

The Root Cause of Retail Shrink? Not Knowing the Root Cause

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Shrink is a persistent headache for retail.

In 2008, US retailers experienced approximately \$40 billion in shrink. After repeatedly failing to solve the problem, many managers conclude, wrongly, that shrink is simply a cost of doing business.

Why are they wrong? The most common mistake retailers make in trying to roll back shrink is the failure to get to the real root cause. That's not to say they don't have theories about the root cause. From headquarters to individual stores, we have heard much accepted wisdom about the alleged root causes of shrink: poor forecasting, undisciplined distribution systems, and theft, among others. Yet over 40% of the time, we have found that managers focus on the wrong culprit, and never do a thorough analysis of why shrink occurs. True, the managers' theories often point to a contributing factor to the shrink problem, but not the *primary* cause. As a result, retailers achieve some level of improvement from their efforts, but never really solve the problem or significantly improve their company's performance.

Case in point: a major US grocery retailer was experiencing fluid dairy shrink rates of 5% - more than twice the industry average – in a group of 300 stores. Initially, the business assumed that the issue was related to a high number of low-volume dairy SKUs (e.g., slower moving items) going past their expiration dates in the dairy case. So convinced by this theory, the company was prepared to reduce the variety of its dairy offerings.

We insisted that they bore down into the facts. We worked with them to conduct a rigorous root cause analysis of the problem and found that their real problem was faulty caps on one-gallon milk containers – one of the company's highest volume SKUs. Throughout the region, defective caps were popping off of milk gallons, resulting in significant product loss. By meticulously examining their every day process, we discovered the real root cause of lost milk. As a result, dairy shrink was reduced by 55% and the company saved over \$1 million per year.

The lesson: in the battle against shrink, it is vitally important for retailers to leverage intuition and experience, but rely on facts.