

BUSINESS2.0

Winning One Customer at a Time

The information portion of any good or service has become a large part of its value. Information is easier to customize than hard goods. Suppliers will find it more profitable to customize products, and consumers will demand individual tailoring.

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Forget about the Information Age — it's already over. And you might as well start cleaning out of the proverbial closets everything you've learned about how to do business. That's right: Your old Economics 101A textbook — gone! [Porter's parables on competing](#) — dead! Those write-ups on value-added component chains about which nearly every consulting company has "unique insights" — out! Because we are at the dawn of a new age of business relationships. The winners and losers in this new era will be determined by whether they harness digital technology and Internet access into a pipeline of two-way interaction and information flow between individuals and organizations.

In the Information Age, interactivity between individuals and organizations was more or less an "hourglass," with a bottleneck for controlling information and transaction flow in the middle. In industries such as health care and insurance, for example, tiers of "middleman" intermediaries offered varied levels of access and different flows of input. An employer could see different information about a medical claim than an insured patient could; ditto for the insurance broker, the insurance provider, the service provider (such as an HMO), the medical provider, and associated vendors. If, as the insured patient, you wanted to make an inquiry on a claim, there was a mountain of paperwork, a labyrinth of approvals, and a delay of perhaps months to get your answer. This bottleneck was further constricted by limitations of technology in providing robust, secure, and convenient access to relevant information about either party. Typically, companies dictated access based on technologies they could comfortably master and afford (customer and product databases, transaction-processing systems, customer service facilities, etc.).

For physical-world distribution, such as for automobiles, you had to go to a dealer — and suffer the ministrations of car salesmen to get the model you wanted. Same thing goes for travel reservations, through travel agents and agencies. Universities for academic records. Banks and brokerages for account information, investments (especially mortgages), and funds transfers. And so on. All the important organizations of your life made you navigate through substantial bureaucracies to get the information you wanted and needed — ironically, information about you!

In many cases, intermediaries became self-perpetuating and added to the bottleneck effect. In extreme cases, virtual mono-polies formed (telecommunications, newspapers, banks, etc.), with all the economic and service inefficiencies that lack of meaningful competition engenders. Does anyone today associate good customer service with any of these "institutions"? We've all suffered through their endlessly annoying (voice response) and costly (account service fees) inefficiencies without much recourse.

The New Economy changes all this. Digital transmission over public networks such as the Internet creates the ability to exchange information, negotiate deals, provide identification, and communicate more efficiently and effectively than anything that came before it in the

physical world. The new gatekeepers of these information pipelines are business-unit managers attempting to enhance relationships with customers, rather than the intermediaries and IT departments that made their living on restricting that interaction. If they're smart, the new gatekeepers will develop these pipelines into sustained transaction flows driven by one-to-one relationships.

This shift, of course, assumes we can all sort through the attendant issues of security, privacy, identification, rights management, microbilling, and other features of the emerging digital-transaction environment. Given that assumption, the essence of this new rule of competition is simple: Offer unprecedented levels of information exchange between individuals and the organizations that are key to their lives. Hard-wire that relationship — with all of the trappings such intimacy can provide — for both parties. Then let the value flow between them at unprecedented levels.

Digital buyers who have the wherewithal, expertise, and access (consumers with digital lifestyles, small home-offices, and high-tech companies) to take advantage of Web-based relationships are already demanding that the organizations they deal with open up such pipelines, and directing their business to those who do. Digital sellers — the organizations that "get it" — are scrambling to satisfy those demands, because these buyers constitute by far the most attractive customer segments in the marketplace. They make money, move money, and spend money. They care about brands, they're willing to pay for convenience and time savings, and they relish new and different things. The enlightened sellers attracting their attention and loyalty are increasingly brand-new companies with a new brand of value propositions, taking franchises away from physical-world organizations still recumbent in their bastions.

Matching buyer and seller

One technique these "infomediaries" use to disintermediate established players is to attack an industry's conventional distribution strategy. Incipient ecommerce abounds with examples of that already: stock trades, classified ads, travel reservations, books, and records. Now consider a new Internet-assisted "ecosystem" that nukes the old distribution system for selling toys: the Beanie Baby ecosystem (see sidebar, below).

Ty, the purveyor of this collection of cute, cuddly bean-bag creatures, has taken consumer branding, aftermarket channel development, and distribution relationships and logistics to a new level by completely bypassing mass retail toy stores as the primary outlet for impulse purchases of toys. The volume of such expenditures siphoned off to Beanie Babies contributes materially to the current financial malaise of Toys 'R' Us and other conventional toy retailers. The hottest impulse items are getting channeled to seemingly every other kind of store, so who needs the aggravation and drudgery of going to a toy store anymore?

Another important way buyers and sellers find each other in the New Economy is through lifestyle portals. Real portals that deliver information and transaction opportunities right to your fingertips. Links that offer turnkey, convenient, easy-to-use digital access to the goods and services of your life.

@Home already augments its high-speed cable access with content (news, stock quotes, community info, etc.) when you fire up your PC. AT&T and Tele-Communications, when the merger is approved, will offer a collection of services — especially focused on Internet access — that will be a communications gateway from homes and small businesses to the outside world — all on one bill! The pell-mell rush toward a global wireless environment will put a premium on self-contained, highly efficient, stylized interfaces to size-constrained devices.

But the model extends to the non-digital consumer as well. HomeRun Network, an Internet startup in Philadelphia, will offer PCs wired to the Internet built into new homes like any other household appliance, amortizing the costs in the mortgage. This company, focusing on the 50

percent of the population that doesn't fuss with or own PCs, is creating a gateway that will direct interactions and transactions to nested shopping communities, community info lines, banks, and other services. Dead-easy solutions for PC illiterates!

Some brands will transcend their existing product relationships to establish lifestyle relationships. Harley-Davidson — perhaps the original product ecosystem — has 600 domestic dealers located primarily in industrial sections of town. These stores became a favorite shopping spot due to the distinctive clothing and accessories of the Harley brand. Toys and novelty items were added, and we now see Harley shops appearing in upscale malls! Harley also has 1,000 H.O.G. (Harley Owners Group) chapters, uniting some 400,000 loyalists around the world. Like Beanie Babies, Harley carefully encourages its consumer community increasingly via the Internet.

This transcendent brand is now moving in several other directions. The brand has been removed from cigarettes out of concern that minors would be affected by advertising (and concern that Harley would become involved in litigation), but is being extended to eyewear and other consumer products. How long before 40-something men select Harley lifestyle portals for their content gateways — not just for clothing and accessories, but for household products, consumables (e.g., microbeer), riding mowers, and mutual funds?

Pity the poor physical stores and distribution intermediaries with static, intractable inventories. For buyers who can plan 24 hours ahead for purchases, a whole constellation of new choices is available.

Sorting through those choices is getting dramatically easier, thanks to facilitated information flows. Go to www.dell.com (\$5 million a day in online sales) and behold the rich, abundant information that is available — about the products, but also about the transaction: when, where, how, how much, how it can be paid for, delivery status, and the like. The savvy online seller's new business-delivery system removes the pain and aggravation of transacting. For business-to-business markets, the decision to abandon mechanically complex and expensive transactional processes like EDI (electronic data interchange) in favor of Web-based systems becomes a no-brainer. Little wonder forecasters predict \$105 billion in online business-to-business sales by 2000.

In the Old Economy, optimization of markets would typically lead to commodity pricing. Certainly, we can see the disintermediating influence of the new information-pipeline exchanges on pricing in many industries. (See "Mott's Matrix," below.) And we are witnessing revolutionary new mechanisms for customized pricing (Priceline.com for airplane tickets, online auctions, etc.).

What we tend to forget, though, is that New Economy electronic warriors enjoy better profit-and-loss performance through Web-enhanced marketing and delivery in the first place, so they can benefit disproportionately from commoditized pricing. Easton Consultants of Stamford, Conn., has a software model, the EC Mentor, that projects that online marketing of many products can enjoy a margin of up to two or three times that of physical marketing on sales, general, and administrative costs alone — before Web-optimized production, with delivery and fulfillment impacts figured in! And the new mechanisms for online bartering provide much better margins than fire sales for moving distressed inventories that either vaporize or extend beyond useful product lives.

Moreover, Web-based marketing greatly reduces the cost of acquiring new customers. Here are some persuasive examples:

- **New credit card accounts** typically cost \$90 to \$100 to acquire; Website applications can be processed successfully for less than \$15 (not to mention sparing the lives of countless trees no longer sacrificed for direct mailers).

- **Wal-Mart Stores' Website** was constructed at a cost of a few million dollars, and produces significantly more transactions a day than an average megastore that costs upwards of \$100 million — and the site appeals to disproportionately more upscale consumers who cannot be reached profitably with megastores in their physical neighborhoods.
- **Toyota spent about \$300,000** last year in banner advertising on various sites, generating an estimated 150,000 click-throughs to its site; within six months, more than 7,000 of those click-throughs resulted in Toyota car sales.
- **Microsoft acquired Hotmail** and its free email service to gain access to, and potential transaction flows from, an average of 90,000 new sign-ups a day.

New value is also produced by creating buying communities. This is most apparent in business-to-business sectors, where companies such as Staples, through its contract and commercial division, deliver customized catalogs with customer-preferred supplies and negotiated prices. Buyers benefit from directed use and controlled purchasing; Staples learns buying habits and preferences of key customers. But buying communities in the consumer sector are also appearing, expanding the model of online buying clubs (Cendant) to lifestyle-segmented offerings (Third Age Media), shared community marketing (GeoCities), and community-experience-based shopping (Amazon.com).

The question is: How do electronic warriors retain customers they lock in with their new business-delivery systems? Certainly usage discounts and loyalty programs help. One of the major discount brokers, for example, is offering volume pricing on trading commissions to meet the challenge of online purveyors that have driven the cost of a single trade below \$10. If you transact a lot, nobody beats their pricing; if you don't, you pay more "normal" rates.

The real leverage in one-to-one marketing, however, appears to be in cross-selling — capturing both a bigger proportion of necessary transactions (such as housing, food, transportation, clothing) and discretionary expenditures (certain investments, travel, leisure, entertainment, toys, and so on). For the former, taking pain and aggravation out of procuring necessities with value-added relationship management seems to be the key. Relationship-pipeline providers can afford to mark down prices on the full "shopping basket" and throw in loyalty kickers, thanks to the lower costs of buyer acquisition and retention.

For discretionary purchasers, utilizing information exchange to consummate the impulse purchase is the secret. In Boston's Fenway Park, a 5-year-old cannot see home plate from one-third of the seats; providing field views to prospective ticket buyers will not only please them, they may even be willing to pay for it. Same thing for checking out views from hotel rooms on special travel occasions. Ditto for 360-degree views of the neighborhood from homes for sale. This stuff is offered free today, because it's hard to get to amid the chaos of today's Internet. But packaged into well-targeted content gateways at lifestyle portals (with efficient microbilling or account-charging mechanisms), we should expect to see "lifetime-relationship economics" driving value in the New Economy.

Winners and losers in one-to-one transacting

We already know some of the new sources of value in a real-time marketplace: personalized information exchange, lifestyle brands, one-to-one relationships, balance of protection with convenience, etc. In order to develop and deliver relationship-era values in a post-Information Age, organizations will likely have to form partnerships with other brands (Citicorp and Travelers, for example) in order to forge new value propositions.

In the end, there will be many losers. Change is too rampant and relentless for everyone to be able to learn and adjust. Among the winners, there will be many new players (eight of the top ten brands on AOL have been in business less than three years — companies that didn't have to invest the \$100 million it usually takes to establish a national brand in the United States). It won't seem fair to many. And the dislocations at the human level will require much sorting

out. The work we do will have to be relevant to the values of the New Economy.

For both individuals and organizations, this realization will come all too quickly. As in *The Truman Show*, things that used to go right won't anymore. Things won't look or act the same. We will begin to question what happened in the past, and test the premises on which the past was based. Sooner or later, a decision must be made about whether to escape from the Old Economy into the New. Anything less will make us history's footnotes, instead of its living script.

Mott's Matrix Blueprint for a New Economy

CARS

- People are shopping for exact models and best prices before visiting a dealer
- Intelligent kiosks are now appearing in General Motors and other dealerships to let buyers configure their exact preferences before ordering
- Toyota and others are finding that Internet leads have extraordinary follow-through rates, and are focusing advertising on this channel

Implication: Dealerships become service/distribution outlets rather than sales centers; car salespeople reinvent themselves as "mobile lifestyle advisors."

FOOD

- Internet trading grows wildly in bull market, as investors divert discretionary part of investment portfolio to low-cost, quick-execution services
- Standard research will move to zero pricing but hot advice will attract crowds with spillover, spur-of-the-moment transactions
- Core portfolios (IRAs, annuities, kids' stocks, etc.) become self-manageable

Implication: Brokerages tend to wealth-creation on a macro level; stockbrokers morph into micro-level "wealth builders," similar to the way insurance agents once were.

DELIVERY SERVICES

- Online grocers and meal providers penetrate urban markets based on service proposition
- Undermotivated, slow cashiers and counter jockeys drive digerati, then families, to convenience and time-savings-despite potentially higher costs
- Local delivery mechanisms extend reach from meals to groceries, pharmaceutical items, videos, etc.

Implication: Branded items and localized delivery services flourish in new distribution channel (we hope the clerks don't become drivers...).

STOCKS

- Federal Express and United Parcel Service save 60 to 80 percent of customer service-call costs and improve service by letting customers track packages online
- Both invest in online shipping, tracking, and facilitation services that will expand penetration to new markets

- Both will "wire" themselves into product distribution systems of key ecommerce players (Dell Computer, Wal-Mart, Lands' End, etc.) and become a more prominent part of their customers' value propositions (and expense stream)

Implication: FedEx and UPS morph into hosts for satellite local-delivery businesses; delivery people enter social communities of end-customers.

BANKING

- One-stop-shop online cash-management services for businesses growing
- True electronic transacting (especially bill payment) finally getting off the ground, with substantial pressure to lower fees and other costs
- Innovative banks will use digital "pipeline" entry point to establish branded links to digerati and other preferred customers

Implication: Consolidation will continue as remaining successful retail banks morph into digitally savvy consumer brands; tellers become account reps; small-dollar accounts suffer even more.

TRAVEL

- More than 32 percent of all eligible airline tickets sold in the United States are etickets and the number is expected to rise as more carriers implement eticketing
- Airfares will be bartered/resold online individually more and more
- Flexible work arrangements will make trip planning more negotiable

Implication: New breed of intermediary will replace agencies; surviving travel agents will morph into loyalty-program coordinators and lifestyle-logistics managers.

Beanie Baby Ecosystem

Beanie Babies have done what few toys have managed to achieve. Ty, the Beanie Babies creator, introduced both Web-based marketing and a new model for controlling distribution to create a vibrant, substantial aftermarket. The result will define toy-marketing for the foreseeable future. Here are some of the mechanisms that built the Beanie Babies ecosystem.

- Producing a large number of items — each with a special name tag giving "birth date" and information relevant to collectors. Distribution appeared to be somewhat random and arbitrary, leading to "rare" and highly sought-after items.
- Creating a Website catalog (and franchising related companies and individuals to produce printed versions — including a New York Times Bestseller version) that lists items still in circulation, introduces new items, and shows "retired" items. Once PC-literate families began downloading color printouts of the collection, demand for home color printers soared in other "Beanie Baby homes" as a result of peer pressure.
- Retiring early releases, thereby instantly creating new value for items that may not initially have been popular sales successes.
- Creating a "lifestyle" of related activities and community-building around the brand ("Ty" in a heart) via the Website and franchised aftermarket activities.
- Supporting the proliferation of aftermarket Website communications, which locate hard-to-find items, appeal to online buyers, and announce the discovery of items made more rare (and valuable) by coloring or printing mistakes.

- Benignly allowing more than 200 Web-sites to promote aftermarket. Many of the Websites entice visitors with Beanie Baby promotions in order to cross-sell their more pedestrian collectibles.
- Vehemently enforcing distribution flows, merchandising regulations, and pricing conventions in the primary market, including cutting off product flow for violators. —
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