

# BUSINESS2.0

## Trial by Fire

**It's not easy to spend \$1 million a day. But Priceline's Webhouse Club did so with bravado up to the very end. The former president tells us what he learned.**

From the December 26, 2000 issue

**Steve Mott**

There are many reasons why those of us associated with this moon-shot called WebHouse Club want it to fade quietly from memory. But to let that happen would be a disservice. I believe it was an inspired enterprise that paved bold new paths into the ecommerce landscape. It was a wild, impulsive \$360 million experiment to fundamentally change consumer behavior, where even the most elemental products and services could and would be priced in real time, according to their relative value at a given moment.



Illustration: Emmanuel Kerner

My involvement with WebHouse began in the summer of 1999, on a recommendation from a consulting client to the company's recruiter. After checking out other enterprises backed by Priceline.com's Jay Walker, I signed on as chief strategist for Walker Digital, Walker's intellectual property think-tank, and was immediately "loaned-out" to WebHouse Club. At the time, Priceline.com was hugely successful, both in profit-and-loss terms and in market valuation. But Walker, having turned over the reins of Priceline.com to professional managers after it went public in mid-1999, saw a bigger opportunity than just airline tickets for his nascent business model. He dreamed of millions of consumers receiving via the Net those critically important items they bought and consumed every day. The potential for controlling "wallet-share"—the Holy Grail of ecommerce—was at hand.

The idea was simple: Consumers would buy products such as groceries online at big discounts—up to 50 percent reductions. They would then pick up the items at local supermarkets using an ATM debit card. The discounts would be funded by companies offering their wares to WebHouse customers and by manufacturers seeking to move more product. It was the quintessential clicks-and-mortar play, using the cost-effective Internet to collect and market to millions of consumers, while staying friendly to retailers, leveraging their investments in stores and distribution systems rather than trying to supplant them.

Three days before WebHouse's launch on Halloween 1999, I was named president. In the next few months WebHouse achieved some impressive successes. It amassed two million customers—a half-million for the gas business alone in just 12 weeks. A national network of 7,000 participating supermarkets was created. There were substantial commitments from marketing partners and manufacturers, including Net2Phone, Essential.com, Kellogg, and Meineke Discount Muffler Shops. The business processed more than 7 million transactions in just 11 months—a growth rate that eclipsed even the early days of Amazon.com and eBay.

But the bet on the table was enormous—it would take more than a \$1 million-a-day burn rate to overcome internal constraints and external inertia and reinvent pricing for these businesses. This fall, Walker shut down WebHouse completely, just weeks before its first birthday. His own access to new capital had been curtailed due to a free-fall in Priceline.com's stock, and outside investors decided they'd had enough of the ride. The money that was so cheap and easy in the

hyper-growth fad just six months before suddenly dried up, leaving no time to spin out or reposition the grocery and gas businesses in Wall Street's new quest for rapid profitability. Not following on the siren song of Wall Street was one of the big lessons I learned from my experience with WebHouse. Here are four more.

## **1. Know thy customer**

For practitioners of direct marketing, the Internet is the ultimate vehicle to sell all things to all people. Yet Priceline.com believed it knew enough about how consumers would behave when presented with a very different value proposition and a relatively complex online-purchase-in-person-pickup process. The thinking went that we just couldn't take the time to perform proper market research on something people had never done before. Just put up the service, fix what doesn't work, and build it as we move along.

It wasn't that simple. We encountered the first problem when it came time for the initial club-card distribution. Everything depended on consumers retaining and activating a strange-looking membership card that was carpet-bombed into their mailboxes and driveways via a massive direct-mail campaign that was supported by extensive broadcast and outdoor ads. Few bothered to hold onto the card and visit the Website to register, confounding predictions of strong response and adoption rates. Tens of millions of dollars were wasted on this untested theory of marketing exuberance.

Another big problem was the site itself. Its presentation was laborious and tedious—something we realized pretty quickly but were unable to address amid desperate efforts just to keep the site running. Repeat-purchase rates sank after the initial enthusiasm waned, diminishing return on customer-acquisition costs. Constant site outages and slow access via America Online also turned off many consumers—as did product and pricing mismatches at participating stores.

Despite the obstacles, several hundred thousand customers stuck with the system, proving Walker's basic premise that there was an interesting market for consumers willing to trade off convenience for savings. But many more customers could have been lured and retained had we tested and improved the service before rolling it out nationally and blindly pursuing horizontal growth.

## **2. Question the technology early**

Mastery of Web-based and transaction technology is no easy matter, as anyone who ever launched and operated an ecommerce site can undoubtedly tell you. Scaling a transaction-based business capable of processing 5,000 orders an hour is fairly trivial for a Unix platform, but not for Windows NT, the platform we used at WebHouse.

NT worked well at Priceline.com, which had much less transaction volume. The choice of the platform for WebHouse was based on at-hand convenience—it was already there, and in the interest of speed (that again), it made sense to leverage that technology to get the business started and then build something better later, when necessary.

On top of that, it was decided that all the various Walker enterprises—Priceline, WebHouse, Perfect YardSale, and others—would share the customer database (Oracle software running on Sun Microsystems Unix boxes). That way, customer data had to be entered only one time and could eventually be accessed by all the enterprises. Sounds good in theory. Trouble was, each business had different approaches for entering and accessing this information, introducing a litany of operational problems and breakdowns.

By spring of this year, the national rollout had to be delayed for a month because the platform broke down so often. Key retailers such as Winn-Dixie Stores had to pull back deployment to give the Website breathing space.

We did try to fix things. WebHouse hired Jim McGill, a world-class CIO from Morgan Stanley, and many members of his team to resuscitate the platform and begin work on a system capable of processing 20 million transactions a day. By late summer, at gigantic cost in both bucks and bodies, the team had stabilized the platform and reduced the outages. But scaling for volume was still daunting, and the gas business, introduced in late June, had to be throttled back to avoid blowing up the site. In late September, with time and cash running out, Walker redesigned the grocery business to address a much smaller customer base. McGill decided to move on, taking with him the last hopes for challenging the technology status quo.

How ironic that such a bold enterprise would fall victim to religious zealotry over the choice of technology when Walker himself repeatedly avowed: "We're a marketing company, not a technology company." Yet the massive problems with the technology platform prevented all but the most minimal marketing nuances to be deployed and thwarted our quest for real breakthroughs in modifying consumer buying behaviors.

### **3. The idea before the man**

Without question, Jay Walker is one of the most creative, intelligent, hard-working, and determined visionaries in this or any era. Using the Internet to collect buyer demand and orchestrate novel pricing schemes was pure genius. Creating the buy-online-pickup-offline business model—a collective effort—was a brilliant and seminal form of clicks-and-mortar.

But much of the PR and positioning of WebHouse was focused on Walker himself—the "New Age Edison" as Forbes called him, rather than on WebHouse as the manifestation of the idea. Few analysts understood that Priceline.com had no stake in the business. Few media tuned in to how far and fast the enterprise had spread. Few people from the investment world had any idea that so much money was being spent in less than a year on trying this idea. Instead, Walker monopolized the media exposure and seemingly focused on building his own, personal brand.

And so it should have been no surprise that when he pulled the plug as suddenly as he did—on the grocery and the more-near-term-viable gas business as well—it was essentially a personal decision. It was his idea and mostly his money, and if he couldn't find outside investors to do it his way anymore, he'd just pack up his toys and go home. The man was just bigger than the idea.

### **4. Speed can kill**

The reasons for the irrational exuberance that held sway from fall 1999 to spring 2000 will be debated for a long time. The stunning shift of venture capitalists and other capital market players from disdaining anything not growing exponentially to insisting on a "quick path to profitability" will be long remembered. The final lesson we can take from the WebHouse experience should be recounted for a longer time still: Speed can kill.

WebHouse consciously wasted money building components of the business model two or three different ways so that at least one working version—if not the best option—would be available and not slow down the enterprise. We pursued customer growth at all costs—especially customer satisfaction. We crossed our fingers and prayed that a doomed technology architecture would somehow see us through, so that we didn't spend time and resources building something better. We accelerated our national rollout (from 12 months to four), at great risk to our operational integrity, to become more relevant and powerful faster. And we enlisted investors who bought the story on faith and wouldn't slow us down.

Experience is still the best teacher, and hopefully we all have profited in a permanent way from living both the incredible achievements and the depressing miscalculations that led to the

WebHouse Club's dramatic fall to earth. It was quite a ride.

**Steve Mott** ([steve@betterbuydesign.com](mailto:steve@betterbuydesign.com)), a former SVP-eCommerce at MasterCard, is CEO-- BetterBuyDesign. He consults with and brokers new ideas between small startup companies with new technologies and large organizations with online ambitions.