

How will you go to market in the eEconomy?

Paul F. Nunes

Ajit Kambil

Diane D. Wilson



Institute for
Strategic Change

In nearly every industry, electronic commerce is transforming the go-to-market strategies of companies. In some industries highly integrated channels are exploding into a network of specialized intermediaries who play key new channel roles. In other industries electronic commerce creates new opportunities to create direct channels to customers. How should a company structure its channels for the eEconomy? This paper provides a new framework to guide managerial choice and thinking about channels in the emerging eEconomy. This framework reconceptualizes channels in terms of six information-based intermediary roles, and provides four distinct strategies for managers to reconfigure their channels.

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A company's go-to-market strategy has always depended on its distribution channels—perhaps the most important conduit between customer and shareholder value. Today electronic commerce is disrupting the old industrial-age channels that connect companies to their customer. Channels are exploding into a network of specialized and interconnected intermediaries, and some companies are bypassing many traditional industrial-age intermediaries to directly connect to the customer. Electronic commerce is thus changing the logic and economics of channels.

Consider the airline industry, where distribution costs rank third behind fuel and labor. Today, traditional travel agents are under intense pressure to create new forms of value as new online entrants like Preview Travel, Microsoft's Expedia, and AMR's Travelocity attack their market share. The new online intermediaries can help users find low-price tickets and vacation packages, and even enable them to create their own bookings. They also preserve detailed information about travel history and provide new levels of convenience. The service that cost a travel agent \$40, on average, costs electronic commerce less than a dollar, on average. Yet most of the dominant online travel sites are not owned by traditional travel agencies, or by travel agencies at all. This has caused a significant loss in market share to travel agents who considered, and relied on, travel services being a local neighborhood business. As electronic ticketing expands to make airline travel services almost completely virtual, the role of traditional travel agents will be further diminished. These changes shift more channel power away from traditional travel agents toward both buyers and sellers. Consumers can inexpensively search for the best travel options, and airlines can leverage e-commerce capabilities to negotiate lower rates with traditional agents or go direct to the customer.

In the automotive industry traditional dealers have relinquished new online opportunities to outsiders, or as in the case of Auto-by-Tel, to insiders that were driven out of the business (Pete Ellis, CEO of Auto-by-Tel, is a former auto dealer whose network of 16 dealerships was forced into bankruptcy in 1994). The major online auto sites, like Microsoft's CarPoint, Auto-byTel, and AutoWeb.com, are helping customers evaluate and price the cars they are interested in, and are referring those customers to dealers who then merely close the sale. These online auto sites have also branched out into insurance and servicing support, creating powerful new intermediaries empowering customers in the traditional automobile industry channels. They helped an estimated four million people in the U.S. select and buy a car last year, that

is, 25 percent of all the cars sold.¹ As in the travel industry, customers are becoming more empowered.

In the chemical industry, most of the incumbents have been caught flat-footed by the rash of new entrants creating online market places: Chemdex, ChemConnect, Polymerland, and ChemMatch, to name a few. These new electronic markets have disrupted long-standing channel relationships, some of which have lasted over 80 years. New electronic markets have reduced the procurement costs of buyers by 5-10 percent, prices by 20-30 percent,² and even the delivery costs to suppliers. Electronic markets also make supply and demand more transparent, creating an added benefit for suppliers in predicting demand and efficiently managing inventories. Yet they displace control away from the seller toward new electronic market intermediaries and the consumer.

Will electronic commerce and new intermediaries disrupt your go-to-market strategy? Yes, they almost certainly will. But how will your channels reconfigure? Today, companies are having a hard time understanding how electronic commerce and new intermediaries will transform their dominant channels. We think the answer lies in re-framing channel intermediaries based on a deeper understanding of the information economics that drive these roles.

The Old Channel Logic

Channel intermediaries provide value to both customers and suppliers.³ Consider the traditional channel model with wholesalers/distributors and retailers as intermediaries between the supplier and customer. For the customer, traditional retailers provided:⁴

- Convenient access to products and services that reduced the customer's search costs
- Assortments that offered variety to the customer
- Local inventories that reduced the wait time for products
- Product knowledge and related services that informed, supported, and educated customers about various alternative choices

For the supplier, the wholesaler/distributor and retailer both provided value by:

- Breaking bulk to small unit sizes desirable to customers and creating efficiencies from volume selling for the supplier
- Offloading financial risks by purchasing inventories
- Managing customer knowledge, relationships, and services

to support sales

- Promotion of goods and services to the customer
- Enabling suppliers to focus on their core competencies of designing or manufacturing goods
- Coordinating efficient logistics and the distribution of the good to the customer

The traditional channel roles of the wholesaler/distributor and retailer were typically organized on the following assumptions:

- Shopping convenience requires a physical retail outlet or sales agent as close to the customer as possible
- Shopping variety is best created by bringing diverse products and services physically together at retail outlets (note the emergence and success of category killers such as Toy's R Us)
- Waiting times from purchase to use are best reduced by local stockpiling of goods (e.g., the creation of retail store inventory)
- Customer service and promotion information are best provided by a local sales or service force
- Manufacturers cannot efficiently provide small lot sizes desired by customers

Given these assumptions, and the traditionally high cost of direct communications between the supplier and the customer, wholesaler/distributor and retailer are natural value-adding channel roles. Wholesalers/distributors and retailers create tremendous efficiencies by breaking bulk in each stage of the distribution channel, and leveraging different scale and scope efficiencies.⁵ For example, wholesalers and retailers realize economies of scope from aggregating and servicing multiple products, creating efficiencies and benefits for upstream suppliers and downstream customers. They also realize economies of scale and scope in storage and distribution, creating channel value.

Today, the old logic of channel design is being transformed by new competitive imperatives and information-processing capabilities that provide more information and services to customers. The resulting new logic requires managers to conceptualize the channel organization in terms of new information-based roles.

New Imperatives and New Channel Opportunities

Two major trends in economies with advanced transportation and communications infrastructures undermine the traditional channel logic. The first trend is to greater product customiza-

tion, driven by greater competitive rivalry and changing customer expectations. Except for minor product enhancements and the creation of product assortments, most product customizations are most efficiently handled at the time of production. This undermines traditional distribution intermediaries such as wholesalers and retailers, as direct delivery from producers of customized products is increasingly enabled.

The second major trend is the continuing dramatic improvements in the price performance of computers, communications, and transportation, leading to falling coordination and delivery costs. Earlier improvements in these infrastructures, such as toll free "800" calling and round-the-clock call centers, have diminished the need for a local presence in creating convenience. And third party, rapid response logistics providers such as UPS and FedEx have caused us to rethink our assumption that availability implies local stockpiling. Today, improvements in Internet technologies as an enabling infrastructure for commerce are further altering our assumptions about channel design. Table 1 illustrates how assumptions about the provision of value to the customer are being transformed.

As illustrated in the Table 1, lower communications and transportation costs, and trends to product and service customization, are undermining the traditional assumptions of organizing channels. As information-processing costs fall, channel intermediaries are rushing to manage either the flow of goods and inventories or the flow of information. Increasingly in the new economy, the imperatives of customization and falling coordination costs drive value add from intermediaries who focus on managing the flow of goods toward "infomediaries"⁶ who leverage new technologies to reorganize and manage the flows of information.⁷

The Emerging Channel Model

But what exactly do these new infomediaries look like. After all, "Channel scholars have long recognized that the key value add activities which intermediaries provide do not, and cannot disappear, but are redistributed over time across different players as new technologies and new efficiencies warrant."⁸ The challenge firms face today is determining how the new technologies of electronic commerce, and specifically the Internet, are redistributing activities and defining new players.

Table 1: Buyer Values and Channel Opportunities

Buyer Values	
Old Channel Logic	New Channel Opportunity
Convenience of Access	
Locate close to the customer	Provide 24/7 access anywhere, anytime through the Internet
Varied Product Assortment	
Large retail stores (category killers)	e-Category killers – with hyperlinks to varied offers and infinitely configurable shelf space
Short Wait Times	
Provide retail outlets and upstream warehouses with sufficient inventory stockpiles to fulfill customer needs through third-party logistics	Trade-off speed for cost and efforts <ul style="list-style-type: none"> ■ Use quick shipment through third-party logistics ■ Use electronic networks to deliver digital products instantaneously ■ Leverage better forecasting and improved supply chains to deliver quickly to customers from centralized warehouses
Product Knowledge	
Have sales people provide most product knowledge to users	Have customers pull relevant information, or push product knowledge to customers online
Product Size/Replenishment	
Limited variety	Provide product in the size and quantity desired by the customer through continuous replenishment

Our research suggests the emergence of a new channel model, built around six distinct intermediary roles: buyer agent, seller agent, market maker, context provider, payment enabler, and fulfillment enabler. We expect channel infomediaries to increasingly specialize in these roles, each category creating its own distinctive value in the channel, and each characterized by its own revenue model. These six roles and the activities they comprise, as well as illustrative examples are illustrated in Figure 1.⁹

Below we examine these roles and consider the conditions under which specialized “infomediaries” emerge to fulfill them.

Buyer Agents

Buyer agents create value in four important ways: they help customers assess their needs; they identify suitable offers to fulfill needs; they compare and evaluate offers; and they match a particular offering with the customer in an attempt to get the “best deal” for the customer. In sum, these activities create

greater convenience and better choices for buyers in the purchase process.

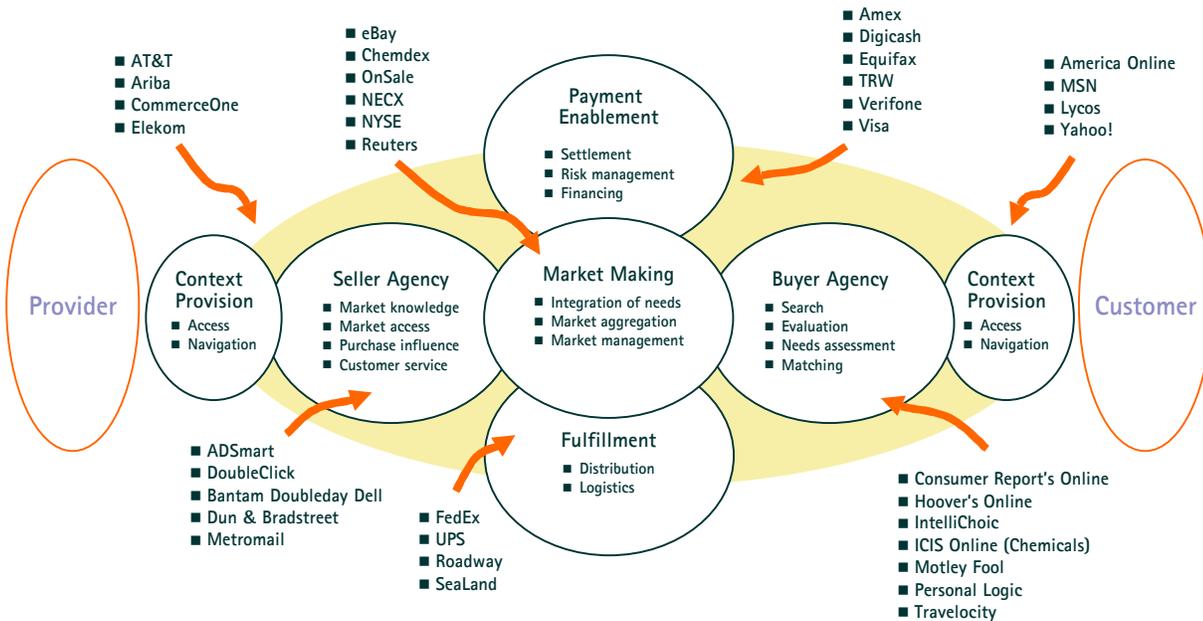
Previously, many buyer-agent roles were undertaken by the customer or seller. Electronic commerce is increasing the value of independent buyer agents by expanding access to buyers and sellers and making the role economically viable. Buyer agents create customer value by reducing the search effort for a product that will meet the customer’s needs at an attractive price. The value of buyer agency grows as the sea of options customers face deepens.

Today, intelligent software agents are creating value by automatically searching out product information and bargains for customers. Smart buyer agents can also check inventories to ensure products are available, reducing the selection and delay risks encountered by the customer. Excite Shopping supports purchasing on the Internet by allowing users to enter descriptions of requested purchases and then searching the Internet for the best vendor fits, returning the information in an easy-to-use format. Similar buying agents are located in Yahoo! Shopping, mySimon, Comparenet, and Bidder’s Edge. PriceSCAN, an online comparison service, has committed itself to independence from seller influence by creating a business model based solely on revenues from advertising and the sale of aggregate information generated in operating the site. This objectivity is critical for providing the best answer, and thus the greatest buyer-agent value, for the customer.

In the automobile industry, Auto-by-Tel, CarPoint, and AutoWeb illustrate how customer search, evaluation, and comparison costs are lowered through online buyer agency. These sites provide detailed information on cars, helping consumers to easily access purchase-related information and to compare alternatives. They also identify potential dealers, from whom they request bids, to help customers find the best deal inexpensively.

Electronic commerce also enables buyer agents to more powerfully assess needs and match customer desires. By increasing the amount of information gathered about individual customers, and across customers, better knowledge is being created about individual customer intent. This knowledge is enabling buyer agents to create more relevant and more customized recommendations and offerings. Today, online buyer agents are developing an understanding of buyer needs and preferences by directly gathering customer opinions through

Figure 1: eCommerce Enabled Electronic Channel System Model



online surveys (see www.epinions.com) and by observing buying behavior and making inferences about preferences through data mining. The latter is mainly done through collaborative filtering, using information about the prior purchases of the user and other customers to predict a customer's likely future preferences. The higher the volume of transactions and the number of participants, the easier it is for companies like Amazon.com to make useful recommendations to customers.

PersonaLogic is a company that provides personalized buying-decision guides that help consumers assess their needs. Customers describe their preferences in a structured online questionnaire, and the PersonaLogic software determines appropriate recommendations from a large repository of stored options. The guides cover topics that range from automobiles to mutual funds, from colleges to pets, and they even allow users to explore and compare options further after initial recommendations have been made. Most importantly, these guides walk consumers through a decision process, helping them to identify and preference the features that matter most, and enabling a highly customized result.

Mercata is a new firm that takes buyer agency even further to help customers get the best deal. It allows consumers to pool their purchasing power and negotiate better deals with suppli-

ers. For example, if you want to buy a Philips videocassette player, Mercata allows the many users who want to buy the same good to pool their purchasing power to get a discounted price. Buyer agency services such as Mercata shift power to the consumer and away from the supplier in the channel.

Most of these early buyer agents have an advertising-based revenue model. As buyer agency evolves further to aggregate buyer power and negotiate good prices we expect the revenue model will include a brokerage fee. But given that online consumers are often indifferent about saving money, even between two well respected brands like Amazon and Barnes&Noble online that are only a click away,¹⁰ buyer agency requires that the customer perceive sufficient value creation for this new "infomediary" role to be economically viable. Thus we expect buyer agents to primarily focus on supporting the purchase of high-value and high-involvement goods.

Seller Agents

The greatest opportunity yet to be fully exploited online may lie in the area of seller services. Seller agents focus on helping producers to effectively present themselves to customers and to the marketplace. They do this by helping producers gain knowledge of the market, gain access to the market-place,

influence customer purchasing through activities such as advertising, and provide customer service.

Opportunities for specialized seller agents are growing, as producers focus on design and production, choosing to outsource customer sales and services online. Seller agency has become increasingly important as electronic commerce has introduced more customers and more marketplaces into the business environment of every industry. This has enabled seller agents to more quickly achieve scale, serving large numbers of producers, and increasing their offering levels in an area that now requires specialized skills.

DoubleClick is one of the most successful Internet seller agents. For sellers, DoubleClick identifies who is the likely viewer of an online advertisement and targets a message to them as part of the web site they are viewing. Other new entrants in seller services include ADSmart, which designs promotion services and supports technologies to manage the buying and selling of Internet advertising. In the pharmaceuticals industry, Professional Detailing is providing improved access to doctors for drug companies that do not have the resources to create their own dedicated sales force. In an industry where innovation is rapid, maintaining this capability in-house is difficult for all but the largest players. Professional Detailing employs over 900 sales representatives who are shared by its clients, which includes six of the top ten pharmaceutical companies. Similarly, INSWeb has created the online equivalent of the independent sales agent in the insurance industry. The independent provision of seller services frees firms in various manufacturing and service industries to focus on their core competencies of developing products to fulfill customer needs.

Success for new seller agents relies on a number of important factors, including:

- Having unique customer knowledge or relationships, otherwise unavailable to the seller, which can support sales (DoubleClick, for example, has detailed data on web-user behaviors and online demographics).
- Enough knowledge of the producer's product and business to effectively represent them.

Adding value to the sales process requires creating greater leverage than the producer has by itself. This can be done through scale, and through established relationships with market makers (e.g., the relationship wholesalers have with retail-

ers). Even in the reduced entry barrier world of the Internet, scale in a chosen market and preferred access will still determine the level of success seller agents achieve.

Market Makers

A third intermediary role is the market maker, electronically matching supply and demand for goods and services dynamically, and discovering prices for exchange. Market making provides aggregation of buyers and sellers, integration of their needs, and active market management, which includes qualification of participants, provision of anonymity where required, quality assurance, conflict resolution, and the provision of real-time market information.

New market makers are arising because the Internet creates new market opportunities by:

- Expanding access to buyers and sellers
- Lowering the costs of making a market, through inexpensive technologies for various market-making functions

This has created opportunities for various new entrants from Band-X, creating a market for telecommunications bandwidth, to Chemdex, creating an online market for chemicals and reagents. There has been an explosion of Net-enabled market makers in almost every industry segment, from electronics components to financial markets, from seafood to utilities, from telecommunications bandwidth to airline tickets, and all the way up to the bric-a-brac of flea markets. Some of these new companies, such as eBay and OnSale, sport enormous multiples and exponential growth. OnSale grew sales from \$140,000 to \$89 million in its first three years of business and now sells over \$200 million dollars annually. The market capitalization of eBay, at \$25 billion dollars, is more than double that of leading bricks-and-mortar retailer Federated Stores, owner of well-known chains like Bloomingdale's and Macy's.

These new companies are combining many approaches to exchange, such as English auctions, reverse auctions, Dutch auctions, real-time trading, electronic Requests For Quotations (RFQs), and more to provide participants a new level of operational and exchange efficiency. These varied market mechanisms are often being aggregated to address a portfolio of customer requirements. For example, Egghead.com, which appears to have successfully made the shift from bricks-and-mortar retailing of software to online selling, is using the phrase "Shop

Three Times Smarter" to describe an online selling approach that combines online superstores with auctions and liquidation selling. This model provides customers three approaches to shopping for the same category of products, creating in essence an "all-in-one" market for these products.¹¹

Success for new market makers relies on a number of important factors, including:

- The ability to generate sufficient market participation to create liquidity. Often a new electronic market requires a substantial subsidy, and failure to quickly achieve a critical mass of users leads to market failure.
- Creating greater value for buyers, sellers, and the intermediaries used by buyers and sellers. The primary value of most market makers is in effectively matching demand to supply and determining a fair price for a good or service through an auction mechanism in contrast to direct negotiations.
- Creating all-in-one markets that combine multiple transactions on the same platform.

Context Providers

While consumers have walked the main streets of towns for centuries as a way to gain access to markets, and have driven to malls for decades to do the same, access to the "market-space" was not readily available to consumers before 1993. This created the need for new firms, now generally referred to as Internet Service Providers, or ISPs, to furnish this access. In addition to these conduits to the market-space, navigation, once provided by roadmaps, became the purview of a second type of context provider: the Internet search engine. Together these context and conduit providers create value for customers by simplifying access, providing information, and creating online spaces where customers can gather, interact, and conduct commerce. Many of the portals, such as Yahoo, America Online, and MSN, fulfill this role, "mall-ing" the Internet in the same way real estate providers create physical malls as meeting places for consumers that provide a context for commerce.

Increasingly, the builders of yesterday's media community, such as Disney and Time Warner, are filling the context-provider role. Disney's Go network was started in December 1998 as a portal for the delivery of content from Disney's media channels: ABC News, ESPN, Family.com, and Mr. Showbiz. At its launch it became the fourth most-visited portal on the Web. Like owners of physical malls, the success of new context

providers depends on the volume of traffic to their sites. This is because they often make revenues from the rental of choice "market-space" and advertising—both of which are dependent on consumer attention and interest. We believe the critical success factors for context providers will depend on the uniqueness, quality, relevance, and ease of use of information provided to customers, and the value generated through community interactions online.

Payment Enablers

Payment enabling is the first role to have moved out from the integrated channel. Forty years ago, even before mainframe computers, payment-support activities moved to specialty providers through the introduction of credit cards. Companies like American Express and bank consortia like Visa and Mastercard have made payment and payment risk management an independently branded activity that today spans almost every industry and every geographic location. And this has occurred not just in consumer spending, but in corporate spending well, as demonstrated by the successful moves these same companies have made into corporate procurement cards, as well as efforts by independents like Citibank and Bank of America, and value-add providers like Cendant and ProCard.

New entrants in online payment have focused primarily on four technology sets for conducting transactions over the Internet: credit cards, digital cash, sales aggregation, and smart cards. Online credit cards are likely to be dominated by the usual players, but digital cash has seen a number of struggling but determined new entrants, including CyberCash, First Virtual, and DigiCash, each of which are aggressively building cash solutions that permit sub-penny transactions and transaction tracking on the Internet. Qpass, Intercoin, and Clickshare have entered the aggregator space, allowing many online charges to show up as a single charge on the customer's credit card. The fourth technology set, "smart cards," allows users to cross between the virtual and physical worlds by loading balances onto chips imbedded in what looks like a credit card. Mondex has been a leader in this technology, holding trials in the United Kingdom, though consumer acceptance has been slow. Electronic commerce has also accelerated the integration of customer and producer risk management activities over the last few years. The rise of the Secure Electronic Transactions (SET) standard, and of large payment platform providers such

as Integration, are ensuring that seamless, robust, and secure electronic payment enablement becomes a reality.

As electronic commerce continues to grow, these new payment specialists must rapidly grow their network memberships to drive efficient scale, or risk being overrun by larger players destined to dominate a market that will likely support only a few top players. In addition, they must successfully manage the transition to online bill presentment and payment, an area of cross-channel value that will likely be won by the first mover to create significant market share.

Fulfillment Providers

Fulfillment providing was the second major group of channel activities to have broadly shifted from vertical integration to an independent channel role. Fulfillment activities include both distribution—the transfer and storage of goods—and the information-based coordination activities which support distribution.

Approximately 20 years ago, with the birth of Federal Express, we began to see fulfillment activities move rapidly to third-party logistics providers. The list of leading providers includes FedEx and UPS, but also companies like Roadway, Ryder, SeaLand, CSX, and, of course, the national post office. The Internet has amplified the power of these companies' leadership positions by enabling them to handle customer inquiries and other aspects of customer service online—reducing their average cost-to-serve and significantly broadening their market reach.

These businesses have grown dramatically. Sales at FedEx have grown from \$5.17 billion in 1989 to \$13.25 billion in 1998, a CAGR over those years of 11.03 percent. Indeed, between 1991 and 1995 the proportion of Fortune 500 manufacturing companies making use of third-party logistics increased from 37 to 60 percent. And we continue to see out-sourcing and specialization in this area today. In the chemicals industry, companies like Ryder and CSX have created new offerings that better manage the challenge of less-than-load shipping, enabling them and their customers to achieve flexible scale across industries.

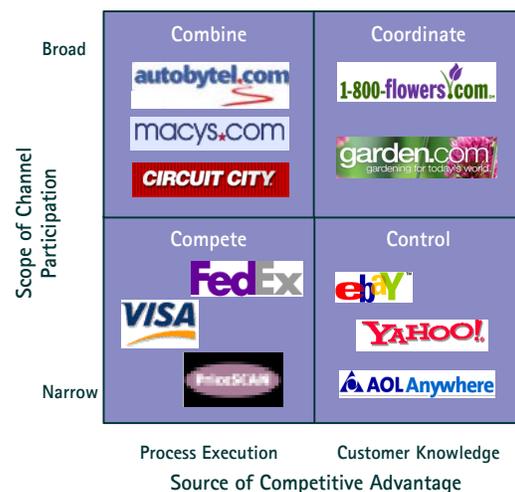
The economics of network externalities supports the continued dominance of market leaders in fulfillment, yet they must continue to innovate or find themselves at risk of being "cherry picked" by new entrants. Many companies are now creating fourth-party logistics services—providers who offer complete

logistics outsourcing to clients through a single interface. By managing the performance of third-party service providers, a "4PL" entity can achieve continuous improvement, with a cost reduction estimated to be at least 20 percent. In two detailed studies, one for a petrochemical company and another for a pharmaceutical firm, cost savings of 26 and 39 percent were reported respectively. Similarly, Pandesic, a joint venture of Intel and SAP, is targeting "supply chain dial tone" services, which may strip value away from distribution specialists by offering a turnkey electronic commerce package that covers all the activities between the storefront and invoicing, including inventory management, warehousing, shipping, and returns.

Four Plays with Infomediaries

How should you go to market in a world with new infomediaries? Our research suggests that companies undertake four distinct channel strategies to prepare for the eEconomy. One choice is to become a specialized infomediary in one of the six roles, and to competitively provide this role across industries. Another option is to specialize in an infomediary role that can enable the company to control the channel. A third choice is to combine multiple infomediary roles under one organization. The fourth choice is for a company to create greater customer value by coordinating best-of-breed specialist intermediaries. Each of these choices requires different types of organizational competence and resource commitments (See Figure 2).

Figure 2



Below we provide illustrative examples of each strategy and identify their critical success factors.

Compete

In this model, companies choose to compete in a specialized intermediary role by developing and sustaining deep competencies in that role. As mentioned, PriceScan is a specialized buyer agent that delivers objective price information across online and off-line markets. Leveraging its core competence at gathering and disseminating pricing information, PriceScan has diversified its services across multiple industries. In the market making role, Priceline is a new specialist that is leveraging its patent on a reverse auction process to compete in market making across airline tickets, automobiles, loans and even groceries.

Competing through specialization is not a new strategy in channel roles. Others deploying this strategy include payment enablers such as Amex, Visa, and Mastercard, and fulfillment providers such as FedEx, UPS, and the Postal Service. Focusing on a particular channel role is particularly appropriate when there are unique assets or process capabilities in that role that can lead to market dominance for the top competitor. For example, success in fulfillment comes from developing a low-cost delivery network through significant investment in capital assets. Market-making excellence comes from flawless and timely execution of electronic transactions. These capabilities are most valuable when exploited to the point of core competency, and ultimately integrated into a network of best-of-breed players.

However, to realize the full value of this strategy, each specialist competitor must parlay their competence across multiple industry channels, gaining economies of scale and scope, while leaving other infomediaries to perform complementary roles. Hence we see Priceline diversifying the application of its reverse auction and other trading models across multiple product and industry categories. To succeed at this strategy, the infomediary must be able to integrate effectively into a network of other specialists and be able to realize economies of scale and scope in role across multiple industries. And, as with Priceline and other similar infomediaries, a distinctive competitive advantage in this role is often predicated on the ownership and implementation of a unique process to fulfill the role. To maintain their advantage, infomediaries who adopt this strategy must continuously improve their processes, rapidly integrating technology innovations, and quickly moving down the learning curve.

Control

In some cases, companies may specialize in a channel intermediary role without achieving superior process efficiencies that can be leveraged into other industries. Yet these companies may be able to leverage their specialized role performance to control the flow of resources in the overall channel. The strategy of controlling the channel is based on a core competence of managing and leveraging relationships in contrast to processes. In certain channel environments, a disproportionate amount of value creation can be captured in roles that enable tight control of key relationships, whether they are with customers or alliance partners. In these channels, it pays to focus on performing the right role, i.e., the role that provides the greatest amount of leverage over relationships in the channel, rather than just role efficiencies.

Today, many firms are hoping and expecting the linchpin role in online channels to be market making. eBay is good example of how a market maker can dominate the channel, in this case for customer-to-customer commerce, not through an inimitable process but through managed relationships. By owning the customer, eBay has been able to run up a fantastic market capitalization as investors have recognized and rewarded what used to be called a natural monopoly. Others attempting similar online control plays in market making include Chemdex in chemical reagents, eSteel for rebar and sheet metal, and the Seafood Exchange for fish. VerticalNets is attempting even greater dominance by aggregating vertical market-making control plays, and includes over 40 industrial sites to date.

But others online entrants and players see context provision, not market making, as the linchpin in their channels. Companies like America Online (AOL) see the customer entry point, or "portal," as the key role that can extract additional value from the channels it enables. By controlling access to a customer base of close to ten percent of all online users, AOL has gained significant influence over both its customers and those who would have access to them. AOL has been able to capture hundreds of millions of dollars of revenue outside their core value proposition of online access by entering into significant partnering relationships with, for example, ABC, the New York Times, and both BarnesandNoble.com and Amazon.com. Its multi-year deal with Tel Save alone garnered them \$100 million of new revenue.

To succeed in controlling the channel, firms must find ways to maintain key relationships by providing superior value or creating switching costs. Portals have done this with some effect by enabling user-customized interfaces, including personalized portfolio lists, news, and weather. Electronic retailers have created high switching costs by capturing customer billing and shipping information in order to provide greater convenience with "one-click" shopping.

When competing in an environment of increasing—not diminishing—returns, market share may be the key to a successful control strategy. The concept of increasing returns is common to many online control plays. Most online companies find themselves with high fixed costs, such as high infrastructure and marketing expenses, but a low variable cost to serve. This unique cost ratio for online plays encourages seeking first mover advantages if one is ever to gain sufficient share to gain control. The second driver of increasing returns is network externalities—when other owners or users make your offering more valuable to new or potential users. Network externalities are particularly valuable for buyer agents, where the knowledge gained from a larger customer base creates greater value to new customers.

But increasing returns can fail, and control can be elusive. An 80-plus percent market share was not enough to save Netscape, a company that for a time seem ready to break the hegemony of Microsoft. Nets.Inc. also seemed to have the right talent, funding, and position, until this early business-to-business market maker ran out of steam shortly after its founding. Even AOL's continued dominance is uncertain in the face of competing technologies like cable-modem Internet player @Home, browser-maker Microsoft, and web portals like Yahoo! Effectively retaining control requires not losing focus on sustained innovation and execution excellence, as well as lock-in and relationship.

Combine

The high cost of transactions in the past made combining different channel roles within an organization the dominant strategy. Traditional wholesalers, retailers, and manufacturer direct-sales forces combined channel roles for many reasons,¹² but largely to simplify customer processes and to provide high-service levels in their channel. While there are strong forces for specialization, combining roles remains a

viable strategic option under many industry and market conditions, particularly when customers prefer the channel to deliver a complete bundle of value.¹³

Companies that choose to combine roles focus on the effective delivery of total-customer solutions, not on the execution of single role. This desire to address the customer's needs at specific quality and service levels not economically feasible by coordinating specialized intermediaries drives these companies to combine roles required to deliver the value proposition. Even much ballyhooed virtual-channel player Amazon.com benefits by combining market making and buyer agency, and though thwarted in its attempt to buy distributor Ingram, it has recently found it necessary to invest in physical warehouses to reduce the delivery time of its books to certain areas of the country.¹⁴

Another motivation to combine roles is to exploit cross-subsidies for competitive advantage. Cross-subsidies enable companies to give away the value in one activity in order to secure greater margins or value in another activity. Cross-subsidies, which are endemic in most industries, can increase the customer's perceived value and often make customers feel they have gotten something for nothing. While less effective in the eEconomy, cross subsidies remain in online selling. NECX.com provides free buyer agency by showing customers, if they desire, the best prices available from its competitors. It will even graph the differences, including lower prices elsewhere, all in the belief that customers will in the end prefer its total package.

All this suggests the need to give serious consideration to combining, even in a world that is being blown to bits. Ultimately, success in combining roles is realized from extracting synergies across roles, and from creating greater customer value in the combination of activities than in independent ownership and execution of roles.

Coordinate

Another strategic option is coordinating channel roles, creating value for customers and channel participants by dynamically and virtually integrating multiple channel roles. This strategy builds on the coordinator's understanding of the customer's total needs and its knowledge of providers who can supply variety in channel functions. While today's heightened level of channel transparency is allowing customers to choose their component providers in some channels, a trusted third

party can still significantly reduce the costs of coordinating multiple interactions with specialized service providers.

Coordination is a particularly strong strategy where there are many undifferentiated infomediary competitors, inter-firm cooperation is low, or variety is required in the channel. Catalog retailers have understood this strategy for years. By allowing customers to select the shipper and payment provider in a transaction, as well as the level of service and cost desired from each, customers received new levels of value and choice. Today, catalog and other direct-marketing companies are leveraging new Internet-based capabilities to better integrate the services of multiple specialist infomediaries. Customers in effect dynamically configure the channel out of multiple specialized competitors, creating not a hybrid marketing system¹⁵ of shared components, but a networked channel that operates and reconfigures in real time. In addition to the shipper and credit provider, they increasingly select online the context in which they wish to participate, the company that will inform their purchase decision, and the market in which the transaction should occur.

Similarly, 1-800-Flowers has leveraged information technology to become the buyer agent of choice for long-distance flower and gift delivery. They have succeeded by creating a network of over 2500 allied independent agents, market makers, and fulfillment providers, and by leveraging new payment capabilities to handle the necessary internal-transfer payments to make the whole thing hold together. Garden.com applies the same strategy to link over 40 grower/suppliers, and a large number of fulfillment and payment partners, to their online base of customers with an interest in gardening.

Another approach to coordinating the channel is to assign roles to specific sole-source providers to form a keiretsu-like buying solution, as in the case of IBM's e-Chemicals solution. This newly formed channel uses select specialized partners in each role: Yellow Freight is the partnering fulfillment provider and SunTrust Banks, Inc. is the payment enabler, with IBM and e-Chemicals playing the role of market maker. By leveraging its strong brand and information-management capabilities across channel roles, IBM is able to garner a larger share of the channel rents than if it were simply to participate.

Successful coordination typically requires a direct interface to the customer through which the firm is able to gather superi-

or customer insight. It also requires the capacity to integrate multiple specialized (and best-of-breed) providers dynamically to provide channel value. The latter requires efficient information-management capabilities across channel roles.

Compete, Control, Combine, or Coordinate – How Will You Go To Market?

How should you make your fortune in the middle kingdom? As electronic channel systems are in their infancy, we see companies successfully undertaking each of the above strategies within an industry.

For example, consider the changing nature of the dealership in the automobile industry. Traditional auto dealers combine multiple channel roles under the same roof. They inform, they sell, they finance, and they deliver. This solution-based value proposition, however, is being diminished as the Internet enables new infomediaries to emerge. These emerging infomediaries illustrate all of the remaining strategies. For example, infomediaries like Edmund's compete in the buyer-agency role, providing pricing, feature, and other information to the customer. Their core competence lies in the processes of accumulating, organizing, and publishing data about cars that is of interest to buyers. While they influence buyer-decision processes and negotiations with dealers, they do not involve themselves in the overall transaction beyond their key area of focus.

In contrast, companies like Auto-by-Tel illustrate the control strategy. Auto-by-Tel has expanded beyond providing basic information to delivering qualified customer leads to partner dealerships under exclusive contract. This attempt to control the flow of information between dealers and customers provides them with greater revenue opportunities than just publishing information. Its exclusive contracts are also difficult for others to replicate.

CarsDirect illustrates the strategy of coordinating multiple specialists and roles. As specialized infomediaries emerge, we expect smart firms will increasingly want to provide a total solution by dynamically coordinating the most desirable infomediaries to solve a customer's problem. Hence, we expect traditional car firms to reinvent their channels by establishing or becoming the coordinator of best-of-breed specialists that vary in geographic and other attributes.

So how should you go to market in the eEconomy? As discussed earlier and illustrated in Figure 2, the source of competitive advantage in the compete and combine strategies are based on process and location advantage. Unless processes are protected as business methods by patents (e.g, Priceline's reverse auction or Amazon's one-click buying), they are replicated across competitors. Thus process-execution advantages diminish over time due to the technology improvements available to all competitors. In contrast, the relational assets and the unique people and organization of the "infomediary" are the more inimitable resource, thus providing the greater competitive advantage.¹⁶ The exclusive knowledge of customer preferences enabled by online customer interactions, and the exclusive relations with channel providers, will enable control and coordinate strategies to dominate other strategies.¹⁷ Customer knowledge will especially allow companies to provide customers with total solutions to increase convenience. We believe customer knowledge and channel relationships are harder to acquire and maintain than process knowledge. Thus we believe that, in the automobile example, Auto-by-Tel's and CarsDirect's strategies have superior advantages to compete and combine strategies.

As in the car industry, firms can go to market with any of the four distinct strategies outlined above. The initial channel strategy will most likely be based on the existing experience and channel competencies of the firm (e.g, Edmunds' moving from paper publishing to electronic publishing). However, over time we expect those firms who want to dominate their channel to migrate to control and coordination strategies. To do this firms must invest in customer insights and relationships that provide them with the information and good will to control/dominate channel behavior across roles. To gain insights all firms will have to either invest in establishing direct contact with customers or own an infomediary that has extensive customer relations and insight. Today, all major car companies host a website informing customers and coordinating transactions with dealers as a first step to direct interactions with customers and the gathering of customer knowledge. At the same time, some major players like Ford are positioning to take ownership of infomediarities like Carpoint, which have access to customer queries about cars across multiple vendors and are able to coordinate a number of different infomediarities in the automotive channel. We believe that manufacturers, like Ford, will increasingly invest in customer insight to execute a control or coordination strategy in their channels.

Conclusions

As illustrated above, electronic commerce is undermining the old channel logic, leading to a greater specialization of channel infomediarities. This creates many new opportunities for both incumbents and new entrants to make fortunes in the middle kingdom between buyers and sellers. As channels evolve, we believe companies will have to choose an infomediary strategy of compete, combine, control, or coordinate. While companies profit from each strategy, our analysis suggests that the control and coordinate strategies will ultimately dominate.

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About the Authors

Paul F. Nunes has been with Accenture for twelve years, most recently as an Associate Partner in the Institute for Strategic Change. His research focuses on new and shifting roles for channel intermediaries, electronic markets, new IT-enabled business models, and the particular challenges large organizations face in confronting electronic commerce. He has published articles on electronic commerce issues in Accenture's *Outlook* magazine, *Computerworld* and *Wired*. Paul may be reached at (617) 454-5379 or paul.f.nunes@accenture.com.

Ajit Kambil is an Associate Partner and Senior Research Fellow at the Institute for Strategic Change. His research focuses on how electronic commerce transforms competition and enables new market structures, channels, and pricing for physical and intangible goods. He has published business and technical articles on electronic commerce issues in *Sloan Management Review*, *Communications of the ACM*, *Management Science*, *Information Systems Research*, and the *Journal of the American Society of Information Science*. Ajit may be reached at (617) 454-8672 or ajit.kambil@accenture.com.

Diane D. Wilson is a Partner in the Information & echnology Strategy practice of Accenture, with a research and consulting focus on electronic commerce. Her research and consulting focuses on the strategic implications of electronic commerce. She has published articles in Strategic Information Technology Management, *Computerworld*, and the *Journal of Economics of Innovation and New Technology*. Diane may be reached at (617) 454-4704 or diane.d.wilson@accenture.com.

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