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Kementerian Pendidikan, Kebudayaan, Riset, dan Teknologi
Universitas Andalas

Manajemen Ritel

Strategi Keuangan Ritel

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Pemenang Hibah Inovasi Pembelajaran Digital (IPD)
Kementerian Pendidikan, Kebudayaan, Riset, dan Teknologi

Questions

- How is a retail strategy reflected in retailers’ financial objectives?
- How do retailers need to evaluate their performance?
- What is the strategic profit model, and how is it used?
- What measures do retailers use to assess their performance?

Retailer Objectives

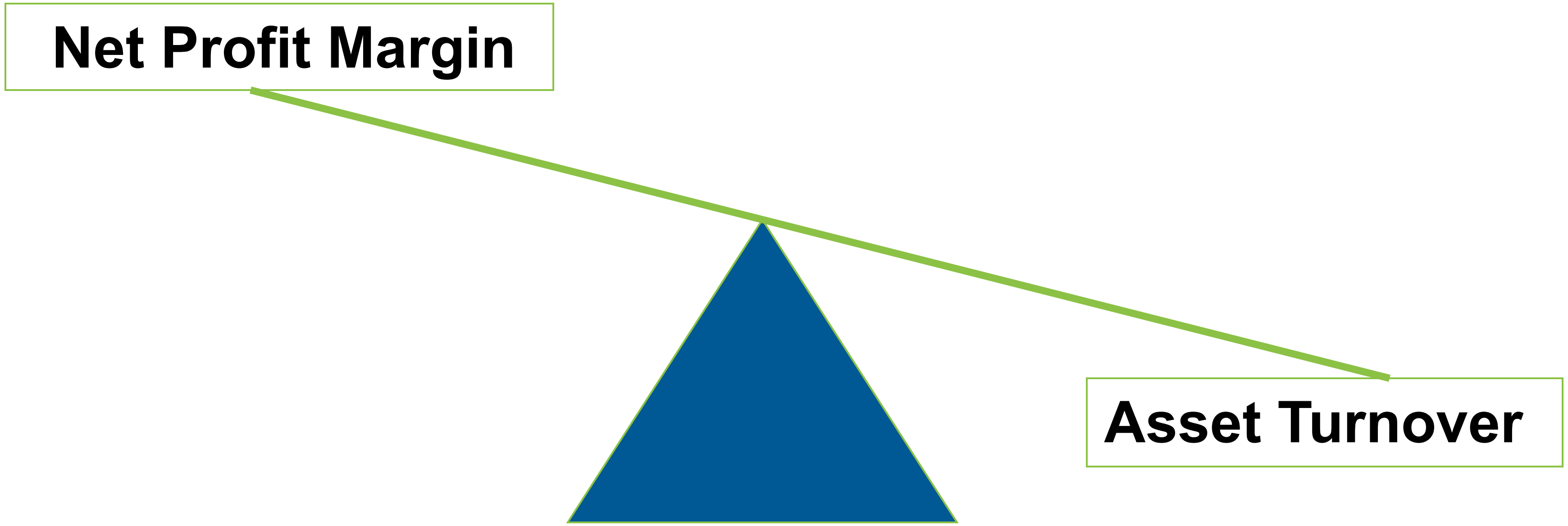
Financial – not necessarily profits, but return on investment (ROI) – primary focus

Societal – helping to improve the world around us

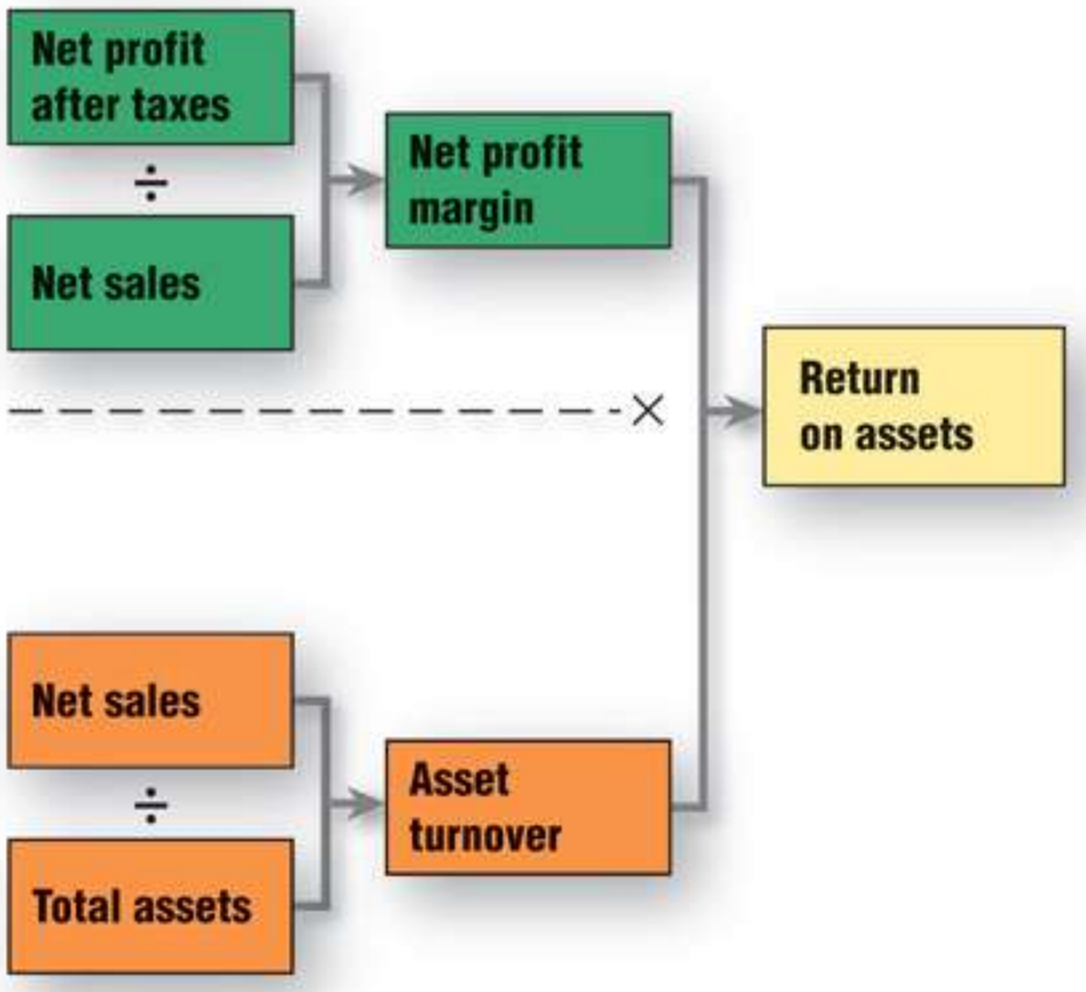
Personal – self-gratification, status, respect

Strategic Profit Model:
Financial Tradeoff Made by Retailers to Increase ROI

Outlines Tradeoff Between
- Margin Management
- Asset (Inventory Management)



Components of the Strategic Profit Model



Profit Margin x Asset turnover = Return on assets

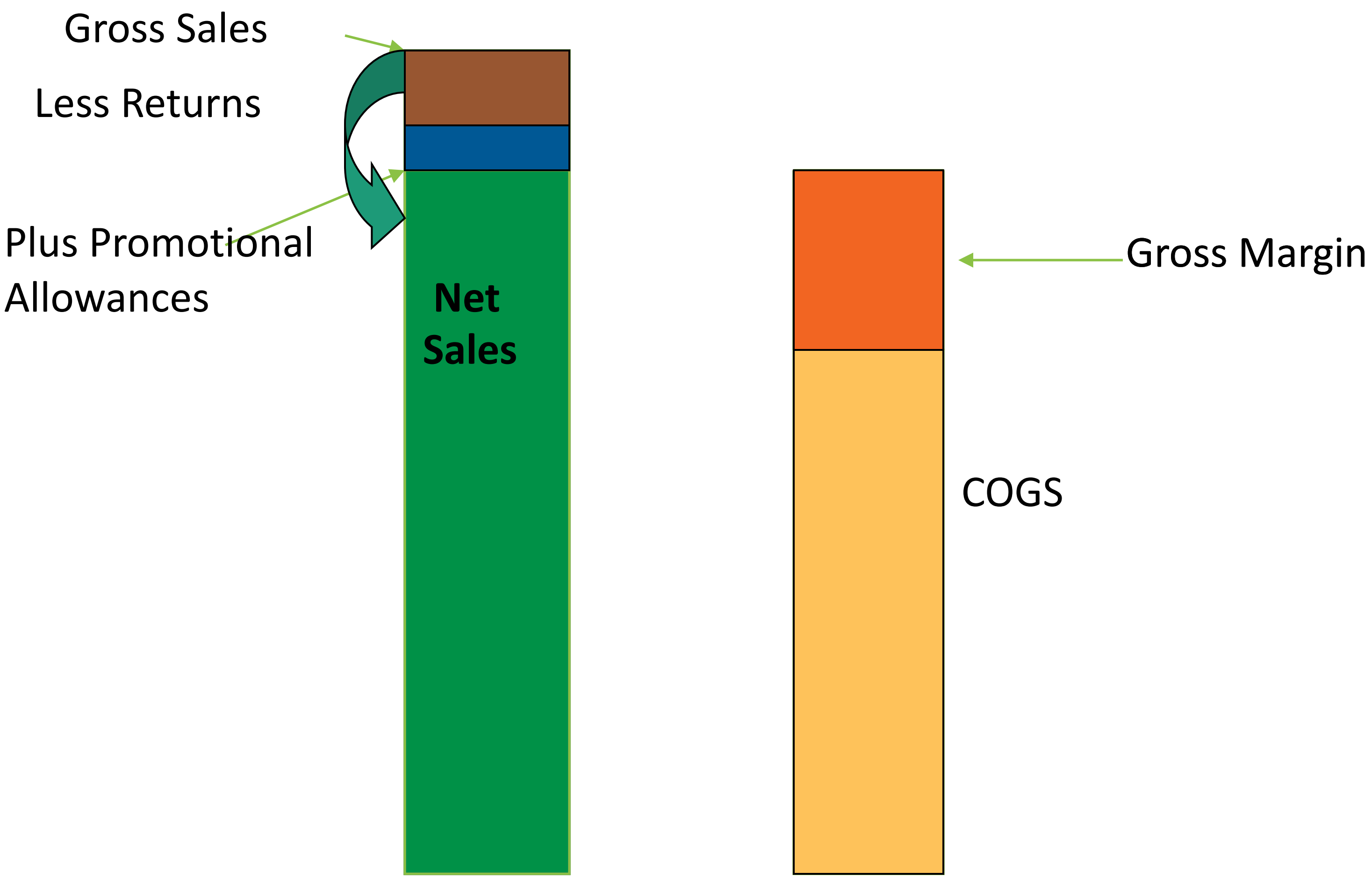
$$\frac{\text{Net profit}}{\cancel{\text{Net sales}}\ \text{(crossed out)}} \times \frac{\cancel{\text{Net sales}}\ \text{(crossed out)}}{\text{Total assets}} = \frac{\text{Net profit}}{\text{Total assets}}$$

Net Profit Margin: reflects the profits generated from each dollar of sales
Asset Turnover: assesses the productivity of a firm’s investment in its assets

Margin Management

- Net Sales = Gross Sales + Promotional Allowances - Return
- Cost of Good Sold (COGs)
- Gross Margin (GM) = Net Sales - COGs
- Expense
    - Variable (e.g.. sales commissions)
    - Fixed (rent, depreciation, staff salaries)
- Net Profit = Net Sales – COGS - Expenses

Components of Gross Margin



Gross Margin (Gross Profit) : profit made on merchandise sales without considering the operating expenses and corporate overhead expenses.

Maintaining/Increasing Margins

- Pay a Lower Price to Vendor
- Charge Customers a Higher Price
- Reduce Price Competition
  - Exclusive Merchandise
  - Brand Variants
- Reduce Retailer Costs -- Direct Product Profitability (DPP), Activity Based Costing
  - Floor Ready Merchandise, Vendor Source Tagging
  - Packaging -- Shipping, Display

Selling expenses	=	Sales staff salaries + Commissions + Benefits
General expenses	=	Rent + Utilities + Miscellaneous expenses
Administrative expenses	=	Salaries of all employees other than salespeople + Operations of buying offices + Other administrative expenses

Net Operating Income

- Before interest expenses/income, taxes, and extraordinary expenses
- A commonly used overall profit measure due to the lack of control over taxes, interest, and extraordinary expenses
- Allows for a comparison of financial performance across companies or divisions within companies

$$\frac{\text{Gross Margin} - \text{Operating Expenses}}{\text{Net Sales}} = \text{Net Operating Income \%}$$

Macy's: $\frac{\$10{,}773 - 8{,}937}{\$26{,}970} = 6.81\%$

Costco: $\frac{\$7{,}406 - \$5{,}781}{\$60{,}151} = 2.70\%$

Net Profit (after taxes)

Net Profit = Gross Margin – Operating Expenses – Net Interest - Taxes

$$\frac{\text{Net profit after taxes}}{\text{Net sales}} = \text{Net Profit \% after taxes}$$

Macy's: $\frac{\$995}{\$26{,}970} = 3.70\%$

Costco: $\frac{\$1{,}103}{\$60{,}151} = 1.83\%$

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Asset Management

- Assets:
  - Economic Resources (e.g., inventory, buildings, computers, store fixtures) owned or controlled by a firm
  - Current Asset and Fixed Asset
- Current Assets =

  Inventory + Cash + Account Receivable
- Fixed Assets = Fixture, Stores (owned)
- Asset Turnover = Sales/Total Assets
- Inventory Turnover = COGS/Avg. Inventory (cost)

Inventory Turnover

- A Measure of the Productivity of Inventory:
  - It is used to evaluate how effectively retailers utilize their investment in inventory
- Shows how many times, on average, inventory cycles through the store during a specific period of time (usually a year)

Inventory Turnover = COGS/avg inventory (cost)
Inventory Turnover = Sales/ avg inventory (retail)

Importance of stock turnover rate

- Inventory turnover rate differs by
  - Industry
  - Product categories

- Most retailers that are having problems achieving adequate profits have a poor Inventory Turnover Rate.

Example: Kmart vs. Wal-mart

Inventory Turnover

$$\frac{\text{Cost of Goods}}{\text{Average inventory}} = \text{Inventory Turnover}$$

Macy's: $\frac{\$16,197}{\$5,317} = 3.04$

Costco: $\frac{\$52,746}{\$4,569} = 11.54$

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Importance of Inventory turnover

- How do retailers increase Inventory Turnover?
    - Increase Sales
    - Decrease Inventory
        - Decrease delivery lead-time
        - Drive waist out

- It's important to have an efficient turnover rate: not so slow that things seem stale and shopworn, yet not so fast that the floor looks half-empty.

Asset Turnover

$$\frac{\text{Net Sales}}{\text{Total Assets}} = \text{Asset Turnover}$$

Macy's: $\frac{\$26,970}{\$29,550} = 0.91$

Costco: $\frac{\$60,151}{\$17,494} = 3.44$

Return on Assets

Net Profit Margin x Asset Turnover = Return on Assets

Macy's:	3.70%	x	0.95	=	3.37%
Costco:	1.80%	x	3.44	=	6.19%

Return on Assets is a very important performance measure because it shows how much money the retailer is making on its investment

Evaluation of Financial Path: Macy's and Costco

Macy's	Costco
Higher net profit margin	Higher asset turnover

- Retailers (and investors) need to consider
  - both net profit margin and asset turnover when evaluating their financial performance
  - the implications of strategic decisions on both components of the strategic fit model
    - EX: Increasing prices => gross margin, net profit margin ↑
      sales, asset turnover ↓

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Profit Margin Management Path: Gross Margin Percent

$$\frac{\text{Gross Margin}}{\text{Net Sales}} = \text{Gross Margin Percent}$$

Stores: $\frac{\$350{,}000}{\$700{,}000} = 50\%$

Gifts-to-Go.com $\frac{\$220{,}000}{\$440{,}000} = 50\%$

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Operating Expense Percent

$$\frac{\text{Operating Expenses}}{\text{Net Sales}} = \text{Operating Expenses \%}$$

Stores: $\frac{\$250,000}{\$700,000} = 35.7\%$

GiftstoGo.com: $\frac{\$150,000}{\$440,000} = 34.1\%$

Net Profit Percentage

$$\frac{\text{Net Profit}}{\text{Net Sales}} = \text{Net Profit Percentage}$$

Stores: $\frac{\$\,59{,}800}{\$700{,}000} = 8.5\%$

Gifts-to-Go.com: $\frac{\$\,45{,}500}{\$440{,}000} = 10.3\%$

Balance Sheet Information for Gifts to Go and Proposed Internet Channel

Balance Sheet Information	Gifts To Go Stores	Gifts-To-Go.com (Projected)	Businesses Combined
Accounts receivable	$140,000	$120,000	$260,000
Merchandise inventory	175,000	70,000	245,000
Cash	35,000	11,000	46,000
Total current assets	350,000	201,000	551,000
Fixed assets	30,000	10,000	40,000
Total assets	380,000	211,000	591,000
Ratios			
Inventory turnover	2.0	3.1	2.3
Asset turnover	1.84	2.09	1.93
ROA	15.70%	21.60%	17.80%

Asset Turnover Management Path: Inventory Turnover

$$\frac{\text{Cost of Goods}}{\text{Average Inventory}} = \text{Inventory Turnover}$$

Stores: $\frac{\$350,000}{\$175,000} = 2.0$

Gifts-to-Go.com: $\frac{\$220,000}{\$70,000} = 3.1$

Asset Turnover

$$\frac{\text{Net Sales}}{\text{Total Assets}} = \text{Asset Turnover}$$

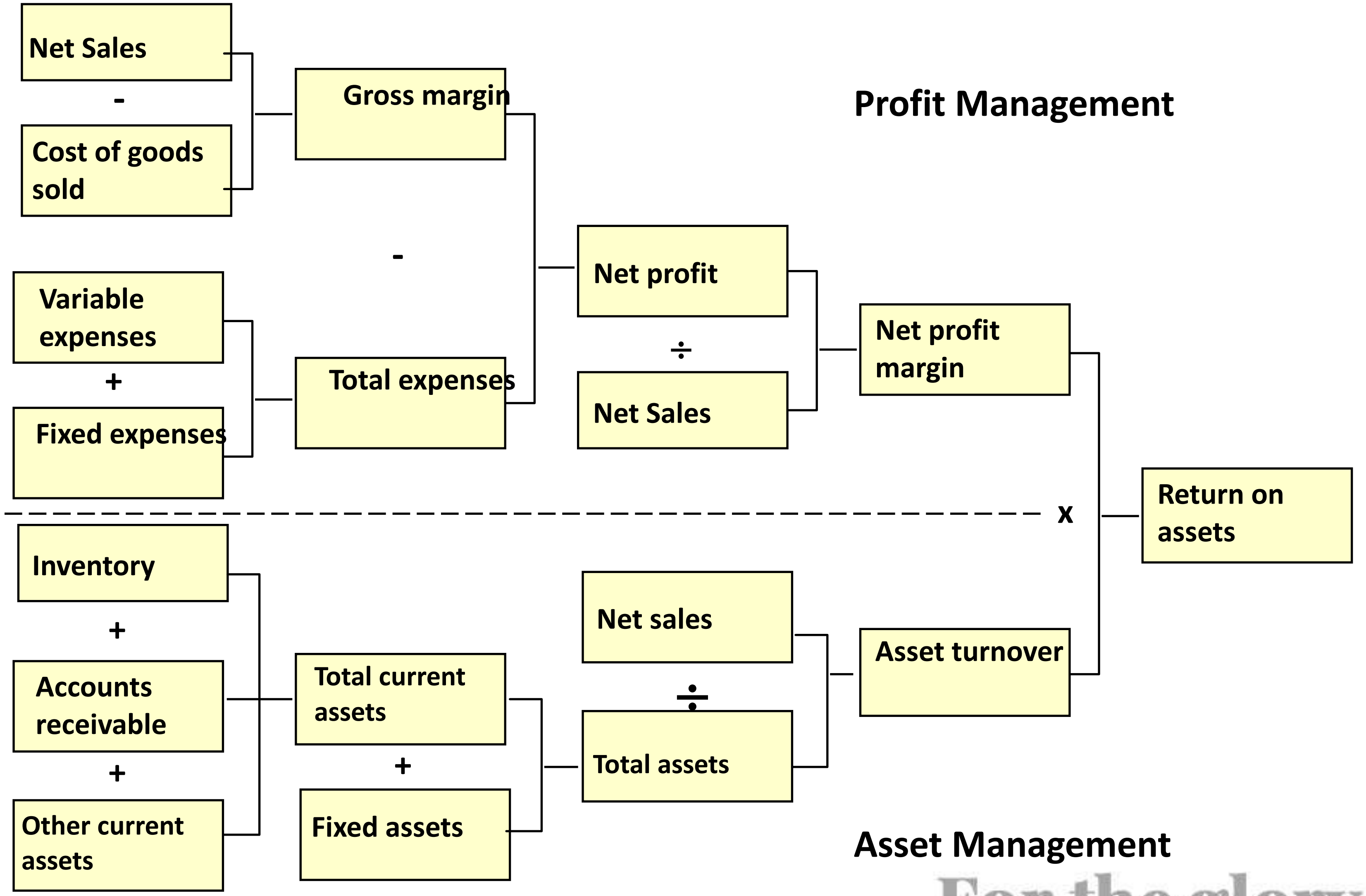
Stores: $\frac{\$700,000}{\$380,000} = 1.84$

Gifts-to-Go.com: $\frac{\$440,000}{\$211,000} = 2.09$

Return on Assets

Net Profit Margin x Asset Turnover = Return on Assets

Stores:	8.54	x	1.84	=	15.7%
Gifts-to-Go.com	10.3	x	2.09	=	21.3%


Profit Management
Net Sales
-
Cost of goods sold
Gross margin
-
Variable expenses
+
Fixed expenses
Total expenses
Net profit
÷
Net Sales
Net profit margin
x
Return on assets
Inventory
+
Accounts receivable
+
Other current assets
Total current assets
+
Fixed assets
Net sales
÷
Total assets
Asset turnover
Asset Management

Setting and Measuring Performance Objectives

Retailers will be better able to gauge performance if it has specific objectives in mind to compare performance.

Should include:

- numerical index of performance desired
- time frame for performance
- necessary resources to achieve objectives

Setting Objectives in Large Retail Organizations

Top-Down Planning
Corporate Developmental Strategy

Category, Departments and sales associates implement strategy

Setting Objectives in Large Retail Organizations

Corporate

Bottom-Up Planning
Buyers and Store managers estimate what they can achieve

Operation managers must be involved in objective setting process

Productivity Measures

Input Measures – assess the amount of resources or money used by the retailer to achieve outputs such as sales

Output measures – asses the results of a retailer's investment decisions

Productivity measure – determines how effectively retailers use their resource – what return (e.g., profits) they get on their investments (e.g., expenses)

Financial Performance of Retailers

Outputs – Performance

- **Sales**
- **Profits**
- **Cash flow**
- **Growth in sales, profits**
- **Same store sales growth**

Inputs Used by Retailers

- Inventory ($)
- Real Estate (sq. ft.)
- Employees (#)
- **Overhead (Corporate Staff and Expenses)**
- **Advertising**
- **Energy Costs**
- **MIS expenses**

Productivity: Outputs/Input

- **Corporate Level**
  - **ROA = Profits/Assets**
  - **Comparable store sales growth (same-store sales growth)**
- **Buyers (Inventory, Pricing, Advertising)**
  - **Gross Margin % = Gross Margin/Sales**
  - **Inv Turnover = COGS/ Avg. Inventory (cost)**
  - **GMROI = Gross Margin/Average Inventory**
  - **Advertising as % of sales**
- **Stores (Real Estate, Employees)**
  - **Sales/Square Feet**
  - **Sales/Employee**
  - **inv. Shrinkage/sales**
  - **Average Transaction (sales/# of transactions)**
  - **Items Per Ticket (total items sold/total transactions)**
  - **Conversion Rate (total transactions/total traffic)**

Level of Organization	Output	Input	Productivity (output/input)
Corporate (measures for entire corporation)	Net sales Net profits Growth in sales, profits, comparable store sales	Square feet of store space Number of employees Inventory Advertising expenditures	Return on assets Asset turnover Sales per employee Sales per square foot
Merchandise management (measures for a merchandise category)	Net sales Gross margin Growth in sales	Inventory level Markdowns Advertising expenses Cost of merchandise	Gross margin return on investment (GMROI) Inventory turnover Advertising as a percentage of sales* Markdown as a percentage of sales*
Store operations (measures for a store or department within a store)	Net sales Gross margin Growth in sales	Square feet of selling areas Expenses for utilities Number of sales associates	Net sales per square foot Net sales per sales associate or per selling hour Utility expenses as a percentage of sales* Inventory shrinkage*

*These productivity measures are commonly expressed as an input/output ratio.

Evaluating Financial Performance

- Growth in Stockholder Value – Stock Price
  - Accounting Measures – ROA (Risk adjusted)
- Benchmark
  - Improvement Over Time
    - Compare performance indicator for three years
  - Performance Relative to Comparable Firms
    - Compare performance indicators with major competitors for one year, most recent

Sources of Information

- Balance Sheet (Snap Shot at One Time)
  - Asset Management
- Income Statement (Summary Over Time)
  - Margin Management
- Annual Reports/ SEC Filings
  - http://www.sec.gov/edgar/searchedgar/companysearch.html

Evaluating Investment Opportunities

- ROI – Discounted Cash Flow
  - Considers time value of money, cost of capital
- Breakeven Analysis
  - How much do we have to sell to breakeven (recover investment)?

Income Statement

Net Sales	**$ 1,000,000**	
COGS	**800,000**	**80%**
Gross Margin	**200,000**	**20%**
Operating Expenses		
Variable	**100,000**	**10%**
Fixed	**80,000**	**8%**
Profit	**20,000**	**2%**

Variable and Fixed Operating Expenses

	Variable	Fixed
Wages & Salaries		
Manager	**20,000**	**20,000**
Salespeople	**60,000**	**20,000**
Clerical	**20,000**	**10,000**
Rent		**20,000**
Maintenance		**10,000**
Total	**100,000**	**80,000**

Break Even Analysis

Profit = Sales - COGS-Var Cost - Fixed Cost

0 = Sales - COGs% x Sales - VC% x Sales - FC

Break-even Sales x (1-COGS% -VC%) = FC

Break-even Sales = FC/(1-COGS% -VC%)

Break-even Sales = FC/(GM%-VC%)

= $80,000/(.2-.1)

= $800,000

Three Business Decisions
Is the Breakeven Going to Increase or Decrease?

1. Breakeven Sales if Retailer Moves To New Location with Rent = $50,000 Fixed

2. Breakeven Sales if Retailer Reduces Prices By 5%

3. Sales if Retailer want to make a profit of $100,000

Break-even Sales = FC/(GM%-VC%)

Breakeven Sales if Retailer Moves To New Location with Rent = $50,000 Fixed

=(60,000+50,000)/(.2-.1) = $1,100,000

Breakeven Sales if Retailer Reduces Prices By 5%

Sales if Retailer want to make a profit of $100,000

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Break-even Sales = FC/(GM%-VC%)

- Breakeven Sales if Retailer Moves To New Location with Rent = $50,000 Fixed

=(80,000+30,000)/(.2-.1) = $1,100,000

- Breakeven Sales if Retailer Reduces Prices By 5%

= 80,000/(.15-.10) = 1,600,000

- Sales if Retailer want to make a profit of $100,000

=(80,000+100,000)/(.2-.1) = 1,800,000

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