How to predict the future of retail

Understanding how retailers meet the levels of human need reveals how the industry will evolve.

Retail is dead. That’s what they’re telling us. They say that humans will have no need for physical stores when anything and everything can be delivered to our doorsteps. Shopping malls might as well close their doors. Doesn’t everyone buy everything online now anyway?

Well, no. Only about 7.4 percent of all U.S. retail sales occur online. And those crowds we continue to encounter on Black Friday or any given Sunday at the local mall seem as big as ever. While some predict a dire end for physical retail, the truth isn’t so simple. Some retailers will shrink their store footprints while others will grow. Some will employ automation and new technology, while others will not.

Decisions about expansion, contraction and new technology will all be made to meet shoppers’ demands. We can make predictions about which retailers will see which changes by using the framework of levels of human need as a guide. Which retailers meet which needs can help answer the big questions.

Only about 7.4 percent of all U.S. retail sales occur online.

The mystery of the lonely kiosks

The line was long at the drug store pharmacist window. On the wall, just next to the line were two kiosks similar in shape to ATM machines. As I waited, I read the instructions on the machine. Those who had called in their prescriptions ahead of time could make their payments at the machine and skip the line. Yet, not one of us in that long line had chosen to use the kiosks. In fact, I had never seen anyone use them.

Supermarket self-checkout lines, which offer similar promises of a shorter wait time, are now used by many shoppers. Why does one automated service fail to attract users while another quite similar one proves successful? The answer may be that while the technologies are similar, the human needs they were intended to meet are not.
In general, the higher the need that a product meets, the bigger the profit margin will be.

Mystery solved
Understanding how the hierarchy works explains why those prescription kiosks in the drug store went untouched on a busy weekend morning. Self-service checkouts in grocery stores have proven a popular option for shoppers on the run because supermarkets primarily meet needs on the lowest level of the hierarchy. At those lower levels, consumers are more likely to sacrifice human interaction for low cost and speed.

Drug prescriptions on the other hand, meet a health need, which is higher up the hierarchy. Not only are goods that meet health needs more expensive, but they are more likely to require human service. A parent with an ailing child wants to know his drug prescription is filled properly and appropriately. An ill shopper wants a pharmacist to guide her toward health and well-being. Machines are not good at any of these things. Is it any wonder that these shoppers willingly sacrificed time for human interaction?
Move up the hierarchy and the same product is worth more

Similar goods can show substantial variations in value, depending upon the level of need they are intended to meet. For example, there is no significant difference between tap water and bottled water. In the United States, with a very short list of exceptions, tap water is just as healthy as bottled water. Indeed, some municipalities employ additives like fluoride which actually make tap water the healthier choice.

Yet bottled water is marketed to meet needs far above basic thirst. “Natural” spring water is “pure” from “alpine” “mountains” infused with minerals, according to their labels. Many bottled waters also boast labels of foreign brands, islands and nationalities.

Tap water meets our most basic of needs, that of thirst. It is available to the most people and comes in no packaging which conveys status or exclusivity. Bottled water promises to meet not just thirst, but also health needs, a level higher up in importance than physiological needs. Exclusive origins and foreign packaging meet needs of esteem and status, another level higher. Higher need fulfillment comes with higher cost.

Nearly every retailer sells goods that meet a variety of needs. That’s why private-label store brands carrying little status are sold alongside nearly identical name-brand goods. Those who are able will pay a premium for status. One study found that filling a shopping cart with private label store brands saved about 30 percent over name brands. For a person that spends $100 per week on groceries and buys name brand goods, that would be an additional $1,500 per year paid in taxes to their higher order needs.

<table>
<thead>
<tr>
<th>Needs</th>
<th>Types of retailers that meet needs</th>
</tr>
</thead>
</table>
| Physiological (food, water, sleep) | - Grocers  
- Basic and discount apparel  
- Quick service restaurants |
| Safety (health, security, stability) | - Drug stores, urgent care, dentists, doctors  
- Tax preparers  
- Natural foods |
| Love and Belonging (friendship, love, family) | - Gift shops  
- Casual dining  
- Ice cream, sweets  
- Toys  
- Furniture |
| Esteem (success, respect) | - Fashion apparel and accessories  
- Automotive  
- Gyms |
| Self-actualization (reaching one’s full potential) | - Yoga  
- Spiritual book stores  
- Educational centers |
How to predict the future of retail

Understanding how retailers meet the levels of human need reveals how the industry will evolve.

Retail property subtypes and the needs they meet
Retail property segments with tenants that meet lower-order needs are at more risk of disruption. These retailers are more likely to successfully automate front-of-house functions, more vulnerable to price competition and less likely to require high levels of human interaction in order to be successful.

<table>
<thead>
<tr>
<th>Retail property segment</th>
<th>Segment description</th>
<th>Vacancy Rate (Q4 2015)</th>
<th>Vacancy compared with national average</th>
<th>Level of human needs met</th>
<th>Risk of disruption</th>
</tr>
</thead>
<tbody>
<tr>
<td>General retail</td>
<td>Single tenant, freestanding, general purpose retail with parking.</td>
<td>3.7%</td>
<td>Significantly higher vacancy rate than average for all retail. (+2.0%)</td>
<td>Lower level needs, including food, safety and health</td>
<td>Medium to high</td>
</tr>
<tr>
<td>Malls</td>
<td>Includes regional malls, super regional malls and lifestyle centers.</td>
<td>5.3%</td>
<td>Slightly lower vacancy than average for all retail. (-0.4%)</td>
<td>Love, belonging, esteem, friendship, family</td>
<td>Low</td>
</tr>
<tr>
<td>Power centers</td>
<td>Multiple freestanding anchors with minimal small tenants.</td>
<td>4.5%</td>
<td>Significantly lower vacancy than average for all retail. (-1.2%)</td>
<td>Food, health, security</td>
<td>Medium</td>
</tr>
<tr>
<td>Neighborhood, community and strip centers</td>
<td>Row of connected store fronts with common parking. May be grocery-anchored.</td>
<td>8.9%</td>
<td>Significantly higher vacancy rate than average for all retail. (+3.2%)</td>
<td>Food, health, security</td>
<td>High</td>
</tr>
<tr>
<td>Specialty centers</td>
<td>Airport retail, outlet centers and theme/festival centers.</td>
<td>5.7%</td>
<td>Vacancy rate the same as national average for all retail.</td>
<td>Love, belonging, esteem, friendship, family</td>
<td>Low</td>
</tr>
</tbody>
</table>
Why do people still buy records?
An understanding of the hierarchy of needs can help explain a whole lot of mysterious human behavior. For example, why do some people buy big bulky records when they can stream any music album on their phone or computer?

The record industry's traditional metric for success is the album sale. While overall album sales have been sliding, the sale of vinyl records jumped by 29.8 percent in 2015. Annual vinyl sales in the U.S. have climbed to almost 12 million records.

In a time when CD and digital album are shrinking, why has the less accessible, physically heavy and cumbersome record seen a resurgence? The answer is that vinyl records have now moved up another level in the hierarchy. Their very cumbersome nature now only adds to their allure. The true music aficionado is purchasing a record in order to meet his or her needs of status, esteem and community.

Meeting shoppers’ desires to be cool is an industry that will in large part persist in physical stores. Urban Outfitters is the second biggest seller of vinyl records in the world. They also sell cassette tapes. No word yet on 8-tracks or wax cylinders.

Shoppers are not efficiency robots, endlessly homing in on the cheapest and fastest option; human needs trump cost and efficiency. Economic models that assume humans will make the cheapest and easiest choices ignore the more complex desires of higher-order human needs.
Why Barbra Streisand’s basement points to the future of malls

Barbra Streisand grew up in Brooklyn in the 1940s. Her father died when she was young and her mother struggled to keep them afloat. Barbra never had any real dolls, just a hot water bottle she would fill with warm water and pretend was a baby. When Barbra Streisand grew up and became a cultural icon, she had the money to do whatever she wanted. So, she built a house with a private shopping mall in its basement. Her mall has among other things a candy store, a costume shop and a doll store.

There must be something special about a shopping mall that would compel a person to build one of her own.

Many shopping centers claim to deliver entertainment and a shopping experience to visitors, but you’ll note that there is no human need for entertainment on Maslow’s hierarchy. Millions visit centers such as the Grand Canal Shops in Las Vegas or the Mall of America each year not to be entertained, but rather to share something unique and special with their families and friends. These shopping malls aim to meet the higher needs of family, love and belonging.

How technology will be used in different retail segments

Virtual shoppers have come to expect unlimited access to goods from around the world. Mobile apps that provide goods or services are not expected to do everything well, but rather do one thing perfectly. Uber, for example, seamlessly connects riders and drivers. Apps are more like physical stores. Technology can help stores create a more perfect experience. But the successful implementation of technology will maintain a keen awareness of human needs.

Eatsa: Technology delivers efficiency and low cost

Retailers that meet needs on the physiological level of the hierarchy are ripe for technological innovation. They are more likely to compete on price and their customers are less likely to reject technology in place of human service.

At Eatsa, a quick-service restaurant with locations in San Francisco and Los Angeles, diners order from a menu of quinoa bowls via a touch screen in store or via mobile app. After ordering, diners wait for about two minutes in a front-of-house lacking in human employees. The diner’s name appears on the transparent window of a cubby hole. The diner touches the glass which opens a window and reveals the order. While there is a kitchen staff to prepare the food, those workers are completely invisible.

Eatsa offers a flashy high-tech experience, but that’s not the goal of its technology. The food offered is tasty and inexpensive. Eatsa delivers a good that meets a low-level basic need. In such a case, the aim of incorporating technology into the shopping experience is purely to lower costs and increase efficiencies.

As technologies improve and costs decrease, we can expect more of the same from daily needs retailers. As we have quickly become accustomed to self-service check-outs in grocery stores, so too will consumers quickly accept even more automated service at quick serve restaurants. However, for retailers meeting higher needs, personal human service is not so easily given up. For those retailers, technology can be employed in other innovative ways, often behind the scenes and beyond the gaze of shoppers.
b8ta: Technology connects buyers with sellers
To the casual visitor, b8ta is a store that sells electronic gadgets and other unique products. But behind the scenes, b8ta is very different. It's really not selling goods at all. Instead, b8ta is selling customers to manufacturers. That's because manufacturers purchase display space in b8ta’s stores. With one desirable storefront in the heart of Silicon Valley in Palo Alto and more to come, manufacturers can expect that a slot on b8ta’s shelves can translate into valuable exposure to higher order shoppers. B8ta employees are trained by the manufacturers on how to demonstrate products to customers. b8ta earns money regardless of sales figures. As long as it can deliver satisfactory customer interactions with the products, manufacturers will continue to pay to have their goods displayed in the store.

b8ta’s business model is hinged upon the idea that manufacturers believe they can sell more goods once consumers have experienced them. This should come as no surprise to those familiar with the hierarchy of needs. Goods sold to meet higher order needs require high-touch customer service and human interaction. In the heart of Silicon Valley, a store sells the least virtual thing of all: physical human interaction.
Higher needs will trend toward physical retail. Lower needs will be delivered in whatever format is cheapest and fastest

In these early decades of e-commerce, we have seen is that anything that can be digitized will be digitized. Any good that can be converted to information and transmitted over great distances will be converted and sold as such. Early victims of this shift included Borders Books & Music, Tower Records and Blockbuster Video. But the so-called war of clicks versus bricks is actually a false dichotomy. Nearly all successful retailers will have to operate in all spaces in order to succeed.

We can use the hierarchy of needs to predict which channels will be most useful to which retailer. A discount grocer with a customer base that is focused primarily on savings will find most of its product meeting basic physiological needs. Thus, this retailer can expect to meet consumer demand by continuing to offer many locations in high-traffic areas. (For more on how grocers are evolving to meet consumer expectations, read our report “Grocers compete, retail real estate wins.”) Furthermore, shoppers at these stores will more readily trade automation and an impersonal experience for savings and convenience.

Apparel sellers often meet higher needs such as esteem. These retailers are serving a smaller audience, but one that requires personal physical interaction. Luxury clothiers, for example, should never plan on ditching too many physical stores in favor of an online presence. That's because luxury shopping is not only a shared experience, it is one that thrives on feelings of status and esteem which cannot be felt in the online vacuum.

Most traditional online retailers should expect their futures to be in physical retail as well. Warby Parker, seller of hip prescription glasses, has already found this to be the case. Its goods, which are health-related (level 2) and fashionable (level 3) are most successfully experienced in a physical setting. This is why Warby Parker has now opened physical stores. The list of pureplay online retailers that deliver higher level goods only online will dwindle.

While e-commerce as a percentage of online retail is still growing, that growth has slowed. In fact, a forecast from Bain & Company finds that e-commerce penetration will plateau at about 20 percent by 2030. Ninety percent of computer sales will be made online by 2030. Apparel sales will plateau at around 25 percent. Furniture, cosmetics and grocery sales will continue to occur mostly in physical stores.¹

Which channel a retailer uses will depend on which needs it caters to, but the future is certain to have a mix of online commerce as well as physical stores. In addition, the use of automation in physical stores will be most successful in retailers that meet lower orders of human needs.

¹ Bain Retail Holiday Newsletter 2015-2016 Issue #4, Bain & Company, Inc.
About JLL
JLL (NYSE: JLL) is a professional services and investment management firm offering specialized real estate services to clients seeking increased value by owning, occupying and investing in real estate. With annual fee revenue of $4.0 billion and gross revenue of $4.5 billion, JLL has more than 200 corporate offices, operates in 75 countries and has a global workforce of approximately 53,000. On behalf of its clients, the firm provides management and real estate outsourcing services for a property portfolio of 3.0 billion square feet, or 280.0 million square meters, and completed $99.0 billion in sales, acquisitions and finance transactions in 2013.

Its investment management business, LaSalle Investment Management, has $50.0 billion of real estate assets under management. JLL is the brand name, and a registered trademark, of Jones Lang LaSalle Incorporated. For further information, visit www.jll.com.

About JLL Research
Jones Lang LaSalle’s research team delivers intelligence, analysis and insight through market-leading reports and services that illuminate today’s commercial Real estate dynamics and identify tomorrow’s challenges and opportunities. Our more than 400 global research professionals track and analyze economic and property trends and forecast future conditions in over 60 countries, producing unrivalled local and global perspectives. Our research and expertise, fueled by real-time information and innovative thinking around the world, creates a competitive advantage for our clients and drives successful strategies and optimal real estate decisions.

About JLL Retail
JLL’s retail experts partners with retailers, investors and owner/operators with an extensive team of dedicated experts around the world. They understand the inherent complexities and variability associated with both the retail industry and increasingly complex capital markets. Its specialists are recognized for their independent and expert advice to clients, backed by industry-leading research that delivers maximum value. With leading in-depth knowledge of the local, regional and global market dynamics, JLL aims to truly partner with its clients for the entire lifecycle of an asset or lease. Its experts deliver clients maximum value that support and shape their investment, site selection and brand strategies.

JLL is the largest third party retail property manager in the United States with more than 1,000 centers, totaling 125 million square feet under management. The firm has more than 140 retail brokerage experts spanning more than 30 major markets, representing more than 900 retail clients. In 2015, JLL’s Retail Group completed transaction management and portfolio optimization on 1,500+ leases, negotiated 500+ leases for retailers and 1,000+ leases for landlords and completed more than $2.7 billion of investment sales, dispositions and financing for investors. For more news, videos and research from JLL’s Retail Group please visit: www.jllretail.com.

© 2016 Jones Lang LaSalle IP, Inc. All rights reserved. All information contained herein is from sources deemed reliable; however, no representation or warranty is made to the accuracy thereof.