**Practice Case 7**

**Business Case 2 – Illy Café**

**Andreas Nugroho R**

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**Illy Café Business Case**

Andrea Illy is CEO of the global premium coffee company that bears his family’s name. As one might expect, he is passionate about coffee – its science, its health benefits, its taste, its beauty. Illy also has a dream that someday soon the coffee market might be transformed into something approaching the market for wine. Where connoisseurs discuss the fine points of various origin coffees and blends, where customers are willing to pay a premium for the finest examples of the coffee-making art, and where the growers, roasters and baristas will be compensated fairly for the expertise they contribute to every cup.

Unfortunately, the current coffee market differs from such an ideal. Coffee growers in most parts of the globe work at a barely subsistence level. One bad harvest (made all the more likely by the ravages of climate change) or a sudden decline in the commodity price of coffee can drop them below subsistence to hunger. Even in good times, growers have little incentive to improve their operation – they have minor contact with the roasters or customers and no knowledge of how their crops get translated into the cup. This disadvantages not only the grower but also the consumer – coffee sourced from good quality beans is hard to find.

Illy believes that the solution to the sad state of affairs is to initiate a “virtuous circle” that draws the grower, the roaster, the barista and customer together. Growers with better knowledge of the market will work to improve their crops or experiment with new varieties. Roasters and preparers will educate their customers as to the qualities of various beans, roasts and preparations. Customers, in turn, will be willing to pay more for the best beans and that premium will be sent back up the chain to pay for even more quality and variety. And so on.

Certainly there have been some positive signs. Indeed, many observers argued that a “third-wave” of transformation in the coffee market was already starting. (The first wave is said to have occurred when Maxwell House and Folgers made coffee a mass commodity, the second wave when Starbucks initiated a move to quality and higher prices.) Specialty coffee roasters had worked to build cafes and brands around origin-based beans sold directly to the roasters without reference to the commodity prices of coffee. With these third-wave roasters, every coffee came with a story of its origins and growers could count on occasionally eye-popping premiums for their beans.

As yet, specialty coffee represented a small sliver of the overall market and there were other signs that it might not ever grow beyond a small circle. New trends like coffee-based drinks and single-portion coffee in pods (e.g. K-cups, Nespresso) actually shifted more of the value-added towards roasters without a premium for growers. A consolidation was taking place among mass roasters that was even sweeping-up third-wave roasters in its wake. Observers argued that could lead to greater uniformity with even less emphasis on origin-based, direct-traded coffee.

Illy’s hope is that someone would come up with an innovation that would solidify the beginnings of the third wave and help reshape the market. Such a change would not necessarily have to involve Illy Caffè; Andrea Illy believes as the world’s premium brand, an increased emphasis on quality in the market would only help his company. The most important thing was to make the coffee supply chain more equitable and coffee better-tasting.

**Questions:**

1. What is the real problem this company facing? And how do you identify it?

2. Which part of business components need improvement? Why?

3. What kind of company transformation that might help the company to strife in the market?

4. Propose an idea/ideas to create a new product

5. How do you propose the solution?

**Answers:**

The real problem that the company is facing is the seemingly slowing down nature of the third-wave coffee progress. Andrea Illy has high hopes that the coffee market would be transformed in a way that would unlock premium values that could be gained from the consumption of specialty coffee. This would benefit the coffee growers as well as the roasters since coffee growers may also be compensated due to the increased revenue from selling premium specialty coffee. Illy seems to have bet a lot of the company’s future on this transformation. However, the progress of the transformation is threatened with the advent of a new instant coffee pod trend which does not put too much value on quality origin-based coffee. This would mean that the future of Illy Caffe is at stake.

I could identify this from Andrea Illy’s hopes that such a transformation would happen. This leads me to think that his company’s future must have been set around the coming of the third-wave of coffee. If read at a glance, it seems that Andrea Illy hyping up this coming transformation so much while Illy Caffe is not the main beneficiary of the transformation (they are roasters while most of the gains from third-wave coffee transformation would go to the coffee growers) would be counterintuitive. The fact that he is worried that such transformation will not come at all means that he must have built his company to be ready to face the third-wave coffee industry.

I have identified R&D, product, logistics, and marketing to be the main business component which are impacted and thus need improvement. The product department is clearly lacking in identifying which product is currently on demand in the market. Therefore, Nestle and the others have taken the lead in catering to the new demands of the coffee market. The R&D department is also lacking in developing quality coffee which can compete with the instant nature of their competitors while keeping their prices competitively low. Furthermore, the logistics department needs to improve their supply chain management so that good quality coffee can be sourced from their origin without too much costs which could burden the production line. This would make the job of educating the market easier if the product is reasonably priced. Thus, the marketing department needs to improve its efforts in educating the market that quality origin-based coffee is highly desirable and much more superior to the current coffee products offered by the competitors so that the market would lean heavily on consuming more specialty origin-based coffee.

I have identified that the supply chain management of Illy and the education of the market regarding specialty origin-based coffee will be the main drivers for company transformation for Illy to be able to push on in the market. Firstly, by educating the market of the advantages of consuming specialty coffee, Illy will make sure that the knowledge of such quality product is not lost in the market. Illy will also be able to position its quality coffee products as premium products and therefore command higher prices. Furthermore, better supply chain management will have various impacts. Environmentally, by keeping in mind the environmental impacts of coffee production, they can ensure future production of coffee. Socially, by involving the growers and farmers more, they can fairly compensate the work of growing premium quality coffee and thus the growers and famers will ensure that level of quality in future production. Business-wise this will educate the market to consume more of this environmentally and socially responsible coffee which will increase revenue.

A new product that could solve this problem, in my opinion, would be premium origin-based coffee which can be consumed from pods instantly, or other drinks which have been infused by origin-based coffee. This kind of product would take advantage of the current trend of coffee consumption in the market right now, while also educating the market of what they could get instead if they consume specially crafted origin-based coffee. Such products would immediately solve two problems at the same time. However, the creation of such product is not easy and also the education of the market would still need to continue in other forms, since it is difficult to pack a lot of information regarding the advantages of premium coffee to such products and therefore it requires other methods of education as well.

I would propose multiple-pronged solution to the problem, but one that is heavily reliant and focused on the education of the market. As mentioned earlier, the R&D, product, and logistics department would still improve their product quality and supply chain management to create the new product which has been mentioned previously. This new product will be the new face of Illy Caffe in its effort to educate the market of the advantages of specialty origin-based coffee. However, added emphasis would be put on the marketing department to come up with unique solutions. One method is to visit some café owners and educate them on the importance of kindness and professionalism in satisfying the customer. Another method is to build a ‘café university’ which will provide a platform for anyone who wants to learn more about the coffee world. The last method is to build a special café in which the atmosphere is unique and very supportive for consuming the quality coffee products from Illy itself. These multiple approaches would provide needed knowledge of product quality to the market, thus creating a bigger market for Illy’s quality products and therefore creating a pathway for the third-wave coffee transformation to arrive to the market.