RETAILING MANAGEMENT

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Newsletter for Instructors

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Using AI to Navigate the Rock and Hard Place of Retail Returns

Use with Chapter 5, “Customer Buying Behavior”, Chapter 6, “Retail Market Strategy”, and Chapter 10, “Information Systems and Supply Chain Management”

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Talk about being stuck between the Scylla and Charybdis. Retailers love it when shoppers buy more; it’s a central goal of many of their marketing efforts! But consistent data also show that the shoppers who buy the most are also the ones who return the most items, and the costs of returns represent one of the most central negative measures that retailers seek to avoid in their marketing efforts. So what’s a seller to do, stop selling more, or accept more returns? With effective AI, they might have another option that will allow them to set sail into a profitable future.

By carefully tracking what happens when people click on search ads, including what they buy, how many, and what they return, machine-learning–based AI can establish which customers tend to be most likely to return products they buy. Then those algorithms combine those data with insights about the return rates for specific types of products (which different retailers can define however they want). With these combined data, the AI system offers real-time predictions about returns and the profits on each sale.

Once it has enough of these combined data points, it integrates all of them together, which then provides meaningful insights into where to target search ads, namely, to whom and for which products, in a way that encourages sales without increasing the risk of return behaviors. One Dutch fashion retailer that adopted such a system ultimately rethought its overall strategy: Rather than trying to increase sales, it would aim to increase customer lifetime value. Thus, it stopped targeting its advertising to consumers that it knew would buy, but that it also predicted were likely to return. As a result, its returns have decreased, even if just by 5 percent, but its profits have risen by 16 percent.

This direct application thus seems effective, but other retailers appreciate more indirect uses of AI to ensure they can keep appealing to all their customers. Consider Perry Ellis for example: “After identifying items with the highest return rates, they used AI sentiment-analysis tools to determine which phrases in those products’ descriptions might create confusion over key elements, such as size or fit, that most often lead to returns.” If consumers were returning clothing because they were confused about its specific attributes when they placed the order, then clarifying the information could eliminate this risk, at little cost. For example, buyers assumed that the simple phrase “Machine Washable,” that appeared on digital product pages for some of shirts meant they could throw the tops in with their regular laundry. But the fine cotton or linen actually requires more gentle care, so the product pages now specify, “Machine wash according to instructions on care label.” Simply by alerting consumers to the need to take more care in washing the items, the brand lowers the risk that people demand returns after just one wash, when their delicate shirt has unraveled after being washed with jeans and towels.

Such efforts are in line with the relatively longer-standing applications of AI by fast fashion brands that rely on machine learning to provide more accurate recommendations to online shoppers. If they buy the right size or know precisely which accessory goes with an item already in their cart, the reasoning goes, they will have less reason to initiate a return. But nearly every retailer continues to look for effective, efficient ways to build on and extend such insights to reduce returns. Today’s consumers believe that easy, free returns are their right. As a result, following the most recent holiday season, they returned an estimated 16.5 percent of the items that were purchased, accounting for approximately $817 billion in returns. That’s a level that demands dedicated AI attention.

Discussion Questions

1. How often do you return items to retailers, and why? Could better information make you return less?

Sources: Patrick Coffee, “Retailers Enlist AI in Fight Against Returns,” *The Wall Street Journal*, December 18, 2023; Liz Young, “Retailers Are Bracing for Their Postholiday Returns Hangover,” *The Wall Street Journal*, December 26, 2023

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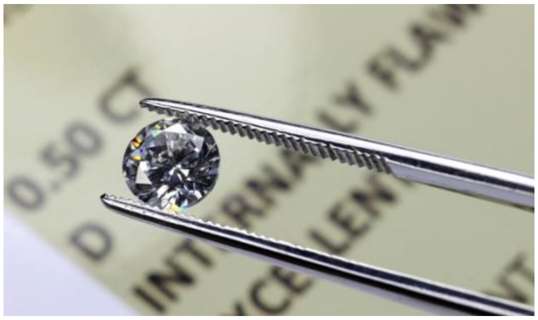
Seeking Clarity in Determining the Value of Diamonds

Use with Chapter 5, “Customer Buying Behavior”, Chapter 14, “Retail Pricing”, and Chapter 15, “Retail Communication Mix”



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Luxury gemologists and retailers often refer to the 4Cs as criteria for assessing the quality of a diamond (i.e., color, cut, clarity, and carat). But for today’s consumers, are those four features sufficient to define the value of such a major purchase? Diamonds offer an especially compelling example for understanding how value can be created, seemingly out of nothing, by good marketing. In the late nineteenth century, the discovery of huge diamond mine reserves threatened to undermine (sorry) the market and drive prices rapidly downward. Because it held a near monopoly on the market, such that it could create a global conglomerate, De Beers worked quickly to avoid this development. It launched a remarkable, well-known, and highly successful campaign (“Diamonds Are Forever”) to convince consumers that the hard, clear, pressurized carbon stones represented the epitome of luxury, as well as the only real way to express love. Soon, diamonds came to be expected as a signifier of affection for any couple deciding to get married.

But as is true of so many traditional forms of consumption, today’s consumers are questioning some of expectations surrounding diamonds. Informed by ethical concerns about blood diamonds and exploitation, some people refuse to consume them whatsoever. In turn, some innovators have proposed lab-grown diamonds as an alternative. Although they occur naturally in only select areas, the gemstones can be created in any setting that imposes enough pressure on carbon, and in just a few weeks. There is thus no concern that miners will be subject to hazardous conditions or that mining operations will pollute the surrounding area in this process. Instead, there are other concerns, based in the amount of energy required for labs to grow diamonds. Because of the energy demands associated with their production, it may be hard to make the argument that lab-grown diamonds are really the sustainable alternative.

However, they are the less expensive option. Mined diamonds remain extremely expensive, such that a recent survey indicated that the average cost of an engagement ring was around $6000. Among Millennial and Gen Z consumers, such a substantial outlay of money seems unnecessary; for many of them, the idea of spending their budgets on a fantastic honeymoon vacation seems much more appealing. Rather than being impressed by the traditional lore surrounding mined diamonds, they find little value difference and deeply appreciate the lower price point for the lab-grown diamonds. The price gap also continues to grow, as production of lab-grown diamonds increases, such that for the same size and clarity, buyers will pay approximately 80 percent for a lab-grown versus mined diamond.

Diamond retailers have responded to these trends in various ways. Some of them have fully embraced the shift, offering both mined and lab-grown diamonds in the same space. But others—especially older, more luxury-oriented retailers—have rejected the lab-grown option out of hand. They cite concerns about the legacy of the manufactured diamonds, which appear unlikely to hold their resale value as well as conventional stones. But they also probably are worried about their own value—that is, the profits they can earn from selling beautiful diamonds at very high prices.

Discussion Questions

1. Of course we’re going to ask: If you were to begin shopping for engagement rings, would you look for a mined or a lab-grown diamond? Why?
2. How should diamond sellers price their offerings of mined and lab-grown diamonds strategically?

Sources: Katie Mather, “Are Lab-Grown Diamonds ‘Worthless’? Experts Weigh In as Engagement Ring Priorities Shift for Millennials, Gen Z,” Yahoo!Finance, January 26, 2024; Thomas Biesheuvel, “Diamond Demand Is Falling so Fast–Courtesy Lab-Grown Stones—and De Beers Is Cutting Some Prices by More than 40%,” *Fortune*, September 3, 2023; Uri Friedman, “How an Ad Campaign Invented the Diamond Engagement Ring,” *The Atlantic,* February 13, 2015

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A Wrinkle in Segmentation: The SephoraKids

Use with Chapter 5, “Customer Buying Behavior”, Chapter 6, “Retail Market Strategy”, and Chapter 16, “Human Resources and Managing the Store”

istockphoto / Arsenii Palivoda

A conventional segmentation approach for skincare and beauty brands relies on consumers’ current needs. People with dry skin get targeted with inducements to buy serious moisturizers; those struggling with acne might receive coupons for products with salicylic acid; and aging consumers often see personalized advertisements for eye creams or overnight lotions that contain retinol. In addition to reflecting the desires of these consumers to obtain solutions that help them look better, this segmentation philosophy is need-based. A consumer with oily skin should not use products formulated to overcome dryness for example.

For most consumers, these sorts of personalized targeting efforts make sense. But some consumers go in the other direction, purposefully and perhaps recklessly seeking out offerings that were never designed for them. That type of behavior is the defining trait of a newly identified group of consumers, referred to on TikTok by the hashtag #sephorakids. These preteen shoppers make a habit of hanging out in physical beauty retail shops, such as Sephora and Ulta, where they trial, experiment with, and purchase skincare products that were formulated for much older people.

Notably, any 10-year-old kid likely lacks the consumer sophistication needed to fully understanding advertising messages. That is, perhaps they simply misunderstand the purpose of antiaging creams that contain relatively harsh acids, designed to address concerns like age spots and wrinkles. But their purchasing habits also might result from arguably irresponsible marketing. These young shoppers have nearly constant access to influencers, many of whom make their skincare routines central to their content. Having watched innumerable beauty experts and influencers spread series of serums, toners, creams, and oils onto their faces, perhaps they believe that everyone should be doing the same, even at their young age.

In turn, some brands are actively catering and marketing to these young shoppers, as part of their constant efforts to expand into new markets and grow their market share. Even if preteens should not be using retinol, brands such as e.l.f. and Bubble stock other formulations that they say can improve the skin texture of young users. The Yawn brand even markets its products as appropriate for children as young as 3 years of age. As detailed by a beauty industry researcher, “I’m also increasingly seeing girls younger than teens using adult products…. From a business perspective, the marketing is there; these younger age groups are actively being targeted.”

In addition to concerns about the risks and implications for young users—including that they are being overly sensitized to worry about their looks and that they might cause real damage to their skin by using harsh products on it—other issues arise with regard to their behaviors while in stores. The thousands of TikTok videos with the #sephorakid hashtag mostly represent complaints about the inconsiderate, entitled, and downright rude behaviors displayed by the preteen shoppers. Employees tell stories of being treated rudely when they tell girls that they are out of stock of new product releases by popular brands such as Drunk Elephant. They also post videos displaying the mess left behind by the children, with spilled serums, ruined lip glosses, and carved up eyeshadow samples. In addition, regular shoppers express their near shock at being “bullied” by kids in the store who try to cut the checkout line, comment on their looks or age, or snatch desired products out of their hands.

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Such anecdotes suggest a deeply unpleasant shopping experience for many consumers and retail employees. But other evidence indicates that there is little chance that the retail stores will seek to put a stop to the preteens' behaviors: Recent market analyses predict that the baby and child skincare market will grow at a nearly 8 percent annual rate, to reach an estimated $380 million in market value.

Discussion Questions

1. How would you explain the growing use of skincare products, designed for older age segments, among young consumers? What do you think is the most influential driver of this consumption behavior?
2. What should retailers do in response to such developments, if anything? Should their goal be to sell to new customer segments, protect the enjoyable shopping experience of existing customers, or something else?

Sources: Mia Taylor, "'Sephora Kids' and the Booming Business of Beauty Products for Children," BBC, January 22, 2024; #sephorakids, TikTok; Statista, "Baby and Child Skin Care–Worldwide," October 2023, https://www.statista.com/outlook/emo/beauty-personal-care/skin-care/baby-child-skin-care/worldwide.

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Continued, Global Price Inflation and the Implications for Branded and Private-Label Retailing

Use with Chapter 7, "Financial Strategy", and Chapter 14, "Retail Pricing"

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Global-level shocks, including not just the pandemic but also extreme planetary weather conditions and international wars and conflicts, continue to disrupt and challenge manufacturers' ability to get products into stores, retailers' ability to ensure sufficient stock, and consumers' ability to find the items they need at a reasonable cost. Even if the most intense inflation of recent years has eased somewhat (remember when eggs were $12 per dozen?), prices on many consumer goods remain troublingly high, with implications for every actor and every price in this supply chain.

In particular, consumers are frustrated and unwilling to keep spending more to get the same amount, or even less, on their regular shopping trips. As a result, their preferences have clearly shifted, toward less expensive and private-label offerings. Although this market has been growing steadily in recent decades, the tumult of the past few years has increase the pace of the transition. According to Nielsen reports, shares of private-label food items increased by 16 percent in a recent two-year period, for example.

Such expansion in private-label success is being egged on by retailers that are determined to keep their customers satisfied and prevent them switching to another, potentially lower priced store. In noting the vulnerability of national brands to price challenges, a vast number of retailers have initiated or expanded their private-label offerings. According to Target's assessments, its store brands, like Good & Gather, have achieved growth rates nearly twice those of branded competitors.

But retailers' responses are not limited to expanded store brand strategies. They also are actively pushing back against product manufacturers that continue to charge high wholesale costs. In France, Spain, Belgium, and Italy, the Carrefour grocery chain simply removed all PepsiCo. products from its shelves, until the beverage and snack provider agreed to lower the prices it was charging. In store aisles, consumers looking for Doritos or Pepsi instead will find signs, placing the blame on PepsiCo. for continuing to raise its prices at a pace even higher than the countries' inflation rates. Notably, Carrefour also has been adding display signs to highlight the manufacturer practice of "shrinkflation"—that is, when companies subtly redesign their products so that the packages contain less volume but continue to charge the same price—so that consumers are not fooled by a hard-to-detect change in container size or shape.

For manufacturing brands, these trends have culminated in intense pressures. PepsiCo confronts the possibility of extended unavailability in Europe; Unilever (which owns brands like Dove soap and Ben & Jerry's ice cream) has been forced to lower its revenue predictions and admit to substantial losses in many of its market segments. Procter & Gamble similarly lowered its profit forecasts for the coming year.

It may be hard to feel particularly sorry for these brands though. The past several years have seen them enjoy tremendous and increasing profits, due to some of the very same macroeconomic factors that are now creating the challenges. For example, noting that people suffering from post-pandemic stress were happy to pay more to access little daily luxuries, like really good snacks or fancy hair care products, many national brands flexed their pricing

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power to obtain the highest profits they could. Now that consumers are tired of paying those higher prices though, the manufacturers appear largely unwilling to lower the costs back down. They also claim that their own costs have risen, such that simply maintaining their margins requires these high price levels.

Discussion Questions

1. If you were advising a grocery retailer, how would you recommend it deal with continued high prices on consumer goods? If you were instead advising a manufacturer facing blowback for high prices, what would you recommend?
2. In your opinion, are prices for consumer goods ever likely to come down?

Sources: Richa Naidu, "Unilever's US, European Market Share Slips as Private Label Booms," *Reuters*, January 24, 2024; Mauro Orru, "Supermarket Giant Drops Pepsi and Lay's over Price Increases," *The Wall Street Journal*, January 4, 2024; Jesse Newman, "The Supermarket Aisle Where Prices Are Still Rising," *The Wall Street Journal*, July 8, 2023

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When It Comes to Pricing for Airport Snacks, Is the Sky the Limit?

Use with Chapter 8, "Retail Locations", and Chapter 14, "Retail Pricing"

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You're a careful traveler, so you arrive at the airport with plenty of time and without any prohibited liquids, such that you get through security easily. But then what happens? Faced with several hours of free time, you might settle in at the gate to scan social media or watch a downloaded movie, but at some point, you also might get hungry or a little bored. And then what? As various memes imply, the rules go out the window when it comes to snacking and consuming in the airport. If the only food outlet open is a hamburger joint, people will scarf down a cheeseburger for breakfast. They will start drinking alcohol well before they would ever do on a regular weekday, and they will indulge in cinnamon buns or donuts that are strictly forbidden in their normal healthy diets.

Such choices likely reflect the unique consumption context that an airport implies. Especially for leisure travelers, arriving at the airport seems like the start of vacation, when most people loosen their self-imposed consumption or behavioral rules. They already are willing to make changes to their regular diets and try new things, because their goal is explicitly to take a break and leave behind their day-to-day, regular lives.

But along with these unconventional and experimental consumption choices, travelers also appear willing to pay far more, even for the same candy bar or magazine, than they would ever expect to pay in their local grocery store. In turn, conveniently located storefronts in terminals can charge much higher prices. A recent, lighthearted (and unscientific) survey of the prices for buying a bag of Chex Mix in different airports revealed just how much higher. Posting on X, a frequent traveler noted that, for the same 8.75-ounce bag, she paid $4.76 at Dallas Fort Worth airport, $5.99 in Indianapolis, and a whopping $9.99 at LaGuardia. Others quickly chimed in too, revealing that Bostonians could grab some Chex Mix at Logan Airport for $5.69, but Chicagoans were out of luck: At both O'Hare and Midway, the snack bag cost more than $12.

Although many fliers might seem willing to pay such prices, some rules are in place to protect these largely captive audiences. Many municipalities subject sellers in public transportation settings to what is referred to as "street pricing plus" standards. That is, they can add a mark-up—which acknowledges that many of these retailers pay substantial fees to be able to operate in the airport—but the increase they impose cannot exceed some set percentage above what a vendor in that area would normally charge. For example, in Los Angeles, the vendors can add an 18 percent upcharge. But in Portland and Salt Lake City, local legislation demands that they charge only the street pricing rate, without any designated "plus" amount.

Of course, even if they have to dump their drinks, travelers could just bring healthy, affordable food items from home. But when the rules no longer apply, and consumers feel free to indulge in ways they would never do in their regular lives, who wants the boring snacks that they have at home?

Discussion Questions

1. Do you indulge more (whether in terms of what you buy or how much you pay) when you travel?
2. What is a reasonable price markup for vendors in an airport? That is, should they be allowed to charge more than the "street price" level?

Sources: Natalie B. Compton, "Chex Mix Has Become the Symbol of Overpriced Airport Snacks," *The Washington Post*, February 7, 2024

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Playing the Global Field to Find a Stable Source of Toys

Use with Chapter 13, “Buying Merchandise”


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Multiple global trends drive manufacturers’ choices about where they want to locate their plants. In recent years, the challenges of COVID-19–related shortages, political tensions, and safety concerns have prompted many firms, in various industries, to seek to move more of their productions outside of their traditional locations in China and explore other international possibilities. These trends appear particularly acute in the toy manufacturing sector.

Major brands such as Hasbro and Mattel are in the process of reducing, minimizing, or eliminating their dependence on Chinese factories to craft the dolls, cars, knickknacks, and so forth that children demand for their playtime. These companies still cite the massive challenges they faced during the pandemic, when families stuck at home sought out more entertainment options, while supply chain constraints left the companies unable to supply that demand. Furthermore, it was not that long ago that Mattel was forced to recall millions of toys, produced in a Chinese factory, that contained lead.

Along with these historical but memorable incidents, the costs of doing business in China continue to rise. The country’s remarkable growth and development have supported rising wages in factories. In addition, if already obvious tensions between China and the United States intensify, it seems likely that new duties will get imposed on toys imported from China.

Unique to toys, the supply chain has distinctive timing constraints. Most companies want manufacturers to produce high volumes for certain times of year and reduce their output at other times. Such fluctuations rarely are profitable, so instead, many of the plants in China produce at relatively consistent levels, then store the toys until U.S. retailers ask for them.

As toy companies look to alternative sites for their production facilities, such as in India, Vietnam, and Thailand, they confront notable challenges. With their relatively underdeveloped infrastructure (compared with China), these other countries cannot hold inventory for months at a time, ensure consistent deliveries, and remain competitively priced. In addition, safety oversight is especially pertinent to toy manufacturers, and in some cases, factories have few such protections in place.

Even with all these motives though, only about 1 percent of all toys imported into the United States or Europe come from India. The need to diversify internationally is clear. The means to do so is less so.

Discussion Questions

1. Why is the demand for moving production beyond China especially acute for the toy industry? What features set it apart from other sectors?
2. If you were starting up a new toy company, where would you consider locating your factories? Provide justification for your answer.

Sources: Richa Naidu, “Toy Manufacturers’ Shift from China Is No Child’s Play,” Reuters, January 15, 2024

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Automated Cart Checks After Checkout: Efficiency in a Different Retail Stage

Use with Chapter 17, “Store Layout, Design, and Visual Merchandising”, and Chapter 18, “Customer Service”

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Efforts to automate store checkout operations continue to increase in variety and prevalence, but thus far, none of them has emerged as dominant. As various retailers continue testing their own (and observing others’) experiments with technology-enabled options for processing what shoppers put in their carts and charging them for those items, automatically and accurately, Sam’s Club has taken a unique perspective on the promise of automated checkout. Rather than relying on artificial intelligence (AI) to scan and ring up customers, maybe it is better suited to perform the subsequent step, that is, checking carts as people leave the store.

As warehouse clubs like Sam’s or Costco, staffers past the registers are a common sight, reviewing people’s cart against their printed receipts to ensure an accurate parallel between them. Some big box retailers like Lowe’s undertake such checks as well, though less consistently. The goal is to protect both consumers and the company, ensuring that shoppers have not been charged for items left behind on the belt while also confirming that they are not taking a “five-finger discount” on anything for which they did not pay.

This check takes substantial time, which irritates customers to a substantial extent. Shoppers generally disparage the need to stand in line twice (once to pay, once to get into the parking lot). In addition, many shoppers allege that the people in charge of the cart checks unfairly target certain customer demographics, such that they are applied more frequently to shoppers of color.

In its attempt to avoid and address both these issues, Sam’s Club wants to install automated, AI-enabled cart check frames at store exits. The structure would rapidly tally up the contents of every shopper’s cart, then compare it against that person’s electronically stored register receipt. Because the check can happen almost instantaneously, people are not slowed down any further, and because it applies to everyone, the dangerous potential for discrimination gets eliminated. The retailer plans to have the devices installed in all of its stores by the end of 2024.

The technology underlying these promising tools is very similar to that which other retailers are attempting to use to make the actual checkout step painless. But its application in this straightforward comparison of what the receipt says a customer bought and what they are leaving the store with is simpler. It thus might be more functional in the short term, with direct benefits for retailers and shoppers. Thus, while consumers continue to wait for technology that enables them to pop into a store and grab whatever they like, with their purchases automatically tallied and charged to the payment option they prefer, at least for now, they can leave warehouse clubs with their hauls without having to spend extra time confirming all they bought.

Discussion Questions

1. Are cart checks necessary? Why or why not?
2. Why are cart checks a pain point for consumers? For retailers? Does automating this step eliminate these pain points completely?

Sources: Sopan Deb, “At Sam’s Club, a Human Will No Longer Check Your Receipt at the Door,” *The New York Times*, January 12, 2024; Dominick Reuter, “Sam’s Club Will Stop Checking Receipts at the Door—And Instead Use AI to Snap Photos of Your Shopping Cart,” *Business Insider*, January 10, 2024; Gili Malinsky and Aine Caine, “Here’s What Costco Workers Are Actually Looking for When They Check Your Receipt at the Exit,” *Business Insider*, August 2, 2022

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Retailing Tidbits

Beyond Football: This Year's Trends in Super Bowl Advertisements

Use with Chapter 15, "Retail Communication Mix"

People who tune into the Super Bowl might be classified into two main groups: sports fanatics who are determined to watch every down, and everyone else, who watches mostly for the commercials (and maybe a Taylor Swift sighting or three). But among this latter, more casual group of viewers, we can also find evidence of true dedication. That is, some 160,000 viewers register in advance of the game, agreeing to rank the commercials during the broadcast, and then *USA Today* publishes the results. The lists offer some interesting insights into current trends. For Super Bowl LVIII, nearly half of the top 10 most popular advertisements leveraged people's nostalgic affection for good buddies: Danny DeVito helped Arnold Schwarzenegger enunciate the final syllable in "neighbor" in State Farm's well-known tagline; Matt Damon complained to Ben Affleck that "Sometimes, it's really hard to be your friend" before participating in a performance by the "Dun'kings" while wearing Dunkin'-branded jumpsuits; Jennifer Aniston (Rachel) forgot who David Schwimmer (Ross) even was, to make room in her brain for recalling what Uber Eats delivers; and the Clydesdales relied on their old Labrador Retriever friend to lead the way for a delivery by Budweiser. As these examples indicate, many of the most popular ads were humorous. But others actively sought an emotional appeal and made ethical claims, including Dove's encouragement of bodily confidence among young girls; Google Pixel's demonstration of how it was working to increase inclusivity among people with limited vision; the NFL's determination to expand access around the globe; or the reminder from the Foundation to Combat Antisemitism that silence allows for hatred to persist, whereas making our voices heard means standing up to hate. In addition to their popularity among the estimated 123.4 million viewers who tuned in, we hope the advertisements were effective in meeting the companies' marketing objectives too, considering that a 30-second slot cost a record-breaking $7 million in 2024.

Sources: "Best 2024 Super Bowl Commercials," *USA Today*, February 13, 2024; Suzanne Vranica, "How Much Does a Super Bowl Ad Cost this Year?" *The Wall Street Journal*, February 13, 2024

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