Supply chain not shop front key to winning online

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John Winner ‘s Winning Group fortunately had a distribution and supply network before it began online sales. **Photo: Nic Walker**

Simon Evans

Heavy investments in glittering websites with dazzling branding and attractive price discounts are being made by a flood of online retailers, as they attempt to steal a bigger share of the $225 billion spent by Australian consumers in the retail sector each year.

But the headlong rush for new customers through keen pricing, an advertising and marketing blitz and new technology has some eerie similarities with the dotcom boom of 1999, which had popped so spectacularly by 2001.

“Everyone’s drinking the Kool-Aid a bit too liberally, but you’ve also got to think about retention,” said Paul Greenberg, a co-founder of the DealsDirect Group in 2004 and one of the pioneers of Australia’s online retailing industry. “The battleground has shifted to the supply chain,” he says.

The large distances between Australia’s capital cities means the online game is being won and lost in how well the supply chain is working, and whether customers return for more.

Costs – a large portion of which stems from expensive IT systems and warehousing, and the actual deliveries of goods to people’s homes once they’ve been ordered online – are stubbornly high, and the new revenues coming in may not be increasing as fast as they need to.

A raft of online businesses are aggressively backing their strategy, none more so than fashion group The Iconic, a figurehead for the new breed. Investors ploughed a further $28 million into the business late last week.

Online retail sales still only represent about 6 per cent of the total amount being spent in the retail sector across Australia, and while that number is growing, it’s a race against time for the new online players to try and accelerate revenues ahead of costs and prove they have a sustainable business model.

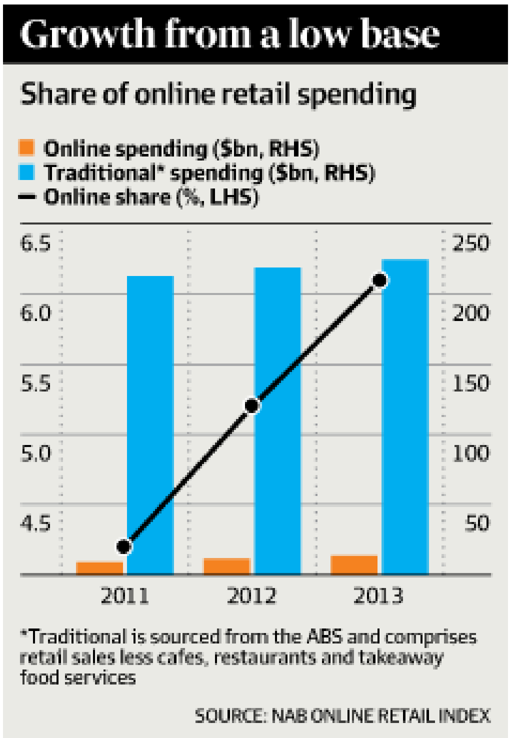
However, the excesses of those heady days 14 years ago aren’t being repeated to quite the same extent because of a new financial conservatism at play since the global financial crisis in 2008. There’s simply less risky capital around.

Fickle customers prove problematic

But there are still substantial sums of money being burnt as new retailers try to elbow out traditional bricks and mortar players. However, keeping increasingly fickle customers is proving problematic, with one mis-step enough to cause a rapid exit into the arms of a new competitor.

Greenberg says while there is an enormous rush on to win new customers it is “getting the end mile right” that is absolutely crucial in retaining those new customers.

Greenberg is now chief executive of the newly formed National Online Retailers Association. But he made his name as a co-founder of the DealsDirect Group, which in 2011 attracted a high-profile investor in billionaire James Packer via the Ellerston Capital funds management arm, owned by the Packer family’s Consolidated Press Holdings.



“For some of the new retailers it’s all about growing the revenues, but unfortunately some of the costs have been going up with it.”

The “jaws” (simple graphs comparing revenue and costs which are closely tracked by company accountants) may not be getting wider, and may in fact be closing up.

In the past few weeks, online fashion retailer The Iconic has been in the spotlight as it went through a painful period, cutting staff after substantial initial investments as it made a big splash in the Australian fashion retailing sector.

The Iconic is a business that is part of a stable of online retailing businesses backed by German group Rocket Internet and has suffered heavy losses since it began in Australia in late 2011.

Last week, The Iconic announced that it had raised a further $28 million in funds as overseas investors including Belgian firm Verlinvest pumped extra funds in. The Iconic managing director Adam Jacobs says the additional funding was part of a planned strategic approach: “It’s us focusing on long-term growth.” He dismissed speculation the group was either aggressively pursuing revenue growth in order to position the business for a sale, or running out of cash. The Iconic claims to be Australia’s No.1 online fashion retailer.

Keep online retail in context

It’s also important to keep online retail in context. The National Australia Bank closely tracks online sales and for the 12 months to May 31, 2013, estimates Australians spent $13.7 billion with online retailers. This represents about 6.1 per cent of total spending in the overall retail sector of $225 billion, a figure which doesn’t include money spent in cafes, restaurants and on takeaway food.

In the 12 months to May 31, 2012, $11.3 billion was spent in the online retailing sector, which represented 5.2 per cent of the total. In the 12 months to May 31, 2011 it was $9 billion, which made up 4.2 per cent of the total.

John Winning, the chief executive officer of the Winning Group, which sells ovens, dishwashers, cooktops, washing machines and televisions, is having a bet each way.

The company has nine retail showrooms, including a new flagship store in the Sydney suburb of Redfern but also a large online business trading under the names Appliances Online, Big Brown Box and PowerBuys.

The Winning Group has more than 350,000 customers, and prides itself on a seamless experience for customers that ensures repeat business and plenty of word of mouth endorsement.

He is bemused at the heavy investment being made by some online retailers, and the prospect that some of those business models may not be sustainable. “At some point when the tide goes out, the ones that are not profitable won’t be there,” Winning says.

He expects real consolidation over the next three to five years.

He says the most important element for business success is a high-quality, efficient distribution and delivery network that ensures customers are always happy.

“It’s the biggest plus.”

Winning Group’s family legacy

Winning Appliances is a somewhat unique business because it had a substantial distribution and delivery network in place first, prior to setting up retail showrooms. This was a legacy of Winning’s family holding the distribution rights for Simpson whitegoods decades earlier, which they subsequently lost.

“They ended with a warehouse and distribution system but nothing to deliver,” he says. That existing infrastructure became the basis of Winning Appliances’ superior distribution system. “We had a logistics business that happened to sell appliances.”

Winning says one of the big advantages is that he has ownership of the delivery business, which has 70-plus trucks operating from seven warehouses in Sydney, Melbourne, Brisbane, Perth, Adelaide and a two-person crew in each vehicle to ensure customers are content, and their big-ticket item purchases are installed and working correctly.

Winning estimates warehousing and delivery represents around 50 per cent of his total costs.

But it is proving a godsend, in driving sales growth of more than 50 per cent in the past year from the online businesses, on top of 100 per cent sales growth in each of the previous four years.

Greenberg says the Winning Group is an example of the success that can be derived from a retail business operating from multiple channels, and that many shoppers like having the choice of how they interact.

“Customers want multiple access points to a brand,” Greenberg says.

Greenberg, who came to Australia in the mid-1990s from South Africa and set up a business selling guitars on eBay to the rest of the world before setting up DealsDirect, says a poor experience with delivery and logistics can wreck the online buying experience for a customer. “It’s got to be seamless and frictionless. There’s all the belts and braces, and the ball can get dropped in the delivery piece.”

Australia Post core pillar of new retail

He says the importance of Australia Post in the growth of online retailing in Australia can’t be understated and “they are a core pillar of the new retail.”

The Iconic’s Jacobs says substantial investment in distribution and delivery has been one of the main factors in driving growth. He says The Iconic has 4 million visitors per month to its site, but he declines to detail how many are making purchases.

The delivery options, which includes a three-hour delivery service in Sydney, are appealing to customers and essential in increasing the “re-purchase rate”’. This is the measure of repeat business, and Jacobs says it’s tracking well. “That’s the real key to being a sustainable business,” he says.

He won’t comment on when The Iconic expects to be profitable but does say it will be faster than the average seven years it takes for a start-up online business.

The Iconic uses Australia Post for deliveries in Australia, and for the three-hour Sydney deliveries it uses the “Want It Now” brand operated by a firm called Mail Call. It uses DHL Express for deliveries to New Zealand.

Jacobs say Australia Post is an important component. “We’ve had a lot of success with Australia Post.”

Richard Umbers, executive general manager Parcel & Express Services at Australia Post, acknowledges that his business has an important role to play in the overall success of online retailing in Australia. “We have been investing heavily in our business and we are spending $1.2 billion on our network, to provide the infrastructure required by our new customer base,” he says.

Umbers says around 70 per cent of parcels delivered by Australia Post originate from an online transaction.

Parcel volumes are experiencing double-digit growth and this has been the case for the past three years.

Parcels revenue larger than letters’

The revenue from parcels is now larger than the letters business.

Australia Post moved to full ownership of parcel delivery business Star Track Express last year by buying out Qantas’s 50 per cent stake for $408 million as part of a strategy of beefing up its parcels business.

Crackawines.com.au, the No.2 player in Australia’s online wine retailing market, is using Australia Post for its deliveries, largely because of the sheer size of its geographic reach. In its infancy, Cracka’s growth was curtailed because of logistics issues.

“There’s very few people who have the reach of Australia Post,” says Dean Taylor, the chief executive and co-founder of Cracka.

He says global giants like Amazon and the Book Depository have set high benchmarks for how fast an item can be delivered, and customers in Australia can’t understand why, if an item is being sourced from an Australian warehouse or business, it can’t be delivered faster than from overseas.

Taylor says Cracka, established in October, 2010, is still in an investment phase and building its scale.

“We’re very close to profitability,” he says. “We’re still re-investing. For us it’s getting it to the scale that we want to be,” he says.

Lower pricing than a bricks and mortar retailer is important in attracting customers.

“People expect that by buying online they’re actually going to save money.”

Constant downward pressure

There is constant downward pressure being brought on the margins of shop retailers and “the internet is starting to break them down”.

But it’s in the delivery where customers become loyal, or a business runs the risk of them switching to a rival and never returning.

“The beauty of online is when a customer thinks you’re great and they’re incredibly loyal so they tell their friends.

“But the moment you let them down they will do the opposite,” Taylor says.

He says online businesses need to be making substantial investment in IT systems, warehousing and infrastructure and constantly improving them, and these are costs that customers are oblivious to, unlike when they walk into a retail shop.

“We do need to continue to invest in things the customer can’t really see.”

It’s not just in fashion and wine where there is hot competition between online retailers and the traditionalists. Paws for Life is trying to muscle in on the $8 billion pet care sector, with a specific focus on selling pet food online.

Michael Frizell, the founder and chief executive of Paws for Life, established the company in 2011. He says between 10-20 per cent of total revenues go into warehousing and logistics. “It’s our second largest cost behind labour,” he says.

Paws for Life now has more than 20,000 customers and claims its prices are on average 20 per cent cheaper traditional shops. “We’re still in investment phase,” Frizell says.

It is currently seeking an extra capital injection of between $4 million to $5 million to expand its operations, and with that additional investment on building additional scale and taking on more employees, it will be another 18 months before it hits its projections of being profitable.

Paws for Life uses a firm called Couriers Please for the vast majority of its metropolitan deliveries, and Australia Post for its deliveries in rural areas.

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