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The retail evolution's great acceleration

How to maneuver in the pandemic-driven recession

The path forward for many retailers requires building trust and embracing emerging trends exposed by COVID-19.



If we've learned anything from previous recessions, it's that they expose existing weaknesses, accelerate emerging trends, and force organizations to make structural changes faster than they had planned. This is particularly true in retail. During the great recession of 2008–2009, e-commerce grew, and brick-and-mortar retail declined; as the economic recovery took hold, that trend continued while off-price and discount players and some other new entrants succeeded by appealing to new consumer demands.¹

We expect a similar pattern to follow—albeit with new trends shaped by a pandemic-driven global recession. Of course, certain truths remain: Retailers struggling before COVID-19 will likely see their declines accelerate. Income disparities will drive continuing business toward off-brand and discount retailers, and online shopping will continue to accelerate.

But we also see several other potential trends shaping the post-COVID-19 retail environment:

- Product mix will likely change, and retailers will need to forge new partnerships to thrive.
- Consumer-retailer interactions will be defined by health and safety expectations.
- Demands for convenience will drive even more contactless transactions.
- Retailers will depend meaningfully on the trust they have with consumers and other stakeholders.

What is clear: Retail orthodoxies will be challenged, and the industry will likely look much different than when we entered this crisis. For now, the picture may appear bleak. But retailers who grasp the challenge and join the gathering trends could well emerge stronger and provide a brighter future for employees, customers, and stakeholders alike.

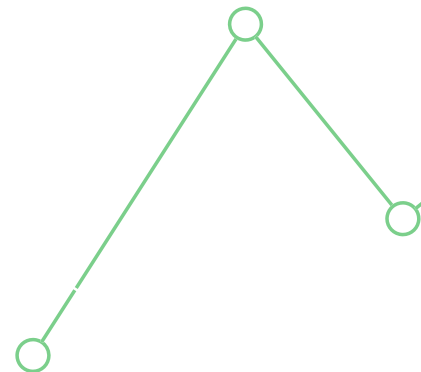
The 2020 COVID-19 recession

To best understand the impact of the current recession on retail, consider this: It's very different than nearly all recessions that have come before it. The United States has experienced 22 business cycles since the beginning of the 20th century.² All but three found their origins in financial markets.³ The "typical" business cycle has involved the overexpansion of credit, underpricing of risk, and eventual bursting of financial market bubbles.

By contrast, the COVID-19 recession was triggered by a sudden shutdown of consumer activity. People simply stopped eating out, traveling, and leaving the home. Roughly 30 million workers were furloughed or laid off as demand shut off and factories and offices were idled to prevent the spread of the virus.⁴ Some sectors, such as health care—which had proven virtually immune to recessions in the past—have shrunk as people have canceled doctor's appointments and suspended plans for elective medical care.

Even consumers with jobs have stopped spending. Retail sales plunged 20% from February to April, with very large declines in categories like clothing and accessory stores (down 89%), and Department stores (down 45%). The personal saving rate jumped to 33% in March from 8.0% in February. That's likely the result of households with employed members cutting back on spending because there wasn't anything to spend money on, and because many households had good reason to wish to increase their savings in an uncertain time—rising saving rates are typical at the beginning of recessions.⁶

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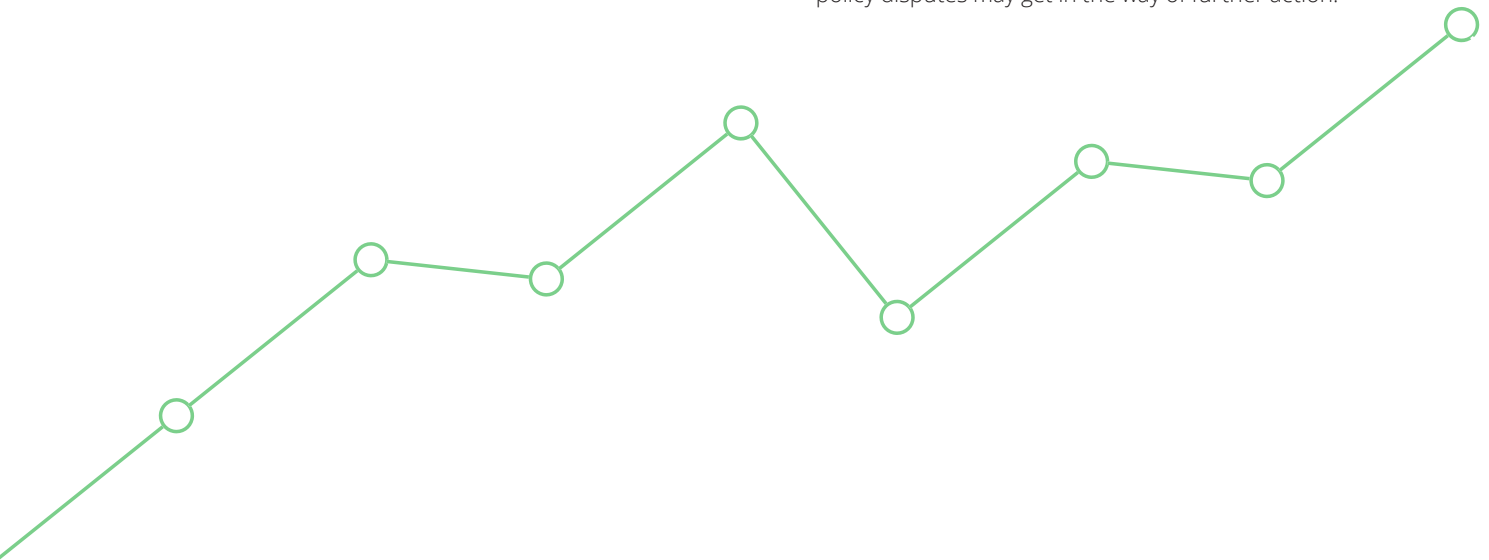
A different type of recovery

Given the pandemic-driven nature of this recession, it stands to reason that an economic recovery will probably look very different than ones we are used to seeing.

First, public health and personal safety will determine when people return to their routines and to work. Important leading economic indicators are public health metrics: How many people are contracting the virus, how many are dying from it, and are we seeing stress in our hospitals and medical centers from the virus's impact? As these metrics decline, we can expect the public to become more confident in venturing out.

Second, although government-required shutdowns led to the declines in economic activity, government action cannot easily "restart" the economy. In the end, that will likely be determined by people if they feel safe or until a vaccine for COVID-19 is widely available.

Third, even when the virus is controlled, the economic damage will persist. Employment typically takes a long time to return to prerecession levels, and so demand will remain depressed. The policies that normally help spur demand and employment gains—either loose monetary policy or fiscal stimulus packages—have already been used aggressively. Politics and policy disputes may get in the way of further action.



Retail's challenged position

Even before the COVID-19 crisis began, our [The next consumer recession report](#) found that retail was facing several financial issues that could make it difficult to weather a recession.⁷ Many retailers faced challenges already: Increasing debt burdens, moderating revenue growth, compressing margins, increasing SG&A, and slowing asset turnover. Not surprisingly, we are starting to see these issues force several retailers to file for bankruptcy in recent weeks.⁸ But across retail, we are seeing significant weaknesses in the foundation: The technology and process architecture of retailers, often vulnerable to sudden shocks, are now completely exposed. Even many retailers that had been making incremental moves toward transformation have not been able to cope with the halt in store traffic, demand on digital, and shocks to the supply chain.

No matter the retailer, one cannot overstate the damage done when stores are closed for months at a time. Each regular customer represents a relationship that took years to develop and nurture; losing that continuity is a risk to any retailer's position in the marketplace. The same is true with other stakeholders. Long-time employees, for example, have mastered what it takes to represent the brand over several years. Retailers are now having to create workforce flexibility, tools for secure collaboration, and positioning around furloughs, all while sustaining morale and keeping employees healthy. Even retailers who are faring well in the pandemic should take account of the damage done up and down their value chain and begin to develop strategies to restore what has been lost. What took years and even decades to build was severely damaged, if not destroyed, in a matter of weeks.⁹

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Acceleration of trends

During the first months of the COVID-19 crisis, there has been an acceleration of digital retail: Those retailers with strong platforms and sophisticated data analysis have succeeded in connecting with consumers and offering them additional services and value. Consumers are willing to embrace and explore new digital experiences due to public health concerns—telemedicine, online learning, virtual payments, and online grocery ordering and delivery. As the convenience of these experiences increases, we expect these trends to accelerate.

Before COVID-19, the convenience trend was being rewritten by players outside of the industry, putting pressure on the retail industry to adjust to reshaping consumer expectations. As the crisis hit, retailers have had to rapidly roll out conveniences such as buy online, pick up in-store (BOPIS), curbside pickup, and delivery. Those that have the systems in place to offer these conveniences have done comparatively better than others. Our Global State of the Consumer Tracker found from mid-April to mid-May that across age groups, the No. 1 reason customers chose BOPIS is because it is safer, followed by convenience.¹⁰

However, for seniors, the second reason they were seeking out BOPIS was to support local stores and workers—an indication that perhaps the disruption that consumers have experienced is reprioritizing values. This could lead to an acceleration of new models of retail where health and sustainability become larger drivers. For example, as populations are experiencing cleaner air because of stay-at-home orders, will they be more interested in conscience consumption? As of mid-May, 39 percent of consumers said they plan on buying more locally sourced items, even if it costs more—a trend that increased since mid-April.¹¹

We also expect discounters to continue to benefit from ongoing trends. With the unemployment rate moving up rapidly (it stood at 14 percent in April) and one-third of those currently employed concerned about losing their job, many consumers are going to look to cut back and save wherever possible. These retailers may stand to pick up customers, similar to what we saw coming out of the Great Recession.¹²

What's next?

As retailers try to understand how to benefit from these accelerating trends while grappling with this crisis, let's take stock of how certain retail orthodoxies have been turned on their heads:

- Direct interaction with shoppers, once the foundation of customer service, has been replaced by virtual or contactless touchpoints.
- Returns processing—likely to increase amid more online sales—will require new safety standards to meet customer expectations.
- Stores have turned into mini-fulfillment centers and pickup points.
- Supply chains are being restructured to fulfill specific orders to households rather than to large-format stores.

All of this calls for structural change in the industry. By challenging traditional orthodoxies, retailers can redefine the basic assumptions of the industry—how to build trust with stakeholders, how to operate stores in new ways, and how to structure their entire operations around new consumer expectations. In short, they can thrive in the new normal of retail.

Establish trust

[Establishing trust](#) with employees and consumers is paramount. Without trust, it can be difficult for retailers to implement effective business strategies and move forward.¹³ And stakeholders will likely focus on two areas of trust in particular: physical health and digital privacy.

Roughly half of US consumers are concerned for their physical well-being, and 42 percent feel safe going to the store as of mid-May.¹⁴ Companies have been severely criticized for not taking enough care with public health considerations while operating.¹⁵ Failing to pay attention to consumer and employee health concerns and expectations for safety will likely do long-term damage to a retailer's brand.

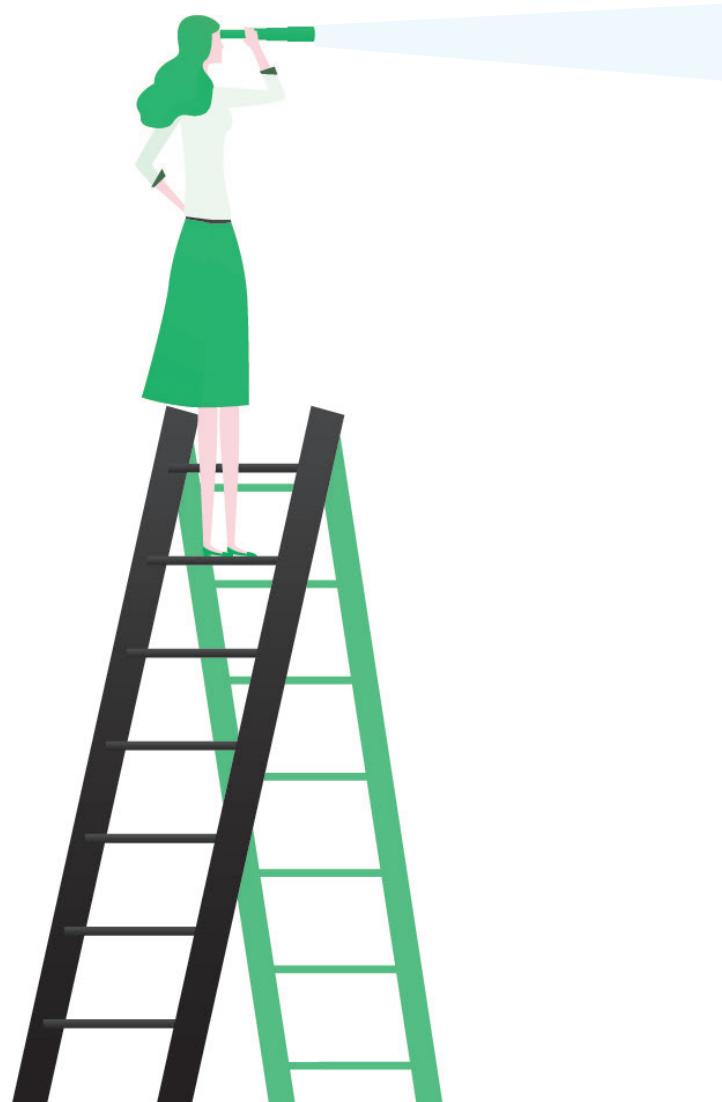
Similarly, data privacy is a basic expectation of many consumers. As of mid-May, 43 percent say they are more concerned about data privacy as they are shopping online more.¹⁶ And employees are growing more alert to data privacy, especially as retailers will be taking their body temperatures before shifts. This is uncharted territory for retailers, and they should be proactively communicating to employees how the data is being protected and used.

Trust should contribute to brand value either way. Younger shoppers are more likely to hold retailers accountable for their response to COVID-19, with 54 percent saying at the beginning of May they will purchase more from brands that responded well to the crisis.¹⁷ This is likely to be the defining moment for an entire generation. By building trust through the responsible protection of public health and data now, retailers can gain loyalty and be rewarded long after the pandemic is over.

Reassess the role of the store

It may be time for retailers to challenge the old orthodoxies that define the physical, brick-and-mortar store as the center of a retailer's identity. As safety concerns shift more retail sales online, it may be time to assess which stores should reopen at all. For those that do open, historical data might not be a valuable guide to set expectations for store performance in the near term. Better to use real-time data to understand where people are shopping, how far they are willing to travel from home, and what they are buying. These will likely drive decisions about which stores to reopen and what role each store should play in the portfolio.

It's critical to recognize that [reopening a store](#) location may involve additional costs, such as equipment to keep the store clean and safe for the public and employees alike, to name just one. Contactless commerce carries with it unique costs; fulfillment is different and can be challenging. Then there is the risk of future store closings in case of flare-ups of COVID-19. As governments closed various industries to stem the pandemic, it became apparent that some retailers were better positioned than others solely because their product assortment allowed them to earn status as an essential business. As retailers plan for a new future, it's important to consider what was learned from this round of restrictions. Are there categories or products that could be added so that if future outbreaks occur, a retailer could be deemed an essential business?



Explore new models of operating

As consumers abandon shopping habits and cope with new public health worries and fresh financial woes, they may well embrace fresh retail formats and other innovations. Retailers have the opportunity to imagine or seek out new partnerships and new retail categories—including product and service categories that consumers didn't know they needed. To seize this opportunity, it's time to rethink partners, suppliers, and alliances and examine ways to serve low-end customers while exploring new markets.

Some ideas may emerge from retail models that had been abandoned: Will drive-in movie theaters prosper again? Could a version of the milkman resurface as consumers seek out ways to support their local economy while wanting to stay safe? By investigating new models of operation or mining old models for inspiration, retailers can position themselves for success.

In the end, retailers will likely succeed only as far as their multiple stakeholders feel secure: Physically, is their health secure in stores? Online, is their data kept private? These questions fundamentally revolve around the trust that retailers are able to build and nurture. If they are successful in achieving that trust, the path of recovery will likely open. With major trends accelerating, retailers have an opportunity to create a resilient architecture and a mandate to thrive in a new way.

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Endnotes

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