

**Klarna.**

# Re-thinking returns: A strategic advantage



**Klarna  
Confidential**

Quick advice  
for merchants

The online shopping experience is not always a linear affair. It's frequently a cyclical journey where 'returns' play a central role, influencing purchasing decisions and brand loyalty. Klarna believes that retailers who focus on creating 'positive return-experiences' are more likely to increase sales and boost profit.

Returns are crucial for online retailers as shoppers are unable to feel or try items before they buy. This means there's more chance they will opt for a refund. Studies show that a frictionless return policy is the most important decision making factor for online shoppers of clothing and apparel. Even more important than price.<sup>1</sup>

### Returns and the law

Legally, retailers must offer customers the option of returning goods bought online within 14 days.

Once shoppers inform the retailer they have another 14 days to return the goods. They must then be refunded within 14 days of the retailer receiving the goods back.

Some retailers choose to extend this period giving shoppers as much as 90 days.

Klarna recently commissioned leading analyst Ovum to ask merchants their thoughts on returns:

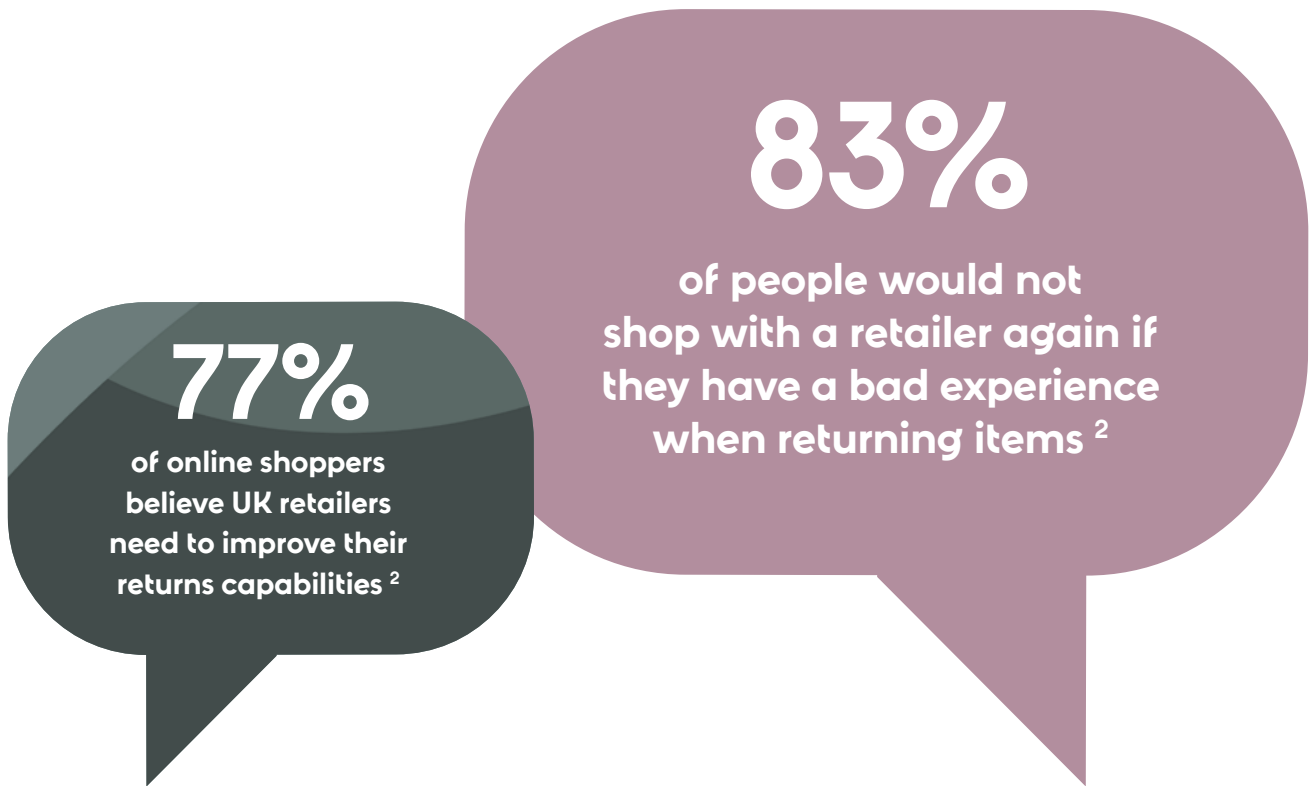
**98%** of retailers feel free returns help increase online sales

**83%** feel they need to improve their return capabilities

**80%** feel millennials are shaping their returns policy

**78%** feel returns can be a competitive differentiator





### Impact on bottom line

Consumers' inherent desire to 'try before they buy' makes online return rates higher than bricks and mortar. For online apparel, it's 20% and for expensive items it can be as high as 50%. In physical stores, it's around 10%.<sup>3</sup>

For some retailers managing the 'reverse logistics' of returns is a major issue. And a huge cost burden for their business. Up to 60% of retailers believe they are negatively impacted by consumers increasingly returning unwanted items. And 30% of online-only retailers admit that managing returns affects their profit margins.<sup>4</sup>

Consequently, a fifth of businesses increase item price to cover the cost of processing customer returns.<sup>4</sup>

But attempting to prevent profit erosion by introducing barriers to returns; or recouping costs through delivery charges, can end up costing sales. 58% of shoppers say a retailer's returns policy impacts their decision to make a purchase online. And 47% would not order an item if they had to pay to return the item.<sup>4</sup>

## Creating sales leverage

**By introducing policies that lock down returns, online retailers are missing a massive opportunity. Their best customers can have the highest return rates and still be the most profitable. They may send unsuitable items back but they also keep more, generating more overall revenue in the long term. Restricting returns simply sends them elsewhere.**

At Klarna, we see the same behaviour with consumers that choose our Pay later service. Because they have more time to pay, the urgency for immediate return is diminished and they are more likely to retain the purchased goods.

### Endowment effect

Giving consumers more time to return items can deliver a clear sales benefit and a reduction — not an increase — in returns.<sup>5</sup> One of the explanations is the “endowment effect”. This is when the longer a customer has a product in their hands, the more attached they feel to it. It also reduces the urgency around the decision over whether to take it back — and after time it becomes less important.

### No-questions-asked

No-questions-asked policies are also likely to increase purchase rates, particularly among younger audiences and those who choose to browse and buy via mobile.



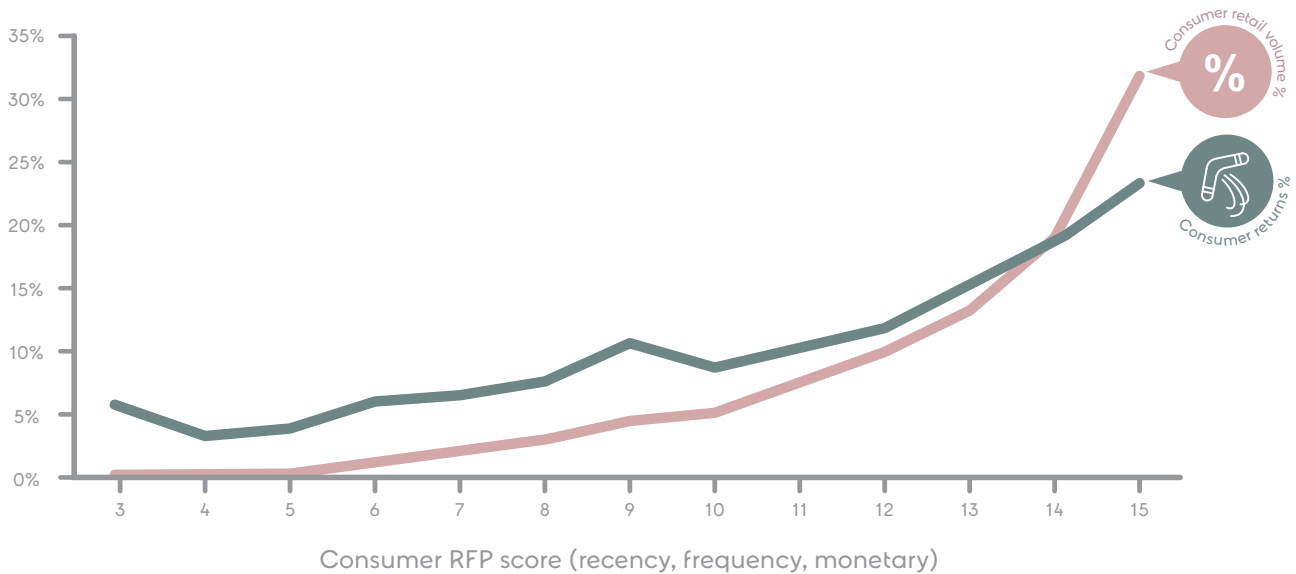
### The rise of the serial returner

In the UK, 63% of women who shop for clothing online returned at least one item.<sup>6</sup> And up to 30% of customers deliberately over-purchase because they can easily return unwanted items, using options such as hourly courier services and local drop-off points. These ‘serial returners’ are regularly blamed for pushing up prices – by tying up stock, incurring high costs and drawing discretionary discounts and offers.

But not all serial returners are ‘Bad’, there are ‘Good’ returners who are profitable because they buy more, keep more and regularly up sell and cross sell. At Klarna, our own customer analysis shows that higher returns are associated with higher value customers who also retain a higher volume of goods.

**83%**  
of people would not shop with a retailer again if they have a bad experience when returning items <sup>2</sup>

### Customer returns, retention and customer value



The secret is being able to differentiate between good and bad, profitable and non-profitable returners. Retailers can use CRM and purchase behaviour analysis to identify these and ensure promotions, campaigns and policies are targeted at the most lucrative audience.

Retailers also need to look holistically at the reasons their customers are locked into this behaviour. For example, with clothing and apparel, it may be that they have no confidence in retailers’ size/fit. So, they buy products in multiple sizes – using their bedroom as a changing room, and sending back what doesn’t work for them. Four in ten shoppers believe standardising clothing and shoe sizes would help them return less frequently.<sup>4</sup>

## Returns and the consumer mindset

Over 2,000 UK online consumers were interviewed for independent research commissioned by Klarna.

### Here's what we discovered:

- **Attitudes to returns vary.**  
35% of online consumers return unwanted items immediately. While 13% NEVER return items. Over 38% of consumers return unwanted items, no matter what. Yet 27% are put off by the 'hassle factor'

- **Fashion has the highest return rate.**  
Consumers annually return 44% of clothing bought online. By comparison only 4.5% of home furnishings are returned. 26% of returns are due to issues with sizing. 40% have ordered multiple items to try on at home and then returned the ones they didn't want
- **A relatively small proportion of overall purchases are returned annually.**  
More than three quarters of online shoppers say they return less than 10% of their purchases annually. And 36.7% have not returned any items. Return values are also relatively low. 43.5% say their annual returns are less than £100
- **Return processes can impact sales.**  
35% would like more retailers to offer unlimited free returns. And 32% want more options for return processes. 64% will only shop with retailers that offer free returns

*'Try before you pay'  
payment options  
encourage more uplift  
than returns<sup>2</sup>*

If Pay later were offered:

**25%** would trust a retailer more<sup>2</sup>

**25%** would be more loyal<sup>2</sup>

**25%** more likely to try a new retailer<sup>2</sup>

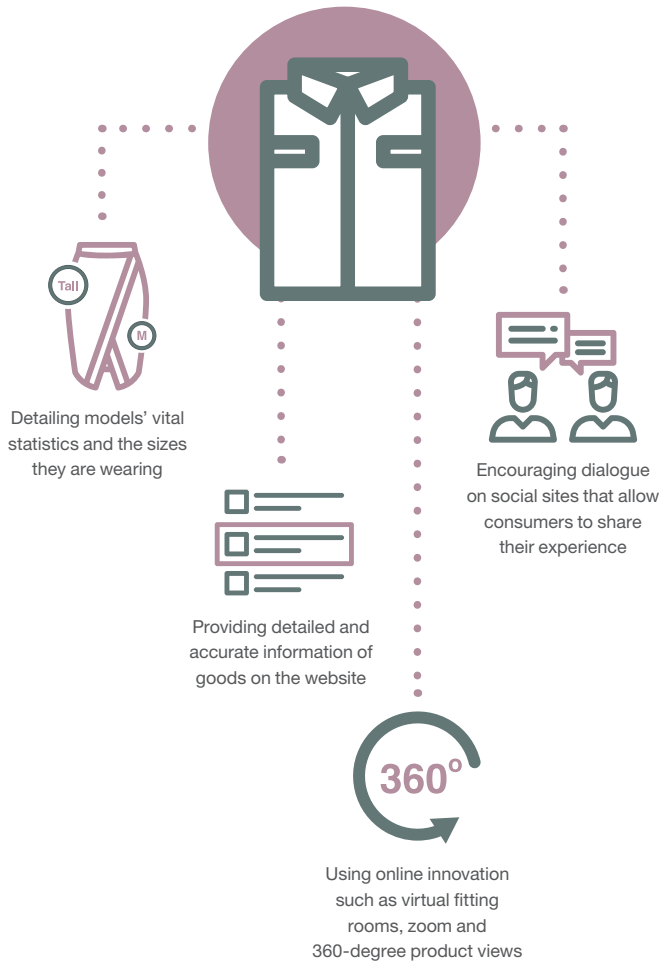
**23%** more likely to purchase<sup>2</sup>

Only **9%** would return more items<sup>2</sup>



## Getting returns right

Taking steps to get the product ‘right-first-time’ goes a long way in alleviating the burden of serial returners – particularly for fashion retailers. This can include:



Pinpointing the optimal returns policy is a complex process. Retailers may have to choose between boosting overall sales or cutting the number of returns. Or to have different return criteria depending on the item and the target audience. If they choose to keep costs low by restricting value added services that could increase returns, they risk compromising their competitiveness.

In the online world, returns are an inevitable part of doing business. The real opportunity for retailers lies in minimising the impact of returns while meeting – and exceeding – customer expectation.

### This can be managed in many ways.

- Investing in technology to aid logistics; linking ERP and operational processes to optimise efficiency
- By providing returnable packaging and ensuring clear and accurate returns information is included with the delivery
- Supplementing customer communications with self-serving return portals or easy access to customer support
- Using payment services like Klarna's Pay later to minimise payment friction; reduce 'commitment fear' and urgency of return

By shifting their perspective on returns from a cost-based view to a customer relationship perspective, retailers can help reassure buyers, build loyalty and differentiate their brand in an increasingly crowded virtual marketplace.

From experience, it's clear that what today's buyers really want is convenience, a seamless experience, good customer care and simple and fast refunds.

## Understanding returns

- 'Serial Returners' can be among the most loyal and profitable customers
- Longer return times can result in fewer returns
- Simple and easy returns differentiate and boost sales
- Virtual changing rooms, social feedback and standard sizing can help reduce clothing returns
- Klarna's Pay later can make 'return decisions' less urgent, increasing the likelihood goods will be kept

1. Granify Survey of 20.8 million consumers. 2. Independent consumer research commissioned by Klarna, Feb 2017, 3. Forrester 4. Barclaycard. 5. University of Texas-Dallas. 6. Savvy Marketing, Radio 4 Survey