

DELIVERY LOGISTICS FOR EUROPEAN E-COMMERCE

AUTHORS

Michael Lierow

Matthieu Sarrat

Sebastian Janssen



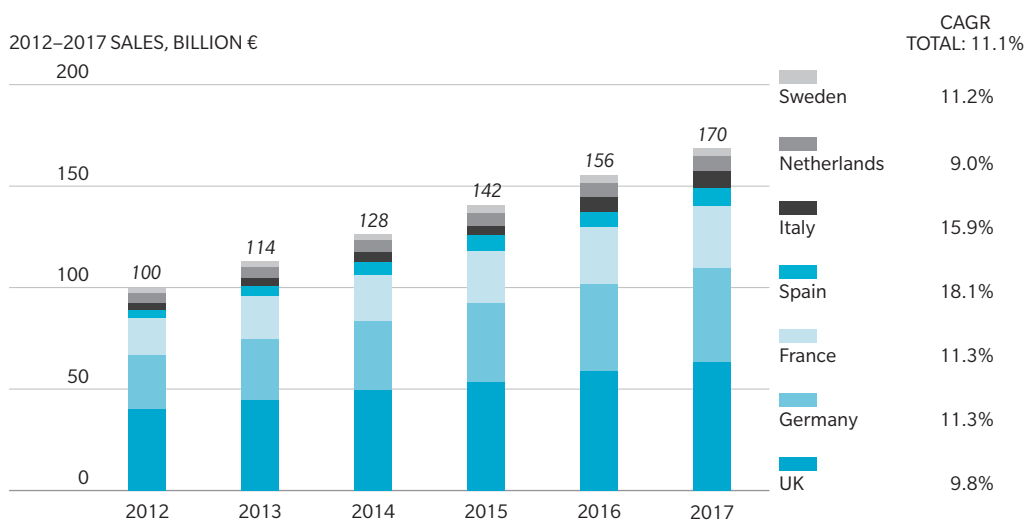
The e-commerce industry in Western Europe is growing rapidly (e.g., revenue growth of 10-15 percent per year) with overall online sales penetration poised to increase by double-digits over the near term. And as Internet-driven business-to-consumer (B2C) package flows expand at nearly the same rate, so too does the opportunity for providers of delivery logistics to grow their businesses—although they will find the e-commerce market radically different from other markets they serve.

The European e-commerce market is at a turbulent stage, with various players competing for market and mind share:

- The giant generalist e-commerce companies and category killers that own their inventory (e.g., Amazon, Asos, Zalando) are driving consumer shopping innovations and further developing fulfillment capabilities. They even capture initial product-related search traffic at their sites.
- Brick-and-mortar retailers (e.g., PPR, H&M, Marks & Spencers) are aggressively adding e-commerce channels and searching for optimal solutions to leverage their existing offline distribution networks.
- Online marketplaces (e.g., Ebay, Overstock) are ever innovating the front end, but are struggling to keep consumer attention, as they lack influence over back-end logistics.

For all companies operating in the e-commerce space, however, offering the most convenient possible shopping experience is a critical component of the value proposition—putting pressure in turn on 3PLs that provide delivery and return services.

EXHIBIT 1: FORECAST FOR EUROPEAN ONLINE RETAIL



Source: Forrester Research Online Retail Forecast 2013, Oliver Wyman analysis.

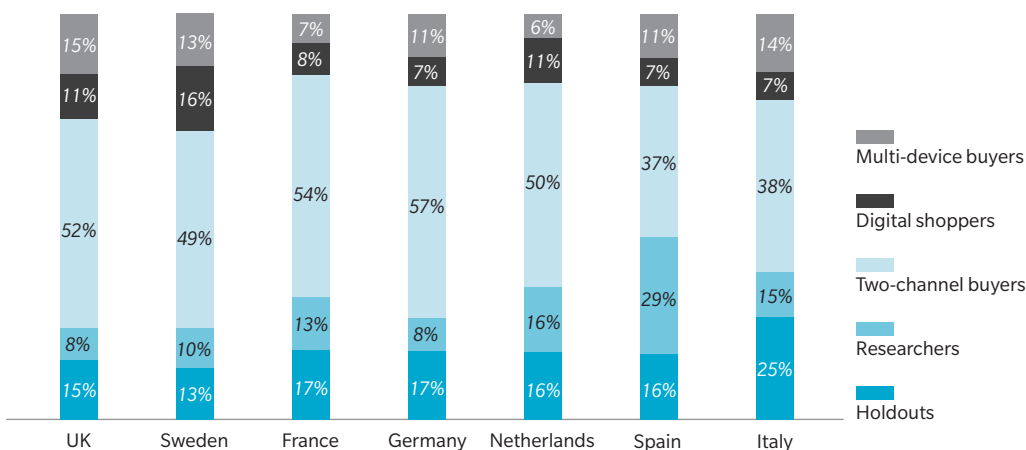
THE CHANGING PARADIGM OF CONSUMER BEHAVIOR

Consumer expectations regarding delivery services have risen as remote-shopping habits have evolved from a careful buying process that accepted some degree of inconvenience and long delivery times to transactions that are increasingly driven by spur-of-the-moment shopping decisions and total customer convenience. The consumer shopping paradigm has shifted:

- From primarily offline and telesales channels (store/phone/catalog) to increasingly frequent multi-device and online channels: 11 percent of shoppers in Europe are multi-device buyers; 57 percent buy using two or more channels (hence the rise of mobile online sales) (Exhibit 2)
- From acceptance of long delivery wait times to expectations that delivery will be as fast as possible, preferably same-day and preferably at no additional cost (hence the rise of same-day offers)
- From inflexible delivery points and uncertain delivery times to consumers wanting the flexibility to get deliveries at the time and location of their choice (hence the rise of time-windows for delivery services, flexible additional delivery attempts, and multiple options for delivery points)
- From policies designed to discourage returns through difficult logistics to the need to minimize returns (e.g., through better product descriptions and online customer reviews); and on the logistics side, making returns as painless as possible (preferably free, with in-store or pickup return options), as an easy return process influences online buying decisions heavily for non-commodity sectors (e.g., fashion)

EXHIBIT 2: TOUCH POINT SOPHISTICATION IN EUROPE

PERCENTAGE OF CUSTOMERS, 2012



Source: European Technographics Online Benchmark Survey 2012, Oliver Wyman analysis.

Meeting these sharpened expectations is one way that e-commerce players can differentiate themselves from their competitors and trigger repeat purchases, increase the value of goods and the average basket size, and reduce return rates. “Beacon” companies, such as Amazon and Asos, drive consumer expectations around delivery service, by constantly improving their offer: Amazon and Asos set service-level benchmarks, consumer expectations quickly adapt, and other e-commerce players must keep up or lose the race.

COMMODITIZATION OF STANDARD DELIVERY SERVICES

Standard delivery services, such as next-day home delivery, are increasingly becoming commoditized. Customers are starting to take convenient delivery for granted: from their point of view, delivery is a fixed component of the purchase, not an extra service. To compensate, e-commerce giants are developing sophisticated purchasing organizations and aggregating increasing volumes of parcels through third-party fulfillment businesses they own, thus increasing their bargaining power with delivery logistics providers.

Pricing of delivery into the product (rather than as a separate line item) and the growth of flat-rate subscription models (such as Amazon Prime)—both powerful retention tools—are exacerbating the need to lower delivery costs. As a result, third-party delivery logistics providers are seeing more volume fluctuation when e-commerce players shift volumes between 3PLs. Prices for next-day delivery in Germany are hovering around two euros per parcel, and are only slightly higher in the UK and France.

FOCUS ON THE DELIVERY EXPERIENCE

In their quest for differentiation, e-commerce players are considering selectively moving into logistics to offer improved delivery and return experiences that “plain vanilla” 3PLs cannot offer (since these 3PLs serve the whole market). Amazon, for example, is no longer happy with the later outbound cut-off times, compared to other e-commerce players. It may consider moving into same-day logistics (e.g., in Germany) if no logistics partner steps up to offer the service.

At the same time, multi-channel businesses (i.e., bricks-and-mortar retailers with online channels) are experimenting with in-store pick-up and return solutions (partially counter, partially locker-based, with 24/7 access in urban downtowns). Well placed and priced—as multi-channel players can save significantly on logistics costs—these solutions have the potential to capture some of the market share vanishing from standard delivery networks.

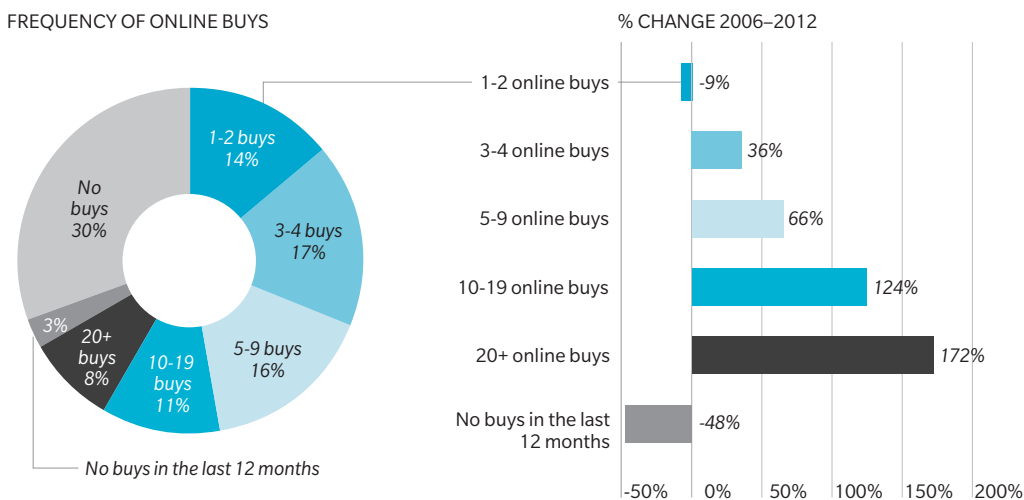
STEPPING UP TO E-COMMERCE LOGISTICS CHALLENGES

E-commerce business models are still developing at a fast pace. The difference versus five years ago, however, is that e-commerce players today are much larger, their bargaining power is greater, and Internet-savvy consumers are both buying more frequently (Exhibit 3) and more willing to try out new offers (which has allowed players like Zalando to quickly gain significant market share as a category killer, by swamping the market through marketing spend). Deliveries and returns for urban and suburban areas for the fashion segment in Germany alone will account for more than 80 million parcels in 2013.

In this dynamic environment, delivery logistics has become a tool for standing out from the crowd. Logistics providers thus not only need to react quickly, but to implement new business design elements:

- Cost focus will remain relevant: To capture volume from large e-commerce players (so as to fill the networks with base volume), 3PL providers need to offer low-priced service—which only works where network assets are well planned and utilized.
- Innovation will be important: 3PLs will need to become better and faster at innovating, whether this involves developing mobile apps to track and trace parcels or tools to enhance customer convenience.
- Multiple location touch points will be necessary to stay competitive:
 - To the door options (standard)
 - Locker options
 - 24/7 retail shop access, serving both urban core (e.g., travel agencies, coffee shops) and suburbs (e.g., petrol stations)
 - Workplace access (mailrooms at large firms, where parcels can be delivered to employees)

EXHIBIT 3: CHANGE IN ONLINE BUYING FREQUENCY IN GERMANY, 2006-2012



Source: Allensbacher Computer- und Technik-Analyse 2012, Oliver Wyman analysis.

Another option for 3PLs, as intermediaries between e-commerce players and consumers, is to get more value out of customer touch points, a hitherto largely ignored but potentially valuable asset. Gathering data on how customers use touch points could provide insights into behavior patterns and preferences that delivery logistics providers could use both to improve their own services and to increase their value as partners to leading-edge e-commerce players.

These solutions hold true not just for 3PLs but also for European postal services, which are facing declining letter volumes. The challenge for postal services will be to move away from their traditional, bureaucratic “letter culture,” to focus on innovation and seamless integration of customer touch points.

Delivery logistics providers who succeed in serving the e-commerce market will be locking in to a long-term growth engine: While B2B parcel growth is projected to remain weak (and declining in some markets), B2C flows are expected to continue expanding over the foreseeable future.

INNOVATION FOCUS CASE EXAMPLE: SAME-DAY DELIVERY

Ever faster delivery is a key e-commerce market trend: D+1 is already quasi-standard for most of Germany and the UK and D+2 for France. The next step for Europe will be same-day delivery service. Same-day is expected to become a widely available option in urban areas of Western Europe within the next five years; indeed, implementation has already begun:

- Shufl and Tiramizoo are back-end services that match an e-commerce order with a courier service for delivery within 90 minutes. They are currently available in the UK and Germany and expanding into the US and other countries. While these services are great examples of bundling single-courier service to become a meaningful market player for same-day delivery in urban areas, they are not all that scalable for lower-cost delivery options.
- DHL is experimenting with same-day delivery from the warehouse, e.g., in the Cologne area, Germany, together with Gourmondo, an online food retailer.
- After setting up regional fulfillment centers, Amazon is expected to further expand its same-day services, by building on already existing evening delivery services. In Germany, for example, Amazon is expected to expand into a differentiating same-day service within the next 12 months.

The same-day trend favors e-commerce players with a net of distribution centers located close to urban areas. Multi-channel bricks-and-mortar businesses may be particularly well positioned, as they sometimes have decentralized warehouses. E-commerce category killers like Zalando are more vulnerable and will have to move from central to regional warehousing to realize the operational foundations of same-day delivery. We expect possible leapfrogging by multi-channel players into same-day service within the next 12 months.

GROWING WITH A GROWING MARKET

The dynamics described above must be considered only a starting point. No delivery logistics provider who wants to serve the e-commerce market can afford to stand still; nor can e-commerce players themselves. Flexibility, keen attention to market trends, and a business culture that embraces change are now critical components of success. B2C flows are becoming more seasonal and more volatile. Consumer shopping habits and expectations will continue to evolve. And, e-commerce players will continue to innovate in their search for an “edge,” putting pressure on their third-party suppliers to keep up. Only through nimble, operationally excellent, and innovative business designs can delivery services providers break the commoditization cycle, increase their bargaining power, and share in the benefits of an expanding e-commerce culture.

OLIVER WYMAN'S E-COMMERCE LOGISTICS EXPERIENCE

Oliver Wyman has worked with a range of pure and multi-channel e-commerce players, delivery logistics partners, and logistics fulfillment companies to develop value propositions and business designs focused on capturing market share and growing margins. Our focus areas include:

| FOR E-COMMERCE AND MULTI-CHANNEL COMPANIES | FOR LOGISTICS PROVIDERS |
|--|--|
| <ul style="list-style-type: none">• Diagnosis of relevance of customer touch points and development of lasting differentiation potential | <ul style="list-style-type: none">• Strategic positioning, identification of strategic customer segments |
| <ul style="list-style-type: none">• Supply chain diagnosis and development from offline centered to true multi-channel logistics | <ul style="list-style-type: none">• Development of market sizing and models to expand services and offers |
| <ul style="list-style-type: none">• Diagnostics and analysis of current logistics/ fulfillment operations | <ul style="list-style-type: none">• Strategic network design to resize networks and capture opportunities from e-commerce |
| <ul style="list-style-type: none">• Development of best-practice strategy and operations in fulfillment and logistics delivery options | <ul style="list-style-type: none">• Consumer requirements mapping with regard to logistics/delivery services |
| <ul style="list-style-type: none">• Operational improvement programs, lean production, integration of offline and e-commerce logistics | <ul style="list-style-type: none">• Operational diagnostics and improvement of service levels |
| <ul style="list-style-type: none">• Competitive benchmarking of supply chains, logistics processes, etc. | <ul style="list-style-type: none">• Volume volatility analysis with respect to utilization of fixed assets, management at peak times during the year |
| <ul style="list-style-type: none">• Consumer surveys on relevance of innovative solutions and willingness-to-pay | <ul style="list-style-type: none">• Due diligence support and strategic analysis on expanding regional and functional expertise |
| <ul style="list-style-type: none">• Make-or-buy decisions for fulfillment/customer service units | |

ABOUT OLIVER WYMAN

Oliver Wyman is a global leader in management consulting. With offices in 50+ cities across 25 countries, Oliver Wyman combines deep industry knowledge with specialized expertise in strategy, operations, risk management, and organization transformation. The firm's 3,000 professionals help clients optimize their business, improve their operations and risk profile, and accelerate their organizational performance to seize the most attractive opportunities. Oliver Wyman is a wholly owned subsidiary of Marsh & McLennan Companies [NYSE: MMC], a global team of professional services companies offering clients advice and solutions in the areas of risk, strategy, and human capital. With 52,000 employees worldwide and annual revenue exceeding \$10 billion, Marsh & McLennan Companies is also the parent company of Marsh, a global leader in insurance broking and risk management; Guy Carpenter, a global leader in risk and reinsurance intermediary services; and Mercer, a global leader in human resource consulting and related services. For more information, visit www.oliverwyman.com. Follow Oliver Wyman on Twitter @OliverWyman

For more information on Oliver Wyman's e-commerce logistics experience, please contact your account representative or one of the following partners:

DR. MICHAEL LIEROW

Partner

+49 89 939 49 757

michael.lierow@oliverwyman.com

GILLES ROUCOLLE

Partner

+33 1 45 02 33 48

gilles.roucolle@oliverwyman.com