Lecture Text
Professor David E. Bell
The Revolution in Retailing

(*edited for clarity*)

Introduction

Revolution in retailing. I started studying retailing in 1992, and when I told people I was studying retailing, they said "Why?" I said I was interested in studying an industry. And they said, "That was the strategy choice for your career, to study an industry?" So I had my free pick of industries. Healthcare could have been a choice, but I picked retailing. And for once in my life I was at the vanguard, because retailing turned out not to be a sleepy industry over the last ten, thirteen years. It's actually been a very exciting industry and I'm hoping to make you converts by the time you leave.

The Scale of Retail

Unless you're in the business, you have no clue what scale we're talking about here. Total retail sales in 2003 in the United States were—I'll mention other countries every now and again, just to show that I'm international—total U.S. retail sales: $3.7 billion. But since everyone in the United States has two cars, that kind of slants the numbers. And so, typically in the retail biz, we take out cars and we take out restaurants. So after you take out automobiles and food service, you're down to $2.1 billion. And just to give you some sense of what the components are, OK? So, building and hardware—well, you can read this: $321 billion. Did I say billion up there? I meant trillion. That's the thing about the B School: You learn to distinguish decimal points. I started out as a mathematician, where the decimals are completely irrelevant. Leave the decimal points to somebody else.

So clothing stores: $178 billion. This disguises the fact that Wal-Mart now probably sells 15 percent of all clothes in the United States. So the categories aren't completely separable.

Grocery: $500 billion. I put up liquor stores. Some of you are keeping them going singlehandedly, I imagine.

Top U.S. retailers: Well, Wal-Mart, they'll come up again sickeningly often in this talk. It says here for 2002—I'm up to date here: $246 billion. Home Depot. Kroger: That'll be dropping. Target. Sears: That has dropped. Costco, my favorite retailer, just in case. . . . I'm trying to do retailing myself and answer all of the questions that I might get at the end. Costco is my favorite retailer. Albertsons. Safeway. JC Penney.

Kmart, still on the list. I said that I started studying in retailing in 1992, and each year since then I've predicted the imminent demise of Kmart. And one day I'll be right.

Walgreens, Lowe's, CVS.

This is my international segment. So top 200 global retailers. This will only take about fifteen minutes. So France: Carrefour, hypermarkets all over the world. The U.S. retailers tend to be high on these world lists, not necessarily because they're able, although actually American retailers are pretty good. This is a big country so you get a head start.

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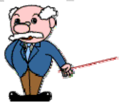

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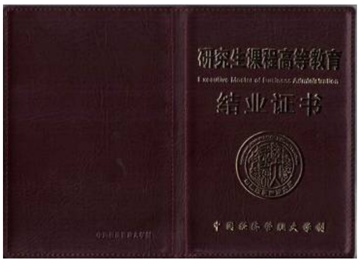

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Germany: Metro. Ahold is all over the world. Tesco, actually, who is all over the world. Costco is not all over the world. Well, they are some places all over the world. Germany: Aldi. Anybody been to an Aldi?

The Role of a Retail Store: the Four Ps of Retailing
So the role of a retail store—if you ask somebody what are the most important three things in retailing, you've been programmed to say?

__: Location, location, location.

PROFESSOR BELL: Yes, well done. Yes, location, location. That's not true. OK? It's efficient distribution between manufacturers, and location is one of those. Location is a part of that efficient distribution. You want to choose a location that's easy for people to get to. So anything I say that compromises that, dismiss what I say next and remember that one.

If you remember back to marketing, I imagine that Four Ps and Five Cs, and things like that, were all the vogue when you were here. These are the equivalents of the sort of Five Cs—no, Four Ps for retailers.

Price
So, first of all, price. One way of thinking about what a retail store is, it's sort of like a buying group. So we as consumers, if we want to buy a refrigerator, if we're negotiating with Westinghouse, we probably won't do too well. So what we do is we form a buying group and then we negotiate with Westinghouse for a job lot of washing machines or refrigerators, and you can think of a retailer as being that. The bigger the retailer is, the more buying leverage they have, the lower prices they can offer. It also helps, of course, if they're efficiently run, so they're not wasting money. So price is one element. You knew about that.

Convenience
Convenience. You want those goods but you don't want to spend a lot of time doing it, usually. So location, location, location.

Something else that's very important is clear positioning. Those of you who aren't keen on shopping will know that one of the most frustrating parts of shopping is having to go from store to store to store to find out what you want. So a store that's very clear about what it sells. So, can you get an electric fan at Staples? One person knows, two people know. Diverse background there. But that's the problem: You go out shopping and you want to know where to go to get what it is you want. And the clearer a store can be about what it offers. . . .

Related to that is in stock, of course. You may know that apparently Staples sells fans, but of course they may be out of stock when you get there. Now, one of the dilemmas of retailing is trying to keep in stock on popular items. So, for example, when you go to a store and you want that suit or you want that dress, or something like that, and they don't have your size, so you say, "Do you have a size whatever?" And what's their answer? "No." I agree, that's the first answer. And then you say, "Why not?" And what's the next answer? Who's the expert here? They say, "That's a very popular size."

Convenience credit—I'll get back to credit in a bit—but credit is a convenience because usually you can't afford . . . And we're not talking about groceries here, but we're talking about when your TV set breaks. My next car is always going to be a very fancy one, but when the thing actually breaks and I have to go get a car and I rummage around in my wallet, then I'm suddenly interested in price orientation. So credit is very important.

Matching
Matching. Matching is when you go in the store and you want a TV set, and the salesperson says, "What type?" And you say, "I don't know, I haven't bought a TV set in five years." So what the salesperson will do, if they're good, is try and figure out what it is you need and match that with what's in the store. And if a store is excellent, they will have figured out their store customer demographic and have already selected down from the universe of 10,000 TV sets to the twenty or thirty that are likely to be desired by their customer base.

So two forms of matching take place by the retailer. One is narrowing down all the possible TVs they could have. And the second is the personal interaction to try and get you the set that matches your needs.

Risk reduction
Risk reduction. Clearly, a concern is that you get this thing home and it doesn't work. And then what do you do? Back to Westinghouse. Where does Westinghouse make refrigerators? You don't want to have to go there to tap on the door and say, "Hey, that refrigerator I bought doesn't work." What you'd like is for the store either to give a store guarantee to make you whole, or you'd like them at least to help you battle Westinghouse. Again, it's the idea that the store is sort of a buying group helping the customer.

Shopping experience
And the shopping experience. Entertainment. Some people still enjoy shopping. It's an activity for a lot of people. They enjoy going to a mall, looking around, spending time with other people, that sort of thing.

And so these are the dimensions on which you can think about any retail store. For any particular concept you can say how good are they at price, how good are they at ambience, how good are they at different things.

Retail Formats
Different retail formats. All of the things you've probably heard of. Category killers—I'll just pick that one. What's a category killer? Toys R Us probably was a pioneer in this. Staples: For people around here, the first Staples store is just down the street.

So the idea of a category killer is this notion that, in the old days, what you used to do would be to go shopping from place to place to try and find the best deals, find out what's available. And, again, certain stores didn't have everything. So the notion of a Toys R Us/Staples category killer is to have everything you might reasonably need within a particular category at a low price; not necessarily the lowest price, but sufficiently low that you feel no incentive to go somewhere else. So you go to Staples. I'll bet you can find stuff cheaper than Staples. You go to Costco, for example. There will be places where you can buy cheaper than at Staples, but it's not worth your trouble, and that's how they make their money. They've got selection, and low, but not the absolute lowest, prices.

So each of these has a different shtick. For those of you who don't get the idea of convenience stores, I'll hold an extra session at the end. But each of these has its own sort of approach to things.

Expansion Strategies
The hardest problem in retailing—if you go back to somebody who has a bright idea and they say, "I think I'll start this store," is—it is very difficult to open a thousand stores all at once. So what happens is you open one store, and the most common question I get when people visit Boston is, "What are the exciting new concepts in Boston that I can visit?" The problem with retailing is that your R&D lab is open to inspection. So you start a new concept. If it's at all interesting, your first thousand customers are your competitors. And they say the store is full, but of course it's all full of their competitors.

So the problem is, the way you open a store at the beginning is not always the way that it should be. You make modifications. You learn as you go along. In fact, even when you're a big chain, you learn as you go along.

Mistakes get made when you expand too rapidly because you suddenly have 40,000-square-foot stores when really you should only have 25,000-square-foot stores. So there's this tradeoff between how quickly you try to expand your concept so that you get first-mover advantage versus actually playing with it to get it right before you expand it.

Expansion is pretty difficult because you need capital; stores are expensive. Training. You can't just suddenly hire. It's like, using the modern theme, if you suddenly decide you want to double the army, you've got some training to do, you've got some capital expenditures. Not so easy. And retailing is similar.

One of the big issues is should you own your own stores or should you lease your stores? Owning them is very capital-intensive, of course. Leasing is not so capital-intensive. You do get some benefits from owning your own store, but they aren't that many. If you're a place like Wal-Mart, you get a lot of benefits because what you do is you buy not only the space that your store is on, but you buy half-a-mile radius around your store because the best place, in some sense, for competitors is to be near Wal-Mart. All of the territory around a Wal-Mart picks up very rapidly when a Wal-Mart opens there. And so Wal-Mart likes to own its own real estate.

One very tempting approach to expanding is franchising. So what you do is you sit back and you let other people do the work. It's a great concept. So McDonald's, a fantastic franchise. In fact, you wonder what happens at McDonald's headquarters. My theory is that it's a twelve-by-twelve room with a couple of phones, because the franchises do everything. We could discuss supply chains. The suppliers are all—everything's subcontracted. There's just Mr. McDonald who's sitting there, waiting.

Actually, the main thing they do is store siting. They have a great ability to site stores. And, Charles, since he knew "location, location, location," also knows the best place to put a Burger King.

__: Right near a McDonald's.

PROFESSOR BELL: Thank you. And he's not even my student! So McDonald's—I don't know if they do this; I don't think they do—they should buy their site and the site next door. Because you know Burger King's going to come looking.

Strategies After Saturation

So we've rolled out over the entire United States, and there's a McDonald's everywhere, there's a Radio Shack everywhere. What do you do next? So those of you who miss two-by-two grids, I reformatted this page this morning because I wanted you to feel fulfilled. So, it's very deep. You can either do the same thing to different people, or you can do different things to the same people, or different things to different people. And I want recognition if ever you use that idea.

So same concept, same customers. My favorite, Costco, a few years ago started adding service. So they sell insurance, they sell mortgages. They've got the same customers coming in. "What else can we sell them?" kind of thing.

Wal-Mart. This is an old story, of course, this is ten, fifteen years ago. Wal-Mart says, "Hey, let's start selling groceries. We've got all these people coming here." This is a good laugh.

My Kmart prediction didn't come out right, but I remember laughing when I heard Gateway was opening stores. Talking of Gateway—customer selection, the cornerstone of marketing. I remember calling up Dell. This is years and years and years ago. But my wife wanted a laptop and I'm in charge of things like that. So I called up Dell, and I said, "I'm interested in getting a laptop." And they said, "What kind of laptop?" And I said, "Well, I don't really know." They said, "Why don't you call back when you do?"

The problem is that you get used to a certain type of customer selection and delivery, and Gateway's messing things up by trying stores. They're actually destroying that easy-to-serve concept because they're trying to attract—well, no longer, of course—but trying to attract people who don't know how to plug it in, basically.

Same customers, different concept. I said that Radio Shack is one of the most successful retail concepts on earth. . . well, in the United States anyway. There's some statistic, which I've forgotten, but it's something like 90 percent of the population in the United States has a Radio Shack within a mile. Their inventory turnover is two. Remember inventory turnover? So if sales at cost are a billion, or whatever they are, they have $500 million of inventory. Now, that sounds on the face of it not like a model of excellence, but their retail strategy is—and I've heard this from the CEO's mouth—that you go in for that piece of cable that's about this long, and the person goes into the back room. He's gone ten minutes and he comes back and he says "I found it," which of course he can at Radio Shack because they've got $500 million worth of inventory.

So then after he's asked you for your zip code, he says, "That'll be eighty-seven cents." Now I feel bad—it's eighty-seven cents. He says, "Have you seen our cell phones? Have you seen these printers?" It's like the only retail concept where they trade you up. You come in for eighty-seven cents, and you walk out with something that's $100, or five-year telephone service, which is the nirvana. Most stores, you go in, like Circuit City, you buy a $500 TV and then they're selling you a plug or something.

So I got on to this because Radio Shack is hugely profitable. And you studied at the Business School the problem of what to do with excess money. Bottom of the list: Give it to the shareholders. So Radio Shack keeps trying to think up new concepts, and they used this grid, after they heard me talk. So they opened an Incredible Universe. It's fantastic, hugely expensive; huge, state-of-the-art electronics store, and it's a miserable failure.

Home Expo, I think, is doing pretty well, which is Home Depot, where sort of . . . Have you been to a Home Expo? Pretty good actually.

Sears Hardware—there's another one where my diplomacy skills are lacking. Arthur Martinez—a graduate. He's not here. I remember—this is name dropping—I was in his office. He was talking about things he was trying to do to revive Sears. After we discussed apparel and its fit with the Sears customer, he mentioned the Sears Hardware stores. The idea is these separate stores, like a True Value store that just sells Sears tools and things like that. It's convenience. I said, "That'll never work." And the senior staff were all exchanging glances. I realized I had hit a raw nerve. Because it's very difficult to run two different concepts at the same time, especially when they overlap on merchandise.

So if you're in charge of tools and hardware for Sears, where are you placing your emphasis? Are you placing your emphasis on the big department stores, or are you trying to get the small hardware stores going? It's very difficult to handle that sort of thing.

International. I think you understand that idea. There have been some successes where somebody just starts over. So Woolworth—great concept for the 1870s. Sure enough, 100 years later, they tried something different: Foot Locker, which has been a huge success. And Dayton Hudson started Target and now they're trying to sell Dayton Hudson.

Critical Success Factors

Critical success factors for retailers. Every time I give this talk, I kind of add one. One of the problems with retailing is that there are a million important things. Every day somebody can say, "In retailing, the really the most important thing is . . ." and then you say, "Oh, my God, it really *is* important."

Reduce complexity

So the first one, actually, is to reduce complexity through focus and positioning. So you open a store, Dunkin' Donuts, and you say, "I think I've got it: donuts." But then it's coffee, and then it's this, and then it's that. I remember walking past a McDonald's and seeing tablecloths and candles! This is a few years ago. I thought, "Oh, my God."

You go into a new store, the new store near you. You go in and the floors are clean, the aisles are wide, you can see everything, everything's clean. You come back three months later and the aisles have got boxes in them and there are extra little stands of things. The store gets cluttered and eventually people lose track of what it is they're selling in that store, and the customers lose track. It's a mess.

Match local needs

Match local needs without sacrificing the economic advantages of centralization. That was written by a lawyer. So the trick in retailing is to have a thousand stores that are identical. That's nirvana. The problem is that different locations require different things. People are different is what you learn. So you say, "What we really want is a thousand stores that are idiosyncratic to the individual neighborhood." There's that tension. How much do you centralize, how much do you . . . ? That's a tension that you never actually solve.

Environment of communication
Create an environment of communication, human and computer, between buyers and sellers. That was written by the same person. Despite the fact that IT is sort of taking over retailing, it still requires a human dimension. There are still mistakes made. I was at Wal-Mart headquarters, and they have these Saturday meetings where people fly in from all over the country to have these discussions. And I remember somebody, the store manager from Alabama was complaining they didn't have air conditioners, and it was in April. And he said, "You guys may not know it, but in April it gets hot in Alabama." When you're trying to do the same thing across all stores, you make mistakes.

I went to Eddie Bauer. When the Web came out and they were suddenly besotted with the Web, selling on the Web, they decided that the stores had to be geared towards the Web. So everything had to go on sale at the same time. Remember these Internet problems? So they had this rule. Everything in the store went on sale at the same time across the country. So in Minnesota, in April, where there's still three feet . . . versus Palm Beach, where it's kind of getting warm around April—they're putting the stuff on sale the same day. It's absolutely nuts.

Hire, train, and motivate
Hire, train, and motivate employees to carry out the company's mission. They're all the hardest thing. This is the hardest thing: How to get the several hundred thousand people you have that are serving customers in the store—you're sitting in corporate headquarters, strategizing, and you've got all these hundred thousand people out there dealing with customers every day. How do you get them to do what you want? Very difficult. One thing is that it helps if you actually have a well-stocked store. One thing that kills service very quickly is if you don't have what customers want. Somebody comes in and says, "Do you have my size?" and you say, "I'm sorry, we're out of that. Would another size do?" "You look good in that fifteen and a half," as you're turning blue.

So what happens is, if you're out of stock and you keep dealing with customers and you can't help them because you're not in stock or, "We don't have that," eventually the staff start hiding in the back room. That's why they abolished back rooms. That's one of the great ideas of the last part of the twentieth century—to eliminate the back rooms, because all of the employees are hiding back there. What you really want is for them to be out helping customers.

Wal-Mart, you know, had this great idea of a greeter. And that works incredibly well in Wal-Mart because it substitutes for service, but that's another story. You know the greeter. They're all smiles. They greet you when you come in. This is absolutely fabulous. And retailing being what it is, people start copying. I went into—this tells you how old the story is—a Caldor or a Bradlees around here, and there was this kid was standing at the front of the store like this. He was about seventeen and he was standing like this. So I went over to one of the staff, being my way, and I said, "What's he doing?" "Oh, he's a greeter." What Wal-Mart does is they find people who are excellent at greeting and put them in that position. Whereas other people say, "Hey you, you're a greeter."

I heard a talk similar to my own. Some fellow retailer was talking, and he said that he was in London and noticed that Sainsbury's—I actually don't know which supermarket it was; I've long since forgotten, but let's say it's Sainsbury's—had this deal where, if the cashier did not say to you, "Thank you for shopping at Sainsbury's," as you checked out, you get a pound. In England, you know, the game show prize is like £10 over there. So you get a pound if the staff does not say, "Thank you for shopping at Sainsbury's." So my colleague, as it were, did what I would have done. You rush right over to see if this actually works. So he buys a few things, he comes through the checkout counter, buys, pays the money, and he's sort of—and no sign of a "Thank you for shopping at Sainsbury's." He goes back and says, "Excuse me, aren't you supposed to say, 'Thank you for shopping at Sainsbury's' or I get a pound?" She says, "Oh, no, that was last week."

Create an environment of respect for customers
I learned this one. You learn something all the time. Maybe it's my math background or something, but I didn't get this one. Trying to motivate people to help customers is often a fruitless task. And what Tesco learned, and maybe generations of people before them, but I learned it at Tesco, is that unless you treat the employees with as much respect as you expect them to treat customers, it won't work. And you may have learned that twenty-five years ago, fifty years ago—sorry—at Harvard Business School, but it took me until now to figure that one out.

Act as the customer's agent
Act as the customer's agent. I mentioned this a few times, actually. I really do believe that retailers should have the mental set that they are there to serve customers. Now all kinds of companies have these mantras about "we're here to serve customers," but I think unless retailers absolutely believe that every day, they're going to make a mess of things.

Be inspired by a merchant
And for that reason, I added seven, and it's for people like Marvin Traub [former CEO, Bloomingdale's], actually, that I have seven; being inspired by a merchant, by somebody who has a passion for delivering good service, etc., etc., to customers.

One of the best operations in customer service that I know of, and somehow it's not customer service, but it's 7-Eleven in Japan; not here. Toshifumi Suzuki runs 7-Eleven, Japan. One of my mantras that I've now deleted from my talk, having talked to him, is that I always said it's criminal that retailers don't pay their staff more. It's some minimum-wage sort of job. So you have these discussions where—I don't know, the greeter—if you paid people a little bit more, you'd get a better person, more educated, this, that, and the other. And, in a polite Japanese way, he said, "You're wrong."

So here's the way I see his explanation. Write down—no, think to yourself, if you were to work in a 7-Eleven for the rest of your life—that's your job offer—what salary would you expect? So somebody's come to you and said, "We'd love you to work in a 7-Eleven, and what salary would just make you give up whatever it is you're doing now and go work in a 7-Eleven?" My belief is that you would actually expect more to work in a 7-Eleven than you would at whatever you're doing right now. Why? Because it's boring as all get-out working in a 7-Eleven.

So his point was that if you raise salaries, you get better-class people, but then they're bored out of their minds. So one thing he does in his stores is try to engage the people by giving them responsibility. This is an extraordinary concept. It's things that they teach you as parents to do with children, which you ignore, but in a retail environment they're actually very important.

All the movement is the other way. The electronic support, all the stuff comes from headquarters. You don't do a thing, you just put the stuff out, you dust, and it's dull. In the 7-Eleven in Japan, you start working at the store, and very quickly you're in charge of a section of the store—reordering—and it gets you involved in that. And you make some mistakes, but at least it makes you more interested in the store.

Current Issues in Retailing
Current issues. Traceability is one, by the way. These days, it's not just terrorists and things like that, but people are very concerned about traceability. So that if there's a mad-cow kind of thing—you know, a cow dies in Seattle and everyone wants to know if they're eating it kind of thing. And the answer's no. I mean, I can speak confidently.

So traceability. And it's not just for safety but, just like wines, you say, "Ah, it's from"—you have no idea where it is from, but you say, "Ah, it's from the something valley. Ah!" I predict that in ten years' time you're going to be doing that with all kinds of things. We're already doing it with water: "Oh, Poland Spring? No, I like European water."

The Mom-and-Pop Grocery Store
So now I'm going to go back a bit. I have a little extra time, and I wanted a picture of a traditional mom-and-pop store, and it's amazing how difficult it is to get photos of things. Turns out this is in the family archives. This is my wife's great-great-grandfather, in Milwaukee, I think. The sad part is, I remember shopping in stores like that. I grew up in England. They were still like this in the 1950s.

And it screams inefficiency, right? Presumably, half of you have done this, but the rest of you won't. But when I was shopping as a kid, you would go into the store, a store just like this, and you'd say, "I want a loaf of bread." The person would disappear, come back with a loaf of bread. Then you'd say, "I'd like a can of peas." This is in England—can of peas. Disappears, comes back; adds it up.

The First Revolution: Mass Production
And then there was this revolution. Actually, the revolution was probably self-service, but there was, from 1860, or something, to 1940—I'm making up these dates, but I'm guessing that you're not going to be checking online—1860 to 1940, manufacturers were the powerhouse. Excuse me, to 1980. Ah, well. The dates are irrelevant.

For a while, manufacturers were in charge of everything because they had mass production, so they could be cheap. So finally, goods were cheap that were provided. They did branding so that you, as a customer, were motivated to go in and buy that brand name. In the old days, you would go to the mom-and-pop, and you'd say, "What's good today?" in that butcher shop—it was a butcher shop—"What's good today?" and the person would tell you. When the manufacturers got big and bad, and all that kind of stuff, and television and radio—see how far I'm going back? And there was one channel. Can you imagine? There was one channel, and everybody watched it. This was really efficient if you're a manufacturer. You advertise on that channel and everybody knows what you're selling. So now you're in charge. The retailer is just a cipher in this.

And self-service, even more so, because now you go in. You don't even ask the people in the store at all. You just go in and you buy the things you've been educated to buy by network television and radio.

So these things, at the top there, the first three things are creating a sort of pulled environment. Remember your marketing. This is a pulled environment. This is where the customer is going in and deciding what it is they want to buy. And refrigeration, automobile, and shopping cart all allow you to buy more things at one time so that you don't want to go the store and ask for one thing and then get it, and then ask for another thing and then get it.

So then we got supermarkets. This will only take about another hour and a half. I hope you're good with it. This was the first supermarket. It's a converted garage, I think it says. King Kullen. You see, even in those days—the Four Ps and the Five Cs—King Kullen. You got it? His name was Cullen, with a *C*, but he realized this would never work. You remember the Four Ps and the Five Cs. Did you ever do the Seven Ss of selling? First one is psychology.

And then with the automobile, they started to build these things out of town. They got bigger. See, before, the answer to efficient purchasing was just to make the store bigger and bigger and bigger. Then somebody had the bright idea, and it wasn't just a bright idea, it was the changing environment that allowed you to have chains.

The Second Revolution: Mass Retailing
So the second revolution was the chain store, basically. And I think the chain store was created in part by knowledge about professional management. Professional management, business schools, and things like that, is a relatively recent phenomena—you know, the last umpteen years. So the advice in the old days was that the owner had to be in the store. But now, of course, you have these chain stores where you're the owner of most of the chain stores in the United States. The retailer became—retailers: chain stores, more volume.

The UPC code was very important. In the old days, the only people who knew how many white shirts were selling were the white shirt manufacturers, because however many they made—this is still true, by the way—however many they make is how many get sold. We're not arguing about what price they get sold at, but everything that gets made gets sold.

With the UPC code, now the retailers know what's selling. It's too hectic an activity in retailing to be counting everything by hand, in the old days. But when the UPC code came, some of the retailers knew what was selling.

The bar code, which is the power of all of our information, is getting more complicated. There is a two-dimensional bar code, but they have these laser things now where they can store absolutely everything about that product. This is actually going to help traceability and things like that—power of information.

The Third Revolution: Mass Customization
The third revolution—you haven't been following my dates, but I've got my dates worked out very nicely here—is sort of mass customization, which hasn't arrived. We thought it was going to arrive three years ago, but it didn't quite yet, but it will. But it arises from this unstructured lifestyle kind of thing where people don't all march to the same drummer. And

one of it is cable TV. We're all watching different channels. Fifty years ago, we were all watching the same channel, and therefore we were all indoctrinated in the same way. Made life easier for the manufacturers because they just made white shirts for everybody.

No one eats dinner with one another anymore. You used to train your kids to eat roast beef and the mashed potatoes and the carrots, or whatever it was, because they had that 400 nights in a row at home, and eventually they get used to it. But now everyone eats whatever they want, whenever they want. The computer, etc., etc.

So what's happening is that, more and more, the consumer is in charge of what stores sell. So in the old days, you bought whatever Heinz chose to manufacture, and then you bought whatever Kroger chose to sell you. And now people are actually demanding things for themselves.

General Evolution
So one way to think about what's happened in retailing is—I put up the Five Rs, the list of different things that retailers do. The three main things a store does, or did—one was physical distribution of goods. When you want something, like an ice cream, it has to be there. But even a vacuum cleaner, you kind of want it to be there. Usually you're buying one because the last one broke. You want it to be there.

Advice. Again, this is this matching thing. You don't know what kind of vacuum cleaner, or whatever, so you go in and you ask for some help.

And the third thing—it was credit; that you couldn't necessarily afford the things you were buying. You got credit.

These things have gradually split up over time. So credit went first when Visa and American Express came out; where the credit went with you, it didn't go with the store. So instead of relying on the store to provide credit, it got outsourced.

The next step, I think, and it's starting to happen with the availability of the Internet, is that the advice is splitting up. So instead of relying on the store, the sixteen-year-old—"What kind of TV set should I buy"—I don't think he's the right person to ask. So what you're trying to do is you're trying to get your advice from somewhere else. In fact, a really good thing, and some stores do this but not on a consistent basis, would be to have a terminal next to each product so that you can log on and get the guidebook, or whatever it is—this, that, and the other; learn about it yourself.

Another way to think about what's happened in retailing over the last hundred years is to think about who makes the production decision. So manufacturers used to make the production decision. There'd be somebody who'd say, "Hey, let's go with blue shirts," and then blue shirts become popular. And then the retailer—and this is the current era, really—the retailer was in charge of deciding whether they're making blue shirts or white shirts. Private label.

And the next step is sort of mass customization, where people just order and it gets made for them.

Wal-Mart
So the next phase. I said I would mention Wal-Mart ad nauseam. This is where it starts. This is where some of my abstract of my talk comes from. So Wal-Mart has obviously been this huge thing. If you remember the ‘90s—how it seemed like everyone was rich during the ‘90s, and the economy was taking off. Semiconductors seemed to have a lot to do with it. McKinsey did this analysis, which fits the style of my talk, and therefore I approve of it. It said, “A quarter of that increased productivity in the ‘90s came from retailing, and about a sixth of that improvement in retail productivity came from general merchandise, most of it directly or indirectly from Wal-Mart.”

So Wal-Mart itself created a lot of efficiency in retailing, which lowered the amount of money you and I had to spend on groceries and other goods. So that helped. But it was also their impact on other retailers who became more efficient. So the whole of the retailing industry became much more efficient during the ‘90s, pressured by Wal-Mart. If you don’t shop at Wal-Mart, I can show you the savings later on.

So homage to Sam Walton. “We’re all working together. That’s the secret. We’ll lower the cost of living for everyone, not just in America, but we’ll give the world an opportunity to see what it’s like to save and have a better lifestyle, a better life for all. We’re proud of what we’ve accomplished. We’ve just begun.” And that isn't just a mantra. That isn't just what’s on the business cards. That’s what Sam Walton believed. And Sam Walton acted to try and deliver on that mission. And that’s why I think of the importance of a merchant, if you like—a head of the company who absolutely believes in what it is the company’s trying to accomplish.

So Wal-Mart. I have to update this slide on like a daily basis. It should be hotwired to the Wal-Mart site, or something like that. So they’ve got 1,428 of those discount stores; 1,553 of the supercenters; $256 billion in sales, that’s a lot; 1.5 million employees. This is an enormous operation.

Financial results
If you were here fifty years ago, when you looked at the annual report, it said, “Notation: money in thousands,” or tens, in Arthur’s case. These are in millions. So $256 million—billion, excuse me. Net sales increase: 12 percent, so it isn't slowing down any. Domestic comparative store sales increase. That’s not so good. We’d like a little better than that. But, on the other hand, they saturated the place.

Operating, selling, and general administrative: $44 billion. That’s 17 percent of sales. That’s enormous for a retailer, that’s fantastic.

Net income: $9 billion. See, the message is, if you’d like to leave now, the message is that Wal-Mart’s taking over the world. It came to me as an epiphany about two years ago. When I talked about Wal-Mart in classes—I have a Wal-Mart case—people used to say, “Ah, you know, look at what happened to Sears. Look at what happened to General Motors. These companies get big.” No. This is the epiphany: Wal-Mart has escaped this orbit. Wal-Mart is now off and free. They’ve got $10 billion of net income.

They have Sam’s Club. Sam’s Club is another of these things. I like Costco, I don’t like Sam’s Club. It’s $34 billion, so they must be doing something right.

I hope I'm not boring you. Net cash provided by operating activities: $16 billion. So they bought ASDA, in the UK, a few years ago. Widely believed to be overpriced. They paid too much, they paid $10 billion. At the time, it was one year's cash flow. The sales increase that they need to keep going at the rate they've gone over the last ten years would require them to add $37 billion of new sales each year, $37 billion.

That means that if they bought Costco, that would keep them going for the next year. If they bought Federated, that would last them six months. Federated owns Macy's, Bloomingdale's. If they bought the Gap, that would last them four months. Did you ever read *The War of the Worlds*? What?

__: How many new stores, then, do they need to keep opening every year if they didn't buy . . . ?

PROFESSOR BELL: Well, $37 billion—let's assume that a new store is $100 million, which it's not, but let's do the math easily and then we'll figure it out, OK? So $37 billion. That's $37 billion divided by $100 million: That's 370. But they're not $100 million; they're like $50 million, so that's 740 new stores a year. That's a lot. In fact, they've just started opening a new concept. Talking about my little grid: the Neighborhood Market. It's a convenience store—45,000 square feet—just for those odds and ends you need in a hurry. Instead of taking the train to go to a supercenter—you connect through Cincinnati on the flight to go to the supercenter—you can go to a convenience store.

Whither Wal-Mart
So whither Wal-Mart: 1993 sales were $55 billion. Sam Walton died just before that. Now they're $256 billion. What do you think they're going to be in ten years' time? This is a math question. But the easy way to think about it is it's gone up about five times over the last ten years. If it keeps going at that rate, it'll be $1,200 billion; $1.2 trillion in ten years' time.

Now, remember, people said ten years ago that they could not grow at the rate they had been for the previous ten years, and they were wrong. So let's think: Is $1.2 trillion plausible for Wal-Mart? In case you fall asleep in the next ten minutes, the answer is going to be yes.

You remember the $2.1 trillion number I had up? I took out cars because it makes the numbers more interesting. So Wal-Mart, in the United States, has $209 billion out of $2.1 trillion. That's about 10 percent. Growth needs: $37 billion a year. That gets larger because of compounding, but at the moment they need an extra $37 billion a year.

Lee Scott, the CEO, says that. . . . Oh, that's the other thing, when you discuss Wal-Mart, and you say growth—in fact, if you just talk to any retailer and you say, "How are you going to grow in the next ten years?" the next word out of their mouths is "international." Lee Scott says that two-thirds of the growth in the next ten years at Wal-Mart is going to be domestic, and I think that's very sensible of him not to try to pin everything on the international.

But if that's the case, then Wal-Mart sales in the year 2013 will be $838 billion, and I did the compounding for you. U.S. total sales should be about $3.6 trillion by that time. So that means they'd have 23 percent of all retail by then. Is that plausible? “Yes” is the right answer. That ruins the next five slides.

Springfield, Missouri, has fourteen Wal-Mart supercenters, seven discount stores, and one Sam’s Club. The competition is 153 supermarkets, 125 mass merchants, 714 convenience stores, and 153 drug stores. Wal-Mart has a 27 percent share in Springfield, Missouri. Wal-Mart: 27 percent; everybody else: 73 percent.

Now, Jay Fitzsimmons, who is the head of finance, who I was talking to about this, he said that Wal-Mart—and I didn’t know this—Wal-Mart has a 30 percent share of men’s underwear. So there are all these people wearing fancy suits and driving a Mercedes, who apparently. . . . But you see—and I thought this was kind of clever; this is what gets you ahead in retailing—if he has a 30 percent share in men’s underwear, there must be like 30 percent of families shopping at Wal-Mart, right?

So that’s one thing. If 30 percent of families shop at Wal-Mart, and they start getting more and more stuff at Wal-Mart, then you’ve got a 30 percent share right there. Don’t do anything. That’s just sitting around, waiting for the United States to catch up on Wal-Mart.

But, you see, because the United States is so big, and because running a big company is so difficult, it’s taken a long time for retailers to start saturating the United States. But in other countries, saturation was achieved years ago. This is why Ahold is one of the world’s biggest retailers, because they’ve run out in the Netherlands. You open five or six stores in the Netherlands and you're looking at exports.

So in other countries, 30 percent share for the largest retailer is absolutely standard. And that’s what’s going to happen here. How many shop at Wal-Mart? More of you will by the time I finish.

Comparable baskets
So this is not Bell going out and looking at a couple of stores. This is UBS Warburg doing a study. It’s about a year old, I think. They went out and did it exactly the way you might hope they would do it. So the first study is comparable baskets. I mean, you’ve got to buy milk and you can’t get Kroger’s milk at Wal-Mart, so you have some comparability differences.

So the first one is comparable baskets—gallon of milk. And the second one is actually identical stuff. And when you e-mail me, and I e-mail this back, you can study these numbers in as much detail as you like. But the savings at Wal-Mart is like—the numbers are 26 percent, 21 percent, 22 percent, 29 percent, 21 percent, 25 percent. You spend 300 bucks a week and you're saving 25 percent. This is $75. So it takes you an hour and a half to get there. You have to figure out whether your time is worth it. But for a lot of people, it is.

Entering the used-car business
But then Wal-Mart enters used-car business with joint venture. So now they're selling cars out of the parking lots. It’s a test market, but they're trying to see if they can sell. See, by the time you arrive at Wal-Mart, it’s kind of an exhausting trip and you’d kind of like to get everything. In fact, your car’s probably worn out from having got there and you’re going to need a new one to go back.

I said at some point that American retailing is absolutely fabulous, and Wal-Mart is absolutely fabulous. But the great untapped opportunity in American retailing is automobile retailing. I mean, it's dreadfully inefficient still, even though they've worked at it. But Wal-Mart may be perfect to be able to do this. If Wal-Mart is able to pull off automobile retailing, then that 2.1—I can put the numbers back in. I'll put food service back in, too, OK? So now we're up to a much bigger number. And if they can get 27 percent of $6.4 trillion, suddenly we have a $1.7 trillion company.

I know, since retailing is not intrinsically interesting to many people, that the reason you're here is because I wrote a snappy abstract. So it says, "AutoNation has been considering whether to offer its own private-label car, according to an article in the *Wall Street Journal*." Therefore, it's true. Wayne Huizenga [Founder of AutoNation] said that they'd been approached by an unnamed car manufacturer to start offering its own private-label cars.

But you know that if AutoNation doesn't do it—if this unnamed car company is approaching AutoNation, and you're saying, "Who might be interested in launching a line of private-label cars?" Wal-Mart I think might be the answer. So I predict you're going to be driving a Wal-Mart. It's the '06. It's a souped-up Wal-Mart.

China? Everybody's been talking about China for umpteen years. You can read this later. But they're opening up like crazy. He said Wal-Mart will move its global purchasing center to Shenzhen, wherever that is. Well, it's China. So Wal-Mart, when you think about these growth numbers, getting into China—they already source. . . . You know, it's a huge amount of stuff from China, so having their purchasing center there makes a lot of sense because that's where all the stuff's coming from.

Competing against Wal-Mart
So if you're in retailing, and some of you are—I know because I talked to you—you're in retailing. You don't work for Wal-Mart, and of course you're not going to. Anybody who attended the Harvard Business School is not contemplating moving to Bentonville. So what would you do here? Well, you go back to this. If you're going to compete against Wal-Mart, you have to do something they're not doing.

Now, what are they doing from that list? Shopping experience? Matching? Well, maybe selection of assortment, but basically what these big stores do is they put everything in the store and you find it. Convenience? No, no, please. It's price. So if you're going to do something to compete against Wal-Mart, you've got to figure out something that isn't price.

Price: Zara is a hot favorite these days because Zara has a concept that is absolutely the antithesis of Wal-Mart.

So one of the important things—back to talking about retailing in general—is getting the right supply chain, and there are different supply chains in retailing. I'm going to describe three to you, of which Zara is the most interesting.

But Christian Dior has an interesting supply chain. What they do is they have these fancy designers in wherever they have them, coming up with things, well . . . things I wouldn't wear, and if I'm any judge of my wife, she wouldn't wear either. But they come up with this stuff, and what happens is that the designer comes up with this stuff. They have the show.

They then collect orders at the show and then, based on those orders, they decide how popular the stuff is going to be, and then they manufacture it. This is a great way of doing things. You like to manufacture stuff after you get the orders in.

Talbots solves the problem a different way. Talbots looks to see what's popular, and then they order the same stuff for next year, because Talbots . . . well, classics, exactly. If you're going to be in fashion, the best fashion to be in is classics because there's no hurry. If you're into the blue blazer business, you don't have to work weekends. Sales for next year are sort of like last year. So that's how Talbots solves the problem.

Now, Zara has a different approach. Zara is absolutely fantastic. Wasting all this money on R&D, like designers in Paris—a complete waste of time. What Zara does is just copies. So stuff comes out, they fax it to China or somewhere—Spain, excuse me, not China—to Spain, and they copy it, and they have it in the stores in no time.

One of the worst things about teaching marketing is that the really successful people in marketing are the people who throw out the rulebook. It's the people who contravene the five lessons of marketing that we drill in. They're the people who make a fortune.

So Zara is failing one of the key messages in the rulebook, which is, as I said at the beginning, to be in stock. They're not in stock. What they do is they copy stuff and they put some of it in the stores, and it sells out in no time. Some of the things sell out and some of the things don't. Now, the rulebook says that if something sells out, you order some more. But they don't do that. They move on to the next one.

They also have very small stores that are very close to big stores. So the idea is that you, as a customer, will go in to see what they have. It's not an inconvenience because you're going to Saks, anyway, and Zara is right next to Saks. The store is small so it doesn't take you a long time to go around it. You won't get tired. And if you see something you like, you buy it, because it's not going to be there, because they don't have enough. So you see something, you say you have to have it. Well, this is fantastic. You've got people coming again, and again, and again through your stores, and just buying anything that they see that remotely fits. It's fantastic.

Shopping experience: So, another one is shopping experience. I had a great shopping experience. It's a rare event. I was in a Nordstrom not so long ago, and it's 200,000 square feet, or something like this, and there was just me and a piano player. I wandered around. I thought maybe it was a holiday or something, and I'm in the store.

But I was in Selfridges, probably two years ago. I was in London. I went to Selfridges and Selfridges was fantastic. Selfridges on Oxford Street—absolutely fabulous. Selfridges has a mission: "Succeeds by creating an exciting shopping and leisure experience. We attract our customers by being groundbreaking and different." This is all great stuff. You've all got things just like that on your companies, but they actually do it.

So, when I was there, they had twenty-three and a half days of Bollywood. What the hell is that? It turns out that the film industry in India is called Bollywood. And India, having a billion people, anything that's for the Indian market tends to be popular. So there are all these film stars in India. It turns out they're available. So Selfridges had these Indian film stars come to Selfridges and appear. And it turns out that there are a lot of Indians in the

United Kingdom, and the place was absolutely hopping—not just Indians, the whole thing is absolutely hopping.

And I said why twenty-three and a half days? And he says, "Well, we were going to have it twenty-four, and I suddenly thought at the last minute, hey, twenty-three and a half!" And it was twenty-three and a half. It's crazy. And when people do crazy things—here's the master of this—everybody else starts saying, "Well, that's interesting." And if you're standing on your head in Harvard Square, the newspapers will be all over you, because there's nothing else to report. So, *Vanity Fair*—not a trivial magazine—is saluting Bollywood. Why is this? Because there's actually something interesting happening. So now you've got the magazines. It's PR.

And I can assure you, it was a lot of fun. It's a lot of fun being in stores where you're being jostled. Me and the piano player—I was beginning to get nervous.

Convenience: What's another one? Convenience. 7-Eleven. 7-Eleven?! I told you about Japan's stuff. The history of 7-Eleven. 7-Eleven was a clever concept: You know when it's open! I went to my CVS store for a prescription. It doesn't appear it , but I'm dying. I went to CVS. It was 8:55. I was there just in time, and the sign said, "For the convenience of our customers, we're now closing at eight."

I remember talking to the head of a drug store chain. It wasn't CVS, but they went to twenty-four-hour opening and sales went up at this drug store. But sales in the extra hours they were open were zero. But why did sales go up? Because you know they're open. It's part of the convenience. 7-Eleven: What time do you think they close?

But 7-Eleven fell on a hard time. Ito Yokado, who was a franchisee—they've got a Japanese franchise—when 7-Eleven went south in the United States, the Japanese franchise bought them. And so now they're—it's a complicated who-owns-whom kind of thing, but basically they're run by the Japanese.

There are 7-Elevens all over the world, you'll be glad to know. I have a 7-Eleven case, and I taught this to a mixed group, a global group. And I started off by asking the Japanese, "Anybody shop at 7-Eleven?" They all did and they all absolutely loved it. Loved it! Americans are scratching their heads, "What's going on here?" And I said, "OK, that's interesting. Now we'll move on." And more Japanese felt that they had been slighted by not being able to say how wonderful 7-Eleven was. "I go there to see the latest concepts." What?! And the Americans talk about gum on their shoes, about being frightened going to a 7-Eleven. This is a different concept.

But I believe people in Japan go there for fresh food, for lunch. It's delicious. I think that the food service is toast. No, not toast. One thing that supermarkets are trying do in the last several years is prepared foods. I think it's ultimately flawed because it's inconvenient. Prepared foods should be convenient. So it's convenient if you're going in for your week's shopping and also want a quick meal. But I don't know think that's the way it works. You know, you want a quick meal.

And so one answer is the restaurant or the fast food. But the other is to get your food from a store. 7-Eleven, a convenience store, and it doesn't have to be 7-Eleven, but a convenience store is the answer to that.

Every now and again I'm driving around, lost, and I pass a fabric store: "Yarn by the half-mile," or something like this. And I wonder, "Who's still making their own clothes? This can't be!" And I think supermarkets are going to be like that in twenty years' time. People buy their own potatoes? What do they do with them?

So, clothes went through this cycle where, first of all, you kept sheep out back, and I'll skip the next twenty steps. But you go to a store and you get the finished product. That's what food is going to be like. And when you buy a suit, like I do, once every twenty years, it doesn't have to be convenient. But if you're buying a meal three times a day, it does.

Apparently the head of Wal-Mart and the head of 7-Eleven—it's claimed that the only two stores that are going to be left in twenty years' time are going to be Wal-Marts and the 7-Elevens: convenience stores and nothing in between.

The Future of Retailing

So the future of retailing: automated checkout inventory. I mean, that's here. People think it's a little crazy that what you can do is just walk out of the store and say, "Oh, yeah, I checked myself out." We're going to get ripped off. But go back to the mom-and-pop store, where the person used to go in the back room and come out with a loaf of bread and then come out with a can of peas. When somebody says, "Hey, how about we have people help themselves, you know, self-service?" Hey, that's crazy, but that's the way we do it. Automated checkout is going to come.

Delivery depots. Back to the thing about distribution. We don't have a lot of deliveries at the Bell household, and our driveway is not so long. But the FedEx guy comes, the newspaper guy comes, the post person comes, the flowers. Stuff comes up the driveway. It's terribly inefficient. So maybe what happens is we can reinvent the post office and have a delivery depot where everything you order, everything that comes to your house comes to a local depot, and it's like one delivery.

Computerized agents. In the Internet era, this was a great remark, but I still think it's going to come. But with the demise of stores that actually help you to buy, a computerized agent that has your preferences of what you're looking for, and just trolls the Internet looking for different deals and creates your own catalogue. People are concerned about privacy. I've never understood this. I would be perfectly happy to have everything I ever bought on my credit card so that people can figure out what it is I might want and what it is I might not want. I think that would be a terrific service. These people that call me at 6:00 at night, 6:05, and they're selling me stuff I just don't want. It's inefficient.

Value chains as competitors. So let me close out here. What's happening with Wal-Mart—Wal-Marts have dedicated suppliers—is that the distribution setup that you learned when you studied economics, or when you tried to get away without studying economics but you kind of read in the newspaper, the idea of the capitalist system is that you have all of these interchangeable players, so there's competition. So a whole bunch of shirt manufacturers compete against one another; a whole bunch of distributors compete against one another; a whole bunch of retailers compete against one another. That's capitalism at work.

That's not the way it's turning out now. Value chains are competing against value chains. So Wal-Mart has its own suppliers. Tesco has its own suppliers. The whole chain is now integrated so it's going to be one chain versus another chain. It's still competition but it's a different form.

So I think, if there's going to be three types of players in retailing that survive, it's going to be the Wal-Mart, which I'm fairly confident about; the place that you go to for excitement, to see the latest concepts, for bustle, for fun; and convenience, which is sort of the 7-Eleven.

And that's the revolution in retailing. Thank you.