EDITORIAL

INTERNET MYTHS

With all the hype surrounding the Internet, we imagine some of our retail subscribers wake up and wonder if they'll soon find themselves next to a dodo bird in a museum exhibit of extinct species. According to the more outspoken "new economy" experts, cyber merchants, unburdened by the high cost of storefronts and personnel, and with access to a world market, are destined to turn traditional bricks-and-mortar stores into the retail equivalent of a buggy whip. In a January issue of *Fortune* magazine, technology columnist Chyna Chen enthused, "Consumers are pressed for time, and with everything they could ever desire just a click away, why would they ever go to a store again?"

"Frictionless" online commerce certainly makes sense in theory: Consumers can shop the world from the comfort of their home and, with a few clicks, access more pricing and product information than any store could ever provide; however, as cyber merchants try to transform this theory into a workable business, we're reminded of the old joke about dog food. The new dog food was perfect in every respect and passed all the marketing tests with flying colors. There was just this one tiny problem: Dogs wouldn't eat it.

As more and more high-profile online merchants crash and burn, we're starting to wonder if "the dogs just won't eat the dogfood." Consider the case of the recently shuttered Toysmart.com. Backed with a massive capital infusion from the Disney Company, Toysmart.com was launched two years ago with every possible advantage. The company spent $2.0 million with AOL to ensure that Toysmart would head the list of Web searches involving anything even remotely related to toys. The prestigious Boston Consulting group gave the Toysmart site its highest five-star rating, declaring, "This is as good as a Web site gets." In the vital fourth quarter of 1999, Disney gave the company millions in free advertising time on its top rated "Who Wants To Be A Millionaire?" series. *Adweek* magazine even declared the Toysmart TV spots "Best Retail Creative" for 1999.

Despite these rave reviews, consumers were not moved to buy. In the fourth quarter of 1999, on sales of just $6.0 million, Toysmart had a staggering loss of $25.0 million. It cost the company $200 in marketing expense to acquire a single customer, yet the average transaction was a paltry $44. If the company had randomly mailed out $50 worth of merchandise to each customer, its financial results would have actually been better. Earlier in the month Disney shut down the operation.

Reel.com, an online video retailer, suffered a similar fate. After the company lost $82.5 million on sales of $41.9 million in 1999, C.E.O. Mark Wattles declared, "I've just given up on the ability to make a profit on the e-commerce business."

The failure of these and other online retailers doesn't discredit the concept of the Internet as a potent commercial vehicle; however, it does debunk some of the popular myths surrounding e-commerce.

Myth Number One: The Internet gives you access to the world. The census calculates that there are 88 million households in the U.S. One hundred percent have mail service, 98% have a telephone, 96% have a television and radio, and 68% receive some type of daily newspaper; yet only 47% have a computer or Internet access. Online merchants miss a big chunk of the market.

Myth Number Two: The Internet is a low-cost retail model. Computer engineers are a scarce and costly commodity, so the personnel costs associated with maintaining a Web site are high. Add to that the incredibly high cost of driving customers to your site. A spokesman for REI, a leading retailer of outdoor equipment, summed it up: "Stores cost a lot less to run than a Web site."

Myth Number Three: Customers love the service and convenience of the Web. If that's really the case, then why can't any of these online retailers charge a premium? From Amazon.com to the majority of online m.i. retailers, most we observe seem to operate on the belief "We lose money on every sale, but we'll make up for it with volume."

E-commerce unquestionably has great potential; however, no one has yet to develop a workable model that combines all the benefits of the Web and simultaneously operates profitably. Venture capitalists are no longer willing to shovel millions at money-losing online businesses, so the issue of profits has taken on a new urgency. It may be new technology, but the old rules still apply.

Brian T. Majeski
Editor