Fashion Institute of Technology
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Cosmetics and Fragrance Marketing and Management Master's Degree Program

Capstone 2013 White Paper DIGITAL COMMERCE

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Introduction

The beauty industry today is very focused on commercial transactions in the traditional brick and mortar channel with 95% of sales in the U.S. taking place in physical stores. Consumers, however, have shifted the way they shop in this new digital age. They do not want brick and mortar to be treated as a separate channel from the online world and expect to get the best of both of these environments wherever they are. Consumers also expect to find whatever they are looking for easily, but the beauty industry still makes them work too hard to get what they want. There is a huge opportunity to leverage technological capabilities to help consumers have better commercial experiences wherever they shop. Only 5% of beauty sales take place in the e-commerce channel (see Figure 1), but other categories have much higher penetration: toys and games 13.9%, consumer electronics 13.1%, consumer appliances 10.2%, and apparel at 6.3% ("Emergence of S Commerce," 2013, 60). This highlights a significant under-index in online sales for the beauty industry, which also means a missed opportunity to capture more consumers and grow industry sales overall.

This is happening for two reasons. First, beauty is an experiential category and consumer-product interaction is essential in the path to purchase. This paper will highlight opportunities to use digital technology to enhance the consumer experience in all channels. Secondly, brands and retailers are not leveraging existing technology to enhance or create new purchase opportunities. This paper will also explain how both the current brick and mortar and online retail channels will need to evolve to keep up with consumers' growing demands, and how a new model of commerce creates opportunities for consumers to transact anywhere and for brands to sell everywhere.

Infinite Commerce Model

In the current state, the online and offline channels are not seamless or frictionless, although brands are beginning to use technology to close the gap. Online and offline began as two separate commercial environments. Over time, these two worlds have moved closer together. Some brands have been successful bringing high-tech elements from the online world into brick and mortar. Other retailers have successfully elevated service by bringing high-touch elements from in-store into the online environment. However, it is still not the seamless experience consumers are seeking. 89% of consumers feel retailers should enable them to shop in whatever way is most convenient and 49% of consumers feel the best thing a retailer can do to improve the shopping experience is to be more seamless between the physical stores, online, and mobile channels (Samuel, 2013).

Consumers have become very comfortable in a complex environment of omni-channel retailing, where technology enables 24/7 access to products, education, and service. A new model of commerce must incorporate the three key drivers that define our interactions with consumers at every touch point: convenience, curation, and customization. The consumer expects a consistent brand experience across all channels. Therefore, it is up to brands and retailers to implement an Infinite Commerce model (see Figure 2), introducing high-touch experiences to the online environment and incorporating digital elements that add value to the in-store experience. Implementing the Infinite Commerce model requires operational and organizational changes from brands and retailers to improve the consumer experience. Consumers will be able to snap a picture of any object and purchase it directly. Image, sound, or video recognition technology locates the product. And the brand ships the product directly to the consumer. The end result of this implementation is that the consumer will experience "Beauty on Demand."

This new model, Infinite Commerce, conveys a continuous cycle of commerce. It addresses the key desires of consumers, utilizes technology to create commercial opportunities everywhere, and allows consumers to opt in for high-touch experiences when needed.

In-store: High-touch Experience

Brick and mortar locations will continue to be a dominant retail channel for the beauty industry, but in order to grow, they will need to evolve. They should introduce meaningful digital technology to the in-store environment and evolve the format of the in-store channel with the end goal of creating a more customized, enjoyable experience that encourages increased consumer engagement and interaction with beauty.

Julie Bornstein, CMO of Sephora has said, "The key is to figure out where technology can add to the physical experience, rather than focusing on just the appeal of an iPad sitting in a store (that wears off quickly)" (Bornstein, 2013). Retailers and brands must bring high-tech to the offline channel to elevate the consumer experience by guaranteeing the most appropriate selection, encouraging discovery and ultimately driving more sales.

Facial recognition and predictive analytics technology will revolutionize the in-store experience. Installations at counter will recognize and synthesize your consumer profile, based on publicly accessible information. It can then recommend products that will work for a consumer's unique beauty needs. As a result, each virtual beauty advisor consultation can be customized and will never start from square one. Layering meaningful digital technology to augment the in-store environment is just the beginning of transforming the in-store experience.

The next phase of the evolution of the

physical beauty retailer will be the introduction of new, smaller-format boutiques. These boutiques can be located as freestanding stores or can pop up within other locations like hotels and airports. Proximity will continue to be a crucial factor, as 75% of all purchases are made within 15 miles of consumers' homes (Joyce, 2012). Consumers are beginning to see the big-box store format as impersonal and overwhelming and there has been a return to "shopping small" with an emergence of localized boutiques. Consumers have always felt their relationship with retailers needs to be genuine and personal and are looking to establish stronger relationships where they shop (Yarrow, 2012). Macy's and Walmart have already begun to capitalize on this trend and have introduced smaller, more localized initiatives, through My Macy's and Walmart Express. My Macy's directs consumers to the best location based on their ZIP code and products they are looking for to make the hunt for something specific easier ("My Macy's Shop Ahead," 2013). Walmart Express is the smaller store format now being offered by the biggest of the big-box retailers, to allow consumers more localized, convenient access, still at its signature everyday low prices ("New Walmart Express Store Opens in Princeton," 2013).

The product assortment and services offered in smaller format boutiques will be customized to the clientele so the selection will vary according to location. Digitally enabling stores will make this possible. Merchandise can be selected and ordered based on local community demographics and shopping habits. The stores will all have WiFi and will be enabled with Geofencing technology, which "works by defining a virtual boundary around a real-world geographical area. In doing so, a radius of interest is established that can trigger an action in a geo-enabled phone or other portable electronic device" ("Geofencing," 2013). As consumers shop their personal mobile devices will be synced with the store's database, allowing the staff to immediately understand their interests and needs, thereby providing the appropriate products. Consumers will discover and explore new product and service offerings which will inspire incremental purchases they may not have located in traditional big-box formats.

Another key to the evolution of the physical store environment is leveraging artificial intelligence technological capabilities, which can be combined with advancements in facial recognition tools in-store. This will produce an elevated and curated offline shopping experience because retailers will have more relevant information than ever before. The evolution of traditional brick and mortar to a more localized and curated approach to retail will further enhance the consumer shopping experience, leading to increased sales.

Online: High-tech Experience

The online channel is lagging behind brick and mortar in beauty sales because it does not replicate the high-touch experience of the in-store environment. Today, the online beauty commercial environment is very flat with static pictures of products and few tools to help consumers make purchase decisions. The high-touch experience, which is essential to beauty, is nonexistent because consumers do not have the ability to experiment with products and get the same level of service that is provided in stores.

The toys and games category enjoys one of the highest penetrations of online sales in the U.S. at 13.9%, so it is an interesting industry to watch for digital innovation ("Emergence of S Commerce," 2013, 60). Video gaming, in particular, is a category that was once very static and flat within the home entertainment category. With various systems striving to offer gamers better experiences through their television sets, Xbox revolutionized the video gaming industry with the introduction of Kinect, which allows the player to be the controller, physically inserting the player into the gaming experience. This same concept will be replicated in the future of beauty e-commerce.

By the end of 2013, an estimated 29.3% of U.S. households will have a TV connected to the internet through either an internet-enabled smart TV, game-console, or other device ("Demographics," 2013). Penetration is on the rise too as it is projected that by 2016, 43.1% of U.S. households will have a TV connected to the internet. The tools to experience beauty in a high-touch format already exist in consumers' homes and are on the rise.

The online retail environment will replicate the high-touch store environment through an interactive screen experience. Motion-activated technology will allow consumers to literally browse aisles of products and make selections for purchase directly from the screen. Brands and retailers will have the opportunity to use this platform to invite consumers to experience their best and most unique stores. It introduces a new type of exploration for two reasons. Consumer interaction with products will evolve into an environment that replicates the engaging layout of a store as well as the opportunity to enjoy "entering" and experiencing far-flung boutiques such as the Chanel flagship in Paris

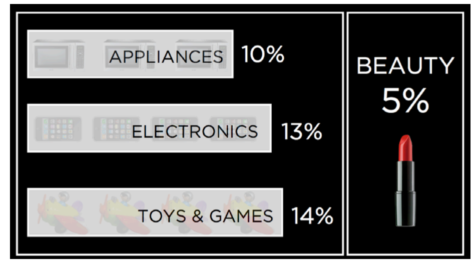

Figure 1

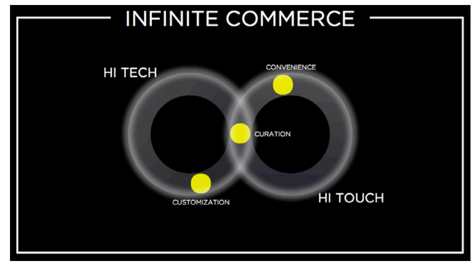

Figure 2

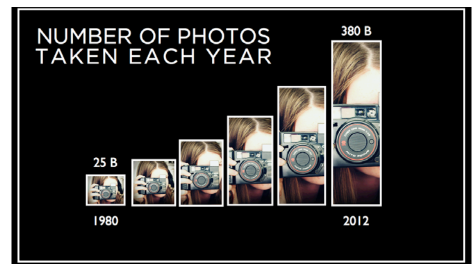

Figure 3

or the new Sephora flagship in Shanghai.

The evolved online experience will be powered by Google Now's natural language user interface, which can answer questions, make recommendations, and perform actions by delegating requests to a set of web services. Content is selected based on the consumer's preferences or online behaviors. Consumers' online and offline shopping experience becomes seamless as the use of predictive analytic technology and artificial intelligence creates a customized in-store shopping experience and fuels a curated environment that lives both in physical retailers and online.

This is an example of how it will work: the consumer has booked a weekend getaway and Google Now utilizes information about the destination to recommend sunscreen and travel sizes of her favorite products. These products are aggregated into a single basket and delivered directly to the consumer's home. They will arrive on the same day because immediate delivery is an emerging consumer expectation and Walmart, Amazon, and Ebay are now piloting same-day shipping services (Wohlsen, 2013, 118-123).

To fully engage the consumer with a high-touch online experience, the service elements will be improved as beauty advisors will be available 24/7 to answer product questions or provide advice. Today, online retail growth is driven by women, many of whom are resorting to this channel because they do not have time to visit physical stores. "The 24/7 access provided by the internet certainly is appealing for busy parents, especially since they may not also have time to shop at brick and mortar stores due to the constraints of normal business hours" ("Beauty Online," 2012, 34). Bringing the high-touch experience to consumers online will enable greater conversion. It frees the consumer to browse brands beyond the regular hours of a physical store and lessens concerns about a desired product being out of stock.

Using technology to blend the high-touch experiences of the offline with high-tech elements of the online is crucial to evolve beauty commerce to be truly seamless for the consumer. The two main commerce channels of brick and mortar and online retail must evolve to keep up with consumers' increased expectations and demands.

Beauty on Demand

Beauty on Demand is the commercial opportunity that will be the future of the beauty industry. The consumer is empowered to purchase anywhere utilizing mobile devices, and brands are enabled to sell everywhere. The new digital world and mobile devices are already having a significant impact on commerce. By 2015, 50% of retail sales will be influenced by digital (Liebmann, 2013). Consumers are beginning to adopt mobile for commerce; 35% of smartphone users have purchased a product or service on their smartphone ("Our Mobile Planet," 2012, 30). Therefore, the next step is to enable consumers to purchase what they capture in pictures and audio clips, allowing brands to take advantage of infinite opportunities for commerce. Consumers are already armed with the tools to make this possible. Smartphone penetration is on the rise in the United States: increasing from 31% of device users in 2011 to 44% in 2012 ("Our Mobile Planet," 2012, 6). 80% of smartphone users do not leave their home without their device ("Our Mobile Planet," 2012, 6).

By the end of 2013, there will be more mobile devices on Earth than people (Murphy, 2013). There are 6.8 billion people on the planet and 5.1 billion (75%) own a cell phone (Edmund, 2012). This number is sharply on the rise too as by 2020 it is projected that there will be 20 billion internet-connected mobile devices globally ("Beauty Online," 2012, 7). Increased consumer connectivity is part of the foundation on which Beauty on Demand is built.

Between 1980 and 2012, the number of photos taken annually increased from 25 billion to 380 billion (see figures 3 and 4) fueled by the omnipresence of smartphones (Schwarz, 2012). Connected consumers are also addicted to sharing, with 90% of online users accessing social sites ("Emergence of S Commerce," 2013, 14). There is an opportunity for brands and retailers to commercialize this consumer behavior while satisfying an unmet desire to be able to purchase anything in the consumer's environment.

Beauty on Demand exposes brands to billions of new Points of Sale (POS). Technology exists to enable transactions between consumers and brands and connected mobile devices are already in the hands of billions of consumers. Google is a leader in visual image recognition and color-matching technology, but it is currently being utilized only to improve search capabilities. Shazam is a leader in audio recognition, yet the app is only commercialized for music. YouTube is leading the way in shoppable video content, although very few consumers or brands are using this platform (see Figure 6). Technology already exists to identify objects through images, sounds, and videos, but no one has commercialized this opportunity. The beauty industry should be the first to capitalize on this technology.

The next step will be to create the connection between the image or sound and a product, and to provide consumers with the opportunity to truly purchase anything. All brand assets, such as the physical products or TV and print advertising, will need to be coded so that visual and audio recognition tools can identify the item and allow consumers to purchase directly. Today, QR codes have been utilized to provide consumers with more product information, but they generally are not designed to close a purchase. They re-direct consumers to a brand website, where the consumer typically needs to click through multiple screens on her path to purchase. This inefficiency leads to dropped baskets and lost sales. According to Baymard Institute, 67% of e-commerce carts are abandoned ("19 Cart Abandonment Rate Statistics," 2013).

The final step for brands, retailers, or both will be to figure out how to ship product quickly and directly to the consumer (see Figure 5). Today, the distribution model confines the ability to sell a product to traditional retailers who can hold and manage inventory. In the future, brands will remain in control of their inventory but will need to be able to ship orders to con-

Figure 4

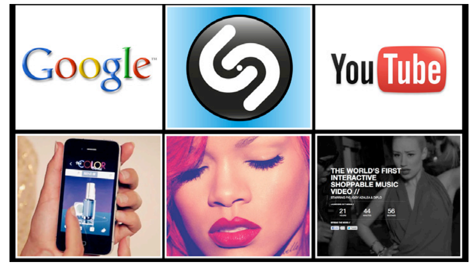

Figure 5

Figure 6

sumers who purchase off of anything. After a consumer clicks to make a purchase, the order is transmitted directly to the brand. To ship these orders efficiently brands should partner with a fulfillment expert. Beauty on Demand recognizes that fast and free shipping will be a point of parity.

The future of beauty commerce will be a new consumer network of brand ambassadors, who serve as affiliates through whom brands fulfill directly to consumers. In essence, the street becomes the future shopping mall. When this happens, consumers become retailers as friends or strangers identify and purchase what they are wearing on the street with a snap of their smartphone. Bloggers become retailers when consumers purchase products straight from their blogs. Publishers become retailers by linking items that editors review. With a touch of a button, consumers can truly have Beauty on Demand by purchasing anything they see in their daily environment. This is the future of Infinite Commerce.

Conclusion and Recommendations

Infinite Commerce is a world where consumers are in charge, empowered by digital technology to transact wherever they choose and where they are both brand ambassadors and new points of sale. The best aspects of the online and in-store environments cross over creating a seamless shopping experience.

Implementing the Infinite Commerce model requires operational and organizational changes from brands and retailers. To do this, we recommend brands invest in technology to deliver convenience, curation, and customization. If these operational and technical capabilities are not part of the brand's core competencies, leverage experts in these fields.

- For convenience, invest in infrastructure and technology to provide excellent customer service and rapid delivery directly to the consumer, or partner with capability experts such as Amazon or Ebay for order fulfillment.
- For customization, in the short-term, enable consumers to shop where they want to shop; and in the long-term, enter into partnerships with technology experts such as Google, Shazam, and Youtube.
- For curation, become a content generator, giving the consumer richer content accessible through mobile.

The real breakthrough of the future and what drives Infinite Commerce is the ability of consumers to buy anywhere, and for brands to sell everywhere. The future does not depend on improving just the in-store experience or just the online retailer. The future of beauty commerce is integrating both so that the high-tech capabilities of the online environment are maximized offline, while the high-touch elements so important to the brick and mortar retailer are now incorporated online. The Infinite Commerce model, which creates the ability to buy and sell online, offline, and anywhere in-between, will bring these worlds together. This new world of Beauty on Demand creates a powerful commercial opportunity for the future of the beauty industry (see Figure 7).

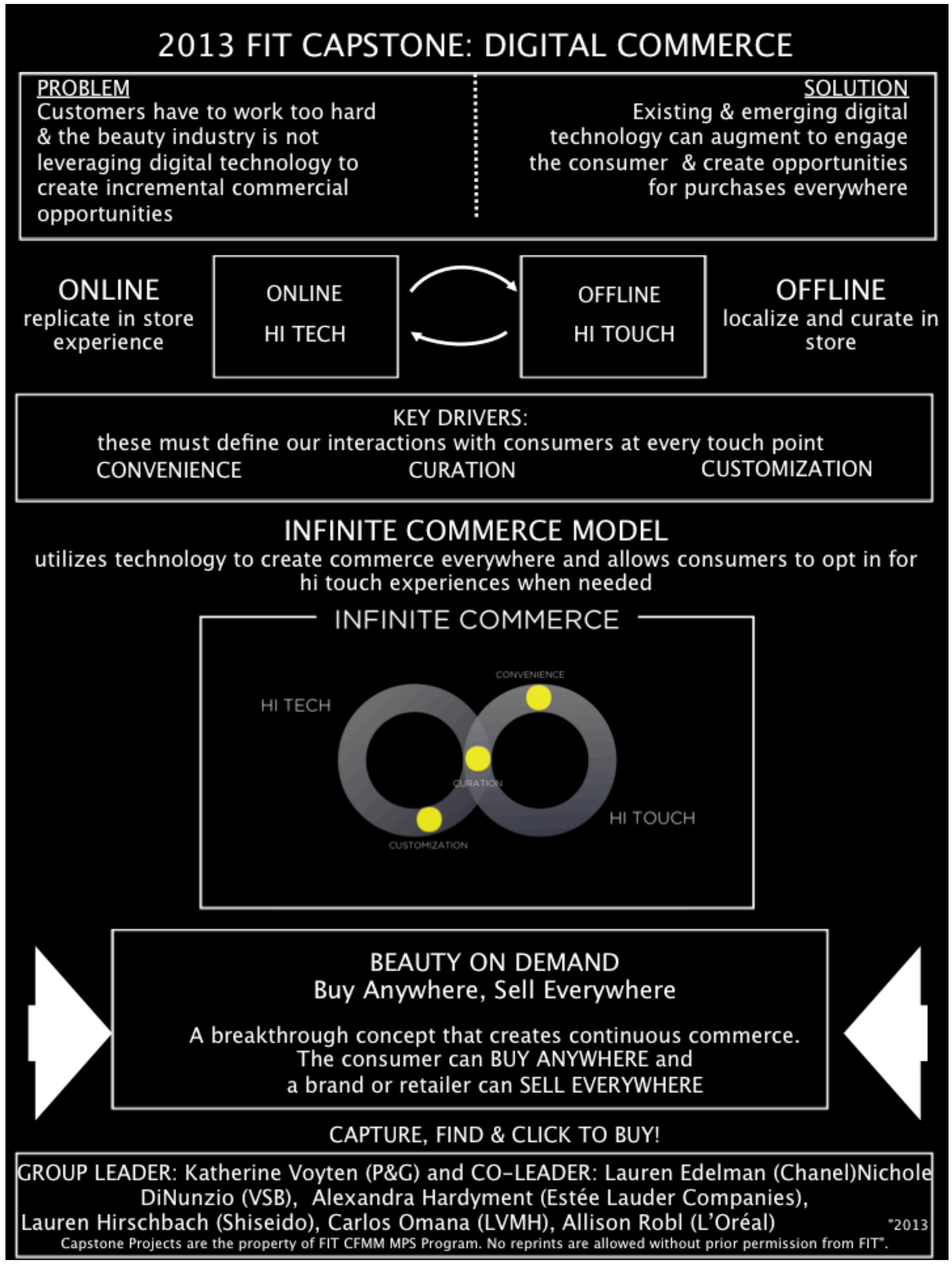

Figure 7

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