Mindtree

A Larsen & Toubro Group Company

Strategizing D2C Fulfillment for Legacy Brands

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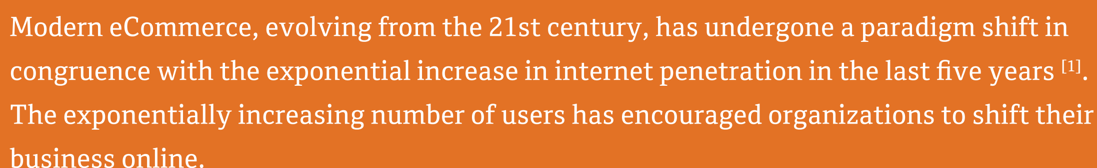
Welcome to possible



Modern eCommerce, evolving from the 21st century, has undergone a paradigm shift in congruence with the exponential increase in internet penetration in the last five years [1]. The exponentially increasing number of users has encouraged organizations to shift their business online.

The Covid-19 pandemic skyrocketed this business disruption in the eCommerce industry. The pandemic devastated the traditional offline commerce industry by bringing businesses to a halt through multiple and multi-variant lockdowns. In addition, people are now extremely reluctant to leave their homes to go shopping. Standard operating procedures for physical shopping have been severely impacted, and offline sales have plummeted with customers only daring to venture out to purchase essentials.

Going outside has been fraught with danger, and this has resulted in an exponential YOY increase in online discretionary spending. While grocery eCommerce has been a key beneficiary, the entire eCommerce landscape is currently undergoing a power boost, with online spending reaching $82.5 billion in May 2020 — a 77% increase from 2019 [2].

As an increasingly more number of users have started to prefer online shopping, the Direct to Customer (D2C) eCommerce model has now become the success mantra for businesses with its numerous benefits. It provides businesses full control over the user experience and supply chain, while removing intermediaries and increasing product margins for the sellers. By marketing and selling directly to customers, businesses are able to get more reach with significantly less overheads. This has compelled legacy commerce brands to optimize their eCommerce strategies, and in many cases, create an eCommerce strategy. Optimizing online profits by removing intermediaries and selling directly to customers from a web store is one of the top priorities in the new normal. In a post-Covid-19 world, this leads to better margins in addition to providing businesses greater control over marketing and sales strategies. In essence, it throws open full ownership of the entire ecosystem to businesses – from manufacturing and marketing to last mile deliveries.

This has changed the goalposts for legacy brands such as Nestlé to move towards online sales and home deliveries, resulting in its acquisition of online meal-kits provider Freshly [3] in the US; in addition to acquiring a majority stake in Mindful Chef [4], a recipe box company in the UK[5].

The shifting business paradigm

Going D2C - The Changing Business Landscape

Increase in Order Volume

eCommerce witnessed an order-volume growth of 17% as on June 2020 [6]

An order volume growth of ~130% was witnessed in beauty & wellness followed by other sectors

New Gen Preference for Digital

Gen-Z prefers online brands when compared with their legacy counterparts, by over 40-45% [7]

As Gen-Z gradually enters peak buying age, the market share is bound to keep growing.

D2C Adoption in Scale

The initiative to go D2C is prevalent across legacy brands in scale.

There is a massive growth of 65% in brands developing their own website to create their own web store [8]

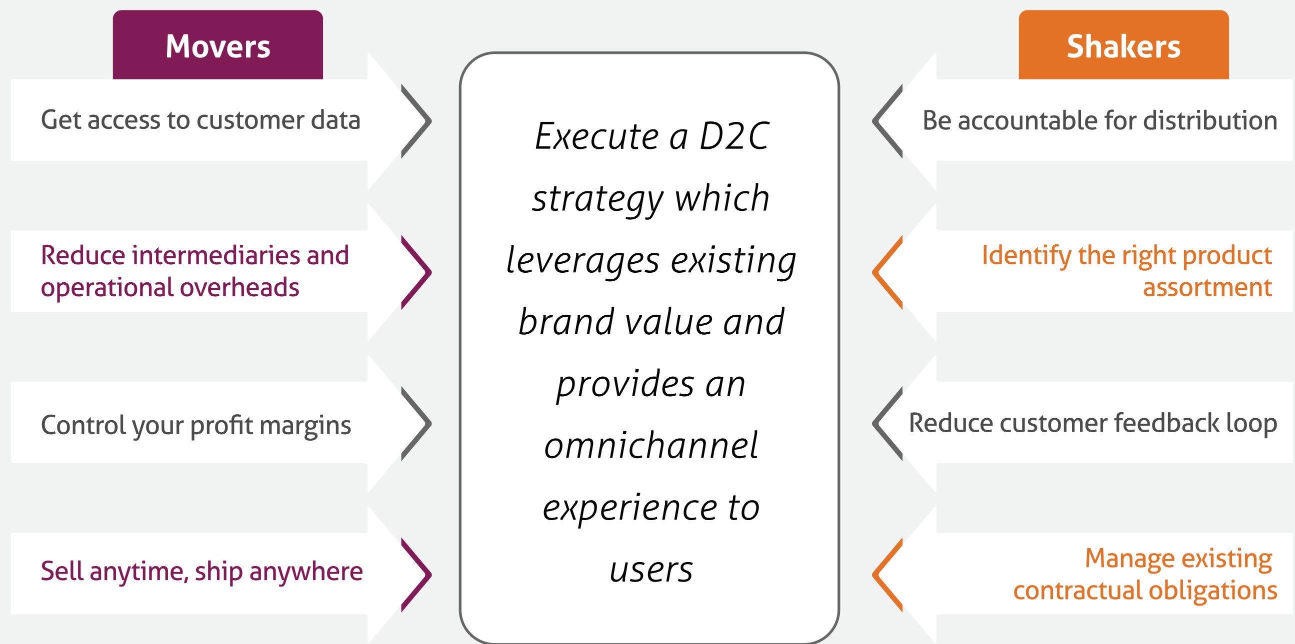
The D2C Success Differentiators

Personalization is at the core of D2C strategy with 89% of legacy brands investing in it.

Brands such as Coca-Cola, Fabletics, Netflix, Sephora, USAA, and Wells Fargo are focused on removing customer pain points to provide individualized experience [9]

While the benefits are massive, challenges faced by legacy brands are unique and strategic when compared to D2C upstarts. By sitting on a large profit pool and being ankle deep in existing ways of doing business, legacy brands are not pressurized to innovate as much as startups are. This was conspicuous when Dollar Shaving Club & Harry's Shaving started selling razors online, disrupting the mainstay presence of a legacy brand like Gillette. This pushed Gillette to launch Gillette Shave Club, which follows a similar business model. Currently, Harry's Shaving continues its online presence while Unilever has acquired Dollar Shaving Club [10].

Explaining this paradigm shift in the business landscape can never be complete without mentioning Warby Parker, the D2C supernova. The eyewear industry was expensive and monopolistic, with almost 80% of high-end eyewear owned by Luxottica, a legacy brand. The industry was waiting to be disrupted when Warby Parker started the fire. By selling from a digital storefront and with vertical ownership of the supply chain, Warby Parker removed the blockers of hefty licensing fees and retail distribution and passed on the benefits to its customers. Cut to today, and Warby Parker is valued at $3 billion and has revolutionized the eyewear industry. [11]



The uniqueness of the challenge faced by legacy brands can be tried to be summarized in two salient points:

1. Challenging the status quo of well-entrenched intermediaries

2. Relooking into existing supply chain models to ensure that order fulfillment is fast and accurate so that the brand value does not dilute or deteriorate. This is challenging, both when competing with online first retailers as well as established online marketplaces

Facets of a D2C strategy

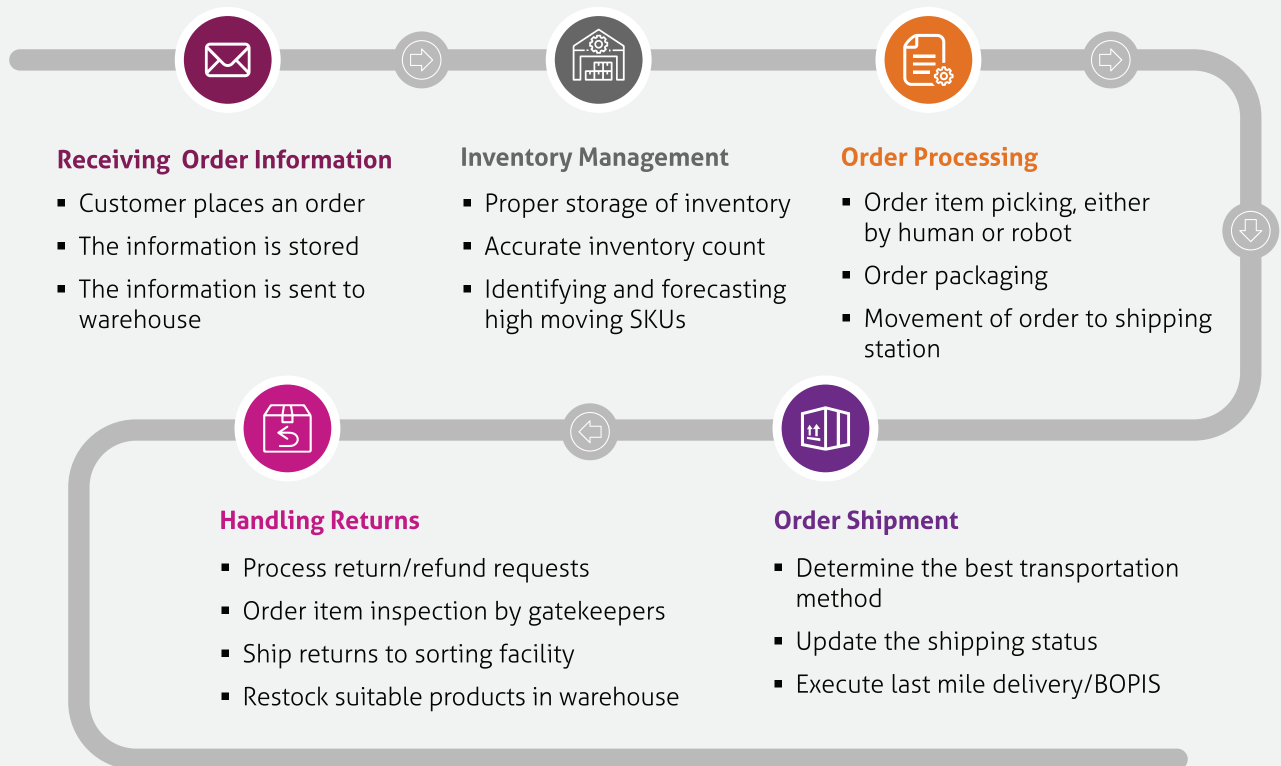
A new commerce strategy must encompass all aspects of a commerce model - from product conception until post-sales service to be successful. When Cavin Kare launched the 'sachet' concept in 1983, it disrupted the Indian market by impacting every aspect of product management. From the product being a sachet to its pricing to its distribution, everything was tailored to this specific business use case unique to the Indian customer base [12].

In the current times, there are many facets to the D2C school of thought. Among these, fulfillment begs to be the most prominent, primarily because by removing third-party wholesalers or retailers, a primary contributor to supply chain price inflation is eliminated. This provides brands greater control over their profit margins, apart from delivering an additional lever to improve customer experience.

"Good roads, canals, and navigable rivers, by diminishing the expense of carriage, put the remote parts of the country more nearly upon a level with those in the neighborhood of the town. They are upon that account the greatest of all improvements. They encourage the cultivation of the remote, which must always be the most extensive circle of the country."

- Adam Smith (Wealth of Nations)

Historically, legacy brands were not actively involved in fulfillment, as distributors and online marketplaces tackled this. This arguably makes order fulfillment one of the biggest challenges for legacy brands when strategizing a D2C shift. Customers expect a fast delivery turnaround with convenience & accuracy, and faltering would erode the customer trust and stickiness, the biggest differentiators and revenue denominators in eCommerce.



Below are some of the key order fulfillment challenges faced by legacy brands when executing a D2C strategy:

1. **Deciding on a Go/No-Go on vertical integration** – By integrating vertically, legacy brands can insure themselves against the risk of a borrowed supply chain. Vertical integration was taken up by Warby Parker[13] to sell their products to customers via a digital storefront and deliver at the doorstep. However, for some businesses, the margins preserved by removing intermediaries from each integrating vertical could be lost because of the uniqueness or variance of each integrating vertical. To ensure that the Customer Acquisition Cost (CAC) remains in line, brands need to ensure that costs of integration are also regulated. Therefore, in certain cases, it may be beneficial for a legacy brand to offload distribution to a third party while it revamps its existing supply chain or creates a new one for the D2C initiative.

2. **Minimum viable packaging** – Over-packaging increases transportation and packaging costs, and creates unnecessary waste material, thereby increasing overheads. Hence, it becomes imperative to innovate on packaging methods for item-wise D2C customer shipments, to ensure that overheads are minimized.

3. **Locating D2C inventory independently** – The D2C offerings may vary significantly from traditional offerings for legacy brands. When the array of D2C product assortments vary from the traditional offerings, managing the D2C inventory becomes challenging. To compound the matter of managing the D2C inventory, the added pressure of commitment to customer shipping and delivery times may pressurize the existing inventory management locations more than ever. Hence, managing a separate location for the D2C inventory to carving out designated places for D2C orders in the existing inventory chain may be the way forward.

4. **Advanced order management systems** – Generally, pure play online marketplaces offer free shipping as it is common for customers to abandon carts when costs arise. When either the brand or the customer pays for shipping, it becomes critical to forecast the cost to either integrate it with product pricing or display it to the customers early in their commerce journey. This could ensure that carts are not abandoned, in addition to maintaining profit margins. Furthermore, order information should be processed quickly and accurately to start the shipment early to ensure customer delight.

5. **Optimizing logistics systems for D2C shipments** – Legacy brands going D2C will always find a conflict between the historical Full Truck Load (FTL) bulk shipments and a picking strategy optimum for single item shipments. A FTL optimum for large freight shipments might not prove economical for item-wise customer shipments. Leveraging LTLs (less-than-truckload) to consolidate shipments with other vendors, utilizing retail stores as fulfillment centers, and consolidating order items to reduce transportation costs can all work in tandem or independently for cost effective D2C shipments.

6. **Conquering the last mile** – A lightning-fast last mile delivery is the final leg and one of the most determinant factors in a positive customer experience. Last mile deliveries are characterized by speed, efficiency in managing & integrating several touchpoints, and transparency in communicating to customers. Originally revolutionized by Amazon Prime, Covid-19 has brought numerous other complexities in scope such as contactless deliveries and BOPIS (Buy Online, Pick in Store).

Alignment of Last Mile Delivery

Which fulfillment strategy works best

For legacy brands, there are some major strategies for order fulfillment, as outlined below:

1. **In-house Fulfillment** – A do-it-yourself approach involves ownership of the entire order fulfillment process, right from receiving to shipment to returns processing. While this provides significant benefits, such as the control of the process and quality, it can also create operational overheads as the D2C business split keeps increasing. It can also be capital-intensive if there were no logistics equipment and systems previously.

2. **Third Party Fulfillment** – Outsourcing logistics to a third-party specialist hands-over the ownership and accountability while the brand focuses on marketing, growth, and other aspects. The benefits are many as third party specialists are logistics veterans with expertise in both fulfillment and negotiation with carriers as they already have a huge volume of shipments. Furthermore, they can mix and match deliveries, carriers, and fulfillment centers to ensure cost effectiveness. However, this entails the loss of control over fulfillment and requires upfront research to ensure that the right service provider is chosen to maintain the right services level so that the brand image does not dilute or deteriorate.

Do it Yourself vis-à-vis Outsourcing

Do it Yourself

- Niche product line
- Niche customer base
- Existing supply chain
- GTM for a highly dense order area
- Capex of supply chain equipment
- Scalability
- Negotiation with carriers
- Non-specialization

Outsource

- Historical expertise
- Ability to scale
- Optimal shipping assortment
- Leverage existing capabilities
- Lack of business knowledge
- Loss of control & brand ownership
- Quality management

3. **Leveraging distributors as fulfillment partners** – Legacy brands can also look at leveraging distributors as fulfillment partners. This hybrid model can be useful when distributors are properly aligned and not alienated with the brand's D2C strategy. Moreover, this can be mutually beneficial, as brands can create a D2C platform while their existing partnerships with distributors change but do not end.

Conclusion

The D2C industry disruption, further maximized by Covid-19, will shape the new normal world. Going D2C is increasingly looking like the only sustainable way forward for brands, while logistics excellence will be a key differentiator in gaining customer trust and stickiness in this era. However, inactivity in maximizing brand value while minimizing costs in transportation and logistics will erode both the bottom line as well as customer trust. In summary, achieving perfection in logistics will ensure that a strong brand value is maintained. This will also make the brand future-ready, in terms of profitability and growth.

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Siddhartha Mohapatra works as a Business Consultant with the Customer Success Team at Mindtree. During his eight years of extensive experience, he has consulted with clients across NAM, APAC & EMEA regions and helped them achieve their B2B & B2C commerce vision. Currently, he works with a global CPG company, partnering with them in achieving their goal of increasing their online revenue split.

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About Mindtree

Mindtree [NSE: MINDTREE] is a global technology consulting and services company, helping enterprises marry scale with agility to achieve competitive advantage. "Born digital," in 1999 and now a Larsen & Toubro Group Company, Mindtree applies its deep domain knowledge to 275+ enterprise client engagements to break down silos, make sense of digital complexity and bring new initiatives to market faster. We enable IT to move at the speed of business, leveraging emerging technologies and the efficiencies of Continuous Delivery to spur business innovation. Operating in more than 15 countries across the world, we're consistently regarded as one of the best places to work, embodied every day by our winning culture made up of over 22,000 entrepreneurial, collaborative and dedicated "Mindtree Minds."

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