

Disruption at Our Doorstep

*A Strategic Perspective on Nordic e-Commerce
and the Imminent Arrival of Amazon*



The Boston Consulting Group (BCG) is a global management consulting firm and the world's leading advisor on business strategy. We partner with clients from the private, public, and not-for-profit sectors in all regions to identify their highest-value opportunities, address their most critical challenges, and transform their enterprises. Our customized approach combines deep insight into the dynamics of companies and markets with close collaboration at all levels of the client organization. This ensures that our clients achieve sustainable competitive advantage, build more capable organizations, and secure lasting results. Founded in 1963, BCG is a private company with offices in more than 90 cities in 50 countries. For more information, please visit bcg.com.

Axcelfuture is a Danish think tank striving to improve the investment climate in Denmark in order to foster prosperity, growth, and jobs. We are a small but targeted organization that operates through a broad network, which spans industry, government, and civil society. Every day, we seek to combine in-depth economic analyses and academic research with hands-on experience from the business world in order to contribute actively to concrete change. We seek to bring insights to a broad audience through events and media visibility, and we participate in the economic debate through our own investment indicator and economic transition model. Our reports, articles, and other publications are available on our website: www.axcelfuture.dk.



THE BOSTON CONSULTING GROUP

AXCEL FUTURE

Disruption at Our Doorstep

*A Strategic Perspective on Nordic e-Commerce
and the Imminent Arrival of Amazon*

**Mai-Britt Poulsen, Emil Stamp, Anker W. Gram, Joachim Sperling, and Katrine
Ellersgaard Nielsen**

May 2018

AT A GLANCE

Nordic e-commerce is booming. Amazon's arrival is likely to accelerate this trend, transform business, and affect society at large in the Nordics.

E-COMMERCE: A VITAL CHANNEL ON A STEEP GROWTH TRAJECTORY

Over the past five years, as Nordic consumers have embraced online shopping—converted by price, convenience, and availability—e-commerce sales have outgrown brick-and-mortar stores' sales by roughly 800%, and the e-commerce tailwind is expected to continue.

AMAZON: GOLIATH APPROACHES

The impending entrance of the e-commerce giant Amazon threatens to disrupt this burgeoning market, put pressure on Nordic players, and, in the long run, impact society.

COEXISTENCE: A STRATEGY MUST BE IN PLACE

Nordic companies face a strategic dilemma—join with Amazon or fight back? Either way, it could be a bumpy ride, and Nordic companies must take action. The Nordics must also determine how to handle Amazon's potential rise to a strong market position, prepare the workforce for a digital economy, and secure e-commerce tax revenue. Preparation by all parties will be critical.

E-COMMERCE IS TAKING HOLD and rapidly growing in the Nordics. But the impending entrance of e-commerce giants, such as Amazon, threatens to overwhelm this burgeoning market. While the change in the e-commerce landscape will benefit consumers at first—bringing broader selection, lower prices, and increased convenience—it will put immense pressure on Nordic e-tailers and bring dislocation to brick-and-mortar stores. How should Nordic countries, retailers and consumer companies prepare for coexistence with digital powerhouses like Amazon?

e-Commerce: A Vital Channel on a Steep Growth Trajectory

The Nordic business-to-consumer e-commerce market for tangible goods (not including services) is sizable and booming; it reached roughly €20 billion in 2017, and today it is a critical channel for consumer packaged goods companies and retailers. Nordic consumers have embraced online shopping—converted by price, convenience, and availability. As a result, Nordic e-commerce has experienced impressive growth—across all categories and countries—outgrowing physical store sales growth by 800% and reducing total brick-and-mortar store space by 1% over the past five years.

Nordic e-commerce has outgrown physical store sales by 800% over the past five years.

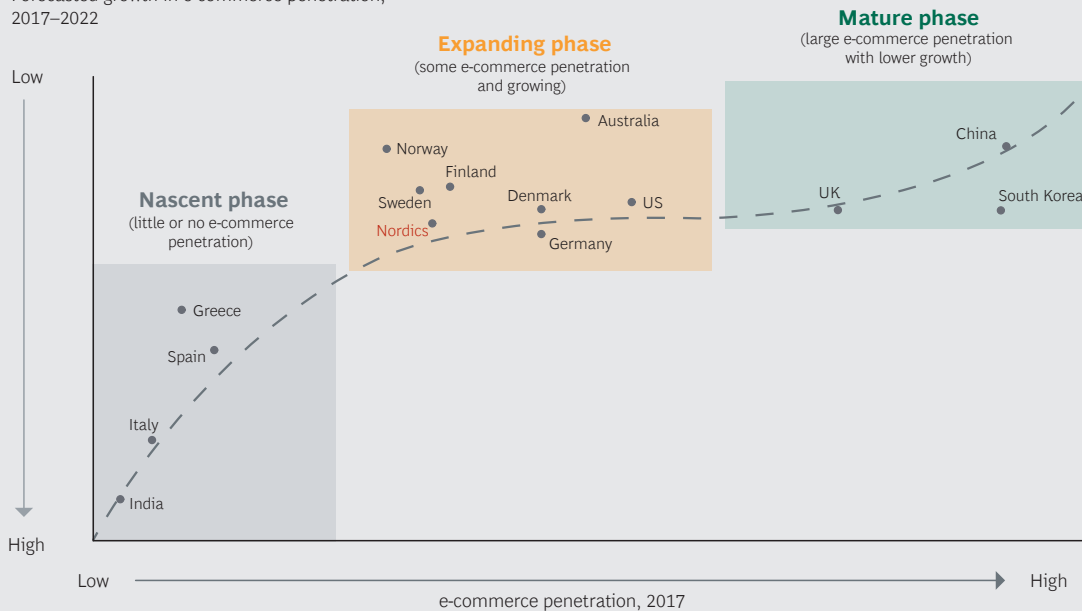
Compared to more developed e-commerce markets, the Nordics are less mature. Nordic e-commerce has advanced from the nascent phase, with little or no online retail penetration, to the expanding phase, with some (growing) e-commerce penetration. And while Nordic e-penetration is behind the curve, it is expected to continue double-digit growth in the next five years. (See Exhibit 1.)

For Nordic e-commerce to sustain its steep growth trajectory, it is vital to ramp up, tap into additional online opportunities, and get Nordic consumers on board. While Nordic consumers enjoy shopping online, their purchasing frequency is low compared with consumers in the UK and the US. In addition, online offerings are limited—because national retailers have not fully embraced the online agenda, and international players have not viewed the Nordics as a priority.

The result is a highly fragmented e-commerce market—not least due to the absence of extensive marketplaces (such as Amazon and Alibaba) that play a key role in mature markets. While some national online marketplaces are starting to emerge in the Nordics, their scope is narrow in terms of geography and categories. Consumers are thus turning to cross-border shopping through international e-commerce platforms, such as Amazon, which hold only marginal market share in the Nordics compared to their focus markets. Although there is some consolidation in certain vertical markets, the top three players in Nordics e-commerce hold an insignificant

EXHIBIT 1 | Nordic e-Commerce Is in the Expanding Phase

Forecasted growth in e-commerce penetration, 2017–2022



Sources: Forrester; BCG analysis.

market share (9% in Denmark and 21% in Norway) compared with a 50% or higher share for top cross-category players in mature markets (47% in the UK, 64% in Germany, and 58% in the US). (See Exhibit 2.) Thus further consolidation is anticipated.

The time to seize the online growth opportunities is now. E-penetration in the Nordics is behind the curve compared with the UK, Germany, and the US. And global e-commerce trends—such as the rise of big data analytics, faster (and better) delivery service, and an increasing share of brick-and-mortar stores entering the e-commerce space—will add to the competition. But it is likely that the biggest disruptor of all will be when the online marketplace powerhouses—such as Amazon and Alibaba—invest in the Nordics in order to take a leading online position.

To get ready for Amazon's arrival requires understanding who Amazon is.

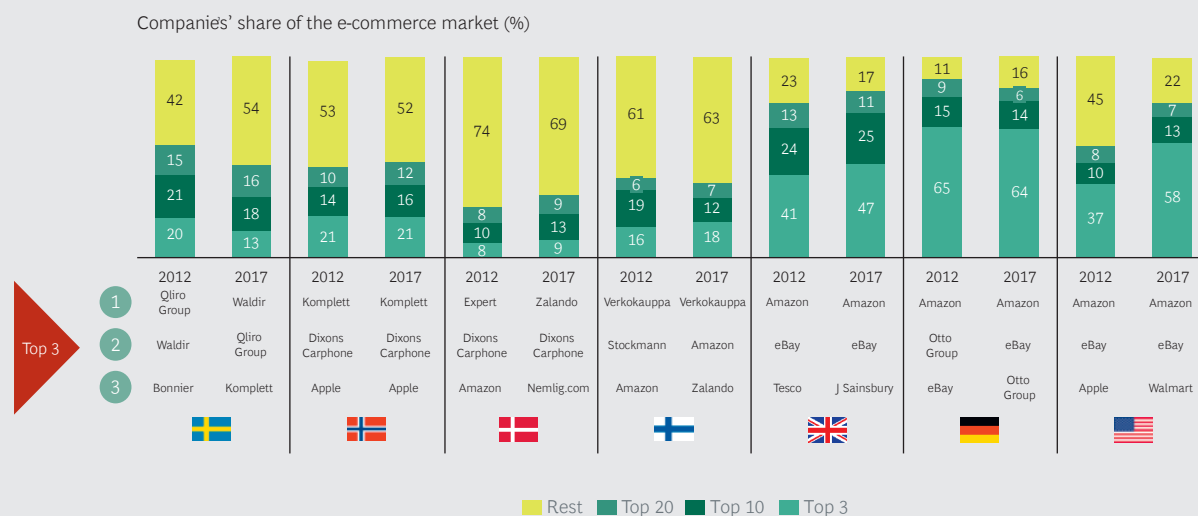
Amazon: Goliath Approaches

While the Nordic countries face the prospect of physical entry from multiple international giants, such as Amazon, Alibaba, and Tencent, it is Amazon that is being monitored most closely. Amazon already has a physical presence in surrounding markets (the UK, Germany, and Poland), while its Chinese counterparts have been more focused on their home market and the surrounding region.

While Amazon is not new to Nordic consumers—it enjoyed an approximate 2% market share in 2017 through cross-border trading—its physical presence foreshadows a more profound effect on Nordic consumer companies and countries. There is still time to prepare, but it is running out.

EXHIBIT 2 | In Mature Markets, the Top Three Players Hold About 50% Market Share

AMAZON IS THE CLEAR LEADER IN THE UK, GERMANY, AND THE US



Sources: Euromonitor; press searches; annual reports; BCG analysis.

Note: For the purpose of this analysis, total sales of private-label brands have been aggregated.

THE BUSINESS ANGLE

To get ready for the arrival of Amazon requires understanding who Amazon is, the disruption it is likely to cause, its game plan for the Nordics, its likely market share development, and which businesses will be affected.

Amazon at a Glance. Amazon attracts customers by offering the broadest selection in the market (500+ million stock keeping units, or SKUs), competitive pricing, and fast delivery. In addition, the company excels in optimizing the customer experience through its big data advantage. Amazon is a leader in collecting, storing, processing, and analyzing information in order to anticipate customers' needs—and build loyalty. For example, by analyzing what customers purchased in the past, added to their shopping cart or wish list, and reviewed or searched, Amazon can suggest additional items that customers might be interested in and encourage impulse purchases—so as to increase satisfaction and sales.

Amazon is not short on success—or ambition. As the third-largest global retailer (after Walmart and CVS) with 2017 revenue of \$178 billion, the company is now vying for the number two spot, driven by impressive growth—a 24% compound annual growth rate (CAGR) in revenue from 2012 to 2017, including acquisitions (the most recent of which is Whole Foods). With a market cap of roughly \$750 billion, it has now joined the race with Alphabet and Apple to reach the \$1 trillion mark. But it is not only Amazon's economic achievements that drive its future. Amazon's formula for success builds on three critical values: customer obsession, passion for innovation, and operational excellence.

Amazon has pushed the limits, creating a gap with its competitors that will be difficult to close.

In Amazon's 2016 annual shareholder letter, the CEO and founder outlines how Amazon can continue its successful trajectory through "True Customer Obsession": "Customers are always beautifully, wonderfully dissatisfied, even when they report being happy and business is great. Even when they don't yet know it, customers want something better, and your desire to delight customers will drive you to invent on their behalf." Its culture of putting customers first has led Amazon to constantly improve the way it serves customers. Its Prime membership program, for example, is now a vital component of Amazon's strategy that gives loyal customers better services (such as faster and cheaper delivery options). More recently, Amazon introduced its Prime members to a key service, which delivers purchases to customers' cars (without requiring a key), heading toward customers providing Amazon access to their private homes for direct deliveries to their refrigerators.

An important part of customer obsession is to be able to translate understanding of customers' needs into new and improved solutions. Passion for innovation enables Amazon to make it happen. Kindle and Alexa illustrate this clearly: they create a "seamless experience" for customers, while driving more sales as standalone products with a link to the platform. But innovation at Amazon is not only about creating new physical products: Amazon was a frontrunner in marketing a modern cloud infrastructure service—today known as Amazon Web Services (AWS). AWS contributed \$4 billion in operating income in fiscal year 2017—driving the largest part of Amazon's operating income.

The third critical value is Amazon's focus on operational excellence—always on the lookout to optimize. At many of its fulfillment centers, Amazon's process and technology leaders continuously scout for opportunities to improve processes and introduce new technologies. For example, to maximize storage density and product flow, every item received from suppliers is categorized and stored based on dimension and velocity. To minimize transportation inefficiencies, the system suggests an optimal box size to the packer, based on overall order dimensions. In addition, Amazon owns a truck and jet fleet, employs an Uber-style delivery system, uses robotics in fulfillment, and has recently opened a physical store without cashiers, resulting in a highly efficient machine.

The company's relentless mission to always improve customer experience, innovate, and drive efficiency has pushed the limits, creating a gap with its competitors that will be difficult to close.

True Disruption. Amazon is disrupting the markets it enters. Not only do the combined weight of its broad offering, attractive prices, and high-quality delivery enable it to quickly capture market share in new markets, it also holds a leading position in many markets where it is physically present (roughly 45% in the US, 40% in Germany, and 30% in the UK). Benefitting from this are the consumers and the companies that successfully join the platform and leverage the vast customer base and traffic. On the other side of the equation, there are local marketplaces with inferior value propositions and retailers lacking clear differentiators that often have to surrender market share to the new entrant—or, in a worst case scenario, shut down completely (as in the case of Best Buy's marketplace and Toys "R" Us). It is critical for local players to carefully consider how best to prosper and survive in the

“Amazon world.” (See the sidebar “A Nordic Sports and Apparel Retailer Discusses the Risk of Being Squeezed from Both Ends.”)

When Amazon moves into the Nordics, it will put pressure on Nordic retailers and the profit pool. The company is not necessarily a price leader, but it is a very efficient price follower, thanks to its advanced pricing algorithm. The algorithm constantly scans competitors’ prices and, in real time, adjusts prices to match the lowest value on the top-selling items in the market. Every time a retailer drops the price on a product to drive more traffic through its channels, Amazon’s algorithm follows suit, effectively mirroring every promotion and every delisting. In addition, unlike typical brands and retailers, Amazon does not look at the profitability of each single item or transaction, but puts all its energy on maximizing its share of the household’s total spend across goods, services, and delivery models, thereby pressuring the overall profit pool.

This pressure will be especially problematic for the Nordic pure e-tailers that typically suffer from low profitability (with 1% to 4% average EBITDA margins across

A NORDIC SPORTS AND APPAREL RETAILER DISCUSSES THE RISK OF BEING SQUEEZED FROM BOTH ENDS

For a Nordic sports and apparel retailer, e-commerce is critical to staying in business. “It’s virtually a life-or-death situation for our business—e-commerce represents about 20% of our total sales today,” the CEO told us. This retailer adopted e-commerce early on and has a substantial online presence. He commented, “It takes a long time to get everything to work, to get employees onboard. If you haven’t started by now, it’s already too late.”

“We are facing threats from strong international apparel marketplaces, Amazon’s potential entry into the Nordics, and brands that might increasingly focus on their own stores and e-commerce,” he noted. “The risk for us,” he said, “is being squeezed in the middle, where we can’t deliver the full experience that brands can through their own channels, and we don’t have the breadth of the marketplaces.” He told us that

“We are less afraid of Amazon in terms of price and delivery options, as we already have very low price points and next-day delivery.” He quickly added, “It’s their analytics capabilities that I fear the most. Only a fool doesn’t fear Amazon.”

Despite the potential for a “winner takes all” in this category, he told us, “I fully believe that we, as a specialty retailer, have a role to play and that an omnichannel offering will continue to be in high demand—although we face some tougher years first, with reduction in square meters from store closures. We provide a complete omnichannel experience in which our customers get professional service, advice, and the full product touch and feel. In addition, we have a large membership base (which provides data on our customers) and strong relationships with large manufacturers (allowing us to get the newest assortment).

categories as compared with 8.5% for Amazon in 2017). Many of these players have limited financial leeway to compete against Amazon. This is especially true within categories such as appliances, electronics, baby equipment, food, and toys and games, which are on the lower end of the profitability range. Across all categories, though, there are pure players that enjoy higher profitability and will be better protected, as well as categories in which Amazon will have a weaker value proposition (for example, fashion and apparel).

Amazon's Game Plan for the Nordics. Amazon's teams in Europe have already conducted extensive due diligence on the Nordic markets. According to experts, Amazon has detailed country profiles with demographics, population density mapping, economics, market landscaping (size, growth, trends, and competitor benchmarks), and logistics capabilities (carrier profiles, capabilities, and last-mile delivery availability). Once Amazon decides to enter the Nordics, it will know the territory and it will move fast. Even now, Amazon's presence in the Nordics is gradually growing, indicating physical entry in the near future. Through its recent introduction of AWS in the Nordics (offices in Denmark and Sweden, and three data centers envisioned for Stockholm by the end of 2018) and an ongoing active search for talent to support this development, Amazon is stepping into the two largest Nordic e-commerce markets.

Once Amazon decides to enter the Nordics, it will know the territory and it will move fast.

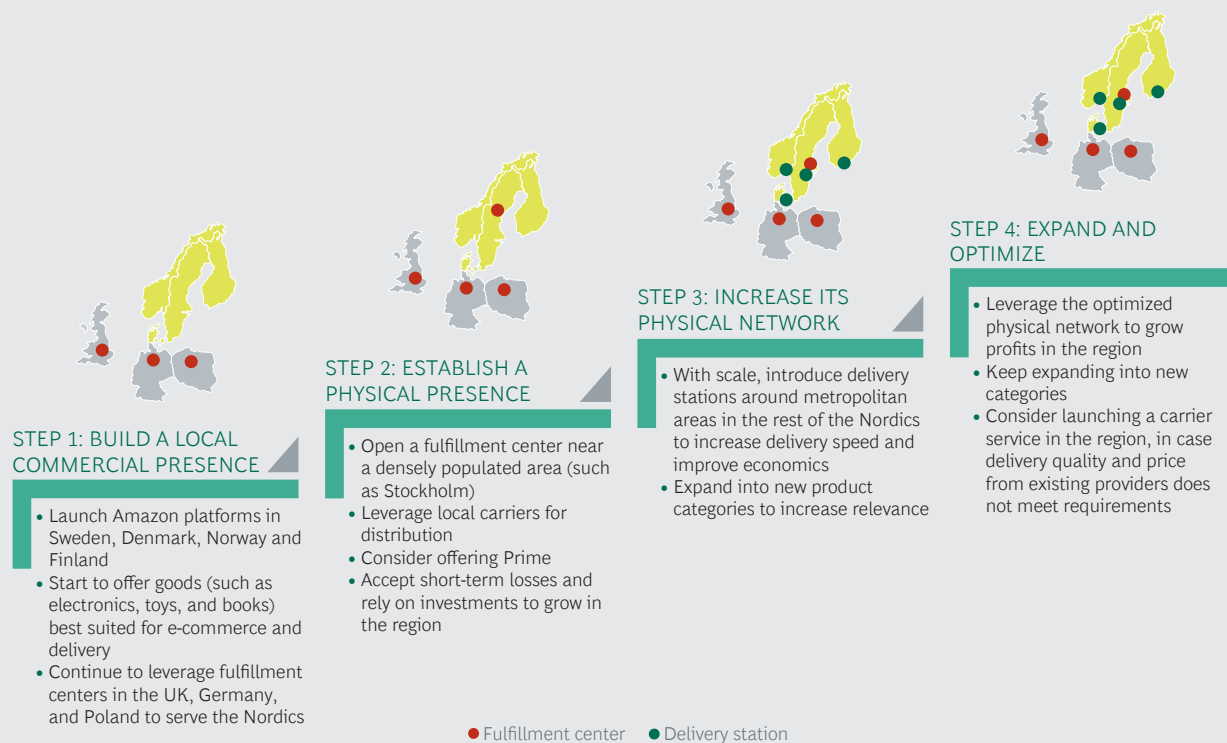
Amazon is well positioned to enter the Nordics, and it can leverage its battle-tested playbook for market entry. It will likely follow a multistep approach. First, it will introduce national platforms, while still serving the Nordic markets from nearby countries. Then it will set up a physical presence with a Nordic fulfillment hub to serve the largest customer pool. From there, it will gradually increase the density of its physical network via delivery stations near Nordic metropolitan areas. Finally, Amazon will focus on optimizing its operations and maximizing its penetration through category expansion. (See Exhibit 3.)

Amazon's Nordic Market Share Is Likely to Increase Quickly. The timing of entry and the speed of expansion will depend on Amazon's willingness to invest in the Nordic region. In particular, the specific category rollout plan and the breadth of Prime membership accessibility will shape market share development. Amazon will need to balance its investments in the Nordics with its numerous other opportunities: growing a fresh foods proposition in the US; expanding in large markets such as India, Brazil, and Mexico; and continuing to build relationships with manufacturers.

Depending on how actively it pursues expansion into the Nordics, BCG estimates that Amazon may capture between 8% and 20% of the e-commerce market within five years. (See Exhibit 4.) The lower limit assumes a more moderate focus on the Nordics, while the upper end depicts a more aggressive scenario. Among the reasons favoring more rapid entry are that Nordic consumers are comfortable shopping online, Amazon is already playing a role today, and the markets, which are highly fragmented, lack a strong online leader across categories. This creates a "white spot," in which a strong player can enter and quickly gain market share.

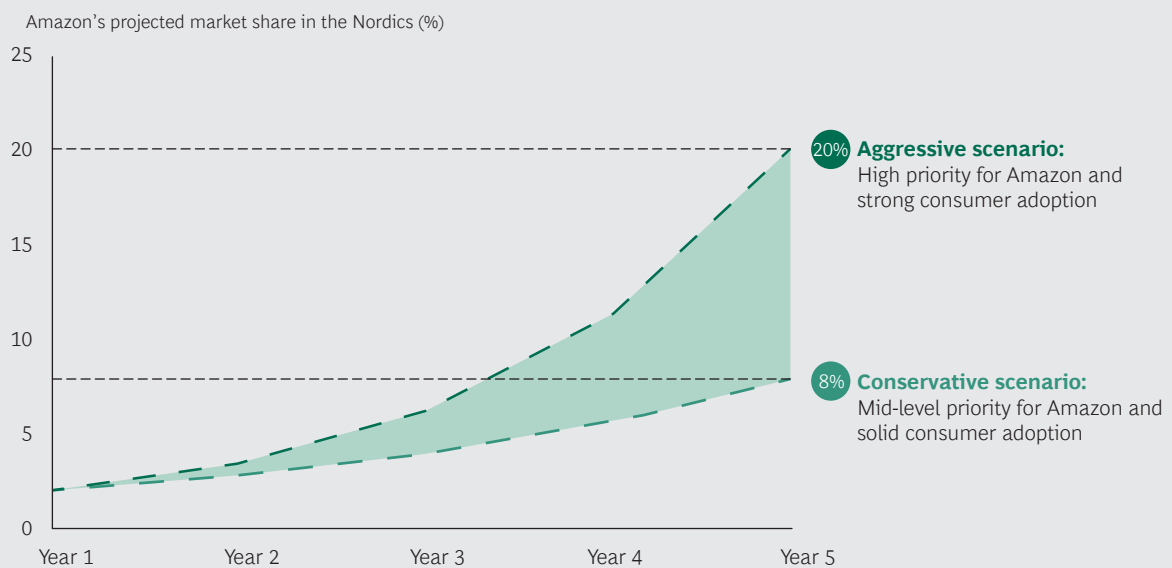
All Businesses Will Be Affected. Brands, retailers and marketplaces will all be affected by Amazon's entry. The degree of impact—threat or opportunity—will

EXHIBIT 3 | Amazon Is Likely to Take a Battle-Tested Approach to Entering the Nordics



Sources: News articles; Insider Nordic; interviews with experts; BCG analysis.

EXHIBIT 4 | Within Five Years of Expansion into the Nordics, Amazon Could Capture 20% of the e-Commerce Market



Sources: Interviews with experts; BCG analysis.

depend on their category play and their ability to differentiate themselves. Pure e-tailers and marketplaces—in direct competition with Amazon—will face the biggest challenge.

THE SOCIETAL PERSPECTIVE

Amazon's entry into the Nordics will also change the fabric of society. To prepare for Amazon's arrival, it is essential to assess the full impact of this strong market leader on society at large, the effect of the transition to a digital economy on the labor market, and the resulting reductions in tax revenue.

The Impact of a Strong Market Leader. Amazon's entry into the Nordics will accelerate the migration from brick-and-mortar stores to e-commerce and facilitate even more cross-border trade. Macroeconomic research shows that cross-border e-commerce has a positive effect on GDP, benefiting consumers and society as a whole.

At first, the entry of Amazon will bring lower prices, enhance the variety of products, and provide greater convenience—all of which are magnets for consumers. But in the longer run, as Amazon gains a stronghold in the markets, it could stifle competition and theoretically have greater incentives to raise prices and offer lower-quality products and services, no longer favoring customers. The risk of this happening, though, is considered low, because it goes against Amazon's culture of putting customers first.

The Effect of the Transition to a Digital Economy. Amazon's increased presence in the Nordics will accelerate the transition to a digital economy—including automation (in which it invests heavily)—and intensify the pressure on brick-and-mortar retailers. The result will be a shift in the labor markets. As machines replace workers throughout the supply chain, and brick-and-mortar stores are forced to downsize, jobs will be lost (1 out of 17 employees works in the retail industry in the Nordics). Despite the fact that dismissed workers will fill job gaps in other areas in the long run, the question is, how long will the transition take and how costly will it be?

Nordic consumer companies face a dilemma—should they join with Amazon or fight back?

The Resulting Reductions in Tax Revenue. The transition toward a digital economy and e-commerce will likely come at the expense of tax revenue to the Nordics—money that is needed to fund public expenditures, such as welfare. Even now, 25% of Nordic online shopping is for cross-border purchases, which to a certain extent enable consumers to avoid the high Nordic value-added tax (VAT). In addition, outdated international tax laws, based on companies' physical presence, fail to capture the value of the data that companies collect through their e-commerce transactions, which can be monetized—resulting in a loss of tax revenue.

Coexistence: A Strategy Must Be in Place

Preparing now is essential to dealing with the disruption to Nordic businesses, and its effects on society, posed by the arrival of Amazon.

THE JOIN-OR-FIGHT DILEMMA

In anticipation of Amazon's arrival, Nordic consumer companies face a strategic dilemma—should they join with Amazon or should they fight back? (See Exhibit 5.)

EXHIBIT 5 | The Choice Is Whether to Join With or Fight Amazon

OPTION 1: JOIN

Join with Amazon, playing with a full or selected proposition and assortment, while pushing your own e-tailing and other channels

Pros & Cons
(not exhaustive)

- Access larger customer base, traffic, and broader geographic scope
- Leverage fast and efficient logistic network
- Use easy-to-manage platform
- Take advantage of swift scale benefits (especially for small retailers)
- Price transparency leading to price erosion and channel conflicts
- Dependency on Amazon or possibly being bypassed
- Data is owned by Amazon, and pulling back on the decision can be costly

How to win?

- Choose the right partner model with Amazon
- Adapt your supply chain to serve Amazon's channel
- Decide how to optimize play with Amazon, such as segment assortment to ensure uniqueness and manage channel conflicts
- Set up strong internal management of key accounts with Amazon



Predominant strategy for brands
but also pursued by smaller retailers

OPTION 2: FIGHT

Exclude Amazon as a channel and instead leverage alternative channels or build your own capabilities to become a successful e-tailer

- No dependency on Amazon; full control of your own platform
- Potential to drive deeper customer relations and personalization
- No referral rates to pay; all profits go to you

- Missing out on the revenue potential from Amazon's traffic
- Impossible to match Amazon's scale and operational efficiency
- Risk of losing brand control if wholesalers sell on Amazon

- Build an ecosystem around your brand with strong customer loyalty
- Focus on your value proposition with proactive personalized customer relationships
- Integrate e-commerce strategy with your physical store network
- Drive operational efficiency, reduce costs, and preserve margins



Predominant strategy for retailers but also
pursued by some brands (rarely for the long term)

Source: BCG analysis.

The answer to that question depends on understanding what makes a market attractive to Amazon, the extent of Amazon's focus on a particular category, and the fit with Amazon's capabilities and value proposition. This assessment will enable companies to gauge how exposed their market will be and to take precautionary measures. For example, Amazon will likely focus on categories that are more homogeneous (the same no matter where they are bought), commoditized (where there is vigorous price competition and transparency), and highly penetrated by e-commerce, such as books and media, electronics, and toys and games—all of which are a good fit with its value proposition. Fresh goods and more specialized categories (like fashion and furniture), on the other hand, will be of less interest to Amazon—at least in the short run.

Joining: Partnering for Success, Preparing for Failure. Amazon can be a great opportunity for brands and for some (mainly small) retailers. But if a company decides to join with Amazon, it is essential not to walk into the partnership with high hopes and no specific plan—Amazon will then come out on top.

To make it a fruitful partnership, companies need to pursue the benefits Amazon has to offer: Amazon is not just a sales channel, it is also a marketing channel that

A NON-FOOD PRIVATE-LABEL RETAILER EYES OPPORTUNITIES WITH AMAZON

Although this non-food private-label Nordic retailer knows that most customers start their shopping journey online before venturing into stores to buy, it is in the nascent phase of e-commerce (with an online showroom but no online sales). Thus for this retailer, it is vital to strengthen its online channel.

This retailer doesn't perceive Amazon as a threat, but rather as a potential partner that would provide access to a vast customer base. Critical to its consideration of such a partnership is that this Nordic retailer remain in charge of the customer relationship.

He commented, "It is very difficult to develop brands on Amazon. We

need to pursue e-commerce through our own channels and make sure that these channels are our primary way of engaging with customers—so that we own the customer relationship and customer experience."

The company believes that it has a strong enough brand to prevent Amazon from taking business away from it (for example, by introducing similar products without the private-label brand). A strategy must be in place, the company acknowledges. And it has started a dialog with Amazon about what a future "join" model could look like.

can help drive sales and increase consumers' awareness. (See the sidebar "A Non-Food Private-Label Retailer Eyes Opportunities with Amazon.") And moving fast can bring benefits: Amazon provides a clear first-mover advantage, driven by its algorithms. (A company can't buy a good shelf position, but the first onboard the platform is more likely to get one—and once a company attains this position, it is very difficult for others to break in.)

For most brands, it is more a question of "when" than of "if" to join with Amazon. It is important to join with a clear strategy in mind about how to leverage the various sales channels (and make them work together)—so that the brand maintains control over its product range, customer experience, and brand positioning.

Nike, for example, avoided a direct relationship with Amazon, but its products were sold on the marketplace anyway; in 2017, it reconsidered and entered into a partnership with Amazon. The exception is high-end luxury brands (such as Chanel and Prada) that typically do not sell their products on marketplaces in order to protect their brand.

Joining with Amazon can also work for small and local retailers looking to expand their reach without overstepping their budgets—leveraging Amazon's online platform and fulfillment centers to scale up their business much more quickly than would have been possible otherwise.

Whether a partnership will be fruitful depends on multiple key strategic choices, ranging from how to sell through Amazon and manage fulfillment, how to determine channel strategy and deal with channel conflicts, which part of the product range to list, and how to allocate marketing spend. In addition, businesses must assess how to adapt their organizations and capabilities to meeting the needs of the partnership—specifically, how to manage the new relationship with Amazon, how to leverage Amazon’s data, how to strengthen the supply chain, and where to develop needed skills and capabilities (for example, in sales, marketing, and IT).

If a company does not make the right strategic decisions regarding the partnership, it risks losing on it. Take the story of Wühstof, a high-quality German knife manufacturer, that started selling its products directly on Amazon—an excellent deal for the company. But when Amazon started selling Wühstof’s products below the recommended retail price—damaging the brand image and reducing Wühstof’s sales from brick-and-mortar stores (which had been a significant share of its revenue), Wühstof decided to delist itself from Amazon.

If a company does not make the right strategic decisions regarding the partnership, it risks losing on it.

Or consider the fate of such small retailers as X Fire Paintball. This family-owned paintball shop had two brick-and-mortar stores and had been in business for 15 years before it decided to join with Amazon via the marketplace. After initial success and a boom in sales (up 400% in less than three years), Amazon started offering the same products on Amazon.com at lower prices by going directly to the supplier. As a result the family-owned retailer ended the partnership.

Fighting: Picking the Right Battleground. Any company that chooses to fight back must understand very clearly why Amazon is so successful and where its weaknesses lie—and then translate this information into strategy. Amazon’s key strengths are attractive prices, the broadest assortment of products, and high-speed, low-cost delivery. Companies should refrain from fighting Amazon on those dimensions alone. (See the sidebar “A Specialty Retailer Prepares for Competition Against Goliath.”) Amazon’s key vulnerabilities are limited personalization in presenting category offerings, only a small online community where consumers come together, and no integration with brick-and-mortar stores.

In general, success stories can be found among companies that know who their core customers are and use that knowledge to create a tailored value proposition. Companies that develop meaningful customer relationships and that can provide the complete customer experience will be able to claim their rightful positions in the market.

Take Ulta Beauty, an American makeup and cosmetics retailer that has created a powerful omnichannel experience by closely linking its stores and e-commerce. In addition, by providing salon services, it differentiates its in-store experience from that of other makeup and cosmetics retail stores. At the same time, customers are offered a true virtual shopping experience online that is similar to an in-store experience. Customers are able to buy products (using tools that assist, for instance, in the choice of color palettes), learn about products, interact with others through online forums and communities, and book appointments for beauty services.

A SPECIALTY RETAILER PREPARES FOR COMPETITION AGAINST GOLIATH

A Nordic specialty retailer sees a significant threat from Amazon's entry into the Nordics and is preparing for a fight. While the company recognizes that it is behind the curve and must define a clear digital strategy (regardless of what Amazon does), it understands the importance of e-commerce for its future success.

Amazon is already challenging this retailer through cross-border trading, and it will likely deliver a stronger punch once it enters the Nordics. For now, the retailer is less concerned about Amazon's ability to compete in terms of pricing (as its prices are very low) than it is of Amazon's owning the relationship with customers and shopping data. The retailer commented, "We are really concerned

that customers will think 'Amazon' every time they embark on a shopping trip."

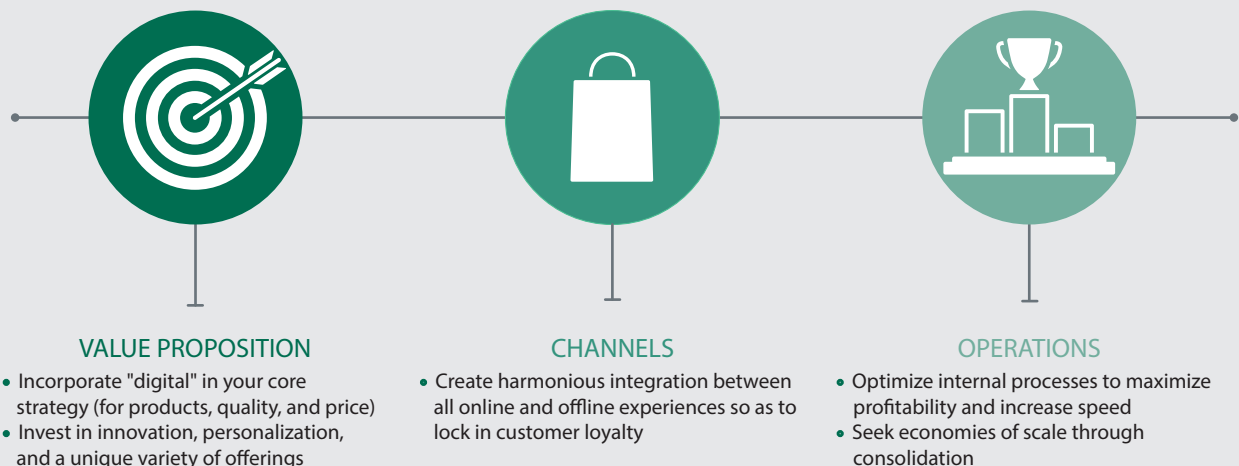
The retailer has identified three central elements in its strategy for differentiating itself from Amazon: becoming a complete-category specialty retailer, respected as an authority in its field; leveraging its brick-and-mortar store network and creating seamless integration between its online and brick-and-mortar store presence; and driving customer loyalty and engagement with its current customers through the use of its customer data. In addition, the retailer acknowledges the need to significantly step up operational excellence in its e-commerce as a "must have" in order to succeed.

For the majority of large retailers "fight" will be the inevitable answer—at least in the long run. The question is more about how to fight successfully. For retailers (both pure players and omnichannels), the key to winning is to focus on what differentiates them from Amazon—and at the same time ensure that all "hygiene factors" (such as price, quality, platform navigation, checkout processes, and delivery) are covered sufficiently. The most meaningful differentiators are brand image and recognition, content that entices, and proactive customer care and assistance—all of which, combined, drive traffic, convey trust, deepen relationships, and convert visitors into loyal customers. In addition, omnichannels have the advantage of being able to integrate all contact points with consumers—e-commerce and "touch and feel"—into one seamless experience, each reinforcing the other.

In addition, acquisitions and partnerships providing fast access to new capabilities or scale should also be considered part of the arsenal used to fight off Amazon, like the proposed J Sainsbury-Asda merger.

Building Strength for Whatever Lies Ahead. Whether companies decide to join with Amazon or to fight back, they have one thing in common: In order to be ready to seize the opportunity or to stand on their own, companies need to make sure "their houses are in order" so as to be prepared for what could be a bumpy ride. Specifically, they must improve their value proposition, channels, and operations. (See Exhibit 6.) It is not yet too late, but time is running out.

EXHIBIT 6 | Nordic Companies Need to Make Sure “Their Houses Are in Order”



Source: BCG analysis.

THE KEY DECISIONS FOR NORDIC SOCIETY

It is important to assess the potential impacts of Amazon's arrival on Nordic society at large. Specifically, how can we safeguard competitive markets going forward? How can we ease the transition to a digital economy? How can we ensure tax revenue from e-commerce transactions?

Safeguarding Competitive Markets Going Forward. There are European competition laws currently in effect in the Nordics to ensure fair competition across the business landscape. These laws prohibit companies that hold a dominant position in a market from squeezing out competitors and from abusing their position. It may be difficult, however, to detect anticompetitive behavior, and it may take years for the authorities to reach a determination on whether or not a company's behavior is illegal—during which time competitors struggle to maintain their businesses and consumers suffer. Further, while the fines for violations are significant, they may not be sufficiently large to discourage anticompetitive activities by giant companies.

While EU Competition Commissioner Margrethe Vestager believes that European competition law is robust, she recognizes that further regulation may be needed: “European competition law is very strong. But we have to be observant and agile in order to make sure that we have the right tools. . . . Of course, we will keep discussing how to understand old concepts and ask: do we need new regulation for the future as this digital revolution develops?”

Consideration should be given now as to whether Amazon's entry into the Nordics calls for new regulatory initiatives that provide open access to platforms on regulated terms. A concrete proposal for such regulation was published by the European Commission in April 2018. Vestager explains the motives behind the proposal: “We are proposing . . . that you have someone to turn to when suddenly someone locked

the door to your business and traffic is just falling like a stone through water. You need some sort of very basic rights as a business operator when you are dependent on a platform. And this we have proposed because unfortunately these unfair practices, they are a factor of business life today.”

Easing the Transition to a Digital Economy. The Nordics should undertake a number of initiatives now that will enable them to thrive in the coming digital economy. To increase their competitiveness in a new economic landscape, companies will need to boost their productivity—for example, by embracing and investing in automation. There is an urgent need for the educational system to teach and hone the skills required for an economy that holds fewer manual jobs and in which IT skills and an understanding of digital business strategies are vital. Initiatives must also be undertaken to educate, retrain, and upgrade the skills of displaced workers so they can continue to contribute to the workforce.

Ensuring Tax Revenue from e-Commerce Transactions. Initiatives are underway to ensure that tax revenue is not lost on e-commerce transactions. New EU rules on VAT, which will take effect in 2021, are intended to level the playing field among e-commerce players in high and low VAT countries. These rules call for a tax in the destination country (the buyer’s residence) on tangible e-commerce (more than €10,000) from cross-border sales. There also will be a new—and potentially costly—liability for e-commerce players (both established and emerging) to pay VAT on imports traded through their platforms. In addition, the European Commission proposes reforming corporate tax rules to cover digital activities. As a long-term solution, they will ensure that profits are registered and taxed where businesses and users interact through digital means. Until such rules are in place, they propose setting up an interim tax on 3% of revenue from three defined types of services, where value is created through user participation.

AS THE NORDICS anticipate Amazon’s arrival, it is imperative that the business community and society at large prepare for a sea change. Disruption is at our doorstep.

About the Authors

Mai-Britt Poulsen is a partner and managing director in the Copenhagen office of The Boston Consulting Group. You may contact her by email at poulsen.mai-britt@bcg.com.

Emil Stamp is a principal in the firm's Copenhagen office. You may contact him by email at stamp.emil@bcg.com.

Anker W. Gram is a consultant in BCG's Copenhagen office. You may contact him by email at gram.anker@bcg.com.

Joachim Sperling is director of Axcelfuture and head of corporate affairs at Axcel Management. You may contact him by email at js@axcel.dk.

Katrine Ellersgaard Nielsen is a senior economist at Axcelfuture. You may contact her by email at kel@axcelfuture.dk.

The authors from the Boston Consulting Group wrote and are responsible for the analysis and discussion of the market and business implications covered in this report. The authors from Axcelfuture wrote and are responsible for the assessment of and discussion on Nordic society.

Acknowledgments

The authors are grateful for the support of our colleagues who contributed their time and experience in providing insight for this report, especially Allan Lyall, Antonella Mei-Pochtler, and Gabrielle Novacek.

The authors would also like to thank Pamela Gilfond for her contributions to the writing of this report and the following members of the editorial and production teams: Katherine Andrews, Gary Callahan, Kim Friedman, Helen Rheem, and Sara Strassenreiter.

For Further Contact

If you would like to discuss this report, please contact one of the authors.

To find the latest BCG content and register to receive e-alerts on this topic or others, please visit bcg.com.

Follow The Boston Consulting Group on Facebook and Twitter.

© The Boston Consulting Group, Inc. 2018. All rights reserved.
5/18

BCG

THE BOSTON CONSULTING GROUP

—AXCELFUTURE