SMARTER PERSPECTIVE: RETAIL

How Modern Retailers Are Evolving Their E-commerce Platforms

By Dustin Miller

January 2025 This article examines a number of ways that retailers are changing their ecommerce strategy in the modern ecommerce environment, as a "growth at all costs" mindset gives way to a larger focus on bottom-line profitability.

INTRODUCTION

In 2024, almost every retailer imaginable, with very few exceptions, has an e-commerce presence. Current trends and forecasts point to the continued growth and importance of e-commerce as a sales channel, with e-commerce sales expected to grow 8.8 percent in 2024 and total U.S. e-commerce sales expected to grow 53.8 percent between 2024 and 2029 to reach $1.9 trillion in total sales by 2029. In 2024, 20.1% of all retail purchases are expected to take place online, a figure that is forecasted to increase to 22.6% by 2027.

However, in the current economic and financial environment, retailers' focus has shifted from e-commerce growth at any cost, to having a rational, sustainable e-commerce channel that does not become a net drain on the business's profitability. Identifying opportunities to reduce costs and optimize e-commerce operations while maintaining a compelling customer value proposition and broad reach will be critical in determining which retailers can create a successful and profitable e-commerce model and which will be running money-losing e-commerce platforms that will ultimately hurt the bottom line. This article will explore some key areas where opportunities exist for retailers to optimize their e-commerce channels.

E-commerce Operations: Ship-From-Store Versus Centralized Distribution Center (DC)

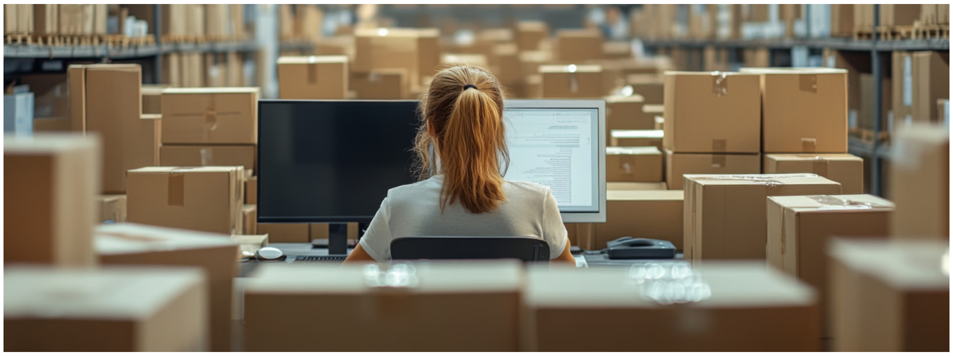
In the early days of e-commerce, most retailers utilized large centralized distribution centers to support their e-commerce operations. Many still follow this approach today. However, due to significant improvements in the software available to manage inventory and sales transactions across multiple sales channels, and the rising cost of shipping, among other expenses, many retailers are experimenting with a different distribution model: ship-from-store.

Ship-from-store refers to e-commerce orders being routed to brick-and-mortar retail stores and having store associates pick the inventory from floor or back stock, package the order, and ship it out from the store, while centralized DC fulfillment refers to e-commerce orders being routed to a dedicated distribution center which fulfills orders using a dedicated warehouse fulfillment team and dedicated inventory.

A ship-from-store model offers several potential advantages over a centralized DC. Ship-from-store can allow retailers to reduce markdowns by opening units in stores to purchase by e-commerce customers, eliminating situations where an item is sold out on the website while units linger in certain stores and are ultimately marked down. Ship-from-store can also allow retailers to reduce expenses by eliminating costly warehouse space and dedicated e-commerce fulfillment staff and instead use existing retail store space and personnel to fulfill e-commerce orders. Ship-from-store has also allowed some retailers to reduce overall inventory levels by creating flexibility to sell units across multiple sales channels and eliminating the need to hold redundant inventory in a centralized DC and stores. Finally, ship-from-store can reduce costly shipping expenses by allowing retailers to ship orders from a store as geographically close to the end customer as possible rather than a centralized DC, which may be on the other side of the country.

On the other hand, ship-from-store has some challenges and drawbacks. Successful ship-from-store fulfillment requires a Company to have sophisticated software with accurate inventory visibility across all stores and DCs and sophisticated algorithms to route orders to the optimal fulfillment location. Retail staff will have to be properly trained on e-commerce fulfillment, and retail staffing levels must be monitored and adjusted to ensure that e-commerce operations do not negatively impact the ability of retail associates to serve in-store customers. Retailers will also need to closely monitor fill and on-time shipment rates to ensure every store is able to handle the e-commerce volume being routed to it.

Many large retailers who are experimenting with ship-from-store are utilizing a hybrid approach, maintaining some centralized distribution while also shifting a portion of e-commerce volume to ship-from-store fulfillment. This approach has allowed them to reduce their warehouse space and payroll expense while maintaining some centralized distribution center capacity to absorb e-commerce volume during peak seasons, handle larger orders, stock additional products not offered in stores but are available on the ecommerce website, and process returns.



E-commerce Shipping and Returns: Free, or Fee?

In the past, it was very common for retailers to offer free shipping and free returns on most e-commerce orders to entice customers to shop with them, which reflected an emphasis on growing top-line e-commerce revenue and gaining market share over profitability. However, in recent years, many of the largest retailers have begun to rethink this approach and have begun to charge shipping and return shipping fees on a significantly larger portion of their orders.

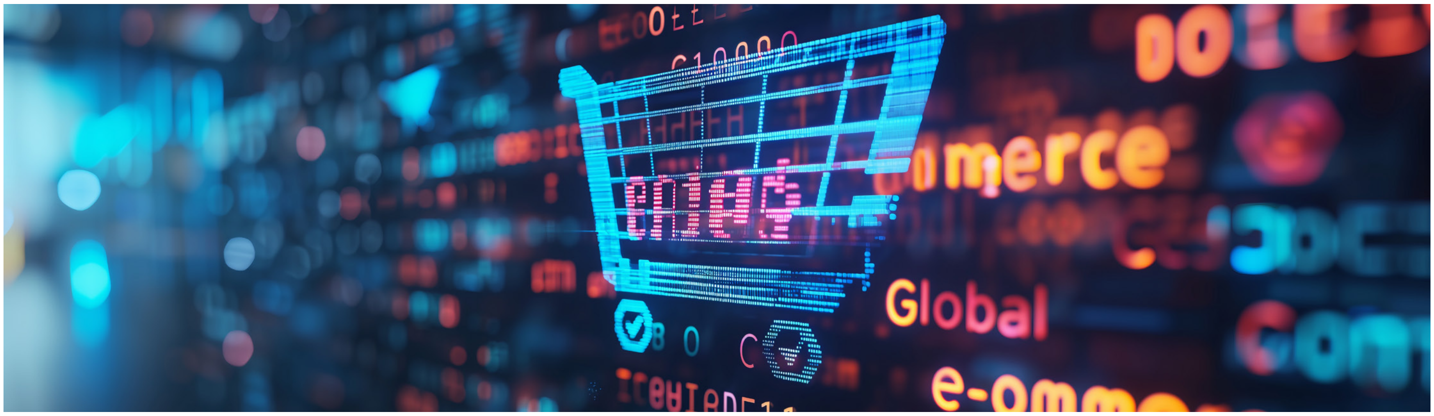
Many retailers now require a minimum spend threshold for free shipping, for example, offering free shipping on orders over $100 and charging a shipping fee for orders below that threshold. Combined with more retailers charging for return shipping, this approach incentivizes customers to spend more and return less. In addition, many retailers will modify the minimum spend threshold as part of their promotional strategy, offering "free shipping on all orders" or a lower spend threshold to qualify for free shipping during certain periods as part of sales and promotions.

A large number of retailers have also added return shipping fees in recent years, and the majority now charge a return fee for at least certain types of returns. In recent years, retailers including Amazon.com, J.C. Penney, Dillard's, Macy's, Zara, J. Crew, Abercrombie, and American Eagle Outfitters, among many others, have made news by implementing fees for certain mail-in returns. In addition, some retailers now offer the option to return in-store for no fee versus charging a fee for mail-in returns. This saves on return shipping costs and generates additional store traffic and revenue, as a portion of customers coming into the store to drop off a return will browse the store and make additional purchases. Some retailers have also announced measures to identify customers who make an unusually high number of returns or otherwise abuse the company's return policy and restrict their ability to make online purchases or qualify for free returns in the future.

Overall, these trends toward passing along shipping expenses to the customer and using return policy to incentivize customers toward preferred return methods reflect an increased awareness of the impact of shipping expenses on e-commerce profitability.

Marketplace Selling: E-commerce Expands Beyond the Retailer's .com

There is an 800-pound gorilla casting a shadow over the entire e-commerce space – Amazon.com. Amazon accounted for 37.6% of U.S. ecommerce spending in 2023 and is expected to surpass 40% in 2024. In addition to Amazon, a number of other large online marketplaces have gained prominence, including Walmart.com, Target Plus, eBay, TikTok Shop, and Instagram Shop. Modern retailers will have to evaluate these channels to determine if they should be selling their products on popular marketplaces in addition to their own websites.



Many brands feel they have little choice but to list their products on Amazon. For one, market research has shown retailers that a certain percentage of customers are highly inclined to search for any product they plan to buy online on Amazon in order to price check it as well as read descriptions and reviews. Additionally, suppose a brand does not list its own products on Amazon. In that case, it is highly likely that a third-party seller will step in and list the Company's products on Amazon, creating the risk of counterfeit products, poor customer service, and other potential issues reflecting back negatively on the Brand. Despite these strong incentives to sell on Amazon, many retailers have found that Amazon's hefty fee structure and rigorous seller compliance requirements make it challenging to use Amazon as a profitable sales channel. Retailers will have to continue to evaluate the trade-offs of Amazon selling and stay aware of any changes to Amazon's seller policy and fee structure to stay relevant in the modern e-commerce environment. (Hilco has written a great article on Amazon's different seller programs and the implications for secured lenders for those interested: https://hilcoglobal.com/perspective/nuanced-understanding-of-amazons-liquidation-environment-drives-new-appraisal-approach/).

In addition to Amazon, there area a host of other marketplaces that retailers and brands can consider selling on: Walmart.com, Target Plus, eBay, Instagram Shop, and TikTok Shop to name a few. It would take too much time to go into all of these in detail, but retailers are experimenting with selling across all of these channels, and success will come down to developing a deep understanding of the true expense of using these channels, what their best use case is (Ebay to sell past-season product, seconds, or returns; Instagram and TikTok Shop to generate viral interest in specific products, etc.), and ultimately arriving at the optimal set of marketplace channels for a particular business and product line.

Conclusion

E-commerce will continue to be a massive and important sales channel for retailers in the foreseeable future. However, in the current economic and financial environment, many retailers are shifting their focus from growth at all costs to finding a profitable, sustainable business model. A large part of this shift will involve identifying operational efficiencies in distribution networks, and finding ways to manage shipping and return expenses. At the same time, retailers are faced with the prospect of additional complexity beyond selling through their own stores and websites due to the prominence of third-party marketplaces, which are continuing to grow in size and importance in the e-commerce landscape. Modern e-commerce is still in flux, and retailers who can best adapt to the shifting landscape will be the next big e-commerce winners.

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