

Under the Buzz

Back to Basics in e-Business

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Under the Buzz is an electronic “viewletter” authored by Philip Lay, managing director at the Chasm Group, a Silicon Valley strategy consulting firm. It is published each month, and delivered free to subscribers via e-mail. It is also posted on the Chasm Group website at: <http://www.chasmgroup.com>. Back issues can be downloaded from the site at: http://www.chasmgroup.com/underthebuzz_archives.htm.

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Editor’s note: Without thus far utilizing any outside e-mail or wire service, we have seen the direct readership of Under the Buzz approach 6,000 since its initial edition several months ago. Needless to say, I am gratified by the overwhelmingly positive response received to date. Besides the many “subscribe” requests we receive every month, it appears that there are legions of readers who continue to receive a copy indirectly - from a colleague, client or other person. If you are one of these people, I encourage you to take a moment to press the url immediately above this paragraph to start receiving your own monthly copy directly. A word of clarification: from time to time we may share our list with other publications that we deem to be credible, though at no time will we charge fees for so doing. As you know, Under the Buzz is published free to all readers and no fees will be charged for mentions or other exposure.

1. Taking a Closer Look at the Benefits of Collaboration

As we have observed in past editions, collaborative applications are gaining attention in the marketplace. In its February 23 issue, Piper Jaffray’s “B2B Analyst” weekly newsletter (www.gotoanalysts.com) went so far as to produce a series of statistics demonstrating that companies involved in collaboration solutions (such as MatrixOne and Agile Software) have experienced significantly stronger performance than Supply Chain and ERP companies. The main performance categories cited were (a) stock price return, (b) revisions in revenue/EPS estimates. In the first category, Collaboration beat out Supply Chain solutions by 24% to 8%, and in the latter revenue/EPS area, the seven Collaboration companies presented a markedly more positive outlook than Supply Chain businesses. The recent slide in the stock market aside, it seems reasonable now to expect great things from applications such as collaborative design, project management, contract management, manufacturing, procurement, logistics, and so on.

Nonetheless, at a time when technology markets are suffering an unprecedented assault on their swagger and self-confidence, I think it’s time to look beneath the covers and try to identify the

compelling benefits that early enterprise customers are discovering in collaborative applications. You never know, if sound evidence is not forthcoming within a short time, the entire category of collaboration could suffer the same halting growth as many earlier product categories – MRP (followed by ERP), Supply Chain optimization, CRM, to name a few – and plunge into the chasm. In case you are unaccustomed to “chasm-speak” (God bless you!), the “chasm” is that yawning abyss that awaits technology products at the end of the Early Market - when a few visionary customers has made their big bets – but before the larger groups of pragmatic or conservative buyers have decided to buy in to the new technology.

Study of Collaborative Application Benefits: “ROI²”

For these reasons, I have decided to investigate the benefits afforded by collaborative applications, by interviewing three main groups of interested parties: vendors, enterprise customers, and their customers or suppliers – in other words, the supposed co-beneficiaries of their investments in collaboration tools. This is a hugely critical point. In conventional business culture, enterprises invest in information technology once they have identified advantages relative to their own business, such as (a) what business problems it solves, (b) its feasibility and (c) the return on investment. With collaborative applications the ramifications are enormous, because it takes two to tango and both dancers should benefit: not only does the primary customer obtain returns from their side of the application, but their suppliers and/or customers will too – thus multiplying the number of beneficiaries and the amount of the benefits achieved.

This is in marked contrast to the old days of EDI, for example, when large organizations such as automotive OEMs – GM, Ford, or Chrysler – were able to force their will on the Tier 0.5 and Tier 1 suppliers in their value chain: invest in EDI systems, or go supply to someone else. Now, the internet enables collaboration and we are in the land of “I won’t do it unless I see the benefits for my organization”. If this pans out, the resulting explosion of business growth should be spectacular. By the same token, if it flops, look out for a new bunch of B2B failures – hardly what the world wants to see these days.

Vendors in the Spotlight

The first companies in my short field survey are Agile (collaborative manufacturing), BlackHog (collaborative direct procurement), and Exterprise/CommerceOne (collaborative contract management). I shall be publishing results of these studies in upcoming editions, and am open to including more companies in the survey, provided that their value propositions (i.e., product offerings) are different from these three – in order to ensure sufficient variety.

Placement in the Technology Adoption Life Cycle

The assumption I am making in this study is that most, if not all, collaboration apps are getting ready to migrate from the early market to the bowling alley – or, in different terms, from custom projects aimed at securing strategic competitive advantage to whole products aimed at enabling larger groups of self-referencing pragmatist customers to fix broken business processes, such as malfunctioning supply chain relationships.

Value Assessment Rationale

In speaking with vendors, enterprise customers, and their suppliers, we shall be looking for answers to questions such as these:

- (a) *Value proposition of the application*: What does the application do, and what general problems does it solve?
- (b) *Primary target customer and their compelling reason to buy*: What job title in what type of organization is funding the solution, and what is the principal driver motivating them to buy the solution?
- (c) *Secondary target customer and their compelling reason to buy*: Who is the co-beneficiary, and what problems does the product solve for them?
- (d) *Whole solution – from all participants’ perspectives*: What are the main components of the complete solution, including core technology, complementary products and complementary services?
- (e) *Key partners required to provide complete solutions*: Examples include systems integrators and consulting firms, plus other software or systems technology vendors.
- (f) *Enterprise sales strategy*: What does the field engagement team look like and how does it operate?
- (g) *Competition avoidance strategy*: What directly competitive point solutions are available, what workarounds exist today that more or less do the job, and how does the new solution bypass these obstacles?

The series of mini case studies will kick off in the next edition of *Under the Buzz*, due out in the first week of May.

2. B2B Exchanges: Total Insanity - or a Step in the Right Direction?

“A vision without an execution plan is nothing but a hallucination”.

- Paraphrase of a statement attributed to Steve Case, Chairman of AOL/Time Warner

“Reasonable men adapt themselves to their environment; unreasonable men try to adapt their environment to themselves. Thus all progress is the result of the efforts of unreasonable men.”

- George Bernard Shaw

Today everyone has their own potted history of internet commerce. During the years following the launch of the web and the browser, events moved at lightning speed toward the promised land of full-blown Internet-based commerce:

- 1) Business-to-consumer organizations sprung up based on the concept of selling consumer products at lower overall cost than was possible through existing retail channels. Among all these sites was one catalyst – eBay – that surprised everyone by creating arguably the “cleanest” business on the entire internet, all based on an auction engine supporting a secondary market trading exchange;
- 2) Inspired by this example, the trickle of pioneers who had been experimenting with trading exchanges – Altra Energy among them – turned into a flood of startups anxious to apply the auction and reverse-auction ideas to hundreds of “vertical” business markets;
- 3) Within months, in early 2000, some large, established enterprises, desperate to get a piece of this incredible action and no longer distracted by the specter of Y2K disruptions, ramped up their PR machines and gave birth to what is now called the industry-sponsored exchange, or consortium;
- 4) Today everyone is speculating about the so-called private exchange, in which individual established companies build their own private “value chain network”, or marketplace.

It’s amazing to think that all of this happened in little over a decade. Nowadays, of course, among all these Internet milestones, it is fashionable to knock online retail as a terminably

unprofitable game (probably true) and slam the B2B exchange idea as no less than an insane hallucination (almost certainly untrue). I find that one of the advantages about being a contrarian is that you get to indulge yourself in pushing back against the trend of current thinking.

Here's my interpretation. Far from being one of the investment calamities of modern business times, the notion of B2B exchanges has provided us with a proof point that instructs us clearly about what will and what won't work in e-business. True, it gained far too much early *investment* traction, in exchange for way too little *market* traction. Thus, when it "failed", you could argue that it created more instability in public stock markets than any other single flop in the past twenty years (not counting the bio-tech failures of the 1980s). However, the real value of this foray into arbitrated e-commerce was that it served as a critical iteration along the way. We all know that innovation requires experimentation – you simply don't get anywhere without trying. Among the many lessons that this experiment has taught us are these: (1) The mystique surrounding complex "business models" was exposed as a dangerous distraction from building a real business based on real value creation; (2) most successful Internet businesses will rely heavily on financial and logistical services, and we learned that the build-out will take a while (surprise, surprise); (3) rather than try to attract buyers and suppliers simultaneously, you have to start by creating pull with one constituency; and so on.

Of course, no one should ever have expected that B2B exchanges would work (a) instantly, nor (b) in every market, as many seemed to assume. As far as we can tell, online exchanges may well be applicable to secondary markets as well as a limited number of primary markets. By secondary markets, I mean markets for "second-hand" products, such stocks on the Nasdaq or the Dow (stocks are second-hand goods, because the IPO market manages the sale of stocks as primary goods), or even eBay itself. And, the primary markets that exchanges seem most suitable for are commodities (such as beef, grains, etc.), as well as markets for surplus, obsolete, or perishable goods. I believe that, provided they can weather the present nuclear winter, many independent net markets will survive, possibly with stronger brick and mortar partnerships, but nevertheless survive.

As for industry consortia, most of them still lack any real mission or sense of true purpose, besides the one they accomplished as soon as they were announced – i.e., to steal some of the thunder and market cap from the B2B upstarts that garnered such extraordinary valuations so early on. Without real purpose, most will surely wilt under the weight of their divided, bureaucratic decision-making, leaving individual corporations to go their own way.

This last and latest iteration – the private value network – is an extremely logical step. Once again, it recognizes the individual enterprise's role as the principal sponsor of new technology innovations for business. Let's not forget that without the experience of B2B exchanges and their ilk we may never have progressed so fast toward the private value chain network.

3. Back to Basics: At Last, Strategy's Back!

The importance of strategy in Internet businesses:

“ By ignoring strategy, many companies have undermined the structure of their industries, hastened competitive convergence, and reduced the likelihood that they or anyone else will gain a competitive advantage. A destructive, zero-sum form of competition has been set in motion that confuses the acquisition of customers with the building of profitability. Worse yet, price has been defined as the sole competitive variable. Instead of emphasizing the Internet's ability to support

convenience, services, specialization, customization, and other forms of value that justify attractive prices, companies have turned competition into a race to the bottom.”

The value of business models:

“The Internet’s destructive lexicon. ... Instead of talking in terms of strategy and competitive advantage, dot-coms and other Internet players talk about “business models”. ... The definition of a business model is murky at best. ... Simply having a business model is an exceedingly low bar to set for building a company. Generating revenue is a far cry from creating economic value.... The business model approach to management becomes an invitation for faulty thinking and self-delusion.”

- Michael Porter – “Strategy and the Internet”, HBR March 2001

Strategy, smatergy! That’s what you heard in the heady days of “first-mover advantage”. Now the dean of competitive strategy has found his voice again. You get the impression from reading Michael Porter’s latest Harvard Business Review article that he has waited for the fuss to die down and is now savoring this opportunity to present a complete set of carefully thought-out arguments in favor of business sanity and reason.

You might expect a strategy consultant like myself to enjoy seeing Porter in action again, especially since, with his customary class and thoroughness, he offers the same criticisms as you have seen in *Under the Buzz* in recent months. In my consulting practice, clients are increasingly focused on finding strategic paths to success, rather than charging ahead on “Internet time”.

In particular, we are seeing startups that currently face the virtual certainty of closing cruel down-rounds – or even “no-rounds” – needing urgently to sharpen their strategies in order to have a chance of securing the next round of funding. A clearer story around the value proposition and go-to-market strategy can help to prevent the down-round from degenerating too far below the previous round. Far from the heady days when general statements about trillion dollar TAMs (Total Available Markets), we are now at the point when investors are once again asking important questions, such as, “Who is your target customer?” and “What critical problem does your product help to solve?” or “What barriers to competitor entry or customer exit can you claim?” Most B2B management teams have either never really found an answer to these questions (except to quote the Forrester Group research numbers), or not ventured out to the marketplace to test their theories out with real target enterprise customers.

What we were referring to as the “bad mood” of the market appears to have turned into a foul mood among investors – especially VC’s, many of whom have now returned with renewed urgency to the habit of doing due diligence again. The trouble is due diligence seems to have turned into due vengeance, as they drive executive teams insane with their insistent questions about market strategy, competitive advantage, and business performance.

My recommendation to companies being “victimized” by their investors during this Purge is to quickly smarten up their go-to-market strategy (relegating the phony market research numbers to the index pages), slim down their pretensions and their organizations, and – above all – get out to the market to meet with potential and actual customers. Too many executives, perhaps not familiar with field marketing and sales activities among enterprise customers, appear over-committed to internal meetings and under-committed to winning customers. These people, by and large, will not survive in their roles, because two things are certain: (1) enterprise customers are back in the driving seat, and (2) it’s tough out there these days, and the smart, aggressive sales-oriented companies will win the race.

4. Internet Hindsight as Seen by Veterans: Mistakes Not to Be Repeated

If you still had any doubts at all that we have just come through several years of unadulterated lunacy, here – courtesy of *eCompany* magazine, in its March 2001 edition – are some bloopers and other quotes from diverse industry figures such as Halsey Minor, Brad Silverberg, George Bell, Henry Blodget, Michael Dell, and Scott McNealy:

Halsey Minor, founder of CNET, on managing an Internet company:

Do you think that managing an Internet company is different from managing a non-Internet one?

I think that over the previous four years there's been no experience in recorded history like managing an Internet company, because you had to maintain the perception of success while simultaneously building a real company underneath the press releases.

Brad Silverberg, founder/CEO of Ignition, on Internet company business plans:

We had one team of entrepreneurs in here pitching us on their business plan, and they made it through the first set of screening questions. We liked what we saw. Then we asked them what their three-year plan was. They gave us a queer look and said, "What, are you kidding? We're IPO'ing in 18 months and then we're doing the next company." We decided to pass. When investors are more committed than the founders are, you know something's wrong.

George Bell, CEO of [Excite@Home](#) on biggest mistakes:

What was your biggest mistake?

Spending money on unmeasured marketing to grow the brand.

Henry Blodget, Merrill Lynch internet analyst, on revenue leverage within the Net economy:

...You had 300 companies go public in a year and a half and each company would raise \$50m. to \$100m., and they would immediately begin buying services from related companies. For example, you would buy professional services from Scient or Viant, you would buy software from Vignette and e.Piphany, hosting services from Exodus, advertising services from Yahoo and AOL, servers from Sun, computers from Dell, and so on. That created incredible performance for a lot of companies but as soon as the capital markets dried up, the revenue disappeared. Because effectively it was IPO money that was effectively converted into revenue.

Michael Dell, founder and CEO of Dell Computer, on the significance of e-business:

In the early days of the Internet, was there anything you thought was really important that turned out not to be? And vice versa?

I think a lot of people initially thought that the "e" in e-business was more important than the "business" part. ... The biggest waste of money has been all the investment in companies with so-called new-economy business models. Business fundamentals haven't changed, and a lot of investors lost sight of that.

Scott McNealy, CEO of Sun Microsystems, on time investment:

What's the single biggest lesson you'd pass on to someone just starting out in this business?

Prepare to dedicate more hours than you planned to the startup. If it is successful, it will consume bazillions of hours. If it is not, ditto.

5. International Operations – Key “Don’ts” and Key “Do’s”

Expanding operations to Europe, Asia, Latin America, or any other region is usually a complicated affair for U.S. based high-tech companies. How so? Well, it all depends on your mental model of what the subsidiary operation needs to look like, what its key objectives are, how it serves the corporate goals, and so on.

Here's how it looks from the point of view of a foreign country outpost. For the right person, the job of country manager is one of the best jobs in the world: you are a player in your local country, perceived as local “president” of a multi-national high-tech company – not too shabby as a corporate assignment. Also, you soon learn that it is vital never to ask permission to do anything of significance; you will only invite micro-management. The trick is to follow your instincts, do what you need to do, then beg forgiveness if something goes wrong. Provided that you take full advantage of the distance separating you from your head office, you stand a good chance to be successful – but you have to perform!

One bugbear is that you have to spend considerable slices of your time explaining to the latest group of visitors from HO how your country, economy and marketplace are “different” from the U.S., and why the parent company's one-size-fits-all marketing approach might not work with your customers. You're being treated like a sales office, but due to cultural issues, complex regulatory requirements, and different market requirements, you have to operate as a company (generally, all major line functions of a software company need to exist in some form – marketing, R&D/product management, sales, support, and professional services). Since your revenue goals are typically just an extension of U.S. sales quotas, no one wants to take account of the ups and downs of the local economy. Usually, there is a controller who is expected to keep an eye on you, rather than a CFO to help you drive the business. And the worst place to be a country manager might just be Canada! For some reason, Americans cannot understand why Canada cannot just behave like a state in the Union, despite the fact that it has a distinct business culture and different government incentives and qualifications regarding high-tech company operations.

So, if you are one of the growing number of U.S. companies that want to do it right and avoid the horrendous problems of having to micro-manage a set of poorly performing, high-maintenance subsidiaries – and there can be some real horror stories! – here are a few “don'ts”, along with their corresponding “do's” (I am using Europe as an example, but many of the same lessons apply to Asia-Pac, or Latin America):

Timing: Don't assume that you need your own subsidiary until at least three major clients have demonstrated their readiness to invest large sums to fund your entry, in order to provide them with necessary product localization and support, and until you are satisfied that the market potential is at least equivalent to the potential in a large U.S. state economy. Until then, use a combination of direct sales from the U.S. and distribution – and *never* grant exclusive rights!

Culture: Don't treat Europe as a single, uniform, "pan-european" clone of the U.S.: in the interests of business - the dominant cultural activity - Americans have invested enormous resources to maximize uniformity and eliminate the element of surprise in main-street America – whereas this is emphatically not the case in Europe. It is imperative to recognize that there are five or six major European economies, plus another twenty or so smaller, but quite distinct ones, where (unlike in the U.S.) social culture still predominates over business culture.

Organizational Model: Don't treat your subsidiary like a U.S. sales office: Avoid making direct comparisons with U.S. territory sales quotas, and hire a strong management team – it's a company that needs to survive on its own merits in the local economy.

Location: Don't assume your European HO needs to be located in the UK: the Brits are still extremely insular with respect to "Europe", as they still tend to refer to the rest of the region. France and Germany also have their peculiarities. Instead, you should seriously consider the Netherlands or Belgium, two countries that are accustomed to being outward-looking and are located close to major markets.

Local Knowledge: Don't be taken in by "plausible" locals who speak excellent English, have studied in the U.S., and smile a lot. Instead, spend time getting to know the marketplace, retain more than one recruiter to form your management team, and stay clear of the "usual suspects" in each country – managers who have a record of moving from one U.S. high-tech company to the next, sometimes for the wrong reasons.

Management Style: Don't lay down the law too much: you are asking for civil disobedience if you don't give your local team space in which to be creative. Europeans have along history of being invaded and easily adopt a stoic "this too shall pass" attitude, finding their own ways to get things done. It's much more effective to hire cautiously, then to give your management reasonable leeway to drive the business the way they see fit.

My final word on this thorny issue is this: if you aren't ready to adopt a different approach than the one caricatured above, consider limiting yourself to using systems integrators and distributors.

In upcoming issues:

- The Five B2C Poster Children: A Year Older and a Lot Less Exciting
- Back to Basics: Where is Your Category in the Technology Adoption Life Cycle?
- Back to Basics: Negotiating the Painful Leap Across the Chasm

Under the Buzz offers a monthly commentary on the business-to-business e-commerce sector. The goal is to provide provocative and accurate insights into the latest events and thinking shaping the rapidly evolving business-to-business marketplace. *Under the Buzz* focuses on strategies for building sustainable competitive differentiation and maximizing market valuations.

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