

E-Retailing Insight Measuring Webstore ROI *December 16, 2008*

In our work with client retailers, we have all too often observed webstore operators that are slow to complete the basic content needed to launch their webstores or to update content in their established webstores. Basic content that generally includes product descriptions, product images and image galleries, product associations, shopping pathways, customer policies, and other product and general information content. We have found these delays in getting content prepared to be both perplexing and challenging.

Provide adequate resources to avoid delay. From our efforts in support of our client retailers while getting their webstores open for business, we have come to realize that the foremost reason for delay in completing content has been and continues to be the thin allocation of resources – time, money, and people – that retailers, both new to the webstore world and experienced operators, are investing in content creation. This seems odd to us. We can be sure that these retailers would not delay opening their storefront locations at the scheduled time. Nor would they delay in getting needed merchandise to their sales floors.

As has been reported widely, the majority of North American webstore retailers do not hold their webstore operations to the same degree of financial account as they hold their other operating units. We surmise that this lack of financial scrutiny is a by-product of retailers not fully, effectively, and finally defining the role, responsibilities, and objectives of their webstores within their overall business operations. Which is to say that a large number of retailers may not be doing a proper job of first preparing a business plan to guide the development, implementation, and operations of their webstores. And, as one immediate consequence of inadequate planning, webstore projects may not be allocated sufficient resources to get the webstore open and operating in a timely and efficient manner.

Proper planning is essential. We believe this lack of adequate advance planning to be a serious mistake and we counsel every retailer who is operating webstore or is looking to open a webstore to immediately develop and follow a webstore operating plan that includes a set of webstore financial and operating performance standards. Financial and operating performance standards start with creating initial and ongoing webstore development expense budgets and annual webstore operating budgets.

With budgets in place, the operators can then determine operating performance standards that will combine to ensure the webstore achieves its financial targets. Webstores, along with every other web-integrated commercial enterprise, offer ideal environments for performance measurement – both financial and overall customer interaction. In this discussion, we are going to focus mainly on one fundamental performance measurement: ROI - return on investment.

Set performance objectives. Before building a webstore development budget, retailers must first establish financial performance objectives and operating standards for their webstores. Questions to answer include: What are the webstore's direct revenue performance targets – sales completed

entirely through the webstore? What are the indirect revenue performance targets – sales driven by the webstore but completed offline? What are the gross profit targets for the webstore? What are the direct operating expenses for the webstore, including webstore content management, online advertising, site hosting, data storage, customer shipping, payment processing fees, and other direct expenses? What is the webstore's profit contribution target within the overall enterprise?

With these financial objectives established, retailers, using readily-available industry performance benchmarks, can then develop an initial set of operating performance standards. Questions to answer in this stage of planning include: What is the planned average sale for transactions completed through the webstore? What is the target closure rate on traffic through the webstore? What amount of traffic, considering average sale and closure rate, does the webstore need to achieve its revenue target?

Experienced retailers will recognize this discussion closely parallels the detailed planning that goes into other business development initiatives. And this, we believe, sits at the heart of the matter. Retailers would not let leased space sit idle for one day longer than it would take to finish and fixture the space, install inventory, and get the doors open to paying customers. Why should opening a webstore be any different?

Investing in a webstore. What are the factors that go into the “investment” side of the webstore ROI equation? Start-up costs for a webstore fall into two parts. The larger part is the costs for planning, designing, and creating content for the webstore. In this, and following on our earlier comments, our observation has been that webstore operators are ready and willing to make hard-dollar investments in professional webstore design and development while badly discounting the need for investment in content creation. The second part of web start-up costs is the costs for establishing the webstore on the Internet. These costs typically include contracts for site and data hosting, domain name registration, initial search engine optimization, and an online marketing campaign in support of the webstore opening.

Costs associated with developing a webstore represent a longer term investment for the webstore retailer. The ROI calculation for this investment should encompass at least two and as much as a three year operating period. By comparison, the costs associated with establishing a webstore on the Internet represent an investment in near-term operating activity with an ROI likely calculated on no more than the first three to six months operating results of the webstore. Unlike webstore development costs, the costs of launching a webstore are ongoing as regular operating costs. Therefore ROI calculations on these investments encompass established operating timeframes.

Webstore ROI. Calculating the full return on investment from a webstore involves a number of “returns” to the retailer from a webstore's operations. The first return, of course, is the profit contributions to the enterprise from sales completed through the webstore. For most retailers, however, this is not the largest portion of the overall return from the webstore. At least as important is the gain to the company from sales supported by the webstore but completed offline. While industry reports suggest that offline sales influenced by a company webstore may be as much as 25% of all sales, we suggest that a more conservative measure be used - perhaps an amount of sales equalling 1.5 or 2 times the sales completed at the webstore. Nonetheless, the return to the company from webstore-influenced sales can be substantial.

In addition to revenue-driven gains (returns), opportunities exist to achieve gains through integrating a webstore into other areas of the enterprise's retail operations. These gains will often take the form of

operating cost savings rather than sales gains. Examples include installing Internet kiosks on retail sales floors that are locked on the webstore. This allows in-store customers to get detailed product information on their own, creating opportunities to improve floor staffing efficiencies and expedite customer throughput.

Another important opportunity for gain is to use a content-rich webstore to support online product and customer service training for the enterprise's retail employees within a secure training sub-site. This facilitates self-paced and group training for new employees, and serves team members wanting a quick refresher on specific product or other information. It is easy to calculate the savings in training costs from improved efficiencies resulting from webstore-content driven training. These are only two examples of cost savings that can add to the return on investment from a full-functioning webstore. There are dozens more that creative retailers are discovering and exploiting.

Quick ROI calculator. As we have discussed there are a number of inputs for correctly calculating the return on investment of a webstore. Here is a basic ROI formula for webstore retailers wanting to introduce webstore ROI measurement into their enterprise:

$$\text{ROI} = \frac{\text{R}^1 + \text{R}^2 + \text{R}^3}{\text{INVESTMENT}}$$

where R¹ = Webstore net profit contribution to the enterprise;

R² = R¹ x 1.5 (or higher factor) as webstore contribution to offline net operating profit;

R³ = Offline operating cost reductions, e.g. in-store Internet kiosks, employee training.

Six key takeaways from this discussion.

1. Do a business plan and financial budget before beginning a webstore development project.
2. Set webstore operating performance objectives and continually measure webstore performance.
3. Include both hard and soft costs when budgeting development of a webstore.
4. Allocate sufficient financial and manpower resources to complete webstore content creation on schedule.
5. Financial gain for the enterprise from webstore operations can include as much or more offline gain as the gain from a webstore's direct profit contributions.
6. Include all "returns" when measuring webstore return on investment.

We invite your comments on this discussion about calculating webstore ROI. Please write us at e-retailing-insights@jammicron.com. Thanks!

Copyright 2008

E-Retailing Insights is a white paper series from Jammicron Technology, aimed at helping retailers get the latest information on Internet retailing. For more information, please visit:

www.jammicron.com