FAQ: E-Commerce Model and Strategy Formulation

**Question 1:** What type of e-commerce is the most dominant, and why?

**Answer 1:** Though the popular press has focused heavily on B2C e-commerce in recent years, the real story has actually been B2B e-commerce. The widespread acceptance of the Internet as a business platform has given organizations new mechanisms for reducing their costs, improving productivity, and streamlining their internal as well as interorganizational business processes. The terms *intranet* and *extranet* entered the business lexicon, referring to the application of Internet technologies and standards to business processes within and without the organization, respectively. Surveys of global economic commercial activity invariably indicate that the B2B space is many times larger—in terms of transaction volume, dollar volume of transactions, or any other measure—than the B2C space.

**Question 2:** What types of activities are included under the umbrella term B2B?

**Answer 2:** Business-to-business e-commerce covers a broad spectrum of applications that enable an enterprise or business to form electronic relationships with their distributors, resellers, suppliers, and other partners. Turban, Lee, King, & Chung (2000) explain the scope of B2B in the following manner:

As Handfield and Nichols (1999) suggest, B2B applications will offer enterprises access to the following sorts of information:

- **Product:** specifications, prices, and sales history
- **Customer:** sales history and forecast
- **Supplier:** product line and lead times, sales terms and conditions
- **Product process:** capacities, commitments, and product plans
- **Transportation:** carriers, lead times, and costs
- **Inventory:** inventory levels, carrying costs, and locations
- **Supply chain alliance:** key contacts, partners' roles and responsibilities, and schedules
- **Competitor:** benchmarking, competitive product offerings, and market share
- **Sales and marketing:** point of sale (POS) and promotions
- **Supply chain process and performance:** process descriptions, performance measures, quality, delivery time, and customer satisfaction

As a result, by using B2B e-commerce businesses can reengineer their supply chain and partnership.

**Question 3:** What are the key elements of an e-commerce business model?
Answer 3: Kenneth Laudon and Carol Guercio Traver (2004) state that "if you hope to develop a successful business model in any arena, not just e-commerce, you must make sure that the model effectively addresses . . . eight elements: value proposition, revenue model, market opportunity, competitive environment, competitive advantage, market strategy, organizational development, and management team" (p. 61). The following describes how these authors define these elements (Laudon & Traver, 2004):

- **Value proposition:** A value proposition defines how a company’s product or service fulfills the needs of customers (Kambil, Ginsberg, & Bloch, 1998). To develop or analyze a value proposition, you need to answer the following key questions: Why will customers choose to do business with your firm instead of another company? What will your firm provide that other firms do not and cannot? From the consumer point of view, successful e-commerce value propositions include personalization and customization of product offerings, reduction of product search costs, reductions of price discovery costs, and facilitation of transactions by managing product delivery (Kambil, 1997; Bakos, 1998) (p. 62).

- **Revenue model:** A firm’s revenue model describes how the firm will earn revenue, generate profits, and produce a superior return on invested capital. To be considered successful, a firm must produce returns greater than alternative investments. Firms that fail this test go out of existence. Although there are many different e-commerce revenue models that have been developed, most companies rely on one, or some combination, of the following major revenue models: the advertising model, the subscription model, the transaction fee model, the sales model, and the affiliate model (p. 63).

- **Market opportunity:** The term market opportunity refers to the company’s intended market space and the overall potential financial opportunities available to the firm in that market space. The realistic market opportunity is defined by the revenue potential in each of the market niches where the company hopes to compete (p. 65).

- **Competitive environment:** A firm’s competitive environment refers to the other companies selling similar products and operating in the same market space. It also refers to the presence of substitute products, potential new entrants into the market, as well as the power of customers and suppliers over a business. Firms typically have both direct and indirect competitors (p. 66).

- **Competitive advantage:** Firms achieve a competitive advantage when they can produce a superior product or bring the product to market at a lower price than most, or all, of their competitors (p. 67).

- **Market strategy:** Market strategy is the plan that firms put together that details exactly how they intend to enter a new market and attract new customers (p. 69).

- **Organizational development:** Companies that hope to grow and thrive need to have a plan for organizational development that describes how the company will organize the work that needs to be accomplished (p. 70).

- **Management team:** Arguably, the single most important element of a business model is the management team responsible for making the model work. A
strong management team gives a model instant credibility to outside investors, immediate market-specific knowledge, and experience in implementing business plans (p. 70).

**Question 4:** What is e-commerce strategy formulation?

**Answer 4:** Strategy formulation is the development of business objectives and strategic plans for the successful management of the opportunities and threats represented by the competitive arena and the environmental landscape, in light of the organization’s strengths and weaknesses (Turban et al., 2000). Typical approaches to strategy would therefore include the standard SWOT (strengths, weaknesses, opportunities, and threats) analysis. Turban et al. (2000) continue as follows:

[I]t includes examining or redefining the corporate or project mission by specifying achievable objectives, developing strategies, and setting implementation guidelines for e-commerce. It should be noted that [this] can be done in several ways . . . an electronic commerce initiative may include such projects as creating a storefront, extranet, or an electronic mall. [In other words,] strategy formulation is relevant for both e-commerce initiatives in general and for individual e-commerce projects.

**Question 5:** What are the critical success factors for e-commerce?

**Answer 5:** Ghosh (1998) suggested a set of questions a company can ask that consider how e-commerce can benefit its customers. Specifically, he suggests that managers examine a series of questions for clarifying value chain statements and for creating new values.

**Value Chain Statements**

- Can I realize significant margins by consolidating parts of the value chain for my customers?
- Can I create significant value for customers by reducing the number of entities they have to deal with in the value chain?
- What additional skills do I need to develop to take over the functions of others in my value chain?
- Will I be at a competitive disadvantage if someone else moves first to consolidate the value chain?

**Creating New Values**

- Can I offer additional information regarding transaction services to my existing customer base?
- Can I address the needs of a new customer segment by repackaging my current information assets or by creating new business propositions using the Internet?
- Can I use the ability to attract customers to generate new sources of revenue,
such as advertising or sales of complementary products?

- Will my current business be significantly harmed by other companies providing some of the value I currently offer on an à la carte basis?

Question 8: What is vertical integration?

Answer 8: According to transaction cost economics, vertical integration solves production problems related to communications, coordination, and control, but at the cost of the increased overhead needed to arrange production organizationally.

Vertical integration leads to efficient and effective coordination through a number of mechanisms that include increased likelihood of physical proximity, established patterns of communication, and greater willingness to cooperate with other members of the same group. It seems plausible that technology could be used in similar ways by treating partners as if they were inside the organization in terms of access to information and the degree to which they are or are not treated adversarially. The prospect of improved control over the actions of suppliers is another rationale often used for vertical integration. Unintegrated partners can exert power over each other as transactions unfold over time. By vertically integrating—combining the supplier and the customers into the same organization—the problem of holdup is eliminated because both report to the same authority at the same level of the hierarchy. Information technology might provide mechanisms for more closely monitoring the actions of partners, but strict monitoring regimes are also not usually associated with trustful information sharing in the long run. In short, vertical integration, like any strategy, can be used in e-commerce only when it matches organizational goals and when the benefits exceed the costs.

References


