The Next Normal: Outlook for Australian Retail in 2022

February 2022
Since the formal declaration of COVID-19 as a pandemic in March 2020, consumers, businesses, and entire industries have grown accustomed to “disruption” as a normalised state of affairs. Australia has been no exception to this rule, and retail as a sector has grappled with a particularly challenging operating environment.

Australian retailers have needed to swiftly respond to evolving consumer behaviour and preferences, disrupted and unpredictable supply chains, shifting operating models, organisational gaps and talent shortages, and inflationary cost challenges, among several more topics.

As we commence 2022 in earnest, our goals in writing this perspective are twofold: (1) to share BCG’s insights on retail-specific trends that will serve to inform the ‘next normal’ and (2) outline the key strategic and operating implications that follow for our clients.

This perspective document only scratches the surface of the trends that are currently unfolding, and how businesses can successfully position for comparative advantage. We would welcome the opportunity to unpack the trends and strategic implications in conversation, together with your leadership team.

**Australian Retail in 2022 | Key sector trends**

Like other industries, retail in Australia is being hit by a confluence of factors that continue to shift as new COVID variants emerge and in turn consumers, markets and regulators respond.

Despite this volatility, BCG posits that seven key trends will serve to structurally shift (or in some cases continue to shift) the retail landscape in 2022, which are critical for our clients to understand. Refer to exhibit 1 for the full trend overview.

1. **New Consumer behaviours post COVID-19 will stick.**

COVID-19 has created many new consumer purchasing behaviours, and in several instances accelerated and cemented the adoption of existing behaviours by 2-4 years (e.g. online share of total retail sales in Australia have reached 15%, which was accelerated by 3 years). We maintain that whilst the pandemic structurally forced adjustments to consumer behaviour, these new behaviours will continue to persist even as the challenges of COVID-19 subside.

Here are a select few consumer behaviours we expect will persist strongly in 2022 (and beyond):

- **Fewer trips, bigger baskets:** Lockdowns, restrictions and general safety concerns migrated customers to...
fewer top-up trips and larger overall baskets (+8-15% bigger baskets on average across retail subsectors), with pronounced impacts to grocery.

- **Accelerated and expanded online**: eCommerce transactions as a share of total retail sales were already reaching up to 10% in Australia pre-COVID, but adoption has increased to 15% as of 2021. This phenomenon is expected to continue as more first-time digital buyers join the segment (+22%) and a large portion of existing customers (+88%) are buying more products across expanded categories online.

- **A greater focus on health (and many more category winners and losers)**: As the pandemic shifted health and wellness to the forefront of consumer minds, the willingness to spend on holistic wellbeing (across products and services) is expected to significantly increase in Australia; with >20% of Australians looking to expand spending to enhance wellness (including using accumulated savings). For a full list of expanding and contracting categories based up BCG’s Australian Consumer Sentiment Snapshot #5, please see exhibit 2.

2. **Personalisation will become ‘table-stakes’ within three years.**

Personalisation has been a pervasive topic in retail boardrooms and leadership teams for the past three years or more. However, we have observed a significant acceleration on consumer expectations for simplified, clear, excellent value personalisation offers and communication over the past 24 months.

Digital advertising has grown to a $10B+ industry in Australia, and the proliferation of information and mass-market advertising has heightened consumer frustration and lowered overall engagement with content.

In this context, leading retailers are already 12-24 months into the personalisation journey – as shown in exhibit 3 - with an end-state capability that allows for dynamic, targeted 1:1 offers, experience and communication with consumers – including such capabilities as personalised content and offers, dynamic pricing and promotions, advanced customer insights and identifiers, and real-time range curation. The requirement to invest has become more urgent, with 75% of customers now expecting retailers to understand their individual needs and expectations.

In 2022, the gap between innovative retailers and laggards will widen quickly. In fact, 80%+ of BCG’s transformation efforts in Australia today have a focus on digital and customer (incl. of personalisation use cases).

### Exhibit 3 – Retailers are typically 12–24 months into the personalisation journey

**Average 2-3% revenue lift**

**Starting Personalisation**

**Average 5% revenue lift**

**Developing basic personalisation capabilities**

**Average 10% revenue lift**

**Scaling Advanced personalisation capabilities**

**Average 15-20% revenue lift**

**Delivering highly connected experiences**

### Exhibit 4 – Omni-channel proposition and seamless transacting becoming the norm

<table>
<thead>
<tr>
<th>Industry adoption</th>
<th>Click and collect</th>
<th>Return to store</th>
<th>Stock info online</th>
<th>Virtual aisle/order &gt;store</th>
<th>Self check-out/digital invoice</th>
<th>Omni-CRM/ clienteling</th>
<th>Click and reserve</th>
</tr>
</thead>
<tbody>
<tr>
<td>55-60%</td>
<td>50-55%</td>
<td>35%</td>
<td>~30%</td>
<td>~30%</td>
<td>20-40%</td>
<td>~20%</td>
<td></td>
</tr>
</tbody>
</table>

**Where adoption is ‘up to date technology in place’ or ‘started but not finished major upgrade’**


### Exhibit 2 – Post-COVID winners and losers

<table>
<thead>
<tr>
<th>Top 10 category winners</th>
<th>Top 10 category losers</th>
</tr>
</thead>
<tbody>
<tr>
<td>Appliances</td>
<td>Alcohol</td>
</tr>
<tr>
<td>Cars</td>
<td>Apps &amp; video games</td>
</tr>
<tr>
<td>Cosmetics/makeup</td>
<td>Business travel</td>
</tr>
<tr>
<td>Fresh meat, fruit and vegetables</td>
<td>Carbonated soft drinks</td>
</tr>
<tr>
<td>Health and fitness activities</td>
<td>Chocolates/candies</td>
</tr>
<tr>
<td>Household care products</td>
<td>Direct to home services e.g., Fostel</td>
</tr>
<tr>
<td>Leisure travel</td>
<td>In-home entertainment</td>
</tr>
<tr>
<td>Spa/salons</td>
<td>Kitchen appliances</td>
</tr>
<tr>
<td>Theme parks/ Cinema</td>
<td>Luxury goods, jewelry, handbags</td>
</tr>
<tr>
<td>Women’s clothing</td>
<td>Tobacco</td>
</tr>
</tbody>
</table>

Source: Australian Consumer Sentiment Snapshot #5, December 2020; 2021 Q1 – (AUS AUS, unweighted, representative within 3% of census or market demographics)
As omnichannel scales rapidly, we can expect significant flow on effects to the role, format and size of bricks and mortar stores, expanded abilities to leverage deep customer data, and significant reconfiguration of supply chains to cater to channel shifts.

4. ESG agendas will increase in urgency and levels of investment.

ESG agendas will be critically important in 2022, as the pandemic continues, climate predictions gain greater awareness and corporate Net Zero commitments expand in scale.

Australian consumers have increased vocal support for making a positive impact to people and our environment, and >80% convey their willingness to reduce consumption to help tackle climate change and >10% are willing to pay more (see exhibit 5).

The increased discourse on ESG, however, should be approached with a measured strategy. The translation from principled alignment to sustainable consumption into greater willingness to pay is as yet not fully proven, and investments into ESG initiatives (e.g. sustainable packaging) should be measured and staged. It will also be critical to understand core customer segments more deeply, for example ESG initiatives align much more strongly with millennials in Australia, and for repeat purchases segments such as grocery.

5. Rising costs and inflation will drive operating pressures in 2022.

We are already observing rising costs and inflationary pressures in Australia, and this is expected to be a continued theme throughout 2022: Headline inflation in the December 2021 quarter was 3.5%, compared to Australia’s 10-year average inflation of 1.9% (see exhibit 6). While this is a moderate rise compared to the 6.9% (annual) increase experienced in the United States, we can expect this to create significant pressure across retail value chains.

Retailers have grappled with increased shipping costs as overseas container prices have quadrupled in the last 12 months. While we see supply chain costs gradually unwinding as supply and demand imbalances are corrected, we expect shipping costs to remain elevated for most of 2022.

The pandemic has also magnified supply issues, and in turn, supply imbalances. As a result, certain pockets have been impacted by cost pressures, with retailers also burdened by increased raw ingredient and commodity costs. As an example, red meat prices have increased by more than 10% in the September 2021 quarter, and shortages in wooden pallets and aluminium have put price pressure on soft drinks.

6. Supply chain disruptions will persist and drive challenges across the value chain.

The COVID-19 pandemic has triggered significant and widespread supply chain disruptions. These disruptions have been caused by a combination of factors including port congestion, limitations in cargo space, container and pallet shortages, and labour constraints. Service levels have decreased across the entire value chain, with a decrease of up to 7pp on shelf availability at the peak of the pandemic.

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Both structural and cyclical supply chain disruptions will endure in 2022.

- **On-shelf availability** – Service levels will continue to be challenged, driven by logistics delays and workforce shortages. In 2022, the Omicron outbreak has already resulted in up to 50% of labour shortages for some of Australia’s largest logistics businesses. This created a significant spike in out-of-stocks for retailers across Australia.
- **Working capital** – Inventory and working capital may continue to fluctuate given unexpected demand shifts and supply constraints along the value chain. During COVID-19, inventory fluctuated by more than 10% for many players in the value chain, which has had ripple effects upon retailers.
- **Supply chain complexity** – Supply chains are expected to experience added complexity as e-commerce continues to accelerate in 2022, and retailers will need to diversify their supply base to meet evolved consumer needs.

7. The race to attract and retain top retail talent continues.

In Australia, COVID-19 has rapidly evolved the workplace, expectations on Employee Value Proposition (EVP) and the relative bargaining power between employers / employees. In 2022, Australian retailers will struggle to attract and retain the best talent, with pronounced challenges in key roles (for example, data scientists and category managers).

Getting the EVP right in 2022 will be essential. Our experience shows that new EVPs must accommodate for and prioritise newly emerging employee preferences (see exhibit 7).

- Other factors matter beyond just compensation: 92% of employees want flexible arrangements in when they work, and 76% for where they work.
- Employees miss their colleagues and in-person activities: 28% of employees miss informal and social interactions, while 23% miss in-person collaboration and brainstorming.
- Employers can gain trust going forward: Over 20% of Australians state the top ways to regain trust are stability and security, good communication, and in-person formal meetings with colleagues.
Implications for Australian Retail in 2022

We expect 2022 will shape up to be a year of continued disruptions resulting in a host of challenges as well as fantastic opportunities for Australian retailers. As we look ahead, it is important that retailers prepare for the ‘next normal’, think boldly, continuously innovate, and look ahead, it is important that retailers prepare for the fantastic opportunities for Australian retailers. As we expect 2022 will shape up to be a year of continued disruptions resulting in a host of challenges as well as

Naturally, every retailer will face a unique set of strategic, operating and financial questions it must address. However, we posit there are three core topics that it will be critical for all retailers to consider and respond to during 2022: (1) becoming an advanced analytics-led organisation, (2) building a refreshed, customer-led offer and (3) developing a resilient operating model for the future as viewed in exhibit 8.

The AA investment can unlock significant benefits of 10-15%+ sales uplift, 500bps+ margin expansion, 5-10% labour savings (and redeployment), and 15-20%+ increase in supply chain efficiencies. This is compounded further when AA use cases are unlocked across the full value chain: customer experience, category management, upstream operations and in-store execution.

Customer-led offer reset

Customer preferences have evolved much faster than typical BAU assortment review and product development cycles. As a result, many retailers are out of sync with the latest preferences, category winners and losers and they are yet to reset category management fundamentals (e.g. pricing strategies) in response to the shift.

As retailers consider this imperative, we believe there are three core components that require addressing (1) getting the core offer right, (2) building a clear omnichannel proposition that gets products and services to customers, and (3) making and keeping clear customer ‘promises’ as seen in exhibit 10.

Exhibit 8 - Three pillars for focus in 2022

Exhibit 9 – Start small and iterate as a world class analytics-powered retailer

World class analytics

Over the past 3-5 years, Advanced Analytics (AA) solutions have scaled and developed considerably to provide greater processing power, storage, and more mature predictive insight technologies. Together with heightened Consumer expectations and increased eCommerce transacting, this creates the right breeding ground for rapid innovation and capability build.

Leading retailers (globally and locally) have begun investing with urgency into digital transformations, and we are seeing this first-hand with our client partners. At this stage, this is no longer the territory of ‘first movers’ but becoming a table stakes investment into future-proofing the business.

As the AA journey requires significant capital and capability builds, the way to ‘win’ is to start small and iterate. It will be critical to galvanise the organisation around AA becoming central to how decisions are made, and to develop a very deliberate sequence of use cases (aka programmatic efforts) that helps to fund the journey and unlock priority customer outcomes as shown in exhibit 9.

Exhibit 7 - Employees rank compensation and flexibility as most important

Source: BCG experience; Andreas Lundmark

Exhibit 9

Assemble cross-functional squads; • Develop program & capability build roadmap • Define strategy and ambition

Baseline existing digital initiatives

Kickstart delivery with 1 high value use case to deliver fast

Assemble cross-functional squads; establish governance, structure

Define strategy

Develop program & capability build roadmap

Buildling momentum

Scaling up

End-state

Starting point

Digital maturity

Op model of the future

Customer promises

Customer-led offer reset

Channel proposition

Right core offer

Cost leadership

Supply chain resilience

Right talent and capabilities

World class analytics

Priority use cases

Future tech stack

Sustainable capability build

Channel proposition

Right core offer

Cost leadership

Supply chain resilience

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Lastly, it is important to consider the long-term consequences of the current market conditions. In the short term, companies must focus on the following areas:

1. **Cost leadership and holistic operating model**: This involves reducing costs across the board, investing in lean operations, and optimizing processes. It also includes focusing on cost leadership, particularly for Goods Not for Resale (GNFR).

2. **Supply chain resilience**: This area requires companies to build mission-led curated ranges across channels, investing into seamless user experiences and engaging with customers through integrated E2E operations.

3. **Right talent & capabilities**: This involves building an Advanced Analytics-led organization, building supply chain resilience, and expanding omnichannel offerings.

Operating model of the future

We recommend focusing on three areas:

- **Cost leadership**: Inflationary pressures as well as capital requirements for growth agendas (e.g., advanced analytics, omnichannel propositions) require unlocking funds via cost excellence. This requires a leadership-sponsored shift in cost controls, spanning holistic vendor management programs, setting up cost review processes and analytics (e.g., on commodity prices and vendor contracts), and driving harder on procurement programs, particularly for Goods Not forResale (GNFR).

- **Supply chain resilience**: In the short term, companies can establish proactive supplier management, active risk management, and expand their contingency inventory. In the medium term, retailers can diversify their supplier base for core items with a focus on suppliers and geography. In the long term, businesses must appreciate and understand all elements of their supply chain, which is where digital supply chains become critical. Control towers – effectively an integrated dashboard of events and information across the entire supply chain – can provide visibility and help companies understand their risks and exposure levels.

- **Right talent & capabilities**: As retailers expand omnichannel offers, add more digital and AA use cases to core processes, there will be a significant impact on the requires capabilities and talent to run the new organization. This requires a rapid look now at key roles and functions that will require rebalancing – e.g. the addition of data scientists or eCommerce or user experience specialists. In a talent-constrained environment, this will require longer lead times.

Conclusion

As discussed, we believe several trends will serve to create a disruptive and dynamic environment for Australian retailers in 2022: new and sticky customer behaviours, expectations for personalisation and an omnichannel offer, increasing prominence of the ESG agenda, rising costs and inflationary pressures, persistent supply chain disruptions and a war on top retail talent.

In this context, building a strategy that is bold, favours innovation and addresses the core business profitability is essential. As discussed, we recommend focusing on the following:

- **Innovate and transform**: Electronic Product Information (EPI) and digital twins are becoming critical. These technologies can help retailers understand and manage their risks and exposure levels.

- **Build a refreshed, customer-led offer**: This involves focusing on the right omni-channel proposition, taking into account customer preferences.

- **Develop a resilient operating model for the future**: This requires capabilities and talent to run the new organization.

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