

# MARKETSPACE STRATEGY AND THE EUROPEAN INFORMATION SOCIETY (POST 1998 DEREGULATION)

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## ABSTRACT

The purpose of this paper is to articulate and speculate on the nature of the risks and opportunities that European companies will face after the deregulation of telecommunications in 1998.

Whether or not executives realize it, the Internet and the World Wide Web have ushered in a globally standard, set of protocols and infrastructure for information transport, messaging, and document sharing. The impact of this critical mass of standards will be at least as profound as the coming of standard parts for manufacturing, radically altering cost structures and capabilities. Now is the time to start planning for these changes. We are in the midst of this change in the nature of competition and the shift from marketplace thinking to a marketpace (Rayport & Sviokla 1994) thinking.

Systematic research at the OECD (Communications Outlook) has shown that high local phone tariffs and monopolistic or quasi-monopolistic control of access to the Internet keeps adoption low. The price elasticity of Internet access is high indeed. The higher the price, the lower the use.

## CHANGES IN THE TELECOMMUNICATIONS LANDSCAPE

The Internet continues to double in size every 12 to 15 months (The Internet Domain Survey). However some countries have more per capita usage than others do. Finland for example is among the fastest growing and has the highest per capita (56 per thousand) Internet host usage. Other European countries, particularly Italy, Spain, and France are among the slowest adopters of the Internet.

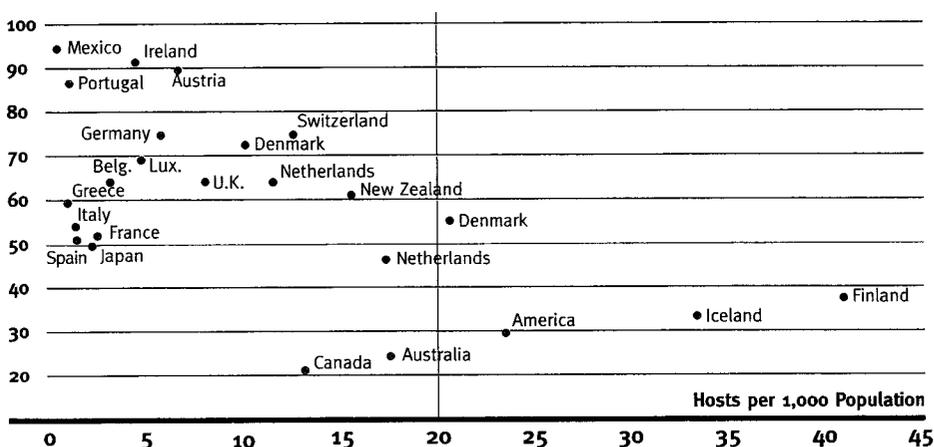
This slow rate of adoption is hampered by high connection costs at the consumer and business level and is a result of Europe's telecommunications structure and monopolistic practices.

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Internet Price/Usage, Source: OECD, 1997

Connection Basket Costs



Europe already lags behind America and Japan in both competitiveness as well as the use of information technology. Over the past 20 years, Europe's potential rate of growth has shrunk, unemployment has risen and competitive position has worsened internationally, compared with America and Japan (European Commission 1994).

In terms of the use of Information Technology Europe also lags. Only 20% of European households own a P.C. while 35% of American homes have one. Web use per capita is also lower in Europe. This is primarily due to high connection costs, which are a result of a highly regulated telecommunications market.

High call charges for Internet access are restricting Internet usage in Europe. This is choking off the emergence of a competitive information economy and society. Left unchanged the implications are serious as European companies:

- ◆ will accumulate less experience with virtual business transactions,
- ◆ be slower to adapt and decode the new marketpace rules of competition,
- ◆ may get left behind in what is becoming a global information based economy.

Meanwhile the Americans in particular will get the first mover advantages in cyberspace and may emerge with significant entry barriers on a global basis.

Deregulation will change all this? Some commentators feel that (Winton 1996) this slower technology adoption could prove a real economic drag on European progress in the marketpace or information-based economy. With deregulation in 1998, the marketpace will expand much faster.

Due to the existing critical mass of standards in document exchange, messaging and file transfer, we believe that telecommunications deregulation will unleash a strong and robust consumer and business marketpace. An important question for management is which markets and which functions will be effected first and how?

**FROM A PRODUCT TO A SERVICE ECONOMY.**

At a macro level, the most important shift in employment and adding of value over the past 50 years has been the increasing number of people and share of wallet spent on services.

The service sector continues to grow in importance relative to manufacturing. Some 60% of Europeans (that's about 70 million people) now work in the service sector. Today there are twice as many working in service as in manufacturing.

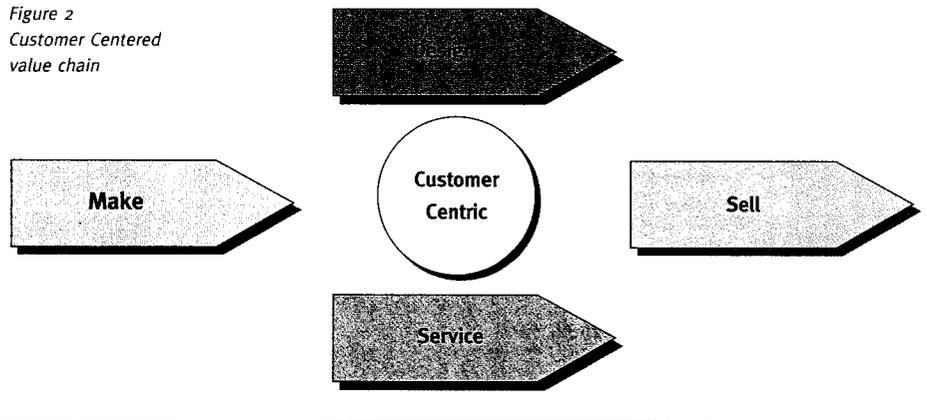
In America the service sector now accounts for over 70% of the workforce. This movement towards an increasing emphasis on service has been termed 'the servitization of business' (Vandermerwe & Rada 1988).

There are two important dimensions to this shift. Firstly the nature of work has moved from physical effort to an increasing knowledge content - from bricks to bits and from brawn to brain - or information work.

Secondly, the value chain is moving from a production focused physical one, comprising key steps such as design, manufacturing, sales and service towards a virtual value chain (Rayport & Sviokla 1995), which is infocentric and consumption focused.

The coming of the Internet and a more and more robustly developed marketplace will mean a continuation of this trend from product to service. In fact, tangible products become more and more like serv-

Figure 2  
Customer Centered  
value chain



ices all the time with customers interacting with information descriptions of the product instead of the product itself.

As the consumption process is becoming more information intense, managers now need to focus their attention on the information content, which is exchanged at the point of consumption. This is the new leverage point in the marketspace. Managers must shift their emphasis away from production centered activities towards customer centered activities to compete effectively in the new marketspace.

The virtual value chain is centered around the customer rather than the producer. Just recently Commissioner Bangemann has stressed that to achieve competitive advantage in the Information Society "companies must focus on the customer; and not only the technology" (Bangemann 1996). We could not agree more.

**PRODUCTS AND SERVICES: INFOCENTRIC AND NON-INFOCENTRIC.**

A critical question for the manager is which products and services will be effected first? We think that the infocentric

products are first to be changed and in time all products and services will be effected.

An infocentric product is one in which the primary value at the point of consumption is given by information. A newspaper is an excellent example of an infocentric product. When someone reads a newspaper, he or she is reading from a physical page. It is a "tangible". But the primary value of this tangible is the information that is passed (from the maker of the paper) to the reader. This is true of every media product, such as books, software and most entertainment products.

On the other hand a piece of clothing is an excellent example of a low-infocentric product. The information about the product, its size, its brand, its place of sale, are all important, but the function of the product, during the process of "consumption" has a low-information core.

Service is defined as 'an act or performance that one party can offer to another that is essentially intangible and does not result in the ownership of anything' (Kotler). As we see from this definition, a service provider often creates a service expressly for the consumer - often, even in the presence of the consumer - which is not inventoried. An infocentric service would be one in which the primary value is transferred by and through information.

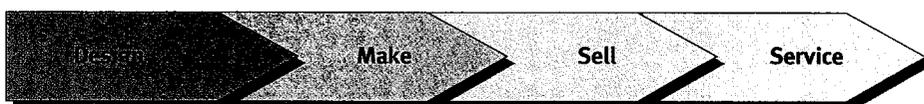
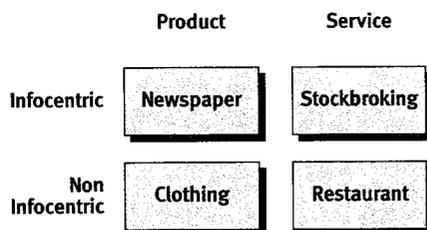


Figure 1 Physical Value Chain

Figure 3  
The Marketplace  
Matrix



### THE MARKETSPACE MATRIX

An excellent example of an infocentric service is stock brokerage. A stockbroker provides information about financial products.

A restaurant would be an example of a non-infocentric service. Certainly the atmosphere is important, as is the attitude of the staff. But, the "core" of the restaurant experience must be the consumption of food and drink.

Of course there are examples we can create that are difficult to classify, and the definitions can be picked apart (e.g. the restaurant must sell products like potatoes, in the process of delivering its service). The key distinction to keep in mind is to ask what is the most important contributor to the margin that the firm creates? For the restaurant, it is the service component that makes the margin. For the newspaper, the information component is what makes the newsprint more valuable.

### WHO WILL BE AFFECTED IN THE MARKETSPACE AND HOW?

Biggest issue: in order to be competitive in a world knowledge based economy Europe needs to have a first class telecommunication infrastructure on a commercial, personal and industrial level. The difficulty is that even with a world class infrastructure dramatic business changes will occur. The Marketplace will allow for new means of distribution, sales, and service in many business sectors.

The big question addressed in this paper is: What types of businesses will be affected and how?

### IMPLICATIONS FOR INFOCENTRIC PRODUCTS

The coming of this new information infrastructure will mean wholesale redesign of the product, distribution channel and customer relationships for many of the products and services in the infocentric category. What do we mean by this?

Let us return to our newspaper example. The advent of an interactive, distributed information system provides the newspaper with a set of opportunities and threats. The primary threat comes from the fact that the paper can be demassified. That is to say, one can take the different components of the newspaper and begin to offer each component of the value equation to the end customers.

Classified advertising represents a significant part of the economics of most newspapers. We can already see, in the United States, a series of on-line competitors, such as Pointcast, who are willing to give away classified advertising as a means to create traffic to their web site. This is very threatening to the existing newspaper franchise.

It is important in this discussion to realize that we are not saying that people will stop reading newspapers. We believe that the newspaper revenue streams may be eroded by on-line services. The vessel that we know as a newspaper will increasingly become a shell where focused competitors may come after each of the value components of the newspaper.

Of course, the newspaper has the option of building its own presence in the marketplace. Many newspaper companies are experimenting with online distribution. Papers like the Wall Street Journal and The Financial Times have limited interactive versions online. The Boston Globe, for example, has started their own online

service called Boston.Com. It features Globe news and advertising, as well as news and advertising from many other local papers and magazines.

The existing players can extend their franchise, if they so choose. As well as going online, the possibility of customizing the message is becoming more realizable. The big benefit here is that the consumer can choose what she/he wants to see and the technology delivers the customized content or personalized paper, eliminating redundant bits of information.

The big threat is that nimble new entrants may, by reconfiguring the value proposition siphon off the revenue streams while the existing players attempt to make their entrance.

For example, in the San Francisco Bay Area, Yahoo!, a popular Internet index gives away classified advertising. In 6 weeks it gathered over 5,000 automobile ads, 10,000 house ads, and 5,000 job ads. The marginal cost of production for these ads is very, very low because customers submit them in electronic form, and Yahoo! simply puts them up on their web site, where the world can view them. Given the potential threats by new entrants, we should wonder, what are the areas of opportunity for the existing players in the emerging marketplace?

### OPPORTUNITIES FOR INFOCENTRIC PRODUCTS:

There are a number of places for which the new, more pervasive marketplace can offer opportunities for infocentric products. If we consider the full customer life cycle, there are a number of leverage points.

- ◆ Cheaper customer acquisition costs
- ◆ New and more direct distribution channels
- ◆ Better customer service and value
- ◆ Tighter feedback design loops
- ◆ An integrated face to the customer.

Consider for example the virtual bookstore Amazon.Com. With over 2.5 million titles searchable online they represent a new

form of cybercompetitor. Unlike their current competition like Barnes and Noble or Borders, Amazon.Com have no assets tied up in physical bookstores, just one big warehouse in Seattle.

Customers can search for the book title they want and order online. Over 300,000 titles are discounted by between 10 and 40 per cent, so the customer is getting considerable value for money too. But there's more. With Amazon.Com customers can signal their interest in say a particular author and they will be notified by e-mail of new books of interest. All this is automated.

Better still, Amazon.com has gone further and built a virtual community of authors and readers. Authors can post interviews online and customers can post book reviews and even contact the authors. Readers can also interact with other readers. Naturally this all augurs well for the book publishers as demand is increased and book sales flourish.

This new online business model deals direct with customers and bypasses the traditional (place based) bookstore. This also establishes a new form of cybercompetitor who is competing along a different dimension – breadth of titles – which is costly to replicate in the existing physical model. Wholesaler and retailer margins get shared out between the customer in the form of lower prices and to Amazon.Com in margins.

Customers also benefit through the increased value and service of the virtual community as well as the convenience of the online shopping experience. Authors for their part get valuable feedback from the marketplace on their work as well as increased customer exposure.

In the online or virtual bookstore Amazon.Com has an advantage over traditional competitors and they will typify a new form of cybercompetitor. They will eventually compete on 'books as bids' rather than atoms, which are electronically deliverable.

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Many infocentric products and services are all at risk in the new marketplace. Non-Infocentric products and services will also be impacted but to a lesser degree.

#### IMPLICATIONS FOR INFOCENTRIC SERVICES

The infocentric services that are transaction focused such as brokerage, will have an incredibly difficult time maintaining their margins. The major service that a broker provides for the customer is the inventorying and sorting of information. These firms face significant redesign of their entire value proposition.

In the new Marketplace the number of brokers that have already gone on to the web are significant. Customers can already shop in some countries for a house by price, location, type and so on. The quality and bandwidth of the interaction, as well as the scale of the database will only increase over time. It will not be long before you can pick a neighborhood, "fly" into a three dimensional version of the houses and "see" what is available. Much of this type of capability is already in place with pictures, financing, and other information. For example Apartments Plus allows the customer to take a video tour of the prospective apartment and gives 360 degree views of the interior and exterior. (<http://www.aptfinder.com>)

As this happens, the customer may still go to a broker, but they will not be willing to pay the traditional margins to the broker. They will see a margin squeeze as the customer can self serve on a considerable amount of the information that makes up the value proposition for this infocentric service. Likewise stock brokers, insurance brokers and financial advisors will continue to see increasing competition and price pressure, particularly as customer search costs fall and services become more electronically enabled via the Web.

The travel industry is another good example of an infocentric service. The Internet now provides a "golden chance to bypass the travel agent" (McCormack

1996). Customers can go direct to airlines, hotels, package operators and tourist authorities. The travel industry has coined the term 'disintermediation' to describe this shift in the distribution channel. Prices will fall, middlemen will be squeezed out unless they dramatically reconfigure their customer value proposition.

Now, in this argument, it is very important to see that the marketspace version of these infocentric services will be total substitutes for the traditional services. We are saying that the price and service expectations will be greatly enhanced by the marketspace, and those brokers who use these new services will have the opportunity to provide more new and innovative services for their clients at lower cost. This will create more competition in the brokerage and travel industry, making it more difficult for them to justify their existing margins.

#### PRODUCT TRANSFORMATION IN MARKETSPACE

Another feature of the emerging marketspace is the ability to re-configure the physical product into a new infocentric service. Take the humble encyclopedia for example. It is now possible to capture the entire content of all the physical books in electronic form (CD-ROM). This eliminates the need for the entire book printing process.

One company has faced this transition with considerable difficulty. Encyclopedia Britannica (Encyclopaedia Britannica Case Study) invented this product category but has lost out in the movement to the new marketspace. In 1994 sales in their traditional business dropped off by 50% and even though they had invested in an information technology representation of their product they had to sell this off. They sold Compton's New Media for \$70m well short of their \$400m asking price. Senior management did not really understand the catharsis taking place in their marketplace as the old rules of value creation and value capture no longer held true in the marketspace.

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Management must understand and manage the transition to the new rules of value creation and capture in the marketspace. The transition from physical to electronic is not an easy management task. New entrants may often have the advantage in these new market forms than existing competitors. So watch out for and study the mould-breakers in your marketplace. Try to discover what their new customer value proposition is, before it's too late.

#### NON-INFOCENTRIC PRODUCTS AND SERVICES

The impact of the emerging Marketspace will not be as dramatic in the non-infocentric products and services. The main impact will be in three primary areas. First, they will have impact on the acquisition of customers. As the interactive network reaches into the home, many advertisers will choose to use this medium because it combines the best of broadcast advertising with the specificity of direct mail.

Every major car company now has a presence on the World Wide Web. When Saturn, a division of General Motors, opened up their presence on the web, they started at over 50,000 inquiries a day quickly going to over 100,000. Their fleet of cars in service is only 3,000,000. It was not clear if these inquiries were incremental (e.g. new to the world) or they had simply shifted from phone or mail to the web. Even if they were entirely made up of people who had shifted to the web, it would make economic sense for GM, because handling a web inquiry is usually 20-50 times cheaper than handling a phone call.

The second domain in which non-infocentric products will be affected is the after-sales service. Companies can give 24 hour a day access through electronic mail to their customer base. They can provide service information. They can sense when people are in need of service through information on service history etc.

The third domain will be in the repeat purchase process. When a customer is ready to have a new version of a product or service, the interactive presence, mentioned above in sales and service, gives the offering company the opportunity to resell to the customer. Information on existing product ownership and use is a new company information asset base.

An important related dimension of this process is the reselling of goods themselves – in a used market. The coming of a broadband, interactive network will provide a liquid market for used hard goods. If your product or service has a long useful life, and a high resale value, the chances are that a robust after-market will be developed. The used car market is already being facilitated by electronic means in the US and Japan and it will come to Europe with a vengeance. AUCNET (AUCNET 1996) for example has constructed a new value proposition in car auction business in Japan. Using information technology the auction takes place in virtual space and the customer buying process has been dramatically reconfigured. So watch out for these new threats and opportunities for your business.

Another interesting development is the possibility of bringing the customer directly into the design process. This can dramatically change the ability to develop fast market responses to customer needs. Levi's (Summer 1996) for example has used technology at the point of purchase to obtain information on customer size requirements for jeans. They use this information to custom manufacture bespoke jeans for the individual lady customer and deliver these at a 40% price premium. This information 'asset' is then bar coded into the jeans and the customer can re-order to suit their size at any time. Understanding and responding to the information exchanged at the point of consumption enhances both customer loyalty and differentiation (price premium).

So even with low-infocentric products and services the marketplace has many opportunities to differentiate. As with non-infocentric products, the main impact on non-infocentric services will be in:

- ◆ Customer acquisition,
- ◆ After-sales service, and
- ◆ Design feedback loops.

#### SUMMARY

The basic argument of this paper is that the coming of the interactive internet-like network to Europe will mean a wholesale redesign of the customer value proposition for those companies that have infocentric products and services. There will also be a much reconfigured customer contact system (acquisition, service, and reselling) for non-infocentric products/services.

Those firms that live on information float, or make a margin due to poor access to information, or hold onto their competitive advantage due to the fact that their competitors cannot reach the end consumer efficiently, must watch out. It will be easier in future to reach that end consumer, and with reasonable telecommunication rates, the information penetration of homes and businesses will be very rapid indeed.

#### MANAGERS – WHAT TO DO?

Given the rapidly impending deregulation in telecommunications in Europe managers need to assess the impact of the marketplace on their businesses and prepare for the opportunities and risks inherent. The following are some key questions to assist this process.

- ◆ How infocentric is your product or service business today? Where does your company fit in the Marketplace matrix?
- ◆ Is your product becoming more service intense? This may signal a re-configuration of your value chain from a physical to a virtual one.
- ◆ How infocentric is the consumption process? Look at the consumption process again from the customer's perspective and focus on the information exchanged at the point of consumption.
- ◆ How vulnerable is your business to a complete redesign of the distribution system, the product or service offering?
- ◆ What marketplace moves are your competitor's making? Be careful to include new competitors as well as your existing ones.
- ◆ What new business opportunities arise out of this new marketplace, to acquire customers at a much reduced cost, to enhance after-sales service, to build customer loyalty or to engage customers in the product/service design loop?

As Commissioner Bangemann has indicated the real key for companies is 'to see where technology can be used to improve customer service and satisfaction'. The marketplace will bring in its wake many new opportunities for European companies to compete for customers in both global and local markets. In this new competitive environment the rules and even the game will change with technology providing new ways to reach existing customers often bypassing the existing business model.

However, without a competitive infrastructure European companies may again be left behind in the rapidly emerging information economy. The future will belong to those companies and countries that are prepared for the new marketplace.