



Looking Down From the Top of the Mountain  
(and forward to higher profits)

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## **Executive Summary**

REI leads outdoor sports stores in the US by offering apparel, gear, and services to the physically active crowd. REI is the largest consumer cooperative in the country, with more than 2.8 million members. With 94 stores in 26 states, REI garners unmatched customer loyalty as an outdoor sports authority. REI's unique, innovative positioning strategy allowed its continued growth over the years. However, many retail stores are adopting REI's strategies, threatening to carry away REI's market share. REI should modify its strategies to maintain its position in the sporting goods industry.

In this report, we analyze REI's strategy using Porter's Five Forces analysis. We analyze threats and show how REI differentiates itself from its rivals to build its brand. Finally, we suggest strategies to stay ahead of competitors and to improve profits.

## **Introduction**

### History and Background

From the 1970s to the 1990s, interest in healthy living and personal fitness has corresponded with an increase in sales of sporting and exercise goods. Originally, sporting goods stores were localized, each serving the activities common to the area. Since the 1980s, these local stores had shifted towards national chains. As consumer preferences are diverse – young, middle-aged, and old all wish to exercise – retail stores sought to provide a large collection of goods. This was aided by the introduction of online sales.

In 1938, a group of mountain climbers formed a co-op to provide high-quality gear to climbers. REI opened its first store in Washington in 1944 and a second store in California in 1975. In the late 1970's, REI began to expand and has since established retail locations across the U.S. (Figure 1).

REI currently offers equipment for hiking, camping, and cycling as well as other activities. Also, REI offers services to customers of varying skill levels and helps them make informed shopping decisions with attentive sales representatives. Online sales

compliment brick and mortar sales and add convenience. REI provides friendly service and widely accessible product information through in-store web kiosks and REI features extensive product description online.

In 1998, REI announced its first overseas expansion into Japan with a flagship store in Tokyo that would carry similar equipment to the American stores. REI already had a small customer base in Japan through catalogue sales, and Tokyo was chosen based on its centrality. The store and REI.co.jp opened in 2000. However, by 2001 financial losses forced REI to close the store and the webpage. The CEO stated on the closure: “REI Japan succeeded in all ways except financial performance.” REI pointed that the reason for the quick withdrawal after an unprofitable year was the high price sensitivity of Japanese customers. This did not fit well with the premium experience REI provides, and REI could not hold out in Japan for very long because it did not have enough capital to devote to expansion. This is the most recent failure at REI in management’s memory.

## **Porter Analysis**

### Rivalry

- 1 Large number of firms
- 2 Differentiated prices and quality

### Substitutes

- 1 Buyers can choose to purchase from the REI, or rivals’ stores and websites
- 2 Low barrier costs between switching from one store to another

### New Entrants

- 1 Large scale entry unlikely because of large cost associated with retail infrastructure
- 2 Online entry likely and possible

### Customer Bargaining Power

- 1 Customers are individual consumers
- 2 Little collective bargaining power
- 3 REI is a Co-op

### Supplier Bargaining Power

- 1 Many different brands to choose from

## 2 Supplier pricing/products sensitive to market fluctuations

### **REI's Current Strategies**

REI differs from the other sporting goods stores in their quality product selection, complements, and excellent brand name promotion. These qualities enable REI to sell merchandise at premium price levels.

#### Product Selection:

Even though the original REI sold exclusively climbing gear, the stores currently carry a wide range of products. The range of products varies from store to store to correlate to the outdoor activities available regionally. The variety of products makes one-stop shopping available to customers with a variety of interests. For example, a member of both the Alpine and Cycling Club can purchase complete sets of climbing and cycling gear at a single REI store. The alternative would be going to several individual cycling and climbing stores, which are dispersed and lack the REI branding. Furthermore, REI sells athletic and outdoor clothing not always available at smaller specialty stores.

#### Complements

##### 1) Ease for Beginners:

The sales associates are well-informed about the products because they are outdoor enthusiasts themselves, and the information they dispense helps customers make informed decisions. This allows REI to easily accommodate beginners. Customers feel free to ask sales representatives for advice on what they need for the next big trip, no matter how experienced or inexperienced they are. Customers can attend workshops on outdoor activities. Some stores even have an indoor trail for customers to test potential purchases, as well as a rock climbing wall.

##### 2) Equipment rentals:

REI rents a whole host of camping and winter sports equipment to its customers. This allows customers to both get involved in an activity before making a large investment as well as giving them the ability to try out equipment before purchasing

it. These services reinforce the one-stop shopping system, adding value to the shopping experience.

### 3) Online Shopping:

REI.com and REI-OUTLET.com sell items that may not be in-stock or carried at a store. The customers can have the products delivered to their homes or pick up the products from the nearest REI store for no shipping fee. The websites are well-organized and are therefore easy to navigate to make them easy to use. They compliment the selection of stores and bring customers in stores to pick up items.

Historically, REI has been a quick mover on has been the internet. According to IBM, a technology provider for the backbone of REI's online storefront, REI was considering Internet based sales as early as 1995. To compete online, REI has taken two separate missions. The first mission is to maintain the brand image and sell premium goods at higher costs to continuing REI customers, and to augment in store sales. The second mission is to sell large quantities of goods at competitive prices. This customer likes the advice and the premium products and image of REI, but values the convenience of shopping at home. The second customer values price above all else and is looking for the lowest prices over all other details. REI stores typically did not cater to this second customer, but a web strategy that can cater to both was adapted. REI offers both REI.com and REI-outlet.com. The outlet stores showcases products that have reduced prices and are moving towards the off season. REI.com offers a full selection of goods at normal REI prices. This strategy allows REI to compete with low price stores while keeping its current customer base at premium level prices.

### 4) Vacations:

REI offers "REI Adventures" trips at many exotic outdoor locations around the world, covering all seven continents. These allow customers to use their equipment without the hassle of planning large trips to far off destinations. They are organized as premium vacations with "carbon-neutral" options to add to REI's ecological appeal.

### 5) Return Policy and 100% Quality Guarantee:

REI has a generous return policy: if for any reason the customer is not satisfied with the product, he can return it for a full refund at any time. Such policy gives customers freedom to buy as much as they wish, with the option of changing their minds later. This compliments shopping because it encourages purchasing. Additionally it is strong signaling that they are committed to the quality of the products they sell. Unlike Big5, which takes the value end of the spectrum, premium marketing requires generous customer-centered policies.

### Brand Name Promotion

Most importantly, REI customers are willing to buy merchandise at full price because they trust the REI brand name, even though REI's prices nonetheless competitive compared to those at specialty shops. Here are a few specific reasons why customers are attracted to the REI brand name.

REI draws fashionable and young customers who enjoy outdoor sports. REI prices products reasonable for a middle-class crowd. The young and savvy customers who participate in outdoor activities together are likely to talk to each other about their latest shopping spree at REI. Therefore, promotion occurs amongst customers via word-of-mouth.

REI touts its involvement in environmental stewardship. REI donates millions of dollars to conservational organizations and public parks. For example, REI partially sponsors American Hiking Society's volunteer vacations program. Since 2007, REI offers "carbon-neutral travel" - when a customer purchases an REI trip, REI will buy a matching amount of "green energy" such that it offsets all carbon emission associated with the trip. Not only are these efforts good for the environment, REI gains reputation for its "green" policies. Environmentally-conscious customers are the market that REI targets, and it draws them to support REI and their "green" efforts.

The REI Membership offers advantages to customers. Customers can join REI for a one-time fee of \$15. For this, 8-10% of purchases are refunded in the form of in store credits. This provides an extra incentive for a customer to buy items at full-price, even though a significant amount of refund is left unclaimed each year (7.30 million or 14.5% in 2005; 6.57 million or 14.9% in 2004). Membership clubs is a good idea because it

encourages customers to revisit. In addition, the climbing wall being free to members brings in customers who have no particular reason to the store to check out the product selection.

### **Analysis of Threats**

REI's current set of strategies is unique, but it is reproducible. It may be a matter of time before a rival builds up comparable brand recognition. Next, we shall discuss current threats that REI faces.

#### Competitors

REI's competitors in the sporting goods industry include companies offering a variety of product ranges; from local small businesses to fellow national chains and online retailers.

#### Independent Stores

These stores are usually privately owned, small businesses that specialize in equipment for one particular outdoor activity, such as skiing, kayaking, or rock climbing. The owners are usually acquainted with their more frequent customers. The appeal of specialty shops is in the service customized to each client, and the variety of gear they carry. The client knows what sort of gear he wants, and the service is knowledgeable (with a small enough stock) to give personalized advice. The disadvantage of these types of stores lies in their limited product range. Specialized local stores can only retain competitive advantage with expensive transportation cost; cheap and easily available delivery (of specialized good) can entice the customer away to general stores.

#### Regional and National Store Chains and Retailers

This category includes competitors such as EMS, Sierra Trading Post, and Dick's Sporting Goods. These companies have an organizational structure similar to REI's; they provide a wide availability of equipment for some general outdoor activities, in large retail stores. Retail stores are usually complemented by an internet retail site, where

customers can also avail themselves of online orders and deliveries. Companies such as EMS have a marketing scheme just like REI's: promoting brand loyalty through quality guarantees and a generous return policy. Other companies, such as Sierra Trading Post, offers very low prices, made known to customers through catalogues sent out via mailing lists. Specialized catalogues are made to satisfy a specialized consumer group; there are catalogues with labels such as Core, Women's, Men's, Outdoors, and Adventure Edge. The online retail sites that stores in this category provides an ease of purchase that competes with REI's marketing scheme.

### Online Retailers

Some sporting goods stores exist purely within an online retail site. They provide low prices and delivery to any reasonable location. Sites such as Moosejaw.com have also distinguished themselves with marketing quirks, and a question-answer system with online submissions and replies.

### Online Distribution

One of REI's disadvantages is its very high prices. Even though REI offers ordering convenience and a good delivery system, this is a feature common to most of its competitors on the national retail level. The system of retail stores coupled with online orders for distribution is now the status quo. To retain market share, REI has to keep up with internet customers' expectations, and REI must itself from its retail competitors.

### Specialization

Though specialty stores lost business in the 80's and 90's, they have popularity today. They are particularly suited to grab market share now that REI tends towards general instead of specialized products. Customers often desire detailed knowledge about a specific product (which REI service cannot consistently provide, even with the in-store web kiosks) and desire products for special sports and activities.

REI offers a wide variety of in the water activities that include kayaking and canoeing. However, REI stores are larger supercenters that combine all activities under

one roof. There is room for competitors to place smaller stores with only kayaking gear by the ocean that can be singly focused on kayaking. Given REI's current strategy of centrally placed stores, opening a superstore on the same block as this smaller store wastes store space not devoted to ocean activities. The rest of the inventory, like hiking essentials, would be wasted on a beach community. Similarly, a ski shop on a mountain open can sell equipment at a higher markup than REI because of its convenience and the better advice that skiing salesman can provide. REI too cannot open a mountain-top store because half the package inventory would not sell to the particular clientele. This is however, if REI maintains its exclusively large footprint store model.

### **Strategies for Improvement**

For future success, REI has to retain market share in an industry that look-alike companies are infiltrating. There are some strategies that REI can implement to reduce loss of market share to similar chain retailers and local specialty shops. First, REI needs to hold onto existing customers, while attracting some new customers. REI should also synergize complements in a way as to give off a high quality image. Exclusive products should be promoted to justify the higher prices REI set. Finally, REI should defend, and even act against specialty stores, through specialization.

### Expanding Complements

REI should aim to project to the customers an air of convenience and accessibility. To improve the online shopping experience, customers should also be able to search the individual inventory of each retail store, and make use of a reviews feature. This will give online customers assurance of product reliability. Expert opinions should be posted, and guides for specific activities should be linked to a database of recommendations (which will self-promote the REI brand). Members of the REI co-op will log in and see a personalized webpage, tailored to their unique purchase history, with personalized recommendations also available. REI should also market itself through online and paper catalogues tailored to individual customers buying history.

To improve the in-store shopping experience, REI should continue its current practice of giving detailed in-store handouts, while sales staff could recommend goods recovered from a member's history. Above all, service and staff should remain friendly and accessible. This gives a similar appearance of the personal transactions that small businesses' service staff provides. REI can then be one of the best sources for advice about sporting equipment and activities.

REI should keep and promote their quality guarantee, shown through an easily workable return policy. Additionally, REI could sponsor more small recreational trips, while cutting down on the larger trips, the planning of which seems to be in a different business from sporting goods retailing. With the exclusivity of an 'REI' brand, all these should improve the customer's perception of quality for all of REI's products: actual gear, activities, advice, and the whole experience.

#### Encourage Customer Loyalty

Sporting goods are durable goods, and their buyers usually have irregular purchase-timing. Thus, the returning (best) customer is very important. REI must try to retain its existing customers, those who make frequent customers. As each member has already expended \$15 in membership fees, they can be turned to lifelong customers by capitalizing on human psychology – the effects of sunk costs and the endowment effect. However, additional benefits should be made known to customers to encourage repeat purchases. The current dividends systems is not guaranteed, and few members actually lay claim to their money; perhaps there should be implemented a guaranteed patronage rebate system, perhaps based on company profits. Since there are currently many unclaimed benefits, there should also be a more active system for member participation; unused credits can be automatically used at the register. More membership benefits will also entice customers to become new members. Though attracting new customers is also important, membership benefits should not be set in such a way as to advantage new in relation to existing customers. This is true as non-members are not essential; they would be good to have, but they could just as easily shop online, or switch to competing retailers. Benefits to existing customers should outweigh, or at least be equal to, benefits for new customers. Keeping track of the best customers will weaken price competition

and offering perks to people buying only (or mostly) REI-brand products can be an additional measure to aid price discrimination.

### Specialization

REI is often accused of “becoming Wal-Mart.” REI should either focus on product availability, or product specialization (which is preferred). By trying to hold a position in both niches, it is losing to more concentrated companies, like low-price retailers and local shops. Should it decide to stay with product availability, then REI should copy the practice of Mountain Equipment Co-op (MEC), REI’s analogue in Canada. MEC sells equipment geared towards one specific focus. This enables MEC to disregard offering goods for specialized activities outside of its product focus.

Alternatively, REI can try for product specialization, adoption a collection of specialized local shops (concentrating in a few outdoor activities) united by a between-stores delivery system and an online catalog, which will also contained frequently asked questions and answers. This way, REI can match price, variety, and knowledge with local specialized shops. Currently, the online delivery system allows product pickup at a local distribution center. Although REI builds more retail stores every year, they could better use this investment by creating local specialty stores. The equipment for each store will depend on the location; for example, kayaking gear might be sold near rivers or rapids, and climbing gear might be sold near mountain ranges. The products from these local stores can be added to specialized catalogues, and delivery of general equipment to the specialty store will encourage a more diverse customer base. The entire collection, of REI general stores and REI specialty stores, will be united by the REI brand and the networked item delivery system. Specialty catalogs can also promote these new divisions. This will not only create entry barrier to new ‘specialty’ shops, this will also allow REI multiple specialized niches (in specialty sports and activities) that can turn profitable. By making the product sufficiently specialized, price rivalry will be weakened.

### Building a Better Brand

With the same free shipping system (low transportation costs provided) between stores, REI can benefit by diversifying its products. REI can either adopt the same

practices as imitation competitors like EMS, by making low-end and high-end products available and priced accordingly, or REI can focus wholly on a single measure of quality.

The better option is make products exclusive. The current sporting goods retail market is saturated with similar quality products, and price rivalry has gotten more intense after the proliferation of online retailers. Thus, REI should create a position separate from other national-chain and online retailers. Customers are somewhat price sensitive, but this issue can be overcome by appealing to the customer's preference for expensive equipment – it correlates in their minds with higher quality. REI should be the first mover, and shift to a more advantageous locale on the price and quality Hotelling line. Prices are already high, so quality should also be high (or at least appear to be so). REI will sell the REI brand, with products both exclusive and expensive – the gear that is recommended to customers. This will prevent imitation competitors like EMS, as the exclusivity of the 'REI' brand will prevent online and chain competitors, like Moosejaw.com and EMS from offering the same good at a lower price. REI's higher prices will be justified, and even enhance REI's image as exclusive and high-quality (a higher quality than competitors).

### Alternative Strategies

There are also some alternative strategies and plans that REI could consider, that wouldn't work (as well, if at all) when compared to the strategies described above. "Green" promotion and awareness in excess of the status quo appears to be a waste of money, and is not the customer's priority. Sponsoring more large recreational trips appears to be a different business, and should be left to other firms. Leaving specialty shops alone is to lose market share that could be captured. Offering new membership benefits promotion at the expense of retaining the best customers will intensify price rivalry and REI could lose more customers overall. Giving discounted prices to sell more shifts REI to a position to encounter price competition. Or REI could do nothing, but keeping to the status quo doesn't seem enough to sustain future profits; REI will gradually lose market share to competitors' new innovative practices.

The main alternative strategy for REI to consider is to make products generally available and lower priced. One reason to avoid the low-cost strategy is its vulnerability

to both specialized stores entrants, and online retailers, who can offer still lower prices with even more extensive inventory. By changing to a point between other national chains and online retailers, REI can offer a combination of greater availability and lower prices. REI could enforce this by offering price matching, and additional clearance and promotional sales. But the presence of online retailers will make price competition felt, while specialty shops will take some of REI's form best customers, who will no longer find the equipment they need at the 'general' REI.

### **Conclusion**

REI has pioneered innovations that were attractive when it first entered sporting goods retailing, but are now rather commonplace. In an industry with low entry barriers, there will always be new entrants, trying to take a share. Currently, REI has a rather incoherent strategy of where to fix on pricing. REI attempts to attract customers with both low prices, lower quality items, and items of high quality, with higher prices. Additionally, customers are often unclear of the distinction between the two types of items, and the two pricing schemes. REI could improve its present position by adopting some new strategies: using complements to create synergies, retaining customer loyalty, specialization, and building a better brand image. With these steps, REI can better ensure future success.

Appendix

Figure 1. States with REI stores (from REI.com).

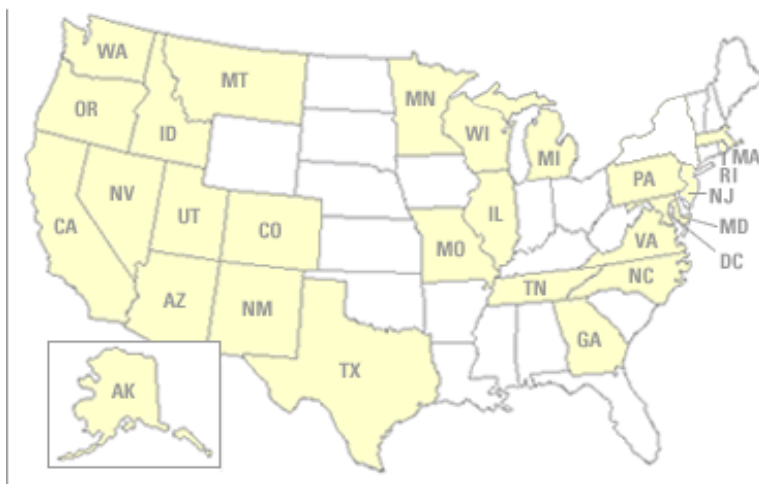


Figure 2. Consumer Guides (from REI store)

### REI PRODUCT INFORMATION

# ROPES

## & ACCESSORIES

**QUICK TIPS**

Rope choice depends on use. If you're a novice, see your instructor for advice.

Always check your rope for wear before each use.

Inspect insulation to absolutely ensure it's in place before climbing.

Single ropes must hold 5 falls; impact force on the first fall can't exceed 12kN (2,688 lbs.). Half ropes are tested with a 54kg (122 lb.) weight and a maximum impact force of 8kN (1,799 lbs.). Maximum dynamic elongation on the first fall cannot exceed 40%. Maximum static elongation with a suspended 80kg (176 lb.) load is 30% for single ropes, 12% for half ropes. Other EN tests also measure sheath strength, rope weight and rope diameter.

**KNOW YOUR DYNAMIC ROPES**

Always check a rope's rating. Single ropes have a circled "1" on both ends; half ropes are circled "1/2". Two ropes have a circled infinity symbol "∞". Half and twin ropes are designed for lead use only as a matching pair. Don't mix sizes or brands—handling, strength, elongation and other attributes are different.

**DYNAMIC ROPES**

- A dynamic rope is the preferred choice for all climbing applications, and the only rope that should be used for lead climbing. Such ropes must be "dynamic" enough to absorb the energy of a fall, yet strong enough to offer only a little stretch under a climber's weight.

**DRY AND NON-DRY ROPES**

- If a rope absorbs water, it gets heavier and less able to withstand forces generated in a fall. When it's cold enough for absorbed water to freeze, a rope gets stiff and uncomfortable; ice crystals can also weaken a rope. Dry treatment prevents absorption and extends a rope's longevity. Use non-dry ropes only on fair-weather climbs and snow-free routes. Dry ropes can have a dry core, a dry sheath or both. Ropes with both offer the greatest moisture protection.

**STATIC ROPES**

Static ropes should be called "semi-static" because they offer a minimal level of stretch. They aren't made to absorb energy from a fall—instead, a climber's body would take most of the force. Thus static ropes are not safe for lead climbing. They are used for carrying, hauling, rappelling and rescue work.

**TESTING**

Dynamic rope standards are specified by European Norm (EN). Impact force is tested by placing an 80kg (176 lb.) weight on a 2.5m section of rope, then dropping it 4.8m.

### REI PRODUCT INFORMATION

# SLEEPING

## PADS

**QUICK TIPS**

The bag feature is hollow so it's lightweight, compact and easy to use.

For family camping, heat or ear travel, and other reasons where size and weight are not the limiting factors, a thicker, longer mattress is an enjoyment-booster.

Water sleeping requires more insulation. On snow REI recommends the use of 2 pads and inflating pad steps a closed air vent foam pad. The foam pad adds insulation and offers protection in case the inflatable is punctured.

**Water-resistant pads offer extra insulation and cushioning to the feet, hip and torso areas. Look for more optimal Vent REI.com.**

**Backpackers** who want more comfort can pack from pads with greater thickness and durability at a modest increase in weight.

**PROS:** Comfortable and lightweight. Fine for backpacking or carrying in warm conditions. Insulated models can be used year-round.

**CONS:** Prone to punctures. Field repairs are not difficult. Non-insulated models offer poor insulation due to free circulation of air inside pad.

**Air mattresses:** These camping mattresses use air for comfort and are much thicker than air pads. They are as close to a real bed as you can get and are usually sized to fit a regular double.

**PROS:** Extremely comfortable. Easy and quick to inflate with a pump. Suitable for use on uneven ground.

**CONS:** Relatively heavy and bulky. Setup required proper inflation. May be prone to punctures or leaks. No insulation for mild climates only.

**Foam pads:** These basic backpacking pads feature dense foam with tiny closed air cells.

**PROS:** Lightweight, responsive, durable, excellent insulation. Won't absorb water.

**CONS:** Less comfortable. Heavily used, so they tend to be bulky.

**TRY THEM OUT!**

Test out a number of models to get a feel for the amount of cushioning you require in the length and width you prefer.

A pad's weight and packability, and for a self-inflating model, how quickly it inflates.

**FREE SHIPPING TO ANY REI STORE. SOME RESTRICTIONS APPLY.**  
FOR DETAILS, VISIT REI.COM OR CALL 1-800-488-4846.

Figure 3. Products offered at REI and Competitors

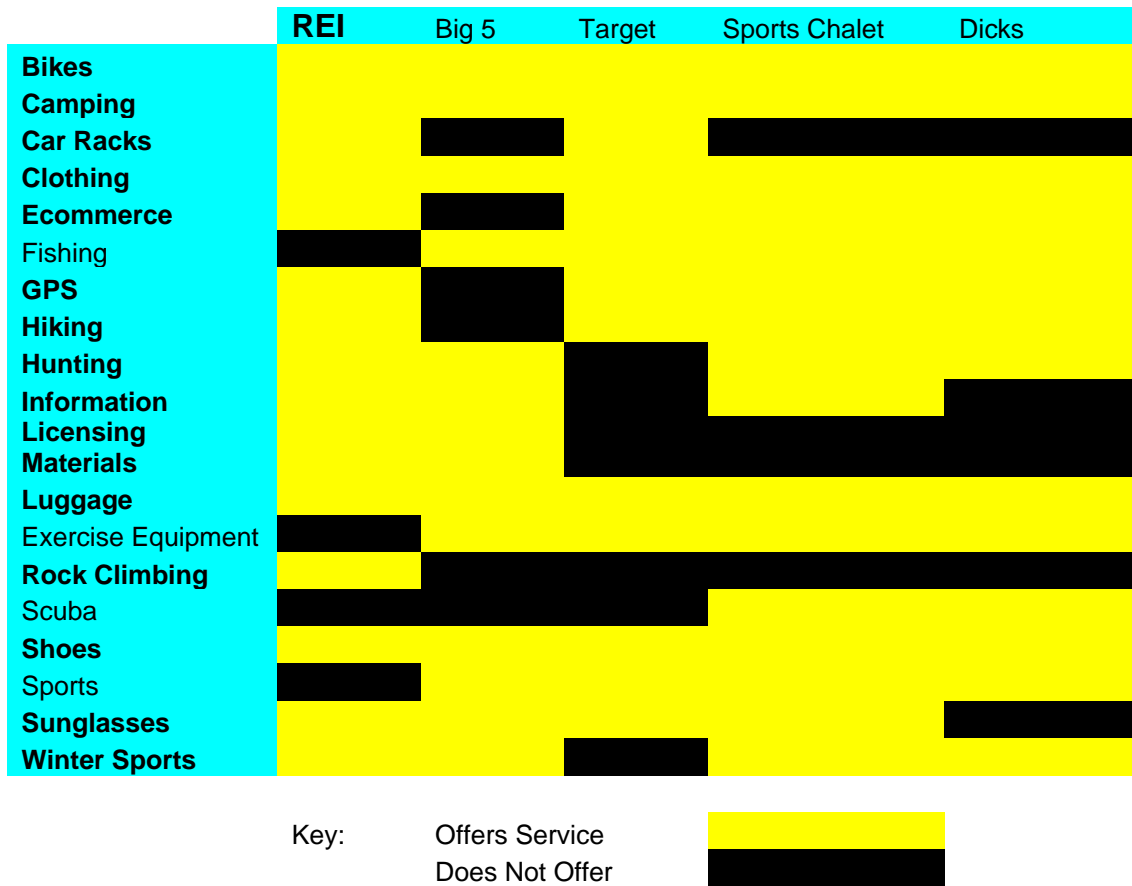
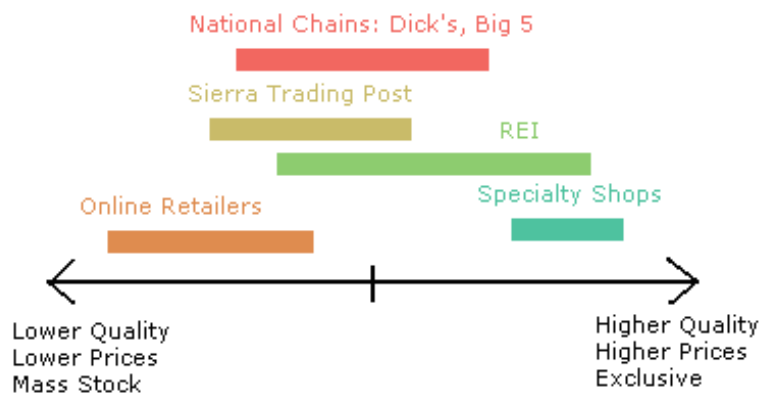


Figure 4. Hotelling Line for Sporting Goods Retail



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Eastern Mountain Sports, REI, Dick's Sporting Goods, Mountain Equipment Co-op