Cross-Channel Integration in Retail
Creating a Seamless Customer Experience
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In July 1995, a startup called Amazon.com sold its first product—a science book—and the clock started ticking on a new era of retail. Nearly two decades later, Amazon is a US$50 billion company, and the digitization of retail has profoundly changed the nature of the shopping experience. With more and more sales shifting online each year, most traditional retailers are facing the biggest challenge in their histories: How do they meet consumers’ expectations of a seamless shopping experience?

The ability to integrate across channels enables retailers to give consumers what they want, and increasingly demand. For traditional retailers, cross-channel integration is fast becoming a competitive necessity. Many have lost market share to Amazon and other online competitors. Developing a viable cross-channel capability is within the reach of traditional retailers, if they make the right moves in five areas—changing the structures of their organizations, improving their logistics, creating a common technology backbone, using business intelligence more skillfully, and reinventing their cultures. It won’t be easy, but retailers no longer have a choice.
E-commerce and mobile commerce have reached critical mass in many industries, a result of huge changes in how consumers use technology. In 2011, unit sales of smartphones surpassed those of personal computers for the first time. Tablet computers are part of the same shift away from traditional computing; unit sales of tablets more than tripled in 2011, to about 73 million units, with Apple selling more iPads than Hewlett-Packard sold PCs. People now spend almost as much time online and using their mobile phones as they do watching television.

The shift to online and specifically to mobile Internet use—eBay says it did some US$5 billion in mobile sales in 2011—has had a significant impact on consumers' shopping behavior. Digital consumers today expect to have the flexibility to find and buy the product or service they want no matter where they are—sitting on their living-room couch, riding in the passenger seat of a car, or even browsing in a physical store. Likewise, they expect to be able to provide feedback and receive service in multiple channels; they want the option of ordering a product online, and then picking it up at the store or getting it delivered to their home. (Today’s consumers also increasingly expect free shipping and returns.) This has created intense pressure for retailers to make the shopping experience seamless, and to give consumers new levels of convenience and choice. It also creates enormous cost pressure because of the need to upgrade logistics and handle online transactions.

Despite consumers’ expectations, very few traditional retailers offer a seamless shopping experience across multiple channels. Even the ones that have significant online sales generally treat their online and offline businesses separately—each in its own silo. This won’t stop consumers from pushing for an experience that feels more integrated. Retailers that understand this, and start to develop a capability of cross-channel integration, are the ones that will have a chance to win.
NEW SOURCES OF COMPETITION

Retailers used to be able to gain advantage through their product portfolios and the quality of their sales personnel—by employing floor staff who knew the products and could help shoppers find what they wanted. Then, for a while, the source of advantage shifted to price. In an age of digitization, most retailers’ source of advantage has shifted again—to greater selection, price transparency, and convenience; improved service, including the ability to process orders at any time of day or night; superior customer insights; and access to ratings and peer reviews. Amid these changes, retailers are facing significant new sources of competition.

Manufacturers Going Direct

Digitization enables a more direct link between consumers and manufacturers, and manufacturers are starting to take advantage of this reality. Online marketing and advertising are the least of it—manufacturers have been doing that for years. Now, more manufacturers are actually selling online, especially higher-margin products in high-growth markets. In doing so, they not only increase their profitability (by recovering some of the margin given up to retailers) but also get valuable new insights as they engage in more direct relationships with their customers than they have ever had before.

Adidas’s opening of retail stores in Russia is a good example of a manufacturer going direct. At its own branded retail outlets and on its online platform, the sneaker maker can sell its whole line, especially high-end footwear, without having to negotiate for shelf space or relinquish percentage points of margin. Manufacturers that have success in going direct may stop working with retailers altogether—or use retailers only for low-margin products.

New Gatekeepers of Consumers

In another era, consumers often started their shopping experience by heading to a retail store or to a mall with multiple retailers. Now, a shopping expedition is just as likely to begin on a search engine like Google (with 730 million daily visitors), a social media platform like Facebook (with 900 million monthly active users), or a price comparison engine or ratings platform such as TripAdvisor (with 50 million customer reviews).

Because of the unique kinds of information and utility they offer, these services have eroded some of the power previously held by retailers, including in the area of product pre-selection and pricing, and have put that power in the hands of consumers. In an earlier era, a retailer might have been able to maintain high prices on infrequently purchased items, because customers might not come to the store with any particular expectation of what they should pay. A search engine like Google changes that dynamic, introducing a kind of transparency that shifts the money flows around shopping. Because their revenue comes from traffic, clicks, and advertising, Google and other gatekeepers are removed from traditional retail economics. In the future, as they inevitably start operating in the purchase stage of the funnel, the new gatekeepers’ impact on retailers will become

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even bigger, to the point where the profits involved in selling products might vanish, replaced by profits from advertising and other business-to-business services. The number of products that are “loss leaders”—there for a purpose other than any profit they themselves produce—will likely expand.

**Online-Only Retailers**
Indigenous online retailers are a relatively new breed. By and large, they don’t operate by the old metrics of traditional retailers; things like margin per square foot or margin per catalog page are irrelevant (or at least less relevant) to them. Nor do they need to open retail stores in populous, easily accessed, high-rent locations; they can gain scale and market share in other ways, such as by creating a great user experience, exploiting their knowledge of search engine optimization, and using technology to support shopping functions that previously had to be done in person. The pure online retailers that have become successful tend to be extremely focused on a few differentiated capabilities; examples are Amazon with its logistics and payment systems and the German online store Zalando with its marketing and data analytics. The fact that pure online players are often still venture capital–funded and not required to make a profit in the short term increases the challenge they pose to traditional retailers.

Where they see an opportunity, online retailers are also challenging traditional retailers on their home turf—and occasionally making big inroads. Apple is the most dramatic example. Its retail stores have been a huge success, generating more than 17 times the sales per square foot of the average U.S. mall retail space. Other online retailers are also adding offline assets, such as print catalogs and temporary stores (see “Cross-Channel Integration for Online-Only Retailers”).

**First-Mover Traditional Retailers**
A final source of competition is other traditional retailers that may be pushing ahead more quickly to create integrated cross-channel experiences. For instance, Germany’s Otto Group, a big catalog retailer, has been an early adopter of online and mobile commerce, bypassing competitors like Neckermann (which declared bankruptcy in the summer of 2012) and Quelle GmbH (now defunct). The race to the cross-channel future has already produced casualties.

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**Cross-Channel Integration for Online-Only Retailers**
Cross-channel integration may only seem relevant to offline retailers, with their entrenched bricks-and-mortar assets.

In fact, integration is important to some indigenous online retailers as well, specifically to those starting to use such traditional assets as catalogs, direct mail, and the occasional real-world outlet.

For instance, eBay opened a temporary pop-up store in London for the 2011 Christmas shopping season. And Zalando, a German online shoe and fashion store, is one of an increasing number of online retailers that now publish an innovative print catalog, mixing a classic catalog with an editorial magazine style to appeal to new and existing customers. It also recently opened a bricks-and-mortar outlet store, where online customers can shop returned products and special deals.

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A QUESTION OF WHEN, NOT IF

This new competitive situation will affect every product category. In western Europe as a whole, nearly 10 percent of total retail sales now happen online. That overall figure obscures big differences among sectors (see Exhibit 1). For instance, 17 percent of books and 35 percent of music are now sold online, whereas most other categories are just moving into the online space. Online sales of groceries and personal care are among the categories that have not yet reached critical mass; both remain far below 5 percent. Ten percent seems to be a rough turning point. Once online sales in a category reach that level, the influence of online—and of consumer expectations—becomes impossible to ignore and the business models start to shift across the complete category. This may also reflect the attention that the

Exhibit 1
Online Retail Penetration

Note: In some categories, the data set is based on a subset of markets and triangulation via retail volumes.
Source: Booz & Company
sector’s leading companies start paying to cross-channel initiatives once online sales pass that threshold.

Generally speaking, the speed at which different retail sectors have come online reflects a number of product- and market-related factors, such as the sector’s product constellation (for example, physical versus intangible or durable versus perishable) and the product category’s degree of standardization and comparability (see Exhibit 2).

Fashion is one of the industries headed for online acceleration in the next three years, thanks to the improved online shops of traditional apparel retailers, the rise of some dynamic online pure-play entrants (for example, Mytheresa.com and Asos.com), and the line extensions of existing online retailers (for example, Zalando). Furniture is another category poised to take

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**Exhibit 2**

*Rates of Online Penetration*

<table>
<thead>
<tr>
<th>Product Characteristics</th>
<th>EASIER TO SELL ONLINE</th>
<th>HARDER TO SELL ONLINE</th>
</tr>
</thead>
<tbody>
<tr>
<td>- Easily digitized or intangible</td>
<td>- Physical products</td>
<td>- Not standardized</td>
</tr>
<tr>
<td>- High degree of standardization</td>
<td>- Relatively standardized</td>
<td>- Individual ‘experience’ products, offered by smaller retailers in fragmented industries</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Logistics</th>
<th>EASIER TO SELL ONLINE</th>
<th>HARDER TO SELL ONLINE</th>
</tr>
</thead>
<tbody>
<tr>
<td>- Limited to none (low weight/volume or digital)</td>
<td>- Physical shipment required</td>
<td>- Physical shipment required</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Examples</th>
<th>EASIER TO SELL ONLINE</th>
<th>HARDER TO SELL ONLINE</th>
</tr>
</thead>
<tbody>
<tr>
<td>- Travel</td>
<td>- Consumer electronics</td>
<td>- Jewelry</td>
</tr>
<tr>
<td>- Music</td>
<td>- Mobile contracts and equipment</td>
<td>- Apparel</td>
</tr>
<tr>
<td>- E-books</td>
<td>- Software</td>
<td>- Fresh food</td>
</tr>
<tr>
<td>- Software</td>
<td></td>
<td>- Plants</td>
</tr>
</tbody>
</table>

Source: Booz & Company
off online, partly because of the creation of new home lines by some non-furniture companies (such as H&M and Zara). In late 2011, the CEO of Rocket Internet, a Berlin-based incubator that has sold early-stage companies to Groupon and eBay, advised his management team that the time had come for “full-scale investment” in the furniture category.

Other categories likely to show high online growth in the next couple of years are cosmetics (with the rise of innovative online subscription models such as U.S.-based Birchbox and European copycats like GlossyBox) and drugstores/over-the-counter pharmaceuticals. The potential of the latter came into focus when Walgreen Company, the largest U.S. drugstore chain, bought Drugstore.com in 2011 and recently acquired Alliance Boots in the United Kingdom.

Although the online trajectory of most categories depends on the category’s characteristics, there are also some differences across geographies. For instance, some emerging markets could develop faster in certain categories because of a lack of physical store networks and low levels of automobile ownership. Another example of a geographic difference is the relatively advanced state of online food sales in Sweden and the Netherlands. In these small countries, with their short distances and their agile and well-developed logistics networks, the inherent obstacles to online food sales are lower than elsewhere, allowing for the development of a cross-channel offering. In the United States, several grocery store chains owned by the Dutch grocer Ahold use Peapod, an online delivery service, to create a cross-channel offering.

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For a few companies, cross-channel integration—giving shoppers a seamless experience—is creating competitive advantage in the marketplace. Eventually, it will move from being a strategic advantage for a few retailers to a competitive necessity for all. Indeed, in some parts of retail that are further along this path, the pressure to adapt and become truly integrated across multiple channels is already taking a toll.

Best Buy is an example of a company that is struggling in an era of increasing cross-channel integration. Although this $51 billion consumer electronics firm now has a significant cross-channel offering—for instance, allowing its customers to order products online and pick them up at the store, and integrating a lot of social media functions across channels—its efforts have not yet yielded satisfactory results either online or offline. Online, the company’s U.S. revenue increased 13 percent in its most recent fiscal year—less than one-third the rate of Amazon’s revenue increase. (Best Buy’s giant physical stores are sometimes derisively referred to as showrooms for Amazon; in a twist on the idea of “ROPO”—research online, purchase offline—more and more consumers now look at products offline at Best Buy, and then go home and order them on Amazon or increasingly do it via their smartphone right in the store.)

In fiscal year 2012—a period in which the company’s total revenue advanced just 2 percent and it lost $1.23 billion—Best Buy closed many of the large-format stores in its international division, including stores in China, the U.K., and Turkey. Best Buy has also started to close big-box outlets in the U.S., in order to reinvest in more specialized outlet formats. While being a potential asset in cross-channel retail, the huge legacy of physical outlets proves to be an inherent disadvantage of traditional retailers versus new entrants that can gear investment funds into customer experience, particularly in the front end and logistics.

In some parts of retail that are further along this path, the pressure to adapt and become truly integrated across multiple channels is already taking a toll.
Media-Saturn, Europe’s largest consumer electronics retailer, is facing similar problems. Since the launch of its online shops in late 2011, the company’s revenues and profits have plummeted, largely due to an online-led reduction in pricing that has affected margins at its physical stores. Media-Saturn’s difficulties may be temporary—exacerbated by the relatively early stage of its cross-channel efforts. Indeed, a 2011 study by the University of St. Gallen put Media-Saturn near the top of a group of German retailers for its channel integration and harmonization. In other words, the company may well bounce back. Still, what has been happening at Media-Saturn during its transition shows why so many retailers shake their heads when we talk to them about their cross-channel strategies and say, “Cross-channel just means crossed signals—and a lot of problems.”

Best Buy and Media-Saturn highlight the challenges of an industry in which cross-channel integration is already a competitive necessity. Retailers in other industries can use a simple diagnostic to figure out their own stage of development, and their readiness for cross-channel integration as their customers increasingly demand it (see “Your Cross-Channel Readiness Profile”).

Your Cross-Channel Readiness Profile
Answers of “yes” show where retailers have work to do.

• Is your organization still running online/mobile as separate silos from offline sales (different sales teams, different marketing teams, maybe even different procurement teams)?
• Is your monitoring system still focusing on traditional KPIs and lacking transparency on online KPIs such as conversion rate?
• Are you experiencing difficulties in allocating sales and marketing and other budgets between functions and channels, especially when it comes to online advertising, search engine optimization, and similar topics?
• Is it becoming more complicated to define the role and format strategy of your physical outlets? Are you experiencing problems in daily management of those physical stores—due to outdated incentive schemes, for instance?
• Are your logistical capabilities struggling with the new requirements of online/mobile sales, perhaps due to different warehouses or system issues?
• Are your IT systems still preventing you from getting full transparency and reaching full performance across all sales channels?
• Do you observe an internal cultural divide between the teams focusing on your traditional channels and the teams driving online activities?
There are five success factors that retailers must address to position themselves to compete in a cross-channel future.

1. **Restructure your organization and processes to enable a true cross-channel experience.** Processes that exist in silos are the enemy of cross-channel integration. For instance, retailers should not have different return policies for products bought in-store and online. Likewise, a customer stopping in at a physical store to check on an item that was ordered online—and never arrived—should not have to explain what product she ordered. At a retailer that is truly integrated across channels, the processes should be seamless and the customer experience should be consistent. Yet this is almost never the reality. One frequent cause of trouble is the existence of a dedicated online sales department. A dedicated sales department is useful to get the online business going, but it creates a barrier that can be counterproductive later on, when the organization needs to provide more of a cross-channel experience.

   The aforementioned Otto Group recently moved to free itself from this trap. To minimize channel conflicts, the company’s leadership restructured its marketing, format management, and category management functions so they are now run centrally across channels, not separately by online and offline units.

2. **Improve operations and logistics.** Whereas traditional distance retailers (for example, mail-order companies) have ample experience mailing products to private households and processing returns, most retailers don’t. They need to build the capabilities to manage returns efficiently or risk being overwhelmed. This challenge has been intensified by some leading companies’ moves to constantly up their game in terms of delivery options, raising customer expectations. For instance, Amazon’s next-day delivery is still not matched by most online competitors, yet Amazon has now introduced same-day delivery in select urban areas. In another example, Tesco, the U.K. food giant, is offering a 90-minute delivery service in London. The same holds true for delivery charges and return policies. Free shipping and returns have started to become the norm around Europe. The U.K. fashion and beauty store Asos.com has taken this idea one step further; it offers free shipping throughout the world. The ante keeps going up, every day.

3. **Create a common IT backbone.** If a retailer’s channels are to be truly integrated, they must be linked to a single IT backbone with a dedicated cross-channel integration layer. The idea is to provide visibility and a seamless experience across channels, so that, for instance, customers checking the website can determine the availability (and the quantity
available) of an item in the store. With the batch systems in place at many traditional retailers, the fact that the last item of something has been sold won’t necessarily be evident to online shoppers. They could show up at the store and discover they’d wasted a trip. There are few faster ways to frustrate a customer.

The creation of a common IT backbone starts with a clear definition of requirements. But that is just the beginning of the job. Complex IT integration projects don’t come together overnight—and they require a significant investment. Upgrading the often outdated enterprise resource planning (ERP) system, for instance, can easily be a multiyear journey and for large retailers often requires an investment of hundreds of millions of euros.

4. **Use business intelligence and customer relationship management in a more sophisticated way.** In the cross-channel future, the analytics that are increasingly becoming part of retailers’ tool kits must operate in every place that customers make transactions, and must benefit every part of the business. This is key to the concept of customer lifetime value. A good CRM system is essential. The idea is to make intelligent product suggestions à la Amazon, except to do it across channels—for instance, to use mobile location services to make an offer when a customer is in a mall, or to use e-mail to make a special, related online offer to a customer who has just bought something offline. An example is the partnership American Express has forged with Twitter and selected retailers. An Amex cardholder can send out a tweet using a customized hashtag and receive special offers from merchants, with Amex issuing a credit within a few days on qualified purchases. Another example is Shopkick, which integrates bonus schemes for consumers across retail channels.

5. **Reinvent the company culture.** The imperative to offer a cross-channel experience represents the largest transformation that many retail leaders have ever faced. It requires a willingness to make big bets, adopt new business models, make greater use of analytics, and change in other fundamental ways. This is not the time to think incrementally. The required changes are so dramatic that they stand no chance of catching on unless senior leadership shows the way. This may require some tough decisions involving personnel. It will certainly require recruiting some new talent from the outside—and perhaps from outside the traditional, purchasing-driven retail culture. What retail companies increasingly need are people who would fit in well at Facebook or Google. To be sure, this will make some staffers and managers uncomfortable and force just about everyone to adapt. But there is no way to get to the future without shaking up the present.
CONCLUSION

Consumer expectations about shopping have changed dramatically in the last few years. Many consumers now take for granted that shopping should be a seamless experience, allowing them to carry out transactions wherever they happen to be. In some respects, the reality already matches this ideal. A consumer’s ability to buy just about anything through a computer or mobile device removes one advantage of traditional retailers, their physical presence. Indeed, in some parts of retail, having too many physical assets has become a liability. This is evident in the move by many retailers to close stores or reduce their footprints in other ways.

The imperative for traditional retailers is to create a cross-channel offering, one in which their customers have the same experience online as in their stores, and can move between the two channels without friction. Here, most retailers have lagged behind. Either they have kept their online and offline channels organizationally separate for too long—a common mistake—or they have combined their online and offline operations but are still struggling to integrate them. What they should evolve into may be clear, but getting there can be hard.

There may be opportunities for pilot programs and quick successes to educate the larger organization. If so, retailers should embrace them. This is a years-long journey that every retailer will have to make unless it has a clear niche positioning. Those that start the soonest will have an advantage.

One Retailer’s Adaptation

A large retailer illustrates the challenges of creating a cross-channel offering. At a relatively early stage in the Internet boom, the company brought in a new team of young, tech-savvy managers to run the online part of its business. It was a useful way of building the required online capabilities, and it enabled senior leadership to quickly build know-how and create a sizable online business, which now accounts for more than half of the company’s revenues.

Still, the company has faced challenges in competing against its nimbler online rivals. Amazon, as well as some “category killers,” has offered lower prices on products in areas core to the company—such as fashion, consumer electronics, and furniture—or value propositions that are superior in other ways. This has hurt the company’s market share and reduced its profitability. In addition, the original organizational structure, which kept the online part of the business separate from the traditional catalog business, led to turf wars between the mail sales channels.

Recently, the company has moved to reduce these conflicts and harmonize the business. There is now an “e-commerce first” philosophy, and functions such as marketing, procurement, and pricing are all in the process of being integrated. The company is also changing its incentive schemes and revising its logistics strategy to meet evolving industry norms in areas like product returns. It is also addressing the required cultural transformation of new and old talent.

To be sure, this company is only partway through its transformation, and it will have to remain flexible. But it has begun to make the adaptations that all retailers must make if they are to preserve their right to win.
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We believe passionately that essential advantage lies within and that a few differentiating capabilities drive any organization's identity and success. We work with our clients to discover and build those capabilities that give them the right to win their chosen markets.

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