Week 8: Case Study – EBay


1. Overview of Company
   a. Product of company – provides market-place for customer to customer transactions; mode of transaction – auction (not two-party bargaining but rather many buyers bidding for each item put up by a seller). Secondary product: old-line auction house (Butterfield & Butterfield).
   b. Product sold in the auctions – wide variety of products (more than 8000 categories) and large number of products. Of 265 million items listed for sale in 2000, the percentage breakdown is: collectibles – 32%, sports (gold-topped Alan Iverson card?) – 12%, toys (beanie babies?) – 10%, books – 6%, pottery & glass – 6%, music – 5%, and a bunch of things less than 5% in share. Largest on-line destination for: Computer and Electronics, Used Cars, Toys, Sporting Goods.
   c. Company History – Started in September 1995 Labor Day; grew rapidly in terms of number of registered users and items offered for sale. For example, CEO interview in September reports 5.6 million registered users; in November 1999 there were 7.7 million registered users and today there are 42.4 million registered users (How many is that per day of new additions?)
   d. Pricing – charge a modest price for listing (between 30c and $3.30). Also charges a commission between 1.25% and 5% when an item sells.
   e. Cost structure – little by way of variable costs other than advertising costs although advertising costs are high (details later). Shipping, procurement (manufacture) costs borne by market participants.
   f. Revenues – Has grown rapidly, $372,000 in 1996, $5.74 m in '97, $47.35m in '98 & projected revenues of $223m in '99, $431.4 millions in 2000 ($392 millions of on-line revenue) (Incidentally, the average price is low; currently, $20 per transaction). Some high-price items have moved (Rolls Royce Phantom III Aero Coupe for $955,000 & Chicago Bulls Courtside Season Tickets for $260,000)
   g. Profits – Has grown rapidly but remains modest. $148,000 in '96 to $874,000 in '97 to $2.4 m in '98. Question: why are profits so low if variable costs are non-existent? Answer – marketing expenses have grown from $32,000 to $1.73m to $20m in same time-period. As of 2000, marketing expenses are $166.8 millions, 38.7% of revenues.
   h. Stock price history – spectacular; IPO at $9 in Sept. 98, now $150 & went from $9 to $90 in 10 weeks.

2. Competition
   a. Three sorts of competition – auction sites such as yahoo auctions & amazon.com auctions (also a bunch of smaller ones); old-style auction houses some with a web presence (Sotheby’s & Christie’s); intermediaries in the auction business including auction search engines such as Auction Watch.com & Bidder’s Edge.
   b. Category 1: Yahoo auction crossed 1 million users mark Nov. 1. Also, Yahoo & Amazon have users for other products (& an international presence). FREE
   c. Category 2: Sell higher priced items. Sotheby’s average price per lot is $10,000 (altho’ 80% of lots sells for less than $5,000). Revenues essentially flat; Sotheby’s increased from $337m to $367m between '97 & '98.
   d. Category 3 – smaller but potentially the most threatening for Ebay; an auction search engine searches every site that is listing beanie babies for example. Allows customers to then go to the relevant site.

3. Network Externalities
   a. CEO Whitman – talking about why she thinks Ebay will win out against the competition – “We have the largest market-place by far. That does matter because the sellers want to be where the buyers are and the buyers want to be where the sellers are.” WSJ op.cit.
   b. Price evidence – Ebay charges but Yahoo etc. do not. (Or is that something else such as quality control as Whitman claims?)
   c. Theory: recall, two predictions of the theory: I) initial advantage even if small can matter (recall Q2 > Q1 even by a small amount today can force firm 1 to drop out of the market completely tomorrow – btw, might have been the Christie’s story) and II) the more intrinsic non-network differences exist, the
more likely is the market going to be a competitive market (i.e., the less will competitors drop out). (Go back & check the network externality model carefully).

d. Is Ebay in situation 1 or 2? Maybe 2 because Yahoo & Amazon are offering other services that are not network-related (e.g., books, gifts, etc. in non-auction format).
e. Bigger problem – don’t the search engines create one large public network? (No wonder Ebay is fighting to block access to Auction Watch!)
f. Entry easy? By Ebay’s own admission technology not a problem. With large public network, is entry easier from a financial standpoint as well?

2. Looking Ahead
a. Niched markets – EbayLA, Ebay Great Collectors, etc
b. Real growth might be business to business. How big is tat market & what does Ebay lose by sitting that one out?
c. Prices will begin to fall? Giveaways?