



Future of Retail

Transitioning from 'retail'
to 'consumer commerce'

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Foreword



Paul Martin
Chair, Global Retail Steering
Group & UK Head of Retail
KPMG in the UK

This is time of deep reflection for the retail sector. After the widespread disruption the sector experienced in 2020 and the positive news of a range of vaccines now emerging, retailers must start to look towards the 'new reality' that will follow. The only certainty is that many aspects of retailing will not return to the way they were before the words 'COVID-19' sent shudders around the global economy.

It is important to highlight that many of the changes we have experienced recently — to buying behaviors, to workforce models, to channel mixes and to business models — are trends we have been speaking about for the last decade. In many cases, COVID-19 has accelerated their progress by 5–10 years. The need to act and to do so at pace has become even more important. As is so often the case, new challenges bring new opportunities to create and dominate markets with new business models. Never has that been more true than today.

Moving from today to tomorrow will not be easy. It will require retailers to take a fresh look at the trends influencing the future, their long-term ambitions and their current capabilities to chart their path forward. It will necessitate a clear view of how current trends are accelerating future business models. And it will take a clear and practical path to implementation.

In this point of view, we explore the critical signals of change currently influencing the global retail environment and *why* the market is changing. We describe *what* the winning business models of the future will look like. And we explore *how* you can transition from today's 'as is' reality to tomorrow's 'to be' vision, describing the key capabilities and strategies you will need to move your organization into the future.

As our title suggests, we view this transition as an evolution of 'retail' towards 'consumer commerce' where, increasingly, consumer-facing businesses offer products and services without the need for a physical store legacy. As they evolve, many may start to ask if they should really still be called retailers at all?

We hope this point of view provides leaders and stakeholders in the sector with valuable insights to help them move into the future with confidence. To discuss these themes in more detail, or to explore how KPMG can help your organization accelerate its transformation, we encourage you to contact your local KPMG member firm or any of the authors listed at the back of this publication.

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Signals of change: Disruption has accelerated

Long before COVID-19 became a ubiquitous threat, the retail sector was undergoing massive transformation.

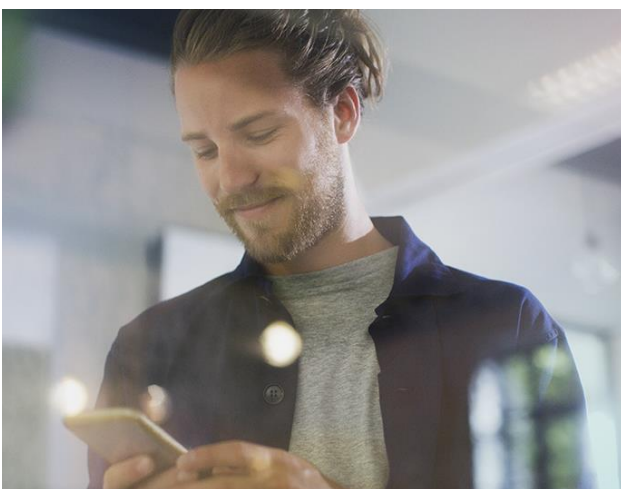
The recent crisis has drawn a stark line under any indecision: the choices retailers make in the coming months will influence their success over the next 5 years or more.

Those retailers able to quickly embrace new consumer and workforce trends will almost certainly have a competitive advantage in this age of accelerated disruption.

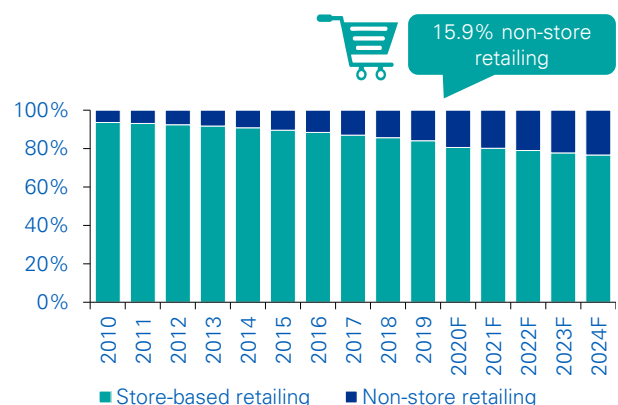
The current disruption has only accelerated existing trends. Indeed, the pre-pandemic shift can be easily illustrated in just a few stats. E-commerce retail sales are expected to increase by almost 17 percent (in CAGR terms) between 2010 and 2024.

The next fastest growing channel (Discounters) will only achieve 3.4 percent growth over that time. Then consider the fact that, before the pandemic, almost 16 percent of sales were already flowing through non-store retailing. The shift towards online and digital channels was already well underway.

The pandemic pushed disruption into hyperdrive. In some markets, consumers were essentially mandated to limit themselves to online shopping during lockdowns. In-store retailing was put into a timeout. Some business models thrived while others were nearly choked into a premature demise.



Global store versus non-store



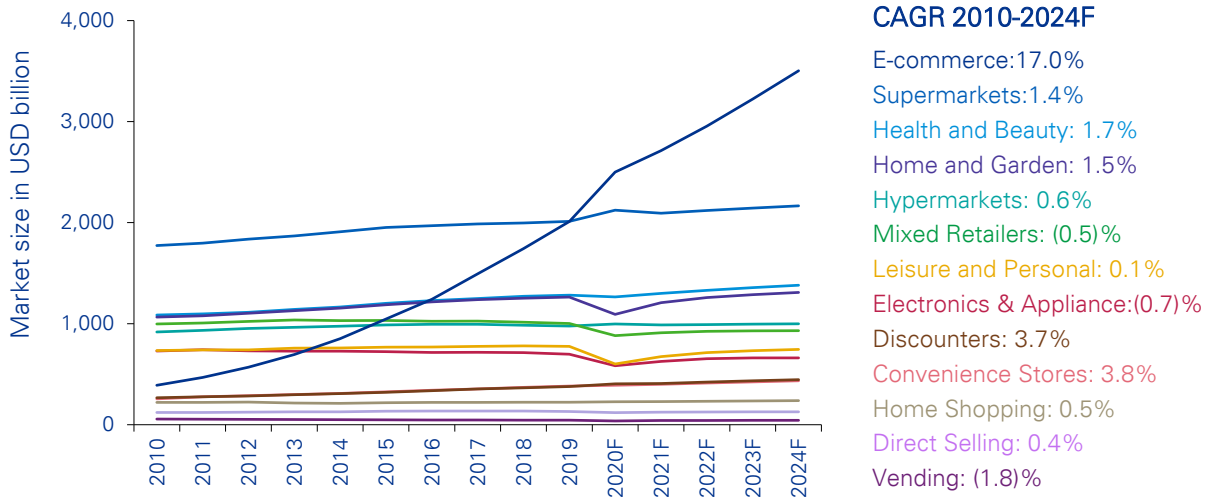
Source: Euromonitor, accessed 19 November 2020



Yet while real GDP is expected to have declined by 3.1 percent globally in 2020, some economists expect growth of 5.7 percent in 2021. Inflation will also start to rise again. And, as the pandemic comes to an end, we expect to see consumers start to — once again — evolve their buying patterns and purchasing priorities to reflect their new reality.

Those retailers able to quickly embrace new consumer and workforce trends will almost certainly have a competitive advantage in this age of accelerated disruption.

Global channel overview



Source: Euromonitor, accessed 19 November 2020

Signals of change: Business models and partnerships

As store-based retailing moves beyond its zenith, the growth of platform ecosystems alongside omni-channel are driving the next wave of competition and business model evolution.

Store-based retailing had already passed its zenith. The pandemic put additional pressure on non-digital business models.

While many physical stores will likely return to growth over the coming years, those looking to drive growth through physical stores alone will surely struggle. This places a question-mark over the overall viability of the retail business model. Until about 10 years ago, the retail business model had remained largely unchanged for decades, if not centuries. The most successful retailers were those that were the best at sourcing desired products, shipping them and selling them in physical locations. Now, with routes to market evolving, this recipe for success has changed. The legacy retail business model has been disrupted.

To succeed in the future, retailers will need to evolve at pace and become either platform ecosystems, true omni-channel players or smaller niche-focused specialists.

This transition will require pace, capital and capabilities — with not all of these available in abundance for most organizations, many will need to proactively consider partnerships.

Platform businesses models already dominate many consumer-focused industries. Indeed, the 10 biggest companies in the world (by market capitalization) are all platform players. In many markets, platforms dominate: Alibaba, a Chinese e-commerce market, is gaining an increasing larger market share with Baidu dominating the market for search, and Paytm moving to capture India's payments market.

Investors certainly seem to believe platform business models will continue to dominate the future business landscape. According to a 2019 study*, platform players enjoy average revenue multiples of almost 9, compared to traditional linear businesses which enjoy multiples of between 2 to 4. Over the past decade, the market capitalization for the top seven platform businesses grew by more than 1,000 percent.

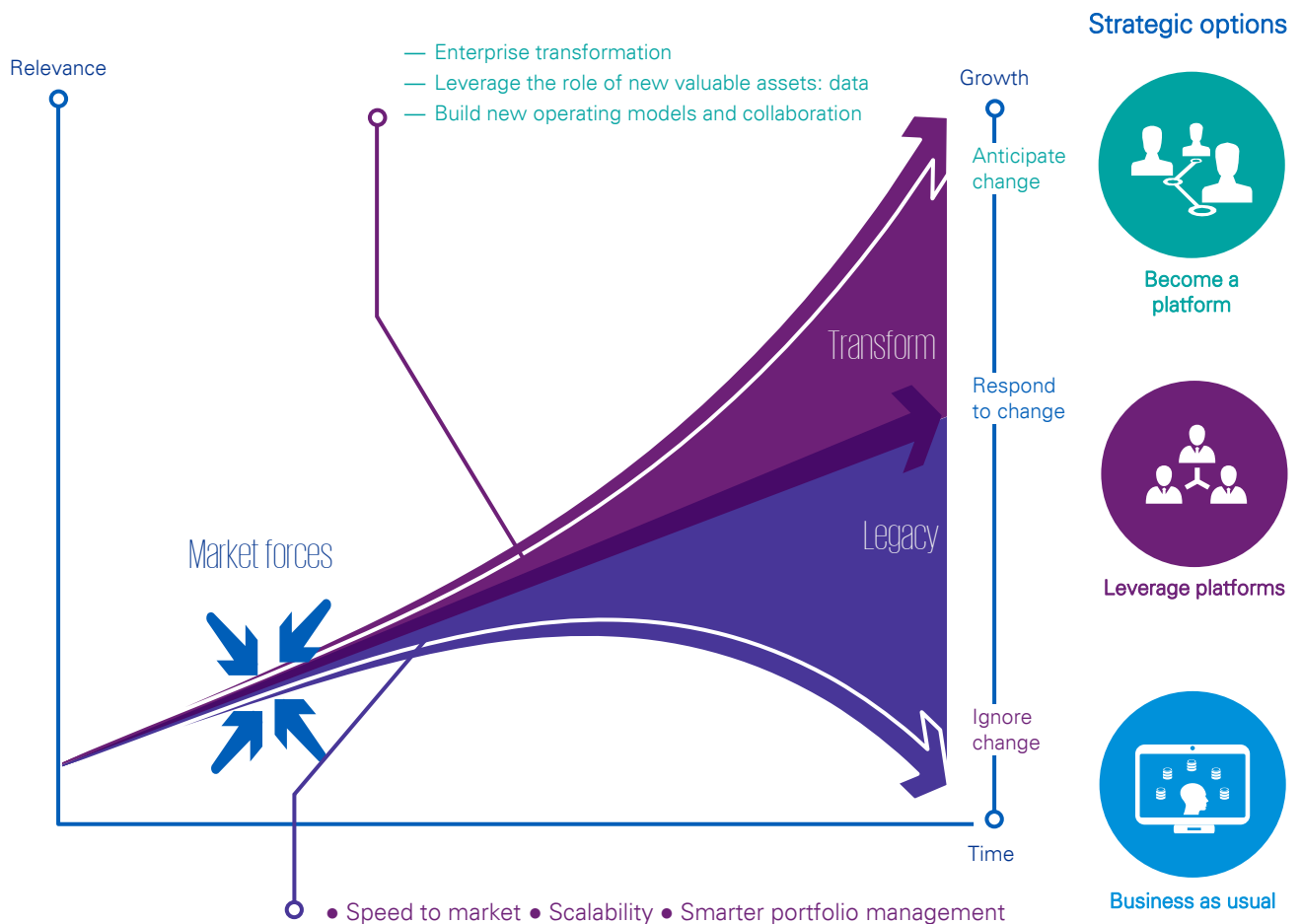
/// To succeed in the future, retailers will need to evolve at pace and become either platform ecosystems, true omni-channel players or smaller niche-focused specialists. ///

*Note: (a) Market Capitalization as on 24 July 2009 and 03 July 2019, sourced via DataStream and S&P Capital IQ; accessed 3 July 2019

In the future, we expect to see platform businesses take their models one step further by offering their capabilities directly to other retailers 'as a service'. Essentially, these partnerships serve as ready-made 'white label' platforms that provide retailers with a quick, proven off-the-shelf option that enables retailers to evolve and scale without investing massive capital into developing the capabilities in-house.

To remain competitive in this environment, retailers will need to define their future strategic path. Those who choose to transform for the new reality will need to decide what role platforms will play in their future business models. However, our view suggests those who choose to ignore change and continue with business as usual will find it increasingly difficult to remain relevant over time.

What's next? — Alternative Strategic Paths:



Signals of change: Customer

Customer expectations and needs are rapidly changing as retail moves from being a 'push' (i.e. B2C) to a 'pull' (C2B) model.

Customers are in charge. Even with lockdowns, travel restrictions and economic uncertainty, it is clear that consumers retain the power in the retail relationship. Indeed, as consumers flock to online channels and platforms continue to capture market share, consumer choice is expanding exponentially, making it increasingly difficult for retailers to retain their customers.

Shoppers want to pay less for more and will search until they find a suitable solution



81%



of customers do online research before committing to purchase²

89%



of these customers begin their buying process with a search engine²

75%



of people don't think that quality goes hand in hand with high prices²

Source: Nielsen Total Till, Retailer Market Share, Nielsen Homescan 2020 KPMG global retail trends 2019

Going forward, we see six key drivers of consumption that will shape consumer purchasing decisions:

01

Value

The hunt for value is increasingly being driven by price-savvy consumers. With growing pressure on household budgets, consumer perception of value is changing. Shoppers want to pay less for more and they are demonstrating that they are willing to search until they find what they are looking for.

02

Convenience

Consumers have less 'free time' and are therefore looking for seamless experiences they can use anytime, anyhow and anywhere. Customers are showing a growing preference for online ordering, curbside pickups and home delivery. They are also looking for easy (and free) returns

03

Experience

Customers are now engaging with retailers beyond the traditional transaction, forcing retailers to focus on delivering more tailored, seamless, responsive and consistent customer experiences. In particular, customers are looking for more immersive and more unique experiences from their retailers.

04

Choice

Even before the pandemic, customers were gravitating towards two ends of the choice spectrum — either online players with almost unlimited choice, or discounters with limited selection but good value for money. Product range is becoming a critical differentiator among retailers.

05

Privacy and security

While, on the one hand, consumers are quickly becoming aware of data privacy risks and concerns, they are also increasingly willing to trade some risk in return for a seamless buying experience with trusted brands. So, while 71 percent of consumers say they are worried about data privacy, 66 percent say they are willing to share their data.

06

Purpose

Consumers are increasingly aware of retailers 'behavior, Those who demonstrate the right behavior while ensuring their purpose is aligned with customers' values and expectations will hold a strong position.

Signals of change: Cost of doing business

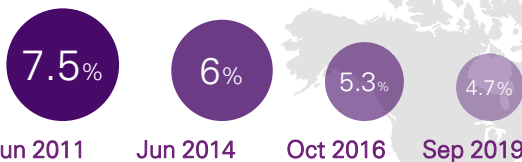
With retail margins under increasing pressure and costs increasing across multiple aspects of the value chain, most recognize that conventional forms of cost cutting are no longer enough to shore up margins and ensure the business is fit for the future.

Margins have been under pressure for years as customers increasingly look for differentiated experiences, across multiple channels, while prioritizing low cost. The economic uncertainty and volatility that is following COVID-19 is only accentuating the pressure.

Higher costs to manage new e-commerce supply chains, growing pressure from suppliers to pass on raw material costs, escalating labor costs, pandemic-related safety measures and the need for new investments into digital capabilities have all rapidly eroded retail margins.

North America

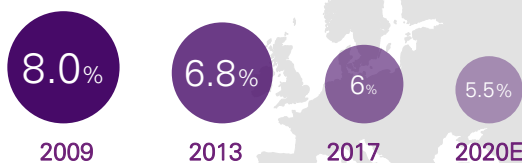
EBIT Margin (% , rolling four quarter basis)



— UBS estimates

Europe

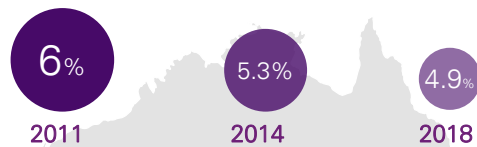
EBITDA Margin (%)



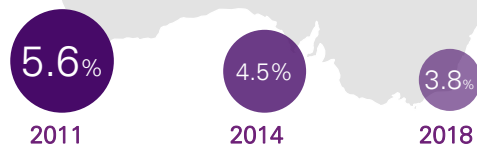
— IMF, Scope ratings

Australia

Net margin (% , Food)



Net Margin (% , Non-food)



— Reserve Bank of Australia

Note: Most statistics are closest approximations from graphs and might not be exact in terms of decimal places



Retailers recognize they will need to go further with optimizing their costs if they hope to return their businesses to profitable growth in the years ahead. Those retailers deemed non-essential during lockdowns may need to cut costs by 20 to 50 percent. Even those deemed essential through the pandemic will need to reduce costs by 10 to 20 percent of current levels.

Our view suggests there are four levers to sustainably reducing the cost of doing business in today's environment.

Range and assortment

01

Retailers will want to review their product range to strategically select the right product assortment to boost efficiencies and increase profits. Rationalization of the product range will enable higher inventory turnover and lower costs, streamlined in-store logistics and enhanced buying power, as well as opportunities to optimize the workforce.

Real estate review

02

It's time retailers reconsider their brick-and-mortar assets and establishments. Given the boom in online shopping and the trend towards 'showrooming' (where consumers can test products before purchasing online), retailers should rethink their physical footprint and the value these assets deliver to the organization and the customer experience. At the same time, the rental business model is increasingly shifting towards turnover rent.

Workforce optimization

03

With customer service and experience top of mind, retailers should be assessing where technology can help automate tasks, thereby making workforces more productive and customer-focused.

Technology and supply chain improvements

04

Pivoting investments from store openings and refurbishments to technology and supply chain improvements will be a central part of the digital transformation, enabling retailers to uncover new cost savings while simultaneously growing their businesses. Some Robotic Process Automation (RPA) deployments in retail, for example, have been shown to cut costs by up to 50 percent.

Signals of change: Purpose



Customers want businesses to stand for something bigger than the products they sell. The recent pandemic has only sharpened consumer preference for purpose-driven organizations.

Studies show that purpose-driven brands enjoy a virtuous cycle that can lead to higher value growth, better KPIs and improved share of wallet.

/// *Purpose is different to the company mission and vision. Purpose explains why your brand exists — it is an articulation of the positive impact the brand has on peoples' lives, society and the environment. ///*



Nearly two-thirds of consumers around the world said they would decide to either buy or boycott a brand based solely on its position on a social or political issue¹



Brands with a clear 'purpose' and a high impact on people's lives grew 2.5 times more than brands with a low perceived impact



Meaningful brands generated almost triple the purchase intent in non-customers and more than double the repurchase intent in existing customers²



Meaningful brands saw share of wallet rise by nine times versus non-meaningful brands



They also outperformed the stock market by 134 percent

¹ Edelman News and Awards, 'Two-thirds of consumers worldwide now buy on beliefs', 2018
² Meaningful Brands survey, 2019

Purpose is different to the company mission and vision. Purpose explains why your brand exists — it is an articulation of the positive impact the brand has on peoples’ lives, society and the environment. More than just an aspect of the Corporate Social Responsibility (CSR) agenda, brands with purpose demonstrate their commitment to that purpose in every action and interaction.

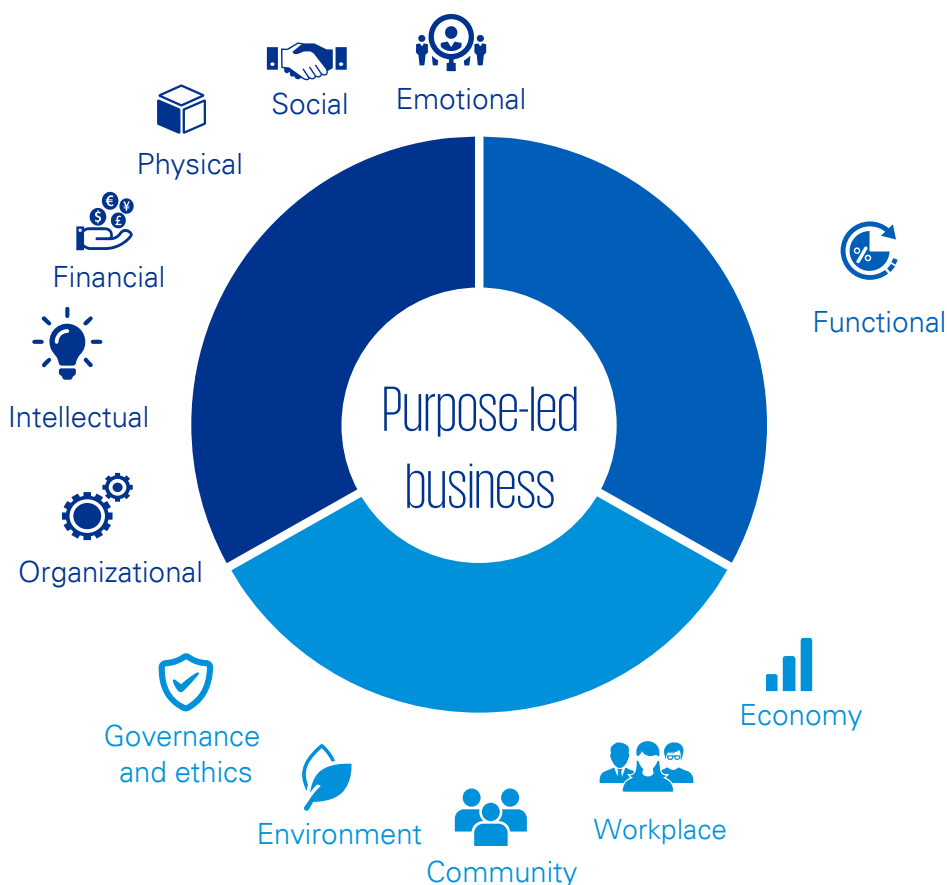
Indeed, customers expect their brands to do more than just talk a good talk. According to the Meaningful Brands survey, only around 38 percent of consumers think companies and brands currently communicate honestly about their commitments and promises³.

Recent backlashes against perceived instances of corporate ‘green-washing’ suggest that consumers are setting a rather high bar for retailers to pass.

In this context, organizations will need to consider how they plan to measure and audit their purpose. They will also need to think carefully about the communication mechanisms they will use for showcasing these outcomes to their various audiences (consumers are not looking for the same content or context as financial stakeholders).

Purpose is an idea beyond profit

Purpose is different from the ‘vision’ or ‘mission’ and explains the reason ‘why’ a firm exists — it is the positive impact a brand has on people’s lives, the society they are a part of, and the environment they live in.



■ Personal benefits i.e. improving peoples’ lives

■ Collective benefits i.e. role in society

■ Functional benefits i.e. does the product/service deliver?

Source: Meaningful Brands survey, 2019

³ Meaningful Brands survey, 2019

A look at the future: Winning business models emerge

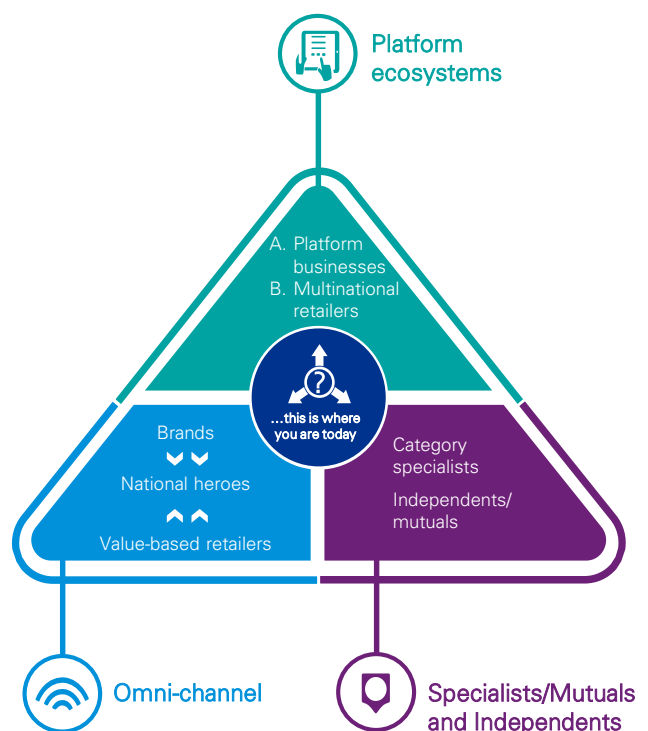
As described in the previous chapter, there are various factors that are driving change in the retail sector. Although these signals of change are not new, COVID-19 has in many cases accelerated their importance further. We predict they will have significant impact on the sector and will define which businesses will succeed or fail in the future. Over the next 5–10 years, we expect to see seven types of business models emerge as retailers evolve to meet changing customer expectations and market dynamics.

In this future ‘consumer commerce’ landscape, traditional retailers with a heritage in bricks and mortar will compete against businesses with deep capabilities in data, technology and supply chain. In some cases, the only real common denominator between these businesses will be the fact that they all sell products and services to the consumer. With a range of new routes to market emerging and evolving, today’s retailers will need to decide which model they want to operate in the future or risk their business failing.

At the top of the triangle, existing platform businesses and multinational retailers are transforming themselves into platform ecosystems who will be taking larger market shares in the years to come. On the right side of the triangle, category specialists and independents are positioning themselves to showcase their strengths as local, purpose-led organizations.

The left side of the triangle will be occupied by ‘true’ omni-channel organizations. They will have to focus on the delivery of a seamless, customer-centric, channel-agnostic proposition. That being said, this positioning will be comfortable for many retailers and competition in this space will be fierce. A ruthless focus on costs will be required.

|| Retailers will need to decide which model they want to operate in the future or risk their business failing. ||



Platform-based businesses: Platform-based businesses have grown in prominence over the last 20 years by harnessing the digital market to deliver their offering. In some cases, platform business models facilitate the exchange of products and services between two or more user groups — a consumer and a producer. They are increasingly dominating the go-to-market channels and take a broader approach to target both B2B and B2C offerings. Platforms provide a retail ecosystem offering customers numerous propositions, from retail products to banking services, in order to maximize customer lifetime value. These organizations are also seeking to 'white-label' their service offerings and provide their Platform as a Service (PaaS) in order to grow their revenue streams.

Direct-to-consumer: Direct-to-consumer is an increasingly important business model for manufacturers, especially with the acceleration of online shopping. In some cases, brands are building or buying their own capabilities to deliver this proposition. Many are leveraging platform businesses in order to bypass traditional retailers and gain additional margins.

Multinational retailers: Multinational retailers are large, international businesses that have expanded to enter new markets to grow their customer base and enhance their capabilities. Over recent years, they have changed their go-to-market strategy in many cases by acquiring digital direct-to-consumer or service-focused businesses. They are using these acquisitions, and their own organic growth to increasingly transform themselves into platform businesses to expand the monetization of their product offerings from traditionally only selling physical products and services to a wider array of propositions.

Value retailers: Value retailers have been one of the fastest growing physical formats over the last 10 years. They aim to undercut the market by providing products and services at a lower price than regular retailers. Their leaner operating and business models have, in many cases, enabled them to deliver more profitable returns than many of their peers. They will now need to establish or evolve their online value proposition to profitably survive in the future.

Category specialists: Category specialists offer unique and focused products and services targeted towards a specific retail category or a defined customer. Specialists may provide a platform for brands that fit their business model or may deliver their own product directly to consumers. Category specialists often offer considerable expertise in product innovation and enjoy a loyal customer base.

Independents/mutuals: Mutuals are retailer -or consumer- owned businesses that aim to focus on the needs of their members, rather than simply increasing profit, thereby uniting retailers and customers under a common goal. Mutuals and neighborhood retailers have the unique ability to directly gather and respond to changing community needs, and are often experts in showcasing their values to the communities they serve. Alongside the mutual we have witnessed independent local retailers re-emerge as viable players, often utilizing online as either their core or an additional channel to market.

National heroes: National heroes are often well-established retailers that have created a strong local brand and identity to deliver a range of targeted products and services. National heroes often have the advantage of securing a loyal customer base and leveraging loyalty programs to meet customer needs. This will likely not be enough to prosper in the future though. As this category comes under increasing pressure from value players and direct-to-consumer businesses, they will also need to focus on creating partnerships to tap into synergies and create scale. For example, they may consider establishing Generation 2 Buying Groups to cooperate with non-geographically competing peers in order to protect themselves against the other types of winning business models.

A look at the future: Foundations of a successful business model

Retail businesses will need to decide which business model(s) will set them up for a successful future. In that context they can choose to either buy, build or partner. If they decide to build, planning for the transition from their 'as-is' state to tomorrow's 'to be' state will require careful consideration. We believe, depending on the type of business you choose to become, there are a set of fundamental capabilities a business needs to develop and deliver.

These capabilities help retailers define a customer-centric approach to digital transformation that connects the front, middle and back offices. Enhancing these capabilities will enable retailers to ensure that every process, function and relationship of the organization is focused on meeting customer expectations, creating business value and driving sustainable growth.

We have defined 8 key capabilities that will be of critical importance to navigate the future 'consumer commerce' landscape. In fact, our research shows that firms that make a moderate or significant investment in all eight capabilities are 2.1x (on average across sectors) as likely to deliver a customer experience that exceeds expectations, successfully execute on one or more customer-centric objectives and achieve ROI on one or more metrics.*



*Note: (a) Base: 1,299 professionals involved with customer-centric strategy decisions.

Source: A commissioned study conducted by Forrester Consulting on behalf of KPMG, September 2018.



Insight-driven strategies and actions

The ability to foster an analytics-driven culture that leverages an integrated customer and product angle to deliver optimal experiences across all touchpoints while addressing customer data integrity, privacy and security.



Innovative products and services

The ability to deliver relevant, valuable and differentiated products targeted to the most profitable customer segments, while meeting demand and balancing cost to serve.



Experience-centricity by design

The ability to design and deliver seamless customer experiences that adapt to evolving expectations across all physical and digital touchpoints, driving engagement, satisfaction and loyalty.



Seamless interactions and commerce

The ability to execute transactional activities seamlessly across distribution, engagement, and servicing touchpoints, consistent with the intended customer experience and performance ambitions.



Responsive operations and supply chain

The ability for a customer to select products in a manner convenient for them, enabled through analytics-driven demand planning, inventory management and distribution.



Aligned and empowered workforce

The ability to align management processes, capabilities and knowledge including top-down executive vision, matrixed and agile organizational structures and integrated performance management.



Digitally enabled technology architecture

The ability to leverage technology systems to efficiently deliver cross-channel experiences, provide employees with enabling tools and maintain information privacy and security.



Integrated partner and alliance ecosystem

The ability to effectively leverage third parties to access new markets and customers, increase speed to market, reduce costs or supplement capability gaps.

Moving from today to tomorrow: Towards a connected future

Now that you know what models will win and what capabilities you need in order to succeed, the big question is how to move from 'here' to 'there'. KPMG firms can help you plan the four main steps you will need to take — define, design, pilot and implement.

Define

The first step is to decide which winning business model (or combination of models) is right for your organization. The answer may be a combination of the winning business models we identified earlier in this report — or it may be a hybrid. There will certainly be space between business models for smart retailers to carve out new niches.

As you work to define your business model, however, three key strategic considerations should be kept in mind — what you want to achieve (both financially and for your customers); where you want to play (what markets, brands and channels); and how you want to execute and win (which influences your core business processes, technology, structure, culture and KPIs). Ultimately, this should lead to a clear view of the right financial model(s), business model(s) and operating model(s) to drive your organization forward.

Design

Once you have defined your future business model, consider how each of the key connected capabilities discussed earlier can influence your success. Think about what aspects you must build yourself, what you can buy and who you can partner with to enhance these capabilities.

As illustrated in the chart on the following page, some capabilities will play a critical role in delivering particular business models; others will play a lesser role. The key is to take a practical and holistic approach to assessing your current capabilities, future requirements and gaps — and then using this information to design a clear roadmap to success.

Pilot

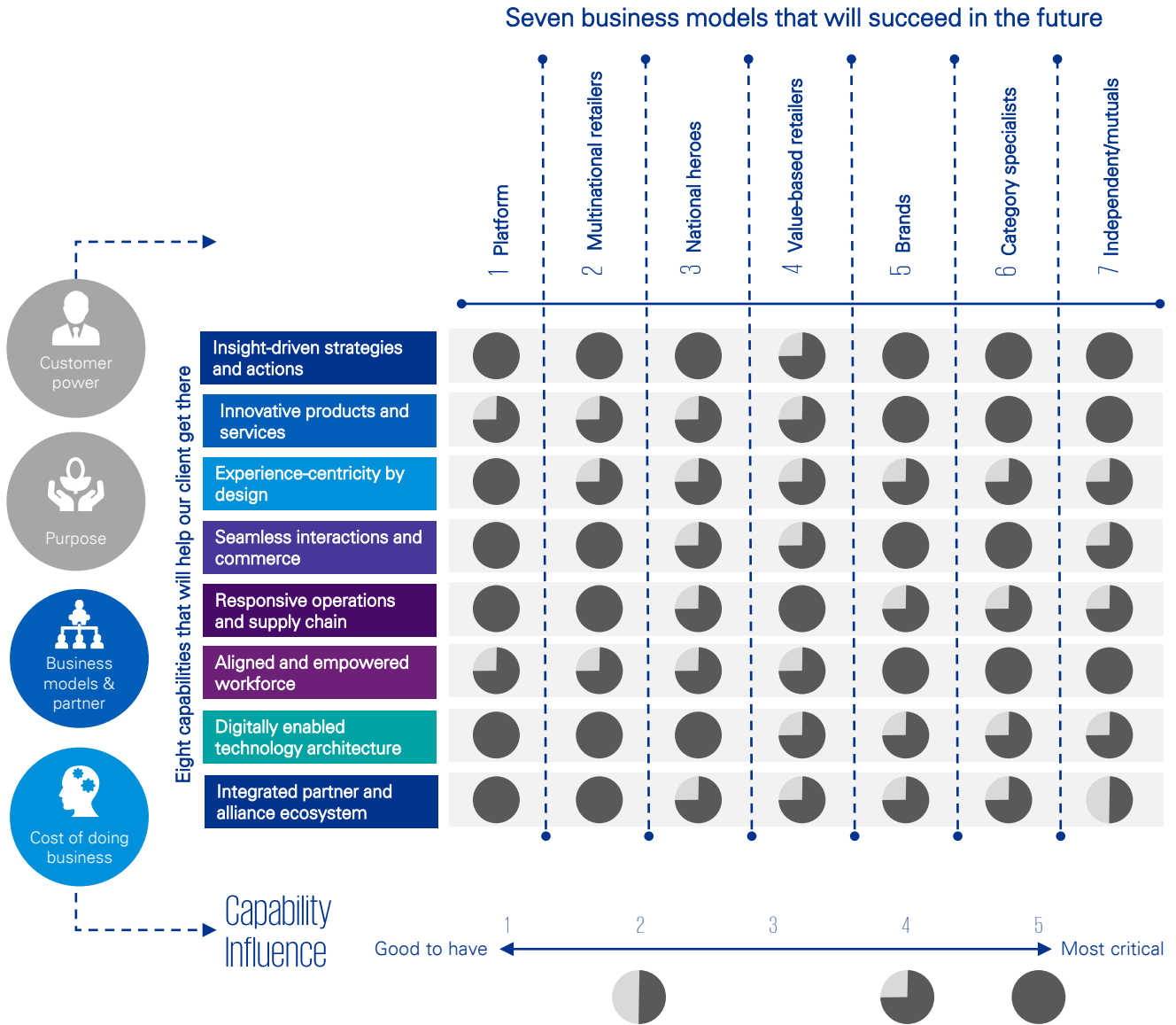
Test and pilot your strategy in high-priority functional areas, seeking not only to validate your strategy, but also to uncover opportunities to tap into a larger potential for change across the organization. A deeper dive into the company's value chain can help identify the best immediate course of action and potential for future change.

Implement

Now it all comes down to activating, scaling and improving your strategies across the enterprise. While this will clearly lead to very different roadmaps and priorities for different retailers, the key is to remember that all of your activities, capabilities and plans are connected — from the front office through the middle office and into the back office.

Connecting trends to capabilities

Once the business model has been selected, KPMG's Connected Capabilities can be used to help determine what changes are required to move the company to its desired state.





Contacts:

Paul Martin

Chair, Global Retail
Steering Group,
UK head of Retail,
KPMG in the UK
E: paul.martin@kpmg.co.uk

René Vader

Global Sector Head,
Consumer & Retail
KPMG International
E: rvader@kpmg.fr

Anson Bailey

ASPAC Sector Head,
Consumer & Retail
KPMG China
E: anson.bailey@kpmg.com

Matt Kramer

Americas and US Sector Leader,
Consumer & Retail
KPMG in the US
E: mattkramer@kpmg.com

Stephan Fetsch

EMA and German Sector Head,
Consumer & Retail
KPMG in Germany
E: stephanfetsch@kpmg.com

Linda Ellett

Head of Consumer Markets,
Leisure & Retail
KPMG in the UK
E: linda.ellett@kpmg.co.uk

Yuji Ito

Retail Sector Leader,
Consumer & Retail
KPMG in Japan
E: yuji.ito@jp.kpmg.com

Kostya Polyakov

National Industry Leader,
Consumer & Retail
KPMG in Canada
E: kpolyakov@kpmg.ca

Robert Poole

National Sector Leader,
Consumer & Retail
KPMG Australia
E: robertpoole@kpmg.com.au

Jessie Qian

Country Sector Head, Consumer
& Retail
KPMG China
E: jessie.qian@kpmg.com

Eric Ropert

Head of Consumer Markets
KPMG in France
E: eropert@kpmg.fr

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