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CIS 410-50 MGMT OF INFO SYSTEMS

Webvan Case Analysis

October 23, 2021

Introduction

Webvan is an early pioneer of online grocery shopping and delivery service; in the two years following its inception, Webvan managed to amass a subscriber base of over 10,000 customers, and, after listing its IPO (initial public offering), rose to a total market value of over $8 billion (Afuah). Webvan's mission is to "build the Last Mile to the consumer", or provide an easy and fast process for customers to order groceries online and have them delivered within a 30-minute window, at a relatively low cost. The company is spearheaded by chairman Louis Borders, who with his brother Tom, co-founded the famous Borders Books in 1971. At 48, Borders has decided to jump into an exciting new venture and enter into the niche and risky business of grocery delivery.

Generic Strategy

Webvan has already achieved a considerable competitive advantage because of their high valuation, and their strong period of growth over the course of just two years, but their generic strategy will be worlds more important in the long run. The generic strategy of an organization is two-fold: strategic scope, where the organization analyzes its demand-side dimension, and strategic strength, where the organization evaluates its core competency, or strength, within the supply-side dimension. There are three types of generic strategies: Segmentation strategy, differentiation strategy, and cost leadership. Webvan utilizes a segmentation strategy because, on the demand-side, Webvan operates within a Narrow Market Scope, which is the niche grocery delivery market, and operates within a uniqueness competency on the supply-side, meaning those who value the grocery delivery business will not find too many other organizations doing the same thing (Tanwar).

Five Forces Analysis

As risky as it is entering such a niche business, Webvan, thanks in-part to the leadership and experience of Louis Borders, has managed to perform well in the market. In just two years, they managed to build an empire of 10,000 customers, while it too over a decade for their greatest competitor, Peapod.com, to garner 100,000. This means that it is entirely probable that Webvan will either continue to compete well with Peapod.com, or even steamroll the competition entirely. However, because there are so many more competitors, like Streamline.com, Shoplink.com, Netgrocer.com, and others, and because Peopod.com and others could react to Webvan's growth and continue to innovate and grow just as Webvan has, and arguably have a comparable ability to do so, the risk of Competitive Rivalry is mid to high for Webvan (Porter's).

The grocery business is tough; the traditional, offline grocery industry's standard operating margins float around 4 percent, which is low. However, Louis Borders estimated that Webvan could achieve 12 percent operating margins. If this turned out to be doable, it would make this niche market relatively lucrative. Juxtapose that with the exponentially growing popularity and adoption of the internet and ecommerce, and you have yourself a significant Threat of New Entrants. Because this market is not government created, does not involve patents or proprietary knowledge, precludes no asset specificity (these are groceries and delivery trucks we're talking about), there are very few barriers to entry. The only barrier is economies of scale;

a business that manages to scale the fastest in this market will shun any new entrants. Until that business is Webvan, the Threat of New Entrants is high (Porter's).

The Threat of Substitutes for Webvan is low because the target audience of the service being provided by Webvan is the market where demand for convenient grocery delivery and a willingness to pay the premium associated exists. This service cannot be emulated in a vastly different way, but it can be scaled and improved. However, the Bargaining Power of Suppliers is moderately high for Webvan, because Webvan allows for a grocery business that can double or even triple the margins of traditional groceries, and suppliers may want to get a cut of that, and possible squeeze Webvan's margins. Webvan's suppliers and the grocers in the surrounding area could create their own grocery delivery services and could potentially offer the same services at a comparable or lower price, stealing Webvan's customers. Webvan would only face one significant risk for the Bargaining Power of Customers – where the overwhelming majority, if not all sales, would be made up of customer purchases, and since this is likely the case for all Webvan's competitors, the risk of the Bargaining Power of Customers is low (Porter's).

The Organizational Value

The organizational value of an organization is a critical component of its valuation. The three types of organizations are value chain, value shop, and value network. Value chain is where an organization's primary output is a product or product in the form of a service, like SaaS, or Software as a Service. Value shop is where an organization produces solutions rather than products, and these solutions involve the use of human capital, like LegalZoom. Lastly, value network is when a network brings together individuals and organizations to conduct business with each other, like Zoom or LinkedIn. Webvan is a value shop because it offers a service that has perceived value to that of their customers. In Webvan's value shop, their product is the grocery delivery service, and the customers who purchase this service place enough value on their time that they are willing to pay a monetary premium for a service they could otherwise do themselves (Harris).

The Organizational Structure

George Shaheen is in the Chief Executive Officer position. In 1999, Webvan signed a $1 billion dollar agreement with Bechtel Group to build distribution centers and the infrastructure needed to make deliveries in the 26 prospective markets over the course of two years (Afuah). Webvan differentiated itself against market by separating its business into two distinct units: customer service and operations. Operations would deal with the day-to-day tasks required to keep the business running. Operations also incudes the software developers who created the necessary, proprietary systems that would automate, link, and track every moving part of the grocery ordering and delivering process. Customer service involved the Webvan “ambassadors” who would be responsible for making the deliveries.

The Problem

According to the Theory of Constraints, the primary theory from *The Goal*, a work by award-winning author Eliyahu Goldratt, Webvan needs to first identify its bottleneck, which is its constraint, in order to continue to grow and operate effectively and profitably (Goldratt). Webvan’s bottleneck, and business impediment, is its margins, or more specifically, its costs. From 1999 to 2001, Webvan maintained particularly high operational costs, and lackluster sales. Webvan was predicted to achieve $518 million in sales in 2001, but would total out to $302 million in overall loss; not to mention, these sales would only account for less than one percent of all grocery market sales (Afuah). Webvan needs to increase sales and decrease costs.

The Stakeholders

Webvan's stakeholders are its customers, its customer service employees, its operations employees, and its shareholders. The customers are those who elected to pay Webvan a premium to retain their valuable time if they are busy. The customer service employees are those who procure the customer service department of Webvan and make the deliveries. For the other half of the business, the operations employees are those who warehouse stock and ensure that the business ran smoothly, and orders were being made, picked, and delivered in a timely manner. Every stakeholder is counting on Webvan's ability to utilize its rapidly growing value shop in a way that ensures its continuity. The shareholders who helped Webvan reach a valuation of over $8 billion after the IPO. The stakeholders will all be negatively affected if Webvan fails to arm itself against its risks from Competitive Rivalry, Threat of New Entrants, and the Bargaining Power of Suppliers. The stakeholders will also be negatively affected if Webvan cannot cut its costs and improve its margins and sales. Let us go over some alternative solutions.

Alternative One: Do Nothing

The first alternative for Webvan is to do nothing. This is a viable alternative because the company continues to grow and continues to increase its constituency and loyalty. Initially, the grocery delivery industry was expected to only capture an insignificant portion of the total grocery market for the first two years since Webvan's 1999 inception. However, this began to change, as competition and demand started to ramp up; Kroger and Safeway, big names in the grocery business, were even piloting their own grocery delivery services. As these events unfolded, more ambitious projections began to rise to the surface, and these new projections were showing a forecast of 20% of all grocery orders being online within five years (Afuah). Webvan has bared its teeth in this emerging market and has the potential to be its face.

Alternative Two: Decrease Costs and Encourage more Spending

Another alternative is to cut costs and encourage higher order totals. Webvan was averaging an order total of $71, which was considerably below the target order total of $101, which was necessary to attain in order to reach revenue goals by distribution center. Webvan's operating costs are too high; they need to be decreased substantially, this could come in the form of cutting ties with distribution centers that are too far away or are situated in locations with particularly low demand, etc. Webvan also needs to incentivize spending more per order. Great incentive programs would lead customers to spend more and drive revenues, increasing profitably juxtaposed with cut costs.

Alternative Three

The third alternative is for Webvan to open itself up to being acquired. This is a viable option because the company would be better poised to tackle operating costs and garnering more sales from being acquired by an already well-established and recognizable company. As mentioned in the case documents, the margin structures involved with the grocery industry were already razor thin, and it was reported that many of these costs were incurred by developing brand recognition. The parent company would not need to incur these costs and would even be able to throw their already competitive pricing into the mix. On top of that, this alternative would likely pose the least amount of risk to the greatest number of stakeholders, mainly the employees and the customers. For the employees, their jobs likely would either not change at all or just change slightly, and for the customers, the service would likely remain the same, and perhaps at an even lower price and faster delivery. The company would be sold, and the higher ups would profit handsomely, so it is in their interest as well.

Executive Summary

Webvan's mission is to "build the Last Mile to the consumer", or provide an easy and fast process for customers to order groceries online and have them delivered within a 30-minute window, at a relatively low cost. Webvan faces a moderate to high risk of Competitive Rivalry, the Threat of New Entrants, and the Bargaining Power of Suppliers. Webvan operates within a narrow market scope and a uniqueness competency, so they therefore employ a segmentation strategy, a strategy they will need to utilize effectively to arm themselves against their risks and challenges. Webvan's organization value is a value shop because their primary output is a product in the form of a service, grocery delivery. Webvan's stakeholders are its customers, its employees (on the customer service side and the operations side), and its shareholders, all of whom are dependent on Webvan's abilities to stay ahead of the competition and continue to employ its strategies effectively and profitably.

I recommend that Webvan go with Alternative Two, or cutting costs and encouraging more sales. I recommend this course of action because Webvan has experienced strong growth, a great valuation, and has the potential to encourage more sales by offering customer incentives. Webvan could achieve this by implementing a rewards program, perhaps with gasoline points, offering a wider variety of products like household cleaners, non-prescription drugs, or even automotive goods like polish and motor oil. This would also allow for Webvan to diversify and compete with the rise of supermarkets (imagine a busy parent not having to go to Kroger, Target, *and* AutoZone, and instead getting all he or she needs in a jiffy). It was reported that the most goods ordered for delivery were perishables (Afuah); Webvan should be showing its customers why they should be adding that box of Cheez-its and jug of Pennzoil, too. As Webvan's distribution and delivery innovates and improves, and as Webvan continues to grow in shareholder equity and brand recognition, costs will decline, and Webvan will have the ability to offer even better services at an even better price, sticking it to the competition.

I did not recommend the first alternative, doing nothing, because Webvan's critical bottleneck is its costs, and if they do not cut these costs, increase sales, or all the above, they will eventually stretch themselves thin. Not to mention, they are now a public company; everything Webvan does going forward will be under a microscope, and doing nothing would be everything a would-be investor needs to see. An investor would only need to peruse the year-over-year balance sheet to see that costs and sales are not improving and wonder why nothing is being done about it. I also did not recommend that third alternative, taking a buyer, because even though this would arguably be a viable decision, this company has become more than just a startup. They successfully launched an IPO and achieved a massive valuation. The momentum is already there, and Webvan needs to use it or lose it. On top of that, there is absolutely no guarantee that the parent company does any better (they could do worse). Webvan cannot effectively utilize its assets and strategies to achieve its mission because a major bottleneck in the form of too-high costs. Webvan needs to cut these costs for the sake of its stakeholders, continuity, and profitability, in that order.

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