Case 4.1 Webvan

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The Problem

Webvan was an emerging e-grocery company that was established in the late 1990's. There was a lot of excitement for their IPO, or initial public offering, despite Webvan's small amount of sales versus huge amounts losses in the two previous years. The main problem that Webvan faced, however, was that they had an unrealistic, poorly adapted business model, one of the determinates of a firm's performance. According to *Internet Business Models and Strategies: Text and Cases,* "A business model is the method by which a firm builds and uses its resources to offer its customers better value than its competitors and to make money doing so." Webvan was trying to become a successful player in a market that was vastly overestimated by financial forecasts, had plenty of competition, was very expensive, and just very risky from the start. They made these decisions because they wrongfully based their business model on the assumption that a new technology would take care of all the risks for them. For example, In Webvan's business model they mistakenly projected annual revenues of $300 million, which is twenty-five times the annual amount of what a conventional, stand-alone supermarket makes at $12 million. This is a colossal amount compared to what well-established grocery stores were already making, and it should have immediately been clear that these numbers were never going to happen. None of the numbers seemed to have any basis of offering a better value than competitors, and had Webvan been a little more realistic with their projections, their losses may not have seemed so surprising.

Webvan also most likely overestimated the impact that e-commerce would have on the already well-established grocery market and failed to account for how many people actually used the internet at the time, or the bounded rationality of their customers. In his book, *Building the Information Age Organization,* James Cash describes the effects of new technologies on an existing organization or market. Cash states that "technology changes can be incremental or discontinuous. Some incremental technical innovations can be readily absorbed into a firm's

business processes, and others render these processes obsolete.” In this case, the new technology in question, the internet, rendered the processes of the old business model obsolete too quickly, thus causing Webvan’s financial department to overestimate their profits by an incredible margin.

Webvan’s business model should have been more rooted in traditional legacy models while still conservatively adding in elements of new technology, like the internet, if they wanted to compete with pre-established grocery companies like Kroger and Safeway. Lastly, Webvan invested a lot of money in their warehouses and inventory system, and based on their earnings before the IPO, it should have been obvious that they could never hope to make all of their investments back. All these things are symptoms of a business model that has been poorly adapted to fit the internet, and that is why Webvan’s business model lies at the heart of their problem.

Industry Competitive Analysis

Mission Statement

The mission of Webvan is that they are an e-grocery service provider in the grocery market that provides ordering and delivery services to consumers that owned a home and needed groceries. They operated with a differentiation strategy.

Organizational Structure

Not much is said about Webvan’s organizational structure, but it can be assumed that they are a functional organization. According to cash, a functional organization is one that is grouped by function, and as the organization grows, main functions may be sub-divided and new functions may be added. There isn’t much in terms of leadership, and many IT firms, like Webvan, are functional organizations as well. Webvan is also likely to be divided up into different functions, such as finance, marketing, or sales, and that is why I believe they are a functional organization.

Business Model

Webvan is definitely a value shop. They provide different products that satisfy the needs of different customers. They also provide the customers with a shipping service to get their products to them. Finally, Webvan is not a manufacturer. Those are all reasons why they are a value shop and not a value chain.

Generic Strategy

The generic strategy of Webvan is differentiation because they offer multiple products to many different customers on an economy of scope, which means that they provided their services in a way that they could be sold anywhere in the world. They also associate specific customer needs with a specific product or service.

Analysis of Porter's Five Forces

1. **Intra-Industry Competition**: **High Risk** because the grocery industry already contains many competitors
2. **Threat of new entrants**: **High Risk** because e-grocery is a new industry and there aren't many barriers to entry
3. **Customers**: **High Risk** because Webvan's customers have high bargaining power. They can switch over to different grocers at any time they want
4. **Suppliers: High Risk** because Webvan's suppliers can just supply to their competition instead. Competitors within the market are all trying to get the same supplies
5. **Threat of Substitutes**: **High Risk** because there is a lot of competition in the grocery market that customers can easily switch over to

Stakeholders

The stakeholders involved in this case are:

- Louis Borders
- Webvan Shareholders/Investors
- Webvan Customers
- Traditional grocery stores

The Webvan investors are a stakeholder because they are the ones the are backing the entire company, and the customers are a stakeholder because they are the ones who receive Webvan's services. If the services are worth it, the customers will use it, and if the services are not, the customers won't waste their time with them. Borders is a stakeholder because he contributes to shaping the direction that the company is going to move in. He was also one of the people pushing Webvan's broken business model. Finally, traditional grocery stores are a stakeholder because Webvan's success, or failure, affects their position in the market. If Webvan is a huge success and buying groceries over the internet became as big as Borders claimed it would, the traditional stores would have been in trouble. The opposite is also true. If Webvan fails, then the traditional grocery stores are going to be just fine. Those are the stakeholders in this case.

Alternatives

The alternative solutions to the problem presented in this case are to:

- Do Nothing
- Webvan works together with traditional grocery stores to deliver groceries
- Webvan tries to come up with a more innovative service
- Webvan leaves the market because it's too risky

1. **Do Nothing**

The first alternative solution for Webvan in this case is to do nothing. In this scenario, Webvan continues to operate with their flawed business model, and eventually is fails due to not having enough customers. There aren't very many pros to this scenario except for the fact that Webvan might have learned a thing or to about the bounded rationality of customers, and to never overestimate the effects of a technology when it is still new. The cons, however, are very abundant if Webvan were to choose this solution. They would lose out on all the money that investors had poured into the company because not as many people used the internet as they thought. Webvan's financial forecast were always going to be off, and the company would learn this the hard way, by losing money. If they continued to do nothing, eventually, Webvan would be unable to survive in a heavily populated and well-established market and go on to fail in the future.

This solution affects the investors because they will never be able to capitalize on the investments that they made through Webvan, and they most likely will not be happy. Borders also stands to lose a lot since he seems to be heavily invested into Webvan. The customers of Webvan will lose a service that they had been using for a time and will likely have to switch to a different service provider. The traditional grocery stores are the only ones to profit from this solution because if Webvan fails, they gain an advantage over their competition, and it will have been proven that online groceries are still a way off. That's the do-nothing solution and how it affects the stakeholders in this case.

2. **Webvan teams up with a traditional grocery store**

If Webvan were to team up with a traditional grocery store, and only offer delivery services, they may stand a better chance at securing their spot within the highly competitive market. This solution is the embodiment of the old saying "if you can't beat 'em, join 'em." Traditional grocery stores were already very well-stablished in the grocery market, and e-grocery websites were still

new, but even still businesses in this industry competed with each other. To have a fighting chance, it seems necessary for Webvan to team up with the traditional stores, and they could use the internet to do just that.

For well-established markets like the grocery industry, the internet is a tool to enhance a business model that has already been perfected or is at least nearly perfect. According to *Internet Business Models and Strategies: Text and Cases* by Afuah and Tucci, the internet has" a profound impact on the 5-Cs of coordination, commerce, community, content, and communications, and nearly every firm's activities rest on some subset of the 5-Cs." If Webvan were to team up with Kroger or Safeway, they could use the internet in a way that enhances the commerce, coordination, communications, and content of the stores by offering their services as an extension of the traditional store. The pros of this solution are that many more customers could potentially be exposed to Webvan's services if they received information about it through the medium that they were already accustomed to. This would ultimately lead to more customers and it would help give Webvan an actual chance to meet realistic forecasts for revenues.

The cons of this solution are that Webvan now has to give up some of its market share to the traditional stores because they teamed up. If Webvan were to go with this solution, the investors would at least be working towards making some of their money back, and the customers receive a great service to compliment the traditional stores that they have already put their trust into. Borders will most likely have to accept the fact that he and his financial division had overestimated the value of e-groceries, but at least the company will still be making some profit. The traditional stores come out on top no matter what because they benefit if Webvan fails, and from the team-up. That is the team up solution.

3. Webvan tries to come up with a new, innovative service

In this solution, Webvan doubles down on new technology and develops even more cutting-edge technologies in e-grocery. An example of this could be a software application that allows customers to submit requests for a specialty catalog, or something along those lines. Either way, Webvan ignores all the risks associated with investing in untested technology and charges ahead to differentiate themselves from their competition.

From here, one of two things can happen. Webvan will create a product that is so well liked that it explodes, and customers can't get enough, or it fails and proves that Webvan should stop investing in new technologies. The new technology could give Webvan a competitive advantage, or the ability to perform better than its rivals in the long term (Afuah and Tucci), over their competition, but it could also be weakened by that same technology. The technology is a double-edged sword. The investors may or may not get their money's worth, and the customer may or may not receive a decent product or service. Borders might still be satisfied, since he seems like an advocate for new technologies, but he could still be let down if Webvan fails. The traditional stores would be weakened if the new technology succeeded and would be strengthened if the new technology failed. That is the new technology solution.

The failure or success of the new technology is determined by two things, imitability and complementary assets. According to Afuah and Tucci, "Imitability is the extent to which the technology can be copied, substituted, or leapfrogged by competitors, and complementary assets are all other capabilities, apart from those that underpin the technology or invention, that the firm needs to exploit the technology." If the new technology is highly imitable, then Webvan is not likely to gain much of an advantage over its competition. If it is unique, then Webvan's competitors will be less likely to copy it simply because it's harder to do so. The technology is made unique by complementary assets, like branding or manufacturing techniques. Both of these concepts directly contribute to the success or failure of the technology and are the reason

that it's unknown whether or not Webvan can realistically create a new technology and thrive in the market.

4. **Webvan leaves the market**

In this solution, Webvan realizes the error of their ways and sees that the market is too risky to continue to be in. They pull out and pursue different opportunities. This does not really solve the problem of the Webvan's poor business model, but it does save them a lot of time, money, and heartache. Not much else can be said about this solution except that the investors, customer, and Borders will all be unhappy because they lose money and a convenient service. The traditional grocery stores are positively affected because they gain Webvan's market share.

My Solution

The correct solution for Webvan to choose in this case is to team up with an existing traditional grocery chain to ensure their survival in the market. As stated earlier, some new technologies can be discontinuous and have little to no early adopters at first. It is safer for Webvan to team up with a traditional store because it eliminates some of the risks. The threat of new entrants, customers, and suppliers all change to a low risk when Webvan teams up with an established chain. There will be the added barrier of having to team up o survive, so new entrants do not pose as much of a threat, customers already shop at these stores in the first place, so the only threat that exists from them now is that they may just ignore your services, and the store will handle the gathering of supplies, so Webvan no longer has to worry about suppliers.

The one problem that Webvan faces in a team up, however, is that they now must negotiate with the traditional stores, and the stores are going to have a lot more bargaining power. Webvan also loses market share to all of its competition. If you compare the other alternative solutions to this one, though, teaming up is the best solution. The do-nothing solution only ensures that Webvan fails to fix their business model, and that all of the stakeholders except for

the traditional stores are negatively affected. Creating a new, innovative technology has its merits, but it also adds more risks. It can't be determined whether the technology will be successful or not, so it's best for Webvan to avoid this solution. Finally, Webvan could leave the market, but that's just giving up, and it doesn't really solve their problem. That's why teaming up with a traditional store is the best solution.

Conclusion

This case study involves Webvan, an e-grocery service provider, that is facing the problem of a poorly adapted business model. This cases study explores solutions to Webvan's problem and presents the best one. The alternative solutions are to do nothing, team up with a traditional grocery store, develop an all-new technology, and to leave the market entirely. The best solution is to team up with a traditional store because it involves the least amount of risks while providing the greatest potential for reward. That is Webvan's problem, the alternative solutions to solve the problem, the best solution, and why Webvan should have pursued this solution.