collective wisdom®

SZABO ASSOCIATES, INC. VOLUME 15, ISSUE 2, JUNE 30, 2000

Dear Friends:

Credit managers in all media have been puzzling over a new dilemma: How do you extend credit to Dot Com companies when the traditional criteria to determine creditworthiness no longer apply? We hope to shed some light on this problem in this issue's feature article.

We've had some wonderful times this spring, including seeing many of our clients and friends at the BCFM convention last month in San Diego. At our annual picnic June 10th, Szabo employees and their families enjoyed eating great food, playing softball, pitching horseshoes, and just hanging out together on the Chattahoochee River.

Looking forward on our Calendar of Events, there's the annual Szabo Awards Banquet in August, when we'll recognize the achievements of our talented employees. Then we're off to San Francisco for the NAB radio show September 20th through the 23rd.

And finally, July 31st marks the end of the fiscal year at Szabo. We would like, once again, to thank you all—our many longtime clients as well as our new ones—for your valued support.

Best wishes for a fabulous summer,

Pete Szabo, President
Szabo Associates, Inc.

Extending Credit to Dot Coms ...

What to Do When the Old Rules Don't Apply

All credit managers know the old rules for extending credit to a company. To put it in overly simple terms, you find out who's responsible for payment, you determine if they're able and willing to pay, and you research their track record, both in general and specifically with regard to media. But what if the company is a one-year-old start-up that has yet to turn a penny's worth of profit?

Increasingly, media credit managers are faced with this dilemma. Do they take a risk with a promising new Dot Com company with a great idea and a bit of start-up capital, or do they forego the opportunity and focus strictly on the more traditional "brick and mortar" companies that can more easily meet their historical criteria for credit extension?

It's hard—and perhaps unwise— to ignore the potential advertising revenue to media that some Dot Coms represent. Let's look, for example, at one major category of e-commerce—online retailing. A study conducted by The Boston Consulting Group found that online business-to-consumer (B-to-C) retailing revenue grew 120% to $33.1 billion in 1999 and predicts 85% growth in 2000, with revenues surpassing $61 billion. Of course, these are gross revenues of all Dot Com retailers combined—not net profits—and the figures do not take into consideration the growing competition that will force weaker companies out of business. Forrester Research, Inc., a leading independent research firm that analyzes the future of technology change and its impact on businesses, stated in an April press release that "the combination of weak financials, increasing competitive pressures, and investor flight will drive most of today's Dot Com retailers out of business by 2001." So how do you determine if your potential customer will leave you with a bag of gold or simply "holding the bag"?

First of all, it is helpful to understand how Dot Coms get their start-up capital. Although venture capital has been gushing into the Internet economy at an incredible rate, the money doesn't flow through the faucet all at once. VCs might give some money to a start-up with a promising idea with the agreement that certain "milestones" must be met in order to make it to "round 2" and "round 3" of capitalization. If they make it that far, the VCs then help the fledgling company find investment bankers to take it public.

The criteria that VCs use to determine a Dot Com's chance of success are also useful to know, because they are the same criteria that you should use to determine its creditworthiness. Here are the basics:

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Dot Coms —

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1. The Value Proposition. Do they have a killer idea? Do they have a market advantage? Is the market big enough so that winning will make a difference? What is their marketing strategy?

Value proposition—basically, what it is they're offering (product or service) that is significantly different and/or better (faster, cheaper, higher quality, etc.) than what others are offering—is perhaps the most important, and elusive, element to evaluate. It is most important because the inevitable shakeouts among Dot Coms due to consolidations, decreasing investment capital, and increasing competition will leave companies with shaky value propositions lying in the dust early on.

2. The Management Team. Is the management team experienced and synergistic, with backgrounds balanced across the creative, operational, and financial functions? Does the management team possess integrity?

3. The Money. How much money do they have and where is it coming from? For you, the credit manager, know not only how much of the principals' money is invested, but who the VC players are and how much they are investing. Also, learn who the partner companies are. Often, Dot Coms will form partnerships with other companies who provide services in exchange for an equity position and/or favorable status. What are the partners' areas of expertise, and how do they affect the value proposition?

You're probably thinking by now, "All fine and good. But this kind of information isn't exactly included on a credit application." True, although there is some cyberspace justice: one of the best sources of the information you need is the place these companies conduct business—namely, the Internet.

In the March, 1999 issue of *Collective Wisdom*, our feature article listed a number of great Web sites for finding credit information on companies. It might be a good idea to review that issue because much of that information is useful when researching Dot Coms; however, this article will give you additional information on how to get the kind of data you need on Dot Coms specifically. Here are a few of the best Web sites:

Wall Street Research Net:
http://www.wsrn.com
We reviewed this great site last year. This year, we noted inclusion on the site's home page of a portal called "internet.com." Billed as "the Internet industry portal," internet.com offers a formidable list of links to Internet-related information. To name a few, there's The Internet Stock Report, offering strategic and financial analysis of the Web industry, including stocks, mergers and acquisitions, forecasts, and trends; VC Watch, which has a searchable database of deals and deal makers; IPO Watch, a complete list of all Internet-specific companies that have recently announced a public stock offering; and the Internet Stock Index (ISDEX), an exclusive tally of the performance of Internet stocks. You can conduct extensive research directly from the Internet Stock Report page on Internet companies on the stock exchange, and you can conduct a "search" for articles on companies, including pre-IPOs, directly from internet.com.

Forrester Research, Inc.:
http://www.forrester.com
Forrester is a leading independent research firm that analyzes the Internet economy and its impact on business and society. This Web site offers articles and insight into the Internet industry. The home page also allows you to "Search our Research" for briefs and reports on specific companies, including pre-IPOs. The text of company-specific articles is available to clients; however, you can register for guest access.

Stockpoint:
http://www.stockpoint.com
This is a rather snazzy site to research Dot Coms on the stock exchange with easy free access to company profiles, quotes, annual income statements, analyst ratings, interactive charts that allow you to plug in a number of variables to determine performance over time, and an easy-to-understand "help" page that explains the data. The site also has direct links to recent news articles about the company.

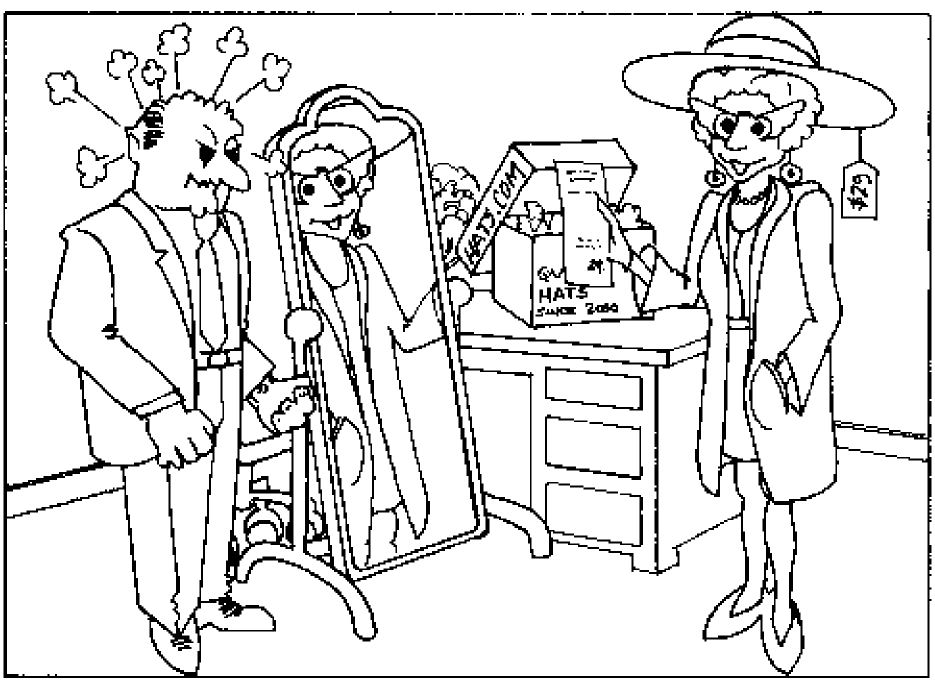
Hoover's Online:
http://www.hoovers.com
Also reviewed last year, we found Hoover's to be extremely helpful in researching pre-IPO Dot Coms as well as more established firms on the stock exchange. We were able to easily find company capsules that not only describe the company but also list partner companies and percentages of investment by VC organizations. This nifty site also has convenient links to company capsules of competitor Dot Coms, information on key people, and key resources that include real-time SEC filings (a new feature). There is also a

link to the Dow Jones Interactive Publication library, which offers articles listed in order of relevance.

Where's It All Going?

One very important development on the Dot Com scene within the past couple of years has been the growth of business-to-business (B-to-B) e-commerce. With analysts predicting that the big money plays would occur when huge corporate transactions moved online, the redirection of investment money, both public and private, into those ventures was inevitable. Forrester predicts that B-to-B online sales will jump to nearly $2.7 trillion in 2004, up almost sevenfold from the $406.2 billion in B to B sales it expects this year. Initially, the primary driver of the B-to-B scene is that the cost efficiency and cost savings they create will force companies to trade there; however, B-to-B drivers are rapidly becoming more about the new channels markets that push top-line growth.

And what about B-to-C e-commerce? Because of the rechanneling of investor money to B-to-B ventures and the difficulties of creating and maintaining a compelling value proposition in the face of fierce competition for consumer dollars, the shakeouts we mentioned earlier will winnow out many B-to-C players. In the case of online retailing, according to Forrester Research, companies must focus on hard assets that support high sales volumes and lower costs per transaction—a large, loyal customer base, in-house fulfillment capabilities, and a solid internal organization—in order to survive. Forrester also predicts that a synchronized presence across multiple channels—brick-and-mortar, mail order, phone order, and Internet commerce—will have a competitive advantage. That prediction is consistent with the findings of new studies on consumer Internet behavior, which indicate that the most powerful use of the Internet for retailing may be in the integration of a Web identity with a familiar, brand-name business that still offers the option of personal interaction.



"I RESEARCHED THE VALUE PROPOSITION OF THAT DOT COM LIKE YOU ASKED, BOSS. HOW'S THIS FOR A GREAT VALUE... ONLY $\$29^{95}$ INCLUDING SHIPPING!"

What's It Mean to You?

We've seen Dot Coms putting an enormous amount of money into marketing in order to acquire customers; however, the constriction of IPO and secondary stock offerings may require many of these companies to spend less and more selectively. And, as some Dot Coms fall by the wayside and others come out clear winners, we may see as many advertising dollars being spent as before, but by fewer players.

Internet marketing firms and media companies hope to pull much of those marketing dollars in their direction, and they may succeed. New technology has enabled online advertising to become increasingly accountable, allowing advertisers to track results from the banner ad all the way to the sale. Secondly, online media seem to be an appropriate avenue to reach online audiences. And finally, it is available for relatively low cost.

Observers have likened the growth of e-commerce to the Gold Rush days of 150 years ago. Then, as now, there were big winners and big losers in the mad rush to get rich quickly. While there's certainly nothing wrong with prospecting for Dot Com advertising dollars, you just have to be smart about it. Research companies carefully, considering their value proposition, management, and capitalization, and beware of last-ditch desperate advertising efforts to get customers with dwindling resources. ♦

The Szabo Difference:
A Broader View of Collections

As you can tell from this issue's feature article on extending credit to Dot Com companies, Szabo Associates pays a good deal of attention to helping you make wise credit choices. Sometimes people ask us if this is really something that a collections service should be concerned with.

The answer is: for a good one, yes.

The more we know about a company, the better prepared we are to determine the most effective ways to negotiate for payment of past-due accounts. Whether the company's growth prospects are secure … whether cash flow is seasonal … whether a merger or acquisition is in prospect … whether a new product is on schedule for introduction … whether an IPO is contemplated … whether the firm's venture capital is restricted—all of these factors and more can determine the way we approach collections. In our style of person-to-person telephone collections, knowledge is an extremely valuable tool to have on our side.

Fortunately, our business also puts us in a very good position to gather and analyze information about the companies you're interested in. Szabo representatives make hundreds of personal contacts each month, and each contact is an opportunity to learn more about new businesses and new means of doing business. In many cases, the people staffing new businesses are people we've become acquainted with in previous business relationships.

We keep computer records of the thousands of companies and agencies we have dealings with.

We're right on the leading edge of credit information. When a business or a business category of business begins to suffer credit erosion—whether it's cyclical or lasting—we are among the first to hear about it.

So while our clients come to us for collections, they often come away with an added bonus—information that's valuable to both sales and credit departments. ♦

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