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Vendor Research

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US ONLINE COMMERCE GROWTH AND OPPORTUNITY THROUGH SHIPPING

SUBJECT TO DISCLAIMER ON COVER
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Market Growth

US Online Retail Spending Increasing by 18 Percent in 2006, While Rising at CAGR of 12 Percent Through 2010

In 2005, online retail sales grew to $81 billion—a $14 billion increase from 2004. Moreover, sales will rise by a similar amount in 2006 to $95 billion. This consistent year-over-year growth signals strong continued channel adoption by US consumers, and this trend will persist through 2010 at a compound annual growth rate (CAGR) of 12 percent. Because the online component is the fastest-growing element of most multichannel retailers’ businesses, investment in online business units will likely return to solid early-market levels. Although online sales of $95 billion will only comprise five percent of the $2.1 trillion US retail market in 2006, impact and opportunity lie in the Internet’s off-line sales influence, representing 45 percent of total off-line US retail sales in 2010.
In 2006, two major drivers will have equal influence on the growth of overall online retail sales. Historically, new online buyers represented the primary force behind increases in online sales, while growth in wallet share of existing buyers drove a small remainder. As online buyers’ share of overall online users nears its cap (approximately 75 percent in 2010), however, retailers will find relatively fewer nonbuyers to convert. With online retail sales continuing to grow at a rigorous pace through 2010, growth will instead come from consumers who already purchase online and have decided to shift more of their purchases to the channel.

Most current online buyers are Net veterans (i.e., online tenure of two years or more). In fact, highly tenured groups have spent significantly more online (at least 21 percent more in 2005) than have groups with relatively less tenure during the past three years, according to JupiterResearch consumer survey data. As these key drivers shift in importance and the online shopping environment matures, retailers will face an increasingly experienced population of online shoppers who are savvy about finding free shipping as well as discount offers and who could have increasingly high expectations regarding customer service as well as the user experience.
Online Consumers’ Demographics and Behavior

Middle-Age Adults Dominate Online Purchasing; Spending by Gender Remains Nearly Equal

Middle-age adults (i.e., ages 35 to 49) will remain the heaviest online spenders, accounting for 42 percent of all online retail sales and 30 percent of all online retail buyers in 2010. Online users, ages 18 to 34, will account for 29 percent of total online retail sales in 2010. Although online buyers, ages 50 and over, will comprise one of the fastest-growing online buying segments, they will only generate one-quarter of these sales in 2010. Regarding the remainder, kids and teens (i.e., ages 17 and under) will account for four percent of online retail sales in 2010.

Women and men continue to spend along gender lines in terms of categories from which they most frequently purchase. Women are dominant purchasers in home, apparel, and family-oriented categories, whereas men are most likely to buy consumer electronics, PCs, and sporting goods. Although slightly more women than men currently buy online—with the proportion remaining constant through 2010 at 51 percent—men actually spend more due to the types of products they tend to buy. In addition, many categories (e.g., groceries, health and beauty aids) that lag behind regarding penetration online represent categories in which women do the heavy purchasing off-line.
Ease of Comparison, Retail Similarity Elevate Importance of Price to Online Buyers

In 2005, 45 percent of online buyers said low price was the most important factor in choosing online stores to purchase from, compared with about 32 percent saying the same in 2004. Brand expansion has given consumers many options, increasing the difficulty regarding their purchase choice. Price could therefore represent a last-resort differentiator. Furthermore, the ease of comparing products online and the aggressive promotional schedules of most retailers could have a relatively more direct effect. For example, growing traffic to comparison-shopping sites (with their expanded product assortments) could result in online shoppers’ increased facility with comparing prices and getting the best deals. In fact, the proportion of online consumers who said they believed visiting comparison-shopping sites was the most efficient way to find and choose products to buy rose from 45 percent in 2004 to 61 percent in 2005—an increase of more than one-third.

<table>
<thead>
<tr>
<th>Question: Which of the following helped you choose the online store from which you made your most recent purchase? (Select up to three.)</th>
<th>Source: JupiterResearch/Ipsos-Insight Retail Consumer Survey (8/05), n = 1,629 (online buyers, US only)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Low price</td>
<td>45%</td>
</tr>
<tr>
<td>Previous experience with store</td>
<td>26%</td>
</tr>
<tr>
<td>Low-cost shipping options</td>
<td>21%</td>
</tr>
<tr>
<td>Products available (enabling quick shipping)</td>
<td>17%</td>
</tr>
<tr>
<td>Promotions/discounts/coupons</td>
<td>14%</td>
</tr>
<tr>
<td>Good reputation of store</td>
<td>14%</td>
</tr>
<tr>
<td>Fast delivery options (e.g., product leaving warehouse on same day as purchase)</td>
<td>10%</td>
</tr>
<tr>
<td>Security guarantees</td>
<td>9%</td>
</tr>
<tr>
<td>Helpful product information</td>
<td>9%</td>
</tr>
</tbody>
</table>

Fig. 3 Most Important Criteria in Consumers’ Choice of Online Store

Percentage of Online Buyers

US Online Commerce Growth and Opportunity Through Shipping

Consumers’ Actions Do Not Match Their Perceptions Regarding Free Shipping

Online holiday spending reached $27.2 billion in November 2005 and December 2005—a 23 percent increase from 2004 online holiday sales. According to a JupiterResearch survey during the 2005 holiday season, free shipping was extremely important to consumers (because of high gas/fuel prices), with 56 percent of online holiday shoppers saying free shipping was a key driver in determining stores from which they purchased. Moreover, customers said free shipping for online purchases during the holiday season had more importance in 2005 than in 2004, regardless of increased, static, or decreased budget plans (vs. their 2004 online holiday spending). However, consumers respond to free shipping offers for regularly planned purchases, rather than for items they have not planned to buy (e.g., holiday gifts). In a recent JupiterResearch post-holiday survey, only 14 percent of online holiday buyers said they took advantage of free shipping offers. Although consumers perceive free shipping as key to online buying, they rarely make the effort to find or redeem these offers beyond regular purchases.

Also, nearly one-third of online buyers said they would be willing to pay for shipping to avoid shopping malls (31 percent) and gas expense (30 percent), which is good news for retailers. These customers are 14 percent more likely to be male, 17 percent more likely to spend more online, and 18 percent more likely to have online tenure of fewer than two years, compared with average buyers. Retailers could capture incremental sales by targeting first-time male buyers and men with buying tenure of less than one year, using “avoid the malls,” “save gas,” and convenience messaging—rather than heavily relying on free shipping offers.
In 2005, 78 percent of online holiday buyers spent more online than they did in 2004. However, only 36 percent of online holiday buyers said they intended to increase their spending in the JupiterResearch survey before the holidays. This difference in intent and actual behavior largely results from consumers’ dismal perception of the economy during the run-up to the holiday selling season. Consumers said macroeconomic factors (e.g., record-high gas/fuel prices) were primary reasons for their cautious approach to holiday spending. However, only three percent of online holiday buyers in the post-holiday survey said high gas/fuel prices prompted them to spend more online in 2005 than in 2004, and less than one percent of the same shoppers said decreasing fuel prices during the season motivated their increased spending. Instead, traditional online shopping motivators (e.g., convenience, discounts)—not macroeconomic factors—were primary drivers of increased spending. To impact the psyche of online buyers, online retailers should include macroeconomic factors in messaging, while highlighting the convenience and benefits of online shopping that motivate consumers’ real action.
Retail Loyalty: Creating Lasting Bonds with Online Customers

Retailers must make loyalty generation a tactical priority to avoid having to reacquire customers and escalate marketing costs. By developing a relatively more broadly defined vision of loyalty, they can fully realize the business benefit these faithful customers bring. Retailers must include the following key components of loyalty in evaluation of their customer bases:

- **Frequency.** Retailers must establish a dialogue and relationship with customers. To do so, they should generate a frequency of interaction appropriate for each type of product sold.

- **Spending.** Alone, spending does not indicate customers’ loyalty. However, a goal of generating loyalty is to increase sales (and spend relatively less in doing so). Thus, spending is a key component of the loyalty landscape.

- **Trust and advocacy.** The degree to which customers trust retailers/brands and refer other customers is somewhat difficult to measure but important in gauging customers’ loyalty. By adding this relatively qualitative view to other quantitative measures, retailers can assess the strength of the emotional bond they have with customers. Also, retailers can evaluate advocacy (e.g., through referral rates), identifying customers who are not necessarily high spenders but who are still very valuable due to their ability to refer new customers.
Top Loyalty Tactics Help Customers to Be Efficient, and Provide Personal Recognition

In a recent executive survey, JupiterResearch asked retailers about tactics they used to drive loyalty among their customers. JupiterResearch then evaluated use of those tactics by their impact on 10 key retail metrics, such as conversion rate and call center contacts, ranking tactics in order from the highest positive influence to the lowest. (See Figure 6.) Tactics that enabled customers to be efficient (e.g., features allowing them to manage their relationships with retailers through the Web), helped customers make good purchase decisions (e.g., rich content), as well as recognized and rewarded customers for past behavior (e.g., personalized offers, rewards) had the most positive effect on metrics overall. These tactics are the most effective because they offer customers tangible value.

Clearly, no single best method of engendering loyalty among customers exists. Instead, retailers should employ a combination of strategies, pulling from each of the three pillars (i.e., frequency, spending, trust/advocacy) designed to induce behavior or provide service. Tactics used must directly serve a clear strategic goal. However, retailers should not overlook frequency-oriented tactics. With a clear strategy of relationship development, retailers should determine the assortment of loyalty tactics appropriate for their business models, and create customer communication strategies to highlight each loyalty tactic.
For example, retailers can use promotions such as free shipping to engage customers, associating these offers with the long-term value they provide (e.g., fast and reliable shipping). By offering rich product and service information on sites, retailers can encourage customers to return to sites after sales, thus building trust. As customers begin to rely on retailers for provision of not only low prices and promotional offers, but also complete and convenient resources, emotional bonds will likely develop. When consumers face their next purchase decisions, competitors will thus have relatively less ability to poach them with promotional offers.

**Formal Loyalty Programs Will Become Commoditized by 2007**

Only 24 percent of online retailers in the US have formal loyalty programs, but another 43 percent plan to implement programs during the next 12 months, according to a recent JupiterResearch executive survey. Thus, two-thirds of US retailers will have formal loyalty programs consisting of points, cash back, or rewards. Retailers interviewed for this report were eager to implement loyalty programs to formalize efforts to gain incremental sales from their customers, despite already-high repeat-customer numbers in some cases. Also, they believed they should implement programs soon to stay ahead of competition.

They are correct. The heavy focus on implementing loyalty programs clearly indicates retailers are feeling the heat from competitors and must step up their efforts to both increase sales and curb attrition. The challenge is creating programs that bolster retailers’ overall value proposition through a combination of experiential and recognition efforts.
Promotions such as free shipping have become ubiquitous among retailers, and retailers perceive promotions as most effective in encouraging loyalty. (See Figure 7.) However, promotions only ranked 10th based on JupiterResearch’s evaluation of impact on metrics. (See Figure 6.) The difference between retailers’ perception and actual results shows retailers rely too heavily on traffic-driving tactics, while overlooking long-term relationship-building tactics.

However, retailers also perceive fast and reliable shipping—a long-term value-oriented tactic—as a critical element in their efforts to encourage lasting customer relationships. With two shipping-related tactics considered most important, retailers therefore believe logistic capabilities are critical regarding customers’ loyalty. In many cases, retailers miss the opportunity to message customers about their solid shipping capabilities. They should weave messages of shipping speed into call-to-action pieces, emphasizing product detail and shopping-cart pages to create a sense of urgency and reliability.
Effectively performing during past sales and meeting customers’ needs for new products (regarding future purchases) play equal parts in repeat business. To drive repeat purchases, retailers must ensure shipping performance delivers. Online buyers must have assurance their products will be quickly and accurately delivered. Retailers will not only have the opportunity to communicate with customers through post-sale transactional e-mail messages, but also be part of consumers’ consideration sets in the future if they have met or exceeded shipping expectations.
Retailers constantly face the problem of cart abandonment. In a recent consumer survey, almost one-third of shoppers said shipping costs were too high. Also, 14 percent said shipping costs were listed too late in the shopping process. Retailers should stress the value of their shipping offerings (e.g., quick delivery), offering consumers shipping information as early as possible in the shopping experience to stem abandonment.
Post-Sale Order Tracking Offers Additional Engagement Opportunities

Retailers must not neglect post-sale interaction opportunities. Offered by 90 percent of retailers, order tracking pages are ideal places to reinforce dialogue with customers and encourage additional purchases. Retailers can test order tracking pages with the following:

- Past purchases (especially purchases that are easily reordered)
- Targeted offers that are dynamically generated
- Site-wide offers
- Offers on subsequent purchases made using promotion codes
Leverage Transactional E-mail to Promote Greater Involvement

Fig. 11 Retailer Communications Consumers Receive After Making Purchases

Note: All responses are not listed.
Question: What communication did you receive from an online store after you made a purchase from it? (Select all that apply.)
Source: JupiterResearch/Ipsos-Insight Retail Consumer Survey (8/05), n = 1,629 (online buyers, US only)

Shipping confirmation e-mails are retailers’ biggest built-in opportunities to reach recent purchasers for the following reasons:

- Retailers must send these e-mail messages. Therefore, they should try to offset their costs with marketing designed to drive additional sales.
- These messages are the only communications consumers really remember.

To leverage post-sale transactional e-mail messages as marketing tools, retailers should consider using tactics similar to aforementioned tactics for testing on-site order tracking pages. Retailers must also present messages to captive audiences in manners consistent with their brand images. For example, Saks Fifth Avenue will probably use a much different order-confirmation marketing message from the one Wal-Mart will use. To add marketing messages to transactional e-mail messages, most retailers will furthermore need to outsource transactional messages. Internal systems that generate these messages cannot currently marry relevant cross-selling data to purchase information.
Report Methodology

The core of JupiterResearch’s products is the perspective and opinion of JupiterResearch’s professionals. JupiterResearch’s analysts are immersed in the industries they cover through ongoing contact with corporate and technology leaders, daily study of trends and events in the online world, and their collective professional experience. Individual analysts’ perspectives are filtered through rigorous collective debate and deliberation, producing research that reflects the combined sensibility of JupiterResearch’s entire team.

Analysts’ perspectives are enhanced and refined through JupiterResearch-designed market research. JupiterResearch uses many data research tools, including consumer surveys, systematic polling of leading industry executives, comScore Media Metrix measurement data, and a rigorous approach to building market forecasting models. Specialists with JupiterResearch’s data research group assist analysts in the technical development of these tools, such as survey design, sample building, data weighting, and data analysis.

This report benefited from a number of specific market research projects, described below.

JupiterResearch Executive Survey

In May 2005, JupiterResearch conducted a formal survey of online retailers regarding initiatives designed to increase customers’ loyalty. Respondents were screened for decision-making responsibility. A total of 220 qualified individuals completed the survey. Respondents received an e-mail invitation to participate in the survey with an attached URL linked to the Web-based survey form. As an incentive, respondents were entered into a sweepstakes for the chance to win their choice of a Canon PowerShot A510 digital camera or an Apple iPod Mini.

In this survey effort, JupiterResearch worked with PriceGrabber.com, Inc. and Shopping.com, Inc. to develop a sample of online retailers and to assist in the technical tasks of survey fielding.

PriceGrabber.com, Inc.

PriceGrabber.com, Inc. attracts more than 18 million unique visitors per month, providing the easiest and most comprehensive environment in which they can find, select, as well as shop for the right products. By providing detailed and comprehensive product, transaction, and merchant information, PriceGrabber.com, Inc. qualifies shoppers and refers buyers to the appropriate merchant to complete the purchase process. PriceGrabber.com, Inc. enjoys the highest conversion rates of shoppers into buyers, resulting in cost-effective sales for merchant partners. PriceGrabber.com, Inc. sends more than $1 billion in customer referrals per month. Also, because PriceGrabber.com, Inc. is one of the fastest-growing comparison-shopping services, these numbers are continuously growing.
Shopping.com, Inc.

Shopping.com, Inc. is a leading provider of comparison-shopping resources. Its flagship Web site, www.shopping.com, is a new comparison-shopping service that helps consumers use the power of information to make the best shopping decisions. Currently, Shopping.com, Inc. is the only comparison-shopping service that combines millions of consumer product reviews with detailed price information on millions of products from thousands of stores to help users find, compare, and buy anything.

JupiterResearch/Ipsos-Insight Consumer Surveys

In January 2006, JupiterResearch designed and fielded a survey to online consumers selected randomly from the Ipsos US online consumer panel. A total of 2,369 individuals responded to the survey. Respondents were asked approximately 25 closed-ended questions about their behaviors and preferences regarding online holiday shopping, wireless services, online dating, and pharmaceutical Web sites. Respondents received an e-mail invitation to participate in the survey with an attached URL linked to the Web-based survey form. The samples were carefully balanced by a series of demographic and behavioral characteristics to ensure they were representative of the online population. Demographic weighting variables included age, gender, household income, household education, household type, region, and market size. Additionally, JupiterResearch took the unconventional step of weighting the data by American Online (AOL) use, online tenure, and connection speed (broadband vs. dial-up), three key determinants of online behavior. Balancing quotas were derived from JupiterResearch’s Internet Population Model, which relies on US Census Bureau data and a rich foundation of primary consumer survey research to determine the size, demographics, and ethno-graphics of the US online population. The survey data are fully applicable to the US online population within a confidence interval of plus or minus three percent.

In October 2005, JupiterResearch designed and fielded a survey to online consumers selected randomly from the Ipsos US online consumer panel. A total of 2,106 individuals responded to the survey. Respondents were asked approximately 25 closed-ended questions about their behaviors, attitudes, and preferences regarding shopping online during the holiday season, browser cookies, Wi-Fi, and e-mail newsletters. Respondents received an e-mail invitation to participate in the survey with an attached URL linked to the Web-based survey form. The samples were carefully balanced by a series of demographic and behavioral characteristics to ensure they were representative of the online population. Demographic weighting variables included age, gender, household income, household education, household type, region, market size, race, and Hispanic ethnicity. Additionally, JupiterResearch took the unconventional step of weighting the data by AOL use, online tenure, and connection speed (broadband vs. dial-up), three key determinants of online behavior. Balancing quotas were determined by an ongoing weekly random-digit dialed (RDD) survey of almost 5,000 US households. The survey data are fully applicable to the US online population within a confidence interval of plus or minus three percent.
In August 2005, JupiterResearch designed and fielded a survey to online consumers selected randomly from the Ipsos US online consumer panel. A total of 2,146 individuals responded to the survey. Respondents were asked approximately 30 closed-ended questions about their behaviors, attitudes, and preferences regarding buying and researching products/services online. Respondents received e-mail invitations to participate in the survey with an attached uniform resource locator linked to the Web-based survey form. The samples were carefully balanced by a series of demographic and behavioral characteristics to ensure they were representative of the online population. Demographic weighting variables included age, gender, household income, household education, household type, region, market size, race, and Hispanic ethnicity. Additionally, JupiterResearch took the unconventional step of weighting the data by AOL use, online tenure, and connection speed (broadband vs. dial-up), three key determinants of online behavior. Balancing quotas were determined by an ongoing weekly RDD survey of almost 5,000 US households. The survey data are fully applicable to the US online population within a confidence interval of plus or minus three percent.

In these survey efforts, JupiterResearch worked with its research partner, Ipsos-Insight, on the technical tasks of survey fielding, sample building, balancing, and data processing. Ipsos-Insight is one of the largest market research companies in the US and maintains a general research panel of 400,000 households. Ipsos-Insight also has access to the Ipsos US online panel, which comprises two million Internet users, offering JupiterResearch an easy way to target and survey current online users. Panel-based market research enables researchers to have baseline knowledge of each survey respondent, increase survey participation rates, and permit careful rationing of survey fielding to reduce survey burnout.

**JupiterResearch Internet Shopping Model**

To quantify the dynamic changes JupiterResearch believes will take place in the online retail industry, JupiterResearch built a complex forecast model capturing current online activity in this space and six-year forecasts of user participation and revenue. This model defines key growth levers as well as market drivers and inhibitors, giving clients a clear, analytical way to think about upcoming changes in their sector. JupiterResearch’s analysts use a variety of quantitative methods in modeling the future, including close examination of analogous markets (either previous growth of new technologies or relevant off-line market case studies), consumer and executive intention surveys, scorecard analysis of market drivers and inhibitors, complex market segmentation analysis, as well as analysis of historical trends. Additionally, all forecast assumptions are rigorously debated and vetted by a large cross-disciplinary group of JupiterResearch’s analysts in a process designed to capture the collective sensibility and experience of JupiterResearch’s entire analyst team.
As part of the forecast modeling, JupiterResearch develops comprehensive historical and base-year market size estimates based on a variety of sources, including public financial documents, executive interviews, JupiterResearch’s proprietary primary consumer research, E-Stat data from the US Census Bureau, and analysis of the vast Web site tracking databases of comScore Media Metrix.

All JupiterResearch’s forecasts are designed by a dedicated team of forecasting analysts within JupiterResearch’s data research group, who build the models, conduct extensive industry research, and manage the process of formally building consensus among JupiterResearch’s analysts. JupiterResearch’s forecasting analysts have backgrounds in investment banking, management consulting, and market research, where they developed extensive experience with industry and company forecasting.
JupiterResearch provides analyst research and advisory services to help companies develop, extend and integrate business strategies across online and emerging channels. Backed by proprietary data, JupiterResearch’s industry-specific analysis, competitive insight and strategic advice give businesses the tools they need to exploit new technologies and business processes. JupiterResearch is headquartered in New York City with offices throughout the United States and around the world. For more information on JupiterResearch’s services, including syndicated research and custom research tailored to the specific needs of your business, visit www.jupiterresearch.com, e-mail researchsales@jupiterresearch.com or call 800 481 1212 (North America), +44 (0) 20 7903 5020 (Europe) or +1 212 389 2032 (rest of world).