



THE CONFERENCE BOARD



# Executive *action* series

No. 242 July 2007

## Crafting a Strategy for Virtual Worlds: Eight Questions to Ask

by Edward M. Roche

Virtual worlds are emerging fast on the business landscape, but few companies have developed a strategy to deal with them. Membership is now in the millions, and many of the participants are probably your customers, not to mention, your employees. So how can you take advantage of this new technology?

### What Is a Virtual World?

A Virtual World is a 3-D Internet-based simulated social networking community usually modeled after the “real” world with buildings, roads, meeting rooms, bars, advertising billboards, and so on. Generally, many users participate at any one time with the interaction being immediate—that is taking place in “real time.” The world continues to exist whether individual users are logged in, and it usually encourages the formation of social groups. Although virtual worlds appear to mimic the real world, this is an illusion. Behind the scenes, a set of software programs determine the options available: what transactions are allowed, acceptable codes of behavior, or what types of corporate information can be imported or exported. While some virtual worlds are based on real-life communities, some are based on fantasy and may resemble medieval kingdoms, complete with dragons. For the business community, choosing the right virtual world to use is a crucial decision.

### The Need for a Corporate Strategy

Virtual worlds are “immersive environments” in which it is possible to re-construct a “virtual” version of reality. Although there are hundreds of virtual worlds, the ones in the press most often [at least in North America] are Second Life (<http://SecondLife.com>); World of Warcraft (<http://WorldofWarcraft.com>); Kaneva (<http://kaneva.com>); and There ([there.com](http://there.com)). Some virtual worlds specialize in providing corporate workforce development for business skills, behavior change and strategy execution. One fast-growing leader is QuestG (<http://www.QuestG.com>). Any of these is a good place to start learning about these new places.

While there are many business uses not yet exploited, a few examples of what virtual worlds enable a company to do include:

- *Provide a Meeting Place.* Build a 3-D immersive environment that can be used by customers, your business partners, and by your own employees.
- *Engage in v-Commerce.* Buy and sell goods and services.
- *Use Advertising and Product Placement.* Rent or build billboards and use other “in-world” channels to advertise your products; place your products in high-volume parts of a virtual world where they will be exposed to a deluge of “traffic” by visitors.
- *Build Organizational Experience.* Single and multiplayer worlds are designed to be explored and interacted with. They produce numerous critical decision points with an emotional connection that carries forward into the real world. This way, you can learn from mistakes and failures in a virtual risk-free place, and then apply that experience to real life.

Leading companies including Cisco, IBM, and Dell already have a substantial presence in Second Life. We would expect that from IT companies. However, retailers such as Circuit City and Sears also have a presence, and information services providers such as Reuters have built large installations that offer a menu of financial data, including videos of up-to-the-minute news clippings. Many others are following.

## The Problem

It is a fact of life, however, that in many quarters, virtual worlds are met with skepticism. Some managers are stuck. They assume that since the underlying technologies for virtual worlds come from video games, there could not possibly be any relevance for their business. This class of managers—the modern-day Luddites—are the type generally resistant to any change.

Other managers are confirmed nay-sayers—the negative types that always chip away at any innovative idea and try their best to make up reasons why it won’t work. They may point to “technical problems,” such as the occasional poor response time or “poor graphics” or “people will never use it” or the all-time favorite bug-a-boo: “security.”

## Why do people say “Immersive”?

The term is used to describe the psychological reaction of most users when they begin to use virtual worlds. At first they feel detached from the simulation, but after a very short period of time, begin to experience the virtual world as though it were reality, e.g., they become “immersed” in the experience.

This type of manager sees only the present, and fails to comprehend how virtual world technologies are rapidly advancing. While there are security concerns because of the newness of virtual worlds, other companies are dealing with them, and security should not be allowed to become a “show-stopper” for a new entrant.

Other managers simply may not have heard of virtual worlds. These types do not read the newspapers, follow the trade press, or watch major news channels, such as CNN, which has regularly been airing specials on virtual worlds and their applications for business.

So the point is this: Whether or not your company decides to “go into” virtual worlds, it is useful to review a few key questions that all companies should ask as they weigh their strategy and make a decision.

## Question 1: What Is Our Entry Strategy?

Strategies do not magically arise from the ether—they are born of necessity; they are caused by something. There are at least three approaches companies are using today.

*First Mover Advantage.* Some companies see virtual worlds as a new frontier, similar to the Internet a decade ago. Their idea is that by aggressively moving into this space, they will be able to attain a “first mover advantage” similar to what Amazon.com did in the book-selling business or what eBay did with online auctions. The thinking is that once a dominant player is in place, it is difficult for others to dislodge them.

*Competitive Necessity.* This term was coined by Eric Clemons, a professor at the University of Pennsylvania’s Wharton School. It boils down to this: “If my competitors are going in, then we are going in too!”

## Frequently Used Terms in a Virtual World

**Avatar** – A representation of self that is a 3-D character inside a virtual world. Most persons choose avatars that are “persons,” but some choose to be animals, wizards, hosts, and so on. Companies building a virtual world presence usually have a well-dressed “avatar” present to answer questions of any visitor.

**Group** – In some virtual worlds, avatars can join special “groups” associated with specific locations or types of activities. Some groups have controlled membership. For companies, it may be useful to identify any of its employees as being in the same group so they can recognize each other. Groups can also be used to provide a special designation to your customers, e.g., “X-Company VIP.”

**Sim** – Abbreviation for “simulation.” Used as a slang term for a virtual world, or a special partitioned portion of a virtual world. “Visit my sim.”

**Role Playing** – In some virtual worlds, the “inhabitants” are able to create special areas that are governed by their own set of rules. For example, in one popular “sim,” there are “masters” and “slaves,” and persons visiting there must act accordingly. There is a significant amount of sociological, political, and psychological research going into understanding role-playing “sims.”

**Scripting Language** – In some virtual worlds, the “scripting language” is the set of software programs that allow users to do things inside the virtual world.

Examples include: creating buildings or translating external data into 3-D “objects” inside the virtual world.

**Social Encoding** – A theoretical term that refers to the programmed software rules governing the virtual world. The “social encoding” determines what avatars can [and cannot] do. Social encoding rules also allow groups to create their own rules. These are sometimes used in special “role-playing” parts of a virtual world.

**Streaming** – A technical term that refers to the broadcast into a virtual world of external information sources, or “streams.” An example is the Reuters installation inside Second Life that “streams” in live video from Reuters, and also provides up-to-the-minute financial information.

**v-Commerce** – Refers to Internet-based e-commerce that is initiated through virtual worlds. Examples include: buying and selling of virtual items inside a virtual world, or using a “click through” approach that will launch a browser to your corporate website if an avatar “touches” an information sign in your company’s installation inside a virtual world.

**VoIP** – Voice over the Internet Protocol. A technical telecommunications standard that allows voice (telephone) traffic over the Internet. Many virtual worlds are adding VoIP so that avatars can “speak” with each other.

Companies constantly monitor each other’s moves in the market, and try, by all means, to block their competitors from taking over a new channel, or getting extra “mindshare” in the marketplace of ideas.

*R&D Experimentation.* Finally, judging by their sometimes half-hearted presence, some companies are using virtual worlds for experimentation. These companies are engaged in trying out new approaches, and taking a “wait and see” attitude. But all the time, they are keeping an eye on their competitors—and probably getting tax breaks by writing off the entire exercise under the R&D budget.

*Global Operations.* Many firms with 24/7 global processes and management are searching for more and better ways to cheat the clock and break down internal barriers. Early results from virtual environments point to higher degrees of collaboration and openness. Only time will tell if this is a fundamental shift or just a workforce reaction to a very engaging technology.

*The key issue is whether you have completed an overall competitive analysis that focuses on what your rivals are up to.*

## Question 2: What Is the Corporate Purpose?

Assuming there is a “yes” on entry, then you must understand the key purpose, a.k.a. “vision” for your “v-strategy.” That is, if your entry strategy is the “Why,” the corporate purpose is the “What.”

Corporations currently are exploring a variety of “visions” for how they will exploit this new technology. Listed roughly in the order of increasing maturity, here are some of the more popular:

*“Showcase.”* The early implementations of corporate presence in virtual worlds appear to be mostly for the purpose of “staking out a claim” or establishing a “showcase” to put everyone on notice that the corporation is “in there.” The showcase approach involves projecting a basic collection of information to the customer. Examples include: (a) use of the corporate logo, (b) providing graphics such as large images of your products, (c) sometimes providing short looping videos that can be viewed by visitors.

*Advertising.* The next step involves development of a more aggressive plan to promote the corporate image, and explain your products and services. In addition to providing information on one’s own “island,” you may take out advertising in other parts of the virtual world and even sprinkle about “portals” that will “teleport” an interested consumer to your corporate location. Companies frequently provide “hot links” that when clicked by the consumer will launch a web browser directed at the corporate website, but independent of the virtual world application.

*v-Commerce.* There is a great amount of buying and selling. For the most part, established companies have used the “click-through” approach described earlier to hook consumers into a visit to their website, hopefully to make a purchase. There exists, however, a large class of companies offering their services completely within virtual

worlds. These include design and systems implementation companies that you might contract with in order to build out your virtual corporate presence. Please note that during the early stages of any new technology, such as “customized” services tend to be considerably more expensive than they will be in a year or so.

*Customer Service.* In the same way that v-commerce might be developed, some companies are using virtual worlds to provide their own customers with information. This is a more mature application of virtual worlds, and is nascent. For the time being, there are some issues: It is problematic to identify exactly who your customers are; and you need to set up some type of registration system to keep track of your virtual customers, or should we say to keep track of virtual representations of your real customers.

*Customer Community Building.* There is some experimentation with bundling together customers to provide them with ways to exchange information. This is roughly analogous to regular monitoring of chat boards or Internet mailing lists to keep track of what customers are saying. Eventually, it might be possible to provide special services to customers, perhaps in exchange for their participation in the “community.” For the time being, however, most of this still is on the drawing board. Some of the major applications are (a) the use of virtual worlds for “product testing,” and (b) development of better collection mechanisms for customer information, including the use of “focus groups” and other, perhaps, automated methods to collect psycho-graphic information.

*Collaboration.* As virtual worlds mature, we will see more focus on collaboration—inside the company, between the company and its customers, and between the company and its business partners. Companies such as IBM already are experimenting and perfecting these applications, but for more or less everyone else who is not an IT company, collaboration should be considered as a strategic direction rather than as an immediate option.

### Question 3: Do We Plan to Offer v-Products?

Virtual worlds offer an opportunity for your company to re-think completely its product and service offerings. But a change of perspective is required.

Are you thinking of using virtual worlds to promote and sell your currently existing products? Or are you thinking of completely new products and services that might be developed?

For the time being, assume it is easy to think through approaches to use virtual worlds as an alternative channel to promote or sell your current products.

If that is a given, then focus on what type of new “v-Products” are being offered today. Here are some that seem to be thriving:

*Systems Design and Programming.* Any company wishing to develop a presence in virtual worlds can choose from a variety of consulting and systems engineering companies hawking a range of services. These include: (a) strategy formulation, (b) designing your virtual world, (c) actually “building” your company presence inside the virtual world, and (d) integrating your “legacy” information systems with the new virtual world environment. These companies range from giant “turn-key” providers to unusually innovative mom and pop shops that provide programming or design and building services.

*Creation and Sale of “Objects.”* There is currently a flurry of activity mostly by small companies building “in-world” objects that are bought and sold. Examples include: special clothing, special effects that might be used by one’s avatar (your avatar is the visual “handle” or display appearance you use to represent yourself in a virtual world). On Worlds Chat and similar sites, you can be a unicorn, a bluebird, or any kind of creature or object that seems right, and even include the creation of special tools, particularly weapons. Although no one has taken the plunge, it is conceivable that brand name clothiers could move into this space.

*Booming Entertainment Market.* A proliferation of entertainment places are springing up in virtual worlds. For the time being, very few are branded. The virtual “Studio 54” is an exception. But this will change. These places most often are either “theme parks” a.k.a. “role playing” locations, or discotheques. Although popular, it’s not clear if any represent a substantial revenue opportunity today. It seems reasonable for the entertainment and hospitality industry to keep an eye on this area.

*Rental Property.* Believe it or not, fortunes have been made in the rental market. It operates more or less like the real market: someone purchases land, improves it, then rents it out. Although much of this activity now is entertainment or leisure related, many companies are launching “meeting spaces” or “collaboration sites” that can be used by virtual teams to coordinate their work. With such a low cost of entry, it’s difficult to see a revenue source here in the absence of a branded and established player, or possibly through a hybrid real-virtual service offering.

The key to any v-product launch is timing. Your company can launch v-products as an entry strategy, as a series of short-term activities, or as part of a long-term product positioning campaign. For the time being, the major companies involved with virtual worlds still are treating them as experimental platforms or as a “Darwinian Stage” for product testing.

### Question 4: Who Is in Charge?

There is unlikely to be a “Virtual Worlds Department” or “Virtual Worlds Vice President” in your company. The Reuters news service has a “Second Life Bureau Chief,” but that is an exception.

Since companies don’t have this function in place, it will need to be invented. But who should take the lead? Here are some solutions and approaches being tried:

*Corporate Committee.* Some companies are forming multi-disciplinary or inter-departmental committees charged with developing a virtual worlds strategy.

*Internet Portal Team.* You may wish to assign the virtual worlds program to the same team already in place and running your corporate website. For many companies this may be a reasonable and quick solution. Virtual worlds are “different,” but not so different that these standing teams cannot take them in.

*Sales and Marketing.* Since much of your virtual world strategy eventually will revolve around selling your products and services, the sales group might be a natural fit, or the marketing team. They can integrate your effort in with other marketing and advertising efforts. Going this route, however, may be more difficult with existing personnel, so an option to consider is allocating a budget to hire a sales and marketing specialist with virtual worlds experience and have him/her report to the senior vice president.

*Strategy.* Some companies maintain a robust strategy organization. This might be a good “home” for your virtual world’s effort until the experimentation and research period is completed.

In general, either the inter-department committee approach or the appointment of a specific function that has “accountability” for the effort will work. It’s only a question of corporate culture and how it is currently organized for assimilating innovation.

## Question 5: Which Virtual Worlds Should Be Used?

Companies can choose between hundreds or even thousands of virtual worlds. But which one is best?

Should you pick one such as Second Life that is popular and is in the news frequently? Should you pick multiple virtual worlds, develop in each of them, and see which one holds out for the long haul? Should you find a virtual world that is specialized—one that is frequented by a specific type of customer you are interested in attracting? Here are a few considerations for picking the virtual world right for your company:

*Understand the Psycho-Graphics of Your Customer.* Many virtual worlds are specialized. Some are visited most frequently by pre-teens, others by “gamers,” still others according to nationality, and so on. Consider this scenario: If you could approach all of the “Level 70” players in World of Warcraft (a leading virtual world), would they be a good prospect to sell a pair of hiking boots? A new consumer electronics gadget? Life insurance? One of your first tasks should be, therefore, to match the age and demographics of your intended audience against virtual worlds they consider the dominant players.

*A Portfolio Approach.* You might develop in several virtual worlds at once. Some might be specialized “niche” worlds; others might be “general purpose” worlds that attract a wide variety of consumers. Much like the insurance or the junk bond markets, starting with a diversified portfolio will lower your risk of ending up with a lemon that either fades away or fails to support your objectives.

*Understand the “Social Encoding” of Each Virtual World.* This may sound like a mouth-full, but it means you need to assess how each virtual world operates—its “rules.” Some are more flexible than others; some have currency, others do not. It is critical, therefore, to make sure that for each virtual world you are evaluating, you review point-by-point the “social encoding” to make sure that you can do what you wish, and that your customers can as well. In a virtual world, nothing is random—unless it is programmed to be!

*Public or Private.* Another dimension of virtual worlds to consider is their public accessibility. For customer market applications, a public world such as Second Life makes sense. For internal applications or applications focused on workforce experience building, a private virtual world, an internally hosted world, or even a very specialized single-player environment that directs avatars to a specific objective may be most appropriate.

## Question 6: How Much Will It Cost?

There is, as yet, no clear set of figures or benchmarks for budgeting for creation of your virtual world. Some companies are spending much more than others. It's too early in the game for determining such budgets. These are the major areas of cost that you can expect to lay out for your virtual worlds strategy:

*Design and Requirements Determination.* For the first foray, a company will probably need to hire a consultant to work with it to create the concept for its virtual world presence, and to help specify the design and the functional requirements, e.g., what it is supposed to do for the company. There are many suitable services on the market, many provided by “new-name” firms. With the exception of IBM, at this point, the large “brand name” consultants still are sluggish followers. Small and nimble may be better at this time.

*Building and Maintenance.* After the design is completed, you will need to invest in actually building your virtual world. Don't expect this process to be completed rapidly—or even to be completed at all! In practice, companies tend to continually change, modify, and elaborate their virtual world presence. Consequently, you should expect to have a “standing order” with the builders to continually “refresh” your virtual presence, as needed. One quote from an avatar: “Each time I come back here, they've added something else interesting,” e.g., so I keep returning.

*Hosting.* Your company will either need to rent space in someone else's virtual world, or build its own. The rental space and hosting services provided by virtual worlds providers is their major source of revenue. You will need to estimate a continual ongoing cost, and, if possible, build in clauses to your contract that will prevent price hikes. In the long term, you will be able to build and host your own world, but in a practical sense, that is years away.

*Systems Integration.* You must budget in the cost of integrating your production information systems with your virtual world presence. Because the methods of doing this only now are being worked out, it is very difficult to estimate these costs up front. A rule of thumb is to take your building and maintenance costs, double it, then give 65 percent to systems integration.

## Question 7: What Is Our Revenue Model?

For most, understanding how to recoup their investment is difficult, at least for now. Much depends on the mode of entry your company chooses. These are a few of the ways companies are justifying their virtual worlds budget:

*Advertising.* If the project is viewed as a means of getting a good word about your products and services out into the marketplace, then the cost becomes only an extension of advertising and can be lumped together with Internet advertising in general.

*Sales and Marketing.* If you are selling products and services through virtual worlds, then the costs can be considered much the same way you would analyze any distribution channel for your goods.

*Customer and Market Research.* If you are able to use your virtual world as a means of product testing or for doing market research, then the investment simply becomes a type of business expense similar to any market research. For some sectors, this budget understandably can be quite high. Pharmaceuticals is one example of a “high research costs” sector.

*Training.* If you adopt a virtual world approach for internal training and education, then it may belong in the human resources budget; however, virtual worlds inherently bring about collaboration and the crossing of traditional functional and business unit boundaries. Therefore, it may best reside in a general manager's or sales manager's budget and be coupled with an eye to business redesign and management process changes.

*New Product Line and Revenues.* If you are selling products and services through virtual worlds, then the financial model is simply one of cost to manufacture and deliver compared to revenues. In this instance, the virtual world becomes simply a specific factor in manufacturing and provisioning costs.

*R&D Only.* Write it off on your R&D budget. In some sectors, this can lead to a considerable tax advantage.

## Question 8: Is IT Up to the Job?

The IT function in most companies is one of the most under-rated and under-appreciated groups. Apart from fighting a 24/7 battle against information terrorism, virus attacks, and various hacker clubs around the world while dealing with the next operating system release, the IT group manages for the most part to keep millions of transactions per second coursing through the electronic veins of an enterprise.

Unfortunately, continual nagging from users and extremely difficult technical challenges tend to make IT resistant to change. Often, a new project is considered little more than another headache. But, ultimately, IT can be counted on to get the job done. Just budget the money and get out of the way.

Here are a few of the key applications challenges and other key decisions that IT teams will be forced to cope with:

**Lack of Personnel.** It is extremely unlikely your IT organization has personnel suitably trained to design, develop and build virtual worlds. Constant budget-squeezing probably has seen to that. Also, most virtual worlds run on open source operating systems such as Linux, while most companies are leather-strapped to the table with Microsoft and can't get out. Consequently, your IT will at first need to outsource this work to others. For the most part, outsourcing is a standard operating procedure, well understood by IT, and there is nothing inherently different about a virtual worlds project. No problem here.

**Security.** There are security issues in any IT project. The newness of virtual worlds technology perhaps enhances the risk. Nevertheless, every IT organization employs a set of accepted risk-minimization strategies. The most important maximum is: "Security must be built into the systems development process"—from the very beginning. Particularly in the earlier stages, security should not be allowed to become a "show-stopper." Leave this to IT.

**Linkages to Production Databases.** This is a more serious problem. If your virtual world is going to point the customers towards product information, or perhaps account information, then some type of mechanism must be designed to "pipe" the information from your corporate databases into the virtual world where it can be viewed and interacted with. This is a formidable problem for IT. There is an absence of reliable technologies and proven approaches to accomplish this. One result is that until these methods and tools are more adequately developed, it will be problematic to move your company up the ladder enabling higher levels of service. This is the real technology headache, invisible to end-users. Just make sure you budget enough and resist the temptation to fall into the trap of subjecting it to some silly "Return on Investment" analysis—at least until you leave the experimental stage (a few years down the road).

**Customer Information.** Eventually, the IT function will be asked to link together live customer information with events in the virtual world. This is a headache, but one far enough into the future not to worry about now.

### Learning the "Learning Curve"

In the end, the best way to think about an entry strategy for virtual worlds is with the learning curve paradigm. Your company will be going through its own learning curve, and so will your competitors, as well as other companies in other sectors and of course the providers of virtual worlds themselves.

How to adjust to this new reality? There is a straightforward answer: Develop your questions, monitor what your competitors are doing, continually assess your options, and set up a standing committee internally to stay on top of this issue.

Move fast enough to benefit your company, but not so fast as to rush ahead and get burned.

## The Conference Board and Virtual Worlds

The Conference Board will be launching a series of Research Working Groups on Doing Business in a Virtual World during winter 2007–2008. The following questions will be addressed:

1. What are the demographic (psycho-graphic) groups that may be addressed through virtual worlds when virtual worlds are used as a corporate communications channel?
2. What are their competitors doing? That is, what type of communications are they using and for what purpose?
3. Are there examples of what to avoid or what to encourage when crafting a corporate communications strategy for virtual worlds?
4. What are the key levers that can be used in virtual worlds and how are they likely to change within the next five to seven years?
5. What types of products and services are available for the company that can be used to implement the strategy?

You may wish to nominate one or more employees to participate and report back to corporate. For additional information, please contact Sophia Muirhead at 212 339 0373 or [sophia.muirhead@conference-board.org](mailto:sophia.muirhead@conference-board.org).

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### Barraclough Virtual World Wiki

Barraclough has set up a Wiki where business persons and researchers from around the world can exchange ideas about virtual worlds. Members of The Conference Board are invited to access this information and participate. The web address is: <http://www.barracloughltd.com/mediawiki>.