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Towards Web-Based Investment Banking

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Abstract

New opportunities for all types of business arise as the Internet expands, and companies are keen to establish a presence on the web. Nevertheless, many web-based businesses fail to recognise the demands of operating a prosperous business in the rapidly changing virtual world.

This article seeks to discuss and analyse the prospects and developments in web-based investment banking through a case study of the process of launching the web-based investment bank, Wit Capital. The fundamental concept in the process has been to combine Internet technology with investment banking. The process is described from its initiation and up to the present day. Success factors and obstacles on the way are covered. Wit Capital has continuously aimed at keeping costs for its customers at a minimum, and the company has experienced some success at each stage of its development.

In conclusion, the article notes that ‘barriers to entry’ are comparatively low for all companies in the virtual world, and it therefore remains to be seen whether there will be a long term ‘first mover’ advantage, both in the case of Wit Capital and generally in e-commerce.

1 Introduction

The Internet explosion has provided new opportunities for all types of businesses. According to the Organisation for Economic Co-operation and Development, ‘the current US$26 billion global e-business market will explode to US$1-trillion in the next seven years’. Companies are keen to establish a presence on the web. Existing companies are finding that new e-commerce competitors are emerging daily with easy access to start-up capital from venture capitalists. As a result, many firms have
attempted to either transfer their proven market niche to the web, or develop a new position on the web. Yet, many web based businesses fail to recognise the demands of operating a prosperous business in the rapidly changing virtual world. This case analyses the process of launching the web based investment bank, Wit Capital (www.witcapital.com). The focus is on the steps taken to transform the company from ‘brewer to banker’. The different phases of growth and development from 1995 to the present day are be analysed, and the success factors, obstacles, and concerns for the future will subsequently be discussed.

2 Investment Banking: Business Environment and Recent Trends

Investment Banking contains several business operations, most notably mergers & acquisitions (M&A), debt capital markets (DCM), private equity, and equity capital markets (ECM). The latter comprise Initial Public Offerings (IPOs), Secondary Public Offerings (SPO) and Follow-On Public Offerings (FPOs), and private placements. DCM and ECM seem to be the areas most likely to come under threat from web based industry developments, in large part due to the ability of customers and issuers to directly interact (the brokering and sales force intermediaries are effectively eliminated). The success of on-line brokerages, like, for instance, Charles Schwab, is testament to this market development. Our research will focus on this area of investment banking.

Traditionally, the requirement for a large infrastructure has, as barriers to the investment banking and underwriting industry, provided a significant deterrent to new. History, a strong reputation, significant financial backing and conformity with a number of rules and regulations, such as the Securities and Exchange Commission (SEC), were notable obstacles to entry. Recently, however, the face of the industry has undergone a major transformation. The challenges today are analogue to those faced by the commercial banking industry in the 1980's (Channon, 1998; Holland et al., 1998; Loebbecke and Jelassi, 1993), with disintermediation requiring established companies to adjust to new entrants (Lux, 1996).

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1 An Initial Public Offering (IPO) is a corporation's first offering of a security representing shares of the company to the public. Growing companies typically use IPOs to raise capital for future business expansion. Generally, an underwriter prepays the issuer for its stock and then goes to the public market to sell it.

2 A Secondary Public Offering (SPO) is the public sale by shareholders of previously issued securities that are already trading publicly. In underwritten Secondary Offerings, a selling shareholder or corporate issuer sells securities to an underwriter who, in turn, resells the securities to investors at the offering price.

3 Follow-On Offering (FPO) is the public sale by an issuer of newly issued securities by a company which already has publicly traded securities. In underwritten Follow-On Offerings, a selling shareholder or corporate issuer sells securities to an underwriter who, in turn, resells the securities to investors at the offering price.
Software, insurance, telecommunications, and independent start-up companies have begun to offer Investment Banking services over the Internet several years ago (Lux, 1996). The most significant competition a player like Wit Capital currently faces comes from companies such as Direct IPO Inc, and Etrade Securities Inc., or VentureCapial.com. Furthermore, the established players in the industry are undergoing a wave of mergers and acquisitions, such as Bankers Trust and Deutsche Bank, Travellers Group and Solomon Smith Barney etc. These activities can be interpreted as their attempt to strategically position themselves to compete in the global investment banking market, broadening the range of services offered to clients. In other words, the industry is expanding every day.

The most significant pressure the investment banking industry has faced is that of improving technology (Lockett and Holland, 1996). Mass trading systems, such as ‘Instinet’ and ‘Posit’, are capable of directly matching buyers and sellers (see also Bakos, 1998). These services significantly diminish broker commissions and spreads, which constitute the major source of investment banking revenue. However, these services are currently only available to large institutional investors. Many established investment banks are working in partnerships to develop reliable on-line trading systems. A strong reputation seems to be crucial for integrity and compatibility of systems among the major players.

Moreover, the degree of competition among existing investment banks is high. Within capital markets, billions of dollars change hands every day. The investment banks play the role of intermediaries and as a result, they compete based on a ‘spread’. Over the past couple of years, discount brokerage houses such as Charles Schwab, have gained popularity among consumers as they apparently offer equivalent services for lower prices. The ability of the web to reduce costs even further and pass on increased savings to customers has forced both big and small banks and ECM raisers to become more competitive on all levels.

3 Research Approach

This case research (e.g. Lee et al., 1992; Orlikowski and Baroudi, 1991; Yin, 1990) investigating one of the first online investment banks is exploratory in nature. It is based on qualitative interviewing (Rubin and Rubin, 1995) and documentary materials. The reason for choosing the qualitative approach clearly lies in the exploratory nature of the study, and the desire to understand the collected data in the organizational context. Interviews have been conducted on site and over the telephone, further clarifications have been reached via e-mail between September 1998 and July 1999. The actual description of the gathered data and the analysis and interpretation have been separated to allow the reader to apply own conclusions and assessments of the economic potential for the case company ‘Wit Capital’ as well as similar start-ups in the field (e.g. Miles and Huberman, 1984; Silverman, 1993).
4 Company Overview

Wit Capital (www.witcapital.com) is a privately owned on-line investment bank that was founded by Andrew D. Klein in April of 1996. The idea for the company grew out of the success of the Internet Initial Public offering of Klein’s Spring Street Brewing Company, which began in March of 1995. Wit Capital has been widely recognised as an innovator in the field of electronic commerce, and is credited with the world’s first ever Internet Initial Public Offering (IPO), the Spring Street Brewing Company in 1995.

With offices in New York and San Francisco, Wit Capital is an issuer-driven Internet company that offers an array of investment banking services, including underwriting for public offerings, private equity services, and strategic advisory. Wit Capital also offers individual investors online brokerage services that include access to IPOs and other securities offerings that previously only were available to institutions and wealthy individuals. So far, Wit Capital has participated in over 130 public offerings (see also witcapital.com/scripts/stok/past-ipos.idc). Wit Capital is a registered broker-dealer and a member of NASD and SIPC. It is a publicly traded company listed on NASDAQ under the symbol ‘WITC’.

Wit Capital’s mission is to “be the premiere Internet investment banking firm focused on the offering and selling of securities through the Internet to a community of online individual investors” (www.witcapital.com). The company employs no commissioned brokers, and has hence limited pressure to buy or sell.

4.1 The Concept in a Nutshell

The fundamental concept behind Wit Capital is to employ new technology, particularly the Internet, to circumvent the traditional investment banking capital markets business model. The traditional process involves high transaction costs as a result of the number of intermediaries involved. Figure 1 below outlines the value-added costs a customer could expect to see in a traditional stock transaction (Wigand and Benjamin, 1995).

![Figure 1: Value added Steps for an individual to trade equities](chart)

Each intermediary involved earns a spread on trades. The costs add up, and are transferred to the customer in the form of higher fees. Wit Capital can offer lower prices per trade, as customers are not subject to order flow, market maker, and the majority of brokerage fees.
In terms of IPOs, Wit Capital has developed a new way for companies to raise relatively small amounts of money, while minimising costs. This has been achieved by a combination of reducing costs and maximising exposure through the use of the Internet.

### 4.2 Products and Services

Wit Capital’s core business is Investment Banking, but the company has recognised that it will take time to build up this core. In the meantime, the company has broadened its focus to include equity trading, hoping that it someday will be able to facilitate trades free of charge (computerworld.com June 17, 1996). Its current product and service offerings include:

- **Public Underwriting**, having pioneered the business of online retail distribution of public offering shares and offers services concerning Initial Public Offerings, Secondary Offering and Follow-On Offerings, and Combination Offerings (capital raising services).
- **Financial Advisory Services**, developing Internet strategies and business in connection with mergers and acquisitions.
- **Private Equity**, assisting private and public corporate issuers, as well as investment funds, in raising private capital.
- **Investment Research**, intending to disseminate the research for free on our Web site to.
- **Digital Trading Facility** (late 1999), allowing Members to buy and sell shares of NASDAQ and listed companies directly with other investors and thus potentially avoid the spreads maintained by market makers and specialists.

By using the Internet to lower transaction costs drastically, Wit Capital has found a niche in the investment banking industry. Membership is free, but requires a minimum bank balance of at least $2,000 in cash and/or securities, and the cost of trading begins at $14.95 for a market order.

### 4.3 Target Market - Companies and Customers

In the IPO sector of the business, Wit Capital has targeted businesses aiming to raise between US$5 and US$10 million. Businesses this size would be unprofitable for large investment banks, but does provide Wit Capital with a largely untapped target market. WIT aims to lower costs associated with traditional IPOs such as legal fees, consulting fees, underwriting fees, syndicate fees, and on-cash expenses. Hence, it provides a practical and affordable alternative for smaller companies.

Wit Capital focuses on multiple tiers of investors,

- the ‘accredited investor’, who is willing to invest about US$1 million in a venture deal, but not the US$3 million plus often needed,
- the US$100,000 to US$300,000 wage earner, who often does not find opportunities for US$100,000 placements, and
the ‘sophisticated but not rich’, who earns between US$75,000 and US$100,000 and may work in the same field as the deal Wit Capital is offering. He is likely to invest in the US$5000 to US$10,000 range.

5 The Evolution of Wit Capital - From Brewer to Banker

5.1 Phase 1 ‘Wit Beer’- Idea, Web-Site, and Issuing of Illiquid Shares

The first development phase started with the need to raise capital for Spring Street Brewing Company. The company decided to attempt this via the Internet. It was uncharted territory at the time, and represented as such a great deal of uncertainty.

The company needed to establish a web site. After a long deliberation, the company settled on a simple and straightforward design. This was seen as essential, as Wit Beer customers were initially the targeted investors. The web address was added to beer labels, posters and coasters. A ‘fancy’ web page, the company reasoned, might lead customers to believe that the offer was not intended for the ordinary investor. As such, the site contained a collage of beer labels, history, information about the company, and a separate section for the stock offering.

The stock offering section was arranged in a manner that eliminated a number of costs. For starters, there was a hyperlink to the prospectus. Potential investors were able to view, download, and print the prospectus. Furthermore, the prospectus included a subscription agreement, which could be printed out, and acted as an order form for the IPO. Investors could fill out the agreement, state how many shares they were interested in, and send a cheque along with the agreement to Spring Street’s office. This saved Spring Street Brewing Company the cost of toll-free telephone calls, printing, and mailings.

Spring Street Brewing Company also created a database to automatically process stock orders. Once it was established that the investors were within their legal rights to obtain the stock and the checks were cleared, the stock certificates were automatically printed.

Within a short while, the media proclaimed Spring Street Brewing Company had performed the ‘world’s 1st IPO on the Internet’ (WallStreet Journal Feb. 9, 1995).

By December 1995, Spring Street brewing Company had sold over 860,000 shares to 3,500 new investors and raised US$1.6 million in fresh capital (Klein 1998). The IPO only incurred a US$200 monthly cost for a web site, and attracted interest from all over the world.

However, the IPO did not provide investors with the secondary trading market that accompanies traditional IPOs. Essentially, owners of Spring Street stock had purchased illiquid shares. Nevertheless, in the months following the closing of the IPO, Spring
Street Brewing was receiving a number of requests for the stock and the number of web page hits was consistently rising. This demand was unexpected and inspired Spring Street Brewing Company to seek a method to create liquidity.

### 5.2 Phase 2 ‘Wit Trade’ - Becoming Matchmaker

In order to create liquidity in Spring Street Street stock, Wit Trade was created in March of 1996. Wit Trade was a site separate from that of Spring Street Brewing Company. The sole function of Wit Trade was to facilitate the trading of Wit Beer stock through the use of HTML bulletin boards. Figure 2 below illustrates how the bulletin boards would appear to customers. The seller said at what price he/she was willing to sell at and this was visible to the buyer.

![Figure 2: Appearance of HTML Bulletin Board](image)

Investors interested in trading the stock posted messages, and had access to read and answer messages posted by others. After an agreement had been made, Wit Trade stepped in to facilitate the trade. Wit Trade created a contract that would bind the customers to the transaction. The contract was prepared in a manner so that it could be e-mailed back and forth, further reducing costs.

It was necessary for Wit Trade to provide protection for their investors. This required Wit Trade to act as an intermediary, so customers could rely on the negotiated deal (see Figure 3). Essentially, Wit Trade would hold the buyers check until it cleared and had received the stock certificate from the seller. Once these requirements had been met, the company would distribute the money to the seller and a new stock certificate to the buyer.

![Figure 3: The Role of Wit Capital](image)
As Wit Trade was performing a market making function for stock in Wit beer, it recognised that customers need additional information to base their transactions on. Again, the Internet ‘offered’ to save the company money. The hard facts that investors often demand when deciding whether to invest in a company can be expensive to distribute. Wit Trade made all of the Spring Street Brewing Company financial data available on-line. Annual reports, prospectuses, and press releases were available for downloading and printing. Furthermore, financial data could be imported into spreadsheets where the data could easily be analysed.

The positive notion for Wit Trade filtered through the media, as press releases were distributed before the launch of the service. Journalists were invited to the ‘grand opening’ where the technology was going to be demonstrated. Wit Trade received strong media exposure, and the site launching was a success. According to Andrew Klein (1998), “within hours of launching the system, tens of thousands of people had visited the Wit Trade site and looked at our materials”.

A few days after the launch, the Securities and Exchange Commission (SEC)\(^4\) contacted Wit Trade and requested that the site be suspended until a review had been completed. The SEC was concerned because there were no precedents that governed on-line stock trading. The potential for fraud was high, and the SEC wanted to be sure that there were mechanisms to protect investors. Furthermore, if Wit Trade was deemed to be a brokerage house, the company could be subject to different regulations and financial requirements.

SEC was willing to work with Wit, and Wit Trade voluntarily suspended trading and co-operated with the SEC. Within two weeks, Wit Trade was able to resume trading, subject to a few modifications pertaining to customer security.\(^5\)

While Wit Trade was triumphant in creating a functioning market for Spring Street Brewing Company stock, the company was still a far from being a fully functioning investment bank.

5.3 Phase 3 ‘Wit Capital’ - Turning into an On-line Investment Bank

In April 1996, Wit Capital Corp. was founded. Initially, the company offered plain discount brokerage services similar to those offered by Internet financial companies such as E-trade and e.Schwab. Customers had the opportunity to invest in private placement and venture capital deals that Wit Capital was underwriting. In the beginning, these deals were Internet-related technology companies. This was a calculated effort to focus on companies that had a relevant affinity group (Horowitz, 1997). Wit Capital

\(^4\) SEC looks to establish credibility and integrity of market.
believed that Web users would likely constitute the majority of investors in these companies, and they would be intrigued by the idea of purchasing shares through Wit Capital.

In the first year, Wit Capital offered ten IPOs in the range from US$5 to US$10 million. These deals were successful and saved the companies substantial fees. Early success led to the expansion of services provided. Private placements, secondary, follow-on, and combination offerings were added. Wit Capital also pioneered a new stock issue called ‘Public Venture Capital Offerings’, which gave individual investors the opportunity to take small positions in companies at early stages of development.

Early 1999, Wit Capital added a fully integrated brokerage system allowing members to trade equities, mutual funds, and options on-line. Members can trade by touch-tone phone, by dialling 1-888-310-6648, or by calling a broker at 1-888-4-WITCAP. Trading securities via the Wit Capital system requires three steps, (1) clicking on the ‘trade icon’, (2) selecting the security one would like to buy or sell and approving the real-time price quote, and (3) clicking ‘submit’. All executed orders are confirmed and monthly statements are distributed via e-mail.

The system updates all order records immediately, regardless of how the orders are placed; on-line or by phone. Wit members can access this information in real-time by clicking on the ‘Members Current Position’ icon located on the site. Wit Capital members have access to NASDAQ, the New York Stock Exchange, the American Stock Exchange, over 3,800 load and no-load funds from over 150 families of funds, options, bonds, money markets, quotes, news and research.

5.4 Phase 4 ‘Wit Capital Group’ - Expanding along Scale, Geographic Spread, Scope

5.4.1 Scale

Wit Capital conducts extensive marketing campaigns on the Internet to attract new companies and investors. All new companies that register with the SEC are approached by Wit Capital. Investors are stored on Wit Capital’s database, and a profile is compiled. Wit Capital uses this profile to conduct direct marketing. For example, if there is an investor that appears to have an affinity for start-up pharmaceutical companies, Wit Capital would send an e-mail to the investor when there was going to be a public venture capital offering. Wit Capital hopes to be able to use the Internet to further reduce the costs of IPO’s by creating on-line roadshows. Wit Capital will be offering multimedia presentations on the Internet, while traditionally, companies go on a roadshow to promote themselves before a stock offering.

5.4.2 Geographic Spread

In the light of geographic expansion - due to or in spite of the global Internet infrastructure - Wit Capital Japan, Inc. was established in July 1999 as a joint venture
between Wit Capital Group, Inc. (NASDAQ: WITC), Mitsubishi Corporation, and Trans Cosmos, Inc.. Similar to its engagements in America, the company offers Japanese individual investors the opportunity to invest in public offerings and venture capital funds using the Internet and the World Wide Web. In addition, Wit Capital Japan provides Japanese Internet and Internet-centric companies with a variety of investment banking services, including underwriting for public offerings, private equity services, strategic advisory, and institutional quality research. Wit Capital Japan also targets US-based companies seeking to create Japanese joint ventures.

5.4.3 Scope
In August 1999, Wit Capital closed its first proprietary fund\(^6\) enabling the company to expand its investment banking services to corporate clients, including public underwriting, strategic advisory, private equity placements, investment research, and the management of venture capital funding. Consistent with Wit Capital’s overall philosophy, the fund was formed to allow accredited individuals to participate in venture capital investments which traditionally are available only to institutional investors.

6 Technology - The Nuts and Bolts

To compile customer profiles used for direct marketing, Wit Capital uses ‘Push’ technology, supported by IBM’s DB2/400 database.

Trading securities via the Wit Capital system requires three steps, (1) clicking on the ‘trade icon’, (2) selecting the security one would like to buy or sell and approving the real-time price quote, and (3) clicking ‘submit’. All executed orders are confirmed and monthly statements are distributed via e-mail.

The trading system consists of Kingland’s Financial Network System/Server (FNS), an IBM 66-bit, AS/400 based, mid-office commission and workflow processing and management system that interfaces to ADP and U.S. Clearing Corp. A telephony piece-FNS Direct Talk allows customers to trade portfolios over the phone via the Internet.

If an order is for a stock listed on an exchange, Wit Capital’s system records the order and routes it through ADP to the NYSE. The order is printed on tape through SIAC and reported to U.S. Clearing Corp. where payment is settled in T+3. However, Wit Capital has plans to move to T+0 in the near future. EPIC is the interface that facilitates this chain of events.

For communication on the investment banking service, Wit Capital uses a TCP/IP FIX 4.0 format, carried over a dedicated network using the IBM Global Network as a Backbone. A mix of protocols are used; SNA, TCP/IP, and bisync. A FNS backbone

\(^6\) Arista Capital Partners LP, a US$39.45 million Internet-related private equity fund.
determines which format, message type, or protocol to use. The system is capable of performing checks to ensure customer validity and to verify that legal regulations are not being violated by transactions. Wit Capital also has the ability to stipulate any additional criteria the company wishes to monitor. For example, the company could subject all trades over $15,000 to immediate review.

Wit Capital’s answer to Customer Delays is load-balancing software acquired from California based Global Center. This software is capable of handling millions of hits per day, and provides protection from freezing and delays during trading rushes (Hemblen, 1998). The system received its first real test during the October 1998 stock market plunge and proved to be successful.

Wit Capital has displayed a strong desire to be at the forefront of trading technology from its inception, and as a result has been able to adapt to the rapidly changing environment that characterises the Internet. This became evident when the company purchased the EPIC trading system. EPIC, which stands for ‘electronic price improvement center’ was ‘adapted from Christopher Keith’s Chicago match system written for the Chicago Stock Exchange’ (Duffy 1997). In addition to acquiring the software, Wit Capital hired Keith, and his ten person development team.

7 Obstacles and Success Factors

As a front runner in the Internet based sector of the investment banking industry, there was considerable risk that the venture would fail. Wit Capital faced three major obstacles on its way to becoming an on-line investment bank. The effective handling of these constraints allowed the company to proceed towards its goal:

• Wit Capital faced considerable backlash from the community of brokers. They were concerned that services like Wit Capital would cut into their spreads, and as a result refused to send Wit Capital any of the orders they received, even if Wit Capital could provide their clients with a better price! Hence, Wit Capital gave up the idea of brokers sending them orders, and instead focussed its efforts on a marketing campaign.

• The Securities and Exchange Commission (SEC) presented what could have potentially been the biggest barrier to trading on the web (see above). Yet, the SEC’s and Wit Capital’s willingness to co-operate made it possible to achieve an advance in the world of investment banking.

• Due to the lack of Internet commerce laws, Wit Capital had to be sure that it was not violating any securities laws. Namely, Wit Capital’s stocks had not been cleared for sale in all countries and states. Wit Capital dealt with this by returning checks from people who lived in states where the stock offerings had not been cleared.

Yet, Wit Capital has enjoyed some success at each stage of its development. The main success factors read like a - by now -widely accepted e-commerce recipe book (see Table 1):
**Effective planning**

Through each stage of the development Wit Capital focused on a clear objective. From raising capital, to providing a liquid trading mechanism, and finally functioning as a small, but full service investment bank, the company had a clear vision.

**Niche strategy**

Wit Capital did not intend to compete head on with the big investment banks, instead the company focussed on the previously untapped small business IPO niche market. This avoided a competitive assault by companies that had access to large amounts of capital. Wit Capital was recognised as a company that was clearly distinguishable from traditional investment banks.

**First mover advantage**

The fact that the company was one of the first of its kind, attracted interest from people who were intrigued by the idea of an on-line investment bank. Wit Capital intended on sustaining this interest and focused heavily on both customers and the media to achieve this goal.

**Media presence.**

The media was involved at every stage of company development, press releases, 'grand openings', company tours and product demonstrations increased Wit Capital's visibility to the general public. Founder and chief strategist Andrew Klein promoted himself as a man with a vision, working in the interest of the individual in a world dominated by large corporations. This created recognition and a positive image to be associated with what many people initially believed was a 'gimmicky product'.

**Community building**

Customers were required to become part of a 'community' and became 'members' in Wit Capital.

**User friendly system design**

First time users found that trading via the Internet was easy, and that trading or investing on-line could realistically eliminate brokers and hence provide substantial savings.

**Updated information offering**

Wit Capital constantly upgraded the site to include important information and increased access to services. Links to established and reputable resource sites, such as CBS Marketwatch, Hoovers, Investors Online, and Wired Magazine were added.

**Strategic partnerships and alliances**

The company formed a number of partnerships with experts in the field of electronic commerce, such as Global Trade Inc., Quick & Reilly, and Mezzina/Brown. This allowed Wit Capital to concentrate on the core activities of its business.

**Flexibility**

Wit Capital has managed to stay atop the competition due to active restructuring. The company has recognised that operating in the virtual world is incredibly dynamic, and accordingly has built flexibility into its business processes and technology.
Value for money to customers.
Wit Capital offered customers access to products they were already purchasing, but at a substantially lower cost.

Additional revenue sources.
Wit Capital found a subsequent source of revenue by selling space on its web page. Research companies and magazines listed in the research and quote section, pay rent to Wit Capital.

Table 1: Wit Capital Success Factors

8 Outlook and Lessons Learnt

In the beginning, when pushing for the innovative business model and working towards becoming a pioneer in online investment banking, Wit Capital was able to keep costs to a minimum as the technology employed was quite plain. However, as the company has evolved, costs have risen rapidly to millions of dollars. In order to arrive at an accurate conclusion of economic success cost-benefit analysis to date would have to be conducted over a number of years.

The company has clearly enjoyed a ‘first mover’ advantage in many respects. But ‘barriers to entry’ to operations are comparatively low in the virtual world, even to competition. The extent to which branding, privileged relationships, and recognition will provide a long term ‘first mover advantage remains to be seen.

In the future, Wit Capital intends to offer on-line trading for free. Revenue would be generated from taking a percentage of the shares in the IPOs that the company conducts. Free trading could shake up the investment banking industry, as both discount and traditional brokers would see their core source of income disappear. In the short to medium term, however, clients also buy respectability, personal insight from brokers, and research analysts’ views when they pay for a trade.

Concerning the further developments of online investment banking, security issues and legal constraints have to be monitored. Currently, the biggest threat to the viability of Internet trading seems to be security. While market activities demonstrate that ongoing requirements have been met, the security issue has turned into a probability ‘game’. One security breach and the entire industry may suffer an enormous setback. The development of laws and regulations for Internet business are have to be monitored closely and continuously. Electronic commerce has naturally developed more rapidly than cyberspace law. In the near future companies may expect to see the law catch up with the technology and will need to adjust to new legislation.

Financial intermediaries will have to adapt to keep pace with the rapidly changing environment of the securities industry. In the future, it is likely that consumers will be able to trade directly with each other, and avoid the costs associated with the traditional process. It is clear that the Internet is capable of providing a functioning market, and undoubtedly more companies will take advantage of it as a method to raise capital.
Wit Capital became a success by facilitating its own Initial Public Offering. What is to stop other companies from doing the same? This presents a considerable threat to Wit Capital’s core business as numerous companies have followed. However, these companies have had mixed success rates and have not benefited from the media frenzy that accompanied the ‘1st ever Internet IPO’. These companies are also subject to increasing concerns about Internet fraud. Wit Capital was the first, and as such, the name still carries with it a sense of security to investors.

References


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