Shivani Patel

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Dr. Barker

Case 4 - Webvan

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**Introduction**

Webvan is an internet-based company that combined online grocery shopping with home delivery. On November 5, 1999, Webvan completed its much anticipated initial public offering (IPO) and made headlines across the business world. Despite tiny sales and big losses to date, shares of the two-year-old company, which company, which combine Internet grocery shopping with home delivery, shot to an 80 percent premium on its first day of trading. At the end of its first day as a publicly traded company, Webvan had a total market value of more than $8 billion, nearly half the capitalization of grocery industry leaders like Safeway. Inc., Kroger Co.

Webvan was found by Louis Borders, who also founded borders books. Borders were confident that Webvan could prevail over its existing online competitors by expanding aggressively. In the internet economy, Borders argued that first-to-scale, not first-to-scale, counted. While Webvan had operated for a mere five months in the San Francisco area, more than 10k people had signed up for the service. This is not bad considering that it had taken its rival Peapod, Inc., 10 years to amass a customer base of 100,000 households. Webvan’s 1999 sales were expected to amount to $11.9 million while its losses would amount $35 million.

**Problem**

The online grocery industry was emerging slowly, however, there were already existing well-established grocers. Peapod was number one in this industry, with an already existing base of customers. Although there were high hopes for Webvan’s profits, the first year the company was forecasted to have losses exceeding $35 million. Webvan needs to break into the online grocery industry and gain a customer following where customers will continuously look to Webvan for their grocery needs. Given that the industry is new, and the market is somewhat unwilling to try online grocery stores, Webvan needs to think of an innovative way of attracting customers to shop online instead of in stores.

**Industry Competitive Analysis (ICA)**

**Generic Strategy**

Webvan’s generic strategy is **differentiation** because they focused on two main areas: operations and customer service. “Differentiation is aimed at the broad market that involves the creation of a product or services that is perceived throughout its industry as unique.” (Porter) Pickers were the employees that saw the orders and then collected the items. They never had to walk more than 20 feet in any directions to get an item. Customers were able to receive their orders the next day and were even able to specify within a 30-minute time frame when they would like the order to be delivered. Webvan offered 50,000 products to their customers when their competitor only offered 30,000 products. Deliveries could be attended or unattended, which mean that the customer could either be home to receive the order or the Webvan associate could drop off the order while the customer was away from home. Webvan's market position as the quality-driven gourmet online grocer with everyday grocery prices was an attempt to differentiate itself from competitors. “Information technology is so woven into the fabric of the firm that it not only must be responsive to the strategic directions of the company but must be considered as an influence on those strategic directions.” (Fried)

**Organizational Structure**

Webvan’s organizational structure is **functional** because common activates are grouped together. For example, food that is liable to spoil have to be monitored to make sure that they do not go bad and frozen or cold food stay cold until the customer receives the product(s).“…An organization’s performance is dependent on all functions working together in a coordinated manner, the functional structure requires extensive information exchange among functions.” (Cash)

**Mission**

The mission of Webvan is to be the lead online grocery store, providing efficient services with a vast range of options, fast delivery, and superior customer service.

Webvan wanted to create a new and improved e-grocery industry. In order to attract customers away from the existing brick and mortar grocery industry, Webvan would have to provide improved “speed of service, convenience, personalization, and price” (Kalakota).

**Porter’s five forces:**

When analyzing Webvan's competitive environment it’s helpful to consider the five competitive forces described by Harvard Business School professor Michael Porter.

1. **Competitive Rivalry:** Rivalry would be **high** because of the constant threat of new entrants and the constant competition for new customers. There are a lot of other online grocery stores. Some of these stores are doing exactly the same thing as they are, some have minor changes like processes or the products, and others are going completely in the other direction like having small refrigerators at their customer's houses that they can drop off food at.
2. **Threat of new entrants:** The threat of the new entrants is extremely high because you can buy food anywhere. In this case, the competition is not just the grocery store, but it can also be gas stations, fast food, etc. There are a large number of new companies that are emerging onto the scene that are all trying to do the same thing. Since there are so many companies doing the same thing, it is important that Webvan differentiates themselves from their competitors to give consumers a reason to use Webvan for their online grocery shopping.
3. **Threat of substitutes:** The threat of substitutes is also very high because consumers can shop around at numerous amount of brick and mortar grocery stores, at online grocery competitors, etc. With brick and mortar grocery stores doing a significant amount of business than online grocery stores already, they play a huge role in the threat of substitutes. Another substitute would be farmers markets and local family run brick and mortar stores.
4. **Bargaining power of suppliers:** Supplier power is low because there are many sources of food and produce that Webvan needs in order to achieve their goals.
5. **Bargaining power of customers**:  
    Customers have low buying power when the number of customers is large in comparison to the number of competitors serving them. (Porter). If we only consider online competition, then this was the case for Webvan’s customers because the industry was relatively new and while there were new entrants to the market there were not yet a lot of competitors for them to switch to. However, in this case, we also have to consider traditional grocery stores as competitors. Switching costs would be very low because there are many other places to buy groceries.

**Internet Enabled Business Model:**

* **Profit Site:** The profit site is when an organization does better than its competition. In this case, the profit site would be the focus on operations as well as customer service. Webvan hoped to compete with the traditional brick-and-mortar grocery stores as well as its other online competitors by providing large distributions centers that would be able to “serve as many customers as 20 normal supermarkets” (Afuah). Webvan was focused on providing a customized and personal shopping experience of which a traditional grocery store couldn’t provide. These were designed to “provide faster and easier shopping services for the time-strapped customer” (Afuah).
* **Customer Value**: The purpose of value is to maximize customer satisfaction. This can be done through **Cost leadership and differentiation**. Webvan was followed by the **differentiation** path. It strived to differentiate itself from traditional grocery stores as well as online grocery competitors. It attempted to exceed brick and mortar groceries by providing more personalized customer service, fast grocery deliveries as well as a large product mix. Webvan hoped to exceed other online grocers by marketing itself as the “quality-driven gourmet online grocer with everyday grocery prices” (Afuah).
* **Scope:** As for Webvan, their scope is approximately 40 square-mile radius around the San Francisco Bay Area. However, they had other centers that could provide a different range of scope.
* **Revenue sources**: Webvan received revenue solely from sales of grocery products and delivery fees. The company did not intend to sell its customer data to third-party database firms, nor did it receive online advertising fees, since it wanted to remain neutral among the different product brands that it sold online. They should have used some form of online revenue.
* **Connected Activities**: “To offer better value to the right customers, a firm must carefully choose which activities it performs and when it performs them” (Afuah). In this case, the primary activities performed are user customization and the fast delivery process. These activities were designed to give Webvan an edge over its competition both online and offline.
* **Implementation**: The strategies Webvan had were great, however, the environment in which they started their business was not friendly to them. “Implementation in an organization depends on the relationships between strategy, structure, systems, people, and environment.” (Afuah)
* **Sustainability:** The three sustainability strategies to survive are run, team up, and block. A sustainability strategy is chosen by looking at an organization using the complementary asset model. This model determines what sustainability strategy an organization should follow based on its incomparable and complementary assets. Analysis of Webvan’s imitability shows that the services it provides are easy to replicate leading to a high imitability. The complementary assets held by Webvan are easily accessible and free for competitors to utilize. A high imitability with free complimentary assets determines that Webvan must use the **run** sustainability model, the most difficult option, which forces an organization to be constantly innovating to stay ahead of its competition. The run model requires a large number of talented people to survive.
* **Cost Structure**: The high costs of creating enormous distribution centers vastly outweighed the relatively small revenue Webvan made from sales. “A firm’s cost structure expresses the relationship between its revenues and the underlying costs of generating those revenues.” (Afuah) They were just losing money from the beginning. In order for an organization to stay in business, it must create a profit. The underlying goal of every organization is to “make money now and in the future (Goldratt). From its inception, the Webvan system was doomed.

**Stakeholders**

1. **Employees:** Employees have a large stake in the wellbeing of Webvan.
2. **Management:** Management is crucial for a company to be successful because they must develop an organizational strategy and structure and align the company’s discussions around them. This will allow the management to make sure that the company is running effectively and making better decisions for the company overall. The company was able to bring in experienced leadership to guide the company into the future. The management team makes the top-level discussions anything that effects the company has a direct impact on them as leaders.
3. **Shareholders:** The shareholders have a critical stake in the success or failure of the company. After its IPO, Webvan’s primary goal was to provide profit to shareholders.

**Alternatives and Impact on Stakeholders**

1. **Do nothing:** This alternative will involve continuing the business as usual. There would be no particularly large impact. We already know that the forecast does not look great, predicting continuous losses. In a long time, this means that the company would fail unless it could render itself profitable. If Webvan were to continue operations as usual, by 2001, they would see sales of $518 million, with an overall loss of $302 million for the year. If this option was chosen, Webvan shareholders would lose their investment in the company and Webvan would eventually go out of business.
2. **Expand product mix:** This alternative would incorporate a larger selection of goods into Webvan’s catalog, provided it did not steal market from Borders of course. The potential impact is larger if the provided product mix is chosen. Offering other types of goods may very well enable sales that would not be possible due to consumers being willing to pay for certain good deliveries as a way to get one-day shipping on other products.
3. **Exit the market:** This option would involve Webvan to exit the market completely and liquidate all of its assets. Since Webvan was making a loss and financial forecasts predicted even more losses for Webvan in the future, Webvan can cease all operations and exit the market completely. This option could save the shareholders from a large loss if Webvan were to fail as a business. This option may cause Borders a large deal of embarrassment since the business failed, it would be better than having to exit based on bankruptcy. The employees would have to find a new place of work. The customers would have to find a new grocer to purchase from.

**Best course of Action**

My recommendation for Webvan would be to exit the online grocery industry. This industry has not been very kind to them. They are currently not making enough money to make a profit. Doing any other of the options would eventually cause them to go bankrupt due to the need for a large number of finances. Consumers, in general, do not use the service and other competitors can easily enter and leave the market unless they attempt to set up a distribution network and sell directly to reduce the labor costs involved with shopping for consumers.

**Rejected options**:

Do nothing would be the worst option because, in a few years, Webvan will likely continue to lose money, unless consumers could be readily convinced of the benefits and convenience of having your groceries delivered.

Expanding the product mix could possibly be successful but it would also increase carrying costs of inventory, and may also take the focus away from the main business operation. Consumers might be drawn to greater product mix but could also simply use Webvan for those items, on which it would have less of a distribution network and less competitive advantage in sales.

**Therefore, the only other option would be to exit the industry. The sooner they do this, the less money they will lose. This would be a difficult option to go with, especially when considering all of the stakeholders, but I think it is the correct decision.**

**Citations:**

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