Unsplash © Prateek Katyal

What does true startup disruption look like?

What does Blockbuster Video have to do with the concept of startup disruption in the 2020s? Disruption is one of those startup terms that I hate even though I love what it means. The term gets tossed around too often, used out of context, and casually stamped on ideas that aren't as disruptive as they are just… stupid.

Disruption isn't about lofty valuations or skirting regulations or moving fast and breaking stuff. It's about getting a whole lot of people to try the unconventional while burying the fact that they'll need to give up the traditional. Disruption is about selling change, discomfort, inconvenience, and a lot of other things people hate.

At first. Then disruption can make you a whole lot of money.

In the 2020s, disruption has gone mainstream. Over the last 20 years, I've been in a position to continuously exploit the availability of new tools to create new solutions for existing problems.

But more recently, the rest of the world has caught up to the concept. Today's customer knows disruption, and they demand it. They will no longer accept a sprinkling of technological fairy dust over an existing product or service. They want more value, less friction, fewer commitments, and more convenience. But they still don't want to give up a lot to get it.

Here's a primer on what startup disruption really means. And to make it abundantly clear, we're going to get into why Blockbuster Video was so pervasive in the 1990s.

"I have nightmares…"

To put this into 2020s context: Last week, I sat down for one of my regularly scheduled advisor sessions with a startup. With this group, I'm working behind the scenes with a team to retrofit the company's existing offering with a new and completely different solution to an existing problem.

We're truly working on the car while it's speeding down the highway, disrupting ourselves along with everyone else in our industry. We've been at it for a year and have made huge strides.

But that morning's session started a little differently. As we were exploring how the tech we've developed would impact the existing business cases, the leader of the team spoke up:

> *"I've been having nightmares about becoming just a tech-enabled version of all the companies in our industry."*

She has a right to worry. She's leading the operations of a multi-million-dollar business with billion-dollar potential. Two very big things could go wrong:

1. What we're doing is so disruptive that we lose existing customers and turn away new customers.
2. What we're doing isn't disruptive enough, as she's vocalizing, and we're just sprinkling technological fairy dust.

Most disruption falls apart at the business cases, where it gets diluted in order not to "scare off the customers." True disruption should scare the hell out of the customers. You're asking them to change the way they've done things forever. You're asking them to give up what they know, what they rely on, and their idea of where the value lies.

You have to ease them into that change, and to do that, you have to change the way they think about the product or the service itself. You can't just use tech to automate the scoring of the game, you have to change the way the entire game is played.

Welcome to Blockbuster Video

Recently, the last remaining Blockbuster Video store became an AirBnB, where you can spend a night reliving 1990s nostalgia. There were over 9,000 Blockbuster stores worldwide at their peak in 2004.

Blockbuster itself was a disruption of a disruption. They rode the disruption of VHS breaking the unbreakable link between movie and movie theater, and mainstreamed that concept into “on-demand movies,” by creating the massive infrastructure needed to make movie rentals available to any consumer, in any location, within driving distance, and for any movie.

For anyone over 40 years old, this was a huge deal. For anyone under 40, I don’t have time in this post to explain what VHS was.

Netflix — rentals to your door

By 1994, Blockbuster was a household name, and there was probably one within five miles of where you lived or worked. They dominated the video rental business, crowding out an existing loose mom-and-pop infrastructure.

In 1997, Netflix launched its DVD-by-mail rental business. In fits and starts, Netflix threw everything they had at being a web-based version of Blockbuster. They sprinkled all kinds of technical fairy dust on an existing service.

But being a web-based service meant there was no brick-and-mortar infrastructure to compete with Blockbuster’s ability to provide instant gratification.

Home rental delivery, the very concept Netflix was built on, was actually a liability. Thus, they could never escape the gravity of Blockbuster, who attacked the 24–48 hour wait inherent in Netflix by promoting instant gratification. Geeks loved Netflix for its web-based convenience, the mainstream ignored it, and continued to pop into Blockbuster on the way home from work.

Then Netflix realized where the damn disruption really was.

Why the hell am I paying late fees?

The flaw in Blockbuster's armor was a concept that all their customers understood and accepted without question: Late fees.

When a customer rented a video, they blindly accepted a contract that's been in place since the dawn of the public library. In order for the public property model to work, the property has to be generally available to the public. That meant you could keep your video overnight, maybe a couple days if you paid a little more up front. But you had to return it within a three-day window or pay late fees.

So late fees were understood and accepted as a form of public apology.

"Sorry I broke the public property model and let everybody down, here's three bucks."

That's just the way things had been done forever. Traditional.

But the folks at Netflix understood that the public property model was, in this case, an economic model. Blockbuster needed to charge late fees, and in fact were chained to late fees, so they didn't have to carry X-times-10 copies of a new release. Those copies, after a couple weeks, were worthless.

So in order to break even on the margins, Blockbuster was limited in the number of copies they could carry in inventory. In order to keep a new release in circulation, they needed to turn each copy around quickly. In order to turn each copy around quickly, they needed to penalize the customer for keeping it too long.

Yes. Penalize the customers. Otherwise, the Blockbuster model breaks.

Renting videos versus borrowing movies

Netflix changed the game with a single instructional sentence: "Keep the movie as long as you like."

The tradeoff for doing the unconventional — waiting for your movie to arrive in the mail — and giving up the traditional — instant gratification — was never having to pay late fees again. In fact, you weren't "renting a video," you were subscribing to a group who " borrowed movies."

Different service. Different model. Different value prop.

For a while, most customers had both memberships, Blockbuster for new releases and Netflix for everything else. Once people got over instant gratification, Blockbuster memberships went to the back burner. That usually happened the first time the customer got hit with a late fee.

Then Blockbuster started playing Netflix’s game.

Blockbuster fights back, then inexplicably pulls back

A little-known fact is that Blockbuster actually could have and should have won the movie-to-your-door fight.

In a rare move of the incumbent getting it right, Blockbuster responded by eliminating late fees, then spending a fortune to replicate Netflix’s movie-by-mail model. Not only that, Blockbuster tied that model back to their still-massive retail footprint, resulting in “Blockbuster All-Access.” This allowed customers to have their movie delivered to their home, then return it to a Blockbuster for immediate exchange, or, instant gratification.

They actually started crushing Netflix. But the incumbent being the incumbent, there was some corporate reshuffling and some Carl Icahn nonsense. Suddenly, for no good reason, Dish Network, now the owner of Blockbuster, went all-in on brick-and-mortar in 2013, shutting down the DVD-by-mail service.

It wouldn’t have mattered anyway, because by this time, Netflix realized the game wasn’t about the DVD, it was about the movie.

Netflix moves to streaming (and almost kills it), then content

In 2007, Netflix started streaming content online. They weren’t the first, and they weren’t alone, but by this time, they had won the DVD-by-mail game and knew that disruption didn’t stop there.

Going all the way back to the freedom hard-won by the VHS videotape and all those mom-and-pop pioneers back in the 1980s, Netflix realized the model was about the content, not the physical media.

In 2011, Netflix split the DVD and streaming companies into two separate products, and nearly killed both with the aggressive way they did it. But the bet that the model was about the content held up, and they won the streaming fight too.

Now, the game isn't about the movie as a property anymore, it's strictly about the content. Today, Netflix is fighting a bigger battle in original content production against movie studios like Disney, entrenched networks like HBO, and even tech newcomers like Amazon and Apple.

The concept of continuous disruption

Say what you will about Netflix and their bully tactics and lack of general profitability and cash burning, you can't deny that they are a continuous disruptor.

Is continuous disruption the model your startup should chase? Absolutely, but maybe not to that cash-burning extreme. That said, disruption is found when the technology hits the business case. If you don't want to be the tech-enabled version of the incumbents in your industry, you have to constantly change the game.

And it all starts with attacking late fees. Whatever that means for your startup and your incumbents.

This article was originally published on Medium by Joe Procopio

Joe Procopio is a multi-exit, multi-failure entrepreneur. In 2015, he sold Automated Insights to Vista Equity Partners. In 2013, he sold ExitEvent to Capitol Broadcasting. Before that, he built Intrepid Media, the first social network for writers. You can read more and sign up for his newsletter at www.joeprocopio.com

---

Article by JOE PROCOPIO