

THE FUTURE OF DEPARTMENT STORES

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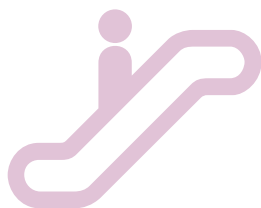
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THE FUTURE OF DEPARTMENT STORES

ERIK VAN HEUVEN & STEFAN VAN ROMPAEY

9 ESCALATORS TO A GOLDEN FUTURE FOR THE DEPARTMENT STORE





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SALE

PREFACE

A new future for department stores

At their beginnings in the 19th century, department stores were hubs of activity, events, innovation, aspiration and shopping. The best still are, but the format has evolved, and that evolution has been dependent on four variables: context, competition, customer and control. These represent; firstly, the impact of the economic and political world on the business; secondly, the relentless incursion of new formats eating away at the department store market share; thirdly, the apparently endless effort of predicting (or chasing) the customers' desires; and fourthly, the tools (technology, organisation and management) available and chosen to operate a sustainable and profitable business. These variables explain why and how the format has been changing and provide indications of a prosperous future which can already be perceived. Department stores are demonstrating a remarkable resilience, which is reflected in some of the great companies mentioned in this book and the choices they are making with an engaged, inspired and visionary leadership.

CONTEXT
Economic and political



COMPETITION
Formats and business models



CONTROL
Management, technology
and organisation



CHOICES
New future
department store

CUSTOMER
Experience and data



//CONTEXT “The biggest revolution since the early days of shopping.” (Adam Fenwick)

Although department stores, at least in the West, have grown as a format since the 1980s, it has more recently become abundantly clear that the polarisation of wealth and income, along with low economic growth, yields political and economic turbulence, uncertainty and discontent. It is no accident that many department stores have shifted towards the luxury end of the market. It is also likely that we will be seeing an increase in measures focusing on margin rather than top-line growth, and this includes department store online retail which “remains an inefficient model” (*Ronald van Zetten*). Revised business-model thinking cannot ignore shifts like the 2019 declaration of the Business Round Table which emphasises the creation of value for all stakeholders and which has been signed by over 180 CEOs from major companies.

//COMPETITION “Our strategy is clear: we want to be a veritable destination store.” (Franco Savastano)

Successful department stores have remained true to their origins. Although buffeted by the serial skirmishes with other retail formats, and sometimes, we have to admit, losing their original focus, the best department stores have developed as the destinations and laboratories of innovation that made them so irresistible at their beginnings. They might occasionally have been tempted to emulate the convenience and value of variety stores, the price and volume of hypermarkets, the cost structure of big-box retailers, the diversity and experience of malls, the bargains of outlet stores, the appeal and responsiveness of fast fashion chains or the service and fulfilment promises of e-commerce. And they may have learnt from them. But the DNA of department stores remains its fundamental attraction as a destination offering innovative experiences.

//CUSTOMERS “Don’t sell products, sell memories.”**(Vittorio Radice)**

Unlike the early aspiring department store customers in the days of industrialisation, today’s customers are no longer searching for products but for “entertainment” (*Maurizio Borletti*), “relationships” (*Philippe Houzé*) or “dreams” (*André Maeder*). The department store business is turning into show business, and its most inspiring leaders into impresarios. Combined with designer buildings in notable cities, stores have often become unique local landmarks, making them even more attractive to tourists. The power has passed from the hands of retailers in a supply-driven economy into the hands of customers in a demand-driven one. Sometimes, these customers demand convenient or frictionless retail; sometimes, they search for experience and friction. In either case, without sustainability and purpose, the retail brand doesn’t stand a chance. The key to knowing your customers is data collection and management: the future motor of the business.

//CONTROL “People, people, people.” (Olivier Van den Bossche)

The early history of department stores is inextricably linked with “scientific management”. In the early 20th century, new forms of organisation paired with emerging technologies gave birth to a type of management which lasted almost a century, albeit in adapted forms including “lean”, “six-sigma”, or “digital Taylorism”. Hierarchical organisation and mechanical technologies compensated for low skills and delivered the efficiency which department stores lacked in comparison with their industrial counterparts. Profits were squeezed from economies of scale in a growth context. It wasn’t until the end of the 20th century that the emergence of the “learning organisation”, combined with low-cost digital technologies, shifted the game towards a service economies employing engaged staff organised in agile flexible structures. This is probably the greatest challenge department stores currently face. While the traditional model was based on solving complicated issues, the future world is forced to face complexity and the puzzling science of non-linear systems. For this reason, investing in training and education is as important for the future as investing in technology. And business education is already beginning to look quite different from what it has been.

//CHOICES “Customers will either recognise themselves in a brand’s values, or they won’t.” (Philippe Houzé)

Contrary to the fundamental tenet of scientific management, it is clear that today there is no “one best way”. However, it is also clear that department stores need to make choices and determine priorities. These concern investments, assortments, price, logistics and supply chain, people, design and experience, and more. Today, a department store may choose to focus on entertainment, fulfilment, curation, innovation, or value. Only when the model is clearly defined can a consistent brand be developed and can the department store recover the attractiveness it enjoyed as a laboratory of innovation.

Hybrid brands are a source of unsustainable confusion, and respond neither to the needs of customers nor to those of stakeholders. But in the interviews that follow, we may already glimpse examples of the new future department stores, which combine clear purpose and values with a sustainable 21st-century business model.

The International Association of Department Stores (IADS)

By 2020, the IADS will have successfully served some 60 department store companies from all continents for 92 years, but now it faces the same challenges as its member companies: how to best prepare for an uncertain, turbulent future in which speed, adaptability, and learning become the new requirements of success, while at the same time maintaining its integrity and the profound values which have made it unique. The journey has begun, with a commitment to further develop the successful Academy learning and development programme, the rich IADS online offer and platform, as well as future-oriented “labs”, exchanges and workshops.

Dr Christopher Knee
Deputy General Manager
International Association of Department Stores (IADS)



A QUICK DEFINITION

We want to emphasise early on: this book is about the sector of department stores, not to be confused with grocery stores, supermarkets or hypermarkets. A department store originated in the mid-19th century and is a large shop – often in an imposing multistorey building – which sells a wide range of goods, from a wide variety of non-food products such as fashion, perfumery, interior decoration, household products, toys ... Well-known department stores include Harrods, Galeries Lafayette or De Bijenkorf. Initially, food was not a category of importance in the department store. Today, this has changed. We'll explain that later on in this book.



INTRODUCTION

From one revolution to another

Department stores owe their origins to the first industrial revolution and rose to unprecedented heights in the first half of the 20th century. In recent decades, however, they threatened to fall victim to yet another industrial revolution - the digital one. But perhaps this turbulent era also offers the prospect of new perspectives for the future.

Will the forerunner become a museum?

It may seem odd: a book about the future of department stores, precisely at a time when many European and American department store players are in dire straits. Is there, in fact, a future? Aren't the forerunners of modern retail doomed to disappear, usurped by new models such as discounters, category killers (large-scale specialised retailers dominant in one category) and e-commerce? Are the former retail palaces still relevant for today's consumers, or will they become retail museums?

These are all pertinent questions, to which this book tries to formulate an answer, on the basis of analyses by retail experts and interviews with top managers hailing from the sector. Even though the picture doesn't look particularly rosy, our observers and interlocutors do discern opportunities, provided that the companies involved reinvent themselves. Today, their heritage, their rich history and their names which still capture the imagination no longer suffice to claim a top position in the minds of modern consumers. They want more.

Industrial revolution

Department stores were indeed pioneers, once upon a time. They came into being in the mid-19th century, as the first form of organised, large-scale retail. Before that, there were markets and itinerant traders, but there were no such places as fashion shops: people made their own clothes, or hired a tailor if they had the budget. Everything was made to measure. The same held true for furniture: craftsmanship was the norm.

That is until clever merchants saw potential in a new way of doing business. For the consumer, it was a revolution: the new shops had fixed, low prices, which made bargaining a thing of the past. The supply was greater than ever. You could find ready-to-wear clothing, and you could walk in and out without any purchase obligation. The world was experiencing the start of mass production. It also marked the beginning of advertising campaigns and promotions. For the first time, shopping became a pleasure rather than a necessity.

This retail revolution ran parallel to the industrial revolution: the whole world changed radically. New means of transport opened up new trade routes - it was not without reason that the first department stores often settled in the vicinity of train stations. Technological progress, like steel construction, made it possible to erect large buildings more efficiently, with imposing architecture. Electric lighting brought about unprecedented possibilities. The escalator saw the light, an indispensable element in any department store. It is so decisive for the shop image that we gave it a central role in this book.

Stores disappear

Today, the world - and therefore the retail sector - is experiencing a new industrial revolution. The impact of digitisation and robotics is only just beginning to manifest. The messages of doom swell. And indeed, in recent years, the number of department stores has fallen sharply. A lot of chains saw no other option but to restructure and cut back on the store network. The Dutch newspaper *Het Financieele Dagblad* calculated that over the past decade, no fewer than a hundred department stores disappeared in Western Europe alone.

In the UK, for example, reputable retailers such as Marks & Spencer, House of Fraser and Debenhams had to close dozens of stores. BHS (British Home Stores) went bankrupt in August 2016: 163 stores were closed instantly because no buyer was found ... In the Netherlands, department store chain V&D went bust. Successor Hudson's Bay failed to fill the gap and had to throw in the towel after less than two years. In Germany, both GALERIA Kaufhof and Karstadt (which already went bankrupt in 2009 and was then taken over by American-German billionaire Nicolas Berggruen) restructured, and now that both players have merged, even more store closures can be expected. In the US, too, a lot of retail icons are forced to drop out: Sears, Kmart, Macy's, JCPenny, Neiman Marcus, Barneys ... They are all going through painful restructuring or are on the verge of disappearing. They call it a "retail apocalypse" ...

Cornered

The analysis is the same for each bankruptcy and restructuring. There are too many department stores, especially in the middle segment. Competition is fierce. In every industry, specialists have taken over. Fast fashion groups such as Inditex, H&M Group and Primark have taken over the high street with brands serving different target groups. In the furniture sector, Ikea, JYSK and made.com set the tone. Electronics are the area of MediaMarkt and Fnac Darty. We could continue this list for a while.

What's more, there's the strong rise of e-commerce, which is putting pressure on profitability in all retail sectors. Traditional, physical retailers are cornered: they must continue to invest in the level of physical experience of their stores in order to remain attractive to the spoilt digital consumer. At the same time, they need to develop their own online channel, which in turn requires major investments in IT, artificial intelligence and logistics. All this in a stagnating or declining market, with constant pressure on prices.

The math is simple: the situation is untenable. Retailers have to make gruelling choices in order to survive. But that's a sore point for most department store chains: all too often, they want to be everything to everyone. This, after all, was once the foundation of their success.

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There is also a demographic factor at play. The rise of the department store paralleled the rise of the middle class. Today, that population group is struggling in the mature markets of Western Europe and the US. The middle class is under pressure, especially the younger generations of the millennials and the centennials. We are faced with a polarisation: on the one hand, discount retailers are doing well, on the other hand, the luxury segment is holding up. The middle segment is bleeding out.

In search of success recipes

Conclusion? According to a lot of experts, exclusive luxury department stores only have potential in the major shopping cities: tourist magnets such as Harrods and Selfridges in London, Le Bon Marché, Printemps and Galeries Lafayette in Paris, KaDeWe in Berlin or La Rinascente in Milan and Rome. Their number of visitors and turnover are still rising, thanks in part to the growth of international tourism. From emerging markets such as China, Russia, India and the Middle-East, wealthy members of the middle-class come to Europe, seduced by the dreams that big luxury brands and historical cities of art manage to sell so cleverly. Those sumptuous shopping palaces still have a future.

For the middle section, however, the final downfall is looming, or so it's said. But is that really the case? We believe some nuance is in order. First of all, the position of those exquisite luxury department stores is not invulnerable. A lot of luxury brands open their own flagship stores, in the same shopping cities and streets where prestigious department stores are active. Additionally, those brands boast their own online channels - while most department stores follow rather reluctantly. Pure players like mytheresa.com also threaten the luxury segment.

John Lewis is bravely holding its own in Great Britain, as is Galeria Inno in Belgium. The Spanish El Corte Inglés even managed to grow considerably. These are certainly not luxury department stores, but players in the upper middle class. They sell a wide range of well-known brands at accessible prices to a large public. So what's their recipe for success?

In this book, we look for the ingredients for a future-proof department store. We consult talented leaders: managers and investors who have developed a real helicopter vision based on their international positions and rich practical experience. We translated their valued input into nine escalators to success for the department store sector.

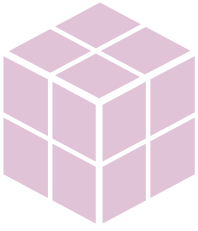
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“Managing a department store is like solving a Rubik’s cube”

Maarten de Groot van Embden (M3Cube)

To be successful again, department stores need to return to their origins: large flagship stores that amaze the shopper with an unrivalled assortment, flawless service and a unique experience. “The average doesn’t work for department stores.”

For 26 years, Maarten de Groot van Embden was secretary-general and general manager of IADS, the International Association of Department Stores. It is the oldest association of department stores, with members from 25 countries, who exchange knowledge and experiences. “Because these members are no direct competitors of each other, they can speak freely.” From this position, our interlocutor has an extensive network and a unique knowledge of the department store industry worldwide. Few people are, therefore, better placed to give us more insight into the trends and evolutions that characterise this sector in motion.

Transport and tourism

“Department stores were the first organised form of retail. They arose in the mid-19th century, in France, Great Britain, the US ... Initially, they were still quite small according to our standards, around 2,000 square metres (21,500 square feet), but they quickly grew bigger and they started to sell more different product categories.”

There is a lot of discussion about which department store came first. Maybe it was A.T. Stewart on Broadway in New York, in 1848. That shop was also called

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the “marble palace”. Bainbridge’s opened in the British city Newcastle in 1849. And Le Bon Marché in Paris dates back to 1852. From the early years, the importance of an ambitious architecture was significant. That had everything to do with the industrial developments at that time. Electricity and the escalator made their appearance. New steel constructions made it possible to erect large buildings. In Mexico City, for example, the five-storey department store Palacio de Hierro, literally “palace of steel”, opened in 1891. Department stores were often built near train stations. “Transport is still an important factor today. I still see enormous opportunities for shopping malls at airports, for example. Tourism is and remains an important source of income for department stores. At Galeries Lafayette, 60% of the turnover comes from visitors from overseas.”

National identity

“Worldwide, you can currently see significant differences in the positioning of department stores. In most Western European countries, for example, department stores are positioned upscale, like Le Bon Marché or Selfridges. But that is certainly not the only option. In some countries in Asia and South America, for example, you see that they are cheaper and more accessible in the market. And that was originally the case in Europe as well: the first British and French players were also cheap. Thanks to their economies of scale, they were able to purchase larger volumes and sell the products at lower prices. In growth markets, you see the same process taking place now.”

In countries such as India, the Philippines or China, larger department stores are appearing, spanning more than 100,000 square metres (1,076,000 square feet), which combine goods and services – sometimes, they even have a church in the store. “Situations can vary significantly throughout the world. A department store always has a national identity, so the concept is difficult to export or internationalise.”