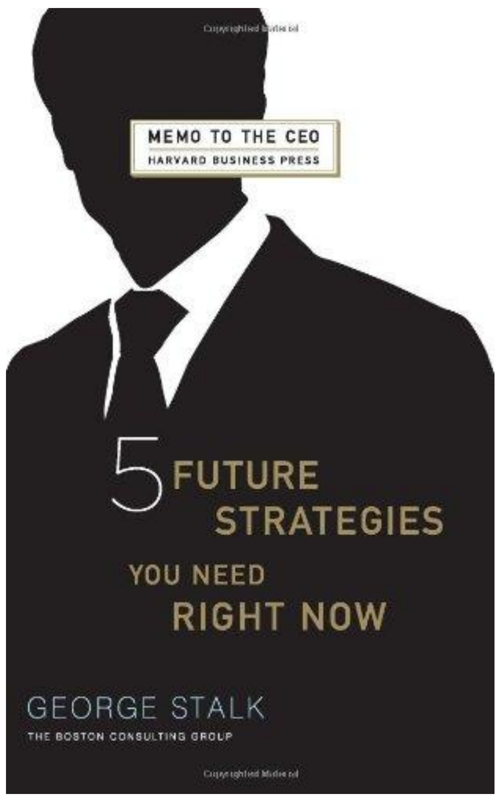
5 Future Strategies you need right now

Summary/ Takeaways from George Stalk's 2008 book



Produced and written by students
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How this summary of the Stalk book came about.

Several years ago at UTSC I had a T.A. for the int'l business course MGTC44 (Tom Snell) . Tom was a great T.A. and very enthusiastic about learning all kinds of things about business. After he finished his final duties he gave me this little hard cover book which was titled "5 Future strategies…"

I kept that book for a coupla of years and thought "I'd should read this, it looks interesting", but, never got around to it. When we were at the point of beginning the MGD415 courses "E-business strategies", I gave it to Tim S. (who has been my T.A. for 2 terms for the 3yr year courses)(what goes around comes around) and I told Tim "why don't you find a few classmates, divide up the sections in the book, and do a summary and analysis which can result in some "teachable points" which we can use in the course running in 2013.

Tim S. did just that, and his team finished writing up their notes end of February. I went through their doc, added a coupla points, made it in to a PDF and FTP'd it up to witiger.com March 8^{th}.

2013 – Tom Snell is Manager, Finance and Initiatives at University of Toronto and looks like he is headed on a good career path.

Supply Chain Gymnastics

(Stalk's book was published in 2008 – which means many of the circumstances of supply chain challenges refer to events and situations in 2007, 2006 and earlier. This review of his book by the 4th yr undergrad students, was done in Feb 2013 and by early 2013 a number of the logistical problems have changed in response to infrastructure changes in China, west coast USA and the North American and European economies… however, the overall strategy of having to effectively "sort out" supply chain problems stands as an important part of a corporate strategy for medium and large sized enterprises operating globally. Prof. Tim Richardson)

See also http://www.witiger.com/internationalbusiness/SupplyChainManagement.htm

Use of supply chain gymnastics to reduce the costs has been related with terms like outsourcing, subcontracting, partnering with other companies, offshoring and bestshoring. This is mainly used synonymous to shipment from China. Supply chain gymnastics help lowering the costs, increasing profits and helps building the share price of the company. However, the shipping and freight related infrastructure of the West Coast US and Western Europe have had problems recently (2008) in dealing with the large amount of shipments they are receiving. This is due to the fact that ports have reached their combined container loading and unloading capacities. Most of the times, the ships are docked for few weeks, until the cargo is cleared, increasing the costs in the long run. Until now, solution has been increasing the inventories, accepting longer lead times, using airfreight or raising prices. But with the demands fluctuating, this has created problems causing overstocking or under stocking of the goods.

The reason for a shift in 'Supply Chain Gymnastics' is due to the following attributes: -

China is an attractive venue for outsourcing / offshoring because of the low production costs. Amongst the companies that outsource from China are the major Fortune 1000 companies. The recent (2008) emergency for modifying supply chain gymnastics has been due to the following reasons.

• In 2004 over 40 percent of containers that entered the Los Angeles/Long Beach- port from Asia ground to halt as harbors, cranes, trucks and trains were unable to keep up with the surge of arriving containers. This affected many companies adversely, including their share price.

• There has been a vast increase in goods entering from China, with a growth rate of 9-12 percent per year.

• Meanwhile China, to reduce their shipping costs has been increasing container-loading berths and capacities, each with lift capacity of 250,000 containers per year.

This has created an emergency to tackle the current supply chain solutions through following ways-

• Increasing the size of the current docks, which are likely to be opposed by communities.

• Increasing the productivity.

• Develop ports that are underutilized.

Every supply chain has two types of profits- economic and accounting and three types of costs- direct, indirect and hidden.

The increasing complexity of supply chain had caused economic and accounting profits to decrease in a divergent manner. Of all the costs hidden costs are the major factors affecting the supply chain.

• They can have effects on the Gross Margin of a company when it doesn't have a product in stock for instance. This can be attributed to be around 40-60 percent of the shelf cost. This is caused by product still unloaded from a container or stuck on rail transport. This affects the economic profit, though accounting profit may still look good.

• Another reason is the exact opposite, i.e. having too much inventory that is not selling affecting around 10-20 percent of the retail cost.

Forecasting errors can be said to be one major reason behind this. Furthermore, economic costs increase as a result of finding defective items in the entire shipping and producing a complete new batch of goods.

The type of supply chain a company uses also affects the supply chain gymnastics. A company can have competitive advantage of supply chain management through the following-

• **Non-integrated supply chain**- In this supply chain the management gets information only on the final link as each information on customer demand is transferred only on consecutive steps, thereby making this a lengthy process.

• **Semi-integrated supply chain-** In this customer demand information is passed down two steps ahead from one or more distribution centers, still making it a lengthy and delayed process.

• **Integrated supply chain**- This is the most efficient step in transferring information related to customer demand since each step in chain has full knowledge of the demand and also makes it possible to notice demand changes immediately. This changes supply chain management into a group support.

To make the supply chain management more efficient certain actions need to be taken. These actions can be summarized as follows:

• Reduce the cycle time and minimum production order quantities.

• Unless needed prefer insourcing or near shoring instead of being dependent on China.

• Even though airfreight might be expensive compared to shipping, in the long run, these expenses will be lower compared to the stock out or overstock costs associated with shipping.

• Go for point-to-point shipping, enabling your product to be last loaded and first unloaded and hence avoiding the huge transportation and storage costs associated with shipping.

Sidestepping Economies of Scale

The problem presented within this chapter focuses on a business overestimating and underestimating demand especially in the early years of a product.

(The problem of estimating demand is slowly being solved by 2013, in part, by advances in the "technological environment", particularly in the category of web-based structures that allow for more accurate estimation of product movement , in conjunction with advances in GPS technology. Prof. Richardson)

Due to such inaccuracies, businesses are often left with "equipment and people" in either excess or too little quantity then required. In order to combat such a problem, businesses need to create greater flexibility in order to sustain or create competitive advantage. To create greater flexibility companies need to re-examine the policies based on the economies of scale. Once a profit making policy can now be seen dropping the income of companies. A strategy introduced to avoid defective forecasting; the idea of "the disposable factory" is introduced. Disposable factories offer lower threat filled methods of going "in and out" of rapid markets. This idea requires the company to assess "the value of scale" alongside to "the potential for market shortfalls" allowing for "investment profitability" through "production inflexibility".

Companies must realize that over time product life cycles are shortening intensely. For example, the ordinary lifespan of a new car platform has shortened to currently about 4 years compared to 8 years about twenty years ago. Research conducted displays that merely 20% of the products with budgets greater than $25 million are acknowledged as a success. At such a time companies are lessening or completely eliminating the use of scales through the use of innovative information technology and deconstruction. Information technology and just-in-time manufacturing allows businesses to operate smaller factories while the output is consistent with high quality and greater productivity then those with larger factories. Similarly, businesses are using deconstruction as an alternative to scale. Where originally longer vertically integrated firms were being transformed from horizontal structures for greater productivity; however, companies are deconstructing this long vertical integration by questioning its effectiveness due to the creation of "intermediate markets" among links.

With the shortening of the product life cycle, disposable companies come into play. Disposable companies are formed to operate with the lowest cost possible with the greatest return from the introduction of a new product in the market. The key feature of such factories is that it can be transformed into what the market demands. This reduces or eliminates the problem of over or underestimating demand due to its flexibility to market adjustments. Furthermore, for companies looking for not a business change but a strategy change, then the "disposable strategy" is proposed. Various strategies face the risk of becoming obsolete even before it is applied; thus, such a strategy provides flexibility for the business owners. An example of when such a strategy was used is in the case of Orbitz, which was similar to a disposable factory that consisted of the five major U.S airlines in 1999: Delta, American, Continental, United and Northwest. The strategy for Orbitz, an online travel website, was to have low distribution costs in order to encourage all airlines to display their inventory unlike its competitor Travelocity. However, for such a strategy to work the company had to grow rapidly. Thus, the company decided to create a temporary management team of a limited internal professionals and members from various external partners and suppliers to equal "the locally sourced, single-task, manufacturing components of a disposable factory". With such a strategy, Orbitz paid large dividends for its owners in just less than two years.

Disposable factories are not promoted to all businesses and/or individuals. It is most suitable under specific circumstances, which include:

- The time constraint, risk, and need for specific assets are unsuitable with other economic models.
- Extreme uncertainty due to highly "dynamic, competitive market" and/or the potential of uncertain innovation.
- Unclear size of the business opportunity.
- Speed up production and test markets.
- Wish to obtain a first-mover advantage.

Dynamic Pricing

One key strategy is known as dynamic pricing. Dynamic pricing is when consumers are categorized into groups each with its own separate demand curves and are then charged different prices based on that curve. This results in the company being able to make a higher profit because they are able to charge customers who are willing to pay a lot more and get more out of them rather than charging everyone a fixed price. However, this does raise some ethical concerns and issues because it can be argued that this is price discrimination if you charge different consumers different prices on the same product or service.

To gain a competitive advantage, there are two pricing strategies that are commonly used. They are known as power by the hour and bundling.

Power by the hour: This strategy is based on charging people based on a usage rate. There are many products and services that people want to use but do not want to own. Eg. photocopy machine.

Example of this strategy:

GE Aviation originally sold spare parts and aircraft engines as well as maintenance services. Consumers were able to pay a set fee over time as opposed to large payments every time there is a bigger issue that surfaces. GE Aviation realized that this costing them money because customers are only paying a set fee and the damages and repairs end up costing GE Aviation more money than how much they are getting paid. The organization saw an opportunity to make a higher profit from maintenance services and decided to invest in technologies to improve the reliability of their products so that there won't be any more defects and they will still get paid.

Bundling: This is when bundle your products and services and offer a group deal which seems cheaper than buying individual products separately.

Dynamic pricing allows adjusting the price to fit consumer needs so that they are able to use the product or service at any given moment. The supplier collects information on the consumers and sets the prices accordingly to cover any costs. Compared to the previous two strategies, as the author puts it, dynamic pricing "leverages extensive and very finely sliced real-time data about consumers and their behavior" (George Stalk, pg. 48)

A simple example of dynamic pricing is road tolls. The toll prices could increase when it gets busy and prices could decrease when it is not busy.

Dynamic pricing can be applied in organizations. In any situations where consumers are willing to pay more, a dynamic pricing strategy should be utilized to achieve competitive advantage. Dynamic pricing also works whenever technology comes into play and replaces human processes. An example of this is airport parking. As the author puts it, " the closeness to the terminal, fullness of the lot, time of day, and length of time the vehicle is parked are important factors – and ones that a human attendant could not easily provide or process" (George Stalk, pg. 58) If you're a first mover, start collecting information on your consumers so that you're able to start coming up with dynamic pricing strategies to get an advantage over your rivals.

Embracing complexity

Complexity in business has more or less always existed in business. But today, the vast increase in the number of products and services has led to failure of business operations. Interactions between organizational components and staff, problems with lines of communication, internally as well as externally, process conflicts or resource availability has led to constant battle in businesses. In the book, the author states, " As the operational people become increasingly burdened with manufacturing, distributing and supporting this ever-more daunting array of products- many of which are not turning much of a profit or are even losing money- they push back" (George Stalk, Pg. 64). Often managers believe simplification by cutting, eliminating, reducing and better forecasting helps with complexity; it is however not the solution. Therefore, the goal is not to find various methods to eliminate complexity, but to embrace it and find strategies to gain a competitive advantage over other competitors in the industry. Therefore, competitive advantage can be achieved through four ways. They are:

1. **Enticing the heavy spender:**

Here the author states the 80/20 rule, which is that there are 20% of customers who normally account for 80% of sales. These customers are characterized as people that like shopping, and prefer complexity in terms of being engaged in the process, choosing from a wide variety of products and services that are offered and are driven by the wealth of information about brands. Therefore "understanding the psychology of the heavy spender is critical to identifying the requirements for attracting them". (George Stalk, Pg. 65)

Heavy spenders therefore serve as an enormous opportunity to gain a competitive advantage. For instance, Coach formats to appeal to heavy spenders as they distinguish their products better than their competitors by offering a wide variety of bags and wallets to select from, and mainly the focus their marketing efforts on just bags and wallets to cater to the needs of heavy spenders. In addition their sales staff is knowledgeable about the various categories of products.

2. **Reducing complexity anxiety:**

Customers often when faced with complexity, leave and search for a simpler and less expensive offering. From a customers' perspective, companies must understand that customers fear complex offering like a complex return policy or complex specifications of a product. Therefore it is crucial that companies reduce this anxiety in order to gain a competitive advantage. For instance, Value Village offers a number of categories of products ranging from shoes to bed and bath, from books to housewares and furniture, from men and women's clothing to kids' clothing. This could lead to extensive complexity, especially purchasing products on their website. But the design of their website has made navigation and search for their preference so easy, that this has retained customers and made the process of purchase easier. This leads to a competitive advantage.

3. **Specifying the best choice:**

The author mentions, "There are many products that are in themselves complicated- cars and computers, for example. To find the combination that satisfies their needs and fits their budget, consumers must sift through a variety of platforms, features, variations and options (George Stalk, Pg. 73). Often salespeople are trained and taught specifications of a product in order to make a sale. They usually mention the best option that is profitable for the company. However when companies specify the best choice for their customers, this will lead the organization to gain a competitive advantage. The greatest example is that of Dell's online ordering system. They allow their customers to take the time to alter the specifications to customize their laptop/ personal computers according to their preference. This strategy has vastly improved the company's performance and has leaded them to gain a competitive advantage.

4. **Searching permutations:**

It is clear that in today's fast growing economy, customers have to select from a wide variety of products/ services offered by different companies. In addition, the permutation of configurations within each choice adds to the complexity faced by customers. Companies must help consumers cope with these challenges. For instance, Online recruiters directory is an e-business that provides a platform to link job seekers and hiring employers to each other. Both the parties fill in their preference and the system matches the database and provides a number of links based on the customers' preference.

Infinite Bandwidth

The fifth strategy is called infinite bandwidth. The term infinite bandwidth is used to refer to companies being able to receive any amount of information, in any shape or form, whenever they want it at no cost at all. Companies that are able to utilize infinite bandwidth to serve their purposes are able to gain a competitive advantage over their competitors in terms of conducting or even creating new businesses. One thing to keep in mind is that although getting all these information might be easy to some, knowing how to use that information to benefit you can be a challenge.

With the rapid advancement in technology in contemporary society, infinite bandwidth is easier to achieve than how it was in the past. Yet many corporate business leaders do not try to utilize this and fail to see the advantages and benefits infinite bandwidth can bring forth to their business.

There are three ways in which companies can utilize infinite bandwidth to their advantage:

Opportunity 1: Pursuing Operational Efficiency and Productivity

- finding new information technology that will help your firm
- value created by improvements in technology will help with price cuts and service gateways

Opportunity 2: Creating New Business Models
(see also http://www.witiger.com/ecommerce/businessmodels.htm)

- once these new information technology are in place, companies have to revamp their original business models to adapt to these changing technologies
- if you are a first mover, you can gain a serious competitive advantage by continuously innovating your business model to fit these information technology that your competitors cannot mimic

Opportunity 3: Birthing New Businesses

- creating new businesses can help your company gain even more strategic value.

- with infinite bandwidth, “companies no longer need information to physically accompany the flow of material goods” (George Stalk, pg. 91)

Vast majority of executives see the potential benefits of infinite bandwidth such as the potential of reduced costs and productivity improvement and increases in sales. However, many express concerns in regards to the technologies that are associated with infinite bandwidth. Primary concerns includes, technologies not being available from a single dependent supplier, unable to deliver the concept of a new business model as well no change in return on investments. A lot of people are waiting for someone else to adopt the concept of infinite bandwidth using the phrase “second mouse gets the cheese” by learning from previous experiences and mistakes. However, people who first utilize the concept of infinite bandwidth properly gain a huge competitive advantage as the saying, “early bird get the worm”.

Takeaways/ Something Useful and Interesting

An essential takeaway from this book is the opposite of what is often taught in economic lectures within academic institutions: the counter effects of economies of scale. Even though the benefits of economies of scale is emphasized when cutting costs comes into play, this also often creates the inaccuracies of businesses being left with “equipment and people” in either excess or too little quantity then required. This book proposed to companies that we must realize that over time product life cycles are shortening intensely. With both the shortening of the product life cycle, and inaccuracies of scale, disposable companies come into play.

Disposable companies are formed to operate with the lowest cost possible with the greatest return from the introduction of a new product in the market. The key feature that stands out is that it can be transformed into what the market demands. We discover that not only does this reduce or eliminate the problem of scale due to its flexibility to market adjustments but also focuses on the success of individual products. Furthermore, “disposable strategy” is also proposed similar to disposable factories, which is an interesting idea that allows for specific strategies to shape out before it can become obsolete in the market.

This takeaway links very well to all other strategies within the book. As hidden costs are relative to supply chain when items are not unloaded on time, stuck in a container somewhere or even ordered at the wrong time, companies can also use disposable strategies in addition to the ones presented in the first chapter. In order to gain a competitive advantage, companies must utilize proper supply chain procedures, otherwise their going to be lagging behind the competition and in order to do this successfully companies must be able to adapt to rapidly changing markets.

Considering we live in the information age an important takeaway is the importance of bandwidth. Companies that are able to utilize infinite bandwidth to serve their purposes are able to gain a competitive advantage over their competitors; however, it is not that simple. It is essential to take away the importance of knowing how to use that information to benefit you in a profitable manner. Furthermore, once new information technology are in place, companies have to revamp their original business models to adapt to these changing technologies. In order to do this, companies must adopt "disposable strategies" as disposable business models to ensure that the business model has not become obsolete even before it could provide a profitable return.

Dynamic pricing is a very interesting concept because many companies fail to squeeze out as much as they can out of consumers. If certain people are willing to pay more than the original price then companies should utilize this to their advantage. By utilizing dynamic pricing strategies in their organizations, companies can really gain a competitive advantage as well as a good amount of profit in the process if done correctly.

Often companies are overwhelmed with the thought of complexity within their organizations. Companies are so worried about all these situations that they fail to realize the successes that they have achieved. Organizations are set with this mindset that simplicity is the way to go; the good way whereas complexity is the bad way. However complexity has its advantages. It gives opportunities for firms to expand and grow into to gain a competitive advantage.

Bibliography

Stalk, George "5 Future Strategies You Need Right Now" 2008 The Boston Consulting Group, Inc.