



DIGITAL BRITAIN

IMRG Submission to the Department for Business, Enterprise & Regulatory Reform (BERR) in response to the Digital Britain Project and highlighting the importance of e-Retail to the UK economy, consumer protection online and future development of the industry.

For the attention of: David Mahoney, BERR.

Author:

Andrew McClelland, Director of Business Development, IMRG

andrew@imrg.org

Forward by: James Roper, Chief Executive Officer, IMRG

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IMRG Submission

Forward

Fifteen percent of total UK retail sales, worth some £50 billion, will take place online in 2009. The first ever secure online transaction took place in 1994, and by 2000 the proportion of retail sales online was less than half a percent. IMRG predicts that in 2020, 90% of all retail sales will be either online or influenced by the internet.

Britain remains digital for only a minority, while most of its population continues to largely miss out on the enormous benefits of choice, convenience and savings that e-commerce delivers. IMRG argues that broadband access must now be seen as a human right and that the Government's UNIVERSAL SERVICE OBLIGATION should be extended to include fast internet access in addition to telephony and postal services.

IMRG's routine consumer surveys show that customer satisfaction with the 'range of goods available online' – the most popular aspect of e-shopping – is now lower (at 84%) than it was two years ago, while its least satisfactory aspect – 'confidence in security' – at just 73.4%, is half a percentage point lower than in 2006 and falling.

Fast, cheap internet access and a secure online trading environment are critical for the future well-being and prosperity of Britain and its people. New research from the Logistics Research Centre at Heriot-Watt University proves that online shopping is already more environmentally friendly than driving to the shops – and with large-scale efficiency improvements in the pipeline, e-commerce is set to make a major contribution to the global effort towards reducing the impacts of energy and material consumption.

IMRG and the 1,000 merchants and facilitators we represent remain standing by to help the Government realise a truly Digital Britain.

James Roper

Chief Executive Officer, IMRG

About IMRG

IMRG is a membership community for the e-retail industry whose vision is to maximise the commercial potential of online shopping. With more than 18 years experience in a rapidly-changing e-commerce market we help members maximise the business opportunities, and stay up to date with developments in the e-retail marketplace. IMRG can be found at www.imrg.org

1. Community

IMRG offers a retail membership network for retailers and suppliers who seek to collaborate, voice ideas and opinions, and grow their network, in an e-retail community, through events and thought leadership programmes. With over 280 members, spanning household High Street brands, major 'pure-play' online only retailers, SME e-Retailers and suppliers to the industry, the IMRG community represents the broad range of interests within the industry.

2. Industry Standards – Best Practice

IMRG promotes retail industry standards and best practices, facilitating self-regulation and the advancement of a comprehensive code of conduct for the retail industry through lobbying activities undertaken by both retailers and suppliers to the industry. The standards and best practices are established and shared by means of online information, white papers, workshops and forums that address key regulatory and innovative issues. These activities include IMRG representing the industry to key decision making bodies, such as the European Commission, Payments Council, Trading Standards and many others.

Members are kept aware of the most up to date and relevant issues that are underlying the e-retail market, as well as being part of a community that shapes the future of e-retail standards.

3. Information – Market Intelligence

IMRG provides an interactive pool of retail data and information from both its own research team, and from a wide variety of external information resources. Members can also share their information through IMRG. IMRG shares e-retail knowledge and information with its members through an online portal and email communication containing retail sales index data, a suppliers directory, white papers, and monthly retail sector review.

4. Consumer Protection

At the request of its membership, IMRG set up and manages the Internet Shopping Is Safe Scheme (ISIS). The ISIS accreditation program was developed over 8 years ago, primarily to encourage consumers to shop online with the added advantage of providing a tool with which industry standards and best practice can be improved. The big brands backed it to promote safe online shopping, whilst smaller brands used it as a tool to encourage shoppers to purchase from a retailer who had little or no brand equity. The ISIS program also offers a mediation service by which disputes between accredited e-retailers and their customers can be settled. With over 800 e-Retailers currently accredited, and a major push planned for 2009, ISIS provides consumers and retailers with a valuable tool for increasing confidence in the online channel.

UK e-Retail Market Overview

Online Retail worth £43.8 Billion in 2008

For many, e-retail encountered a false start during the late 1990's; much was promised but little was delivered. Since early 2001, the industry returned to retailing basics with many high street brands either taking a 'wait and see' brief or making tentative steps. The early promise of online was based on choice, value and convenience, many of the traits which are making it highly successful during the financial climate of late 2008 and onwards. For many small retailers, online trade has provided an opportunity to trade outside of their geographical location; no longer is a prime high street presence the key to a successful retail business. Likewise, those same businesses who have faced a dwindling high street as out of town shopping centres gained popularity, the option of taking their business online has mitigated some of the effects; such as reduced foot fall, competition from local 'mega' stores, and rising rents. With a few notable exceptions, the early drivers of online retail have been smaller retailers specialising in electronics and entertainment products.

More recently, spurred on by the competition provided by a large group of online specialists, market growth has come from well known high street brands opening web stores which closely integrate with their traditional high street operations. The debate has moved swiftly from cannibalisation of sales from stores to online; to a situation where providing the customer with a choice of channels with which to trade is paramount.

The growth of e-commerce, in its many forms, is now being driven firmly by consumer choice. Consumers have never before been given so many opportunities to make informed purchasing decisions from such a diverse range of suppliers. An IMRG / Royal Mail calculation in 2004, estimated that there were in the order of 23,000 retail websites. Working with Hitwise and Royal Mail data, it is estimated that an aggregated total at present is in the order of 150,000 retail websites currently trading. It is worth noting that this figure does not allow for individual retailers having an online store within multiple portals. The difficulty in estimating these figures is compounded by the fact that Standard Industry Classification Codes (SIC codes), as used by the ONS and others, do not specifically split out online only retailers from traditional retail outlets.

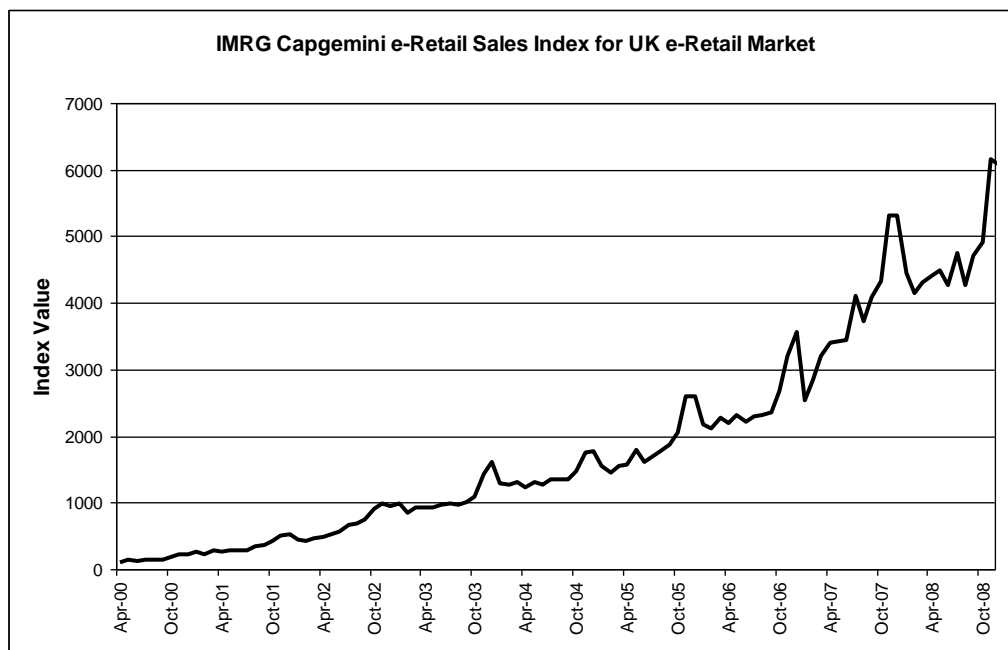
With increasing consumer expectations comes a responsibility on retailers to provide usable, functional and informative websites catering for a wide range of customer expectations and utilising ever more complex and systems hungry applications; a stable, wide spread and fit-for-purpose digital network is at the core of this service provision.

IMRG Capgemini e-Retail Sales Index

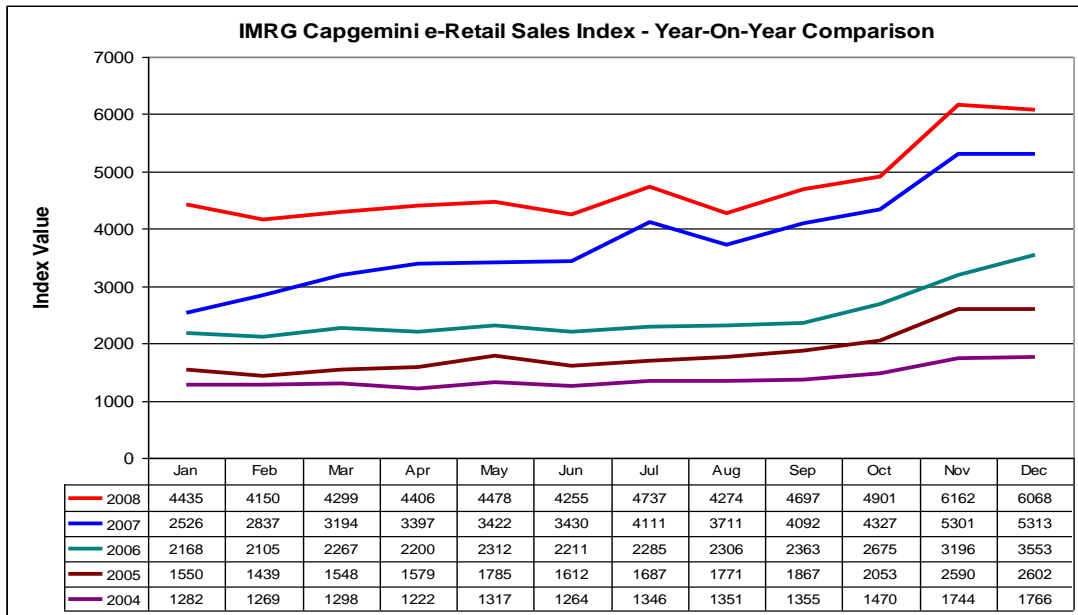
The IMRG Capgemini Index has been tracking UK e-retail sales since 2000 and now has over 90 e-retail participants, including Arcadia Group, ASOS, Comet, Debenhams, John Lewis, Marks & Spencer, Freemans Grattan Holdings, Shop Direct Group, Tesco and many more. The Index reveals online sales have grown from an estimated £0.8 billion in 2000 to £43.8 billion in 2008. There are now around 28 million online shoppers in the UK, spending an average of just over £1,500 each year on the internet.



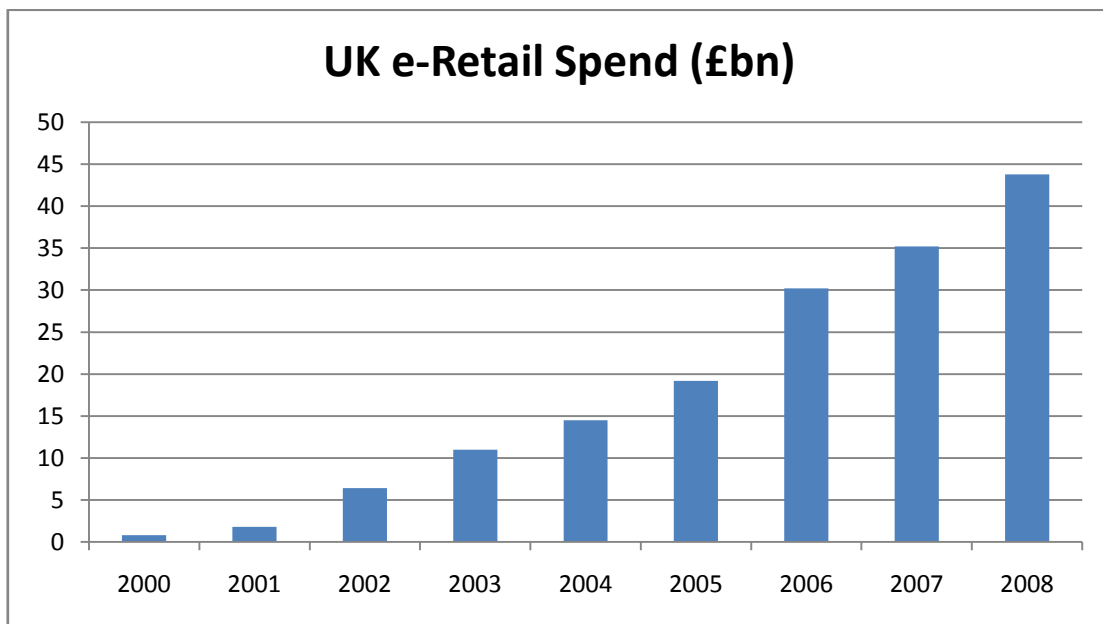
Graphic showing headline growth of e-Retail – Source, IMRG Capgemini e-Retail Sales Index



This chart shows UK online shopping sales April 2000 to December 2008 - Source, IMRG Capgemini e-Retail Sales Index



This chart shows how e-Retail's annual growth rate is changing each year - displaying the values from Jan 2004 to December 2008 - Source, IMRG Cappgemini e-Retail Sales Index



During the festive shopping season in 2008, it is clear that shoppers turned to the web to beat the credit crunch and worsening economy, with e-retail sales in December estimated to be worth £4.67 billion, a year-on-year increase of 14.2%. However, online sales dropped by 1.5% from November – the first month-on-month decrease between November and December since 2002. This could be attributed to several factors, including a greater than average month-on-month growth in November, when sales increased by 26% from the previous month.

The clothing, footwear & accessories sector was the fastest growing online category during 2008, consistently outperforming the total market in terms of Index growth. Online sales of clothing, footwear & accessories grew by an average of 30% year-on-year every month last year, although the overall growth in online retail slowed to around 15% in the second half. Sales of accessories also saw a general upward trend throughout last year, with sales peaking in November, soaring 108% from the previous month and 68% year-on-year. The Index also reveals that the gifts sector

was the worst performing category in 2008, however this sector does have peaks in February and December. Online sales of health & beauty products showed no year-on-year growth last year. However, the Index reveals health & beauty sales peaked in November when sales increased 61% from October 2008 and 39% from November 2007.

Future Market Growth

During 2008 the Index grew 25% year-on-year, however e-retail sales growth slowed to around 15% in the second half of the year, the Index reveals. In the first six months of 2008 the Index showed 38% growth, down from the 50% growth seen in the second half of 2007. IMRG and Caggemini predict e-Retail growth will continue in 2009 at around 15%, with total sales reaching approximately £50 billion for the year.

Allied Industries

Whilst it is the growth of Online Retail that grabs the headlines, the underlying support industry plays an equally important role in its development and, in its self, represents a large contributor to the wider economy. Online advertising spend, as reported by the IAB (www.iabuk.net), reached £2.8 Billion in 2007, up 38% on the previous year and responsible for 15.3% of all advertising spend in the UK. More recently, an OFCOM report published in November 2008 indicated that online accounted for £1 GBP out of every £5 GBP spent on advertising in 2008. Early indicators are already hinting at this growth continuing as online content providers look to monetize offerings and advertisers look for more cost effective and targeted advertising delivery.

The delivery industry has also had to undergo major change over the last 8 years, moving from a primarily Business to Business (B2B) model where all your customers are virtually guaranteed to be available to accept deliveries during business hours, to a Business to Consumer (B2C) model where over 90% of UK households are empty during business hours (Royal Mail Figures). This change has necessitated the development of models which allow for 'out-of-hours' delivery options, difficulty in planning economic delivery routes and a fragmented end-consumer base. However, the fulfillment industry has been driven by rapidly increasing demand with 820 Million e-Retail related parcels being delivered to 27 Million consumers with 714 Million physical deliveries in 2008 (IMRG Home Shopping Delivery Survey 2008).

Whilst no figures are available to indicate the importance of e-Retail as an employment generator and the positive impact that this has on the UK economy, the development of e-Retail has driven the formation of a new industry in a very short period of time (12 years); digital services, fulfillment, software services, IT and systems, marketing services, network development and new financial services to name but a few sectors that have developed from nothing to the current position in a very short period of time. IMRG member, Hitwise, currently tracks traffic going to over 40,000 e-Retail websites. The employment potential of these, both in terms of within those businesses, and their third party suppliers, should not be underestimated.

Investment

From an investment perspective, small retail businesses in the early 2000's could expect to pay a couple of thousand pounds to develop a website and start trading. Now, whilst there are several 'off the shelf' websites that provide much of the functionality that consumers expect for under £1,000 GBP, a sensible investment guide for a bespoke website would be in the order of £25,000 GBP. For larger retailers who have existing customer expectations to meet, and a large product range, a budget of £2 Millions GBP or more would be appropriate (IMRG Member estimate). In addition, connectivity to a digital network will also form a large portion of the businesses fixed costs. For example, a small online retailer can expect to pay in the order of £900/month for a 2MB connection, with dedicated leased lines for larger retailers costing many thousands of pounds per month (IMRG survey of membership). This connection is effectively an e-Retailers front door and any strategy paper looking at the development of the digital network does really need to engage with content providers and e-commerce operations as they provide consumers with the reason for investing in connectivity in the first place.

With many online retailers showing high double digit growth over the past years, managing, financing and planning for this level of expansion is placing many demands on these businesses. Indeed, the need for a stable, accessible and

economically viable digital network forms a cornerstone to the sustained and successful development of online retail and its associated businesses.

This requirement for a stable network also reflects the symbiotic requirement between the network and content providers; without the content there is no requirement for the network and vice versa. Therefore, any investment, planning and legislative framework changes needs to take into account that, whilst high speed, robust and widespread networks are desirable, they are only the means to an end, not the end in itself.

The ongoing costs of operating a business are obviously difficult to generalize. However, the initial barrier to entry for offline retailers i.e. rental payments, leases and staffing costs, whilst not applying to online retailers, has been replaced by high up-front development costs for the website, marketing services and warehousing facilities for stock.

What is clear is that consumers have invested heavily in gaining access to the Internet (Personal Computers, Laptops, software, network connectivity and time), content providers have made significant investments in technology, staffing, and content (Yahoo!, BBC, MSN and The Times, to name a few) and retailers have also done the same. It is now time for the networks and government to ensure a stable digital network is made available for the next generation of users, technologies and business development.

Online Safeguards

Early in the development of online retail, consumers were wary of the new online experience and the thought of passing personal information and payments details to a faceless machine proved a step too far. Also, it was a time where it was easy for unscrupulous traders to profit from this lack of knowledge and those with criminal intent to take advantage of an unsophisticated public.

However, the benefits of online trade were obvious to many; choice, convenience and value were the key drivers behind many online stores and those early adopters succeeded to a degree in encouraging shoppers online.

Today, those three drivers are as valid as in the early days of development and, coupled with the UK Governments desire to reduce the digital divide and promote financial inclusion, the services and benefits that online trade can deliver make it worth the effort required to ensure that consumers have a safe and beneficial experience when trading online. Recent years have also seen household names open transactional websites which has also increased the confidence of consumers to venture online themselves. Once consumers have had a good experience with these brands, they are more likely to try other brands, perhaps online only, or companies that they have never heard of before. The rapid increase in social networking has helped many consumers, through membership of likeminded communities, ensure that there is a wealth of information available to more confident online users before they make an informed purchase from an unknown trader.

Internet Shopping Is Safe (ISIS)

To encourage consumers to purchase goods online in the early stages of the industry, IMRG members asked that it develop a consumer confidence marque, to encourage consumers to shop online but also to bring an element of self regulation and best practice to the industry. The result was Internet Shopping Is Safe (ISIS), a e-retailer accreditation program that has more than 1000 accredited retailers who represent approximately 2/3rds of online trade in the UK by value.

The ISIS program has several functions. Large brands display the marque to encourage widespread use of the internet as a shopping channel; smaller retailers display the logo to counter the lack of brand equity and awareness; the ISIS code of practice is based on the appropriate legislative frameworks, but also includes elements of best practice and thereby improving levels of customer service and performance within the industry; a website to provide information to

consumers and retailers; a mediation service between accredited retailers and consumers when transactions do go wrong; and a level of confidence for consumers that a respected organization has audited a web retailer and is available to assist should something go wrong.

The ISIS team at IMRG has a good reputation for handling customer queries, ensuring that retailers are abiding by the letter and spirit of the scheme, withdrawing accreditations as appropriate and displaying relevant information to help consumers should an accredited retailer go out of business. The program also has good links with Consumer Direct and the Trading Standards Institute. The ISIS website also provides a wealth of information to support retailers trading online, including boiler plate Terms and Conditions produced in conjunction with LACORS, and references for consumers looking to understand their rights and responsibilities, advice on safe online usage and links to industry, government and non-governmental information portals.

Online Trading Issues – The Retailer

In February, 2009, IMRG surveyed the ISIS community to determine key priorities and concerns from a community that falls predominantly in to the SME (Small to Medium sized Enterprise) category.

1. It was widely suggested that more effort be made to educate consumers about safe online shopping, what to look for from a reputable e-retailer and extending training and awareness to those communities that would benefit most from the benefits of shopping online (rural, aged population and the disadvantaged as examples). Suggestions included that this education effort should be facilitated by Government for the benefit of consumers, businesses and the economy.
2. National focus at Government level to address issues around e-Crime, Online Fraud and data security; Police Authorities should have tackling e-Crime included in their performance metrics. The private sector is already investing heavily in counter fraud tools, Identity Verification, collaborative information sharing (within Information Commissioners Office guidelines), data protection registration and the Payments Card Industry Data Security Standards (PCIDSS). It is now widely felt that this investment should be backed up with government action on assigning resources for law enforcement agencies to assist in this work and ensure that perpetrators of online fraud and e-crime face the full weight of the law. It is an area that is seen by the criminal fraternity as a low risk area with the potential for large financial gain.
3. Noting that the majority of consumers will find that their payment card details are compromised offline, but the act of using those details in a fraudulent manner is more likely to take place online. The introduction of Chip-N-Pin has seen card related fraud migrate online with CNP fraud (Card Holder Not Present, which includes online, telephone and mail order) reaching £161 Millions in the first half of 2008, up 18% on the previous year (APACS). However, online retail increased by 35% over the same period. There are current processes being introduced by the card schemes (MasterCard and Visa) called 3D Secure which introduces an element of verification to ensure that the card holder making a payment online is authenticated as the person eligible to use that card. The two processes are called MasterCard SecureCode and Verified by Visa. Whilst there are limitations and concerns around these, they do represent a very positive step forward for consumer safety and mitigating losses to fraud for businesses.
4. Whilst responses to the survey were strongly in favour of protecting consumer rights, improving standards within e-Retail and industry development, it was felt that the consumer protection element of the Distance Selling Regulations were overly in favour of the consumer and definitely restricted consumer choice through the types of products and services that e-Retailers were prepared to offer. For example, the distance selling directive does not link the return of a product with a refund. The retailer is obliged to refund a customer within 30 days of cancelling an order, irrespective of whether the retailer had the product back or not. This has led to situations where the retailer refunds the customer and never receives the product back. It is recognized that

the Distance Selling Regulations were designed to provide a distance customer with similar freedoms to one on the high street i.e. the opportunity to touch and assess the product, the only recourse to an online retailer in this case is to make a claim through the Small Claims Court. Also, cross-border trade is being hindered by the cost of compliance for the many local interpretations of the core Distance Selling Directive and other European legislation such as Waste Electrical and Electronic Equipment (WEEE) legislation. The authors recognize that there is a current review of the Distance Selling Directive by the European Commission to harmonise the legislation and facilitate cross border trade in the European marketplace.

Online Trading Issues – The Consumer

IMRG conducts a quarterly survey of online consumers, the IMRG e-Digital Research e-Customer Satisfaction Survey. With a sample size of several thousand, the results are seen as particularly robust and give useful insight as to consumer perceptions of online retail.

Cumulative Customer satisfaction: All categories: % satisfaction December 2006 - November 2008

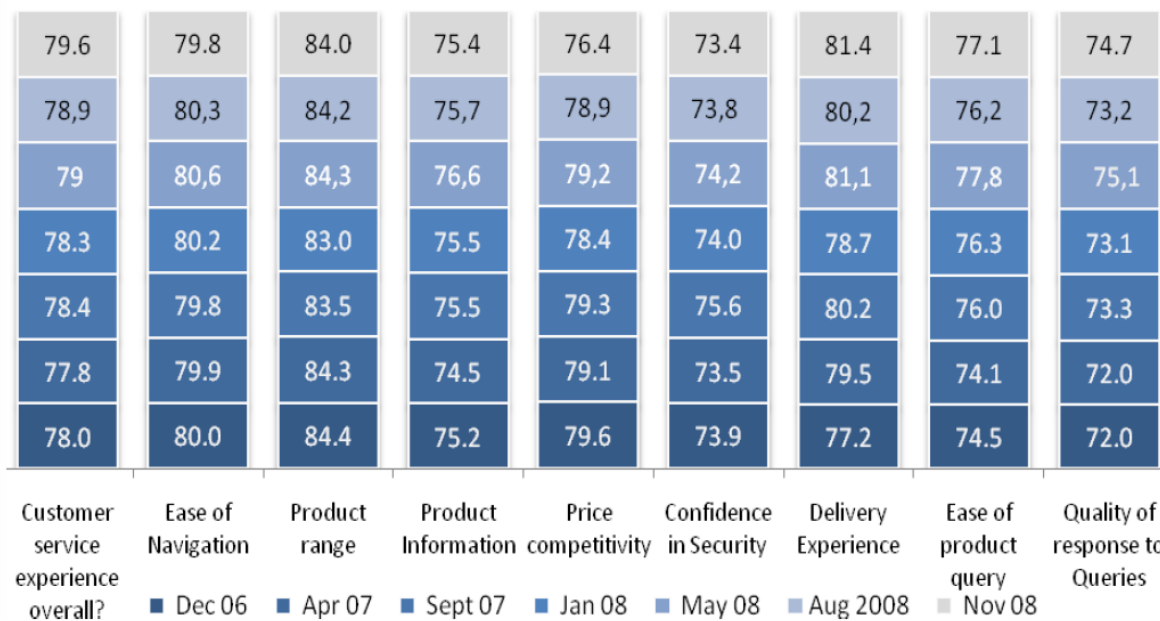


Table showing cumulative results of the IMRG E-Digital Research e-Customer Satisfaction Survey (source: IMRG)

Whilst it is accepted that this survey takes place online, and the respondents obviously have a propensity to shop online, the findings provide valuable insight in to a consumers view on online retailing. Obviously, expectations of regular users are going to exceed those of new users, this experience level can also be seen as a sensible bell-weather for attitudes.

1. Most alarming is the perception that confidence security online has worsened despite some of the aforementioned developments that industry has put in place. It also points to the industry needing to do more to promote best practice; promote consumer confidence marks such as ISIS and for government to engage with key stakeholders, such as IMRG and Trading Standards Institute so as to ensure that key issues are understood, that the importance of online to the UK economy is recognized and that consumer protection issues are promoted through cooperation with industry partners.

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2. Overall though, e-Retail appears to be getting it right in most other areas, pointing to strong growth, as evidenced in the IMRG Capgemini e-Retail Sales Index, and with many industry led initiatives addressing other areas highlighted in this survey.
 3. Whilst respondents from the IMRG survey of ISIS accredited retailers highlighted the requirement for improved standards within the industry as a means to encourage more consumers to shop online, there is a need to understand that there are less scrupulous trades people looking to offer sub-standard retailing experiences online and that this group is recognized to bring the whole industry into disrepute. Consumers are also vulnerable and concerned about these 'rogue traders' and this highlights the importance of an industry quality mark, such as ISIS, becoming a beacon of trust and confidence in the market place. This vehicle for self regulation, best practice and consumer confidence benefits both the consumer and retailer. The future growth of online is very much determined by attracting new consumers online and trust is an integral part of this.

International e-Retailing

The growth of online retailing is not a phenomenon limited to the UK. America has led the way, with online retail worth \$133 Billion in 2008 (emarketer, March 19, 2009) whilst European Markets are still developing at a slower rate than the UK. However, France saw e-retail sales reached €20.1 Billion in 2008, up 29% on the previous year. The French market also serves 22 Million online customers in 2008. Other key markets include Germany with e-retail sales of €19.3 Billion in 2008 (Bundesverband des Deutschen Versandhandels 03.02.09); and Spain, €758 million in Q3 2008 which is up 57.2% on the same period in 2007 (Comision del Mercado de las Telecomunicaciones, 20.01.09). Interestingly, 17% of this total was spent on foreign websites, indicating the appetite for cross-border trade in continental Europe.

The growth potential in these markets and the relative maturity of the UK market, is leading to an increasing interest from UK e-retailers in trading cross-border; both into continental Europe and further afield. Many UK e-retailers are in a strong position, having successful businesses in the UK, key understandings of the technology and providing a customer proposition and the positive benefit to the UK economy of this cross-border trade should not be underestimated.

Aside from the challenges of fulfillment, multi-lingual customer support and technology, the biggest barrier to cross-border trade within Europe is the variety of local interpretations of the Distance Selling Directive which places a significant cost barrier in the path of e-retailers looking to trade into continental Europe.

The UK can also provide an excellent staging post for companies looking to trade into the European Union. The provision of a stable digital network, the rich skills base available and geographical location can all provide substantial benefits to these organizations, and the UK economy. IMRG has seen a large increase in interest within its membership around cross-border trade and the ISIS community is also presenting similar views to the organization.

Conclusion

Consumer demand has been driving growth in the online consumption of products, services and content over the past 12 years. The consumer was in the marketplace first, with many retailers developing propositions to take advantage of consumer appetite and the increasingly competitive landscape that online retail drove. Consumer choice was the main beneficiary, whilst businesses were able to trade outside of their geographical regions and, in some instances, take on the high profile brands and dominate this new sector. Through this development, consumer protection has come to the forefront and, in many instances, affords the consumer greater protection than in the offline environment. New threats are emerging in the shape of fraud, data loss and identity theft. Many of these already existed in the offline world but, the face-less nature of online, and the reach of the network, has facilitated a rapid growth in these areas, with businesses currently bearing the brunt of the associated costs; there is very definitely a role for government to play in this area. Continued development of confidence schemes, such as ISIS, is central to the future development of the market and IMRG will be playing a full role in this process. International trading for online retailers is now coming to the fore in their development plans for the near future, with potential benefits to the UK economy and the opportunity for the UK to stand as a 'centre of excellence' in this field.

Considering the government's stated aims of increasing financial inclusion, reducing the digital divide, and developing the digital economy in the UK, online retail, its associated businesses, content providers and a stable digital platform are all elements that can play a major role in achieving these goals.