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Thinking inside the subscription box: New research on e-commerce consumers

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We surveyed thousands of US shoppers to understand subscription e-commerce trends. The findings have implications for start-ups, as well as retailers and consumer brand manufacturers entering the market.

Subscription e-commerce, led by start-ups such as Dollar Shave Club, Blue Apron meal kits, and Stitch Fix personal styling, is a fast-growing new way of buying online. Our research shows that 15 percent of online shoppers have signed up for one or more subscriptions to receive products on a recurring basis, frequently through monthly boxes. Subscription e-commerce services offer these consumers—often younger, affluent urbanites—a convenient, personalized, and, often lower-cost way to buy what they want and need. Churn rates are high, however, and consumers quickly cancel services that don't deliver superior end-to-end experiences.

The subscription e-commerce market has grown by more than 100 percent a year over the past five years. The largest such retailers generated more than $2.6 billion in sales in 2016, up from a mere $57.0 million in 2011.[1] Fueled by venture-capital investments, start-ups have launched these businesses in a wide range of categories, including beer and wine, child and baby items, contact lenses, cosmetics, feminine products, meal kits, pet food, razors, underwear, women's and men's apparel, video games, and vitamins.

This strong growth has attracted established consumer brand manufacturers and retailers, which have also entered the space; for example, P&G (Gillette on Demand), Sephora (Play!), and Walmart (Beauty Box) have all launched new subscription businesses. The market has also seen significant M&A activity—in particular, Unilever's $1 billion acquisition of Dollar Shave Club (2016) and the $200 million-plus deal that the grocery chain Albertsons did for meal-kit company Plated.

To better understand the drivers of the subscription e-commerce market, we surveyed more than 5,000 US consumers (see sidebar, "Our survey methodology"). The goal was to assess the overall penetration of e-commerce subscription services and the demographics and buying

[1] Reflects revenue for subscription e-commerce companies on Internet Retailer's Top 500 list.

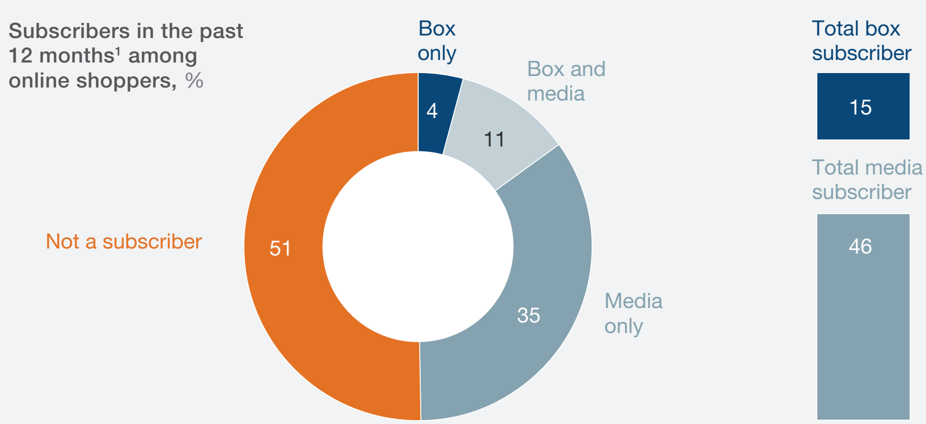
behavior of their consumers. We also wanted to understand why consumers subscribe and why they cancel their subscriptions, an overriding worry for players in this space. Our article summarizes the survey's high-level insights, which have important implications for subscription e-commerce companies—either start-ups or larger entrants—as they seek to accelerate the building of scalable, profitable businesses.

Adopting the subscription lifestyle

Subscriptions are an increasingly common way to buy products and services online. Although streaming-media subscriptions have been popular for some time—46 percent of consumers in our survey subscribed to an online streaming-media service, such as Netflix—shoppers are now also turning to subscriptions for consumer goods. Our research indicates that 15 percent of online shoppers have subscribed to an e-commerce service over the past year. Most e-commerce subscribers have streaming-media subscriptions as well (Exhibit 1).

Exhibit 1

Subscriptions are an increasingly common way to buy products and services online.



Note: Figures may not sum to 100%, because of rounding.

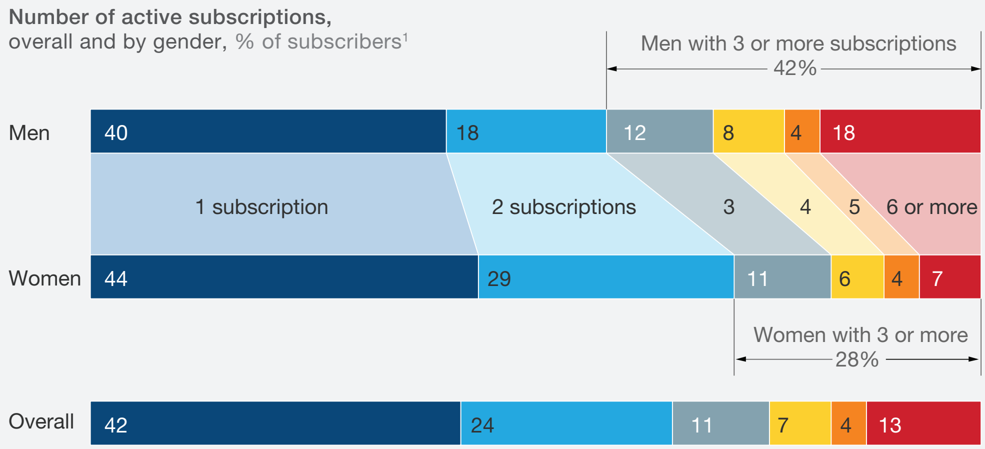
[1]Which of the following have you purchased or subscribed to in the past 12 months? % of those selecting online subscription-box service that delivers products regularly (eg, Blue Apron, Dollar Shave Club, Ipsy, Stitch Fix), subscription-based media (eg, ClassPass, Hulu, Netflix, Spotify), both, or neither.

McKinsey&Company | **Source:** McKinsey analysis

E-commerce subscribers tend to be younger urbanites with money. Compared with the general US population, they are more likely to be 25 to 44 years old, to have incomes from $50,000 to $100,000, and to live in urban environments in the Northeastern United States. These subscriptions particularly appeal to women, who account for 60 percent of them.

Exhibit 2

Women account for the majority of subscriptions, but men are more likely to have three or more active subscriptions.



Note: Figures may not sum to 100%, because of rounding.

[1]When was the most recent time you subscribed to the following online subscription-box service? Count of respondents by gender and overall selecting "currently subscribe" from a list of 34 subscription-box companies, including Blue Apron, Dollar Shave Club, Ipsy, and Stitch Fix. Overall n = 435; men n = 179; women n = 250.

McKinsey&Company | **Source:** McKinsey analysis

For those who subscribe, the model can be quite appealing. The median number of subscriptions an active subscriber holds is two, but nearly 35 percent have three or more. Male shoppers are more likely than women to have three or more active subscriptions—42 percent versus 28 percent, respectively—suggesting that men particularly value automated purchasing and the ability to limit store trips (Exhibit 2).

There are three broad types of subscriptions: replenishment, curation, and access. Replenishment subscriptions allow consumers to automate the purchase of commodity items, such as razors or diapers. Curation subscriptions seek to surprise and delight by providing new items or highly personalized experiences in categories such as apparel, beauty, and food. Last, access subscribers pay a monthly fee to obtain lower prices or members-only perks, primarily in the apparel and food categories. Curation services, with 55 percent of total subscriptions, are by far the most popular, suggesting a strong desire for personalized services. Replenishment accounts for 32 percent of subscriptions and access subscriptions for 13 percent (Exhibit 3).

The most popular services are Amazon Subscribe & Save (consumer packaged goods) and Dollar Shave Club (razors), which have nearly twice as many subscribers as the next services on the top ten list (Exhibit 4). Ipsy (beauty), Blue Apron (meal kits), and Birchbox (beauty) round out the top five. Both men and women, buying for themselves or for others, use many of the leaders, but women are more likely to subscribe to beauty and apparel services, including Stitch Fix (apparel), AdoreMe (lingerie), and ShoeDazzle (shoes). Men, by contrast, are much more likely to gravitate to razors (Harry's is the third-most-popular service for men but the seventh overall), video-gaming gear and collectibles (Loot Crate), and meal-kit or food-delivery services (Home Chef and Instacart's subscription delivery option, in addition to Blue Apron and HelloFresh).

Exhibit 3

E-commerce subscriptions generally fall into one of three categories.

E-commerce subscriptions, %		Key consumer value	Description	Example companies
Subscribe for replenishment	32	Save time and money	Replenish the same or similar items Primary categories are commodity items such as razors, vitamins	Amazon Subscribe & Save, Dollar Shave Club, and Ritual
Subscribe for curation	55	Be surprised by product variety	Receive a curated selection of different items, with varying levels of consumer decision making required Primary categories are apparel, food, beauty products	Birchbox, Blue Apron, and Stitch Fix
Subscribe for access	13	Gain exclusive access	Membership provides access and can convey additional "VIP" perks Primary categories are apparel, food	JustFab, NatureBox, and Thrive Market
	100%			

McKinsey&Company | **Source:** McKinsey analysis

Exhibit 4

Men and women gravitate to different types of subscription e-commerce offerings.

Top 10 sites with highest number of current subscribers by gender

McKinsey&Company | **Source:** McKinsey analysis

Many of the most popular services (including Birchbox, Dollar Shave Club, and Ipsy) charge relative low monthly fees of $10 or less. Others, such as Blue Apron and Stitch Fix, have higher fee structures and can therefore generate higher revenues on a smaller customer base; for example, Blue Apron's average order value was $58 and its average revenue per customer was $245 in the third quarter of 2017.[2]

Expecting great experiences, not great subscriptions

Consumers do not have an inherent love of subscriptions. If anything, the requirement to sign up for a recurring one dampens demand and makes it harder to acquire customers. Rather, they want a great end-to-end experience and are willing to subscribe only where automated purchasing gives them tangible benefits, such as lower costs or increased personalization, as our interactive Exhibit 5 shows.

A recommendation, including word of mouth and positive online reviews, is a key trigger for consumers to sign up with a subscription service, particularly those for curation and access. Subscribers to both also want something new and innovative. In contrast, replenishment subscribers are more motivated by financial incentives, such as discounts, and by a strong need for the product.

To continue subscribing, consumers (particularly curation and access subscribers) expect personalized subscriptions to become more tailored over time: 28 percent of both groups said that a personalized experience was the most important reason for continuing to subscribe. Curation subscribers also want to be surprised and delighted and to feel they are getting good value for the money. In contrast, access subscribers emphasize convenience as a reason to subscribe, in addition to personalization. For replenishment subscribers, convenience (24 percent) was the most important consideration, though value for the money (23 percent) and personalized experiences (22 percent) were also important.

Finally, consumers are quick to cancel services that don't deliver a superior experience—for example, because of poor product quality, dissatisfaction with the assortment, or a lack of perceived value. Curation and access subscribers also cancel when they don't feel that they are getting value for the money, probably because these services offer more discretionary products. A key challenge for all subscription e-commerce providers is matching supply and demand; consumers are much more likely to cancel when products pile up or they can't customize order volumes to match their actual requirements (for example, if they are going on vacation or need less product in a given week or month). In these situations, subscribers say they would prefer to buy the products when they need them, either in stores or from transactional e-commerce services, instead of subscribing.

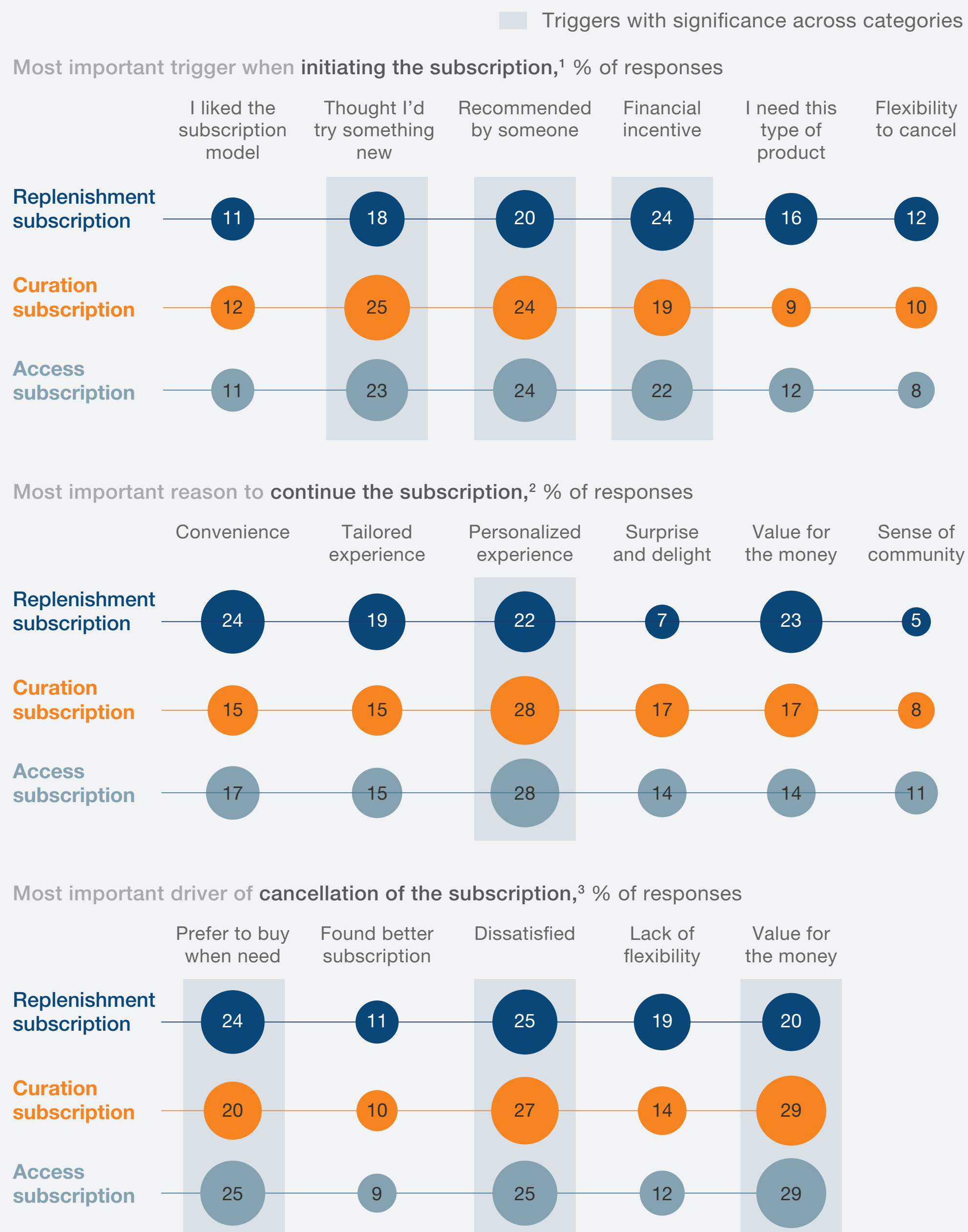
Making the subscription model work

It can be difficult for subscription e-commerce companies to acquire and then retain consumers. On the acquisition side, only 53 percent of consumers know about even one

[2] "Blue Apron Holdings, Inc. reports third quarter 2017 results," November 2017, investors.blueapron.com.

Exhibit 5

Recommendations often trigger subscriptions, but consumers cancel services that don't deliver a superior experience.



[1]In response to questions: Thinking back to when you first started thinking about subscribing to [brand], what are the 3 main reasons you subscribed to [brand]? Which of the following is the most important reason you first started thinking about subscribing to [brand]?
[2]In response to question: Now, what is the most important reason why you continue to subscribe to [brand]?
[3]In response to question: You indicated that you used to subscribe to [brand] but no longer do. Which reasons below best describe why? Note: Only showing individual brands that were answered by 40 or more respondents.

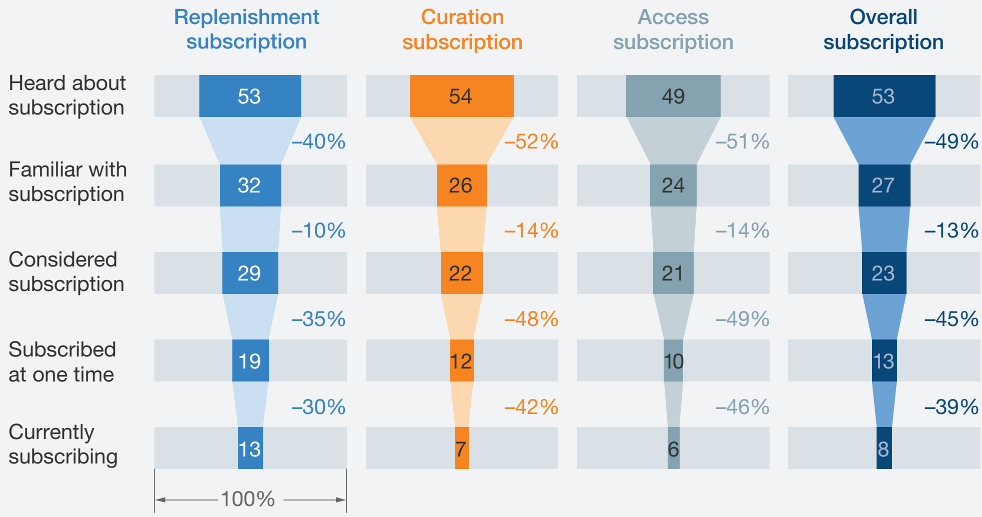
McKinsey&Company | **Source:** McKinsey analysis

of the top services. Moreover, conversion is weak: only 55 percent of those who consider a service ultimately subscribe, probably because people are reluctant to sign up for a long-term commitment. Replenishment services have a higher conversion rate than curation or

Exhibit 6

Acquiring and converting customers for subscription services is a challenge—but there's room to grow.

Performance across purchase funnel[1] by type of subscription e-commerce service,[2]
% of subscriber responses



[1]In response to questions: How familiar are you with the following brands of online subscription-box services? Answer options: never heard of; heard of, not familiar; or familiar. Have you ever subscribed to any of the following online subscription-box services? Never considered subscribing, considered but did not subscribe, or subscribing. When was the most recent time you subscribed to the following online subscription-box services? Currently subscribed, subscribed in the past but canceled.
[2]People who are currently subscribing or have subscribed in the past year.

McKinsey&Company | **Source:** McKinsey analysis

access services (65 percent, 52 percent, and 51 percent, respectively). But the subscription e-commerce market has plenty of room to grow as more consumers become aware of it (Exhibit 6).

The bigger challenge facing subscription e-commerce companies is churn. These businesses depend on their long-term relationships to provide predictable revenue growth and deep insights into customer behavior to personalize the experience. Churn can dramatically undermine their viability, since the cost of replacing lost subscribers could not only make it difficult to meet their growth objectives but also quickly drain their cash reserves.

Overall, we found that nearly 40 percent of e-commerce subscribers have canceled their subscriptions. These rates are similar across replenishment, curation, and access subscription services. The higher the churn rate, the more difficult it becomes for subscription e-commerce companies to cover their acquisition costs and to scale their revenues.

Many consumers who churn do so quickly, which suggests that companies should be careful not to overinvest in free trials or heavy discounts unless these promotional investments have a clear payback. More than one-third of consumers who sign up for a subscription service cancel in less than three months, and over half cancel within six. The meal-kit category seems to have particularly high rates of cancellation within the first six months (60 to 70 percent and higher), probably reflecting highly competitive prices and broad similarities among the leading players.

The good news is that subscription e-commerce consumers can be sticky once they find a service they like. Replenishment services have particularly high long-term subscription rates: 45 percent of members have subscribed for at least one year, about ten percentage points higher than the level for curation or access services. The companies with the highest long-term subscription rates include Amazon Subscribe & Save, Dollar Shave Club, Ipsy, JustFab fashion, and Loot Crate.

■ ■ ■

The subscription e-commerce market is growing quickly. For consumers, subscription products or boxes offer a convenient, personalized, and often lower-cost way to buy what they want and need. Companies in the space must develop great experiences (as opposed to great subscriptions) to avoid high churn rates and to accelerate both growth and profitability. □

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Our survey methodology

We had an online survey in the field from November 8 to 12, 2017, and garnered responses from more than 5,093 participants in the United States. Of those, 4,057 (80 percent) were online shoppers, defined as people who had spent at least $25 online in the past month. Of those, 607 (15 percent) had subscribed to at least one service over the past 12 months. Most of our analysis centers on the stated preferences and behavior of this subset of survey respondents.

In addition, we examined the respondents' familiarity and history with 34 of the leading subscription services (including Amazon Subscribe & Save, Birchbox, Blue Apron, Dollar Shave Club, and Stitch Fix) across numerous product categories. Of the 607 subscribers in our sample population, 505 answered this set of questions.

Our survey sample reflected the population of the United states and had a margin of error of plus or minus 3 percent for gender, age, income, and ethnicity.

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