



EXECUTIVE INSIGHTS

What Brands Need To Know About Digital Commerce

Digital commerce rose to new prominence during the disruption caused by COVID-19. At their peak, online sales reached 16.4% of seasonally adjusted sales during the second quarter of 2020.¹

Although a COVID bump was somewhat expected, the growth has been challenging to sustain. Online sales fell back to 14.3% of seasonally adjusted sales during the first quarter of 2022 as some shoppers returned to physical stores.² Still, online sales were just 10.3% during the same quarter three years earlier.³

That means digital commerce remains an even more important piece of the growth puzzle. For brands that have invested in establishing or shoring up digital commerce — and for many brands' direct-to-consumer online sales channels — the focus now is on optimizing digital commerce via a consumer-centric approach.

But digital strategies aren't one-size-fits-all. In this *Executive Insights*, we'll discuss how the right approach varies by company, category, target consumer and a multitude of other variables that you need to consider.

The digital commerce landscape

The digital commerce landscape is dominated by three types of platforms: retail ecommerce, digital marketplaces and direct-to-consumer (DTC) websites.

Retail ecommerce providers offer consumers a wide variety of products from different brands similar to what is available in-store, although in some instances they only sell online.

These platforms typically act like a wholesale partner to the brands available on the website. For brands, retail ecommerce provides access to consumers familiar with the respective retailer — often a national retailer with wider consumer reach than any one brand has at its disposal. From the consumer's perspective, retail ecommerce offers a wide assortment of goods tailored to a specific category or subcategory, making it easier for consumers to find the quality items they're searching for.

For example, HomeDepot.com provides consumers with easy access to a wide assortment of home improvement-focused brands they otherwise might not find online. At the same time, brands get valuable exposure and consumer reach they otherwise might not attain, given the expense of marketing at that scale.

Digital marketplaces are platforms available to all brands and allow businesses widespread access to consumers.

A digital marketplace will likely offer a wide selection of categories or can provide shopping on social media sites. Amazon.com is the obvious and most relatable example. Amazon vendors have access to what may be the world's largest pool of online consumers, plus a number of Amazon-provided services like pricing assistance and product fulfillment. For their part, consumers have access to a wide array of products and can readily compare product reviews, seller reviews, prices and more as they shop.

Digital marketplaces aren't limited to consumer goods. Uber Eats, DoorDash and Grubhub are a blend of marketplace and retail ecommerce, fulfilling retailer demands as they partner with consumer packaged goods brands for advertising. The three platforms saw combined growth of 275% between 2019 and 2021, topping \$15 billion in revenue with 140 million total users.⁴

DTC websites include any brand-specific website offering its products directly to customers, often resulting in higher margins for the seller.

DTC websites allow the seller to have a more intimate connection with consumers. They can offer benefits to loyal customers, such as free shipping, member discounts or a tailored, virtual portfolio of items sent via email on a recurring basis.

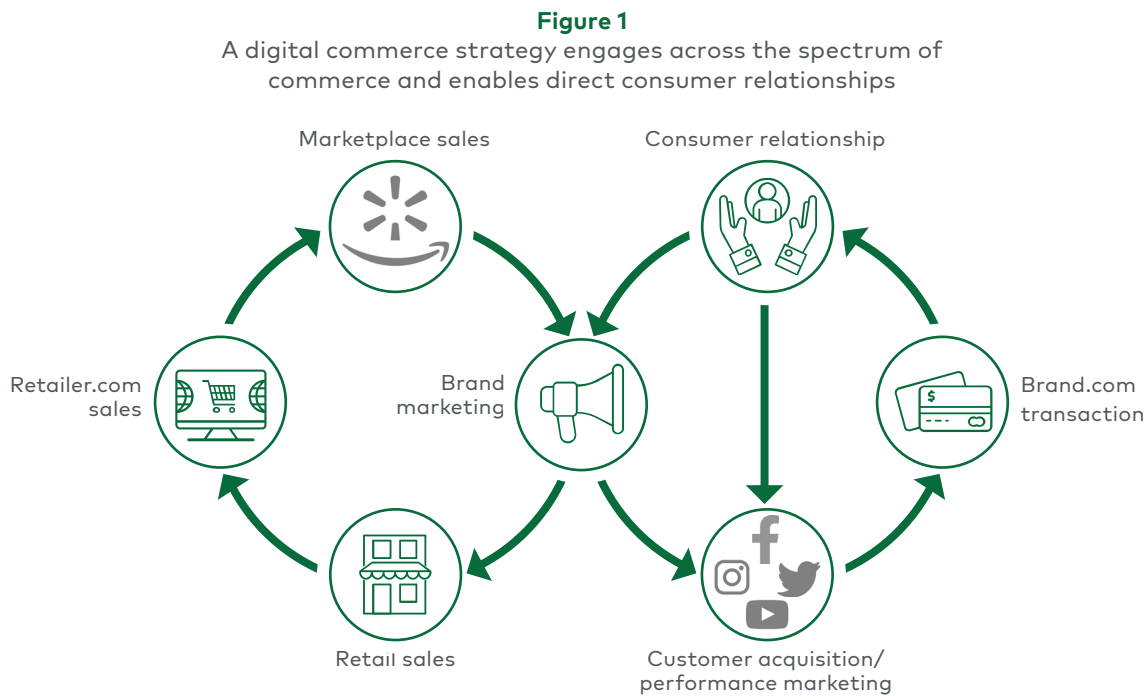
WarbyParker.com is a good example of a well-designed DTC website. It offers a wide variety of eyeglasses and sunglasses, which consumers can try on virtually before they buy. Consumers can also have up to five frames delivered to their home for in-person try-on at no charge.

Creating a myriad of benefits

Digital commerce has a direct effect on customer sales and relationships. But the indirect effects may be even bigger. For instance, although just 11% of U.S. consumers say they've bought items via social media, 65% say they've bought items on other channels after being exposed to them on social media.⁵

Even among avowedly brick-and-mortar shoppers, digital commerce can play a critical role in brand perception, loyalty and ultimate purchasing intent. Consider that 37% of consumers say they prefer to research online, then buy in-store. That's more than twice the number (17%) who say they'd rather research online, then buy online.⁶ By one estimate, 56% of in-store purchases are influenced by digital transactions.⁷

These realities are why an effective digital commerce strategy requires working across the spectrum of digital commerce. That way, you can create a myriad of benefits across all sales channels, not just digital ones (see Figure 1).



Source: L.E.K. research and analysis

Navigating the pitfalls

An effective digital strategy also requires recognizing the potential pitfalls of working with digital platforms so you can manage those relationships carefully.

Competition. Digital commerce offers consumers greater access to information, a wider selection of products from suppliers anywhere in the world and lower barriers to switching. As a result, competition between brands is greater than ever.

Rising fulfillment costs. Stockouts, supply chain bottlenecks and rising shipping expenses are putting digital commerce margins under pressure. These same issues can cause reputational harm and customer loss if brands don't manage their messaging.

Limited control. Consumers are increasingly factoring buyer reviews and social media into their purchasing decisions, making it harder for brands to directly influence consumers through traditional advertising.

Rising customer acquisition costs. The average amount merchants spent to acquire every new customer went from \$9 in 2013 to \$29 in 2021, a 222% rise. Much of that is due to higher digital advertising costs.

The push for privacy. A recent survey revealed that while consumers are more willing to share data today than they were two years ago, 43% still don't like sharing their personal data. Software and device makers are responding to these privacy concerns with tools that give consumers greater control over their online footprint (think Apple's App Tracking Transparency). That's a dilemma for merchants because consumer data is a big part of what makes ads more targeted and engaging in the first place.

Six steps to a winning approach

So, what does it take for brands to win in digital commerce?

1. Set the right goal for each channel

Understand the role of each digital commerce channel — be it discovery, volume, consumer data-gathering, brand reputation or something else. Then determine the consumer targets, merchandising, inventory positions, pricing and consumer value that would maximize your profitability. Use this information to determine where your digital presence would yield the greatest impact.

Case in point: Starbucks closed its online store in 2017 in favor of selling on third-party retail sites. Since then, Starbucks has focused its digital investment on its mobile app. There, customers can place orders and gain rewards points while the company's Deep Brew AI engine delivers personalized offers and suggestions. A quarter of all the orders Starbucks receives now come through the app.⁸

2. Invest in capabilities and infrastructure

Omnichannel is more than just inventory, positioning and pricing. It's about the entire customer experience. You'll need to coordinate with teams like analytics, merchandising, content development and marketing throughout the customer journey. You'll also need the right consumer and operational data to help with your decisions. And you may need certain technologies and partnerships to fully deliver on each channel's value proposition.

Case in point: In December 2021, CVS partnered with Microsoft to accelerate its consumer-centric digital strategy. Among other things, CVS intends to scale up its retail loyalty and personalization programs using advanced machine learning models on Microsoft's Azure cloud computing service.

3. Adapt your data capture strategies

Gone are the days when a generic 10% coupon code was enough to keep consumers engaged. As digital evolves to a privacy-first mindset, you'll need strategies that reflect the value that consumers derive from sharing their data as well as the value your brand will get from collecting it.

Case in point: By offering a chance to win prizes, Pets at Home persuaded its VIP members to complete an interactive questionnaire about various products and preferences. The campaign generated about 140,000 responses⁹ that helped Pets at Home serve their most loyal customers better.

4. Expand your data sources

Websites, social media, marketing campaigns and customer feedback are all valuable sources of data that help allocate product promotions and motivate customers to make a purchase. But if you want to understand your customers even better, look beyond the four walls of your marketing department. Consider the data that retailers get through in-store transactions, loyalty programs, location tracking and their own websites. A data-sharing arrangement can give brands and retailers alike a more complete view of the customer journey.

Case in point: Subaru collects data from its website, mobile app and social media. Subaru dealers, meanwhile, collect data from customers' activities in the showrooms. The automaker recognized that combining these data sources could improve its own predictive models and provide dealers with customer journey information that would improve purchase conversion. This proved true, resulting in an increase in conversion and reduced customer acquisition cost.¹⁰

5. Engage across the ecosystem

Don't try to do everything in-house. Look for organizations outside of your immediate market that can drive value to your customers through product, service and experience collaborations. As you expand your partner ecosystem, you can broaden your range of customers along the way.

Case in point: Nike and Dick's Sporting Goods collaborated across both physical and digital marketplaces to offer a more integrated shopping experience.¹¹ Customers also gained loyalty perks such as member-exclusive footwear and apparel launches. The arrangement allowed Dick's to round out its omnichannel experience and product catalog, while Nike gained enhanced customer touchpoints for its products.

6. Continually evolve your offerings

Digital commerce isn't standing still. Platforms are under continuous development, and consumers are a moving target. Although 71% of retailers feel they excel at personalized marketing, only 34% of consumers think the same.¹² To meet consumers when and where they desire, prepare to revisit every aspect of your digital commerce capabilities based on consumer feedback and market engagement.

Case in point: Walmart has advanced its buy online, pick up in-store capabilities and adapted its website to regional consumer preferences using location data. The retailer has also rolled out a mobile app that lets users build shopping lists, use barcode scanners and buy items with Walmart Pay.

Digital commerce done right

A successful digital commerce strategy approaches each channel in a way that's tailored to the nuances of each business and category. It also requires effective management by:

- Optimizing your digital ad spending
- Ensuring you have the infrastructure necessary to efficiently manage supply chain and logistics
- Properly assorting and merchandising your products for each digital commerce channel
- Making sure the business is positioned to scale as seamlessly as possible with demand

These aren't trivial challenges. But tackling them in a thoughtful way can increase brand exposure to a wider audience and lead to new, more intimate relationships with shoppers. Those are reasons enough to establish a digital presence where it's profitable and the consumers you're after are ready to engage.

For more information, please contact strategy@lek.com.

Endnotes

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