EXECUTIVE INSIGHTS

VOLUME XVII, ISSUE 39

Better Together: The New Logic of Retail Partnerships

Partnerships have long been a familiar feature in certain parts of the retail landscape with Starbucks and/or banks inside your local grocery store, but lately they've been popping up all over — Sephora inside of JCPenney; at Target, which recently turned over its pharmacy business to CVS; and at big-box stores like Best Buy, where Samsung and other brands operate their own stores within the store.

More recently retail partnerships have evolved and broadened to assume many forms, among them retailer-in-retailer, digital, loyalty and marketing partnerships.

When partnerships succeed, they deliver value to both parties; the sum is greater than its parts. But partnerships can be tricky. Neither party should enter into one without first performing a thorough analysis to determine potential benefits, possible pitfalls and the likelihood of success.

Partnership Benefits — Separate but Equal

The best partnerships benefit both parties — by lowering costs, expanding markets, delivering deeper and more varied customer data that can fuel future growth, building customer loyalty, and securing a greater share of the customer's wallet. At the same time, traditional retailers facing unprecedented disruption from digital competitors, declining mall traffic, and shrinking margins have strong reasons to consider their options as hosts:

Make better use of space. Big-box retailers saddled with too much static or unloved real estate may profit by allowing popular brands they already sell to ramp up their presence and create distinct, in-store destinations, as Best Buy has done with Samsung, Apple and others.

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Stimulate foot traffic. Some brands are powerful draws all by themselves, no matter where they set up shop. A bank or large retailer might bring in a coffee shop, for instance, to attract new customers who may then decide to cross-shop at the host retailer. Capital One's partnership with Peet's coffee to create their 360® Café concept is a clear example of this.

Improve customer experience. New and thrilling retail experiences can generate excitement throughout the store. Furniture stores, for instance, can partner with restaurants and electronics stores so that customers have more reasons to shop there in the first place and more reasons to stay. Marketing and loyalty partnerships can enable "surprise and delight" consumer experiences that would otherwise be impossible or prohibitively expensive.

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Increase competitiveness and profitability in a specialized category. When it comes to certain product categories that lie outside a retailer's core business, serving customers in a compelling and profitable way can be challenging. That's why Target chose to partner with CVS — a category leader that understands the specialized nuances of staffing, SKU complexity and reimbursement in the pharmacy business. Even in cases where the gap between core businesses is not as wide, a specialized partner may have better inventory, more developed supply-chain relationships and more sophisticated knowledge of the market. Partnership means sharing revenue, but the result is often higher profits for both parties.

Partnership Models At-a-Glance

Traditional brand-retail partnerships. A well-known brand carves out "store-in-a-store" space within a larger retail setting. Clothing and cosmetics labels have been doing this for years inside department stores. The model varies depending on the autonomy of the brand, which may bring its own staffing and systems. The Samsung-inside-Best-Buy model is a recent example, offering consumers a distinct, self-contained, branded experience, and a full range of connected products — an arrangement that provides real value to Samsung by creating the opportunity to tell a coherent story.

Retail-retail partnerships. One retailer sets up shop, or takes over exclusive control of a category, inside another retailer's store. CVS's recent acquisition of Target Pharmacy takes Target out of the pharmacy business altogether, replacing Target's pharmacy with what amounts to a mini-CVS store within the Target stores. It's a familiar model to Target, which has long hosted Starbucks coffee shops, but the CVS arrangement is a step-change given that the pharmacy was a focus for Target for many years. Meanwhile, although JCPenney has stepped back from a plan to position itself as an emporium for other brands, Sephora inside JCPenney remains a key performance driver for both brands and has transformed the beauty offerings at the department store. Similarly, the Finish Line and Macy's partnership looks to improve sales of athletic footwear in Macy's stores.

Digital partnerships. A smaller brand leverages the traffic, systems, and/or logistics infrastructure of a larger ecommerce player in what amounts to the digital equivalent of a mall. Although this arrangement is not as popular as it once was with big players, more of whom have come to recognize the critical strategic importance of developing their own branded presence across channels, it is still an effective strategy for small retailers and brands that don't have the scale and reach to maintain a profitable online presence on their own.

Loyalty partnerships. Companies such as non-competing retailers and travel organizations engage in the soft sharing of incentives and data across loyalty programs. This model is less common in the U.S. than in other markets, such as the U.K. and Canada, with notable exceptions including Sears, which has been very active in this area and the recently launched Plenti® rewards program that is run by American Express. At the most basic level, loyalty partnerships may also include re-selling each other's gift cards.

Marketing partnerships. Brands targeting the same consumer demographic will co-develop content for direct mail, broad-reach ad spots, and other channels, resulting in lower customer acquisition costs and better ROIs. Examples include Under Armour's partnership with Dick's Sporting Goods in holiday advertising and the direct mail campaigns shared by start-ups Blue Apron, Casper, Favor and others.

Donors, meanwhile, have their own compelling reasons for pursuing partnerships:

Reduce cost. Partnering with a large retailer under one roof can deliver more traffic and is almost always more affordable than establishing a stand-alone presence, especially for specialized brands with a narrow range of products. The same holds true for marketing reach, where a lesser-known brand can "borrow" the larger store's equity to drive more rapid growth in awareness while the larger brand or retailer simultaneously benefits from lower costs and a connection to another consumer set.

Attract new customers. You may be able to reach new customers — younger or older; more or less affluent — who might not otherwise consider trying your brand, whether introduced via co-marketing or co-location. For example, Sephora has broadened its market by partnering with JCPenney, while at the same time introducing new customers to its host.

Gain retail expertise. Brands that don't have a scalable retail model of their own can learn from their hosts, while also gaining access to profitable markets in a way that's true to the brand and showcases the brand experience.

Partnership Pitfalls

The only partnerships that last are ones that make strategic sense for both parties. That's a challenge, given that no two retailers — much less a retailer and a brand — enter a partnership with identical goals. It is therefore critical that each partner proceed with caution and follow these imperatives to avoid common pitfalls:

Protect your strategic priorities. It may be tempting to partner with another organization specifically to gain access to best-in-class practices in an area where your own organization is weak. Just be careful not to relinquish what really ought to be an internal strategic priority. That's the mistake many brick-and-mortar businesses made in the early days of ecommerce. For example, Borders outsourced its ecommerce program to Amazon, and consequently never developed that critical digital capability for itself.

Beware of weak strategic rationale. Does it make sense to put a doctor's office in a department store purely to take advantage of foot traffic? Probably not given the impact of appointments, low correlation with trip purpose and limited convenience of a large store — a drug store is a much better fit. Examine the potential benefit skeptically and ask yourself, "How critical is this benefit to my retail concept?" and "How does this really improve the customer's experience?" If there isn't a clear and compelling (and often obvious) answer to these questions, the partnership is starting on unstable ground without a true value proposition.

Protect your identity. Hosts should be careful not to surrender so much of themselves to partners as to diminish the value they can deliver to customers on their own. First and foremost, customers need a reason to visit the host. The same applies to donors, who must be sure the partnership helps them deliver what consumers expect from them.

Avoid unhealthy relationships. Partnerships can leave both parties exposed to each other's weaknesses. Even a smart, well-executed partnership might not be enough to prevent a weaker party from closing stores or compromising its brand in a way that harms the other party.

Key Elements of Success

Successful partnerships share these traits:

Similar markets. Customer overlap need not be 100% — part of the goal, after all, is to expand the market for both parties — but the pairing needs to make sense.

Clear expectations. Both parties should understand and support one another's goals from the outset. Requirements include a thorough business plan, aligned incentives and an activation plan designed to deliver maximum value across the board. Aligned metrics and financial incentives are a must.

Adequate resources. Cooperation is key. Both parties must make the appropriate organizational and resource commitment — at the corporate level and the store level. There must be a close working relationship in order to present the customer with an experience that's true to both brands.

Flexibility. Both parties must commit to revisiting the partnership on a regular basis, typically with reference to a set of specific milestones. They must each be willing to refine the terms of the partnership as results indicate, or abandon it altogether and part ways if it's not creating value.

Is a Partnership Right for You?

Partnerships are by no means a simple cure-all solution for what ails your business. Research, preparation and realistic goal-setting are critical. But in a rapidly evolving retail universe, partnerships may be more relevant than ever — for making profitable use of excess space, increasing foot traffic, developing new strategic capabilities, gaining fresh insights into consumer behavior and developing ever stronger bonds with customers. The right partnerships create a whole that is much greater than the sum of the parts, by connecting and leveraging each party's key strengths all while creating a better value proposition for each business's customers.

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