HOW THE NEW AMERICAN CONSUMER IS CHANGING THE NATURE OF PHYSICAL RETAIL SPACE

By David Berliner and David Shim

The first half of 2015 has seen numerous retail store closing announcements and several new retail bankruptcy filings including those of Wet Seal and RadioShack.

As each month brings new announcements of store closings or news of another retail bankruptcy filing, one question naturally emerges: How many more retailers will file amidst the industry turbulence?

While there is no quick or easy conclusion, any discussion of the changing retail industry must examine two of the key issues driving the current industry turmoil: (i) financial strain caused by unprofitable physical locations, and (ii) the emergence of a new American consumer increasingly motivated by changing tastes and new technology. These factors will continue to drive further industry restructuring in the near term as established retailers confront new realities facilitated by rapidly changing consumer behavior.

2015 STORE CLOSINGS AND RETAIL BANKRUPTCY FILINGS

The chart on the next page shows a sample of announced store closings toward the end of 2014 and through the first half of 2015. The
THE NEW AMERICAN CONSUMER

With the near-ubiquity of smartphones in today’s society and the ability of these devices to penetrate every aspect of life, especially for younger generations, shopping is increasingly taking place in a mobile manner and without the need to visit physical store locations. Traffic to physical stores was down 9.8 percent on average year-over-year in Q1 2015. Declining foot traffic in malls is harming many traditional retailers. Without the consistent flow of potential customers, struggling retailers are seeing declines in revenue per store and the impulse buys associated with foot traffic.

Younger consumers now demand multi-channel engagement through multiple mediums such as Facebook and Instagram in addition to access to the latest styles. More agile retailers that focus online are able to better engage their customer base with active social media activity and can more quickly introduce new styles through their e-commerce platforms than traditional retailers. Many popular retailers have found success with limited to no physical locations. For example, companies such as Bonobos and the Nordstrom-owned Trunk Club are offering consumers a predominantly online shopping experience supplemented by select physical locations that act as “clubhouses” for customers to further engage and shop with the company.

REMAINDER OF 2015 AND BEYOND

The National Retail Federation (NRF) recently cut its retail sales forecast to 3.5 percent growth for 2015 versus its 4.1 percent forecast in February. The NRF attributes the soft growth to inclement winter weather in the beginning of the year, the West Coast port shutdown and expected weaker back-to-school sales. For example, the NRF’s recently released back-to-school spending survey revealed that U.S. consumers were expected to spend 9.3 percent less than last year. Also, the Commerce Department announced June retail sales decreased 0.3 percent as consumers held back on a range of goods. Furthermore, the Conference Board just reported that its index of consumer confidence dropped to 90.9 in July from a revised 99.8 in June and consumer expectations for economic activity over the next six months plunged to 79.9 from a revised 92.8.

COSTLY LEASE AGREEMENTS

With U.S. consumer confidence plunging and retail sales remaining relatively stagnant, retailers must be prepared to adapt to a more selective American consumer who is also less likely to visit a physical store. As revenue growth is increasingly being sourced from online sales, lease and other operating expenses associated with unprofitable stores are becoming more pronounced and an unsustainable drag on the cost structures of brick-and-mortar retailers. This increases the need for certain retailers to trim their store networks as they simply do not have enough revenue to support them.

These factors, in conjunction with a falling top line, have caused retailers such as Wet Seal, RadioShack, and A&P to file for Chapter 11 protection in order to reject the leases at unprofitable locations, and use Bankruptcy Code section 363 to sell certain other stores. However, outside of bankruptcy, it is not a simple decision to shutter unprofitable stores as companies must analyze their lease agreements to determine the costs to shut a shore with remaining life on the lease versus the cash burn of running a store until the lease expires. As landlords are finding it difficult to replace tenants, they have often made it too expensive for retailers to buy out leases.

<table>
<thead>
<tr>
<th>Retailer</th>
<th>Type</th>
<th>Store Closings</th>
<th>Announcement Date</th>
<th>Last Available 12 Months Sales ($ millions)</th>
<th>Bankruptcy Result (If Applicable)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Guess</td>
<td>Apparel</td>
<td>50</td>
<td>August 2014</td>
<td>$2,374</td>
<td>N/A</td>
</tr>
<tr>
<td>Sears</td>
<td>Department Store</td>
<td>77</td>
<td>October 2014</td>
<td>29,201</td>
<td>N/A</td>
</tr>
<tr>
<td>Debs Shops</td>
<td>Apparel</td>
<td>300</td>
<td>December 2014</td>
<td>205 Liquidation</td>
<td>N/A</td>
</tr>
<tr>
<td>Delia’s</td>
<td>Apparel</td>
<td>92</td>
<td>December 2014</td>
<td>120 Liquidation</td>
<td>N/A</td>
</tr>
<tr>
<td>Gymboree</td>
<td>Apparel</td>
<td>40</td>
<td>December 2014</td>
<td>1,233 Liquidation</td>
<td>N/A</td>
</tr>
<tr>
<td>Body Central / Body Shop</td>
<td>Apparel</td>
<td>265</td>
<td>January 2015</td>
<td>226 Liquidation</td>
<td>N/A</td>
</tr>
<tr>
<td>C. Wonder</td>
<td>Apparel</td>
<td>32</td>
<td>January 2015</td>
<td>51 Liquidation</td>
<td>N/A</td>
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<tr>
<td>JC Penney</td>
<td>Department Store</td>
<td>40</td>
<td>January 2015</td>
<td>12,313</td>
<td>N/A</td>
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<tr>
<td>Macy’s</td>
<td>Department Store</td>
<td>14</td>
<td>January 2015</td>
<td>28,058</td>
<td>N/A</td>
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<tr>
<td>Wet Seal</td>
<td>Apparel</td>
<td>338</td>
<td>January 2015</td>
<td>488 Liquidation</td>
<td>N/A</td>
</tr>
<tr>
<td>Cache</td>
<td>Apparel</td>
<td>21</td>
<td>February 2015</td>
<td>203 Liquidation</td>
<td>N/A</td>
</tr>
<tr>
<td>RadioShack</td>
<td>Electronics</td>
<td>1,784</td>
<td>February 2015</td>
<td>2,300 Partial Sale</td>
<td>N/A</td>
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<tr>
<td>Children’s Place</td>
<td>Apparel</td>
<td>125</td>
<td>March 2015</td>
<td>1,756 Liquidation</td>
<td>N/A</td>
</tr>
<tr>
<td>Dollar Tree / Family Dollar</td>
<td>General Merchandise</td>
<td>340</td>
<td>April 2015</td>
<td>19,476 Liquidation</td>
<td>N/A</td>
</tr>
<tr>
<td>Frederick’s of Hollywood</td>
<td>Apparel</td>
<td>31</td>
<td>April 2015</td>
<td>81 Liquidation</td>
<td>N/A</td>
</tr>
<tr>
<td>Pier One</td>
<td>Home Furnishings</td>
<td>100</td>
<td>April 2015</td>
<td>1,879 Liquidation</td>
<td>N/A</td>
</tr>
<tr>
<td>Simply Fashion</td>
<td>Apparel</td>
<td>250</td>
<td>April 2015</td>
<td>64 Liquidation</td>
<td>N/A</td>
</tr>
<tr>
<td>Anna’s Linens</td>
<td>Home Furnishings</td>
<td>200</td>
<td>June 2015</td>
<td>300 Liquidation</td>
<td>N/A</td>
</tr>
<tr>
<td>Gap</td>
<td>Apparel</td>
<td>175</td>
<td>June 2015</td>
<td>16,318</td>
<td>N/A</td>
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<td>A&amp;P</td>
<td>Grocer</td>
<td>25 Liquidated</td>
<td>July 2015</td>
<td>7,242 Partial Sale</td>
<td>N/A</td>
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</tbody>
</table>

Notes:
A – 11-month period cited in Bankruptcy Declaration of CRO Stephen Marotta
B – Store closings result partially from consolidation post-merger
C – Merger pending between Dollar Tree and Family Dollar. Revenue figure taken by combining last reported 12 month figures for both companies
D – Pending bankruptcy proceedings calls for initial store closings of 25 with the potential for further closings
Data used to develop the chart is from S&P Capital IQ and bankruptcy filings where the company is/was private

Announcement
Last Available
12 Months
Sales
($ millions)
Bankruptcy
Result
(If Applicable)
leading many retailers to continue to operate unprofitable stores. On the other hand, retailers with company-owned stores may be able to leverage their real estate portfolio to fund operating losses or invest in a turnaround strategy, such as what Sears has done with its recent REIT and joint ventures with mall owners.

CONCLUSION

Back-to-school sales are not a sure fire predictor of overall holiday sales performance, but can point to which individual retailers are poised for success or failure. If a retailer underperforms at back-to-school, there is a good chance it will also do poorly during the holiday season.

As the economy turns more toward e-commerce from brick-and-mortar sales, it is likely that additional stores will close, and more retailers will file for bankruptcy, until a new balance has been achieved. Although malls and stores will continue to exist, the prevalence of smart phones, tablets, and apps continues to make e-commerce an increasingly natural avenue through which purchasing and consumption occur. Traditional brick-and-mortar stores, with their high rent and employee costs, face a significant challenge – how to convince busy consumers to come to their stores, shop and thereby mitigate or reverse the declining foot traffic in retail shopping malls. The number of retail bankruptcies during 2015 demonstrates how difficult these challenges can be in certain cases and more retail store closings and bankruptcies can be expected in the remainder of 2015 and beyond.

1 Includes 2,122 closings associated with the RadioShack and Wet Seal bankruptcy proceedings.

A version of this piece previously ran on the Consumer Business Compass blog.

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UNDERSTANDING THE ELECTRONIC PAYMENTS ALPHABET & THE IMPENDING EMV DEADLINE

By Dennis Hoyt

As technological innovations emerge and our world becomes increasingly connected, the intersection of retail and technology continues to evolve.

With the spotlight on Apple Pay and the emergence of potential competitors, such as Samsung Pay and CurrentC, 2015 has brought a surge of interest and dialogue around electronic forms of payment, both among retailers and consumers. These technologies have prompted fascination with their ease of use and speculation about their perceived security. As new and evolving electronic payment technologies are being employed, understanding their unique advantages and intended uses can arm retailers with increased security of their point-of-sale (POS) systems, reduce instances of credit card fraud and ultimately, lower costs.

So, what can retailers expect to encounter when it comes to electronic payments?

TECHNOLOGIES

EMV (Europay/MasterCard/Visa) is the new worldwide standard for processing face-to-face transactions, and its stated purpose is to reduce instances of fraud. This technology involves a "smart" card with an embedded computer chip, which is read by special terminals. Unlike traditional magstripe cards - which are swiped at terminals - the new chip card is inserted into a terminal for a few seconds while the transaction occurs. The card itself uses dynamic data, rendering it extremely difficult to counterfeit. More about EMV later.

NFC (Near-Field Communications) NFC, or “Tap to Pay," sends data via very short electronic signals from a device with an NFC antenna to a contactless card reader. Mobile payment apps use smartphones with NFC capabilities to allow purchases at a contactless terminal. Few retailers implemented NFC-capable terminals from the outset, but once EMV and the iPhone 6 with its NFC capability came along, and other smartphone manufacturers began getting involved, the growth of mobile payments has accelerated rapidly. As more retailers implement NFC payment technology, and as momentum continues to build around its use by consumers, its future looks promising. Smartphones with NFC technology provide customers with an exceptionally secure payment method, and in the case of Apple Pay...
EMV DEADLINE

and Samsung Pay, they minimize the transfer of customer data to third parties.

Last fall, Apple introduced its latest smartphones with NFC capability, as well as the ability to purchase using Apple Pay. To set up Apple Pay on an iPhone, users “load” up to eight cards, simply by either taking a picture of the card or entering the card data. To pay, users hold their iPhone near a contactless terminal very briefly with their finger on the secure Touch ID. Then, using its EMV chip, a unique Device Account Number and dynamic security code are generated and transmitted for payment, but not the card number. Aside from the app’s ease of use, Apple also claims its technology is more secure as it includes a number of features to mitigate fraud. For instance, once entered into the iPhone, the only card data available is the card type and the last four digits of the card number; card data is not maintained on the iPhone or Apple servers.

Samsung Pay on Android phones is similar to Apple Pay and is currently available in the Samsung Galaxy S6 and its successors. In addition to NFC, it has an added technology called Magnetic Secure Transmission (MST). This allows purchases to be made from an S6 at a terminal with no NFC capabilities. The card data is instead read by the terminal’s magstripe reader, which allows the S6 owner to make a purchase at any card terminal – whether or not it’s NFC-capable.

Most other Android phones will also have NFC purchasing capability, coming preloaded with Google Wallet software. However, Google Wallet users will not have biometric security as iPhone 6 and Samsung Galaxy S6 users do, and although retailers will not be collecting customer data, some of the app providers may.

MCX (Merchant Customer Exchange) is a mobile payments venture owned by more than 50 major U.S. retailers. CurrentC is its mobile wallet app currently in development, with testing scheduled to begin at a few retailers in August 2015. MCX’s major goals are twofold: reduce the fees paid by retailers to card networks and incentivize customers to make more purchases by offering discounts electronically for products and services. To set up the app, customers provide personal and banking information, and then download both the CurrentC app and each retailer’s app. At the point of sale, instead of using NFC technology, they simply enter their QR code from their smartphones. Although QR code scanning technology may be secure, CurrentC will be collecting customers’ personal, banking and shopping information, possibly leading to hesitation from consumers. Also, very similar to MCX’ CurrentC app, European-based Seamless rolled-out its SEQR app (pronounced “secure”) in Europe in 2014, going live in the U.S. this past summer.

**IMPEENDING EMV DEADLINE**

While the technology and its many benefits should be top of mind for businesses, perhaps even more important is the approaching deadline that U.S. retailers face regarding their payment systems. For those retailers adopting or updating EMV systems, keep in mind that Oct. 1, 2015, is the “liability shift” date for credit card fraud. On that date, the liability for any card fraud will shift from the card issuer to the party that has the least EMV-compliant systems in place (be it the merchant or the card issuer). In other words, if the card issuer has issued chip-based cards, but a merchant hasn’t yet updated its system and terminals to accept those cards, then the merchant will be liable for any fraud at their store. Therefore, to avoid a potentially significant increase in their liability, face-to-face retailers will need to have payment terminals and systems in place that are capable of reading and processing EMV card transactions.

This new standard for liability comes from the fact that the EMV process is considered the new gold standard of payment technology. Not only does it involve cards with a more secure computer chip, it also utilizes more robustly protected terminals and processing systems. Unlike magstripe cards, the new chip card contains data that are updated at checkout when the card is inserted into an EMV terminal. With this secure system in place, the process will be more difficult to interrupt and the card more difficult to counterfeit.

Along with reduced instances of card fraud, fewer data breaches for brick-and-mortar merchants and an increased sense of security for customers, the new technology brings other benefits. For merchants with EMV terminals capable of accepting both contact and contactless payments, if 75 percent of their card transactions originate from EMV terminals, they will be exempt from the Payment Card Industry Data Security Standard (PCI DSS) validation requirements each year (though they must still be PCI-compliant). Additionally, virtually all new EMV platforms provide retailers with the ability to accept contactless payments. This is not only attractive to customers, but also allows retailers to stay ahead of this increasingly popular payment method.

The transition period begins this October and ends when all terminals and cards will be EMV-only – likely several years from now. During this period, most terminals will accept both magstripe and chip cards, and cards will be issued with both magstripes and chips, which is referred to as “backwards compatibility.” And even though retailers with EMV terminals that accept magstripe-only cards can still be victims of fraud, they will not be liable for the costs of fraud because of their EMV compliance. That being the case, we recommend retailers update their terminals sooner rather than later.

Still, even as magstripe cards are completely phased out, the threat of fraudsters still looms. In the near term, they’ll likely continue to use fraudulent magstripe cards at storefronts, while in the long run, they may shift more of their nefarious activity to the internet – a trend we’ve already seen in other countries. With that in mind, as businesses consider their transition to EMV technology, they should be sure to closely monitor chargebacks and reversals, check customer IDs at the point-of-sale and bolster e-commerce payment platforms with stronger controls, such as MasterCard’s SecureCode program andVerified by Visa.

A version of this piece previously ran on the Consumer Business Compass blog.

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MILLENNIALS SET TO REBUILD RETAIL INDUSTRY FROM THE GROUND UP

By Doug Hart and Stuart Eisenberg

Retailers, are you prepared for the Millennial effect?

Born roughly between 1980 and 2000, Millennials, are poised to cause a tidal shift in the retail industry because of their spending power and unique characteristics that greatly influence how and what they purchase. According to Advertising Age, Millennials will spend more than $200 billion annually starting in 2017 and $10 trillion in their lifetimes.

Given Millennials’ immense buying power and the fact that there are more than 80 million of them – making their generation larger than Baby Boomers and 20 percent bigger than Generation X – retailers should consider re-evaluating their business strategies to ensure they align with the preferences of this influential demographic.

Critical to retailers ensuring their business strategies are in sync with Millennials is understanding the demographic’s priorities and behaviors. Unlike consumers from previous generations who have shared common characteristics, Millennials possess an incredibly unique behavioral profile. Millennials are:

• "NOwners" – Prizing experiences over ownership, they love shopping but see it as a form of entertainment and are often inclined to browse, but not buy. Smart retailers are turning this to their advantage and offering shoppers a fun experience. For example, H&M’s store in midtown Manhattan has a runway shoppers can walk down wearing their new clothes – they are filmed and the best videos are displayed on storefront screens.

• Tech-savvy – Millennials are glued to their mobile devices and have a strong preference for brands that offer seamless integration between online and offline shopping. According to research from data and analytics company Annalect, 52 percent of Millennials surveyed said that the technology a brand uses is the most important factor when making a purchase, compared with 48 percent who said brand name is most effective.

• Impatient – With all the world’s stores at their fingertips, Millennials prefer not to stand in line or wait for purchases to be delivered. This desire for instant gratification, in fact, drove an uptick in so-called click-and-collect (buy online, pickup in-store) purchases during the U.K.’s holiday shopping period. Click-and-collect purchasing allows customers to make purchases online and receive a discount when they pick up their purchase at a designated store. Some commentators see retail stores eventually transforming to serve as distribution hubs, with qualified experts on hand to offer advice.

These generation-defining behaviors are largely born out of the technological revolution in which Millennials grew up and which is responsible for the generation’s overall penchant for online shopping. And while Millennials like shopping online, they still appreciate the brick-and-mortar experience. According to a study by OpinionLab, digitally savvy Millennials are the only generation that prefers shopping malls over shopping carts, despite their proclivity for technology.

However, for retailers to attract Millennials to their physical locations, they need to adjust their approach to real estate. To be better aligned with the type of in-store experiences Millennials crave, retailers should consider the following factors for their brick-and-mortar establishments:

• Interiors – Renovate and retrofit interiors to make them bright, attractive, esthetically pleasing places to be. Install charging stations, with comfortable seating and WiFi, so shoppers can recharge their mobile devices on the go. Rotate signage frequently to remain fresh, and include self-service kiosks to reduce line waiting times.

• Tenant mix – Have or be close to a wide variety of businesses, including fitness and entertainment providers, so that Millennial shoppers can also work out, relax and socialize.

• Pop-ups – Once an oddity, pop-up stores are becoming more common and popular with Millennials. They also can afford retailers short-term leases – often lasting just a couple of weeks – that provide new and online stores with a temporary storefront to increase their brand awareness, and deliver the new and differentiated experiences Millennial are seeking.

Because it will take more than an appealing physical space to attract Millennials, retailers also need to rethink their marketing and merchandising strategies in order to more effectively target this key age group and should consider:

• Featuring low pricing for quality merchandise – as well as consistent pricing across channels – to appeal to Millennials who came of age during the Great Recession. According to a study by The Intelligence Group (TIG), 36 percent of Millennials claim they only make purchases they deem as necessary.

Read more
MILLENNIALS

- **Telling a cohesive and engaging online story** – to keep pace with Millennial consumer desires. Millennials rely heavily on the Internet and social media for shopping and researching products. According to the data in a *Forbes* article, 72 percent of Millennials research and shop their options online before buying, looking at price comparisons, peer reviews and social networks for information. While they may ultimately spend a higher share of dollars online compared to other generations, according to a recent *Reuters* article, many Millennials primarily care about what their personal networks think and say about products, and that the retailers they follow have an appealing social presence. In fact, *Forbes* also reports that 32 percent of Millennials claim they have quit purchasing from brands that have “unacceptable” social practices.

- **Offering personalized interactions and consistency across channels** – to satisfy consumer demands for integrated, seamless and customer-centric shopping experiences. Millennials shop for entertainment. Results from the same TIG study reveal that 50 percent of Millennials say they browse for items regularly without the intention of purchasing. According to a *NPD Group* report, overall conversion rates are lowest among Millennials. To stay ahead, online retailers must provide compelling destinations for shoppers, along with entertaining and memorable shopping experiences.

There’s no denying Millennials are transforming retail. And to alleviate FOMO (Millennial speak for “Fear Of Missing Out”), retailers must evolve with this demographic – not only the products and prices they want, but also the experience and the speed that they have come to expect.

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**PErspective in CONSUMER BUSINESS**

The trend of retail "rightsizing" has continued in 2015, with many big-name brands shrinking retail square footage and corporate headcounts as customers make more of their purchases online. The growth in e-commerce, coupled with sluggish consumer spending, has hit department stores and high street chains especially hard – J.C. Penney, Macy’s and Sears have all seen multiple store closings over the last couple of years as part of the multi-year trend.

Distressed retail firms are being forced to shutter stores, even if the savings they stand to realize seem low. This year, Gap announced it would close 175 underperforming stores in North America – a quarter of its physical locations in the region – after posting sales declines for five quarters in a row. According to CNBC, overall square footage among retailers could shrink by a third to a half in the next five to 10 years. In an effort to bridge the physical-digital divide, retail firms are experimenting with omnichannel models, offering services such as in-store pickup for online orders, self-serve kiosks and online returns.

Another way retailers are adjusting their strategies is by establishing more discount outlets in order to connect to a wider audience. J. Crew recently launched J. Crew Mercantile, which will offer similar savings and merchandise to its existing discount brand J. Crew Factory. J. Crew Mercantile will be located in more Main Street and mall locations, closer to residential areas as opposed to out-of-town factory outlet malls.

PE firms may find the most opportunities in the middle market, as small to mid-sized retailers become distressed and seek assistance to right-size their operations. According to *Reuters*, middle market lending is a rare bright spot for PE firms in the current challenging buyout environment, due to smaller deal sizes. With regulatory restrictions on the amounts of debt banks can offer, it is increasingly difficult for PE firms to finance highly leveraged takeovers.

M&A activity is booming in many sectors, but PE firms are finding it harder to get in on deals, facing stiff competition from cash-rich corporates. According to New York-based data firm Dealogic, just 5 percent of deals announced so far this year have been private-equity backed, the *Wall Street Journal*’s CFO Journal blog reports. However, while they are finding it hard to put their dollars to work, PE firms are seeing increased exit volumes, according to *Business Insider*. This is also true in the retail consumer business segment. High-end retailer Neiman Marcus recently filed for an initial public offering after 10 years in private-equity hands. The current owners Ares Management and the Canada Pension Plan Investment Board bought the century-old firm from Warburg Pincus and the Texas Pacific Group (now TPG Capital) for $6 billion in 2013.

PErspective in Consumer Business is a feature examining the role of private equity in the consumer business industry.
ETHICAL CONSUMERISM IS ON THE RISE. ARE YOU READY?

By Doug Hart

Ethical consumerism – the practice of making purchasing decisions based on a product’s social and ethical positioning – is on the rise as consumers look to drive change by where and what they spend their dollars on.

Nielsen’s corporate social responsibility survey data revealed more than half (55 percent) of global respondents say they are willing to pay extra for products and services from socially responsible companies last year – a number that could possibly increase even more this year. Retailers need to radically shift their bottom-line focus and toward promoting the following:

TRANSPARENCY

The cornerstone of selling to ethically minded consumers is the elimination of the walls that once separated retailers from consumer oversight. For retailers to be considered transparent, “there must be an absence of hidden agendas and conditions, and a minimum degree of disclosure wherein transactions, practices, dealings and agreements are open to all for verification.”

For transparency to be realized, retailers need to pull back the curtain on their inner operations, from how they treat their talent to where they source their goods. Good.Must.Grow. reports that treatment of employees is the biggest factor (45 percent) when people decide how responsible a company is, followed by environmental impact (40 percent).

“Consumers, governments and companies are demanding details about the systems and sources that deliver the goods. They worry about quality, safety, ethics and environmental impact,” according to Steve New’s Harvard Business Review article, “The Transparent Supply Chain.” And retailers are responding by making more information on their supply chains available to the masses. With this increased openness surrounding operations, retailers have been forced to rethink how they work with their supply chain partners to ensure their values and standards align with the retailer’s own as well as consumers.

According to Raconteur, “This is why retail businesses are at the moment, for example, working closely with supply chain partners at home and overseas, devising guidance documents and sharing best practices to ensure certain minimum standards are met in the tens of thousands of factories from which retailers source their goods around the world.” For example, Levi Strauss & Co. was the first in its industry to establish global guidelines for water quality standards for its suppliers in...
an effort to minimize its burden on the global water supply.

To showcase for consumers the efforts they are taking to improve their supply chains, retailers are turning to new technologies. New reports in his Harvard Business Review article that retailers are using revealing technologies to allow consumers access to an unprecedented level of detail about the products they are purchasing through the use of technology tags, like RFID (radio-frequency identification). He notes: “The ubiquity of such mobile devices means that consumers can readily access this ‘Internet of things,’ gathering provenance information not just at the generic level of the item category or type but for the specific item. If I’m interested in, say, food safety, the technology can tell me not just about this type of chicken, but this chicken.” For example, Patagonia’s Footprint Chronicles is a website that allows people to trace its Nano Puff Pullover, Chucabuco backpack and more than dozen other products from design through the manufacturing process and into its distribution system.

By using transparency to empower consumers and place them in a position to hold businesses accountable, retailers are cultivating a stronger sense of trust. And it is this trust that helps retailers grow and diversify their consumer bases to include more of the ethically minded.

AUTHENTICITY

For retailers to achieve an authentic reputation, they need to demonstrate:
1. How their offerings make consumers’ lives better; 2. how the brand is committed to a customer’s well-being; 3. how the brand contributes to society as a whole. By showcasing how their companies contribute to the communities in which they work, live and play, retailers not only build meaningful relationships with their consumers, especially the ethically minded, they can also grow their bottom lines.

For example, Patagonia has embraced an “environmental ethos,” appealing to customers who also value sustainability. In a recent campaign, the retailer urged consumers to repair clothing instead of purchasing new, and it engaged with advocates and customers alike to support the sustainability movement. Throughout the year, sales reportedly increased by almost one-third to $543 million.

The New York Times reports that several studies have proven the impact that authenticity – real or perceived – can have on the bottom line. This bottom line impact might be because companies who are honest are preferred by consumers. According to an October 2014 study on authentic brands by Cohn & Wolfe, the behavior consumers demand most from big brands is communicating honestly about products and services.

Beyond demonstrating honesty, companies aiming to strengthen their reputation as an authentic brand should also consider highlighting the following:

- **Sincerity:** A while back, Levi Strauss & Co.’s “Go Forth” black-and-white videos highlighted the aftermath of Hurricane Katrina on New Orleans. According to Entrepreneur, the campaign positioned Levi Strauss & Co. as the “brand for pioneers who are in the process of building a new America.” It was in alignment with the company’s roots - selling built-to-last pants to pioneers during the California gold rush – without pushing its wares and showcasing its support of and faith in the community to rebuild itself. In the end, audiences felt it was a powerful demonstration of the company’s sincerity.

- **Contribution To The Greater Good:** At the core of Seventh Generation – the nation’s leading brand of household and personal care products that help protect human health and the environment – and driving its marketing plans is the company’s mission to enable consumers to make a difference in the planet and public’s health through everyday consumer choices. For Seventh Generation, this means providing consumers the opportunity to make a positive difference through their purchases of laundry detergent, paper towels and other household products.

- **Heritage:** According to The New York Times, “Tito’s Handmade Vodka, of Austin, Texas, is another company that emphasizes authenticity in its marketing. Its website tells the life story of Tito Beveridge, the founder, highlighting his commitment to quality while also pushing the heritage angle: The vodka is “made in small batches in an old-fashioned pot still,” using a “time-honored method.” The approach seems to be working: In 2013, the company sold 1.3 million cases of vodka, compared with 365,000 in 2010.”

Ultimately, according to The New York Times, people love being a part of an authentic brand because they aren’t just buying into a logo, they’re also “buying into a set of values.” And the Authentic Brand Index (ABI) has shown that the stronger a brand’s perceived authenticity, the more likely people are to become advocates for it.

Through promoting transparency and authenticity, retailers can achieve more than just growing their ethical consumer base. They acquire and develop brand loyalists who will journey with them beyond the transaction.
2014 was the third consecutive year of growth for U.S. initial public offerings (IPOs), in terms of both the number of offerings and proceeds raised.

But when we released our 2015 BDO IPO Outlook earlier this year, capital market executives were somewhat divided in their forecasts of IPO activity in 2015: 43 percent predicted an increase in IPOs for the coming year, while more than a third (35 percent) thought activity would fall flat compared with 2014. A smaller proportion (22 percent) anticipated a decrease in offerings on domestic exchanges. The second half of the year is likely to mirror the first half, as well, according to our recently released IPO Halftime Report. In fact, 54 percent of executives surveyed expect IPO activity to remain at the same level as the first half of the year, while over a quarter predict an increase in pace and one-fifth anticipate a decrease in offering activity.

Some key factors underlie this decrease in offering activity. In particular, despite optimistic predictions, it was almost inevitable that the IPO market was going to slow in growth due to the dramatic increases experienced in 2013 and 2014. At the same time, it is likely that the availability of private funding at attractive valuations is the main contributor to the decrease in the number of offerings in 2015 thus far. With an uptick in late-stage financing opportunities, start-up businesses have been able to delay going public. If access to private funding continues, bankers believe that a trend of fewer but better IPOs will emerge.

Bankers are least optimistic about the consumer and retail industry. In fact, consumer and retail IPOs are anticipated to either remain stable (42 percent) or decrease (35 percent) in the second half of 2015. This is more modest than executives’ projections at the beginning of the year, when 45 percent of executives predicted they would remain stable and 29 percent thought they would decrease. This is, however, a slightly better outlook than that of executives in our 2014 IPO Halftime Report, when less than one-fifth (18 percent) of respondents forecast an increase in consumer and retail IPO activity.

What’s behind the modest expectations for the sector? It may be that the first half of the year was actually much stronger than expected, with Renaissance Capital reporting 13 retail and consumer goods IPOs thus far in 2015, just slightly behind the 16 total IPOs reported for all of 2014. In fact, some of this year’s retail IPOs have been among the strongest seen across all industries, with Fitbit and Blue Buffalo pet products ranking among the top five IPOs this year so far (raising $732 million and $677 million, respectively). Retail IPOs have raised nearly $9 billion so far this year, according to Bloomberg, and capital markets executives may expect the sector to be unable to keep up with this atypical pace in the final months of 2015.

Additionally, mixed economic signals may continue to make it difficult to forecast IPO results through the end of the year. Low commodity prices continue to put dollars back into consumers’ pockets and decrease the cost of domestic manufacturing, but are also unsettling investors who remain uncertain as to when prices will rebound and how the markets will react. At the same time, market volatility abroad, particularly in China, is rattling U.S. public markets as foreign currencies decline against the dollar and threaten profit margins among international companies. Chinese e-tailer Alibaba – one of last year’s blockbuster consumer IPOs – saw its stock prices decline precipitously in August, with founder Jack Ma and Joseph Tsai announcing on Aug. 17 that they would buy back approximately $4 billion in shares in an effort to stabilize prices.

But investors may still find some bright spots in the retail IPO market. Luxury retailers continue to perform well, with Louis Vuitton Moet Hennessy reporting strong growth in the first half of the year, and many investors eagerly anticipating Neiman Marcus’ second attempt at a public offering. While there may be fewer offerings and continued uncertainty among investors focused on the retail and consumer business space, there may still be good deals lingering on the horizon to close the year on a good note.
What led you to focus your accounting work in the consumer business industry?
My background in retail and consumer products began long before my accounting career. Having worked for two major retailers throughout high school and college, it was a natural progression to pursue the consumer business industry when entering the professional arena. After college, I sought to work for a firm that served retail and consumer products clients, which I quickly learned did not narrow down my list of prospective employers. I actually have two tenures with BDO: one for four years right out of college, and another beginning in 2005 after I served a few years as a controller for a distribution company. During my first stint with BDO, the market was in a very different place, so I actually didn’t work with a retail client until I returned in 2005 – which marked the start of my retail background from a more formal accounting standpoint. Having worked in-store on the operational side armed me with valuable insights and context when I began working on the accounting side, and the blending of the two has allowed me to understand the practicalities of being in-store while looking at the bigger financial picture.

What are some of the biggest opportunities for growth that you see in the consumer business industry?
Some retailers are again focusing on their catalog businesses. Major players like Pottery Barn and Victoria’s Secret maintain brick-and-mortar stores as well as an online presence, but are still using catalogs to reach customers. To the extent that retailers can have touch points with customers, all of those various spaces contain opportunities. As we know, online and mobile have taken the spotlight, but just because something may seem like an antiquated strategy, it’s important to remember that any method to reach customers is a potential sale. Retailers should look back and realize that history illustrates that seeking opportunities for consistent touch points helps build brand recognition. If a retailer is not finding ways to be top of mind for consumers, then regardless of how robust a website or mobile offering is, customers aren’t going to visit its website or enter its store to make a purchase.

What do you see as some of the biggest challenges within the industry right now?
Challenges can range from internal business issues to external market difficulties. Operating in the digital space remains as one of the biggest opportunities as well as one of the biggest challenges. Retailers today, at the very least, must be technologically advanced enough to be in the face of the public and present a seamless online shopping experience without major glitches. Customer service also plays a major role in a consumer’s shopping experience, whether online or in-store. If a shopper’s experience is anything less than stellar, which is what they’ve grown to expect, they will be more likely to shop with a competitor moving forward. Therefore, it’s critical for brands to hire the right people and have the right technology in place in order to reach their target audience. They must remain cognizant of the fact that there’s always going to be another player that’s trying to take away market share.

What do you see as the overall impact of the work you do?
I’ve learned that at BDO, we approach our client relationships collaboratively. We strive to be a sounding board, to be available to answer calls and questions in a timely fashion, and to truly be a resource. We have such a breadth of experience within the Consumer Business practice that no matter the question, we have the answer. I devote a great deal of time getting to know my clients, both new and existing, and diving deep to understand their strategies and challenges. Even if the challenges my clients are facing are not accounting related, I look to connect them with the right resources to help solve their problems, be it from a tax-saving or transaction advisory perspective. I don’t want to be known as simply my clients’ auditor, but rather as the person who helps get them answers to the business challenges they face.

If you could give one piece of advice to your clients, what would it be?
So many of our clients focus on achieving growth, and we can be excellent advisors to them in reaching this goal. But we need to understand what growth means in the context of their business, so it’s imperative that they are constantly challenging their perceptions of why, how and where they hope to expand.

Does it mean growing organically? Does it mean growing geographically? The conversation starts with a hyper-focus on where it is a retailer wants to go and how they can get there. Then, commit to that path, because especially in this industry, it often takes time to gain traction. Of course, retailers can play it safe and prosper in markets in which they are comfortable. But they can also look for new and innovative opportunities to drive growth cautiously when the timing is optimal.

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MARK YOUR CALENDARS

The following is a list of upcoming conferences and seminars of interest for retail and consumer product executives:

**SEPTEMBER 2015**

- September 27-30
  - National Retail Tenants Association’s 2015 Annual Conference
  - Orlando World Center Marriott
  - Orlando

**OCTOBER 2015**

- October 5-7
  - Shop.org Annual Summit 2015
  - Pennsylvania Convention Center
  - Philadelphia

- October 8-9
  - TAMU Retailing Summit 2015*
  - Westin Galleria Hotel
  - Dallas

- October 11-14
  - NACS Show
  - Las Vegas Convention Center
  - Las Vegas

- October 14-16
  - Franchise Leadership and Development Conference
  - InterContinental Buckhead
  - Atlanta

- October 27-28
  - Women’s Wear Daily Apparel & Retail CEO Summit
  - New York

- October 28-30
  - RILA’s Retail Law Conference
  - JW Marriott San Antonio Hill Country
  - San Antonio

**NOVEMBER 2015**

- November 4
  - K.I.D.S./Fashion Delivers Annual Gala
  - American Museum of Natural History
  - New York

- November 15-17
  - Private Label Trade Show
  - Rosemont Convention Center
  - Chicago

**JANUARY 2015**

- January 7-8
  - AGENDA*
  - Long Beach Convention Center
  - Long Beach

*Indicates that a BDO representative will be present at the event

**BDO’S CONSUMER BUSINESS PRACTICE**

BDO has been a valued business advisor to retail and consumer product companies for 100 years. The firm works with a wide variety of retail clients, ranging from multinational Fortune 500 corporations to more entrepreneurial businesses, on myriad accounting, tax and other financial issues.

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