TRENDS + SUMMARIES

Are Category Killers Still Killers?

One of the fundamental tenets of McMillan|Doolittle's "EST" Theory of Retailing is that retailers can win by being "Best" on at least one of four key elements:

- **Cheapest.** *Having the lowest prices. This is almost always accompanied by having the lowest costs. Wal-Mart has done pretty well here.*
- **Hottest.** *Winning by offering the latest products just as customers begin to buy them in volume. The Gap, Starbucks and Crate & Barrel are all examples of companies who win by being Hot.*
- **Easiest.** *Excelling with outstanding customer service. Companies who win here include Nordstrom and Saturn. Recently, we broke Easiest into another dimension,* ***Quickest.*** *Quickest companies work to remove all shopping barriers and help customers get their tasks done fast. Quickest companies include McDonald's & Walgreens.*
- **Biggest.** *These companies win by offering dominant assortments in a particular category of merchandise. They have also been called "category killers" because they dominate what ever category they participate in. Wall Street has also nicknamed these companies "Big Box Retailers," for obvious reasons. They helped fuel an enormous boom in power center retailing.*

Is Biggest Still a Valid "EST"?

This theory has held up very well for many years. In fact, it was the most straightforward "EST" of all: just offer more merchandise than anyone else in a meaningful category and you will win. However, over the past few years, we have seen some disturbing trends in this category:

- *Toys "R" Us still has more toys than anyone else, so why are they struggling?*
- *PetsMart went from stock market darling to a troubled company without any change in their Biggest strategy.*
- *Sports Authority (or any other big box sporting goods retailer, for that matter) is also suffering.*

There are plenty of examples in other categories as well. The computer superstores are far from healthy and automotive superstores are not as compelling as they once were.

We also seem to be running out of new categories to kill — there have not been many "new" category killers in recent years and the tried and true formula is definitely under attack.

What's Happening Now?

As in any discussion, the issues are not always black and white. Many of the companies that have struggled have also suffered from poor execution, competitive threats or simply took their eye off their customers.

However, we see a fundamental shift in customer purchasing habits that requires significant change in how a category killer must behave:

- **Continued time pressure.** *We think it is more than a coincidence that the growth of Quickest retailers seems to correspond with the decline of some of the Biggest competitors. PetCo, as an example, surrounds PetsMart stores with many more locations. Do they have as much merchandise? No. Do they have what most customers need? Absolutely. Plus they are quicker and easier to shop.*
- **One-stop shopping and the "Wal-Mart Effect".** *We have resisted (rejected, really) the notion of one-stop shopping for several reasons: It is an overused phrase voiced by retailers who offer lousy assortments of convenience product under the guise of a one-stop shop; and to truly be an authoritative one-stop shop your store had better be very big. Meijer, the most successful supercenter, builds stores that are 240,000 square feet & they are still not authorities in all categories.*

  However, discount stores have done an extremely credible job of offering respectable assortments in a number of categories. Most, as an example, have very good toy departments. Not as good as Toys "R" Us, but extremely representative and often selling at lower prices.

  The effect of Wal-Mart, Target and Kmart can be felt in nearly every merchandise category by almost every retailer. They are highly skilled merchants and simply too big to be ignored.
- **Micro Killers.** *Category killers also tend to be generalists. They reach for the broad middle of the market by*

offering good assortments in many areas. This leaves them vulnerable to micro killers, specialists who can carve out a narrower niche. Zany Brainy takes a chunk of the educational toy market from Toys "R" Us. FAO Schwarz goes after fashion. In a similar vein, golf specialty stores like Golf Galaxy and outdoor specialists like Bass Pro and Cabela's take on various categories of the general sporting goods stores.

- **"E"tailing.** *Remember, we don't believe that e-commerce is taking over the world anytime soon. However, these companies could further skim the cream off the top of many categories in the future.*

Biggest is Not Enough

For these reasons (and others) we conclude that a retailer can no longer win by just being Biggest. And, perhaps they never did. The reality of "EST" has always been that you must own one dimension and be at least very good at one or more of the others. Toys "R" Us has always been Biggest, but at one time they were also Hottest. Who else did they have to compete against?

While big selection will continue to be a powerful driver, it needs to be accompanied by something more. Piling out lots of stuff simply won't win anymore.

- **The right products versus more products.** *With less time, customers want more help from retailers. More products can actually be a negative, making the shopping experience harder than it needs to be. Incredible Universe did not win by offering three times as many TVs as Circuit City. They reached the law of diminishing returns very quickly and did not provide any other meaningful benefits to customers. Retailers must be trusted "merchants," pre-selecting the right products for customers. In some sub-categories, that may still mean lots of choices; in others it calls for carefully edited assortments.*
- **Solutions versus "stuff."** *Category killers have organized themselves for their own efficiency, not necessarily the customer's. Solution selling helps customers by providing a total solution, not just an endless series of products. Home Depot demonstrates solutions or ideas on nearly every endcap in the store. Retailers like Pottery Barn and Restoration Hardware continually cross traditional product boundaries to provide integrated solutions — selling complete solutions instead of a single product.*
- **Expanded purpose.** *There are still many examples of successful Biggest retailers. But, they have changed considerably over time. Office supply stores began as typical category killers — pens, folders and paper displayed in neat aisles. They have evolved into solution stores for small business/ home office customers. Along with traditional supplies, they now offer comprehensive printing services and large selections of office needs such as furniture and electronics. Home Depot also continues to evolve, offering more and more solutions to an expanding range of customers. Note their floor covering department, in terms of both the greatly expanded range of products they offer and their comprehensive installation services. Not only are they moving toward more solutions, they are also expanding their base to reach more "Do It For Me" customers.*
- **Lifestyle needs.** *As big as Barnes & Noble and Borders stores are, their assortments are tiny compared to Amazon.com, just a click away. But, as Amazon will find out (and tries to respond to in an e-commerce way), Biggest alone won't cut it. Barnes & Noble offers fashion, provides customers with ideas and information, and also acts as a social meeting place. There is a lot of Hottest in these stores, along with a lot of books.*

It's Time to Up Your "EST" Dimensions

If you're a category killer, think hard about how you can continue to win. More products probably won't be the answer. Biggest stores better excel on more than one "EST" dimension.

Customers are changing. Biggest retailers better begin changing too.

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