# Lessons from the B2B Exchange Washout



B2B exchanges, once so full of promise, have fallen on hard times. Some exchanges have seen their market value decline more than 99%, and the stocks of platform vendors Ariba and Commerce One are down more than 90%.

It's worth remembering what made exchanges seem so exciting: They were going to get around the limitations of Web technology. The Web supports only one-sided relationships, but business relationships have power, rights, and responsibilities on both sides. In a Web relationship, the server side possesses all the data; this is why Internet privacy is a concern. But businesses don't want to turn all their data over to a trading partner. The Web may be adequate for relationships orchestrated by a single overwhelmingly powerful partner, such as those between Cisco or Dell and their thousands of clients and resellers. But most buyers and sellers couldn't automate their relationships with the Web.

Exchanges were going to resolve this stalemate through business model innovation. With the exchange as a trusted intermediary that would manage all data and automate relationship processes through Web interfaces, buyers and sellers would gain the advantages of Web automation without one party having to give away all power to the other.

While this innovation may have solved the balance-of-power problem, it did so at the cost of degrading relationship quality. Previously, one party to the relationship had to live with the low-power side of a Web relationship – the browser side – but at least the powerful side could build sophisticated applications on top of a database. But with the arrival of exchanges, *both* sides would have to live with low-power interfaces.

Even apart from technology considerations, the introduction of an intermediary inherently diminishes relationship quality. As in the children's game of telephone, where passing a message through intermediaries corrupts it, the business-to-business relationship suffers from passing through the exchange.

Exchanges brought another quality impairment: Partners were unable to innovate freely within relationships. They were limited by the ability of the exchange to modify its software, and the exchange was limited by its need to serve all its clients, not just the innovators.

Exchanges tried to justify their existence by showing that automation would reduce costs. But what is the value of a cost reduction that is won through quality impairment? Despite their ability to reduce costs, B2B exchanges could not offer a clearly beneficial value proposition.

In practice, B2B exchanges succeeded in relationships where cost matters and quality doesn't, like the acquisition of office paper. But they failed in every relationship requiring quality.

The lesson of the last two years is that there is no way around the limitations of the Web. What business-to-business relationships need is a new technology infrastructure that is capable of automating the highest quality relationships. I call such technologies *relationship platforms*.

Only time will tell what the keys to a winning relationship platform will be, but I believe these three features are essential:

- The platform must know about entities like people and firms, and provide support for marketing. In other words, relationship platforms will not only help automate existing relationships but also help create new ones.
- Buyers and sellers must be able to build arbitrary applications on their end of the relationship platform. This will enable parties to customize their relationships at will.
- Data must be transferred with *rights* attached. Security will be enforced by applications at the level of individual data elements. The platform will provide a security standard and security services that applications can rely upon.

Relationship platforms are just beginning to emerge, and several technologies are vying for a leading role. Server-based peer-to-peer networks appear to offer the best architecture. Considerable investments are being made to upgrade the Web to foster server-to-server interactions. Initiatives like Universal Description, Discovery, and Integration (UDDI) will help provide support for marketing. XML provides a means for wrapping descriptive metadata, including rights information, around data. These technologies are creating pieces that will eventually coalesce into a true relationship platform.

What, then, will become of B2B exchanges? Buyer-seller relationships do not need intermediaries, but they do need enhancement. The best opportunity is to provide buyers and sellers with technology and e-commerce services that enhance relationship quality. B2B exchanges should model themselves on credit card companies, who enhance retail relationships without obstructing the relationship between buyer and seller.

Relationship services may not be a sexy business warranting huge valuations, like the $59 billion valuation given to Covisint in its deal with Commerce One. But service businesses will be profitable and sustainable. And after the B2B exchange washout, that looks pretty attractive.

Paul Jaminet is Vice President, Strategy and Corporate Development at WorldStreet Corporation, a supplier of peer-to-peer networking infrastructure. He is currently writing his first book, *Relationship Economics and the Evolution of Business Practice*. This article appeared in the *Boston Business Journal*, April 17, 2001.