WHITE PAPER

Originally written by retail analysts from an independent, third-party consulting group based upon their analysis of return optimization business cases presented for their client base.

Retailers who have recently optimized their return transactions have increased consumer conversions while reducing fraud and abuse, resulting in increases of over 1–2% in net sales.

Optimizing the Value in Return Transactions

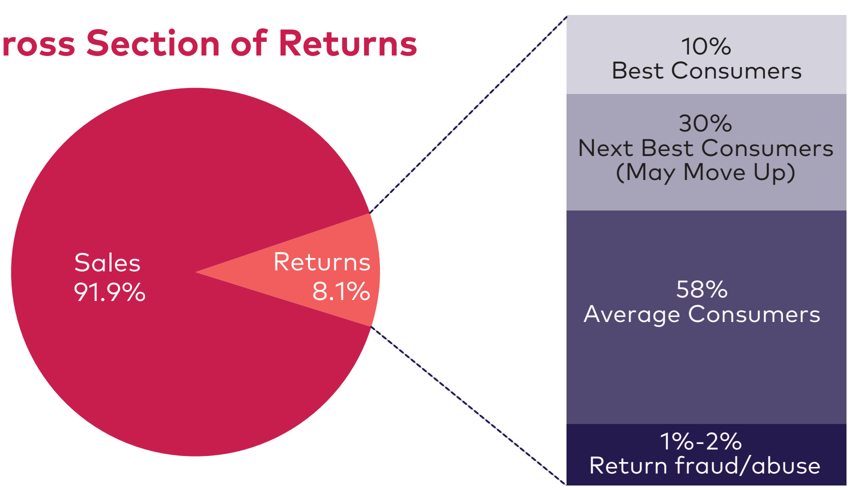
There are only so many dials that can be turned to increase sales and reduce expenses, and most have been turned at least twice already. But what about returns? Historically, return transactions have just been "a part of doing business,"—however, they can unfortunately cause BOTH a negative sales impact AND an increase in expenses. But, what if new value could be created—previously ignored in return transactions—adding new sales? Or what if fraud and abuse could be reduced without creating stricter policies that can frustrate good consumers—and still save costs by reducing return rates? What if a NEW dial could be turned? Think about it, if providing a higher level of customer service and generating both revenue and increased margin during the stressful return or exchange process could be possible, then an improved bottom line and a competitive advantage would have just been created.

Return and exchange transactions are a dark part of the retail environment—accepted out of necessity and/or customer service pressures, yet often left unexamined. Most retailers are so accustomed to seeing the returns bucket on weekly reports that they simply gloss over it, or grumble about the negative effect returns have in transforming gross sales into net. But returns hold significant promise, and we believe that the concept of Return Optimization may be one of the keys to unlocking their extraordinary value.

What Is Optimal Return Rate?

The optimal return rate occurs when a retailer creates an environment that encourages consumers to purchase with confidence yet prevents problem-atic returns. This optimal level accepts all legitimate returns and strikes the right balance between a situation that permits too many returns that lead to net losses or fraud, and a situation that allows so few returns that it limits consumers' desire to make purchases, leading to lower revenue.

Cross Section of Returns



*Percentages based on Number of Transactions

A New Perspective on Returns

Traditionally, retailers have utilized policies and procedures to manage returns and try to curb fraudulent return transactions. In the past few years, Returns Management applications, focused on receipt validation and return authorization, have been introduced to help contain the losses from returns—yet returns and return fraud and abuse continue to grow.

To compound the problem, most retailers who are trying to "manage" fraudulent returns by implementing stricter policies and procedures are often alienating good consumers and causing sales associates additional headaches as they try to enforce them. Retailers may have strong return procedures and policies in place and empowered store managers to apply discretion when processing returns, but still many have not examined the numbers that drive their stagnant or, worse yet, growing return rate. Shouldn't there be a better way to minimize fraudulent returns and ensure adherence to return policies while maximizing customer service?

"If you have not focused on managing return dollars as a method of protecting your profits, then you may be leaving money on the table . . . it was the highest and quickest capital ROI in the company."

—Paul Jones,
COO, Turning Point Justice

(commenting on implementing a solution while at Limited Brands)

Retailers already spend a lot of their time and marketing, operating, and training budgets trying to get shoppers into the store and then convert them to paying consumers. With a return, the shopper is already in the store, plus they have money to spend; why not encourage them to spend it in the store immediately? It is the perfect time for a conversion attempt.

In this age of advanced communications and technology, we believe that returns can now be examined and even exploited to further reduce the amount of red ink. Part of the awareness comes when considering that returners are a cross section of regular shoppers, including some of the best and worst consumers. The trick is to improve customer service and convert the 99% of good consumers, while still deterring return fraud and abuse. Return Optimization can provide retailers with these benefits in addition to generating new revenue.

Return Optimization is a process that tracks purchase and return histories and combines them with statistical models to discourage fraudulent and abusive return behavior, while at the same time encouraging good consumers to continue their shopping experience by issuing incentives. Traditional Returns Management solutions verify the consumer receipt for validity; however, Return Optimization goes above and beyond by also examining consumer data, trends, purchase history, and products to discourage abuse and fraud while utilizing predictive behavior and retailer-specific business objectives to generate incentives and reward thresholds.

Opportunity to Generate New Revenue

How can retailers minimize the negative impact of a return transaction? What is needed is an improved return experience—an opportunity to win consumer confidence and earn their loyalty at a critical point in the relationship. It's also a huge sales opportunity: *The shopper has cash in-hand from the recent return, so keep them in the store . . . spending!*

Here's how to convert a previously "un-convertible" return consumer:
When a good consumer returns a product, give them an incentive that rewards them if they stay in the store and spend money. The byproduct of this incentive is also a significant boost to customer satisfaction.

Fraudulent and abusive returns cost retailers approximately $17-22 billion annually, accounting for nearly 6.5% of the return dollars.

Source: Consumer Returns in the Retail Industry, NRF

Here is what happens next:
The consumer stays in the store for additional purchases, generating new sales—a 1% (or more) increase in sales!

There is no better time to retain a good consumer and ensure their ongoing patronage than when they are standing inside the store. Rewarding them says, "We apologize that the product wasn't what you wanted," and can simultaneously defuse an awkward and potentially stressful transaction. Use the return transaction to enhance the consumer relationship by offering an intelligent incentive to convert the consumer and keep the money in the store. Use Return Optimization to identify the consumer and point them back into the store with a specific promotion tailored to the consumer's and the store's needs, not just a generic discount to be redeemed anytime. Offering an intelligent discount to be applied immediately will raise retailer and customer satisfaction and create that "wow" factor which retailers and consumers continuously seek.

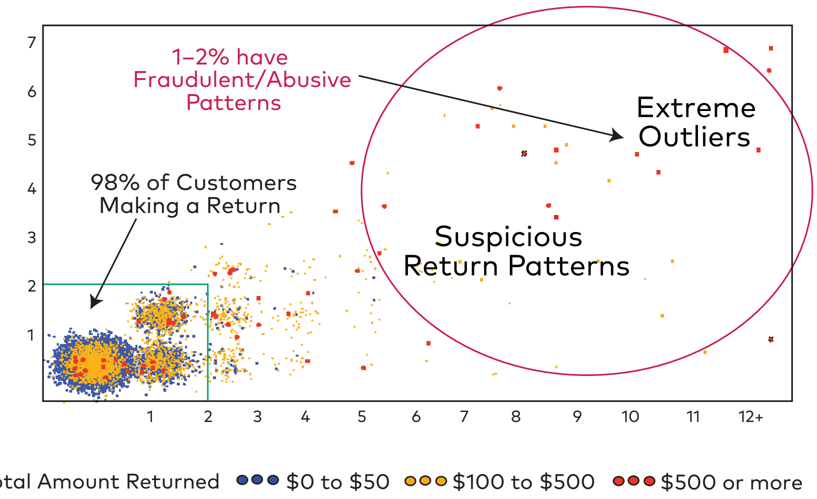
Opportunity to Reduce Fraud, Costs, and Shrink

Fraudulent and abusive returns cost retailers approximately $17–22 billion annually, accounting for nearly 6.5% of the return dollars (Source: Consumer Returns in the Retail Industry, NRF). Most retailers wrestle with return procedures on the customer "service versus strictness" spectrum, but the decisions that get applied as store-level policies may do more harm than good. Enacting stringent across the board policies impacts good shoppers as well as fraudulent shoppers.

Some retailers have chosen simple receipt verification, provided that their point-of-sale system will validate that the item was in fact purchased at the store. Recent POS Benchmarking Surveys indicate that approximately 30% of the top 100 retailers actively use a centralized returns management solution. These host-based databases can verify if the receipt and the original purchase are valid, but, unfortunately they cannot intelligently advise the store as to whether or not it should accept the return. This simple receipt verification is a good starting point and certainly improves the management of returns; however, the problem with this approach is:

- It does not account for shopper return trends and behavior; there are many examples of return abuse where every receipt may be valid, but the returner is clearly exhibiting negative behavior. Receipt verification looks only at a specific transaction and is unable to detect those behavior trends.
- Depending on the application, receipt verification may be configured simply to provide the information to the store employee, but it still leaves the decision-making to the store employee whether to allow the return. This introduces subjectivity and accountability issues which may be applied or enforced very differently across an entire chain.
- Receipt verification does not address the problems associated with "non-receipted" and "no-consumer-identified" return transactions.

Instead, what is needed is a statistical modeling approach that helps more accurately determine true return fraud, eliminating abusive returns while allowing legitimate returns. Using the same type of statistical algorithms that have transformed Price Management, Return Optimization is now available to identify which consumers to reward for their patronage during the return process and which consumers are abusing services and/or defrauding the business.



Progressive retailers who have implemented Verify® Return Authorization have realized an average of 8% overall reduction in returns (and a 13% reduction in shrink) without negatively affecting customer service ratings. They continue to offer high customer service to their good consumers, while discouraging abusive consumers (through education and warnings) and preventing fraudulent returns.

Store associates appreciate Return Optimization because they are able to deliver good service to good consumers but let the system choose an appropriate action for abusive or fraudulent returns. The enforcement of the corporate returns strategy is transferred to an outside provider, deflecting confrontation between the store associate and the fraudulent consumer. The process has helped many retailers reduce fraudulent transactions much the same way Check Verification Systems did in the 1990s.

Returns Opportunities

Returns represent a major untapped opportunity in retail. Retailers now have a new dial to turn—one that increases conversions and revenue and also reduces fraud and abuse, without negatively impacting customer satisfaction.

What are the next steps to discover the opportunities and address the challenges in the current environment? Retailers need to ask themselves the following questions:

- How is the consumer return experience at your store?
- What are your current return policies?
- Do your return policies adversely affect your best customers?
- Do you have a method for receipt validation at the point of return?
- Can you identify what actions and overrides are being performed during the return process?

- How do associates feel about the return process at your store?
- What is your current consumer conversion rate?
- How are good consumers being rewarded for their patronage?
- Does anyone review "good customer" returns?
- Do you incorporate the return transaction into your reward system?
- Do you have a process in place to help move an "average customer" up to be a "best customer?"
- How much impact could Return Optimization make to your bottom line?

The ability to properly manage abusive and fraudulent return behavior by identifying, tracking, educating, and then deterring unwanted consumers without negatively impacting good consumers can significantly increase sales. When you combine that ability with a reward system based on converting returns into purchases and creating positive interaction at a touch point that can often be frustrating for both the consumer and the associate, the impact to the bottom line can be dramatic.

"Retailers should have systems that not only discourage poor consumer return habits, but also provide the key performance indicators that identify and reward good consumers. Creating a new 'Returns KPI' centered on surprising and delighting the consumer and converting those returns into purchases is a must," remarks Ken Morris, retail industry consultant and principal at Boston Retail Partners. "This will help turn a bad customer into a good customer, while creating good customer service and keeping the sale."

Retailers have a real opportunity to put more on the bottom line AND increase-customer satisfaction. Instead of just trying to manage returns, there is a better way to minimize fraudulent returns and consumer frustration, while maximizing return transactions' untapped value—Return Optimization.

Americas +1 949 262 5100
Europe/Middle East/Africa +44 (0)20 7430 0715
Asia/Pacific +1 949 262 5100

APPRISS® RETAIL
apprissretail.com