On-demand delivery platforms and implications for the parcels sector

The on-demand delivery sector has grown rapidly over the past few years. Invented as a way of enabling small food outlets and retailers to provide a home delivery service, on-demand providers have tapped into a latent source of consumer demand.

This article explores the sector in more detail including:

- What is meant by ‘on-demand’
- How on-demand business models work
- The economics behind success and failure
- Whether there are opportunities for express parcels companies in the sector
- A case study of GeoPost’s acquisition of an on-demand platform
- Future prospects for the sector

What is on-demand?

In a recent article published in the Supply Chain Forum journal, authors Dablanc *et al* provide the following definition: ‘Instant delivery services provide on-demand delivery within two hours – by either private individuals, independent contractors, or employees – by connecting consignors, couriers and consignees via a digital platform.’*

There are two key elements to this definition.

- On-demand has a timescale attached - in fact a very short timescale of below two hours.
- On-demand is facilitated by a digital platform which matches demand with supply, usually via a smartphone.

On-demand should not be confused with crowd-sourcing or crowd-shipping which refers to the type of transport used rather than the service supplied. Crowd-sourced deliveries often involve private individuals using their own or public transport to fulfil a delivery. This could be a sub-section of the on-demand market but whereas on-demand is growing quickly, crowd-shipping has yet to take off.

‘On-demand’ has also been used interchangeably with other terms such as ‘gig economy’, referring to the use of self-employed contractors working on an ad hoc basis. This also is not strictly accurate as although many platforms’ business models require flexible resources to deal with the peaks and troughs of demand, some on-demand retailers are starting to employ delivery agents directly. This is partly due to regulatory issues and pressure from labour organizations, but also due to issues of control and quality.

Instacart in the US, for example, has recently started to hire many of its contractors as employees, which benefits the company by allowing it to train its workers (the US tax authorities use training as a way of deciding on the status of a worker). Better trained workers improve the customer experience, both in terms of picking goods from stores and the final delivery.

On-demand is perhaps most closely associated with the delivery of meals prepared by restaurants in a local area. However, it is certainly not confined to this sector, with some markets offering on-demand deliveries of:

- Groceries

- Fresh food
- Alcohol
- Laundry
- Consumer goods

Perhaps the most important trend driving the market is the concept of 'instant gratification'. Whether meals, products bought online or fashion items bought at a shop but delivered to buyers' homes, consumers increasingly want immediate access to their purchases. Whether a good thing or not, this is an unalterable part of modern life which suggests that on-demand will be with us for many years to come.

Moreover, it seems inevitable that the market will continue to grow. Consultants BIA/Kelsey estimate that in the US only 7% of the addressable market is served which suggests in other, less mature, parts of the world, the opportunities are even bigger. Other estimates suggest that the UK market is growing at a rate of 10% or more a year, a rate which is probably mirrored throughout the rest of Europe.

How does on-demand work?

On-demand platforms do not regard themselves as logistics or delivery companies. Rather they see themselves as a matching service, allowing consumers to connect with retailers or restaurants.

Some, such as Just Eat or Delivery Hero, do not provide delivery capabilities, instead solely providing the software platform over which consumers can place their orders with restaurants. These are then fulfilled by the restaurants themselves. Others, such as Deliveroo, provide the delivery networks to restaurants which otherwise would not be able to offer home delivery. Even so the latter companies do not own assets, using the services of largely self-employed couriers.

The way these companies define themselves is important. Very recently the European Commission decided that Uber – which regarded itself as a similar platform for personal mobility – was a 'taxi' service provider and should be regulated as such. On-demand platforms may face similar types of regulation in the future, especially if controversy continues over the treatment of sub-contractors.

Another issue which has yet to be fully addressed is the issue of insurance. A normal courier company would provide a range of insurances from public liability to goods-in-transit. Responsibility is potentially unclear in the on-demand chain if the on-demand company is variously regarded as either a restaurant provider, a grocery retailer, a delivery company or, as they would prefer, purely an online platform.

The on-demand business model

In order to attain scale and market leadership, which are essential attributes in the on-demand market, the platforms obviously need to build a strong marketing presence as well as being focused around price.

This is only part of the equation, however. In order to retain both customers and couriers, on-demand providers have to achieve a competitive advantage by developing best-in-class functionality involving:

- Efficient dispatch of orders to couriers
- Availability of good quality couriers
- Capacity planning
- Integrated relationships with consignors

One critical question for companies providing on-demand delivery services is whether or not there is a large enough market to support them.

In order to make a profit, on-demand businesses need to have a high frequency of orders within an operational area, and if this frequency drops below a certain rate, the unit economics of the service are unworkable.

There are two main underlying causes of this:

1. The market was never large enough to support the service in the first place
2. Competition from rival service providers has diluted market share

So long as competing start-ups possess the funding to expand their business, the latter issue can be addressed by pricing incentives for both couriers and consumers in order to build effective economies of scale. However, this inevitably results in financial losses, forcing start-ups in a competitive market to make tough choices when the money begins to run out.

The economics of an on-demand service provider are reasonably straightforward. Revenue comprises:

- Commission charged by the platform to the restaurant (perhaps 25-30%)
- Delivery fee to customer (typically around €2.50/£2.50 in Europe and the UK)

Whereas the costs derive from:

- Fee paid to the courier (per job or per hour)
- Overhead

Therefore, revenues are driven by the value of the meal ordered, their volume, and the delivery fee (if the market allows – 'free delivery' is becoming common). Running costs depend on the utilization rate of the courier, if paid by the hour, although this is not as important if paid by the job. This explains why on-demand companies rely heavily on the 'gig-economy' – the model is far harder to make work if the courier is an employee or a worker paid by the hour. Whether this is sustainable in the long run due to lobbying by unions and governments looking to garner labour taxes is yet to be seen. Of course, couriers have a choice not to work below a certain remuneration and will find better paying on-demand platforms. This will create a vicious cycle – the company will not be able to hire sufficient couriers, leading to longer delivery times and low customer satisfaction. With reducing volumes, more couriers will leave and so it goes on.

According to Adrien Roose, co-founder of TakeEatEasy, an on-demand platform which shut down in 2017, 'Courier utilisation is one of the most important metrics in our business. Assuming couriers need to make minimum 15€ / hour not to churn, a low courier utilisation (<1.5 deliveries / courier / hour) implies a negative contribution margin.'

Bluntly, if on-demand companies are not able to attract and retail good quality contractors they will quickly go out of business. Pay is crucial to this, but some companies are able to provide benefits such as supplementary insurance.

As the on-demand market consolidates, so does a finite supply of financing, and it becomes harder for even some of the larger providers to find more funding when they are losing market share and money. The demise of TakeEatEasy was blamed by senior management on such a situation when even one of its own investors decided to acquire and fund a better placed rival.

Consolidation amongst the existing companies is inevitable, through M&A and bankruptcy. Due to the geographical nature of this market, it is likely that certain companies will dominate in certain countries.

Hong Kong, where Lalamove and GoGoVan are two of the market leaders, has seen the number of competitors shrink over the past five years from approximately 300 to just a handful. Commentators believe that, for this market at least, consumers on their own are not able to create a big enough market. There needs to be a business market as well and these customers are driven by service and reliability rather than cost promotions which can build market share.

These two successful on-demand companies have attracted the most investment. Lalamove has recently been valued at $1billion and has raised $100m with plans for an IPO by 2020. The money will be used to build out its international HQ in Hong Kong and help it reach 200-250 cities across China and South East Asia. GoGoVan says it wants to raise $200m to allow it to develop operations around the world.

Interestingly, the market is moving so quickly that disruptors can themselves become the disrupted. Amazon, for example, in many markets can be regarded as the incumbent, and vulnerable itself to disruption by on-demand retailers. Instacart in the US, by employing agents to pick from established bricks and mortar retailers, is able to provide consumers with 1 hour deliveries and provide a very broad range of goods. In contrast, Amazon has a vertically integrated model, using national and regional distribution centres, perhaps similar to traditional retailers. Instacart can add an on-demand layer to existing retailers' capabilities allowing them to participate in this sector and compete against Amazon.

Are there opportunities for parcels companies in on-demand?

Although on-demand is attracting huge attention from investors, the opportunities for express parcels companies to move into this fast growing sector would seem limited.

On-demand services rely on a critical mass of users and drivers, but on a localized basis. This means that there are very few synergies to be had between the national, regional or global express parcels companies and on-demand operations which work on a city-by-city basis.

The likes of FedEx, UPS, and DHL operate models which rely on the movement of vast volumes of parcels in order to maximize the utilization of national and international network infrastructure rather than the instant collection and delivery of an order within a limited area.

However, that has not stopped one major parcels company, GeoPost, from exploring the sector. The subsidiary of the French post office has acquired outright an on-demand operator, Stuart, in which it originally took a minority shareholding in 2015.

As is indicated in the case study below, although there will be a certain amount of integration with GeoPost the operation will remain autonomous.

Case study: GeoPost and Stuart

GeoPost has acquired 100% of Stuart Delivery Ltd's share capital, having acquired a 22% share in 2015.

Founded in 2015 by Clément Benoît and Benjamin Chemla, Stuart is a technology platform which connects retailers with a fleet of independent couriers to help business meet the delivery expectations of their end-customers.

Stuart has built algorithmic dispatch for both on-demand and scheduled jobs, and integrated its API with leading multinational retailers across France, the U.K. and Spain. With 100 employees across technology, data, product, operations and business development, Stuart facilitates thousands of deliveries per day for more than 500 active customers including Carrefour, Franprix, Burger King, The Kooples, Pizza Hut and Cdiscount.

Paul-Marie Chavanne, GeoPost's CEO, stated that "This decision logically follows our investments in Stuart over the past 2 years. Stuart completes our delivery service at a local level and embodies the future of express urban delivery, a rapidly expanding strategic activity for us."

Benoît and Chemla further commented: "We are extremely proud of the journey that we and our more than 100 employees have taken over the last two years. GeoPost's acquisition will enable Stuart to maximise its potential and become the leading player in last mile delivery in Europe."

Stuart will remain an independent brand and subsidiary in order to ensure the autonomy of its management team and its commitment to technological innovation. However, the company will be co-chaired by Diego Magdelénat and Paul-Ambroise Archambeaud, the founders of Pickup, a start-up specialising in alternative delivery which GeoPost acquired in 2009. Pickup's leaders will integrate Stuart within GeoPost in order to maximise synergies between the companies, including developing value-generating solutions for the Group's customers.

As well as operational, there are other reasons why express parcels carriers may not be keen to buy into the market. In some quarters the sector is regarded as highly toxic due to the controversy over working practices and remuneration in the 'gig economy'.

If they were to consider entry, cost may also put them off. Acquiring an established player, such as Deliveroo, would be very expensive, with investors looking to realise highly inflated multiples. Instead, as with GeoPost, it is more likely that acquirers would look at an early stage start up (like DHL did to develop their Saloodo road freight platform), or hire some expensive and clever engineers to get them to develop the technology internally.

Conclusion

Just because there are few synergies between on-demand and express parcels networks does not necessarily mean that we should look upon GeoPost's acquisition of Stuart as an isolated acquisition. As the on-demand sector becomes more mature, more opportunities for express companies to become involved in the market may well present themselves. For example, the technology which underpins the platforms may well prove useful in B2B sectors such as Service Parts Logistics, providing a step change in the costs of fulfilling narrow delivery windows to meet service level agreements. The delivery of restaurant food may well be the start for many providers, but the future of on-demand may well be other business sectors which still remain untouched.

In the end, the market may just become too big for the express parcels giants to ignore. However, for the time being, the risks of picking the wrong on-demand provider are probably too great – it would seem more sensible to let financial investors bear the strain of building the necessary scale or indeed losing their stakes if they fail.

Reference

**Laetitia Dablanc, Eleonora Morganti, Niklas Arvidsson, Johan Woxenius, Michael Browne & Neïla Saidi (2017) The rise of on-demand 'Instant Deliveries' in European cities, Supply Chain Forum: An International Journal, 18:4, 203-217*

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