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Case 4: Webvan

Webvan was formed in the mid-1990s as an ambitious project headed by chairman Louis Borders, CEO of the already successful Borders bookstore. The aim of Webvan was to intercept a segment of the grocery industry by offering a service in which customers could place an order online and have the groceries they needed delivered directly to their door. By using a logistics chain consisting of custom-built warehouses and distribution centers, Webvan wanted to maximize convenience by making deliveries as soon as possible. However, Webvan was poised to face many issues. The dotcom boom brought on a multitude of competitors who attacked the same market with varying degrees of success. Even with growing intra-industry competition, the online grocery market had only gained roughly 1 percent of the total grocery market share by the turn of the century. Even with slow-growing but promising growth in customer base and infrastructure, Webvan was facing major obstacles. With many people set in their ways with their knowledge of how to grocery shop, and many who had little or no experience with online shopping, customer acquisition costs, or CAC, which “generally refers to sales and marketing costs that are incurred in the process of acquiring a customer,” (Olenski) are very high. This, combined with Webvan’s quickly apparent overvaluation, made investors as well as key Webvan personnel worried that the current burn in capital wouldn’t see the payoffs that were originally forecasted for the company. So, what can be done to get Webvan out of the hole that it has quickly dug itself into?

Webvan expanded aggressively by planting infrastructure and expanding the reach of their logistics chain, as a result, they were quickly burning through capital. However, they lacked the customer base to lessen the margins on losses. In a nutshell, Webvan needs to find a way to get customers quick if they wish to continue their operations, or at least, their aggressive expansion. If they fail to accrue a meaningful customer base soon, they will likely fail. The Complementary Asset Model can be applied to Webvan's situation, which describes the possibilities which the company can pursue (Run, block, team up). Before explaining further which alternative Webvan should pursue, we must first analyze the business and the environment that it resides in. To do this, we will look at Porter's five forces (Porter).

First, we'll begin with the suppliers for Webvan. In the grocery industry, food and home products come from a variety of different places. With most foods, the suppliers will operate on a low-cost basis, so they don't have a ton of bargaining power over Webvan, who can easily shop around for suppliers of specific home products. Webvan must be able to offer a service in which food prices are competitive, or even more affordable, than traditional grocery stores. In fact "Americans spent just over 10% of their disposable income on food in 2003. This amount equals the lowest level recorded since 1929, and is well below the peak level of 25.2% experienced in 1933." (Miller) Americans just aren't spending as much money on food as in the past compared to their income level especially on commodity foods. If Webvan sticks to common commodity foods, their suppliers don't have a ton of power over them because their model itself is built on being able to supply it at the lowest cost.

Next, we'll look at the intra-industry competition that Webvan faces. There are quite a few competitors mentioned in the case. Competitors that are significantly larger than Webvan from a customer base perspective have an advantage over them currently due to how difficult it is to convert customers in this space to a somewhat foreign seeming idea of buying groceries online. The case mentions that one competitor has spent 10 years acquiring one hundred thousand customers, there's probably a reason for that. Webvan has large amount of capital to take over as the leader in the online space, but not the customers yet. Other competitors employ differing "gimmicks" in their business model, such as one business who delivers to a locker that is accessible from the customer's garage. These competitive gimmicks may hurt or help grow these fledgling companies depending on how well the market receives them.

Third, we'll look at the threat of new entrants. With the capital that Webvan needs to engage with their market, they keep some power over this force. However, the software side is easy and doesn't cost a lot of money to replicate. This creates a gap in security as far as their market share goes strictly on the software side. To counter this, Webvan has built a massive distribution center that cannot be replicated by just anyone. This environmental threat will continue to exist as long as they're an internet-based company (especially during the height of the dotcom boom), but they can continue counter it with physical infrastructure.

Fourth, we'll look at the customers. This is likely Webvan's greatest threat. Customers have a variety of options when it comes to grocery shopping. With the high potential switching costs of learning to use an online shopping model, adjusting to a delivery schedule, and potentially paying premiums to have the groceries delivered, many will be reluctant or unwilling to switch. Customers hold a huge amount of bargaining power over Webvan.

The last force we must look at is the threat of substitutes. The substitute here are traditional brick and mortar grocery stores. They already have the customers, they already have a working business model and have many years of success and trust. Webvan is trying to undercut these businesses and take their customers but will not do so unless they can attract new customers and prove that their model supports both scalability and sustainability.

Now that we understand Webvan as a company and the environment that they reside in, we need to discuss the decisions that are plausible for Webvan as a company to make going forward. I will define to three most plausible alternatives, define the main stakeholders involved in the decision, and lastly, how the decision will affect them and why it’s the correct or wrong choice.

Stakeholders are people that are impacted by changes in an organization. The main stakeholders I will reference are the customers who Peter Drucker describes as the most important stakeholders (Drucker), investors, and corporate employees. These stakeholders are the ones that are most heavily affected by any major decision in the company. These are the people that should be taken into account when deciding any major decision crisis.

The first decision would be to simply do nothing and continue to operate as they currently have been. They will continue struggling to accrue a meaningful market share. Given the losses that Webvan has already endured, this isn’t fiscally possible. The company will hemorrhage capital until it finally goes bankrupt. Corporate employees would not be happy due to the grievous losses and the high cost of acquiring customers making recovery difficult. Investors’ capital will be burned. Current customers would soon be forced to return to traditional shopping or to using another delivery service, if one is still available. To do nothing would essentially be the death of Webvan.

The next decision would be to attempt to be bought out by one of the larger companies as a subsidiary to their company. This will no doubt fix most of the customer acquisition problems, and would allow for an integration with an existing logistics chain that will likely be exponentially larger than what Webvan could build on its own. This will allow for the already stable brick and mortar stores to acquire a possible would-be competitor, allow them to offer a new service, and will allow Webvan to inherit a larger customer base. Corporate employees will likely have mixed feelings. Webvan will continue to operate, but ownership of the company is gone, and key personnel could potentially be replaced, and jobs could be lost. Investors will again be mixed because Webvan may continue to grow but their stock will likely be bought out by the acquiring company, which may or may not create gains for investors. Customers will be happy because they will continue being able to order online and most likely will see a larger selection when you combine the warehouse model they built already with a large store chain. This alternative isn't ideal, but it would allow for Webvan to continue its operation.

The final decision would be to team up with other online distributors. As previously stated, the customer acquisition problem is the largest problem any of these online grocery stores are facing. It is very difficult to encourage customers to retrain themselves to shop differently than they've done their whole lives. In fact, "change generally is harder as we age because we become more comfortable and familiar in our lives" (Grohol). Being bought by a brick and mortar store doesn't guarantee customers will try their service, even with the added peace of mind of being backed by a company that they already know and trust. Teaming up with intra-industry online grocery competitors will allow these companies to absorb multiple markets that have switched over customers and combine them to one customer base. Webvan has generous capital and rapid expansion, and even then, it still struggles. It is likely that most companies in this market are feeling the same growing pains. This means that teaming up could cheap and lucrative for Webvan right now. Customers will be happier due to the combined great features of both companies. Corporate will continue to operate and retain ownership of the company. Investors will be happy because they will see Webvan continue to grow and reap returns.

It seems clear to me that if Webvan wishes to succeed, their best option is to accept a buyout from a major retailer such as Kroger or Walmart. These other online delivery companies are struggling just as much as Webvan, and I don't think that teaming up will provide enough mutual benefit to keep the companies afloat. A buyout and subsequent integration with a larger, established retailer would give Webvan a massive competitive advantage in the form of an expanded logistics chain, exponentially larger (and loyal) customer base, and it would provide Webvan the capital it needs to expand and improve its service in the long-term, as more and more people turn to internet-enabled businesses to serve their needs in the 21st century.

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