BCG
OPPORTUNITIES *for* ACTION

CONSUMER

■ *Once the choice of only a few players, multichannel retailing is fast becoming a competitive requirement and a rare opportunity to increase revenues and profits in today's crowded markets*

■ *According to recent data, consumers who shop in more than one channel can be three to five times more profitable than single-channel shoppers*

■ *To create a multichannel advantage, retailers must provide a seamless shopping, purchase, delivery, and service experience, whether through a store, a catalog, a Web site, a call center, a television network, or direct mail*

■ *Besides* big *investments in technology integration, retailers should make* smart *investments in activity coordination and organizational incentive alignment—shifting from a profit-and-loss focus on channels to a cross-channel focus on high-value customers*

The Multichannel Imperative

Once an option chosen by only a handful of businesses, multichannel retailing has become a market imperative that retailers are striving to implement as fast as they can. And no wonder. From 2002 to 2007, annual sales growth for the U.S. retail market hovered at around 5 percent, whereas sales for multichannel retailers grew 8 percent per year. Over the same period, annual shareholder returns for the S&P 500 averaged 8 percent, compared with 15 percent for multichannel retailers.

Retailers that satisfy consumer expectations when it comes to multichannel shopping—and that encourage their own customers to shop across channels—have much to gain. Consumers who shop in two channels are, on average, three times as profitable as single-channel shoppers, and those who shop in three channels are more than five times as profitable. But creating a multichannel advantage is not just about selling online. Consumers expect a seamless experience when they shop, purchase, receive deliveries, and request after-sale service—whether through a store, a catalog, a Web site, a mobile Web site, a call center, a television shopping channel, or direct mail.

That's asking a lot. Yet retailers often overestimate the challenge. Instead of focusing only on *big* investments in large-scale technology integration, they should also be looking at smaller but *smart* investments geared toward targeting high-value consumers, coordinating activities, aligning organizational incentives, and delivering smooth execution at all touch points. Such investments will result in better customer service and a larger share of profitable customers' wallets, as well as lower costs and reduced complexity in serving customers.

The Case for a Multichannel Strategy

For many retailers, a multichannel strategy is one of the few opportunities for growth in an environment characterized by tougher competition and a limited ability to continue to grow by adding more stores. Consider the example of Tesco, the U.K.-based international grocery and merchandising chain. From its beginnings as a chain of grocery stores, Tesco has expanded into several formats—Extra, Metro, and Express—

as well as into online and catalog channels. Each channel and format is positioned for a different shopping occasion and serves different needs in terms of convenience, assortment, "touch and feel," promotions, and price points. This variety of channels and formats has allowed Tesco to capture a greater share of purchase occasions for its traditional categories and to expand into clothing, consumer electronics, financial services, furniture, music downloads, and even travel—products and services that could not be offered as effectively through the company's brick-and-mortar stores. Tesco maintained an annual growth rate of 10 percent in its core U.K. market from 2002 to 2007, compared with only 3 percent for all U.K. retailers combined. The annual growth rate of its online businesses (some of which are outside the United Kingdom) was approximately 29 percent over the same period.

Demand for multichannel shopping continues to grow. The numbers reported by another large U.K. retailer are typical: telephone and Internet orders for products that customers picked up in-store increased from 7 percent of sales in 2004 to 13 percent three years later, and Internet orders delivered to customers' homes doubled, from 4 percent to 8 percent. U.S. retailers, too, are taking full advantage of the trend. Neiman Marcus uses its catalog and Web site to showcase new designers and offer virtual trunk shows, and J. Crew leverages its site to test new categories, such as wedding dresses, jewelry, its Crewcuts line of children's clothing, and the upmarket J. Crew Collection. The increasing number of consumers who are researching and purchasing products across channels are turning out to be today's biggest and most profitable spenders. Compared with single-channel consumers, they tend to be more loyal, more inclined to purchase in more product categories, and more likely to spend a greater share of their wallets.

Indeed, selling through multiple channels and formats is one of the few ways to increase both sales *and* profits. Because retailers tend to focus more on revenues than on costs, they may not realize that multichannel customers often cost less to serve than single-channel customers because back-end processes in purchasing and inventory management can be shared. Multichannel capabilities do require some initial investment, but companies can achieve a scale advantage by targeting high-value customers and meeting their expectations.

The Challenges for Retailers

Retailers that are accustomed to traditional business models and unfamiliar with multichannel processes often make the mistake of simply transferring old ways of operating into the new environment. Many treat each individual channel as if it were an independent silo in competition with other channels for the same customers, and therefore fail to capture scale economies across channels. In a series of in-depth interviews conducted by The Boston Consulting Group with leading multichannel retailers, more than half of the respondents revealed that their inventory and order-management systems weren't integrated across channels. More than a third said that merchandising was organized by channel rather than by category. And the same number reported that customer data weren't shared because the company's dominant channels tended to fear cannibalization of sales by the other channels.

Retailers that want to optimize their multichannel processes should also beware of overpromising. The risks of not delivering on expectations are high: dissatisfaction in one channel can damage the overall customer relationship. In a survey we conducted with multichannel consumers, one respondent noted that a well-known European retailer refused to take catalog returns in the store, so she gave up on the company and switched her business to a competitor.

To be sure, consumers who move from one channel to another without even thinking about it assume that they won't hit any bumps. When consumers were asked last year to rank the services that they expected from multichannel retailers, they put notification of order status and shipping delays, as well as the ability to cancel or modify an order and track its status in any channel, at the top of their lists. (See the exhibit "Consumers Have High Expectations for Service Across All Channels.") Consumers also expected stores to be able to specially order products and find out-of-stock items at other locations, to accept returned products (including those purchased online) at any location, and to help them research prices. They even expected customized services, such as notification of when their favorite products went on sale—and in the channel or channels of their choice.

Some retailers are meeting these challenges, and more and more consumers are voting with their feet (or clicks)—shifting their allegiance to competitors that are getting it right. Therefore, in addition to realizing a larger share of their existing customers' wallets, retailers that make multichannel shopping easy and attractive can win profitable new customers away from rivals unable to satisfy consumers' multichannel needs. And that amounts to a huge competitive advantage, because the more channels consumers can shop in, the more profitable they tend to be—a good reason to measure their relative value and shopping patterns by and across channels.

Creating a Multichannel Advantage One Step at a Time

The good news is that the difficulties involved in achieving a multichannel advantage are often exaggerated. There's no need for a retailer to wait until its systems and technology are state-of-the-art before launching a new format or channel. Taking a few basic steps toward channel integration (which nearly all retailers are capable of) can produce a multitude of benefits for consumers and retailers alike. At the same time, retailers can test new approaches and learn from their customers' reactions. They can improve their offering while minimizing the risks associated with start-up investments. Here's how.

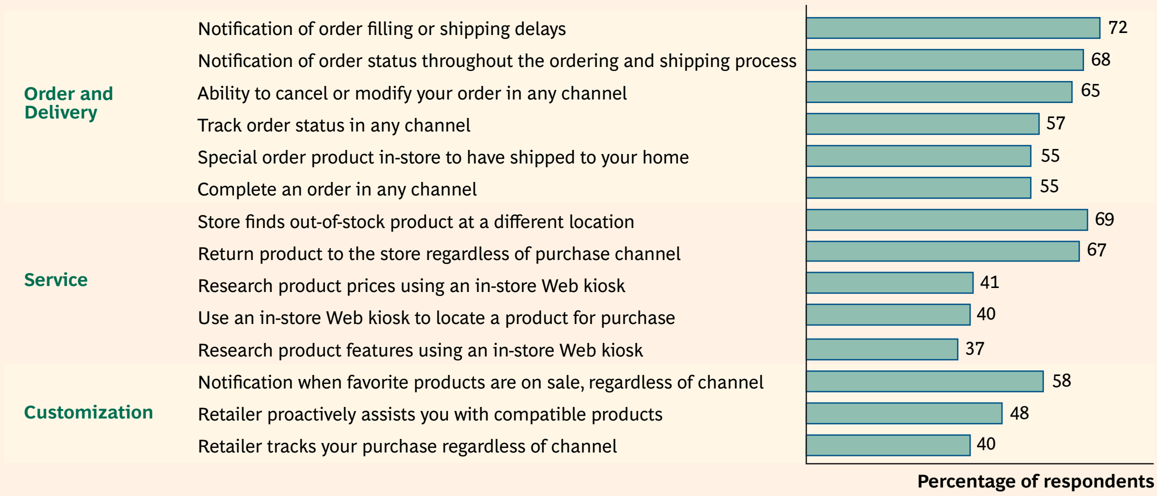
Begin to think in terms of consumers rather than technology, searching out the most valuable ones and paying close attention to how they shop. This requires going beyond compiling credit-card data to understanding how consumers behave in various categories and across retailers. It also calls for tracking your customers—and those of your competitors—across channels. Rather than viewing the different channels as independent silos or standalone businesses, treat them as integral components in a new business model whose goal is to create long-lasting relationships with your most profitable customers.

Know what each channel is best suited for—at every point in your go-to-market value chain as well as in the customer's purchasing experience. Although it is important to know how consumers use—and expect to use—all the shopping channels available to them, that doesn't mean that every channel needs to be all things to all people. Some channels are better for educating consumers about products, offering promotions, or allowing consumers to experience products firsthand. Others are best for cross-selling, up-selling, or encouraging loyalty. Still others are especially good for managing after-sale support services, answering questions, and nurturing online consumer communities.

Consider Fnac, France's largest retailer of music, books, and consumer electronics, which sells through several channels: urban shops, suburban stores, a Web site, and a mobile Web site. Customers can go online to check for in-store availability of specific products, receive assistance in the use of equipment, and learn about exclusive promotions and "flash" sales. Every channel has a differentiated offering, but all are integrated through a common loyalty program, shared customer-relationship management tools, and a single ordering, tracking, and delivery system. For example, Fnac offers an assortment of mobile phones, LCD high-definition televisions, and

Consumers Have High Expectations for Service Across All Channels

What do you expect from a multichannel retailer?



Source: Sterling Commerce/Deloitte, "What Consumers Want in Their Shopping Experience," August 2007, based on a survey of 5,003 U.S. consumers.

compact digital cameras both online and in its stores, but some products in each category are available exclusively online, and some are offered at a discount either at the store or online. This differentiated assortment and pricing between the company's stores and its Web site has enabled Fnac to post the same prices for individual items online and offline, and at the same time offer attractive online discounts for bundled products. It also allows the company to manage product assortment and pricing throughout a product's life cycle.

Determine which functions to provide in each channel and align costs with consumers' expectations. Most retailers evolve from running their channels as separate operations, to partially integrating them in a few functional areas, to coordinating activities—including branding, promotions, inventory forecasting, product returns, and product assortment and positioning—across all channels. The ultimate goal is to develop tailored offerings in every channel, as Tesco has done by varying its product assortment across formats and channels and also by creating in-store promotions that bring shoppers to Tesco.com in order to purchase additional services.

Not every company should pursue the same approach to multichannel integration. But our experience in working with some of the best multichannel retailers has convinced us that any approach must involve an organizationwide effort to upgrade not only metrics but also reporting relationships, incentives, and personnel. We offer the following checklist for companies that are considering a multichannel investment or that want to measure their progress to date.

- Are we building our multichannel capability incrementally in order to earn credibility for future investments?
- Are we careful not to disappoint customers by overpromising on capabilities that we can't deliver?
- Does each of our channels excel at what it does best?
- Are we clear about how consumers use our channels and for what occasions?
- Do we understand the cost of providing the same customer with the same product in each one of our channels?
- Can we justify to consumers any inconsistencies in our offerings and pricing across channels?
- Do we test the smoothness of our multichannel integration by putting ourselves in the customer's place?
- Are we actively recruiting multichannel customers? (Persuading a customer in one channel to try another is often easier than going after entirely new customers.)
- Have we provided organizational incentives to actively enable and promote cross-channel shopping, as opposed to maximizing an individual channel's sales?
- Do we share customer data across channels in order to gain a full understanding of shopping behavior and opportunities?

Shifting the organization from a profit-and-loss focus on channels to a cross-channel focus on customers is not an easy task, but the payback in profitable customer relationships is worth the effort. You'll earn more repeat sales because customers will know more about your products and brands—and you will lower your costs through process and resource sharing. The imperative is clear and so is the mandate: create a multichannel advantage by investing your dollars strategically to increase the spending of your most profitable customers across all of your channels.

Brad Loftus
John Mulliken
Jonathan Sharp

Brad Loftus is a partner and managing director in the Washington office of The Boston Consulting Group. John Mulliken is a principal in the firm's Boston office. Jonathan Sharp is a principal in BCG's London office.

You may contact the authors by e-mail at:
loftus.brad@bcg.com
mulliken.john@bcg.com
sharp.jonathan@bcg.com

To receive future publications in electronic form about this topic or others, please visit our subscription Web site at www.bcg.com/subscribe.