What Went Wrong with B2B?

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Introduction

The failure of B2B companies is garnering almost as much press as the failure of B2C companies did a year earlier. As late as last summer, financial research reports touted the ability of the B2B companies to survive and excel in a troubled financial market. Since that time, high-flying B2B companies have lost as much or more value than their B2C cousins. How could this happen?

The Failure of On-line Marketplaces and Trading Hubs

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B2B companies are not all alike. Some have created and manage Web-based trading hubs, some manage MRO (Maintenance, Repair, and Operations) and some supply software for managing portals and Web-based catalogs. Since the Web was virgin territory, many of the entrepreneurs who started these companies thought they would address the simple problems first. After all, in the era of quickly assembled dot com companies why go through the pain of dealing with legacy COBOL applications when you can create innovative new solutions from Web components?

The problem with that approach is that money is to be made by solving the difficult problems, not by presenting new approaches that have not stood the test of time. The concept of the trading hub, where suppliers publish catalogs, buyers issue requests for quotes and support materials are auctioned, was based on the idea of "perfect information" or "transparency."

In business transactions comprised of perfect information there is no transaction friction; all information is freely available. In theory this environment minimizes purchasing overhead costs. However, companies cannot realize these benefits without increased communication and most companies are loath to share information about their internal operations, especially with competitors.

Just because these approaches and solutions are inherently problematic, does not mean that e-commerce will not work. In fact there are huge opportunities to apply technology to improve the purchasing process that remain under-developed.

In the end, these failures are the failures of specific companies, not the failure of e-commerce or the web.

Assumptions that went wrong:

So, what went wrong? Let's look at four assumptions that lead these early B2B approaches to failure.

Solve The Easy Problems First

Purchases made by any corporation can be divided into two kinds: direct material and indirect material. Sometimes direct material purchases are also called productive purchases and indirect material purchases are called non-productive. Direct material purchases involve raw material that goes directly into the company's product. Indirect material purchases are for supporting material that does not go into the product, for example stationary. Improving the indirect material purchasing process is an easier problem than improving the direct purchasing process. Why? Because indirect materials are not critical to the corporation and savings are typically unexpected surprises. Ariba is an example of a company that is based on this assumption.

"Direct material purchases involve contractual relationships. Indirect material purchases are based on casual relationships."

The problem with this assumption is that corporations place most of their focus and resources in activities involving direct material purchases, but direct material purchases are managed by legacy systems that are inherently difficult to upgrade. Direct material purchases involve contractual relationships. Indirect material purchases are based on casual relationships.

IBM Buys A Lot Of Pens

Big companies buy lots of simple stuff. IBM buys a lot of pens, GM buys a lot of name tags, and Sears buys a lot of light bulbs. Hence, the assumption goes, saving IBM one cent on every pen they buy can save IBM millions of dollars a year.

In tough times, corporations have many ways available to extract savings in indirect materials purchases including, most importantly, simply buying less. However, every penny IBM saves on components that go into its computers, every penny GM saves on steel that goes into its cars, and every penny Sears saves on products it resells to its customers is a savings that can not be acquired by simply buying less. You can provide significant value to a corporation if you save costs associated with critical purchases that cannot be postponed.

If You Build It, They Will Come

Many B2B companies thought that if they built it, the customer would come. What they were not prepared for was that these

trading hubs and on-line marketplaces required a sales force and long sales cycles, much like off-line products. Simply owning a domain name like www.cheapsteelhub.com does not bring you business. (I was actually told by an entrepreneur that he would be successful because he owned a large collection of such domain names!)

There Is No Business Language, So Invent It

This assumption was completely false. The assumption was that every business has built up proprietary forms and communication mechanisms with its suppliers and, hence, a standard purchase order, invoice, shipping notice, etc., does not exist. E-commerce groups would try to develop their version of the generic purchase order, either for a specific industry or for all industries. Examples are Rosetta Net, cXML, and xCBL. It turns out that the development of each of these new generic business documents takes a long time and integrating these representations into existing customer purchasing systems is also increasingly time consuming.

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There is a language of business documents that has been around for dozens of years. It is widely used by big business and is general enough to represent business documents from manufactured goods companies, service companies and government organizations. The language is Electronic Data Interchange or EDI. There are two standards bodies managing these documents: X12 for the US and EDIFACT for Europe. The point-to-point nature of EDI does limit it. However, the Internet provides a mechanism to break the point-to-point nature of EDI. EDI carries pure data, but Internet savvy representations of EDI, such as XEDI, add in metadata. By directly interfacing with EDI systems e-commerce can be quickly implemented at large companies.

Where to Make Big Money in Big Business

It is clear what big business needs to reduce procurement costs and streamline its operations. It needs to make its direct material purchases more visible to management, easier to manage and cheaper. The addition and management of trading partners must be simplified. The time it takes to purchase an item or send an invoice or send a shipping notice needs to be reduced.

This last business factor is important not just because things should be made faster, but because delays in purchasing, invoicing and shipping cause expensive inventories to accumulate. By controlling the time it takes to execute these processes and controlling the distribution of the documents involved, collaboration between multiple suppliers becomes possible. An order for a large quantity of steel can automatically send out orders for metallurgical analysis services, notices to transportation services, and bank requests for letters of credit.

It is predicted that within a few years we will see a large corporation report quarterly earnings before the end of the

quarter. For a corporation to be that nimble, it must be able to execute control over its supply chain and its material procurement management.

Despite the missteps of B2B companies, there is still a bright future for e-commerce. B2B technology companies need to remain focused on adding true value to their customers by solving problems involved in their most critical activities and purchases. Other efficiencies created by the Internet will follow, but as the lackluster impact of B2B e-commerce has shown, big money is in solving the difficult problems.

About The Author

David Jakopac is Vice President of Lisle Technology Partners, LLC, a consultancy specializing in strategy and software services for advanced technology start-up companies. David was a founder of three start-up companies, one of which went public. At LisleTech, David is involved in strategic start-up development, software technology design and management, and venture capital due diligence. David had designed and managed the implementation of software technologies for start-up clients in the areas of XML translators, call record processing for Telco billing, business strategy execution tools, logistics systems interfaces, 3D web-based visualization of new home construction options, and on-line 3D racing and skateboarding games. Some of David's technology developments have resulted in patent applications. David has also performed technical due diligence for several private investors and venture capital firms on companies in the following markets: web-based stock purchasing and portfolio management, Enterprise Application Integration, and Business-to-Business Integration. David holds Ph.D. and M.S. degrees in Computer Science and Electrical Engineering from Northwestern University, and a B.S. in Computer Science from the University of Florida.

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