

MARCH 19, 2001



## The Mighty Mini-Dots

Small, frugal, and unflashy, they are making money where the big guys couldn't. When Aron Benon founded [Florist.com](#) in 1997, his strategy couldn't have been more different from the many dot-coms then exploding onto the Web scene. Instead of raising millions of dollars in venture capital, he converted half his tiny Beverly Hills (Calif.)-flower shop, Floral & Hardy, into a threadbare online operation and hired just four employees, including his wife. Still pinching pennies, he told his Web employees to bring cell phones to work the week before Valentine's Day, so they wouldn't tie up the company's bare-bones phone system.

Roughing it paid off big time for the online small fry. Last year, Florist.com turned a \$1 million profit on \$3 million in sales. Benon's success stands in stark contrast to the fast rise and even faster failure of other, more high-profile gift sites such as Send.com, which bit the dust in January, a year after blowing \$20 million on a quirky ad campaign. "I knew the bubble was going to burst," says Benon. "I said, 'No, I'm going to keep it grassroots.' We take one baby step at a time. Only when the business proves itself to us will we spend the money to get bigger."

Dot-coms may be going down in flames every day, but a surprising group of Web survivors is emerging unscathed: small businesses, the mighty mini-dots. With just a handful of employees and annual sales of \$5 million or less, these intrepid independents are doing what almost none of their venture-capital-funded brethren could: make money online.

Who would have thought? After the rise of big dot-coms such as Amazon.com Inc. ([AMZN](#)) and the later arrival to the Web of big retail chains such as Wal-Mart Stores Inc. ([WMT](#)), a lot of experts predicted the Web giants would crush small businesses like bugs. Instead, it was other dot-coms--all playing high-stakes, get-big-fast games with multimillion-dollar portal deals and tv ads--that got slammed. Thousands of small businesses, flying under the radar, are turning modest but healthy profits.

Already, the evidence is coming in. The National Trust for Historic Preservation, which tracks business in city downtown districts, reports that Main Street merchants have logged an average 12.8% increase in sales since launching their Web sites. Says Kennedy Smith, director of the Trust's Main Street Center: "That kind of boost can make a huge difference in profitability." According to ActivMedia Research, 44% of companies with fewer than 10 employees turn a profit on their Web sales, compared with 26% of companies with 100 employees or more.

**Size matters.** Now, these mini-dots are proving they're an online force to be reckoned with. Indeed, they're teaching their bigger rivals a thing or two--including the value of

common sense. Unlike some dot-coms with inexperienced executives, the mini-dots are succeeding by employing the same strategies that small-business owners have relied on for centuries: They're sticking to niches they know well. They scrimp on expenses, forgoing expensive portal deals and using Net resources, from e-mail to customer-sharing arrangements, to save money. And they're banding together on the Web, presenting a bigger face to the online world.

So far, it seems to be working--so well that small businesses appear poised to play a greater role in the growth of e-commerce than anyone expected. Small companies will see their online sales grow 336% from 2000, to \$120 billion by the end of 2002, predicts ami-Partners Inc., a New York consultant to small and medium-size businesses. That will outpace overall e-commerce revenue growth of 249%.

Of course, size matters, even in the New Economy. But in some crucial ways, the Net helps level the playing field for small outfits. For one thing, the cost savings of selling online and dispensing with store rents or direct-mail costs makes some businesses viable that otherwise wouldn't be--say, a home-based collectibles business.

Moreover, the global nature of the Web goes a long way toward negating one key disadvantage of the small fry: geographic reach. Now, even a niche seller of specialty pet supplies can amass enough customers to be viable. Finally, the easy communications afforded by the Net may make more small businesses, especially services such as graphic design, attractive to larger businesses seeking to outsource jobs.

The impact of a mini-dot explosion could have big implications beyond the Web. By 2004, even the tiniest of these e-merchants--those with fewer than 10 employees and \$3 million in annual sales--could account for as much as 10% of the U.S. gross domestic product, according to e-commerce researcher Keenan Vision Inc. While President Vernon Keenan concedes that's an "aggressive" forecast, it may not be unreasonable, says Small Business Administration chief economist Robert E. Berney, who says that small businesses overall currently produce more than 40% of gdp. "Small businesses online are going to be a significant economic force," says Keenan. "The Web is just going to be the way to do business."

Maybe so, but big questions remain about how much the Net will boost the number of small businesses and what impact they'll truly have on the economy. For one thing, says William C. Dunkelberg, chief economist for the National Federation of Independent Business, it's possible the Net is simply shifting existing sales online, not expanding markets enough to support many new businesses. "The Web isn't going to increase the number of blue jeans people buy," he says. And, he adds, it's likely that the most successful online businesses will put the other mom-and-pops out of business, lessening the net gain. Most traditional small businesses fail, and the same may well be true online.

And for all its advantages, the Internet presents a lot of challenges to the little guys, too. In many parts of the country, pokey Net connections limit how many visitors these sites can handle. And it can be tough for traditional businesses coming online to handle both channels at once. Those factors may explain why, for all the small businesses that have launched online, many more have not yet moved beyond sites that are nothing more than online brochures. According to ami-Partners, 22% of small businesses had Web

sites in 2000, but only 8% were engaging in e-commerce.

Still, none of these challenges has stopped a growing number of small businesses from embracing the Web as a new sales channel and productivity tool. Many of the online newbies are longtime Main Street merchants or industrial-goods manufacturers. There's also a raft of service providers--computer programmers, graphic designers, lawyers, and such--who have left Corporate America to hang a shingle on the Internet.

The Web is spawning new breeds of small companies, too. They include tens of thousands of people who never ran a business before but now make a living selling collectible ornaments, antique toys, and other odds and ends on sites such as eBay Inc.'s ([EBAY](#)). About 13,000 stores have sprouted on the Yahoo! Stores section alone since June, 1998. Says Shannon Ledger, vice-president and general manager of Yahoo! Inc. ([YHOO](#)) production: "Clearly, there is now a core set of merchants using the Internet as their primary way to make money."

What these disparate businesses have discovered is that the Net is less a magic carpet to a newfound land of riches than a tool to turbocharge an already sound business model. "The Internet is what the telephone was when it was invented--a way to further our reach," says Wendy Haig, founder of Washington (D.C.)-based Global Strategy Corp., which counsels troubled dot-coms. "We didn't call that t-commerce, and we didn't rely on it to bring us revenues. With its vast reach, the Internet will enhance any small business that uses it properly."

How so? First, they're using the Net's access to a global customer base to zero in on defensible niches, instead of offering all things to all Web surfers. Pets.com Inc., for instance, went bust in December partly because it tried to sell all kinds of pet supplies--even huge bags of inexpensive dog food with high shipping costs and margins under 10%. By contrast, Lee (Mass.)-based [Waggin' Tails](#) sells scarce items such as Provi-Tabs dog vitamins and Hi-Tor prescription cat food. That allows the Web store to charge high enough prices to turn a 30% profit margin on well under \$5 million in annual sales. "Are we the cheapest game in town? No," admits founder John Gigliotti. "But our customers typically can't find a full-blown selection of super-premium foods in their local pet shop, so they're not very price-sensitive."

In some cases, the Web's global reach has allowed entrepreneurs to offer entirely new types of narrowly focused services. Patti Glick, a San Francisco nurse trained in podiatry, makes a living speaking at companies on foot health and safety. Before, she had to do a lot of personal networking, such as mingling at Toastmasters meetings. Now, by participating in various online podiatric sites and women's portals, Glick has drawn corporate customers intrigued by her screen name, "footnurse." "When they see me online, there's a natural curiosity," she says. She expects to earn \$30,000 this year working part-time hours that allow her to spend time with her 10-year-old twins.

Small businesses also are using the Net to save big bucks--enough, in many cases, to make a pipe dream a going business. Selling Beanie Babies and other collectibles online out of a bedroom in his Lawton (Okla.) home, Perry Calton is grossing annual sales in the low six figures. Says Calton: "I never figured I could make a living doing this."

Besides saving money, the Net also provides mini-dots a wealth of new marketing channels. E-mail and discussion newsgroups can be far less expensive and more

effective than direct mail and print or tv advertising. Carrie Hardy, founder of Aurora (Colo.)-based scrapbook-supply site Scrappin' Happy, sends newsletters to 1,100 past customers and posts messages on scrapbooking newsgroups. Instead of buying \$80, three-line ads in trade magazines that never drove any traffic anyway, she spends nothing and gets a far better response: After mailing her February newsletter, sales doubled the next day. "Online promotions are far more productive," she says.

No online marketing channel has proved more effective than online auctions, pioneered by eBay in 1996. Besides spurring the formation of thousands of new small businesses online, they have prompted existing businesses to branch out. Some wholesalers are using eBay to go retail: Andrew J. Waites took his Hattiesburg (Miss.) retail overstock business, Inventory Procurement Services, directly to consumers over eBay--leading to what he hopes will be a twofold-plus jump in sales this year, to \$7 million, and a gross profit margin online of 50%, 10 times the original business.

Finally, the Net has allowed farflung small businesses to gang up and pool their resources against their bigger and louder competition in ways they can't do in the physical world. The American Booksellers Assn., which promotes independent bookstores, runs a program called BookSense.com that allows members to offer amenities only big chains could offer before, such as gift certificates good at any member store. Moreover, their online customers can order any book in print from their site, even if they don't stock it themselves. Kerry Slattery, owner of Skylight Books in Los Angeles, partly credits the program for a higher-than-expected 15% rise in her store's sales in 2000, to \$1 million.

**Daunting prospect.** All that's not to say the Web can turn any small business into a raging success. Most entrepreneurs are running into obstacles on the Web that are hard to overcome with limited staff and resources. One of the toughest jobs: providing superior customer service. After all, to make up for what they may lack in product breadth--not to mention customers' ability to click instantly to another site--they have to offer much more personal service. After auction glitches prompted some buyers to post negative reviews on eBay, for instance, Inventory Procurement Services' Waites had to hire four people focused exclusively on customer service.

Another challenge is Internet technology itself. Fast broadband connections are still largely unavailable, especially in rural areas, leaving many small businesses stuck with snail-like modem connections. And many worry that they could lose a lot of customers if their connection goes down. Says Deepinder Sahni, vice-president at researcher ami-Partners: "What we are hearing is that they are hesitant to put their crown jewels--their companies--on the Internet."

For many small businesses, the prospect of competing with the online behemoths is daunting--for good reason. It may be only a matter of time before the big guys notice how well they're doing and jump onto their turf. So they must stay vigilant, even paranoid, about differentiating their offerings. Scrappin' Happy's Hardy, for instance, continually prowls rivals such as Michaels Stores Inc. Says Hardy: "If they have something I sell, I get rid of it." To keep dodging the big guys, the small fry may well have to stay small.

That, however, is not the main worry of most small businesses that have moved online. Their problem: too much business. When Jordan Dossett posted her graphic-design portfolio a year ago on [eLance.com](http://eLance.com), a Web marketplace for freelance workers, she was buried under an avalanche of work offers from companies as far away as Russia. So she quit her job as art director for a law firm and opened The Design Studio in her Washington (D.C.) home. After hiring three employees, she expects to rake in \$350,000 in sales--and a tidy gross profit of \$250,000. "I had no idea the amount of demand out there," she says. "Suddenly, I'm slammed." Now, that's a problem a lot of dead dot-coms would love to have had.

---

By Arlene Weintraub