

Chern's Company History and Organization

Siblings Ryan and Ann Chern founded Chern's, an upscale men's and women's department store, 20 years ago after they graduated with their MBAs. The pair had planned to launch their own company for years, and refined their business model after each spent a great deal of time learning about the retail industry by working in different retail organizations. The product mix and high-quality products Chern's sells made it rapidly successful, and the company developed a loyal following. The firm quickly expanded its product line and began opening additional locations 15 years ago. Ryan and Ann have turned their basic idea of providing customers with the best service, selection, quality, and value into a thriving business. The two are now co-presidents of Chern's: Ryan serves as the company's chief executive officer; Ann serves as the company's chief operating officer.

Chern's pursues an aggressive growth strategy. Currently the company has 140 stores in 28 states on the East Coast and in the Midwest. Chern's employs an average of 19,000 full- and part-time employees. Providing superior customer service has been the company's main business strategy and has successfully differentiated it from its competitors. Although the company's products are expensive, the high product quality and excellent customer service have made the company successful. Because customers' tastes can differ from one store to the next, the company tries to be as decentralized as possible. Therefore, it gives its store managers a considerable amount of discretion in terms of how they run their stores. Likewise, each manager runs his or her own department as a small business and is rewarded according to the department's and the store's overall success.

Because customer service lies at the heart of the company's business strategy, it is a core part of the corporate culture of Chern's. Ann and Ryan believe that customer service is the essence of selling and that because the firm's sales associates are in direct contact with customers, they are the core drivers of the company's performance. Both department managers and assistant department managers support the sales associates. Besides giving the sales staff their full support, the department managers at Chern's are, in turn, supported by their store managers, assistant department managers, buyers, and merchandising managers. **Figure A-1** illustrates these relationships.

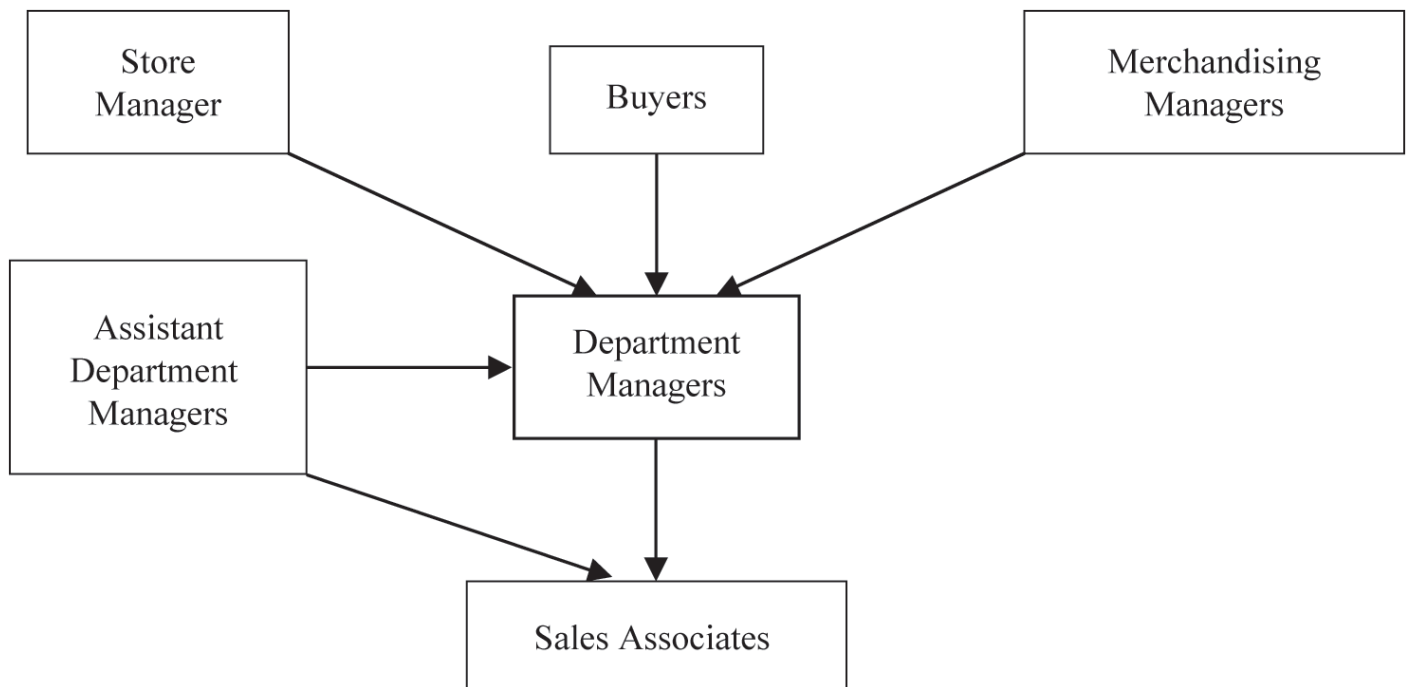


Figure A-1 The Sales Support Relationships among Chern's Staff Members

Core values are an essential part of the Chern's brand and are the foundation of its culture. The company's family ownership contributes to its desire to make every employee and customer feel valued and cared for. The firm is known for its strong and unique culture, which it feels is due to its belief that the best approach to business is to hire good people. As such, Chern's tries to identify and select the right people, train them, and give them the tools and autonomy they need to succeed. Successful employees are rewarded with above-market base salaries and generous bonuses.

The management philosophy at Chern's is based on empowerment. Chern's believes that by hiring well it can trust its employees to use their own judgment. Consequently, the firm gives them a considerable amount of freedom in terms of how they do their jobs. By striving to create a fair and positive environment and giving each employee the tools and autonomy he or she needs to succeed, the company feels it has created an environment in which its sales associates can truly excel. In fact, last year, 42 Chern's sales associates sold at least \$1,000,000 in merchandise—a company record.

Because Chern's has a strong reputation for customer service, quality, and selection, it enjoys very positive brand recognition among its targeted customers. It is consistently named one of the top three retailers in regional customer surveys and has been listed among *Fortune* magazine's top 100 best companies to work for. Last year the company ranked number 72 on *Fortune*'s list, down from 44 the previous year. It was the second-highest retailer on the list, behind Nordstrom's. It also ranked as having the best customer service among retailers for the past three years in customer surveys developed by the National Retail Federation.

In addition to focusing on customer service, selection, quality, and value, Chern's has invested heavily in information-technology tools to improve its inventory management and help its sales associates make efficient transactions with customers. The company recently implemented a Perpetual Inventory System to help its buyers react more quickly to the feedback given to them by its sales associates and to track inventory to quickly adjust each store's product mix and clothing sizes available. The technology has helped the company increase its efficiency and lower its costs as well as add value for its customers.

Chern's Financial Performance

Chern's has enjoyed a strong financial performance over the last few years. Over the past five years, the company's share price has increased 134 percent and the company's revenues have grown at an annualized rate of 9 percent. Revenues and net income have grown as all of the firm's stores have reported sales increases every year over the past three years. Growing revenues and income have provided the company with the financial base and stability it needs for further expansion. The five-year growth strategy at Chern's is to open 15 new stores a year and to continue to grow at an annual rate of 9 percent. **Figure A-2** shows the company's revenue, gross profit, and net income trends for the last three years.

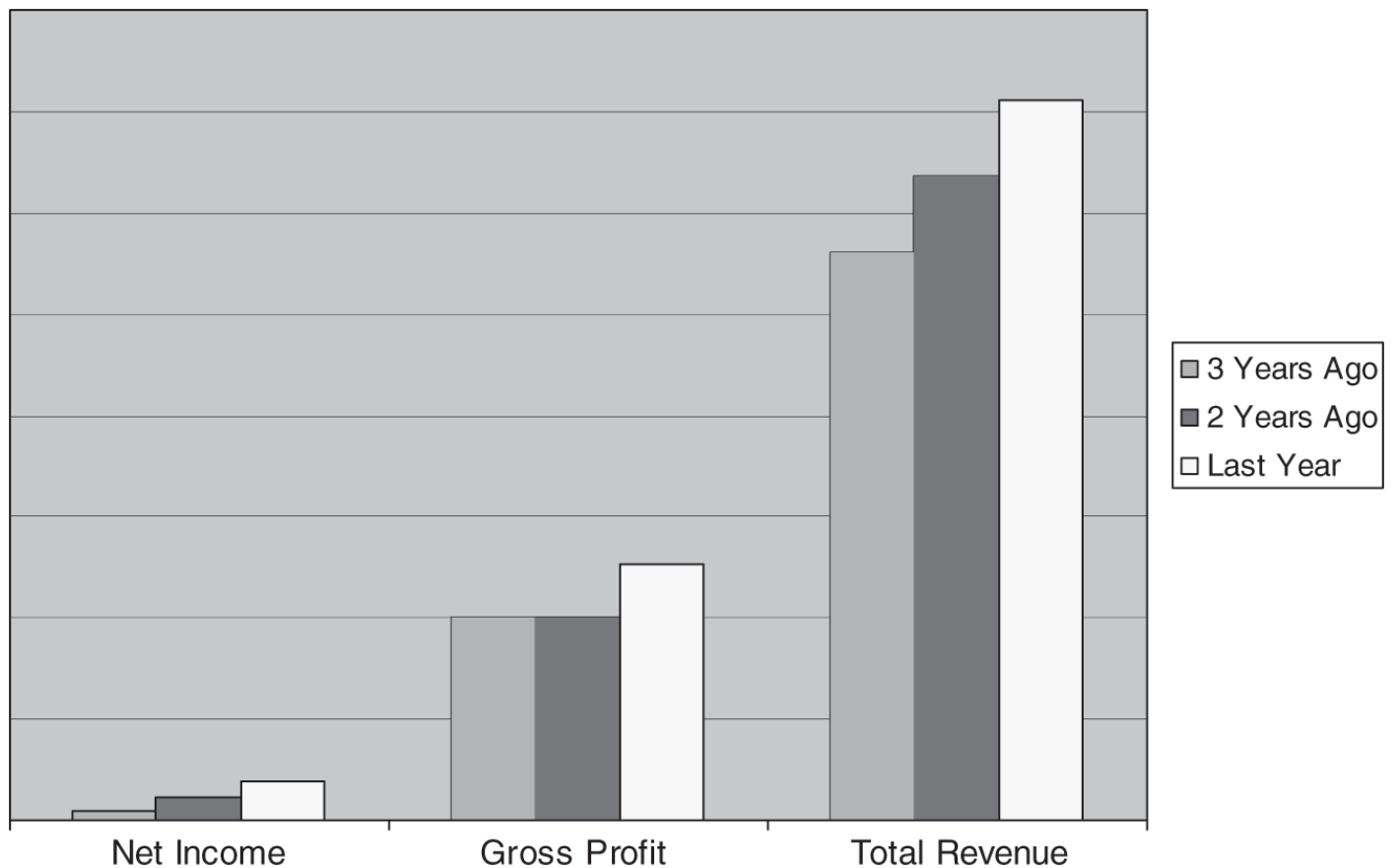


Figure A-2 Three-Year Revenue, Gross Profit, and Net Income Trends for Chern's

The company's good financial performance has translated into strong operating cash flow, giving it the option of reinvesting in its business, buying back shares, or passing some of its earnings to investors in the form of dividends. **Figure A-3** shows the operating cash flow trend at Chern's over the past three years.

Chern's has funded its expansion using its earnings rather than by taking on debt. The company believes that its conservative debt policies and strong cash flow help create shareholder value by enabling it to expand into new markets.

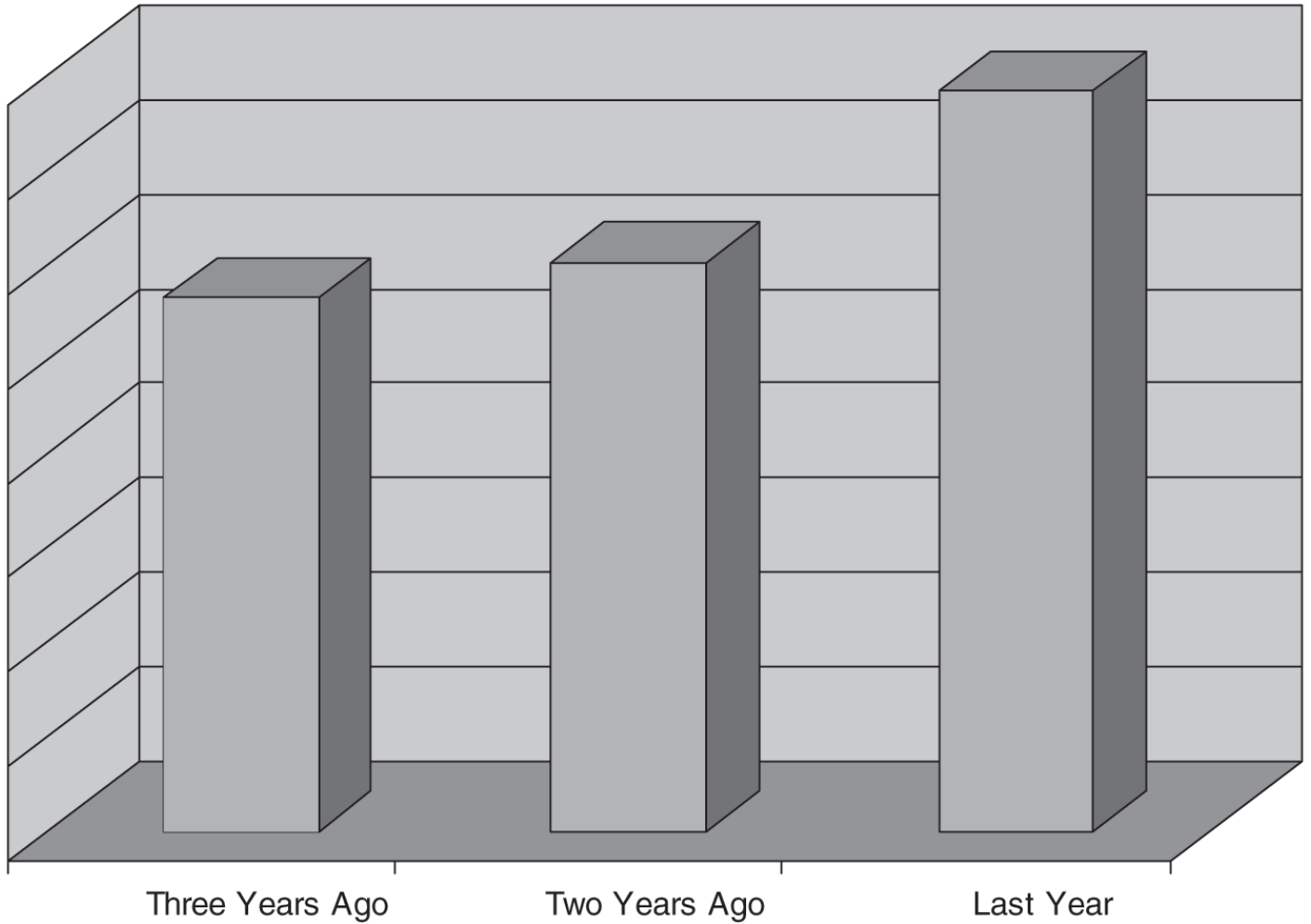


Figure A-3 Three-Year Cash Flow Trend for Chern's

Chern's Human Resources

Chern's averages 1 store manager, 8 department managers, 8 assistant department managers, and approximately 100 full-time and 25 part-time sales associates per store. Full-time employees receive a generous benefits package, two weeks paid vacation, and are eligible for bonuses. Part-time employees are considered members of the core workforce and receive prorated benefits and bonuses. Because it feels that they would not reinforce its culture, Chern's does not currently utilize temporary or contingent workers of any kind. Turnover among its full-time sales associates has been relatively stable, averaging 20 percent over the past three years. Turnover among the company's part-time sales associates has also been relatively low compared to similar retail operations, averaging 15 percent over the past three years. The part-time sales associates are used to increase the number of sales associates on the floor during peak periods.

The human resources department at Chern's generally does a good job supporting the company's business strategy. The company's compensation, performance management, and training are all designed to get sales associates up to speed and selling quickly. The base pay they earn is 20 percent above the market average, and Chern's matches in their 401(k) plans up to 10 percent of their base pay. Twenty percent of a sales associate's bonus is tied to the person's customer service performance as rated by his or her department manager, 40 percent is based on individual sales performance in relation to that person's sales target, and 40 percent is based on overall store sales. New employees have a reduced sales target for their first year. Sales associates can earn up to 150 percent of their base pay in bonuses based on both sales and customer satisfaction ratings. Top performers at Chern's earn well above the market average in pay.

Semiannual performance evaluations assess sales associates' initiative, customer service behaviors, coworker support behaviors, and leadership. Raises to an associate's base salary include a cost-of-living adjustment based on inflation, and from 0 to 10 percent based on the department manager's perception of the sales associate's performance, adherence to company values, and leadership contributions. Sales associates are also given 10 personal days, including sick days, and generous health and dental benefits. If a sales associate refers a candidate to Chern's, and the person is hired, the company gives the employee a \$1,000 referral bonus after the new hire passes the six-month mark with strong performance.

Chern's largely focuses its training and development activities on its new hires. New hires undergo a two-day orientation. Each then receives on-the-job training from his or her department manager and shadows another sales associate for one week. Employees receive additional training only if they fail to reach their sales quotas two months in a row. Sales associates who fail to reach their quotas four months in a row are given a warning. Those who fail to meet their quotas five months in a row are terminated.

Sales associates can use the store's technology to identify how they are performing relative to their quotas. Chern's expects its employees to be relatively "tech savvy" and be willing and able to quickly learn its systems. Customer information, including information about their previous purchases and fashion preferences, is stored in the company's computer for fast retrieval. Chern's also uses technology to give its buyers feedback about its customers' preferences and purchasing trends. The company's sales associates are also required to record information about customers' inquiries and unfilled requests for particular types of clothing. This is critical because it helps each department better track its inventory and quickly adjust its product mix and sizes to meet the changing demands of its customers. Sales associates can also use the store's computers to check inventory at other Chern's locations to better assist clients in locating desired products.

The Competition Chern's Faces

Chern's primary competitors include Nordstrom, Dillard's, Barney's, Nieman Marcus, and Saks Fifth Avenue. **Table A-1** shows the previous and current year's sales, net income, and employee headcount for Chern's relative to its competitors.

Table A-1 One-Year Performance of Chern's Relative to Its Competitors

	Chern's	Nordstrom	Dillard's	Barney's	Nieman Marcus	Saks Fifth Avenue
Previous year's sales (\$ millions)	3,800	8,111	8,525	326	4,390	2,249
Current year's sales Growth (%)	9.7	9.9	(.9)	2.3	6.9	8.2
Previous year's net income (\$ millions)	193.4	672.5	242.2	24.2	247.8	164.2
Current year's income growth (%)	9.0	6.9	.8	(.6)	6.0	6.4
Previous year's headcount (full and part time)	19,000	56,500	54,300	1,400	17,900	11,750
Current year's headcount growth (%)	9	2.9	(1.2)	.9	4.1	3.9

At Chern's, sales associates execute the company's customer service strategy by building long-term relationships with their clientele. Sales associates feel empowered, and their business freedom is strongly supported by the corporation as long as the employees work hard and do their best. Chern's tries to hire sales associates with an entrepreneurial spirit, a drive to be successful, and a desire to make money. The sales force's accountability for results and Chern's high expectations of them means that Chern's wants to hire only elite sales associates.