



The Coming Reality of Virtual Commerce

Imagine trying on a shirt by your favorite designer without leaving your home. Don't like the color? Simply wave your hand to better coordinate with the rest of your outfit. Imagine gazing at a new couch in your living room, considering how it works with the rest of your furniture. Too big for that room? Just whisk it to the family room without an ounce of effort. Imagine crawling into a tent with two of your friends to test if everyone will fit...despite the fact that you are physically located in three different cities!

These scenarios may seem like far-off, sci-fi fantasies, but they are real opportunities for retailers. In the first of a multipart series on virtual commerce, L.E.K. Consulting examines how augmented and virtual reality — AR and VR, respectively — are on the verge of transforming the way consumers shop. Just as retailers are racing to manage the fact that 10, 20 or 30+% of their businesses have moved online, a confluence of technologies like artificial intelligence (AI), computational imaging and beacon technology have emerged to disrupt, yet again, the emerging omnichannel paradigm.

While unsettling and scary, the successful incorporation of AR/VR into retail models also has the potential to vastly change the way retailers are thinking about stores-of-the-future. The successful navigation of this sea change will inevitably create new opportunities — and winners.

The momentum for augmented and virtual reality in retail applications is building. Investment in the sector is hot, with AR/VR startups raising \$658 million in equity financing in 2015, across 126 deals.¹ Headset manufacturers like Facebook (Oculus Rift), Microsoft (Hololens), HTC (Vive) and Sony (PlayStation VR) are also aggressively investing, looking to win a share among the early adopters and establish themselves as the leaders in the space. Many of these units are expensive (Oculus is \$599 and the Hololens is \$3,000), but prices will drop and entry price points will be tested (e.g., the Samsung Galaxy VR was released at \$99). On the back of a coming wave of mass-market products and a proliferation of associated gaming content, headsets should soon start to penetrate mainstream. CS Insights expects the number of sold VR devices to grow from 2.2 million in 2015 to 20 million in 2018.

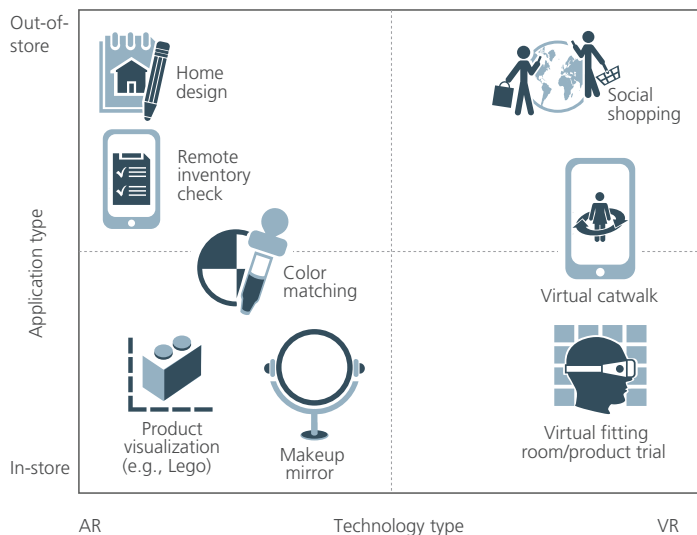
The reality is that most consumers already have AR-equipped smartphones (every modern iPhone or Android device is a potential platform), but thus far there has been no “killer app” to prompt widespread use. If other entertainment successes follow, businesses will need to accelerate the pace at which they translate similar AR functionality into their worlds.

The Coming Reality of Virtual Commerce was written by **Dan McKone** and **Robert Haslehurst**, Managing Directors, and **Maria Steingoltz**, Principal, in L.E.K.'s Consumer Products and Retail practice.

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Figure 1

V-Commerce choice framework
(Early applications and likely environment for initial traction)



Source: L.E.K. analysis

AR/VR has the opportunity to be a game changer for the retail sector because it enables retailers to eliminate customer pain points, elevate customer service and create a differentiated, personalized customer experience. Some projections put AR/VR in retail at approximately \$30 billion by 2020 (from nothing today) — or nearly 20% of the entire exploding industry.²

The landscape of virtual commerce can be considered along two dimensions. First is the question of whether an individual application is best realized as augmented or virtual reality. VR is a fully immersive system that puts the consumer inside a virtual world. It requires stand-alone technologies like headsets and, typically, a controller. AR is partially immersive. The consumer overlays virtual elements onto real-life objects, augmenting reality. It only requires a consumer to simply have a smartphone or tablet, rather than an incremental device, although appealing “glasses” may emerge once the content and killer app have been established. VR, while potentially more compelling, presents a higher barrier in the near term as consumers haven’t (yet) been conditioned to wear devices (even in their homes) or do anything more than play games. With the emergent AR gaming craze, e.g., Pokémon GO, AR suddenly seems tangible — just the next generation of the bionic extension that has become the personal device.

Second is the question of whether the application will be used in-store or out-of-store. In the long run, the in-store versus out-of-store dimensions are likely to blend together, but in the near term, there is a subset of environments where early applications are expected to gain traction (see Figure 1). In-store applications would involve a consumer interacting with AR/VR either within the physical

four walls of a traditional shopping environment (e.g., on the sales floor or in the dressing room) or right next to it (e.g., through windows). Out-of-store applications would have the consumer virtually engaging with the retailer at home, at another physical location, or even on the go. For example, an ecommerce-only player could transform itself into an asset-light, omni-channel player by virtually re-creating the benefits of physically being in a store.

With a backdrop of slow-to-negative traditional store comps and increasingly pressured returns on invested capital, retailers certainly have every incentive to vet the potential of AR/VR. The first step is to pick which spots to focus on; in particular, retailers must decide in which box(es) of the v-commerce choice framework to invest and then follow a multi-faceted approach.

- Determine the customer target.** Retailers must identify the segment(s) of their customer base for which an AR/VR solution would be most appealing. This will typically be cohorts who have the greatest need for a solution given current pain points (e.g., budget or time constraints), or who would have the most to lose without it. Defining the characteristics of the target customer (demographic, behavioral, psychographic) will help ensure organizational alignment to tailor the solution to a particular group, of a particular size. A clear benefit of an AR/VR offering is the ability to micro-target an offer to appeal to consumers on a one-to-one basis.
- Establish the value proposition.** A compelling value proposition must be immediately obvious to consumers at their initial point of interaction with a retailer’s AR/VR application. To do that, retailers must first ensure that their offer is relevant to their end consumers by explaining how the application solves their problems. Second, the solution must deliver specific benefits that are uniquely differentiated from those available from the competition. Retailers must ensure that the content offered and the solution’s value proposition are compelling and resonate with consumers. This will be critical not only to acquiring customers but also to engaging and retaining them after an initial trial.
- Develop the business model.** Once the customer target and value proposition are defined, the retailer must develop the business model for its AR/VR application, which will determine the rules by which the business should operate. These rules will involve defining the resources that are to be deployed, the organizational structure of the business and the responsible parties for decision-making. A successful business model must also set concrete financial goals and metrics by which to measure progress, and then evaluate its development at regular intervals. Doing so will ensure a nimble approach to meeting consumer needs with a still-developing technology.

Executive Insights

While the AR/VR landscape is emerging, retailers should begin taking steps to prepare for its full potential. Aptly navigating the v-commerce choice framework can help unlock the value of this emerging technology for retailers. Deciding how to play early, and which bets to place now, will let retailers lead in this emerging space and not be left behind. We will continue to explore opportunities in virtual commerce in future installments of this multipart series.

¹ Investment In AR/VR Startups Hits A New All-Time High in Q4'15, CB Insights, January 5, 2016.

² Augmented and Virtual Reality to Hit \$150 Billion, Disrupting Mobile By 2020, TechCrunch.

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How Is AR/VR a Game Changer?

1. It eliminates customer pain points:
 - **Time:** reduces or eliminates the time it takes to go to a physical store; look around for a product, size or alternatives; and wait to check out
 - **Budget:** enables customized offers to be delivered to consumers at a relevant time and location
 - **Lack of convenience:** facilitates interaction with a product individually (e.g., virtual dressing room, home design) or in a social setting (e.g., social shopping, virtual catwalk)
2. Elevates customer service by providing enhanced information about products, eliminating wait times and better enabling brands to deliver on their brand promises
3. Creates a differentiated, personalized customer experience by virtually delivering the exact product and offer that is relevant to a given consumer

About the Authors



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