Electronic Retailing

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Introduction

Perspectives on electronic retailing have changed dramatically over the past seven years. In 1998, most analysts predicted that a new breed of high-tech, web-savvy entrepreneurs would dominate the retail industry. Everyone would shop over the Internet, stores would close owing to lack of traffic, and paper catalogs would become obsolete. The prospects for electronic retailing were so bright that companies invested, and lost, billions of dollars in Internet retail entrepreneurial ventures such as Webvan, eToys, and Garden.com – companies that are no longer on the retail landscape.

Even though online retail sales continue to grow much faster than retail sales through stores and catalogs, we now realize the Internet is not a revolutionary new format replacing stores and catalogs. Although the Internet continues to provide opportunities for entrepreneurs, in the retail industry it is primarily used by traditional retailers as a tool, complementing their store and catalog offerings, for growing revenues and providing greater value for their customers. For the majority of retailing activity, the Internet is a facilitating rather than a transformational technology (Weitz 2001).

For example, REI’s website enables its customers to buy merchandise that is available in its stores online. Orders can be shipped to the customer or be picked up at a store. Besides providing this e-commerce capability, the Web site has more than 45,000 pages of schedules for events and clinics in local stores, extensive product information, comparison charts, and how-to articles on a comprehensive range of outdoor sports and activities. As a result, REI offers online shoppers across the world an experience that complements its stores, where its staff provides personalized assistance in selecting the right outdoor gear, apparel, and accessories.

This chapter first describes the unique benefits and limitations offered by an electronic channel relative to store and catalog channels – factors affecting the potential growth of electronic retail. Then it reviews the approaches electronic
retailers are taking to exploit the advantages of an electronic channel and addresses its limitations. The chapter concludes with a discussion of issues associated with electronic retailing, such as the types of merchandise that can effectively be sold online, the potential increase in price competition resulting from the low search costs associated with online shopping, and what firms are best positioned to exploit the potential for an electronic retail channel.

**Potential Growth of Electronic Retailing**

Even though the annual growth of electronic retail sales is more than 30%, the electronic channel accounts for slightly less than 3% of retail sales in the United States and Europe, and an even smaller percentage in Asia. The relative benefits and limitations of Internet shopping as against shopping through traditional channels (stores and catalogs) will affect the future penetration of electronic shopping (Alba et al. 1997).

**Benefits of Shopping over the Internet**

The following, somewhat futuristic, scenario illustrates the potential benefits of shopping online. Laurie Waters wants to buy a present for her son Allan, whose 13th birthday is in a few days. On her home computer, she accesses her personal shopper program called FRED, and has the following dialog:

FRED: Do you wish to browse, go to a specific store, or buy a specific item? [Menu appears and Laurie selects]
LAURIE: Specific item
FRED: Occasion? [Menu appears and Laurie selects]
LAURIE: Gift
FRED: For whom? [Menu appears]
LAURIE: Allan
FRED: Type of gift? [Menu appears]
LAURIE: Toy/Game
FRED: Price range? [Menu appears]
LAURIE: $75–$100

[FRED shops the world electronically, visiting the servers for companies selling toys and games in Europe, Asia, Africa, Australia, and North and South America.]
FRED: 121 items have been identified. How many do you want to review? [Menu appears]

LAURIE: 5

[FRED selects the five best alternatives on the basis of information about Allan's preferences, typical preferences for children Allan's age and Laurie's preference for nonviolent, educational toys. Details of five toys appear on the screen, with the price and brand name of each. The retailers selling the toy are also listed beneath each one, along with the nearest store with the toy in stock. Laurie clicks on each toy to get more information about it, including evaluations by Consumer Reports and comments from parents who have bought the toy. With another click, she sees a full-motion video of a child Allan's age playing with the toy. Finally, she selects a toy.]

FRED: The nearest stores that have the toy in stock are listed below along with the prices. Do want to pick the toy up at a store, have it shipped to your home, or shipped to your office? [Menu appears]

LAURIE: Pick up at Toys "R" Us store near Perimeter Mall

FRED: Toys "R" Us suggests several books that appeal to children who like the toy you have selected. Do you want to review these books?

LAURIE: Yes

[The books are displayed on the screen. Laurie reviews the books and decides to order one.]

FRED: Would you like this gift wrapped?

LAURIE: Yes

[The different designs for wrapping paper are displayed on the screen and Laurie selects a baseball motif.]

FRED: How would you like to pay for this? [Menu appears]

LAURIE: American Express

More Alternatives. This scenario illustrates that, besides the benefits offered by all nonstore channels (convenience and security of shopping from home or work at any time), the electronic channel has the potential for offering a greater selection of products. However, the benefit of having many more alternatives has diminishing returns for consumers. It is unlikely that anyone would look through all 121 alternatives located by FRED. Having many alternatives is only meaningful if customers have access to intelligent agents such as FRED that can identify consideration sets based on the consumer's preferences.

More Information. The electronic channel also has the potential for providing customers with as much information as they need to make a decision. Customers shopping online can drill down through web pages until they feel comfortable with their choice. Also, the information on the electronic channel database can be fre-
quently updated and is available all day and night. Finally, the electronic channel can format the information so that customers can use it effectively when evaluating products.

**Personalization.** Perhaps the most significant benefit of the electronic channel is the ability to use the Internet’s interactive capabilities to economically personalize information. Service-oriented retailers such as department and specialty stores hope their sales associates will provide this benefit. They would like their sales associates to know or find out what their customers want and then recommend appropriate merchandise. However, an electronic agent such as FRED can be more effective in searching through an extensive range of alternatives, selecting a small set, and providing the information that the customer typically considers when making a purchase. Also, FRED is never in a bad mood, is paid nothing, and is always available – 24/7.

In the future, electronic agents such as FRED may be computer software programs bought by consumers or offered as a service to their customers by retailers or third parties. These agents could learn about a consumer’s preferences by asking questions or analyzing past search and purchase behaviors.

**Problem Solutions.** The electronic channel also offers an opportunity to go beyond the traditional product information offered in stores to provide tools and information for solving customer problems and selling ancillary services. For example, online wedding sites, such as www.weddingchannel.com, offer couples and their families planning guides, tips, and an opportunity to chat with other couples getting married. The site sells wedding dresses, invitations, and flowers. Couples can create gift registries, featuring Federated stores, and broadcast them to their guests by e-mail. They can select potential reception locations by looking at photos. Finally, they can have their personal area on the site, on which they can post their own wedding pictures.

**Limitations of Electronic Shopping**

Although the electronic channel offers some unique benefits, it also has some limitations relative to stores and catalogs. Some of these limitations are the opportunity or ease with which consumers can: (1) browse through the retail offering, (2) locate information needed to evaluate merchandise, (3) use all five senses – touching, smelling, tasting, seeing, and hearing – when evaluating merchandise, (4) receive personal attention, (5) have their privacy protected, (6) provide a stimulating experience that can be shared with others, (7) purchase merchandise with cash, and (8) get the merchandise when they buy it. These issues do not arise or are less difficult for consumers to deal with when shopping in stores. For example, if a store shopper wants to know whether a store stocks an item that the shopper cannot find, the consumer can simply ask a store employee. However, when shopping online, the consumer has to send an e-mail to the retailer and sometimes wait days for a response.
Factors Affecting the Growth of Electronic Sales

Two important factors affecting the growth of electronic retailing are: (1) the number of people with broadband access and (2) the degree to which electronic retailers exploit the benefits and address the limitation of electronic shopping.

Internet Access

A substantial number of people worldwide have access to the Internet and thus can potentially engage in electronic shopping. According to the Computer Industry Association Factbook, in 2004, 934 million people had Internet access, and it estimated that this figure will increase to 1.35 billion by 2007. The countries with the greatest access are the United States (185.5 million people), China (99.8 million), Japan (78.1 million), Germany (41.5 million), United Kingdom (33.1 million), South Korea (31.7 million), France (25.5 million), Italy (25.5 million), Brazil (22.3 million), Russia (21.2 million), and Canada (20.5 million).

In August 2004 in the US, about 75% of people with Internet access were classified as active at-home users. Nielson/Net Ratings estimates that, in July 2004, 50% of the US homes with access had broadband connections. Broadband’s prevalence is important, because consumers need such connections to take advantage of many of the innovations in electronic retail offering discussed below. Nielson/Net Rating also reported that the 2004 average monthly usage for member of their US panel was 25 hours in 31 separate sessions visiting 52 domains. However, in the US in 2004, only 26% of active Internet users (64 million people) bought products and/or services over the Internet. Thus, there is a substantial number of active Internet users who do not shop over the Internet.

Exploiting the Benefits and Addressing the Limitations – Electronic Retailing Best Practices

Given the significant penetration of Internet usage in industrial counties, the primary factor driving the growth of online retail sales will be the degree to which electronic retailers exploit their benefits and address their limitations (Putnam 2003). This section reviews some of the steps retailers using an electronic channel are taking to make shopping online more appealing.

Security Concerns. Perhaps the biggest challenge for online retailers is establishing and maintaining trust. Spam, fraud, identity theft, and fly-by-night e-retailers threaten consumers’ fragile trust in online marketplaces. However, reputable retailers have taken steps to offer secure connections and protect their internal data. Also, as consumers become more accustomed to placing orders over the Internet, their concerns about security are diminishing. Retailers offering customers the option of calling in an order rather than ordering online report that the vast majority of orders are placed online.

Although consumer security concerns are declining, online retailers face increasing losses owing to credit card fraud. It is estimated that credit card fraud will
cost online US retailers more than $1 billion in 2004. Online retailers use a variety of fraud management techniques, including using in-house or commercially available screens, requesting card verification numbers, and checking orders with credit card authentication services.

**Browsing – Navigation and Search.** Before an electronic channel was offered, consumers rarely described their shopping process as searching for a product they needed. They used terms such as browsing and window shopping, behaviors that often lead to unplanned purchases. Such browsing is more difficult for consumers shopping online.

When using an electronic channel, customers have a much more limited visual field than they do in a store. Only a limited number of items can be featured on the first web page and subsequent web pages viewed by shoppers. In contrast, in a store, many other items are in a shopper’s sight line beyond the items prominently displayed on an end-cap or on mannequins. Although shoppers in stores do not mind walking a few steps to look more closely at merchandise, there is a substantial reduction in “foot traffic” on secondary Web pages.

Online retailers are addressing this limitation in two ways: (1) customizing the main page to display items of interest to the customer and (2) improving the search function. We shall discuss the customization of the main page in the section below on personalization.

The ease of navigation and quality of the search function facilitate browsing through a web site as well as locating specific merchandise. More than half of online purchasers use the search function to locate products. The search function is typically the second most heavily trafficked page on a retail Web site.

Traditional web site search functions rely on the exact words the shopper has entered in the search box. Many retailers now use “intelligent” search functions that respond to natural language inquiries such as “sweater under $100” and then refine the search by responding to secondary questions such as “ones that are red.” These intelligent search functions also interpret the words and grammar to match responses to the retailer’s merchandise assortment. For example, when searching the website of an automobile part retailer for an “air filter,” a search function will not include coffee filters but may include links to related products, such as “engine cleaners.” This search capability enables the retailer to accommodate the shopper’s initial inquiry and also cross-sell and up-sell more effectively. Finally, these intelligent search functions get better over time as they learn the terminology used by the retailer and its customers.

However, implementing an intelligent search function can cost millions of dollars, along with an annual maintenance cost. For retailers with less complicated product lines, these costs may not produce an acceptable ROI.

**Provision of Sufficient Information and Customer Service.** At many points during the shopping process, consumers may need information before making a purchase. Service-oriented store retailers satisfy this customer need through their sales associates. However, providing timely information is more challenging for electronic retailers.
Consumers find the traditional online solution, posting web pages with retailers’ policies and FAQs, fails to meet their needs. It is often difficult to comb through a list of FAQs to locate the information needed. Another standard feature addressing this need is the offer of an 0800 number or an e-mail address for asking questions. However, these solutions often fail to provide the timely information customers seek and may not be feasible for the consumer using the house’s only telephone line with a dial-up connection to access the retailer’s website. Two new applications for responding to customer information needs in an efficient and timely manner are live, online chat and automated self-service solutions:

*Online chat* provides customers with the opportunity to click a button at any time and conduct an instant messaging e-mail conversation with a customer-service representative. Other applications allow a consumer to initiate a voice conversation with a customer-service representative. These applications also enable electronic retailers to automatically send a proactive chat invitation to customers on the site. The timing of these invitations can be based on the time the visitor has been on the site, the specific page the customer is viewing, or a product on which the customer clicked.

These *self-service solutions* are economically attractive. The average cost per customer service session for self-service is $1.17, as opposed to $7.80 for live chat, $9.99 for e-mail, and $33 for a telephone customer session.

Electronic retailers vary in how they make the tradeoff between stimulating sales and increasing customer satisfaction with the cost of providing online instant chat. Some online retailers make this service option available and highly visible on their home page and highly trafficked pages, while others deliberately make these services hard to find to encourage customers to use less costly options such as FAQs and self-service applications.

*Overcoming the Need for Sensory Information.* When evaluating some types of merchandise, information about “look-and-see” attributes, such as grams of fat in a breakfast cereal or color and style of a wool scarf, can be effectively communicated over the Internet. However, “touch-and-feel” attributes are more difficult to communicate online. Owing to the problems of providing “touch-and-feel” information, apparel retailers experience returns rate of more than 20% on purchases made through an electronic channel and only 10% for purchases made in stores.

*3-D/Zoom Imaging.* Electronic retailers are taking steps to overcome this limitation by converting “touch-and-feel” information into “look-and-see” information. Online customers now expect large, accurate product images. However, electronic retailers are going beyond offering the basic image to giving customers the opportunity to view merchandise from different angles and perspectives using 3-D imaging and/or zoom technology. Although only a limited number of electronic retailers are employing these technologies for a few products, the use of these image-enhancing technologies has increased conversion rates (the percentage of consumers who buy the product after viewing it) and reduced returns.
However, these imaging technologies can frustrate consumers using dial-up connections because of the slow download times. Also, some of the technologies require plug-ins that have to be downloaded and may not work effectively with all browsers. Finally, some retailers initially utilized these imaging technologies but have now removed them because visitors were not using them.

Virtual Models. To overcome the limitations experienced because apparel obviously cannot be tried on, online apparel retailers have started to use virtual models. These virtual models enable consumers to see how selected merchandise looks on an image with similar proportions to themselves and then rotate the model so the “fit” can be evaluated from all angles. The virtual models are either selected from sets of “pre-built” models or constructed on the basis of the shopper’s response to questions about their height, weight, and other dimensions.

For example, at Landsend.com, online shoppers choose a model that looks like them. The customer then dresses the model using a “click-and-drag” interface. Items are suggested while the customer “tries on” apparel. Land’s End reports that customers using the virtual model feature are 28% more likely to make a purchase and spend 13% more on the average purchase. When JCPenney offered this feature on its website, more than 100,000 customers saved their model for future visits.

In a similar way to the imaging technologies discussed previously, the virtual model technology is complex and results in slow download speeds for consumers who have no broadband connections. Also, the present applications are not true fit predictors, but provide some information about how combinations of apparel and accessories look together and what apparel styles might flatter a specific figure. However, these applications are harbingers of future applications in which customers can have a personal, 3D, digitized body scan serve as an actual model rather than a virtual model. Also, the measurements for the body scan could be inputted along with information about the garment to a predictive model advising customers on how well a specific item fits using a five-star rating system and then suggesting the appropriate size.

Personalization. One of the attractive features of Laurie Waters’ online shopping experience, previously described, was the personalized service offered by FRED. This personalization assisted Laurie in satisfying her need for a gift. Had FRED’s services been offered by a retailer, the personalization would have engendered Laurie’s loyalty to the retailer. When a retailer has a thorough understanding of her preferences and uses this it effectively to facilitate Laurie’s shopping experience, she has little incentive to switch to other retailers lacking this capability.

Although not achieving the level of personalization offered by FRED, Amazon.com is clearly on the forefront in terms of personalizing its offering. Visitors are greeted by a personalized “store” featuring their name and recommending products based on their past purchases, click-stream data, or expressed preferences. Besides personalizing the websites, customers can elect to receive e-mails announcing the availability of new product in which they might be interested. However, an important issue related to personalization is that of privacy concerns.
Privacy. Although detailed information about individual customers helps retailers to provide more benefits to their better customers, consumers are concerned about retailers violating their privacy when they collect this information. These concerns are particularly acute for online customers, because many of them realize the extensive amount of information that can be collected without their knowledge. Besides collecting transaction data, electronic retailers can collect information by placing cookies on visitors’ hard drives.

In the US, legal protection for individual privacy is limited. Existing legislation is limited to the protection of information in a few specific contexts, including government functions and practices in credit reporting, video rentals, and banking. However, the European Union (EU) is much more aggressive in protecting consumer privacy. Some of the provisions of the EU directive on consumer privacy are:

- Businesses can only collect consumer information if they have a clearly defined purpose, such as completing the transaction.
- The purpose must be disclosed to the consumer from whom the information is being collected.
- The information can only be used for that specific purpose.
- The business can only keep the information for the stated purpose. If the business wants to use the information for another purpose, it must initiate a new collection process.

Businesses operating in Europe can only export information from the 25 EU countries to importing countries with similar privacy policy. Thus, US retailers cannot transfer information from Europe to the US, because the US does not have similar privacy policies. Basically, the EU perspective is that consumers own their personal information. Retailers must get consumers to explicitly “opt in” and agree to share this personal information. On the other hand, personal information in the US is generally viewed as being in the public domain and retailers can use it any way they desire unless consumers explicitly “opt out.”

There is a growing consensus that personal information must be fairly collected and the collection must be purposeful. The information should be relevant, maintained as accurate, essential to the business, subject to the rights of the owning individual, kept reasonably secure, and transferred only with the permission of the consumer. To address these concerns, most online retailers that collect customer information have posted privacy policies.

Cash Purchases. The lack of credit cards inhibits teens and tweens, a sizable and fast growing retail segment, from shopping online. However, several Internet service providers let parents establish an account for children using a credit card to set the initial balance. The teenager logs onto the site using a password, browses the site’s electronic retailer partners, selects desired merchandise, and puts it in an electronic shopping cart. The shopping site takes care of the payment. Using their own passwords, parents can check up on their teens’ buying habits and balance.
Although online retailers are using technology to address the limitations of online shopping, the store channel continues to offer superior benefits to an electronic channel, such as providing information about "touch-and-feel" product attributes and ability to get products immediately after purchasing them, and offering a stimulating, social experience. Thus, most analysts project that online retail sales will only be 4-5% of total retail sales by 2010. However, retailer websites play a major influence on retail shopping behavior. A recent survey of a representative sample of internet users found that more than 40% of consumers shopping for consumer electronics, books, PCs and peripherals, clothing, and CDs visited a retailer's website and then shopped at its store. This synergy between electronic and store channels is one factor leading to the growth of multi-channel retailing that will be discussed briefly at the end of this chapter and in more detail in the chapter by Sonneck and Ott in this book.

**Electronic Retailing Issues**

**What Types of Merchandise Will Be Sold Effectively Through the Electronic Channel?**

Presently, the greatest penetration of internet sales is for travel services, computers and peripherals, and books. In purchasing these products and services, consumers feel the "look-and-see" information provided is sufficient. Other product categories, such as automobiles and houses, have had limited internet sales, because the information available over the internet is insufficient to make high-risk purchase decisions. Also, one suspects that products with important "look-and-see" attributes will not be purchased over the internet (Zeng, Reinartz 2003).

Even though it is limited to providing "look-and-see" information, in some situations the electronic channel might even provide better information than stores. For example, if Laurie Waters went to a store to buy a toy for Allan, she might just see a picture on the side of the box containing the toy. However, by shopping online, she can get superior information from the full-motion video clip showing a child playing with the toy.

The difficulty of providing "touch-and-feel" information online suggests that jewelry, clothing, perfume, flowers, and food, products with important touch-and-feel attributes, will not be sold successfully through an electronic channel. This type of merchandise is presently sold through nonstore channels, such as catalogs and TV home shopping and, as discussed previously, electronic retailers are using technology to convert "touch-and-feel" attributes into "look-and-see" attributes.

*Branded Merchandise.* Branding, both the branding of the merchandise and the retailer’s brand image, overcomes many of the uncertainties in purchasing merchandise without touching and feeling it. Consider branded merchandise such as Nautica perfume or Levi's 501 jeans. It is not possible to smell a sample of the perfume or try on a pair of the jeans before buying, but this need not matter since the brand insures that each bottle smells the same and each size fits the same.
The retailer’s brand reputation can also provide information about the consistency and quality of merchandise. For example, consumers might be reluctant to buy produce online because they cannot see fruits and vegetables before purchasing. However, the same consumers would be likely to feel comfortable buying fruit from the Harry and David catalogs or Internet site, because Harry and David has established a reputation for selling only the highest quality fruit (Ba, Pavlou 2002). Branding even provides enough information to facilitate the sales of high-risk products with important “touch-and-feel” attributes, such as high-fashion apparel (bluefly.com and Neimanmarcus.com) and expensive jewelry (bluenile.com).

*Gifts.* In other situations, “touch-and-feel” information might be important but the information in a store is not much better than the information provided electronically. Since the gift-giver lacks complete information about the recipient’s preferences, stores offer little benefit over an electronic channel.

Thus, the critical issue determining what types of merchandise can be sold successfully online is whether the electronic channel can provide enough information to make sure customers will be satisfied with the merchandise once they get it. There are many buying situations in which an electronic channel can provide sufficient information even though the merchandise has important “touch-and-feel” attributes.

**Will Offering an Electronic Channel Lead to More Price Competition?**

Many store-based retailers offer similar assortments of branded merchandise and thus have difficulty differentiating themselves on the basis of their merchandise offering. However, price competition between these store-based retailers offering the same merchandise is reduced by geographical constraints. When using the Internet, the number of stores that consumers can visit to compare prices is no longer limited by physical distance. Also, the ease of searching for price information is facilitated by shopping bots.

Although consumers shopping online can collect price information with little effort, they can get information about the quality and performance of products at a low cost. The additional information about product quality might lead customers to pay more for high-quality products, thus decreasing the importance of price (Lynch, Ariely 2000). Also, online retailers can differentiate their offering by providing better services and information. Even with the low search cost, research shows that significant price dispersions for online retailers persists (Ancarani, Shankar 2004, see also Bolton, Shankar, Montoya in this book).

**What Resources Are Needed for Successful Operation of an Electronic Channel?**

A consideration of the critical resources needed to profitably sell merchandise online explains why so many of these retail Internet entrepreneurs have failed and the evolution to multi-channel retailing. The key resources needed, shown in
Table 1. Resources Needed for Selling Merchandise Online

<table>
<thead>
<tr>
<th>Resources</th>
<th>Internet retail entrepreneur</th>
<th>Catalog retailer</th>
<th>Store-based retailer</th>
<th>Manufacturer</th>
</tr>
</thead>
<tbody>
<tr>
<td>Brand reputation</td>
<td>NO</td>
<td>YES</td>
<td>YES</td>
<td>YES</td>
</tr>
<tr>
<td>Retail skills</td>
<td>NO</td>
<td>YES</td>
<td>YES</td>
<td>NO</td>
</tr>
<tr>
<td>Customer information</td>
<td>NO</td>
<td>YES</td>
<td>YES</td>
<td>NO</td>
</tr>
<tr>
<td>Complementary merchandise</td>
<td>YES</td>
<td>YES</td>
<td>YES</td>
<td>NO</td>
</tr>
<tr>
<td>Unique merchandise</td>
<td>NO</td>
<td>YES</td>
<td>YES</td>
<td>YES</td>
</tr>
<tr>
<td>Web-Based information systems</td>
<td>YES</td>
<td>NO</td>
<td>NO</td>
<td>NO</td>
</tr>
<tr>
<td>Fulfillment systems</td>
<td>NO</td>
<td>YES</td>
<td>NO</td>
<td>NO</td>
</tr>
</tbody>
</table>

Table 1, are (1) well-known brand name and trustworthy image to attract customers to its website and reduce customer uncertainty in purchasing information, (2) retail skills for developing assortments and managing inventory, (3) customer information to personalize merchandise presentations, (4) complementary merchandise and services to provide a one-stop shopping experience, (5) unique merchandise to reduce price competition, (6) information systems for effectively presenting information on web pages and managing the fulfillment process, and (7) a fulfillment system to efficiently ship merchandise to homes and receive and process returns (Levy, Weitz 2004).

As indicated in Table 1, catalog retailers are best positioned to exploit an electronic retail channel. They have efficient systems for taking orders from individual customers, packaging the merchandise ordered for shipping, delivering it to homes, and handling returned merchandise. They also have extensive information about their customers and the database management skills needed to effectively personalize service. Finally, they have the visual merchandising skills used for preparing catalogs that are similar to those needed in setting up an effective website.

Many store-based and catalog retailers have established brand reputations and the capability of developing assortments and efficiently managing merchandise inventories – resources that most manufacturers and pure electronic retailers lack. Also, store-based and catalog retailers typically have more credibility than manufacturers when suggesting merchandise, since they offer an assortment of brands from multiple suppliers. These traditional retailers also have relationships with vendors, purchasing power, and information/distribution systems to manage the supply chain from its vendors to the retailers' warehouses. Finally, some catalog and store-based retailers sell unique merchandise – they have developed private-label merchandise.

However, most store-based retailers and manufacturers lack the appropriate systems for shipping individual orders to households. Their warehouse systems...
are designed to fill large orders from retail firms or stores and deliver truckloads of goods to retailers’ warehouses or stores. To address this problem, store-based retailers such as Target, Borders, and Toys “R” Us outsource their fulfillment for online orders to Amazon.com and third parties. However, store-based retailers can use their stores as convenient places for online shoppers to pick up their merchandise and return unsatisfactory purchases.

Internet retail entrepreneurs were immersed in Internet technology and had considerable skills in the design of Web sites and developing systems to manage transactions. However, they did not have the wealth of post-purchase data that store-based and catalog retailers had. Also, the electronic-only retailers lacked the retailing skills necessary in building merchandise assortments, managing inventory, and fulfilling small orders to households. Finally, they also lacked the brand reputation to attract consumers and reduce their uncertainty.

Manufacturers also lack some of the critical resources needed to sell merchandise online directly to consumers, by-passing retailers. Retailers are more efficient than manufacturers in dealing with customers directly. They have considerably greater experience than manufacturers in distributing merchandise directly to customers, providing complementary assortments, and collecting and using information about customers. Retailers also have an advantage in that they can provide a broader array of product and services to solve customer problems. Finally, manufacturers lack information and distribution systems to fulfill individual consumer orders.

What Motivates Traditional Store-Based Retailers to Evolve in Multi-channel Retailers?

Traditional store-based and catalog retailers are placing more emphasis on their electronic channels and are evolving into multi-channel retailers for five reasons (see also chapter by Weitz, Whitfield in this book). First, the electronic channel gives them an opportunity to reach new markets, expanding their market beyond the locations of their stores. Second, they can gear up their skills and assets to grow revenues and profits. Third, an electronic channel overcomes some limitations of their traditional formats, for example by way of the convenience and security of shopping from home 24/7. Fourth, an electronic channel enables retailers to gain valuable insights into their customers’ shopping behavior. Finally, providing a multi-channel builds “share of wallet” and customer loyalty (Hyde 2001).

Adding an electronic channel is particularly attractive to firms with strong brand names but limited locations and distribution. For example, retailers such as Tiffany’s, Harrod’s, Saks Fifth Avenue, Bloomingdale’s, and Neiman Marcus are widely known for offering unique, high-quality merchandise, but, before they launched an Internet channel, customers had to travel to England or major US cities to buy many of the items they carry.

Store-based retailers can exploit their assets to greater effect when they add an electronic channel. For example, traditional retailers can use their existing format
to economically create awareness for an electronic channel. For example, they can advertise the URL of their Web sites on in-store signs, shopping bags, credit card billing statements, POS receipts, and print or broadcast advertising used to promote their stores. The physical stores and catalogs also serve as advertisements for all the retailer’s channels.

Store-based retailers can also utilize their stores to lower the cost of fulfilling orders and processing returned merchandise. The stores can be used as “warehouses” for gathering merchandise for delivery to customers. They can offer customers the opportunity to pick up and return merchandise at the stores rather than paying shipping charges.

One of the greatest constraints facing store-based retailers is their store size. The amount of merchandise that can be displayed and offered for sale in stores is limited. By blending stores with Internet-enabled kiosks, retailers can dramatically expand the merchandise assortment they offer.

An electronic channel can provide valuable insights into how and why customers shop and are dissatisfied or satisfied with their experiences. For example, information on how customers shop a merchandise category would be useful for designing a store or a website. The store and website layouts need to reflect whether customers shop by brand, size, color, or price point. Customer willingness to substitute one brand for another is valuable information for assortment planning. The task of collecting this information from store or catalog shoppers would be quite difficult. Someone would have to follow the customers around the store or observe them going through catalog pages. However, collecting data as customers navigate through a website is quite easy.

Although offering an electronic channel may lead to some cannibalization, using an electronic channel synergistically with other channels can result in consumers making more purchases from a retailer. The electronic channel drives more purchases from the stores, and the stores drive more purchases from the website. Retailers report that multi-channel customers spend 30% more than customers who shop only in the retailers’ stores (Myers, Pickersgill, Van Metre 2004); however, it is unclear whether this effect is caused by the availability of an Internet channel.

**Evolution of Electronic Retailing**

Compared with shopping in stores and through catalogs, online shopping has both benefits and limitations. The store channel enables customers to touch and feel merchandise and to use the products shortly after purchasing them. Catalogs enable customers to browse through a retailer’s offering at any time and anywhere. A unique benefit offered by the electronic channel is the opportunity for consumers to search across a broad range of alternatives, develop a smaller set of alternatives based on their needs, and get specific information about the alternatives they want.
To some extent, retailers operating an electronic channel are using new technologies to address these limitations. But, the penetration of online sales is expected to be limited owing to the inherent advantages offered by in-store shopping. Although the bubble burst for most Internet retail entrepreneurs, traditional store-based and catalog retailers are adding an electronic channel and evolving into integrated, customer-centric, multi-channel retailers. This evolution toward multi-channel retailing is driven by the increasing desire of customers to communicate with retailers any time, anywhere, from any place.

By offering multiple channels, retailers overcome the limitations of each channel. Retailers can use websites to extend their presence and the assortment offered by the store channel. They can also use websites to update the information they provide in catalogs. Stores can be used to provide a multiple sensory experience and an economical distribution capability supporting the electronic channel.

References


