We analyze the incentives for incumbent bricks-and-mortar firms and new entrants to start an online retail channel in a differentiated goods market. To this end we set up a two-stage model where firms first decide whether or not to build the infrastructure necessary to start an online retail channel and then compete in prices using the channels they have opened up. Consumers trade-off the convenience of online shopping and the ease to compare prices, with online uncertainties. Without a threat of entry by a third pure online player we find that for most parameter constellations firms’ dominant strategy is not to open an online retail channel as this cannibalizes too much on their conventional sales. As the cannibalization effect is not present for a pure Internet player, we show that these firms will start online retail channels under a much wider range of parameter constellations. The threat of entry may force incumbent bricks-and-mortar firms to deter entry by starting up an Internet retail channel themselves. We also show that a low cost of building up an online retail channel or online shopping conveniences may not be to the benefit of online shopping as the strategic interaction between firms may be such that no online retail channel is built when the circumstances seem to be more favourable.

Keywords: E-Commerce, Internet, multichannel competition, online uncertainty, online shopping convenience.

JEL Codes: D43, L13, M30