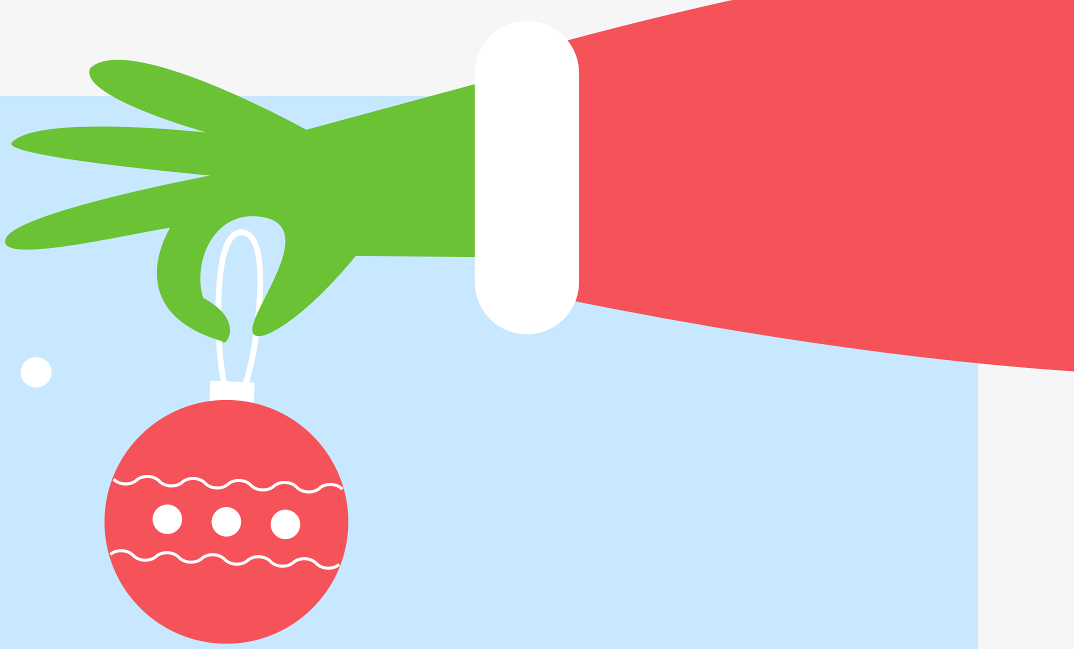
We wish you happy holidays!

Fabric



# How the "Shipocalypse" Stole Christmas

**Why carrier-imposed capacity limits and cut-off dates are revenue killers during the holiday season & what retailers can do about it**

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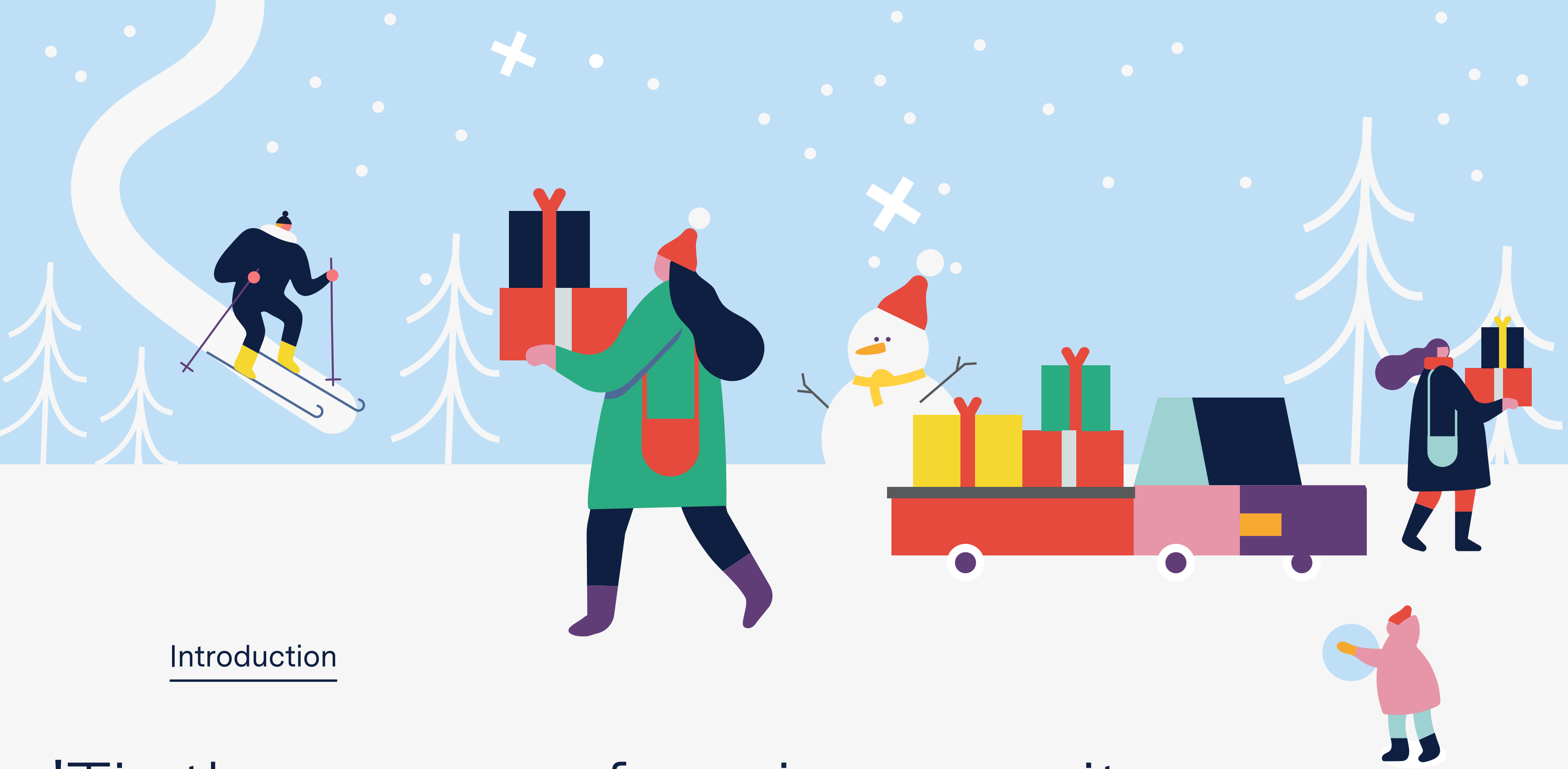


Introduction

# 'Tis the season of carrier capacity constraints and cut-off dates

Few things capture the imagination as much as the winter holiday season — the decorations! The music! The gifts! As with all fantasies, the reality is often far less idyllic: families fight. Lights get tangled. Trees get kicked to the curb.

**For retailers and brands, the 2021 holiday season is shaping up to be more "shipocalypse" than it is shiny and bright.**

The meteoric rise of e-commerce since the onset of the pandemic has already placed retailers under unprecedented strain. Labor shortages are acute and industrial real estate prices have skyrocketed, leaving retailers with insufficient fulfillment capacity to meet consumer demand. What's more, consumer preferences have become more exacting, with the majority of consumers expecting their deliveries at their doorsteps faster than ever, a proposition that's incredibly complex and expensive for retailers to provide.

All of that is the status quo on a good day. Now with the 2021 holiday season well underway, businesses are running the gauntlet with an additional set of complications and challenges.

The latest headlines are consumed by stories of congested ports and empty shelves, and although the "first mile" of the supply chain is indeed besieged with disruptions, the "last mile" is poised to be especially hellish this holiday season. We have new data that quantifies the extent of the damage of last year's "shipocalypse" and why retailers expect losses to be even greater this holiday season.

We surveyed 200 retailers and brands to get a clearer picture of the challenges they're facing this holiday season, and we learned that **there's one last-mile lump of coal that far outweighs all other concerns: shipping carrier constraints.**

# Key Findings

**01 Brands and retailers cite shipping carrier constraints as a top threat to their entire e-commerce business**

The threat of shipping carrier constraints even outweighs retailers' concerns about labor shortages, high shipping costs, and high fulfillment costs.

**02 Under the sheer glut of demand, private shipping carriers have the power to cut off retailers at their discretion**

"We're controlling the volume that comes into our network because we're laser-focused on revenue quality. We used to think that every package was the same; we don't think that anymore" - UPS CEO Carol Tomé

**03 Retailers estimate they lost an average of 24 percent of sales last holiday season as a result of carrier-imposed capacity limits**

Much has been written about last year's "shipocalypse" when shipping carriers cut off many retailers. Now we know just how bad the damage was in terms of lost sales.

**04 Retailers expect to lose even more this holiday season as a result of carrier-imposed capacity constraints, with 1 in 3 predicting they'll lose up to 50 percent of sales**

The writing is already on the wall: it's projected that demand for peak-season parcel delivery will exceed capacity by about 5 million pieces a day.

**05 As a result of carrier-imposed cut-off dates, 64 percent of retailers must stop promising delivery 4-7 days or more before Christmas**

Retailers have their hands tied exactly when consumers want last-minute deliveries the most. 98 percent of retailers say that these cut-off dates lead to lost sales.

**06 Retailers are resorting to a number of stop-gap solutions — start holiday promotions early, promote BOPIS, and even foot the bill of a premium delivery service themselves**

But these solutions are only workarounds and bandaids that fail to capture the full spending potential of the inevitable last-minute online holiday shopper.

**07 Long-term, 95 percent of retailers are planning to implement a distributed fulfillment strategy from a network of local sites**

It's time to reevaluate the way supply chains work and move away from centralized fulfillment models. Most retailers we surveyed understand that distributed fulfillment is the key to future-proofing their e-commerce businesses.

## The rise of holiday e-commerce

# Christmas comes but once a year, and in the age of e-commerce, that's exactly the problem

It's hard to overstate the importance of the winter holiday season to retail. According to NRF, holiday sales have accounted for about one-fifth of annual retail sales over the past five years, and for some businesses, it's an eight-week window that can account for more than half of a retailer's annual sales.[1]

For traditional brick-and-mortar retailers, this sudden peak in spending is without a doubt the most wonderful time of the year. NRF states that "holiday sales can be more profitable because the increased volume of purchases comes without significantly increasing retailers' fixed costs of doing business[2]."

But with the sudden rise of e-commerce, holiday sales have become much more complicated. 2020 was the biggest holiday season ever for online shopping, with consumers spending $236 billion online in the U.S., up 43 percent over 2019.[3] This year, e-commerce is expected to hit even higher levels of penetration, with Salesforce predicting that online holiday sales will hit $259 billion in the U.S., an increase of 10 percent over last year.[4]

**The problem? Peaks are extraordinarily challenging for e-commerce operations.**

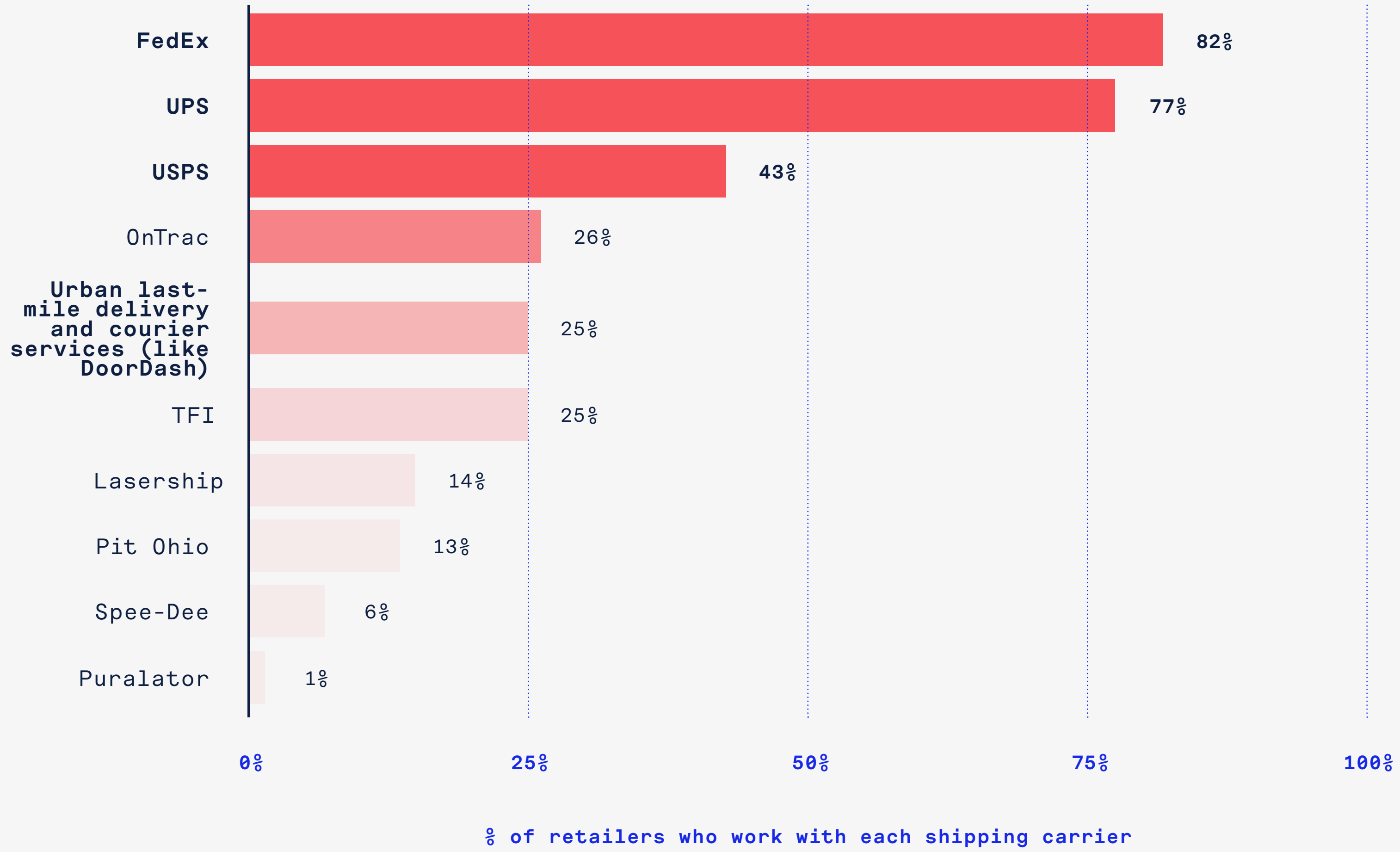
It's no longer a matter of extending store hours and ushering consumers through check-out lines faster and more efficiently; for e-commerce, retailers need to forecast capacity and throughput requirements far in advance and ensure they have the infrastructure and labor in place to pick, pack, and dispatch online orders at speed and scale.

"Peaks are challenging because of their fleeting nature: a peak is not a constant, and it's hard to gauge the degree of flexibility and agility your business will need (and when and where it will be needed)," writes DHL. "Cultivating logistics capabilities that can 'switch on and off' as necessary is a process that takes time."[5]

Even for businesses who get the critical timing right, manage to adjust their capacity at the flip of a switch, and successfully meet skyrocketing demand for online orders, there's still one intractable challenge during peak season: shipping carrier constraints.

The shipping carrier problem

# Retailers overwhelmingly rely on national shipping carriers to deliver their online orders



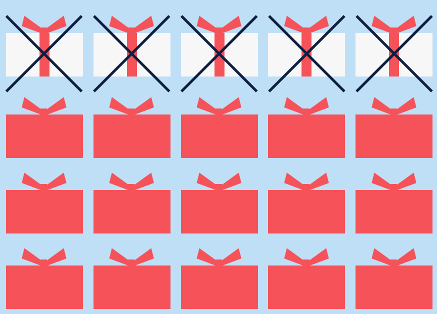

Source: Fabric retailer survey, September 2021

The vast majority of retailers and brands we surveyed rely overwhelmingly on the big three national shipping carriers — FedEx, UPS, and the United States Postal Service (USPS) — to ship online orders to their customers: 81 percent of the retailers we surveyed work with FedEx, 77 percent work with UPS, and 43 percent work with USPS. Far fewer work with regional carriers or urban last-mile courier services such as DoorDash. In fact, among the retailers we surveyed, 16 percent reported working with courier services occasionally and only 9 percent work with them on a regular basis.

### In a stinging rebuke, retailers cite shipping carrier constraints as a top threat to their entire e-commerce business.

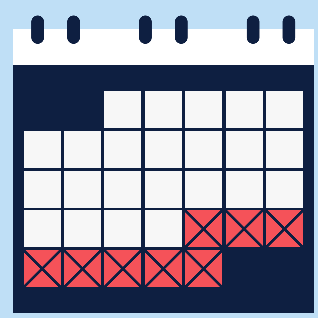
The surge in e-commerce penetration and retailers' reliance on the national carriers has created a supply and demand imbalance that "puts carriers in a position of power,[6]" says Jefferies. **In fact, the retailers we surveyed identify shipping carrier constraints as a top threat to their entire e-commerce business, eclipsing their concerns about labor shortages, high costs of shipping, and high costs of fulfillment.**

# The businesses we surveyed feel the pain of relying on national carriers in two distinct but interrelated ways:



## Capacity limits

How many orders a retailer can rely on the carrier to dispatch during a specific period of time



## Cut-off dates

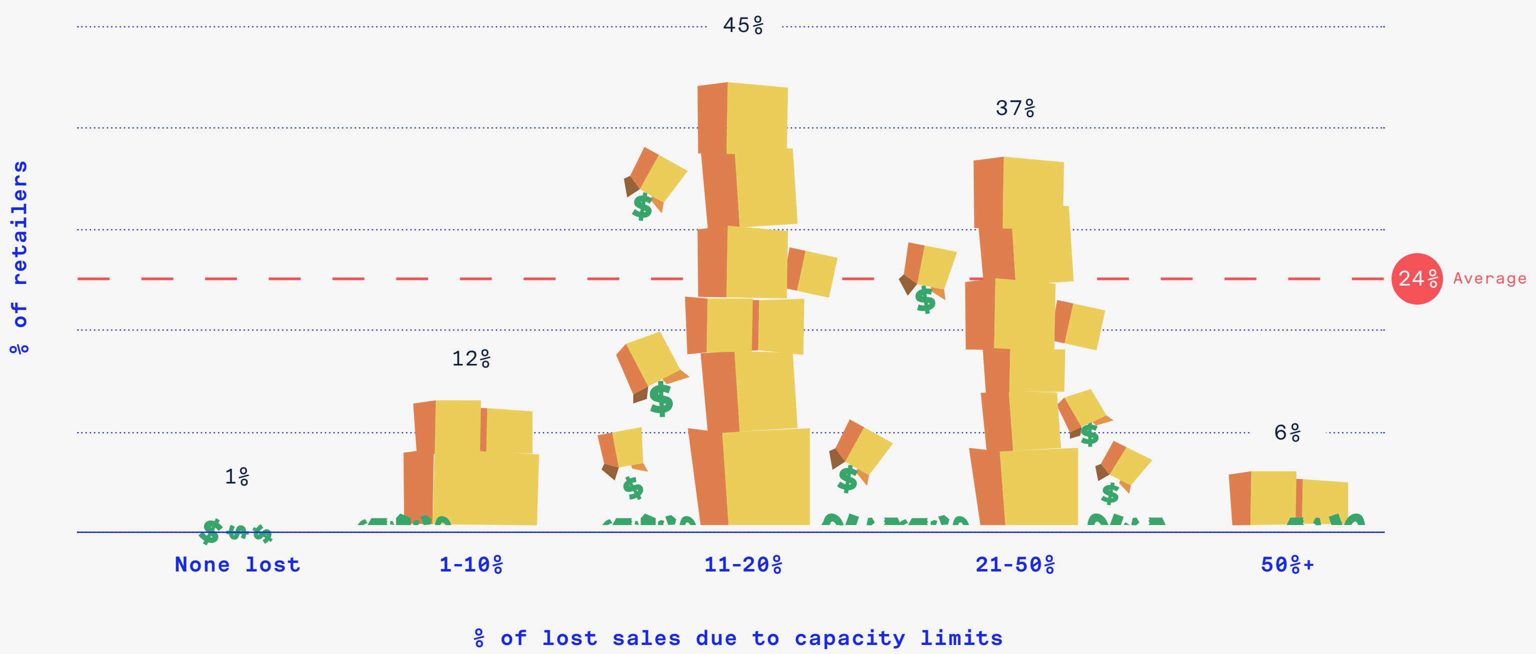
The date that items need to be shipped to make it to their destination on time

The relationship between retailers and shipping carriers is fraught and complex even outside of the peak season. The sudden explosion of e-commerce means that residential deliveries have surged while B2B deliveries have declined, and residential deliveries are inherently less efficient and profitable for carriers: the number of pieces per delivery is low, residences are usually not in close proximity to each other, and it's an operation prone to headaches such as porch piracy and address mix-ups.

That means that retailers are facing heightened surcharges for residential deliveries all year round, and during the "peak on top of a peak" — which is how FedEx referred to last holiday season — the stakes become that much higher in what is often already a strained relationship.

The shipping carrier problem: **Capacity limits**

## Retailers estimate that they lost an average of 24 percent of sales last holiday season as a result of carrier-imposed capacity limits




Source: Fabric retailer survey, September 2021

**Due to capacity constraints imposed by carriers in 2020, U.S. retailers estimate they lost nearly a quarter of sales on average last holiday season, with 37 percent estimating they lost as much as 50 percent of sales.**

Horror stories abound: on Cyber Monday, UPS suddenly instructed drivers to stop picking up packages from several large retailers, including Gap, Nike, and Macy's — "no exceptions."[7] The *Washington Post* reported that under the sheer glut of demand, FedEx and UPS cut off many retailers, rerouting a tidal wave of packages to the USPS, who, unlike private shippers, can't reject delivery orders. The USPS became "gridlocked" as a result, causing delays even in the delivery of first-class mail such as letters and bills. [8]

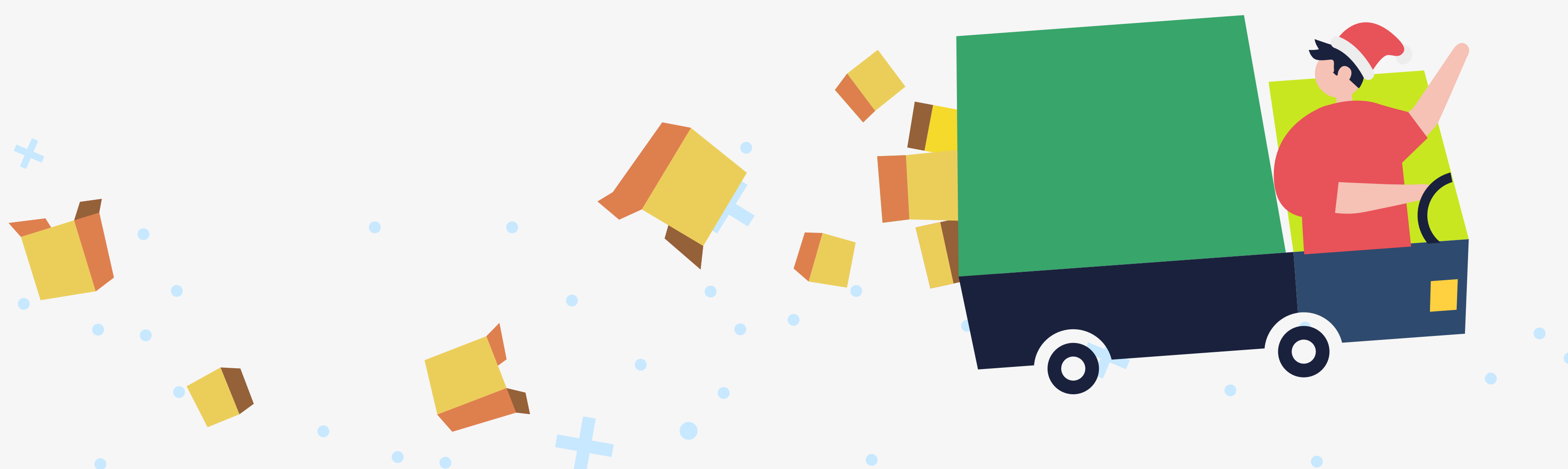
At the peak of the season, the nation's entire delivery infrastructure — including FedEx, UPS, the USPS, and other shippers — were reportedly failing to pick up an estimated 6 million packages a day.[9] Adding insult to injury, most customers affected by shipping delays blame the retailer rather than the shipping company that handled the delivery.[10]

The shipping carrier problem: **Capacity limits**

## Bracing for even worse losses this year, 1 in 3 retailers predict that they'll lose as much as 50 percent of sales as a result of capacity limits


Source: Fabric retailer survey, September 2021

Though it's hard to imagine anything being worse than last year's "Shipocalypse," retailers haven't been able to mitigate their reliance on carriers and anticipate that the problem will only be worse this year. The brands we surveyed expect that they will lose an average of 25 percent of sales this holiday season as a result of carrier capacity limits, with 30 percent anticipating they'll lose as much as 50 percent of sales. The writing is already on the wall: ShipMatrix forecasts that demand for peak-season parcel delivery will exceed capacity by about 4.7 million parcels a day,[11] a projection corroborated by the Chief Executive of UPS CEO Carol Tome who puts the estimate at 5 million pieces a day.[12]



*"We're controlling the volume that comes into our network because we are laser-focused on revenue quality.*

*We used to think that every package was the same; we don't think that anymore. For some shippers, we're no longer delivering their packages and that's OK with us.*

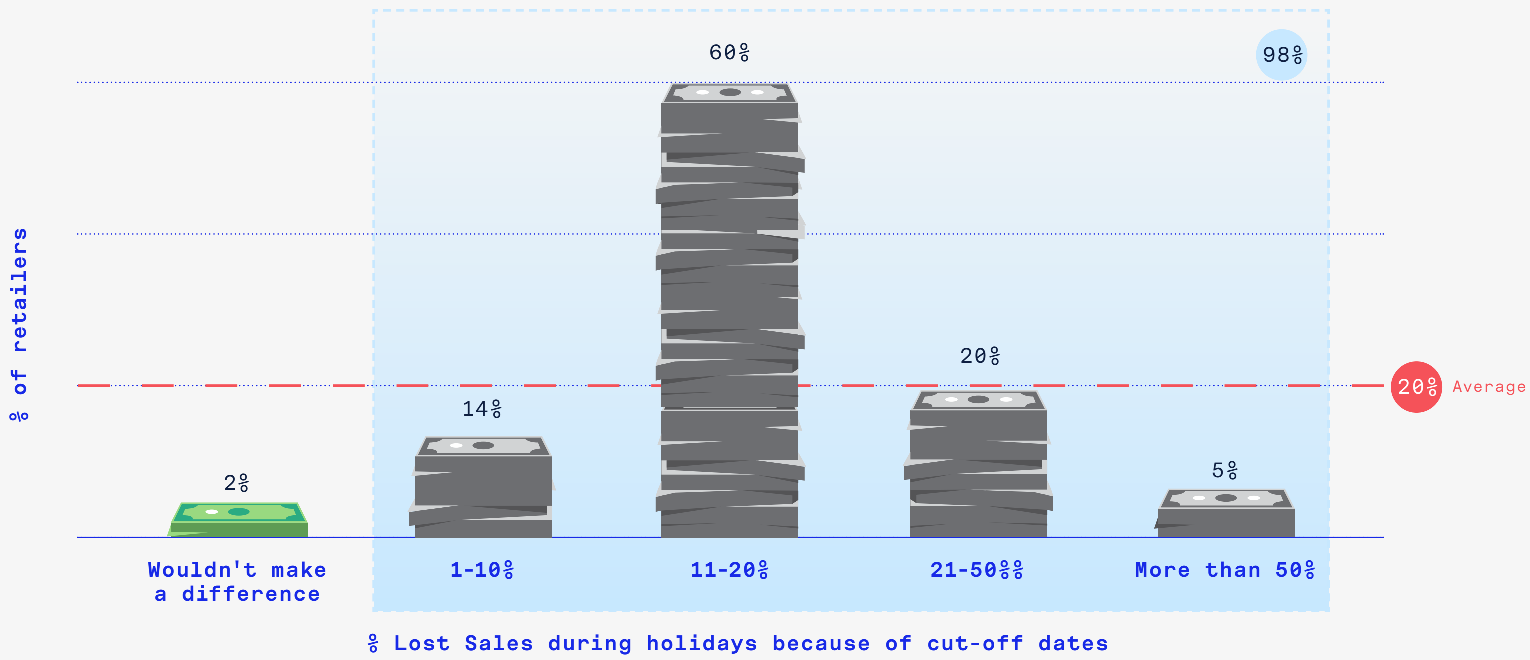
*Now, if we think about our largest customer, we've got a great relationship with our largest customer. And really, I'm pleased with where that relationship stands."*

— **Carol Tomé, CEO of UPS,** *Q3 earnings call, October 26, 2021* [13]

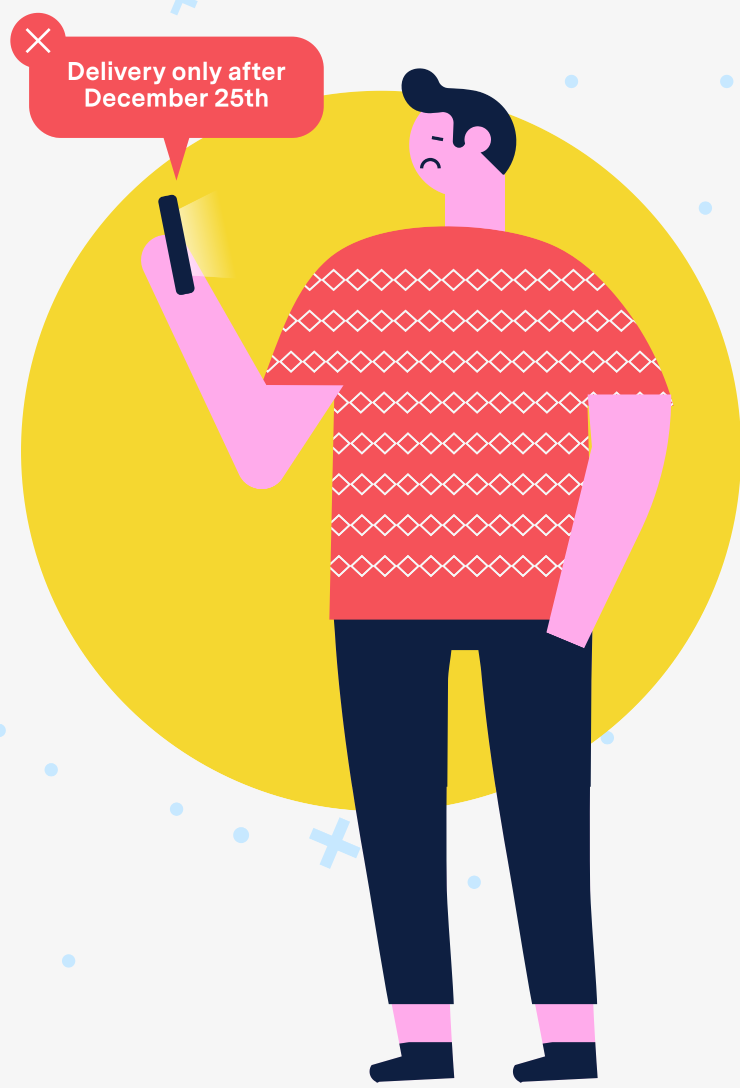
**UPS' biggest customer?** Amazon, who made up 13.3% of their revenue in 2020. [14]

The shipping carrier problem: **Cut-off dates**

## 98 percent of retailers say carrier-imposed cut-off dates cause them to lose sales during the holidays




Source: Fabric retailer survey, September 2021



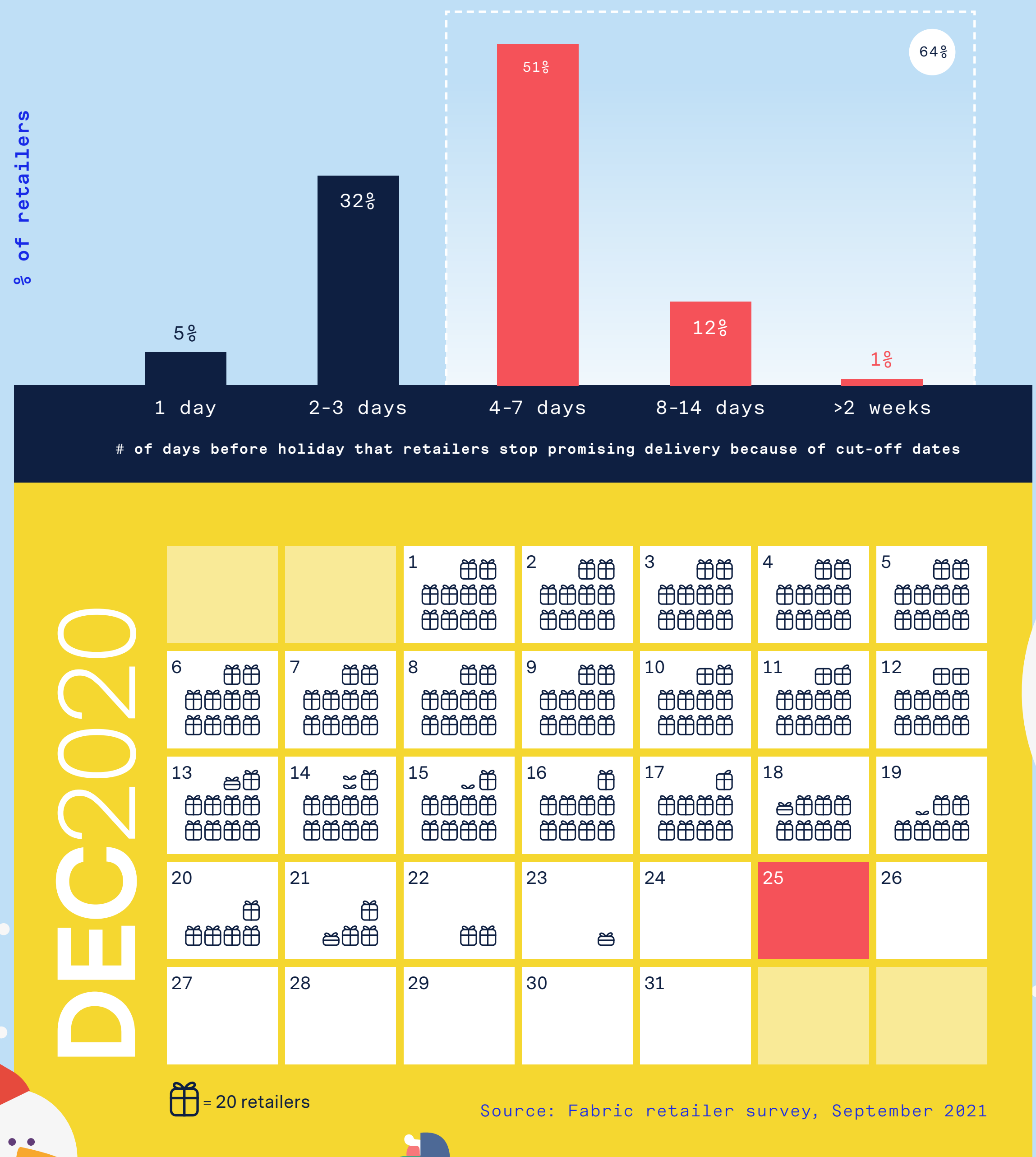

Carrier-imposed cut-off dates also cause retailers to bleed profits during the holiday season. 85 percent of retailers we surveyed reported that cut-off dates cost them more than 10 percent in lost sales, 20 percent of retailers reported that it cost them up to 50 percent, and another five percent say it cost them more than 50 percent. The source of these lost sales?

**The fact that most retailers miss out on an entire week of online sales leading up to Christmas day.**

**The shipping carrier problem: Cut-off dates**

## 64 percent of retailers say they have to stop promising delivery 4-7 days or even more before major holidays

Due to carrier-imposed cut-off dates, 51 percent of retailers are forced to stop promising delivery to their customers 4-7 days before Christmas, and another 13 percent stop accepting orders as much as two weeks prior. For 64 percent of retailers, this amounts to roughly a week of lost sales (or more!) during the most critical sales period of the entire year.

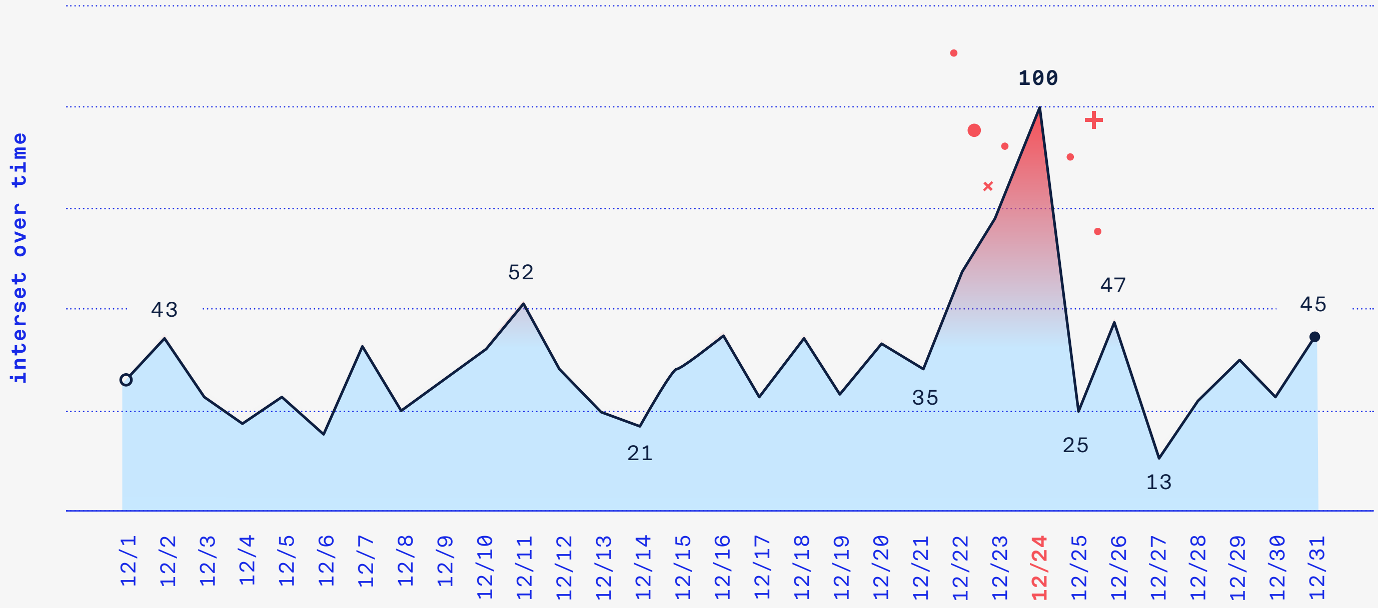



Of the 200 retailers we surveyed, **only 10 can accept orders on December 23** and still guarantee arrival by Christmas

The shipping carrier problem: **Cut-off dates**

## Consumers are desperate for last-minute holiday deliveries, exactly when retailers are limited most

### Google searches for "same-day delivery," Dec 2020




Source: Google Trends

**Consumers have an immense appetite for last-minute deliveries during the holidays.**

Google Trends data from last year show that searches for "same-day delivery" began to spike on December 22nd and reached peak popularity on December 24th. This is consistent with Salesforce's findings that online sales last year grew around 58 percent during the five days leading up to Christmas. [15]

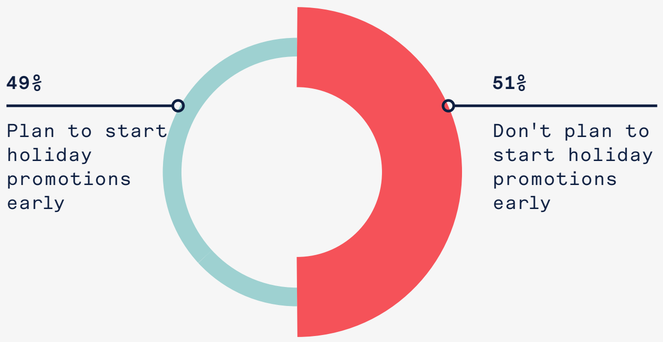
If most retailers have their hands tied during the final week, where do these last-minute online sales go? The answer is clear, if not painful: to the giants who have negotiated preferential treatment from the shipping carriers as well as have their own delivery fleets and supply chain infrastructures in place. The New York Times found that while Amazon's share of e-commerce sales tends to drop around Thanksgiving, it peaks about one week before Christmas — exactly when consumers have no other alternative.[16]

As for those who don't make it under the wire in time, it's estimated that over 2 million packages weren't delivered in time for the holidays last year.[17] And although carriers might argue that retailers' shipments will arrive eventually, a gift that was intended to be opened Christmas morning but instead arrives on December 27th is likely to end up as a return.

Stop-gap solutions

# To overcome these constraints, retailers are planning a number of stop-gap measures

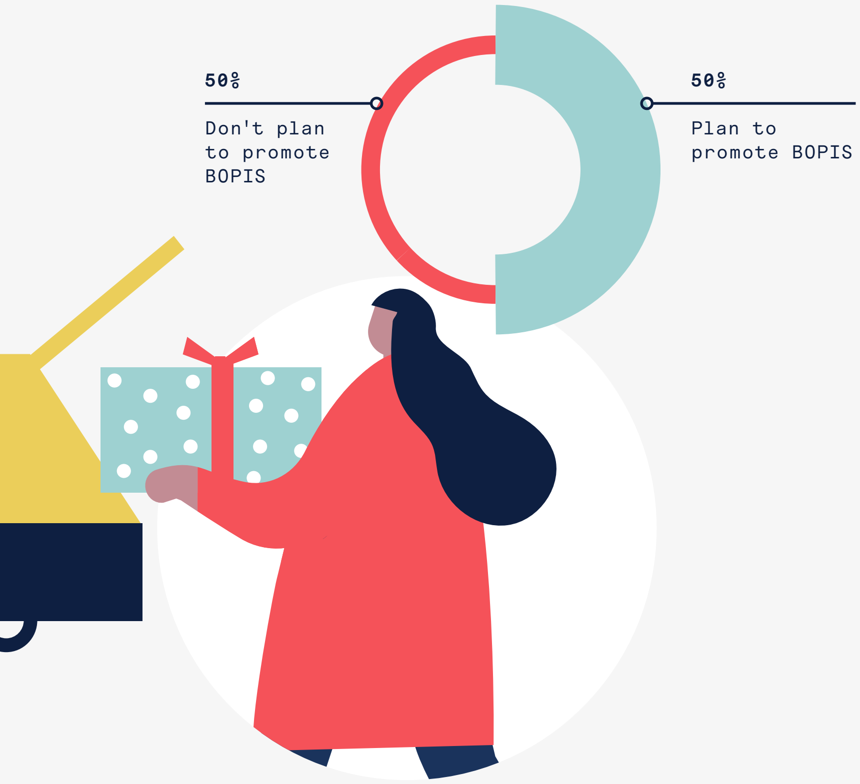
**49 percent of retailers plan to start holiday promotions early**



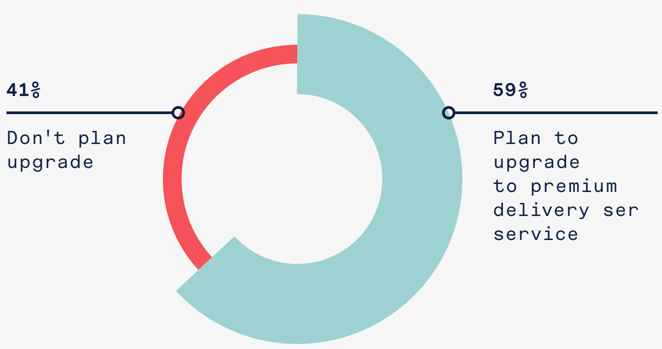

Source: Fabric retailer survey, September 2021

If it seems like the holiday season starts earlier and earlier every year, it's because it does — and "Christmas creep" is just one workaround retailers are pursuing to overcome carrier capacity constraints. Many retailers this year kicked holiday cheer into overdrive at the beginning of October, with Nordstrom unveiling Christmas tree displays in early October [18] and Target promising the "lowest prices on gifts" starting October 10.[19] Both luxury retailer Neiman Marcus and budget chain Big Lots began selling holiday goods such as lights and trees right after Labor Day. In a sense, retailers are trying to "flatten the curve" of the holiday peak by kickstarting it as early as possible, but **such measures still fail to capture the dollars of the inevitable last-minute online shopper.**

### 50 percent of retailers plan to promote buy online, pick up in-store (BOPIS)




### 59 percent of retailers plan to upgrade to a premium delivery service at their own expense




Source: Fabric retailer survey, September 2021

Retailers understand that guaranteeing consumers 11th hour, on-demand deliveries remains a critical service — so much so that given the constraints of cut-off dates, most of them plan to foot the bill of a premium delivery service at their own expense this year. While this would be an expensive undertaking at any time, it's especially costly today.

Curbside pickup is another bandaid measure that enables retailers to side-step shipping carriers altogether and continue selling online during the critical last week of the holiday season. Salesforce found that retailers that offered curbside and in-store pickup options last year increased their digital revenue 49 percent on average year-over-year, while retailers that didn't saw only 28 percent average growth. [20]

While BOPIS is a creative workaround to carrier-imposed cutoff dates, it still doesn't serve the many consumers who'd prefer delivery even if (especially if!) it's the night before Christmas. In its recent holiday retail survey, Deloitte found that **consumers overwhelmingly prefer delivery to BOPIS or curbside pickup:** 73 percent of consumers prefer standard delivery and 47 percent prefer same-day or next-day delivery, while 33 percent prefer buy online, pickup in store and only 21 percent prefer curbside pickup.[21]


Three-day delivery of a two-pound package from New York to Chicago costs more than $14 via UPS and more than $19 via FedEx, and that's without the holiday surcharges. To cover peak-season operating costs, UPS and FedEx have either increased existing surcharges or implemented new surcharges targeting e-commerce shipments. That means that during the winter holiday season, the same three-day delivery of a two-pound package could cost almost $20 via UPS and almost $25 via FedEx. [23]

With these delivery expenses in mind, retailers are between a rock and a hard place when it comes to the consumer appetite for last-minute holiday delivery: they can either pay astronomical shipping costs or lose the sale completely.

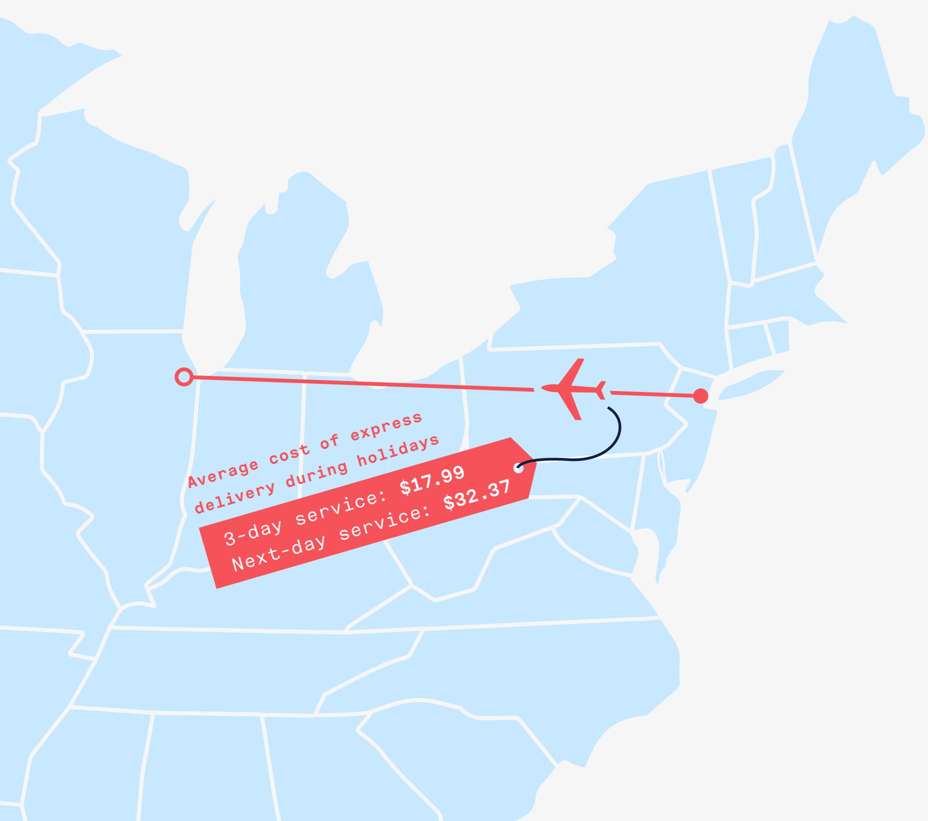
# The retailers who plan to pay for premium delivery to overcome cut-off dates face exborbitant costs

### Cost of shipping a 2-lb package from New York to Chicago

| Service (Zone 5) | Discounted Rate | Residential Peak Premium | 50% discounted residential surcharge | Total |
|---|---|---|---|---|
| UPS 3-Day Select | $14.21 | $3 | $2.50 | **$19.71** |
| UPS Next-Day Air Saver | $24.10 | $3 | $2.50 | **$29.60** |
| FedEx Express Saver | $19.20 | $3 | $2.48 | **$24.68** |
| FedEx Standard Overnight | $23.85 | $3 | $2.40 | **$29.25** |
| USPS Priority Mail | $9.60 | | | **$9.60** |
| USPS Priority Mail Express | $38.25 | | | **$38.25** |
| UPS Ground | $6.76 | $3 | $2.23 | $11.99 |
| FedEx Ground | $6.76 | $3 | $2.48 | $12.24 |

Won't arrive before December 25

Source: Last Mile Experts North America in collaboration with Fabric




## Discount assumptions

- UPS Ground: 50% off
- UPS 3-Day Select: 30% off
- UPS Next Day Air Saver: 65% off
- FedEx Ground: 50% off
- FedEx Express Saver: 10% off
- FedEx Standard Overnight: 65% off
- USPS no discounts

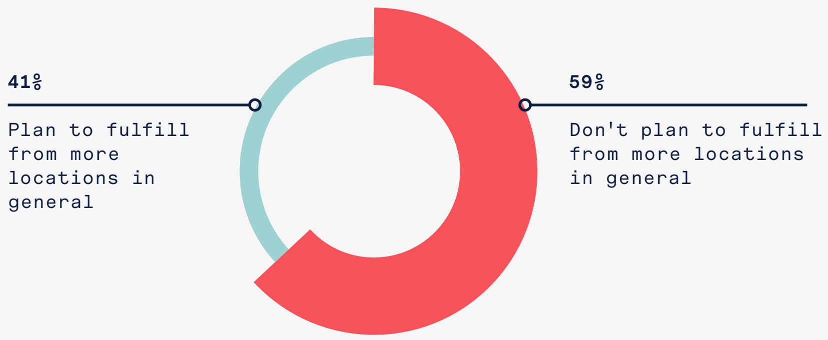
## Additional assumptions

- Existing residential surcharge discount: 50%
- Large shipper volume-based residential surcharge: $3/package
- Ground services: $2 minimum charge discount

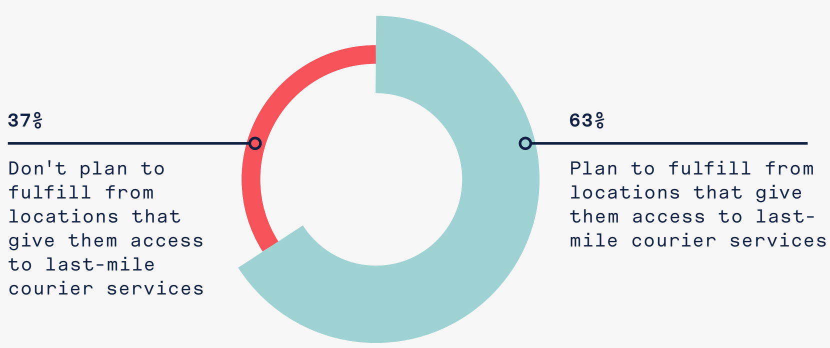
Long-term strategy

# More strategically, 95% of retailers are planning to implement a distributed fulfillment strategy

**57 percent of retailers plan to fulfill from more locations in general**




**63 percent plan to fulfill from locations that give them access to last-mile courier services** such as DoorDash




**63 percent plan to fulfill from locations closer to customers to reduce shipping time**


The vast majority of retailers we surveyed — 95 percent, in fact — reported that they are working to implement a strategy to fulfill e-commerce orders from a distributed network. In order to overcome carrier-imposed capacity limits, 57 percent of retailers we surveyed plan to fulfill from more locations in general, and 63 percent plan to fulfill from locations that give them access to last-mile courier services such as DoorDash. And in order to overcome carrier-imposed cut-off dates, 63 percent of retailers plan to fulfill from locations closer to customers to reduce shipping time.

This indicates that retailers' reliance on shipping carriers is only a symptom of a larger problem. **While centralized fulfillment has traditionally helped brands and retailers reduce fulfillment costs through economies of scale, it's no longer a model that is sufficient on its own.** Most retailers know that in order to sustainably fulfill the influx of online orders at speed and scale, they need to augment their existing operations with a distributed fulfillment strategy in the markets that are most critical for them.

Conclusion

# May your fulfillment networks be merry and distributed

Although carriers are indeed in positions of power vis-a-vis retailers, it's not that they're the villain of this holiday story with hearts that are "two sizes too small;" just like retailers, they are constrained by labor shortages, spiraling costs, and maxed-out capacities. They are only one stakeholder in a vast and complex infrastructure that's been stretched to the limit.

The problem is ultimately a systemic one: the entire paradigm of how goods find their way to consumers' homes has transformed at lightning speed, and no one can keep up. While retailers at the moment might have their heads down, weathering their way through the latest "shipocalypse," when the dust settles, **it will be time to reevaluate the way supply chains work and start taking actionable steps towards a sustainable and long-term solution.**

We believe that retailers and brands would be best served by augmenting their existing fulfillment operations with automated micro-fulfillment in the right markets.

A distributed fulfillment network mitigates risk overall — no longer will retailers' proverbial eggs be in one centralized basket. When working with shipping carriers, retailers can spread their capacity across a distributed network of inventory rather than in just a few larger sites. Crucially, it also enables retailers to work with last-mile courier services in addition to national carriers, alleviating the power imbalance that so painfully limits their selling potential. Finally, fulfilling online orders in close proximity to consumers also enables the fast deliveries that consumers have come to expect at profitable unit economics.

This strategy — fulfilling e-commerce orders from a distributed network of local sites — is a long-term solution that enables retailers to future-proof their businesses and maximize their profits during holiday peaks that will increasingly shift online.

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Fabric

Fabric is a retail technology company on a mission to enable on-demand retail for everyone. By combining highly efficient robotic fulfillment operations with local last-mile operations, Fabric is redefining how supply chains work. The company has developed its own proprietary software and robotic micro-fulfillment technology and is running micro-fulfillment operations for grocery and general merchandise retailers in New York City, Washington, DC, and Tel Aviv. The company will expand to major U.S. metro markets in the coming year.

Fabric has offices in New York City, Tel Aviv, and Atlanta, with over 300 team members globally. Founded in 2015, Fabric is backed by leading investors including Corner Ventures, Innovation Endeavors, Aleph, Playground Ventures, Canada Pension Plan Investment Board (CPP Investments), Evolv (Kraft Heinz), Temasek, Princeville Capital, and more.

For more information visit getfabric.com

How the "Shipocalypse" Stole Christmas:
Why carrier-imposed capacity limits and cut-off dates are revenue killers during the holiday season & what retailers can do about it



The survey is based on responses from the United States from 200 senior managers responsible for supply chain, innovation and digital in e-commerce companies with online revenue of $30M+. The respondents were recruited through a global B2B and consumer research panel, invited via email to complete the survey, with all responses collected during September 2021.