**Shrinking Shrink:**

**Best Practices for Managing Shrink**

**Contents**

**SHRINKING SHRINK**

Shrink is a daunting problem for retailers and suppliers alike.  According to a recent National Retail Security Survey, shrink costs the retail industry about $31 billion annually.  For some retailers, shrink accounts for a staggering 20% of operating profits.  In an industry where profitability hinges on a few cents per dollar, every penny makes a difference.

The thing is … shrink hasn't gotten any better over the last several years.  In fact, according to the 2006 National Retail Research Group's study on shrink, 84% of retailers say that shrink has either increased or stayed the same over the last two years.  The irony is that 68% of shrink is caused by a breakdown in operational best practices and could be prevented with a pre-emptive shrink initiative.

**SO WHAT IS SHRINK EXACTLY?**

Several industry experts have described shrink as "the difference between the retail value of product received versus the amount received for that product at the time of its sale" … or, "whatever number you have on YOUR store operating statement."  Park City Group describes shrink as: the loss of product due to theft, fraud, error, and faulty processes … and possibly the last free money on the table for the hard-pressed retail industry.

**WHERE DOES SHRINK COME FROM?**

When the National Retail Research Group conducted its 2006 study on supermarket shrink, over 100 retailers responded.  Each retailer had an average of 148 stores; with annual store sales of $22 million; and 100 employees, 40 of whom are cashiers. Average shrink was 2.76%, resulting in over $608,000 in losses.

According to the survey, shrink comes from the following areas:

| | |
|---|---|
| Employee theft | 56% |
| Shoplifting | 21% |
| Receiving | 10% |
| Retail Pricing | 5% |
| Accounting/Admin | 4% |
| Damaged goods | 4% |

**MANAGING SHRINK**

But take heart … the news isn't all bad.  The key to managing shrink is a combination of employee awareness and training, industry best practices, and the use of technology.

**Employees**

Hiring honest employees can reduce shrink by 13%.  Things like background checks, previous employment verification, and written integrity surveys help ensure a more honest employee.  Employee

training – and openly discussing preventative initiatives – can lower shrink by over 20%.  The more employees and managers are aware of shrink and the company's policy toward loss prevention, the higher the impact (in a positive direction) on shrink.

**Best Practices**

The National Retail Research Group has outlined nine best practices to help control shrink.  Each item is described in greater detail in the chart that follows.

1. Start with a smart order
2. Practice the "Rule of 3"  (order what can be sold in 3 days)
3. Turn over your inventory storage
4. Display space allocation
5. Product handling
6. Sanitation & Refrigeration
7. Manage your physical inventory
8. Product ID and scan file management
9. Check Out Operations


**Technology**

Park City Group isn't really equipped to help with employee awareness, but we do have technology solutions that support and enable the best practices outlined above.  The proper use of technology – including POS data mining, exception reporting, and performance scorecards – can reduce shrink by 18 to 20%.

**Store Level Replenishment (SLR):**
Park City Group's Store Level Replenishment (SLR) solution will increase your effectiveness at the store shelf, reduce out of stocks, and help lower shrink.  How?  By using POS data to create accurate forecasts and spot-on replenishment plans for regular turn and promotion products – by item by store.  This solution consists of a powerful forecasting engine, an inventory planner, and replenishment ordering logic.

**Scan Based Trading (SBT):**
A commerce model where the supplier owns the inventory until it scans at the point of sale, Park City Group's SBT solution provides visibility into store-level product movement, allows suppliers to spend more time merchandising product, and removes time-consuming operational drudgery from the retailer-supplier relationship. In most SBT relationships, retailers and suppliers share shrink.  So shrink control – and its costs – are critical to a successful SBT program.

**Visibility & Analytics (V&A):**
Park City Group's V&A suite is a web-based business intelligence tool that utilizes daily store-level data, as well as information from other enterprise applications, to create visibility into and analyze data around shrink trends, sales performance, inventory levels, and trading partner performance (scorecarding).  V&A also helps to identify root causes and highlights problems that need to be addressed.

# A SOLUTION THAT FITS

The following chart gives you an "at-a-glance" look at the nine best practices for managing shrink, and how Park City Group can help.

| BEST PRACTICE | HOW PARK CITY GROUP HELPS | | |
| --- | --- | --- | --- |
| | SLR | SBT | V&A |
| **Start with a smart order.** Writing a smart, well conceived order to meet anticipated sales and display requirements is key to optimizing sales, minimizing shrink, and assuring customer satisfaction.  SELL THROUGH = LOWER SHRINK! | Better manage your inventory by ordering what you need, based on daily monitoring of store level activity. | Get visibility into real-time consumer demand through the capture of POS data – see what items are selling and which are sitting on the shelf. | The V&A Sales module compares deliveries to sales.  The inventory module provides visibility into in-store stock positions, stock position limits, and product flow. |
| **Practice the Rule of 3.** If your product is perishable, order only what you can sell in three days. | Park City Group's SLR monitors daily store-level activity, allowing you to generate a more accurate order. | SBT allows you to see spikes in POS data as they occur, allowing you to act immediately, rather than having to wait for your in-store personnel to do a physical count and adjust the next delivery. | The V&A Inventory module can identify product flow issues — are you ordering more product than you can sell in three days? |
| **Turn over storage inventory.** A tell-tail sign of a department under control is an organized, code dated storage cooler. | As part of the forecasting process, SLR considers not only what is on the shelf, but also what inventory is in storage. | With Park City Group's SBT, you can refocus labor to deliver appropriately and deal with fewer returns (or no returns!) | The V&A Shrink module analyzes shrink trends before and after you change your ordering process. |
| **Display space allocation.** Adopt and adhere to a philosophy. | With SLR, you have an accurate real-time view of store inventory, enabling you to respond quickly to over-performing items, potential stock-outs, and planogram compliance. | Use the POS data from Park City Group's SBT application to take specific action at the shelf and improve category performance. | The V&A Performance module analyzes shelf capacity and identifies overstocked or out of stock conditions based on shelf stock criteria. |
| **Product handling.** Most shrink in a perishable department can be traced to improper product handling. | If your forecasts are more accurate, you won't over-order, thereby minimizing the number of times a product has to be handled. | SBT focuses on delivering the right amount of product, limiting product handling. | Score your stores on overall shrink reduction.  Analyze data by department to drive down perishable shrink. |
| **Sanitation & Refrigeration.** Poor sanitation contaminates and poor refrigeration accelerates the product deterioration process. | Proper ordering prevents products from having to be un-refrigerated to relocate. | With SBT, partner collaboration in the refrigerated/frozen categories has lead to proactive management of refrigeration cases, for fewer shrink losses. | With Park City Group V&A tool, you can analyze, trend and rank stores, vendors and products — focusing on improving product losses by store. |
| **Manage your physical inventory.** Excess inventory is a breeding ground for shrink. Restrict backroom inventory to less than 8 – 10% of total store inventory. | Park City Group's SLR inventory planner calculates perpetual inventory on a daily basis.  Scan sales, deliveries, item counts, inventory policies and shelf capacity are all taken into consideration. | SBT facilitates improved delivery management and reduced returns, keeping inventory in check, reducing shrink, and increasing sales. | Use V&A Inventory to analyze return ratios to identify any potential ordering issues.  Use the V&A Performance module performance measures to identify trends and rank stores for improvement. |

| BEST PRACTICE | HOW PARK CITY GROUP HELPS | | |
|---|---|---|---|
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| **Product ID & Scan File Management**. When retailer and supplier item data is consistent, products are more easily tracked. | Having accurate product data is necessary to ensure the accuracy of the SLR ordering and replenishment process. | Basic item synchronization (the foundation of SBT) keeps product and scan files current and accurate. | If a product is improperly cataloged, analysis results will show an inconsistency between sales and deliveries. |
| **Check out operations.** Education of employees is critical: 11% of produce shrink occurs at checkout, where the cashier can't identify the product | Proper product scanning is important to collecting accurate POS data. | Park City Group's SBT program includes training of cashiers, along with technology that provides more accurate scans (scan eaches; for SBT-disabling quantity key/department key) | Do your sales about equal your deliveries for an optimized period? This simple analysis can open a window into other issues, such as cashier theft or consistently poor scan processes. |

**CONCLUSION**

You know the old adage … if you don't measure it, you can't manage it.  So be sure to measure shrink consistently and accurately so you always know just how big the problem is, and whether your attempts to manage shrink are effective.

By implementing excellent hiring and training programs, you can reduce the number one source of shrink – employee theft.  If you hire a better caliber of people, they will provide a better shopping experience for your customers.  And according to a Cornell/Yale retailer study, there is a direct and measurable relationship between shrink and customer satisfaction.

For those issues that aren't employee related – such as vendor fraud – leverage the appropriate technology to implement the best practices around managing shrink … such as store level replenishment and scan based trading.  And finally, use a business intelligence tool like Park City Group's Visibility & Analytics to monitor shrink and analyze your trends and performance, as well as the performance of your trading partners.

With the right programs in place, you **can** out-think shrink!

## About Park City Group

Park City Group is a trusted business solutions and services provider that enable retailers and suppliers to work collaboratively as strategic partners to reduce out-of-stocks, shrink, inventory and labor while improving profits, efficiencies, and customer service. Our innovative solutions provide trading partners a common platform on which they can capture, manage, analyze and share critical data, bringing greater visibility throughout the supply chain, and giving them the power to make better and more informed decisions. For more information, go to [www.parkcitygroup.com](www.parkcitygroup.com).