

Kurt Salmon ✨

# Winning the Ship-from-Store Battle

Strategies and Tactics



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**Many retailers are** hurrying to implement ship-from-store programs, and for good reason. They can deliver significant revenue growth, margin increases and service improvements while helping to delay massive capital costs. And enabling ship-from-store may seem relatively straightforward, due to widely available technology solutions.

But in a rush to enable ship-from-store, retailers can put their profitability and customer experience at risk. A carefully planned approach will help minimize risk, and it starts with strategic decisions like defining store coverage, creating order management rules and detailing key organizational changes. With those answers in place, retailers can shift to tactical decisions around optimal store operations. While the typical implementation for a large, 500+ store chain usually takes less than two months and can begin to deliver results immediately, the ability to execute against these strategic and tactical issues will separate winners from losers over the next five years.

### **Defining Store Coverage**

The first decision point many retailers face when defining store coverage is how many stores to enable. Overall capital efficiency should drive this decision. The cost of implementing a ship-from-store strategy must be weighed against the overall margin uplift it can provide, which is driven by numerous factors. While many of the first attempts

at ship-from-store were cost plays driven by supply chain groups who desired to push down spending on parcel service and 3PL costs, the equation evolved as retailers began to notice additional benefits.

These benefits quickly proved that, far from being a simple cost saver, ship-from-store could also drive inventory advantages while increasing both sales and store traffic. For example, online sales at American Apparel have increased by 30% since they started using their stores as backup fulfillment centers. And Nordstrom attributes a 39% online sales bump to efforts to integrate its online and in-store inventories. Ship-from-store helps inventory positions because retailers do not need to buy as much e-commerce-specific product if they can ship from stores as well. Better yet, some stores experience up to 17% comps due to sales credit from selling e-commerce-only SKUs brought into the store through returns. Retailers can also choose to have store associates ship items with high in-store stock from the store to decrease the odds of needing a markdown at a later date.

Retailers looking to implement ship-from-store can also use it to alleviate peak season demand on current distribution centers, and this will help drive the number of stores selected for ship-from-store implementation. With increasing e-commerce business beginning to stress fulfillment capacities to the breaking point during peak

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season, retailers who lack ship-from-store capabilities are often operating at maximum capacity. This means that if they want to increase their delivery speeds, their only option is to invest ~\$100 million for a new distribution center to cover peak periods (during which demand can spike to five to 10 times higher than average). This is an expensive proposition that can add up quickly for businesses growing e-commerce sales by double digits year over year. In many cases, the cheaper option is to enable ship-from-store in enough stores to reduce the strain.

Geography is also an important consideration. As delivering products faster is one of the biggest reasons why retailers are implementing ship-from-store, the right store locations are a critical factor. Small-scale rollouts should include stores near large metropolitan areas, and national rollouts should attempt to balance coverage with delivery speed.

### **Determining Order Management Rules**

Ship-from-store order management rules can be thought of as a sourcing profitability equation bound by constraints. The constraints should be defined first and often include business rules. For example, one Kurt Salmon client developed their own internal fulfillment logic to determine (by SKU) when and where they should source orders. Their first constraint was that they would never split an order. Therefore, the first decision might be, “Where can we source this order so the customer is receiving all items together?” The next constraint could be based

around service level or capacity (e.g., “I will ship this order from store ‘Y’ to fulfill a next-day promise” or “I will ship this order from store ‘Z’ to alleviate a constraint on my regional DC”).

Once these business constraints are navigated, retailers should look at the most profitable place from which to ship inventory at a given moment. Profitability in this case can be influenced by pulling multiple levers to influence margin:

#### **1 Avoiding markdowns.**

Shipments should be made from stores with high inventory on the tail end of a product lifecycle to maximize full-price sell-through. Chains with a highly localized product mix will also find that ship-from-store is a great way to sell SKUs from the wrong store/region without heavy markdowns (e.g., a winter coat bought in Buffalo returned to a store in Miami). For example, Toys R Us reported that 33% of items sold through its ship-from-store program are considered “inactive products” at their traditional stores. Instead of marking down those items, Toys R Us was able to sell them at full price.

**2 Cost levers can include shipping costs and labor costs (e.g., using store labor vs. a 3PL or shipping from a national DC vs. a local store).** The cost of direct-to-consumer distribution is roughly five times the cost of retail distribution, and stores are even less efficient without the automation and scale of a DC. This means ship-from-store SKU selection will be critical to controlling costs, especially on single-line orders. The order management engines driving these decisions must be able to determine the least expensive option after looking at margin and service levels.

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Unfortunately, most retailers' IT systems are not currently equipped to provide the flexibility necessary for ship-from-store, and their order management systems will have to evolve to make fulfillment decisions based on inventory levels, shipping costs, delivery speeds and service-level expectations from an ever-widening pool of choices. Ship-from-store also has important implications for fulfillment rules and allocation algorithms. Forecasting how much of each SKU is needed for each store and warehouse

is a herculean task, and at the moment, there are no comprehensive software solutions to tackle it.

#### **Preparing for Needed Organizational Changes**

After determining which items will be shipped from which stores, retailers must tackle the significant organizational change inherent to any ship-from-store effort. While determining order management algorithms takes serious brain power, agreeing upon shared sales credit and defined store metrics to prevent "passing" on orders can be just as difficult.

### **SHIP-FROM-STORE TECHNOLOGY**

**Retailers must be prepared to embrace new technologies to ensure that systems run smoothly and effectively. Two important systems to consider are DOM and RFID:**

- 1** Creating a distributed order management (DOM) system is essential to enabling a ship-from-store program. Such systems ready the stores for order fulfillment and workforce management while defining sourcing and fulfillment rules that are consistent across channels. A DOM system provides a centralized network of information that ensures consistency in delivery. DOM systems develop rules for prioritization, sourcing and exceptions in inventory sourcing. Inventory can be segmented and prioritized based on order type, due date, service commitments and other factors. Retailers can also hold and release inventory based on any attribute to fulfill anytime, anywhere customer pickup or delivery. DOM systems also address sourcing by determining where orders should be sourced based on capacity, inventory, cost or margin. Ultimately, the DOM system creates a set of sourcing rules that pools together all of this information to source inventory from the optimal location. The system also considers exceptions like specific reserve and release orders, backorders, and product substitutions.
- 2** By enabling a DOM system, stores can achieve greater inventory accuracy and develop better fulfillment practices. However, such systems by themselves are not enough. Data information in stores is only 50% to 70% accurate. RFID technology now provides retailers with up to 99% inventory accuracy in stores. While RFID also provides numerous other benefits, retailers considering ship-from-store and other omnichannel strategies benefit greatly from the inventory accuracy afforded by RFID cycle counting.

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Successful ship-from-store strategies do not stop after determining revenue sharing; this is only half of the profitability equation. Retailers must also determine how costs will be shared. Broadly, ship-from-store can be thought of as a transfer of work from the supply chain to the store. But in reality, it's less of a hand-off, and instead will require more collaboration between the two. This has big implications on who will provide and pay for additional staffing and space. These issues are exacerbated during the holidays, when space, inventory and labor in stores and distribution centers are at a premium. Division of labor can cause trouble if the staff is not trained or able to flex between required areas and if organizational leaders are not aligned. Today, less than 40 percent of retailers assign strategic control over both store and consumer-direct fulfillment to a single executive, according to the 2012 State of the Retail Supply Chain report. Often, these responsibilities are split among multiple leaders. Though each channel operates under the same brand name, they are controlled as entirely separate business units. This makes a collaborative plan all the more important.

Further complicating the picture is the fact that most retailers have separate retail and e-commerce organizational divisions. This division creates a second environment (besides DCs and stores) for competing internal objectives. Aligning P&L responsibility and shared services models is often difficult, as many organizations made the decision years ago

to grow these businesses as separate entities. This can affect flexibility and responsiveness, especially without common metrics and measures of success.

Finally, ship-from store has considerable implications for key retail decisions such as order volume, allocation, replenishment, promotions and markdowns, often requiring a complete rethinking of how these business decisions are made. This is especially true of the analytics that support these decisions. A senior executive of a leading retailer recently expressed that the analytic impact of ship-from-store was an underappreciated aspect of their project plan. Leading retailers such as Macy's and J. Crew are already beginning to address these analytical challenges of ship-from-store.

#### **Reaping the Benefits**

While store fulfillment requires significant change management to orchestrate the focus areas discussed above, there are immediate benefits available once the foundational requirements of DOM, store fulfillment systems and store processes (inventory, pick, pack, service, returns, etc.) are met. These benefits can quickly alleviate the specter of unmet service levels, overcapacity DCs (or expensive 3PLs) and increasing e-commerce competition. Those who execute quickly and efficiently can gain a lasting competitive presence in the new omnichannel world. But retailers without the underlying foundational infrastructure in place may find themselves losing sales, leaking margin and straining under organizational chaos.

## TACTICAL CONSIDERATIONS

Once the major strategic decisions have been made, the next step is addressing a laundry list of tactical decisions. Common questions may include, but are by no means limited to:

### Process

- » What are the best processes for picking (back vs. front/batch vs. order), packing, shipping and inventorying?
- » What measurements and metrics will be tracked post implementation to quantify value/success?
- » What physical changes do we need to make to facilitate operations?

### People

- » What are the controls and responsibilities for managing operations within the stores?
- » How will individual stores manage labor planning, particularly during heavy coincidental Internet and store peaks (e.g., Cyber Tuesday)?
- » When will associates work (during or after store hours)?
- » Who will create the SOPs?
- » Who will define and distribute best practices?

### Systems

- » Which systems (or changes to existing systems) are needed to support ship-from-store?
- » How are orders routed using a preferred fulfillment logic engine?
- » Which store pick-and-pack system (e.g., WMS or similar) will be used?
- » Which parcel shipping systems will be used?

### Implementation

- » When will these processes/changes need to be deployed?
- » What is the best way to pilot/test to improve the program before rollout to the broader chain?
- » How will stores organize and structure associate training?
- » Which parcel shipping systems will be used?

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## AUTHORS

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The logo for Kurt Salmon, featuring the name "Kurt Salmon" in a black, handwritten-style script font.

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