

Market share, profit margin, and marketing efficiency of early movers, bricks and clicks, and specialists in e-commerce

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Abstract

We examine three strategic issues that have been frequently discussed and debated in e-tailing: early mover advantages, bricks and clicks combinations as compared with pure-plays, and generalizing versus specializing. We develop hypotheses and test them utilizing annual and quarterly financial data from 42 public online retailers. We use a multilevel repeated-measures model to analyze our data because of its flexibility and ability to handle unbalanced repeated measures. The results indicate that early movers in e-commerce do not have a significant advantage in market share, profit margin, or marketing efficiency compared with later entrants. The bricks and clicks combinations in our sample possess higher market share and higher marketing efficiency than do pure-plays. Last, while specialists have lower market share and lower marketing efficiency, they nevertheless can be successful because they command higher profit margins than do generalists. The managerial implications of our findings are discussed.

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1. Introduction

Presently, empirical research on the strategic levers that drive e-tailer profitability and success is limited (Grewal et al., 2003). The few studies that are reported are largely managerial and descriptive and generally do not use sufficient controls or measures of variables such as size of firm and product category that can impact the success of a particular strategy (Bughin and Zeisser, 2001). Case studies and stories about individual stars, such as Amazon.com and Dell abound, are suggestive but hardly generalizable (Zhu and Kraemer, 2002). At the same time, existing research on offline retailing is likely to apply to e-tailing in a limited fashion, given that there are unique operational issues, such as website design, privacy, and security when selling online (Grewal et al., 2004). Thus, research studying strategic marketing issues in the online setting is likely to uncover findings unique to e-tailing environments.

In this research, we address three important strategic marketing issues in e-commerce simultaneously. First, we

examine whether there are early mover advantages in the e-commerce context. Writers have argued for and against their presence in e-tailing. For example, Porter (2001) argues that the first mover advantage in the Internet is a myth, specifically suggesting that, “switching costs are likely to be lower, not higher, on the Internet than they are for traditional ways of doing business... on the Internet, buyers can often switch suppliers with just a few mouse clicks” (p. 68). On the other hand, Reichheld and Scheffer (2000) insist that “price doesn’t rule the web, trust does” and claim that they have observed the presence of significant “loyalty effects” in e-tailing. If first movers use their early entry to determine who their profitable customers are and what their customers want, and then successfully fulfill promises to customers, then, first movers will be the recipients of loyalty effects.

The second strategic issue that we address in this paper is how bricks and clicks combinations perform in Internet commerce as compared with pure-plays. Many pure dotcom players viewed the relative newness of e-commerce as an opportunity to introduce a new business and brand to an innovative audience. They believed that their new businesses would be more efficient than the older offline businesses, offering lower overhead, better prices, and, thus, competitive advantages as compared with offline counter-

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parts. Nevertheless, many industry analysts now predict that as the online channel evolves, “incumbents [bricks and clicks combinations] will have a golden opportunity” (Silverstein et al., 2001).

Another key research question is “Do specialists perform better than generalists do in e-tailing?” *Online specialists* carry narrow product lines with a deep assortment within each line. *Generalists* carry a wide product mix with varied product lines. Both strategies have been adopted and implemented online abundantly. The broad product line of generalists facilitates cross selling for e-tailers who have developed a trustworthy reputation. However, there may be advantages to specializing on the Internet because the web aggregates niche markets and offers consumers products that they may not be able to buy easily offline.

The main contributions of this study are twofold. First, we empirically test three widely discussed e-commerce strategies simultaneously. By doing so, we control a significant portion of variation in e-tailing performance. For instance, we test early mover advantage hypotheses, holding other important strategic variables constant, such as bricks and clicks, and specializing. Thus, we can more accurately assess the success of particular e-tailing strategies than do industry commentators. Second, we measure market share, profit margin, and marketing efficiency utilizing annual and quarterly financial data rather than focusing on intermediate performance measures, such as number of visitors or customer satisfaction, or on the penultimate outcome, survival. Thus, this study enriches the understanding of e-commerce strategies and their outcomes.

2. Hypotheses

In our development of hypotheses, we use three measures of online retailing performance: (1) market share, (2) profit margin, and (3) marketing efficiency. Market share has been widely used as a performance measure to assess first mover advantages in empirical (e.g., Kalyanaram and Urban, 1992; Urban et al., 1986; Robinson and Fornell, 1985) and theoretical studies (e.g., Bohlmann et al., 2002; Freshtman et al., 1990). We define profit margin as (sales revenue – cost of goods sold)/sales revenue. Profit margin is the proportion contributed to profit with one dollar of sales revenue; thus, lower profit margins are associated with lower profit levels. Finally, we define marketing efficiency as sales revenue/marketing and selling expenses. Marketing efficiency is the sales revenue response to one dollar of marketing and selling spending.

2.1. Early mover advantages in online retailing

The excellent survey of Lieberman and Montgomery (1988) of the literature suggests that first mover advantage

can arise from several sources, including a pioneer’s pre-emption of assets, learning and patent protection, buyer preference for the pioneering brand, and buyer switching costs. Ample empirical studies on first mover advantages find that early movers have greater market share (e.g., Urban et al., 1986; Robinson, 1988; Robinson and Fornell, 1985) and enjoy higher consumer trial and repeat purchase rates than later entering brands do (Kalyanaram and Urban’s, 1992).

Early mover advantages in e-tailing can be both customer- and producer-based (Golder and Tellis, 1993). Potential customer-based advantages in e-commerce include (1) customer familiarity with a specific website and its features and (2) the trust that results when a customer successfully places an order and receives items (Jarvenpaa and Tractinsky, 1999; Reichheld and Scheffer, 2000; Urban et al., 2000). An additional possible customer-based benefit for early e-commerce movers is the ability to gain superior knowledge about customers. If this information is used in a way that respects consumer interests, time, and privacy, early movers will be able to leverage their accumulated customer knowledge to a greater degree than later entrants can.

In addition to the customer-based benefits, there are possible producer-based benefits. These benefits include desirable website names, partnerships with major portals and content sites, and affiliate relationships. Early entrants may have more access to financial resources than do later movers. Economies of scale and learning can lead to lower costs for early entrants (Robinson and Fornell, 1985; Urban et al., 1986). Finally, staying at the forefront of technology may enable early movers to offer better website functionality and more efficient and effective fulfillment than their competitors.

But there may be disadvantages for early entry as well (Golder and Tellis, 1993; Lieberman and Montgomery, 1988). At least three disadvantages are directly relevant to e-commerce. First, in e-commerce, late movers can “free ride” on early movers’ investments, including improved buyer education and awareness and increased security of transactions and other infrastructure development. The effect of free riding might be substantial, as early movers in e-commerce faced skeptical customers who were hesitant to make an online purchase (Greenspan, 2002).

Second, late movers can enter after technological uncertainties in e-commerce are resolved. In many new-product markets, technological uncertainty is resolved through the emergence of a dominant design (Suarez and Utterback, 1995; Christensen et al., 1998). While the standardization of web design principles is still not complete, each year of “Internet time” has brought increased understanding of web design principles and improved customer conversion rates (Nielsen, 2001; Nielsen and Tahir, 2002; Pastore, 2000a).

Third, in e-commerce, customer needs and expectations when shopping online often have not been well understood, especially by early entrants. Only in recent years

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