WEBVAN

REINVENTING THE MILKMAN

CIS 410-02

Ajay Singh

4/10/17

Contents

1. Executive Summary

Webvan was started by Louis Borders who was also the founder of Borders Books and wanted a new challenge following the success of the bookstore. Webvan had been relatively successful as the company had signed up 10,000 customers in the San Francisco area in five months. This was supported during the initial IPO offering where the stock shot to an 80 percent premium despite the mounting losses, 35 million dollars on expected sales of 11.9 million dollars in 1999. Borders was faced with questions about what the future strategy such as if Webvan continue to push with additional product lines or should Webvan consider a takeover offer by a large grocery chain such as Kroger.

2. Competitive Analysis

Webvan was started by Louis Borders who had demonstrated his business expertise with the launch of Border Books, second largest bookstore company that became successful due to his market disrupting approach, and wanted a new challenge. Borders saw an opportunity in the online grocery business with the emergence of Internet. Online grocery sales were expected to be 156 million in 1998 and were expected to grow to several billion in 2003 which was still a fraction of overall grocery sales of 453 billion dollars. Borders was confident of Webvan's success as he believed that the first-to-scale counted more than the first-to-market which lead Webvan to make a billion dollar deal to build new distribution centers along with delivery infrastructure in 26 new markets within next couple years. Other larger grocery chains held most of the market share now but as Morgan said, "Without regular updates, any knowledge gained from using Porter's model will quickly be out of date as it was only designed to provide a snapshot of any particular market" (Morgan). Larger chains were understanding the cost of stagnation following the Webvan IPO and were working on ways to keep their advantage.

Webvan was adopting a divisional organization structure as the company was creating distribution centers that were to serve their respective areas and have transport network to support it. The first distribution was built in Oakland, California to service customers within a 40-square mile radius around San Francisco Bay area. This provided company with better responsiveness by increasing adaptability, accountability and time efficiency should the situations change due to customer demand, local competition, or other conditions affecting the divisions (Cash, 41). Webvan had a lot of competition in the grocery market especially with the emergence of the internet as any company could enter the business with relatively small investment due the economies of zero.

Internet brought a lot of opportunities with it as it removed some barriers faced by traditional organizations. Internet decreased the time it took to share information which in turn allowed organizations to respond faster to changing market conditions. Internet paved a way for online organizations that had a low cost per transaction due to the decreased variable cost namely labor as people were no longer needed to accept orders because the customer could submit the order via the website. "Long distance networking minimizes geography as a constraint in doing business" which meant that organizations could reach more people than was previously possible (Cash,257). We can also apply the 4 Es to Webvan as the benefits provided by the internet allowed Webvan to enter a congesting market and be successful. Borders had plans to extend the area Webvan services quickly to be more effective. Internet would also allow to expand the things Webvan sells to increase the profit margins and test out new product categories to see what is successful and what is not like was in the Borders Books where AI system calculated which books sold more and ordered those while removing the ones that didn't sell. Webvan could also experiment with new products as it would be easy to exit that market if it wasn't profitable. This would not be possible for brick-mortar stores as the cost of exit for them is very significant. Webvan was also tackling the problem of convincing people to use their services as people still resisted ordering groceries online as it is something new and something they are not comfortable with. Tacit knowledge also comes to play with fresh produce as people usually prefer inspecting it themselves and picking the produce that passes their quality measures. Webvan has a lot of problems to overcome before they can be successful and Borders must decide on what strategy he would like to adopt, or if he would like to just sell the business as a larger chain might be better equipped to overcome this challenge.

The analysis of Porter's five forces is as follows(Lima):

High threat of new entrants: Threat of new entrants has greatly increased with the emergence of the internet as organizations located anywhere geographically can compete against Webvan which makes ever new grocery store a direct competitor to the company. Internet has also reduced the cost of entry and cost of each transaction making it easier for new online grocery stores to enter the market.

High threat of substitutes: Webvan operates in a saturated market where customers can either go to another online grocery store or just visit their local super market to purchase their groceries.

High supplier power: Webvan is a reseller and is reliant on seller to provide products for Webvan to sell. Sellers have other grocery stores that can sell the same products and in no way rely only on Webvan. And since Webvan is still relatively new with only 10,000 customers, suppliers have little reason to give into any of the Webvan's demands which increases their power.

High buyer power: Customer in purchasing groceries have a lot of options when purchasing products ranging from other online stores to local super markets to local grocery shops. Shoppers can also substitute products to something similar if that specific product is only sold at Webvan.

High degree of rivalry: Webvan is facing competition from local grocery stores and chains to other online retailers from other parts of the country that are all trying to provide the services customers want effectively.

3. Generic Strategy

Generic Strategy for Webvan was differentiation by focusing on operations and customer service. Webvan created a proprietary system that automated, linked, and tracked every part of the grocery ordering and delivery process. A larger distribution center would server the customer in the surrounding area through use of delivery vans that would take items to customers' homes. The system was designed to be effective at meeting customers' needs while being efficient to increase profit margins for the company. Each distribution center could handle more than 8,000 orders per day for a potential 300 million in revenues with half the labor cost of a traditional supermarket. Webvan wanted to provide the best customer experience and hence provided the option for customers to receive groceries the next day within any specified 30-minute period. Webvan increased the products for customers to choose from 50,000 products while increasing the ease of use and saving their time that they would have wasted while trying to find the items in a super market. Webvan also restricted couriers from accepting tips and were thoroughly screened and trained in which helped customers feel comfortable about inviting stranger to their home to deliver groceries.

4. The Stakeholders

a. **Webvan:** The company, including the stockholders, is a major stakeholder. The decision made by Borders could have drastic effects on the company as Webvan is running mounting losses. Stockholder would want to see a return on their investment soon. Any decision made by Borders will directly affect the company and its stockholder could mean Webvan's disappearance from the marketplace to becoming the leader in the online shopping arena.

b. **Webvan Employees:** Any decision made by Webvan would influence the employees as it would affect their job status. Employees could lose their jobs if company was to go out of business or be sold to another company but it could also result in bonuses and pay increases if company does well and becomes profitable.

c. **Louis Borders:** Louis Borders has a large stake in the company as its founder. Louis has been successful with his other venture, Borders books. The success of Webvan would have an effect on his reputation as he is currently viewed as a revolutionary that changed the book selling landscape.

d. **Webvan Contractors:** Contractors for Webvan have a major stake in the company as it could affect their revenues. Webvan has a contract with Bechtel Group to create distribution centers and delivery infrastructure in 26 new markets which would be in jeopardy if Webvan were to go out of business.

5. The Alternatives

a. **Do nothing:** This would be the default decision for the company as Borders could decide to leave the company as it is with existing plans in place. The company is currently losing a lot of money which could continue if Borders' expectations end up being incorrect. Company does have a considerable about of funding left to remain in business and wait it out but as a public company, investors would want quicker results and returns on their investment.

b. **Buy regional grocery chains:** Webvan could decide to purchase some regional grocery chains that have their own supplier and distribution network set. Webvan could leverage the equipment from the distribution centers to complement its own network. Webvan could also use the existing customer base of the regional chain to boost their member count. Webvan is creating huge distribution centers that can support several times the orders that Webvan currently accepts in hopes to remove order bottlenecks which are defined as any resource whose capacity is equal to or less than the demand placed upon it (Goldratt, 145). Bottleneck for Webvan's expansion currently, other than the consumer reluctance to try new services, is the time and resources taken to build new distributions centers. Purchasing the regional chains would speed up the process of entering a market although it would result in higher costs which would result in more losses. Investors would want to see results as soon as possible which this could help with but at significant upfront costs.

c. **Expand the product line:** Borders could expand the product line that they currently offer to include more items that customers might be willing to purchase online. Products chosen to carry would could be picked based on true strategies, one that sell the most with good margins, or ones that complement their existing product lines. As an ecommerce company, Webvan would be better off by offering products that people are open to buying online such as electronic. Once people order those products and receive the intended service, they would be more trustworthy of the company and will be more willing to purchase perishables from them. It would help Webvan overcome the bounded rationality. This option could result in further losses due to the resources required to convince people give the company a chance along with the costs to expand and stock the product line. Since, Webvan is an ecommerce company, their costs for expanding and contracting the product lines is low. Product lines that Webvan decides to expand to would have an effect on local stores as they could potentially lose business as Webvan moves in but that is not a concern of the organization as it is duty of the executive to work in the best interests of the shareholders as told by Morgan in THE UGLY FACE: INSTRUMENTS OF DOMINATION (Morgan, 298).

d. **Sell the company to a larger competitor:** Webvan's stock boosted to 80% premium but that boost will not last if company does not return the profits that investors are expecting. Webvan could try and find a buyer that would be able to buy the company at the current price before the stock starts to drop. A larger grocery chain will have a supplier network and distribution network already in place, and might be better equipped to turn the online grocery business into a profitable one. This option would get some of the investment back for Borders and other investors.

6. The Recommendation

Recommended option for Webvan is to expand their product line to include a variety of items. Online grocery business is struggling as is shown by other competitors who are struggling to make a profit. Webvan has a huge task to convince people to use its services by overcoming their requirement for tacit knowledge and bounded rationality. Consumers are not yet comfortable with ordering their groceries online and having it delivered to their home especially fresh produce. Webvan could try selling other items such as electronics, appliances that consumers do not need to experience before purchase. Webvan has already built a distribution center that can deliver any product to the customer should Webvan decide to expand. Webvan could as easily stop carrying items that do not sell and do not attract new customers.

Works Cited

- Cash, et. al. Buildi, the Information Age Organization
- Goldratt, E. The Goal
- Morgan, Gareth. Images of Organization
- Unknown. Apes Demonstrate Basic Facts about Humanity
- Unknown. The Rules of Bureaucracy
- Tony Lima, Michael Porter's "Five Forces" Model