Case: Webvan

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Executive Summary

After going public, Webvan was facing high expectations to become a dominant company in the grocery and e-commerce industries. Webvan had a consumer base that was growing and a total market value of more than $8 billion but were witnessing losses and faced many challenges ahead. These challenges included having strong competition in both the online grocery industry and traditional grocery chains, attracting and retaining more customers, and projecting and forecasting into the future. The founder, Louis Borders, believed he could provide efficient operations and tailored customer service that would allow Webvan to become a leading figure in the industry. However, with high operational costs and low initial sales, Webvan was projected to have little impact in the grocery market. With this uncertain future, Borders must make significant strategic decisions that would make the stakeholders satisfied. In this case, Webvan has the option to do nothing, team up with other grocery chains, or innovate and invest in new product lines.

Business Problem

Louis Borders founded Webvan after recognizing the growth of e-commerce in the 1990s. He believed he could take advantage of this phenomenon and discover a cheaper and more efficient way to bring products to customers. Webvan was designed to combine Internet grocery shopping with home delivery and had the main goals of achieving a large consumer base along with respectable levels of customer service, satisfaction, and retention. After operating 5 months in the San Francisco area, more than 10,000 people had signed up for the service which meant they were on better pace than their competitor Peapod, Inc. when they started. However, sales in 1999 were low at $11.9 million while the company could face losses at $35 million. Webvan could not continue to operate if they continued to witness these high losses.

The losses that Webvan were taking were a result of several issues. One issue was that the competition was abundant with seasoned competitors along with new entrants that were flooding the market. Large traditional grocery chains already had large customer bases and Webvan was falling victim to the bounded rationality of consumers and concept of tacit knowledge. Not many people bought groceries online, in fact, the number was less than 1 percent of all the 14.5 million users who had made purchases online. People were not going to switch over to something more convenient right away if it is dramatically different from the way they are used to doing things. Consumers like to pick out the groceries and be confident in what they were buying for themselves. When customers are faced with too many options that offer similar products, they will look for the cheapest, most familiar, or best quality product (Ravi & Robinson). In this case, customers are gravitating to the traditional grocery stores because it is the most familiar.

Moreover, these consumers have tacit knowledge which is knowledge that is hard to verbalize and embedded in the routines of people (Afuah & Tucci). It is routine for customers to physically go to the grocery store and specifying exactly what you want in terms of produce and other goods can be difficult, so people would rather do it themselves. Webvan must figure out a way to alter the consumer’s mindset surrounding purchasing fresh goods and other groceries online. Also, the customers that did buy online were using companies like Peapod which have been around longer. Webvan had to convince those that wanted to purchase groceries online that they were the best.

On the other hand, Webvan and Borders believed their service would eventually stand out and that they could cut costs by having centralized warehouses, fewer employees, and the lack of real estate. While he may have cut down some costs, he made a $1 billion agreement with Bechtel Group to build distribution centers and still faced issues in earning revenue. Moreover, they still had the costs of attracting customers which costs five to ten times as much as keeping existing ones (Ravi & Robinson). Competitors were starting sell more than grocery items and large grocery chains were starting to come out with their own e-commerce solutions. Additionally, forecasts were expecting Webvan to have an overall loss of $302 million for 2001 and sales of $518 million which would be less than 1 percent of the entire grocery market. Borders would have to find a way for Webvan to stay competitive and make the customers feel comfortable in buying their groceries online.

Industry Competitive Analysis

The mission of Webvan is to provide convenient delivery of groceries directly to public consumers through means of differentiated and tailored service. Webvan wanted to make sure their customers had the best and most flexible options they could have. Webvan's generic strategy was differentiation through providing a delivery service unlike their competition in both operations and customer service. They had 80 software programmers who created proprietary systems that automated and tracked every part of the ordering and delivery process. Moreover, they allowed customers to order from over 50,000 products, get delivery next day in any 30-minute period, and had custom shopping lists for them. Webvan was organized functionally with each distribution center operating in the same manner from the ordering to delivery process. Porter's five forces help better analyze Webvan and their environment:

Bargaining Power of Suppliers: The supplier's power is low as there are multiple sources supplying groceries and food products for Webvan to shop around from and find reasonable prices.

Bargaining Power of Buyers: The power of their buyers is high considering there are many grocery stores for customers to choose from. Customers can go to different grocery stores if they feel like they can get better service, price, or products.

Threats of New Entrants: New entrants were a high threat as many companies were taking advantage of the opportunities provided by the Internet and the numerous possibilities of e-commerce.

Threats of Substitutes: The threat of substitutes was high as the market for online grocery was still unstable while traditional grocery stores have thrived and been around for a long time.

Rivalry Among Competition: There was high rivalry with other companies in the traditional grocery industry and online grocery industry. Offline businesses like Kroger and online grocery stores like Peapod had more costumers and an established reputation.

Stakeholders

Louis Borders: He is the founder of Webvan and influences major decisions regarding the future of the company. The direction he encourages Webvan to take will affect the company's operations along with his current and future business ventures.

Webvan Employees: The employees will be affected as the decisions made high up could alter their jobs or eliminate them. Employees will want a decision that will best benefit their career goals now and in the future.

Webvan Shareholders: A change in the company could increase or decrease returns for shareholders. Shareholders will want a decision that will best maximize their returns.

Webvan Customers: Many customers already signed up and are expecting services to be carried out. The decision could affect the options customers have, how they will receive their orders, and if they will want to continue using Webvan.

Bechtel Group: They are an engineering and construction firm that made a $1 billion-dollar agreement with Webvan. They will want a decision that will honor their agreement and possibly encourage future deals.

Alternatives

Do nothing: Webvan can decide to do nothing in their situation and continue operating as normal. They would continue with their plan in building distribution centers, having efficient operations, and reliable customer service in hope that they put the major losses behind them and can bring in more revenue.

Innovate and invest in new product lines: Webvan can decide to add and make new innovate products available for their customers. They would hope this decision would differentiate themselves further from the competition and thus attracting a wide range of customers who may have been skeptical at first. Being relatively new in the market, Webvan can add new products and innovate because they do not have old culture to handicap them and old knowledge to unlearn making it easier for them to adapt (Afuah & Tucci).

Team up with existing organization: Webvan can decide to partner with an existing offline grocery store or online grocery to better position themselves in the market. This would allow them to share the resources of an already established organization and help save time and money. Webvan would not have to fight for as many customers to switch over to their business and use physical locations and distribution centers the existing organization has.

<u>Impact on Stakeholders</u>

Do nothing: By doing nothing, Louis Borders is not planning or strategizing for the future and putting the company in danger of more losses. This decision could negatively affect the how much money the company and Borders make, therefore, could affect the future of Webvan and how Borders runs his other businesses. On the other hand, the customers that have already signed up will be satisfied as they receive the service they desire. However, shareholders will not be happy by doing nothing because it could result it more losses and little return on their investment. Bechtel Group would be satisfied as they would continue with their agreement and build more distribution centers for them.

Innovate and invest in new product lines: Through innovating and making new products available that customers could be interested in, Louis Borders and Webvan will be set up for possible future success. Initially, it could result in some loss, but it could eventually attract more diverse customers that would not have thought of ever buying groceries online. By adding new products, it will make the current customers satisfied by giving them more options and potential customers intrigued with the possibility of trying Webvan. Innovation could also make shareholders happy by giving them a greater possibility of large returns. Bechtel group will be satisfied as it could lend more opportunities for them to build more distribution centers for Webvan.

Team up with existing organization: Partnering with an established grocery chain or company will provide Louis Borders with less pressure and more flexibility through giving Webvan more resources and a larger consumer base. Some customers could be satisfied as their service will still be provided but some may dislike decision if they do not like the direction the partnering organization is heading. Shareholders could see returns if they are acquired but the amount would depend on how much they were acquired for. Some might be disappointed if they believed Webvan had higher potential. Moreover, if Webvan decides to purchase a company, shareholders would not be satisfied as it could result in spending more money and earning less returns. Bechtel Group could be negatively affected if this process halts their agreement of making more distribution centers since Webvan will now be sharing resources.

Recommendation

My recommendation would be for Webvan to innovate and add new products to their inventory for their customers to purchase. Selling more than just grocery items would allow for greater differentiation from their competitors and attract a larger number of people to use their services. When analyzing this decision with the Internet Enabled Business Model, one can see it is the best choice. Firstly, it would increase their profit site and customer value by adding differentiated products. Currently, their competition is strong and offers similar products to Webvan. Webvan might operate more efficiently and provide a better service to their customers, but with them being a relatively new company, they need to be able to deliver more products than seasoned competitors. Customers would be more willing to switch to purchasing from Webvan if they offer products that their competition does not. No traditional retailer could offer as vast an array of products as online companies can because of limited shelf space and inventory constraints (Ravi & Robinson). By increasing and diversifying their products, Webvan can separate themselves from the traditional grocery chains.

Moreover, Webvan can also increase their scope and revenue sources. With Webvan being a relatively new company and whose operations are a different concept to most, they are falling victim to the bounded rationality of customers. By offering a wider selection of innovative products, customers may feel more comfortable purchasing these different products online rather conventional groceries they are accustomed to buying in the store. This would expand their scope by increasing the number of diverse customers and tap into revenue centers that were not there when they just offered groceries. Once customers buy from Webvan, they may be more willing to trust the company to deliver traditional groceries to their home. Through staying innovative, Webvan will not just be picking the alternative that best benefits the stakeholders, but also the alternative that Webvan needs to survive.

Doing nothing is not the best choice for Webvan and will only lead to more losses. While they are expanding and had a successful IPO, the future was bleak for online grocery shopping. Industry analysts estimated there was $156 million online grocery sales in 1998 which is less than 1 percent of the entire grocery market. Moreover, market projections for the year 2003 ranged from $4.5 billion to $10.8 billion and it was difficult to expect which companies would even be that successful. Peapod, eGrocer, and Streamline.com were already differentiating themselves with new products and were giving customers more options. By doing nothing, Webvan is expecting customers to switch to their service even though they will offer less variety than competing companies. Doing nothing will not improve their profit centers and customer value as they are not adding differentiated products. Their scope and revenue centers will not grow because they are not reaching more diverse customers while their sustainability will not improve because they are not innovating.

Teaming up with an existing organization to share resources and customers is also not the best choice. Well established offline grocery stores are aware of the threat of e-commerce, but they are not sitting idle. They are trying to establish their own services and online presence. If a firm is going to team up, it must do so while it still has something to bring to the table and partners have not yet imitated the technology (Afuah & Tucci). Webvan might have strong investments, but they have proved little and are projected to have future losses while other grocery stores are beginning to imitate the technology. Webvan also would not benefit from purchasing another grocery chain as it would cost them more money along with future overhead expenses like real estate that would set them back even further from making considerable revenue. Most importantly, the industry and its environment are not set up best for teaming up and this option will hurt Webvan's sustainability. Teaming up is only best when complimentary assets are tightly held which is when they are rare or hard to substitute for. In the grocery store market, complimentary assets may be purchased and are easy to develop, therefore, are not tightly held.

The best alternative for Webvan to choose would be to innovate and invest in new products because it will best improve Webvan's sustainability. The business is easy to imitate, and complimentary assets can be purchased and are not tightly held. Therefore, Webvan should operate in quadrant 1 and pursue a run strategy and keep innovating new technology and goods before the competition has the chance (Afuah & Tucci). Running involves changing some components of the business and innovating and investing in new products would do just that. They should not block or protect their position because this business is easy to imitate as seen by the new companies entering the market. Doing nothing would lead Webvan to fall behind their competition while teaming up would be unnecessary. Webvan has already been built distribution centers and made agreements for more. If they were to team up, they would be gaining complimentary assets that don't fit their business model like physical retail stores or assets they could build themselves like more distribution centers. Through analyzing the Internet Enabled Business Model, innovating and adding new products will increase profit sites, customer value, scope, revenue sites, and sustainability. Therefore, innovating and investing in more products gives Webvan the best chance of reaching their potential.

Works Cited

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Louis Borders founded Webvan after seeing how e-commerce had grown throughout the 1990s

which combines Internet grocery shopping with home delivery, shot to an 80 percent premium on its first day of trading. As the trading day ended, Webvan had a total market value of more than $8 billion, nearly half the capitalization of grocery industry leaders such as Safeway, Inc., and Kroger Co.2

While Webvan had operated for a mere five months in the San Francisco area, more than 10,000 people had signed up for the service—not bad considering that it has taken rival Peapod, Inc., 10 years to amass a customer base of 100,000 households

1999 sales were expected to amount to $11.9 million—less than large grocery chains make in one day—while losses would amount to $35 million

What additional, if any, delivery markets and products could Webvan pursue in the long term?

Borders recognized that retailing through the Internet, a phenomenon that had exploded throughout the 1990s, would never become really big unless someone could discover a more efficient and cheaper way to deliver products to people's doorsteps.

With this goal in mind, Borders founded Webvan, an online grocer that was "arguably the most ambitious e-commerce initiative to date.

n 1990 Peapod emerged as a front-runner in this industry, and many smaller players followed suit. However, since these smaller players relied on partnerships with traditional grocery stores, they were not able to sell goods cheaper than the actual store.

New competitors, such as Webvan and eGrocer, sprang up in the marketplace, while more seasoned competitors, such as Peapod and Streamline.com, attempted to stay competitive. The original phone-and-fax players who were already in the marketplace were anxious to take advantage of the Internet channel and soon developed websites with product offerings that included not only groceries, but other items such as videos, flowers, music, and toys.

Its primary aim was to achieve a sizable customer base, respectable levels of customer service, satisfaction, and repeat usage

New entrants to the grocery delivery businesses planned aggressive national expansion programs by rapidly rolling out high-capacity customer distribution centers in most major metropolitan areas. Their goal was to steal market share from the enormous off-line grocery market and also to create new market opportunities by providing combinations of delivery services that did not yet exist in the bricksand-mortar world

y benefit the online grocery channel provided to consumers was convenience.

less overhead by using centralized warehouses and employed fewer people than traditional stores, cost savings could potentially be transferred to the end consumer. Lastly, eliminating the costly real estate

Industry analysts estimated online grocery sales of $156 million in 1998, less than 1 percent of the entire grocery market. Market projections for the year 2003 ranged from $4.5 billion (Andersen Consulting) to $10.8 billion (Forrester Research). With such vastly different market projections, it appeared difficult to predict which online companies would do well, if any

of the 53.5 million people who were online in the United States, only 435,000 ever purchased food online. This number represented less than 1 percent of the 14.5 million users who had made purchases online.7

1999 signed a $1 billion agreement with Bechtel Group, an engineering and construction firm, to build distribution centers and delivery infrastructure in 26 new markets over the next two years. In addition, Borders foresaw a safe, secure online customer experience that offered nearly double the selection of products of a typical grocery store and at comparable price

Webvan looked to Federal Express as the blueprint for its hub-and-spoke delivery system, to traditional grocers as the model for maintaining food quality in transit, and to Wal-Mart as an example of breadth of product selection. Webvan's website emulated Yahoo! for speed and Amazon.com for the shopping experience.

Webvan differentiated itself within the online grocery market in two distinct areas: operations and customer service.

80 software programmers created proprietary systems that automated, linked, and tracked every part of the grocery ordering and delivery process.

The Webvan model could do all of this with half the labor and double the selection of products of regular supermarkets. Because of these innovative efficiencies, Borders believed that each of these facilities would make money within nine months of launch.

Once orders were placed on the Web, they were automatically routed to the warehouse. "Pickers" were stationed throughout the distribution center to assemble the orders in plastic boxes or totes

None of these vans traveled more than 10 miles in any direction and the route was mapped out by a system that optimized travel time. At peak performance, Webvan expected that each facility would handle more than 8,000 orders a day, totaling 225,000 items, and generate annual revenues of $300 million

Webvan customers could order a shopping list of items and receive the groceries the next day within any specified 30-minute time period.

Additionally, Webvan aimed to provide its customers with 50,000 products from which to choose compared to a normal grocery store that carried 30,000 items.10 Personalized shopping lists, which appeared after a customer's initial order, were also designed to provide faster and easier shopping services for the time-strapped customer

With high operational costs and low initial grocery sales, Webvan's 1999 losses were forecasted to be $35 million. Total sales for 1999 were expected to be only $11.9 million.11 Forecasts called for Webvan to have sales of $518 million by 2001, with an overall loss of $302 million for the year. Sales of $518 million would be less than 1 percent of the entire grocery market (including bricks-and-mortar sales).

Webvan's average grocery order, as of September 1999, was $71. This was significantly below the average order size of approximately $101 that was needed to generate annual targeted revenues per distribution center of $300 million.12 However, Webvan's services had only been operational for a few months, so management believed that the average order size would increase over time.

Now that Webvan had become a public company, the pressure of investor sentiment would be a major factor in Webvan's future strategic choices. Every decision made would directly affect the company's stock price and standing among Wall Street analysts and individual investors.

Should Webvan use its large market capitalization to buy regional grocery chains in markets it was interested in pursuing? These regional chains already possessed supplier networks as well as their own distribution centers. Webvan could possibly leverage some equipment from these distribution centers while attempting to replicate its existing distribution centers. This option would also eliminate a few competitors in these regions. On the other hand, should Webvan ever consider a takeover offer from a large grocery chain? Although Webvan's lofty valuation provided some protection against takeover, this certainly did not provide a permanent guarantee. Furthermore, should Webvan continue to push forward with additional product lines?