Supermarket Strategic Alert
Special Report

2002

FROM THE REGULAR AND SPECIAL EDITIONS

January through December 2001

Clicks-and-Order e-Tailers

FROM THE 2001 REGULAR AND SPECIAL EDITIONS

Special Report: 2002

Clicks-and-Order e-Tailers

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Clicks-and-order e-Tailers

As the world reeled from dot-com failures generally, the conventional supermarket industry watched and smiled in vindication. Not more than five years ago, consultants and gurus advocated a central distribution facility for home delivery of groceries. Store-based picking was doomed in their minds because of inefficiencies, complexities and inconsistencies and the belief that Americans would do anything to avoid a trip to the supermarket.

So much for consultants and gurus. 2001 saw the death of virtually all the freestanding distribution center players. Most notable was the crash-and-burn of Webvan. From darling to disaster, the company's fortune might best be remembered from its zenith as sponsor of the San Francisco Giants baseball team (because of stadium signage) to its demise and selling its software to Kaiser Permanente—a health maintenance company. Not a player in the supermarket or retailing industry jumped to acquire any part of it. Streamline, HomeRuns, Kozmo and others also closed.

Peapod was saved from the same fate by Ahold USA—now its controlling owner. Very quickly, Ahold integrated Peapod operations into existing bricks-and-mortar stores, closing dedicated distribution centers. So much for consultants and gurus--what made sense on paper was stymied by consumer behavior. Shoppers were not willing to embrace Web, fax or other ordering. As much as they complain about trips to supermarket, they still went.

Safeway's investment in GroceryWorks looked like another save...but. By year end, Tesco—the UK-based chain that boasts profitability in home delivery by having started small—was a major shareholder in GroceryWorks. And Tesco made it very clear in making that investment that it was looking to become a significant US player. Stay tuned.

Still, some supermarketers (D'Agostino, Harris Teeter, etc.), recognizing the value of their own brand names, have started offering home-grown (Publix) or third-party (MyWebGrocer.com) Web ordering and home delivery options.

NetGrocer seeking retail partners

With the announcement of a new president at NetGrocer, the company took the opportunity to announce that it is looking for retailer partners. What NetGrocer has to gain is obvious: access to an enormous customer base. Retailers would gain by having a drop-ship option for their shoppers who currently visit warehouse clubs and other outlets to stock up on staples. Further support for the move come from the recent Ahold / Peapod and Safeway / GroceryWorks alliances and the synergy gained therein.

Source: *SN*, January 1, 2001. NetGrocer Seeks Brick-and-Mortar Alliance, by Jon Springer, p. 1, 4.

Peapod to use Ahold suppliers

Peapod ended its 10-year-old supply relationship with Jewel-Osco in Chicago as expected, since it is now part of Ahold and Jewel-Osco is a division of competitor Albertson's. Peapod will now be supplied through American Sales and Tops, both affiliated with Ahold. American will supply HBC items and private labels (replacing Jewel's President's Choice); Tops the remainder of the grocery line. Perishables will be purchased from Chicago's South Water Market. Local and national providers will supply meat and seafood.

The move will lower Peapod's inventory costs by taking advantage of Royal Ahold's buying power. Lowering inventory costs is crucial as Peapod tries to prove to Wall Street that it can make money. Its management expects to turn an operating profit in Chicago, Peapod's largest market, by the middle of next year. Investors remain skeptical of Peapod and other Internet grocers in an industry that has seen its share of revamped business plans, do-or-die mergers and shutdowns.

Source: *SN*, January 1, 2001. Peapod, p. 4. *Chicago Tribune*, December 28, 2000. Peapod to sever connection with Jewel, by Ameet Sachdev.

HEB.com launches with car sweepstakes

HEButt's March launch of HEB.com will be hyped with a sweepstakes grand prize of a Chrysler PT Cruiser. Two thousand people a week have been registering instore and online since the sweepstakes began on November 22. The site offers 20,000 of the 35,000 items carried at a typical store, accepts credit cards and electronic checks. There will be a $9.95 delivery charge or free order assembly for customer pickup.

Source: *SN*, January 1, 2001. HEB.com Cruises Toward Launch, by Peter Perrota, p. 19, 21.

Trends to watch for

SN-Supermarket News identified the following trends in Internet grocery shopping for the coming year: (1) Pure plays are losers, hybrids are winners. (2) Independents and regionals are building their online operations. (3) Customer pickup is growing in popularity over delivery service. (4) Shoppers are showing a preference for ordering from local retailers rather than from third parties. (5) Online players are either charging for delivery or only doing bulk orders.

Source: *SN*, January 15, 2001. Web Watch, by Christine Blank, p. 39-40, 45.

Post mortems on the concept

Grocery Headquarters reviews the headstones for dead Internet grocery companies, observing that despite these ventures being lauded as a boon to B2C virtual marketing, they never really were virtual. Those interviewed cited the following reasons for the demise of so many of the pure plays: (1) High infrastructure costs, including residential delivery, warehouses and customer service centers, (2) Attracting a customer base. Despite targeting dense metropolitan areas, delivery and service incentives were insufficient to lure enough shoppers.

A PricewaterhouseCoopers study confirms what many considered obvious: while 42% of Internet users want to spend less time grocery shopping, only 11% are willing to pay a fee for it. The year-end consensus is that the survivors will be a combination of pure play technology and land-based operations. These alliances will leverage retail infrastructure (stores, warehouses, personnel, etc.) and provide the financial cushion to wait until scale is achieved. Support for this is the high ratings existing retailers get from consumers for the services they provide. Albertsons.com was top-rated by Gomez Advisors consumer rankings. Many believe that grocery shopping has a relationship element, and local retailers already have that relationship with their customers.

Source: *Grocery Headquarters*, January 2001. Who will survive? By Alison Paddock, p. 18-21.

Webvan not yet profitable

Prior to any official announcement, Webvan warned of lower than expected earnings in the 4th quarter due to decreased marketing expenditures, delivery difficulties and the need to conserve cash. Since the stock has been trading below $1 for almost 30 days, the stock risks delisting from the NASDAQ. The company has $200 million in cash which will last only two more quarters.

Profitability in the tech-savvy, harried San Francisco area where the company started is critical to retaining investment community confidence beyond its current venture capital backers. *The Wall Street Journal* reports that for the San Francisco operation to have been profitable in the last quarter, volume would have had to increase 40%. The fourth-quarter loss totaled $173.1 million, almost twice what was reported a year earlier. The company has reduced its estimate of daily orders required in San Francisco from 3500 to 3200, but reached only 2160 and is postponing further expansion to focus on profitability.

Business Week/e.biz profiles 15 tech companies that have fallen from favor because of lack of cash and calculates their ‘cash burn’ rate. The majority can be described as technology infrastructure or service companies—those that provide the backbone for Web communications or Internet service providers. Also on the list is Webvan. The magazine estimates that it has enough cash to maintain operations through June and would need $80 million to last through the end of the year.

Source: *SN*, January 15, 2001. Webvan Sees Revenues Declining in 4th Quarter, by Jon Springer, p. 1, 71. *The Wall Street Journal*, January 25,2001. Cash Supply Shrinks While Webvan Losses Continue, by Nick Wingfield, p. B1, B4. *The Wall Street Journal Interactive*, January 25, 2001. Webvan Posts 4th-Quarter Loss, Postpones Expansion of Service. *Business Week/e.biz*, January 22, 2001. Dead Companies Walking, by Peter Elstrom, p. EB 63.

Canadian mail order pharmacies

The definition of alternate channel competition needs to be further broadened. Just as supermarkets discovered potential sales increases from building pharmacy operations, they are being hit by a new competitor—online Canadian drugstores. All prescription fillers are watching the Canadian operations carefully. From a consumer standpoint, they offer significant discounts for just a few mouse clicks, are easier than the trips that many seniors make to Canada for their regular drugs, and subject to the strong currency exchange rate as well.

Still—the process is illegal. Individuals are allowed to import three months of drugs for personal use, only if they are not available in the US. The FDA has chosen to look the other way on small consumer transactions because of manpower considerations. Canadian authorities are less open-minded and looking into ways to plug the loophole. Currently the three operating Canadian Web drugstores fill only a small proportion of the total 3 billion US prescriptions, but with discounts of 20-50% they are under scrutiny.

Prices are lower because generic equivalents of some drugs available in Canada are not yet available in the US under patent protection, but also because the pharmaceutical companies charge higher prices in the US to recoup discounts elsewhere to fund research. Canadian authorities do require prescriptions to be written by

Canadian doctors. One site has a Canadian doctor review US prescriptions and write a new one. Another has a doctor review patient histories and co-sign prescriptions. Another mails the prescriptions to the US doctor. Legal questions remain, but interpretation varies and prosecution is untried. Canadian provinces are looking to plug loopholes, but pharmacists are lobbying against such legislation, noting that shoppers will buy in other provinces—the very benefit that the Internet offers. The leading Canadian Web pharmacies are CanadaMeds, CanadianDrugstore and CanadaRx.

Source: *The Wall Street Journal*, January 18, 2001. Canadian Web Drugstores Offer Deep Discounts and Legal Quandaries, by Laura Johannes, p. B1, B4.

Webvan developments

This month Webvan announced that it would pull out of the Dallas market area to conserve cash and help reverse its losses, thereby cutting 220 jobs. The e-grocer remains in nine other cities. Peapod will pull out of San Francisco and is simultaneously asking Royal Ahold, its majority owner, for more cash to continue operations in remaining markets through 2001 and attain profitability by 2003.

For those keeping a scorecard, this leaves Webvan without significant competition in the San Francisco Bay area, possibly improving its profitability and survival there. In Dallas, it leaves GroceryWorks (a Safeway partner) without significant competition. PublixDirect will enter the Atlanta area by the summer of 2002, complicating Webvan's efforts there. Market watchers says the Publix brand name will be a distinct advantage.

Outside e-commerce observers, unencumbered by the reality of the supermarket business, say the biggest problem these operators face is the overpromise of delivering at a certain time—the elusive 'last mile.' Also inventory management remains a challenge. Moving past groceries to higher margin products only complicates the situation.

Creative thinkers and venture capitalists fed off each other creating an 'arms race mentality.' Now both are scaling back expectations and designing coupons instead of kitchens of the future. Futurist automation does not pay off either: Highly automated equipment in freezer areas slows to a crawl at low temperatures making the equipment slower at picking and packing than parka-clad employees.

Source: *The Wall Street Journal Interactive*, February 21, 2001. Webvan Group to End Service In Dallas in Cash-Saving Effort, by Nick Wingield. *The New York Times*, February 21, 2001. Online grocer Quitting Dallas, p. C7. *Chicago Tribune*, February 22, 2001. Peapod To Quit San Francisco Market Amid Quarterly Loss, by Ameet Sachdev. *E-Commerce Times*, February 20, 2001. Web Delivery Services in Crisis, by Lori Enos. *Atlanta Journal Constitution*, February 23, 2001. Publix plans Web-based food service, by Renee DeGross. *The New York Times*, February 19, 2001. Some Hard Lessons for Online Grocer, by Saul Hansell.

Newsweek faults underlying logic

Newsweek offers an analysis of the demise of e-tail darlings and the underlying logic that made their downfall inevitable. To begin with, *Newsweek* argues that the Internet is technology, and that selling goods over the Internet is merely one use of the technology. The problem, however, is that the Internet does not make retailing any easier. The entrepreneurs who flocked to e-tailing made several mistakes: (1) They launched business with questionable potential, usually limited to precise product categories. There was little evidence to support selling toys or pet food online as long-term business propositions. (2) These entrepreneurs underestimated the intricacies of retailing, often arguing that e-tailing was different. Customer service is critical: In the e-tailing world it must be three-pronged: online, phone and mail. (3) Competition is often fiercer because comparison shopping is only a click away. (4) Shipping and fulfillment costs make low-margin businesses even less profitable. (5) An easy-to-use, customer friendly Web site is expensive and challenging to build. (6) Many shoppers still fear using credit cards for online sales.

To be fair, online retailing does have some advantages: (1) possible lower capital investments because physical stores are not necessary, (2) better cash management, since customers can be charged before inventory bills are paid, (3) 24/7 sales capability, (4) customizable shopping experiences, (5) ease in adding new products and categories, and (6) simpler global expansion.

Still, with 20/20 hindsight, the only companies that remain possible long-term players in this arena are eBay, which has actually shown profitability, and Amazon, although that's questionable after recent layoffs. *Newsweek* suggests the real winners may be landbased retailers, Wal-Mart chief among them, because they have the experience and the deep pockets to play by the rules and potentially rewrite them.

Source: *Newsweek*, February 12, 2001. Clicks for Bricks, by Jeff Fischer, p. 66-7.

USA Today predicts more partnering

USA Today observes that online grocers are partnering or being bought out by supermarket chains 'faster than shoppers go through tubs of Rocky Road.' Webvan is currently the only major exception. A partial list of these alliances follows: (1) Stater Bros. (155-store Southern California chain) began online sales with delivery service WhyRunOut.com. (2) Safeway is the sole supplier for Texas-based GroceryWorks.com. (3) Royal Ahold took a majority stake in Peapod when it was struggling.

During 2001, online grocery sales are estimated to hit $2 billion, less than a mere 1% of US grocery sales. Jupiter Research believes 'the fear of losing market share will motivate most of the big players.' This explains why so many grocery chains are building their own online enterprises: a sale is a sale and losing it to the competition is not an option. (1) Publix will launch PublixDirect this summer in Pompano Beach FL, expanding to Orlando in 2002. (2) Supervalu (wholesaler and retailer) will begin online shopping for select stores in the next three months. Customers will shop online and pick up groceries at the store. (3) Albertson's offers Seattle customers pick up privileges through Albertsons.com and also offers home delivery in Seattle and Dallas/Fort Worth.

Still, skeptics remain: (1) Kroger, the largest grocery chain in the US, is only experimenting with online shopping in Denver. (2) Winn-Dixie has no online plans.

Source: *USA Today*, February 12, 2001. Online grocers run for cover. Partnerships with traditional chains offer security, by Michelle Kessler, p. 1B.

Christian Science Monitor sees benefits

James Turner—computer consultant and avid Web surfer—summarizes online grocery shopping from a consumer standpoint for the *Christian Science Monitor*, adding that online-grocery services are one of the most useful Web applications for the disabled, over-scheduled or those who dislike lugging groceries and are prepared to pay not to do so. The glitch is that such services have yet to prove themselves money-making propositions. (1) Full-line grocers (Webvan, Peapod, etc.) are suffering. Many have shut down. (2) Specialty/niche retailers offer unique products and charge more than most grocery services because special packaging is used to keep perishables fresh during cross-country deliveries. (3) Nationwide services such as NetGrocer ship via FedEx, usually offering only non-perishables. (4) Local services are available in defined areas. Often with specific instructions they can meet unusual needs, but substitutions do occur. Delivery and pick up options vary; some require being at home to receive the goods.

Source: *Christian Science Monitor*, February 12, 2001. Online grocers try to extend their shelf life, by James Turner.

Webvan cure?

Randall Stross—contributing editor to *US News & World Report* writing on *The Wall Street Journal* editorial page—proposes a solution for Webvan. He says that the $212 million that Webvan has on hand is a lot of money and that can best be spent on infrastructure so that the company can provide what it originally promised: timely grocery delivery. As a San Francisco customer, he observes that the only available delivery windows are usually three days hence. Noting that consumers do adapt to change—as they did in the case of ATMs and paying at the pump for gasoline, Stross emphasizes that Webvan's problem is not that it is just trying to modify behavior, but that it cannot force Safeway stores to close. In the other examples, the banks closed branches and the gas stations eliminated registers. Stross' cure is to advertise so that all the satisfied first-timers return to the fold. He contends that many have lost interest because when they do go to order, the delivery is so far off they cannot wait for the goods.

Source: *The Wall Street Journal*, February 2, 2001. Only a Bold Gamble Can Save Webvan Now, by Randall Stross, p. A10.

Editorial Alert: Insiders rebut that Web grocery shopping is not on life support. Marc Van Gelder—ceo of Ahold's Peapod—describes 'last year (as) a restructuring year. This year is a harvesting year.' Analysts agree that his company has a better chance than most because of the deep pockets of parent Ahold. Jupiter Research projects online grocery sales to triple this year to $2 billion and to reach $18.5 billion in 2005, but a model that makes money rather than burns it has yet to emerge. (The Wall Street Journal Interactive, February 16, 2001. Small Business Suite: Struggling Net Grocers Are Eager to Deliver, Associated Press. Dow Jones Newswires, February 23, 2001. Peapod CEO: 2001 Cash Needs Will Be Fully Met By Ahold, by Eric Ahlberg.)

Red Light at BlueLight.com

Kmart's BlueLight.com is changing its pricing policy. Under the plan, beginning in March, anyone who signs up for basic services will receive 12 hours per month for free. (The service has been totally free.) To get up to 100 hours of Internet access, customers will have to pay $9.95 per month, or for unlimited access, make a purchase on BlueLight.com. There is no minimum purchase; however, customers who spend more than $100 will receive another month of free service. For every additional $50 spent over the $100, customers receive another free month. A company representative said the decision is a way to cut costs and get the online service back to its core business. BlueLight.com, with 6.3 million subscribers, launched using Internet service provider Spinway, which generated revenues from advertisements to cover the costs of the free service. When Spinway shut down last month, BlueLight.com was forced to buy the service provider and inherit all of the costs.

Source: *Detroit Free Press*, February 14, 2001. BlueLight changes policy. For free Web access, customers have to buy, by Sheryl Kennedy. *The New York Times*, February 22, 2001. Bluelight.com, p. C4.

5-year projections

Data from Jupiter Market Metrix suggests that although the top five online retail categories in the year 2000 were dominated by technology-related items, sales in 2005 will be very different. The top five online retail categories in 2000 were: PCs with sales of $6.2 billion, apparel and accessories at $2.4 billion, books at $2.2 billion, computer peripherals at $1.5 billion and software at $1.3 billion. Jupiter predicts that by 2005, grocery sales online will top the list at $18.5 billion—after mastering logistics. PCs will be in second place with sales totaling $12.3 billion.

Source: *The New York Times*, March 5, 2001. Shopping by PC For More Than PC's, by Tim Race, p. C4.

Peapod: Massachusetts & California

Peapod is raising delivery fees in Massachusetts, bringing those fees in line with its delivery fees in the rest of the country: $4.95 for orders of $75 to $100, $9.95 for orders of $50 to $75 and free delivery on orders over $100, up from $60. The minimum order will be $50.

Peapod, which shut down its San Francisco operations to focus on the East where parent Ahold has more retail operations, is directing its customers to formal rival Webvan. The message posted on Peapod's Web site informs San Francisco customers they can continue buying their groceries over the Internet via Webvan. In keeping with customer privacy preferences, Peapod asked customers whether they wanted their private information turned over to Webvan. Webvan will pay Peapod an acquisition fee for every Peapod customer completing a transaction.

Source: *SN Daily News*, March 1, 2001. Peapod Raising Delivery Fees in Massachusetts. *PG Daily News*, March 12, 2001. Peapod, Webvan Enact Deal for San Francisco e-Shoppers. *The New York Times*, March 13, 2001. Peapod, Online Grocer, Quits San Francisco, p. C6.

Webvan starts advertising

Webvan is beginning a 4-6 month advertising push in nine markets with the objective of increasing shopper purchase frequency. Described as 'Ally McBeal-style' TV commercials and radio spots, the campaign is described as targeted…although spokespeople declined to place a price tag on the effort.

Source: *Seattle Times*, March 7, 2001. Ailing Webvan begins ad campaign, by Monica Soto. *SN Daily News*, March 9, 2001. Webvan Launches Television Ads in Nine Markets.

Netgrocer's positive feedback

PlanetFeedback.com's 2000 Consumers' Voice Awards cited Netgrocer as 'a top e-retailing site.' PlanetFeedback is an online consumer feedback service that presented awards to 24 companies in 11 industries with the highest percentage of positive feedback from their users last year. PlanetFeedback data shows that more than 80% of Netgrocer's consumer responses are complimentary, compared to an industry average of only 39%.

Source: *SN Daily News*, March 9, 2001. Netgrocer Recognized as a Top E-Retailing Site.

Land-based operators remain cautious

With widespread publicity about the travails of pure play Web grocers, traditional supermarketers' ventures into Internet grocery shopping are under greater scrutiny. Schnucks Express Connection is the only supermarket-sponsored Internet grocery shopping outlet in St. Louis, and has been around since 1997 though not promoted. The company is reluctant to promote it broadly until it is more efficient and profitable. The service is currently available to all of the communities Schnucks serves in Illinois, Indiana and Missouri, where Schnucks operates four distribution centers. About 15,000 items ordered over the Internet are received, picked and packed at these facilities. The flat delivery fee is $9.95. Now Internet orders are 3x-4x bigger than normal orders—appealing to customers who value convenience above all else, two-income families, the elderly and the disabled.

HEButt has indefinitely postponed its plans to open its home shopping Web service, which was slated to start in Austin TX this month. The company Web site is being revised, but there is no timetable for the shopping launch. HEButt postponed its launch due to soft demand for online grocery shopping, as demonstrated by difficulties encountered by pure plays, not because of technical difficulties. Employees associated with the project have been reassigned elsewhere in the company. Webvan recently announced that it was closing its Texas operation, which analysts believe took the pressure off HEButt's introduction. The HEButt Web site will be redesigned and relaunched, but without the shopping component.

GroceryWorks.com's minority owners are suing majority owner Safeway for damages. One newspaper reports the online operation will be out of capital by May and minority holders think Safeway has not lived up to its alliance terms. Minority holders believe Safeway only wanted the technology and violated agreements by not reselling groceries at its cost, by failing to promote the GroceryWorks logo on the shopping bags and trucks of Tom Thumb and Randalls, and by selling flowers and prescriptions on its own Web sites instead through GroceryWorks. Safeway said the suit is without merit.

> Source: *St. Louis Post-Dispatch*, February 26, 2001. Schnucks' low-key Internet grocery site delivers success where others have failed, by Thomas Lee. *SN*, March 5, 2001. H-E-B Puts Its On-line Shopping on Hold, by Dan Alaimo, p. 1,58. *Executive Technology*, March 2001. HEB Puts On-Line Shopping on Hold, by Dan Alaimo, p. 45. *PG Daily News*, March 12, 2001. Report: Safeway Named in Lawsuit Filed by GroceryWorks.com Minority Owners. *SN*, March 19, 2001. GroceryWorks Shareholders Seek Damages from Safeway, by Elliot Zwiebach, p. 1, 50.

Editorial Alert: Despite high profile troubles at pure plays, some retailers are stepping up their e-commerce operations. Ingles (North Carolina) launched an online grocery shopping service for its Georgia market area. The debut of ingles2go.com comes on the heels of PublixDirect's Atlanta expansion and Webvan's withdrawal from the area. Carolinas' Piggly Wiggly is also jumping into the South Carolina and Georgia market area with www.thepig.net using technology from ShopEaze Systems. See Food Distributor *for an excellent summary of where pureplay and land-based operators currently stand on their B2C efforts. (*SN Daily News*, March 7: Ingles Markets Launches On-line Grocery Shopping. March 20: Piggly Wiggly Carolina Launches On-line Shopping.* Food Distributor*, March 2001. Groceries on the Internet: A Tough Sell, by Carole Edwards, p. 23-7.)*

Seattle & California Dreaming ?!

Britain's Sunday *Times* reported in early March that Wal-Mart and Amazon ceos are working on a deal that will be announced within six months. Neither company would comment, but the *Times* said that Amazon would become Wal-Mart's e-commerce supplier and Wal-Mart would gain access to the e-tailer's expertise in managing the retail chain, from online ordering to home delivery. Wal-Mart would provide Amazon with needed cash, presence in Wal-Mart's 4,500 stores, and a percentage of the sales made through the retail sites.

The Wall Street Journal subsequently cited 'a person familiar with the matter' saying that a deal is not likely anytime soon, but not ruling anything out. Amazon's stock price soared more than 25% on the rumors, while Wal-Mart investors saw little effect. The stock price changes underscored the desire e-tail investors have for some positive news. Analysts believe Amazon will have a tougher time with suppliers as its cash reserves dwindle. Wal-Mart.com, however, is not without aspirations. The company acquired editorial assets of Garden.com and is looking at other faltering e-tailers for distress pricing on bits and pieces that could add to its site.

History would make Amazon and Wal-Mart strange bedfellows: (1) Amazon is already the order fulfiller for Toys 'R Us, a Wal-Mart competitor in the toys category. Wal-Mart, as the world's largest retailer, is not likely to form an alliance with a company so closely allied to a competitor. (2) There have been lawsuits between the two companies about calling Amazon 'the Wal-Mart of the Web' and recruiting Wal-Mart info tech employees.

Business Week sees advantages for both Amazon and Wal-Mart…and customers. Shoppers would win because they would get 'unprecedented choice of how to buy, receive and return merchandise.' Amazon would win because it would get visibility beyond the Net, in Wal-Mart stores, and be able to acquire customers more cheaply. Amazon would also gain Wal-Mart's inventory management expertise. Wal-Mart could gain from e-commerce expertise necessary to make its Web store a serious contender. Problem: their customer bases are so different.

Executive Technology suggests that this could be the 'next step in high-profile partnerships and the engagement of the biggest players...in the multichannel war...in retail.'

> Source: *Reuters*, March 4, 2001, Wal-Mart, Amazon.com in strategic talks. *MSNBC*, March 5, 2001. Wal-Mart, Amazon.com in talks/ Deal expected in less than six months. *The Wall Street Journal*, March 7, 2001. Amazon

and Wal-Mart Have Discussed An Alliance, but No Deal Is Likely Soon, by Nick Wingfield & Ann Zimmerman, p. B6. *PG Daily News*, March 7, 2001. Amazon, Wal-Mart: Talking the Talk, But Not Walking the Walk (Yet). *SN*, March 12, 2001. Wal-Mart and Amazon Talking About Linking Up…, p. B6. *Business Week*, March 19, 2001. Amazon + Wal-Mart = Win/Win, by Rob Hof, p. 42. *Executive Technology*, March 2001. The Wal-Mart-Amazon.com Alliance, by Marc Millstein, p. 6. Wal-Mart, Amazon to Partner? by Jo Fleischer, p. 8.

Netgrocer.com solution

Shari's Kitchen is a new interactive meal planning option available through NetGrocer.com. It allows shoppers to browse a database of recipes and then simply 'click-to-buy' ingredients. The database now features 200 recipes.

Source: *SN*, March 26, 2001. NetGrocer Unveils Meal Planning Service, p. 4.

Meltdown at Webvan continues

Deloitte & Touche, Webvan's auditor, included a sentence in the company's annual report saying that Webvan 'has suffered recurring losses and negative cash flows from operations that raise substantial doubt about its ability to continue as a going concern.' Such language is part of a standard clause that auditors use when a company's ability to stay in business through the year is in question. Spokespeople for Webvan say (1) Plans are in place to sharply cut its capital reserve burn rate, but the company sees the need to raise $5-$15 million in capital in the fourth quarter to make it through the end of the year. (2) Delisting from the NASDAQ is likely on April 12, since the company was warned on January 12 that its common stock had to sustain a minimum bid price of $1 or more for at least 10 consecutive trading days, which has not happened. To avoid this, the company can institute a reverse stock split. (3) Webvan will 'vigorously' defend itself against the suit filed by Amazon.

Amazon.com, 6% owner Webvan after its acquisition of Homegrocer.com, has sued Webvan for breaching a marketing contract between the two companies. Amazon is requesting $6.25 million plus attorneys fees and expenses because HomeGrocer breached its advertising agreement with Amazon. In November 1999 Amazon agreed to promote HomeGrocer's service via e-mail messages to Amazon's customers. In exchange, HomeGrocer agreed to pay Amazon $10 million in eight quarterly payments of $1.25 million each. In December 2000, Webvan notified Amazon that it would stop the payments and Amazon stopped promoting Webvan's business through e-mail messages earlier this year.

On Friday, April 13, Webvan announced the resignation of George Shaheen, the ceo recruited from Andersen Consulting in September 1999. He concluded 'a different kind of executive is needed to lead the company at this time.'

Source: *The Wall Street Journal*, April 3, 2001. Webvan Auditors Question Grocer's Ability to Continue, by Nick Wingfield, p. B6. *PG Daily News*, April 3, 2001. Online Grocer Foresees Grim Future. *San Francisco Chronicle*, April 4, 2001. Webvan Near Collapse, Auditor Says, by Carrie Kirby. *Seattle Times*, April 4, 2001. Webvan facing end of road? by Monica Soto. *SN*, April 9, 2001. Auditor Says Webvan Needs More Capital Soon, p. 6. *Associated Press*, April 13,2001. CEO of cash-starved Webvan resigns, by Michael Liedtke. *The Wall Street Journal*, April 13 (Web)/16 (paper), 2001. Shaheen Resigns as CEO, Chairman of Troubled Internet Grocer Webvan, by Nick Wingfield, p. B7. *The New York Times*, April 16, 2001. Early Defector to a Dot-Com Is Leaving Online Grocer, by David Leonhardt, p. C2. *E-Commerce Times*, April 13, 2001. Webvan CEO Shaheen Resigns, by Jon Weisman. *SN*, April 23, 2001. Shaheen Exits Webvan, p. 6. *The Standard*, April 2, 2001. Webvan, Check Aisle 5 for a Lawsuit: The Net grocer is sued by Amazon for allegedly breaching a marketing contract, by Miguel Helft. *SN Daily News*, April 5, 2001. Reports: Webvan Fast Running Out of Money.

Changes at HomeRuns.com

HomeRuns.com will more than double its delivery charges in an effort to become profitable next year. The closely held company will raise service charges to $5.95 from $2.50. (Last month, its competitor in Massachusetts—Peapod—raised its rates.) Along with the fee hike, HomeRuns introduced Sunday deliveries—for $10.95, due to higher labor costs on that day. Although HomeRuns offers a double-your-money-back guarantee on products and waives service fees for late deliveries, it is weather permitting. The company has instituted the higher fees and other changes, including a revamped Web site, to lead to profitability this year in the Boston market and in early 2002 in Washington DC.

Robert Tarr, ceo-HomeRuns, acknowledged in a rare interview with the *Boston Globe* that HomeRuns.com will need to raise $20-$30 million in today's 'less than favorable' climate. HomeRuns was formally 'orphaned' from Hannaford last year when New York investment firm Cypress Group put up $100 million and a new management team. HomeRuns.com today still gets the bulk of its groceries from Hannaford at wholesale price. Tarr believes that in the long run all online grocers will have retail partners. HomeRuns currently offers 10,000 SKUs, compared with Peapod's 8000, in Boston. It has eliminated bottle and can recycling—but not service to inner city neighborhoods in its quest for profitability.

> Source: *Boston Globe*, March 27, 2001. HomeRuns.com hikes service charges, by Stephanie Stoughton, p. F1. April 5, 2001. Dot-com survivor, by Stephanie Stoughton, p. 1.

The Web: Online ordering adds to sales growth

According to a University of Minnesota Food Industry Center Survey among 344 randomly selected stores, those that had implemented online ordering had higher median sales growth: 4.4% versus 1.7%. However, other variables also influenced sales and other performance measures: (1) Chains of between 31 and 60 stores grew fastest at 3.6%, with chains of other sizes growing less than 2% on average. (2) Although warehouse store sales growth is negative, they have high labor productivity and sales per square foot. (3) More efficient space, labor and inventory management result directly from emphasizing best practices in supply chain and human resources management. (4) Although wholesaler-supplied stores can be competitive, self-distributed stores have higher turns. (5) Supercenter competition stunts growth: stores competing with supercenters grew an average of 0.7%, compared with stores without supercenter competition at 2.1%. The Food Industry Center is inviting another 1600 stores to participate in the 2001 survey.

> Source: *SN*, March 5, 2001. Internet Ordering Capability Spurs Sales Gains..., p. 24. *RetailTech*, March 2001. Jury Out on B2B Exchanges, by John Snyder, p. 31-2.

Emergence of 'dot-bams'

Datamonitor predicts the US online grocery sector will reach a market value of $26.8 billion by 2005—assuming both online and offline players raise consumer awareness to drive adoption. The data comes from a report entitled *Online Grocery in the US 2001*, and estimates a compound annual growth rate of 108.6% from $0.8 million in 1996 to $1.5 billion in 2000. Roadblocks to immediate growth are lack of brand awareness—and supermarket skill at building it—and lack of knowledge of Web sites.

Datamonitor predicts 'dotbams' (bricks-and-mortar retailers in online shopping services) will emerge as key players because they will provide (1) a full range of grocery items and (2) a more flexible and less expensive order fulfillment through store pick-up. The dotbams will also be able to leverage their existing brand, current customer base and preexisting infrastructure—which will result in lower costs and quicker profitability. Datamonitor also foresees joint ventures between leading online service providers, including Amazon, and land-based grocers.

> Source: *PG Daily News*, April 4, 2001. $26.8 Billion Up for Grabs in Online Grocery Market. *SN*, April 23, 2001. Lack of Awareness Cuts On-Line Sales: Report, p. 24.

Albertson's moves to store picking

Twelve months after opening a single combination store/fulfillment center in the Seattle area, Albertson's is moving to a five-store picking system. The new system is based on the successful Tesco home shopping program pioneered in Britain. Simultaneously, the company is broadening assortment in meat by 53%, bakery 38% and general merchandise by 59%.

Source: *SN Daily News*, March 30, 2001. Albertson's Shifts Online Shopping To Store Pick System, by Dan Alaimo. *Executive Technology*, April 2001. *Albertson's Dot-Com Shifts to New System, by Dan Alaimo, p. 29. SN Daily News*, April 20, 2001. Albertsons.com's New Format to Run Out of Five Stores.

Profitability at Peapod this year

In its 10K filing with the SEC, Peapod acknowledged that it still needs substantial additional capital for 2002. The filing, which indicated that Peapod is researching ways to fund its business plan from 2002 on, said it can't be certain that the additional financing will be available on favorable terms, or at all—despite its increased credit line ($50 million, up from $20 million) with majority owner Ahold. Peapod now has more than $60 million in cash resources and anticipates its cash needs to be $50 million for this year. Also stated in the filing: Chicago operations will become profitable by the middle of the year, along with one East Coast market.

Source: *Dow Jones Newswires*, April 3, 2001. Peapod Sees Need For More Capital In 2002.

Tesco hunting for US partner

Speaking at the *Supermarket News/Executive Technology* Summit, Tesco executives revealed the company has been (1) actively seeking a US joint venture partner and (2) testing online shopping with two unnamed North American retailers. Although Tesco has recently expanded to Ireland and will enter Korea, where Internet penetration is also high, it sees the US as its primary target since Tesco brings experience with an inter-store-network. Tesco wants a 40-50% stake, so along with expertise, it is bringing capital. Based on experience in Britain, Tesco believes the right US operation can be even more successful because US supermarkets carry more SKUs than British ones, and basket size improves with more SKUs. Other US advantages: lower labor costs, higher picking productivity, lower delivery vehicle costs.

Source: *SN*, April 2, 2001. Tesco Eyes U.S. Market For Online Grocery Venture, by Dan Alaimo, p. 36. *Executive Technology*, April 2001. Tesco Eyes US Market for On-Line Grocery Venture, by Dan Alaimo, p. 25, 32.

Carrefour hedges e-business bets

Carrefour has launched its second online shopping operation, Carrefourdirect.com, for shopping in Lille and Orleans, France, and uses the Tesco store-pick model. Delivery is offered the next day for about $10, and 6000 food and nonfood items are available. Its first Web grocery store, Ooshop.com, assembles orders from dedicated distribution facilities.

Source: *Progressive Grocer*, April 2001. Carrefour goes direct, Global update, p. 12.

Rest in peace: Kozmo.com

Kozmo.com joined the dot-com graveyard this month when it shut down operations in nine cities. Founded in 1997, it made its name delivering movies and snacks in New York City before expanding elsewhere. During its short life, it got cash infusions from Amazon, Softbank, Oak Investments and Flatiron Partners, some as recently as January 2001—but none were enough to keep it going. At one time the company operated 16 distribution centers with 3500 employees and hoped to go public. Catalogs with limited snacks, movies, CDs and high-end technology equipment arrived in New York area homes as the obituaries appeared in local papers. Those with 20/20 hindsight observe that even if Kozmo had been able to corner the last-minute delivery business, the business would not have been sufficient to support the $280 million investment.

Source: *The Wall Street Journal*, April 12, 2001. Web Delivery Firm Kozmo Shuts Down, by Julia Angwin, p. B10. *The New York Times*, April 13, 2001. Behind Kozmo's Demise: Thin Profit Margins, by Jayson Blair, p. B7. *wsj.com*, April 17, 2001. Strategy, Inefficiencies Hurt Kozmo, Say Its Competitors in New York, by Stephanie Miles. *US News & World Report*, April 23, 2001. The takeout takedown, by Kit Roane, p. 42.

Grocery Gateway: Profitable?!

Grocery Gateway—a Web grocer serving the Toronto, Canada area—claims it will break even on its deliveries within 60 days. Management attributes its ability to do the so-far-impossible to its minimum order size $60, minimum delivery fee of $8 and conservative strategy of serving only one limited geographic area. Skeptics familiar with the situation do not accept the statements at face value, noting that the company timed the announcement to coincide with (a) Webvan's woeful annual report announcement and (b) its first geographic expansion—two days a week of deliveries an hour away from Toronto.

Source: *Toronto Globe & Mail*, Wednesday, April 11. E-grocer soon to break even on deliveries, by Patrick Brethour. *SN Daily News*, April 16, 2001. Canadian On-line Grocer Hopes to Break Even on Delivery.

Webvan: Restructuring and more

After the resignation of ceo George Shaheen, Webvan announced a series of changes designed to keep it afloat: (1) Atlanta operations will be terminated. The company had already enlarged the delivery window to 60 minutes, after building this facility costing about $35 million. Georgia state law prohibiting home delivery of alcoholic beverages hampered profitability, since 7% of Webvan sales tend to be in this category. Consumer response was also generally cooler to the service than in other areas. Webvan also plans to leave Sacramento and Dallas this year as well. (2) The company will lay off 300-400 people in its Foster City CA and Kirkland WA facilities, as well as the 485 in Atlanta. (3) There will be a 25:1 reverse stock split to prevent action from the NASDAQ, which threatened delisting because the stock had traded below $1 for more than 10 consecutive trading days (actually several months). (4) New Economy board member Timothy Koogle of Yahoo will be replaced by new ceo Robert Swan—of Old Economy General Electric. One venture capitalist will be replaced by another.

These actions should preclude the need to go to capital markets for additional funds during 2001. Webvan did burn through significant cash reserves—in the first quarter, it reduced capital from $212 million to $115 million. First quarter 2002 will require about $25 million. The company will continue to operate in San Francisco (its original market), Portland/Seattle (territory inherited from its HomeGrocer acquisition) and Southern California. After the initial restructuring announcements, Webvan auctioned off $1.3 million in kitchen equipment (at about 42 cents on the dollar) and decided to sublease an idle $25 million facility in the Seattle area. Both outlays were from the days when it planned to compete with HomeGrocer.com. Webvan does continue to lease unused property in New Jersey and Baltimore.

Webvan emailed its customers the first week in May answering the oft-asked question 'how can I ensure Webvan's survival?' The answer: Buy more and buy more often. It also announced a late spring introduction of Webvan rewards, a program for big customers to win free deliveries and other bonuses.

Further announcements confirm that George Shaheen will profit for life from losing his job. His severance package includes annual payments of $375,000 for life and to his widow.

The stock price fell on these announcements from 14 cents to 10 cents. At the same time, the company reported a loss of 18 cents a share compared with 17 cents last year.

Source: *The Wall Street Journal*, April 26, 2001. Webvan Group Sets Initiatives for Recovery, by Nick Wingfield, p. A3, A10. *The Standard*, April 27, 2001. Webvan Crashes, by Miguel Helft. *SN*, April 30, 2001. Webvan Quitting Atlanta, Searching for More Capital, p. 46. *The Wall Street Journal*, May 1, 2001. Webvan's 'Candid Call,' p. B5. *Executive Technology*, May 2001. Will Anyone Step Up to Save Webvan? p. 6. *Seattle Times*, May 23, 2001. Webvan shifts gears, fixing Kent center for lease, not new home, by Monica Soto. *CNET News.com*, May 22, 2001. Webvan cuts fat to bring home some bacon, by Greg Sandoval. *SN*, April 30, 2001. GroceryWorks Shifts to Store-Based Fulfillment, p. 4.

GroceryWorks closes distribution centers

GroceryWorks.com, on-line grocer of which Safeway is a majority owner, will close its distribution centers in Dallas and Houston TX. Deliveries will be assembled in Randalls and Tom Thumb stores—also owned by

Safeway. Benefits according to a company spokesperson: getting deliveries to people faster, lowering drive times and using the same drivers to the same neighborhoods every day. Store-based fulfillment was tested in Austin before making the decision to close the distribution centers, which cost between $10 and $12 million to set up.

GroceryWorks employees will work in Safeway stores to assemble the orders. Although there is no off-the-shelf technology for store picking, GroceryWorks estimates that store picking can assemble six orders at a time at a cost of about $100-150. The warehouse model offered 11,000 items; through Safeway stores about 35,000 will be available. Still, skeptics argue that with store picking, there is less control over items being in stock and the challenge of hiring employees to do the picking and delivery.

> Source: *SN*, May 14, 2001. GroceryWorks Closes DCs, Shifts to Store Fulfillment, by Dan Alaimo, p. 23, 26. *LocalBusiness.com*, April 27, 2001. GroceryWorks.com revamping model in fight for survival, by Wayne Carter.

Peapod/NetGrocer alliance

Beginning May 15, Peapod will use NetGrocer.com for its national pack and ship delivery service, replacing 'Peapod Packages' for shoppers outside Peapod's local delivery areas. Shoppers who select 'Peapod Packages' from the Peapod home page or enter a ZIP code out of Peapod's local service areas will be linked directly to Netgrocer.com, where they can shop for all of their non-perishable household staples. NetGrocer delivers non-perishables and other goods via Fedex. Financial terms were not disclosed.

Separately, but perhaps more important, Peapod announced that Chicago, its first market, has reaches operating profitability—and three months ahead of schedule. Connecticut and Long Island should reach profitability by mid-year.

> Source: *E-commerce News*, May 7, 2001. Peapod's Loss Is Netgrocer's Gain, by Beth Cox. *PG Daily News*, May 8, 2001. Peapod Partners with Netgrocer.com. *SN*, May 14, 2001. Peapod Aligns with NetGrocer for Shipping, p. 4. *SN*, May 21, 2001. Peapod: Next Profitable Markets in NY Suburbs, by Nancy Brumback, p. 4.

Editorial Alert: For a quick recap of all the excitement in the last year surrounding dot-com grocery companies, see Progressive Grocer, *May 2001. (Thick as a brick, by Barry Janoff, p. 87-8). Those listed in the graveyard include Streamline, Priceline's WebHouse Club, ShopLink, UrbanFetch and Kozmo. HomeGrocer was acquired by Webvan, which is teetering at the entrance to the graveyard at this writing. The survivors are GroceryWorks—which can thank Safeway for its majority investment, Peapod—now part of Royal Ahold, as well as some operations started by the bricks-and-mortar retailers Publix, Albertson's, Kroger and Tesco, which proudly touts its operation as reaching profitability. Analysts attribute the demise of the pure plays to underdelivering in convenience, value and reliability. Multi-channel operation—bricks-and-clicks—appears destined to overcome deficiencies of pure plays and add the benefits of established store names and impulse shopping.*

Use the right business model

Roger Blackwell, university professor and e-commerce observer, notes that the problems encountered by Webvan were not technology or service-related, but rather that shoppers were unwilling to pay for the true costs associated with the service. He offers the following advice on surviving in the online grocery order-delivery arena: (1) Focus on 'commerce,' not just 'e,' by mastering inventory management, sourcing, transportation and distribution, customer attraction and retention, warehousing and logistics. Logistics matter as much as Web site design. (2) If consumers are willing to do things for free, a model that over the long term absorbs costs associated with those things is doomed. The majority of shoppers remain willing to pick and deliver their groceries at no cost to the retailer. Webvan could not afford to take on these costs—even to generate trial. (3) New technology is compelling to consumers only if it provides a better solution…and today more than three-quarters of grocery shoppers like grocery shopping and are not looking for a better way to do it. (4) Be sure e-tail strategies match the lifestyles of target segments. In reality, those most interested in home delivery would be working women not home during the day to receive those deliveries and not willing to spend evenings online ordering them. (5) Ensure an efficient strategy if competing in a mature, efficient industry. Fierce competition in the grocery industry is exacerbated by giant companies making it very difficult for newcomers to enter.

Source: *The Wall Street Journal*, July 16, 2001. Why Webvan Went Bust, by Roger Blackwell, p. A23.

Tesco buys into GroceryWorks

Tesco—the largest food retailer in Britain and developer of the much-touted profitable store picking, home delivery model—will begin deploying the model with Safeway in the US. This alliance will replace Safeway's current GroceryWorks operation, which suspended operations June 26 temporarily and will resume under the Safeway name. In Britain, Tesco's online shopping business has almost 1 million registered customers, receives 70,000 orders per week and had 2000 annual sales of $420 million. Tesco will pay $22 million and contribute intellectual property to GroceryWorks, along with taking a 35% stake. Safeway has a 50% stake. Safeway said this strategic change is part of the plan to make GroceryWorks into the biggest online grocer in the US, expanding quickly into all US markets where Safeway currently operates.

Outside the US and the industry, the related talk is about Tesco, not Safeway, and its march to become a more significant global player. Executives at Tesco insist that new products and new markets can accelerate home-country annual sales growth of 6-7% to double digits. Analysts agree but believe the current stock price is too high, discounting start-up costs and inevitable problems. Overseas sales account for only 13% of total sales today, but going global is never easy and not all who have tried have been successful. Further, home shopping is not necessarily a sure-fire sales builder either. Profitability of the model notwithstanding, the failure of several US companies suggests that even the Safeway/GroceryWorks arrangement will be an uphill battle. Brits appreciate the irony that their home delivery model is being exported to the home of the Internet. The *Industry Standard* described the overall status of grocery home delivery as looking 'a lot less high tech' after this deal.

Source: *CNN*, June 25, 2001. Tesco in U.S. online deal. *Dow Jones Newswires*, June 25, 2001. Tesco Enters Online Shopping Tie-Up With US Safeway. *The Wall Street Journal*, June 26, 2001. Tesco, Entering the US's Online Market, to Take Stake in Safeway's GroceryWorks, by Steve Stecklow, p. A18. July 5, 2001. British Supermarket Giant Cooks Up Plans to Go Global, by James Hagerty & James Hall, p. A9. *The Economist*, June 30, 2001. Surfing USA, p. 58. *SN*, July 2, 2001. Safeway to Tap Tesco's Expertise at Net Sales, by David Ghitelman, p. 1, 33. *Industry Standard* , July 16, 2001. Online Groceries: Shop the Tesco Way, by Miguel Helft. *The New York Times*, July 20, 2001. Early Winner in Online Food, by Suzanne Kapner, p. C1, C6.

Ahold buys more of Peapod

Ahold will buy the remaining 42% of Peapod that it does not already own for $35 million. Peapod's board has approved the transaction, which will result in delisting Peapod from the NASDAQ. Executives insist that both Peapod and Ahold have faith in the future of their 'clicks-and-bricks' model. Ahold noted that 'the web-based grocery business combined with a store network under strong local brands will prove to be a powerful concept to attract and retain loyal customers.' The plan was one of several the Peapod board considered for long-term survival. Over its 12 years of existence, Peapod evolved from offline ordering with picking at Jewel stores to online ordering with picking at distribution centers.

Source: *The Wall Street Journal*, July 17, 2001. Ahold Will Buy Rest of Peapod for $2.15 Per Share..., by Sarah Ellison, p. B3. *The Wall Street Journal*, July 23, 2001. Online Grocer Peapod Feels Chill Of Its Rivals' Failure, by Amber Holst, p. B6. *SN*, July 23, 2001. Ahold to Launch Offer for All Peapod Shares, by David Ghitelman, p. 8.

Winners...overlooked by association

The Wall Street Journal summed it up: 'Traditional Grocers Feel Vindicated by Webvan's Failure.' Others, however, may be less complacent. Some e-tailers have generated significant returns for 2001 through July 6, basically under the radar screen because of all the focus on the failures. Among them: Priceline up 496% (since exiting the grocery business and focussing on airline tickets), delia's up 362%, FTD.com up 357% and Expedia.com up 340%. In attempting to avoid the freefall among e-tailers, fund managers flocked to infrastructure plays during the same period…they were down 67% as a group.

Source: *Business Week*, July 23, 2001. E-tailers Are Clicking, by Lewis Braham, p. 73.

Webvan/R.I.P.—July 9, 2001: Final days

By the opening of the business day on July 9, 2001, the word was out that Webvan had shut down operations and planned to file for protection under Chapter 11 of the U.S. Bankruptcy Code. There will be an orderly wind down of its operations and sale of its assets and business, just days after shareholders at the annual meeting had voted on a 25:1 reverse stock split in hopes of avoiding NASDAQ delisting. In preparation for that meeting, a *Seattle Times* reporter interviewed Robert Swan-new ceo of Webvan. Key acknowledgements: (1) Webvan no longer had aspirations about being a major national player. (2) Commitments are important. (3) What keeps everyone going, despite underwater options, is continued positive customer feedback.

In the formal announcement days later, Robert Swan explained that although cost cuts had been implemented and the cash burn rate reduced, the number of orders received second quarter 'declined considerably,' making capital needs immediate. About 2,000 workers will be terminated as a result of the announcement. Since there are no funds for severance, these employees are grateful to the anonymous source who is providing a $900 'gift' for everyone. Former ceo George Shaheen will be less happy, since he must stand in line with other unsecured creditors for the $375,000 he was supposed to receive for life as part of his severance package.

Source: *Seattle Times*, June 26, 2001. Webvan curbing appetite for growth, by Monica Soto. *Associated Press*, June 29, 2001. Webvan looks to shareholders in last-ditch effort to stay on Nasdaq, by Michael Liedtke. *The Wall Street Journal*, July 2, 2001. Webvan Group Inc., p. B9. *The New York Times*, July 3, 2001. Webvan Shareholders Approve Reverse Split, by Susan Stellin, p. C6. *The Wall Street Journal Interactive*, July 9, 2001. Webvan Shuts Down Operations, Plans to Seek Chapter 11 Protection. *The Wall Street Journal*, July 10, 2001. Webvan Joins List of Dot-Com Failures, by Mylene Mangalindan, p. A3, A6. *The New York Times*, July 10, 2001. An Ambitious Internet Grocer Is Out of Both Cash and Ideas, by Saul Hansell, p. A1, C10. *US News & World Report*, July 30, 2001 Requiem for Webvan, by Randall Stross, p. 39.

Webvan demise: Potential beneficiaries

Peapod is benefiting from Webvan's Chicago closing and taking over its customers in Chicago, the only market where the two operators faced off. Peapod spokespeople say their orders doubled the day the shutdown was announced. Albertsons.com reported a 300% increase in orders in Seattle resulting from the Webvan shutdown there. An upcoming study from IBM consultants predicts that by 2004, there will be sufficient demand in some metro areas to support three profitable online operations.

Ever the optimist, Terry Drayton, the founder who left HomeGrocer a month before it was sold to Webvan in June 2000, said he had offered to buy back the HomeGrocer.com name and a Webvan facility in Seattle. Drayton contends Webvan's problem was poor management and that he could build a profitable Portland/Seattle online grocery delivery service for between $10 million and $15 million. He acknowledges there might be a problem getting investors.

Pacific Bell Park—home of the San Francisco Giants—has also been swept into the Webvan demise. In March 2000, Webvan outbid rival Safeway for a three-year contract to emblazon the ballpark and cupholders with its name. The contract is paid up through this year, and valued in the millions. While the ballpark avoided agreements with dot-coms, this is the second time (Petco was the first) it has had to resell advertising rights. Webvan stock certificates (obtained by investors early on) sold for over $100 on eBay after the bankruptcy (until the illegal practice was halted) as collectibles, advertised as 'great item to own from the Internet era.'

Source: *Dow Jones Newswires*, July 9, 2001. Peapod In Talks To Acquire Webvan's Chicago Customers, by Erik Ahlberg. *Chicago Tribune*, July 9, 2001. Rival Peapod stands to gain from demise, by Ameet Sachdev. July 18, 2001. What killed Webvan was bricks, not clicks, by Jorge Rufat-Latre, p. 21. *San Jose Mercury News*, July 11, 2001. HomeGrocer.com dreams of relaunch following Webvan's demise. *The Wall Street Journal*, July 11, 2001. Traditional Grocers Feel Vindicated by Webvan's Failure, by Devon Spurgeon, p. B4. *The Wall Street Journal*, July 12, 2001. It Ain't Over Till…, by Ann Grimes, p. B5. *SN Daily News*, July 11, 2001. Albertsons.com Expands Service in Seattle Area After Webvan Shuts Down. *The New York Times*, July 15, 2001. Doing Reverse Splits to Avoid Delisting, by Michael Brick, p. BU8. *Business Week*, July 23, 2001. Commentary: Webvan Left the Basics on the Shelf, by Linda Himelstein & Gerry Khermouch, p. 43. *Time*, July 23, 2001. E-Grocers Check Out, by Chris Taylor, p.65. *The New York Times*, July 19, 2001. Mining a Dot-Com Disaster of eBay Sales, by Todd Lappin, p. G3. *SN*, July 16, 2001. As Webvan Fades, Net Companies Soldier On, by David Ghitelman, p. 1, 6.

HomeRuns/R.I.P.—July 12, 2001

On Thursday, July 12, online grocer HomeRuns.com shut down in Boston and Washington because of lack of funding for continued operations. Relative to the media noise surrounding the Webvan demise, this was a quiet event: a short press release provided no details about numbers of customers, orders or employees, but thanked loyal customers. Founded by Hannaford Brothers in 1996, Homeruns never reached profitability and controlling interest was ultimately sold in January 2000 to Cyprus Group for $100 million. Peapod wins again since it operates in the Boston area as well. Peapod created special advertising to attract HomeRuns customers.

Source: *Ideabeat.com*, July 12, 2001. HomeRuns.com Death Largely Remains A Mystery. *PG daily News*, July 13, 2001. Online Grocer HomeRuns.com Folds. *Boston Globe*, July 13, 2001. Online grocer abruptly closes, by Stephanie Stoughton, p. 1. *Dow Jones Newswires*, July 13, 2001. Peapod Sees Growth After Another Web Grocer Checks Out, by Erik Ahlberg. *SN*, July 23,2001. HomeRuns Shuts Down..., by David Ghitelman, p. 8.

*Editorial Alert: Both Wal-Mart and Kmart will buy out minority venture capital partners in their online operations. Describing the move as 'more evolutionary than revolutionary,' saying a lot has changed in 18 months and wanting greater bricks-and-clicks synergy, both firms' executives declined to discuss details but were careful to praise existing operations which will remain in California. (*The New York Times*, July 24, 2001 Wal-Mart Assumes Compete Control of Its Online Store, by Constance Hays, p. C2.* The Wall Street Journal*, July 24, 2001. Kmart and Wal-Mart Aim to Purchase Balance of Shares in Their Internet Sites, by Ann Zimmerman & Any Merrick, p. B2.)*

Webvan: Postmortems from an investor and user

Writing as an early investor, a user of the service and *Fortune* technology columnist, Stewart Alsop loves the concept of Webvan. But in his postmortem, he credits management stupidity with the company's downfall. Among the missteps: (1) Rebranding and repainting the trucks while the company was hemorrhaging. Alsop attributes this gaffe to the company not being run by entrepreneurs, who would have been more tightfisted and less image-conscious. (2) Excessive infrastructure, which Alsop saw after he was invited by ceo Shaheen, but was met by someone else who showed him the facility and all the features that were mothballed because of insufficient volume. Alsop believes that a seasoned grocery executive with Web savvy could have led the company properly.

Source: *Fortune*, August 13, 2001. The Tragedy of Webvan, by Stewart Alsop, p. 52.

Webvan auctions: Too little and late

Webvan raised $3 million from bidders in the Atlanta area for its plastic tote bins, company T-shirts, office equipment, kitchen equipment, two delivery trucks, and a Volkswagen. Two more auctions are planned for Baltimore MD and Oakland CA.

The company is hoping to make more from the auction of its business units, technology platforms and other assets before the August 27 bidding deadline. The crown jewel is Webvan's technology, which includes a range of functions from a completely integrated e-commerce platform to supporting warehouse management and delivery operations. Also on the block: HomeGrocer's technology platform. Even after these auctions, Webvan does not expect to have any funds for stockholder distribution.

Source: *PG Daily News*, August 13, 2001. Webvan Soliciting Bids for Assets. *Ideabeat*, August 13, 2001. Bankrupt Webvan Picks Up $3 Million At Auction.

Webvan: Lessons learned

Based on insights from consultants, industry insiders and outsiders and behavioral scientists, *Grocery Headquarters* concludes there are three lessons learned from the demise of Webvan: (1) Grocery orders don't fulfill and deliver themselves. (2) Consumers don't want to totally alter their existing shopping habits. (3) You can't be everything to everyone. *Frozen Food Age* thinks it was simpler than that: Webvan's model did not cover its costs, despite the fact that shoppers have long been willing to pay extra for convenience. They do it at convenience stores everyday.

Source:*Grocery Headquarters*, August 2001. Is there life after Webvan, by Alison Paddock, p. 57-60. *Frozen Food Age*, August 2001. Dot's All, Folks, by David Wellman, p. 8.

Editorial Alert: There's no more free breakfast, lunch or dinner from Peapod. The online grocer announced that even orders over $100 (formerly with free delivery) would carry a $4.95 service charge beginning September 1. Service will expand in Washington DC through Giant Food. PublixDirect will begin delivery in parts of Florida for $7.95 in September; Atlanta in spring 2002. Customer pickup plans are on hold as Publix hopes to meets 80% of consumer needs with delivery within a 90-minute window. (SN, August 13, 2001. *Peapod Expands..., p. 4.* Ideabeat.com*, August 23, 2001. Free Of Competition, Peapod Cuts Out Free Deliveries.* Atlanta Journal-Constitution*, August 23, 2001. A fresh approach, by Renee Degross.)*

Target & Amazon: Bricks-and-clicks

Another alliance between bricks-and-clicks has been announced: Target will begin selling merchandise on Amazon.com and next year Amazon will handle distribution, customer service and technology for Target's online sites. Target (including the Target and Marshall Fields divisions) executives say their products will receive broader Web exposure through Amazon, a Web site that claims 35 million customers. Next summer, Target-owned Web sites will relaunch using Amazon's e-commerce technology platform, allowing them to outsource the 'vast majority' of online product distribution and some call-center functions. Target executives believe this will allow for faster online expansion than if handled independently.

Under a five-year agreement, Target will pay Amazon per-unit fees and annual fixed fees. The companies also said they will share some revenue, without disclosing exact terms. Because of existing Amazon agreements with other retailers, Target will not be able to sell baby products, health and beauty goods, luggage, or toys via its Amazon store, although it can direct shoppers to Target.com for these categories.

Source: *Minneapolis Star Tribune*, September 12, 2001. Target to sell products at Amazon.com store, by Melissa Levy.

Labor: possible key to online viability

Inc magazine, crediting Booz-Allen Hamilton's operations practice, has whittled the decline of the online grocery business down to three factors. Despite the fact that the business grew from $200 million in 1999 to an estimated $1 billion in 2001, selling groceries is a low-margin business that depends on three things. So far, no online player has the key to all three—explaining the downfall of several online grocers.

The reasons are: (1) Buying power: smaller players did not have it. Peapod has achieved it through Ahold, reducing acquisition costs of groceries by 2%. (2) Marketing expertise: To date, no players have convinced shoppers to do more than try the various services. While some are more loyal than others for dry groceries or staples, average purchasers return to online grocers only every three months, rather than the 2+ times per week they visit a store.

(3) Labor: supermarkets emerged to cut down on labor, and in fact, shoppers themselves account for a major contribution to labor by filling their own carts and getting the goods into their kitchen cabinets. Herein lies the truth: technology in the end may be able to perform some of the labor tasks…but unlikely all. And delivery costs unpalatable to shoppers may be the last straw.

Source: *Inc*, September 30, 2001. Incubator: Food for Thought, by John Case, p. 44-6.

Webvan's legacy

Global retail intelligence consultants at PricewaterhouseCoopers believe the failure of Webvan has given new life to regional online grocers. Specifically, the failure of the 'national' operation suggests that the existing infrastructure of traditional grocery retailers may well be the edge required for long-term success. The consultants fault the Webvan model with requiring a major shift in consumer shopping behavior—something that happens very slowly. The online ordering aspect was not the major behavioral shift required, rather it was planning to be home and waiting for the delivery. Key targets remain those with special dietary needs, mobility problems or lifestyle preferences. Other online ordering models that offer store pickup are judged to be more viable. Further, the group expects Tesco to move beyond its US Safeway alliance, perhaps making an acquisition.

Webvan received bankruptcy court approval to sell its software, technology and related assets to Kaiser Permanente for $2.65 million. Kaiser's HMO unit bid on the software and other intellectual property after Webvan founder Louis Borders withdrew his earlier $2.5 million bid. Kaiser plans to use the software and other assets to distribute pharmaceuticals.

Separately, the Alameda County Food Bank will miss Webvan: the defunct grocery distributor contributed 10% of the total food it received. Now the food bank is looking to bricks-and-mortar retailers to pick up the slack.

As its swan song, Webvan is referring former West Coast customers to WhyRunOut.com. Webvan's former customers may elect to have their personal shopping histories and home addresses turned over to WhyRunOut and must sign up by October 24—after which time all Webvan data will be deleted. WhyRunOut fulfills grocery orders in Southern California from six Pink Dot stores and transports groceries for Stater Bros. in Orange County. Webvan referred shoppers to Peapod elsewhere.

Source: *SN*, October 8, 2001. Stores May Succeed Where Webvan Failed, by Dan Alaimo, p. 24. *Seattle Post-Intelligencer*, October 4, 2001. Webvan's sale of assets to Kaiser is approved. *Business Week e.biz*, October 1, 2001. They'll Miss Webvan, p. EB4. *Ideabeat*, October 8, 2001. Webvan Sells Technology Assets. *CNET News.com*, October 16, 2001. Webvan delivers customers to start-up, by Greg Sandoval.

Publix home delivery: In-house model

Florida-based Publix debuted its online ordering Web site, PublixDirect.com, to Broward County residents and hopes to expand service shortly from South Palm Beach County to North Dade County and later to Atlanta and Orlando. Previously the company acknowledged that online ordering could eventually account for 20% of sales, thus justifying the $51 million spent on development.

Key elements of the business according to *The South Florida Sun Sentinel* are: (1) The site carries about 9,000 items, versus up to 40,000 SKUs carried in typical stores. (2) A separate fulfillment center, not existing stores, handles delivery. (3) Coupons are not currently accepted. (4) The minimum order is $50.00, plus a $7.95 service fee (waived for the first 30 days of the test). (5) Deliveries are made every day except Friday, and customers can choose a one-hour delivery window; shoppers have to be home to accept delivery. If a customer is not home, another time will be scheduled, with a redelivery fee of $7.95. If no redelivery time is set, there is a restocking fee of $20.

After test driving the site, Ideabeat.com says the color scheme, while familiar and comforting, may be too bland. And some type is too small to be easily read, likewise pictures. Ideabeat.com suggests that nutritional information should be given more prominence and that the site should be linked to store operations—a conscious decision the company has made, but which might change after the test period.

Source: *Ideabeat*, September 28, 2001. PublixDirect.com Debuts, Testing Grocery E-Tailing Service. *Ideabeat*, September 28, 2001. Site Of The Week: PublixDirect.com Goes Online, by Kevin Coupe. *SN*, October 8, 2001. Publix Launches Online Service, p. 4.

Outsourcing home delivery

Third-party online shopping providers—application service providers—have largely been under the radar screen with the ramp up and free fall of Webvan, Streamline and the like. IDS (Independent Delivery Systems) counts Bashas, Marsh and Roundy's among its clients. MyWebGrocer boasts Unified Western Grocers, Dorothy Lane, Lowes Foods and D'Agostino. Recently Harris Teeter shifted from IDS to MyWebGrocer, fearing financial problems at IDS.

As recently as June IDS had notified its customers that it had lost funding and was in search of alternate financing. At that time, Bashas, Marsh and Roundy's provided the necessary funding—demonstrating their support of the operation. Terms of the deal were not disclosed. All three cite a significant point of differentiation that builds their confidence in the IDS model: it supports phone and fax orders in addition to online ordering.

According to IDS, the company was profitable as of July in part because fees were renegotiated by store rather than per order. IDS disputes the proposition that an ASP can cover its costs by using a per-order revenue model alone. Independent researchers suggest that these ASPs need 650 to 700 stores to be profitable, although MyWebGrocer says its model breaks even at less than half that level.

Source: *SN*, October 8, 2001. Fearing Financial Difficulties, Harris Teeter Switches to MyWebGrocer, by Dan Alaimo, p. 28.

Editorial Alert: For those who have not seen enough details and diagrams about the Tesco and Peapod models, two articles may satisfy appetites. Business Week e.biz *offers a detailed review of Tesco's operation. The article shows how $58 million spent over four years compare with Webvan's $1.2 billion in one year. Currently, the biggest concern is pickers clogging the aisles for traditional shoppers and more.* Progressive Grocer *shows a floor plan of Peapod's Norwalk CT operation, which is concentrated on the second floor of a conventional store. The article details picking, scheduling and deployment of deliveries. (*Business Week e.biz, *October 1, 2001. Tesco Bets Small—and Wins Big, by Andy Reinhardt, p. EB26-32.* Progressive Grocer, *October 2001. Click by Brick, by Jenny Summerour, p. 28-34)*

Peapod reimburses shoppers

Peapod's 5000+ Massachusetts customers will receive about $4 for every $1 they were allegedly overcharged in a settlement announced this month. Without admitting wrongdoing, Peapod settled charges of misleading customers about its pricing policies, agreeing to pay $200,000 in restitution and $100,000 in legal costs. Peapod was not owned by Ahold at the time.

The issue: whether Peapod was involved in deceptive advertising. Participants in the class-action suit claimed that Peapod originally told shoppers that its online prices were the same as those at the Stop & Shop supermarkets. Subsequently, the Web site began charging 10% more than the stores, without disclosing the increase. Peapod blamed an internal communication flaw. Currently, the Web site specifically states that prices at Stop & Shop stores may be different from online prices.

The bigger issue, of course, is the long-term viability of online grocery shopping. At the time the case was filed, Peapod offered free delivery which is no longer. Also as a wholly owned subsidiary of Ahold USA, actual operating costs may prove difficult to track.

Source: *E-Commerce Times*, December 13, 2001. Survival of the Internet's Sneakiest Grocer? by Keith Regan. *FoodLogistics.com*, December 11, 2001. Peapod and Stop & Shop to Compensate Boston-Area Customers. *SN*, December 17, 2001. Peapod Settles Price Suit, p. 4.

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