10 KPIs

for retail CEOs who want to lead their company into the future

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LS Retail
an aptos company

Retail businesses across the world are trying to use data, analytics, and AI more effectively to inform their decision-making. However, many of them are being held back by the **lack of a data-driven culture**, the Harvard Business Review reports.

CEOs can play a key role in transforming their company from a traditional one into a modern, data-driven business. The process starts with having **measurable goals**, and structured ways to calculate how close or far the company is from them.

Some goals are the same across all industries: make a profit, have positive cash flow, be profitable. Retail, especially modern retail that includes physical stores and online commerce, has more than a few **industry-specific goals** to choose from. Once the goal is set, there may be several key performance indicators (KPIs) that can help a company track whether that goal is being met. In fact, a **KPI** is a **measurable value that indicates how well a company is doing in meeting its critical objectives**. Unlike business metrics, KPIs take into account the connection between data and its impact on essential business measures. This e-book walks you through retail KPIs that are central to measuring goals connected to business in general, sales, returns on investment (ROI), and customer experience.

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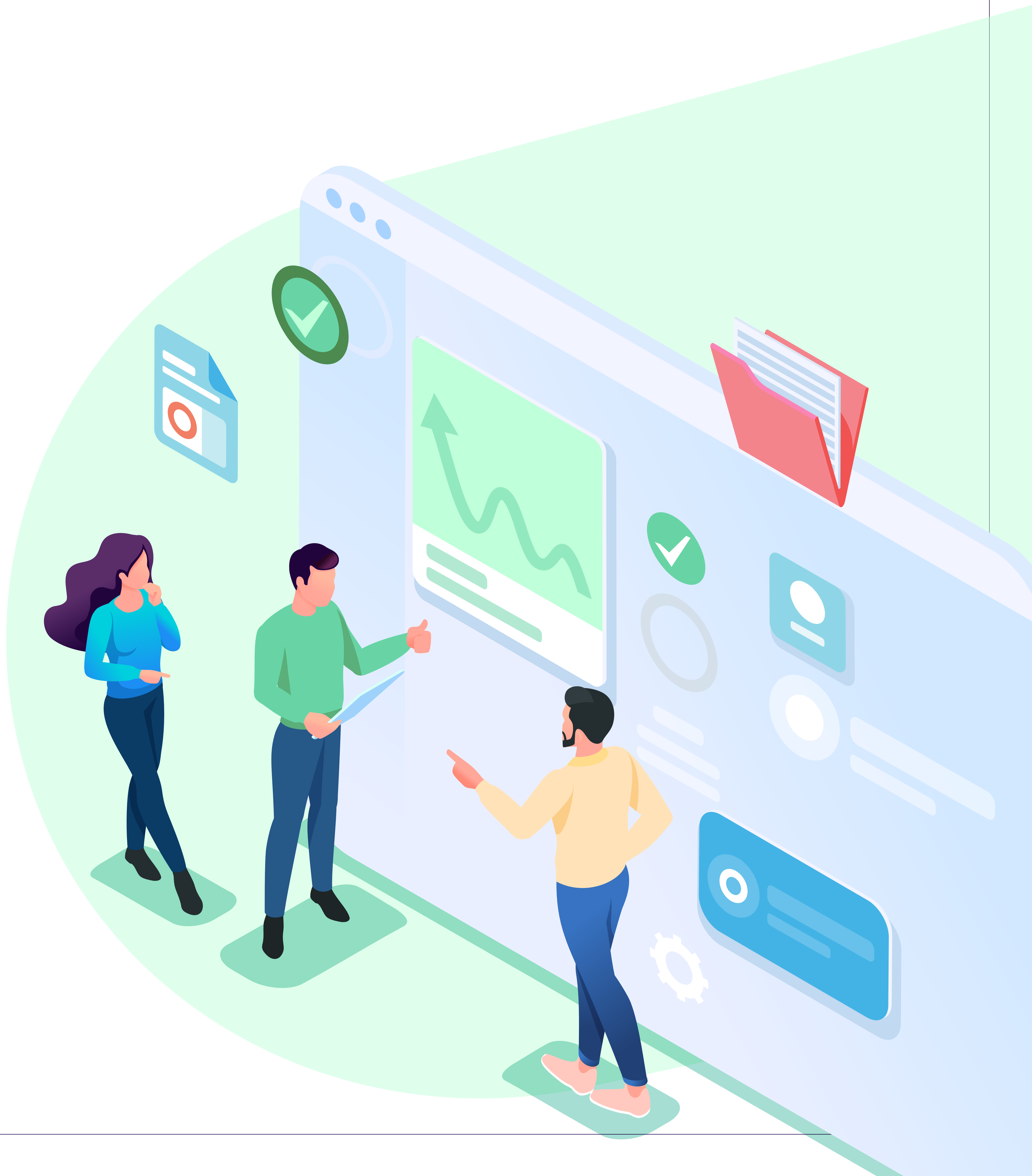
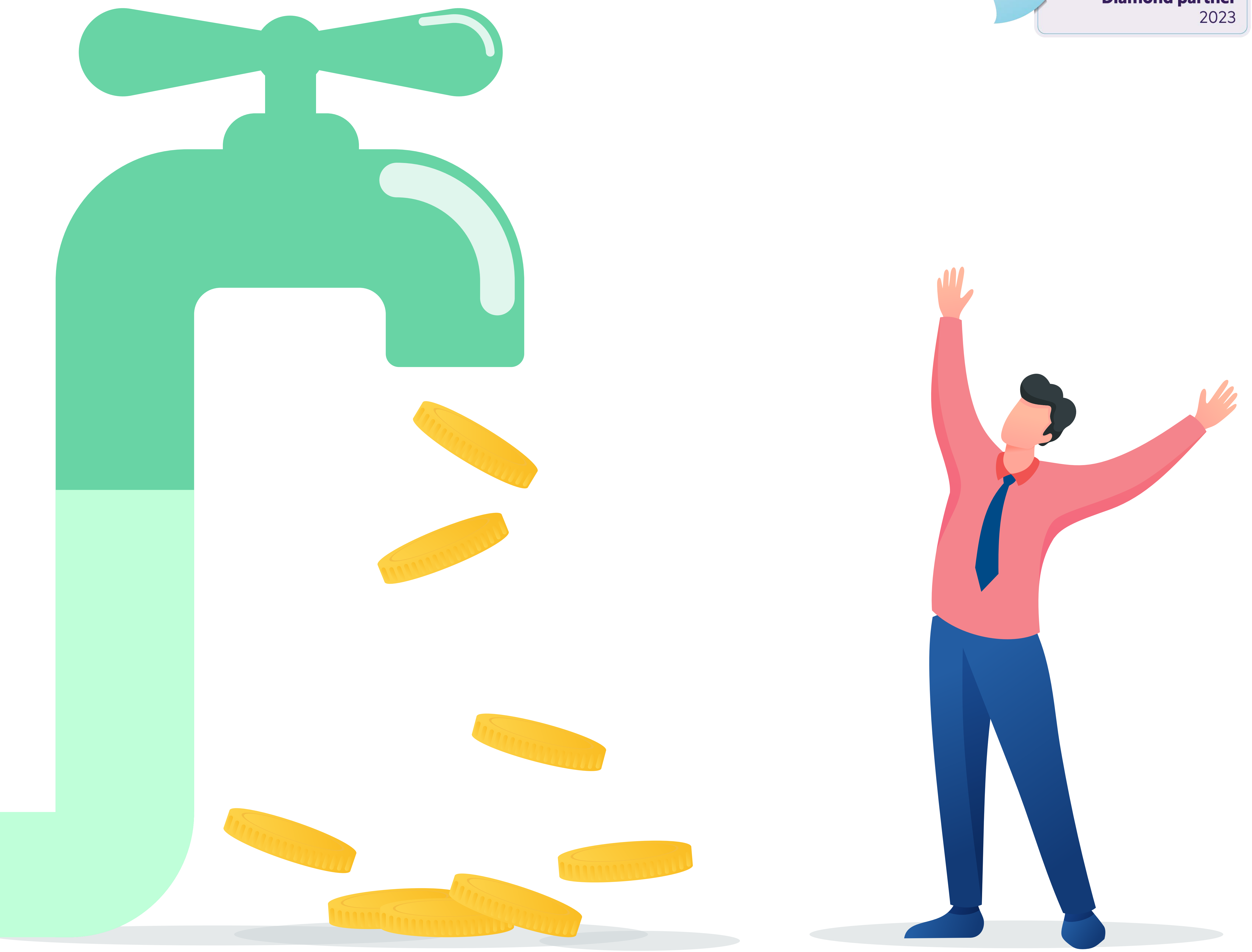




1. The Basics

Let's start with **the basics of business**. Whether your business goal is to pay off a debt, expand, or offer a new line of products, these two KPIs can help show how close the business is to those goals; ignoring them can lead to a company's downfall.

Cash flow

The number one predictor of a company going out of business is cash flow. This has the relatively simple formula of

cash from operating activities - capital expenditures

Businesses want to have positive cash flow both in the moment, and forecast into the future. This ensures that they will do more than meet their financial obligations, giving them the opportunity to expand, pay down debt, or pay out dividends to stockholders. Negative free cash flow could be a warning sign that your business may not be around much longer, especially if it persists over a longer time.

Time, though, is one of the keys to understanding KPIs, especially cash flow in retail. The cyclical aspect of retail, sales up during one season and down during another, can make it seem like your company may be in the negative regarding cash. However, taking cash flow snapshots from multiple time periods, such as quarters, months, or even years, and comparing them will help to get the best overall picture of the company's cash situation. Understanding the past results will also mean stronger forecasts of future cash flow.

Another measure to take into account with cash flow is **working capital.** A KPI of its own, it is one that can impact cash flow if, for example, your company takes on a large project such as opening new stores or introducing a product line. So if the goal is to expand, it may pay to take working capital into account.

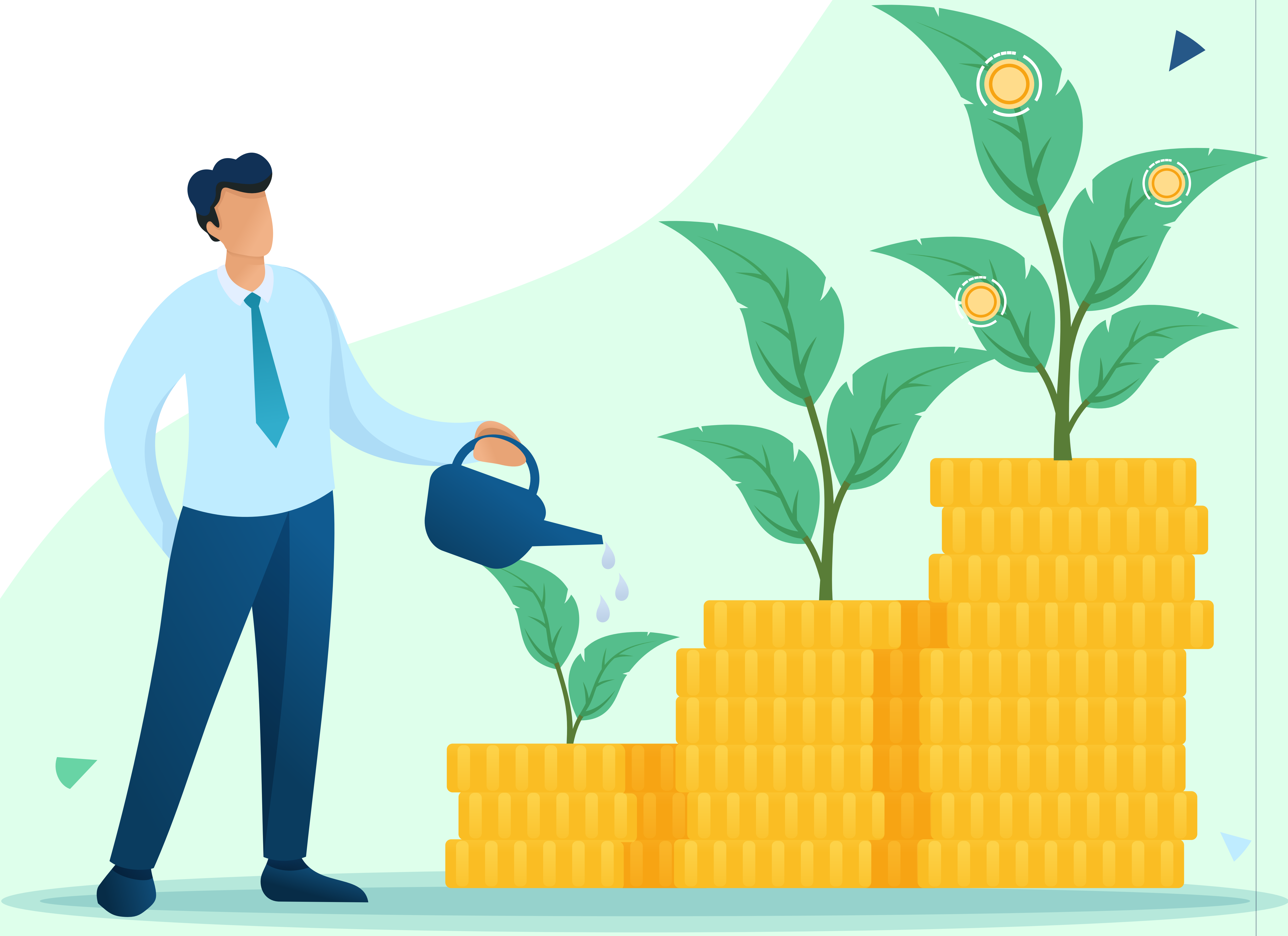
Gross profit margin

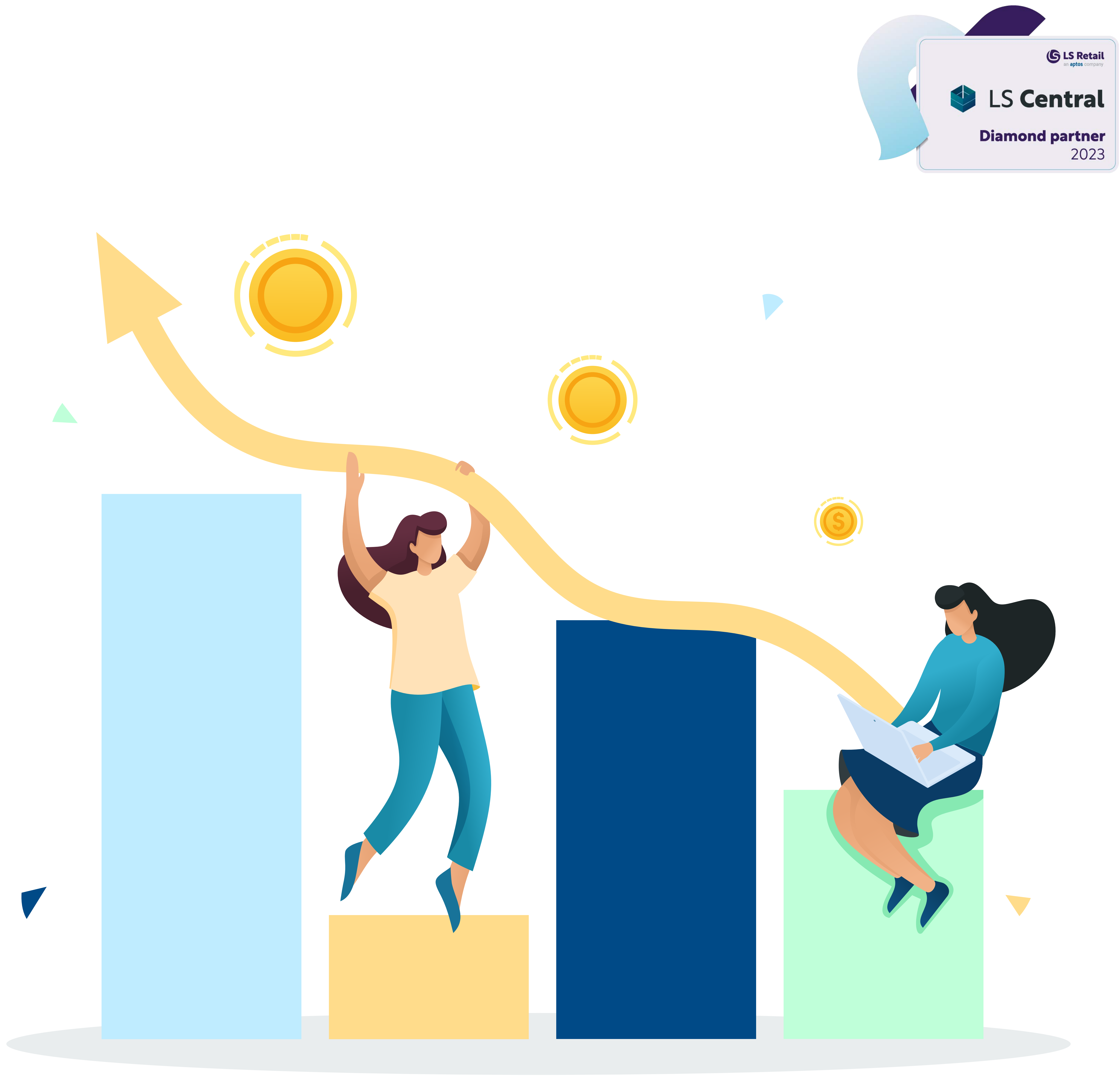
Gross profit margin, or gross margin, looks similar to cash flow in that it takes into account what is coming into the company and what is going out. The formula is:

$$\frac{\text{revenue} - \text{cost of goods sold (COGS)}}{\text{revenue}} \times 100$$

Revenue is the actual money your company receives during a given period, or the total number of goods you sold at the prices you sold them. Those goods didn't come for free, though, and **their cost needs to be taken in account** to get the gross margin. COGS is subtracted from revenue and then the entire thing is divided by revenue to give the margin in a percent. There are a couple of things to keep in mind with this formula. First, **revenue does not always equal sales made**, even in retail. You may have income from other activities such as licensing, rentals, or other revenue producing source. Second, COGS needs to take into account both **direct and indirect costs**. Those costs may include transportation costs, handling costs, warehousing costs, and operational costs. Each of these can be a KPI of its own.

Again, it is important to look at **gross margin over a specific time period**. With modern ERP and POS systems and the right business intelligence, this can be easily and quickly done for any period of time. This allows for fast comparisons between, for example, your busiest season last year versus this year or even between last week and this week. The right software also allows fine-grained profit information across channels or for specific items within or between channels.





2. Sales

A common goal in retail is to increase sales, but all sales increases are not made the same. A data-driven retail CEO knows that a company needs to be granular, and track more KPIs than just general sales.

Sales by year

Yearly sales are calculated by

$$\left(\frac{\text{sales for time period this year}}{\text{sales for time period last year}} - 1\right) \times 100$$

The formula gives a percentage comparison of current sales to sales a year ago. Again, **choosing the time period for comparison** is part of the equation. If you just came off a peak sales season, it is good to check your numbers against those from last year. If the percentage comes out positive, then sales increased. If the percentage is negative, then sales decreased compared to a year ago. No matter the outcome, this core KPI shows you if you are meeting a business goal, and where to go from there.

If you use a powerful, **unified ERP and POS software** you can break sales down even further. A savvy CEO knows that one number is not enough for modern retail business decisions. If the total sales number is up or down, the question remains of **what** is driving the change. **Business intelligence (BI) software** can answer that question, giving you the opportunity to analyze your results across channels and locations or per single channel or store, for product types and groups, and more, allowing for a more nuanced understanding of sales.

You can't have a clear vision of your business if you are using many separate systems.
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Sell-through rate

Sales as a KPI gives a broad overview that allows for a year-to-year, quarter-to-quarter, or even season-to-season comparisons. The sell-through rate, though, give a more detailed look at the stock on hand at the beginning of the month versus sales. It is calculated as

$$\frac{\textbf{sales}}{\textbf{stock at hand (at beginning of month)}} \times 100$$

Not only is this KPI a good indication of your rate of sales, it also gives insight into the company's **return on its investments (ROI)**. In retail, online or in person, stock is one of the biggest investments. It isn't enough to know the inventory and the sales, though. You need to combine those two to see how much and what kind of stock is actually being sold in a given time period (a month in the equation above).

With the right system, the sell-through rate can be **tracked by individual item via SKUs**. Perhaps your goal is to reduce the amount of square feet used for inventory in your physical stores. The sell-through rate of specific products can tell you how many of those items the store should keep on hand, allowing for reduced stock in products that don't sell quickly and reduced overall space for inventory. By comparing season-to-season across years, you can keep the items that sell in stock when needed.

Units per transaction

The adage in retail is that the second item makes the profit. If the goal is to increase profit, then looking at units per transaction can help in deciding how to reach that goal. The equation is simply

$$\frac{\textbf{total units sold}}{\textbf{total transactions}}$$

That looks easy enough, but what if the goal is to increase the number of items sold online versus those sold in physical stores? Units per transaction, like sales and the sell-through rate, can be **tracked according to sales channel** and right down to POS with the right business software. Another goal may be to increase **employee upsell rates**. Tracking units per transaction per employee or store is one way to gain insight into how well employees are meeting that goal.

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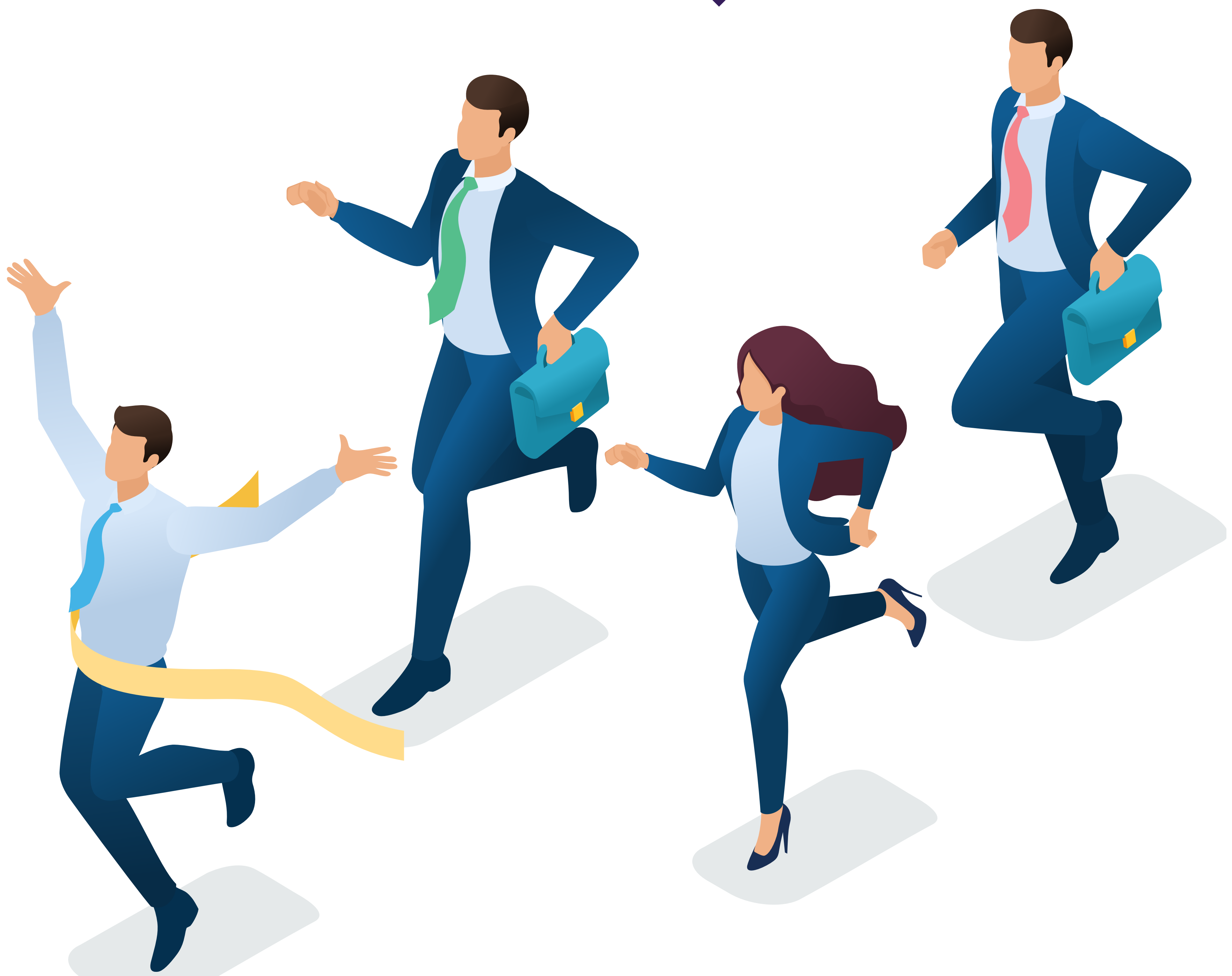


3. Stock

Stock is a key investment, and challenge, for a retail business. Having too much or too little can impact the business negatively, but finding that elusive just-right amount can be very difficult. It's not enough to just know how much is invested in inventory. Profitability is one way of measuring a company's profitability. It shouldn't be confused with profit: **profit** is the amount left over from revenue after all expenses are subtracted. **Profitability**, on the other hand, looks at the ability of a business to have a return on its investments. How can retail businesses measure profitability? The sell-through rate is one measure, since it indicates a return on investment. Two KPIs tied to inventory are important for this.

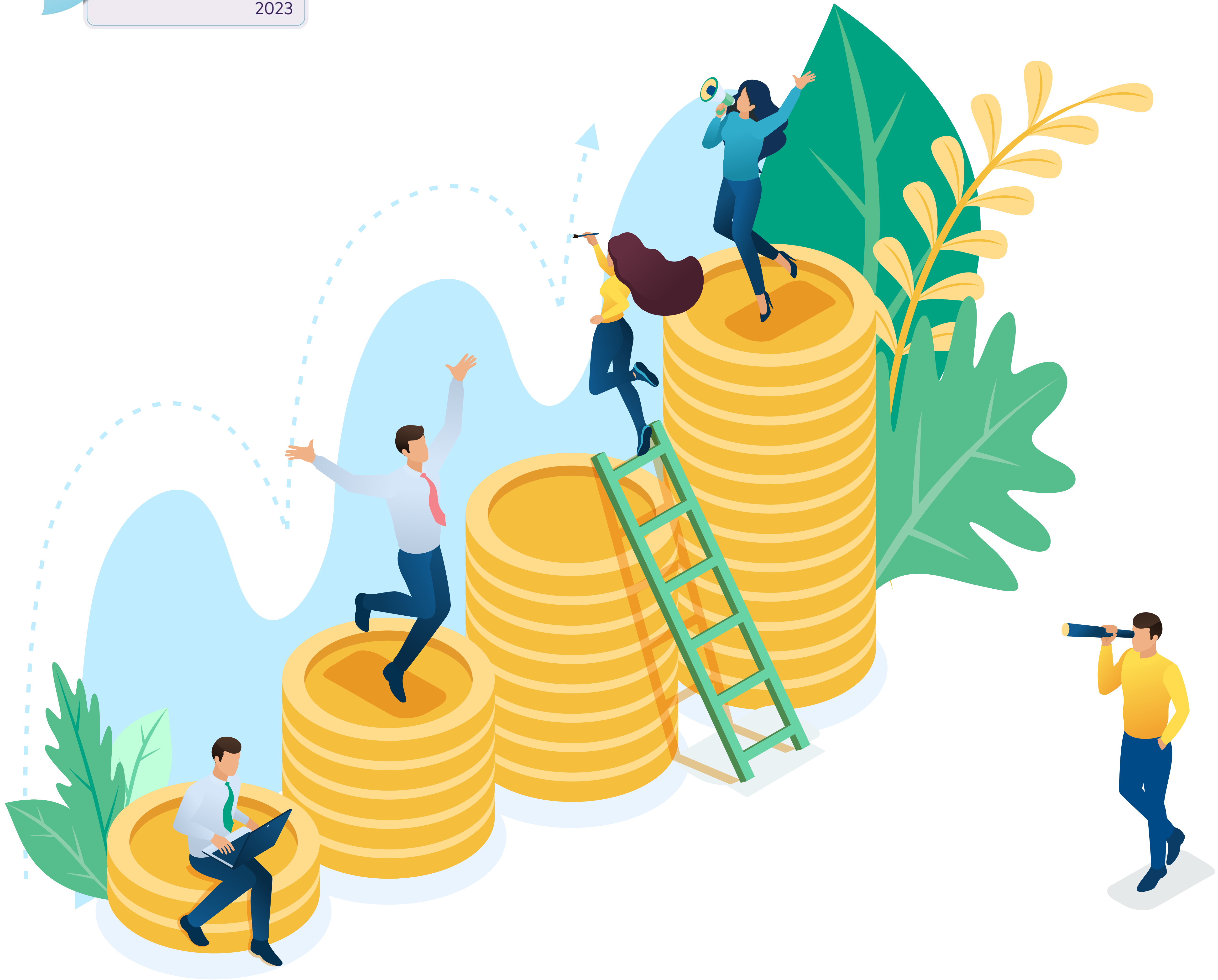
Inventory turnover

The equation for inventory turnover, typically measured in terms of a 365-day period, is:

$$\left(\frac{\text{average inventory}}{\text{cost of goods sold}}\right) \text{x365}$$

Yes, this KPI is very similar to the sell-through rate, but it gives different insights into the return on inventory investment. First, it is a **year-to-year** measure of stock coming in and sales going out, not month-to-month like the sell-through rate. Second, not knowing how retail inventory is turning over can cost a business a lot of money in **unsold items** (unrealized investments) or in **lost purchases**, because items are not in stock when needed.

TotalRetail reported that retailers are losing $1.75 trillion a year on overstock and out-of-stock issues combined with returns. Don't let the returns fool you; they only account for 40% of that number, leaving **stock issues** as the remaining **60%**. Of course, that is an average number for an entire industry. If you want to know how your retail business stacks up against the industry as a whole, using inventory turnover as a KPI is an excellent place to start.



GMROI

The title of this KPI may seem like alphabet soup, but it means the **gross margin return on investment**. This is another way of seeing if the business's investment in stock is returning a profit, but it is expressed differently.

$$\frac{\textbf{gross margin}}{\textbf{average inventory cost}}$$

Gross margin is the second KPI we discussed. It is a percentage that indicates whether or not a company is making money. To calculate GMROI, the gross margin should be a dollar amount that comes from the beginning of the gross profit margin equation.

Revenue - cost of goods sold (COGS)

Once gross margin is calculated, it can be used in **other KPIs**, such as this one, to relate it to various business functions.

The average inventory cost is calculated by summing the ending inventory over a number of periods, and then dividing by the number of periods. This is probably best explained with an example. In Fran's Automotive Superstore, the sum of the ending inventory for the last year by month is $6,000. Once that is known, the $6,000 is divided by 12 for the 12 months of the year, leaving an average inventory cost of $500. That 500 becomes the average inventory cost for calculating Fran's GMROI.

To finish the calculation, let's say that Fran's has a gross margin of $550. So the GMROI would be 1.1. Any number above one is considered a positive result for GMROI, but 1.1 is probably not what Fran was hoping to see, because it isn't very much above 1. Now that Fran has the data, the goal can be to increase that number. GMROI should be used to track how the company is doing in reaching that goal.

4. Customers

A retail CEO needs to not only **understand the customer**, but also understand how to **change** the business in the customer's favor. Here are three KPIs that can lead to clearer insight on how customers currently experience the business, and what might need to change.

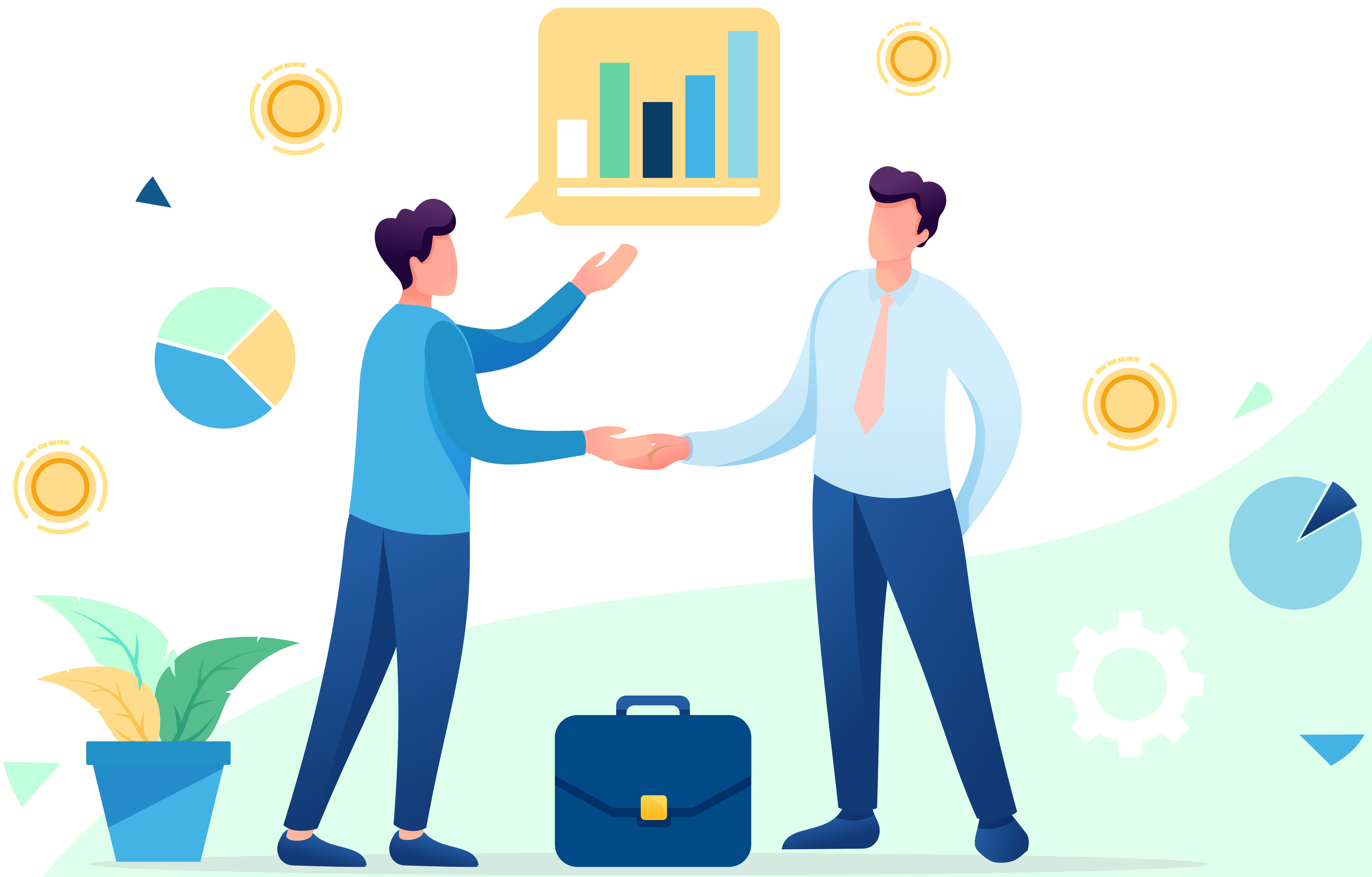
Customer satisfaction

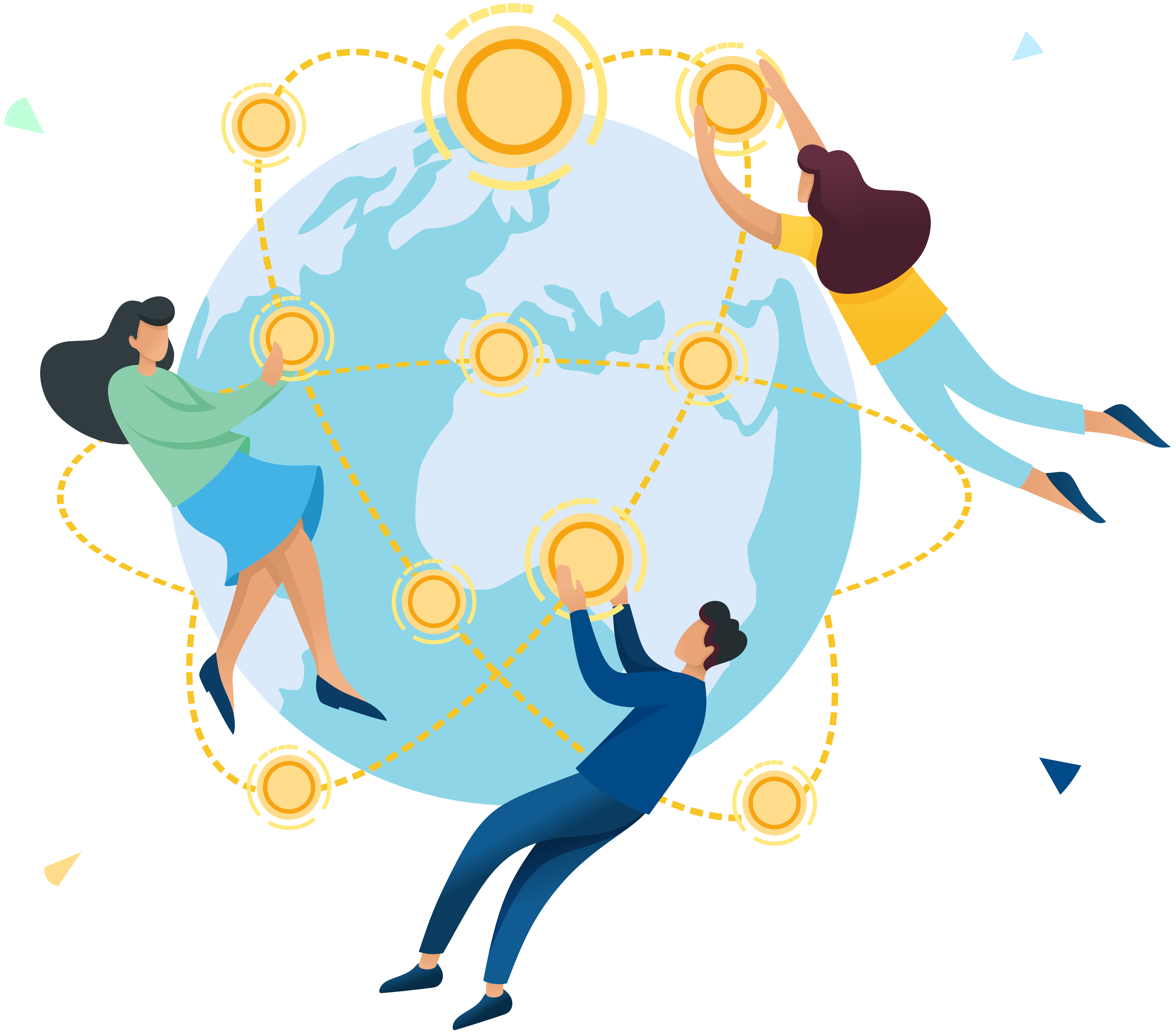
Unlike the financial, sales, and inventory KPIs, customer satisfaction may seem a little less concrete, and harder to measure. These concerns should not lead to not measuring this important KPI. One, long-standing measure is the **net promoter score**. This is measured by an average of customer answers to one simple question: "How likely are you to recommend us to a friend?" Customers answer on a scale of zero to nine. The eights and nines are considered to be promoters, or those who would recommend the business to a friend. The sevens and eights are neutral, and are left out of the equation. Anyone who answers with a six or below is a detractor. These are unhappy customers who may pass negative comments on to their friends. The equation to calculate the score is

$$\frac{\%\ \textbf{of promoters}}{\%\ \textbf{of detractors}}$$

A score of above one means that a business has more promoters than detractors. **The higher the score, the better** the ratio of promoters to detractors.

Asking people if they would promote your business is easy in online retail, but what about an **in-store measure?** Tracking repeat customers through a loyalty program is one way to do this, as a repeat customer tends to be a happy customer. Another way of measuring satisfaction is by using **happy buttons**. They have popped up in all types of retail locations, and ask customers to rate how satisfied they were with the store, or some aspect of the store, by pushing one of four buttons. The grinning, bright green button indicates the highest level of satisfaction. The red, frowning face indicates the lowest. Again, a score can be calculated by taking the average of the green, satisfied button pushes and dividing it by the average of the red, dissatisfied button pushes. A result above one indicates more satisfied customers and the higher the number, the better.





Customer experience (CX)

This may seem even more elusive than customer satisfaction, but the fact that **Chief Experience Officers (CXO)** are becoming common in retail companies around the globe shows that customer experience is essential. How to measure customer experience depends on the type of retail business. A customer that frequents a small fashion boutique is probably looking for a **different experience** than one who buys from a big box store. The same is true for online commerce. A customer browsing the newest furniture in a large, online retailer is looking for a different experience than one who is ordering a custom couch online.

The KPI above, customer satisfaction, is one part of the picture for customer experience. Other measures may include the rate of **returns**, the number of **calls** to a call center for problems with products, and customer **reviews**, both good and bad.

Whatever methods you choose for tracking customer experience, they should give you **baselines and continuing measurements** for your customer-centered goals. **A unified commerce software** uniting all channels can help track the customer experience KPIs online and offline.

Conversion rate

The Temkin Group found that a better experience correlates strongly with likelihood to purchase in the future. That is, **a good experience could turn a potential customer into an actual customer**. The conversion rate can help you measure if and when visits turn into sales.

$$\frac{\textbf{people who visit}}{\textbf{people who purchase}}$$

Unlike the customer satisfaction rates above, **the lower the number, the better the customer conversion**. If all the people who visit also buy, then the rate will equal 1. Anything above 1 means that more people are visiting than are purchasing, which will almost always be the case. If your goal is to get the rate as close to 1 as possible, meaning more purchasers and fewer browsers, then this KPI is essential for tracking that goal.

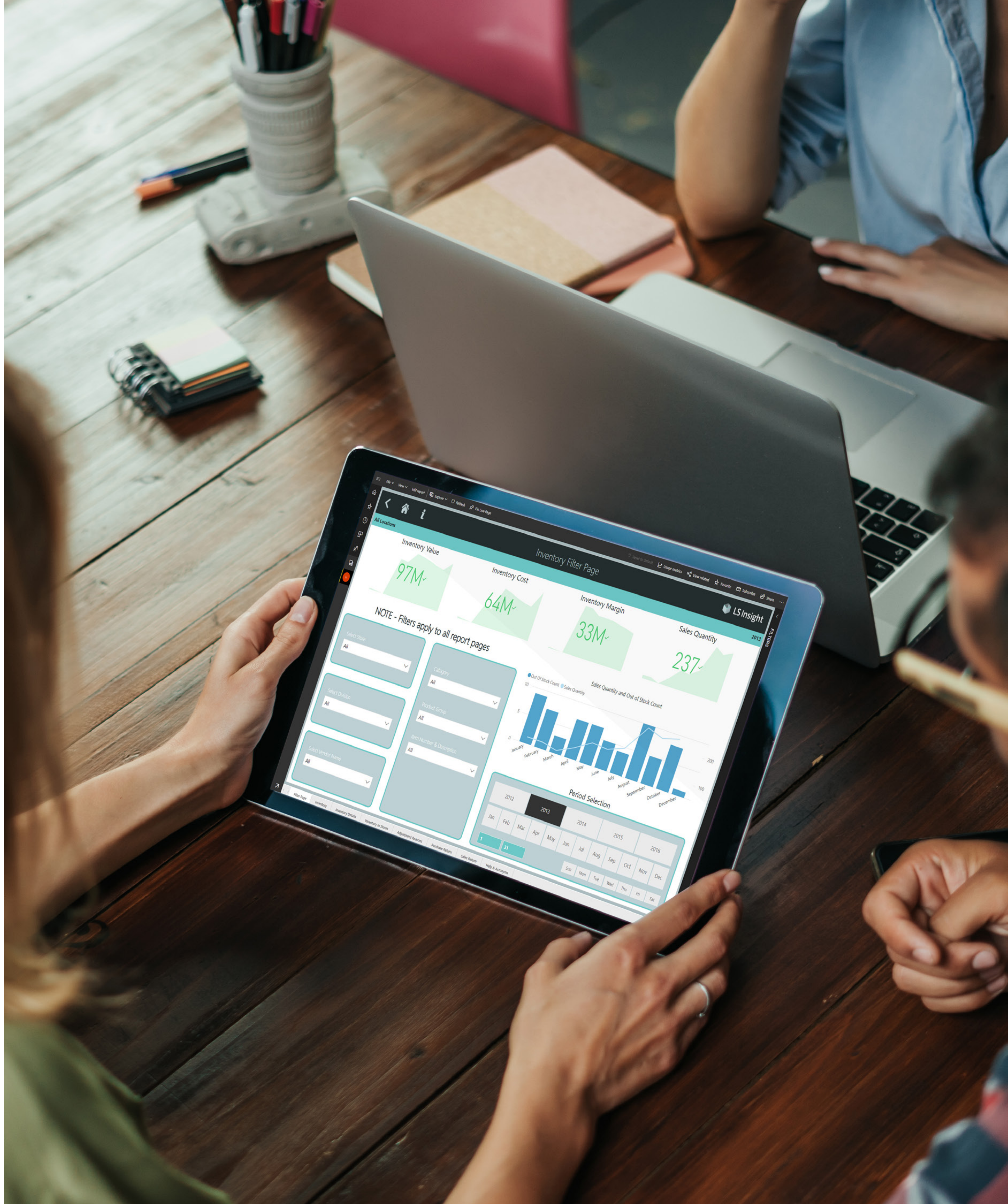
Having the right data and the right tools

Having the right data and understanding it is essential to making crucial, data-driven business decisions. The sheer amount of data available to a retail CEO can be overwhelming, especially if this data is not properly calculated and understood within the company. Key performance indicators are exactly the calculations needed to make sense of how your retail business is doing. When they are individually or collectively connected to business goals, they bring the right insights for tracking and adjusting those goals.

To assure that you are using the most up-to-date and accurate for your KPIs, you need to equip your business with the right tools. If you are using patchwork, out-of-date business applications, all you'll see are siloed, disconnected data, which you can't use to analyze and steer your business. A truly **unified commerce** system that combines inventory management, POS, customer relations, ERP and more for all your sales channels into one platform is the only way for you to get real-time, reliable data. Once you have clear, reliable information then you can use business intelligence tools to crunch that data and turn it into KPIs. A unified commerce platform brings all the parts of your business together to make the process of data to KPI to goals and decisions seamless, fast, and easy.

LS Insight is the business intelligence software that offers powerful retail analytics, highly visual dashboards and actionable reports for better decision making.

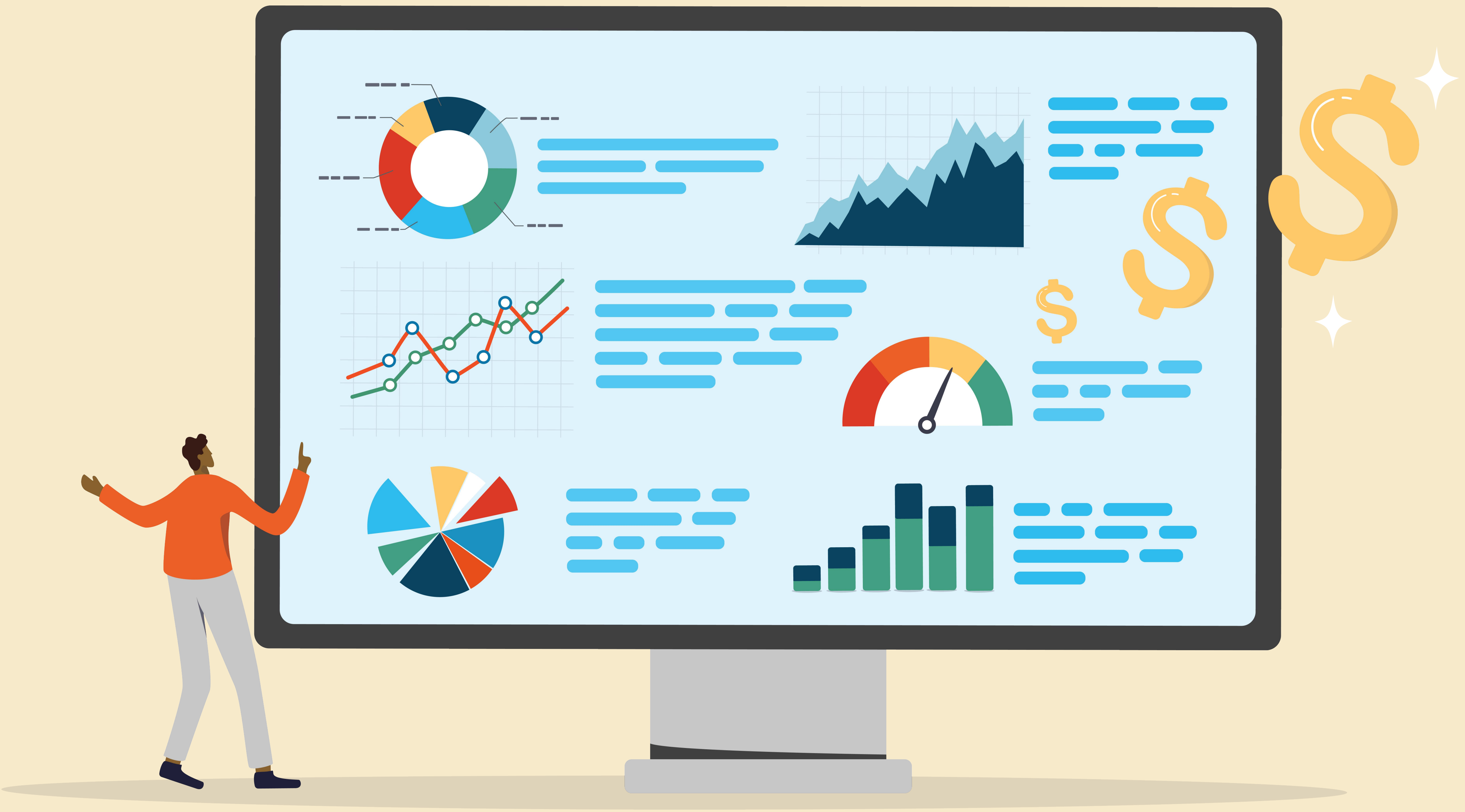
It's built on Microsoft Power BI, and it's free if you are using one of the LS Retail unified commerce solutions.
Discover LS Insight



Don´t let chance guide your business decisions

Success in business depends on many factors. Some of the most important ones are a clear vision, a sense of timing, a bit of luck, and the ability of selecting the right people and the right tools.

Do you need help finding a software solution that can give you the visibility you need to track and build your success?



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