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How Bricks-and-Mortar Companies Can Make It on the Internet

How do you turn your real-estate investments into a thriving Web storefront? Make sure you have a strategic approach to reaching your customers.

by Victoria Griffith

Ask anyone to cite the strongest brands on the Internet. Amazon.com, E*Trade, Yahoo! and America Online will top the list. The world's most famous brands — Coca-Cola, McDonald's, Bud Light — will not make the cut, nor will high-technology companies with big commitments to the Internet, such as the Microsoft Corporation or AT&T. The most recognized brands on the Internet exist, well, only on the Internet itself.

In the early days of the World Wide Web, newcomers just elbowed their way in. They did not have advertising budgets — indeed, many did not have budgets at all. They survived on the buzz created first by Internet surfers, then by the media. Traditional marketers just did not see the point of mounting a challenge.

All this is changing — and fast. Offline businesses have discovered cyberspace. Clothing retailers that already had well-developed catalogue businesses, such as Lands' End, The Gap and Eddie Bauer, have led the charge. Barnes & Noble Inc., seemingly content at first with the success of its superstores, has finally taken on Amazon.com Inc., the ubiquitous book, video and music Internet marketer. Wall Street seemed at first to smirk at the E*Trade Group, which invited investors to make their own trades on the Internet. Then the Charles Schwab Corporation jumped at the challenge and now leads with 27.4 percent of the nation's online market, according to C.S. First Boston. Schwab averaged 93,000 trades a day in the fourth quarter of 1998 and has 2.2 million online accounts. Other brokerages, such as Merrill Lynch and Quick & Reilly, are scrambling to catch up. In the fourth quarter, C.S. First Boston calculates, there were 340,000 Internet trades a day.

All companies, competing now with tens of thousands of Web sites, need more than a buzz to create a significant presence. Word-of-mouth is

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no longer sufficient to get the word out about a Web site; traditional advertising plays a large role. Television, radio and print are inundated with advertisements for Web sites.

"People who seem to be developing strong brands are just plain everywhere, with their Web site featured on television advertisements, radio and stationery," said Doris Ehlers, a partner at the research company J.D. Power & Associates. "You have to do that."

The cost of creating a Web presence is escalating quickly — ranging from $1.5 million to $3 million, according to Forrester Research. Competing with an established Web presence can push those figures into the stratosphere. Barnesandnoble.com, for instance, will spend $60 million on Internet advertising this year. Cyberspace entrepreneurs may be left in the dust by traditional offline businesses with deep pockets — at least those willing to not only spend big but also change their brand-building strategies. These companies, however, face enormous barriers.

INVESTMENT EXPECTATIONS

Investors have different perceptions of offline and online companies. They assume Barnes & Noble will continue to be profitable; they expect Amazon.com — which lost some $46 million in the fourth quarter of 1998 alone — will be in the future. Barnes & Noble had a price-to-earnings ratio of 45.86 in January; America Online's was 381.94 and Yahoo!'s 35,000. The combined market capitalization of America Online, Yahoo! and Amazon.com in mid-January was $3.5 billion, 41 times the companies' combined earnings.

Because the Internet requires huge up-front investments in order to build an effective presence, companies can expect early losses before the kinks are worked out. A halfhearted commitment to the Web is likely to fall flat, as Bloomingdale's and Macy's discovered when they offered only a few products online to customers used to a vast array of choices. Both retailers had to relaunch their Web sites with wider selections and easier navigating.

One strategy used by bricks-and-mortar companies to keep the uncertainty of Web income from smudging the bottom line is to create separate Internet companies — the route taken by Barnes & Noble in October 1998. The Web company — Barnesandnoble.com — has two parents with deep pockets: Barnes & Noble and Bertelsmann A.G., the German

media giant that paid $200 million to get a 50 percent interest in the project and plans its own challenge to Amazon.com in Europe.

"Spinning out its Web division may be the best decision Barnes & Noble made regarding the Web," said Rob Parker, head of marketing for CDnow, a large, Internet-based music vendor. "Both investors and people in the new company can now get on with the business of building a digital brand."

ADVERTISING IS NOT ENOUGH

In the early days, most Web sites were built around the Internet's novelty. The Web site for Coors beer had a virtual bar in which customers could order a brew and chat with others at the site. American Cybercast, borrowing from Charles Dickens, hosted weekly soap operas. Both sites are now defunct. According to America Online, most users today log on for one of two reasons: to get practical information such as the latest weather, traffic or news report, or to shop. People are far more interested in avoiding a trip to the mall than in quaffing an online brew.

In fact, e-commerce has grown much faster than anyone anticipated. Researchers at Jupiter Communications report that Web sales reached $2.5 billion in 1997; mushroomed to $7 billion in 1998, and are expected to reach $12 billion this year and $41 billion by 2002. At least for now, these sales seem to be coming at the expense of retail stores. In December, some shopping malls in New England complained that they had lost as much as 5 percent of the holiday business to the Internet.

Part of the spurt can be attributed to companies that now see that a billboard ad is just not enough — sales must occur. For instance, Clinique, the cosmetics company owned by the Estée Lauder Companies, was surprised to find in a survey it conducted on the Web last year that 80 percent of the people logging on to its informational site said they would like to buy the products online. Clinique responded by creating a virtual store.

The need to sell in cyberspace has challenged many industries. Some manufacturers have no experience in selling directly to consumers; others see one-on-one relationships as simply impractical. (Would you log on to the Coca-Cola site to order a six-pack; Gillette's for razor blades, or Perdue's for a roaster?)

Unsure of what to do, many companies have stuck to the old formula of gimmicky sites that yield little real value to the consumer. Marc Johnson, an analyst with Jupiter, names Coke's site as one of the worst on the Internet. The company features games and cute sayings such as "Nice work Houdini," but not much more.

"They're living in the past with an emphasis on childish games, and no utilitarian benefit," Mr. Johnson said.

Consumer products companies could leverage their Web presence, however, by giving out coupons and sending users through a point-and-click system to virtual grocery stores such as Peapod and Netgrocer. Even more important, the consumer products companies could work together with online stores to make sure their products are listed often and prominently as customers move through the virtual aisles.

For some manufacturers, selling directly to the consumer has obvious benefits, while for others, just providing exhaustive information about their products can help sales on the showroom floor. Vehicle sales are one example. Manufacturers, by providing good information on their Web sites, and links to dealerships and leasing companies, can capture and engage a large audience.

It sounds simple, but here is an example that shows it is not. J.D. Power reports that only 16 percent of those logging on to a car site get referred to a dealer. Once buyers do make it to the dealers' sites, another 83 percent drop out of the process early on, put off by a lack of responsiveness and up-to-date information. "They want to see a photograph, car description and price, but all they get is hours of opening and a map that shows how to get to the dealership," said Ms. Ehlers of J.D. Power.

Some manufacturers are understandably afraid of killing the goose that lays the golden egg. For The Gap, the Web site is just another tool to help customers place an order. For Tommy Hilfiger, however, which sells most of its clothing through big-name department stores, Web sales could cannibalize store sales, thereby straining relations with its retailers. But will that happen?

These fears may be exaggerated. Take the example of Clinique. The company was at first reluctant to sell its cosmetics online, nervous about

Point and Click Your Way to Success

The technology for building a Web site is the easy part; it's the strategy that makes many companies stumble. Here are a few guidelines for creating an effective Web presence.

- Make sure all senior managers are on board and intimately involved in the Internet strategy. The setup and running of the site may be centralized, or even outsourced, but executives should know exactly what the site is trying to do and how well it works from a practical standpoint. A site with glitches should not be allowed to launch, no matter how "cool" it is.
- Make technological improvements slowly. This may sound counter-intuitive, but many in the Web universe have older computer equipment and software and need ease of access more than they need bells and whistles.
- Guide customers to purchase quickly. Every extra click needed — and the concomitant delay — presents a chance of losing the customer.
- Try to protect existing distribution outlets, but do not worry too much about cannibalization. Chances are, you will find more new customers than you thought possible through the Web.
- If it seems a sweeping commitment to the Internet will hurt your share price, consider spinning off the venture as a separate company to take the first bruises.
- Leverage existing expenditures on brand-building as much as possible. A corporation's Web address should be listed on television commercials, stationery, shopping bags and receipts. Showroom floor sales people should be trained to mention the Web site to customers.

its crucial department-store relationships. Mindful of this, when Estée Lauder, its parent, decided to take the plunge, it contacted its distribution outlets and explained what it was trying to do. At the same time, Clinique offered to help department stores in setting up their own sites. The company managed to convince the stores that consumers were not facing an either/or situation.

"We're happy that our Happy perfume is the No. 1 seller on both our site and at Macy's [site]," said Angela Kapp, vice president of special markets at Estée Lauder. "If consumers come to our site, they should be able to buy. But if they're at Macy's buying a sweater and also want our perfume, they shouldn't have to switch sites. Obviously the stores weren't thrilled with the idea of [us as] a manufacturer doing something on our own, but they've accepted it."

Clinique is now enjoying a higher margin on Web sales than it does in department stores. The company has also been surprised at how little cannibalization has actually occurred. "We know that at least 20 percent of our online buyers are new customers," said Ms. Kapp. "And 41 percent of purchases are of products customers have never used before. This is adding to, not detracting from, our overall sales."

Corporations that have invested heavily in building a physical presence are understandably uneasy about turning their backs on bricks-and-mortar shops. To ignore this fixed overhead in favor of virtual shopping is frightening. Still, to succeed on the Internet, it must be done.

Managers who have built up online brands with independent companies dedicated to the Web say they cannot imagine doing it any other

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Yes, I Have No Bananas

During the course of three months in 1998, I logged on to the Web site of HomeRuns, the grocery delivery service run by a Boston-based company, for a terribly disappointing experience. Time after time, the screen would freeze at "check-out," leaving me unable to complete the order. I would call the company's help desk, which would complete the process from its end, but I was unable to check the final order.

As a result, I once received 30 boxes of Cornflakes (I had asked for three) and 11 bunches of celery. The company said it was having trouble with its new Web site, but was fixing the problems. After a half-dozen tries, I gave up. Friends said they, too, had been having trouble. Although they had been very enthusiastic users before the glitches began, many were reluctantly switching to a competitor, Peapod.

The incident shows the difference between branding online and branding offline. Problems with branding in the real world can be interpreted as an image problem. Consumers perceive that the company has failed to keep up with competitors on price or quality, or has just become "uncool." Yet HomeRuns never had an image problem. The company advertises itself, in flyers and in a test television commercial in Cambridge, Mass., as a friendly, price-effective service that delivers high-quality produce right to your doorstep.

Customers never questioned the truth behind this image, and in the midst of its Internet troubles still commended the service for its dependability. The HomeRuns trucks almost invariably arrived within the desired two-hour time frame; the produce was of good quality and sold at competitive prices.

Yet customers were still abandoning the service because the company had created an online branding problem. In the real world, intangibles such as name recognition and loyalty are important. In the virtual world, site efficiency and usability are key factors. The speed and ease with which consumers can purchase a product drive sales just as much as quality and price do. HomeRuns was losing business simply because its Web site did not work for a lot of customers.

How did such a branding lapse occur? At least some of the problem can probably be traced to the group's management structure and organization of responsibilities. Most of HomeRuns' senior staff comes from the group's parent company, the supermarket chain Hannaford Brothers. While they know the food world in and out and keep close tabs on inventory and personal service, they left the building of a new Internet site up to a group of "techies." The result was a Web site that looked great for some, but proved unusable to others.

"We made some mistakes when we launched the new system in July," said Alison Berglund, head of sales and marketing at the group. "One immediate hard lesson was that you can't move too fast with technology. Customers don't always have the latest browser." To its credit, the company has now loosened up its technology requirements to accommodate lower-end users, and its old clientele seems to be flocking back.

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way. "All the successful brands have come from cyberpioneers," said Mr. Parker of CDnow. "They didn't know the old rules. They were starting from scratch and had nothing to cannibalize. They also had no other business to distract them. Building up sales on the Web was the only business goal, and everyone in the company was committed to that."

In bricks-and-mortar companies, on the other hand, managers may be at odds with each other in their assessment of the Internet's importance. "Offline companies are not structured internally to effectively use the power of the Net," said Jim Nail, an analyst for Forrester Research. "In the Net world, all departments must work seamlessly together. In the real world, there may be independent points of pressure. Different departments may not have a history of teamwork."

Certainly, it has been a challenge for real-life groups to drum up enthusiasm for the new medium. This is not, as some would have it, a generational battle between computer-savvy youngsters and gray-flannel wheezers. Bob Pittman, president of America Online, has always stressed that the company is more defined by customer service than technology. A manager need not be a computer guru, but does need to be hooked into what people want on the Web.

WHAT THE CUSTOMER WANTS

To succeed, the top levels of a company must know what they have always needed to know: what their customers want, whether from a retail outlet or a Web site. Successful Internet companies know this. One common theme among successful Internet executives is a genuine interest in what happens in cyberspace. They go into their own sites, and competitors'

sites, on a regular basis, and actually try to purchase the products. They get friends and relatives to do the same and pay attention to informal criticism.

"Everyone at this company spends a lot of time on the Internet," said Mr. Parker of CDnow. "We know what's out there. The Net is not a part-time job; it's not something you just dabble in."

Successful Internet managers are obsessed with streamlining the process. They know how many clicks it takes to get to the point of sale, and how long it takes them to respond to e-mail. Last year, CDnow ran a test that measured exactly how many clicks it took to get online consumers to purchase. The group then worked on consolidating steps to eliminate the unnecessary work. "We got from 20 clicks down to 10," said Mr. Parker. "That gave us an immediate competitive advantage."

While it is not easy or cheap, bricks-and-mortar companies can build a presence on the Web. And as e-commerce expands, it will become increasingly vital for them to do so. In many areas, they hold a strong advantage over their purely online competition. Coca-Cola (which spends about $200 million a quarter on advertising) is still a far better-known name, worldwide, than Amazon.com. These companies already advertise in traditional media — television, print and radio — and can push their Web addresses for relatively little extra cost. They have years of experience in their business. They are big enough to influence suppliers.

Yet to build brands in cyberspace, bricks-and-mortar companies will have to let go of some of the thinking that has been holding them back. Senior managers must embrace the medium with gusto. They must overcome their fears of cannibalization and the loss of distribution channels. They must realize that interactivity on the Internet does not mean a fun game, but sell-through marketing. They must become closely involved in all aspects of the group's Web strategy. When this happens, the upstart Internet groups need to take note as the marketing giants awaken to the possibilities.

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