

Betfair.com: Five Technology Forces Revolutionize Worldwide Wagering

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The online betting exchange Betfair.com has not only revolutionized sports and racing wagering, it has won export and innovation awards and had its founder listed as one of the world's major innovators in Time magazine. It has also however attracted the attention of sports bodies, major competitors and governments, who seem uncertain about how to deal with this revolutionary player, as well as customers globally, who are attracted by the far superior value proposition the firm offers. In this paper we describe the Betfair business model, and use five technological forces to explain its strategic success. These forces are generalizable, and can be used to explore the impact of technology on any industry.

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Introduction

The City of London has been a center for the exchange of information about bonds and shares (The London Stock Exchange), commodities (The London Metal Exchange), and the financial consequences of events (Lloyds) for centuries. The earliest trading occurred at the end of the 17th century (Bernstein, 1996). With the beginning of the 21st century, a new financial exchange has emerged in London.

Betfair is a financial exchange for knowledge and opinions on sporting, political and other events. All of these exchanges operate by assembling a large numbers of buyers and sellers to trade the value of their information, be it based on fact, opinion, or wishful thinking (e.g., Laffey, 2005). Our focus is on the newest of these exchanges.

Players wishing to have a wager on a football game, or a flutter on a horse race, or to back up their opinions on a political election or the outcome of the Oscars, have until recently had few alternatives. In a majority of European countries, Canada, and most states in the USA their only option would have been to place a bet on a pari-mutuel or totalizator system, while in countries such as the United Kingdom and Australia, and in U.S. States such as Nevada, they would also have access to licensed bookmakers. Both of these systems place the player at a significant disadvantage, not least of which is the fact that the "rake-off" or house percentage is considerable. This means that winners get paid well below the "true" odds against their choice. Furthermore, neither of the two systems allows a player to pick a "loser" – the player can only stake on a winning outcome. In simple terms a player cannot back a team to lose – they can only back the other team to win or on a draw. A specific disadvantage of pari-mutuel systems is that subsequent weight of money for a player's choice will reduce the payoff, so that there is no opportunity to exercise any skill in the timing of a bet. Both systems profit not from the losers (as most inexpert gamblers believe) but from winners,

by paying them out at less than true odds. In the case of pari-mutuels the house percentage is around 20%, and even the most generous bookmakers make books that have an edge of around 14% in their favor.

Andrew Black's Bright Idea

In the late 1990s, Andrew Black was a software programmer and professional gambler. He concentrated mainly on playing bridge and betting on horses. His software for odds calculations for soccer aided him in making an acceptable return. He was, however, dissatisfied with traditional bookmakers.

"By the time they [the bookmakers] build in their margins, you've got to be 20 percent smarter to make money. And if [you] make a mistake, [you] can't trade out of it. I thought, there's got to be a better way." (Time Magazine, 2004)

On a May evening in 1998, Alan Black gained the key insight for creating Betfair when he imagined creating an Internet betting exchange operating along similar lines to the U.S. stock exchange. He recalled,¹

"The big jump was realizing the numbers in the model didn't have to be a price. If you substituted these numbers for odds, it still worked." (Dey, 2005)

By 2004, Betfair was the world's largest betting exchange, with more than 50,000 people placing bets each week on the many events the website features. Elections, major horse races, golf tournaments, and soccer matches inevitably trade more than GBP 3 million at a time.

In this article we use the example of Betfair to illustrate the profound forces that technological change can have on industries and markets. We begin by showing how Betfair offers a significant advantage over the incumbent alternatives in betting markets. We describe how the Betfair system works, and how it offers advantages to players while at the same time providing significant financial benefits to its owners. Next, we introduce five "technological forces" and apply these to the Betfair case in a manner that can then be generalized to other industries and markets. We conclude by exploring issues of risk syndication and the market for opinions, and speculate on how Betfair can grow its business in the future.

Bookmakers and Totalizator Systems

Traditionally, gamblers on events have used a pari-mutuel totalizator system or a bookmaker to make a wager. Pari-mutuel systems (Figure 1) deduct a percentage of all bets (normally around 15 percent, but in many cases as high as 20%), and winners receive a ratio of the remaining pool to their stake. The totalizator can never lose – much like a lottery; it simply takes as its income a fixed percentage of

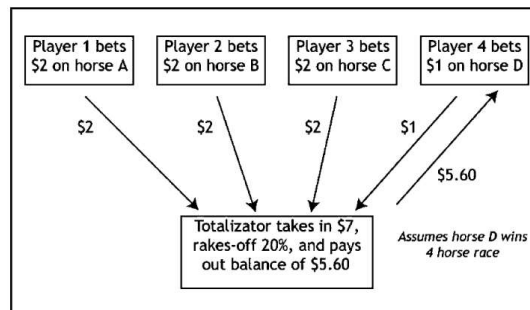


Figure 1 Totalizator System

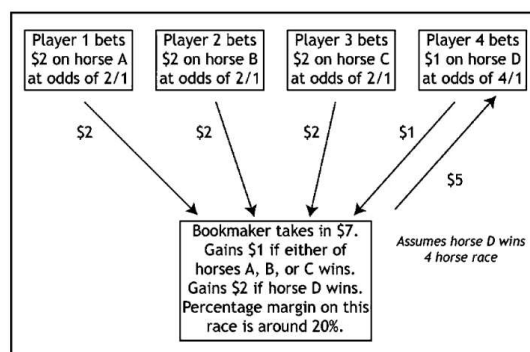


Figure 2 Bookmaker

all funds wagered. Players, however, have no idea in advance of the odds for their selection. Thus, it is difficult for them to use any kind of betting system to minimize their risk or gain a higher return.

When placing a bet with a bookmaker (see Figure 2), the better is quoted fixed odds that will not be changed by the subsequent bets on their or other choices, as in the totalizator case. To cover their risks, bookmakers offer the gambler odds shorter than the true probabilities in order to profit in the long run – typically around 14 percent of turnover although this will vary from event to event, market to market, and indeed, bookmaker to bookmaker. Bookmakers do take risks, but attempt to manage these. Unlike totalizator systems, bookmakers lose on some events when they misjudge the probabilities and offer over-generous odds or when some of the potential outcomes they have anticipated do not attract sufficient bets to cover exposures. Because of their financial interest in the outcome of an event, bookmakers have sometimes been accused of fixing races, bribing jockeys, and other actions to change the course of an event. Such actions are not in the ordinary gambler's best interests.

While the models for the totalizator and bookmaker differ in many ways, their basic premise is the same: Use the money taken from losing bets to pay winning ones, and allow for a percentage "rake-off" before doing so.

Betfair

Launched in 2000, Betfair turned over GBP 1.5 billion² in 2002, and won a Queen's Award for Innovation in 2003. In mid-June 2004, Betfair had a larger turnover on the Kentucky Derby than the totalizator on the track at Churchill Downs, the race venue. Betfair attracts gamblers because it provides an opportunity to bet on a huge range of sporting, social and political events. The company also offers a range of financial bets on most of the world's major markets, such as whether the FTSE or the Dow Jones index will rise or fall.

The Betfair System

Betfair has no interest in the outcome of any event it makes available to gamblers. It simply provides a market for opinions and for trades to take place. It requires players to make and/or take fixed odds and all income is derived from a small percentage commission (ranging between 2 and 5 percent, depending on a player's turnover) on a player's net winnings on an event (see Figure 3). In general terms, the greater an event's turnover, the more revenue and profit Betfair generates, although Betfair's income is strictly a function of the total net winnings on an event, not turnover.³ Why this is important will be referred to later. It is successful when it can assemble large numbers of gamblers – and provide a market for them to interact with each other.

For events, Betfair shows the possible outcomes, and columns entitled "Bet" and "Lay." The "Bet" column shows the odds available to a player who wants to back an outcome and how much money a player can place on those odds. Odds are inevitably made and taken, and the margins are minuscule, much

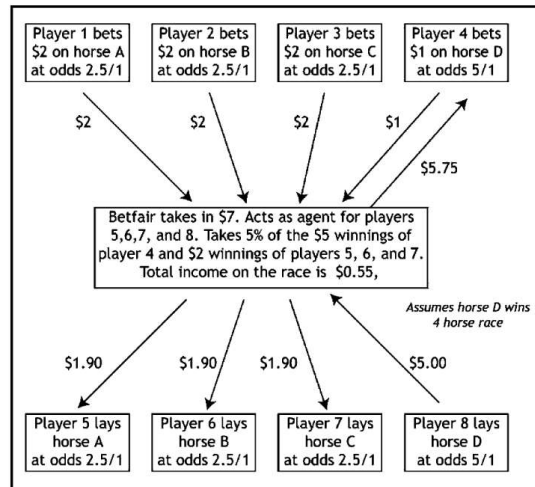


Figure 3 Betfair

smaller than those of even the most generous bookmaker. For an example see the screen capture below (Figure 4) from Betfair for betting on the 2005 SuperBowl.

Customers can place funds with Betfair through a variety of means (e.g., credit card, bank transfers), and Betfair maintains a record of each person's account balance and transactions. As well as reducing the balance every time a customer makes a bet (e.g., backs a horse), it also reduces the on-reserve every time a customer lays a bet (i.e., incurs a potential liability by laying an outcome at odds). Net winnings are credited to the appropriate account. Customers with a positive balance can withdraw at any time and request to have all or part of their positive balance re-credited to their credit cards or bank accounts.

NFL Season 04/05 - SuperBowl Winner							Refresh
View P&L [Settings] ?		101%		99.5%			
Total selections:(4)	USD	Back		Lay			
New England Patriots	2.72 \$42	2.74 \$17	2.76 \$140	2.78 \$1025	2.8 \$1291	2.82 \$1038	
Pittsburgh Steelers	3.45 \$50	3.5 \$4219	3.55 \$330	3.6 \$296	3.65 \$1060	3.7 \$840	
Philadelphia Eagles	3.95 \$8	4 \$4623	4.1 \$1161	4.2 \$2007	4.3 \$706	4.4 \$196	
Atlanta Falcons	7.8 \$5	8 \$2096	8.2 \$617	8.4 \$159	8.6 \$187	8.8 \$13	

Figure 4 SuperBowl (Jan 17, 2005)

Betfair's Success

By the end of 2004, Betfair's turnover was in excess of GBP 50 million a week in matched bets, about 13 percent of the estimated USD 35 billion global annual online sports-betting industry (Time Magazine, 2004). Betfair had more than 300,000 registered customers in 85 countries, of which some 50,000 were regular punters betting every week. Major events could attract up to 12,000 wagers per minute. About 10 percent of its business was done via the phone, to cater for traditional gamblers who were not comfortable with the Internet. Furthermore, an independent study of 4,000 races in the United Kingdom published towards the end of 2004, reported that punters were about 10 percent better off dealing with Betfair compared to a bookmaker (Hannan, 2004). As well as English, players can trade in a number of languages, including German, Italian, Danish, Swedish, and Mandarin.

On an ordinary mid-week horse race in the UK, the website regularly matches bets exceeding GBP 400,000. On Australian and American races, the site averages around GBP 25,000 a race, and even in smaller centers such as South Africa (on which the site provides betting on races on a daily basis), the site averages around GBP 10,000 on a race.

For horse racing fans, Betfair has around the clock racing coverage, because of the differences in time zones. When racing in Europe and South Africa finishes for the day, horses are galloping in the U.S. (from coast to coast and usually at about 8 or 9 venues). About an hour after the last race in California, racing begins again on Australia's east coast, progresses west, and by the time the last race finishes in Western Australia, there is only an hour to wait before racing begins in Europe and South Africa again.

The Five Forces enabling Betfair's Success

Betfair represents a classic case of five technology-related forces, which when working in concert, cause radical change in industries and markets. These are:

1. Moore's Law, which means that ever more powerful, ever more affordable computing gives firm and customers alike access to enormous processing power.
2. Metcalfe's Law of Networks, which means that as the number of customers using Betfair multiplies, so the utility to each customer increases, by creating greater liquidity in the market, and hence greater efficiency.
3. The Internet as a communication medium, and Betfair's technology, reduces the transaction costs for all concerned, especially the customers.
4. Innovations such as Betfair are difficult for both governments and incumbents to regulate and control in conventional ways (the Flock of Birds phenomenon).
5. Innovations as radical as Betfair very rarely originate within an industry's traditional players (the Fish tank phenomenon).

Betfair enables an intriguing examination and extension of these forces. Observers of industries as diverse as music (e.g., Napster) and telecommunications (e.g., Skype) will immediately recognize the generalizable parallels between these innovations and Betfair, and the applicability of the five forces.

Moore's Law

In 1965, an engineer at Fairchild Semiconductor named Gordon Moore noted that the number of transistors on a computer chip doubled every 18 to 24 months. A corollary to "Moore's Law," as that observation came to be known, is that the speed of microprocessors, at a constant cost, also doubles every 18 to 24 months. Moore's Law has held up for more than 30 years. It worked in 1969 when Moore's start-up, Intel Corporation, put its first processor chip - the 4-bit, 104-KHz 4004 - into a Japanese calculator. And it still works today.

Although observers have been saying for decades that exponential gains in chip performance would slow in a few years, experts today generally agree that Moore's Law will continue to govern the industry for another 15 years, at least. The implications of Moore's Law are that computing power becomes ever faster, ever cheaper. This not only means that just about everyone can therefore have affordable access to powerful computing, but that the power of computers can be built into devices other than computers themselves.

It would be fair to say that without the effects of Moore's Law, Betfair would not exist. On the one hand, just ten years ago, the computing power required to process, manage and store the millions of rapid transactions Betfair handles each day was simply unavailable.⁴ On the other, Betfair relies on the fact that its customers also have access to considerable computing power, in the form of affordable and easy to use laptop and desktop computers, and that these have access to the Internet. A generation ago, only pari-mutuels and the very largest book-making firms had access to computers, and the ordinary player had none. Moore's Law has made affordable, powerful computing accessible to all in the Betfair community.

Betfair is regarded by many as one of the most astute users of computing power in the world. For example, Gary Nugent, *iForce*⁵ Partner and Mid Market sales director at Sun Microsystems, regards Betfair

as one of the most technology-critical firms he has encountered:

"Technology is critical to the success of Betfair.com. It required a highly scalable infrastructure that could provide optimum customer security." (Sun System News, 2005)

Metcalfe's Law

Robert Metcalfe, founder of Novell, 3COM Corporation and the designer of the robust Ethernet protocol for computer networks observed that new technologies are valuable only if many people use them. Roughly, the usefulness, or utility of the network equals the square of the number of users, the function known as Metcalfe's Law. The more people who use software, a network such as the Internet or cellular phone system, a particular standard, a game, or even a language such as English, the more valuable it becomes and the more new users it will attract. This increases both its utility and the speed of its adoption by still more users.

Metcalfe's Law is a very real factor explaining Betfair's success. The fact that more than fifty thousand customers use the site to place and lay bets each day means that the likelihood of any individual player finding a match for what they want (assuming that what they are asking for is reasonable) is very high. This of course results in highly efficient and very liquid markets, which are to the advantage of all players. This is a phenomenon observed in other markets on the Internet, including term-life insurance (Brown and Goolsbee, 2002) and real estate (Levitt and Syverson, 2005).

Networks are important because they create short cuts. Anyone who is part of the network is by definition in contact with anyone else that is part of it, and can therefore bypass more traditional channels and structures (such as conventional bookmakers and totalizators in this case). As networks grow, their utility increases, so Metcalfe's Law tells us – this is true for those who are part of the network, and for those who then choose to join it. Neither traditional bookmakers nor totalizators enjoy the same network advantages as Betfair: Bookmakers only have access to players in their geographic vicinity or those with telephone access. Totalizators are on tracks only in some countries, where they will be affected by liquidity problems on quiet days, and even when they are not, they are restricted by local geography. Betfair faces none of these restrictions, and can enable the world to wager.

Coasian Economics

Nobel Prize winner in economics, Ronald Coase made a discovery about market behavior that he published in a 1937 article entitled "The Nature of

the Firm" (Coase, 1937). Coase introduced the notion of "transaction costs" – a set of inefficiencies in the market that add or should be added to the price of a good or service in order to measure the performance of the market relative to the non-market behavior in firms. They include the costs of learning, searching, contracting, monitoring and enforcing. The effect of communication technology on the size of firms in the past has been to make them larger. This has enabled multi-nationals such as General Motors, Sony and Unilever to operate as global enterprises, essentially managed from a head office in Detroit, Tokyo or London, or wherever. So large firms brought more activities within the firm (or the "hierarchy" in transaction cost terms), for it was cheaper to do this than to rely on the market.

In the age of the Internet these same communication capabilities are now in the hands of individuals, who can pass messages round the world at as low a cost as the biggest players – essentially, for free. The effect of the new communication technologies, accelerated by Moore's Law and Metcalfe's Law will be to reduce the costs of the hierarchy (Downes and Mui, 1998). But more especially, they will reduce the costs of the market itself. When contrasted with traditional bookmaking firms, Betfair is a fine example of the potential of low cost, networked computing to make markets more efficient by lowering transaction costs. Traditional bookmakers need to be well informed (studying horse racing and sporting events carefully) in order to make odds, and need to monitor market changes constantly in order to avoid being taken advantage of, or of being over-exposed. Betfair simply provides the platform for many individuals (theoretically, "firms of one") to do this for themselves. These individuals do not have to rent space or equipment, advertise, or employ staff. With a click of a mouse they can essentially either do what Ladbrokes or William Hill does – or, if the fancy takes them, play their fancies.

The Flock of Birds Phenomenon

A feature of recent communication technologies such as the Internet has been the fact that in many cases they do not "belong" to any one institution, nor does any particular authority control them. Some have referred to this as the "flock of birds phenomenon" (see for example The Economist, 1995). When one observes a flock of birds flying in formation, or fish schooling in a distinct pattern, one is tempted to speculate whether there is or could be a "bird in charge" or a "head fish". Zoologists will explain that flocking is a natural phenomenon and that there are indeed no "head" fishes or birds in charge – flocking is instinctive behavior. The network becomes the processor.

Humans have been conditioned to seek a controlling body or authority for most of the phenomena that we experience in life, for that is indeed how most modern

societies have been organized. The response to the questions, "Who's in charge?", "who controls this?", or "who owns it?" is generally, "some large firm", "the government", a government department or ruling institution. In the case of many of the phenomena of recent years, such as the Internet, there is indeed no one in charge. They are like giant flocks of birds or schools of fish. The response to questions such as "Who owns them?" or "Who's in charge?" is either "We all do", or "No one does". These are great mechanisms for democracy, but their effects can also be anarchic, and society may have to develop new ways to deal with these liberating effects.

The case of Betfair has seen some interesting reactions from incumbents and also governments at various levels, who attempt to deal with the Flock of Birds phenomenon in conventional ways, such as legislation or fiat. Traditional competitors have attempted to cry, "No fair", as they struggle to contend with a player whose methods they don't fully understand, and against whom they find it difficult to compete in traditional ways. Sports bodies are anxious to understand the possible impact of a firm such as Betfair on the potential for financial abuses in their domains. Governments, while supposedly welcoming competition as a force in consumer interest, will immediately seek new ways to tax new entrants such as Betfair, for it seems like, yet is not like, traditional firms such as bookmakers and totalizators, which have traditionally been rich sources of revenue.

In the United Kingdom, Betfair has been the focus of lawsuits by the major British bookmaking firms such as Coral, William Hill, and Ladbrokes. They have charged that by allowing individuals to lay bets (rather than merely take them), they are acting as bookmakers, and are not licensed to do so. Graham Sharpe, spokesman for William Hill argues,

"If you have a bet on an exchange, you don't know who it's with; if [the person] is offering extravagant odds, you don't know why"

The British courts have thrown out all the cases and rejected the bookmakers' arguments, and Betfair has been allowed to proceed with its business. While bookmakers might not like the idea of the site, it is evident that many of them are using it, either to buy back bets at advantageous prices, or to lay bets for which they might otherwise not have been able to find takers. The substantiation for this is the significant amounts of money that are available to be traded on many events.

In Australia, not only have bookmakers objected to the site and attempted to close it down through legal

action, it has also been the focus of an aggressive advertising campaign by TABCORP (essentially a consortium of Totalisator operators), a listed company that is the world's fourth largest gambling and entertainment business. Its advertising has attempted to cast Betfair in a negative light by claiming that betting on exchanges encourages dishonesty in sporting events and racing, a similar argument used in the United Kingdom by bookmakers. Betfair has disabled certain features on its Australian site to comply with Australian gambling legislation (for example, Australian players are not able to bet "in the running" – that is, after an event has started or a race is running). Gambling is more a matter of State than federal legislation in Australia. While the legislation is not quite clear whether it is legal or not for Australians to bet on betting exchanges or online casinos outside of Australia, there is no legislation prohibiting players in one State betting on operations in another.

The real effect of the Flock of Birds phenomenon is that access is equalized by mechanisms such as Bet-

“In the case of the phenomena of recent years, such as the Internet, there is indeed no one in charge”

fair when they operate online, unlike what occurs in traditional operations such as bookmakers and totalizators. In a very real sense, no one has a "better right of access", and no one, even the largest corporation, can shout louder. The smallest player, the individual, has a right and opportunity to be seen and heard through their

market action. Furthermore, many laws designed to regulate a physical world don't work as effectively when no one owns or controls the medium. This has been apparent in the lack of success in the traditional incumbents' attempts to fight Betfair in courts of law.

It has also been demonstrated by Betfair being a better, not less effective, mechanism for the detection of dishonest dealings in sport. If a particular player has inside information on an event, there is nothing stopping them exploiting this advantage by placing large cash bets either with bookmakers or totalizators, and reaping the benefits of this insider trading anonymously. Betfair is arguably in a better position to deal with this type of problem. For example, in July 2004, Betfair was dragged into the spotlight when it reported suspicious betting patterns on its exchange to the Jockey Club in the United Kingdom just before the Lingfield race in which leading jockey Kieren Fallon, riding favorite Ballinger Ridge, lost to Rye after seemingly easing down before the finishing line. News of the World alleged Fallon had told an undercover journalist that Rye would win. Launched in 2000 No proof was found that the race was fixed, but a Betfair spokesperson was quoted as saying:

"We are putting a searchlight on the sport and helping it clean up its act. There is a clear paper trail on our site that doesn't exist in high-street [betting] shops. We are entirely transparent. We have no vested interest in the outcome of a horse race."

As observed, there is also the issue of how governments will attempt to tax firms such as Betfair. Ideally, from the firm's point of view, tax would best be levied on net profits (which in simple terms would amount to net commissions on winnings less other direct costs). However, governments might not see it in that way, and might attempt to tax market makers such as this based on other measures, such as turnover (as alluded to in the introduction). Because of the fact that turnover is not an accurate measure of financial performance, as explained earlier, such a measure could be very detrimental to the firm and its thousands of players.

The Fish Tank Phenomenon

Moore's Law and Metcalfe's Law combine to lower entry barriers, and give individuals inexpensive and easy access to new media and the networks they facilitate. This means that any one can set up a website and theoretically at least, be seen by the world. As a result many have noticed the so-called "Fish Tank phenomenon" (The Economist, 1995). The fish tank phenomenon is named after the fact that in the early days of websites, people used to put a video camera on top of their tropical fish tank (or coffee percolator, for that matter), so that when surfers logged on to their site that is what they saw. There was an awful lot of junk out there – fish tanks, coffee percolators, and sites that caused Elvis Presley to giggle when the mouse ran across his belly. The question that this prompts is, wouldn't it be better if, instead of relying on individuals for their input on the net, we depended instead on the considerable resources of extant large institutions and corporations?

The answer to this query really lies in another question: What is more profound? And the answer to this second question is that, actually, it is the creative inputs of millions of individuals, all over the world who now have the ability and platform to show us what they can do. In other words, the creative outputs of millions of individuals will beat the doings of large institutions in a great majority of cases. So, while we may see lots of junk, such as fish tanks, coffee percolators, and devices to tickle a long dead rock artist, every now and then some individual is going to produce something so revolutionary that it will change our world.

The recent years of the Internet provide many examples of individuals entering markets with long

established incumbents, and changing the way these markets work. In the great majority of cases these individuals have had little or no experience of or presence in the industry or market, yet by entering it and subtly changing it they immediately become a very serious threat to the incumbents, who seem to have no effective way of dealing with it. Bezos entered the book retailing business with Amazon.com, and it was never the same again. Sean Fanning (a teenager working from his bedroom) invented Napster and turned the music industry upside-down forever. Andrew Black invented Betfair and changed sport wagering forever. The point is that none of these three individuals had previous experience of the industries that they changed, and none had worked for any of the established incumbents previously.

Conclusion

It is the general business principles that can be extracted from a case that make it valuable because these tenets can be redeployed in different circumstances. As well as being an outstanding example of the five technology forces, Betfair also illustrates two business principles: risk syndication, and opinion markets.

Risk Syndication

Edward Lloyd's coffee house in London was a point of congregation in the late 17th century for those seeking information about shipping and related matters. During meetings at the coffee house, wealthy individuals made deals to spread the risk of insuring ships, other items, and events across multiple parties. Risk diversification is common practice in the corporate world, and markets and instruments exist to allow large trades to execute efficiently. Small trades, however, are a nuisance, and individuals have few opportunities to syndicate a risk (for a start, the transaction costs of syndicating small risks are generally as high as those of syndicating large ones).

In the 21st century, Betfair, also based in London, syndicates risk using information technology. The outcome is the same, a large risk is spread among many, but Betfair executes risk syndication with lightning speed across individuals scattered throughout the world. A bookmaker or a large player taking a big bet can lay a portion of it with literally hundreds of small punters in a few minutes. Thus, Betfair has created the platform to enable individuals to syndicate risk. Personal electronic markets are not only places for buying and selling goods (e.g.,

“Andrew Black invented
Betfair and changed sport
wagering for ever”

eBay), they are also places for syndicating risks (e.g., Betfair). Most important, the transaction costs of syndicating both small and large risks are equally low.

A Market for Opinions

Much of human interaction is centered on the voicing of opinions and the liberal exchange of different viewpoints. Opinions, however, need not be freely bartered, and indeed opinions can have real value. Markets can create value for opinions when they enable the opinionated to back their views with their money. Betfair can be thought of as a market for opinions. Such markets can have considerable value for firms. For instance, Hewlett-Packard researchers discovered that setting up a market of about a dozen employees to trade opinions on future printer sales resulted in better predictions than standard market demand analysis (Science News, 2003). The aggregated opinion of a group is often a very precise estimate (Surowiecki, 2004), and Betfair has a strong record of predicting outcomes (e.g., the U.S. Presidential election of 2004 and the U.K. election of 2005).

Organizations have struggled for years to manage knowledge. They have invested considerable energy in codifying, storing, and providing access to knowledge. Many subscribe to the view that knowledge is something to be managed (Hansen, Nohria and Tierney, 1999). An alternative perspective, arising from reflecting on Betfair, is that knowledge is something to be collected when required. Players in an opinion market share the essence of their wisdom in a very concise and focused form. Knowledge is not collectively managed, but individually applied when needed. Thus, firms might look for opportunities to create opinion markets that surface knowledge while bypassing the complications of codification, storage, and dissemination. Perhaps the message is, don't manage knowledge; trade knowledge.

When reflecting on Betfair, executives in general, and information systems professionals in particular, might want to ask themselves two questions.

1. Can we apply the principles of Betfair to syndicate risk in our business?
2. When might trading knowledge be more effective than managing knowledge?

As Betfair continues to prosper, the most intriguing question of course, is how can it grow the business? As a senior executive observed recently: "I want to take Betfair into whole new business areas. This is

primarily a technology company, not a betting one. I don't think of Betfair as a gaming company, but more of an Internet technology company. I see no reason why the technology can't be used in other areas."

The five technological forces discussed with reference to the Betfair case are also relevant to all firms, industries and markets. While their impact in some circumstances will be far more intense than in others, executives might want to consider questions such as: What will the impact of ever more powerful, ever cheaper (frequently disposable) computing be on our business? What will happen when networks

dominate our industry to the extent that not only can we talk to our customers and suppliers, but they can also talk to each other, and provide value to each other? What happens when transaction costs are lowered to the extent that markets become so efficient that hierarchies diminish in power and status

and the ideal large firm is a small one? What mechanisms will evolve when the traditional regulatory machinery proves insufficient to deal with new business forms and technologies, and new ones are slow to develop? How does a firm deal with a competitor who is unseen at first, unanticipated, unknown and unsuspected? How does an incumbent cope when the next threat is not from the large firm across the road, across the city or indeed across the world, but a kid in their bedroom, an enthusiast at a computer screen, or someone so unfamiliar with current practices that they invent entirely new ones?

Notes

1. Time Magazine, July, 2004. (<http://www.time.com/time/europe/html/040719/gdi/black.html>).
2. Because it is a British firm, most financial figures on Betfair are quoted in Great Britain pounds sterling (GBP). However, players in different countries can choose to see and play in the currency of their choice – e.g., Americans can see markets in USD, Australians can see markets in AUD.
3. A very simple example illustrates this principle: Assume there are only two players, A & B, trading on an event. Player A bets \$10 on Team X to win at even odds; Player B lays \$10 on Team X to lose at even odds. Betfair's turnover on the game is \$20. Now assume Player A loses confidence in Team X, and sells the bet back (i.e. now lays \$10 on team X to lose) at evens, to Player B (who we now assume has a similar lack of confidence in Team X's likelihood of losing). Betfair's turnover is now \$40 on the event, but since there will now not be a net "winner", Betfair's commission will be zero. To reiterate: Betfair's commission on an event will be directly related to net winnings, not to turnover.
4. While it could be argued that firms such as Visa or MasterCard process as many or more transactions daily, neither of these firms experiences the sheer intensity of volume of transactions, such as shortly before a big horse race or major soccer game.
5. www.sun.com/executives/iforce/.

“Betfair can be
thought of as a market
for opinions”

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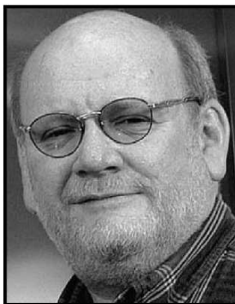
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