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Today's typical shoe-shopping experience is relatively universal. A consumer enters the store, quickly scans its entire contents in a single gaze, identifies and moves towards his or her preferred selection, then fingers three or four sample shoes while awaiting the help of a salesperson.

Later, after sheepishly sending the salesperson on repeated trips to the storeroom and self-consciously trying on the shoes before this employed audience of one, the customer (hopefully) purchases a pair and slips out of the store, grateful that the whole event is over.

DSW, a US specialty branded footwear retailer, has created a very different experience with a unique business model that has brought the company 16 years of success and growth. Now, despite having just wrapped up a year that—unusually—brought less than thrilling sales figures, the company is embarking upon an even more daring transformation. Armed with lessons learned in 2007, the company enters 2008 with the pragmatic optimism needed to ensure the transformation is a triumphant one.

DSW today

One step inside a DSW store immediately reveals its most defining characteristic: more than 30,000 pairs

of shoes in a 2,000 square-metre warehouse. But whereas immensity traditionally suggests lower quality, DSW boasts designer names (such as Coach, Sebastian and Tahari) as well as seasonal, trendy styles. "These are quality brands," says Douglas J. Probst, executive vice president, chief financial officer and treasurer of DSW. "Our buyers have access to the same vendors that the department stores do."

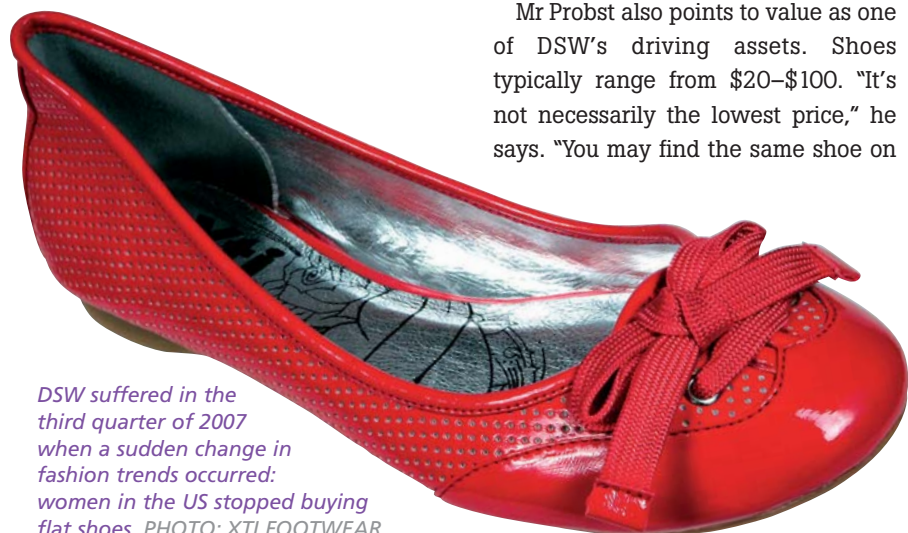
Shoes are placed atop shelves containing boxes of varying sizes so that the customer can help herself (or himself, though DSW identifies women as its target market). "The ability to touch and try on the goods is part of the experience at DSW," says Mr Probst. "Shoppers are willing to try on shoes they might not feel

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comfortable asking a sales assistant for."

DSW is certainly not the only shoe store to take the self-service approach, although it is an approach generally reserved for sellers of generic, low-budget shoes. A neat stack of boxes beneath a \$500 shoe is a rare sight.

Mr Probst also points to value as one of DSW's driving assets. Shoes typically range from \$20–\$100. "It's not necessarily the lowest price," he says. "You may find the same shoe on



DSW suffered in the third quarter of 2007 when a sudden change in fashion trends occurred: women in the US stopped buying flat shoes. PHOTO: XTI FOOTWEAR



Part of the new look for DSW stores in 2008 will be a bank-style check-out area. PHOTO: DSW

offer for less elsewhere, but shoppers can count on getting a value price."

Stylish, easily accessible and vast: this is what DSW's research says its target customers—women—want in a shoe selection.

"We're focused around the woman customer," says Peter Horvarth, president of DSW. "Quite frankly, the men's experience is about getting the shoe and getting out." For many women, shopping for the shoe is the experience, and while the large warehouse approach has thus far been consistently fruitful—the chain currently has 250 stores, having opened approximately 30 stores annually for the last few years—the company has decided to take the advice of consumers and further tweak its business model.

DSW tomorrow

The most immediately evident change will be to the store size: the space is being reduced to between 1,400–1,600 square-metres. Mr Horvarth emphasises that this change

will not alter the shopping experience; he calls it an effort "to harvest the unproductive space—the space that was used for managers' offices". Offices will now be a more "appropriate size" and are moving to the back.

Now, according to Mr Horvarth, the new DSW will still have a warehouse look on the outside, but will be more like a boutique within. The ambience will be more "residential, more feminine," he says. Stores will be staffed with salespeople of a very particular type. He describes them as follows: "[She will be a] passionate shoe enthusiast. She is there if you need her, but not intrusive. She's that friend you go shopping with who is an enabler; helping you to spend more money than you would have otherwise." Even if sales aren't immediate, Mr Horvarth envisions a level of engagement that will bring the customer back earlier and more frequently than might otherwise have been the case.

Grocery-store style check-outs

(multiple purchase points, multiple queues) will be replaced by bank-style queues (one queue feeding into multiple purchase points). Even the lighting will be adjusted to improve the colour rendering within the store.

Beyond the physical changes at DSW, the company is investing more into both its loyalty rewards programme and website capabilities. In 2007 alone, the company spent more than \$8 million on a new e-commerce website; its launch is planned for the first half of 2008. "We understand that multichannel customers represent significant growth potential," says Mr Horvarth, "and we are excited by the prospect of combining e-commerce with our loyalty programme."

The company has already found success within the loyalty programme by lowering the points threshold from \$250 (at which point the cardholder received a \$25 credit towards DSW) to \$150 (when customers will now receive a \$10 reward). Currently the company is enrolling between ➤

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40-50,000 new members each week. It hopes that its website will work in tandem with the loyalty programme to strengthen activity in both.

However, many of the changes are less tangible, and in fact have been under way for some time. According to Mr Horvarth, today's morphing is a continuation of an evolution that began 10 years ago. This is when Deborah Ferrée, chief merchandising officer, turned DSW "from an off-price business to an in-line, in-season, fashion business that offers quality and brand range that are comparable to [the offerings of] department stores," he says. "In the past, the model of an off-price discounter involved keeping the store clean, not letting people steal, and keeping the floor in stock. We still believe in all of those things, but our primary objective is to give the customer a great experience. Our customers have responded to that through the years."

Cautious progress

DSW's key offerings, Mr Horvarth insists, will remain unchanged. "The breadth of assortment and perception of value will not be dented," he says.

Or so he hopes. Central office can dictate breadth of assortment, but perception of value is for the consumer to decide. Mr Horvarth admits there was concern that customers may be put off by the "pricey" new look of the store, but the

company has thus far not found that to be true. "Customers love the new store design," he says. "We will end this year with 35 stores in the new design format, including five remodels."

He adds that capital planning decisions will be based on the sales of the five remodels, and that initial indications are encouraging. Typically, a new store operates at 80% its first year, earning \$2,100 per square metre. "Our new stores," says Mr Horvarth, "are operating at 30-40% better sales productivity."

The company-wide enthusiasm for DSW's burgeoning model has been dampened slightly, however, by a turbulent 2007. Unseasonably warm weather and unexpected—and sudden—shifts in fashion trends have left the warehouses with more inventory than intended and less profit than expected.

Shoppers passed over high-end autumn boots in favour of sunnier (and cheaper) sandals and other casuals. The real shock, however, was young women's third quarter rejection of the flats that they so loved in quarters one and two.

"In all my years in retailing, I've never seen a category start to decelerate in sales as aggressively as it did in the middle of quarter three," says Ms Ferrée. Sales in quarters one and two were outpacing inventory, but in quarter three the opposite started to occur.

"I think there was so much novelty in fashion in the industry that the trends in how the customer is shopping and what she's shopping for actually started to shift," she says. That shift appears to be towards a more classic, cleaned-up look across multiple departments, and DSW will distort its spring inventory accordingly. She adds: "Early indications are that spring will be a strong season for dress shoes and colour will be important."

In a store that carries 30,000 pairs of shoes, predictions gone wrong are inevitable; the key to continued growth as a company, according to Ms Ferrée, is to learn from and remedy the miscalculations.

"A few quarters back I said that the place we were struggling the most was finding the right inventory levels for the [men's] traditional dress and casual component of the business," she says. "We have steadied that now, finding the right blend between dress and casual traditional and the inventory levels support that. The strategy behind that was to reduce SKU (stock-keep unit) count, and to be in stock on core items and key vendors so that the male consumer coming in to buy core product would be able to find his size."

The department that continues to be a challenge is young men's fashion. "We continue to revise our sales based on customer response and

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our inventory levels," she says, "but I don't think we're there yet." Unpleasant surprises such as the abandoned flats, or persistent conundrums like men's fashion, have contributed to 2007's unenviable, and unprecedented, distinction of having failed to top the previous year's full-year earnings growth. "This is a first for us as a public company, and we are disappointed," says Mr Horvarth. "And while we're very aware of the external factors, our focus continues to be on controlling the controllables ... we continue to learn from both our successes and disappointments."

Although the 2008 strategy aims to address the distortion issues that marred 2007's sales figures, he acknowledges that imperfect predictions are inevitable: "In the fashion business, you have to make distortions. If you don't, you miss fashion trends. The team has been very good at looking around corners and matching these distortions to what the customers' desires are. The level of inventory put behind a distortion is always a gamble."

According to Mr Horvarth, spring will be approached with a more conservative hand. The company will minimise potential loss by limiting distortions overall and leaving more leeway for chasing trends in season. "We are positioning the opportunity to chase the trends," he says, "should the trend be stronger than our inventory."

A happy new year

At a recent webcast announcing quarter-three earnings, a caller asked whether 2008 was going to have the same "volatility" as 2007. Initially, Mr Horvarth explained that 2007 had actually reflected the company's general predictions and had

therefore not been volatile, but the caller was not satisfied with this answer.

The president then reiterated the factors—those that were anticipated and those that were not—that had influenced 2007's results, and how such factors will be managed in 2008. "To use your words," Mr Horvarth eventually concluded, "we're expecting less volatility if we hit our plan."

And he expects to hit the plan: opening at least 30 stores, launching an e-commerce channel and continuing investment into the company's system infrastructure. "If

anyone wants to know what we talk about on Mondays," he says, "we talk about progress against the strategy. And so far, so good."

That strategy seeps into every crevice of the business; even head office, in Columbus, Ohio, has undergone a makeover to better reflect the evolving brand. Recruitment is up—by number and quality. "We've not had many rejections in the past, but we've struggled to get people," he says. "Now people are talking about us, as opposed to us telling them about DSW." 



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