E-COMMERCE

Whitepaper

Should you sell direct?

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E-Commerce

SHOULD YOU SELL DIRECT?

Overview

Traditionally, consumer products manufactures have marketed their products though the normal retail customer channel, or in many cases through company owned brick and mortar stores. Companies with strong brand images have been able to successfully market in both spaces through line exclusivity offerings or protective pricing strategies. The evolution of global sourcing and declines in domestic manufacturing have some manufactures now behaving more like wholesale brokers where goods are designed domestically, but produced by overseas factories.

With a tough economy and constant margin pressure, retailers are self sourcing an increasing percentage of goods. In some cases from the very same overseas factories contracted by the traditional brand manufacturers. The retail private label market is here to stay, and growing quickly as retailers chase higher margins and a competitive edge in the marketplace. This is limiting the brand manufacturers' shelf space and brand exposure. Add into the mix the growth of internet retailing and emerging mobile technologies and the challenges become more pronounced.

According to Forrester and Gartner, despite the rapid growth of online commerce, an estimated 90 percent of manufacturers do not sell online and 66 percent identified channel conflict as their single biggest issue hindering online sales efforts. However, results from a survey show that click and mortar businesses have an 80% greater chance of sustaining a business model during a three-year period than those operating just in one of the two channels. Among others, the reach will be enhanced by creating another selling channel.

Manufacturing has changed, retailing has changed, and consumer buying patterns have changed. Is it time to change the way you sell your merchandise?

The e-commerce market

Direct sales by consumer-brand manufacturers are one of the fastest-growing areas of online retail, increasing almost 13% in 2008, according to Vertical Web Media, a Chicago-based research firm. Manufactures such as Procter and Gamble, Levi Strauss & Co, Mattel, Ralph Lauren, and Columbia Sportswear are now positioning themselves as retailers with revised and revamped consumer friendly websites. "There is no question that the customer around the world increasingly wants to shop online, and those who do tend to be more valuable customers for us, particularly if they also shop at our brick-and-mortar stores," T. Farah of Ralph Lauren told analysts.

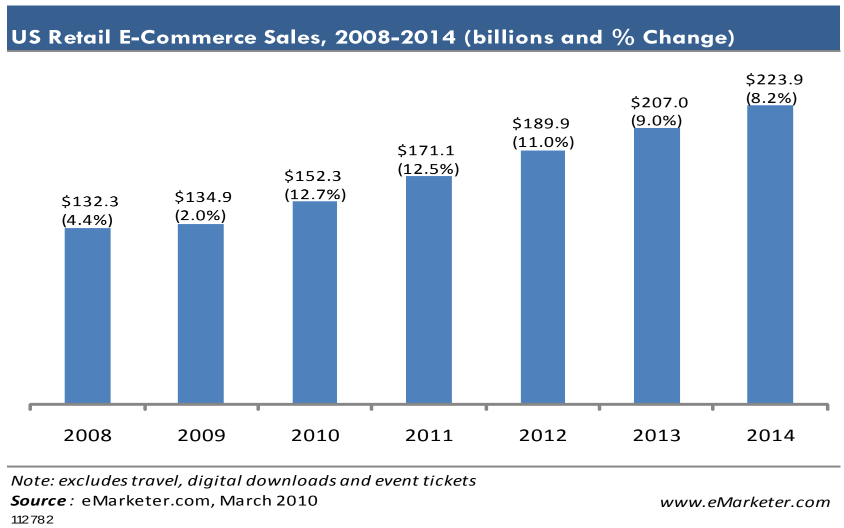
Online Sales of the Top 500* US Retail Website, by by Company Type, 2008 (billions and % share)

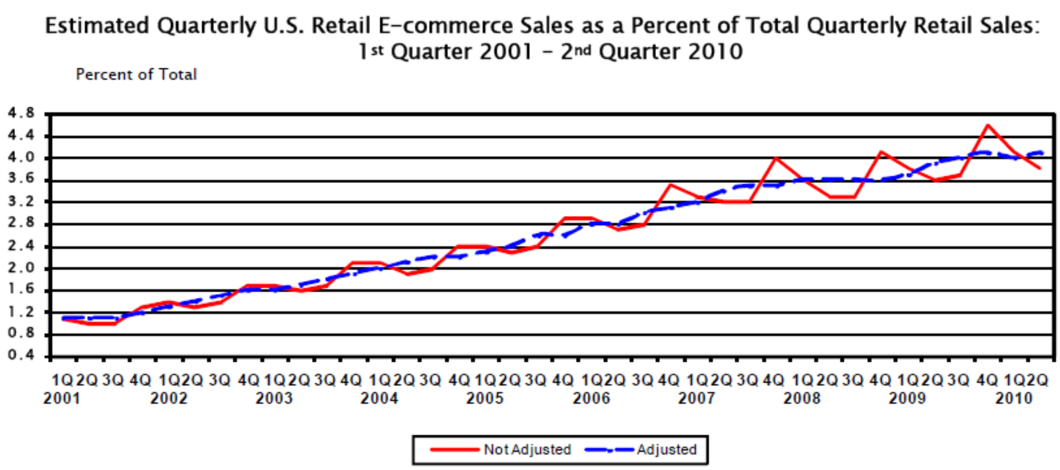
	Online sales	% of total
Retail Chain	$45.11	38.9%
Virtual (web only)	$36.84	31.8%
Catalog/call center	$19.90	17.2%
Consumer brand manufacturer	$14.00	12.1%
Total	**$115.86**	**100.0%**

*Note: numbers may not add up to total due to rounding. *ranked by online sales*
Source: Internet Retailer, *Top 500 Guide May 2009

www.eMarketer.com

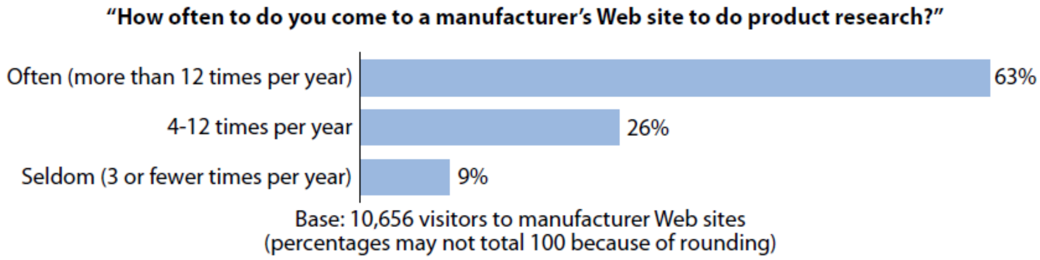
After 2 subpar years of growth, US retail e-commerce sales in 2010 (excluding travel) will climb to 12.7% on volume of $152 billion according to eMarketer. This follows the US Census Bureau's release showing that online sales in Q4 2009 grew by 14.6% over a year earlier, the biggest gain in 8 quarters. Online sales growth outperforms total retail growth because shoppers are moving more of their purchases from stores to the Web to take advantage of lower prices, convenience, and selection.



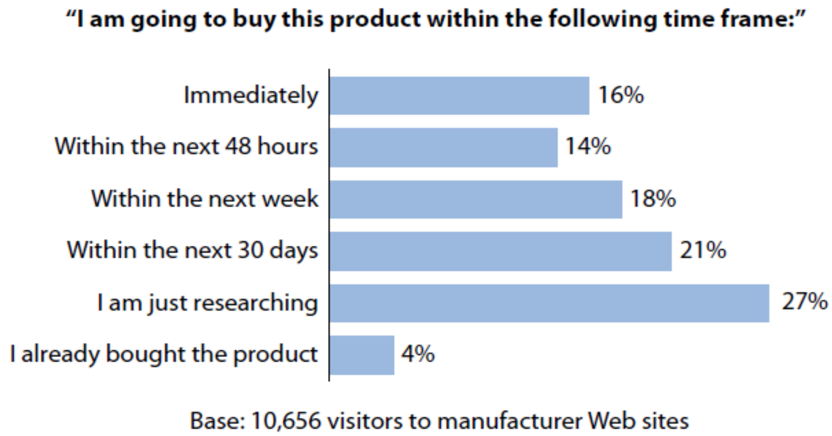


Manufacturer sites are already established as the trusted resource for product information. Forrester Research reported that 77 percent of consumers expect manufacturer web sites to have the best product information and 75 percent say they should be useful for post-purchase information. Because of this existing mentality of trust, manufacturers are finding themselves in a position to influence sales and customer satisfaction in a way that never has been available to them before.

Visitors to manufacturer Web sites believe that information about products is most reliable and of the most value. In a recent Forrester research survey respondents often made the manufacturer Web site the first stop in the shopping process, which begins with gathering information. In addition to visiting manufacturer sites first, consumers also visited these sites often. The vast majority — 63% of all respondents — said that they visited manufacturer Web sites more than a dozen times per year. 69% indicated that they were going to make a purchase in 30 days or sooner.



Source: Channel Intelligence



Source: Channel Intelligence

Channel conflict is a problem that many manufacturers see as a consequence of devising an online sales strategy. Drastically lower transaction costs and higher margins make Internet-based direct customer sales irresistible. While companies fret over alienating their resellers, they risk losing valuable time and market share to aggressive competitors that move to become online distribution fixtures. These simple economics lay at the heart of channel conflict. 66 percent of the consumer goods manufacturers surveyed listed channel conflict as the chief barrier to online selling according to Forrester. However, the fact of channel conflict appears to be inevitable as more companies move to direct to consumer marketing.

The Private Label Market

As economic conditions have become more demanding, manufacturers have seen their traditional retail client incorporate more profitable private label goods. In many cases these are being sourced by the retailers directly, cutting the consumer products manufacturer out of the picture. Private-label goods accounted for 22% of consumer-packaged products sold in the U.S. in 2009, up from 20% the year before, according to The Nielsen Co.

In the consumer packaged goods industry, the worldwide share of private label merchandise is expected to increase to 22 percent by 2010. By 2020, with increasing globalization and consolidation of retail, private label share should hit the 25 to 30 percent range. In fact, Western Europe is expected to reach the 30 percent mark by 2010.[1] And this development is not restricted to packaged goods--witness the success of private labels in other industries. For example, the share of private labels in U.S. apparel is predicted to increase from around 40 percent today to 60 percent in 2020. By 2010, an additional $100 billion to $200 billion per year will be lost that otherwise would have gone into the pockets of brand manufacturers.

[1] Nirmalya Kumar & Jan Benedict E.M. Steenkamp , Are Brands dead?, Entrepreneur, July –August 2007.

The growing importance of private label product to leading retailers is undeniable. These products are continuing to generate more growth than traditional national brands among major chains for nearly every category. Perhaps more importantly, more than half of all consumers believe that retailer-sponsored products are "at least as good as" nationally branded products and 48 percent say they actually prefer and seek out private brands.

Leading retailers of nearly all but the smallest sizes are investing more of their time and marketing dollars in the development of "private label" brands. The goal of this increased focus is both a growth (loyalty building) and survival tactic (owning an equity or line of products that differentiates them from larger competitors). Most retailers are either in the process of refining their "own brand" strategies or focusing on positioning their lines to maximize loyalty, competitive differentiation and market share.

Process and System Challenges

Even though the business case is overwhelming that the e-commerce market is growing and online sales becoming more prevalent, the many challenges to entry must be considered. Manufacturers who sell online don't just need to become web merchants, they need to become retailers, and that presents some interesting and often sticky strategic issues. The key challenges that must be met in this environment are listed below.

- **Product offering and pricing decisions -**There are key decisions to be made around the online offer. The whole assortment or an edited version? Exclusive products or just clearance and overstock items? And then there's pricing. Will they sell only at MSRP or discount readily based on promotions? Is the same promotional pricing available to the retailers?

- **Product information -** As mentioned previously, consumers expect that product information from the brand manufacturer is the most complete. Is it "retail ready" and orientated towards selling products to end users? Many manufacturers find that their product images and copy are geared towards product spec manuals for retail buyers vs. online shoppers.

- **Customer service -** Discreet processes, systems and people will be needed for e-commerce. When the end consumer calls customer support, will the manufacturer have the internal staff to efficiently handle the call? Order status, warrantee information, returns processing, complaint handling, escalation policy etc will all be required to assist the consumer.

- **Fulfillment -** Separate processes and systems may need to be set up to effectively manage consumer shipments and returns. Is the distribution center prepared to handle increases in single order returns? Are there inspection, repair and re-classing of goods processes already in place in the returns area? Is the fulfillment center well integrated into package shipment vendors and staffed for increased package shipment volumes? To support B2C orders a warehouse needs to support 1-Day, 2-Day, ground and overnight shipping (maybe international); boxes and packaging for direct-to-consumer is different than B2B and returns processes need to be thought through.

- Inventory Management – The brand manufacturer will now have to provide an accurate and timely "available to sell" quantity by SKU to the web front end. The frequency will vary from daily to several times and hour depending on the business. The questions to ask are:

    - How much to show? (Do you want to expose an overstock situation?)

    - What is the floor? (Under how many pieces do you consider too risky to show?)

    - Do you segregate the web store inventory? If so, what is the impact to your warehousing solution?

    - Do you buy to a forecast for web sales and is it included in your overall demand forecast?

- **E-commerce backend systems** – While choosing the best web front end partner will likely be a key decision for the manufacturer's online project, equally important is the suite of supporting systems (many of them possibly in "legacy" condition) that will need upgrading or readied for integration. ERP, Order management, CRM, WMS systems, and Business Intelligence tools to name a few will be asked to execute an entirely new selling process.

Resources - Manufacturers often do not have a dedicated e-Commerce groups that can focus on the channel, hindering execution of consistent initiatives that could maximize the company's overall multichannel efforts and bring a truly customer-centric approach to the Web. IT staffs that are geared to support legacy ERP processes will need new training and skill sets to achieve success.

Conclusion

Manufacturers who sell directly to consumers risk losing their wholesale accounts, as well as tarnishing their reputation as a reputable manufacturer. Over the past few years, many manufacturers have struggled with the notion that they are doing all the legwork (product development, purchasing, warehousing, shipping, etc.) while drop-ship retailers are reaping all of the benefits oftentimes at a higher margin than the manufacturer themselves make. Retailers are aggressively pursuing private label products that cut the brand manufacturer out of the retail space altogether and that market is growing rapidly. We are finding that more and more, manufacturers and distributors are turning to retail e-commerce websites in an effort to expand their customer base and increase sales. Whether you should sell direct or not, you as a manufacturer or distributor need to ask yourself if you are ready to do it. There are significant sales and margin wins in that space, but it takes a serious investment of human resources, IT infrastructure, and well thought out marketing plan to be successful.

About the Vision Suite

All of Jesta I.S.' solutions are real-time, web-based applications that automate complex business processes, manage workflow and deliver exception-based business intelligence to our clients. Each solution is internationalized and modular allowing our clients to use only the modules they need. Jesta I.S. is committed to continuous product development based on customer feedback as well as internal and external market analysis.

From retailers who source their own goods, to manufacturers who are selling direct to the consumer, Jesta's Vision Suite provides organizations with end-to-end solutions for ERP, Retail, Store Operations and Supply Chain Management. The Vision Suite includes; Vision Merchandising, Vision Financials, Vision Planning, Vision Store, Vision E-DOM (Electronic Distribution Order Management), Vision SCM, Vision Sourcing & Demand Management.

Vision Sourcing and Vision Demand

As Vision Sourcing and Vision Demand Management create business value by efficiently managing the balance of supply and demand. Through better business practices, improved visibility and process management organizations can gain greater control over the procurement of raw materials, full package sourcing, accurate inventory and allocation of available merchandise and much more. These applications are specifically designed to meet the requirements of the entire supply chain as well as the complexities associated with an extended enterprise. Vision Sourcing & Demand Management handles even the most complex supply chains including a mix of international and domestic production for organizations that require quick turn-around orders, and enables management of sourcing locally even when production is abroad.

About Jesta I.S. Inc.

Jesta I.S. is a leading supplier of business solutions leveraging more than 40 years of expertise in supply chain management systems for manufacturers, distributors and retailers primarily in the soft goods and specialty industries worldwide. Jesta I.S. is recognized for its expertise, innovative products and services and its commitment to evolving business solutions in today's rapidly changing business world. Jesta I.S.' solutions process essential business management information for well known industry leaders including Perry Ellis International (NASDAQ: PERY), Puma AG (XETRA: PUMV.DE), Genesco Inc. (NYSE: GCO), Town Shoes Limited, Cole Haan, Haggar Clothing Co., Cavender's Boot City and DSW Inc. (NYSE: DSW) as well as many others.

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