

Under the Buzz **Back to Basics in e-Business**

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Under the Buzz is an electronic "viewsletter" 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/underthebuzz.htm>. Back issues can be downloaded from the site at: http://www.chasmgroup.com/underthebuzz_archives.htm.

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1. E-Business Conferences: Vendors Sounding Upbeat

After attending *Enterprise Outlook* and *Line56Live!* in San Francisco during the last week of June, I got the impression that people are beginning to come out of their foxholes after several months of suffering the "nuclear winter" that has hit much of the high-tech sector. Not only are vendors and customers venturing out in greater numbers than at earlier conferences this year, but they are dealing with the new reality of building business the old fashioned way. In every keynote, panel session, and company presentation, speakers went out of their way to point out their key customers (even when they only had one or two to mention), to emphasize that they have detailed knowledge of their customers' major reasons for buying, as well as the results they are helping them to achieve. Twelve months ago, the same company presentations tended to provide ethereal statements about business models, then-trendy concepts like "dis-intermediation", and news of strategic alliances.

Line56Live! – June 28-29, San Francisco

At Line56Live!, which was quite upbeat, it seemed that the main thrust was to take the temperature of e-business in the current environment. Speakers and panelists appeared to be in agreement that the lessons to be learned from the dramatic fall in high-tech valuations have been learned and it's time to get going again, this time with both feet on the ground. Hearing attendees speak solemnly today about the solid principles and time-honored practices required to build a sustainable business, it's difficult to believe how many of these individuals are the same people who so recently participated wholeheartedly in the

consensual illusion of the “internet economy” in its initial version. In lighter vein, it’s a bit reminiscent of the turnabout made by many of my fellow baby boomers, who thirty years ago indulged freely in every known sensual experience but, faced with the everyday responsibilities of raising children and pursuing careers in the last twenty years or so, turned into serious citizens – and even at times frightful prudes - whose collective amnesia about the good ol’ days can be hilarious.

Back to the conference agenda: as part of the joint presentation by myself plus two other speakers on the “ROI vs. Strategy Dilemma”, I put forward a thesis that this is more of a “both/and” issue than an “either/or” one. In other words, in an effective, balanced organization (if such a thing exists in high-tech!), I argued that ROI is a metric that tells you whether your strategy is working or not. And, independent of economic conditions, it is important to manage IT investments using both short-term *and* long-term ROI metrics, so that companies don’t lose sight of the end-objectives of their investments. Thus, strategic objectives are best served when they are tied to short-term results that operate as milestones for the bigger goals. Here are three of the main arguments I used to support this thesis:

1. **Seesaw between Infrastructure and Applications:** My colleagues and I at the Chasm Group frequently debate the cyclical “seesaw” that initially favors investments in IT infrastructure (e.g., client-server database and development tools in 1989-93, and e-business platforms and integration from 1998 to early 2001), then switches to a focus on application-oriented investments (client-server ERP from 1993-1997, and e-business apps from 2001 on). I would further suggest that infrastructure-heavy investment coincides with relative boom economies, whereas applications-focused investment coincides with downturns, when every customer is obliged to tie each IT investment to concrete results gained by solving specific, identified business problems.
2. **Different ROI strategies for different conditions** (see 2x2 ROI matrix below): The recent “rediscovery” of the importance of ROI justification has created a false impression that ROI only matters during an economic downturn. I would argue that enterprise customers take ROI seriously *in all economic conditions*, whether or not they actually measure the eventual results carefully – the key difference is in the type of ROI approach used.

ROI Matrix	Soft Benefits	Hard Benefits
Strategic goals	Reshape the industry	Fix broken business process
	Revolutionize business processes	Achieve dramatic efficiencies
Tactical/operational objectives	Increase user productivity	Achieve short-term savings
	Increase customer satisfaction	Increase cross-selling results

Not surprisingly, during boom times there is a high tolerance for soft benefits related to strategic goals (top left quadrant); in contrast, during downturns there is a low tolerance for these soft benefits, in favor of a greater focus on tangible, measurable benefits that are achievable in the short term (bottom right quadrant)! The danger here is that an excessive focus on tactical/operational hard benefits can lead companies to stray from strategic goals aimed at achieving “soft” benefits, such as differentiating themselves against competitors in order to optimize shareholder value. To avoid this risk, it is critical to maintain the link between both strategic and

tactical/operational “hard” benefits: for example, a company can still set its sights on fixing a broken process (top right quadrant) such as customer service by implementing a redesigned process plus technology that may take months to implement fully, while focusing on tactical milestones that result in short-term savings (bottom right quadrant), for example, by outsourcing a specific customer service task, such as hot line support. In fact, I would argue that it is vital to maintain a *correlation between all these components* – soft & hard benefits, and strategic & tactical objectives – in order to keep an organization balanced. This balance will tend to prevent counter-productive flip-flops in IT investment strategy based on passing economic conditions.

3. **In a recession, every customer may look like a pragmatist, but...:** During a downturn every customer is obliged to adopt some of the behavior of a pragmatist – even highly placed executives accustomed to making visionary decisions must set an example when asking employees for the sacrifice of subjecting every IT investment to strict ROI justification. This does not mean, however, that we must all forget about long-term strategic value creation. In fact, risk-oriented customers will still make the odd big bet when they are convinced that the benefits of doing so outweigh the risk of waiting and missing out on the opportunity to be first.

Enterprise Outlook – June 26-27, Burlingame - California

The main theme of this conference, held at the San Francisco Airport Marriott, was *“Building the Connected Business”*, focusing on e-commerce between trading partners. The ninety or so vendor companies presenting their businesses operate mainly in collaborative commerce, supply chain management, procurement, application and process integration, and outsourced IT services. Of the top ten companies voted by conference attendees and a special panel as the most likely to succeed, five were in supply chain management and/or collaborative commerce. These included Comergent (channel management services), DataSweep (manufacturing collaboration) Savi Technology (global logistics management), SeeCommerce and Tillion (supply chain event management and analytics).

As previously noted in June’s edition of Under the Buzz ([June 2001 – Vol 2, Number 6](#)), the panel that I moderated was tasked with addressing the B2B integration theme *“Providing the New Breed of Tools that Connect Trading Partners”*. The four panelists - Mani Chandy, Chief Scientist of iSpheres, Sean Fitts, president & CTO of CrossWeave, Rocky Stewart, CTO for e-Commerce Integration at BEA Systems, and Richard Koo, CTO for Vitria’s principal product suite, BusinessWare, and a last-minute substitute for his colleague Dale Skeens – provided contrasting points of view on the questions we discussed. Nonetheless, here are the conclusions I took away from the panel debate:

1. **Impact of current business climate – need to focus on the customer’s business problem:** As already noted, the current business downturn is forcing customers to focus on IT investments that produce concrete results, preferably in a short timeframe, whereas, previously, it was often sufficient for vendors to compete for a B2Bi contract as part of a customer’s project to build out their e-commerce infrastructure. Today, more than ever before, vendors must build a clear, compelling business case to justify each customer purchase. To achieve this, B2Bi vendors need increasingly to focus on the business problem that their customers are attempting to solve, and the corresponding e-business application that customer is investing in, rather than just focusing on selling their tools and services, as occurred to a certain extent during the past few years. Taking the example of a high-tech manufacturer’s

- need to eliminate its difficulties in meeting rigorous time-to-market objectives and thus achieve its revenue growth goals, the B2Bi vendor may need to find a way to play a critical role in a collaborative product design solution, despite the fact that it does not produce all the technologies required to solve the problem.
2. **New tools vs. existing B2Bi infrastructures:** In order to avoid creating excessive disruption and delay for customer deployments, new B2Bi players – among them iSpheres and CrossWeave – are obliged to provide tools and solutions that leverage customers' existing application integration infrastructure, rather than requiring legacy systems to be uprooted.
 3. **Web services – solution or hype?:** Overall, the panel judged that web services, though highly promising as a future solution for accelerated application deployment, are still an immature technology, due in part to the need for a basic set of services to be developed and field-tested over time in real-life customer implementations, and for consensus standards to establish themselves.
 4. **Importance of application servers:** Although the application server may be a catalyst for web services, different types of B2Bi vendor will need to collaborate to help realize the key objective of enterprise customers, to have one core set of tools available to tie together the myriad existing systems and human processes between one company and its various trading partners.

Finally, in response to a question from the audience about web services, panelist Richard Koo suggested that, based on early indications, the financial services sector may turn out to be a primary early adopter of web services, and RosettaNet stood the best chance of becoming a basic standard on which for major enterprises will base their investment decisions.

Footnote: One of the more refreshing sessions at Enterprise Outlook was a luncheon keynote by Bryan Stolle, co-founder and CEO of Agile Software. More than anything, Stolle's message was that companies can be successful even during severe downturns by concentrating on what they do well (outsourcing everything else), and remaining focused on providing complete solutions to the needs of a specific target market. For example, when asked by a member of the audience when Agile will move out of the high-tech contract manufacturing market, in which it is building a dominant share for collaborative product design/engineering solutions, Stolle shot back: "Why would we? It's a \$5 billion market, and we're not a \$100m-revenue company yet!"

2. The Implications of Poor Governance in High-tech Companies

Anyone who appreciates the comedic style of Dennis Miller can identify with his patented "rants". Well, to borrow his catchphrase, I don't want to get off on a rant here, but has anyone noticed the role of weak or non-existent governance in many high-tech companies – not only among the flimsier internet companies, but among larger and relatively more developed equipment vendors and software companies that should know better. You would think that, with all the MBA diplomas and management experience to be found among members of high-tech boards and executive teams, the governance structure of these organizations would be more carefully thought out and implemented. Unfortunately, you would be naïve to assume such a thing. In a business that is still largely dominated by the testosterone school of management – according to which the concept of effective management is limited to the admittedly complex task of getting a good product to market as fast and aggressively as possible – it is not considered a high priority to pay much attention to "designing" the organization that is most appropriate to the specific line of business, nor to manage it with real thought.

Interestingly, the crisis of confidence in technology valuations following the internet bubble of 1997-2000 provides boards and executive teams with an ideal opportunity to review the basic principles of sound governance and business management from here on. Certainly, Wall Street investment banks such as CSFB are coming under fire for not managing their tricky conflicts of interest during the bubble, and its burst. Of course, they make perfect targets for popular indignation, especially when egged on by an eager press. Having said that, I'm not sure the same is likely to happen regarding company governance – the basic rules and processes that determine how companies are governed, or managed, from the Board of Directors down – in part because the topic seems so uninteresting (or perhaps obscure) to most investors and managers. The trouble is that, in innumerable recent cases, technology companies have experienced dire emergencies – and even gone out of business – because the board has, like Nero, been “fiddling while Rome burned”. So, how can one gain an early insight into the possible existence of poor governance in order to implement necessary measures to avert disaster? Here are a few examples of typical symptoms and possible remedies:

1. Roles of chairman and CEO accumulated by one person: It always amazes me to see how many companies permit this abuse of basic common sense, because in permitting this to happen the company loses a fundamental check and balance. And, even the most conscientious chief executive must find it difficult to manage this situation effectively over time. As everyone knows, a company's board of directors has a fiduciary, moral and functional obligation to shareholders, to ensure that the company is run effectively. From my way of looking at things, if the CEO is also the chairman of the board, they are responsible for selecting or approving new members, setting the Board's agenda and, worst of all, determining the flow of information to the board. In such cases, it doesn't take a rocket scientist to figure out who is most likely to have the greatest influence over the board's decisions. And, this being so, what chances are there that such a board will be able to appraise the CEO's performance objectively, and apply any corrections to the company's direction or management, before a real emergency occurs? Besides the above disadvantages of this concentration of authority, it also leads directly to symptom #2, described below.

Suggested remedy: Quite simply, the company's articles of incorporation should be written to forbid this accumulation of responsibilities. In most cases, if the chairman is not also the CEO, there will be a tendency for the Board to be more evenly composed. Nonetheless, the required composition and specific duties of the board should be clearly defined in the articles, to reflect specific governance roles and responsibilities. Also, auditing firms should be tasked with providing periodic certification that board meetings and decisions occur and are acted on as required in the statutes.

2. Board of directors composed of the CEO's friends and allies: This excess, which can soon become a serious sin, occurs most often as a direct result of point #1. By looking at the list of board members and asking a few questions, it is possible to determine if this situation exists. In such cases, by default the chairman/CEO (and their team) drive the board's agenda, and their fellow board members are reluctant to rock the boat with any serious questions or challenges until eventually they are driven to do so by the extent of the emergency faced by the company. At this point, it is often too late to do any good.

Suggested remedy: Besides the remedy above, CEOs and boards should be educated to understand the value of serving the company's interests by helping to put together the best possible Board of directors, deploying its energies in the most productive manner possible –

and avoiding at all costs the conflict of interests that results from CEOs being placed in a position to drive the board's agenda.

3. Advisory board does nothing of substance: Ten years ago the advisory board was a rarity in high-tech, but today almost every company has at least one. Companies funded by VC firms are among those that generally appoint an advisory board at the outset, in order to attract rapid customer adoption, among other benefits. Usually, however, these boards are not tasked with much more than occasional feedback or putting their rolodexes to work, and in fact many "advisors" are way over-subscribed, some sitting on six or eight boards, besides managing their own full-time businesses.

Suggested remedy: Although advisory boards do not have any duties regarding governance, they can be a very effective group for helping companies to succeed as well as to head off impending crises, because among other duties they can act as facilitators between the board and executive team. It is important to structure the advisory board's activities in such a way as to require frequent meetings to address agendas that force specific actions by each advisor – making sure at the outset that each advisor recognizes that they will be required to actually perform important tasks aimed at enhancing the company's chances of success in the marketplace.

4. Executive team structure reflects an earlier stage of the company's development: In many cases, as the business grows, high-tech management structure lags the company's growth by a couple of years or more. In these cases, founders may be occupying management positions for which they are ill-suited; key managerial roles may also be centralized under one individual for historical rather than logical reasons, resulting in composite responsibilities which at the outset are set up for mediocrity or failure (examples include amalgams of COO & CFO, CEO and chief software architect, VP of sales & marketing, VP of engineering and customer support, and the above-mentioned chairman & CEO). Furthermore, the "team" may not be accustomed to operating as a real unit, especially if - as is commonplace - real decision-making happens only in small groups of two or three executives. This is frequently an indication that the executive team is a team in name only. Another example: a larger group of company officers and director-level managers known internally as "e-staff" meets regularly without ever really making decisions. Over time, managers placed in this predicament quickly becoming disillusioned with their inability to influence effective decision-making, and they eventually become misaligned on strategic issues.

Suggested remedy: The Board should be required to periodically review the company's organizational design and decision-making processes, making sure that some kind of partial redesign or adjustment occurs at least every two years, or at regular "growth intervals" - such as when the company experiences organizational growth of over 50% (possibly measured by number of employees and outsourcing relationships).

5. Tactical behavior predominates over strategic behavior: My observation is that this problem occurs mostly as a direct result of the testosterone school of management, which basically seeks instant gratification for its pet goals. Any high-tech company that describes itself as "sales-driven" or "technology-driven" is likely to be in this boat, because both these orientations serve the interests of the vendor company more than their customers. A word of warning: being sales-driven is frequently associated with being "customer-focused". But, if this is so, how on earth can enterprise customers feel confidence in an organization that is motivated primarily to close new deals, rather than providing service in existing deployments and installations? The product-driven

organization is similarly focused on satisfying its internal needs, preferring to sell its technology without specific regard for the urgent business problems that customers need to solve. In such organizations, there is usually a high sense of tactical urgency (to fulfill their own sales or product objectives) but a low sense of strategic urgency (to really understand what can most benefit customers over time, and what sustainable differentiated value they bring to the table). These organizations are generally characterized by their preoccupation with executing urgent but unimportant tasks, which get confused with urgent and important tasks, and often win out over important but not urgent tasks (per Stephen Covey).

Suggested remedy: The Board must make sure that the executive team understands the difference between being market- or customer-focused, and being sales- or product-driven, and should actively educate executives to indulge in thoughtful decision-making and careful communications, and discourage management behavior that focuses only on satisfying internal needs. In particular, the board should regularly review the company's target market strategy, using a model that begins with precise definitions of target market segments and customers, their compelling reasons to buy, and the whole product solution required to solve the target customer's most critical problem(s).

6. Absence of contingency plans until the emergency hits: This sin is, in my view, unforgivable. Nevertheless, I have personally seen over twenty internet companies spend away their cash while the executive team flails away, adopting RIF after RIF in the hope of turning the tide. In these cases, contingency planning is virtually non-existent, almost as if alternative plans in such a high-failure line of business as high-tech are something to be avoided, based on some ill-founded superstition or assumption of success. How on earth can a self-respecting board of directors stand by and watch as the hopelessly optimistic (or resigned) internet company executive team flounders around trying to recover its poise, after losing 80-90% of its value on the stock market, without any real contingency plan in sight? In these cases, the most frequent last resort is an increasingly dramatic reduction in force, which often serves only to weaken the organization beyond any chance of salvation.

Suggested remedy: Once again, this should be a basic requirement for the board of directors to regularly review. If such plans – like fire drills - are not properly handled, the board is signing up to what amounts to no less than gross mis-governance, as the absence of a plan to save the company before things get out of hand can cause more rapid evaporation of shareholder value than many direct business issues. As evidence of this risk of value erosion, what other reason can there be to explain why so many internet companies are being valued at a severe discount to cash in the bank?

As Dennis Miller says, "Of course this is just my opinion, I could be wrong".

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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