Opportunities for Action in Consumer Markets

Strategic E-Triage: Identifying Essential E-Business Initiatives

THE BOSTON CONSULTING GROUP

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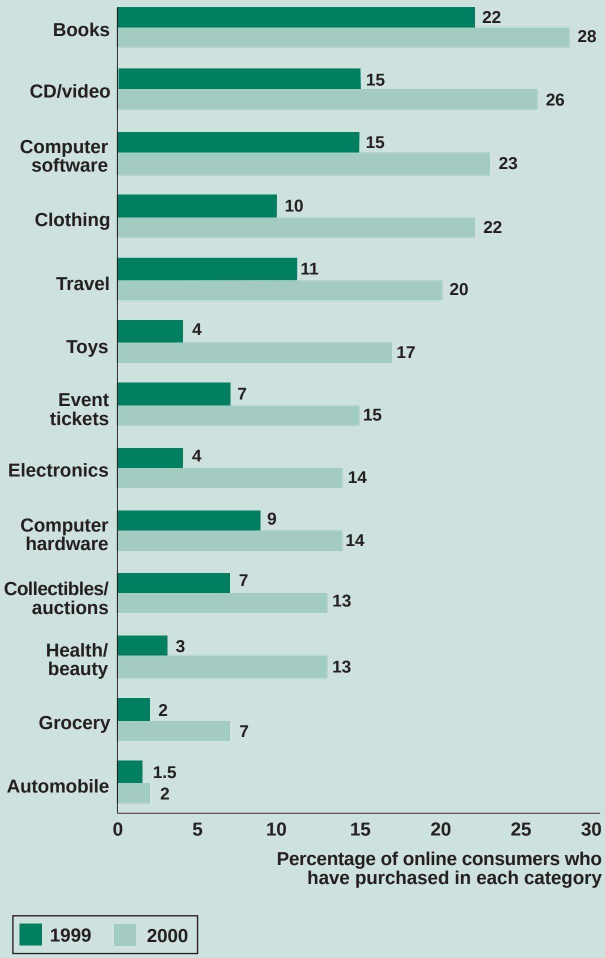
> E-business has been overhyped. Wise companies will cut budgeted investments sharply.
>
> E-business will transform relationships between companies and their customers, suppliers, and employees. It will revolutionize competition.

Which of these statements do you believe? Probably, like us, you think both are true. That's what makes setting the direction for e-businesses so difficult. In an effort to slash expenses and boost profitability, consumer companies are writing off many of the e-business initiatives they approved during the past three years. Usually, however, they embark on this exercise without a clear sense of which projects to kill and which to keep. As a result, most companies will overreact and cut too deeply.

The Boston Consulting Group's work with clients confirms that many companies can prudently reduce e-business expenses by as much as half. That's not to say that some of their remaining initiatives don't offer real opportunities. To give a new twist to the old proverb "All that glitters is not gold": All that is "e" is not dead.

Indeed, consumers have widely adopted the Internet as a vehicle to seek information about various products. They use search engines with ease and are increasingly turning to the Internet for books, music, computers, software, and travel. (See Exhibit 1.) Online purchases in 2001 reached nearly $60 billion—up from $44.5 billion in 2000.

Exhibit 1. Online Buying Has Increased in All Categories



SOURCE: BCG proprietary online panel, 1999 and 2000.

NOTE: The total number of respondents was 1,958 for 1999 and 1,869 for 2000.

In our client work, we've found that almost every consumer company has two or three e-business projects that are well worth continued investment. If managers can integrate those projects into core processes, they can generate significant incremental profits. Here are some examples of companies that did just that:

- Low-cost airlines have further extended their advantage by obliterating their distribution costs. In Europe, companies such as easyJet have built a cost advantage of several hundred basis points over traditional airlines through their low-cost Internet-based booking systems.

- Procter & Gamble has learned how to use the Web to cut its advertising costs. It developed a site for dentists and offered them an 800 number to build critical mass for its Whitestrips tooth whitener before launching it in retail stores. The success with early adopters encouraged the company to launch the product with minimal advertising. The experiment paid off: after just six weeks, Whitestrips hit its sales target for the entire year.

- BMW leveraged the Internet to increase brand awareness among targeted high-income consumers. During the past year, several million people visited bmwfilms.com to see a series of edgy short movies, spending an average of 11 minutes at the site. A television advertising campaign drawing equal exposure would have cost $20 million to $25 million more than BMW spent on the site.

- A grocery retailer used its frequent-shopper transaction data to better target its promotional offers and saved 1 percent of sales.

- Both Kraft Foods and Campbell Soup Company built valuable relationships with their heavy users through permission-based marketing of recipes and tips on the Internet.

- Unilever estimates that its e-business will deliver revenue and cost benefits equal to 2 percent of sales.

Some of these initiatives push profits up in the short term but are quickly copied by competitors. Others create genuine, sustainable advantage, and those are the ones that will change the competitive landscape over the next decade. But managers face a ticklish problem. It takes a while for shifts in advantage to show up in relative profitability, particularly since innovators tend to invest heavily in growth, making their profitability appear artificially low in the early years. That being the case, how can managers pursue the short-term opportunity to reduce costs in e-business activities without destroying necessary investments to sustain and build longer-term competitive advantage? Both agendas are valid and must be acted on. Yet in a world of simplistic sound bites, it's all too easy to lose sight of the subtle complexity of a company's real needs.

In our work with consumer companies, we have seen enormous benefit accrue to those that use a strategic e-triage approach to evaluating e-business investments. The process is straightforward and entails the three steps described below.

Step 1. Audit All E-Business Initiatives

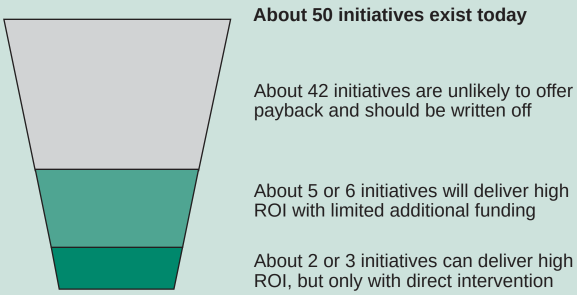
The first step is to compile a detailed inventory of every e-business project in the company. That means gathering such information as who is in charge of each project, what resources are involved, the original rationale for investment, and the results to date.

Once a company begins this process, it usually discovers many more initiatives than it expected to find, some without even a rudimentary business case. Project proliferation often happens in companies that operate through geographic subsidiaries—with each region likely to have its own initiatives—as well as in companies that have separate “czars” for business-to-business, business-to-consumer, and business-to-employee projects. Most companies find that they have 30 to 75 initiatives. The goal is to end up with a focused list of no more than 10. (See Exhibit 2.)

Step 2. Estimate the Opportunity for Each Initiative

Before the list can be winnowed, the business potential of each initiative must be assessed. We recommend linking each project to specific business processes, such as supply chain management. This pegs the project to concrete, measurable objectives—revenue growth, cost reduction, or efficiency improve-

Exhibit 2. E-Triage Reduces Initiatives to a Handful



SOURCE: BCG analysis.

ments—and provides it with a clear "owner" to judge it. (See Exhibit 3.) Then you can work with the owner to understand the expected financial impact. For many initiatives, benchmarks and pilot results are available to evaluate business cases, and if tailored to the specific environment, they can help generate good estimates. Working with the line manager responsible for an area or process should also reduce double-counting or undue optimism.

Beyond the direct financial expectations, you also need to assess whether the initiative will have an impact on competitive advantage. Is there a first-mover advantage? Is there a chance to lock in key suppliers or customers and raise switching costs? Is there scale to be exploited? Could you create capabilities that are hard to replicate? Is the advantage sustainable or is it easy to copy?

Exhibit 3. Link Each E-Business Initiative to Measurable Objectives

E-Business Initiative	Measurable Objectives
E-procurement	Reduction in direct-materials costs and purchasing transaction costs
Collaborative planning, forecasting, and replenishment	Reduction in inventory carrying costs and stockouts
Collaborative new-product development	Increase in the number of innovative projects and in speed to market for new products
Customer relationship management	Increase in cross-selling (measured by average purchase or number of categories purchased) and customer retention
Knowledge management	Increase in employee satisfaction and retention; decrease in the amount of time it takes to resolve a customer's problem
Employee benefits	Decrease in the amount of time it takes for employees to change addresses and update benefits

Source: BCG experience.

Step 3. Develop a Framework for Setting Priorities

Once a company has identified all its e-business initiatives and assessed their potential, it is ready to develop a framework for deciding which projects are worth continuing and under what conditions. Of course, projects that generate high returns would warrant top priority and, perhaps, further investment. Indeed, one of the main benefits of cutting investment elsewhere is often the opportunity to increase it here.

Projects that are likely to generate high returns but offer little competitive advantage might assume the follower's position, adopting the best tactics of competitors as quickly as possible. That makes it easier to bring a tested system in-house and limits the drain on scarce internal resources. It also helps strengthen a company's skills at being an effective fast follower.

If the initiative creates a lot of advantage but depresses short-term returns, that is a real tradeoff. Is there a way to explain the advantage to investors? Is there a way to cut costs by working with an outside partner—without losing the advantage? If there is no way around the tradeoff, then it's advisable to fund only the best of such opportunities and carefully manage the complex tradeoffs they present.

Exhibit 4 shows one framework that BCG uses with many different kinds of companies to help them prioritize their e-business initiatives. A packaged-goods manufacturer, for instance, placed e-procurement in its first-priority quadrant because low costs were critical to its market position. It worked closely with FreeMarkets' auction system to reduce the cost of its direct materials by a staggering 8 percent. It also established customized interfaces with many of its suppliers to trim 15 percent from the transaction costs of purchasing.

Another manufacturer, whose products tend to be impulse purchases, put collaborative planning, forecasting, and replenishment (CPFR) in its first quadrant and immediately began to exchange information with its key retailers to reduce stockouts. That provided a 20 percent sales lift. But, unlike the first manufacturer, it gave e-procurement second priority because it was content to move more slowly in that area. Consequently, it worked with established systems on its noncommodity inputs and refrained from committing IT resources to customized solutions. Nevertheless, it captured an incremental 2 percent savings on its direct-materials costs—enough to remain competitive in that area.

Exhibit 4. Setting Priorities for E-Business Initiatives

High ROI	**Priority 2** Be a fast follower in these initiatives—no customized solutions	**Priority 1** Invest in these initiatives, even if they require customization
Low ROI	**Priority 4** Stop all activity on these initiatives and reallocate resources	**Priority 3** Reduce costs (consolidate into global effort, work with partners)
	Low alignment with strategy/does not create advantage	**High alignment with strategy/creates advantage**

SOURCE: BCG experience.

Interestingly, initiatives that ended up in the fourth quadrant—whether the client was a service company, retailer, or manufacturer—often turned out to be driven by the IT department, with little or no strategic input from the business units. Because our matrix is grounded in a company's individual strategy and supported with hard data, it permits a clear and precise view of where crucial resources could be freed up from low-priority initiatives and moved to higher-priority ones.

To conduct a quick audit of your e-business initiatives, consider the following questions:

- How many e-business initiatives are really operating inside our company?

- How many of them are supported by a business case and an estimated return on investment?

- Do we know which initiatives are critical for competitive advantage and which could be fast followers? Are our IT resources aligned accordingly?

- Does each initiative have a senior owner? Is that owner working to integrate the initiative into our core business processes?

- Does senior management receive updates on progress every quarter?

- Do we routinely stop initiatives that offer little in returns or competitive advantage?

The Role of Top Management

Periods of change are always the most exciting time to be a senior manager. And the most dangerous. In the last few years, we have gone from regarding the Internet with skepticism to a period of unbridled optimism and then to skepticism again. Yet despite this emotional roller coaster, the technology continues to advance day by day, year by year. Many of us will get caught up in the exciting swings because they create fascinating stories. But the more important story is the long-term silent shift in advantage.

For senior managers, now is the time to make those difficult tradeoffs between the short term and the long term, and to allocate the company's resources to create advantage. Like so many strategic issues, e-triage is worth the time and effort because the short-term ups and downs of the stock market and the shifting views of the media are often very poor guides.

Katrina Helmkamp
Neil Monnery

Katrina Helmkamp is a vice president in the Chicago office of The Boston Consulting Group. Neil Monnery is a senior vice president in the firm's London office.

You may contact the authors by e-mail at:
helmkamp.katrina@bcg.com
monnery.neil@bcg.com

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