

# RTG Newsletter

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Published quarterly by The Retail Technology Group  
May, 2004

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## **FROM THE PRINCIPAL'S OFFICE**

In this issue we address best practices in inventory replenishment. Long-time associate and author Barbara Anderson wrote the article for this issue. As always; Barbara is direct and on point.

We are also beginning to see the long-awaited turnaround in retail spending. Retailers are talking about doing projects apparently encouraged by stronger sales in some sectors. It is high time..

Enjoy the Newsletter!

Bob Amster  
Principal

## **BEST PRACTICES**

### **INTEGRATED RETAIL REPLENISHMENT**

BY BARBARA V. ANDERSON

#### **Introduction**

The goals of most new retail technology are the same goals that have eluded retailers for decades:

- Higher turns while reducing inventory out-of-stocks
- Improve consumer service by freeing store personnel to assist the customer and providing an excellent in-store stock position
- Reduce the cost of inventory acquisition

Best Practices of Integrated Retail Replenishment can achieve these goals while positioning leading retailers to take full advantage of new technologies such as RFID. The most successful retailers will adopt the Best Practices of Data Integration and Integrated Retail Replenishment NOW, to be ready to use new and future technologies as they become functional and commonplace. Those retailers who have not implemented systems that integrate their supply and demand chains as well as their supplier and retailer data streams and practices will find that RFID offers them great data - all dressed up with no place to go.

Integrated Retail Replenishment is not a future technology. Retailers already using this technology are achieving substantial

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reduction in out-of-stocks (80% reduction) while increasing their inventory turns. At the same time redundant manual store operations such as store re-order and cycle counting have been eliminated thus freeing store personnel to serve the customer and better merchandise the store.

**Integrated Retail Replenishment** today is based on the following Best Practices:

- ✓ Integrate the Demand and Supply Chain by Integrating Forecast and Inventory based on:
  - Accurate Micro-forecasting
  - Optimized Inventory Target and Ordering
  - Total Inventory Approach
  - Speed and Maintenance of the models
- ✓ Automate Manual Processes
  - Automate Store Ordering
  - Enable Accurate Ordering
  - Eliminate Excessive Inventory Counts
- ✓ Optimize Inventory by accurately or systemically calculating:
  - When Inventory is Purchased
  - The Method and Quantity of Inventory Acquisition
  - How Inventory is Merchandised
  - Managing Service Level Expectations and Presentation Stock
- ✓ Differentiate Operational from Strategic Functions
- ✓ Fulfill and Analyze Sales, Logistics and Merchandising Needs
- ✓ Integrate Supplier and Retailer Processes
  - Planning
  - Collaboration

## **Integrate the Demand and Supply Chain by Integrating Forecast and Inventory**

The "buzz" phrase of the last decade has been "demand-driven" retail. The meaning has varied between consumer-direct retailing and POS-driven warehouse ordering. The integrated demand and supply chain is not merely "demand-driven". Best Practices in replenishment call for the full integration of the forecasted need of individual stores with the total inventory position to optimize the supply and demand chains. The requirements of this process include:

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## ***Accurate Micro-forecasting***

Accurate forecasting requires advanced statistical techniques that self-learn and self-adjust, automatically select the best forecast model for each unique store/SKU and time period combination, and classify and select the most meaningful sales influences. It is important not to assume that every retailer and every store within a retailer and every item within a store will be subject to the same sales influences. Flexibility to accept and use those sales influences that actually affect the quality of the forecast and to adjust the weight of the influences is imperative to an accurate forecast.

A micro-forecast uses the most granular data uniquely from each store/SKU to drive aggregate functions rather than using aggregate data to drive item-specific functions.

## ***Optimized Inventory Target and Ordering***

Cost-based Optimal inventory uses the real costs associated with lost sales, which may create a significant loss of a customer's shopping basket or even the customer. Least Cost Ordering optimizes order quantities based on all the cost factors and ordering limitations.

## ***Total Inventory Approach***

Supplier production and DC ordering are driven not only on past history of sales (POS) but on the forecasted future store need as derived from store micro-forecasts and store and DC inventories. It is interesting to know how much product a store might sell but it is imperative to know how much product a store may want to order

## ***Speed and Maintenance***

Errors of processing speed and maintenance are the largest single reason that systems such as CAO have failed in the past. It is simple. If it was a difficult process, such as seasonal profiling, to maintain for six warehouses, it is going to be an impossible process to maintain for hundreds or thousands of stores. Statistical forecasting and ordering techniques cannot be simply moved from the DC to the store without considering the implications of system maintenance

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## **Automate Manual Processes**

The second biggest reason for failure to implement effective integrated demand and supply chain models has been the expectation that store personnel have nothing better to do than to manage data. Their job is to serve customers not computer systems.

### ***Automate Store Ordering***

Accurate store forecasting combined with optimized ordering enables an exception-based approach to store ordering. The exceptions are inventory problems that store personnel should be investigating anyway in order to insure that all of the product in the store is available to sell to the customer.

### ***Enable Accurate Ordering***

Many retailers have in excess of 100% store labor turnover. Accurate store systems enable the ordering of inventory that is unfamiliar to newly trained staff.

### ***Eliminate Excessive Inventory Counts***

There is an easy way to fail at in-store perpetual inventory - base it on the expectation that store staff has the time and ability to continually count and re-count stock. This is an area that item-specific RFID is supposed to greatly enhance but until that day, there are systems that detect problems in inventory by exception, thus counting inventory only when there is a need to review the on-shelf stock position. If you don't believe me, try accurately counting the lipstick section.

## **Optimize Inventory**

Optimization in retail is fundamentally cost-optimization of demand and supply chain processes that include:

### ***When Inventory is Purchased***

Do not confuse least-cost inventory with the least quantity of inventory. Sometimes in our eagerness to improve unit turns we decrease dollar turns. Yes, less sometimes is more, but in the case of inventory less can be more labor, more cost of acquisition, more handling and more shrink. A good strategic analysis of the framework for ordering will establish when less inventory and less cost match.

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## ***The Method and Quantity of Inventory Acquisition***

The quantity of the shipment, the logistical ship unit, the choice of manufacturer-pack size, the frequency of delivery, and the delivery method should all be analyzed by strategic systems for the cost optimization.

## ***How Inventory is Merchandised***

Integrate the planogram system with the automated ordering system. These are not separate functions and should be integrated from optimizing space plan set, ordering within space limitations, and exception-based analysis of store-specific space sets.

## ***Service Level Expectations and Presentation Stock***

Use systems to analyze the cost-benefit of Service Level Expectations and Presentation Stock. Service level expectations can create costly and expensive goals for ordering systems and should never be arbitrarily set without the analysis provided by cost optimization. Presentation Stock drives retail from planogram sets through ordering and is often set by 'gut feel'. Yet this single number is enormously costly as it sets the minimum for every single store for every single item. Strategic systems can and should optimize the presentation.

## **Differentiate Operational from Strategic Functions**

Differentiating Operational from Strategic Functions is an important element in successful store-specific driven forecasting and ordering. The framework of ordering including the parameters (goals), the methods and frequency of delivery, and pack sizes should be analyzed on an as needed basis. This is information for people to consider and then change business practices accordingly. These tasks should never be confused with the fast-running operational systems that deliver their output directly to other systems (such as automated ordering) with only the exceptions to be manually reviewed. When they are mixed together, the manual review process becomes tedious and burdensome and the strategic process often is overlooked.

## **Fulfill and Analyze Sales, Logistics and Merchandising Needs**

All of the product in a store will not be sold tomorrow. Now that's a pretty simple and easy to agree upon statement, but it

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has immense implications for our systems. The timing and quantity of product in our stores has as much to do with merchandising and logistical considerations as with actual sales need. Our systems must be able to strategically analyze the costs of those logistics and merchandising needs and operationally fulfill the logistical and merchandising requirements as well as sales requirements - automatically. That means a store system must recognize all the requirements of replenishment. It means that the supplier and DC must be able to ship when the store needs the product for both merchandising and immediate sales purposes.

## **Integrate Supplier and Retailer Processes**

It's an old saw now that that when a supplier and retailer work together, it is a win-win situation. Unfortunately heretofore it has been a manual old saw not a power saw, and in many cases that old saw has no teeth. Whether we are talking about multi-method statistical forecasting, optimization techniques, neural nets, or pattern recognition, we've come a long way from the days when every buyer could reproduce the recommended order with a hand held calculator. Unfortunately our business practices have not progressed as quickly.

### ***Planning***

A good system can and should analyze and establish the span and frequency of every forecasted order with the recognition that yearlong forecast may use different parameters than the next day's forecast. Today's systems can produce short-term (replenishment) forecasted need, mid-term (demand planning) forecasts, and long-range (merchandise planning) forecasts.

### ***Collaborative Data Sharing***

If you want a power saw; collaborate on data rather than the result of the data. Provide a single system with the best information possible in a timely fashion and watch today's statistical techniques create usable accurate forecasts beneficial to both the retailer and the supplier. Today's forecasting systems only lack sufficient data to produce accurate predictions of future product need.

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## **Why is all of this important?**

By changing simple business practices and implementing automated store reordering against - integrated the length of the demand and the supply chain - substantial improvements in basic inventory goals are achievable today. These same systems will then be in place and ready to receive and use the improved data from the exciting developments in RFID and data integration.

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## **WHAT'S NEW**

### ***Visit our Web site!***

You can read about us at [www.RetailTechnologyGroup.com](http://www.RetailTechnologyGroup.com).

### ***L'Oréal***

We are pleased to announce that L'Oréal selected RTG to conduct a POS software evaluation project for the company's three brands of retail stores. L'Oréal is a vertically integrated manufacturer retailer with about ten brands of cosmetics, including L'Oréal Paris, Maybelline, Lancôme, Biotherm, Ralph Lauren and Giorgio Armani Fragrances and Kiehl's.

### ***Bain & Company***

We are also pleased to announce that we are continuing our relationship with Bain as part of Bain's Global Expert Network, of which we are part. We have been asked to provide expert support on a new phase of work for an off-shore department store client.

In addition, Bain invited RTG and strategic partners to address its retail and consumer products world-wide group of vice presidents on the state of technology in specific disciplines.

Pete Abell, Roland Faubert, Stephen Hill and Bob Amster addressed RFID, CPFR, Advanced Merchandise Planning, and Retail Revenue Management respectively.

### ***Coach***

We are pleased to continue our work with this successful and popular retailer. We have been assisting the company on a number of project management, deployment and quality assurance issues.

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