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WHATEVER.COM PHASE II – SEEKING SOURCES OF STRATEGIC ADVANTAGE VIA THE INTERNET

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In August 1999 we published a monograph entitled “*Whatever.com – Strategic Thinking for the Economy*” to begin a dialog with our clients and friends about the strategic influence the Internet is and can have on their businesses. Given the rapid pace of change, growth and development both on the Internet and in the economy generally, the time has come to update and expand upon that discussion.

Since last summer, e-commerce has grown rapidly. The early research indicates that 1999 online sales exceeded projections. Further, holiday season sales far exceeded projections and, for the most part, online shoppers were satisfied with their experience (e.g., over 90% of those responding to surveys indicated that they will return to the Internet to shop in 2000).

Yet, virtually all of the underlying strategic principles we laid out in our first “*Whatever.com*” monograph have proven to be on the mark.

- Supply chain reconfigurations, improvements, and disruptions continue to emerge at a rapid pace – to the benefit of the savvy and the detriment of others.
- Both “*pure play*” e-commerce companies and “*clicks and mortar*” incumbents are creating unique advantages using the web as a sales and marketing channel.
- Changes in the availability, cost, and management of information are yielding an unending stream of positive case studies as well as horror stories.
- Finally, companies that exist solely on or because of the Internet (e.g., portal companies, ISPs, etc.) are exploiting the novel aspects of this marketplace. For instance, portals are cementing their positions as the most visited sites on the web and are gaining a real advantage from that position (Yahoo is tremendously profitable, AOL is now much more than an ISP and portal, etc.).

In this monograph we explore sources of strategic advantage in three areas – supply chain reconfiguration; channel management; and information management. Each presents opportunities for virtually any business – traditional or “*pure play*.”

SUPPLY CHAIN RECONFIGURATION

There has been a great deal of research – and hype – around the concept of disintermediation (i.e., the elimination of intermediaries within a supply chain via the Internet). In our view, one man’s disintermediation is another’s intermediary. Very few genuine cases of disintermediation exist. Rather, new web-based intermediaries are simply displacing traditional intermediaries – both at the retail and wholesale distribution levels.

- Genuine disintermediation does occur, however. Take the Advanced Book Exchange as an example. ABE compiles lists of rare and out of print books available from book dealers around the country. A bibliophile looking for a particular edition of a particular title can search ABE's database and then deal directly with the book dealers offering the title – no middleman, no distributor, just a new means to make direct contact between a buyer and a seller.
- Most examples of disintermediation cited by researchers and pundits, however, are nothing more than one intermediary displacing an incumbent.
 - Amazon.com displaces other book retailers – it does not link the buyer directly to publishing houses.
 - Metalsales.com brokers overstocks and out of specification roll stock – it displaces a role played by metal service centers, but does not directly connect buyers to major steel companies.
 - eBay is displacing classified advertising (in most instances) – not eliminating the need for an intermediary.
 - While there are a number of interesting and compelling business models at work (e.g., buyer and/or seller “marketplaces,” few-to-few, many-to-many, one-to-many, etc), most are new types of intermediaries – not genuine disintermediation.
- Jim Seymour of PC Magazine notes that there are cases of “reintermediation” occurring. For instance, Alibris acts as an intermediary of rare and out-of-print books – sourcing, “inspecting,” and repackaging the same rare books that one can purchase directly via a search of ABE. Alibris grew its business by buying Interloc – a genuine disintermediary much like ABE. Thus, Alibris has actually “reintermediated” the rare book market.

CHANNEL MANAGEMENT

As we pointed out in the first “*Whatever.com*,” traditional bricks and mortar incumbents enjoy certain advantages that, when coupled with a compelling e-channel strategy, can be used to win in a competitive marketplace. For instance, manufacturers have more control and influence over the supply chain, account for more of the margin inherent in a product, and have a choice of market channels. Contrast this to an Internet intermediary of that same manufactured product – they are restricted to a single channel, cannot integrate (or disintegrate) the supply chain to improve costs or margins, and thus, must rely on an imaginative combination of pricing, service, and agility to capture market share.

Even traditional retail and wholesale intermediaries can establish or defend advantages that their Internet-base competitors lack. For instance, most wholesale intermediary businesses are built on reputations and relationships. While a low price, nimble Internet-based competitor enjoys important advantages, the incumbent might be able to defend core relationships simply by deploying online order tracking and order entry systems – augmenting the positive relationships a direct sales force has built over many years.

And, the rise of “*experience-based*” retail stores bodes well for some retail intermediaries. For instance, can an Internet-based store (i.e., web site) really displace the experience a mother and daughter have during an outing to the American Girl store?

Published research on many fronts is beginning to underscore the strong long-term advantages smart “*clicks and mortar*” incumbents have over their “*pure play*” competitors.

- A joint study by eStrategy consulting firm Mainspring and Bain & Company (December 1999) found that retailers who combine on and off-line assets have stronger customer economics than Internet “*pure plays*.”
- Similarly, Mercer Management Consulting documented the advantages of a hybrid “*clicks and mortar*” strategy in a recent research piece entitled “*E-Venge of the Incumbents*.” Mercer found customers’ expectations are more likely to be met by a combination of online and offline capabilities (creating disadvantages both for “*pure plays*” and for traditional brick and mortar companies).
- Web rating agency Media Metrix found that the “*clicks and mortar*” competitors have made significant strides over the past year in bringing hybrid approaches to the market. In 1999, five traditional competitors’ web sites cracked Media Metrix’ top 25 most visited sites – Barnes and Noble (4th), Toys R Us (5th), KB Kids (12th), and JC Penney. No traditional companies’ sites made the top 25 in 1998.
- International Data Corporation goes even further and predicts that “*pure play dot.com companies will gradually peter out this year (2000)*.”

While we stop short of predicting the demise of the “*pure play*” dot.com companies, we have long been convinced that traditional companies, with an effective channel strategy – one that leverages the advantages of physical infrastructure and web enabled efficiencies – are best positioned to win in the new economy.

INFORMATION MANAGEMENT

There are countless examples of the power of Internet enabled information management. Simply, the Internet provides a tool for information networking and management that can have a dramatic impact on business performance – for good and for ill.

A few positive examples of how the Internet is being used as a backbone for information management follow.

- Kaiser Permanente is using the Internet and its own network to improve the quality of care, reduce errors, and cut costs. Among the solutions Kaiser has deployed are online prescription drug screens, online appointment scheduling, Internet-enabled patient record management (physicians have secure access to up-to-date records), and online healthcare management guidelines.
- Cisco Systems ties its business partners (i.e., suppliers, customers, and strategic alliance partners) together with an impressive web-based knowledge sharing system. For instance, Cisco’s suppliers can tap directly into Cisco’s systems to get real-time access to product logistics and order flow information. Cisco estimates that it has saved over \$500 million annually from web-based information management focused on the supply chain, technical support, software distribution, and other processes.
- More broadly, a joint study by the Economist Intelligence Unit and Booz-Allen & Hamilton found that “*improved knowledge sharing*” is considered to be the most valuable payoff from internally focused Internet, Intranet, and Extranet investments.

Of course the openness and expansive growth of the Internet also creates new risks and a fair number of “*horror stories*” relative to information – its availability, management, misuse, and abuse. Recent attacks on popular web destinations like Yahoo, Amazon, E*Trade, and other sites underscore the risks we have accepted in opening our networks to the Internet. Perhaps more disturbing are the cases of extortion being perpetrated by hackers on companies as small as CD Universe and as large as Visa. Spending on network security is expected to grow to \$13 billion by 2002 (more than double 1997 levels).

STRATEGIC IMPLICATIONS

We believe there are some basic questions our clients and friends need to answer to gain strategic advantages via the Internet. With 2000 widely predicted to be the year business-to-business e-commerce growth accelerates rapidly, now is the time to address these questions and revise your business strategy appropriately.

- **Supply chain configuration** – Where do links in your supply chain need to be strengthened (creating “*eLoyalty*” within the supply chain)? Where are costs essentially wasted (e.g., excess inventories, lead time lags, etc.)?
- **Channel strategies** – What channels are customers (and customers’ customers) using? What are customers’ expectations vis-à-vis alternative channels? How might channels compliment and/or cannibalize each other?
- **Information management** – Where is your organization’s information and knowledge most valuable, most costly, and/or most critical inside and outside the company?

Things the Internet Does Not Change

- ◆ If you sell someone a product, they expect to receive it in a timely manner, in good condition, and fully warranted
- ◆ When a customer has a question or difficulty, someone needs to help them or they will leave (your store or your web site)
- ◆ Physical goods move through real (not virtual) space at a real cost to someone
- ◆ To paraphrase Peter Drucker, “*Profitability is the cost of staying in business over the long term.*”
- ◆ There is no such thing as a free lunch – free PC’s require a three year commitment to an ISP, free ISP’s force intrusive adds onto your browser, and free Internet-based long distance requires all parties to pass through an incredibly tacky web-site (that launches itself every time you log on).

Smock•Sterling Strategic Management Consultants exists to help clients develop and implement strategy. We can help you to address these and related questions. Contact us at (847) 615-8833, jsterling@smocksterling.com.

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