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E-Business Transformation at the Crossroads: Sears' Dilemma

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E-BUSINESS TRANSFORMATION AT THE CROSSROADS: SEARS' DILEMMA[1]

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It was December 2002, and Garry Kelly, the newly appointed CIO of Sears, Roebuck & Company, looked out of his office window and contemplated the issues he needed to discuss in the management committee meeting the following day. Garry had arrived at Sears only a few weeks ago when the company was at a critical juncture. Sears' net income in 2001 had fallen to $735 million on a revenue level of $41.1 billion. These figures reflected only half of the profits it had recorded two years earlier, on a similar level of sales. Sears also faced intense competition from rival retailers across the nation, new dot-com e-tailers as well as from the specialty stores that had been eroding the profit base for the last couple of years. Investors, stakeholders, and employees were anxiously looking for signs of turnaround at the giant in the U.S. retailing industry.

Garry was brought in after the former CIO Jerry Miller suddenly moved out of the company, just days after Sears had announced its acquisition of Lands' End, a premier Internet and catalog clothier company. The company had appointed an interim CIO and Garry came as a replacement from the shoe retailer Payless ShoeSource.

Garry as well as the senior management at Sears clearly understood the impact of Internet on the retailing industry and had no second thoughts about their quest to exploit the Web for boosting the company's profitability. Although Sears had made significant investments in its online e-business initiatives, it was facing significant challenges in realizing the returns on these investments. A couple of issues were at the forefront of Garry's attention. These issues and challenges needed to be resolved to pave the way for future decisions and strategies pertaining to e-business.

While the customer base for online shopping was increasing steadily, Sears was facing severe competition. Sears sells a broad range of products from appliances to apparel, and had followed a largely incremental approach for moving its product range online. It was not clear if Sears needed to focus exclusively on a select line of products, or sell its entire set of products online. An added dilemma was whether to have multiple sites with different selling and return policies for different product categories, or to have a unified, integrated site with uniform product policies across all kinds of goods. Another issue was Sears' foray in the business-to-business e-commerce arena. In 2000, Sears joined hands with Oracle Corporation and Carrefour, a large retailer in Europe and Latin America, to form GlobalNetXchange, an on-line marketplace that would enable the suppliers and retailers to communicate, collaborate, and manage their supply chains. Sears and Carrefour expected to cut down their combined purchasing costs that totaled $80 billion annually and effectively manage a fleet of over 50,000 suppliers. Despite the investments in the B2B exchange, Sears faced mixed results.

Only six months ago, Sears had acquired one of the largest catalog and Internet specialty clothiers, Lands' End, being one of the most successful direct-only apparel companies, had a great brand appeal, sophisticated technological infrastructure, and sound operations backbone. Moreover, Lands' End had also made impressive strides in using the Internet to attract and improve their sales.

Lands' End recorded a net profit of $66.9 million, on sales of $1.6 billion at the end of 2001, making a margin of 4.3 percent, which was nearly double that of Sears' profitability. Given the successful operations of Lands' End, Sears has been moving with great caution in order not to disrupt the Web-sales and catalog operations of Lands' End. Both companies have significant

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[1]The authors prepared this case as a basis for class discussion, rather than to illustrate either effective or ineffective handling of an administrative situation.

differences in their product line, customer base, and brand appeal. However, the merger has paved the way for immense opportunities to multi-channel across stores, Web sites, and catalog operations. Sears can potentially offer its customers the opportunity to buy everything from automobile parts to shirts through any of its channels. Considerable synergies could be exploited in back-end business operations, marketing, promotion, and distribution. Could Sears take advantage of Lands' End's strengths to improve its own e-business efforts?

U.S. Retail Industry

Retail represents the second-largest industry in the United States both in number of establishments and number of employees. In 2003, the U.S. retail industry employed over 23 million individuals and generated more than $3 trillion in sales. Based on the type of products they sell, retailers are classified into two sectors: durable and nondurable. Durable goods include building, garden supplies, automobiles, computers, home furnishings ,and furniture. Nondurables include general merchandise, food, drugs, apparel, accessories, and such goods. Since 1988, the retail industry had grown between 4 and 5 percent annually, with sales of durable goods growing a bit faster than nondurables. A major portion of the nondurable sales came from stores in the general merchandise category that included department and discount stores.

Many retailers, including department and discount stores, had pursued rapid expansion strategies in the 1970s and 1980s, fueled by the rise in consumer spending. The retail square footage increased from 8 square feet to 19 square feet per capita between the years 1976 and 1995. This rapid expansion of retail stores and selling space ultimately resulted in an environment with many matured market segments. As a result, mergers, restructuring and consolidation activities intensified in the industry. (Exhibit 1 presents an overview of the U.S. retailing industry and Exhibit 2 presents the top retailers.) The commercialization of the Internet in the mid-1990s led to the emergence of a number of online retailing firms. Several virtual retailers like *Amazon.com* posed a serious challenge to traditional brick-and-mortar retailers. In response to the competition from new e-tailers, several brick-and-mortar companies launched their online channel in the late 1990s. By the turn of the millennium, the U.S. retail industry environment reflected a mature industry with considerable over-capacity. Exhibit 3 presents the trends in U.S. retailing industry, along with online retailing. Exhibit 4 shows the online market shares for pure play online retailers and the traditional firms. Exhibit 5 presents the online sales trends based on different product categories.

Sears, Roebuck and Company

The seeds of Sears were sown in 1886 when Richard Sears began the R. W. Sears Watch Company in Minnesota. A year later, he moved to Chicago and teamed up with Alvah C. Roebuck, and Sears, Roebuck and Company was born. In 1888, the company started its catalog business, which was the first of its kind in the country. The catalog operations were a huge success as Sears offered a wide variety of products that were not easily available to consumers. The Sears catalog for each season was welcomed with great anticipation and business soared. In 1925, the company expanded into retail store operations and opened its first retail store, and within four years the strength grew to 324 stores across the country. Sears' retail stores carried a variety of merchandise such as apparel, jewelry, cosmetics, electronics goods, tools, household appliances, cookware, and bedding. In the following decades, Sears grew rapidly, becoming an icon in the U.S. retailing industry.

By the early 1980s, discount stores such as Wal-Mart and K-Mart had become dominant forces in the retail industry, eroding Sears' market share. In an effort to boost its competitive position and performance, Sears tried a number of different retailing initiatives such as "store of the future," "everyday low pricing," and "stores within a store," and also diversified into financial services and real estate. But such initiatives bore little fruit. Profit margins continued to decline taking the company almost to the brink of bankruptcy. In 1992, Sears had a new leader for its retail operations, Arthur C. Martinez, who was named as the company's CEO three years later. Martinez faced the arduous task of turning around the company.

> Well, the company was in big trouble, really floundering. We were losing over $100 million in the catalog, retail was making zero money, and the credit business was making a couple of hundred million dollars. When you put the whole package, together there was no money and very little cash flow coming out of the retail business.[2]

[2]T. Savage, "T. Terry Savage Talks Money with Arthur Martinez," *Chicago Sun-Times*, April 29, 2001 (available online at **http://www.suntimes.com/savage/talk/arthur_martinez.html**).

Martinez took several cost cutting measures to improve profitability. He changed the product-mix and placed special emphasis on middle-class female customers. The reorientation was reflected in the new slogan, "Come see the softer side of Sears." Martinez also steered the credit card business that offered customers more flexibility in paying for their purchases at Sears. After a spate of restructuring exercises, Sears had operations in three broad areas: retailing, service, and credit. CEO Martinez said: "After the restructuring in '92, the business did take off in 1993. The sales trend was fantastic all the way through '97."[3] However, this revival was short-lived. Sales stagnated again and several key executives moved out of Sears. Competitors such as Home Depot, Lowe's, and Circuit City garnered considerable portions of Sears' market share. Other discount stores such as Old Navy, Target, and Wal-Mart chipped away at Sears' apparel business. An industry analyst described this situation as "It's been a middle market squeeze for Sears—from the department stores on one side and value-oriented business on the other."[4]

By this time, the e-commerce wave had started sweeping through corporate America. Many retailers were looking at exploiting the Web to promote, market, and sell their products. Sears was initially skeptical about the Internet. CEO Martinez remarked, "I was a serious skeptic for a long time…I saw this as a domain of fanatics."[5] However, subsequently, Sears started taking a serious look at the Internet to improve its profitability and performance. Exhibit 6 traces the key e-business initiatives at Sears.

Crawling in Cyberspace: E-Business Initiatives at Sears (1996-1999)

Sears had all the important pieces to be an early e-commerce leader, but the process of restructuring in the mid-1990s hurt its chances. Sears, in a partnership with IBM, owned 50 percent of Prodigy, one of the first commercialized online services. This could have given a lot of momentum to its online initiatives. However, as a part of corporate restructuring, the company sold its stake in Prodigy in 1996. Sears also had good distribution, fulfillment, and direct-marketing catalog operations, fundamental building blocks of a successful e-tail business. Yet, Sears closed its catalog operations in 1993. With such handicaps, Sears had to cautiously plan its e-business moves.

Sears made its online debut in 1996 as an information-only Web site. Sears did not add any transaction or selling capabilities to its Website as it preferred to wait-and-watch to see if electronic shopping would be a lucrative channel. In 1997, it decided to sell over 3,500 of its Craftsman tools online. Sears chose Craftsman tools as it wanted to experiment in online selling with a product line that not only had a strong business potential, but also a recognized brand name. "Craftsman is a brand where quality and features are well known, so there is a high chance of customer satisfaction and even higher chance of overall success,"[6] remarked a senior marketing executive. While the rival department stores were dealing with the complexities of selling apparel online, Sears stared its online selling with hard goods like Craftsman tools.

In an effort to experiment in online selling of softer products, Sears decided to sell gift items from its Christmas wish book catalog. The online experiment from Craftsman and the wish book products generated about $10 million in sales. Despite the encouraging results from this initial experimentation, serious skepticism arose among a section of executives on the viability and profitability of e-business. Skeptics pointed out that Sears had earlier tried both catalog and home shopping and the results had not met expectations. Having come a full circle, Sears might face the same experience with the Internet as well. Concerns were also raised about the problems in filling orders for bulky items such as washers and dryers. A section of executives also argued about the risks of cannibalization. They saw the Internet as a threat that would draw customers away from their retail stores. Even among those executives who favored e-business, it was not clear if the company should adopt a faster rollout of all its products online or if it should take an incremental, category-by-category approach to e-business transformation. Further, the company conducted focus group sessions to understand the potential impact of its online initiatives. "We discovered through focus groups that the Internet was a great mechanism for delivering solutions. Even if customers aren't comfortable buying online, the site is important for their

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[3]Ibid.

[4]E. Brown, "Big Business Meets the E-World," *Fortune* (140:9), November 1999, pp. 88-98.

[5]Ibid.

[6]D. Claymon, "IT Takes Tools," *Redherring*, February 1998.

product search,"[7] said a general manager. While the debates and arguments continued for several months, a clear mandate emerged from top management in favor of an incremental approach to moving online. "If we worry about cannibalization, we'll miss the opportunity,"[8] declared CEO Martinez. The CEO was convinced about moving online. The modest success of the initial e-business efforts resulted in stronger top management commitment. The CEO decided to go ahead with converting Sears into an effective brick-and-click organization. A new head was appointed for online ventures, and an internal Web team with about 35 employees was formed to exclusively focus on the e-business efforts.

> The notion that all old economy companies were going to be marginalized and put out of business was a laughter to me. The people who were advancing that view were talking out of their own self-interest, not a strategic viewpoint. We saw the Internet coming, and asked ourselves how we could use it as an additional channel of distribution and an additional channel for customer relations….It wasn't another new business model, just another tool in the toolkit of how to run your business [CEO Martinez].[9]

In early 1999, Sears took a major step by launching the *PartsDirect* site as a part of Sears.com to feature more than 4.2 million parts and accessories from over 400 manufacturers of appliances, power tools, and other home equipment. Apart from selling these parts, the site also included extensive assembly and repair manuals that would aid do-it-yourself customers.

Within a month of launching *PartsDirect*, Sears added its major appliances—refrigerators, freezers, stoves, dishwashers, washers and microwaves—to its Web site. "Major appliances are Sears' strength. We have 38 percent of the market. If you put the No. 2 through [No.] 15 retailers together, that's our market share,"[10] said an executive. Appliances were not only an area of traditional stronghold, but Sears also had the necessary infrastructure to take care of logistics, distribution, deliveries, installation, and repairs to make online selling possible. The appliance launch marked the online availability of over 2000 brand-name appliances that included popular names such as Kenmore (Sears' brand), GE, Maytag, and Whirlpool. Sears treated the Web site as an additional channel rather than as a separate business unit. The Web site served as a complementary channel for marketing and selling appliances, with Sears' 850 department stores and 680 dealer stores providing the backbone distribution infrastructure. To strongly integrate its Web operations with that of store retailing, Sears extended all the services such as repairs, warranty, pricing, etc. to online customers as well.

The experience from selling appliances online allayed the cannibalization fears in the minds of in-store salespeople. Sales representatives started realizing that their jobs were getting easier as the Web site educated customers about the varied products, schemes, and services. The appliance information and the side-by-side product comparison feature in the site greatly helped customers in their product research. The in-store sales crew began to appreciate the online channel as customers started bringing in printouts of online research to the stores to complete their purchases. Through an internal study, Sears also found that about 13 percent of customers who purchased goods from their stores used their Web site for some research prior to their purchases.

The next logical step for Sears was to market its online channel. Sears started banner ads on Microsoft's MSN network in mid-1999. It also pushed its marketing efforts by promoting Sears.com through television and print commercials. The company spent close to $100 million in marketing its Web site. In preparation for the holiday season, Sears also enhanced its Web site by adding holiday products and items, and by introducing new features such as product comparison aids. Sears also introduced its Sears card and gift card services online. "It's a truly clicks-and-mortar type of holiday season for Sears. Not only have online tool and appliance sales surpassed our expectations this season, but we have sold thousands of Sears gift cards online as well,"[11] said a general manager.

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[7]C. Zimmerman, "Partnerships Are Important to Sears Web Strategy," *InternetWeek,* February 1998 (available online at **http://www.redherring.com/mag/issue51/tools.html**).

[8]N. Brumbach, "Sears Sees Web Sites as Add-On Volume for All Inventory,"*Home Furnishing News*, March 1, 1999, p. 38.

[9]Savage, op cit.

[10]R. Williams, "The Software Side of Sears," *Interactive Week*, September 2001 (available online at **http://www.eweek.com/article2/0,4149,1243780,00.asp**).

[11]Sears press release, December 17, 1999.

By 1999, Sears had invested between $75 and $100 million in its e-business initiatives. In December 1999, Nielsen/Netratings ranked Sears.com fourth on its list of fast growing online properties. It also estimated that Sears.com had about 250 percent growth in terms of unique audience, or first-time visits to its site during the 1999 holiday shopping season. Site-performance tracker Media Metrix also reported Sears.com to be a leader in the online retail segment in terms of unique visitors, with about 1.9 million customers logging on at least one time in a month. Further, more than 90 percent of the online orders were completed perfectly, in terms of delivery times and correct fulfillment of the product and quantities.

By the end of 1999, Sears had 100 full-time employees exclusively working for its online division. Further, 50 employees from several departments were involved in different e-business projects. The company also started involving several departments and employees in its e-business initiatives. It also empowered its divisional managers to develop ideas for expanding the online presence of the company.

The Cyber Marathon: E-Business Initiatives between 2000 and 2002

By the turn of new millennium, a new crop of startups such as Homewarehouse.com, Hardware.com, and Ourhouse.com had emerged on the dot-com terrain. Moreover, some of Sears' suppliers also launched their own Web sites, trying to directly sell to customers. Discount stores such as K-Mart and Wal-Mart had stepped up their online efforts. K-Mart had launched an independent e-commerce spin-off, bluelight.com and Wal-Mart had started making impressive gains through its Wal-Mart.com site. Other competitors like J.C.Penny and Home Depot had also beefed up their Web sites to increase their online presence.

In an effort to counter the frenzied online competition, Sears decided to pursue a partnership approach to enhance its e-business efforts. To gain immediate access to capabilities that were not readily available within the company, Sears decided to form a number of strategic alliances and joint venture relationships with other firms. "Our strategy has been to look for the absolute best partners to build e-business,"[12] remarked the General Manager for Sears online.

Sears entered into a partnership with IBM to launch thegreatindoors.com, a site dedicated to home decorating ideas and products. To combat Home Depot, Sears and home improvement guru Bob Vila created an online joint venture, bobvila.com, as a site for home improvement solutions. According to CEO Martinez, this joint venture, "latest in the series of alliances" was a part of "new and powerful online strategy" that Sears planned to use to build its digital capabilities.[13] Sears also formed an alliance with *Sun Microsystems* to promote the Internet-connected home. Through this project, homes could function more safely and efficiently using Sun's networked products. Sears was responsible for installation, service, and financing of the products.

To further improve its marketing efforts, Sears entered into a partnership with America Online (AOL). The deal was to make AOL a preferred ISP for Sears, with AOL providing links to direct its customers to Sears.com. The deal also included offering Internet access through AOL's browser that would make it easier for customers to get in touch with Sears' customer service representatives. Further, AOL subscriptions could be paid online through Sears credit cards. "These deals help both sides gain deep penetration into each other's markets. It helps both Sears and AOL reach new customers that they didn't get or know about before,"[14] said an industry analyst.

As the e-business initiatives grew, Sears started building its information technology capabilities through strategic technology partnerships. Sears collaborated with Viant Corporation in planning and implementing product additions to its online offerings. Sears also teamed up with Xpedior, an E-Business solutions provider, to build and integrate multiple product lines and legacy systems into the sears.com Web site. To evaluate and monitor the online customer behavior and buying patterns, Sears worked with E.piphany to deploy a system for gathering marketing, operational, and technical metrics concerning online customers and Web site visitors.

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[12]Zimmerman, op cit.

[13]Sears press release, March 3, 2000.

[14]*The Gazette* (Montreal), "AOL, Sears Forge Web Alliance: Partnership Will Focus on Expanding Each Company's Business via Internet," March 15, 2000.

In its efforts to become the most desired online destination for home solutions, Sears added lawn and garden power equipment to its online offerings in April 2000. The company president said, "As a part of our online strategy to provide solutions for the home, during the past 12 months we have introduced the largest appliance store and the largest parts site for the consumers, as well as expanded to 120 brands on sears.com's tool territory. Our online efforts are designed to build relationships with our existing customers and attract new customers to Sears."[15]

In August 2000, the company relaunched its Web site with additional product offerings and a number of new features. Home electronics, computers, and office equipment, small appliances and cookware, and baby products were added to the existing set of offerings. A senior executive said, "Our customers can go to a single online store to shop, or to comparison shop and buy in-store. This will be essentially convenient for our customers during gift-buying seasons, when furnishing a new home, getting ready for a new baby—or for all those students going back to school next month who still need an iron, coffee maker, laptop, refrigerator or an MP3 player."[16]

Sears continued to add a number of new features to its Web site. In October 2000, it implemented a new online scheduling capability, through which customers could arrange for service and repairs to appliances and heating and cooling systems in their homes. The company also implemented an on-line bill payment service. Partnering with *Mercado Software*, Sears added an advanced search solution to its Web site to enable its customers to quickly and easily find the products or services for which they are looking. Sears formed an alliance with PCsupport.com, to provide online technical support on its Web site to Sears' customers who had purchased computers. This service enables customers to diagnose the problem in a 24 × 7 timeframe, get live technical support through e-mail or chat, and access online self-help resources.

Sears took a number of measures to increase the integration between its online and offline operations. Apart from being an additional sales channel, Sears saw the Web site as a means to drive its customers to make in-store purchases. Sears offered in-store pick-up for products that were sold online. This arrangement was to pull more of its shoppers into the stores so that they could make additional purchases. "Sears.com influences about 10% of in-store purchases of major appliances, and that's about $500 million a year. One of every 20 purchases of home office or home and garden products is influenced by the site,"[17] said a senior executive. To efficiently manage in-store pickups, Sears purchased 15,000 handheld devices that were used by its employees to scan store merchandise and reserve it when an order came in over the Web. This ensured that the items were in stock when the customer walked into the store to pick up the order placed through the Web site. As a part of its brick and click integration, Sears also introduced in-store kiosks. This enabled customers to do product research without the help of sales personnel at the retail stores. Sears also included an automotive category on its site, allowing customers to conduct online research on tires, batteries, and other automotive maintenance parts for their vehicles. Customers could research the parts, brands, and prices online and make the purchase from nearest Sears store. Because the products must be installed on the vehicle, they were not available for online purchases. The main intent of the automotive category was to enable online research and in-store purchase, installation, and service.

Furthering the efforts to integrate its online and offline operations, Sears also carefully aligned the incentives of its store-based personnel with online efforts. Sears decided that the stores would receive a commission according to the ZIP code of the Web orders. This commission was to be divided among the employees of the particular product section. This step helped eliminating the cannibalization fears, apart from motivating the in-store personnel to help those customers who come into the stores to gather information and then purchase the product on the Web. "Sears.com and our stores strongly complement each other. Our aim is to maximize the overall sales, whether through Web or stores," said an executive. In addition to incentives for sales personnel, the vendors are also credited for Web sales based on the category of the merchandise purchased online.

Business-to-Business Initiatives

Continuing its collaboration efforts, Sears teamed up with Oracle corporation and Carrefour, a large retailer in European and Latin American countries to launch a business-to-business marketplace to bring their combined 50,000 suppliers under one trading

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[15]Sears press release, April 12, 2000.

[16]Sears press release, July 25, 2000.

[17]Williams op cit.

platform. The e-marketplace, named GlobalNetXchange (GNX) was aimed at bringing down the procurement costs and product prices in addition to streamlining the purchase processes. The exchange also offered a full range of trading mechanisms including bidding and auctions. When it announced the initiative, Sears expected other major retailers to join the exchange so as to increase the economies of operations. Soon U.S. retailer Kroger, European retailers Metro AG and J Sainsbury Plc, and Australian retailer Coles Myer Ltd. joined the exchange.

With a volume that is twice that of Sears' and Carrefour's combined, and with a streamlined internal procurement process, Wal-Mart decided to have its own B2B exchange. GNX also faced competition from other retailer exchanges. For instance, the Worldwide Retail Exchange (WWRE) was started with backing from some popular retailers including Target, Albertsons, Best Buy, Kmart, Walgreen's, and J.C.Penny. More than 200 retailer exchanges with different product categories emerged in 2000 and 2001.

An industry analyst observed, "For suppliers, this exchange may not be very attractive. In addition to price reduction, they will also have to pay some fees whenever their goods are sold. It makes sense for some suppliers to start their own exchanges because that will help them retain some revenues and also control." Several suppliers initiated their own private exchanges.

Acquisition of Lands' End

In May 2002, Sears announced that it would be acquiring Lands' End for $1.9 billion. Lands' End is among the country's largest specialty apparel Internet and catalog companies, with a 2001 revenue of about $1.6 billion. Through this acquisition, Sears would be able to reintroduce its catalog business that it exited in 1993. Further, Sears hoped to attract its online customers to the softer goods segment. An internal study showed that 70 percent of the customers who shopped at Sears for appliances shopped elsewhere for apparel. "Lands' End is a very successful and well-managed company. We were drawn to Lands' End's brand strength across all apparel categories, including men's, women's and children's. It is an excellent fit for Sears and our customers and will aid us in becoming the preferred shopping destination for families. We can help accelerate the growth of the Lands' End direct business through Sears' extensive customer relationships,"[18] said the Sears CEO Alan Lacy.[19] As a part of the deal, Sears would carry and sell Lands' End merchandise in its stores and Lands' End would assume responsibility for Sears' customer-direct business, including Sears.com. Lands' End's CEO was named the head of Sears' customer-direct business. As an initial experimentation, Sears also decided to stock and sell Lands' End's apparel in 180 of its 800-plus stores.

In addition to its Web and catalog operations, Lands' End operated 16 outlet stores in Wisconsin, Illinois, Minnesota, and New York, plus three outlet stores in the U.K. and one in Japan. Lands' End launched its site in 1995, featuring about 100 products as well as stories, essays, and travelogues. Over time, its product range, selection, and customer base grew. The company also introduced several innovative features for shoppers on its Web site, including My Virtual Model, a tool that allowed shoppers to create a three-dimensional model for their body to ensure a better fit for clothing they order. The company also offered My Personal Shopper service, which allows customers to set up a profile of their wardrobe style preferences so they receive recommendations from Lands' End. A brief comparison on the Web site features of Sears and Lands' End is provided in Exhibit 7. Exhibits 8 and 9 present the Web sites of both Sears and Lands' End.

Both companies had some differences in their customer base. While Lands' End typically had affluent and brand conscious customers, Sears catered to a broader customer base. Lands' End had built a solid brand name over the years, and it ran the risk of diluting its brand image if its' goods were sold together with other brands at Sears. An industry analyst remarked, "If they don't dilute the brand and they keep the quality, I think that Sears is going into a good direction."[20] Sears and Lands' End also had differences in the way they handled product returns, and in their approaches to marketing.

Both the companies had adopted different approaches to information technology sourcing as well. Sears had historically relied on in-house development and in-house expertise for its IT as well as Web operations. However, Lands' End has licensed or

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[18]T. Robinson, "Sears Shells Out $1.9B for Lands' End," *E-Commerce Times*, May 14, 2002.

[19]Alan Lacy became CEO of Sears in October 2000 after Arthur Martinez retired.

[20]T. R. Weiss, "Sears Buying Lands' End," *Computerworld*, May 13, 2002 (available online at **http://www.computerworld.com/managementtopics/ebusiness/story/0,10801,71132,00.html**).

adapted unique technologies for its Web operations. They had also, for the most part, been relying on external expertise to build their technology and applications infrastructure.

While stock markets reacted very favorably to the news about Sears' acquisition of Lands' end, a short communiqué from Sears a few days later announced the departure of its CIO, who had played a key role in building its e-business.

Garry Kelly reflected on his objective to make Sears a truly brick-and-click organization, a multichannel retailer that would be a compelling place for customers to research, order, and shop. He must help return the $41 billion company to health, while simultaneously digesting a $1.6 billion direct-sales operation. He knew that in order to fulfill this goal, he had to reorient his technology organization, reexamine and improve on the e-business initiatives, and move forward. The technological growth has been particularly haphazard and he needs to set it in order. CEO Alan Lacy explained, "We've had a very fragmented approach, and we're basically trying to standardize much more so than we have in the past.…We've got too many point-of-sale systems, too many inventory systems, too many this, that and the other thing, because we basically allowed for many, many years each business to do its own thing, which we're not going to do anymore."[21] Given the current scenario at Sears, it wasn't clear which direction would be best for its future.

Garry rose from his desk, considering the three strategic questions on the future course of e-business that faced his company. First, what was the best way to utilize the Web site and Internet to attract and sell a varied range of products? Second, how should Sears extend and enhance its business-to-business e-commerce initiatives to stay ahead of the pack and beat the competition? And finally, could Sears utilize Lands' End's technological and operations capabilities to turn around its e-business?

[21]C. Silwa, "CEO Says Company Will Standardize Technology," *Computerworld*, January 20, 2003 (available online at **http://www.computerworld.com/industrytopics/retail/story/0,10801,77715,00.html**).

Exhibit 1. Annual Sales Trends in U.S. Retail Industry ($ Millions)

	1992	1995	1996	1997	1998	1999	2000	2001
Discount Department stores	93,871	118,661	121,936	128,049	131,004	135,713	138,360	139,895
Chain Department stores	87,384	92,258	95,065	97,013	97,543	100,350	100,387	94,780
Specialty Stores								
Furniture, home furnishings, electronics, and appliance stores	97,757	130,447	137,930	144,303	154,555	167,151	178,834	179,241
Clothing and accessories stores	120,346	131,605	136,860	140,565	149,442	159,888	167,541	169,127
Total	$401,350	$474,966	$493,787	$511,927	$534,542	$565,101	$587,122	$585,044

Source: U.S. Census Bureau

Exhibit 2. Top Retailers in U.S. Market

		Volume ('000)		Earnings ('000)		Units	
	Company	2001	2000	2001	2000	2001	2000
1	Wal-Mart	$219,812,000	$193,295,000	$6,671,000	$6,295,000	4,414	4,190
2	Home Depot	53,553,000	45,738,000	3,044,000	2,581,000	1,348	1,134
3	Kroger	50,098,000	49,000,400	1,042,500	876,900	3,534	3,660
4	Sears	41,078,000	40,937,000	735,000	1,343,000	2,960	2,960
5	Target	39,362,000	36,362,000	1,368,000	1,264,000	1,381	1,307
6	Albertson's	37,931,000	36,762,000	501,000	765,000	2,400	2,533
7	Kmart	37,028,000	35,925,000	-244,000	403,000	2,150	2,172
8	Costco	34,797,037	32,164,296	602,089	631,437	369	335
9	Safeway	34,301,000	31,976,900	1,284,400	1,091,900	1,773	1,688
10	JCPenney	32,004,000	31,846,000	98,000	-705,000	3,770	3,725

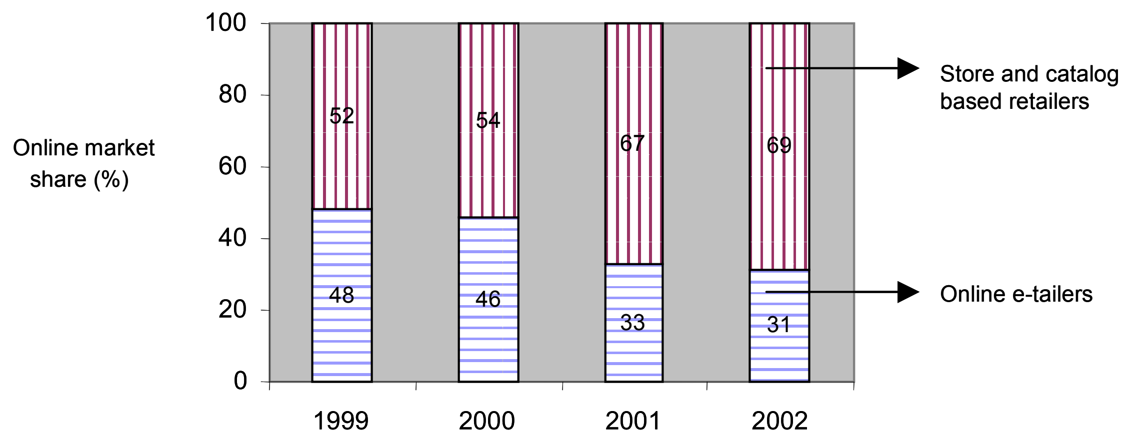
Source: Stores Magazine, National Retail Federation

Exhibit 3. U.S. Retail Industry Sales—Total Retail and Online Sales ($ Millions)

Period		Retail Sales: Total	Retail Sales: E-commerce
1999	4th Quarter	784,278	5,481
2000	1st Quarter	711,600	5,814
	2nd Quarter	771,691	6,346
	3rd Quarter	765,536	7,266
	4th Quarter	810,311	9,459
2001	1st Quarter	724,224	8,256
	2ndQuarter	805,245	8,246
	3rd Quarter	782,088	8,236
	4th Quarter	856,285	11,178
2002	1st Quarter	743,810	9,880
	2nd Quarter	825,243	10,265
	3rd Quarter	827,461	11,061
	4th Quarter	869,588	14,334

Source: U.S. Census Bureau

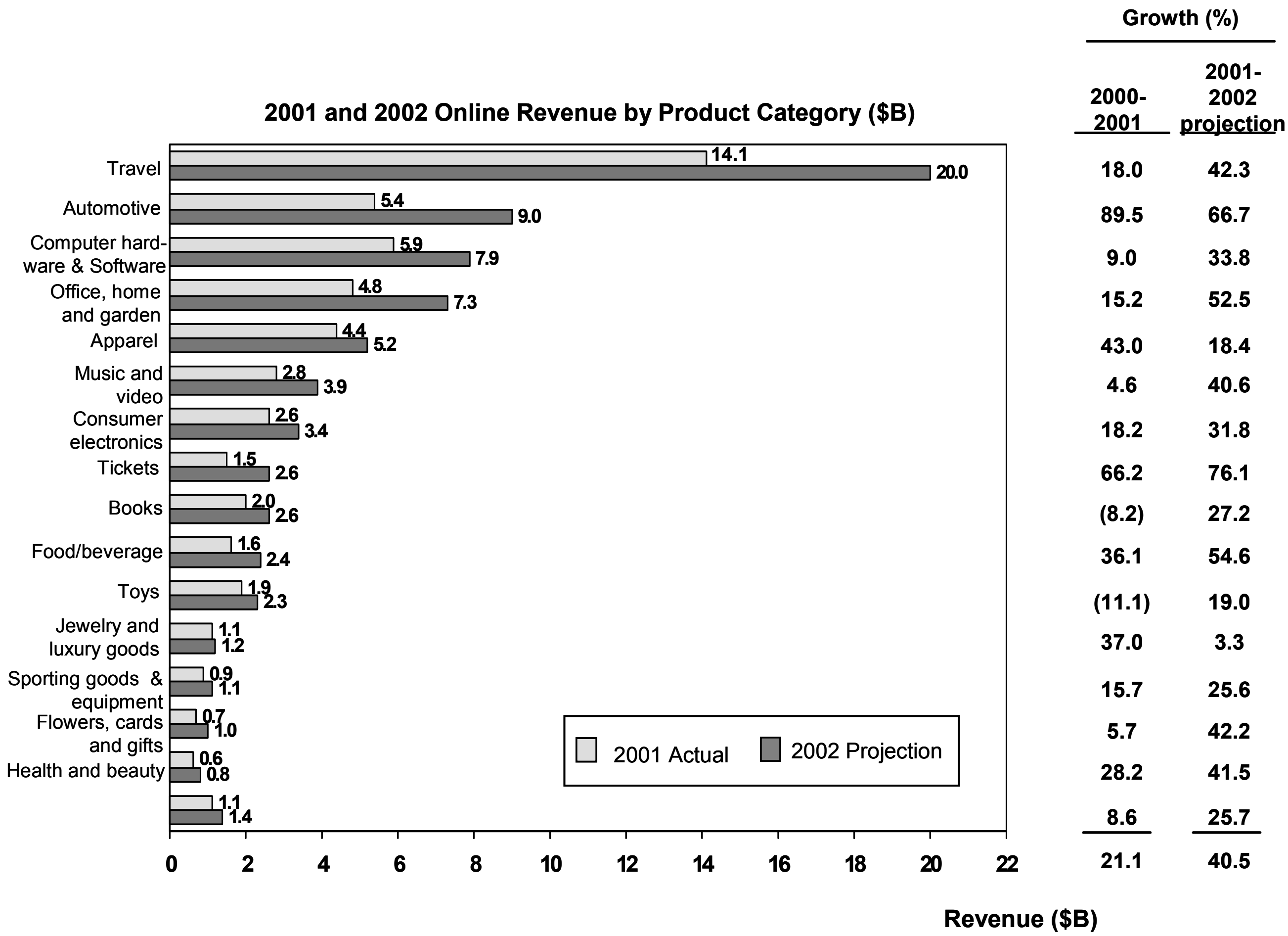
Exhibit 4. Trends in Online Sales: Traditional (Store + Catalog) Retailers Versus Online E-Tailers



	1999	2000	2001	2002
Total online market ($bn)	25.5	42.4	51.3	72.1
Growth rate - online e-tailers (%)	257.5	60.8	-14.4	33.3
Growth rate - store/cataglog retailers (%)	132.8	71.4	52.2	44.1

Source: The State of Retailing Online 5.0 (Boston Consulting Group, Forrester Research and comScore Networks)

Exhibit 5. Trends in Online Sales by Product Category



Source: The State of Retailing Online 5.0 (Boston Consulting Group, Forrester Research and comScore Networks)

Exhibit 6. Key E-Business Initiatives at Sears

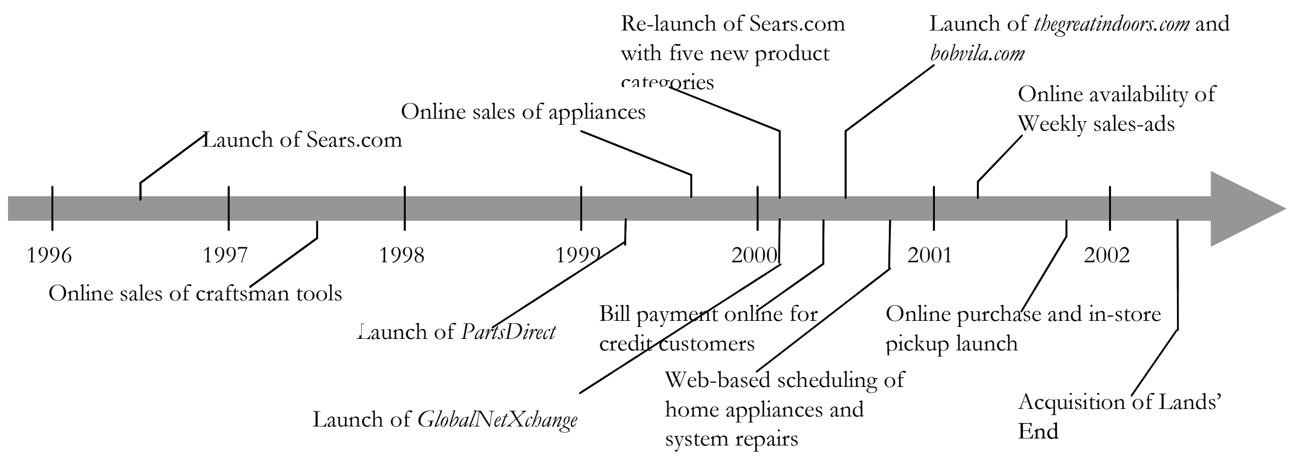


Exhibit 7. Sears Vs Lands' End Sites: A Comparison of Online Processes and Features (2002)

Process/Features	Sears	Lands' End
Return	In-store or by mail	By mail only
Pickup	By mail/In-store (for selected & based on availability)	By mail only
Price matching	Within 30 days	NA
Geographical scope	U.S. only (separate site for Canada)	Global (International sites available in multiple languages for Europe, U.S. and Asia)
Product Presentation	Dominantly through text and graphic images.	Text, graphic images and advanced visual presentations through virtual models etc.
Customer service channels	Phone, email, FAQ	Live Chat, Personal Shopper, Virtual model, Shop with a friend, Call back, Phone, email, FAQ
User Registration	Required	Required

Exhibit 8(a). Sears' Site Map – 1997

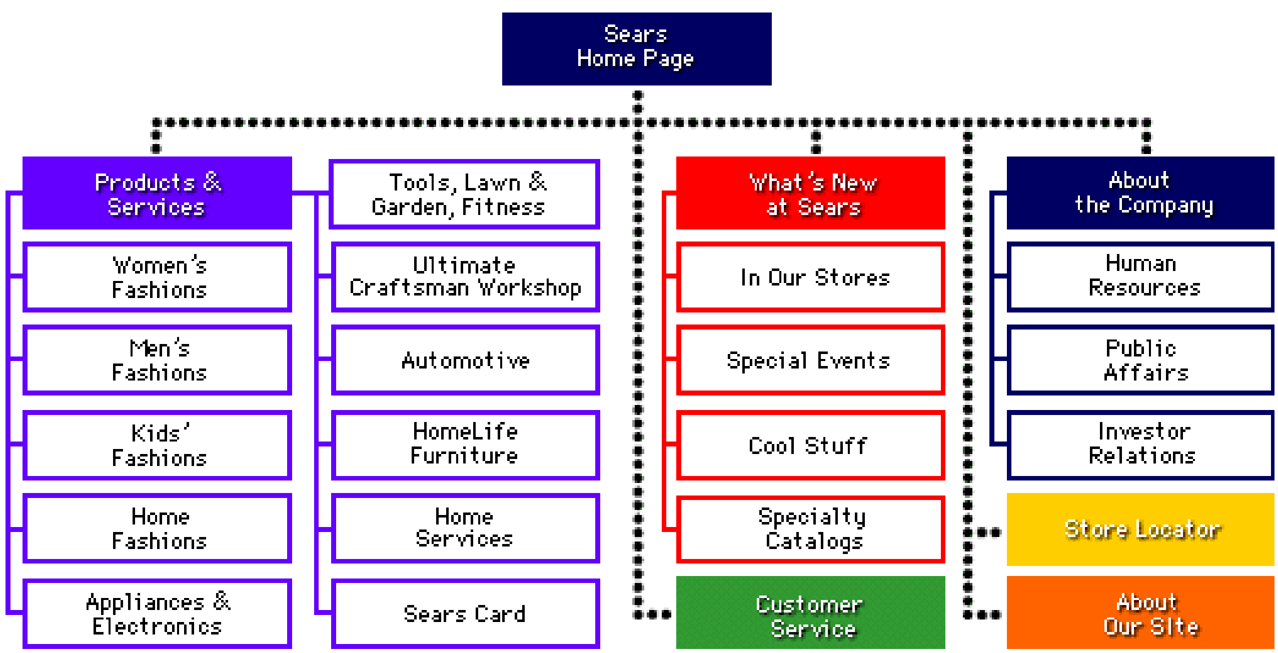


Exhibit 8(b). Sears' Site Map — 2003

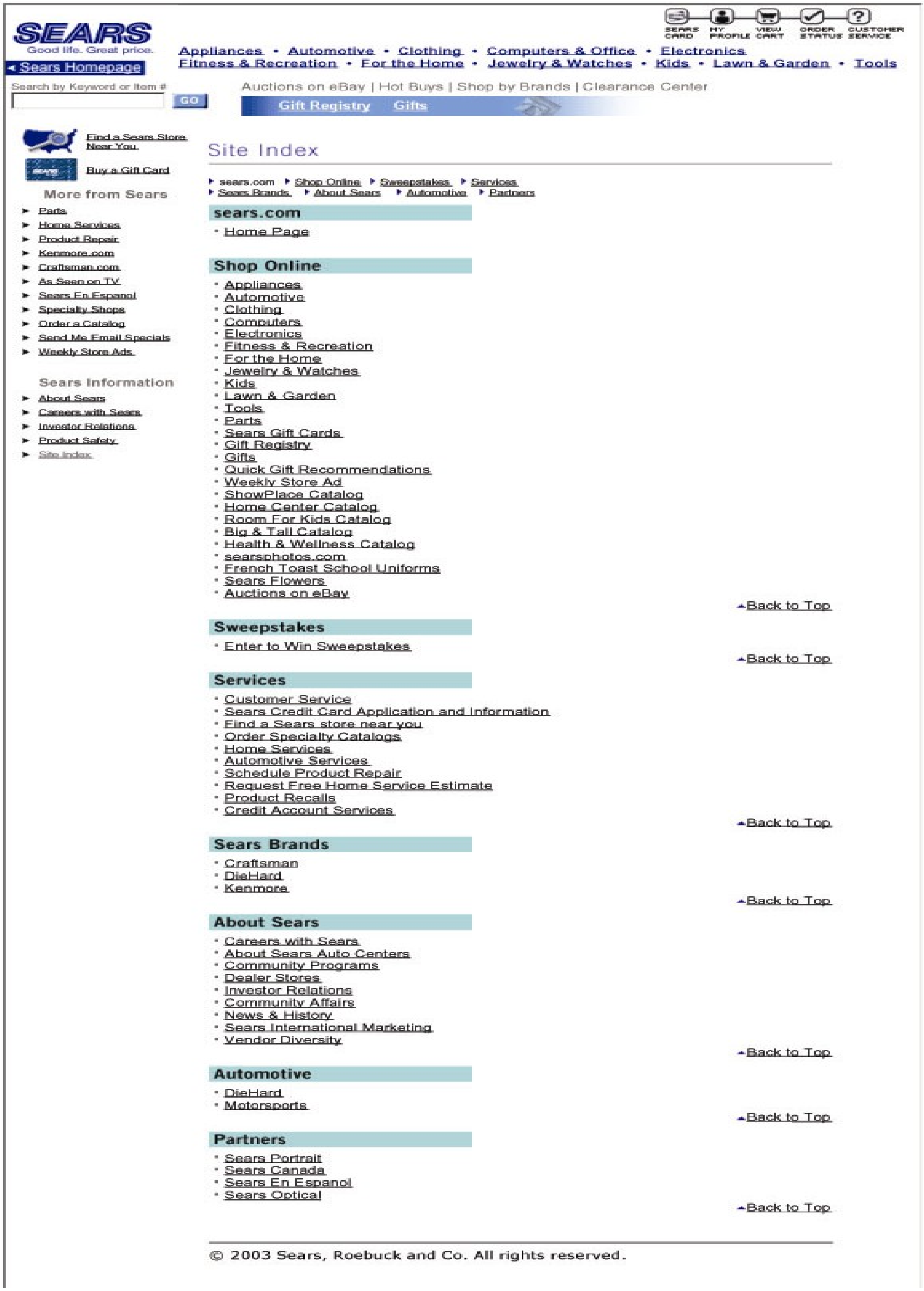


Exhibit 8(c). Sears' Web Site — 2003

Exhibit 9(a). Lands' End Sitemap — 2003

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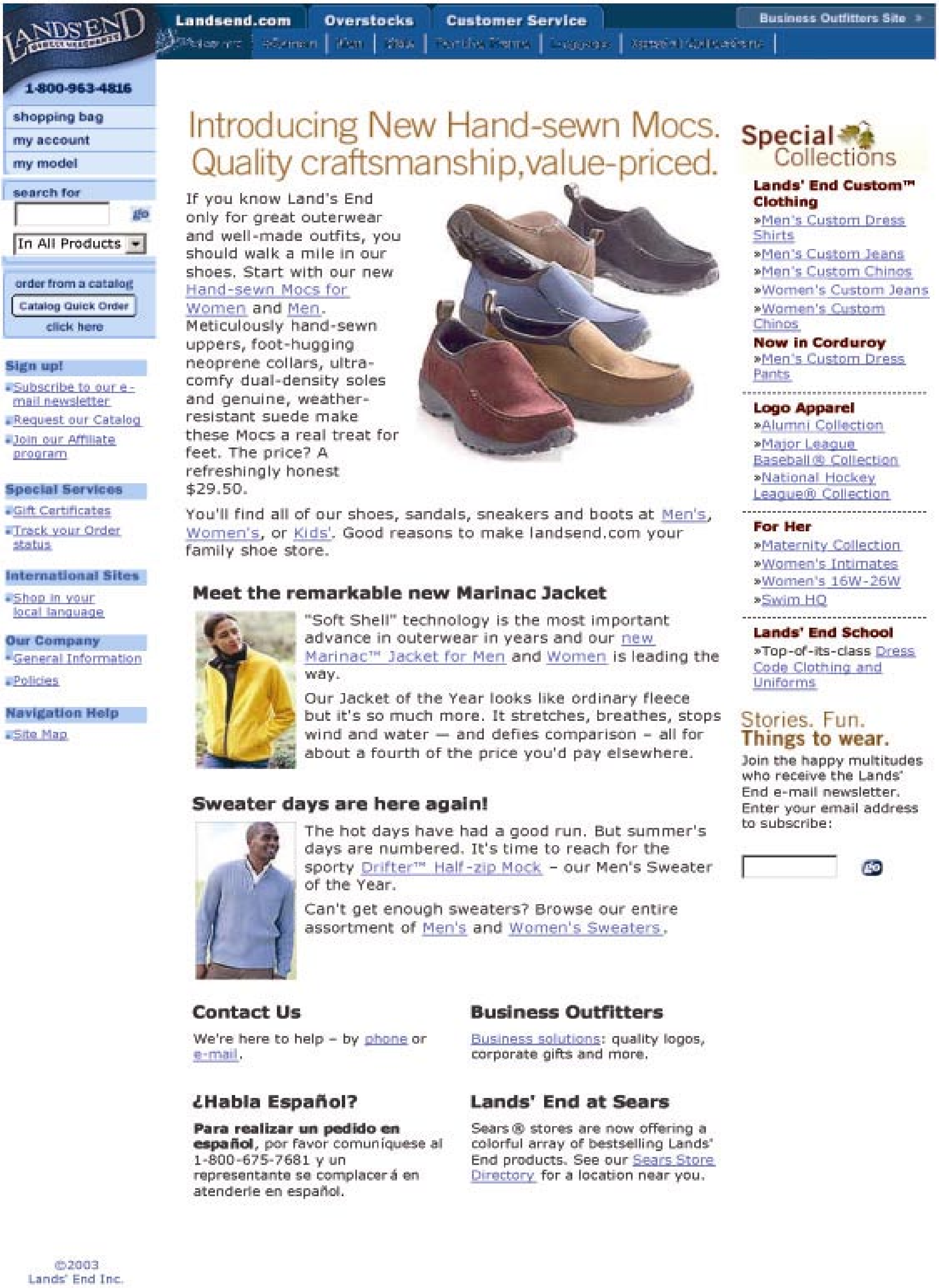
Exhibit 9(b). Lands' End Website — 2003



E-Business Transformation at the Crossroads: Sears' Dilemma

— Teaching Note (Synopsis)[22] —

Case Synopsis

This case discusses the challenges facing Sears in its efforts to transform itself into an effective brick-and-click organization. It presents the issues faced by a new CIO who has taken over the technology and e-business affairs at Sears at the end of 2002.

This case addresses Sears' e-business initiatives in the face of intense competition in the U.S. retail industry. In a fairly matured industry like retailing, traditional rivals such as Wal-Mart, J.C. Penny, and Home Depot are infringing on the online consumer space, while new pure-play Internet e-tailers like Amazon.com are trying to capture a significant portion of the market. Sears has responded to this competition by continually expanding their online efforts in e-business transformation. Sears is using different mechanisms such as acquisitions and strategic alliances to build its e-business capabilities and turnaround its dwindling fortunes.

The case documents the on-going efforts of Sears to become a successful brick-and-mortar organization. As a part of its evolving e-business strategy, Sears acquired Lands' End in order to gain access to its catalog and Internet operations, technological infrastructure and the apparel business.

Broad learning opportunities from this case include

- What are the key challenges and decisions facing a firm making a digital transformation?
- How to develop an e-business strategy that is aligned with the firm's business strategy (or that which drives the business strategy)?
- What e-business capabilities are required to make a successful e-business transformation? How can firms build these e-business capabilities?

In the context of retailing industry, the learning will pertain to

- What product, pricing, and selling strategies are effective for online retailing?
- How can a traditional retailing firm make an effective e-business transformation?
- Can the external mechanisms such as outsourcing, alliances or acquisitions help in building sustainable e-business capabilities?

Target Audience

This case is appropriate for graduate students in MBA, MS-IS, or MS E-Commerce programs for a course in e-business strategy or IS strategy.

Primary Teaching Objectives

The case can be used to enhance the students' understanding of the following issues:

➢ Understanding of the competitive dynamics and the impact of the Internet on the retailing industry
➢ Formulation of a firm's e-business strategy – incremental versus big-bang approaches.
➢ Evaluating the potential of online channel and product-portfolio strategies for selling online.

[22]The complete teaching note is available from the first author on request.

- Assessing the external sourcing mechanisms (alliances, acquisitions, outsourcing etc.) for building e-business capabilities for effective e-business transformation
- Challenges in transforming a traditional organization into a digital business, and in integrating digital and traditional businesses.

Suggested Assignment Questions

1. Sears' objective is to convert itself into an effective brick-and-click organization. How will you evaluate its current approach to making an e-business transformation? What are the key issues that need to be resolved in order to make a successful e-business transformation?

2. What are the critical capabilities that are required for successful e-business transformation? How has Sears been building its key capabilities for e-business? What are the advantages and disadvantages of its approaches to building e-Business capabilities?

3. If you were Garry Keller, how will you tackle the following issues:
   a. Sears sells a variety of merchandise ranging from appliances to apparel. How should it position itself online? Should it sell all of its goods, or focus on a few selected goods? Why / Why not?
   b. What will you decide about Lands' End? Should it be integrated into Sears' e-business, or should it be a separate entity? What are the implications of each of these alternatives?

Major Topics for Discussion in Classroom

- Analyzing the impact of the Internet on retailing industry
- Critical e-Business capabilities for a brick-and-mortar retailer, and the alternatives for building these capabilities
- E-business transformation—incremental versus the big bang approaches
- Alignment of a firm's business strategy and its e-business strategies.
- Integration of brick and click strategies, processes, and operations.