



DEFINING A PROFITABLE AND RESILIENT PATH FORWARD IN RETAIL

PRACTICAL GUIDANCE FOR RETAIL CFOS

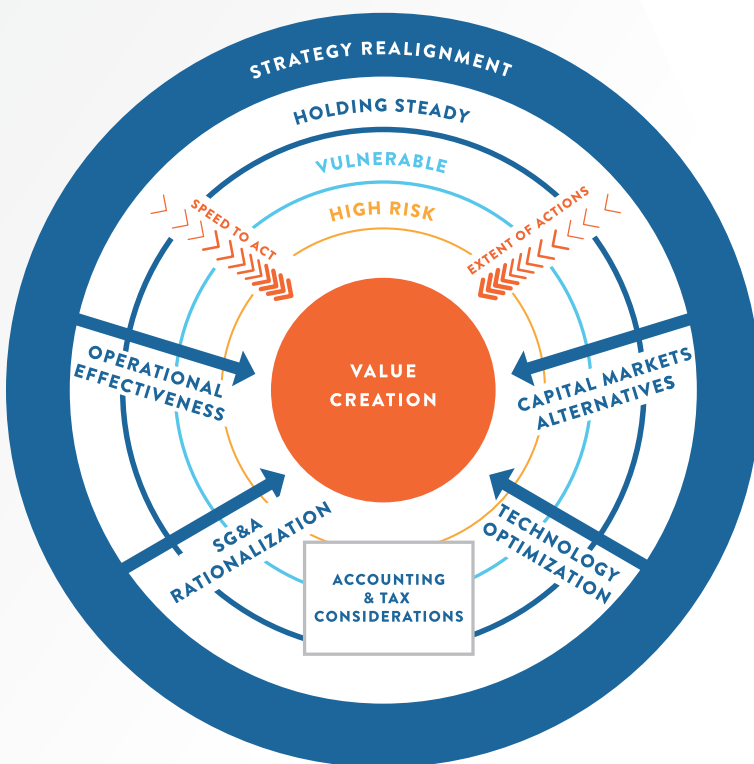
The retail industry is at an inflection point. COVID-19 has shuttered factories worldwide, disrupted global supply chains, and stalled physical retail. With production reduced and overall demand significantly down, companies have to create demand for their products in the face of changing resources and a shifting global landscape. While the supply side can be managed by retailers that identify alternative supplies and production sites, changes in demand are harder to influence as customer sentiment is difficult to affect. In order to reopen, retailers are also faced with the logistical challenges of bringing back furloughed employees and resuming operations at malls across the country. And, once the stores are open, it is still uncertain how quickly customers will reembrace in-store shopping.

Within the retail industry, food and non-food retailers are facing different challenges due to the roles they play in consumers' lives. Food retailers have experienced a spike in demand, witnessing in March their highest levels of growth in almost 20 years, despite supply chain disruptions, complexities in store operations (e.g., how often and how to clean stores), and staffing issues. Non-food retailers have borne the brunt of the shock, as demand and liquidity continue to plummet. In March alone, sales were down 51% for apparel and accessory stores. That same month, retail sales saw their worst month-over-month drop on record, falling 8.7 percent from February. Consumer spending fell an annualized 7.6 percent during the first quarter, the largest drop since the second quarter of 1980¹. The retail industry is expected to lose approximately \$430 billion in sales between March and June².

DEFINING THE PATH FORWARD

To maintain business continuity and resiliency, non-food retailers must proactively deal with the immediate turmoil and prepare for what the new normal will bring. The magnitude of the current disruption, which is high for most retailers, and the core health of the business will dictate the extent and speed at which change must be implemented. Companies that navigate the immediate disruption, near-term planning and transition period, and long-term transformation will come out ahead.

Our guide, [*The Next: Defining Your Path Forward*](#), provides a structured approach and practical guidance to lay the groundwork for preserving profitability and maximizing stakeholder value in the post-pandemic operating environment.



STRATEGY REALIGNMENT

Assess your near- and long-term strategic initiatives and realign to an extended period of reduced discretionary demand.

VALUE LEVERS

Create value for the organization across marketing, operations, SG&A, technology, and capital markets.

ACCOUNTING & TAX CONSIDERATIONS

Proactively address potentially challenging accounting, financial reporting, and tax issues and opportunities.

Retail CFOs and other leaders must prepare for the future by navigating the immediate disruption and fostering long-term resiliency through strategic planning and successful implementation of transformation initiatives. Retail CFOs should consider the following priorities and action items to help define and drive the path forward.

STRATEGY REALIGNMENT

Reassess near- and long-term strategy and determine which initiatives are most critical to implement to achieve business objectives.

- ▶ Update financial models to reflect new 'normal' from revenue (e.g., store traffic, category mix, average unit retail, and basket size are likely to change) and cost sides (stores, distribution centers (DC), fulfillment, vendor managed inventory)
- ▶ Create scenario analyses of rate of recovery of consumer demand and run associated models
- ▶ Elevate the importance of e-commerce organizationally and through distinct forecasting
- ▶ Lead finance and accounting organizations through near-term change, cost reduction, and efficiency efforts
- ▶ Co-author roadmap for full end-to-end digital readiness with other functional leaders for a more "virtual" near-term reality (virtual sampling, virtual showrooms, virtual events, etc.).
- ▶ Work with chief merchant on financial and strategic projections for fall/winter
- ▶ Analyze real estate footprint and associated store (re)openings and permanent closures, including store layout and sizes, as well as operational issues such as allocations, sanitization, and traceability
- ▶ Assess opportunities to enhance e-commerce business to offset brick and mortar downturn
- ▶ Evaluate opportunities to convert existing stores to dark stores for e-commerce fulfillment
- ▶ Actively engage in defining and helping to drive cross-functional initiatives
- ▶ Lead forecasting and financial modeling on all initiatives for inclusion in financial results

OPERATIONAL EFFECTIVENESS AND SG&A RATIONALIZATION

Drive meaningful and sustainable improvements in profitability and cash generation through quick decision making and execution across key revenue and direct cost levers. Optimize overhead structure by variabilizing cost basis to drive greater alignment between revenue generating and support activities.

- ▶ Baseline current costs and identify key value levers setting targets by functional area
- ▶ Analyze inventory levels throughout supply chain and assess further order cuts; decide on actions for excess inventory (e.g., take markdowns, sell to off-price retail, hold in DCs until next relevant season)
- ▶ Renegotiate leases and lease exits with landlords
- ▶ Drive store labor cost models with expected increase in customers utilizing curbside pick-ups (BOPIS) instead of in-store shopping as well as additional costs due to personal protective equipment for store staff
- ▶ Focus on driving operational excellence (at stores, DCs, and corporate) working with COO and other key stakeholders, including initiatives such as zero-based budgeting, vendor consolidation, permanent reduction of discretionary spend, outsourcing of non-core activities, and lean operations.
- ▶ Model medium-term risk of cuts and financial impacts/ROI of growth initiatives
- ▶ Evaluate return on investment and structure of loyalty/rewards program with CMO and analyze marketing mix
- ▶ Assess third-party risk exposure in areas such as accounts receivable, IT, and supply chain
- ▶ Upgrade supply chain monitoring and management capabilities

TECHNOLOGY OPTIMIZATION

Leverage existing tools and platforms to reduce costs while also preparing for new ways of working and dynamic growth in the future.

- ▶ Assess technology options for stores, DCs, and back office to drive efficiency and enhance the shopper experience in the new normal
- ▶ Optimize, postpone, and reduce IT spend leveraging existing tools and platforms, shutting down non-critical, low-usage tools and accelerating migration to cloud technologies
- ▶ Analyze vendor matrix and consolidation opportunities
- ▶ Enhance online security and business continuity/redundancy plans and tools
- ▶ Implement and/or enhance tools and technology critical for the new normal (e.g., more digital retail and upgraded expectations for traceability, safety, and security)

CAPITAL MARKETS ALTERNATIVES

Pursue capital market solutions that support both near-term liquidity requirements and the long-term growth strategy.

- ▶ Focus on cash: delay accounts payable and collect unpaid accounts receivable, draw down lines of credit, file for the Paycheck Protection Program (if applicable), renegotiate debt and lease terms, monitor performance versus covenants, and investigate asset-based credit options
- ▶ Optimize existing capital sources/restructure existing debt
- ▶ Investigate new funding sources (debt and equity)
- ▶ Divest to free up capital or monetize embedded value

ACCOUNTING & TAX CONSIDERATIONS

Proactively address challenging accounting, financial reporting, and tax regulatory issues to ensure external reporting to stakeholders that fosters timely and informed decision making.

- ▶ Incorporate impacts of negotiated lease changes, such as modifications or rent concessions
- ▶ Identify impairment implications for assets (e.g., store assets, right-of-use assets, goodwill and other intangibles) due to decline in revenue
- ▶ Identify proper treatment and disclosure of restructuring charges, such as headcount reductions, lease cancellations, or store closures
- ▶ Evaluate inventory for obsolescence based on decrease in volumes

HOW WE CAN HELP

Retail demand will likely remain low in the near term, as we continue to work our way out of the current crisis. Once the economy begins to rebound and demand for consumer goods picks up, retailers can pivot from their current defense-oriented positioning to a more aggressive go-to-market approach that will enable them to emerge even stronger.

With our deep finance and operations expertise and experience guiding retail CFOs and their organizations through times of distress, we help retailers to preserve profitability and maximize stakeholder value in the post-pandemic operating environment. Contact our Retail lead, [Anand Raghuraman](#), to learn more.

¹ *National Retail Federation Monthly Economic Review: May 2020* Jack Kleinhenz, Chief Economist, May 6, 2020

² *The Impact of COVID-19 on the Retail Landscape* Kantar, April 17, 2020