Transforming Retail Business

U B Pravin Rao
Senior Vice President - Retail (North America)

My name is Pravin Rao. I am heading the retail IBU. This is relatively a new practice started earlier this year and focuses on retail industry in North America. It gives me great pleasure to be here and present our plans for the retail business. In this presentation, I will be covering primarily the retail market, the competitive situation, key demand drivers, and Infosys strategy.

I am actually on this slide on industry size and outlook. The total retail sales in 2002 were $3.6 trillion. It is expected to grow to $3.8 trillion in 2003. The revenues from some of the key retail segments are shown in the graph. Clearly the key segments are specialty retailers like a Best Buy or Circuit City, general merchandizers like JC Penney, Wal-mart, or a grocery or supermarkets like Crogers. Retail is a low-margin, high volume business. The industry fortune is clearly linked to consumer spending and state of economy. In the first half, the demand was very sluggish, but retailers are expecting the second half to be much better. So, they are cautiously optimistic about the prospects for the industry in the second half. Wal-mart continues to dictate the agenda for most retailers. Wal-mart started off as a general merchandizer and has started offering products in almost all other segments of retail and they are slowly edging out local competition by their wide variety of products at very low prices. So an important element of retailer's strategy is therefore competitive differentiation vis-à-vis Walmart.

Traditionally retailers are low adapters of technology, they view IT more as a cost center. IT spend is about 1.5%, which is very low when compared to some of the other industries like financial services. In 2003 the total IT spending is expected to be about $31 billion. Out of this the total, spend on external service providers is about $9 billion, in addition the spend of $11.9 billion on internal spending, also presents a significant opportunity for outsourcing. The success of Wal-mart is to a large extent attributed to their investment in IT, so as such today IT is increasingly seen as a critical element of business strategy. In fact the Wal-mart factor is driving additional investments in IT amongst the retailers. Retail IT is also very metric driven with very strong focus on ROI. Some of the initiatives in IT are around reducing operating cost, improving productivity and customer retention. The other characteristic of retailers is they are very reluctant to outsource. They believe that the retail industry and the retail business is very unique and it is very difficult for outsiders to comprehend. So domain knowledge is therefore very key to work on this barrier.

The market place is very crowded, the big four and IBM have significant presence in retail. Amongst the Indian players, Infosys probably has the largest share, but as far as the retailers are concerned today, they perceive very little differentiation amongst the tier- one Indian players. There are also a lot of packages in the retail space. Retailers prefer packages to custom-solutions and they typically go in for best of breed package solutions. What this means is many of the retailers could be using Retek for their core merchandizing, they could be using Global Store from Fujitsu for their operations in their stores, and they could be using PPKMS from Manhattan in their warehouses. There are lot of product vendors and apart from some of the vendors like Retek and JDA whose products address the entire retail value chain, there are a large number of niche product vendors addressing very focused very niche segment in retail like type optimization or warehouse management or demand forecasting. There have been lot of alliances between the big four, IBM, as well as some of the ISPs but most of the alliances have not been very effective to date and they are not really delivering the intended benefits to the business. So there is definitely a play for creating a differentiated position by providing high business excellence coupled with execution excellence.

Some of the drivers for IT spending are listed here. From the business perspective some of the drivers are pressure from Wal-mart, increasing focus on customers, lowering companies' operating cost and the emerging multi-channel environment. If you look at it from the IT side, some of the

drivers are IT platform consolidation, ever-increasing pressure to reduce IT costs and package focus. As Wal-mart continues to squeeze out local competition by their variety of products at very low prices, retailers are forced to have more efficient processes and technologies to stay competitive. So there is a lot of investment in technology due to this factor. Retailers are also increasingly focusing on customers as they are finding it very difficult to get additional savings from operations. So there are a slew of customer facing initiatives that they are investing in. Multi-channel environment is another hot area. Today customers can order through stores, they can order through web, or they can order through catalogue. Retailers have a multiple variety of systems for order capture, order management and execution, and the experience of consumer is varied across these channels. Today the consumer is demanding uniform experience irrespective of the channel they chose to order from, so this presents a good opportunity for retailers and is forcing retailers to come up with uniform order management and fulfillment system to provide a seamless experience to the consumers. On the IT side there is consolidation happening, retailers are trying to consolidate the various legacy IT platforms in order to save cost. They are also implementing newer systems, which are lot easier to maintain.

So to summarize today, the buying behavior is very different from what we talked in the past. The buying behavior is today driven mostly by cost saving and return on the investment focus. The decision making is today jointly between IT and business, they jointly take decisions on IT projects. There is also more scrutiny on projects, vendors, and budgets. Retailers today prefer stable vendors with deep experience in domain as well as solid execution capabilities.

Retail has been a very important sector for Infosys since its inception. We have a very good experience in retail. In 2003 the total sales from retail worldwide was $86 million that is about 11% of Infosys' revenues, and retail has been growing at a CAGR of 51% over the last five years. Retail North America share is about 70 million in 2003, which represents about 9% of total Infosys sales. Today in North America we have more than 25 retail clients and we are growing strong.

As I said earlier, retail is a relatively new unit and we have our own structure, we have a dedicated sales force, dedicated domain and business consulting group, we have our own technology consulting and delivery units. The sales force in retail has good knowledge of retail industry and are able to identify specific needs across various retail segments. They also have good experience in solution selling. The domain consulting group decides their business and domain consulting skills as well as chain management skills. They also have very strong experience in many of the retail functions. They also have good expertise in several of the best of breed retail packages. The technology consulting as well as delivery groups also have good experience in retail domain as well as in various retail products having worked in this industry for quite some time. We will continue to strengthen and build on this expertise and we believe that we are right now well positioned to address the unique problems facing the retail industry by providing innovative solutions.

So to summarize, retail IT spending is very metric driven with high focus on return on investment. The decision making is shared by business and IT and there is a very strong focus on providing effective solution to business. Business needs also vary across retail segments and this calls for segment-specific deep domain understanding. Domain knowledge is also very critical to overcome the retailers' barrier to outsourcing. Retailers also prefer by and large packages over custom solutions and there is a wealth of products out in the retail space. Many of the alliances between ISPs and system integrators have not been very successful and they have not delivered the intended business benefits, so there is definitely a need for a true end-to-end retail functional understanding coupled with execution excellence. Our strategy for this market is to focus on a set of retail solutions that addresses specific points of retailers, leveraging the global delivery model and existing service offerings. We will work closely with our alliance partners as required to enhance the quality and innovativeness of the solutions. We believe that this will help us in extending our lead and provide differentiated services and as well as position Infosys as a business solution provider enabled by the best and most cost- effective global delivery capabilities. While we are focusing on solutions, we are also parallely working on strengthening and capitalizing on our existing service offering, capabilities,

and client relationships. And our IBU structure with its own dedicated sales force, domain, and business consultant and technologies will help us in aligning us to these needs.

While we are working on multiple solution areas, let me talk about one of the solution areas - lead time optimization. Today in fashion industry, the products are sourced mainly in Far East due to enormous cost benefits that they bring. The lead times are very large typically six to eight months, whereas the lifetime of this products are very short, may be three to four months, these products can be sold only in the season in which they are made for. So for instance if you are making a product for a fall season which starts in August-September, typically you need to place orders with your suppliers for the product as early as January and the fall season just lasts for three to four months, from say, August through November. The demand in the fashion industry is also very volatile because it is very difficult to predict the fashion changes, the fashion choices six to seven months in advance. So this leads to a very unique situation in this industry in the sense that there are times when retailers realize that products are not selling as much as they expected and they are forced to cut down the prices. These are called mark-downs, and there are times when the products are selling like hot cakes but retailers are not able to leverage on this because it take long lead time to source this products. So in a fashion industry today, the biggest opportunity is therefore not in reducing the transaction cost but in recapturing the margins lost due to stock outs and mark-downs. It is estimated that more than 40% of retailer sales are lost due to markdowns and stock outs. The LTO solution that we offered, enables the retailers to postpone the decision closer to the actual consumption as well as help them analyze the cost benefits of the various sourcing scenarios. This therefore helps them in bringing down the revenue leakages due to mark-downs and stock outs. This is actually a very powerful solution for overcoming the demand risk and the richest source of profitability in short life cycle industry.

We have partnered with a leading vendor in US who has a product in this space. This vendor is very experienced in short life-cycle products and we have partnered with this vendor to go to market with this LTO solution. We are actually piloting this product with one of the leading retailers in North America. Prior to the pilot, we did a business case where we clearly estimated that the retailer would have increased revenues of more than one billion dollars in three to four year by investing about 100 million. So this is the kind of solutions that we want to take to the market, and as you can clearly see, the benefits to the business are tremendous and these solutions really address the business problems. A typical LTO engagement consists of opportunity assessment, business case justification, production pilot, and a full scale roll-out, and the skills really required for this are program management skills, functional and process consultants skills, supplier adaption specialist technical consultants, chain management and training specialist, LTO black belts, etc. As you can see the solutions are not merely changing by doing some programing work or implementing a package, it is much more than that. In many of these cases, the solutions call for lot of chain management and organization change itself.

So in conclusion, to ensure sustained and profitable growth, we in retail IBU are bringing solution focus to all that we do for our clients. We are weaving together our services, portfolio, the global delivery model, our technology excellence, the alliances, the execution excellence, and the deep domain knowledge to create innovative newer solutions and all this is enabled by the structure of retail industry focus, sales and relationship management teams, business and domain consultants, and technologies. We strongly believe that this will help us in growing much faster and much more profitable in the year to come. Thank you.