internet retailer
STRATEGIES FOR MULTI-CHANNEL RETAILING

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feature article

Some slipping on shipping

With fuel prices rising, retailers struggle to keep shipping fees steady.
By Katie Deatsch

Two things are clear: online retailers are paying more to ship goods to consumers, and many shoppers want to pay little or nothing for shipping.

So what's an online retailer to do?

An *Internet Retailer* survey of 14 larger Internet merchants across several categories finds five have raised at least some of their shipping fees in the last year. The rest have kept fees steady, in some cases trying to trim expenses elsewhere to cover their higher delivery costs. (See chart on facing page.)

"Pricing shipping rates is definitely a balancing act between giving our customers low or free shipping and trying to cover our costs," says Sue De Boer, supervisor of pricing at Amway Global/Quixtar, a direct marketer of health and beauty products owned by Alticor Inc. The retailer has raised its shipping fees on orders above $120 by between 80 cents and $2, about 5%.

Most of the retailers surveyed said they would offer some shipping promotions during the upcoming holiday season. But offering deals on expedited shipping will be especially tough, because carriers are imposing higher surcharges for air delivery than for ground shipping.

The dilemma:

The pressure on retailers to offer good deals on shipping is greater than ever because many consumers are turning to e-commerce sites as a way to avoid paying higher gas prices, which have increased from an average of $2.78 a gallon a year ago to $3.85 last month, according to the American Automobile Association.

The high price of gasoline will prompt 36% of consumers to do more holiday buying online, according to a July survey by Harris Interactive for e-commerce technology provider iCongo Inc. 60% cited free shipping as a reason they are more likely to shop on the web. Another study from comparison shopping engine Pricegrabber.com found 20% of consumers who buy big-ticket household items on the Internet are motivated to buy online because of free shipping and delivery.

As much as they would like to satisfy that demand for free shipping, online retailers face the reality that such major carriers as UPS, FedEx and DHL are passing along their higher fuel costs in the form of surcharges.

Air freight soars:

In the past six months fees for 1-, 2- and 3-day shipping services have increased by as much as 20%—mainly because of higher fuel surcharges, says Bob Boylan, president of Xpert Fulfillment Inc., a third-party order fulfillment provider.

Surcharges are especially high for air freight, says Brian Hodgson, vice president of marketing and business development for shipping software vendor Kewill Americas, a subsidiary of U.K.-based Kewill Systems Plc. He estimates fuel surcharges for packages shipped via air average about 30% of the standard fee, while ground surcharges are about 10%.

Those increases have forced outdoor gear and apparel retailer Backcountry.com to raise some delivery charges on orders that don't qualify for free shipping, such as expedited orders and purchases of under $50. And it's getting tougher to continue offering free standard shipping on all orders of $50 and up, says Jeff Carter, vice president of fulfillment at the online retailer.

"It's putting more pressure on us to be more efficient in our warehouse operations," he says. "Every penny you can shave off counts."

With an average order value of $115, Backcountry.com ships many packages for free, Carter says. And so the retailer, which on its heaviest day ships about 40,000 orders from two distribution centers covering 240,000 square feet, has taken a hard look at its warehouse operations to trim costs so it can continue to provide the incentive.

Backcountry, which uses UPS to deliver most of its orders, has automated its distribution center's packing system to save money. It also carefully tracks carriers' fuel surcharges each month, adjusting its shipping plans accordingly. "We have an analyst who monitors our shipping fees and makes decisions and builds them into our financial forecast based on what he thinks they will be over the year," Carter says.

Outdoor apparel retailer L.L. Bean is feeling the pain of higher shipping costs—and passing some of it on to its customers, increasing the shipping charge on most orders by $1. But the retailer offers free shipping and returns for shoppers that use its co-branded Visa credit card.

Grocery e-retailer Peapod has responded to higher gasoline costs by tacking on a fuel surcharge to its delivery prices. The fee, imposed any time gas prices reach $2.75 a gallon, starts at 28 cents and increases 10 cents each time gasoline prices jump a dime.

"Since the price of gas has risen dramatically over the past year, we have instituted a temporary fuel surcharge as we are no longer able to absorb these costs," the e-retailer says on its web site. "We hope to be able to reduce or remove this surcharge in the very near future." Peapod's surcharge last month was $1.38.

Recreational Equipment Inc., a multi-channel outdoor apparel and gear retailer, raised its shipping fee $1 on most orders, and by more on certain expedited orders.

Cutting costs:

But other big-name retailers are finding ways to cope, sometimes by using their large volume of shipments as leverage with carriers. Costco Wholesale, for example, says it has a lucrative contract with UPS. "We've negotiated a large volume contract that somewhat protects us from rising fuel prices," says Randy Terashima, assistant vice president, technology. "We pass along all savings to our members to keep shipping as low as possible."

Oriental Trading Company, which sells party supplies and novelties, also has kept shipping prices steady, recognizing customer sensitivity to those charges. “Historically, the free shipping type offer is the one that most of our customers have responded to,” says Brian Moen, vice president of e-commerce. “They are looking for that shipping savings and looking at that as an important factor.” He says the retailer plans to offer free shipping frequently throughout the holiday season.

Oriental Trading also is trying to cut costs in other areas so it can absorb carrier costs. For example, by encouraging consumers to place orders online, rather than by phone. “With online orders, we don’t have to have customer service taking phone calls manually,” Moen says. Although Oriental began as a catalog business, more than half of its sales are now online. The retailer says it’s working to drive more consumers to the web through marketing messages in its print materials, on its web site and in e-mails.

Oriental also is working to keep shipping costs low by using regional carriers. While the retailer won’t name the carriers its works with, Hodgson of Kewill says delivery services such as Eastern Connection on the East Coast and LoneStar Delivery and Process in the South offer competitive rates and flexibility in the regions they serve. “With regional carriers, you can do a pick-up at 11 p.m. and it can get there the next day if it’s within their region,” Hodgson says.

According to a recent survey by Kewill, which works with more than 250 online retailers, high-volume shippers are more likely to use regional carriers. 43% of retailers that shipped over 10,000 packages a day used a regional carrier, compared to 20% of retailers shipping 250 to 2,500 orders daily, the poll found. None of the retailers shipping under 250 packages a day used a regional carrier.

Pressure on small retailers:

Absorbing shipping costs can be tougher for smaller e-retailers that often lack leverage in negotiations with carriers, says Boylan of Xpert Fulfillment. Boylan, whose company specializes in retailers that have relatively few SKUs, says he’s seeing more merchants with low order volumes increase their flat shipping rates, hike rates for specific categories that have been hit hardest by fuel surcharges, or raise the purchase amount that triggers free shipping.

Outsourcing fulfillment to companies like Xpert is one option for retailers struggling with high shipping costs. Another is the web-based application from RedRoller, which helps retailers compare prices across such major carriers as the U.S. Postal Service, DHL and FedEx. Merchants enter the origin, destination, package content, weight and a preferred delivery time and RedRoller provides the prices of various shipping options, says John Kruzan, vice president of business development. The fee for the service is based on volume and ranges from $14.95 for up to 150 orders per month to $89.95 for more than 1,000.

Beyond mixing and matching carriers, e-retailers can sack fuel surcharges by using the U.S. Postal Service, which doesn’t have any. “It never added them,” Hodgson says. While Hodgson says UPS, FedEx and DHL offer better tracking, and more easily integrate with warehouse systems from vendors such as RedPrarie and HighJump, he says USPS offers competitive prices, particularily on small packages.

However, retailers consider integration capabilities important. 39% of respondents to the Kewill survey who said they did not use the USPS cited the lack of an easy-to-use and maintain integrated service as the top reason. 33% blamed lack of order tracking.

Integration and tracking can be especially important during peak times, such as Christmas, when retailers have to get orders in boxes and out the door fast. Some online retailers, such as Zappos, use their ability to deliver last-minute orders in time for Christmas as a selling point. “We guarantee that if the free shipping option is chosen, the order will still arrive by Christmas Eve, even if it’s less than four to five business days away,” says CEO Tony Hsieh.

That puts pressure on competing online shoe retailers. And all e-retailers face the pressure of the transparency of the Internet, which applies also to shipping, as consumers can turn to sites like freeshipping.org to find the best shipping deals available on the web.