2024 US retail industry outlook: Looking for loyalty in all the right places

Rekindling profitable loyalty through experiences, personalization, and trust

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Introduction

The last two years have been anything but ordinary. Consumers witnessed a 40-year inflationary high in June 2022 and 11 Federal Reserve rate hikes by July 2023. Given this volatility, it's reasonable to assume that consumers' collective psyche would be bruised and they would retreat from the marketplace.

However, consumers have endured, surprising analysts by challenging conventional wisdom. In fact, consumers continue their consumption binge, with some benefiting from wage increases while others are presumably burning through savings and accumulating debt even as economic uncertainty continues to loom. Will 2024 finally signal the end of this spending spree?

Expert opinions vary. Economists are encouraged that moderating inflation and a tight job market will support current consumption rates, though those rates may slow down (see below for more about our economic forecast). But retailers and Wall Street analysts remain uncertain that debt-loaded consumers facing a cost-of-living squeeze can maintain their recent spending trends, especially on discretionary goods.[1] One thing is certain: Inflation has left its mark. Despite inflation approaching the Federal Reserve's target rate of 2% in the last six months, three in four consumers remain concerned about rising prices.[2] With this inflation mentality locked in, consumer behavior has been confounding—even for seasoned retailers[3]—as consumers consider trade-offs, try out the competition, and hunt for the best deals.

As retailers face an uncertain 2024 economic outlook, focusing on trust could lead to profitable loyalty.

US Economic Forecast[i]

A note from Deloitte US Economists Danny Bachman and Akrur Barua:

The US economy seems to have avoided a recession even as inflation has dropped. This is good news, especially at a time when geopolitical tensions are rising, growth in key US economic partners is slowing, and there is uncertainty over budget funding.

Consumers have benefitted from rising wages due to a strong labor market and declining inflation. They have also drawn down their pandemic-era savings to fund more purchases. This dip in personal savings, however, will weigh on consumer spending in 2024–2025. In addition, consumers face headwinds from high rents, rising house prices, and repayment of student loan debt.

Two key trends will shape the future business environment: tighter labor markets and higher long-term interest rates. First, slow labor force growth and continued high demand require companies to offer higher wages to lower-skilled workers and to be more imaginative about hiring.

Second, long-term interest rates are unlikely to return to the lows of the late 2010s. The slowing of China's savings growth, a need for large investments (public or private) to address climate change, and efforts to build supply chain resiliency will likely keep capital demands strong.

Deloitte's baseline forecast anticipates continued growth in consumer spending at a rate slightly below GDP growth (figure 1 in the appendix) due to falling inflation, low unemployment, and increasing productivity growth. The aftermath of the pandemic led to a shift in consumer spending patterns, with the dollar value of durable goods increasing 43% vs. a 24% rise in spending on services since Q4 2019. This is unlikely to continue, with the forecast suggesting a slower growth trajectory for durables spending relative to consumption and income over the next five years.

Is there a loyalty crisis?

The pandemic-induced e-commerce surge and supply chain disruption caused a loyalty calamity. Three in four consumers tested new brands and stores as they faced empty shelves.[4] When life began normalizing, retailers focused on enticing customers back to their stores and keeping them in the so-called family. Then inflation hit.

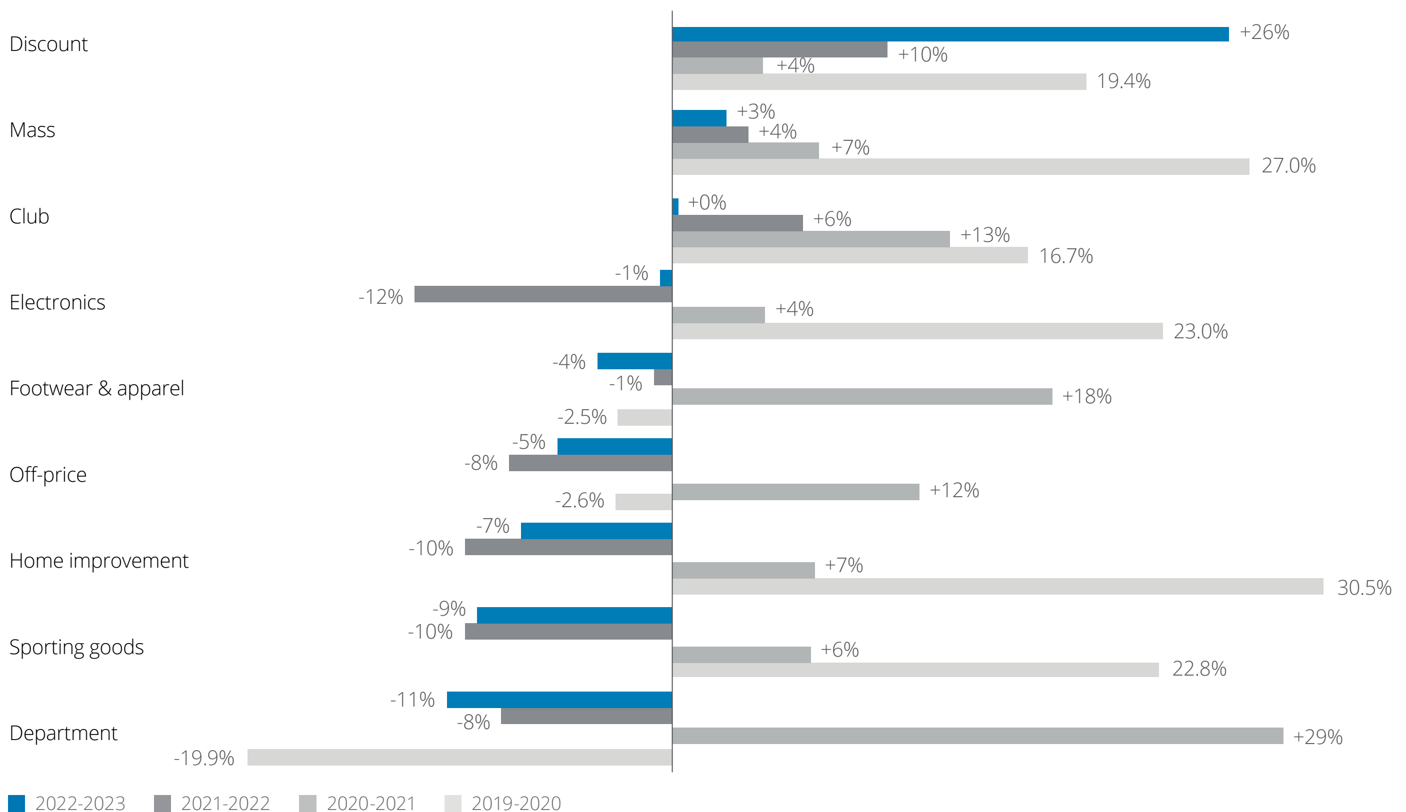
Are you a winner?

Who wins the incremental dollar in a slower growth, inflation-bit consumer environment? The data (figure 1) suggests discount retailers, mass merchants, and club stores are edging out specialty formats.

One-half of retail executives expect consumers to value price over loyalty in 2024.[5] The fact that the new e-commerce discount entrant, Temu, was the most downloaded Apple iPhone® app in the United States in 2023[6] suggests their view is not unfounded.

Two-thirds (64%) of retail executives also expect inflation-weary consumers to purchase fewer goods—something that also concerns consumer packaged goods (CPG) companies as they pivot to ***profitable volume***.[7] Many CPG companies have successfully increased prices in the past few years, but that lever may have run its course.

Figure 1. Consumers spending at discount retailers increased significantly year-over-year



YoY % growth by Retail Subsector, October–November 2019–2023

Source: Affinity Solutions, Inc. – Deloitte InSightIQ Analysis, October–November 2021–2023; inclusive of inflationary impacts.

What drives loyalty?

As consumers focus on price, what is behind a fair price? There is a positive relationship between brands that consumers rated as having the most reasonable prices and trust. For example, the top four auto brands rated for pricing fairness scored 1.4 times higher on trust than the industry average.[8] Trusted companies financially outperform their peers by up to four times, and customers who trust a brand are 88% more likely to buy again.[9] As trust improves, customers are 1.9 times more likely to defend a brand against criticism.[10] In short, trust drives greater loyalty.

Who cares about loyalty?

In our exploration of outperforming retailers, we see a focus on rekindling loyalty.

We analyzed the return on assets (ROA) and debt-to-EBITDA ratio during FY2020-22 for the top 39 US-based retailers (see appendix tables 1–3 for more details on our financial analysis).[11] Over these turbulent years, the outperformers we identified grew profitably, ensured healthy debt levels, and prioritized loyalty.

Outperformers bested their industry peers in revenue growth, margins, and return on invested capital. Our analysis suggests they were more efficient at asset utilization and capital allocation. They also effectively reprioritized investments based on new opportunities and threats. And several leaned into optimizing their operations through modernized technologies.

Outperformers also mentioned *loyalty* and associated elements like *trust*, *engagement, retention, net promoter score,* and *lifetime value* 1.25 times more frequently in earnings calls than their underperforming peers from January 2020 to December 2022.[12]

Eight in 10 retail executives from outperforming companies said their customer loyalty was well above the industry average over the past three years, compared to five in 10 underperforming companies.[13]

Our analysis also indicates that customer loyalty is an important differentiator for outperformers. Most (65%) retail executives from outperformers expect revenue growth of 5% or more in 2024, while 71% of executives from underperformers expect 1% to 4% growth.[14] Looking ahead, analysts expect these outperformers to be approximately 2.6 times more profitable than their retail peers over the next two years (see appendix table 2).

While outperformers do many things right, profitable loyalty is a key focus.

Rekindling profitable loyalty in 2024 and beyond

With bargain-hunting consumers skipping from source to source and customer acquisition costs increasing 222% in the past decade,[15] loyalty programs remain a hot topic. And with the opportunity to utilize first-person data from loyalty programs to create additional revenue, it's no wonder retail executives' most cited growth opportunity for 2024 was strengthening loyalty programs.[16]

Based on what we are hearing and seeing, 2024 will be the year to rewrite the loyalty playbook by putting trust at the center. We see three key opportunities:

- Lean into loyalty programs
- Enhance omni-experience through in-store investments
- Drive individual engagement at scale with trustworthy AI

Opportunity No. 1: Lean into loyalty programs

In the competitive landscape for consumers' incremental dollars, retailers face competition not only from other retail formats but also from leisure travel as consumers continue to prioritize experiences. Additionally, households replenishing their savings accounts poses another challenge, emphasizing the opportunity for retailers to strategically craft loyalty programs to build trust and stand out in the current market dynamics.

On average, nearly two-thirds of US consumers belong to between one and five loyalty programs.[17] However, most consumers use 50% or less of their memberships,[18] so the challenge for retailers is developing engaging programs that convert members into users, and in turn, create profitable loyalty. A recent study found that customers who belonged to a retail brand's loyalty program reported an average of 61% higher trust in that brand than non-loyalty program members,[19] while a consumer industry case study found that increasing trust with existing loyalty program members could potentially boost annual spending by 30%.[20] These gains were primarily attributed to deploying personalized experiences at scale.[21]

Some retailers have homed in on this opportunity. Dillard's outperformed many other department store chains in FY2020–22 by driving customer loyalty through effective merchandising with a strong portfolio of owned private-label and exclusive brands,[22] personalized in-store customer service, and high employee engagement.[23] Ulta Beauty grew its active loyalty program members from 30.7 million in FY2020 to 40.2 million in FY2022, deriving more than 94% of its annual sales from these members in both years.[24] As the company considers its loyalty program a key driver of success, it launched a revamped program in January 2024 with additional perks and a more personalized birthday benefit.[25]

For 2024, we believe that retailers have an opportunity to attain profitable loyalty through personalization, co-branding, and data monetization:

Status tiering: Tiering by customer loyalty allows retailers to offer additional perks to their top tier in a more financially viable manner. Many retailers do this publicly, and consumers understand the benefits of their status. Consumers are also seeking tiered programs, with 62% saying tiered programs are important features.[26] While tiering programs are not new, we see more investments occurring behind the scenes that take a more scientific approach to segmenting. This includes providing different offers, benefits, and communication to higher tiers and working toward migrating people up. This strategy has been a success for one retailer that saw a 98% year-over-year retention rate from its top-tier loyalty members.[27] Seven-in-10 outperformers say consumers' expectations from free loyalty programs will increase (versus four-in-10 underperformers), indicating that tiering may be a way to reward the most loyal consumers.[28]

Co-branding benefits: Retailers should consider looking for a portfolio of benefits so that the retailer (or the brand) is not necessarily responsible for all the benefits provided. For example, since 2021, Target has offered benefits linked to partnerships with their store-within-a-store formats from Ulta and Apple. These partnerships allow loyalty members to earn "Ulta Beauty Rewards" as well as "Target Circle" benefits when they purchase Ulta Beauty items at Target (once they link their loyalty accounts). Target also offers its members free trials on various Apple services (e.g., Apple TV+®, Apple Music®, iCloud+℠, etc.).[29] Similarly, loyalty members can earn "Sephora Beauty Insider" points as well as "Kohl's Rewards" for Sephora purchases made at their store-within-a-store format at Kohl's.[30] The key for consumers is flexibility: Six in 10 consumers believe earning and redeeming points with both partners is important.[31] Retailers should also consider potential benefits from joint promotions with travel loyalty programs involving airlines, hotels, or restaurants. A recent poll indicated that over a quarter of people planning to buy apparel were preparing for a trip.[32] By co-branding the benefits, retailers can get greater exposure and plug into a broader set of consumers while providing exciting benefits with shared costs, potentially improving the program's profitability.

Monetizing data: Some 58% of retail executives said they're making moderate-to-major investments in building or expanding additional revenue streams.[33] With the introduction of Apple's iOS™ 14.5 in 2021, the majority of users opted out of app tracking,[34] opening opportunities for brands to step in where third-party data had once dominated through retail media networks (RMNs: digital advertising platforms owned by retailers that brands can leverage to reach consumers through the assets of the retailers).[35] These can be extremely valuable, particularly when a retailer has the scale of consumer and shopper information in terms of digital and in-store visits, and they have the extra fidelity of many of those customers being part of a retailer's loyalty program. Nearly two-thirds of retailers share or plan to share loyalty data with RMN advertisers.[36] These advertisers value the audiences that retailers can provide, especially when they include details about loyal segments and can demonstrate there is a direct correlation between loyalty and propensity toward a particular brand or behavior. For example, Walmart Connect ("a closed-loop system that integrates online and in-store behavior to build a comprehensive picture of Walmart customers") growing their Q4 FY2023 advertising revenue by 41% year-over-year.[37]

Opportunity No. 2: Enhance omni-experience through in-store investments

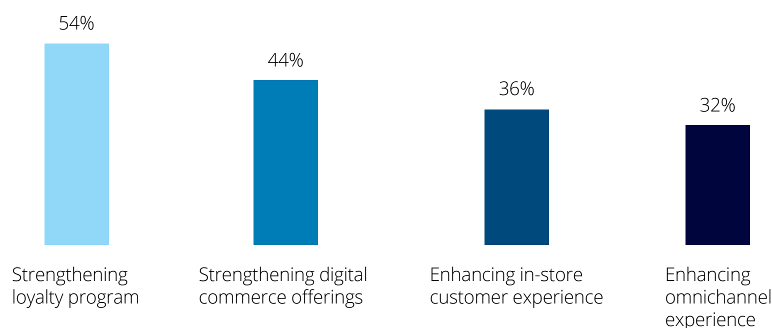
The digital acceleration from the pandemic was a boon for online and omnichannel shopping. Tech upgrades helped with some of the shortfalls of the online experience, from fit to envisioning products in homes. Social media and influencers brought products to life in short video content. Digital wallets and new last mile and return options expanded, creating less friction for consumers to click and collect. Despite these advances (and how tired the topic may feel), a cohesive, consistent omni-experience is often lacking, potentially eroding trust.

Omnichannel inconsistencies and failed execution are potentially detrimental to loyalty. Three in 4 customers say they are more loyal to stores with consistent customer service and experiences.[38] A review of 145 companies' omnichannel capabilities during Cyber Week (November 21–23, 2023) showed while BOPIS (buy online, pick up in-store) and BORIS (buy online, return in-store) were widely available, only one in 10 offered alternative delivery pickup, and a third failed to indicate how long it would take to receive a refund. Shipping was also a sore spot; by December 5, only a third listed shipping cutoff times for Christmas arrival. And when we tested the claims of 17 companies offering on-time delivery of holiday gifts purchased on December 19, nearly one-quarter of the holiday delivery orders arrived after December 24.[39]

When we examined trust in various channels, customers purchasing in-store indicated the lowest trust scores.[40] Interestingly, despite lower trust scores than digital channels, physical channels are the most preferred medium of engagement, indicating a significant opportunity for brands to help boost trust among a considerable fraction of their customer base.

Enhancing the in-store experience was a top-cited growth opportunity for driving growth in 2024 (figure 2).[41] Retailers are facing unprecedented headwinds from labor costs and availability, as well as challenges around shrink (see appendix figure 2 for additional challenges/opportunities). These issues are converging with pricing pressure and high customer expectations, forcing retailers to do more with less—adversely affecting the customer experience. It has created a significant shift in how retailers think about their stores, including how to make associates more productive while creating a more consistent experience for shoppers, how automation can help, and how to reduce shrink.

Figure 2. Top four growth opportunities in 2024 (% of retail executives)[42]



Some retailers are planning expansive store remodels that can immediately create more pleasant environments and sticky behavior from consumers.[43] Target recently noted that sales increase 2% to 4% on average during the year once stores are renovated.[44] But we also see an opportunity in innovative tech that uses data to create efficiencies and consistent experiences, potentially building profitable loyalty (see figure 3).

These tech tools not only elevate the overall shopping experience but also equip retailers with enhanced data, a more nuanced understanding of shopper profiles, and a competitive advantage by offering a personalized and complete omni-experience.

Figure 3. Innovative retail technologies

Opportunity No. 3: Drive individual engagement at scale with trustworthy AI

Retail was built from a supply-focused model to meet the needs of the masses. With consumers wanting more bespoke experiences, retailers are looking for ways to personalize at scale. Deloitte's Future of Consumer work sees this as "a critical transition from mass-market approaches to strategies that prioritize relevance for specific consumer groups. We refer to this shift as an industry moving from mass to micro."[45] Retailers making this shift have an opportunity to delight consumers with product recommendations and tailored interactions, especially if they embed trust at the center of their design.

Driving personalization at scale with AI

Half of retail executives are prioritizing AI-driven personalized product recommendations in 2024. However, only five in 10 retail executives are confident in their company's ability to use AI effectively across their businesses.[46] As retailers gather larger volumes and potentially more sensitive types of data, using this information skillfully is vital to maintain the delicate balance between what data consumers are willing to share and the experiences retailers can offer. Consumers are wary of AI: Eight in 10 consumers from Deloitte's holiday study had little to no trust in retailers' ability to use artificial intelligence responsibly in their operations.[47] Retailers also see this as a challenge, as more than three-quarters said using next-generation AI technologies in the next five years will strain consumer trust and heighten their concerns around privacy violations, surveillance, lack of transparency/accountability, and job displacement.[48]

Introduce and build AI with trust in mind

According to Deloitte research, trust in a brand drops 144% for customers who know a brand is using AI.[49] But data also shows that keeping trust at the center of AI design can create greater adoption from employees and customers and quadruple market value.[50]

The secret to trust is derived from competence and intent. Retailers should reliably deliver on their promises. They should also show enough humanity and transparency to demonstrate their best intentions. To build trust, brands and employers should anchor their design, implementation, and messaging of AI tools on the Four Factors of Trust:[51]

1. **Humanity:** When defining the goals for AI tools for customers, retailers should expand beyond the technical to focus on building human interactions. To construct these human interactions, AI should be trained with an expansive set of rules to be responsive to the context of the customer. For example, if a customer mentions a death in the family, the AI may be trained to build humanity by saying, "I'm sorry; my condolences."

2. **Transparency:** When communicating about AI to customers or employees, messaging should be anchored with precise and tangible use cases. For example, retailers should explain how and why chatbots are being used, providing specific details about their purpose and function.

3. **Capability:** When driving adoption and trust in AI tools for the workforce, retailers should consider bringing the benefits and capabilities to life to demystify the technology. For example, retailers could provide opportunities for employees to try these tools firsthand by offering a "sandbox" to build comfort and familiarity in a zero-risk environment. Additionally, they could highlight the benefits in a human way, focusing messaging on the positive impact of the tools for each employee while underscoring that the tools do not undermine their work and value.

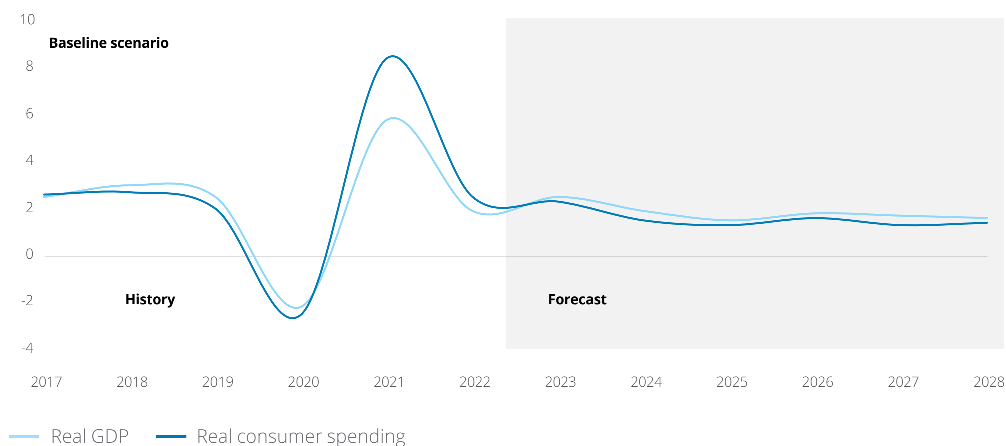
4. **Reliability:** When implementing AI tools for customers, retailers should be clear on what they can expect and the limitations of the interactions. For example, if the bots cannot provide a particular type of support, retailers could triage accordingly for customers upfront. Doing so will ultimately drive perceptions of reliability.

Conclusion

As retailers look to woo price-sensitive consumers in 2024, loyalty will have to be earned. To make that happen, trust will need to be the cornerstone of their profitability playbook.

Appendix

Figure 1: GDP versus consumer spending growth %



Note: Forecasts are by Deloitte's US Economics team.
Source: United States Bureau of Economic Analysis (sourced using Haver Analytics); Deloitte analysis.

Table 1: Metrics determining outperformers and underperformers

FY2020–22 median	Outperformers	Middle of the road	Underperformers	Overall
Return on assets (ROA)	16.2%	10.2%	3.8%	11.6%
Total debt-to- EBITDA	1.8x	2.2x	4.5x	2.2x

Notes: Deloitte analysis of 39 leading US-based retailers. Three-year averages are used to summarize company-level performances over FY2020–22. The table represents the median values across companies in each group. Outperformers had ROA of 11.6% or more and Debt-to-EBITDA of 2.2x or less, while underperformers had ROA less than 11.6% and Debt-to-EBITDA exceeding 2.2x over FY2020–22.
Source: S&P Capital IQ

Table 2: Profitable growth

FY2020–22 median	Outperformers	Middle of the road	Underperformers	Overall
Revenue CAGR	10.7%	6.3%	2.7%	7.5%
EBIT margin	10.8%	7.5%	2.5%	6.0%
Net margin	7.8%	5.3%	0.2%	4.0%
Total assets turnover	1.8x	1.3x	1.5x	1.5x
Return on invested capital (ROIC)	12.8%	8.3%	-1.5%	8.3%
FY2023–25 median				
Revenue CAGR	3.1%	4.0%	0.7%	3.1%
EBIT margin	10.9%	6.6%	3.4%	5.9%
Net margin	8.3%	4.8%	2.2%	3.9%

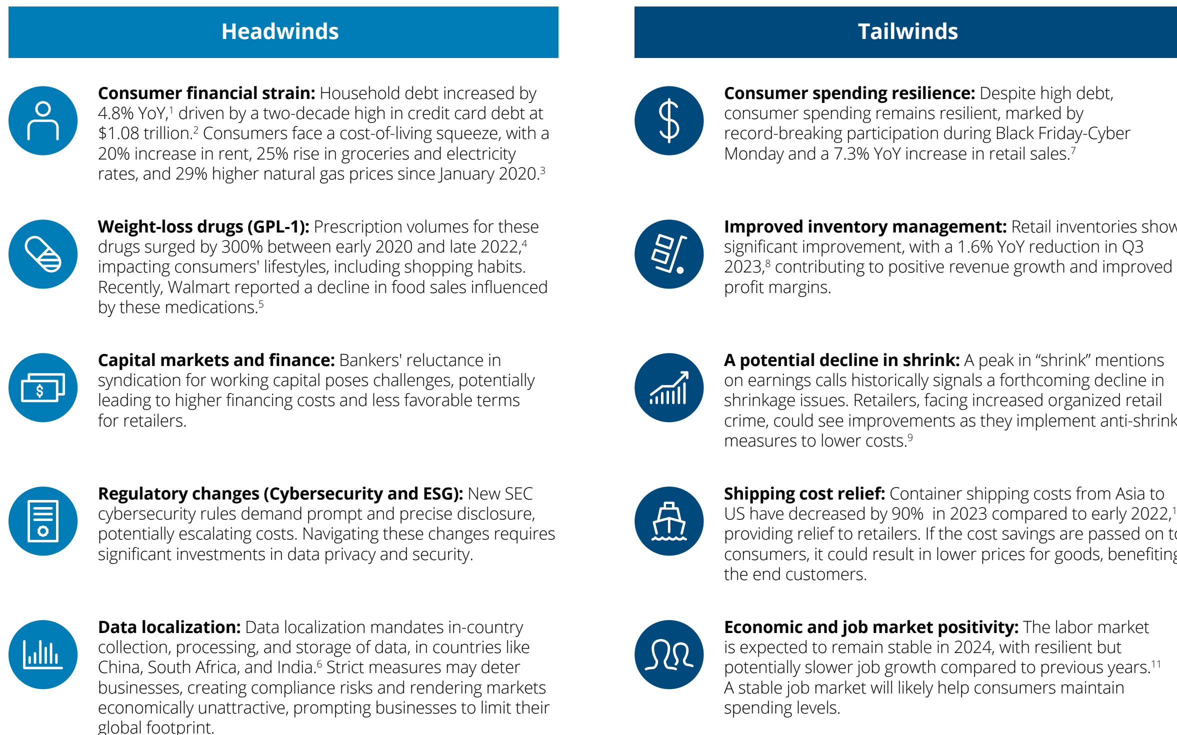
Notes: Deloitte analysis of 39 leading US-based retailers. Three-year averages are used to summarize company-level performances over FY2020–22 for metrics other than revenue. Estimated metrics for FY2023–25 are calculated based on consensus analyst estimates sourced from S&P Capital IQ as of December 8, 2023. The table represents the median values across companies in each group.
Source: S&P Capital IQ

Table 3: Balancing debt and growth ambitions

FY2020–22 median	Outperformers	Middle of the road	Underperformers	Overall
Revenue CAGR	10.7%	6.3%	2.7%	7.5%
Capital expenditure % of revenue	2.0%	3.4%	2.2%	2.3%
Total assets CAGR	5.1%	6.3%	2.5%	4.1%
Total debt CAGR	-1.2%	-0.9%	-0.3%	-0.9%
Total debt-to-capital %	56.6%	55.7%	70.2%	60.8%

Notes: Deloitte analysis of 39 leading US-based retailers. Three-year averages are used to summarize company-level performances over FY2020–22 for metrics other than revenue, total assets, and total debt. The table represents the median values across companies in each group.
Source: S&P Capital IQ

Figure 2: 2024 challenges and opportunities



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