The impact of electronic commerce on the retail industry

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Over the past few years, many businesses including retail organisations have identified the need to conduct business electronically. Electronic commerce can take different forms including Business-to-Business (B2B), Business-to-Consumer (B2C), Business-to-Business to-Consumer (B2B2C), and Consumer-to Business (C2B) transactions.

B2B electronic commerce refers to commercial transactions involving two or more organisation, for instance between Tesco and its suppliers.

B2C transactions occur between an organisation and its customers. The transaction between an individual purchasing an item from eBay constitutes an example of B2C.

Turban et al, suggested B2B2C e-commerce takes place when an organisation provides another client organisation with a product or service which the client organisation transfers to its own customers without adding value to it. An example of this type of e-commerce transaction can be university of Aberdeen providing its student with e-mail services through Windows Live. In this case students are the customers of Aberdeen University which is in turn a client to Microsoft.

Finally, C2B e-commerce refers to " individuals who use the internet to sell to organisations as well as individuals who seek sellers to bid on products and services they need (e. g. Priceline. com)"[2]

According to a research conducted by Nikolaeva, R. (2006), the adoption of e-commerce in the retail sector was driven by organisational readiness and external influences for the majority of retailers. These results are in contradiction with the view from economic theory and most empirical studies which suggest that the adoption of e-commerce is mostly driven by its perceived economic value[3].

The development of E-commerce in the retail sector can be divided into two phases. The first phase was characterised by the belief of first mover advantage. Organisations which went online were the ones with considerable resources[4]. During this first phase of e-commerce, organisations were more focused on market share, number of visitors to a website and gross revenues and expecting that in the long term, these would result in extremely high levels of profits[5]. Experts predicted that e-commerce was going to create a ‘ frictionless commerce’ due to factors such as ‘ disintermediation’ and the elimination of unfair competition[6].

Nevertheless, this first phase of e-commerce saw a lot of online retailers going bankrupt and some of the traditional retailers which went online not being able to perform as well as they did in their normal brick and mortar setting. Example of E-commerce failures can be seen in the light of companies like eToys, Useem 2000, Perkins and Perkins 2001. This failure phenomenon has led many economists and business experts doubt the viability of e-commerce and even predict its collapse.

On the other hand, e-commerce has also seen some successes like eBay and today, as it is well known, millions of consumers purchase products of their favourite brands from home, using the internet at their convenience and this has resulted in a significant growth in e-commerce revenues. According to a survey of UK SMEs conducted by Actinic (UK e-commerce software specialist) in July 2010, there has been a 15% increase in e-commerce revenues over the period of April to June as compared to the same period in 2009. Also, more and more businesses including SMEs are present on the internet, in order to make their offerings accessible to a large number of people.

3- E-Commerce and changes in industry structures

The advent of the internet has prompted the development of new types of businesses and consequently the proliferation of new business models and this has affected industry structures. A lot of organisations today can operate without necessarily having a physical location and hence, have a completely different way of conducting their activities in relation to traditional businesses. For example, ‘ Pure clicks’ in the light of Amazon, eBay, and CDNow operate differently from ‘ brick and click’ organisations like Marks and Spencer, Tesco, Next and others.

According to Hamel and Sampler (1998), the traditional retail business model which is a location-centric model is shifting to a web-centric model, giving rise to higher levels of customer expectations in terms of speed, comparability, and price[7]. E-commerce business models are different from traditional business models because e-commerce offers firms different market opportunities and changes organisations’ revenue models, competitive environments and advantages, which are core elements of a business model.[8]With the internet, consumers have access to a wider range of choices. They can research products extensively before making the actual purchase. Internet also facilitates product or service comparison by providing detailed information at almost no cost to Consumers and thus reducing customer’s search cost. ‘ Pure click’ organisations like Amazon have capitalised on the consumers’ need for information to expand their business by providing consumers with a tool to compare a multitude of products. This type of business has been referred to by Evans and Wurster (1999) as the business of ‘ pure navigation’. Also, ‘ Pure clicks’ often allow individuals and organisations to compete directly with them on the same product offerings. Amazon for instance allows individuals to sell the same book it sells on its own webspace. In a traditional business setting, it would have been absurd for an organisation to sell products on behalf of its competitors.

E-commerce has also prompted an era of mergers, acquisitions and collaborations between organisations that traditionally were competing against each other. Most organisations have identified the need to collaborate with their competitors in order to achieve operational effectiveness and stay in competition with ‘ pure clicks’. An example of this collaboration can be that between Universal and BMG, two giants of the music industry. These two companies got together to create getmusic. com which is an electronic joint venture to sell music.[9]

Traditional ‘ brick and mortar’ organisations have also recognised the threat of ‘ pure clicks’ and in response have adopted a mixed strategy which combines both physical outlets and online presence. This new type of organisation is what some authors refer to as ‘ brick and click’ organisations. In contrast to ‘ brick and mortar’ organisations which are horizontally integrated, ‘ brick and click’ organisations are rather vertically oriented. The Horizontal and vertical integration in this context are in relation to distribution channels. Traditional brick and click retailers by selling their products through many distributors are horizontally integrated and brick and clicks like Marks and Spencer by selling directly to their consumers are vertically integrated (see fig1 below).

Fig1. Horizontal and Vertical integration of distribution

Organisation Organisation

Distributor1 Distributor2 Distributor3 Retail Stores and Website

Consumer A Consumer B Consumer C Consumers

Horizontal Integration Vertical Integration

Porter (2001), used his five forces that determine an industry’s attractiveness (bargaining power of suppliers, bargaining power of buyers, barriers to entry, availability of substitute products and inter-firm rivalry) to analyse the effect of e-commerce on industry structure, and drew the following conclusions. E-commerce by allowing consumers access to information has increased their bargaining power. It has also increased inter-firm rivalry by making the world a global village and thus increasing the threats of substitute products. There is also a lower barrier to entry in terms of access to channels and physical assets. As for the bargaining power of suppliers, it could be said to be high as suppliers have access to more customers. Nevertheless, the other side of the coin is that, as suppliers have access to more customers it creates a situation where all suppliers have equal access to the same customers and that reduces the bargaining power of the suppliers and shifts it to the buying organisations.

From Porter’s point of view, the ‘ new’ industry structures make some industries unattractive because of the fact that the internet also makes it more difficult for companies to translate internet benefits – easier and faster business transactions – into profit. Nevertheless, Porter also argues that industry structure is fluid and is determined by the decisions taken by competitors.

4- E-commerce and Strategy

Strategy has been described by Chaffey, D. (2007) as “ the definition of the future direction and actions of a company defined as approaches to achieve specific objectives”. With the advent of e-commerce and the changes it has brought to industry structures and competitive advantage, a lot of questions have been raised by researchers and businesses on the best strategy to adopt to face the ‘ new’.

This part of the paper is presenting and comparing three different views on strategy in the era of e-commerce.

4-1 Evans and Wruster’s position

The first view is that of Philip Evans and Thomas S. Wurster in their article ‘ getting real about virtual commerce’, the second view is that of Michael Porter in ‘ Strategy and the internet’ and the final view, that of Don Tapscott in ‘ Strategy in a networked world’.

Evans, P. and Wurster, T. S., (1999) suggested that in the next generation of e-commerce, organisations in order to be competitive would need to become navigation businesses and compete on three levels which are: reach, affiliation and richness.

Traditional ‘ brick and mortar’ retail organisations have always been competing on reach by locating their stores at convenient places for easy customer access. Today, the internet has rendered physical presence limited in reach. This is because on average, physical stores and warehouses cannot be as accessible to consumers as e-stores which are just a click away from their computers. In order to be competitive today, retailers will have to be present on the internet, so as to reach a larger group of individuals. Retailers also have to make sure their websites are user friendly and provide all the necessary information consumers need.

Competing on affiliation implies that successful organisations will be those which will demonstrate to have consumers' best interest at heart instead of their own. An example of such organisations can be confused. com which offers customers the possibility to compare insurance policies. What makes it possible for confused. com to be more empathetic towards consumers is the fact that no matter the insurance company the consumer buys from, confused. com will get its commissions so far as the policy was purchased though its website. A lot of consumers purchase products through such organisations because they believe they can always get the best and cheapest deal. Evans and Wurster nevertheless recognise a problem for pure navigators when competing on affiliation. That is, pure navigators are at a disadvantage when the comparison of a product requires more sophisticated selection criteria which need product information richness. Product information richness refers to detailed information on product features, specification, performance that usually only manufacturers are knowledgeable about.

Richness refers to both the depth of information organisations can have about their customers and the amount of information those organisations can make available to their customers. According to Evans and Wruster, when competing on richness, traditional retail organisations are at an advantage over pure navigators because they have better consumer information and logistics.

4-2 Michael Porter's position

In contrast to Evans and Wruster's view, Porter suggests that, organisations in order to compete effectively in the era of e-commerce will have to use the internet as a complement rather than using it to replace conventional ways of doing business. Organisations will have to compete by defining unique selling propositions targeted at profitability instead of mere growth. Porter describes that internet as just an ‘ enabling’ technology that can be used as part of any strategy. He argues that the internet rather enhances the importance of strategy in an organisation’s success. This is because the use of the internet for most organisations has been at the detriment of their economic value through discounted prices and the likes and the only way to redress economic value is to design and use strategies that proved to be successful. According to Porter, the internet has been detrimental to organisations’ economic value because a lot of organisations have failed to see the internet as a mean to an end and rather treat it as an end in itself.

Finally Porter suggests that, in the era of e-commerce, organisations need to differentiate themselves from the lot by ‘ achieving a sustainable competitive advantage’ through operating at a lower cost than their competitors and/or by commanding a premium price. To date, the internet is the most effective tool to achieve operational effectiveness because it offers organisations the possibility to perform at faster rates. But at the same time, the internet also makes it difficult for organisations to be more cost effective than their competitors because of the equal opportunities available, thus making strategic positioning the most important way to achieve competitive advantage. Strategic positioning involves setting the right goal, possessing the enabling factors to deliver a value proposition, foregoing some benefits in order to be unique, synchronising all business activities and finally having a continual direction[10].

4-3 Don Tapscott's position

On the other hand, Tapscott (2000) offers a balanced point of view about e-commerce and strategy by outlining the reasons for new business models and the need for organisations to operate differently and compete on new rules by applying business fundamentals. New business models are evolving because the internet makes search easier and allows organisation to coordinate their business activities and contract at lower costs. Tapscott also argues that the internet shifts the basis of competitive strategy because it changes industry structures. Organisations can actually deploy the internet to create unique products, operational efficiencies and enhance customer service and relationships. Also, by shifting bargaining power to customers, the internet actually forces organisations to offer higher values to their customers and find innovative ways of competing. This is the real sense of competition and building competitive strategies. Finally, in the era of e-commerce, the internet has to be seen as an opportunity and " business strategists need new tools, including strategic concepts and analytical methods, to comprehend and exploit new business architectures like b-webs (system composed of suppliers, distributors, service and infrastructure providers and customers that uses the internet for business communications and transactions)"[11]

4-4 Summary of the three points of view on e-commerce strategy

In a nutshell, the position of Evans and Wruster on e-commerce and strategy is that, retailers will have to embrace navigation as a separate business and forget traditional ways of competing such as cost leadership, differentiation, or niche strategies.

Porter's view on the other hand suggests that organisations do not have to change the way they were conducting their activities. All they need to do is to treat the internet as another channel of distribution and develop strategies accordingly.

These two views above represent two extreme positions. On one hand an author trying to demonstrate that internet is ' everything' and will replace existing ways of doing business and on the other hand there is another author trying to convince businesses to stay away from the internet and continue to do what has made them successful over the years. But the truth of the matter is that the advent of electronic commerce is a radical innovation that has brought changes which organisation will have to deal with[12]. According to Lee, C., ' the internet is transforming the rules of competition and inventing new value propositions'. This position comes to support that of Tapscott who suggested that organisations will have to be inventive and innovative in order to compete under the new rules. What both authors simply mean is that organisations do not have to use the internet to cannibalise their existing businesses, nor treat the internet as just another communication technology by using it to replicate their traditional ' brick and mortar' outlets. What organisations need to do is to recognise the impact of the internet on industry structures and find new ways to use e-commerce effectively to reinforce their strategies. In this same direction, Laudon, C. and Traver, C. (2004) suggest that the internet provides organisations with a unique opportunity to differentiate their offerings and pursue business strategies. While the internet provides organisations with means to pursue cost leadership or differentiation strategies, it also forces them to find innovative ways of doing it.

Finally, Chang et al. (2002) suggest organisations integrate e-commerce activities into their strategic objectives and identify IT opportunities that will help them respond to the challenges that the changes in industry structure create.

5- E-Commerce and Profitability in the Retail sector

Profit refers to the " difference between the price a firm is able to charge for its products and the cost of producing and distributing goods"[13]. In other words, if an organisation is not able to make customers buy its products at a price that exceeds its cost, that organisation is likely to run at a loss.

Over the years, a lot of questions have been raised around the profitability of e-commerce. Porter (2001) suggested that profit levels in the era of e-commerce are comparable to zero because of the fact that most organisations were competing on price and charging very low prices for their products in the hope to increase online market share.

Also, during the first stage of e-commerce, which saw the effervescence created by high stock valuations of ' pure clicks', financial results were not as positive as expected and as a result a lot of e-commerce organisations went bankrupt. Companies like Amazon were declaring losses for every financial year and had to depend on heavy borrowings from banks and investors to sustain their businesses[14]. In the movie and music industries for instance, sales revenues decreased due to the fact that individuals no longer needed to pay for movies or music because the internet made information sharing free and easy.

Today nevertheless, the trend in e-commerce has changed and ‘ pure click’ organisations have been able to sustainably make profits over the years. Amazon declared it first ever profit in 2002 and has not declared any loss since. These new trends, in the economic value of e-commerce perhaps suggest that the main questions on e-commerce’s profitability might need to shift from whether e-commerce organisations can make profit and rather move towards, whether since the advent of e-commerce, levels of profitability in the retail sector have increased or decreased and also to identify which business types are likely to be more profitable.

Recent researches conducted by Actinic (2010) showed that, even though online sales are growing faster than that of physical outlets, on average, the amount of money spent online by consumers has dropped slightly from £87. 09 in the second quarter of 2009 to £72. 35 in the second quarter of 2010. The implication of it for retail organisations was an increase in promotional offers, discounted lines or even the offering of lower value products in order to increase sales volumes and revenues.[15]As a logical consequence of this phenomenon, profit margins will be lower. These results also suggest that retail organisations are still measuring the benefits of e-commerce in terms of sales revenues and the number of people who buy from their websites rather than profit levels.

In analysing e-commerce’s profitability in the retail sector, it is also important to compare the levels of profitability of the main actors of e-commerce which are ‘ pure clicks’ and ‘ brick and clicks’, in order to identify the business types that are likely to be more profitable According to a paper written by Min and Wolfinbarger (2005), it was concluded that ‘ brick and click’ organisations’ performance in terms of market share, profit margins and marketing efficiency will be greater than that of the ‘ pure click’ counterpart. This is mainly due to the brand advantage that ‘ brick and clicks’ have and their ability to offer their customers multi-channel shopping.

Case illustration: Marks and Spencer Plc.

Marks and Spencer PLC is one of the largest UK retailers. The company was created around 1985 by Simon Marks who first started it as a stall at Leeds Kirkgate Market. Today, the company can boast of over 21 million people visiting its stores every week.

In 2000, Marks and Spencer launched its e-commerce website which is now ‘ one of UK’s top ten retail websites’[16]with over four million customers’[17]. In March 2007, the company re-launched its e-tail website with the help of ‘ pure clicks’ like Amazon. The collaboration with Amazon was to redevelop M&S website so as to improve the functionality of the website in terms of navigation, search capability and ordering[18]. During the same year 2007, M&S appointed Martha Lane Fox of Lastminute. com (a travel website) as a non executive director in order to boost online sales. These moves suggest that M&S acknowledged that pure clicks had something to teach traditional retailers when it comes to the use of internet to conduct business. This alliance between M&S and Amazon and the appointment of Martha Lane Fox illustrate the changes e-commerce has brought to competition in the retail industry. On the 12 may 2010, Marks and Spencer also launched the first UK

‘ high street retailer’ mobile retail site because the company believes that “ as traditional online retail matures, mobile is expected to become the growth area for internet retailing”.[19]A mobile retail site is a website specially designed to accommodate the use of mobile devices like mobile phones for the purpose of commercial transactions.

In terms of strategy, Marks and Spencer (M&S) uses e-commerce as a mean to achieve its quest of becoming a multichannel retailer, thus, considering the internet as another channel of distribution. This is in line with the prescription of Porter, M (2001) discussed earlier in terms of how organisations that were successful in their traditional setting should treat the internet.

Again, from the annual reports published, it appears that M&S still measures the success of it e-commerce activities in terms of the number of visitors to its website (eyeballs) and revenues rather than profitability. This makes it difficult to assess the profitability of the online business. Another reasons why it might be difficult to assess the profitability of the company’s online activities can be identified in the fact that the sales of goods online are usually credited to the account of stores in which those goods were delivered for collection by customers.

The general perception about e-commerce is that; it first of all helps organisations reach a large number of individuals and thus, reduces the need for physical locations. In the case of Marks and Spencer, even though the first assertion might be true, the second one does not apply. This is because in 2009, the company invested more than ever in building new stores and also redesigning old stores as part of its strategy to achieve a target of £500 million sales by 2010/2011. This implies that e-commerce cannot be or is not yet an alternative to traditional ‘ brick and mortar’ ways of doing business for a high street retailer like Marks and Spencer. One may argue that this strategy works for Marks and Spencer because the company has ‘ the brand advantage and the ability to offer multi channel shopping’[20]

In terms of the profitability, since 2000 when M&S website was launched, the company has experienced variations in its profit levels which cannot be directly related to its online activities. Nevertheless the internet has contributed to some extent to the success of Marks and Spencer. During the first year following the launching of the website, the company’s profits went down mainly because of an increase in operating costs partly caused by IT investments to support its online business. In 2003, M&S worked towards reducing operating costs through global sourcing and reduced the number of warehousing contractors. This strategy paid off by an increase in the organisation’s operating profit. After 2007 when the company’s website was re-launched with the collaboration of Amazon, online sales revenues grew to £100 million for the first time ever. The company’s e-commerce website was again re-launched in October 2009 to respond to “ customers’ demand for a more engaging and interactive web experience”[21]. According to the company’s 2009/2010 annual report, UK operating cost for the year increased by 1% and the cost of maintaining its IT system alone increased by 7. 5%. On the other hand, UK operating profit went down by 1. 3%. Also the company acknowledged the fact that its 3. 2% increase in total revenues for the year was mainly due to “ an improvement in like-for-like sales as well as the addition of new space in the UK and a strong performance in International business”. These results could suggest that the cost of IT investment is not offset by online sales revenues.

Marks and Spencer has also recognised the fact that consumers more often than not use the internet to browse for bargains and this has led most retail organisations offer discounts, free shipping or some kind of incentive to attract consumers[22]. This coupled with cost of IT maintenance might be a cause of high sales volumes but lower margins and might suggest that the use of the internet as a distribution channel might not be so profitable. Thus organisations like Marks and Spencer might need to find a more profitable way to use the internet.

Conclusion

The advent of e-commerce raised a lot of questions in relation to its impact on businesses. In the beginning of e-commerce, it was believed that organisations went online because of the perceived economic value of e-commerce. On the other hand, researchers have suggested that most retail organisations moved online because of organisational readiness and external influences.

E-commerce by offering organisations and consumers flexibility, created new business types in the light of B2B, B2C and B2B2C and also organisations that were ‘ born’ on the internet and those that moved to the internet by combining a brick and mortar presence with an online presence. The proliferation of new business types also led to changes in traditional business models which affected industry structures. More than ever, collaborations and alliances were created with partners which were not possible in traditional business settings.

In relation to strategy, there were diverging views about the best strategy to adopt in order to succeed in the era of e-commerce. Evans and Wruster suggested organisations should abandon their old ways of competing and fully embrace e-commerce by competing on reach, affiliation and richness. On the other hand Porter advised organisations to continue doing what made them winners and treat the internet for what it is, which is another channel of distribution. In contrast to the two extreme views presented above, Tapscott proposed organisations return to business fundamentals and apply some fresh thinking which is required in an era where competition rules have changed.

E-commerce has also affected organisations' revenues models and consequently their levels of profitability. Porter argues that the competitive environment of e-commerce makes it very difficult for organisations to make profit because, it encourages price competition. On the other hand, successful organisations like Dell, Amazon and eBay suggest that it is possible to make profit on the internet. When it comes to the type of organisation which is likely to make more profit, a research conducted by Min, S. and Wolfinbarger, M., (2005) suggested that ' brick and click' combinations have an advantage over ' pure clicks'. This is because ' brick and clicks' have the brand and the physical stores advantage which they can use to a certain extent to offset the cost of IT

Finally, ‘ brick and clicks’ like Marks and Spencer give the impression that retailers still use the internet as a channel of distribution and thus making e-commerce a replicate of their ‘ brick and mortar’ businesses.