

# Good research paper on factors for failure

[Business](#), [Company](#)



[Assignment Number]

[Section Number]

## **Introduction**

The Internet Bubble, also called the “ dot-com boom” was created by Tim Berners-Lee in 1993. Historically, it was a speculative bubble, which means that people reached conclusions about its continued profitability that were not based on facts. The bubble covered a period from 1997-2000 and reached its ultimate climax on March 10, 2000 with NASDAQ stock trading reaching an unprecedented high of 5, 408. 60 in one day before the close of trading. That day stock markets in the industrialized countries saw the prices of their stocks rise briskly both in the Internet Segment and interrelated areas of activity. Although that day the rise was a sudden increase and break cycle, the Internet boom is usually referred to as the stable and continual expansion and development of the World Wide Web. This era was prominent for the opening and in many instances stunning closure of many Internets based companies commonly known as “ dot-coms”. Companies simply added the title “ e” which increased the value of their stocks .

One of the major reasons for the bursting of the bubble was the general assumption that Internet companies would continue to generate profits because the use of the web was increasing every day. This led to individual speculating in stocks because of the large amounts of available capital. All these factors projected environments in which investors willingly ignored conventional investment parameters and safety measures such as the P/E ratio in favor of the overconfidence in technological progressions. The bubble

collapsed during 1999-2001 in which some large companies were completely wiped out while many others lost a large portion of their venture capitalization, but still remained steady and lucrative such as Cisco whose stock prices were reduced by as much as 86%. Others, such as Amazon. com whose stock crashed from \$07 from \$107 per share, recovered slowly and a decade later its stocks rose to unprecedented heights of \$400 per share

### **Some other companies that survived and in fact prospered from the bubble are:**

E-Bay went public and its share prices were traded at a high price of \$18/= at the opening bell and went on to be traded for \$53/= per share. The reason was that E-bay had a sound foundation of selling and its continued expansion into areas that it was not doing business in before. This proved very successful for the company whose revenue topped \$9 billion. Priceline. com, a travel related website survived and made good when its shares jumped from \$16/= to 86/= and then fell to less than \$10/= over the next several years. Today its shares trade at \$500/= per share. “ Shutter-fly” a publishing service also survived and prospered. Today its shares are valued at above \$60/= per share. “ Coupons. com” a private company trading in coupons was among one of the few companies that did not crash with the bubble. The company is currently valued at billion Well known companies that crashed in the internet bubble were: 360HipHop, AmyCy. com, Boo. com, Broadband Sports, Cyberial Outpost, Cyber Rebate, Digi-Scents, E-Loft. com. Flooz. com, Excite@Home, Kozmo. com, theGlobe. com. Kibu. com, Psuedo. com, Yadaayada. com and Zap. com . The use of the Internet is growing daily and in less than two decades it has changed the lives of people in a way that was

not thought possible. Every characteristic of current life is affected by the Internet whether it is shopping, watching news or entertainment. The net has altered the way business has evolved. Established businesses are still making millions in profits from the Internet, and will continue to do so in the future unless there is another bursting of the bubble. The bubble was created by entrepreneur's unrealistic expectations of the potential of the net, and unless people are careful there might a re-occurrence of the bursting of the bubble. One very obvious factor in the failure was that many analysts concentrated on appearances that had very little to do with how businesses were generating revenues or their cash flows. One theory is that the bubble burst because of an obsession with the " network theory" which meant for many people that the value of a network grew proportionally as the sequences of " nodes" (computers housing the network) amplified and improved. Although in a way this did make sense, it ignored the most important means of evaluating the network: that was the capacity of the company for using the network to produce cash and make profits for its investors .

Besides ignoring the necessary metrics, analysts used excessively high figures in their models and formulas for the assessment of internet companies, which conveyed improbable and exaggeratedly positive evaluations. Although conformist analysts expressed doubts, their suggestions and endorsement were literally ignored because of the hype generated by the financial community for promoting internet stocks .

## **Understanding the Internet Bubble**

The creation and extensive use of the Internet generated an exhilarated approach towards e-commerce business and stimulated great optimism for the growth and development of online business. Because it was the going thing, many companies were launched because investors thought that any company operating online was going to be worth millions. But obviously, a lot of companies did not succeed and with the abundance of dot. com companies stocks were escalated beyond what they were actually worth. When the volume of business generated by dot. com failed to meet investor expectations, these companies crashed causing losses worth trillions of dollars for investors. In fact the Internet crash lead to the 2001 crash of the stock market with losses to investors of 4. 5 trillion. The stocks of internet companies were overvalued by 40% in nearly all cases as individuals and entrepreneurs all dreamed of becoming Internet millionaires. So caught up were most people with their dream of becoming millionaires, that they did not heed the warning signs of trouble that the market was about to crash .

## **What could have been done to stop this unsafe surge in valuation?**

One way to prevent this disaster was for investors to have followed the necessary financial precautions by looking at profits that the companies were generating before buying stock at astronomical prices. They should have also looked at past performances of the companies whose stock they were snapping up, and taken the advice of conservative analysts who predicted that this was too good to be true and the market could not absorb and utilize the amount of equity capital pouring in. The Administration for its

part could have informed the public about the real state of the economy and not project optimistic analysis that were not true. The economy was shrinking at 8.9 percent but government figures initially put it at 3.8 percent in 2008 when it was actually 6.2 percent. This provided false information to investors who paid caution to the winds and continued to buy up overpriced stock because the administration kept insisting that the economy was recovering and everything would be well .

## **Lessons Learnt from the Internet Bubble**

There is an old saying: “ that everything that glitters is not gold”. People should realize that there is a limit to the ascendancy of everything, and what goes up must come down. People ignored sound financial advice and indicators and assumed that since the use of the internet is increasing with every passing day, revenues too would increase proportionally. The increase of business does generate greater revenues, but not when everyone is jumping on the bandwagon and everyone is launching an internet company. Currently, there is another bubble being created which is the introduction and success of social media. Currently the four largest players in the field are Face-book, Twitter, Linked-in and Group-on. Again people are dazzled by the success of their companies and do not look closely at the figures that these companies post. Consider this, that last year Face-book stated with a lot of pride that its advertising revenues were around \$1.86 billion. This is an impressive figure, so nobody is really asking as to what the profits are in the \$1.86 billion revenues .

Face-book’s public stock may be valued at \$100 billion, but this evaluation is not supported by traditional financial measuring standards such as the “

dividend discount model” which categorically emphasizes that the value of any company should be assessed on its current and future net income. Although Twitter has more 200 million users, it has yet to find a cohesive way of making a profit and is only kept from crashing by contributions from its investors. The thing is that investors do not consider earnings when they evaluate Twitter, despite it being obvious that Twitter has no consequential revenue inflow. LinkedIn is in the same position as Twitter, but its stock is trading at around \$90 per share. Its profit margin in 2010 was a very modest 2 million dollars, but despite all this investors are expecting high returns in future despite indicators showing that this might not happen. In fact market rumors are that it might also be headed for a bubble like many other companies. In the same view the popularity of Group-on may be declining and its future revenues might not be so promising as investors anticipate, or in the way that its shares are being traded . Being popular does not mean that the companies are making or will make profits. Investors should carefully study all financial indicators before putting their money into internet ventures. Although these stocks will do well in the short term, their long term future profitability may not be that optimistic because for long term viability, stocks need strong revenue sources to be of continued interest to investors.

## **Conclusion**

Investors should follow some sound financial advice and never invest in any company in the hopes of future revenues or performance unless it has a track record of real numbers and at least a little expectation for future improvement. Individuals and entrepreneurs should keep in mind that the

first Internet Bubble cost trillions, making the same mistake is the last thing that they should do. It is like giving away money which will never be recovered.

## References

- B. M., & Nagel, S. (2004). Hedge Funds and the Technology Bubble. *The Journal of Finance*, 59(5), 2013–2040.
- Bias, R. G., & Mayhew, D. J. (2005). *Cost-justifying Usability: An Update for an Internet Age*. San Francisco: Morgan Kaufmann.
- Hawkins, R. (2004). Looking beyond the dot com bubble: exploring the form and function of business models in the electronic marketplace. *Springer Link*, 65-81 .
- Henning, M. (2006, June). The Rise and Fall of CORBA. *Queue - Component Technologies*, 4(5), pp. 28-34.
- Koller, T., Goedhart, M., & Wessels, D. (2010). *Valuation: Measuring and Managing the Value of Companies*. New Jersey: John w.
- Koller, T., Goedhart, M., & Wessels, D. (2010). *Valuation: Measuring and Managing the Value of Companies*. New Jersey: John Wiley and Sone.
- Malkiel, B. G. (2003). The Efficient Market Hypothesis and Its Critics. *American Economic Association*, 17(1), 59-82.
- Ofek, E., & Richardson, M. (2003). DotCom Mania: The Rise and Fall of Internet Stock Prices. *The Journal of Finance*, 58(3), 1113–1138.
- Rovenpor, J. (2003). Explaining the E-Commerce Shakeout: Why Did So Many Internet-Based Businesses Fail. *E Service Journal*, 3(1), 53-76.
- Watkins, M. D., & Bazerman, M. H. (2010, December 19). Predictable Surprises:. *Harvard Business Review*, pp. 5-12.



Winston, B. (1998). Media Technology and Society: A History : from the Telegraph to the Internet. New York: Routledge Publishers.