OnLine Case 10.4
Next

At the end of 1988 George Davies lost the chairmanship of Next, the retail company that he had built which had experienced rapid growth and success during the 1980s. Recent strategic changes had failed to provide the desired level of success. Arguably, the speed of the growth and the extent of the diversification had been too great for Next's resources, and profits had fallen as a result. Over four years and with a series of strategic moves, Davies had transformed the relatively dowdy menswear retailers J Hepworth into Next, a group which was innovative, design led and fashion orientated. J Hepworth had started trading in 1864 and had divested into womenswear only in 1981 when it bought Kendalls. The Next brand began life a little later.

Next segmented the retail market, selling fashionable clothing to younger men and women, as well as for children and as well as jewellery and furniture. However, alone a strategy of targeting new segments is not a source of sustained advantage. Rivals will soon see the new opportunity and seek to move in. In addition, Next had diversified into general mail order by the acquisition of Grattan, one of the largest catalogue retail operations.

The moves which proved problematical occurred in 1987 and 1988. In 1987 Next took over Combined English Stores (CES), a large and already diversified retail group which included Biba (the West German fashion retailer), Zales (jewellery), Salisbury's (luggage, handbags and the like), a chain of chemist's shops, a carpet business and a holiday company. This gave Next a substantial high-street presence, together with the problem and expense of converting a large number of stores to the fashionable Next image and format, which was regarded as a key factor in their record of success. Critics argued that Next had acquired too many stores, however, and Zales and Salisbury's were sold to Ratner's in autumn 1988. This reduced the extent of Next's diversification, and helped to reduce the gearing from 125%.

In January 1988 the Next Directory, an exclusive mail-order catalogue, was launched and *sold* to potential customers through advertising and direct mail. At this time catalogues were normally free. The product range in the Directory was designed to appeal to upmarket buyers, not the traditional mail-order customers, who could specify when they wanted their goods delivered. The launch and the new concept proved less successful than forecasts and expectations. Moreover, in 1988 there was growing friction between Next and Grattan. Grattan disagreed with Next's plans to redevelop their product line. Davies has claimed that in October 1988 there were serious discussions about splitting Next and Grattan.

At the end of 1988 Next's profitability had declined, its strategy was not co-ordinated, and there were concerns about a fall in demand in 1989 as a result of increased interest charges and inflation.

question: Had the diversification into mail order and the acquisition of Combined English Stores been appropriate and feasible?

Next was unable to provide all of the necessary resources at the time they were required; and George Davies was quoted in the *Financial Times* on 5 December 1988 as saying, 'The lesson that I've learnt this year is that you must stick to the markets you know'.

Next, also, was a highly innovative company, yet Davies was seen as an autocratic strategic leader who had failed to develop an appropriately supportive team of managers and an organization that was sufficiently decentralized.

After Davies' departure Next concentrated on two principal businesses:

- retailing ladies', men's and children's clothing, accessories and home furnishings – the remaining retail businesses were divested
- the Next Directory – Grattan was sold to Otto Versand, the German mail-order company.

George Davies, whose subsequent collaborative alliances with ASDA and Marks & Spencer have both been successful – he introduced the George range of clothing tp Asda and per Una to M&S - was replaced as chief executive by David Jones, who had joined Next when it acquired Grattan. Jones has been described as a cautious, conservative accountant.

I probably gamble a little more than people think, but only when I have the information to ensure it is a safe bet.

(David Jones)

Jones' strategies for rationalizing and consolidating the business proved very successful and by the end of 1995 Next had been turned around.

	Index of sales revenue (1986 = 100)	**Trading costs as a % of turnover**	**Return on capital employed**
1986	100	88	11.4
1989	500	97	6.7
1992	255	93	19.2
1994	344	86	33.6

The figures show how quickly sales revenue rose during the 1980s with the acquisitions and the more aggressive retailing style, but costs were also rising and profitability was falling. With divestments sales then fell, before rising again. Under Jones the return on capital advanced steadily. In 1995 Next was not only profitable, it had accrued cash reserves of £150 million.

question:

What strategies would be appropriate, desirable and feasible for utilizing these resources effectively?

In the event, there was some international expansion but no major acquisitions. Paradoxically, once there were no major crises to deal with, some complacency set in. Next sales fell back during 1998, the first reduction during the 1990s.

- There had been operational misjudgements – resulting in inadequate stocks of the best-selling lines of women's and children's wear.
- By switching its range emphasis to provide a stronger appeal to 'higher fashion' customers Next had partially taken its eye of its core customers.
- The problems were compounded by complacency over issues at the store level. After the run of success Next management had turned its attention more to improving its warehousing and logistics.

Jones commented: 'We do not have a divine right to be successful'.

The real danger was that some customers might have been lost permanently to rival high-street retailers.

question: David Jones has clearly been successful – and he remained as strategic leader. But: could a case be made for ensuring that he had a 'partner' with a greater willingness to take risks and who would deliberately seek to stretch the organization more?

In 1999 Internet selling was added to the Next Directory operations; and in 2001 flowers were added to the Internet product range.

Next began to experiment with a new larger store format. It was successful and several more have been opened. At the same time some of the smallest stores have been closed down. As a result the average store size has gradually increased from 5000 to 7000 square feet.

David Jones became Executive Chairman in 2002 and Simon Wolfson (from a family of renowned retailers linked previously to Great Universal Stores) was appointed as CEO in his place. The first true overseas branch of Next was opened in Denmark in 2004; previously Next had operated through franchises. The company was also offering call centre service facilities to customers such as British Gas through its Ventura subsidiary.

Between 2002/3 and 2003/4 the company was clearly growing. UK Retail now accounted for some 72% of turnover and profits. The Next Directory (21%), Ventura (5%) and overseas franchises made up the rest.

By 2005 Next was being affected by a resurgent Marks & Spencer and the market generally was changing with the increasing popularity of low price clothing from Primark, Matalan and Asda. However Next's catalogue sales were doing well, as were direct sales through the Internet. The new larger stores programme continued. In 2007 it was commented that Next was still struggling with in-store ranges, displays and competition.

Question: It has been said that whilst David Jones was in charge, Next was not very exciting in terms of acquisitions and divestments – but it seemed to have a clear strategy. And maybe this is just what it needed. What do you think?How well structured and prepared for the 2008-9 recession do you think Next was?

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