Staples, Inc.: Revising the Strategy

**Taking Over**

Back in January 2002, Ronald Sargent assumed the reins of office supply superstore Staples from founder Thomas Stemberg. At that time, Sargent and Staples faced many challenges. The office supply market seemed to be maturing-industry sales in 2001 actually shrank 3 percent after years of double-digit growth. Further, although Staples had significantly more stores than its two major competitors-Office Depot and OfficeMax-it trailed Office Depot in sales revenue.

There were bright spots for Staples-whereas both Office Depot’s and OfficeMax’s sales had declined 5.6 percent and 9.7 percent, respectively, in 2001, Staples’s sales had inched up 0.7 percent; and its profits had soared from just US$59.7 million in 2000 to US $265 million in 2001. Yet, analysts noted that Staples’s return on net assets (RONA) was below its weighted-average cost of capital (WACC) and argued that the firm needed to improve its profitability. Sargent knew he had his work cut out for him.

**Taking Stock**

Sargent began by questioning one of the company’s basic strategic assumptions-build a store with lots of inventory and the lowest prices in town and customers will beat a path to your door. Under this philosophy, Staples operated 400 more stores than OfficeMax and 541 more than Office Depot. Staples’s stores typically stocked its stores from floor to ceiling, warehouse style, with all sorts of products. Yet, Staples’s sales revenue per store was well below Office Depot’s.

Sargent therefore decided to slow the company’s store expansion. He also closed 32 underperforming stores, the largest store closing in the company’s 16 year history. Moreover, the company planned to open only 115 new stores in 2002, down from 160 in 2001. It would also open most of these new stores in existing markets rather than new market areas in order to take advantage of operating efficiencies.

Further, focus groups with Staples’s target market of small-business customers indicated that those customers did not like the warehouse look. Customers wanted to be able to see across a store and to determine quickly from signage where items were located. Staples responded by experimenting with a smaller store (1860 square metres versus about 2230), lower shelving and a more open atmosphere. This meant that it had to reduce inventory. As a result, the company removed many items that it found were not necessary, such as child-oriented computer games and educational software. Based on customer feedback, it also stopped offering some business services, such as health insurance or prepaid legal services, so that it could focus on consumable products. Customers, it found, did not want to shop at Staples for these services.

The results with this new store format proved promising, with sales increasing up to 10 percent with about 10 percent less inventory. Sargent noted, “We’re doing the same sales volume with two printers selling for more than [US] $100 than we did selling five printers at the different price points.” As a result, Sargent decided to roll out the new format and reconfigure 280 stores in 2002 in hopes of improving both sales and inventory turnover. Staples’s inventory turnover ratio was about 5.1 times as compared with Office Depot’s 6.3 times.

As a second part of his strategy, Sargent turned to what the company called its “North American Delivery” segment. This segment includes the company’s Internet, catalogue, and corporate contracts operations-all of its operations that bypass its stores. In 2001, this segment accounted for 28 percent of sales and 40 percent of profits. Competitor Office Depot got 34 percent of its sales and 33 percent of its profits from similar operations. In a Home Furnishing Network survey of website traffic for the first four months of 2002, Office Depot had the highest number of unique website visits, more than 24 million, of the top 20 retail websites, ahead of Best Buy, Wal-Mart, Target, and others. Staples’s site, [www.staples.com](http://www.staples.com), came in seventh, with just fewer than 14 million visits, while OfficeMax finished tenth, with just fewer than 10 million visits. Forbes magazine named Staples’s site as the “Best of the Web Pick for Entrepreneurs” for the third year in a row, based on its ability to assist smaller businesses to run as smoothly as larger organizations.

To handle its catalogue operations, Staples has a subsidiary, Quill.com. A survey ranked Quill.com as highest in terms of its online sale conversion rate of 30.3 percent versus the average site’s rate of 8 percent or lower. Quill offered 35 percent of its products as private label brands as compared with 7 percent for Staples. Sargent saw this as an opportunity for Staples to offer more of it own private-label brands that carried higher margins.

Although Staples built its business by targeting small business while OfficeMax had targeted house-hold consumers, it also developed programs for businesses with more than 100 employees. Its StaplesLink program allowed companies to link their internal procurement systems with Staples’s computer systems. This allowed users to place their orders directly with Staples, which then prepared the order and delivered it to the business the next day.

For both its catalogue and contract businesses, Sargent believed that Staples should beat a path to customers’ doors. He ordered the doubling, to 400, of Staples’s special sales force, which worked with customers to get them to order through its catalogue or its website. He also added 100 staff members to the 600 person sales force that worked exclusively with corporate and small-business accounts.

To help get small-business customers into the stores, Staples entered a test with FleetBoston Financial Corp. to open ten offices in select Staples store in the Northeast. These 14 square metres, in store offices would have two Fleet staff members who would work with business owners to open specially designed business chequing accounts, get debit cards, and make small-business loan applications. The offices would not dispense cash or take deposits and would be open six or seven days a week. Fleet had more than 100 non-traditional branches, mostly in supermarkets.

Next, Sargent planned to continue Staples’s international expansion. The retailer already operated 180 stores in the United Kingdom, Germany, the Netherlands, and Portugal. It planned to add 20 new stores in Europe and to open in one more country. European operations accounted for about US $796 million of sales in 2001.

Finally, Sargent focused on customer retention. He understood that getting a customer was expensive. The company estimated that a customer doing business for three years was 4.5 times more profitable than a new customer. Staples’s managers estimated that the company had a 30 percent share of their customers’ office supply purchases, and they wanted to increase that share.

**Taking the Challenge**

Sargent knew that Staples’s 53000 employees would have to execute all of these strategic moves for the company to reach its target of US$12 billion in sales and US$440 million in net income by 2003. And, he knew that competition was only going to intensify. The struggling OfficeMax was trying to capture more of Staples’s small-business customers. These customers were often willing to buy higher-margin items, thus leading to Staples’s higher-than-average margins. In an industry with lots of stores, catalogues, and internet sites offering similar merchandise at similar prices, maintaining a competitive advantage would not be easy. Further, Sargent worried about offering the same products and services to the same customers through multiple channels. Would this strategy generate channel conflict within the company?