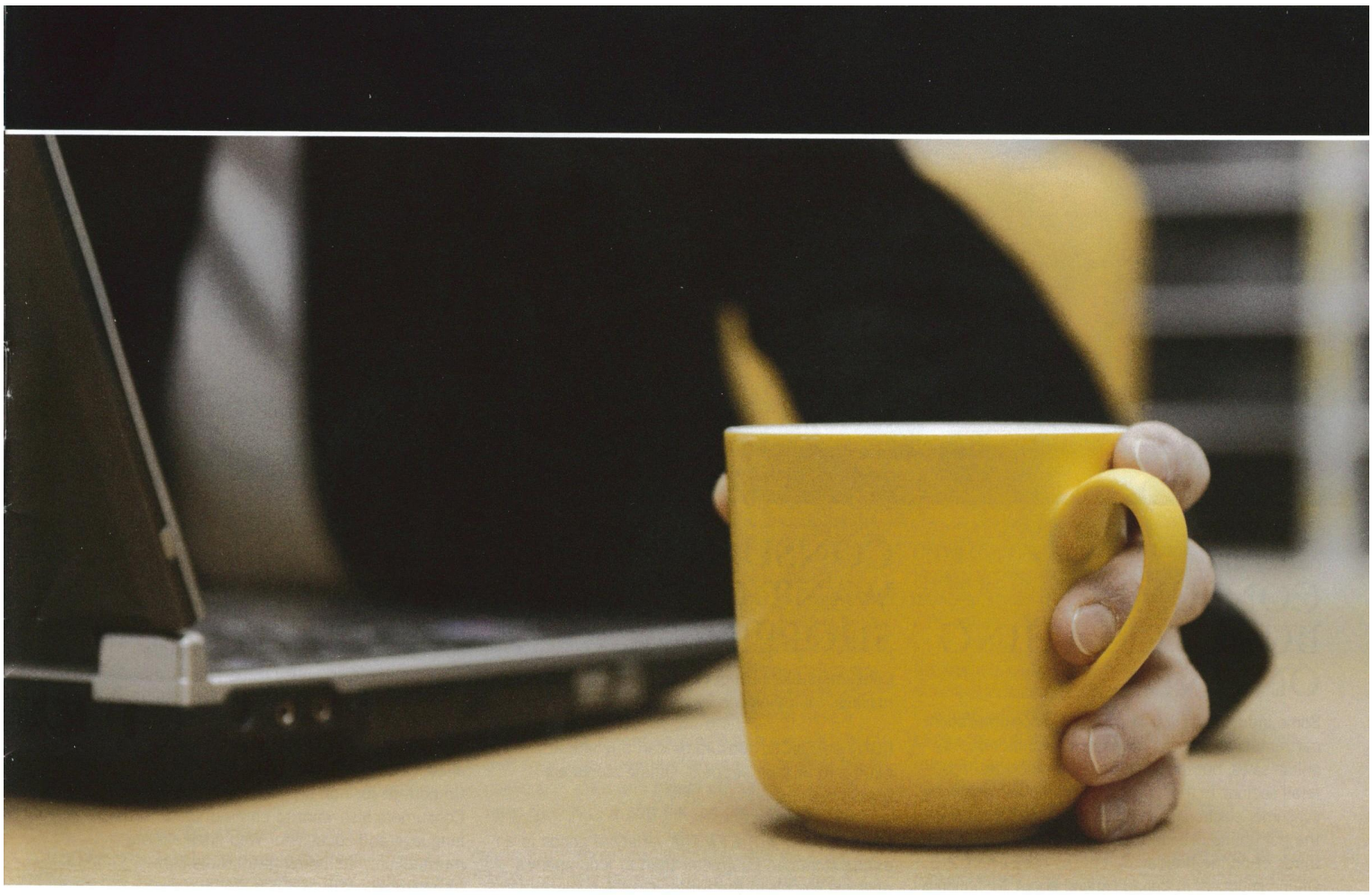
ONLINE SHOPPING GOES MAINLINE

BY IAN GORDON

Blue Nile, Inc. is an online retailer of diamonds, jewellery and watches, and has a Canadian Web site. Blue Nile was founded in 1999. The firm now receives 739,000 online visitors a month. Over the last year, Blue Nile's revenues were $194 million and net income $12 million.[1] Its market capitalization is $647 million.



CONSUMERS GO ONLINE TO BUY

Blue Nile's rapid success demonstrates that consumers are now willing to buy even expensive items online. Online has become mainline as consumers fill their virtual shopping baskets or window shop before they buy. More than 3.2 million Canadian consumers make over 21 million purchases and spend in excess of $3 billion online annually.[2] At least a further 1.7 million Canadians go online to window shop and then buy from a physical store, so a retailer's Internet presence can impact in-store sales, too.

The trend to online shopping seems to be accelerating. During the 2002 holiday season, US online consumers made 16% of their holiday purchases online. By comparison, in 2005, 27% of all spending in the holiday season was online.[3] As online shopping has grown, in-store buying has declined and is now about 68% of the total holiday spending.[4] Chart 1 provides detail.

Online shopping is here to stay. Consumers are buying online later into the holiday season, a sign of increasing comfort and trust with online shopping that is confirmed by customer satisfaction data. Consumers are becoming more satisfied with online shopping – 64% of US shoppers say they are very satisfied or somewhat satisfied with online shopping, and 6% express dissatisfaction (somewhat or very dissatisfied). In 2002, the comparable dissatisfaction level was 8%.[5]

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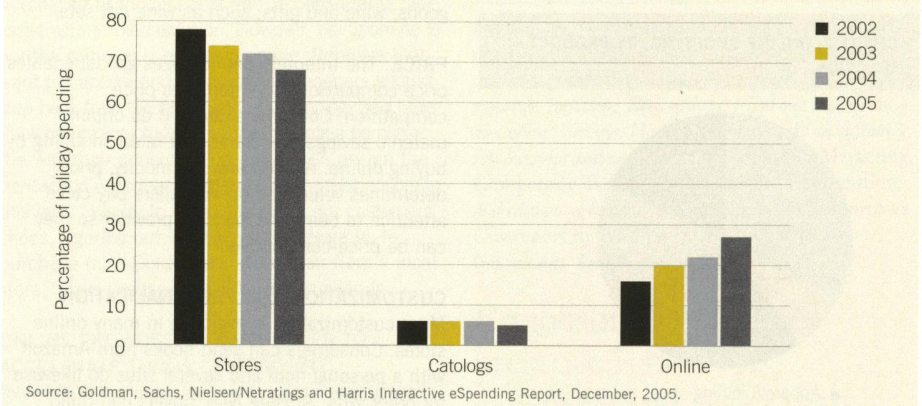
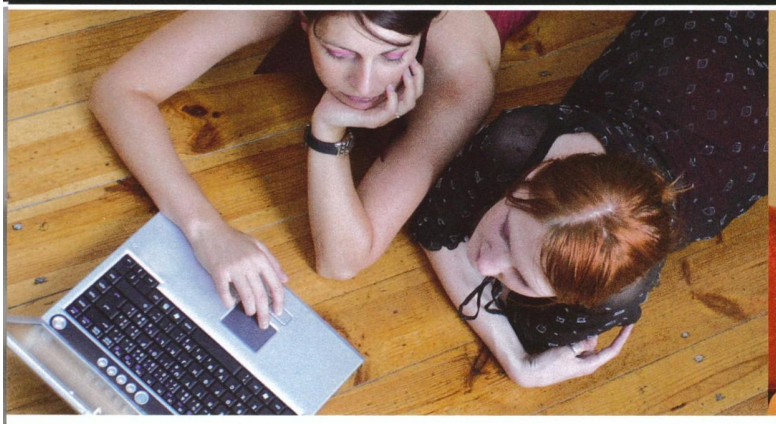
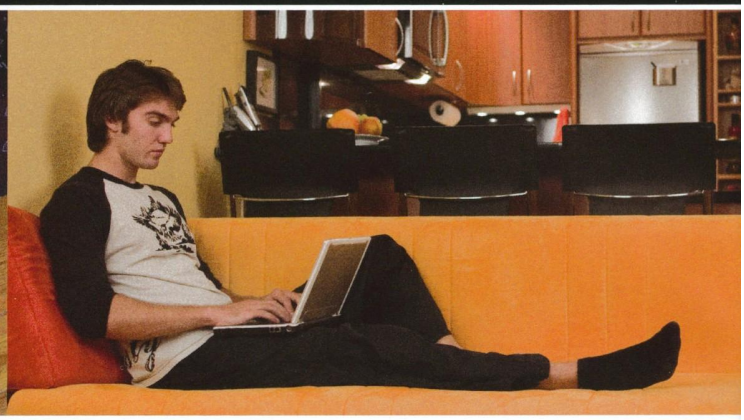
CHART 1: HOLIDAY SPENDING, BY CHANNEL



Source: Goldman, Sachs, Nielsen/Netratings and Harris Interactive eSpending Report, December, 2005.

1 All figures in US dollars. Figures are summed from the most recent 12 months of reported data.
2 2003 Household Internet Use Survey (HIUS), Statistics Canada, September 23, 2004.
3 Excludes travel.
4 US data; source: Goldman, Sachs, Nielsen/Netratings and Harris Interactive eSpending Report, December, 2005.
5 Goldman, Sachs, Nielsen/Netratings and Harris Interactive eSpending Report, December, 2005.





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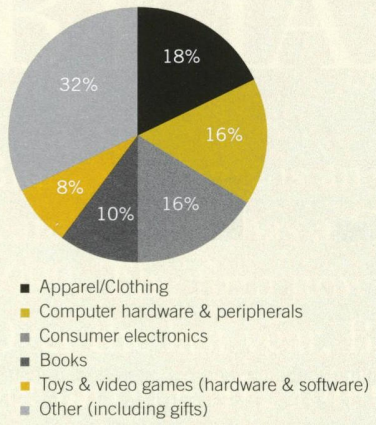
CONSUMERS BUY EVERYTHING ONLINE

Some industries, such as air travel, accommodation, car rentals and books have been revolutionized by online sales, but today online selling includes most retail sectors. In the US, apparel, computer products, consumer electronics and toys and video games are the hot online sellers, together comprising over two thirds of online holiday purchases (See Chart 2).[6] Online shoppers in Canada spend about $1 billion a year on gifts and products other than apparel, consumer products, toys and games.[7] As demonstrated by the success of companies such as Blue Nile, jewellery has also become a big seller on the Internet.[8]

CHART 2: ONLINE SHOPPING, BY PRODUCT – US, 2005



Source: Goldman, Sachs, Nielsen/Netratings and Harris Interactive eSpending Report, December, 2005.

CONSUMERS WANT ONLINE SHOPPING

Consumers like buying online for a number of reasons, including the following:

CONVENIENCE. Consumers can buy late at night and in their slippers. Online stores are always open;

CHOICE AND VARIETY. The variety of goods in an online store can be greater than in a company's physical store and the Internet collectively presents consumers with unlimited variety. Online retailers try to offer customers more goods than they expected. For example, 1-800-Flowers sells flowers online and also provides popcorn, baked goods, wine and gifts, such as wine gift sets;

PRICE. The Internet commoditizes goods, enables price comparison and intensifies price competition. Consumers can and do obtain material savings over traditional retail shopping by buying online. As with any commodity, price determines volume so online sellers pay close attention to being the low cost provider so they can be price-competitive.

CUSTOMIZATION AND PERSONALIZATION. Mass customization is available in many online stores. Consumers can send books from Amazon with a personal note and several sites do likewise for other gifts. At Blue Nile, buyers can build their own five-stone diamond ring online. At Goldspeed.com, consumers can choose from among 1,000 wedding rings. The purchase is inscribed with a personal message and shipped for delivery within a day.

EXPERIENCE. Online retailers can engineer the shopping experience and standardize it, which is not as easy to do in-store. Consumers want information presented in an uncluttered manner, quick downloads, easy check-outs and a reasonable return policy. Blue Nile is increasing the functionality of their sites rather than what they reportedly term "razzle-dazzle."[9] Other online sites demonstrate their products in use and allow close up inspection from different angles (important for non-standard or expensive items). Consumers also want to communicate in their language and successful Web sites are often multilingual, including giftbaskets.com, for example.

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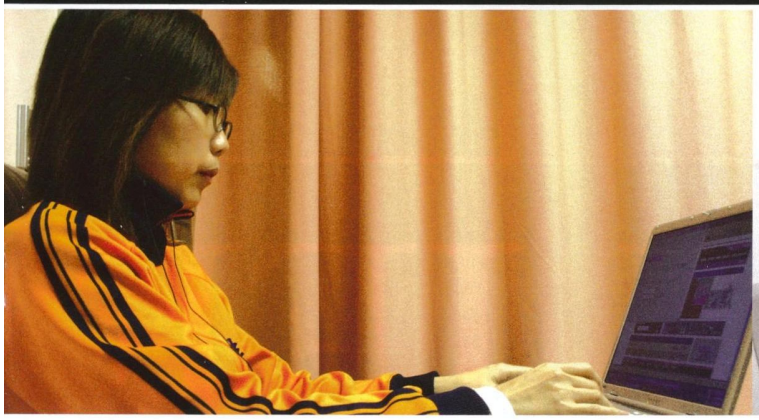
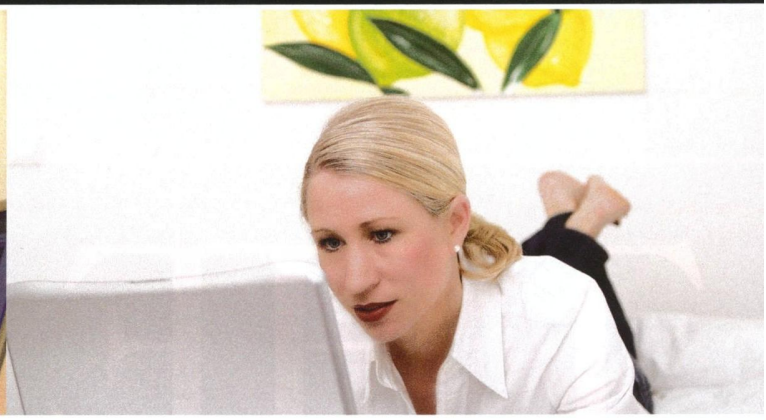
6 Goldman, Sachs, Nielsen/Netratings and Harris Interactive eSpending Report, December, 2005.
7 Assuming Canadian purchasing patterns are similar to those in the US.
8 On-line stores set sales records, Omar El Akkad, Globe and Mail, December 26, 2005.
9 Best of the Web 2006, Internet Retailer, December 2005.





IMPLICATIONS FOR GIFTWARE RETAILERS

Canadians are shopping for gifts online, so giftware retailers ought to consider whether they can be more profitable by participating in online sales of giftware in addition to their current operations. When examining the opportunity for online selling, the following should be considered:

ONLINE SALES DO AFFECT GIFTWARE RETAILERS. It used to be said that consumers will never buy giftware online because they prefer being in-store to browse and touch merchandise. This is likely still the case for many and perhaps most consumers who value their local giftware retailer, and respect the store and the products they carry. On the other hand, it is clear that some consumers are indeed being tempted to buy online by well-known retailers, less established online operations – especially those selling recognized brands, and independents with store operations that want to extend their reach. Online may not displace all in-store sales, but it may cause traditional retailers to feel they have lost some sales without being able to pinpoint readily the reasons why.

LEVER EXISTING ASSETS TO KEEP ONLINE COSTS DOWN. Over 100 years ago, department stores complemented their store operations with mail order. Eaton's printed the first mail order catalog in Canada in 1885 and operated a mail order business for 80 years. Mail order expanded Eaton's market reach and allowed them to share functions such as warehousing and distribution to benefit both in-store and mail order operations. Now Internet selling can also achieve the same benefits for retailers, allowing them to expand markets and sales by leveraging their brand and store operations.

ONLINE PROVIDES CONSUMERS WITH CHANNEL CHOICE. Consumers like choice and an online presence can actually expand in-store sales, something that department stores and others have already found out. Multi-channel operations – those with both "clicks and bricks" retailing – sell more than a retailer would with only an online presence or only a physical store. Companies that have a physical store before opening a web presence find that they have lower marketing costs, higher buyer conversion rates and higher customer retention rates than if they only had an online store.[10]

IT IS EASY TO GO ONLINE, BUT NOT AS EASY TO SUCCEED THERE. Establishing an online presence is now less expensive and easier than it used to be, so a company can readily begin to sell products online. Well-featured software that includes credit card connectivity and shopping basket features can be purchased at modest cost and IT consultants can assist with implementation. However, being online is not the same as succeeding online. Retailers that want to capture and retain online shoppers should step back from the time traps of technology and other implementation challenges, see the online purchase the way their consumers do, and then design the transaction experience and the ongoing relationship to this end. "We try to put ourselves in our customers' shoes, figuring out what would motivate us to purchase from Goldspeed rather than from a local store," says Goldspeed CEO, Neil Kugelman.[11]

ONLINE PROVIDES OPPORTUNITIES TO ACCELERATE TURNS OF OBSOLETE INVENTORY. Online selling can aid the disposal of end of life, slow moving or obsolete inventories, and product where only a few items remain for sale. Some retailers also set up partnerships with niche suppliers to market lower volume items online than they would carry in their stores.

Online shopping is growing in importance and impacting traditional stores, including giftware retailers. There are hundreds of companies selling gifts online.[12] Some well regarded giftware Web sites include Amazon.com, BlueNile.com, GiftBaskets.com, Gifts.com, Goldspeed.com, Illuminations.com, PersonalCreations.com, and VermontTeddyBear.com. Other sites, such as eBay.com are also indirect competitors. Retailers that reject being online will be affected by those retailers that are online. The online opportunity may well be there but it is different than traditional retailing and this alone might cause some retailers to consider online as a poor fit. For these retailers, the choice is stark. Will they allow the mass merchants' and chain stores' online operations to further erode the independents' in-store giftware sales? Or will they instead reach out online for new sales and customers? ■

Ian Gordon is a management consultant who conducts strategy, marketing and sales planning assignments, customer relationship and loyalty projects and market research, including focus groups, telephone interviews and online surveys. He has authored books on customer relationships and competition: Relationship Marketing, Competitor Targeting *and* Beat the Competition, *and editions of Ernst & Young's publication* Tomorrow's Customers in Canada.

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10 Shop.org data as presented in Retail Power, Lawrence Stevenson, Joseph Shlesinger and Michael Pearce, McGraw Hill, 1999, pp. 215-218.

11 Best of the Web 2006, Internet Retailer, December 2005.

12 Top 400 Guide, Internet Retailer, 2005 Edition.