



## **Chapter II**

# **Building E-Commerce from the Ground Up: A Study of the Retail Industry**

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## **INTRODUCTION**

The selling of goods and services on the Internet has evolved from a hypothetical business concept into a thriving, multi-billion dollar industry which has prospects of sustained double-digit growth well into the first decade of the 2000s. This new market channel is estimated to achieve over \$108 billion in sales transactions by 2003 (*Business Week*, Sept. 1999). There are various definitions regarding what is meant by “electronic commerce,” however for the purposes of this chapter, we will confine our definition of the term to that segment of the retail industry which comprises sales transactions for products and services consummated via the Internet. This is a critical distinction from the far more vast array of literature devoted to companies’ use of electronic commerce such as Electronic Data Interchange for the purpose of reducing operating costs by streamlining productivity and efficiency. In short, we will limit our view of e-commerce to the business of selling goods and services via the Internet.

Within this realm of e-commerce, there are several critical issues that arise for companies seeking to open an e-commerce storefront. In this chapter, we will use the actual experiences of one retailer to highlight various approaches to those issues.

### **The Electronic Field of Dreams**

Conventional new store wisdom states that, if you build it, the customers will indeed come to your storefront. This is why the old adage “location, location, location” is all-important for a store. This is also why one store’s success will almost always guarantee that a friendly neighboring store will also be built to capitalize on the first store’s traffic. And, with traffic, stores typically realize proportional sales volume. Traditional traffic builders are print advertising, radio and television. Further, depending on whether the store is part of a larger chain or not, traffic can be driven to a new store location by in-store advertising at the other locations. The latter does not simply play a shell game with sales, moving sales from one location to the next, rather it helps build sales because word-of-mouth advertising about the presumably more convenient location starts driving new traffic to that location.

### **The Company**

For an example of what works and what does not, we will use the example of the Army and Air Force Exchange's (AAFES) site [www.aafes.com](http://www.aafes.com). AAFES is better known by its name of PX® or BX®, standing for Post Exchange (PX) and Base Exchange (BX) depending on whether one is on an Army post or Air Force base. A Post or Base Exchange is a full-line retail department store which is situated on a military posts or base. We chose AAFES as an example because, while AAFES is a part of the United States government, its profile is quite similar to that of a broad cross section of retailers such as Dayton-Hudson Corporation's Target chain of discount stores. As an entity of the federal government of the United States, AAFES' financial operations are also open for scrutiny without violating internal confidentiality that one would typically find with a civilian sector retailer. As such, this chapter delves into detail regarding how AAFES chose to inaugurate its e-commerce, how the site is promoted, and how the operation of the site is meeting expectations. In another respect, AAFES represents a closed environment which makes it ideal for our research.

One needs to understand some basics about AAFES in order to understand why AAFES made some of the decisions it did. AAFES is what is called a "non-appropriated instrumentality of the United States government." That translates: The organization is a Federal entity that does not receive tax dollars to operate. Instead, AAFES operates off of its self-generated revenues derived from retail sales made to authorized military customers. Net sales of more than \$6.3 billion in AAFES' fiscal year ending January 1999 make AAFES the eighth largest discount store operator in the United States. Retail operations encompass stores in more than 20 countries throughout the world; essentially, wherever there is a presence of United States armed forces.<sup>1</sup> Operations include more than 190 full-line discount department stores; 300 convenience stores; plus a variety of gas stations, electronics stores, and a full-line direct marketing operation. The latter produces a semi-annual catalog which is distributed to more than a half-million customers around the world.

AAFES also has the distinction of being the second largest Burger King® franchisee in the world with more than 170 restaurants in operation. AAFES provides a wide variety of other services including dry cleaning, optical shops, in-store banking, video rental, pizza delivery and operation of more than 170 movie theaters. AAFES is quite literally "The Company Store." A complete listing of all major business units within the organization and the respective sales for the most current fiscal year given in Appendix A.

There is competition. AAFES has competition both within the military retailing community and external competition from retailers who build large discount stores immediately outside the gates of military installations. Within the military resale community, there are two other similar military retailers: Nexcom, which sells to personnel of the United States Navy and the Marine Corps Exchange System which sells to personnel of the United States Marines Corps. Customers from any branch of the military service may shop at any of the military stores.

### **The Customers**

While AAFES' operation is in many ways a mirror image of various civilian-sector retailers and service providers, a key difference is that AAFES' potential customer base is finite. We use the word "potential" because, while customers may be authorized to shop the military resale stores, there is no assurance they actually do so. The customer base is finite because only active duty military, military retirees, and the National Guard and Reserve are authorized to shop at AAFES' facilities and Internet site. This provides a potential customer

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