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Bed Bath & Beyond: Is Online the Solution?[[1]](#endnote-1)

Wolfgang Messner, Suzanne Ducker, and Katherine C. Wilson wrote this case solely to provide material for class discussion. The authors do not intend to illustrate either effective or ineffective handling of a managerial situation. The authors may have disguised certain names and other identifying information to protect confidentiality.

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In December 2017, Bed Bath & Beyond Inc. (BBBY) announced its third-quarter earnings results, revealing a 50 per cent year-over-year decline in net profits and a 45 per cent decline in stock price as compared to the beginning of 2017. BBBY was facing a steady decrease in physical store sales even as digital sales showed growth.[[2]](#endnote-2) Steven Temares, then chief executive officer (CEO) of BBBY, acknowledged that “how [customers] discover product[s], their expectations and knowledge around pricing and services offered, and how they share their thoughts about their shopping experiences are all changing rapidly.”[[3]](#endnote-3)

But the rapid shift to online sales simply could not cover the losses in a business that historically depended on in-person shopping. Over the previous 10 years, BBBY had experienced continuously decreasing gross margins, pressure from shipping expenses for increasing online orders, lower merchandise margins, and expenses from discount coupons. In 2017, BBBY also spent US$264 million[[4]](#endnote-4) in capital expenditures for technology investments related to both online sales and improvements to store infrastructure, and its advertising and employment expenses increased.[[5]](#endnote-5)

Combined, the growing expenses and declining profits brought about significant questions about BBBY’s future and its ability to adapt in the rapidly changing retail market. Jaime M. Katz, a Morningstar equity analyst, noted,

These efforts are not enough to differentiate Bed Bath from its competitors that are undertaking similar efforts. […] We do not believe Bed Bath & Beyond has established an economic moat, given the brand’s limited pricing power, nonexistent consumer switching costs, and unsustainable cost advantages.[[6]](#endnote-6)

Now in 2018, how could BBBY stay relevant and competitive?

Company Background

BBBY, founded in 1971 by Warren Eisenberg and Leonard (“Lenny”) Feinstein, had its headquarters in Union, New Jersey.[[7]](#endnote-7) The retailer provided a wide variety of home furnishings and domestic merchandise, and its mission was “to be trusted by customers as the expert for the home and ‘heart-related’ life events.”[[8]](#endnote-8) It later expanded to include multiple subsidiaries that broadened its reach under these market categories, and it expanded to reach consumers through a combination of physical retail store locations, online e-commerce platforms, and mobile applications. The company went public in 1992 with its shares traded under the symbol BBBY on the Nasdaq Global Select Market.[[9]](#endnote-9)

BBBY had three main objectives: (1) provide customers with a variety of quality products; (2) provide services to assist customers in using these products; and (3) deliver an engaging and personalized shopping experience. The company’s focus on the “home and heart life events” was bolstered by specialized offerings for wedding and baby registries, student and new home transitions, and home decoration.[[10]](#endnote-10)

By the end of 2017, the company had over 1,530 stores, covering all states of the United States, Puerto Rico, and Canada. Of these stores, 1,020 were store locations for BBBY, 280 for Cost Plus World Market, 100 for Buy Baby Inc., 80 for Christmas Tree Shops, and 50 for Harmon Stores Inc. (see Exhibit 1).[[11]](#endnote-11) The company owned three distribution facilities and leased about 10 others to support these retail locations; it also had more than seven locations for institutional sales-related functions. BBBY had also expanded into the Mexican retail market through eight joint ventures.[[12]](#endnote-12)

BBBY was jointly led by Temares and the company’s original founders, Eisenberg and Feinstein, who were both co-chairs of the board. Klaus Eppler was appointed as lead independent director to serve an independent interest, in line with Nasdaq listing rules. The board of directors included three executive and seven independent members, who were tasked with electing the company’s executive officers for one-year terms. Eisenberg, Feinstein, and Temares were all members of the board of directors in addition to serving as executive officers for the company.[[13]](#endnote-13)

The founders of BBBY played key roles in the company’s leadership team. From the company’s start in 1971 until 2003, Eisenberg and Feinstein held positions as co-CEOs, and from 1992 until 1999, Eisenberg served as chairperson while Feinstein was the company’s president. Since 1999, the pair had held positions as co-chairmen. Although both elected “senior status” under their employment, the two co-founders actively continued to bring their extensive retail industry and company experience into BBBY’s strategy and operations.[[14]](#endnote-14)

Temares, who graduated first from Rutgers University with a major in economics and a minor in philosophy and then from the University of Pennsylvania Law School, in 1983,[[15]](#endnote-15) joined BBBY’s team in 1992 as the director of real estate and general counsel. He had played a part in the leadership of BBBY throughout its time as a public company. In 1997, Temares was appointed chief operating officer and executive vice-president. In 1999, he became the company’s president, and when he was named CEO in 2003, his company leadership was informed by over 20 years of experience with BBBY.[[16]](#endnote-16)

Industry Background: E-commerce

Prior to the mid-1990s, electronic commerce (e-commerce) had mainly involved phone orders from catalogues and advertisements on television or in magazines. The 1990s were characterized by a more widespread use of personal computers along with development of the Internet. In 1994, Mosaic Communications Corporation announced the release of a free Internet browser, Netscape, and soon, the first efforts toward advertising and marketing on the Internet started. This was considered the beginning of the current e-commerce industry.[[17]](#endnote-17)

High speed connections were developed, and trust with online vendors was established. Part of that trust included transparency and protections for consumers with regard to filling orders, making payments, and returning items. With these foundations in place, companies such as eBay Inc. and Amazon.com Inc. (Amazon) began to expand their reach in the e-commerce market. In 1995, Amazon shipped its first online book sale, and in 2002, the company made its first profit.[[18]](#endnote-18) By 2016, the online retailer reported over 310 million active customer accounts globally.[[19]](#endnote-19)

Characterized by rapid growth and continuous transformation, the e-commerce industry changed the way consumers interacted with markets. Online shopping developed from basic product purchases to a more interactive experience where consumers customized products, managed membership and rewards accounts, and engaged with fellow customers through online product feedback. Online retailers soon began to offer personalized shopping experiences tailored to customer preferences and previous purchase patterns, made shipping of online purchases easy and fast, and offered simple and flexible return policies.[[20]](#endnote-20)

The convenience and price transparency of online shopping turned e-commerce into a major competitor for physical retail stores. With online retailers expanding into nearly every industry, physical stores found it difficult to compete in attracting customers and matching the ever-lowering prices from online sources. In the United States in 2017, e-commerce accounted for more than 18 per cent of houseware and home furnishings sales, and the expectation was that the proportion was likely to grow.[[21]](#endnote-21) Footfall in shopping malls and brick-and-mortar stores continued to decline. Many companies that had traditionally centred on sales from physical store locations were therefore quickly developing strategies for transitioning into the e-commerce market to avoid losing their market presence.

BBBY’s Challenges and New Strategies

In this rapidly changing retail environment, BBBY had to transform quickly in order to survive the increased competition with online platforms such as Amazon and megastore companies such as Walmart Inc. In early 2017, BBBY lowered the free shipping threshold for online purchases from $49 to $29, but this left the company with fewer, smaller online sales.[[22]](#endnote-22) And absorbing shipping costs (especially on larger items) reduced the margins. Nonetheless, BBBY showed growth in digital sales even as its physical sales continued to decline, and by 2017, the company’s online business represented roughly 15 per cent of its overall sales.[[23]](#endnote-23)

Analysts noted that “given that the company’s investment in digital initiatives have come later than many of its competitors, [BBBY] does have a lot of scope to grow further and offset the declining foot traffic.”[[24]](#endnote-24) Competing with established Internet retailers came at the price of overall shrinking gross margins (see Exhibit 2),[[25]](#endnote-25) but the company still held an 11 per cent share of the US domestic home furnishing retail market at the end of 2016.[[26]](#endnote-26)

In an effort to increase customer stickiness and rival competitors’ online member services, such as Amazon Prime, BBBY launched its membership program, Beyond+, in 2017. For an annual membership fee of $29, Beyond+ offered customers a flat 20 per cent off all purchases plus free shipping for any order.[[27]](#endnote-27) In addition, the retailer provided coupons to prospective and existing customers alike for 20 per cent off one single item, $20 off a purchase over $75, or simply $5 off any purchase. The coupons were generously distributed through email distribution lists, traditional mail campaigns, print catalogues, and advertisements in magazines. However, many of the brand name items were also available from other online retailers at low prices.[[28]](#endnote-28)

Morningstar, the investment research company, considered BBBY to have no sources for an economic moat (see Exhibit 3);[[29]](#endnote-29) that is, it was a company without a sustainable competitive advantage:

As the company competes in largely commoditized retail categories with ample domestic brick-and-mortar and online rivals, we believe the lack of moat has become evident in the frequency and size of couponing, which underscores a consistently promotional environment (with few indicators of a near- to medium-term reversal or abatement) and the price-sensitivity of the consumer base, which has easy access to pricing comparisons through use of smartphones and other handheld devices.[[30]](#endnote-30)

BBBY also initiated a series of structural and managerial changes. Capital expenditures were high, so the company was looking at increasing the pace of store closures when leases came up for renewal and favourable terms could not be negotiated.[[31]](#endnote-31) BBBY’s stores were big and inefficient—with an average floor space of nearly 44,000 square feet, only generating $239 in sales per square foot. In comparison, an average store of the consumer retail company Williams-Sonoma Inc. had a floor space of just over 10,000 square feet but generated $392 in sales per square feet.[[32]](#endnote-32)

BBBY closed approximately 15 stores in the United States in 2017. Management restructuring efforts that same year resulted in a reduction of 880 department and assistant store manager positions, and organizational changes were expected to result in future pre-tax cost savings of $16 million.[[33]](#endnote-33) Still, BBBY’s stock price dropped to a low of $24.47 in December 2017[[34]](#endnote-34) from a high of $66.84 in September 2014 (see Exhibit 4).

BBBY tried to catch up with competitors in digital initiatives, gain and retain customers through discount and membership programs, and keep a close control on costs. Temares publicly expressed his optimism:

We have made considerable progress in our ability to align the organizational resources to accelerate our strategic priorities. . . . Each of the initiatives we are working on has its own framework and structure built around cross-functional coordination to expedite results, to further our mission, and to drive greater efficiencies to achieve operational excellence.[[35]](#endnote-35)

Temares’s reliance on efficiencies and resources was laudable, but he needed to keep BBBY relevant and competitive in the long term in a retail sector that was evolving at breakneck speed.

the Evolving Retail Sector

Leading management consulting companies and other business news outlets published thought leadership viewpoints based on their knowledge of the retail sector, understanding of the trends and events, and deep insight into the market players’ potential challenges throughout 2016 and 2017.

Customer Journey

The traditional model of the customer journey consisted of six steps. First, prospective customers experienced a “trigger” or an event that motivated them to look for a certain product or service. From there, they found an initial consideration set from which they eventually purchased or not. Next, they actively evaluated and narrowed their selections. However, during this time, they may have added other brands to their consideration set. Then there was the all-important moment of purchase, the post-purchase experience, and if this experience was a good one, the loyalty loop (see Exhibit 5).

Traditionally, a retailer’s most substantial growth came from targeting existing customers with marketing and advertising, which meant focusing on the loyalty loop. However, more recent research showed that top-line growth was actually coming from bringing in new customers. McKinsey & Company published a study in 2017 that pulled numbers from their consumer database of over 125,000 consumers and over 350 brands. They divided those customers into three categories: loyalists, vulnerable re-purchasers, and switchers. Loyalists were those who re-purchased the same brand without shopping around. Re-purchasers tended to shop around and evaluate other brands, but ultimately re-purchased the same brand. Switchers shopped around and purchased different brands. Loyalists made up only 13 per cent of the sample, meaning an overwhelming majority of customers were shopping around. Of the 87 per cent who were shopping around, 29 per cent were vulnerable re-purchasers and 58 per cent were switchers.[[36]](#endnote-36)

In the digital age, shopping around was not a choice; it was a side effect of simply shopping. More companies were able to reach customers during their active evaluation and make their way into the consideration set, dislodging others. It was therefore important to study customer behaviour and preferences well before the moment of purchase—and even before customers’ active evaluation.

Shift to Subscription Models

The subscription economy became more popular in 2017. Subscription-based business models allowed businesses to build continuous relationships with their customer base by translating single purchases into multiple purchases. This model was attractive to firms because it gave easy access to customer behaviour and usage data, and it made predicting future revenue much more reliable. Many traditional retailers launched subscription-based services in an attempt to capture a segment of the market they felt they had been missing.[[37]](#endnote-37)

Companies like New York & Company Inc. and Ann Inc.’s Ann Taylor launched “rent the runway”–style programs wherein customers paid a monthly fee for access to an unlimited online closet. Both programs allowed customers to rent three items at a time, return them when they were ready for new items, and purchase an item from the box should they choose to keep it.[[38]](#endnote-38) Gap Inc.’s Old Navy launched a subscription service for children’s clothing. The “Old Navy Superbox,” a quarterly subscription for children aged 5 to 12 years, contained six clothing items valued at $100 and sold for $70.[[39]](#endnote-39) All the parent needed to do was choose the child’s size, gender, and style.

Under Armour Inc. offered the “Armour Box.” Customers took a style and usage quiz; received four to six items for no initial fee; had seven days to evaluate the items and return unwanted items; and paid only for those they kept. The advantage to customers of the Armour Box was a 20 per cent discount on any items that were kept.[[40]](#endnote-40) Target Corporation also jumped on the subscription trend, offering a “Beauty Box,” a “Cat & Jack Baby Box,” and for children, a “Cat & Jack Outfit Box.” Target’s boxes could be ordered quarterly or one time only, and they were available at the start of each season.[[41]](#endnote-41)

The drawbacks to subscription-based business were threefold: (1) it was expensive to attract customers; (2) customers were not loyal; and (3) customers were not exclusive. To attract customers, subscription-based businesses had to buy customers’ business. The retailers artificially depressed the prices of their products or spent heavily on marketing and advertising. Eventually, the retailers needed to raise prices or expand their market or industry base. Low subscriber loyalty was attributed to “churn”—attrition among individuals in certain groups[[42]](#endnote-42)—which was sensitive to both competition and price. Lastly, given the many options customers had for their subscriptions, it was impossible to gain exclusivity with any one customer. Ultimately, the boom in subscription-based business meant that there was not enough market demand to meet the supply.[[43]](#endnote-43)

Building Customer Experience through Human Interaction

Artificial intelligence (AI) in retail allowed consumers to expand their shopping and purchasing opportunities through augmented reality, such as virtual shopping. But “experience disconnect” was a main drawback of AI in retail. It occurred when, despite having an enhanced shopping experience and ease of access to products and services, customers were still dissatisfied with the experience.[[44]](#endnote-44) A survey conducted by Pricewaterhouse Coopers (PwC) in 2018 found that 75 per cent of consumers wanted more human interaction rather than less, and almost 75 per cent of consumers thought that experience trumped price and quality. Further, 65 per cent of surveyed consumers said that brand experience beat advertising when it came to making a purchasing decision. With regard to human interaction, the same survey showed that customers abandoned a brand after several bad experiences, and 32 per cent changed brands after just one bad experience.[[45]](#endnote-45)

Companies were putting the emphasis back on experience by creating communities for their customers, empowering their employees, and hiring employees versed in data analytics. Nordstrom Inc. and Amazon turned the usual retailing experience upside down. Nordstrom opened a boutique in Manhattan exclusively for men. In addition to custom tailoring services, the boutique offered shoe shines and virtual dressing rooms. A visit to the boutique was a memorable event rather than just an errand. Amazon opened its first brick-and-mortar store, Amazon Go, which was a cashier-less grocery store. While the experience was a novelty in its own right, employees were still able to connect with shoppers by helping them to locate items or prepare food.[[46]](#endnote-46)

Another company that focused on curating experiences was REI (Recreational Equipment Inc.), the popular recreational and outdoor equipment co-op. It encouraged its employees to explore the outdoors, have their own experiences, and share these experiences and engage with customers under the hashtag #OptOutside.[[47]](#endnote-47) The #OptOutside movement was so successful that it became a part of REI’s customer-facing culture.

Lastly, in order to drive the customer experience, retail employees needed to be able to understand and use the data available to them. This meant understanding analytics, supply chains, marketing, and technology. Organizations like the National Retail Federation and UpSkill America offered specialized training to make future retailers more well-rounded and better able to meet the changing needs of the sales world.[[48]](#endnote-48)

PwC’s study shed light on five themes for garnering customer loyalty through experience: (1) delivering the right experience, (2) driving loyalty, (3) keeping it simple, (4) prioritizing employees, and (5) investing in the experience.[[49]](#endnote-49)

Theme 1: Deliver the Right Experience

Providing customers with the experience they were expecting carried a hefty price premium. At most, a great experience could earn a company a premium valued at 16 per cent. Providing the right experience required information about what customers wanted; 63 per cent of surveyed consumers stated that they would allow brands they trusted to collect and track their data.

Theme 2: Drive Loyalty

Conversely, delivering a bad experience meant a drastic drop in customer loyalty and sales. For brands they loved, 59 per cent of Americans said they would walk away after several bad experiences, and 49 per cent of Latin Americans said they would walk away after just one bad experience. The numbers varied by country and culture, but the theme was clear: bad experiences lost customers.

Theme 3: Keep It Simple

Stand-out customer experiences, while aided by innovation and cutting-edge technology, were based on simple things: efficiency, convenience, and helpfulness. Almost 80 per cent of consumers in the United States were more concerned with the essentials of the experience than with the “wow” factor.

Theme 4: Prioritize Employees

Taking care of employees meant that they in turn took care of customers, and as a result, customers kept coming back. Incentivizing employees and focusing on the element of human interaction addressed the needs expressed by 82 per cent of American consumers and 74 per cent of consumers in international markets outside the United States.

Theme 5: Invest in the Experience

Customers drove revenue, and experience drove customer engagement. Over 70 per cent of consumers said that experience was more important than price or quality when it came to making a purchasing decision. However, 54 per cent of American consumers thought that companies were not putting enough focus on experience. According to PwC, only 10 per cent of companies were prioritizing experience as part of their branding, which was in line with the disconnect that their customers felt.

Showrooming

The same PwC survey also found that, for the fourth year in a row, consumers had increased the amount of time they spent shopping in physical stores versus online outlets. When asked about shopping experiences, 53 per cent of respondents said they most valued an in-person interaction with a courteous and knowledgeable salesperson, whereas just 40 per cent valued personalized offers, and 39 per cent valued in-store screen displays.[[50]](#endnote-50)

Retailers needed to be especially attentive to the changing nature of the path from consumer to buyer, which was increasingly complex and resembled a journey more than a straight line from point A to point B. This explained consumers’ affinity for brands like Amazon, Alibaba, Apple, and Walmart, which had created best practices for gaining customer loyalty: create great value consistent with a wide selection while minimizing the stress, difficulty, and friction of the buying process. These companies illustrated where other companies needed to put their focus: in helping consumers as they navigated their shopping journey. It was no longer sufficient for retailers to simply follow the habits of consumers. Retailers that could forecast consumers’ habits and innovate accordingly to reinforce them were forecasted to win customers and their loyalty.

The future of retail seemed to be with voice-assisted home control devices like Google Assistant, Amazon Echo, and Alexa devices, or with Apple Inc.’s Siri. With the rise of the Internet of things (IoT), smart devices were expected to become more integrated with the shopping experience. Personal smartphone devices carried the capability for many of the tools essential to future shopping experiences, such as proximity marketing, personalized offers, and location- or time-based reminders. It was predicted that companies would leverage customers’ smart devices in tandem with cloud-based services to analyze and forecast customer preferences, behaviour, and habits.[[51]](#endnote-51) This allowed companies to create a start-to-finish personalized and interactive experience for the consumer. For the consumer, this meant being able to access information about the products they desired. In the long run, AI was expected to facilitate the relationship between the company and the consumer.[[52]](#endnote-52)

A 2016 Business Insider study showed that almost half of millennials were browsing online, or “webrooming,” while they were shopping in a store, and 84 per cent of shoppers webroomed before shopping anywhere.[[53]](#endnote-53) Retailers were therefore advised to connect with customers using omnichannel strategies. While the earlier consumer journey was shaped and evolved over years, with the increased integration of technology and access to knowledge, a reshaped journey now evolved over a matter of days. The companies that kept pace were predicted to capture the greatest share of customer loyalty and business.[[54]](#endnote-54)

BBBY’s Future

Summarizing BBBY’s situation in 2017, analysts like the Motley Fool painted a bleak picture:

Unfortunately, the retailer [BBBY] faces significant headwinds, and management doesn’t seem concerned enough about tackling them. . . .

It remains in the direct path of much bigger competitors, and it’s standing still like a deer in the headlights.[[55]](#endnote-55)

The same analyst later noted that “There’s simply no real reason for shoppers to keep visiting Bed Bath & Beyond, and the retailer’s desperate attempts to win them back will crush its earnings growth for the foreseeable future.”[[56]](#endnote-56)

In light of these dire predictions and emerging retail sector trends, could Temares keep BBBY relevant and competitive in the long term? What opportunities did BBBY have for encompassing some of the newer trends to ultimately stay relevant and successful in the home-goods market?

Exhibit 1: Bed Bath & Beyond, Company structure

|  |  |
| --- | --- |
| Retail Stores | Bed Bath & Beyond |
| Christmas Tree Shops |
| Christmas Tree Shops and That! |
| Harmon Stores, Inc. |
| Harmon Face Values |
| Buy Buy Baby Inc. |
| World Market |
| Cost Plus World Market |
| E-Commerce Platforms | Of a Kind Inc. |
| One Kings Lane Inc. |
| PersonalizationMall.com |
| Chef Central |
| Decorist Inc. |
| Linen Holdings LLC |

Source: Created by the case authors with information from “Corporate Profile,” Bed Bath & Beyond, accessed February 9, 2018, http://bedbathandbeyond.gcs-web.com.

Exhibit 2: Bed Bath & Beyond, Gross margins over the past ten years (in %)

Source: Created by the case authors with information from Jaime M. Katz, “Bed Bath & Beyond Inc. BBBY (XNAS),” Equity analyst report, Morningstar, March 3, 2018, accessed March 3, 2018, www.morningstar.com/stocks/xnas/bbby/quote.html.

Exhibit 3: Economic Moat



Source: Created by the case authors with information from “Moat Size,” Morningstar Investing Glossary, accessed November 15, 2018, www.morningstar.com/InvGlossary/moat\_size\_definition\_what\_is.aspx.

Exhibit 4: Bed Bath & Beyond, Five-year stock price

(December 2012—December 2017, in USD)

Source: Created by the case authors with information from Sydnee Gatewood, “Bed Bath and Beyond Falls Despite Earnings Beat,” Nasdaq, December 21, 2017, accessed December 17, 2018, www.nasdaq.com/article/bed-bath-and-beyond-falls-despite-earnings-beat-cm896089.

Exhibit 5: Customer journey and loyalty loop



Source: Created by the case authors with information from David Court, Dave Elzinga, Bo Finneman, and Jesko Perrey, “The New Battleground for Marketing-Led Growth,” *McKinsey Quarterly*, February 2017, 65–75, accessed October 15, 2018, www.mckinsey.com/business-functions/marketing-and-sales/our-insights/the-new-battleground-for-marketing-led-growth.

endnotes

1. This case has been written on the basis of published sources only. Consequently, the interpretation and perspectives presented in this case are not necessarily those of Bed Bath & Beyond Inc. or any of its employees. [↑](#endnote-ref-1)
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