Executive Insights

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Total DTC: Building a Better Approach to Reach Your Consumers

Over the past few years, both leading and emerging brands have increasingly embraced direct-to-consumer (DTC) distribution alongside traditional retail. DTC is being ushered in by three factors. First, the rise of technology and scalable platforms has made reaching consumers directly easier and cheaper than ever before. Second, DTC natives (digitally native vertical brands such as Dollar Shave Club and Casper) have provided a range of archetype business models, and with them an understanding of what works and what doesn't. And third, consumers' expectations have shifted, and they now expect brands to authentically interact with them.

Many companies have already embarked on a DTC journey, especially online. L.E.K. Consulting recently studied 176 representative brands across consumer goods categories, finding that almost all of them have made significant inroads when it comes to engaging directly with consumers; 65% of brands sell directly on their own sites, over half incorporate consumer feedback into their sites and approximately half have their own stores. Indeed, whether digital or physical, can brands afford not to move their DTC strategy forward in a world of complex new purchase journeys and big data?

Total DTC strategy

Direct to consumer means just that: reaching customers directly, without a middleman such as a physical retailer, an online retailer, a cable company or a travel agent (for more, see our video Direct to Consumer: Challenges and Opportunities). That alone is a significant shift, as brands have traditionally reached consumers through these intermediaries, and haven't built the capability to directly manage their own customer relationships. But too often we see clients hear "DTC" and go straight to a narrow focus on selling direct on their website. We believe that in order to win, brands need to think about DTC more broadly, to coordinate every touch point with the consumer — to embrace "Total DTC."

Total DTC means building a DTC strategy that covers every stage of the customer life cycle, with a particular focus on acquisition, selling and customer engagement. DTC can therefore sometimes mean fundamental changes to the product, such as offering subscriptions and services where once there was only product. DTC is also inherently multichannel, encompassing brand.com websites but also other digital channels and the brands' own physical stores. We also see DTC as inexorably linked to marketplace strategy, and particularly to how brands manage their presence on Amazon, given how important marketplaces are in product discovery and customer acquisition. So success of a Total DTC strategy should be seen in both direct sales and overall brand health — with measurable impact on sales through other channels.

Total DTC: Building a Better Approach to Reach Your Consumers was written by **Rob Haslehurst**, **Jon Weber** and **Noor Abdel-Samed**, Managing Directors, and **John Moran**, Principal, in L.E.K. Consulting's Consumer Products practice.

For more information, contact consumerproducts@lek.com.

And Total DTC isn't just relevant for consumer goods. The media industry, for example, is also in the midst of a DTC transition, as are the travel industry, parts of financial services, healthcare and more.

The DTC revolution

Digitally native vertical brands such as Warby Parker, Bonobos, Allbirds, Dollar Shave, Uber and Netflix have seen opportunities to build businesses from scratch in the new world — and have become household names in the process. They have leveraged digital technology to fundamentally alter how individuals consume their products and interact with the brand. In return, they get to understand their consumers more quickly and more fully, which has led to a virtuous circle of improvement.

Figure 1

Proportion of brands with transactional websites and reviews on websites

Source: L.E.K. research and analysis

But established powerhouse brands such as Nike, Disney and Apple have also embraced DTC and have made changes to their corporate organization to address DTC's strategic role. For example, Nike recently created the "Nike Direct organization," which brings together Nike.com, owned retail and Nike+ digital products. Disney, a company that was arguably already a "direct" pioneer in its stores and theme parks, has established a DTC business unit — including Disney-branded TV and film content, as well as the ESPN+ platform — to compete with online streaming services.

These mega firms are not the only brands investing in DTC, though. In terms of brands selling on their own websites, our review across consumer goods categories found that current strategy varies significantly by sector. Apparel and footwear brands have widely embraced DTC sales, whereas penetration is lower in consumable categories like food, beauty and personal care. (See Figure 1.) But far fewer brands engage in the full personalized life cycle marketing needed to drive ongoing loyalty. Of the brands we looked at, only about half — mostly concentrated in luxury and apparel — have a brick-and-mortar retail presence.

The three components of a Total DTC strategy

A DTC strategy has to address each of the three key phases of the customer life cycle: acquisition, sales and engagement (sometimes thought of as maintenance or churn management). Brands can touch customers directly at each step of the life cycle, but also must recognize that consumers don't move in direct pathways and are free to interact across both direct and indirect channels, so strategies have to account for those other touch points as well. (See Figure 2.)

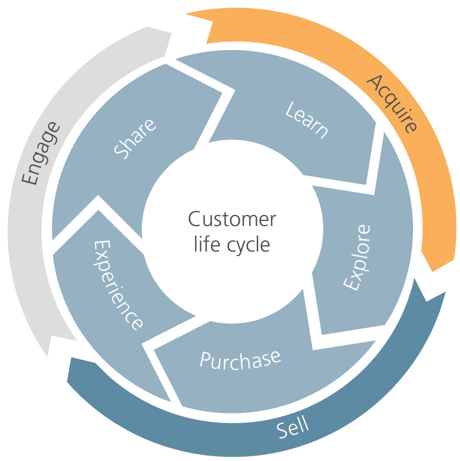
1. Acquire new customers.

Most brands are already familiar with marketing, but making DTC core to a brand's strategy means retooling the consumer pipeline to maximize DTC impact. Brands already spend on social media, search engine marketing and other digital tools as part of their broader marketing mix, but the needs of a DTC business up the game in terms of personalized marketing. A commitment to Total DTC typically starts with having to develop a channel-centric customer segmentation (a view of customer segments that factors in channel preferences and interest in direct engagement; this may exist alongside style or loyalty segmentations) that lets brands focus on delivering the right DTC experience to different segments based on their potential. By combining this with an investment in customer identity, you can direct consumers with different characteristics to the most effective messaging and experience. It is also helpful to build an advocacy strategy that leverages loyal customers to authentically amplify your brand's reach both online and offline.

2. Sell to customers directly.

The sales step is a critical part of DTC, but it is rare that a brand can use its website to affordably build the traffic needed to make dot-com sales meaningful on Day One. Furthermore, leading ecommerce players are continually raising the bar. Users need a seamless experience, safe and hassle-free checkout, free or cheap shipping, and customer service for when things go wrong.

Figure 2
A robust DTC strategy presents opportunity to optimize all parts of the customer life cycle



Source: L.E.K. analysis

Success at DTC selling therefore means success at building out a retail function — which for many brands means using a new muscle group. Brands must have capabilities and processes in merchandising, fulfillment, technology, customer service and more. To do this, they often need to set up a new business unit, bring in outside talent and selectively leverage partnerships. Some larger consumer companies have acquired DTC native brands to rapidly build these capabilities, as Serta Simmons did in its acquisition of Tuft and Needle.

Brands also need to manage adjacent channels such as marketplaces as customer acquisition tools, while being clear about any "third rails" of channel conflict. While in most cases we see discomfort about channel conflict being overblown, there are going to be times when brands need to be willing to (strategically) walk away from current channels. As it transforms to appeal to younger consumers, jewelry brand Alex & Ani is in the process of shifting from an already high DTC penetration of close to 50% to more than 75% by trimming specialty/mass retail partnerships and refocusing on owned ecommerce and its own stores, as well as pop-ups.

3. Engage with customers.

There are many ways that brands can create and nurture communities of customers, about whom they now know much more. Taking a life cycle view of consumers and talking to them in a relevant and authentic manner are both critical. For subscription DTC businesses, churn management and maximizing lifetime value are also absolutely critical, and brands have to maintain a dialogue with customers to encourage them to keep seeing value in their purchase. In other cases, there may be a role for a loyalty or advocacy program to reward and encourage customers to maintain ongoing engagement. Either way, the level and goal of consumer engagement for a DTC brand are an order of magnitude higher than for traditional brands. Procter & Gamble's Tide laundry detergent, for example, instituted a subscription service for its Tide pods, as well as an on-demand laundry service in select cities. Together these services build ongoing, habitual relationships with Tide customers.

Benefits of a Total DTC strategy

Increased control over the customer experience. DTC allows brands to decide how and where they engage with customers, the types of messages that reach those customers, and — by extension — the essence of the brand.

Higher-margin sales. Selling direct to consumers eliminates third parties and expands margins. However, in addition to the cost of acquisitions, brands need to use those higher gross margins to offset new costs, such as for shipping, staff, packaging and rent.

Deeper customer loyalty and lifetime value capture. Dealing direct lets brands take control of their lifetime value and benefit from recurring economics, particularly through subscription models.

Larger quantity and better quality of consumer data. Data is the key to personalization, and the direct model puts that in the hands of the brand.

Limited brand exposure to shocks/disruption within the traditional value chain. The retail graveyard, from Toys R Us to Sears, makes clear the risks in the retail landscape. A mature DTC strategy provides a hedge against these shifts, letting brands weather downstream change.

In spite of all the benefits that a focused DTC strategy will yield, brands looking to develop one will face several challenges. One is how to balance the needs of any current channel partners. Another is how to develop capabilities that will allow brands to reach — and understand — their customers. In order to successfully develop those capabilities within the "acquisition" and "engagement" phases, brands need to build and maintain the knowledge and skills necessary to identify, reach and message their customers. That could mean investing in new infrastructure and talent across the organization — from sales and marketing to technology, analytics and more. And to support their sales strategy, they will need to build infrastructure, which could include anything from an online review platform to real estate for a flagship or pop-up store.

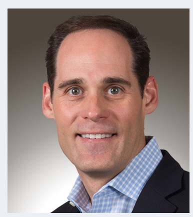
The way forward for DTC

As consumers expect more personalized engagement from their brands, those brands can stay relevant if they develop an effective Total DTC strategy covering the three stages of the customer life cycle.

How brands implement their strategy will depend on who their customers are and what the brand hopes to achieve, and brands must create a tailored approach. For example, some will rely solely on digital components of DTC, while others will go broader. Some may choose to focus on using DTC as a way to maintain customers, while others may focus on sales or the acquisition of new customers. Some will look to purchase these capabilities (or even to purchase another native DTC brand), some will partner, and others will develop their capabilities organically. Regardless, the bar will keep on rising, and brands that fully embrace a Total DTC approach will be best positioned to stay ahead.

About the Authors

Robert Haslehurst is a Managing Director and Partner as well as the head of L.E.K.'s Boston office and a member of the firm's Americas Regional Management Committee. He is focused within the Retail and Consumer Products practices. Rob advises clients on a range of issues, including corporate strategy, consumer insights, new product development, program management, corporate finance and M&As.



Jon Weber is a Managing Director and Partner in L.E.K. Consulting's Boston office. He serves on the firm's Global Leadership Team and leads L.E.K.'s global Retail and Consumer Products practices. Jon has extensive experience working across retail channels and with worldwide consumer brands, and is a leading advisor to the apparel and footwear industries.

Noor Abdel-Samed is a Managing Director and Partner in L.E.K. Consulting's Boston office and a Consumer Products sector specialist. He has deep expertise in digital, omnichannel, ecommerce, consumer segmentation, pricing and promotions, and has significant experience leading teams through market-facing and organization-changing initiatives from conception through implementation.

John R. Moran is a Principal in L.E.K. Consulting's Boston office. John focuses on commercial strategy for consumer and travel companies, specializing in issues such as innovation, digital, customer experience, channel management and M&A. He previously worked at P&G.

About L.E.K. Consulting

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