

The Worshipful Company of World Traders

The XIIth World Traders' Tacitus Lecture

Delivered at the Guildhall in the City of London on

24th February 1999

by

Peter Job, Chief Executive Reuters

Technology and Global Trade Beyond the Millennium

Lord Mayor, My Lords, Ladies and Gentlemen,

Modesty is not the principal characteristic of new age gurus – perhaps they feel there is nobody around to contradict them. Looking at the title of my talk today – global trade beyond the millennium, you may be asking yourselves what possible qualification I have to develop my chosen theme of electronic commerce. E-commerce covers all business and much of human life. People gaily make forecasts that it will be worth 60 billion euros in three years time. Meteoric Internet companies are bought and sold on huge multiples, putting everyday household names in the shade, yet they make losses. There appears to be a disconnection between market capitalisation and profit – capital value no longer appears to equate to the discounted value of future earnings. Managers talk in terms of founding businesses that they can swiftly sell for astronomical sums, instead of building businesses with attractive profit potential. You will not need reminding that not everyone who went to the Klondyke struck gold, but some found nuggets of it.

The vague qualification I claim for talking on the subject is that the E-trading world starts and ends with information. It is the fuel that primes the pump and lights the after-burner when the engines have got started. This gives me some confidence to dissect the principles involved without claiming to know the exact shape of things to come.

The principles that I want to talk about therefore begin with information. Another issue is regulation. Then there is the concept of a gateway, now known by the more fancy term “portal”, in particular so-called “sticky portals”. Then there are the factors of disintermediation, integration, and customer experience. Where out of this jumble will come the business models that in future make companies worth the high sums now being paid for them?

Reuters operates in societies where even reporting the facts is not acceptable

First the information side. Reuters operates in societies where even reporting the facts is not acceptable. Perhaps it is because these societies are so riven with dissent or consumed with their growth process that nobody can agree what the facts are. After a time this gives way to a social background in which the facts are fairly readily agreed though opinions about them may differ, and need to differ to give the citizen the chance to help form his individuality. In the next stage, information is consumed for entertainment, facts often being rather immaterial – after all there is no state of emergency, no secret police, you can always learn the facts if you really want. This could be characterised as a condition affecting many industrial democracies at the onset of the Internet age. A classic example was a recent Internet web site report that Hilary Clinton became so annoyed with her errant husband that she “lost it” and hit him so hard about the face that he had to wear make-up to cover up the bruise for a TV appearance. There was as far as I know no obvious reason to believe this though the British newspapers published the report with glee. The information was there, it was free. Random information can be searched with the utmost facility across a whole range of web sites which may have no particular track record or credentials. It’s movement, it’s action, it’s modern, it’s transatlantic.

It’s also boring after a while. So we have to anticipate the emergence of a demand by the consumer to navigate his or her areas of interest in a more structured way, guided by preferred information brand names that can be bought together easily. This gives a potentially superior result to the use of the existing media since it is a physically cumbersome process to compare what one newspaper is saying with another, or to switch between broadcast TV channels to make real-time comparisons. From the idealistic point of view such thoughtful comparisons produce the ultimate in responsible citizenry. From the practical point of view it is the beginning of the segmentation of the market for E-commerce, and therefore the start of our ability to form business models around such segments.

To give you an example of what I mean, we were approached some time ago by a company producing skin cream who want to enliven their web site with news. They told us, somewhat to our surprise, that we produce quite a few items on this subject every day. They had probably established that competitors did too. Thus specialised information bought from us and others could be used to attract people with specific interests. In the same way the medical news we produce is used as a backdrop for websites which curious consumers search because they no longer accept all their doctors tell them. In the same way second-hand car sales on the Net need a penumbra around them of specialist reviews and evaluations of the latest models or advances in technology.

Let us start by noting that there is an incentive here for the purveyor of goods to pay for information. This is arguably a better model than the one people started off with. They simply assumed that the old media would transfer to the new. Information would be free or almost free and subsidised by advertising as it pretty much always had been. Advertising revenue would pay everyone's bills and generate a stream of sales. This is one model but it may be too coarse-grained for universal application. Advertisers seem to prefer the old way of projecting brands on broadcast television, which is a very efficient way of reaching millions of people simultaneously. Nor is there much evidence that people want to use on-line services to watch the equivalent of broadcast television. There are big projections for Internet advertising and no doubt it will take off, but there is something missing in the formula. If you assume that people go onto the Net because they are part of a consumer segment that is actually looking for something rather than offering themselves as Internet couch potatoes, a different world opens up. Advertisers can place material to appeal to specific niches, and, due to the inter-active nature of the medium, they can be given a much better idea than is possible on the broadcast media as to which relevant buyers or potential buyers are actually watching the computer screen. So there is a possible business model here for advertisers, on-line information providers and e-commerce aspirants, which is based on personal objectives, not random search or the need to exercise itchy fingers on the keyboard.

What is it that gives a web site its magnetism in the first place?

This brings us to the next question – what is it that gives a web site its magnetism in the first place? How does anyone ever arrive there? A web site is thought to be a great liberator because you can use it to communicate, even if you are an SME (small to medium sized enterprise) in Andalucia. But that is no use if no one is listening. Possession of a web site, which is expensive if done properly – like a million dollars a year – is not much use if no one is taking any notice. It is rather like having a costly telephone. Chatting does not make value either. Indeed the chat rooms on the Internet, full of random information communicated outwards, seem to perform rather a similar function that the old black phone offers people. After a hard day at the office they can just go out and talk to whomsoever will listen. Valuable for them, no doubt, but unstructured and it is difficult to create value universally from this.

This is where the concept of aggregation, and “portals” comes in. You can go to these well-known sites easily – and let's not forget that ease of use underlies the whole Internet phenomenon in the first place. There you can find that collection of brands that you like, with good software and linkages to help you through the maze, whether to healthcare, skin cream, cars or anything else. Portal companies command great multiples because it is thought that their dominant role in attracting traffic will enable them to take high tolls of all who pass through their pillars. If this were true, it would be a negative for the development of e-commerce. But I doubt if it is. In a fast-moving technological world, there will always be another aggregator waiting in the wings. If

the turnpike charges are too dear, another road can be found round it. The aggregation companies themselves generally own no content and find it difficult to buy content with highly-valued paper from canny media companies who have been around for a long time. Fashion has moved from the idea that content is king to the notion that portals are the gateway to an investor paradise. The fact is that information sources and the aggregation of those sources in an attractive combined format are both equally necessary. Portal companies need data and e-commerce relationships in order to be “sticky”. In other words these relationships give them competitive differentiation in that they can be used not only to know the right information, but ultimately to buy or sell as well.

In search of the consumer experience

So here we need to set out in search of the consumer experience – there are fields of information and gateways onto them, but what sort of idea is compulsive enough to making people contemplate buying and selling on the Internet. The word disintermediation is the one that immediately pops up in this space. You do not need to go to a bookstore to buy books. You can download music electronically. Why bother with a network of car dealers when you can go straight to a web site to find the model you want. This reasoning is particularly effective in sprawling geography where people have to drive a long way to get what they require.

But there does appear to be a price for such insistence on disintermediation. The organisations that set themselves up to do it are favoured because of the promise of lower cost. Granted that many cost-saving efficiencies are possible, the margin may still turn out to be low in this relentlessly deflationary model. Turning the world upside down, scaring all existing suppliers out of their wits, is not enough. The new intermediaries, which is what we really should call them, have to add value, not just offer lower cost. Some see themselves establishing a position of power simply by dominating the direction of traffic. If you manage to disintermediate car dealers, then you can extend your reach to establishing consumer preference information which car manufacturers would be forced to buy from you. But is it really the case that the large manufacturers would willingly allow a new intermediary to stand between them and the customer in this way? This may prove to be a David and Goliath argument in which Goliath is the winner.

Yet I do not doubt that there is an information exhaust that can be derived from a preferred web site, and that this can be used to add layers of personalised value and profitability. At a basic level it is nice to be alerted to new books by your favourite author and given a list of popular writers on the same subjects. It seems to me that as we exit the phase in which disintermediation is touted as a fearsome threat, a more user friendly approach will prevail, and permit more interesting combinations of value. Perhaps addition of business lines is part of the answer – after all people with certain

preferences in books may also respond to similar treatment of their musical needs. Synergies will have to be exploited across business segments in the time-honoured way.

Electronic share broking

To summarise the way things may go, let us look at the development of electronic share broking. This is probably the most advanced version of E-commerce that there is in the world today. Much attention is currently focused on E-brokers who offer minimal cost of execution – perhaps eight dollars per trade instead of several hundred. But the price may fall further, and they will have to gear up their fixed costs to handle larger and larger volumes, only to be left stranded perhaps by a cyclical fall on market turnover. I prefer the idea of a broker offering a totally integrated customer experience. The investor clicks on a headline to find details of the target company, and a second click takes him into the real-time market where he can choose to trade. The information output measures his success against what he had hoped to achieve and offers alternative courses of action. Keeping a checking account with the same broker becomes a useful convenience. If he has a complex trade he can still phone up a human being and discuss it, in return for paying a larger commission, and ultimately, if he is really in need of detailed advice, he still has the chance to go into a red brick building somewhere and discuss the matter – at an extra cost of course. It is not difficult to see that this more complex chain of value could lock in a loyal and satisfied rather than just opportunistic customer segment over a wide range of cross-promoted services which together would produce good profits and begin to justify the extravagant capital values now being assigned to some of the players in this market.

What stands in our way? One of the biggest obstacles lies in getting to a new form of regulation. I will not dwell here on the well-known issues such as copyright law, security, anti-fraud measures and protection of privacy. Each of these is difficult but the growing sophistication of Internet technology will make the problems easier to solve. I would rather analyse the bigger question – how to transit from the national order of things to the chaos of globality, involving a whole range of applied to commerce, taxation, media and advertising as well as the communications industry. There is a history of national monopoly approaches here. Communications were monopolistically organised in Europe for example and the change which we are now undergoing will take years to bite – right now the links on which the Internet user depends are far more expensive than in the US. Control of advertising, determining which products can be advertised at what time and in what order, can easily be managed over a few broadcast television channels, in themselves closely regulated, but this is just not possible on a web site that might be located in Panama. Even across Europe, different approaches to advertising regulation are ferociously defended.

One obvious solution would be to make the applicable commercial law that of the European country of origin of the web site concerned, but this idea provokes much anguish since people are very attached to rules they have made in their own nation-states. Therefore there is a strong pressure for applying the law of the country where the signal is received. If the applicable rules are indeed those of the country of receipt rather than origin of the signal, E-commerce may never get started properly since everyone will be worried about running foul of unknown civil or criminal law provision. It is against this background that one sees the sense of “harmonisation” by Brussels, just as one clearly sees the sense of a single currency in an E-Commerce setting. Customers are not going to want to build a foreign exchange calculation on top of their price, they will want a single European price.

How far and how quickly the legal basis of societies can be changed

So we have some of the dynamics for change under way, but they will take much time and trouble, and run into unexpected points of resistance. For example consumers surfing the net may well come to expect that all new drugs be made available simultaneously in all national markets instead of waiting for decades, as Japanese women have done, for the contraceptive pill. Consumer advertising, already permitted in the US, may come to be permitted in Europe because of the inevitability of international Internet access (Viagra may be a harbinger of this). But this in turn may generate official resistance, because of the suspicion that it might drive bigger health bills in countries like those of the EU where every effort is being made to constrain the cost of public health, including through application of price controls which differ from country to country and are themselves at odds with a unified electronic world. All this is not as to dismiss national regulation as senseless or outdated, it merely serves to raise the question as to how far and how quickly the legal basis of societies can be changed.

Well this is called the Tacitus lecture. (The Roman Historian) Tacitus wrote about Britain nearly two thousand years ago at the time of Boadicea’s revolt which spread from Colchester (in what is now the eastern county of Essex) to London in AD61 and seems to have petered out somewhere near the extension of the Jubilee line (Stratford, now the eastern edge of London). Tacitus wrote of our forefathers that “they took no prisoners, sold no captives as slaves and went in for none of the usual trading of war. They wasted no time in getting down to the bloody business of hanging, burning and crucifying”. We have moved on apace from the days of this original Essex girl who at least managed to get her statue raised on the Victoria Embankment by the River Thames.

There is going to be no bloody E-Commerce Internet revolution. The ideas of tension between Information haves and have nots are equally spurious. Both the big and the small can gain from the new technology era by serving each other and by together

serving the customer under the gaze of a watchful but flexible regulator and a population that abandons some of its established customs in the name of progress.

Journalists usually know better than to forecast matters immediately ahead since they may soon be proven wrong. But I agreed to do this lecture so I had a better give some kind of prognosis.

World electronic trade will develop further and more markedly

World electronic trade will develop further and more markedly because information will be available to support transactions in a very convenient way. The providers of the information will make good margins because they will to a large extent re-use assets they already have. They will not be hanged by the wayside.

Aggregators will be there to guide people through a random Internet world to the right place. They will make some money because the cost of performing this function is not huge and advertisers will pay them for offering new and popular means of access to defined audiences. They will not need to or be able to enslave anyone else to their interests along the way.

Advertisers will benefit because they will be able to offer their clients new techniques of pinpointing particular market segments without changing their current means of reaching the vast mass of consumers through broadcast TV. Broadcasters will not be hanged or crucified by the Internet.

Businesses will make money in some cases from selling consumer goods to people who for one reason or another want the convenience of buying through the Internet. However pricing is likely to be low and margins thin perhaps. They will initially make more money selling high-margin goods and especially services into niche markets which are expensive and difficult to reach using more scatter-gun methods. They may get burned a little along the way but the ones that succeed will be big enough to take it.

There will be horizontal integration in some parts of this value chain but vertical integration will be more difficult. However, some organisations will achieve a presence in more than one part of the value chain, and establish a superior rate of profitability. This is more likely to happen with services than physical goods. It is more likely to happen if there is a strong need for information around the product.

All this will take time, not least because the regulation of the process is going to prove to be a political hot potato within Europe and between Europe and elsewhere.

This campaign will not peter out near the end of the Jubilee Line.

Tacitus Lecture – Questions and Answers

David Breeze (World Trader):

Mr Job, I wonder what you believe is going to happen with deals that frankly still to this day take face-to-face dealings. You have outlined very clearly what you would do for mass distribution but I wonder what kinds of examples you believe still require the knowledge between the buyer and the seller? Thank you.

Peter Job: You are putting in the position here of countering my own thesis, so my grey cells are working hard. I am trying to think of cases and there must be cases where credit between parties would need to be established. However, is that a process which cannot be electronified? I believe it probably can be electronified. Trust as embodied in credit can be handled. Just as you can have a security module out there saying, 'By the way this envelope shows I am who I say I am', you can probably have in that envelope a portion of credit that has been agreed between you and somebody else. So what appears to be an insuperable obstacle in this case of mutual trust based on credit lines may actually be conquerable electronically. I cannot think off hand of a human process which is not susceptible to being automated, although I am quite sure it would take a huge amount of time to automate every single process and it would probably be very boring if we did!

Alan Powell-Jones (Mondex International):

Given that something like half the world has never made a telephone call, is this electronic commerce and the use of the Internet going to drive a larger wedge between the first and the third world? Given the pressure on reducing margins, what is the incentive to wire the third world?

Peter Job: There are two issues here. Wiring the third world is something that is looking after itself. If you go to southern China today, people are crossing the road with a telephone on each ear! You do not have to dig up vast quantities of countryside now in order to wire things. Soon we will have the first low earth orbit satellites with 400 low-flying satellites, which will enable you to communicate from a phone via a satellite somewhere else. So the question of the economics of wiring up the third world are likely not to be that terrifying and will proceed much faster under the mobile technologies.

The issue in relation to what we could loosely call the third world goes back to what I was saying about the news element in societies. Probably I should start by saying that I do not believe the third world concept means very much, but let us just take certain parts of Asia and narrow it down a little.

How are you going to have electronic commerce and all the information flow that that generally requires if you cannot tolerate facts? There will be a little difficulty, barring

the usual de-monopolisation process for example, of people having excellent communications all over China and so on, but China at the same time does take steps, which are fairly well known, to bar access to unapproved Internet sites.

I have some questions in my mind as to whether there is a conflict between attempting to stand Canute-like in this tide of information, stopping it from going any further beyond your feet, or demonstrating in the historical case that the king had no power to stop the tide – I should be proper in my reference to King Canute. Anyway, is there any point in trying to stop the tide when your whole infrastructure needs to be able to transact electronically in order to narrow the gap between the western economies and the developing economies of a place like China?

There is something of an issue here between relaxation and liberalisation of information flows in countries which have ambitions to leap-frog their more advanced neighbours, and it may lie with them to do that.

Roger Chadwick (Bowyers Company):

Do you feel that we are held back by free Internet access in this country compared with the United States, where local telephone calls are free?

Peter Job:

I believe it is likely so. We in Europe have become tolerant of high costs in a manner which is not the case across the Atlantic. In our company, we have done various studies which show that the cost of lease lines, which form the backbone on which Internet traffic is passing every day, in Europe for a comparable length of circuitry in the United States could be anywhere between five and 10 times greater. So the optimal competition across Europe, including in this country, has not yet arrived and the costs have not been driven down by that competition to a level at which we can expect the maximum expansion of Internet use in my view.

David Ball (Charles Stanley, stockbrokers):

At the beginning of your lecture, Mr Job, you likened the Internet frenzy to the Klondike gold rush. Now we know that it was not the unfortunate gold-diggers who made the fortunes; it was the men supplying the shovels. Who in your opinion in these days of the Internet frenzy are the shovel-makers and suppliers?

Peter Job:

Let us say the stockbrokers – that would be good for a start! *[laughter]* There is a huge raft of people selling their supplies to the digging miners here, and they have been doing very well for quite some time out of the stocking-up, the fitting-out of the Internet shop. They are the companies like Nortel or Cisco that provide routers which lie at the heart of the whole switching of traffic across the network. They are the companies like Netscape, which has now been bought by America Online, which

invented the original browser which was the philosopher's stone, the ease of use thing that we were all waiting for in order not to be frightened of our computer biting us. So software suppliers have been enormously aided by this and certain types of hardware cum software suppliers like router supplies have been greatly aided by this.

I believe this will go on because if you look at the way in which Internet traffic is developing, one of the problems with it is that, if you have a popular site from which everybody wants to retrieve information, it cannot handle the load. To give you a case in point, our Reuters website went down because it was unable to handle the load on Princess Diana's death. On the other hand, you can see a world out there now not very far away in which the user who is interested not in anything as gruesome as that, but let us say in a royal wedding, will just say I have a profile that says that whenever there is a royal wedding, send it to me. That means that not everybody who is interested in royal weddings is rushing to get the same information from the same computer at the same time.

The implication is a new set of software, a new set of sales right across the world of things to embed in your computer which handle things better. So we have a real growth in middleware here, not just the display software, not just the hardware with the routing instructions, but the middleware which handles the means by which traffic is transmitted across the Internet. There are quite a number of pick, shovel and spade providers out there who are taking gold nuggets in return for the goods they provide.

Eric Stobart (Lloyds TSB):

Do you see the development of supra-national regulators and, if so, under whose auspices?

Peter Job:

The problems are so awkward that we may finish up by needing an alien to come from outer space to solve it. We still do not have the question [*question repeated*]. It is very difficult to see that the world can progress without a very extensive agreement at any rate at a supra-national level on certain basic principles. How the hell we get there is a mystery to people like me. The Americans have such a different view on copyright, for example. Europeans tend to place a heavy value on copyright and great restrictions but many American economists argue for the international exhaustion of rights, which say that patents do not last as long as you might have thought. They do not have the same defence of copyright as we do in Europe. Therefore, there are enormous amounts of gaps which the regulators have to bridge, both within Europe and across the Atlantic, before order can intervene.

We also know that the ability to do this supra-nationally is problematic to say the least. I would predict that it is much more likely that it will be a bilateral matter largely between America and Europe for the next two or three years, with many differences of

opinion within Europe at the same time complicating matters, just as differences in opinion between congress and the administration in the United States complicate matters. In the old days, it used to be on the American side that the complications existed but now with Europe in its present state, everybody having to agree and endless political settlements about what has to be done, we will have two moving pieces trying to talk to one another to resolve a set of very complex problems.

I have no doubt that the momentum of the subject matter will push the regulators along. Regulators are usually pretty honest people who want to do a good job and feel dismayed if they do not do it. The momentum behind this subject is so great that, in spite of the difficulties, I would be optimistic that a pretty high level of administrator, who comes to deal with this sort of problem in Brussels, in European capitals or in Washington, would be able to handle it in the end.

Master:

Peter, perhaps I might put the final question to you. You spoke for some time about disintermediation and the creation of new intermediaries. It seems to me that in another sense e-commerce, or the use of technology, has the ability to remove some of the current intermediaries. As Anthony Hilton mentioned in an article fairly recently, where you have organised marketplaces with major participants perhaps doing the vast majority of trade in those marketplaces, they will, rather than going through an organised market structure, start selling directly to the customers, or using that much more as the way they do their business, and with each other. Would you like to make some comments about that?

Peter Job:

I would like to make a comment about that. It is a very interesting subject and one with which I did not think to deal. An example which I would give you of it is that in the United States securities market where the normal habit, as in any other stock market, has been for retail investors to put in small orders for wholesalers in the market to bundle them into bigger orders and then load them into the liquidity of the main central market, this has started to become unnecessary.

With new changes in regulation introduced by the SEC a couple of years ago, it is now possible for small orders to go straight into the central market and for the brokers to avoid excessive administration by simply netting down at the end of the day. So the whole process of rolling up small orders into bigger orders in certain instances of which I am aware – and I would not dream of saying that this is a common practice – has happened and it is happening in scale. So there is an element here not of getting rid of intermediaries so much as electronics reducing redundant process.

Master:

Thank you Peter. I am afraid that time is against us so that must be the end of the question time.

As you already know, this is our 12th Tacitus Lecture and for some years we have had the good fortune to hold it here in Guildhall. Usually, that has been next door in the old library, which is where we are going to have refreshments afterwards. However, as Sheriff Brian Harris mentioned in his introduction, such has been the tremendous response we have had tonight, and I am very grateful to everybody who has come, we have had the privilege of being able to move into the Great Hall.

The response we have received and the number of people who have turned up is, in itself, a tribute to our speaker, Mr Peter Job, and his subject tonight. I am delighted that he has had the opportunity to display his knowledge and experience to us in this wonderful setting here.

Peter, you have brought with you tonight a tremendous amount of experience and knowledge and you have given us a wonderful insight into the way the markets and the use of technology may develop and e-commerce may grow and evolve over the next few years. I have certainly learnt an enormous amount tonight about the way in which the market is structured and the different components of it, which will help to contribute and evolve in the way that the markets will go over the next few years or so.

I was interested to know the obstacles which you also saw and that you believe that those obstacles can, and will, be overcome in time. I was particularly interested in the issue you raised about disintermediation in the market and the creation of new intermediaries. That, I believe, is perhaps the most significant point that I felt, from my point of view and the interest which I have, came out tonight. Peter, thank you very much indeed.

Thank you also for kindly giving to us your centenary book – *The Power of News* – copies of which will be available for people as they leave afterwards. That is a tremendous thing and thank you very much for that, Peter.

As you may have noticed, there are no papers out giving the content of Peter's speech tonight. Happily, I can tell you that transcripts have been prepared and they will be bound up over the next few days and we hope to have them out to all of you by this weekend.

Of course, an event such as this needs a speaker but it also needs to be laid on, supported and paid for. We have had very good fortune tonight to receive tremendous sponsorship from a wide range of companies, and it is only with their help that such an event as this is possible. They are mentioned in the back of your flier but I believe it is only proper that I should personally thank them myself tonight. They are: BT, Cisco

Systems, Compaq Computers, Garretts, IBM, The International Petroleum Exchange, The London Clearing House, Price Waterhouse Coopers, Slaughter & May and Sun Microsystems. Our thanks to all of you for your generous and tremendous support.

Peter, once again thank you very much for a tremendous insight into the way you see the market evolving in the next few years. I am delighted you have confidence it will evolve and that the obstacles which may be in its way at the present moment will be overcome in due course. Our thanks to you and on behalf of the Company it gives me great pleasure to give you this memento. [*applause*] That concludes the formal part of our evening and we hope to see you next door for a reception where we can all meet and chat about the subject which we have just heard about tonight. Thank you.