach its objectives and fulfill its mission

A. Mission Statement

The beginning of a retailer's strategic planning process is the formulation of a mission statement. The **mission statement** is a basic description of the fundamental nature, rationale, and direction of the firm. It provides the employees and customers with an understanding of where future growth for the enterprise will come from. Yet not every retailer has a mission statement. Consequently, because so many businesses don't know where they want to go and how to get there, they end up as failures. However, the lack of a written statement is not a cause by itself for success or failure if the firm has a clearly understood, even if unwritten, mission and plan of action.

While mission statements vary from retailer to retailer, good ones usually include three elements:

- How the retailer uses or intends to use its resources
- How it expects to relate to the ever-changing environment
- The kinds of values it intends to offer in order to serve the needs and wants of the consumer.

A mission statement can be short or long, as long as it provides the retail enterprise with its future.

Just having a mission statement is not enough in today's business climate. The retailer must adhere to its mission and not change with every new fad. However, at times a mission statement must be changed or redefined.

B. Statement of Goals and Objectives

The second step in the strategic planning process is to define specific goals and objectives. These goals and objectives should be derived from and give precision and direction to the retailer's mission statement.

Goals and objectives serve two purposes:

- They provide specific direction and guidance to the firm in the formulation of its strategy.
- They provide a control mechanism by establishing a standard against which the firm can measure and evaluate its performance.

If the results are less than expected, then it signals that corrective actions need to be taken.

While goals and objectives can be expressed in many different ways, retailers will usually divide them into four dimensions:

- Market performance, which compares a firm's actions to its competitor's
- Financial performance, which analyzes the firm's ability to provide a profit level adequate to continue in business and in many cases grow its business
- Societal objectives, which are phrased in terms of helping society fulfill some of its needs
- Personal objectives, which relate to helping people employed in retailing to fulfill some of their needs.

Market Performance Objectives

Market performance objectives establish the amount of dominance the retailer seeks in the marketplace. The most popular measures of market performance in retailing are:

- Sales volume
- **Market share**—the retailer's total sales divided by total market sales or the proportion of total sales in a particular geographic or product market that the retailer has been able to capture.

Usually, when a retailer wants to grow its sales more rapidly than the growth of the overall market or economy, it needs to expand the number of stores it operates. Thus, high sales growth retailing is directly linked to expanding the size of the enterprise's chain of retail stores.

Research has shown that profitability is clearly and positively related to market share. Three things drive this relationship:

- A firm gains market share, at least in a stable or growing market, by increasing its' sales faster than competitors, which allows it to gain the operating efficiency.
- As a retailer gains market share, it has increased recognition among consumers so its advertising expenditures relative to competitors are more efficient.
- High–market share retailers have higher store traffic that allows their employees to be more productive.

Unlike manufacturing, where an employee can work on making something without a customer present, in retailing most employees can only do meaningful work when customers are in the store. Exhibit 2.1 illustrates this relationship.

Thus, market performance objectives are not pursued for their own sake but because they are a key profit path.

Financial Objectives

Retailers can establish many financial objectives, but they can all be conveniently fit into the categories of profitability and productivity.

Profitability Objectives

Profit-based objectives deal directly with the monetary return a retailer desires from its business. The most common way to define profit is the aggregate total of net profit after taxes—that is, *the bottom line of the income statement*. Another common retail method of expressing profit is as a percentage of net sales. However, most retail owners feel the best way to define profit is in terms of *return on investment* (ROI).

This method of reporting profits as a percentage of investments is complicated by the fact that there are two different ways to define the term *investment*. *Return on assets* (ROA) reflects all the capital used in the business, whether provided by the owners or by creditors. ROI, also referred to as *return on net worth* (RONW), reflects the amount of capital that the owners have invested in the business.

The most frequently encountered profit objectives for a retailer are shown in Exhibit 2.2: the strategic profit model (SPM). The five elements of the SPM are:

- **Net profit margin**—the ratio of net profit (after taxes) to net sales. It shows how much profit a retailer makes on each dollar of sales after all expenses and taxes have been met.

- **Asset turnover—**total sales divided by total assets and shows how many dollars of sales a retailer can generate on an annual basis with each dollar invested in assets.
- **Return on assets (ROA)**—net profit (after taxes) divided by total assets.
- **Financial leverage—**total assets divided by net worth or owners' equity and shows how aggressive the retailer is in its use of debt.
- **Return on net worth (RONW)**—net profit (after taxes) divided by owners' equity.

Attempts to increase asset turnover by merely reducing inventory levels can lead to **stockouts** (where products are not available for customers when they want them), thus creating a dissatisfied customer who may never return.

Managers are usually evaluated on ROA since financial leverage is beyond their control. In addition to the five elements of the SPM, another measure of profitability is the gross margin percentage, which is gross margin divided by net sales.

All retailers establish some form of profit objective. The specific profit objectives developed will play an important role in evaluating potential strategic opportunities. Incidentally, the last 25 years in the United States has seen relatively low price inflation. But when price inflation rises, retailers as well as other enterprises develop higher profit objectives. Or in the case of individuals, they have higher expectations in terms of annual raises and compensation levels because, with inflation, each dollar is worth less than the prior year.

Productivity Objectives

Productivity objectives state how much output the retailer desires for each unit of resource input. There are three major resources at the retailer's disposal and they are:

- *Space productivity*—net sales divided by the total square feet of retail floor space. A space productivity objective states how many dollars in sales the retailer wants to generate for each square foot of store space.
- *Labor productivity*—net sales divided by the number of full time-equivalent employees (employees who work 40 hours per week; typically, two part-time workers equal one full-time employee). A labor productivity objective reflects how many dollars in sales the retailer desires to generate for each full time-equivalent employee.
- *Merchandise productivity*—net sales divided by the average dollar investment in inventory. This measure is also known as the sales-to-stock ratio. Specifically, this objective states the annual dollar sales the retailer desires to generate for each dollar invested in inventory.

Productivity objectives are used by a retailer to program its business for high-profit results.

Societal Objectives

Societal objectives reflect the retailer's desire to help society fulfill some of its needs. The five most frequently cited societal objectives are:

- *Employment objectives*—relate to the provision of employment opportunities for the members of the retailer's community.
- *Payment of taxes*—is the retailer's role in helping finance societal needs that the government deems appropriate.
- *Consumer choice*—a retailer may have an objective of competing in a way that gives consumers a real alternative. A retailer with such an objective desires to be a leader and innovator in merchandising and thus provide the consumer with choices that previously were not available in the trade area.
- *Equity*—reflects the retailer's desire to treat the consumer and suppliers fairly and not endanger their living conditions. In addition, retailers will not engage in price gouging consumers in instances of merchandise shortages.
- *Being a benefactor*—the retailer may desire to underwrite certain community activities.

Personal Objectives

Personal objectives reflect the retailers' desire to help individuals employed in retailing fulfill some of their needs. Generally retailers tend to pursue three types of personal objectives:

- *Self-gratification*—focuses on the needs and desires of the owners, managers, or employees of the enterprise and the pursuit of what they truly want out of life.
- *Status and respect*—all people strive for status and respect. In stating this objective, one recognizes that the owners, managers, and employees need status and respect in their community or within their circle of friends.
- *Power and authority*—reflects the need of managers and other employees to be in positions of influence.

Exhibit 2.4 provides a synopsis of the market performance, financial performance, societal, and personal objectives that retailers can establish in the strategic planning process.

C. Strategies

A **strategy** is a carefully designed plan for achieving the retailer's goals and objectives. It is a course of action that when executed will produce the desired levels of performance. Retailers can operate with three basic strategies:

- *Get shoppers into your store*—often referred to as a retailer's *traffic strategy*, many retailers think getting people to visit the website or the store is one of the most difficult tasks in retailing.
- *Convert these shoppers into customers by having them purchase merchandise*—often referred to as a "retailer's conversion" or "closure" strategy, this means having the right merchandise and services, using the right layout and display, and having the right price, and having the right type and quality of employees.
- *Do this (get shoppers in your store and convert them into customers) at the lowest operating cost possible that is consistent with the level of service that your customers expect*—this is often referred to as a "retailer's cost management" strategy.

Many retailers go further and develop strategies that enable them to differentiate themselves from the competition as they accomplish these three tasks. However, one of the greatest failings in retailing today is that too many retailers have concentrated on just one means of differentiation: price. Some better forms of differentiation for a retailer are:

- *Outstanding design of the market offering*—by offering brilliant and innovative merchandising.
- *The selling process*—by offering excellent customer service.
- *After-purchase satisfaction*—by offering "satisfaction guaranteed" programs.
- *Location*—or the ease with which the customer can get to the retailer
- *Never being out-of-stock*—being in stock with regard to the sizes, colors, and styles that the target market expects the retailer to carry.

A retailer develops a strategy to differentiate itself by analyzing its strengths and weaknesses, as well as the threats and opportunities that exist in the environment. This process is often referred to as *SWOT* (strengths, weaknesses, opportunities, and threats) *analysis*.

D. Strengths

- What major competitive advantage(s) do we have?
- What are we good at?
- What do customers perceive as our strong points?

E. Weaknesses

- What major competitive advantage(s) do competitors have over us?
- What are competitors better at than we are?
- What are our major internal weaknesses?

F. Opportunities

- What favorable environmental trends may benefit our firm?
- What is the competition doing in our market?
- What areas of business that are closely related to ours are undeveloped?

G. Threats

- What unfortunate environmental trends may hurt our future performance?
- What technology is on the horizon that may soon have an impact on our firm?

After performing the SWOT Analysis, the retailer must develop a retail marketing strategy with strong financial elements. A fully developed marketing strategy should address the following considerations:

- The specific **target market** is the group(s) of customers that the retailer is seeking to serve. It is important for retailers to understand that different target markets demand different product offerings
- The **location**(s) should be consistent with the needs and wants of the desired target market.
- The specific **retail mix** a retailer intends to use to appeal to its target market and thereby meet its financial objectives is the combination of merchandise, price, advertising and promotion, location, customer services and selling, and store layout and design that the retailer uses to satisfy the target market. (Exhibit 2.7).
- The retailer's **value proposition** is a clear statement of the tangible and intangible results a customer receives from using the retailer's products or services. It is the difference between the benefits offered by one retailer versus those of the competition.

II. The Retail Strategic Planning and Operations Management Model

Exhibit 2.8 suggests that a retailer must engage in two types of planning and management tasks:

- Strategic planning
- Operations management

Each task is undertaken to achieve high-profit results.

A. Strategic Planning

Strategic planning is concerned with how the retailer responds to the environment in an effort to establish a long-term course of action. The strategic plan should best reflect the line(s) of trade in which the retailer will operate, the market(s) it will pursue, and the retail mix it will use. Strategic planning calls for a long-term commitment of resources by the retailer. An error in strategic planning can result in a decline in profitability, bankruptcy, or a loss of competitive position. On the other hand, effective strategic planning can help protect the retailer against competitive onslaughts or adverse environmental occurrences.

The initial steps in strategic planning are to define the firm's mission, establish goals and objectives, and perform a SWOT analysis. The next steps are to select the target market and appropriate location(s). It is important to note that most retail managers or executives have very little control over location decisions. After selecting the target market and location, the retailer must develop the firm's retail mix. Retailers can best perform this strategic planning only after assessing the external environment.

Exhibit 2.8 profiles the major environmental factors that need to be assessed:

- *Consumer behavior*—the retailer will need to understand the determinants of shopping behavior so it can identify likely changes in that behavior and develop appropriate strategies.
- *Competitor behavior*—retailers must develop a competitive strategy that is not easily imitated.
- *Supply chain behavior*—the behavior of members of the retailer's supply chain can have a significant impact on the retailer's future. For example, are certain supply chain members such as manufacturers or wholesalers always seeking to improve their position in the supply chain by establishing their own Internet sites and thus bypassing the retailer?
- *Socioeconomic environment*—the retailer must understand how economic and demographic trends will influence revenues and costs in the future and adapt its strategy according to these changes.
- *Technological environment*—the technical frontiers of the retail system encompass new and better ways of performing standard retail functions. The retailer must always be aware of opportunities for lowering operating costs.
- *Legal and ethical environment*—the retailer should be familiar with local, state and federal regulations of the retail system. It must also understand evolving legal patterns in order to be able to design future retail strategies that are legally defensible.

B. Operations Management

Operations management is concerned with maximizing the efficiency of the retailer's use of resources and with how the retailer converts these resources into sales and profits. In other words, its aim is to maximize the performance of current operations.

Exhibit 2.8 shows that operations management involves managing the buying and handling of merchandise, pricing, advertising and promotion, customer services and selling, and facilities. All of these activities require day-to-day attention.

Operations management can, however, extend beyond the retail store if the retailer is a chain store retailer and is self-distributing or essentially performs the wholesaling function and buys direct from manufacturers. In this situation, the retailer will operate one or many distribution centers that receive shipments from manufacturers and then sorts the shipments into new shipments of broader assortments for delivery to its stores. Most of the work of transporting and handling merchandise is an operations management function.

C. High Performance Results

The far right box of the retail strategic planning and operations management model (Exhibit 2.8) suggests that the cumulative effect of well-designed and executed strategic and operations plans will be the achievement of high profit. Mistakes in either of these two areas will severely hamper the retailer's performance and prevent it from being among the leaders in its industry.

The need to strive for a high profit is tied to the extremely competitive nature of retailing. Retailers are well advised to set high but realistic profit objectives so that if their planned profits are not reached, they at least have a chance of achieving average profitability. Exhibit 2.9 shows how the strategic profit model (SPM) results of high-performance retailers compare to the median performance for similar retailers.

As a general rule of thumb, retailers should strive for the following goals when planning their SPM:

- Net profit margin of 2.5–3.5 percent
- Asset turnover of 2.5–3.0 times
- Financial leverage of 2.0–3.0 times

REVIEW AND DISCUSSION QUESTIONS:

[LO01] <u>Explain why strategic planning is so important and describe its components</u>.

1. Why is strategic planning so important in retailing today? Should a retailer, even a small retailer, always have a strategy to change the rules of the game as it is currently being played? Why?

   Strategic planning involves adapting the resources of the firm to the opportunities and threats of an ever-changing retail environment. Through the proper use of strategic planning, retailers hope to achieve and maintain a balance between resources available and

opportunities ahead. Also, a clearly defined plan of action is an essential ingredient in all forms of successful business management.
All retailers should have a strategy in place so that they are able to change the rules of the game being played or, if they can't change the rules, to have a strategy to win the game as it is currently being played. The strategy should consist of a specific objective, an area of operation, and the understanding of what makes a retailer better than its competitors.

2. How do the retail firm's mission statement and its stated goals and objectives relate to the retailer's development of competitive strategy?

   The beginning of a retailer's strategic planning process is the formulation of a mission statement. It provides the employees and customers with an understanding of where future growth for the firm will come from. But, just having a mission statement is not enough in today's business climate.
   Then goals and objectives are derived from, and give precision and direction to, the retailer's mission statement. Goals and objectives serve two purposes. First, they provide specific direction and guidance to the firm in the formulation of its strategy. Second, they provide a control mechanism by establishing a standard against which the firm can measure and evaluate its performance.

3. Many people have either strong favorable or unfavorable opinions of retailers in their community. Suppose you were asked to advise one of the retail businesses near your home, your place of work, or college, what suggestions would you make for it to differentiate itself?

   Depending on the availability of retailers in their community, students' answers will vary. Development of a differentiation strategy will start with an analysis of the retail owner's strengths and weaknesses as well as the threats and opportunities that exist in the community. This process of SWOT (strengths, weaknesses, opportunities, and threats) analysis will involve asking the following baseline questions:
   <u>Strengths</u>
   - What is its competitive advantage?
   - What is it good at?
   - What do students like about it?

   <u>Weaknesses</u>
   - What are the competitive advantage and strength of its competitors in that area?
   - What are its major weaknesses?

   <u>Opportunities</u>
   - What is the probable student population in that area; those who still do not frequent nightspots?

- How are the competitors performing in that area?
- Is there any emerging market trend that can affect the business?

Threats

- Is the market facing any unfortunate economic downturn?
- Is student population declining because of exams or holidays?
- Is the consumer affected by competitor's marketing strategies?

4. Can a mission statement be too narrow in scope? Can it be too broad in scope? Explain your answers.

   A mission statement can be short or long, as long as it provides direction for the future of the firm. The mission statements vary from retailer to retailer, and good ones usually include the following three elements:

   - How the retailer uses or intends to use its resources
   - How it expects to relate to the ever-changing environment
   - The kinds of values it intends to offer in order to serve the needs and wants of the consumer

   However, in today's business climate, just having a mission statement is not enough. The retailer must adhere to its mission, but at the same time a mission statement must be changed to accommodate the changing business environment.

5. Choose any two supermarkets operating in your community. Compare and contrast their retail mix as they seek to satisfy the needs of their target market given their present location. What changes would you suggest to the management of these retailers as they develop their strategic plans for the coming year?

   Answers will vary depending on which two supermarkets are selected for comparison and contrasting purposes. The instructor should assist in the discussion by clarifying the students' understanding of the components of the retail mix (i.e. the combination of merchandise, price, advertising and promotion, location, customer services and selling, and store layout and design). When a clear understanding of these components is achieved, the instructor will want to ask the students' perception of the respective target markets. Building upon that, the various changes and adjustments can be proposed and discussed.

6. An automobile dealer located near your campus visits your class. During the presentation, the dealer notes that their mission statement is "We will provide the best vehicle sales and service experience for our customers. We will do this in a way that will foster the continuous improvement of our people and our company. We will be a top performing, thoroughly professional, and genuinely caring organization in all that we do." Would you offer any suggestions for changing this mission statement? If so why?

Students may take various positions on the strength of this mission statement. Their suggestions will also vary in accordance to the varying answers. What is important here is, to verify the answers to following questions before drawing out the strengths, thus suggestions to the given mission statement may include:

- Does this mission statement really answer the question, "What business the retailer is in?"
- Does it provide direction for the future of the firm?
- Is it motivational?
- Does it relate to the ever-changing environment?
- Does it serve or intend to serve the needs and wants of the consumer?

7. Many people are using location-based apps like Foursquare, Yelp, and Gowalla to stay in touch with friends and as described in the chapter's "What New?" box, retailers are now capitalizing on this to increase store traffic or closure. Describe some other ideas not discussed in this chapter that might represent possibilities for retailers to benefit from these apps.

   Answers will vary. Students may take various positions on the possibilities for retailers to benefit from these apps. The instructor should assist in the discussion by clarifying the students' understanding of the components of the retail mix (i.e. the combination of merchandise, price, location, advertising and promotion, customer services and selling, and store layout and design). When a clear understanding of these components is achieved, the student can be asked its perception on such programs. Building upon that, discussions can be held.

8. Why do you think the strategic profit model is often used in retail planning and management?

   Students' answers may vary. However, students should emphasize that using a strategic profit model in retail planning and management helps retailers monitor the following five elements, which in turn help the retailer know its performance:

   - Net profit margin—the ratio of net profit (after taxes) to net sales. It shows how much profit a retailer makes on each dollar of sales after all expenses and taxes have been met.
   - Asset turnover—computed by taking the retailer's annual net sales and dividing by total assets. This ratio tells the retail analyst and retail management how productively the retailer's assets are being used.
   - Return on assets (ROA)—annual net profit divided by total assets, depicts the net profit return the retailer achieved on all assets invested regardless of whether the assets

were financed by creditors or by the firm's owners.

- Financial leverage—total assets divided by net worth or owners' equity. This ratio shows the extent to which a retailer is using debt in its total capital structure.
- Return on net worth (RONW)—net profit divided by net worth or owner's equity. RONW, shown at the far right of the SPM, is usually used to measure performance from the owner's or shareholder's perspective.

9. What is space productivity? Why is it important in retailing?

Space productivity is defined as net sales divided by the total square feet of retail floor space. A space productivity objective states how many dollars in sales the retailer wants to generate for each square foot of store space.

[LO02] Describe retail strategic planning and operations management model.

10. What are the major environmental forces that retailers will face over the next five years? Is any one of these more important than the others?

The major environmental factors that a retailer must face are:

- Consumer behavior—understanding the determinants of consumer's shopping behavior.
- Competitor behavior—understanding how the behavior of competing retailers will have an impact on strategies the retailer will want to develop.
- Supply chain behavior—keeping abreast of the behavior of channel members (e.g., manufacturers opening up their own retail stores) and its impact on retailer behavior.
- Socioeconomic environment—understanding how economic trends and demographics can influence future retail sales.
- Technological environment—gathering data on new and better ways of performing the many tasks of a retailer (e.g., use of computers to improve inventory control).
- Legal and ethical environment—familiarizing yourself with federal, state, and local regulations having an impact on the retailer's performance and behaving at the highest level of ethical performance.

Given these environmental factors, students will need to forecast the varying ways these forces will impact retailers. For example, a student may propose that within the context of consumer behavior, consumers within the next five years will continually move toward the desire for products to be delivered via the Internet. Should the student propose this, they may also want to give a specific example such as the desire to obtain music via an Internet download service as opposed to purchasing CDs at a brick-and-mortar store.

These forces cannot be controlled by a single retailer. However, threats emanating from the forces are usually translated into opportunities by successful retailers. Questions of importance will be varied in the opinions expressed by the students regarding each of the discussed forces.

11. Does strategic planning become more or less important as the uncertainty the retailer faces increases?

    Strategic planning is necessary and important in situations where certainty is either high or low. In situations of high uncertainty, its importance is heightened because of constraints on a retailer (e.g., monies available). If a wrong decision is made, there is no opportunity for a second chance. This can be true in an environment of high certainty, but the degree of risk may be lessened.

12. When doing the strategic planning and operations management tasks described in our model, does the retailer use creative thinking or analytical problem solving?

    When doing the planning and management tasks as described in the model in the text, the retailer should use both creative thinking and analytical problem solving. For example, McDonald's uses creative thinking in making the decision to locate at army bases, hospitals, and universities. At the same time, analytical problem solving comes into play in the decisions the retailer makes on how to better motivate employees. At times, when looking at retailers, it is difficult to distinguish these approaches from one another but nonetheless both should be used.

13. A person once said, "A good manager can overcome a bad plan." Agree or disagree with this statement and explain your reasoning. Use current examples, if possible, in your answer. Would your answer be the same if the person said, "A good plan can overcome a poor manager?"

    Answers will vary. Students will take different positions on the above statement. The instructor has to assist in understanding of the retail strategic planning and operations management model (Exhibit 2.8). The model suggests that the cumulative effect of well-designed and executed strategic and operations plans will be the achievement of high profit. Mistakes in either of these two areas will severely hamper the retailer's performance and prevent it from being among the leaders in its industry. The instructor can also take the help of McDonald's example discussed in the text.

14. Why is it so important for a retailer to seek high profit performance? Isn't it enough to be above average?

    In the highly competitive world of retailing, it is not enough to be above average in performance. Retailers must seek high performance results to both succeed and survive. Being slightly above average can place you in fourth or fifth place. With the fierce competition that now exists, this might not be sufficient. However, a below average retailer can hope to achieve slightly above average results as an intermediate goal; the long-run goal is superior results. Students must realize that when averages are presented by organizations such as the National Retail Federation, performance figures by all types of retailers are included.

WRITING AND SPEAKING EXERCISE:

Dolph Drake, the owner of Bulldog Books, has three bookstores near the campus of a large state university. In the past, he has run his stores very informally. He likes to claim that he is successful because he doesn't think too much and that he makes most of his decisions by the "seat of his pants." Over the past five years profits at each store have increased between 5 percent and 7 percent each year, despite the fact that the average price of textbooks has doubled. Also, Drake has never given much thought to changing his original plans for his bookstores.

While Drake was the first to open off-campus stores and therefore got the prime locations, competitors are beginning to appear near all three of his stores. In fact, just recently an out-of-town competitor gathered the majority of the end-of semester textbook buy-backs, one of the most profitable activities for a campus bookstore. This out-of-towner merely set up a drive-through buyback operation at a nearby parking lot so that students could pull up under an awning, hand over their books, and drive off with money within minutes. Even though the competitor left town the next day, Drake expects other book buyers will seek to "hit and run" at the end of the fall semester.

As a result of this recent loss of business, Drake feels that it is time to develop a more structured approach for his business and asks you as part of your summer internship to research the strategic planning process. You are to prepare a memo on the basic steps and tasks that are involved in developing a strategic plan. Be sure to include in your memo a mission statement and a list of objectives that Bulldog Books should seek to achieve.

Suggested Answer:
The students may choose to approach this question from a variety of angles within the context of strategic planning. However, there are some common elements that should be discussed:

- First, the memo should include supporting reference that explains why strategic planning is so important. This might include a discussion on how "planning is the anticipation and organization of what needs to be done to reach an objective." Illustrations on how the lack of planning can spell disaster also help substantiate the need for strategic planning. Clarification between strategy and objectives as well as delineation between strategic plans and financial plans will substantiate the argument that a strategic plan is necessary to improve performance.

- Second, the memo should include a discussion of the major environmental forces in play. In this particular situation, three forces are highly applicable:
  - Consumer behavior—it appears students were attracted by the ease of disposal of old textbooks which to Drake meant taking away a major share of one of the most profitable activity of campus bookstore.
  - Competitor behavior—in this case, the book buyer merely set up a drive-through buy-back operation at a nearby parking lot.
  - Supply Chain behavior—more book buyers will seek to "hit and run" at the end of the fall semester.
- Third, the memo should include a tie-in from these environmental forces at play to the threats and opportunities presented to the retail chain. Garnering from the information the individual students provide, they will want to expound on how the firm will perceive these as a threat and an opportunity, given the resources, current positioning, and competitive environment.
- Finally, the memo could include an outline of how these forces, threats, and opportunities fit in with the bookstore's market performance and financial objectives and ultimately its mission statement.

RETAIL PROJECT:

Go to the library and either look at the most recent annual reports for four or five of the Top 25 U.S. retailers listed on the inside cover of this text or locate the 10-Ks of those firms on the Internet. (Note: All publicly held firms need to file their U.S. Security and Exchange Commission 10-Ks, a more complete financial analysis of the firm's performance, electronically. To look up this information, go to www.sec.gov/edgarhp.htm). Use the SPM described in Exhibits 2.2 and 2.9 to calculate your own SPM numbers for these retailers.

Finally, after you have calculated these numbers, which retailer do you believe is the best at achieving financial superiority?

Suggested Answer:
The correct answer for this assignment will depend on the retailer's performance in future years.

PLANNING YOUR OWN ENTREPRENEURIAL RETAIL BUSINESS:

In the "Planning Your Own Entrepreneurial Retail Business" exercise in Chapter 1, you learned how to estimate the net profits that your business might earn. You saw what would happen if your sales estimate was off by 10 percent. Now it's time to analyze the dollar investment you need in assets to support your business and how you might finance these assets.

Your investment in assets needs to cover inventory, fixtures, equipment, cash, customer credit (i.e., accounts receivable) and perhaps other assets. These assets could be financed with debt or by investments you or perhaps other investors make in the business.

Compute the strategic profit model ratios under the assumption that your first year sales are $800,000, net profit is $56,000, total investment in assets is $400,000, and the total debt to finance these assets is $300,000. (Hint: net worth is equal to total assets less debt.) What would happen to these ratios if net profit rose to $65,000?

Suggested Answer:

NPM	**Asset Turnover**	**ROA**	**Financial Leverage**	**RONW**
Old				
Net Profit/Total Sales	Total Sales/Total Assets	Net Profit/Total Assets	Total Assets/Net Worth	Net Profit/Net Worth
S56,000/ $800,000	S800,000/ $400,000	S56,000/ 4100,000	$400,000/ $100,000	$66,000/ $100,000
7.0%	2.0%	14.0%	4.0%	66.0%
New				
Net Profit/Total Sales	Total Sales/Total Assets	Net Profit/Total Assets	Total Assets/Net Worth	Net Profit/Net Worth
$65,000/ $800,000	$800,000/ $400,000	$65,000/ $400,000	$400,000/ $100,000	$65,000/ $100,000
8.12%	2.0%	16.25%	4.0	65%

CASE:

Rethinking Strategy at Macy's

While many business leaders claim to embrace change, Macy's CEO Terry Lundgren may have learned that some parts of the past were valuable keys to customer loyalty.

Throughout its 150-year history, the midrange department store had grown by acquiring small regional department store chains such as Bamberger's in New Jersey (1929), O'Connor Moffat in San Francisco (1945), and John Taylor Dry Goods in Kansas City (1947). These stores were usually renamed Macy's within a few years. Besides economies of scale in advertising and back-office operations, the Macy's management thought that customers would be attracted to the cachet of a New York City icon in their cities and towns. While there was often nostalgia for the traditional local retailer's name, the renamed stores generally prospered.

While it had continued some signature items, Macy's would not try to persuade former customers to give the store another look. Instead, Macy's would focus on attracting a new group of customers with exclusive merchandise.

Questions

1. How should Macy's balance the strength in advertising and promotion from having a national branded store with the strength that comes from having a locally branded store? After all, do consumers in Chicago care that much about a Thanksgiving Day parade in New York City?

   Suggested Answer:
   Answers will vary. Instructor has to assist students to understand how to develop a marketing strategy. A fully developed marketing strategy should address the following considerations: the specific target market, location, the specific retail mix that the retailer intends to use, and the retailer's value proposition.
   In this case, Instructor can give some inputs like the following: each store can be designed and merchandised to reflect local tastes in order to recapture a sense of local affiliation, understand local customer preferences for styling, sizes, and colors. Macy's can also decentralize to address local strategies effectively. Such guided discussion could lead students explore through various strategies and address the question.

2. If Macy's continues as a national brand, other than merchandising to local tastes, what can be done to make the store more local?

   Suggested Answer:
   There are many strategies to consider. However, it is important to set out well-defined goals and objectives to accomplish with any merged operation. With those in mind, the target market needs to be fully identified. Then, the location in which the offering is presented (online/store/mixed offering) should be well marked. Planning for the retail mix needed for the target market is also essential. Finally, the value proposition of the additional offerings should be determined. In looking at these areas, the students should suggest a better, more focused strategy for Macy's.

Source: This case was written by Professor Jan Owens, Carthage College, Kenosha, Wisconsin.

TEACHING TIPS

1. This rather short chapter is one of the most important in the whole text because it deals with the importance of planning. All too often retailers tend to react instead of plan and as a result many retailers that were hot yesterday are gone today. It is because of these oversights that the authors placed the planning chapter at the beginning of the text and not at the end. Unless students understand the role of planning in the overall success of a retail operation, they won't understand the significance of the next section of the text—The Retailing Environment. After all, the need for planning is based on an understanding of the changing environment.

2. Have the students locate the mission statement for one of their favorite retailers. After the mission statement is identified, have students critique the mission statement based upon the guidelines for mission statements presented in the chapter. Ask the students to recommend changes to improve the mission statement. These recommendations can be presented and subsequently discussed for further understanding of what makes a good mission statement.

3. If the class has the necessary background, the instructor might want to spend a little extra time on the strategic profit model, Exhibit 2.2, which is a good vehicle for reviewing the impact of various strategic decisions on the retailer's financial performance. A simple discussion of the difficulty of increasing both the net profit margin and asset turnover at the same time can be informative.

4. Students often ask if return on assets (ROA) is a better measure than return on net worth (RONW) for assessing a retailer's financial performance. It is probably safest to use return on assets (ROA) when measuring a retailer's efficiency since making a return on all funds invested in the firm whether contributed by owners or creditors is expected. Using only return on net worth can be misleading if it is high due to high financial leverage rather than efficient management of assets. However, if owners or shareholders want to assess the overall financial performance of the entire retail organization, such as JCPenney or Sears, then use of return on net worth (RONW) is most appropriate since it clearly states what the owners got out of the business (net profit) given what the owners have invested in the business (net worth).

5. The chapter's "Retailing: The Inside Story" box highlights the plethora of changes JCPenney is making to its retail mix in order to reinvent the department store experience and get shoppers back into its stores.

6. While less than seventy-five percent of small retailers engage in a continuous comprehensive strategic planning process to reexamine niches in the marketplace and identify changes, ninety percent of large retail firms do it. Nevertheless, here are some of the key mistakes

retailers make when doing strategic planning:

- Thinking strategic plans are merely extensions of financial plans
- Confusing strategy and objectives
- Expecting consultants to plan
- Too much reliance on in-house staff experts and on quantitative tools
- Focusing on expansion and diversification and ignoring the base business
- Taking too narrow a perspective

7. Pose the question: “How should a retailer determine the proportion and the number of market performance, financial performance, societal, and personal objectives?” This question is intended to stimulate discussion as student’s search for their own understanding of retail’s role in their lives. For example, some students may view that a retailer should serve societies interests and thus should have more societal objectives than financial objectives (The Body Shop is one example of a retailer that employs a great number of societal objectives); while others may view the retailer as an economic entity whose primary purpose is financial. Here, there is no right or wrong answer necessarily, but rather a structured platform upon which students can question the role of retailers in the strategic planning and operations management process.

8. Instructors may also find it useful to have students, either individually or in small groups, create mission statements (conforming to the guidelines for mission statements) and a statement of goals and objectives for popular retailers, such as Walmart, Amazon.com, etc. Then, each student or group’s mission statement and statement of goals and objectives can be written on the board. A comparison of individual/groups perspective is typically quite enlightening as most often each individual’s/group’s perspective is unique, stressing differing aspects of the retailer’s role.

9. The Teaching in Action section presents a SWOT analysis for a popular restaurant, Outback Steakhouse. The authors have found that most students are familiar with Outback and as such the exploration on the restaurant’s strengths, weaknesses, opportunities, and threats provides for an invigorated discussion. In a small class, this exercise can actually be conducted in the restaurant during a field trip to truly bring retailing to life for students.

10. The instructor can use the Teaching in Action SWOT analysis for Outback Steakhouse or the SWOT analysis for TrueValue store found in the chapter’s “Exhibit 2.5” box as a model for completing a SWOT analysis of a retailer. In fact, the instructor could review the SWOT analysis for TrueValue found in the text and then assign the SWOT analysis for Outback Steakhouse as an activity to be done in class or as homework. Then, the instructor can guide the students through the process as practice. Finally, the instructor can ask the students to perform a SWOT analysis for a retailer of their choice. This will cement the concept of

SWOT analysis and heighten student awareness of the various components when discussing other retailers in the course.

TEACHING IN ACTION

SWOT Analysis for Outback Steakhouse

One of the most interesting areas of retailing to observe is the restaurant industry. This industry is highly competitive. Restaurants open, shine briefly, and then die, as low-wage employees take off while costs spiral and the restaurant's popularity and prices decline. One of the most successful restaurant operators to open during the past decade has been Outback Steakhouse. Here is what their SWOT analysis might look like and provides an insight as to why Outback has been so successful. Outback positioned itself between the "low-end" 1960s-era "family steakhouses" like Bonanza and Ponderosa with their $8.00 average tab per person and the white-table-cloth steakhouses with their $50.00 per person tabs.

<u>Strengths:</u>

- What are the major competitive advantages we have over the competition?
  - A "catchy name and atmosphere" that sets us apart from the competition.
  - Veteran managers at all stores as a result of requiring managers to have an ownership in their restaurant. This enables us to keep an entrepreneurial flame burning inside them. This is also supported by an unconventional decentralized management structure that results in an extremely low manager turnover (5.4% vs. a 30%-40% industry average).
  - High wages for staff since we are only open for dinner (Average ticket is $16 with bar tab, thus a typical table of four generates a tip of $10.00 or about $30 an hour in tips. This enables the chain to hire and retain only the best.)
- What are we good at?
  - We have one of the highest cash flows in the industry.
- What do customers perceive as our strong points?
  - High quality steak in a clean atmosphere with excellent service/staff.

<u>Weaknesses:</u>

- What is the major competitive advantage that competitors have over us?
  - A few competitors that are perceived as being at the higher-end of the market, such as Ruth's Chris and Del Frisco's Double Eagle, with a more formal white-table-cloth dinning atmosphere. However, their prices really put them out of our market.
- What are competitors better at than we are?
  - Some restaurant operators, such as Bonanza, Ponderosa, and Golden Corral, have lower prices but not our quality and/or service. However, we have added "value items," i.e.; hamburgers, on the regular menu in order to attract some of these

customers.

- What are our major internal weaknesses?
    - Many competing restaurants operate in better locations in comparison to us. However, by not competing for the lunch crowd, we have no need to operate in high-rent areas. We can operate in lower-rent suburban areas where people are at night.
    - A feeling that some customers have expressed but isn't true—that we are rushing them in order to turn the tables faster. These customers want to enjoy a leisurely meal with friends and family. This is a problem because many other customers want that type of fast service.

<u>Opportunities:</u>

- What favorable environmental trends exist that may benefit our firm?
    - The fact that steak remains the country's favorite entree.
    - A growing trend toward casual dining exists throughout the country.
- What is the competition doing in our market?
    - Many older restaurants will soon be exiting the marketplace and some may try to copy us as a means of survival.
    - Others, such as Texas Land & Cattle Co., Velandi Ranch, and Lone Star Steakhouse have also targeted our market in recent years.

<u>Threats:</u>

- What unfortunate environmental trends exist that may hurt our future performance?
    - Press reports warning consumers about the dangers of eating too much red meat.
    - An economic slowdown that has negatively impacted sales at higher-end restaurants in recent years, but hasn't yet reached the middle-priced types such as ours.