Case #02 - Ebay/Paypal/Amazon - the story of online commerce (1995) [SH]

There are few things in life that are guaranteed to cause as much worry as money. People need to feel safe when they spend it, safe that they are getting a good deal, safe that the money isn't wasted, safe that their credit card details aren't being scammed. People need to trust the monetary transactions that they are involved in, and without trust, commerce, in the shop or on the web, will not thrive. The eBay and Amazon story demonstrates how this trust was developed, and then embedded, in the online world.

In 2012, when we think of online commerce we think of Amazon, eBay, iTunes or any number of online stores selling anything from shoes to groceries. But purchasing possibilities outside of the High Street still existed prior to the Internet, such as mail order catalogues or special offers in newspapers and journals that could be cut out, filled in and sent with a money order to buy x-ray specs or a set of royal wedding memorial plates. A certain trust had been established in the way payment systems were set up, with cheques and money orders being part of a recognised framework that as close to guaranteed something would turn up on your doorstep in the weeks following an order (whether the x-ray specs would work or not was another matter).

The spread of credit cards from the U.S. to Europe in the 1960s saw a new method of shopping come into the mainstream. Plastic credit cards required the establishment of trust on the part of both issuing banks and consumers. The familiarity bred by the purchasing of goods with 'plastic' and without cash was essential to the development of the online economy, as it was important that early adopters could quickly feel they were engaging with reputable businesses, in the same way as they could on the high street. People needed to feel that their details were safe (PBS, 2004; Wang and Emurian, 2004; Metzger, 2009).

The development of SSL Encryption in 1994 delivered this safety and has remained essential to supporting trust in e-commerce ever since (Verisign, 2010). In the beginning, the first businesses to recognise the trust issue went on to gain a stranglehold on the market. eBay, for example, was there at the beginning, and is still one of the most trusted Internet brands today. From humble beginnings in 1995 through to 97 million active users and total assets of over USD27bn at the end of 2011 (eBay, 2011; Locke, 2011), it, more than any other site, showed that people wanted to partake in commerce online, they were comfortable selling and buying to/from strangers, and that very often they wanted to buy the strangest, most niche of items (Woyke, 2011). With online payment processor PayPal standing beside eBay as a trusted partner and guardian of credit card details, plus a unique eBay rating system that allowed users to post feedback on both buyers and sellers, thus offering that all important trust factor, Internet users felt freer than ever before in indulging their shopping needs online (Nielsen/NetRatings, 2005).

Meanwhile, none of this had escaped the attention of Jeffrey Bezos, a computer science graduate and entrepreneur from New Mexico. Bezos knew an opportunity when he saw one and he founded a company selling books online at a massive discount. This company, Amazon, quickly grew, taking advantage of a unique feature of the early World Wide Web — regulation of online commerce was in its infancy and a 1992 U.S. Supreme Court ruling prohibited a state from forcing a business to collect sales tax unless it had physical stores in that state (Poggi, 2011). Amazon was incorporated in 1994 and today it is the world's leading e-commerce site with an established brand that makes it a first stop shop for online purchases. E-commerce itself was first popularised as a term in the mid-1990s, and once eBay and Amazon had taken it to the masses, online salesmen and women — and consumers — never looked back.

By the millennium, e-commerce had gone way beyond the selling of books. Larger consumer goods, such as televisions and stereos were on sale via Amazon and elsewhere by 1999, followed soon by property and automobile sales (Amazon, 2011). At the same time, however, new thinking was needed to explain the ease with which the Internet was satisfying more esoteric needs — Chris Anderson coined the term 'Long Tail' in 2004 to describe how even the strangest tastes could be catered for online, as previously hard to find goods and services started being offered by specialist sellers that previously might have languished in a back alley in Soho only selling second hand vinyl to the crowd that knew (Anderson, 2004).

This 'clicks and mortar' moment, when offline stores embraced the possibilities offered by being online, marks the point when e-commerce became embedded in all business. Services — banking, insurance, travel agencies — had to have an online services division or become redundant in the face of competition. By the year 2000, fuelled by a surge in online adverts such as banner ads, online advertising in the U.S. was worth USD8.1bn and surfers could hardly move for commercials trying to sell us one thing or another (Evans, 2009; Arandilla, 2011). Traditional secondary businesses, such as transportation, were being revolutionised as a result of delivery activity — supermarkets even started offering home delivery options for groceries, proving that there really was no sector e-commerce couldn't touch (Tedeschi, 2002; McKinnon, 2003).

By the second decade of the 20th century there literally isn't anything you can't buy online. The online advertising industry — worth USD21.2bn in 2007 but USD55bn in 2010, and today largely dominated by the world's biggest search engine Google — drives us there with increasingly personalised ads (Evans, 2009; Business Insights, 2012). Gold. Diamonds. Babies (Associated Press, 2009). Drugs (Reuters, 2012). You can even get together with like-minded individuals through services like Groupon to drive the price down and get a better deal on your aerobics lessons or two-for-one pizza. What's more, you can do all of this on a mobile phone, through a never-ending stream of apps that making purchasing easier, quicker, trusted.

Importance

Aside from letting us get our hands on more stuff, far more easily, the real importance of the e-commerce explosion is the development of security and trust online. Payment processor PayPal, now wholly owned by eBay, has over 100 million users and reported revenue of over USD4bn in 2011 (PayPal, 2012). E-commerce platforms such as Amazon and eBay are now almost the bedrock of the World Wide Web. It's certainly difficult to imagine life without them, even if they are not yet 20 years old. And it's this familiarity that shows us another equally important outcome of e-commerce: it has created a new order, and new commercial giants that have caused chaos to established players and indeed threatened to turn the global economy on its head.

Existing businesses that dealt in easily digitised cultural products — music, movies, books — suffered badly from the advent of e-commerce. Giant record labels and music publishers, guardians of huge amounts of artists' rights and some of the best known songs of the 20th century utterly failed to manage the shift to a digital marketplace and were left watching as a technology company — Apple — developed the iTunes sales platform for digital music in 2003 and took a cut from every one of their online sales. The personalisation that new e-commerce platforms offered—

wishlists and recommendations, or iTunes genius playlists — all contributed to the deepening loyalty to the new vendors. This is a key lesson from the story of e-commerce: sound business plans in the offline world don't necessarily translate to an online space where a more personal touch is expected. Furthermore, without a secure technology platform to offer one's goods, there will be a reliance on those who know how to operate in the new environment.

Once trust in online commerce had reached critical mass, consumer expectations began changing. When searching for digital goods such as music, immediate access was seen as essential or else users could turn to easily accessible illegal versions — prior to the launch of iTunes, illegal file-sharing Napster had over 20 million users (Jupiter Media, 2001) Territory ceases to be an issue for the online sale of physical goods as well — or at least it should. eBay members may sell all over the world if they so choose, and Amazon delivers worldwide. There are no inherent technological restrictions on digital files being transferred globally either. However, copyright licensing issues and Digital Rights Management (DRM) create frustrating territorial and technical restrictions and it has become the natural reaction of some customers to start looking at easier alternatives. The rise of piracy is discussed in another case study later in this paper.

But if consumers had expectations about services, the market and its investors also had expectations too. The tremendous rise in e-commerce was not the only factor in the bursting of the dot-com bubble in 2000, but a factor it was (German, 2012). Many new businesses attempted to get on that gravy train, and many were swept away in a flood of crushed hopes and wasted investment capital. Just as old business models needed new technology platforms to survive, a new technology platform alone was not going to be enough to keep a company's head above water. Just ask Webvan or Boo.com (Lanxon, 2008). While the bursting of the bubble managed to bring more than a few people back down to earth however, the goldrush feeling hasn't quite gone away, and the idea that a new startup should monetise itself as soon as possible, with a medium-term view to a public stock offering, is still prevalent in the environment today (Halliday, 2012; Salmon, 2012).

What is clear is that those who do make it to the IPO and are successful, like Amazon, or eBay, are embedding themselves further into many users' day to day Internet experience — for example, in June 2011 one in five global Internet users visited the Amazon site (Comscore, 2011). In doing so, they are acting in similar ways to ambitious companies in the pre-Internet age. Throughout its development, Amazon has been carefully diversifying, moving from the sales of books through to other goods, branching out in the digital sale of music and then employing its masterstroke, the development of the Amazon Kindle (The Economist, 2012). The Kindle, the world's most popular e-reader, allows Amazon to begin taking control of another part of the new information environment, by manufacturing and selling devices intended to host digital content that it is being sold….by Amazon. But there is more besides – in 2011 Amazon became a bona fide publisher with a stable of big name authors, all of whom will write for Amazon, and exclusively sell through Amazon in exchange for contracts that make their previous ones look positively 19th century. The world's biggest publishers, the so-called Big Six, have been gazumped (Streitfeld, 2011).

Right now, the mainstream Internet is being developed under the guidance of those who made it during the e-commerce boom, not those who were big in the days of analog. Although sales tax could soon be applied to Amazon and their competitors in the U.S., these new companies have taken their seat at the top table and are lobbying for preferential treatment to keep them there. The old guard will fight back, but it is unclear what they will be able to achieve. In this fight, consumers will trust those who give them what they want when they want. They don't want goods crippled by DRM, or territorial restrictions. In other words, they will trust those who have been most successful at reproducing a superior offline shopping experience, online.

It is Internet users who have the most to gain from this situation. Once trust was established, users felt free to explore their niche interests online in a commercial sense, and to feel comfortable in their positions of instant access, wherever they are and on whatever device. This freedom is crucial in understanding how users will react to the future stages of the Internet's development — there will be no wish to go back to times of limited choice and scarcity. The level of participation and personalisation that e-commerce also gives the consumer must be considered, for it was eBay that gave users the option to be buyers and sellers (and Amazon that copied this system in its Marketplace offering), and to post feedback on their purchases (ditto). These feedback systems are now part of online life, and extend to all areas of Internet activity.

There is another point to consider when looking at how e-commerce has affected user expectations online. As trust between consumers and vendors developed, consumers have shown themselves more than willing to give up personal information about themselves and their shopping habits, if they feel there is a return for them in this transaction. Amazon in particular has pioneered this approach to online shopping, and tries to direct consumers on to ever more purchases 'they might like' every time an item is purchased. Generally, consumers seem happy with this state of affairs, enjoying the serendipitous purchasing opportunities it offers, and trusting the Internet giant not to abuse its position by making nefarious use of their data. This situation — comfort with an invasion of privacy in exchange for a good deal — is an important factor to take into account as we move forward to consider the future development of the Internet.

Set against this, it is not clear how comfortable the majority of large pre-Internet businesses are, particularly if they were in the business of selling content. If anything, the 18 years since the founding of eBay have seen big businesses struggle to scale when it comes to online commerce, never quite finding the Goldilocks business model for the Internet age. Businesses whose product easily translates to zeros and ones, such as the legacy entertainment companies in the music and motion picture sectors, have struggled to move online, and Amazon's expansion has seemingly impacted on every other sector from white goods to office products.

But for those businesses that were savvy enough to keep up there is plenty to be cheerful about. The Internet has provided a new frontier that keeps on giving, first by enabling startups to take advantage of previously inaccessible tax loopholes, then with its ability to enable them to sell a niche product, and finally by supporting a seemingly never-ending production line of new computers and mobile devices that can all be configured to sell us things in new, exciting ways. The bravest can even try the newest of business models, from the freeconomy to the type of social buying facilitated by Groupon and its ilk. Combine this with the attitudes of the modern, net-savvy consumer and it would seem that these businesses are likely to be feeling more comfortable than some of those in the recorded music or publishing industries.

Standing on the outside of this and looking in are, of course, the world's governments. With a traditional role in the modern capitalist economy as something of a hands-off regulator of business, governments have had to watch the development of e-commerce with what must be enthusiasm on the one hand and trepidation on the other. Clearly, anything that ploughs new energy into the commercial sector will be viewed as a good thing, but with large businesses, particularly those in the creative sectors, often very closely tied in with major political machines, there will also be forces mobilising in government that seek to protect the status quo — or at least give industry time to catch up and develop a viable business plan for the Internet age, whenever that will be (Masnick, 2012).

Supporting start-ups is a great way for a government to show it cares about business on the Internet. Getting to the point where a suitable legislative framework can be constructed to nurture new digital businesses is another thing however, particularly when there are high streets to protect and established copyright-based content industries to consider. This is the conundrum that needs to be addressed, because finding a balance between the two will be difficult if not impossible. Perhaps the biggest struggle for governments going forward is to ensure that they have enough people working in policy development who actually understand the issues, and are able to make sensible decisions to benefit both vendors and users — without throwing the baby out with the bathwater.

Where are we now with e-commerce? It is here, it is established. Trust in online retailers exists, and there is no going back. Of course, the rise of Amazon, eBay and other e-tailers poses problems for the established, those who were there and powerful before online shopping and secure transactions became ubiquitous. This will undoubtedly be cause for concern for the boards of Sony BMG, or Harper Collins, but it won't matter much to the consumer. For they are the real winners in the story of e-commerce.