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Omni-channel point of view 5

Product returns: Closing the omni-channel loop
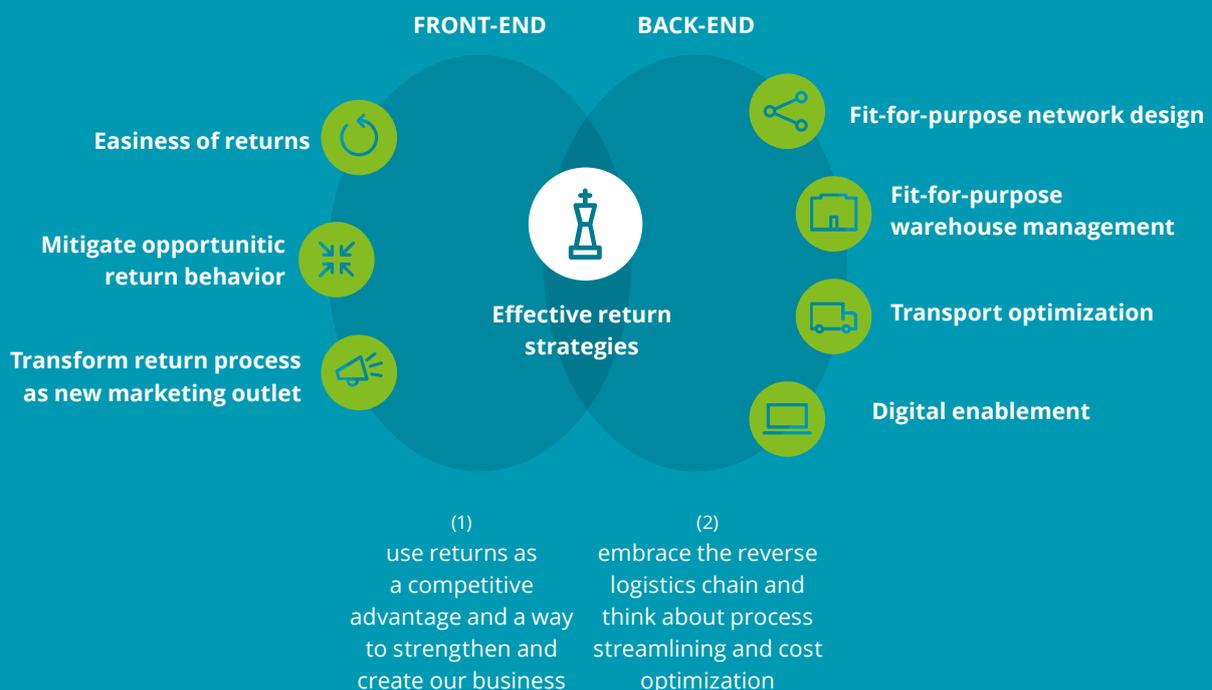
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Introduction

Throughout this series of Point of Views, there has been one common thread: how to build a competitive advantage around a key capability of the omni-channel supply chain. Whether it is through inventory & product availability, personalized fulfillment or delivery, an effective omni-channel supply chain knows to respond in a customer intimate way.

The customer e-journey moves beyond the point of product delivery. Returns have always been an integral part of a supply chain. Common examples include physical product returns, reverse logistics for packaging or stocking materials such as pallets and empty bins, or even customer service enquiries. Nevertheless, the order of magnitude in the number of returns is typically more outspoken in omni-channel environments, reaching levels between 25% and 30% for clothing versus a more modest 8% in the traditional brick-and-mortar clothing stores.[6]

Traditionally, returns have been perceived as a burden on the operational cost of a supply chain. From the early days onwards, companies have undertaken strategies like the milk run concept to minimize the transportation cost, but fail to cope with the overall fallout from returns. This operational burden is not only caused by the increased logistics complexity, but also the need for customized processes, dedicated warehouse handling zones, and additional administrative work.

For instance, the Financial Times calculated that, in the UK, a returned product passes on average through 6 or 7 pairs of hands before it is listed for resale. This results in a loss in value of the product – not just because of damages, but also because seasonal products might already be outdated before they get back for sale.

So, returns are a complex matter, leaving companies with the following two options, or a combination of both:
(1) we can use returns as a competitive advantage and a way to strengthen and create our business, or
(2) we can embrace the reverse logistics chain and think about process streamlining and cost optimization.

FRONT-END   BACK-END

Easiness of returns

Mitigate opportunitic return behavior

Transform return process as new marketing outlet

Effective return strategies

Fit-for-purpose network design

Fit-for-purpose warehouse management

Transport optimization

Digital enablement

(1)
use returns as a competitive advantage and a way to strengthen and create our business

(2)
embrace the reverse logistics chain and think about process streamlining and cost optimization

Front-end – returns as a competitive advantage

The seamless customer experience positions itself as a mantra within the modern omni-channel organization. This thinking extrapolates towards the reverse logistics flow. The "anything, anywhere, anytime" slogan resonates as well with customers from a returns perspective.

Easiness of returns

The cost of a return together with the diversity of return channels are key levers for highly effective return policies. Hence, easiness of returns is one of the main drivers for customer loyalty: 66% of shoppers consult a retailer's return policy before making a buying decision and 92% of consumers would buy an article again if the online return process would be easier[7]. A bad return policy offers limited return options, stringent return windows, involves an administrative burden, creates skepticism towards damages, or applies seals or restocking charges. Clothing retailers like Zara, Mango or Macy's have addressed some of these issues by disregarding the purchase sales channel, i.e. you can return your clothes to any department store or to any drop-off location. This even increases the client facing time, with potentially additional sales. Others send the return packaging along so that the customer does not need to pay extra. It is clear that returns render additional supply chain costs. Often, retailers claim that a return product flow costs twice as much as the delivery[8]. Consequently, a good return policy trades off the expected customer value with the cost-to-serve. Integrating the forward flow as much as possible with the return flow is therefore recommended.

Mitigate opportunitic return behavior

Of course, you want to avoid opportunistic customer behavior. Hedge spenders buy items at full price and will resend them once they can find that item at a discount. Intentional returners deliberately over order because they know returns are easy and cheap. And how do you deal with returns of less tangible products like software?

Transform return process as new marketing outlet

By acknowledging that returns are an inherent part of the omni-channel supply chain, companies have managed to transform the return cycle as an additional marketing and sales channel, by leveraging supply chain capabilities. Upselling and cross-selling concepts are extensively exploited within e-tailing. Omni-channel players send other products as samples or add accessories that perfectly match the shirt that you have bought. It is a matter of trading off the customer's probability to respond to the temptation with the typically limited additional cost of upgrading the shipment.

In a digitized world with paramount data on customer behavior, omni-channel logistics optimization is not just a matter of cost anymore, but it includes revenue in the equation.

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7   Descartes kenniscentrum
8   Financial Times (2016) – "UK retailers count the cost of returns"

Back-end – reverse logistics flows and processes

However, a front-end alone is not sufficient to attain an effective return management process. From a back-end perspective, returns need to be seen as an integral part of your Supply Chain Strategy and Design process:

Business area	Observation	Strategic impact
Fit-for-purpose network design		
Network Design	Returns bring additional flows in the network and could therefore impact the optimal location of production facilities, warehouses and distribution centers	Forecast return flows and include the flows and costs in the network optimization models
Fit-for-purpose warehouse management		
Warehouse Management	Returns require additional capabilities, together with space and equipment needs	Warehouse designs to include return flows and processes ranging from reception to inspection and warranty validation
		Accommodate when and how returns become included in the inventory again
Transport optimization		
Transportation Management	Dealing with returns might have an impact on your tendering approach	Include return flows in the tendering process and negotiations with carriers
		Extend the transportation outsourcing/insourcing decision to the return flow
Digital enablement		
Information Technology	Return flows not only bring physical complexity but also result in additional transactions in ERP systems	Translate the business requirements for the return flows into functional requirements and user stories for your WMS, TMS and planning systems
Data mining and analytics	Companies can leverage data on how often shoppers return purchases to adjust the return policy	Develop a clear strategy on how analytics on the return flows can drive strategic and operational decisions in terms of return policy and logistics optimization

Traditional companies that start the omni-channel journey might face difficulties in embedding returns into their traditional forward-facing operations. Indeed, reverse flows add to transportation and handling costs, which are two key drivers of physical network decisions. Reverse logistics deals with questions on (de-)centralization of inventory and handling like "do I return to local or central locations" and "do I in- or outsource the return transportation and handling".

Next to the physical set-up, returns require new receiving processes, different quality checks and a tailored invoicing process. In order the benefit from the inventory ecosystem, returns should be part of the omni-channel inventory as quickly as possible. In that sense, returns could be used as a way to balance inventory allocation in the network.

Depending on the policy, customers can return the product to a store, a distribution center or a third party. Nevertheless, the costs allocated to each option significantly differ. While returns to store might be the cheapest and have the shortest turnover time for resale, they cause considerable additional workload and reduced resale margins. Therefore, e-tailors often favor a hybrid solution of in- and outsourcing[9].

E-tailers have become more creative in reducing the number of back-and-forth flows with customers. Clothing companies sometimes send multiple sizes of the same product. You know that your customer is going to send it back, but you might avoid the last forward flow of sending a new size in a different shipment. In a B2B context, spare parts are sent with the new product.

Finally, new (digital) technologies enable companies to reduce return flows or reshape the way they are managed.
- Amazon, that is expected to become the leading US apparel retailer in 2018, is investing in 3D body-scanning technology to enable customers to virtually try on clothes in order to find the best fit[10]
- Sports retailers, like Adidas and Nike, are already using 3D printing to print the perfect shoe
- By modular designs, you can create your own product based on standard building blocks
- Artificial intelligence and data analytics assist companies to better meet your needs, resulting in less returns
- Drone delivery and internet of things initiatives are leveraged in the return flow to reduce transportation costs

9   Alixpartners.com
10   The Wall Street Journal – "Amazon Wants to Know Your Waistline"

Cases

Case 1:
Outfittery

Outfittery, a shopping and styling service targeted to male customers, does not only excel in "Personalized Fulfilment", but they also embrace returns as a competitive advantage. In order to make the shopping experience as convenient as possible, Outfittery has made return management an integral part of their business model.

After the customer receives a personalized box consisting of a full outfit, he has 7 days to try on and return the items he does not like, want or need. Depending on the country, the customer can then return his box free of charge by dropping it off at the post office, service point or pack station of the relevant service provider. Recently Outfittery, has made the return process even easier by introducing a free pick-up service. The company is now cooperating with service providers to collect returns whenever and wherever the customer likes.
Moreover, each return allows the company to further adjust to the customer preferences. The styling service and products shipped become more precise, resulting in a decrease of returns and increase of margins.

Case 1:
Sears

Even for companies for which return management is not an integral part of the business model, the management of reverse logistics could still aim for supply chain efficiency and reduce costs. With this approach, it is important to note that preventing reverse logistics is more important than optimizing it.

Sears, a chain of department stores in the United States, has informed and educated its store teams to optimize the 'sort and segregation' routines in accordance with returns terms and rules. Improved decision-making at the point of return prevents Sears from moving product back up the supply chain only to scrap it, thus saving on transport and handling costs.
Items that are sent back by the store eventually go to one of three service centers (operated by FedEx Supply Chain, formerly Genco) for evaluation, handling, aggregation, and return to vendor or for salvage.[6]

6   supplychain247.com

Case 3:
Zalando

Zalando, Europe's biggest online fashion retailer, has recently been forced to tighten its returns policy. With about half of Zalando products being returned, the German fashion platform has been struggling with high operating costs and feeling the pressure to make a sustainable profit.[7]

Zalando does not charge any shipping or return costs, which results in many customers 'taking advantage' of the service by wearing an outfit to one or more events and then sending it back (a concept known in the fashion industry as 'wardrobing'). To limit the number of returns Zalando has decided to attach a 10 by 15 cm label stating "do not remove this tag" to items that can be used for wardrobing (typical examples include evening dresses and gala gowns).[8]

And Zalando may already have benefited from the new return conditions by exceeding analysts' expectations in making a small operating profit for the first quarter of 2019.[9]

The next step for the German fashion web shop could be to make customers pay for returns or the delivery itself, meaning the age of 'free' policies would come to an end. Zalando is already experimenting on a small scale with delivery costs of 3.5 euros for orders below 25 euros, and if this tactic proves successful it will likely be rolled out to other countries.

7   businessoffashion.com
8   retaildetail.eu
9   retaildetail.eu

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Effective return strategies

Developing a reverse logistics and returns management program should look both at the strategic angle as well as the operational angle. The strategic angle needs to combine a strategy targeted towards customer, suppliers and internal returns. The operational angle needs to cover the return transportation, processes and customer service.

By accommodating for product returns as a key sales driver and by integrating reverse flows in our logistics strategy, we close the omni-channel loop. Returns should not be just a matter of cost optimization, but render important business value. Also towards the future, circularity concepts and sustainability pressures might put more emphasis on optimally organize the reverse logistics flow.

Nevertheless, being agile stays also essential in the context of returns. Omni-channel supply chains are dynamic and are subject to changes in market conditions and expectations. The Learning supply chain is in this sense a fifth enabling capability to put on the agenda.

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