



The year 2011 will represent a turning point for Australia's retailers, with dramatic growth in the number of consumers willing to shop online. But will retailers be able to rise to the occasion?

How Australia's retailers can profit from the coming boom in online sales

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It's no secret that Australia lags other countries in making online purchases. Although Internet penetration is strong, Australians spend one-third as much online as US consumers on a per-capita basis and one-fourth as much as shoppers in the UK. Why is Australia so far behind?

Unlike their US and UK counterparts, the overwhelming majority of retailers in Australia have focused efforts on their traditional stores, where they've made heavy investments, instead of developing online outlets. And with the Australian online market still relatively small, even those retailers with an online presence have found investments in a broad product range or advanced website functionality difficult to justify.

Despite these issues, Australian consumers are on the verge of a major shift in their shopping habits. A new Bain & Company survey of more than 1,000 Australian consumers concludes that online spending will dramatically increase this year. The question is, will Australian retailers—sellers of everything from white goods to cosmetics to travel to groceries to mobile phones—be able to profit from the coming boom? Or will they lose the sales to overseas sites? With the Australian dollar suddenly soaring—reaching parity with the US dollar for the first time in 2010—more consumers are bypassing Australian retailers and shopping overseas.

Online sales overall in Australia are expected to grow almost threefold by 2015, to nearly \$30 billion, according to Morgan Stanley. For the second consecutive year, Bain surveyed consumers representing all ages, incomes and locations throughout Australia. The results show online retailing is beginning to reach mass adoption rates. Based on the survey results, the number of consumers who have shopped in some categories has doubled in the past 12 months. This growth is particularly striking given subdued consumer confidence and weak retail sales growth overall. Meanwhile, the number of consumers who would “consider” shopping online has more than doubled in certain categories—a strong indicator of the growth still to come (see Figure 1).

Our survey was designed to help us understand who is shopping online in Australia, what they're buying and the challenges facing companies hoping to sell to them. We learned that the highest growth in online shopping is likely to be in categories where sales penetration has so far been relatively low: hardware and do-it-yourself products, fitness/sport and furniture (see Figure 1). And people who have already bought books, videos or travel services online (among the most popular items) are now buying a wider range of new products, everything from fitness equipment to stationery to groceries, a traditionally unpopular online category. The survey results show a 50 per cent increase in the past year in the number of consumers who tried online grocery shopping.

We also learned that in addition to the growth of low-penetration categories, we can expect increased activity in high-penetration categories such as digital content, event tickets, travel, insurance and mobile phones. For example, we found the ranks of those who purchased digital content grew by 34 per cent this year, to the point where more than half of the consumers we surveyed have now bought digital content.

Consumers who are trying online shopping and are satisfied with the initial experience tend to return to those sites

An increase in spending

In addition to expanding the range of products they will purchase online, Australian shoppers expect to spend more over the next 12 to 24 months. Among those surveyed, nearly 7 per cent plan to increase substantially the amount they spend on Web purchases of general merchandise, and more than 26 per cent will modestly increase their spending. More than 50 per cent intend to spend roughly the same amount, and only 17 per cent said they would either not purchase general merchandise online or would spend less. That rise in volume has implications for retailers. Consumers who are trying online shopping and are satisfied with the initial experience tend to return to those sites. In a market that is moving quickly from a small base, first movers have an advantage.

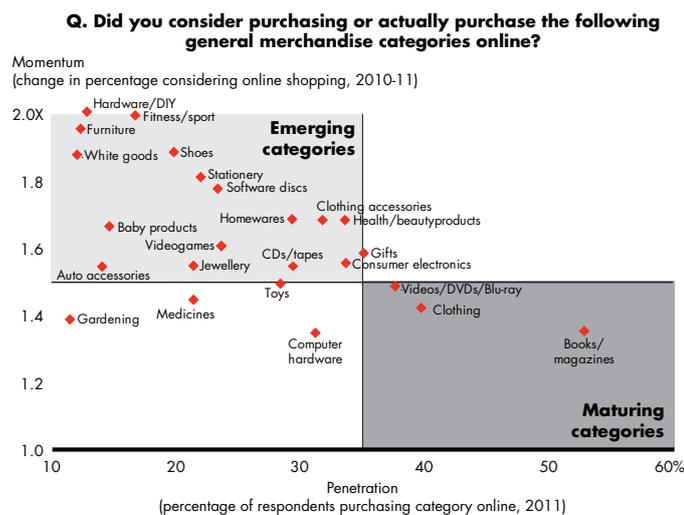
In an increasingly competitive online market, Australian retailers argue that overseas sites have an unfair advantage because they are exempt from collecting the goods and service tax on purchases below \$1,000. A

more serious issue may be the prices that the owners of global brands have come to expect that Australian consumers will pay, and the strong gross margins that Australian retailers have come to enjoy. A full 53 per cent of survey respondents who shopped on overseas websites said that price was the main reason they did so, and nearly 40 per cent said that product selection or availability was the main reason. But our survey found that Australians are willing to shop on domestic sites if they provide the right mix of price, selection, convenience and security. In fact, Australian consumers in 2010 still made 77 per cent of their online purchases on Australian websites compared with 23 per cent on overseas sites. Australian retailers will need to invest in their online capabilities—and some may need to reduce prices—if they are to maintain this advantage.

What do consumers want?

How can retailers better satisfy the Australian consumer? Average transaction size varies by category (see Figure 2), but to dig deeper

Figure 1: Online shopping will continue to grow



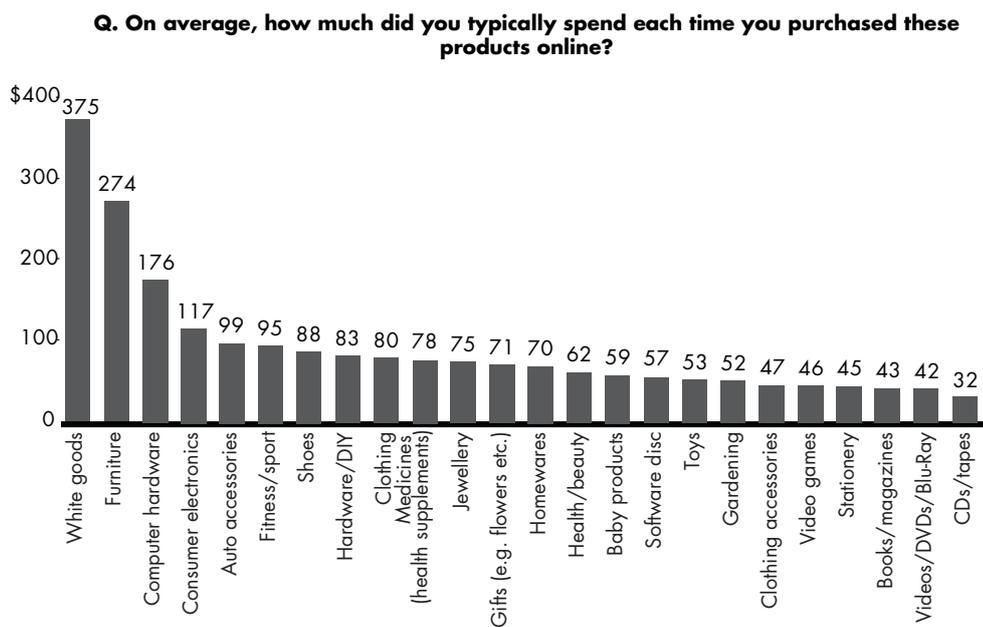
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into what consumers want, we asked survey participants to rate the importance of 13 different factors in making online purchases. They ranked secure payments and low price at the top of the list, followed by ease of delivery, convenience (shopping outside regular business hours) and the quality of the website (see Figure 3). While consumers who have made online purchases are generally happy with the price, value for money and convenience, they are less satisfied with online customer service. The message to online retailers is unambiguous: invest in a site that looks good and makes it easy for customers to find what they want, and don’t forget the importance of having superior customer service online.

What’s keeping shoppers from going online for even more of their purchases? The No. 1 reason among respondents was something that online retailers sometimes find difficult to overcome: 31 per cent ranked a desire to touch and feel the product as the most important factor (see Figure 4). To address this issue, a growing number of

companies offer easy return policies, and in the US, some retailers are experimenting with creative online solutions. For example, Lands’ End customers can zoom in on a picture of a garment to see the weave of the fabric. Other issues raised by consumers may be easier to address. For example, among survey respondents, 13 per cent cited delivery concerns as a reason to resist shopping online. To help overcome this obstacle, companies are introducing next-day or even free shipping. Coles and Woolworths both offer next-day grocery delivery (for a fee) and, to make it more convenient, customers can pick a two-hour delivery window. Eleven per cent of our respondents say they don’t shop online because they want to speak to a salesperson. Proactive companies now offer online chat options. And 9 per cent say they don’t trust online payments. That opens the door for retailers to convince consumers that online transactions are secure.

Figure 2: Spending on general merchandise varies by product segment



Note: Eliminated top and bottom 5% of each product category data as outlier; question asked to respondents who have online shopping experience

Taking advantage of the online shopping trend

Based on the survey results, traditional Australian retailers have a tremendous opportunity as consumer habits undergo a radical shift and they spend more online. To take full advantage of the move to online shopping, retailers can look at success stories overseas and at home. Online pure plays like US-based Amazon.com have ushered in the waves of innovation that define what e-commerce is today. Survey results show that Amazon attracts more Australian general merchandise shoppers than any Australian website.

Amazon pioneered the concept of providing shoppers with extensive product reviews, purchase suggestions and a mix of new and used product choices. The company has steadily powered growth with a long-term strategy that includes building partnerships and making acquisitions. As of 2010, Amazon was the pure-play leader, with annual sales

that topped \$34 billion. Its core business remains books and media, categories that lend themselves to online retail because of the products’ high value relative to weight, the emergence of digital content and the opportunity for follow-on purchases.

That’s one reason Amazon acquired Zappos, the No. 1 seller of shoes online. Zappos has set the standard when it comes to assuring consumers they can buy a product on the Web as personal as shoes without trying them on. The retailer introduced the no-questions-asked return policy that’s good for 365 days after a purchase, and it also provides a 24/7 call centre.

That’s not to say Australian retailers haven’t developed successful online strategies

Australian consumers list four sites as their favourites for new general merchandise: eBay, Amazon, DealsDirect and JB Hi-Fi. DealsDirect is an online-

Figure 3: Security and price are the most important factors when purchasing online, followed by convenience

Q. On a scale of 1 to 5, how important are the following elements to you in deciding whether to purchase a new general merchandise product online?



Note: Question asked to respondents who have online shopping experience

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only retailer that has used bargains and a wide range of products to become Australia’s largest online department store. Its cavernous 40,000-square-metre distribution centre allows it to offer everything from toys to furniture to kitchenware to bedding for immediate delivery. JB Hi-Fi is an even more important example for traditional retailers. The consumer electronics player has emerged as one of Australia’s most successful online retail shops, offering a broad range of products and competitive prices. The company invested in online capabilities while also building out its network of physical stores. Experian Hitwise named JB Hi-Fi the second-most frequented Australian online retailer. In the nine months ending January 1, the site had 9.5 million hits. Only Apple, with 10.8 million hits, had more.

Like JB Hi-Fi, other Australian retailers will find that their biggest advantage when competing with overseas websites may be their brick-and-mortar assets. The winners

will be those that make the most of their substantial investment in physical stores to build online sales and vice versa.

Building blocks for winning online

As Australian retailers race to catch up with fast-changing consumer shopping habits, they need to develop a long-term strategy and clear road map to take full advantage of the e-commerce revolution under way. We’ve found that five building blocks underpin winning online retail sites. They arm retailers with the information, tools and insights needed to identify which consumers want to shop online, how to cultivate their loyalty and how to improve the overall shopping experience. It’s a five-step formula for sustained success.

Step 1 Understand customer opportunities. Building a successful online business involves developing insights into customers’ unmet needs—and using those insights to discover

Figure 4: Shoppers' desire to touch and feel products is the key roadblock to online shopping

Q. What is currently stopping you from purchasing more general merchandise goods online?



Note: Respondents allowed two choices

To stem the flight to overseas sites, Australian retailers need to focus more clearly on what customers want to buy online

how best to give customers what they want. The process starts by identifying high-value customers or customer segments—they may be a subset of your existing customers or they may be new ones. Next, profile the targeted customers to determine the size of the opportunities. Understand how shopping varies by segment, category and channel—and how much of this shopping will or could move online.

To find these answers, retailers have to conduct research into shopping habits and behaviour and learn which products targeted online shoppers are interested in buying, for which occasions and why they will opt to make their purchases on your site. To learn their priorities, ask what's most important—the ability to compare products easily, a secure and fast checkout process, a no-fuss return policy and customer support? Retailers rely on an array of data sources to create an in-depth view of the value and needs of existing and potential customers. They include gathering qualitative and quantitative customer research; analysing transaction records and purchasing data from loyalty programmes; reviewing email and promotion response rates; and tracking consumers' online searches, shopping patterns and social media exchanges. Based on the resulting insights, winners innovate offerings that can change the very nature of the consumer value proposition.

For example, a company we'll call OfficeSupply Co. used this approach to jump-start growth and sales. Its traditional channels—retail stores, mail order and direct sales—were experiencing declining sales and profits. And it faced a stagnant market for years to come. OfficeSupply Co. conducted in-depth customer and market research to identify its most valuable clients and the most profitable channels to serve them best. The company discovered that it had four main customer segments, and it needed a new market strategy that matched each segment with the best channel to maximise

both growth and profitability, including the launch of an online shopping site. By first clearly identifying and understanding its Web shoppers, OfficeSupply Co. was able to tap the potential of its online customer segment.

Step 2 Get the range of products right. Simply put, make sure you stock what consumers want to buy. Retailers should never underestimate the power of an online store's product assortment to attract shoppers and keep them coming back. Remember, nearly 40 per cent of the survey respondents said they shopped on overseas sites because they had a broader range of products. According to JP Morgan, many major Australian retailers' sites, including Big W, David Jones, Myer and Just Group, offer a more limited selection than in their physical stores.

To stem the flight to overseas sites, Australian retailers need to focus more clearly on what customers want to buy online. Many e-commerce leaders take a comprehensive approach, using a wide range of products to attract customers. For example, US-based Foot Locker gives shoppers on footlocker.com the ability to buy everything stocked in its distribution centre, which has a much broader range of sporting apparel products than traditional Foot Locker stores. If you type in the words "men's basketball shoes" up pop more than 300 shoes in a range of styles, colours and sizes.

Other retailers use their websites to create a specialised offering. Take J.Crew: The apparel retailer attracts shoppers with exclusive lines found only at its online store. And low online infrastructure costs also make it possible to launch specialty shops like J.Crew's "Handbag Shop" and "The Men's Shop" to profit from categories with high online purchase histories.

A cautionary note: while the product assortment online and in physical outlets may not be identical, shoppers shouldn't feel like they're in two completely different stores.

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Aligning the “look and feel” of the shopping experience in different channels is critical for a brick-and-mortar retailer building an online business.

Step 3 Make your online offering distinctive.

Survey respondents rank lower prices and convenience as among the top reasons they shop online. Meanwhile, some sites have found that enjoying a personalised experience that they can't find in traditional stores and being part of online communities are other strong draws. We've found that by giving shoppers a customised and satisfying online experience, they're more likely to return and spend even more. In fact, competing primarily on price can become a risky and unsustainable game.

How to do it? Several sites give repeat shoppers customised recommendations based on their prior selections. This is territory pioneered by Amazon, which culls data from a customer's browser history to recommend other products. Companies like Nike take customisation to another level with NIKEiD. At nikeid.com, shoppers can personalise the colour, style and details of their footwear, apparel and equipment. And Longchamp allows its customers to create “your very own Le Pliage” purse, down to the type of handle and embroidery options. Australian Moonpig.com.au, an online personalised greeting card company, offers shoppers no fewer than 7,000 designs. Within 24 hours, the cards are printed and shipped.

In addition to personalising the experience, online leaders engage customers and win their loyalty by building a community. Australians lead the world in time spent each month (over seven hours) on social media sites, according to Nielsen Company research. So they are primed for online retailers that enrich the shopping experience through online communities and social networking. The use of social media by retail sites runs the gamut, from peer product ratings and reviews to

promotional offers to forums for swapping experiences, posting pictures and organising activities. In its simplest form, social media is a highly effective and inexpensive way to reach consumers directly. The impact can be huge. Consider Victoria's Secret's use of Twitter. The company tweets 140-character promotions and alerts about its lingerie and apparel lines—and customers follow. Between November 2010 and February 2011, Victoria's Secret doubled the number of its Twitter followers to 60,000. Another retailer capitalising on the growth of social media is beauty products retailer Sephora. By using third parties like Facebook, Sephora generates a buzz and leads customers to its website. Its Facebook page has over one million fans. Consumers find special offers, a discussion board and product links.

Marks & Spencer, Macy's and other retailers have discovered the power of user ratings and reviews on social media to gain trust, convert shoppers, build loyalty, boost sales and reduce the number of returned products—all of which results in fewer dissatisfied customers. Macy's uses online customer ratings within product categories to enhance searches. Petco.com, the US-based pet products retailer, found that its customer conversion rate rose by nearly 50 per cent for its top-rated products.

Retailers have found some unexpected benefits to communicating with consumers online. Consider the value in negative product reviews. Land of Nod, a high-end children's furniture maker, uses them as a way to learn about product flaws and reach out to unhappy customers that they otherwise wouldn't have known about. For example, when customers posted complaints about the surface of an expensive activity table, the company redesigned the product—and offered to send free replacements. Winning online retailers invest in state-of-the-art technology that constantly updates customers' favourite picks on their sites. The investment pays off in deeper trust and

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Online leaders engage customers and win their loyalty by building a community

the ability to take full advantage of customer feedback—research shows that when online stores spotlight “most viewed items,” it influences like-minded shoppers.

Community forums also give consumers a voice, strengthening their engagement and often their loyalty. For example, Toyota uses its site to connect brand fans, urging fellow Toyota owners to share their “stories from the road”.

Step 4 Leverage your physical stores. Retailers should make the most of their substantial investment in brick-and-mortar assets to build online sales and vice versa. In the US, companies like Sears allow customers to make purchases online and then, after they are notified of product availability through an email, pick up the products in the stores within minutes of their arrival. The service enables customers to overcome worries about missed or late deliveries. Companies like Starbucks use their online presence to generate store traffic, sending out alerts to such promotions as “Free Muffin Day”. Customers bring in a voucher printed from their computer at a specified day and time for a free muffin with a coffee purchase. Nordstrom, Peter Alexander and others allow in-store returns of purchases made online, making the returns process easier and more convenient. They also give in-store customers the ability to order a wider range of products via kiosks that link them to online sites. Another move: providing in-store customers with coupons that give them discounts for online purchases.

Step 5 Deliver an outstanding customer experience. Recruiting online shoppers means addressing their concerns. Almost 40 per cent of surveyed shoppers pointed to security and delivery as two of the major reasons they don't shop online. To overcome these barriers, retailers must create convenient, fast, easy-to-use and secure online stores. Leading retail sites have innovated a number

of solutions. Again, Amazon has taken the lead. The company has won over customers wary of complicated online payment processes by offering “single click” purchases and express checkout.

The growth of online payment services such as PayPal and security services like VeriSign help assure consumers that their online purchases are secure. But even with such options, smaller retailers may find themselves at a disadvantage in gaining consumer confidence: the absence of a strong, trustworthy brand will be a barrier for some consumers. That is one of the advantages well-known traditional retailers enjoy.

It's equally important to offer an efficient, cost-effective shipping policy. Best Buy's in-store pick-up service fills an important need. Customers who purchase products online are notified within 45 minutes when they'll be available for pick up at a local store.

Easy return policies are critical, too. That's why Zappos includes a free return shipping label with each delivery, good for 30 days. It's one of the many policies that have helped the company generate loyal customers.

Online success stories like Zappos can serve as a model for Australian retailers as they join their counterparts in the US and UK online. Even late to the game, Australian companies can surpass competitors at home and abroad by embracing the possibilities online, and by knowing the building blocks for success. That means understanding the customer opportunities, getting the range of products right, making online offerings distinctive, leveraging physical stores and delivering an outstanding customer experience. 

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Founded in 1973 on the principle that consultants must measure their success in terms of their clients' results, Bain works with top management teams to beat competitors and generate substantial, lasting financial impact. Our clients have historically outperformed the stock market 4:1.

Who we work with

Our clients are typically bold, ambitious business leaders. They have the talent, the will and the open-mindedness required to succeed. They are not satisfied with the status quo.

What we do

We help companies find where to make their money, make more of it faster and sustain its growth longer. We help management make the big decisions: on strategy, operations, technology, mergers and acquisitions and organization. Where appropriate, we work with them to make it happen.

How we do it

We realize that helping an organization change requires more than just a recommendation. So we try to put ourselves in our clients' shoes and focus on practical actions.



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