B2B E-Commerce

The Dawning of a Trillion-Dollar Industry

This issue of *The Motley Fool's Internet Report* covers the largest and most complex topic in the *Internet Report*'s fairly short history — Business-to-Business (B2B) e-commerce. The opportunity for these companies to radically transform the economy is awesome, and there will likely be several multibillion-dollar Rule Makers that will arise from B2B. In this report, we'll look at the industry as a whole, then spotlight one company to keep an eye on. But first, let's review what's happened in the Internet world since our last issue.

MOTLEY FOOL RESEARCH™

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Industry News

BY NICO DETOURN (TMF NICO@AOL.COM)

IN THE SHADOW OF AOL TIME WARNER

The merger of **America Online** (NYSE: AOL) and **Time Warner** (NYSE: TWX), announced January 10, will combine the world's largest provider of interactive services with the world's largest producer and distributor of packaged information, creating AOL Time Warner — the world's largest company.

The terms of the deal are simple enough: Time Warner shareholders will get 1.5 shares of the new company for each share of Time Warner they own. AOL shareholders will receive one share of the new company for each share of AOL they own. When the deal closes, AOL shareholders will own 55% of the new company and Time Warner shareholders will own 45%. AOL chairman and chief executive Steve Case will be the company's chairman, and Time Warner chairman and chief executive Gerald Levin will be its CEO.

Based on the closing price of each company's stock on Friday, January 7, the combined company was valued at $350 billion. The merger values Time Warner stock about 70% higher than its close that Friday, a nice surprise for Time Warner investors but a sore spot for some of those who hold AOL. That hefty premium, and the reason AOL was willing to pay it, only add to the intrigue that continues to surround the merger. Two months after the announcement, the deal still casts a shadow over much of the Internet and the online medium. And it is safe to say that the long-range impact of AOL Time Warner is nowhere near apparent.

There were many reasons given for the merger, ranging from the vague and visionary — "building a new medium for the new millennium" — to the specific and practical. The merger should position the new company for the convergence of diverse media platforms in a post-PC world, and will provide it with more channels to reach more people more often. It gives the already brand-conscious AOL first dibs on and control over some of the most respected information and content properties available. The deal creates unprecedented cross-media and cross-brand marketing opportunities by harnessing online's unique attributes — targeting, personalization, interaction, content on-demand — and Time Warner's already ubiquitous properties. It gives AOL a relationship with Time Warner's customer base of over 100 million, and makes Time Warner the premier "old media" player in the interactive era, a status that it has long worked for, but never quite achieved. The merger also creates a one-stop, globe-spanning media network through which other firms can advertise.

THE VALIDATION OF CABLE

Throughout the merger announcement are references to speeding and driving the growth of the online medium and accelerating the development and deployment of interactive services and content — specifically of the cable broadband variety. And it is on Time Warner's cable assets that most of the attention has focused, at times, it seems, to the exclusion of the larger merger.

Time Warner Cable is the nation's number-two cable operator and provider of broadband Internet access through its Road Runner service. America Online's need to add a strong cable leg to its broadband strategy has been a consistent theme in the analysis of the company, as well as those it competes with — in particular,

Excite@Home (Nasdaq: ATHM). Excite@Home has alternately been painted as the contender to AOL's throne, the victim of AOL's lobbying efforts, and an acquisition target of AOL's broadband lust. For these reasons, the Time Warner merger and its cable systems are seen as a solution to AOL's problems.

Interestingly, the merger has also been widely read as a validation by AOL of things not directly related to it, including the actions and strategies of other companies. With a focus on the over 20 million homes in Time Warner's cable system, and on the premium AOL is paying for the company, the deal is said to validate cable as an Internet distribution pipe, and high-speed access as the online medium's future. The merger is also said to validate the approximately $120 billion **AT&T** (NYSE: T) has recently spent buying cable systems to become the nation's largest cable operator. And with AT&T as its largest shareholder, AOL as its archenemy, and Road Runner as the next closest thing to itself, Excite@Home's business model and strategy of combining access and content has also been validated by the AOL-Time Warner merger.

THE COMPETITION RESPONDS

After such an earth-shaking announcement, the question of how competitors will respond to the deal immediately presents itself. Do **Yahoo!** (Nasdaq: YHOO) and **Microsoft** (Nasdaq: MSFT) have to acquire a **Disney** (NYSE: DIS) or an NBC — owned by **General Electric** (NYSE: GE) — in order to keep up? Do those conventional media companies have to be acquired by a "new economy" company in order to survive? The heads of these and other companies explained that they see no need to respond in kind to AOL's move with one of their own.

Each of these companies is unique, with certain assets that would be difficult and costly, if not impossible, to duplicate or match. Two or more such companies in combination would also be unique. Thus even if Yahoo! thought buying Disney was a good idea, doing so wouldn't qualify as an in-kind response to the AOL-Time Warner merger. Disney and Time Warner are both content powerhouses, but Disney lacks a Time Warner-like cable infrastructure to offer Yahoo! AOL and Yahoo! are both world-class aggregators and organizers of other people's content, but Yahoo! doesn't have AOL's need to defend a subscription fee revenue stream from being siphoned off by free ISPs and faster broadband services.

The different circumstances and needs of these companies help highlight the limitations of an analysis based on finding validation in rough parallels that focuses on mere similarity at the expense of real difference. And when it comes to something as industry-defining as the merger of AOL and Time Warner, the reasons the deal was done, and its potential consequences, it is worth going beyond the first take. In this case, it means looking at the validity of the "validation analysis."

THE MOTLEY FOOL'S INTERNET REPORT

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THE VALIDATION ANALYSIS

The AOL-Time Warner merger is said to validate cable as a broadband Internet platform. There is no question that it will raise the visibility of high-speed access and increase broadband's small fraction of the total Internet access market. However, even with its tiny market share, cable broadband is hardly in need of validation — who would argue against the advantages and inevitability of high-speed Internet access? What cable broadband needs is to continue fulfilling its promise by growing faster, meeting current demand, and driving future demand.

The merger is also supposed to validate the integration of content and access. However, at the product level, the flagship AOL service and its market strategy have in fact been characterized by the integration, or packaging, of content and access since day one. Merging with Time Warner and gaining access to cable broadband adds nothing new on that count.

It could be said that because AOL developed and still primarily operates on a narrowband platform, the merger validates the integrated content/access model specifically for the broadband platform. But for all the changes broadband brings — new content forms, services, and production technologies — the specific impact it will have on the relationship between content and access is an open question. America Online mostly aggregates third-party content for its services and produces little of its own. After the merger, AOL Time Warner will derive significant revenue and cash flow through content ownership, but this need not change the character of the integrated model at the product level.

Related to the integrated packaging of content and access are questions concerning the business advantages or disadvantages of the ownership of both content and distribution infrastructure by a single company. It could be argued that AOL's acquisition of Time Warner Cable and Road Runner is a validation of the ownership of distribution by a media company. The move also suggests a departure from what has been AOL's successful practice of not owning distribution infrastructure, and ownership issues may well be different for broadband than for narrowband. The question, then, is whether the growth of broadband will change AOL's long term views on distribution ownership. No matter how that question is answered, the relatively small footprint of Time Warner Cable, and Road Runner's complex ownership structure — involving a motley gang of companies including Microsoft, **Compaq** (NYSE: CPQ), and MediaOne (soon to be acquired by AT&T) — caution against too quickly reading the Time Warner merger as a long-term pipe play on AOL's part.

So it is not clear exactly what the AOL-Time Warner merger validates. The integration of content and access in the AOL service predates the merger by over a decade. The ownership and upgrading of substantial cable assets by Time Warner, the quintessential content company, also predates the merger by a half-decade at least. Both obviously predate the merger of @Home and Excite, which at the time it was announced was widely read as an effort to create something more along the lines of — and thus more competitive with — AOL. In addition, while Road Runner and Time Warner Cable are roughly comparable to @Home and its cable partners (size notwithstanding), there are few meaningful similarities between Excite and the balance of Time Warner's non-cable assets other than that they are both media companies.

ACCELERATE, DEPLOY, COMMODITIZE

The merger announcement's many references to AOL's intention to use Time Warner's cable assets to accelerate the deployment of interactive services has already been mentioned. With all the excitement surrounding broadband, and the expectations of a long-overdue high-speed cable move by AOL, it is understandable that the cable implications were picked up on right away. But the references to accelerated deployment in order to drive consumer usage, advertising, and e-commerce — and speed the growth of the medium itself — should not be overlooked. Those references outline the strategy behind the merger.

In a way, there is nothing new here. AOL has from its earliest days been about aggressively growing its subscriber base and scaling its operations. However, the combined assets of AOL Time Warner will allow the new company to operate on a scale that is not simply larger, but will let it attempt things it otherwise could not.

Perhaps the most significant thing about the merger is how it positions AOL to respond to some of its long-term challenges, the most famous of which is the need to move its business into the broadband era and deal with price competition from free Internet access. In fact, those two challenges are more related than they appear, and the Time Warner merger is as much a response to free access as it is AOL's move to "get a broadband strategy." For although broadband is just now ramping up and has yet to fully arrive, and free ISPs are a phenomenon of the fading narrowband era, the merger lets AOL approach both from the same angle, and attack them as aspects of a common and overriding issue, namely, the eventual commoditization of access.

We are not going to see free broadband and free narrowband services competing head-to-head any time soon, of course. But even for broadband, the long-term trend is the same, and if anyone knows this, it's AOL. America Online is not only the largest provider of Internet services, it is also the largest consumer of Internet services, buying them wholesale from companies like **MCI WorldCom** (Nasdaq: WCOM) and then branding and reselling them to AOL subscribers. With about two-thirds of AOL's revenues coming from monthly subscription fees, few things are more important than monitoring demand, projecting usage trends and patterns, and using this information in plotting the future course of the business. This is why AOL's actions must be read with an eye toward how it is positioning itself in relation to the long-term trend of commoditized access.

EFFICIENCIES OF SCALE

During the December quarter, AOL added 1.2 million domestic users and 227,000 modems to its leased network, and saw daily usage increase between 3% and 4% with member retention at record levels. With all that, it saw a simultaneous 10% quarterly decline in average network costs per hour. This was not due to the commodity-access trend. It resulted from operating and cost efficiencies being driven by increased scale. In other words, as more people subscribe to AOL, the more cost-efficient it becomes, which enhances management's ability to grow and expand the service. In addition, this increasingly efficient subscription service is what brings members into contact with AOL's advertising and e-commerce, which grew about 80% over the last 12 months, 25% in the last quarter, and which, taken together, are the company's fastest growing revenue stream.

These dynamics suggest how AOL's long-term interests can align with falling access costs and a reduction — or even an elimination — of subscription fees without adversely affecting the business.

Given the efficiencies of scale in its subscriber operations and the faster growth in non-subscription revenues, AOL's intentions to accelerate deployment, drive consumer usage, and speed the growth of the medium are more easily seen as the outline of a new strategy. However, while the quick focus on the cable properties can make the strategy appear to be one that newfound broadband assets make possible for AOL, the underlying business dynamics reveal it as a strategy that AOL will be applying to broadband and to connectivity in general. Whether it's narrowband or broadband, to accelerate deployment and drive usage is to also accelerate and drive the commoditization of access. Merging with Time Warner allows

AOL to, in effect, embrace the potential threat and benefit from the inevitable.

Combining Time Warner's revenues, cash flow, and earnings with its own reduces AOL's dependence on subscription fees, almost all of which are currently from narrowband users. (Of Time Warner's six main operating units, one has revenues that substantially exceed AOL's total, another that essentially matches it, and three others that are within clicking distance.) This blunts the threat to AOL of free ISPs, which are themselves beneficiaries of falling prices and rising demand. The same dynamics at work on the narrowband platform also benefit broadband operations, with special emphasis on deployment and making the basic service available to more users. Once done, the key is still to increase usage and leverage user engagement into advertising and commerce revenues.

CONTENT AND COMMERCE

The Internet's most successful players compete in a game where the object is not subscribers, as such, but consumers, and in which relationship, scale, and leverage reproduce themselves. Because subscription fees are not based on usage and trend down over time, the true value of a subscriber is not in her subscription fees, but in her availability for commerce and other "after access" opportunities. Access is a requirement when offering and using an interactive service, but it is not the service itself. Similarly, once the goal is defined as commerce and the delivery of commerce-friendly services, the most important qualities of access are that it be ubiquitous, reliable, as cheap as possible, and bandwidth-compatible with the immediate task at hand.

All of this points to the AOL-Time Warner pairing as being less about the combination of content and connectivity than about the combination and rapid scaling of content and commerce. But that has always been AOL's game, and access, whether owned or leased, is a necessary cost of doing business. There is no reason to think AOL has changed its basic view and understanding of the medium, and no reason to think that broadband, for all its unique qualities, would force such a change. Beyond that, size and scale produce influence. And the Time Warner merger signals that AOL is prepared to play its game in its way on a field that it intends to shape.

And while on some level it might appear to be a "validation" of cable broadband, on another level it might be closer to the opposite. If America Online has aligned its strategy with the trend toward commodity access and is prepared to aggressively pursue that strategy — including the advantageous acceleration of that trend and its application to broadband — then it threatens to destabilize the system of fee-based consumer Internet access, even though AOL has been the greatest beneficiary of that system. It's a fascinating game to watch. But it's still hard to see what is being validated, other than AOL, by and for AOL. And the Internet, of course.

Timeline

(JANUARY - FEBRUARY 2000)

JANUARY

01/01/00 — Wal-Mart expands Web presence.
01/03/00 — Lycos takes 14% stake in iCOMS Corp.
01/03/00 — America Online announces $2.5 billion in holiday shopping sales.
01/03/00 — Broadband Digital Group launches FreeDSL.
01/04/00 — CNET and AMFM to create the country's first all-technology radio format.
01/04/00 — AOL's Nullsoft Winamp and Liquid Audio form multi-year digital music alliance.
01/04/00 — Russ Pillar named head of CBS Corporation's Internet initiatives.
01/05/00 — America Online, Casio announce e-mail via Casio personal computers.
01/06/00 — Excite@Home launches free Internet access service.
01/07/00 — Yahoo!-branded computer accessories to be available in retail channel.
01/07/00 — Microsoft cancels PC rebate offer.
01/09/00 — General Motors and America Online announce major strategic alliance.
01/09/00 — Ford and Yahoo! team to serve consumers online.
01/10/00 — NetZero reaches 3 million registered users.
01/10/00 — TheStreet.com to become free site and hub of new network.
01/10/00 — America Online and Time Warner announce merger.
01/13/00 — General Motors signs strategic alliance with NetZero.
01/13/00 — Microsoft names Steve Ballmer President & CEO; Bill Gates will be Chairman, Chief Software Architect.
01/14/00 — Theglobe.com acquires Chips & Bits, online game retailer.
01/14/00 — Softbank, ZDNet, and Yahoo! Japan form Softbank ZDNet Japan.
01/14/00 — CMGI completes acquisition of Flycast Communications Corporation.
01/18/00 — CMGI and *The Simpsons* offer free ISP.
01/20/00 — AT&T and MediaOne file suit against Henrico County.
01/20/00 — Engage to acquire Flycast and Adsmart from CMGI.
01/20/00 — CNET to acquire MySimon.
01/21/00 — RIAA sues MP3.com over copyright violations.
01/24/00 — Warner Music Group and EMI to form world's premier music group.
01/24/00 — Amazon.com enters strategic partnership with drugstore.com.
01/24/00 — CMGI and @Ventures launch new $1 billion technology venture capital fund.

01/25/00 — CMGI and Pacific Century CyberWorks establish Asian joint venture.
01/25/00 — RealNetworks acquires Netzip, Inc.
01/25/00 — Excite UK announces Web deal with Vodaphone.
01/26/00 — Priceline.com teams with Hutchison Whampoa in Asian expansion.
01/26/00 — Chalkboardtalk.com seeks criminal judgment against Yahoo!
01/26/00 — Asia Global Crossing announces GlobalCenter Japan.
01/27/00 — AOL blocks distribution of prototype software.
01/30/00 — Vodafone AirTouch and Vivendi to establish Internet and telecom alliance.
01/31/00 — Critical Path acquires RemarQ.
01/31/00 — Webstakes changes company name to "Promotions.com."
01/31/00 — McAfee.com acquires leading personal firewall vendor.

FEBRUARY

02/02/00 — AOL service surpasses 21 million members.
02/02/00 — NetZero sues Excite@Home over trademark infringement.
02/03/00 — Excite@Home and Lipstream launch integrated voice, text chat.
02/03/00 — Go.com launches "EXPN" sports brand.
02/03/00 — Two million BlueLight.com free ISP CD-ROMs available at Kmart.
02/03/00 — Maverick Recording Co. and AOL announce exclusive Madonna promotion.
02/03/00 — EMachines ends free Internet access.
02/04/00 — EarthLink and MindSpring complete $4 billion merger.
02/07/00 — Lycos launches network in Latin America.
02/07/00 — Medscape's CBS HealthWatch, AOL launch co-branded consumer sites.
02/07/00 — Yahoo! target of denial of service attack.
02/08/00 — Lycos acquires Valent community provider.
02/08/00 — GO.com and eBay announce multi-year strategic marketing agreement.
02/08/00 — AOL and Footlocker.com announce $21.5 million alliance.
02/08/00 — eBay target of denial of service attack.
02/08/00 — Amazon.com target of denial of service attack.
02/09/00 — AltaVista acquires Transium to deliver custom search hosting services.
02/12/00 — Excite@Home announces wireless initiative.
02/14/00 — Bluemountain.com hits all-time record high for Valentine's Day.
02/14/00 — CMGI to acquire Tallan.
02/14/00 — LookSmart signs Amazon.com in major advertising deal.
02/14/00 — CNET and techies.com partner to launch co-branded career site.
02/15/00 — E-Stamp receives U.S. Postal Service approval for browser-based postage.
02/15/00 — Visto adds wireless access services.
02/16/00 — 24/7 Media, NetZero announce strategic marketing agreement.
02/16/00 — CMGI, StarMedia start free Latin American ISP.
02/17/00 — America Online and Blockbuster Inc. expand strategic alliance.
02/17/00 — AOL, Time Warner announce *Sports Illustrated* swimsuit issue promo.
02/18/00 — ABCNEWS.com to offer interactive exit polls for primaries.
02/18/00 — Magnitude Network joins iCAST.
02/18/00 — Charles Schwab site hit by outage.
02/18/00 — Staples to raise $250 million for website.
02/22/00 — AOL announces $60 million strategic alliance with Homegrocer.com.
02/22/00 — CNET to acquire Digital Media Services, Inc.
02/22/00 — Lycos and Columbia Records offer exclusive, new Bob Dylan music.
02/22/00 — Dow Jones & Company and Excite@Home form new company, Work.com.
02/22/00 — Global Crossing to acquire IXnet.
02/23/00 — Former CFO of Citigroup joins Priceline.com as VP, CFO, and board member.
02/23/00 — CNET debuts free trial version of BlackICE security software.
02/24/00 — Excite@Home invests in ecentives, direct marketer.
02/24/00 — SOFTBANK invests $57 million in Toysrus.com.
02/25/00 — Priceline.com announces Name-Your-Own-Price-For-Gasoline on the Internet.
02/28/00 — Amazon.com announces wireless Web portal.
02/28/00 — EarthLink, Sprint team extend wireless Internet services.
02/28/00 — America Online announces six wireless agreements.
02/28/00 — Excite@Home joins wireless standards consortium.
02/28/00 — Microsoft announces MSN Mobile 2.
02/29/00 — America Online and Time Warner announce open-access framework.
02/29/00 — Lycos launches free Internet access.
02/29/00 — Priceline.com announces expansion to Australia and New Zealand.
02/29/00 — 24/7 Media signs agreement to acquire Exactis.com.
02/29/00 — CMGI announces share exchange for Pacific Century CyberWorks stock.
02/29/00 — iCAST partners with RioPort for digital music downloads.
02/29/00 — Network Solutions makes strategic investment in MyComputer.com.
02/29/00 — Excite@Home's FreeLane surpasses 500,000 users in record time.

Industry Analysis

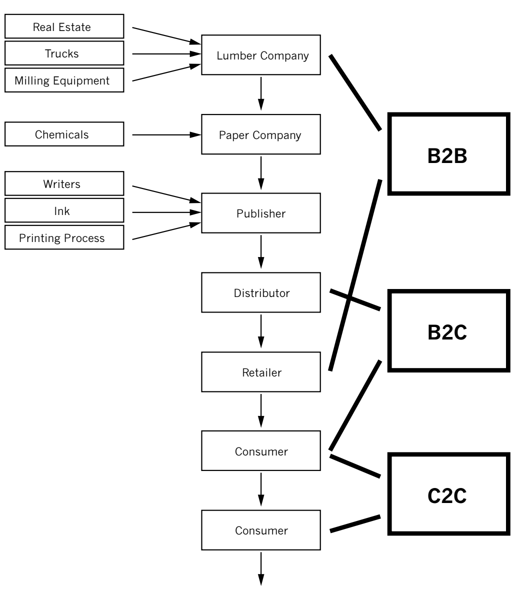
BUSINESS TO BUSINESS E-COMMERCE

BY PAUL LARSON (PAULL@FOOL.COM)

WHY CONSIDER B2B?

There are plenty of reasons to make an effort to study B2B e-commerce, and probably the largest reason (no pun intended) is that the potential market is simply huge. Forrester Research predicts that there will be $1.5 trillion in goods and services transacted online among domestic businesses by 2003. Internationally, the firm believes the number could reach $2.5 trillion. Any way you slice it, this is an enormous amount of money that will be changing hands online.

For comparison's sake, Forrester expects B2B e-commerce to be about 14 times larger than B2C e-commerce by 2003. To see why B2B is so much larger, let's consider the lifecycle of a book. Looking at the graph below, it should be readily apparent that when creating a book there are many more steps in the B2B realm than there are in the B2C realm. When a consumer buys a book (or any other good, for that matter), it's the last step in a long chain of events.



Since there are many more B2B than B2C transactions, that means there are that there are a vast number of ways in which processes can be streamlined and markets made more efficient. B2B is not just about making the office paperless. Rather, e-commerce of all types is about creating entirely new ways for buyers and sellers to meet and efficiently do business.

It's not that often that we as investors can watch the entire economy be reformed and rewired. We are in the midst of a major paradigm shift in how businesses interact with one another, and B2B may represent one of the largest new market opportunities to arise in our lifetime. In short, we would be quite foolish (small f) to ignore the Internet's effect on the other 90%+ of the economy beyond the consumer realm.

HISTORY OF B2B

B2B commerce is actually nothing new. Near the turn of the last century, the vast majority of our economy was dependent on an industry that was almost entirely designed to facilitate trading between businesses. That industry was the railroad industry. Next time you are stopped at a railroad gate, take a close look at what the train is carrying and you will see that the majority of cars are carrying goods (coal, grain, lumber) going from one business to another.

While there were numerous passenger trains back in the railroad industry's youth that largely created the demand for the rails, the railroad network came to be dominated by traffic between businesses. If history is any guide, today's online retailers will see their revenue dwarfed in size by B2B transaction volume. B2B commerce, whether online or not, is simply an enormous part of our economy.

Online transactions are also nothing new. Many companies have been working with Electronic Data Exchange (EDI) for decades. EDI was basically a way for companies to communicate

Select Internet B2B Companies

Accrue Software	(Nasdaq: ACRU)
Agile	(Nasdaq: AGIL)
Ariba	(Nasdaq: ARBA)
Aspect Development	(Nasdaq: ASDV)
BEA Systems	(Nasdaq: BEAS)
Breakaway Solutions	(Nasdaq: BWAY)
Clarus	(Nasdaq: CLRS)
CMGI	(Nasdaq: CMGI)
CommerceOne	(Nasdaq: CMRC)
eBay	(Nasdaq: EBAY)
eMerge	(Nasdaq: EMRG)
FreeMarkets	(Nasdaq: FMKT)
i2	(Nasdaq: ITWO)
Internet Capital Group	(Nasdaq: ICGE)
Harbinger	(Nasdaq: HRBC)
MicroStrategy	(Nasdaq: MSTR)
Onvia	(Nasdaq: ONVI)
Oracle	(Nasdaq: ORCL)
RazorFish	(Nasdaq: RAZF)
Sabre	(NYSE: TSG)
Siebel Systems	(Nasdaq: SEBL)
SilkNet	(Nasdaq: SILK)
Stamps.com	(Nasdaq: STMP)
Ventro	(Nasdaq: VNTR)
VerticalNet	(Nasdaq: VERT)
Viant	(Nasdaq: VIAN)
Vitria	(Nasdaq: VITR)

electronically with both their vendors and customers. However, these EDI networks were notoriously expensive to use. Their complex and proprietary nature also severely limited their use among corporations. However, this is changing now, and corporations are rushing online to do business.

While the personal computer, EDI, and business-to-business commerce have been around for a long time, it is only in recent months that B2B has caught Wall Street's attention. It would be an understatement to say that B2B has been scorching hot. It's hard not to look at the hundreds of billions in stock market capitalization that have been created in the last nine months and ask, "Why now?"

First, the Internet is just now reaching ubiquity in the corporate world. The cost of buying a PC and connecting it to the Internet has gone from several thousands of dollars to a couple hundred dollars. It has only been in the last few years that most companies found themselves online at all. Connecting to the Internet is cheap, and is getting cheaper every day.

Not only have network and computer costs come down significantly, but the Internet is a wide-open standard and a common meeting place. The problem with EDI networks was that they were proprietary and closed. The number of firms on any given EDI network was highly limited, making their value also quite limited. On the other hand, the Internet is a common medium where anyone and everyone can communicate. Today, anyone with a browser can conduct e-business if they so choose.

Metcalfe's Law of Networks states that any network's value grows by the square of the number of nodes on that network. A railroad that only goes between two cities is much less valuable than one that can take rail cars anywhere in the country. Same goes for a telephone system, an e-mail system, or a network that allows online commerce. The point is that large, ubiquitous networks are much more valuable and useful than smaller, closed ones. The Internet is just now reaching the point of being within the walls of every major corporation.

Finally and perhaps most important, large organizations are slow to change their ways. As they say, it takes time to turn the *Titanic* around. It has only been in recent months that corporate strategic planners realized they had to be online now or face a major disadvantage against their competitors.

And going back to our railroad example, it was the individual consumers riding passenger trains that were largely responsible for much of the early railroad traffic. On the Internet, it was also consumers who were among the first to start using the network for commerce. Individual consumers simply tended to be earlier adopters than major corporations.

In short, it has only been in recent months that the Internet has become prevalent enough in the corporate world to be used for sizable B2B commerce. Plus, the capital did not start to flow to the B2B service companies in any meaningful way until 1999, yet investor enthusiasm has now created a gusher of money flowing into the sector.

B2B Dictionary

B2B — Business-to-Business

B2C — Business-to-Consumer (e-tailing)

C2C — Consumer-to-Consumer (auctions, classifieds)

Vertical — Generally used to describe different industries and sectors. For example, the "paper vertical" is just another way of talking about the paper industry.

Horizontal — Generally used to describe products and services that are used across many different industries (verticals). An example may be recruiting services, which are something all industries need.

Hosts — Another term for "market maker." A host connects buyers and sellers and facilitates e-commerce within verticals.

Functional Hubs — Another way to describe horizontal products and services. Companies acting as functional hubs may also be called "enabling service providers."

MRO — Short for "maintenance, repair, and operating supplies."

ASP — Application Service Provider. Typically used to describe companies serving horizontal needs.

CRM — Customer Relationship Management. The software that allows companies to interact and keep track of their customers and vendors.

ERP — Enterprise Resource Planning. Basically, the software used to run the day-to-day operations of a business. Most ERP software is today being designed with e-commerce in mind.

EDI — Electronic Data Exchange. Essentially, B2B e-commerce before the Internet.

Network Effect — When a market's attractiveness greatly increases with additional buyers and sellers. Additional buyers attracts additional sellers and vice versa. This is the effect that has eBay atop the C2C domain.

Fulfillment — The act of physically getting a product to a buyer.

IS IT TOO LATE?

It is quite easy to look at the stock market performance of many of the recently public B2B companies and say, "Oops, I guess I missed that train!" Most B2B companies that came public in the past year are now several times higher than the price at which they held their IPO (see chart on p. 8-9).

What do you think?
PLEASE FILL OUT THIS QUICK ONLINE SURVEY!

VERTICALNET'S STOCK PRICE OVER THE PAST YEAR

INTERNET CAPITAL GROUP'S STOCK PRICE OVER THE PAST YEAR

ARIBA'S STOCK PRICE OVER THE PAST YEAR

What do you think?
PLEASE FILL OUT THIS QUICK ONLINE SURVEY!

SIEBEL SYSTEMS' STOCK PRICE OVER THE PAST YEAR

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COMMERCE ONE'S STOCK PRICE OVER THE PAST YEAR

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Yet as the old cliché goes, we advise not driving through the rear-view mirror. Those who got scared of heights created by strong stock market performances would have been scared out of AOL in 1996, Yahoo! in 1998, and **Cisco** (Nasdaq: CSCO) at just about any time in the last decade. Unlike in the real world, sometimes things that go up in the stock market stay up.

Looking forward at the B2B industry, it is still in its early, formative stages. While few of the B2B companies have proven their worth in any substantive way, the market opportunities these companies are chasing are enormous.

One way to see this is to compare the top B2C companies with the top B2B companies. It should become readily apparent from looking at the chart below that even though the market opportunity for the B2B companies is several times larger than those of B2C or C2C, the combined stock market capitalization is still less than those of the consumer-related Internet companies. An argument can easily be made that the B2B companies as a group may actually be undervalued relative to their potential market size.

Market Capitalization of Leading Internet Companies

B2C and C2C

Company	Ticker	Market Cap. ($ in millions)
AOL*	AOL	131,486.9
Yahoo!	YHOO	83,183.8
CMGI	CMGI	36,302.2
Amazon	AMZN	21,299.2
eBay	EBAY	19,336.0
Priceline	PCLN	10,982.0
Excite@Home	ATHM	12,001.8
Lycos	LCOS	6,487.6
WebVan	WBVN	3,829.3
Go.com	GO	3,131.3
Buy.com	BUYX	1,703.0
Combined Market Cap.		329,743.2
Estimated 2003 B2C and B2C E-commerce		$175 Billion
Group Market Capitalization / 2003 Market Size		1.9

Note: For Domestic Commerce Only * Before the Time Warner merger

B2B

Company	Ticker	Market Cap. ($ in millions)
Internet Capital Group	ICGE	31,128.9
Ariba	ARBA	29,984.3
Siebel	SEBL	29,823.9
I2	ITWO	26,269.2
Bea Systems	BEAS	19,995.5
CommerceOne	CMRC	16,968.2
MicroStrategy	MSTR	14,498.6
Vitria	VITR	11,250.8
VerticalNet	VERT	8,962.7
Ventro	VNTR	7,213.4
FreeMarkets	FMKT	6,933.9
Combined Market Cap.		203,029.3
Estimated 2003 B2B E-commerce		$1.5 Trillion
Group Market Cap/2003 market size		0.1

Sources: Forrester Research, S&P Comstock,Fool Research (As of 3/4/99)

Again, the B2B industry as a whole is still extremely young, and none of the B2B companies are producing today anything close to the cash flow needed to justify their current valuations. Nevertheless, there is the potential for enormous cash flows three to five years out, and that is what investors are counting on today.

THE TWO DIFFERENT TYPES OF B2B

Let's now take a step back and talk about the two main types of B2B companies that are out there. The two types are vertical and horizontal companies. Vertical is really just a fancy way of saying "within an industry." Vertical B2B companies go by many different names. Sometimes they are called market makers or hosts. These names are actually fairly descriptive of what vertical companies do. That is, they create markets within certain industries so firms within that given industry can electronically communicate with potential suppliers and customers.

Vertical companies also tend to have a great deal of content on their sites about the different industries that they serve. One example of a vertical company is this issue's spotlight company, **VerticalNet** (Nasdaq: VERT). VerticalNet runs sites for dozens of different industries, and these sites offer content and make markets for commerce within a given sector. Some of the content offerings include what is common in trade journals such as industry news, buyers' guides, directories, etc. The sites also have commerce offerings such as classifieds, auctions, and requests for proposals.

There are literally hundreds of different verticals in existence. Every industry is different, requiring B2B hosts to become intimately familiar with variations in processes and products within a given vertical. VerticalNet is the most prominent vertical company since it runs approximately 50 different industry-specific websites with dozens more in the works.

The second major type of B2B company is that of the so-called horizontal service provider. These are companies that serve the same needs across numerous different industries and verticals. One example of a horizontal (sometimes called "functional hub") includes raw goods procurement at the top of each vertical. This is where companies like **CommerceOne** (Nasdaq: CMRC) and **Ariba** (Nasdaq: ARBA) are excelling. On the other end of the spectrum, every vertical needs to get its finished product to consumers which is where shipping providers like **FedEx** (NYSE: FDX) and **UPS** (NYSE: UPS) come into the picture.

ADDING VALUE, REWIRING THE ECONOMY

Now that we know about the two different types of B2B services, let's take a look at why companies are excited to embrace B2B commerce.

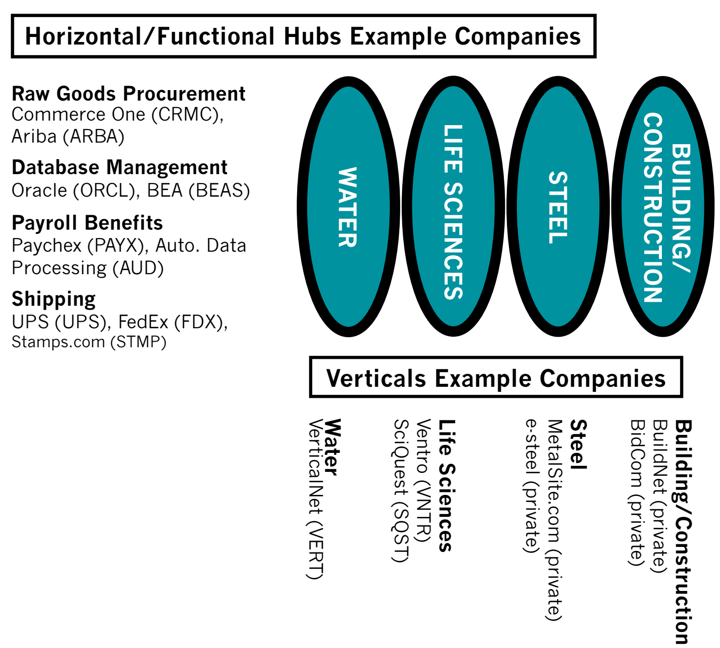
- **Reduced purchasing costs.** Probably the most obvious way in which firms can cut costs is by remodeling the way that they purchase their raw goods. The National Association of Purchasing Managers says that the average manual purchase order costs a company $79. This is because locating goods needed and then filling out the necessary paperwork is a time-consuming process littered with red tape. Searching for products online requires much less time than flipping through a paper catalog, and electronically processing an order greatly streamlines the entire activity.

- **Increased market efficiency.** By using the Internet, companies can quickly get price quotes from numerous different suppliers. By increasing the number of sellers, buyers are more likely to get a fair price, and vice versa. Just as **eBay** (Nasdaq: EBAY) has created an efficient market for everything from Pez dispensers to old Elvis records, B2B hosts make connections between buyers and sellers that may not have otherwise happened.

- **Decreased inventory levels.** By using B2B technologies, companies can better utilize their inventory and raw materials. The Internet allows even more time to be shaved off for companies using "just in time" manufacturing techniques. In essence, it allows firms to use less working capital to do the same amount of work, freeing these funds to be invested elsewhere.

- **Increased capacity utilization.** Going hand-in-hand with decreased needs for working capital, companies are also better able to utilize their fixed assets. Moreover, if a company creates excess product or has extra raw material, B2B hosts allow that excess to

The Two Types of B2B Commerce



be turned right back into cash. In the old days, excess material might have sat and collected dust or even been simply thrown away. The Internet has created a market for just about anything.

- **Greater market intelligence.** B2B hosts give producers a better insight into the demand levels in any given market. Spot price levels can be determined for everything from paint pigments to plastic cups. This allows companies to make better decisions regarding what and what not to produce.

The main attraction that runs throughout B2B is that it makes companies much more efficient as a whole. Increasing efficiencies means reducing costs, which is something every company is extremely interested in.

HOW DO B2B COMPANIES MAKE MONEY?

How a B2B firm takes in revenue is largely a function of what type of business it is in. There are many different business models surrounding B2B, but they all seem to have four common revenue generators:

- **Sales of product.** Most horizontal B2B companies are in the business of selling solutions in the way of software. Just like most other software companies, these businesses have high start-up costs but correspondingly high incremental margins. Some software companies also elect to license their software instead of doing outright sales.

  Vertical companies are more often involved in the sales of product within their vertical. The so-called "catalog model" has the vertical B2B companies actually taking inventory and acting as middlemen in the sales process — a sort of industry clearing house.

- **Services, maintenance fees.** For horizontal companies, an important way to get recurring revenue on their software is to charge for service and support on those products. Consulting services are also a major revenue generator. Illustrating a typical example for the size of this revenue source, 37% of **i2's** (Nasdaq: ITWO) sales in the most recent quarter were thanks to services and maintenance fees.

- **Transaction fees, listing fees.** These sources of revenue are among the most attractive to the vertical companies who are interested in e-commerce. Whenever a classified listing is created or an auction completed, the vertical companies take a small commission on the sale.

- **Advertising.** This is also an important revenue source for most vertical sites since many of them are content-driven today. The vertical sites can also charge fairly high rates for their space since their ads are placed with a highly targeted and motivated audience.

WHY THE BUSINESSES ARE ATTRACTIVE

If you're wondering why there is so much excitement surrounding B2B, it is because the businesses have some fairly attractive attributes. Let's now take a look at some of those qualities.

- **Huge market opportunity.** Most of the companies in existence are still fat and inefficient. The B2B firms are offering what are essentially miracle weight-loss systems. We have no reason to doubt the sky-high predictions of the market opportunity published by Forrester Research.

- **Financially light business models.** Just like most other Internet-related companies, the B2B service firms have financially light business models, meaning they carry very little (if any) physical inventory and do not have to invest in costly factories.

- **Scalable.** Going hand-in-hand with having light business models, most B2B firms have highly scalable businesses. Once a software product is made or a vertical auction market created, the cost side of the equation does not change much, even at extraordinarily high volumes. This means there is a great deal of operating leverage built into these businesses, and the profit potential is explosive.

- **Acquisition costs/network effect.** Once critical mass is achieved in a vertical market, customer acquisition costs should plummet. This is thanks to the same network effect that has kept eBay atop the C2C auction vertical. Moreover, companies engaging in electronic commerce are going to have a major cost advantage over those doing things the old-fashioned way with pen, paper, and snail mail. Most verticals will be "winner takes most" markets, and the winners in any given niche are going to find it very easy to defend their positions.

- **Sticky products.** Once a company has made the upfront investment to join a B2B market, it will be reluctant to change. In addition, since we believe most verticals will be "winner takes most," there are going to be very few viable alternatives within any given vertical. Customers of the horizontal providers also have high switching costs. Beyond the upfront investment in the software, most companies will find their operations intimately united with those products.

- **Multiple revenue streams.** Most B2B companies are going to be harvesting revenue from several different sources. Auction sites can start to put advertising on their pages, while advertising-driven content sites can start offering e-commerce. A B2B company building one revenue stream will likely see others branch off.

WHAT TO LOOK FOR

With a topic as large as B2B, we are forced to talk in very vague terms. Hopefully, we've given an investor new to the idea of B2B a framework of how exactly to start looking at these companies. Now, we'll share what we think are some of the more important attributes to look for in potential investments.

- **Traction.** When we say "traction," we mean that we want our companies acquiring customers (both buyers and sellers) at a decent rate. This means not only looking closely at the company press releases for customer metrics, but also expecting significant sequential sales growth. If there isn't at least 10% sequential sales growth in each quarter, the company is probably losing the traction and acceleration needed to attain critical mass against its competitors.

- **Strategic partnerships.** Just like in the rest of the world, it's not what you know, but who you know. Companies like VerticalNet and **Internet Capital Group** (Nasdaq: ICGE) can bring several companies under one umbrella to share expertise, create marketing alliances, generally reduce costs, and increase intelligence.

- **A large war chest.** This means having enough cash to quickly acquire customers. Being public gives companies greater liquidity and visibility via Wall Street and the media.

- **Technology platform.** It is particularly important for B2B companies to have a platform that is robust, scalable, secure, and able to flawlessly process billions' worth of transactions. For the vertical companies, this generally means teaming up with horizontal companies that specialize in different areas.

- **Leaders, leaders, leaders**. If we had to summarize what we look for in one sentence, it would be this: We are looking for leaders and shying away from the second- and third-tier players. There are several reasons for this, but probably the most important is the network effect. Leaders tend to have many of the above qualities that may be more difficult for the laggards to come by.

CONCERNING VALUATION

About the only real measure of valuation we can use today is the price-to-sales ratio (PSR). The PSR gives us the faintest of clues as to companies' valuations relative to one another, but the conclusion regarding absolute valuation is almost identical for all the companies — they're all expensive.

However, these are all very early-stage companies, and buying into the company with the right business plan or the best positioning is the most important right now. In short, investors in the B2B sector are forced to think more like venture capitalists than value investors.

THE NEXT MICROSOFT

While B2B is indeed a quite attractive sector, it's worth noting that not every company will be able to have a 70% market share in its market. This is especially important to keep in mind with the horizontal companies, many of which are angling for the same piece of the pie. Either way, it is important with all B2B companies to keep track of the competitive landscape.

Within the individual vertical markets, there should be much less competition thanks to the network effect discussed earlier. However, there are literally hundreds of different vertical markets, and there are likely to be dozens of companies serving each peacefully side-by-side. In other words, VerticalNet's wateronline.com does not compete with the life sciences vertical of **Ventro** (Nasdaq: VNTR), which does not compete with cattle vertical of **eMerge** (Nasdaq: EMRG). However, vertical companies tend to operate in many different verticals, and before long there will likely be several different companies vying for the same placement within any given industry.

SUMMARY

The opportunities are without a doubt astonishing within B2B, and Wall Street is partially justified in going ga-ga over the limited number of B2B-focused companies now in existence. However, just like in the early days of the Internet, for every AOL and Microsoft, there will be fading stars like Prodigy and Netscape. In other words, the losers will far outnumber the winners, and we are smart to choose carefully.

Looking at B2B today is like looking to invest in the PC industry in 1988 or the consumer Internet companies in 1994. Unfortunately, many of the B2B companies already carry valuations that are several years ahead of their time. It's always important to study carefully and be picky about what to purchase in the stock market, and that's especially true here. That said, there are few sectors that have as bright a future as B2B, and studying the industry further will surely be worth the effort. After all, the companies that lead their respective niches have an awesome chance of creating significant cash flows with nicely guarded moats around their businesses.

The Internet is an invention that begets more inventions. The B2B sub-invention may just be the most profound in our times. Everyone will benefit — suppliers, producers, and even consumers. The advent of ubiquitous B2B e-commerce will grease the wheels of the economy, making it more efficient. As efficiencies trickle down, it will allow us as consumers to enjoy more products and services for less work. That is a beautiful thing and worth investigating further for potential investment.

PROFILES OF THE MAJOR B2B PLAYERS

Now that we have a framework of how the B2B industry is constructed, here is a quick summary of some of the major B2B players that have publicly traded shares. Think of it as a "who's who" in the B2B industry and a starting point for further research.

- **Ariba** (Nasdaq: ARBA); www.ariba.com
  Ariba is one of the leading suppliers of software that allows

B2B Company Valuation Snapshot

Company	Ticker	Type of B2B	Stock Price	Next Year's Est. Earnings	Forward PE Ratio	Market Capitalization	Sales Run Rate	Ratio
Internet Capital Group	ICGE	Incubator	$119 1/16	NA	NA	$31,128.9	$6.8	4577.8
Ariba	ARBA	Horizontal	$329 31/32	$(0.52)	NA	$29,984.3	$93.9	319.3
Siebel	SEBL	Horizontal	$154 23/32	$0.73	211.9	$29,823.9	$42.1	708.1
I2	ITWO	Horizontal	$170 3/4	$0.35	487.9	$26,269.2	$701.1	37.5
Bea Systems	BEAS	Horizontal	$126 1/4	$0.33	382.6	$19,995.5	$596.7	33.5
CommerceOne	CMRC	Horizontal	$235 1/16	$(0.94)	NA	$16,968.2	$67.6	251.2
MicroStrategy	MSTR	Horizontal	$188	$0.25	752.0	$14,498.6	$277.4	52.3
Vitria	VITR	Horizontal	$177 7/8	$(0.15)	NA	$11,250.8	$48.8	230.6
VerticalNet	VERT	Vertical	$251 23/32	$(1.70)	NA	$8,962.7	$40.4	222.1
Ventro	VNTR	Vertical	$220	$(3.20)	NA	$7,213.4	$77.1	93.5
FreeMarkets	FMKT	Horizontal	$204 13/16	$(1.20)	NA	$6,933.9	$31.4	221.0

(As of 3/4/00)
Sources: S&P Comstock, I/B/E/S, Company Filings

companies to connect to their suppliers and buyers. Its Operating Resource Management (ORM) products help companies track supply purchases over the Internet. In addition, it can automate and digitize the purchasing activities of a company and can also integrate with custom forms and expense reports, helping to make the dream of a paperless office that much closer to reality. The company is a true horizontal B2B company since its products and services are used in numerous different industries.

Ariba has many large companies using its products including everyone from consumer products company **Unilever** (NYSE: UL) to travel-booking company **Sabre** (NYSE: TSG). There's a reason that Ariba is one of the most richly valued B2B companies, and that's because its products (along with those of competitor CommerceOne) are aimed at cutting fat where businesses tend to be the chubbiest.

- **BEA Systems** (Nasdaq: BEAS); www.beasys.com
BEA Systems bills itself as "The E-commerce Transactions Company." In a nutshell, BEA provides a variety of software and services that enable other companies to offer electronic commerce. Most of BEA's software is considered middleware, which is software that essentially glues together a dispersed network made of widely different computer systems. This "glue" allows the network to effectively handle a high volume of transactions as a single unit. Among BEA's most popular products are the WebLogic family and BEA Tuxedo. The company claims Tuxedo is the world's most widely deployed e-commerce transaction platform.

BEA's client list includes many of the heavies of the e-commerce industry, including such leaders as **Amazon.com** (Nasdaq: AMZN), FedEx, and **E*Trade** (Nasdaq: EGRP).

BEA was founded back in 1995 by a couple of former **Sun Microsystems** (Nasdaq: SUNW) executives named Bill, Ed, and Alfred — hence the BEA name. Most of BEA's products were not originally produced by the company but were acquired from other firms. Much of the money used in these acquisitions came from money management firm Warburg Pincus. Warburg is BEA's largest single shareholder, owning just under half of the company's equity.

- **CommerceOne** (Nasdaq: CMRC); www.commerceone.com
CommerceOne is locked in a heated battle with Ariba to control how businesses go about procuring supplies online. The company sells software that connects buyers and suppliers of business goods and services, all using the Internet. Its products simplify the buying process by providing product catalogs from different suppliers, automating purchase order approvals, and making management easier by enforcing specific policies of both buyers and sellers. It also does a fair amount of hosting via MarketSite.net, which enables buyers and sellers using different software to connect and perform online transactions. In addition, CommerceOne provides numerous ancillary B2B services such as content management, order tracking, and transaction information support.

Much like Ariba, CommerceOne is aimed at slimming down one of the fattest and most inefficient parts of most businesses — raw goods procurement. It is a horizontal company since its products are used across numerous different industries. The company's stock is up more than 10-fold since its July 1999 IPO.

- **FreeMarkets** (Nasdaq: FMKT); www.freemarkets.com
FreeMarkets is to B2B what eBay is to C2C. FreeMarkets is the largest site for B2B auctions around the world. Over the past five years, over 3,000 companies from 45 countries have participated in a FreeMarkets auction. The company operates in approximately 70 different vertical industries, offering industrial parts, raw materials, commodities, and services on its auction platform. Just about anything from injected plastic to tax services to circuit boards can be traded on FreeMarkets.

FreeMarkets is also a horizontal company since its can, in theory, run auctions related to just about any industry. FreeMarkets also offers support services for its buyers and sellers and is a little bit more "hands on" in its auctions than eBay. It also operates reverse auctions where suppliers can

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place bids to fill an order. The company was founded in 1995, and came public in December 1999.

- **Internet Capital Group** (Nasdaq: ICGE); www.icge.com
Probably the best way to describe Internet Capital Group is to call it the "land barron" of B2B e-commerce. Other monikers that might fit include "angel investor" and "incubator." The company has essentially no operations itself but is actively involved in the industry through its investments in numerous other B2B e-commerce companies. As of this writing, the company has approximately 55 B2B partners/investees in its portfolio. Its largest and most lucrative investment is its 35% ownership stake (worth $3.1 billion) in this issue's focus company, VerticalNet. Internet Capital also owns significant stakes in **Breakaway Solutions** (Nasdaq: BWAY) (about 30%, or $0.7 billion), **Onvia** (Nasdaq: ONVI) (about 22%, or $1 billion), and eMerge (about 21%, or $0.4 billion). In addition, it owns stakes in many other pre-IPO B2B companies that operate both vertically and horizontally.
The best way to value Internet Capital is not to look at its sales and earnings since accounting rules really don't allow the company to record any revenue from its partners. Rather, it is best to add up the value of the company's investments and then compare that to its market capitalization.
It is not much of a stretch to say that Internet Capital Group stands to profit the most if B2B continues to be white hot on Wall Street. Few companies are better positioned to benefit from the industry's overall success. Likewise, Internet Capital will be hurt if its partner companies take a nosedive. It is a firm that is really best viewed as a basket of other B2B companies, and it's probably worth taking a further look at the company for those interested in the overall industry.

- **i2** (Nasdaq: ITWO); www.i2.com
i2 is a company that attempts to help other businesses learn to make "better decisions, faster" than their competitors. The company's RHYTHM software product helps companies manage their supply chains. This allows companies to plan and schedule raw materials procurement, production, and product delivery using "just in time" manufacturing in an attempt to optimize efficiency in the process. Much like Cisco Systems, i2 has bought numerous other companies in recent years to complement its product offerings.
i2 was founded in 1988 and came public in 1996. The company has seen sequential sales growth in every single quarter since coming public, and has also strung together four straight profitable years. i2 is a titan in the supply-chain market, and is among the oldest and most experienced of the horizontal B2B suppliers.

- **MicroStrategy** (Nasdaq: MSTR); www.microstrategy.com
MicroStrategy makes software and related products that allow its clients to analyze specific data from databases that log a high volume of transactions, including both online sites as well as from corporeal world cash registers. The information created by MicroStrategy's software is then used by its clients to analyze trends in customer behavior. This information can then be used to customize marketing plans. MicroStrategy tries to make businesses smarter with the customer and market data they have at their disposal.
Similar to competitor i2, MicroStrategy is now profitable and has shown some stunning growth over the past two years. The company's stock is up over 20-fold since coming public in June 1998.

- **Siebel Systems** (Nasdaq: SEBL); www.siebel.com
Siebel Systems is a leading provider of sales automation and customer service software. The company's software allows the access of client information and decision support either through an intranet or over the Internet. In essence, Siebel's products extend the power of a company's sales force by providing critical and proprietary information to remote places.
Siebel Systems was founded by a former **Oracle** (Nasdaq: ORCL) executive, Thomas Siebel, back in 1993. The company dominates its sales-support niche, but is trying to extend is business offerings by moving into supplying customer service and marketing automation products. Siebel Systems is among the fastest growing software companies in the nation, going from $39.1 million in sales in 1996 to $762 million in 1999.

- **Ventro** (Nasdaq: VNTR); www.ventro.com
Ventro recently went through a name change and used to do business under the moniker "Chemdex." The company's main business is that it is a vertical market maker in the life sciences industry, selling equipment and supplies to biotechnology companies and universities. The reason the company changed its name is because it intends to expand into other verticals, using the platform it designed for its life sciences sites in other industries. Beyond the life sciences sites run by Chemdex, Ventro also owns Promedix (specialty medical), Broadlane (healthcare supply), and Industria Solutions (fluid processing).

- **VerticalNet** (Nasdaq: VERT); www.verticalnet.com
VerticalNet is the leading operator of vertical trade communities within numerous different industries. The company's sites tend be very narrowly targeted and attract buyers and sellers by specializing content and commerce for individuals and companies with similar professional interests. VerticalNet is our focus company in this issue.

- **Vitria** (Nasdaq: VITR); www.vitria.com
Vitria Technology makes software applications that allow various computers to talk with each other in a large corporation's network. Vitria's enterprise application

integration software is similar to that offered by BEA Systems in that it is "middleware" that glues different computer systems together so that they can work and communicate as one cohesive unit. Vitria's software also allows a company to automate the fulfillment process, digitize (e-mail) status reports of service requests, and securely allow proprietary information to be accessed over the Internet. It is a horizontal company that is targeting the B2B e-commerce in the later stages where products and services near the consumer realm.

Focus Company

BY JEFF FISCHER (JEFFF@FOOL.COM)

VERTICALNET

VerticalNet, Inc.

Ticker and exchange:	Nasdaq: VERT
Stock price as of March 10, 2000:	$273.19
Trailing 12-month sales:	$20.75 million
Trailing 12-month net income:	-$39.87 million
Estimated 3-to-5-year annual EPS growth rate:	100%
Forward consensus EPS estimates:	
FY2000	($1.70)
FY2001	($0.19)
First estimated to be profitable:	Q3 '01 or Q4 '01
Stock Specifics	
Approx. shares outstanding:	35.9 million
Estimated amount of shares held by institutions:	39%
Approx. float (shares available for trade):	14.8 million
Market capitalization:	$9.6 billion
Cash and equivalents (12/31/99):	$58.7 million
Long-term debt:	$116.7 million
Company Information	
Muriel Lange, Director of Investor Relations	
700 Dresher Road	
Horsham PA 19044	
(2150 315-3367	
mlange@verticalnet.com	
www.verticalnet.com	
Last earnings report:	February 1, 2000; reported 4Q '99 revenue of $10.1 million
Next earnings report:	Mid-April, 2000
Estimated results for next quarterly report:	$18.2-20.2 million in revenue, $0.49 loss per share
Next stock dividend:	2-for-1 stock split, effective 3/31/00

VERTICALNET'S STOCK PRICE SINCE ITS IPO

Founded in 1995, VerticalNet was the first business-to-businesss e-commerce company focused exclusively on the needs of industrial markets. At last count, the company ran 57 individually branded websites, each of which provides content, community, and, increasingly, e-commerce to industrial audiences. VerticalNet's first website, wateronline.com, was launched in 1995. The company has since launched nearly five dozen new sites, more than half of them in 1999, grouped under the 10 headings of Advanced Technologies, Communications, Environmental, Food and Packaging, Foodservice, Hospitality, Healthcare and Science, Manufacturing and Metals, Process, and Service.

VerticalNet derives its name partially from the vertical nature of its online sites, each of which provide end-to-end solutions, beginning with content, leading "up" to community and ending in transactions. VerticalNet's formula for online success is:

(Content + Community + Commerce) x Strategic Partnership = VerticalNet Success

With regard to commerce, the company is focused on creating communities that drive demand to product suppliers, or, in other words, that match new and incremental buyers with existing suppliers.

To our eyes, VerticalNet is pursuing one of the most aggressive online business-to-business commerce strategies among its peers. Not only is the company addressing several dozen industries, but it also offers website creation, management, and hosting services for thousands of companies and trade organizations. Called "storefronts," VerticalNet recently hosted nearly 3,000 such properties as well as related "e-commerce centers" for clients. VerticalNet creates and hosts the sites for several thousand dollars in monthly fees apiece. As management says, "If you are looking to create an interactive megasite offering online commerce, company databases, catalogs or communications, let VerticalNet's expertise build your online presence."

Meanwhile, on its wholly owned, proprietary websites, each of VerticalNet's trade communities provide:

- **Content:** Editorial content is updated daily on each site and includes white papers written by industry leaders, timely industry news, product information, industry directories, classified advertisements, interactive software, job listings, and more. The idea is to build "sticky" content that makes customers return repeatedly.

- **Community:** Over 40% of VerticalNet's traffic is international, so the company's sites congregate industry professionals from all around the world. On VerticalNet's sites, professionals can monitor industry events, exchange thoughts, create new relationships, find career opportunities, communicate with like-minded professionals, and more.

- **Commerce:** All of VerticalNet's websites foster an environment for buyers and sellers to conduct business. Increasingly, VerticalNet is making this possible with new commerce software that it will likely institute across all of its sites over the course of 2000 and early 2001. (The focus of its first four years was to build content and community, and now commerce is the big focus.)

Overall, VerticalNet is working to leverage the Internet's interactive nature and global reach to create multinational business communities and commerce exchanges in every industry that it targets. While many business-to-business e-commerce hosts, such as Chemdex.com, focus primarily on one or two related industries, VerticalNet will continue to open (or acquire) new industry sites as long as it appears attractive to do so. In 2000, the company could surpass 65 sites serving at least 65 industries.

HOW DOES THIS COMPANY MAKE MONEY?

An important question that all Foolish investors should ask of any company they study is, "How does this company make money?"

Ads

To date, most of VerticalNet's revenue has been derived from advertising. Advertising is a steady stream of revenue because the company typically signs year-long contracts with advertisers (when it doesn't, it signs three-month contracts) and, to date, VerticalNet's customer retention rate is 90%. This means that 9 out of 10 advertisers have continued to advertise with VerticalNet after their first contract expired. VerticalNet had $20.75 million in revenue during 1999, about 90% of it from advertising, and it had $9.7 million in deferred revenue at the end of last year, again most of it ad revenue.

Deferred revenue represents ad sales that are guaranteed by contracts but not yet booked because the ads will run over the length of the contract. Advertisers on VerticalNet sites are typically mid-size to large businesses, ranging from aerospace firms to computer chip companies, who advertise on any industry-related sites. Online advertising of this sort could grow into a $10 billion industry by 2002, according to IDC Corp., up from an insignificant few hundred million dollars in 1998. VerticalNet is very well-positioned to participate in business-based advertising across several industries.

Storefronts

A second source of revenue is derived from building and hosting storefronts for businesses. VerticalNet hosted 2,903 storefronts at the end of 1999, for 1,795 different clients. Due to recent strategic deals, including a partnership with **Microsoft** (Nasdaq: MSFT), VerticalNet is guaranteed to host over 85,000 storefronts before 2004. (That's right, 85,000 — not 8,500.) As with VerticalNet's advertising contracts, storefront contracts are typically a year long, thereby providing investors great visibility regarding annual revenue.

E-Commerce

A third source of revenue is e-commerce transaction fees. This currently includes fees collected from existing auction services on VerticalNet sites, and from referral commissions earned on the sale of books, software, and other goods on third-party websites. VerticalNet is only now beginning to offer broad e-commerce solutions across many of its sites, using the technology it gained in a key 1999 acquisition, so this revenue stream is the smallest of the three, but it promises — if met with success — to eventually be the largest.

VerticalNet's Business-to-Business Websites

Advanced Technologies
Aerospace Online
Autocentral.com
ComputerOEM Online
Embedded Technology.com
Plant Automation.com
Semiconductor Online
Test and Measurement.com

Food Packaging
Bakery Online
Beverage Online
Dairy Network.com
Food Ingredients Online
Food Online
Meat and Poultry Online
Packaging Network.com

Manufacturing & Metals
Machine Tools Online
Metrology World.com
Safety Online
Surface Finishing.com
Tooling Online

Communications
Digital Broadcasting.com
EC Online
Fiber Optics Online
Premises Networks.com
RF Globalnet
Wireless Design Online
Wireless Networks Online

Foodservice & Hospitality
Foodservice Central.com
E-Hospitality.com

Service
HR Hub.com
Property and Casualty.com
PurchasingNetwork.com

Process
Adhesives and Sealants.com
Chemical Online
Hydrocarbon Online
Oil and Gas Online
Paint and Coatings.com
Pharmaceutical Online

Environmental
ElectricNet
Pollution Online
Power Online
Public Works.com
Pulp and Paper Online
Solid Waste Online
Water Online

Healthcare/Science
Bioresearch Online
Drug Discovery Online
E-Dental.com
Home Health Provider.com
Hospital Network.com
Laboratory Network.com
Labx.com
Long Term Care Provider.com
Medical Design Online
Nurses.com

Other
Oil Link.com
Industry Deals.com
IT Career Hub.com
Professional Store.com

Main Revenue Sources

	Q3 1998	Q4 1998	Q1 1999	Q2 1999	Q3 1999	Q4 1999
Advertising	$897	$1,209	$1,876	$3,374	$4,700	$7,133
e-Commerce & related	$0	$64	$58	$178	$482	$628
Number of websites	28	29	35	43	51	55
Number of storefronts	1,094	1,313	1,600	2,094	2,676	2,903

Sales in thousands.
Source: Company documents, Robertson Stephens.

E-commerce revenue is estimated to represent as much as 50% of total revenue at VerticalNet by the end 2001, and considerably more in future years. As our industry report discussed, the estimates for online business-based commerce are so large that it is almost pointless to cite them. There are many estimates out there, all large, but according to Forrester Research, online business-to-business commerce could reach $843 billion in total sales by 2002, up from $43 billion in 1998. Commissions for e-commerce hosts clearly stand to be substantial.

Other sources of revenue at VerticalNet include career planning and education services that are targeted at each vertical community.

If VerticalNet continues to be a well-run company, its primary revenue streams (namely advertising, commerce, and site-hosting fees) could represent high margin, stable, and recurring sources of cash flow.

HOW CAN VERTICALNET GROW TO CREATE LASTING VALUE?

VeritcalNet shares the same fate of all online commerce companies, meaning it must increase site traffic if it is going to grow sales and thrive. The company appears to be at an advantage with many of its industry-specific sites because it was the first mover in building and offering the services, and because it offers daily content that is building "community." Once a community on a site becomes large enough, it becomes self-perpetuating. Professionals in the industry will tell other professionals about the site, and it will thereafter grow by word of mouth.

As a community grows, its usefulness grows by the square of the number of people involved (Metcalfe's Law of Networks, discussed in the "Industry Analysis" section of this report). In the case of VerticalNet, its sites become increasingly useful for job-seeking, industry discussion, and commerce as each community becomes larger. Once a site reaches a certain size (or critical mass — which will prove different for each industry), competitors seeking to serve the same industry face barriers to entry. VerticalNet is most likely beginning to hit critical mass at some of its oldest websites, but it is difficult to know because numbers are not shared on a site-by-site basis. For now, we need to rely on the company's total revenue growth as an indication of early, and growing, success.

How can VerticalNet continue to grow? First off, VerticalNet wants to participate in dozens of industries that will reach billions of dollars apiece in annual e-commerce sales, but that currently only have small online beginnings. By putting itself in front of a giant tidal wave just as the wave is beginning to form, VerticalNet is hoping to catch a great, big, sloshing bucketful of business. Second, to capitalize on the long-term possibilities and build a lasting, value-creating business, management is adeptly pursuing strategic acquisitions, forming key partnerships, and starting new initiatives.

VerticalNet Quarterly Revenue Growth

	1996	1997	1998	1999
Q1	$0	$163	$377	$1,934
Q2	$0	$197	$587	$3,551
Q3	$0	$191	$898	$5,182
Q4	$0	$241	$1,273	$10,090
Total Revenue	$0	$792	$3,135	$20,757

Three-year sales growth rate: 480%

Sales in thousands.
Source: company documents.

Acquisitions

Since going public in January 1999, VerticalNet has made several sizable acquisitions.

- **NECX**. In November 1999, VerticalNet announced that it would acquire NECX, a business-to-business commerce leader in electronics and computer products. In its prior year, NECX had $350 million in gross merchandise sales and $37 million in transaction revenue. The company primarily conducts its business over the telephone, but VerticalNet is moving NECX online, integrating much of the company's sales into VerticalNet's exsiting communities focused on technology. NECX helps technology companies sell excess inventory.

- **Isadra.** VerticalNet purchased Isadra in August of 1999. This acquisition was integral in VerticalNet's emerging e-commerce initiative. Isadra designs comprehensive e-commerce software personalized for each user, allowing for convenient shopping in one place online. VerticalNet is expected to use this technology widely across all of its online properties.

- **Labx.com.** Labx.com was a leading commerce community focused on scientific laboratory equipment. VerticalNet acquired it and its 45,000 users in July 1999, and is integrating the service into its existing healthcare vertical communities.

- **RFGlobalNet.** VerticalNet acquired RFGlobalNet, a wireless communications portal, to integrate into its technology communities.

- **Infomatrix.** This "property and casualty" vertical community was purchased and integrated into VerticalNet as well.

- **SafetyOnline, TextileWeb, GovCon.com.** Same deal with these three vertical websites. We expect several more acquisitions of this nature.

PARTNERSHIPS

In the first two months of 2000 alone, VerticalNet announced four key partnerships involving Microsoft, Softbank in Japan, and both **British Telecom** (NYSE: BTY) and Internet Capital Group in Europe. These partnerships and others demand review.

- **IBM.** In the fall of 1999, VerticalNet agreed to promote **IBM** (NYSE: IBM) across its communities while committing to use IBM servers for its business. As part of the deal (a classic business case of "I rub your back, you rub my back"), IBM agreed to pay $1.5 million for 375 VerticalNet storefronts by the winter of 2000. IBM will also spend $500,000 for advertisements on VerticalNet property.

- **Microsoft.** When VerticalNet's deal with Microsoft was announced, the stock leapt over 30%, adding a few billion dollars in market value. Making its largest investment in business-to-business e-commerce to date, Microsoft invested $100 million in VerticalNet (via preferred stock) and the software giant has warrants to purchase another $104 million of VerticalNet stock within three years. In addition, Microsoft entered a binding three-year business contract with VerticalNet.

  Microsoft will purchase approximately 80,000 storefronts and e-commerce centers from VerticalNet at a discounted rate, 20,000 of which should be live before the end of 2000. This deal is expected to result in $225 million in additional revenue at VerticalNet over the next three years. Considering that VerticalNet had only $20 million in total revenue last year, the impact of the deal is enormous

  As part of the agreement, VerticalNet will spend $135 million with Microsoft over the same period, broken down approximately as follows: $60 million for advertising on Microsoft-related sites; $56 million in software licensing fees; and $19 million for technology development. VerticalNet will also pay royalties to Microsoft on renewals of storefront contracts that were initiated by Microsoft.

  Finally, a senior executive from Microsoft is also joining VerticalNet's board of directors. Microsoft is promoting its online business software aggressively, and in VerticalNet it has found a new friend to help its cause. In the process, VerticalNet went from being a company that expected to reach breakeven results with its operations in the middle of 2002 to a company that expects to reach breakeven by mid-2001, about a whole year earlier. Very nice. (Now attempt to estimate the long-term value of 80,000 storefronts. Extra nice.)

- **3M.** VerticalNet formed an agreement with **3M** (NYSE: MMM) in November of 1999 that providers VerticalNet users access to 3M's products online. The upside: 3M taps into a large, widespread, new sales channel, while VerticalNet will gain advertising and transaction fees from 3M, as well as strong brand association.

International

- **British Telecom and Internet Capital Group** (VerticalNet Europe). On February 1, 2000, VeritcalNet announced the formation of VerticalNet Europe, a new company that will work to duplicate the VerticalNet business model across Europe. Working in a $227 million partnership with British Telecom and Internet Capital Group, VerticalNet Europe will initially create 6-10 websites serving the United Kingdom. A meaningful financial impact is not expected from VerticalNet Europe until late 2001 at the earliest, but tapping the long-term potential is of course the objective. (By the way, The Motley Fool's May 2000 *Internet Report* will cover the young industry dubbed "Internet incubators," or investor-companies, including Internet Capital Group, which happens to be VerticalNet's largest shareholder.)

- **Softbank** (VerticalNet Japan). A joint venture with Softbank in Japan, announced on January 17, 2000, will be called VerticalNet Japan Kabushiki Kaisha (say that 10 times fast). As with VerticalNet Europe, the objective is to create vertical communities modeled after VerticalNet's U.S. operations, but meant to serve Japanese businesses. This partnership was widely applauded, even though a positive financial impact is not expected until 2001 at the earliest.

Summary

Led by a CEO who hails from America Online, VerticalNet's management has been very savvy in making smart acquisitions at reasonable costs, creating valuable partnerships, and pushing into international markets with strong partners. Combined, the company's strategies appear to be hitting on all cylinders early in the race. This doesn't guarantee that VerticalNet will succeed, of course, but it certainly helps the company's chances.

Selected Business Partners

3M
Biz Travel
British Telecom
ComTex
Deja News
IBM
Intellicast
Internet Capital Group
Metropolis
Microsoft
SAIC
Softbank

Source: VeritcalNet website.

RISKS AND REWARDS

Although online business-to-business commerce promises to grow like a jungle and VerticalNet may appear to be a young King Kong, not all is rosy and certain. Risks and uncertainties abound like kangaroos in Australia.

First, unlike most business-to-business, e-commerce-hosting competitors, VerticalNet is attempting to host commerce across several industries — in fact, several dozen industries — and VerticalNet's sites will compete with companies that focus exclusively on one industry. Focused competition could eat VerticalNet's lunch in many of the industries that the company is working to address. Plus, investors don't truly have a way to gauge whether or not this is already happening. Overall, it isn't unrealistic to assume that some of VerticalNet's properties will ultimately fail, resulting in a closure or a sale. This would lead to special charges on the books and negative press for VerticalNet.

VerticalNet is also the most editorial-centric business-to-business e-commerce company that we know of. The creation of daily content is neither inexpensive nor easy. The costs to remain current with each industry and the cost of maintaining daily, high-quality content across dozens of websites will be challenging on a continual basis. Even America Online has preferred to run externally created content rather than create its own.

Our next concern regards the industry itself and the competition. Business-to-business e-commerce is only just emerging. Therefore, uncertainties surround the industry. Which business models will lead, vertical or horizontal? Will manufacturing companies merely work together online, essentially cutting out "middle" sites such as VerticalNet? Michigan's largest automakers recently agreed to work online together. In a similar vein, does a company like Cisco or General Electric need a company like VerticalNet? Perhaps only if the competition is finding success on VerticalNet will other industry leaders need to utilize the service, too.

Our next concern regards new initiatives. VerticalNet is interested in opening new websites to serve different industies and it has partnerships to start businesses focused in Japan and Europe. How well any new initiative will perform is always an uncertainty, typically for at least a few years.

Our final two concerns shouldn't be surprising: profitability and valuation. VerticalNet is expected to turn profitable by the third or fourth quarter of 2001, approximately seven quarters from now. If profitability is delayed, the stock will likely suffer. When the company does become profitable (assuming it does), it is expected to achieve very strong profit margins, with its gross margin topping 80%. Some analysts even estimate a gross margin of 90%, which would rival Yahoo! and Microsoft. This isn't impossible, but we'll believe it when we see it.

Finally, there is valuation. VerticalNet was recently valued above $8.9 billion. Any company with $20 million in trailing revenue, shareholder equity of a few hundred million, and a valuation of over $1 billion (let alone $9.6 billion!) is trading at a steep valuation on any traditional measure. Believe it or not, however, VerticalNet is one of the lower priced, top-tier companies in its industry, which is one of the reasons we chose to feature. As long as investors are bullish about the potential of business e-commerce, and as long as companies continue to grow rapidly, the leading stocks are likely to continue to trend higher. However, VerticalNet's valuation still presents great risk. We'll look at valuation in our next section. To refresh your memory regarding peer valuations, see our table on page 9.

Reward Factors

- **Diversified business strategy.** Unlike many competitors, VerticalNet didn't put all its eggs in one basket. By addressing nearly five dozen industries so far, the company ensures that even if it fails in some industries, it should still succeed in others. VerticalNet is arguably the most diversified business-to-business e-commerce company on the market.

- **Content advantage.** VerticalNet has differentiated itself from most competition by offering daily content on its trading communities. VerticalNet hopes that its daily content will keep buyers and sellers returning and increase the utility of its sites, resulting in more traffic and more trade than sites offering just trade alone.

- **A young, high-growth industry.** Business-to-business e-commerce is only beginning to get its wings and VerticalNet is well-positioned to catch flight with the industry. The growth prospects are enormous over the next decade for leaders.

- **International partners.** Investors applauded the stock when VerticalNet announced partnerships with Softbank in Japan and British Telecom and ICG in Britain. The company is on solid footing for international expansion.

- **High-margin business model.** Though unprofitable so far, the groundwork is being laid for VerticalNet to become a high-margin business, with gross margins that could equal eBay's at over 80%.

Risk Factors

- **Far-spread strategy.** By trying to address several different industries, VerticalNet may become an "apprentice" in many and a master of none, losing the lead in each industry to new companies that have a much tighter focus.

- **Content expenses.** Daily content is typically expensive and resource draining. VerticalNet argues that content is key to creating community and commerce, but sites including eBay have shown that commerce can grow without much content, too, possibly putting competitors without content at an advantage.

- **Highly uncertain industry.** The current business models that address online business-to-businesss commerce may not stand the test of time. Many new twists could occur before the ideal trading format is found across various industries, making VerticalNet vulnerable.

- **New initiatives.** New initiatives are expensive and invite risk, and VerticalNet is engaged in dozens of them, both domestically (over two dozen of its websites are less than a year old) and now internationally.

- **Profitability and cash needs.** Profitability is expected before the end of 2001, but the potential exists for failure to reach profits. Plus, due to current operating losses, it is very likely that VerticalNet will need to raise additional capital in 2000 via a debt or stock offering. If profits are delayed, even more cash will likely need to be raised.

- **Valuation.** The company's valuation appears aggressive on traditional measures, decreasing the risk-to-reward scenario.

- **New developments.** Overall, how business-to-business e-commerce will develop is a question no one can answer with certainty. VerticalNet's management will need to be extremely adaptable over the next decade if the company is to survive, let alone lead.

THE ENIGMA OF VALUATION

When this Fool read three different institutional research reports on VerticalNet, each report without fail addressed VerticalNet's valuation with merely a comparative analysis to peers — peers that have no more valuation certainty than VerticalNet. Plus, each report attributed no more than one or two paragraphs to the entire issue of valuation. It appears that we truly do live during the golden age of stock investing — valuation doesn't matter! In all seriousness, however, the Wise weren't completely incorrect to all but brush over valuation in this case. In fact, some arguments exist for doing just that.

A company is best valued on the amount of positive earnings it can create over the life of an investment. Valuing a company on earnings power usually works best when the company being valued is established and has a reliable stream of earnings and a predictable growth rate. Thus, trying to value a young, profitless company that has the potential to serve many large markets, all of them growing extremely rapidly for the next decade, is a nearly pointless endeavor. A "fair" valuation almost certainly can't be determined with any accuracy. That said, the following is how one of the largest, most respected institutional Wall Street firms recently addressed VerticalNet's valuation:

"VERT shares are currently trading [at $252] at 125 times our estimated preliminary calendar 2000 gross profits.... Its comparable company peer group is trading at 115 times 2000 estimated gross profits. If VerticalNet can hold at least its peer group multiple, 12 months from now it could be trading at 115 times our preliminary 2001 gross profit estimate of $145 million (mid-point range). This translates to a $350-plus stock price (or $175 post-split). [Reminder: the stock splits March 31.] Therefore, we are raising our 12-month price target for VERT to $350 (or $175 post-split) from $250."

So, after looking at VerticalNet's peer group and averaging its multiple to gross profits, this large investment house put a price target of $350 per share on VerticalNet, or about $12.6 billion. If only it were that simple!

In reality, comparative analysis of this kind is grossly simplistic and could prove highly misleading. Just because a basket of peer stocks is trading at a certain multiple doesn't mean they will continue to do so. They could easily all sink together. So, it is actually much more meaningful, in our opinion, to instead value a young company like VerticalNet as a whole. In doing this, we want to ask, "What does VerticalNet's $8.9 billion market valuation say to you?"

Knowing the projected size of business-to-business e-commerce, the industries VerticalNet is addressing, and understanding VerticalNet's strategic position and initiatives, do you believe that the company's 5- to 10-year potential is already priced into its $8.9 billion valuation? Or, do you believe that the company could create considerably more long-term value?

THE BACK OF THE ENVELOPE, PLEASE

Revenue estimates for VerticalNet in 2000 average $114 million. In 2001, revenue is expected to nearly double to $225 million. This puts the $8.9 billion company at 39 times 2001 revenues estimates. This is not a high multiple compared to many Nasdaq-traded companies today, and the sales estimates for the next two years are fairly predictable because large contracts with IBM, Microsoft, and other companies help to guarantee them.

Beyond 2001, however, anything could happen. We can't predict how many acquisitions, partnerships, and new initiatives VerticalNet will undertake. We only know there will likely be many. We also can't predict, of course, how quickly VerticalNet's existing businesses — all 57 of them! — will grow. Therefore, we are unable to meaningfully predict what revenue will be after 2001. We can only slap on sales growth rates and hope they prove reasonable. Thus:

Year	Est. Sales Growth
2000	470%
2001	97%
2002	65%
2003	45%
2004	35%
2005	25%
2006	20%
2007	20%

What do you think?
PLEASE FILL OUT THIS QUICK ONLINE SURVEY!

These estimates could prove either quite conservative or too optimistic. There is no hard science behind the numbers; the only thing supporting them after 2001 is our belief that they are at least attainable.

If sales were to grow at this pace, in 2007, VerticalNet would book revenue of $1.3 billion. (From 2000 to 2007, the company would earn $5.2 billion in total sales.) Assuming the business has done well and achieves an 80% gross margin, the company could have a 30% profit margin, resulting in $390 million in net income in 2007. The company has 36 million shares outstanding today. After dilution, we'll assume (with "back of the envelope" estimates) at least 48 million shares by 2007. With 48 million shares outstanding, $390 million in earnings would amount to $8.12 in earnings per share. Assuming that the share price stayed flat, at $250, the stock would trade at 30 times these earnings in 2007. If the company could truly grow at this rate over the next seven years, and achieve these profit margins, it would likely trade at a significant premium to this earnings multiple. How significant? Could it double? Perhaps.

And what if these growth estimates prove too low? Then it's a whole new ballgame, with more potential. Business-to-business commerce is expected to hit the Internet like a monsoon, raining down growth for years, and VerticalNet is holding 57 buckets in its hands. This said, what if growth estimates are too high? And what if VerticalNet fails in many of its initiatives — what if it drops many of its buckets? As you can see, uncertainty is still the only certainty, especially after 2001.

CONCLUSION

VerticalNet is employing a comprehensive business-to-business strategy across several large industries which, if successful, could create lasting, recurring returns on investment. By building individually branded websites that offer timely industry content and resources, the company is working to create "sticky" communities that will result in recurring traffic and hopefully large amounts of e-commerce.

Because everything is so young (the company, the Internet, business-to-business e-commerce, the competition), uncertainty reigns. However, VerticalNet is positioned to sharply increase revenue in at least the near-term and the company will likely become profitable in 2001. The stock's valuation is rich based on the company's past financial results, but the valuation is based on the company's immense and diversified market opportunities, all of which offer aggressive growth prospects. The valuation is also based on management's leadership and ability to execute. Finally, as long as investor sentiment remains highly positive toward the industry, the stock could trend higher regardless of valuation. The long-term hope of early investors is that the business eventually grows into its valuation.

If an investor believes that VerticalNet can create a company worth considerably more than its $8.9 billion market valuation, then he should consider a long-term investment in this top-tier, business-to-business e-commerce leader. If an investor's risk tolerance is tapped out at this price, he may wish to put VerticalNet on his radar and hope for a lower valuation, at which time he can reconsider investing based on the company's most recent performance.

FOR MORE DISCUSSION

The Motley Fool discussion boards provide a means for investors to ask questions, share insights, and learn more about a company, including most recent company developments, in a timely, engaging manner. If you haven't experienced the Fool's discussion boards yet, you should give them a try. Registration and use is free. Among the discussion boards where VerticalNet is often a topic of discussion (or the focus!) are the following:

VerticalNet, Inc.:
http://boards.fool.com/Messages.asp?id=1270156000000000

The Motley Fool Internet Report:
http://boards.fool.com/Messages.asp?id=1010019000143001

Rule Breaker Companies:
http://boards.fool.com/Messages.asp?id=1030064000606002

VerticalNet Annual Results

	1999	1998
Exchange sales transactions	$16,500,781	$0
Cost of transactions	$14,171,345	$0
Net exchange revenue	$2,329,436	$0
Ad and e-commerce revenue	$18,428,485	$3,134,769
Combined net revenue	**$20,757,921**	**$3,134,769**
Expenses:		
Editorial/operational	$8,611,317	$3,237,971
Product development	$7,396,316	$1,404,557
Sales and marketing	$26,268,370	$7,894,662
General & administrative	$11,886,681	$3,823,593
Operating loss	**-$33,404,763**	**-$13,226,014**
Net interest	$1,344,233	-$85,271
Cash loss	-$32,060,530	-$13,311,285
Amortization expense	$7,819,351	$282,990
In-process R&D charge	$13,600,000	
Net loss	-$53,479,881	-$13,594,275
Pro forma loss per share	**-$0.96**	**-$0.63**
Shares counted	$33,329,371	$21,270,978

VerticalNet Balance Sheet

	12/31/99	12/31/98
Assets		
Current assets:		
Cash & equivalents	$14,253,828	$5,662,849
Accounts receivable	$45,776,520	$1,794,728
Inventory	$5,509,525	$0
Cash deposit on inventory	$400,356	$0
Investments - short term	$44,131,135	$0
Prepaid expenses	$5,564,066	$747,951
Total current assets	**$115,635,430**	**$8,205,528**
Net property and equipment	$13,147,628	$1,072,063
Long-term investments	$23,585,183	$0
Other assets	$10,612,323	$613,393
Goodwill and intangibles	$177,923,928	$2,451,991
Total assets	**$340,904,492**	**$12,342,975**
Liabilities and shareholders' equity		
Current liabilities:		
Current portion of long-term debt	$1,372,255	$288,016
Line of credit	$0	$2,000,000
Accounts payable/accrued exp.	$34,616,657	$2,802,600
Deferred revenues	$9,768,394	$2,176,585
Total current liabilities	**$45,757,306**	**$7,267,201**
LT and convertible debt	$116,749,935	$5,351,924
Shareholders' equity	$178,397,251	-$276,150
Total liabilities and shareholders' equity	**$340,904,492**	**$12,342,975**

Source: Motley Fool Research, company documents.

Updates

PRICELINE.COM

BY NICO DETOURN (TMF NICO@AOL.COM)

Priceline.com was the focus stock in issue one of The Motley Fool's Internet Report, released May 1999.

Stock price as of March 10, 2000: $94.50

It's been a busy couple of months since we last looked at **Priceline.com** (Nasdaq: PCLN) — especially in early March, when the stock price jumped some 60% in a matter of days. Why? The company's accelerated timetable for profitability is the most likely trigger. Another reason would be the accumulating evidence that the company is moving forward, aggressively scaling its business, adding new product lines, and continuing to pioneer new ground in the uncharted territory of electronic commerce.

We explored Priceline's unusual business model, known as the "reverse auction," in issue one of the *Internet Report*. To quickly recap, in the reverse-auction model buyers name their own prices for products and services, then sellers decide if those prices are acceptable. Priceline serves as an intermediary between buyers and sellers.

This is an ultralight model where the company carries no inventory, allowing it to scale well and fast. And not only in size. Once in place, the model also lends itself to expansion into a wide range of products and services. Indeed, expectations that Priceline would leverage this scalability have been present from the start, when name-your-own-price airline tickets were its claim to fame. Hotel reservations, new cars, home mortgages, and similar big-ticket purchases were soon added to Priceline's offerings with great success.

In early January, ahead of reporting its fiscal year results (discussed below), the company announced its first $3 million revenue day, with its core airline and hotel services setting seven-day sales records selling, respectively, 80,000 or some 3%, of all leisure airline tickets, and over 20,000 room nights. Priceline noted that these records came one week after launching a popular TV ad campaign featuring a singing William Shatner. Priceline also announced a doubling of its new car service to 26 states and anticipates completing a national roll out in the first half of the year. A previously announced name-your-own-price car-rental service was launched in February with Budget Rent-A-Car and National Car Rental as the program's first participants, nicely complementing the travel and hotel services.

PRICELINE WEBHOUSE CLUB GROCERIES

Priceline's first expansion into the everyday world of repeat purchases was WebHouse Club, which applied the name-your-own-price model to groceries. Customers shop, name their prices, and purchase groceries online, then pick them up from Priceline's network of over 1,500 participating local grocers. Interest in the service has been strong. On January 11, the company reported its first 10,000-customer day, along with the news that it had sold more than 2 million grocery items to over 100,000 members in the New York area, the service's initial market, within the first 60 days of operation. This was followed shortly by a 50% growth in traffic over 14 days as the TV ads continued driving brand awareness.

On February 29, Priceline announced that WebHouse Club had passed the 250,000-member mark in New York after 16 weeks of operation, with 3% of New York households pricing 5,000 items an hour. Priceline reports 85% of sales coming from repeat members — an indication of customer satisfaction and the growth potential in the model — and calls itself the largest online grocery service in the U.S. The service has so far been introduced in Philadelphia, Baltimore, Washington, D.C., and Detroit. Expansion to Boston and central Michigan are expected this quarter and a full national roll out is planed by the end of the year.

PRICELINE PERFECT YARDSALE

Reports had circulated for some time about Priceline's entry into the consumer auction space dominated by eBay. But the January 19 announcement of Priceline Perfect YardSale brought an unusual twist, as befits a business model based on reversing conventional processes.

Perfect YardSale is an "Internet-based market-maker" for the buying and selling of used goods. But unlike with auctions where the best bid wins — a process that drives prices higher — Perfect YardSale operates on a take-it-or-leave-it basis. Buyers register and tell the system what they're looking for and what they're willing to pay. Sellers register their stuff and indicate the price they're willing to accept. Priceline YardSale does the rest, connecting local buyers with sellers via e-mail and providing a simple but secure mechanism for a cashless transaction that the company itself backs with a no-questions-asked 30-day extended warranty.

After being notified that the exchange has taken place, Perfect YardSale charges the buyer's credit card and deposits the funds in the seller's Priceline account after a seven-day money-back guarantee period expires. For both the buyer and seller, the hassle of conventional classified ads and yard sales is eliminated and the fear of being ripped-off is greatly reduced by the Perfect YardSale guarantee. Initially launched in Atlanta, plans are for the service to be available nationwide by the end of the year.

CASH FLOW FUEL INJECTION

On February 25 Priceline.com announced a name-your-own-price for gasoline service to be launched May 20 through

WebHouse Club. Members will save 10-20 cents per gallon of gas by naming their price and, if it is accepted, locking it in by prepaying online for up to 50 gallons a month. The gas is pumped as needed at participating local major-brand gas stations where instead of a credit card a “Priceline for Gasoline” card uniquely identifies the member, keeps track of the prepaid price, the number of gallons used, and what remains for the month. The member comes out ahead if the price at the pump is higher than the agreed price. If the price is lower, that cheaper price is paid and the member’s credit card, on file with Priceline, is refunded the difference, with a refund also issued for whatever gas is unpumped at the end of the month.

With oil prices rising, the timing of the Priceline for Gasoline announcement couldn’t have been better. But the novelty of this latest variation on Priceline’s name-your-own-price scheme is nevertheless striking. It brings the logic of the commodity futures market to the practical world of the consumer, locking in one-month upside protection against price increases without the downside risk of paying more than the market is asking should the price at the pump fall. Gasoline is a highly price-sensitive purchase where nickels and dimes are counted, so the program should have strong and broad consumer appeal. And unlike leisure travel or new cars, gas is also a necessary and repeat purchase. Looking further out, it provides Priceline opportunities to cultivate and leverage a customer base in tune with the company’s unique approach to pricing and shopping, and open to the introduction of even more services.

Indeed, this leverage is already apparent, with participating gas stations paying WebHouse a few pennies per gallon for the incremental business, and with paid advertising appearing on the WebHouse pages. Also, as the intermediary and keeper of the customer’s credit card, Priceline gets paid up to 30 days in advance for something that has not yet been delivered, making Priceline for Gasoline the financial equivalent of fuel injection to the company’s cash flow.

EXPANSION DOWN UNDER

Taking good advantage of the leap year, Priceline’s high-capacity press machine announced on February 29 that it is creating a new company, called MyPrice, to introduce its buyer-driven name-your-own-price business model to Australia and New Zealand and their combined population of 23 million. The new company will be led by two of Australia’s most senior telecommunications executives, both formerly with Telstra Corporation Limited, Australia’s largest provider of telecom and Internet services. MyPrice is expected to begin operating in Australia and New Zealand later this year. Following the same formula that has worked domestically, the services will initially sell leisure airline tickets before expanding into hotels, rental cars, financial services, telecommunications, and automotive sales.

A NOTE ABOUT WEBHOUSE CLUB, PERFECT YARDSALE, AND MYPRICE

Although clearly stated in Priceline.com’s many announcements, it is nevertheless easy to overlook the fact that Priceline WebHouse Club, Priceline Perfect YardSale, and MyPrice are not in fact business units of Priceline.com. They are instead privately held, independently financed companies that license Priceline.com’s patented business systems, technology, and brand name. In exchange, Priceline.com has received warrants allowing it to take equity stakes in the companies. Unless and until these are exercised, the financial results of the companies will not be included in Priceline.com’s financial statements.

Priceline WebHouse and Priceline Perfect YardSale are both subsidiaries of Walker Digital, the privately held “intellectual property laboratory” behind Priceline’s business model, whose chairman, Jay Walker, is also the founder and co-chairman of Priceline.com. Walker Digital also owns the intellectual property rights underlying some of the technology Priceline.com uses and licenses from Walker Digital, under a perpetual, non-exclusive, royalty-free agreement. The companies are thus not only from the same mold but are joined at the fountainhead through cross-licensing agreements and the common use of the Priceline name.

MyPrice is jointly funded by Priceline.com and SFN Investments, a new consortium of Australian and international business executives and investors, including George Soros. MyPrice will also pay an annual licensing fee to Priceline for use of its intellectual property. A similar but separate agreement was announced in January between Priceline and Hutchison Whampoa, one of Asia’s largest Internet and telecom infrastructure operators, to introduce the Priceline model and e-commerce platform throughout Asia, including China, Hong Kong, Taiwan, Korea, India, the Philippines, and Vietnam.

There are any number of reasons for the creation of separate companies and the use of licensing agreements but two in particular are worth noting. Priceline’s business is based on patents it has been granted for key components of its business model. The company is currently suing Microsoft for starting a “copycat” name-your-own-price service at its 85%-owned Expedia travel site. By formally licensing its business systems to other parties, Priceline helps demonstrate and enforce the validity of its patents by receiving third-party compensation for the use of its intellectual property rights. On that premise, if the structure and relationships between the separate companies allow adequate daylight to pass between them, the legal advantages of licensing can be gained while keeping the intellectual jewels within the family.

Another more immediately practical reason for Priceline.com’s use of this licensing structure is described by chairman and CEO Richard S. Braddock who, in announcing WebHouse Club, said that the decision “to employ a new business development model... allows outside investors to

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provide the significant infusion of new capital a start-up requires, allows us to tap the strength of the Priceline.com brand name, and assures enhanced speed to market" while minimizing the exposure of Priceline.com and its shareholders to the risks of high-maintenance and unproven business models — other than Priceline's, of course. As already mentioned, the results of these operations are not yet being consolidated into Priceline.com's financial statements. However, the undisclosed licensing royalties Priceline.com receives from these arms-length start-ups do indeed find their way into its quarterly results, the most recent of which we'll now give the once-over.

FOURTH QUARTER AND FISCAL YEAR RESULTS

On January 27, 2000, Priceline.com announced its financial results for the fourth quarter and fiscal year 1999, its first full year of operation. Revenue for the quarter came in at $169.2 million, up 791% from the $19 million reported in the year-ago quarter, and up 11% from third-quarter revenue of $152.2 million. Excluding certain non-cash charges, Priceline's net loss for the quarter was $10 million, or $0.06 per share. This was 2 cents better than consensus estimates and less than half the $0.14 per share loss in the fourth quarter of 1998. The fourth quarter also saw gross margin continue to rise, coming in at a record 14.2%, beating the third quarter's 12.2% and the second quarter's 9.8%, which were also records.

For the full year 1999, Priceline shows revenue of $482.4 million, a 1,270% increase over 1998 revenue of $35.2 million. Excluding non-cash charges, Priceline's net loss for 1999 was $52.5 million, or $0.39 per share. This beat consensus estimates by 3 cents and compares to a 1998 net loss of $44.4 million, or $0.55 per share. Gross profit for fiscal 1999 was $59.4 million, compared to 1998 gross profit of $1.7 million.

Priceline ended the year with a customer base of 3.8 million, having added a record 982,000 customers during the fourth quarter, including 80,000 through Priceline WebHouse Club since its November 1 launch. Almost half of total customers came on board in the last six months. As a comparison, eBay and Amazon.com, which have been operating more than twice as long as Priceline, counted year-end customers at 10 million and 17 million, respectively.

Priceline.com Balance Sheet December 1999

(millions)	
Cash and investments:	$133.10
Total current assets:	$211.74
Property & equipment:	$28.00
WebHouse Club warrants:	$189.00
Other assets:	$13.14
Total assets:	$441.88
Total liabilities:	$39.25
Long-term debt:	$0.00
Total shareholder equity:	$402.63

Priceline Pro-forma Income Statement December

(millions)	Q4 1999	Q3 1998
Revenue:	$169.20	$19.00
Gross profit:	$24.10	$2.30
Operating loss:	($12.70)	($12.90)
Net loss:	($10.00)	($12.70)

Priceline Gross Margin Comparison

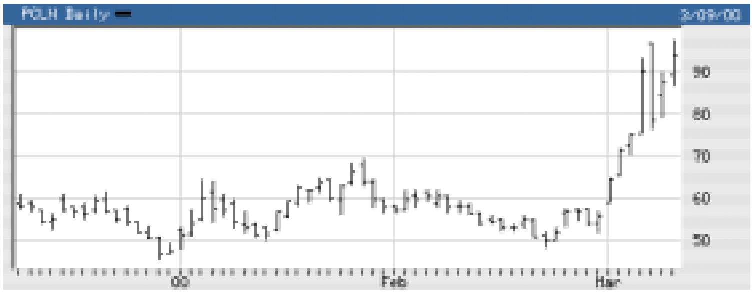
(millions)	FY 1999	Q4 '99	Q3 '99	Q2 '99
Revenue:	$482.4	$169.2	$152.2	$111.5
Product cost:	$424.6	$145.5	$133.6	$100.6
Gross margin:	12.0%	14.0%	12.2%	9.8%

LOOKING FORWARD

Priceline's ongoing reduction in quarterly operating losses, combined with revenue growth and improved operating margins, have management making bullish sounds. In reporting what he called a "landmark quarter," Braddock said revenues for the current March quarter would increase at a rate of at least 30% from Q4 1999. On that basis, the company has set a $1 billion revenue target for this year, more than twice that of 1999. More significantly, with expectations of a continued reduction in operating loses through 2000, and with faster than expected growth in customers, revenues, and gross margins, the date for profitability has been moved up from the second half of 2001 to the first half of 2001, a "substantial difference," in the words of President and Chief Operating Officer Dan Schulman.

It should be emphasized that these key financial metrics are being revised upward at the same time Priceline is aggressively entering new markets and launching new services. Some of these, such as WebHouse groceries and Perfect YardSale, offer lower margins than the big ticket items the company started with. So should management's new expectations of early profitability prove correct, it would dramatically affirm the cost effectiveness and efficient scalability of Priceline's lightweight business model which, as it turns out, even the inventors and practitioners who know it best had underestimated.

PRICELINE.COM PRICE OVER THE PAST THREE MONTHS



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TIMELINE

2/29/00 ($55.94) — Priceline.com announces expansion to Australia and New Zealand. Priceline WebHouse Club passes 250,000-member mark in New York after 16 weeks of operation.

2/25/00 ($56.94) — Priceline.com announces name-your-own-price for gasoline service.

2/23/00 ($51.88) — Priceline.com CFO Paul E. Francis is named CFO of Priceline WebHouse Club, and executive chairman of Priceline Perfect YardSale. Francis is replaced by Heidi Miller, former CFO of Citigroup, as Senior Executive Vice President, CFO, and member of the Board of Directors.

2/18/00 ($51.00) — Priceline WebHouse Club passes 200,000-member mark in New York after three months of operation and announces name-your-own-price grocery service with local pickup in Detroit.

2/3/00 ($59.56) — Priceline.com launches name-your-own-price rental-car service. Priceline.com auto services releases top-10 new car models and makes for January 2000.

2/2/00 ($59.56) — Priceline.com announces 50% growth in grocery service over 14 days as William Shatner ads increase awareness; 2% of New York households price 5,000 items per hour, 24 hours a day.

1/31/00 ($58.00) — Priceline.com completes move to Norwalk, CT.

1/27/00 ($64.13) — Priceline.com reports record fourth-quarter financial results.

1/26/00 ($66.25) — Priceline.com receives notice of allowance for its seventh U.S. patent and announces alliance with Hutchison Whampoa Limited to bring buyer-driven e-commerce to Asia.

1/19/00 ($62.44) — Priceline launches Perfect YardSale consumer-to-consumer service.

1/17/00 ($59.19) — Priceline.com names Michael McCadden, former Gap EVP, as new Executive Vice President and Chief Marketing Officer and Jeffery H. Boyd as new Executive Vice President and General Counsel.

1/12/00 ($51.13) — Priceline.com announces doubling of name-your-own-price new car service to 26 states, anticipates national roll out complete in first half of year.

1/11/00 ($52.81) — Priceline.com announces WebHouse Club grocery service sold 2 million items in first 60 days, with 100,000 members in New York Metro area. New TV campaign leads to record $3 million revenue day; airline and hotel sales unit set seven-day sales record.

1/10/00 ($54.25) — NextCard and Priceline.com announce co-branded name-your-own-terms credit card program. General Atlantic Partners and Paul Allen's Vulcan Ventures increase stake in Priceline.com by 5 million and 2 million shares, respectively.

1/5/00 ($59.94) — Priceline.com pre-announces record customer growth and leisure airline ticket sales in fourth quarter. Tells investor conference that it expects to report nearly half a billion.

EXCITE@HOME

BY NICO DETOURN (TMF NICO@AOL.COM)

Excite@Home was the focus stock in issue two of the Internet Report, released July 1999.

Stock price as of March 10, 2000: $28.56

Maybe it's in the company's name: Excite@Home. Two words, one suggesting action; the other, rest. Or maybe not. The contrast, however, captures how the stock trades in a frustrating show best described as lethargic volatility. It jumps around a lot, but doesn't go anywhere. Nowhere good, that is; in early March it revisited levels not seen since December 1998, trading as low as $31.06. But while there is little joy in the stock, the company continues to offer one of the more interesting studies in its space.

EXECUTIVE SHUFFLE

Excite@Home made a number of key executive appointments in the first weeks of the new year. Of these, none was more important than the promotion of president George Bell to the additional role of chief executive officer, replacing long-time CEO Tom Jermoluk who will remain in his position as chairman of the board, concentrating on the company's strategic direction and its relationships with its cable partner-owners. Bell, who was CEO of Excite when it was acquired last year by @Home, will run the day-to-day show. This new division of labor at the top represents a rebalancing of the company's business model and a new focus on the growing importance of content and media services going forward.

The company also appointed two more in a recent series of former executives from AT&T, Excite@Home's largest and most important cable partner. Byron Smith was hired as a senior VP of Marketing and is charged with leveraging the

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"synergistic relationship" between his new and former employers and helping to keep Excite@Home's "objectives aligned" with Ma Bell. Smith successfully marketed several of AT&T's consumer long distance services and will hopefully work the same magic in "aggressively building the @Home brand" and taking @Home's customer base to the next level. The company also named Mark O'Leary senior VP and general manager of its @Work business-to-business division. O'Leary has held a number of positions with AT&T and was most recently a VP for the AT&T Solutions division. He replaces Don Hutchison, who was named chairman and CEO of Work.com, Excite@Home's new business portal with **Dow Jones** (NYSE: DJ).

WORK.COM ALLIANCE WITH DOW JONES

On February 22, Dow Jones and Excite@Home announced the formation of a new company to develop a business portal catering to the needs of small and midsize businesses. The company will be a 50-50 venture of Excite@Home and Dow Jones with a possible initial public offering later this year. The portal will be named Work.com and will combine the operations of the existing Work.com site, started in September by Excite@Home's @Work business-to-business division, and the dowjones.com site, launched by Dow Jones last July. Rather than compete in the same space for the same customers, the idea is to leverage what each company does best, applying Excite's site-building and personalization experience to the vast news and information resources of Dow Jones. The site is expected to launch later this year.

In addition to the now-standard assortment of portal tools like e-mail, calendars, and community services, Work.com will offer users in over two dozen industry categories free and eventually fee-based front- and back-office business applications including Web-hosting, payroll and accounting services, and customer relationship management. Although not stated, we can expect Work.com to offer advertising and marketing services through Excite's MatchLogic division and high-speed Internet connections through the @Work division.

The deal between Excite@Home and Dow Jones has echoes of the mid-1998 deal in which Excite partnered with Netscape, both still independent companies at the time, to develop, manage, and market portions of Netscape Netcenter. As with that arrangement, the Dow Jones partnership reveals revenue potential in Excite@Home's media properties and services not as readily apparent when the company is viewed head-on as "just" a consumer portal and a broadband network.

FOURTH QUARTER AND 1999 FINANCIAL RESULTS

On January 20, Excite@Home reported its financial results for the fourth quarter and all of 1999. These combine the historical results of Excite and @Home on a pro forma basis. As anticipated, the company showed its first profit in Q4, albeit a marginal one. Revenues for the quarter were $128.8 million, an increase of 76% over the fourth quarter of 1998. Income was $514,000, or $0 per share. This compares to a loss of $4.5 million, or $0.01 per share, in the fourth quarter of 1998. For the full year, revenues came in at $420.5 million, an increase of 107% over fiscal 1998. The pro forma loss for the year was $14.6 million, or $0.04 per share, compared to a 1998 loss of $46.7 million, or $0.14 per share.

While these numbers match consensus estimates, show progress, and point in the right direction, it should be noted that they exclude some steep charges, most of them related to the Excite merger and the costs of distribution agreements. The small reported profit resulted from interest income, rather than operations, which still ran at a loss. Importantly, about two-thirds of total revenue comes from Excite and the related media properties. The table below provides a snapshot of the Q4 and FY 1999 financial highlights.

Excite@Home Balance Sheet December 1999

($ in thousands, except EPS)

Cash and investments:	$525,223
Current assets:	$630,906
Property & equipment:	$176,077
Goodwill & other intangibles:	$7,614,847
Total assets:	**$9,104,279**
Current liabilities:	$241,883
Convertible debentures:	$736,294
Shareholder equity:	$8,067,017

Pro-forma Income Statement December 1999

	FY 1999	4Q99	3Q99	2Q99	1Q99
Revenue:	$420.49	$128.75	$112.50	$110.40	$78.70
Net income:	($1457.60)	($723.00)	($498.60)	($249.10)	($25.70)
Adjusted net income*:	($14.62)	$0.51	($4.20)	($5.90)	($6.60)
Adjusted EPS*:	($0.04)	$0.00	($0.01)	($0.02)	($0.02)

*Adjusted income is before investment gain, cost of distribution agreements, and merger and acquisition related expenses.

@HOME SUBSCRIBER GROWTH

Along with its financial results, Excite@Home reported 1.15 million subscribers to its consumer cable broadband service as of December 31, an increase of 310,000 or 36% from the previous quarter and more than three times 1998's final tally. This is a key metric for the company and was in line with expectations. Approximately 24 million homes have been upgraded and can offer the service, an 85% increase over last year. This represents one-third of the company's 72 million worldwide homes under contract and about 40% of its total

North American homes. Of those upgraded homes, 4.8% have actually subscribed to the service, nearly twice the penetration level at the end of 1998. Internationally, the company has 13 million homes under contract, with 11 million of those added in 1999.

During the fourth-quarter conference call CEO Bell offered that the company was preparing to offer by the end of this year high-speed service over phone lines using DSL, the main rival technology to cable. This would let Excite@Home provide its service in areas where it does not have cable partners or where cable upgrades have not been completed. The plan raises a tangle of questions concerning Excite@Home's exclusive contracts with its partners. It also shows the company preparing for the time, still over two years out, when those contracts start expiring. It's also further evidence of the company's intention to aggressively market its brand and pursue growth on a broader basis than is permitted by the relatively fixed footprint of the cable platform. Related to this, Excite@Home also announced several wireless and mobile device initiatives aimed at getting its branded services into the hands of more people.

@Home Subscriber Growth

Quarter	@Home Cable Subscribers	Upgraded Homes	Market Penetration
Sep. '97	26,000	2,700,000	0.96%
Dec. '97	50,000	4,500,000	1.11%
Mar. '98	90,000	5,700,000	1.58%
June '98	147,000	7,900,000	1.86%
Sep. '98	210,000	10,000,000	2.10%
Dec. '98	331,000	13,200,000	2.51%
Mar. '99	460,000	15,000,000	3.07%
June '99	620,000	17,000,000	3.65%
Sep. '99	840,000	21,000,000	4.00%
Dec. '99	1,150,000	24,000,000	4.79%

EXCITE, MEDIA, AND MARKETING GROWTH

The Excite Network received 123 million daily page views in December, 38% more than in September and more than double the traffic in December 1998. Media Metrix counts approximately 28 million unique users of the Excite Network, a reach of 42.5% of all Web users in December. These numbers include December traffic to the Bluemountain.com site, which showed an 85% increase for the month, with Bluemountain visitors sending more cards in the fourth quarter than in all 1998. Leveraging and monetizing that kind of predictable traffic was the driver of the Bluemountain acquisition and to that end, Excite@Home reported that ads focusing on gift-giving opportunities now run on about one-fifth of the site's pages. It should be noted, however, that the Excite Network traffic saw a fairly steady decline throughout 1999 in absolute numbers and as a percent of total Web users. And while there is nothing wrong with buying eyeballs, per se, the dramatic increase in traffic due to the Bluemountain acquisition does not make a trend. It also does not address the issues that led to the fall-off in traffic volume, which was apparently more "organic" in nature. These visitor numbers, like all numbers, need to be watched over time and taken with a large grain of context.

Also important are registered users at the Excite.com portal, which grew to 51 million in December from 44 million in Q3 and increased 150% since December 1998. Of those registered users, 43% have personalized a My Excite Start Page, a key driver of user loyalty and repeat visits. It also helps the company's MatchLogic division target potential subscribers to the @Home broadband service, with those efforts showing a 30% increase in Q4 sales leads and a response rate of about 5%. These interactions between the portal and the broadband service bring a new dimension to Excite's traffic numbers.

The company's @Work division counted over 5,100 businesses using its high-speed DSL services in December, 20% more than in the third quarter of 1999. Over 2,000 new merchants have set up online storefronts on Excite@Home's eBusiness Services platform, and present opportunities for integrating these services and customers with the Excite@Home-Dow Jones Work.com portal when it launches later this year.

Excite Network Traffic from Media Metrix

Date	Excite Network Unique Visitors (millions)	Total Web Users (millions)	Percent Web Users
1/99	18,225	63,210	28.83%
2/99	18,081	63,868	28.31%
3/99	18,861	65,251	28.91%
4/99	17,423	64,968	26.82%
5/99	15,167	65,369	23.20%
6/99	17,112	66,021	25.92%
7/99	16,408	66,641	24.62%
8/99	16,062	66,956	23.99%
9/99	15,322	67,136	22.82%
10/99	15,021	67,571	22.23%
11/99	14,975	68,795	21.77%
12/99	27,670	69,197	39.99%
1/00	25,439	72,722	34.98%

FREEWORLD GROWTH AND NAME CHANGE

Excite@Home's advertising-supported free ISP is another tool for acquiring Excite users and @Home subscribers. The company announced in late February that the service had "reached more than 500,000 users" since launching on January 6. Although an impressive number, typically only about half of a free ISP's registered users sign on over the course of a month, a number we might expect to be lower due to initial curiosity following a launch.

Perhaps more significant than the registration numbers was the accompanying news that the name of the free ISP was changed from FreeWorld to FreeLane. No reason was given. But it is surely no coincidence that **NetZero** (Nasdaq: NZRO), the largest free ISP with some 3 million registrants, had recently filed suit accusing Excite@Home of infringing the "Defenders of the Free World" trademark NetZero was awarded in December and had been using since last October. Renaming the free service will probably have a negligible impact on its value to Excite@Home as an advertising revenue source and marketing vehicle. Though it was an avoidable misstep, its better that it happened after only six weeks than after six months.

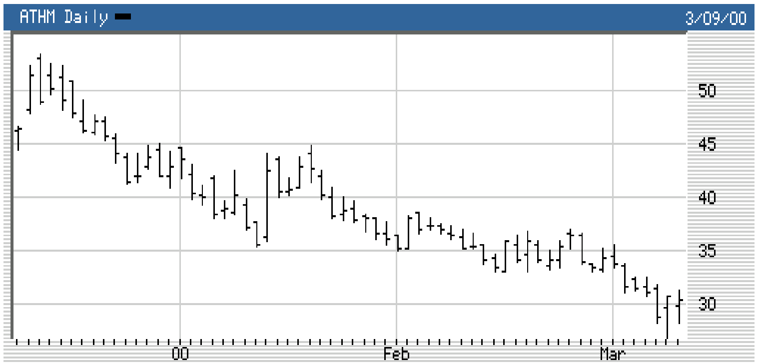
EXCITE@HOME ONE YEAR LATER

More than a year after announcing one of the largest Internet mergers to date, we find Excite@Home operating in a space where some of the industry's most important trends intersect and where its most controversial issues are focused. Like few other so-called "Internet companies," Excite@Home combines under one roof a connectivity infrastructure with a variety of media and commerce operations that define a capable and flexible content/commerce infrastructure. This makes for a promising but also volatile mix, with the company subject to an especially wide range of outside influences. It also accounts for the uncertainties that have weighed on the stock which has been down as much as 66% since hitting all-time highs just under one year ago.

One such uncertainty is the open-access issue, and the ruling in AT&T's Portland appeal, in particular. A decision in that case is expected literally any day now and may have been announced by the time you read this. However, regardless of how that turns out and its immediate impact on the stock, we can see that Excite@Home is positioning itself in ways that should minimize the longer-term importance of the issue. Indeed, the main reason for merging @Home with Excite was to broaden the company's scope into media services, not only in anticipation of the end of cable exclusivity — which open access in effect threatens to bring about prematurely — but to set the company up for a time when Internet access, including broadband, has become a commodity.

Recent actions and initiatives show the vision that created today's Excite@Home coming into focus. That, in turn, helps ease uncertainty about whether conflicts with AT&T over Excite@Home's content and media strategy would hinder the company's development; the two companies seem to have found a working "alignment" of their interests. Additional uncertainties remain, such as the impact of the AOL - Time Warner merger on the competition between Excite@Home and AOL, and on the industry overall. But uncertainty and complexity are more the rule than the exception. All in all we might allow ourselves to optimistically say that Excite@Home seems to be finding its balance after a difficult year of fits and starts. Should that prove correct, we might reasonably expect the stock to respond in kind.

EXCITE@HOME PRICE OVER THE PAST THREE MONTHS



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TIMELINE

3/2/00 ($31.69) — Excite@Home merges operations in Australia.

3/1/00 ($33.81) — Excite@Home expands presence in Canada with launch of Excite.ca.

2/29/00 ($34.31) — Excite@Home's free ISP passes 500,000 users; changes name to FreeLane.

2/28/00 ($33.38) — Excite@Home and Dow Jones & Company name Chairman/CEO of Work.Com. Excite@Home appoints former AT&T executive to head commercial division; joins consortium to build standards for synchronizing wireless and mobile devices. Excite@Home's MatchLogic adds lead generation and online promotions to form integrated suite of customer acquisition products.

2/25/00 ($34.00) — Tandy expected to pick Excite for cable modems.

2/24/00 ($36.44) — Excite@Home invests in ecentives, direct marketing and promotions.

2/23/00 ($35.44) — Newmedia.com partners with MatchLogic to create rich media site with Enliven interactive advertising.

2/22/00 ($34.19) — Dow Jones & Company and Excite@Home form new company, Work.com.

2/14/00 ($33.38) — Bluemountain.com hits all-time record high this Valentine Season; doubles electronic cards sent.

2/3/00 ($37.00) — Excite@Home and Lipstream launch integrated voice and text chat into all of Excite chat.

2/2/00 ($38.00) — Excite Search announces 250 million indexed webpages the largest among top ranking portals.

1/31/00 ($36.05) — Excite@Home to host sixth annual U.S. Comedy Arts Festival; Offers broadband security with McAfee.com.

1/26/00 ($37.81) — Excite@Home bought out its Spanish subsidiary from Retevision; offers personal firewalls.

1/25/00 ($38.81) — Excite@Home and Freeworks.com partner to provide administration solutions for Work.com users; Excite@Home announces Web portal deal with Vodafone.

1/20/00 ($42.63) — Excite@Home reports Q4 and FY 1999 results; President George Bell promoted to additional post of chief executive officer, replacing Tom Jermoluk who continues as chairman.

1/18/00 ($40.63) — Excite@Home introduces personalized Web-based e-mail, voicemail, and fax. Excite@Home introduces broadband film service at Sundance Film Festival.

1/13/00 ($42.56) — Excite@Home adds marketing executive from AT&T. Excite@Home shares rise on AT&T takeover speculation.

1/12/00 ($35.63) — Excite@Home expands commerce management team.

1/6/00 ($38.38) — Excite@Home launches free Internet access service, FreeWorld Powered by Excite.

DRUGSTORE.COM

BY PAUL LARSON (PAULL@FOOL.COM)

Drugstore.com was the focus company in issue three, September 1999, of The Motley Fool's Internet Report.

Stock price as of March 10, 2000: $21.13

Probably the largest news over the past eight weeks to hit concerning Drugstore.com had to do with its largest shareholder, Amazon.com. On January 24 it was announced that Amazon would be investing another $30 million into the company, bringing its stake in Drugstore to near 28%. In a related agreement, Drugstore will be paying Amazon $105 million over the next three years to get a "tab" on Amazon's virtual store shelves. Some of Drugstore's operations will be intimately tied in with Amazon.

This deal, in total, is probably a wash for Drugstore. On the positive side, the agreement should give a fairly good boost to Drugstore's visibility. Amazon is, by far, the most trafficked shopping website in existence, and it will surely be able to divert some of that traffic Drugstore's way. On the negative side, the $105 million agreement is a hefty contract for a company of Drugstore's size. At the end of the fourth quarter, Drugstore only had $143 million worth of cash and equivalents on its balance sheet. The Amazon additional investment will mitigate this somewhat, but the marketing deal will nevertheless be a major cash drain over the next three years.

Another mitigating factor to the cash situation is the announcement that Drugstore would be selling 6 million shares of its stock in a secondary offering. Only 4.5 million shares are actually being sold by the company and will add to Drugstore's cash balance. (The rest are being sold by insiders.) Unfortunately, the company's timing is not the greatest since the stock is near its low. If this follow-on sale of shares had happened a few months ago, the company could have gotten twice the cash for the same amount of dilution.

Drugstore did find itself buying another company in fairly short order since we last reported. The company bought online beauty products retailer Beauty.com for approximately 1.3 million shares. It is a fairly small acquisition that simply extends the company's product offerings. What's interesting about this acquisition is that it only took three weeks from its announcement until the close.

Of course, we also had an earnings announcement to digest in the last couple weeks. Drugstore's reported financials for the fourth quarter looked like this:

Drugstore.com's Fourth Quarter Financials

(in millions)

	Q4 1999	Q3 1999
Revenue	$18.5	$12.2
CoGS	$18.8	$14.1
Gross profit	($0.3)	($1.9)
Marketing & sales	$28.5	$16.5
Overhead expenses	$8.8	$11.0
Intangible expenses	$5.3	$14.6
Operating loss	($45.4)	($43.9)
Interest income	$2.0	$1.9
Net loss	($43.5)	($42.0)
EPS	($1.02)	($1.04)
Shares outstanding	42.6	40.3
Gross margin	(1.8%)	(15.7%)
Operating margin	(246.1%)	(361.1%)
Net margin	(231.1%)	(345.2%)

I think it should be fairly obvious that these numbers aren't pretty. Any time a company has a negative gross margin and reports a net loss more than triple its revenue it should be a major red flag. On the bright side, there was some fairly substantial margin improvement across the board. It remains to be seen if this was a temporary blip created by the holidays or if it was a real step forward in the right direction towards profitability. Either way, Drugstore.com has a long road ahead if it wishes to become profitable, and in the future we'll be keeping a close eye on its margins to make sure the company is headed in the right direction.

DRUGSTORE.COM'S STOCK PRICE OVER THE PAST THREE MONTHS

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TIMELINE

2/9/00 ($27.75) — Drugstore.com files with the SEC to potentially sell up to 6 million shares in a follow-on offering; 1.5 million shares are being sold by insiders with the other 4.5 million being sold by the company to raise cash.

1/24/00 ($35) — Amazon.com reaches agreement with Drugstore.com. In exchange for $105 million, Drugstore.com will be given a tab on Amazon's shopping site for three years. Moreover, Amazon will invest an additional $30 million into Drugstore.com, boosting its already sizable stake. Fourth-quarter earnings are announced. The company recorded $18.5 million in revenue for the quarter and racked up an operating loss of $45.5 million.

1/12/00 ($30.5625) — Drugstore.com announces intention to buy beauty supply site Beauty.com for 1.3 million shares. The deal closed on February 2.

1/10/00 ($31.25) — Drugstore.com competitor **CVS** (NYSE: CVS) and online healthcare titan **Healtheon/WebMD** (Nasdaq: HLTH) announce an alliance.

EBAY

BY JEFF FISCHER (JEFFF@FOOL.COM)

eBay was the focus company in issue four, released November 1999.

Stock price as of March 10, 2000: $193.25

On January 25, eBay announced fourth-quarter 1999 results that topped estimates by two pennies per share. The auction giant announced fourth-quarter revenue of $73.9 million, up 139% from the same quarter last year, and well above the average estimate of $66 million and our estimate of $70 million. Earnings per share rang in at $0.04, doubling the 2-cent estimate. Registered users on the site topped 10.0 million to end 1999, up from only 2.2 million at the end of 1998. Gross margins leveled off at 70.8%, just as we hoped, and this margin should rise, the company announced, later in 2000. In 1999, gross margins averaged 74.4%.

After earnings were released, eBay held a conference call where it stated that:

- Revenue in 2000 should be about $380 million to $390 million.
- The company is comfortable with the estimated $0.36 per share in 2000 earnings (up 140%).
- Margins should be relatively flat the next two quarters, but should rise in the later half of the year.

eBay Q4 Results

($ millions, except EPS)

	Q4 1999	Q4 1998	Change
Sales	$73.9	$30.9	139%
Gross profit	$52.3	$25.0	109%
Operating profit	$0.5	$3.6	NA
Net income	$4.9	$2.6	88%
EPS	$0.04	$0.01	300%
Gross margin	70.8%	80.9%	
Operating margin	0.6%	11.7%	
Net margin	6.6%	8.4%	

Past Annual Results

	1999	1998	1997
Sales	$224.7	$86.1	$41.4
Gross profit	$167.1	$70.0	$33.0
Operating profit	($1.1)	$12.8	$10.0
Net income	$10.8	$7.3	$7.1
EPS	$0.08	$0.04	$0.05
Gross margin	74.4%	81.3%	88.9%
Operating margin	(0.5%)	15.0%	24.1%
Net margin	4.8%	8.4%	17.1%

From the tables showing financial results, you can see how margins have fallen as the company has spent money to build its business. At an established company, this would be disturbing, but at eBay the decline in margins was expected. eBay is spending now in order to capitalize on market opportunities before the competition does, as well as to bolster it current offerings. As spending slows down (by the end of 2000 most likely) and the business continues to grow stronger, margins should rise. The company targets long-term gross margins of 80% to 85% and operating margins of 30% to 35%.

NEW DIRECTIONS AND EARLY SUCCESS

In February, eBay announced a partnership with NEC in Japan that strengthens the eBay Japan site, which has been live and operating the past month. eBay will officially open the site in early March, when the company's CEO, Meg Whitman, visits Japan to do so. Recently touring Europe, Meg Whitman shared that eBay was searching for business partners in Scandinavia for future eBay sites serving the area specifically. These countries possess high levels of Internet usage per capita, and most of the Internet users have above-average income and net worth.

From Germany, Meg Whitman shared that eBay Germany (www.ebay.de) is now the second-largest auction site in the world based on gross merchandise sales. The site is hosting $600,000 in daily merchandise sales, behind only eBay itself, which hosts $10 million in daily sales. eBay is also testing eBay Pro in Germany, a business-to-business e-commerce site. At a March conference, management shared that eBay Pro is doing very well and eBay is considering other business-to-business initiatives.

The following day, March 7, eBay announced a stake and partnership with privately held AutoTrader.com, a leading online used automobile seller with 5 million monthly visitors. So, eBay has many irons in the fire, from business-to-business possibilities, to building out its auto and other big-ticket auction services. All the while, the company remains steadfastly focused on serving its lifeblood: the thriving eBay community. So far, everything at the company continues to appear on track.

To close on eBay for now, our final analysis remains unchanged from last November, though we will continue to update our forward estimates and provide the updates in a future issue of the *Internet Report*. Interestingly, a lead analyst at a large institution started coverage of eBay in February citing the potential for eBay to become a $125 billion company by 2009. In November, we suggested a $100 billion company was possible by 2009. eBay was recently valued around $21 billion.

TIMELINE

03/07/00 ($162.81) — eBay invests in privately held AutoTrader.com as the two create an auction format for used cars.

03/04/00 (NA) — eBay CEO Meg Whitman interviewed on Fool Radio (to listen online: http://www.fool.com/radio/radioonline.htm#archive).

03/02/00 ($150.13) — "The Best of Hollywood" debuts on eBay.

02/17/00 ($145.25) — eBay and NEC announce a joint venture in Japan.

02/08/00 ($169.75) — Go.com and eBay announce a multi-year marketing agreement.

02/02/00 ($151) — Former president of Phillips Auctioneers joins eBay.

01/26/00 ($153.56) — eBay launches "Chinatown" sales area on its site.

01/25/00 ($137.50) — Fourth-quarter 1999 results announced. Revenue up 139% to $73.9 million, registered users climbed to 10 million, earnings per share was $0.04, or $6.1 million. 1999 revenue totaled $224.7 million.

01/12/00 ($130.38) — eBay selects e-Stamp to provide its community with online postage.

LAUNCH MEDIA

BY PAUL LARSON (PAULL@FOOL.COM)

Launch was the focus company in issue five, January 2000, of The Motley Fool's Internet Report.

Stock price as of March 10, 2000: $21.00

It has been a relatively quite two months since we last covered **Launch Media** (Nasdaq: LAUN). A small acquisition here, an earnings announcement there, but nothing totally earth-shattering or surprising happened with the company. The stock also traded in a fairly tight range, as the chart on page 33 shows.

Let's first talk about Launch's acquisition. The company bought a small firm named NVS that streams music videos to commercial places such as shopping malls, hotels and restaurants. The deal really shouldn't effect Launch's finances one way or the other, but it will further Launch's brand image as a cutting-edge way to discover new music and music videos.

There was one merger in the music industry that affects just about everyone in the sector, including Launch. As if one major merger with AOL wasn't enough to keep Time Warner's lawyers busy, it was announced in late January that Warner would be joining forces with EMI. Together, Time Warner and EMI will control about a quarter of the music industry's sales.

One deal Launch made worth checking out is the exclusive agreement it signed with CheckOut.com. CheckOut will become the sole provider of music CDs and related products on Launch's website. Launch will also provide CheckOut with content for its online store. Whenever someone clicks a link from Launch to CheckOut and buys a CD, Launch will get a small commission. We suspected just such a deal would happen, leveraging Launch's content into commerce. However, the fact that Launch went with a second-tier retailer like CheckOut is a bit surprising.

Launch's very effective "sticky" application LAUNCHcast did emerge from beta testing a few weeks ago. From our informal sampling of the application's usage, it seems that the number of users listening at any given time is up between 50-75% from when we first wrote about the company. Yet we, as users of the service, have yet to see a thousand simultaneous listeners. It will be important to keep tabs on the service to make sure that its usage is indeed growing.

Finally, we have the company's fourth-quarter earnings to digest. The raw numbers looked like this:

Launch's Fourth Quarter Financials

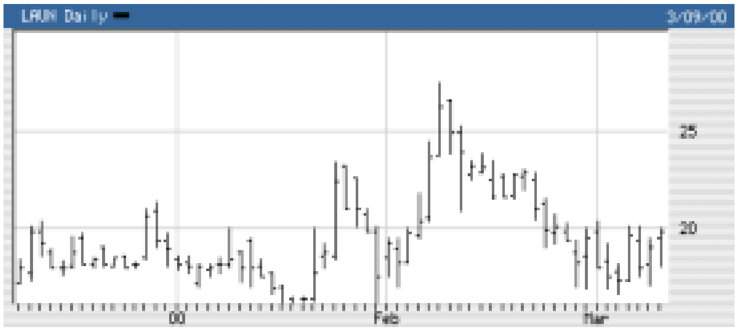
($ millions, except EPS)

	Q4 1999	Q3 1999
Revenue	$6.6	$5.3
Direct costs	$1.1	$1.0
Sales & marketing	$8.8	$6.9
Content & product dev.	$3.3	$3.8
Warrant charge	$5.0	NA
Sales & administrative	$1.3	$1.5
Depreciation & amortization	$2.9	$2.4
Operating loss	($15.7)	($6.3)
Interest income	$0.8	$0.9
Net loss	($14.9)	($9.3)
EPS	($1.17)	($0.73)
Shares outstanding	12.779	12.672
Gross margin	84.1%	81.7%
Operating income*	(162.3%)	(192.9%)
Net income*	(150.0%)	(176.0%)

*Excludes one-time warrant charge

To be concise, the earnings were roughly about where we expected them to be. Probably the most encouraging thing to see was that the company's margins continued to improve quite nicely. While still nowhere near attaining profitability, over the past year the company has been able to shrink both its operating and net losses relative to sales. Much like Drugstore.com, improving margins is a vital and measurable step towards the company attaining profitability. Next quarter, we'll again be looking more at the sales growth and margin situation than at the absolute losses.

LAUNCH'S STOCK PRICE OVER THE PAST THREE MONTHS



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TIMELINE

3/3/00 ($17.38) — W.R. Hambrecht initiates coverage of Launch with a "Market Outperform" rating.

2/16/00 ($21.63) — Launch's interactive online radio station, LAUNCHcast, comes out of beta testing.

1/31/00 ($17.50) — Deal is signed where online retailer CheckOut.com will become the exclusive provider of pre-recorded CDs, cassettes, video games and videos for Launch. Launch will also provide content to CheckOut.com and will receive a small commission on each sale generated through its site.

1/27/00 ($21) — Time Warner and EMI agree to merge, shaking the entire recording industry. Both EMI and Time Warner own minority stakes in Launch.

1/26/00 ($21) — Fourth-quarter earnings are released. Launch reports sales of $6.6 million in the fourth quarter and a net loss, after extraordinary items, of $14.9 million.

1/25/00 ($22.44) — Raymond James starts coverage of Launch with a "Strong Buy" rating.

1/18/00 ($16) — Launch acquires California company NVS, a firm that specializes in streaming videos to commercial establishments like shopping malls, restaurants, etc. Terms of the deal were not disclosed.

1/12/00 ($18) — Launch and Time Warner reach deal where Warner's content, including its music videos, are fully licensed by Launch. Time Warner will receive a small royalty on each video played, and the company also agreed to take about a 1% equity stake in Launch.

Appendix
Media Metrix Data

Top 50 Digital Media/Web Properties
Combined At Home and At Work

(1/1/00 through 1/31/00)

Rank	Digital Media/Web Properties	Unique Visitors (000)
Total	**Universe**	**72,722**
1	AOL Network · Proprietary & WWW	56,457
2	Yahoo Sites	44,258
3	Microsoft Sites	42,673
4	Lycos	31,404
5	Excite@Home	25,439
6	Go Network	22,666
7	NBC Internet	16,700
8	Amazon	15,480
9	AltaVista Sites	13,439
10	About.com Sites	13,160
11	Time Warner Online	12,996
12	Go2Net Network	12,584
13	Real.com Network	12,351
14	eBay	11,587
15	ZDNet Sites	10,684
16	LookSmart	10,293
17	CNET	9,458
18	Weather Channel, The	8,921
19	JUNO / JUNO.COM	8,387
20	Infospace Impressions	7,633
21	GOTO.COM	6,899
22	Viacom Online	6,865
23	AT&T Web Sites	6,855
24	BARNESANDNOBLE.COM	6,477
25	Ask Jeeves	6,352
26	IWON.COM	6,330
27	CitySearch-TicketMaster Online	6,129
28	iVillage.com: [The Womens Network]	5,976
29	Snowball	5,906
30	Fortunecity Global Community	5,861
31	earthlink.net	5,390
32	freelotto.com	5,276
33	smartbotpro.net	5,199
34	bonzi.com	5,100
35	News Corp. Online	5,005
36	MarketWatch.com Sites	4,928
37	Theglobe.com Network	4,862
38	Sony Online	4,853
39	Uproar Network, The	4,765
40	travelocity.com	4,719
41	CDNow, Inc.	4,642
42	directhit.com	4,451
43	mypoints.com	4,441
44	Sportsline.com Sites	4,390
45	Women.com Networks, The	4,310
46	MindSpring	4,293
47	Shockwave	4,200
48	lifeminders.com	4,179
49	mapquest.com	4,154
50	Discovery Network	4,085

Top 50 Websites
Combined At Home and At Work

(1/1/00 through 1/31/00)

Rank	Websites	Unique Visitors (000)
Total Universe		**68,325**
1	yahoo.com	43,338
2	msn.com	34,170
3	aol.com	31,376
4	microsoft.com	26,025
5	netscape.com	22,845
6	go.com	20,334
7	lycos.com	17,926
8	passport.com	16,636
9	hotmail.com	16,410
10	amazon.com	14,703
11	excite	14,060
12	bluemountainarts.com	13,014
13	altavista search services	12,697
14	tripod.com	11,727
15	ebay.com	11,547
16	real.com	11,514
17	angelfire.com	10,800
18	snap.com search & services	10,719
19	zdnet	10,467
20	about.com	9,913
21	weather.com	8,921
22	looksmart.com	8,920
23	xoom.com	8,337
24	cnet.com	8,233
25	msnbc.com	8,184
26	infospace.com	7,581
27	disney online	6,919
28	goto.com	6,899
29	barnesandnoble.com	6,477
30	iwon.com	6,330
31	askjeeves.com	6,264
32	earthlink.net	5,390
33	espn	5,374
34	freelotto.com	5,276
35	smartbotpro.net	5,199
36	bonzi.com	5,100
37	ivillage sites	4,997
38	sony online	4,853
39	macromedia.com	4,817
40	travelocity.com	4,719
41	cnn.com	4,706
42	windowsmedia.com	4,650
43	cdnow.com	4,616
44	go2net.com	4,605
45	icq.com	4,578
46	pathfinder.com	4,563
47	uproar.com	4,526
48	expedia.com travel	4,493
49	directhit.com	4,451
50	mypoints.com	4,441

What do you think?
PLEASE FILL OUT THIS QUICK ONLINE SURVEY!

Chart Definitions

Digital Media: Includes users of the World Wide Web, proprietary online services, and/or other ad-supported digital applications such as e-mail services and CD ROM.

Top 50 Digital Media & Web Properties: The top 50 Digital Media & Web properties are based on unduplicated audience reach, also known as unique visitors. "Digital Media & Web Properties" include the largest single brands as well as consolidations of multiple domains that fall under one brand or common ownership.

Top 50 Web Sites: The top 50 Web sites are based on unduplicated audience reach, also known as unique visitors. Top sites are from Media Metrix' At Home and At Work samples.

Unique Visitors: The actual number of total users who visited the reported Web site or online property at least once in the given month. All unique visitors are unduplicated (only counted once) and are in thousands.

Average (Daily) Unique Pages per Visitor in a Month: The average number of different page requests made per day over the course of the month by those persons visiting the specific site or category.

Our Next Issue

The May 2000 issue of *The Motley Fool Internet Report* will cover the emerging "Internet Incubator" industry, whose early leaders include **CMGI** (Nasdaq: CMGI) and **Internet Capital Group** (Nasdaq: ICGE). Companies like these are being joined by many other, young public companies that also hope to create tremendous market value by investing in online business. If you have questions regarding the Internet incubator industry that you'd like to see addressed in our forthcoming issue, please post them on the *Internet Report*'s message board before April Fool's Day arrives. Post here:
http://boards.fool.com/Messages.asp?id=1010019000143001

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