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CASE ANALYSIS, MODULE 6B

WEBVAN

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Overview

After the huge success of building bookstore legacy Borders Books, brothers Louis and Tom decided to turn their attentions to a new industry in which they saw immense potential: Grocery delivery, with the help of the increasingly popular technology of the internet. Webvan would be an internet-based company offering grocery shopping with home delivery services. After a mere five months after the company's foundation, Webvan had acquired a customer base of more than 10,000 people in the San Francisco area. In contrast to other similar companies' growth, this was an incredible feat. On its first day of trading in 1999, shares of the two-year old company rose to an 80 percent premium, and the company had a total market value of more than $8 billion. Despite sales expected to amount to $11.9 million in 1999, the company was also facing losses amounting to $35 million, raising concerns by the founder Louis Borders about the sustainability of the company, and prompting an inquiry on how the company could continue to grow and compete in the grocery industry.

The Problem

Webvan's business model is not unique and it had entered the market to be among several already established grocery delivery companies. Added to this competition are the number of substitutes in regular retail brick-and-mortar grocery stores and chains that offer the same products that Webvan would, and had significantly more profits and customers at their disposal. The problem boils down to how to ensure the sustainability of the company after such a successful initial public offering. The Webvan company has a choice to make regarding its sustainability – will it run from the issues at hand, block new entrants and competition from poaching its business, or find a partner in the industry that can benefit the business.

The Solution

Webvan must decide its course of action if it will continue to compete with other businesses offering similar services as well as well-established grocery chains. Analysts estimated that online grocery sales in 1998 would mount to $156 million, which while only a partial percent of what the entire grocery industry sells, has incredible potential for the future. Those customers who had begun grocery shopping online proved to be reliably repeat customers, which Webvan can use to its advantage.

Industry/Competitive Analysis

Webvan

Webvan was not the first, nor will it be the last internet based grocery delivery company. But the founder's success with Borders Books gave him the vision to focus on being first-to-scale rather than first-to-market, and planned to use operations and customer service – based on, and inspired by the success of operations and customer service seen while growing Borders Books – in order to differentiate itself from the competition.

Threat of New Entrants

The threat of new entrants in this industry is high. It would take a lot of capital to begin a new grocery chain, and it would take several years in order to balance out the return of profits in order to see profits rise. However, in the internet-aided grocery industry specifically, the bar to enter the market is much lower. Someone else with the same vision may better be able to set up a supply chain to serve their customers, and can become established in a relatively short amount of time, just as Webvan did. Established grocers might see the ease at which they can enter the market for internet-based delivery orders and could easily hit the ground running with little to no additional cost. The internet allows an established chain to enter the internet-based grocery market with ease due to economies of zero.

Bargaining Power of Buyers

The power customers in the grocery industry is high. Switching costs for customers are fairly nonexistent – a customer may be accustomed to retrieving their groceries at a particular store due to selection, location, convenience, and could easily make the switch to getting some or all of their groceries delivered at home, but there is little to keep them from returning to their already established grocery habits if internet delivery does not fulfil their needs. The industry relies on customers repeat business, and therefore must make a big focus on not only attracting new customers, but keeping their interest.

Bargaining Power of Suppliers

Bargaining power of suppliers for groceries is medium. Some popular brands may have agreements with certain grocery chains in order to sell their products, which may put a barrier for new entrants of the grocery business to attain the supplies of products that their customers want to buy. Webvan will have little bargaining power in its relationship with suppliers, because the supplier can get their product to customers through a different company.

Threat of Substitutes

Threat of substitutes in the internet grocery delivery industry is high. Not only are there other options for customers to choose for specifically internet ordering of groceries, but they may also switch to the traditional grocery store trip with very little additional cost to them. Other companies offering the same services may have slightly different business models, or may specialize in providing one type of product over another, so a business must establish what makes it unique and more beneficial to customers over its substitutes.

Competitive Rivalry

Webvan's competitive rivalry is high. Not only is Webvan competing against incumbent grocery chains that people are already accustomed to visiting for their grocery needs, they are also competing against other companies with very similar service offerings. Peapod, Streamline, Shoplink, Netgrocer, eGrocer, among others, all offer similar services, though what exactly they offer may vary slightly, the demographics they serve certainly overlap with the customer base of Webvan.

Stakeholders

Webvan Shareholders

Webvan is now a publicly traded company, so its success is very important to its shareholders. Because of the initial success and quick rise of Webvan, it may have been a bit of a risky investment, but the potential is certainly there. Webvan's success would mean success not only to the business, its employees, and its founder, but shareholders will benefit and will be more likely to continue investing in and supporting business ventures linked to Webvan and the Borders name.

Employees

Webvan employees will certainly be negatively effected in the event that Webvan ends up a failure. Though Webvan employs only half the labor force as a regular grocery retailer, there are also others on its payroll such as software programmers. These workers are in on the ground floor of something with great potential, and though the software programmers would arguably have an easier time finding new employment if Webvan were to fail, the other part of the labor work force may not. Having the experience in an operations and distribution center could be really advantageous to these workers.

Consumers

Customers of Webvan have less to lose than its shareholders and employees, but those who use the service and have continued to use it will have come to rely on the delivery service to get the time back that would have been sunk at the grocery store. Sure, there are alternatives for delivery, and one alternative is to return to the habit of going to a physical store, but this would not be the ideal outcome for those that have made the switch to grocery delivery.

Contractors

Webvan had signed a contract in 1999 for $1 billion with Bechtel Group, an engineering and construction firm, to build Webvan distribution centers and delivery infrastructure over the course of two years. These workers certainly depend on the success of Webvan, as that is a lot of money for this contractor to accept for a plan of this scale. If Webvan were to fail, and the contract fell through, this contractor could suffer a huge blow.

Potential Solutions

Do Nothing

Webvan could continue to operate as it is, and hope that they are able to poach more customers from established physical grocery stores by offering the convenience of delivery. Research did show that 89% of customers that had begun purchasing groceries online visited the grocery store fewer times, which could be used as a tactic to transform customer's ideas of what grocery shopping is, and attract new customers.

Partner With or Sell To an Incumbent Grocer

With how easy it would be for an established grocer to offer their own grocery deliver service, I believe Webvan could consider partnering with one of these grocers in order to get their business more well established and used by customers that may not be initially willing to change their habits and use a delivery service for groceries rather than going to a physical store. Webvan can capitalize on its already established name and business model to market itself to a grocery chain that may be seeing the potential for expanding its business to include an internet based delivery service. As in any industry, large grocery chains will need to adjust their business models in order to continue to compete with substitutes such as Webvan's service, or they will fall behind the curve.

Focus on a Smaller Market

If Webvan focuses on serving the Bay area with their grocery delivery service, they could focus on being successful in one area before eyeing other markets for expansion. While Webvan invested in an agreement that would expand its distribution and delivery infrastructure, the company could stop at the expansion it planned in 26 new markets, and focus on those established areas to fine-tune their business and systems. The text did not specify where these markets were, but I will assume they are fairly geographically close, probably within a certain mile radius of the bay area. To have an initial "test" market with an already established customer base and the investment capital to expand, there is immense potential for Webvan to get its strategy right before it continues to grow.

Employ Technology to Become a Standout in the Industry

Technology can be used by companies to expand their reach, attract new customers, make ordering and supply chain more simplified, among a number of other advantages. Webvan can use technology to its advantage to gather information from its customers about what types of products they enjoy purchasing for internet delivery, what kind of products they wish they could buy, and to study the purchasing habits of their customers in order to make suggestions to those filling their digital baskets.

Exit the Industry

It would be reasonable for the owners of the business to look at their situation, see an impending failure, and cut their losses by exiting the industry.

Selected Option: Partner With or Sell To an Incumbent Grocer

If Webvan is to avoid the same fate as failed internet enabled business models such as Pets.com, I recommend that it should either partner with or sell to an already established grocery chain in order to strengthen its supply chain and gain customers before it considers expanding its business. I believe it is going to take a very special service to convince people that actually going to a physical store to "squeeze the tomatoes" as it were, is no longer the preferred way of acquiring the week's groceries. This service would be very helpful to specific groups of people that would benefit from spending the time shopping at a grocery store on other activities, or may want to avoid the hassle of getting to and from the store – mothers with small children, the physically disabled, and those with medical issues that prevent them from driving, to name a few.

Additionally, Webvan must come up with a solution to the amount of time it takes for a new customer to set up their account and first order. If they do not improve their 45-minute initial setup time, they will lose the interest of many initial customers. Webvan has such potential if it uses the internet to its advantage to improve how it conducts business, markets products, and delivers its service. If the company were to use the data of its customers – not to sell to third parties, but to use its own – it could revolutionize how people view shopping for groceries. Technology can help people curate their grocery lists, remind them of things they may be missing in a cart, suggest products that would go good together, and countless other marketing opportunities. Grocery stores already use placement to expose customers to products that may not be on their lists, and Webvan can use the same tactics when helping people build their grocery baskets online. I believe that it is not out of the realm of possibility to use technology in order to increase the average order size to the point where targeted revenues are met or exceeded.

If partnered with an established grocer or grocery chain, Webvan could focus less on the supply side of things, and focus more on the delivery of its goods and services. Perhaps the founder could use his knowledge of the Borders inventory system to improve the inventory system of the grocery chain they partner with. Though Borders believed that eliminating store costs like real estate, clerks, and storage, it would seem that partnering with a grocer would not only grow their available inventory, but not be an additional burden on the internet enabled business model. Webvan could continue to use warehousing and distribution to deliver its products, but with the added advantage of having back-up stock and additional workers if necessary.

Rejected: Do Nothing

I believe that doing nothing would be the ruin of this company. It's business strategy is not necessarily unique enough to really stand apart from its competitors, and to not take the opportunity as it's seen so much success in a short amount of time to assess its standing in the industry and adjust its trajectory would be ill-advised. A company that is not adjusting to its environment – including its relationships to rivals, suppliers, customers, and technology – is doomed to flail and ultimately fail.

Rejected: Smaller Market

If Webvan is to focus on a small market in order to really fine-tune its business model before expanding to larger markets, it really needs to focus on delivering a unique service. Diversifying its inventory, working with resources on the internet to spread word of mouth, and focusing on improving its delivery service will certainly help the company become established, but I don't believe that is enough to become a company that is ready to expand into multiple markets, let alone nationally.

Rejected: Standout

One of the biggest questions in this case is how Webvan can stand out amongst its competitors. While I believe that Webvan should seize some of the infinite opportunities that the internet offers for growing its business, I don't believe this is the key to ensuring sustainability, rather it is the key to staying cutting-edge and ahead of the competition in the industry. Webvan would do well to use data from its users to develop programs that could suggest products, recommend adding a product to a cart if a customer adds another (buying pancake mix? Make sure you offer eggs, oil, butter, syrup, etc.), and even improve delivery routes and practices. It would be foolish to discount how much technology could take Webvan from a promising burgeoning company to a well-established leader in its industry, and able to successfully compete with the large retail grocers.

Rejected: Exit

Although leaving the industry would allow the founders to pursue another business venture that may be more easily lucrative, I believe that this is not the best option. There has already been a significant cost sunk into establishing the business – not to mention new shareholders would be unhappy about the dismantling of what they saw as a business with huge potential – and it could be a really successful business model if the right solution is found in order to make them continue to make profits. Instead of completely exiting the industry, the company must first find a business partner that can help it improve its business model.

Resources

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