# Entrepreneur Journeys

# From e-Commerce to Web 3.0

## How To Leverage The Evolution Of The Internet

*Sramana Mitra*

To My 1M/1M Team

# Contents

**I want my own digital personal shopper. ASAP.**

*- Sramana Mitra*

# From e-Commerce to Web 3.0

Back in 2007, even before the iPhone was launched, giving us a powerful computer in our pockets or handbags, I started outlining a vision for Web 3.0.

There are numerous definitions of Web 3.0 floating around. Tim Berners-Lee, a father of the World Wide Web, talks about the "Semantic Web," a way that computers employ the meaning of words – not just pattern matching – along with logical rules to connect independent nuggets of data and so create more context for information. The formula that makes the most sense to me is this: Web 3.0 results from combining content, commerce, community and context, with personalization and vertical search. Or, to put it in a handy phrase: Web 3.0 = (4C + P + VS).

Here's what it means.

Web 1.0 was all about driving online commerce and trying to find "anything" in the tangled jungle of the Web. It produced companies like Yahoo!, Amazon.com, eBay, Netflix and Blue Nile. The rush for dollars also resulted in the dot-com meltdown. Even so, people's habits of searching, buying and selling genuinely changed. Today, you will find hundreds of thousands of merchants selling everything from cable organizers, window blinds, clothes, water filters, and everything else under the sun through specialized online stores. Specialty retail, in other words, has made a decisive transition to the web.

Web 2.0 has been primarily focused on social networking through online communities. Facebook, Twitter and LinkedIn, have been the most notable companies to emerge. But there are a plethora of others where you can "meet," "connect" and "make friends" online these days – habits no longer considered weird.

At the same time, we've seen a great deal of investment in vertical search companies. If you are looking for a job, you can go to a site like Indeed.com and search across various job portals and career sites. Or go to Kayak if you've got travel questions, or TheFind if you're seeking shopping advice. In each case, the sites have carefully customized search parameters (job seekers, for instance, can search on salary ranges, locations, job levels and so on). Therein lies the big difference with Google, a generic horizontal search engine.

Finally, Web 2.0 has brought an onslaught of user-generated content in the form of blogs, podcasts, appending comments at the bottom of articles, posting reviews of restaurants, movies, stores, and hotels. Media has become truly interactive, as opposed to the one-way world we were used to. Many more voices are being raised, and heard. The media industry, as we have known it, has been shaken to its roots.

The next wave – Web 3.0 – will organize itself around two different elements: context and the user.

By "context," I mean the intent that brings you to the Web, your reason for surfing. Looking for a job is "context," as is planning a trip or shopping for clothes. Fundamental to context is the user. And when you fuse a specific user with genuine context, you wind up with truly personalized service.

Imagine this: You are planning a trip to Rome. You are looking for a hotel around Piazza di Spagna, but not something large and impersonal – which rules out the Hassler Villa Medici. You like smaller bed-and-breakfasts, with charm, warmth, character. You want an online travel agent who can understand your needs and preferences, and find you not only the right hotel but really interesting restaurants, boutiques and shows all aligned with your taste. Normally, you use Guide du Routard as your travel guide, but today there is still a gulf between travel guides and online travel-booking sites – in other words, content and commerce are fragmented. In Web 3.0, you will see content and commerce finally come together in a big way, no longer forcing you to hop from site to site to get one job done.

On this same trip, you would love to meet local people who share your interests – say, cooking, jazz, opera. In Web 3.0, you will see the community elements of Web 2.0 pulled into context, making it as easy to find new friends with common interests, even in a distant city, as it is to book a hotel room.

Some user-generated content is already evolving into an integral part of travel planning today. At TripAdviser, for instance, travelers report back on their experiences at hotels around the world. The missing element, however, is the notion of the individual user and his or her personal needs. You don't want to read reviews from anyone. You want to read reviews by people whose taste and judgment you trust.

In a Web 3.0 world, then, a personalized travel agent will help you find and book a highly customized itinerary, leveraging all the power of previous generations of Web technology –searching (both generic and vertical), community building, content and commerce. That's how I get Web 3.0 = (4C+P+VS) – the sum of content, commerce, community and context, with personalization and vertical search.

This is complex technology, requiring sophisticated artificial-intelligence algorithms. After all, your Web 3.0 travel agent will not be a "person" but a "bot", or intelligent agent.

But I suspect you will like your travel bot. And your career bot. And your shopping bot. Let's look at a shopping bot, in fact.

I am a petite woman, dark-skinned, dark-haired, brown-eyed. I have a distinct personal style, and only certain designers resonate with it (Context).

I want my personal SAKS Fifth Avenue which carries clothes by those designers, in my size (Commerce).

I want my personal Vogue, which covers articles about that style, those designers, and other emerging ones like them (Content).

I want to exchange notes with others of my size-shape-style-psychographic and discover what else looks good. I also want the recommendation system tell me what they're buying (Community).

There's also some basic principles of what looks good based on skin tone, body shape, hair color, eye color . . . I want the search engine to be able to filter and match based on an algorithm that builds in this knowledge base (Personalization, Vertical Search).

Now, imagine the same for a short, fat, white, red-haired man, who doesn't really have a sense of what to wear. And he doesn't have a wife or a girlfriend. Before Web 3.0, he could go to the personal shopper at Nordstrom.

With Web 3.0, the Internet will be his personal shopper. Aided with ubiquitous, mobile presence, these digital shoppers will anticipate all his needs, all of each of our needs.

So be patient with the technology entrepreneurs around the world, who are working through these generations of the evolving Web, trying to bring about a dramatically better user experience. After all, they – and their bots – are working for you.

In this ninth volume of the Entrepreneur Journeys series, we will spend time with a number of entrepreneurs who have built successful electronic commerce businesses, and explore what we can learn from them. Through their journeys, we will also trace the evolution of the web, extract strategies and tactics to apply to build and grow similar or related businesses.

In other words, we're going to simulate the experience of having coffee with 15 really successful e-commerce entrepreneurs and learning from their journeys.

Enjoy!

# Interview with Valerie Holstein, Cableorganizer.com

*Valerie Holstein's story is a clear case for building self-financed 'lifestyle' businesses that can become quite large. What exactly is wrong with a $16 million revenue, highly profitable niche e-commerce company, other than the fact that you do not have investors breathing down your neck?*

**Sramana Mitra: Valerie, let's start with your background. Where were you born, and where did you grow up? What was the path you took to arrive here today?**

**Valerie Holstein:** I was born in Paris, France. I studied there until it was time to go to college. I decided to attend college in the United States because I wanted to improve my English, and I wanted to take a break from the French academic format. I came to the US as an exchange student and that is when I met my husband.

**Sramana Mitra: Where in the US did you come as an exchange student?**

**Valerie Holstein:** I came to Tampa, Florida in 1993. I enrolled in a community college in Ft Lauderdale. My fiancé and I decided to get married. He was already working because he is 10 years older than me. He was well out of college while I attended college. I did not study very much in community college because they had me take very basic English classes, which I felt was a complete waste of my time and money. As a result I quit college and got a job as a landscaper.

Later on I went back to a private school to study graphic design and web design. I graduated from the institute and I went on to work for a couple of Internet providers. I set up websites for Sandals Beach Club and FedEx Latin America. This was back in the day when websites were hand coded. I was not making that much money, so I went on to work as a drafting engineer for a screen enclosure company. I was making more money because I was allowed overtime. I also worked in the IT department of an insurance company.

I was job-hopping for many years. I was homesick, and I like to go back to France every year. In the US you only get one or two weeks of paid vacation. However, I wanted to take a month every summer, so I basically had to quit my job every year in June. When I returned to the US, I would have to find another job. Even if I took an unpaid leave nobody was interested in having an employee who wanted to have a month off. That was the case until we started CableOrganizer.

**Sramana Mitra: When did you start CableOrganizer?**

**Valerie Holstein:** We actually started the company 10 years ago when I was nine months pregnant with my child. I was still working full-time as a drafting engineer for a screen enclosure company. My husband was working more than full time at Computer Science Corporation. He was a trainer and consultant. He did two years in Toronto, a couple of years in Massachusetts, and he was scheduled to go to Brazil for six months. He was also scheduled to go to Taiwan at the time. I did not see much of my husband. We sacrificed a lot to pay off our house. My husband was working six days a week and I was working five days a week as well as doing extra work on the weekends.

I knew that when my child was born that I wanted to stay home and spend time with my child. I also knew that at heart I was a career woman. I could not be just a stay-at-home mom. I was still independent and felt the need to earn money.

I looked for customer service jobs for a long time with companies like American Express where I could handle calls from home. I was not able to find any job that I could do at home or on the Internet. I eventually gave up and my child was born. My husband and I were in the process of renovating our home office. We had a hard time hiding all the ugly cables we had behind our computers. We had two desktops and a few laptops as well as printers. We had a roommate at the time who had a computer, printer and hubs.

The room itself was very pretty. We had painted and put in crown molding and a new desk. All of the computer cables made the room look ugly. I was looking for products to conceal them, and I could not find anything. I looked for a month and a half and I finally got the idea of putting Velcro straps around the cables to bundle them. I then found a surface raceway at HomeDepot which we were able to stick the bundled cables into.

My husband and I thought that we could not be the only people who had that problem. A lot of people have more than one computer or a media center. There are a lot of cables in American homes. We decided, spur of the moment, to set up a website to tell people about a few products they could purchase to conceal wires. We only had a couple of pages on the website. After about a week I started getting comments on the website. People were asking us where they could buy the products, so my husband and I decided to purchase $40 worth of inventory in our garage, and we started selling the products online.

**Sramana Mitra: In 2002 when you started selling things to hide computer cables, how did people find your website? Was it primarily via your blog?**

**Valerie Holstein:** Yes, it was from the blog. I had a couple of pages that explained the issues we had and what products were helpful in hiding the cables. People started asking where they could find those products. I figured that if people were looking for the products, why not just sell them ourselves? I was hoping we could make a couple of hundred dollars a month. It was attractive because suddenly I had people calling me and asking me for the products. I was happy because it would give me something to do while I stayed home and raised my child.

I had no expectations or goals going into the business. I was dreaming about making $500 a month. A few months later, we started making real money. I had more and more inquiries, and people started referring products to me, hoping that I would carry them on my website. Everything grew via word of mouth. I kept adding products slowly but surely. That prompted me to make phone calls to a few big vendors who accepted our small business. They were large vendors in the cable management industry, and I think they were just tickled by the idea of selling something online. They did not have a lot of faith in it, but they thought it was interesting. They gave us a shot, which let us start distributing products. That put us in a different price bracket because before that, we were buying products at our local hardware store and marking them up to sell on our site.

**Sramana Mitra: How did you finance the inventory?**

**Valerie Holstein:** I just bought retail priced inventory and added a 20% markup. I really did not have to finance that inventory. People had no clue what to look for, so they were willing to pay for the products on our site because I made it easy for people to find what they were looking for. At the time, keyword analysis was not well known, but we focused on a lot of unique keywords that I knew people were using to try to find these solutions. Nobody knew to look for a surface raceway; they had no clue what they were called. I brought a packaged solution to people and they responded. When you make it easy, things happen. I was driven by what the customer feedback was.

**Sramana Mitra: Was this all just you or was your husband working on the business?**

**Valerie Holstein:** He was working on the backend of the business. His specialty is ERP, so he set us up with UPS and USPS. He set us up with a free shopping cart. There are a lot of shopping cart systems out there that are free if you transact under a certain amount of money each month. They are not very sophisticated, but they do exist. Amazon was already there and eBay was there, but nothing else sophisticated was really out there.

**Sramana Mitra: Did your husband keep his job at CSC during this timeframe?**

**Valerie Holstein:** Yes, he did. He was working full time for a year and a half, and I was still working 20 hours a week. We had 1.5 paychecks coming in.

**Sramana Mitra: How much revenue did you generate from CableOrganizer.com during your first year?**

**Valerie Holstein:** I did a little bit under $200,000.

**Sramana Mitra: Wow! That is not bad for a garage, grass roots operation.**

**Valerie Holstein:** Every penny that we made was reinvested in purchasing more inventory. Whatever was not reinvested in additional inventory was saved. We kept everything to pay off our mortgage.

**Sramana Mitra: How many customers were transacting on your site?**

**Valerie Holstein:** At the time, we probably had about 20 customers a day.

**Sramana Mitra: Were they all finding you via Google searches?**

**Valerie Holstein:** Yes. Google and word of mouth.

**Sramana Mitra: Were you aware of search engine optimization and keyword optimization at the time?**

**Valerie Holstein:** I was. By the end of the first year, search engine optimization had come on in a big way. By the end of that year, I had gone in and added it on all of my pages. I did heavy-duty keyword analysis. I went retroactive on my pages, which prompted more business.

At the end of our first year we also had another surprise. Somebody called to congratulate us on our article in the Wall Street Journal. I told them they must be mistaken because we were a very small company and we did not have any PR. Somehow somebody from the Wall Street Journal was writing an article about cable management and came across our site online. They did not call us but they mentioned our products in a one-page editorial. We had 90 sales that day. My husband and I were afraid that they were fraudulent orders, but they were not. We were shocked.

**Sramana Mitra: That also must have driven your keyword ranking up like crazy.**

**Valerie Holstein:** It did. Absolutely. Sometimes things happen that you are not even aware of. You don't know who is watching, and you get great surprises. By the end of the second year, my husband quit Computer Science Corporation so that we could work full time. I had a tough time juggling parenting and running the business. I did not have time to look for a nanny. It was hard to find time to take a nap. I was working from 8AM to 2AM or 3 AM every day. I had to do customer service, bookkeeping and do post office runs every day. I had to put my phone on an answering service so I could take care of next-day air shipments. I would then come back and answer the phone for another three hours. I would then come and take a break between 7PM and 8PM, which is when I caught a nap and got an energy drink. I did not even have time to do grocery shopping. My neighbor helped me out a few times and got me food.

From 8PM until midnight, I would be back on the phones handling the West Coast phone calls. I then had the military folks in Iraq or Afghanistan calling me at 2AM. I would pack orders at 3AM so they were ready for the following day. Once my husband quit his job I was able to dedicate more time to product development. I set up more product pages on our website and the business just grew very rapidly from that point on.

**Sramana Mitra: How much did you do the second year?**

**Valerie Holstein:** Close to $1 million. The third year we did $3 million. Now, we are out of our garage, and we have a 40,000 square foot warehouse. We have 47 employees. We are a global company with revenues at around $16 million.

**Sramana Mitra: You had massive growth from $200,000 in revenue to $16 million in revenue. What did you do in terms of marketing?**

**Valerie Holstein:** Believe it or not, I was not doing any advertising at that time. It was all organic growth and traffic. I could not go fast enough to serve the customer base that we had. I did not have a single minute to think about advertising. We started advertising and making a catalogue in 2005 after we were well into the company.

**Sramana Mitra: How did you do inventory financing?**

**Valerie Holstein:** We did organic financing. We have never been in debt. We do have a mortgage on the current building that we own, but other than that, we have never required financing. All of the inventory is based on revenue and cash. We have maintained that to this day. We have $1.5 million of inventory, and I have never taken debt for it.

My husband was a CPA in a previous life. He is a finance guy. He is one of the best CPA's I know to this day. He has a strong ERP and computing background as well. We were both brought up by parents who did not believe in debt. We don't believe in credit. I do have a credit card, but, we pay it off at the end of the month. To this day, we pay our vendors in advance and leverage that to get an extra 1% to 2% off. We just don't believe in debt.

I have no visibility or clue into what is going to happen with this economy. If I can't afford something now, then how am I going to afford it later with 30% interest and fees added on? I don't like to work that way. We have had plenty of opportunities to work that way; we just don't like to.

**Sramana Mitra: How did you build your team?**

**Valerie Holstein:** About a year and a half into the business I was beyond exhaustion. I could not function anymore. I was working 24/7. I worked weekends and holidays, including Christmas. If the phone rang, I picked it up. There is no 9 to 5 in my world.

After 2001, a lot of my husband's colleagues got laid off. One of them was one mortgage payment away from foreclosure and bankruptcy. We asked him to come on board. We told him that we had the money to pay him on a month-by-month basis only. The salary was low because we could not afford much.

We made the jump to hire him, and it was not an easy decision. The first employee and the first warehouse were both big decisions. We had to make sure we could make enough money to afford and sustain the employee. We knew we couldn't afford not to hire someone because we were growing too fast. If we did not start hiring, we would shoot ourselves in the foot. We would not be able to answer our customers like we should.

Once we hired one person we then grew by 1400% in one year. Once you make that jump, it is much easier to make the decision to hire a second, third and fourth employee.

**Sramana Mitra: What are the functions that you staff for today? Customer support and shipping are obviously key roles.**

**Valerie Holstein:** Right now it is mostly customer service associates and outside sales people. We have a reverse approach to business. We are technically 100% e-commerce, but we recognize that in order to leverage our exposure, we need to go back and find more traditional ways to reach the regional market. The international market is reached easily via the Internet. Over the years we have realized that people still like to be stroked on the back. They like to be visited.

**Sramana Mitra: What kind of customers are you visiting?**

**Valerie Holstein:** Local contractors. Ft. Lauderdale is the Venice of America. The marine industry is very prominent. We visit boat manufacturers as well as all the people who refurbish boats.

**Sramana Mitra: Are you primarily focusing on Ft. Lauderdale and not other markets?**

**Valerie Holstein:** We visit folks in the Tri-County area. Anyone in other locations, like the West Coast, is reached via the Internet.

**Sramana Mitra: Theoretically, however, you could apply that model to sell with contractors in other regions as well if necessary.**

**Valerie Holstein:** We could. We were thinking that in a few years we could open a fulfillment facility somewhere on the West Coast to alleviate shipping cost and shipping delays. That would allow us to be closer to our customers on the West Coast. We also have a subsidiary in France that handles all of the sales in Europe, Africa and the Middle East. That is all e-commerce business.

**Sramana Mitra: How prepared did you feel to take on this business?**

**Valerie Holstein:** I don't have an MBA. I came into this position by default. My husband said "congratulations, you are the President of CableOrganizer.com; get going" and that was it. We took off from there. I had to hire, do bookkeeping, supply chain management, logistics, inventory management, inventory control and everything else you can imagine. I had a lot of sleepless nights.

**Sramana Mitra: You have much more than any old MBA. You have built a 16 million dollar business from scratch. How many MBA's know how to do that?**

**Valerie Holstein:** I just don't know. I have never gone to school. I still think I might go do an eMBA. I come from a long line of teachers in my family and I think I am missing that MBA.

**Sramana Mitra: If you are seriously thinking about heading out to get an executive MBA, then I will tell you to save yourself the money and trouble. Just do 1M/1M. We teach everything about entrepreneurship in a very efficient program for just $1,000 a year.**

**Valerie Holstein:** Maybe I should do that. I will definitely look into it. Just last month I went to an accounting class that I did not understand. I will have to take it again. The course went too fast for me because I don't speak the accounting lingo. I do FranklinCovey Classes, and I am on various LinkedIn groups. I am part of the Business Marketing Association. I am all over the place. We have been a Top 500 Internet Retailer for the past five years.

**Sramana Mitra: I know the numbers of the top 500 retailers, and that is great that you are there. Both you and your husband still work on the company full time. You have been doing business together for 10 years. How has that experience affected your relationship?**

**Valerie Holstein:** In the beginning it was easy. He worked full time outside of the country. I saw him about 20 hours a week. Everything regarding the business was on me. After 10 years of traveling non-stop all over North America, he suddenly came back home, and he was home full time. Not only did he come back but he also had a job inside the house. It took us a year to adjust.

He had his own habits, and I had my way of doing things. When he came back, we had to adjust. It was definitely an adjustment period. Then we had the brilliant idea to have office space that was adjoining. That was a disaster because he could hear my conversations on the phone, and I could hear his. When we disagreed, it was done in public and out loud. It was making employees uncomfortable. It took a few years but we had to learn not to criticize each other in front of employees.

We had to learn to respect each other's positions as well as each other's personal space. The best thing that we did was to have offices on the opposite sides of the area. We also decided not to manage everything together and instead divided our responsibilities. IT, logistics, finance and accounting are his. I am the marketing, HR, business development, PR and trade show person. That is how we have separated it, and it is working really well.

**Sramana Mitra: Thank you. I have really enjoyed your story. It is wonderful to see you succeed like this. I look forward to keeping in touch.**

# Interview with Jay Steinfeld, Blinds.com

*Jay is the CEO of Blinds.com, a company he founded in 1996. It has since achieved revenues surpassing $100 million. It is also the world's top retailer for blinds, shades, and other window coverings. Starting with a pure play e-commerce focus, Jay has leveraged many aspects of Web 2.0 and Web 3.0 to make the user experience richer and more engaging.*

**Sramana Mitra: Tell me first about your personal background leading up to this venture.**

**Jay Steinfeld:** I was born in New Jersey and moved to Dallas when I was 11. In high school I had several businesses, but the main business was custom t-shirts. I always knew I was going to be in business for myself. I interviewed people when I was in high school whom I considered to be successful businesspeople.

I asked them what I should study in college so that I would be able to best be equipped to run a business some day. Almost all of them said that I needed a financial background and that I should study accounting, because once you have a fundamental understanding of numbers then it is really up to you what business you go into. I followed their advice and got a BA in accounting from the University of Texas. At the time it was the Big 8, and I worked for KPMG.

**Sramana Mitra: What year was this?**

**Jay Steinfeld:** I graduated from college in 1976. I worked for KPMG for three years. I knew then that accounting was not something I was interested in. I did not want to count other people's money or doing those CYA tasks. I did not like providing reports which gave as much information as was needed to minimize and eliminate liability. That was not creative or something that was inspiring.

After that I had the opportunity to move to Houston, which is where I live now. I worked for the national franchise Mieneke Discount Mufflers. I was VP of finance and worked there for seven years. When I started I was working with Sam Mieneke. I remember getting in at 5:30 or 6:00 a.m. and being mentored. That is where I learned a lot about the fundamentals of business. At the time when I started there were only 35 franchises. When I left there were 900, and it was nationally owned.

**Sramana Mitra: Were you only involved in finance, or did you get a broader perspective of the business?**

**Jay Steinfeld:** I got a much broader perspective. I actually worked on a targeted marketing program, which I developed. We would find holes where franchises were being developed. I would research and determine where we wanted to establish franchises to cover those holes. They were typically in smaller markets such as Savannah [Georgia]. I would advertise and seek managers who could eventually buy into the business and become franchisees. That worked well.

I was also involved in the selling process. Once a franchise was sold, we had a final filtering process in which we would review the contract with them to ensure that no misrepresentations were being made to that franchisee. If a franchise fails, the first thing the owner does is sue for fraud or misrepresentation. We tapped those meetings to ensure that there was no misrepresentation as to how the contract was sold. We wanted to have accountability.

**Sramana Mitra: How were you tackling your original aspiration of owning your own business at that point of your career? Were you waiting and planning? How was that gestating?**

**Jay Steinfeld:** The business was growing, and I was involved in all aspects of it. At the time that satisfied my need, because I was learning so much. I was learning much more about businesses than auditing companies. It was inspiring for me and it was exciting. I loved seeing the growth. I loved seeing the ability to establish a formula of success, which is what a franchise is.

**Sramana Mitra: What did you do after Meineke?**

**Jay Steinfeld:** The company was sold, and I got fired. They pushed me out of the company and forced me to deal with what I wanted to do. Right before I was fired we were looking at other businesses to franchise. We were really experts in franchising, even more than we were experts at running muffler shops. We were in the franchise business more than we were in the muffler business.

We were looking to franchise other businesses. One of those businesses was window coverings. The British company that bought us abandoned the idea of buying other companies. We were really keen on that industry, so we launched some stores in window coverings and started franchising those. I then decided that I would run, with my wife, some drapery and blinds stores. That was around 1986. My wife actually started it and I was doing some marketing consulting.

**Sramana Mitra: You are talking about actual brick-and-mortar stores, correct?**

**Jay Steinfeld:** Yes. My third child was born in 1990 and my wife decided she wanted to stay home with the three kids. We merged the stores, and I was the only one running this store. It was only 1,001 square feet, including the bathroom. I was going to people's homes and selling blinds and shades. I was a shop-at-home decorator. I was working seven days a week. I was out the door when it was dark and by the time I got home it was dark. That is what I did Monday through Saturday. On Sunday I was doing all the paperwork. It was a true mom-and-pop situation, and I was the pop.

In 1993, I read an article in a trade magazine about the World Wide Web. I had been in business for seven years by that point. AOL had 500,000 subscribers. I decided that I would set up a website. I was the first one in the industry, to my knowledge, to establish a website for my store. I still have a giant poster of that homepage in my office because I want to remember what it was like on day one.

**Sramana Mitra: It sounds as though you are one of the first e-commerce ventures period, right there with Amazon.**

**Jay Steinfeld:** Correct. I was one of the first. People had no idea what I was doing. I did it from my garage. In 1993, it was just a website that was a brochure for my store. In 1996, I realized that people were selling things.

**Sramana Mitra: So you were not actually selling in 1993?**

**Jay Steinfeld:** No, I didn't know how. I started selling online in 1996. I was the only employee. I did all the marketing and everything myself. I had a company in Ohio that I found online do my website. It cost me $3,000 to do the first site. That is all the money I have ever put into the business. It has grown organically since.

**Sramana Mitra: In 1993 did you generate any business at all from the website?**

**Jay Steinfeld:** Yes. It generated appointments and leads. Not a lot, but it was enough. I advertised it on everything I had.

**Sramana Mitra: Today if you have a website, there is a certain amount of search traffic that automatically comes to you. That was certainly not happening at that point.**

**Jay Steinfeld:** No. I was doing the guerilla marketing tactics that people are talking about now. Once I started selling online in 1996, I really became active at marketing.

**Sramana Mitra: How much revenue did you do in 1996?**

**Jay Steinfeld:** I started it in the last week of June 1996. I probably did $500 a week. That is rough, but I am sure I did not do more than that. I was hoping for a sale a day back then.

**Sramana Mitra: Did the sales require high-touch customer interaction?**

**Jay Steinfeld:** Our shopping cart did not allow someone to buy something and have the price show up. It was a text field form in which you basically had to type in the name of the product and use a pricing grid to look up the price and enter the price in the proper text field. You then had to add them up yourself. I would personally have to doublecheck the math.

When people would call with questions, there was nobody to answer the phone. I had a message that said "all of our customer service representatives are busy," and I would get somebody to check these messages and call me on my cell phone. I would typically be on the road so I would pull into a parking lot in my van. I had my calculator, my price sheet, and my order form on the front seat of my van. I would call the customer back and talk with them and hopefully fill in the form with my pencil and pen. At night I would run the credit card through. I had a template for the order confirmation so that it looked like it was automatically generating their name.

**Sramana Mitra: Did you have to help the customers pick the actual product, or could they pick out what they wanted based on the information that was on your website?**

**Jay Steinfeld:** Both. At the time most of the people called, at least 80%. People were afraid to use their credit card online.

**Sramana Mitra: I understand that from a security perspective, but what about product Q&A? That really changes the dynamics if you have to do consultative selling online.**

**Jay Steinfeld:** We had a lot of content. I had a lot of articles on my website because even back then I was focused on search engine optimization. We were ranked number 1. Those articles did help inform the customers.

**Sramana Mitra: Tell me more about your search engine strategies. Not many people did search engine optimization in 1997.**

**Jay Steinfeld:** I found Danny Sullivan back then, and he did the search engine optimization with me.

**Sramana Mitra: What kind of keywords were you optimizing on?**

**Jay Steinfeld:** Blinds and window blinds were the two main words.

**Sramana Mitra: Has it broadened since?**

**Jay Steinfeld:** We have thousands of keywords and phrases. We have negative keywords. We probably have upwards of 10,000. We have a very elaborate process today.

**Sramana Mitra: Is it your top customer acquisition strategy?**

**Jay Steinfeld:** No. It is near the bottom. The top is customer experience. Almost half of our customers, 42%, are repeat and referral customers. That will remain our top strategy. We also do PPC advertising, but now that represents less than 15% of our revenue.

**Sramana Mitra: How does PPC compare to organic SEO?**

**Jay Steinfeld:** Organic is better. We do all our PPC and organic optimization in-house. We have two to three people assigned to those things, and that is all they do.

**Sramana Mitra: If 42% of your business is referrals, what percentage is driven by search strategies?**

**Jay Steinfeld:** I am not sure how you want to consider it, but we have a lot of direct-type in traffic due to the name, blinds.com. Our actual revenue numbers breakdown is as follows: 34% are repeat buyers and 13% are referrals. Natural search traffic and direct type-ins account for 20% of our business and paid search accounts for 18%. Affiliate programs bring in 8%, radio brings in 3%, and miscellaneous methods account for 4%.

**Sramana Mitra: You took this business from $500 a week and turned it into something very significant. I think that it is important to understand some of the mechanics of how you got there.**

**Jay Steinfeld:** At the heart of it all is customer experience. An e-commerce business is just a regular business that is using the Web. It always comes back to the value proposition. If you have to continue to buy customers, then your customer acquisition will be too high. Everything we do is based on the question "Is this going to wow the customer?" and focusing on continual improvement. We are constantly looking for ways to experiment here and there. That ultimately creates the momentum that has everybody in the company focused on improving themselves, improving the company, and improving the customer experience. It is just a fundamental thing. Customers sense that. They feel the sincerity.

**Sramana Mitra: How many customer service reps do you have today?**

**Jay Steinfeld:** We have a total of 70 employees doing about $51 million. Around half of them, 40 of them, are in the sales and customer service department.

**Sramana Mitra: You have always had a lot of content on the website itself that talks about the product and provides education. Tell me more about the content strategy.**

**Jay Steinfeld:** The strategy right from the beginning was to provide relevant information so that customers would not have to call me for it. I knew, from the buying process, what questions people would ask. I would provide answer to the questions that I knew they were asking, hopefully in that same linear order.

**Sramana Mitra: That was a result of your hands-on experience, right?**

**Jay Steinfeld:** Correct. I was just digitizing the sales process that I already knew. It was consultative selling but it was not interactive. Now it is interactive.

We have filters, artificial intelligence, and all different ways to sort. We even have our own recording studio where we have done our own videos. People are talking now about how videos will increase your sales. It is absolutely true. I had videos in 1997. I filmed them in my bathroom.

I had a guy who knew how to film. We created 15-second videos on how to install four or five different products. It was the same window, and I was the one doing the installation. The cameraman did the narration. It was hilarious, but it worked. Even back then we had testimonials as well as customers who called me and let me record their audio testimonials.

I had fake testimonials, which were obviously fake because they were from Abraham Lincoln and Paul Bunyan [a North American lumberjack who was the subject of many folk tales]. Those were there for fun. I had impersonators do the voice of all those people. That let people realize that I was having fun with what I was doing as well.

I patterned my company after Car Talk, the show on National Public Radio. You had two really smart guys who loved their business and had fun doing it. They had puzzlers. The name of my company at the time was No Brainer Blinds because I wanted to make buying blinds and shades a no-brainer. The address of my company was 1 Brainer Tower, which was the address of my house. My address literally read '1 Brainer Tower, Houston, TX'. Mail got to me.

**Sramana Mitra: Fast forward and compare where you are now at the end of 2009. Back then you were filming videos in your bathroom, and now you are using artificial intelligence. What else are you doing?**

**Jay Steinfeld:** Some people know exactly what they want. We want to provide them with the type of filtering that will let them find what they know they want very quickly. If you go to Blinds.com, you will also find a 'help me choose' feature. In that case we know we are working with somebody who does not know what they want at all. By asking six questions, we will narrow hundreds of opportunities down to fewer than five. That really helps.

We have also found that in many cases people did not know what product they wanted, but they knew what results they wanted. Specifically, they wanted to cut the glare in their room, or they had a kid's room that they wanted to make dark. That led to the 'I Want To' section, which is on the left side of the page under other buying options. That is really our shop-by-need feature. We pre-sort the products so that the top sellers for people who have similar needs can find the products they want rather than wondering which products will satisfy their needs.

**Sramana Mitra: How did you come up with that type of clustering?**

**Jay Steinfeld:** We know this business. I have been in the business for almost 25 years. I had sold over 10,000 jobs when I was going to people's homes back in the day.

**Sramana Mitra: So it is based on your knowledge because you know the business inside out?**

**Jay Steinfeld:** Yes. It is not that I am great at technology, because I am not. I do know my product and I know how to sell it. I also know how my customers buy it.

**Sramana Mitra: How did you take your domain knowledge and transfer that into your 'shop-by-need' features?**

**Jay Steinfeld:** We do everything, our entire platform, in-house. It is a combination of my marketing team and my IT team. We have a vision document, and we set the parameters of our desired features. From the vision document we developed use cases and did a whole development process.

We got our people from the call center to give their ideas. We used them as our beta testers. We brought them into our meetings and asked them what they thought of our questions. How would they answer? We would refine questions and change them if they came up with incorrect results. We had to keep changing until our customers were actually providing the answers that they intended to provide instead of misinterpreting our question and answering the wrong way.

We AB test everything. We have a person who is in charge of customer intelligence. He must have seven or eight tests going on at a time. Half the country sees one feature and the other half does not. We look for a lift, and if we notice one then we know it is working so we try to do it even more. If there is no lift, then we don't need to put more resources that way.

**Sramana Mitra: Tell me about how you built the team around you if you did not know technology well.**

**Jay Steinfeld:** I knew very little about all that. I was worried. I read a lot. I tried to hire people like Danny Sullivan, who is now one of the SEO experts. Everything he taught me was direct from an expert. The things you do not know really require you to hire the best people you possibly can. Do not use an amateur. You will get what you pay for.

**Sramana Mitra: What about your CMO? Is that someone you hired early on who has stayed with the company?**

**Jay Steinfeld:** It is someone I brought on later. We could not afford it early on. I did all the advertising myself. We made an acquisition in 2005. At that time we doubled the size of the company, and we knew we needed to bring in staff. That is when I started bringing in my C-level people. Prior to that, the company was run very flat. It was a pancake with a toothpick in the middle. I was the toothpick.

**Sramana Mitra: What were your revenue levels when you starting bringing in your executive team?**

**Jay Steinfeld:** That was in 2005 and at that point we were doing $15 million. We acquired a company that was doing $18 million, which brought us to $33 million. With that acquisition I got a COO from the other company. That is when I realized I needed a CMO and a CPO. All but one is still working for me.

**Sramana Mitra: Did your CMO also have an online marketing background?**

**Jay Steinfeld:** He worked for the online division of Reliant Energy. He is still with me, and he is awesome.

**Sramana Mitra: Let's talk about the acquisition. Why did an $18 million company want to be acquired by you?**

**Jay Steinfeld:** I believe the seller had built up the company and was happy where he was. If I was willing to pay a certain amount of money, well that was way beyond his wildest dreams. He didn't want to build the company to the next level. His mother was working for the company, and she still works for me. She is fantastic.

**Sramana Mitra: Did you have to raise any capital for this venture?**

**Jay Steinfeld:** In 2001, I decided to go full time online. I sold my store and acquired a company in St. Augustine, FL, that was doing $3 million online. I was doing $1.5 million online with two employees and my store was doing about $1 million. I sold the store for $250,000. I then raised $500,000 and assumed some debt of the target company of $300,000. The total acquisition cost was $800,000. Those investors have now not only received their investment back, but they have received far more than they ever dreamed they could have gotten. We have paid out significant amounts in dividends. I 2005, I did raise a few million more from the same investors, which allowed me to make the second acquisition.

**Sramana Mitra: What is your relationship with your investors?**

**Jay Steinfeld:** They are personal relationships. They are all smart, successful, and entrepreneurs. This is right up their alley.

**Sramana Mitra: What is your debt level now?**

**Jay Steinfeld:** It is zero. We have paid everything off from revenues. It took me seven months to pay off the debt we incurred in 2005. Our trailing 12-month gross margin has been improving every quarter for the past three years. That is significant when you consider there are so many people trying to do what we are doing along with the fact that our industry has been tanking for the last three years.

**Sramana Mitra: The cost of blinds is not necessarily going down.**

**Jay Steinfeld:** The cost is indeed going up, and there are several downward pressures on price. There is far less demand because the housing industry has been going down. The PPC search on keywords associated with blinds has been dropping in a linear line. Even with a net increase in Internet usage, there is still a decrease in the number of people looking for blinds. The fact that we are improving gross margin, top line, and bottom line is very satisfying.

**Sramana Mitra: How are you able to increase gross margins when prices and demand are going down?**

**Jay Steinfeld:** In a bad economy, if you are strong and well financed, you have an opportunity to talk to manufacturers who are hurting from decreased demand. We offer to pay them very quickly if they give us better prompt payment discounts. If we buy more from them, then we start getting better volume pricing.

Then we tell them that we want to have promotions and offer our customers special deals, but we do not want to absorb that. We show them analytically that if we promote a decreased price for a certain period of time that two things happen. One, there is an increase in purchases of their product. Two, the following month when there is no promotion, people return and buy more of the product because they did not buy enough the first time. We use Omniture to show them the analytics. We do a post-promo analysis every time and show that data to our manufacturers. We show them that they actually make money by offering promotions.

**Sramana Mitra: How big is the window blinds market?**

**Jay Steinfeld:** About $4 billion. We have plenty of room to grow. We believe that Home Depot and Lowes are our competition. That is where the price-sensitive market goes to shop. We believe that market is about $1 billion and that our market is at least $1 billion. It used to be that 75% of the market was

Sears, Montgomery Wards, and JC Penney's. Sears and Montgomery Wards got out of it, but mom-and-pops came into it. Home Depot and Lowes came in and started supplanting the mom-and-pop stores. Manufacturers still see mom-and-pop stores as their core constituency. But mom-and-pops just cannot compete in the 'do-it-yourself' market. The economy, however, is turning people into do-it-yourself consumers.

**Sramana Mitra: How do you win a customer who would normally go to Home Depot or Lowes?**

**Jay Steinfeld:** Until about a year ago we were not finding them other than word of mouth. People started going online enough that we finally started national advertising and public relations. We have done a lot of host endorsed talk radio. That goes really strong. We are going to start television in Q1 of next year.

**Sramana Mitra: You have done a nice job creating your own brand. That aligns with my Web 3.0 formula which indicates the web is contextualizing. That formula is Web 3.0 = (4C + P + VS). The 4Cs are community, content, commerce, and context. P represents personalization and VS is vertical search. Your business covers all these elements to some degree.**

**Jay Steinfeld:** I read that article. We are doing vertical search. We do have the 4Cs. We are doing a lot of personalization in our email campaigns and behavioral targeting.

**Sramana Mitra: Do you use anything like Baynote?**

**Jay Steinfeld:** No. We are doing it on a much cruder basis. We are looking to see if they have been on the website before and which products they have purchased. We have not done behavioral marketing as sophisticated as we could. That is on our to-do list for Q2/Q3 of 2010.

**Sramana Mitra: Are you planning to hold on to this company as a private company?**

**Jay Steinfeld:** That is a difficult question to answer. I think that all companies are for sale. The way I am running this company is via a two-pronged approach. I run the company as if it were going to go public. We have this transparency, honesty and, internal controls that are required, with no intent of ever going public. We also run the company as if we will never sell it, as if we are just going to build it into a $500 million company.

We just created a partnership with some big public companies and it launched two weeks ago. We just got the go-ahead, so I really can't talk about it in detail.

**Sramana Mitra: What kind of partnership?**

**Jay Steinfeld:** It is a big-brother/little-brother relationship where major retailers outsource the entire department of custom blinds to us. We have done a cart-to-cart integration. When you go to their site it is seamless. You don't even know it is us. We handle the phones, the customer service, and the fulfillment. We have no inventory because it is all drop-shipped from our manufacturers. If you want to look at return on capital employed, it is like dividing by zero.

**Sramana Mitra: Wow. That is awesome!**

**Jay Steinfeld:** Everything is custom made and drop shipped. We have no inventory and no receivables. The trailing 12-month return on capital employed is basically incalculable. We only have capitalized technology.

**Sramana Mitra: If you are not taking inventory, how do you negotiate fast payment deals?**

**Jay Steinfeld:** When we buy from you, we will pay you in a week. Our pricing is set on volume. We will consolidate purchases from multiple manufacturers and give you a higher percentage of it if you give us a better price based on our hitting specific targets.

**Sramana Mitra: I love your business and the way you run it. Congratulations!**

# Men's Fashion e-Commerce Entrepreneurs Thriving

Most major retailers are latching on to the e-commerce trend but there is also a growing number of online men's fashion upstarts like Combatant Gentleman and JackThreads that are using social media channels to understand the consumer and sell effectively under their own retail brands.

Combatant Gentleman's strength lies in creating a brand that produces high quality clothing at an affordable cost and then effectively selling it to their target customerof young, aspiring professionals through Facebook. CEO Vishaal Melwani says, "One of the big reasons that we still, to this day, take away clients [from competitors like Men's Warehouse] is because their messaging is incorrect. They don't understand the pains and the trials and tribulations that our guy goes through on a daily basis."

On the other hand, JackThreads' focus is on providing street wear and contemporary fashion brandsat great discounts. They have flash sales of authentic brands and engage their customers with new offerings every day. In the first year, they reached out to blogs writing about the brands they were selling. Once users found their site and recognized the value proposition, they became extremely engaged. And it was viral.

They sell products that are geared towards all aspects of a lifestyle and have been very successful with t-shirts, pants, denim, accessories and watches. They have a members-only community and they know what their shoppers are interested in and what they are recommending for their friends to buy.

In May 2010, they were acquired by Thrillist, an online publication for urban men.They have editions in 16 cities and write a daily newsletter showing the newest and coolest in fashion, nightlife, and dining for urban guys who are 18 to 35 years old. The brands that JackThreads were selling were the same ones that Thrillist wrote about. CEO Jason Ross says, “We saw them as a trusted voice that put a brand in front of an audience who trusted whatever they said. On the other side of that story, we are selling the same products. It is a great, cohesive strategy for us to be the same company.” Revenue at JackThreads grew from $5 million at the time of acquisition to $50 million in 2012 and the number of users ballooned from 150,000 to 1.8 million. See what combining Content and Commerce in Context does to a business?

Combatant Gentleman’s focus is on providing a premium fashion experience at a price point even lower than Men’s Warehouse. Using the e-commerce model, they are able to save on the overheads incurred in running a brick-and-mortar store. Apart from this, they generate margins of up to 16% by deep vertical integration to the level of producing their own cotton and wool. They bootstrapped to $700,000 in revenue, followed it up with a $2.2 million financing round, and are on track to deliver $15 million in revenue in 2014.

They target young, aspiring professionals who spend a lot of time on social media channels like Facebook. Their clothes can be used for multiple purposes and their value is in providing a high return on investment. They inventory all the likes on their Facebook page and study their characteristics and interests. A lot of their customers use them as a service and ask their stylist for recommendations. Nearly 50% of their customers come back for more and also act as their brand ambassadors.

Men and women have very different shopping dynamics. Women spend a lot of money on clothes. Men don't spend as much. However, these retailers understand that when men find a brand that they trust, they are loyal to that brand, andwill spend significant amounts on that particular brand. Men are more brand-conscious while women would shop and experiment with new styles and designers that resonate with their style. Brands perhaps last longer in men's fashion. This psychographic tendency works beautifully online, as retailers can almost become replenishment businesses for basics like black turtlenecks, khakis, boxers, etc.

These men's fashion e-commerce entrepreneurs are thriving because they are able to leverage technology and understand the newage, social media savvy male shoppers well. They are creating brands that their customers trust. They take away the pain of shopping for them. They provide great quality at great prices. They are bringing content and commerce together and doing it in context.

All of these are winning strategies to build significant e-commerce companies!

# Interview with Jason Ross, JackThreads

*Jason Ross founded JackThreads in Columbus, Ohio. The idea for the July 2008 launch of JackThreads.com came from Ross's interest in street wear and men's contemporary fashion, plus his appreciation of a good deal. Ross saw the company as a more discreet way for men to buy premium brands on sale, without sacrificing the top-tier images they worked to build. JackThreads was acquired by Thrillist.com in May 2010, bringing a content and commerce company together, a trend that we see elsewhere as well, including in the wildly successful NastyGal.*

**Sramana Mitra: Jason, let's start by reviewing your background. Where do you come from?**

**Jason Ross:** I am from Cleveland, Ohio. My father was in the military so we traveled a lot, but we settled in Ohio and I went to Ohio State. I got a degree in finance and have stayed in the area ever since. When I left school I wanted to be an entrepreneur. During my first two years out of school, I started a company where we sold consumer products into retail stores. We were targeting sports enthusiasts.

I was not as passionate about that company as I should have been. After two years I decided that I needed to take the experience from running that business and marry it with a great business plan that I was passionate about. That is when the idea for JackThreads came about.

**Sramana Mitra: What were the circumstances that brought JackThreads into existence? What were you watching in the marketplace that led you to identify this opportunity?**

**Jason Ross:** With JackThreads I thought of myself as the target customer. I could not find what I was looking for, so I decided to create it.

**Sramana Mitra: What were you looking for?**

**Jason Ross:** I have always been into better street wear and contemporary fashion brands for guys. At the same time I am a discount shopper. The customer who goes to the boutique or retail store and knows brands and their product lines but does not necessarily need to have it right away is the ideal type of customer. I realized there was no outlet for that niche. I could not find the products I wanted at a discount anywhere.

I ran into a company in Europe, Vent Privé, that had an interesting business model. It is an online, private shopping club that features authentic brands in short 72-hour sales. A product goes up and is featured to a private audience. The sale lasts only 48 to 72 hours, so there is an incentive for consumers to buy now.

**Sramana Mitra: When you were envisioning JackThreads, were you thinking about new products or off-season products? High-end brands have struggled with their e-commerce strategies and that makes room for entrepreneurs.**

**Jason Ross:** I was thinking about off-season products from contemporary brands.

**Sramana Mitra: How did you go about launching the company?**

**Jason Ross:** It was a long and joyful journey. In January of 2006 I wrote the business plan despite having no fashion industry or e-commerce experience. I made a pact with myself that whatever barriers would come up would not stop me and that I would find a way to make this happen. I found various website developers around the Columbus, Ohio, area who helped me make a website. It took me two years to get a website up that was working because I did not know what I was doing.

At the same time I was traveling to trade shows in New York and California. I was meeting with the brands that I wanted to work with on the supplier side. Walking into a trade show for the first time with no experience was a unique experience. I walked from booth to booth pitching my idea to people. I had no contacts. It was frustrating and challenging at first, but the more I saw the same people over those two years the more trust I was able to build. Over that two-year period I was able to get enough brands to commit to working with me if I was able to build the site functionality.

**Sramana Mitra: How did you sustain yourself for two years while you sold the concept?**

**Jason Ross:** I was doing anything I could to get by. I worked at restaurants and bars at night so that I could have my days free. I ended up taking a part-time consulting gig for a consumer products company here in town. I basically leveraged my experience from the first company I started where I sold products to retail, and I helped this consumer products company take new products and sell them into retail doors.

**Sramana Mitra: After two years of trade shows, what were the terms that you came to with the brands? Did you actually have to buy their products?**

**Jason Ross:** The first model was to work on consignment. I realized quickly that unless we had a massive audience of people on day one, our consignment idea would not happen. In the beginning we committed to products. We were purchasing the goods outright. My message to the brands was that I would buy the products if they would commit to me because I was determined to build the business. A lot of the brands respected that approach.

**Sramana Mitra: What were the first brands to trust their merchandise to you? What was that negotiation like?**

**Jason Ross:** We started out with a couple of brands; I remember Creative Recreation and an Australian brand called Insight were among our earliest. Persistence was the key to getting started. It was going to the same shows for two years, and meeting the same people for two years. Over time they became convinced that I was going to do what I promised them that I would do. I had met a buyer from Urban Outfitters during that time and I was able to develop a relationship with him. He taught me how to negotiate these types of deals. That is what gave me the basis for our initial inventory purchases.

**Sramana Mitra: What did you learn from your mentor?**

**Jason Ross:** I learned how to negotiate pricing. He taught me about standard industry off price arrangements. It gave me a ballpark to work with. I was flying completely blind before that, so he gave me the basic information about standard deals in the fashion world. I used that to construct my pitch.

**Sramana Mitra: What about the terms?**

**Jason Ross:** We were actually purchasing products from our initial six brands. We bought the merchandise and I had it shipped into my house. I stored the product in the master bedroom of my home.

**Sramana Mitra: How did you finance that inventory?**

**Jason Ross:** I financed it from my savings, from the money I made on my first business, and debt. I never raised any money. Everything was bootstrapped.

**Sramana Mitra: How much money did you have?**

**Jason Ross:** A low five-figure amount.

**Sramana Mitra: How much money did you put into acquiring your initial inventory?**

**Jason Ross:** Every penny that I had and then some. It was close to six figures at its highest point.

**Sramana Mitra: How did it feel to put all of your money into inventory that you were not sure if you would be able to sell?**

**Jason Ross:** It was scary at times. The way I justified it was that I spent a lot of time planning and meeting the right people. I felt I had made the right decision. At the same, time I made a pact with myself that I would make this business work no matter what. I promised myself that if I could not find products that sold I would find ways to get rid of them and that I would go buy something else. Fortunately, I did the right research and planning up front, and the initial inventory that we bought turned very quickly for us.

**Sramana Mitra: Who were you selling to, and how did you acquire those customers?**

**Jason Ross:** Originally I did not have much money for a marketing budget. I knew that if I did the research to get the right brands, then we would get a customer base because brands have loyal customers. For us, having those brands at heavily discounted prices meant that I just had to find the bloggers or writers online who covered those brands and get them interested in the JackThreads business model. For the first year I relied on as many blogs and media outlets that would listen and write stories about what I was doing. After that I started search marketing.

**Sramana Mitra: What year did you manage to get the site live?**

**Jason Ross:** We went live on August 1, 2008.

**Sramana Mitra: When you launched your site how many visitors did you get and what was the conversion rate?**

**Jason Ross:** We had zero customers on the first day. There was not much traffic for the first month or two. There were no orders coming in, and to see no traction was very scary. That is when I really started reaching out to the blogging community. I reached out to any blog who was writing about the brands we were selling. I had been following most of those blogs as a customer anyways. Not all the blogs listened, but I just kept e-mailing and calling. I was not moving inventory, so I had the time to do that.

**Sramana Mitra: What was the story or the angle that you pitched to the blogs?**

**Jason Ross:** The fact that they were already writing about the brands we were selling, so I just explained that they should write about a business that was selling 100% authentic merchandise for great prices. Our prices were better than any other prices I could find online. I was able to share my story with some of the blogs, and they respected the bootstrapped venture with two years of sweat.

**Sramana Mitra: When you were telling your story, did you explain the flash sale notion as well?**

**Jason Ross:** The flash sale was important because it illustrated that there was something new every day. There were no stale offerings. That helped to keep people engaged.

**Sramana Mitra: How did that work since you had already bought the merchandise and it had been sitting for a couple of months?**

**Jason Ross:** It worked in the beginning because our audience was so small. By week eight we would have an entirely new group of people. The product was fresh for that group of people. It was the way I had to do it in the beginning because I had no more capital to invest in inventory.

**Sramana Mitra: In the beginning, did you have different merchandise for sale every day?**

**Jason Ross:** In the beginning we did sales three times a week, and we rotated the merchandise so each sale had something new. A couple of months later we had enough of an audience to move to sales five days a week. Shortly afterward we began having sales seven days a week. Today we have multiple branded sales every single day, which is the level I originally wanted to be at from the first day. I just did not have the resources or audience back then to make that type of offering.

**Sramana Mitra: How do you market and run the flash sales? How do you get the word out about them, and how do you manage them on the back end?**

**Jason Ross:** On the back end we have a buying team that works with close to 300 brands now. They stay in touch with sales reps and inventory managers for those brands. We want to be the person they call first, and that remains our strategy to source merchandise. We have a photography studio with models and photographers. When a deal is done with a brand, they ship merchandise to our warehouse and our studio takes over. They get the models ready and do a photo shoot of the items. In terms of marketing we now have a mid six-figure membership base that has opted to receive daily e-mails.

**Sramana Mitra: How did you build that membership? You said you had very few visitors for the first six months. When did the membership start to take off?**

**Jason Ross:** The third month was the first time we received blog press. The press was viral, and our sign-ups rose significantly every day. That turned out to be key to our growth. For the first nine months all we did was market ourselves to blogs. At the same time we implemented a system where members who invite friends who actually make a purchase receive a $10 credit on the site. A lot of people take advantage of that and use it as a way to make money to buy goods on our site. That has helped us out a ton.

In August 2009 we realized we needed to grow quicker. We were a year into the business and that is when we hired a full-time marketing professional. We started with Google and Facebook and did test advertising campaigns. It took a month or two of tinkering to acquire customers at the right price and get that money back. Two months into our campaign, we began seeing ROI on it.

**Sramana Mitra: How did JackThreads's traffic ramp after the third month?**

**Jason Ross:** The growth was not significant, but it was enough to indicate we had something. We were lucky to be involved early on when there were not many other entrants in this space. We had the luxury of going slower. I don't have hard data for site visitors, but I remember that it was enough to indicate that we had an opportunity to scale quicker.

**Sramana Mitra: How long did it take to recoup your investment and become cashflow positive?**

**Jason Ross:** It took a couple of months once we received publicity from the blogs.

**Sramana Mitra: What threshold was that?**

**Jason Ross:** It was a low five-figure revenue from a monthly point of view.

**Sramana Mitra: How many months into the business was it before you started doing paid key word marketing?**

**Jason Ross:** That was 12 months into the business.

**Sramana Mitra: Did you select keywords around the specific brands?**

**Jason Ross:** The keywords were either brand or lifestyle specific. Some were product specific. We cast a wide net and then cut out the campaigns that were not working as quickly as possible. Our goal was to have campaigns fail fast.

**Sramana Mitra: Keywords have been a tremendously effective way of marketing for many e-commerce companies. Managing their keyword strategies is key to success. Can you elaborate on your strategy?**

**Jason Ross:** When I think about marketing an e-commerce company online, I think the more keywords you market the more successful you will be. We were selling a number of name-brand products. We found people who were looking for those brands and the type of lifestyle. We knew the products we were selling already had a built in audience. We knew that those people were already on the Internet looking for those products.

**Sramana Mitra: Keyword campaigns do well if you have that type of audience; otherwise, they do not do that well.**

**Jason Ross:** Exactly. That is how we were successful in the beginning.

**Sramana Mitra: When you started your keyword advertising in 2008, did you find that there was already a lot of competition for those keywords?**

**Jason Ross:** Absolutely. We found that when a user found our site and recognized the value proposition they became extremely engaged. It was viral. It is a viral business model. We were able to leverage the built-in followings that the brands we carried already had. Once consumers visited our site, we were able to keep them engaged. We also enticed those users to spread the message for us.

**Sramana Mitra: Essentially, you are saying that it was worth the money it took to acquire your customers because they were highly engaged and generated new customers. Is that correct?**

**Jason Ross:** Exactly.

**Sramana Mitra: How much were you paying to acquire those customers?**

**Jason Ross:** It was a couple of dollars per sign-up, not necessarily for someone who makes a purchase.

**Sramana Mitra: If you were paying a couple of dollars per sign-up, what kinds of conversion rates were you experiencing as you built the business?**

**Jason Ross:** We would probably spend 50 cents per click, and every six clicks resulted in a sign-up. The number of sign-ups that actually turn into buyers was a low percentage, close to 10%.

**Sramana Mitra: Of the 10% who converted into active buyers, how much would an average paying customer spend on your site over the course of a year?**

**Jason Ross:** The average transaction size is close to $100. The users that do buy are very engaged.

**Sramana Mitra: I have found that men and women have very different shopping dynamics. Women spend a lot of money on clothes; men don't.**

**Jason Ross:** That is true. I have found, however, that when guys find a brand that they trust then they will focus on that particular brand and spend accordingly. Men don't want to spend time shopping. That is why they like JackThreads, because we do the shopping for them.

**Sramana Mitra: What merchandise category is the most active for JackThreads?**

**Jason Ross:** There is activity across the board. We have been very successful with t-shirts, pants, denim, accessories and watches. We sell products that are geared towards all aspects of a lifestyle and have seen interest across the board.

**Sramana Mitra: You mentioned that you have your own studio. Do the brands have any problems with that?**

**Jason Ross:** No. We do that so we can control how the brand is portrayed on our website. From day one I have invited the brands to have a say regarding how they are presented on our site.

**Sramana Mitra: Do you have to send photographs to the brand for approval?**

**Jason Ross:** No we do not. The brands we are working with today trust JackThreads as a brand. We have over 300 brands today and we have a solid reputation. We keep an open relationship with the brands and are willing to let them have a say in how we represent the merchandise. We have actually had brands that we work with refer other brands that they are close with to JackThreads as well.

**Sramana Mitra: Today you have 300 brands and a great relationship. Did you have an issue with photography representation of products when you were just starting up? High-end brands are very sensitive to that issue.**

**Jason Ross:** No, that has never been an issue. In the beginning we had six brands and it was very easy to have a phone call with each one. We invited them to check our site out and I never received negative feedback about the photography. Even today when an event goes up a person from the brand checks that site out. If they have an issue with photos we can make that change.

**Sramana Mitra: What do you think about merging content, commerce, and community within one integrated user experience? What are you doing in regards to that strategy?**

**Jason Ross:** Today we are a pure e-commerce site. I don’t want to create a confusing message for our audience by adding too many pieces. We want to sell product and we want our audience to find great products. I think giving the user more targeted messages based on their JackThreads shopping history is in our future. We have a members-only community and we know what our shoppers are interested in and what they are recommending for their friends to buy.

We need to have technology in place to identify and message a member when we have an event based on a certain brand that the member has purchased in the past. That is one component of where we need to go. Suggested selling is another component we need to add. We need to recommend other items that might interest the user.

**Sramana Mitra: Do you have the technology for recommended shopping?**

**Jason Ross:** We are exploring recommendation technology right now. We are not doing it yet but it is in the works.

**Sramana Mitra: I am a big believer in putting user-generated content on your site, because it captures a huge amount of organic search traffic that you do not have to pay for. What is your current traffic level, and how do you propose to grow your traffic and subsequent business?**

**Jason Ross:** We were acquired in May by Thrillist, an online publication for urban-dwelling guys. They have editions in 16 cities and write a daily newsletter showing the newest and coolest in fashion, nightlife, and dining for urban guys who are 18 to 35 years old. We were an advertiser with them and we saw that the brands JackThreads were selling were the same ones that Thrillist wrote about.

We saw them as a trusted voice that put a brand in front of an audience who trusted whatever they said. On the other side of that story, we are selling the same products. It is a great, cohesive strategy for us to be the same company.

**Sramana Mitra: How big is Thrillist?**

**Jason Ross:** They have over 2 million subscriptions now.

**Sramana Mitra: How many members does JackThreads have?**

**Jason Ross:** Our membership is in the mid six figures right now, heading toward seven figures.

**Sramana Mitra: So, you were excited about the acquisition due to all the new potential customers?**

**Jason Ross:** Absolutely. There is a lot of value in the trusted voice, and the audience they have access to is a major opportunity for us.

**Sramana Mitra: What was your revenue level last year? Close to $5 million?**

**Jason Ross:** Yes, but we are heading toward eight figures now.

**Sramana Mitra: Did JackThreads have more revenue than Thrillist when the acquisition occurred?**

**Jason Ross:** No, we were smaller in terms of revenue. Their business model is advertising to their niche. They are based out of New York, and they focus on various urban areas.

**Sramana Mitra: Both companies were private when the acquisition happened. Generally, private-to-private transactions are very difficult**

**because it is hard to put a valuation on the two assets. How did the two companies negotiate this transaction?**

**Jason Ross:** That was a five-month journey in and of itself. We were an advertiser of theirs, and I approached them about doing something bigger. I proposed some sort of revenue share and we had a conversation with their marketing team that did not go anywhere. Shortly afterward I was introduced to their CEO, which is when the potential acquisition discussions began. That was in the fall of 2009. It took until May of 2010 to close the deal because of the complexities and paperwork. It was a huge learning experience.

**Sramana Mitra: Was it a cash or stock transaction?**

**Jason Ross:** It was cash, although I am still an owner of the business. I did get a cash amount as part of the sale.

**Sramana Mitra: How was the value of JackThreads determined? How did you set a price on your company?**

**Jason Ross:** JackThreads at the time had been approached by a number of other firms. As a result, I was able to understand what was going on in the market and what position JackThreads had. I was able to use all the different meetings I had with VCs and other potential buyers to determine what the business was worth and come up with a fair number based on growth and timing. That is what we settled on.

**Sramana Mitra: What is the size of your operation in terms of people, and how does that compare to Thrillist?**

**Jason Ross:** Thrillist has 55 employees, whereas JackThreads is closing in on 20. I think the two companies are showing that content and commerce are being paid attention to now.

**Sramana Mitra: Content and commerce need to come together, and it must be done in context.**

**Jason Ross:** Absolutely. We are showing a lot of success in that niche. We are going to prove that it is the way of the future.

**Sramana Mitra: I am deligted to hear your story. It is interesting and validates a lot of what I am talking about regarding the future of the Web. Thank you for sharing your story.**

# Interview with Steve Hafner, Kayak

*One of the hardest things to pull off in the world of venture capital funded companies is a private-to-private merger, otherwise known as a roll-up. Steve Hafner not only managed to seduce his largest competitor to the negotiating table, but also completed the transaction. Both companies were then vying for the top spot in the prized vertical search category for the travel industry.*

*I spoke with Steve soon after.*

**Sramana Mitra: Steve, I would like to start with some details about where you grew up, and how you got into all of this?**

**Steve Hafner:** I'm originally from Austin, Texas although I've lived all over. I was born in Lima, Peru. My mother is Swedish and we moved around a lot. I have lived in Peru, Guatemala, Costa Rica, Texas, Sweden and ultimately went to college in New Hampshire. I got my MBA at Northwestern. I went down the consulting path and worked for a couple of consulting companies. I then helped start Orbitz.

**Sramana Mitra: How did you end up starting Orbitz? What was going on in the market that captured your interest?**

**Steve Hafner:** It was an interesting time. It was post-bust and I had been working for BCG for 4 years. I was being billed as an e-commerce expert yet I did not know much about e-commerce at the time, which did not stop us from overcharging for my services. We had a couple of clients in Delta Airlines and United Airlines who wanted to create a competitor to Expedia. They retained

BCG for an initial 60 day period to help them think through the strategy and the business case. I was sufficiently impressed by the strategy that I left BCG to help start it.

**Sramana Mitra: How many years did you spend at Orbitz, and what were the nuggets from those years?**

**Steve Hafner:** I was there from inception in 1999 until two weeks after the IPO in September 2003. While I was there I led business development, advertising, marketing and product development. Basically everything that had to do with the consumer website except for customer service and the engineering of the code.

I saw a company start from a few PowerPoint pages and grow to the point that when I left it was booking $4 billion a year in tickets and hotel rooms. It was a great experience. It was a wild ride.

**Sramana Mitra: What gave you the idea for Kayak?**

**Steve Hafner:** Orbitz was a great company, but it never fulfilled its original mission which was to help consumers find great airline and hotel deals. The reason it did not fulfill its original mission is because we could not convince every airline, hotel, and rental car company to list their products and services on Orbitz. Half of all the consumers who came to Orbitz were just doing a search and then booking directly because they did not want to pay an additional fee to Orbitz.

I thought it was odd that we were really a search service which did not do search very well, and we were definitely not giving consumers what they wanted which was the ability to book direct.

That was the genesis of the concept of Kayak. I bounced my ideas off of the former CEOs of Travelocity and Expedia. They all agreed that none of the companies fulfilled the vision of a one-stop shop. So, we all decided to start a new company. Just two weeks after I left Orbitz we incorporated Kayak.

**Sramana Mitra: Tell me the story of Kayak. How long did it take you to assemble a team and get your service launched?**

**Steve Hafner:** It is a bit funny how things change the second time around. I had the benefit of doing Orbitz first. I knew how to build a team and structure contracts. I knew how to build an organization. As a result Kayak built a whole lot faster than Orbitz did. We incorporated within three days of the initial PowerPoint presentation. We had twelve employees on staff within 10 days. We had our first distribution agreement with AOL within two and a half months. We did not have business cards or a company name yet! We launched the Alpha site five months after we started. The public launch was about 10 months after we started.

Contrast that with Orbitz. We started in 1999 and we did not launch to the public until June 2001.

**Sramana Mitra: You said your observation coming out of Orbitz was that consumers did not have a one-stop shop, so what exactly did you do at Kayak that addressed that issue?**

**Steve Hafner:** Kayak is not a booking site, it is a search site. We help users find deals from all of the other travel websites. There are thousands of travel websites out there, so depending on when you ask the question and how you ask the question, you are going to get different answers. We thought by doing a bit of what Google does, which is build a very simple and sleek interface which goes out and searches on behalf of consumers and brings the results back in a comprehensive display, we would give consumers a choice of where to buy. We felt that would enable us to give the consumer great service, and so far that seems to be working.

**Sramana Mitra: When did you launch the service?**

**Steve Hafner:** It was October 2004.

**Sramana Mitra: Can you give us an idea as to what kind of ramp you saw in terms of traffic building and adoption? The vertical search concept was still new in 2004.**

**Steve Hafner:** There had been folks who tried to do it in the past but they did not have the scale or traction needed. They were not ambitious enough, did not have the right capitalization, and did not have the engineering talent to do it right. It is very hard to do, if you want to do it right. When we launched, everyone was aware of the deficiencies at Expedia, Travelocity and Orbitz. Everyone saw the value of the consumer proposition but the big question was how to commercialize it. How do you get paid for those referrals? How do you get consumers to become aware of your website and visit it?

The big online agencies spend hundreds of millions of dollars a year getting people to their websites and they already enjoy 90% brand awareness. In the first year or two of Kayak we focused on building a great product. We felt if we built a great product consumers would stumble on it, like it, and tell their friends. When Orbitz launched we spent $20 million in the first month on TV adds. As a result it was the biggest Internet launch ever. When we flipped the switch on day one at Kayak we did 15,000 searches. In the first month we did about 500,000. Contrast that with this month where we will do 14 million searches. We are half the size of Orbitz in terms of search volume yet we spend next to nothing in marketing.

**Sramana Mitra: You didn't buy any traffic from Google?**

**Steve Hafner:** The problem with a traffic arbitrage based approach is that it gets competed away. Traffic becomes expensive. We are of the mentality that for every dollar which could be placed into marketing we would rather place it into engineering and make the product better. If you do that then you will always have the best product. That means your audience will be more loyal than the next guy. You won't have to spend money on Google, Yahoo! or offline TV advertising. One of the things that struck us about Expedia is that they will spend about $1 billion on marketing this year but their website, which is essentially their company, has not fundamentally changed in 4 or 5 years. We would much rather invest in the website than marketing.

**Sramana Mitra: So you have built traction with organic word of mouth?**

**Steve Hafner:** It is a page out of Google's playbook. Build a great technology, syndicate that out to other affiliates like AOL who already have audience and then keep innovating on the product to make folks come back to you directly.

**Sramana Mitra: What other affiliate deals have you done besides AOL?**

**Steve Hafner:** We have over 10,000 affiliates. Our biggest are AOL, Comcast, and USA Today.

**Sramana Mitra: Do they drive a lot of traffic to your site?**

**Steve Hafner:** Not really. They used to. Affiliates are great at building a significant piece of business, but affiliates never grow. Once you plug in AOL they do not grow their traffic channel for you although your organic traffic does grow. If you were to go back over the past four years and plot the affiliate share of Google's total volume you will see that the Google traffic is growing much faster than the affiliate component.

**Sramana Mitra: Let's discuss the competitive landscape. What was it like when you started, and what is it like now?**

**Steve Hafner:** The market has evolved quite a bit but not as much as we expected it to. Initially, the only competition came from two companies. One was called FareChase and they did not have a consumer facing application. It was mainly used by travel agents to find Southwest Airline's fares. There was another company called SideStep which did not have a website. Instead they had a downloadable toolbar that would launch automatically when you visited an airline or agency website and it would show you fares on the side. Neither company was well capitalized and neither company had more than 30 employees. The competitive landscape was pretty insignificant and the product offerings were not that great either.

When we launched it attracted a lot of attention because of our top tier talent. We had a lot of financial backing and a big distribution deal with AOL. As a result we grew much faster than they did. To their credit there was a lot of cross-pollination of ideas once we launched. We borrowed things from them, they borrowed things from us, and ultimately consumers saw a lot of improvements in a very short period of time among all three companies. Yahoo! ended up buying FareChase in late 2004. We recently ended up buying SideStep at the end of 2007.

**Sramana Mitra: More competition has emerged in the past three years.**

**Steve Hafner:** On the Internet there is always going to be a lot of competition because it is easy to build a website. The hard part is making that website scale. There are a lot of international travel search engines that have tried to emulate the Kayak model. They do not have good brand awareness, they are not well capitalized, they do not have good supplier relationships, and ultimately their technology platform won't support 50 million queries a month. We built our architecture to support a billion searches a month. A lot of these other companies are just scraping websites in real time.

You are right though that the competitive landscape continues to evolve. Just this week Microsoft bought FareCast which was founded two years ago. We refer to them internally as the Kayak JV, but they actually have a really good tech team. They were acquired for $100 million. Kayak is 20 times their size in terms of search volume.

**Sramana Mitra: You have mentioned capitalization a few times as being a vital part of your strategy. What was your capitalization and financing strategy?**

**Steve Hafner:** It was to take a lot of money from various smart investors by selling them on the goal of becoming the number one travel site. The top travel sites at the time we launched were Expedia, Travelocity, and Orbitz. They made money by charging both consumers and airlines booking fees. They also collected a booking fee from a technology vendor called a GDS. As a result they were only paid when someone booked travel through their website. They biased their displays to show providers who paid them more. Their functionality was not terribly inspiring.

Our goal was to create a company that did search better than these major players and we knew it would require a lot of capital. At Orbitz we raised $205 million before we turned profitable. At Kayak we have raised $230 million to date although we turned profitable after burning just $15million.

**Sramana Mitra: What was your source of financing? Can you break it down by rounds?**

**Steve Hafner:** Our first round raised $6.5 million, which was a pretty large Series A, especially since it was on a PowerPoint presentation.

**Sramana Mitra: Did you put in any of your own money?**

**Steve Hafner:** Paul English and I put in $1.5 million each. Paul co-founded Kayak with me.

**Sramana Mitra: Who where your first round investors?**

**Steve Hafner:** General Catalyst Partners. They really knew Online Travel. Our second round was done by Sequoia Capital which brought our total raised capital to $15.5 million.

**Sramana Mitra: How far did you get with the A and B round of funding?**

**Steve Hafner:** We had already launched the product by the time we did our Series B, and shortly after closing the deal with Sequoia we turned cashflow positive. We have built the base of our business with this funding.

**Sramana Mitra: Obviously you made a big departure from established business models in the travel industry.**

**Steve Hafner:** Our business model is very similar to Google's. We get paid for the referral. We are unbiased which is great for consumers because when you have an advertising driven model the incentive is to have more comprehensive search results.

Another key aspect of our business model is that we are very lean. Today we only have 56 people. We can charge very little to our advertisers. Since we charge little and have a large volume of queries we can make a decent living and provide tremendous value to those marketing on our website. Our ratios are much better than traditional OTAs like Expedia or Orbitz. The difference is where Expedia will do $12 billion in gross bookings we will only do $150 million in gross revenue. However we will have a much higher profitability than they have.

**Sramana Mitra: Is your business model in competition with Google, or is it a complimentary model? Expedia is obviously one of the biggest advertisers on Google and they are probably big advertisers on your site as well.**

**Steve Hafner:** In the Internet everyone competes for consumer attention. In some ways Google is the biggest travel site on earth. People go there for their entry into travel research. Expedia is certainly the biggest travel site in terms of bookings. We would like to do a little bit of both. We want to be the best place to find travel information and we want to be the best place to find the supplier of your travel needs. I think we compete with Expedia and Google for audience, but ultimately we are not taking share from either because the transaction has to happen somewhere.

**Sramana Mitra: By raising two rounds of funding you were already cashflow positive. Why did you have a Series C?**

**Steve Hafner:** That series was led by Accel Partner's London office. At that time we only operated in the US and we wanted to export Kayak abroad. The Series C was designed to help fund the international expansion. The US was the least expensive, most efficient market to get started in. In Europe the marketing channels and the language requirements make it much more capital intensive.

**Sramana Mitra: How big was the Series C, and what did it provide in terms of international presence?**

**Steve Hafner:** We raised $18 million. We are in seven markets now. We launch a new market every 2 months. International is still less than 10% of total sales, however that is primarily because the US business is just so big. This month the US will bring in north of $12 million in revenues, which is up 15% month over month.

**Sramana Mitra: What was the reasoning for your recent purchase of SideStep, and have you benefited from the acquisition?**

**Steve Hafner:** At Kayak we are an engineering driven company. We did not have a sales force, a display ad business, or an email business. SideStep did. It is a bit like Google buying Yahoo!. The one thing we knew at Kayak is that our systems scaled better, our algorithms monetized the website better, and we fundamentally had a better product which provided a better user experience. SideStep had an audience albeit one that was a third of the size of Kayak. They also had a commercialization aspect we did not have. I approached their CEO in October of last year with a simple email that said, "Do you want to get married?" and he wrote back "Let's talk." In the course of three weeks we hammered out a deal and signed an agreement in mid-December [2007]. We raised money and closed the deal within two weeks, which is unheard of.

**Sramana Mitra: Can you talk some about the negotiation of a private to private merger? Those deals are always tough in terms of valuation.**

**Steve Hafner:** There are two ways to approach it. The first is on a relative valuation side. If you can agree on relative valuation then sometimes you can just issue your paper for their paper. We could not agree on relative valuation.

We then looked at how much money is invested in their company and the expectations of their VCs around valuation. We were able to get clarity in terms of cash expectations, and get comfort in terms of the metrics to validate those expectations. We then agreed to give them cash and subsequently went out and raised cash based on Kayak's trajectory. We raised cash at a high enough valuation that we were able to get over the relative issues. So, ultimately, it was an all cash acquisition.

**Sramana Mitra: What did that mean for the SideStep team? Did you want to retain that team or not?**

**Steve Hafner:** We wanted to retain their sales and marketing teams. At the time Kayak had 46 people and SideStep had 83 people. When all the dust cleared we had 7 or 8 of their people left.

**Sramana Mitra: The major gains from purchasing SideStep were adding their display advertising business and their email marketing platforms?**

**Steve Hafner:** That is right.

**Sramana Mitra: How big was that business for them?**

**Steve Hafner:** It was half of their revenues. At Kayak we are much less commercialization focused. I am personally not a big fan of display ads. We are very careful how we take SideStep's commercialization approach and apply them to Kayak. You will see some changes on the Kayak website based on insights we picked up and assets we gained from SideStep, however these changes are done in a very measured and controlled way.

**Sramana Mitra: Their revenue was approaching $35 million when you bought them?**

**Steve Hafner:** It was at $30 million.

**Sramana Mitra: Is that revenue stream continuing for you?**

**Steve Hafner:** That revenue stream is much higher now.

**Sramana Mitra: What kind of ramp did you see in the first six months after purchasing them?**

**Steve Hafner:** It was a very impressive ramp. Going back to the analogy of Google buying Yahoo!, just imagine Google powering the ads on Yahoo!. The user experience does not change all that much but Google is able to monetize 30% better than Yahoo! because their targeting capability is so much better. That is not a bad analogy when applied to how much better we can monetize the SideStep traffic.

**Sramana Mitra: Let's talk about applying a Vertical Ad Network within Kayak.**

**Steve Hafner:** One of the items in the secret sauce of Kayak is our ads along the right hand side of our search results pages. These ads look very similar to the search result ads that Google or Yahoo! provide. They are three lines of text and a hyperlink. The difference is that our ads are based on the actual search parameter. We know that Google doesn't know the city pair and the travel dates. When American Airlines buys ads on Google they are buying out the keyword pairs. They buy phrases like "cheap Chicago flight". The person might be searching for a flight from Omaha and American may not fly that city pair. American has wasted their money and the consumer has wasted their time. If the consumer does click the ad they get to a page on American Airlines which does not have that much information on it because American Airlines didn't know they were starting in Omaha.

With the Kayak model American Airlines ads will only show up on the routes they fly. When someone clicks on that ad we pass the search parameters on to American. The result is you get a search results page on American that contains the actual city pairs. The ads are targeted, which means they are more useful for the consumer and the results page is more useful as well. The net impact of that is a much higher ROI for American Airlines as well as for all of the other advertisers. It is also a much better consumer value proposition and it monetizes much better than Google does.

**Sramana Mitra: What is your read on some of the other travel Ad Network players out there? There are some Vertical Ad Networks which have been reasonably successful so far.**

**Steve Hafner:** There are three things you need to do to have a viable Vertical Ad Network. You need to get a set of publishers, you need to get an audience, and you need to match them with technology. It is my observation that Travel Ad Network has a network of publishers and they are distributing display ads. They do not have the technology yet. It is primarily an outsourced sales effort for display ads. I don't think that approach works long term.

**Sramana Mitra: Most of the Vertical Ad Networks out there work like that right now.**

**Steve Hafner:** Which is not sustainable unless you have a technology that scales. The difference with our approach is we are building the platform and the technology to allow our advertisers to manage their own campaign and determine where their search results show up.

**Sramana Mitra: So far what you have talked about is specific to flights and hotels. There is a lot of publisher inventory out there that is not transaction focused such as travel guides.**

**Steve Hafner:** Absolutely. It is a less targeted business and as a result the CPMs are much lower. I believe the most valuable consumers are the ones at the point of purchase. If we get that piece right it is much easier for us to go up the food chain into the consumer's research cycle than it is for a publisher to come down into our space.

**Sramana Mitra: What do you think of Mobissimo?**

**Steve Hafner:** Not much. I think Beatrice is a great person and a pretty good CEO but they are undercapitalized, their technology does not scale, and they have not gotten any traction over the past three years. I would say Mobissimo is an example of a travel search company which built a product with a small team, got it out there, and received a little bit of press coverage. They don't have the capability to turn that into a mass market product.

**Sramana Mitra: What else do you see out there in terms of travel related sites?**

**Steve Hafner:** There is still a lot of innovation going on. The social networking sites are interesting but they do not monetize well in the travel space. There is room for someone to tell consumers where the best rooms are in hotels. There is a lot to be done on reducing friction in the check-in and check-out process. There is plenty of room for better utilization of mash-ups.

**Sramana Mitra: My main problem with the travel category is that it is still a fragmented experience. I have to hop from site to site. You don't solve that problem.**

**Steve Hafner:** We don't even solve cross-shopping on rates yet. What Kayak has been able to do is reduce the number of sites you have to visit when shopping for fares.

**Sramana Mitra: Are you going to try to get content in context eventually?**

**Steve Hafner:** We will have to do that to become the number one travel site world-wide and fill consumers' comprehensive needs. Those are our goals. It is a question of prioritization and time.

**Sramana Mitra: The next big thing for Kayak is the Vertical Ad Network and getting international business to ramp. Is that going to be mostly organic? I don't think there is a lot to acquire outside of Mobissimo.**

**Steve Hafner:** They do not have an audience. Their audience is really limited to cheap international flights. There are very few companies that have an audience. We are going to have to build our solutions from scratch.

**Sramana Mitra: I don't think there is a Vertical Ad Network available to acquire.**

**Steve Hafner:** The beauty of a Vertical Ad Network is if you get the right launch partners and you have 8-10 of the largest advertisers to buy coming out of the gates you have a very vibrant ecosystem within a month of launching.

**Sramana Mitra: Is there anything else I should have asked you that I didn't?**

**Steve Hafner:** No, this has been a fun interview. I really did enjoy the article you wrote on Forbes. I thought it was very insightful and spot on with what we are trying to do.

# Interview with Sean Broihier, CEO, Fine Art America

*Sean Broihier launched FineArtAmerica as an online marketplace for artists and photographers. I was blown away to hear that the company does $5 million in revenue with just three employees. Imagine that! Of course, ultra-light startups happens to be a key trend in the industry, and so is online marketplaces in the world of electronic commerce. eBay launched the trend back in the days of Web 1.0, and since then, many niche, contextualized online marketplaces have emerged. FineArtAmerica is a great case study that I find incredibly inspiring.*

**Sramana Mitra: Sean, let's start at the beginning of your story. Where are you from? What is your background?**

**Sean Broihier:** I am from a small town just outside Chicago. I was born and raised in the same house my entire life. My parents, two older brothers, and a younger sister lived there with me. My brothers are seven and eight years older than me. There were an old Commodore 64 and a Tandy TRS-80 lying around the house when I was a kid. I picked up a little book that taught me how to program BASIC, and I learned how to program as a seven-year-old on that Tandy.

I don't know why, but I took to it and loved it. I considered myself a normal kid. I played sports like soccer, baseball, and basketball all the way through high school. There is something about learning a skill at a very young age that sticks with you. I think you are better off learning a certain skill very young than trying to learn it later in life.

**Sramana Mitra: What about college?**

**Sean Broihier:** I went to the University of Illinois. I studied mechanical engineering. I programmed on and off through high school and took a big chunk of time off at college. I was in college from 1996 to 2000, and the Internet exploded. That is right when Netscape came out. I just became fascinated with programming for the Internet around that time. I graduated from college and took a job as an engineer in New Jersey. I worked there for 10 years, but I always knew I wanted to be an entrepreneur.

I attempted to quit that job multiple times. At one point I was trading stocks in Manhattan. Another time I was in Chicago trying to start my own engineering firm. Around 2005 I had my first good web business idea. I built a marketplace for engineering firms that allowed them to advertise their products on the Internet. They could advertise products, advertise upcoming events, and issue press releases. I built it, and it is called LocalAutomation.com. It still exists today, and for simplicity's sake, you can describe it as Facebook and an online marketplace for engineers. I built that at nights and on weekends while working a regular job. It was moderately successful.

My brother was working for an art gallery in Chicago. About a year later I was doing a basic website for the gallery he was working at. Every time an artist put out a new piece, was going to do an in-store appearance, or was changing a price on something, he was calling me to update his website. I realized there were artists and photographers all over the world who wanted an easy way to get their artwork online to sell.

I had an entire infrastructure in place from my engineering website that allowed engineers to upload items to the Internet. Back in the pre-Facebook and MySpace days, that was still a novel idea. I had that entire platform that had much better potential in the art space. I re-purposed the code from the engineering site and launched it as FineArtAmerica.com in early 2007. It just took off from there.

**Sramana Mitra: What is the business model behind FineArtAmerica?**

**Sean Broihier:** The business model is to create a marketplace of buyers and sellers. We allow artist and photographers to upload their images to our site. We then offer them for sale as framed prints, stretched canvases, acrylic prints, greeting cards, and so on. We have a print-on-demand business model. Independent artists and photographers all over the world can open an account on our site and upload their images, and our software will determine what sizes and products we can sell based on the size of the image. The artist or photographer gets to name exactly how much they want to charge for each product or size of the print that is made available.

When a buyer comes along, he or she can pick the print and size. We allow buyers to choose additional features such as colored mats and frames. They can customize the entire picture via our website and place the order. FineArtAmerica takes care of the entire transaction for the artist. We print, frame, package, ship, collect payment, and send the profits to the artist.

**Sramana Mitra: That is brilliant for photography. What if you are doing a painting or something that is not quite so customizable?**

**Sean Broihier:** For paintings we require a high-resolution digital file. You can either take a picture with a 12-megapixel camera mounted on a tripod, or you take it somewhere and have it professionally scanned. We allow the artists to offer the original paintings on the site, but we do not participate in that transaction at all. If you come to the site and see an original listed for sale, you will see a link to contact the artist to arrange a direct transaction.

**Sramana Mitra: Do you charge the artists a fee? How do you make your money?**

**Sean Broihier:** If an artist lists a print at $100, we consider that the cost of doing business. The buyer is going to want a frame and other enhancements. We treat the artist's cost as a material cost, so the buyer will only see the final price, which includes what we charge for the frame. Everything is paid for by the buyer. FineArtAmerica makes money because we get a wholesale discount on the frame and mat.

**Sramana Mitra: How did people start finding out about FineArtAmerica?**

**Sean Broihier:** There is a viral component to our business. We sell artwork by living artists. Art.com is the biggest name in the industry just because of the URL, but they sell artwork from classic artists. We sell artwork by living artists. They upload images and sell products through us and receive a check in the mail 30 days later. Artists get excited and tell their friends and families about our site. They join and upload their pictures. That feeds on itself.

I obsess over search engine optimization. We are number one for millions of search terms. "Landscape print" is a very competitive search term, and we are number one for that term. That brings in buyers and the excitement of selling brings in more sellers.

**Sramana Mitra: You rely on search engine optimization to provide a supply of customers through organic search. You rely on word of mouth to entice artists and photographers to sell their work through your site.**

**Sean Broihier:** I designed the entire site to be fully automated. It gives artists the sales and marketing tools they need to be successful. By doing so, the artists become a sales and marketing force not only for their own artwork but for FineArtAmerica as well. I built a capability that I would compare to ConstantContact into FineArtAmerica. It allows the artists to create attractive HTML newsletters through FineArtAmerica.

When you join our site as a member, you get a profile. You can load all of your images into the site and offer them for sale. With a few simple clicks, you can drag images into your newsletter, load in your email list, and send out a great newsletter. Artists love it because it is free and allows them to do email campaigns. They can track and see who opens their notes. When people click on the image link, it takes them to FineArtAmerica. That brings in benefits for FineArtAmerica and the artist as well.

**Sramana Mitra: So, you rely on that to drive a viral effect and bring a wide range of customers to FineArtAmerica?**

**Sean Broihier:** That is correct. The artists are happy and willing to send traffic to FineArtAmerica because we are their order fulfillment partner. I have written plenty of newsletters to artist and photographers explaining why they need an order fulfillment partner. It is very difficult to try to do this on your own. If you want to be able to sell your own prints from your home with custom matting and framing, you need a custom printer. You then have to stock a lot of materials, deal with customers, frame the products, manage shipping, and deal with returns. It is a nightmare.

All artists and photographers need an online fulfillment partner and that is the role we serve. We become their online store, and they are happy to have us work in that role. They post online links to us from their Twitter, Facebook, and social media accounts.

We give artists display tools on their websites. They can have their images scroll through and link back to FineArtAmerica. We provide them with a Facebook shopping cart. We give the artists a tool that allows them to embed a FineArtAmerica shopping cart on the Facebook fan page. This provides them a new tab on the bottom that says ‘shop.’ When people click on it, they see all of their artwork for sale.

**Sramana Mitra: There are significant logistics to your business. Would you explain how you manage that piece?**

**Sean Broihier:** We are currently partnered with three different fulfillment companies around the U.S. They are located in North Carolina, Atlanta, and Los Angeles. The entire system is fully automated. I will not do anything unless it is automated because I have such a small staff. The whole process of uploading images and setting prices is accomplished by the artists. The minute an order comes in a, FineArtAmerica staff member quickly reviews each order, examines the images, and makes sure everything is correct. Photographs are not an issue; they get approved and sent off to fulfillment immediately. Paintings are a little tricky because sometimes painters are not the best photographers. Sometimes the pictures they upload are blurry or are not cropped correctly. There is potential there could be an issue with the image. As soon as our staff member confirms that the images look good, they submit the order.

Processing the credit card is fully automated. The order details are instantly transferred to one of our fulfillment centers. Each center handles a different product. Greeting cards are handled in Atlanta. Framed prints are handled in North Carolina. Our code knows where to send the orders. Those companies handle the printing, framing, packaging, and shipping. Their system is tied into ours, so as soon as they ship an order the details come back to us. We send out the email confirmation to the buyer, and that is it.

Our volume is large enough that we have a dedicated group of people at each site who handle the FineArtAmerica orders every day. As far as the buyer is concerned, it is a seamless process. If they are not happy with the product, they ship it back to FineArtAmerica directly.

**Sramana Mitra: In 2009 you did $1 million in revenue. How have you ramped since then?**

**Sean Broihier:** We crossed $5 million in revenue just two years later.

**Sramana Mitra: How have you built the business from a team perspective? How many employees do you have, and what functions do they serve?**

**Sean Broihier:** The entire company has three people on payroll: me and two other individuals who cover customer service and technical support. Our customer service representative answers the phones, which typically is inbound calls from customers inquiring about orders. She also answers any emails that come into our customer service account.

Our technical support representative is in charge of quality control on all orders. We do quality control at the time of sale because of the sheer volume of images uploaded to the site. We are getting close to 10,000 uploads per day. It is humanly impossible to have someone look at 10,000 images a day and check them for quality. Our technical support representative is also the go-between

between FineArtAmerica and the order fulfillment centers. She is responsible for answering technical support emails, which typically come from the artists about how to use the site.

I am responsible for everything else. I do all of the programming, I write the newsletters, and I do the sales and marketing.

**Sramana Mitra: How do you manage all of the different functions?**

**Sean Broihier:** We have to send out profits to our artists once a month. We send out payments on the 15th every month. Half our artists choose to receive payments via PayPal. The other half chooses to receive payments via check. We send checks only to artists who live in the United States because we do not want to send checks all over the world.

I have built myself a dashboard where I click a button that generates a list of every artist who is due to receive a payment via PayPal. I click over the PayPal, load the information into PayPal and click submit. I pay several thousand people via PayPal in that manner in under three minutes. When it comes to checks, I have an agreement with Webmasterchecks.com that essentially follows the same procedure as PayPal, only with checks. My code spits out an Excel file of who is due to receive a payment and I upload that into my account at Webmasterchecks.com. They will send out all the checks on my behalf.

In terms of money coming in, we do all of our payment processing with PayPal. The money comes in and shows up right away in our account. Money going out is very simple. It is just my payroll that is done automatically by ADP. We pay our three fulfillment centers once a month. The business is really money coming in, payroll going out, three big payments per month to fulfillment centers, and payment to artists. It is all fully automated in our system, and we know all the information because we are the marketplace.

I do all of the programming on the site. Any new features that need to be developed are done by me. We are getting ready to offer a new product in about a month. I will write all the code to manage the image rendering and make the images appear on that product.

**Sramana Mitra: You are demonstrating a modern way of doing business. This is an efficient way of doing business and bootstrap. Do you use any freelance workers?**

**Sean Broihier:** I have outsourced my server administration. When I started the business in 2007, it was running on one server and now we have eight servers. When I do run into an obstacle that I know I am not well suited to address, I find a freelancer to help me address it. I have TV commercials airing now and I have contracted with an animator out of Canada who put together a fantastic 90-second video about FineArtAmerica. It is hand-drawn in the old Disney style. We run it on the website, and he is in the process of cutting it down to a 30-second version that we will run on TV.

**Sramana Mitra: How did you find the animator who has done your commercials?**

**Sean Broihier:** l lived in New York for a couple of years. I know a few people who run Internet-related businesses in New York. He did some animation work for them, and I saw it and loved it. I reached out to him in the middle of last year and asked him to do a project for me.

**Sramana Mitra: I hired a cartoonist through oDesk not long ago. We now have a cartoon strip running on YouTube. We do a lot of freelance**

**hires. Our payroll is zero. I agree that these types of projects are better done in freelance mode.**

**Sean Broihier:** I love what he has done, and I will use that ad for an entire year. I don't need an animator on staff. I just need someone for a project-by-project basis. It is sort of becoming a freelance world out there. Yes, he charges more than it would cost me if he were on my staff, but in exchange, I don't have to have someone on my staff year round whom I have to find work for year round.

**Sramana Mitra: Would you provide us some key metrics? How many artists and customers do you have?**

**Sean Broihier:** We are at 92,000 artists right now. We are adding anywhere from 150 to 300 new artists a day. We will be passing 100,000 artists sometime in March. Our sales for 2012 should be around $15 million.

**Sramana Mitra: How many customers does it take for you to do your current $5 million in revenue?**

**Sean Broihier:** Fewer than 200,000 customers. It is actually on par with the number of artists we have, just slightly higher.

**Sramana Mitra: That is interesting. This is a relatively small community. I am not saying that in a judgmental way. If I had to guess, I would have assumed that the number of customers would be tenfold the number of artists.**

**Sean Broihier:** The vast majority of orders go to non-artists who have found us through Google or Facebook. You would expect that if you had five artists, you would have 25 buyers to keep them happy. However, because we are free to join and everyone has seen how fast the business is growing, we have attracted a ton of artists. The pace of buying has not kept up currently. Obviously, we are growing quickly. If word got out that FineArtAmerica was doing incredibly well, then I could have another 200,000 artists sign up overnight. I am not necessarily going to see a correlation in the number of buyers signing up at the same time.

**Sramana Mitra: What kind of money do your most successful artists make in sales from FineArtAmerica?**

**Sean Broihier:** Our best-selling artists are in the range of $5,000 to $10,000 a month. That is a small number of artists.

**Sramana Mitra: What accounts for the success of some artists and the lack of success of others on FineArtAmerica?**

**Sean Broihier:** There is a disproportionate distribution of wealth because we do not have a huge bulk of buyers relative to artists. There are some artists who are making an enormous amount of money and some who are making relatively little money. It all comes down to how the artists take advantage of the tools we give them and how they market themselves. The artists who are making $5,000 to $10,000 a month are putting in the required time and energy to generate their own sales. They are doing email campaigns, they are going to art fairs, making TV appearances, and attending trade shows. We are just doing fulfillment orders for those types of artists.

We are a marketplace that gives you tools to be successful. With so many artists on the site, we cannot provide them all with individualized sales and marketing attention. All we can do is give them tools to help them be successful. People who sit around and take the wait-and-see approach will have one or two sales a year. As for anything in life, you will not be successful unless you put effort into it.

**Sramana Mitra: From your business point of view, you are expecting to go from $5 million to $15 million of revenue in a year. What are the levers of that threefold growth?**

**Sean Broihier:** We have been on a threefold growth curve for years now, and it shows no signs of stopping. It has been a very predictable curve where we peak in October, November, and December. Based solely on the trajectory that we have been on for the past three years, I expect to hit $13 million to $15 million of revenue this year.

When 99% of the general population thinks about buying artwork online, there is no company that comes to mind. There is no dominant brand. They don't know where to buy artwork. When they decide they want to buy a New York [City] print, they just go to Google and search for it. I take steps to make sure that I am the top search result naturally and paid. On top of that, I have a bunch of programs in place to brand FineArtAmerica to buy artwork online. When you think of buying books, you go to Amazon first. When you think of buying art, I want you to think of FineArtAmerica first.

I have a bunch of plans in place. We have marketing efforts in place to focus on branding the business. We have great growth in artists, great growth in buyers and great growth in traffic. I now want to see great growth in the brand.

**Sramana Mitra: It sounds like you are expanding your search engine marketing beyond just SEO and are now doing pay-per-click. It also sounds like you are adding in branding efforts and TV commercials to**

**establish yourself as the place to buy art online. Where are you going to run these TV commercials?**

**Sean Broihier:** They run all over the place right now. We have them running on Bravo, HGTV, and other places.

**Sramana Mitra: That's expensive.**

**Sean Broihier:** It is pretty expensive. It is hard to gauge and correlate that an ad ran at 8 p.m. on Thursday to any defined number of orders. When you see a Coca-Cola ad on TV, you are not immediately running to their website to buy a Coke. After weeks and months, when you have seen enough ads on TV, you will start to think about Coke when you are thirsty.

**Sramana Mitra: I am not convinced that this is a good idea. I think you are going to spend a lot of money with limited returns.**

**Sean Broihier:** What if I told you it was not that expensive?

**Sramana Mitra: Running ads on Bravo is expensive.**

**Sean Broihier:** For us it is not as expensive as you might think.

**Sramana Mitra: Whom do you consider as your competitors? If Art.com is selling Picasso, they are not your competitors.**

**Sean Broihier:** Most of the artwork on our site is from living artists and photographers from all over the world. The images that Art.com is selling are supplied to them from large image libraries all over the world. National Geographic sells all of their nature photography through Art.com. National Geographic also has an account through FineArtAmerica and sells images through us as well. The company that provides the stock images of Picasso and

Monet to Art.com provides the same images to us as well. We do compete head to head with them on those images. On top of that, we have the added advantage of being a vibrant community for living artists.

Aside from Art.com, we compete against CafePress.com, not only against the artwork they sell on their site, but they bought Imagekind.com in 2008. That is a direct competitor to FineArtAmerica. There is a company called RedBubble out of Australia that has a similar business model. Zazzle sells artwork as well.

The big advantage I have against competitors like Art.com or CafePress is that their model is that they sell a product for a set price and they will offer to cut the artists a 15% commission, take it or leave it. In the case of a 24" by 36" print, Art.com will decide how much it will sell for. If they sell it for $30 they will cut the artists a 15% commission, which will be $4.50. It does not matter if it is an independent artist or Getty Images. That is all they offer. We allow the owner of the content to set whatever price they want. When I approached National Geographic, they were shocked that they could charge whatever they wanted for the images. They consider their images to be premium images, and we allow them free reign to set pricing as they please. As a result, big image libraries are signing up with us.

**Sramana Mitra: Does anybody have a serious hold on the PPC and SEO terms that you are competing for?**

**Sean Broihier:** In terms of PPC, I find that Art.com and their sister company AllPosters.com are primarily the ones who are active. The [market] is a free for all, and I like to think that we are doing a great job of being in the top three on all the terms.

**Sramana Mitra: I love the story and how efficiently you are operating the business. You are creating value and generating money for artists all over the place. Great work.**

**Sean Broihier:** Thank you. Every once in a while I get asked why we are so small and why we are not creating a ton of jobs. I use my North Carolina fulfillment center as an example to answer that type of question. I am not in that facility day in and day out, but there is a dedicated staff of people who fulfill FineArtAmerica orders day in, day out. They are not on our payroll, but we have essentially created those jobs. We send out thousands of payments to artists all over the world. Everybody gets to set exactly what they make, and that is what I like about our model. Our artists are happy, fulfillment centers are happy, and FineArtAmerica is happy.

**Sramana Mitra: You have created an ecosystem that supports and awful lot of people. How many artist are making over $1,000 a month?**

**Sean Broihier:** I would say that there are 50 people who make over $1,000 a month. We send out thousands of payments of less than $1,000 a month to artists.

**Sramana Mitra: Great. This is a fantastic story; thank you for sharing it with me!**

# Interview with Alexander Zacke, CEO, Auctionata

*Auctionata is a professional online auction house. We're about to encounter the online version of Christie's and Sotheby's. This is also a marketplace, but a much more deeply personalized one, and a great deal closer to a Web 3.0 experience.*

**Sramana Mitra: Alex, let's start at the beginning of your story. Where are you from and where were you raised? What are the roots of your entrepreneurial journey?**

**Alexander Zacke:** I was born in Vienna in 1966. I grew up in a family of art dealers and collectors. The family business goes back four generations. I was raised among amazing art collections. I have known art from various cultures my entire life.

Very early on, I was interested and hooked on Chinese art and culture. I spent a week in Taiwan and I had a backpack. I slept outside of the National Palace Museum because it had the largest collection of Chinese art outside of China. I did not have the money to stay in a hotel and travel from the hotel to the museum, so I just slept outside of the museum for three nights. On the fourth night, they came out and told me they would give me a little room to sleep in, since I was so interested in Chinese art.

I founded my first gallery when I was 18. I published roughly 100 publications on Asian art, primarily Chinese art.

**Sramana Mitra: Where are you based now?**

**Alexander Zacke:** I am based in Berlin. I moved to Berlin two years ago to start Auctionata. I have also lived in Switzerland and Asia. I spent a long time in Australia as well. I have always been involved in the art business though. The art business has always been a global business and required a lot of travel.

**Sramana Mitra: What was the premise of the new company that you moved to Berlin to start?**

**Alexander Zacke:** All of the businesses I had before that were businesses that my family owned 100%. We never had an Internet business or anything like that. We had always been very conservative in our businesses. In the art world, there is a small group of people who do everything among themselves. It is almost like the science communities.

I did a lot of traveling and I learned about eBay in 1998. I was the first European seller that had $100,000 of sales in 1998. That impressed the people with eBay and they contacted me. Since that time, I did a lot of work for them. I built the eBay academy in Europe and I did political work with the European Union for e-commerce. I watched as eBay's business grew to embrace art auction within the eBay platform. That happened in 1999. They even tried to work with live auctioneers and for some reason their art attempts never worked.

**Sramana Mitra: What did you learn from watching eBay's struggle with art auctions?**

**Alexander Zacke:** In the mid-2000's, it became clear that the peer-to-peer marketplace model, although extremely powerful and scalable, did not work beyond a certain price point. The fine art world will begin at $1,000, which was 20 times the price point of eBay.

I started to develop the idea of building an online marketplace for fine art and fine art auctions. It was very difficult because eBay had failed. If a multi-billion dollar company with top global management has failed, then it is hard to believe that you will succeed in the shadow of their failure. I am not even a tech guy, I'm an art guy. So I had to go find a tech guy.

My co-founder who runs the tech side of Auctionata was introduced to me by the CEO of eBay Europe. We set out to create a marketplace and just put it out there to see what feedback we would get. We did that in 2011 while we were still in Vienna.

**Sramana Mitra: What was in your minimum viable product?**

**Alexander Zacke:** We launched a product that was a peer-to-peer moderated marketplace with a lot of live auction and listing functionalities. We also had a Facebook-type platform built in. It was as if we had put PayPal, eBay, Amazon, and Facebook into a single website. It was too complicated and became an enormous fiasco. It did not work at all.

**Sramana Mitra: Did you fund this effort from your family business?**

**Alexander Zacke:** I have always been very careful to keep the family business money separate from my personal business money. I did it with my own money and with some investment of my friends. We also brought on one of the top early stage VCs in Germany in the middle of 2011.

We got a lot of feedback from our first release. What we discovered is that our user base wanted us to replicate a brick and mortar auction house online. It really was that simple. We decided to shut down the old business and re-launch the site. I knew that I needed designers, marketers, and tech guys. That is when

I decided to move to Berlin. Vienna just does not have a tech startup scene that I could rely on.

We did our re-launch in November of 2011. We had no more funding so I rented a hotel room and that was our business office. I then met a former eBay executive who was now the CEO of a large rental marketplace. He gave me a few rooms in his office space.

**Sramana Mitra: You said that you wanted to replicate a traditional auction house. What did that look like for an online business?**

**Alexander Zacke:** A traditional auction house has three services. They provide valuation to potential sellers. They obviously provide the auction service. They also provide a fixed-price format. When we did our re-launch we decided to start with valuation. We created an expert network and offered everyone a free valuation. We would provide that valuation for any antique, piece of art, or collectable.

We put that offer online in a very simple, clear manner. We launched it at midnight and the following morning when I logged in at 9 a.m., we had 27 valuation requests waiting for us. At that point, I knew there was an enormous demand out there for people to get expert online valuations.

**Sramana Mitra: Did you expand Auctionata to include other auction house functions once you had verified market interest through valuation services?**

**Alexander Zacke:** From there, everything progressed very quickly. We did 400,000 valuations in our first year.

**Sramana Mitra: How did people find out about the site? How did they know you existed and that you offered the valuation services?**

**Alexander Zacke:** They came to us through organic Google searches. The people who were on the site spent a lot of time on the site and did a lot of things. The traffic was small but very valuable. The site also rated very well in Google searches for keywords such as antiques, auctions, or valuations. We had a lot of artist names, which really helped out. The vast majority of our valuation requests came from those organic searches.

**Sramana Mitra: Can you describe how you fulfilled the valuation requests? Did you have to get the art shipped to you?**

**Alexander Zacke:** No, that is the key part of our story. We do it all online. We have 300 art experts from 45 countries that cover 1,100 categories. We have built online software that allows you to upload the image of the piece of art that you would like to have us evaluate. We gather some basic information, such as the size and any history you may have with the piece.

That information goes into our back-end database. It is automatically categorized and forwarded to several of our experts. Whoever picks the case first will add their description and valuation of the piece. That is processed in our software and the valuation is returned to the individual who requested that we perform that service.

Our experts are paid a fixed-fee based on the number of minutes they spent on the case. That payment is done automatically and is processed into their PayPal accounts. If the item goes to auction, then they will also receive a commission. Once the valuation has been provided to the requester, our in-house team will have access to them. They will pick the top 20% of the cases they see every day and will offer the owners a contract to put the piece up for auction. Half of the time people just wanted to know what the piece was worth, the other half of the time they decide to sell.

Once the contract is in place, we will have the piece shipped to us. We will put it up for auction or we will put it on our online shop, depending on the value of the piece.

**Sramana Mitra: How do you manage the courier service? Is it your own service or do you use a commercial service? Where are you having the paintings shipped to?**

**Alexander Zacke:** We pick up the merchandise as soon as we obtain an auction contract. We then catalogue the item and run it through our in-house services. We take photos, authenticate the pieces, write descriptions, and link our work with research found in international art databases. We catalogue the piece scientifically and then list it in our online shop or put it up for auction.

When we do send a piece to an auction, it goes to an auction team. Contemporary team, the old masters team, or the Chinese masters team are a few examples. We have one live auction topic every week and it always changes. It may be contemporary art one week and wine the following week. Sometimes we have two auctions a week.

We acquire most of our merchandise from within the European Union, primarily in Germany and Switzerland. We do not accept consignments outside of the European Union unless they are extremely important pieces of art. It is customary to have logistic operations close to the seller. If we were to do consignments in the United States, we would have to run logistic operations there. That is a major operation and we are building that in New York City, but until that is open we won't accept consignments from the United States.

When we sell merchandise from auctions, we find buyers from over 100 countries. We ship globally to any country in the world. We have specialized logistic services depending on the categories of art. We have different shipping companies that we use for wine as opposed to jewelry. Right now 10% of our buyers are from China and the other 10% are from the United States. We have never had bidders from fewer than 25 countries in an auction and have had as many as 85 countries represented in bidding.

**Sramana Mitra: What is your competition? Do Christie's and Sotheby's have online auctions that compete against you?**

**Alexander Zacke:** There are no other online players that provide the same services as Sotheby's and Christie's. Our competitors are traditional auction houses. All of the auction houses are online to some extent. Some allow online bidding. At the end of the day, they all print catalogues that they send to their clients and they all exhibit the items they have on sale. We don't do any of that because we are 100% online. In the end, online buyers want to deal with online companies.

**Sramana Mitra: What kind of volume do you do?**

**Alexander Zacke:** We started having weekly auctions in May of last year. It took us a year to launch the valuation network. We have acquired roughly $50 million of merchandise and we have grown sales in the last 6 months from $0 to $16 million. Our current revenue run rate is $30 million and the net revenue run rate is $10 million.

**Sramana Mitra: What is your commission structure?**

**Alexander Zacke:** Our standard fees are 20% from the seller and 20% from the buyer. Our fees are negotiable, depending on the value of the consignment. The overall commission we receive will likely be less than 30%.

**Sramana Mitra: You said that you raised some money to build this company. Can you talk a bit more about your financing strategy?**

**Alexander Zacke:** We did a small round in 2012 and then a Series A after our first round of successful auctions. We took a total of $21 million from German venture funds between the seed and Series A. By the time we took our Series A financing, we had already shown a large user base and a viable business.

One of the key metrics in our industry is bidding volume versus net revenue. A healthy ratio is 1:5, and we are 1:11 or 1:12. The bidding volume in the past 10 months for Auctionata was $115 million. That is extremely high for a business that has been around for only a few months. For every dollar we have in sales, there are 10 times the amount of bids. That has been a key metric for our Series B round, which we are currently raising.

**Sramana Mitra: What did you have in place before you raised the first $3 million?**

**Alexander Zacke:** We did not have anything. We had a PowerPoint presentation. We raised that money on a concept.

**Sramana Mitra: I'm assuming the reason you raised that money was because of your deep understanding of the art auction business. Is that fair to say?**

**Alexander Zacke:** Yes, and we have a very credible strategy for bringing that business online. When I look back at that presentation today, I can see that we have executed exactly what we said we would. We have also hit the revenues exactly as we said that we would. That plan would never have happened without what we learned from our first unsuccessful launch.

**Sramana Mitra: How did you finance the failed beta launch?**

**Alexander Zacke:** It was done with my money and my co-founders' money.

**Sramana Mitra: So your lessons learned from that failed beta launch was compelling knowledge to let you raise $3 million in seed funding?**

**Alexander Zacke:** Yes, that was the important part. We made it clear that it would take a long time and that we would have to build a lot of infrastructure to bring a fine art business online. At that time, if you asked art dealers and auction houses about our plan, they would have told you that nobody would buy art online without having seen the work in person. We did not believe that hypothesis. I really believed that we could crack the code of selling 7-digit art pieces online if we did it right. We knew that if that turned out to be true, then we could build a business with billion dollar revenues like the major auction houses.

**Sramana Mitra: There is a very compelling element to your story. You are going to have access to the larger ticket items that are the economic drivers of a traditional auction house. However, traditional auction houses do not have the ability to scale. Auctionata has the ability to scale much faster.**

**Alexander Zacke:** That is exactly the case. We can scale very quickly. Auction houses have not grown as fast as the market that surrounds them. We believe that since we can reach a global audience, we can scale much better. People are coming from all over the world to these auctions. They will register and then 30 minutes later, buy a piece for $100,000 and send the money the following morning.

I have called some of those people and asked them why they were willing to do that because I did not think it would be possible at that price point. The outcome was that they had trust in our site and that they felt we were a very serious business. Most of them thought that our business had been around for a long time and we had just created our online presence. That proves that we executed our strategy. We have 300 art expert profiles online which includes their resumes. That is how people know that we are serious.

**Sramana Mitra: This is one of the best e-commerce business models that I have seen in a long time. The only one that comes to mind that is close to what you are doing is BlueNile. They also deal in expensive items and build trust with their consumers. You said a large percentage of your business is from China. Obviously, there is a lot of new money there. What are they buying?**

**Alexander Zacke:** We do a lot of auctions with Chinese art and those are good auctions. The Chinese are everywhere in the world and they bring art back to China. In the early 20th century during the Boxer Rebellion and the subsequent looting of the imperial palaces, there was an enormous amount of Asian art taken out of China.

When the economic rise of China started in the late 1990's or the 2000's, there was an enormous wealth that came up. There are over 1 million people who have over $1 million in their bank accounts. In the early 2000's, they started to find out that a lot of art was in Europe and America and that although people collected art, it was not that expensive. They started to buy this art and the prices really started to explode. Something that I would have sold 20 years ago for $1,000 will now sell for $100,000 or even $1 million. Chinese painters have risen dramatically during this time. There are eight Chinese painters in the top 20 right now.

The Chinese have a very different business culture. We absolutely must have Chinese speaking people in our business providing customer support. Our catalogs must be translated into Chinese. We even have Chinese support agents during our live auctions who can assist with bids.

**Sramana Mitra: You also get a lot of auction traffic from India. What do Indian's buy?**

**Alexander Zacke:** They buy pretty much everything except European furniture. They don't really like it. They buy a lot of Indian art, miniatures, and contemporary Indian art. I see the same trend happen in Morocco, Argentina, Mexico, and Turkey, where artists of those nationalities get a lot of attention within their countries.

The crazy thing with the art world is that there are artists everywhere and nobody recognizes they are there. They are hiding in small galleries and they tour around. Someone will buy a painting and hang it in their apartment. A year later, they have forgotten the artist's name. After 30 years, they die and their kids decide they want to learn about the painting because their parents liked it so much. They send it to us and we tell them everything about it, and often surprise them by telling them that the painting is worth $250,000. It's funny because in a lot of cases they are often ready to give it away.

This is the reason that Auctionata has become so popular in the media in Germany. Just last week, a major TV station featured us on one of their shows. They have a hidden camera show that tests consumer services. This show was about people who have an estate that they need to clear out, and the pickers that come in and make offers on the estate items. They contacted us and asked us to put in some rare paintings to see if the pickers would make a fair offer. They had 20 pickers come through and not one of them identified any of the paintings. We had paintings worth $50,000 and others worth $250,000 on the wall. They were making offers like $50 or $100.

The pickers were rather surprised when they found out the actual art prices. That show demonstrated to the audience that you have to be really, really careful when you inherit something. You may inherit an estate with a lot of items, but just one painting may be worth more than the entire estate.

**Sramana Mitra: I love this story. My husband is from Belgium and we have collected a lot of art.**

**Alexander Zacke:** Then you know what I am talking about.

**Sramana Mitra: Yes! I will be checking out your website as soon as we are done talking!**

**Alexander Zacke:** One day, you will have to check out a live auction. We do them every Friday, 9 a.m. Pacific time. It would be interesting to login and watch the live stream. If you are in a German auction, you can switch to the English stream. It is a lot of fun to see that auction. We have art experts there explaining the art to the audience. It is interesting to see where the dealers are coming from. You will see the country flags for all the people who bid on pieces.

**Sramana Mitra: Fantastic! I have really enjoyed your story, thanks for sharing.**

## From eBay Seller to $20 Million Revenue Business

Back in the days of Web 1.0, eBay kicked off the trend for online marketplaces in the world of electronic commerce. Since then, many ultra-light startups have mushroomed that focus on niche segments. Ultra-light startups have become a key trend in the e-commerce world andWatchUwant CEO OJ Whatley's entrepreneurial journey offers some delightful insights. Selling a product on eBay that was a passion, he went on to build a $20 million business with just 20 employees.

Watches had always been a passion with OJ. From Star Wars R2-D2 and Darth Vader watches, his passion evolved to freestyle sports watches and Casio G-Shocks.He bought his first luxury watch, a Rolex Submariner, with some prize money that he won in college. With WatchUWant, he wanted to take his passion and turn it into a profit opportunity.

After graduating from the University of Miami in 1992, OJ worked in the financial services industry and then at a software company. But watches were never far from his horizon. He started selling them on eBaywhile working at the software company. In 2000, when the software company looked likely to shut down, he focused on buying and selling watches from a brand called Panerai, which has been around since 1860.

OJ adds, "In fact, Panerai is the only company that's ever been able to buy watches from Rolex, put their name on those watches, sell those watches with Rolex dials or Panerai dials. When Rolex collectors had finally owned every vintage Rolex watch they could get their hands on, they turned to Panerai. All of a sudden, a new market was born. These vintage Panerai watches, which in

1998 were going for $5,000, were selling for $150,000 to $250,000 once the Rolex collectors hopped on."

Another reason for focusing on Panerai was that they were half the price point of Rolex. He could afford to buy $1,500 watches and make $500 to $800 on every watch.

In 2000, he sold 25 watches by himself. He reinvested every dollar he made back into his business. It was organically funded with a $3,500 credit card. In 2001, he sold 25 watches at an average of $2,500 per watch. In 2002, he sold about 40% to 50% more.

He bought these watches from collectors on a collector's forum site and on a watch-trading site. "What I found was that I could buy watches from enthusiasts who owned the watch and have grown tired of it or are ready to buy something else. I could buy those watches from them and make a market to sell those watches to people who were just starting to learn about Panerai."

It is interesting to note how OJ built up on the context, content, and community aspects of his Web 3.0 e-commerce business. Focusing on the Panerai watches provided the context of the business.

In 2000, he found some coffee table books on the history of Panerai at their store. This provided the content for the business and he found that they were selling from $100 to $150 at eBay while they could be ordered for free from the store. He had his co-workers at the software company order these books and in exchange took them out for lunch. He would then sell them on eBay for anywhere between $50 and $300.So, the content part of his strategy also became a big piece of his initial capital.

It also led the way to getting in touch with other Panerai enthusiasts and building on the community aspect. OJ also served as an advocate on the Paneristi.com site, which has grown from 10 followers in 1999 to 100,000 hits per month today.

OJ says, "Part of my success was by being an enthusiast as well as a dealer. I created alliances with other collectors and enthusiasts. I couldn't possibly dream of paying them $100,000 for a watch that I might sell for $120,000. They allowed me to sell the watch on their behalf on a consignment basis."

In 2003, when it became hard to find Panerai watches, OJ started selling other brands. His inventory had diversified, so he was selling more watches and by 2006, he was making $6 million in revenue working out of his house. The business was ultralight in every sense of the word: "It was me, myself, and I," OJ recounts laughingly.

However, in 2007, he was forbidden from selling on eBay. He had to sue eBay to be reinstated in 2008.eBay is still an invaluable showcase for their watches. However, this incident turned out to be a blessing in disguise as it forced him to look outside of eBay and start building his own site. They now have a website with substantial traffic and have a private showroom and sales office with 20 employees. They are expecting revenue of $20 million in 2014.

For an ultra-light e-commerce startup, the 4Cs (Context, Commerce, Content, Community) play a crucial role. You need to have a passion to be able to focus on a niche area (context) and find the passion to advocate the product and engage with other enthusiasts to build a community. Great content helps to engage such a community. If you get the formula right, you have a winning strategy for a successful ultra-light startup.

# Interview with OJ Whatley, CEO of WatchUwant

*OJ Whatley built a business up to $6 million with 'me, myself and I' and scaled it to $20 million with a small team. It's a jaw-dropping ultralight startup story!*

**Sramana Mitra: Let's start at the beginning of your story. Where are you from? Where did you grow up and in what kind of background?**

**OJ Whatley:** I was raised in Chicago. My father was a commodities trader. That's where I got in my blood the idea of buying low and selling high – the idea of speculation and entrepreneurship.

**Sramana Mitra: Entrepreneurship and speculation are not the same things.**

**OJ Whatley:** I think in a way they are. Entrepreneurship involves a lot of risk.

**Sramana Mitra: I don't believe in the idea that entrepreneurship is speculation.**

**OJ Whatley:** Put it this way. To me, speculation is calculating risk as a function of reward and making good decisions based on that equation.

**Sramana Mitra: I'd be very blunt about my absolute bias against speculation in the raw form, which has come to dominate, especially, the world of finance today. It's reckless and unbridled speculation that is causing a tremendous amount of damage in the financial system. That's something that we are vehemently against. If you actually care to look at**

**our site, you would see that the whole project – 1M/1M – to a large extent came in response to that kind of speculators hijacking the system.**

**OJ Whatley:** Then I can see where you have a bias against that word, so I will certainly refrain from the use of that word.

**Sramana Mitra: This is not a trading company. It's a company where you're selling products. That's not necessarily speculation. Let's go back to your roots. What about college?**

**OJ Whatley:** I was raised in Chicago. The day I graduated high school, my parents retired to the west coast of Florida whereupon I went to the University of Miami for college. I majored in International Finance and Marketing and received the BBA degree in 1992. Having a father who was a commodities trader, financial services was always in my blood. Prior to starting WatchUWant, my foundation was financial services. That's where I learned to establish relationships and build value-added relationships where the value proposition is to understand what's important to your clients and help them basically visualize what's important to them, querify it, and then bring them the solutions that will allow them to get where they want to go.

**Sramana Mitra: You graduated in 1992. What happened after that? Did you start the company right after?**

**OJ Whatley:** No, I started this company in 2000. I was in the financial services industry working with life insurance and brokerage companies. I started with John Hancock Life Insurance and then went on to New York Life Insurance and Merrill Lynch.

**Sramana Mitra: What time frame does that cover?**

**OJ Whatley:** 1992 to 2000.

**Sramana Mitra: So in 2000, the dot-com crash happened. What did you do after that?**

**OJ Whatley:** In 1999, I sold my soul for the dot-com world, so to speak. I left the financial services industry to go work for a Linux-based software company.

**Sramana Mitra: What is it in your background that drew you to that?**

**OJ Whatley:** I think that's a really good question. I think there were two pieces to it. Number one was the allure of the dot-com world and technology. More fundamental than that though is that I was tired of being rejected. I had a lot of conviction and knew that the solution that I was offering was the best solution. No matter how good you are, it's still a game of numbers and about getting in front of as many people as you can. The level of competition and differentiation is minimal and the level of rejection is extremely high. So when I started WatchUWant, it was with the idea that I would buy watches and put them on eBay. Then, people who were interested in buying those watches would contact me. That was the genesis of WatchUWant.

**Sramana Mitra: You didn't want to do in-person selling that would give people an opportunity to reject you. It sounds like that's the core motivating factor.**

**OJ Whatley:** No, what it was about was that I didn't want to spend my time trying to court people who weren't interested in what I had to say. So I wanted to find something where people would come to me. I could still sell and selling is still a key component but the idea of selling to people who are interested in what you have to say as opposed to trying to find those people – a world of people who are sort of desensitized because they've heard it every day.

**Sramana Mitra: When did you start WatchUWant?**

**OJ Whatley:** I started WatchUWant in 2000 while I was working for the software company.

**Sramana Mitra: Why watches?**

**OJ Whatley:** I've always loved watches. Even going back to my days as a 10-year-old, I was always enamored of watches.

**Sramana Mitra: It's a passion.**

**OJ Whatley:** Yes. The price points were $10 to $300. I was always obsessed with watches and I've been wearing a watch since I was about 12 years old. It evolved. It started with Star Wars R2-D2 and Darth Vader watches. I wear some of them on a chain around my neck. It progressed to Casio calculator-type of watches and watches that would play music. Then, it progressed to the freestyle sports watches and Casio G-Shocks.

While a freshman at the University of Miami, I was representing my college on the Wheel of Fortune and won $16,900. Of this, $4,500 was a gift certificate to a jewelry store in Beverly Hills where I redeemed that gift certificate for two stainless steel Rolex Submariner watches – one for myself and one for my father. That was the first real luxury watch I ever bought.

**Sramana Mitra: What were you doing to do with WatchUWant in 2000? What was the game plan?**

**OJ Whatley:** The game plan was to make millions in the dot-com world.

**Sramana Mitra: I'm asking for more specifically what kind of watches were you going to sell? How much inventory were you going to buy? Where were you going to source these from?**

**OJ Whatley:** I couldn't afford the watches I wanted to buy. I couldn't afford to keep them but I could buy them and sell them for more than what I paid for them. So I could take a passion and turn it into a profit opportunity. While working for this software company, we started getting notices that said something to the effect of, "Great news! For every dollar you don't take in salary or payroll, we'll give you a thousand stock options." After not taking any compensation for about two months, suddenly the light went on that this company may not survive. That's when I stepped up my efforts to buy and sell watches primarily focused on one particular brand, which by 2000 I had a keen interest in. It was a brand called Panerai.

**Sramana Mitra: What drew you to that brand?**

**OJ Whatley:** What I like about Panerai is it was the largest watch in terms of size. It was 44 mm and that was gargantuan in 1999. In fact, it was comically oversized. What I fell in love with about the watch was that it had a genuine and unique history. During World War I and World War II, it was involved in making military spec-type components for special force military groups. Panerai was making the watches and underwater compasses that the underwater ballistic guys would use while diffusing bombs underwater or in underwater tactical warfare . It was a real history. There are history books written about these various special force groups. There's an Italian special force group. There's an Egyptian special force group and they're all outfitted with gears from Panerai.

**Sramana Mitra: What was the price point of this watch?**

**OJ Whatley:** One of the reasons I like Panerai so much was because it was half the price point of Rolex. I couldn't afford to buy and sell Rolexes but I can afford to buy $1,500 watches and make $500 to $800 on every watch.

**Sramana Mitra: Where were you buying these watches?**

**OJ Whatley:** I was buying these watches from collectors on a collector's forum site and on a watch-trading site.

**Sramana Mitra: These were separate sites? You were buying from these collectors from other sites and then selling on eBay?**

**OJ Whatley:** That is correct. In fact, one of the sites was called Paneristi.com, which is still in operation today. The other site is Timezone.com, which is a watch enthusiast community and one of its parts is the watch-trading forum. What I found was that I could buy watches from enthusiasts who owned the watch and have grown tired of it or ready to buy something else. I could buy those watches from them and create a market to sell those watches to people who were just starting to learn about Panerai.

**Sramana Mitra: How many of these transactions were you able to do?**

**OJ Whatley:** In 2000, I probably sold 25 watches.

**Sramana Mitra: You were by yourself, right? How about in 2001?**

**OJ Whatley:** In 2001, I just stepped up the volume.

**Sramana Mitra: Were you investing many to buy inventory?**

**OJ Whatley:** I was reinvesting every dollar I was making back into my business.

**Sramana Mitra: It was basically organically funded?**

**OJ Whatley:** It was organically funded with a $3,500 credit card.

**Sramana Mitra: In 2001, what kind of volume did you get to?**

**OJ Whatley:** In 2001, I probably sold 25 watches at an average of $2,500 per watch. In 2002, I probably did 40% to 50% more. My business just grew exponentially from there. In 2006, I was doing $6 million in revenue out of my house with me, myself, and I.

**Sramana Mitra: Just selling these watches?**

**OJ Whatley:** Buying and selling watches.

**Sramana Mitra: On eBay?**

**OJ Whatley:** On eBay, that's correct. My model became eBay-driven in 2003.

**Sramana Mitra: Talk a bit more about some of the granular details of specific elements?**

**OJ Whatley:** In 2000, I walked into a watch store and I happened to pick up these hardcover books on the history of Panerai. They were like coffee table books. I went on eBay and found about eight of these in different languages. I noticed that they were selling from $100 to $150 each. I found out that you could call Panerai on the 800 number and ask them to send these books to you and they would send them to you for free. I had my co-workers order these books and in exchange, I would take them out for lunch. I would then sell them on eBay for anywhere between $50 and $300. That was a big piece of my capital.

**Sramana Mitra: Was that also getting you in touch with people who are passionate about Panerai?**

**OJ Whatley:** 100%. These went hand in hand with the people who were buying the watches – who were trying to educate themselves about the watch. They were starving for every piece of history that they could get their hands on because Panerai is a company that's been around since 1860. In fact, one of the interesting facts about Panerai is that they're the only company that's ever been able to buy watches from Rolex, put their name on those watches, sell those watches with Rolex dials or Panerai dials. It really was an unheard of relationship that to this day, no one understands how it came to be. That association with Rolex really drove the brand and drove the reputation especially for vintage Rolex collectors because when they had finally owned every vintage Rolex watch they could get their hands on, they turned to Panerai. All of a sudden, a new market was born. These vintage Panerai watches, which in 1998 were going for $5,000, were selling for $150,000 to $250,000 once the Rolex collectors hopped on.

**Sramana Mitra: Were you able to get to that market – to be able to source a $5,000 watch and be able to sell up for $150,000?**

**OJ Whatley:** That's a great question. In fact, part of my success was by being an enthusiast as well as a dealer. I created alliances with other collectors and enthusiasts. I couldn't possibly dream of paying them $100,000 for that watch that I might sell for $120,000. They allowed me to sell the watch on their behalf via a consignment basis.

**Sramana Mitra: Then shared the profit?**

**OJ Whatley:** Either shared the profit or they would just say, "Hey, get me $100,000 and anything over that is yours to keep."

**Sramana Mitra: You were making very good margins from these transactions?**

**OJ Whatley:** Yes. Every watch you buy, you don't always sell for a profit. Sometimes you do lose money.

**Sramana Mitra: Go back to the book strategy through which you connected with some of these passionate individuals.**

**OJ Whatley:** The book strategy was a website called Paneristi.com, which in 1999 had 10 followers. Today, they probably have 100,000 hits a month.

**Sramana Mitra: You own that site?**

**OJ Whatley:** I don't own that site. I became friends with the founder of that site and I basically served on that site as an advocate. I was an advisor so that whenever anyone had a question about buying their first Panerai, I would normally get shout-outs from the community. People would say, "Hey, call OJ. He can get you what you're looking for." I have a lot of support from the community because I put myself out there as someone who wanted to meet other people who were enthusiastic about Panerai. I became accessible. My calling card was my name and my cellphone number.

**Sramana Mitra: You were active in the Panerai community?**

**OJ Whatley:** Yes, very much so and I still am today.

**Sramana Mitra: How big is that community?**

**OJ Whatley:** From 2000 to 2010, Panerai was the number one hottest selling watch brand in the world.

**Sramana Mitra: How much of that community are you in touch with?**

**OJ Whatley:** It's a really good question because what I quickly found out was that Panerai enthusiasts were typical watch enthusiasts. You don't decide you like watches and then fall in love with Panerai. You typically love watches and then you discover Panerai. Or you liked watches but there was something about Panerai that you just didn't understand. When someone explained it to you, all of a sudden it made sense and you develop this voracious appetite to learn, and consume as much Panerai knowledge and buy as many Panerais as you can get your hands on.

One of the keys to Panerai's success in the early 2000 was a very limited production along with every watch being individually numbered so you knew exactly how many watches they made for that year. It was a very simple serial number system where you could identify the year of manufacture followed by how many pieces were made for that year. There was total transparency. This was ground breaking because no other watch brand had any way to tell people when watches were made or how many were made. Rolex had a serial numbering system but it was a little convoluted. With as many watches as they are turning out, it was very difficult to really get clarity but with Panerai, if there was an A on the case stack, it means that it was made in 1998. B is 1999. C is 2000 and all the way up to the current letter which is P, which is 2014 production.

**Sramana Mitra: It sounds like your business was entirely Panerai until what year?**

**OJ Whatley:** Until about 2003.

**Sramana Mitra: What did you do after 2003?**

**OJ Whatley:** Again, I've always loved watches. Panerai has captured my heart. In fact to this day, my license plate is Panerai. I fell in love with Panerai like no other watch. I love watches to begin with. It took me a couple of years because a lot of people were telling me that Panerai was a bubble. It was going to burst – that Panerai couldn't justify the resale prices or the profit margins on the watches I was making.

Most importantly, I had conviction because I really loved the brand and loved what it stood for. I put myself out there as a specialist, an advocate, and an enthusiast. I was willing to talk to dealers about it because most dealers didn't understand Panerai. I became their go-to Panerai guy. Whenever they got a Panerai to buy or sell, I was the first call they made. I would tell them exactly how much I want to buy it for. I would tell them exactly how much they could sell it for. Sometimes, they sell it to me and other times, they didn't. I figured it was all part of the business.

**Sramana Mitra: In 2003, you decided to sell other watches. Can you talk about that?**

**OJ Whatley:** It wasn't necessarily that I decided. It was that I figured I could sell more watches if I took trades. As much as I love Panerai, to buy and sell only Panerai was a limiting proposition. Coming from the investment field, I know all about diversification. I figured out that I could sell a lot more Panerai as well as other watches by taking trades and by becoming an authority in other brands. I can't say that from 2000 to 2003, I never sold anything but Panerai. I sold other brands other than Panerai but Panerai was where my passion was.

**Sramana Mitra: So what happened in 2003?**

**OJ Whatley:** It became a little harder to get the watches. There was a little more competition. Again, I didn't make a conscious decision per se, but my inventory had diversified, so I was selling more watches and doing more volume. In doing more volume, there was more trade.

**Sramana Mitra: This is actually a good segue into a question I'd like to ask you. How much of an inventory do you have to manage? It sounds like you were doing this out of your house. These are big-ticket items. You're operating out of a small space.**

**OJ Whatley:** I recall one time leaving on vacation for a week and taking my inventory of watches, putting them in a bag, and putting them in my ceiling because I didn't have a safe. I only had an alarm and I didn't have insurance because I wasn't a business operating out of a business. I was a business operating out of a house and therefore, I can't get insurance.

Interestingly enough, because I started this business working out of my house, I never advertise my home address as my business address. I always use a shipping store. That would allow me not to have to worry about being there for package pick-ups and deliveries. It also allowed that people I didn't know wouldn't just stop off of my house, ring my doorbell looking to see watches. Even before then, I was conscientious of security and trying to maintain a low profile. In fact, I would meet people at Starbucks to show them watches. If I was unsure after I showed them the watches at Starbucks, I would drive around in circles before I went back to my house just to make sure I wasn't followed.

**Sramana Mitra: If you looked at the progression through the years, is the volume that you're transacting significantly high now? Do you need a warehouse?**

**OJ Whatley:** We have private showroom and sales office. I've got 20 employees here and we do maintain a substantial amount of inventory.

**Sramana Mitra: You're based in Florida?**

**OJ Whatley:** When I was working out of my house in 2003, I moved in to a new house and I got a safe built into the closet. At that point, I probably had about 30 watches with a value of around $2,000 per watch. Again, I was just turning watches. I would put them on eBay. I would sell the watch. I'd get an offer to take another watch in trade. I had private clients I was doing business with locally in South Florida. My business was just growing. Again, I wasn't taking anything out of the business. There was one watch I sold for a substantial profit and I didn't get a penny out of the business. I just used it to buy more inventories.

**Sramana Mitra: You said in 2006 you were doing $6 million?**

**OJ Whatley:** Yes, $6 million – $500,000 in receipts per month.

**Sramana Mitra: What was the inventory situation at that point?**

**OJ Whatley:** I probably had closer to 50 to 80.

**Sramana Mitra: That's still out of your home?**

**OJ Whatley:** It was still out of my house.

**Sramana Mitra: The built-in closet was where you were storing all these?**

**OJ Whatley:** Yes. The reason I moved into an office was not because I wanted to expand the business. It was because I couldn't get insurance working out of my house. That and I needed a phone system. I really needed to build a real infrastructure.

**Sramana Mitra: When was the first time you added employees into the business? You said until 2006, you were alone.**

**OJ Whatley:** In 2005, I brought on an accountant who would come in once a week and help me with my books. Then when I moved into the office, he became my controller. Then I brought on a sales associate.

**Sramana Mitra: What was the role of the sales associate?**

**OJ Whatley:** Helping to put watches on eBay as well as to help us buy and sell watches.

**Sramana Mitra: Is the business still an eBay only business or has it gone beyond that?**

**OJ Whatley:** It's definitely beyond eBay. eBay is still an invaluable showcase for our watches. We have a website where we have substantial traffic as well as our offerings get taken and get aggregated to other watch sites.

**Sramana Mitra: What year did you move beyond eBay?**

**OJ Whatley:** In 2007, I was told that I could no longer sell watches on eBay.

**Sramana Mitra: Why?**

**OJ Whatley:** To this day, I still haven't gone to the bottom of it.

**Sramana Mitra: That sounds very odd, doesn't it?**

**OJ Whatley:** It's extremely odd. It's unheard of. I had to sue them to get back on to eBay and I was reinstated on eBay in November 2008.

**Sramana Mitra: I assume you were a huge eBay power seller at that point in 2006. Why would eBay cut you out?**

**OJ Whatley:** It's still an unanswered question to this day. I literally had to sue them over the course of a year to get reinstated.

**Sramana Mitra: While you were shut out of eBay, what did you do?**

**OJ Whatley:** I started building my own website and I started allowing dealers to represent my inventory.

**Sramana Mitra: Did that generate commensurate business as you did on eBay?**

**OJ Whatley:** I don't think it generated the same level of business because it took us six months to get our website up and going. Even then, you still had to start growing traffic. It was enough to survive. In a world where I thought the sky was falling, it was enough to survive.

It goes back to my philosophy that I had when I started this business. When I started this business, it wasn't about profit. It was about cash flow. It was about as long as you've got watches, and you're not taking money out of the company, and you need money, so you need to sell those watches. It's not about what you can sell those watches at. It's that you need money, so you need to sell watches. As you long as I had inventory, I was able to sleep well at night.

Back in those days, I wasn't looking at gross profit margin. I wasn't looking at average cost per unit or average profit per unit. I didn't have that kind of business intelligence or metrics. For me, it was how much cash flow did I generate? How many watches do I have in my safe? How many did I sell last week? What are the watches that I can buy? Much of my selling activity was generated as a function of buying opportunities more so than having any kind of sales goals, per se.

**Sramana Mitra: At the end of 2007, you got reinstated on eBay?**

**OJ Whatley:** No, in November of 2008.

**Sramana Mitra: So 2007 to 2008, you had to operate with your own website?**

**OJ Whatley:** Yes.

**Sramana Mitra: It sounds like this also forced you to look outside of eBay and start building your own site, which at the end of the day, turned out to be a good thing.**

**OJ Whatley:** That's diversification, right? When we got kicked off of eBay, I had registered the domain name WatchUWant.com. However, when you went to WatchUWant.com, you would basically see a hyperlink that said, "Click here to view our watch collection." That would take you directly to our eBay store. That's how devastating being kicked off eBay was, especially not knowing why and not having anyone that you could talk to about it. To this day, I still don't know why. I believe it was pressure put on eBay by the manufacturers. For what reason, I don't know because I've never knowingly sold a counterfeit or fake watch in my life. I'm the biggest fan of the manufacturer there is. Like I said, it's one of those mysteries that will probably go to my grave unsolved.

**Sramana Mitra: Regardless, in 2008 you were generating business at your own site. Talk to me specifically about your own site – developing your own site, business on your own site, the traffic. How much business do you do today on your own site?**

**OJ Whatley:** Back then, as it is today, it's primarily keyword-driven. Originally, it was all organic. It was a matter of getting as many relevant keywords in the title and in the top 10% that Google might scrape to have relevancy. I think one of the things that gave us greater relevancy and searchability was the fact that we were constantly putting up new inventory. That's true today as well. Each day, we probably post five to ten new watches every day. There's a constant new supply of inventory and content coming in.

**Sramana Mitra: In that effort, what kind of competition do you have to deal with? Are there other sites online that are doing similar things that you compete with?**

**OJ Whatley:** Our business has evolved significantly. We have now become the largest buyer of pre-owned luxury watches in the world. As a result of being the largest buyer of pre-owned luxury watches in the world, we're probably the largest seller of pre-owned luxury watches as well.

**Sramana Mitra: From a search engine optimization point of view, you are in the first or second slot in every single search of pre-owned luxury watches?**

**OJ Whatley:** Yes.

**Sramana Mitra: So organic search traffic is still powering a lot of your traffic?**

**OJ Whatley:** Yes, but you can imagine, we have a substantial pay-per-click and digital marketing budget today. It's probably one of our single greatest expenses on an annual basis. It truly is about staying on top of mind and it's truly about maintaining the position on top. There're always ten guys looking to spend more money than you, take your credibility, just knock you off the block, or render you irrelevant.

**Sramana Mitra: What is the split today – from business that happens on your own site versus business that happens on eBay?**

**OJ Whatley:** I would say eBay. I would say probably that 20% of our business is done via eBay. Keeping in mind that eBay is still the largest aggregator of watches in the world, so consider eBay to be a showcase and some people choose to do the business through eBay. Other people see the watch on eBay and choose to call us directly. It's not a perfect science in that you can't say exactly what percentage is eBay-driven.

I can tell you what percentage of our business is done on eBay with people completing the transactions through eBay. That's probably around 20%. But as far as what our real eBay business is, it's a hard number to get a hand on because you get a guy who sees a watch on eBay and then he calls our office. We have to track the fact that he saw us on eBay first.

**Sramana Mitra: Is the price different on your site versus on eBay?**

**OJ Whatley:** No.

**Sramana Mitra: Do you have the same price on eBay versus direct?**

**OJ Whatley:** Our goal is to maintain clarity. The price at which you can buy it on eBay is typically the same that we advertise on our website. Does that trend right into the prices we sell our watches out on eBay? No, because eBay has a built-in fee structure that can be pretty significant when you start adding in 3% for PayPal and 2% to 3% completed auction surcharge.

We have more negotiating room when someone buys a watch from us off eBay because you can negotiate the method of payment. I'm not going to charge you the same price if you pay me by wire transfer versus paying me by credit card because my best price is a function of payment by wire transfer. I'm going to give you a discount for payment by wire transfer or check. Whereas with credit card, I'm going to stick to my ask price.

**Sramana Mitra: Today, you have 75% to 80% of your business on your own website, right?**

**OJ Whatley:** Yes.

**Sramana Mitra: It sounds like that whatever calls that got you got kicked out of eBay actually turned out to be a blessing in disguise. You were forced to build up your own diversified strategy that you are much more in control of and have better margins on. It looks like this has resulted in a much more robust business today.**

**OJ Whatley:** Absolutely. There's certainly much more corporate value, so to speak, of having a website that gets 100,000 hits a month. I know that we can put up a watch today, and probably within three hours, someone will call us to buy that watch.

**Sramana Mitra: What is the revenue right now?**

**OJ Whatley:** We're shooting for $20 million.

**SramanaMitra: $20 million for 2014?**

**OJ Whatley:** That's correct. What I want to emphasize is part of my journey. I started this business as a guy who wanted to work out of his house without relying on anyone. Now in 2014, the success of my business is from relying on other people. Being able to communicate my vision as it evolves so that we can grow the way I see us growing.

**Sramana Mitra: How many people do you have?**

**OJ Whatley:** We currently have 20 employees.

**Sramana Mitra: That's very good – 20 employees, $20 million in revenue.**

**OJ Whatley:** Half of those are sales associates.

**Sramana Mitra: That is my next question. What is the composition? Half are sales associates, what is the other half composed of?**

**OJ Whatley:** I just want to clarify because our business is about buying watches. We'll sell the watches we buy but we've to get the watches in first. About 70% of our efforts are focused on getting watches and 30% are focused on selling.

**Sramana Mitra: When you say sales associates, it's actually the buyers and sellers?**

**OJ Whatley:** Correct. In addition to those 10 sales associates, I've a full time professional photographer on staff who brings to life all of our watches. I've a full-time controller and bookkeeper because we have a lot of transactions and we have a lot of documentations. I've an operations manager who handles all of the incoming and the outgoing. I've a full time professional master watchmaker on staff. I've got a full-time refinisher and an assistant watchmaker on staff. I got a President who oversees all daily operations. I also have an eBay manager and a posting manager.

**Sramana Mitra: Nonetheless, it's a relatively small team. $20 million in revenue being managed by a headcount of 20 people, it's a very light team. From a business model point of view, the beauty with what you built is it's, in a sense, an ultra-light startup.**

**OJ Whatley:** We've been growing and shrinking. It's definitely an evolving process and one that you just can't stand to chance. You have to be constantly asking yourself, "Is this the right structure?"

**Sramana Mitra: I have one last set of questions. In the realm of optimization, it sounds like you have an ad hoc process of figuring out what price to sell something at. If you applied some more systematic optimization here, you could make a lot more money.**

**OJ Whatley:** I think you're very perceptive in that. In fact, we do have a lot of systemization. In terms of identifying the watches we buy and the watches we sell, that's where we've taken a really hard look and not left it up to chance. We have metrics where we can measure if we're doing a better job at buying or a better job at selling. We have metrics to dictate what we should pay for that watch, what we should ask for that watch, or how we can optimize the turnover on that watch.

For example, for us to buy a watch and sell it the first day we have it, is to me leaving money on the table. If the watch is here for two weeks and is reduced in price and is then sold, that tells me that we're optimizing and being the true market maker we want to be. That tells me that we are making the market for our watches as opposed to taking orders. Just because we buy right doesn't mean we can squeeze more profit out of each watch we sell. Again, trying to translate that to multiple layers is a big challenge, but we do have internal processes and systems that are unparalleled by any other company. They are all homegrown that are allowing us to scale and optimize internally so we don't make the same recurring mistakes.

**Sramana Mitra: This might be something that you want to run by a Mathematician or an Operations Research person. You can see if they**

**can model and help you come up with a process that allows you to do more. It sounds like that market of buyers has a lot of elasticity. They are tolerant of price. They will want the product. There's a lot of passion and desire to own the product. That's the kind of buyer with whom you have lots of negotiating leverage.**

**OJ Whatley:** We have more leverage with the seller than the buyer. The seller of the watch only has a few different alternatives where he can turn around and sell his watch. We get our customers more money for their watches than anyone else because we know what watches sell. We know what makes a watch more saleable. We understand what's important to our customers when they're selling a $20,000 watch. It's not about the price at that point. It's about the relationship, credibility, reputation, the process, and the experience. That's where I believe we're unparalleled at. That's where our differential advantage is. We understand that we are the best way to sell that watch for that customer if it's the right watch for us.

**Sramana Mitra: Very interesting story, OJ. Congratulations on what you've built here.**

# Mompreneurs Love To Sell Baby Products

The e-commerce model of business allows women entrepreneurs to have greater flexibility in their lives. That is probably why we see several mompreneurs launching home-based businesses, and some of them scale to much bigger outfits. Of particular significance are mompreneurs selling baby products online. Here are three inspiring stories of mompreneurs who used their love for babies, clothes, shopping, and sharing to create successful e-commerce ventures.

**Women Love to Share**

Smocked Auctions sells children's smocks and other clothing through comment-selling on Facebook. It was started by two friends and mompreneurs, Amy Laws and Nicole Brewer. They met in 2008 while trying to get back in shape after having their first children. They had a lot in common – their sons were of the same age and they soon had little girls. They became great friends and it was in the summer of 2010 while attending a sample sale in Dallas that the idea of doing business together was born.

The wholesale showrooms in places like Dallas and New York purchase sample sets from manufacturers and at the end of season, sell off the remaining stock through sample sales. The sample sale that Amy and Nicole attended was for children's smocks and outdoor play clothing and they thought the idea of shopping that way was brilliant. The clothes were their children's sizes and the prices were great. They thought they could host a sale, get some great clothes, and also provide a great service to their friends. They had their first sample sale in August of 2010 and sold 700 units for $20,000.

For some friends who could not attend their sale, they took pictures of clothes left over from the sale and posted them on their Facebook pages. Within hours of doing this, people they did not know showed interest in these clothes. That was when they decided to start auctioning through their company site on Facebook.

Their auction model is a cross between eBay and Craigslist. The price does not increase during the auction and there is no outbidding. The first person to comment for that size gets to buy that item. In their first year, they made a million dollars.

What strikes me as the foremost reason for the success of Amy and Nicole was that being moms themselves, they understood the product and the market very well. They were passionate about their products and wanted to share the shopping experience with their friends and customers. Their personal taste resonated with that of the customers. They offered great quality at great price points. They soon brought in their own label to control the style and volume of the clothes.

**Women Love Clothes**

When Amber Schaub started children's apparel company RuffleButts, she was not a mom yet but was planning to become one. She had left her job and wanted to start her own business. The idea for the company came when she went to a store to buy ruffled bloomers as a gift for a friend. The saleslady told her they didn't have any and wondered why they did not carry them because people came in looking for them all the time. That is what spurred Amber to get into this specific industry and start RuffleButts.

Amber did not have a design background but designs all the clothes for RuffleButts. She researched and studied how to design, get samples, and how the retail industry works. She even took a sewing class. She would draw things up and take her designs to a pattern maker who would convert them into a paper pattern. She would send those paper patterns to the factory where they would cut the fabric based on that pattern.

Amber adds, "I designed from a common sense perspective. I just put myself in the shoes of a mother who will be purchasing and I asked myself what would be important. It has to be soft, it has to hold up in the wash, and it has to have quality. I could not produce bargain apparel, but I still wanted it to be available and affordable to the masses."

Amber and her husband Mark invested $40,000 to start the business. She worked on getting a full collection produced and launched her site with e-commerce capabilities in August 2007. For about half a year, they operated in red. Amber worked hard on getting publicity for the business. Luckily, she got an opportunity to do an event at the Golden Globes with a few celebrities and their babies. Some of the celebrities were impressed, supportive and that catapulted her brand.

In late 2008, she had her first child and around the same time retailers like Nordstrom contacted her for her products. Soon, Target, as well as mom and pop stores across the country, followed suit because customers were asking for their products. In 2009, gross revenue was $375,000. In 2010, they crossed a million dollars and her husband left his job and joined her to maximize the opportunity. In 2013, their gross revenue was $5 million.

I have seen several talented professional women turn to entrepreneurship to achieve more satisfaction and a balanced life. Many of them have a strong sense of aesthetics and a fine understanding of what mothers want for their babies. Amber worked hard to combine these into a successful venture.

**Women Love Shopping Deals**

Steals.com is a daily deals website that caters to women in four niche areas– babies, scrapbooks, kids, and women. They are branded BabySTEALS.com, scrapbookSTEALS.com, kidSTEALS.com, and sheSTEALS.com, respectively. They launch one new 'steal'every 12 hours for high-quality products at 40% to 80% off the manufacturer's suggested retail price.

Founder Jana Francis decided to become a mompreneur after the birth of her third daughter. She had always been frugal and on the lookout for great deals. Her friends called her the Dotcom Princess, as she would tell them where to go online for the best deal. While looking for ideas to start a new business, she realized that there was no e-commerce site in the baby space that would tell you the story of the product, why you wanted it, and what problem it solved for you.

It took 18 months for Jana to go from concept to creation while working a full-time job with three children. The month before they launched the site, she took two weeks of vacation and went to a baby expo in Salt Lake City where she got 160 people to sign up for her email list. The night before the site was launched, she emailed her family, friends, and everyone on that list to share the website and spread the word. Today, they have 375,000 emails that are sent every day and have shipped 1.7 million orders. In their first year, revenue was about $650,000 and the next year, they did $2.4 million. They launched a new site every year and in the fourth year with four sites, their revenue was $16.4 million.

It is interesting to note how Jana also uses a niche talent pool of women like herself who are mothers of young children. 70% of her staff is women and 25% of them have had a baby in the past two years. Her buying team is full of talented women who are good at product selection and are in tune with their audience. She has also recruited some of her top customers and fans. Most of her customer service staff is able to work from home for 30 hours a week, which is tremendously helpful for them.

Jana mentioned, "I have two employees who brought their babies with them to work today. We use our team's babies on our website as models and we actually sign the release paperwork for that. It's a lot of fun for our employees. For me, it is very rewarding to know that the situation I dreamed of for myself is being provided for so many moms in Utah who would not have a job if they were not working here."

These case studies reiterate my thesis that Web 3.0 will organize itself around two specific elements: context and the user. Mompreneurs are perfectly tuned into a niche segment of mothers, a user that is very particular and passionate about the products that she wants for her babies. They are able to give mothers what they want because they themselves are mothers.

# Interview with Jana Francis, Steals.com

*Jana Francis had a career in corporate America when she was about to give birth to her third child. She wanted to continue working with three small children, and decided to switch to a mompreneur role, working out of her home. It's a common and sound choice, and online businesses, especially e-commerce ventures, lend themselves to this mode of work very well. In due course, Jana went on to build over $16 million in revenue and a wonderful environment for other moms to work at her company.*

**Sramana Mitra: Jana, where does your story begin? Where are you from and where did you grow up?**

**Jana Francis:** I grew up in Utah. My father was an engineer. I was raised in a household that had computers in every room when virtually nobody else even had one in their house. We had the original Apple, and my father would teach me how to write programs to get my name to flash across the screen. I was a very early adopter of technology.

I moved to Silicon Valley for four years to put my husband through chiropractic school. My time in the Bay Area was interesting. I became an eBay power seller.

**Sramana Mitra: When were you in the Bay Area?**

**Jana Francis:** I was there between 1996 and 2000. I was there in the good days. It was the height of the dotcom boom. I remember driving to work and seeing the eBay building go up. I looked it up and became a power seller before a lot of people were even buying online.

**Sramana Mitra: What were you selling online?**

**Jana Francis:** I would go to garage sales and find things that I knew were worth more money. I would take my own pictures, write my own descriptions, and resell them. That is how I paid my house payment. It was very expensive to live there, and my salary was not quite enough to cover the house and my husband's school. That taught me a lot about shopping and selling online.

Many other things happened while I was there to spark my entrepreneurial spirit. Fast-forwarding to 2006, I had my third child, a daughter, six years after my second boy. I had been working with KSL, a media company in Salt Lake City, and was heading back to work. A few things happened at that time. First, I almost did not enjoy my maternity leave because I was so focused on the day I had to go back to work. When I did go back to work, I pulled out of the driveway and felt very sad. I really wanted to be home to enjoy my motherhood, but did not have that chance.

**Sramana Mitra: Is that what drove you to become an entrepreneur?**

**Jana Francis:** As I drove away, I realized that I was a capable, smart girl who had been through harder things in life. I was perfectly capable of coming up with something that I would be able to do from home and make enough of an income to support the family. Once I had that realization, the ideas started to flow. I was not trying to think of an idea, they just popped in the back of my mind. I also really wanted to spoil my little girl. The reality is that they have cuter things for baby girls than baby boys. I started looking online for all the cute things there were for girls.

I was almost overwhelmed because a lot of the e-commerce sites were very generic. There was a picture, the same canned description, and possibly some measurements. There was not much there that would explain why I wanted to buy that item. It told me nothing about the brand.

My friends all called me the dotcom princess because online shopping was not mainstream in Utah, and I could always tell them where to go online to buy something for less. I have always been extremely frugal and I have always been looking for a deal. I have found ways to save money and make money. I went online to find the best things at the best price.

I always assumed a website existed that spoon-fed you the latest and greatest. I assumed there was a website in the baby space that would tell you the story of the product, why you wanted it, and what problem it solved for you. Once I started to do some research, I realized that it did not exist. I decided I needed to create it, and I had a burning fire to do it. I could not stop thinking about it. It did take me 18 months to go from concept to creation because I had a full-time career and three kids, one of which was a newborn.

**Sramana Mitra: Did you start the website while you were doing your full-time job?**

**Jana Francis:** Yes. I worked for KSL, the NBC affiliate in Salt Lake City. I had been there for eight years at the point that I left. I was in sales management running the Internet sales for our dotcom. That was a demanding career and that was one of the reasons it took me so long to make my dream a reality.

I did both for about five months. I really was the breadwinner in the family. My husband had graduated from chiropractic school, but he was still getting his business going. I did not have the ability to just quit my job and start a business.

**Sramana Mitra: In our program, we encourage people to start businesses**

**while holding onto a job. It takes a while for businesses to start generating income. Bills have to be paid. Starting a business on the side is a perfect way to bootstrap.**

**Jana Francis:** I agree. I had to leave five months into the business to focus on my startup.

**Sramana Mitra: What is the business model of your company?**

**Jana Francis:** The business model itself is extremely demanding. The name of the company is Steals.com, and we have four niche daily deal websites that cater to women. The first one I started is BabySTEALS.com. We launch one new steal every 12 hours at 8 a.m. and 8 p.m. Pacific time. It is typically a high-quality product, most often a boutique or higher brand name product, at 40% to 80% off the MSRP [manufacturer's suggested retail price]. We run the product at that price until it sells out, or until 11 hours have passed.

BabySTEALS.com was the first site launched, but I now have scrapbookSTEALS.com, kidSTEALS.com, and sheSTEALS.com as well. We have launched a new STEALS site every year.

**Sramana Mitra: Do you have a number of different items, or do you focus on just one item?**

**Jana Francis:** We will typically stock multiple numbers of each item. When you come to one of our websites, you will see one brand item, such as baby swings. You will then see many different patterns and sizes available for selection. We may have a thousand total baby swings, but there will be a different combination of patterns and prints. Consumers never know how many we have, and you never know when you are going to sell out. We don't know either because it depends on which items are popular.

We do buy the inventory in advance, which is unusual in the deal space. We were the first site for women, long before Groupon. We partner with manufacturers directly on the promotion of their products. It is really advertising for the manufacturers. We are giving them a stage, by themselves, in front of thousands of targeted customers. There are no competing products. There are no ads. It is just their stories, their products, and their brands.

We partner with the manufacturers in advance and select a date for the promotion. We buy the inventory that we select, and they ship us the goods. Our receiving department verifies the quantity, quality, color, and everything else. It goes through our photography department so that we can take images if necessary, which is almost always the case. We then send it through our copyright department. Since we have it in stock, we are able to ship within 24 hours of the purchase. The new deal sites that come up are really just middlemen; they place orders after the sale is over. That can take 14 days to 8 weeks to ship depending on fulfillment agreements.

We've named the company STEALS.com. Our tagline is that *it is not just a deal, it's a steal*. For us it's more than just price. It is about the overall experience and knowing you are getting a high-quality product at a great price. I would put our customer service department up against any e-commerce site, and I would bet that we would exceed expectations every time.

**Sramana Mitra: You spent five months working a full-time job and working your startup business in parallel. What were you able to accomplish in those five months?**

**Jana Francis:** Our deals start at 9 a.m. I would be at my desk job at work at that time. I would take a break at work and make sure every deal that was supposed to go off went off as planned. After that quick 5-minute break, I would work my day job until lunch, at which time I would run packages to the post office. I would also make phone calls to manufacturers and source products.

I would work until 5 p.m., and then I would go home and follow up on all of my emails. I would place one or two additional purchase orders for future deals. I would also go through my incoming shipments and verify that everything was in order. I would then have to pack orders that were sold that day and answer any customer questions that came in that day.

On the side I handled accounting and selected future manufacturers whom I would target for calls in the upcoming weeks. I also had to prepare everything for the website publishing. I would write all the copy and take photos and send them off to the webmaster.

**Sramana Mitra: Did you do all of this alone? You have not mentioned anything about customer acquisition. How did you promote the website?**

**Jana Francis:** I promoted the website in many ways. The month before we launched I took two weeks of vacation and went to a baby expo in Salt Lake City. I did not have a website yet, but I had a logo that I had made a banner out of and a PowerPoint presentation. I took my flat screen TV and set it up on a table under my banner and ran the PowerPoint presentation. I also made bookmarks asking people to bookmark us in their web browser.

I sat at that table for two days, and I told every woman who walked by my booth all about the business. I got a lot of feedback, and I could tell how excited people were. I got 160 people to sign up for my email list exactly one month before we launched. I encouraged them to tell their friends.

The night before I launched the site, I emailed my family and friends as well as everyone on that list. I encouraged them to share the website and spread the word. That is, with no exaggeration, the only thing that I have done to get the word out. Even to this day we have very little customer acquisition spending.

**Sramana Mitra: How did you find your webmaster?**

**Jana Francis:** She was the webmaster for the company that I worked for and she left on maternity leave a few years earlier and decided not to return to work. She started freelancing from home.

**Sramana Mitra: Did anyone else do this venture with you?**

**Jana Francis:** It was me and my business partner, Rett Clevenger. He is our CEO and the other owner of the company. Shortly after the baby expo, I got an email from Rett. We had never worked together, but my company had worked with his company, BackCountry.com, which was a large e-commerce site located in Utah. A few days after the baby expo I was trying to pick the back-end e-commerce solution for the shopping cart, and he emailed me out of the blue. I had narrowed it down to two options, and he sent me a recommendation for one of them. The next day we went to lunch and we walked out of that as full business partners. We launched the website on April 28th of that year.

**Sramana Mitra: How did you fund the startup?**

**Jana Francis:** I put it on my personal American Express card at first. I covered the first month of products myself. We have never taken any funding. I was able to quickly pay myself back for the products. I would say I put around $5,500 of my own money in before we started the business. I had to get the website built, the logo created, and pay for the baby expo fees. I wanted a self-sustaining business that was cool enough that people would tell other people about it because it was exciting and they were treated well.

**Sramana Mitra: You started the business with an email list that had 160 emails. How did that list evolve and grow?**

**Jana Francis:** Today we have 375,000 emails that are sent every day. We have shipped 1.7 million orders. That gives you an idea of the growth of the business. Our list grew very quickly at first.

**Sramana Mitra: If you are sending out 375,000 emails every day, how many of them are transacting on the site every day?**

**Jana Francis:** Many. The reason is that we have never bought any of our names and we do not require you to give us your email address in order to see our deals. We have a huge return rate on our database because those people chose to give us their email addresses in the first place.

**Sramana Mitra: How much revenue do you do?**

**Jana Francis:** The first year we did about $650,000 in revenue. The next year we did $2.4 million. Our third year we did $10 million and the following year we did $14.8 million. Last year we did $16.4 million.

**Sramana Mitra: What kind of margins do you work on? You obviously are getting an attractive deal from the manufacturer.**

**Jana Francis:** I have never shared that with anyone; however, our average discount to the consumer is 56% if you equal out all the deals. It has to be at least 40% off to make our site. We have usually only done less than that if it is brand new from the manufacturer. Many other deal sites buy wholesale at 40% off and are fine with a 10% margin. We are very different in that regard.

**Sramana Mitra: The question mark around the entire deals category is whether there is enough margin to build a business. You can definitely get revenues. Groupon and LivingSocial are all struggling.**

**Jana Francis:** You are exactly right. We are profitable and have not lost money. We don't have loans or investors. We have done business with 1,500 manufacturers, and we don't owe any of them a dime. We have over 70 full-time employees here in Salt Lake City. In general, deal sites are not profitable. They have focused on top-line revenue for so many years that they have lost sight of profitability. The sites you listed have left everything up to the supplier for the customer experience.

**Sramana Mitra: Groupon and LivingSocial squeeze their merchants so much that they do not return. Do yours come back?**

**Jana Francis:** I can't think of one manufacturer that we have worked with that would not want to work with us again. The reality is that we only have two steals a day on each website, so that limits the number that we can repeat with. There is a huge entertainment factor to our business, so I do not want to repeat. We try not to repeat brands. We do repeat some of the larger brands, and in some cases we have the product made specifically for us.

**Sramana Mitra: You said you have 70 people working on this project. Tell me a bit more about how you have built the team.**

**Jana Francis:** There was no pool of people that I could go hire from who had done this before. You have to find and curate an amazing product that has a story. Our buyers needed to have sales prowess and account management skills. Calling manufacturers and convincing them to give you a high volume of their product at a discount that they never would have considered selling at. They are essentially letting us compete against them for a day because they sell those products for full price on their website. It takes a skilled person to help a manufacturer understand that. Our buying team is full of talented women who are amazing at product selection and are in tune with their audience. I have found that people from media sales are great in this position. Perhaps that is because that was the career I came from and I knew the skill sets they came from.

Some of our best employees are also people who have been our top customers. I have recruited them over the past several years. Our customer service director was a fan of ours before she joined three years ago. Our vendor manager was one of our biggest local fans. She has moved up in our organization consistently since joining. All of our employees are based in Salt Lake with exception of one.

We have 18 people in merchandising. Each website has two buyers and then we have a few floaters who will buy for any of our websites. We have a lot of maternity leave here because 70% of our staff are women and 25% of them have had a baby in the past two years.

We have 12 people in our customer service team and 12 people in our shipping team. We have 8 people on our engineering team. We have one HR director and we have three people on our social media team and four people on our photography team. We have channel managers that focus on reselling inventory that we had left over. We have a few in returns, quality control and receiving.

**Sramana Mitra: You seem to have found a niche in your business as well as your workforce. You have great loyalty and employee retention with a very stable team.**

**Jana Francis:** We have been very fortunate, yes. We don't pay the best because we are a bootstrapped company. Our engineering team does well in terms of pay, and our customer service team does a bit better than an average customer service job. Most of our customer service staff is able to work from home for 30 hours a week. That is very nice for them.

**Sramana Mitra: I think what you are doing is a wonderful thing. Women who choose to have children have to raise those children. A lot of them want to continue working and have that flexibility. You have created a culture that is accommodating of that. That is a very unique talent attraction position.**

**Jana Francis:** It really is. I have two employees who brought their babies with them to work today. We use our team's babies on our website as models and we actually sign the paperwork for that. It's a lot of fun for our employees. For me it is very rewarding to know that the situation I dreamed of for myself is being provided for so many moms in Utah who would not have a job if they were not working here.

**Sramana Mitra: I think what you have done is fantastic. Our ecosystem has created a talent war for the same people. There is talent everywhere and there are different niches and lifestyles. Being able to carve out a niche like you have is fantastic HR strategy.**

**Jana Francis:** Two of our employees had a goal of working part-time only, but they applied for a job here because they were interested in what we do. Suddenly, they had full benefits, which previously were only available through their husbands. That has in turn allowed their husbands to go chase their dreams of becoming entrepreneurs because their wives now had health insurance. It is hard to afford quality health insurance when you are self-employed.

**Sramana Mitra: How do you evaluate the venture capital opportunities when they are presented to you? I am sure they pitch you on the ability to grow faster and make acquisitions. You probably also get acquisition offers. How do you process those opportunities?**

**Jana Francis:** I do respond to every inquiry. I have learned a tremendous amount talking with these people, and it has helped me understand the market better. They talk to my competition and a lot of people in the industry. I take every phone call. I also know that the time to ask for money is when you don't need it.

The relationships that I am fostering now may very well pay off in the future. I already have an idea who would be the best fit for us and what arrangements would be the best for us. The research that I have done just by taking calls and listening, as well as telling my story, has really helped me understand that venture capital is not right for our business because of what they would require in the next three to five years. Those requirements will not be met if I am not doing more than two sales a day, and I know that if I process more than two sales a day that consumers will get tired of us. I have seen that in our competition. They do 6,000 deals a day and we have 8.

I have even created a pitch deck and gone out and pitched to VC firms just because I wanted to know the process. I was very clear about that up front and they all knew I was not necessarily interested.

**Sramana Mitra: That is a great method to clarify your own thoughts and understand your options and the limitations of your business model.**

**Jana Francis:** Thank you. It really did reiterate for us that we are still excited about our business model five years in. They ask very hard questions, and when you are the owner of your company you don't have employees asking you those questions. It is really cool to get those questions. They push you a little bit.

**Sramana Mitra: If you have a $10 million to $15 million business and you make 30% to 40% profit, then you have a fantastic situation.**

**Jana Francis:** As long as I can keep it rolling. The Achilles heel of our model is what happens when you don't sell what you have invested in advance. Every day I feel like I am sitting at a roulette table in Las Vegas eight times. We put all of our eggs in one basket. If it does not go well, we can't put it up again. We have had to create other departments in the company to handle those dogs that don't do well.

**Sramana Mitra: How do you handle those situations? Do you partner with Overstock.com?**

**Jana Francis:** We partner with Overstock.com but we have not seen much success with them. Believe it or not, when we don't sell it half price we sell it for full price on Amazon. We have an Amazon store where we sell leftover inventory. It will eventually be a full-price boutique online, but for now it is an Amazon store that sells our leftover inventory. It does not work all the time, but it earns a couple of hundred thousand dollars each year. Our feedback rating there is phenomenal because they get the same support that our Steals.com customers get. The reality is that we usually have $2 million of unsold inventory at all times.

**Sramana Mitra: This has been a fantastic story. Congratulations on your success. I look forward to following your journey.**

# Interview with Amy Laws and Nicole Brewer, Founders of Smocked Auctions

*Advertising on Facebook is complicated. You can spend tons of money getting 'Likes' without making any sales. Smocked Auctions is very smart about actually 'selling' on Facebook. Much to learn from these mompreneurs who have bootstrapped to almost $5 million in revenue!*

**Sramana: Amy and Nicole, I would like to start by talking a bit about your personal journeys. Where are you from? What circumstances were you raised under?**

**Amy Laws:** I was raised in a small town in Mississippi. My father was a physician in the town of 10,000 people. My parents always stressed the importance of education. They always told me that my education would be the one thing that nobody could ever take away from me. I think that was very important to me while growing up.

My mother passed away from cancer when I was 16. I have one older sister. I would say that we had a very traditional upbringing. I went to the University of Mississippi. After a brief stop in Nashville, I moved to Dallas in 2002. I worked as the head of sales and marketing for an IT consulting firm, which was wonderful. I had an amazing mentor there who had her own small business that she had started. I learned a tremendous amount from her about what it takes to work in a small business and build it from the ground up.

I met Nicole in Dallas in 2008 after the birth of our first boys. We met at a stroller fitness class because we were both trying to get back in shape after having our first children. We struck up a friendship.

**Nicole Brewer:** I am originally from Dallas. I have a very close family. I have a sister who is eight years younger than I am. I went to SMU for College. My father was an attorney and my mother was a reading specialist although my mother quit working after my sister was born. Both of my parents are go-getters. They are very hard working and very family oriented.

After college I worked for a non-profit here in Dallas. I worked with their corporate sales clients. After I got married, I started working for a women's clothing company that did trunk shows in homes. After that, in January of 2008, my son Charles was born. In July of 2008, Amy and I met. We both had little boys who were three months apart and we became great friends. We were friends for about two years before we started the business. In between that time, we both had little girls.

When people ask me when I had the moment that changed my life, I tell them that it was when I had my son because I learned that I could love someone more than I ever thought was possible. It was also the reason that I met Amy. Our friendship has changed both of our lives.

**Sramana: At what point in the friendship did the idea of doing a business together start coming into the foreground?**

**Amy Laws:** That was in the summer of 2010. We had attended a sample sale. The wholesale showrooms in places like Dallas, New York, and Atlanta purchase sample sets from their manufacturers. That is what they use to show potential clients who are going to come in and shop for their stores. They routinely try to sell the samples once the season is over. They will sell the samples on consignment to folks who will then turn around and sell the samples to anyone.

We attended one of these sample sales for children's smocks and outdoor play clothing and we absolutely loved it. We thought the idea of shopping that way was brilliant. The clothes were our children's sizes and the prices were great. It was a great way to shop. We had little girls and we wanted to dress them a certain way but it was very expensive to do so. It was not in our budget to dress our children that way on a non-special occasion basis.

After attending the sample sale, we thought we could also have a sample sale. Our kids were the perfect age and we had a ton of friends we could invite. We would also get first pick of the samples for our daughters. We thought we could host a sale, get some great clothes, and provide a great service to our friends. We had our first sample sale in August of 2010.

**Sramana: What was the process of procuring the samples?**

**Amy Laws:** We went down to the Dallas Market Center and met with each of the individual show rooms. We talked to them about what we wanted to do. I brought my mother-in-law to one of the first meetings, because I thought she would lend some credibility since they did not know us and we were just going in there to ask for their samples.

We discussed where the sale would be held, which was at Nicole's house in Dallas. It was at the end of the season so they had already tried to sell some things. They basically felt that if we were able to sell the samples it would be fantastic. We did have to meet with them and build some trust and then they let us have the samples.

We turned around and made a small commission off of those sales. When we turned in our sales receipts, they were very impressed. We had put everything into a spreadsheet and were very organized with our process. They had been doing that for 15 years and nobody had shown up with that level of detail, which I credit Nicole with. We built trust with them very quickly and they expressed interest in continuing to work with us.

**Sramana: What volume of merchandise were you able to push during that first sale?**

**Nicole Brewer:** We sold 700 units during our first sample sale. That amounted to around $20,000 of business. Once that sale was over we realized we had a lot of fun and we wanted to do it again, but without having everyone over at my home.

We still had some clothes left over after the first sample sale. Some of our friends who did not live in Dallas were not able to attend the first sample sale. We started taking pictures of the clothes and emailed them out to people. We then started posting them on our personal Facebook pages. One of our friends had boy girl twins and we found several outfits that were matching, so we posted those on our Facebook page.

Within hours of doing this, we had people we did not know started asking us to be friends on Facebook. We were nervous about accepting friend requests from people we did not know personally so that is when we started a company page. About 2 weeks later, we had our first sale on Facebook. We only had one size of each item and we did not have any multiples.

During our first auction, we sold 30 items. We posted 1 item a minute. From our first auction, we had 300 fans on our Facebook page. After that, we grew organically. We did not do any advertising on Facebook our first year, we just built our business from word of mouth. They would talk about us at the park with their friends.

**Sramana: Were you completing the transactions on Facebook, or were you displaying on Facebook and sending people to a separate auction site?**

**Amy Laws:** From an auction standpoint, what is interesting about what we do is that it is a cross between an eBay and a Craigslist. The price does not increase during the auction. You are not outbidding other customers. The reason for the auction is that we have limited quantities. The first person to comment for that size gets to buy that item. It's like Craigslist in that regard, if you get there first, then it is yours.

One of the things people liked about what we were doing was that the price point was great and the garment quality was fantastic. We were selling clothes from the best manufacturers in the business. After we would use Facebook as a picture posting mechanism, we would manually invoice them from PayPal. It was a completely manual process.

**Sramana: At what point did you switch out of that manual process to something more automated?**

**Amy Laws:** We moved the business out of my house in August of 2011 and moved into a real office.

**Nicole Brewer:** It took us another year to move to an automated buying process. We shifted that over in August 2012.

**Sramana: How much volume and revenue were you able to generate in the early days when you had the manual invoicing process and were working out of your homes?**

**Nicole Brewer:** We did a million dollars our first full year of business.

**Sramana: Was that all consignment?**

**Nicole Brewer:** After about three weeks of our auctions, we sold out of the samples that we had. We went back and purchased the overstock from those locations. About 6 weeks after that, we ended up private labeling our own items, and designing our own items because there was no more overstock to buy.

**Sramana: How much overstock inventory did you have to buy in dollar terms?**

**Amy Laws:** We probably bought $30,000 of inventory.

**Sramana: What kind of markups were you getting on that $30,000 overstock inventory?**

**Amy Laws:** We were probably selling those at a 100% markup.

**Sramana: That's about what I would expect. I actually ran a fashion company on the Internet in the early days, in 1999. So you turned $30,000 into $60,000 and then decided to manufacture your own. Tell us a bit more about that and your design process. Do you have design skillset in your shop or did you get somebody to do that for you? How did you handle manufacturing?**

**Nicole Brewer:** We had to find great people to help us. Amy and I do not have any technical design background, but we knew what we liked. We had children in this age range, and we knew what we wanted for them. We had sketches of what we wanted, and we found great manufacturing partnerships to get them made.

**Sramana: Did you find those partnerships in the US or overseas?**

**Amy Laws:** Both. We did quite a bit locally in Dallas. About 50% of what we sell is made overseas and the other 50% is made domestic.

**Sramana: Are you completely private label at this point?**

**Amy Laws:** I would say that 95% of our clothing is private label. We buy some clothing wholesale. There are some brands that we like and that our customers liked and which do a very good job. We buy pieces from these brands that we like if we can get them at great price points. We have more flexibility in garments that we design because we control the costs.

When we buy wholesale, we stick to the wholesaler's rules. We mark those up 50% as per their directions. One of the things that is key is that there are two ladies here who are mothers. We don't have formal design training but we have strong points of view when it comes to what we like to see our daughters in. We know what our friends like.

Our personal style seemed to resonate with our customers. We could not find what we liked in the showrooms. We did not like being constrained by what the manufacturers would present. They only offered the summer collections and the winter collections. Our customers expected fresh, new goods at each and every auction. We started off having two auctions per week and there was no way to get that variety buying wholesale. By bringing in our own label, we were able to control that ourselves. We could control the fabric and the volume of merchandise that we could get.

Very early on, we told ourselves that if we could not afford to buy it we would not do it. We operated and still operate debt free.

**Sramana: In this business building process, how have you prioritized? If you are doing little girls' or little boys' clothing, there is a pretty sizeable range of age groups. Where did you prioritize your sweet spot and where did you expand from there?**

**Amy Laws:** The buying patterns of our customers dictated that. The girls' moms far surpassed the boys' moms in terms of volume of buying. Our best selling sizes are our 12 month to 3T. That is because moms are still in control of what they dress their kids in. Once the kids get older, they start to have their own opinion.

We get emails from moms who are frustrated because their daughters refused to wear something on a particular day. Some little girls just want to wear princess clothes everywhere they go.

We only go up to a size 6 for that reason. Once you get above a size 6, size ranges get more varied. You have more continuity of size in the younger ages.

**Sramana: What percentage of the business is girls clothing versus boys clothing?**

**Nicole Brewer:** About 70% to 30%. Girl moms definitely shop more than the boy moms. You can do a lot more with a girl.

**Sramana: When you decided to move to a more automated payment process, how did you manage that decision process?**

**Nicole Brewer:** When we moved into our space, we knew our business was real. At that point we started to hire people to help us. We wrote down everything we needed from a technical sense and we found a contractor to build the stuff for us. At the time there was nothing on the market that would serve our purposes. We spent a year developing the technology.

**Sramana: None of the shopping carts on the market would fulfill what you were looking for?**

**Nicole Brewer:** No, because we needed an upside down shopping cart.

**Amy Laws:** Shopping carts are designed for a customer to put items into it. You get on the website and choose those items. When you were shopping with us you did not know that you won an item. We may only have 40 of one particular dress and have 150 people competing for that dress. We had to design an invoicing system that had a reverse engineered shopping cart. It really had to be an invoicing system.

The software we built is completely proprietary. We did not utilize any off the shelf components because of the uniqueness of what we are doing. We built an inventory system specialized to our requirements. We had an accounting system and a rewards system built in.

**Nicole Brewer:** We also had dynamite fulfillment. That was very important to us. One thing that has separated us from others is that our shipping is very fast. You pay and we ship the next day.

**Amy Laws:** Definitely. Fulfillment and fantastic customer support are our trademarks. We outgrew that software and it was not scalable for what our goals were. We have recently started using different systems.

**Sramana: Now you have done another round of change in the technology infrastructure. What have you done in this round?**

**Nicole Brewer:** This round focused on scalability. We want the ability to add other lines of business in addition to Smocked Auctions. We just built a much larger, robust engine.

**Sramana: Are you still doing custom software development?**

**Nicole Brewer:** We have used off the shelf pieces to build a customized environment for us. It was very important for us to continue selling on Facebook and Instagram. We had never sold on a website before. We just launched that this February. Before that, the only thing you could do on our website was pay your bill. We really wanted to expand our website into something that would allow customers to have a single experience. They can now shop there and take advantage of our rewards program.

**Sramana: So now in addition to your auctions, you are also offering traditional e-commerce on your website?**

**Nicole Brewer:** Yes. We still have our auctions as well.

**Sramana: What infrastructure do you use to complete your auctions? Is that still custom software?**

**Nicole Brewer:** We have a partner that we are using. We post a picture along with a price and quantity. As soon as a customer sees an item that they want, they just post in the comment that they want the item. They provide us with the size and email address. Within minutes, they have an invoice sitting in their email.

They click on that email, open it, and pay for the item. We ship the item out the next morning, or send the item to be monogrammed after which it is shipped out.

**Sramana: What happens if a customer does not pay within a certain amount of time?**

**Nicole Brewer:** We have something called second choice invoices. If an item sells out and you were not on the initial winning list, and one of the initial winners decides not to pay their invoice, then the item will be offered to you. It will be available for 48 hours. In that case, we pre-authorize the credit card.

**Sramana: It sounds like there is some complexity in the algorithm needed to manage that process.**

**Amy Laws:** I think what was interesting about how we started and what we were doing is that it was a very unique approach. We had to pave our own way. That's why we built custom software initially. We made some errors but we made some great decisions along the way. That has been a lot of fun.

**Sramana: What is an example of a major goof up?**

**Nicole Brewer:** When we initially decided to do private label, we initially were working with just one factory. We quickly realized that took away negotiating power. If there were any floods, labor strikes, or anything like that our business was in one person's hands. We have since diversified the countries and towns we are in. That has given us greater negotiating power.

**Sramana: How have you used Facebook as an advertising channel?**

**Amy Laws:** Facebook has been our primary advertising avenue. We did not advertise for the first year. We did not know what we were doing. Our first

10,000 fans were completely organic. Once we hired someone to do some marketing strategy and consulting, we finally got into a groove with Facebook. We have since started using Google AdWords.

Word of mouth is still extremely powerful. Running a business on social media forces you to take care of your customers in a way that retail has never had to do.

**Sramana: On the surface Facebook advertising does not seem all that complicated. A lot of people also experience that fans don't turn into leads. You are getting leads and transactions out of Facebook. What have you learned that is worth sharing?**

**Amy Laws:** Once that fan likes your page, you have to put your best foot forward every single day. We can tell very quickly if the new fans are helping us grow or not. Being on social media and understanding the importance of the 'Like' has forced us to have the best service possible. A 'like' on our page is not just a number. A 'like' that does not equal a sale for us means nothing.

I think if we had completely figured out Facebook, that would be amazing and we would be shouting from the rooftops. I know that a lot of businesses advertise in a lot of different places. This is our only advertising expense. Keeping it fresh and trying different things is very important. The market of companies actually doing transactional business on Facebook is a small fraction of what people use Facebook for. If they are trying to get people to physically visit a store, it is a lot different from getting people to visit our page. Our call to action is still based in social media and we bring them what we are selling.

**Sramana: You are actually making people comment on your Facebook page. That is the indication from the customer to you that the customer wants to transact. They are putting down their email addresses, right?**

**Nicole Brewer:** Yes, they write the email address and the size that they want.

**Sramana: I imagine for every auction, you are getting a large stream of comments. The algorithm Facebook has relies on the number of likes and comments. That gets Facebook to show your picture more. That is not necessarily the case with other businesses. You have created a structure where you are leveraging Facebook to show your product more.**

**Amy Laws:** Facebook does perceive our page as being interesting because customers have to interact with our page to get what they want. That is inherent in our business model.

**Sramana: That is very smart. Is anyone else doing that?**

**Nicole Brewer:** Yes, we have competitors. There are other people who do comment-selling. When we started, there were very few. Interestingly enough, children's clothing was one of the first industries that started selling this way. It is a very visual purchase. Jewelry is another interesting model. There are things that are not going to be successful being sold this way. We have a great price point and we make it easy for people to buy from us.

**Sramana: You two started working from your home. How did the team evolve?**

**Amy Laws:** We have always looked for good people who compliment our skills. We have 10 people working with us today. They work in customer service and fulfillment. We also have someone who helps with photography and someone who runs the auctions. Everything else is contracted.

**Sramana: How did you choose your partner for software development?**

**Amy Laws:** Our most recent contractor has been here in the United States. Working with American developers, we have found a much more interactive feedback process. When we worked offshore, everything was delivered very literally.

**Sramana: Are there any lessons learned that you would like to pass on to other entrepreneurs?**

**Amy Laws:** Social media is extremely public, but it is the only business method we know. We operate completely open to all of our fans. We have never deleted a negative comment. Everyone sees how we work through our customer engagements. If someone is not happy, they will let 400,000 people on our page know it. Anyone who wants to do business on social media needs to be hyper sensitive to social media.

**Sramana: Congratulations. Good luck as you continue to build your business. It's a fascinating story.**

# Interview with Amber Schaub, CEO, Rufflebutts

*RuffleButts is a perfect story on how to bootstrap with a paycheck. Amber Schaub started RuffleButts, a children's apparel company, in March of 2007, backed by her husband's full-time job. He later joined in 2010 as the COO after the company had gained traction.*

*This is also a very good case study of how Amber built a brand around a new product line that she wanted to bring to market.*

**Sramana Mitra: Let's start at the very beginning of each of your stories. I imagine you co-founded the company?**

**Amber Schaub:** I grew up in Louisville, Kentucky. I had the entrepreneurial spirit from a very young age. I used to convince my cousins to help me start lemonade stands, baby sitting clubs, and we even tried to start a grocery delivery business in middle school. My dad is an entrepreneur. My parents were divorced so I watched what my mother had to do as a single mother. She worked a 9 to 5 job for a utility company and had to raise a child on that income. We did not live a lavish lifestyle, but I always had what I needed.

I knew that if I wanted to go to college, I was going to have to pay for that on my own. When I graduated from college I was very enticed by the money to take a job in pharmaceutical sales. I was not passionate about what I was doing but the company car and paycheck was good. That did not last all that long because I got enticed into real estate during the boom years, but once again I was not fulfilled. I was shocked by the lack of ethics in the business world. I made a decision very early on that I was going to run a business based on the golden rule. Ethics are extremely important to me and I attribute that to my mother.

**Sramana Mitra: When was RuffleButts founded?**

**Amber Schaub:** I founded it in March of 2007, which means I conceived the idea and got the trademark. I started down the path of teaching myself how to run a children's apparel company. I had no experience in retail, designing, or selling. I had no children of my own, so children's apparel was not something that I would have considered myself an expert at.

**Sramana Mitra: So why did you decide to launch a company in children's apparel? I hear stories about this from moms who are passionate about their kids and that is what led them to start the business.**

**Amber Schaub:** I get that a lot. I was passionate about children although I did not have any at the time. I was passionate about the business side and about creating a product that I could be proud of. I knew I wanted to start a business and it took me three months to figure out what business that was going to be. Mark was supportive of my quitting my job to start a company. I did a lot of research to decide what business to start. At that time, there were a lot of glossy stories about entrepreneurs who followed their dreams to start 10 million dollar businesses.

We had a longer road to parenthood than we wanted at the time. RuffleButts became my baby. The idea came because I wore ruffled bloomers when I was a baby and my mom always called them my rufflebutts. I went into a store looking for them when I was shopping for a gift for a friend. I asked the lady if they had them and she told me they did not, but she did not know why they did not carry them because people came in looking for them all the time. That is what spurred me to get into this specific industry.

I thought everyone called them rufflebutts and fortunately found out that nobody else knew about that name. The trademark and the domain name were both open. That is how the name of the company was born.

**Sramana Mitra: You had the intuition to react to something that a retail salesperson was giving you. What did you do next? How did you go about setting up your business?**

**Amber Schaub:** My first step was to go back to Mark and share my idea. I also had to get the trademark, which cost $400. I remember telling Mark that $400 was a lot of money to spend. Mark told me that I either had to go for it or do nothing, so I just went for it.

After that, I went full steam ahead. I started doing research and read anything I could get my hands on about how to design, how to get samples, and everything else you need to do in the retail space. I called everyone I knew who had knowledge of sample making and I took a sewing class. I had to be able to talk to the person who would make the product to describe the fabric and seams that I wanted to use.

**Sramana Mitra: What about the website and transaction capabilities? When did you have a site online?**

**Amber Schaub:** I immediately went down the path of development and production. That was ambitious, considering that I had no sales. I knew that I had to produce the product so that people could see it and purchase it with immediate shipment. I hired a small web development company and they designed a basic e-commerce site for me. At that point, I showed everything to

Mark and he helped me take the website to the next level. We launched that website in August 2007.

I also attended a trade show, which is a common way to sell clothing in the children's apparel industry. I rented out a booth and asked my mom to fly out from Kentucky and help me, since I had no employees. We did our first trade show so that we could get feedback, and also to try to sell our RuffleButts wholesale.

**Sramana Mitra: Where were you living?**

**Amber Schaub:** I was living in South Florida when I started the business, but the trade show that we attended was in Las Vegas.

**Sramana Mitra: In terms of the product itself, what strategy did you follow? How did you get the product built?**

**Amber Schaub:** In 2007, information was not as readily available as it is today. When I went out looking for production partners, I could not just do a quick Google search to find partners to produce children's apparel. Today you could probably do that, but I could not do that in 2007.

I just looked for any factory contact I could find. I was fearful of producing overseas and my quantity was very low, so most overseas factories would anyway not produce at our quantity level. I ended up finding a gentleman who lived in South Florida who owned a factory in the Dominican Republic. He agreed to produce the entire first line for me.

**Sramana Mitra: How many units were in your first line and who did the designs?**

**Amber Schaub:** I did 100% of the design and still do today. I don't have a design background, so I had to figure out how to make that work. I designed from a common sense perspective. I just put myself in the shoes of a mother who will be purchasing and I ask myself what will be important. It has to be soft, it has to hold up in the wash, and it has to have quality. I cannot produce bargain apparel, but I still wanted it to be available and affordable to the masses.

**Sramana Mitra: You said you designed the clothing yourself even though you did not have a background in design. Can you explain that process to us?**

**Amber Schaub:** I would draw things up and take my designs to a pattern maker. She would take my designs and convert them into a paper pattern. I sent those paper patterns to the factory, and they cut the fabric based on that pattern.

**Sramana Mitra: How many different design variations did you have in your first line?**

**Amber Schaub:** The first line had a RuffleButt Bloomer, a RuffleButt Crawler which is a pants version of our Bloomer, T-shirts to coordinate with the RuffleButt Crawler and tops to match the RuffleButt Bloomers.

**Sramana Mitra: How much did you have to spend to get that line developed?**

**Amber Schaub:** Mark and I invested $40,000 to start the business. We decided we would put it all in and use that money to get the website up and going as well as place our first order. We had no outside investors.

**Sramana Mitra: How much inventory did that get you?**

**Amber Schaub:** At that time, we ordered about a dozen pieces of each item, per size, per color.

**Sramana Mitra: It sounds like you had a pretty sizable inventory.**

**Amber Schaub:** In the beginning when I started the business, I realized that in order to attract customers to my website I needed a full collection. I could not offer a bloomer in two colors and pretend that it was sufficient. I decided to go all the way and produce a full collection from the beginning.

**Sramana Mitra: Mark, you kept your job during this time frame. It sounds like you were bootstrapping with a paycheck.**
**Interestingly enough, there are a lot of businesses founded by couples where one of the two keeps a job while the other develops the business.**

**Mark Schaub:** It fit together like a perfect puzzle. I was in real estate development flipping homes, and then for the months in between homes sales, Amber would have the steady paycheck. It was a change of pace and role reversal for me to keep the steady job so that Amber could do the startup.

**Sramana Mitra: What about customer acquisition? How did the first customers come to your site?**

**Amber Schaub:** Looking back, it is still amazing to me. I had no marketing budget and I did not get to advertise. I just organically got the word out, which is amazing. We launched the website in August and the first shipment arrived in December. Everything I sold from August to December was a pre-sale item.

**Sramana Mitra: Was that wholesale?**

**Amber Schaub:** It was both retail and wholesale. We had the website, which appealed to retail but I was also selling wholesale. I spent a lot of time on the phone with stores trying to introduce them to this line. I was trying to convince them to order the product for their stores for a January shipment. I really focused on building the brand. I wanted to use the brand to drive traffic to the company.

I was very fortunate to receive a call from a stylist in LA with Celebrity Babies. I had called her in December to let her know about my company. She called and asked me to fly out to California the following week to do an event with a bunch of celebrities and their babies for the Golden Globe.

**Sramana Mitra: How did you handle such a big event so early on? I imagine it was quite an ordeal to get ready for celebrity exposure.**

**Amber Schaub:** I only needed 300 pieces to be able to do the event, so I had the factory send the completed work out to the hotel in LA. I was crossing my fingers that everything would be OK, and of course when I got there that was not the case. When I arrived and started going through the bloomers, I saw that half of them were made perfectly and the other half was a mess. I went through and found the best of the best so that the celebrities could represent our brand well.

We pulled that off and we made an impression on some of the celebrities. Ali Landry took her daughter to the beach in Malibu wearing our RuffleButt Bloomer. The pictures were on TMZ. She was just one of many who were very supportive of what we were doing. That catapulted our brand from the very beginning.

**Sramana Mitra: Did that create buzz around the brand and draw traffic in?**

**Amber Schaub:** Yes. I would also work with any publicist that would pay attention to me. I would email them my story and beg them to cover it. We were fortunate to get into Baby Talk Magazine as an editor's pick with a picture of a baby wearing our RuffleButts Bloomer. Back then, Mark and I would celebrate getting a couple of hundred orders. Today that is a slow day. With all the celebrity and press, the stores started to come to us.

**Sramana Mitra: The e-commerce business you were developing was basically a shell business. It sounds like the retailers were the ones ordering products.**

**Amber Schaub:** We had folks like Nordstrom's and Target call us. Mom and pop boutiques all over the country were applying to carry our products because customers were asking for our products. In the beginning, 95% of the stores we sold to came to us, which was incredible.

On the retail side, the publicity also drove consumers to us. They were very supportive of my story. They would promote us on their Facebook pages. They have always been very supportive of us.

**Sramana Mitra: There is a built-in viral aspect to your product. Moms like to take pictures of their babies.**

**Amber Schaub:** Exactly. We are so lucky that we have a product that is all about happy moments and childhood. When I started the business, I thought that moms and grandmothers would be fun customers. I wanted to have a product that would make people happy. You take your child out in RuffleButts and you will get compliments from everyone. We are very fortunate to have that organic aspect.

**Sramana Mitra: You started in August of 2007. How did your business ramp during your first year?**

**Amber Schaub:** When we received the first shipment, I faced the harsh reality of what entrepreneurship really is. When that first shipment arrived, half of the apparel was unsuitable to sell. Production was very bad. I debated whether or not I wanted to share that publicly because I did not want people to think bad about our brand. However, I wanted other entrepreneurs to see the reality of what starting a business is all about.

I had to fly my mother to Florida so that we could measure each garment. I was not about to sell products that did not meet my quality standards. I questioned if I was really ready to do this. We did not start selling until January of 2008. That first year, we sold about $100,000 of products.

**Sramana Mitra: Did you gain traction with the brick and mortar retail stores?**

**Amber Schaub:** We did get some good success early on. Nordstrom contacted us in late 2008.

**Sramana Mitra: How big was your first Nordstrom order?**

**Amber Schaub:** They did a 5 store trial order, which at the time, seemed huge to us since no stores had put us in. They ended up putting us in 50 stores and I thought that order was just incredible. Today that is pretty standard.

**Sramana Mitra: You said you put in $40,000. How long did it take you to break even?**

**Mark Schaub:** We operated in the red for about half of the year.

**Sramana Mitra: What was your revenue number in 2009? How did the business ramp.**

**Mark Schaub:** In 2009, we did $375,000 gross. In 2010, we did $1.1 million gross. In 2011, we did $2.5 million gross and in 2012, we did $3.7 million. We finished just under $5 million gross last year.

**Sramana Mitra: What were the key milestones in 2009 and 2010?**

**Amber Schaub:** On a personal level, we had our first child at the end of 2008. I had a big learning experience in 2009 where I had to learn how to be fully devoted to the company as well as my child.

In 2010, we hit the point where we needed help. Mark sacrificed his career to join RuffleButts to maximize the opportunity we had in front of us. By that point, I had a customer service representative and I had also hired an assistant. When Mark came on board, we did a big website upgrade and we moved into the wholesale arena.

**Sramana Mitra: How did you manage a full year with a newborn while operating the company before hiring that help?**

**Amber Schaub:** I hired a part-time assistant who worked half-time during the week. Looking back, I have no idea how I did it. You face what you have to face and you do it. After 5 months, I put her in daycare. My mother lived in a different state.

**Sramana Mitra: What was your team growth like?**

**Amber Schaub:** Our team grew quickly. In 2010, we hired someone to pass the orders and pull the orders. We hired someone to cover customer service.

**Sramana Mitra: Were you still operating out of your home?**

**Amber Schaub:** We were. We had converted our basement into the RuffleButts headquarter and we had fantastic team members who were willing to come to our home to work on a daily basis. My son was born in April of 2011. In May of 2011, we moved into our first office warehouse.

**Sramana Mitra: How have you expanded your team from 2010 onward? What has your recruitment philosophy been? What positions have you hired for and how have those people helped you scale the business?**

**Amber Schaub:** Throughout the process, we have hired on a need basis. We are a family business and we did as much as we could before we hired anyone else. We would almost be bursting at the seams before we brought on another team member. I suppose that is an entrepreneurial manner of working because the budgets in a bootstrapped startup impose that reality. Today we have 18 employees, including Mark and I.

**Sramana Mitra: How are the roles of your 18 team-members divided?**

**Amber Schaub:** Mark runs the operations and financial side of the business. I run the big picture, design, marketing, PR, and sales side of the business. Operations take up 60% of the employee base. We have people who pack and warehouse. They manage fulfillment. The other half of our team is sales, marketing, production, and customer service.

**Sramana Mitra: I understand the pick, pack, and ship side of your business, that clearly makes sense. What is the sales angle for your team members? Are they focusing on wholesale deals with stores?**

**Amber Schaub:** Yes. Our sales team has grown over the years. In the beginning, most of the stores came to us. Stores filled out applications and I would then sign the stores up online. We are a lot different than other companies in that we are e-Commerce driven. Traditional wholesale apparel companies are used to trade shows and faxed orders. We had our customers placing orders on our website from day one.

Our sales team is responsible for approving any applications from customers that may come in. They introduce our line to other stores where we may be a good fit. I would estimate that 80% of their time is spent helping existing customers and 20% of their time is spent attracting new stores.

**Sramana Mitra: How many of these sales people do you have?**

**Amber Schaub:** Three.

**Sramana Mitra: What percentage of your business is wholesale?**

**Mark Schaub:** We are about 60% wholesale.

**Sramana Mitra: What do you do in marketing?**

**Amber Schaub:** We do Google AdWords. We do some print marketing. Our marketing is somewhat traditional e-Commerce marketing. We have a Facebook page and manage our own social media.

I handle the majority of our marketing, print and social media. We have another person who manages the AdWords and online advertising. Mark manages that side of the house as well.

**Sramana Mitra: Do you still do all of the design work yourself?**

**Amber Schaub:** Yes. Hopefully not for too much longer! That is the driving force of our business, so I have maintained control over that aspect.

**Sramana Mitra: Are you still working with the same factory in the Dominican Republic?**

**Amber Schaub:** No. After all the mistakes that we had to deal with in the first order, we had to make a change. We worked with them for a short period of time. Over the years, we have developed relationships with manufacturers. Our product line has expanded significantly and we have different manufacturers in different locales.

That being said, our bows are still hand-made by the same lady who started making them on day one. They are hand-made here in the US. Our apparel products are made primarily overseas.

**Sramana Mitra: Have you taken external financing?**

**Amber Schaub:** No.

**Sramana Mitra: What happened at *Shark Tank*?**

**Amber Schaub:** We participated last October. We had an offer for 9% of the business for $600,000. That was a handshake deal on the show. We were in the *Shark Tank* for 2 hours and they only aired 10 minutes of it. We entered the due diligence phase and we are still in that phase. I doubt that the deal will happen.

**Sramana Mitra: What about *Shark Tank* interested you?**

**Amber Schaub:** We were big fans of the show. I think a show that inspires entrepreneurs is a win. We put a lot of thought into our decision to participate in the show. We felt the ability to showcase the brand was a once-in-a-lifetime opportunity, as well as a chance to get a strategic partner. We are at the point in our business where we could bring on some major retailers to take us to the next level. We saw the show as a very good opportunity.

**Sramana Mitra: A lot of entrepreneurs are building businesses as a couple, especially when it comes to capital-efficient businesses. What have you learned as a couple about starting a company together?**

**Amber Schaub:** We use the analogy of the show *Survivor* a lot. We have watched time and time again that those who win are those who build an incredible alliance. Our partnership is an alliance. There is nobody I trust more than Mark. Trust goes a long way in this business.

The one lesson we learned early on is that we need two separate offices. Mark needs to run his area of the business and I don't get involved in the day-to-day operations there. We have strategic goals that are aligned, but each of us runs our own aspects of the business. We are fortunate that our talents align with our job responsibilities.

We do find that we sometimes fall into the pitfall of business talk during family dinners or vacations. We have had to learn how to draw the line when we can. My honest answer is that we have a hard time drawing that line, but we are both passionate about what we do. At some point in the evening, we have to stop talking business.

**Sramana Mitra: I love these kinds of stories. Thank you for taking the time to share your story and inspire our entrepreneurs.**

## Zero-Logistics eCommerce Businesses Kick Ass

A key factor for the success of an e-commerce business is the management of inventory and logistics. Especially for bootstrapping companies, this could be a major challenge. One way to work around this challenge is be a zero-logistics company. Shoplet, eComfort, and CarPartKings have all successfully applied this method in their businesses and they surely kick ass!

Shoplet is an online retailer selling discounted office supplies. They cover 16 major categories including furniture, cleaning and break room supplies, green products, and security and safety. Their products cut across categories and feature many unconventional products that small and medium sized businesses need.

Tony Ellison, CEO of Shoplet started the business in 1994 with 1,000 of the most popular items in CD-ROMs. The Internet was in its infancy at that time, so Tony invested his own money and built a basic site with shopping cart capabilities. But instead of buying the inventory, he got them drop shipped. This took away the need for a warehousing operation and the related overheads. It also enabled him to bootstrap and provide the products at greater discounts.

At that time, there was no Google PPC but a Macworld magazine reviewed their business in 1995. Overnight, their site gained enough visibility and their business idea was validated. They were advertising a CD-ROM product called Encarta Encyclopedia for $24 while retail stores were selling it for $69 dollars. That year, they averaged 100 orders a day as the idea of buying online at discounted prices caught on. In the first year of their operations, their revenue crossed the $100,000 level. He had two other part-time employees and they became full-time employees by the end of the year.

The business also scaled from 1,000 items to 120,000 items in 1996 and they added more people and even had an office. Adding more people took a toll on their margins and they decided to focus on B2B customers and offer an e-procurement platform. They turned profitable in 1997 and have been cashflow positive since then.

Shoplet has close to 75 people now and has expanded to the UK and Canada in 2013. They stuck to a bare essentials model using the infrastructure and services of distributors and trading partners for shipping the products. They were able to connect to the back end of their databases, provide inventory to their users and handle all the marketing, SEO, and SCM. Partnerships with distributors and trading partners enabled Tony to bootstrap the company and expand to great heights.

The e-commerce industry has evolved now and the drop ship model has brought in several smaller players. That is why Michael Dash, CEO of CarPartsKing wanted to start an e-commerce company which was not that easy to get into and would have a high barrier to entry. He chose auto parts and started the company in 2011. Since he did not want to carry any inventory, he talked to a number of distributors or drop shippers who would lend him the data, let him process it, and then fulfill orders.

These distributors have large warehouses that stock autopart inventories, which are set up as shipment and fulfillment warehouses. Every order received at CarPartKings is electronically transmitted to them. They pick that part and ship it to the customer and charge CarPartKings for that service.

In 2012, they started out selling in the easiest way possible, which was by selling through marketplaces like eBay, Amazon, Sears, and others. In 2013, their revenue was $6 million with 14 people.

Michael says there are hundreds, if not thousands of drop shippers to choose from, which has allowed them to expand. They now sell plumbing parts, electrical supply parts, and plan to expand further to other verticals. However, he is selective with distributors and believes in having one distributor for covering 99% of a category. The logic behind this is that if you spend a million dollars a month with one distributor, then you can negotiate the prices better.

Again, Michael is particular about the category he chooses as well. "I go after businesses that have been around a long time. They have had a hard time going online, perhaps because they are older businesses. People just have not taken the time to bring these businesses online."

CEO Pavel Sokolovsky of eComfort.com also used the zero-logistics strategy to bootstrap to $13 million in four years with an e-commerce business in the niche area of heating and cooling. Pavel and his co-founder Victor leveraged their relationships with distributors that they knew from their previous work. Initially, convincing the distributors that they could pay their bills was a challenge but over time, it became less so. They sold inventory that was made available to them. They focused on keeping the inventory to a bare minimum so that it made sense financially.

With the advances in logistics, it is much less expensive and easier to move products across the country. Pavel says their value proposition lies in finding players in the supply chain who have operating efficiency and deliver value, thereby providing a smooth experience for the user.

The zero-logistics model is fantastic for bootstrapping e-commerce businesses. You can partner with distributors and use their infrastructure and services without having to carry the additional burden of handling delivery. However, it works best when you target a niche area where you can differentiate yourself, especially where there is limited competition. You are able to create good relationships with distributors and drop shippers.

Finally, the model requires that you trade off some margin to keep your operations simple.

# Interview with Tony Ellison, CEO, Shoplet

*The Shoplet case study is interesting because it illustrates how an entrepreneur has bootstrapped a category leading e-commerce venture in office supplies by trading off margins in favor of minimizing logistical challenges. Tony outsources all the physical aspects of his e-commerce business while running a 100% virtual shop. Blinds.com and FineArtAmerica.com have also followed the same model to build category-leading businesses.*

**Sramana Mitra: Tony, let's start with the beginning of your story. Where were you born and raised? What is the backstory of the Shoplet story?**

**Tony Ellison:** I was born and raised in Israel. I came over to the US to study and I stayed here. The Shoplet story began as an accident out of my research. I have seven years of experience on Wall Street and I realized from my time there that more and more companies were migrating to e-commerce. I also realized that the Internet offered a level playing field for small and medium sized businesses, allowing them to compete with big businesses. That is where my journey began.

In 1994, I looked at different industries and wound up in the office product industry because of the sheer size of the market and the fact that it was a commodity-driven industry. There has not been a substantial change in it over the past 100 years and it was ready for a transition to an online platform.

**Sramana Mitra: How did you get an e-commerce business off the ground in 1994?**

**Tony Ellison:** In the early days, I experienced a lot of trial and error. The industry itself is not very well defined. There is overlap between traditional office supplies, imaging and printing, and break room supplies.

In the very beginning, I was focused on building a proof of concept. I wanted to know if I could take the top 1,000 items used in the industry and sell them online. In 1994, there was not much available in terms of infrastructure. The Internet was very much in its infancy. I had to invest my own money and build a very basic site that included shopping cart capabilities. We only offered 1,000 items.

Macworld reviewed us in one of their magazines in 1995. The next day our site crashed and our answering machine had over 200 messages because we were advertising a CD-ROM product called Encarta Encyclopedia for $24 which included almost 100% margin. Retail stores were selling it for $69 dollars. I realized at that point that our business model could offer customers enormous savings.

That first experiment was very successful. I knew that we were on to something big. That was the moment that I really focused on scaling this business idea into the company that it has become today.

**Sramana Mitra: You decided to go to market with 1,000 of the most popular products in your market segment. Did you buy that inventory?**

**Tony Ellison:** No, everything we did was drop shipped. We bootstrapped the business, so our only way of making things work was to partner with a distributor out of Chicago. For example, the Encarta software was really just CD-ROMs. The good thing about CD-ROMs is that you don't need to touch them to buy them. A lot of people had PCs at that time and CD-ROMs were in high demand. There was no need for a warehousing operation, the entire business was managed from my apartment. When orders started flowing in, I realized that I needed a whole lot more than a one-bedroom apartment.

**Sramana Mitra: Did you finance the startup costs out of your pocket or were there investors involved?**

**Tony Ellison:** I used my own funds. I did not take any outside funds. We have remained privately owned and have not taken any outside funds. We have had a lot of offers, but it just makes no sense for us to take outside funding. We hit profitability early on in the process and our company was growing at a nice pace while being entirely self-sufficient. There was no reason to lose control of the company or start dividing it up between ourselves and investors who may have had completely different agendas.

**Sramana Mitra: Let's trace that journey in a systematic way. The Macworld article gave your site enough visibility to validate your hypothesis that there are enough people willing to buy office products online in 1995.**

**Tony Ellison:** Yes. By 1995 we were already averaging over 100 orders a day.

**Sramana Mitra: Other than the Macworld article how else did people find out about you? There was no Google PPC at that point.**

**Tony Ellison:** If you remember the early days, the popular site was Yahoo. I was one of the fortunate people to have an email from Jerry Yang telling me that I was approved to be listed in their directory. They were building some pretty impressive directories and they covered just about every topic you can imagine. That was a great source of getting discovered. Lycos was also a site that was on the scene. We knew how to leverage SEO at that point and we were coming up on a lot of their search results.

To give you a sense of how scalable our business was, in 1996, we went from 1,000 items to over 120,000 items overnight. That never would have happened if we were a traditional brick and mortar retailer.

**Sramana Mitra: Were you still relying on drop shipping and avoiding the requirements of taking on inventory?**

**Tony Ellison:** Yes. Our model is very much a bare essentials model. We did not invest in any warehousing until recently. We have been working with distributors and trading partners who would ship the products. We were able to connect to the back end of their databases, provide inventory to our users and handle all the marketing, SEO, and SCM.

**Sramana Mitra: Does your business model still rely on third party logistics?**

**Tony Ellison:** Yes, by and large. We have a lot of 3PL relationships as well as a lot of private brands. Today, we offer over 600,000 items. We are in close to 16 different major categories. We started in CD-ROMs and then moved into basic office supplies and ink and toner. Today, we also cover furniture, cleaning and break room supplies, security and safety items, and several other items.

**Sramana Mitra: In 1995, you started getting orders on the Internet. You hit 100 orders a day. What revenue level did you reach that year?**

**Tony Ellison:** We hit the low 7 figures in our first year of operations.

**Sramana Mitra: What kind of margins were you able to maintain?**

**Tony Ellison:** Back in those days, we were able to maintain gross margins in the mid 30% range.

**Sramana Mitra: What about operating margin? What did you need on the operating side to be able to run this business?**

**Tony Ellison:** We were slim and lean. We had operating margins of 10% to 12%, and that is probably a high estimate.

**Sramana Mitra: What was the composition of your team at that time?**

**Tony Ellison:** In the beginning, I had two other part-time employees helping me. They became full-time employees by the end of the year.

**Sramana Mitra: You operated with around $100,000 of profit in your first year. Is that about right?**

**Tony Ellison:** Yes, there was a lot of sweat equity. I was not looking to get paid. Our major expense was G&A because we were operating out of my apartment. My help would come in 4 hours a day here and there. We later opened offices in downtown New York.

**Sramana Mitra: During the period when you were working under a distributor supported model, where was the pick/pack/ship happening?**

**Tony Ellison:** Most of that was done by the distributors. They were the ones who supplemented my Internet savviness. They took over once we captured the order. They did the pick, pack, ship, and management of returns. They handled all of that.

**Sramana Mitra: What changed in 1996 and 1997?**

**Tony Ellison:** The vision expanded. We started to offer a much larger assortment of products and we delved deeper into the IT world. We also started to hire more people. We hired professional IT people and started to market a lot more aggressively. I had built a newsletter by then, I had email campaigns running, and I did a lot of marketing to target customers.

**Sramana Mitra: You were still operating under limited cashflow, right?**

**Tony Ellison:** Yes, I had hired a team of 6 people and I had office expenses. I started to invest in a lot of software. I had to personally fund a lot of that investment and growth.

**Sramana Mitra: Where did that personal funding come from? Did you raise money from friends and family?**

**Tony Ellison:** My previous stint was at Goldman Sachs and that is where I made my money. I worked with private wealth management. I was so passionate that I believed that investing my money in my company would be the best investment that I could make.

**Sramana Mitra: In 1996, you added more people and secured an office. Was there any difference in your distribution or customer acquisition strategies?**

**Tony Ellison:** There was a lot of change in 1996. The biggest expansion was in terms of people and our margins started to erode because of that added expense. We also started adding other products that did not have margins as high as CD-ROMs. My vision was to concentrate on B2B customers as opposed to running a B2C business because B2B customers spent 15 times as much. We also spent a lot of effort retaining those customers instead of acquiring them. That is how the model progressed and evolved during our first three years.

When we looked around at our competitors, we noticed something interesting. All of the sites back then were billboards. They all had their products listed and they all had a shopping cart. There was not any competitive advantage from one site to another one. At that point, I realized that we needed to do something more. We had a tremendous selection, which was an equalizer when it came to competing with the big guys, but we saw that customer acquisition was quickly sky rocketing in our market. That was especially true in 1998 and 1999.

We decided to offer an e-procurement platform. We shifted our focus entirely to B2B. Around that time, Ariba had a very successful IPO. I had the idea that we should take 20% of the functionality from Ariba that is used 80% of the time, and make it available to small and medium sized businesses that could not afford the $750,000 for those types of applications, and create a retention strategy around that. It has worked and has been a great success for us. That is how we started retaining customers, especially from 1999 to 2000 when customer acquisition was shooting through the roof. We were profitable and had better retention rates than our competitors.

**Sramana Mitra: How were you selling to your B2B customer base?**

**Tony Ellison:** We have a sophisticated platform. By 2000, we were offering close to 200,000 items. We realized that we would need to bring in inside sales people to engage in relationship building and explain the benefits of e-procurement. We had to show what the impact was to people who had never thought of using our platform before. Once we showed and demonstrated that to potential customers, they realized how much time they could save and how we were saving them time. They could see how easy it was for them to control the purchase process. There was not a way for small and medium sized businesses to have purchase enforcement across their company. We made that possible for them.

**Sramana Mitra: What timeframe did you start the B2B business?**

**Tony Ellison:** By 1997, we had the e-procurement platform in place. We had solid ground to pursue businesses. By that time, we knew that B2B was the customer base we had to focus on.

**Sramana Mitra: Tell me a bit more about merchandising. Outside of the core office supplies, what else belonged in your product portfolio?**

**Tony Ellison:** Today, we have close to 600,000 items with a mantra of social responsibility. There is no reason why businesses should not purchase eco-friendly products, especially since the prices have dropped and the quality is very high. Since day one, our merchandising strategy has been to offer the largest selection of green products.

We had two primary methods of differentiating ourselves. The first was through our e-procurement, because nobody else had it. The second was our dedication to offering the largest selection of green products anywhere. In order to offer those products, we had to train and educate customers about the benefits.

We came up with tools and approaches to encourage customers to consider eco-friendly products. If a customer wanted to purchase a product that was not eco-friendly, we would provide an option at the point of purchase to convert that order into an eco-friendly product. We also have a green card label that will tell you the aggregate tree and carbon footprint savings of all customers.

We have built an element of social responsibility that has resulted in saving 97,000 trees, which equates to saving 20 forests.

**Sramana Mitra: What are the different categories of product that are included in your scope?**

**Tony Ellison:** Green products, traditional office supplies, furniture, paper, ink and toner, cleaning products, food and break room supplies, tools, medical supplies, restaurant supplies, safety supplies, and other categories.

**Sramana Mitra: Are there segments of SMB customers where you are bigger than others?**

**Tony Ellison:** We seem to be doing very well in the health industry. We also do well in the financial services and retail categories.

**Sramana Mitra: How much of your own money did you have to put in to get the business to this stage?**

**Tony Ellison:** In the early days, I invested all of the savings that I had. I bootstrapped this business to become the number one e-commerce player in our category. We have done all of that by maintaining social responsibility. We have a vision to make green products a standard in the industry and I don’t know anyone else that has attempted to start that trend. We have found that our efforts have been very well received.

We have the largest selection of products in our industry. I have noticed that recently Staples decided to copy our model. They are a huge believer in funneling down and have maintained a catalogue of 10,000 high value items, which has given them leverage in negotiations. Now they are reversing that funnel. I am hoping that the next thing they announce is that they will be as green as we are.

**Sramana Mitra: You have crossed a lot of categories that are not traditional for your market area. What was the strategy behind that decision?**

**Tony Ellison**: We are the first in our industry to cross the traditional lines of office supplies and offer many unconventional products that businesses need. This is important because we cater to small and medium sized businesses. Most of the time there is one buyer who is responsible for not only business supplies but pretty much all purchase. Shoplet is the trailblazer in our industry. We have defined the borders. We have defined the responsibility our industry has to take. We have defined the rules of engagement that companies like ours must have with customers and what the expectation should be from the SMB perspective.

**Sramana Mitra: Are you still doing all outsourced distribution?**

**Tony Ellison**: By and large we still follow the outsourced model. We have engaged with 3PL companies and we have a number of items we can ship that way. We also have a select amount of products that are now our own brand.

**Sramana Mitra: I think that one of the secrets of your ability to bootstrap the company to the extent that you have done is not having to carry inventory. You have not had to take out loans to cover inventory.**

**Tony Ellison**: I completely agree that it was a low risk strategy.

**Sramana Mitra: It has also enabled you to expand into other categories and have such a large product offering. Maintaining the correct**

**distribution relationships is not necessarily easy to do. A key aspect of running an e-commerce business is having reliable fulfillment.**

**Tony Ellison**: You have hit the nail on the head. It was not only having the distribution figured out, it was using the Internet. Otherwise, I would have had to penetrate markets state by state. I was able to offer a solution on a national basis. As a result the addressable market became much bigger. We were able to gain a huge market with very low risk, which gave us universal appeal to distributors. I am proud to say that we transformed the industry.

**Sramana Mitra: You said you have some private label products. In retail private label is a very profitable strategy that all retailers deploy once they reach a certain critical mass. Which categories contain your private label products?**

**Tony Ellison**: We followed a specific strategy for private labeling. We don't have the physical stores that the big boys have. It is important for us to have a small catalogue as a leave behind. Branding was key to our strategy.

We also wanted to control some of the variables on those products. We have private labeled ink and toner, which is a low margin business and requires us to source it very well. When you go private label and make buying commitments, you can get much better margins but you also have to source it properly.

We felt that private labels let us achieve a premier status in the industry. If you don't have private label paper then you are not viewed the same way that the big boys are.

**Sramana Mitra: I would imagine you are using the private label strategy to drive margins up, correct? That is one of the levers that you can push.**

**Tony Ellison:** Yes, that is correct.

**Sramana Mitra: What categories offer you the best levers for your private label strategy?**

**Tony Ellison:** Traditional office supplies. We segmented our industry into A, B, C, and D. A and B are commodity segments and C and D are long tail products. Anything that falls into C and D are where we will find the margins.

**Sramana Mitra: You started by outsourcing, then brought on part-time employees who later converted into full-time employees. How has your team building experience developed since then?**

**Tony Ellison:** Our team has been built very quickly. We have close to 75 people now. We expanded internationally in 2013 when we opened up business in the U.K. and Canada. We have bodies on the ground in both of those countries.

**Sramana Mitra: When you pivoted your business into a B2B procurement mode, did you have to make a significant investment in your workforce?**

**Tony Ellison:** Yes, you are correct. Most of our development work was done in house and that required a fair amount of capital.

**Sramana Mitra: How are your 75 employees organized?**

**Tony Ellison:** We have about 25 inside sales people. We have 17 in customer service. We also have business development, creative, and IT developers. There are 6 of us on the leadership team.

**Sramana Mitra: Do you operate a warehouse to manage your private label strategy?**

**Tony Ellison:** You can use a virtual warehouse. You can strike an agreement with any of the 3PL houses out there, which saves you on the upfront cash requirements. We pay slightly more, but we reduce our risk substantially. We turned profitable in 1997 and we have been cashflow positive since then. We have built the business on our cashflow.

**Sramana Mitra: It sounds like you have traded off margin to keep the logistical complexity of the business to a minimum.**

**Tony Ellison:** That is correct.

**Sramana Mitra: That is a very smart move.**

**Tony Ellison:** Thank you! I think we have built a phenomenal playbook. We know how to go to other parts of the world who are e-commerce friendly. About 95% of our business is transferable, the remainder requires some tweaking.

**Sramana Mitra: You can expand anywhere there is a logistics infrastructure. There are some very large countries that do not have logistics infrastructure, such as India where that is an absolute disaster.**

**Tony Ellison:** We looked at India and arrived at the same conclusion very quickly. India and China pose significant challenges. Japan is a lot better. We are also interested in Brazil.

**Sramana Mitra: Fantastic. Thank you for sharing your story and congratulations on your success.**

# Interview with Peter Mann, Founder of Oransi

*Peter Mann started Oransi as a B-to-C e-commerce company. Today, 40% of his $10M revenue comes from China. This is the kind of company America hopes to see more of – selling American products to international consumers.*

*Peter started with selling other people's products, and eventually, developed a product line of his own.*

**Sramana Mitra: Peter, let's start with your background. Where were you born and raised? What kind of background leads up to your entrepreneur story?**

**Peter Mann:** I was born in Syracuse, New York. I lived in the same house till I was 18 and went off to college. My father was a mechanical engineer. He was a manager at General Electric. He comes from a time when people worked 40 years in a company and then get their retirement package. He was also a professor of Mechanical Engineering at Syracuse University. We were heavily involved with the university. I grew up around a university atmosphere during my childhood.

**Sramana Mitra: What about college? What path did you follow?**

**Peter Mann:** I went to the University of Rochester, which was 90 minutes down the road. My degree was in Statistics. I really like Math. The further I got into Math, the more theoretical it became. I like more applied Math. That's how I ended up in Statistics. I went to Rochester on a Navy ROTC scholarship. I liked the idea of having a job when I got out of college as well as having my tuition paid for four years. It was a good deal for me. At that time in

Rochester, 10% of the student body was in Navy ROTC. It was a pretty large group.

**Sramana Mitra: What did you do after college?**

**Peter Mann:** I went into the Navy after college. In college, another thing that I did that was helpful to me was starting a fraternity. Instead of joining a fraternity, I got together with a group of friends and started our own fraternity. That was a really good experience in terms of forming an organization and going out and recruiting people. At this point – 25 years later – it's growing strong and is consistently ranked as the top fraternity at the university. That's something we're very proud of.

Upon graduation, I went into the Navy. I was in Newport for Officer Training. I was stationed at a frigate out of North Virginia. I was there for about three and a half years. That was a really good experience because I was just 21 and was given 23 people to manage – nearly all of whom were older than me. You are in a situation where you have to respond very quickly and use your training but also use people skills to get the job done. Most people under 21 wouldn't get a management position like that.

Shortly after that, the Gulf War began and so we were sent over to the Red Sea for about six months. That was a life-changing event for me. I got married a year out of college. We got married very young. My wife was expecting. I missed the last six months of the pregnancy and I missed the birth. I didn't actually find out that my son was born until a day or two after because we didn't have Internet.

**Sramana Mitra: What year are we talking of when you got back from the Gulf War?**

**Peter Mann:** I got back at the beginning of 1992.

**Sramana Mitra: What did you do when you got back?**

**Peter Mann:** I started looking for a job. While you're in the military, the notion is that you get a great experience and then you can get out and take a job. What I, and a lot of other people, found out was that while you have skills, it's somewhat difficult to transfer that to a relevant business experience. Leveraging my Statistics degree, I got a $20,000 a year entry-level job at a manufacturing company in Florida, which is where my wife is from. I quit the job because that wasn't my career aspiration. I felt it was easier to find a job when you had a job than to have a gap show up in your resume. I only worked there for about a year.

I applied to a job for a similar position at Tech Data, which is a large computer distributor. This is more of an individual contributor position. It's more about leveraging my Statistics degree and analytical skills. That was a great experience for me. The company was doing $900 million in sales. The seven years that I was there, we reached over $20 billion. I moved up in position from entry level to a director level.

**Sramana Mitra: What year does that bring us up to? About the end of the '90s?**

**Peter Mann:** That brings us up to 2000. From 1991 to 1992, I was at that manufacturing company. Then from 1993 to 2000, I was at Tech Data. When I was at Tech Data, our second son was born. I went to school at night to get my Masters degree in Engineering Management at the University of South Florida. It was a pretty busy and exciting time.

My son, when he was born, had asthma. It was just an awful experience for everyone. There were times when he just couldn't breathe. He was helpless. How can you help someone breathe? That was really a challenging time for about a year when he was really struggling health-wise. That stuck with me. It led me to our current business.

**Sramana Mitra: What happened in 2000?**

**Peter Mann:** I was recruited by Dell to be a Senior Manager and develop dell.com. That's how I ended up in Austin. I did that for about a year and a half. I had two positions there where I was responsible for strategy for all of the products and I was pretty heavily involved with the launching of Dell printers. Dell was getting into the printer market in a strong way. I had a big role in watching that product. That was a really good experience in terms of bringing a product into the market. I didn't get it in MBA. Between Tech Data and Dell, I got experience on the job which was as good or better than what you would get in a business school.

**Sramana Mitra: What happened after Dell?**

**Peter Mann:** When I was at Dell, I learned pretty quickly that the culture wasn't what I was expecting. At the same time, the Internet bubble burst. Dell started going through round after round of layoffs. The morale was low. It was a difficult environment from a cultural perspective. I was confident that I wasn't going to lose my job but at the same time, no one really knew what was going to happen.

I had a friend in Austin who had an e-commerce business. We were talking and we decided that we were going to create an e-commerce business together. I worked at Dell during the day. This was my night job. I'd put in a few hours after work. After six months, it got to a point where I was able to replace my Dell salary with this business. So, I moved full time into that business in 2003.

**Sramana Mitra: What kind of e-commerce business were you involved in?**

**Peter Mann:** We were selling higher-end appliances – things that require more of a consultative type of sale. That did well. In 2009, I sold my 50% stake in the business to my business partner to work full time on my own company that focuses on indoor air quality and clean air. That's how I got into the manufacturing of higher range air purification products.

**Sramana Mitra: You basically got out of your e-commerce company where you were an equal shareholder and then you started your own company after that? What was the value of your 50% share in the e-commerce company?**

**Peter Mann:** I can't really say. I would tell you, but the other person's very sensitive to the numbers.

**Sramana Mitra: But was it a significant amount of money?**

**Peter Mann:** It was for me. It was big enough to start this business.

**Sramana Mitra: Sounds like you were able to self-fund your new company.**

**Peter Mann:** Yes, I totally self-funded this business.

**Sramana Mitra: What drew you to this concept and what was in your mind when you started this business?**

**Peter Mann:** I grew up in New York and moved to the South. I have self-developed allergies that I never had as a kid. While we sold air purifiers, I never really found one that was effective for me. Also, the experience that I had with my son and his asthma drew me to this. I know there are a lot of people with asthma and allergies who are looking for non-invasive, non-drug type of products. I just thought that there had to be a way. That was what drove me.

Initially, I started with a couple of factories in China and started with those products to get the business started. These were mostly Chinese developed products that I adjusted and branded. It wasn't really manufactured from the ground-up by us. Shortly thereafter, I started looking at air purifiers. In its simplest form, it's a motor, fan, and a filter. My idea was to get the best filters, motors, and fans and put them together. That kicked off about a year's worth of research into different motor manufacturers. I was looking at it as a high-end consumer product with industrial-quality components. I evaluated component after component until I settled on the components that we felt comfortable putting into the product. We built a prototype and ran it for several months. That's how we got into the current air products at Oransi.

**Sramana Mitra: Even though in the beginning you just sold some products that were manufactured by Chinese manufacturers, you were also really working on an industrial quality product of your own for high-end consumers?**

**Peter Mann:** Correct. We were going to transition away fairly quickly from the Chinese products and focus on the American-made products. I also wanted to get some more consumer feedback and some experience in bringing a product to market. It's much easier to get growing more quickly when there's a product that's almost built.

I didn't really want to bring in investors. I was looking more into bootstrapping it. If I can generate some cashflow, then that was a better way to go than getting outside investors.

**Sramana Mitra: I imagine you were building a customer base and a brand around the whole air purification category on the Internet. Correct?**

**Peter Mann:** We were building up the brand and getting some experience, because I knew it would take time to launch the US-made product.

**Sramana Mitra: At what point in your journey with Oransi were you able to launch your own product? You started in 2009. When was the new product launched?**

**Peter Mann:** We launched five American products in 2013. We did a lot of testing. It takes some time with research and design.

**Sramana Mitra: Let's get some of the specifics of what happened between 2009 and 2013 while you were selling products from the Chinese manufacturers. How many different types of products did you have in your roster? What was the customer acquisition model?**

**Peter Mann:** We started the company at the end of 2009. 2010 was when we started selling. We really sold just a few products. We kept it at two products of the private-labeled Chinese products. The sales channel has been online direct.

**Sramana Mitra: Do you acquire customers through Google PPC? How do you acquire customers?**

**Peter Mann:** Yes, through Google. There's a big engine there. We do some of the other smaller search engines like Bing and some of the shopping comparison sites.

**Sramana Mitra: It's mostly paid search-based customer acquisition – PPC?**

**Peter Mann:** That's how we started. We have a brand that no one has ever heard before. It's hard to get started and so PPC is the quick way to get up and going. It's expensive, though. We're trying to have PR and some other marketing in place as well. Google PPC is still probably two-thirds of our advertising spend though. It's down from close to 100%.

**Sramana Mitra: Is there any other marketing strategy that stands out as a successful one besides Google PPC?**

**Peter Mann:** Amazon gets stronger every year. We sold through one or two catalog companies. That wasn't as successful as I'd hoped. Over time, they start to create their own brands so your products don't get the focus. They have their own business and they got to do what makes sense to them. We sell through a couple of Internet-based sites that are pretty big. They focus on air quality.

**Sramana Mitra: You're selling in the Amazon marketplace?**

**Peter Mann:** We're selling on Vendor Central. Amazon inventories our products and stocks it. Every week, Amazon orders from us and they ship direct to customers. We never see the customer orders that Amazon serves.

**Sramana Mitra: But the customer acquisition is done by Amazon or by you?**

**Peter Mann:** By Amazon.

**Sramana Mitra: Essentially, Amazon is selling your product catalog?**

**Peter Mann:** Yes.

**Sramana Mitra: What are the terms of working with Amazon under that model?**

**Peter Mann:** Sunday night or Monday morning, we get a batch of orders from them.

**Sramana Mitra: Amazon is purchasing at wholesale price?**

**Peter Mann:** Yes, they get the wholesale price. They have the retail model but they're buying at a wholesale price. They also have payment terms.

**Sramana Mitra: The products that you are selling through Amazon, is this the America- or China-made product?**

**Peter Mann:** Amazon carries the entire catalog. That's part of their pitch to get you in.

**Sramana Mitra: Let's talk about the product that you've launched of your own. You obviously did a lot of research and designed the product. You said you were manufacturing in the US. Tell me more about that. Did I hear you right that you are manufacturing that product in the US?**

**Peter Mann:** The product is being manufactured in the US. We've designed the product and then we found a contract manufacturer to put the pieces together. That was another decision point because to go out and get the equipment required a lot of capital expenditure. It's made out of different types of metals and some of these are very big pieces and require very modern and complicated equipment to manufacture. The decision was either go out and buy the equipment or outsource it.

**Sramana Mitra: It definitely makes sense to outsource but you chose not to outsource to China. You chose to outsource to a US contract manufacturer. What drove that decision?**

**Peter Mann:** We looked at doing it in China but we couldn't get to the same level of quality.

**Sramana Mitra: Where is your contract manufacturer in the US?**

**Peter Mann:** They're in Connecticut.

**Sramana Mitra: Are you selling the new product in the US only?**

**Peter Mann:** We sell in the US, Canada, and China.

**Sramana Mitra: Talk to me more about how come you're selling it in China and how you're selling it in China.**

**Peter Mann:** We've been getting requests from companies in China to sell our products. They expressed interest in selling America-made products. The air quality there is bad and it's very well reported on. The EPA has standards for measuring air quality – the air quality index. They measure two different ranges of particulate sizes. Two years ago, the US embassy in Beijing started recording using the same standards to report on daily air quality levels. Before that, it was the Chinese government but there wasn't a lot of confidence in those numbers. Once they use the EPA metrics, people realize how serious a problem it is. That has driven awareness and huge demands for air purification products in general, as well as higher-end air purifier products.

In a few years, depending upon what research you read, it's supposed to be between $20 billion and 30 billion in sales. In the US, it's just a billion dollar market. China is a much bigger market with much more demand. There're really few products that come close to what we offer. There's nobody that has the product we have in the US. We started small in China. We sell through distributors.

**Sramana Mitra: Are they online distributors or physical distributors?**

**Peter Mann:** Physical distributors who sell primarily to Chinese consumers.

**Sramana Mitra: There's a market developing in China right now where e-commerce companies are being set-up in China. These guys order wholesale from US manufacturers to sell US products into China.**

**Peter Mann:** We are aware of that, but we haven't signed any deals with those sites to date.

**Sramana Mitra: What about other geographies? Obviously, there are several countries where air pollution is a very big problem. The things that drew you to start this company are very big problems in Brazil and India, for example. What are your plans to expand into those countries?**

**Peter Mann:** We are evaluating those markets. I know India, in particular, is similar to China in terms of severity of the problem. The market and the people haven't gotten to the point where they're actively looking for products to solve that problem. India will get there but the market today is not there yet, from a demand standpoint. We're a relatively new company and it's easier to sell where the demand is than trying to create the demand. It hasn't really got market acceptance. It's in the very early adopter stage in those places. We're very interested in those markets, but the market size is very small at the moment for a higher-end product like ours.

**Sramana Mitra: How much business are you doing in China? What percentage of your revenue comes from China right now?**

**Peter Mann:** This year, we're planning to do $10 million. I would say 40% would be in China this year.

**Sramana Mitra: Probably significantly higher percentage of revenue over the next couple of years will come from China.**

**Peter Mann:** Yes. The market is 20 times bigger.

**Sramana Mitra: That's very interesting, because it's one of the stories that the American audience wants to hear about where America-made products are being sold abroad.**

**Peter Mann:** Yes, we had to learn how to do exporting because not many people export into China.

**Sramana Mitra: You have so far self-financed the company right?**

**Peter Mann:** Yes.

**Sramana Mitra: What about the team? You started the company yourself. How have you fleshed out the team to support the kind of revenue that you're generating now?**

**Peter Mann:** We have a very lean organization. We do a lot of outsourcing. The manufacturing is outsourced. Warehousing is also outsourced. These are companies that are really extensions to our business because we couldn't get here without their expertise. We focus on our core competencies, which is designing and developing new products, and customer support. We're not going to outsource customer service to another company. We want to hear, firsthand, from customers, what's happening. You really can't outsource sales. Outside of that, we've been leveraging other companies' expertise in certain areas. It's really been good because we can't afford a higher-level person in a broader range of skill sets. We can work with engineers at the factory to help with designing the products. Although they are different companies, we really treat them as an extension of our business. We have weekly conference calls and meetings.

**Sramana Mitra: Except that you get to use expertise across a broader portfolio.**

**Peter Mann:** Yes, we get a lot of expertise that a company of our size can't afford.

**Sramana Mitra: I talk to many entrepreneurs who are doing these e-commerce companies that have heavy logistics and other processes that are not necessarily so easy to build up internally. What they do is trade-off margin, to some extent, to keep the logistics of the business relatively simple. I think you're doing the same thing.**

**Peter Mann:** Yes. I'm in Austin. There's an organization called the Incubation Station. It's their third year and they are working with consumer goods companies. That's the model that most of these companies follow – to outsource particularly manufacturing, co-packing, and fulfillment. In China, that's not the standard. When we're talking to distributors and they see our model, we have to explain to them that this is how we do business in America. It's not the traditional huge company with a thousand employees.

**Sramana Mitra: I think that infrastructure is not as well built in many of the other countries – whether it's China or India. I think the logistics infrastructure in China is better than India though. The logistics infrastructure in India is quite poor. You can do business like this in the US much more easily than in a lot of other places.**

**Peter Mann:** Right.

**Sramana Mitra: I think I've got your story. Is there anything else you want to share?**

**Peter Mann:** I'm good. I appreciate your time.

**Sramana Mitra: Excellent. Very nice talking to you Peter. Good luck!**

# Interview with Aaron Block, CEO, Bay.Ru

*Aaron Block is the CEO of Bay.ru, the first cross-border e-commerce business in Russia and the fastest growing shopping site in Russia. Bay.ru's growth has been powered by affiliate partnerships with eBay and Amazon, each of which provides Bay.ru an integrated product catalog in a wide range of categories.*

**Sramana Mitra: Aaron, let's start with your personal story. Where are you from? What kind of background leads up to the Bay.ru story?**

**Aaron Block:** I was born and raised in Chicago. I studied urban and regional planning at the University of Illinois. I started my career in commercial real estate with Cushman and Wakefield, the third largest global real estate firm in the world. I was a commercial real estate broker in Chicago and New York City. I had an opportunity to go to Moscow to grow and manage the largest division of Cushman and Wakefield's newly acquired Russian business in Moscow in 2005.

From 2005 to 2008 I was living in Moscow with my fiancée and now wife. We built that business from a couple hundred thousand to $10 million a year. That was quite an event and a lot of fun. At the end of 2008 my wife was pregnant with our first child, so we moved back to the United States. I was recruited to run the Chicago and Midwest division of Cushman and Wakefield. I stayed there until 2010, which is when I joined Bay.ru via a mutual friend. He was an investor in the company and asked me to join the board and invest. I was originally an investor in the business, but at the end of 2010 I decided to take a deeper, operational role in the business.

**Sramana Mitra: What is the genesis of Bay.ru?**

**Aaron Block:** It was founded in 2007 by two brothers who had emigrated from Russia when they were young. Their mission when driving this business was to solve the problem of cross-border shopping for their friends and family. It was somewhat altruistic. They wanted their friends and family in the former Soviet Union to be able to shop the same way that they shopped online in the United States. Their goals were to provide the same convenience, safety, reliability, and price that they themselves experienced in America. As a lot of people who are not from the United States know, when people go back to their home countries they are often asked to bring toys, electronics, and other goods to their friends and families. They end up being mules! These men had a great idea and were able to build an incredible operation surrounded by technology. They met great investors and were able to scale in a way that many others have not been able to do.

**Sramana Mitra: How does the sales cycle work? Is delivery fulfillment happening in Russia with merchandise stored in Russian warehouses?**

**Aaron Block:** We are a middleman in Russia, but in the U.S. we are known as a cross-border e-commerce company. There are a number of players in the cross-border space. The cross-border space means that you shop from a location outside of the U.S., typically the big markets from which you would buy are the U.K. and China. You will shop online and have the goods delivered to you, the consumer, directly from abroad.

In terms of our business, there is very little going on in terms of a supply chain inside the former Soviet Union. The entire operation, including the Russian-speaking call center, happens to be in the suburbs of Chicago. The goods move from the manufacturer, wholesaler, or retailer in the United States to our warehouse in Chicago. We open the goods to do quality control and reconciliation against the order to make sure that the item ordered is the exact item shipped. That is a big step in the process for a cross-border company. We then do a few value-added services such as photographs, consolidation, and quality assurance. At the customer's request, we will repackage and ship to the former Soviet Union with proper customs forms completed. The packages are shipped directly to the end user.

**Sramana Mitra: Is the order taken directly by Bay.ru?**

**Aaron Block:** Yes. The consumer never sees the vendor and the vendor never sees the consumer. That creates a lot of trust and eliminates a lot of problems in the process. We are experts at capturing demand. Over the past five years there has been tremendous demand that far outstrips supply in the former Soviet Union. The populace is becoming wealthier by the day, as many of us know. The emerging middle class has a lot more money to spend. The supply chain infrastructure in Russia is not robust enough to satisfy this demand. In addition, there are problems with payment online. They are still a cash-based economy. Credit cards have not yet taken hold like they have in the U.S.

We offer 500,000 payment points in Russia. Customers browse more than 200,000,000 SKUs on our site because we integrate other catalogs such as Amazon and eBay on our site. A customer is captured by our marketing channels and drive to our site where they can browse and order what they want. They check out using a single shopping basket, which starts the operations process. A payment confirmation call comes from Chicago and the movement of the goods to the user via Chicago begins.

**Sramana Mitra: How many touchpoints do you have in Russia to take orders?**

**Aaron Block:** We have 500,000 touch points in Russia.

**Sramana Mitra: What does that mean? Do you have kiosks?**

**Aaron Block:** Kiosks are prolific in Russia. People pre-pay with telephone bills among other bills. We also have a presence in Russian bank branches**,** Russian post offices, Western Union stores, and online payment systems. We have found a way to accept every which way a person might find to be a comfortable manner of payment.

**Sramana Mitra: It sounds like one of the innovations you have accomplished was creating a wide range of payment options for Russian consumers. Is that a fair statement?**

**Aaron Block:** Yes, definitely. It took a significant amount of work to create all of the payment touchpoints in a way that resounded with the Russian consumer.

**Sramana Mitra: Let's discuss your catalog innovations. When you bring in a catalog from eBay or Amazon, do you find it easy to interface with those catalogs?**

**Aaron Block:** We have built our own catalog via our relationships with wholesalers and manufacturers in the United States. We also present the goods from eBay and Amazon in our catalog. Those two catalogs are collected via APIs. We do real-time search, and those conversations occur directly between our servers. We happen to be a very large buyer of eBay seller goods and Amazon seller goods. We like to think we have a good relationship with them as we help them build their brand and their relationships in Russia.

**Sramana Mitra: Your customers are not looking at Amazon and eBay websites, are they? They are looking at the Bay.ru website, correct?**

**Aaron Block:** Exactly. They are looking at our website and seeing goods that are, in many cases, sourced from eBay and Amazon. We take the eBay and Amazon catalog information and present it in a truly Russian fashion. We have spent five years doing usability testing and have made plenty of mistakes. We have found a way to present the catalog data and photographs in a way that suits the Russian sensibility. It is the 'built by Russians, for Russians' mentality as opposed to the localization of an international site that is another competitive advantage for us.

**Sramana Mitra: What is special about 'built by Russians, for Russians'? What are some of the nuances of that phrase?**

**Aaron Block:** The way the shipping is presented is important. Obviously cross-border e-commerce makes shipping difficult. We make the options for shipping very, very clear. How we present the photographs of the goods is different from what you would see with other e-commerce websites. Other sites would consider our methodology to be a bit busy, but usability testing has told us that our methodology works well for us. Catalog integration is something that other people do not do well. We have become good at allowing our users to search for goods across multiple catalogs.

**Sramana Mitra: When it comes to buying items from wholesalers and owning your own catalog, I can see a very straightforward retail business model. What is the business model behind your integrated catalog?**

**Aaron Block:** The customer pre-pays us 100% of the price of the good. We will then source the good from the appropriate vendor, manufacturer, or retailer depending on where the item was browsed and the reputation and reliability of the seller. Our job is to deliver the end good to the consumer as quickly as we can in its "as described" condition.

**Sramana Mitra: When you are buying wholesale, you have enough margin on the sale price to make a decent profit. If you are buying from other retailers, the margins tend to be less interesting. Is your margin with eBay or Amazon acceptable?**

**Aaron Block:** There is a market for international goods in Russia. The markup above retail price is anywhere from 9% to 45%. We collect margin there. We also provide a number of value-added services during the supply chain process. We also buy shipping at wholesale prices because we are an enormous exporter of goods. We use a lot of freight, postal, and courier services, so we have ample opportunities to get margin on that side. When everything is combined, our margins work out well.

**Sramana Mitra: You are basically making your margins based on prices that consumers are willing to tolerate, and shipping margins?**

**Aaron Block:** In addition to what you have mentioned, we achieve margins on the value-added services around the online retail portion of what we do.

**Sramana Mitra: What is the merchandise mix? Where is the interest of the Russian consumer?**

**Aaron Block:** We track very closely to eBay's largest categories. Our largest category by far is auto parts, followed by fashion and electronics. However, we have a very long tail of consumer goods. People shop from America because they are enthusiasts or they are looking for something specific that is not carried in the mainstream retail market in Russia. We sell a lot of toys, jewelry, and collectibles. The list goes on from there.

**Sramana Mitra: Are the founders of the company still involved with the business?**

**Aaron Block:** They are. Part of the reason I decided to join the business after I invested is because of the shared approach, and capabilities of the founders. One founder is now the chief marketing officer and the other is the chief operating officer. One handles the capturing and creation of demand, while the other controls the supply chain process. Both are incredibly important roles.

The younger brother, Anton, is the chief marketing officer and the real founder of the business. This was his baby from the beginning. He had been selling on eBay while he was in college and dropped out to attend to this business full time, much to the chagrin of his older brother and partner, Gene, who at the time was working at Orbitz as the director of software technology. Between Gene's technology savvy and Anton's entrepreneurial spunk, the two found a way to get the operational, entrepreneurial, and technology aspects of the business figured out. This all came about because Anton and Gene were constantly asked by their family and friends to bring items back with them to Russia.

**Sramana Mitra: How did the Bay.ru business get off the ground? Did the founders bootstrap or take financing?**

**Aaron Block:** They took some loans from friends and family as well as some personal loans. They really bootstrapped the business, and that culture persists today. We consider ourselves a frugal organization. We just reached profitability in March, which is exciting. We watch every single penny, and that is part of the culture that attracted me to this company. Any startup needs to mind its pennies and dollars to be successful.

**Sramana Mitra: What was the ramp rate of the business?**

**Aaron Block:** The company ran pretty close to breakeven from the beginning. They had a slight loss the first couple of years. They brought on the first round of outside investments in 2009. They had two subsequent rounds, so there are now $2.3 million invested in the business. We reached our first $100,000 revenue months in 2010. We had our first $500,000 and million dollar revenue months in 2011. We reached our first $2 million revenue month this year. We will be at a $40 million run rate by the end of this year.

**Sramana Mitra: How are you growing the business? What are the levers you are pushing?**

**Aaron Block:** The most important thing is talent. We need to have very smart people and focus on improving the operations. We have somewhat complex operations relative to other startups that do not handle the movement of goods across multiple countries. Finding ways to bring in the right technologies and people to minimize headcount growth is one important lever.

Another key is for us to take advantage of the Russian marketing opportunity. We were just scratching the surface of pay-per-click marketing when I joined. We have been building out a robust marketing platform with the help of our team in Russia. Our biggest growth problem so far is lack of awareness. The cross-border shopping market is estimated to be $700 million this year. Getting the word out has been a big piece of what we are doing.

**Sramana Mitra: What else is interesting about your business that is worth covering in this story?**

**Aaron Block:** The founders, Anton and Gene, created a proprietary shipping algorithm. This does not get a lot of press, but it is a reason why we compete so well in our space. We estimate the fully loaded and fully landed shipping cost before the checkout is finished. The customer knows exactly what he or she is going to pay before they make the transaction. If people try other forms of cross-border e-commerce, they often have to buy the goods separately and have them shipped to a middleman service, have the goods weighed and priced, and then pay a second round of shipping costs. We integrate everything into one cost based on our five years of experience shipping to all time zones of Russia.

**Sramana Mitra: Would you say that your shipping algorithm is one of your core competencies?**

**Aaron Block:** Our proprietary shipping algorithm is something we think is very special and we covet it. Another interesting aspect of our business is that we have the majority of our operation in Chicago even though we focus on the former Soviet Union. We have 55 employees between the two countries and more than 40 of them are based in Chicago. There are only four of us in the company who were not born in the former Soviet Union.

**Sramana Mitra: You basically have Russians working in Chicago for an e-commerce company that sells in Russia?**

**Aaron Block:** Correct. Most of them are immigrants, and some of them are here on assignment. Most of us in the executive ranks travel back and forth a lot. I spend a week or two there every month. The head of Russian operations spends one to two weeks in Chicago a month.

**Sramana Mitra: What is the Russian marketing strategy? How many customers are transacting through your platform?**

**Aaron Block:** This year we should do 200,000 orders.

**Sramana Mitra: You are going to do $40 million on 200,000 orders?**

**Aaron Block:** Yes.

**Sramana Mitra: Wow. I assumed this was more of a consumer business, but those numbers are along the lines of a B2B business.**

**Aaron Block:** It is a consumer business. The order values are very high.

**Sramana Mitra: That is fascinating. Tell me more. Who are your customers?**

**Aaron Block:** Our customers cut across the entire population. If you have money and want to buy goods, then you are going to be interested in shopping abroad because the supply is so far below the demand in Russia. Our customers range from one-off purchasers in small villages in Siberia to twenty-something cosmopolitan yuppies in St. Petersburg and Moscow. About half of our business comes from a combination of the Moscow and St. Petersburg regions. The other half comes from the rest of the country.

**Sramana Mitra: Are there any other nuances to the Moscow and St. Petersburg customer base? How do you figure out whom to target when you market there?**

**Aaron Block:** People are very brand oriented. We spend a lot of time focusing on brand preferences. We do a lot of digital marketing although television is on the horizon. That has been a great success venue for other online businesses in Russia.

**Sramana Mitra: Traditionally, consumer marketing is defined by demographics like age, disposable income, geography. Do you know that data for your customers?**

**Aaron Block:** I would rather not go into too much detail, but yes, we do know that data. Our customer base is primarily men. We have a very uncommon business. We have high-value orders, a predominantly male customer base, and a distribution that covers the entire country.

**Sramana Mitra: How much money have you invested or raised to build this company?**

**Aaron Block:** We have raised $2.3 million of angel investment.

**Sramana Mitra: Congratulations, you have done a fantastic job of building a business with very little capital.**

**Aaron Block:** I am sure you advise your incubator companies on the value of bootstrapping. It is very sexy to interact with venture capital, but I think it is more important to give yourself a runway.

**Sramana Mitra: I completely believe in capital-efficient business practices. That is not the method of Silicon Valley, and sometimes people think entrepreneurship means financing. I believe entrepreneurship means customers, revenues and profits. This is a difficult concept for young entrepreneurs to grasp.**

**Aaron Block:** All of our key people are shareholders. We give straight stock grants. We talk about what dilution and fundraising mean as we balance the need to grow. Every time you raise money, you are selling a piece of your company, and the people you are selling to may or may not share your values. You need to make sure you have everyone pointed in the same direction. We handpick our angel investors to make sure we have people who embrace the same ideology. I can't take any credit for the success of this business. We have a bunch of smart people who have the same, shared ideology as we do.

**Sramana Mitra: What is your strategy going forward? Do you want to grow faster with the aid of external financing now that you know the mechanics of the business?**

**Aaron Block:** We are keeping all options open. We are not raising money now. I have been through that a few times, and it can be very distracting. In our business it is important to keep your head down and grow. We believe that having a healthy, profitable, fast-growth business is the most important thing. We will give up top-line growth to maintain this profitability. Right now we are content, but that does not mean that we will not address this later this year. We are a retail business and that does mean we are a bit seasonal. We are going to have a big push coming up soon. Once we get through that, we can sit down and reevaluate our options for 2013 and 2014.

We are just a bunch of pragmatic Chicago guys who are trying to build a great business. It is refreshing to hear someone else who shares those values, especially since you coach entrepreneurs. I have spent a bit of time on your site, and you do great things. I talk to a lot of people who get caught up in hype. Good luck to you.

**Sramana Mitra: I look forward to keeping in touch. Congratulations on your success; you have built a great company.**

## E-Commerce in India

Relatively speaking, the Indian e-commerce has grown at a slow pace.

Compared to India's 2013 market of ~$2 billion, the Chinese market was ~$300 billion, surpassing the US as the world's largest e-commerce market.

Forrester says, India had a total population of 1.28 billion in 2013, of whom, nearly 16% or a little over 200 million are online. Only 14% of the online users currently purchase online (~30 million).

Forrester expects the online buyer population in India to grow to 128 million by 2018.

Many factors stand of the way of India's online shopping adoption. For one thing, Indian consumers do not like to pay with credit cards for merchandise they shop for online. Remember 1993 America? Consumers were slowly getting comfortable with putting in their credit cards on online shopping sites. India's situation is not so different from the 1993-95 America. Whereas China has made a gigantic, concerted leap into the 21st century, India is still muddling along with a low-trust society that prevents high velocity business growth, a terrible infrastructure with poor logistics and supply chain capabilities, and an overall lack of reforms that can accelerate growth.

All this has created an advantage for Flipkart, the market leader, to create a strong brand, invest in supply-chain, and get ahead. Flipkart was founded in 2007 and bootstrapped for two years by Sachin and Binny Bansal, before receiving its first institutional financing of $1 million from Accel Partners in 2009. Once Accel invested, and Flipkart was able to position itself as the horse to bet on for the Indian e-commerce market, money started to flow in, even though the e-commerce market was not growing at a fast pace.

Investors decided that would basically invest in 'making' the market – a decision they seldom make.

A financing bonanza followed: $10 million in 2010, $20 million in 2011, $150 million in 2012, $360 million in 2013, and over $1.2 billion in 2014.

In July 2014, the company raised its most recent round of $1 billion financing valued at $7 billion.

Of course, investors do not build companies, entrepreneurs do. Flipkart's run rate has crossed $1 billion in 2014, so the entrepreneurs have executed well so far. They have also followed a roll-up strategy, acquiring players like Myntra, a strong player in the Indian fashion vertical. They have built an immense logistics infrastructure, something the Indian market lacks completely. There is no equivalent of UPS for reliable delivery!

While the policy malaise thus far in the retail sector has worked in Flipkart's favor, giving them a strong competitive position, I happen to be of the opinion that if major foreign retailers were allowed to come and do business in India, they would make solid investments in improving the logistics, supply chain, as well as increase the overall TAM for e-commerce.

Ultimately, Flipkart and other Indian retailers would benefit tremendously if India's consumers got more used to buying products online, without the need for sand in the gear like cash-on-delivery, having to build their own delivery service, etc. If, for example, hundreds of e-commerce businesses were doing billions of dollars of business, strong logistics companies would also get built with robust financing and growth.

And finally, Internet adoption itself has been slow. China's Internet population has surged to 564 million (75% on mobile). India is at less than 1/10th the number. The e-commerce number can only grow fast if the Internet penetration grows sufficiently fast.

Recently, a couple of exciting things have happened. Amazon responded to the Flipkart financing announcement saying that they would invest $2 billion in the Indian market.

Also, the election of Narendra Modi as India's prime minister is likely to ease the protection for the retail sector, opening the market up further.

All this should accelerate the market, offering strong opportunities for growth, and new e-commerce companies to be created.

# Interview with Sachin Bansal, Flipkart

*Flipkart is India's flagship e-commerce success story. This interview is a conversation with Sachin Bansal, the architect of that success, on how he and his partner Binny got started. At the time of publication, Flipkart has raised its most recent round of financing at a $7 billion valuation.*

**Sramana Mitra: Sachin, let's begin by exploring the genesis of your story. What is your background?**

**Sachin Bansal:** I am originally from Chandigarh, which is the capital of Punjab. My business partner, Binny, is also from Chandigarh. We are not related in any way, it just happens to be a coincidence that we are now working on Flipkart together. We both grew up in Chandigarh and went to the same schools yet did not know each other well. I went to the Indian Institute of Technology in Delhi, where I studied computer science, and that is where I really got to know Binny because he was studying computer science as well.

We graduated from IIT in 2005, and we took different jobs in Bangalore. I joined a company called Techspan. Our paths converged again in 2006 when we both joined Amazon.com India. Amazon was building Amazon Web Services ,which is very big now. We built things like Amazon S3. Their services have powered more than half of the startups in the United States.

**Sramana Mitra: When did you begin thinking about doing your own startup, and was your original concept Flipkart?**

**Sachin Bansal:** We started thinking about that in the middle of 2007. That was driven by the fact that everybody we knew in Bangalore was working hard building great technologies, but they were building them for U.S. companies. We could not relate to that. Amazon is a great business, but as users we could not relate. Benny and I decided to start something on our own and see how it went.

**Sramana Mitra: You wanted to build a company that catered to the Indian market?**

**Sachin Bansal:** Yes. We wanted to have customers we could relate to. We thought about our parents, friends, and cousins. We wanted to build something that they could use.

**Sramana Mitra: Once you had decided what type of company you wanted to build, what path did you take to build it?**

**Sachin Bansal:** We both approached the problem from a typical software engineering mentality. We felt we could write some code and make a million dollars. We did not want to make something that requires a lot of running around. We wanted to write some code and make a successful company, and we felt we could do that with a comparative shopping engine.

**Sramana Mitra: Why did you decide to write a comparative shopping engine?**

**Sachin Bansal:** They were a big thing in the U.S. but there wasn't any in India. We started doing some market research. We found that there were almost no other sites to compare against. Rearden Commerce was the only company that had any real offerings in India, but it was not really doing a good job. We concluded that comparative shopping in India would probably be a bad thing because there was no user market.

**Sramana Mitra: It could definitely have been a sign that the market was immature.**

**Sachin Bansal:** Exactly. That is when we decided to just build an e-commerce company. It was just two people who knew nothing about business starting a business out of their homes. We were good only at writing code and we had a basic idea of how provide a customer experience. We had limited capital. We had to figure out if two guys sitting at home could do a better job than a whole team of engineers in a well-funded startup. We were very optimistic and thought we could. We both quit our jobs in September and launched the site in October 2007.

**Sramana Mitra: When you launched your e-commerce site, what were you selling?**

**Sachin Bansal:** We were selling books online. We had searched for product categories to focus on, and books came out as a very strong category for a small business like ours. The cost of setting up an online bookstore is lower, and the risk of products getting lost in the mail is lower as books do not cost as much as other items such as cameras. Books don't get damaged easily in transit. Books are also a very high margin business with the benefit of negative working capital. Finally, they are not very expensive, so the amount of money a customer has to spend to try out your service one time is very minimal.

**Sramana Mitra: Explain how it is a negative capital working business. How did you source the inventory, and what were the terms?**

**Sachin Bansal:** We spoke with a lot of book suppliers in Bangalore. They were distributors who had been supplying inventory to bookstores throughout the area. We approached them and explained that we were a small company and asked them if they would be willing to work with us. The first time they all said no. They had two people like us coming to them almost every day and asking the same types of questions. They could not differentiate which offers were serious and which ones were not.

We re-approached them and demonstrated that we were indeed good with technology. They had also heard that before. We then asked them to simply tell us their terms. We managed to get deals with two suppliers out of 25 in the city. We just started with them.

The terms required us to pay in cash every time we placed an order, and that we had to go to their warehouses to pick up our orders. In the end we did most of the heavy lifting because we were the new faces to the suppliers.

**Sramana Mitra: How much money did you put into acquiring inventory to sell?**

**Sachin Bansal:** They had computer systems which maintained inventory of their stock. We received a download of that every day.

**Sramana Mitra: So you were taking orders online and then going to the suppliers and fulfilling orders from their warehouses?**

**Sachin Bansal:** We would just pick the books up at their warehouse, but we had to take them to our place to pack and ship them.

**Sramana Mitra: In terms of working capital, however, you did not have to buy aninitial inventory.**

**Sachin Bansal:** If we had to buy that inventory it would have taken a lot of working capital.

**Sramana Mitra: Were you able to get the entire inventory of both suppliers listed on the Flipkart website?**

**Sachin Bansal:** Yes.

**Sramana Mitra: That is very resourceful maneuvering and a good example for Indian e-commerce. How did you acquire customers for the front end of the website?**

**Sachin Bansal: Customer acquisition** was a challenge. We did not have a clue what we were doing there. At that time our only philosophy was to provide good customer service to entice customers to return, and that did start happening, but growth was slow. We studied other website around the world and a big thing that came out was the need for us to solve SEO. Any online business has to solve that to be successful.

We taught ourselves how to do SEO, and we learned Google AdWords from scratch. We were able to drive a lot more traffic to our site. A lot of people just continued, but some customers did make a purchase and tried out the service because our costs were so low. Once they tried us out, they continued to use us.

**Sramana Mitra: How did the business ramp up in terms of sales?**

**Sachin Bansal:** The first three months were very tough because we would sell only about five books a day. After the first three months business started picking up because of word-of-mouth advertising. We hit our breakeven point in six months. It was still just the two of us, but we were still working out of the house so that is when we finally found ourselves and office. We also hired our first two employees. One job was to handle the operations and to pick up the books so that we did not have to do it ourselves every day. The other handled marketing initiatives. Both are still with us today.

**Sramana Mitra: What was your 2008 and 2009 revenue?**

**Sachin Bansal:** Our revenue in March of 2008 was quite low. Our March 2009 revenue was about 2.5 crore (~$560,230).

**Sramana Mitra: Let's fast forward to March 2009. How have the relationship with the distributors and the operational mechanics of your business changed?**

**Sachin Bansal:** We actually opened another distribution center in Dehli. To our surprise, almost every distributor in India knew about us, so it was not hard to make a new relationship in Dehli. We had multiple suppliers in Bangalore and had just finalized some arrangements with international suppliers. We were a well-known company throughout India and were regarded by many as the best online bookstore in India. Today we work with more than 500 suppliers and have operations in five cities, with distribution centers in Bangalore, Delhi, Bombay, and Calcutta.

**Sramana Mitra: It sounds like you were a well-known brand throughout India and had become part of the book distributors' [network] as a high-volume retailer.**

**Sachin Bansal:** We were definitely a well-known brand, and we were receiving the best terms the distributors could offer us. Today we receive better terms than almost every other bookseller in India.

**Sramana Mitra: How does that industry work, and how were you able to improve your terms?**

**Sachin Bansal:** We started with 35% margins on the manufacturer's recommended price (MRP) in 2007. Today, we are able to get anywhere from 40% to 60% margins based on discounts from suppliers. We started by paying for all items with cash in advance. Today, we enjoy a credit line of three to six months.

**Sramana Mitra: In March 2009 you had about $560,000. How did the numbers come up in March 2010?**

**Sachin Bansal:** In March 2010 we did about $6.76 million.

**Sramana Mitra: How do you compare with the major bookstore chains in India?**

**Sachin Bansal:** Our numbers today are comparable to theirs. We sell more than $1.128 million worth of books a month. We are all in the same ballpark in terms of volume. I don't know the major bookstore numbers exactly, but our common distributors tell us that we are a bigger buyer than they are.

**Sramana Mitra: Tell me more about your international strategy. You are the only retailer in India that carries the international versions of my books.**

**Sachin Bansal:** We found that dealing with international suppliers was much easier than dealing with Indian suppliers. International suppliers are much more organized, they are larger, all of their systems are automated, and they use a lot of technology in their operations. They are extremely predictable. We signed our first international deal with Ingram Books in 2008. Today we work with three U.S. suppliers and two suppliers in the UK.

**Sramana Mitra: What were your terms like with international suppliers?**

**Sachin Bansal:** That has also improved a lot. We started with a three-day credit line, and now we have the best credit lines they offer. I cannot disclose the discounts we receive from them, but our discount terms have improved over time.

**Sramana Mitra: Internationally, the book industry is going through huge changes. Now that you have years of experience in the book industry, what are you hearing in terms of dealing with e-books and e-readers? Amazon expects that e-books will overtake paper books in the near future.**

**Sachin Bansal:** I have been following that, but as I am focused on India I follow that news in terms of the Indian market. India is slower moving with e-books. It would take some time for India to use digital in the way the rest of the world does. The majority of Indians are not very tech savvy.

**Sramana Mitra: The infrastructure does not exist. There is no ubiquitous pile of broadband like there is in the United States.**

**Sachin Bansal:** That is one challenge that India faces. The cost of the devices are also too high for the Indian market. A book that is $30 in the United States will be distributed in India at $6 to $7 as a paperback.

**Sramana Mitra: That is one of the reasons that I chose not do another deals with Hachette India, which published my first two books. I did not want to play that game. I produce high-quality content, and I want**

**readers to pay for it. I am not willing to discount the price of the book that much. Hachette offered me a bad deal, so I turned it down. They were very angry about that.**

**Sachin Bansal:** The per-capita income in India justifies the different book prices in India.

**Sramana Mitra: The people who buy my books are making money. The software and technology industry employees in India make enough money to buy my book.**

**Sachin Bansal:** It is a question of demographics, because those industries do get higher pay. If the target market is the entire populace, then it makes sense to price it lower. If the target market is one like yours, then there should be different considerations. There are other authors who are priced the same in India as they are in other parts of the world.

**Sramana Mitra: I did not know the book business, so I played the game for the first two books. Once I learned the business, I changed the way I played the game.**

**Sachin Bansal:** We are more than happy to sell your books in India!

**Sramana Mitra: Let's talk more about e-commerce in India. How has the ecosystem and market evolved in India when it comes to e-commerce adoption? How have the macroeconomics changed?**

**Sachin Bansal:** When we first started we met with a lot of VCs. They all told us that India did not have enough buyers online to support e-commerce companies and that we should wait for buyers to come online. We just could not understand how VCs expected buyers to come online if there was nobody willing to sell to them. In my mind, the issue with Indian e-commerce is for the sellers to become better. If you try to copy a model from China, South America, or the U.S. you will find it does not work.

**Sramana Mitra: What do you think is different about the Indian consumer as far as e-commerce is concerned?**

**Sachin Bansal:** The main difference is trust. Indian consumers are more cautious buying online. They were burned a lot when the first companies came out seven years ago. Building a service which people can trust and enjoy is very important. It is not like opening a street shop. With e-commerce you are asking the consumer to trust you with their money before they even see the goods. That has not traditional in India.

**Sramana Mitra: What you are describing happened in the U.S. in the mid-1990s when Amazon.com started. The notion of giving a credit card to a website was foreign to the consumer, but now it is normal.**

**Sachin Bansal:** Yet the U.S. had an advantage because e-commerce is an extension of mail order. That was a huge industry. People were OK sending money knowing they would receive a product. The mail order industry does not exist in India and people do not have a lot of money to spend, so they buy very cautiously.

**Sramana Mitra: At this point, India has developed a digitally savvy consumer base which is very affluent. How will this impact the future of Flipkart?**

**Sachin Bansal:** I expect that people will adopt e-books, but at a rather slow pace. The digitally savvy consumer base may have money, but most of them have the same background as ordinary Indians and have kept some of that mentality. They are misers.They want reassurance that if they give their money to a company, they will either get the product or receive their [money] back. E-books make for a very quick purchase cycle, so that helps, but the price of the devices must drop.

**Sramana Mitra: What is the size of the e-commerce market in India? How many consumers are buying and selling online?**

**Sachin Bansal:** It is still a small population. I do have a lot of hope, however, because travel and education are both very strong online markets in India. It is estimated that in the past year 2 million to 3 million people have transacted online in India.

**Sramana Mitra: Does that include the online travel market?**

**Sachin Bansal:** It does not include that market, and overall it is a rough estimate.

**Sramana Mitra: Based on your customer base and your knowledge of their behavior, what do you think will happen over the next five years?**

**Sachin Bansal:** We see the market doubling in size. As a company, we expect to have a customer base of ten million people.

**Sramana Mitra: How will you attract this customer base? Are you still focusing only on SEO, or are you advertising as well?**

**Sachin Bansal:** We still do not spend a lot of money on marketing. Word of mouth is our strongest method of advertising. We have a very high customer retention rate. Those same customers bring us the best quality new customers, and most of those new customers become repeat customers.

**Sramana Mitra: You have now decided to take venture funding. What was your reasoning for that decision?**

**Sachin Bansal:** We determined that now is the ideal time to capture the market. Most companies have not figured out how to do e-commerce in India, while we have figured out how to do some things right. We want to use this funding to build a long-term business.

Our plan is to use the money we raised from the VCs to invest in growth. We need to expand our infrastructure to support e-commerce. We also need to improve our physical warehouses throughout India.

**Sramana Mitra: What has been your experience with the logistics infrastructure in India?**

**Sachin Bansal:** The delivery infrastructure is not in good shape, and it is the largest challenge we face today. We are working with all delivery companies in India, and we are working to help them become better. We do not know about logistics, but we do know about customer service. We provide input to our delivery companies about their performance and how it impacts our customer experience. Nobody has ever thought about customer experience in India.

**Sramana Mitra: Does your customer base access Flipkart only through desktops and laptops?**

**Sachin Bansal:** We have mobile commerce, but it has very little traction.

We believe strongly in working with great people. We are now ramping up the company, have 300 employees, and will have 1,000 within a year.

**Sramana Mitra: What do you need 1,000 workers for?**

**Sachin Bansal:** Our employees are divided across many areas. We have our management team, customer support, software engineering, salespeople, and warehouse operations.

**Sramana Mitra: How large is your software team?**

**Sachin Bansal:** We have a small team, but it will expand as we grow and need support. We are a technology company at the core. We try to solve as many problems as possible with technology. We have optimized our warehouse operations and our customer support by using technology.

**Sramana Mitra: Are you reinventing customer support and warehouse systems rather than buying off-the-shelf systems?**

**Sachin Bansal:** We are not buying commercial systems. We were not able to find any that met our requirements. Developing them ourselves gave us flexibility. As a company we are learning 10 or more new things a day. By developing our solutions, we have the flexibility to adapt our solutions to our needs.

**Sramana Mitra: You are illustrating a very Indian mentality by reinventing the wheel at every level. There is one philosophy of management that wants you to build everything yourselves, and another philosophy that wants you to focus on what you do well. In your case, you do Indian e-commerce very well. You should use the ecosystem for the rest of your needs.**

**Sachin Bansal:** The more we have looked, the more we have not found an ecosystem in India for e-commerce operations.

**Sramana Mitra: There is an international ecosystem. When you play at the high level of the game, you should be purchasing those systems from international players.**

**Sachin Bansal:** Indian consumers are different and have needs unlike those of any other consumers in the world. The systems that work for other countries do not work in India.

**Sramana Mitra: You can try and sell me that ideology, but right now I am not buying it. Indian companies believe they have to do everything themselves.**

**Sachin Bansal:** Our understanding is that the systems that are available on the market will not do what we want them to do. We want our growth flexibility incorporated into our systems.

**Sramana Mitra: What does your competitive landscape look like today?**

**Sachin Bansal:** Our brand is well known today. A bunch of other companies have started after us, but we are the largest, especially in books.

**Sramana Mitra: What other segments of e-commerce are maturing well in India?**

**Sachin Bansal:** Electronics such as mobile phones. The market is still segmented, and no clear dominant player has emerged yet. We hope to compete there as well. Some people are trying to sell apparel online, but that will be very hard to do in India.

**Sramana Mitra: What percentage of the book market in India have you been able to capture?**

**Sachin Bansal:** The online market is about 10% of what the established retail book market is. We have more than half of the online book market. The remaining online book market is segmented among very small e-commerce companies.

**Sramana Mitra: This is a great story, and I hope you go much further. Good luck!**

Note: Flipkart has raised $1.75 billion in funding as of mid-2014. The company has had to build a full logistics infrastructure from scratch that not only delivers merchandise to consumers, but also handles cash-on-delivery. India, at this point, remains extremely weak on the logistics infrastructure, and no company like UPS exists in the market. Flipkart is, effectively, building this network, and sits at an advantageous point to be able to operate across various e-commerce categories because of it. They recently acquired Myntra, the leader in clothing e-commerce in India, and it would be safe to assume that they will acquire other category leaders in due course. Flipkart aims to be India's first $100 billion e-commerce company.

# Interview with Mithun Sacheti, CaratLane

*Mithun Sacheti is the founder of CaratLane, an online jeweler in India and one of the country's leading e-commerce companies. Mithun grew up in the jewelry industry and prior to founding CaratLane, he opened new stores for his family business throughout the southern regions of the country. He has studied gemology in California and Bombay. This is a concept arbitrage of Blue Nile, a highly successful e-commerce venture in America that went on to have a very successful life as a public company based in Seattle. Mithun obviously knew the jewelry trade well, and CaratLane is built on that deep domain knowledge.*

**Sramana Mitra: Mithun, let's start at the beginning of your story. What is your journey that leads up to CaratLane?**

**Mithun Sacheti:** My family has been in entrepreneurship for many generations. My father moved to Bombay from Rajasthan to set up his own jewelry stores. I was born in Bombay in 1978 and I did my education there before moving to California to study gemology engineering and manufacturing. When I moved back, the most logical thing for me was to start something allied to the jewelry industry. I grew up in that industry and my education was in that industry.

I moved to Chennai and decided to build a store. In 2000 I started to build out the first store under my father's brand name. This was an extension of the family business, and I was the first one to move to the south. That had always been considered a different territory because the language and everything else was different. That is where jewelry and entrepreneurship started for me.

I built up that store for a couple of years. I found that 2001 was not the greatest year. The world was in a recession, so it was not a great time to be starting a business. I sustained it for three years by selling to everyone who walked through the door. I ran a three-man operation back then. Slowly but surely, we grew to the point where in 2004 we added another floor to our store. By 2005, we were one of the best stores in the city. Anyone who was looking for fine jewelry knew about us.

**Sramana Mitra: What as the revenue level at that point?**

**Mithun Sacheti:** In 2004 we were around $7 million or $8 million from the store I was managing. At that point I also started looking at doing something new, so I opened another store in the south of India. It was an attempt to build a professional store. In India, everyone was used to the family concept when it came to jewelry stores, where the owners sat in the store to sell everything themselves. I was trying to break that model. I built the second store like a little palace since space was not as expensive. It was a concept store and came out very beautiful. It is one of the best stores in the country today.

One thing that kept sticking with me was my past experiences during my studies in California. I used to go to downtown L.A., where the diamond industry was based. I would pick up loose diamonds I knew from family connections. I would then bring those to retail stores in San Diego for them to sell on Saturday and Sunday. The wholesale business was shut in those days. I was basically just transferring inventory from L.A. to a retail store and hoping that something would click. The first year went very well, but in 1999 we saw Blue Nile come in, which really marginalized prices. The money I made from that became my pocket money. I also saw the power of Blue Nile.

**Sramana Mitra: I have followed Blue Nile for a long time. I have a friend who was an early investor there.**

**Mithun Sacheti:** What I saw from Blue Nile stuck with me for a long time. Things happen in different industries that transform the entire industry. If you really look at our industry, you will see that jewelers have a limited value addition. I came to believe that if you could create the right tools online to educate people so they do not have to rely on blind trust, a business model similar to Blue Nile could be re-created in India.

At the stores we had limited inventory, but we tried to sell a lot of volume by educating people on the specifications. That helped us sell very well. My 2007 revenues were around $14 million using those techniques. I realized that people were willing to put some time into understanding diamonds so they could make better choices. With that in mind, I went to my friend and co-founder and told him that I felt there was a business opportunity here.

My co-founder was a client at the store. He had a strong technology background. I had known him for several years, and I had socialized the idea with him for a few years. He had started a technology business and bought out his investors in 2004. He thought the idea was interesting, but he wanted to see a proof of concept. It just so happened that one of his friends came down from California and wanted to buy some jewelry, so he took him to my store.

One thing led to another, and the three of us had a conversation and his friend ended up telling us the specifications of the diamond he was looking for. Both of us talked about the specifications and explained what was available at our store. He was able to compare our prices with the prices available to him in India because we used the same specifications. It took him 30 minutes to make up his mind in the store, and he placed an order for a $55,000 diamond. That was actually normal business for the store. However, my co-founder saw this entire process. He realized that this client did not see the actual diamond and bought it based solely on the specifications. He understood certifications and he was willing to spend $55,000 on a product because of the certifications. That gave my co-founder a lot more confidence in our business concept.

After that, our discussions got a lot more serious. We incorporated a business in 2007. We built an aggregation model where we could aggregate inventory from all over the world to enable people to list their solitaires with us. We launched in October 2008.

**Sramana Mitra: I know the Blue Nile model well, and I am smiling as I listen to your story. Imagine what kind of uphill battle Blue Nile had when they decided they wanted to sell online.**

**Mithun Sacheti:** Blue Nile was not the first to sell diamonds online, but they were the first to do it and cut the price. That was the big step they did right. Everyone else before them did the aggregation, but they did not cut prices.

**Sramana Mitra: They also positioned their site for men. They had an understanding of how business happens in the diamond industry.**

**Mithun Sacheti:** And their marketing was great. The real kick was to get the pricing factor right.

**Sramana Mitra: I don't think they did aggregation. They did a pure retail model of buying and reselling diamonds.**

**Mithun Sacheti:** Aggregation comes in the form of buying after you have a sale. BlueNile started off with 50,000 diamonds listed on their site. They definitely did not own all 50,000 diamonds. We had about 45,000 diamonds on our site when we launched. When a consumer comes to our site and likes a diamond based on specifications and decides to purchase the diamond, we can then backorder the diamond.

**Sramana Mitra: So, the business model is to build supply relationships for a reliable supply of diamonds, and you then purchase the diamond after the order is placed, right?**

**Mithun Sacheti:** Absolutely. This is the model that everyone uses now. The major consideration now is, how large can you become? How deep into the pipeline of diamonds can you go? The closer you get to the cutter, the better.

**Sramana Mitra: How did you go about developing your diamond aggregation pipeline? Did you primarily rely on your family's history and contacts?**

**Mithun Sacheti:** Aggregating diamond suppliers in India alone was not enough. We needed to be everywhere. We had to go deep and get inventory from Hong Kong, Israel, New York, Antwerp, and Bombay. Those were the biggest trading centers around the world, so if we were going to really be a player we had to be in all of those areas. Antwerp was the last one that we addressed because there were a lot of logistic issues there. Even today Antwerp is our single biggest challenge.

We had to visit every one of these locations, explain our business model, and convince them to work with us. The American guys understood us very quickly because they knew Blue Nile. The immediately asked us if we were going to be the Indian Blue Nile, and we told them we certainly hoped so. Their problem was that if they had Indian inventory, there was a slight problem because that was the pipeline that I was buying from anyway. There was a set of challenges like that everywhere we went.

We had to spend a lot of time talking about how to plan diamond inventory and how to plan real-time inventory. In many cases we provided them with tools to help them manage their real-time inventory.

**Sramana Mitra: Did you have to make minimum business commitments?**

**Mithun Sacheti:** We did make those commitments when it came to vendors we really valued and whom we really wanted in our system.

**Sramana Mitra: How much of this did you need to have in place in 2008 when you launched?**

**Mithun Sacheti:** We had 40,000 items in place when we launched. We had our solitaires in place. We did not have very many mounts in place at that time. Jewelry was not in place because we were very focused on the solitaire aspect of the business.

**Sramana Mitra: Were you just selling solitaires and not the settings?**

**Mithun Sacheti:** We did not have the level of settings we wanted simply because we focused so much on the solitaire inventory. We may have had 20 mounts for people to choose from, whereas today we have 200 or more.

**Sramana Mitra: You went to market with a minimal viable business option, which is a great starting point.**

**Mithun Sacheti:** Starting in the market is definitely better than sitting at home. We had already spent 14 months getting this started. There is a lot that goes into the back end. There are some very large, rigid vendors that require us to follow their guidelines. We had to adjust to work under their system. They key to our entire operation was to reach the cutters. We went very deep after that market. Our goal was to aggregate from levels that were so close to the cutters we could expect them to not have IT solutions.

**Sramana Mitra: What kind of capital requirements did you have to get the business launched?**

**Mithun Sacheti:** We budgeted $500,000 between the two of us. We were determined to launch the business once we had spent that amount regardless of where we were, and determined that once we had spent that amount, we would sit down and plan our next steps. That was the amount of money we were willing to risk. However, at the point of launching the business in 2008 we had spent $100,000.

**Sramana Mitra: Where did you get the original $500,000?**

**Mithun Sacheti:** It was from my savings. My brother and I both invested.

**Sramana Mitra: What was your co-founder's role?**

**Mithun Sacheti:** He had a technology company, and he put money into the business as well. At the point of launching the business, we had both spent portions of our equity investments. He promptly agreed to invest in the business.

**Sramana Mitra: Was it a 50/50 partnership?**

**Mithun Sacheti:** No, my family is the majority shareholder of the business.

**Sramana Mitra: What happened after your initial launch in 2008? You mentioned you had 40,000 solitaires and a few settings. What came next?**

**Mithun Sacheti:** Two weeks before we launched, Lehman Brothers collapsed. Nobody was willing to listen to us at that point. We sat at a point without selling a single diamond. We really struggled in terms of getting ourselves out there and heard. Luckily in October, a major TV station carried a story on us saying that it was amazing that anyone would buy solitaires online. That story actually started getting us traction. We relied heavily on PR for those three or four months. We were also perfecting the product as we moved through that time.

We started getting 150,000 visitors a day, but we were still having no conversions. We had one solitaire sale in October. A man in Japan was purchasing something for his mother in Delhi, and we had a very difficult time getting that transaction pushed through the payment gateway. It was a high-value transaction from an overseas card. That transaction set off every possible red flag that a credit card fraud department could imagine.

**Sramana Mitra: How long was it before you started earning money?**

**Mithun Sacheti:** In December things started to turn for us. We started adding more jewelry. We needed to have smaller value products, so we focused on that. At the same time we built out an exhaustive education system. People learned a lot more about what we were doing. That yielded benefits for us, and we began to see weekly transaction in the solitaire business. Shortly after that we were doing a couple of transactions per day.

**Sramana Mitra: What kind of revenue did that add up to?**

**Mithun Sacheti:** We had a couple of interesting things occur. Back in the day, people who wanted to buy higher value would look at us. We ended March just shy of $1 million in revenue. The interesting thing is that $200,000 came from one particular transaction. There were significant outliers.

**Sramana Mitra: What was the $200,000 transaction?**

**Mithun Sacheti:** A customer bought a pair of three-carat diamonds. She knew exactly what she was looking for. She knew what the retail price was. Our early adopters were people who knew exactly what they wanted and knew exactly what the retail price was for their solitaire.

**Sramana Mitra: Are your customers all from India?**

**Mithun Sacheti:** Yes, we sell only in India.

**Sramana Mitra: By 2009 you had started going deeper into the supply chain and were reaching cutters directly. How did 2009 end for your business?**

**Mithun Sacheti:** We ended at around $3 million in revenue. We had around 90,000 diamonds listed at that point. We had really developed our international pipeline by then. If at any point the rupee got strong, we could buy the same diamond out of America for a lower cost. Our system was dynamic, whereas in an unstable market diamond pricing moves a lot. Unstable markets force local retailers without a huge pipeline to raise their costs dramatically, which was something we were insulated from.

**Sramana Mitra: Did you have an IT system to manage your pipeline?**

**Mithun Sacheti:** Yes. Our entire back end process was automated. There was no way we could have done that manually; we would have made a lot of mistakes. We were very conscious of the fact that we had to stay ahead of the game when it came to pricing. A competitor could come online any day to challenge us, so we always had to go deeper and deeper.

**Sramana Mitra: Listening to your story, it sounds like price is the major differentiator.**

**Mithun Sacheti:** If people know what they are looking for, price really is the only thing we can do. Our focus was price and trust. We did second level certifications to validate that a diamond that was shipped to us truly did match the certificate on which it was shipped. That was more than any jewelry store could provide.

**Sramana Mitra: What did you do to reach the cutters?**

**Mithun Sacheti:** We encouraged them to sell directly to consumers. They were always stuck selling to wholesalers, and as a result they would not get paid for 90 days. If they wanted to get paid in cash they were squeezed for that as well. Our pitch to them was that if they sold directly to consumers that they could get paid early enough at a price that was favorable to them. We demonstrated to them that most of the wholesalers they were dealing with were already selling through us anyways. We had to work with each cutter individually to convince them to come on board.

**Sramana Mitra: What cutter market are we talking about, Bombay?**

**Mithun Sacheti:** Yes, Bombay. There are around 150 companies that do diamond cutting. If you have only 20 vendors and you are selling $100 million, then the vendors can use their exclusivity against them. We realized that in the long run we had to go deeper and get as broad of a platform as possible. Today we have about 350 cutters working for us directly globally.

**Sramana Mitra: How do the cutters align geographically?**

**Mithun Sacheti:** For every 10 diamond cutters in India, there is one in Hong Kong, one in New York, one in Antwerp, and two in Israel. In India they cut the .3 and .4 carat diamonds. The other sites cut larger diamonds, so they do not need as many employees.

**Sramana Mitra: How do your diamond prices compare internationally?**

**Mithun Sacheti:** We are one of the best priced sources for diamonds globally. We know that long-term price alone is not a final strategy, especially in a luxury product. Ultimately, the diamond is a gift for a spouse or fiancée. You want to make sure the person who is buying is getting top quality. We don't advertise that we have the cheapest diamonds, we advertise that we have the best price for the quality. We talk about having the widest choice possible. You can see other people's inventory on our site as well. Pricing gets competitive when you include as many vendors as possible. In the back end our vendors can see what others are pricing their diamonds for, which helps them keep their pricing competitive but also consistent.

**Sramana Mitra: Essentially you are walking a tightrope with your messaging. People need to know that you have the best price, but they can't be perceived as being cheap for shopping at CaratLane. Is that fair?**

**Mithun Sacheti:** Yes. I think we will hit the best price solely because of the number of vendors we have. That is why we can [send a] message on education and quality then talk about our reduced pricing due to our efficiency as a company. The product maintains its perception of quality and status this way.

**Sramana Mitra: How has the diamond market evolved in India between October 2008 and October 2012?**

**Mithun Sacheti:** Let me break the business into two parts, solitaires and jewelry. When it comes to solitaires, there are six other companies that play in this field right now. They have gone to market at five times or seven times the level of where we were in 2009.

If you look at the jewelry side of the business, in 2010 there were five players in this space. This year we have seen another 15 companies join it. Everyone sees opportunities in jewelry. This is an easier space to enter than the solitaire space because there are so many roadblocks over there. The supply relationships and value propositions are more difficult in solitaires.

**Sramana Mitra: How many consumers are buying solitaires online?**

**Mithun Sacheti:** I don't have data available outside of our business. Last year we sold 3,000 solitaires. Some people buy pairs, but that still represents around 2,000 customers.

**Sramana Mitra: So, the total number of people buying diamonds online is probably fewer than 5,000.**

**Mithun Sacheti:** I don't think that all of our competitors combined sell more than 1,000 solitaires.

**Sramana Mitra: How about the jewelry side?**

**Mithun Sacheti:** That is very difficult to estimate. There are a lot of Indian jewelry companies online, and we don't know their numbers. EBay claims to sell a piece of jewelry every four minutes, but they sell jewelry that we would not even classify. We had about 12,000 customers purchase jewelry online last year. I would assume there are around 75,000 to 100,000 people who are customers in the space.

**Sramana Mitra: No matter how you look at it, there is a lot of headroom in this marketplace.**

**Mithun Sacheti:** Absolutely. The potential is exciting.

**Sramana Mitra: I assume you use cash on delivery?**

**Mithun Sacheti:** We just started. It was one of the toughest things we have had to figure out. Jewelry is risky to do cash on delivery. Until now we did credit cards sales. We just started cash on delivery a month back, and we do not do cash on delivery for diamonds.

**Sramana Mitra: How much capital has gone into this company? You spent $100,000 to launch. Did you have to add more capital?**

**Mithun Sacheti:** We did. We had to put in some capital to launch and then periodically added more. In 2011 we got funded by Tiger Global.

**Sramana Mitra: How much funding did you receive from your family?**

**Mithun Sacheti:** We put in about $500,000. We have a positive cashflow model; we were operating on our positive cashflow. We were really running on fumes for about a year.

**Sramana Mitra: How much revenue were you bringing in by the time you raised money from Tiger Global?**

**Mithun Sacheti:** We were at $5 million in revenue. We raised $6 million from Tiger.

**Sramana Mitra: What is your revenue forecast this year?**

**Mithun Sacheti:** We closed in March 2012 at close to $18 million.

**Sramana Mitra: You were already a profitable company when you raised money. Where did you put the funding?**

**Mithun Sacheti:** We were not profitable. We kept investing to keep growing. We set up a large manufacturing facility so that we could provide just-in-time manufacturing for the product that we make. That is something that we invested heavily in, and we built that in Chennai.

**Sramana Mitra: You have built a company with huge potential. What is your assessment of what is happening in India with the family businesses that have multigenerational wealth, yet the modern generation of these families are looking at different types of businesses? To me it seems like a trend. Do you think it is?**

**Mithun Sacheti:** I think that there is a trend. When I started in 2007, there were hardly any Internet companies around. My brother tried to build a website in 2001. He was too far ahead of his time. He wanted to focus on gemstones instead of diamonds. When the crash happened, it seemed that websites were a bad thing to do.

Today there are a lot of e-commerce portals that have received several rounds of funding. I get a call every day on my cell phone from somebody who has an e-commerce idea he or she wants to build out. There might not be a genuine need for it in the market, but someone thinks there is enough demand to build a business. All of them are people whose families have great businesses.

**Sramana Mitra: The advantage of coming out of family businesses is the availability of seed capital. India still has a tremendous seed capital problem.**

**Mithun Sacheti:** A few years ago that was the case. Today almost every city has an angel organization. I would imagine they are looking for ideas now.

**Sramana Mitra: I work with all of the angel groups. I know that space intimately, and seed capital remains an acute problem. Angels have started behaving like VCs. Who is going to fund the proof of concept if**

**you have not the ability to fund the proof of concept yourself?**

**Mithun Sacheti:** That is very true. Your insight there is invaluable. The angels are behaving like VCs. They are walking in after the concept has been proven. A lot of people I meet think getting funded is the goal. That is not the goal. Making the company successful is the goal.

**Sramana Mitra: In 1M/1M we say that entrepreneurship equals customers, revenue and profit. Financing is optional. There is a tremendous misconception in the world that entrepreneurship equals financing.**

**Mithun Sacheti:** This myth needs to get cleared in the media. The moment you get financed, the media wants to write about you.

**Sramana Mitra: On this topic the media is supremely dumb.**

**Mithun Sacheti:** For me, it was easier to get my second round funding story out there than it was to get press on the launch of an unbelievable product.

**Sramana Mitra: If you told the media that you have achieved $18 million in revenue, they would not understand the significance. They understand the significance of a $5 million financing. It is ridiculous.**

**Mithun Sacheti:** We are not doing couponing. We are bringing real value. We use technology as an enabler, not an end game. E-commerce is another way of selling diamonds. My product is diamonds. I can create stores and sell diamonds there, too.

**Sramana Mitra: You can proliferate and create one brand that encompasses retail and e-commerce. That is how you grow the company.**

**Mithun Sacheti:** We have been toying with something that will take us tenfold from where we are. I am excited about that, and it is based on the concepts we are talking about.

**Sramana Mitra: Good luck. This is a great story; I enjoyed it very much.**

# E-Commerce in Latin America

There is a market of 500 million people – nearly 8.6% of the world's population – that the business media all too often neglects, serving up story after story on China and India. Forgotten is all of Latin America.

Between 2000 and 2007, the number of Internet users in Latin America grew from 18.1 million to 122.4 million, a compounded annual growth rate of 32% compared with only 12% in North America during the same period. Average penetration across Latin America was approximately 21.5%, compared to 71.4% for the US. Even with such low penetration, Latin America's Internet population represented close to 10% of the world's Internet users.

Fast forward to 2014, numbers have exploded, touching 300 million. Analysts forecast 393 million users in 2017.

Not surprisingly, Latin America is developing its own collection of Internet stars. One of those is a unicorn: MercadoLibre, which translates to "free market", is an online marketplace that facilitates the buying and selling of computers, electronics, photography equipment, household items, even cars. Stanford Business School graduate Marcos Galperin started it in 1999 in Buenos Aires, Argentina. MercadoLibre invited me to visit the company in the autumn of 2007 and advise them on strategy. What I learned impressed me.

Although MercadoLibre had a rocky start, the company is now delivering stellar results, with a market cap close to $5 billion. The moral of this story: It takes patience to build a great company, even in Internet time.

In its original incarnation, the company had a pure auction platform modeled after eBay. Galperin and friends, despite originally being from Argentina, weren't sure what the Latin American market would tolerate. Sitting around the Stanford University campus in sunny and wired California, they could not possibly have imagined that it would take so long for the Internet – let alone online auctions – to gain adoption in Latin America. Silicon Valley, after all, is a reality-distorting environment that makes us entrepreneurs extrapolate wildly!

Latin America had less than 3% Internet penetration in 1999, and already 40 companies were doing exactly the same thing as MercadoLibre. While MercadoLibre had some venture money and was developing software, they had to wait for customers to materialize. And during that Godot-like wait, many of their competitors went out of business.

Ironically, Galperin believes the dot-com crash actually helped MercadoLibre. "There was no more financing. We were lucky, because we were able to do our second round of financing just after the crash in May 2000, and we closed out a $46 million round." Other companies were short of cash, except for DeRemate, a direct competitor started by some Harvard University graduates. The funding crunch lasted for almost five years. "All of the smaller competitors died away. It helped us tremendously," Galperin recalls.

Even Mercado's backers were skittish and threatened to shut the company down and take back their money. Venture capitalists are not known for their patience. They tend to get really anxious when markets don't develop really quickly. Other entrepreneurs had their doubts, too. Luis Riviera, a native of Venezuela, who later became Chief Executive of Lyris, was asked to join MercadoLibre in 2002. He turned the company down, citing lack of market maturity in Latin America.

But gradually the market itself, once a dream, became a reality. Revenues started to materialize for MercadoLibre. "After the drought between 1999 and 2002, I believe we did $4 million in 2003, and $12 million in 2004. In 2006 we did $52 million," Galperin says. For the year ended Dec. 31, 2007, MercadoLibre's annual revenue increased by 63.5% to $85.1 million.

That was the year the company went public – in the midst of another financial crisis. "We were quite unlucky in that we did our road show in the middle of the subprime crisis," recalls Galperin. "The day we priced, the market broke 400 points. And the day our stock went live was the day the Fed, the European Central Bank and the Bank of Japan, all intervened in the markets and gave liquidity, which was something that had not happened since Sept. 11, 2001." Despite that, the stock performed well.

MercadoLibre has become the No. 1 online marketplace for Latin America. It facilitates the buying and selling of merchandise in the same way eBay and Amazon do. Items range from computers, cameras and MP3 players to furniture and household items, even Toyotas. The business, unlike eBay's auction-based model, is primarily driven by fixed price transactions. In that sense, they are closer to Amazon. MercadoLibre also has an online payment offering a la Paypal called Mercado Pago, which is seeing good adoption and has huge potential to facilitate commerce in the Latin America market.

MercadoLibre has evolved into a strong brand that many people on the street recognize. Its team is well set and stable. Unlike Silicon Valley or other "hot" markets such as India or China, attrition is low, making it easier for the company to bank on the talent base that has been trained and matured on its clock.

Some of MercadoLibre's strength came from simply outliving its local competition. Language and culture, I believe, are substantial barriers to international competitors, as multinationals like Google and Yahoo! have discovered in China. (Even so, eBay had a 20% stake in MercadoLibre – a smart strategy for the US company) The region does not have an active venture capital industry, so competition has continued to be limited. Those factors give MercadoLibre a nice, clean runway to build a dominant Latin American e-commerce business without a lot of interruption.

The moral of this story is that in an emerging market, if entrepreneurs can get in early, and get a group of deep pocket investors to back them with a very long-term view, gigantic companies can be built. The same story is playing out with Flipkart in India. Other geographies that offer such opportunities are Africa, Indonesia, and Russia.

The trouble is, investors seldom have the confidence to bet on a strategy like this, and for entrepreneurs, it is an uphill task to convince them.

# Interview with Marcos Galperin, MercadoLibre

*MercardoLibre is Latin America's flagship e-commerce company.*

*I first heard of MercadoLibre in 2007 when I received a call from the company, inviting me to Buenos Aires to help with their strategic planning. This interview with Marcos Galperin was conducted at the cafeteria of the company's Buenos Aires headquarters, during the lunch break on one of the days during my visit. In the basement of a tall building, the cafeteria was bustling with hundreds of people, all MercadoLibre employees, and we found ourselves a corner to sit down and talk.*

*Over the course of the days I spent with the MercadoLibre team, one thing became obvious to me: Latin America is ripe for an entrepreneurial outbreak akin to what India and China have experienced. In the last seven years, that promise has started to gain momentum.*

**Sramana Mitra: Let's go back to the story before MercadoLibre. Let's start with your background – where did you grow up?**

**Marcos Galperin:** I grew up here in Buenos Aires. When I was 17, I went to college in the US. I studied at the Wharton School at the University of Pennsylvania from 1990 to 1994. When I graduated I came back and worked for an oil company which was the largest oil company in Argentina. I did Finance there for three and a half years. Afterwards I went to do an MBA at Stanford. When I came back I started MercadoLibre.

Actually, I started it when I was at Stanford. I wrote the business plan and contacted investors in a class there. One of my professors put me in touch with one of the founders of a private equity fund; he let me drive him back to the airport after he came to speak to our class. I gave him an abbreviated business plan, and he thought it was great. That is how it all started.

**Sramana Mitra: Your co-founder was also in your Stanford class, yes?**

**Marcos Galperin:** Hernan [Kazah] had accepted a job at a different company which was also a startup, but he agreed to help me out with some marketing ideas. He basically never stopped, and he became my co-founder.

**Sramana Mitra: And your idea at the time was eBay for Latin America?**

**Marcos Galperin:** That is exactly how we thought about it. Through Stanford, we contacted classmates and people at eBay to get a sense of where Latin America was on their radar, to see if it made sense for us to launch something or not.

But all of them spent all of their money doing mass marketing, doing the Pets.com strategy.

**Sramana Mitra: Did you get the sense that eBay was not focused on Latin America? What was the Latin American Internet market at the time? What kind of Internet penetration?**

**Marcos Galperin:** It was very small. There was 3% penetration, roughly. Today it is 20%, so it can still grow a lot. Out of that 3%, e-commerce was probably 10% or less. It was very, very small. One of the things I think we did right, relative to the rest – there were 40 companies doing exactly what we were doing – some of them raised more funds than we did. But all of them spent all of their money doing mass marketing, doing the Pets.com strategy.

We saved our cash and developed our products. From the very beginning, we focused on building a good product and our IT backbone. That is a very big difference between us and everyone else in the region.

**Sramana Mitra: Which other companies were able to raise financing besides you?**

**Marcos Galperin:** There were a couple of others. DeRemate was founded by a Harvard group, so it was a huge rivalry.

**Sramana Mitra: Harvard people do not make good entrepreneurs?**

**Marcos Galperin:** At least these ones didn't. They were very big on spending money and doing PR, but not very good at building their company and building a good platform.

**Sramana Mitra: What was the source of your technical expertise?**

**Marcos Galperin:** The second person to join the team was my cousin. He was the CTO, and had a very technical background. He was with us for a few years and then he stepped out. He groomed our current CTO before he left.

**Sramana Mitra: What were some of the early milestones that gave you the indication that you were starting to be successful?**

**Marcos Galperin:** At the beginning there were not that many!

**Sramana Mitra: Having just 3% Internet penetration must have been very frustrating!**

**Marcos Galperin:** Exactly! We tried to focus more on milestones which were operational but not necessarily revenue. We still remember the first time someone came and paid their bill at the office. We still have the PDF of the scanned check. We tried to focus more on the platform, and expanding to other countries and ensuring we had a team in every country. The business was a very small business in the beginning.

We always have fun reading the eBay story. Checks started arriving to Pierre Omidyarís home because the guy who hosted the site for him told him he was having too much traffic and they would need to start charging Omidyar, so he sent an email [to customers] saying that he would have to start charging because he was being charged. Checks started arriving in such a large quantity that he realized he had a business ñ he actually hired someone just to take care of the checks. In Latin America, that would never have happened! We spent a lot of time waiting for the checks.

But we did two things well. One was to focus more on the platform and less on mass marketing. The other one was to understand the differences between implementing a business model in the States or Europe versus implementing one in Latin America.

**Sramana Mitra: What were some of those key differences?**

**Marcos Galperin:** The way buyers and sellers interact is different. eBay was very big into ensuring buyers and sellers could interact before the transaction. We felt that if we let them interact before the transaction we would never collect a payment. Instead we created a Q&A message board which ended up having very important side benefits. The message board is a great community generating tool. It is a great customer service tool for the seller who only answers questions once. It is great for buyers because you see questions which you perhaps may not have thought to ask, but which will make you feel more comfortable knowing the answer to.

It ended up being great at preventing phishing and fraud schemes to sellers. In the old eBay system, if you could contact the seller then you could solicit information from the seller. eBay eventually disabled the ability to send an email to the seller. Fraud rates are very, very low on our platform and we believe that is one of the reasons why ñ nobody can ever get our sellersí email addresses.

**Sramana Mitra: What was your platform in those early days – an auction platform or a fixed price platform?**

**Marcos Galperin:** Complete auction platform, and today it's a 90% fixed priced platform. Another thing we did different is that we did not like the Buy It Now feature on eBay. We used it as a transition from pure auctions to a fixed priced environment, but very rapidly we took it away and just left two options – auctions or fixed priced. Overwhelmingly, and across different countries, sellers were choosing to use fixed prices for their items, with the exception of used products or items where the market prices were difficult to determine.

**Sramana Mitra: Is it a C2C or a B2C business?**

**Marcos Galperin:** It is mostly B2C, with small businesses. 75% of the items sold are new items and we believe most of them are small businesses which are selling them.

**Sramana Mitra: Do you have any idea as to what percentages of small businesses in South America are using MercadoLibre as a platform to sell?**

**Marcos Galperin:** I cannot give you an accurate answer there.

**Sramana Mitra: It is an interesting metric to look at, since retail is a relatively weakly organized sector in the region.**

**Marcos Galperin:** I think we could get a good estimate of the number of small businesses in a region, and then see what number of sellers we have in a region. That could give us a percentage.

**Sramana Mitra: Your business, the vertical penetration of the business, is it primarily consumer electronics and gadgets?**

**Marcos Galperin:** I would say 50% is consumer practicals – gadgets, computers, photography equipment, etc. The remaining 50% accounts for all other services and sales.

**Sramana Mitra: You also have a strong automotive category.**

**Marcos Galperin:** Car auctions are very strong for us.

**Sramana Mitra: Did the dotcom crash in the United States impact you here?**

**Marcos Galperin:** Yes, because there was no more financing. We were lucky, because we were able to do our second round of financing just after the crash in May of 2000, and we closed out a $46 million round. Nobody else was able to access cash, with the exception of DeRemate – they were able to get more funds. Most companies were not able to get financing for 4-5 years, which gave us a great advantage. All of the smaller competitors died away. It helped us tremendously.

Operationally, before the crash, it was all about building the platform. After the crash, it was about building the business. From 2000 to 2003 is when we grew the most. People here continued to adopt the Internet, the telecoms continued to invest in broadband.

**Sramana Mitra: What was Internet adoption like in 2003?**

**Marcos Galperin:** I do not remember year by year. I think the evolution was somewhere around 10% per year.

**Sramana Mitra: What type of revenues were you seeing in 2003?**

**Marcos Galperin:** I believe we had $4 million in 2003. I would have to check that number, but 2006 was $52 million, and in 2005 we had $28 million.

**Sramana Mitra: You raised $46 million in financing in the middle of 2000! I find that unbelievable.**

**Marcos Galperin:** Exactly. Two years later we only had $2 million in revenue.

**In 2001, we barely managed to avoid one of our major investors shutting down the company.**

**Sramana Mitra: How did the investors feel about that?**

**Marcos Galperin:** In 2001, we barely managed to avoid one of our major investors shutting down the company. The founders still had a good number of shares, so we were able to outvote them.

**Sramana Mitra: How did you manage to keep a good number of shares with a $46 million preferred share investment?**

**Marcos Galperin:** The valuation was quite high.

**Sramana Mitra: No kidding! What was the valuation?**

**Marcos Galperin:** We do not disclose that.

**Sramana Mitra: That is an amazing deal. The investor in that round was a private equity firm, you said.**

**Marcos Galperin:** The lead investor was Goldman Sachs. Others also invested, such as Chase Capital, GE Bank, Banco Santander Centro Hispano, a large bank in Europe and throughout Latin America.

**Sramana Mitra: In 2003 you had $4 million in revenue, and $12 million in 2004. Were the investors starting to warm up to the idea?**

**Marcos Galperin:** Yes, they were wanting us to be profitable as soon as we could, but eBay was a shareholder by then and they believed it was more valuable for us to continue gaining market share and growing our top line rather than focusing on whether we made or lost half a million per year. We agreed with that. We could have become profitable in 2004, but we decided not to. We became profitable in 2005.

**Sramana Mitra: How many employees did you have by 2005?**

**Marcos Galperin:** I believe we had about 200 people.

**Sramana Mitra: Is it expensive? How much does the workforce cost in South America?**

**Marcos Galperin:** It varies by country, but it is typically much cheaper than what it is in the US. It depends on the type of person you are looking for.

**Sramana Mitra: Are the technology skill sets easy to find?**

**Marcos Galperin:** The technology market in Argentina, where we hire most of our people, has heated up a lot. It is getting harder to hire people.

**Sramana Mitra: So you grew well through 2006, and in 2007 you went public. How was the IPO received in the investor community?**

**Marcos Galperin:** Very well. The stock went up quite a bit. We were quite unlucky in that we did our road show in the middle of the sub prime crisis. The day we priced, the market broke 400 points. And the day our stock went live was the day the Fed, the European Central Bank and the Bank of Japan, all intervened in the markets and gave liquidity, which was something that had not happened since Sept. 11, 2001. Despite that, the stock preformed – we went out at 18, and the stock is now trading at above 40.

**Sramana Mitra: Your investor base is mostly institutional investors, right?**

**Marcos Galperin:** Mostly US institutional investors.

**Sramana Mitra: US Mutual funds?**

**Marcos Galperin:** Today we do not have a very clear picture of exactly who holds our shares. During the IPO, Tiger and General Atlantic both put a relatively large allocation. We need to see results of the most recent quarter. We believe there are other large funds which have been buying our shares, but we have not been able to confirm that.

**Sramana Mitra: Is there a particular type of analyst who is responding to the stock, such as Latin American analysts or technology analysts?**

**Marcos Galperin:** Mostly it is the technology analysts, and recently we have received some Latin American coverage. In our road show, we have focused much more on the technology global growth investors. We think as shareholders, they are much more likely to add value. They have seen different stories in different parts of the world, and understand the differences in business throughout the world.

**Sramana Mitra: They won't panic either.**

**Marcos Galperin:** No, they won't. They understand the challenges and know what we are doing to address them. They can also see where the future market is going.

**Sramana Mitra: What is the plan going forward? The IPO went well, the market is going well, adoption is increasing – where do you see yourself headed?**

**Marcos Galperin:** Continuing to focus on what we are doing. We got into our industry in the very early stages in Latin America. We want to continue being very concerned about the trends going on. We need to focus on regional trends to ensure we know what to change and where to adapt to successfully grow in the region. I think for the next 5-10 years we will continue to focus on that rather than anything else. We have our open payments platform [Mercado Pago] in Chile. Originally it was a closed system with an escrow component, and would not work outside of MercadoLibre. We converted that to an open system, much like the PayPal model, and we believe that is a powerful business opportunity.

**Sramana Mitra: Does PayPal operate in South America?**

**Marcos Galperin:** You can withdraw money but you cannot fund a PayPal account. They do not have a Spanish speaking site either.

**Sramana Mitra: What is your dynamic with eBay today? Competitive or collaborative?**

**Marcos Galperin:** They own 18.5% of MercadoLibre. They are a very big shareholder. We have a very good working relationship with them. We have had very good best practices sharing in the past. Our non-compete agreement expired in September of last year, but we continue to do best practice sharing. They are focused right now in regaining momentum in the US and Germany, their two biggest markets where growth has slowed a lot. As we were saying earlier, the markets we compete in are different, and the formulas work differently. I think they are happy to be minority shareholders and have a local team that drives business at this stage. That is also what they ended up doing in China. They were a minority shareholder, and then they bought everything, then went back to being a minority shareholder.

**Sramana Mitra: In India they bought the largest provider, Bazee.com.**

**Marcos Galperin:** I think the group in India was much smaller than we are though.

**Sramana Mitra: They were. Am I reading this right – that you are the type of team that is more interested in building the company as opposed to flipping it?**

**Marcos Galperin:** We have been building it for 8 years now, so we better be into building!

**Sramana Mitra: Are you tired?**

**Marcos Galperin:** No, I am not tired at all. We just had our end of year party, and I gave a message there. We have opportunities now like we have never had before. Unlike other periods when we were losing money, or as we were saying before, just focusing on the platform, but the business was not there, now the business is there and we are growing and we are profitable. Everyday we have more cash in the bank than we did the day before, which is a good feeling for us because for many years that was not the case. Now we have the cash, we have the team, we have a very strong platform, and we have a very strong brand. Add to that all the opportunities there are in this space, and it is an exciting time.

**Sramana Mitra: How does the entrepreneur network in Latin America work? Are there many entrepreneurs in Latin America now?**

**Marcos Galperin:** Yes, there is a foundation called Endeavor Foundation. They select entrepreneurs in their region and then support them. This foundation was founded by Linda Rosenburg and Peter Kelner, two Harvard graduates. They got the big private equity investors, Latin American market investors, and emerging market investors, and they involved them in the founding of this organization because they wanted entrepreneurs to have access to these people. They do an incredible process of selection.

**Sramana Mitra: Is it like an incubator?**

**Marcos Galperin:** No, not exactly. They do a process to select you, which is really competitive. Potential entrepreneurs present their business plans to different panels in their respective countries. This is now in place in 12 countries. Each country sends their finalist to a final panel in Miami. This organization started in South America, but it is also in Turkey and South Africa now. It will continue expanding in the Middle East as well.

The judges are big investors, entrepreneurs from all over the world. A consensus vote is required ñ just one vote against the entrepreneur means they are not elected. By the time you are elected, you have really gone through an extensive process. Once you are elected, you are plugged in with all of the entrepreneurs in Latin America, South Africa, Turkey and the other expansion areas that the Foundation plays in. This is very useful. The board of each country is made up of very influential people. When an entrepreneur encounters a problem, they are able to take it to their network and really get help dealing with it.

**Rather than giving money to poor people, the support goes to the people who give jobs to the poor.**

**Sramana Mitra: It sounds like a great model.**

**Marcos Galperin:** It is a very interesting model. It has been thought of as the best way to help emerging markets. Rather than giving money to poor people, the support goes to the people who give jobs to the poor.

**Sramana Mitra: Have there been a lot of success stories?**

**Marcos Galperin:** I just went to the ten year anniversary in New York because we were the first Endeavor company to do an IPO.

**Sramana Mitra: You are the poster child of the Endeavor program, that is great!**

**Marcos Galperin:** Thank you, it has been a great experience building MercadoLibre.

Note: MercadoLibre continues to experience tremendous growth now that the Latin American market is ramping up. They did $472 million in 2013 revenue and has a mid-2014 market cap of $3.5 billion.

# Web 3.0 and Online Fashion

In 1999, long before fashion on the Internet actually took off, I started a company called Uuma. It was a traditional venture-backed personalized fashion startup that received an acquisition offer from Ralph Lauren_before the company was caught in the first dotcom crash.

I am going to articulate the vision behind Uuma, particularly because that vision still remains unrealized. I hope that some entrepreneur, somewhere, will execute on it.

As you know, I define Web 3.0 as a verticalized, personalized user experience. The web is still utterly fragmented. You have to go to different places to find information about the same context. I have long had the vision of a personalized Saks Fifth Avenue. I want my store — my personal store — that carries merchandise that applies to me; that suits my hair color, eye color, skin tone, body shape and personal style. I want it to stock my favorite designers and more like those. And I want to see articles and community discussions that are specific to my interests.

I start from the notion of context and propose that all the contextual elements are made available within the same site or web service. That includes content, community, commerce, vertical search and personalization.

Every season, the merchandise will need to be entered into the inventory database according to the categorization. This is a complex system to build and to my knowledge, it hasn't been built yet. At Uuma, this is what we had started to build. This was the central vision driving Uuma's personalized store and personal shopper service.

Let's talk about the Computer Science needed to power such a system. The entire expert system needs to have a data structure against which the merchandise gets categorized and a rules engine that does the matchmaking based on that characterization. In other words, all the parameters — user, mood, size, event, location, time — need to be clustered, categorized and tied to a rules engine that *is* the personal shopper. And, ideally, the system also learns. It learns about tastes and preferences, and becomes better at predicting what to merchandise a personal store with.

So far, the experience of a personal shopper has mostly been available to high-end, luxury customers. My version of personalized shopping could be made available more broadly.

There are, of course, degrees of personalized experiences. A basic level of personalization can be achieved by mass brands using technology, especially intelligent agents. But luxury brands could layer in additional levels of personalization, including human personal shoppers who use technology to track your closet and your preferences and then offer additional judgment to augment the user experience and put together custom collections. My point is, the entire user experience can be massively enhanced to reach degrees of customization and personalization that we haven't seen yet.

Finally, if you mine the data collecting in these online stores and pass some of that back to the designers, they can create custom collections based on specific types and styles of customers and be able to sell them effectively, knowing exactly what retail interfaces the customers are hanging out at. These are incredibly exciting possibilities for the business of fashion to become more personalized on the one hand — and also more scientific on the other. The fashion industry could become more financially successful by utilizing personal data: analyzing it and designing and merchandising accordingly.

Now, one objection to this kind of personalized recommendation system could be: "What about my individuality? I don't want someone telling me what I should wear!"

No, but you do want to walk (or browse) into a store and find thinks that you will like, rather than random merchandise that has no synergy with your taste, size, style.

A personalized store is not in conflict with personalized style. More personalization data in the hands of designers would mean a higher degree of precision in custom designing for different types / styles of consumers … and yes, a personalized store would make it easier to find things that you like.

The other reality is something I learned a long time back by interviewing personal shoppers at different luxury fashion stores. A large percentage of their customers do NOT know what looks good on them. The personal shoppers often act as stylists, educating them on how to accentuate their advantages, and de-emphasize the drawbacks of their body.

By creating a higher degree of personalization around specific body types, this process of education can be delivered much more widely.

Fashion is a HUGE industry. The global women's clothing industry, just a piece of it, is expected to exceed $621 billion in 2014. How many industries do you know of that scale?

Yet, online, fashion has still relatively a small presence.

If I synthesize what I see is the core issue with online fashion, it is that entrepreneurs are thinking of the industry as a distribution channel a la Amazon, with price being the core differentiator. This is a gigantic mistake. Flash sales sites like Vente-Privee and Gilt Groupe focus squarely on price.

Other experiments are in social media. Polyvore is a Pinterest like social media site where people put outfits together. It's a toy, although, their bet is that they will make affiliate commissions in the range of 10-15% from the overall online fashion e-commerce industry, which isn't a bad bet. It has brought them investment from Benchmark.

The closest to what I would like to see, although it has no visual merchandising, is also a Benchmark company called Stitch Fix that sends a personalized selection of items to people's homes. Customers can pay for what they keep, and return the rest. I don't like this one, because I don't want things to be sent over that I have not had a chance to see online first. The logistics of return, to me, are not attractive.

To give you a flavor of what could be, a high-end consumer of women's fashion has a very big annual budget for clothes and accessories. The actual number can be well above $10,000. It is not price that drives this consumer segment. It is design, style, fit, the experience of shopping, discovering interesting new designers, and regularly checking the works of their favorite designers. A personal shopping/store site that can create a compelling user experience for this category could win, say, 20% of the wallet share of this consumer. At $2000 annual spending level, the site would only need 100,000 customers to reach $200 million in revenue. There are very few consumer industries that have the potential of that level of growth with that few customers, which makes it a venture scale opportunity.

So what is the secret of such a site? Why doesn't it exist yet?

In my opinion, to achieve the full potential of such a site, we need an entrepreneur team who understands Fashion at sufficient depth, as well as Computer Science at sufficient depth. Understanding Fashion means understanding design, merchandising, and marketing of fashion. Understanding Computer Science means understanding expert systems and machine learning to be able to create a software engine that can really get to know each customer, and merchandise to that taste, dynamically create a well designed personal store that showcases that merchandise, and consistently buy products from designers who cater to that taste.

Further, this basic concept could also be applied to a specific designer who designs and markets a new line with some of the same principles as above. Instead of a personalized SAKS that carries multiple designers, we could also look at the opportunities to develop a personalized Ralph Lauren or Donna Karan. This would mean, Silicon Valley will need to start funding new design houses, which it has absolutely no clue how to do.

We could conclude that New York has an edge in this industry. To some extent, that is true. So do London, Paris, and Milan. On the design, marketing, merchandising aspects, yes, there is a basic understanding. However, how to translate that understanding into technology is serious Computer Science. That knowledge doesn't exist anywhere else to that extent except in Silicon Valley.

And that tells me, it is time for the Valley to wake up, and start exploring these opportunities. There's not one, not two, not five, but hundreds of very large global companies to be built in online fashion.

And we haven't even started!

Needless to say, online fashion remains a special interest area of mine. If you are an entrepreneur working in the field, I would very much like to hear from you.

# Epilogue

Of all the categories of web businesses, the one that monetizes best, and with the least headache, is e-commerce. In this volume of *Entrepreneur Journeys,* I have provided you with case studies of entrepreneurs who have built successful e-commerce businesses.

Through their work, and their stories, I wanted to share with you a window into the day-to-day running of such businesses, the decisions they made on a daily basis, the important steps and strategies that have determined their long-term success.

There is a lot more to do in e-commerce, especially as gigantic international markets open up their frontiers.

For the hundreds of thousands of e-commerce merchants out there, I felt that these conversations would throw light on the issues you are facing in growing your businesses.

I hope you find them useful and inspiring!

# Final Word:

**Entrepreneurship = (Customers + Revenues + Profits)**

**Financing is Optional**

**Exit is Optional**

## Author Bio:

Sramana Mitra is the founder of the One Million by One Million (1M/1M) global, virtual incubator that aims to help one million entrepreneurs globally to reach $1 million in revenue and beyond.

She is a Silicon Valley entrepreneur and strategy consultant, she writes the blog Sramana Mitra On Strategy, and is author of the Entrepreneur Journeys book series and Vision India 2020. From 2008 to 2010, Sramana was a columnist for Forbes, and currently syndicates to numerous venues including Harvard Business Review and Huffington Post.

As an entrepreneur CEO, she ran three companies: DAIS, Intarka, and Uuma. She has a master's degree in electrical engineering and computer science from the Massachusetts Institute of Technology.

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## **One Million by One Million** Mission

One Million by One Million (1M/1M) is a global virtual incubator that aims to nurture a million entrepreneurs to reach a million dollars each in annual revenue and beyond, thereby creating a trillion dollars in global GDP and ten million jobs.

## Founder

Silicon Valley entrepreneur and strategy consultant Sramana Mitra founded 1M/1M to create a framework for Capitalism 2.0, which she envisions as distributed, democratic capitalism. The program was born out of her 2010 New Year Resolution.

## The Program

We offer a case-study-based online educational program, video lectures, lean, capital-efficient methodology guidance, online strategy consulting at public and private roundtables, as well as introductions to customers, channel partners and investors. The public roundtable is a free program accessible from anywhere in the world. The rest of the services are for our paying members only. Please note that we focus on business strategy and execution; capital is optional, and may or may not be appropriate for your particular business. Less than 1% of businesses that seek funding are actually fundable. However, we are perfectly happy to help the other 99% build sustainable businesses as well, irrespective of fundability or interest in external financing. 1M/1M is a for-profit business, not a foundation or a non-profit.

Meet some of The One Million Club members, and review the Quantified 1M/1M Value Equation.

If you are looking to start or expand an incubator, please look at our Incubator-in-a-Box program.

## Free Public Roundtables

As part of the 1M/1M initiative, Sramana Mitra offers free online strategy roundtables for entrepreneurs looking to discuss positioning, financing, and other aspects of a startup venture every week.

Only the first five who register to pitch will be able to present their business ideas. These roundtables are public forums and recordings of all sessions are available here.

"There are large numbers of people that want to start web-based companies but don't know where to begin. Your curriculum should be mandatory. It has enormous value by itself, but when coupled with the Roundtables and 1M/1M community there is no substitute." — Dan Stewart, CEO, HappyGrasshopper

Sramana requests that entrepreneurs use the 1M/1M Self Assessment Tool to help to prepare their pitches. We strongly recommend that you address the following items in your roundtable pitch:

Your roundtable pitch should be no more than three minutes, and consist of four slides, as suggested above.

Register at http://1mby1m.com

**Contact: support@1mby1m.com**

Twitter: @1mby1m

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