Beyond the Exchange

The Future of B2B
by Richard Wise and David Morrison

To see how business-to-business commerce will evolve on the Internet, you need only look at the revolutionary changes that have transformed financial markets in recent years: an influx of specialists, a proliferation of creative business models, and a new set of challenges for buyers and sellers. Here's a road map for what's ahead.
THE USE OF THE INTERNET to facilitate commerce among companies promises vast benefits: dramatically reduced costs, greater access to buyers and sellers, improved marketplace liquidity, and a whole new array of efficient and flexible transaction methods. But if the benefits are clear, the path to achieving them is anything but. The B2B market is still in its infancy, and its structure and players remain in rapid flux. Despite breathless press coverage, very little is known about how business-to-business commerce will evolve on the Internet.

The high level of uncertainty is causing widespread anxiety among executives—and for good reason. Whether as buyers, sellers, or both, all companies have substantial stakes in the business-to-business marketplace. Their supply chains, their product and marketing strategies, their processes and operations—even their business models—will be shaped by the way B2B relationships are formed and transactions are carried out. Yet at this moment even the most basic questions remain difficult for companies to answer: Which exchanges should we participate in? Should we form a trading consortium with our competitors? Should we demand that our suppliers go on-line? What software should we invest in? Executives understand that the wrong choices could have dire consequences, but they also know that in the fast-paced world of the Internet they need to act soon or they’ll be left behind.

Fortunately, there is a model for the future shape of B2B: the financial services industry. Characterized by information-based transactions, large and liquid exchanges, and intense competition, financial markets closely resemble the new B2B markets. But unlike their B2B counterparts, the financial markets have been around for centuries. Their evolution provides important clues to the likely evolution of B2B. In particular, the recent restructuring of the financial industry suggests that, counter to the common wisdom about B2B today, exchanges are not the primary source of value in markets that are information intensive. Rather, value tends to accumulate among a diverse group of specialists that focus on such tasks as packaging, standard setting, arbitrage, and information management.

We will use the financial services industry as a window into the future of B2B. We will show why the current exchange-based model is structurally flawed, examine the major trends that will influence the strategies of both entrepreneurs and established companies, and describe the key market players that are likely to emerge and the roles they’ll play. The future we envision is already coming into being. New B2B players are now emerging with business models that mirror those that have come to define and dominate the financial industry.

The Flaws in the Exchange Model

Most B2B activity to date has centered on on-line exchanges and auctions, and most observers have assumed that these electronic marketplaces would come to dominate the B2B landscape. Once you look beyond the hype, however, you quickly see that most Internet exchanges are floundering. They suffer from meager transaction volume and equally meager revenues, and they face a raft of competitors. One of the leading chemical exchanges, for example, has seen its postings grow considerably since its launch in early 1998, but it’s still processing less than one trade per day. The hard truth is that few of these exchanges will ever create the liquidity needed to survive.

The current B2B model has three fatal flaws. First, value proposition offered by most exchanges—competitive bidding among suppliers allows buyers to get the lowest possible prices—runs counter to the best recent thinking on buyer-seller relations. Most companies have come to realize that getting supplies at the lowest price may not be in their best economic interest. Other factors, such as quality, timing of deliveries, and customization, are often more important than price in determining the overall value provided by a supplier. (That’s particularly true for the many manufacturers that have adopted lean, low-inventory production systems that depend on reliable, precisely scheduled shipments of supplies and components.) Many companies have spent the last two decades methodically forging tighter, more strategic relationships with suppliers—many such affiliations have involved joint product-design efforts, integration of complex processes, and long-term service contracts. The on-line exchanges’ focus on arm’s-length, price-driven transactions flies in the face of all this hard work.

Second, the exchanges deliver little benefit to sellers. Yes, suppliers have access to more buyers with only a modest increase in marketing cost, but that benefit is overwhelmed by pricing pressures. Few suppliers want to be anonymous contestants in ruthless bidding wars, and for the highest-quality, most innovative suppliers, price battles are anathema. As a result, the buyer-biased exchanges that characterize B2B today will not be able to achieve a critical mass of participants and transactions—they will be forever starved of liquidity. To be successful in the long run, B2B markets need to offer strong incentives to both buyers and sellers.

Finally, the business models of most B2B exchanges are, at best, half-baked. In their rush to get on-line, the

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companies that run the exchanges haven’t taken the
time to study their customers’ priorities in-depth, create
distinctive offerings, or even map out paths to profit-
ability. They’ve simply used off-the-shelf software to set
up simple auctions as quickly as possible. Because the
software is readily available and relatively cheap, the bar-
riers to entry are low, and the resulting proliferation of
new exchanges is undermining the margins of all play-
ers. Indeed, the influx of new entrants is leading to the
same type of market fragmentation that exchanges were
designed to overcome in the first place.

The current B2B model, propped up by cheap invest-
ment capital, is not sustainable. As the markets mature,
they will have to evolve in ways that fix the problems of
the existing system. New structures will enable buyers
and suppliers to form tight relationships while still
enjoying the reach and efficiency of Internet commerce.
Rewards will begin to flow to sellers as well as buyers.
And new business models will provide profits in a world
of dirt-cheap transactions. The B2B business will, in
other words, reshape itself to resemble the financial
services industry.

Four Formative Trends

Until recently, business-to-business markets had little in
common with financial markets. But with the spread of
digitization and, in particular, the Internet, B2B com-
merce has taken on many of the characteristics of finan-
cial trading. Greater market liquidity and transparency
have enabled more efficient pricing and more effective
matching of buyers and sellers, and, most important,
value has shifted from the product itself to information
about the product. While the transfer of physical goods
may remain the end result of a business transaction, the
information that shapes the transaction—price, availability, quality, quantity, and so
on—can now be separated and exchanged
electronically. And that information is often
more valuable to companies than the under-
lying goods.

Over the last two decades, as deregula-
tion and digitization have swept through
financial services, the industry has gone
through a radical restructuring. Traditional brokerage
and banking channels have been dismantled, and trans-
action fees have fallen precipitously. As a result, power
and profit have migrated away from centuries-old busi-
ness models toward a wide variety of innovative and
often highly specialized new models. Four major trends—
good predictors of how B2B commerce will evolve—have
combined to reshape the industry.

From Simple to Complex Transactions. To fulfill
complicated financing needs, a company once had to
forge a close working relationship with a major bank
that could offer tailored loans. Even though the process
of customizing a financing package was time consum-
ing, expensive, and restricting, there was often no alter-
native. In recent years, however, highly complex financial
transactions have been successfully packaged as securi-
ties that can be freely bought and sold. Securitization
has vastly increased the financing choices available to
companies—and vastly reduced the fees earned by tradi-
tional banks.

Standards made securitization possible. By adopting
universal standards for loan terms and lending parame-
ters, the financial industry enabled more customization
within open marketplaces. Consider the mortgage
market. Traditionally, mortgages were customized loans
handled by local banks. Rates, terms, and lending require-
ments varied greatly. But spurred by the advent of lend-
ing agencies such as Fannie Mae and Ginnie Mae, the
mortgage business has evolved into an efficient national
marketplace of securities, with arm’s-length transactions
between dispersed buyers and sellers. The traditional
bank’s role of generalist, in which it handled every aspect
of a mortgage, has been split into three specialist roles:
origination, a customer relationship task still handled by
local banks or mortgage brokers; securitization, a finan-
cial task handled by Fannie Mae and Ginnie Mae working
with investment banks; and loan servicing, a processing
task handled by large-scale service companies.

We expect to see a similar fragmentation of roles in
the B2B world as markets are restructured to accommo-
date the complex goods and services that account for the
bulk of most companies’ spending. Already, some ex-
changes are repositioning themselves to play narrower
but more lucrative roles. FreeMarkets, best known for
running Internet auctions, is rapidly turning itself into
what might be called a specialist originator—a company
that helps buyers gather and analyze the information
necessary to purchase complex products and services
electronically. FreeMarkets knows that its greatest value
lies not in conducting auctions, which is rapidly becom-
ing a commodity service, but in identifying and qual-
ifying bidders and in creating detailed, standardized
requests for proposals that enable the bidders to provide
comparable quotes even on highly specialized products.
Auctions are becoming adjuncts to FreeMarkets’ primary
role of providing structure, standards, and liquidity for
complex transactions.

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As FreeMarkets handles more transactions, its product descriptions will become more refined and standardized, reducing the investment it has to make in subsequent auctions and expanding the range of auctionable items. It is unlikely, however, that FreeMarkets will be able to retain proprietary control over the standards it is helping create. The experience of the financial industry provides another clear lesson here: while many securitized products, from auto leases to credit card receivables, started out as proprietary inventions, they eventually became routine, widely traded offerings. In much the same way, the standards for describing products for on-line sale will become universal as other exchanges copy FreeMarkets’ templates or as industry-specific standards emerge for describing product and transaction attributes.

As this happens, FreeMarkets’ focus will likely shift to two areas: providing on-line expertise in sorting out which product features best meet a particular buyer’s needs and leveraging its knowledge of qualified suppliers to serve buyers as a demand aggregator. Like a mortgage originator, FreeMarkets will concentrate on the initial qualification, specification, and packaging role, handing off the transaction itself to larger, more liquid exchange partners. (For a business-to-consumer version of this model, see the sidebar “Learning from B2C: MySimon.”)

From Middlemen to Speculators. As financial markets became more competitive, transaction fees steadily eroded. Stock trades that used to generate fat commissions, for example, are now executed for a few dollars—or even for free. The disappearance of transaction income has set off an intense search for new sources of revenue, which has in turn given rise to a new set of business models. Instead of extracting fees from transactions, a number of financial services players now make their money by actively trading in the underlying market. Several of the leading investment banks, for instance, have increasingly dedicated their capital and people to investing for their own accounts, and these investments generate a large and growing share of their overall profits. The companies still need to be closely involved in client transactions, but mainly for the information about market trends they provide.

As the profit margins of B2B exchanges get pushed down by competition, some exchanges will start to take their own speculative positions, buying and selling large quantities of the goods traded in their markets. In this “e-speculator” model, running the biggest exchange still provides a source of competitive advantage, but, just as in the financial markets, the advantage comes not from fees but from a superior window into the dynamics of the market. Ultimately, exchanges might even reduce their commissions to a price below zero; that is, they might pay for a flow of deals in order to gain valuable information about the market.
through an array of purchase dimensions, decide which areas are important to them, and then see how well the available offerings match up with their requirements.

Here's how you buy a DVD player through MySimon. First, the Web site provides an overview of DVD players, highlighting key specifications and the most important ways that each model varies from the others. Then, through Active Research's proprietary recommendation engine, MySimon walks you through a real-time trade-off survey assessing the value you place on various features and brands and testing different bundled attributes—all to assess what you care about in a DVD player (Exhibit 1).

The Active Buyer's Guide then recommends several DVD players that best fit your needs (Exhibit 2), lists sites on the Web where those models are available, and shows the prices (Exhibit 3). You can click through to place an order.

Exhibit 2
produces a list of recommendations...

Exhibit 3
sortable by price and linked to purchase sites.

MySimon renders obsolete the value-added role of the trained salesperson and goes beyond the role of the typical e-retailer. Rather than selling the product, MySimon acts as a personal adviser to guide the customer to a source for purchase. The company generates revenues from vendor slotting fees and advertising.

With similar decision-support tools, more complex B2B sales will become feasible on-line. This trend will likely be accelerated by the advent of extensible markup language (XML), a set of software standards for displaying and sharing detailed information such as pricing and product specifications over the Web. Purchase support could become a unique source of value and customer loyalty, with the actual transactions handed off to sites that compete solely on price and availability. Companies such as General Electric and Milacron are already moving to provide more of this decision-making information on their Web sites.
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One pioneer in e-speculation can be found in the financial industry itself. Knight Trading Group, a wholesale market maker for stocks, executes trades behind the scenes for the largest on-line trading firms, including E*Trade and Ameritrade. Knight has invested in a highly automated system that can execute a large volume of trades efficiently, and roughly 40% of all on-line trading now flows through the company. Rather than earning profits through commissions on trades, however, Knight pays the on-line brokers for their order flows. The company uses the order information to analyze market movements and adjust its own positions accordingly. While most exchanges struggle to break even, Knight enjoyed a 35% operating margin and a 68% return on equity for the 12 months that ended with April 2000.

Enron is also using the e-speculator model. Originally a gas pipeline operator, the company steadily expanded to become a major provider of many other energy products. It has recently exploited its privileged position to establish a thriving on-line exchange in which it makes money not from commissions but from buying and selling a variety of energy products, including natural gas, electric power, pulp, and pollution credits, for its own account.

Following the lead of investment banks, Enron is now pursuing the logical extension of the e-speculator model: creating and selling derivatives such as options, futures, and swaps, which allow other market participants to mitigate their price risks. Enron currently transacts $1.5 billion in derivatives per day on-line, and it has been doubling its transaction volume each quarter. These instruments allow the company to profit in two ways. They are lucrative to sell, and they allow Enron to hedge its market positions, decreasing its exposure to trading losses.

From Transactions to Solutions. Decreases in transaction income have also led financial firms to emphasize comprehensive money-management services to enhance profit margins, cement customer relationships, and lock in predictable revenue streams. An early sign of this shift was the rise of mutual funds and asset management services in the late 1980s. More recently, we have seen a proliferation of sophisticated services such as investment planning, tax and estate planning, and tailored investment accounts. In addition to generating substantial returns for the providers, such integrated services have considerable appeal to well-heeled clients, who want to manage the overall costs and returns of their portfolios rather than maximize the value of any one transaction.

The B2B landscape is also well suited to solution providers. By using the Internet to bundle products with related information and services, creative companies can improve the effectiveness and efficiency of their clients’ businesses. By doing so, they will be able to forge strong, long-lasting client relationships that will de-emphasize product price and exchange-based transactions. Early examples of solution sites are now appearing on the Internet. Some are operated by suppliers looking to counter the role of the exchanges; others are portals operated by third-party intermediaries.

An example of the first type is Milpro.com, a site operated by machine-tool manufacturer Milacron. Milpro sells high-margin Milacron coolants, cutting wheels, and drill bits directly to small machine shops. But the site also helps these customers handle a broad array of related business challenges, such as buying and selling used equipment, identifying new business opportunities, and troubleshooting problems. For example, the site includes a software “wizard” that guides customers through a set of questions about a process (such as grinding) and related problems (such as chatter marks) and then recommends particular products, much as an experienced sales representative would. Through such services, Milacron has been able to attract the attention and the business of small machine shops, a group that’s difficult and expensive to reach through traditional channels. Those shops, in turn, gain access to expertise that they could not otherwise afford—and that would not be available through a transaction-focused exchange.

An example of a third-party solution site is Biztro.com, a portal for small-business transactions. Biztro aims to solve small-business managers’ back-office headaches through an integrated suite of applications for such functions as payroll, benefits management, human resources management, and procurement. Biztro has signed deals with a group of product and service providers, including Dell and OfficeMax. The providers are able to sell through the portal, and Biztro earns a commission on the transactions. By providing a high level of convenience, Biztro shifts customers away from purely price-based purchases.

From Buyer-Seller Exchange Transactions to Sell-Side Asset Swaps. With the rise of large, sophisticated market makers and the emergence of digital networks, more and more securities trades are being executed without hitting the floor of a traditional exchange. Many
financial companies, for example, are joining electronic communications networks, or ECNs, in which they can match trades with other participating members, saving them the cost of going through an exchange and allowing them to trade day or night. Charles Schwab has gone even further. It runs its own internal trading operation, enabling it to carry out many mutual fund transactions by simply swapping shares among its customers without involving or even notifying the mutual fund companies. Besides eliminating transaction costs, such internal trading preserves Schwab's control over client transactions and the resulting information.

Similar sell-side swap models are emerging in B2B e-commerce. In stark contrast to most existing exchanges, which tend to penalize sellers, asset swaps benefit suppliers by allowing them to better utilize their key assets—whether factories, trucks, warehouses, or containers for shipping. At the same time, they enable buyers to tap a broader, more efficient supply base.

The swapping model is particularly attractive in highly fragmented industries, where small-scale suppliers often lack a broad geographic reach and are highly vulnerable to fluctuations in demand. The trucking business is a perfect example. Many segments of the trucking market are populated by independents or small firms that cannot individually achieve scale economies, partly because of the unpredictability of their routes. Unable to coordinate pickups and deliveries among their own small sets of customers, truckers routinely return from deliveries without cargo. That means higher costs for the truckers and higher shipping fees and slower delivery times for their customers.

Most B2B Web sites in the trucking business don't help truckers address these problems. Instead, they use auctions to pit carriers against one another in cutthroat bidding wars, which only exacerbate an already bad situation. Transportal Network, in contrast, uses the Internet to allow carriers to trade capacity with other

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The Emerging B2B Landscape

1. **Mega-exchanges** act as central hubs for the execution of most transactions and for buyer-supplier communication.

2. **Specialist originators** standardize and automate the buyer decision-making process for more complex products and then send the transactions to the exchanges for execution.

3. **E-speculators** participate in or run exchanges, gaining real-time information in order to take direct or derivative market positions.

4. **Solution providers** operate separately from open exchanges by embedding the product sale in a suite of unique, valuable services.

5. **Sell-side asset exchanges** gain efficiency by swapping and reselling orders among a closed set of suppliers.
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Carriers, filling those empty trucks and creating a better system for all involved. In conjunction with its asset-swapping service, Transportal also offers truckers the ability to pool their purchases of employee benefits and insurance, parts and equipment, financing, and other products, enabling them to gain scale advantages without losing their independence. Customers, meanwhile, benefit from a stronger, more efficient base of carriers.

New Business Models

The restructuring of the financial services industry took two decades. The changes will happen much more quickly in B2B e-commerce, where regulation is thin and competition is already intense. As the trends we've described play out, B2B commerce will be structured very differently from the way it is today. (See the exhibit “The Emerging B2B Landscape.”) Rather than being dominated by monolithic exchanges, it will encompass several distinct, interdependent business models.

Because scale and liquidity are vitally important to efficient trading, today's fragmented and illiquid exchanges will consolidate into a relatively small set of mega-exchanges that will occupy the center of the B2B universe. Although most transactions will flow through them, they will not generate much profit or shareholder value. As transaction fees fall or disappear entirely, the exchanges may turn into nonprofit collectives. (See the sidebar “For the Traditional Exchange, a Collective Approach.”) Many B2B players will maintain stakes in the exchanges for the benefit of more lucrative e-commerce endeavors such as origination or speculation.

Surrounding the mega-exchanges and plugged into them in various symbiotic ways will be the specialist companies. Originators such as FreeMarkets will structure and take orders for complex transactions, aggregate them—bundle them into large order requests—and send them to mega-exchanges for execution. The originator role will be most valuable in markets with relatively expensive products that are neither commodities nor completely customized, such as automotive and aircraft components, industrial equipment subassemblies, and complex services such as insurance.

To be successful, an originator will need to concentrate initially on creating standards for trading complicated products and providing real-time support for customers on-line. An originator will be able to achieve an advantage by understanding a complex product category and customer decision-making parameters better than its competitors; it will also benefit by adeptly using configuration and decision-support software. Profits will come primarily from commissions and from slotting fees paid by vendors and exchanges in return for preferential positions with the originator, much as food manufacturers pay slotting fees to grocery chains for prime shelf space. Many of the niche portals already in operation will likely use their knowledge of narrow business communities to move toward an originator model.

Savvy e-speculators, seeking to capitalize on an abundance of market information, will tend to concentrate where relatively standardized products can be transferred easily among a large group of buyers. They'll also look for price volatility, which will provide trading spreads. Expect to see e-speculators in markets for specialty chemicals, paper, and certain basic auto parts.

To thrive, an e-speculator will need to develop strong financial and risk-management skills. A speculator's advantage will come from having better, more timely market information than other participants. To get that information, it will have to partner closely with at least one mega-exchange or operate as the profit-making arm of at least one.

An Overview of the New B2B Models

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<th>Key enabling characteristics</th>
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<td><strong>Mega-exchange</strong></td>
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<td>• Maximum liquidity</td>
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<td>• Common transaction standards</td>
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<td><strong>Specialist originator</strong></td>
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<tr>
<td>• Complex products</td>
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<td>• Relatively expensive products</td>
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<tr>
<td><strong>E-speculator</strong></td>
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<tr>
<td>• High degree of product standardization or fungibility</td>
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<td>• Moderate to high price volatility</td>
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<td><strong>Solution provider</strong></td>
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<td>• Product cost a small portion of overall costs</td>
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<td>• Product-related issues impact other costs</td>
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<td><strong>Sell-side asset exchange</strong></td>
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<tr>
<td>• High fixed costs</td>
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<td>• Relatively fragmented supplier and customer base</td>
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Speculators will likely earn profits not only by trading but also by creating and selling various hedging instruments.

In many markets, a handful of independent solution providers with well-known brand names and solid reputations will thrive alongside mega-exchanges. Like Milacron, a good number of them will leverage distinctive technical expertise to become indispensable to customers—and thus reduce the importance of price in buying decisions. Many will derive a substantial proportion of their profits from high-margin add-ons and consumables. The solution model will be most common in markets where the product itself represents a small portion of a customer's overall costs but heavily influences those costs, as in specialty chemicals, engineered plastics, and cutting tools. For example, specialty chemical admixtures represent a small percentage of the cost of concrete, but the wrong admixture can cause an extremely costly problem: the cement won't cure properly.

Many B2B transactions will consist of sell-side asset exchanges, in which suppliers will trade orders among themselves, sometimes after initial transactions with customers are made on the mega-exchanges. Sell-side swapping will be most valuable where markets are highly fragmented, both on the buyer and seller sides—where, for geographic or information reasons, demand and supply are often mismatched and where suppliers can benefit greatly from keeping expensive fixed assets fully utilized. Industries with these characteristics include transportation, metalworking, plastic molding, farming, and construction.

A company seeking to pursue the asset-exchange model will need to have strong relationships with the supplier community, since success will hinge on its gaining a critical mass of supplier transactions. It will also need to be adept at understanding supplier problems; sales of products and services that solve them will likely be an important source of profits.

Investing in New Skills

Whether a company is hoping to play a role as a B2B service provider or simply needs to transact business with other companies, it will have to develop a deep

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<th>Sources of profit</th>
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<td>Major horizontal purchase categories</td>
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<td>Electronic and mechanical components</td>
<td>Strong consultative sales skills</td>
<td>Deep knowledge of product category</td>
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<td>Automotive and aircraft components</td>
<td>Deep product understanding</td>
<td>Effective use of decision-support software</td>
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<td>Chemicals</td>
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<td>Replacement auto parts</td>
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<td>Alignment with a major buyer or seller</td>
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<td>Engineered plastics</td>
<td>Problem-solving mindset</td>
<td>Brand strength</td>
<td>Higher product margins</td>
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<td>Cutting tools</td>
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<td>Rich set of offerings</td>
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<tr>
<td>Transportation</td>
<td>Strong supplier relationships</td>
<td>Customer lock-in</td>
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<td>Metal machining</td>
<td>Ability to offer additional relevant services</td>
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<td>Selling ancillary products/services to members</td>
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<tr>
<td>Construction</td>
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knowledge of the emerging landscape and the various business models it will contain. (See the exhibit “An Overview of the New B2B Models.”) As we’ve seen, the players’ value and power will vary considerably depending on the industry and the products involved. Each company will have to create its own path to success—and not all products are suited to Internet transactions: very complex, very expensive items such as aircraft or merger-and-acquisition advisory services will continue to be sold primarily through personal relationships and multistep purchasing processes.

Many of the financial services companies that ultimately profited from the restructuring of the markets were not traditional banks or brokerage houses. They were companies that were able to spot disruptive trends and were willing to reconfigure their businesses, often at high cost and risk, to seize the new opportunities. Charles Schwab is perhaps the best example. Schwab reinvented itself not once but three times: it started as a discount broker, became a provider of asset management and back-office services to financial planners, developed a mutual fund “supermarket,” and then became a hybrid clicks-and-mortar solutions provider combining Web-based transactions with personal advice. Each reinvention required significant investments—such as the recent purchase of U.S. Trust to fulfill the goal of providing asset management solutions—but ultimately increased Schwab’s customer base, profits, and market valuation.

Managers contemplating their next B2B move should take the example of Schwab to heart. Radical changes in markets require radical responses. For many companies, traditional skills in such areas as product development, manufacturing, and marketing may become less important, while the ability to understand and capitalize on market dynamics may become considerably more important. Enron’s experience illustrates the point. In building its e-commerce market-making capabilities, Enron has aggressively brought in new people with new skills. Engineers have been replaced by traders, economists, and risk managers. That kind of change is tough to make, but as Schwab and Enron understand, it’s essential to success. Indeed, in the digital age, timidity is just another word for irrelevance.

For the Traditional Exchange, a Collective Approach

First-generation B2B exchanges, faced with boycotts by suppliers and antitrust scrutiny from regulators, are likely to evolve in two important ways. First, since the best method of achieving sufficient market liquidity is to enlist every participant’s support, the exchanges will move away from being for-profit entities and move toward being collective industry efforts run for the benefit of all.

Second, they will move beyond executing transactions to create the infrastructure and standards necessary to streamline communication between buyers and sellers. This will address pressing issues of efficiency, such as speeding up the flow of product information, automating billing and payment, and linking buyer and seller production processes more closely. And it will allow them to handle not only simple products but complex custom components and services, which account for most business purchases.

Covisint, the automotive mega-exchange hatched by General Motors, Ford, and DaimlerChrysler, is already moving down this path. Conceived as a for-profit enterprise that would earn commissions on the transaction volume generated by its founders, Covisint has changed that proposition in the face of resistance from suppliers. To ensure broad participation, Covisint has opened up its exchange to many other auto manufacturers as equity owners, and 40 suppliers have been given profit-sharing stakes. In their public comments, Covisint’s owners are now talking less about sponsoring auctions and are instead trying to reduce the roughly $140 currently spent to process an average purchase order.

If the automotive industry—where buyers are concentrated and suppliers are fragmented—is moving toward a collaborative exchange model, other industries are bound to follow. Once again, this mirrors a similar evolution in financial markets. Over the past several decades, numerous subscale regional stock exchanges were replaced by two large exchanges, the NYSE and the NASDAQ. Both exchanges operate primarily for the benefit of members rather than to maximize the profits of the exchange, and both have played a key role in developing the information standards and infrastructure for electronic trading and funds exchange.