

**TRANSFORMING BUSINESS IN THE
MARKETSPACE: STRATEGIC MARKETING
AND CUSTOMER RELATIONSHIPS**

by

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Transforming Business in the Marketplace: Strategic Marketing and Customer Relationships

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Abstract

This paper presents an analysis of how the business models of organizations are getting transformed in the Marketplace created by the Internet and WWW. We use a model comprising the four P's - Product, Price, Promotion and Placement - and one C - Customer Relationship. We study how these four P's and one C are being transformed by the fundamental characteristics of real-time interactivity and global connectivity in the Marketplace. Our conclusions are drawn from the results of a recent survey of 167 organizations chosen from a number of sectors across the globe. We observe that few organizations are exploiting the unique business potential of the Marketplace. Most organizations are simply transporting limited aspects of their current business models into the Marketplace.

Transforming Business in the Marketplace

Pioneer organizations are today using the Internet to adapt, and in some cases revolutionize, their business models and create innovative forms of customer relationships [1,2,4,5,6,7,8,12]. For instance, consider Security First Network Bank (SFNB) - the first FDIC insured Internet bank. While SFNB has one branch (for regulatory requirements), it has a dramatically distinct lower cost structure as compared to traditional banks. Traditional retail banking has been built on the fundamental premise of bricks and mortar - branches which exist in communities and to which customers go for different services. SFNB is able to offer a radically different concept of a bank: a virtual bank, a bank which is open 24 hours a day, which is available within the comfort of a customer's home (or office) and is able to offer distinctly competitive products and services. All these are possible primarily due to the new electronic paradigm of the Marketplace created by the Internet and WWW [10].

The role of customers is also getting transformed in the Marketplace. A radical, new customer self-service model is emerging. Consider the example of stock trading by individual investors. The traditional model has long been based on a trading firm having direct access to current stock market activity data and extensive historical data about company and industry performance. Individual customers approached these firms for all information and advice regarding stock trades. The business has been filled with commissions, fees and other expenses which went to pay for the time of analysts, portfolio managers and other experts. Today in the Marketplace, information is widely and (frequently) freely available to all. Individual customers can act, if they choose to, as the analyst, the portfolio manager and the broker. Through Web-based firms such as E*Trade, anyone with an extra \$1000 to invest and the right inclination can take charge of his own investment choices. While E*Trade is an example of a Web-based company, traditional companies, such as

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Charles Schwab, are aggressively transforming their strategies and operations to take advantage of the Marketplace.

The above trends are significant because recent studies (e.g., CommerceNet/Nielsen Media Research Survey [3]) show a near doubling in the commercial use of the Internet over the last year. The Internet is becoming increasingly mainstream with a more diverse and non-professional group of active users.

The focus of this paper is on studying the impact of the Internet on the strategic business models of organizations and on evaluating the degree to which these ideas are in evidence in companies today. The emphasis is on business-to-consumer commerce rather than business-to-business relationships (see [11] for a discussion of Internet-based EDI). Towards these goals, the paper is structured as follows. The next section presents an overview of the level of commercial presence in the Marketplace identified in our survey. The following section outlines a 'Marketplace model' which is used as the basis for this research. The next sections describe the results from a study based on the Marketplace model conducted in February 1997 (see box insert for details of the study). The concluding section summarizes the key findings from this study.

Box Insert about here

Establishing a Commercial Presence in the Marketplace

Most of the surveyed organizations have initiated a commercial presence in the Marketplace. Figure 1 depicts the extent and perceived effectiveness of the Marketplace presence of the surveyed firms. The extent dimension ranges from a rudimentary presence (1) to a full fledged commercial presence (7). The effectiveness dimension ranges from poor (1) to excellent (7). While 'effectiveness' in our context is subjective, it reflects an aggregate consumer-oriented perspective.

Figure 1 about here

There are several interesting trends in Figure 1. More than half of all organizations have established a fairly extensive presence in the Marketplace. About 15% of the firms are pioneers who are using their Web sites for conducting extensive electronic commerce. These pioneer organizations range from new Web-based virtual companies such as E*Trade who conduct almost all their business in the Marketplace to more established companies such as Charles Schwab who have embraced the capabilities of the electronic medium whole-heartedly.

For example, E*Trade offers about a dozen different types of accounts on-line and allows customers to buy and sell on-line OTC and listed stocks and options and indexed options. Due to its Web-based nature, E*Trade is able to offer impressive degrees of customization and competitive rates to its customers. Customers are able to create individual portfolios and scan them through a customized home page. Pricing is simple and very competitive. For example, customers pay only \$14.95 for listed market orders and \$19.95 for Nasdaq orders below 5000 shares. This is less than a third of what a customer would typically have to pay with a traditional trading service!

About one third of the evaluated organizations have only rudimentary facilities for electronic commerce. This might be of some concern to these organizations since they may soon find themselves at a strategic disadvantage in the rapidly evolving Marketplace.

Figure 1 also shows that the Marketplace presence of about half of all the organizations is not very effective. Some organizations are seemingly treating the Marketplace as primarily a one-way medium. For example, Adidas's Web site provides no way to get in touch with the organization through the Web. There are no phone numbers, no email addresses, except for the Webmaster who

does not even work at Adidas! A call to the Adidas' US headquarters revealed that they do not accept emails from outside the company. This speaks volumes for the willingness of the company to build customer relationships in the Marketplace!

Other organizations are simply extending their paper-based communication mechanisms on-line and missing the commercial potential of the Marketplace. For example, Hoechst views its Marketplace presence largely as a corporate communication tool and not as a commercial tool. Hoechst does not have any product information on its site and neither attempts to learn about visitors to its Web site nor engage them in any meaningful manner.

About half of the surveyed organizations have effective Web sites as perceived by visitors to their sites. They have succeeded in building Marketplace sites which are open and inviting to visitors, present relevant information to potential customers and allow customers to conduct all or partial commercial transactions on-line. This is supported by recent data [3] which show that an increasingly large number of people are using the Marketplace to collect product information and make purchase decisions.

The Marketplace Model

The model underlying the study consists of two perspectives: a technology perspective and a business perspective as depicted graphically in Figure 2. The technology perspective includes two fundamental characteristics of the Internet and the WWW:

- **Interactivity:** due to the real-time on-line nature of the Internet, relationships between organizations and customers are becoming more interactive in the Marketplace. This is enhancing the richness of customer relationships and creating new paradigms of product design and customer service; and
- **Connectivity:** the open and global nature of the Internet is fostering the creation of a shared global Marketplace. The radical increase in connectivity enabled by the Internet is giving rise to new communication and co-ordination mechanisms both across organizations and customers, and also within groups of customers themselves.

Figure 2 about here

The business perspective includes the four P's [9] - Product², Price, Promotion and Placement (or Distribution) and one C - Customer Relationships. The technology perspectives of increased interactivity and connectivity are having a fundamental impact on the business perspectives - the nature of the 'four P's and one C' - in the Marketplace. The following sections describe these impacts in more detail.

Technological Sophistication

The technological sophistication of the surveyed Web sites was evaluated along four dimensions:

- The information content of the sites - ranging from limited information (1) to extensive business information (7);
- The ease of navigation of the site - ranging from difficult (1) to easy (7);
- The visual appeal of the site - ranging from poor (1) to attractive (7); and
- The technical performance of the site - ranging from slow (1) to fast (7).

² We shall use the term 'Product' in this paper to refer to both products (tangible and intangible) and services.

The results of our study are summarized in Figure 3. Most companies are doing relatively well along the above dimensions, and this reflects both ongoing improvements in Web-technology and the focus of efforts within most organizations to build visually appealing, easy to search and informative Web sites.

Figure 3 about here

Catalogs, annual reports and FAQs (frequently asked questions) are the most commonly used methods for presenting information (each of them being used by about 40% of the surveyed firms). Other methods which were used by fewer organizations included electronic magazines, try and buy options (for digital products such as software) and membership clubs. A Table of Contents is the most popular mechanism among firms (75%³) to help visitors navigate their Web sites. About half of the surveyed organizations employed one or more of the following mechanisms: Forward/Back buttons, Hot Links and a Site Map. Search Engines were also used by 39% of the surveyed organizations. While the use of simple graphics was relatively common (63%), 3-D virtual environments (7%), video clips (17%) and animation (26%) were found to be used much less by the surveyed firms. While the technical performance was deemed as satisfactory for the majority of the surveyed firms, few sites offered either non-graphical versions (9%) or the choice between high and low resolution graphics (22%).

Product

The transformation of products in the Marketspace was evaluated along three dimensions:

- The availability of product related information online - ranging from limited information (1) to detailed information about the complete product line (7);
- The level of customization of products for individual or groups of customers - ranging from no/low customization (1) to a high degree of customization (7); and
- The degree of participation of customers in the specification and design of products - ranging from no/low participation (1) to a high degree of participation (7).

Figure 4a summarizes our findings. Products are increasingly being moved on-line, starting with usually detailed product information and in some cases, including the ability to customize products on-line to individual customers. For example, Bank of America allows Home Banking through its Web site. Customers can access their bank account, get information on current balances, and perform transactions such as pay bills and transfer funds across accounts. A particularly innovative service offered by Bank of America on its Web site is called 'Build your own Bank'. The bank allows for customers to customize the nature and type of banking services and information which they desire.

Figure 4a about here

While the move towards on-line versions of products is natural for banking and other 'soft' sectors, similar trends are underway in traditional 'hard' sectors also. For example, Nokia's Web site is a sprawling network of inter-linked screens and even ties in with country and language-specific versions for seven countries around the world. Even though Nokia is unable to physically sell its products on-line, the site does an excellent job of presenting information on its entire product line. Each item is listed in detail on various lists, each of which is linked to a product page that provides precise specifications and features, as well as information on compatibility with other

³ For ease of presentation, we often quote percentage numbers within brackets. These numbers are to be interpreted as the proportion of the surveyed firms having implemented the item under discussion.

products and accessories. The site even allows users to try out different designer colors on virtual product models and engages users in a 'mobile phone story' contest.

While product information is increasingly being moved on-line, a large majority of the organizations are yet to provide extensive and detailed on-line product-related information. Electronic catalogs (36%), brochures (38%) and FAQs (33%) are each used by only about one third of the surveyed organizations to present product-related information. Figure 4a also shows that organizations have yet to take advantage of the Marketspace to either customize their products or involve customers in the design and development of products.

In some instances, the electronic medium of the Marketspace is transforming the fundamental nature of products, and causing dramatic shifts in the manner in which they are priced, promoted and distributed to customers. For example, the information content of traditional 'hard' products is increasing. Images and specifications of traditional 'hardware' components such as doors and windows are now stored in 'soft' digital formats and distributed electronically by organizations such as Autodesk to architects and designers. In the near future, Autodesk envisions on-line libraries of such 'soft' representations which can be purchased in real-time, in individual elements and on demand by customers.

Promotion

The Internet is having an impact on the way organizations provide promotional information to customers. Beside the usual advantages of being an anytime and anywhere medium, the Marketspace also allows for increased interactivity and customization of promotional information. Our study evaluated the transformation of Promotion in the Marketspace along the following dimensions:

- The extent of use of on-line advertising - ranging from negligible (1) to extensive (7);
 - The use of on-line promotions such as sales and discounts - ranging from low (1) to extensive (7);
 - The level of customization of on-line promotions - ranging from low (1) to high (7);
 - The level of participation of customers in on-line promotions - ranging from low (1) to high (7);
- and
- The extent of links with other organizations in organizing on-line promotions - ranging from low (1) to extensive (7)

The results of our study are summarized in Figure 4b. Several organizations have started to use the Marketspace for advertisements and to send promotional information to customers. For example, American Airlines' Web site has a 'What's New' section which promotes exotic destinations and special fares. Their Net SAAvers program offers registered customers with weekly Email on discount flights. CompuServe's online advertising includes banner ads, newsgroups, yellow pages and special events. On-line promotions such as free trials (ten hours for the first month) and contests (to win a war) are used to attract customers to the company.

Figure 4b about here

Our study shows that the most popular advertising mechanisms used are: What's New (47%), New Products (44%), Special Events (42%) and Banner Advertisements (32%). A smaller proportion of organizations use Online Malls (11%), News Groups (19%) and Yellow Pages (13%). Contests (19%), Samples (18%) and Sales (17%) are the most common promotional mechanisms used. Coupons (2%) and Frequent Buyer (5%) promotions are used by a much smaller proportion of organizations.

The interactivity of the Internet is also slowly leading to the creation of a new genre of participative promotions. For example, Cybergold is creating interactive games for customers to try out certain products of the company. At the end of the game, customers are asked to take a quiz which tests the degree of effectiveness of the advertisement (such as retention quality). If the customer passes the quiz, he is given a prize.

About a third of the surveyed companies attempt to customize their on-line promotion. Some possible ways to customize the advertising content, based on customer profile or input, include changing the content description (simple or complex), displaying only a range of products which are relevant to the particular customer, changing the price (e.g. discount for club members), allowing for new functionality in some cases (e.g. coupon available only under certain conditions), or changing the path used to navigate in the service. For example, Yahoo! provides customized pages along with focused advertisements for specific demographics and groups, such as *Yahooligans* for children, *The Beatrice Guide* for women, *Get Local* for specific regional groups and even *My Yahoo!* for specific individuals. From our study we note that customization for groups (19%) is more popular than customization for individuals (12%).

The connectivity of the Internet allows for innovative forms of promotional links across organizations. For example, Yahoo's *Yahoo To Go!* service allows external organizations to simply put a Yahoo! button on their Web site and provide an automatic and easy link to Yahoo's resources. Cross-linking of sites for promotional purposes is becoming increasingly popular in the Marketplace. About 20% of the surveyed organizations offer promotional links to other firms.

Price

Organizations are now using the Marketplace to customize a product's characteristics to the needs of specific customers and to customize their pricing strategies for specific customer profiles. The more an organization is able to learn about specific customers and their habits, the greater the degree to which it can customize the price charged for its services and products. For example, when a reader buys a newspaper, he typically pays a 'price' for the entire contents of the paper. The typical reader is not interested in all that a newspaper contains. Suppose that our hypothetical reader is only interested in the Sports and Business sections. Further, assume that the newspaper is available in an on-line version (as is today true for most major publications). Then the capability of the Internet can be used to allow this reader to buy and pay for only those elements of information which interests him. This is precisely what the Wall Street Journal is offering its customers today.

Further, a publishing house typically collects more information than it is able to print in a particular edition of the paper. If the publishing organization knows that our hypothetical reader is very interested in Sports, it can make more detailed information on Sports available to him on-line at a fee. The end result is that the customer is happier and the organization also benefits from the arrangement.

The increased interactivity possible with the Internet also opens up new avenues for pricing. As a customer engages in real-time interactions with organizations, it is conceivable for customers to negotiate prices directly with organizations. In fact, these negotiations can extend across a set of customers. For example, airlines such as Cathay Pacific and American Airlines now auction tickets over the Internet. Customers are invited to submit electronic bids for tickets and an electronic clearing mechanism decides which customer obtains which ticket at what price.

The study evaluated the transformation of pricing strategies in the Marketplace along four dimensions:

- The degree of customization of prices to customers - ranging from no/low customization (1) to extensive customization (7);

- The degree to which prices are varied dynamically in real-time - ranging from no/low variation (1) to extensive variation (7);
- The degree of on-line price negotiation possible - ranging from no/low negotiation possibility (1) to extensive negotiation scope (7); and
- The possibility to charge customers for only proportions of products/services consumed - ranging from no/low possibility (1) to extensive facilities for metered pricing (7). -

The results are summarized in Figure 4c. It is evident that pricing is an area where most organizations have done very little beside simply displaying prices on-line. Only about 17% of the surveyed organizations asked customers to register - a necessary first step before any customization of pricing can be done. Most organizations seem to have no idea of who visits their Marketspace sites and for what reason. Dynamic price variations are being done by a small group of organizations, primarily through the use of auctions (4%) and discounts (10%). Only about one percent of all surveyed firms use any form of metered pricing or employ micro-payments or offer price negotiation.

Figure 4c about here

Placement

The World Wide Web can be used as a distribution channel in the following ways:

- Physical products, also sold in conventional stores, which can be advertised, described and/or ordered on-line (e.g., computer hardware, wine); and
- Products which can additionally be delivered over the electronic commerce medium, such as information, music or software.

Examples of the first type are electronic catalogs such as the Internet Shopping Network, selling all sorts of electronic and computer related goods; and Virtual Vineyards, selling wine and food products. These catalogs offer information on the products, support on-line ordering and payment, and sometimes online customer service. These services are of particular value in markets where information is of significant added value to the products being bought. For instance, in the wine industry, information on the winery, the type and quality of the wine, or the food it goes well with are of significant value to customers, and usually hard to get through the traditional sales channel (e.g. supermarkets, liquor stores, etc.) Consolidating this information digitally and making it available interactively with the product is therefore of significant value for customers.

In the case of information products, the electronic commerce medium actually becomes the delivery medium. As such, an electronic newspaper does not use paper anymore and can be fully delivered in digital format. In some cases, (for instance ZDNet, a service reporting on the computer industry), there is actually no paper version of the service. In another case, software.net, a company selling software, currently sells more than 300 packages which can be delivered digitally over the Internet and can be used right after buying them.

The study evaluated the transformation of placement strategies in the Marketspace along four dimensions:

- The extent to which the site distributes its products on-line - ranging from low (1) to high (7);
- The availability of one-line order processing - ranging from no/low (1) to complete (7);
- The availability of secured on-line payment - ranging from no/low (1) to complete (7); and
- The extent of involvement of partner organizations in on-line distribution - ranging from some involvement (1) to extensive involvement (7).

Figure 4d summarizes our findings along the above four dimensions. About a quarter of the surveyed organizations are distributing a substantial part of their products via the Internet. Most surveyed organizations in sectors such as software and publishing with 'digital' products are distributing products via file downloads (27%). Some firms are also providing on-line service through Interactive responses (19%). On-line order processing and secured payment are not provided by the vast majority of firms. Order forms (13%) and shopping carts (7%) are available in only a small number of sites. Credit cards (12%) is the most common form of payment, with very few organizations opting for other forms of payment such as Ecash or Cybercash. Third party distributors such as Federal Express and UPS are used by about 57% of the surveyed firms. About a quarter of the surveyed firms distribute their products in conjunction with other organizations - links across sites (27%) is the most common way to do this.

Figure 4d about here

Customer Relationships

The transformation of customer relationships in the Marketplace was studied along the following dimensions:

- The provision of on-line customer service - ranging from some (1) to extensive (7);
- The identification and tracking of customers to provided customized services - ranging from some (1) to extensive (7);
- The provision of on-line forums for customers - ranging from no/some (1) to extensive (7); and
- The solicitation of on-line feedback from customers - ranging from limited (1) to extensive (7).

Figure 4e summarizes the results of our study. About a third of the surveyed organizations provide significant on-line customer service and solicit on-line feedback from customers. The most common methods for the provision of customer service are e-mails (45%), inquiry forms (32%) and FAQ (21%). Emails (52%) and feedback forms (23%) are also used relatively widely to solicit on-line feedback from customers. About a quarter of the firms appear to be identifying and tracking customers. Registration forms (38%) and cookies (11%) are the most common techniques being employed to do this.

Figure 4e about here

The ability to provide on-line answers to problems, through resolution guides, archives of commonly encountered problems, electronic mail interaction, and all that 24 hours a day, 365 days a year, builds customer confidence and retention. Monitoring how customers use this support information also provides insights on improvement areas in current products and help in the design of new products. For example, Amazon.com, an electronic bookstore on the Web, allows its customers to program agents to send them relevant information. Suppose you are looking for a book on technology and strategy, Amazon will provide you with a list of the existing books, but also offers to keep your request in mind, and send you information on newly published titles as they arrive. This information is sent through electronic mail and links with the online bookstore.

Only about 15% of organizations are making serious attempts to build on-line forums and/or links across customers and thus exploit the connectivity inherent in the Marketplace. Mailing lists (10%) and Chat rooms (9%) are commonly used by these organizations. For example, BlackSun includes on its site, a model of the Atlanta Braves' stadium where fans can 'talk' to other fans and participate in contests to win prizes. Another unique feature was a virtual treasure hunt, the 1996 CyberRoute contest, in which customers had to explore six cities in the United States. BlackSun keeps track of customer profiles by requiring them to register while participating in various on-line,

interactive games and forums. Firefly is another interesting organization that attempts to link customers with similar tastes and interests.

Conclusion

This study is unique in the respect that it explicitly focuses on evaluating the degree to which organizations are transforming their business models in the Marketplace.

The overall finding is that most organizations are simply taking their existing business models and transporting them to the Marketplace with different degrees of effectiveness. Few organizations are seriously evaluating (as much as can be concluded from the way they interact with customers today) the transformational impact of the Marketplace on their current business models. Most firms seem to be content to view the Internet as an extension of the telephone - simply 'yet another' channel. Firms which do not realize the paradigm shift inherent in the Marketplace may lose their competitive edge in the next years.

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Box Inset

Design of Study

Based on the Marketspace model, a questionnaire with 34 questions was designed to explore how the technology perspective of increased interactivity and connectivity were having a fundamental impact on the business perspective - the nature of the "four P's and one C". Most questions required a response on a seven point scale with one and seven indicating low and high levels of achievement respectively along the dimension addressed by the question.

The Marketspace questionnaire was pre-tested and evaluated by independent observers. The actual study of the organisations was conducted in Feb. '97 by 230 1st year MBA students at the Haas School of Business, University of California at Berkeley. Students self-selected themselves into groups of four or five members and chose companies based on their interests from an initial list of about 400 organisations. The list of organisations was formed largely from lists of major corporations compiled by Fortune, the Financial Times and Asiaweek. Also included were the recent CommerceNet Award Nominees for innovative web-sites.

In total, one hundred and sixty seven organizations were evaluated. A geographical distribution of the surveyed organizations is as follows: North America (53%), Western Europe (25%) and Asia Pacific (22%). A sectoral split of the evaluated firms is as follows: Airlines and transportation (11%), Chemicals and Pharmaceuticals (6%), Electronics and computers (13%), Financial services (17%), Media and publishing (9%), Retail and wholesale (7%), Software and services (14%), Telecommunications and utilities (4%) and Traditional manufacturing (19%)

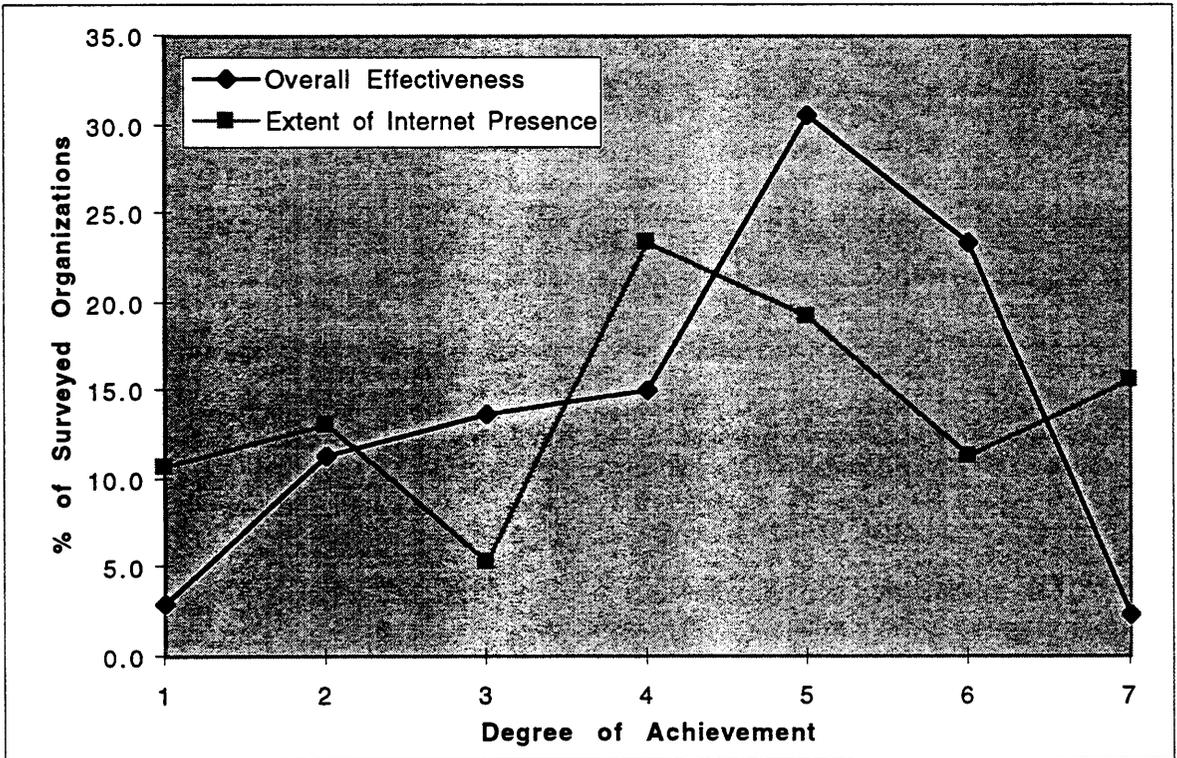


Figure 1: Extent of presence and degree of effectiveness

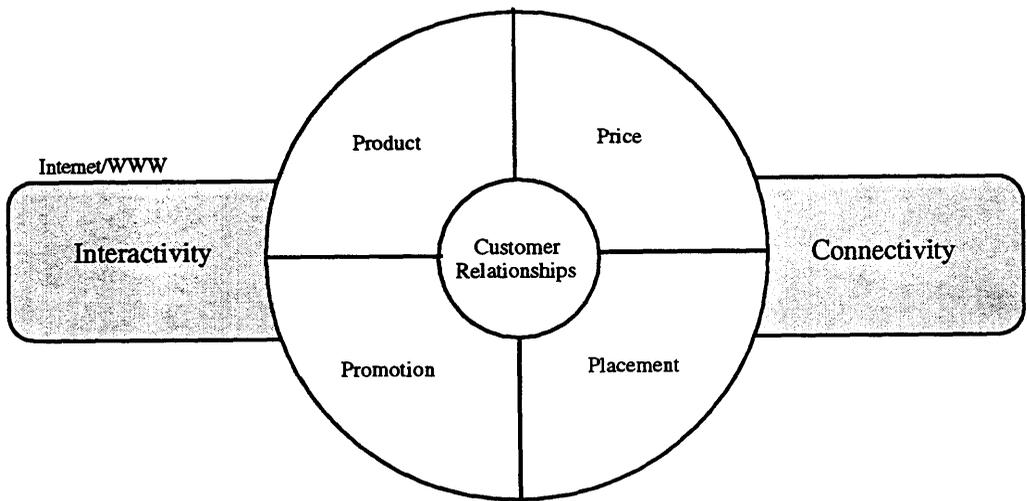


Figure 2: The Marketplace Model

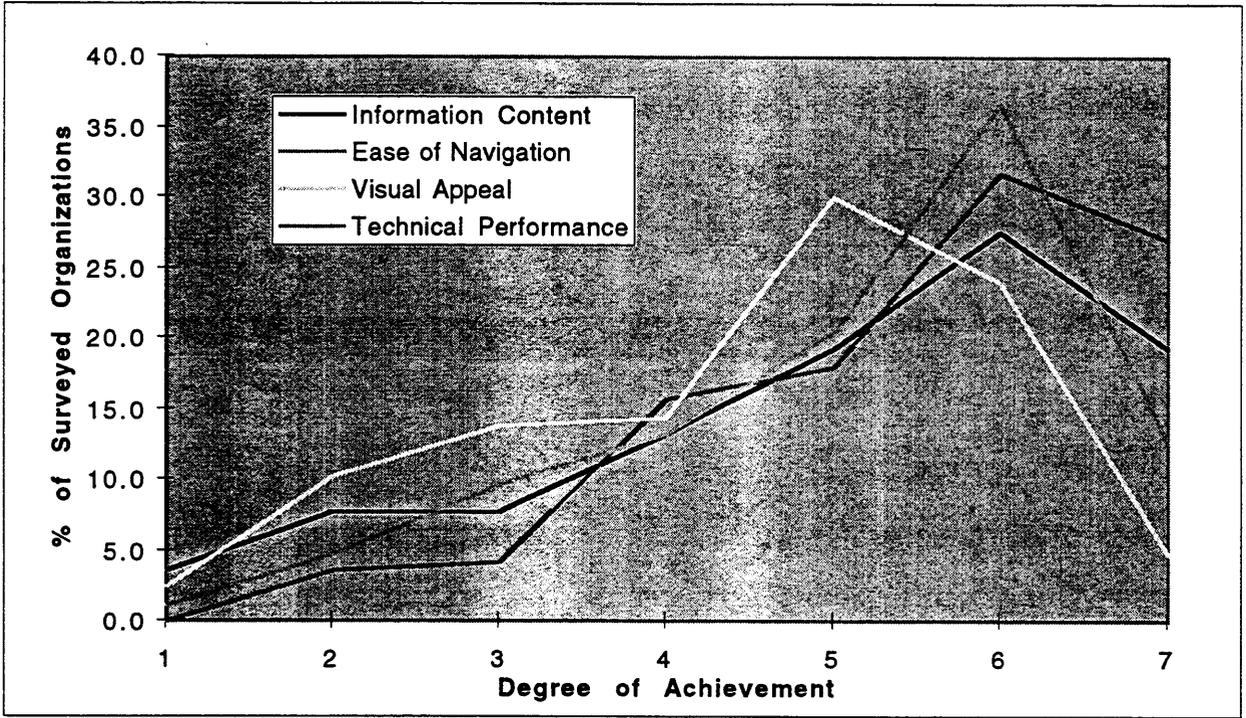


Figure 3: Dimensions of Technological Sophistication

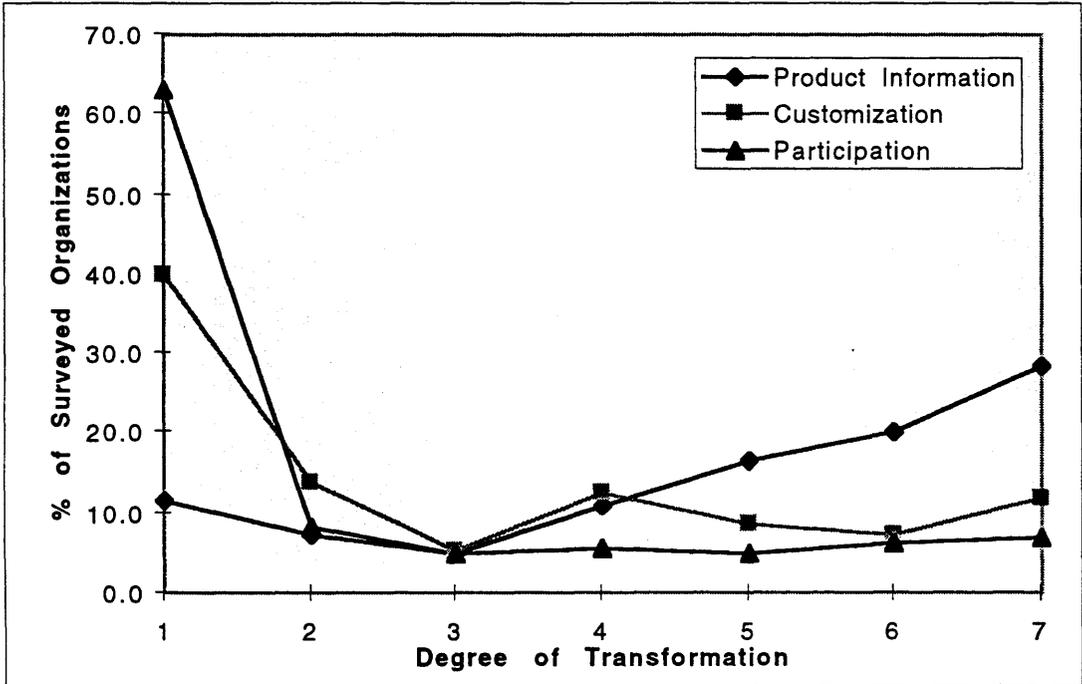


Figure 4a: Dimensions of Product Transformation

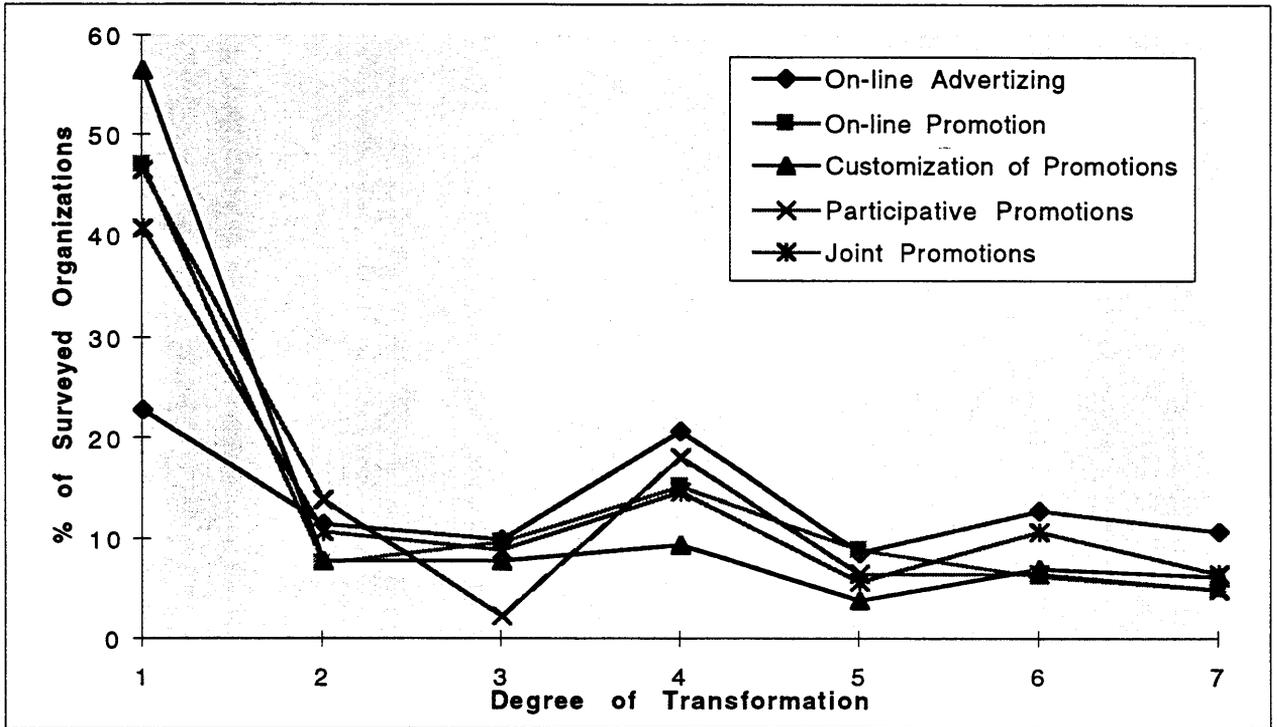


Figure 4b: Dimensions of Promotion Transformation

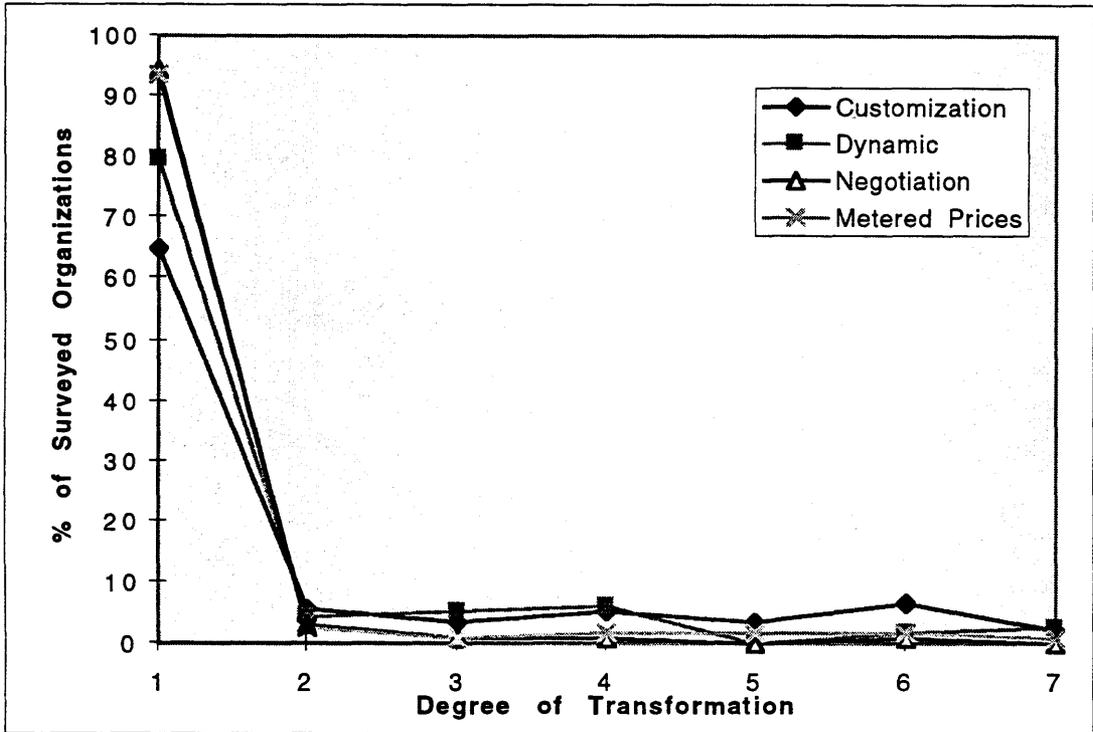


Figure 4c: Dimensions of Price Transformation

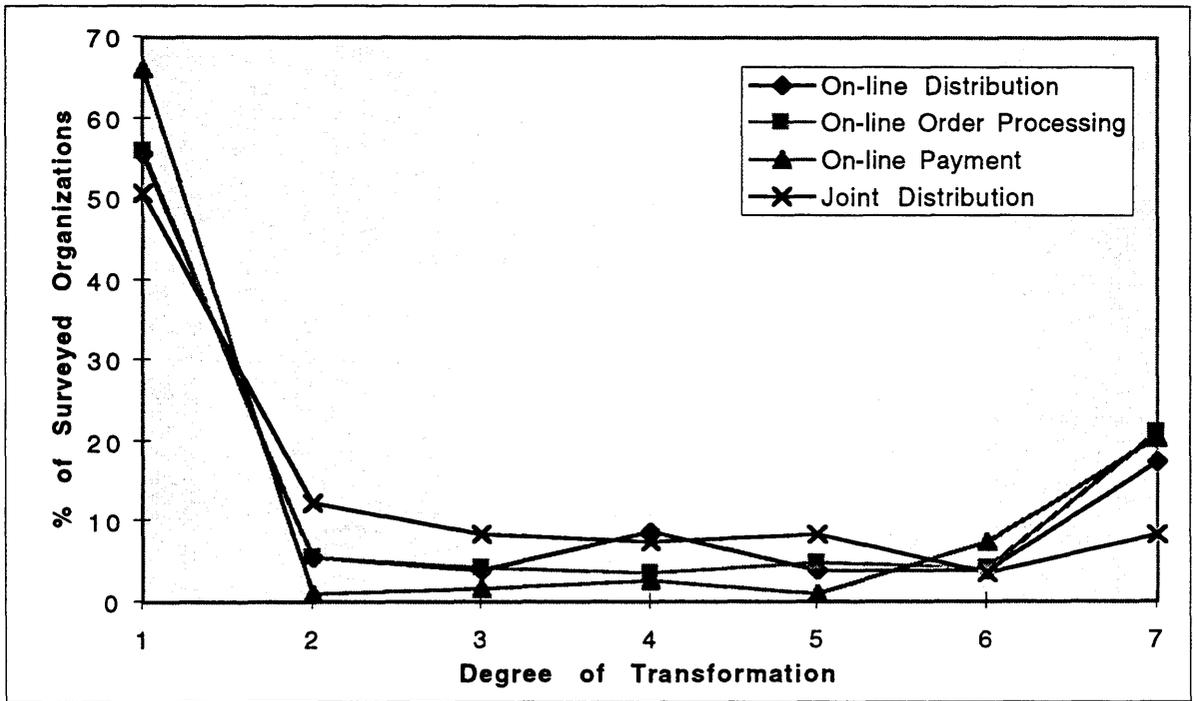


Figure 4d: Dimensions of Placement Transformation

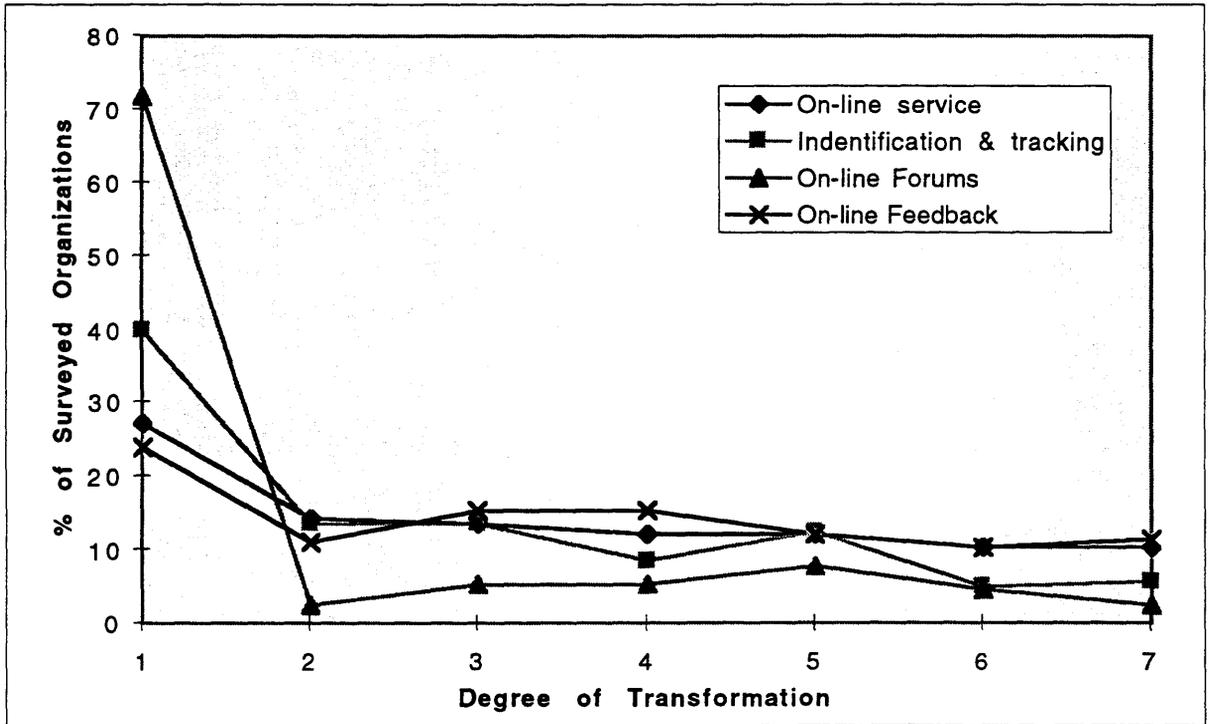


Figure 4e: Dimensions of Customer Relationships Transformation