

Front-End FOCUS

Best Practices For Superior **Checkout** Merchandising

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White Paper



Background

Front-end check stands deliver over \$5.5 billion in retail sales, but significant opportunities still exist. A potential of \$2 billion in incremental sales has been identified in the Front-End Focus research study. The key to realizing those incremental sales is following front-end merchandising best practices.

Front-End merchandising in retail outlets has historically been poorly managed, with limited rationale for the selection of categories and products that end up on the check lane racks. Numerous buyers and category managers are involved in the process, with each of them trying to maximize the space given to their categories. The result has been competition for space based on the perspective and objectives of each buyer, and the categories they represent, not a strategic exercise designed to maximize overall front-end performance based upon the goals of the organization. Decisions are also often based on a very limited set of measures, such as the amount of money paid for space, and key measures such as sales volume, turns and gross margin may receive only secondary consideration.

If front-end performance is to be optimized, a more disciplined merchandising approach must be put in place.

Recommendation for Managing the Front-End

The Front-End Focus study identified the following key strategies for managing the front-end:

- Recognize the value of the front-end to store sales and profits
- Focus on the power categories that drive front-end sales and profits
- Base decisions of total profits from sales revenue and placement fees
- Take advantage of the growth opportunity by adopting the Best Practices of top performing retailers
- Manage the front-end as a department with a dedicated manager

As a result, it is recommended that one individual, the Front-End Director, should have control of front-end merchandising decisions. The Front-End Director should have an objective of maximizing overall front-end performance, have responsibility for all front-end selection and merchandising decisions, and not have any vested interest in the performance of individual categories, manufacturers or items. The Front-End Director would determine what categories and items will be merchandised on the front-end, and will allocate space on the check stand racks to those various categories. He or she would be in charge of rack configuration and any promotional merchandising on the front-end, including temporary displays, such as clip strips and dump bins. The Front-End Director will also be accountable for the financial results of the front-end.

While the concept of placing one individual in charge of the front-end is often accepted, there have been challenges in execution, including:

1. **Data Availability** - Data has historically not been available to split sales for items that are merchandised on the front-end and additional in-line locations, such as batteries, film and selected magazine titles. This data is required to develop a financial scorecard for the Front-End Director.

As a practical matter, dual location items represent a fairly small percentage of total front-end sales, and there are a number of workable solutions to this data issue, including:

- Carry only unique items on the front-end – This approach eliminates all data issues, and has been put in place by a number of retailers. Important items, such as batteries, can utilize different pack sizes at the front-end (6 pack AA in-line, 8 pack AA at the front-end), or have unique UPCs. While this approach may add incremental items to the retailer's overall UPC count, the number of additional items is not significant.
 - Conduct periodic audits to determine the percentage of dual location items that are sold from the Front-end location – The percentage used could be based on industry averages or on retailer specific data. Retailer specific data would obviously be more accurate, and preferable, but will require additional effort on the part of the account. If industry averages are used, minimally the data should be from the same class of trade (food, mass, etc.), and ideally from the same geographic region. **An example of front-end sales percentages from the Front-End Focus Study can be found in the Appendix.** The data should also be adjusted on a period or quarterly basis to account for any seasonal impacts on sales patterns. While this approach will not be as accurate as carrying only unique items, it will provide very good “directional” data on the performance of dual location items. Again, since dual location items represent a relatively small portion of total front-end sales, the overall front-end data will be very accurate.
2. **Split Category Responsibility** – Categories that are carried at the front-end are virtually always merchandised elsewhere in the store. This creates the concern of how to divide responsibility between the "in-line" category managers and the Front-End Director. We recommend the following approach to minimize this issue:
- There are two categories, batteries and film/photo-finishing, where a significant portion of total category sales occurs at the front-end, and the total number of SKUs in the category is limited. In addition, in the film/photo-finishing category, the “other” location is often an end cap near the front of the store or the front-end lobby area. Having everyday category responsibility could also help fill out the Front-End Directors workload during periods of limited front-end activity. For these reasons, we recommend that the Front-End Director have total responsibility for these categories.
 - In the balance of traditional front-end categories, there is a relatively clear distinction between items sold on the front-end and the items sold in line. For instance, in confection, typically singles (and possibly limited king size items) are carried at the front-end, and the balance of the category is in-line. Exceptions would be beverage and blades, where there are dual-location items, but it would not be practical to give the Front-End Director complete responsibility. The beverage category is too large, requiring virtually a full time category manager, and blades are typically combined with other HBC categories, such as shaving and skin care. **The exception for Beverages may be that the Front-End Manager has responsibility for the unique 20 oz. Water and Carbonated Beverages that are commonly stocked in coolers at the front-end checkouts.**

As a result, for these remaining categories, responsibility should be split between the Front-End Director and the in-line category manager. Data issues are resolved by adding an identifier to the scan database for all items that are carried on the front-end, allowing them to be separated from the balance of the category and combined with other front-end items for reporting and scorecarding.

There will be a need for coordination between the Front-End Director and the category managers in areas such as itemization and promotion planning. Manufacturers will work with both, and will be required to have joint or multiple appointments for the same category. A new item targeted at the front-end would have to be presented to both, and the decision coordinated between the manufacturer, the Front-End Director and the Category Manager. Manufacturers will also need to divide promotional funding between non-front-end items and those on the front-end. Although this approach does add complexity to the process, the benefits gained by having one individual in charge of all front-end activities outweigh any drawbacks.

The Front-End Director Job Responsibilities

The rationale for having one individual in charge of the front-end is driven by the need to improve overall front-end performance, and have one individual accountable for front-end results. To accomplish this, the Front-End Director will have “general manager” responsibility for all decisions at the front-end. The key levers for improved performance are itemization, merchandising, space allocation between categories, promotion, display and in-store conditions. **The Front-End Manager will need to work closely with other category managers to get their input regarding items merchandised on front-end checkouts.**

Merchandising - The Front-End Director will be directly responsible for determining the items that will be carried on the front-end, allocating space to front-end categories and developing front-end schematics. Included in this responsibility will be negotiating placement allowances with all manufacturers. The Front-End Director will be responsible for rack design and quality, and negotiating cost and terms with rack manufacturers. He or she will also be responsible for determining the placement and number of alternative front-end racks, such as beverage coolers.

Promotion - The Front-End Director will control merchandising of temporary front-end displays, such as battery clipstrips and candy dump-bins. Category managers who wish to display products at the front-end must present their programs to the Front-End Director, who must approve all temporary displays.

In Store Conditions - While improvement in store conditions is not directly under the control of the Front-End Director, he or she can significantly influence results. The keys to improvement are optimizing manufacturer and broker retail coverage plans and educating the operations side of the retail organization on the sales and profit contribution of the front-end, and the importance of maintaining in-stock conditions. As a result, the Front-End Director will be responsible for influencing the structure and call frequency of third-party coverage plans, and regularly meeting with the appropriate parties to evaluate results. The Front-End Director will also be responsible for communicating the importance of maintaining front-end schematics and in stock conditions to the operations group in their own organization, and for developing programs with operations to improve front-end conditions.

Store Openings and Remodels - The Front-End Director will be responsible for the merchandising of the front-end at all new store openings and remodels. This will include determining the types of front-end racks that will be in each store, and the number of alternative racks, such as beverage coolers, that will be placed in each store. The Front-End Director will also be responsible for determining the type of racks and merchandising that will be executed on self-scanning lanes. The Front-End Director must approve all changes to the front-end racks and merchandising.

The Front-End Merchandising Process

The initial step in the process is to determine the role and strategy for the front-end in the retail organization, such as profit or revenue maximization. Based upon that strategy, key criteria for decision making are developed.

The Front-End Director will then use the criteria to begin making decisions on what categories will be carried on the front-end. In addition to the categories controlled by the Front-End Director, this will include working with the relevant category managers who would like to have items from their categories carried on the front-end.

The decision to carry categories and items on the front-end should include a financial analysis with *all* key factors considered. Consideration of all relevant factors is critical, and decisions must not be based on just the significant space payments that are attached to front-end placement. In the past, very poor decisions have been made by failing to consider all of the facts, such as sales volume and profitability, in addition to space payments. Factors to be analyzed should include

- Sales volume
- Gross margin
- Turns
- GMROI
- Placement allowances
- Consumer wants and needs

The result should be a space-based projection of performance, showing projections for each square foot or linear foot of space requested, from each category. Each category should be evaluated using the same template and approach, allowing an “apples to apples” comparison of the projected contribution of each category to be made.

To make the best possible decisions, it is important to go beyond the internal numbers, since such an analysis, while important, will only give a perspective on what has happened in the past at that particular account. To understand what is happening elsewhere in the industry, and gain an outside perspective on potential merchandising “best practices”, it is important to look outside of the retail organization. Numerous groups can bring this outside perspective. Manufacturers, distributors, brokers and magazine publishers who have products they would like placed on the front-end locations will be very interested in the process, and their input should be considered when making front-end merchandising decisions.

In addition, a selected magazine publisher has traditionally played the added role of “quarterback” for front-end merchandising efforts, and provided valuable assistance, both in terms of labor and expertise, to retailers. There are additional groups such as rack manufacturers, possibly a RDA consultant, and others, who will want to be involved in the merchandising decisions. Their reasons will be varied, some self-serving and some not, and they may be able to offer a valuable outside perspective.

Research initiatives that evaluate overall front-end performance, such as the Front-End Focus study, can be a valuable source of objective information regarding industry best practices and guide final decisions on space allocation, frequency of location and merchandising layout. The bottom line is that the Front-End Director must take in all available input, apply the objective criteria outlined above, and make the space allocation and rack design decisions that will give the organization the best chance of achieving its strategic objectives.

Based upon the analyses presented and any additional input required, the Front-End Director allocates space on the front-end racks, including determining if categories will be carried on all check stands, alternate check stands, etc. Following the allocation of space, the Front-End Director makes the final decisions on what items to carry on the front-end, with input from the in-line category managers as needed. They are the category experts, and will have valuable input on how to maximize results within the given space.

Major merchandising changes will occur with the re-racking of the front-end, which typically occurs every three to five years. During the re-racking process, the Front-End Director will have the additional tasks of finalizing the design of the racks and selecting a rack manufacturer. Rack installation can then be scheduled, and the installation process supervised.

Once the racks are installed, it is difficult to make significant changes to the space allocation between categories in the interim years. There should be an annual update of the itemization within categories, and minor re-allocation of space as needed and rack design allows. Quarterly updates can be made as needed to accommodate significant new item introductions.

Measuring Results and the Front-End Director Scorecard

As discussed above, there will be data considerations for items in dual locations. Once an approach to eliminating these data concerns has been selected, it is possible to use traditional performance measures to evaluate the Front-End Director's performance. Measures should include:

- Dollar sales
- Unit sales
- Gross margin %
- Gross margin dollars
- Promotional funds

Measures should be evaluated versus prior year and objective. Reporting should be available at the item, segment, category and total front-end levels. A scorecard mock-up is included separately.

Two measures that are not included in the mock-up are turns and GMROI. Both are important, and would be included if data were available, but it is not possible to capture the store level inventory data to calculate results on an ongoing basis. That does not mean turns and inventory productivity should be ignored, however. Inventory turns should be addressed during the rack design process, where the Front-End Director will make trade-offs between holding power, turns and potential out-of-stocks. The frequency of deliveries and retail coverage patterns should also be planned to allow maximum turns without creating out-of-stocks.

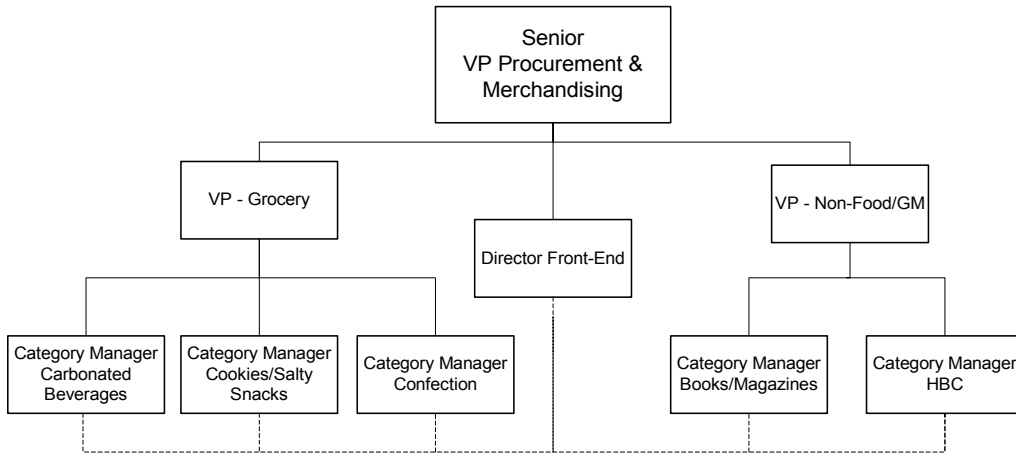
If unique UPCs are not carried on the front-end checkstands, the sell-down method identified under the Data Availability section on pages one and two needs to be completed at least once every couple of years to understand what percentage of sales are coming from the front-end checkstands. This would only apply for items that are carried on the front-end checkstands and that have duplicate distribution around the store.

In addition, there are unique aspects to properly managing the front-end that, while not quantifiable, should also be considered qualitatively when evaluating performance, including:

- Matching front-end merchandising to the strategic goals of the organization
- Effectiveness and efficiency of the re-racking process
- Balancing the often conflicting goals of maximizing front-end sales and maximizing space payments

Organization Structure

The Front-End Director will have responsibility for all front-end related procurement and merchandising activities, and will be required to work with a number of category managers in the course of these duties. While the Front-End Director will not have direct authority over the category managers whose product categories are included on the front-end, they will have final authority and final decision power for all front-end related decisions. With that in mind, a dotted line reporting relationship would make sense.



The actual organization structure put in place for the front-end merchandising process will depend on the existing organization and the overall roles and responsibilities of individuals involved in the process. What is most important, however, is that there is clearly one person with authority to make final decisions for all front-end related activities.

Summary

Research has clearly shown that there is an opportunity to improve front-end sales and profits through improved merchandising. Identification of this opportunity has led to the realization that is necessary to give one individual responsibility for front-end decision making. The critical activities are:

1. Selecting the categories that are merchandised on the front-end
2. Determining how space is allocated between categories
3. Determining how to present the front-end merchandise to consumers
4. Determining the types of racks to be placed in all stores
5. Planning and controlling all front-end promotional activity
6. Working with operations and third-party service providers to ensure there is adequate retail coverage to maintain front-end merchandising at the desired level

A number of approaches have been suggested, including designating one category manager to run the front-end. However, due to the importance of the front-end, the recommendation is to elevate and expand the authority of the position, and give responsibility for the all front-end decisions to a Front-End Director of Procurement and Merchandising.

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Appendix

Sell-Down Ratios

Purpose: For items that are carried on the front-end checkouts and also in other locations in the store, a sell down must be conducted to understand what percentage of the item’s total strong sales are generated from the front-end registers, versus other locations in a store.

Methodology: For items that are carried on the front-end checkout and are also stocked in other locations, an initial inventory is taken by item, by location, and for the front-end checkstands, by lane. A few days later, a secondary inventory is taken by item, by location, and for the front-end checkstands, by lane. The difference between the second inventory and the first are product sales. Divide the sales of the items from the front-end checkouts, by the total sales of the item across all stocking locations to identify the ratio of sales coming from the front-end. Apply that ratio to the all-store sales data for these items to track trends of only front-end sales. The ratio should not change frequently so audits could be conducted every year, or once every two years.

Percentage of Sales from Front-End Checkouts*

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|---------------|-----|
| Batteries | 67% |
| Lip Care | 83% |
| Oral Care | 74% |
| Photo | 50% |
| Razors/Blades | 60% |

*Percentage of only those items carried on the front-end checkstands and not the entire category, as identified from the Front-End Focus Study