The Online Paradox
From margin dilutive home delivery to a profitable online business
Introduction

This document shares the basis of online grocery, the financial implications of transactions moving to online, and a translation towards a profitable future.

**THE ONLINE GROCERY BASIS**

Provide an insight into the grocery industry, corresponding trends, and share typical margins for store and online transactions.

**KEY PROFIT DRIVERS**

Deep dive on the transaction overview, key cost and revenue drivers that lie underneath the online paradox to understand the key issues of different fulfillment options.

**THE PATH TO SUCCESS**

Share solution directions that can help to turn The Online Paradox into a profitable online business model.
Introduction to Grocery

Worldwide, 26% of consumers purchased fresh groceries online (more than 40% in mature markets), resulting in an expected 10% of online grocery market share in the next years. This increase of online sales also means a shift from store-based fulfilment to home-fulfilment.

Grocers need to move their business online in order to stay relevant, but every transaction that moves from offline to online requires massive upfront investments, and tends to be less profitable or potentially margin dilutive.

Adgild Hop
Retail Sector Lead
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Retail used to be based on the consumer doing the fulfillment themselves, coming into the store, doing ‘the pick’, and doing the ‘last-mile logistics’ themselves. Yet now we’re all increasingly setting the expectation that this massively value-adding activity can be owned by the retailer without getting fully reimbursed for this service. And this expectation of service keeps growing: shorter lead times, smaller delivery windows, etc.
Margin dilutive home delivery – The transactional costs

Every transaction that moves from store to home delivery tends to be margin dilutive. Typically grocers can reach an indicative profit margin of approximately 5% on a store basket, while home delivery typically entails an extra 7-13% of costs. It does not take a mathematician to conclude this has a significant impact.
Deep dive on the transaction overview, key cost and revenue drivers that lie underneath the online paradox to understand the key issues of different fulfilment options.

Margin dilutive home delivery – home delivery drivers

The margin impact of home delivery is driven by the operational model (picking and last mile transportation) and commercial model (delivery fee).

Indicative home delivery profitability

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Wesley Snoeren
Online Fulfilment Specialist
Deloitte NL
Indicative Click & Collect profitability

Sources: Deloitte analysis, company P&L data, annual reports, desk search, expert interviews
Lead solution directions that can help to turn The Online Paradox into a profitable online business model.

If we assume that ignoring the online grocery trend is not an option, for the majority of retailers, the question is how to minimise margin impact. This comes down to two key questions: 1) how to optimise the commercial model to ensure the consumer pays a fair share and 2) how to set up the online grocery operation while minimising the incremental costs.

Mark-Jan Grootenboer
Online Fulfilment Lead
Deloitte NL

The Path to success

Leading grocers implemented multiple initiatives to try to pivot into profitability, with limited success. We believe that online grocery has the potential to be a cost neutral and possibly even profitable business. This is only feasible through a holistic approach, combining best practices of leading grocers, and optimise the commercial and operational model in parallel. A clean model based on clear choices is key.

Optimise the Commercial Model
An optimised commercial model brings the right value to the consumer while making sure a fair reimbursement in pricing or consumer effort is introduced. However, consumer perception is key to take into account for all commercial improvements.

Optimise the Operational Model
An optimised operational model makes sure the commercial offering is executed in a cost efficient way. However, transactional cost benefits need to be evaluated with the necessary investments. In addition, strategic decisions define the extent of optimisation possible (e.g. centralised vs decentralised fulfilment).
Solutions

What should an optimised commercial and operational model look like? A combination of leading examples such as milk-run model, automated picking, delivery subscription fees, and hybrid delivery solutions like click-and-collect could eventually result in a healthy online grocery business.

Profitability solutions home delivery

- **High potential solution**: Making sure consumers pay a fair share of the delivery operation increases profitability, dependent on pricing strategy.
- **High potential solution**: Incentivising consumers to use click-and-collect options instead of home delivery increases profitability with 5-7% per order.
- **High potential solution**: Automating the online picking operation in the warehouse increases profitability, dependent on the degree of automation.
- **High potential solution**: Creating fixed delivery timeslots and using a modern milk-run model potentially doubles the orders delivered per hour.
- **Other solutions**: Diversifying the ship-from location (CDC, RDC, store) based on proximity to the consumer and market density creates an optimal balance between picking and last mile costs.

Profitability solutions Click & Collect

- **High potential solution**: Automating the online picking operation in the warehouse increases profitability, dependent on the degree of automation.
- **Other solutions**: Lockers where consumers can pick-up C&C orders without interaction with store employees eliminates customer-facing store costs.
- **Other solutions**: Combining click and collect orders with regular store replenishment decreases the replenishment costs, but the additional warehousing operations needed increase warehousing costs.
- **Other solutions**: Diversify the ship-from location (CDC, RDC, store) based on proximity to the consumer and market density creates an optimal balance between picking and last mile costs.
Do you want to create a successful online business?
Connect to our online fulfilment specialists

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