Competitive Strategies in the Internet Era
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The development of the Internet is one of the factors causing most turbulence within companies. It has been said many times that the accelerated rhythm of change which the Internet has brought has caused those traditional tools which used to be useful when formulating competitive strategies to become obsolete.

It is stated that we can no longer make structural analyses of the new business models, such as the B2B portals, which the extension of the net has made possible. Equally, it is argued that the classic financial focus, based on the updating of cash flow, is no longer useful when valuating new companies with high technological content. In this article I am going to develop the contrary theory, arguing that the traditional cash flow tools are still valid even though the relative importance of each instrument has indeed changed.

The generic mission of companies is still the creation of wealth for the shareholder, and this can only be achieved through future cash flows which contribute present positive net value when discounting the opportunity cost of the resources. But what is now truer than ever is that anticipated cash flows should not be determined using past data. One thing we know for sure is that the Internet is creating a new unprecedented order. Hence we must think of solutions which offer continuity.

The future cash flows of a company depend on four variables: the structure of the sector, positioning, sustainability and flexibility.

The structure of the sector is important because each business has a different profit potential. The classic tool for analysing the said potential has been called the analysis of the five forces: entry barriers, power of negotiation by suppliers and customers, existence of substitutes and level of competitive rivalry. This focus is still valid with two small inclusions: the inclusion of the compliments and the analysis of the so-called network externalities.

It must be remembered that in the new world which information technology is creating, some products are "complementary", in other words, demand for one of them stimulates demand for the other and vice versa. A good example are computer applications. Without them the PC sector would not have experienced a boom over the last ten years. Another phenomenon which is key to studying the economic structure of Internet based businesses are the so-called "network externalities", also known as external or network effects. These "externalities" come about when the use which one consumer derives from the consumption of a good increases in line with the total number of consumers of the same. Bill Gates made full use of this principle when turning Windows into the de facto standard for use in the PC sector. With the incorporation of these two additions, the structural analysis is not only still valid but is more necessary than ever before.

Something similar can be said of the analysis of positioning: for a company, whether it is an Internet company or not, what is really important is the distance which separates it
from its competitors, especially when the network externalities create a dynamic of the "winner takes all" kind.

In the Internet world the basic principle of analysis of sustainability is as important as ever. In other words, high returns on investment are usually short lived unless the company has been able to develop obstacles to avoid imitation by competitors. The empirical evidence is overwhelmingly: for the vast majority of companies, high profits tend to decrease after five years or less. But in my conceptual outline, the most interesting factor for the Internet world is the one which appears in fourth and final position: flexibility. Indeed some believe that this is the only important factor.

In a world as quickly changing as the Internet, the only competitive advantage would be the capacity to continuously adapt to new environments. I do not believe this is so: a competitive strategy still requires persistence in a stable position. What is indeed true is that the need to combine a sustained undertaking with agile tactical movements is more necessary than ever. Here a sports metaphor regarding judo is sometimes used. In this sport, the most important ability is to know how to use the existing resources in such a way as to turn the opponent's strengths back on him. In many traditional sectors the competitive game is based on a sport with opposing characteristics: sumo wrestling. In this sport, what counts most is the weight and brute strength of each opponent. The video rental sector is illustrative of the contrast between judo and sumo wrestling as a way to compete.

Throughout the 1980s many small traders entered into this business attracted by the high levels of growth in the sector, which became greater and greater as domestic videocassette recorders became more widespread. The profits obtained, however, were rather more modest. Once again it was shown that the growth of a sector does not in itself bring about the desired structures. The entry barriers were low and, consequently, so were the levels of profit. At the end of the eighties a different competitor, Blockbuster Video, appeared in the video rental business.

This company put into practice one of the best ways we know to create economic value: to identify a fragmented sector with still unrealised potential economies of scale, to put them into practice and to consolidate the sector. The founder of Blockbuster Video also identified some clear weaknesses in the traditional establishments: an unwelcoming atmosphere and a lack of tapes of recent blockbuster films. Blockbuster Video decided to target family customers. One of its first decisions was to not include a section of erotic films and to create an attractive atmosphere in its establishments through careful interior and exterior design. Moreover, they decided to offer a wide range of the most recent "hits", so reducing the chances of a customer being unable to rent the film he came for. Finally its large size gave it greater negotiating powers and so it was able to obtain better conditions from the suppliers of video material.

Blockbuster's basic strategy perfectly illustrates what we called the "sumo wrestling" focus. Its large size and financial clout were too much for the small traders who had occupied the sector up until then. Not long ago, a serious competitor to Blockbuster Video appeared in New York: a company known as Kozmo. Its strategy is based on a lucid diagnosis of the leader's weaknesses. Blockbuster Video can offer a wide range of recent films, but its offer of
what we could call "classic films" is relatively small, something which is disappointing to film buffs. Kozmo, on the other hand, boasts that it offers ten times more films than Blockbuster. But the essential element of its strategy is its home delivery and collection. The only condition is that the order is made over the Internet. If the customer is willing to do so, Kozmo guarantees home delivery of the tape in less than one hour as of the moment the order is made.

What is the secret behind Kozmo's competitive strategy? Firstly, it avoids the high rental costs which Blockbuster pays for its premises. The tapes are stored at premises in a neglected area, which involves much less cost.

On the other hand, the logistical system is based on a large number of youngsters using bicycles or mopeds to swiftly distribute the tapes, just as if they were delivering pizzas. Home delivery is more convenient since parking near Blockbuster establishments is often difficult. Moreover, by processing the orders over the Internet, considerable cost savings can be made. And to complete its offer, Kozmo can also deliver popcorn, soft drinks and hot dogs along with film, should the customer so wish.

Kozmo's strategy is a clear example of the "judo" focus. By changing the rules of the game, Kozmo has created a system of activities which Blockbuster will have difficulty replying to. This company has its hands tied given its high investment in establishments in privileged locations. Its "strength" has become its principle obstacle to counter-attacking Kozmo. It is not easy for them to go back on what they have done. On the other hand, Kozmo's strategy is clearly better than Blockbuster's with regards to the management of a critical factor for many clients: time.

More and more people are realising that time is one of the scarcest resources and is one of the most difficult to reproduce, something which makes it especially valuable. One Spanish company which is an expert in judo is Bankinter. It is a medium-sized bank whose corporative vision is that of "leading change" in the Spanish banking sector. For this reason it has always developed strategies based on things the large banks cannot or are unwilling to do. In the 87-88 period it developed a product known as "special deposit", which had the best price on the market and whose secret was based on the fact that the large banks would not wish to copy it for fear of the negative effects of cannibalism on the assets in their balance sheets.

On 11th September 1989 the Banco Santander launched its own "Super Account", so turning the judo match into a sumo-wrestling match. Banco Santander not only wanted to compete in the price, but it also launched a massive advertising campaign which, given the necessary economies of scale, was impossible for a medium-sized bank to respond to.

A few years later Bankinter decided to go on the attack again by offering a telephone deposit with a rate of interest of 16%. Here they believed the large banks would not dare to counter-attack given the threat which the generalisation of telephone banking represented for its branch network. Again, the judo expert Bankinter centred on the large banks' fears of cannibalism. The strategy worked well for some time until Banco Santander converted the judo match into a sumo-wrestling match by launching Open Bank.
The appearance of the Internet in the Spanish banking sector has allowed Bankinter a new chance to practise judo with its competitors. It could be argued that this time the large banks have counter-attacked quickly: both the BBVA and the BSCH. But this time they have gambled on more than just competitive strategy: now they wish to achieve a change of mentality which the large banks cannot imitate.

For the moment the capital markets appear to go along with Bankinter. To recap: in the Internet world the classic tools are still valid but we need to place special emphasis on flexibility in keeping with a judo competitor.