

# CHAPTER 9

## Technology's Impact on Business

### Zen and the Art of Net Startups

#### Banana Republic's founders try to work their magic online

by Linda Himmelstein in Greenbrae, California

Mel Ziegler remembers the exact moment he figured out the Web. It was 18 months ago when his doctor recommended he take fresh ginseng. Unsure of where to get the stuff, the 55-year-old Zen enthusiast turned to the Web. A quick search led him to a small ginseng farm in Wisconsin. Ziegler marveled at how he could instantaneously communicate with the farmer in Wisconsin while sitting at his computer in Mill Valley, Calif. He also began to wonder how he and wife, Patricia, co-founders of Banana Republic and the Republic of Tea, might use the medium for business themselves.

True, they knew little about the Internet and even less about technology. But they knew—gasp—how to build a profitable business. So when the Zieglers began scouting late last year for investors in their apparel site, ZoZa.com, Silicon Valley's best and brightest jumped. Even as the fortunes of consumer dot-coms were fading, Softbank Technology Ventures, which backed portal Yahoo and finance site E\*Trade, gladly kicked in \$12 million for a 22% stake. "We've built two very strong brands before, and we don't need parental supervision," says Mel Ziegler.

More than that, the Zieglers represent what many experts say will be the next wave of Internet hotshots: the clicks-and-bricks entrepreneurs who will benefit from offline business acumen and experience and have the advantage of previous e-tailing roadkill and successes to learn from.

ZoZa.com, the first proprietary apparel brand launched online, won't spend big on advertising or a flashy Web site. It won't sell low-margin commodity items such as compact disks. And it won't be run by twentysomething engineers. Rather, it'll be directed by a seasoned team of retail executives who know how to manage everything from customer service to inventory control. "We've done a lot of sobering up in the last several months," says Softbank partner Scott Russell. "We are now in a phase where you have to be a better business person to build an online business."

**SACK DRESS.** Set to debut in mid-October, ZoZa aims to define a new category of clothing. The Zieglers call it urban performance wear, which blends comfort, high-fashion, and practicality. The Zieglers have designed much of their tailored lines out of fabrics normally associated with sweat pants, bathing suits, or outdoor gear. The garments absorb moisture, move and stretch with the body, and are machine washable. Some items come with pouches for cell phones or handheld computers. One evening gown comes folded in a tiny bag. "We are living in the 21st century but dressing for the 20th," says Mel Ziegler. "We are offering a new proprietary product coming out of the Internet culture."

Trouble is, apparel has proven to be a tough sell on the Net. Consumers still want to touch fabrics, see colors, and try items on for size. Less than 1% of the sales of all apparel, footwear, and other fashion categories took place online last year, compared with more than 7% for such goodies as computers or books, according to market researcher Forrester Research Inc. By 2005, online apparel purchases are expected to rise to 12%, or \$43 billion, of all such sales. However, that's still less than sales of products ranging from flowers to pet supplies to sporting goods, says Forrester. "It's tough to convey image, quality, and cut of styles on a flat screen," says Forrester analyst Evie Black Dykema.

You don't have to tell the Zieglers that. They, too, have been disappointed by the Web. Initially, they planned to use virtual-reality technology so customers could mix-and-match items and feel like they were trying on clothes. They also wanted to provide a personal assistant to shoppers who could recommend items based on an individual's coloring. But the Zieglers scrapped all that when they found that the technology ruined the shopping experience because it took too long to download. "The medium is far more rigid than we imagined," says Mel, a former newspaper reporter who is writing an online magazine called *Zozazine* for the Web upstart.

Patricia, a former newspaper illustrator who designs many of the clothes, was put off by the poor quality of colors on the Web. And she was really bummed to learn how complex it was to swap out items that weren't selling well. "We have to change 27 to 32 different links to swap out just one style—from the fabric to sizing to color," she says.

So the Zieglers have gone back to basics. Although it cost roughly \$7 million to build, their

Web site is, well, stark—a picture of Zen minimalism. Navigation is simple and uncluttered. Nothing exists on the site that can't be optimally used with a standard 56K modem. The one concession to flash comes in the form of so-called mind crackers, which are Zen sayings about life hidden behind little snowflakes that have been sprinkled throughout the site.

Although the Zieglers hope most of their customers will shop online, they know many won't. So they are relying on some old-fashioned methods to market their new company and its products. In place of splashy online and television ads, ZoZa is borrowing a page from retailer Banana Republic and sending out 300,000 catalogs shortly after launch. And the company plans to build small outlets—the equivalent of brick-and-mortar kiosks—that will allow customers to sample clothing and then place orders online. The first one will open in Mill Valley in late October. And finally, ZoZa will open its first of up to 50 flagship stores in downtown San Francisco next year—a move ultimately aimed at winning customers offline before converting them to Web shoppers.

Now that dot-commers can no longer get away with endless red ink to fund their branding campaigns, the multichannel approach may be the only route left to getting known fast. "You can't go out and raise \$100 million and spend \$45 million on TV campaigns," says ZoZa Chief Operating Officer Brian Laliberte. "You have to have stores as billboards, which are also generating revenue."

**ALL SET.** You also have to be able to service customers from the get-go. Gone are the days of forgiven botched deliveries and lost orders. That's why ZoZa has outsourced virtually all of its back-end operations to logistics specialists, such as ClientLogic,

which have promised to handle as many orders as ZoZa can throw at them. Although the upstart expects to process 30,000 orders this holiday season, it has the capability to handle at least 300,000. The same goes for traffic to its Web site. ZoZa anticipates 450,000 unique visitors by yearend. But it says it's prepared to greet at least 10 times that figure.

Of course, none of this will matter if ZoZa can't meet its ambitious profit projections. Mel says the company should go into the black a year after launch—and eventually head toward an initial public offering. He expects sales to reach \$1 billion within seven years.

To get there, ZoZa is banking on hefty 60% gross margins usually enjoyed by cash-rich software companies to help it along. That can add up quickly considering that its average order is expected to be more than \$100, vs. the average \$42 order at Amazon.com Inc. What's more, the company won't face the same price pressures that the eToys of the world do, since its merchandise will only be available through ZoZa.

Dot-commers new and old will be watching to see if the ZoZa hybrid can make it. What's clear is that the Zieglers are out to create an upstart that reflects their unique personalities and the new realities for e-tailers. The dress code at the company's barren offices in Greenbrae, Calif., encourages going shoeless, and a gong is used to assemble the 40-plus employees to meetings. A genuine Zen master is part of the ZoZa team, and Zen messages are sewn inside ZoZa's clothing. Unique stuff to be sure. But achieving profitability in 12 months? Now, that might be the most unique thing of all.

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