

## THAT MAKES CENTS



### Measuring the future of retail

**Host:** Bobby Stephens, principal, Deloitte Consulting LLP

**Guests:** Rod Sides, vice chairman, US Retail, Wholesale & Distribution leader, Deloitte LLP

Meredith Darnall, SVP, business intelligence & strategy, Brookfield Properties

**Bobby Stephens:** Hi there. I'm Bobby Stephens, and welcome to That Makes Cents. This is a show where we get real about the consumer industry. Each episode, I invite expert guests to chat through a key trend and share their thoughts on the future of retail and consumer products through the lens of that trend.

This episode, we're looking into how success is measured in retail. As consumer expectations, digital, the economy, and other factors massively change the retail game over time, do the metrics, such as same-store sales, that we've typically leaned on, still hold up?

To help us break this down, I've invited Meredith Darnall, senior vice president of business intelligence & strategy at

Brookfield Properties, and Rod Sides, who leads retail and wholesale distribution for Deloitte.

Meredith, Rod, welcome to the show. To jump right in, there are certainly a myriad of trends that have driven drastic changes in retail over the past few years, not to mention the past decade. We'd love to dive into those.

First, tell us more about who you are and what you do, and tee up a couple of trends that you are seeing in retail before we dive deeper.

**Meredith Darnall:** So thank you. I'm happy to be here today. Again, my name is Meredith Darnall, and I lead the business intelligence and strategy team for the retail

portfolio at Brookfield Properties. So we really spend our time thinking about, you know, how are consumers spending time and money and how that's impacting the retail model, and then how are the retailers that are located across our 163 regional malls in the US reacting to those shifts in the business, and how can we best partner?

So I spend a lot of my time really thinking about shopping patterns and exactly how consumers are wanting to interact with their favorite retail brands. And so today, I think it's really important that retailers are creating that emotional engagement with their consumer. And we see the most successful retailers are really doing that, not just in stores or through online, but really across all the touchpoints in which a consumer interacts.

So the retail brands that are successful are those that are really personalizing the experience and making the shopper feel like they are a part of the brand themselves.

**Rod Sides:** This is Rod Sides. I lead the retail practice for Deloitte. Some of the trends we're seeing today in the market is really a rise of alternative business models as a way to enhance the customer service. So that would be one. Two is to understand the ability to shop anywhere, anytime, and have a point-of-sale device in each of our hands is another one of the key things we're seeing in the marketplace today. So a lot of those trends we've seen coming for a while, but I think they're here today, and the future is now.

**Bobby Stephens:** Awesome. We're going to get into a lot of those as we go forward. For me in particular, I really am interested in the notion of—and you both hit on this—sort of making the consumer feel like he or she is part of the brand, part of the experience and, in some cases, making her feel that she can have more control over the experience.

So one question I really have is, why did we go after metrics? Why did we start down this path to look at what the metrics are today, what the metrics might need to be for the future?

**Meredith Darnall:** Metrics are important, not just to the retail business, but all the retail partners as well, because historically, we see that the metrics were looking at the retail business in terms of very specific business protocols. So stores were measured using one set of metrics to determine their success, online and digital assets may be measured differently, and then you may have had individual metrics as to how retailers were thinking about their marketing efforts, as well as other operational strategies.

And what we find if we continue in this traditional metric view, we're not seeing the whole story and seeing what each touchpoint is contributing to the overall value of the brand. So really, we believe that retailers today could be operating with insufficient information to really understand

the holistic value of the brand and start to make changes to their strategy or really grow their strategy in meaningful ways.

And it's not a belief that the traditional metrics aren't useful anymore, it's really thinking about "How do we expand the metrics that we are using?"

**Rod Sides:** So, Bobby, the view that we had within the firm was that looking at standalone metrics and traditionally same-store sales as an example, or sales per square foot, doesn't tell the whole story. So as we've seen digital start to disrupt the retail space, we didn't change any of the metrics over the last 25, 30 years, and we still measure success in the same way, and yet, business models have evolved.

What we found to a large degree was that growth was happening with the digital footprint more so than, say, bricks and mortar, but the two combined made for a much more compelling case. And if we started to look at how we measured performance historically, it just left out just half the story, as Meredith was talking about.

So we thought the time had come to go have the conversation. We felt like the playing field wasn't necessarily balanced or perhaps were using a different set of rules, depending on where entities were in their development stage. And so the time had come to have a real conversation about it in the marketplace, not to try to find the right four or five metrics, but more importantly, to make sure we understood essentially the profit thesis that stood behind many of the entities that are coming into market today. So that's why we chose to take this on at this point in time.

**Meredith Darnall:** I love Rod's point. I think that's absolutely correct. And to illustrate his perspective, we were speaking to an international apparel retailer who was discussing how they're evaluating their store portfolio, and their example was, they have a store that if you look at it through their traditional lens of sales per square foot, as well as a few other kind of key traditional metrics, it was the second-worst-performing store in their portfolio and should be considered for closure. However, when



they started to assess its impact in terms of driving customer acquisition, helping reduce fulfillment costs and really helping to build brand impressions to consumers, it actually was the second-highest-performing store within their portfolio.

So I love that example, because it really illustrates the holistic strategy that needs to be applied, and especially when it comes to thinking about stores, that's especially critical because the store is still very meaningful to the consumer.

And so how we value the contribution of that store, we think needs to evolve to really reflect the total role it plays within the retail strategy.

**Bobby Stephens:** So building on the store and the role that the store plays, I think, Meredith, you're going to come at it from a really unique perspective in terms of a landlord, as thinking about how do I maximize the success of the business overall and the partnership long-term, right? Not thinking transactionally for a time-period-over-time-period, but how do I make sure that this brand can be successful in my properties across the portfolio?

A lot of places we're seeing brands kind of lean in to be more destination stores, more experiential retail, and I'm sure you're seeing pockets of that as well. I would love for you to talk a little bit more about that, how you're seeing that impact both consumer engagement, but also how that impacts how you look at your overall business and how you engage with your retail partners when thinking through that type of experience.

**Meredith Darnall:** Absolutely. The experiential retail is becoming very important, and retailers are starting to understand that it's no longer about just a transaction. And I love that we have many of our major national brands who have decided that their first and foremost priority, when they really think about the shopping experience within their stores, is to drive customer engagement, and really emotional engagement.

And so what we've really seen are retailers who have embraced this idea and have started to open stores that have such an experiential and kind of fun element, but most importantly, that element's authentic. So the experience isn't just set, it doesn't necessarily need to be gamified, it doesn't have to be offering something unusual. The best experiential retailers are those that are thinking about what the brand means to the consumer and really creating an experience that's authentic to that brand ethos and how the consumer wants to interact with it. So particularly in the beauty area, we've really seen a lot of our retailers embrace this idea and create a sense of fun. So when you're going into the store experience, it's not just featuring the product, there's a story behind the product, you're interacting with the sales associates, and there are also digital touchpoints that come into play that are really enhancing it overall and allows the consumer to really customize that shopping experience for themselves.

So we see that as very important because one, it starts to build interest and differentiation in the retail experience, but also blends very well with our centers because they have now, you know . . . We see our centers as positioned to really be a community offering, a community gathering space for retailers. And so now we can collectively join strategies with the retail brands to create that sense of community, to create a place where consumers want to come and spend time, they socialize, they learn something new, and they're really able to discover new products, new brands, new trends, kind of new ideas. And are interacting with our venues in a very different way.

**Rod Sides:** To build on Meredith's point around venues, the role of venue has changed over the last 10 to 12 years. So if you think back to where retail was, say, around 2000, most of the inspiration that happened within retail started at the store. So you would come in, you'd get ideas, you would browse, etc. And so that became the center to go discover new products.

But then with digital and the rise of digital, what we've found is that folks are starting their journey now. So our most recent holiday study that was published back in October, we ask about 4,000 folks to tell us, "Where do you start your shopping journey?" And many start online. So the first two areas are either online retail or in search engines. The No. 3 response was in stores.

So the role of the store has changed, and it does have to have that element of excitement. You know, kind of the experiential piece is really important to be able to complete the entire journey over time. And so as we've seen that role change, again, when we look at how it plays a part in marketing and not just selling the product, that's part of the reason why we needed to spend time thinking about the metrics.

**Meredith Darnall:** Rod, I love what you're saying about venues are changing, and to take it a little bit further, the role of the store format can also evolve too. I think traditionally retailers would have one prototype, and that prototype would come in and no matter where you were in the United States, if you walked into a shopping center and you saw that retailer, the store experience would be the same. But as we have a better understanding of what drives consumer behavior and we have better data, frankly, that we can analyze and understand how the store is adding value for that retail brand, we expect store formats will evolve. So if customer acquisition becomes the goal in a given marketplace, the retailer could choose to have more of a flagship experience, offering them something that's more brand-immersive, or really focusing on using the store as a marketing platform or really a marketing activation tool to drive that acquisition.

In other locations, that store may really primarily serve as a fulfillment center, offering something convenient so the consumer can bring back returns or pick up items. So that store format may look a little different, and that's when we really start to think about the future and where metrics become important. The more we start to understand and really rethink how we ascribe the value of that particular location to a retail brand, the store formats could evolve, become much more localized to what that particular consumer needs, as well as drive more productive sales.

**Bobby Stephens:** Meredith, you've been talking a lot about the brand experience and thinking through the portfolio of stores, even within one brand sort of set of stores and, Rod, you mentioned earlier that the notion of alternative business models and how retailers are thinking differently at all stages and all sizes about how they're driving revenue. So I'd really be interested to understand how those two things are intersecting, and how are potentially alternative business models enabling retailers to think differently in their stores, yet supplementing growth in other ways, or vice versa?

**Meredith Darnall:** It's interesting now that retailers are really using a lot of strategies for the customer acquisition. So they're incorporating models like memberships, subscriptions, offering credit cards, and really finding a way to extend the relationship beyond the simple transaction that day. Our opportunity is really to understand the attribution of those particular alternative models to the store itself and really ascribe a value. We see retailers that are attempting to do that, and there are several national retailers in the US that are really being leaders in the strategy and are sticking to not just measure their stores in terms of individual sales, but really are looking at customer lifetime value and how each location is playing into prolonging and really sustaining the relationship between the brand and the consumer.

**Rod Sides:** You know, Bobby, what we've found with some of these alternative business models is that they're trying to make it easy and convenient for the

consumer in a variety of ways. So it's about more than extending the market basket or share wallet from a consumer perspective, but it is kind of creating a different way to create value for the consumer. So to me, the intersection between the two is really, really important because, as we've seen the rise of alternative business models, almost every company I talked to today, that's one of the first two or three questions that come out of the executive branch is to say, "Tell us, what are others doing?" How do I monetize the assets that I have? Because the model of delivery to the consumer has gotten so expensive over time, because now I have to pick the product in the store. I may have to walk it out to you. It's just a different element of cost that's out there. So being able to enrich that experience with the consumer is really important and having a physical footprint to be able to do that is a big part of the model that we're seeing emerge.

What you find with many of the clients that we serve is they're fast followers. If they see something that works, that resonates with the consumer, many of them are going to make that move. The challenge in the digital world is there's a huge first-mover advantage, and so if you're the first move in the market—we've seen it over and over with different types of services—that is a competitive advantage. So I think a lot of companies are looking for that as a way to get out front and differentiate in the eyes of consumers. So when we talk about metrics, it's really important to understand if that's part of the core strategy. We're not going to opine on whether it's the right strategy, but being able to share that profit thesis with key stakeholders is really important to understand the kinds of strategic bets that are being placed by management so that, as an investor, you could determine whether that's something that you want to be a part of or not.

**Meredith Darnall:** I agree, Rod. I think it's very interesting that it is about driving that convenience to the consumer and thinking about where those investments are meaningful and being a leader. What's really exciting now is that there are national retailers that are starting to report actual results where they've gained efficiencies in costs or actually gains in margin because

these types of investments, they really are serving the consumer in the way the consumer wants to be served, and allowing the consumer more convenience is really paying off in the financial results. That's encouraging because it's really a relatively fast implementation for some of these brands, even as first movers, and the payoff is there. So it's the right time for us to start thinking about the, really, how do we start to expand the new metrics, be able to scale some of these solutions across a store fleet or across physical locations so that the benefits can be realized for more and more national retailers, and we're molding into giving the consumer greater choices.

**Bobby Stephens:** So let's get to the , I don't know, what is it, billion-dollar, trillion-dollar, more question. What types of metrics or specific metrics are you starting to use internally as you manage your own businesses, but externally with your partners and clients to get a better view of the business or, sort of put more frankly, what metric should retail be looking to use as we move forward?

**Meredith Darnall:** We're really focused on looking at our retention of consumers across our centers and understanding how frequently they're visiting, what their dwell time looks like, and beyond that, how are they interacting with the venue and how they want to really shop across the different brands. The more we understand about the consumers that are coming within our centers and sharing that back with our retailers and helping them see not just what's occurring within their four walls, but what is their opportunity outside to capture and what they may be missing and how that can influence their customer acquisition strategy.

It really becomes important as they're considering "Where are the best places to think about where I positioned my stores?" It's interesting that we've been talking to the head of real estate for a major national brand, and he shared that he really thinks it's no longer about an occupancy formula and deriving the value of stores, but really we have to be thinking about geography because having a localized view and financial strategy is going to be very important. As we

look at how consumers are engaging both with stores and online, we know in some areas digital engagement may be higher in certain markets and less in others.

If it's higher, you need to have the exact right store location. You may not need many stores, but you need a store located right central to not just your existing consumers, but the consumers that you want to capture.

**Rod Sides:** We tried to bubble it down into two major categories. The first thing we'd want to understand is, how is value created? And then how's value captured? Because it's one thing to create value. The big question is how you pass that value on from a shareholder perspective. So let me start with the value-creation ones. As we thought through it, we thought there were really two things we wanted to understand. First of all, as Meredith's talking about, customer acquisition is very important. So we suggest a measure that looks at sales per unique customer. And so what we're after with that measure is to really understand what's it cost to be able to create more market basket or share of wallet across the consumer step. So how much investment is needed to be made there, etc. The challenge with a lot of retailers, they don't really want to give unique customer account per se, but the sales number already exists. So from that perspective, it's reasonably easy to get at that particular number, and we can start to see if they are winning more on average or not.

The second measure, which is a little more controversial, is to understand retail profit per transaction. So what we're after there, what we're suggesting, is let's take the sales number and let's back out specifics around subscription revenue, let's take that out. Let's take out credit card revenue that might be out there. Let's take out ad revenue that may be in addition. You could go so far as to take sales promotion and take that out.

So what is the profit that we're making for each unique product that we sell? And the reason why we think that's important is, there's a number of players out there that make all of their profit, for the most part, either on subscriptions or on memberships. Again, it's not a bad business model necessarily, but it does illuminate

what the profit thesis is for that particular organization. So we think that's a really important measure. So as a stakeholder, you understand that the sale of product is being subsidized by a different part of the business. Again, not a bad issue, but if you think about where we've been in the last 10 years in our industry, a number of activist investors have come in and really encouraged retailers to spin off their real estate portfolio to create more of what upholds shareholder value.

But at the same time, we've allowed a lot of these alternative businesses to creep up. And in some certain instances, these are billion-dollar-plus businesses that have evolved. And yet there's not really a call for us to be able to separate those businesses per se.

But we believe that those two would give us a pretty good idea of "Am I making money and selling product or not?" or "Am I selling something else?" And if I'm selling something else, that unique experience for the customer is of high value. And so as a result, that's where we had some views toward "How do we create value?" Now, from a capturing value perspective, a lot of the standard metrics that we've used to sort, they're still there. Free cash flow is one. We looked at revenue growth overall. We don't want to penalize someone for coming up with an alternative business model. So that would be a second. And then from there, we would go to maybe a third model that would look at ROIC, return on invested capital.

**Bobby Stephens:** So to wrap up, let's get your opinion on something. What do you think it's going to take for an industry that's been doing something the same way for quite a while to really make a change and adopt these new metrics?

**Meredith Darnall:** From my perspective, I think it's really about changing partnerships and really changing the dynamic of what was the landlord-tenant relationship. And today, what we have proven through our analysis at Brookfield is that Brookfield and the retail brands rise and fall together. Collectively, we can drive to a better result and a mutually beneficial result for both of us. So I'd like to see the dynamic move from

just tenant-landlord really into more of a partnership model that includes joint business planning and setting goals collectively. Additionally, I think, again, it's going to be having more discussions like we've had today and bringing more stakeholders to the table and really speaking honestly, not just among the retailers and ourselves, but also among the investment community so we continue to advocate for the importance of the expansion of metrics.

**Rod Sides:** So I think to get adoption, what we're going to have to find is an increased dialogue across the industry key stakeholders. I think as the analyst community starts to ask questions, as key stakeholders start to talk about the profit thesis and are pretty open about it, that will drive us to a different point where we'll have different discussions. So from my perspective, I think it's . . . This is the beginning of a journey to start the dialogue and use this really as a springboard to start asking some real questions about what does the profit thesis and the future of retail look like.

**Bobby Stephens:** Awesome. The way I'm hearing it, how we keep score in retail will have a profound effect on how companies operate on all sides of the market, from retailers to suppliers to real estate companies. Also, it sounds like, if done right, it can help us normalize the interaction between physical, digital, and emerging business models that are sure to continue to increase in the retail landscape.

I think it's also a critical language that all players need to speak and agree upon as we move forward for the overall success of the industry. So I really, really appreciate the time you spent here.

For just a bit more on this topic, listeners, you could find a detailed report called *The future of retail metrics* on Deloitte.com.

But before we go, thanks, Meredith, thanks, Rod, for joining me on the show today and sharing some of your amazing expertise on retail and retail metrics.

**Meredith Darnall:** Thank you.

**Rod Sides:** Thank you, Bobby.

**Bobby Stephens:** You can listen on your favorite podcatcher, whether it be Apple podcast, Stitcher, or Spotify. Simply search for That Makes Cents. Connect with me on social media: Bobby Stephens on LinkedIn or @bobbystephens on Twitter.

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