High-Shrink Store Programs: Why Focusing Your Resources on the Worst Performing Stores Will Reap the Most Benefits

Introduction: Why shrink matters

Retailers are used to managing a certain amount of shrink in the business – it's a fact of life. However, that doesn't mean that executives should accept that shrink can't be substantially reduced, particularly in an age where corporate financials are under the microscope on a regular basis. High-shrink programs, which marshal resources from all levels of the retail organization, are a key tactic in driving down shrink at outlets with the highest loss rates.

According to the 2005 National Retail Security Survey (administered by the University of Florida), retail shrink appears to be on the decline overall: Respondents reported an average shrink rate of 1.6 percent of annual sales, a slight increase from the 2004 rate of 1.54 percent – the lowest since the survey was first introduced in 1991. The average rate had been on a generally steady decline in the past several years, according to the survey.

While the reduction in shrink is a positive development for retailers, there is still a significant amount of revenue that goes out the door along with the merchandise. The 1.6 percent average translates into a $37 billion annual loss for U.S. retailers, according to the 2005 National Retail Security Survey. Even as shrink trends downward, shareholders who are demanding profitability will look closely at retailers' efforts to curb any losses.

In other words, retail executives should never become complacent about shrink or about the need to address the problem.

The presence of a comprehensive, targeted program to reduce shrink rates at stores with the highest losses will impress shareholders, vendors and other key constituents – and naturally, such a loss-prevention program offers other benefits. By focusing efforts specifically on high-shrink stores, retail companies can noticeably impact revenues or earnings per share.

One of the world's largest retailers established a high-shrink program three years ago and continues to reap the rewards. Shrink at the retailer is at an all-time low, less than half of the industry standard. These continued reductions are driven by the program's emphasis on the worst shrink stores, and holding the operations and loss-prevention teams accountable at all levels – from stores, districts and regions.

Thanks to new technology such as audit software and point-of-sale exception-based reporting, retailers may be able to more easily identify which stores are suffering from the worst shrink problems – and this may make them more inclined to address shrink.

What is a high-shrink store program?

A high-shrink store program is a loss-prevention initiative designed to focus many resources on the areas of the company where losses are highest. This targeted approach delivers the best results in a shorter period of time, compared to an overall loss-prevention program that is aimed at stores companywide. The accepted maxim in retail is that a small percentage of a retailer's stores cause a very large percentage of shrink losses – therefore, it makes sense to focus the program on these stores for maximum impact.

As part of a high-shrink store program, the top stores from a loss standpoint are identified. Corporate, district and in-store managers examine the performance of these stores to identify possible causes of shrink, pinpoint weak processes and policies that may be contributing to shrink, and initiate regular reporting and auditing to monitor improvements.

For many retailers, an outsourced high-shrink store program is most efficient. Even those companies with in-house loss-prevention programs may find it smarter to choose an outside specialist. When a high-shrink store program is managed in-house, executives must take time away from other vital functions to see the program through from start to finish. Outsourced programs don't rob resources from current company operations.

For a high-shrink store program to be successful, the coordinator of the program must have operational expertise and experience, and must be able to cultivate the right relationships within an organization. Often, the best way to achieve these results is to bring in a specialized consultancy with senior executive-level loss-prevention experience.

How do you know if your company needs a high-shrink store program?

The most compelling reasons to implement a high-shrink store program revolve around profitability. The process starts by compiling a list of stores and their shrink rates, with the highest rates at the top of the list. In general, executives will see that a large portion of shrink – often at least 30 percent – is represented by the top 5 percent to 10 percent of all stores.

Using modeling tools, analysts should examine the benefits of reducing shrink by given amounts – for instance, 10 percent or 20 percent – on profits and on earnings per share, if applicable. These "what if" scenarios can help retailers decide if the cost and time necessary to implement a high-shrink store program will offer adequate benefits. The more dramatic the impact of reducing shrink, the greater the arguments for implementing a high-shrink store program.

Analysts and managers also should consider the causes of shrink (assuming that they are known and understood), in order to decide if a shrink program can solve these problems. For instance, shrink rates are traditionally higher at stores in major metropolitan and/or urban areas – so, to some extent, higher-than-average losses are expected at these outlets.

However, an important part of a well-defined shrink program involves looking beyond the assumptions about why losses occur. Analysts can help managers look at high-loss stores in order to find other, solvable reasons for shrink – such as weak policies or lack of training for employees.

It's also important to examine the performance of management within high-shrink stores, and the performance of district managers. If poor performance is apparent (for instance, via reviews or anecdotal information), then in theory, that performance should be improved by a program that addresses the weak links in management.

Analysts should consider whether managers can obtain buy-in on a high-shrink program from store managers and store personnel, since their participation is essential to the program's success. Finally, the program's owners should determine whether corporate managers can provide high-shrink stores with the support they need – for example, training – to follow through on the program.

As part of its high-shrink store program, a major U.S. apparel retailer conducts shrink strategy meetings at each of its targeted stores with local personnel in order to develop tactics, address staff commitments and work on an action plan for reducing shrink. The corporate shrink committee also meets monthly to discuss store performance. In two years, the company has reduced shrink in its targeted stores by 25 percent, and "graduates" stores off of the program on a regular basis.

By carefully considering all of the above business issues, retailers can make a sound decision about the benefits, and potential for success, of a high-shrink store program.

What are the benefits of implementing a high-shrink store program?

Addressing the problem of shrink via a high-shrink store program offers an organized, methodical approach to reducing losses. By examining loss statistics, identifying causes of shrink, and implementing policy and process changes to reduce opportunities for loss, retailers stand the best chance of lowering shrink rates. Besides the obvious improvement in revenue numbers, there are other benefits associated with these programs:

- A high-shrink store program helps define roles and responsibilities for everyone from store employees to corporate managers, making it easier for staff at all levels to take part in the program's success. Having clearly defined roles also makes it possible to audit performance of key players in the program, ensuring that benchmarks are met.
- The presence of a program should help retailers reduce shrink rates over a shorter time period than if no program existed.
- The public establishment of a program will spur store managers and employees to succeed and reduce losses. When managers and employees know that their performance is being monitored, and must deliver progress reports on a regular basis, they are encouraged to meet their individual goals.
- Having a high-shrink store program may allow managers to argue for (and get) more capital funds for improvements, such as Closed Circuit Television (CCTV), Electronic Article Surveillance systems (EAS), pre-employment screening tools or better training, which may help further reduce the shrink rate.

Who should be involved in the program?

The success of a high-shrink store program is very much dependent on the involvement of employees at all levels of the retail organization. When people at every level are stakeholders in the program, they have added incentive to change the status quo. In addition, if they are aware that personnel from top to bottom are watching high-shrink stores, stakeholders will want to succeed – rather than fail – publicly.

At the aforementioned U.S. apparel retailer, the high-shrink store program is considered a success in part because of its high profile within the organization. The retailer's corporate shrink committee includes the company's loss-prevention director, operations director, and top merchandise and retail executives.

At the store and regional level, the program should include employees and managers of high-shrink stores, local human resources staff, and district managers and loss-prevention staff. At the corporate level, the program would include human resources executives, managers of any existing loss-prevention program, and executives with direct-line responsibility for the high-shrink stores, from operations to finance.

Questions to ask before launching a high-shrink store program

As a high-shrink store program begins to take shape, managers and business analysts should consider the following questions to help define and direct the program:

What are the criteria that will represent a high-shrink store?

Managers should decide how they will identify the stores that will be targeted in the high-shrink store program. For instance, they might examine shrink as a percentage of overall sales revenues, as well as historical data that would indicate percentage change in loss from year to year at each location.

How many stores should be included in the program?

Managers need to consider the number of stores that they can comfortably address within a high-shrink store program without sacrificing resources needed for other locations. If an outside loss-prevention consultant is chosen, the program can ensure the right number of stores is selected that can be managed effectively, and help ensure the desired outcome is achieved.

What are the roles and responsibilities for each level of an organization?

As mentioned above, defining the roles of everyone who is participating in the program will make it easier to reach goals and monitor results. Thought should be given to the responsibilities for everyone who has a stake in the program.

What tools will help participants keep track of the program?

Managers may want to develop a workbook, including shrink analysis and an action item template, for each target store, and customize the workbook to the needs of that particular store.

What paperwork do corporate and store managers need to review on a daily/weekly basis?

Sales records that are not normally reviewed at regular intervals may be valuable in understanding where and why shrink is occurring.

What policies and processes should be reviewed as part of the program?

For instance, since refunds, voids and merchandise credits can be a source of shrink, managers may consider reviewing the processes by which refunds and credits are approved, in order to close any loopholes that allow shrink to occur.

Do you need to create a store shrink committee? Who should be part of it?

An in-store committee can help foster a sense of teamwork among associates and managers who are taking part in the program. It also can help boost morale at stores that may need to create an empowering environment for employees.

Should higher standards for merchandise security be established?

Managers may want to examine methods for making merchandise less susceptible to loss – for example, tagging theft-prone items or installing CCTV systems.

Should store managers' personnel reviews be impacted by results of the program?

Managers can be rewarded when losses are reduced, and their reviews can be tied directly to store performance.

Should field managers have greater presence in high-shrink stores?

A successful high-shrink store program should include greater management involvement, such as planning for how often district managers will visit, who they will meet with, and the possibility corporate managers may need to make additional visits.

If results improve, should employees or managers be paid bonuses, or rewarded in some other way?

Executives in charge of the high-shrink store program should discuss incentive compensation for managers and employees who are directly involved in loss-reduction activities.

Are pre-employment screening standards in place at high-shrink stores?

Store and HR managers should address the value of pre-employment screenings, including drug testing and criminal background checks, in order to lessen the likelihood of loss from poor hires.

Does everyone "feel the heat" – i.e., will district and corporate managers, as well as store employees, be held responsible for results?

Store managers should not feel that they are the only employees who will be held accountable for shrink.

Is the corporate office open to providing more resources to high-shrink stores?

The ability of corporate managers to direct training, capital improvement funds and other benefits to high-shrink stores can be a factor in the success of the program.

Conclusion

A carefully planned and managed high-shrink store program can increase the impact of an overall loss-prevention program, and accomplish what an overall loss-prevention program cannot: It can drive results by focusing many resources on a concentrated group of stores.

High-shrink store programs draw stakeholders at every level – from corporate managers to store associates – into the program, raising the odds for success. With buy-in from every part of the retail organization, managers and associates can play a role in reducing losses, and have a clear idea of their roles within the program.

Even when outside influences – such as urban environments – contribute to high-shrink rates, there is much that can be done to reduce or eliminate many causes of retail loss. For the retailer who is carefully allocating corporate resources, hiring a consultant to develop and manage the high-shrink store program can reach stated goals more efficiently and in a much shorter time frame.

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